

## E. PERFORMANCE AND REPORTING UNDER THE FISCAL RESPONSIBILITY ACT 2012

The *Fiscal Responsibility Act 2012* (FRA) requires the Government to report on performance against the FRA's objective, targets and principles as part of the budget papers.

The FRA sets the policy objective of maintaining the State's triple-A credit rating, supported by two fiscal targets and three principles of sound financial management (see Table E.1).

Table E.1: *Fiscal Responsibility Act 2012 – object, targets and principles*

Object	Fiscal targets	Fiscal principles
Maintain the triple-A credit rating	1) Expense growth kept below long-term average revenue growth	1) Responsible and sustainable spending, taxation and infrastructure investment: <ul style="list-style-type: none"> <li>aligning general government revenue and expense growth</li> <li>stable and predictable taxation policies</li> <li>investment in infrastructure that has the highest benefit for the community</li> </ul>
	2) Eliminate unfunded superannuation liabilities by 2030	2) Effective financial and asset policies: <ul style="list-style-type: none"> <li>performance management and reporting</li> <li>asset maintenance and enhancement</li> <li>funding decisions</li> <li>risk management practices</li> </ul>
		3) Achieving intergenerational equity: <ul style="list-style-type: none"> <li>policy to have regard for its effects on future generations</li> <li>the current generation to fund the cost of its services</li> </ul>

### Review of the FRA

Five years after the FRA's commencement in 2012, the Treasurer was required to review the FRA to determine whether its policy objective remains valid and the terms remain appropriate for achieving the objective. In 2018, the review was tabled in each House of Parliament and stated the following key findings:

- the Government has met the FRA's objective and targets, and has pursued the principles of the FRA. Recent initiatives such as the NSW Generations Fund and the *Government Sector Finance Act 2018* further support the objective
- the objective to maintain a triple-A credit rating is unique but an appropriate mechanism to support fiscal discipline
- the Commonwealth downgrade remains a risk to maintaining the State's triple-A rating. This risk should be managed appropriately by the NSW Government continuing to maintain a sustainable operating position and levels of debt consistent with a triple-A credit rating. The principles of the FRA should continue to be adhered to, in particular '*responsible and sustainable spending, taxation and infrastructure investment*' and '*achieving intergenerational equity*'

- the current targets support the objective of the FRA, with adherence to the 5.6 per cent expense growth cap helping to deliver solid budget results over the prior five years. With revenue pressures that may put pressure on the operating position over the medium term, the Government should continue to maintain a sustainable operating position to ensure debt levels remain manageable
- The Government should continue to pursue the principles of sound financial management to support the objective of the FRA, with work to date demonstrating a significant modernisation of the State's financial framework.

## Performance

### Maintaining the triple-A credit rating

New South Wales continues to meet the objective of the FRA. Both major credit rating agencies – S&P Global and Moody's – reaffirmed the State's triple-A credit rating in September 2018.

As a sub-sovereign, the credit rating for States and Territories is capped by the rating on the sovereign, the Commonwealth Government. In July 2016, S&P placed the Commonwealth on a negative outlook, which flowed through to New South Wales (and the other triple-A rated States and Territories). In September 2018, S&P Global revised the Commonwealth's rating outlook from negative to stable, and S&P subsequently revised the New South Wales outlook back to stable.

New South Wales is one of only five comparable sub-sovereigns outside the United States to hold a triple-A credit rating from both Moody's and S&P Global (refer Table E.2).

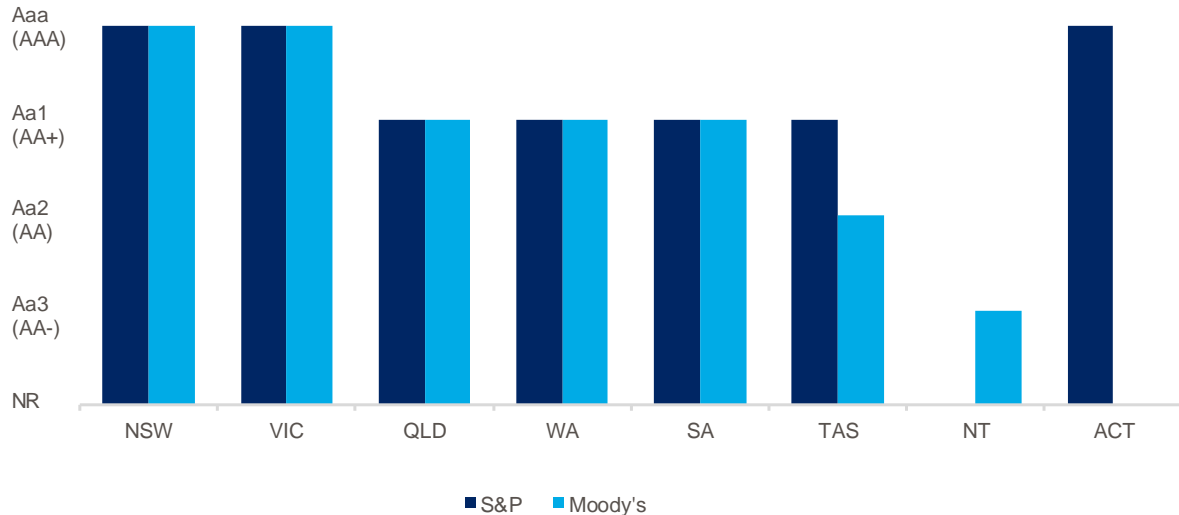
Table E.2: New South Wales is one of five states rated triple-A by Moody's and S&P Global<sup>(a)</sup>

Moody's	S&P Global
<b>New South Wales (AU)</b>	<b>New South Wales (AU)</b>
<b>Victoria (AU)</b>	<b>Victoria (AU)</b>
<b>British Columbia (CA)</b>	Australian Capital Territory (AU)
Saskatchewan (CA)	<b>British Columbia (CA)</b>
<b>Baden-Wuerttemberg (DE)</b>	Vaud (CH)
<b>Bavaria (DE)</b>	Zurich (CH)
Brandenburg (DE)	<b>Baden-Wuerttemberg (DE)</b>
	<b>Bavaria (DE)</b>
	Saxony (DE)

(a) Sub-sovereigns in bold text reflect a triple-A rating issued by both rating agencies.

Note: shows sub-sovereigns comparable to the State of New South Wales i.e. states, provinces, landers, cantons etc. Abbreviations: AU (Australia), CA (Canada), CH (Switzerland) and DE (Germany)

Chart E.1: New South Wales has the highest credit ratings possible in Australia



## Meeting the FRA targets and principles

The FRA sets out two fiscal targets and three principles of sound financial management to help support the object of the Act, as described in Table E.1.

### Target 1 – Expense growth below long-term average revenue growth

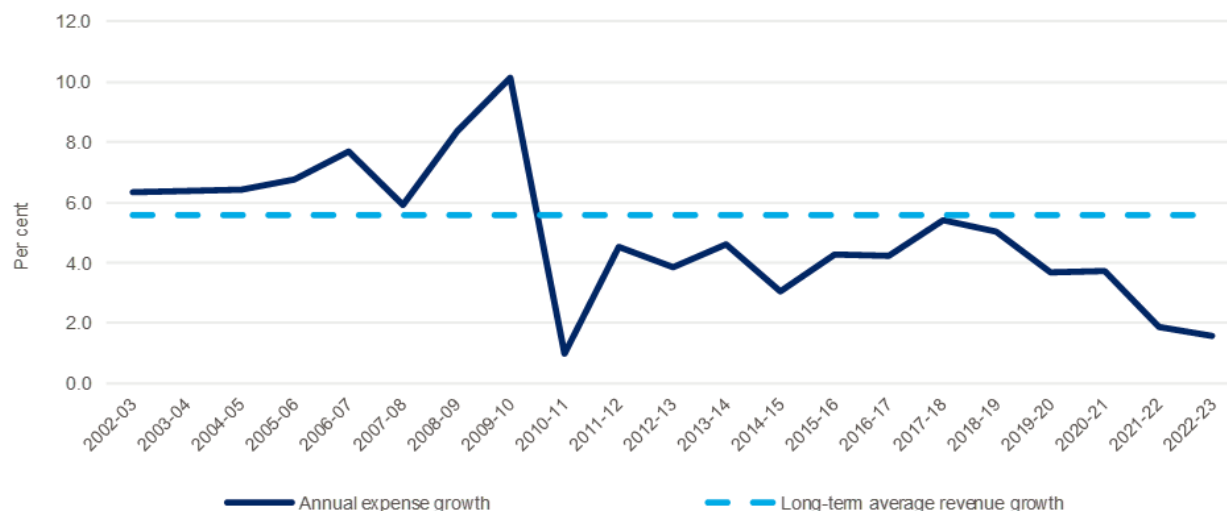
The FRA requires annual general government expense growth to be maintained below the long-term average general government revenue growth (5.6 per cent as set in the *Fiscal Responsibility Regulation 2013*).

This limit on expense growth has been supported by the Government's 2.5 per cent public sector wages policy and various savings measures such as efficiency dividends.

The Government has achieved this target since the introduction of the FRA in 2012 and is projected to continue to do so over the budget and forward estimates in the 2019-20 Budget (see Chart E.2).

Over the long-term, there is a divergence in the revenue outlook from long-term revenue growth (which was noted in the review of the FRA). As revenue pressures emerge over the medium term, the Government will need to not only carefully manage expense growth, but maintain a sustainable operating position and manageable debt levels.

Chart E.2: General government annual expense growth



## Target 2 – Fully funding the State’s superannuation liabilities by 2030

The FRA requires the Government to fully fund the State’s unfunded superannuation liabilities by 2030. If not properly managed, unfunded super liabilities may result in long-term financial imbalance that impacts intergenerational equity and puts pressure on the credit rating.

To achieve this target, the Government makes annual cash contributions to the State’s defined benefit superannuation schemes in line with a funding plan set at each triennial review of the schemes. This funding plan takes into account any changes in both the asset (e.g. market returns) and the liability (e.g. demographic and actuarial assumptions) components of the schemes. Following the latest triennial review in October 2018, it was confirmed that New South Wales remains on track to fully fund the State’s superannuation liabilities by 2030.

Total state unfunded super liabilities are estimated to be \$61.0 billion at June 2019 and are projected to decline to \$40.9 billion at June 2023, reaching zero at June 2030 (see Chapter 6 for further analysis).

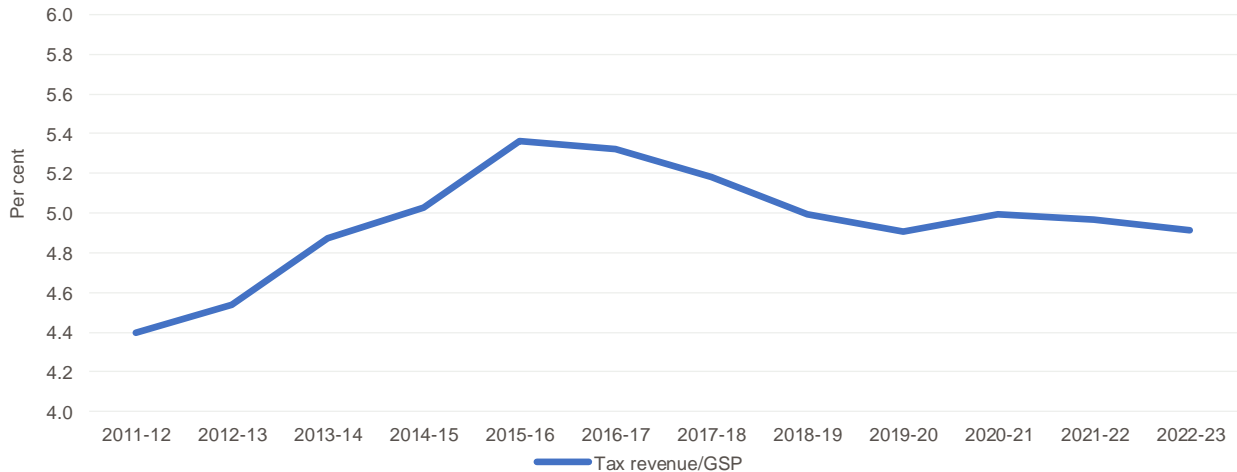
## Principle 1 – Responsible and sustainable spending, taxation and infrastructure investment

The principle of responsible and sustainable spending, taxation and infrastructure investment includes aligning general government revenue and expense growth, stable and predictable taxation policies, and investment in infrastructure that has the highest benefit for the community. This underpins the ability to maintain a strong and sustainable fiscal position, shown by an operating position appropriate for current conditions, and debt that can be sustainably managed while providing recurrent services and infrastructure investment.

Keeping general government expense growth below the long-term revenue growth rate of 5.6 per cent as per the FRA target reflects the commitment to responsible and sustainable spending.

State taxation has remained consistent and low, with the ratio of tax receipts to gross state product (GSP) declining from 5.4 per cent in 2015-16 to a projected 5.0 per cent in 2018-19, and remaining around that ratio across the forward estimates (as shown in Chart E.3).

Chart E.3: Taxation revenue, ratio to GSP



The Government continues to deliver its infrastructure program with total investment in the general government sector reaching \$71.7 billion over the four years to 2022-23.

The sustainability of this investment is made possible by financing predominantly through operating surpluses and the proceeds from the asset recycling program, which have moderated the need for additional debt.

The State continues its transformation to an outcome budgeting framework. The 2018-19 Budget set out the 46 State Outcomes providing a “citizen perspective” of the Budget. Another major milestone was reached in December 2018 with the release of Treasury’s Policy and Guidelines Paper on *Outcome Budgeting* (TPP18-09). This provides guidance on developing and maintaining the outcomes framework, the financial and non-financial requirements for performance reporting, and the timetables for finalising outcome, performance and equity measures.

## Principle 2 – Effective financial and asset management policies

The principle of effective financial and asset management policies includes having sound policies and processes for performance management and reporting, asset maintenance and enhancement, funding decisions and risk management practices.

The Government has continued to focus on the State’s balance sheet management, funding decisions and risk management through the inter-departmental Assets and Liabilities Committee (ALCO). This includes improved cash management and optimisation of the State’s balance sheet and a whole-of-government foreign exchange risk policy.

Some additional reforms and policies implemented by the Government include:

- the passage of the *Government Sector Finance Act 2018* which modernises financial structures, principles, guidelines and controls across the entire public sector
- establishment of the NSW Generations Fund
- strengthened reporting and management of contingent assets and liabilities
- the first issuance of Green Bonds (in November 2018) to fund projects delivering environmental and social benefits.

### **Principle 3 – Progress in achieving intergenerational equity**

The principle of intergenerational equity includes ensuring any policy decisions have regard to their financial effects on future generations, and that the current generation funds the cost of the services delivered today.

The FRA commits the Government to ensure that policy decisions are made with consideration to their financial effects on future generations. Each budget reports the impact of its measures on the long-term fiscal gap, which is a summary indicator of the budget's financial effect on future generations.<sup>1</sup> The 2016 Intergenerational Report highlighted that if current trends continue, a widening fiscal gap will emerge where expenditure would exceed revenues resulting in a fiscal gap of 3.4 per cent of GSP by 2055-56.

There is no change to the fiscal gap as a result of measures in this Budget. Savings initiatives such as reducing expenditure to reflect recent machinery of government changes allow the Government to invest in new services and infrastructure for the NSW community without further impacting long-term fiscal sustainability. This shows that prudent budget management continues to be effective in limiting the financial burden shifted to future taxpayers.

With intergenerational challenges on the horizon, the Government became the first state in Australia to create a vehicle to support intergenerational equity by establishing the NSW Generations Fund in 2018. The dedicated debt retirement fund is projected to grow to more than \$28 billion over the next decade, strengthening the State's balance sheet and supporting intergenerational equity for the people of New South Wales.

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<sup>1</sup> The fiscal gap is calculated for the general government sector and is the difference between the base period primary balance as a share of GSP and the primary balance as a share of GSP at the end of the projection period, on a no policy change basis. The primary balance is the gap between spending and revenue excluding interest transactions but including net capital expenditure. A positive gap implies that fiscal pressures will be building over the projection period.