



**Treasurer of New South Wales
Australia**

2003-04

Half - Yearly

Budget Review

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EXECUTIVE SUMMARY

The general government budget result for 2003-04 is expected to be a modest surplus of \$150 million, \$107 million above the June 2003 budget estimate.

Since the Budget the Government has provided for operating expenditure in essential areas including:

- \$386 million for education. This includes \$229 million in 2003-04 for the teacher pay increase (\$308 million a full year) following the interim award made by the Industrial Relations Commission on 19 December 2003 which covers the six months to 30 June 2004. The additional amount in 2003-04 includes a one-off \$75 million increase in the cost of teachers' long service and other leave. Additional money will also be spent on school cleaning, higher-than-expected enrolments and increased administrative staff hours;
- \$90 million for health which includes \$71 million for increased wages for nurses (\$86 million in a full year), following the recent Industrial Relations Commission decision on 11 December 2003;
- \$71 million for public transport including additional funding for the State Rail Authority;
- \$72 million for community services to support the activities of the Department of Aging, Disability and Home Care; and
- \$64 million for the NSW Police including additional police officers and IT upgrades.

The Government has utilised an expected increase in transfer duty revenue of \$654 million above the budget estimate, due to the stronger than anticipated housing market, to fund these additional costs and services. The remaining surplus of \$150 million will be used to reduce the State's net financial liabilities in anticipation of a more difficult fiscal position in 2004-05, as the level of transfer duty falls and expenditure commitments grow.

Transfer duty revenue is expected to decline in 2004-05. In addition, the Government will provide additional funding for the improved delivery of existing services including those promised in the 2003 Election, particularly in the areas of health, education and transport. The cost of the recent nurses and teachers wages decisions by the Industrial Relations Commission, estimated at \$394 million a year, will also increase expenditures in 2004-05.

The estimated budget result for 2004-05 on a no policy change basis is a deficit of \$275 million. Results in later years are expected to improve as revenue growth returns to normal.

Projected Budget Results

	2003-04 \$m	2004-05 \$m	2005-06 \$m	2006-07 \$m
Budget Time (June 2003)	43	303	821	932
Half-Yearly Budget Review	150	-275	94	106

General government underlying net debt is projected to be \$999 million less in June 2004 than forecast in the 2003-04 Budget and \$500 million less than the level in June 2003. Net financial liabilities are expected to fall by a similar amount compared with the budget time projection.

General government net financial liabilities, which also include unfunded superannuation, are expected to rise slightly over the next four years, partly due to the projected deficit in 2004-05, but continue to decline as a proportion of Gross State Product.

Based on the projected budget results, general government underlying net debt will be reduced to \$1,516 million by 30 June 2007, a reduction of \$1,722 million since June 2003.

Net worth of the general government sector is projected to rise by June 2004 to more than \$123 billion, a \$2,079 million increase on the year before.

The State's overall financial position remains strong as a result of budget surpluses in recent years. However, the growing costs of providing key services, including the payment of increased wages to teachers and nurses, along with the projected downturn in transfer duty, will place increasing pressure on State finances over the next few years. Should further fiscal shocks occur, corrective action may need to be taken to protect the State's longer term financial position.

A readers guide to this document is found in Appendix B.

1. STRATEGIC DIRECTION AND ENVIRONMENT

1.1 STRATEGIC PERSPECTIVE

The Government has had in place a medium-term fiscal strategy since 1995.

The objective of the fiscal strategy is to ensure that the State has the financial resources to support ongoing service delivery through:

- reducing net debt and other financial liabilities to levels where the State's finances could absorb adverse cyclical economic or short-term fiscal shocks without the need for disruptive expenditure cuts or tax increases;
- constraining aggregate expenditure while supporting spending priorities; and
- maintaining a competitive tax regime that is conducive to business investment and the State's future growth.

Implementation of the strategy requires:

- reducing and then maintaining total financial liabilities at a sustainable level;
- judiciously managing both the mix of liabilities (debt, unfunded superannuation and insurance) and the level and composition of financial assets;
- maintaining general government sector budget surpluses during periods of above-trend revenue, but allowing deficits if necessary in cyclical downturns. Revenues are more sensitive to economic conditions than expenditures, necessitating the achievement of a sustainable level of net financial liabilities;
- keeping general government expenditure growth within the underlying growth of the revenue base and anticipating, to the extent possible, short-term budget risks;
- taking into account the financial position of public trading enterprises, as these affect the budget both directly (mainly through financial distributions received and subsidies paid) and indirectly (for example, via guarantees); and
- in the longer term, building up the fiscal capacity to deal with foreseeable long-term budgetary pressures such as demographic trends, technological advances and global competition.

Full details of the strategy, including recent performance and progress against fiscal targets and principles are contained in 2003-04 Budget Paper No.2, Chapter 1.

The revisions detailed in this Half-Yearly Budget Review indicate that the fiscal strategy remains on track this year. A budget surplus remains in prospect for 2003-04. Delivering budget surpluses at a time of reasonable economic growth and buoyant revenue continues the process of strengthening the State's financial position.

While projected expenses in 2003-04 have been revised higher, so too have projected revenues, generating a projected surplus that is \$107 million above the budget estimate.

Continued strength in the property markets explains the bulk of the projected revenue increase.

On the expense side, there have been a number of expenses that were unanticipated at budget time, including increased spending on education, health, police and disability services. Education and health expenses have increased mainly due to the decisions by the Industrial Relations Commission for increased wages for teachers and nurses.

General government underlying net debt at June 2004 is now expected to be below the budget estimate, at \$2.7 billion or 1.0 percent of GSP. Net financial liabilities are expected to be about \$25.1 billion and are expected to decline as a proportion of gross state product, from 9.5 percent in June 2003 to 8.9 percent in June 2004. By that time, net financial liabilities will have fallen 23 percent from \$32.8 billion at June 1995.

Although the economy remains strong, there are considerable uncertainties and challenges for the budget outlook and hence the achievement of the medium-term strategy:

- In terms of the economy and hence tax revenue, the sustainability of the current global recovery remains to be seen, as does the extent of the slowdown in the residential property sector and the impact of monetary policy on a highly leveraged household sector.
- In terms of non-tax revenues, beyond 2003-04 there are significant risks associated with revenue from Commonwealth payments particularly the outcome of the 2004 methodology review of the Commonwealth Grants Commission.
- In respect of expenditures: major public sector wage agreements expire prior to and during 2004-05 - each percentage point increase in wage rates raises general government expenses by about \$170 million; and spending pressures are building in some major portfolios associated with the delivery of existing services.

Nonetheless, past adherence to the fiscal strategy has delivered significant improvements in the State's finances and the State is well placed to meet any cyclical downturn. In its latest report on New South Wales issued in October 2003, Standard and Poor's indicated that its reaffirmation of the State's AAA credit rating was based on, among other things, its low level of financial obligations and its prudent fiscal strategy. S&P further observed that any changes to the State's AAA credit rating would probably require "*several years of much weaker financial outcomes than currently forecast, combined with government inaction in addressing fiscal problems*", and that either of these scenarios appeared "*highly unlikely*".

The low level of net debt permits increasing flexibility in the management of the State's balance sheet. Future surpluses will be directed more towards increasing superannuation assets rather than further reductions in net debt. Beyond 2003-04, the budget result (the element impacting on the State's net financial liabilities most directly in the Government's control) is expected to be in deficit in 2004-05 and recover to modest surpluses in succeeding years.

This should continue the process of moving the State towards a position of sustainable general government net financial liabilities. These are expected to remain relatively flat in dollar terms, but continue to decline as a percentage of state output in the three years to 2006-07.

1.2 ECONOMIC OUTLOOK

Overview

Uncertainties in the global economic outlook and correspondingly the domestic outlook have changed rapidly over the course of the last six months. At Budget-time, a reasonably optimistic outlook was forecast, though the balance of uncertainties in that outlook was seen as decidedly to the downside. At present, a slightly more optimistic outlook seems more assured, with uncertainties more evenly balanced. As an example of how quickly the balance of uncertainties in the outlook has changed, in June 2003 the Reserve Bank indicated that if adverse trends in the global outlook continued, a reduction in interest rates was likely. By year end, however, the Reserve Bank had not reduced, but rather raised interest rates in both November and December.

In the 2003-04 Budget, improving agricultural conditions and a firming in world growth were expected to offset a decline in dwelling construction and slower growth in other components of state demand. NSW gross state product was expected to increase by 3¼ percent, employment growth was projected to moderate to 1¼ percent with the unemployment rate falling to 5¾ percent.

Since June, downside uncertainties in the global outlook have progressively dissipated and clear signs of the anticipated global recovery have become evident. Domestically, consumer confidence and spending have been buoyed by these improving global signs, low interest rates, rising house prices and declining unemployment. These more favourable than anticipated trends for the NSW economy are reflected in revisions to the forecasts for the current financial year.

While near-term uncertainties in the outlook are more balanced, in the longer-term there remain several key uncertainties that could affect the economy in 2004-05 and beyond. These include the sustainability of the recovery in the global economy, the path of adjustment in the dwelling construction sector and the future course of monetary policy.

Table 1.1: Economic Performance and Outlook ^(a)

	<i>Actual 2002-03 Outcome</i>	<i>Budget 2003-04 Forecast</i>	<i>Revised 2003-04 Forecast</i>	<i>Medium Term Projection</i>
New South Wales				
Gross State Product	2.2	3 ¼	3 ½	3 ¼
State Final Demand	5.1	3 ¼	3 ¾	
Employment	2.1	1 ¼	1 ½	1 ¼
Unemployment (rate)	5.9	5 ¾	5 ½	
Sydney CPI	2.8	2 ¼	2 ½	2 ½
Wage Cost Index	3.5	3 ¼	3 ¾	3 ½
Australia				
Non-farm GDP deflator	3.0	2	2	2 ½
Ten year bond (rate)	5.3	5 ½	6	6 ½

(a) Year average percent change, unless otherwise indicated

World Economy

When the Budget was formed, it appeared likely that recovery in the world economy would be slow and hesitant, with uncertainties weighted to the down side. The balance of global economic data released since the Budget has been increasingly buoyant, particularly in the United States, Japan and East Asia. Fears of deflation and SARS contagion have both dissipated rapidly. Consensus economics forecasts of world growth have undergone four consecutive upward revisions. The OECD's *Economic Outlook* in November expects growth in the industrialised economies to lift from 2 percent in 2002 to 3 percent in 2004. Expectations of faster world growth have been reflected in rising prices for primary commodities and in a 5 percent gain in Australia's terms of trade in the year to September.

Domestic Economy

The domestic economy has strengthened since the Budget. The pace of consumer spending has increased, business profits and confidence are high, and the labour market has tightened. Agricultural output has partially rebounded from the drought — although the impact on exports and incomes is only just starting to be felt. Buoyant world commodity prices have benefited the mining sector, partly offsetting the drag from the higher exchange rate. These improvements were reflected in the strong September quarter gains of 1.2 percent in national GDP and 0.6 percent in NSW state final demand. Overall, prospects for the domestic economy are markedly better than was the case six months ago.

In the Budget, the outlook for agriculture was hopeful but uncertain. Subsequently, late winter rains across most of southern Australia provided the basis for a much improved wheat crop in 2003-04. ABARE forecasts that NSW winter grain production in 2003-04 will be 138 per cent higher than the previous year, although rainfall variation has reduced yields and downgraded grain quality in some regions. The recovery in farm output should provide a strong boost to rural incomes and to businesses in the agricultural sector as the year progresses.

In the Budget, household consumption growth was expected to moderate in 2003-04. Consumer demand instead has strengthened, with robust growth in retail trade and motor vehicle sales. Household confidence has been boosted by further gains in dwelling prices, a recovery in equities, a strong labour market, and a steady flow of positive world economic news. Annual growth in household consumption accelerated to 4 percent in September — the strongest in three years.

NSW dwelling investment was expected to ease further in 2003-04, and this has been borne out in trends to date. Dwelling construction activity fell 0.4 percent in March, 1.1 percent in June, and 3.3 percent in the September quarter. Dwelling approvals regained strength in the September quarter, however, pointing to firmer activity in the December quarter. The sector's resilience was also reflected in continuing strong trends in housing credit and house prices through September-October.

In the Budget, business investment was assumed to remain strong in 2003-04. Evidence to date has been mixed. Business investment declined slightly in the September quarter, with strong growth in business and equipment offset by a drop in non-residential construction. Nonetheless, surveyed capital expenditure expectations for 2003-04 have strengthened at the national level, especially in sectors such as construction, retail, finance and insurance in which New South Wales is well represented. In addition the pipeline of NSW engineering construction work yet to be done has doubled in the year to June and may be the precursor to much higher activity levels over the course of 2003-04.

In the Budget, employment growth was expected to slow substantially in 2003-04. Instead, employment growth strengthened in the first four months of the new financial year, driving the unemployment rate half a percentage point below its budget time level. Forward-looking indicators of the labour market, such as the ANZ job advertisements index and the NAB survey of employment expectations, remain positive for the outlook.

In the Budget, wage costs were expected to be constrained by slack in the labour market and slower construction activity. Trends have remained strong, however, with wage costs accelerating to an annual rate of 3.9 percent in September 2003 (compared to 3.1 percent in September 2002). The robust pace of domestic demand and employment, and major claims in the public sector, may keep wages under some pressure ahead.

Despite strong growth in wages and house prices, consumer prices were almost flat in New South Wales in the June and September quarters. Inflation was held in check by lower prices for imported goods which benefited from the rising exchange rate. While the budget forecast of 2¼ percent average inflation in 2003-04 has not been changed, the balance of uncertainties has swung to the down side.

In the Budget, a slowdown in domestic demand and only gradual global recovery was expected to allow the RBA to leave monetary policy unchanged. By November, however, the RBA judged that improved global conditions and domestic performance, together with excessive growth in private credit, required a move in policy from “accommodative” toward “neutral” levels (around 5½ to 6 percent). It raised the cash rate ¼ of a point in November and a further ¼ of a percentage point in December. Futures markets at mid-December were pricing in a further ¼ to ½ percent increase by mid-2004. Although the lag between monetary policy moves and changes in the real economy is often long and variable, some initial impact (particularly on more highly-leveraged property investors) is expected to be felt during the second half of 2003-04.

Uncertainties in the Outlook

While the outlook has generally improved since the Budget and near-term uncertainties appear more balanced, elements of uncertainty for the outlook in 2004-05 and beyond remain substantial:

The global economy remains vulnerable to a reversal of recent gains. The sustainability of recent growth surges in the US and Japan remains to be demonstrated. Severe financial imbalances (large and growing fiscal and current account deficits) and geopolitical stresses persist in the United States. Japan has yet to complete the restructuring required to corporate and financial institutions. European policy responsiveness remains hampered by the EU Stability Pact. The global economy thus remains extremely exposed to further shocks.

Full recovery from the 2002 drought may take several years: losses to breeding stock are larger than previously anticipated, and reservoir levels are still low. This increases the vulnerability of the agricultural sector to a recurrence of adverse climatic conditions.

While the forecasts assume only a moderate downturn in the dwelling sector, past history demonstrates the extreme volatility of this sector. Given the linkages between housing construction and the broader economy, the implications of a larger than anticipated adjustment should not be underestimated.

Falling unemployment, while welcome, may increase wage pressures over the next two years.

In its recent monetary policy statement the RBA clearly focussed its concern on the excessive pace of growth in private sector credit. If a return of policy to “neutral” proved insufficient to dampen credit growth, then still higher interest rates could not be precluded. The impact of such a scenario on demand and economic growth in 2004-05 might be substantial.

2. FISCAL POSITION AND OUTLOOK

2.1 ACTUAL RESULTS FOR FOUR MONTHS ENDED 31 OCTOBER 2003 AND LATEST PROJECTED 2003-2004 BUDGET ESTIMATES

Table 2.1: General Government Sector 2003-04 Operating Statement

	12 Months to 30/06/2003 Actual \$m	12 Months to 30/06/2004 Budget \$m	12 Months to 30/06/2004 Projection \$m	Variance \$m	4 Months to 31/10/2003 Actual \$m
State Revenues					
Taxation	14,161	14,198	14,981	783	5,079
Commonwealth Grants	15,228	15,497	15,548	51	5,573
Financial Distributions	1,238	1,496	1,538	42	506
Fines, Regulatory Fees & Other	864	842	829	(13)	278
Total State Revenues	31,491	32,033	32,896	863	11,436
Operating Revenues					
Sale of Goods and Services	2,726	2,656	2,706	50	915
Investment Income	443	637	643	6	195
Grants and Contributions	698	346	602	256	202
Other	688	264	308	44	79
Total Operating Revenues *	4,555	3,903	4,259	356	1,391
Expenses					
Employee Related					
- Superannuation	2,150	2,320	2,298	(22)	769
- Other	14,264	14,745	15,364	619	5,013
Other Operating	7,292	7,355	7,691	336	2,344
Maintenance	1,319	1,207	1,385	178	379
Depreciation and Amortisation	1,773	1,791	1,775	(16)	596
Current Grants and Subsidies	5,419	5,516	5,574	58	1,948
Capital Grants	1,315	1,182	1,243	61	309
Finance	806	796	772	(24)	262
Total Expenses *	34,338	34,912	36,101	1,189	11,620
GFS Operating Balance	1,708	1,024	1,054	30	1,207
Less Capital Expenditure	3,348	3,499	3,369	(130)	925
Plus Depreciation	1,773	1,791	1,775	(16)	596
Asset Sales	486	727	689	(38)	118
BUDGET RESULT	619	43	150	107	996

(*) Note: Includes \$287 million for the first time inclusion for accounting purposes of school bank accounts in 2003-04.

BUDGET RESULT

The projected general government budget result for 2003-04 is \$150 million. This represents an increase of \$107 million from the budget estimate of \$43 million.

Revenues

Total revenue is projected to be 2.6 percent or \$932 million higher than the 2003-04 Budget estimate. This is net of the first time inclusion for accounting purposes of school bank account transactions of \$287 million which have increased both revenues and expenses by the same amount.

Taxation revenue is expected to be \$783 million above budget, primarily due to the continued strength of the property market. Transfer duty revenue is now projected to be around 9 percent higher than in 2002-03. Strong demand for property has been evident in higher house prices and robust sales volumes. A significant feature of the current market is the historically high level of investor demand.

There are early signs that the property market may be close to its peak. After a long period of sustained price increases, growth in Sydney house prices was relatively low in the September quarter and auction clearance rates have fallen to below the corresponding period last year. While housing finance approvals remain strong, available data has yet to reflect the impact of the two successive interest rate increases. The current estimates incorporate an expected easing in property market conditions, which will mainly affect revenue in 2004-05.

Commonwealth grants revenue is projected to exceed the budget estimate by \$51 million, mainly as a result of an increase in specific purpose payments (SPP's) of \$83 million, the main component being a \$49 million increase in drought assistance. This is offset by a reduction of \$25 million in National Competition Policy payments due to penalties imposed by the Commonwealth in relation to chicken meat industry legislation and regulation of liquor sales.

Financial distributions are projected to be \$42 million or 2.8 percent higher than the budget time estimate. Dividends from the Snowy Hydro Limited are expected to increase by \$22 million due to favourable electricity spot market and contract prices over the past 12 months. Snowy Hydro Limited was also able to successfully negotiate innovative commercial opportunities in regards to their water management strategies. Dividends are also higher due to increased spot volume and prices within the electricity sector more generally, increased land sales within Landcom and sustained market demand for structural timber supplied by State Forests.

Operating revenues are expected to increase by \$70 million, net of the above mentioned school bank account transactions. This is predominantly due to receipts of \$80 million received by the RTA for construction of the Lane Cove Tunnel. Additional expenditure of \$60 million in this year and \$20 million in 2005-06 is now planned offsetting this additional income.

Expenses

Expenses are projected to exceed the budget estimate by 2.6 percent, or \$902 million, net of the above mentioned school bank account transactions of \$287 million.

A number of unexpected expenses have arisen in the current year which have affected the budget result.

The methodology for calculating long service leave has been adjusted to allow a more accurate estimate of this expense. This review has resulted in an increase in the expense in 2003-04 by \$38 million.

The drought is projected to increase expenditure by \$70 million in the Department of Agriculture and the Rural Assistance Authority, partly funded through higher Commonwealth grants.

These increases have been partly offset by a reduction in superannuation expenses of \$22 million. This is due to higher investment returns expected in 2003-04, in the defined benefit fund, offset by revised estimates of contributions to accumulation schemes. Interest costs are also expected to be lower due to higher than anticipated cash balances at June 30, 2003.

Additional resources have been made available to the following priority areas:

- Department of Education and Training expenses are projected to increase significantly above budget (net of school transactions noted above). This includes \$229 million for the recent teachers award in 2003-04 (\$308 million in a full year). Additional money also be spent on school cleaning, higher-than-expected enrolments and increased administrative staff hours.
- The Roads and Traffic Authority expenses are projected to increase by \$253 million on maintenance, road safety, traffic and transport management programs and revised depreciation road cost indexes. These are to be funded from increased RTA revenues and a re-allocation of funds from the capital program. Consequently this has minimal impact on the budget result.
- Ministry of Transport expenses are projected to increase by \$71 million reflecting additional grants to the State Rail Authority to meet operating costs; funding for private transport operators to meet the costs of subsidy schemes including school student transport; the establishment of the Independent Transport Safety and Reliability Regulator and transport costs associated with major sporting events (partially offset by fare revenues).
- Health expenses are projected to increase by \$90 million. The cost of the Nurses award decision will be an additional \$71 million. This decision also raises expenditure in the forward years. Other increases in health expenditure include increased ambulance service costs.
- The Government will provide the Department of Ageing, Disability and Home Care with a further \$72.4 million in 2003-04 to support the department's service delivery. This includes funding for the Department's Service Access System, progression of the devolution program, accommodation services for people with disabilities and adult training and learning support programs.
- NSW Police will incur additional expenditure in 2003-04 of \$64 million. This includes \$38 million for additional police officers and \$10 million for operational costs associated with the IT network upgrade.
- Other increases in expenditure include \$12 million in structural adjustment payments to farmers in the Namoi Valley, \$13 million to cut red tape in business licencing, and \$7 million for counter-terrorism measures, including a new police helicopter and Opera House security.

Some of the above increases in expenses have been offset by calling on the Treasurer's Advance of \$240 million.

OPERATING SURPLUS

The above revenue and expenditure revisions have increased the projected GFS operating result by \$30 million to \$1,054 million. In addition, lower capital expenditure, offset by lower than expected asset sales, have contributed to an expected improved Budget result of \$150 million.

Depreciation expenses are projected to be lower than budget mainly due to a revised accounting treatment in the Roads and Traffic Authority.

Capital expenditure is projected to be lower than budget mainly due to reclassifications to maintenance projects for the Roads and Traffic Authority and Education, delays in gaol constructions within Corrective Services, partly offset by NSW Police's IT network upgrade.

Asset sales and other adjustments are expected to be lower than budget mainly due to revisions to the sale of Crown land and financing arrangements for motor vehicles.

Table 2.2: 2003-04 Statement of Financial Position

	30-Jun-2003 Actual \$m	30-Jun-2004 Budget \$m	30-Jun-2004 Projection \$m	Variance \$m	31-Oct-2003 Actual \$m
ASSETS					
Financial Assets					
Cash and Deposits	1,091	866	994	128	1,270
Advances Paid	1,403	1,438	1,406	(32)	1,400
Investments, Loans and Placements	7,941	8,410	9,067	657	8,837
Other Non-Equity Assets	5,381	5,617	5,794	177	5,576
PTE/PFE Equity	66,216	50,942	67,073	16,131	66,518
Other Equity Assets	563	487	563	76	523
Total Financial Assets	82,595	67,760	84,897	17,137	84,124
Non-Financial Assets					
Land and Fixed Assets	78,944	76,321	80,033	3,712	79,009
Other Non-Financial Assets	1,046	1,122	1,150	28	1,091
Total Non-Financial Assets	79,990	77,443	81,183	3,740	80,100
TOTAL ASSETS	162,585	145,203	166,080	20,877	164,224
LIABILITIES					
Deposits Held	52	67	55	(12)	46
Advances Received	1,804	1,694	1,672	(22)	1,776
Borrowing	10,166	10,192	9,969	(223)	10,272
Provisions	25,889	27,461	27,818	357	26,458
Other Non-Equity Liabilities	3,634	3,402	3,447	45	3,153
TOTAL LIABILITIES	41,545	42,816	42,961	145	41,705
NET WORTH	121,040	102,387	123,119	20,732	122,519
Net Debt (underlying) ^(a)	3,238	3,737	2,738	(999)	2,514
Net Financial Liabilities ^(b)	25,166	25,998	25,137	(861)	24,099

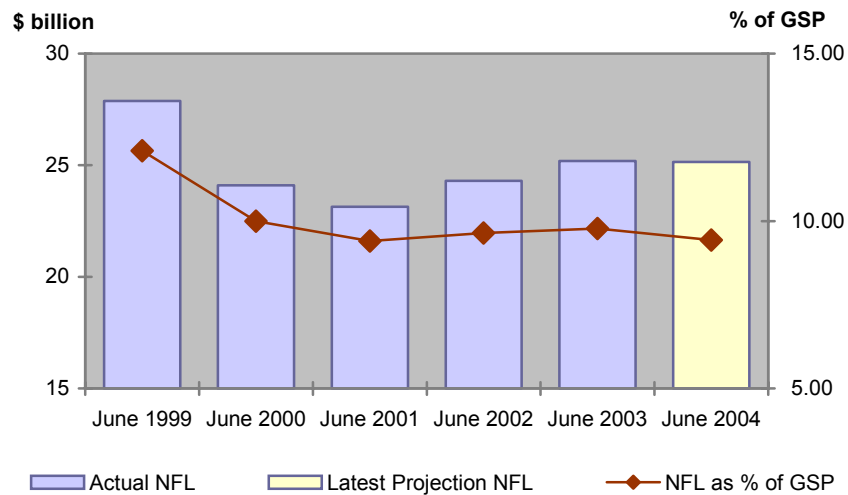
(a) Adjusted for the deferral of superannuation contributions for the period 1 July 2003 to 30 June 2007. During this period payments will be made to the Liability Management Ministerial Corporation, reducing unadjusted net debt.

(b) Excludes PTE/PFE Equity

NET FINANCIAL LIABILITIES

Net financial liabilities as at June 2004 are projected to be \$861 million lower than the budget time estimate. This is primarily due to stronger budget results in 2002-03 of \$420 million, and the expected improvement in 2003-04 of \$107 million. The 2002-03 improved result has been invested as a health super-growth fund, with annual interest earnings of \$23 million dedicated to capital projects within the Department of Health. Cash assets are also anticipated to be higher in 2003-04 compared to the 2003-04 Budget due to the consolidation of school bank balances amounting to \$226 million.

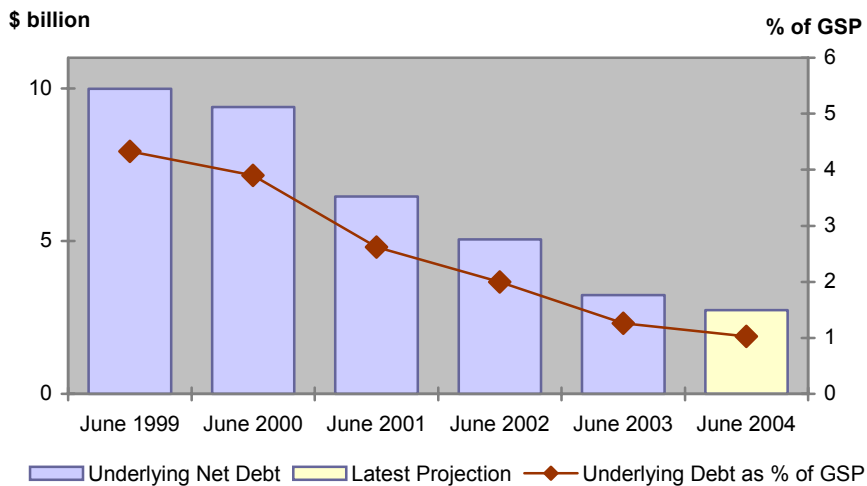
Figure 2.2: General Government Net Financial Liabilities (NFL)



NET DEBT

Underlying net debt as at June 2004 is projected to be \$999 million lower than the budget time estimate. This is primarily due to the decrease in underlying net debt of \$765 million between the June 2003 Budget time projection and the actual 30 June 2003 result and a projected increase in the cash result for 2003-04 amounting to \$256 million.

Figure 2.3: General Government Underlying Net Debt



NET WORTH

General government sector net worth was \$122,519 million at 31 October 2003. The projected result for 30 June 2004 is \$123,119 million, which is \$20,732 million higher than the budgeted figure of \$102,387 million.

The increase of \$20,732 million is primarily due to the improvement in net worth of \$20,617 million between the June 2003 Budget time projection and the actual 30 June 2003 result (see below). Net worth is further improved by the increased projected operating surplus for 2003-04 of \$30 million.

The \$20,617 million improvement in net worth in 2002-03 was primarily due to transactions that occurred in June 2003.

Assets increased by \$11,937 due to revaluations within public housing of \$6,760 million, \$2,179 million for rail infrastructure assets and \$3,269 million for the Roads and Traffic Authority's infrastructure and property assets.

There was a reinstatement of rail infrastructure assets of \$7,828 million.

There was also the recognition for the first time of Australian Museum collection assets (\$530 million) and payroll tax receivables of (\$171 million) and cash balances associated with school bank accounts (\$226 million).

Figure 2.1: Net Worth of the General Government Sector

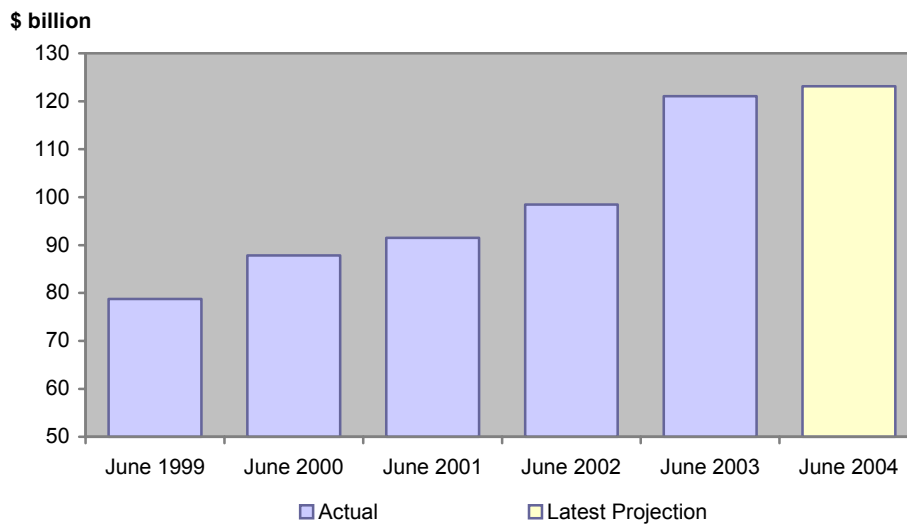


Table 2.3: 2003-04 GFS Cash Results

	12 Months to 30/06/2003 Actual \$m	12 Months to 30/06/2004 Budget \$m	12 Months to 30/06/2004 Projection \$m	Variance \$m	4 Months to 31/10/2003 Actual \$m
Cash Receipts from Operating Activities					
Taxes Received	13,956	14,183	15,098	915	4,820
Receipts from sales of goods & services	3,053	2,875	2,853	(22)	1,037
Grants/Subsidies Received	17,696	15,329	15,648	319	5,461
Other Receipts	4,093	4,181	3,994	(187)	1,474
Total Cash Receipts from Operating Activities	38,798	36,568	37,593	1,025	12,792
Cash Payments from Operating Activities					
Payments for goods & services	(23,978)	(24,918)	(26,067)	(1,149)	(8,635)
Grants & Subsidies Paid	(6,987)	(5,227)	(5,310)	(83)	(1,760)
Interest Paid	(822)	(873)	(854)	19	(163)
Other Payments	(1,759)	(1,810)	(1,447)	363	(553)
Total Cash Payments from Operating Activities	(33,546)	(32,828)	(33,678)	(850)	(11,111)
Net Cash Flows from Operating Activities	5,252	3,740	3,915	175	1,681
Cash Flows from Investments in Non-Financial Assets					
Purchases of New Non-Financial Assets	(3,003)	(3,152)	(3,029)	123	(710)
Sale of Non-Financial Assets	477	684	645	(39)	118
Total Cash Flows from Investments in Non-Financial Assets	(2,526)	(2,468)	(2,384)	84	(592)
Cash Flows from Investments in Financial Assets					
Financial Assets for Policy Purposes	966	188	113	(75)	87
Financial Assets for Liquidity Purposes	(1,114)	(1,299)	(1,016)	283	(898)
Cash Flows from Financing Activities					
Advances Received (net)	(31)	(95)	(130)	(35)	15
Borrowing (net)	(1,018)	(305)	(455)	(150)	(107)
Deposits Received (net)	(10)	(1)	1	2	(7)
Total Cash Flows from Financing Activities	(1,059)	(401)	(584)	(183)	(99)
Net Increase/(Decrease) in Cash Held	1,519	(240)	44	284	179
Net Cash from Operating Activities, Investments in Non-Financial Assets and Distributions Paid	2,726	1,272	1,531	259	1,089
Assets acquired under finance leases	(345)	(347)	(340)	7	(215)
Equals Surplus/(Deficit)	2,381	925	1,191	266	874
Impact of contributions for prepaid superannuation and Liability Management Fund					
	(1,651)	(847)	(857)	(10)	(276)
Adjusted Surplus/(Deficit)	730	78	334	256	598

The projected underlying cash result for 2003-04 of \$334 million is \$256 million higher than the budget estimate of \$78 million. This is due to the same factors impacting the budget result and a \$109 million movement in accruals, mainly relating to superannuation and insurance liabilities and financial distributions.

2.2 FORWARD ESTIMATES 2004-05 TO 2006-07

Table 2.1: General Government Sector Operating Statement - Forward Estimates 2004-05 to 2006-07

	2003-04 Latest Projection \$m	2004-05 Estimate \$m	2005-06 Estimate \$m	2006-07 Estimate \$m
State Revenues				
Taxation	14,981	15,163	16,033	16,946
Commonwealth Grants	15,548	15,789	16,472	16,770
Financial Distributions	1,538	1,419	1,673	1,780
Fines, Regulatory Fees & Other	829	878	873	827
Total State Revenues	32,896	33,249	35,051	36,323
Operating Revenues				
Sale of Goods and Services	2,706	2,734	2,826	2,899
Investment Income	643	789	907	1,021
Grants and Contributions	602	576	582	589
Other	308	211	206	229
Total Operating Revenues	4,259	4,310	4,521	4,738
Expenses				
Employee Related				
- Superannuation	2,298	2,439	2,596	2,762
- Other	15,364	16,057	16,813	17,736
Other Operating	7,691	7,837	8,192	8,568
Maintenance	1,385	1,251	1,324	1,366
Depreciation and Amortisation	1,775	1,796	1,819	1,861
Current Grants and Subsidies	5,574	5,450	5,648	5,842
Capital Grants	1,243	1,381	1,373	1,312
Finance	772	712	695	636
Total Expenses	36,101	36,923	38,460	40,083
GFS Operating Balance	1,054	636	1,112	978
Less Capital Expenditure	3,369	3,242	3,165	3,028
Plus Depreciation	1,775	1,796	1,819	1,861
Asset Sales & Other	689	535	328	295
BUDGET RESULT	150	(275)	94	106
Adjusted cash deficit/surplus	334	34	288	434
Net Debt (underlying)^(a)	2,738	2,695	2,023	1,516
Net Financial Liabilities^(b)	25,137	25,760	25,871	26,102

(a) Adjusted for the deferral of superannuation contributions for the period 1 July 2003 to 30 June 2007. During this period payments will be made to the Liability Management Ministerial Corporation, reducing unadjusted net debt.

(b) Excludes PTE/PFE Equity

Forward Estimates

The projected GFS operating statement of the general government sector for the four years to 2006-07 consists of three surpluses totalling \$350 million and a deficit in 2004-05 of \$275 million.

The 2003-04 projections are fully discussed in section 2.1 of this Review. The revised results for 2004-05 onwards are driven by a number of post budget developments, the most significant of which are:

- The impact of two recent award wage decisions. The teachers' wage award is expected to increase education expenditure by around \$308 million each year and the nurses' wage award is expected to increase Health expenditure by around \$86 million each year;
- Increased expenditure in a number of agencies including the Departments of Education, Health and Transport;
- A joint Commonwealth and State commitment to restore the Murray River by providing 500 gegalitres of water at a cost to New South Wales of \$69 million over the next 3 years (\$115 million over a total period of 5 years);
- Lower Commonwealth grants reflecting changed parameters;

Offset by:

- Lower superannuation expenses due to higher than anticipated investment returns and taxation changes;
- Lower interest costs from receipt of regearing funds in 2003-04;
- Improved taxation revenue forecasts reflecting the carry-forward effects of upward revisions in 2003-04. However transfer duties in 2004-05 will decline, as a result of the expected downturn in the property market; and
- Higher than budgeted financial distributions in 2005-06 and 2006-07 in the Water and Property development sectors.

Table 2.5: Budget Results

	2003-04 \$m	2004-05 \$m	2005-06 \$m	2006-07 \$m
Budget Time	43	303	821	932
Half-Yearly Budget Review	150	-275	94	106

GFS CASH RESULT

The general government sector is projected to be in surplus in all years. The cash results are higher than the accrual budget results mainly because of the differential impact of superannuation, insurance and financial distributions on cash and accrual results.

NET FINANCIAL LIABILITIES

Net financial liabilities are expected to increase from \$25.1 billion in 2003-04 to \$26.1 billion in 2006-07. This reflects the impact of budget results over the forward estimates period.

2.3 FACTORS AFFECTING BUDGET OUTCOMES

Mid year review estimates are framed on a “no policy change” assumption – ie, that fiscal policies at the time apply to the forward estimates period.

In practice, however, actual financial outcomes will depend on various factors, including policy changes, changes in parameters influencing the demand for or cost of government services, and unexpected events such as natural disasters.

FACTORS AFFECTING TAX REVENUES

The major factors affecting tax revenues relate to the economic outlook, with, in particular, the outlook for employment and wages affecting payroll taxes.

- The global outlook has rapidly improved since the Budget. However, it is not yet clear that the global recovery will be sustained through 2004.
- Domestically, consumer confidence and spending have been buoyed by low interest rates, rising house prices, declining unemployment and the improved global outlook. These represent more favourable conditions than anticipated in the last Budget, leading to slightly higher output and employment growth forecasts.

Perhaps the key factor expected to affect tax revenue in 2003-04 and 2004-05 is the residential property market cycle, which will directly flow through to transfer duty and mortgage duty revenues. Always volatile, the outlook for these revenues is particularly uncertain at this time. Transfer duty revenue is vulnerable to volatility resulting from variations in both property prices and sales volumes.

- Latest estimates allow for a softening in the property market in the second half of 2003-04. Transfer duty revenue is expected to decline by around \$400 million in 2004-05, a relatively mild decline compared with previous cycles which have involved declines of as high as 35 percent in a single year.
- While the extent and timing of a property market downturn is extremely difficult to predict, there are clear signs that construction activity in New South Wales has slowed. As yet, however, there are only tentative signs that the overall residential property market has peaked.
- The RBA raised interest rates in late 2003 in response to an improved global outlook and an unexpected lift in growth in Australian domestic demand. A continuation of strong domestic demand growth could fuel inflation concerns and higher than expected interest rates next year. A more restrictive monetary policy stance than assumed would likely lead to a greater slowdown in the property market than is assumed in the revenue forecasts.

FACTORS AFFECTING NON-TAX REVENUES

Commonwealth Grants

Commonwealth grants (of which the largest component is GST revenue grants) are the largest single non-tax revenue item. New South Wales' share of general purpose grants is based on relativities recommended by the Commonwealth Grants Commission (CGC) and ABS population estimates each year.

General purpose grants in 2003-04 have been revised due to changes in inflation and population estimates.

Much greater uncertainty arises in relation to general purpose grants from 2004-05, as these will depend on the outcome of the 2004 methodology review of the Commonwealth Grants Commission. The review is nearly complete and is due to be presented to the Minister for Finance and Administration on 25 February 2004. The report will determine inter-State relativities for Commonwealth grants from 2004-05.

While no change in relativities from the methodology review is assumed for the purpose of this report, NSW has made a strong submission to reduce its \$2,541 million a year subsidy to other States.

A number of major specific purpose payment (SPP) agreements between the Commonwealth and States, including for vocational education and disability services, are under renegotiation, with implications for SPP funding over the medium term. Like general purpose grants, most SPP funding is also dependent on inflation and ABS population estimates.

Risks in Commonwealth payments also arise in relation to National Competition Policy (NCP) payments. The National Competition Council (NCC) can impose penalties (ie, a reduction in NCP payments) depending on its assessment of States' compliance with agreed reforms under the competition policy agreements. Penalties may be reversed in future years depending on NCC assessment of progress.

Revenue from Public Trading Enterprises

Revenue from public trading enterprises may be affected by uncertainties in the economic outlook - which directly affects their trading environment - and regulatory decisions on prices. Developments in financial asset markets also flow through to revenue from PTEs - eg, increases in PTE superannuation liabilities/expenses due to poor asset returns, or changes in the regulatory regime, or adverse developments in global commodity markets, can lead to reduced dividends.

Investment Income

Investment income is subject to the volatility of financial markets. As clearly suggested by financial outcomes in previous years, poor investment returns can significantly reduce investment income from assets of the Insurance Ministerial Corporation.

FACTORS AFFECTING EXPENDITURE

Changes in demand for public sector services

- Changes in demand for public sector services are difficult to predict, and are driven by demographic, technological and social change and other factors outside of the Government's control. These changes may exert pressure on the Government's capacity to maintain existing programs, particularly those that are demographically sensitive.

Unexpected events

- Unexpected events, such as natural disasters (eg, drought and bushfires), corporate collapses such as that of HIH and the need to respond to political developments abroad (eg, increased need for security and anti-terrorist measures) may generate additional funding demands. Events such as adverse weather can also affect the implementation of capital works programs.

Unfunded superannuation liabilities

- Factors affecting the level of unfunded superannuation liabilities eg, financial markets yielding poor returns on superannuation assets, or changes to demographic and other macroeconomic assumptions increasing the actuarially calculated liability, may increase superannuation expense. The experience of recent years has shown that such impacts on the financial statements of the public sector can be substantial.

Employee related expenses

- The single largest cost faced by the NSW Government is employee related expenses - wages, superannuation and other employee costs – which account for almost half of total expenses of the general government sector. Major public sector wage agreements are due to expire prior to and during 2004-05. Each percentage point increase in wage rates raises general government expenses by roughly \$170 million. Public sector wage claims over and above existing agreements or from new claims after current agreements expire may therefore significantly affect the estimates.

Contingent liabilities

- Expenditure pressures may also arise from contingent liabilities, which normally include claims for compensation or litigation; state guarantees under statute; other guarantees extended in order to facilitate the provision of services and infrastructure; or other developments where government intervention is justified on the basis of the public interest.

APPENDIX A: UNIFORM PRESENTATION OF GOVERNMENT FINANCE STATISTICS

A Uniform Presentation Framework (UPF) for financial aggregates has been agreed between the Commonwealth, State and Territory Governments.

As part of the Framework, each jurisdiction is to publish a mid year report, ie a Half-Yearly Budget Review, by the end of February each year. The financial data in this report is consistent with the Australian Bureau of Statistics (ABS) Government Finance Statistics (GFS). This UPF report is prepared on an accrual basis and includes operating statements, balance sheets and cash flow statements for NSW General Government Sector, Public Non-Financial Corporation Sector and Total Non-Financial Public Sector. In the GFS classification scheme each state public sector body is categorised into one of three sectors:

- General Government (GG), which covers all agencies that are generally engaged in the production of goods and services outside the normal market mechanisms;
- Public Non-financial Corporations (PNFC)^(a) which are largely self-funded from user charges and have been given a specific charter to run their businesses on commercial lines, including the achievement of a commercial rate of return on the resources employed (PNFCs are responsible for supplying public infrastructure services, including electricity, ports, water and public transport); and
- Public Financial Corporations (PFC)^(b) which may accept demand time or savings deposits and/or have the authority to incur liabilities and acquire financial assets in the market on their own account (an example of a PFC is NSW Treasury Corporation).

The Half-Yearly Budget Review presents revised fiscal estimates for the current Budget year and the three following years for the GG Sector. In addition, revised estimates are presented for the PNFC Sector and the Total Non-financial Public Sector (ie a consolidation of the GG Sector and the PNFC Sector). These revised estimates take into account fiscal and economic developments since the commencement of the budget year.

The Half-Yearly Budget Review also includes a revised estimate of the Loan Council Allocation.

TREATMENT OF CERTAIN COMMONWEALTH PAYMENTS

The estimates in this appendix differ from those contained in the main body of the Review because of the treatment of certain Commonwealth payments.

For certain Commonwealth payments (eg non-government schools and local government tax sharing and road funding) the State essentially acts as an agent of the Commonwealth. Despite the fact that the State has no control over these payments and is not involved in any negotiations concerning them, GFS conventions require their inclusion in the State sector.

While the inclusion of these payments does not distort the underlying financial position, the growth in expenditure in these areas can be significantly different than for the remainder of the State sector. In light of these considerations, certain Commonwealth grants classified as passing through (rather than to) the State in the Commonwealth Budget are excluded from the tables in the main body of this review.

Notes:

(a) The PNFC sector was formerly known as the Public Trading Enterprise or PTE sector.

(b) The PFC sector was formerly known as the Public Financial Enterprise or PFE sector.

PUBLIC NON-FINANCIAL CORPORATIONS SECTOR PERFORMANCE

The commercial policy framework that applies to the Public Non-financial Corporation (PNFC) Sector is designed to promote the appropriate management of financial risk and shareholder value. Therefore it is to be expected that the performance of the sector in aggregate will reflect reasonable commercial outcomes, while being mindful of the constraints under which a number of New South Wales PNFCs operate.

The considerations influencing the management of financial liabilities of PNFCs differ from those relevant to the General Government Sector. The financial liabilities of commercial enterprises support assets that earn a financial return in addition to providing public services. In contrast, assets held by the General Government Sector do not earn market returns and are funded from taxation revenue.

The amount of debt held by PNFCs should generally reflect typical gearing levels of private firms in the relevant industries, in order to provide incentives for public enterprises to use their resources efficiently. Net debt of the PNFC Sector will increase over the forward estimates period, reflecting the continuing shift to commercially comparable gearing levels and new investment in electricity networks, water and sewerage systems, rail track and other infrastructure.

Over recent years the PNFC Sector has been regeared to ensure that government commercial authorities face the same commercial discipline as the private sector.

The PNFC Operating Statement reported in Table A-2 includes two important measures, the Net Operating Balance and Net Lending/Borrowing. The 2003-04 Net Operating Balance is projected to be negative \$45 million compared to the budget of positive \$223 million.

During 2003-04 PNFCs will be investing in excess of \$3.5 billion in transport, power, water and other infrastructure. The Sector's Net Borrowing result for the year is projected to be \$1,968 million compared to the budget of \$1,612 million. There are many factors affecting the projected increase in Net Borrowing. They include higher expenditure for Landcom's development activities, an increase in electricity generator coal stocks, and higher water operating costs associated with the drought. Further, some PNFC land sales have been deferred.

The equity of the PNFC Sector, reported in Table A-5, is expected to increase to \$67,468 million by June 2004. The primary reason for the increase is an upward revision to the valuation of some rail infrastructure and public housing assets since the original budget was established.

Table A-8 reports a projected cash deficit for the PNFC Sector of \$1,555 million compared to the budgeted deficit of \$1,286 million. This is primarily explained by the factors outlined above for the Net Borrowing result.

Table A-1: NSW General Government Sector Operating Statement (ABS Basis)

	Budget	Revised	Forward Estimates		
	2003-04	2003-04	2004-05	2005-06	2006-07
	\$m	\$m	\$m	\$m	\$m
GFS Revenue					
Taxation revenue	14,199	14,981	15,163	16,033	16,946
Current grants and subsidies	16,557	16,870	17,161	17,909	18,403
Capital grants	917	917	864	799	610
Sales of goods and services	2,909	2,961	3,039	3,114	3,129
Interest income	637	643	789	907	1,021
Other	2,651	2,719	2,476	2,743	2,887
Total revenue	37,870	39,091	39,492	41,505	42,996
less GFS Expenses					
Employee expenses	15,941	16,556	17,323	18,129	19,106
Depreciation	1,791	1,775	1,796	1,819	1,861
Other operating expenses	9,862	10,370	10,398	10,848	11,277
Nominal superannuation interest expense	903	880	974	1,076	1,184
Other interest expenses	796	772	712	695	636
Other property expenses	...	...	...	...	...
Current transfers	6,338	6,408	6,240	6,422	6,612
Capital transfers	1,215	1,276	1,413	1,404	1,342
Total expenses	36,846	38,037	38,856	40,393	42,018
equals GFS net operating balance	1,024	1,054	636	1,112	978
less Net acquisition of non-financial assets					
Purchases of non-financial assets	3,152	3,029	3,002	3,018	2,911
less Sales of non-financial assets	(684)	(645)	(505)	(302)	(267)
less Depreciation	(1,791)	(1,775)	(1,796)	(1,819)	(1,861)
plus Change in inventories	2	1	(1)	...	...
plus Other movements in non-financial assets	302	294	211	121	89
equals Total net acquisition of non-financial assets	981	904	911	1,018	872
equals GFS Net lending / (Borrowing)^(a)	43	150	(275)	94	106

Notes:

(a) Also known as Fiscal Balance.

**Table A-2: NSW Public Non-financial Corporation Sector Operating Statement
(ABS Basis)**

	<i>Budget</i>	<i>Revised</i>	<i>Forward Estimates</i>		
	<i>2003-04</i>	<i>2003-04</i>	<i>2004-05</i>	<i>2005-06</i>	<i>2006-07</i>
	<i>\$m</i>	<i>\$m</i>	<i>\$m</i>	<i>\$m</i>	<i>\$m</i>
GFS Revenue					
Sales of goods and services	9,821	10,076	10,879	11,508	12,140
Current grants and subsidies	1,467	1,494	1,385	1,405	1,419
Capital grants	634	634	693	670	655
Interest income	52	53	54	57	59
Other	804	771	778	808	814
Total revenue	12,778	13,028	13,789	14,448	15,087
less GFS Expenses					
Employee expenses	3,017	3,141	3,133	3,207	3,326
Depreciation	1,660	1,715	1,851	1,923	1,986
Other operating expenses	5,433	5,764	6,228	6,497	6,748
Interest expenses	900	894	936	1,017	1,096
Other property expenses	1,416	1,429	1,361	1,596	1,698
Current transfers	129	130	127	131	137
Capital transfers	...	...	...	...	...
Total expenses	12,555	13,073	13,636	14,371	14,991
equals GFS net operating balance	223	(45)	153	77	96
less Net acquisition of non-financial assets					
Purchase of non-financial assets	3,640	3,573	3,902	3,917	3,760
Sales of non-financial assets	(276)	(248)	(193)	(195)	(107)
less Depreciation	(1,660)	(1,715)	(1,851)	(1,923)	(1,986)
plus Change in inventories	13	232	20	87	81
plus Other movements in non-financial assets	118	81	92	95	99
equals Total net acquisition of non-financial assets	1,835	1,923	1,970	1,981	1,847
equals GFS Net lending / (Borrowing) ^(a)	(1,612)	(1,968)	(1,817)	(1,904)	(1,751)

Notes:

(a) Also known as Fiscal Balance.

Table A-3: NSW Non-financial Public Sector Operating Statement (ABS Basis)

	<i>Budget</i>		<i>Forward Estimates</i>		
	<i>2003-04</i>	<i>2003-04</i>	<i>2004-05</i>	<i>2005-06</i>	<i>2006-07</i>
	<i>\$m</i>	<i>\$m</i>	<i>\$m</i>	<i>\$m</i>	<i>\$m</i>
GFS Revenue					
Taxation revenue	13,545	14,312	14,472	15,319	16,213
Current grants and subsidies	16,523	16,836	17,135	17,889	18,382
Sales of goods and services	12,562	12,871	13,751	14,451	15,095
Capital grants	917	916	862	798	609
Interest income	638	646	794	916	1,033
Other	1,950	2,004	1,830	1,884	1,979
Total revenue	46,135	47,585	48,844	51,257	53,311
less GFS Expenses					
Employee expenses	18,883	19,624	20,449	21,328	22,423
Depreciation	3,451	3,489	3,647	3,742	3,847
Other operating expenses	14,471	15,295	15,763	16,459	17,117
Nominal superannuation interest expense	903	880	974	1,076	1,184
Other interest expenses	1,646	1,616	1,600	1,664	1,685
Other Property expenses	...	...	...	...	...
Current transfers	4,987	5,066	4,967	5,125	5,323
Capital transfers	547	606	655	674	658
Total expenses	44,888	46,576	48,055	50,068	52,237
equals GFS net operating balance	1,247	1,009	789	1,189	1,074
less Net acquisition of non-financial assets					
Purchase of non-financial assets	6,791	6,600	6,901	6,932	6,669
Sales of non-financial assets	(960)	(893)	(697)	(497)	(374)
less Depreciation	(3,451)	(3,489)	(3,647)	(3,742)	(3,847)
plus Change in inventories	15	234	19	87	80
plus Other movements in non-financial assets	419	373	303	216	188
equals Total net acquisition of non-financial assets	2,814	2,825	2,879	2,996	2,716
equals GFS Net lending / (Borrowing) ^(a)	(1,567)	(1,816)	(2,090)	(1,807)	(1,642)

Notes:

(a) Also known as Fiscal Balance.

Table A-4: NSW General Government Sector Balance Sheet (ABS Basis)

	Budget	Revised	Forward Estimates		
	June 2004	June 2004	June 2005	June 2006	June 2007
	\$m	\$m	\$m	\$m	\$m
Assets					
Financial assets					
Cash and deposits	866	994	963	760	884
Advances paid	1,438	1,406	1,407	1,377	1,370
Investments, loans and placements	8,410	9,067	10,257	11,883	13,610
Other non-equity assets	5,617	5,794	5,768	6,097	6,359
Equity	51,429	67,636	69,721	70,837	72,104
Total financial assets	67,760	84,897	88,116	90,954	94,327
Non-financial assets					
Land and fixed assets	76,321	80,033	81,033	82,149	83,115
Other non-financial assets	1,122	1,150	1,200	1,268	1,353
Total non-financial assets	77,443	81,183	82,233	83,417	84,468
Total assets	145,203	166,080	170,349	174,371	178,795
Liabilities					
Deposits held	67	55	55	55	55
Advances received	1,694	1,672	1,628	1,485	1,440
Borrowing	10,192	9,970	9,718	9,332	9,245
Superannuation liability ^(a)	16,481	16,173	17,923	19,770	21,678
Other employee entitlements and provisions	10,980	11,645	12,042	12,555	13,131
Other non-equity liabilities	3,402	3,446	3,402	3,448	3,473
Total liabilities	42,816	42,961	44,768	46,645	49,022
NET WORTH	102,387	123,119	125,581	127,726	129,773
Net Financial Worth ^(b)	24,944	41,936	43,348	44,309	45,305
Net debt ^(c)	1,239	230	(1,226)	(3,148)	(5,124)
<i>Notes:</i>					
<i>(a) Comprises unfunded obligations.</i>					
<i>(b) Net financial worth equals total financial assets minus total liabilities.</i>					
<i>(c) Net debt equals the sum of deposits held, advances received and borrowing, minus the sum of cash and deposits, advances paid, and investments, loans and placements.</i>					
<i>(d) Adjusted for Crown deposits to the Liability Management Fund and for fund earnings that have been set aside to meet future superannuation obligations.</i>					
GFS net debt	1,239	230	(1,226)	(3,148)	(5,124)
<i>Impact of deposits to the Liability Management Fund</i>	2,498	2,508	3,921	5,171	6,640
Underlying net debt ^{(c) (d)}	3,737	2,738	2,695	2,023	1,516

**Table A-5: NSW Public Non-financial Corporation Sector Balance Sheet
(ABS Basis)**

	Budget	Revised	Forward Estimates		
	June 2004	June 2004	June 2005	June 2006	June 2007
	\$m	\$m	\$m	\$m	\$m
Assets					
Financial assets					
Cash and deposits	848	950	710	758	718
Investments, loans and placements	597	349	352	335	403
Other non-equity assets	2,173	2,122	2,216	2,292	2,344
Equity	54	50	79	93	109
Total financial assets	3,672	3,471	3,357	3,478	3,574
Non-financial assets					
Land and fixed assets	69,525	85,937	89,699	92,753	95,658
Other non-financial assets	308	241	275	268	262
Total non-financial assets	69,833	86,178	89,974	93,021	95,920
Total assets	73,505	89,649	93,331	96,499	99,494
Liabilities					
Deposits held	95	93	103	110	114
Advances received	1,056	1,090	1,064	1,037	1,010
Borrowing	13,799	13,554	14,981	16,556	17,911
Superannuation liability ^(a)	988	947	1,049	1,153	1,257
Other employee entitlements and provisions	4,457	4,648	4,715	5,120	5,446
Other non-equity liabilities	1,926	1,849	1,935	1,983	2,004
Total liabilities	22,321	22,181	23,847	25,959	27,742
Shares and other contributed capital ^(b)	51,184	67,468	69,484	70,540	71,752
NET WORTH	...	...	...	...	...
Net financial worth ^(c)	(69,833)	(86,178)	(89,974)	(93,021)	(95,920)
Net debt ^(d)	13,505	13,438	15,086	16,610	17,914

Notes:

(a) *Comprises unfunded obligations.*

(b) *The Australian Bureau of Statistics treats 'shares and other contributed capital' as a liability to the general government sector and deducts it to calculate a zero GFS net worth and negative net financial worth. However, these shares and other contributed capital reflect the value of the government's equity and cumulative earnings over time for the PFE sector.*

(c) *Net financial worth equals total financial assets minus total liabilities and minus shares and other contributed capital.*

(d) *Net debt equals the sum of deposits held, advances received and borrowing, minus the sum of cash and deposits, advances paid, and investments, loans and placements.*

Table A-6: NSW Non-financial Public Sector Balance Sheet (ABS Basis)

	Budget	Revised	Forward Estimates		
	June 2004	June 2004	June 2005	June 2006	June 2007
	\$m	\$m	\$m	\$m	\$m
Assets					
Financial assets					
Cash and deposits	1,714	1,944	1,673	1,519	1,602
Advances paid	382	316	343	340	360
Investments, loans and placements	9,007	9,415	10,607	12,216	14,012
Other non-equity assets	4,386	4,453	4,497	4,566	4,615
Equity	300	219	315	389	462
Total financial assets	15,789	16,347	17,435	19,030	21,051
Non-financial assets					
Land and fixed assets	145,846	165,970	170,732	174,901	178,773
Other non-financial assets	1,427	1,393	1,475	1,535	1,617
Total non-financial assets	147,273	167,363	172,207	176,436	180,390
Total assets	163,062	183,710	189,642	195,466	201,441
Liabilities					
Deposits held	162	148	158	165	170
Advances received	1,694	1,672	1,628	1,485	1,440
Borrowing	23,991	23,522	24,697	25,888	27,154
Superannuation liability ^(a)	17,469	17,120	18,972	20,923	22,935
Other employee entitlements and provisions	12,850	13,615	14,061	14,640	15,277
Other non-equity liabilities	4,509	4,514	4,545	4,639	4,692
Total liabilities	60,675	60,591	64,061	67,740	71,668
Shares and other contributed capital	...	...	...	...	...
NET WORTH	102,387	123,119	125,581	127,726	129,773
Net financial worth ^(b)	(44,886)	(44,244)	(46,626)	(48,710)	(50,617)
Net debt ^(c)	14,744	13,667	13,860	13,463	12,790
GFS net debt	14,744	13,667	13,860	13,463	12,790
<i>Impact of deposits to the Liability Management Fund</i>	<i>2,498</i>	<i>2,508</i>	<i>3,921</i>	<i>5,171</i>	<i>6,640</i>
Underlying net debt ^{(c) (d)}	17,242	16,175	17,781	18,634	19,430

*Notes:**(a) Comprises unfunded obligations.**(b) Net financial worth equals total financial assets minus total liabilities.**(c) Net debt equals the sum of deposits held, advances received and borrowing, minus the sum of cash and deposits, advances paid, and investments, loans and placements.**(d) Adjusted for Crown deposits to the Liability Management Fund and for fund earning that have been set aside to meet future superannuation obligations.*

Table A-7: NSW General Government Sector Cash Flow Statement^(a) (ABS Basis)

CASH FLOW	Budget	Revised	Forward Estimates		
	2003-04	2003-04	2004-05	2005-06	2006-07
	\$m	\$m	\$m	\$m	\$m
Cash receipts from operating activities					
Taxes received	14,183	15,098	15,157	16,030	16,946
Receipts from sales of goods and services	2,875	2,853	3,043	3,094	3,106
Grants/subsidies received	17,264	17,582	18,024	18,709	19,013
Other receipts	4,181	3,994	4,290	4,365	4,694
Total receipts	38,503	39,527	40,514	42,198	43,759
Cash payments for operating activities					
Payment for goods and services	(24,918)	(26,067)	(26,979)	(28,094)	(29,501)
Grants and subsidies paid	(7,161)	(7,244)	(7,223)	(7,358)	(7,441)
Interest paid	(873)	(854)	(683)	(866)	(636)
Other payments	(1,811)	(1,447)	(1,445)	(1,479)	(1,517)
Total payments	(34,763)	(35,612)	(36,330)	(37,797)	(39,095)
Net cash flows from operating activities	3,740	3,915	4,184	4,401	4,664
Net cash flows from investments in non-financial assets					
Sales of non-financial assets	684	645	505	302	267
Purchases of non-financial assets	(3,152)	(3,029)	(3,002)	(3,018)	(2,911)
Net cash flows from investments in non-financial assets	(2,468)	(2,384)	(2,497)	(2,716)	(2,644)
Net cash flows from investments in financial assets for policy purposes	188	113	(245)	203	69
Net cash flows from investments in financial assets for liquidity purposes	(1,299)	(1,016)	(1,191)	(1,628)	(1,726)
Net cash flows from financing activities					
Advances received (net)	(95)	(130)	(58)	(158)	(62)
Borrowing (net)	(305)	(455)	(171)	(286)	(207)
Deposits received (net)	(1)	1	(1)	(1)	(1)
Other financing (net)	...	...	(1)	...	1
Net cash flows from financing activities	(401)	(584)	(231)	(445)	(269)
Net increase (decrease) in cash held	(240)	44	20	(185)	94
SURPLUS / (DEFICIT)					
Net cash from operating activities and investments in non-financial assets	1,272	1,531	1,687	1,685	2,020
Finance leases and similar arrangements	(347)	(340)	(240)	(147)	(117)
SURPLUS / (DEFICIT)	925	1,191	1,447	1,538	1,903
<i>Notes:</i>					
(a) A positive number denotes a cash inflow, a negative (i.e. bracketed) sign denotes a cash outflow.					
(b) Deposits by the Crown to the Liability Management Fund and the fund's earnings have been set aside to meet future superannuation contributions.					
GFS SURPLUS/ (DEFICIT)	925	1,191	1,447	1,538	1,903
Impact of deposits to the Liability Management Fund ^(b)	(847)	(857)	(1,413)	(1,250)	(1,469)
UNDERLYING CASH SURPLUS/(DEFICIT) ^{(c) (d)}	78	334	34	288	434

**Table A-8: NSW Public Non-financial Corporation Sector Cash Flow Statement^(a)
(ABS Basis)**

CASH FLOW	Budget	Revised	Forward Estimates		
	2003-04	2003-04	2004-05	2005-06	2006-07
	\$m	\$m	\$m	\$m	\$m
Cash receipts from operating activities					
Receipts from sales of goods and services	10,023	10,466	11,367	12,081	12,666
Grants/subsidies received	2,123	2,144	2,093	2,091	2,088
Other receipts	1,949	1,997	2,075	2,171	2,200
Total receipts	14,095	14,607	15,535	16,343	16,954
Cash payments for operating activities					
Payment for goods and services	(8,685)	(9,391)	(9,685)	(9,965)	(10,257)
Grants and subsidies paid	(126)	(126)	(123)	(127)	(133)
Interest paid	(889)	(903)	(918)	(1,006)	(1,090)
Other payments	(1,574)	(1,743)	(1,726)	(1,938)	(2,056)
Total payments	(11,274)	(12,163)	(12,452)	(13,036)	(13,536)
Net cash flows from operating activities	2,821	2,444	3,083	3,307	3,418
Net cash flows from investments in non-financial assets					
Sales of non-financial assets	276	248	194	195	107
Purchases of non-financial assets	(3,640)	(3,573)	(3,902)	(3,917)	(3,760)
Net cash flows from investments in non-financial assets	(3,364)	(3,325)	(3,708)	(3,722)	(3,653)
Net cash flows from investments in financial assets for policy purposes	(27)	(7)	(51)	(15)	(19)
Net cash flows from investments in financial assets for liquidity purposes	22	227	(3)	16	(68)
Net cash flows from financing activities					
Advances received (net)	(165)	(163)	(26)	(222)	(67)
Borrowing (net)	1,372	1,293	1,421	1,570	1,352
Deposits received (net)	8	...	9	6	4
Distributions Paid	(743)	(674)	(965)	(893)	(1,007)
Other financing (net)	1	(3)	...	1	(1)
Net cash flows from financing activities	473	453	439	462	281
Net increase (decrease) in cash held	(75)	(208)	(240)	48	(41)
SURPLUS / (DEFICIT)					
Net cash from operating activities and investments in non-financial assets	(543)	(881)	(625)	(415)	(235)
Distributions Paid	(743)	(674)	(965)	(893)	(1,007)
Finance leases and similar arrangements	...	...	...	...	...
SURPLUS / (DEFICIT)	(1,286)	(1,555)	(1,590)	(1,308)	(1,242)

Notes:

(a) A positive number denotes a cash inflow, a negative (i.e. bracketed) sign denotes a cash outflow.

Table A-9: NSW Non-financial Public Sector Cash Flow Statement^(a) (ABS Basis)

CASH FLOW	Budget	Revised	Forward Estimates		
	2003-04	2003-04	2004-05	2005-06	2006-07
	\$m	\$m	\$m	\$m	\$m
Cash receipts from operating activities					
Taxes received	13,530	14,299	14,469	15,315	16,211
Receipts from sales of goods and services	12,724	13,241	14,227	14,997	15,593
Grants/subsidies received	17,230	17,539	17,998	18,686	18,991
Other receipts	5,000	4,956	4,961	5,169	5,402
Total receipts	48,484	50,035	51,655	54,167	56,197
Cash payments for operating activities					
Payment for goods and services	(32,721)	(34,515)	(35,800)	(37,173)	(38,849)
Grants and subsidies paid	(5,223)	(5,252)	(5,218)	(5,331)	(5,465)
Interest paid	(1,711)	(1,707)	(1,552)	(1,823)	(1,679)
Other payments	(3,012)	(2,880)	(2,785)	(3,029)	(3,130)
Total payments	(42,667)	(44,354)	(45,355)	(47,356)	(49,123)
Net cash flows from operating activities	5,817	5,681	6,300	6,811	7,074
Net cash flows from investments in non-financial assets					
Sales of non-financial assets	961	894	697	497	374
Purchases of non-financial assets	(6,791)	(6,600)	(6,901)	(6,932)	(6,669)
Net cash flows from investments in non-financial assets	(5,830)	(5,706)	(6,204)	(6,435)	(6,295)
Net cash flows from investments in financial assets for policy purposes	(3)	(72)	(328)	(35)	(19)
Net cash flows from investments in financial assets for liquidity purposes	(1,276)	(789)	(1,194)	(1,612)	(1,794)
Net cash flows from financing activities					
Advances received (net)	(95)	(130)	(59)	(158)	(62)
Borrowing (net)	1,067	854	1,257	1,286	1,147
Deposits received (net)	6	1	8	5	3
Distributions Paid	...	...	...	...	...
Other financing (net)	...	(3)	...	1	...
Net cash flows from financing activities	978	722	1,206	1,134	1,088
Net increase (decrease) in cash held	(314)	(164)	(220)	(137)	54
SURPLUS / (DEFICIT)					
Net cash from operating activities and investments in non-financial assets	(13)	(25)	96	376	779
Distributions Paid	...	...	...	...	...
Finance leases and similar arrangements	(347)	(340)	(240)	(147)	(117)
SURPLUS / (DEFICIT)	(360)	(365)	(144)	229	662
<i>Notes:</i>					
(a) A positive number denotes a cash inflow, a negative (i.e. bracketed) sign denotes a cash outflow.					
(b) Deposits by the Crown to the Liability Management Fund and the fund's earnings have been set aside to meet future superannuation contributions.					
GFS SURPLUS/ (DEFICIT)	(360)	(365)	(144)	229	662
Impact of deposits to the Liability Management Fund ^(b)	(847)	(857)	(1,413)	(1,250)	(1,469)
UNDERLYING CASH SURPLUS/(DEFICIT)	(1,207)	(1,222)	(1,557)	(1,021)	(807)

LOAN COUNCIL REPORTING REQUIREMENTS

Table A-10 presents the Budget time estimates of the State's Loan Council Allocation (LCA) for 2003-04 and a revised estimate taking into account fiscal and economic developments since the commencement of the budget year.

As confirmed at the 1997 Loan Council meeting, States are to report their full contingent exposure to infrastructure projects with private sector involvement. Exposure is to be measured by the Government's termination liabilities and disclosed as a footnote to, rather than a component, of LCAs.

Overall, the positive Loan Council Allocation requirement of \$1,306 million for New South Wales for 2003-04 has been revised to positive \$788 million. The movement in the LCA results from an improved position on superannuation.

Table A-10: 2003-04 Loan Council Allocation Estimates for NSW

	<i>Budget-time Estimate 2003-04 \$m</i>	<i>Loan Council Revised Estimate 2003-04 \$m</i>
General government sector cash deficit / (surplus)	(925)	(1,191)
PNFC sector cash deficit / (surplus)	1,286	1,555
Non-financial public sector cash deficit / (surplus) ^(a)	360	365
Minus Net cash flows from investments in financial assets for policy purposes ^(b)	3	72
Plus Memorandum items ^(c)	943	351
Loan Council Allocation	1,306	788

Notes:

- (a) Does not directly equate to the sum of the General Government and PNFC cash deficits due to intersectoral transfers which are netted out.
- (b) This item is the negative of net advances paid under a cash accounting framework
- (c) Memorandum items are used to adjust the ABS deficit to include in LCAs certain transactions – such as operating leases that have many of the characteristics of public sector borrowings but do not constitute formal borrowings. They are also used, where appropriate, to deduct from the ABS deficit certain transactions that Loan Council has agreed should not be included in LCAs – for example, the funding of more than employers' emerging costs under public sector superannuation schemes, or borrowings by entities such as statutory marketing authorities.

PRIVATE SECTOR INFRASTRUCTURE

CONTRACTS TO BE ENTERED INTO IN 2003 – 2004

LANE COVE TUNNEL

Project Description

The Lane Cove Tunnel will link the M2 Motorway at East Ryde and the Gore Hill Freeway at Artarmon. The proposed 3.4 kilometre twin tunnels have been designed to run under Epping Road as much as practical.

The Project also includes:

- modification to Epping Road / Longueville Road to provide bus lanes in each direction, additional right turn lanes, a continuous bicycle path from Wicks Road, Ryde to Naremburn, and other improvement to the Urban environment;
- an extra westbound lane on Epping Road from Lane Cove River to Wicks Road;
- widening the Gore Hill Freeway to include a transit lane in each direction between the Pacific Highway and Warringah Freeway; and.
- adding new north facing ramps between Falcon Street and the Warringah Freeway to provide access between the Warringah Freeway and Falcon Street/Military Road.

The Lane Cove Tunnel Consortium (sponsored by Thiess Pty Ltd, Transfield Pty Ltd and ABN AMRO Australia Limited) was selected to undertake the project in October 2003. The project reached financial close in December 2003, and construction is expected to commence in early 2004. The Consortium's estimated total construction cost is \$1.1 billion. The project is to be funded by toll revenue.

Government Contingent Liability

Nil

ROYAL PRINCE ALFRED HOSPITAL CAR PARK

Project Description

Detailed proposals have been submitted by the private sector to finance and build a new 1,000 space car park on the Royal Prince Alfred Hospital campus. The total construction cost for the project is estimated to be \$13.5 million. The successful proponent will, under a 20 or 25 year licence, operate and collect user charges from around 1,300 campus car park spaces, including the 1,000 new spaces.

The form of the arrangement is expected to be similar to that for the Randwick and St George Hospital Car Parks. The expected contract execution date is August 2003. At this time no government liability is anticipated based on the termination provisions of the draft contract.

Government Contingent Liability

To Be Determined

APPENDIX B: GUIDE TO THE 2003-04 HALF-YEARLY BUDGET REVIEW

The 2003-04 Half-Yearly Budget Review reports on the current and projected financial performance of the NSW General Government Sector. The General Government Sector covers all agencies that are generally engaged in the production of goods and services outside the normal market mechanisms.

In practice, this means that entities which operate outside normal market mechanisms (eg Audit Office of New South Wales) and self funded regulatory agencies (eg the WorkCover Authority and the Motor Accidents Authority) are included, as well as agencies which receive an appropriation in the Annual Appropriation Act (eg the Department of Health and the Department and the Department of Education and Training).

The *Public Finance and Audit Act 1983* requires the Treasurer to publicly release a statement by December each year containing:

- The latest economic projections for the current financial year and an explanation of any significant variation from the budget time projections contained in the Budget Papers; and
- Budget projections for the current financial year and an explanation of any significant variation in major aggregates from those budget time projections.

The NSW Budget is compiled in accordance with the Government Finance Statistics (GFS) standards.

The Half-Yearly Budget Review for 2003-04 meets this legislative requirement, incorporates the financial statements for the General Government Sector for October 2003 and meets the requirements for uniform reporting of State finances agreed to by the Loan Council.

The Review provides:

- The actual financial performance of the General Government Sector for the four months ended 31 October 2003.
- The projected results for 2003-04 compared with the June 2003 budget estimates; and
- The latest projection of the financial performance for the three subsequent years to 2006-07.

The revised forward estimates, like the original estimates, are predicated on a number of assumptions. The key assumption is the continuation of current policies. Thus, the forward estimates are based on existing policies and should not be regarded as forecasts for the budget outcomes in future years, as these outcomes will reflect future Government policy.

For the capital works program, it is assumed in the forward estimates that the size of the discretionary program including works in progress will be constant in real per capita terms. This means that the forward estimates contain an allowance for new works that has not yet been allocated to specific projects.