A plan for budget repair

Interim report –

an independent assessment of the Northern Territory's fiscal position and medium-term outlook

December 2018

Contents

1 | Fiscal position and outlook

Key points

- Over the past 20 years the Territory has incurred fiscal deficits not only during contractions in the economic cycle but also in times of expansion. This practice has complicated the budget and debt management task in the current economic downturn.
- The deterioration in the Territory's operating balance from 2016-17, following reduced GST revenues, has placed the Territory in the unsustainable position of needing to borrow to pay for recurrent activities, including interest expenses.
- At the time of the 2018 Budget, the outcome for the Territory of the Productivity Commission inquiry into horizontal fiscal equalisation was unknown.
- Following the passage of the Commonwealth's *Treasury Laws Amendment (Making Sure Every State and Territory Gets Their Fair Share of GST) Act* in November 2018, there is now greater certainty that the Territory GST revenue share will remain below historic trends over the medium term.
- Since the 2016 Pre-Election Fiscal Outlook (PEFO), in recognition of its deteriorating fiscal position, the Territory Government has progressed budget improvement measures totalling around $830 million to reduce expenditure growth.
- However, due to the Territory Government's efforts to support employment and population growth in response to moderating economic conditions, new policy decisions (for example, Royal Commission response) and ongoing demand pressures (for example, health services), the budget improvement measures have been insufficient to stem expenditure growth.
- The relative disadvantage and isolation of the Territory's population, particularly in remote areas, mean that the cost of providing, and demand for, government services is significantly higher per person compared to other jurisdictions. Despite the reduction in the Territory's GST revenues, these needs have not changed.

The Territory budget

Sociodemographic and economic context

The Territory Government delivers services to a small and relatively dispersed population across a large land mass. The inherent diseconomies of scale and relative disadvantage and isolation of the Territory's population, particularly in remote areas, mean that the cost of providing, and demand for, government services is significantly higher, especially on a per person basis compared to other jurisdictions. These expenditure challenges are relatively constant and do not fluctuate with economic conditions or funding cycles.

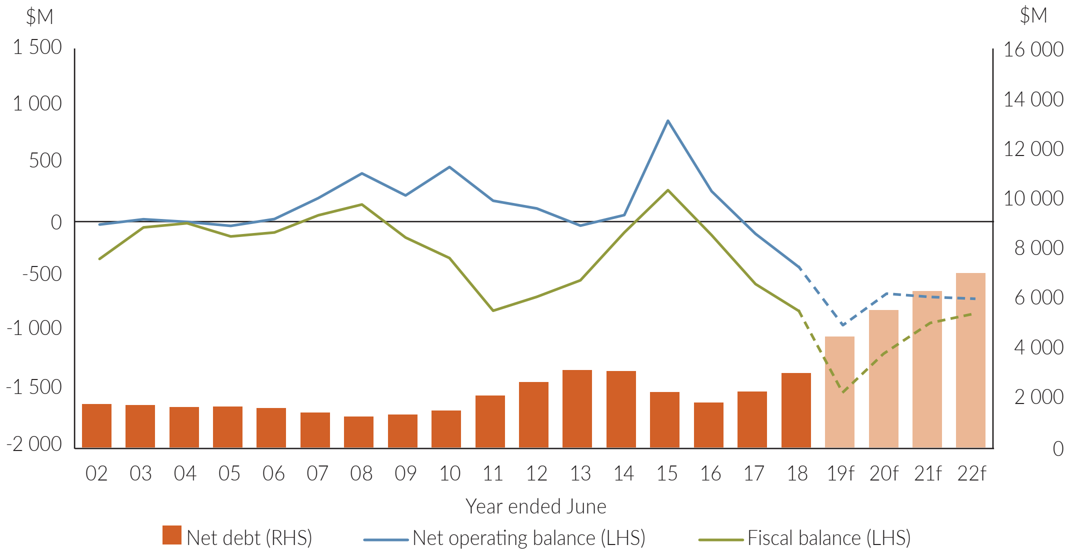
The Territory's economy is small and quite variable in economic growth rates, with business cycles and population growth driven by the timing of major projects. This makes long-term infrastructure planning challenging and drives an approach to infrastructure investment that focuses on countering fluctuations in the economic cycles rather than long-term sustainability. The Territory's own-source revenues mirror the economy in relative size and volatility, which coupled with high service demand and cost, leads to a reliance on Commonwealth revenues.

Budget performance

Over the past 20 years, the Territory has incurred deficits not only during contractions in the economic cycle but also in better times. Chart 1 shows that while the Territory averaged an operating balance (revenue less recurrent expenditure) surplus of around $140 million per annum between 2001-02 and 2017-18, the average fiscal balance (revenue less recurrent and capital expenditure) was a deficit of around $240 million per annum[1].

This means that while the Territory was sustainably financing its recurrent activities, capital expenditure was, on average, funded through borrowing[2]. This was particularly pronounced following a lull in major projects around 2009-10, prior to the commencement of the Ichthys LNG project, when the Territory Government undertook a range of stimulatory infrastructure projects. The net result was an increase in the Territory's net debt from around $1.7 billion to around $3 billion over the period.

Chart 1: Key fiscal aggregates – non financial public sector



Source: Department of Treasury and Finance, 2018 Mid-Year Report.

The deterioration in the Territory's operating balance from 2016-17, following reductions in GST revenue, has placed the Territory in the unsustainable position of needing to borrow to pay for recurrent activities and interest expenses.

Persistent operating deficits, compounded by further borrowing to fund capital expenditure, will result in a rapid escalation in government debt if left unchecked.

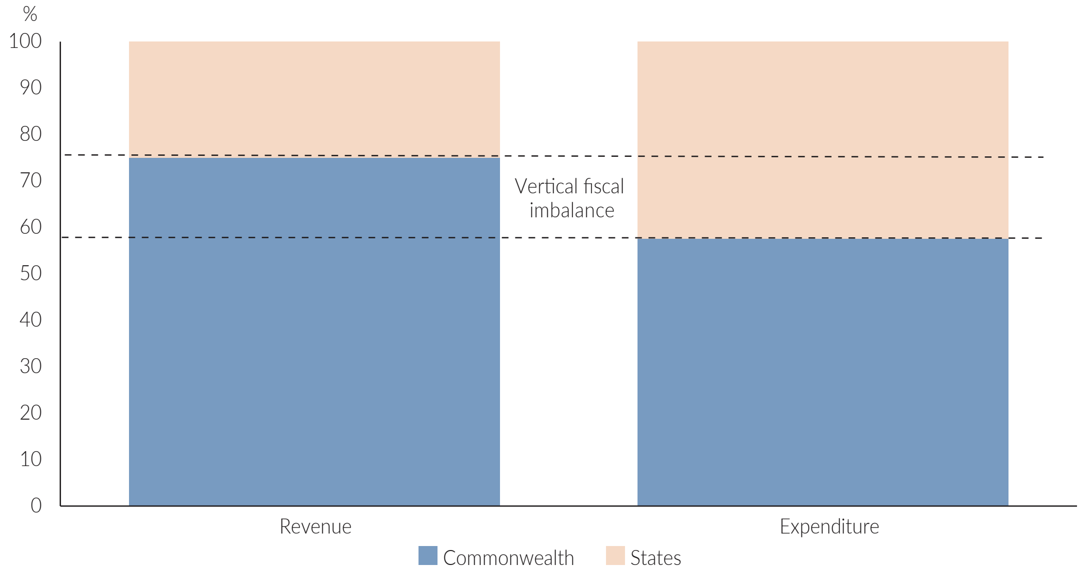
1 Government's financial performance is commonly measured at the general government level, which captures the bulk of services delivered by government. However, the general government sector excludes revenue and expenditure associated with public non financial corporations such as Power and Water Corporation, Jacana Energy and Territory Generation, which are intended to operate on a commercial basis but are not yet on that footing. Due to the aggregate fiscal drag of these entities on the Territory Budget, the Territory focuses on fiscal outcomes at the non financial public sector level to ensure a comprehensive assessment of the Territory's financial performance in its reporting.

2 Borrowing to fund infrastructure can be fiscally and economically prudent in circumstances where the assets deliver long-term economic returns to the Territory in excess of financing costs.

Revenue

A feature of the Australian federation is that the Commonwealth Government raises revenues in excess of its expenditure responsibilities, while state and territory governments have insufficient own-source revenues to fund their expenditure responsibilities. This reflects responsibilities established in the Australian Constitution, is common to many federal systems, and is referred to as vertical fiscal imbalance (Chart 2).

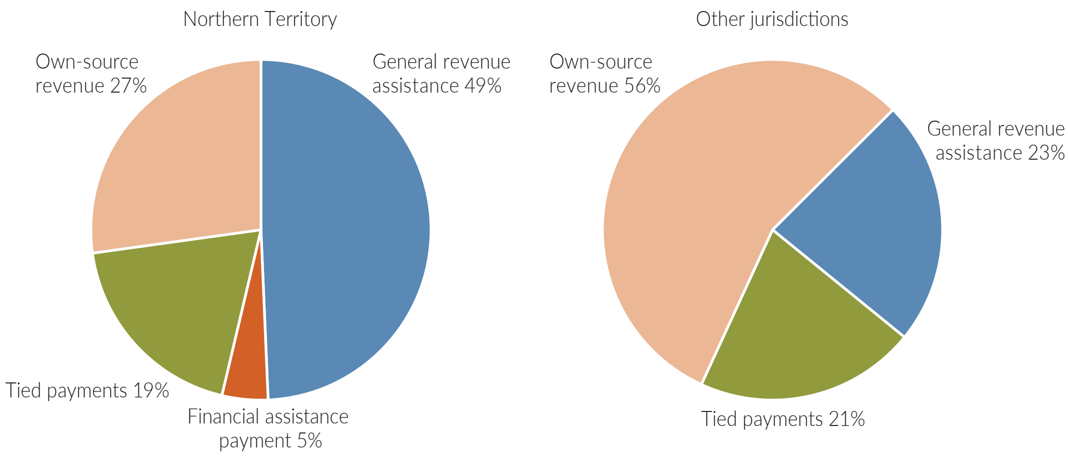
Chart 2: Comparison of Commonwealth and states' total expenditure and revenues, 2016-17



Source: Commonwealth 2016-17 Final Budget Outcome; state and territory 2016-17 annual financial reports.

The Commonwealth Government provides funding to states and territories to address the imbalance through a range of tied and untied funding arrangements. Due to its demographic and geographic characteristics, the Territory has the most acute imbalance of the states and territories, which is reflected in the Territory Government's above average reliance on Commonwealth revenues (Chart 3).

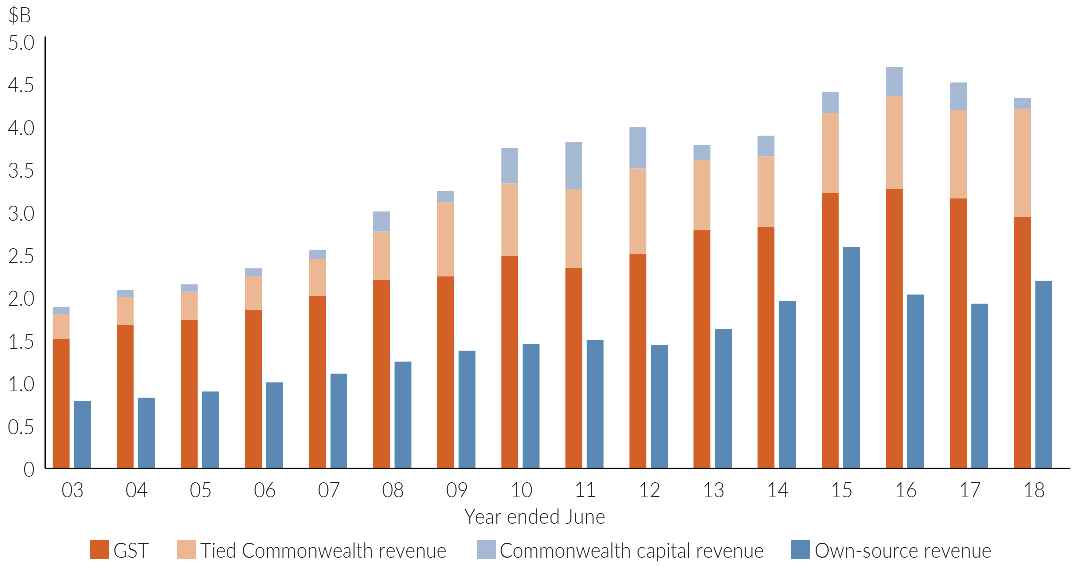
Chart 3: Sources of revenue, 2017-18



Source: Australian Bureau of Statistics, Government Finance Statistics.

Since 2002-03, the Territory has experienced solid revenue growth, with compound annual growth averaging 5.9 per cent. However, the growth is marked by two distinct periods: pre global financial crisis (GFC) (average annual growth of 8.5 per cent); and post GFC (average annual growth of 4.4 per cent) (Chart 4).

Chart 4: Commonwealth and own-source revenue, 2002-03 to 2017-18



Pre global financial crisis

Between 2002-03 and 2007-08, Commonwealth revenues, especially GST revenues, grew rapidly supported by a mining led economic boom at the national level, with escalating wages underpinning strong consumption and growth in GST collections.

GST revenues grew by an annual average of 8.8 per cent[3], mainly driven by growth in national GST collections of around 8.2 per cent per annum, and modest increases in the Territory's relative population share and relativity[4]. Tied Commonwealth revenue also grew strongly due to increased payments in the areas of health, education, housing and community amenities, and social security and welfare, reflecting the strength of the Commonwealth budget.

Locally, own-source revenues were supported by economic and population growth associated with major projects such as the Darwin LNG plant and Alcan G3 refinery expansion, and significant increases in commodity prices throughout the mining boom.

Post global financial crisis

Between 2007-08 and 2017-18, average annual GST revenue growth moderated to 2.9 per cent, mainly reflecting slower growth in national GST collections (4.1 per cent) due to the impact of softening global economic conditions and a national shift in consumption patterns towards items that do not incur GST, and a decline in the Territory's GST relativity from around 5.10 in 2007-08 to 4.66 in 2017-18[5]. The Territory's GST relativity subsequently fell to 4.26 in 2018-19, a historic low.

3 GST growth is measured from its inception on 1 July 2001. Other revenues are measured from 2002-03 due to data limitations.

4 GST revenue is determined on a weighted per capita share of national GST collections basis. The per capita weighting is referred to as a relativity (that is, need relative to equal per capita). The Territory has historically averaged a relativity of around 5.1, meaning it has historically received around 5.1 times an equal per capita share of national GST collections.

5 The impact of a ±1 per cent variation in the Territory's GST relativity is around ±$26 million per annum. A ±1 per cent variation in the Territory's GST relativity in each year of the forward estimates period would have a cumulative effect of around ±$112 million.

The average annual growth in Commonwealth tied revenue remained strong post GFC, supported by new health and education national agreements. The Northern Territory Emergency Response (NTER) (the Intervention) also provided significant funding to the Territory through the 2007-12 NTER package, 2012-13 National Partnership Agreement on Stronger Futures in the Northern Territory (SFNT) and the current 2015-16 National Partnership Agreement on Northern Territory Remote Aboriginal Investment (NTRAI).

Own-source revenue growth moderated from 9.6 per cent to 5.8 per cent as commodity price falls slowed royalty income growth, employment growth related to major projects began to slow, impacting payroll tax and stamp duty revenues, and gambling tax growth tapered as the market for sports betting matured, competition increased (particularly online) and legislative changes impacted gaming machine numbers and patronage (indoor smoking reforms).

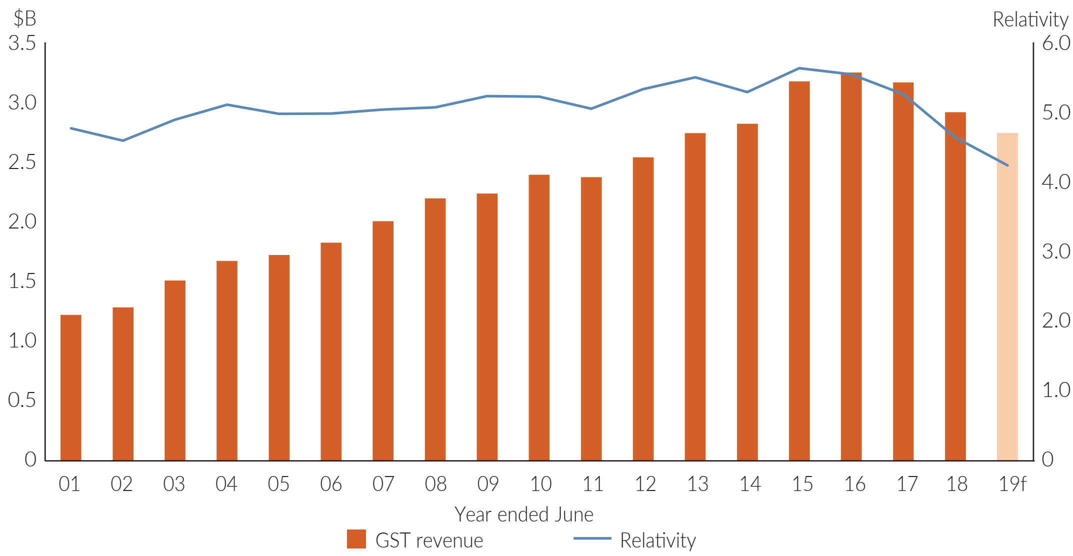
Own source government revenues were significantly boosted in 2014-15 and 2015-16 through asset sales including $424 million for the Territory Insurance Office and $506 million for the long-term lease of the Port of Darwin. These one-off revenues were predominantly used to fund a range of infrastructure stimulus and investment initiatives during a relatively strong period of economic growth. A small proportion of total sale proceeds was used to retire debt (around $75 million).

2016 Pre-Election Fiscal Outlook (PEFO)

At the time of the 2016 PEFO, GST revenue growth over the forward estimates was forecast to average around 3.2 per cent per annum, broadly consistent with its post GFC growth path. Further moderation in own-source revenue was forecast as the local economy was expected to adjust when the Ichthys LNG project, one of the largest of its kind in the world, transitioned from the construction to the production phase.

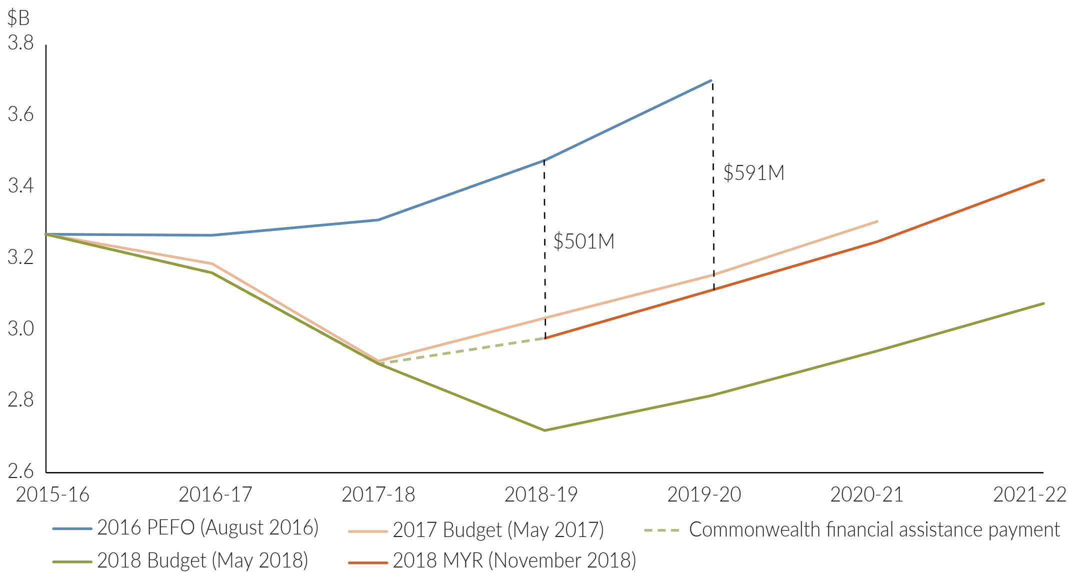
The 2016 PEFO forecasts, while moderately conservative from a historical perspective, did not factor in the substantial reductions in GST revenue, equating to around $3.4 billion over the budget cycle to 2021-22, subsequently experienced by the Territory.

Chart 5: Territory GST revenues and annual relativities



These reductions were somewhat offset by a $260 million financial assistance payment from the Commonwealth for 2018-19, with a further Commonwealth guarantee regarding the Territory's GST relativity for the next three years set out in its response to the Productivity Commission's Inquiry into Horizontal Fiscal Equalisation (HFE)[6]. This reduced the impact of the GST reductions from $3.4 billion to $2.4 billion (Chart 6), still in excess of $500 million per annum.

Chart 6: GST Revenue changes since the 2016 Pre-Election Fiscal Outlook



The reduction in GST revenue since 2016 PEFO was mainly driven by declining GST relativities, which in 2018-19 fell to the lowest recorded since the introduction of the GST. The decline was due to factors outside of the Territory's control, including a shift in the expenditure patterns of the more populous states towards urban service delivery[7], and an increase in the Territory's share of tied Commonwealth payments that offset the Territory's assessed expenditure need. Nonetheless, the requirement for the Territory Government to deliver essential services and infrastructure remained unchanged.

While higher than expected own-source revenues, predominantly mining royalties and payroll tax, have slightly offset the GST reductions since the 2016 PEFO, the Territory's total revenue growth is nonetheless expected to average just 1.7 per cent per annum between 2018-19 and 2021-22, well below the long-term average of 5.9 per cent and the post GFC average of 4.4 per cent. This reduction in revenue has been the dominant cause of the deterioration in the Territory's fiscal position since the 2016 PEFO and it has become evident that revenue growth rates will not return to pre GFC levels in the foreseeable future.

6 In November 2018, the Commonwealth passed the *Treasury Laws Amendment (Making Sure Every State and Territory Gets Their Fair Share of GST) Act*, which provides the Territory with short-term funding to guarantee a minimum GST relativity of 4.66024 between 2019-20 and 2021-22. While the guarantee temporarily reduces the Territory's GST relativity risk until 2021-22, it nevertheless does not restore the Territory's share of GST revenue to historical levels. Further, the risk beyond this period is significant given the GST distribution system will move away from full equalisation to a form of partial equalisation and there is currently no guarantee of a relativity floor for the Territory beyond 2021-22.

7 The Commonwealth Grants Commission assesses expenditure needs based on the average expenditure patterns of all states, which are driven predominantly by the more populous jurisdictions. In recent years, per capita expenditure growth at the national level for urban based services (for example, urban transport) for which the Territory has relatively low needs has outpaced expenditure on remote based services (for example, rural roads, community health and remote schools) for which the Territory has relatively high needs. As a result, the Commonwealth Grants Commission has assessed that the Territory needs a lower share of GST revenue to deliver the average level of services in the Territory.

Over the longer term, a key challenge for the Territory will be redressing its acute reliance on Commonwealth funding through growing the Territory economy to increase its own-source revenue base. While the Territory Government has recently undertaken a review of its taxes and royalties following the release of the Northern Territory Revenue Discussion Paper, the Territory's own-source revenue raising effort remains below the national average (Table 1). Increasing the revenue-raising effort to the national average would require the Territory to raise around $100 million in additional own-source revenues per annum.

Table 1: Revenue Raising Effort, 2016-17

NSW	Vic	Qld	WA	SA	Tas	ACT	NT
97.8%	96.6%	103.6%	101.0%	102.9%	87.9%	153.6%	91.8%

Source: Commonwealth Grants Commission 2018 Report.

Notwithstanding, in the short to medium term, movements in Commonwealth funding, mainly GST revenue, will continue to dominate the Territory's fiscal outcomes and as such it will be important that the Territory secures a share of untied Commonwealth funding that is more commensurate with historical levels.

Tied Commonwealth revenue

Changes in tied Commonwealth funding, while generally having no direct net impact on fiscal outcomes (the revenue being offset by expenditure) can have a range of indirect consequences particularly over the medium to long term. For example, community expectations can be raised through the establishment or expansion of services without a Commonwealth commitment to ongoing funding, with the Territory Government funding subsequently required to continue the service when Commonwealth priorities shift.

In recent years, onerous co-contribution, reporting and maintenance of effort requirements have increasingly become a feature of Commonwealth funding support. These requirements tie up a growing proportion of state and territory budgets resulting in reduced budget autonomy and state sovereignty. Examples include, the National Housing and Homelessness Agreement (NHHA) and National Schools Reform Agreement (Quality Schools package).

Under the NHHA, the Territory is required to match contributions for homelessness services and is subject to performance reporting on areas outside the Territory Government's control. The Quality Schools package imposes onerous contribution and maintenance of effort targets on states and territories, including annual indexation requirements well in excess of inflation that severely constrains the Territory's ability to implement fiscal repair.

Northern Territory Emergency Response and Closing the Gap in the Northern Territory

The Territory has traditionally received substantial support from the Commonwealth to assist in addressing Indigenous disadvantage, which is not recognised through the GST distribution model. On 21 June 2007, the Commonwealth announced the Northern Territory Emergency Response (NTER), with broad measures to protect Aboriginal children in the Territory from sexual abuse and family violence. The NTER package and the Closing the Gap in the Northern Territory National Partnership Agreement were estimated to provide $2.1 billion over five years, from 2007-08.[8]

8 Northern Territory Emergency Response Evaluation Report 2011, http://www.territorystories.nt.gov.au/jspui/bitstream/10070/252540/1/NTER%20evaluation%20report%202011.PDF, p. 74.

After an evaluation of the NTER package and nearing expiry of the legislative basis for the Intervention, a 10-year package of initiatives was announced to replace the NTER. The resulting Stronger Futures in the Northern Territory (SFNT) package was introduced, providing an estimated $3.45 billion over 10 years from 2012-13[9] to expiry in 2022-23, aimed at improving outcomes for Aboriginal people in the Territory, including closing the gap on Indigenous disadvantage.

SFNT incorporated provisions for a review of the Territory's fiscal capacity to support the progressive transfer of fiscal responsibility of services delivered under the agreement every two years. No transfers were made under the agreement.

In 2014, the Territory entered into negotiations to vary the Implementation Plans (IPs) under SFNT, to better meet its objectives. Subsequently, a new, more streamlined agreement, Northern Territory Remote Aboriginal Investment (NTRAI), was announced in the Commonwealth's 2015-16 Budget, effectively replacing SFNT and incorporating more realistic and achievable milestones, with an outcomes focus.

NTRAI is expected to provide around $987 million to the Territory, excluding non-government school payments, between 2015-16 and 2021-22. As shown below, the funding over the life of the agreement follows a similar path as SFNT, with a downward taper in the later years reflecting the Commonwealth's expectation that responsibility for funding these services will progressively transition to the Territory[10].

Table 2: Estimated financial contributions under SFNT and NTRAI, year ended 30 June

	2012[1]	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
	$M	$M	$M	$M	$M	$M	$M	$M	$M	$M	$M
SFNT (original)	26.9	98.7	197.1	180.1	182.3	171.4	166.6	109.0	101.2	97.3	98.2
NTRAI (new)					330.8[2]	160.7	153.6	94.5	85.6	80.3	80.6

1 An in-advance payment made in 2011-12 for services to be delivered in 2012-13.
2 Funding in 2015-16 included a payment of $154.8 million for the Northern Territory to assume responsibility for the provision of municipal and essential services.

The funding provided under SFNT and continuing under NTRAI supplements service delivery to Aboriginal people living in remote areas of the Territory, including health, education, community safety and housing, which the Territory Government would not otherwise be able to provide.

In recent years the Commonwealth has also provided substantial funding to the Territory to help address remote Indigenous overcrowding, homelessness and poor housing conditions through several agreements, including the National Partnerships on Aboriginal Remote Indigenous Housing (NPARIH) (2009-16) and Remote Housing (NPRH) (2016-18). This funding is critical to ensuring Indigenous disadvantage can continue to be addressed. While the Commonwealth's 2018 Budget announced a new NPA on Remote Housing to provide funding from 2018-19, totalling $550 million over five years to complement the Territory Government's $1.1 billion 10-year commitment, there is no formal agreement currently in place.

9 An in-advance payment of $26.9 million was made in 2011-12 for services to be delivered in 2012-13.

10 NTRAI specifies that it is intended to provide Commonwealth funding on a one-off basis to support addressing Indigenous disadvantage and that it is not anticipated the Commonwealth will provide any further funding to the Territory beyond the agreement's expiry.

The level of disadvantage in remote communities is such that the Territory cannot sustain the level of investment required to redress the entrenched disadvantage. Despite a 10-year funding commitment from the Commonwealth, intergenerational investment is necessary before real gains will be evident. Given the severe fiscal challenges facing the Territory, maintaining the Commonwealth's commitment to closing the gap in Indigenous disadvantage will be critical to ensuring progress to date is not lost.

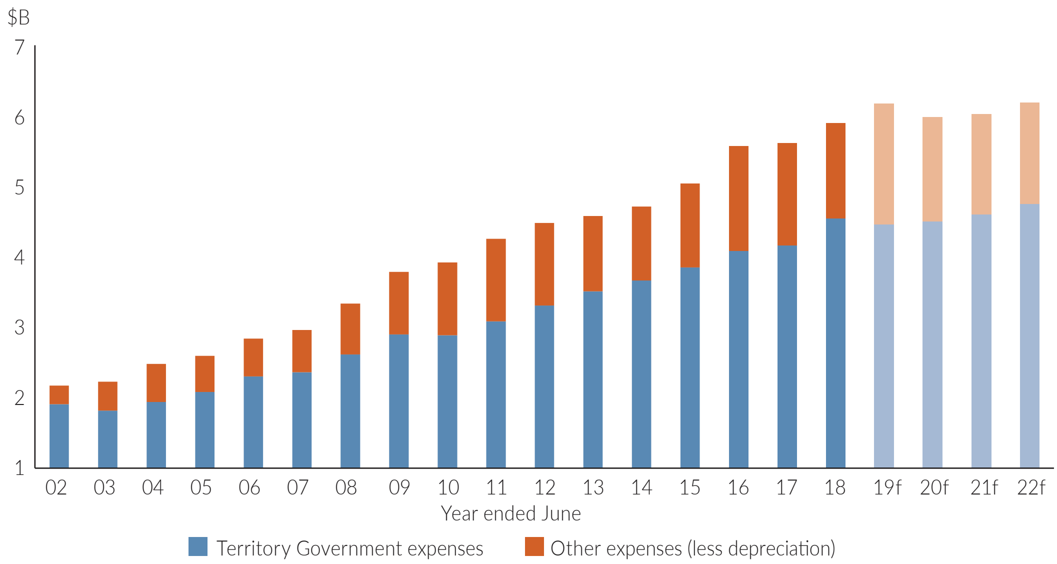
While tied funding targeted at Indigenous disadvantage is required, it is also important that any such funding does not reduce the Territory untied funding as an unintended consequence through the GST relativity calculations. For example, remote Indigenous housing funding was originally excluded from the Commonwealth Grants Commission's (CGC) GST relativity calculations, ensuring that efforts to address the historic lack of housing and reduce overcrowding in remote communities were not undermined by reduced GST revenue to the Territory. However, in 2015 the CGC changed its treatment of these payments so that they now affect the calculations.[11] Under these arrangements, it is estimated that around $205 million in GST has been redistributed away from the Territory to other jurisdictions between 2015-16 and 2018-19, with the level of redistribution to significantly increase in future years.

The Territory has strongly argued to have the Commonwealth's remote Indigenous housing payments excluded from the CGC calculations and the Commonwealth has provided an undertaking that the 2019 Update Terms of Reference will direct the CGC to exclude these payments from GST calculations. However, this undertaking is yet to be confirmed.

Recurrent expenditure

Between 2001-02 and 2017-18, expenditure in the general government sector funded through own source and untied revenues (that is, excluding tied Commonwealth funding) has grown at an average annual rate of around 5.6 per cent. Unlike the Territory's revenue sources, the rate of expenditure growth accelerated slightly post GFC (5.7 per cent compared to 5.4 per cent pre GFC).

Chart 7: Expenditure growth over time[1]



1 Excludes depreciation. Other expenses is primarily tied funding from the Commonwealth.
Source: Department of Treasury and Finance, 2018 Mid-Year Report.

11 In the 2016 Update, the CGC treated 25 per cent of the payments as having no effect.

Table 3 details the areas of recurrent expenditure growth in the Territory since 2001-02, which reflect a combination of demand growth (for example, increased health, child protection and housing services, new schools, a new prison, etc.) and new policy initiatives such as additional police, increased school resourcing, various alcohol reforms (for example, Enough is Enough, Alcohol Mandatory Treatment, Banned Drinker Register, etc.), tourism initiatives, early childhood reform, economic development initiatives (for example, Bringing Forward Discovery, major project support, Northern Australia Development Office, etc.) and the election commitments of various governments over the period.

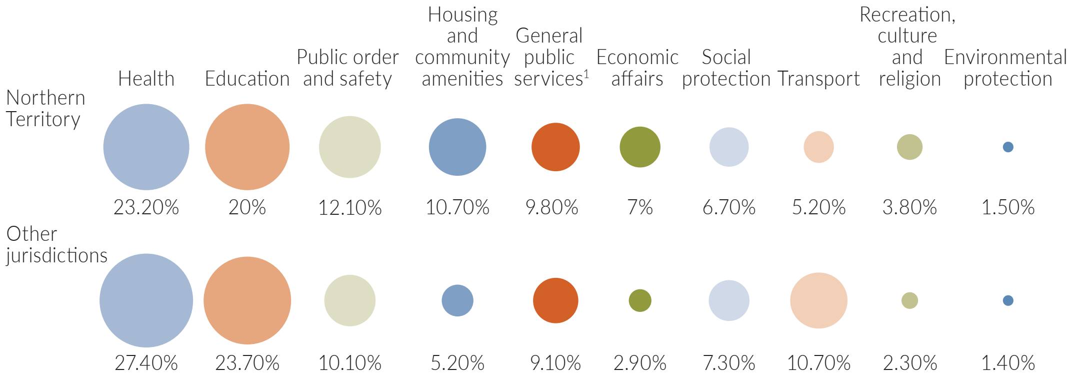
Table 3: General government recurrent expenditure growth rates 2001-02 to 2017-18

Classification	Average annual growth rate
	%
Social protection	15.1
Housing and community amenities	10.3
Health	8.0
Public order and safety	7.5
Transport	7.2
Economic affairs	7.2
Education	5.6
Recreation, culture and religion	4.4
Environmental protection	2.9
General public services	- 0.5

Source: Department of Treasury and Finance.

In 2017-18, the Territory spent around $6 billion, including Commonwealth funding, delivering government services to Territorians. In the Territory, as in other jurisdictions, the largest expenditure categories were health and education, however, the Territory devotes a significantly higher proportion of expenditure towards housing and community amenity than other jurisdictions, mainly due to the socioeconomic and demographic challenges faced by the Territory. Similar trends exist in social protection, and public safety and law and order.

Chart 8: Budget comparison by expenditure function, general government sector

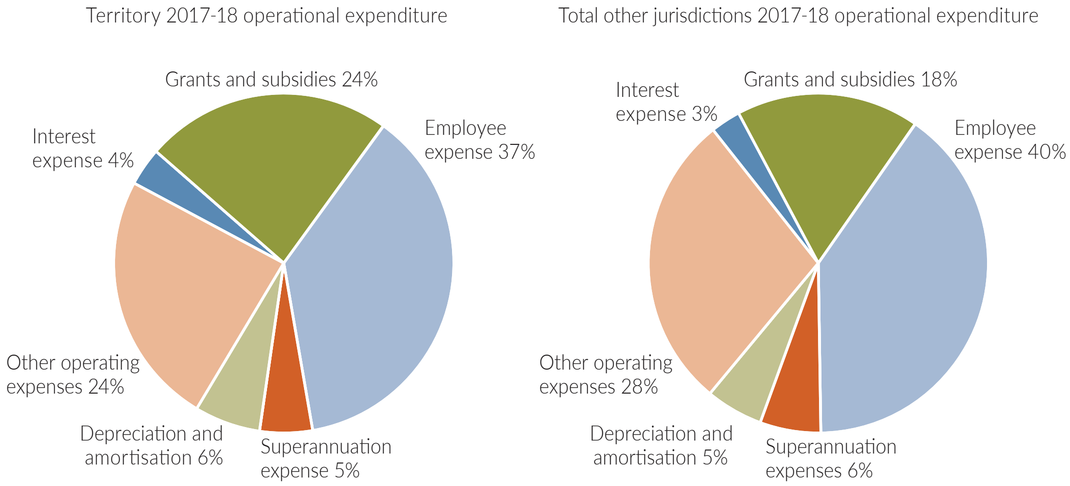


1 General public services includes executive and legislative functions, financial and fiscal affairs, external affairs, foreign economic aid, general services, basic research, research and development on general public services, general public services not elsewhere classified, public debt transactions, and transfers of a general character between different levels of government.

Source: Department of Treasury and Finance; other state and territory governments.

In terms of expense type, the Territory budget is broadly similar in composition to the national average, with around 40 per cent of expenditure related to employee costs. The Territory has a slightly higher proportion of its budget allocated to grants and subsidies, potentially reflecting differences in service delivery arrangements and the impact of stimulus measures in recent years (for example, capital grants).

Chart 9: Budget comparison by expenditure type, general government sector



Source: Australian Bureau of Statistics, Government Finance Statistics.

Government spending per person is significantly higher in the Territory compared to other jurisdictions and the gap has widened in recent years (Chart 10). The main drivers of the widening gap in per capita expenditure have been health and public order and safety (Chart 11).

Chart 10: Per capita expenditure comparison (2007-2017)

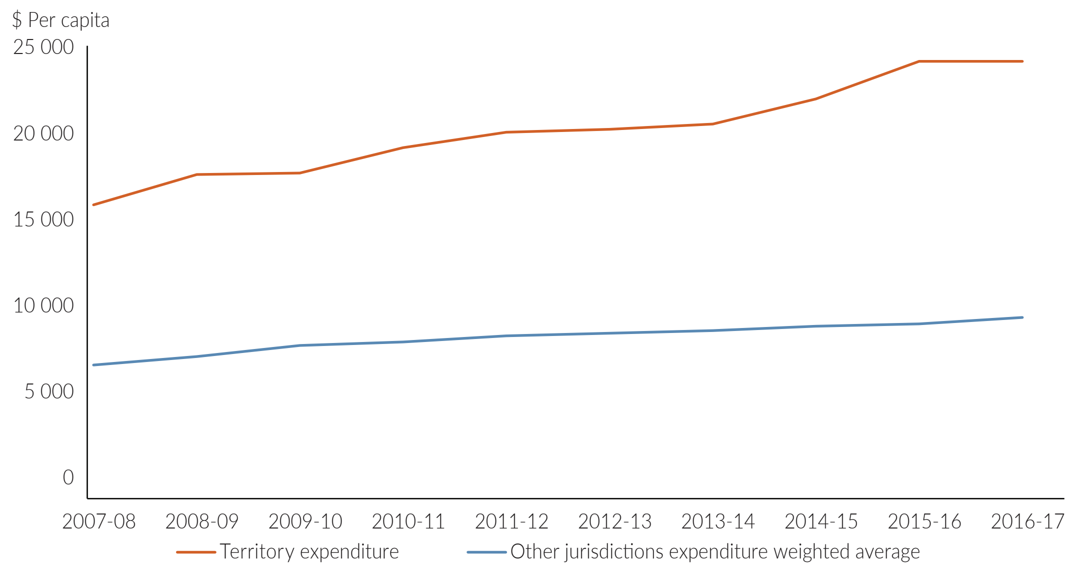
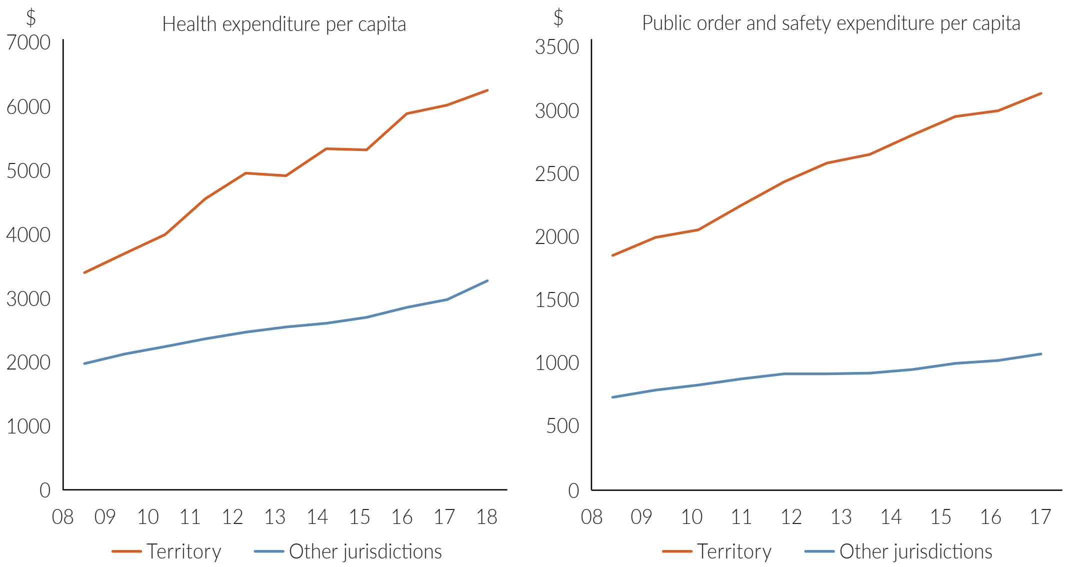


Chart 11: Comparison of expenditure per capita by category over time (2007-2018)



Demand for government services, and community expectations regarding service standards, will continue to increase. The resulting pressure on the Territory budget will be compounded by the need to deliver services to small and remote communities, with complex needs. As a result, making the right investment choices for the Territory's future will require careful consideration of demographic trends.

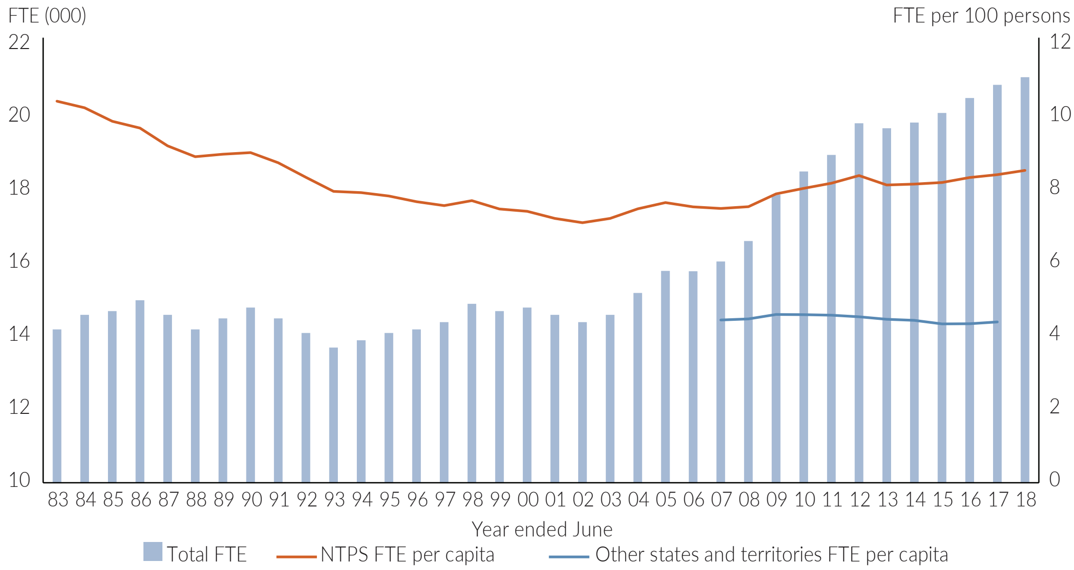
Over the next 30 years the Territory's population is projected to grow by over 30 per cent, with an increasing proportion aged 65 and over. As a result, the Territory Government is likely to face escalating demand pressures for health, community services and housing. These services will need to operate more efficiently to enable service levels to be maintained or improved in a fiscally responsible manner.

Northern Territory Public Sector

As at the October quarter 2018, the Northern Territory Public Sector (NTPS) comprised around 21 453 full-time equivalent staff. While the number of public servants per capita is significantly higher in the Territory compared to the national average, the overall number is relatively small. For example, the total NTPS is less than one third of the size of Queensland's Department of Education and Training.

Between the early 1980s and early 2000s the size of the NTPS remained relatively static. However, following the introduction of the GST in 2000-01, commencement of the Commonwealth's Northern Territory Emergency Response in 2007, and strong population growth associated with a number of major projects across the Territory, NTPS numbers rose rapidly and have remained at elevated levels.

Chart 12: Staffing over time (annual average)

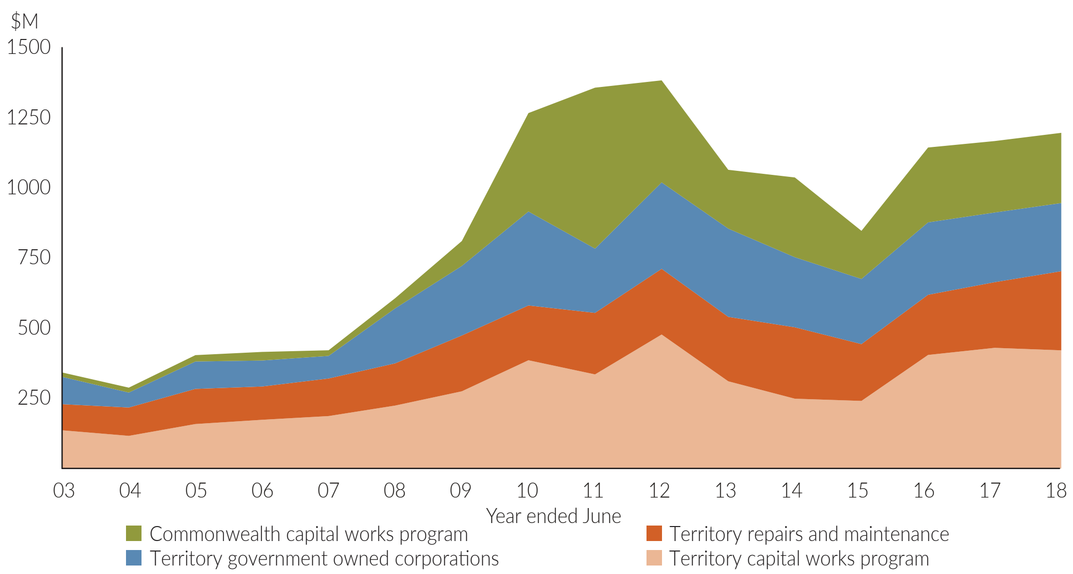


A key pillar of any budget repair will be ensuring that NTPS growth is limited to population growth over the medium term. Achieving this while managing increasing community expectations for better services will require shifting the mindset of the public sector towards a single enterprise focus to improve productivity, minimise duplication and provide a more agile service.

Infrastructure expenditure

The Territory's infrastructure expenditure[12] has averaged around $860 million per annum since 2002-03, funded primarily by the Territory Government (54 per cent), with government owned corporations contributing 24 per cent and the Commonwealth contributing around 22 per cent (Chart 13).

Chart 13: Infrastructure investment over time



12 Includes capital works, minor new works and repairs and maintenance expenditure but excludes capital grants and infrastructure related expenses.

In more recent years there has been a step up in the annual program. This has reflected in the main the Commonwealth's contribution to Territory infrastructure, which increased significantly following the GFC. The Commonwealth's proportion of total expenditure increased from around 11 per cent in 2008-09, peaking at around 42 per cent in 2010-11. The increase mainly reflected the Commonwealth's Strategic Indigenous Housing and Infrastructure Program and the Nation Building and Jobs Plan.

As these programs reached completion in 2012-13, the Commonwealth's contribution reduced, with its share of total infrastructure investment tapering down to around 21 per cent where it has remained relatively static. Territory funded infrastructure also reduced as the Territory experienced record levels of private investment associated with the Ichthys LNG project, but remained above long-term average levels.

From 2015-16, as private sector investment began to moderate from its peak, the Territory Government significantly increased its investment, returning infrastructure expenditure to near record levels through a number of stimulus programs, including:

- Building the Territory ($126 million over three years from 2015-16), funded by proceeds from the sale of TIO
- Boosting our Economy ($98 million over three years from 2015-16), funded by proceeds from the long-term lease of the Port of Darwin
- economic stimulus package ($236 million in 2017-18), partially funded by proceeds from the long-term lease of the Port of Darwin
- Turbocharging Tourism (capital elements) and shovel-ready stimulus programs ($181 million over three years from 2017-18).

Given the Territory's fiscal position, infrastructure investment will continue to be fully funded by borrowing over the forward estimates. As such, it is crucial that this investment is targeted towards infrastructure that provides long-term economic returns to the Territory.

While governments commonly seek to stimulate their economies in times of reduced economic growth, such investments generally represent a small fraction of annual GSP and the impact on net debt levels of sustaining investment at stimulatory levels for extended periods can become burdensome. Stimulating private investment is more effective in generating growth and employment, and is vital to sustainably growing the Territory economy.

The level of Commonwealth funding for infrastructure purposes also needs to be reviewed. Notwithstanding the Commonwealth's initiatives noted above and the investments it makes for defence purposes, the absolute amount of Commonwealth investment in the Territory remains small by comparison with other jurisdictions. Its investments through the Northern Australia Infrastructure Facility (NAIF) remain small and further opportunities need to be pursued.

Government owned corporations

The Territory has three government owned corporations, Power and Water Corporation (PWC), Territory Generation (T-Gen) and Jacana Energy (Jacana). PWC is responsible for providing monopoly type services including electricity networks and system control, water services and Indigenous Essential Services. T-Gen is responsible for electricity generation in urban and regional areas and Jacana is responsible for retailing electricity in the same markets.

The government owned corporations are established by government to deliver services in markets where government participation is deemed necessary to address instances of market failure, including natural monopolies and the provision of strategic infrastructure, goods and services.

The key objective of the government owned corporations is to operate a government business at least as efficiently as any comparable business and provide sustainable returns to the Territory on its investment in the business. To date, returns to the Territory from the government owned corporations have been modest.

In 2014, a reform agenda focusing on the utilities market commenced including: the structural separation of PWC (into the three government owned corporations), phased adoption of relevant aspects of the National Electricity Rules, and introduction of an interim wholesale electricity market for Darwin-Katherine. The reforms aimed to promote greater efficiencies and more effective competition in the provision of utilities services.

The Territory continues to heavily subsidise the provision of services by the government owned corporations through significant community service obligation (CSO) funding. Total CSO funding to the government owned corporations in 2017-18 was over $110 million, with $19 million provided to support Pensioner and Carer Concessions. In 2018-19, total CSOs are forecast to be around $119 million.

The cost of the CSO remains heavily dependent on the wholesale costs of generation. Further work is being undertaken in this area as part of the Territory's utilities reform agenda, adoption of the government's 50 per cent renewables target and to encourage greater competition, efficiency and innovation in the delivery of wholesale generation. Under the government owned corporations legislative framework, each government owned corporations agrees a Statement of Corporate Intent (SCI) annually, including a four year financial forecast with the shareholding minister. The current SCI period is 2018-19 to 2021-22.

In 2018-19, PWC will pay dividends for the first time since structural separation as a result of its profitability in 2017-18. Over the SCI period, PWC is forecast to achieve improved financial performance and sustainability. PWC is undertaking a program of modernising its operating practices, which should improve its financial performance. However, there are a number of risks to PWC's SCI, including the outcome of the 2019 Network Price Determination for regulated network revenue.

At the time of structural separation, T-Gen and Jacana were established with appropriate capital structures to operate in competitive markets.

T-Gen's financial performance has rapidly declined since structural separation, primarily due to increased operating costs and a reduction in electricity demand partially related to the uptake of renewables. T-Gen's financial performance is forecast to improve only marginally over the SCI period and is largely dependent on the corporation achieving efficiencies through transformation projects including major infrastructure upgrades in Alice Springs and Tennant Creek. T-Gen's financial position is supported over the SCI period by the provision of a $15 million equity injection from government and a dividend holiday. This is not a sustainable outcome.

Jacana's financial performance has remained relatively steady since structural separation and is forecast to remain stable over the SCI period. It has paid marginal dividends to government since 2015-16, however, these are underwritten by increases in wholesale generation charges and significant CSO funding provided by government.

Continuing with the electricity market reforms should encourage the government owned corporations to be more efficient and accountable. The ultimate objective of the government owned corporations is for them to achieve financial sustainability, while maintaining affordable and reliable levels of service.

Fiscal management

Prudent fiscal management means maintaining a whole of government fiscal position that is sustainable and resilient to the shocks that impact all economies from time to time. Achieving modest budget surpluses over the course of the economic cycle also enables the sustainable provision of services and provides flexibility and capacity to deliver on government's strategic priorities.

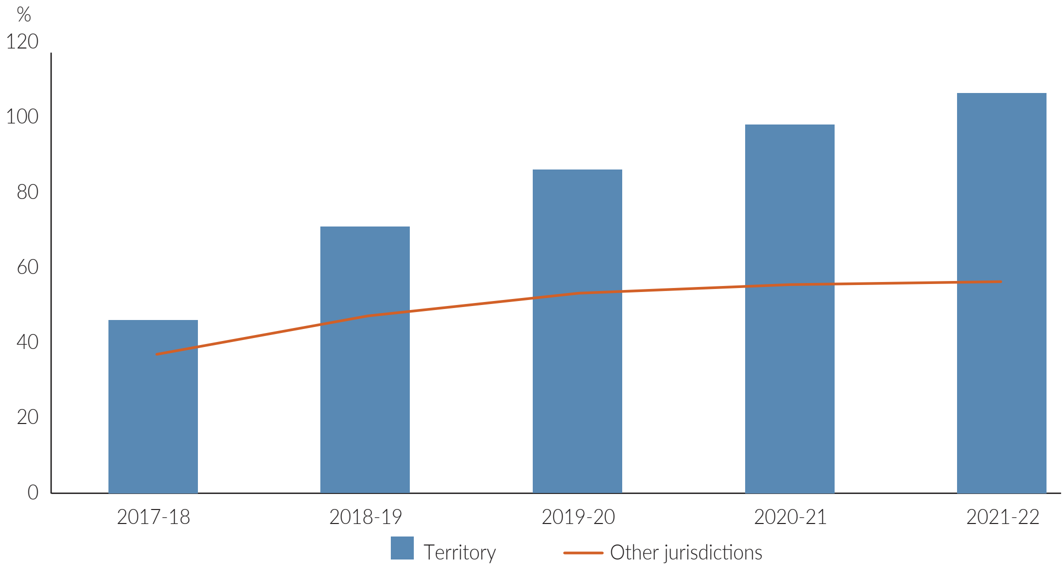
The sustained accumulation of government debt through persistent budget deficits impacts on intergenerational equity by shifting the financial burden of today's spending to tomorrow's generation. This can make sense where future generations benefit from today's investment (for example, economic enabling infrastructure); however, borrowing to fund recurrent expenditure will ultimately lead to higher taxation and/or reduced services in future, potentially undermining public and investor confidence.

Governments must provide essential services to their communities on as constant a basis as possible. In periods of poor economic conditions, governments commonly borrow to fund these services and debt markets recognise that they are ultimately backed by the power to raise taxes to fund their borrowings, and that economies as a whole will recover from setbacks. This means that in response to short-term shocks, government finances can incur temporary deficits to maintain service delivery through difficult times.

However, the willingness of markets to lend to governments at competitive interest rates is not unlimited. Governments that incur persistent budget deficits for an extended period face the risk of increasing costs for their debt. This can result in mounting repayment obligations, which erodes capacity to provide services or invest in infrastructure.

The Territory is not immune from these challenges and already has an above average net debt to revenue ratio (a key indicator of capacity to service debt). Should the Territory's budget continue to deteriorate, the cost of maintaining government service levels will escalate in the form of higher interest charges associated with lower credit ratings, eroding the Territory's capacity to sustainably manage interest costs.

Chart 14: Net debt to revenue ratio



It is important that industry leaders and the Territory community more broadly, understand and acknowledge the limitations of government's spending capacity. Given the potential risks to all Territorians, it is essential that the Territory operates in a fiscally responsible and sustainable manner.

Existing budget repair measures

Since the 2016 PEFO, in recognition of its deteriorating fiscal position, the Territory Government progressed a range of budget improvement measures to reduce expenditure growth while also continuing to support employment and population growth, particularly in the short term. The cumulative impact of the measures totals around $830 million comprising:

2017 Budget measures

- operational and program efficiencies, including rationalising administration tasks to focus on core agency functions
- revising the wages policy from 3 per cent to 2.5 per cent
- reducing CPI indexation on agency budgets to nil in 2017-18, 1.5 per cent in 2018-19 and 2.5 per cent thereafter, consistent with updated economic forecasts
- reducing the efficiency dividend discount for frontline agency budgets from 75 per cent to 67 per cent from 2017-18, to drive further productivity improvement in back office functions

2018 Budget measures

- further revision to the wages policy from 2.5 per cent to 2 per cent for all new enterprise agreements from 1 October 2018 (later extended to 14 December 2018).
- further reducing CPI indexation on agency budgets to 1 per cent in 2018-19 and 2 per cent in 2019-20 and 2.5 per cent thereafter, consistent with updated economic forecasts
- returning the repairs and maintenance program towards pre-stimulus levels

- implementing sustainable workforce strategies to control the growth of the public sector, including 250 targeted voluntary redundancies and a freeze on creating new positions
- driving efficiencies in Territory Generation
- reviewing grant arrangements to ensure value for money.

Table 4 summarises the financial impact of the 2017 and 2018 Budget measures.

Table 4: Budget improvement measures since 2016 PEFO

	2017-18	2018-19	2019-20	2020-21	2021-22	Total
	$000	$000	$000	$000	$000	$000
2017 Budget measures	74 000	112 000	128 000	140 000	140 000	594 000
2018 Budget measures		40 850	53 300	63 800	76 600	234 550
Total	74 000	152 850	181 300	203 800	216 600	828 550

Despite these measures, significant budget deficits are forecast across the forward estimates as expenditure has continued to grow due to increasing demand for government services (for example, health), unexpected costs associated with the Royal Commission into the Protection and Detention of Children in the Northern Territory, and significant economic and infrastructure stimulus.

The Territory Budget is based on a forward estimates model, with indexation factors applied to the underlying ongoing budget of each agency, and additional funding incorporated for initiatives approved throughout the year.

Due to the compounding and ongoing effect of indexation, variations can have substantial impacts on the Territory Budget over the medium to long term. For example, reducing wages indexation by 0.5 percentage points generates a saving of around $11 million in the initial year, increasing to around $55 million per annum by the fifth year.

The Territory Government applies an efficiency dividend to agency budgets to drive ongoing productivity improvements in the public sector. The 2018 Budget included an efficiency dividend of 2 per cent in 2018-19 and 2019-20, reducing to 1 per cent from 2020-21. The efficiency dividend is reviewed annually as part of the budget development process.

While modest efficiency dividends can drive a sustained focus on productivity improvement, over reliance on this relatively blunt instrument can lead to unsustainable practices (for example, underspending on repairs and maintenance, which can reduce the useful life and efficient performance of an asset) and defer the need to make difficult decisions on specific program and activities. The scale of the Territory's fiscal challenge means that budget repair will need to focus on targeted and structural reforms rather than increased efficiency dividends.

2 | Medium-term fiscal projections

Key points

- The Department of Treasury and Finance has been developing a medium-term fiscal model for the Territory to assess sustainability of current policies beyond the forward estimates to 2029-30.
- The modelling includes scenario analysis to inform the development of future budgets and government policies.
- Continuing on a business as usual path (scenario 1) is not an option as debt would escalate to unsustainable levels.
- Restraining expenditure growth (scenario 2) through a new fiscal strategy underpinned by structural reforms to the public sector would achieve a fiscal surplus in the non financial public sector in 2028-29.
- Restoring the Territory's share of untied Commonwealth revenue to historical average levels, in conjunction with expenditure restraint under a new fiscal strategy, would bring forward the return to surplus to 2025-26.

The Territory Government publishes budget and fiscal outlook reports that, as required by the *Fiscal Integrity and Transparency Act 2001*, include financial projections for the budget year and the following three financial years for the general government and non financial public sectors. The three financial years following the budget year are commonly referred to as the forward estimates.

The three-year forward estimates model is used at the state and federal level in Australia and provides the estimated fiscal outcomes over the period on a no-policy change basis but incorporating the impact of relevant assumptions (for example, wage growth and inflation) on future revenue and expenditure. This provides a lens through which strategic policy issues can be assessed and against which financial discipline can be measured.

Table 5 provides a summary of the Territory's key fiscal aggregates as at the 2018 Mid-Year Report.

Table 5: Key fiscal aggregates

	2017-18	2018-19f	2019-20f	2020-21f	2021-22f
	$M	$M	$M	$M	$M
General government sector					
Net operating balance	- 375	- 917	- 696	- 730	- 749
Non financial public sector					
Revenue	6 532	6 346	6 475	6 478	6 640
Expenses	- 6 932	- 7 259	- 7 109	- 7 141	- 7 320
Net capital payments	- 953	- 1 156	- 1 033	- 755	- 656
Fiscal balance	**- 790**	**- 1 513**	**- 1 122**	**- 871**	**- 789**
Net debt	3 008	4 502	5 573	6 355	7 072
Net debt to revenue (%)	46	71	86	98	107
Interest expense	- 290	- 312	- 364	- 406	- 458
Interest to revenue (%)	4	5	6	6	7

f: forecast
Note: the fiscal balance does not include depreciation. As a result, elements in the table are not additive.
Source: 2018 Mid-Year Report.

In recent years, a number of jurisdictions have recognised the need to increase the focus on challenges beyond the traditional forward estimates period and have undertaken medium-term fiscal modelling and, in some cases, published intergenerational reports to assess the medium (5 to 10 years) to long (+10 years) term sustainability of government policies.

Since the 2018 Budget, which forecast significant and persistent operating and fiscal deficits over the budget and forward estimates, the Department of Treasury and Finance has been developing a medium-term fiscal model for the Territory to assess the sustainability of current policies over the medium term to 2029-30. The modelling has also included scenario analysis to inform the development of future budgets and government policies.

The modelling and scenarios presented in this report are based on the most up to date figures and forecasts in the 2018 Mid-Year Report. Tied funding from the Commonwealth is assumed to have no net impact on the projections (that is, expenses match revenues). Further details are provided at Appendix A.

Scenario 1: Business as usual

The business as usual scenario assumes that recurrent expenditure growth continues to reflect historical patterns. That is the growth in operating expenses (excluding interest expenses) trends in line with growth rates of 6.2 per cent a year, well above the growth rates in scenario 2. This scenario also assumes that capital expenditure remains at current stimulus levels and grows at long-term average rates over the projection period.

Own-source revenues match the 2018 Mid-Year Report and then assume stronger payroll tax, stamp duty on conveyances and mining royalty revenue over the projection period, reflecting an expected economic recovery driven by an expanded onshore gas industry from 2022-23. Remaining taxation revenues are projected to grow at 3.9 per cent (reflecting CPI plus long-term population growth).

GST projections match the 2018 Mid-Year Report. An ongoing relativity floor of 4.66 is also assumed. The projections factor in the Commonwealth's $600 million top up to the national GST pool in 2021-22 and $250 million top up 2024-25 as well as changes in the *Treasury Laws Amendment (Making Sure Every State and Territory Gets Their Fair Share of GST) Act*.

Under this scenario the Territory Government would not achieve a fiscal surplus in the non financial public sector over the period to 2029-30. Net debt would reach $35.7 billion by 2029-30, with a net debt to revenue ratio approaching 320 per cent (more than four times the current level).

These fiscal deficit and net debt outcomes would worsen the Territory's credit rating and significantly increase borrowing costs. These impacts would have significant adverse ramifications for the Territory Government's economic and fiscal management credibility.

Scenario 2: A new fiscal strategy – medium-term budget repair

This scenario assumes the Territory Government implements a new fiscal strategy as part of the 2019 Budget, which restrains expenditure growth over the forward estimates and projection period.

Recurrent and capital expenditure growth over the forward estimates reflect the 2018 Mid-Year Report. Growth over the projection period is 3 per cent per annum (reflecting CPI plus long-term population growth less a reform dividend). The exception is interest expenses, which are based on projected borrowing requirements assuming a long-term borrowing rate of 5 per cent.

Achieving this outcome will require a combination of significant structural reform and prudent budget management to ensure that demand increases for services such as health are offset by increased productivity or efficiencies across government. Stimulus funding, beyond that already approved, would also need to be offset by savings in other areas.

Own-source revenue and GST projections match scenario 1.

Under this scenario the Territory Government would achieve a fiscal surplus in the non financial public sector in 2028-29. Net debt would peak at $8.8 billion in 2026-27, with the net debt to revenue ratio peaking at 112 per cent.

The challenges to achieving this scenario are constraining expenditure growth (recurrent and capital), in an environment of increasing demand for government services, resisting pressure to provide further stimulus in the short term to cushion dampened private investment associated with the Ichthys LNG project transition and securing an ongoing commitment from the Commonwealth for the 4.66 relativity floor.

Restoring the Territory's share of untied Commonwealth revenue to historical average levels, in conjunction with expenditure restraint under a new fiscal strategy, would bring forward the return to surplus to 2025-26.

What do the scenarios mean?

The scenarios demonstrate that, in the absence of immediate and sustained expenditure restraint, the next generation of Territorians will bear a growing burden of current expenditure through interest costs and reduced capacity for service delivery with interest expenses approaching $2 billion per annum, or around 12 per cent of total expenditure. This also means that a substantial proportion of borrowing over this period would be used to pay interest costs rather than deliver the services that future Territorians will need.

Without a new fiscal strategy, underpinned by structural reforms to drive expenditure restraint, the Territory will have little to no capacity to respond to unanticipated shocks and a greater exposure to interest rate movements.

Private investors and businesses are forward looking, making decisions today based on their best estimate of the future and an assessment of risk. Large and growing government debt undermines the private sector's willingness to invest and create jobs, by sending the message that future governments will have to either increase the general level of taxation, or spend less on the enabling infrastructure and services that support economic growth, such as efficient transport infrastructure and the skills of our workforce.

3 | Economic context

Key points

- Following a period of strong growth, driven by a series of major projects of increasing value since 2001-02, the Territory is currently experiencing a downturn in the economic cycle.
- While headline economic growth (GSP) over the forward estimates is likely to be supported by additional net exports generated mainly from LNG, state final demand is expected to contract.
- In the long run, growing the Territory economy will reduce the Territory's reliance on Commonwealth funding. However, in the short to medium term, changes in the Territory's economy and the subsequent impact on own-source revenues will continue to play a secondary role given the relatively small share of own-source revenue as a proportion of total Territory revenue.
- The Territory cannot grow its way out of the current fiscal predicament in the timeframe required.

The Territory economy

The Territory economy is characterised by a relatively large public sector, a significant defence force presence and a small and remote population, distributed over a large and isolated area.

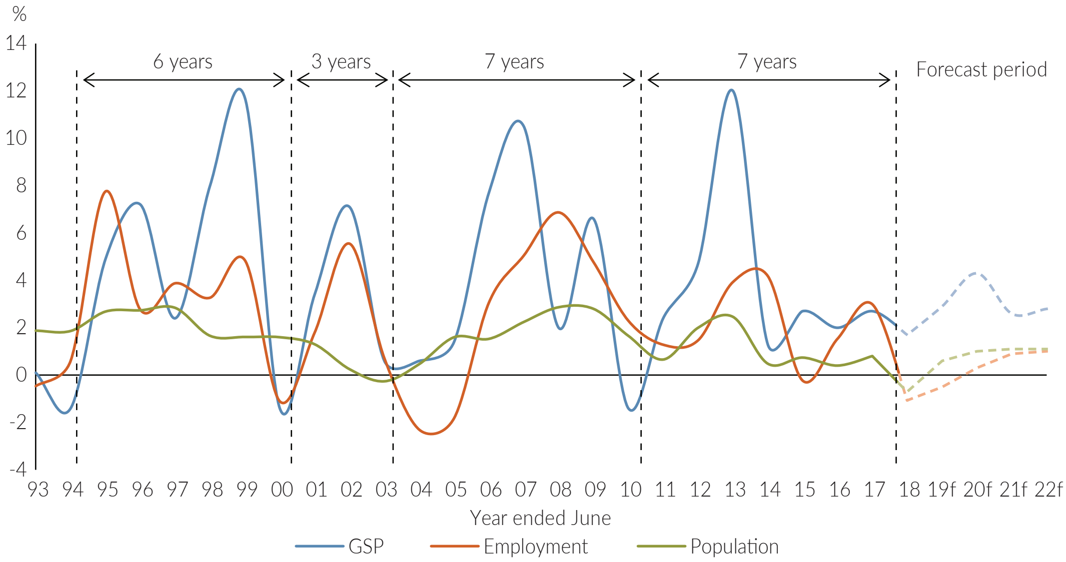
The construction and mining industries have historically been the main drivers of the Territory's economic growth, largely influenced by major projects.

The Territory economy, like all economies, is subject to cyclical effects with the frequency, magnitude and length of time between periods of growth linked to the structure and size of the economy, reliance on key industries and vulnerability to external factors such as commodity prices and exchange rates. The Territory's economic cycles tend to be more volatile than other jurisdictions, largely reflecting the structure of the economy and exposure to commodity prices, exchange rates and external factors.

As a small, open and resource driven economy, the economic cycles in the Territory tend to be more pronounced than in other jurisdictions. Over the last 25 years the Territory has experienced growth cycles averaging six to seven years, with expansionary cycles followed by periods of contraction.

Following a period of strong growth, the Territory is currently experiencing a downturn in the economic cycle, which is reflected in low growth across a number of key economic indicators including the Territory's gross state product, employment and population (Chart 15).

Chart 15: Key economic indicators, year on year change (%)



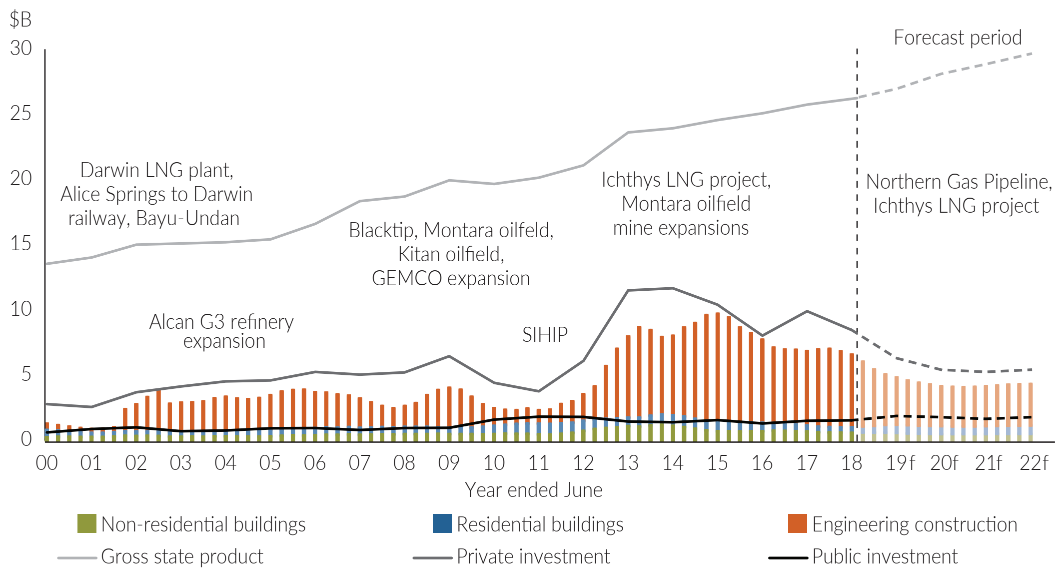
Headline economic growth in the Territory moderated to 1.7 per cent in 2017-18 but is forecast to strengthen over 2018-19 and 2019-20, mainly reflecting the transition of the Ichthys LNG project from the construction phase to its export and production phase.

Economic forecasts

While economic growth over the forward estimates is likely to be supported by net exports, as well as modest growth in household consumption, state final demand is still expected to contract. Other key economic indicators are also forecast to remain subdued or in some cases decline in the next couple of years before gradually strengthening again over the forward estimates.

The economic contribution of the construction sector is expected to decline in relative terms over the forward estimates as private sector construction returns to long-run average levels following the transition of the Ichthys LNG project from the construction to the production phase.

Chart 16: Economic growth and construction work done



In the long run, growing the Territory economy will reduce the Territory's reliance on Commonwealth funding. However, in the short to medium term, changes in the Territory's economy and their subsequent impact on own-source revenues will continue to play a secondary role given the relatively small share of own-source revenue as a proportion of total Territory revenue.

The Territory cannot grow its way out of the current fiscal predicament in the timeframe required and historical economic patterns demonstrate that the Territory economy, like economies in other jurisdictions, will continue to grow and expand largely independent of government stimulus and infrastructure investment.

4 | Fiscal strategy

Key points

- The relevance of the Territory's current fiscal strategy has diminished following significant, successive and ongoing reductions in the level of untied Commonwealth funding, principally GST revenue, to the Territory since 2016-17.
- The reduction has not been matched by a corresponding decline in expenditure, resulting in ongoing operating and fiscal deficits over the medium to long term.
- The resultant structural deficit requires a revised fiscal strategy in response that adopts a medium to long-term focus.
- The new fiscal strategy should continue to incorporate the non financial public sector and include efficiency targets for government owned corporations to measure their progress towards operating on a commercial footing.
- The Territory should also review its financial management frameworks and enabling legislation to ensure they remain contemporary and support accountable and transparent financial decision making.

A new fiscal strategy

The *Fiscal Integrity and Transparency Act* (FITA) requires that the Territory Government publish a fiscal strategy, based on the principles of sound fiscal management, that among other things:

- specifies government's medium-term fiscal objectives
- explains the broad strategic priorities on which the budget is or will be based
- specifies the key fiscal indicators that government considers important and against which fiscal policy will be set and assessed.

The Territory's current fiscal strategy comprises short and medium-term fiscal objectives and targets, with the aim of supporting the economy in the short term and providing a pathway back to a balanced budget and reduced debt levels over the medium term.

The relevance of the Territory's current fiscal strategy has diminished following significant, successive and ongoing reductions in the level of untied Commonwealth funding, principally GST revenue, to the Territory since 2016-17. These revenue reductions are structural rather than cyclical and require a revised fiscal strategy in response, with a medium to long-term focus.

The new fiscal strategy will need to be supported by a range of structural reforms to the NTPS to return the budget to a sustainable position. It provides a rare opportunity to implement strategic and generational change in the delivery of government services to Territorians.

Fiscal strategy principles

The key principles of the current fiscal strategy (sustainable service provision, infrastructure for economic and community development, competitive tax environment, and prudent management of debt and liabilities) remain relevant. The use of timeframe specific targets, also remain relevant, to provide flexibility to respond to economic and fiscal shocks within an overarching goal of returning to balance. However, a new strategy will need to embrace a more medium to long-term focus in recognition of the structural reform required to return the budget to balance and the FITA's medium to long-term focus.

Due to the fiscal drag of the government owned corporations on the budget, the new strategy should also include efficiency targets for the government owned corporations to measure their progress towards operating on a commercial footing and providing sustainable returns on the Territory's investment in this area.

More broadly, the Territory should review its financial management frameworks and enabling legislation to ensure they remain contemporary and support accountable and transparent financial decision making.

5 | A plan for budget repair

Key points

- A steadfast commitment to expenditure restraint and significant reform will be necessary to return the budget to a sustainable position over the medium term.
- The Territory will continue to face pressure to provide high quality services irrespective of the fiscal environment. In this context it will be essential that the Territory ensures its structure, policies and programs are as effective and efficient as possible.
- There are a range of structural reform opportunities that should be investigated with a particular emphasis on reducing duplication and achieving economies of scale.
- This report provides the basis for informed stakeholder engagement and community input to assist in the development of a framework for medium to long-term fiscal repair.

Whole of government reform framework

A steadfast commitment by government, the public sector and the broader community to expenditure restraint and significant reform will be necessary to return the budget to a sustainable position over the medium term, regardless of the fiscal strategy adopted, and to avoid the negative economic and fiscal consequences of sustained deficit spending including:

- an inability to maintain a competitive service delivery and infrastructure standard as interest payments consume an escalating proportion of the Territory's budget
- a reduced ability to respond to economic shocks through counter cyclical investment
- a reduction in consumer and investor confidence as escalating debt levels increase the likelihood of austerity and revenue raising measures
- credit downgrades that:
  - exacerbate interest costs through the need to offer higher returns to investors to secure funds
  - limit the availability of investment funds to the Territory
- shifting the burden of funding current services to future generations of Territorians, which is inconsistent with the requirements of the FITA.

To drive expenditure restraint and a return to budget more broadly, the Territory has developed a high level medium term whole of government plan that includes six broad reform themes:

- financial management
- organisational capability
- program evaluation
- workforce sustainability and capability

- machinery of government
- revenue optimisation.

A high level diagram of the fiscal strategy plan is provided at Appendix B. A number of the reforms, particularly those associated with corporate services productivity improvements, can be progressed relatively quickly with minimal impact on the broader public.

Next steps

The Territory will continue to face pressure to provide high quality services irrespective of the fiscal environment. In this context it will be essential that the Territory ensures its structure, policies and programs are as effective and efficient as possible.

In addition to reviewing the Territory's financial management framework, there are a range of structural reform opportunities that should be investigated with a particular emphasis on reducing duplication and achieving economies of scale.

This report provides the basis for informed stakeholder engagement and community input to assist in the development of a framework for medium to long-term fiscal repair. Stakeholders will have the opportunity to contribute through a variety of channels including face to face discussions with the panel, written submissions and the Department of Treasury and Finance website.

How to provide your feedback

Send us your written submissions via:

Email	FiscalStrategy.dtf@nt.gov.au
Post	A plan for budget repair interim report feedback Department of Treasury and Finance GPO Box 1974 Darwin, NT 0801

Download a copy of this report and the overview at www.treasury.nt.gov.au

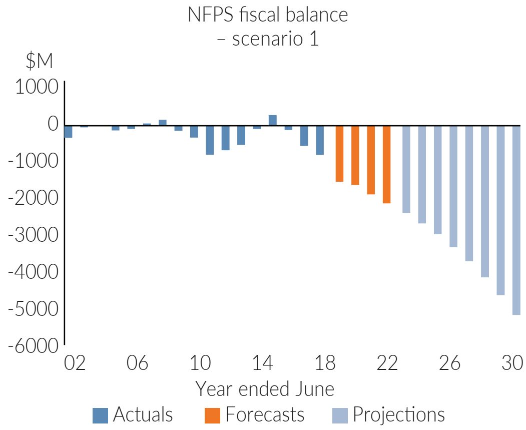
Appendix A: Scenarios

Scenario 1

Base GST projections. Business as usual expenditure growth, which differs from the figures published in the 2018 Mid-Year Report.

Key indicators	Historical average[1]	Forecasts[2]	Projections[3]
	%	%	%
Revenue growth	5.9	5.2	5.3
Expenditure growth	6.2	6.9	7.4
Average net debt to revenue ratio	44.4	94.9	224.5

1 Average growth between 2002-03 and 2017-18.
2 Average growth between 2018-19 and 2021-22.
3 Average growth between 2022-23 and 2029-30.

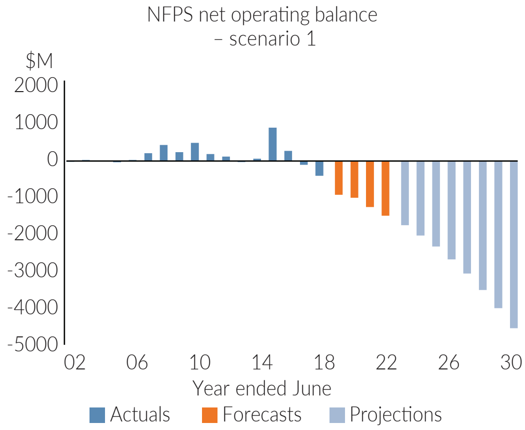


Key scenario assumptions

Revenue

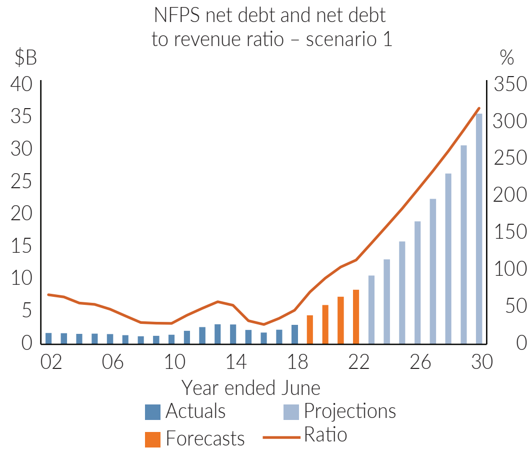
GST projections match the 2018 Mid-Year Report. An ongoing relativity floor of 4.66 is also assumed. The projections factor in the Commonwealth's $600 million top up to the GST pool in 2021-22 and $250 million top up 2024-25 as well as changes in the *Treasury Laws Amendment (Making Sure Every State and Territory Gets Their Fair Share of GST) Act 2018*.

Own-source revenues match the 2018 Mid-Year Report and then assume stronger payroll tax, stamp duty on conveyances and mining royalty revenue over the projection period, reflecting an expected economic recovery driven by an expanded on shore gas industry from 2022-23. Remaining taxation revenues are projected to grow at 3.9 per cent (reflecting CPI plus long-term population growth).



Recurrent expenditure

Recurrent expenditure growth assumes a continuation of historical average rates, differing from the 2018 Mid-Year Report, which includes
a level of expenditure restraint. Interest expenses are based on borrowing requirements assuming a long-term borrowing rate of 5 per cent. Tied Commonwealth expenditure is assumed to net off against revenues over the period (no impact on fiscal balance).



Capital expenditure

Capital expenditure growth remains at current stimulus levels and grows at long-term average rates over the projection period.

Key risks

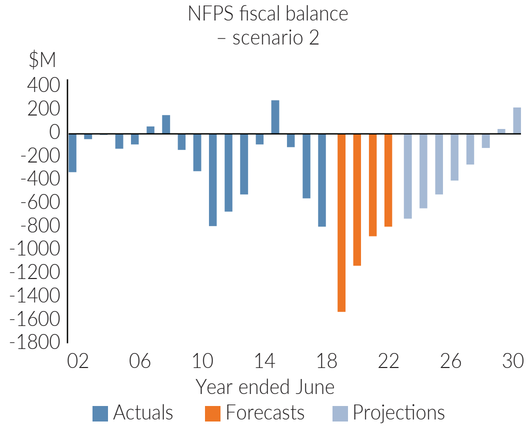
The fiscal outcomes under this scenario would be untenable and have significant adverse ramifications for the Territory Government's credit rating and economic credibility. This scenario also raises significant intergenerational equity issues.

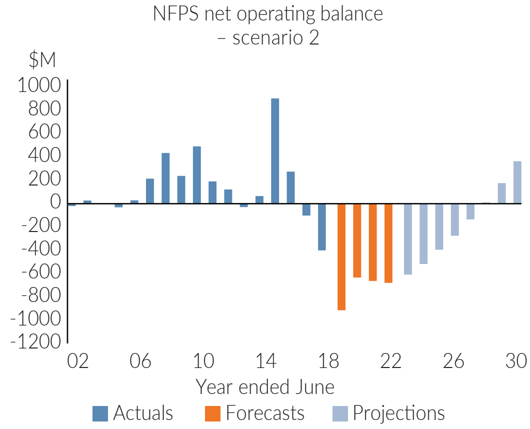
Scenario 2

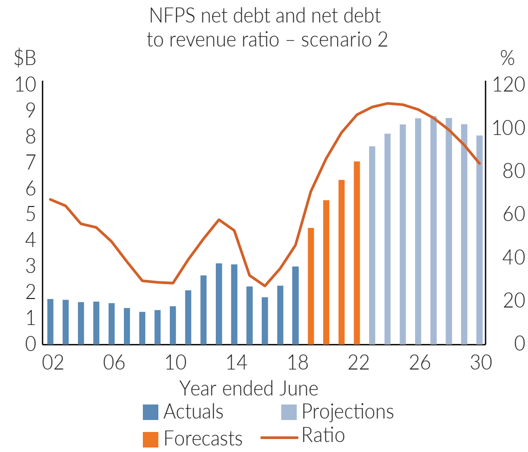
The Territory implements a new fiscal strategy as part of the 2019 Budget, which restrains expenditure growth. GST projections match the figures published in the 2018 Mid-Year Report for the forecast period and continue at similar levels over the projection period.

Key indicators	Historical average[1]	Forecasts[2]	Projections[3]
	%	%	%
Revenue growth	5.9	1.5	4.8
Expenditure growth	6.2	0.3	2.9
Average net debt to revenue ratio	44.4	90.4	102.8

1 Average growth between 2002-03 and 2017-18.
2 Average growth between 2018-19 and 2021-22.
3 Average growth between 2022-23 and 2029-30.







Key scenario assumptions

Revenue

GST projections match the 2018 Mid-Year Report. An ongoing relativity floor of 4.66 is also assumed. The projections factor in the Commonwealth's $600 million top up to the GST pool in 2021-22 and $250 million top up 2024-25 as well as changes in the *Treasury Laws Amendment (Making Sure Every state and Territory Gets Their Fair Share of GST) Act 2018*.

Own-source revenues match the 2018 Mid-Year Report and then assume stronger payroll tax, stamp duty on conveyances and mining royalty revenue over the projection period, reflecting an expected economic recovery driven by an expanded on shore gas industry from 2022-23. Remaining taxation revenues are projected to grow at CPI (2.5 per cent) plus long-term population growth (1.4 per cent).

Recurrent expenditure

Recurrent expenditure growth matches the 2018 Mid-Year Report figures. Growth over the projection period is 3 per cent per annum (reflecting CPI plus long-term population growth less a reform dividend). The exception is interest expenses, which are based on projected borrowing requirements assuming a long-term borrowing rate of 5 per cent.

Capital expenditure

Capital expenditure matches 2018 Mid-Year Report figures, with growth of 3 per cent (reflecting CPI plus long-term population growth less a reform dividend) assumed over the subsequent projection period.

Key risks

Achieving sustained expenditure restraint through reform, returning capital expenditure to pre-stimulus levels and securing an ongoing commitment from the Commonwealth for the 4.66 relativity floor represent the key risks to this scenario.

Appendix B: A plan for budget repair

PHASE
01
IMMEDIATE

FISCAL STRATEGY REFORM

Fiscal Strategy Experts

- External expertise
- Establish case for change
- Review fiscal strategy and financial management policies
- Provide advice
- Avoid new taxes

Financial Management Framework

- Review *Financial Management Act* and *Fiscal Integrity and Transparency Act*
- Refresh supporting instruments and policies
- Implement program evaluation framework

PHASE
02
SHORT TERM

STRUCTURAL REFORM

Financial Management Reform

- Reform Treasury portfolio issues:
  - Refresh budget framework
  - Review tied funding arrangements
  - Review cash management policies and processes
  - Enhance forward estimates budgeting and reporting

Machinery of Government Reform

- Identify opportunities to improve productivity through contemporary organisational models
- Harmonise policies and procedures

PHASE
03
MEDIUM TERM

ORGANISATIONAL AND PROGRAM REFORM

Organisational Reviews

- Ongoing program of review and reform
- Focus on effective and efficient service delivery

Public Sector Employment Reform

- With Stakeholders:
  - Review wages policy
  - Contemporise employment policies and legislation
  - Develop public sector capability and capacity

Revenue

- Revenue policy reform:
  - Strengthen revenue compliance
  - Develop public asset management framework