Report of the Auditor-General

Auditor-General's Department

Report 10 of 2022

State finances and related matters

Government of South Australia

[P.P.4H

Report of the Auditor-General

Report 10 of 2022

State finances and related matters

Tabled in the House of Assembly and ordered to be published, 18 October 2022

First Session, Fifty-Fifth Parliament

By authority: C. McArdle, Government Printer, South Australia

2022

The Auditor-General's Department acknowledges and respects Aboriginal people as the State's first people and nations, and recognises Aboriginal people as traditional owners and occupants of South Australian land and waters.

Auditor-General's Department

www.audit.sa.gov.au

Enquiries about this report should be directed to:

Auditor-General
Auditor-General's Department
Level 9, 200 Victoria Square
Adelaide SA 5000

ISSN 0815-9157

Government of South Australia
Auditor-General's Department

Level 9
State Administration Centre
200 Victoria Square
Adelaide SA 5000
DX 56208
Victoria Square
Tel +618 8226 9640
Fax +618 8226 9688
ABN 53 327 061 410
audgensa@audit.sa.gov.au
www.audit.sa.gov.au

17 October 2022

President
Legislative Council
Parliament House
ADELAIDE SA 5000

Speaker
House of Assembly
Parliament House
ADELAIDE SA 5000

Dear President and Speaker

Report of the Auditor-General:
Report 10 of 2022 *State finances and related matters*

Under the *Public Finance and Audit Act 1987*, I present to each of you this Report.

Content of the Report

The 2022-23 State Budget was tabled in Parliament in June 2022. This Report provides our observations on the State's public finances based on our review of the Budget. This involved:

- reviewing the Budget against the SA Government's stated fiscal strategy
- analysing new budget measures and initiatives
- examining Budget estimates and forecasts
- analysing major assets and liabilities
- analysing South Australia's key fiscal measures compared to other Australian states
- reviewing credit rating agency reports on South Australia.

Our analysis is based on data provided in the 2022-23 Budget Papers, supplemented by representations and information provided by the Department of Treasury and Finance. The 2021-22 estimated result in the 2022-23 Budget reflects the activities of the previous SA Government from July 2021 to March 2022, and the current SA Government from March 2022 onwards.

In the few months since the 2022-23 Budget was released there have been significant emerging and evolving events, which may impact budget forecasts. This includes large waves of COVID-19 infections in South Australia during the winter period and high inflation leading the Reserve Bank of Australia to raise its cash rate target by 2.25%.

Acknowledgements

The review team for this Report was Salv Bianco, Ken Anderson, Stephen Gladigau and Simon Altus.

We appreciate the cooperation and assistance given by staff of the Department of Treasury and Finance during our review.

Yours sincerely

Andrew Richardson
Auditor-General

Contents

1 Executive summary

1.1 Introduction

This Report provides our observations on key matters, trends and risks for the State's public finances based on our review of the 2022-23 State Budget (2022-23 Budget).

The 2022-23 Budget is the first budget of the current SA Government following its election in March 2022. It was tabled in Parliament in June 2022 and aims to deliver the current SA Government's election commitments.

The 2021-22 estimated result in the 2022-23 Budget reflects the activities of the previous SA Government from July 2021 to March 2022, and the current SA Government from March 2022 onwards.

In the few months since the 2022-23 Budget was released there have been significant emerging and evolving events, which may impact budget forecasts. This includes large waves of COVID-19 infections in South Australia during the winter period and high inflation leading the Reserve Bank of Australia (RBA) to raise its cash rate target by 2.25%.[1]

1.2 Key observations and risks

1.2.1 Significant economic uncertainty increases risk that actual results will substantially differ from Budget forecasts

The 2022-23 Budget assumes moderate economic growth over the four years of the Budget, however it notes that this will be against a backdrop of several economic risk factors.

The economic risks that may impact forecasts in the 2022-23 Budget include:

- rising inflation and interest rates placing pressure on the fiscal sustainability of governments
- the emergence of new, more virulent or vaccine-resistant variants of COVID-19 that may require further restrictions, negatively affecting consumption and investment
- continued global supply chain disruptions.

The ongoing and emerging impacts of these economic risk factors mean there is an increased likelihood that actual results will differ from Budget estimates. In the few months since the 2022-23 Budget was released, there have been significant new waves of COVID-19 infections in South Australia, inflation has increased rapidly with several rises in RBA interest rates and

[1] The RBA cash rate target effective at the time of the 2022-23 Budget released on 2 June 2022 was 0.35%. This rate has increased to 2.6%, effective 5 October 2022, <https://www.rba.gov.au/statistics/cash-rate/>.

global economic forecasts have been revised downwards. These emerging trends and events may place upward pressure on health expenditure, interest expenses, operating costs and capital project costs.

The Department of Treasury and Finance (DTF) advised us that, at the time of the 2022-23 Budget, it considered the impacts of these risks to be potentially significant and highly uncertain. However, it also considered the economic forecasts in the Budget to be, on balance, likely to prevail in the face of the assessed risks.

Section 3.2 provides further details on the risks and uncertainties impacting 2022-23 Budget forecasts. The SA Government's 2022-23 mid-year budget review (MYBR) will provide an update on the evolving budget impacts of these risk factors and also capture impacts from the new Commonwealth Government's revised 2022-23 Budget.

1.2.2 SA Government will face several challenges delivering forecast net operating surpluses

The SA Government is forecasting a moderate net operating balance surplus for the general government sector in 2022-23 ($233 million), following significant net operating deficits between 2019-20 and 2021-22. Net operating surpluses are forecast to increase gradually over the remainder of the forward estimates, rising from $487 million in 2023-24 to $643 million in 2025-26.

The risk factors that may prevent a return to surplus in 2022-23 and over the forward estimates include:

- economic conditions reducing consumption and investment expenditure and consequently reducing revenues from GST and state taxation
- SA Health facing challenges achieving its budget target of reducing total expenditure by 6% between 2021-22 and 2022-23 given ongoing COVID-19 impacts, inflationary pressures and its history of not achieving savings goals
- non-frontline agencies needing to identify significant new operating efficiency savings totalling $411 million in addition to those already made in previous budgets, while trying to maintain current service levels
- growth in employee expenses exceeding that allowed for in the forward estimates, as current enterprise agreement negotiations capturing 44% of general government sector employees are occurring during a period of high inflation.

The Australian Regional Governments report issued by Moody's credit rating agency on 5 September 2022 commented that:

- it expects state revenue growth across Australia to moderate as housing market activity slows and the higher cost of living constrains consumption-driven revenue

- higher costs of living and rising interest rates also pose upward pressures on state budgeted expenditure profiles, amid wage agreement negotiations, rising debt levels and increasing recurrent new health spending
- increasing expenditure pressures will quickly erode already slowing revenue growth, potentially delaying targeted returns to operating surpluses.

The successful delivery of savings and maintenance of net operating surpluses may become more challenging if the SA Government's savings strategy continues to focus on non-frontline agencies.[2] It is important that monitoring of these savings considers any potential service delivery impacts.

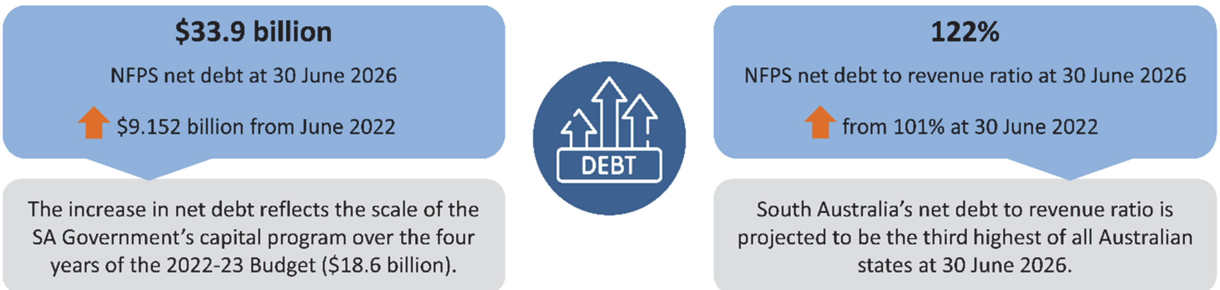
The 2022-23 Budget notes that the SA Government considers efficiency savings to be an essential component of ensuring a responsible budget and sustainable debt levels in the context of rising interest rates. It also indicates that, except for SA Health,[3] agencies have to date generally achieved these efficiency savings requirements and will be required to continue to find efficiencies to deliver future savings.

Sections 4.5 and 4.6 provide further details on revenue and expenditure trends and risks in the 2022-23 Budget.

1.2.3 Further large interest rate rises would put pressure on the State's fiscal sustainability

The SA Government's net debt increases significantly over the four years of the Budget, as shown in figure 1.1.

Figure 1.1: Key net debt trends in 2022-23 Budget



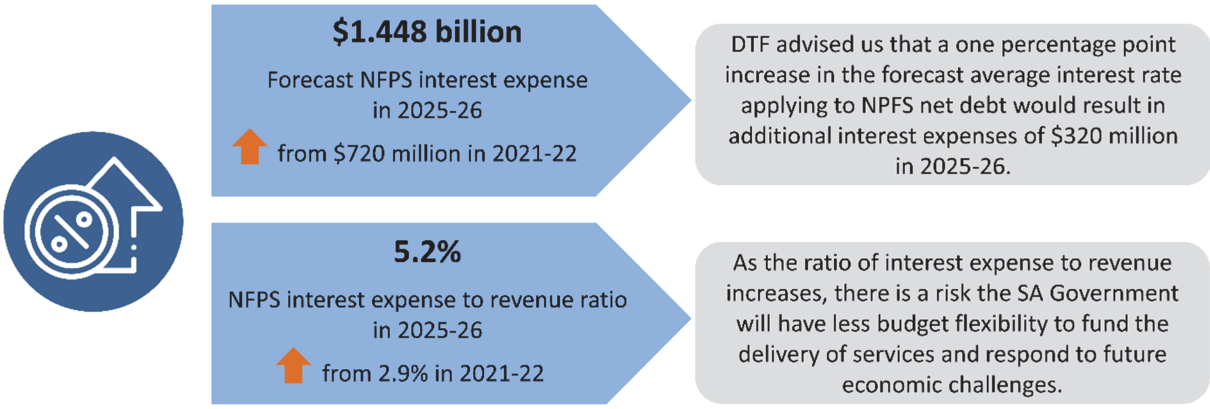
Large infrastructure initiatives included in the 2022-23 Budget are likely to result in further net debt increases beyond the forward estimates. DTF advised us that, at the time of the 2022-23 Budget, significant expenditure was expected to be incurred for the North-South Corridor River Torrens to Darlington project ($6.478 billion) and new Women's and Children's Hospital ($539 million) after 2025-26.

2 Page 20 of 2022-23 Budget Paper 3 *Budget Statement* indicates that the SA Government is seeking operating efficiencies in non-frontline services. No additional savings task has been allocated to health, education, police, child protection, TAFE SA, courts and emergency services.

3 SA Health comprises the Department for Health and Wellbeing, local health networks and the SA Ambulance Service Inc.

The RBA expects to increase interest rates further over the months ahead[4] and higher net debt levels will increase the SA Government's exposure to these interest rate rises. The forecast increases in interest expenses in the 2022-23 Budget are shown in figure 1.2.

Figure 1.2: Key interest expense trends in 2022-23 Budget



The SA Government's debt management objective is to minimise long-term average interest costs subject to acceptable levels of interest rate risk. This includes the South Australian Government Financing Authority (SAFA) issuing long-term fixed or floating interest rate securities to meet the State's funding requirements and minimise exposure to short-term movements in interest rates.

The SA Government has also set a fiscal target of achieving a level of net debt that is sustainable over the forward estimates, however it has not set a clear and quantifiable measure to assess its performance against this target. As pressures on fiscal sustainability increase, it is prudent for the SA Government to establish a clear measure of the sustainability of net debt for ongoing budget monitoring and management purposes.

Section 5.4 provides further details on the trends and risks associated with net debt and interest rates.

1.2.4 Capacity constraints and material shortages significantly increase risk of capital program cost escalations and delays

Purchases of non-financial assets for the non-financial public sector (NFPS) are projected to total $18.596 billion over the four years of the 2022-23 Budget, an increase of $687 million on purchases over the four years of the previous Budget. This is also $6.222 billion, or more than 50%, higher than the amount spent in the four years to 2021-22.

The high investing expenditure in the 2022-23 Budget reflects significant amounts allocated to the North-South Corridor River Torrens to Darlington project ($3.193 billion) and the new Women's and Children's Hospital ($1.439 billion) over the four years of the Budget.

---

[4] Reserve Bank of Australia 2022, *Statement by Philip Lowe, Governor: Monetary Policy Decision*, media release number 2022-28, 6 September, <https://www.rba.gov.au/media-releases/2022/mr-22-28.html>.

Major capital projects carry high inherent risks associated with estimating costs, complex contract arrangements, cost escalations and timeliness of completion. There are several significant challenges and risks for the SA Government's capital program, including:

- the availability of key building materials and appropriately skilled labour as governments across Australia undertake large capital programs
- the impact of inflationary pressures on material costs
- the capacity of the South Australian building industry to cope with the significant volume of works required and the potential for associated cost pressures on project budgets.

A review of the new Women's and Children's Hospital project was completed in September 2022, and estimated that the project may now cost up to $3.2 billion.[5] This represents an upwards revision of $1.16 billion from the estimate in the 2022-23 Budget. The SA Government is also currently conducting a detailed review of the costings for the North-South Corridor River Torrens to Darlington project. These are the two most significant current capital projects of the SA Government, with a total estimated cost in the 2022-23 Budget of $11.992 billion.

In the 12 months to June 2022, South Australian non-residential building construction costs increased by 4.7% and road and bridges construction costs increased by 10.9%.[6] There is a high likelihood that cost estimates for major capital projects in the 2022-23 Budget will need to be revised upwards and the additional costs will need to be funded at least in part by further borrowings, leading to higher net debt than forecast in the 2022-23 Budget. Where upward cost revisions for capital projects are significant, it would be appropriate for the SA Government to revisit relevant business cases to reassess how expected benefits compare to the revised costings and the impact on project viability.

DTF advised us that allowances for major project cost escalations are embedded in agency project budgets. For each State Budget and MYBR, agencies submit budget adjustment requests for cost pressures they have identified. These requests are considered by Cabinet and, where appropriate, additional expenditure is approved.

Section 5.3 provides further details on challenges and risks associated with the SA Government's budgeted capital program.

---

5 New Women's and Children's Hospital Project 2022, *New Site Identified*, Government of South Australia, 27 September, viewed 29 September 2022, <https://www.newwch.sa.gov.au/news/new-site-identified>.

6 Australian Bureau of Statistics 2022, *Producer Price Indexes*, June, cat. no. 6427.0, table 17, viewed 23 August 2022. Section 5.3.5.2 provides further details.

2 Review mandate, objective and scope

2.1 Our mandate

The Auditor-General has authority to conduct this review under section 36(1)(b) of the *Public Finance and Audit Act 1987*. This section allows the Auditor-General to report on matters that, in his opinion, should be brought to the attention of Parliament and the SA Government.

2.2 Our objective

The objective of this Report is to provide independent commentary and analysis on the 2022-23 Budget to highlight key matters, trends and risks for the State's public finances.

2.3 What we reviewed and how

We reviewed the 2022-23 Budget to identify key matters, trends and risks for the State's public finances. This involved:

- reviewing the Budget against the SA Government's stated fiscal strategy
- analysing new budget measures and initiatives
- examining Budget estimates and forecasts
- analysing major assets and liabilities
- analysing South Australia's key fiscal measures compared to other Australian states[7]
- reviewing credit rating agency reports on South Australia.

Our analysis is based on data provided in the 2022-23 Budget Papers, supplemented by representations and information provided by DTF.

2.4 What we did not review

This Report primarily comments on Budget information. The data and assumptions underlying this information are not subject to audit and no audit opinion is provided on the accuracy of historical or forecast figures presented in the 2022-23 Budget. We also have not performed work to provide an opinion on the effectiveness of the SA Government's budgetary control.

[7] Appendix 1 provides further details on key fiscal measures.

3 2022-23 Budget policy measures and parameter variations

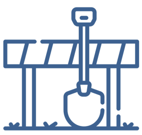
Key points

- The ongoing and emerging impacts of COVID-19, rising inflation and international conflict increase the risk that budget forecasts may not be achieved.
- Improved forecast revenues are largely offset by expenditure on new policy measures.
- Contingency and timing adjustments for existing capital projects are significantly larger than recent budgets and mainly relate to the North-South Corridor River Torrens to Darlington project and new Women's and Children's Hospital.
- SA Health will face challenges achieving its budget target of reducing total expenditure by 6% between 2021-22 and 2022-23 given ongoing COVID-19 impacts, inflationary pressures and its history of not achieving savings goals.
- New operating savings totalling $701 million have been introduced for non-frontline agencies. Achieving these targeted reductions while maintaining current service levels may be a challenge.

3.1 Overview of key trends

Figure 3.1 highlights key trends for new policy measures in the 2022-23 Budget.

Figure 3.1: Key 2022-23 Budget policy measure trends for the general government sector[8]



$3.4 billion

New investing expenditure initiatives

$2.1 billion higher than initiatives in 2021-22 Budget

$2.9 billion

New operating expenditure initiatives

$1.2 billion higher than initiatives in 2021-22 Budget

$20 million

Decrease in revenue from new revenue measures

[8] 2022-23 Budget figures reflect the period 2021-22 to 2025-26 and 2021-22 Budget figures reflect the period 2020-21 to 2024-25.

3.2 2022-23 Budget objectives and assumptions

3.2.1 2022-23 Budget aims to deliver the new SA Government's election commitments in a fiscally sustainable manner

The 2022-23 Budget aims to deliver the commitments that the SA Government, then in Opposition, announced during the March 2022 State election. It indicates that the SA Government has made a substantial investment in health services to fund its health priorities and deliver its promises of a better health system for all South Australians.

The 2022-23 Budget also notes that the SA Government is committed to implementing its election policies in a fiscally sustainable manner and has introduced a number of new savings measures, including seeking operating efficiencies in non-frontline services.

The current SA Government has retained the fiscal targets of the previous government. Sections 4.4.1, 4.6.2 and 5.4.5 provide further details on the SA Government's performance against these targets.

3.2.2 Considerable uncertainty continues for economic and budget forecasts

The 2022-23 Budget notes that the COVID-19 pandemic and resulting restrictions had a significant impact on the economy and the State Budgets in 2020-21 and 2021-22. With the current high levels of vaccination in Australia, the reopening of international borders and a minimal level of public restrictions, the impact of COVID-19 on the State Budget is expected to reduce in 2022-23. At the time the Budget was prepared, the COVID-19 impact in 2022-23 was expected to be focused on ensuring the health system has the capacity to respond to current variants.

The 2022-23 Budget notes that Australia's economy continues to perform very strongly, with historically low unemployment levels supported by the re-opening of the international border and a gradual easing of restrictions on business activity across the country. The outlook is for further moderate growth, but this will be against a backdrop of several risk factors.

Figure 3.2: Economic risk factors for 2022-23 Budget

The 2022-23 Budget highlights the following risk factors:

- Rising inflation and interest rates, exacerbated by Russia's invasion of Ukraine and continued global supply chain disruptions, placing pressure on the financial sustainability of governments.
- COVID19 The emergence of new, more virulent or vaccine-resistant variants of COVID-19 that may require further restrictions on public activity, negatively affecting private consumption and investment.
- Continued low growth in household income and its impact on household consumption, particularly given high levels of household debt and likely further interest rate rises.
- The pace at which international tourism and education can return to pre-pandemic levels.
- The ability to deliver significant public sector infrastructure investments due to sector capacity constraints.
- Agricultural output being subject to significant climate variability.

The ongoing and emerging impacts of COVID-19, rising inflation and international conflict mean there is an increased risk that actual results will differ from Budget estimates. In the few months since the 2022-23 Budget was released, there have been significant new waves of COVID-19 infections and hospitalisations in South Australia[9] and several increases in RBA interest rates,[10] the war in Ukraine has continued and global economic forecasts have been revised downwards.[11] These emerging trends and events may place upward pressure on health expenditure, interest expenses and operating and investing expenditure.

3.2.3 2022-23 Budget assumes forecast economic outcomes will prevail in the face of the assessed risks

DTF advised us that the economic forecasts prepared for the Budget are based on the latest available data and a balanced judgement on the likely future trajectory for a range of interrelated economic variables. This judgement incorporates an assessment of short and medium-term risks to the end of the forward estimates (ie 2025-26).

DTF also indicated that at the time of the Budget, inflation was in the very early stages of rising from previously longstanding low rates. However, the magnitude of the rise in

---

9 SA Health COVID-19 dashboard, viewed 1 September 2022, <https://www.sahealth.sa.gov.au/wps/wcm/connect/public+content/sa+health+internet/conditions/infectious+diseases/covid-19/response/latest+updates/covid-19+dashboard>.

10 The RBA cash rate target effective at the time of the 2022-23 Budget release on 2 June 2022 was 0.35%. This rate has increased to 2.6%, effective 5 October 2022, <https://www.rba.gov.au/statistics/cash-rate/>.

11 The 2022-23 Budget refers to the International Monetary Fund's April 2022 World Economic Outlook, which forecast growth in advanced economies of 3.3% in 2022. The July update revises the forecast for growth in advanced economies down to 2.5% in 2022. This includes revising forecast growth for Australia in 2022 down by 0.4% to 3.8%. International Monetary Fund 2022, *World Economic Outlook Update, July 2022: Gloomy and more uncertain*, viewed 15 August 2022, <https://www.imf.org/en/Publications/WEO/Issues/2022/07/26/world-economic-outlook-update-july-2022>.

inflation, its duration, and the timing and extent of potential policy responses to combat inflation were unknown.

DTF considers the potential impacts of risks associated with COVID-19, rising inflation and the Ukraine war to be potentially significant but highly uncertain. These risks form part of the back-drop to economic forecasts, however explicit allowances have not been factored into the forecasts and projections across the forward estimates. DTF's judgement at the time of the 2022-23 Budget was that the main drivers of economic outcomes were, on balance, likely to prevail in the face of assessed risks.

The 2022-23 MYBR will provide an update on the evolving budget impacts of these risk factors and also capture impacts from the new Commonwealth Government's revised 2022-23 Budget, which is planned for release on 25 October 2022. The SA Government does not currently have a scheduled release date for the 2022-23 MYBR, but it is usually issued in December of each year.

3.2.4 2022-23 Budget assumes COVID-19 less likely to have major economic impact as it becomes managed at endemic level

In preparing the 2022-23 Budget, DTF assumed that COVID-19 variants are likely to occur in coming years. The virulence of future variants is unknown but potentially serious. Large economy-wide containment measures in response to future outbreaks are possible, but considered less likely to have a major economic impact than in the early stages of the outbreak in 2020 and 2021. Given high rates of vaccination, it is less likely that widespread public health restrictions on economic activity will be required.

The 2022-23 Budget sets out the additional resources provided to agencies for costs related to COVID-19 and the expected time-limited nature of those additional measures. The most resources were provided to SA Health for COVID-19 public health functions. Section 3.4.2 provides further details on this initiative.

DTF also advised us that since the 2022-23 Budget, the states have agreed to pay 50% of the costs associated with the Pandemic Leave Disaster Payment scheme while mandatory isolation periods remain in effect across the country. This initiative and any updates for impacts associated with any further COVID-19 response measures will be included in the 2022-23 MYBR.

3.2.5 Climate change risks are not specifically factored into economic estimates presented in the 2022-23 Budget

The 2022-23 Budget identifies climate variability as an economic risk factor. DTF advised us that:

- risks associated with climate change can have significant economic consequences, including impacting agricultural output
- the nature of such events, including their frequency, timing and severity, are highly uncertain

- if climate change-related events were to occur, there are likely to be associated adverse economic outcomes of some magnitude.

However, DTF indicated that climate change-related events would not necessarily have a significant impact on annual growth forecasts (for example, the impact of the 2019-20 summer bushfires in the Adelaide Hills and on Kangaroo Island is estimated to have been less than a quarter of a percentage point of annual growth in gross state product), with any such economic impact potentially offset by recovery initiatives. For these reasons, the potential for climate change-related events is not factored into economic forecasts for the forward estimates period presented in the Budget.

3.3 Policy and parameter variations

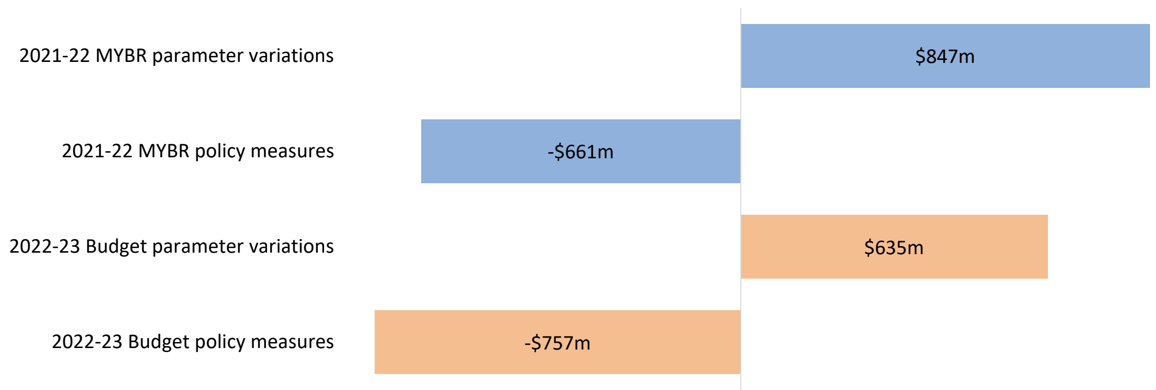
3.3.1 Improved forecast revenues largely offset by expenditure on new policy measures

The Budget Papers include a reconciliation of policy and parameter variations since the 2021-22 Budget for the net operating balance and net lending.[12] This explains differences between the 2021-22 Budget and 2022-23 Budget arising from:

- policy changes – decisions made by the SA Government to increase or decrease taxation, fees and charges and spending
- parameter changes – variations that do not flow from policy choice changes, such as changes in taxation collections owing to economic conditions.

Figure 3.3 shows how policy and parameter variations since the 2021-22 Budget impact net operating balances for the period 2021-22 to 2024-25.

Figure 3.3: Total general government sector net operating balance policy and parameter variations since the 2021-22 Budget[13]



[12] 2022-23 Budget Paper 3 *Budget Statement,* tables 1.5 and 1.6.

[13] Policy measures and parameter variations for the 2021-22 MYBR relate to the previous SA Government, while the measures and variations for the 2022-23 Budget relate to the current SA Government.

Figure 3.3 highlights that improvements in net operating balance forecasts due to parameter variations were largely offset by expenditure on new policy measures. The net impact of all policy and parameter variations since the 2021-22 Budget was to revise total forecast net operating balances for the period 2021-22 to 2024-25 upwards by $64 million.

Parameter variations are mainly due to improved revenue forecasts, offset largely by decreases in Commonwealth major project funding and higher interest expenses, as shown in figure 3.4.

Figure 3.4: Significant parameter variations since the 2021-22 Budget impacting net operating balance (NOB) for general government sector

Parameter variation	Impact on NOB	Key drivers
GST	↑ $1.016 billion	Upward revisions to the national GST pool across all years in the Commonwealth Government's 2022-23 Budget.
State taxation	↑ $1.38 billion	Higher: • payroll tax collections supported by strong labour market conditions • conveyance duties due to strong residential property market activity and prices • gambling taxes owing to higher than expected collections from gaming machines in hotels and clubs.
Commonwealth specific purpose grant revenue	↑ $497 million	Higher: • Commonwealth Quality Schools funding reflecting additional enrolments in the non-government school sector • health funding for creation of additional beds and higher activity levels.
Sales of goods and services	↑ $283 million	Higher land services fees and Lotteries Commission of South Australia gambling revenues.
Commonwealth national partnership grant revenue	↓ $1.088 billion	Adjustments to major project provisions and timing, including deferral of capital project funding.
Interest expenses	↓ $489 million	Higher interest rates on borrowings.

Sections 3.4 and 3.5 provide further details on new policy measures in the 2021-22 MYBR and 2022-23 Budget.

3.3.2 Significant new investing expenditure initiatives and large contingency and timing adjustments for existing capital projects

Figure 3.5 shows how policy and parameter variations since the 2021-22 Budget impact net lending balances[14] for the period 2021-22 to 2024-25.

[14] Net lending is used in this Report as an abbreviation of net lending/borrowing (fiscal balance). Figure A.2 provides the definition of this term.

Figure 3.5: Total general government sector net lending policy and parameter variations since the 2021-22 Budget[15]

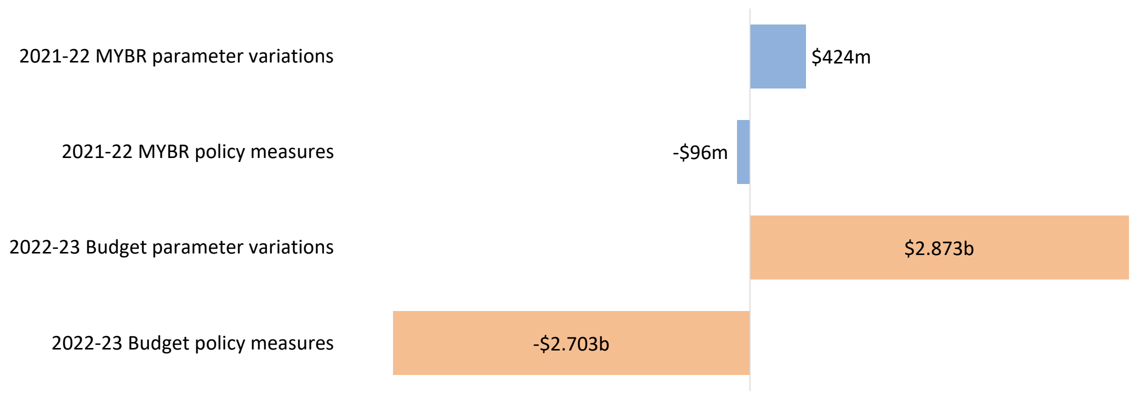


Figure 3.5 highlights that the improvement in net lending balance forecasts due to parameter variations is largely offset by new policy measures.

Total net lending parameter variations are significantly larger in the 2022-23 Budget ($2.873 billion) than they were in the 2021-22 Budget ($969 million). Net lending parameter variations in the 2022-23 Budget mainly reflect investing contingency adjustments and the changed timing of expected investing project expenditure. This includes contingency and timing adjustments for the North-South Corridor River Torrens to Darlington project and new Women's and Children's Hospital.

Sections 5.3 and 5.4 provide further details on the changed timing of the North-South Corridor River Torrens to Darlington project and new Women's and Children's Hospital, and how these projects are expected to impact net debt beyond the forward estimates.

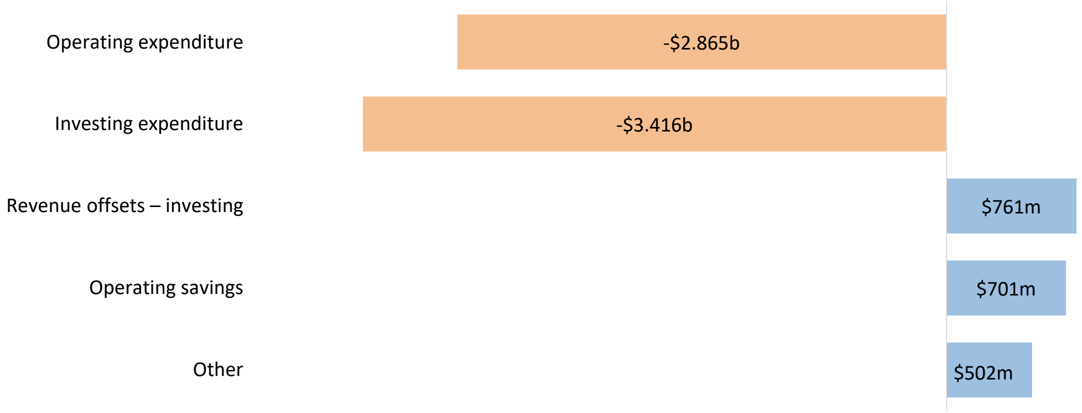
Net lending policy measures in the 2022-23 Budget almost entirely comprise new investing expenditure initiatives and are further detailed in section 3.5.

3.3.3 New operating and investing expenditure policy initiatives significantly higher than 2021-22 Budget

Figure 3.6 provides a breakdown by category of new policy measures in the 2022-23 Budget for the period 2021-22 to 2025-26.

[15] Policy measures and parameter variations for the 2021-22 MYBR relate to the previous SA Government, while the measures and variations for the 2022-23 Budget relate to the current SA Government.

Figure 3.6: New general government sector policy measures in the 2022-23 Budget for period 2021-22 to 2025-26[16]

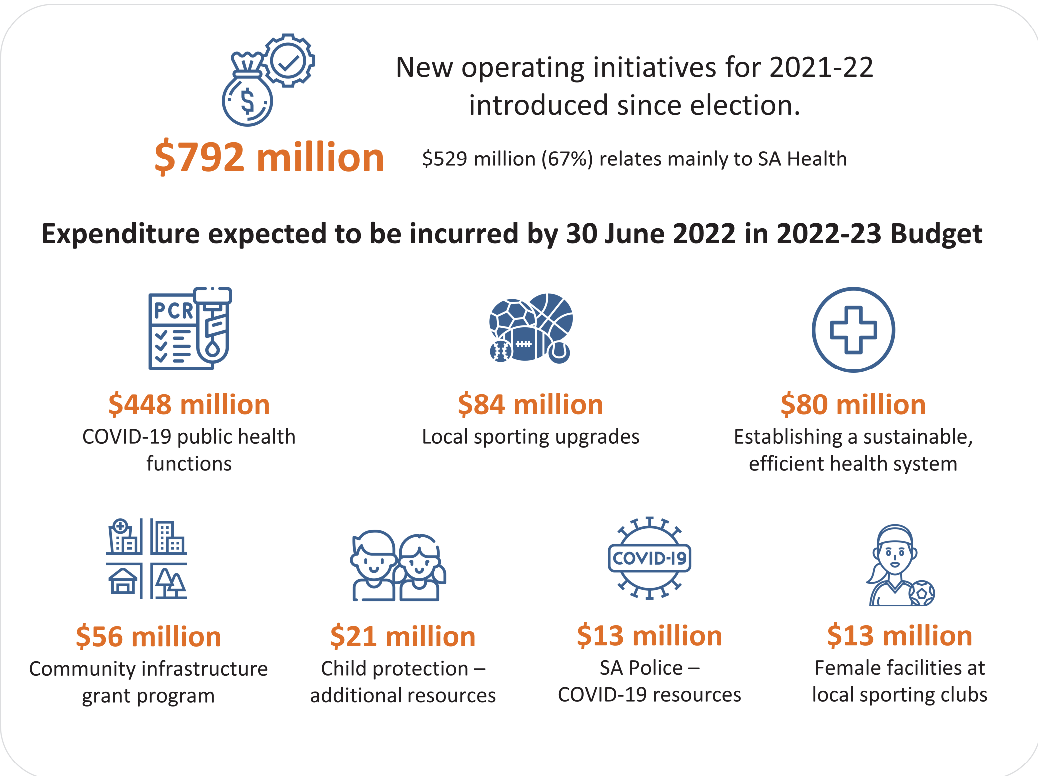


The most significant new budget measures are operating and investing expenditure initiatives. Revenue offsets – investing mainly reflect Commonwealth funding for a portion of the investing expenditure initiatives.

New operating and investing expenditure initiatives in the 2022-23 Budget are significantly higher than in the 2021-22 Budget, with operating expenditure initiatives up by $1.229 billion (75%) and investing expenditure initiatives up by $2.116 billion (263%).

Figure 3.7 shows the new operating expenditure initiatives for 2021-22 introduced by the current SA Government since its election.

Figure 3.7: New general government sector operating expenditure initiatives



16 The ‘other’ category comprises operating expenditure revenue offsets, revenue measures – taxation, revenue measures – other, asset sales and investing savings.

Section 3.4 provides further details on these initiatives.

3.3.4 Annual savings rise to 2.4% of total forecast expenditure in 2025-26 and are targeted towards non-frontline agencies

Savings in the 2022-23 Budget total $1.876 billion. New operating savings ($701 million) and investing savings ($13 million) were introduced in the 2022-23 Budget, in addition to existing savings totalling $1.162 billion from prior year Budgets.

DTF advised us that the savings introduced in the 2022-23 Budget reflect the value announced in the current SA Government's March 2022 election costing document. The savings are a combination of the cessation or scaling back of the former government's programs, the redirecting of some existing agency resources and the removal of unrequired spending provisions, with the balance then allocated as an additional efficiency measure.

Total savings are expected to increase steadily over the forward estimates, rising from $288 million in 2022-23 to $611 million in 2025-26. The savings total in 2025-26 represents 2.4% of total forecast expenditure in that year.

Operating efficiencies in the 2022-23 Budget total $411 million and cover a range of agencies. The most significant operating efficiencies are expected from the:

- Department for Industry, Innovation and Science ($85 million)
- Department for Infrastructure and Transport ($78 million)
- Department of the Premier and Cabinet ($66 million).

No additional savings task has been allocated to health, education, police, child protection, TAFE SA, courts and emergency services. DTF advised us that for the remaining agencies, while a percentage of net cost of services formed the broad basis for apportioning the additional efficiency measure, the final values were adjusted for other savings being asked of agencies and the relative priorities of the SA Government.

The 2022-23 Budget also notes that the savings are an essential component of ensuring a responsible budget and sustainable debt levels in the context of rising interest rates.

DTF advised us that the monitoring of new operating efficiency measures approved as part of the 2022-23 Budget will be included in its 2022-23 quarterly monitoring process. Agencies will be required to identify whether they are on track to deliver budgeted savings. This will be done on a quarterly basis using a traffic light method. Agencies that assign a red traffic light must quantify the size of the expected shortfall in the financial projection and the reason for not being able to meet the savings required.

DTF will engage with agencies who are projecting not to meet their savings task to understand the actions they have implemented to meet it and will report on progress as part of the quarterly monitoring process.

3.3.5 SA Government may face challenges achieving new operating efficiency savings as its savings strategy focuses on non-frontline agencies

DTF advised us that savings reflect the new operating efficiencies approved as part of the 2022-23 Budget or the continuation of ongoing efficiency dividends. The 2022-23 Budget indicates that, except for SA Health, agencies have to date generally achieved these efficiency savings requirements and must continue to find efficiencies to deliver future savings.

Operating efficiency measures are a budget policy tool the government uses to constrain growth in departmental operating funding. It is intended to create budgetary pressure to incentivise departments to seek ways to operate more efficiently.

A well-managed operating efficiency measure should result in at least the same quality and level of services as is currently being provided, but at a lower cost. However, there are some risks associated with efficiency measures. If agencies experience difficulty realising efficiency gains they may reduce expenditure through other means, which can negatively impact workloads, outputs and service quality.

Achieving the target reductions while maintaining current service levels may be a challenge, since about 40% of the State's total expenses are for employees, and these costs are generally subject to annual increases in enterprise bargaining agreements. If expected efficiency gains are not all realised, the SA Government will need to find alternative funding to deliver its budgeted service and infrastructure commitments, or refine, rephase or cease one or more of them.

The successful delivery of savings and maintenance of net operating surpluses may become more challenging if the SA Government's savings strategy continues to focus on non-frontline agencies.[17] This is because they represent less than half of total Budget expenditure and have already implemented a number of operating efficiencies in previous years.

3.3.6 SA Government has more limited options to achieve net operating surpluses without new revenue raising policy initiatives

The 2022-23 Budget notes that it does not include any new taxes or tax increases. The annual indexation factor for fees and charges has been set at 2% for 2022-23, which takes into account annual public sector wages growth and the CPI.

The new revenue policy measures in the 2022-23 Budget are limited and reduce revenue over the period 2021-22 to 2025-26 by $20 million. The new measures mainly relate to the reintroduction of the outer areas registration concession for owners of vehicles ($12 million) and free travel for seniors ($5 million) initiatives.

If prevailing economic conditions do not drive forecast revenue increases and expenditure growth is not constrained, the lack of new revenue policy measures may remove one avenue for achieving net operating surpluses.

---

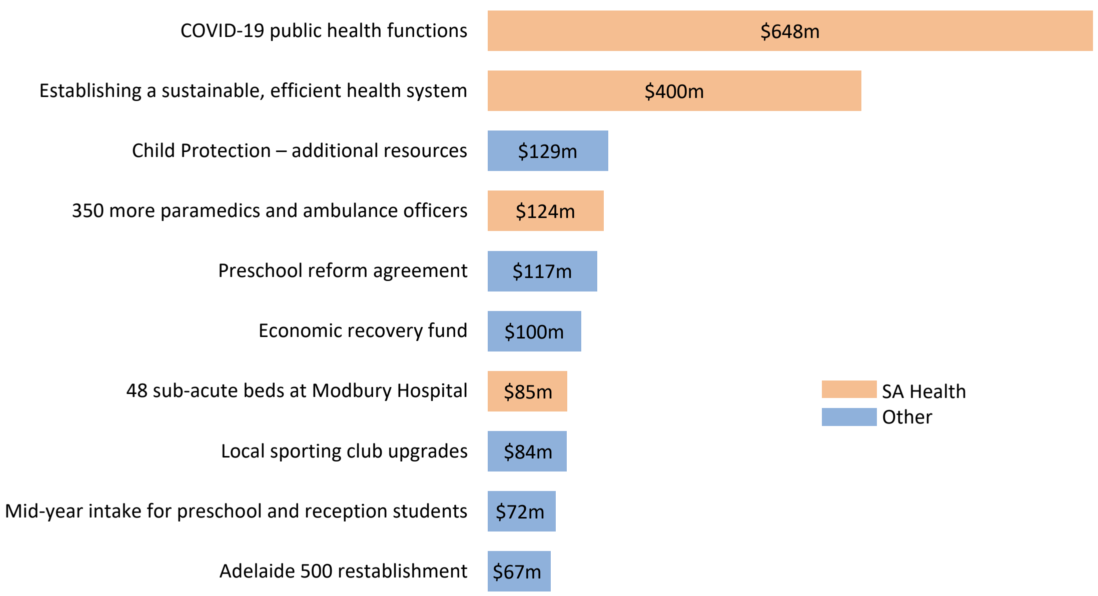
[17] Page 20 of 2022-23 Budget Paper 3 *Budget Statement* states that the SA Government is seeking operating efficiencies in non-frontline services. No additional savings task has been allocated to health, education, police, child protection, TAFE SA, courts and emergency services.

3.4 Operating expenditure initiatives

3.4.1 Over half of new operating expenditure policy initiatives in the 2022-23 Budget are for SA Health

Figure 3.8 shows that several of the most significant new operating expenditure initiatives in the 2022-23 Budget are for SA Health.

Figure 3.8: Major new general government sector operating expenditure measures in the 2022-23 Budget for the period 2021-22 to 2025-26



New SA Health operating expenditure initiatives total $1.514 billion and represent 53% of total new operating expenditure initiatives.

The Commonwealth Government is expected to fund more than half ($342 million) of COVID-19 public health functions under the COVID-19 National Partnership Agreement. It will also largely fund the new Preschool Reform Agreement ($113 million).

3.4.2 SA Health expenditure on COVID-19 response continues to be significant

The COVID-19 public health functions initiative provides additional operating expenditure of $448 million in 2021-22 and $200 million in 2022-23. $204 million was also provided as part of the 2021-22 MYBR to ensure South Australia's health system was COVID-19 ready as restrictions on interstate and international travel were relaxed and removed.

The $648 million COVID-19 public health functions initiative in the 2022-23 Budget recognises the additional expenditure incurred by SA Health for required measures to respond to the impacts of the Omicron variant, including:

- supporting SA Pathology's increased testing capacity, the state control centre and the emergency information call centre

- supporting the vaccination program
- opening additional public hospital beds and virtual care services
- the provision of the rapid antigen test program.

The 2022-23 Budget notes the continuing need for certain COVID-19 functions into 2022-23, albeit at a reduced level, as South Australia moves to the next phase of living with COVID-19. Functions that will continue into 2022-23 include making sure that hospitals have sufficient capacity to support COVID-19 patients and the potential demand pressures through the winter flu season, continuing PCR and rapid antigen testing capacity, and resourcing for SA Health's Communicable Diseases Control Branch.

DTF advised us that, in response to emerging COVID-19 impacts since the release of the 2022-23 Budget, the SA Government has provided additional operating expenditure funding in 2022-23:

- to manage the winter surge in COVID-19 cases, the expansion of eligibility to a fourth vaccine dose and revised plans to increase testing and clinical support services ($20 million)
- for a further 107 temporary private sector beds to provide further system capacity to address the immediate winter period, and 24 additional beds at Regency Green to support the discharge of people from public hospital ($18 million).

It is estimated that approximately $17 million of this expenditure will be funded by the Commonwealth Government.

It is DTF's view that the pandemic continues to evolve and its impacts are difficult to predict, with any further responses beyond the above being considered by the SA Government as needed.

3.4.3 SA Health did not achieve its 2021-22 savings target and continues to have its saving targets reduced

Figure 3.9 shows the revised SA Health savings target reflected in the 2022-23 Budget, as advised by DTF.

Figure 3.9: Summary of SA Health's revised savings targets

	2021-22 $million	2022-23 $million	2023-24 $million	2024-25 $million	2025-26 $million
2021-22 Budget savings target	**80**	**160**	**240**	**320**	**320**
Adjustment to savings target – Establishment of a sustainable, efficient health system initiative	-80	-80	-80	-80	-80
2022-23 Budget savings target	**-**	**80**	**160**	**240**	**240**

SA Health's savings target totals $720 million over the four years of the 2022-23 Budget.

The 2022-23 Budget notes that the SA Government supports the overall objective of seeking to improve the efficiency of our health system and deliver public hospital services at the national efficient price.[18] This is consistent with the objective set by the previous SA Government in the 2021-22 Budget.

SA Health did not achieve its 2021-22 savings target. DTF advised us that SA Health faced significant operational pressures throughout the year, including the ongoing response to the COVID-19 pandemic.

The establishment of a sustainable, efficient health system budget measure provides $400 million between 2021-22 and 2025-26 to reduce SA Health's savings targets by $80 million per annum, as recent significant increases in the national efficient price[19] mean that less savings are now required overall to achieve this objective. The aim is for SA Health to deliver services at the national efficient price by 2024-25. This is consistent with the targeted timeline set in the 2021-22 Budget.

DTF also advised us that SA Health provided it with an update on how the health system is tracking compared to the national efficient price in April 2022. The 2019-20 financial year data is the most recently completed data set available. SA Health advised that it is estimated to have operated at approximately 118% of the national efficient price overall in 2019-20. SA Health notes that the national efficient price is set prior to the start of each financial year, and that all jurisdictions operated above the national efficient price in 2019-20.

The total amount allocated to the establishment of a sustainable, efficient health system budget measure since the 2018-19 Budget is now $3.024 billion, as shown in figure 3.10.

Figure 3.10: Sustainable, efficient health system budget measure since 2018-19 Budget

	2017-18 $million	2018-19 $million	2019-20 $million	2020-21 $million	2021-22 $million	2022-23 $million	2023-24 $million	2024-25 $million	2025-26 $million
2018-19 Budget	70	175	183	191	181	-	-	-	-
2018-19 MYBR	-	59	24	-	-	-	-	-	-
2019-20 Budget	-	95	89	89	89	89	-	-	-
2020-21 Budget	-	-	16	227	248	168	94	-	-
2021-22 Budget	-	-	-	93	95	97	93	15	-
2022-23 Budget	-	-	-	-	80	80	80	80	80
Total	**70**	**329**	**456**	**600**	**693**	**434**	**267**	**95**	**80**

18 The national efficient price is a set amount that is used to work out the funding for a public hospital activity. A public hospital service operating at the national efficient price will be able to provide episodes of patient care (on average, across all types of care, as measured using agreed classifications) and other services (including teaching, training and research) at or below the national benchmark price. The Independent Health and Aged Care Pricing Authority (IHACPA) determines the national efficient price for public hospital services through the analysis of data on actual activity and costs in public hospitals. Costing information used to determine the national efficient price is drawn from the National Hospital Cost Data Collection. This data is submitted to IHACPA by states and territories. <https://www.ihacpa.gov.au/about-ihacpa/faqs>.

19 The national efficient price was $5,134 per National Weighted Activity Unit (NWAU) in 2019-20. It has trended upwards since 2019-20, rising from $5,320 per NWAU in 2020-21, to $5,597 per NWAU in 2021-22, and $5,797 per NWAU in 2022-23. This represents a 13% increase in the national efficient price between 2019-20 and 2022-23. The national efficient price for 2022-23 is based on the average cost of public hospital activity in the 2019-20 financial year. Independent Health and Aged Care Pricing Authority 2022, National Efficient Price Determination, viewed 8 September 2022, <https://www.ihacpa.gov.au/health-care/pricing/national-efficient-price-determination>.

$693 million in additional funding has been provided over successive budgets for 2021-22, which represents 8% of SA Health's total estimated 2021-22 expenditure in the 2022-23 Budget ($8.665 billion).

This highlights the significant additional funding the SA Government has had to provide SA Health compared to that initially budgeted, mainly due to SA Health not meeting its budget target of achieving the national efficient price.

3.4.4 SA Health will face challenges reducing total expenses by 6% between 2021-22 and 2022-23

The 2022-23 Budget for SA Health total expenses is $7.715 billion, compared to a 2021-22 estimated result of $8.221 billion.[20] This represents an expected $506 million (6%) decrease in total expenses between 2021-22 and 2022-23.

The 2022-23 Budget indicates that SA Health has incurred substantial additional costs in 2021-22 due to the need to respond to the public health challenges of COVID-19, including the Omicron variant. These functions and costs are expected to reduce substantially in 2022-23 as COVID-19 is managed at an endemic level, with additional functions phased out by the end of 2022-23. The COVID-19 public health functions initiative provides $448 million in funding in 2021-22, compared to a reduced $200 million in 2022-23.

Achieving expenditure constraint presents a significant challenge for SA Health in 2022-23, given ongoing COVID-19 impacts, inflationary pressures on health costs and not achieving its savings targets for several years.[21] As SA Health represents such a significant proportion of the SA Government's total budget (33% of total expenses), this may put forecast net operating balance surpluses in the 2022-23 Budget at risk.

Further details on SA Health's 2021-22 budget performance are provided in the section of Part C of my 2021-22 Annual Report titled 'Health sector overview'.

3.4.5 Department for Child Protection has required funding for additional resources in recent budgets

The 2022-23 Budget provides $129 million to the Department for Child Protection (DCP) for additional resources, indicating that this reflects more children and young people in non-family based care in 2021-22 and 2022-23, and the expected higher growth of children and young people in care over the forward estimates.

Since the 2018-19 Budget, funding totalling $471 million[22] has been provided to DCP for additional resources through operating expenditure policy initiatives. DCP advised us that the average annual growth in children and young people in care over the past five years has

---

[20] The 2021-22 estimated result for SA Health is based on table 2.6 in 2022-23 Budget Paper 3 *Budget Statement*.

[21] Auditor-General's Report 8 of 2021 *State Finances and related matters,* pp. 20-22.

[22] This reflects total operating expenditure policy initiatives for additional resources over the forward estimates period in the 2018-19 Budget ($31 million), 2018-19 MYBR ($34 million), 2019-20 Budget ($27 million), 2020-21 Budget ($124 million), 2021-22 Budget ($42 million), 2021-22 MYBR ($84 million) and 2022-23 Budget ($129 million).

been 6.7%.[23] Given this recent growth and the fact that DCP has required funding for additional resources in every budget since 2018-19, we expect it will face challenges meeting its operating expenditure targets in the 2022-23 Budget.

Further details on DCP's 2021-22 budget performance are provided in the section of Part C of my 2021-22 Annual Report titled 'Department for Child Protection'.

3.4.6 Economic recovery fund criteria are still being developed

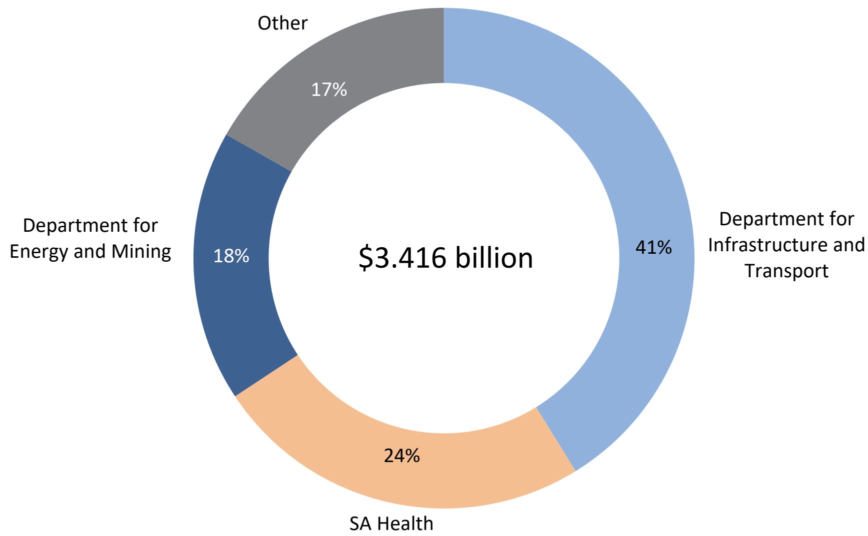
$100 million has been provided for a new Economic Recovery Fund in the 2022-23 Budget to support initiatives that promote economic growth and development opportunities in South Australia. DTF advised us that the specific details and criteria for the Economic Recovery Fund are being developed to ensure it is targeted to achieve the best outcomes for the South Australian economy. No economic modelling or business case analysis has been performed for the Economic Recovery Fund to date.

3.5 Investing expenditure initiatives

3.5.1 Large new investing expenditure initiatives in SA Health and Energy and Mining

New investing initiatives in the 2022-23 Budget total $3.416 billion between 2021-22 and 2025-26. Figure 3.11 shows the breakdown of them by agency.

Figure 3.11: New general government sector investing initiatives by agency



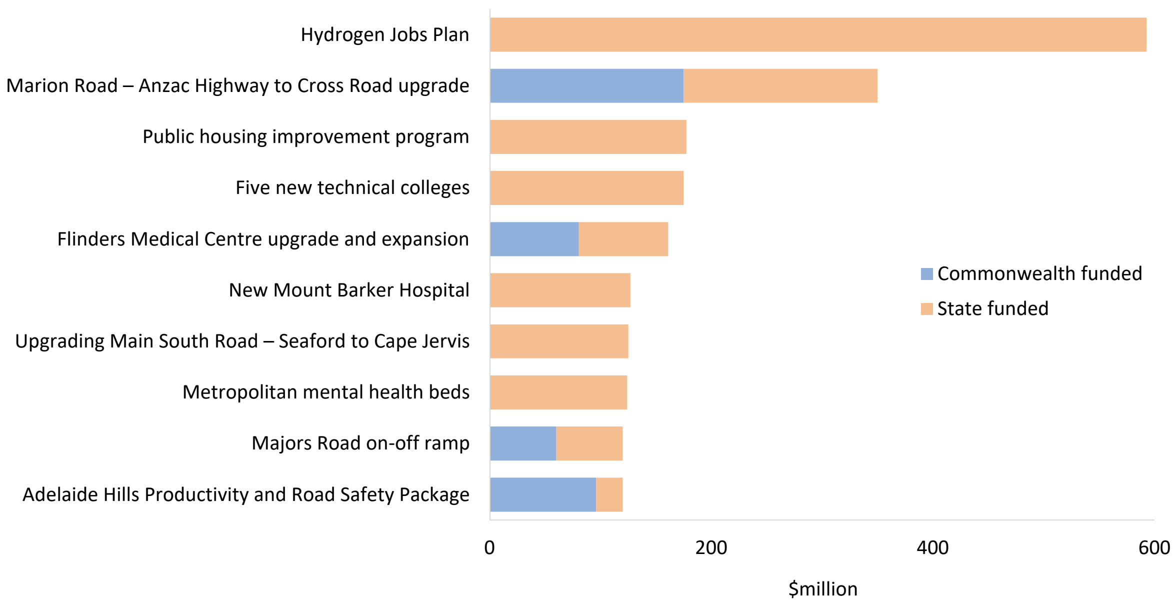
[23] This is based on the average number of children and young people in care in each annual 12-month period between 2017-18 and 2021-22.

Investing expenditure initiatives in the Department for Infrastructure and Transport total $1.407 billion in the 2022-23 Budget compared to $1.047 billion in the 2021-22 Budget, an increase of $360 million. Despite this, the proportion of total investing expenditure initiatives attributable to the Department for Infrastructure and Transport has decreased significantly from 80% in the 2021-22 Budget to 41% in the 2022-23 Budget. This is mainly due to large new investing expenditure initiatives in SA Health and the Department for Energy and Mining.

3.5.2 New hydrogen facility is most significant new investing initiative and its detailed costings are not yet finalised

Figure 3.12 shows the most significant new investing initiatives in the 2022-23 Budget and the Commonwealth Government funding provided for them.

Figure 3.12: Major new investing initiatives in the 2022-23 Budget for the period 2021-22 to 2025-26



The largest new investing expenditure initiative, the Hydrogen Jobs Plan, provides $593 million over the four years of the Budget to establish a new hydrogen facility including electrolyers, a combined cycle turbine plant and a hydrogen storage capacity in the Whyalla region.

DTF advised us that the $593 million capital budget for the delivery of the Hydrogen Jobs Plan was based on independent advice from Frontier Economics, which was commissioned by the then opposition to support the development of the election commitment.

The Office of Hydrogen Power South Australia was established to oversee the delivery of the Plan and is developing detailed project costings in line with the capital budget.

Several of the other significant new investing initiatives focus on road and infrastructure upgrades and many are largely or partly funded by the Commonwealth Government. The Marion Road – Anzac Highway to Cross Road upgrade and Majors Road on-off ramp will be 50% funded by the Commonwealth Government. The Commonwealth Government will also provide 80% of the funding for the Adelaide Hills Productivity and Road Safety Package.

The Flinders Medical Centre upgrade and expansion initiative provides $161 million over four years from 2022-23 to begin the upgrade and expansion of Flinders Medical Centre and upgrades at the Repat Health Precinct. It is expected that the SA Government will partner with the Commonwealth on a 50:50 basis to deliver a total $400 million upgrade and expansion, delivering 160 extra beds for the south of Adelaide.

The 2022-23 Budget also discontinues the construction of a new Riverbank Arena initiative, which was in the previous SA Government's 2021-22 Budget. The 2022-23 Budget notes that this will save $246 million over the four years of the Budget and $662 million in total by 2027-28.

4 Operating statement

Key points

- The 2021-22 estimated net operating balance has deteriorated by $336 million since the 2021-22 Budget to a $1.733 billion deficit, due to range of factors including new expenditure initiatives to respond to COVID-19.
- South Australia is expecting to return to net operating surplus from 2022-23. A key driver of the forecast return to surpluses is limiting growth in expenditure, including a 6.1% expenditure decrease between 2021-22 and 2022-23 as COVID-19 expenditure winds down.
- South Australia continues to be more reliant on Commonwealth grant revenue than any other Australian state, except Tasmania.
- The SA Government expects the new GST distribution arrangements to negatively impact the State's share of the national GST pool from 2027-28 after transitional arrangements cease.
- Wage negotiations are planned to occur for 44% of general government sector employees in 2022-23, which may raise challenges for the SA Government in constraining expenditure growth.

4.1 Overview of key trends

Figure 4.1 shows key operating statement trends in the 2022-23 Budget for the general government sector.

Figure 4.1: Key operating statement trends

	2022-23	2023-24	2024-25	2025-26
Net operating balance	$233 million	$487 million	$606 million	$643 million
	Forecast return to net operating surplus in 2022-23			
Revenue growth	↑ 1.9%	↑ 3.9%	↑ 3.1%	↑ 3.7%
	Average growth of 3.1% per annum over the four Budget years			
Expenditure growth	↓ 6.1%	↑ 2.9%	↑ 2.6%	↑ 3.7%
	Average growth of 0.8% per annum over the four Budget years			

4.2 2021-22 estimated results

4.2.1 The estimated net operating balance has deteriorated by $336 million since the 2021-22 Budget

Figure 4.2 shows that the 2021-22 net operating balance[24] for the general government sector is estimated to have deteriorated by $336 million since the 2021-22 Budget.

Figure 4.2: 2021-22 Budget and estimated result for net operating balance

2021-22 Budget		Estimated result		Increased deficit
$1.397 billion deficit	→	$1.733 billion deficit	=	$336 million

Figure 4.3 summarises the key factors that have contributed to the increased deficit.

Figure 4.3: Key account balances contributing to the variance between the 2021-22 Budget and estimated result for net operating balance

	2021-22 Budget		2021-22 Estimated result
TOTAL REVENUE	$21.9b	▲ 7%	$23.3b
Other grants	$5.8b	▲ 10%	$6.4b
Taxation revenue	$4.8b	▲ 12%	$5.4b

	2021-22 Budget		2021-22 Estimated result
TOTAL EXPENSES	$23.3b	▲ 8%	$25.1b
Other operating expenses	$7.7b	▲ 12%	$8.6b
Grants	$3.5b	▲ 18%	$4.1b

Total expenses are estimated to be higher mainly due to new operating expenditure initiatives for 2021-22 in the 2021-22 MYBR ($511 million) and 2022-23 Budget ($792 million), which primarily relate to the SA Government's COVID-19 response. Section 3.4.2 provides further details.

The estimated increase in total expenses is partly offset by upward revisions to Commonwealth grant revenue ($684 million) and higher taxation revenue ($556 million) mainly due to higher estimated conveyance duty collections of $395 million.

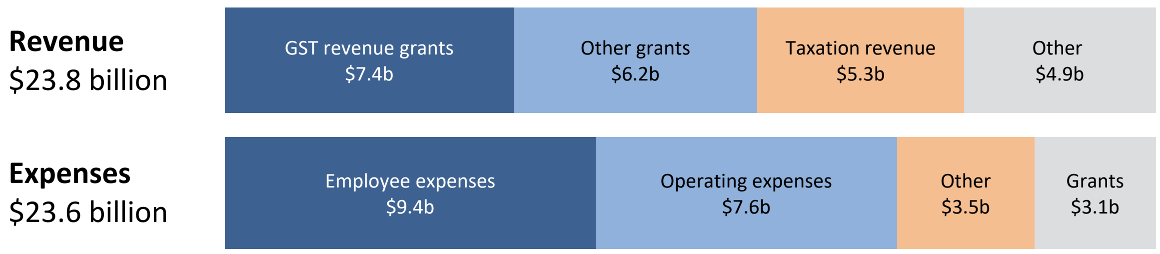
[24] The net operating balance is the net result of revenue and expenses from transactions. It is a summary measure of the sustainability of operations that shows whether the SA Government has to borrow money to cover operating activities. If this measure is in surplus, operating revenue is sufficient to fund operating expenses.

4.3 Operating statement overview

4.3.1 Grants and taxation represent 79% of total revenue while employee and operating expenses comprise 72% of total expenses

Figure 4.4 shows the main components of total general government sector revenue and expenses for the 2022-23 budget year.

Figure 4.4: Main components of total general government sector revenue and expenses in 2022-23 budget year



Budgeted revenue in 2022-23 primarily comprises grants (57%) and taxation revenue (22%). Payroll tax, property taxes, conveyance duty and motor vehicle taxes make up 79% of taxation revenue.

Employee and operating expenses make up 72% of total budgeted expenses. Operating expenses include supplies and services, consultancies, contractors, National Disability Insurance Scheme contributions, and repairs and maintenance expenses.

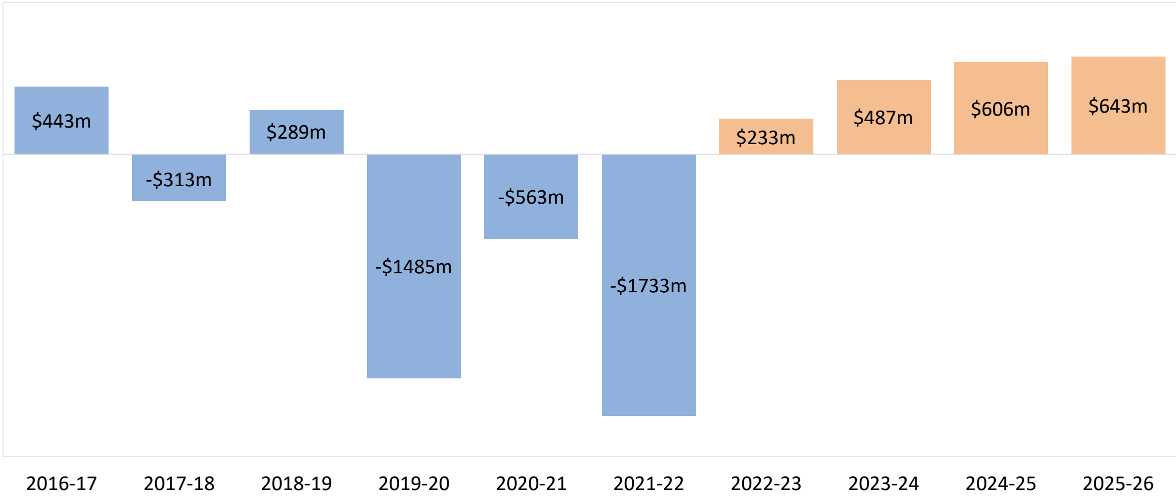
4.4 Net operating balance

4.4.1 The fiscal target of achieving a net operating surplus every year is expected to be met from 2022-23

The new SA Government has retained the fiscal target of achieving a net operating surplus in the general government sector every year, to enable the funding of operating expenditures from operating revenues.

Figure 4.5 shows the actual outcomes for the general government sector net operating balance for the period 2016-17 to 2020-21, the estimated result for 2021-22 and the expected outcomes for the four years of the 2022-23 Budget.

Figure 4.5: General government sector net operating balance for the period 2016-17 to 2025-26



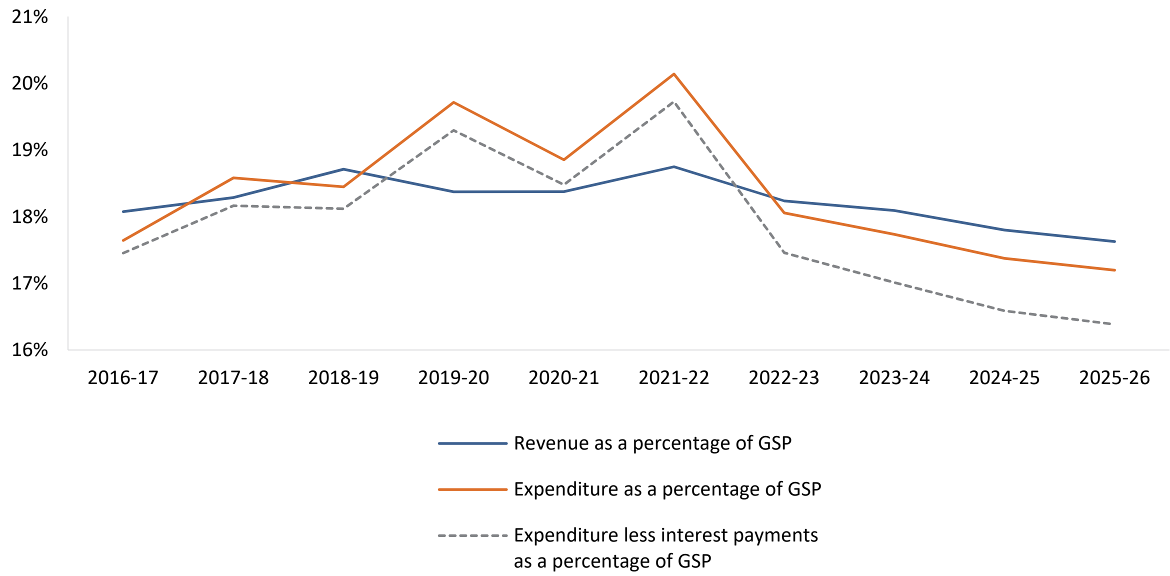
The Budget is expected to return to a modest surplus of $233 million in 2022-23 following significant deficits from 2019-20 to 2021-22.

While the 2022-23 Budget notes that it is anticipated that the impact of COVID-19 on the economy and State finances will be reduced in 2022-23, some greater than usual uncertainty remains for the global, national and State economic outlook. There are a number of risk factors that might prevent a return to surplus in 2022-23. Sections 3.2.2 and 3.2.3 provide further details on these risks.

4.4.2 Limiting growth in expenditure is a key driver of the return to net operating surpluses

Figure 4.6 shows revenue and expenditure for the general government sector as a percentage of gross state product (GSP) from 2016-17 to 2025-26. It also shows expenditure less interest payments as a percentage of GSP.

Figure 4.6: General government sector revenue and expenditure as a percentage of GSP



Source: Audit calculation based on 2022-23 Budget Paper 3 *Budget Statement* and information provided by DTF.

The forecast return to net operating surplus in 2022-23 largely relies on limiting the growth in expenditure rather than revenue growth. Expenditure as a share of GSP is forecast to fall from a high of 20.1% in 2021-22 to 17.2% by 2025-26. Revenue as a share of GSP is also expected to fall over this period but at a slower rate than expenditure.

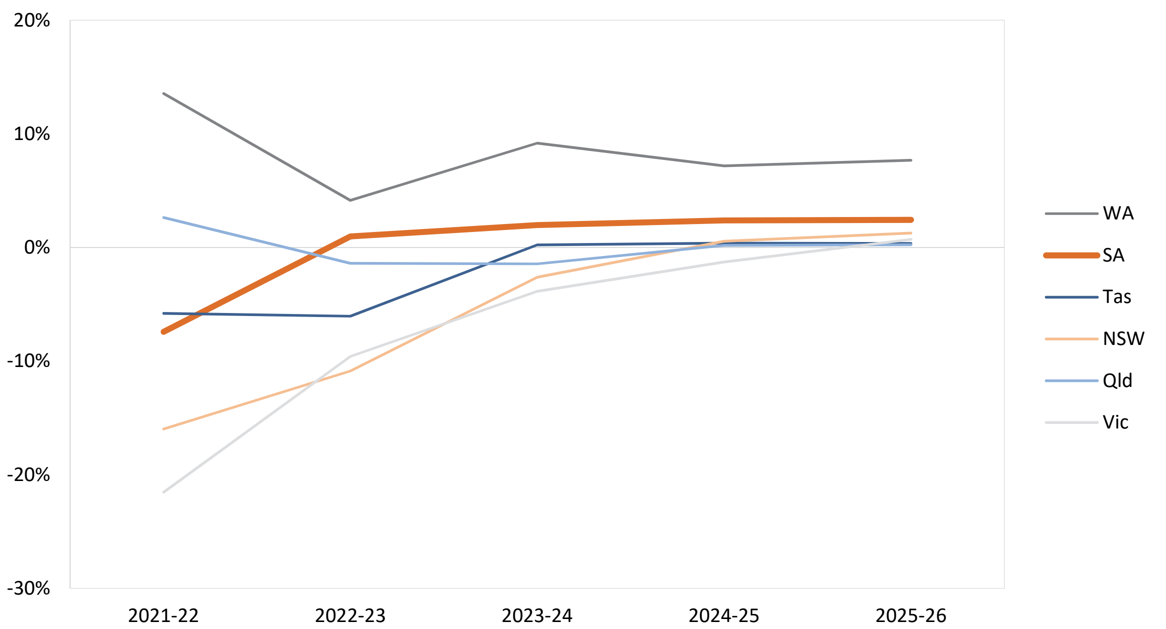
The 2022-23 Budget notes that the fall in expenditure as a share of GSP is expected to occur as measures that respond to COVID-19 phase out and expenditures return to sustainable levels. The extent of the estimated reduction is even more evident for expenses excluding interest payments in figure 4.6. This reflects the increasing proportion of SA Government expenditure that will be spent on interest expenses from rising government borrowings over the forward estimates.

To help constrain expenditure growth over the four years of the Budget, the SA Government has introduced a new measure that seeks operating efficiencies of $701 million in agencies that deliver non-frontline services. This measure is discussed in sections 3.3.4 and 3.3.5. Agencies not achieving these efficiencies and not meeting other existing savings targets may impact the SA Government's ability to achieve a net operating surplus in 2022-23 and across the forward estimates.

4.4.3 South Australia is forecasting a return to net operating surplus earlier than most other states

Figure 4.7 shows the expected trend in general government sector net operating balance as a percentage of total revenue[25] compared to other Australian states for 2021-22 to 2025-26.

Figure 4.7: Net operating balance as a share of total revenue for Australian states between 2021-22 and 2025-26



Source: 2022-23 South Australian and interstate budget papers.

[25] Due to substantial differences in the size of state budgets, net operating balance as a percentage of total revenue has been used to compare net operating balances between states on a comparable basis.

South Australia's net operating balance trend over the four years of the 2022-23 Budget is favourable compared to all states except Western Australia.

South Australia's general government sector net operating balance is forecast to return to surplus in 2022-23 and remain in surplus across the forward estimates. All states are forecast to progressively return to surplus by 2025-26, with South Australia forecast to return to surplus earlier than most other states.

4.5 Revenue

4.5.1 South Australia continues to be more reliant on Commonwealth grant revenue than any other state except Tasmania

South Australia's reliance on Commonwealth grant revenue is expected to range between 57% and 58% of total revenue over the four years of the Budget. Over half of this revenue relates to GST revenue grants.

South Australia continues to be the second most reliant state on Commonwealth grant revenue. This mainly reflects South Australia's more limited ability to generate its own revenue (ie weaker fiscal capacity[26]) compared to most other states, and therefore greater need for Commonwealth revenue to provide public services.

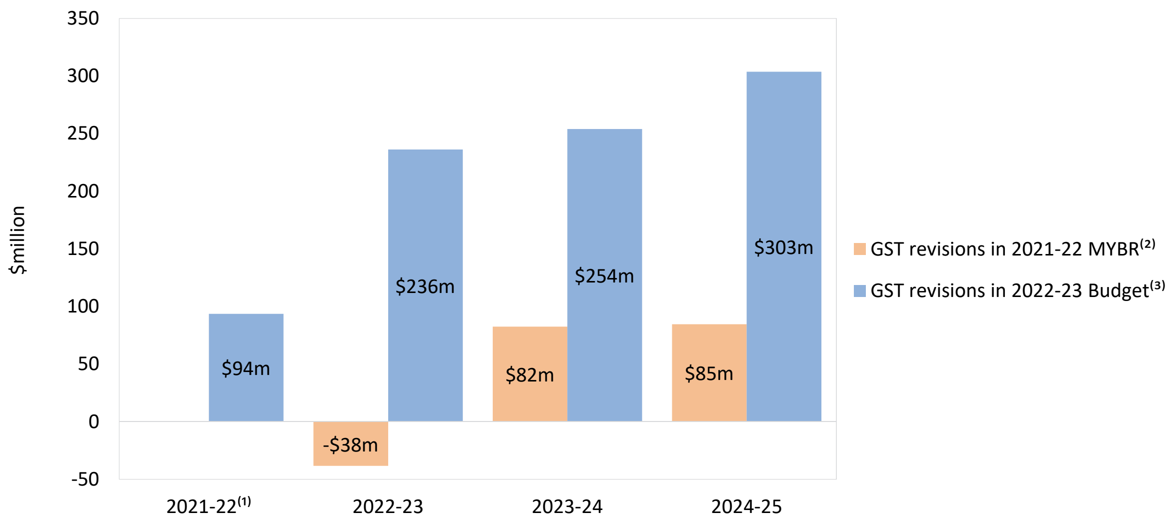
Given the significance of Commonwealth grant revenue to South Australia's revenue base, future trends in Commonwealth grant revenue, and in particular GST revenue, will be critical to the SA Government's ability to generate operating surpluses and pay down its significantly increased net debt.

4.5.2 Estimated total GST revenue revised up by $1.016 billion in the 2021-22 MYBR and the 2022-23 Budget

Figure 4.8 shows that GST revenue has been revised up by a net total of $1.016 billion in the 2021-22 MYBR and 2022-23 Budget.

[26] States have different fiscal capacities due to differences in economic, social and demographic characteristics that affect their expenditure and revenues. Some of the main reasons for the differences are mining production, property sales, taxable payrolls, remoteness, Indigenous status and population growth.

Figure 4.8: GST revenue revisions in the 2021-22 MYBR and the 2022-23 Budget



Total revisions made since the 2021-22 Budget	$94m	$198m	$336m	$388m

(1) GST revenue for 2021-22 was not revised in the 2021-22 MYBR.
(2) Revisions from the 2021-22 Budget included in the 2021-22 MYBR.
(3) Revisions from the 2021-22 MYBR included in the 2022-23 Budget.

GST revenue has been revised up in all years between 2021-22 and 2024-25 in the 2022-23 Budget. GST revisions since the 2021-22 MYBR total $887 million.

4.5.3 GST revenue upward revisions are due to higher forecasts for the national GST pool

Figure 4.9 shows that upward GST revisions in the 2021-22 MYBR and the 2022-23 Budget are due to higher forecasts for the national GST pool, partly offset by the impact of changes to South Australia's GST grant share.

Figure 4.9: Factors contributing to GST revenue revisions in the 2021-22 MYBR and the 2022-23 Budget

Source: Information provided by DTF.

The size of the national GST pool is impacted by the amount of GST collected across Australia and is directly influenced by national trends in consumer spending and housing construction. DTF advised us that in forecasting GST revenues it uses the Commonwealth's estimate of the national GST pool and assumptions for the growth in the national pool.

The Commonwealth Government's 2022-23 Budget indicates that the forecast growth in the national GST pool is mainly driven by:

- expected increases in employment and wages flowing through to higher household spending

- increases from housing construction, partly due to supply chain shortages driving up prices in the construction sector.[27]

4.5.4 South Australia has a significant risk exposure if rising interest rates limit household spending and reduce growth in the national GST pool

GST revenue is a large component of South Australia's revenue base. It is expected to represent 31% of total revenue in 2022-23 and increase to 32.5% in 2025-26.

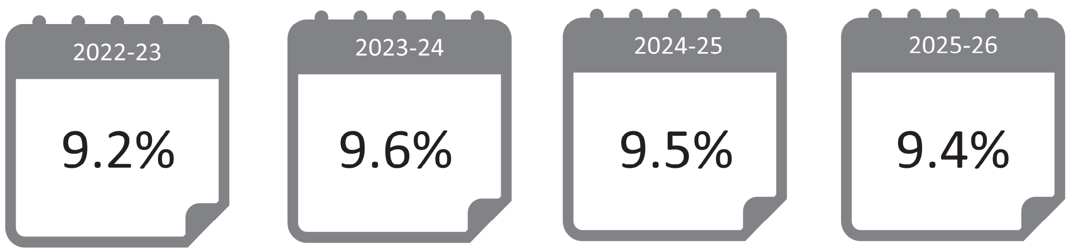
The Budget Papers highlight the importance of GST revenue to the Budget projections and note that the Budget is particularly exposed to changes in growth in the national GST pool. Risk analysis in the Budget indicates that a 1% change in GST pool growth has a revenue impact for South Australia of about $71 million per annum.

Rising interest rates may limit growth in household spending across the country and put forecast growth in the national GST pool at risk.

4.5.5 South Australia's share of the national GST pool is expected to remain relatively stable over the four years of the Budget

Figure 4.10 shows that DTF is not expecting large downward movements in South Australia's share of the national GST pool over the forward estimates.[28]

Figure 4.10: South Australia's estimated GST grants share from 2022-23 to 2025-26



Source: Information provided by DTF. Includes estimated 'no worse off' guarantee payments from the Commonwealth Government.

The estimated grant share for 2022-23 is based on the Commonwealth Grants Commission's (CGC's) relativity determination and the grant shares for the remaining three years are based on DTF's relativity forecasts. While DTF is forecasting that South Australia's grant share is expected to be relatively stable over the forward estimates, actual outcomes may vary. This is because calculating a state's grant share is influenced by many factors including:

- property sales and land values
- royalties received from mining production
- wage costs and payroll tax
- Commonwealth Government payments received for specific purposes

---

[27] Commonwealth of Australia 2022, 2022-23 Budget Paper No. 1, *Budget Strategy and Outlook 2022-23*, viewed 23 August 2022, <https://budget.gov.au/2022-23/content/bp1/index.htm>.

[28] The estimated GST grants share shown in figure 4.10 are calculated using South Australia's GST grants (including estimated 'no worse off' payments from the Commonwealth Government) as a percentage of the national GST pool (including the pool boost from the Commonwealth Government discussed in section 4.5.6).

- population growth rates and characteristics such as age and socio-economic status
- other factors introduced under new GST distribution arrangements (see section 4.5.6).

4.5.6 New GST distribution arrangements expected to negatively impact the State's share of the national GST pool after 2026-27

New arrangements for distributing the national GST pool to the states started in 2021-22 and are being introduced over a six-year transitional period that ends in 2026-27. Figure 4.11 shows key features of the new arrangements and the transition.

Figure 4.11: Key features of new GST distribution arrangements

New equalisation system
States will be equalised based on the fiscal capacity of New South Wales or Victoria (whichever has a higher fiscal capacity each year) instead of being based on the fiscal capacity of the strongest state.

A minimum GST relativity (relativity floor)
If a state's GST relativity is lower than the minimum floor it will receive additional funding through reductions to other states' GST grants. Currently, only Western Australia's GST relativity lies below the floor.

No state will be worse off during the six year transition period
A legislated guarantee for each year up to 2026-27 ensures that, cumulatively, no state will receive a lower GST share than it would have received under the previous distribution arrangement.

The size of the GST pool will be permanently boosted
The Commonwealth Government will provide more funding to permanently boost the size of the GST pool to be distributed.

Source: 2022-23 Budget Paper 3 *Budget Statement.*

Over the four years of the 2022-23 Budget the risk of South Australia's GST revenue share reducing because of the new arrangements is mitigated by the 'no worse off' guarantee.

The main risks during the six-year transitional period remain consistent with those under the previous arrangements, specifically reductions in estimated national GST pool growth and the State's relativity as determined by the CGC each year. When the transition period ends in 2026-27, all states excluding Western Australia will be exposed to a higher risk of lower grant shares. This is because the 'no worse off' guarantee will end.

The 2022-23 Budget notes that South Australia's share of the national GST pool in 2022-23 would be $289 million less under the new GST distribution arrangements if the 'no worse off' guarantee was excluded. The CGC's March 2022 update[29] shows that this impact is mainly due to Western Australia's 2022-23 GST relativity being raised to a minimum floor. This results in Western Australia receiving additional GST grants funded from reductions to other states' GST grants, including South Australia's.

DTF engaged an external firm in February 2022 to analyse the potential impact of the GST

[29] Commonwealth Grants Commission 2022, *GST Revenue Sharing Relativities 2022 Update*, viewed 25 August 2022, <https://www.cgc.gov.au/publications/2022-update>.

distribution changes. It found, for most economic scenarios modelled, that South Australia would be worse off in the final year of the transitional period (ie 2026-27). The 2022-23 Budget notes that this offers a reasonable indicator of the potential ongoing impacts of the new arrangements following the expiry of the 'no worse off' guarantee.

4.5.7 Taxation revenue forecast to decline in 2022-23 due to reduced property market activity and then grow steadily to 2025-26

Taxation revenue is forecast to decline by 1.7% in 2022-23 after significant growth of 10.5% in 2021-22. The 2022-23 Budget notes that this reflects an expected fall in conveyance duty collections following a strong level of property market activity in 2020-21 and 2021-22.

Growth in total taxation revenue of 2.6% is forecast in 2023-24, with average growth of 3.7% per annum forecast in 2024-25 and 2025-26 from expected growth in payroll tax and conveyance duty collections.

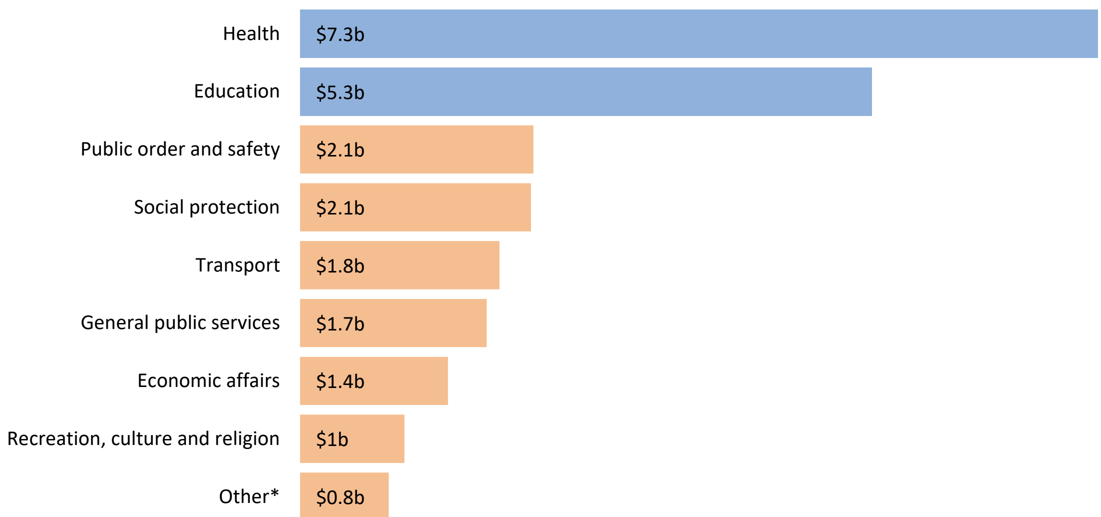
The 2022-23 Budget notes that it includes no new taxes or tax increases. Section 3.3.6 discusses how this might impact the SA Government's delivery of net operating surpluses.

4.6 Expenditure

4.6.1 Health and education sectors comprise just over half of total expenses in the 2022-23 Budget

Figure 4.12 shows the split of 2022-23 Budget expenses by sector and highlights the significance of the health and education sectors for total SA Government expenditure.

Figure 4.12: General government sector expenses by function[30]



* Includes environmental protection and housing and community amenities.

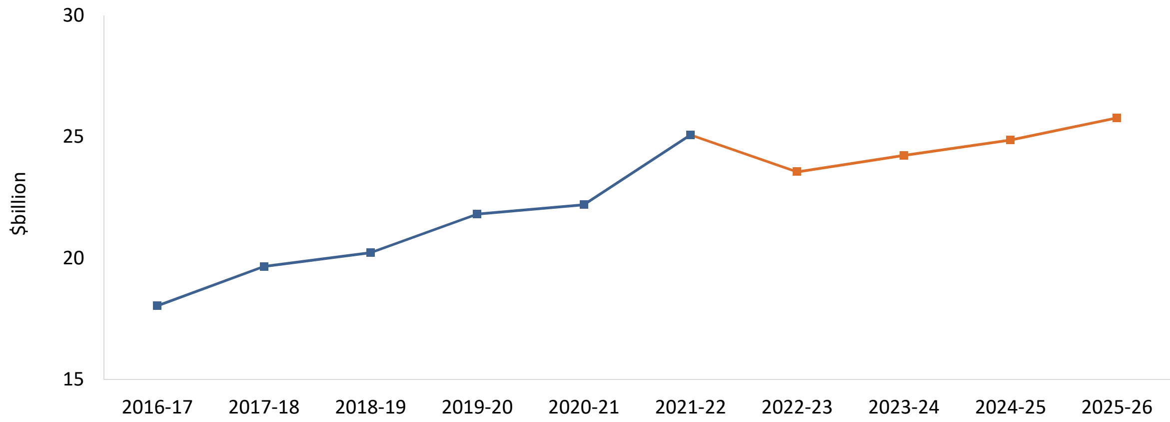
[30] Sourced from 2022-23 Budget Paper 3 *Budget Statement*, table A.13.

Health (31%) and education (22%) sector combined expenses are $12.597 billion, making up just over half of total general government sector expenditure ($23.554 billion).

4.6.2 Total expenses expected to decrease by 6.1% in 2022-23 as COVID-19 expenditure scales back but then steadily grow again over the forward estimates

Figure 4.13 shows trends in total expenses and annual expenditure growth over the four years of the 2022-23 Budget against the experience of the previous six years.

Figure 4.13: General government sector total expenses from 2016-17 to 2025-26



Annual expenditure growth	5.7%	9%	2.9%	7.9%	1.8%	13%	-6.1%	2.9%	2.6%	3.7%

Source: 2022-23 Budget Paper 3 *Budget Statement*, table B.4, and audit calculation.

The SA Government has a fiscal target of limiting the average growth in operating expenditure to trend growth in household income (4% per annum).

The 2022-23 Budget shows average annual expenditure growth of 0.8% over the four years of the Budget. Growth rates are expected to remain below trend growth in household income over the forward estimates, consistent with the SA Government's fiscal target.

Expenses are forecast to decline by 6.1% in 2022-23 as time-limited COVID-19 expenditure winds down and COVID-19 is expected to be managed at an endemic level. The increased growth rates from 2023-24 onward partly reflect:

- higher interest expenses as net debt levels and longer-term interest rates increase
- higher depreciation expenses as projects are completed under the SA Government's infrastructure program.

4.6.3 Total general government sector workforce numbers expected to fall in 2022-23 following recent growth

Total general government sector FTE levels over the first three years of the Budget are expected to fall by an average of 0.7% per annum, then increase by 1.6% in 2025-26. This contrasts with growth of 1.5% in 2020-21 and estimated growth of 3% in 2021-22.

FTEs are projected to fall by 2.1% in 2022-23, from 89,572 to 87,704, mainly due to COVID-19 public health functions being progressively phased out and non-frontline agencies implementing savings measures.

The FTE impact of new policy measures in the 2022-23 Budget is shown in figure 4.14.

Figure 4.14: Estimated FTE impacts of 2022-23 Budget measures

	2022-23 FTE impact	2023-24 FTE impact	2024-25 FTE impact	2025-26 FTE impact
Total FTE impact of new policy measures	**1,026**	**1,105**	**1,289**	**1,434**
SA Health	758	855	1,056	1,402
Education	376	386	406	245
Other agencies	257	250	224	217
Savings measures	(365)	(386)	(397)	(430)

Source: 2022-23 Budget Paper 3 *Budget Statement*, table 2.11, information provided by DTF and audit calculation using data from 2022-23 Budget Paper 5 *Budget Measures Statement*.

The increase in FTEs from 2022-23 Budget policy measures is mostly for new SA Health initiatives. This is offset by an estimate of FTE reductions by non-frontline agencies to meet new savings measures. The SA Government has indicated that it does not require these savings to include FTE reductions and that agencies can pursue a range of options to meet the savings targets, including reducing expenditure in other areas.

If non-frontline agencies reduce expenditure in areas other than FTEs, the growth in FTEs and employee expenses may be higher than forecast over the four years of the Budget.

4.6.4 Wage negotiations may raise challenges for the SA Government in constraining expenditure growth

Salaries and wages are a major public sector operating cost and represent $9.384 billion (40%) of total general government sector expenses in the 2022-23 Budget.

The 2022-23 Budget notes that wage negotiations will start in 2022-23 for major employee groups in the general government sector, as shown in figure 4.15.

Figure 4.15: Employee groups[31] subject to enterprise agreement negotiations in 2022-23

* Other employee groups include visiting medical specialists, wages parity trades, State Theatre Company of SA workshop and props staff and Rail Commissioner tram operations, maintenance and infrastructure employees.

31 The 2022-23 Budget Papers indicate that wage negotiations are continuing for SA Ambulance Service Inc operational employees. DTF advised us that since the 2022-23 Budget these wage negotiations have been completed and a new enterprise agreement approved.

Education staff (including teachers) and nursing and midwifery staff are two major employee groups subject to wage negotiations in 2022-23, with DTF advising us that they comprise 45% of estimated total employee expenses in the 2022-23 Budget.

The 2022-23 Budget indicates that the outcomes of future wage negotiations will be crucial in determining whether expenditure forward estimates in this Budget can be achieved and the planned level of government services can be delivered. Figure 4.16 highlights the significance of the wage negotiations, which are taking place in a period of high inflation.

Figure 4.16: Wage negotiations that are continuing or starting in 2022-23 for general government sector employees

$4.657 billion total estimated wage base

50% of estimated total employee expenses in the 2022-23 Budget

44% of total general government sector employees

$251 million estimated budget impact in 2025-26 if general government sector wage outcomes for new enterprise agreements vary by 1% per annum from allowances in the forward estimates

Source: 2022-23 Budget Paper 3 *Budget Statement* and information provided by DTF.

DTF advised us that the estimated budget impact in 2025-26 increases to $378 million if outcomes vary by 1.5% per annum and $507 million if outcomes vary by 2% per annum.

The 2022-23 Budget provides for anticipated wage increases from enterprise agreement outcomes over the forward estimates, both in individual agency budgets and in the total of the contingency items in DTF's administered items.

5 Balance sheet

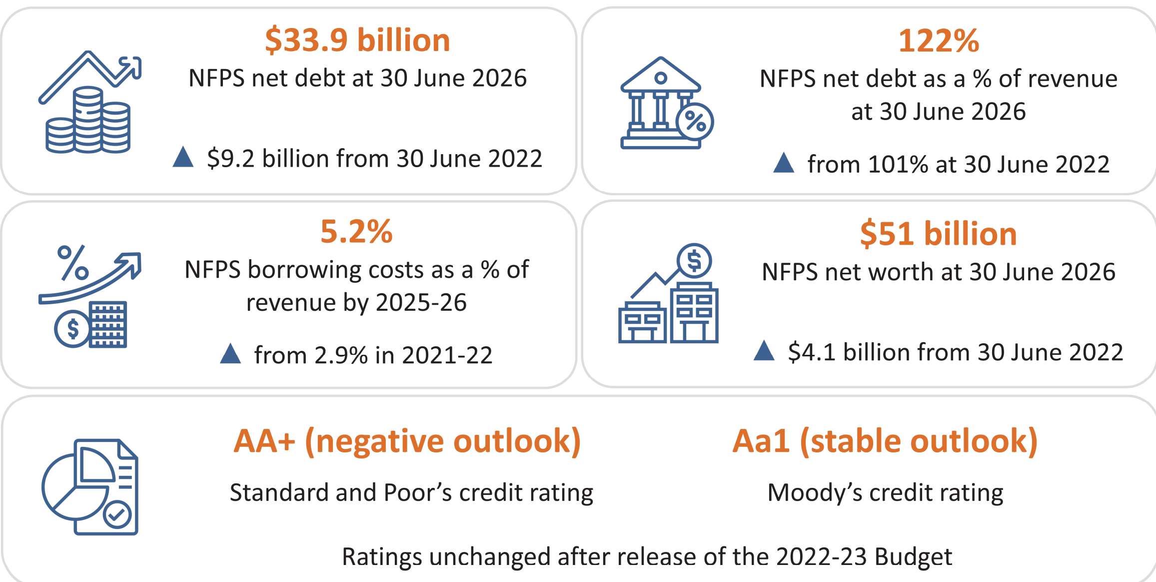
Key points

- The NFPS capital program is $18.6 billion over the four years of the 2022-23 Budget, an increase of $687 million on the four years of the 2021-22 Budget. The expanded capital program will see land and fixed assets increase by $11.7 billion between 2022-23 and 2025-26.
- The SA Government will face significant challenges in ensuring its capital program is completed on time and on budget given capacity constraints, shortages of key building materials and skilled labour, and cost pressures.
- Forecast net debt levels have improved compared to the previous Budget, mainly due to improved revenue forecasts. However, borrowing costs as a percentage of revenue exceed the estimates in the previous Budget.
- The trend in South Australia’s net debt and its ability to fund budgeted expenditure after meeting borrowing costs are generally comparable to other Australian states.
- There is a high likelihood that net debt levels will rise further after the forward estimates period due to substantial planned infrastructure project expenditure and other budget risk factors.
- South Australia’s risk exposure to interest rate rises is significantly increased by higher net debt levels.

5.1 Overview of key trends

Figure 5.1 shows key balance sheet trends in the 2022-23 Budget for the NFPS.

Figure 5.1: Key balance sheet trends in 2022-23 Budget

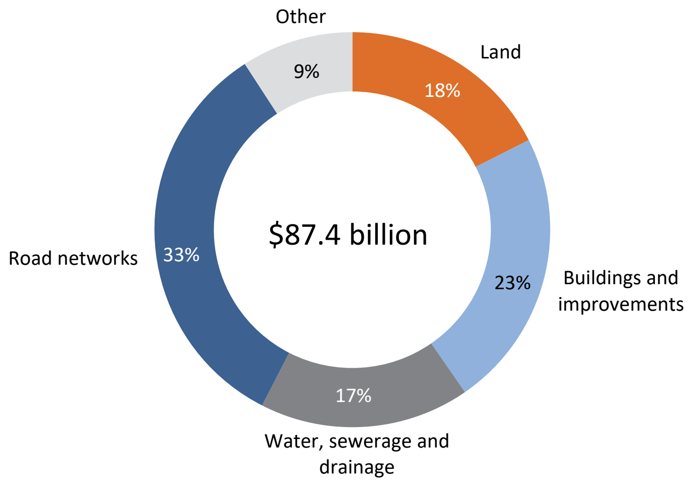


5.2 Balance sheet overview

5.2.1 Land and other fixed assets represent the vast majority of total assets

The vast majority of estimated total NFPS assets at 30 June 2022 are land and other fixed assets (88%).[32] Figure 5.2 shows the composition of land and other fixed assets.

Figure 5.2: Composition of NFPS land and other fixed assets estimated at 30 June 2022

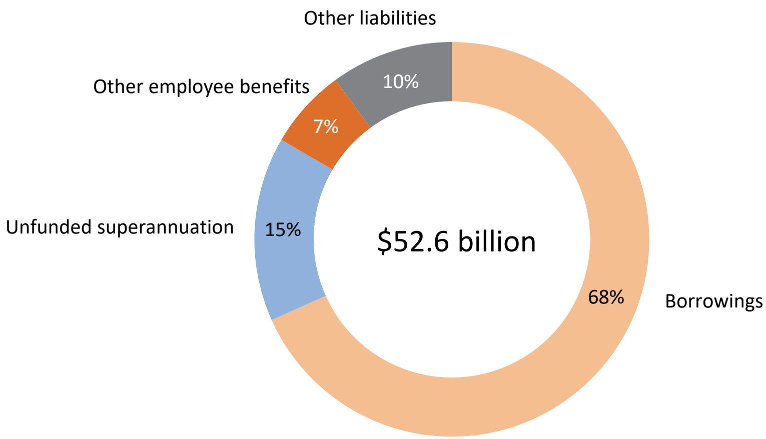


Road networks represent the largest component ($29.11 billion), with the other major components being buildings and improvements ($19.975 billion), land ($15.296 billion) and water, sewerage and drainage assets ($15.013 billion).

5.2.2 Liabilities primarily comprise borrowings and the unfunded superannuation liability

Figure 5.3 shows the estimated composition of total NFPS liabilities at 30 June 2022.

Figure 5.3: Composition of total NFPS liabilities estimated at 30 June 2022



[32] Balance sheet data in this section is for the NFPS unless otherwise stated. The NFPS consolidates the general government and public non-financial corporations (PNFC) sectors.

The major components of total liabilities are borrowings ($35.951 billion) and the unfunded superannuation liability ($7.961 billion).

NFPS borrowings increased from 65% of total NFPS liabilities at 30 June 2021 to an estimated 68% of total NFPS liabilities at 30 June 2022. The increase was principally to fund the significant purchases of non-financial assets ($3.357 billion) in 2021-22.

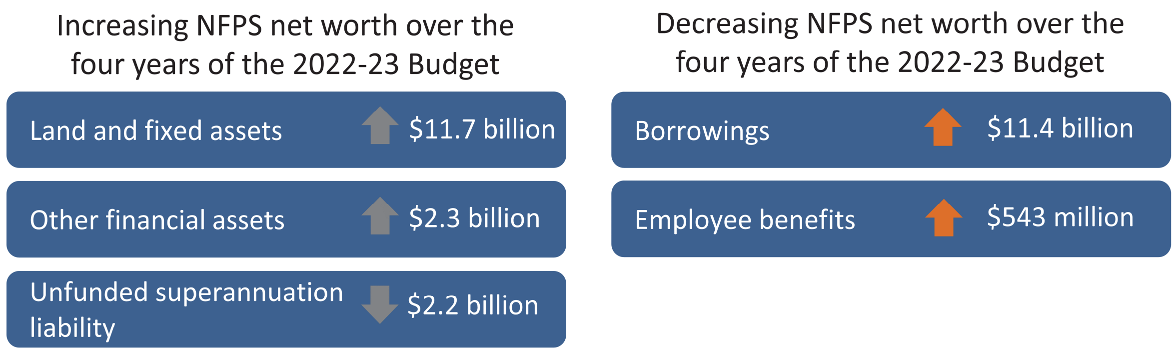
The unfunded superannuation liability is a long-term liability to current and past members of the closed defined benefits superannuation schemes.[33] The liability decreased from 19% of total NFPS liabilities at 30 June 2021 to an estimated 15% of total NFPS liabilities at 30 June 2022.

The 2022-23 Budget reports that the SA Government has a long-term funding strategy in place and is on target to fully fund the State's defined benefit liability by 2034. By then, superannuation assets are projected to be $9.8 billion, fully offsetting projected superannuation liabilities.

5.2.3 Net worth forecast to increase by $4.1 billion over the four years of the 2022-23 Budget

NFPS net worth is expected to increase by $4.138 billion, from $46.827 billion at 30 June 2022 to $50.965 billion at 30 June 2026. Figure 5.4 shows the major drivers of this increase.

Figure 5.4: Major drivers of the increase in NFPS net worth over the four years of the 2022-23 Budget



While NFPS borrowings are projected to increase significantly, they will principally be used to fund the SA Government's capital program, which is reflected in the increase in the value of NFPS land and fixed assets. Commonwealth Government funding for specific capital projects over the forward estimates will also partly fund the SA Government's capital program. Section 3.5.2 provides further details.

[33] The unfunded superannuation liability is calculated in line with Australian Accounting Standards as the net difference between the estimated value of the accrued defined benefits superannuation obligations and the value of the asset set aside to meet these obligations.

5.3 Purchases of non-financial assets

5.3.1 NFPS capital program over the four years of the 2022-23 Budget is $18.6 billion

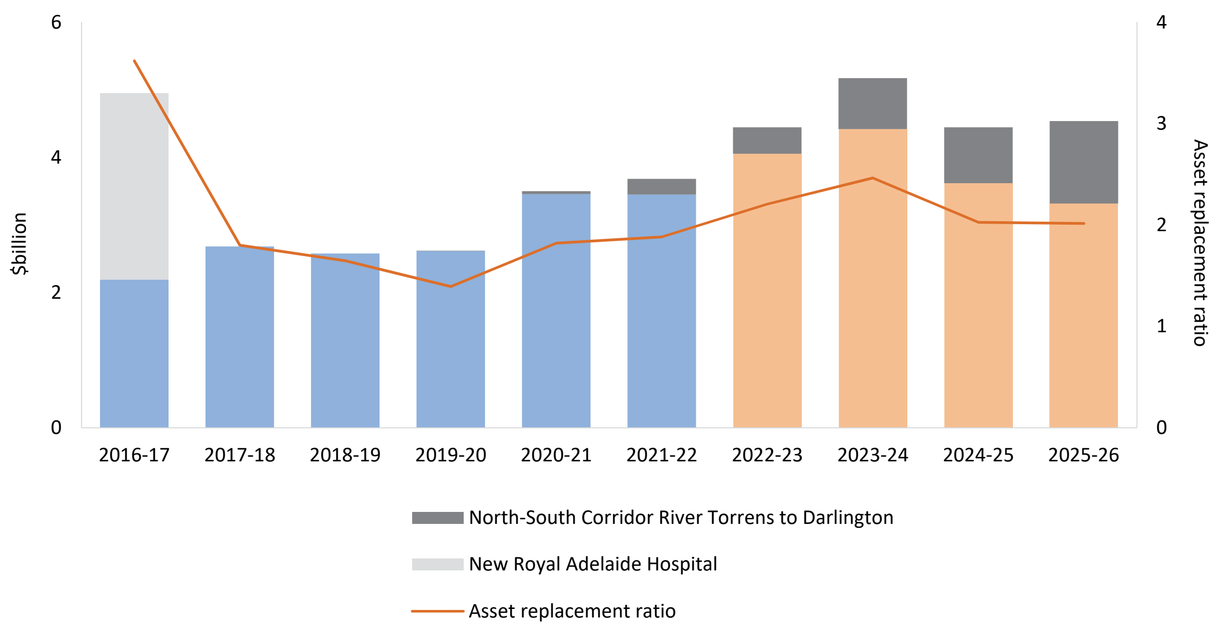
Purchases of non-financial assets for the NFPS are projected to total $18.596 billion over the four years of the 2022-23 Budget, compared to $17.909 billion over the four years of the 2021-22 Budget.

The 2022-23 Budget indicates that the SA Government's investing program is focused on building key economic and social infrastructure, improving existing facilities and supporting job creation. It includes:

- $3.4 billion in new general government sector investing initiatives (see section 3.3.3 for details of these initiatives)
- investing expenditure of $3.2 billion for the North-South Corridor River Torrens to Darlington project and $1.4 billion for the new Women's and Children's Hospital.

Figure 5.5 shows the purchases of non-financial assets for the NFPS over the 10 years to 2025-26 compared to the asset replacement ratio.[34]

Figure 5.5: NFPS purchases of non-financial assets from 2016-17 to 2025-26



[34] The asset replacement ratio compares capital expenditure to depreciation to assess whether assets are being consumed at a rate consistent with their replacement. Ratios higher than 1:1 indicate that assets are being replaced faster than they are consumed.

Figure 5.5 shows that purchases of non-financial assets for the NFPS over the four years of the 2022-23 Budget are substantially larger than prior years. It also shows that the North-South Corridor River Torrens to Darlington project forms an increasingly significant component of the NFPS purchase of non-financial assets over the forward estimates period.

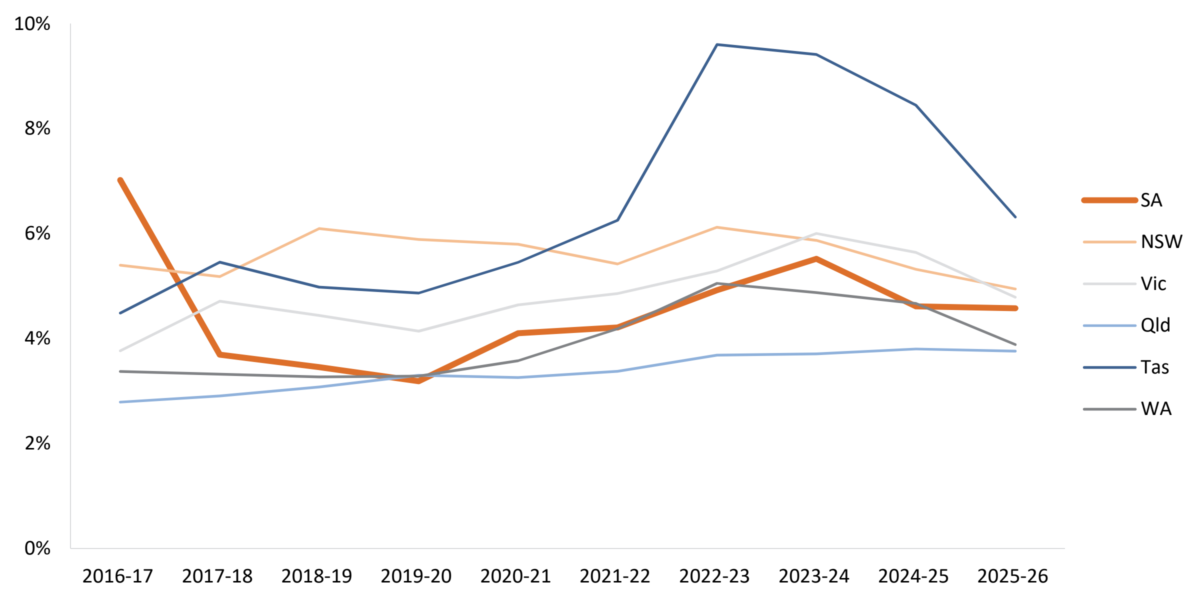
The one-off large increase in 2016-17 was mainly due to the recognition of the new Royal Adelaide Hospital finance lease asset ($2.758 billion), which represented 56% of total NFPS purchases of non-financial assets in that year.

Figure 5.5 also highlights that since 2019-20 the asset replacement ratio has generally been trending higher. It ranged between 1 and 2 for the period 2017-18 to 2021-22 and rises to 2 or higher between 2022-23 and 2025-26. This indicates that the SA Government has spent or expects to spend more on replacing and renewing assets each year than the consumption of assets through depreciation.

5.3.2 South Australia's planned capital program as a percentage of its asset base is largely consistent with most other states

Figure 5.6 compares the SA Government's NFPS capital program as a percentage of its land and fixed assets to other Australian states over the 10 years to 2025-26.

Figure 5.6: South Australia's NFPS net purchase of non-financial assets as a percentage of its land and fixed assets compared to other Australian states from 2016-17 to 2025-26



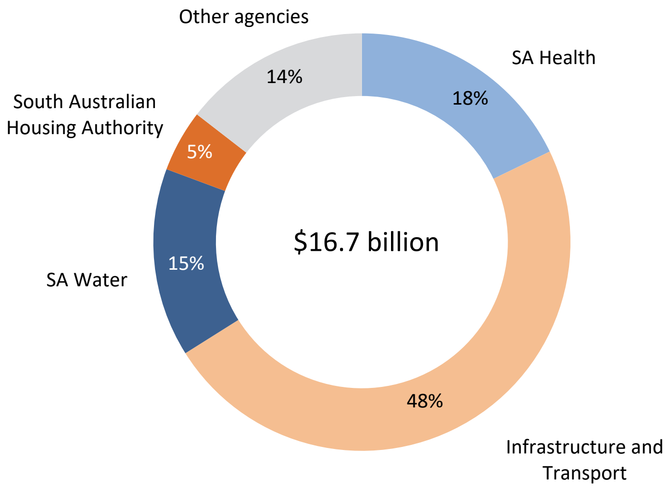
Source: South Australian and interstate budget papers and financial reports.

Figure 5.6 highlights that in 2022-23 each state's NFPS capital program as a percentage of its land and fixed assets base increases from that in 2021-22. It also highlights that the SA Government's annual NFPS capital program as a percentage of its land and fixed assets base over the four years of the 2022-23 Budget is largely consistent with most other states, averaging 4.9%.

5.3.3 Department for Infrastructure and Transport, SA Health and the South Australian Water Corporation have the largest capital programs

Figure 5.7 provides a breakdown of the capital program by agency over the four years of the Budget.

Figure 5.7: Breakdown of NFPS capital program by agency[35]



A large proportion of the capital program over the four Budget years is attributable to the Department for Infrastructure and Transport (DIT) ($8.072 billion), SA Health ($2.990 billion) and SA Water ($2.449 billion). The South Australian Housing Authority ($802 million) also has a significant capital program.

The NFPS capital program also includes $1.893 billion over the four years of the 2022-23 Budget that has not been allocated to agencies (10% of the total NFPS capital budget). This mainly comprises contingency provisions that are allocated to specific investing projects and general contingencies. The portion allocated to general contingencies provides the SA Government with some flexibility over the nature and timing of its investing program.

The portion of the capital budget not allocated to agencies has declined from $6.972 billion over the four years of the 2021-22 Budget to $1.893 billion over the four years of the 2022-23 Budget. This is primarily due to the transfer of contingency amounts for the North-South Corridor River Torrens to Darlington project and the new Women's and Children's Hospital to agency budgets.

---

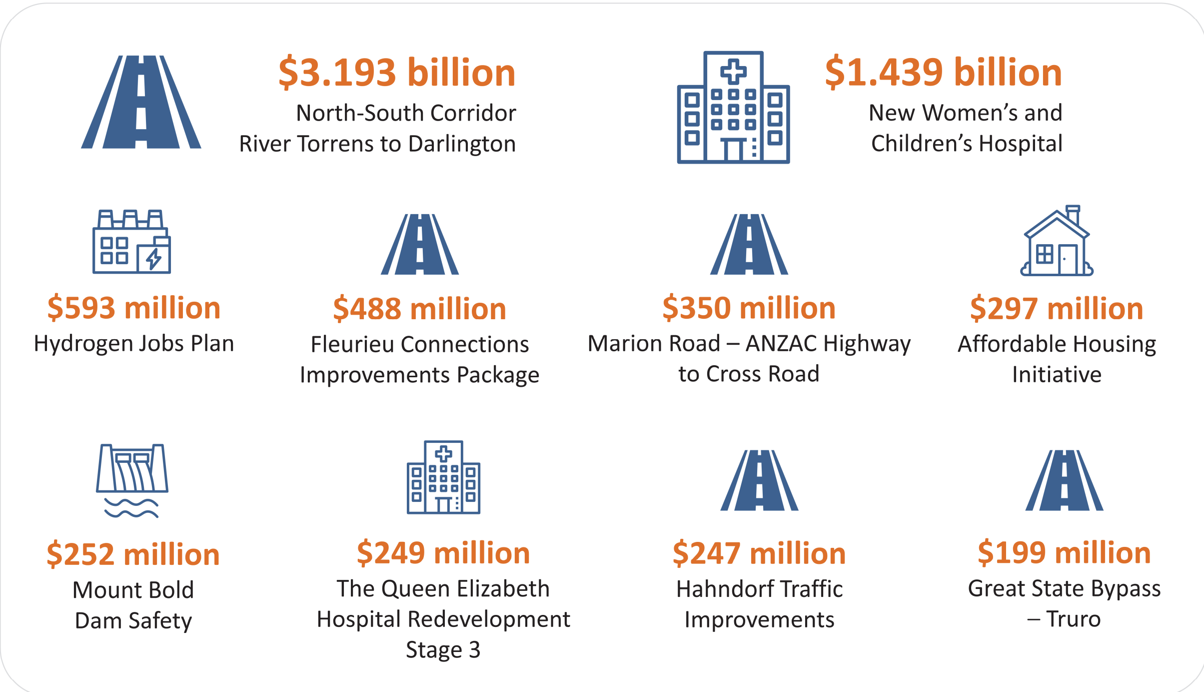
[35] The $16.7 billion total reflects the portion of the NFPS capital program that has been allocated to agencies.

DTF advised us that a transfer from contingency to agency budgets for investing projects will generally occur after a Cabinet approval for final costs and project scope. A transfer may also occur after DTF receives a signed agreement with another party (eg a Commonwealth National Partnership agreement) or when an agency enters into a contract to deliver the works. In these circumstances the Treasurer's approval to transfer contingency is sought, either specifically or through the budget process.

5.3.4 North-South Corridor River Torrens to Darlington project and new Women's and Children's Hospital expected to incur the most expenditure over the four years of the Budget

Figure 5.8 details the most significant capital projects over the four years of the 2022-23 Budget.

Figure 5.8: Major capital projects over the four years of the 2022-23 Budget[36]



The North-South Corridor River Torrens to Darlington project and new Women's and Children's Hospital are expected to incur the most investing expenditure over the four years of the 2022-23 Budget. Other projects with significant capital expenditure include the Hydrogen Jobs Plan[37] and Fleurieu Connections Improvements Package.[38]

---

[36] Includes amounts held in contingencies for these projects.

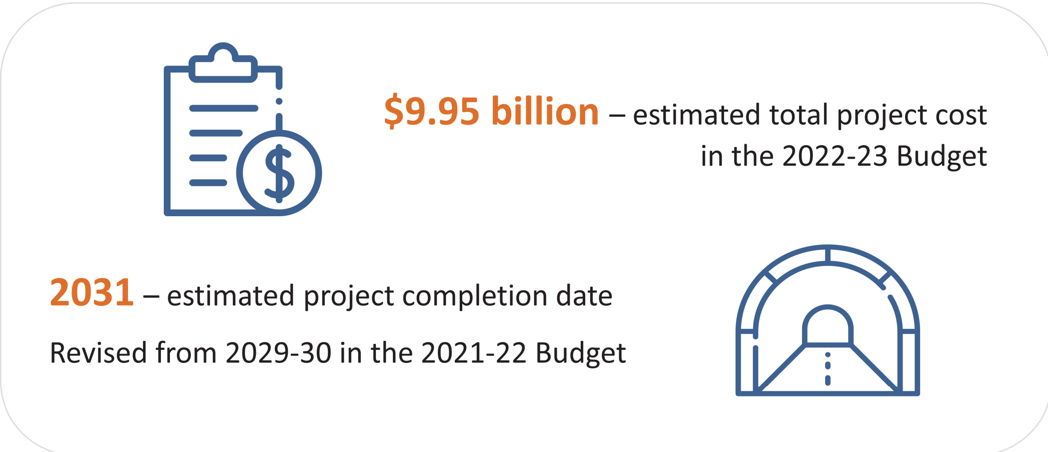
[37] The Hydrogen Jobs Plan involves establishing a new hydrogen facility including electrolysers, a combined cycle turbine plant and a hydrogen storage capacity in the Whyalla region.

[38] The Fleurieu Connections Improvements Package includes the Main South Road duplication from Seaford to Aldinga and Victor Harbor Road duplication projects.

5.3.4.1 A review of the North-South Corridor River Torrens to Darlington project, including its estimated cost, is being undertaken

A summary of the status of the North-South Corridor River Torrens to Darlington project in the 2022-23 Budget is shown in figure 5.9.

Figure 5.9: North-South Corridor River Torrens to Darlington project cost and time frame in the 2022-23 Budget



The 2022-23 Budget notes that DIT has been tasked with reviewing the delivery implications of the project. As part of the review, DIT is looking to reset the project with the right scope and a realistic construction program and budget expenditure profile.[39]

The project expenditure has been re-profiled in the 2022-23 Budget to reflect the revised timing of estimated cash flows for the project. This resulted in $1.1 billion of project expenditure being moved beyond the forward estimates.

DTF advised us that the project cost is subject to change as project planning and the business case need to be finalised and considered by Infrastructure SA, and the project is also subject to review by DIT.

5.3.4.2 Project cost and time frame for new Women's and Children's Hospital revised in the 2022-23 Budget

The cost and time frame for completing the new Women's and Children's Hospital project were revised in the 2022-23 Budget. The revisions are summarised in figure 5.10.

[39] Parliament of South Australia, House of Assembly, *Reprofile of North-South Corridor T2D cashflows*, tabled 31 May 2022, p. 3.

Figure 5.10: New Women's and Children's Hospital project revised cost and time frame in the 2022-23 Budget

$2.04 billion – estimated total project cost in the 2022-23 Budget

Revised from $1.94 billion in the 2021-22 Budget

September 2027 – estimated project completion date

Revised from June 2026 in the 2021-22 Budget

The $100 million increase in the estimated project cost is for 50 additional inpatient beds to ensure the new hospital has adequate capacity to cater for future growth in demand.

A review of the project completed in September 2022, after the 2022-23 Budget was issued, estimated that it may cost up to $3.2 billion.[40] This would represent an upwards revision of $1.16 billion from the estimate in the 2022-23 Budget. The expected time frame for completing the project was extended to 2030-31.

5.3.5 The SA Government will face challenges in ensuring its capital program is delivered on time and on budget

The 2022-23 Budget outlines a large capital program with significant capital projects to be delivered over several years. Major capital projects carry high inherent risks associated with estimating costs, complex contract arrangements, cost escalations and timeliness of completion. Proper planning, management and control of them is critical to achieving budgeted outcomes.

There is an increased risk that significant revisions may be required to project costs for larger and more complex capital projects.[41] For example, the estimated cost to deliver the North-South Corridor River Torrens to Darlington project increased by $1 billion in the 2021-22 Budget.

---

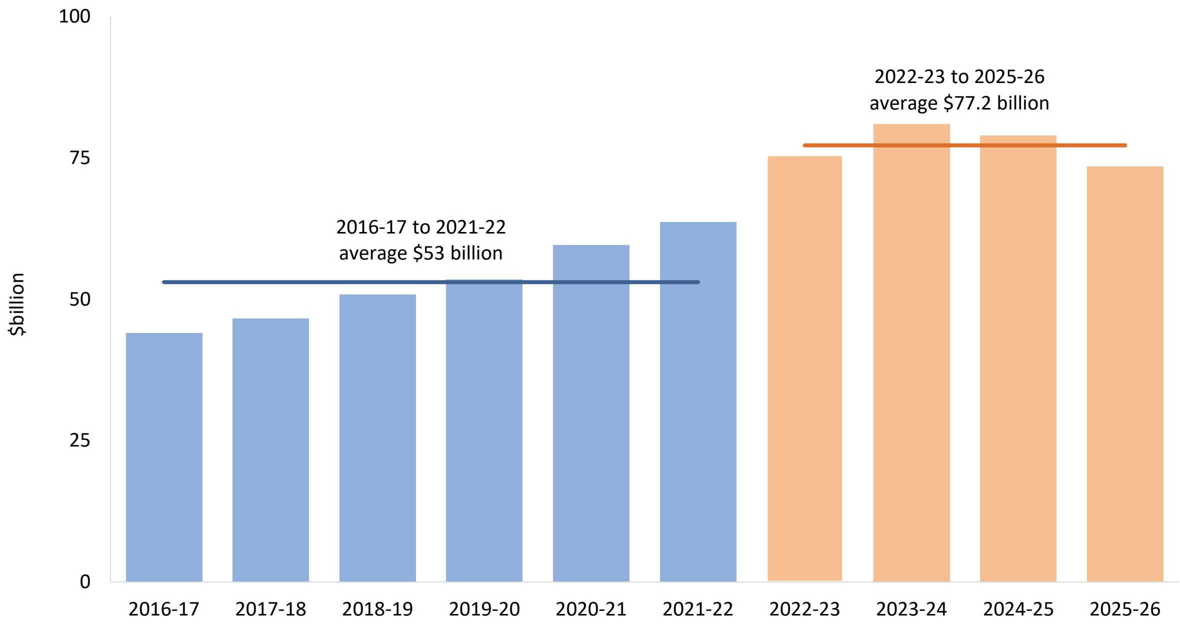
40 New Women's and Children's Hospital Project 2022, *New Site Identified*, Government of South Australia, 27 September, viewed 29 September 2022, <https://www.newwch.sa.gov.au/news/new-site-identified>.

41 The Grattan Institute analysed all public road and rail projects costing more than $20 million completed between quarter 1, 2001 and quarter 1, 2020. It found that 45% of projects with an initial estimated cost above $1 billion had a cost overrun. The average cost overrun for these projects was $1.05 billion. Terrill M, Emslie O and Moran G 2020, *The rise of mega projects: counting the costs*, Grattan Institute, 8 November 2020, p. 17.

5.3.5.1 Budgeted capital spending across all Australian states is expected to be significantly higher than historical trends

The SA Government's capital program in the 2022-23 Budget is 65% larger than the four-year capital program in the 2018-19 Budget, and other states are also budgeting significant capital programs. Figure 5.11 shows the combined value of capital programs of all Australian states over the period 2016-17 to 2025-26.

Figure 5.11: Australian states' NFPS purchases of non-financial assets from 2016-17 to 2025-26[42]



Source: South Australian and interstate budget papers and financial reports.

The large pipeline of public infrastructure investments across Australia combined with private sector infrastructure investment, and the resulting increase in demand for workers, materials and equipment, are likely to lead to further capacity constraints. Infrastructure Australia has noted:

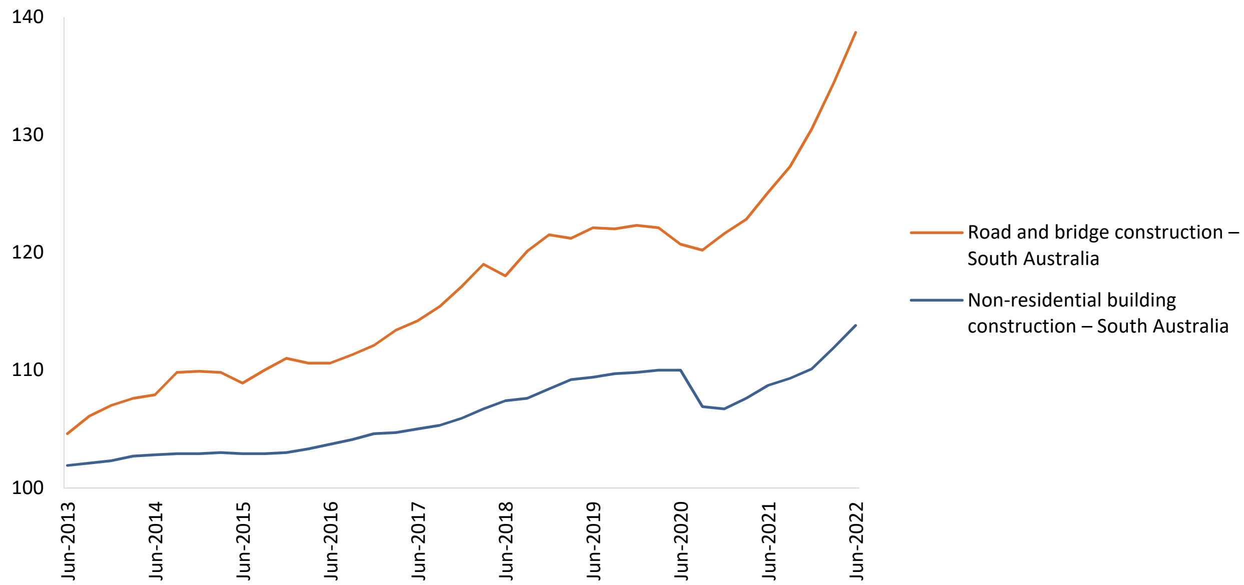
> *The scale of the demand for skills and resources is highly likely to exceed the normal capacity increases expected in the market.*[43]

5.3.5.2 Capacity constraints and inflationary pressures may drive significant cost escalations for South Australia's capital program

Supply chain disruptions, skilled labour shortages and increased activity driving demand for trades and materials have seen a sharp increase in construction costs over the last year. Figure 5.12 highlights the increase in non-residential building and road and bridge construction costs currently being experienced in South Australia.

[42] NFPS purchases of non-financial assets for Victoria included in figure 5.11 include changes in inventories.
[43] Infrastructure Australia 2021, *Infrastructure market capacity*, October, p. 9.

Figure 5.12: Construction price indexes – South Australia – June 2013 to June 2022



Source: Australian Bureau of Statistics 2022, *Producer Price Indexes*, June, cat. no. 6427.0, table 17. Output of the construction industries, subdivision and class index numbers, Index No 3020: Non-residential building construction South Australia, Series ID: A2333748X, Index No 3101: Road and bridge construction South Australia, Series ID A2333742K, accessed 23 August 2022.

Figure 5.12 shows that in the 12 months to June 2022, non-residential building construction costs increased by 4.7% and road and bridge construction costs increased by 10.9%.

The 2022-23 Budget identifies that the current high demand for infrastructure-related labour and materials increases the risks of cost escalations for capital programs. It also notes that project estimates include prudent allowances for cost escalations.

DTF advised us that the allowances for major project cost escalations are embedded in project budgets. It also advised us that the total project cost is developed by each agency on a project-by-project basis. As such, the size of the allowance for cost escalations is dependent on the nature of the project and any project-specific risk factors identified at the time the budget is developed.

Significant increases in construction costs above the allowances provided for in the agency project estimates pose the risk of projects exceeding forecast cost estimates.

5.3.5.3 SA Government will need robust controls and appropriate skills and expertise to deliver its capital program on time and on budget

Appropriate procurement, contract and project management expertise, as well as sound information systems and financial controls, are required to effectively manage the risks associated with the capital program and meet budget targets.

Infrastructure Australia has noted that inadequate public sector procurement expertise, including oversight of projects during delivery, can result in the taxpayer being exposed to inappropriate risks or costs and compromise the capability of projects to achieve user outcomes.[44]

My previous Reports have highlighted significant scope to improve the planning, procurement, project management and contract management of major capital projects.[45] It is important that due consideration is given to the findings and recommendations in these Reports when planning and managing the State's capital program.

5.3.5.4 SA Government Cabinet Committees, Infrastructure SA and DTF have responsibility for oversight of the investing budget, while DIT is responsible for project delivery

Effective governance and oversight of the SA Government's investing budget is critical to ensuring risks with the capital program are identified and effectively managed, to enable delivery of the capital program on time and within budget.

An overview of roles and responsibilities for the oversight and management of the SA Government's investing budget as advised to us by DTF is provided in figure 5.13.

Figure 5.13: Roles and responsibilities for the oversight and management of the SA Government's investing budget

Cabinet Committees	Government Performance Cabinet Committee – responsible for monitoring the status of major election commitments, including infrastructure projects. Budget Cabinet Committee – responsible for monitoring and reviewing infrastructure projects, reviewing proposals in advance of Cabinet consideration and identifying and proactively managing emerging issues.
Infrastructure SA	Provide independent advice to the SA Government to enable informed and evidenced based decisions on infrastructure planning, investment, delivery and optimisation. Monitor capital projects over $50 million in accordance with the Infrastructure SA Assurance Framework and report to Cabinet (through the Budget Cabinet Committee on outcomes and findings of project assurance reviews).
DTF	Broad oversight of the SA Government's investing program by: • providing advice to SA Government on prospective new projects • regular oversight of projects through quarterly major investing project monitoring • working closely with agencies to oversee successful implementation of projects.

DTF also advised us that DIT is responsible for the providing major infrastructure safely and efficiently, to sustain and support growth and maximise the benefit of the SA Government's investment in transport assets. DIT also establishes strategic plans, standards and program

---

44 Infrastructure Australia 2019, *An Assessment of Australia's Future Infrastructure Needs: Australian Infrastructure Audit 2019*, June, p. 236.

45 Auditor-General's Report 7 of 2020 *Flinders Link Project* and Auditor-General's Report 11 of 2019 *Darlington Upgrade Project* provide examples of projects where significant scope for improving planning, procurement, project management and contract management of major capital projects was identified.

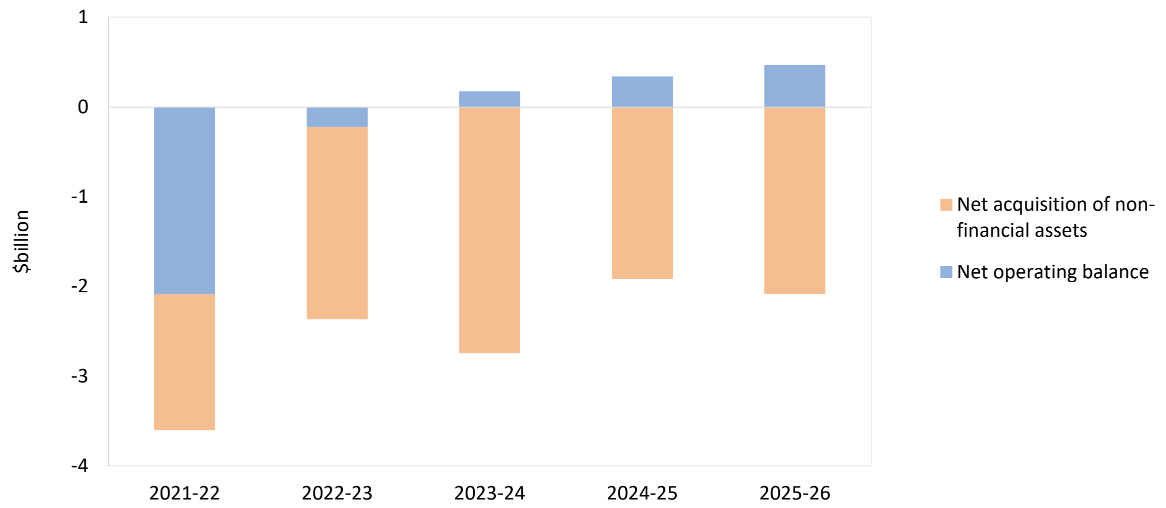
management frameworks for network development to deliver positive community and economic benefits.

5.4 Borrowings and net debt

5.4.1 Net lending deficits projected over the four years of the 2022-23 Budget driven by the net acquisition of non-financial assets

Figure 5.14 shows the NFPS net lending balance for the period 2021-22 to 2025-26, and the extent to which it is driven by the net operating balance and total net acquisition of non-financial assets[46] in each year.

Figure 5.14: Composition of NFPS net lending balance for the period 2021-22 to 2025-26



Net lending balance	-$3.603b	-$2.369b	-$2.573b	-$1.579b	-$1.619b

Figure 5.14 shows that the net lending deficits projected over the four years of the 2022-23 Budget are driven by the net acquisition of non-financial assets, in particular the SA Government's large capital program, as a small operating deficit is projected in 2022-23 and operating surpluses are projected from 2023-24.

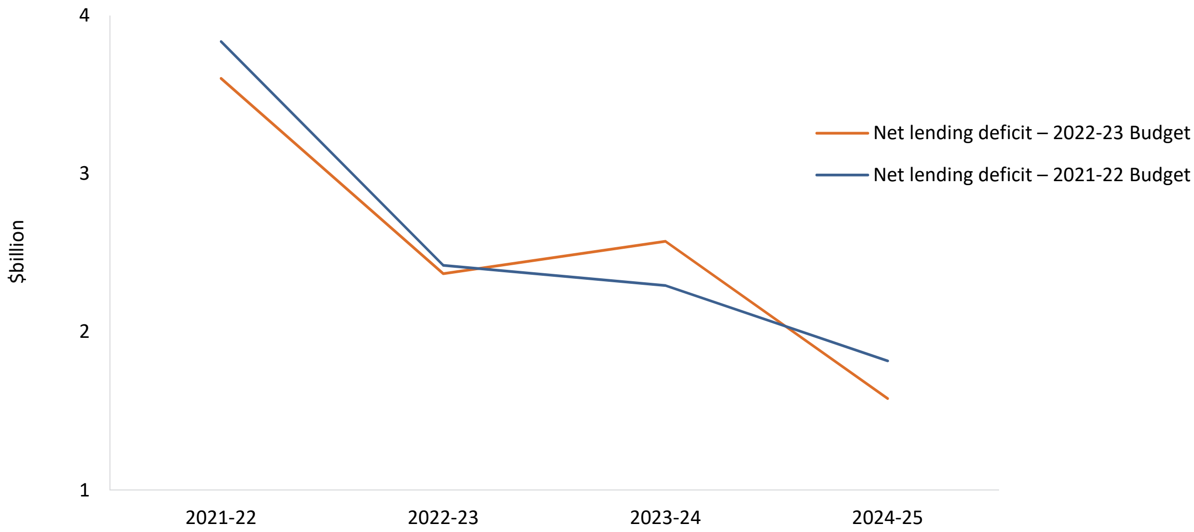
The projected net lending deficit for 2021-22 reflects the large operating deficit and the SA Government's large capital program in that year.

5.4.2 Forecast net lending balances have improved slightly since the previous Budget but significant increases in net debt are still expected by 2025-26

NFPS net lending deficits for 2021-22, 2022-23 and 2024-25 are now projected to be lower than that forecast in the 2021-22 Budget, as shown in figure 5.15.

[46] Net acquisition of non-financial assets equals the purchase of non-financial assets less depreciation and sales of non-financial assets plus changes in inventories.

Figure 5.15: Comparison of NFPS net lending deficits in 2021-22 and 2022-23 Budgets



The improved net lending deficits are mainly due to:

- a decrease in expected purchases of non-financial assets for 2021-22 compared to the 2021-22 Budget estimate due to delays in project expenditure
- improved net operating balance forecasts for 2022-23 and 2024-25 compared to the 2021-22 Budget.

The NFPS net lending deficit for 2023-24 ($2.573 billion) is forecast to be higher than the previous Budget ($2.294 billion). This is primarily due to an increase in expected purchases of non-financial assets for 2023-24 in the 2022-23 Budget ($5.172 billion) compared to the previous Budget ($4.902 billion).

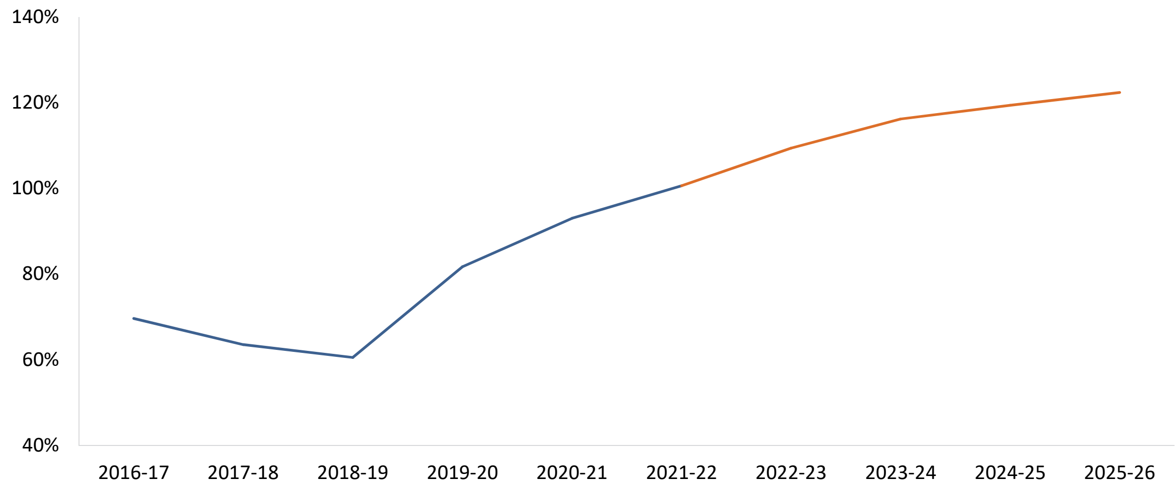
The net lending deficits result in significant expected increases in net debt. NFPS net debt is projected to increase by $9.152 billion, from $24.71 billion at 30 June 2022 to $33.862 billion at 30 June 2026. Most of the increase in NFPS net debt relates to the general government sector ($8.29 billion).

However, NFPS net debt is expected to be $1.611 billion lower at 30 June 2025 than estimated in the 2021-22 Budget. This is mainly due to improved revenue estimates (see section 3.3.1).

5.4.3 NFPS net debt projected to rise to 122% of revenue by 30 June 2026

Comparing net debt to a state's revenue provides one measure of the sustainability of a state's debt levels. Figure 5.16 shows the NFPS net debt to revenue ratio over the period 2016-17 to 2025-26 for South Australia.

Figure 5.16: NFPS net debt to revenue ratio from 2016-17 to 2025-26



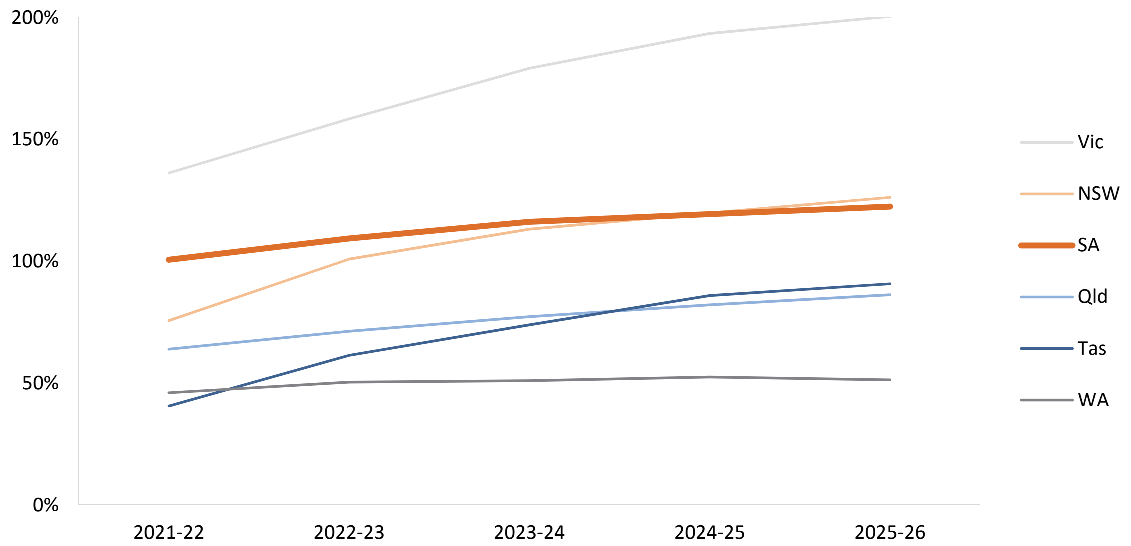
The NFPS net debt to revenue ratio has increased significantly from 70% in 2016-17 to a forecast 122% in 2025-26. This mainly reflects higher borrowings to fund:

- the operating cash deficits between 2019-20 and 2021-22 resulting from the economic impacts of COVID-19 and the SA Government's economic stimulus response
- the SA Government's large capital program since 2020-21.

5.4.4 South Australia's net debt as a percentage of revenue forecast to be third highest of all states from 2024-25

Figure 5.17 compares South Australia's NFPS net debt to revenue ratio to other Australian states for the period 2021-22 to 2025-26.

Figure 5.17: South Australia's NFPS net debt to revenue ratio compared to other Australian states from 2021-22 to 2025-26



Source: South Australian and interstate budget papers.

Figure 5.17 highlights that the NFPS net debt to revenue ratio for all Australian states is expected to trend upwards from 2021-22 to 2025-26.

Coming into the COVID-19 pandemic in 2019-20, South Australia's NFPS net debt to revenue ratio was comparable to Victoria but higher than the other states.[47] By 30 June 2026, South Australia's net debt to revenue ratio (122%) is expected to be similar to that of New South Wales (126%) and substantially lower than Victoria (200%).

The increase in the NFPS net debt to revenue ratio across Australian states reflects increased borrowings by each state to implement significant capital investment programs to support job creation and economic growth.

5.4.5 No specific quantifiable measure established to monitor performance against the fiscal target of achieving a sustainable level of net debt

The SA Government's Fiscal Target 3 aims to achieve a level of net debt that is sustainable over the forward estimates. The 2022-23 Budget notes that this target requires the maintenance of sustainable debt levels that allow for sustainable borrowings for investment in key infrastructure without placing undue burden on future generations.

The SA Government has not set a clear and quantifiable measure to assess its performance against Fiscal Target 3. Without this, it may be difficult to assess what is a sustainable level of debt over the forward estimates and whether it has been satisfactorily achieved.

DTF advised us that the new SA Government has retained the previous SA Government's fiscal targets and will consider the views of the credit rating agencies, benchmarking against interstate peers and the level of interest cost burden in assessing the sustainability of its debt levels.

DTF also advised us that:

- Fiscal Target 3 acknowledges that there can be variability in debt levels over time as decisions are made to invest in infrastructure or the budget responds to challenging short and medium-term fiscal circumstances
- the SA Government assesses the sustainability of its net debt levels annually through the budget process, and credit rating agencies also assess the SA Government's position and budget annually
- while increases in interest rates and large investing programs will, in isolation, have implications for debt, the level of net debt beyond the forward estimates will be determined in the 2023-24 budget process, as the SA Government can tailor its expenditure decisions over time to manage its financial position.

---

[47] Auditor-General's Report 8 of 2021 *State finances and related matters*, pp. 53-54.

Fiscal Target 3 only considers the sustainability of net debt over the forward estimates. The SA Government has committed to several significant investing expenditures beyond the forward estimates, which may lead to further large increases in net debt (see section 5.4.11). Given this, it is prudent for the SA Government to also consider its investing expenditure commitments beyond the forward estimates when assessing the sustainability of its net debt.

5.4.6 Borrowing costs projected to increase significantly due to rising interest rates

In 2021-22 bond yields increased due to investor expectations of higher inflation. This required central banks to unwind stimulatory monetary policy measures, including by increasing interest rates. The high inflation experienced in Australia has seen the RBA increase its cash rate target by 2.5% since the start of May 2022.

Consistent with the increase in bond yields, SAFA's borrowing rates have increased. The 2022-23 Budget notes that:

- the interest rate on SAFA's three-year select bond has risen from 0.5% in 2020-21 to over 3.25% as at 6 May 2022
- the interest rate on SAFA's 10-year select bond has risen to 4% as of 6 May 2022 (it ranged between 1.25% and 2% in 2020-21).

The increase in SAFA's borrowing rates has resulted in an increase in interest expense projections in the 2022-23 Budget from those in the 2021-22 Budget, as shown in figure 5.18.

Figure 5.18: NFPS interest expense in 2021-22 and 2022-23 Budgets

	2021-22 Budget	2022-23 Budget	Increase
2022-23	$852 million	$997 million	$145 million ↑
2023-24	$968 million	$1.206 billion	$238 million ↑
2024-25	$1.181 billion	$1.354 billion	$173 million ↑

DTF advised us that SAFA modelling is used to determine interest expense forecasts in the Budget. SAFA's modelling calculates the average cash loan[48] and cost of funds loan[49] balances based on the forecast Consolidated Account receipts, and applies an average interest rate to determine interest expense projections.

48 Loan from SAFA to the Treasurer to meet the working capital needs of general government agencies.

49 Cost of funds loan portfolio includes liquid nominal rate liabilities and hedge instruments and certain non-liquid nominal long-term borrowings.

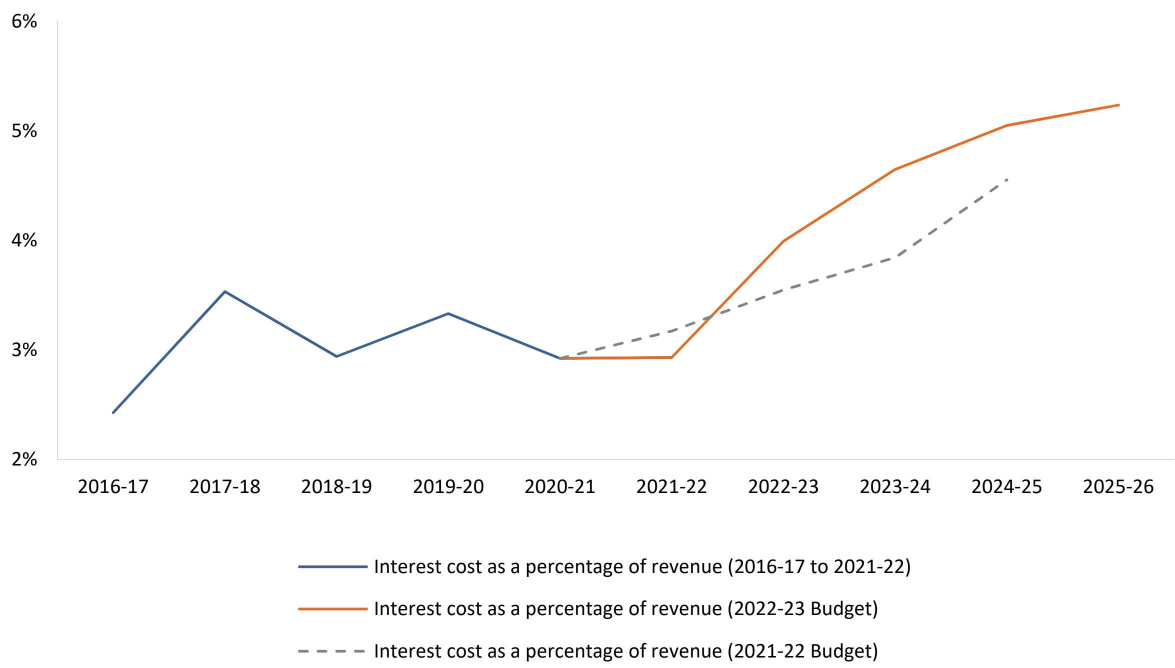
DTF also advised us that the interest rate used to forecast interest expenses in 2024-25 for the Treasurer's:

- cost of funds loan is 0.48% higher than the interest rate used in the 2021-22 Budget
- cash loan is 0.99% higher than the interest rate used in the 2021-22 Budget.

5.4.7 Borrowing costs as a percentage of total revenue are higher than those estimated in the 2021-22 Budget and will rise to 5.2% by 2025-26

Interest expense as a percentage of total revenue (interest expense to total revenue ratio) is an indicator of a state's capacity to fund its borrowing costs from operating revenues. Figure 5.19 shows the NFPS interest expense to total revenue ratio over the period 2016-17 to 2025-26 for South Australia.

Figure 5.19: NFPS interest expense to total revenue ratio from 2016-17 to 2025-26



The NFPS interest expense to total revenue ratio is forecast to increase significantly from 2.4% in 2016-17 to 5.2% by 2025-26. This principally reflects the increase in NFPS borrowings and interest rates.

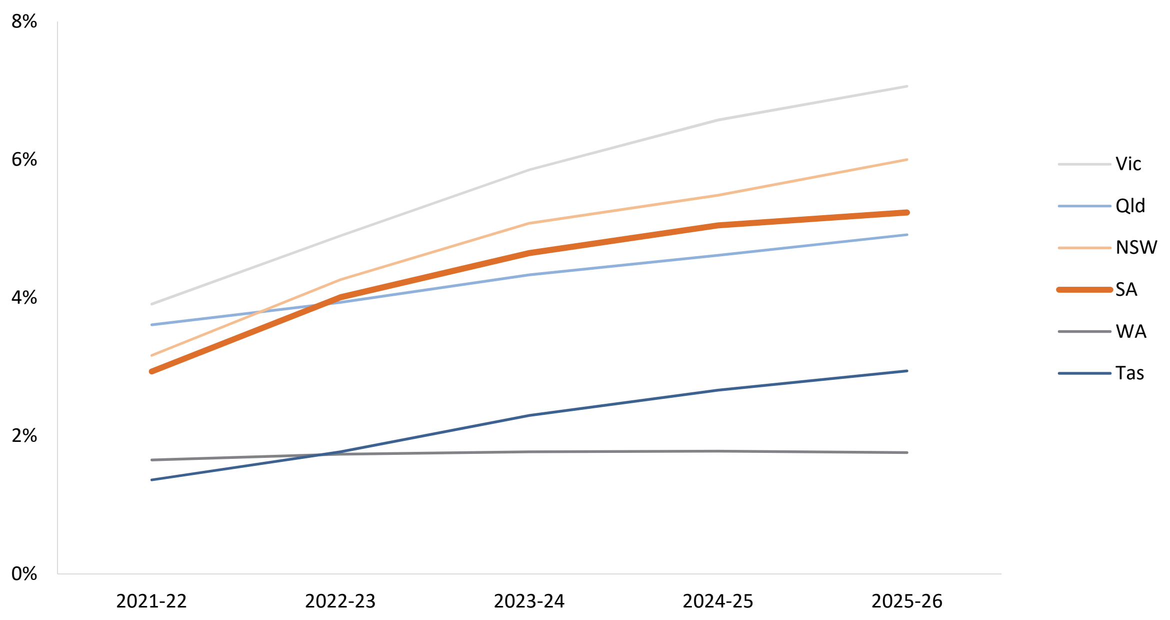
Figure 5.19 highlights that borrowing costs as a percentage of revenue over the forward estimates period is forecast to be above that estimated in the 2021-22 Budget. The NFPS interest expense to revenue ratio is now forecast to average 4.7% over the four years of the 2022-23 Budget, compared to 3.8% over the four years of the 2021-22 Budget.

As the ratio of interest expense to revenue increases there is a risk the SA Government will have less budget flexibility to fund service delivery needs and respond to future economic challenges.

5.4.8 South Australia's borrowing costs as a percentage of total revenue forecast to rise to the third highest of all states from 2022-23

Figure 5.20 compares South Australia's NFPS interest expense to total revenue ratio to other Australian states for the period 2021-22 to 2025-26.

Figure 5.20: South Australia's NFPS interest expense to total revenue ratio compared to other states from 2021-22 to 2025-26



Source: South Australian and interstate budget papers.

Figure 5.20 highlights that by 30 June 2026 South Australia's interest expense to total revenue ratio is expected to be considerably higher than Western Australia (1.8%) and Tasmania (2.9%), comparable to Queensland (4.9%) and considerably lower than New South Wales (6%) and Victoria (7.1%).

Western Australia's ratio is considerably lower than all other states, reflecting its low level of net debt compared to other states due to its substantial surpluses in 2020-21 and 2021-22 and projected surpluses over the four years of its 2022-23 Budget.

5.4.9 South Australia’s risk exposure to interest rate rises is significantly increased by the higher level of net debt

There is a risk that central banks may need to increase interest rates at a faster rate, and/or by more than bond markets expect, to combat rising inflation, leading to further increases in bond yields.

The SA Government’s projected rising level of net debt significantly increases its exposure to increases in interest rates. Figure 5.21 shows the borrowing cost impact of a one and two percentage point increase in the average interest rate applying to NFPS net debt.

Figure 5.21: Impact on NFPS interest expenses of increases in interest rates

	1% increase in interest rates	2% increase in interest rates
2022-23	$247 million	$494 million
2023-24	$273 million	$546 million
2024-25	$301 million	$602 million
2025-26	$320 million	$640 million

The 2022-23 Budget notes that the SA Government’s debt management objective is to minimise long-term average interest costs subject to acceptable levels of interest rate risk.

SAFA is the State’s central borrowing authority and is responsible for managing most of the State’s debt, including interest rate risk. It lends funds raised from financial markets to various South Australian public sector clients, including the Treasurer (who borrows on behalf of public sector agencies to support their operational requirements) and SA Water.

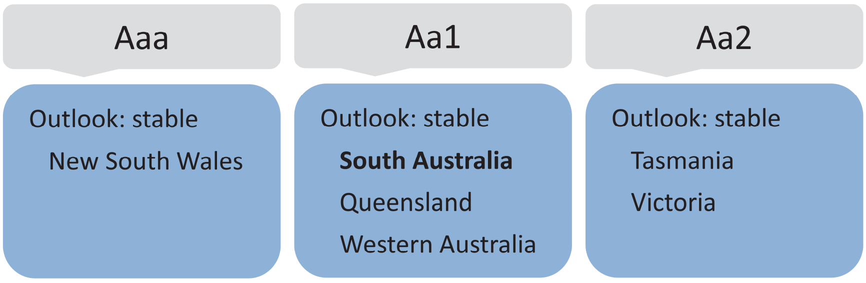
Further details on SAFA and its debt and interest rate risk management approach are included in the section of Part C of my 2021-22 Annual Report titled ‘South Australian Government Financing Authority’.

5.4.10 No change made by Moody's or Standard & Poor's to South Australia's credit ratings after the 2022-23 Budget

5.4.10.1 Moody's maintained South Australia's credit rating at its second highest level

Following the release of the 2022-23 Budget, Moody's maintained South Australia's credit rating at Aa1 with a stable outlook. Figure 5.22 shows Moody's credit rating for each Australian state at 31 August 2022.

Figure 5.22: Moody's credit ratings for Australian states (August 2022)



Source: Information provided by DTF.

The only state with a higher Moody's credit rating than South Australia is New South Wales.

Moody's indicated that the stable outlook for South Australia's credit rating reflects its expectation that the underlying strength of the broader Australian economy will remain solid. This will sustain GST distributions and other Commonwealth grants and transfers that underpin the SA Government's capacity to fund expenditure and service its debt. Moody's also indicated that South Australia's credit rating could be:

- upgraded if effective implementation of measures sustains strong revenue growth with strong control over spending, resulting in a prolonged period of budget surpluses and material and sustained reductions in debt
- downgraded if it believes the SA Government's resolve or ability to contain fiscal deficits and reduce its debt is diminished.

Moody's also noted that inflation pressures and new recurrent costs increase the SA Government's vulnerability to an unexpected revenue shock. Moody's indicated that spending discipline will be key in determining the SA Government's capacity to deliver a balanced operating position in 2022-23.

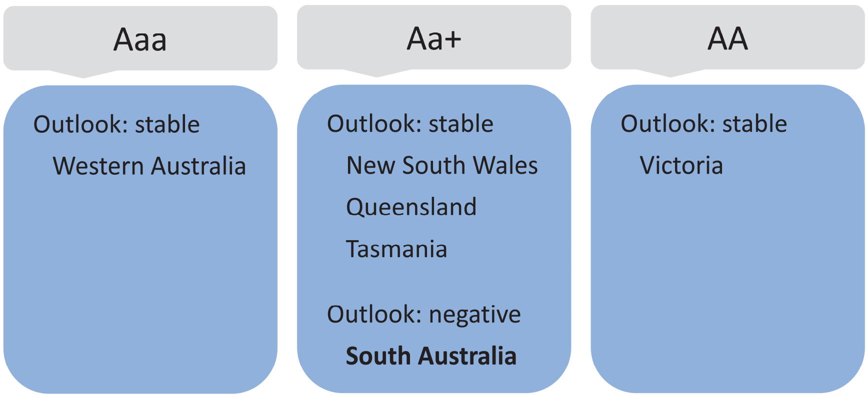
On the SA Government's capital program, Moody's noted:

- the 2022-23 Budget delayed some large capital spending projects and introduced a near-term focus on smaller projects to provide increased flexibility amid rising cost pressures, labour shortages and elevated supply chain disruptions
- the budgeted levels of infrastructure spending may be difficult to achieve given market capacity, raw materials and labour supply constraints.

5.4.10.2 Standard & Poor's (S&P) maintained South Australia's credit rating at its second highest level with a negative outlook

In August 2022 S&P affirmed South Australia's credit rating at AA+ with a negative outlook. Figure 5.23 shows S&P's credit ratings for each Australian state at 31 August 2022.

Figure 5.23: S&P's credit ratings for Australian states (August 2022)



Source: S&P's website, <https://www.spglobal.com/ratings/en/>.

South Australia has the same S&P credit rating as all other Australian states except Western Australia, which has a higher S&P credit rating, and Victoria, which has a lower S&P credit rating.

S&P indicated that its negative outlook for South Australia's credit rating reflects its view that South Australia's financial metrics could weaken beyond its current forecasts on the back of cost pressures and a growing capital budget. S&P also indicated that it could:

- lower South Australia's credit rating over the next two years if its fiscal metrics do not recover to the degree it forecasts. This could occur if operating deficits persist while the SA Government rolls out large infrastructure spending, resulting in wider after capital account deficits
- revise its outlook for South Australia's credit rating to stable in the next two years if it narrows its deficits in line with S&P's forecasts.

On the SA Government's large capital program, S&P noted that there is some risk of cost overruns, skilled labour shortages and project delays due to the record levels of infrastructure construction occurring across Australia. Section 5.3.5 discusses these risks and other challenges the SA Government will face in ensuring its capital program is delivered on time and on budget.

5.4.11 Net debt levels will likely rise further as a result of substantial infrastructure project expenditure planned beyond the forward estimates and other budget risk factors

Major investing expenditure commitments that exist beyond the forward estimates period are summarised in figure 5.24.

Figure 5.24: Major investing expenditure commitments beyond the forward estimates

North-South Corridor River Torrens to Darlington

Total project cost: $9.95 billion

Expenditure beyond the forward estimates: $6.478 billion

Commonwealth funding beyond the forward estimates: $3.239 billion[50]

New Women's and Children's Hospital[51]

Total project cost: $2.04 billion

Expenditure beyond the forward estimates: $539 million

No Commonwealth funding

Flinders Medical Centre Upgrade

Total project cost: $400 million

Expenditure beyond the forward estimates: $239 million

Commonwealth funding beyond the forward estimates: $120 million

Other investing projects[52]

Total project costs: $855 million

Expenditure beyond the forward estimates: $253 million

Commonwealth funding beyond the forward estimates: $89 million

These large infrastructure initiatives may result in further net debt increases as they will be primarily funded by the SA Government.

A review of the scope, timing and costings for the new Women's and Children's Hospital was completed in September 2022, while a review of the North-South Corridor River Torrens to Darlington project is in progress (sections 5.3.4.1 and 5.3.4.2 provide further details).

It is planned that the budgeted cost to build the new Women's and Children's Hospital will be resolved in early 2023 and it is estimated that it may now cost up to $3.2 billion.[53] This represents an increase of up to $1.16 billion from the project cost in the 2022-23 Budget.

---

[50] In February 2022, the Commonwealth Government announced additional Commonwealth funding of $2.26 billion for the North-South Corridor River Torrens to Darlington project. This increased the total Commonwealth funding for the project to $4.971 billion.

[51] Represents the project cost and expenditure profile in the 2022-23 Budget.

[52] Other investing projects comprise the new Mount Barker Hospital, Marion Road and Sir Donald Bradman Drive intersection upgrade, Marion Road upgrade between ANZAC Highway and Cross Road and the Adelaide Hills productivity and road safety package.

[53] New Women's and Children's Hospital Project 2022, *New Site Identified*, Government of South Australia, 27 September, viewed 29 September 2022, <https://www.newwch.sa.gov.au/news/new-site-identified>.

This highlights the risk that cost estimates for major capital projects may need to be revised significantly upwards from estimates in the 2022-23 Budget. This may result in an increase in net debt, as any increase in project costs is likely to be funded, at least in part, through increased borrowings.

Debt levels may also increase if:

- inflation is higher than anticipated, flowing through to higher operating expenses and upward pressure on interest rates increasing borrowing costs
- agency savings targets are not achieved
- growth in employee expenses exceeds that allowed for in the forward estimates due to enterprise agreement negotiation outcomes
- additional expenditure measures are required by the SA Government to respond to COVID-19 outbreaks or to stimulate economic recovery from the pandemic.

Given these risk factors and the substantial infrastructure expenditure planned beyond the forward estimates, it is important the SA Government closely monitors its net debt fiscal target and budget risk exposures to ensure its net debt remains sustainable.

Appendix 1 – Reporting framework

Uniform Presentation Framework (UPF)

By agreement between the Commonwealth, states and territories, each jurisdiction presents its Budget Papers and mid-year budget update on a UPF basis.

The primary objective of the UPF is to ensure that Commonwealth, State and Territory Governments provide a common core of financial information in Budget Papers to enable direct comparisons across jurisdictions.

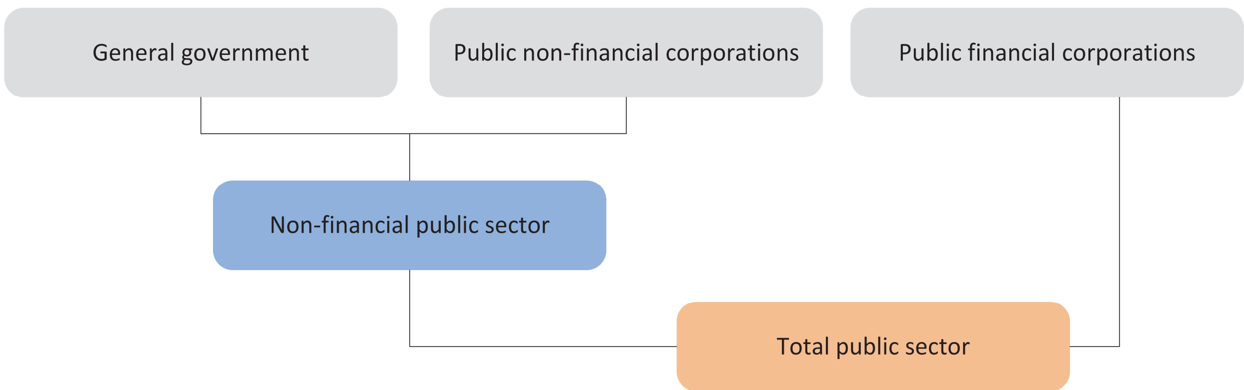
Institutional sectors

Budget reporting is prepared for the following institutional sectors:

- **General government sector** – agencies providing services free of charge or at prices below their cost of production or service cost. These are the services that tend to be primarily financed through taxes and other charges, and for this reason this sector tends to be the focus of fiscal targets.
- **PNFC sector** – trading enterprises mainly engaged in producing goods and services for sale in the marketplace at prices that aim to recover most or all of the costs involved. In South Australia this sector includes SA Water and the South Australian Housing Authority.
- **PFC sector** – bodies primarily engaged in providing financial services. This includes financial institutions such as SAFA, HomeStart Finance and the Superannuation Funds Management Corporation of South Australia.
- **NFPS** – the consolidation of the general government and PNFC sectors.

Figure A1 shows the structure of the sectors, which when consolidated form the total public sector (whole of government).

Figure A1: Sectors of government activity



Budget reporting

Budget estimates are presented on an accrual basis. Three primary statements are prepared for the general government sector, PNFC sector and NFPS:

- operating statement including other economic flows
- balance sheet
- cash flow statement.

PFC sector data is not published in the Budget Papers.

Fiscal measures

The UPF prescribes various fiscal measures as a basis for evaluating the soundness of the government's fiscal position and the effect of fiscal policy. Figure A2 sets out the key fiscal measures in the UPF referred to in this Report.

Figure A2: UPF – key fiscal measures

Fiscal measure	Description
Net operating balance	Revenue from transactions less expenses from transactions. The net operating balance excludes expenditure on the acquisition of capital assets, but includes non-cash costs such as accruing superannuation entitlements and the consumption of capital (depreciation). This provides a measure of the sustainability of the government's fiscal position over time and provides an indication of the sustainability of the existing level of government services.
Net lending/borrowing (fiscal balance)	Net operating balance less the net acquisition of non-financial assets. This measures a government's investment-saving balance. A net lending balance (fiscal surplus) indicates that a government is saving more than is required to finance all of its investment spending. A net borrowing (fiscal deficit) position indicates that the public sector's level of investment exceeds its level of savings.
Net debt	Sum of deposits held, advances received and borrowings, less the sum of cash and deposits, advances paid, investments, loans and placements.
Net worth	Total assets (both financial and non-financial) less total liabilities, shares and other contributed capital. Net worth incorporates a government's non-financial assets, such as land and other fixed assets, which may be sold and used to repay debt, as well as financial assets and liabilities not captured by the net debt measure, most notably accrued employee superannuation liabilities, debtors and creditors.

The glossary in Budget Paper 3 provides further detail on the terms used in the Budget Statement and definitions.

Appendix 2 – Abbreviations used in this Report

Abbreviation	Description
CGC	Commonwealth Grants Commission
DCP	Department for Child Protection
DIT	Department for Infrastructure and Transport
DTF	Department of Treasury and Finance
Education	Department for Education
FTE	Full-time equivalent
GSP	Gross State Product
GST	Goods and services tax
IHACPA	Independent Health and Aged Care Pricing Authority
MYBR	Mid-year budget review
NFPS	Non-financial public sector
NOB	Net operating balance
NWAU	National Weighted Activity Unit
PFC	Public financial corporations
PNFC	Public non-financial corporation
RBA	Reserve Bank of Australia
S&P	Standard & Poor’s
SAFA	South Australian Government Financing Authority
SA Water	South Australian Water Corporation
UPF	Uniform Presentation Framework