OVERVIEW

BACKGROUND

The Northern Territory's first Labor Government was elected on 18 August 2001 and took office on 27 August 2001.

An integral part of Labor's policy platform was the document *Labor's Financial Statement* which set out the financial initiatives to be pursued during the first term of the Northern Territory Labor Government. *Labor's Financial Statement* included a range of initiatives across the functional areas of health, lifestyle, education and training, law, order and emergency services, and business. The document also dealt with priorities for capital works under a Labor Government. Total initiatives were estimated to cost $19.6 million in 2001-02 rising to $69 million in 2004-05 with the cost of these initiatives being met through a combination of savings identified in a number of specific areas and reduced capital works expenditure.

However, immediately following the election, the Treasury advised the Government that the underlying budget position was unsustainable, being closer to a deficit of $102 million than the $12 million that had been estimated in the Budget Papers. The reason for the difference was twofold. The first was that the estimated outcome included $50 million from a one-off asset sale related to the sale of NT Fleet assets thus masking part of the underlying deficit. The second reason was that ongoing financial requirements in a number of functional areas, particularly health, education and some law and order functions were, in Treasury's assessment, understated and increases in the Budget for these purposes during 2001-02 would be required. After receiving that advice, the Government determined that it would commission an independent assessment of the Territory's current and future fiscal position. Professor Percy Allan was appointed to undertake this task.

Professor Allan confirmed Treasury's initial advice and estimated the underlying (i.e. net of other influences such as one-off items) 2001-02 deficit to be $107 million. Professor Allan concluded that the Territory's budget position, if unchanged, was unsustainable and that a deficit reduction strategy was required in order to place the Territory's finances on a fiscally responsible footing. Professor Allan provided an indicative deficit reduction strategy in his report.

The Government determined that it would introduce a Mini Budget in November 2001 in order to establish a more appropriate allocation across functional areas, to incorporate into the 2001-02 Budget and forward estimates the Government's initiatives and also to adopt a deficit reduction strategy similar to that suggested by Professor Allan.

Professor Allan also recommended a number of other changes, including the introduction of Fiscal Integrity and Transparency legislation similar to that which has been adopted by the Commonwealth and other State jurisdictions in Australia. Such legislation requires the Government to compile and report its financial information in accordance with externally determined standards, notably Government Finance Statistics as promulgated by the Australian Bureau of Statistics, the Uniform Presentation Framework as agreed by Governments, and Australian Accounting Standards; for the financial information to be prepared by the Treasury without the influence of the government of the day with the Under Treasurer to certify the independence and accuracy of the estimates and projections; and for the Government's fiscal strategy to be assessed against these financial estimates and projections.

A Fiscal Integrity and Transparency Bill was introduced into the Northern Territory Legislative Assembly in October 2001 and it is expected that the Bill will be passed during the November 2001 Sittings, the same sittings in which the Mini Budget will be presented. This Budget Paper, the *Economic and Fiscal Outlook*, has been prepared to the extent possible in accordance with that legislation even though it has not yet been passed by the Northern Territory Legislative Assembly. The legislation provides for progressive implementation of the various requirements, particularly the move to accrual accounting and reporting and the associated observance of accounting standards in that process. Further developments will be included in the 2002-03 Budget.

FINANCIAL PROJECTIONS

After a period of budget deficits from 1997-98, the outlook for the Northern Territory total public sector is a return to a more sustainable budget position over the forward estimates period. This has been achieved after:

- resetting the base budgets of Agencies to more accurately reflect their fiscal requirements and giving greater priority to health, education and law and order functions;
- the incorporation into the 2001-02 Mini Budget and forward estimates of Government initiatives; and
- putting in place a deficit reduction strategy.

TABLE 1.1 : NORTHERN TERRITORY TOTAL PUBLIC SECTOR (a)

	2000-01 Actual (b) $M	2001-02 May Budget (c) $M	2001-02 Mini Budget (d) $M	2002-03 Forward Estimate $M	2003-04 Forward Estimate $M	2004-05 Forward Estimate $M
Total Expenditure	2 318	2 132	2 252	2 244	2 276	2 327
Total Revenue	1 981	2 073	2 064	2 139	2 209	2 269
Financing Transactions	337	59	188	106	67	58
less Increase in Provisions	62	51	62	62	62	62
Deficit (Surplus)	**275**	**8**	**126**	**43**	**5**	**(4)**

(a) Excludes AustralAsia Railway Corporation, and Territory Insurance Office.

(b) Includes $165 million contribution to the Alice Springs to Darwin railway.

(c) UPF scope; deficit on Budget Scope was $12 million.

(d) Includes $17 million carryover expenditure from 2000-01; a similar amount is expected to be carried out into 2002-03.

Table 1.1 shows that over the period of its first term, the Government's intention is to achieve a cash surplus, largely by placing strict controls on expenditure growth across all functions while still increasing the priority attributed to health, education and law and order functions over this period.

Table 1.2 shows the projected outlook for the general government sector.

TABLE 1.2 : NORTHERN TERRITORY GENERAL GOVERNMENT SECTOR (a)

	2000-01 Actual (b) $M	2001-02 May Budget $M	2001-02 (c) Mini Budget $M	2002-03 Forward Estimate $M	2003-04 Forward Estimate $M	2004-05 Forward Estimate $M
Total Expenditure	2 187	2 032	2 157	2 175	2 200	2 250
Total Revenue	1 940	2 032	2 018	2 103	2 175	2 238
Deficit (Surplus)	**247**	**0**	**139**	**72**	**25**	**12**

(a) Excludes AustralAsia Railway Corporation.

(b) Includes $165 million contribution to the Alice Springs to Darwin railway.

(c) Includes $17 million carryover expenditure from 2000-01; a similar amount is expected to be carried out into 2002-03.

The worsening of the general government sector relative to the total public sector is largely due to the removal from the general government sector of the Northern Territory Treasury Corporation which is now classified as a public financial corporation.

The Northern Territory has up until now made minimal differentiation between entities in its general government sector and those which operate in a more commercial environment. This has been due, for the most part, to the operational aspects of the *Financial Management Act* where there was no material difference in a budget sense between different types of agencies. However, it is expected that two significant policy initiatives: notably the move to an accrual output framework for the general government sector in 2002-03; and the passage of Government Owned Corporations legislation in November 2001, will contribute to improved financial outcomes overall and a greater budget focus on the general government sector. The commercial sector will have greater flexibility but will be increasingly expected to improve its financial performance.

ECONOMIC OUTLOOK

Recent Economic Performance

During the mid to late 1990s, the Territory economy outperformed the rest of Australia. This was largely due to impetus provided by the defence relocation program, with high population growth creating strong demand and fuelling a construction boom. As the stimulus from the defence force program eased back, the construction boom ended, the labour market softened and growth eased.

Over 2000-01, the Territory economy continued to experience relatively subdued growth. Gross State Product (GSP) growth of 4.5 per cent was recorded but this was mainly due to the full year effect of the increase in offshore oil production as new capacity from the Laminaria-Corallina oil fields came on stream. The spike in oil production acted to mask the weaker underlying rate of onshore economic growth in 2000-01. Offshore oil production has a limited effect on the Territory's onshore economy, as most of the labour and capital required are sourced from interstate or overseas.

After three years of strong growth, Territory private consumption growth weakened markedly in 2000-01, reflecting the overall slowing of the onshore economy and the lagged effects of previous interest rate rises as well as high petrol prices. Dwellings investment fell significantly for the second year in a row, reflecting slowing population growth and defence related activity, but also the magnitude of over-building and build up of excess stock during the boom period.

Outlook

After two years of weak onshore growth, economic activity is expected to show some signs of a pick up over the remainder of 2001-02. Territory GSP is forecast to grow by 5 per cent in 2001-02. Growth will be driven by domestic factors, notably construction of the $1.3 billion Alice Springs to Darwin railway and a pick up in dwellings investment and household consumption expenditure.

Construction of the railway will continue to boost employment in 2001-02, although employment in tourism-related sectors will suffer the effects of the world economic slowdown, exacerbated by recent international events and the collapse of Ansett. Private sector forecasters have been forecasting strong employment growth in 2001-02, however, given recent events and uncertainty surrounding major oil and gas projects, the anticipated phase of sustained employment growth may be delayed.

Population growth has moderated with the army relocation program, falling to around 1 per cent in 2000-01, but is expected to increase in 2001-02, with less outflow through net interstate migration.

The outlook for Territory economic growth has been affected recently by the deferral of the gas pipeline to Darwin from the Timor Sea and the decision by Methanex to pursue an alternative location for its methanol plant. In addition, the impact of an already weakening world economy has been exacerbated by fallout from the US terrorist attacks and the collapse of Ansett. Despite short term uncertainty, the Territory's medium term economic growth prospects have significant upside, particularly considering the number of potential gas-related projects under serious consideration.

The work done on the railway will boost output, employment and incomes in the Territory. The additional activity in the construction and manufacturing industries will provide a timely boost to these industries and related sectors as the residential construction cycle begins to pick up again. Local contracts and employment associated with the railway will also act to improve consumer confidence and business sentiment.

Private consumption, which weakened markedly in 2000-01, is set to turn around through 2002, although consumer confidence will play an important role in the short term in determining how quickly consumption expenditure recovers. After two years of negatives, dwellings investment is now forecast to make a positive contribution to economic growth in 2001-02.

Table 1.3 sets out key economic statistics for the Northern Territory.

TABLE 1.3: KEY TERRITORY ECONOMIC STATISTICS (YEAR ON YEAR PERCENTAGE CHANGE)

	1999-00 Actual	2000-01 Actual	2001-02 Forecast
GSP (chain volume measure)	0.9	4.5	5.0
Employment [1]	-2.2	1.1	3.0
Population [2]	1.5	1.0	1.3
Darwin CPI	1.4	5.4	2.5

1. 2001-02 forecast from Access Economics.
2. 31 December estimates.

External Risks

Exports contributed strongly to growth in 2000-01. The spike in oil output from Laminaria-Corallina production was the major factor, although growth in international tourism also played a role. This will change in 2001-02 as oil field pressure and therefore production from Laminaria-Corallina falls. Deteriorating external conditions will act to undermine demand for Territory exports of goods and services.

A large proportion of Territory exports are used in manufacturing production in South East Asia, often for subsequent export to the United States and other industrialised nations. It is through these industry and end use consumer demand linkages that economic conditions in the major growth centres of the world can affect the Territory economy.

The twin effects of the US terrorist attacks and weaker economic conditions in many parts of the world will affect discretionary international travel. The number of international visitors to the Territory has been growing strongly, but in-bound international tourist numbers now look set to fall in the short term, although Australia’s ‘safe haven’ status and competitive dollar will cushion the impact to some extent. There is also increased likelihood that Australians will defer international travel in favour of domestic travel.

GOVERNMENT’S FISCAL STRATEGY STATEMENT

Part 4 of the Fiscal Integrity and Transparency legislation requires the Treasurer to publicly release and table the first fiscal strategy statement at or before the time of the Government’s first budget. The November 2001 Mini Budget is not the Government’s first budget. Rather, the 2002-03 Budget will be the Government’s first budget, planned to be presented on an accrual basis.

Labor’s Financial Statement included a fiscal strategy statement although it is fair to say that the development of the deficit reduction strategy as part of the Mini Budget has gone further than the fiscal strategy statement. The assessment below is based on the fiscal strategy statement included in *Labor’s Financial Statement*. However, it is expected that this strategy statement will be reviewed prior to the 2002-03 Budget.

ASSESSMENT OF FISCAL STRATEGY STATEMENT

The benefits of a formal fiscal strategy are three-fold. It advances transparency and accountability in Territory Government fiscal policy, supports responsible management of the Territory's finances over the longer term, and promotes investor and financial market confidence in the Territory economy.

The overriding fiscal objective in the November 2001 Mini Budget is to move the total public sector into surplus by 2004-05. This will be facilitated by the Government’s current fiscal targets as outlined in *Labor’s Financial Statement*, which are:

- maintain current expenditure to growth consistent with inflation and population growth;
- maintain a surplus in current revenue over current expenditure, except in exceptional circumstances (such as natural disasters);
- maintain Territory taxes, fees and charges to comparable State-like levels;
- adopt a transparent, equitable, counter-cyclical capital works program that complements activity in the private sector to stabilise employment in the construction sector through each economic cycle; and
- reduce net debt as a proportion of economic activity over time.

An assessment of budget aggregates against the fiscal strategy is set out below.

THE FISCAL STRATEGY

Element 1: Maintain current expenditure to growth consistent with inflation and population growth.

Table 1.4 details estimated current expenditure growth for 2001-02. As the table indicates current expenditure is estimated to be maintained in real per capita terms between 2000-01 and 2001-02.

TABLE 1.4: ESTIMATED CURRENT EXPENDITURE

	2000-01 Actual	2001-02 Mini Budget	Average 2002-03 to 2004-05
Current Expenditure ($M) [1]	1 904	1 981	
Year on Year Growth (%)	5.3	4.1	2.1
Population Growth (NT % change in year to 31 December) [2]	1.0	1.3	1.5
CPI Growth (8 capitals % change year on year) [3]	6.0	2.8	2.5
Combined Population and CPI (%)	7.1	4.1	4.0

1. Total Public Sector – excludes transactions of the AustralAsia Railway Corporation.
2. December 2000 ABS Catalogue 3101.0, December 2001 *Commonwealth Mid-Year Economic and Fiscal Outlook 2001-02*.
3. Headline CPI, ABS Catalogue 6401.0 and *Commonwealth Mid-Year Economic and Fiscal Outlook 2001-02*.

Current expenditure is estimated to increase by 4.1 per cent in 2001-02, which meets the forecast target (combined rate of inflation and population growth). In real per capita terms, 2001-02 expenditure has stayed constant. In 2001-02, health, education and law and order have received an increased share of budget funding while other sectors have maintained a lower level of current funding.

In the forward estimate years, 2002-03 to 2004-05, current expenditure is projected to grow by an average of 2.1 percent, well below the projected combined rate of population and CPI growth of 4.0 per cent.

Element 2: Maintain a surplus in current revenue over current expenditure, except in exceptional circumstances (such as natural disasters).

Table 1.5 details the difference between current revenue and current expenditure. While current expenditure is available from Northern Territory Budget Papers, current revenue needs to be derived. Current revenue is calculated as total Territory revenue less Commonwealth capital grants and the proceeds from capital asset sales.

TABLE 1.5: SURPLUS OF CURRENT REVENUE OVER CURRENT EXPENDITURE

	2000-01 Actual	2001-02 Mini Budget	Average 2002-03 to 2004-05
	$M	$M	$M
Current Revenue [1,2]	1 847	1 937	2 070
Current Expenditure [1]	1 904	1 981	2 049
Current Surplus(+) / Deficit (-) [3]	-57	-44	21

1. Total Public Sector – excludes transactions of the AustralAsia Railway Corporation.
2. Current revenue = total revenue less Commonwealth capital grants less receipts from sale of capital assets.
3. Current surplus/deficit = current revenue less current expenditure.

As a result of the large deficit inherited by the Government, current expenditure is expected to exceed current revenue in 2001-02, although this current deficit is an improvement on the 2000-01 outcome. The presence of such a deficit justifies the introduction of a deficit reduction strategy as recommended by the Allan report.

In each of the forward estimate years a current surplus is forecast as a result of implementing the deficit reduction strategy. On average an annual surplus of $21 million is projected.

Element 3: Maintain Territory taxes, fees and charges to comparable State-like levels.

This element of the strategy reinforces the Territory's commitment to maintaining State-like levels of taxation, fees and charges.

Direct comparison of the Territory's taxes, fees and charges is not an easy task. This is primarily due to the wide variety of imposts across jurisdictions. This is further complicated by a wide range of conditions and exemptions within individual imposts which makes comparisons between jurisdictions difficult.

In determining this element, it is useful to examine the level of taxation revenue per capita. This compares the level of taxation imposed per head of population in each of the jurisdictions. This is demonstrated in Table 1.6.

TABLE 1.6: TAXATION REVENUE PER CAPITA

	2000-01 Actual $ per capita	2001-02 Budget $ per capita
New South Wales	1 907	1 744
Victoria	1 745	1 613
Queensland	1 109	1 144
Western Australia	1 436	1 419
South Australia	1 336	1 206
Tasmania	1 114	1 011
Six State Aggregate	**1 599**	**1 501**
Northern Territory [1]	**1 117**	**1 084**

Sourced from State Budget Papers - Non-Financial Public Sector.

1. Northern Territory figure for 2001-02 refers to the November 2001 Mini Budget.

In 2001-02, the Territory is expected to have the second lowest level of taxation revenue per capita after Tasmania. While this measure indicates that Territorians enjoy a lower rate of taxation per capita compared to other jurisdictions, it does not make any allowances for a jurisdiction's capacity to raise revenue.

The Commonwealth Grants Commission (CGC), in assessing each jurisdiction's need for Commonwealth financial assistance, does assess each jurisdiction's capacity and effort in raising taxation. Table 1.7 details the Territory's revenue raising capacity and effort expressed as a percentage of the Australian average in 1998-99 and 1999-00.

TABLE 1.7: NORTHERN TERRITORY REVENUE RAISING CAPACITY AND EFFORT

	1998-99 %	1999-00 %
TOTAL TAXATION		
Capacity (a)	81	77
Effort (b)	93	101
TOTAL OWN-SOURCE REVENUE		
Capacity (a)	94	90
Effort (b)	79	83

Source: Commonwealth Grants Commission 2001 Update.

(a) Northern Territory's capacity to raise revenue compared with the Australian average.

(b) Northern Territory's revenue effort compared with the Australian average, given the capacity available.

As Table 1.7 indicates, the Territory has a low capacity to raise taxation revenue, which results in low taxation revenue per capita. When taxation revenue raising effort is included in the analysis, it confirms that the Territory Government is raising taxation revenue at close to the Australian average. This demonstrates that Territorians pay taxation at comparable State-like levels.

Total own-source revenue encompasses fees and charges in addition to taxation revenue. At this broader level of revenue, the CGC assesses that the Territory has a higher, but still less than average capacity to raise revenue. More importantly, the CGC assesses that the Territory makes only an 83 per cent effort to raise total revenue. In particular, the CGC assesses that the Territory makes a below average effort with mining royalties (where there is some concern about the CGC's methodology); interest earnings; contributions by trading enterprises; and other revenue.

This would suggest that the Territory has scope to raise additional revenue without exceeding the average revenue effort of all States and Territories.

Element 4: Adopt a transparent, equitable, counter-cyclical capital works program that complements activity in the private sector to stabilise employment in the construction sector through each economic cycle.

The adoption of a counter-cyclical capital works program is highly dependent upon the correct timing of capital works programs as well as knowledge of the current and future state of the local economy.

For counter-cyclical strategies to be successful, early recognition of a downturn in the economy is essential due to the time lags associated with implementing capital works programs. Table 1.8 represents the level of capital expenditure on new fixed assets for 2000-01 and 2001-02.

TABLE 1.8: CAPITAL EXPENDITURE ON NEW FIXED ASSETS

	2000-01 Actual	2001-02 Mini Budget	Average 2002-03 to 2004-05
New Fixed Asset Expenditure ($M) [1]	224	256	
Growth (%)	-7	15	-6

1. Total Public Sector – excludes transactions of the AustralAsia Railway Corporation.

Expenditure on new fixed assets is set to increase by $32 million between 2000-01 and 2001-02 from $224 million to $256 million, which represents a 15 per cent increase. When combined with the effect of the construction of the Alice Springs to Darwin railway (which is not included in the above analysis), the Territory is well placed to offset any cyclical downturn in private sector construction.

In the forward estimate years new fixed capital expenditure is projected to decline by an average of 6 per cent per annum following the significant increase in 2001-02 and in-line with an expected recovery in the private sector, largely related to Railway construction.

Element 5: Reduce net debt as a proportion of economic activity over time.

Table 1.9 illustrates the change in net debt as a proportion of gross state product for 2000-01 and 2001-02.

TABLE 1.9: NET DEBT AS A PROPORTION OF ECONOMIC OUTPUT

	Net Debt [1] $M	Economic Output [2] $M	Proportion %
2000-01	1 588	8 719	18.2
2001-02	1 714	9 286	18.5
Average 2002-03 to 2004-05			16.4

1. Total Public Sector – excludes transactions of the AustralAsia Railway Corporation.
2. 2000-01 ABS Catalogue 5220.0, 2001-02 NT Treasury estimate.

Debt as a proportion of gross state product has increased from 18.2 per cent in 2000-01 to an estimated 18.5 per cent in 2001-02, representing a small increase in debt as a proportion of economic output.

This analysis confirms the current deterioration in the Territory's budgetary position and the necessity for a debt reduction strategy (as recommended by the Allan report) to address the current budgetary imbalance. This strategy is also an essential ingredient in putting the Territory's ratio of net debt to economic output back on a downward trend. The forward estimates project that this will occur with the net debt to gross state product ratio averaging 16.4 per cent from 2002-03 to 2004-05.