REPORT ON PROCEEDINGS BEFORE

STANDING COMMITTEE ON STATE DEVELOPMENT

INQUIRY INTO THE DEBT RETIREMENT FUND

CORRECTED

At Macquarie Room, Parliament House, Sydney on Friday 21 July 2023

The Committee met at 1:15 pm

PRESENT

The Hon. Emily Suvaal (Chair)

Ms Abigail Boyd (Deputy Chair)
The Hon. Greg Donnelly
The Hon. Wes Fang
The Hon. Stephen Lawrence
The Hon. Damien Tudehope

PRESENT VIA VIDEOCONFERENCE

The Hon. Anthony D'Adam
The Hon. Bob Nanva

CORRECTED

The CHAIR: Welcome to the hearing of the Standing Committee on State Development inquiry into the Debt Retirement Fund. I acknowledge the Gadigal people of the Eora nation, the traditional custodians of the lands on which we are meeting today. I pay my respects to Elders past and present and celebrate the diversity of Aboriginal peoples and their ongoing cultures and ongoing connections to the lands and waters of New South Wales. I also acknowledge and pay my respects to any Aboriginal and Torres Strait Islander people joining us today. Today we will hear from key stakeholders, including the Treasurer, a representative from NSW Treasury and Professor Stephen Bartos, a governance and public finance expert. While we have witnesses with us in person, some will be appearing via videoconference. I thank everyone for making the time to give evidence to this important inquiry.

Before we commence, I will make some brief comments about the procedures for today's hearing. Today's hearing is being broadcast live via the Parliament's website. A transcript of today's hearing will be placed on the Committee's website when it becomes available. In accordance with the broadcasting guidelines, the House has authorised the filming, broadcasting and photography of committee proceedings by representatives of media organisations from any position in the room, and by any member of the public from any position in the audience. Any person filming or photographing proceedings must take responsibility for the proper use of that material. This is detailed in the broadcasting resolution, a copy of which is available from the secretariat.

While parliamentary privilege applies to witnesses giving evidence, it does not apply to what witnesses say outside of their evidence at the hearing. I therefore urge witnesses to be careful about comments they may make to the media or to others after they complete their evidence. Committee hearings are not intended to provide a forum for people to make adverse reflections about others under the protection of parliamentary privilege. In that regard, it is important that witnesses focus on the issues raised by the inquiry terms of reference and avoid naming individuals unnecessarily.

All witnesses have a right to procedural fairness according to the procedural fairness resolution adopted by the House in 2018. If witnesses are unable to answer a question and want more time to respond, they can take a question on notice. Written answers to questions taken on notice are to be provided by Monday 31 July 2023. If witnesses wish to hand up documents, they should do so through the Committee staff. In terms of the audibility of the hearing, I remind both Committee members and witnesses to speak into the microphone. As we have a witness appearing via videoconference, it may be helpful to identify who questions are directed to and who is speaking. Finally, could everyone please turn their mobile phones to silent for the duration of the hearing.

Professor STEPHEN BARTOS, University of Canberra, affirmed and examined

The CHAIR: I now welcome our first witness. Would you like to start by making a short statement? Please keep it to no more than a few minutes.

STEPHEN BARTOS: Thanks very much, Chair. I have sent the Committee a submission. That submission is based largely on some previous work that I did that was commissioned by Coolabah Capital Investments. They've kindly said that it's fine to reproduce any of that material and the Committee should feel free to be able to use it as you wish. That was done in 2021, at a time when it appeared that New South Wales was actively increasing its levels of debt holdings in order to put more money into shares through the Debt Retirement Fund. That situation has changed since then, of course, for the obvious reasons that we know about in terms of the New South Wales fiscal situation. But I think the principles outlined in that report that I did still apply. What they essentially indicate is that a prudent stance for a State government, in terms of fiscal policy, is to manage debt in a way such that risks to taxpayers are reduced.

In that regard, I think it's really important to note that New South Wales hasn't been, unlike many other jurisdictions, publishing gross debt as a target but simply focusing on net debt, which has had the perverse effect of disguising the fact that contributions that are made to the Debt Retirement Fund, if they're based on raising debt, will increase gross debt. Because they're treated as an offset, they don't change the metric of net debt. I was actually very interested to read the submission from Treasury to this Committee, which I think was a welcome development. There's just one sentence—I would have loved it if Treasury had expanded it more—from Treasury that says that perhaps one alternative is to look at targeting gross debt in the State budget, which I think is a suggestion from Treasury as a possible alternative that's well worth pursuing.

There's a broad philosophical question that I think it's really appropriate for a committee like this to handle: What is the role of government? That is opening up a big question, of course. But is it the role of government to be a fund manager and invest in the stock market? Or does government actually want to achieve other things, and the activities of managing something like a Debt Retirement Fund are really an incidental or an adjunct to achieving that overall purpose? It is true that you'll make a better return from equities than from debt over the long term. That's for a couple of reasons. One is that, clearly, investing in the share market is riskier and therefore investors get a higher return. But even beyond that level of risk, there is something in the economics literature that's worth the Committee being aware of called the equity premium puzzle. It says that, even after allowing for risk, there is still a much higher return from equities than you would expect. There are various possible theories; it's called a puzzle because there is no consensus yet as to why this higher premium on equities exists. But some of the possibilities come from behavioural economics and people's short-term focus.

Whatever the reason, it's certainly the case that governments can make money over and above what they would get from debt by investing in shares—but is this a good role for government? Is this something that governments should be doing? I'm reminded that when young graduates used to come into—I used to be a deputy secretary in the finance department. They would ask, "Hey, I've just had a brilliant idea! Government borrows money at really low rates and you can get big returns on the stock market. Why don't we borrow lots more money and go and punt it on the stock market?" It had to be carefully explained to them that there are really good reasons why this is a bad idea. One, investing in the stock market entails risk and you're exposing the government to the fluctuations of the stock market. Two, when taken to extremes this leads to much higher levels of government ownership than would be really desirable. It's not something where it's the core business of government to be investing in shares. Three, it opens up possibilities for corruption and mismanagement, which is probably worth thinking about as a committee as one of the risks that you're looking at in terms of your terms of reference. We can maybe look at that if members of the Committee have queries about that.

Finally, I would like to take up one of the points that's raised in the Treasury's submission, which seems to suggest investing in the Debt Retirement Fund only when the State is in the fortunate position, as it has been in the past, of having no net debt—that is, it's paid off all its debts. If you have got spare money in that situation, I think having a Debt Retirement Fund into which you invest your moneys is desirable. I wouldn't be suggesting to the Committee that one of your recommendations should be closing down the fund. If New South Wales manages to get itself back into the lucky situation of having no net debt and continues to generate surpluses, then it will have to work out what to do with those surpluses and using the Generations Fund and the Debt Retirement Fund part of it as management of those future surpluses is maybe not a bad idea.

But that would be something that I would be doing only when you have no net debt. Treasury describes that as a risk-averse position. I think that's a mischaracterisation. It's a sensible position. It's a prudent position. We adopted a position, which seemed to be where the previous Government was heading, of every time you have a surplus, which happens much more frequently in New South Wales, putting the surplus into the stock exchange, then you won't make headway on addressing the problem of excessive debt.

I will finish by drawing the Committee's attention to the wellbeing statement *Measuring What Matters* that was released by the Federal Treasurer just a few hours ago. In that, one of the metrics of whether Australia is a resilient and sustainable nation is fiscal sustainability. The metric that the Federal Treasurer and Treasury department suggest be used is levels of government gross debt as a share of GDP. And why? Because "stabilising and reducing debt as a share of the economy will help rebuild fiscal buffers, enhance the ability of governments to respond to shocks and secure sustainable provision of government services".

In other words, don't just focus on net debt and, if you've got surpluses and you still have a high level of gross debt, the much better option is to use those surpluses to pay down that level of debt you've got until you are in a situation where you have a much more sustainable level of gross debt because what you do by doing that is, one, build in buffers against future adverse movements and, two, give yourself greater ability to respond to shocks in future. So that is why I think that the characterisation of the Treasury submission of that as a risk-averse statement isn't correct. The much more sensible move is the one in effect advocated by the *Measuring What Matters* statement of actually paying down debt when you've got the opportunity to do so.

The Hon. DAMIEN TUDEHOPE: Thank you, Professor Bartos, for making yourself available. You were a late addition, were you not, to the witness list for the purposes of this hearing?

STEPHEN BARTOS: Yes, I was—well, I don't know what you mean by "late". I was contacted and asked to make a submission, and I think the likely reason is that the Committee secretariat, or maybe the Committee Chair, became aware of the previous work I'd done. I'd also put in a caveat here that I am known to the New South Wales Parliament in that I have been the Parliamentary Budget Officer, a term of office that concluded on 30 June. But nothing I've said reflects any of the information that I gleaned while I was PBO.

The Hon. DAMIEN TUDEHOPE: And that's interesting in itself. So you say you were contacted late. Who contacted you?

STEPHEN BARTOS: The Committee.

The Hon. DAMIEN TUDEHOPE: And said that you should put in a submission?

STEPHEN BARTOS: Yes—no. One of the advantages of being here is that I can actually find that if you wish.

The Hon. ANTHONY D'ADAM: Point of order: I believe this line of questioning is actually outside the terms of reference of this inquiry. The provenance of how a witness came to be before the Committee is a matter that's been determined by the Committee. The Committee's made a decision to call Mr Bartos. It's not appropriate to question the witness on the basis of an assertion that there are some issues around the process that arose for the witness coming before the Committee.

The Hon. WES FANG: To the point of order: Firstly, can we stop the clock for the question time? The second thing is that any related matter on this that covers the questioning, and establishing the context of why the witnesses are appearing, is certainly relevant. I do not believe there is a point of order. Certainly nothing within the standing orders prevents Mr Tudehope asking the questions that he is asking.

The Hon. STEPHEN LAWRENCE: To the point of order: It would be my suggestion that we might deal with this issue, if necessary, at a later time and not during his evidence?

STEPHEN BARTOS: Yes.

The Hon. STEPHEN LAWRENCE: Because it wouldn't seem to pertain to the terms of reference.

The CHAIR: I'm prepared to make a ruling on the point of order. I agree that the line of questioning was outside the terms of reference for the inquiry. That being said, I understand there is quite wide latitude given for questions. Given the time we have for the hearing, I would ask that Mr Tudehope, if you—the other thing is that the list of witnesses did go to the Committee for feedback. So if there was an issue, that probably would have been a better time to feed that in.

The Hon. DAMIEN TUDEHOPE: Dr Bartos, you had previously prepared a paper in relation to the subject matter of your report.

STEPHEN BARTOS: Yes.

The Hon. DAMIEN TUDEHOPE: To a great extent, your report, or the submission you have made to this inquiry, reflects the advice that you had previously given, does it not?

STEPHEN BARTOS: Yes.

The Hon. DAMIEN TUDEHOPE: You were invited to prepare that submission, were you not, by Coolabah Capital?

STEPHEN BARTOS: No. I was invited to prepare a report for Coolabah Capital Investments a couple of years ago. I was invited by the Committee to prepare my submission.

The Hon. DAMIEN TUDEHOPE: Who from Coolabah Capital Investments invited you to make that submission?

STEPHEN BARTOS: Christopher Joye.

The Hon. DAMIEN TUDEHOPE: Did he provide you with a letter of instructions in respect of the subject matter which he asked you to address?

STEPHEN BARTOS: He asked me a series of questions. In fact, I have linked to my report in my submission that I have provided to this Committee. That report outlines the questions that I was asked to address, and the way I proceeded with doing that report was to answer the questions. From memory, I think there were seven or eight questions that I was asked and I answered each of them in turn.

The Hon. DAMIEN TUDEHOPE: Mr Joye wrote to you, did he, in respect of obtaining that report?

STEPHEN BARTOS: Yes.

The Hon. DAMIEN TUDEHOPE: Have you got a copy of that letter available?

STEPHEN BARTOS: It was an email, but yes. It was an email asking that series of questions from Christopher Joye. I have it somewhere. It is not easily in front of me, but I'm sure it's around.

The Hon. GREG DONNELLY: Point of order—

The Hon. WES FANG: Can we stop the clock please?

The CHAIR: No, because we're going to eat into the questioner's time.

Ms ABIGAIL BOYD: That's not how we—

The Hon. WES FANG: We can all play this game.

The CHAIR: We're not stopping the clock.

Ms ABIGAIL BOYD: We have never stopped the clock before.

The Hon. GREG DONNELLY: I respect the honourable member's right to ask questions as he sees fit with respect to this inquiry. But what was clearly to be the next question—and I think the words were almost coming out—was could you please provide a copy of the email, which was an engagement for a report that had been previously done which does have some tangential relationship to the report, or rather the content of the submission. But I have to say, it's a very long bow to be asking for that and I think it should be ruled out of order.

The Hon. WES FANG: To the point of order: Chair, this is now wasting time. The submission from Mr Bartos relates partly to the submission that was done by the Coolabah Capital institute. Mr Tudehope's questions are related to that. They are well within order and well within the scope of the inquiry. I ask that these frivolous points of order be withheld, otherwise I ask you to call members to order and eject them. Mr Tudehope should be allowed to continue asking his questions.

The Hon. DAMIEN TUDEHOPE: To the point of order: The Hon. Greg Donnelly is correct about what my next question was. But it is relevant to say, when you prepare a report, what are the parameters of preparing that report? What are the questions being asked? I think it goes to the substance of what we are actually inquiring into and it goes certainly to the submission which the witness is addressing.

STEPHEN BARTOS: Mr Tudehope, could I say that this is actually all on the public record. I am a great believer in transparency. It's all there. So the questions that I was asked have all been published, so there are no secrets there.

The Hon. DAMIEN TUDEHOPE: So you'd have no objection to producing a copy of that email.

The Hon. GREG DONNELLY: Point of order: I think—

The Hon. WES FANG: You're not answering the question, Greg.

The Hon. GREG DONNELLY: I'm taking a point of order about this question specifically—

The Hon. WES FANG: What's the standing order?

The Hon. GREG DONNELLY: Please don't interrupt. It was anticipating this very point, and that is it was seeking to press the position of seeking a copy of an email which was effectively around a matter of an engagement for the production of a report which is tangential to what is before us here today.

The Hon. WES FANG: It's interesting that you're running a protection racket, mate.

The Hon. GREG DONNELLY: I've got to say I'm not aware this has ever happened, where there's actually a briefing—

The Hon. WES FANG: It's interesting that they've sent you here to run a protection racket.

The Hon. DAMIEN TUDEHOPE: To the point of order: The witness has indicated that he is very open to being transparent. The request is something that the witnesses has already said, "I am prepared to engage in it because I am a person of integrity and I am someone who has no objection to ensuring that documents that I have received and which, in fact, elicit a response are made available to a committee." I just think that raising this point of order when the witness has already indicated that they have no real objection to being transparent about the whole of this process—

The CHAIR: Thank you, Mr Tudehope and Mr Donnelly. In terms of the point of order, I'm happy for you to proceed but, given Dr Bartos is appearing remotely and may have some difficulty, it's perhaps a better question for written notice.

The Hon. DAMIEN TUDEHOPE: If the witness is able, by next Monday, which I think is the date for the submission—are you able to provide, Dr Bartos, a copy of the correspondence from Coolabah Capital Investments to you seeking your advice in respect of the various issues which you are now placing on the record before this Committee?

The Hon. GREG DONNELLY: Just to be clear, correspondence suggests plural, so I think what the honourable member is asking for is—

The CHAIR: It's the list of questions.

The Hon. GREG DONNELLY: No, all of the potential correspondence over the engagement.

The Hon. WES FANG: Stop running a protection racket, Greg.

The Hon. GREG DONNELLY: I think, if that's the case, you should say that you want the series of correspondence, back and forth, not just ultimately the engagement letter if that's what you're getting at.

The Hon. WES FANG: Stop running protection. Let him answer.

The Hon. STEPHEN LAWRENCE: Point of order: I take a point of order in relation to the Hon. Wes Fang, who is continually interjecting suggesting a protection racket. That has a certain imputation not just on the honourable member Mr Donnelly, but also on the witness potentially. I'd ask that he be brought to order.

The Hon. WES FANG: Well, stop running a protection racket, mate.

The Hon. STEPHEN LAWRENCE: I note that he is interrupting me during my statement. It is totally inappropriate.

The Hon. DAMIEN TUDEHOPE: I haven't got many more questions. Perhaps I can deal with it this way. Was there a series of correspondence entered into between you and Coolabah Capital Investments in respect of the provision of your advice, Dr Bartos?

STEPHEN BARTOS: I think it would be wrong to characterise it as a series of correspondence. There was an email to myself and there was a report that I provided. There was some—I don't recall whether there were any emails at all in relation to that report when it was in draft. I believe I had a telephone conversation with Christopher Joye and then I sent him an invoice for it. But if I can anticipate where you may be going with this question, if there is any suggestion at all that, in preparing this report, I was influenced by the views of Coolabah Capital Investments, I certainly wasn't. I made it clear that I was undertaking this assignment for them on the basis of my own professional judgement and expertise, and the report was fully independent and not beholden to anything that they might have said to me. And they respected that. They didn't actually instruct me what to write in any way at all.

The Hon. DAMIEN TUDEHOPE: In those circumstances—and I accept that answer—would you be prepared to provide that correspondence to the Committee?

STEPHEN BARTOS: Yes. I've already said that. I can't see any problem with that, with one proviso and that is—

The Hon. DAMIEN TUDEHOPE: In view of the short time that I have—

STEPHEN BARTOS: Can I also just, out of courtesy, make sure that Coolabah Capital is happy with that as well?

The CHAIR: Yes, thank you, Dr Bartos.

The Hon. DAMIEN TUDEHOPE: It is relevant because they in fact made a submission to this Committee.

STEPHEN BARTOS: Yes.

The Hon. DAMIEN TUDEHOPE: Dr Bartos, I go to another issue. In evidence before this inquiry—S&P, the credit agency, on 27 March 2023 identified a risk to New South Wales' double-A credit rating from "higher overall spending on public sector wages, which would "call into question the quality of the state's financial management." Could you confirm that the Parliamentary Budget Office costings of Labor's wages policy also identified significant risks that wage growth could exceed the Government's targets and that fully offsetting savings may not be identified with a material risk that the quality of service is lowered?

STEPHEN BARTOS: I am not entirely sure that that's the subject matter of the inquiry into the Debt Retirement Fund. But, again, the PBO costing of Labor's wages policy is on the public record. It's not quite as you characterise it. What the PBO did was—

The Hon. DAMIEN TUDEHOPE: I'm quoting you, Dr Bartos.

The CHAIR: We will move now to questions from the crossbench. Time has expired for Opposition questions.

Ms ABIGAIL BOYD: Thank you, Professor Bartos, for your contribution to this inquiry. I would like to engage in the substance of your submission and also go right back to the terms of reference for this inquiry. We're being asked to consider, in amongst other things, what the optimal size the Debt Retirement Fund should be. I note the EY Port Jackson Partners report that was done for NSW Treasury in March of this year and the few different ways that they've looked at how we could set that optimal size. What's your view on the optimal size of this fund?

STEPHEN BARTOS: I think that the approach suggested by Treasury is the correct one, which is that what you should be looking at is metrics that look at ratios of debt to gross State product or that kind of ratio measure. Setting an optimal size of a fund in advance—if you look at some of the references, including those from the IMF, which I've drawn to the attention of the Committee—is, in a sense, not possible in that what you are trying to do with this fund is—there's various different types of funds. But what you're trying to do with the New South Wales sovereign wealth fund is make provision for the future. How much provision you can make depends on the state of the budget and depends on how much the State can manage fiscally to set money aside or, as it should be doing at the moment, as I think I made clear, pay down debt. Therefore, trying to set a dollar figure doesn't work. What's important is to set principles for how you should manage the flows into and out of the fund.

Ms ABIGAIL BOYD: So, for example, a percentage of gross debt or a metric around how much gross debt there is.

STEPHEN BARTOS: Yes. And a target, for example, of progressively reducing gross debt as a percentage of gross product would, I think, be entirely appropriate. Then you can measure progress over time in each successive budget against that target.

Ms ABIGAIL BOYD: You referred just now to the DRF as a sovereign wealth fund, but it's not really a sovereign wealth fund for so long as we have gross debt that far exceeds the amount in this fund. When we look at a sovereign wealth fund in other countries, it's when there has been a surplus and a boon, and that's gone into a fund for a rainy day. What we have here is a debt reduction fund that sets an amount offsetting our gross debt in order for there to be a certain amount of net debt. Can you talk through what the difference is and how we could actually make the NGF as a whole work as what would be more understandably known as a sovereign wealth fund as opposed to something that sits there as an offset account?

STEPHEN BARTOS: Yes. Well, there is a sense in which it is a sovereign wealth fund and that's why I referred you to that IMF document on the different types of sovereign wealth fund. One of the biggest sovereign wealth funds is in Singapore but there are others that I am sure committee members are fully aware of, such as the Norwegian pension fund, which are separately managed very large funds that also operate, according to international statistical standards, as an offset to the debt in those jurisdictions. In that sense I see the point you're making and that is that while you are accumulating a lot of other debt on the side then really the other way of thinking about the Debt Retirement Fund is just as an offset account. So I think the IMF would classify it as a sovereign wealth fund, but that's just to quibble over words.

The more basic point is whether we want to get New South Wales to the enviable position that Norway was in, where they had a very large, stable sovereign wealth fund that enabled, and has continued to enable, them to ride out crises, including COVID, with fiscal management that has been a lot more stable. If you're wanting to get to that level—and Norway got there because they had North Sea petroleum—New South Wales could conceivably get there in future as well. But that's not where we are right at the moment. That's made very clear by the Treasury submission.

Ms ABIGAIL BOYD: Say we end up setting a target where we say the optimal level of what I think of as an offset fund is a certain amount, a percentage, of our gross debt, what should we be looking at then? You mentioned the IMF sovereign wealth fund guidelines, rules or concepts. What should we be using? Have you got a figure that we could use or some sort of ratio that's like a benchmark for this sort of fund?

STEPHEN BARTOS: Ideally you should be targeting a situation where there's no net debt and the net wealth of New South Wales rises over time. I don't think you should put a figure against it but in an ideal world that's where you would get to. As I say, we're a long way away from that right at the moment due to the fiscal pressures that the State is under, following COVID.

Ms ABIGAIL BOYD: One of the other core principles, as I understand it, of the sovereign wealth fund is that you pay in in the good times. You're saving in the good times to spend in the bad. If you look at what New South Wales has done so far, if we wanted to make this a true sovereign wealth fund rather than an offset account then would we be looking at paying debt down to a more sustainable level and then putting further contributions in only when there is surplus? Is that sort of it?

STEPHEN BARTOS: Not only when there's surplus. If you achieve a surplus, you use that surplus to pay down debt. Probably the first and best use of a surplus is to pay down debt to reduce your exposure, so that makes you a more sustainable fiscal entity. I'd go even further and say: Use surpluses to pay down debt. Conceivably use some of the Debt Retirement Fund to pay down debt, not in a precipitate manner; only when it makes financial sense to do so—that is, you can pay down expensive debt or avoid taking on newly expensive debt. Keep doing that as your strategy and not throw extra money into the Debt Retirement Fund until you've eliminated net debt entirely.

Ms ABIGAIL BOYD: What about the risk appetite and investment principles of the fund? You talked a lot about investing equities versus debt. There's a mysterious bunch of investments listed. I forget—there's the alternatives then there's another grouping of types of investments that this fund is investing in, which I found quite interesting. Is there an argument to be made that we could have a higher total fund balance if we had a more conservative investment strategy? Is that something that you've looked at?

STEPHEN BARTOS: I haven't looked at that. The fund managers would be able to advise you on that. But I think what that goes to is one of the risks with funds like this, and that is that you have to balance the need for government to give it direction in terms of what the overall social preferences are of the people of New South Wales, because it's their fund. And who's going to tell the fund managers what those social preferences are other than elected governments? But, having said that, you don't want too much by way of direction for the fund because that will then mean that it can conceivably be investing in areas where the returns are lower, which is bad for the longer term interests of the voters of New South Wales.

This is one of the problems as to why it's actually a bad idea for governments to have very large shareholdings. And it's one of the reasons why, for example, the Norwegian pension fund's mandate is to invest only in countries outside Norway—because investing domestically just raises the temptation for the governments of the day to get their fingers into too many domestic pies and get the investment decisions wrong. So good management of a fund sees it investing very broadly, in order to spread risk, and mainly non-domestically, in order to avoid that potential risk of political interference.

Ms ABIGAIL BOYD: In terms of the treatment of this fund as a fund that nets against gross debt, we have that both for accounting perspective and for rating agencies or, at least, for S&P's perspective. From an S&P perspective, it's by no means certain, is it, that they will continue to treat the NGF as an offset to gross debt when thinking about net debt?

STEPHEN BARTOS: I can't speak for S&P, but it certainly is by no means certain. But it's also worth noting that S&P is—when it rates any jurisdiction, not just New South Wales—concerned about gross debt.

The Hon. STEPHEN LAWRENCE: I was wondering, Professor, are there any lessons that we can take from the operation of the Future Fund operated by the Commonwealth Government in terms of what sort of decisions should be made about contributions to the DRF in, let's say, the short and medium term in terms of the pattern that has occurred with deposits into the Future Fund at different times of different economic activity?

STEPHEN BARTOS: Yes. I think the Future Fund actually provides some good lessons. The Future Fund was set up, and the then Treasurer—now Future Fund manager, Peter Costello—made no bones about it. He was in a fortunate position, as a result of the then mining boom, of running very large surpluses, and rather than spending those surpluses, which were only temporary—governments aren't guaranteed to run surpluses forever; they run them when times are good and times were certainly very good in the Commonwealth for a while—Peter Costello decided to set up the Future Fund to ensure that at least some of that revenue that was flowing into government coffers could be set aside for future purposes. But that's been essentially the principle that the Commonwealth has applied. Certainly the Commonwealth hasn't raised additional debt in order to pump it into getting the Future Fund to buy shares, which is something that I think the Future Fund would be very wary of.

The Hon. STEPHEN LAWRENCE: So there's been a pattern, would you agree, of less or lower deposits into the Future Fund at times of higher Commonwealth debt, effectively?

STEPHEN BARTOS: Yes, absolutely.

The Hon. STEPHEN LAWRENCE: Are you able to talk briefly to how financial and economic conditions impacting New South Wales have changed since the DRF was created?

STEPHEN BARTOS: Yes, though in a way it's a pity that Treasury witnesses aren't on before me, because their submission outlined it particularly well. The pre-election budget update issued by Treasury illustrated just how dramatically New South Wales' fiscal fortunes have turned, primarily as a result of COVID. The State now has much higher levels of debt—for good reasons. I mean, nobody says that the States should not have invested during the pandemic times to try to tide businesses and individuals and households over during the times of hardship. But it has left New South Wales in a much higher debt position and a much more precarious fiscal position than it was at the time that the NSW Generations Fund and the Debt Retirement Fund component were created.

The Hon. STEPHEN LAWRENCE: In terms of international examples of State or provincial governments, are there any examples overseas that would support, as a policy here, continued deposits in the short term into the DRF—in terms of what's happening with other such funds operated by State or provincial governments overseas?

STEPHEN BARTOS: Not that I'm aware of. Look, there are a number of State and provincial funds but primarily in developing countries and primarily set up for a completely different purpose and that is to help local businesses. For example, there's a Lagos sovereign wealth fund that's about helping businesses in that part of Nigeria. For those sorts of sovereign wealth funds, often they actually do go out and they try to access debt markets. But that's because international financial institutions don't trust the governments very much but they do trust the sovereign wealth funds and are maybe prepared to lend to them in a way that they wouldn't lend to a government. So there are examples that I'm aware of in those sorts of developing country instances, but that's for a totally different purpose from what you would use a fund in New South Wales for. New South Wales doesn't have any need to have a government fund that borrows money to pump into local businesses. They have access to financial markets for themselves.

The Hon. STEPHEN LAWRENCE: Lastly, would continuing in the short term to deposit money into the DRF represent a conservative approach to fiscal management or a less conservative, higher risk approach?

STEPHEN BARTOS: It would represent a less conservative, higher risk approach. A more conservative, lower risk approach would be if New South Wales finds itself with spare money on its hands—you'd have to keep fingers crossed that the situation will arise some time in the future. The more conservative—maybe conservative is the wrong word. Just simply the more prudent approach would be to use that to pay down debt or avoid incurring new debt rather than pump it into the DRF.

The Hon. GREG DONNELLY: In light of your submission and your overall general experience in this area, I'm wondering whether you could share your thoughts on matters of issues of transparency around the DRF, in particular reflecting on the fact that the annual budget of the government is always seen to be the most significant public statement of the affairs of the government financially to enable people, whoever they might be, to understand what the government is planning to do. In light of that comment, in terms of the DRF and the amount of contributions made to the fund since its operation, do you have any comment about how good, bad or otherwise the reflection of information in the budget was about this matter of the amount of contributions?

STEPHEN BARTOS: I think it's the case that the amount of contributions to DRF and the interaction between DRF and the budget balance was not as transparent as it could have been, partly because of the issues that I raised previously of the budget not reporting on gross debt levels. I'm not saying that the budget should report only on gross debt either; don't get me wrong, it should report on both. Fuller reporting rather than narrow reporting is what will give voters in New South Wales the best information. Reporting on total debt levels, reporting on the interaction of the DRF and reporting on future programs would I think be highly desirable. I also note the contrast with, say, the Reserve Bank of Australia, which has a quarterly statement on monetary policy. A quarterly statement on New South Wales debt policy, including full disclosures about movements in DRF investments, would be potentially a good thing—and briefings to the market from the managers.

The other thing that I think is worth reflecting on is that I actually think that, seen in isolation, you could argue that the managers of the DRF are doing the right thing: They're operating according to their mandate. The issue here is that the different moving parts in relation to the total New South Wales budget include not just DRF but also what TCorp is investing in and how much of a surplus or deficit the Government is running. What is needed is something that brings together those three different moving parts so you can see how they interact, and that's where the gap has been.

The Hon. GREG DONNELLY: Following on from that issue of the amount of contributions, and once again in the context of the budget, the matter of where the money is being invested on this issue of transparency—any comments you'd like to make in regards to that in addition to your reflections in your submission?

STEPHEN BARTOS: I think my submission indicates it is good to have that information. Not all of the investments made by DRF are obvious, as one of the Committee members mentioned earlier. There are some categories of its investment that seem particularly opaque. But, by and large, it does a report. Again, I think that the reporting is, by comparison with some international wealth funds, pretty good. By comparison with, for example, the Norwegian fund, though, not as good, and so there are some good international examples you could draw on.

The Hon. GREG DONNELLY: Can I just pressure, Professor, in part of you answer you said that it's good; you used the word "good" for this matter of transparency. But can I challenge you that that may not be the best word. Are we in fact wanting something stronger than good? I'm not being picky here, but for the purposes of being specific—

STEPHEN BARTOS: No, I understand the point you're making. I think what I'm reflecting on there is that more than half of the sovereign wealth funds in the world don't report at all, but that's because a very large number—

The Hon. GREG DONNELLY: Coming off a low base then.

STEPHEN BARTOS: The base is low, but by comparison with the really well-regarded, top-of-the-rank global sovereign wealth funds, I think there's room for improvement—yes, absolutely. But bear in mind that a lot of sovereign wealth funds are set up for what you might call broadly political purposes in developing countries where the standards are very different from what you'd expect in New South Wales.

The CHAIR: Thank you for attending this hearing, Dr Bartos. Committee members may have additional questions for you after the hearing. The Committee has resolved that the answers to these along with any answers to questions you have taken on notice today will be returned by Monday 31 July 2023. The secretariat will contact you in relation to those questions.

(The witness withdrew.)

The Hon. DANIEL MOOKHEY, MLC, Treasurer, before the Committee

Ms MARINA VAN DER WALT, Deputy Secretary, Financial Management and Services, NSW Treasury, sworn and examined

The CHAIR: I now welcome our next witnesses.

The Hon. DAMIEN TUDEHOPE: Madam Chair, before those witnesses are sworn, can I just get some clarity in relation to the manner in which evidence will be given? I assume that the Treasurer will give evidence separately from the Treasury officials, who have also sought to make a submission.

The Hon. ANTHONY D'ADAM: I've lost audio.

The CHAIR: I think that's a matter for—they're in the same time slot.

The Hon. DAMIEN TUDEHOPE: With respect, the Treasurer is here to make a submission and will be asked a separate series of questions. What I would be suggesting is that there are separate questions for the Treasurer and separate questions for the Treasury official, who has made a submission, and they ought to be treated separately. In fact, the Treasurer should be allowed to leave—

The CHAIR: I think it should be up to the—

Ms ABIGAIL BOYD: To the point of order—

The Hon. DAMIEN TUDEHOPE: It's not a point of order. It's just clarity I needed.

Ms ABIGAIL BOYD: Fine. To the point, it's very standard for there to be multiple people attending on a panel.

The CHAIR: Yes, I'm aware.

Ms ABIGAIL BOYD: To the extent that someone wants to ask a question directly to one witness rather than the other then that's within their rights.

The CHAIR: It's not unusual for a department to appear alongside a Minister. It's a matter for them to determine how they're going to take the line of questioning.

The Hon. DAMIEN TUDEHOPE: With respect, it shouldn't be a matter for them.

The CHAIR: You are now eating into the time for asking questions. I would now like to welcome our next—

The Hon. GREG DONNELLY: Madam Chair, change of substitution; I think the Hon. Bob Nanva—

The CHAIR: Yes, Bob Nanva should be appearing online.

The Hon. GREG DONNELLY: Can we just check that that is the case?

The Hon. ANTHONY D'ADAM: Can I just request that—I can't hear any of the proceedings so it's very difficult to know what's going on.

The Hon. WES FANG: That's probably why it's better you turn up in person.

The CHAIR: Can you hear, Anthony?

The Hon. ANTHONY D'ADAM: I will remember that, Wes, when you want to use Webex.

The Hon. WES FANG: He can hear!

The Hon. ANTHONY D'ADAM: I will make sure that that's a point I make.

The CHAIR: While we're checking if Mr Nanva is online, I now welcome our next witnesses. Ms van der Walt?

MARINA VAN DER WALT: I joined NSW Treasury in November last year as Deputy Secretary, Financial Management and Services. I have the Strategic Balance Sheet Management Division in my group and they are responsible for overseeing the whole-of-State balance sheet and risks that affect the balance sheet as well as liaise with TCorp on the investment matters and liabilities.

The CHAIR: Would either of you like to start by making a short statement? Please keep it to no longer than a few minutes.

The Hon. DANIEL MOOKHEY: Thank you, Chair. I would. I would like to begin by thanking the Committee for inviting me here today. I have been following today's hearing with great interest and appreciate the opportunity to provide feedback and speak on behalf of the New South Wales Government and NSW Treasury on matters to do with the Debt Retirement Fund. This is the first time I've appeared before an upper House inquiry as a witness, so I hope that the Committee can show me some novice courtesy, if you don't mind, in that respect.

The Hon. WES FANG: Not a chance.

The Hon. DANIEL MOOKHEY: I have been aware of the Debt Retirement Fund since it was established by the previous Government in 2018. It was seeded with proceeds from privatising WestConnex, with an intended use as an effective sovereign wealth fund, allowing New South Wales to buy foreign and domestic stocks and bonds, property locally and overseas, and invest in instruments offered by hedge funds, high yield funds, banks and other financial institutions. As I regularly noted in the previous Parliament, this kind of financial strategy made sense in an environment of low inflation and historically low interest rates when the State had effectively a nil net debt and low gross debt position. That would have seemed logical in the circumstances of 2018 before COVID and the war in Ukraine.

Today, of course, inflation is a pre-eminent economic challenge for New South Wales and the present Government understands that the State has to deal with our own contribution to that overall high-inflation environment. I, of course, know that the Committee would note that the Reserve Bank's monetary policy response to inflation has been 12 interest rate rises in 14 months, raising the cost of debt for all borrowers, including the New South Wales Government. Families across the State are sacrificing so much more to stop our living standards from falling, and in three years' time the State will be handing our lenders $7 billion in annual interest payments—billions more than we spend to fund the entire NSW Police Force. That is the situation I inherited as Treasurer. More money spent on interest leaves us with less money to provide our public services, like our schools, our hospitals. Incurring more debt during times of high inflation risks adding to inflation, especially if we fail to use any of the spending to add to our productive capacity. That is the wider fiscal context upon which decision-making in respect to the Debt Retirement Fund has to take place.

Upon becoming Treasurer in March I was briefed about the upcoming and future contributions of the State's Debt Retirement Fund. Under those settings, the intended balance for the fund is to reach $50.8 billion by 2027. This would require the New South Wales Government to raise $25.3 billion of more debt to allow the equivalent amount to be deposited into the Debt Retirement Fund. I do note that the New South Wales Government had not given a meaningful update on the Debt Retirement Fund since December 2021's half-year statement. So you can, of course, imagine my personal surprise upon being given this advice. This plan has an element of risk to it because it exposes New South Wales to potentially billions of dollars' worth of losses if the economy faces another shock akin to COVID-19 or the global financial crisis. To put it in really crude terms, we are risking $25.3 billion so we can improve the State's net debt position by just two. That is the equivalent of placing a bet worth $12.50 which will only pay out $13.50 if you win.

At the same time, swelling the size of the Debt Retirement Fund artificially improves the budget bottom line because the budget assumes we earn a return of 7 per cent on every dollar we deposit into the fund, even when it ultimately loses money. This is, as I have said in my economic statement to the Parliament, a key concern. Should we find ourselves in a situation in a few years' time when the fund is doing very well, for example, we could find the State reporting budget surpluses that are quite large, yet at the same time having to explain to people why money isn't available to invest in essential services, despite the State showing a strong operating result.

If the projected returns are stripped out of the budget forecast, New South Wales will record consistent deficits every year over the forward estimates. This is not an ideal situation. The last budget plan for New South Wales was to add $58.7 billion of additional debt in the next three years, and by June 2026 we will be on track to owe our creditors a total of $188 billion in gross debt, which is equivalent to roughly 21 per cent of our GSP. This is, of course, the largest debt any incoming State Government has inherited from its predecessors in more than three decades.

I welcome this inquiry. I've been eager to share information that has been provided to me as Treasurer to the Parliament through this forum, including particularly the report that was commissioned during, I believe, the caretaker period by the Treasury, and then was produced for any of the incoming governments, whether it was to myself or it was to Treasurer Kean, presumably, as well. I did make sure that our Government took steps so that we could release that report to this inquiry so the inquiry could see the same information that we had. It is important to note that that report was not commissioned by this Government. That report was given to this Government, and now it's been given to this Parliament as well. It has been the report which has shaped some of the thinking that has informed the Treasury's submission. Of course, final decision-making around the DRF will have to take place in the budget. I welcome questions.

The Hon. DAMIEN TUDEHOPE: Thank you. Treasurer, I will be pleased if you would give short answers. These are very concise questions which I want to ask you, and I would be appreciative if you would not give speeches in respect of the questions—without seeking to limit your great ability. Just starting, when did you first meet Christopher Joye of Coolabah Capital Investments?

The Hon. DANIEL MOOKHEY: I've never met Christopher Joye.

The Hon. DAMIEN TUDEHOPE: Have you received text messages from him?

The Hon. DANIEL MOOKHEY: I've spoken to Christopher Joye. In fact, the first instance, I believe, I spoke to him was during the lockdown, when he drew my attention to the market shock that New South Wales experienced in—

The Hon. DAMIEN TUDEHOPE: He sent you a significant number of text messages, has he?

The Hon. STEPHEN LAWRENCE: Point of order: The witness had barely begun his answer. He wasn't finished with his answer. He was interrupted by the honourable member.

The CHAIR: I will uphold that.

The Hon. DANIEL MOOKHEY: As I was saying, he drew my attention to the fact that there was a big spike in the New South Wales Government's spread—borrowing costs. That spread's relative to the Commonwealth benchmark rate as well as to the Victorian rate and the Queensland rate. He was one of a few people who I then used to engage with the market to see what was going on as shadow Treasurer. I should point out this was four weeks, I believe, after I became shadow Treasurer. I equally at that time then saw a few reports that were published by ratings agencies, particularly S&P, which, I believe, we may have attached as well. Then, in addition to that, I spoke to other participants in investment markets—

The Hon. DAMIEN TUDEHOPE: I must stop you there, Treasurer, because I am not going to get through these questions if you want to continue to give speeches.

The Hon. DANIEL MOOKHEY: I'm not giving a speech; I'm answering your question.

The Hon. DAMIEN TUDEHOPE: No, you're not answering my question. My question was really specific about text messages from—

The Hon. STEPHEN LAWRENCE: Point of order: It is the same point of order. If you ask a question in this forum, you should pay basic courtesy to the procedure.

The Hon. DAMIEN TUDEHOPE: He should be required to answer it.

The Hon. STEPHEN LAWRENCE: You should also allow people to make points of order, I would suggest. He should allow the witness to complete his answer. He clearly—having regard to the subject matter of it—has not completed the answer.

The CHAIR: Yes, I remind all members present that all witnesses are entitled to procedural fairness as per the resolution from the House.

The Hon. DANIEL MOOKHEY: The only other thing I was going to say was that in addition to Mr Joye and S&P, I also at that time recall speaking to multiple analysts at different banks who were involved heavily in the bond market as I was interrogating why New South Wales was paying more for its debt than expected. And, incidentally, why New South Wales' gross borrowing task for that particular year was well above forecast.

The Hon. DAMIEN TUDEHOPE: That's fantastic. Will you just confine yourself, if you can, to answering the question which I—this is a serious matter, Treasurer. It is a very serious matter that I'm raising with you. When was the last time you received a text message from Mr Joye?

The Hon. DANIEL MOOKHEY: I would have received text messages from Mr Joye, I believe, when I became Treasurer.

The Hon. DAMIEN TUDEHOPE: Have you received any in the last fortnight?

The Hon. DANIEL MOOKHEY: I don't think so but I will take that on notice and come back to you.

The Hon. DAMIEN TUDEHOPE: Would you? Can you give us a ballpark figure of how often Mr Joye contacts you and corresponds with you? Just a ballpark figure.

The Hon. DANIEL MOOKHEY: To be fair, I'm happy to—

The Hon. STEPHEN LAWRENCE: Point of order: I think some latitude has been given by the Government members but there is a fundamental question here: How is any of this relevant to the terms of reference of this inquiry?

The Hon. DAMIEN TUDEHOPE: I'll come to that.

Ms ABIGAIL BOYD: Come to it quicker.

The Hon. STEPHEN LAWRENCE: It should be addressed on the point of order, I would suggest.

The CHAIR: On the point of order, there is usually wide latitude given to questions but this is straying closer to the fringes. Mr Tudehope, if you could—

The Hon. DAMIEN TUDEHOPE: It's close to the fringes but just give us an answer. How many text messages would you have received?

The Hon. DANIEL MOOKHEY: Look, how many—

The Hon. DAMIEN TUDEHOPE: Ballpark figure.

The Hon. DANIEL MOOKHEY: I text Mr Joye too. It's not just that he texts me. I often text him when I think his columns are right. I often text him when I think his columns are wrong. Can I say I'm happy to provide that service to others, if people would like to receive it.

The Hon. DAMIEN TUDEHOPE: Would you be prepared to make those text messages available to this Committee?

The Hon. DANIEL MOOKHEY: No.

The Hon. STEPHEN LAWRENCE: Point of order: That is so obviously outside the terms of reference.

The Hon. DAMIEN TUDEHOPE: No? No is the answer to the question.

The Hon. DANIEL MOOKHEY: Yes. The answer is no.

The Hon. DAMIEN TUDEHOPE: We've got the answer. You are not prepared to make those text messages between you and Mr Joye available?

The Hon. DANIEL MOOKHEY: No.

The Hon. DAMIEN TUDEHOPE: What I would say to you then is that when you respond to Mr Joye in respect of this fund and in relation to his observations in relation to this fund, do you take into account the fact that he is an investment manager?

The Hon. DANIEL MOOKHEY: Yes.

The Hon. DAMIEN TUDEHOPE: And that he purports to run activist campaigns in concert with you?

The Hon. STEPHEN LAWRENCE: Point of order: There are substantial policy issues posed by the terms of reference. We are yet to hear a question from Mr Tudehope that goes to any of them. It's outside the terms of reference.

The Hon. WES FANG: No, it's not.

Ms ABIGAIL BOYD: To the point of order: We've heard no actual substantive question from the Opposition at any point, but I don't think that's necessarily a problem if they want to waste their time that way.

The CHAIR: I uphold the point of order. There seems to be a significant amount of interest in the text message exchange here, which is well outside the terms of reference of the inquiry.

The Hon. WES FANG: It is not.

The CHAIR: Mr Tudehope, if you could continue.

The Hon. DAMIEN TUDEHOPE: Are you aware, Treasurer, that Coolabah Investments has interests in fixed income securities?

The Hon. DANIEL MOOKHEY: Yes, they have advertisements in newspapers in which they encourage people to put investments into fixed instruments. I am aware of that.

The Hon. DAMIEN TUDEHOPE: In fact, they would stand to benefit by decisions which may be made in relation to the investments in the NGF and the debt reduction fund. They would stand to benefit.

The Hon. DANIEL MOOKHEY: I can't speak to whether or not they would stand to benefit because I am not aware of what their particular investment strategy is.

The Hon. DAMIEN TUDEHOPE: I put to you that if they had investments in TCorp and money was in fact used to reduce gross debt, would they benefit?

The Hon. DANIEL MOOKHEY: I can't answer a hypothetical.

The Hon. DAMIEN TUDEHOPE: I put to you that they would stand to benefit by a reduction in gross debt.

The Hon. DANIEL MOOKHEY: Mr Tudehope, you might need to put that to the Committee in its report, not to me.

The Hon. STEPHEN LAWRENCE: Point of order: It is becoming clear from the questions—

The Hon. WES FANG: That you are running a defence.

The Hon. STEPHEN LAWRENCE: —that some aspersion is fundamentally being cast here. I again raise the question about how any of this could possibly be construed as going to the terms of reference which pose policy questions, rather than an opportunity to engage in some sort of collateral attack on somebody who's made a submission.

The Hon. DAMIEN TUDEHOPE: To the point of order: What I'm putting to this witness is that there are significant circumstances where the Treasurer is acting in circumstances where he has an undisclosed conflict of interest in respect of one of the persons who has made a submission to this inquiry. A person who has made a submission to this inquiry with whom he has regular correspondence stands to benefit by decisions he makes in relation to contributions to the Debt Retirement Fund.

The Hon. STEPHEN LAWRENCE: Further to the point of order: It might be helpful if the Hon. Damien Tudehope could perhaps explain how that line of questioning goes to the terms of reference rather than just explaining what it is.

The Hon. DAMIEN TUDEHOPE: Further to the point of order: It goes to whether the Treasurer has disclosed, for the purpose of coming here today, that significant conflict of interest, which he has in fact aided and abetted in terms of the manner in which he has conducted this inquiry.

The Hon. STEPHEN LAWRENCE: That is so absurd as to be frivolous.

The CHAIR: I'm prepared to make a ruling—

The Hon. WES FANG: No, it also goes to the integrity of this inquiry.

The CHAIR: There is a significant amount of argument in the line of questions that are being proposed by the Opposition. I would ask them to restrict their line of questioning to those as per the standing orders.

The Hon. DAMIEN TUDEHOPE: Do you accept, Treasurer, that if there was a significant change in the value of TCorp, Coolabah Capital Investments may in fact—

The Hon. STEPHEN LAWRENCE: Point of order: It's outside the ruling that has just been made. It's exactly the same question.

The Hon. DAMIEN TUDEHOPE: No, it's a different question. It may in fact benefit Coolabah Capital Investments—

The Hon. DANIEL MOOKHEY: Shadow Treasurer—sorry, Mr Tudehope, TCorp doesn't have value. TCorp is a public finance corporation.

The Hon. DAMIEN TUDEHOPE: Well, they issue bonds.

The Hon. DANIEL MOOKHEY: No, TCorp is a public finance corporation. It doesn't issue equity. It has no value as a structure. So I don't understand your question because TCorp isn't a trading fund manager. It's not listed on the stock market. The people of New South Wales own TCorp, so I don't think there's any conflict of interest that arises because TCorp is not an entity in which people—

The Hon. DAMIEN TUDEHOPE: Well, TCorp has value.

The Hon. DANIEL MOOKHEY: It has got value. I accept the point that TCorp has great value to the people of New South Wales. TCorp, which was established in the 1980s, I believe, is an example of a public finance corporation that has been mirrored by other structures. But it is wrong to say that people can invest in TCorp—

The Hon. DAMIEN TUDEHOPE: But do you accept it?

The Hon. DANIEL MOOKHEY: No, I'm not accepting it, Mr Tudehope, for the reasons I gave you.

The Hon. DAMIEN TUDEHOPE: Do you accept that there could be a perceived conflict of interest in relation to your—

The CHAIR: Mr Tudehope, we'll just let the Treasurer finish the answer—

The Hon. DANIEL MOOKHEY: I'm very happy to answer that question—

The Hon. DAMIEN TUDEHOPE: —relationship with Mr Joye?

The Hon. DANIEL MOOKHEY: No, absolutely not. Here's why.

The Hon. DAMIEN TUDEHOPE: That's what you say, Mr Mookhey, and I accept that that is—

The Hon. DANIEL MOOKHEY: I reject that. Here's why, Chair: Because I—

The Hon. DAMIEN TUDEHOPE: I'd like to ask Ms van der Walt a question—

The CHAIR: If we could just hear the answer to the question?

The Hon. STEPHEN LAWRENCE: Point of order: An aspersion has been put and the Treasurer hasn't been allowed to answer.

The Hon. WES FANG: He's answered the question.

The Hon. DANIEL MOOKHEY: Again, Mr Tudehope, perhaps I've noticed that in terms of what is a conflict of interest, myself disclosing public information to the people of New South Wales, making statements in Parliament and asking this inquiry to undertake a public policy exercise isn't a conflict of interest. I'd argue—and I'd suggest perhaps the Committee should endorse—that it is an example of transparency that should have been adopted back in 2021—

The Hon. DAMIEN TUDEHOPE: But you won't disclose the text messages between you and Mr Joye.

The Hon. DANIEL MOOKHEY: —when the previous Government made a decision to deposit $25 billion into this fund.

The Hon. DAMIEN TUDEHOPE: Will you disclose the text messages?

The Hon. DANIEL MOOKHEY: I welcome the fact that I'm here today as Treasurer to be able to answer your questions because this is an important issue of public policy. The question that is in front of the Government, which we would welcome the assistance of the Parliament towards, is whether or not we should be borrowing effectively $25 billion and putting it on the stock market, and other risky trades—

The Hon. DAMIEN TUDEHOPE: I will come—can I just ask the Treasury official—

The Hon. DANIEL MOOKHEY: That $25 billion is the equivalent of building the entire Metro West project. It's not a small financial decision. The fact is it was open to me as Treasurer, through the Cabinet process, to simply make the decision as a government. But I think it's important for the people of New South Wales to understand the stakes, to understand the informed decision—

The Hon. DAMIEN TUDEHOPE: I understand you don't want to—

The Hon. DANIEL MOOKHEY: —and to be able to use this forum to interrogate it. In addition to that, because questions of financial management are intergenerational in nature, of course the Parliament should have a role in it. The fact that this inquiry would require you and other parliamentarians who are not from my party to have to take a position on it I think is a good thing. I actually think it's a good thing that we are making financial decisions like this collectively as a Parliament. Ordinarily that is done through the appropriation bills process and through the budget estimates process.

The Hon. DAMIEN TUDEHOPE: Point of order: This is completely an attempt to—

The Hon. DANIEL MOOKHEY: I welcome the fact that insofar as—

The Hon. DAMIEN TUDEHOPE: —obfuscate the process.

The Hon. WES FANG: And run the clock down.

The Hon. DANIEL MOOKHEY: —there is an assertion that my bringing an inquiry reflects a conflict of interest, I reject it because I brought this inquiry here—

The Hon. WES FANG: We have relevant questions of integrity.

The Hon. DANIEL MOOKHEY: —for the purposes of using this forum to interrogate Executive Government—

The Hon. STEPHEN LAWRENCE: Point of order—

The Hon. DANIEL MOOKHEY: —and to allow the people of New South Wales a say in such an important financial decision that affects them.

The Hon. DAMIEN TUDEHOPE: Thank you. Can I ask you a question, Ms van der Walt? To your knowledge, has the New South Wales Government ever borrowed money for the express purpose of it being invested in the Debt Retirement Fund?

MARINA VAN DER WALT: The Debt Retirement Fund was established in 2018 and seeded with $10 billion worth of investment: $3 billion from cash reserves and $7 billion from the proceeds of the sale of WestConnex. At the time there was a budget surplus, net debt was negative and the economy was in a different place, and the State's fiscal position was in a different place than it is today.

The Hon. DAMIEN TUDEHOPE: Just confining my question, has the New South Wales Government ever borrowed money for the express purpose of investing in the Debt Retirement Fund—to your knowledge?

MARINA VAN DER WALT: The current fiscal position is—

The Hon. DAMIEN TUDEHOPE: No—

MARINA VAN DER WALT: —outlined in our submission.

The Hon. DAMIEN TUDEHOPE: No, the question is to your knowledge has the New South Wales Government—the previous New South Wales Government—ever borrowed money for the express purpose of investing in the Debt Retirement Fund? Yes or no—to your knowledge.

MARINA VAN DER WALT: The current—

The Hon. DAMIEN TUDEHOPE: The previous government.

MARINA VAN DER WALT: —fiscal position, as I was saying in my—

The Hon. WES FANG: Point of order: The witness is clearly trying to get around the question. The question is quite simple: Has the previous Government ever borrowed money—yes or no?

The Hon. STEPHEN LAWRENCE: To the point of order: It is not a simple question—

The Hon. WES FANG: It is! It's a very simple question.

The Hon. STEPHEN LAWRENCE: —and when a government is borrowing money overall and is in debt and is depositing into a debt fund, in effect that is occurring. So to suggest that it's a yes or no question is ridiculous, and the witness should be allowed to elucidate her answer, I would suggest.

The Hon. DAMIEN TUDEHOPE: The question was framed this way—

The Hon. WES FANG: It was framed as historic.

The Hon. DAMIEN TUDEHOPE: It was for the express purpose of—

The CHAIR: I'm prepared to make a ruling on this. The Treasury official was partway through, I believe, what was the first sentence of an answer. So if you could please continue.

MARINA VAN DER WALT: What I might add to that response is that in 2021 the contributions were suspended by the previous Government.

The Hon. DAMIEN TUDEHOPE: Correct.

MARINA VAN DER WALT: And no further contributions have been made.

The Hon. DAMIEN TUDEHOPE: Correct.

MARINA VAN DER WALT: Those decisions were disclosed in the half-year result and in the 2021-22 half-year result as well.

The Hon. DAMIEN TUDEHOPE: Can I take you back to my question: Has the New South Wales Government ever borrowed money for the express purpose of investing in the NSW Generations Fund—for the express purpose?

The Hon. STEPHEN LAWRENCE: Point of order—

The Hon. DAMIEN TUDEHOPE: Yes or no?

The Hon. STEPHEN LAWRENCE: It's been asked and answered—

The Hon. WES FANG: Okay, I'm going to rephrase the question.

The CHAIR: A point of order has been taken.

The Hon. STEPHEN LAWRENCE: —and I would seek to be heard on the point of order rather than being interrupted by Wes Fang. She, the witness, has answered the question and to again come back to it and seek to characterise it as a "yes or no", in terms of the complexity of the issue I think is frivolous and wasting the time of the Committee, frankly.

The Hon. WES FANG: Chair, I'm going to ask a question—

The CHAIR: To the point of order—or you're asking a question?

The Hon. WES FANG: I'm going to ask a question. I contend that the previous Government never borrowed money for the express purpose of the Debt Retirement Fund. Would you believe that my statement is wrong?

MARINA VAN DER WALT: I can refer you to Standard and Poor's frequently asked questions about the NGF and commentaries made in there about the increase in gross debt. And also Standard and Poor has made commentary that all money is fungible.

The Hon. DAMIEN TUDEHOPE: Can I just ask the questions again and this time I think it is a yes or no answer. When you borrowed for the express purpose of investing in the Debt Retirement Fund to your knowledge?

MARINA VAN DER WALT: I wasn't there at the time.

The Hon. DAMIEN TUDEHOPE: Good. Thank you. Is work currently being done by Treasury to amend the NSW Generations Funds Act?

MARINA VAN DER WALT: No, not to my knowledge.

The Hon. DAMIEN TUDEHOPE: Is there any other legislation proposed which would affect the DRF?

The Hon. DANIEL MOOKHEY: Chair, that's a question to do with Government policy, actually, which I might answer.

The Hon. DAMIEN TUDEHOPE: No, the point is—and I made this point before—these are two separate witnesses. I'm asking this witness this question—not you, Treasurer.

The Hon. STEPHEN LAWRENCE: To the point of order—I assume it's a point of order—it is well within the prerogative of the Treasurer when it is a question of Government policy for him to answer because questions could arise, for example, about privilege.

The Hon. WES FANG: This is not estimates.

The Hon. STEPHEN LAWRENCE: So there's a whole range of issues there.

The Hon. WES FANG: This is not estimates.

The CHAIR: I believe that that is well within the scope of having the Treasurer answer that question.

The Hon. WES FANG: Point of order—

The CHAIR: I have made a ruling.

The Hon. DANIEL MOOKHEY: I have issued no instructions to the Treasury to prepare any legislative options for government whatsoever. The Government policy is not to pursue legislative amendment. I point out that the last Parliament had on its *Notice Paper* an Act to amend the NGF that was never then pursued in the upper House. That, to my knowledge, is the last time any government sought to amend the NGF Act.

The Hon. DAMIEN TUDEHOPE: Ms van der Walt, can you provide an itemised list of the State's current debts and the cost of servicing—that is, the interest expense in respect of each debt?

MARINA VAN DER WALT: Of the whole State?

The Hon. DAMIEN TUDEHOPE: Yes.

MARINA VAN DER WALT: I will need to take that on notice.

The Hon. DAMIEN TUDEHOPE: I am happy for you to take that on notice and provide that to us. In designing the sovereign wealth fund, what sort of asset allocation is typically considered best?

MARINA VAN DER WALT: The NGF's investment strategy, which was prepared by TCorp and endorsed by the Asset and Liability Committee and recommended to the Treasurer, contains investment in a broad range of asset classes, including equity, debt, international—

The Hon. DAMIEN TUDEHOPE: I notice that the Treasurer is very content with running down the clock in relation to that.

The CHAIR: We will now move to crossbench questions.

The Hon. DAMIEN TUDEHOPE: This is a serious inquiry.

The Hon. STEPHEN LAWRENCE: Point of order: I ask that the Hon. Damien Tudehope be brought to order. He is essentially screaming at the witness now.

The Hon. WES FANG: You should be brought to order for wasting our time on this questioning.

The CHAIR: We will now move to crossbench questions.

The Hon. DAMIEN TUDEHOPE: For the manner in which you conduct this inquiry for your own purposes.

The CHAIR: We are now eating into Ms Abigail Boyd's time.

Ms ABIGAIL BOYD: Okay, enough.

The Hon. STEPHEN LAWRENCE: Point of order: I ask that Mr Tudehope be brought to order.

The Hon. WES FANG: You should be brought to order, Mr Lawrence.

Ms ABIGAIL BOYD: Thank you for coming and thank you for providing the EY Port Jackson Partners report, which I will resist asking about from a consultant's perspective until we get to that in our consulting inquiry. Engaging in the substance of the terms of reference that we have in front of us, there were a number of things that we were asked to consider in this inquiry. One of the things that's not really covered there and isn't covered in the EY PJP report is the concept of—if we're looking at what would be the best level of NGF, we've had discussion around it potentially being a percentage of gross debt, or whatever it happens to be. How are you thinking about it in terms of the risk appetite of the actual investment? We have at the moment this target of CPI plus 4.5 per cent, which made some sense before we had massive amounts of inflation. In terms of looking at that target rate and then also looking at increased volatility and the rest of the things that are going on around the world, is there also a question about just how risk-averse we should be in terms of the investment strategy and what sits in the NGF?

The Hon. DANIEL MOOKHEY: Yes, there is, Deputy Chair. In fact, that question gets to the heart of a policy question that is in front of the Government that the Government is yet to resolve because we want to hear from this Committee, which is—

The Hon. DAMIEN TUDEHOPE: Well, do your job.

The Hon. DANIEL MOOKHEY: With respect to the risk, it's fair to say that the risk is different now than it was in 2018, and in that the source of capital that we were effectively paying very little interest on, the fact that we are now in a high-interest environment obviously affects the cost of the strategy—that is, the amount of money that we have to borrow to execute the strategy, even if it's a good strategy. It also affects its risk-return metrics as well. Ultimately, the question as to how much risk people are prepared to take—there does need to be, I think, a policy framework developed to provide guidance to this Government and future governments, and this Treasurer and future treasurers, as to how to approach it. But, ultimately, there are great questions of judgment that need to be exercised here.

The current circumstance in which we are in a quantitative tightening cycle across the world, where the Federal Reserve in the US is withdrawing funds from the global system and when you have other banks doing the same, with the exception of the Bank of Japan, is creating a very different investment climate as well in terms of what you invest in. A few years ago investing in equities relative to debt was one thing. Currently, in terms of being able to obtain a return of the interest rate, the Government's risk-free rate or the US Treasury rate are far less risky. And, yes, governments are going to have to decide what their risk appetite is.

Where I'm sitting at, as Treasurer, taking $25 billion of effectively leverage and depositing it in a fund for what, in effect, has been advised to me is roughly a $2 billion net debt improvement is risky. It is highly risky.

It's something which this Government is grappling with as we develop our first budget. The broader questions that I think, Ms Boyd, you were getting to, and I heard you asking the same question to Mr Bartos, are what are the right set of metrics? What should we be targeting? That is something which does require quite a bit of policy work as to what it is. Right now we pay gross debt—we pay our interest on our gross debt. We should distinguish this fund from other forms of government investment funds for which the funds can be used for different purposes. For example, one of TCorp's funds is just our cash fund, and that is cash on hand that's invested that can be used for all of the Government's operating expenses. That's a different sort of risk profile than one that can only be used for debt retirement.

This is the key point in the budget presentation—is that in a few years' time we will be reporting, potentially, income from this fund that will appear the same way our taxation revenue does and our dividend revenue does, but we can't use it for the same purposes because of the way in which this particular Act has been designed. That is something which, in human speak, would result in this Government and future governments having to sit down with, for example, its essential workforce and say, "Actually, in terms of whether there's money available to fund pay increases, it might look like there is, but there actually isn't." That's going to create a whole bunch of distortions which I think we should anticipate.

Ms ABIGAIL BOYD: You may have heard me talking before about looking at the way that S&P treats this. My understanding is that S&P look at the DRF effectively as an offset against gross debt, but they do look at the particulars of it in order to work out exactly how much of that NGF they treat as an offset. So it is not just a simple amount of every dollar in that account is worth the same. It depends what it is invested in and what the risk profile is. Whereas Moody's and Fitch would look at a more holistic basis in terms of assets and liabilities across government and its agencies. When we're talking about the idea of borrowing more debt and putting a certain amount of more debt into the DRF, presumably—you know, S&P aren't stupid. Even if you did that, there's still the possibility that they would view that negatively from a ratings perspective. Is that right?

The Hon. DANIEL MOOKHEY: Yes, Ms Boyd. I can't speak for S&P because I obviously don't represent them and I'm also mindful of the fact that those rating agencies keep their assessment criteria relatively private, but I can refer you to what their public comments have been. S&P did issue, I believe, a note back in 2021, which Mr Tudehope and I were discussing a bit earlier, in the wake of the surprise that took place in 2021 in which they pointed out that how they assess the DRF does turn on the source of its inflow—that is, how the money that has been put into it has been arrived at. And that, yes, as in all financial assets, they will test it, I believe they said, about whether or not that money is available for a government to use should there be an immediate requirement for debt retainment in the same way. To the extent to which they think it is or is not will lead them to either discount the balance of the NGF, so they are providing a fair assessment of its finances in that respect.

But the second point you make goes to a key point that EY made in this report, which is one of the risks to do with the NGF in general is that there is a chance that ratings agencies change their criteria, and they can change their criteria exogenously to anything to happen with the Australian economy—as in, a point that's been made in this report is that should, for example, S&P change how they assess the Canadian fund or should they, for example, change how they judge the sovereign wealth fund of a country like Brazil as well, for no reasons whatsoever to do with Australia, we could find ourselves at the mercy of our credit rating effectively being affected because they have changed their criteria as a result of a development in another market. That is a significant issue for this Government and for future governments as well.

Ms ABIGAIL BOYD: So that sort of treatment by S&P of the Debt Retirement Fund as effectively an offset account is unique to New South Wales and one Canadian province. Is that right?

The Hon. DANIEL MOOKHEY: Again, I can only refer to what S&P has said publicly because I don't speak for them. But it's fair to say that in their public report they did make the point that such an arrangement does exist. I think it's in the Ontario province of Canada, but I could be wrong. But they did make the point that, as far as some national jurisdictions go—that is, non-central governments or federal governments—yes, Canada and New South Wales are a bit unique in this. Equally, as the report EY makes, sub-national governments having sovereign wealth funds of this scale and over this period of time is pretty much unique to New South Wales.

Ms ABIGAIL BOYD: If we look at the NGF and the relevant legislation, it does refer back to the Fiscal Responsibility Act, which talks about that—we've had this discussion and this primary goal of it being about maintaining a triple-A rating rather than it being about the actual tangible impact on the people of New South Wales. Because of that link between the NGF and the other legislation, do you have a concern that when you are redesigning policy in this space or working out what the next steps are, you will be somehow hampered or restricted by that connection? Or is it just so murky with S&P that it's—

The Hon. DANIEL MOOKHEY: No. Again, as a matter of having to, as Treasurer, assess the requirement to satisfy the FRA, it's fair to say that with this particular strategy it may well have the potential of creating conflicts between how we achieve the certain objectives of the FRA. That is not to say that all the objectives of the FRA could be resolved potentially with the way in which this strategy has been developed. For example, one thing that the FRA requires us to do is to triple-A credit rate, which of course requires us to then assess what are the right levels of metrics we should be setting the budget to hit. That could lead to a situation where, for example, depending on the cost of our interest, we could find ourselves, because we are effectively increasing the amount of gross debt to fund this strategy, creating an issue with another way in which the credit rating agencies assess us as well.

One point that has been speculated upon that credit rating agencies assess is whether or not, for example—your interest to your revenue ratio. I know from your background, Ms Boyd, that you would be aware that that is just a standard metric as well. If we find ourselves in a situation where we are expanding gross debt too far, regardless of whether it's for this strategy or for other strategies, that could definitely create questions about the FRA and whether we could satisfy that. The FRA, as you would also be aware, requires us to effectively keep revenue growth higher than expense growth over the long term. Depending on if we borrow at this rate and if the expenses go up, that will create tension points as well. So it's not easy to reconcile this strategy with compliance of the FRA because, in effect, it's going to require us to choose which is the most important part of the FRA that we should satisfy.

Ms ABIGAIL BOYD: If we are looking then at going forward, I think we've already seen in the political commentary around this issue that it is complex. If you were trying to explain this to the public and the concept that you could actually be raising more gross debt and the result would be lower net debt—are you able to explain that in any easy way so that you could then explain to people why you could have the next budget looking like you've got a higher net debt, even though you've got a lower gross debt?

The Hon. DANIEL MOOKHEY: It's the other way around—

Ms ABIGAIL BOYD: Sorry.

The Hon. DANIEL MOOKHEY: —but, yes, I can, Ms Boyd. The best I can say is that we are going into debt to repay debt.

Ms ABIGAIL BOYD: Yes. But the bottom line on the budget is that even though we're going to have a lower gross debt and be materially better off—

The Hon. DANIEL MOOKHEY: Lower net debt. This strategy, if executed to the letter as designed, would lower the State's net debt but increase gross debt.

Ms ABIGAIL BOYD: Right. Yes. If you don't do that, then you will effectively have a lower gross debt but a higher net debt.

The Hon. DANIEL MOOKHEY: Yes, that's right.

Ms ABIGAIL BOYD: Because the budget relies on that net debt figure, it makes it look like the budget will actually be in a worse position. You will have your political opponents jumping down your throat saying that you have somehow worsened the budget.

The Hon. DANIEL MOOKHEY: It's a good point. I'm sure my political opponents wouldn't be jumping down my throat in any circumstance because that's just not how they roll. But all I would say is that we pay our interest on our gross debt. That is important in terms of this Government because the fastest source of cost pressure in the budget right now is actually the rise in interest expenses, which is growing at roughly 29 per cent, from memory, over the forward estimate period. That is huge. In a scenario in which we are saying to, for example—like the previous Government did—essential workers, "You can't have a pay rise", but at the same time we're having to find more money to pay our creditors and our bond holders, that's a political trade-off there. In terms of what my priority is in a high inflation environment, it is to make sure that we are doing our bit to lower inflation and in the course of that protecting the families of New South Wales.

Being able to say to New South Wales families and to be able to say, for example, to New South Wales' essential workers, "You have no right to even ask for a pay increase but I'm going to play this fiscal strategy that will simply lead to us having to pay more income and more of our interest costs on our operating expenses, to bond holders"—that is a difficult position to make. This is the point about, I guess, why there's been a change of government: so there is a fresh set of eyes on these questions.

Ms ABIGAIL BOYD: There's also that narrative—which I thought until I actually looked into this—that this was a sovereign wealth fund in the same way that Norway has.

The Hon. DANIEL MOOKHEY: It's not.

Ms ABIGAIL BOYD: No, but it was something where this was saving up for the future and if you were to somehow to gut this Debt Retirement Fund, it would be taking away from the future. But it's not because it's an offset fund against debt that you've raised. I guess, what's to stop us using that debt now and taking a big chunk of it—sorry, not the debt but the fund, the DRF—and actually using it to pay down our debt?

The Hon. DANIEL MOOKHEY: Well, let me answer those first three points in very quick succession. Firstly, you're quite right to say that it should be distinguished from the Norwegian sovereign wealth fund, which I believe is the world's largest. The Norwegian sovereign wealth fund's purpose is to effectively remit foreign currency that Norway receives out of the country so they always are a capital exporter because they're an oil-based economy. As an oil-based economy, if they were to suck up so much capital to their domestic market, they'd hollow out every one of their other industries. That is the Dutch disease—which I think is how economists traditionally referred to it originally, which I think is now a bit pejorative. But the whole point of the sovereign wealth fund in Norway is they can only invest in assets outside of Norway to be able to get it out. It's not the same. Incidentally, Professor Max Corden of the ANU is the world's leading expert in this, I believe, and as well he's written a lot about this.

The second point you make, which is why we don't just liquidate the fund, is an interesting question. I would make the point that you can assess that on a policy and philosophical level, on which people will have different views. My perspective as Treasurer, on the pure pragmatics of it, is that that would see New South Wales effectively run the risk of realising some losses in the current market circumstance. You would effectively see New South Wales having to do two things in the marketplace. Firstly, liquidate all its current investments that are in the fund on a relatively short succession, and we can't guarantee precisely what we'll get for them particularly relative to their benchmark value. The second thing I would say is that you could only use that money to go into the secondary market to buy back bonds. I'd make the point that just because of the way of the bond cycle—in terms of New South Wales Government debt issuance has taken place—we'd be going back to buy back the cheapest debt we owe, not the most expensive debt.

The debt we were issuing three years ago—we were issuing into a market of roughly the two-year/three-year spread—was close to 1 per cent or lower, and we're issuing debt today at 4. In terms of what bond lines are available to be bought back, we'd be buying back our cheapest debt as to issuing it. I don't think, therefore, from a market operation perspective it's a sensible strategy to be pursued right now in terms of liquidating the existing balance. The question that's in front of the Government and the Parliament is whether we put 25 more in.

Ms ABIGAIL BOYD: Yes. I totally understand that in terms of having a trajectory of where you want it to get to, looking at the maturity of the bonds that are on issue, looking at how easy it is to liquidate particular parts of the fund.

The Hon. DANIEL MOOKHEY: One other point I just want to make is I agreed with Treasurer Perrottet's decision not to put the proceeds of the second WestConnex sale into the DRF in that situation. I think Treasurer Perrottet made a good decision to use that money to retire debt over that period of time. Had that money been deposited in the DRF, we would have lost a lot of it just in terms of the market cycle. We already will be behind, so I would point out at the time I was calling on Treasurer Perrottet not to do it and in fact, dare I say, campaigning for him not to do it, but he made a good decision when he chose not to put that deposit in.

The Hon. STEPHEN LAWRENCE: Thanks, Treasurer. I was wondering if you could talk to how financial and economic conditions have changed since the DRF was created?

The Hon. DANIEL MOOKHEY: Yes, I can. In 2018 the market conditions were very different. We were in a situation of low to no inflation. We were in a situation of quantitative easing that was lowering interest rates worldwide. Therefore the spread between the cost of government debt issuance as well as the return that's possible from a market strategy was very much favoured towards a return rather than the risk part of the risk-return ratio. In addition to that, around 2018 the State fiscal situation was in a different position to what it is now. Right now we have the complete converse economic situation. We're in a high inflation scenario. We're in a scenario where government finances and government balance sheets across the country and the world are under much more stress and pressure as a result of the necessary support that governments had to provide during the COVID crisis. In addition to that, the outlook in markets is very different as well, and the risk appetite of different investors is very different as well, which is changing the valuation of certain asset classes compared to what it was back then. To put it really simply, it's a much riskier time now than it was in 2018.

The Hon. STEPHEN LAWRENCE: Can you talk a bit about when money is contributed into the DRF under the current settings?

The Hon. DANIEL MOOKHEY: The previous Government's last declared policy position was that deposits would resume at a point where the State had a cash-operating surplus—not an operating surplus, a cash-operating surplus. As this report makes clear, there's a distinction that State governments generally adopt, which is different to the Federal Government. We report our numbers operating on an accrual-based accounting system as our primary balance and the way in which our people assess our balance sheet. We also do produce cash statements, which people who are as big fans of budget papers as I am would know is at the back of *Budget Paper No. 1*. You can see both sets of accounting standards. The last forward estimates that were provided at PEBU—or maybe before PEBU—showed that we were meant to be returning to a cash-operating surplus for 2023-24 onwards, which would see deposits of effectively that cash surplus.

The effect of depositing the cash surplus into the DRF is that you cannot use that cash surplus to offset your infrastructure borrowing, which is what most governments do with cash-operating surpluses, particularly at a State level. For example, in places like Queensland, traditionally, they would take their operating result or the cash result on the general government sector and then take their infrastructure program, figure out their borrowing task and use the cash-operating surplus to lower the amount of debt they need to issue into the market. If you divert that cash-operating surplus into the DRF, you have to effectively offset it by borrowing more to fund your infrastructure program than you otherwise would. That's why, as I think the deputy secretary said, S&P pointed out that money is fungible. But the net effect of this is that instead of borrowing to build schools, hospitals and railways, you are borrowing money to put into the DRF. It's a different situation.

The Hon. STEPHEN LAWRENCE: Under the current settings, how much in funds is contributed each year?

The Hon. DANIEL MOOKHEY: It's fair to say that perhaps after some further public attention that arguably I created as shadow Treasurer, the previous Government halted contributions into the DRF—

The Hon. DAMIEN TUDEHOPE: I'm sure that's not the case.

The Hon. DANIEL MOOKHEY: —for the last two years, I believe. That's right?

MARINA VAN DER WALT: Yes, that's right.

The Hon. DANIEL MOOKHEY: So there hasn't been a deposit for the last two years. Deposits are slated to recommence effectively from this fiscal year onwards.

The Hon. STEPHEN LAWRENCE: Under the current settings, are contributions limited to the amount of budget surplus?

The Hon. DANIEL MOOKHEY: No. There's no limit to what could be contributed. That's a good point, because if you follow the logic of this through to its end, what's to stop the State from just borrowing even more and plugging it in? One way in which arguably you could solve the operating deficit that the State is in is just to borrow more money and put it into the market and then rely on the fact that it's accounted for differently to create the budget surplus. In fact, there is no rule. From what I can tell in terms of what the logic of the contribution is, there is an element of discretion that's available to a government of the day.

It's fair to say, though, that Treasury had developed—and this is me just simply going off my time in opposition really. But it's fair to say that, at the time that this was created, there was a theory that we would create this and this would provide a bit of balance sheet power over time and there would come a point where we would stop contributing and just rely on the investment returns for the balance to grow. I believe that was towards the end of this decade. Actual capital accumulation in the fund would stop and it would simply rely on its investment returns to reach a balance of $90 billion by 2031, I believe that was.

To be fair to the previous Government, that was outlined in their 2021-22 budget and in their 2021-22 half-year budget after adjusting for the non-deposit of the second proceeds of WestConnex privatisation. They released in the half-year review that the intended balance was $81 billion, I believe, at that time. I don't believe the previous Government did make any further statements about what their intended balance was by that period of time. Certainly, the situation I've inherited suggests perhaps that $81 billion figure was still the trajectory as well. It is important to say that that is a policy decision of government. That is not the decision of Treasury. It is not the decision of TCorp. That is a decision of governments to get it to that size.

The Hon. STEPHEN LAWRENCE: How often have contributions related to privatisation?

The Hon. DANIEL MOOKHEY: Most of this inflow came from privatisation. I think, as the deputy secretary said, the fund was seeded with the sale of the first WestConnex privatisation, which I think was to the tune of $7 billion at the time—and then cash balance of $3 billion. The other point which should be made is that technically the NGF owned the State's residual share in WestConnex after privatisation. That is, when the previous

Government established WestConnex, they established a company called Roads Retained Interest Pty Ltd. At one point in time the shareholder, I believe, was either the Treasurer or the finance Minister and the transport Minister. That actual interest got assigned to the DRF. So the DRF became the owner of the State's residual interest in WestConnex. The issue when WestConnex was sold, or the remaining share was sold the second time—the actual owner was the DRF. Therefore, the money had to go to the DRF.

To be fair to the previous Government, that was their explicit policy intent. But it's fair to say there was a disjuncture between the previous Government's political rhetoric and the actuality in that they said that, by privatising WestConnex, they'd be able to build railways and establish WestInvest. In truth, that wasn't the case. Every dollar that came from the second proceed of selling WestConnex went into debt retirement. That flow of funds was towards debt retirement. To put this again in perhaps more human speak, we had created a toll road, we privatised it and then we used the money in the DRF; we didn't use that money to create further assets.

The Hon. STEPHEN LAWRENCE: You spoke earlier about the fund being associated with higher levels of gross debt. Are you able to explain what risks that creates for the State?

The Hon. DANIEL MOOKHEY: Yes. Well, for example, assume that it gets to its $50 billion balance by 2027. A 10 per cent market variation shock would see the State lose $5 billion. A 10 per cent accretion would see us gain $5 billion. But the $5 billion gain cannot be used the same way we could, for example, if there was a windfall gain in royalties or a windfall gain in property prices, because you can only use it for this particular purpose. I just stress a $5 billion variation even on that size is sizeable. All of a sudden, New South Wales will find itself in a position where it's arguably having to explain what is going on with its finances and why it is as volatile as it is as well. It's different if we were to achieve that $50 billion balance over 20 years or 30 years. The risk profile is very different depending on how long it's taking you to develop that size relative to the rest of your assets and the rest of your income. But to effectively artificially use leverage on your balance sheet just changes the risk profile across the entire balance sheet.

It's fair to say owning a financial asset is not the same as owning the other forms of asset classes that New South Wales does, because it is subject to more volatility depending on what's going on in market conditions. Going back to a point I think Mr Bartos made, there is a philosophical question to be answered here: Should the New South Wales government be effectively a fund manager of this size? I'd also make the point that using debt on your balance sheet is something which banks cannot do and they have not been able to do that since the Great Depression.

Equally, super funds can't do it. I mean, superannuation funds cannot use leverage to accrete or expand their returns for the quite obvious reason that you do not want to jeopardise people's retirements should there be a risk. Because we're not regulated by APRA, we make our own rules, and you can make those rules to take more risk or you can make more rules to decrease risk. It's a question of Government policy of the time. But if a super fund was using debt to increase their returns, their directors or trustees would be facing some pretty serious questions.

The Hon. STEPHEN LAWRENCE: With this investment in volatile financial markets, can you speak a bit more about what risks that poses to the State?

The Hon. DANIEL MOOKHEY: Yes, I can. It all turns on how long you need to hold the fund for. Dr Bartos was making the point about the well-known phenomenon of an equity premium that exists, which means over time if you own equities you should do well compared to debt. That's a good philosophy for a person who is an investor, but the State is not the same as other investors. We have other obligations that we have to do and we have to fund. We have to decide how much money we can put into schools and into hospitals and into our Police Force and into our TAFE system. We've got to compete multiple objectives here. By simply pretending that the State is the same as every other investor in financial markets, you are risking the ability to achieve other objectives that only governments can do. It's not like other investors are benevolently funding our schools and hospitals; we have that obligation.

I think each Treasurer may reach a different view on this, but from my perspective how much volatility we're prepared to take does turn on what your other priorities are, and this Government's priority is to rebuild our essential services after 12 years of neglect. That is what we have to focus on, in my view. It's going to be very hard for any of us to explain to a person that your ability to get investment into your school and hospital is secondary to the State's need to effectively run this fiscal and financial strategy in order to satisfy certain requirements of markets and credit rating agencies.

My other point in all of this is that there are other ways for the State to potentially attain the same result without having to embark upon such a risky strategy as well. Again, $25 billion to realise a $2 billion net debt save—it does ask questions about whether the State can realise that $2 billion net debt save by pursuing other strategies that are less risky. That's an important point here because there are other ways to obtain the same result, which, to be fair, I'm certainly interested in working with.

The Hon. STEPHEN LAWRENCE: Can you speak to how that risk changes with the varying size of the DRF over time?

The Hon. DANIEL MOOKHEY: Obviously as the size expands, and depending on the source of inflow of the funds, the risks expand. Part of the issue that I think the Deputy Chair was asking before—why not liquidate it? Is it risky in its current settings? To be fair, that was a question that perhaps the previous Government was in a better position to answer than I was because we have just gone through a big economic shock and the DRF did exist during that time as well. The State managed to manage it. The result of that is we still have big, big budget deficits and we have a lot of other debt that we are now having to deal with and the consequence of it, especially given that lots of that debt is not because of COVID. You've got to look at this in terms of the wider Government priorities, which is what I was making the point about earlier as well. It is something which again does require serious public inspection and serious public scrutiny because it's a big decision for the State and the State's future.

The Hon. STEPHEN LAWRENCE: You spoke earlier about the high-inflation environment. Can you speak to how that affects the DRF?

The Hon. DANIEL MOOKHEY: Twelve interest rate increases—are we up to 13 now? Twelve or 13—I think we're at 12—over 14 months.

The Hon. WES FANG: The Treasurer doesn't know how many interest rate increases we've had?

The Hon. DANIEL MOOKHEY: It's hard to keep up.

The Hon. WES FANG: That's interesting.

The Hon. DANIEL MOOKHEY: It's 12 over 14, but I certainly do know what impact it's having on families and what it's having on consumer spending. I just think that anyone who is talking to a person on the street right now understands just exactly what the trouble is with inflation. For us, the fact that the RBA has hiked interest rates by 12 has meant that the cost of New South Wales government borrowing has shot up as well. When I became shadow Treasurer in 2021, I believe our three-year borrowing was roughly 0.43 per cent. I haven't checked today how much our debt is trading on the secondary market but it's probably 3.98 or 3.9 to four point something. That's a tenfold increase in the cost of government borrowing. In addition to that, we're having to issue new debt, we're having to refinance old debt from a low-interest environment into a high-interest environment as well, and that's part of the reasons why our interest expenses are rising to $7 billion. It's not the same as it was back in 2018. When you are paying 10 times more for capital than you were previously, you've got to ask yourself whether you're getting 10 times the return.

The CHAIR: Treasurer, could I just ask where the previous Government reported the amount of contributions to the fund in the budget?

The Hon. DANIEL MOOKHEY: Sorry, I just need to correct the record. I think I said that we were borrowing at 3.9. To be fair, that was on our three-year debt. I have just been advised we are borrowing at 4.7 on our 10-year debt, and I think we will get the number for our three-year debt soon for you as well.

The CHAIR: Thank you. I assume Hansard have got that. Treasurer, where did the previous Government report the amount of contributions to the fund in the budget?

The Hon. DANIEL MOOKHEY: They never did. The last statement that I'm aware of that the previous Government made in its budget papers, I believe it was chapter three of *Budget Paper No. 1* in 2021-22, in which there was a box that described it rising to $90 billion. Then I think it was page 46 of the half-year review of 2021-22, in which they then said it was $81 billion. Now, that's a good question, Chair, because I spent—

The Hon. WES FANG: You wrote it.

The Hon. DANIEL MOOKHEY: I spent two weeks going through the back of the budget papers in June 2021 as the Opposition's shadow Treasurer, trying to understand why we were having to—where else the inflow was. I've got say, I really got to understand the difference between the particular line item in the accounting statement that is—I think it's in the cash flow statement—around net borrowing for liquidity purposes versus net borrowing for policy purposes and the difference between it. If you then traced all the lines through there and you then benchmarked it to previous earlier reports, you could definitely see there was a shock.

Chair, you might be making the point that there might be more transparent ways upon which to report what's going on with the DRF. As a person who is not an accountant and not an expert in government finances at that time, I definitely wouldn't encourage people to spend two weeks trying to get to the bottom of how to read the New South Wales Government accounting statements. Incidentally, I would say at that time it was a credit to the Victorian Treasury that they actually published a glossary that explained every term that was in those cash flow statements, because armed with that knowledge, you could actually figure it out.

Dare I say, I wasn't unique in that. I may have been a layperson at the time, but there were other market participants who were struggling just as much to understand what was going on with the finances at the time. In fact, at the time, as I was saying, when I was interrogating what was going on and talking to market participants, including Mr Joye and others, I was meeting with bank analysts whose full-time job is to analyse bond issuance, who were making the point that it took them a while to figure out what was going on and what explained the shock.

Equally, I would point out—and I can't speak for S&P—that I think when S&P issued their report, they made reference to the fact that they had to issue that report in response to interest amongst their clients for an explanation as to why the spreads had deviated so much from market expectations at that point in time. I definitely think that this Committee should think about whether or not there are better ways upon which contributions can be reported to that so people can at least know what's going on.

The Hon. WES FANG: You have the chance to do something about it.

The Hon. DAMIEN TUDEHOPE: Do your job.

The CHAIR: Thank you for attending this hearing. Committee members may have additional questions for you after the hearing. The Committee has resolved that the answers to these, along with any answers to questions taken on notice today, be returned by—

The Hon. DANIEL MOOKHEY: Chair, sorry to interrupt you, so I don't have to come back to it on notice, if I can just add to clarify one further detail. I said that we were borrowing at 3.98. On our three-year debt, we're borrowing at 4.26 as of today, I believe, or yesterday—

MARINA VAN DER WALT: Last night.

The Hon. DANIEL MOOKHEY: Last night. When markets closed last night, New South Wales' three-year debt was trading at 4.26 per cent.

The CHAIR: Thank you, Treasurer. The Committee has resolved that the answers to supplementary questions—additional questions, rather—along with any answers to questions taken on notice today, will be returned by Monday 31 July 2023, and the secretariat will contact you in relation to these questions. I thank all witnesses who gave evidence today, and that concludes the public hearing for this inquiry.

(The witnesses withdrew.)

The Committee adjourned at 15:10.