1. How to look at SALM?
2. Useful features
3. Challenges in use
4. To what extent is it used in Australia?
What is ALM for government?

➢ For the *private sector* (business) it is an *‘optimizing tool’*
  • A key focus of financial risk management to dampen volatility of returns and value

➢ For *government* it is a *framework/guidelines*
  • Government has a wider range of assets, liabilities & risks to consider. Different governance & decision making processes to match multi-dimension objective function. Challenges in managing longer-term social, fiscal and economic policy aims with very many variables (inflation, currency shifts, business confidence etc)
What are useful features for government?

- Can use to gain efficiencies in cash management; and Budget structure
- Better identify and understand risks to balance sheet (*although measurement, appetite and mitigation are another matter*)
- Can be used to impose discipline on fiscal policy decisions
- Helps to clarify fiscal aggregates (cash balances, net worth, gross debt, net debt etc)
Challenges in using an ALM approach?

➢ Who decides the ‘shape’ of the balance sheet – usually relates to policy decisions – not delegated to a committee or ‘balance sheet manager’ (although there is scope for an advisory role)

➢ How to resolve conflicts between competing policy objectives (for eg fiscal exposure to indexed welfare benefits and issuing inflation indexed debt) OR value assets (such as multiple-use non-financial assets)?

➢ Policy directions can and do change appreciably with a change of government – this could shorten horizon of useful balance sheet planning
Challenges cont..

➢ How is risk appetite determined and expressed?
➢ Who becomes the ‘gatekeeper’ for introducing new risks to the balance sheet (contingent liabilities; new borrowing; hypothecated funds, etc)?
Australian Government Public Sector

Government ‘owns’ all of these entities but balance sheet is not managed as a whole – nor are cash flows associated with corporations included in Budget aggregates

<table>
<thead>
<tr>
<th>Public Financial Corporations</th>
<th>General Govt Sector</th>
<th>Public Non-financial corporations</th>
</tr>
</thead>
<tbody>
<tr>
<td>Created as separately managed entities by legislation:</td>
<td>Includes:</td>
<td>Provide a range of services (eg defence housing; postal service; defence procurement)</td>
</tr>
<tr>
<td>Includes: Reserve Bank of Australia</td>
<td>• Agencies and departments funded by Budget,</td>
<td>Receive - equity injections &amp; loans from Pay- dividends</td>
</tr>
<tr>
<td>Sovereign Wealth Fund</td>
<td>• Cash portfolio</td>
<td></td>
</tr>
<tr>
<td>Export Finance Corp</td>
<td>• Sovereign debt portfolio</td>
<td></td>
</tr>
<tr>
<td>Largely <em>self-funded</em> but pay dividends</td>
<td>• Dedicated funds (for policy purposes)</td>
<td></td>
</tr>
</tbody>
</table>

* *self-funded* but pay dividends
To what extent is ALM used in Australia?

➢ Sits in a broader context - primary tool is a fiscal strategy that incorporates commitments to managing a number of fiscal aggregates (Underlying Cash Balance; Net Debt; Net Financial Worth)

➢ There is no central ‘single’ manager of the government balance sheet – the largest asset pool (Future Fund) and Debt Portfolio are managed separately – is this a problem?

➢ There is a legislated ‘Charter of Budget Honesty’ and policy commitment to triple-A sovereign credit rating – these are to an extent ‘anchor points’ to fiscal and balance sheet discipline
To what extent is ALM used in Australia? cont…

➢ There is highly centralised cash management (all expenditures for GG sector ‘released from’ a central government fund)

➢ Generally a good awareness of balance sheet risks (but can conflict with policy aspirations); main risks are guarantees; loan ‘performance’; inflation; interest rate; fx; returns on financial assets

➢ FX risk is not actively managed

➢ The use of dedicated ‘funds’ continues to some extent but awareness is improving