

12 November 2014

## **Treasury Response to the External Review of Treasury's Fiscal Policy Advice**

Today marks the publication of the External Review of the Treasury's Fiscal Policy Advice.

In the spring of last year, the Treasury committed to undertake a review of its fiscal policy advice, focusing on performance over the last decade. Almost twenty years after the Fiscal Responsibility Act came into force, and having weathered the effects of the global financial crisis, we considered it a good time to review the fiscal policy framework and the Treasury's advice within that framework, to ensure it has been - and will be - appropriate to the characteristics of the New Zealand economy, and consistent with best international practice.

The review demonstrates the Treasury's ongoing commitment to the assessment and improvement of our performance. The choice of conducting this assessment by External Review was intended to ensure full transparency in the analysis of the Treasury's fiscal policy by bringing an outside viewpoint and international comparison.

The Treasury would like to thank our reviewer, Teresa Ter-Minassian, for her work on the report. As a former director of Fiscal Affairs at the IMF, Ms Ter-Minassian has a wealth of technical expertise and awareness of international fiscal regimes which have been invaluable to the Review.

The Review shows that although New Zealand's fiscal policy framework differs from that in many other countries, and despite facing many economic challenges as a result of our small size and distance from major markets, the performance of the government accounts has been strong in the face of substantial shocks. While it has been the decisions of successive governments that have produced this performance, Treasury advice is assessed to have informed and supported much of this.

The Review also highlights the Treasury as a 'first-class' example of performance-orientated financial management, in terms of transparency, breadth of coverage and commitment to fiscal responsibility. We also welcome the recognition of our work as being in line with international best practice in preparing long-term fiscal projections, the development of the Living Standards Framework, the analysis of the Crown's balance sheet, and our efforts to improve inclusivity through seeking input and feedback from external specialists.

The report also discusses areas where the way in which we put together our advice can be improved. We thank Ms Ter-Minassian for identifying these in her report, and for developing a series of recommendations for the Treasury's consideration. The detail of these recommendations is extensive. As a result, the benefits of the Review are likely to be reaped over a long period, as we seek to address these points with the depth of analysis and considered approach that we aim to bring to all policy advice.

There are recommendations identified by the Review which it is clear we can begin to address more quickly, and in some cases we have already begun work on. These include:

- Further detailing the Treasury's views on fiscal policy settings relating to the fiscal-monetary mix, and targets for net debt, which have been incorporated into advice provided to the Government from Budget 2014 onwards.
- Systematically including in Budget documents more extreme (tail risk) scenarios for the economic and fiscal forecasts. We recognise the need to understand the potential impacts of shocks of a similar magnitude to those that occurred in recent years.
- Conducting more systematic analyses of the impact of general fiscal risks on major components of the balance sheet, taking into account the correlation of such risks within and among different types of assets and liabilities. The Treasury is already 'pioneering' in conducting analysis of the government's balance sheet, as shown by the publication of the 2014 *Investment Statement*; the Treasury intends to develop this analysis further to better understand the correlations between different parts of the Crown balance sheet.
- The development and integration of the models used for macro-economic forecasting with those for long-term projections and policy analysis, and the construction of a new form of model to estimate the effects of fiscal policy options. The Treasury has undertaken work to identify the potential for developing such models, and to understand the resources required in their research and development in future.
- Continuing to engage with other departments and agencies in a collaborative effort to 'lift the collective game' in improving the sustainability, efficiency, and effectiveness of operating and capital spending, and of the Crown's assets. We aim to continue to develop the tools for performance-orientated financial management across government.

The Treasury will take into account all the recommendations of the Review, and reflect these in the analysis that informs the advice provided to current and future governments, and is included in key Treasury publications such as the *Economic and Fiscal Updates*, *Long-Term Fiscal Statement* and *Investment Statement*.

We hope that the Review encourages informed public discussion and increases the visibility of New Zealand's fiscal policy framework in the international arena.