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• BUDGET SPEECH •



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TREASURER
MINISTER OF FINANCE

23 May 2002

Budget Speech

Mr Speaker, I move that the Appropriations (2002/2003 Estimates) Bill be now read a second time.

Budget 2002 represents the completion of the fiscal aspects of the programme announced in the Speech from the Throne at the start of this Parliament. It is, therefore, appropriate in presenting this Budget to look back over the last two and a half years as well as to look forward to the framework for growth and innovation which will help drive the lifting of New Zealand's long-term economic performance.

On entering office, the Labour-Alliance Government made it clear that it had certain key policy commitments which it was determined to implement quickly to keep faith with the electorate. This would require significant front-end loading of expenditure during the parliamentary term. A counting limit for the period of \$5.9 billion was initially set, and was raised to \$6.125 billion in Budget 2001. That revised counting limit has been adhered to in Budget 2002 with net new spending totalling \$6.124 billion, excluding some limited spending on new security measures arising out of the events of last September.

The most important commitments that drove that front-end loading were related to New Zealand Superannuation, income-related state housing rents, and tertiary student loans and fees.

With respect to New Zealand Superannuation, the previous National Government had determined to lower the wage-relativity floor from the 65 percent base relativity level set in the 1993 multiparty accord to 60 percent. Restoration of that level to 65 percent by the present Government will cost some \$684 million during the period over which the counting limit applies. The result is that a married couple on New Zealand Superannuation is now receiving \$21 more a week than would have been the case under the policies we inherited.

The restoration of income-related rents for state housing has cost an estimated \$257 million over the same period. The Government regards this as quality expenditure. It has significantly increased the disposable income of many low-income households as well as exerting some downwards pressure on rental prices at the lower end of the housing market.

Finally, the abolition of interest payments on student loans while students are still in full-time study, other changes to the loans scheme, and funding to enable tertiary fees to be held at constant levels instead of the large annual increases to which students had been subjected have a fiscal cost of \$490 million over the same period.

These three key elements, which contribute to social equity, economic development and a restoration of faith in the integrity of government, thus account for nearly a quarter of the total net new spending of \$6.124 billion. The remainder, \$4.7 billion, represents a tight net new expenditure level for all other priorities.

This emphasises how sound and prudent the Government's fiscal management has been. At the beginning of this term of office, in the March 2000 *Budget Policy Statement*, I forecast that Government spending would be 33.5 percent of GDP in the 2002/03 year that this Budget covers. The actual estimate of spending for 2002/03 is 33 percent of GDP. Gross debt was forecast to be 30 percent of GDP and net debt 18.9 percent. Gross debt is now estimated at 28.6 percent and net debt 16.8 percent.

Thus, despite the concerns expressed by many at the start of the Government's first term in office that expenditure would not be well managed, it has been and within sound parameters. There has been but one modest increase in the counting limit, and that was to cater for unavoidable pressures associated with preserving our national and regional security.

The Government is clearly on track to meet the operating balance and debt goals that it has set for the term. Indeed the operating balances now forecast are stronger than previously anticipated. The operating outturn for the 2001/02 year is now expected to be an operating surplus of \$2.6 billion. The more meaningful measure, the Operating Balance Excluding Revaluations and Accounting Changes, is estimated for 2001/02 at \$2.3 billion. This is more than adequate to cover the transfer into the New Zealand Superannuation Fund of \$600 million in the current year.

For the fiscal year 2002/03 the operating balance is forecast to be \$2.3 billion compared with the transfer into the Fund of \$1.2 billion. For the outyears the operating balances forecast are \$3.1 billion and \$3.9 billion compared with Fund transfers of \$1.8 billion and \$2 billion.

The Government will, therefore, be placing New Zealand in a much stronger position for the future. Net Crown debt is forecast to be around 17 percent of GDP at 30 June 2003 and around 15.5 percent at 30 June 2006. The accumulated assets in the New Zealand Superannuation Fund will be \$1.9 billion or 1.5 percent of GDP at 30 June 2003 and \$8.9 billion or 6.3 percent of GDP at 30 June 2006.

Consequently, net debt minus the Super Fund assets will, at the end of the forecast period, be down to 9.3 percent of GDP. It will continue to fall rapidly thereafter with the surplus in the Fund forecast to equal net debt by 2009/10.

The Government set itself responsible but tough fiscal goals on assuming office. It has met them and provided for the future in a way which no previous New Zealand Government has. We could be fiscally feckless now – governments have always found that to be an easy option – but only at the cost of substantially increased future fiscal strain.

Mr Speaker, by far the single largest item of increased expenditure is Vote Health. In each of the next three years \$400 million is being added cumulatively to health expenditure, to a total of \$2.4 billion. This is in addition to baseline adjustments for demographic change, which average around \$100 million a year. It is also in addition to special funding of \$149 million spread over the next three years (with the bulk allocated for 2003/04) to provide for meningococcal vaccination to deal with the scourge which has afflicted so many young New Zealanders in particular, in recent years.

The major increase in Vote Health is an additional \$1,220 million over the next three years for district health boards. But the Government lays greater stress on the significance of

the \$410 million that has been set aside for the progressive implementation of its Primary Health Care Strategy.

With other factors pushing health expenditure, the result is that forecast Vote Health operating expenditure rises from \$7.4 billion in 2001/02 to \$7.9 billion in 2002/03, \$8.5 billion in 2003/04, and \$8.9 billion in 2004/05.

To put it another way, total health expenditure has risen from 5.2 percent of GDP in 1989/90 to 6.4 percent in 1999/2000 and is expected to be 6.8 percent in 2004/05. As a proportion of government spending it is forecast to have gone from 13.9 percent to 21 percent over the same period.

This strong upward trend is not matched in any other major area of government expenditure during this period. It is driven by a continuation of circumstances such as the ageing of the population and the availability of new surgical procedures and new pharmaceuticals.

Clearly there is a limit to the extent to which Vote Health can grow much faster than nominal GDP without placing excessive fiscal pressure on future governments. In this period, it is crucial that those in the health sector understand that the building into the expenditure baseline of substantial increases does not represent an opening bid to which they may respond with higher bids. The sector and the Government will need to cooperate to ensure spending is kept within the forecast path.

Internationally, there is generally a very close relationship between GDP per capita and the proportion of GDP spent on health per head. New Zealand is, and has been for some years, pretty well exactly on the trend line. On the basis of current projections the health funding path will keep us there.

Mr Speaker, from this two conclusions flow. The first is that to increase substantially the proportion of GDP spent on health we will need to lift our sustainable growth rate beyond the rate to which we have been accustomed, and which is still embedded in current long-term forecasts. The second is that our capacity to do that will not be assisted by excessive growth in expenditure which squeezes out opportunities for contributing directly to economic development.

Budget 2002 reflects the new commitment that this Government has brought to assisting economic development. This was signalled in Budget 2000 with the initial funding for Industry New Zealand.

The growth and innovation framework, released in February, marked a further stage in this reorientation of the role of government away from that of simply being a neutral referee disinterested in the outcome. For it is on the outcome that our social and economic fortunes depend.

The growth and innovation framework does not envisage yet another bout of theory-driven restructuring. It sets out a comprehensive programme aimed at lifting our game and raising our sustainable growth rate through innovation. Innovation, however, transforms at the margin. It is no substitute for, and indeed relies on, a strengthening of our economic foundations.

The framework is different in two crucial respects. It does not simply place the emphasis on economic results, with social dividends to flow at a future undefined time when they

can be afforded. It lays out a pathway where social development and environmental protection not only rank alongside economic growth, but become agents of that growth. It thus expresses this Government's firm commitment to sustainable economic development.

Secondly, it blends the vertical and horizontal dimensions of change.

The vertical dimension can be seen as a chain of innovation. In order for innovation to take place routinely and often, we cannot have missing links or weak links in the chain. It starts with the basic ideas that will eventually underpin new enterprises and industries. Ideas have to be nurtured through appropriate support systems, in order to convert them into profitable enterprises.

Production has to be funded and marketed. We need to fill any gaps that might exist or emerge in the venture capital market, encourage an inflow of foreign direct investment to leverage the potential of the embryonic industries, and expand market opportunities by both forging new trading partnerships and exploiting the full potential of those that already exist. In doing this, we intend to use the network of talented and well connected Kiwis who reside abroad to tap ideas, sources of capital and market opportunities. Highly skilled people have to be available to supply the needs of an increasingly sophisticated economic system, and so education, training and immigration policies need to be recalibrated around the requirements of an innovative culture.

On the horizontal level, we recognise that there are advantages of environment and national aptitude and attitude that need special attention if we are to deepen activity and avoid too thin a spread of activity. There is no point in a focus on an area of advantage unless it is also an area where the potential of the global market coincides with the potential of New Zealand to sell into it.

We have identified three areas where there is a good fit: biotechnology, information and communications technology, and creative industries. It is important to stress that we are not trying to pick industries as winners. Innovative advances in these areas have the potential to complement each other and to thicken value added in a number of industries that use the technologies. They are sectoral competencies that have multi-industry applications.

In constructing Budget 2002, Cabinet agreed that economic transformation, the process of implementing the growth and innovation framework, should be one of three priorities along with health and education. Indeed, a good part of the resources flowing to education are central to that transformation, which will not be sustained except with an increase in the quality and quantity of human capital.

Budget 2002 forecasts solid, sustained growth over the current year and the two following, averaging 3 percent. This will put New Zealand growth rates in the top half of the OECD over this period should present forecasts translate into reality.

This is consistent with New Zealand performing at the upper end of its presently assumed 3 percent sustainable growth rate. There is now a broad consensus that there is a need to lift that sustainable growth rate, in the first instance to somewhere around the 4 percent mark if we are to see a long-term rise in our standard of living relative to the rest of the developed world. There is far less consensus about the means to achieve that lift in performance.

In achieving such a consensus we need to recognise three facts which are all too often ignored. The first is that New Zealand's long-term growth performance has been by no means calamitous. The absolute standard of living of the average New Zealander is far higher than it was some 50 years ago. This is reflected in such key indices as life expectancy, infant mortality, and ownership of a wide range of key consumer goods. New Zealand has not seen a declining standard of living: its growth has simply not been as fast as in some other countries. This should serve to avoid the bouts of panic which sometimes seem to afflict at least some commentators.

The second fact which must be recognised is that this long-term underperformance – for such is its real nature – is due to a complex interrelationship of factors which do not lend themselves to simplistic bumper sticker solutions.

The third fact is that there is little evidence to support what are sometimes portrayed as the key reasons for that underperformance and therefore the guides to its improvement.

The most frequently asserted of these is the contention that New Zealand is highly taxed by developed country standards. This assertion usually rests upon a misrepresentation, wilful or otherwise, of the comparative tax rates and structures of different countries. New Zealand is highly unusual in having very little by way of social security taxes or levies on either individuals or businesses. Even in comparison with Australia, with its Medicare levies and compulsory superannuation payments, this can give a very misleading picture if comparisons are made without taking all such factors into account.

That New Zealanders themselves make such comparisons to the detriment of our image overseas in order to support partisan arguments domestically is a sad commentary on our inability to deal rationally with taxation issues.

A recent *Economist* article compared the total cost to business of corporate taxes, social security levies, local body rates, and excise duties. In the six countries studied the total burden varied from 9.5 percent of GDP (for the USA) to 19 percent of GDP (for France). The comparative figure for New Zealand is about 7 percent of GDP.

A more broadly based study of the tax wedge on labour carried out by the OECD showed that New Zealand had the third lowest tax wedge out of 29 OECD nations. Only Korea and Mexico had lower figures. The New Zealand figure was less than half of that of 15 of the OECD nations.

Thirdly, tax plus our only social security levy, ACC contributions, for a single person on the average full-time wage represents about 20.5 percent of gross income in New Zealand. This is lower than 12 out of 15 countries in another recent *Economist* study.

Finally, New Zealand has more experience of the effects of major cuts to tax rates than almost any other developed nation in the last 15 years or so. Significant cuts to personal taxes in 1986, 1988, 1996 and 1998 and a massive cut to the corporate tax rate in 1988 all failed to lift the sustainable growth rate.

There are significant revenue losses that result from tax cuts, with consequential pressure on either expenditure or the Government's operating balance. Therefore, the onus of proof rests upon the proponents of such cuts to demonstrate that they will lead to anything other than the unsustainable and inflationary lift in the growth rate that would come from any fiscal loosening. So far their failure to do anything more than offer repeated assertions is apparent to the great majority of New Zealanders.

There is very little point in taking bold steps in the wrong direction. This is not to say that there are not ways in which addressing problems in the tax system can contribute to improving economic efficiency and performance.

The Government has given particular priority to simplifying the tax system, especially for small to medium-sized enterprises. We have been tackling the issue on two fronts – the policy front and the operational front.

Inland Revenue is reviewing its operations so as to provide better services to taxpayers targeted at the specific needs of different industries and variations over time in those needs.

On the policy side, the Government moved quickly to legislate clear laws in the priority areas identified by the private sector. This included clarifying the tax treatment of expenditure on research and development and removing complex rules on company interest deductions.

Tax legislation now in front of Parliament includes further major areas of simplification. They include clarification on over- and underpayments, reducing the number of taxpayers exposed to use-of-money interest and allowing the pooling of tax payments.

We will be doing further work on simplifying the tax obligations of small to medium-sized enterprises. We will be examining whether current legal forms available to small business are appropriate, and developing ways of reducing the tax impact on businesses during different phases of their life cycles.

The Government is also reviewing the existing rules to see whether income can be calculated on a cash rather than an accrual basis for small taxpayers.

The second area of great interest to the Government is the taxation regime on superannuation. Considerable discussion has occurred on this matter. It now seems clear that the largest amount of leverage over savings behaviour at reasonable fiscal cost is likely to be achieved in relation to employment-based superannuation. As a first step, I am considering two options.

The first is to reduce the employers' specified superannuation contributions withholding tax for those earning under \$38,000 to their statutory marginal tax rate. The alternative is to extend the present 6 percent concessional rate enjoyed by those earning over \$60,000 a year to all income earners. It is my intention that one or other of these changes will be introduced from 1 April 2004.

The Government is not considering upfront tax incentives. These are likely to have to be very large – with fiscal costs running to many hundreds of millions of dollars a year – before they have any desirable effect on overall savings. Their abolition in the mid-1980s represented sensible tax policy on both equity and efficiency grounds.

The third area of the tax system which requires attention to assist economic transformation are those aspects of the international tax regime and related matters which may encourage investment and skilled migration. The recommendations of the McLeod Committee in this area are under intensive study.

Possible avenues for exploration are the introduction of a time-limited exemption for overseas earnings for new migrants and the application of the risk-free return method to

the broad area of offshore equity investment on capital account outside a business context. Officials have concluded that significantly lower rates of tax could not be restricted to new foreign direct investment except as a transitional measure. As a consequence, it seems unlikely that such a reduction would produce sufficient benefits to New Zealand to offset the welfare costs of raising revenue on other productive activity in New Zealand.

No decisions have yet been taken in these respects and given the complexity and likely controversial nature of any changes in the international tax regime, a further round of consultation with the private sector will be undertaken.

Underpinning all of these tax issues is the need to lift investment in the New Zealand economy. This, along with increasing our human capital, promoting exports, encouraging innovation, and transforming that innovation into successful businesses are surely the basic elements of economic transformation.

Budget 2002 incorporates a major new initiative to attract investment. The Government has decided to merge the Investment New Zealand arm of Trade New Zealand and Industry New Zealand's Major Investment Service into a single world-class investment promotion agency operating under the wing of Industry New Zealand. The budget for the new agency will initially be \$14.5 million. I anticipate that, as the agency gets underway, it will be able to make use of substantially increased funding to generate greater investment consistent with the Government's overall economic strategy.

Alongside this initiative the Budget provides the resources for expanding the number of investment promotion teams.

The Government's renewed efforts to complement the investment drive will be creating offshore platforms for exporters and the expansion of export networks. These will provide facilities offshore to assist market entry by exporters as well as providing links with expatriate New Zealanders.

Offshore export promotion services will be enhanced to provide greater accuracy of relevant information directed to clients in the timeframes in which they require it. Trade New Zealand will, at the same time, be mounting a series of marketing campaigns targeted at engaging priority sectors and markets through e-business channels.

Supporting the export drive will be a new emphasis on the promotion of brand New Zealand, creating higher-level brand values positioning New Zealand as an exciting, innovative producer of high-quality goods and services.

For such a branding to have substance it is essential that New Zealand is at the forefront in terms of being a networked nation. The Government is putting resources into implementing recommendations arising out of the Boston Consulting Group and LEK reports which were part of the background to the development of the growth and innovation framework.

This includes resourcing of membership of the Global Biodiversity facility – a network of biodiversity databases and information technology databases that enables the use of global biodiversity information to produce national economic, environmental and social benefits. There is a range of other initiatives provided for in Budget 2002, the most important of which relates to the introduction of broadband technology throughout New Zealand.

Tens of millions of dollars have been set aside over two years for a major initiative in this respect. The initiative is funded jointly from Vote Education and Vote Economic, Industry and Regional Development. While the early beneficiaries of broadband deployment will be schools, once it is deployed local businesses and most government departments will also start to benefit.

Broadband is the nervous system of the new economy and is as important to New Zealand as the roads, power lines, railways, and telephone cables were last century.

The Government's objective is to ensure that the majority of schools have access to high-speed two-way internet by the end of 2003, with infrastructure being made available to more remote schools by the end of 2004. This objective will be attained in a way that optimises opportunities for communities to access broadband services as well. Today's funding is a major step towards that goal.

The Government has already funded studies in rural and provincial New Zealand on the impact of broadband on economic development. In addition, the Government has, in partnership with local communities, funded five regional pilots to test a demand aggregation model whereby communities and schools, health centres, tourist operations, transport companies, libraries, marae and others bundle up their demand for the new telecommunications technology and offer that demand by way of competitive tender to telecommunications companies.

The financial resources will be used for a centrally managed series of regional tenders for the provision of broadband infrastructure. There will be opportunities for regional and local government and private sector businesses to work in partnership with the Government, to ensure that their priorities and interests are met through the rollout of broadband to their area.

This initiative emphasises the growing importance of the links between education and economic development in the new economy. If New Zealand needs to be a networked nation, it equally needs to be a learning nation.

This Budget represents the culmination of a reform process to bring about much stronger links between the tertiary education sector and the rest of the economy and society.

The intention is to shift away from a single focus on attracting students to centring much more on contributing to the nation's development through increasing quality, building system capability, and encouraging stronger relationships with the sectors and communities that the system serves.

This is the reason the Government is establishing the Tertiary Education Commission to provide leadership to steer the tertiary education sector and to ensure that all parts of that sector are contributing in a coordinated manner to growth and innovation in New Zealand. This encompasses all learning beyond the school system including industry training, foundation education programmes such as Training Opportunities and Youth Training, adult literacy initiatives, and adult and community education.

A five-year Tertiary Education Strategy will set the strategic direction for the tertiary education sector's contribution to economic and social development through teaching, learning and research.

The Tertiary Education Commission's role is to ensure the Tertiary Education Strategy is implemented. In this it will be guided by the Government's annual Statement of Tertiary Education Priorities, which will establish specific goals, actions and performance measures for the following one to three years.

The Strategy and the Statement of Tertiary Education Priorities will allow the Commission to make an assessment of strategic relevance with regard to courses, programmes and providers. Those that cannot demonstrate strategic relevance will not be funded.

This will become apparent in the short term for private training establishments. Overall funding to private training establishments will be capped next year with new courses, programmes and providers being funded from a strategic pool within the overall cap.

As the information base and experience of the Commission increase, assessments of strategic relevance will be applied increasingly in both the public and private sectors. This will take place as part of a new process of approving organisational profiles for funding purposes.

Together, charters, profiles and the assessment of strategic relevance will ensure that funding to providers is aligned with the key directions in the Tertiary Education Strategy.

The strategic focus will be reinforced through the design of a new, integrated funding framework for all tertiary education, with three broad elements. The first will be funding for teaching and learning through a combination of mechanisms. The second will be funding for research through the Performance-Based Research Fund, Centres of Research Excellence, and existing research top-ups. Finally, there will be targeted funding, through a Strategic Development Fund.

Within the funding for teaching and learning a new Student Component will replace the existing Universal Tertiary Tuition Allowance or "EFTS system". This will balance a commitment to wide participation with performance and strategic considerations. It will contain a performance-related element and will be set on the basis of a rolling funding triennium from 2004 onwards. The Student Component will ensure limits on tuition fees from 2004 through a fee maximum system.

The Performance-Based Research Fund will focus on increasing the average quality of research and improving the quality of information on research output, while underpinning the core strengths of tertiary education research.

The Strategic Development Fund to be established from January 2003 will assist tertiary education organisations to develop capacity in key areas, align better with national development goals, and put in place sustainable long-term strategies.

The Government is committed to lifting the skills of New Zealanders and, in so doing, lifting the profitability of enterprises and the competitiveness of the New Zealand economy. Our prosperity relies on the skills and knowledge of our people and how successfully these skills and knowledge can be applied to generate economic growth. This requires an effective labour market coupled with a healthy tertiary education and training system that achieves a good match between the skills demanded in the labour market and those delivered via education and training.

The record of the Government in this regard is an impressive one.

A total of 95,263 trainees participated in industry training in 2001 compared with 81,343 in 2000 – an increase of 17 percent. A total of 66,225 trainees were registered with Industry Training Organisations at December 2001 – a 5 percent increase over the course of the year. Trainees achieved a total of 9,498 National Certificates during the year – a 52 percent increase.

In our first 100 days in office the Government rehabilitated the notion of apprenticeship and launched the Modern Apprenticeships Programme. Targeted primarily at young people, this initiative applied the traditional strengths of apprenticeship – mentored work-based training – to a wider range of industries including those at the cutting edge of growth and innovation.

There are now over 2,500 young New Zealanders employed as Modern Apprentices in a wide and growing range of industries.

Today I am announcing a commitment by the Government to provide sufficient funding to double the numbers of Modern Apprentices so that we will have 6,000 in employment by December 2003. That represents an additional investment of \$41 million over the next four years.

The Government is also introducing a pilot Māori Trade Training programme which will assist young Māori to make the transition from school to programmes like Modern Apprenticeships.

Modern Apprenticeships also signals the Government's commitment to lifting the rate of participation and the profile of industry training across the board.

In this Budget we make a further investment in the future skills and prosperity of this nation. The Government is to increase the level of the Industry Training Fund by \$14 million over the next four years. This is on top of the additional \$56 million over four years that I announced in last year's Budget and represents an unprecedented investment in industry training.

Industry training is highly cost effective because it attracts a significant industry contribution – currently 30 percent of the cash cost is met by industry. The Government remains committed to a partnership approach to industry training, with Industry Training Organisations being funded to purchase training in line with the needs of industry.

Industry training needs to address the upskilling of those who are in work, as well as provide pathways into learning and employment for those making the transition from school. Over the past year the Government has been piloting the Gateway programme, which gives students workplace experience and opportunities to begin to acquire qualifications. The evaluation of the pilot has been extremely positive and I am announcing today \$7.2 million of new funding over the next four years to enable a continuation and extension of this programme. More schools will now have the opportunity to develop links with local employers and offer a wider range of learning options for their students.

Change in the tertiary education system is already underway with new programmes such as Centres of Research Excellence, Modern Apprenticeships and the Gateway initiative in schools. Changes will build progressively from here. The Strategic Development Fund will come into effect from 2003, charters and profiles will be in place from 2004, and the Performance-Based Research Fund will be phased in gradually throughout the period until

2007. Tertiary education organisations have already started changing their behaviour. Within five years, the system will have changed dramatically in terms of both its composition and its outlook.

The other key element of the integration of tertiary education and economic development is research, science, and technology. Budget 2002 provides for an additional \$27 million in operating expenses and \$20 million in capital over the next three years for Centres of Research Excellence, with ongoing funding of \$11 million a year.

The Government is committing more than \$100 million of new investment to Vote Research, Science and Technology over the next four years, almost half of which is focused on funding partnerships with industry.

An extra \$48 million will be invested in such partnerships over the next four years, mostly through funding of research consortia by the Foundation for Research, Science and Technology. These consortia bring industry and public institutions together for research programmes that are jointly funded, with shared decisions about the direction and focus of the research.

The funding available for consortia will increase by \$6.3 million in each of the next four years.

Such partnerships produce more relevant research and more immediate application of the results. Examples include meat industry research into bioactive compounds for new “functional foods”, such as dietary iron supplements, and research into new forms of wood products and pasture.

Partnership funding is also delivered through Technology New Zealand, which accelerates business uptake of new technology. The Technology for Business Growth programme will be increased by almost \$4 million a year for the next four years. One million dollars a year will support a new “one stop shop” service to coordinate the support that Industry New Zealand, Trade New Zealand and the Foundation for Research, Science and Technology provide to business.

In health research, a partnership for the future has been forged with the Wellcome Trust, which will contribute half of a five-year \$17.5 million research fund focused on improving the health of Pacific peoples. The fund will open in 2003, but the Government’s funding commitment has been made now to secure the Wellcome Trust’s contribution.

Because we recognise that basic research underpins all scientific and technological progress, it receives a substantial funding increase. More than \$34 million extra will be invested in basic research over the next four years, primarily through the Marsden Fund and the New Economy Research Fund. This is the third successive increase in funding for basic research.

The Government is following through on the Royal Commission on Genetic Modification with funding of \$9.5 million over the next four years for the Biotechnology Strategy and for research into the environmental and social impacts of genetic modification. A further \$8 million over four years from Vote Environment will enable us to establish the Bioethics Council and develop necessary law changes.

We will continue supporting excellence in science education with \$1.7 million a year from 2003 for the science, mathematics and technology teacher fellowships.

Total funding for research, science and technology has now increased by \$77 million under this Government, an improvement of 18 percent since we took office.

We are also focused on extracting more value from the public investment in science. Funding is being redirected from mature fields of research, where the private sector can take more responsibility, towards higher-risk opportunities that promise innovation and new business. Public funds are being used more for investigation of new fields such as biopharmaceuticals and natural New Zealand-sourced agrochemicals. We are delivering, in other words, smarter as well as greater investment in science.

Mr Speaker, the emphasis in Budget 2002 has been very much on health, education, and economic transformation. This does not mean that other priorities have been ignored. The Budget contains initiatives covering the entire range of government activity. I want, in the remainder of my speech, to single out four areas: law and order, conservation and the environment, housing, and social services and employment.

Safety and security in the community is a concern to all New Zealanders. The Government has moved to work with the Police, justice, and other government agencies along with the community, to reduce criminal offending.

The latest Police summary of recorded and resolved criminal offences highlights encouraging results. Recorded offences per 10,000 population were down to a 13-year low during 2001. Recorded burglaries were at a 20-year low in 2001.

This year's Budget includes initiatives that allow the Police to continue critical Police operations. Counter-terrorism programmes include increased operational funding for counter-terrorism initiatives at domestic airports and additional resources for counter-terrorism investigation and intelligence-gathering activities.

Second, as the Minister of Police has already announced, an additional \$2.5 million each year is being allocated to assist the Police in Auckland.

The Government has also approved changes to appropriations for 2002/03 and outyears to enhance initiatives jointly organised by the Police and Ministry of Justice to reduce youth offending and violent crime committed by young people. These programmes will be developed in consultation with local authorities and community groups in up to five high-crime areas, including South Auckland and Auckland City.

The Government has developed two new programmes which focus on intensive rehabilitation of serious young offenders. The programmes include the establishment of new Day Reporting Centres. These will provide individualised, intensive, relatively long-term programmes at centres administered by the Department of Corrections and by Child, Youth and Family Services. The programmes will focus on meeting education and vocational needs. Two Centres catering for approximately 130 offenders per year are to be established initially, with \$12 million over four years provided in Budget 2002.

The Government is also creating a new serious recidivist young offenders' programme. This is an 18-month, three-stage programme incorporating a residential period of up to one year. Budget 2002 will provide \$2.85 million (including \$700,000 capital expenditure) over three years. Initially involving one centre, the programme may be expanded to four others if evaluation proves positive.

In Vote Conservation the key feature is the largest increase in funding ever for outdoor recreation on public conservation land.

Over the next 10 years the Government will increase the Department of Conservation's maintenance budget for recreational facilities from \$37 million a year to more than \$80 million a year. DoC will be funded to provide properly for depreciation starting with \$3 million in 2002/03 and rising to \$24.9 million in 2007/08 while also providing for accumulated depreciation at the rate of \$18 million a year for 15 years starting in 2007/08. This means that by 2009/10 DoC's annual recreation budget will be more than double its present level. This will progressively address the scandalous under-maintenance of DoC's recreational facilities.

This funding will ensure that New Zealanders and overseas visitors will be able to enjoy our world-class network of national parks and reserves and our unique flora and fauna. It will ensure that Kiwi kids will be able to explore safely our country and learn about and experience kiwi and kereru, kauri and kahikatea. And because walking and tramping are healthy activities, a spin-off benefit from this investment will be fitter and healthier people.

Budget 2002 is again investing in the protection of New Zealand's natural heritage with funding of \$38 million for this year's Biodiversity Strategy projects. This is the third consecutive annual funding boost for the Strategy, which is designed to prevent the extinction and promote the restoration of our endangered native species.

The Government's \$187 million five-year funding commitment to conservation through the Biodiversity Strategy is the most substantial ever made and provides the investment necessary to turn the tide on the decline of our biological diversity.

The National Energy Efficiency and Conservation Strategy receives a boost of more than \$3 million a year. As we move towards implementation of the Kyoto Protocol substantial additional investment may be required in this area. Other funding boosts to promote environmental concerns occur with respect to the New Zealand Waste Strategy, national policy statements and national environmental standards, clean-up of orphan sites (with \$7.4 million over three years), and reducing business compliance costs under the Resource Management Act 1991.

The present Government has laid great emphasis on improving access to quality housing, especially for low-income New Zealanders. The restoration of income-related rents has been by far the largest cost item in that respect.

Over the next three years \$54 million has been allocated for the expansion of the rental housing acquisition programme, resulting in a total investment of \$262 million for adding to the state rental stock over the period.

The "Healthy Housing" programme will be expanded by \$21 million over the next three years, leading to total expenditure on the programme of \$46 million over the period.

New spending in this year's Budget also includes \$36 million capital expenditure plus associated operating costs over the next three years to address substandard housing in Northland and the East Coast/Bay of Plenty regions. This will help to generate local employment and community pride in those regions.

In the social services and employment package there are some 50 new initiatives. These range from increased funding for the Community Organisation Grants Scheme to the development of an electronic labour market portal.

The largest increases in spending are structured around making it easier for beneficiaries to move into paid employment. These include: an additional \$24.5 million over three years for employment support for people with disabilities, rising to \$15.5 million a year in outyears; \$41.8 million over three years for enhanced case management; and \$27 million over three years for increased funding for out-of-school care and recreation.

Mr Speaker, it will not have escaped the House's notice that 2002 is an election year. Traditionally, election year Budgets have been occasions when Ministers of Finance engage in a mixture of substantial new spending or the promise of tax cuts to come. Often both are fiscally unsustainable and followed by the inevitable reversal of policy the following year.

Instead, the Government has continued to balance prudent fiscal management with innovative policy promises. We chose deliberately to commit resources early in this three-year term to keep faith with the people's expectation of early delivery of key election promises.

The superannuitants on their restored wage relativity, the low-income state house tenant on an income-related rental, the student who is not paying interest on their loan and has not had a fee increase over the past two years all have reason to remember that the Government kept faith with them in those respects.

As the 2002 *Fiscal Strategy Report* notes, we are proud of our achievements. We continue to deliver as promised on our policy commitments, keeping within our spending provision for the term while building up New Zealand's infrastructure.

Yet, at the same time, we have put an unprecedented focus on the future. We have done this in many ways – through our Biodiversity Strategy, our intention to ratify the Kyoto Protocol, our reforms to tertiary education, our creation of new agencies and the provision of new funding for business development, investment attraction, and trade promotion. Above all, in that respect, we have begun to build up financial assets to help fund the longer-term costs of an ageing population. And we have done this while continuing to meet our long-term fiscal objectives and, indeed, exceeding them in many key respects.

It is crucial that New Zealand does not revert to a short term view of life. Tax cuts for a few now which will be paid for by a reduced standard of living for the many later makes neither fiscal, economic, nor social sense.

In Budget 2002 the Government's focus has clearly shifted to the task of economic transformation. This nation has no reason to wallow in either self-pity or self-recrimination about its past performance. Any New Zealander who travels overseas quickly recognises that we are securely part of the democratic, developed world.

But we can do better. Lifting our game as a nation is not just about rewarding a few at the expense of the many. It is about enlisting the support of the many in the interest of improving our standard of living for all. After years of bitter debate over the direction of economic and social change there is now a greater awareness of the need to lift our skills, attract more investment, promote our exports, grow more businesses, and become an innovative, knowledge-based nation known for its excellence and quality.

Budget 2002 contributes to this task in two simple ways. First, it provides an underpinning of sound fiscal management, which puts us in the premier division of the international league for fiscal prudence and predictability.

Second, it prioritises new spending and reprioritises existing spending to those areas which underpin the Government's growth strategy. It is a Budget with its eye firmly focused on the long-term, not just the next six months. It is, most definitely, not an election-buying Budget. It may well be an election-winning one.