

Reference: 20150037

10 April 2015



Thank you for your Official Information Act request, received on 12 February 2015. You requested the following:

“• All advice, briefings, communiques and the like written by the Treasury since 1 November 2014 (that are not currently available on the public Treasury website) for the Minister of Finance, or his office or his associate Ministers or their offices regarding the 2014/15 OBEGAL surplus target.

Where information is withheld, I request you provide the title and date of the communication/document withheld, the reason for refusal and the grounds in support of that reason as required by section 19(a)(i) and (ii) of the Official Information Act.

On 12 March 2015 I extended the time limit for deciding on your request by an additional 20 working days.

Information Being Released

Please find enclosed the following documents:

Item	Date	Document Description	Decision
1.	7 November 2014	Treasury Report: Update on HYEUFU 2014 Forecast and Fiscal Strategy	Release in part
2.	27 November 2015	Draft Cabinet Paper: Budget 2015: PRIORITIES AND OPERATING ALLOWANCES	Release in part

I have decided to release the relevant parts of the documents listed above, subject to information being withheld under one or more of the following sections of the Official Information Act, as applicable:

- personal contact details of officials, under section 9(2)(a) – to protect the privacy of natural persons, including deceased people, and
- names and contact details of junior officials, under section 9(2)(g)(i) – to maintain the effective conduct of public affairs through the free and frank expression of opinions.

In making my decision, I have considered the public interest considerations in section 9(1) of the Official Information Act.

As you have excluded documents already available on the Treasury website from your request, I have assumed you are familiar with information that has been made public regarding the 2014/15 OBEGAL surplus target from previous OIA requests.

Please note that this letter (with your personal details removed) and enclosed documents may be published on the Treasury website.

This fully covers the information you requested. You have the right to ask the Ombudsman to investigate and review my decision.

Yours sincerely

Tim Ng
Director, Macroeconomic and Fiscal Policy

Encl

Information Being Released

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Treasury Report: Update on HYEFU 2014 Forecasts and Fiscal Strategy

Date:	7 November 2014	Report No:	T2014/1748
		File Number:	MC-1-5-2

Action Sought

	Action Sought	Deadline
Minister of Finance (Hon Bill English)	Discuss at fiscal issues	10:30am, Monday 10 November
Associate Minister of Finance (Hon Steven Joyce)	Note the contents of this report	
Associate Minister of Finance (Hon Paula Bennett)	Note the contents of this report	

Contact for Telephone Discussion (if required)

Name	Position	Telephone	1st Contact
<i>Withheld under s9(2)(g)(i)</i>			✓
Tim Ng	Director, Macroeconomic Policy	04 917 6124 (wk)	<i>Withheld under s9(2)(a)</i>

Actions for the Minister's Office Staff (if required)

Return the signed report to Treasury.

Enclosure: No

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Treasury Report: Update on HYEFU 2014 Forecasts and Fiscal Strategy

Executive Summary

This report provides an overview of the 2014 preliminary *Half Year Economic and Fiscal Update* (HYEFU) forecasts and projections along with their implications for the Government's fiscal strategy. It provides you with the opportunity to make changes to fiscal settings prior to the finalisation of forecasts for the HYEFU, which is due to be published alongside the 2015 *Budget Policy Statement* on 16 December.

Not relevant to request

The preliminary forecasts and projections, which assume a \$1.5 billion operating allowance for Budgets 2015-17, remain consistent with making progress towards your fiscal strategy of returning to surplus and reducing debt, but show a delay in meeting your fiscal targets on current fiscal settings. Operating balances are forecast to increase through time which will eventually put debt on a declining path, and core Crown expenses will continue to fall as a share of GDP. However, forecasts now indicate an OBEGAL deficit in 2014/15 of \$1.0 billion and a small deficit in 2015/16 of around \$100 million, compared with forecast surpluses for both years in both the BEFU and PREFU. Net debt is forecast to peak at a higher level, before falling to 20.3% of GDP in 2020/21.

Economic factors explain most of the weaker OBEGAL in 2014/15 since PREFU (\$1.0 billion of the \$1.3 billion downgrade), notably lower tax revenue from lower export prices and interest rates. Core Crown expenses are forecast to be \$0.4 billion higher in 2014/15, largely reflecting the transfer of expenses by Departments from the previous year.

The Government's short-term fiscal intention to return to surplus in 2014/15 has always been "subject to any significant shocks". Given the magnitude of the reduction in dairy prices, a deficit in 2014/15 is unlikely to raise concerns in financial markets and rating agencies about fiscal intentions, as long as the overall fiscal strategy remains on track. That the latter remains true is indicated by the structural fiscal balance being forecast to return to surplus in the same year (2016/17), even though the path is a little lower than in the PREFU in each year of the forecasts.

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Not relevant to request



Recommended Action

We recommend that you:

Not relevant to request



- d **note** that preliminary forecasts are consistent with your overall fiscal strategy to increase surpluses and reduce debt, but show a delay before your fiscal targets are met

- e **note** that re-phasing operating allowances over the Parliamentary term in line with pre-election announcements to \$1 billion for Budgets 2015 and 2016 with a higher allowance in Budget 2017 would be sufficient to ensure progress towards your fiscal objectives beyond 2015, assuming dairy prices rebound as currently forecast

Not relevant to request



Pages 5-8 not relevant to request

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Not relevant to request

13. OBEGAL is forecast to be in deficit by \$1.0 billion in 2014/15 and \$0.1 billion in 2015/16, with a surplus of \$1.2 billion in 2016/17.

Not relevant to request

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OFFICIAL INFORMATION ACT

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Not relevant to request



Fiscal implications

24. Your overall fiscal strategy is to return to a path of rising operating surpluses and falling net debt. The 2014 *Fiscal Strategy Report* outlined the following short-term intentions and long-term objectives:

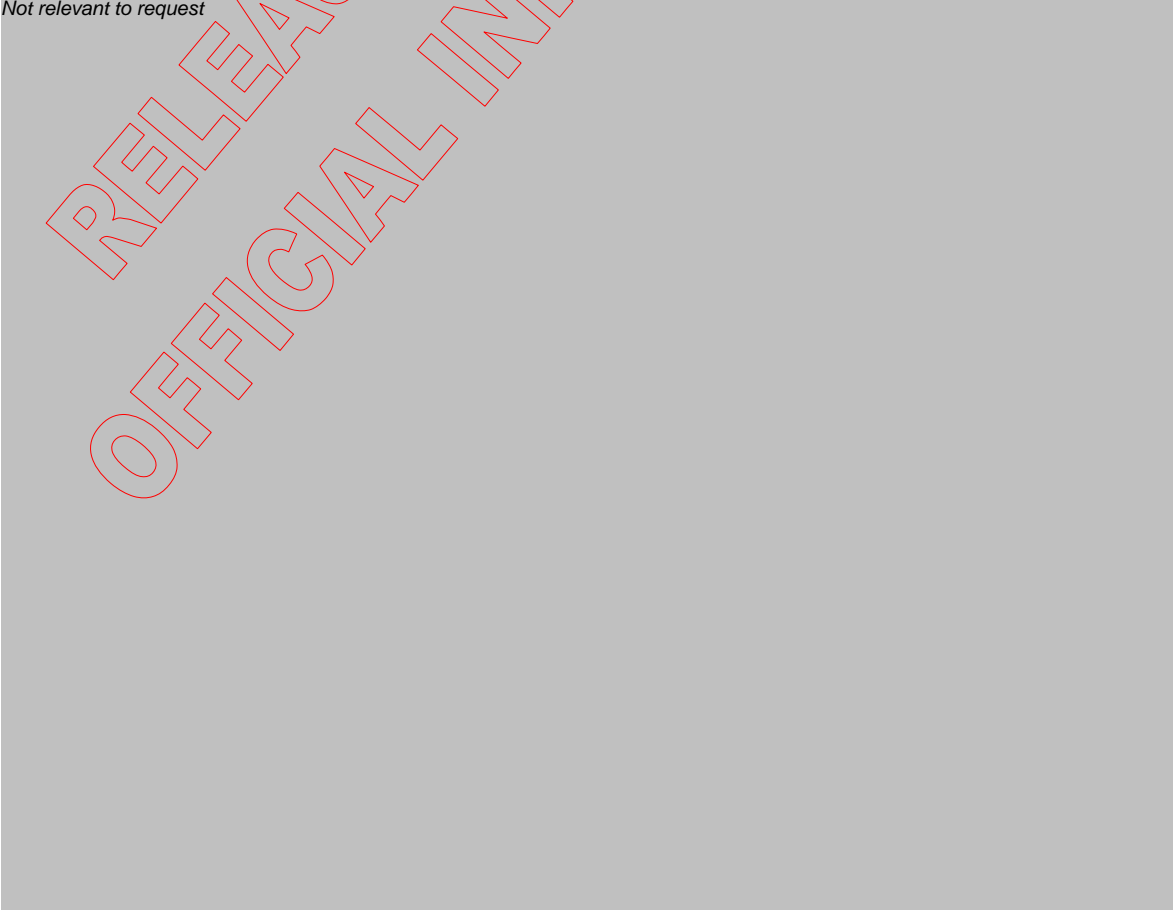
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- Return to OBEGAL surplus in 2014/15 and to run increased surpluses thereafter, and
 - Reduce net debt to 20% of GDP by 2020, and maintain it within 10-20% over the economic cycle.
25. Preliminary forecasts and projections show the Government is broadly on track to achieving its fiscal strategy, although progress towards the fiscal intentions and objectives has been delayed compared with Budget 2014. This section discusses each objective in turn.

OBEGAL

26. The Government's preferred fiscal balance measure, OBEGAL, remains on an improving path. The OBEGAL deficit is forecast to continue declining and return to surplus. However, current forecasts show the return to surplus is delayed until 2016/17. The goal to return to surplus in 2014/15 has always been "subject to any significant shocks". The large negative shock to dairy prices and uncertainty around the forward path suggest a need to reconsider the appropriate timeframe for returning to surplus. The structural balance is forecast to return to surplus at the same time as previously estimated (2016/17).
27. There are limited options for returning to surplus in 2014/15, although some options remain. Increasing revenue, through levies and excises or pharmaceutical payments, or reducing expenses, e.g. treaty spending and ODA, would improve the fiscal position in 2014/15. If expenditure is pushed out to future years, the impact on 2015/16 should be considered. Any decisions you take to reduce the forecast deficit in 2014/15 will be reflected in final fiscal forecasts.

Not relevant to request



Pages 12-17 not relevant to request

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Office of the Minister of Finance

27 November 2014

Chair
CABINET


Budget 2015: PRIORITIES AND OPERATING ALLOWANCES

Not relevant to request



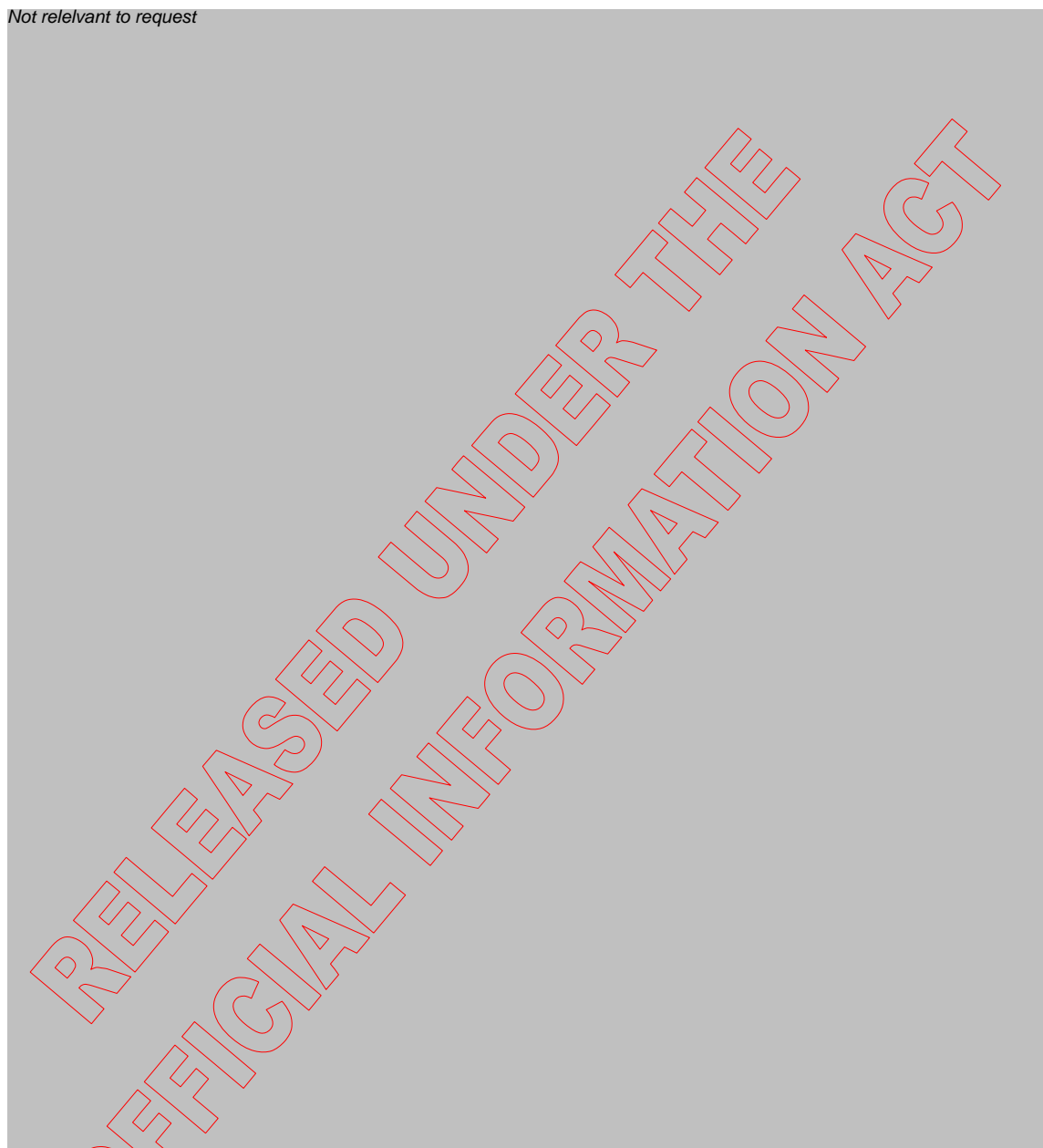
3. In this context, the Government's focus remains on successfully managing the growing economy and delivering our long-standing fiscal objectives. Over the past two Parliamentary terms the Government's fiscal strategy has ensured we have remained on a solid and credible path despite facing a number of severe economic and fiscal challenges. While the recent fall in global dairy prices has made the immediate goal of returning the operating balance to surplus more challenging, the Government remains on track to meet its longer-term objectives of reducing net core Crown debt and expenses.

Not relevant to request



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Not relevant to request



10. Given the lower forecasts for tax revenue, under this operating allowance profile the forecasts to be published in the Treasury's *Half-Year Economic and Fiscal Update* (HYEFU) will show a return to surplus in 2015/16. However, with the underlying strength of the economy combined with constrained government spending, I remain confident we can still deliver a surplus this fiscal year when the final accounts are published in October 2015.

Pages 3 and 4 not relevant to request

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Continuing to deliver responsible fiscal management

Current fiscal strategy

18. Returning the operating balance before gains and losses (OBEGAL) to surplus has driven our past Budget decisions. Over the past six years we have navigated a global financial crisis, a recession, the Canterbury earthquakes, and a slow global recovery. This required us to run temporary deficits and led to a build up of debt. However, our efforts over the past two Parliamentary terms have ensured that, through all of this, the fiscal position remains on a solid and credible path. As the economic recovery continues, our focus has moved to managing a growing economy. We aim to deliver sustained economic growth over the medium-term, keeping interest rates lower for longer to help households with mortgages, business investment, and exporters by taking pressure off the New Zealand dollar.

19. Our key target continues to be delivering an operating surplus in 2014/15, which will only be known once the final accounts are published in October 2015. The recent fall in global dairy prices and lower interest rates has made this goal more challenging. The lower dairy prices and resulting reduction in incomes earned by our dairy producers, means the growth in the Government's tax revenue is now expected to be lower than previously forecast. In addition, the forecast for interest rates to remain low for longer compounds the tax weakness by reducing RWT, which shows the largest downward revision of all tax types. These effects have not yet shown up in tax outturns, which have been relatively strong to date. However, tax revenue is anticipated to weaken later in the 2014/15 fiscal year.

20. Forecasts to be published in HYEFU will show a small deficit in 2014/15 of \$572 million, with the return to surplus expected to be achieved in 2015/16 – a year later than forecast at Budget 2014. While a surplus in 2014/15 has long been a goal of this Government, I do not propose to respond with large adjustments to our tax and spending plans that may destabilise economic and social outcomes.

21. At only 0.2 per cent of GDP, the forecast deficit in 2014/15 is unlikely to raise concerns among financial markets and rating agencies about our fiscal intentions. This is particularly so given our goal to return to surplus in 2014/15 has always been "subject to any significant shocks", such as the recent significant fall in global dairy prices. Conditions in global dairy markets are also expected to be largely temporary, with prices expected to recover through 2015. As a result, despite the delay in achieving an operating surplus, the Government remains on track to meet its longer-term fiscal objectives. The core Crown residual cash balance is now expected to return to surplus in 2017/18, a year earlier than at Budget 2014, due to lower forecast capital spending. As a result, net core Crown debt is forecast to be \$1.5 billion lower by the end of the forecast period and is projected to fall to under 20 per cent of GDP by 2020/21. Core Crown expenses are also forecast to reduce to around 30% of GDP by 2015/16.

22. It is also worth noting that the HYEFU forecast for 2014/15 is not yet a reality and forecasts can move significantly in a short period of time. The underlying strength of the economy combined with constrained government spending can still deliver a surplus this fiscal year when the final accounts are published. While many of the swings in tax revenue such as those from movements in global dairy prices are

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beyond our control, we do have more control over government spending. Over the past six years we have shown that increases in government spending are not required to deliver better public services if we address the drivers of public service costs and demand.

23. Part of the weaker forecast in 2014/15 represents higher spending forecasts by departments of around \$400 million, mainly reflecting spending transferred into 2014/15 from the previous year through expense transfers and automatic roll-overs of unallocated spending in multi-year appropriations (MYAs). Some examples of these increases included in HYEFU were expense transfers totaling over \$200 million for health spending, Aquaculture Settlements, Ultra-Fast Broadband and Apprenticeships Re-Boot, among others. A continued strong focus on managing spending over the next few months will increase our chances of turning this deficit around.

Not relevant to request



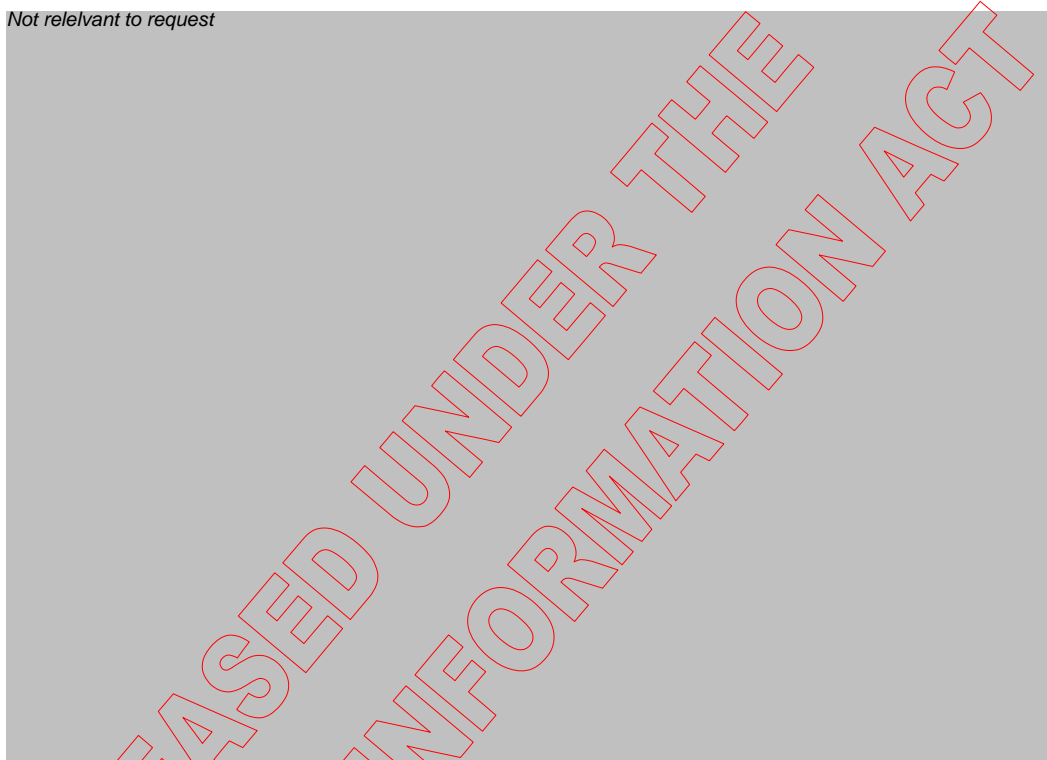
Pages 7-10 not relevant to request

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Recommendations

50. I recommend that Cabinet:

Not relevant to request



6 **note** that progress continues to be made towards the Government's fiscal targets, as the OBEGAL deficit has declined and net debt is projected to fall to under 20 per cent of GDP by 2020/21

7 **note** that forecasts in the *Half-Year Economic and Fiscal Update* will show the return to surplus has been delayed until 2015/16, reflecting the sharp downturn in dairy prices

Not relevant to request



Hon Bill English
Minister of Finance