

Reference: 20170004

10 April 2017



Thank you for your Official Information Act request, received on 11 January 2017. You requested the following:

- *A copy of any reports, briefings and advice prepared by Treasury regarding the Crown's exposure to the Kaikōura earthquake, since November 2016;*
- *A copy of any reports, briefings and advice regarding the Kaikōura earthquake recovery, since November 2016.*

You subsequently clarified that your request covered advice prepared by Treasury and sent to Ministers' offices. You also clarified that you are particularly interested in the cost to the Crown and impact on the Crown's books, such as documents relating to infrastructure costs, tax, EQC exposure, tourism and impact on businesses.

On 27 January we transferred responsibility for the document "Kaikoura and Marlborough Earthquake Relief Package" to the Ministry of Health, and on 30 January we extended the time limit for deciding on your request by an additional 40 working days.

Information Being Released

Please find enclosed the following documents:

Item	Date	Document Description	Decision
1.	14 November 2016	Email correspondence - macro earthquake advice	Release in part
2.	14 November 2016	Aide Memoire: Preliminary fiscal and economic assessment of the 14 November earthquake	Release in part
3.	15 November 2016	Email correspondence: Update on early advice for MoF on Earthquake impacts	Release in part
4.	17 November 2016	Aide Memoire: Business Support Package after the 14 November 2016 Earthquake	Release in full

5.	17 November 2016	Advice for MoF on Fiscal Impact of Kaikoura EQ	Release in part
6.	18 November 2016	Aide Memoire: Strategic Considerations in Responding to 14 November Earthquakes	Release in full
7.	18 November 2016	Treasury Report: Budget Allowances in the BPS	Release in part
8.	18 November 2016	Oral item for Cabinet - economic and fiscal impacts of Kaikoura EQ	Release in part
9.	18 November 2016	Aide Memoire: Update on the Half Year Economic and Fiscal Update and 2017 Budget Policy Statement	Release in part
10.	21 November 2016	Pre-Cab Briefing 21 November 2016	Release in part
11.	23 November 2016	Budget Policy Statement Cabinet Paper	Release in part
12.	28 November 2016	Pre-Cab Briefing 28 November 2016	Release in part
13.	29 November 2016	Aide Memoire: Treasury comments on the RBNZ Financial Stability Report November 2016	Release in part
14.	1 December 2016	Monthly Economic Indicators November 2016	Release in part. (Note attachments to report are publicly available.)
15.	2 December 2016	Aide Memoire: Advice on the Kaikoura Earthquake - reinstatement of South Island Corridors Cabinet paper	Release in part
16.	2 December 2016	Kaikoura earthquake – future decisions: prioritisation and sequencing	Release in part
17.	5 December 2016	Email correspondence on 'Aide Memoire: Advice on the Kaikoura Earthquake - reinstatement of South Island Corridors Cabinet paper'	Release in part
18.	9 December 2016	Oral item - Kaikoura Earthquake - Support for rehabilitating Kaikoura Harbour	Release in part
19.	12 December 2016	Pre-Cab Briefing 12 December 2016	Release in part
20.	12 December 2016	Kaikoura Harbour talking points for Cabinet and aide memoire table	Release in full
21.	20 December 2016	Treasury Report: EQC Risk Financing Framework	Release in part
22.	20 December 2016	Pre-Cab Briefing 20 December	Release in part
23.	20 December 2016	The Crown Guarantee - Suggested OIA	Release in part

		Redactions	
24.	21 December 2016	Budget 2017 - Initial Budget Initiatives and Business-as-usual Pressures	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,
- commercially sensitive information, under section 9(2)(b)(ii) – to protect the commercial position of the person who supplied the information, or who is the subject of the information,
- advice still under consideration, section 9(2)(f)(iv) – to maintain the current constitutional conventions protecting the confidentiality of advice tendered by Ministers and officials,
- names and contact details of junior officials and certain sensitive advice, under section 9(2)(g)(i) – to maintain the effective conduct of public affairs through the free and frank expression of opinions,
- advice subject to legal privilege, under section 9(2)(h) - to maintain legal professional privilege,
- commercially sensitive information, under section 9(2)(i) - to enable a Minister of the Crown or any department or organisation holding the information to carry out, without prejudice or disadvantage, commercial activities, and
- confidential information, under section 9(2)(j) – to enable the Crown to negotiate without disadvantage or prejudice.

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

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

Simon McLoughlin
 Manager, Earthquake Recovery Strategy

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OIA 20170004

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Not covered by your request

RELEASED UNDER THE
OFFICIAL INFORMATION ACT

From: Angela Mellish [TSY]

Sent: Monday, 14 November 2016 12:36 p.m.

To: Sam Tendeter <Sam.Tendeter@parliament.govt.nz>; Vicki Plater [TSY] <Vicki.Plater@treasury.govt.nz>; Daniel Cruden [TSY] <Daniel.Cruden@treasury.govt.nz>; Andrew Blazey [TSY] <Andrew.Blazey@treasury.govt.nz>; Fiona Whiteridge [TSY] <Fiona.Whiteridge@treasury.govt.nz>; Peter Gardiner [TSY] <Peter.Gardiner@treasury.govt.nz>; David Taylor [TSY] <David.Taylor@treasury.govt.nz>; Tim Ng [TSY] <tim.ng@treasury.govt.nz>; Kamlesh Patel [TSY] <Kamlesh.Patel@treasury.govt.nz>

Cc: Sam Direen [TSY] <sam.direen@treasury.govt.nz>; Renee Philip [TSY] <renee.philip@treasury.govt.nz>; Catherine Atkins [TSY] <Catherine.Atkins@treasury.govt.nz>; @Forecasting <Forecasting@treasury.govt.nz>
Subject: RE: Eq advice

And a few more points on resilience:

1. On economic resilience, the economy is currently growing strongly and so any negative short-term impacts arising from business disruption may not be noticed (not to deny that they might still occur). Business and consumer confidence have been buoyant; this contrasts with a situation in which activity might be weak and confidence low – the earthquake might affect activity more in such a situation. However, there could still be a negative impact on activity and confidence in the economy.
2. On the fiscal side, the government recorded a surplus (before gains and losses) in the June 2016 fiscal year and surpluses were projected to increase in coming years. Net debt stood at just less than 25% of GDP at 30 June 2016, giving the government room to increase debt if necessary to increase expenditure for repairs and recovery, and/or cover EQC-style insurance payments..
3. On recovery, resources may have to be redirected to a reconstruction effort given that capacity is already constrained in the construction industry. Planned infrastructure projects may have to be temporarily delayed so that resources can be directed towards reconstruction. However, since the extent of the damage is uncertain at this stage, this response is also uncertain.

Sent with Good Work (www.blackberry.com)

From: Angela Mellish [TSY] <Angela.Mellish@treasury.govt.nz>
Date: Monday, 14 Nov 2016, 12:32 PM
To: Sam Tendeter <Sam.Tendeter@parliament.govt.nz>, Vicki Plater [TSY] <Vicki.Plater@treasury.govt.nz>, Daniel Cruden [TSY] <Daniel.Cruden@treasury.govt.nz>, Andrew Blazey [TSY] <Andrew.Blazey@treasury.govt.nz>, Fiona Whiteridge [TSY] <Fiona.Whiteridge@treasury.govt.nz>, Peter Gardiner [TSY] <Peter.Gardiner@treasury.govt.nz>, David Taylor [TSY] <David.Taylor@treasury.govt.nz>, Tim Ng [TSY] <tim.ng@treasury.govt.nz>, Kamlesh Patel [TSY] <Kamlesh.Patel@treasury.govt.nz>
Cc: Sam Direen [TSY] <sam.direen@treasury.govt.nz>, Renee Philip [TSY] <renee.philip@treasury.govt.nz>, Catherine Atkins [TSY] <Catherine.Atkins@treasury.govt.nz>, @Forecasting <Forecasting@treasury.govt.nz>
Subject: RE: Eq advice

Hi all,

Here are some initial thoughts with respect to economic forecasts (we locked down final economic last week & were due to report to MoF later this week after we were to finalise tax forecasts tomorrow).

From Patrick:

At this stage I do not consider that we need to adjust our final HYEFU forecasts, for the following reasons:

1. The economic cost of the earthquake is uncertain at this stage until a full assessment of the extent of the damage is carried out. Likely impacts are increased infrastructure expenditure to repair roads, etc; and decreased tax revenue in the short term as a result of business disruption. The extent of the former is still uncertain, although there is significant damage to the roads on the Kaikoura coast. That could also cause disruption to business, eg transport of goods from Picton (North Island) to Christchurch and the rest of the south Island (and vice versa). There could also be disruption to business and to government in Wellington, depending on the extent of damage to infrastructure (eg port, roads) and to buildings (office blocks, etc). Any reduction in tax revenue as a result of business disruption is also uncertain at this stage.
2. At this stage, the impact does not seem to be as great as the second (Feb 2011) Chch earthquake which affected a densely populated area with a concentration of business activity. With the exception of Kaikoura, this earthquake does not seem to have had that effect so far. That is not to underestimate its impact on the regions that it has affected, and its social and personal impact in that region.
3. Another area of liability for the government to consider is arrangements under the Earthquake Commission. I don't know how the government sees those responsibilities currently, but I would expect that it would want to ensure that the same arrangements and guarantees would continue to apply as before. That would imply a liability to the Crown which may have to be shown in the HYEFU fiscal projections.
4. While the short-term economic and fiscal impact would be negative (reduced tax and increased expenditure), the medium and longer-term impact would be positive measured in terms of GDP. The repairs and rebuild would be included as economic activity, even though they would be replacing capital which had been destroyed or damaged. As in the case of Chch, there would be an insurance pay-out which would fund at least some of this increased expenditure (for the private sector, at least). Given the tight constraints in the construction industry, that increased activity could be inflationary. Resources may need to be redirected from other activities to rebuild/repair work. At the time of the Feb 2011 earthquake, The Reserve Bank reduced the Official Cash Rate by 50 basis points; this had the effect of supporting confidence. As the economic situation deteriorated later that year, the OCR reduction was left in place and not reversed. Natural disasters are generally considered to be inflationary as the subsequent repairs place additional demand on resources.

5. HOWEVER, with all of this I would emphasise the uncertainty of the extent of the damage and so the economic impact. We will continue to monitor developments and assess the situation.

Please let me know if you would like any additional information.

Cheers, Patrick

s9(2)(a)

Cheers
Angela

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From: Sam Tendeter <Sam.Tendeter@parliament.govt.nz>
Date: Monday, 14 Nov 2016, 11:44 AM
To: Vicki Plater [TSY] <Vicki.Plater@treasury.govt.nz>, Daniel Cruden [TSY] <Daniel.Cruden@treasury.govt.nz>, Andrew Blazey [TSY] <Andrew.Blazey@treasury.govt.nz>, Fiona Whiteridge [TSY] <Fiona.Whiteridge@treasury.govt.nz>, Angela Mellish [TSY] <Angela.Mellish@treasury.govt.nz>, Peter Gardiner [TSY] <Peter.Gardiner@treasury.govt.nz>, David Taylor [TSY] <David.Taylor@treasury.govt.nz>, Tim Ng [TSY] <tim.ng@treasury.govt.nz>, Kamlesh Patel [TSY] <Kamlesh.Patel@treasury.govt.nz>
Subject: RE: Eq advice

Thanks for this. Can I suggest somebody pulls this together into a lish page note for mof (just bullet point form fine), which also sets out what further information we will provide tomorrow and include something on how treasury is engaging on the issues. Appreciate there will be limited info at this stage on the impacts, but a couple of sentences setting out how/when that info will come through will be useful.

Would also be good to have the dollar number for nzta fund.

Sam

Sent with Good (www.good.com)

From: Vicki Plater [TSY]
 Sent: Monday, 14 November 2016 11:29:15 a.m.
 To: Sam Tendeter; Daniel Cruden [TSY]; Andrew Blazey [TSY]; Fiona Whiteridge [TSY]; Angela Mellish [TSY]; Peter Gardiner [TSY]; David Taylor [TSY]; Tim Ng [TSY]; Kamlesh Patel [TSY]
 Subject: RE: Eq advice

Hi Sam

Some things have gone through to Nick and Nicola this morning (I'll make sure you get copied in on anything like that from now). I'll forward those through to you.

At our recently-finished Crisis Mgmt team teleconference Gabs indicated that he thought we should take stock tomorrow morning on the economic and fiscal - incl with respect to the forecasts - but that we probably wouldn't have enough material today. Prob means only high-level comments today.

I'll forward you what's already been sent. If today is critical to get something more let us know.

Vicki

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IN-CONFIDENCE



Reference:

Date: 14 November 2016

To: Minister of Finance
(Hon Bill English)

Deadline: 4pm, Monday 14 November 2016

Aide Memoire: Preliminary fiscal and economic assessment of the 14 November earthquake

This Aide Memoire provides preliminary advice on the fiscal and economic impacts of the 7.5 magnitude earthquake that was centred in North Canterbury near Hanmer Springs today.

Given the limited information at hand, there is a large degree of uncertainty regarding the extent of damage, particularly to local infrastructure, which makes assessing the economic and fiscal costs difficult at this time. We will continue to monitor developments and begin a fuller assessment Tuesday morning.

The Treasury have near finalised its economic forecasts for HYEFU, and will finalise fiscal forecasts on 21 November. In light of events today, forecasts will be reviewed, and adjusted to account for the economic and fiscal consequences associated with the rebuild and recovery activities. Fiscal forecasts will accordingly be updated.

Key points include:

- **Magnitude of the economic impacts appears to be less:** Initial reports indicate that the size and extent of the damage is not as great as either Christchurch earthquakes in September 2010 or Feb 2011. Whilst more consistent with the first Christchurch earthquake in September 2010, the fact that it was centred in a less densely populated area of the country and during the night, the economic consequences are likely to be lower.
- **Economic Resilience remains:** The New Zealand economy has relatively strong momentum, business and consumer confidence. With relatively low public debt, and a strong surplus there is fiscal headroom to support the rebuild and recovery. And there is space for further monetary policy easing if required.

IN-CONFIDENCE**Economic and Fiscal Assessment**

Due to the location and timing of today's earthquake, the economic and fiscal impacts are likely to be lower than previous earthquakes in Christchurch in September 2010 and February 2011, which affected a densely populated area with a concentration of business activity. Several rural townships, including Kaikoura, have reportedly suffered extensive damage, with limited impact in major centres. That is not to underestimate its impact on the regions that it has affected, and its social and personal impact in that region.

Today's earthquake was centred in the upper South Island, with damage to areas including Canterbury and Wellington. The areas most affected by today's earthquake: the upper South Island, including Tasman, Nelson, Marlborough regions, and the West Coast make up 3.5% of New Zealand's economy, or \$8.3 billion in regional gross domestic product. By comparison, Canterbury's GDP was \$33 billion, or 13.6%, and Wellington \$32 billion.¹

The most significant impacts are likely to be increased infrastructure expenditure to repair roads and other utilities infrastructure; and decreased tax revenue in the short term as a result of business disruption. The extent of the former is still uncertain, although there is significant damage to the roads on the Kaikoura coast, and to port facilities in Picton and Wellington. That could also cause disruption to business, eg transport of goods from Picton (North Island) to Christchurch and the rest of the south Island (and vice versa).

There could also be disruption to business and to government in Wellington, depending on the extent of damage to infrastructure (eg port, roads) and to buildings (office blocks, etc). Any reduction in tax revenue as a result of business disruption is also uncertain.

While the short-term economic and fiscal impact would be negative (reduced tax and increased expenditure), the medium and longer-term impact would be positive measured in terms of GDP. The repairs and rebuild would be included as economic activity, even though they would be replacing capital which had been destroyed or damaged.

As in the case of the Christchurch earthquakes, there would be an insurance pay-out, which would fund at least some of this increased expenditure (for the private sector, at least). Given the tight constraints in the construction industry could be inflationary.

Resources may need to be redirected from other activities to rebuild/repair work. At the time of the Feb 2011 earthquake, The Reserve Bank reduced the Official Cash Rate by 50 basis points; this had the effect of supporting confidence. As the economic situation deteriorated later that year, the OCR reduction was left in place and not reversed. Natural disasters are generally considered to be inflationary as the subsequent repairs place additional demand on resources.

The earthquake occurred when financial markets were closed. When they did open, financial markets responded cautiously to the news of today's earthquake. The New Zealand dollar recovered after falling in early trading. The ANZ reported that markets are to trade cautiously until a greater clarity of the earthquake damage emerges.

¹ Based on Stats NZ regional GDP statistics, 2015.

IN-CONFIDENCE**The NZ economy remains resilient**

On economic resilience, the economy is currently growing strongly and so any negative short-term macro impacts arising from business disruption may not be material (not to deny that they might still occur). Business and consumer confidence have been buoyant; this contrasts with a situation in which activity might be weak and confidence low – the earthquake might affect activity more in such a situation. However, there could still be a negative impact on activity and confidence in the economy.

1. On the fiscal side, the government recorded a surplus (before gains and losses) in the June 2016 fiscal year and surpluses were projected to increase in coming years. Net debt stood at just less than 25% of GDP at 30 June 2016, giving the government room to increase debt if necessary to increase expenditure for repairs and recovery, and/or cover EQC-style insurance payments..
2. On recovery, resources may have to be redirected to a reconstruction effort given that capacity is already constrained in the construction industry. Planned infrastructure projects may have to be temporarily delayed so that resources can be directed towards reconstruction. However, since the extent of the damage is uncertain at this stage, this response is also uncertain.
3. Regarding Monetary policy, despite recent reductions in the OCR, the latest being a 25 basis point cut to 1.75 basis points last Thursday, there remains policy space to undertake further reductions to the OCR if required. In the days following the second Christchurch earthquake, the Reserve Bank lowered the official cash rate by 50 basis points.

Other information includes:

- The National Land Transport Fund has funds put aside for emergency works.
- There is provision under the Public Finance Act for the Government to approve expenditure in an emergency, if an emergency is declared under the Civil Defence Act and Civil Defence Emergency Management Act.
- Local councils will also have their own insurance.

The published 2015/18 National Land Transport Programme (NLTP) provided \$154m for response to emergency events on State highways and a further \$268m for similar works on local roads. The provision for local roads had been increased to accommodate ongoing rebuilding of the roads in Christchurch and the significant damage to the roading network in Whanganui/Taranaki following the June 2015 storm event.

s9(2)(i)

Page 4 withheld under s9(2)(i)

From: Tony Burton [TSY]
Sent: Tuesday, 15 November 2016 11:48:30 AM
To: Sam Tendeter
Cc: Sam Direen [TSY];Angela Mellish [TSY];Renee Philip [TSY];Catherine Atkins [TSY];@Forecasting;Vicki Plater [TSY];Daniel Cruden [TSY];Andrew Blazey [TSY];Fiona Whiteridge [TSY];David Taylor [TSY];Kamlesh Patel [TSY];Mark Blackmore [DPMC];Tim Ng [TSY];Peter Gardiner [TSY];@ELT (Executive Leadership Team) [TSY]
Subject: RE: Updat on advice for MoF

Sam

A little more back ground detail from Patrick. (Someone is sorting out the RB phone issues for us):

The economic impacts are most likely to be in the following areas: business disruption in terms of transport, travel and tourism, especially in the Kaikoura and Hanmer area; repairs and reconstruction of infrastructure (a cost to the government, but a boost to economic activity); private sector repairs and reconstruction (this should be largely paid for from insurance payments, but will also include claims on the government via EQC).

The fiscal impacts are likely to include: immediate costs in terms of rescue, clean-up and social assistance; possible assistance for businesses directly affected by the earthquakes; some drop in tax revenue as a result of business disruption; the cost to the government of repairs and reconstruction of infrastructure (as above); subsequently increased tax revenue from any increase in activity (above what would have been the case) as a result of private sector rebuilding and reconstruction; insurance claims against the government via EQC.

The other main economic impact to consider is the ability of the economy to respond to additional demand. In general, the economy is considered to be operating close to its potential level of output (unemployment is just below 5%, capacity utilisation is high) and the construction industry in particular is operating at a high level of capacity utilisation (residential activity is growing rapidly, there are a number of large infrastructure projects underway or planned, wage growth in the industry is higher than in other sectors, and recent business talks revealed capacity constraints in the industry affecting labour and materials as well as infrastructure bottlenecks, eg supply chains, etc).

These factors suggest that any additional construction activity would be in place of planned projects; new government spending in response to the earthquakes may have to be in place of other government construction activity already planned (ie, reprioritisation of spending) OR in place of private sector work (ie, displacement of economic activity). The alternative would be increased capacity constraints in the construction industry, leading to higher inflation (ie higher costs of projects and higher inflation in the economy as a whole). While inflation is currently low (although it is expected to pick up to 1% apc in the December quarter), non-tradables inflation is being balanced by negative tradables inflation and inflation pressures in the economy are expected to increase as capacity constraints increase across the economy as a whole. Notwithstanding those considerations regarding inflation, the more important issue is the ability of the construction industry to undertake the additional work without reprioritisation and/or displacement of work. That suggests that any additional demand would be offset to some degree by reduced output in other areas, leaving total output (ie GDP growth) only slightly

higher. However, it is impossible to know the extent of that impact at this stage without knowing the full extent of the damage and the size of the repair and reconstruction work required.

Other possible economic impacts include ongoing reduced tourism spending in the region affected (although offset to some degree by redirection of spending to other regions, eg Nelson, Marlborough, West Coast). There may also be impacts on the balance of payments, eg higher imports of construction materials and reduced services exports (tourism).

At this stage it is not possible to quantify the impact of the earthquakes on the economy and fiscal position and projections. We should be able to give some estimate of the impact when more information on the extent of the damage and likely cost of repairs comes to hand.

Tony Burton | Chief Economic Advisor (Acting) | **The Treasury**

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From: Tony Burton [TSY]

Sent: Tuesday, 15 November 2016 11:27 a.m.

To: 'Sam Tendeter' <Sam.Tendeter@parliament.govt.nz>

Cc: Sam Direen [TSY] <sam.direen@treasury.govt.nz>; Angela Mellish [TSY] <Angela.Mellish@treasury.govt.nz>; Renee Philip [TSY] <renee.philip@treasury.govt.nz>; Catherine Atkins [TSY] <Catherine.Atkins@treasury.govt.nz>; @Forecasting <Forecasting@treasury.govt.nz>; Vicki Plater [TSY] <Vicki.Plater@treasury.govt.nz>; Daniel Cruden [TSY] <Daniel.Cruden@treasury.govt.nz>; Andrew Blazey [TSY] <Andrew.Blazey@treasury.govt.nz>; Fiona Whiteridge [TSY] <Fiona.Whiteridge@treasury.govt.nz>; David Taylor [TSY] <David.Taylor@treasury.govt.nz>; Kamlesh Patel [TSY] <Kamlesh.Patel@treasury.govt.nz>; Mark Blackmore [DPMC] <Mark.Blackmore@dpmc.govt.nz>; Tim Ng [TSY] <tim.ng@treasury.govt.nz>; Peter Gardiner [TSY] <Peter.Gardiner@treasury.govt.nz>; @ELT (Executive Leadership Team) [TSY] <ELTExecutiveLeadershipTeam@treasury.govt.nz>

Subject: Update on advice for MoF

Sam

Update from Peter's aide memoire:

- The economy is in generally good shape and the reaction of the markets suggests national and international confidence in the NZ economy remains high.
- We have comfortably enough liquidity to deal with immediate costs and since there is no evidence of adverse market reaction, this is likely to continue as the response develops.

- There is no clear picture of the overall costs, nor of what would materially change our forecasts. There is work going on in the Ministry of Transport and MBIE on the costs and we will be linking in with that work. To address this we propose:
 - o Delay the HYEPU (and therefore probably the Budget Policy Statement release) by a week, so provisionally release on 15 December. This gives us the space to provide a better estimate of the costs and potential economic impacts.
 - o We will provide an update on Friday this week (18th November) that will include an alternative timetable for HYEPU if the release date was pushed out.
- There are some issues with statistics releases:
 - o On the current timetable the delayed HYEPU would be released on the same day as September quarter GDP.
 - o However damage to Statistics New Zealand's Wellington building means there will be delays in data releases, including first tier economic statistics. They will update us later today on the revised timetable.
- Treasury will be setting up a team to manage its response to the earthquake similar to the team managed by Tom Hall that ran our response to the Christchurch earthquakes.

Ring me on s9(2)(a) if you want to discuss,

Tony

Tony Burton | Chief Economic Advisor (Acting) | **The Treasury**
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From: Sam Tendeter [<mailto:Sam.Tendeter@parliament.govt.nz>]
Sent: Tuesday, 15 November 2016 8:43 a.m.
To: Peter Gardiner [TSY] <Peter.Gardiner@treasury.govt.nz>; Mark Blackmore [DPMC] <Mark.Blackmore@dpmc.govt.nz>
Cc: Sam Direen [TSY] <sam.direen@treasury.govt.nz>; Angela Mellish [TSY] <Angela.Mellish@treasury.govt.nz>; Renee Philip [TSY] <renee.philip@treasury.govt.nz>; Catherine Atkins [TSY] <Catherine.Atkins@treasury.govt.nz>; @Forecasting <Forecasting@treasury.govt.nz>; Vicki Plater [TSY] <Vicki.Plater@treasury.govt.nz>; Daniel Cruden [TSY] <Daniel.Cruden@treasury.govt.nz>; Andrew Blazey [TSY] <Andrew.Blazey@treasury.govt.nz>; Fiona Whiteridge [TSY] <Fiona.Whiteridge@treasury.govt.nz>; David Taylor [TSY] <David.Taylor@treasury.govt.nz>; Tim Ng [TSY] <tim.ng@treasury.govt.nz>; Kamlesh Patel [TSY] <Kamlesh.Patel@treasury.govt.nz>
Subject: RE: Eq advice

Hi Peter, all

Thanks again for pulling this together in short order yesterday.

It would be helpful to have an updated state of play on the economic and fiscals by 11.30am.

I am conscious that the PM spoke about the potential scale of the costs yesterday evening.

Sam

Sam Tendeter | Economic Advisor
Office of Hon Bill English | Deputy Prime Minister, Minister of Finance
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From: Peter Gardiner [TSY] [<mailto:Peter.Gardiner@treasury.govt.nz>]
Sent: Monday, 14 November 2016 3:17 p.m.
To: Sam Tendeter; Mark Blackmore [DPMC]
Cc: Sam Direen [TSY]; Angela Mellish [TSY]; Renee Philip [TSY]; Catherine Atkins [TSY]; @Forecasting; Vicki Plater [TSY]; Daniel Cruden [TSY]; Andrew Blazey [TSY]; Fiona Whiteridge [TSY]; David Taylor [TSY]; Tim Ng [TSY]; Kamlesh Patel [TSY]
Subject: RE: Eq advice

[IN-CONFIDENCE]

Sam et al

Attached is a summary that draws together various e-mails – a good amount from Patrick. I will update if additional information comes to hand.

Please circulate as needed

Give me a call if you want to discuss, regards

Peter Gardiner | Manager | The Treasury

Tel: +64 4 917 6902 | [s9\(2\)\(a\)](mailto:s9(2)(a)@treasury.govt.nz) | Peter.Gardiner@treasury.govt.nz

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From: Angela Mellish [TSY]
Sent: Monday, 14 November 2016 12:33 p.m.
To: Sam Tendeter <Sam.Tendeter@parliament.govt.nz>; Vicki Plater [TSY] <Vicki.Plater@treasury.govt.nz>; Daniel Cruden [TSY] <Daniel.Cruden@treasury.govt.nz>; Andrew Blazey [TSY] <Andrew.Blazey@treasury.govt.nz>; Fiona Whiteridge [TSY] <Fiona.Whiteridge@treasury.govt.nz>; Peter Gardiner [TSY] <Peter.Gardiner@treasury.govt.nz>; David Taylor [TSY] <David.Taylor@treasury.govt.nz>; Tim Ng [TSY] <tim.ng@treasury.govt.nz>; Kamlesh Patel [TSY] <Kamlesh.Patel@treasury.govt.nz>
Cc: Sam Direen [TSY] <sam.direen@treasury.govt.nz>; Renee Philip [TSY] <renee.philip@treasury.govt.nz>; Catherine Atkins [TSY] <Catherine.Atkins@treasury.govt.nz>; @Forecasting <Forecasting@treasury.govt.nz>
Subject: RE: Eq advice

Hi all,

Here are some initial thoughts with respect to economic forecasts (we locked down final economic last week & were due to report to MoF later this week after we were to finalise tax forecasts tomorrow).

From Patrick:

At this stage I do not consider that we need to adjust our final HYEFU forecasts, for the following reasons:

1. The economic cost of the earthquake is uncertain at this stage until a full assessment of the extent of the damage is carried out. Likely impacts are increased infrastructure expenditure to repair roads, etc; and decreased tax revenue in the short term as a result of business disruption. The extent of the former is still uncertain, although there is significant damage to the roads on the Kaikoura coast. That could also cause disruption to business, eg transport of goods from Picton (North Island) to Christchurch and the rest of the south Island (and vice versa). There could also be disruption to business and to government in Wellington, depending on the extent of damage to infrastructure (eg port, roads) and to buildings (office blocks, etc). Any reduction in tax revenue as a result of business disruption is also uncertain at this stage.
2. At this stage, the impact does not seem to be as great as the second (Feb 2011) Chch earthquake which affected a densely populated area with a concentration of business activity. With the exception of Kaikoura, this earthquake does not seem to have had that effect so far. That is not to

- underestimate its impact on the regions that it has affected, and its social and personal impact in that region.
3. Another area of liability for the government to consider is arrangements under the Earthquake Commission. I don't know how the government sees those responsibilities currently, but I would expect that it would want to ensure that the same arrangements and guarantees would continue to apply as before. That would imply a liability to the Crown which may have to be shown in the HYEFU fiscal projections.
 4. While the short-term economic and fiscal impact would be negative (reduced tax and increased expenditure), the medium and longer-term impact would be positive measured in terms of GDP. The repairs and rebuild would be included as economic activity, even though they would be replacing capital which had been destroyed or damaged. As in the case of Chch, there would be an insurance pay-out which would fund at least some of this increased expenditure (for the private sector, at least). Given the tight constraints in the construction industry, that increased activity could be inflationary. Resources may need to be redirected from other activities to rebuild/repair work. At the time of the Feb 2011 earthquake, The Reserve Bank reduced the Official Cash Rate by 50 basis points; this had the effect of supporting confidence. As the economic situation deteriorated later that year, the OCR reduction was left in place and not reversed. Natural disasters are generally considered to be inflationary as the subsequent repairs place additional demand on resources.
 5. HOWEVER, with all of this I would emphasise the uncertainty of the extent of the damage and so the economic impact. We will continue to monitor developments and assess the situation.

Please let me know if you would like any additional information.

Cheers, Patrick

s9(2)(a)

Cheers
Angela

Sent with Good Work (www.blackberry.com)

Not covered by your request

Not covered by your request

From: Vicki Plater [TSY]
Sent: Monday, 14 November 2016 11:29:15 a.m.
To: Sam Tendeter; Daniel Cruden [TSY]; Andrew Blazey [TSY]; Fiona Whiteridge [TSY]; Angela Mellish [TSY]; Peter Gardiner [TSY]; David Taylor [TSY]; Tim Ng [TSY]; Kamlesh Patel [TSY]
Subject: RE: Eq advice

Hi Sam

Some things have gone through to Nick and Nicola this morning (I'll make sure you get copied in on anything like that from now). I'll forward those through to you.

At our recently-finished Crisis Mgmt team teleconference Gabs indicated that he thought we should take stock tomorrow morning on the economic and fiscal - incl with respect to the forecasts - but that we probably wouldn't have enough material today. Prob means only high-level comments today.

I'll forward you what's already been sent. If today is critical to get something more let us know.

Vicki

Sent with Good Work (www.blackberry.com)

Not covered by your request

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Reference: T2016/2226 DH-3

Date: 17 November 2016

To: Minister of Finance (Hon Bill English)
Associate Minister of Finance (Hon Steven Joyce)

Deadline: None
(if any)

Aide Memoire: Business Support Package after the 14 November 2016 Earthquake

A small group of Cabinet Ministers¹ will shortly consider a business support package for employers and employees affected by the 14 November Kaikoura earthquake. The proposed package is similar to that which was implemented following the 2011 Christchurch earthquake and will include an *Employee Support Subsidy* and *Earthquake Job Loss Cover* and is in addition to the existing suite of hardship support available.

Overall Treasury supports the proposed package and recommendations in the paper to provide short-term relief to businesses affected by the earthquake and support the principles for intervention set out in paragraph 16 of the Cabinet paper.

The two substantive parts of the proposed package are:

1. **Earthquake Support Subsidy:** This subsidy is similar to the subsidy introduced following the September 2010 and February 2011 Canterbury earthquakes. The subsidy is aimed at assisting eligible employers in paying their employees who are unable to work because their employers are unable to operate because of the earthquake.
 - The subsidy will be paid to the employer in a lump sum, on behalf of the employee, at \$500 gross per full time employee, per week and \$300 gross per week per part-time employee.
 - The subsidy will be available as soon as feasible and payments may be made retrospectively to include the period from Monday 14 November 2016.

¹ The Prime Minister has authorised a group of Ministers to have Power to Act to take any urgent Cabinet level decisions on the government's response to the earthquake. The group comprises the Prime Minister, Minister of Finance, Acting Minister of Civil Defence, and the Minister of Economic Development, in consultation with relevant portfolio Ministers.

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2. **Earthquake Job Loss Cover:** This part of the package is designed to support employees when the employer / employee relationship cannot be maintained. If an employee cannot continue to work for their employer and receive a wage or salary, it will allow them time to adjust to the change in their financial circumstances.
- The programme will pay \$500 net per week to employees who have lost their income. It is proposed that part-time employees receive the full rate of subsidy or payment for the initial four weeks the programme is available as it is not possible to verify the status of part-time employees through Inland Revenue.

The Treasury acknowledges that, at this early stage the duration and cost of the proposed business support package is uncertain but consider these estimates are based on sound assumptions, and that higher end costs are reasonable and appropriate given the nature of the situation.

Considerations around support subsidies

This subsidies above are based on the assistance package implemented in the Canterbury region after the 2011 Christchurch earthquake. There are two important differences to note in the affected area of the 14 November earthquake compared to Christchurch.

First, more of the local employment in the Kaikoura area is focused on tourism and primary sectors. As a result, it is likely that more of the local labour market will be relatively seasonal/transient compared to Christchurch. In these instances, the need to help keep people attached to their workplace, and remain in the local area until business resumes, is less significant and any support subsidies should instead be focused on those resident in the local area. The flexibility to shed such seasonal workers will also be an important mechanism for local businesses to cut costs in face of temporary drop in demand (e.g. from lower tourist numbers)

Second, given the relative 'localised' nature of the earthquakes, it is possible that some suppliers to the affected districts will not be locally-based and may therefore fall outside of the region eligible for support subsidies while still experiencing a loss of custom or increased expense involved in alternative routes (although they will have a greater ability to adjust than those in the affected area). These impacts would likely not be visible immediately but, should they eventuate, may need to be considered as part of any ongoing business assistance.

Given the need to implement an assistance package quickly and simply, **Treasury supports the subsidies as currently proposed** as the package will provide the necessary relief to employers and employees in the near term. However we suggest that the issues noted above are revisited prior to any extension of the proposed subsidies.

Michael Chatterley, Analyst, Economic Performance & Strategy, 04 917 6030
Matthew Gilbert, Manager - Economic Performance & Strategy, 04 917 6048

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Note on Kaikoura Earthquakes for Fiscal Issues

17 November, 2016

Provisional judgement on overall costs

Our estimate of the overall costs is:

- If we plan to integrate our response with other investment priorities, particularly transport, then our estimate is between **\$1bn and \$3bn**
- If we fund to rebuild as it was, that means replacing low value assets and our estimate is between **\$3bn and \$5bn**

A full table of known costs is provided as an annex, but note:

- We are waiting for detailed information from Ministry of Transport and Kiwirail.
- The experience of Christchurch suggests transition and other unknown costs are likely to push up initial estimates
- Seismological advice is there will probably be further significant earthquakes
- s9(2)(i)



Funding options for direct costs

Our assessment of the wider economic impacts of additional direct costs is:

Table 1: Economic impact of increased fiscal spending

	Net increase in fiscal spending (p.a.)		
	<\$1 billion	\$1-\$3 billion	>\$3 billion
Economic size	Less than 0.5% of GDP	Around 1% of GDP (\$250 billion)	More than 1% of GDP
Impact on GDP / inflation	negligible	marginal	may be material

Note: A material impact has an impact on measured GDP and/or inflation.

Treasury advice is that likely operating costs could be managed within operating allowances. However, it is likely to be more of a challenge to manage capital spending within existing capital allowances. **Thus our advice is that funding of the earthquake response should combine re-prioritised capital spending and increased capital allowances (resulting in higher net debt):**

- Not covered by your request
- Additional borrowing of up to \$3bn will have little economic impact and would keep debt within the current target of around 20%

IN-CONFIDENCE**HYEFU – Decisions that need to be made**

To complete the fiscal forecasts a **decision** is required on **settings for future Budget capital allowances**. We will send a Treasury Report on 18 November seeking Finance Ministers agreement on settings, for approval by Cabinet on 28 November.

Capital allowances will need increase, but there is a choice whether they go up now or at budget. At this stage, with limited information around expected cost estimates we recommend signalling the possibility to increase allowances to fund earthquake cost in the BPS.

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Reference: T2016/2254

File No. MS-1

Date: 18 November 2016

To: Minister of Finance
(Hon Bill English)

Deadline: none

Aide Memoire: Strategic Considerations in Responding to 14 November Earthquakes

This note provides high-level advice on responses to manage the economic and fiscal impacts of the 14 November 2016 earthquakes, drawing on experience gained from the Canterbury earthquakes.

We note four points in particular:

- Initial estimates of the economic and fiscal impact are likely to be conservative. Other (worse) scenarios should also be borne in mind in considering the Government's response;
- The Government's response in Kaikōura and the surrounding area will set a precedent for expected responses to other local natural disasters. That means the response from the outset will need to be well-grounded in sound principles for Government support;
- In terms of the wider recovery, decisions taken early in the piece (for example, around reinstating national infrastructure) are likely to have significant long-run implications, and so need to be taken with those opportunities and long-run strategy in mind;
- And looking beyond this event in itself, the Kaikōura earthquake signals again the benefit of sound policies and institutions to support resilience in the New Zealand economy.

Conservatism in initial estimates of economic and fiscal impact

The scale of the economic and fiscal impacts is uncertain, and will remain so for some time. Early and tentative indications suggest the total (gross) fiscal cost could be in the range of \$2.0 billion to \$3.0 billion (if infrastructure was to be reinstated much the same as was before). (T2016/2232 refers).

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The experience from the Canterbury earthquakes would suggest the balance of risk around this figure is that the estimates are more likely to be revised up than down as more information comes to hand. There is a strong possibility of further damage from further aftershocks. And deliberate policy decisions by the Government may well add to the cost. On the other hand, decisions on the future shape of infrastructure may moderate that cost (see below).

In terms of economic impact, the initial indications are that the overall nationwide economic impact from disruption is likely to be fairly minor. Experience from the Canterbury earthquakes would also illustrate the underlying adaptability and resilience of New Zealanders and the New Zealand economy. That said, there is a lot of uncertainty about the likely duration of disruption to transport infrastructure (road, rail, ports), and its impact on supply chains.

The implication of this is that the scale of economic and fiscal impacts may well prove to be larger than initial estimates would suggest. Accordingly, scenarios where the final costs are higher (and potentially, quite a lot higher) should be borne in mind when considering your response to the earthquakes.

Precedent and principles

The context in the Kaikōura earthquakes is different from that of the Canterbury earthquakes, and that has a bearing on the Government's stance in responding to the earthquakes. The Canterbury earthquakes were characterised by widespread damage to commercial and residential property and local infrastructure in a major urban area, directly affecting hundreds of thousands of people. By comparison, the direct impact for Kaikōura and surrounding areas, while hugely significant for the people involved, is different both in scale and kind – the key economic and fiscal impact from the Kaikōura earthquakes is less about the impact to Kaikōura, and more about the damage to national infrastructure (road, rail, ports). That means that the responses adopted in the Canterbury events will not necessarily be appropriate for the Kaikōura event.

Further, the Government's stance in response and recovery support in Kaikōura will set the scene for disaster response in small communities in the future. There is something of a dilemma here: given the limited national significance, it would be reasonable to rely more on local authorities in the recovery; however, being a small community, the local authorities are likely to lack the resources and capability to support local recovery, and that is likely to put central government more in the spotlight.

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In terms of assistance to business and the community, the principles developed as a part of the Canterbury recovery¹ are useful touchstones:

- An assistance package must reflect the need for specific and tailored solutions that will best meet the needs of affected businesses. It also needs to satisfy some key principles for business recovery measures and where possible be driven by the business community.
- Any action should:
 - be timely (provide assistance when it is needed)
 - be time limited (taking into account that recovery will take some time)
 - be targeted (address a clearly defined problem, have clear parameters for use, and be capped). Local involvement is also critical for success
 - minimise transaction costs for businesses
 - be proportional to the magnitude of the effects, including the cumulative impact of prolonged stress on businesses and their owners and employees
 - make the best use of private sector resources, information and professional advice and local/regional resources, and
 - not displace or detract from private and voluntary effort and resources directed at business recovery.

Ministers have already drawn on these in developing the support package announced on Thursday 17 November 2016. It will be important to ensure that any consideration of future assistance continues to be anchored in these principles.

There are conventions and practice around cost-sharing with local government in disaster response – in essence a 60-40 split between local and central government. This convention may well come under pressure in the context of small local authorities (like Kaikōura and Hurunui) facing large infrastructure bills, and decisions taken here are an opportunity to reset expectations around cost-sharing for local authorities going forward.

Strategic implications of early decisions

One lesson from Canterbury is that decisions taken early on have the most impact. These are essentially strategic judgments that set the scene for how the recovery unfolds, and either allow or close off options later. And given strong path dependence and precedence, actions at the start end up having a big impact. But that also meant that they were often done at pace, and under a high level of uncertainty.

With the Kaikōura earthquakes, there are a number of issues that will need early attention that will have long-run implications, and may be an opportunity to progress broader strategies.

¹ Paper to Adhoc Cabinet Committee on Canterbury Earthquake Recovery, 'Christchurch earthquake: short to medium term business support measures'. 2011.

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The most important of these is around infrastructure. Care will be needed to ensure that the desire for early action to restore national infrastructure doesn't mean that the opportunity to develop a more resilient, more integrated and more efficient transport network is lost. This includes consideration of the future shape of the highway network, rail network (indeed the future of KiwiRail), and ports.

There are also likely to be issues around land use and zoning that will come up. These too will need to be considered in light of their long-run implications (e.g., suitability given rising sea-levels).

The interactions with local authorities will also raise issues of local authority capability and competence, and questions about amalgamation.

Wider implications

The Kaikōura earthquakes also point to some wider issues that may need attention at some point. These are around the policy and institutions to manage risk and support resilience in the New Zealand economy. These include:

- building regulation: The performance of several commercial buildings in Wellington CBD raises further questions about the robustness of the building regulatory system.
- pricing of risk, and well-functioning insurance markets: the earthquakes are likely to lead to some reassessment of risk in New Zealand markets, and reinforce the importance of seeing insurance as a systemic issue.
- more indirectly, the fact of a further major earthquake, and ongoing seismic instability, may add to perceptions of risk in New Zealand. As a result, the Government's performance in responding to this earthquake will likely matter more than otherwise in shaping perceptions of New Zealand as a place to visit, live, work and invest.

Simon McLoughlin, Manager, Economic Performance & Strategy, 917 6011

BUDGET-SENSITIVE**Treasury Report: Budget Allowances in the BPS**

Date:	18 November 2016	Report No:	T2016/2220
		File Number:	BM-2-9-3-2017

Action Sought

	Action Sought	Deadline
Minister of Finance (Hon Bill English)	Agree capital allowances for inclusion in the HYEPU forecasts	Monday 21 November
Associate Minister of Finance (Hon Steven Joyce)	Agree capital allowances for inclusion in the HYEPU forecasts	Monday 21 November
Associate Minister of Finance (Hon Paula Bennett)	Agree capital allowances for inclusion in the HYEPU forecasts	Monday 21 November

Contact for Telephone Discussion (if required)

Name	Position	Telephone	1st Contact
Ben Udy	Analyst, Macroeconomic & Fiscal Policy	+64 4 890 7428 (wk)	s9(2)(a) ✓
Renee Philip	Manager, Macroeconomic & Fiscal Policy	+64 4 917 6046 (wk)	

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

Return the signed report to Treasury.

Note any feedback on the quality of the report

Enclosure: No

BUDGET-SENSITIVE**Treasury Report: Budget Allowances in the BPS**

Executive Summary

Not covered by your request

The proposed budget allowances for the HYEPU were determined before the recent Kaikoura earthquakes. The cost of the earthquakes is still very uncertain. It is likely that some of the cost will be treated as fiscally neutral (e.g. a loan to EQC or investments covered by insurance proceeds). You may also want to consider whether other initiatives can be deferred or scaled to make room for earthquake expenditure, as part of the budget process.

To the extent that expenditure associated with the earthquakes cannot be managed within budget allowances, these allowances may need to be further increased in the Budget 2017 process. You may wish to signal in the Budget Policy Statement that if costs of the earthquake are unable to be met within these allowances, an increase may be required at Budget 2017.

The Government's commitment to prudent fiscal management has meant that the fiscal position is well placed to cope with shocks such as this, as net debt is at relatively low levels and forecast to decline. On current forecasts, there is some fiscal headroom to increase allowances while still remaining consistent with the target to reduce net debt to around 20% of GDP by 2020.

Final decisions on capital allowances and the draft Budget Policy Statement will be considered by Cabinet on Monday 28 November. If there are any further changes to allowances, these will not be incorporated into the Treasury's HYEPU forecasts.

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Recommended Action

We recommend that you:

Not covered by your request



h **note** that the Treasury's previous fiscal policy advice (T2016/2045 refers) did not consider the impact of the recent Kaikoura earthquakes on the economic or fiscal outlook;

i **note** that to the extent that earthquake expenditure cannot be managed within current allowances, Budget allowances may need to be further increased in the Budget 2017 process;

j Not covered by your request

k



BUDGET-SENSITIVE

I Not covered by your request

Renee Philip
Manager, Macroeconomic & Fiscal Policy

Hon Bill English
Minister of Finance

Hon Steven Joyce
Associate Minister of Finance

Hon Paula Bennett
Associate Minister of Finance

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Treasury Report: Budget Allowances in the BPS

Not covered by your request

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BUDGET-SENSITIVEImplications for Budget 2017

Not covered by your request

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Kaikoura Earthquake

12. On 14 November 2016 New Zealand was struck by a M7.8 earthquake centered near Kaikoura. The largest impacts of the earthquake were in the Kaikoura region, however, a number of other regions across New Zealand were also impacted. You have been provided with an initial estimate of the costs, although these estimates will change as new information comes to hand. The fiscal forecasts presented in the HYEPU will make an adjustment for the fiscal impact of the earthquake based on reasonable estimates available to us at present.

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13. The proposed budget allowances for the HYEPU were determined before the earthquake occurred. Ideally, any additional costs of the earthquake would be managed against Budget allowances (although some costs such as the loan to EQC would typically be treated as fiscally neutral for the purposes of the budget allowance). However, as indicated above, meeting the operating and capital allowances was already likely to require careful management and prioritisation.

14. Not covered by your request

15. If the expenditure relating to the earthquakes is larger than can be managed within allowances, you could consider a further increase to capital allowances. Given the current level of uncertainty around the costs of the Kaikoura earthquake and the funding mechanism e.g. insurance proceeds, the Treasury recommends Ministers do not increase Budget allowances (over and above the proposals discussed earlier) for the HYEPU. Instead, Ministers should signal in the Budget Policy Statement that if expenditure relating to the earthquake is unable to be met within existing resources and budget allowances, further increases may be required.

16. The focus on responsible financial management means the Government can afford to respond to economic or fiscal shocks such as this. As noted in previous advice (T2016/2045 refers), the Government currently has some scope to increase allowances if required while remaining consistent with its intention to reduce net debt to around 20% of GDP by 2020.

Not covered by your request

Oral item for Cabinet – economic and fiscal impacts of the Kaikoura Earthquakes: initial view

18 November 2016

- On 14 November, New Zealand was struck by a M7.8 earthquake near Kaikoura.
- Due to the location and timing of this earthquake, the economic and fiscal impacts are expected to be lower than the Christchurch earthquakes, which affected a more densely populated area with a larger concentration of business activity. The earthquake occurred at 12:02 am and so most people were at home and not at work. However, the recent earthquakes have also affected some Wellington buildings.
- The New Zealand economy is resilient. The economy is expected to grow strongly at nearly 3 per cent a year, on average, over the next five years. It continues to be supported by high levels of construction activity, exports (particularly tourism), a growing population and low interest rates.
- The Government's fiscal position is also strong, particularly compared to other countries. The operating balance has returned to surplus and net debt has started to reduce relative to GDP, although debt is still higher than we would like it to be. This provides us with some room to respond to emerging events without undermining our overarching fiscal strategy.
- The Kaikoura earthquakes caused a significant amount of damage and will affect economic activity in the region considerably. The Government will support the repairs and recovery where it is needed. However, the Treasury's view is that this won't disrupt the overall momentum of the economy, which is resilient and reflected in broad-based consumer and business confidence.
- The fiscal impact, however, is likely to be larger. The Treasury's initial estimates (based on information from agencies) suggest overall fiscal costs to the government¹ of around \$2.0 – \$3.0 billion, primarily for repairs to the state highway network, local roading, rail network, and EQC costs for residential property owners facing damage as a result of the earthquakes.
- This is still an early estimate, and it is unclear the extent to which this will be covered by insurance, reprioritising other spending, utilising existing contingencies and allowances, or reducing debt repayment.

s9(2)(i)

¹ Overall fiscal costs to the government represent gross costs related to recovery from the Kaikoura earthquakes. They do not capture options for funding these costs such as reprioritisation of other expenditure, phasing or using existing funding pools. Depending on how these costs are funded, the direct fiscal impacts on the operating balance and debt indicators are likely to be different from these gross cost estimates.

- As we know from past experience, risks are to the upside:
 - The experience of Christchurch suggests other unknown costs and government decisions about the shape of the recovery are likely to push up initial estimates.
 - Seismologists' advice is there will probably be further significant earthquakes.
- As we move towards recovery, there is a need to take stock of infrastructure requirements and options available to us to meet those requirements. This work is likely to take some time to progress.
- Such events also highlight the need to consider our wider policies and interactions with local government. ^{s9(2)(f)(iv)}
- The Kaikoura earthquakes underscore the drivers behind our fiscal strategy. Getting on top of spending and paying down debt in the good times ensure we are in a good position to cope with economic shocks and natural disasters, and allow the Government to support New Zealand communities through challenging times.
- At Cabinet next week I will update you on how the Treasury have incorporated the economic and fiscal impacts of the Kaikoura earthquakes into their Half Year Economic and Fiscal Update, which will be released alongside our 2017 Budget Policy Statement on 8 December. At this stage, I do not propose any additional changes to budget allowances as a result of the Kaikoura earthquakes. To the extent that costs cannot be met from within existing allowances, they may be increased at Budget 2017.

Additional Background:

Breakdown of gross costs estimates:

	Initial Estimated Cost
EQC claims costs	^{s9(2)(i)}
State Highway repairs	\$500m - \$1,000m
Local roading repairs	\$500m
^{s9(2)(i)}	
Local infrastructure	^{s9(2)(i)}
Emergency response costs	\$10m (net)
Housing	<\$10m
Health and Education	^{s9(2)(f)(iv)}
Business and Farmer support	<\$20m
Wellington disruptions costs	<\$30m
Other	\$80m
Total	\$2,086 - \$2,816 million

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Reference: T2016/2232

BM-1

Date: 18 November 2016

To: Minister of Finance
(Hon Bill English)Associate Minister of Finance
(Hon Steven Joyce)Associate Minister of Finance
(Hon Paula Bennett)Deadline: None
(if any)

Aide Memoire: Update on the Half Year Economic and Fiscal Update and 2017 Budget Policy Statement

The purpose of this Aide Memoire is to provide an update on the production of the Half Year Economic and Fiscal Update (HYEFU) and 2017 Budget Policy Statement (BPS), in light of the 14 November Kaikoura earthquake.

This note covers:

- our proposed treatment of the Kaikoura earthquake in our HYEFU economic and fiscal forecasts (including an initial estimated costs related to the Kaikoura earthquake), and
- Not covered by your request

You will receive further reports today, including T2016/2220, which will set out the remaining decisions required to finalise HYEFU.

Proposed Treatment of the Kaikoura Earthquake

Given the limited information at hand on the Kaikoura earthquake, there is a large degree of uncertainty regarding the extent of damage, particularly to local infrastructure, which makes assessing the economic and fiscal costs difficult prior to the forecast finalisation dates for HYEFU.

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Overall our approach for the forecasts will be to include material impacts where reasonable estimates are available, supplemented with discussion about uncertainties and scenario analysis in the narrative to our forecasts.

Economic Forecasts

The economic forecasts were finalised on Thursday 10 November, prior to the Kaikoura earthquake. Based on (very limited) information currently available, there is not a lot of evidence to suggest that the medium-term growth picture for the whole of the NZ economy would be substantially different overall. The earthquake was centred in the upper South Island, with damage to areas including Canterbury and Wellington. The areas most affected by the earthquake: the upper South Island, including Tasman, Nelson, Marlborough regions, and the West Coast make up 3.5% of New Zealand's economy, or \$8.3 billion in regional gross domestic product. By comparison, Canterbury's GDP was \$33 billion, or 13.6%, and Wellington \$32 billion¹.

Although at this stage we do not consider the macroeconomic picture to be materially changed, this does not preclude that there may be regional, sectoral, compositional and timing changes to activity as a result of the earthquakes and associated recovery activity. In the Half Year Update documents, we plan to include a qualitative discussion of the compositional changes and other risks that might be expected as a result of the earthquakes. See T2016/2216 for further discussion of the final economic and tax forecasts for the Half Year Update.

Fiscal Forecasts

Fiscal forecasts are due to be completed by Monday 21 November, so there is likely to be limited information available around the recovery plan and expected cost estimates from the Kaikoura earthquake.

We have performed a bottom-up exercise of gathering information from agencies on their initial assessment of fiscal impacts. These estimates are an initial view of costs. As such, there has been limited scope to perform robust review and challenge. The results of this exercise are outlined in table 1 below.

Overall the fiscal cost is estimated to be between \$2 billion and \$3 billion.

¹ Based on Stats NZ regional GDP statistics, 2015.

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Table 1: Initial Estimation of the Cost

	Initial Estimated Cost
EQC claims costs	s9(2)(i)
State Highway repairs	\$500m - \$1,000m
Local roading repairs	\$500m
s9(2)(i)	
Local infrastructure	s9(2)(i)
Emergency response costs	\$10m (net)
Housing	<\$10m
Health and Education	s9(2)(f)(iv)
Business and Farmer support	<\$20m
Wellington disruptions costs	<\$30m
Other	\$80m
Total	\$2,086 - \$2,816 million

The above estimate does not include costs to repair the rail tunnel, which is currently unable to be surveyed. These repairs would not be covered by insurance, therefore these costs are likely to increase. A more detailed table of these costs is attached in Appendix One, including a comparison of the current estimate to the cost of the Canterbury earthquakes.

Costs are based on a gross estimate and include assumptions such as replacing the current asset, rather than policy choices which may affect the investment required. Costs will change over time as the recovery plan becomes clear and the Government considers wider options in light of this event.

s9(2)(i)

In addition, initial indications are that there are some quite different aspects to the Kaikoura earthquakes. The direct costs to the Government for the Canterbury earthquakes reflected the densely populated city. As such, costs included residential property assistance (red zone), repairs to local roads, the central city rebuild and repairs to water infrastructure. While these types of costs may also be present in the Kaikoura earthquakes, it's more likely that costs associated with repairing the state highway and rail network will be far more significant.

Table 1 represents an initial estimate of the total costs of the earthquake. However, not all costs will require additional funding from the Government. For example, the roading costs are likely to be met from the National Land Transport Fund and future hypothecated tax revenue. In addition some costs may be met from delaying other projects rather than new spending while others will be funded from existing budget allowances or insurance payouts.

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As a result the impact on the fiscal forecasts will be with regards to new funding (or incremental costs). Costs that are likely to be funded through reprioritisation or existing Budget allowances will not impact the fiscal forecasts.

Our experience with the Canterbury earthquakes would suggest that these initial estimates are likely to be under-estimated. Our initial estimate of the Canterbury earthquakes in Budget 2011 was \$8.8 billion, almost half of the current estimate of \$18 billion. Almost \$4 billion of the increase was in relation to EQC claims costs. While some of the remaining \$5 billion increase was due to subsequent government decisions (e.g. red zone), estimates also changed as more information came to light. The majority of these increases were managed within existing budget allowances.

At the time the fiscal forecasts are completed the level of costs to be met outside existing budget allowances will not be known. Our initial view is that there is some room in the existing budget allowance to enable costs to be absorbed. We can provide further advice on this as estimates crystallise.

As such, and given this event is likely to cost less than Canterbury, there can be a reasonable level of comfort that cost increases can be met within budget allowances, particularly as they are likely to be capital in nature.

However, discussions about these uncertainties will form an important part of the HYEPU documents.

Table 2: Impact of Fiscal Forecasts

	New funding	Added to fiscal forecasts
EQC claims costs	Yes	s9(2)(i)
Roading repairs	No - reprioritisation	-
s9(2)(i)		-
Local infrastructure	Yes	s9(2)(i)
Emergency response costs	Yes	\$10m
Housing	Yes	\$10m
Health and Education	Yes	s9(2)(f)(iv)
Business and Farmer support	Yes	\$20m
Wellington disruption costs	Yes	\$30m
Other costs	Yes	\$80m
Initial cost estimate		\$955m
Rounded up		\$45m
Increase in fiscal forecasts		\$1,000m

In order to mitigate the tendency to over forecast upper limits have been used. In addition, we have rounded the costs to \$1 billion to provide a further, albeit minor, buffer for unknown costs.

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The majority of these expenses will be operating expenses and recognised in the current financial year. As such, there are no budget allowances that these can be charged against. The additional \$1 billion operating expense will therefore reduce the forecast OBEGAL surplus for 2016/17.

The \$1 billion increase in net debt will occur over the next few years and cash payments are made. s9(2)(f)(iv) and s9(2)(i)

Not covered by your request



Kamlesh Patel, Team Leader, Budget Coordination, Fiscal and State Sector Management, 04 917 6094
Nicola Haslam, Manager, Fiscal Reporting, Fiscal and State Sector Management, 04 917 6943

s9(2)(f)(iv) and s9(2)(i)

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APPENDIX ONE – INITIAL COST ESTIMATE

	Estimated Cost of Canterbury Earthquakes	November 2016 Earthquakes – Comments	Initial Cost Estimate
EQC	\$6,981 million	<p>Significant building and land claims in Kaikoura and Seddon. Numerous of smaller claims in Wellington, Christchurch, and Marlborough.</p> <p>s9(2)(f)(iv) and s9(2)(i)</p>	<p>s9(2)(f)(iv) and s9(2)(i)</p>
State Highway repairs	<p>\$62 million</p> <p>The bulk of roading costs in Canterbury were local roads rather than state highways.</p>	<p>s9(2)(f)(iv) and s9(2)(i)</p>	<p>s9(2)(i)</p>

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<p>Local Roothing repairs</p>		<p>s9(2)(f)(iv)</p>	<p>\$500 million</p>
<p>s9(2)(i)</p>			
<p>Horizontal infrastructure – storm water including stop banks, water supplies, and sewerage</p>	<p>\$1,607 million. \$646 million of these costs relates to local roading. These costs do not include costs associated with state highway repairs.</p>	<p>The Government is obligated under the <i>National Civil Defence Emergency Management Plan</i> to fund Councils for 60% of the three waters horizontal infrastructure and just over 83% of eligible roading. s9(2)(i)</p>	<p>s9(2)(i)</p>
<p>Hospitals and DHB spending</p>	<p>\$1,081 million Capital funding in relation to hospital rebuilding. Some funding was provided from DHB balance sheet.</p>	<p>Kaikoura hospital is currently operating with some additional staff to support emergency. Nelson Hospital is a potential risk as we know key buildings at the hospital have seismic issues, but from a fiscal perspective the redevelopment of this hospital was already in the pipeline – the business case process is already underway.</p>	<p><\$5 million</p>

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Schools	\$931 million Capital funding in relation to school rebuilds, which also addressed long-term demographic/new capacity needs.	s9(2)(i)	s9(2)(i)
Housing – emergency and temporary, and social housing	\$374 million The majority of this spending was capital spending on state housing.	The MSD earthquake response team is reviewing what numbers can be obtained (scale, scope) and the council are inspecting properties in Kaikoura now. Social housing supply situation in Christchurch is good, so do not consider additional funding would be required (insurance kicks-in above \$10 million).	<\$10 million
Business Support Package	\$305 million	Ministers have agreed to a package to support businesses and employees.	\$8.8 million
Farmer Support Package	-	MPI has estimated costs and is seeking funding of a package to support affected primary industries, including fisheries, at \$10 million over two years.	\$10 million
Emergency response costs	\$225 million	Civil Defence response costs (for which appropriation is currently \$2m) and NZDF costs (within the appropriation for emergency response).	\$10 million ** ** Net of existing appropriation for this purpose
Department of Conservation	-	For repairs to roads, bridges and structures on conservation land, as well as administrative infrastructure. At this stage, this is very much an estimate as many of the structures are in isolated areas and have yet to be assessed.	<\$5 million

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Pre-Cab Briefing 21 November 2016

Notes:

- The Treasury will brief the Minister of Finance and Associate Ministers of Finance on Monday 21 November.

Papers for Cabinet Consideration

Item	Title		
	Description and analysis	Fiscal implications	Treasury Recommendation
9	Kaikoura Earthquake: Business Support Package: Decisions by Ministers with Power to Act		
	The paper sets out a package of business assistance support following the 14 November Earthquake. It includes an Employee Support Subsidy and Earthquake Job Loss Cover and is in addition to the existing suite of hardship support available. The proposed package is similar to that which was implemented following the 2011 Christchurch earthquake.	The cost of the package is \$8.840m in 2016/17 only.	Support
10	North Canterbury Earthquake: Proposal for a Special Primary Sector Assistance Package		
	This paper seeks agreement to a primary sector assistance package following the Kaikoura Earthquake. The non-fisheries components are based on a similar relief package that Cabinet agreed to following storms in the Manawatu in 2015.	\$5m for research for affected fisheries and \$5.4m for other components over two years, to be funded from the Between Budget Contingency.	Partial support Treasury supports the \$5.4m component of the paper, but considers that the proposal for research into affected inshore fisheries (\$5m) is not as urgent as the other components and could be considered at a later date alongside any other initiatives that may arise from the Kaikoura earthquake.

Not covered by your request

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**Treasury Report: Budget Policy Statement Cabinet Paper**

Date:	23 November, 2016	Report No.:	T2016/2179
		File Number:	MC-1-5

Action Sought

	Action Sought	Deadline
Minister of Finance (Hon Bill English)	Sign the attached Cabinet paper and Cabinet submission form	

Contact for Telephone Discussion (if required)

Name	Position	Telephone		1st Contact
Ben Udy	Analyst, Macroeconomic & Fiscal Policy	+64 4 890 7428	s9(2)(a)	✓
Renee Philip	Manager, Macroeconomic & Fiscal Policy	+64 4 917 6046		

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

Return the signed report to Treasury.
Lodge the Cabinet paper with Cabinet office.

Note any feedback on the quality of the report

Enclosure:

Yes

(attached)

Treasury Report: Budget Policy Statement Cabinet Paper

Executive Summary

Attached is the Cabinet paper titled '*Budget Policy Statement 2017 and Proposed Spending Allowances*' for your consideration. The paper seeks Cabinet agreement to the capital and operating allowances for Budget 2017, and has been prepared in consultation with your office and the Prime Minister's office.

We ask that you sign the attached paper and accompanying cabinet submission form before 10.00am Thursday 24 November, for consideration by Cabinet on Monday 28 November.

Recommended Action

We recommend that you **sign** the attached Cabinet paper and Cabinet Submission Form before 10.00am Thursday 24 November 2016.

Renee Philip
Manager, Macroeconomic & Fiscal Policy

Hon Bill English
Minister of Finance

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Office of the Minister of Finance

Chair, Cabinet

BUDGET POLICY STATEMENT 2017 AND PROPOSED SPENDING ALLOWANCES

Proposal

1. This paper seeks confirmation of our fiscal priorities and agreement to the operating and capital allowances to be included in the Budget Policy Statement 2017. It also informs Cabinet about the economic and fiscal forecasts for the Treasury's Half Year Economic and Fiscal Update (Half Year Update).

Not covered by your request

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Pages 2 & 3 not covered by your request

19. The surplus in 2015/16 was larger than expected at \$1.8 billion. However, going forward, surpluses are expected to be more in line with prior expectations. This is largely due to the improved tax forecasts being offset by the fiscal impact of the South Island Earthquakes, weaker results from ACC and increased benefit expenses (mostly New Zealand Superannuation).
20. Treasury's initial estimate is that the gross cost to the Government of the South Island Earthquakes will be between \$2 billion and \$3 billion. This is still an early estimate, and it is unclear the extent to which this will be covered by insurance, reprioritising other spending or reducing debt repayment.

Not covered by your request

Fiscal Strategy

26. The Government's current fiscal strategy prioritises building surpluses and starting to pay down debt in order to rebuild fiscal buffers to ensure New Zealand is well placed to manage future economic shocks or natural disasters.
27. The South Island Earthquakes highlight the importance of delivering on the Government's fiscal strategy. While the earthquakes are significant both in terms of their impact on the community, and their fiscal cost, the strength of the Government's books means we are able to respond as needed. Cost will not be a constraint on the recovery effort.

28. Not covered by your request

29.

30.

31. The improving fiscal situation gives the Government choices around progressing these objectives while also supporting communities hit by the South Island Earthquakes and investing in priority public services and infrastructure.
32. When it is affordable, and when economic conditions permit, the Government would like to lower income taxes, with a focus on lower and middle income earners. However, responding to the South Island Earthquakes and reducing debt are currently of higher priority.
33. The improved fiscal outlook means that we are able to increase Budget allowances without changing the Government's fiscal strategy or priorities.

Budget 2017 Priorities and Allowances

34. Budget 2017 will continue to progress the Government's programme and priorities. These have been updated in light of the recent earthquake. These priorities are:
- Responsibly managing the Government's finances
 - Building a more productive and competitive economy
 - Delivering better public services within tight financial constraints, and
 - Rebuilding Christchurch and Responding to the South Island Earthquakes

35. Not covered by your request

36.

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42. The Government will do what is required to support the recovery from the recent major earthquakes. It is too early to know exactly the extent of damage and the likely fiscal cost. The most significant impacts are likely to be increased infrastructure spending to repair roads and other utilities. To the extent this cannot be managed within existing operating and capital allowances, these allowances may be increased at Budget 2017.

Consultation

43. This paper was prepared by Treasury. The Department of Prime Minister and Cabinet was informed.

Not covered by your request

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j) **note** that Government is committed to funding what is required to respond to the South Island Earthquakes and if these costs are cannot be managed within existing operating and capital allowances, these allowances may be increased at Budget 2017;

Not covered by your request

Authorised for lodgement

Hon Bill English, **Minister of Finance**

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Pre-Cab Briefing 28 November 2016

Notes:

- The Treasury will brief the Minister of Finance and Associate Ministers of Finance on Monday 28 November.

Papers for Cabinet Consideration

Item	Title		
	Description and analysis	Fiscal implications	Treasury Recommendation
1	Kaikoura Earthquakes: Urgent Legislation		
	In response to the Kaikoura earthquakes, this paper proposes passing legislation under urgency in the week of 28 November to: (a) bring forward the commencement date of the Civil Defence Emergency Management Amendment Act 2016 to 30 November 2016; (b) clarify that a number of provisions in the Civil Defence Emergency Management Act and the Amendment Act relate to the management of buildings after an emergency; and (c) provide the power to request an assessment of structures (e.g. an engineering assessment of a building).	-	Support
3	Amendment to Business Support Package after the 14 November 2016 Earthquake		
	This paper confirms decisions made by delegated Ministers to amend criteria for the Business Support Package, and to extend it to larger firms, subject to conditions.	-	Support
Not covered by your request			

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Not covered by your request

Oral items

- **Update on Kaikoura (Hon Brownlee)**

Not covered by your request

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Reference: T2016/2342

SH-11-4-3-1



Date: 29 November 2016

To: Minister of Finance
(Hon Bill English)

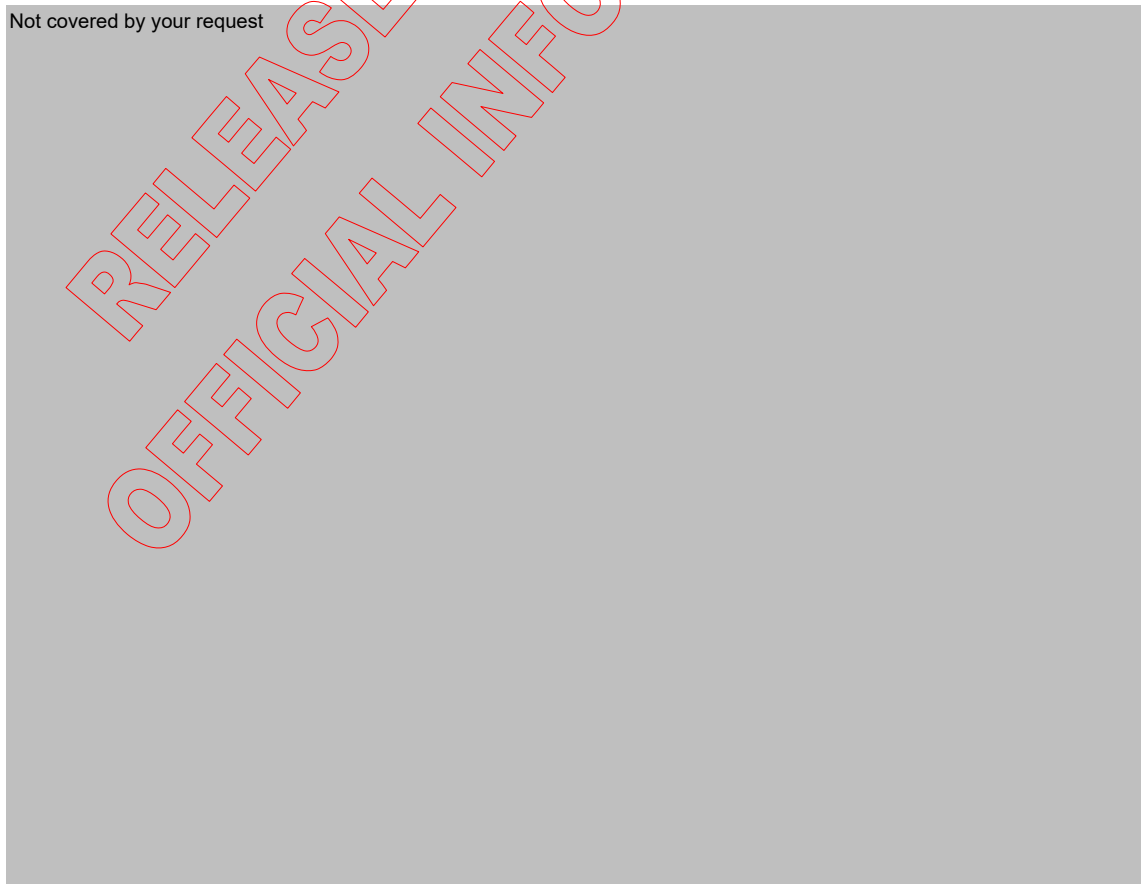
Deadline: Wednesday, 30 November 2016
(if any)

Aide Memoire: Treasury comments on the RBNZ Financial Stability Report November 2016

Overview

The RBNZ will be releasing its six-monthly Financial Stability Report (FSR) on Wednesday 30th November 2016 at 9am. This note provides you with its main findings and some comment.

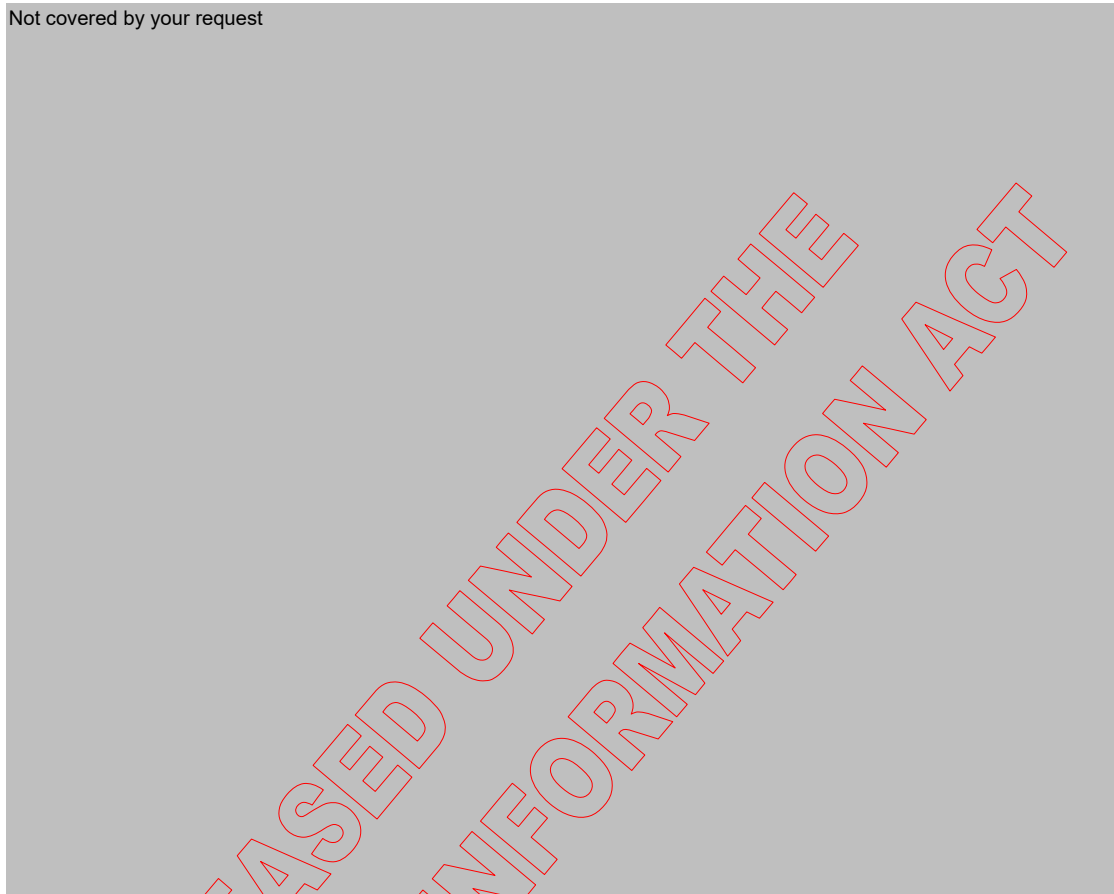
Not covered by your request



Pages 2 & 3 not covered by your request

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Not covered by your request



Other risks

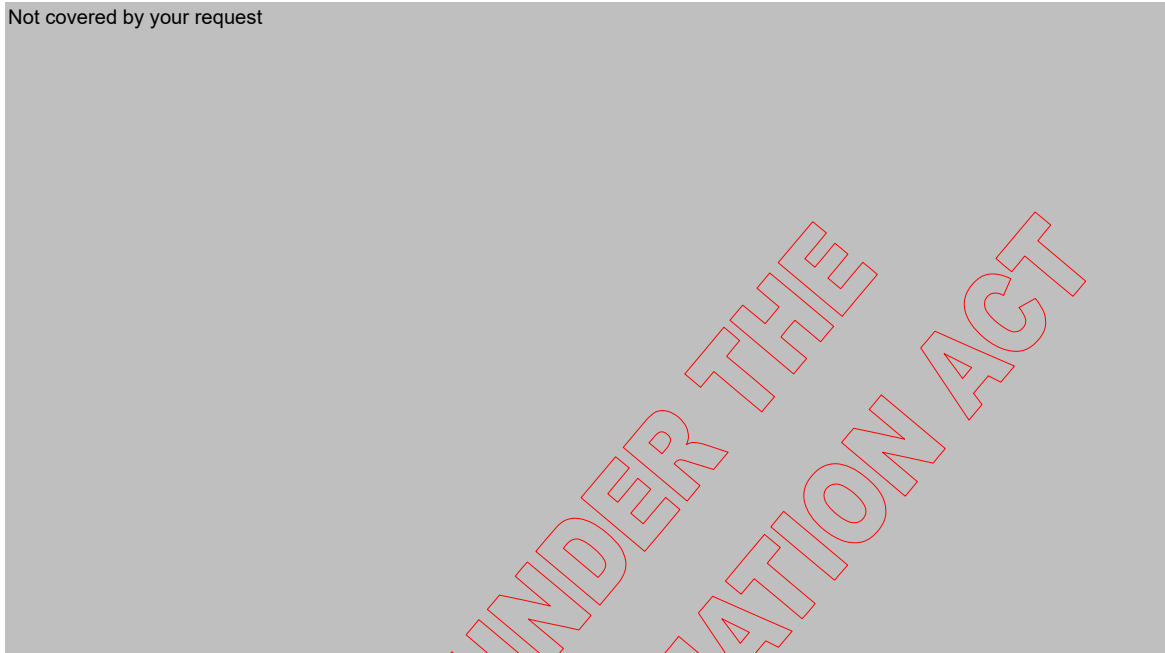
Damage from the Kaikoura earthquake on 14 November is still being assessed. The insurance sector as a whole appears better positioned than in 2010 to meet claims and other earthquake-related costs. This has been helped by the move of private insurers to a sum-insured basis and that they have about \$14 billion more in catastrophe reinsurance and capital than they did at the time of the Canterbury earthquakes.

Not covered by your request



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Not covered by your request



Barrett Owen, Analyst, Financial Markets, +64 4 917 6103
Craig Fookes, Team Leader, Financial Markets, +64 4 917 6234

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Treasury Report: Monthly Economic Indicators November 2016

Date:	1 December 2016	Report No:	T2016/2361
		File Number:	BM-3-3

Action Sought

	Action Sought	Deadline
Minister of Finance (Hon Bill English)	Note the contents of this report Note a copy of this report has been sent to the Prime Minister	The MEI will be published on the Treasury website at 2pm Monday 5 December
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
Brendon Riches	Senior Analyst	+64 4 917 6297 (wk)	✓
Patrick Conway	Principal Advisor	+64 4 917 6957 (wk)	

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

Return the signed report to Treasury.

Note any feedback on the quality of the report

Enclosure: [\(Monthly Economic Indicators - November 2016 \(FINAL MEI\):3624566\)](#)
[\(Economic Chart Pack Nov 2016:3624014\)](#)

IN-CONFIDENCE**Treasury Report: Monthly Economic Indicators November 2016**

Executive Summary

- Robust labour market and retail sales data point to solid third quarter GDP growth
- An earthquake on 14 November caused some localised disruption to activity in central New Zealand but nation-wide impacts appear limited
- Global financial market volatility increased in November, reflecting the unexpected change in the outlook for US economic policy in light of the presidential election

Economic data released over November reinforced the outlook for solid GDP growth over the second half of 2016. Activity in the third quarter was underpinned by robust growth in the labour market and in retail sales. Wage pressures remained benign, reflecting the rapid pace of expansion in labour supply and subdued inflation expectations. Nonetheless, labour income growth remained solid, driven by the increase in employment.

Income growth supported a further expansion in real retail sales in the September quarter, which increased 0.9% from the previous quarter. Tourism, which also contributed to retail sales growth in the September quarter, showed further strength in October, with the number of visitor arrivals 14.5% higher than the same month a year ago.

Other indicators of activity in the December quarter were also generally positive, while business and consumer confidence remained high. Overall, we expect growth over the second half of 2016 to be similar to that recorded over the first half of the year.

Risks to the outlook arose from the large earthquake that occurred on 14 November. The earthquake caused extensive damage and some loss of life in the Kaikoura and adjoining regions. The town of Kaikoura, which is an important tourist centre and on the main South Island road and rail network, was extensively damaged and transport links were blocked by large slips. There was also damage to housing and commercial buildings in Kaikoura and adjoining regions, including Wellington.

While the impact of the earthquake and subsequent aftershocks on the region directly affected is significant, its impact on the economy as a whole is considered likely to be relatively minor at this stage. The Special Topic this month discusses the likely regional and national economic impacts.

The housing market is a further source of risk to the outlook. The Reserve Bank observed that growth in house prices remained excessive and was posing a risk to financial stability. Nonetheless, the Bank reduced the Official Cash Rate (OCR) from 2.0% to 1.75%. The Reserve Bank projected the cash rate to remain at this level over the next two years or so, although it did not rule out the possibility of a further reduction.

The global economy showed some resurgence of demand according to data released this month, while business activity indicators remained subdued. There was increased volatility in financial markets arising from an unexpected change in the outlook for US economic policy in the light of the presidential election.

IN-CONFIDENCE**Recommended Action**

We recommend that you:

- a **note** the contents of this report
- b **note** this report will be available on the Treasury website at 2pm, Monday 5 December 2016
- c **note** that the next Monthly Economic Indicators Report is scheduled for delivery to you on Thursday 2 February 2017, and
- d **note** a copy of this report has been sent to the Prime Minister

Patrick Conway
Principal Advisor

Hon Bill English
Minister of Finance

Hon Steven Joyce
Associate Minister of Finance

Hon Paula Bennett
Associate Minister of Finance

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Reference: T2016/2378

DH-37-1-1

Date: 2 December 2016

To: Minister of Finance (Hon Bill English)

Deadline: 4 December 2016

Aide Memoire: Advice on the Kaikoura Earthquake - reinstatement of South Island Corridors Cabinet paper

Background

- The paper recommends that Cabinet:
 - Support a proposal to reinstate the State Highway 1 and rail corridor between Ward and Cheviot at an estimated cost of s9(2)(f)(iv). The estimated time to complete the project is 12 months.
 - Agree that the Crown fund the s9(2)(f)(iv) roading component of the project.
 - s9(2)(i)
 - Authorise the Minister of Transport to prepare an Order in Council to enable the necessary works and approvals for the project.
 - Invite the NZTA Board to manage the project on behalf of the Crown.
- The project has the following cost components:

Component	Estimated cost (\$ million)
Road	
SH1 Reinstatement	s9(2)(f)(iv)
Upgrade SH1 safety and resilience	
Alternate SH route	
Local roads	
Emergency fund contribution	
Total Roads	
Rail	
Rail reinstatement cost (MoT estimate)	s9(2)(i)
Potential insurance contribution	
Total Rail	
Total Estimated Cost	

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Financial impact

- 3. The Treasury's initial estimate of the road and rail reinstatement costs is between \$1.5 billion and \$2.0 billion. However, the fiscal forecast for the HYEPU assumed no fiscal impact as the assumption was that costs would be met from the National Land Transport Fund and KiwiRail insurance.
- 4. The proposed funding request is all for State Highways and therefore it is all capital in nature. If the full amount of the proposed request is funded by the Crown this would nearly exhaust the Budget 2017 capital allowance. This highlights the importance of working through a process to look at funding options and mechanisms.
- 5. There may also be a positive effect on the road tax revenues due to increased use of road freight by rail freight customers.
- 6. Investment in KiwiRail's network would be treated as capital, however it is possible that this would need to be impaired to reflect that expected future revenue flows will be less than the capital outlay.

7.



8.

Comment

- 9. The Treasury does not support the paper as it is written for four reasons:
 - a A key lesson learned from the response to the Canterbury earthquakes was to avoid committing early to irreversible expensive decisions. At this stage, there is sufficient uncertainty in the cost estimates and other components of the project to support further investigations to be completed before fully committing to Crown fund the preferred option.
 - b The level of service required should inform the option chosen to reinstate the transport corridor and the mix of transport modes on the corridor. An assessment of the medium to long term levels of service required for road and rail, in the context of local, regional and national transport networks should be carried out before confirming the preferred route and which transport modes are reinstated.
 - c Earthquake recovery costs should be met, as far as is possible, from existing funding sources. Further analysis is required to assess options for the National Land Transport Fund to meet the roading costs of the recovery

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and other potential funding approaches before committing to a Crown grant.

- d There are sufficient funds available to the NZTA through the National Land Transport Fund to support the initial project design and recovery process. These funds are made up of the \$125 million emergency fund and a \$75 million loan facility. This means that the project would not be delayed while further analysis is undertaken to inform decision making.

Treasury Recommendation:

10. We recommend the following approach to support the recovery and inform decision making for this project:
 - a Agree, in principle, to support the reinstatement of a transport corridor on the coastal route to allow the NZTA to continue project design and preparatory work, firm up cost estimates and project duration, and to continue the preparation of the Order in Council to facilitate the project.
 - b Commission transport officials to assess the medium to long term level of service requirement for the transport corridor. This work should assess the requirements of all traffic types (e.g. freight, tourists), the role of each transport mode in terms of connectivity and as part of the wider transport network.
 - c Ask officials to continue working with KiwiRail to confirm the costs to reinstate the rail network ^{s9(2)(f)} following the Kaikoura earthquake. This work would also look to clarify the short and long term financial impacts on the company and the implications of this on its business plan supporting its 2017 Budget Bid.
 - d Instruct officials to carry out an assessment of the funding approaches available for this project. This would include analysing the ability of the NLTF to directly support a portion of the roading costs (e.g. betterment costs) and options for Crown funding including a loan or a grant.
 - e Following the completion of this work, you and the Minister of Transport would report back to Cabinet in early 2017 on the outcome of the above actions with recommendations for the reinstatement option and funding approach.
11. We recommend that you do not support recommendations in this paper, and instead table the alternative recommendations in Annex 1(changes are underlined).

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Annex 1: Alternative Recommendations

1. The Minister of Finance recommends that Cabinet:
 1. **note** that several strategic options have been considered for the reinstatement of the critical South Island transport routes damaged by the Kaikōura earthquake sequence
 2. **agree, in principle, to reinstate the transport corridor along the current coastal route, with improvements to the safety and resilience of the route**

Legislative implications

3. **note** that an Order in Council will be required under the proposed Hurunui/Kaikōura Earthquakes Recovery legislation to modify certain enactments to provide for works to clear landslips and restore access to State Highway 1
4. **agree** that the Minister of Transport, in consultation with the Acting Minister of Civil Defence, the Minister of Finance [and all Ministers responsible for legislation covered by the Order in Council], have the Power to Act in respect of submitting any Order under the proposed Hurunui/Kaikōura Earthquakes Recovery legislation to the Executive Council
5. **authorise** the Minister of Transport to instruct Parliamentary Counsel to prepare the necessary Order in Council under the Hurunui/Kaikōura Earthquakes legislation, subject to recommendation 3 above

Financial implications

6. **note** the estimated cost of the preferred reinstatement option is \$1.4 billion to \$2.0 billion, ^{s9(2)(i)} [REDACTED]
7. **agree** that the Crown contributes to the roading costs to reinstate the transport corridor that cannot be met from the National Land Transport Fund
8. ^{s9(2)(i)} [REDACTED]
9. **note** that officials will assess the medium to long term level of service requirement for the transport corridor as part of the wider transport network

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10. **invite** the Minister of Transport and Minister of Finance to report back to Cabinet in early 2017 with recommendations for the reinstatement option, updated cost estimates and a proposed Crown-led funding approach
11. **agree** that any Crown contribution to the reinstatement and the funding approach will be confirmed as part of the Budget 2017 process
12. **note** that the mechanism to give effect to these decisions is that the Minister of Transport will invite the Board of the New Zealand Transport Agency to lead and coordinate with the Board of KiwiRail to deliver the reinstatement of the South Island Transport corridor project on behalf of the Government
13. **note** that preparatory work for the preferred option, as well as work on the alternative Springs Junction/Lewis Pass route and the emergency inland route, will be funded from the emergency works allocation of the 2015-18 National Land Transport Programme

Next steps

14. **note** that the New Zealand Transport Agency and KiwiRail expect to begin work immediately and that it is hoped that restricted access to Kaikōura from the south will be available prior to Christmas and that restricted access will be available from the north in around 12 months

Publicity

15. **note** that a press release will be issued announcing decisions in this paper.

Jon Butler, Senior Analyst, National Infrastructure Unit (NIU), +64 4 917 7254

David Taylor, Manager, National Infrastructure Unit (NIU), +64 4 890 7200



DEPARTMENT of the
PRIME MINISTER and CABINET

Te Tari o Te Pirimia me Te Komiti Matua



THE TREASURY

Kaitohutohu Kaupapa Rawa

Kaikoura earthquake – future decisions: prioritisation and sequencing

Date:	2 December 2016	Priority:	High
Security classification:	Sensitive Commercial In-Confidence		

To: Rt Hon John Key
Hon Bill English
Hon Gerry Brownlee
Hon Steven Joyce

PM, Ministers

Executive summary

This note sets out preliminary advice on options for prioritisation and sequencing of upcoming decisions, and seeks your confirmation of the approach officials are taking to shape up advice on earthquake-related matters. It also sets out some thoughts and advice on the degree and manner of involvement iwi and local government could have in the process and decision making.

We have also attached the fourth update on the key recovery issues that agencies have identified as a result of the Kaikoura earthquake. As a reminder, this has been developed by DPMS with all relevant agencies. The traffic light ratings are agencies' own – they should be taken as indicative.

To date, Ministers have primarily focused on the decisions that need to be taken within their own portfolios to get the response up and running. As we move more clearly into the recovery stage, there are some upcoming decisions which would benefit from being taken as a package and assessed against a consistent standard, including:

- the design and progression of Orders in Council (noting that there will be a degree of coordination given Hon Brownlee's role as the Minister responsible for the Act)
- upcoming decisions related to supporting economic recovery in Kaikoura and the broader upper South Island (e.g. a Tourism Support package, whether to re-open the Kaikoura cray fishery, and renewal of the earthquake support subsidy)
- any decisions on increasing Wellington regional resilience and network infrastructure over the medium term.

Recommendations

We recommend that you:

1. **indicate** if you have any feedback on:
 - a. the prioritisation and sequencing proposals on page 5 and in the appendix
 - b. your preferred approach to working with iwi and local government

- 2. **forward** copies of this briefing to Ministers Bridges and Smith, given the fundamental importance of their portfolios in the recovery.

Anneliese Parkin
**Deputy Chief Executive,
Policy
DPMC**

David Mackay
**Director,
Growth and Public Services
Treasury**

PM do you agree to refer copies of this briefing to Ministers Bridges and Smith?	Yes / No
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Upcoming decisions

Ministers have faced and will continue to face numerous decisions across many portfolios responding to the effects of the 14 November earthquake. Some of these decisions are of an immediate and short-term nature, managing the initial shock and dislocation to communities, businesses and transport, while others will have more enduring impacts, such as rebuilding infrastructure and determining the desired level of resilience to future events.

We believe the collective positive impact of these decisions on the Government's broader objectives will be greater if they are framed through principles underlying existing central government priorities and interventions, and linking explicitly to local recovery priorities as articulated by iwi and Councils. This will help ensure that decisions across different portfolios are coherent and mutually reinforcing. It will also help ensure that decision-making is coherent from the perspective of the affected communities in which they land. This is particularly so for decisions with more enduring or precedential impacts.

Clear command and control structures are critical for effective rapid response, but collaborative ones are equally important to enable efficient and effective recovery and resilience building in the longer term.

Core issues

While the Kaikoura earthquakes raise a great many issues across a wide range of government activity and interests, as we see it, the list of core strategic issues requiring decisions is relatively short:

Transport

- Following Ministers' decision to reinstate State Highway 1 and associated rail infrastructure, deciding on related transport infrastructure in the upper South Island and its connections to the North Island
- Taking any required action to enable appropriate management of transport infrastructure and travellers' expectations until the reinstatement is complete

Economic and social recovery

- Supporting the recovery of Kaikoura and surrounding communities to a sustainable future state, including setting out:
 - the expectations and obligations on central and local government and others regarding disaster response and recovery (e.g. given the small size and potentially limited capacity of the Kaikoura District Council)
 - agreed outcomes, respective contributions, resources and capabilities available from both central and local government (e.g. the 60/40 split and Local Government Risk Agency proposals)
- Monitoring and if necessary shaping market impacts, including:
 - insurance as an important risk transfer tool for people and business
 - national and local labour, equipment and materials markets arising from increased demand
 - access to goods, given disruptions to supply chains
- Considering what wider support is needed in other areas (e.g. Wellington and Marlborough)

Resilience

- Reviewing current land use planning and building regulatory and compliance systems, particularly in light of damage to some modern buildings within the Wellington CBD
- Deciding on and delivering initiatives to improve Wellington's preparedness and resilience, including at a household level
- Enhancing national response capacity and capability.

Testing Future Decisions

Treasury recently gathered a collection of lessons identified from the Christchurch events. Key lessons relevant to this context include:

1. Take a dynamic and adaptive approach to policy development. Where there is significant uncertainty, avoid committing early to irreversible expensive decisions.
2. Consider carefully the Government's recovery narrative. In the Canterbury earthquakes it was not to rebuild as it was, but to rebuild a dynamic resilient city.
3. A key role for central government is informing, influencing and supporting the many recovery actors.
4. Keep expectations realistic. Recovery takes a long time.
5. Good relationships between policy advisors, decision-makers, implementing agencies and other key stakeholders, particularly between the central and local levels of government, can do a lot to support the pace and quality of decisions on recovery (and difficult relationships can slow things down a lot). Carefully consider the relationship management dimension in processes and decisions.

In light of the above we have developed the following questions, to help frame our analysis and advice:

1. Does the initiative progress the Government's overall priorities?
2. Does it support local priorities?
3. Is the initiative efficient, effective and cost-effective? Is it a good use of public funds?
4. Does it increase infrastructural, social and environmental resilience, e.g. does it work towards reducing the costs and dislocation of *future* disasters?
5. Does the initiative inappropriately inhibit market mechanisms and signals that people should be factoring into their decisions on where to live, work and invest?
6. Are the right actors (i.e. those with the best knowledge, capacity, motivation and alignment with relevant regional or national interests) making the decisions (central or local government, individuals or market participants)?
7. Does the decision-making process appropriately balance decision speed and inclusive processes with community and stakeholder involvement?
8. What precedents and expectations will the initiative create, and are these appropriate?

Sequencing and prioritisation

The table in Appendix 1 sets out our preliminary thoughts on decisions that will need to be taken and timing.

As you're aware, the alternative route between Blenheim and Christchurch is already under significant pressure and transport routes (including shipping) may need active management. Early communication of intent to take any concrete steps to actively manage freight movements, or the triggers that would lead agencies to take such steps, would reduce the risk of others planning on one thing happening and then another eventuating (e.g. this could affect how any tourism facility funding grants are allocated).

We recommend that the design of any economic recovery support should be focused on recovery of independence / economic wellbeing of individuals and families, rather than places – and not necessarily assume a return to the pre-earthquake status quo. As you know, the sudden change in transport routes is causing a significant change in the distribution of economic activity. Some of this will continue until SH1 is fully rebuilt, but there are likely to be ripple effects for many years beyond that. People and capital should be encouraged to respond and adjust to those changes.

As noted above, we suggest considering the economic recovery decisions as a package. Funding decisions should reflect a consistent approach on issues like whether the government will support businesses to retain staff until business as usual activity resumes, particularly given the long recovery times expected for some industries (e.g. paua) and the seasonality of the tourism industry.

You have received a separate paper on Wellington / lower North Island resilience to a large-scale earthquake. There is a discussion to be had on how much resource Ministers want to exert in this space. At this stage the direction sought is primarily in relation to scoping and developing greater understanding. It would be useful to signal Ministers' appetite for central government spending and involvement in this so that effort is appropriately prioritised. An alternative to public sector spending would be to ask officials to look at regulatory options for requiring the private sector to take steps to increase infrastructure and supply chain resilience.

Iwi and local government involvement in earthquake-related process and decision making

Iwi

There are multiple iwi interests in the earthquake recovery process. The model that iwi appear to have in mind is the strategic partnering model in the Christchurch earthquake legislation, which provided for a "strategic role" for Ngai Tahu in the recovery and in working with CERA. There are some signs Ngai Tahu is going further in its asks, e.g. asking for involvement in any decision on a Recovery Manager, or in consenting processes.

The Government needs to decide if it wants to replicate such a model and whether it is willing to go further. Although it would bring benefits, operating the Christchurch model in this instance is likely to be more complex given the multiple interests involved.

While the Kaikoura/Hurunui situation is confined in terms of the breadth of issues needing to be resolved, it is geographically spread across a number of settled iwi. Therefore, the role of Ngai Tahu is more limited and its interests need to be considered alongside the interests of other top of the South iwi. The Kaikoura legislation also doesn't establish a new authority like CERA that iwi would be able to engage with, nor does it call for a formal recovery strategy in the same way (you'll recall that, for Christchurch, the strategy had to be developed in consultation with Ngai Tahu).

If the Government was of a mind to develop a non-legislative recovery strategy, then, consistent with the ideas below, central and local government could develop the strategy informed by the interests of iwi within areas of interests or involving resources of particular interest.

It will be important to ensure that recovery efforts don't impact on Treaty settlements without express engagement and agreement with settled iwi.

There is a substantial iwi energy and commitment that can be capitalised on, using existing processes and relationships. For example, iwi already have well established partnerships with ECAN and the relevant territorial authorities. If Ministers consider iwi engagement in recovery is desirable, then realistic expectations would need to be agreed from the outset, remaining mindful that iwi have their own resources and capability that can be used to solve problems.

Local government

Central government officials have met with local government officials from Kaikoura, Hurunui, Waimakariri and ECAN following the quakes. They were extremely grateful for the effective and coordinated first response efforts across central government to assist them (e.g. evacuation support by NZDF as well as financial support for Kaikoura). They also expressed their gratitude for the personal interest taken by multiple central government Ministers who have taken the time and effort to visit and show support.

It is also clear from these meetings that the Local Authorities in the 'top of the South' have collaborated effectively to give practical on the ground support to each other across the region. For example, small communities like Kaikoura and Hurunui have been able to draw on the experience of ECAN to help them identify how to deal with both immediate issues such as how to manage spoil from clearing land slips through to longer-term issues like how to manage the social impacts of the quakes on the community in the lead up to the Christmas period, when a sense of isolation can set in.

In Wellington, officials have also been meeting to ensure that local and central government response and recovery efforts are well aligned. This close collaboration is particularly important as the Wellington regional and city councils hold (or are responsible for managing Council Controlled organisations that hold) many of the most immediate assets that are critical for the capital's resilience in case of a further sizeable earthquake. This applies particularly to the management of water supplies but also to other critical infrastructure such as roads, Wellington's port and electricity network.

Working with iwi and local government

In working through how to engage with iwi and local government, we suggest the following could be helpful:

- It should be clear what the respective parties' roles, responsibilities and decision-making rights are.
- Expectations should be clear and met once agreed.
- Engagement should be proportionate to interests and respectful of the various players' resources.
- Continued good coordination on service delivery and investment strategy is important to achieve an integrated response that meets the practical needs of the local community as well as the national interest.

Background - Impacts of the Kaikoura Earthquakes

The Kaikoura earthquakes have had significant, but manageable, impacts so far. You have been provided with initial estimates of the costs that central government may face in responding to these impacts and early discussion of possible economic impacts. These fiscal costs are largely a bottom-up exercise and have a number of caveats attached to them given the early stage of assessment and decision-making and the uncertainty involved. These fiscal estimates, of net and gross costs to the Crown of \$1 billion and \$2-3 billion respectively, are included in the *Half Year Update* forecasts being released on 8 December.

The New Zealand economy is expected to be resilient and adaptable to recent events, as it was in response to the larger impacts in Canterbury after the 2010/2011 earthquakes. The regional impact will be significant, but the macroeconomic effects for the national economy are likely to be limited as affected activity is either displaced elsewhere or delayed. These effects are expected to be less than with the Christchurch earthquakes given the smaller amount of damage and smaller impacts on a main urban area.

There will be short-term disruption to economic activity from the damage to infrastructure and impact on the transport network. This is likely to detract from real GDP growth and may add to price inflation (e.g. freight costs) in the short-term. Activity associated with the immediate response may help offset disruption, as occurred in early 2011. Tourism and primary production, including fishing, will be negatively affected.

The recovery from the earthquakes will support activity, although the net impulse to the economy will depend on a range of factors including how much capacity is available to rebuild damaged infrastructure, repair damaged buildings, and undertake any additional investment that takes place to increase resilience to future events, given wider pressures in the construction sector.

There is still uncertainty about the impact of recent events and risks to the estimates above. Based on the experience of recovery in Christchurch, the gross estimates of fiscal costs are likely to rise, potentially significantly, as more information comes to hand and as Government decisions are made. As you'll be aware, there is also the potential for a major aftershock to cause significant further damage, disruption and costs.

Both the economy and the fiscal position are in a better place than when the Christchurch earthquakes occurred in 2010/11. The economy had slowed through 2010 and contracted in both the September and December quarters of that year, with the unemployment rate sitting at 6.2% in December 2010. Recent events have occurred with strengthening economic growth and lower unemployment. In contrast to 2010/11, the operating balance is now in surplus compared with substantial deficit. And while net debt is currently higher than it was at the end of 2010, the forward trajectory is now down compared with up. There also remains room for monetary policy to respond, but this does not currently appear to be required. However, as in 2011, there remain a number of global risks that could impact negatively on this positive outlook.

Appendix – Prioritisation and sequencing of decisions

Area	Before Christmas 2016	First quarter 2017	Mid 2017 (incl Budget)	Longer term
Legislation / regulatory regime	<ul style="list-style-type: none"> Finalised OIC Bill following Select Committee recommendations Any OICs needed before Christmas (coordination required) Decision on whether to give notice of a National Transition Period Enhancement of national response capacity and capability 	<ul style="list-style-type: none"> Interaction between any Recovery Plan & existing plans & regulation 		<ul style="list-style-type: none"> Transition from OICs to 'normal' regulatory environment Review of regulation in light of lessons identified s9(2)(f)(iv)
Transport	<ul style="list-style-type: none"> Decisions on SH1 and rail [Cabinet 5 Dec] Potential decisions on regulation of / support for coastal shipping, and powers of transport agencies to manage freight and people flows until SH1 and rail reinstated 	<ul style="list-style-type: none"> Potential bespoke legislation to support SH1 and rail rebuild if needed Potential bespoke legislation for CentrePort repairs / rebuild Detailed SH1 and rail rebuild design / business case decisions s9(2)(f)(iv) 	<ul style="list-style-type: none"> Funding for road and rail rebuild s9(2)(f)(iv) 	
Economic and social recovery	<ul style="list-style-type: none"> Government contribution to Kaikoura public infrastructure rebuild Decision on expectations of, and obligations on, local government regarding disaster response and recovery (after reviewing resources and capabilities available to them) Review of the Earthquake Support package Tourism Support package – purpose, scope and funding Review of Kaikoura Cray fishery closure 	<ul style="list-style-type: none"> Review of Kaikoura paua fishery closure s9(2)(f)(iv) Any decisions emerging from the Regional Economic Growth Programme in relation to quake affected areas 	<ul style="list-style-type: none"> Potential review of Tourism Support Package once SH1 south of Kaikoura is open 	<ul style="list-style-type: none"> Potential generic approaches to economic support in an emergency, including to businesses, rural communities and sectors, e.g. tourism
Resilience	<ul style="list-style-type: none"> Direction on pace and scale of work to improve Wellington and Lower NI resilience Potentially set of early specific decisions on options to increase lifeline resilience 	<ul style="list-style-type: none"> s9(2)(f)(iv) Any decisions required following 111 system review to ensure future resilience 	<ul style="list-style-type: none"> s9(2)(f)(iv) 	<ul style="list-style-type: none"> s9(2)(f)(iv)
Community, local government and iwi engagement	<ul style="list-style-type: none"> Governance mechanisms and working arrangements to support collaborative partnerships between central government, local government, iwi and community leaders 			

From: Jon Butler [TSY]
Sent: Monday, 5 December 2016 9:00:10 AM
To: Sam Tendeter; ^Parliament: Samantha Aldridge
Cc: ^Parliament: David Kidson; s9(2)(g)(i); David Taylor [TSY]; Simon McLoughlin [TSY]; Siobhan Coffey [TSY]
Subject: RE: Aide Memoire: Advice on the Kaikoura Earthquake - reinstatement of South Island Corridors Cabinet paper

Hi Sam

Answers in bold below.

Happy to clarify anything by phone.

Regards

Jon

Jon Butler | Senior Analyst - National Infrastructure Unit | **The Treasury - Kaitohutohu Kaupapa Rawa**
Tel: +64 21 862290 | Jon.Butler@treasury.govt.nz

From: Sam Tendeter [mailto:Sam.Tendeter@parliament.govt.nz]
Sent: Sunday, 4 December 2016 5:22 p.m.
To: Jon Butler [TSY] <Jon.Butler@treasury.govt.nz>; ^Parliament: Samantha Aldridge <Samantha.Aldridge@parliament.govt.nz>
Cc: ^Parliament: David Kidson <David.Kidson@parliament.govt.nz>; s9(2)(g)(i); s9(2)(g)(i); David Taylor [TSY] <David.Taylor@treasury.govt.nz>; Simon McLoughlin [TSY] <Simon.McLoughlin@treasury.govt.nz>
Subject: RE: Aide Memoire: Advice on the Kaikoura Earthquake - reinstatement of South Island Corridors Cabinet paper

Hi

Thanks for this note.

As you are recommending a number of different changes to the recommendations it would be helpful to be able to clearly set out which changes relate to which concern. The more simply this can be explained the easier.

I understand that there are 3 treasury concerns:

Primary concern – There does not appear to be a compelling reason to lock in funding decisions at this stage. Through the emergency fund, NZTA have cash flow to continue design work/ clearing slips in the short term. Following further work, funding decisions can be made with more certainty.

- 1.) new crown funding may not be needed for the full cost (I.e. Could be funded via loan or additional land transport fund contribution).
- is Treasury view that the phrase "crown fund" is inconsistent with a loan? **It is not inconsistent, but it would be better to make it clear that all Crown funding options are still on the table to be considered.**
 - if this was the only concern cabinet want to respond to, is it correct that all that needs to change is insertion of your recc 7 for the original recc 9. This would also allow for greater contribution from nltf. **Yes**
 - The cabinet paper suggests that nltf is needed for works on emergency route and Lewis pass. I also note \$125m emergency contribution is already factored into estimated costs. Do these things fully exhaust any existing funding? And therefore the only way more would be available is 1.) existing projects deferred; or 2.) there is upside revenue because of increased road freight (presumably this wouldn't be huge?). **More a question of timing, than quantum of the funding at this stage. The emergency funding should allow for work to proceed in the short term until enough information is available to make a more informed decision. This would include analysis of the funding options available.**
 - the cabinet paper says there are no expected capacity constraints – **We have not received any information to support this. This project is estimated to spend ^{s9(2)(f)(iv)} the 10 year plan lists planned investment of \$1.3bn over 5 years. Marked difference and it would be good to see supporting information.**
 - in the event full crown funding was agreed and there subsequently turned out to be further nltf funding available, could a subsequent funding decision be made to adjust crown contribution; and/or are there other projects in the pipeline where this additional funding could be used instead of crown funding? **This would be possible, and there would likely be other projects (e.g. paying down debt etc). But this approach seems the wrong way round, assuming that there is time now to do the analysis.**
- 2.) whether to agree to that specific road option. More analysis may lead to a different preferred option.

No specific issues with the supporting the coastal route option. But we should fully understand the long term level of service required on the route (volume, use type, speed, safety, resilience) before committing to a design and cost. There is time to do the analysis to inform decision making.

s9(2)(g)(i)

We are more comfortable with supporting/ communicating a 'transport corridor', rather than "reinstatement of the road and rail" until this analysis is done.

- noting the cost and length of time (5 years?) needed for inland road options, does treasury consider these should be kept on the table? Or does treasury consider the realistic options are limited to coastal road? Or is it just too early to tell? (If it is too early to tell what kind of information (e.g. X option actually x faster and x cheaper and road service demand x more, may

support a different approach) **As above, discarding inland routes not a primary concern.**

- if this was a concern and some greater flexibility was wanted to be able to decide on inland routes (I.e. If after further analysis/coatings it seemed a better option) your rec 2 (with addition of rec 9) would be needed to replace cab paper rec 2? Although this still gives a strong signal to reinstatement option. **Yes, this would work**
- if cabinet were sure a replacement coastal road was the only valid option then the existing cab paper rec 2 is ok? **Yes for roads – but not for rail.**

3.) how to replace rail. And that costs are still very uncertain.

- if options want to be kept open here, insert your recs 8 and 9 with can paper recs 7 and 8. **Yes keep options open here.**

There also appear to be a various wording changes to other recs. Are all of these essential?

No not essential – mainly due to slight changes in the final lodged version.

I do not have the information to answer the next set of questions. My understanding is that the costs/ project plan will firm up once NZTA can get access to the route in late December/ January. The paper suggests the following:

Para 28 – robust business case process will be undertaken by NZTA– we support this.

Para 38 – funding decisions will be taken as part of budget 2017

When would a final decision need to be made in order to support proposed 12 month timetable? (Is this budget or before? And what costs are expected to be incurred by then?)
When are rail costings expected to be known?
Are there dependencies that mean a final decision on the road and rail should be taken at same time? ^{s9(2)(i)}

Any comments first thing (before 9am ideally, or if not brought to precab). Happy to discuss them.

Many thanks, Sam

Sent from iPhone

Sent with Good (www.good.com)

From: Jon Butler [TSY]
Sent: Friday, 2 December 2016 1:20:26 p.m.
To: Sam Tendeter; Samantha Aldridge
Cc: David Kidson; Annelise Bunce [TSY]
Subject: Aide Memoire: Advice on the Kaikoura Earthquake - reinstatement of South Island Corridors Cabinet paper

[IN-CONFIDENCE]

Hi Sam and Samantha

As discussed, please find attached our aide memoire and the final version of the cabinet paper received today from MoT.

We do not support the paper as it is written and we have provided alternative recommendations for the paper.

Please give me or Annelise a ring to discuss if any clarification is required.

Cheers

Jon

Jon Butler | Senior Analyst - National Infrastructure Unit | **The Treasury - Kaitohutohu Kaupapa Rawa**
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Office of the Minister of Finance

9 December 2016

Kaikoura Earthquake: Support for rehabilitating Kaikoura Harbour

Context

Damage to Kaikoura harbour from earthquake

1. The earthquake has caused the Kaikōura harbour to rise by 1-2 meters. This has rendered the port and wharf structures not suitable for purpose. In effect the old low tide is the new high tide (see appendix 1 for photos of the impact).

Impact of harbour damage on local industry and local economy

2. The earthquake has caused significant disruption to the tourism and fishing sector in Kaikōura, which is a critical part of the local economy. The tourism spend in the region was \$125 million in the year ended October 2016, with the tourism-related sectors of accommodation and retail the second and third largest sources of income and employment respectively (agriculture is the largest).
3. While a lack of road access is clearly a significant barrier, much of the tourism industry is reliant on the harbour. The largest tourism company in Kaikōura, with approximately 70 employees, is Whale Watch. It can currently only operate during a two-hour window around high tide. Encounter Kaikoura, with 40 employees, is the next largest operator and has similar issues.
4. The damage to the harbour has also had a significant impact on the local fishing industry. We understand that most Kaikōura based fishing operations are 'trailer-launched', meaning they are effectively out of business until the remediation work has been undertaken. We understand 300 jobs have been affected by the earthquake, though only a portion of those would be related to the damage to the harbour.

Impact on lifeline capacity

5. The seabed rise has meant that the harbour is not (except around high tides) available to provide an alternative route for supplies, people and emergency response support into Kaikōura. The existing road links are tenuous and could be severed again if there were another earthquake or in poor weather.

Options for restoring Kaikōura harbour to functioning state

6. Based on initial assessment from Kaikōura District Council and Environment Canterbury there are two options:

Option 1:	Option 2:
<ul style="list-style-type: none"> • 6-month construction time • Undertakes work in sequence so that limited access to the harbour is possible during construction • \$3-5 million estimated cost 	<ul style="list-style-type: none"> • 4-month construction time • Requires harbour to be fully closed for that period – causing disruption to the limited existing lifeline capabilities and continuing the economic impact • \$3-5 million estimated cost, but much more likely to be at the lower end of that scale
<ul style="list-style-type: none"> • Both options: Scope of works limited to emergency works to deepen the channel and harbour basin to allow restored functionality.¹ 	

Recommended approach: Option 1

7. We recommend Option 1 on the basis that it strikes an appropriate balance between speed and the availability of the harbour. While it does take an extra two months, the impact of fully closing the harbour for four months would be large. Local authorities have a strong preference for Option 1.

Seeking funding in advance of detailed costings

8. Kaikōura District Council and Environment Canterbury have commissioned Tonkin and Taylor to provide a more detailed assessment of the damage to the harbour, a more definitive breakdown of the cost of repair, and options for additional future improvements. The report is due on Friday 16 December.
9. In ordinary circumstances we would not advocate making a funding decision in advance of receiving this more detailed assessment, but in this case there are good reasons to make this decision earlier:
- there is an (increased) risk of further earthquakes in the area, and the harbour is a critical lifeline – i.e. Waiting for more than absolutely necessary would needlessly put lives at risk when the outcome of the assessment is not going to change
 - every day the harbour is not functioning, local businesses are losing money and more reliant on State support – any needless delay to starting work will

¹ Note: Kaikōura District Council are prioritising the full restoration of the harbour under the Hurunui/Kaikōura Earthquake Relief Act 2016.

cost the government more money (in support payments to individuals and businesses) than a detailed report would be likely to save.

- There is also the significant potential psychosocial cost of needless delays to starting the work.
10. If the funding is made available shortly then the local authorities can use the emergency works provisions under the Kaikōura/Hurunui Earthquakes Emergency Relief Act 2016 and the Resource Management Act 1991 and the work can be started immediately.² After this window has closed the approval process would take longer.

Possible sources of existing funding

11. Kaikōura District Council is the owner of the harbour assets but they would face significant difficulty obtaining the funding for the dredging operation as they have a very limited revenue base.³
12. Advice from the Ministry of Civil Defence is that there is also no avenue for funding this work through the civil defence reimbursements for costs of emergency response and recovery. In particular, it does not fall within the criteria of “essential infrastructure repair” or of “special policy” financial assistance (the primary reason for ‘special policy’ financial assistance is to decrease the likelihood of the occurrence of a similar emergency).

The case for government financial assistance

13. We recommend that the government does provide some sort of financial support for the harbour damage as soon as possible. Our rationale is set out in appendix 2 but in summary:
- The benefits of doing this work substantially outweigh the costs, and if Government doesn’t assist, the work won’t happen, at least in the short to medium term

² The Kaikōura/Hurunui Earthquakes Emergency Relief Act effectively enables the necessary resource consents to be obtained retrospectively under a simplified process. The Act deems the harbour restoration to be a controlled activity – instead of its current status as a ‘prohibited activity’.

s9(2)(i)

- The proposed work is well supported at a local level, including by local iwi Ngati Kuri
- We do not consider this intervention creates a significant precedent effect as the nature and circumstance of this particular damage is very unusual.

Options for government financial assistance

Option	Benefits	Costs
Option 1: Fund as a grant	Simple and likely to be agreed by parties more quickly Provides faster certainty to Kaikōura business	May be unnecessary expenditure if a loan option is available Risk of costs increasing to meet funding cap
Option 2: Fund as a concessionary loan	Significantly lower cost to the Crown Council incentivised to keep costs down (though discretion on restoring the channel and harbour depth is likely to be minimal, so benefits of this are questionable)	Would be complex. May be difficult to agree terms before Christmas Bearing in mind financial constraints, may still be unmanageable even at concessionary rates
Option 3: Fund the harbour rehabilitation as a grant and explore appropriateness of using a concessionary loan mechanism for other assets that Kaikōura District Council will likely struggle to repair – for example the swimming pool	Council would be able to proceed quickly with the harbour while allowing longer discussion on other areas of damage and on how to restore the harbour beyond the basic functionality that the proposed rehabilitation work would enable	Signalling the option of concessionary loans for other damage creates some precedent risk as almost all other damage in Kaikōura is already covered by a funding regime and either has insurance or could have had insurance

Recommended approach: Option 3

14. We recommend that you agree for Kaikōura to be given a grant to undertake the harbour work. We propose that you allocate \$5 million, which is the top of the estimated price range, and that the actual costs are kept in check through the management arrangements (see below).
15. The grant would be administered through a new appropriation established in Vote Prime Minister and Cabinet, with the Minister of Civil Defence as the appropriation Minister.
16. Treasury, DPMC and DIA will also undertake work on whether there is scope for a concessionary loan to address other damaged assets. While this work does

have some urgency it is less pressing than the harbour works, and there are complexities and risks that need to be considered. As noted above, almost all other damage in Kaikōura is already covered by a funding regime and either has insurance or could have had insurance.

Governance of the project

17. To ensure adequate oversight of this project, and mitigate against the risk of cost escalation – which is a heightened concern due to making such an early stage commitment – we propose a joint governance arrangement between local and central government.
18. The parties to this governance would be
 - Environment Canterbury – which has been leading the initial phase of scoping the work, but would play a monitoring and authorising role
 - Kaikōura District Council – as the operational lead for the harbour works,
 - DPMC – as the central government representative and administrator of the funding appropriation
19. Kaikōura District Council would draw down the funding as required, following approval from Minister of Civil Defence - based on recommendations from the joint governance group.

Recommendations

It is recommended that you:

1. **agree** to spend up to \$5 million to rehabilitate the Kaikōura harbour and restore it to a functioning state
2. **agree** that the funding is by way of a grant, administered by a joint governance group of Environment Canterbury, Kaikōura District Council and the Department of Prime Minister and Cabinet
3. **agree** that Kaikōura District Council is able to draw down the funding in phases as appropriate by approval from Minister of Civil Defence based on recommendation from the joint governance group
4. **agree** to establish the following new appropriation:

Vote	Appropriation Minister	Title	Type	Scope
Prime Minister and Cabinet	Minister of Civil Defence	Rehabilitation of Kaikōura harbour	Non-Departmental Other Expense	This appropriation is limited to a contribution to the Kaikōura District Council acting on behalf of Environment Canterbury for work necessary to restore the functionality of Kaikōura Harbour

5. **approve** the following changes to appropriations to fund the rehabilitation of Kaikōura harbour, with a corresponding impact on the operating balance:

Vote Prime Minister and Cabinet Minister of Civil Defence	\$m – increase/(decrease)				
	2016/17	2017/18	2018/19	2019/20	2020/21 & Outyears
Non-Departmental Other Expense: Rehabilitation of Kaikōura Harbour (funded by revenue Crown)	5.000	-	-	-	-

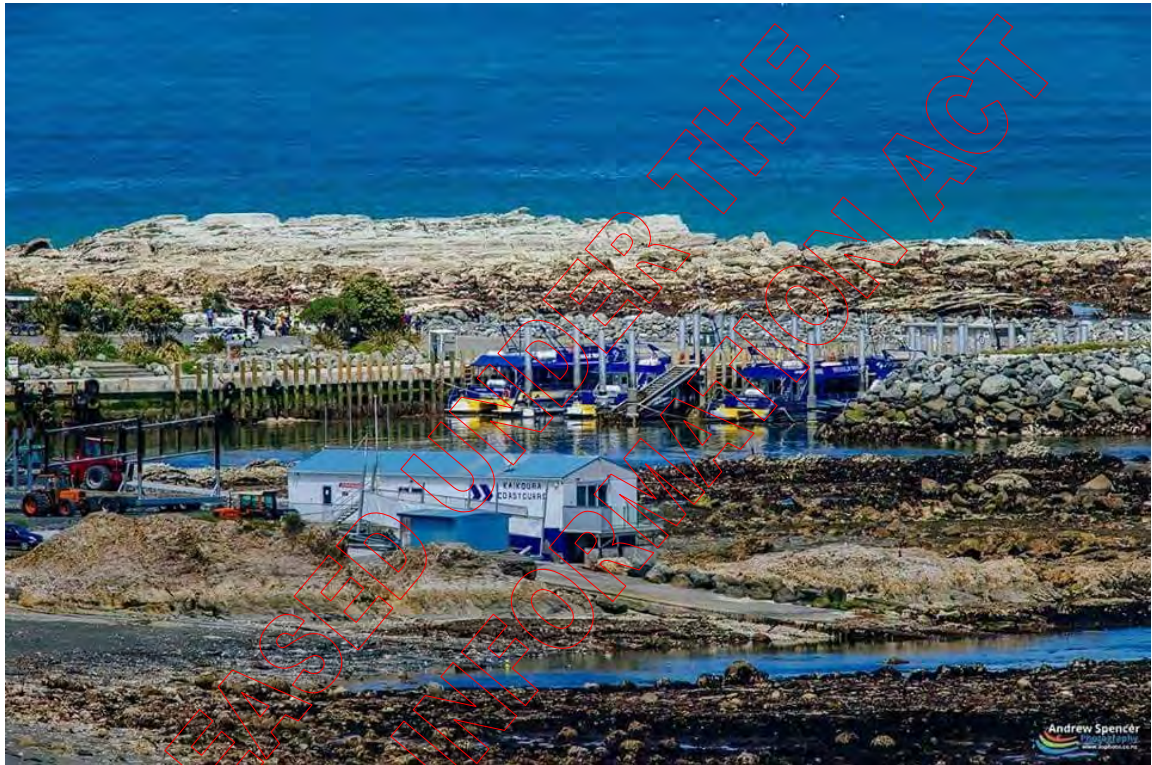
6. **agree** that the proposed changes to appropriations for 2016/17 above be included in the 2016/17 Supplementary Estimates and that, in the interim, the increase be met from Imprest Supply
7. **agree** that the expenses incurred under recommendation 5 above be a charge against the between-Budget operating contingency, established as part of Budget 2016
8. **agree** that Treasury, DPMC and DIA undertake work on whether it would be appropriate for the Crown to give a concessionary loan to Kaikōura District Council to address any other damaged assets they own

Hon Bill English
Minister of Finance

/ 12 / 2016

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Appendix 1: Harbour damage



Appendix 2: Guiding principles for Government investment in Kaikōura Earthquake Recovery

1. Does the initiative progress the Government's overall priorities?
2. Does it support local priorities?
3. Is the initiative efficient, effective and cost-effective? Is it a good use of public funds?
4. Does it increase infrastructural, social and environmental resilience, e.g. does it work towards reducing the costs and dislocation of future disasters?
5. Does the initiative inappropriately inhibit market mechanisms and signals that people should be factoring into their decisions on where to live, work and invest?
6. Are the right actors (i.e. those with the best knowledge, capacity, motivation and alignment with relevant regional or national interests) making the decisions (central or local government, individuals or market participants)?
7. Does the decision-making process appropriately balance decision speed and inclusive processes with community and stakeholder involvement?
8. What precedents and expectations will the initiative create, and are these appropriate?

Assessment against key criteria

Is the initiative efficient, effective and cost-effective? Is it a good use of public funds?

- The \$3 – 5 million cost can be seen as a justifiable investment when weighed against the significant economic impact that restoring the harbour would have on the local economy, as outlined above. It is also clear that without central government intervention the work would not proceed, at least in the short to medium term.

What precedents and expectations will the initiative create, and are these appropriate?

- Funding this initiative and considering it under such compressed timeframes would create only a very limited precedent effect. The damage is very unusual, which is evidenced by the fact that it falls outside all existing emergency funding frameworks.

- Environment Canterbury has confirmed their view that this damage does not create a precedent for future possible claims.
- Funding this initiative does create a precedent for any future similar earthquake damage to harbours. A clear example would be Wellington, where the seabed rose substantially in the 1855 Wairarapa earthquake. In circumstances, as outlined above, this limited precedent effect is justifiable.

Does the decision-making process appropriately balance decision speed and inclusive processes with community and stakeholder involvement?

- In broad discussions across the community Environment Canterbury has encountered overwhelming support for rehabilitating the harbour. While there may be minor questions about method and design all are in support of getting the harbour functional. They have gathered even more support with the proposal to maintain limited harbour access throughout the operation.
- The Chairman and CEO of Environment Canterbury and Mayor and CEO of Kaikōura District Council have both had discussions with Henare Manawatu, the Kaiwhakahaere of Ngāti Kuri, the rūnanga of Kaikōura. He and his supporting consultant have indicated their support for the harbour restoration and their acceptance of the disturbance necessary to do this.
- Essentially the area to be deepened is that of the existing harbour where deepening has occurred previously, over much of the area only 15 years ago (works undertaken by Downers). Environment Canterbury have confirmed that every attempt would be made to move kaimoana and other species from the area before deepening operations commence.

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Briefing for Cabinet on 12 December 2016

Notes:

- There is no Pre-Cab on Monday

Papers for Cabinet Consideration

Not covered by your request

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	Funding to improve the seismic performance of unreinforced masonry buildings following the Kaikoura earthquakes		
This paper seeks Cabinet agreement to establish a \$2 million fund to improve the seismic performance of unreinforced masonry (URM) buildings. This fund would assist owners of these buildings by providing up to fifty percent of the funding required up to	<table border="1"> <tr> <td data-bbox="678 1767 1141 1973">Recommendation 7 proposes delegation to joint Ministers. We do not support this delegation for any decisions that would have implications on new funding sought. For example if the areas were extended, presumably the amount required in the fund would</td> <td data-bbox="1141 1767 1461 1973">Do not support at this time - s9(2)(f)(iv) s9(2)(f)(iv)</td> </tr> </table>	Recommendation 7 proposes delegation to joint Ministers. We do not support this delegation for any decisions that would have implications on new funding sought. For example if the areas were extended, presumably the amount required in the fund would	Do not support at this time - s9(2)(f)(iv) s9(2)(f)(iv)
Recommendation 7 proposes delegation to joint Ministers. We do not support this delegation for any decisions that would have implications on new funding sought. For example if the areas were extended, presumably the amount required in the fund would	Do not support at this time - s9(2)(f)(iv) s9(2)(f)(iv)		

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Item	Title		
Description and analysis		Fiscal implications	Treasury Recommendation
<p>\$25,000 to secure vulnerable street facing fixtures of URM buildings.</p> <p>This paper does not make a strong case for urgency. Immoderate risk reduces with time and by the time grants are made and contractors engaged the heightened post Kaikoura event risk will have reduced substantially.</p> <p>Given the urgency of the paper and the risk to life that these buildings pose, is fifty percent of funding for building owners who otherwise have 15 years for the work with no additional liability enough of an incentive? We question whether the response is appropriate.</p> <p>The proposal isn't placed in context of other initiatives, several recently legislated and national risk and demand in areas beyond Greater Wellington.</p> <p>The long run effects are not identified. For example, a Government subsidy may incentivise retention/reinstatement of buildings that might otherwise be demolished and replaced by modern, safe and productive structures, or addressed by local government and MBIE under other powers and incentives.</p>	<p>also extend. This decision should be made by Cabinet/Ministers with Power to Act.</p> <p>The \$2 million requested does not seem like enough. Rough estimates show that if the 309 building owners in Wellington and the Hutt used the fund at \$25,000 per building, the costs would be almost \$8 million. The \$2 million is only 25% of this cost. The paper should provide the rationale behind only asking for \$2 million and also address whether if the areas are extended, if the costs would increase?</p>	<p>s9(2)(f)(iv)</p>	
<p>Tourism Support/marketing package for Hurunui District following the Kaikoura earthquake</p>			
<p>The paper seeks agreement to support a marketing package of \$0.350 million for the Hurunui district following the Kaikoura Earthquake.</p> <p>The paper proposes that the Crown:</p> <ul style="list-style-type: none"> • Provide up to \$250,000 to in marketing support to help the regional tourism organisation and Visit Hurunui attract Cantabrians and other tourists to visit Hurunui district. • Provide funding of up to \$100,000 for 1.5 full-time equivalent positions within the regional tourism operator through to the end of March 2017, to manage and support the short-term recovery period. <p>Recent evidence shows signs of recovery in spending levels for the Hurunui district. This suggests that Hurunui is beginning to recover</p>	<p>Proposed Crown contributions will be met through the between Budget contingency which will have a direct impact on OBEGAL.</p>	<p>Do Not Support.</p>	

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Item	Title	
Description and analysis	Fiscal implications	Treasury Recommendation
<p>and any additional spend by the Crown may not deliver the addition benefit sought and anticipated.</p> <p>Second, the Treasury has limited clarity as to the current capacity and capability of Visit Hurunui and the regional tourism organisation. Specifically, it is unclear as to whether or not this is something that can be achieved within existing or additional resourcing of Visit Hurunui and the regional tourism organisation.</p>		

Oral items

- Not covered by your request
- Kaikoura tourism
- Kaikoura Earthquake - Support for rehabilitating Kaikoura Harbour (briefing attached.)

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IN-CONFIDENCE**Talking points for Cabinet: Kaikoura Earthquake: Support for rehabilitating Kaikoura Harbour**

- This paper seeks approval for the Crown to give Kaikoura District Council funding of up \$5 million to restore the Kaikoura Harbour to a functioning state.
- Following the earthquake the seabed rose between 1 and 2 metres, meaning boats can now only launch in a 2 hour window around high tide.
- This has in practice stopped many of the major tourism activities that are critical to the Kaikoura economy, such as whale watching, and also stopped local commercial fishing – which is almost solely trailer launched.
- The harbour is also not able to be used effectively as an alternative lifeline utility, which is important bearing in mind the fragility of the roads.
- Practically, if funding is secured I understand work could begin within 5 working days, using the emergency recovery provisions. I am proposing that the work would be undertaken over six months, which would allow the harbour to stay open during that time. A four month option would require the harbour to be closed.
- The Kaikoura District Council does not have the financial capacity to fund the restoration itself, bearing in mind its low rating base and other earthquake pressures.
- The paper notes there is the option of offering a concessionary loan to Kaikoura District Council instead of a grant. The two key downside to this are that:
 - it would take some time to agree the terms and there are real benefits to moving quickly on this
 - the Council may not be able to service the loan, even at concessionary rates, bearing in mind their financial position.
- The paper does seek approval for officials to explore whether it would be appropriate for a concessionary loan to be granted for other damaged assets – though taking into account the precedent and moral hazard risks
- To minimise risks around improper expenditure on the harbour restoration, I am proposing that the funding is governed through a Joint governance arrangement – ECAN, Kaikoura District Council, and the Government (DPMC) – with funding drawn down in tranches, requiring approval of Minister of Civil Defence.
- ECAN and Kaikoura District Council are supportive of the approach in this paper and have noted widespread local support for restoring the harbour, in particular if harbour is kept open during repairs.
- ECAN and Kaikoura District Council have also consulted with Henare Manawatu, the Kaiwhakahaere of Ngāti Kuri, the rūnanga of Kaikōura, who is also supportive of restoring the harbour.

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[IN-CONFIDENCE] Title	Description and analysis	Fiscal implications	Treasury recommendation
<p>Kaikoura Earthquake: Support for rehabilitating Kaikoura Harbour</p>	<p>This paper seeks approval for the Crown to give Kaikoura District Council funding of up \$5 million to restore the Kaikoura Harbour to a functioning state</p> <p>The earthquake has caused the seabed to rise 1-2 meters, meaning the harbour can only be used for two hours around high tide. This has caused ongoing damage to the tourism and fishing industries, as well as removing the harbour as a lifeline utility.</p> <p>Kaikoura District Council is not able to finance the restoration and there are key benefits from moving quickly, which discounts a concessionary loan arrangement.</p>	<p>Proposed Crown contribution will be met through the between Budget contingency which will have a direct impact on OBEGAL.</p>	<p>Support</p> <p>To minimise risks around improper expenditure the funding would be governed through a Joint governance arrangement – ECAN, Kaikoura District Council, and the Government (DPMC) – with funding drawn down in tranches, requiring approval of Minister of Civil Defence</p>

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Treasury Report: s9(2)(f)(iv)

Date:	20 December 2016	Report No:	T2016/2514
		File Number:	CM-1-3-15

Action Sought

	Action Sought	Deadline
Minister of Finance (Steven Joyce)	note the report and provide feedback prior to the deadline.	Saturday, 31 January 2017
Minister Responsible for the Earthquake Commission (Hon Gerry Brownlee)	note the report and provide feedback prior to the deadline.	Saturday, 31 January 2017

Contact for Telephone Discussion (if required)

Name	Position	Telephone	1st Contact
Bradley Woods	Senior Analyst, Commercial Operations – Strategy and Policy	+64 4 917 6269 (wk)	s9(2)(a)
Andrew Hagan	Head of DMO Risk Policy & Balance Sheet	+64 4 917 6937 (wk)	✓
Craig Weise	Manager, Commercial Operations – Strategy and Policy	+64 4 917 6149 (wk)	

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

Return the signed report to Treasury.

Note any feedback on the quality of the report

Page 2 not covered by your request

Enclosure: No

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Recommended Action

We recommend that you:

- a **note** the report and provide any feedback that you may have

Craig Weise
Manager, Commercial Operations – Strategy and Policy

Steven Joyce
Minister of Finance

Hon Gerry Brownlee
Minister Responsible for the Earthquake Commission

Page 4 not covered by your request

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8. Not covered by your request

9.

Kaikoura Earthquake

10. The recent Kaikoura earthquake has triggered further claims on EQC under the scheme. Prior to this event EQC had a negative balance sheet equity position but it had not had to draw on the guarantee by using ongoing levy income and the remnants of the NDF to meet its obligations.

11. A letter written by Minister English to EQC stating that the Crown intended to fulfil his obligation to ensure that the EQC can meet all its liabilities as they fall due (refer T2011/2050) is referenced by EQC in its financial statements, in relation to EQC's negative equity position.

12. s9(2)(f)(iv), and s9(2)(j)

13. Looking forward, EQC continues to underwrite risk from new events under the scheme. With depleted financial resources to meet any new claims activity and/or to fund reinsurance procurement or self-insure, the likelihood of further calls on the Crown guarantee are likely. Left unaddressed this could result in unnecessary guarantee "churn", as both EQC and the Crown incur continued overhead dealing with repeated guarantee calls.

Not covered by your request

s9(2)(f)(iv)

Remainder of document not covered by your request

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Pre-Cab Briefing 20 December 2016

Notes:

- Pre-Cab is at 12.30pm on 20 December.

Papers for Cabinet Consideration

Item	Title	
Description and analysis	Fiscal implications	Treasury Recommendation
Not covered by your request		
6	Regulatory modifications and funding to improve the seismic performance of unreinforced masonry (URM) buildings following the Kaikōura earthquakes	
<p>An earlier version of this paper was considered at EGI on 14th December. The Minister for Building and Housing was invited to come back to Cabinet on 20th December.</p> <p>Note that this briefing has been prepared having only seen a draft of the revised paper with under an hour to provide comments.</p> <p>This revised paper proposes to develop an Order in Council under the Hurunui/Kaikoura Earthquakes Recovery Act 2016 to amend the Building Act 2004 to mandate the strengthening of unreinforced masonry (URM) buildings in certain areas with a heightened risk of earthquakes (Wellington, Lower Hutt and Blenheim) to secure their street facing facades and parapets within 12 months. The paper proposes modifications to the Building Act 2004 and the Resource Management Act 1993 to expedite timeframes given the risk to public safety. This paper also seeks Cabinet agreement to establish a \$3 million fund to help building owners meet the costs associated with the new requirements. This fund would assist building owners by providing up to fifty percent of the funding required up to \$25,000 to secure vulnerable street facing fixtures of URM buildings.</p> <p>Analysis:</p> <p>There is a precedent risk associated with establishing this fund and mandating the strengthening work. These risks have not been considered in the paper.</p>	<p>The fiscal costs proposed in the paper do not look adequate. Rough estimates show that if the 334 building owners in Wellington, Lower Hutt and Blenheim used the fund at \$25,000 per building, the costs would be over \$8 million. The volumes noted in the paper suggest that the \$3 million fund would be oversubscribed.</p> <p>This paper is seeking \$3 million from the Between Budget Contingency (BBC) to cover the costs of establishing the fund. Because the BBC is exhausted for 16/17 this will have an effect on OBEGAL.</p>	<p>Partial support – we recommend supporting the proposed Order in Council. However, we do not support the establishment of a \$3 million fund on the terms outlined in the paper.</p> <p>We recommend that the fund should be available on application and means tested in line with other earthquake support packages. We also recommend that the amount of the fund be revised to better meet demand.</p>

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Item	Title	
Description and analysis	Fiscal implications	Treasury Recommendation
<p>The proposal isn't placed in context of other initiatives (e.g. the Heritage Equip funding), several recently legislated, and national risk and demand in areas beyond Greater Wellington</p> <p>s9(2)(f)(iv)</p> <p>The long run effects are not identified. For example, a Government subsidy may incentivise retention/reinstatement of buildings that might otherwise be demolished and replaced by modern, safe and productive structures, or addressed by local government and MBIE under other powers and initiatives.</p> <p>The paper does not consider alternative funding options, such as means testing those eligible for assistance, or consider other business support packages that are available to building owners or tenants. Several of these owners may be large property investors, supported by major banks, raising the issue of moral hazard in providing subsidies.</p> <p>A RIS has not been prepared for this Cabinet Paper due to the urgency of the paper.</p>		

Not covered by your request

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Item	Title
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Not covered by your request



Oral Items

- SH1/Kaikoura (Bridges)

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**Treasury Report: The Crown Guarantee**

Date:	20 December 2016	Report No:	T2016/2487
		File Number:	CM-1-3-15

Action Sought

	Action Sought	Deadline
Minister of Finance (Steven Joyce)	s9(2)(f)(iv)	Tuesday, 10 January 2017
Minister Responsible for the Earthquake Commission (Hon Gerry Brownlee)		Tuesday, 10 January 2017

Contact for Telephone Discussion (if required)

Name	Position	Telephone	1st Contact
Bradley Woods	Senior Analyst, Commercial Operations – Strategy and Policy	+64 4 917 6093 (wk)	s9(2)(a)
Craig Weise	Manager, Commercial Operations – Strategy and Policy	+64 4 917 6149 (wk)	✓

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

Return the signed report to Treasury.

Note any
feedback on
the quality of
the report

Enclosure: No

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Treasury Report: The Crown Guarantee

Executive Summary

As a result of the Kaikoura/Culverden earthquakes, the Earthquake Commission (EQC) are forecast to potentially exhaust their cash assets in s9(2)(i) here are three options available to Ministers for meeting this asset deficiency under the Earthquake Commission Act 1993 (the EQC Act):

- **An Operating Grant** - made to EQC under the permanent appropriation authority of section 16 of the EQC Act that would not be required to be repaid. (*Equity Equivalent*)
- **An Advance** - given to EQC under the permanent appropriation authority of section 16 of the EQC Act that would be repayable from its future operating surpluses. (*Debt*)
- **A Capital Grant** - established via an annual appropriation authority that would facilitate the purchase of EQC share capital by the Crown as permitted under section 7 of the EQC Act. (*Equity*)

s9(2)(f)(iv)

Beyond these considerations, analysis of EQC's forecast cash flows and a timetable for funding resolution are presented.

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Recommended Action

We recommend that you:

a **note** the timing of the forecast EQC asset deficiency in this paper

and

b s9(2)(f)(iv) [Redacted]

Agree/disagree.
Minister of Finance

Agree/disagree.
Minister Responsible for the
Earthquake Commission

or

c s9(2)(f)(iv) [Redacted]

Agree/disagree.
Minister of Finance

Agree/disagree.
Minister Responsible for the
Earthquake Commission

Craig Weise
Manager, Commercial Operations – Strategy and Policy

Steven Joyce
Minister of Finance

Hon Gerry Brownlee
Minister Responsible for the Earthquake Commission

IN-CONFIDENCE**Treasury Report: The Crown Guarantee**

Purpose of Report

1. The purpose of this report is to detail the options available to Ministers for meeting the forecast asset deficiency of the Earthquake Commission (EQC). Solutions under section 16 (the Crown Guarantee) of the Earthquake Commission Act 1993 (the EQC Act) are explored along with a possible section 7 intervention (capital grant). An update on the expected quantum and timing of EQC's asset deficiency is also provided.

Background

Section 16

2. Section 16 of the EQC Act, sets out the obligation of the Crown to fund any deficiency in the assets of EQC:

"If the assets of the Commission (including the money for the time being in the Fund) are not sufficient to meet the liabilities of the Commission, the Minister shall, without further appropriation than this section, provide to the Commission out of public money such sums by way of grant or advance as may be necessary to meet the deficiency upon such terms and conditions as the Minister determines."

3. s9(2)(h)

4. As a result, on 29 September 2011 the Minister of Finance wrote to the Chair of EQC stating that the Minister would fulfil the obligation under section 16 to meet the liabilities of the Commission as they fall due. That is, on a cash flow rather than balance sheet basis. Since that time EQC has run a negative equity position and has not required additional funding to meet its cash flow obligations.

Section 17

5. Under section 17 of the EQC Act, in return for the Crown Guarantee, EQC must pay a guarantee fee to the Crown that is "determined from time to time by the Minister". This fee is intended to compensate the Crown (taxpayers) for the risk of providing funds to EQC to meet its liabilities. If this fee is appropriately priced, it will ensure that catastrophe risk covered by EQC is being fairly shared between tax payers and levy payers. That is, taxpayers are not subsidising the levy payers or vice versa.
6. A complicating factor in setting the guarantee fee at an appropriate risk-priced level is that the EQC Act is ambiguous as to whether the fee is in return for a grant or an advance. Currently, under section 16 of the Act, the guarantee can take either form at the Minister's discretion. Officials have considered this issue and believe that the Crown guarantee fee paid by EQC to date is consistent with the provision of a grant. That is, in paying the guarantee fee, EQC have been essentially paying a reinsurance

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premium for the Crown to reinsure its residual risks that are not covered by the NDF or its reinsurance programme.

7. This view also accords with Treasury conversations with Mr David Middleton, ex-Chief Executive Officer of the EQC (between January 1993 and March 2010) whom indicated that EQC's view, both at the time of implementation of the guarantee and subsequently, was that the guarantee was akin to a further layer of reinsurance.
8. As originally envisioned, the guarantee fee was seen as a key mechanism for transmitting total Crown risk appetite signals to EQC. However, since 1998 the guarantee fee has remained unchanged at \$10m per annum despite significant changes in the Crown's fiscal position, Crown risk tolerance and EQC's balance sheet.

s9(2)(f)(iv)

Guarantee Options

9. There are three options for meeting an asset deficiency within the EQC Act.

An Advance (repayable)

10. An advance represents a loan from the Crown to EQC that would be repayable from its future operating surpluses. It would be provided to cover EQC's asset deficiency as cash was required and could include any conditions the Minister sees fit to impose, e.g. an interest rate, maximum loan tenor, fixed repayment timetable. How the cost was shared between taxpayers and levy payers, and how fast the NDF replenished, would depend on whether the EQC levy is adjusted upwards to repay the advance.
11. If the levy was not adjusted upwards to repay the advance, the advance would be economically equivalent to a grant. That is, the advance would not change the sharing of costs and risks between EQC policy holders and taxpayers. Repaying the advance would simply suppress the recovery of the NDF balances, opening the Crown to an offsetting increase in the potential future exposure associated with the Crown Guarantee. For reporting and budget purposes, however, it would still be treated as an advance if repaid within 10 years i.e. it would not count against budget allowances.
12. It should be noted that EQCover premiums currently are not set with regard to having to cover the burdens imposed by an advance such as interest. Consequently, the only mechanism EQC would have of meeting the costs of an advance post-event would be a levy increase. Failing this, Crown net debt would be higher forever.
13. If the levy was adjusted upwards, the cost of the advance would be fully borne by levy payers. Net debt would increase initially as the advance was drawn but would then decline over time as EQC made repayments, ultimately resulting in a fiscally neutral outcome. An increased levy would reduce the delay before the NDF replenished and would also flow through to an increase in OBEGAL and the operating balance.
14. Despite these advantages, it should be stressed that levy payers would effectively be paying twice for the guarantee with an advance if the levies were increased. Officials are strongly supportive of a levy that is appropriately risk-priced and incorporates all relevant long run costs of the EQC scheme. In principle, this means the levy should only be changed to reflect and incorporate new information on the appropriate long run costs and risks of the scheme. s9(2)(f)(iv)

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15. As detailed in paragraph 7 above, an advance with a levy increase is inconsistent with official's view that EQC has historically paid a guarantee fee that is commensurate with a grant from the Crown. A further issue with an advance lies in determining what an appropriate repayment period for the advance might be. Assuming levies were increased to repay the advance, having a short repayment period would impose a higher burden on current, rather than future, levy payers. Conversely, the longer the repayment period, the more the outcome would resemble the outcome of a grant. That is, having little impact on current levy payers or the future level of levies.

An Operating Grant (non-repayable)

16. In contrast with the foregoing, under an operating grant, the asset deficiency would be funded entirely by taxpayers and would not need to be repaid by EQC. That is, levy payers would not be paying twice for the guarantee as in the case of an advance. Although this would result in an increase in net debt initially, over the long term net debt would be unaffected if the guarantee was fairly priced. That is, guarantee fees would offset the guarantee provision.
17. Whilst OBEGAL would not be effected by the provision of an operating grant, as it is simply a transaction within the government reporting entity, it is an open question as to whether Ministers would "count" it against budget allowances. Traditionally, any grant would be counted given the effect on net debt. However, given section 16 is a permanent legislative authority that does not require a new appropriation, Ministers may decide against this.
18. Beyond these advantages, an operating grant would avoid the issues associated with repayment timeframes and ongoing administration associated with an advance. It would also facilitate more rapid replenishment of NDF balances from EQC operating surpluses and align with official's view that, historically, the guarantee fee paid by EQC is more consistent with a grant being provided.

A Capital Grant (non-repayable)

19. Under section 7 of the EQC Act, the Government may contribute equity to EQC. Compared to an operating grant or an advance payable under section 16, an amount larger than the estimated liability deficiency could be paid. That is, a capital grant is the only mechanism for reseeding the NDF under the EQC Act, beyond the accumulation of operating surpluses which an operating grant and an advance may impact only tangentially.
20. The fiscal effects of a capital grant are the same as an operating grant, however, a capital grant would need to be appropriated via a budget bid, and thus require cabinet approval. In contrast, an operating grant or advance could be provided immediately under the permanent legislative authority established by section 16 of the EQC Act.
21. To facilitate a capital grant before the forecast cash flow deficiency eventuates s9(2)(f)(iv) and s9(2)(i) see below) would incur significant administrative burden given the advanced stage of the current budget process. It would also introduce undesirable uncertainty for EQC in terms of its ability to effectively plan and discharge its obligations. Although it might be argued this burden is worthwhile to achieve the greater oversight and control of spend that an appropriation structure allows, it should be noted that both an operating grant and an advance can be structured in such a way to achieve similar ends.
22. In the case of Southern Response, for instance, the Crown has utilised a combination of a capital grant (preference shares) and an operating grant (callable cash facility) to meet claims liabilities. The latter has been set such that every quarter the liability estimate is updated and further provisioning provided via a delegation to Treasury officials. This has the advantage of limiting the potential for overcapitalisation, ensures

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appropriate oversight of claims disbursements and avoids the need to revisit a cabinet process to secure additional funding. It also provides certainty to Southern Response on its funding whilst balancing Crown considerations around the timing and cost of capital provision.

Option Summary

23. The table below compares the three options against various considerations.

	ADVANCE	OPERATING GRANT	CAPITAL GRANT
Fairness	Unfair if levies are increased	Fair	Fair
Consistency with Guarantee Fee Payment	Inconsistent	Consistent	Consistent
NDF Replenishment	Only possible via impact on operational surpluses s9(2)(f)(iv)	Only possible via impact on operational surpluses s9(2)(f)(iv)	Full replenishment possible without need to rely on operational surpluses
Control over Disbursement	All options can be structured to allow appropriate oversight and disbursement control		
Administrative Burden	High	Low	Highest
Net Debt	s9(2)(f)(iv)	Increased initially but unaffected over the long term if the guarantee fee is appropriately priced	Increased initially but unaffected over the long term if the guarantee fee is appropriately priced and/or s9(2)(f)(iv)
Budget Allowances	s9(2)(f)(iv)	Potentially lowered	Potentially lowered
OBEGAL	s9(2)(f)(iv)	Unchanged	Unchanged

Remainder of document withheld under s9(2)(f)(iv) and/or S9(2)(i) and/or s9(2)(j)

BUDGET-SENSITIVE



Treasury Report: Budget 2017 - Initial Budget Initiatives and Business-As-Usual Pressures

Date:	21 December 2016	Report No:	T2016/2530
		File Number:	BM-2

Action Sought

	Action Sought	Deadline
Minister of Finance (Hon Steven Joyce)	Not covered by your request	10 January 2017

Contact for Telephone Discussion (if required)

Name	Position	Telephone	1st Contact
s9(2)(g)(i)			✓
Kamlesh Patel	Team Leader, Budget Coordination	04 917 6094 (wk)	N/A (mob)

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

Return the signed report to Treasury.

Note any feedback on the quality of the report

Enclosure: Yes

BUDGET-SENSITIVE

Treasury Report: Budget 2017 - Initial Budget Initiatives and
Business-As-Usual Pressures

Executive Summary

Not covered by your request



BUDGET-SENSITIVE

Not covered by your request



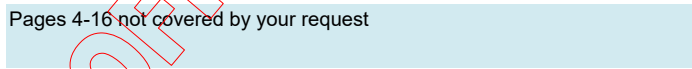
Our initial analysis of Budget initiatives suggest that there are minimal bids received to date in relation to the Kaikōura earthquakes. There are likely to be both urgent funding proposals which will require consideration by Recovery Ministers, and proposals for Budget 2017 which relate to earthquake recovery and response.

Fiscal costs following the Kaikōura earthquakes are likely to put additional pressures on Budget 2017 allowances. The fiscal forecasts in HYEPU included an impact of a net \$1 billion, but decisions and new information about costs is likely to revise this number higher ahead of Budget 2017.

Not covered by your request



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Potential implications of the Kaikōura earthquakes

- 38. Treasury’s preliminary estimates from HYEFU of the fiscal impact of the earthquakes was around \$2 to \$3 billion as at 21 November. There remains a significant level of uncertainty around these estimates. The HYEFU also included an incremental net cost of \$1 billion to fund earthquake response and recovery (e.g. after reprioritisation and insurance proceeds), although this did not represent a funding envelope.
- 39. In the wake of the 14 November earthquake, Ministers have approved funding for a number of proposals relating to response and recovery. There are likely to be both urgent funding proposals which will require consideration by Ministers, and proposals for Budget 2017 which relate to earthquake recovery and response.

Transport Implications

- 40. On Monday 5 December, Cabinet agreed to rebuild and improve State Highway 1 and the main trunk rail line along the current coastal route, with improvements for safety and resilience of the route, at an estimated cost in the range of \$1.4 billion to \$2.0 billion (CAB-16-MIN-0675 refers). The Crown contribution to the State Highway 1 reinstatement will be confirmed as part of the Budget 2017 process.
- 41. In order to continue with the required works for the SH1 reinstatement project

s9(2)(i)



s9(2)(i)




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s9(2)(f)(iv)

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