2016 BUDGET

Fiscal Strategy Report

Hon Bill English, Minister of Finance

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Guide to the Budget Documents

A number of documents are released on Budget day. The purpose of these documents is to provide information about the Government's spending intentions for the year ahead and the wider fiscal and economic picture. The documents released on Budget day are as follows:

Budget at a Glance

The *Budget at a Glance* is the overview of all the Budget information and contains the main points for the media and public. This summarises the Government's spending decisions and key issues raised in the *Budget Speech*, the *Fiscal Strategy Report*, and the *Budget Economic and Fiscal Update*.

Budget Speech

The *Budget Speech* is the Budget Statement the Minister of Finance delivers at the start of Parliament's Budget debate. The Budget Statement generally focuses on the overall fiscal and economic position, the Government's policy priorities and how those priorities will be funded.

Summary of Budget Initiatives

The *Summary of Budget Initiatives* lists and describes the new initiatives included in Budget 2016.

Fiscal Strategy Report

The *Fiscal Strategy Report* sets out the Government's fiscal strategy in areas such as the balance between operating revenues and expenses, and its debt objectives. The report includes the Government's long-term fiscal objectives and short-term fiscal intentions plus fiscal trends covering at least the next 10 years.

The Government must explain changes in the *Fiscal Strategy Report* from the *Budget Policy Statement* and the previous year's *Fiscal Strategy Report* and any inconsistencies between these documents.

Budget Economic and Fiscal Update

The *Update* includes Treasury's economic forecasts and the forecast financial statements of the Government incorporating the financial implications of Government decisions and other information relevant to the fiscal and economic outlook.

The Estimates of Appropriations

The *Estimates* outlines for the financial year about to start (the Budget year) expenses and capital expenditure the Government plans to incur on specified areas within each Vote, and capital injections it plans to make to individual departments. The *Estimates* is organised into 10 sector volumes, with each Vote allocated to one sector. Supporting information in the *Estimates* summarises the new policy initiatives and trend information for each Vote and provides information on what is intended to be achieved with each appropriation in a Vote and how performance against each appropriation will be assessed and reported on after the end of the Budget year.

Also released on Budget day:

The Supplementary Estimates of Appropriations

The *Supplementary Estimates* outlines the additional expenses, capital expenditure and capital injections to departments required for the financial year about to end. Supporting information for each Vote provides reasons for the changes to appropriations during the year, related changes in performance information and full performance information for new appropriations.

To download these documents and explore additional interactive content visit **www.budget.govt.nz**

Fiscal Strategy Report

Summary

The Crown's books are in good shape and the outlook for the economy is positive.

The operating balance before gains and losses (OBEGAL) is broadly in balance and is expected to grow significantly over the next few years. Net debt peaks as a percentage of gross domestic product (GDP) next year before falling to around 20 per cent of GDP in 2020 and around 8 per cent of GDP in 2026. Core Crown expenses fall to 29.7 per cent of GDP in 2015/16 and continue to decline over the forecast and projection periods. This outlook is consistent with the Government's short-term intentions and long-term objectives.

The operating allowance for Budget 2016 has been raised to $1.6 billion, which is more than offset by a reduction in the Budget 2017 allowance to $1.5 billion.

Budget 2016 provides for a significant increase in capital spending, although much of this will be funded through reprioritisation within the Crown's balance sheet.

Overall, the adjustments to the operating and capital allowances ensure the Government remains on track to achieve its debt objective.

While focused on responsible fiscal management, the Government will continue to invest in public services to get better results for New Zealanders, meet its net capital requirements and invest in infrastructure.

Fiscal Performance

The New Zealand economy entered recession in early 2008 and was subsequently hit by the global financial crisis. Fiscal projections, prepared in early 2009, showed that if there was no policy response net debt would increase to over 50 per cent of GDP within 10 years.

The incoming Government's response was to support the economy in the short term by running operating deficits. However, it also began to make well-considered spending changes that would bring the operating balance back to surplus and gradually reduce debt to more prudent levels.

Budget operating allowances were reduced, efficiency savings were made across the public sector and specific programmes were altered to control long-term costs. Government agencies focused on working together to achieve results under an assumption of limited new funding. Significant tax changes were introduced in a fiscally-neutral package. Contributions to the New Zealand Superannuation (NZS) Fund were suspended and capital was reallocated from within the Crown's balance sheet.

In 2010/11, following the Canterbury earthquakes, the operating deficit reached a peak of $18.4 billion, or 9 per cent of GDP. By 2014/15, however, OBEGAL was showing a small surplus, in line with the Government's stated goal. Net debt increased by the equivalent of 20 per cent of GDP between 2007/08 and 2012/13 but has now plateaued and is expected to start falling relative to GDP after 2016/17 as surpluses grow more strongly.

Economic Context

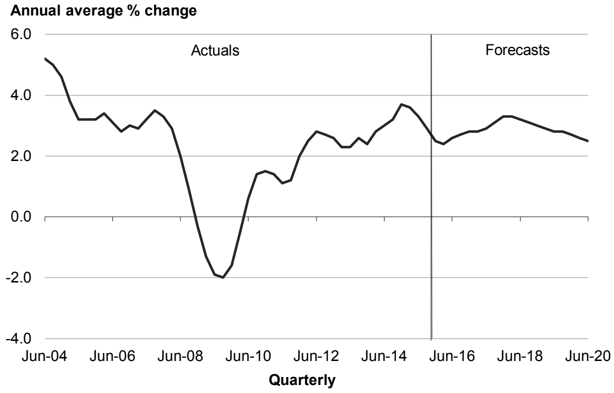
The outlook for the economy is positive (Table 1). Latest GDP figures show real GDP grew 2.5 per cent in the year ended December 2015, a little stronger than anticipated in the Treasury's *Half Year Update*.

The Treasury's *Budget Update* forecasts real GDP growth of around 2.9 per cent over the coming year, and 2.8 per cent on average over the five years to June 2020 (Figure 1). This period of growth is expected to reduce the unemployment rate to below 5 per cent in 2018.

Consumer spending and services exports are two key factors driving economic growth, supported by ongoing strength in net migration and tourism. Further impetus is apparent in a large pipeline of construction projects, and low interest rates should continue to stimulate spending and investment activity.

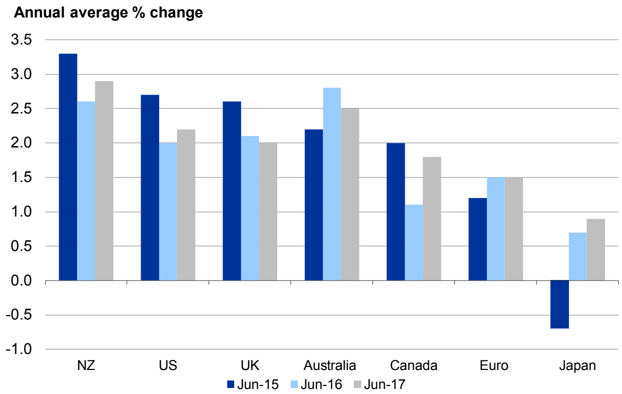
Global trading conditions, however, remain challenging (Figure 2). The outlook for trading partner growth has deteriorated since the *Half Year Update* in December and export commodity prices, particularly for dairy products, remain soft.

Figure 1 – Real GDP growth



Sources: Statistics New Zealand, the Treasury

Figure 2 – New Zealand and trading partner GDP growth



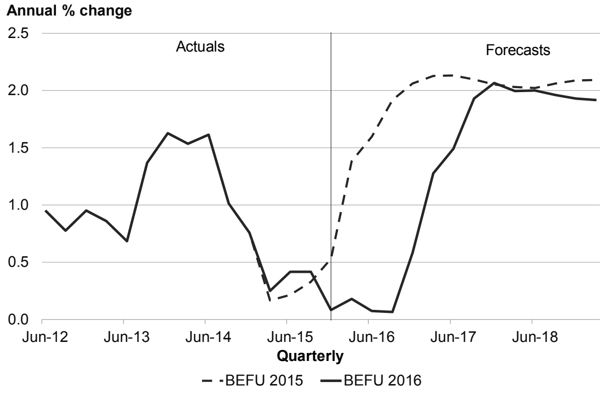
Sources: IMF, the Treasury

Inflation is currently low but is forecast to reach 2 per cent in 2017 (Figure 3).

The pace of real GDP growth over the second half of 2015 has contributed to a significantly higher level of nominal GDP and tax revenue than was expected in the *Half Year Update* (Figure 4). Compared to the *Half Year Update*, nominal GDP is forecast to be a cumulative $17.3 billion higher over the five years to June 2020.

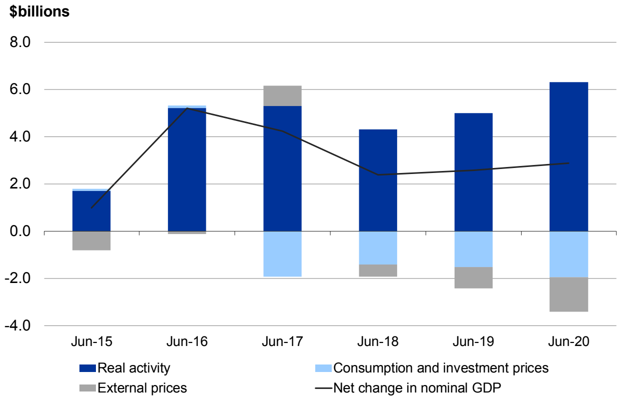
As usual, there are many uncertainties and risks around this outlook. A number of these are external and beyond the direct reach of New Zealand policy-makers, reinforcing the need for prudent fiscal policy. There are ongoing questions about China's transition to consumption and service sector growth, and many countries are struggling to exit the low-growth, low-inflation path they have experienced since the global financial crisis. The magnitude of New Zealand's net migration inflows, house price inflation and construction cycle could also differ from those assumed in the forecasts.

Figure 3 – CPI inflation



Sources: Statistics New Zealand, the Treasury

Figure 4 – Change in nominal GDP since the *Half Year Update*



Sources: Statistics New Zealand, the Treasury

Table 1 – Summary of the Treasury's Economic Forecasts in the *Budget Update*

June years	**2015 Actual**	**2016 Forecast**	**2017 Forecast**	**2018 Forecast**	**2019 Forecast**	**2020 Forecast**
Real GDP growth (annual average % change)	3.3	2.6	2.9	3.2	2.8	2.5
Consumers price inflation (annual % change)	0.4	0.1	1.5	2.0	1.9	2.1
Unemployment rate (June quarter)	5.9	5.6	5.6	5.1	4.6	4.6
Current account (% of GDP)	-3.5	-3.5	-4.6	-4.1	-4.3	-4.8

Sources: Statistics New Zealand, the Treasury

The Government's Fiscal Priorities

The Government's long-term fiscal objectives are to have net government debt between 0 per cent and 20 per cent of GDP, core Crown expenses below 30 per cent of GDP and operating balances sufficient to meet net capital requirements, including NZS Fund contributions.

Delivering on the debt objective will put New Zealand in a good position to cope with economic shocks and natural disasters, maintain credibility with international lenders and reduce the fiscal burden on future generations. The objective for core Crown expenses ensures government spending is kept to a moderate level, doesn't place excessive demands on taxpayers and allows other sectors of the economy to grow.

Consistent with the long-term objectives, the Government's shorter-term fiscal priorities are:

- maintaining rising OBEGAL surpluses over the forecast period so that cash surpluses are generated and net debt begins to reduce in dollar terms
- reducing net debt to around 20 per cent of GDP in 2020
- if economic and fiscal conditions allow, beginning to reduce income taxes, and
- using any further fiscal headroom – including from positive revenue surprises – to reduce net debt faster.

Another priority mentioned in the *Budget Policy Statement* was to implement a new funding policy for the Accident Compensation Corporation (ACC). This policy has now been confirmed, and will inform ACC's levy consultation later this year. These policy changes follow a period of ACC levy reductions and after 1 July 2016 employers, workers and motor vehicle owners in total will be paying close to $2 billion less in ACC levies than they were five years ago.

Operating allowances have been rearranged since the *Budget Policy Statement* (Table 2).

Table 2 – Operating allowances

$billions	**Budget 2016**	**Budget 2017**	**Budget 2018**	**Budget 2019**	**Budget 2020**
Operating allowances *Half Year Update*	1.0	2.5	1.5	1.5	1.6
Operating allowances *Budget Update*	1.6	1.5	1.5	1.5	1.5

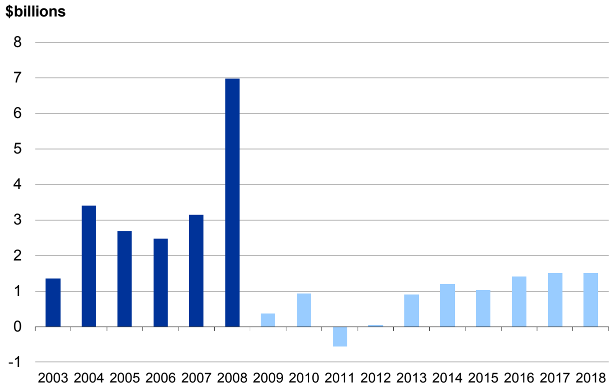
Source: The Treasury

A portion of spending previously earmarked for Budget 2017 has been brought forward into Budget 2016, in part to recognise that higher-than-expected population growth is putting pressure on health, education and other budgets. The increased Budget 2016 allowance also provides funding for key public services such as health and child protection, and investment in productivity-enhancing initiatives in areas such as tax and innovation.

Another portion of spending previously earmarked for Budget 2017 has been used to reduce net debt to help reach the 2020 debt target.

The operating allowances remain well below those adopted in the mid-2000s (Figure 5).

Figure 5 – New operating allowances in each Budget (final-year impact)



Source: The Treasury

New capital spending for Budget 2016 has been set at $1.4 billion, slightly lower than anticipated in the *Budget Policy Statement*. However, in addition, significant new capital spending will be funded from reprioritising capital within the Crown's balance sheet. As a result, total new spending on capital in this year's Budget is one of the largest new investment in the past 10 years, at $2.6 billion. This new investment is focused on core public infrastructure such as schools and transport.

For subsequent Budgets in the forecast period, the capital allowance will be set at $900 million.

These changes to the allowances will reduce spending by around $1.2 billion over the next five years, helping to further reduce debt and meet the Government's net debt targets.

A key part of the Government's fiscal strategy is managing pressures through reducing demand and better management of capital. This requires the connection of active risk management with future forecasts and projections.

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 who have faced fiscal drag as their incomes continue to rise. However, reducing debt is currently a higher priority than reducing revenue. The Government is also cautious given the wide band of uncertainty around economic and fiscal forecasts. The new operating allowances mean there isn't an explicit provision for tax cuts in the forecasts, but the Government will continue to consider options around lowering tax rates or thresholds – either in Budget 2017 or after – if the fiscal situation improves further.

Budget 2016 forecasts are consistent with the Government's short-term intentions. Operating surpluses are expected to rise, cash surpluses are forecast from 2018/19 and net debt is projected to be 19.3 per cent of GDP in 2020/21. Core Crown expenses fall to 29.7 per cent of GDP this year and stay under 30 per cent thereafter.

Forecasts, however, are uncertain and are revised every six months. The Government's fiscal strategy takes a medium-term approach to economic and fiscal management, looking through temporary ups and downs and focusing on the overall path of the Crown's finances.

The impact of discretionary fiscal policy is expected to be broadly neutral on average over the forecast period. While the Government does not actively use fiscal policy as a stabilisation tool, it does take into account the impact of fiscal policy decisions on monetary policy.

The Government's short-term fiscal intentions and long-term fiscal objectives are set out formally in Annex 1.

Fiscal Forecasts and Projections

For Budget 2016, fiscal forecasts have been prepared for the period 2015/16 to 2019/20 (Table 3). Longer-term projections have been prepared out to 2029/30 (Annex Table A1.4).

Table 3 – Summary of the Treasury's fiscal forecasts in the *Budget Update*

Year ended 30 June	2015 Actual	2016 Forecast	2017 Forecast	2018 Forecast	2019 Forecast	2020 Forecast
$billions						
Total Crown OBEGAL[1]	0.4	0.7	0.7	2.5	5.0	6.7
Core Crown residual cash	-1.8	-2.1	-4.2	-2.1	2.0	3.9
Net core Crown debt[2]	60.6	62.3	66.3	68.3	66.3	62.3
Net worth attributable to the Crown	86.5	83.5	86.6	91.6	99.3	108.9
% of GDP						
Total Crown OBEGAL[1]	0.2	0.3	0.3	0.9	1.7	2.2
Core Crown residual cash	-0.8	-0.8	-1.6	-0.8	0.7	1.3
Net core Crown debt[2]	25.1	24.9	25.6	25.0	23.1	20.8
Net worth attributable to the Crown	35.8	33.4	33.4	33.5	34.5	36.4

1 Operating balance before gains and losses.

2 Net core Crown debt excluding the NZS Fund and advances.

Source: The Treasury

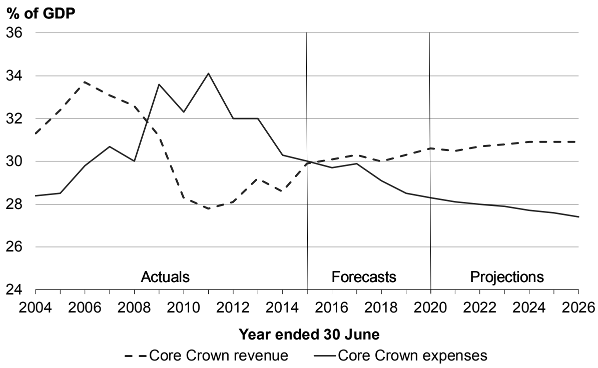
The forecasts show an increase in core Crown revenue as a share of GDP (Figure 6). This increase is greater than forecast in the *Half Year Update*, largely as a result of a stronger pace of growth in the second half of 2015. Similarly, core Crown tax revenue rises over the forecast period, but is assumed to remain relatively constant as a share of GDP over the projection period.

Core Crown expenses are forecast to rise in dollar terms (Figure 7), but fall as a share of GDP (Figure 6).

Core Crown expenses have fallen from 33.6 per cent of GDP in 2008/09 to an estimated 29.7 per cent in 2015/16, reflecting the Government's expenditure control, and are expected to continue to decline as a share of GDP over the forecast and projection period, consistent with the Government's short-term intentions and long-term objectives.

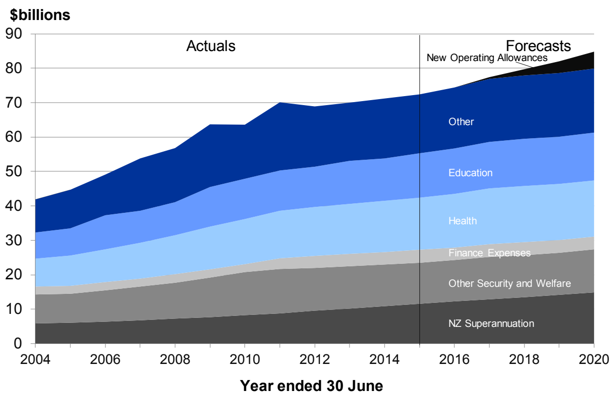
These revenue and expense tracks lead to growing operating surpluses.

Figure 6 – Core Crown revenue and expenses



Source: The Treasury

Figure 7 – Core Crown expenses



Source: The Treasury

Note: Future increases in spending on health and education, for example, will be allocated from the forecast for new operating allowances.

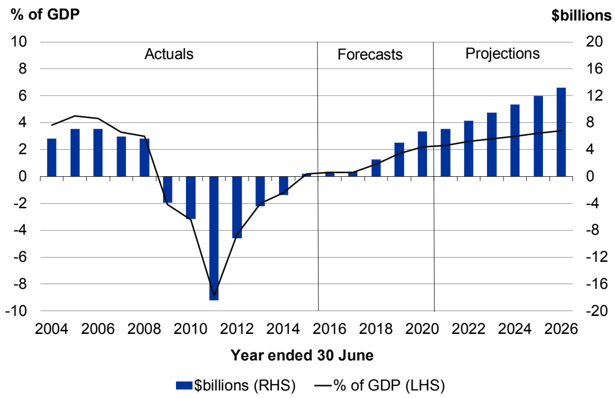
Small OBEGAL surpluses are forecast for this year and next, before rising strongly from 2017/18 (Figure 8).

The residual cash balance is forecast to be in surplus in 2018/19, which will allow the Government to begin reducing net debt in dollar terms. Residual cash declines in the first year of the projection period as contributions to the NZS Fund resume (see below), but continues to rise thereafter (Figure 9).

Net debt peaks at 25.6 per cent of GDP next year, then gradually declines to 19.3 per cent of GDP in 2020/21, in line with the Government's short-term debt intention (Figure 10). Contributions to the NZS Fund are expected to resume in 2020/21, two years earlier than forecast in the *Half Year Update* (Annex 1). In 10 years' time, net debt is forecast to be 7.9 per cent of GDP, consistent with the long-term debt objective.

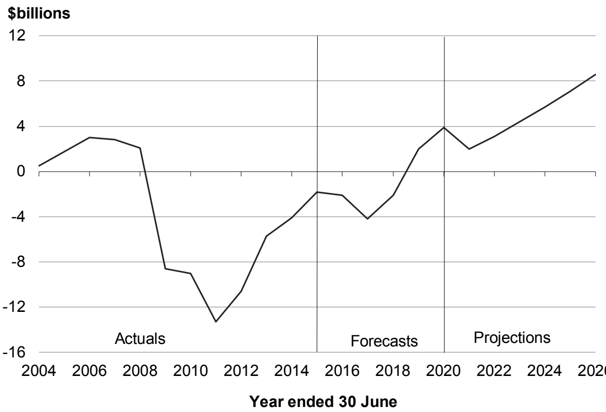
Crown net worth is expected to continue to increase in line with the improving fiscal outlook and the forecast reduction in net debt (Figure 11).

Figure 8 – Total Crown operating balance (before gains losses)



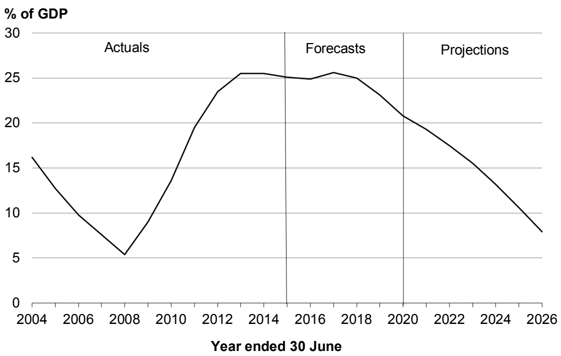
Source: The Treasury

Figure 9 – Core Crown residual cash



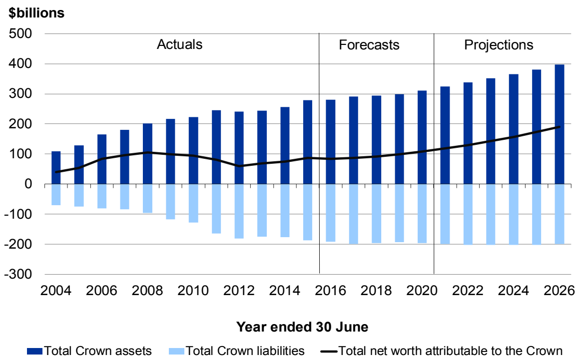
Source: The Treasury

Figure 10 – Core Crown net debt



Source: The Treasury

Figure 11 – Net worth attributable to the Crown



Source: The Treasury

The Treasury's *Long-term Fiscal Statement* shows projections over a much longer time period. Reducing net debt to within a range of 0 per cent to 20 per cent of GDP, resuming NZS Fund contributions as planned, and delivering further improvements in public-sector performance will have a significant effect on long-term projections of the Government's fiscal position and reduce the burden on future generations.

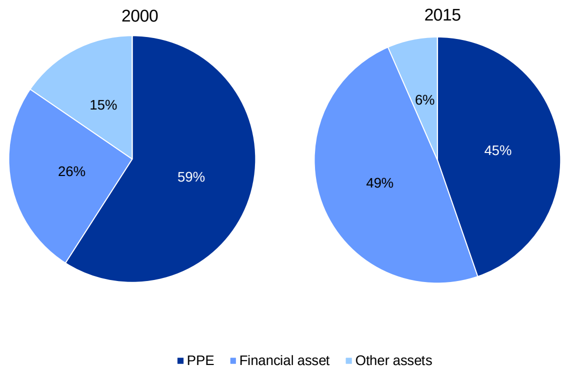
The changing nature of the Crown's balance sheet

If the Crown's balance sheet is strong, governments can meet financing requirements over time without needing significant changes to existing tax and spending policies even in the face of significant shocks. This is the essence of fiscal sustainability. Net worth is a measure of balance sheet strength that can be used to help assess fiscal sustainability.

How has the Crown's balance sheet changed over time?

Since the first publication of a Crown balance sheet in 1993, the nature and size of what the Crown owns and owes has changed considerably. As recently as the year 2000 for example, 59 per cent of Crown assets consisted of the traditional plant, property and equipment (PPE) used to deliver core public services such as education and health, while around 25 per cent were financial assets (Figure 12). In contrast, in the year ended June 2015 around 50 per cent of the balance sheet was made up of financial assets while PPE was 45 per cent.

Figure 12 – The changing composition of the Crown's assets



Source: The Treasury

What are the implications?

Spending decisions and tax revenue have traditionally had the greatest impact on Crown finances. However, as the balance sheet evolves, changes in the values of assets and liabilities will continue to have a greater effect on the overall fiscal position than in the past.

For example, as Table 4 illustrates, given the Crown's current shareholdings as at 30 June 2015, a 10 per cent increase in share prices, all else equal, would have increased the operating balance and net worth by approximately $2.5 billion. In contrast, in 2007 a similar increase in share prices would have increased the operating balance by just $1.3 billion. Additionally, if permanent, a 10 per cent increase in share prices now would have the equivalent effect to reducing net core Crown debt by around 1 per cent of GDP. This highlights the growing importance of managing the Crown's balance sheet, including its overall risk exposures.

Table 4 – Sensitivity analysis

Year ending 30 June $millions	Impact on the operating balance 2007	 2015
Financial assets and liabilities		
Impact of a 1% fall in interest rates	444	539
Impact of a 10% decline in the NZD exchange rate	364	1,043
Impact of a 10% increase in share prices	1,334	2,522
Significant long term liabilities		
Impact of 1% decline in the risk-free discount rate[1]	-3,085	-7,062
Impact of a 1% decline in the inflation rate[2]	1,813	4,106

1 Based on the impact on the ACC claims liability and Government Superannuation Fund (GSF) retirement liability.

2 Based on the impact on the ACC claims liability.

Note: The impacts on net worth are broadly similar to the operating balance impacts.

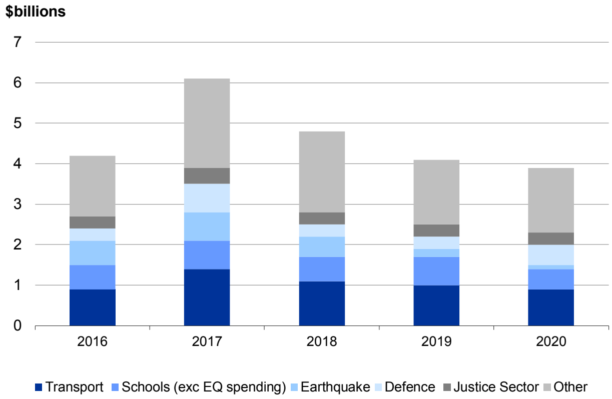
Managing the Crown's Assets and Liabilities

The Crown's assets support the delivery of valuable public services. Its liabilities help to fund these services and consist mostly of debt issued by the Crown.

The most recent year end results show the Crown currently owns $279 billion of assets (up from $223 billion five years ago) and has $186 billion of liabilities. The difference between these numbers represents the Crown's net worth.

More than $23 billion is forecast to be spent on capital across all parts of the Crown over the next five years (Figure 13). This investment will be funded through a combination of general taxation, ring-fenced levies, capital recycling and government debt.

Figure 13 – Total capital spending over the forecast period



Source: The Treasury

The Crown has many liabilities requiring careful management. These can arise owing to contractual arrangements, such as government employee superannuation schemes or insurance obligations such as ACC. In addition, the Crown is exposed to contingent liabilities such as Crown guarantees, and a range of commitments driven by existing policy settings, the largest of which is New Zealand Superannuation.

The Government has been taking a more consistent and deliberate approach to balance sheet management. This involves, among other things:

- introducing private sector capital and disciplines where appropriate, for example through public-private partnerships
- better monitoring of Crown-owned entities and of actual investment performance against expectations, for example through the regular release of major projects performance reports
- requiring Government agencies to produce long-term investment plans, improve capital investment decisions and develop meaningful asset performance measures
- increasing transparency in the use of Crown assets and liabilities to deliver public services
- monitoring the impact of asset and liability risks on the operating balance, and
- a deeper assessment of balance sheet liabilities, including the impacts of policies on future balance sheets and contingent or implicit liabilities.

Execution of this balance sheet strategy will ensure the Government gets the best value possible from its capital spending and from the Crown's existing assets.

Managing the Crown's Revenue and Expenses

The Government supports a broad-base, low-rate tax system that responds to New Zealand's medium-term needs in a planned and coherent way, minimises economic distortions, rewards effort, has low compliance and administrative costs and minimises opportunities for tax avoidance and evasion. Further details on the Government's revenue strategy can be found at www.treasury.govt.nz/government/revenue/strategy.

The current tax policy work programme focuses on three areas:

- using Inland Revenue's business transformation programme to modernise policy and tax administration settings
- dealing with issues relating to international tax and base erosion and profit shifting, and
- improving and enhancing tax and social policy within the Government's broad-base, low-rate tax framework.

The Government also receives revenue from other sources including sales of goods and services by Crown-owned companies, interest income and dividends. Total Crown revenue is expected to stay relatively constant as a percentage of GDP over the forecast and projection periods.

Expenditure control is key to achieving the Government's fiscal objectives. The policy of fixed nominal baselines means that the amount of funding an agency receives each year does not automatically increase to adjust for inflation. Instead, a specific policy decision is required to increase most expenditure items. The operating allowance is the pool of new operating funding available at each Budget, and the Government will continue to keep a tight rein on the size of this allowance.

The Government will continue to develop performance frameworks to drive demand reduction across government services.

The Government's social investment programme is using analysis and commercial tools such as actuarial valuations to understand the long-term needs of society's most vulnerable, and the cost of meeting these needs. Evidence-based tools are being applied to existing and new spending to decide when and how to intervene. Effective intervention in turn reduces the need for spending in the long run.

The Ministry of Social Development, for example, has been using the social investment approach to help people move from welfare into work. As a result, the latest figures show the welfare system's future lifetime cost has reduced by $12 billion over the past four years.

Annex 1

Short-term Fiscal Intentions and Long-term Fiscal Objectives

The Government's short-term fiscal intentions are substantially unchanged since the *Budget Policy Statement*. There are minor changes to the intentions reflecting the revisions to the fiscal forecasts, largely reflecting the stronger outlook for economic activity and changes to Budget allowances (see Table A1.1). These revised fiscal intentions are consistent with the Government's long-term fiscal objectives (see Table A1.2) and the Treasury's *Budget Update* forecasts.

Table A1.1 – Short-term fiscal intentions

Fiscal Strategy Report 2016 (May 2016)	***Budget Policy Statement 2016 (Dec 2015)***
Debt	***Debt***
Our intention is to reduce net debt to around 20 per cent of GDP in 2020. Gross sovereign-issued debt (including Reserve Bank settlement cash and Reserve Bank bills) is forecast to be 30.4 per cent of GDP in 2019/20. Net core Crown debt (excluding NZS Fund and advances) is forecast to be 23.1 per cent of GDP in 2018/19, 20.8 per cent of GDP in 2019/20 and is projected to be 19.3 per cent of GDP in 2020/21.	Our intention is to reduce net debt to around 20 per cent of GDP in 2020. Gross sovereign-issued debt (including Reserve Bank settlement cash and Reserve Bank bills) is forecast to be 33.5 per cent of GDP in 2019/20. Net core Crown debt (excluding NZS Fund and advances) is forecast to be 25.6 per cent of GDP in 2018/19, 24.0 per cent of GDP in 2019/20 and 21.9 per cent of GDP in 2020/21.
Operating balance	***Operating balance***
Our intention is to maintain rising operating surpluses (before gains and losses) so that net core Crown debt begins to reduce in dollar terms (subject to any significant shocks to the economy). The operating balance (before gains and losses) is forecast to be 0.3 per cent of GDP in 2015/16. The operating balance (before gains and losses) is then forecast to be 0.3 per cent of GDP in 2016/17 and 2.2 per cent of GDP in 2019/20. This is consistent with the long-term objective for the operating balance. The operating balance is forecast to be 3.2 per cent of GDP in 2019/20.	Our intention is to maintain rising operating surpluses (before gains and losses) so that net core Crown debt begins to reduce in dollar terms (subject to any significant shocks to the economy). The operating balance (before gains and losses) is forecast to be -0.2 per cent of GDP in 2015/16, rising to 0.1 per cent of GDP in 2016/17 and 1.7 per cent of GDP in 2019/20. This is consistent with the long-term objective for the operating balance. The operating balance is forecast to be 2.6 per cent of GDP in 2019/20.
Expenses	***Expenses***
Our intention is to support fiscal surpluses by restraining the growth in core Crown expenses and managing these to below 30 per cent of GDP. Core Crown expenses are forecast to fall from 29.7 per cent of GDP in 2015/16 to 28.3 per cent of GDP in 2019/20. Total Crown expenses are forecast to be 36.4 per cent of GDP in 2019/20. This assumes a new operating allowance of $1.5 billion in Budget 2017 and for the remainder of the forecast period, growing at 2 per cent thereafter.	Our intention is to support fiscal surpluses by restraining the growth in core Crown expenses and reducing these to below 30 per cent of GDP. Core Crown expenses are forecast to fall from 30.6 per cent of GDP in 2015/16 to 29.1 per cent of GDP in 2019/20. Total Crown expenses are forecast to be 37.3 per cent of GDP in 2019/20. This assumes a new operating allowance of $1 billion in Budget 2016, $2.5 billion in Budget 2017 and $1.5 billion from Budget 2018, growing at 2 per cent thereafter.

Fiscal Strategy Report 2016 (May 2016)	*Budget Policy Statement 2016 (Dec 2015)*
Revenues	***Revenues***
Our intention is to support fiscal surpluses by growing revenue in dollar terms, although maintaining it at broadly the same proportion of GDP.	Our intention is to support fiscal surpluses by growing revenue in dollar terms, although maintaining it at broadly the same proportion of GDP.
Total Crown revenues are forecast to be 38.8 per cent of GDP in 2019/20.	Total Crown revenues are forecast to be 39.2 per cent of GDP in 2019/20.
Core Crown revenues are forecast to be 30.6 per cent of GDP in 2019/20.	Core Crown revenues are forecast to be 30.7 per cent of GDP in 2019/20.
Core Crown tax revenues are forecast to be 28.2 per cent of GDP in 2019/20.	Core Crown tax revenues are forecast to be 28.4 per cent of GDP in 2019/20.
Net worth	***Net worth***
Our intention is to strengthen the Crown's balance sheet as a buffer against future adverse shocks.	Our intention is to strengthen the Crown's balance sheet as a buffer against future adverse shocks.
Total net worth attributable to the Crown is forecast to be 36.4 per cent of GDP in 2019/20.	Total net worth attributable to the Crown is forecast to be 36.2 per cent of GDP in 2019/20.
Total Crown net worth is forecast to be 38.4 per cent of GDP in 2019/20.	Total Crown net worth is forecast to be 38.2 per cent of GDP in 2019/20.

The Government's long-term objectives relate to the next 10 years. There have been minor amendments since the 2016 *Budget Policy Statement* to make them more robust to future developments and thus enhance their durability.

Table A1.2 – Long-term fiscal objectives

Fiscal Strategy Report 2016
Debt
Manage total debt at prudent levels.
Manage net debt within a range of 0 per cent to 20 per cent of GDP.
Operating balance
Deliver operating balances sufficient to meet the Government's net capital requirements, including contributions to the NZS Fund, and ensure consistency with the debt objective.
Operating expenses
Control the growth in government spending so core Crown expenses are below 30 per cent of GDP.
Operating revenues
Ensure sufficient operating revenue to meet the operating balance objective.
Net worth
Ensure net worth remains at a level sufficient to act as a buffer to economic shocks. Consistent with the debt and operating balance objectives, the Crown will build up net worth ahead of the full fiscal impact of the demographic change expected in the mid-2020s.

These short-term intentions and long-term objectives are consistent with each other and with the principles of responsible fiscal management as set out in the Public Finance Act 1989. More detailed information on the principles can be found at www.treasury.govt.nz/publications/guidance/publicfinance/fiscalpolicyframework/.

Contributions to the New Zealand Superannuation Fund

Contributions to the NZS Fund are projected to resume in 2020/21 when net debt falls below 20 per cent of GDP.

This delay in contributions will not affect New Zealanders' entitlement to New Zealand Superannuation, either now or in the future. Low debt is equally as important as NZS Fund assets in meeting some of the future fiscal pressures from population ageing.

Table A1.3 shows the contributions that would be required if they started again in 2016/17.

Table A1.3 – New Zealand Superannuation Fund calculations ($billions)

Year ended 30 June	2017	2018	2019	2020
Calculations of annual contributions if they were to resume in 2016/17	2.1	2.4	2.6	2.6

Fiscal projections and assumptions

Fiscal projections out to 2030 are made using the final forecast year (2020) as a base (Table A1.4). These are constructed using the Fiscal Strategy Model. The main changes to fiscal projections, since the *Fiscal Strategy Report* 2015, reflect changes to economic and fiscal forecasts, including changes to the outlook for nominal GDP, and the profiles for the operating and capital allowances. The only other significant change to assumptions since the *Fiscal Strategy Report* 2015 is a reduction in the long-run stable assumption for the annual rate of return on Government 10-year bonds. After reviewing this assumption, the Treasury elected to reduce it from a nominal annual return of 5.5 per cent to 5.3 per cent at the recent 2015 *Half Year Update*.

The full set of modelling assumptions is outlined on the Treasury website at www.treasury.govt.nz/government/fiscalstrategy/model. Key assumptions include:

- non-welfare spending growth is largely determined by operating allowances
- operating allowances are $1.6 billion in Budget 2016, and $1.5 billion across the remainder of the forecast period, then growing at a rate of 2 per cent per annum for subsequent Budgets
- new capital spending allowances are $1.4 billion in Budget 2016, and $0.9 billion across the remainder of the forecast period, then growing at a rate of 2 per cent per annum for subsequent Budgets, and
- the economy is assumed to grow at trend growth rates with no economic cycles three years after the forecast period.

Table A1.4 – Summary of fiscal projections, as percentages of GDP

Year ending 30 June	2016	2017	2018	2019	2020	2021	2022	2023	2024	2025	2026	...	2030
	Forecasts					Projections							
Core Crown revenue	30.1	30.3	30.0	30.3	30.6	30.5	30.7	30.8	30.9	30.9	30.9	…	31.0
Core Crown expenses	29.7	29.9	29.1	28.5	28.3	28.1	28.0	27.9	27.7	27.6	27.4	…	26.5
Total Crown revenue	39.1	38.9	38.6	38.7	38.8	38.8	39.0	39.1	39.2	39.2	39.2	…	39.3
Total Crown expenses	38.6	38.5	37.5	36.8	36.4	36.3	36.2	36.1	35.9	35.8	35.6	…	34.6
Total Crown OBEGAL[1]	0.3	0.3	0.9	1.7	2.2	2.3	2.6	2.8	3.0	3.2	3.4	…	4.5
Total Crown operating balance[2]	-1.0	1.2	1.8	2.6	3.2	3.2	3.5	3.8	4.1	4.4	4.6	…	5.8
Gross soverign-issued debt	37.6	39.0	35.3	31.9	30.4	28.9	27.1	25.1	22.8	20.3	17.6	…	4.4
Net core Crown debt[3]	24.9	25.6	25.0	23.1	20.8	19.3	17.5	15.5	13.2	10.6	7.9	…	-5.2
Total Crown net worth	35.7	35.7	35.6	36.6	38.4	40.0	41.9	43.9	46.2	48.7	51.3	…	63.8
Net worth attributable to the Crown	33.4	33.4	33.5	34.5	36.4	38.0	40.0	42.1	44.4	46.9	49.5	…	62.1

1 Operating balance (before gains and losses).

2 Excludes minority interests.

3 Excludes financial assets of the NZS Fund and core Crown advances.

Source: The Treasury