

The Treasury

Budget 2020 Information Release

July 2020

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Treasury Report: Budget 2020: Emerging Package Advice

Date:	12 February 2020	Report No:	T2020/157
		File Number:	BM-2-4-2020

Action sought

	Action sought	Deadline
Minister of Finance (Hon Grant Robertson)	Discuss this report with officials at Budget Matters on 13 February 2020	13 February 2020

Contact for telephone discussion (if required)

Name	Position	Telephone	1st Contact
Jess Jenkins	Graduate Analyst, Budget Management	[39]	N/A (mob) ✓
Alex Harrington	Manager, Budget Management	[23]	

Minister's Office actions (if required)

Return the signed report to Treasury.

Note any feedback on the quality of the report

Enclosure: Yes (attached)

Treasury Report: Budget 2020: Emerging Package Advice

Executive Summary

Ministers submitted initiatives for Budget 2020 in November 2019. Since then, we have engaged with you on different packages of initiatives, including cost pressures and new spending initiatives that fall outside the five Budget 2020 Priorities.

On 31 January the Coordinating Ministers for each of the Budget 2020 Priorities submitted draft packages, enabling us to begin viewing the emerging Budget 2020 package as a whole.

Budget 2020 allowances are under considerable pressure, as indicated in the table below:

Item	Operating (\$m p.a.)			Capital (\$m 10 year total)		
Allowances	3,000			8,400		
Pre-commitments	374			49		
Between-Budget Contingency	40			-		
Cost Pressures (current package based on your feedback in January)	1,845			4,198		
'Other' New Spending (current package based on your feedback in January)	341			1,438		
Sub-total	2,600			5,685		
[33]						
Total	3,292	3,642	4,479	6,080	6,351	6,443

[33]

To support Ministers in making these decisions, this report identifies key themes across the current Budget package as a whole (taking the smallest Priority options as a starting point). These include where:

- the Treasury considers the value to lie across these packages;
- there are risks in relation to the impact or deliverability of initiatives, including workforce constraints and market and agency capability, and the extent to which those risks can be mitigated; and
- there are options to scale, phase, or defer initiatives (for example, where there are timing issues such as ongoing industry consultation or sector reviews underway, or known feasibility constraints).

Overall we have been impressed with the processes run by Coordinating Ministers and their secretariats, which are a step forward for collaboration in the Budget process. Secretariats have used their sector expertise, robust assessment processes, and understanding of Ministerial priorities to put together packages with Ministerial and departmental buy in, and which complement each other around key policy priorities.

The benefits of the new process are balanced against some weaknesses, including variable quality of information underpinning some initiatives, leading to limited confidence in the achievability of intended outcomes in some instances. There is also mixed alignment with existing work programmes, and some Government commitments are not funded in the proposed packages.

[33]

We are meeting with you to discuss this report on Thursday 13 February. Following this discussion, you are scheduled to meet with Budget Ministers on Tuesday 18 February to give them an update on the Budget package, and seek their views on their priorities and how the package should be further developed before it is finalised.

Recommended Action

We recommend that you:

- a **note** that Coordinating Ministers submitted draft packages for each of the five Budget Priorities on 31 January;
- b **note** that, based on draft packages, Budget allowances are under considerable pressure, and that Ministers have choices about how to manage this pressure; and
- c **discuss** this report with officials at Budget Matters on Thursday 13 February 2020.

Agree/disagree.

Alex Harrington
Manager, Budget Management

Hon Grant Robertson
Minister of Finance

Treasury Report: Budget 2020: Emerging Package Advice

Purpose of this Report

1. This report advises you of key considerations as you enter the decision-making phase in Budget 2020, ahead of Budget Ministers meetings and Cabinet Committee consultation.
2. Consistent with the focus on collaboration through Budget 2020, the intention of this advice is to complement the work undertaken by Coordinating Ministers and their secretariats by providing system-level insights across the Budget 2020 package as a whole and, in particular, highlighting:
 - the focus, spread, and value of proposed investment across portfolios and priorities;
 - workforce implications;
 - risks associated with the submitted packages, and the extent to which they can be mitigated; and
 - relationships between initiatives included in the Priority packages and those in your current cost pressures and ‘other’ new spending packages, which may impact the feasibility or implementation readiness of the proposed Priority packages.

Background

3. Budget 2020 seeks to build on the successes of the Wellbeing Budget 2019 through increased collaboration by Ministers and departments in the development of initiatives and packages that align with the Budget Priorities.
4. In November 2019 you asked the Coordinating Ministers for each of the five Budget 2020 Priorities to develop and submit draft packages at ^[33]

[33]
5. Since then, cross-agency secretariats and Ministerial groups have been working together to consider submitted initiatives, and develop packages that will contribute to the objectives of the Priority areas. On 31 January, Coordinating Ministers submitted their draft packages to you. ^[33]
6. We have previously provided you with draft cost pressure and ‘other’ new spending packages (T2019/3701 and T2020/10 refer). You have confirmed your comfort with these as a starting point for your Budget package, noting that they may continue to shift as further information becomes available.

Limitations

7. The collaborative focus of Budget 2020 has provided sector expertise in the development of Priority-aligning packages and built joint ownership (Ministerial and departmental) of the Budget 2020 package. However, it has meant the Treasury's understanding of the detail of Priority-aligning initiatives is more limited when compared to that of the secretariats.
8. This advice has been produced at pace following the submission of draft packages on 31 January. Where there is a lack of information for certain initiatives (for example, FTE implications), we have not had the time to obtain that information from departments. Accordingly, this advice focuses on system-level, thematic considerations across the Budget package and its various components. We can work with secretariats to provide you with additional information, should you have further requests following this advice.

Overall view of the Budget 2020 Package

9. The table below pulls together the various components of the Budget 2020 package. It takes your earlier indications on cost pressures and 'other' new spending packages as a starting point, and then adds the initiatives that have been submitted by Coordinating Ministers. As shown, the allowances are under considerable pressure.
10. While certain initiatives in the cost pressure package may decrease in size (such as Mycoplasma Bovis and the Census), it should be noted the figures do not yet include funding for the Defence portfolio.

11. [33]

If you

wish to remain within existing allowances, you will need to consider which components of the Priority packages can be cut, scaled, or funded through other sources. You may also wish to revisit the current cost pressure and 'other' packages.

Item	Operating (\$m p.a.)	Capital (\$m 10 year total)
Allowances	3,000	8,400
Pre-commitments	[33]	[33]
Between-Budget Contingency	40	-
Cost Pressures (current package based on your feedback in January)	1,845	4,198
'Other' New Spending (current package based on your feedback in January)	341	1,438
Sub-total	2,600	5,685
[33]		

Spread of investment (operating per annum)

12. The table below sets out how much funding the largest portfolios would receive as a result of the proposed Budget packages:

Top ten portfolios	Draft Other	Cost Pressures	[33]
\$ millions			
Health	-	1,019	
Education	-	186	
Social Development	9	95	
Biosecurity	-	108	
Police	70	28	
Transport	89	2	
Children	-	54	
Housing and Urban Development	-	28	
Corrections	13	61	
Economic Development	-	51	
Total	182	1,631	

13. You have received advice on the Health and Education portfolios ahead of your bilateral meetings with those portfolio Ministers.

Spread of investment (capital)

14. The table below sets out the currently-supported largest capital initiatives across the packages:

Portfolio	Initiative Title	Package (\$ million)				
		Cost Pressure	Other	Low	Med	High
Health	District Health Boards' Capital Investment	[33]	-	-	-	-
Transport	Future of Rail – Rolling Stock Investment to Support a Resilient and Reliable Rail Freight System	-	[33]	-	-	-
Transport	Future of Rail – Investment in improved resilience and reliability of core assets	-		-	-	-
Transport	Future of Rail – New Interisland ferries to support a resilient and reliable rail freight system	-		-	-	-
Internal Affairs	Preserving the Nation's Memory (PtNM)	-		-	-	-
[33]						
Justice	Justice Property Health and Safety Remediation	[33]	-	-	-	-
[33]						

¹ Note the Treasury Vote team has provided revised options for this initiative in advice for your Priority E and Health bilaterals [T2020/159 refers]

Assessment and identified risks

15. In October 2019 you agreed to the assessment of large capital investment proposals for Budget 2020 by a Capital Investment Panel.² You are receiving a separate Treasury Report on the Panel's assessment process and recommendations.
16. The Panel considers that, despite the general attractiveness of initiatives due to the priority areas they cover, the underpinning information on planning, resourcing, and sequencing is not robust, leading to uncertainty around achievability for a number of initiatives. Although mixed, there is a general lack of evidence on the implementation-readiness of these investments, with only five of the 17 largest initiatives having completed business cases available. There are also concerns based on the historic ability of agencies to deliver similar projects. In order to obtain full value from the supported capital initiatives, there are agency capability and capacity constraints that need to be supported.
17. Of concern is the relationship between the proposed capital investment through Budget 2020 and the capital investment package announced through the Budget Policy Statement. The additional investment in infrastructure raises questions around the capability and capacity of agencies, as well as the market's capability and capacity to deliver the outputs, outcomes, and benefits from the Government's additional investment. As discussed below, there is significant labour market pressure in the construction sector, which raises risk in relation to the deliverability of all funded initiatives.

Workforce implications and labour market constraints

18. The proposed Budget 2020 package would fund significant numbers of FTE staff through various departmental initiatives. This is likely to contribute to existing labour market pressures, and raises achievability concerns in relation to supported initiatives.
19. There is already significant pressure in the public sector labour market. Budget 2019 saw continued FTE growth with increasing impacts on recruitment and wage growth. Treasury analysis of initiatives in Budget 2019 showed approximately 4,000 additional departmental FTEs were sought, with approximately 2,000 FTE funded, representing a 5% increase in departmental staffing levels. This growth reflects longer-term expansion in the public sector workforce.³
20. Unemployment rates are at historical lows and the December 2019 ANZ Business Outlook survey identified finding skilled labour as the second greatest problem for all firms (and the greatest problem in the construction sector, which increases the achievability risk for capital investment proposals). Together, increasing labour demand and constrained labour supply are placing pressure on wages, resulting in public sector wage growth that outstrips the private sector.⁴ There are also indicators of increased wage growth in core public service departments.⁵ Upcoming collective bargaining and pay equity claims will add further pressure on public sector wages.

² The Capital Investment Panel is comprised of: Treasury's Investment Management and Asset Performance team, the Government's Chief Data Officer and Chief Data Steward, the New Zealand Infrastructure Commission, and New Zealand Government Procurement and Property.

³ The Quarterly Employment Survey reported at 8.1% growth (8,700 jobs) in the wider Public Sector in the year to 30 September 2019, while the State Services Commission's latest Human Resource Capability Survey showed a 5.8% (or 2,898 FTE staff) increase in core departmental FTE from 30 June 2018 to 30 June 2019 to 52,628 FTE.

⁴ Statistics New Zealand latest Labour Cost Index (LCI) release showed wage growth in the public sector was higher than in the private sector for the first time since 2016, and at its highest rate since June 2009 (noting that pay settlements in Education, Health and the Police are a significant driver).

⁵ The latest HRC data shows the average salary for the public service increased by 5% in the year to June 2019, from \$77,900 to \$81,830 (noting this is an approximate measure of wage growth, with no adjustment for changes in the composition of the workforce).

21. [33]

Four specialist workforces with FTE sought through Budget 2020 are particularly constrained: senior policy analysts, data analytics, asset management, and Māori capability.⁷

22. In many areas of sustained funding growth, the additional FTE sought in Budget 2020 sits atop increased funding from Budget 2019, adding further to workforce demand pressures. We expect increasing pressure on the public sector labour market, resulting in increased turnover, recruitment and wage growth, to start impacting on achievability of funded initiatives' outcomes through reduced delivery and/or increased price.
23. Ministers and agencies are increasingly aware of public sector workforce issues, and you provided advice to all the Budget Priority Secretariats to consider FTE and capability issues when making decisions. However, most initiatives generally still require new staff. Our current estimates highlight the need to consider whether funding new FTE is realistic given labour market pressure, and the long-term implications of doing so (for example, in relation to DHB deficits).
24. Comment is provided in the Priority sections below where FTE implications raise specific concerns about the achievability or flow-on impact of packages or initiatives.

Cross-cutting priority policy areas

25. There are some priority policy areas that are set to receive funding through initiatives across the various Budget Priority packages. Brief comment is provided below on whether the investment across Priorities is considered to be cohesive, and in alignment with sector strategies.

Housing

26. Housing has been identified as a Ministerial priority for this Budget. [33]
We are aware of significant cost pressures for Housing (some of which will create funding cliffs in the next twelve months). The Housing portfolio received funding for the capability initiative in the cost pressure package, however there are further pressures (discussed below) which should be prioritised through this Budget.

[33]

⁶ Please note that this estimate should not be compared to Budget 2019 estimates as it has a broader scope, including non-departmental workforces where possible.

⁷ Subsequent discussions with functional leads working in these areas has confirmed these workforce related issues, including impacts on turnover, recruitment, and the 'poaching' of experienced staff across agencies.

[33]

30. At your request we can provide further information on the most important Housing cost pressures to fund through this Budget.

Justice

31. There are currently [33] initiatives supporting the justice sector reforms ([33] Hōkai Rangi) recommended across the draft [33] Packages. These total [33] per annum new operating funding [33] and [33] capital funding [33]. This includes the following initiatives that we consider to be high priority:

- *Caseflow*,
- [33]
- *Pre-Trial Services*, and
- [33]

[33]

34. The Minister of Justice has provided you with scaling options, however these options are typically higher than the funding currently included in the draft Cost Pressure package (which is [33] per annum operating funding and [33] capital funding). There are two areas where the Minister has identified savings over the existing amounts in the Cost Pressure package ([33] and *legal aid*) which provide savings of \$6.7 million operating funding per annum. The Ministry has also identified some small expected underspends in 2019/20, that could further reduce the Justice component of the cost pressure package, although the amounts concerned have yet to be confirmed.

35. We do not recommend any further scaling of cost pressures as funding is primarily to address:
- compliance spending in courts buildings (the majority of the capital funding)
 - remuneration cost pressures related to upcoming wage negotiations
 - core infrastructure requirements – addressing deferred maintenance and the depreciation impacts of asset revaluations, and other non-discretionary pressures over which agencies have little control (demand-driven services such as legal aid, Serious Fraud Office caseload, Canterbury Earthquakes Insurance Tribunal, and electronic bail; and the implementation of the Arms Legislation Bill).

Recap of cost pressures and 'other' new spending

41. You have previously signalled your comfort with a draft 'high' cost pressures package (T2019/3701 refers). This package has been revised to \$1.8 billion operating per annum and \$4.3 billion in total capital. We advised you that this level of funding is consistent with supporting system sustainability and wellbeing outcomes, while leaving a credible amount for new spending initiatives. There are a number of areas within this package where decisions are still outstanding and the total amount may be revised:
- This draft package does not yet include funding to address Defence cost pressures. We will include an amount following your discussion of the Defence Baseline Review with the Minister of Defence on 12 February.
 - We have maintained 'high' placeholder funding amounts for Votes Health and Education in this draft package, pending your bilateral meetings with Portfolio Ministers. We will provide you with revised cost pressure amounts for these portfolios following these meetings.
42. You have previously signalled your comfort with a new spending – 'other' package at a current annual average of \$341 million operating and \$2.1 billion total capital (T2020/10 refers). This amount could vary depending on your choices regarding several significant initiatives, and does not include a number of initiatives where decisions are still outstanding. This amount includes several initiatives you indicated you wished to include in the new spending – other package following discussions with the Treasury:
- Defence new spending included in this package is the vote team's preferred option, which is significantly lower than the amount sought. We will revise this following the outcome of your discussion with the Minister of Defence.

- You have agreed to baseline funding for the Census of Population and Dwellings, with a large proportion of this being made through a technical adjustment at the March Baseline Update with a corresponding impact on OBEGAL, rather than through the Budget 2020 allowances (T2020/171 refers). As a result, funding for Census at Budget 2020 will comprise only the portion of funding not met by the newly established baseline. To progress this further, the vote team would like your agreement-in-principle to funding for Stats NZ of \$232.5 million operating and \$11.9 million capital over four years to deliver Census 2023, with the proportion to be sought at Budget 2020 to be determined based on your decisions in due course about the size of the newly established baseline.
- This package does not yet include funding for GSCB/NZSIS new spending initiatives. ^[33]
- You indicated you had a number of questions in relation to investment in KiwiRail through the new spending – other package. The vote team is preparing further advice, which will be provided to you next week, with a focus on how to deliver on the ‘reliable and resilient’ investment scenario, within the Government’s fiscal constraints.

Priority Packages

43. A spreadsheet of all initiatives in each of the Priority packages is provided at Annex 2.
44. The development of Priority packages by Ministers and secretariats has generally run well, and the new process has produced packages at various funding scenarios with departmental and Ministerial ownership.
45. Allowances are tight, and Ministers now have choices about the concentration of investment across the Priorities, as well as the relative value of additional spending in the cost pressures, and ‘other’ packages. For comparison, the funding across the Priorities at Budget 2019 is provided below. It is important to note that the operating allowance was greater (\$3.8 billion), and the Priority totals included spending on certain cost pressures.⁸

Budget 2019 Funding Priority	Average operating (\$ m)	As proportion of total (\$ 3.8 billion)
A: Transforming the economy	157	4%
B: Building a productive nation	265	7%
C: Supporting Māori and Pasifika aspirations	148	4%
D: Improving child wellbeing	875	23%
E: Taking mental health seriously	346	9%
Investing in New Zealand	1,667	44%
Other tagged contingencies	330	9%

⁸ Summary of Initiatives, Budget 2019.

46. It is also worth noting the varying levels of oversubscription across the priorities, as shown in the below graph.

[33]

47. The Priority sections below briefly analyse the submitted packages in each Priority, providing an overview of investment, including themes adopted by Ministers, alignment with sector strategies if relevant, and departmental impact. [33]

48. [33]

49. Secretariats and Treasury officials have worked together on the wellbeing analysis of the draft Priority packages. Insights from this work have been integrated throughout the Priority sections below. Work is underway on 'wellbeing summary' A3s, and these will shortly be provided to secretariat groups. They will also be provided to you once completed.

50. Assessment of initiatives with a significant data, digital, or ICT component has been jointly undertaken by the GCDO and GCDS. The GCDO and GCDS provided advice to the Budget Priority secretariats and to Treasury, which included a view of achievability and attractiveness of initiatives from an overall system perspective. Where there are concerns for any supported initiatives, these have been integrated into the sections below, and conditions are recommended where relevant.⁹ The GCDO and GCDS have also outlined where an initiative is considered to be attractive from a digital, data and ICT system perspective but has not been included in the packages.

51. Where you have raised questions in your bilaterals with Coordinating Ministers, we have sought to provide further information; however, as identified above, our ability to provide detailed information on all initiatives is limited, and analysis generally focuses on the investment themes adopted by the Priority groups, with more specific comment provided where available.

⁹ Where conditions are recommended, these will be integrated into the Significant Budget Cabinet paper financial recommendations.

52. Looking across the packages, there are a number of initiatives where ongoing policy work or public consultation makes the timing of Budget decisions an issue. These instances represent opportunities to scale, phase or defer initiatives; however, if Ministers wish to fund these at Budget 2020 the issue of timing can be managed by establishing contingencies, and we can provide a list of suitable initiatives.

Alignment with Government work programmes

53. The Priority packages have mixed alignment with various ongoing Government work programmes. We have provided a high-level indication of the Priorities' alignment with various programmes at Annex 1.

Priority A: Just Transitions

54. Priority A is focused on *“Supporting New Zealanders in the transition to a climate-resilient, sustainable, and low emissions economy.”*
55. The sub-priorities are:
 1. *“Enable land use to deliver higher value and improved environmental outcomes”;*
and
 2. *“Promote a sustainable and affordable energy system”*

[33]

¹⁰ Note that the package A3 submitted by Priority A Ministers only includes operational funding sought.

Priority B: Future of Work

64. Priority B is focused on *'Enabling all New Zealanders to benefit from new technologies and lift productivity through innovation'*.
65. The sub-priorities are:
- *Enabling workers to adapt to technological change by continually upskilling, reskilling, and participating in productive and fair employment, and*
 - *Supporting businesses by enabling uptake of new technology and improving access to global markets, skills and infrastructure.*

[33]

[33]

Priority C: Māori and Pacific Peoples

73. Priority C is focused on *“Lifting Māori and Pacific incomes, skills and opportunities”*.

74. The sub-priorities are:

- *Lifting Māori and Pacific peoples’ skills, education, income and employment outcomes, and*
- *Improving Māori and Pacific health and housing outcomes through housing quality, affordability, and tenure.*

[33]

Priority D: Child Poverty and Child Wellbeing

83. Priority D is focused on *'Reducing child poverty and improving child wellbeing'*.

84. The sub-priorities are:

- *Improving housing quality and income levels for low income families; and*
- *Prevention and early intervention for children and whānau with the greatest needs, including continuing to address family violence and sexual violence.*

[33]

[33]

Priority E: Physical and Mental Wellbeing

93. Priority E is focused on *‘Supporting improved health outcomes for all New Zealanders’*.

94. The sub-priorities are:

- *Strengthening existing mental health services in the health sector and beyond, with a focus on under 24-year-olds; and*
- *Delivering a sustainable and equitable public health and disability system.*

[33]

[33]

[33]

Next Steps

106. We are scheduled to meet with you to discuss this report on Thursday 13 February.
107. The third Budget Ministers meeting for Budget 2020 is scheduled for Tuesday 18 February, where we are expecting you to give your colleagues an update on how the Budget package is developing and seek their views on how it should progress from here. Material for that meeting needs to be finalised by Friday 14 February. When we meet with you on Thursday 13 February, we would like to discuss with you the material that you wish to share with Budget Ministers, and the decisions or views you wish to seek from them at the meeting.
108. You have met with Coordinating Ministers Clark, Twyford, and Parker to discuss their draft Priority packages, and you will be meeting with Coordinating Ministers Martin and Davis next week. We have provided you with a list of questions to raise with Ministers. In particular, you may wish to ask for an indication from the Ministers of their preferred scaling options for the packages, and risks they are aware of in relation to achievability or implementation readiness of the supported initiatives.
109. The Treasury is providing you with fiscal strategy advice, including on the size of Budget allowances, on 26 February.

Annex 1: Alignment with Government work programmes

This Annex provides you with an overview of the alignment of each Priority package with existing government work programmes, including reviews, responses, and inquiries. A cross indicates that the Priority package in some way supports progress on, or overlaps with, the corresponding work programme (or review). We do not have detailed information at this stage, but can provide further information to you if requested.

Existing Work Programmes	Priority Packages
	[33]
Accelerating Renewable Energy and Energy Efficiency	
Better Later Life Action Plan	
The Biosecurity Act Overhaul	
Child and Youth Wellbeing Strategy	
Cancer Action Plan	
Careers Action Plan	
Construction Skills Action Plan	
Crown Response to the Inquiry into Historical Abuse in State Care	
Early Learning Action Plan	
Home-based Early Childhood Education Review	
Economic Plan	
Electricity Price Review	
Employer-assisted Temporary Work Visa Policy Changes	
Employment Strategy and Employment Action Plans	
Essential Freshwater	
Family and Sexual Violence Joint Venture	
Future of Work Tripartite Forum	
Government Response to the Productivity Commission Low Emissions Economy Report	
Government Response to the Small Business Council Report	
Government Response to the Trade for All Advisory Board Report	
Hāpaitia te Oranga Tangata & Hōkai Rangi	
He Poutama Rangatahi	
Housing Kaupapa Inquiry	
Industry Policy/Industry Transformation Plan	
Ka Hikitia – the Māori Education Strategy	
Pacific Education Action Plan	
PM's Business Advisory Council	
Maihi Karauna Strategy	
Maihi Māori Strategy	
NCEA Review	
Oranga Tamariki Operating Model	
Reforming the New Zealand Emissions Trading Scheme	
Reform of Vocational Education	
Research, Science and Innovation Strategy (draft) ¹³	

¹³ The strategy has not yet been agreed by Cabinet

Government Response to He Ara Oranga: Government Inquiry Into Mental Health and Addiction	[33]
Response to the Independent Panel Review of the 2014 Family Justice Reforms	
Resource Management Act Review	
Review of Financial Assistance for Caregivers	
Review of the Crown Minerals Act 1991	
Government Response to Expert Advisory Panel Review to Overhaul the Welfare System (WEAG)	
Space Strategy (draft) ¹⁴	
Temporary Migrant Worker Exploitation Review	
Urban Growth Agenda	
Waste Minimisation Levy Review	
Total	

The Priority Packages notably do not contribute to the following work programmes:

[33]

¹⁴ Ibid

