

# The Treasury

## Budget 2020 Information Release

### July 2020

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- [34] 9(2)(g)(i) - to maintain the effective conduct of public affairs through the free and frank expression of opinions
- [35] 9(2)(g)(ii) - to maintain the effective conduct of public affairs through protecting ministers, members of government organisations, officers and employees from improper pressure or harassment;
- [37] 9(2)(i) - to enable the Crown to carry out commercial activities without disadvantage or prejudice
- [38] 9(2)(j) - to enable the Crown to negotiate without disadvantage or prejudice
- [39] 9(2)(k) - to prevent the disclosure of official information for improper gain or improper advantage
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## Treasury Report: Options for fiscal objectives at Budget 2020

<b>Date:</b>	3 April 2020	<b>Report No:</b>	T2020/759
		<b>File Number:</b>	MC-1-5-2 (Fiscal strategy)

### Action sought

	Action sought	Deadline
Hon Grant Robertson <b>Minister of Finance</b>	<b>agree</b> to change the short-term intentions and long-term objectives for fiscal policy in the 2020 Fiscal Strategy Report.	Monday 6 April 2020

### Contact for telephone discussion (if required)

Name	Position	Telephone	1st Contact
Anna Hamer-Adams	Analyst, Macroeconomic and Fiscal Policy	[39]	N/A (mob) ✓
Renee Philip	Manager, Macroeconomic and Fiscal Policy	[23]	

### Minister's Office actions (if required)

**Return** the signed report to Treasury.

Note any feedback on the quality of the report

**Enclosure:** No

## Treasury Report: Options for fiscal objectives at Budget 2020

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1. This report seeks your agreement to change your current short-term intentions and long-term objectives for fiscal policy in the 2020 Fiscal Strategy Report (FSR).

### Your fiscal strategy will need to be revised in light of COVID-19

2. The Public Finance Act (PFA) requires you to outline your fiscal strategy in the FSR by publishing long-term objectives for the years 2020/21 – 2030/31 at least (henceforth objectives) and short-term intentions for the years 2020/21 – 2022/23 (henceforth intentions) for debt, the operating balance, expenses, revenue and net worth.
3. COVID-19 has had, and will continue to have, a significant impact on the fiscal position. As a result, you will not achieve almost all the short-term intentions set out in the 2020 Budget Policy Statement (BPS), and we would recommend a review of the long-term objectives (ref Tables 1 and 2).

### We recommend setting new fiscal objectives and intentions in the 2020 FSR

4. Setting new objectives and intentions in the 2020 FSR will provide guidance to the public and credit markets around your strategy for fiscal policy going forward. This guidance is important given how significantly you are forecast to deviate from your current fiscal targets.
5. While your current fiscal targets are ‘subject to any significant shocks’, we do not recommend committing to return to net core Crown debt in the range of 15-25% of GDP within the next ten years. The rapid fiscal consolidation that would be required to meet this target is inadvisable given the need to support a medium-term recovery following COVID-19.
6. You could decide to delay changing your objectives/intentions in the 2020 FSR until the 2021 BPS. This approach gives more flexibility for fiscal policy, and you will have the benefit of better information at the 2021 BPS for setting new objectives/intentions. A similar approach was taken in the 2009 BPS during the Global Financial Crisis. However, this approach limits guidance for the public and credit markets to what you signal in the text of the FSR and the fiscal projections. The PFA will also require a number of disclosures in the FSR under this approach. We do not recommend this approach.

### Flexible objectives and intentions will support agile policy-making and recognise uncertainty

7. At this stage we recommend setting flexible, broad targets, rather than rules with specified numeric target levels and target dates. Doing so will provide guidance about the direction of future fiscal policy while placing a high weight on supporting flexibility for policy-making, given significant uncertainty about the future fiscal position.
8. Note, the FSR will also signal your aims for fiscal policy through the text in the report and through fiscal projections (required by the PFA). In an upcoming Treasury Report, we will present you with options on projection tracks of fiscal variables for your feedback on the desired trajectory.
9. **New short-term intentions** should recognise the need for a period of further fiscal expansion to cushion the impact of COVID-19 and support the recovery. To do so, your intentions could explicitly state net debt and OBEGAL deficits will rise in the near-term.
10. Table 1 presents the current and possible new short-term intentions. The three main changes we recommend are for the net debt, operating balance and net worth

intentions, as these three variables summarise the main channels of the COVID-19 fiscal response. In all cases we recommend avoiding numeric targets and linking the intentions to COVID-19 explicitly to avoid overly constraining fiscal policy.

11. Setting short-term intentions for rising net debt and operating deficits and decreasing net worth is not consistent with the PFA principles of responsible fiscal management. This inconsistency is allowed in the PFA, provided it is temporary and you explain the reason for departure from the principles and the approach you will take to ensure the intentions become consistent with the principles again. The draft Fiscal Strategy Report you will receive next week will propose text to meet these requirements.
12. **New long-term objectives** need to cover a period of at least ten years. As such, they should signal a longer period of consolidation to stabilise (and potentially reduce) debt and return OBEGAL to surplus over time. They should also reflect your broader long-term vision for fiscal policy.
13. Table 2 presents the current and possible new long-term objectives. The three main choices are around the net debt, operating balance, and operating expenses objectives.
  - a **Net debt.** We recommend aiming to stabilise net core Crown debt at prudent levels. This wording accounts for uncertainty around where net debt will end up and what prudent debt will be post-COVID-19.
  - b We do not recommend setting a specific long-term debt objective at this stage. The prudent long-term level of debt will change as the impacts of, and global and domestic responses to, COVID-19 continue to emerge. We will provide further advice about your fiscal headroom later this month. You could signal in the FSR that you will look to set a more specific objective in future, once the extent of the shock becomes clearer.
  - c **Operating balance.** An explicit reference to returning to surplus will provide more guidance than the current objective.
  - d **Operating expenses.** The current operating expenses objective signals the size of government will remain comparable to recent history. If you see a larger role for the government in future (e.g., if a substantial part of the response to COVID-19 is not unwound in future), you may wish to amend this objective.

## Next steps

14. Decisions around the fiscal intentions and objectives will be reflected in the Fiscal Strategy Report. You will receive a first draft of the FSR on 9 April, which will be updated iteratively with feedback from you and your office.
15. If you decide to change the fiscal intentions and objectives, you may wish to inform Cabinet. This could be done by taking an oral item to Cabinet, and could occur in the week of the 20<sup>th</sup> or 27<sup>th</sup> of April, before the FSR is finalised and printed.

**Table 1 – Short-term fiscal intentions**

	<b>Intentions in 2020 Budget Policy Statement</b>	<b>Recommended intentions</b>	<b>Alternative options (not recommended)</b>
<b>Debt</b>	Our intention is to reduce the level of net core Crown debt to 20 per cent of GDP within five years of taking office (subject to any significant shocks in the economy). We will continue to maintain debt at prudent levels (a range of 15-25 per cent of GDP).	Our intention is to allow the level of net core Crown debt to rise while the economic response to COVID-19 is ongoing.	<p><i>Rise in short-term:</i> Our intention is to allow the level of net core Crown debt to rise in the short-term.</p> <p><i>Upper limit:</i> Our intention is to allow the level of net core Crown debt to rise to no more than x% of GDP.</p> <p><i>Time limit:</i> Our intention is to allow the level of net core Crown debt to rise until the mid-2020s to support wellbeing.</p>
<b>Operating balance</b>	Our intention is to deliver operating surpluses (before gains and losses) to ensure net debt falls to 20 per cent of GDP within five years of taking office and to maintain it at prudent levels thereafter (a range of 15-25 per cent of GDP).	Our intention is to run operating deficits in the short-term to fight COVID-19, cushion its impact, and position New Zealand for recovery.	<p><i>Deficits in short-term:</i> Our intention is to run operating deficits in the short-term.</p> <p><i>Upper limit:</i> Our intention is to run operating deficits no larger than x% of GDP in the near-term.</p> <p><i>Specify measures:</i> Our intention is to run operating deficits in the near-term through delivering mostly time-limit measures to respond to COVID-19.</p>
<b>Operating expenses</b>	Our intention is to ensure expenses are consistent with the operating balance objective.	<i>Keep intention unchanged.</i>	
<b>Operating revenues</b>	Our intention is to ensure sufficient revenue to meet the operating balance objective.	Our intention is to ensure revenue <i>is consistent</i> with the operating balance objective.	
<b>Net worth</b>	Our intention is to increase net worth consistent with the operating balance objective.	Our intention is to use the Crown’s net worth to cushion the economic shock from COVID-19. Significant risks will be transferred onto the balance sheet through the response period.	<i>Minor wording change:</i> Our intention is to ensure net worth is consistent with the operating balance objective.

**Table 2 – Long-term fiscal objectives**

	Objectives in 2020 Budget Policy Statement	Recommended objectives	Alternative options (not recommended)
<b>Debt</b>			
<i>Total debt</i>	Maintain total debt at prudent levels.	<i>Keep total debt objective unchanged.</i>	
<i>Net debt</i>	The Government will reduce the level of net core Crown debt to 20 per cent of GDP within five years of taking office and maintain it at prudent levels thereafter. Prudent levels of net core Crown debt are within a range of 15 to 25 per cent of GDP (subject to any significant shocks to the economy).	The Government will stabilise and then reduce net core Crown debt to prudent levels over the next 15 years. Prudent levels of net core Crown debt are those where a debt distress episode is unlikely and include a buffer against future shocks.	<p><i>Stabilise:</i> The Government will stabilise net core Crown debt over the projection period.</p> <p><i>Stabilise + target date:</i> The Government will stabilise net core Crown debt to prudent levels from mid-2020.</p> <p><i>Debt target:</i> The Government will work to reduce net core Crown debt to around x% of GDP over a reasonable period.</p> <p><i>Debt target + target date:</i> The Government will reduce net core Crown debt to x% of GDP by the early 2030s</p>
<b>Operating balance</b>	The Government will deliver a sustainable operating surplus across an economic cycle.	The Government will return the operating balance (before gains and losses) to surplus and maintain an operating balance consistent with the debt objective thereafter.	<p><i>Keep objective unchanged.</i></p> <p><i>Target date:</i> The Government will return the operating balance (before gains and losses) to surplus by mid-2020 and maintain an operating balance consistent with the debt objective thereafter.</p>
<b>Operating expenses</b>	<p>The Government will maintain its expenditure to within the recent historical range of spending as a ratio of GDP.</p> <p>The Government will take a prudent approach to ensure expenditure is phased, controlled and directed to maximise its benefits, in particular prioritising investments to address the long-term financial and sustainability challenges facing New Zealand.</p>	<i>Keep both objectives unchanged.</i>	<i>Keep only second expenses objective, remove first objective.</i>

<b>Operating revenues</b>	The Government will ensure a progressive taxation system that is fair, balanced, and promotes the long-term sustainability and productivity of the economy.	<i>Keep objective unchanged.</i>	
<b>Net worth</b>	The Government will strengthen net worth consistent with the debt and operating balance objectives.	<i>Keep objective unchanged.</i>	



## Recommended Action

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We recommend that you:

- a **agree** to change the short-term intentions and long-term objectives for fiscal policy in the 2020 Fiscal Strategy Report as recommended in Table 1 and Table 2.

*Agree/disagree.*

- b **note** we will ask you to signal your desired trajectory for fiscal variables in the Budget Economic and Fiscal Update (BEFU) projections in an upcoming Treasury Report, before the final BEFU fiscal forecasts are completed.

Renee Philip  
**Manager, Macroeconomic and Fiscal Policy**

Hon Grant Robertson  
**Minister of Finance**

## **Annex 1. Public Finance Act requirements**

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### **The PFA requires you to set fiscal objectives and intentions in the FSR**

16. The PFA requires you to publish long-term objectives (henceforth objectives) and short-term intentions (henceforth intentions) in the FSR. The objectives and intentions must be set for: operating expenses, operating revenues, the operating balance, level of total debt and level of total net worth. The objectives must refer to the years 2020/21 – 2030/31 at least, while the intentions must refer to the years 2020/21 – 2022/23 at minimum.
17. In the FSR, you must explain how your intentions and objectives are consistent with (1) one another, (2) with the Budget Economic and Fiscal Update (BEFU) forecasts and projections, and (3) with the PFA principles of responsible fiscal management. If your intentions and objectives are not consistent with one or more of the above, the FSR must justify the reasons for departure and state your approach to ensure the intentions become consistent again over a specified time period.
18. The FSR must also include projections of the five fiscal variables mentioned above for at least 10 years.