TE TAI ŌHANGA
THE TREASURY

Reference: 20190833

6 May 2020

s9(2)(a)

Thank you for your Official Information Act request, received on 16 December 2019. You requested the following:

> *Under section 12 of the Official Information Act 1982 ("the Act") I request all analysis, advice or correspondence with, or provided, to the Minister of Finance (or his office) relating to HYEFU 2019 (excluding administrative emails such as meeting invitations etc.)*

On 28 January 2020, I sought an extension of 40 working days and on 1 April 2020 Treasury provided you with our decision to grant your OIA request prior to delivering the requested documents under section 15(1)(b) of the Official Information Act.

We subsequently contacted you to let you know the response would take a little longer due to the pressures on the Minister of Finance's office owing to COVID-19 decision-making. We appreciate your patience and understanding.

**Information being released**

Please find enclosed the following documents:

| Item | Date | Document Description | Decision |
|---|---|---|---|
| 1. | 17 October 2019 | Treasury Report: HYEFU 2019 Preliminary Economic and Tax Forecasts | Release in part |
| 2. | 29 October 2019 | *Email:* FW: Preliminary fiscal forecasts | Release in part |
| 3. | 31 October 2019 | Treasury Report: Half Year Economic and Fiscal Update 2019 Preliminary Fiscal Forecasts | Release in part |
| 4. | 13 November 2019 | *Email:* RE: SFRs Chapter TR Timeframes | Release in part |
| 5. | 15 November 2019 | *Email:* Draft Final HYEFU TR | Release in part |
| 6. | 18 November 2019 | Treasury Report: Half Year 2019 Economic and Tax Forecasts | Release in part |
| 7. | 18 November 2019 | Aide Memoire: Phasing of Additional Capital Investment | Release in part |

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| | | | |
|---|---|---|---|
| 8. | 20 November 2019 | Treasury Report: HYEFU 2019 Specific Fiscal Risks Draft Chapter | Release in part |
| 9. | 25 November 2019 | *Email:* Final fiscal forecasts - HYEFU 19 | Release in part |
| 10. | 28 November 2019 | Treasury Report: Half Year Economic and Fiscal Update 2019 Final Fiscal Forecasts | Release in part |
| 11. | 28 November 2019 | *Email: SFRs Update* | Release in part |
| 12. | 5 December 2019 | RE: Treasury Report_ Half Year Economic and Fiscal Update 2019 Final Fiscal Forecasts.DOC | Release in part |
| 13. | 6 December 2019 | *Email:* Budget Matters Agenda (10 December 2019) | Release in part |
| 14. | 6 December 2019 | Budget Matters Agenda (10 December 2019) | Release in part |
| 15. | | New Risks since MoF Draft for BMatters discussion | Release in part |

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

- 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,
- 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,
- names and contact details of officials, under section 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,
- confidential information, under section 9(2)(j) – to enable the Crown to negotiate without disadvantage or prejudice
- direct dial phone numbers of officials, under section 9(2)(k) – to prevent the disclosure of information for improper gain or improper advantage.

Direct dial phone numbers of officials have been redacted under section 9(2)(k) in order to reduce the possibility of staff being exposed to phishing and other scams. This is because information released under the OIA may end up in the public domain, for example, on websites including Treasury's website.

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 reply addresses the information you requested. You have the right to ask the Ombudsman to investigate and review my decision.

Yours sincerely

Alex Harrington
**Manager, Budget Management**

# 20190833
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**BUDGET-SENSITIVE**

TE TAI ŌHANGA
THE TREASURY

# Treasury Report: HYEFU 2019 Preliminary Economic and Tax Forecasts

| **Date:** | Thursday 17 October | **Report No:** | T2019/3177 |
|---|---|---|---|
| | | **File Number:** | BM-3-6-1 |

## Action sought

| | **Action sought** | **Deadline** |
|---|---|---|
| Hon Grant Robertson<br>**Minister of Finance** | **Note** the Treasury's preliminary economic forecasts show an economic growth outlook that is, on average, weaker than the Budget forecasts<br>**Note** core Crown tax revenue is cumulatively $4.6 billion lower over the four years to June 2023, reflecting the weaker economic outlook<br>**Refer** this report to Associate Ministers of Finance | Budget Matters meeting, Tuesday 22 October 2019 |

## Contact for telephone discussion (if required)

| **Name** | **Position** | **Telephone** | | **1st Contact** |
|---|---|---|---|---|
| Harrison Steiner-Fox | Analyst, Forecasting | s9(2)(k) | N/A (mob) | ✓ |
| Peter Gardiner | Manager, Forecasting, Modelling and Research | | s9(2)(g)(ii) | |

## Minister's Office actions

**Return** the signed report to Treasury.

If agreed, **refer** a copy of this report to Associate Ministers of Finance.

| Note any feedback on the quality of the report | |
|---|---|

**Enclosure**: No

# **Treasury Report:** HYEFU 2019 Preliminary Economic and Tax Forecasts

## Executive Summary

This report provides an overview of the Treasury's preliminary Half Year 2019 economic and tax forecasts, which underpin the preliminary fiscal forecasts currently being compiled. There will be an opportunity to discuss the preliminary economic and tax forecasts, and fiscal strategy in light of the economic and tax forecasts, with officials at Budget Matters on Tuesday 22 October. You will receive information on the preliminary fiscal forecasts in the week beginning 29 October.

You will receive fiscal strategy advice on Wednesday 30 October that takes into account preliminary economic, tax and fiscal forecasts. A decision on fiscal options is needed by 4 November in order to incorporate any fiscal policy decisions into the final economic forecasts.

This report also includes a summary of our talks with businesses in September (see Annex 2) and the implications of changes to forecast assumptions for fiscal projections in the Fiscal Strategy Model (see page 13 and Annex 3: Implications of forecasts for the Fiscal Strategy Model). Changes to forecast assumptions include a higher net migration and a slower increase in productivity growth relative to BEFU 2019, reflecting historical trends. The combined effect of these changes has little impact on projected fiscal indicators. You will receive a report recommending updates to the Fiscal Strategy Model in late November.

***The economic outlook has softened…***

**Relative to the Budget Economic and Fiscal Update (BEFU) 2019, the outlook for the New Zealand economy is weaker reflecting recent declines in business and consumer sentiment, a softer global outlook, and heightened global uncertainty.** These factors drive lower growth in business investment, household consumption and services exports. On the supply side, this is reflected as slower productivity growth relative to BEFU.

**Annual GDP growth is forecast to average 2.4% over the four years to June 2023 compared with 2.7% at BEFU 2019.** On a per capita basis, the average is 0.9% compared with 1.3% at BEFU.

The weaker outlook flows through to nominal GDP, with tax revenue cumulatively $4.6 billion lower.

**GDP growth slows modestly to 2.2% in 2019/20 reflecting lower household consumption and service exports.** However, an increase in government spending, consistent with the BEFU forecasts, provides a partial offset. GDP growth is forecast to pick up to 2.6% in 2020/21 supported by low interest rates, rising house prices and a modest recovery in trading partner growth. These factors help to support household consumption and business investment growth.

Beyond 2020/21, growth eases slightly to 2.4% and remains flat thereafter as the impulse from government spending wanes, population growth continues to slow, placing downward pressure on residential investment growth, and productivity growth rises. Relative to BEFU, the pickup in GDP growth is delayed and lower.

**Table 1: Forecast summary**

| June years | | 2019 Actual | 2020 Forecast | 2021 Forecast | 2022 Forecast | 2023 Forecast | 2024 Forecast | 5-year total |
|---|---|---|---|---|---|---|---|---|
| Economic growth[1] | Budget | 2.4 | 3.0 | 2.8 | 2.4 | 2.4 | - | |
| | **Half Year** | 2.4 | 2.2 | 2.6 | 2.4 | 2.4 | 2.5 | |
| Economic growth per capita[1] | Budget | 0.7 | 1.5 | 1.5 | 1.3 | 1.2 | - | |
| | **Half Year** | 0.8 | 0.7 | 1.1 | 1.0 | 1.1 | 1.2 | |
| Unemployment rate[2] | Budget | 4.2 | 4.0 | 4.1 | 4.2 | 4.3 | - | |
| | **Half Year** | 3.9 | 4.1 | 4.3 | 4.3 | 4.3 | 4.3 | |
| CPI inflation[3] | Budget | 1.7 | 2.0 | 2.1 | 2.0 | 2.0 | - | |
| | **Half Year** | 1.7 | 1.8 | 1.9 | 2.0 | 2.0 | 2.0 | |
| 90-day bank bill rate | Budget | 1.8 | 1.9 | 2.3 | 2.5 | 2.6 | - | |
| | **Half Year** | 1.7 | 0.7 | 0.7 | 0.9 | 1.1 | 1.3 | |
| Current account balance[4] | Budget | -3.4 | -3.4 | -3.4 | -3.3 | -3.3 | - | |
| | **Half Year** | -3.4 | -3.0 | -3.2 | -3.3 | -3.3 | -3.4 | |
| Nominal GDP[5] | Budget | 3.8 | 5.7 | 5.4 | 4.8 | 4.6 | - | |
| | **Half Year** | 3.7 | 5.2 | 4.8 | 4.9 | 4.9 | 4.8 | |
| Nominal GDP ($billions) | Budget | - | 317.0 | 334.0 | 350.2 | 366.6 | - | |
| | **Half Year** | 300.1 | 315.6 | 330.8 | 347.0 | 364.0 | 381.4 | |
| | Change | - | -1.4 | -3.2 | -3.2 | -2.6 | - | -10.3 |
| Tax revenue ($billions) | Budget | | 89.2 | 95.1 | 100.2 | 105.6 | - | |
| | **Half Year** | 86.5 | 88.8 | 94.0 | 98.5 | 104.1 | 110.1 | |
| | Change | - | -0.4 | -1.1 | -1.6 | -1.5 | - | -4.6 |

1. Production GDP, annual average % change 2. June quarter 3. Annual % change 4. Annual as % of GDP 5. Expenditure measure, annual average % change

***…although we forecast continued resilience in the labour market.***

**The labour market is expected to remain tight despite the weaker growth outlook relative to BEFU 2019.** The unemployment rate is forecast to rise from 3.9% in 2018/19 to 4.1% in 2019/20, reflecting slowing employment growth. Thereafter the unemployment rate gradually increases to 4.3%. Wage growth remains elevated relative to recent history supported by a tight labour market and government labour market policies.

***The weaker global economy still presents risks.***

**Risks to the international outlook remain prevalent and skewed to the downside**. We assume growth in our top 16 trading partners falls from 3.8% in 2018 to 3.1% in 2019, before making a modest recovery. A more severe slowing in global growth is a key risk to the forecasts. Such a slowdown could be triggered by a weakening in global labour markets and household incomes, a further escalation in trade tensions, or a major adjustment in global financial or equity markets.

These events could have large spill-over effects due to the interconnectedness of the global economy, leading to a sharper and broader decline in trading partner growth. The New Zealand economy would be impacted through a range of channels including reduced demand for exports, export commodity price movements, lower confidence and shifts in financial conditions and asset prices.

## Recommended Action

We recommend that you:

a **note** the Treasury's preliminary HYEFU economic forecasts show an economic growth outlook that is, on average, weaker than BEFU 2019. Annual GDP growth is forecast to average 2.4% over the four years to June 2023, compared with 2.7% forecast at BEFU 2019

b **note** preliminary tax forecasts show core Crown tax revenue is cumulatively $4.6 billion lower over the four years to June 2023 compared with BEFU 2019, largely reflecting a weaker economic outlook

c **note** that fiscal strategy advice will be provided to you on 30 October and will incorporate the preliminary economic, tax and fiscal forecasts and will set out short and medium-term fiscal impacts based on these forecasts, and

d **refer** this report to:

- Hon Dr David Clark, Associate Minister of Finance

*Refer/not referred.*

- Hon David Parker, Associate Minister of Finance

*Refer/not referred.*

- Hon Shane Jones, Associate Minister of Finance

*Refer/not referred.*

- Hon James Shaw, Associate Minister of Finance

*Refer/not referred.*

Peter Gardiner
**Manager**

Hon Grant Robertson
**Minister of Finance**

**BUDGET-SENSITIVE**

# Treasury Report: HYEFU 2019 Preliminary Economic and Tax Forecasts

## Purpose and Context of Report

1. This report provides an overview of the Treasury's preliminary Half Year 2019 economic and tax forecasts. This report is one of several reports (Table 2) you will receive over the next two months in the lead up to the publication of the Half Year Economic and Fiscal Update (HYEFU) 2019 and Budget Policy Statement (BPS) on 11 December.

**Table 2: Reports and points of engagement for HYEFU 2019**

| Reports/briefings | Budget Matters | Date |
|---|---|---|
| Preliminary economic and tax forecasts | | 17 October |
| | Preliminary economic and tax forecasts | 22 October |
| Preliminary fiscal forecasts | | Week beginning 29 October |
| Road check report (fiscal strategy advice) | | 30 October |
| Decision due for fiscal options | | 4 November |
| Specific Fiscal Risks | | 15 November |
| Final economic and tax forecasts | | Week beginning 18 November |
| | Final economic and tax forecasts, Specific Fiscal Risks | 20 November |
| Final fiscal forecasts | | Week beginning 25 November |
| Fiscal Strategy Model assumptions | | Late November |
| HYEFU 2019 chapters | | Early December |
| | Final fiscal forecasts | 3 December |
| HYEFU & BPS release date | | 11 December |

2. There will be an opportunity to discuss the economic and tax forecasts, and fiscal strategy in light of the economic and tax forecasts, with officials at Budget Matters on Tuesday 22 October. These economic and tax forecasts underpin the preliminary fiscal forecasts that are currently being compiled. You will receive information on the preliminary fiscal forecast in the week beginning 29 October.

3. You will receive fiscal strategy advice on Wednesday 30 October that takes into account the preliminary economic, tax and fiscal forecasts. Your decision on fiscal options is needed by 4 November in order to incorporate any fiscal implications into the final economic forecasts.

4. The final HYEFU forecasts will reflect any fiscal decisions you take following the fiscal strategy advice. In addition, they will include updated economic information, in particular September quarter 2019 CPI and labour market data.

5. Annex 1 of this report provides tables with additional details on the economic forecasts including the changes since the Budget Economic and Fiscal Update (BEFU) forecasts.

6. This report also includes a summary of our talks with businesses in September (see Annex 2) and the implications of changes to forecast assumptions for fiscal projections in the Fiscal Strategy Model (see page 13 and Annex 3).

## Economic developments since BEFU 2019

7. **On balance, economic data released since BEFU point to a weaker near-term outlook for the New Zealand and global economies**. A further deterioration in survey measures of activity[1], weaker than expected household consumption growth, re-emergence of trade tensions, and downgrades to the global outlook point to a further easing of growth over the second half of 2019.

8. We now forecast combined growth over the final two quarters of 2019 of 1.0%, down from 1.6% at BEFU.

9. **The global outlook is expected to be softer.** An intensification of US-China trade tensions and broader concerns around the possibility of a global recession have weighed on export oriented sectors, particularly manufacturing, and led to broader declines in business sentiment and confidence globally. An easing in global monetary conditions will help to offset some of these developments. In addition, robust consumer spending supported by resilient labour market conditions has so far placed a floor on the extent of any global slowdown.

10. Reflecting the weaker economic outlook, the Reserve Bank's Monetary Policy Committee has reduced the Official Cash Rate (OCR) by 75 basis points since BEFU to support economic activity and the achievement of its inflation and employment targets. Other supportive domestic factors include strong growth in residential building consents over the first half of 2019, which should see rising residential investment growth over the second half of 2019, rising wage inflation and a low unemployment rate supporting household spending, and continued demand for New Zealand's commodity exports.

11. **Our talks with businesses in late September found that businesses were generally expecting continued growth, albeit at slower rates than the recent past (see Appendix 2).** While the tone was more positive than survey measures, businesses also expressed considerable uncertainty about the outlook. This uncertainty was creating a reluctance to invest despite low interest rates and good credit conditions.

12. Factors weighing on investment intentions included an expected slowing in global demand; the recent 50 basis point Official Cash Rate cut being perceived as a signal that the economy is slowing more than expected; capacity constraints in the construction sector making it difficult to take on new projects; concerns over government policy; and uncertainty regarding the future pipeline of public infrastructure projects. The Zero Carbon Bill and the Essential Freshwater changes were cited frequently as key policy uncertainties, particularly in the agricultural sector.

13. The Treasury will publish a summary of these business talks in the November Monthly Economic Indicators. This is consistent with past practice.

[1] The September 2019 Quarterly Survey of Business Opinion (QSBO) points to a sharp deterioration in GDP growth for the September quarter. However, the Treasury's broader indicators of GDP growth suggest GDP growth in the 0.3-0.4% range.

## Economic Outlook

***GDP growth has slowed over the past three years reflecting a mix of factors…***

14. Economic growth has progressively eased from above trend growth of just below 4.0% over 2016 to 2.4% in the year ended June 2019. Slowing migration-led population growth, falling house price inflation and the winding-down of Kaikōura and Canterbury earthquake-related investment have contributed to this slowing.

15. More recently, global growth has also slowed and become increasingly uncertain, impacting on businesses' willingness to invest and spending by foreign consumers on more discretionary areas, such as tourism. Capacity constraints in the tourism sector have also contributed. New Zealand businesses have also shown a reluctance to invest reflecting both domestic policy uncertainty and concerns about global demand.

***…and is forecast to remain broadly flat, averaging near its current rate of 2.4%.***

16. Annual economic growth averages 2.4% over the four forecast years to 2022/23 compared with 2.7% at BEFU (Figure 1). On a per capita basis, the average is 0.9% compared with 1.3% at BEFU (Figure 2).

17. Real GDP growth slows modestly to 2.2% in 2019/20 reflecting lower household consumption and service exports. However, an increase in government spending provides a partial offset.

**Figure 1: Real GDP growth**

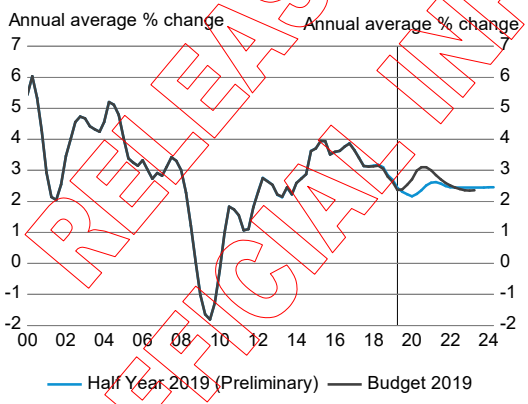
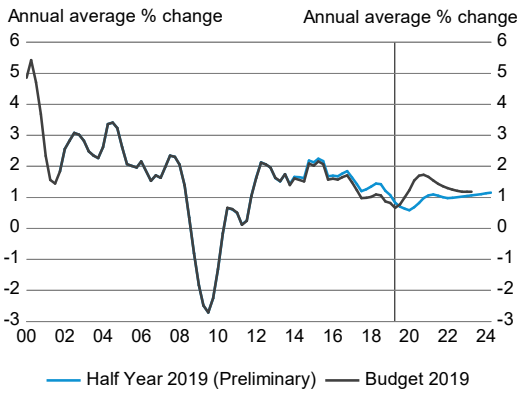



**Figure 2: Real GDP per capita growth**




18. GDP growth is forecast to pick up slightly to 2.6% in 2020/21 supported by low interest rates, rising house price inflation and a modest recovery in trading partner growth. These factors help to support household consumption growth and modest growth in business investment. Beyond 2020/21 growth eases to 2.4% and remains flat thereafter as the impulse from government spending wanes, population growth continues to slow, placing downward pressure on residential investment growth, and productivity growth rises.

***Nerves about the global economy combined with declines in business sentiment and expectations for future profitability see subdued business investment growth.***

19. As highlighted in our talks with businesses, global and domestic uncertainty, compressed margins and declining expectations for future profitability have weighed on business investment growth (Figure 3). We expect these factors will continue to limit investment growth in the near-term, outweighing the positive stimulatory effects of rising government spending.

20. High and stable commodity prices relative to recent history and low interest rates should help to reduce the risk of an outright contraction in investment activity.

21. Nevertheless, in an environment of high uncertainty, businesses are more likely to prefer expanding production through relatively temporary labour rather than risking more permanent investment.

**Figure 3: Investment indicators**

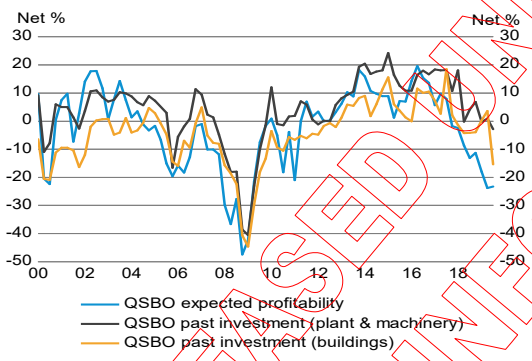
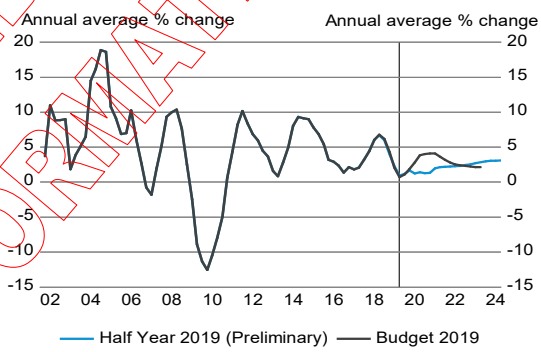



**Figure 4: Business investment growth**




22. Business investment growth is forecast to rise gradually from 1.4% in 2019/20 to 3.1% in 2023/24, as firms respond to low interest rates, a slowing labour supply, rising labour costs and a small recovery in global growth (Figure 4).

23. Business investment is a more cyclical and unpredictable component of GDP and can turn in either direction relatively quickly. There is a risk that uncertainty and sentiment have a greater impact on business investment leading to a contraction in activity. Conversely, global risks and uncertainty could unwind spurring business investment growth.

***Inflation returns only gradually to 2.0% by 2020/21…***

24. We forecast inflation to return more gradually to 2.0%, with a weaker outlook for non-tradables inflation than at BEFU. While global weakness dampens international prices of traded goods, a lower New Zealand dollar outweighs this, resulting in slightly higher tradables inflation relative to BEFU.

***…and combined with slowing GDP growth, sees the Reserve Bank provide additional monetary stimulus…***

25. The 90-day bank bill rate is forecast to fall from around 1.3% in September 2019 to 0.7% by late 2019/20 (Figure 5). This outlook is consistent with market pricing at the time of finalisation, which fully captured two 25 basis point reductions in the OCR. Interest rates are then forecast to stay on hold until 2021/22, rising modestly from 2021/22.

**Figure 5: 90-day bank bill rate**

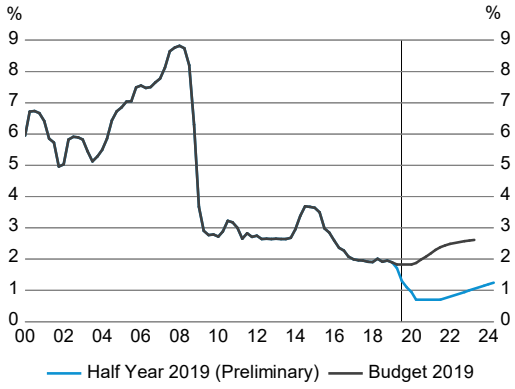
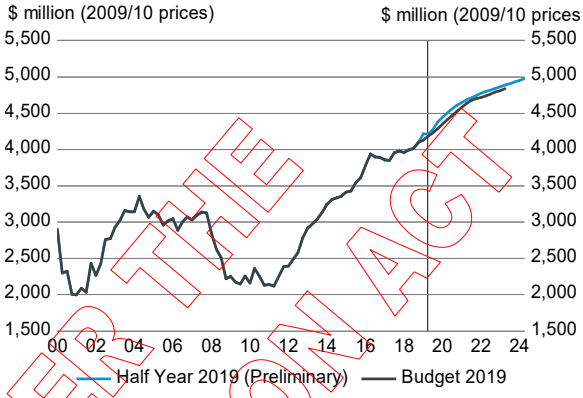



**Figure 6: Real residential investment**




***…which supports house price inflation and together with a steady pipeline of consented activity, sees rising residential investment growth.***

26. Low interest rates, rising house prices, and a steady pipeline of consented activity see residential investment growth rise from 4.0% in 2018/19 to 6.5% in 2019/20. Residential investment growth then slows to 1.8% by 2023/24 as population growth continues to decline and the Reserve Bank gradually increases interest rates to contain inflation.

27. The overall level of residential investment is higher relative to BEFU 2019 (Figure 6). This reflects a mix of a higher starting point, stronger population growth and lower interest rates relative to BEFU 2019.

28. The government makes a material contribution to housing investment over the forecast period, with investment of just over $8 billion through to June 2024.

***After slowing in the near-term, faster labour income growth and house price growth support household spending.***

29. Employment growth has been slowing in recent years reflecting easing economic growth. In the near-term, slowing economic growth is expected to continue to affect hiring decisions seeing employment growth slow to 1.6% in 2019/20, weighing on household consumption.

30. Beyond 2019/20, a modest increase in economic growth sees employment growth rise, and together with rising house price growth, support an increase in household consumption growth from 2.3% in 2019/20 to 2.8% in 2023/24 (Figure 7). Private consumption growth remains low relative to recent years as households are cautious given the uncertain outlook and elevated debt to income ratios, and because population growth is lower.

**Figure 7: Real private consumption**

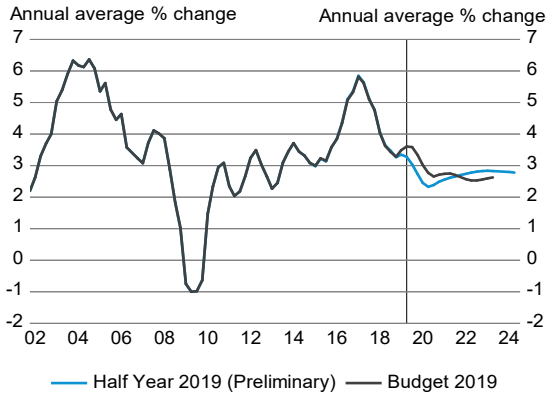
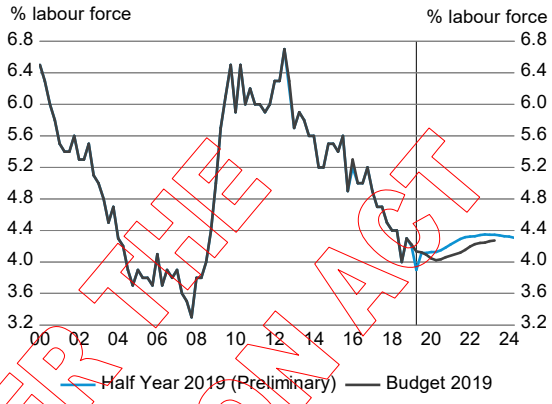



**Figure 8: Unemployment rate**




31. **The labour market is expected to remain tight despite the weaker growth outlook relative to BEFU 2019.** We forecast the unemployment rate to rise from 3.9% in 2018/19 to 4.1% in 2019/20 (Figure 8), reflecting slowing employment growth. Thereafter the unemployment rate gradually increases to 4.3%. Wage growth remains elevated relative to recent history supported by a tight labour market and government labour market policies.

***Trading partner growth slows owning to ongoing trade tensions and uncertainty regarding future demand…***

32. Relative to BEFU, heightened global policy uncertainty (Figure 9), concerns about future demand, and an intensification of trade tensions sees forecast trading partner growth weaker in the near-term. Trading partner growth is forecast to decline from 3.8% in 2018 to 3.1% in 2019 before gradually rising to 3.4% (Figure 10). This compares to a post-GFC average of 3.8%.

**Figure 9: Global uncertainty indexes**

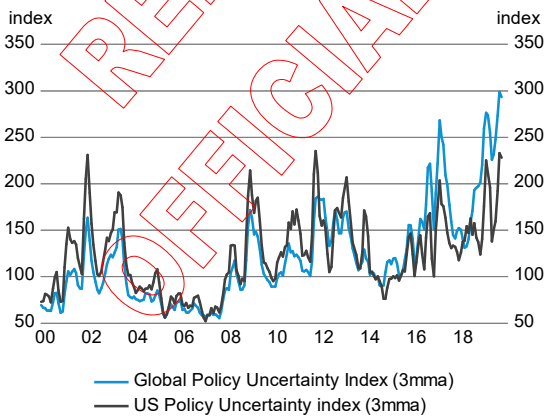
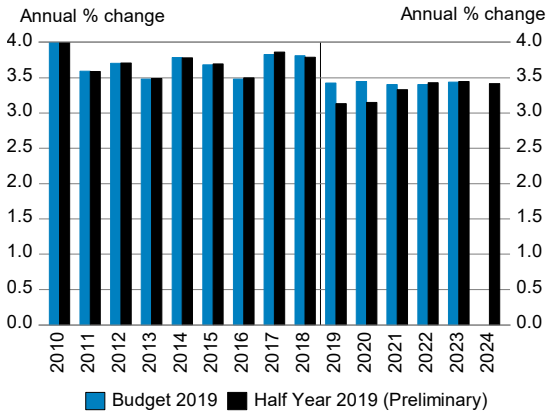



**Figure 10: trading partner growth**



***…while demand for New Zealand's commodity exports remains robust, the weakening world outlook impacts tourism.***

33. To date the direct impacts of softening global growth on New Zealand appear to have been relatively muted. The slowdown in global trade growth has largely been centred on manufacturing and investment goods. Global labour markets and household consumption have remained resilient supporting demand for New Zealand's commodity exports, which are predominantly consumption goods. The preliminary HYEFU forecasts expect the robustness in household spending to continue.

34. Meat export price growth is projected to accelerate as Chinese consumers seek alternative protein options to pork, for which stocks have been reduced by African swine fever. Dairy prices have come off their recent peak, however continued solid demand should see modest increases in prices over the forecast period.

35. While much of the impact of global jitters on the New Zealand economy have been indirect through its influence on confidence and therefore investment, weaker demand for services exports, particularly tourism, represents a key direct link. Tourism growth is forecast to remain subdued in the near-term, which is the largest contributing factor to weaker export growth relative to BEFU 2019.

36. A weakening world outlook sees subdued import price inflation and combined with continued strength in goods exports prices, leaves the terms of trade elevated relative to recent history.

37. A more severe slowing in the global economy, particularly if it was to more directly impact on consumer demand, poses downside risk to these forecasts. If household incomes are materially weaker than expected then this would lead to a sharper and broader decline in trading partner growth. The New Zealand economy would be impacted through a range of channels including reduced demand for exports, export commodity price movements, lower confidence and shifts in financial conditions and asset prices.

***Weaker nominal GDP is a driver of lower tax relative to BEFU.***

38. Relative to BEFU 2019, lower economic growth and a more gradual increase in CPI inflation to 2.0% sees nominal GDP – a key driver of tax revenue – a cumulative $10.3 billion lower over the four years to June 2023.

## Tax Outlook

39. Core Crown tax revenue for the year ending June 2019 was $1.8 billion above BEFU 2019 forecast. $1.1 billion of this variance was in other persons tax, the remaining $0.7 billion variance was broad-based across all tax types excluding GST. Part of the variance in other persons tax was timing in nature and arose from underestimation of the impact on revenue of Inland Revenue moving the administration of income taxes from its old FIRST system to its new START system in April.

40. We consider that $0.5 billion of the $1.8 billion starting point variance reflects timing and other technical issues that will not persist. We have made a judgement that the remaining variance persists through the forecast period.

41. Despite the higher starting point for tax revenue, lower forecasts for nominal GDP growth and interest rates result in lower aggregate tax forecasts throughout the forecast period (Table 3).

42. In addition to the $4.4 billion of forecasting changes, policy and administrative changes reduce tax revenue by around $0.2 billion over the forecast period.

**Table 3: Estimated[2] change in core Crown tax revenue since BEFU 2019**

| June years, $ billions | 2019 | 2020 | 2021 | 2022 | 2023 | 2024 | Totals | 5-yr totals (inc 2019) |
|---|---|---|---|---|---|---|---|---|
| 2019 BEFU | 84.7 | 89.2 | 95.1 | 100.2 | 105.6 | | | |
| % of GDP | 28.2 | 28.2 | 28.5 | 28.6 | 28.8 | | | |
| *Forecasting changes by tax type:* | | | | | | | | |
| RWT on interest | +0.0 | -0.2 | -0.7 | -1.2 | -1.2 | | -3.3 | -3.3 |
| GST | -0.1 | -0.3 | -0.5 | -0.5 | -0.4 | | -1.7 | -1.8 |
| Corporate tax | +0.4 | -0.1 | -0.2 | -0.3 | -0.2 | | -0.9 | -0.5 |
| Net other persons tax | +1.1 | -0.2 | +0.1 | +0.1 | +0.1 | | +0.1 | +1.1 |
| Source deductions | +0.2 | +0.3 | +0.2 | +0.2 | +0.3 | | +1.0 | +1.2 |
| All other taxes | +0.2 | +0.1 | +0.1 | +0.2 | +0.2 | | +0.5 | +0.7 |
| ***Total forecasting change*** | ***+1.8*** | ***-0.4*** | ***-1.1*** | ***-1.6*** | ***-1.4*** | | ***-4.4*** | ***-2.6*** |
| Policy changes | - | -0.1 | -0.0 | -0.1 | -0.1 | | -0.2 | -0.2 |
| *Total change* | *+1.8* | *-0.4* | *-1.1* | *-1.6* | *-1.5* | | *-4.6* | *-2.8* |
| **2019 Half-year Update prelim** | **86.5** | **88.8** | **94.0** | **98.5** | **104.1** | **110.1** | | |
| % of GDP | 28.8 | 28.1 | 28.4 | 28.4 | 28.6 | 28.9 | | |
| *Changes by principal driver:* | | | | | | | | |
| Macroeconomic effects | -0.3 | -1.0 | -1.5 | -1.4 | -1.1 | | -4.9 | -5.2 |
| Interest rates (RWT) | +0.0 | -0.2 | -0.7 | -1.0 | -1.0 | | -2.8 | -2.8 |
| Policy changes | - | -0.1 | -0.0 | -0.1 | -0.1 | | -0.2 | -0.2 |
| Other factors | +2.1 | +0.8 | +1.1 | +0.8 | +0.7 | | +3.4 | +5.5 |
| *Total change* | *+1.8* | *-0.4* | *-1.1* | *-1.6* | *-1.5* | | *-4.6* | *-2.8* |
| *Nominal GDP* | | | | | | | | |
| 2019 BEFU | 299.7 | 317.0 | 334.0 | 350.2 | 366.6 | | | |
| 2019 Half-year Update prelim | 300.1 | 315.6 | 330.8 | 347.0 | 364.0 | 381.4 | | |
| *Total nominal GDP change* | *+0.4* | *-1.4* | *-3.2* | *-3.2* | *-2.6* | | *-10.3* | *-10.0* |

43. Inland Revenue has also prepared a set of tax forecasts, based on the Treasury's economic forecasts, but using their own tax forecasting models and judgements. Across the five years of the forecast period, the Treasury's forecasts are in total $0.7 billion higher than Inland Revenue's, equivalent to around 0.1% of total tax revenue (Table 4).

[2]Fully consolidated core Crown tax revenue for HYEFU 2019 was not available at the time this document was written. We have estimated core Crown tax revenue using BEFU 2019 eliminations.

**Table 4: Differences between the Treasury and Inland Revenue forecasts**

| June years, $ billions | 2020 | 2021 | 2022 | 2023 | 2024 | 5-yr total |
|---|---|---|---|---|---|---|
| Treasury forecast | 88.8 | 94.0 | 98.5 | 104.1 | 110.1 | |
| Inland Revenue forecast | 89.1 | 93.9 | 98.3 | 104.0 | 109.6 | |
| *Treasury less Inland Revenue* | *-0.2* | *+0.1* | *+0.2* | *+0.1* | *+0.5* | *+0.7* |
| *Percentage difference* | *-0.3%* | *0.1%* | *0.2%* | *0.1%* | *0.5%* | *0.1%* |

## Key Judgements and Government Policy Changes

44. Since the publication of BEFU 2019, we have received additional data and information that has challenged our judgements regarding migration, productivity, neutral interest rates, and pay equity. As a result, we have made the following changes outlined below.

45. **Migration:** annual migration is higher than forecast at BEFU 2019. We expected labour market conditions to remain favourable relative to Australia, slowing the growth in net outflows of New Zealand citizens. Non-New Zealand citizen net inflows are expected to remain higher than historical averages, as demand for education services continues and domestic labour shortages persist.

46. Annual net migration is assumed to decline from 50,000 in September 2018 to 35,000 by June 2024, compared with BEFU 2019 where annual net migration was assumed to decline from 50,000 in June 2018 to 25,000 by June 2022. Migration contributes 72,000 more people to the population by the end of the forecast period.

47. **Labour productivity:** these forecasts assume a pickup in annual labour productivity growth from 0.5% in 2018/19 to 1.0% by 2023/24. This represents less of a pickup than forecast at BEFU. Relatively slow productivity growth has been a feature of the global economy since the Global Financial Crisis.

48. Over the forecast period, the GDP growth impact of the upward revision to migration broadly offsets the impact of the downward revision to labour productivity. However, the impact on GDP per capita growth is negative.

49. The Treasury is reviewing its long-run labour productivity growth assumption (currently 1.5% per year) as part of the development of the Long-term Fiscal Statement (LTFS) 2020 [T2019/2766 refers]. In the LTFS, the Treasury is likely to update the assumption to 1.2%, which is the median over the past 30 years.

50. Labour productivity growth is also a key assumption in the medium-term fiscal projections generated by the Fiscal Strategy Model (FSM). Preliminary FSM results suggest the overall impact of changing the labour productivity growth assumption on GDP growth and fiscal aggregates (as a share of GDP) is small, when combined with the impact of the higher net migration on population. Further information is contained in Annex 1.

51. You will receive fiscal strategy advice on Wednesday 30 October that incorporates the preliminary economic, tax and fiscal forecasts. The medium-term fiscal projections in this advice will be based on the updated labour productivity growth and net migration assumptions described in Annex 3.

52. We view these assumptions as the most appropriate for making policy judgments, but it will be your decision as to which assumptions are published in the FSM and Budget Policy Statement in December. We will provide detailed advice on the assumptions in November.

53. **Neutral interest rates:** an important judgement relates to how stimulatory (the extent to which a reduction in interest rate motivates increased investment, consumption and supports exports through a lower exchange rate) a given interest rate is. As interest rates have been low for a prolonged period of time economists in New Zealand and abroad have been reassessing their estimates of what rate of interest is "neutral" in the sense that it is consistent with a fairly stable and on-target rate of inflation.

54. Based on internal Treasury research, we have lowered our own assumption of the long-run neutral interest rate from 3.75% at BEFU to 3.0%. The effect is interest rates need to rise at a slower rate and to a lower level than previously expected to contain inflation. We will publish a summary of this research in the October Monthly Economic Indicators.

55. **Pay equity.** These forecasts include the economic impacts of updated pay equity estimates [TR 2019/3037 refers]. The total increase relative to BEFU of around $200 million over the four years to 2022/23 is small relative to the total economy wage bill.

**BUDGET-SENSITIVE**

## Annex 1: Forecast Summary Tables

### Table A1: Summary of economic forecasts – June years

| June Years | 2016 | 2017 | 2018 | 2019 | 2020 Forecast | 2021 Forecast | 2022 Forecast | 2023 Forecast | 2024 Forecast |
|---|---|---|---|---|---|---|---|---|---|
| Private consumption | 4.4 | 5.6 | 3.6 | 3.3 | 2.3 | 2.6 | 2.8 | 2.8 | 2.8 |
| Public consumption | 1.5 | 2.6 | 2.9 | 2.1 | 3.6 | 2.3 | 1.3 | 1.1 | 1.1 |
| **TOTAL CONSUMPTION** | **3.7** | **4.9** | **3.5** | **3.0** | **2.6** | **2.5** | **2.4** | **2.4** | **2.4** |
| Residential investment | 9.9 | 4.2 | 2.6 | 4.0 | 6.5 | 5.1 | 2.9 | 2.0 | 1.8 |
| Business investment* | 2.4 | 2.1 | 6.7 | 0.9 | 1.4 | 2.1 | 2.3 | 2.8 | 3.1 |
| **TOTAL INVESTMENT** | **4.2** | **2.6** | **5.6** | **1.7** | **2.8** | **2.9** | **2.5** | **2.6** | **2.7** |
| Stocks (contribution to GDP growth) | -0.3 | 0.3 | -0.1 | -0.2 | 0.0 | 0.1 | 0.0 | 0.0 | 0.0 |
| **GROSS NATIONAL EXPENDITURE** | **3.4** | **4.7** | **4.0** | **2.4** | **2.7** | **2.6** | **2.5** | **2.5** | **2.5** |
| Exports | 5.7 | 0.6 | 3.9 | 2.5 | 1.4 | 2.5 | 2.4 | 2.3 | 2.3 |
| Imports | 1.2 | 6.2 | 8.0 | 1.7 | 1.8 | 2.9 | 2.7 | 2.6 | 2.4 |
| **EXPENDITURE ON GDP** | **4.5** | **3.1** | **3.0** | **2.6** | **2.6** | **2.5** | **2.4** | **2.4** | **2.4** |
| **GDP (PRODUCTION MEASURE)** | **3.6** | **3.4** | **3.2** | **2.4** | **2.2** | **2.6** | **2.4** | **2.4** | **2.5** |
| *- annual % change, June quarter* | 4.0 | 3.1 | 3.2 | 2.1 | 2.4 | 2.5 | 2.4 | 2.4 | 2.5 |
| **Other Output Measures** | | | | | | | | | |
| Real Gross National Disposable Income | 3.8 | 4.3 | 3.5 | 2.2 | 3.1 | 2.4 | 2.4 | 2.4 | 2.4 |
| Nominal GDP (Expenditure Basis) | 5.1 | 6.3 | 5.7 | 3.7 | 5.2 | 4.8 | 4.9 | 4.9 | 4.8 |
| Potential GDP | 3.0 | 2.9 | 2.8 | 2.7 | 2.6 | 2.6 | 2.5 | 2.5 | 2.5 |
| Output gap (June qtr,% of potential) | 0.3 | 0.5 | 0.9 | 0.4 | 0.2 | 0.2 | 0.1 | 0.0 | -0.0 |
| **Total Population (thousands)** | 4,634 | 4,725 | 4,806 | 4,882 | 4,958 | 5,033 | 5,106 | 5,176 | 5,242 |
| **Real GDP per capita (Production basis)** | 1.7 | 1.4 | 1.4 | 0.8 | 0.7 | 1.1 | 1.0 | 1.1 | 1.2 |
| **Labour Market** | | | | | | | | | |
| Employment | 2.2 | 4.8 | 3.1 | 1.7 | 1.6 | 2.0 | 1.8 | 1.7 | 1.5 |
| Unemployment Rate (June quarter) | 5.0 | 4.7 | 4.4 | 3.9 | 4.1 | 4.3 | 4.3 | 4.3 | 4.3 |
| Labour Productivity (Hours worked basis) | 0.8 | -1.2 | -0.6 | 1.2 | 0.4 | 0.7 | 0.8 | 0.9 | 1.0 |
| Wages (QES average hourly ord time earnings, APC) | 2.1 | 1.6 | 3.0 | 4.4 | 3.4 | 3.3 | 3.4 | 3.5 | 3.5 |
| **Monetary Conditions** | | | | | | | | | |
| 90-day Bank Bill Rate (June quarter ave) | 2.4 | 2.0 | 2.0 | 1.7 | 0.7 | 0.7 | 0.9 | 1.1 | 1.3 |
| 10-year Bond Rate (June quarter ave) | 2.7 | 2.9 | 2.8 | 1.8 | 0.9 | 1.1 | 1.4 | 1.8 | 2.1 |
| TWI (June quarter ave) | 73.6 | 76.5 | 73.8 | 72.7 | 70.0 | 70.0 | 70.9 | 71.7 | 72.5 |
| - annual % change (June quarter) | -3.4 | 3.9 | -3.5 | -1.5 | -3.7 | 0.0 | 1.3 | 1.2 | 1.1 |
| **Price Measures** | | | | | | | | | |
| CPI Inflation (ann % change, June quarter) | 0.4 | 1.7 | 1.5 | 1.7 | 1.8 | 1.9 | 2.0 | 2.0 | 2.0 |
| Consumption Deflator | 0.8 | 0.9 | 1.3 | 1.7 | 1.7 | 2.4 | 2.4 | 2.3 | 2.1 |
| GDP Deflator | 0.6 | 3.1 | 2.7 | 1.0 | 2.6 | 2.2 | 2.5 | 2.4 | 2.3 |
| House Price Inflation (ann % change, June qtr) | 15.0 | 6.5 | 3.6 | 0.9 | 4.4 | 6.4 | 6.4 | 5.8 | 5.0 |
| **Key Balances** | | | | | | | | | |
| Current account balance ($ million) | -5,423 | -7,046 | -9,597 | -10,296 | -9,536 | -10,750 | -11,456 | -12,056 | -12,792 |
| Current account balance (% of GDP) | -2.1 | -2.6 | -3.3 | -3.4 | -3.0 | -3.2 | -3.3 | -3.3 | -3.4 |
| Terms of Trade (goods) - SNA Basis | -2.7 | 5.0 | 4.6 | -3.4 | 1.6 | -0.4 | 0.1 | 0.2 | 0.2 |
| Household saving ratio (% of HHDI, June yr) | -0.6 | 0.1 | -1.4 | -0.6 | 0.9 | 0.7 | 0.2 | 0.0 | 0.2 |
| Net International Investment Position (%GDP) | -62.1 | -55.0 | -53.4 | -55.3 | -55.6 | -56.3 | -56.9 | -57.6 | -58.3 |

* Total investment excluding residential

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## Table A2: Change in economic forecasts from Budget – June years

| June Years | 2016 | 2017 | 2018 | 2019 | 2020 Forecast | 2021 Forecast | 2022 Forecast | 2023 Forecast |
|---|---|---|---|---|---|---|---|---|
| Private consumption | 0.0 | 0.0 | 0.0 | -0.3 | -0.6 | -0.3 | 0.1 | 0.1 |
| Public consumption | -0.0 | -0.0 | -0.1 | 0.2 | -0.6 | 0.5 | 0.4 | 0.1 |
| **TOTAL CONSUMPTION** | **0.0** | **0.0** | **-0.0** | **-0.2** | **-0.6** | **-0.1** | **0.2** | **0.1** |
| Residential investment | -0.0 | -0.0 | 0.0 | 0.6 | 1.3 | -0.3 | -0.5 | 0.0 |
| Business investment* | -0.0 | 0.0 | -0.1 | 0.2 | -2.4 | -1.5 | -0.1 | 0.7 |
| **TOTAL INVESTMENT** | **-0.0** | **0.0** | **-0.0** | **0.3** | **-1.4** | **-1.1** | **-0.2** | **0.5** |
| Stocks (contribution to GDP growth) | 0.0 | -0.0 | -0.0 | -0.1 | 0.1 | 0.0 | 0.0 | 0.0 |
| **GROSS NATIONAL EXPENDITURE** | **0.0** | **0.0** | **-0.0** | **-0.3** | **-0.4** | **-0.5** | **0.1** | **0.2** |
| Exports | 0.3 | 0.3 | 0.3 | -0.3 | -1.6 | -0.3 | -0.2 | -0.2 |
| Imports | 0.1 | 0.0 | 0.1 | -0.4 | -2.2 | -0.5 | 0.4 | 0.3 |
| **EXPENDITURE ON GDP** | **0.1** | **0.1** | **0.1** | **0.1** | **-0.6** | **-0.4** | **-0.1** | **0.0** |
| **GDP (PRODUCTION MEASURE)** | **-0.0** | **0.0** | **0.0** | **0.1** | **-0.8** | **-0.2** | **-0.0** | **0.1** |
| *- annual % change, June quarter* | *0.0* | *0.0* | *0.0* | *-0.0* | *-0.8* | *-0.1* | *0.1* | *0.1* |
| **Other Output Measures** | | | | | | | | |
| Real Gross National Disposable Income | 0.0 | -0.1 | -0.1 | -0.3 | -0.2 | -0.5 | 0.0 | 0.2 |
| Nominal GDP (Expenditure Basis) | 0.1 | 0.1 | 0.1 | -0.1 | -0.6 | -0.6 | 0.1 | 0.2 |
| **Per Capita Output Measures** | | | | | | | | |
| Real GDP per capita (Production basis) | 0.1 | 0.2 | 0.3 | 0.2 | -0.9 | -0.4 | -0.3 | -0.1 |
| Real Gross Nat. Disp Income per capita | 0.1 | 0.1 | 0.3 | -0.2 | -0.3 | -0.7 | -0.2 | -0.0 |
| Nominal GDP per capita (Expenditure basis) | 0.2 | 0.3 | 0.4 | -0.0 | -0.7 | -0.8 | -0.2 | -0.0 |
| **Labour Market** | | | | | | | | |
| Employment | -0.2 | -0.4 | -0.6 | -0.6 | -0.3 | 0.3 | 0.4 | 0.4 |
| Unemployment Rate (June quarter) | 0.0 | 0.0 | 0.0 | -0.2 | 0.1 | 0.2 | 0.1 | 0.1 |
| Labour Productivity (Hours worked basis) | 0.2 | 0.4 | 0.6 | -0.2 | 0.0 | -0.5 | -0.4 | -0.3 |
| Wages (QES average hourly ord time earnings... | -0.0 | -0.0 | 0.0 | 1.1 | 0.1 | -0.3 | -0.1 | -0.1 |
| Unit Labour Costs (Hours worked basis) | -0.2 | -0.4 | -0.6 | 0.7 | 0.8 | 0.2 | 0.3 | 0.1 |
| **Monetary Conditions** | | | | | | | | |
| 90-day Bank Bill Rate (June quarter ave) | 0.0 | 0.0 | 0.0 | -0.1 | -1.2 | -1.6 | -1.7 | -1.6 |
| 10-year Bond Rate (June quarter ave) | 0.0 | 0.0 | 0.0 | -0.1 | -1.3 | -1.4 | -1.3 | -1.2 |
| TWI (June quarter ave) | 0.0 | 0.0 | 0.0 | -1.0 | -3.7 | -3.8 | -3.1 | -2.4 |
| - annual % change, June quarter | 0.0 | 0.0 | 0.0 | -1.4 | -3.7 | -0.1 | 0.9 | 1.1 |
| **Price Measures** | | | | | | | | |
| CPI Inflation (ann % change, June quarter) | 0.0 | 0.0 | 0.0 | -0.1 | -0.2 | -0.1 | -0.1 | -0.0 |
| Consumption Deflator | -0.0 | -0.0 | 0.0 | -0.1 | -0.7 | -0.1 | 0.2 | 0.2 |
| GDP Deflator | 0.0 | -0.0 | 0.0 | -0.2 | 0.0 | -0.2 | 0.2 | 0.2 |
| House Price Inflation (ann % change, June qu... | 0.0 | 0.0 | 0.0 | -2.0 | 0.6 | 2.1 | 2.1 | 1.0 |
| **Key Balances** | | | | | | | | |
| Current account balance ($ million) | 361 | 337 | 213 | -186 | 1,229 | 678 | 244 | 103 |
| Current account balance (% of GDP) | 0.1 | 0.1 | 0.1 | -0.1 | 0.4 | 0.2 | 0.0 | 0.0 |
| Terms of Trade - SNA Basis | -0.0 | 0.0 | -0.2 | -1.5 | 1.5 | -0.5 | -0.0 | 0.1 |
| Household saving ratio (% of HHDI, March year) | 0.0 | 0.0 | 0.0 | -0.0 | 1.3 | 1.3 | 1.0 | 0.9 |

* Total investment excluding residential

## Annex 2: HYEFU 2019 Business Talks

In late September, officials from the Treasury visited a range of businesses and other organisations to discuss the outlook for the economy (a full list of businesses visited is provided in Table A2.1).

Overall, the sense gathered was that businesses are doing okay, with economic growth expected to continue albeit at a lower level. This overall picture is somewhat at odds with business confidence surveys, such as the Quarterly Survey of Business Opinion (QSBO), which indicates more of a negative sentiment among businesses. Indeed, some businesses commented on this, noting that demand from other businesses for their products is stronger than they would expect given surveyed business confidence levels.

Many businesses expressed uncertainty about the future – both in terms of the international outlook and in terms of domestic conditions. Uncertainty over future policy developments was a common theme. Businesses also commented that they are facing compressed margins – with rising costs (labour, in particular) combined with an inability to increase prices.

***Demand remains strong…***

Most businesses had a positive outlook about demand for their products. Businesses commented that residential and non-residential construction is strong, that there is good demand and high prices for agricultural products, and steady manufacturing demand. However, there was doubt expressed by some in the construction industry about future demand.

Companies in the retail and tourism sectors commented that they expect demand growth to be lower than previously, but are not expecting a fall. Some tourism businesses noted that growth in recent history had been very high, so were comfortable with the respite of a period of slower growth.

Commodity exporting businesses mentioned concern over the global economic environment (slowing worldwide growth, and uncertainty from the US/China trade war and Brexit); however, they commented that nevertheless they expect demand for their products to hold up.

***… and the labour market is very tight***

Most firms stated that it was very difficult to find labour, consistent with data from the QSBO and very low unemployment levels. Some businesses also commented that they were facing issues with delayed work visa approvals, particularly problematic where foreign labour use was particularly high (such as hospitality businesses in tourism centres).

Businesses reported that they are seeing higher than normal wage inflation due to minimum wage increases and the tight labour market more generally. Some businesses reported that the minimum wage increases have flowed on to higher wage expectations for higher-paid staff, to ensure relativities are maintained.

***Businesses are facing squeezed margins…***

Many businesses reported that they are facing squeezed margins – with rising costs but an inability to pass these on through higher prices. This inability was often attributed to the internet, due to the impact it has had on both price transparency and increased competition.

Some businesses commented that they are able to ameliorate this margin squeeze by reducing their reliance on labour (for example, in the retail sector, by increasing focus on online sales, which is a less labour-intensive sales channel) and by seeking lower-cost inputs, particularly from offshore. However, these businesses noted these measures only partially offset their margin squeeze; overall, profitability outlook is weakening.

***… and business investment is slowing…***

Businesses commented that credit conditions are generally good with very low interest rates. Despite this, most firms we visited were not planning large-scale investment in the near term. Uncertainty was a common reason for this reticence, with businesses citing factors including:

- the slow-down in expected economic growth internationally
- the August cut in the OCR by 50 basis points, with businesses taking the unexpectedly large cut as a signal that the economy is slowing more than anticipated
- capacity constraints in the construction sector making it difficult to take on new large-scale projects, and
- concern over potential changes in Government policy – with the Zero Carbon Bill and the Essential Freshwater changes being cited frequently.

A few businesses also commented that the pipeline of future major infrastructure investments is unclear. They noted that several large investments are nearing completion, and that they are unsure if there will be new projects to move onto once those are completed. These businesses expressed a risk that, without a clearer pipeline, workers will move to Australia resulting in an erosion of future capacity for large-scale infrastructure projects.

***…with sentiment among farmers particularly low.***

A common theme was that confidence among farmers was very low – due to concerns over potential changes in Government policy (water quality and climate change).

Farming businesses expressed concern about the Zero Carbon Bill and potential changes to the Emissions Trading Scheme, even though no specific climate-related policies that would directly affect them have been decided. Farmers were aware of the long-term price indications used in reports, such as the Productivity Commission report on the transition to a low carbon economy, so had a sense that emissions prices would be higher at some point in the future and that they would be exposed to those prices.

Farming businesses also mentioned that commodity prices are elevated at present, creating some room to absorb costs from new regulations. However, they noted that commodity prices are volatile, so there is concern about the impact of any new regulations when prices inevitably fall.

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**BUDGET-SENSITIVE**

## Annex 3: Implications of forecasts for the Fiscal Strategy Model

The Fiscal Strategy Model (FSM) is used to generate the medium-term fiscal projections published in the Fiscal Strategy Report required under the Public Finance Act 1989. The Act does not require the publication of fiscal projections in the Budget Policy Statement. However, the FSM is customarily published alongside the Budget Policy Statement for transparency purposes.

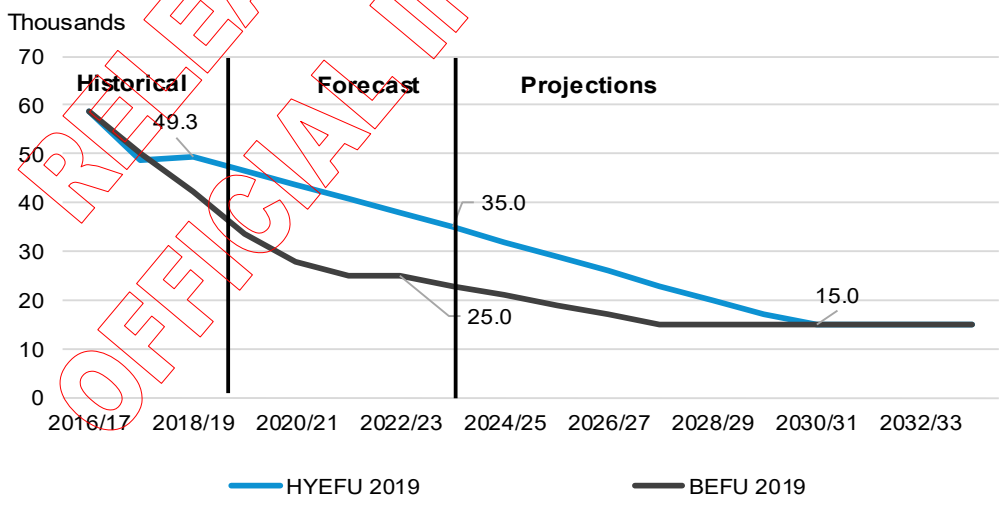
In contrast to the economic forecasts, you are responsible as the Minister of Finance for the published medium-term fiscal projections and the assumptions underpinning them. You will receive advice in November outlining the Treasury's recommendations for assumptions in the FSM and seeking your agreement to any changes to the assumptions. This advice will also include options around how the changes are communicated externally.

**Net migration is higher for longer…**

At Budget 2019, annual net migration was assumed to decline 25,000 by June 2023 (Figure A3.1). Over the projection period (2022/23 – 2032/33) annual net migration was assumed to decrease by 2,000 per annum for 5 years until it reached the long-run projection assumption of 15,000.

In the preliminary HYEFU 2019 economic forecasts, the Treasury assumes annual net migration declines to 35,000 by the end of the forecast period (2023/24). For the purpose of the medium-term fiscal projections, we propose decreasing net migration by 3,000 per annum to reach the long-run average net migration of net 15,000 by 2030/31.

**Figure A3.1 – Annual net migration**



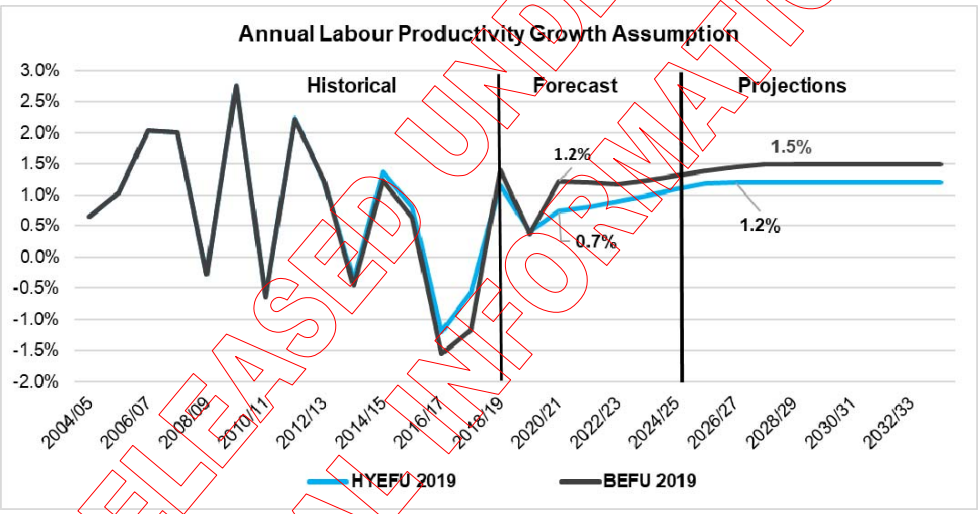

**… and labour productivity growth is lower reflecting historical trends.**

The assumption for labour productivity growth is one of the factors that determines the FSM's economic growth projections and consequently the projections of key fiscal indicators such as net core Crown debt and the Operating Balance before Gains and Losses (OBEGAL). All else equal, a higher labour productivity growth assumption leads to higher economic growth over the projection period, higher tax revenue and hence stronger fiscal position.

The FSM currently assumes labour productivity growth of 1.5% per annum (Figure A3.2). This is also the labour productivity assumption used in previous versions of the Treasury's Long-Term Fiscal Statement (LTFS). As noted above, the Treasury is reviewing its labour productivity assumption for the LTFS. The Treasury is likely to update this assumption to 1.2% per annum, which is the median over the past 30 years.

This change reflects a number of considerations, including a review of the approach taken by other Treasuries and public finance departments, who largely base their assumption on an historical average. We have also reviewed the evidence on convergence towards high-income countries, trends in hours worked, and the possible effects of population ageing on productivity. Other New Zealand government agencies are also using lower productivity growth assumptions in their economic modelling and publications.

**Figure A3.2 – Annual labour productivity growth**




### The net impact on fiscal indicators is small

Using the Budget fiscal forecasts for illustrative purposes, as the HYEFU fiscal forecasts are currently being compiled, Figures A3.3 and A3.4 show that the combined impact of the assumption changes has very little impact on key fiscal variables over a 10-year horizon. Net debt as percentage of GDP is only 0.1 percentage point higher compared to the BEFU 2019 level. OBEGAL is still in surplus and 0.1 percentage point lower than the BEFU 2019 level.

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**Figure A3.3 Net core Crown debt (% of GDP)**

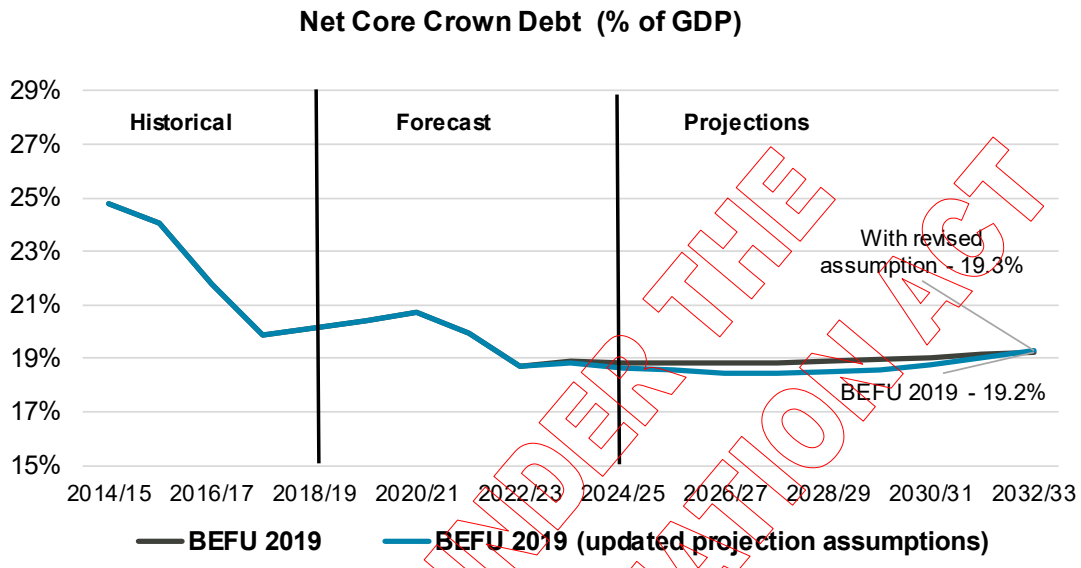
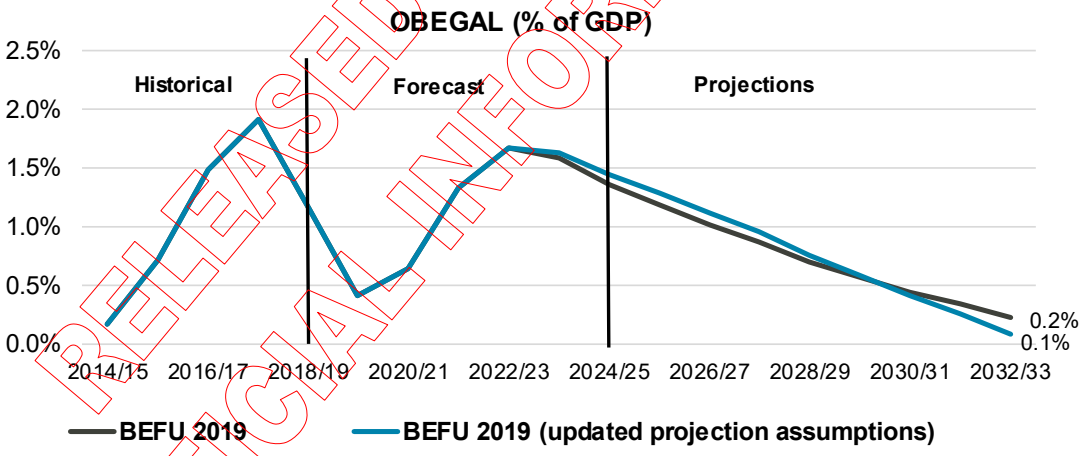



**Figure A3.4 OBEGAL (% of GDP)**



**From:** Jayne Winfield [TSY]
**Sent:** Tuesday, 29 October 2019 8:52 AM
**To:** Catherine Manning [TSY]
**Cc:** Kamlesh Patel [TSY]
**Subject:** FW: Preliminary fiscal forecasts



**From:** Talei Pasikale <Talei.Pasikale@parliament.govt.nz>
**Sent:** Tuesday, 29 October 2019 7:38 AM
**To:** Jayne Winfield [TSY] <Jayne.Winfield@treasury.govt.nz>
**Cc:** ^Parliament: Daniel Cruden <Daniel.Cruden@parliament.govt.nz>; ^EXT: Alastair Cameron <Alastair.cameron@parliament.govt.nz>
**Subject:** RE: Preliminary fiscal forecasts

Kia ora Jayne

Thanks for sending this through.

Could you please provide asap:

1) a year by year breakdown of the change in OBEGAL by reason (ie. so much is deficit, so much is slower growth etc etc)

2) options for short term management of the deficit (this could include DHB deficit management but also broader options).

Thanks, Talei

Talei Pasikale, Economic Advisor | Office of Hon Grant Robertson s9(2)(k)

**From:** Jayne Winfield [TSY] <Jayne.Winfield@treasury.govt.nz>
**Date:** Friday, 25 Oct 2019, 6:57 PM
**To:** Alastair Cameron <Alastair.Cameron@parliament.govt.nz>
**Cc:** Talei Pasikale <Talei.Pasikale@parliament.govt.nz>
**Subject:** Preliminary fiscal forecasts

[SEEMAIL][SENSITIVE]

Hi Alastair,

Today we have finalised the preliminary fiscal forecasts for HYEFU 19. These are based on the preliminary economic forecasts (completed on 3 October).

The table below shows a lower operating balance before gains and losses (OBEGAL) when compared to the 2019 Budget Update (BEFU) across the forecast period, with deficits in the first two years of the forecast. Net debt in the near term is lower than was forecast at BEFU, however this trend reverses near the end of the forecast period. As a

percentage of GDP net debt is expected to peak at 20.9% in 2021/22. Residual cash remains in deficit until the final year of the fiscal forecast, when it returns to surplus.

| | Actual | | | Forecast | | |
|---|---|---|---|---|---|---|
| $ billion, June years | 2018/19 | 2019/20 | 2020/21 | 2021/22 | 2022/23 | 2023/24 |
| OBEGAL - prelim HYEFU 19 | 7.5 | (0.4) | (0.6) | 0.8 | 3.2 | 5.2 |
| OBEGAL - BEFU 19 | | 1.3 | 2.1 | 4.7 | 6.1 | .. |
| Total Change | | (1.7) | (2.7) | (3.9) | (2.9) | 5.2 |
| Residual Cash - prelim HYEFU 19 | (0.7) | (4.3) | (6.5) | (4.5) | (0.9) | 2.2 |
| Residual Cash - BEFU 19 | | (4.2) | (4.3) | (0.6) | 1.2 | .. |
| Total Change | | (0.1) | (2.2) | (3.9) | (2.1) | 2.2 |
| Net Debt - prelim HYEFU 19 | 57.7 | 61.5 | 68.1 | 72.5 | 73.0 | 70.5 |
| Net Debt - BEFU 19 | | 64.7 | 69.2 | 69.9 | 68.5 | .. |
| Total Change | | 3.2 | 1.1 | (2.6) | (4.5) | (70.5) |
| % of GDP, June years | | | | | | |
| Net Debt - prelim HYEFU 19 | 19.2 | 19.5 | 20.6 | 20.9 | 20.1 | 18.5 |
| Net Debt - BEFU 2019 | | 20.4 | 20.7 | 19.9 | 18.7 | .. |

***OBEGAL:***

- Tax revenue has decreased $4.7 billion across the forecast period, largely due to economic forecasting changes.
- Benefit expenses are $2.2 billion higher across the forecast period than what was forecast at BEFU reflecting increases in jobseeker support and NZ superannuation expenses .
- s9(2)(j)
  s9(2)(j)
- DHB deficits have increased since the Budget 2019 forecasts by $1.6 billion across the forecast period, with further work being done prior to final fiscal forecasts.
- ACC OBEGAL has decreased by $1.9 billion across the forecast period, this is primarily due to the impact of lower discount rates increasing the insurance claims costs across the forecast period.

***Residual cash***

Overall, residual cash is forecast to be $8.3 billion lower than Budget 2019 from 2019/20 to 2022/23. With the exception of ACC and DHB's above the residual cash decrease is in largely consistent with the OBEGAL results.

***Net core Crown debt***

Net core Crown debt is forecast to be $4.5 billion higher than at Budget 2019 at $73.0 billion (20.1% of GDP) in 2022/23.

The key changes to net core Crown debt are:

- Residual cash increases net debt by $8.4 billion
- Stronger 30 June 2019 results has meant a $2.6 billion lower net debt starting position.

***Next steps***

We are expecting to send a Treasury Report providing further details of the preliminary fiscal forecasts to your office on Wednesday.

Thanks

**Jayne Winfield | Manager Fiscal Reporting | Te Tai Ōhanga – The Treasury**

s9(2)(k) Email/IM: jayne.winfield@treasury.govt.nz
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**BUDGET-SENSITIVE**

TE TAI ŌHANGA
THE TREASURY

# Treasury Report: Half Year Economic and Fiscal Update 2019 Preliminary Fiscal Forecasts

| | | | |
|---|---|---|---|
| **Date:** | 31 October 2019 | **Report No:** | T2019/3417 |
| | | **File Number:** | BM-2-3-2019-2 (October Baseline Update) |

## Action sought

| | Action Sought | Deadline |
|---|---|---|
| Minister of Finance<br>(Hon Grant Robertson) | **Note** the Treasury's 2019 Half Year Update preliminary fiscal forecasts.<br>**Discuss** the preliminary fiscal forecasts with officials at the upcoming Budget Matters meeting.<br>**Refer** this report to the Associate Ministers of Finance.<br>**Agree** to key dates for specific fiscal risks feedback and statement of responsibility sign-off. | Prior to the Budget Matters meeting on 5 November 2019 |

## Contact for telephone discussion (if required)

| Name | Position | Telephone | | 1st Contact |
|---|---|---|---|---|
| Catherine Manning | Senior Government Reporting Accountant, Fiscal Reporting | s9(2)(k) | n/a (mob) | ✓ |
| Jayne Winfield | Manager, Fiscal Reporting | | s9(2)(g)(ii) | |

## Minister's Office actions (if required)

**Return** the signed report to the Treasury.

If agreed, **refer** a copy of this report to the Associate Ministers of Finance.

| | |
|---|---|
| Note any feedback on the quality of the report | |

**Enclosure**: No

# Treasury Report: Half Year Economic and Fiscal Update 2019 Preliminary Fiscal Forecasts

## Executive Summary

This report provides a summary of the Treasury's preliminary fiscal forecasts (2019/20 – 2023/24) in the lead-up to the *2019 Half Year Economic and Fiscal Update* (*Half Year Update*). The fiscal forecasts completed on 25 October capture the preliminary economic forecasts (completed on 3 October) and other significant information that has become available since completing the 2019 *Budget Economic and Fiscal Update (Budget Update)* forecasts.

The 30 June 2019 results reported a strong fiscal position with both the operating balance before gains and losses (OBEGAL) and net core Crown debt outperforming expectations. As previously signalled, a lot of this strength was one-off or timing in nature, therefore it has not persisted into the current years and beyond.

At the *Budget Update* in the near-term we expected that OBEGAL surpluses would narrow and net core Crown debt would rise. This was a result of tax revenue growth remaining relatively flat, while core Crown expenses growth rose, reflecting the impact of past spending decisions.

The preliminary fiscal forecasts follow a similar trend as the *Budget Update*, however the softer forecasts for economic growth, a stronger wage outlook and a lower interest rate track have meant the expected drop in OBEGAL from 2018/19 to 2019/20 is greater than previously expected, with a deficit of $0.4 billion now forecast for the 2019/20 fiscal year. In the near-term, the stronger starting position of net core Crown debt has somewhat softened the impact from the weaker fiscal outlook.

The economic conditions mentioned above are expected to continue across the rest of the forecast period. As a result, tax revenue forecasts have been revised down, benefit expenses are now expected to be higher and the cost of future ACC claims has increased. In addition, there have been increases in some items that are managed outside of Budget allowances that have adversely influenced the fiscal outlook (s9(2)(j) and on-sold properties).

***Table 1*** – Key fiscal indicators

| Year ended 30 June | Actual | | | Forecast | | |
|---|---|---|---|---|---|---|
| | 2018/19 | 2019/20 | 2020/21 | 2021/22 | 2022/23 | 2023/24 |
| **$ billion** | | | | | | |
| Total Crown OBEGAL | 7.5 | (0.4) | (0.6) | 0.8 | 3.2 | 5.2 |
| Core Crown residual cash | (0.7) | (4.3) | (6.5) | (4.5) | (0.9) | 2.2 |
| Net core Crown debt | 57.7 | 61.5 | 68.1 | 72.5 | 73.0 | 70.5 |
| Total Crown operating balance | (2.3) | (0.9) | 3.1 | 5.0 | 7.8 | 10.2 |
| **% of GDP** | | | | | | |
| Total Crown OBEGAL | 2.5% | (0.1%) | (0.2%) | 0.2% | 0.9% | 1.4% |
| Core Crown residual cash | (0.2%) | (1.4%) | (2.0%) | (1.3%) | (0.3%) | 0.6% |
| Net core Crown debt | 19.2% | 19.5% | 20.6% | 20.9% | 20.1% | 18.5% |
| Total Crown operating balance | (0.8%) | (0.3%) | 0.9% | 1.4% | 2.1% | 2.7% |

Overall, the fiscal outlook is weaker than at the *Budget Update.* OBEGAL deficits are expected for the next two years before returning to a surplus in 2021/22 and reaching $5.2 billion in 2023/24. Net core Crown debt is expected to slowly rise, peaking at 20.9% of GDP in 2021/22, before falling to 18.5% at the end of the forecast period. Residual cash deficits are expected up until 2022/23 and these are $8.3 billion larger than at the *Budget Update*.

The preliminary fiscal forecasts will be updated to reflect the final economic forecasts, and any other decisions or material developments. The Treasury's fiscal forecasts for inclusion in the *Half Year Update* are due to be finalised on 25 November. At this stage, we are aware of a number of items that may influence our final forecast including:

- decisions around increasing the multi-year capital allowance and delivering a capital package to be announced in the 2020 Budget Policy Statement;
- s9(2)(f)(iv)
- an updated valuation of the Government Superannuation Fund (GSF) liability, which is likely to adversely impact the fiscal outlook given the drop in discount rates since 30 June 2019; and
- further analysis of the District Health Boards (DHBs) forecast results may lead to an increase in the level of deficits. You will be receiving further advice on this later this week.

In addition, we will be completing further analysis of the forecasts, which may result in updates to our preliminary forecasts. Overall, our assessment is that the risks are more likely to adversely impact key fiscal indicators.

There is an opportunity to discuss the preliminary fiscal forecasts with officials at the Budget Matters meeting scheduled for Tuesday 5 November.

A timeline of upcoming key milestones in the production of the 2019 *Half Year Update* is outlined in paragraph 45. In order to ensure we can deliver a high-quality *Half Year Update*, it is important that we receive the following from you:

- confirmation of decisions made by Budget Ministers by **Monday 11 November 2019**,
- your feedback on specific fiscal risk disclosures by **Tuesday 19 November 2019**; and
- the signed Statement of Responsibility by **Monday 2 December 2019**.

## Recommended Actions

a. **note** the Treasury's 2019 *Half Year Update* preliminary fiscal forecasts

b. **note** that overall the fiscal outlook is weaker than that at the *Budget Update*

c. **note** that these forecasts will be updated on 25 November 2019 to reflect final economic forecasts and any other decisions and new information available

d. **note** that risks known to date are more likely to adversely impact the key fiscal indicators presented in this report

e. **discuss** the preliminary fiscal forecasts with Treasury officials at the Budget Matters meeting on 5 November 2019

f. **note** the key production milestones for the 2019 *Half Year Update* set out in Table 10

g. **agree** to write to the Secretary to the Treasury confirming any Budget Ministers decisions that impact the Treasury's forecast by Monday 11 November 2019

*Agreed/Not agreed*

h. **agree** to provide feedback on the specific fiscal risks disclosure for the 2019 *Half Year Update* by Tuesday 19 November 2019

*Agreed/Not agreed*

**i.** **agree** to sign the Statement of Responsibility for the 2019 *Half Year Update* on Monday 2 December 2019, and

*Agreed/Not agreed*

j. **refer** this report to:

- Hon Dr David Clark, Associate Minister of Finance

*Refer/not referred*

- Hon David Parker, Associate Minister of Finance

*Refer/not referred*

- Hon Shane Jones, Associate Minister of Finance

*Refer/not referred*

- Hon James Shaw, Associate Minister of Finance

*Refer/not referred.*

Jayne Winfield
**Manager, Fiscal Reporting**

Hon Grant Robertson
**Minister of Finance**

# Treasury Report: Half Year Economic and Fiscal Update 2019 Preliminary Fiscal Forecasts

## Purpose of Report

1. This report outlines the preliminary fiscal forecasts (for the five years 2019/20 to 2023/24) completed on 25 October 2019 and outlines the key risks and assumptions underpinning these forecasts. The report is broken into the following sections:
   - Preliminary Fiscal Forecasts;
   - Changes since the *Budget Update*;
   - Summary of Key Risks;
   - Summary of Key Fiscal Assumptions; and
   - Next Steps and Key Dates for the *Half Year Update*

## Preliminary Fiscal Forecasts

2. The table below sets out the key fiscal indicators for the preliminary fiscal forecasts.

**Table 2** – *Summary of key indicators*

| Year ended 30 June | 2019 Actual | 2020 Forecast | 2021 Forecast | 2022 Forecast | 2023 Forecast | 2024 Forecast |
|---|---|---|---|---|---|---|
| **$ billion** | | | | | | |
| Core Crown tax revenue | 86.5 | 89.2 | 93.9 | 98.4 | 104.0 | 109.5 |
| Core Crown expenses | 87.0 | 93.9 | 99.0 | 102.1 | 106.3 | 109.1 |
| Total Crown OBEGAL | 7.5 | (0.4) | (0.6) | 0.8 | 3.2 | 5.2 |
| Core Crown residual cash | (0.7) | (4.3) | (6.5) | (4.5) | (0.9) | 2.2 |
| Net core Crown debt | 57.7 | 61.5 | 68.1 | 72.5 | 73.0 | 70.5 |
| Total borrowings | 110.5 | 122.2 | 127.0 | 137.7 | 138.0 | 144.4 |
| Total Crown operating balance | (2.3) | (0.9) | 3.1 | 5.0 | 7.8 | 10.2 |
| Net worth attributable to the Crown | 139.7 | 138.9 | 142.0 | 147.1 | 154.9 | 165.1 |
| **% of GDP** | | | | | | |
| Core Crown tax revenue | 28.8% | 28.3% | 28.4% | 28.4% | 28.6% | 28.7% |
| Core Crown expenses | 29.0% | 29.7% | 29.9% | 29.4% | 29.2% | 28.6% |
| Total Crown OBEGAL | 2.5% | (0.1%) | (0.2%) | 0.2% | 0.9% | 1.4% |
| Core Crown residual cash | (0.2%) | (1.4%) | (2.0%) | (1.3%) | (0.3%) | 0.6% |
| Net core Crown debt | 19.2% | 19.5% | 20.6% | 20.9% | 20.1% | 18.5% |
| Total borrowings | 36.8% | 38.7% | 38.4% | 39.7% | 37.9% | 37.9% |
| Total Crown operating balance | (0.8%) | (0.3%) | 0.9% | 1.4% | 2.1% | 2.7% |
| Net worth attributable to the Crown | 46.6% | 44.0% | 42.9% | 42.4% | 42.6% | 43.3% |

### *Operating deficits are expected in the near-term*

3. Modest OBEGAL deficits are forecast over the next two years of $0.4 billion and $0.6 billion respectively. OBEGAL surpluses return from 2021/22 and reach $5.2 billion by the end of the forecast period.

4. In the near-term, growth in core Crown expenses outpaces core Crown tax revenue, primarily reflecting the impact from previous Budget decisions (e.g. the 2019 Budget package of $3.8 billion per annum). This trend is expected to reverse from 2021/22 as

smaller increases are assumed for new spending allowances, while core Crown tax revenue is expected to grow broadly in line with the economy.

5. As a percentage of GDP, core Crown expenses stay below 30% across the forecast period, consistent with the Government's Budget Responsibility Rules.

6. On an aggregated basis, SOEs are expected to record modest surpluses over the forecast period. While the Crown entities sector is forecast to run deficits of around $2.0 – 2.5 billion across the forecast period. DHBs and ACC made up most of these deficits.

7. An operating balance deficit is also forecast in the current year largely owing to valuation losses on the Government's long-term liabilities from a drop in discount rates since 30 June 2019.

***While residual cash deficits are forecast until 2022/23***

8. Net cash flows from core Crown capital spending are expected to exceed net operating cash flows up until 2022/23, resulting in residual cash deficits. Over the entire forecast period, residual cash deficits total $14.0 billion.

9. Net capital spending over the forecast period is expected to be around $41.2 billion, which is broadly consistent with the spending signalled in the *Budget Update* over the five-year period between 2019 and 2023.

10. The residual cash shortfall has been largely met from increasing borrowings. The Crown's bond programme is expected to increase borrowings by around $20 billion over the forecast period.

***Resulting in net core Crown debt increasing***

11. Overall, net core Crown debt is expected to increase by $12.8 billion over the forecast period. Net core Crown debt peaks in 2022/23 at $73.0 billion before starting to reduce in the final year of the forecast as residual cash surpluses are achieved.

12. Net core Crown debt (as a percentage of GDP) increases to reach 20.9% in 2021/22 before declining across the remainder of the forecast period to stand at 18.5% of GDP by 2023/24.

***Total borrowings and net worth also increase over the forecast period***

13. Total borrowings are forecast to increase by $33.9 billion to stand at $144.4 billion by 2023/24. This increase is largely owing to borrowings to fund the residual cash shortfall mentioned above, increases in Kiwibank deposits ($10.8 billion), and borrowings from Crown entities.

14. Net worth attributable to the Crown is expected to increase over the forecast period, reaching $165.1 billion by 2023/24. This growth is primarily from the accumulation of operating balance surpluses from 2020/21 onwards. However, in the current year a $0.9 billion operating deficit is forecast. As such, net worth attributable to the Crown is forecast to decline in 2019/20 before starting to grow again in 2020/21.

## Changes since the Budget Update

***Table 3*** – Summary fiscal indicators compared to the *Budget Update*

| Year ended 30 June | Actual | Forecast | | | | |
|---|---|---|---|---|---|---|
| **$ billion** | **2018/19** | **2019/20** | **2020/21** | **2021/22** | **2022/23** | **2023/24** |
| OBEGAL - *Half Year Update* 2019 - preliminary | 7.5 | (0.4) | (0.6) | 0.8 | 3.2 | 5.2 |
| OBEGAL - *Budget Update* 2019 | | 1.3 | 2.1 | 4.7 | 6.1 | .. |
| Total Change | | (1.7) | (2.7) | (3.9) | (2.9) | |
| Residual Cash - *Half Year Update* 2019 - preliminary | (0.7) | (4.3) | (6.5) | (4.5) | (0.9) | 2.2 |
| Residual Cash - *Budget Update* 2019 | | (4.2) | (4.3) | (0.6) | 1.2 | .. |
| Total Change | | (0.1) | (2.2) | (3.9) | (2.1) | |
| Net Debt - *Half Year Update* 2019 - preliminary | 57.7 | 61.5 | 68.1 | 72.5 | 73.0 | 70.5 |
| Net Debt - *Budget Update* 2019 | | 64.7 | 69.2 | 69.9 | 68.5 | .. |
| Total Change | | 3.2 | 1.1 | (2.6) | (4.5) | |
| **% of GDP** | | | | | | |
| Net Debt - *Half Year Update* 2019 - preliminary | 19.2 | 19.5 | 20.6 | 20.9 | 20.1 | 18.5 |
| Net Debt - *Budget Update* 2019 | | 20.4 | 20.7 | 19.9 | 18.7 | .. |

15. Overall, most key fiscal indicators are weaker than forecast at the *Budget Update*. On average OBEGAL and residual cash are weaker by around $2.8 billion and $2.1 billion per annum respectively. Net core Crown debt is $4.5 billion higher by 2022/23. Tables 5 and 6 provide a detailed breakdown of the movements in OBEGAL and net core Crown debt since the *Budget Update*. In summary, the most significant movements are due to economic factors, additional costs from items managed outside of Budget allowances and weaker forecast results from SOE/Crown entities.

***Weaker economic growth and lower interest rates have reduced tax revenue***

16. Tax revenue is cumulatively $4.7 billion lower than previously forecast mainly owing to a weaker economic outlook. Weaker growth in macroeconomic factors has resulted in a $5.3 billion reduction, with a reduction in interest rates also reducing tax revenue forecasts by $2.8 billion. Partially offsetting this, other factors have increased tax forecasts by $3.4 billion. These other factors mainly reflects our judgment that some of the higher growth experience at year end will continue into the current year and beyond. The lower forecast tax revenue is across all major tax types with the exception of source deductions and other persons' tax which is higher than previously forecast (T2019/3177 refers).

17. Tax receipts follow a similar trend to tax revenue and are cumulatively lower by $4.9 billion compared to the *Budget Update.*

***While higher wage growth and economic conditions have increased benefit costs***

18. Social assistance expenses have increased by $2.2 billion over the forecast period since the *Budget Update*. The increase is mainly owing to New Zealand Superannuation payments, Jobseeker Support and Emergency Benefits and the Supported Living Payment. This increase reflects higher recipient numbers and a higher wage growth track that contributed $1.6 billion and $0.7 billion respectively to the overall increase.

19. A higher wage growth track compared to the *Budget Update* has resulted in an increase across most benefit types. The upward revision to the expected wage level has the largest impact on New Zealand Superannuation due to the large volume of people receiving the payment. Figure 1 outlines the movement in the wage track compared to the *Budget Update*.

20. Actual recipient numbers for the Jobseeker Support and Emergency Benefit (such as emergency housing) and the Supported Living Payment are tracking above what was expected at the *Budget Update*. In addition, the softening in economic conditions in the near-term have also resulted in an expected lift in recipient numbers. Overall, the increase in recipient numbers from these two benefit types have increased expenses by around $1.0 billion over the forecast period. Refer Table 4 for the changes in recipient numbers for these two benefit types.

***Figure 1*** – Wage track – annual average % change

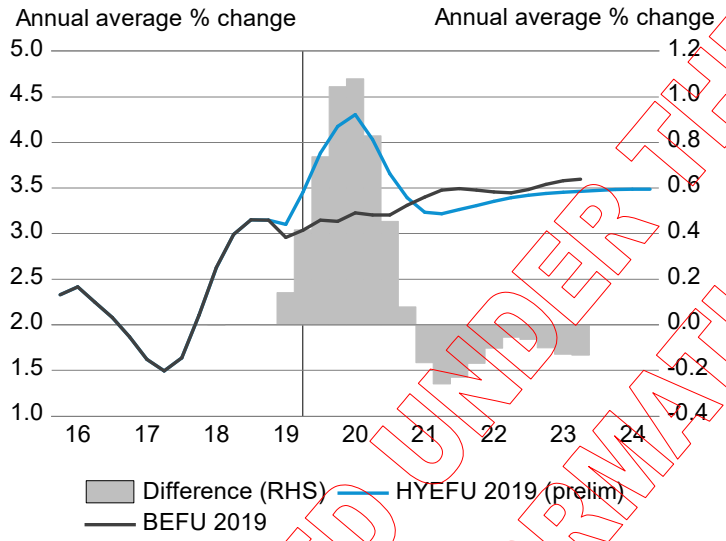



***Table 4*** – Changes in recipient numbers for key benefit types

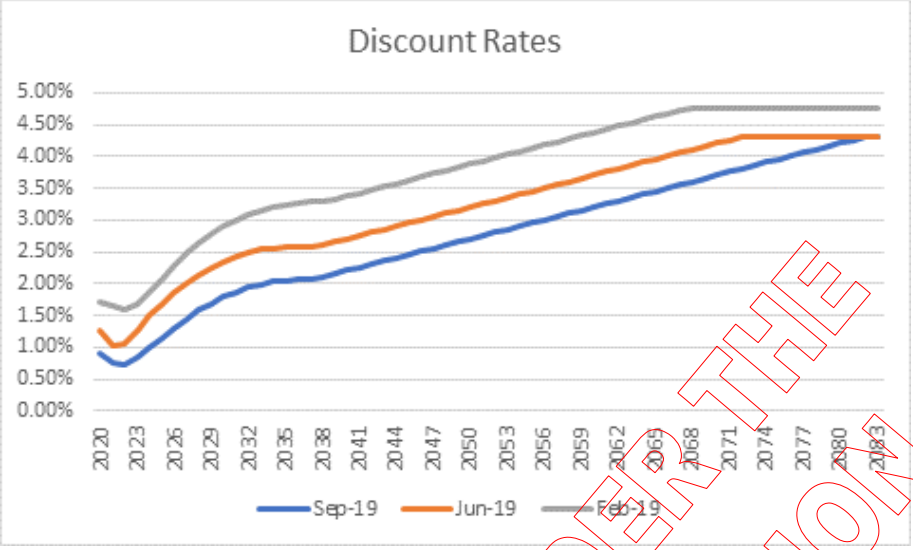
| Year ended 30 June | | Forecast | | |
|---|---|---|---|---|
| **Recipient numbers** | **2019/20** | **2020/21** | **2021/22** | **2022/23** |
| **Jobseeker Support and Emergency Benefit** | | | | |
| *Half Year Update* 2019 - preliminary | 151,874 | 156,075 | 156,032 | 154,723 |
| *Budget Update* 2019 | 144,768 | 142,887 | 140,423 | 138,571 |
| Total Change | 7,106 | 13,188 | 15,609 | 16,152 |
| **Supported Living Payment** | | | | |
| *Half Year Update* 2019 - preliminary | 95,582 | 95,912 | 96,224 | 96,190 |
| *Budget Update* 2019 | 95,083 | 94,470 | 93,545 | 92,173 |
| Total Change | 499 | 1,442 | 2,679 | 4,017 |

***Lower interest rates have also resulted in higher costs for ACC***

21. ACC is expecting higher insurance claims costs then previously forecast. The ACC liability and insurance costs are particularly sensitive to discount rates (used to value the lifetime cost of all existing and forecast claims in today's dollars). ACC's updated forecast is based on the 30 June 2019 valuation updated for 30 September 2019 discount rates. As discount rates have continued to fall since the *Budget Update*, the lifetime cost of forecast claims are now higher in present value terms than the same claims forecast at *Budget Update* (based on February discount rates). Refer to Figure 2 for the different discount rates used in this preliminary forecast and the *Budget Update*. The increase in forecast claims costs are partially offset by the increase in levy revenue forecast based on the current funding policy, resulting in a total reduction in OBEGAL of $1.9 billion across the forecast period.

22. The total reduction in OBEGAL from ACC does not flow through to residual cash or net core Crown debt as ACC is outside of the core Crown.

***Figure 2*** – Movement in discount rates




***However, lower interest rates have had a minimal impact on net finance costs***

23. Although the weaker fiscal outlook has resulted in an increase to net core Crown debt, net finance costs are actually expected to be lower across the forecast period by $0.6 billion compared to the *Budget Update*. The level of financial assets held by the Crown are expected to reduce in order to fund the increase in the cash shortfall, which has resulted in a reduction in interest revenue, however this has been more than offset by lower debt servicing costs now forecast due to lower yields on new debt being issued at a lower interest rate. The current low interest rate environment has reduced the yields on new issued bonds, however the coupon rates paid on some of these issued bonds remains unchanged, therefore the cash impact of net finance costs are higher than previously expected.

***There has been an increase in some costs managed outside of Budget allowances***

24. s9(2)(j)

25. Cabinet has agreed to compensate homeowners for the repair costs of eligible on-sold Canterbury properties. The costs from this decision were not managed against Budget allowances, therefore have directly impacted OBEGAL and net core Crown debt (T2019/2916 dated 23 September refers).

***Overall SOE and Crown entity results are weaker***

26. SOE and Crown entity forecast results have come in weaker than forecast at the *Budget Update*. Of these, the largest changes were in relation to ACC (discussed above), DHBs and KiwiRail:

- The DHBs are currently forecasting deficits across each year of the forecast ($0.7 billion in the current year, and increasing by $0.2 billion each year to reach $1.3 billion in 2022/23). These forecast deficits have increased in each of the years with an overall increase in the deficits of $1.6 billion since the *Budget Update*. We have included further discussion in the key assumptions section of this report – refer paragraphs 40-41.

- Updated forecasts for KiwiRail also show a weaker outlook than previously forecast by $0.7 billion across the forecast period. This is due to higher depreciation expenses now being forecast, owing to the increase in the value of the rail network, from the change in the valuation approach adopted in the 2019 fiscal year.

***Reforecasting by agencies has marginally impacted the fiscal outlook***

27. Some agencies have changed the timing of expenditure (both operating and capital), which overall have had a positive impact on OBEGAL and net core Crown debt of $0.7 billion and $0.9 billion respectively in total across the forecast period. These timing changes were mainly relating to spending from the Ministry of Transport, Ministry of Education and the Ministry of Housing and Urban Development.

***The stronger starting position has somewhat softened the impact of the weaker fiscal outlook on net core Crown debt***

28. The results from 30 June 2019 have meant that there is a stronger starting position for net core Crown debt heading into the current fiscal year. As a result, this improvement has partially offset the additional residual cash shortfall expected since the *Budget Update*.

***Assumed uptake of the 'Fixed Price Option' under the Emissions Trading Scheme (ETS) has also improved net core Crown debt***

29. ETS receipts have increased by $2.1 billion across the forecast owing to an expectation that more ETS participants will take up the 'fixed price option' where they can pay the Government $25 for each unit they are liable to surrender to meet their ETS obligations. This has resulted in a $2.1 billion improvement in net core Crown debt from the *Budget Update*.

30. Although, the uptake of the Fixed Price Option has improved net core Crown debt it has also increased the Government's obligation under the ETS, which will need to be settled in the future. By the end of the forecast period, it is forecast to reduce net core Crown debt by around 0.7% of GDP.

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[redacted]

s9(2)(j)

[redacted]



## Summary of Key Risks

31. Along with the inherent uncertainty regarding forecasts, there are some known risks to the preliminary fiscal forecasts:

- The preliminary fiscal forecasts do not reflect economic data received after the economic forecasts were finalised on 3 October 2019. This information will be incorporated into the final fiscal forecasts.

- ACC's forecasts for the preliminary fiscal forecasts are based on the current policy settings for the non-earners' account (NEA) and ACC levies. [redacted]

s9(2)(f)(iv)

[redacted]

- The preliminary fiscal forecast does not reflect the GSF liability valuation as at 30 September. This valuation will be received in early November and incorporated into the final fiscal forecast. We are expecting an adverse impact on the fiscal forecasts due to the discount rate being lower than at 30 June 2019.

- Budget allowances are assumed to be the same as the *Budget Update* and in line with the *Budget Policy Statement 2019*. Fiscal Strategy advice regarding the level of allowances will be forwarded to you this week. We will update the final fiscal forecasts for any decisions around allowances.

- Further work is being completed in relation to DHB deficits. Any changes as a result of this work will be incorporated into the final fiscal forecasts.

- Kāinga Ora have included borrowings in accordance with their existing agreement with the Minister of Finance ('the borrowing protocol'); we are aware that an increase to the approved level of borrowings in this protocol is going to be requested. This is not expected to occur prior to the finalisation of the fiscal forecasts, but we will include a specific fiscal risk in the *Half Year Update*.

## Summary of Key Fiscal Assumptions

32. The preliminary fiscal forecasts are based on the preliminary economic forecasts (completed on 3 October 2019), information provided by individual entities, coupled with central adjustments made by the Treasury for items which are not captured in individual entity forecasts. Summarised below are some of the key assumptions worth noting that have required some degree of judgement by the Treasury.

### Consistency of assumptions

33. The preliminary economic forecasts that were completed on 3 October 2019 were provided to agencies whose forecasts are underpinned by key economic indicators to ensure consistency of assumptions. Discount rates and CPI assumptions are also centrally set by the Treasury for use in key asset and liability valuations (e.g. ACC claims liability, GSF liability and student loans valuation).

### Top-down adjustment

34. The top-down adjustment is a central adjustment to expenditure forecasts (both operating and capital) to reflect departments' tendency to use appropriations (upper spending limits) rather than best estimates when preparing their forecasts. The level of the central top-down adjustment is dependent on the quality of forecasts received from departments. Based on our analysis, the central top-down adjustments included in the forecasts are set out in Table 7 below.

**Table 7** – Top-down adjustment assumed for the preliminary 2019 *Half Year Update*

| $millions | 2019/20 | 2020/21 | 2021/22 | 2022/23 | 2023/24 |
|---|---|---|---|---|---|
| Operating | 1,200 | 825 | 675 | 575 | 575 |
| Capital | 800 | 300 | 200 | 150 | 150 |
| **Total** | **2,000** | **1,125** | **875** | **725** | **725** |

35. We have adjusted these amounts since the *Budget Update*, reducing the operating adjustment in the current year, and increasing the adjustment the outyears. The decrease in the current year is reflective of two things: an increase due to the size of the expense transfers into 2019/20, more than offset by entities' forecasting large underspends in the current year with some of these moving into the next financial year.

36. The capital adjustment has been reduced in the first three years to reflect re-phasing of capital spending by departments with some capital spending now falling outside of the forecast period.

37. Generally the top-down adjustment in the current year (2019/20) and the next year are higher than the other years in the forecast period to compensate for expenses being transferred in from previous years. This was the case for both operating and capital, where expense transfers have occurred from 2018/19.

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[redacted]



### *DHB deficits*

40. The DHBs have forecast large deficits across each year of the forecast. While the DHBs have been forecasting deficits for some time, the size of the deficits is now quite significant and has increased since the *Budget Update* – refer Table 9 below.

**Table 9** – DHB forecast deficits

| **$millions** | **2019/20** | **2020/21** | **2021/22** | **2022/23** |
|---|---|---|---|---|
| *Half Year Update* 2019 - preliminary | (700) | (900) | (1,100) | (1,300) |
| *Budget Update 2019* | (607) | (607) | (607) | (607) |
| Change since the *Budget Update* | (93) | (293) | (493) | (693) |

41. Further work is expected to be completed on the level of these deficits in advance of the final fiscal forecasts.

## Next Steps and Key Dates for the *Half Year Update*

42. The Budget Matters meeting with officials on 5 November 2019 will give you an opportunity to discuss any questions you may have on these preliminary fiscal forecasts.

43. Our recent advice provided on the fiscal strategy for the 2020 Budget Policy Statement (T2019/3343) recommended not to make policy changes in order to return to surplus immediately. This advice is on the basis of the current macroeconomic environment and the relatively small sizes of these deficits.

44. It is much harder to manage deficits in the current year as spending plans are already underway. Beyond the current year the simplest options for reversing deficits would be to reduce the Budget 2020 operating allowance or manage some of the increases in expenses (e.g. benefit forecast changes) against Budget allowances, however this would have an impact on economic growth. If any spending is decreased to manage deficits, this should be focused on items which are unlikely to impact macroeconomic conditions (e.g. KiwiSaver contributions).

45. Table 10 outlines key dates for the *Half Year Update 2019* through the remainder of the production process, including highlighting where your input will be required. If these dates are not met, it will compress already tight timeframes required for robust quality assurance and production processes, which will compromise our ability to deliver a high-quality *Half Year Update 2019* on 11 December 2019.

**Table 10** – Key milestones for 2019 *Half Year Update* production

| Date | Key milestone | Input required from you and/or your Office |
|---|---|---|
| Mon 11 Nov | Details of any capital package to be announced in the BPS and the Budget 2023 operating allowance for inclusion in the fiscal forecast. | *Letter from you to the Secretary to the Treasury confirming Budget Ministers decision with fiscal implications* |
| Fri 15 Nov | Treasury provides you with a report outlining specific fiscal risks identified for the *Half Year Update*, including risks proposed for exclusion under Section 26V | |
| Mon 18 Nov | Treasury provides you with a report on the final economic and tax forecasts | |
| **Tues 19 Nov** | **Feedback on specific fiscal risks received by Treasury at Budget Matters**, along with discussion of final economic and tax forecasts | Feedback from you on additional *matters to be included as specific fiscal risks and agreement to exclude any risks under Section 26V* |
| Thurs 28 Nov | Treasury provides you with a report on the final fiscal forecasts | |
| **Mon 2 Dec** | **Treasury provides you with a Statement of Responsibility for signing**, along with near-final *Half Year Update* chapters for your information | *Sign the Half Year Update Statement of Responsibility confirming you have met your obligations under the Public Finance Act 1989* |
| Wed 4 Dec | *Half Year Update* to printer | |
| Wed 11 Dec | Print documents delivered at 8am and published online at 1pm | |

**From:** Talei Pasikale <Talei.Pasikale@parliament.govt.nz>
**Sent:** Wednesday, 13 November 2019 8:13 AM
**To:** Jess Jenkins [TSY]
**Subject:** RE: SFRs Chapter TR Timeframes

Kia ora Jess

Yes, that's fine to send across next week. By the Wednesday afternoon bag would be great (ie, finalise after Budget Matters in case anything relevant comes up but with enough time for the Office to look at it before I put into the weekend bag.)

Thanks, Talei

Talei Pasikale, Economic Advisor | Office of Hon Grant Robertson | s9(2)(k)

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**From:** Jess Jenkins [TSY] <Jess.Jenkins@treasury.govt.nz>
**Date:** Tuesday, 12 Nov 2019, 4:34 PM
**To:** Talei Pasikale <Talei.Pasikale@parliament.govt.nz>
**Subject:** SFRs Chapter TR Timeframes

[UNCLASSIFIED]

Hi Talei –

As discussed at our catch-up yesterday, if the MoF would be happy to deal with the SFR chapter TR on the papers (rather than discuss at Budget Matters on Tuesday), we were wondering if it would be fine for the report to come across next week.
We would like to have his feedback/agreement to the report by COP Monday 25 November. Do you have a preferred day next week that you would you ideally like to have the report to give him time to review ahead of Monday?

Happy to discuss over the phone if easier!

Jess

TE TAI ŌHANGA
THE TREASURY

**Jessica Jenkins** (she/her) **| Graduate Analyst, Budget Management | Te Tai Ōhanga – The Treasury**
s9(2)(k) Email/IM: jess.jenkins@treasury.govt.nz
Visit us online at https://treasury.govt.nz/ and follow us on Twitter, LinkedIn and Instagram

*Curious about why I share my pronouns on my email signature? This article explains.*

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**From:** Hamish Slack [TSY]
**Sent:** Friday, 15 November 2019 5:00 PM
**To:** ^Parliament: Talei Pasikale
**Cc:** Karam Shaar [TSY]; Peter Gardiner [TSY]
**Subject:** Draft Final HYEFU TR
**Attachments:** Treasury Report_ Half Year 2019 Economic and Tax Forecasts.doc

[SEEMAIL][SENSITIVE]

Hi Talei – as discussed, please find attached the draft TR on our final economic and tax forecasts. We will send the final version on Monday.

The report details the changes in the Treasury's economic and tax forecasts since the preliminary forecasts. Most of the changes are due to the additional capital spending due to be announced in the Budget Policy Statement; of the $12 billion increase, Treasury assumes $8.1 billion will be spent over the forecast period. A key assumption in these forecasts is the fiscal multiplier – a multiplier of 0.5 is assumed, reflecting that some of new spending will be on imports and capacity constraints in the economy. Relative to the preliminary forecasts, cumulative nominal GDP is $7.3 billion higher and core Crown tax is $2.5 billion higher over the forecast period.

This report is being sent in draft as the numbers and figures need a final QA. We do not anticipate significant changes.

Many thanks
Hamish

**Hamish Slack** (they/he) **| Team Leader – Forecasting | Te Tai Ōhanga – The Treasury**
s9(2)(k) Email/IM: hamish.slack@treasury.govt.nz
Visit us online at https://treasury.govt.nz/

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# Treasury Report: Half Year 2019 Economic and Tax Forecasts

| | | | |
|---|---|---|---|
| **Date:** | 18 November 2019 | **Report No:** | T2019/3638 |
| | | **File Number:** | BM-3-6-1 |

## Action Sought

| | Action Sought | Deadline |
|---|---|---|
| Minister of Finance (Hon Grant Robertson) | **Note** the final economic and tax forecasts<br>**Refer** this report to Associate Ministers of Finance | Budget Matters meeting, Tuesday 19 November 2019 |

## Contact for Telephone Discussion (if required)

| Name | Position | Telephone | | 1st Contact |
|---|---|---|---|---|
| Karam Shaar | Senior Analyst, Forecasting | s9(2)(k) | N/A (mob) | ✓ |
| Hamish Slack | Team Leader, Forecasting | | N/A (mob) | |

## Actions for the Minister's Office Staff

**Return** the signed report to Treasury.

If agreed, **refer** a copy of this report to Associate Ministers of Finance

Note any feedback on the quality of the report

**Enclosure**: No

# Treasury Report: Half Year 2019 Economic and Tax Forecasts

## Executive Summary

This report summarises the Treasury's Half Year 2019 economic and tax forecasts and their underlying key judgements. There will be an opportunity to discuss the economic and tax forecasts at **Budget Matters on Tuesday 19 November 2019**.

The economic forecasts underpin the final fiscal forecasts — a Treasury Report summarising the fiscal forecasts will be sent to you on 28 November 2019. A near-final draft of the Half Year Economic and Fiscal Update (HYEFU) document will be shared with you on 2 December 2019. There will be a chance to discuss the Treasury's fiscal forecasts at the Budget Matters meeting on 3 December 2019.

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GDP growth is forecast to pick up to 2.9% in mid-2021, supported by higher government spending, low interest rates and rising house price inflation. Beyond 2021, growth eases to 2.4% by the end of the forecast period in June 2024. The slowing in growth is owing to slowing migration-led population growth, rising interest rates, and the waning growth impact from the fiscal impulse. Cumulatively, nominal GDP is $7.3 billion higher relative to HYEFU preliminary forecasts. **Core crown tax is forecast to be $2.5 billion higher** over the forecast period compared to HYEFU preliminary forecasts.

**Table 1: Forecast summary**

| June years | | 2019 Actual | 2020 Forecast | 2021 Forecast | 2022 Forecast | 2023 Forecast | 2024 Forecast | 5-year total |
|---|---|---|---|---|---|---|---|---|
| Economic growth[1] | **Half Year** | **2.4** | **2.2** | **2.8** | **2.7** | **2.5** | **2.4** | |
| | Preliminary | 2.4 | 2.2 | 2.6 | 2.4 | 2.4 | 2.5 | |
| | Budget | 2.4 | 3.0 | 2.8 | 2.4 | 2.4 | - | |
| Economic growth per capita[1] | **Half Year** | **0.8** | **0.7** | **1.4** | **1.3** | **1.1** | **1.1** | |
| | Preliminary | 0.8 | 0.7 | 1.1 | 1.0 | 1.1 | 1.2 | |
| | Budget | 0.8 | 1.5 | 1.5 | 1.3 | 1.2 | - | |
| Unemployment rate[2] | **Half Year** | **3.9** | **4.3** | **4.2** | **4.2** | **4.3** | **4.3** | |
| | Preliminary | 3.9 | 4.1 | 4.3 | 4.3 | 4.3 | 4.3 | |
| | Budget | 3.9 | 4.0 | 4.1 | 4.2 | 4.3 | - | |
| CPI inflation[3] | **Half Year** | **1.7** | **1.9** | **1.9** | **2.0** | **2.0** | **2.0** | |
| | Preliminary | 1.7 | 1.8 | 1.9 | 2.0 | 2.0 | 2.0 | |
| | Budget | 1.7 | 2.0 | 2.1 | 2.0 | 2.0 | - | |
| Nominal GDP ($billions) | **Half Year** | **300.1** | **315.3** | **331.7** | **349.1** | **366.3** | **383.7** | |
| | Preliminary | 300.1 | 315.6 | 330.8 | 347.0 | 364.0 | 381.4 | |
| | Budget | 299.7 | 317.0 | 334.0 | 350.2 | 366.6 | - | |
| | Change v. Prelim | 0.0 | -0.3 | 0.9 | 2.1 | 2.3 | 2.3 | 7.3 |
| | Change v. Budget | 0.0 | -1.7 | -2.3 | -1.1 | -0.3 | - | -5.4 |
| Tax revenue ($billions) | **Half Year** | **86.5** | **88.7** | **94.3** | **99.2** | **104.8** | **110.5** | |
| | Preliminary | 86.5 | 89.2 | 93.9 | 98.4 | 104.0 | 109.5 | |
| | Budget | 84.7 | 89.2 | 95.1 | 100.2 | 105.6 | | |
| | Change v. Prelim | - | -0.4 | 0.4 | 0.8 | 0.8 | 1.0 | 2.5 |
| | Change v. Budget | 1.8 | -0.5 | -0.8 | -1.0 | -0.8 | | -1.3 |

1. Production GDP, annual average % change 2. June quarter 3. Annual % change

## Recommended Action

We recommend that you:

a s9(2)(f)(iv)

b **note** tax revenue is forecast to be $2.5 billion higher compared to the preliminary forecasts, but $1.6 billion lower relative to the Budget forecasts

c **note** there will be an opportunity to discuss the economic and tax forecasts at Budget Matters on Tuesday 19 November 2019

d **note** a Treasury Report summarising the fiscal forecasts will be sent to you on 28 November 2019, and

e **refer** this report to:

- Hon David Parker, Associate Minister of Finance

*Refer/not referred.*

- Hon Dr David Clark, Associate Minister of Finance

*Refer/not referred.*

- Hon Shane Jones, Associate Minister of Finance

*Refer/not referred.*

- Hon James Shaw, Associate Minister of Finance

*Refer/not referred.*

Hamish Slack
**Team Leader, Forecasting**

Hon Grant Robertson
**Minister of Finance**

# Treasury Report: Half Year 2019 Economic and Tax Forecasts

## Purpose of Report and Context

1. You received a report summarising Treasury's preliminary Half Year economic and tax forecasts on 17 October 2019 [T2019/3177 refers]. Since then, you informed the Treasury of the Government's intention to announce an increase in capital spending. Economic data has also been released since then.

2. This report summarises the Treasury's Half Year 2019 economic and tax forecasts and the underlying key judgements, including the impact of the increase in capital spending. There will be an opportunity to discuss the economic and tax forecasts at Budget Matters on Tuesday 19 November.

3. The economic forecasts underpin the final fiscal forecasts — a Treasury Report summarising the fiscal forecasts will be sent to you on 28 November. A near-final version of the Half Year Economic and Fiscal Update (HYEFU) document will be shared with you on 2 December. There will be a chance to discuss the Treasury's final forecasts at Budget Matters on 3 December. HYEFU will be published on 11 December, alongside the Budget Policy Statement (BPS).

**Table 2: timetable of key milestones and engagements**

| Reports | Budget Matters | Date |
|---|---|---|
| Final Economic and Tax forecast | | 18 November |
| | Final economic and tax forecasts | 19 November |
| Final fiscal forecasts Treasury Report | | 28 November |
| HYEFU 2019 chapters | | 2 December |
| | Final forecasts discussion | 3 December |
| HYEFU & BPS publication | | 11 December |

## Developments since the preliminary forecasts

***The data released since finalising the preliminary economic forecasts in early October, on balance, suggest no material change to the outlook***

4. Annual inflation fell to 1.5% in the September 2019 quarter from 1.7% in the June quarter. The fall was due to weak tradables inflation, mainly because of petrol prices, which tend to be volatile. Annual non-tradables inflation reached its highest rate since 2011, at 3.2%. The strength in annual non-tradables inflation indicates the spare capacity in the economy has been eroded. Inflation expectations remain subdued, with the two-year-ahead inflation expectations dipping to 1.8%, the lowest level since late-2016.

5. The unemployment rate rose to 4.2% in the September quarter, while the underutilisation rate, a broader measure of labour market capacity, fell to 10.4%, the lowest level since 2008. Ordinary time average hourly earnings grew 4.2% in the year to September, compared with 4.7% in the preliminary forecasts. The lower-than-forecast outturn for the quarter affects annual wage growth forecasts through to June 2021 (Figure 6).

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6. The forecasts assume the 90-day rate will fall further in early 2020, although not as far as assumed in the preliminary forecasts, reflecting changed market expectations. Interest rates will then remain on hold until 2020. Contrary to the implicit assumptions made in the forecasts, the Reserve Bank kept the OCR unchanged in its announcement on 13 November. This does not materially change our views on the 90-day rate forecasts as a further OCR cut in early 2020 remains likely. Note that the Treasury forecasts the 90-day rate of interest while the Reserve Bank sets and forecasts the OCR.

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## Economic Outlook

***GDP growth is forecast to average 2.5% over the forecast period...***

14. Annual economic growth averages 2.5% over the forecast period to June 2024, compared with 2.6% at BEFU. On a per-capita basis, the average is 1.1% compared with 1.3% at BEFU.

**Figure 3: GDP growth**

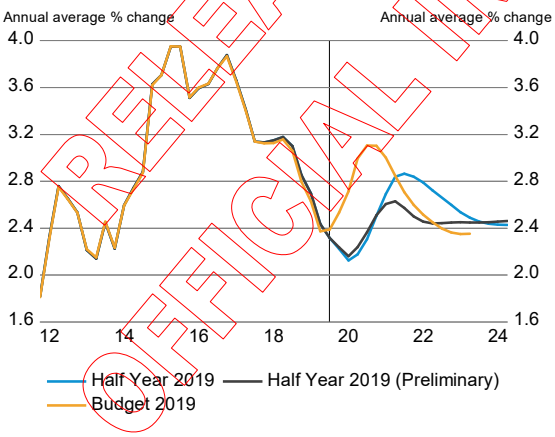
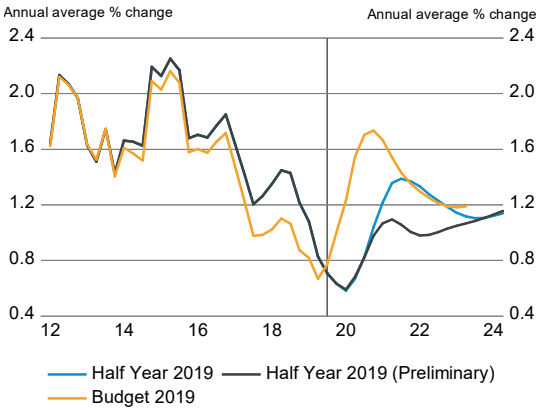



**Figure 4: GDP per-capita growth**




15. Economic growth has eased from above-trend growth of just below 4.0% over 2016 to 2.4% in the year ended June 2019. Weakening business sentiment, slowing migration-led population growth, falling house price inflation and the winding-down of Kaikōura and Canterbury earthquake-related investment have contributed to this slowing.

16. GDP growth is forecast to slow modestly to 2.1% by March 2020, reflecting slowing growth in household consumption, business investment, and service exports. However, the increase in government spending provides a partial offset.

17. GDP growth is forecast to pick up to 2.9% in mid-2021 supported by higher government capital spending, low interest rates and rising house price inflation. These factors help to support household consumption growth. Beyond 2021, growth eases to reach 2.4% by the end of the forecast period in June 2024. The moderation in growth is owing to slowing population growth as net migration gains are assumed to decline, rising interest rates to curb rising inflation and the waning growth impact of the fiscal impulse.

***…while investment recovers modestly in 2021, before slowing again***

18. Global and domestic uncertainty, compressed margins and declining expectations for future profitability have contributed to a deceleration in business investment growth over the past year.

19. Business investment growth is forecast to rise gradually from 0.4% in June 2019 to 4.4% in the second half of 2021, as firms respond to higher government capital spending, supportive commodity prices, low interest rates, and a small recovery in global growth.

20. Further deteriorations in business sentiment might see investment growing at a pace slower than forecast. Conversely, global risks and uncertainty could unwind, spurring business investment growth.

***Inflation rises gradually to 2.0% in late 2021 as economic activity picks up and monetary policy remains stimulatory***

21. Since late 2011, CPI inflation has generally remained below the Reserve Bank's mid-point target of 2.0%. This has been largely due to the weak tradables inflation. Two-year-ahead inflation expectations dipped further below 2.0% in the December 2019 quarter, coming in at 1.8%, the lowest level since late-2016. The slowdown in inflation expectations, combined with a forecast slowdown in GDP growth in the near-term, underpin an assumption that the OCR will be cut by 25bps in early 2020. Stimulatory monetary policy helps push CPI inflation closer to the target mid-point.

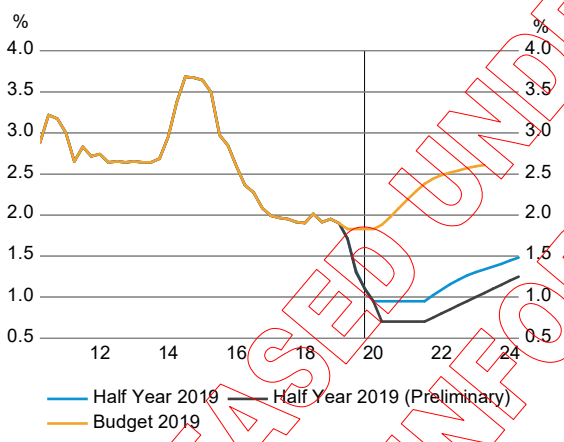
***Interest rates are forecast to remain on hold until late 2021, pushing inflation back to target…***

22. With interest rates remaining low, activity accelerates and non-tradable inflationary pressures increase. Tradables inflation is also forecast to increase at a faster pace supported by a weaker New Zealand dollar. CPI inflation is forecast to reach the mid-point target in late 2020 and remain broadly stable after that.

***…but remain at historic lows***

23. After the forecast cut to the OCR in early 2020, the Treasury forecasts the 90-day interest rate to remain unchanged until late 2021, which is in line with market expectations as of 15 November. Interest rates are forecast to rise gradually from late 2021 to keep inflation at 2.0% as capacity pressures intensify. Interest rates increase by 50 basis points by June 2024, which is small relative to previous movements. This is largely because the tightening in capacity constraints remains limited and due to the OCR being less stimulatory than assumed at BEFU.[2] The change in the forecasts for the 90-day interest rate from HYEFU preliminary forecasts is owing to the change in market expectations, reflecting improved sentiment about the economic outlook.

**Figure 5: 90-day bank bill rates**




***After slowing in the near-term, rising labour income growth and faster house price inflation support household spending.***

24. Employment growth has been slowing in recent years and has been accompanied by a decline in labour supply growth, which has seen the unemployment rate average just above 4.0%. In the near-term, slowing economic activity is expected to continue to affect hiring decisions seeing employment growth slow to 1.4% in 2019/20, weighing on household consumption.

25. Beyond 2019/20, a modest increase in economic growth sees employment growth rise together with rising house price growth support an increase in household consumption growth from 2.3% in 2019/20 to 2.8% in 2023/24. Private consumption growth remains low relative to recent years as households are cautious, given the uncertain outlook and elevated debt to income ratios.

26. **The labour market is expected to remain tight despite a weaker growth outlook relative to BEFU 2019.** We forecast the unemployment rate to rise from 4.2% in September 2019 to 4.3% by the end of the forecast period. Wage growth remains elevated relative to recent history supported by a tight labour market and government labour market policies. However, the lower-than-forecast outturn the September 2019 quarter is carried forward to mid-2021.

[2] The change in the Treasury's assumption on the "neutral rate of interest" was discussed in the latest Monthly Economic Indicators (October): https://treasury.govt.nz/system/files/2019-11/mei-oct19.pdf

**Figure 6: Wage growth**

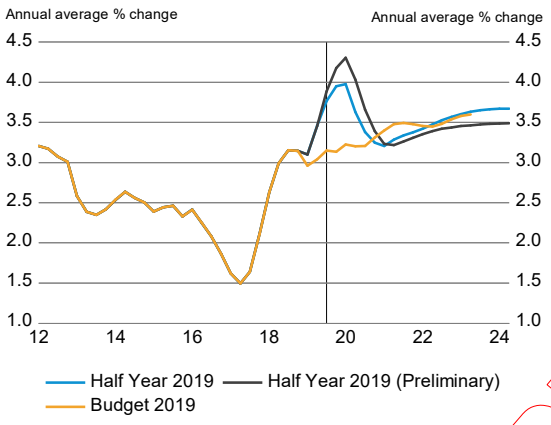
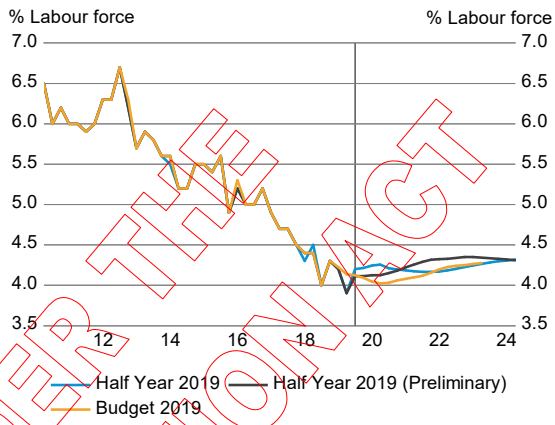



**Figure 7: Unemployment rate**




***Demand for New Zealand's commodity exports remains robust, however a weakening world outlook constraints tourism growth***

27. While aggregate trading partner growth is forecast to moderate over the forecast period, household consumption is likely to hold up. Given the nature of New Zealand's exports, the demand for New Zealand's exports is forecast to hold up.

28. Meat price growth is projected to continue to increase as Chinese consumers seek alternative protein options with African swine fever depleting pork stocks. Dairy prices have come off their recent peak. However, a continued solid demand should see modest increases in prices over the forecast period.

29. While much of the impact of global jitters on the New Zealand economy has been indirect through its influence on confidence and therefore investment, weaker demand for services exports, particularly tourism, represents a key direct link. We forecast tourism growth to remain subdued in the near-term, which is the largest contributing factor for weaker growth in exports relative to BEFU 2019.

***Nominal GDP…***

30. Relative to BEFU 2019, nominal GDP is cumulatively $5.4 billion lower over the four years to June 2023. Relative to the preliminary forecasts, nominal GDP is $7.3 billion higher over the five years to June 2024.

## Tax Outlook

31. Core crown tax is forecast to be $2.5 billion higher over the forecast period compared to HYEFU preliminary forecasts, mainly owing to the inclusion of the fiscal package and a higher interest rate track due to the removal of one interest rate cut. As a percentage of GDP, the final tax revenue forecasts are similar to the preliminary forecasts.

32. Over the forecast period, the changes in the tax forecasts broadly follow changes in the macroeconomic forecasts, namely:

- a stronger growth profile for operating surplus as a result of the fiscal package has raised our forecasts of corporate tax from 2021 onwards. In 2020, the stronger operating surplus growth has more-than-offset a downgrade to the NZS Fund's income tax forecast
- net other persons tax has increased by $0.6 billion, mainly owing to higher contracting income from the fiscal package and the effect of a lift in dairy prices on entrepreneurial income, and
- the removal of one rate cut in our forecasts has resulted in Resident Withholding Tax (RWT) on interest increasing by $0.3 billion in total across the forecast period.

33. The effect of the fiscal package will flow mainly through the business channel rather than through households. This has caused an increase in the forecasts of business income taxes, such as corporate tax and other persons tax, while leaving household-related taxes, such as source deductions and GST, virtually unchanged.

**Table 3: Estimated change in core Crown tax revenue forecasts[3]**

| June years, $ billions | 2019 | 2020 | 2021 | 2022 | 2023 | 2024 | Totals |
|---|---|---|---|---|---|---|---|
| 2019 HYEFU Prelim | 86.5 | 89.2 | 93.9 | 98.4 | 104.0 | 109.5 | |
| % of GDP | 28.8 | 28.3 | 28.4 | 28.4 | 28.6 | 28.7 | |
| *Forecasting changes by tax type:* | | | | | | | |
| Corporate tax | - | -0.4 | +0.3 | +0.5 | +0.5 | +0.5 | +1.4 |
| Net other persons tax | - | - | +0.1 | +0.1 | +0.1 | +0.1 | +0.4 |
| RWT on interest | - | - | +0.1 | +0.1 | +0.1 | - | +0.3 |
| Source deductions | - | -0.1 | - | +0.1 | +0.1 | +0.2 | +0.3 |
| GST | - | -0.1 | - | - | - | - | -0.1 |
| All other taxes | - | +0.1 | -0.1 | - | - | +0.2 | +0.2 |
| ***Total forecasting change*** | ***-*** | ***-0.5*** | ***+0.4*** | ***+0.8*** | ***+0.8*** | ***+1.0*** | ***+2.5*** |
| **2019 Half-year Update final** | **86.5** | **88.7** | **94.3** | **99.2** | **104.8** | **110.5** | |
| % of GDP | 28.8 | 28.1 | 28.4 | 28.4 | 28.6 | 28.8 | |
| ***Total change since 2019 BEFU*** | ***1.8*** | ***-0.5*** | ***-0.8*** | ***-1.0*** | ***-0.8*** | | |

34. Compared to the 2019 BEFU forecasts, core Crown tax revenue is $3.1 billion lower across the years 2020 to 2023 (2024 was not forecast in the 2019 BEFU). Changes to nominal GDP forecasts reduced the tax revenue forecast by $4 billion, and changes to interest rate forecasts reduced the forecasts of RWT on interest by $2.1 billion. Partially offsetting these effects, the underlying strength (relative to the 2019 BEFU forecast) in tax revenue in the year to June 2019 added $3 billion to the forecast.

35. Inland Revenue has also prepared a set of tax forecasts, based on the Treasury's economic forecasts, but using their own tax forecasting models and judgements. Across the five years of the forecast period, the Treasury's forecasts are in total $0.7 billion lower than Inland Revenue's, equivalent to around 0.1% of total tax revenue (Table 4).

[3] Crown tax eliminations have not yet been finalised. Therefore the numbers in table 3 may differ from the final core Crown tax revenue forecast that will be included in the consolidated fiscal forecasts of 25 November.

**Table 4: Differences between the Treasury and Inland Revenue forecasts**

| June years, $ billions | 2020 | 2021 | 2022 | 2023 | 2024 | 5-yr total |
|---|---|---|---|---|---|---|
| Treasury forecast | 88.7 | 94.3 | 99.2 | 104.8 | 110.5 | |
| Inland Revenue forecast | 89.1 | 94.5 | 99.3 | 104.9 | 110.4 | |
| *Treasury less Inland Revenue* | *-0.4* | *-0.2* | *-0.1* | *-0.1* | *+0.1* | *-0.7* |
| *Percentage difference* | *-0.4%* | *-0.2%* | *-0.1%* | *-0.1%* | *0.1%* | *-0.1%* |

## Risks to the Economic Outlook

36. **Risks to the international outlook remain prevalent and skewed to the downside**. We assume growth in our top 16 trading partners falls from 3.8% in 2019 to 3.1% in 2020, before making a modest recovery. A more severe slowing in global growth is a key risk to the forecasts. Such a slowdown could be triggered by a weakening in global labour markets and household incomes, a further escalation in trade tensions, or a major adjustment in global financial or equity markets as a result of a more disruptive Brexit.

37. These events could have large spill-over effects due to the interconnectedness of the global economy, leading to a sharper and broader decline in trading partner growth. The New Zealand economy would be impacted through a range of channels including reduced demand for exports, export commodity price movements and shifts in financial conditions and asset prices.

**BUDGET SENSITIVE**

# Annex 1: Forecast Summary Tables

## Table A1: Summary of Economic Forecasts – June Years

| June Years | 2016 | 2017 | 2018 | 2019 | 2020 Forecast | 2021 Forecast | 2022 Forecast | 2023 Forecast | 2024 Forecast |
|---|---|---|---|---|---|---|---|---|---|
| Private consumption | 4.4 | 5.6 | 3.6 | 3.3 | 2.3 | 2.6 | 2.9 | 2.9 | 2.8 |
| Public consumption | 1.5 | 2.6 | 2.9 | 2.1 | 3.6 | 2.3 | 1.3 | 1.1 | 1.1 |
| **TOTAL CONSUMPTION** | **3.7** | **4.9** | **3.5** | **3.0** | **2.6** | **2.5** | **2.5** | **2.5** | **2.4** |
| Residential investment | 9.9 | 4.2 | 2.6 | 4.0 | 5.6 | 5.6 | 3.4 | 1.6 | 1.1 |
| Business investment* | 2.4 | 2.1 | 6.7 | 0.9 | 1.5 | 4.2 | 3.9 | 3.0 | 2.5 |
| **TOTAL INVESTMENT** | **4.2** | **2.6** | **5.6** | **1.7** | **2.6** | **4.6** | **3.8** | **2.6** | **2.2** |
| Stocks (contribution to GDP growth) | -0.3 | 0.3 | -0.1 | -0.2 | 0.1 | -0.1 | 0.0 | 0.0 | 0.0 |
| **GROSS NATIONAL EXPENDITURE** | **3.4** | **4.7** | **4.0** | **2.4** | **2.8** | **2.8** | **2.9** | **2.5** | **2.4** |
| Exports | 5.7 | 0.6 | 3.9 | 2.5 | 0.6 | 3.0 | 2.5 | 2.4 | 2.5 |
| Imports | 1.2 | 6.2 | 8.0 | 1.7 | 1.7 | 3.2 | 3.1 | 2.6 | 2.4 |
| **EXPENDITURE ON GDP** | **4.5** | **3.1** | **3.0** | **2.6** | **2.5** | **2.8** | **2.7** | **2.5** | **2.4** |
| **GDP (PRODUCTION MEASURE)** | **3.6** | **3.4** | **3.2** | **2.4** | **2.2** | **2.8** | **2.7** | **2.5** | **2.4** |
| *- annual % change, June quarter* | 4.0 | 3.1 | 3.2 | 2.1 | 2.3 | 2.9 | 2.6 | 2.4 | 2.4 |
| **Other Output Measures** | | | | | | | | | |
| Real Gross National Disposable Income | 3.8 | 4.3 | 3.5 | 2.2 | 3.0 | 2.7 | 2.6 | 2.3 | 2.2 |
| Nominal GDP (Expenditure Basis) | 5.1 | 6.3 | 5.7 | 3.7 | 5.1 | 5.2 | 5.3 | 4.9 | 4.8 |
| Potential GDP | 3.0 | 3.0 | 2.8 | 2.7 | 2.6 | 2.6 | 2.6 | 2.6 | 2.6 |
| Output gap (June qtr,% of potential) | 0.4 | 0.5 | 0.9 | 0.4 | 0.1 | 0.4 | 0.4 | 0.3 | 0.1 |
| **Total Population (thousands, mean quarter ended)** | 4,670 | 4,759 | 4,835 | 4,912 | 4,983 | 5,055 | 5,126 | 5,194 | 5,259 |
| **Real GDP per capita (Production basis)** | 1.7 | 1.4 | 1.4 | 0.8 | 0.7 | 1.4 | 1.3 | 1.1 | 1.1 |
| **Labour Market** | | | | | | | | | |
| Employment | 2.2 | 4.8 | 3.1 | 1.7 | 1.4 | 2.1 | 1.9 | 1.6 | 1.5 |
| Unemployment Rate (June quarter) | 5.0 | 4.7 | 4.5 | 3.9 | 4.3 | 4.2 | 4.2 | 4.3 | 4.3 |
| Labour Productivity (Hours worked basis) | 0.8 | -1.2 | -0.6 | 1.2 | 0.2 | 1.0 | 0.8 | 0.9 | 1.0 |
| Wages (QES average hourly ord time earnings, APC) | 2.1 | 1.5 | 3.0 | 4.4 | 3.0 | 3.3 | 3.6 | 3.7 | 3.7 |
| **Monetary Conditions** | | | | | | | | | |
| 90-day Bank Bill Rate (June quarter ave) | 2.4 | 2.0 | 2.0 | 1.7 | 1.0 | 1.0 | 1.2 | 1.3 | 1.5 |
| 10-year Bond Rate (June quarter ave) | 2.7 | 2.9 | 2.8 | 1.8 | 1.3 | 1.5 | 1.8 | 2.3 | 2.6 |
| TWI (June quarter ave) | 73.6 | 76.5 | 73.8 | 72.7 | 70.8 | 70.8 | 71.6 | 72.1 | 72.6 |
| - annual % change (June quarter) | -3.4 | 3.9 | -3.5 | -1.5 | -2.6 | 0.0 | 1.1 | 0.8 | 0.6 |
| **Price Measures** | | | | | | | | | |
| CPI Inflation (ann % change, June quarter) | 0.4 | 1.7 | 1.5 | 1.7 | 1.9 | 1.9 | 2.0 | 2.0 | 2.0 |
| Consumption Deflator | 0.8 | 0.9 | 1.3 | 1.7 | 1.7 | 2.3 | 2.4 | 2.3 | 2.2 |
| GDP Deflator | 0.6 | 3.1 | 2.7 | 1.0 | 2.6 | 2.4 | 2.5 | 2.4 | 2.3 |
| House Price Inflation (ann % change, June qtr) | 15.0 | 6.5 | 3.6 | 1.3 | 4.9 | 6.1 | 6.2 | 5.6 | 4.9 |
| **Key Balances** | | | | | | | | | |
| Current account balance ($ million) | -5,423 | -7,046 | -9,597 | -10,296 | -10,168 | -11,209 | -12,453 | -13,507 | -14,424 |
| Current account balance (% of GDP) | -2.1 | -2.6 | -3.3 | -3.4 | -3.2 | -3.4 | -3.6 | -3.7 | -3.8 |
| Terms of Trade (goods) - SNA Basis | -2.7 | 5.0 | 4.6 | -3.4 | 1.8 | -0.3 | 0.1 | 0.2 | 0.3 |
| Household saving ratio (% of HHDI, June yr) | -0.6 | 0.1 | -1.4 | -0.7 | 1.1 | 0.9 | 0.5 | 0.3 | 0.4 |
| Net International Investment Position (%GDP) | -62.1 | -55.0 | -53.4 | -55.3 | -55.8 | -56.5 | -57.2 | -58.2 | -59.3 |

* Total investment excluding residential

**BUDGET SENSITIVE**

## Table A2: Change in Economic Forecasts from Preliminary HYEFU – June Years

| June Years | 2016 | 2017 | 2018 | 2019 | 2020 Forecast | 2021 Forecast | 2022 Forecast | 2023 Forecast | 2024 Forecast |
|---|---|---|---|---|---|---|---|---|---|
| Private consumption | 0.0 | 0.0 | 0.0 | 0.0 | -0.0 | 0.0 | 0.1 | 0.1 | 0.1 |
| Public consumption | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| **TOTAL CONSUMPTION** | **0.0** | **0.0** | **0.0** | **0.0** | **-0.0** | **0.0** | **0.1** | **0.1** | **0.0** |
| Residential investment | 0.0 | 0.0 | 0.0 | 0.0 | -1.0 | 0.5 | 0.5 | -0.4 | -0.7 |
| Business investment* | 0.0 | 0.0 | 0.0 | 0.0 | 0.1 | 2.0 | 1.6 | 0.1 | -0.5 |
| **TOTAL INVESTMENT** | **0.0** | **0.0** | **0.0** | **0.0** | **-0.2** | **1.6** | **1.3** | **-0.0** | **-0.6** |
| Stocks (contribution to GDP growth) | 0.0 | 0.0 | 0.0 | 0.0 | 0.1 | -0.2 | 0.0 | 0.0 | 0.0 |
| **GROSS NATIONAL EXPENDITURE** | **0.0** | **0.0** | **0.0** | **0.0** | **0.1** | **0.2** | **0.4** | **0.0** | **-0.1** |
| Exports | 0.0 | 0.0 | 0.0 | 0.0 | -0.8 | 0.5 | 0.1 | 0.1 | 0.2 |
| Imports | 0.0 | 0.0 | 0.0 | 0.0 | -0.0 | 0.3 | 0.4 | 0.1 | -0.1 |
| **EXPENDITURE ON GDP** | **0.0** | **0.0** | **0.0** | **0.0** | **-0.1** | **0.2** | **0.3** | **0.0** | **-0.0** |
| **GDP (PRODUCTION MEASURE)** | **0.0** | **0.0** | **0.0** | **0.0** | **-0.1** | **0.2** | **0.3** | **0.0** | **-0.0** |
| *- annual % change, June quarter* | *0.0* | *0.0* | *0.0* | *0.0* | *-0.1* | *0.4* | *0.2* | *-0.0* | *-0.0* |
| **Other Output Measures** | | | | | | | | | |
| Real Gross National Disposable Income | 0.0 | 0.0 | 0.0 | 0.0 | -0.1 | 0.2 | 0.2 | -0.1 | -0.1 |
| Nominal GDP (Expenditure Basis) | 0.0 | 0.0 | 0.0 | 0.0 | -0.1 | 0.4 | 0.4 | 0.0 | -0.0 |
| **Per Capita Output Measures** | | | | | | | | | |
| Real GDP per capita (Production basis) | 0.0 | 0.0 | 0.0 | 0.0 | -0.0 | 0.3 | 0.3 | 0.0 | -0.0 |
| Real Gross Nat. Disp Income per capita | 0.0 | 0.0 | 0.0 | 0.0 | -0.1 | 0.3 | 0.2 | -0.1 | -0.1 |
| Nominal GDP per capita (Expenditure basis) | 0.0 | 0.0 | 0.0 | -0.0 | -0.0 | 0.4 | 0.4 | 0.0 | -0.0 |
| **Labour Market** | | | | | | | | | |
| Employment | -0.0 | 0.0 | -0.0 | 0.0 | -0.2 | 0.1 | 0.2 | -0.0 | -0.1 |
| Unemployment Rate (June quarter) | 0.0 | 0.0 | 0.1 | 0.0 | 0.1 | -0.1 | -0.1 | -0.1 | 0.0 |
| Labour Productivity (Hours worked basis) | 0.0 | 0.0 | 0.0 | 0.0 | -0.2 | 0.2 | 0.0 | 0.0 | 0.0 |
| Wages (QES average hourly ord time earnings, APC) | -0.0 | -0.0 | -0.0 | -0.0 | -0.3 | 0.1 | 0.1 | 0.2 | 0.2 |
| Unit Labour Costs (Hours worked basis) | -0.0 | -0.0 | -0.0 | 0.0 | -0.2 | -0.2 | 0.0 | 0.1 | 0.1 |
| **Monetary Conditions** | | | | | | | | | |
| 90-day Bank Bill Rate (June quarter ave) | 0.0 | 0.0 | 0.0 | 0.0 | 0.3 | 0.3 | 0.3 | 0.3 | 0.2 |
| 10-year Bond Rate (June quarter ave) | 0.0 | 0.0 | 0.0 | 0.0 | 0.4 | 0.4 | 0.4 | 0.5 | 0.5 |
| TWI (June quarter ave) | 0.0 | 0.0 | 0.0 | 0.0 | 0.8 | 0.8 | 0.7 | 0.4 | 0.1 |
| - annual % change, June quarter | 0.0 | 0.0 | 0.0 | 0.0 | 1.1 | 0.0 | -0.2 | -0.4 | -0.4 |
| **Price Measures** | | | | | | | | | |
| CPI Inflation (ann % change, June quarter) | 0.0 | 0.0 | 0.0 | 0.0 | 0.1 | -0.0 | 0.0 | 0.0 | 0.1 |
| Consumption Deflator | 0.0 | 0.0 | 0.0 | 0.0 | -0.0 | -0.0 | 0.0 | 0.0 | 0.1 |
| GDP Deflator | 0.0 | 0.0 | 0.0 | 0.0 | -0.0 | 0.1 | 0.1 | -0.0 | 0.0 |
| House Price Inflation (ann % change, June quarter) | 0.0 | 0.0 | 0.0 | 0.4 | 0.5 | -0.3 | -0.2 | -0.2 | -0.1 |
| **Key Balances** | | | | | | | | | |
| Current account balance ($ million) | 0 | 0 | 0 | 0 | -632 | -459 | -997 | -1,451 | -1,632 |
| Current account balance (% of GDP) | 0.0 | 0.0 | 0.0 | 0.0 | -0.2 | -0.1 | -0.3 | -0.4 | -0.4 |
| Terms of Trade - SNA Basis | 0.0 | 0.0 | 0.0 | 0.0 | 0.1 | 0.1 | -0.1 | -0.0 | 0.1 |
| Household saving ratio (% of HHDI, March year) | 0.0 | 0.0 | 0.0 | -0.1 | 0.2 | 0.2 | 0.3 | 0.2 | 0.2 |

* Total investment excluding residential

## Table A3: Change in Economic Forecasts from BEFU – June Years

| June Years (Annual average percent change, unless specified otherwise) | 2016 | 2017 | 2018 | 2019 | 2020 Forecast | 2021 Forecast | 2022 Forecast | 2023 Forecast |
|---|---|---|---|---|---|---|---|---|
| Private consumption | 0.0 | 0.0 | 0.0 | -0.3 | -0.6 | -0.3 | 0.2 | 0.2 |
| Public consumption | -0.0 | -0.0 | -0.1 | 0.2 | -0.6 | 0.5 | 0.4 | 0.1 |
| **TOTAL CONSUMPTION** | **0.0** | **0.0** | **-0.0** | **-0.2** | **-0.6** | **-0.1** | **0.2** | **0.1** |
| Residential investment | -0.0 | -0.0 | 0.0 | 0.6 | 0.4 | 0.2 | -0.0 | -0.4 |
| Business investment* | -0.0 | 0.0 | -0.1 | 0.2 | -2.3 | 0.5 | 1.5 | 0.9 |
| **TOTAL INVESTMENT** | **-0.0** | **0.0** | **-0.0** | **0.3** | **-1.6** | **0.5** | **1.1** | **0.5** |
| Stocks (contribution to GDP growth) | 0.0 | -0.0 | -0.0 | -0.1 | 0.2 | -0.1 | 0.0 | 0.0 |
| **GROSS NATIONAL EXPENDITURE** | **0.0** | **0.0** | **-0.0** | **-0.3** | **-0.3** | **-0.3** | **0.5** | **0.2** |
| Exports | 0.3 | 0.3 | 0.3 | -0.3 | -2.5 | 0.2 | -0.1 | -0.1 |
| Imports | 0.1 | 0.0 | 0.1 | -0.4 | -2.2 | -0.2 | 0.8 | 0.4 |
| **EXPENDITURE ON GDP** | **0.1** | **0.1** | **0.1** | **0.1** | **-0.7** | **-0.2** | **0.2** | **0.1** |
| **GDP (PRODUCTION MEASURE)** | **-0.0** | **0.0** | **0.0** | **0.1** | **-0.8** | **-0.0** | **0.3** | **0.1** |
| *- annual % change, June quarter* | *0.0* | *0.0* | *0.0* | *-0.0* | *-0.9* | *0.3* | *0.3* | *0.1* |
| **Other Output Measures** | | | | | | | | |
| Real Gross National Disposable Income | 0.0 | -0.1 | -0.1 | -0.3 | -0.3 | -0.2 | 0.2 | 0.1 |
| Nominal GDP (Expenditure Basis) | 0.1 | 0.1 | 0.1 | -0.1 | -0.7 | -0.2 | 0.4 | 0.2 |
| **Per Capita Output Measures** | | | | | | | | |
| Real GDP per capita (Production basis) | 0.1 | 0.2 | 0.3 | 0.2 | -0.9 | -0.2 | 0.0 | -0.1 |
| Real Gross Nat. Disp Income per capita | 0.1 | 0.1 | 0.3 | -0.2 | -0.4 | -0.4 | -0.0 | -0.1 |
| Nominal GDP per capita (Expenditure basis) | 0.2 | 0.3 | 0.4 | -0.0 | -0.7 | -0.4 | 0.2 | 0.0 |
| **Labour Market** | | | | | | | | |
| Employment | -0.2 | -0.4 | -0.6 | -0.6 | -0.5 | 0.4 | 0.6 | 0.4 |
| Unemployment Rate (June quarter) | 0.0 | 0.0 | 0.1 | -0.2 | 0.2 | 0.1 | -0.0 | -0.0 |
| Labour Productivity (Hours worked basis) | 0.2 | 0.4 | 0.6 | -0.2 | -0.1 | -0.2 | -0.3 | -0.2 |
| Wages (QES average hourly ord time earnings, APC) | -0.0 | -0.0 | -0.0 | 1.1 | -0.2 | -0.2 | 0.1 | 0.1 |
| Unit Labour Costs (Hours worked basis) | -0.2 | -0.4 | -0.6 | 0.7 | 0.5 | 0.0 | 0.4 | 0.3 |
| **Monetary Conditions** | | | | | | | | |
| 90-day Bank Bill Rate (June quarter ave) | 0.0 | 0.0 | 0.0 | -0.1 | -0.9 | -1.3 | -1.4 | -1.3 |
| 10-year Bond Rate (June quarter ave) | 0.0 | 0.0 | 0.0 | -0.1 | -1.0 | -1.0 | -1.0 | -0.7 |
| TWI (June quarter ave) | 0.0 | 0.0 | 0.0 | -1.0 | -2.9 | -3.0 | -2.4 | -1.9 |
| - annual % change, June quarter | 0.0 | 0.0 | 0.0 | -1.4 | -2.6 | -0.1 | 0.7 | 0.7 |
| **Price Measures** | | | | | | | | |
| CPI Inflation (ann % change, June quarter) | 0.0 | 0.0 | 0.0 | -0.1 | -0.2 | -0.2 | -0.1 | -0.0 |
| Consumption Deflator | -0.0 | -0.0 | 0.0 | -0.1 | -0.7 | -0.1 | 0.2 | 0.2 |
| GDP Deflator | 0.0 | -0.0 | 0.0 | -0.2 | 0.0 | -0.0 | 0.2 | 0.2 |
| House Price Inflation (ann % change, June quarter) | 0.0 | 0.0 | 0.0 | -1.7 | 1.1 | 1.8 | 1.9 | 0.8 |
| **Key Balances** | | | | | | | | |
| Current account balance ($ million) | 361 | 337 | 213 | -186 | 597 | 219 | -752 | -1,348 |
| Current account balance (% of GDP) | 0.1 | 0.1 | 0.1 | -0.1 | 0.2 | 0.0 | -0.2 | -0.4 |
| Terms of Trade - SNA Basis | -0.0 | 0.0 | -0.2 | -1.5 | 1.6 | -0.4 | -0.1 | 0.1 |
| Household saving ratio (% of HHDI, March year) | 0.0 | 0.0 | 0.0 | -0.1 | 1.4 | 1.5 | 1.3 | 1.2 |

* Total investment excluding residential

BUDGET-REPORT-SENSITIVE

TE TAI ŌHANGA
THE TREASURY

Reference: T2019/3597 BM-2-3-2019-2

Date: 18 November 2019

To: Minister of Finance (Hon Grant Robertson)

Deadline: Tuesday 19 November 2019



# Aide Memoire: Phasing of Additional Capital Investment

This aide memoire outlines our approach to phasing the additional $12 billon capital investment agreed by Cabinet on 4 November 2019 (CAB-19-MIN-0572). The phasing profile outlined in this note will be incorporated into the Treasury forecasts presented in the 2019 Half Year Economic and Fiscal Update (HYEFU).

## Background

The forecasts presented in the Economic and Fiscal Updates represents the Treasury's best estimate of the economic and fiscal outlook based on our best professional judgement. With the recent Cabinet decision to announce an additional $12 billion capital package at the Budget Policy Statement (BPS), the Treasury has made some judgements to determine the phasing profile for this additional investment.

For modelling, the fiscal impact of the additional spending in the scenarios presented in our advice on the Fiscal Strategy for the 2020 Budget Policy Statement (T2019/3343) a simple and high-level assumption was used to determine the spending profile. Given the intention is to announce a specific Capital package at the BPS it is important that our forecast best reflect the impact from this package.

## Phasing Assumptions

Our understanding is the Government's intention is to commit and announce $8 billion of the additional capital investment at the BPS, with the remaining $4 billion added to the Multi-Year Capital Allowance (MYCA). We have looked at these two components separately in forming our view on the phasing profile. The reason for this is the Capital package to be announced at the BPS is likely to be more certain in nature (e.g. quantified by specific sectors) than the increase in the MYCA.

For the Capital package we do not have details of the specific projects and their timing to incorporate into our economic forecasts (finalised 8 November) and our fiscal forecast (finalised 25 November). Therefore, we have applied some key judgements in determining our phasing assumptions for what will be included in our HYEFU forecast.

*Table 1: – Summary of key judgements*

| | Capital Package | Increase to MYCA |
|---|---|---|
| **Amount** | $8 billion | $4 billion |
| **Sector Split** | Based on the list of sectors identified and discussions with your office, we have split the amount of the Capital Package into the following categorises:<br>• Transport short-term projects **($1.8 billion)**;<br>• Transport medium projects **($5.0 billion)**; and<br>• Other sectors **($1.2 billion)**. | Not specified |
| **Timing** | In determining the timing assumption of the investments we have looked at the three categories separately.<br>• For the **transport short-term projects** we have assumed this is invested equally over the next four years (2021 to 2024). This phasing is based on analysis provided by NZTA around possible projects that could commence within the next 18 months.<br>• For the transport **medium-term projects** we have used data provided by NZTA on projects which could commence after 24 months. At an aggregated level, the analysis showed 45% of the spending on these projects would occur within the forecast period. The phasing for the portion that falls within the forecast period has been spread based on the project breakdown provided by NZTA.<br>• For the investment in **other sectors**, we have assumed this spending occurs equally over the next two fiscal years (2021 to 2022). | It is assumed this will be allocated equally across the next four budgets and then phased by fiscal year (over a five-year period) based on previous historical trends of new capital investments **(This is consistent with our current approach for allocation the MYCA)**. |

## Fiscal Implications

Based on the above judgements we expect that $8.1 billion of the additional capital investments will fall within the forecast period. If added to our preliminary HYEFU forecasts, net capital investments would be around $49 billion over the next five years.

*Table 2: – Phasing of additional capital investment*

| $millions | 2019/20 | 2020/21 | 2021/22 | 2022/23 | 2023/24 | Post-2024 | Total |
|---|---|---|---|---|---|---|---|
| Capital Package at BPS | - | 1,075 | 1,350 | 1,275 | 1,275 | 3,025 | 8,000 |
| Increase to Multi-Year Capital Allowance | 50 | 400 | 750 | 950 | 950 | 900 | 4,000 |
| | 50 | 1,475 | 2,100 | 2,225 | 2,225 | 3,925 | 12,000 |

The additional capital investment is a key driver of the stronger economic growth and tax revenue now expected compared to our preliminary forecast (refer T2019/3638). The impact on key fiscal indicators from the additional capital investment and updated tax revenue forecasts are modelled in Table 3.

*Table 3: – Fiscal impact from the additional capital investment*[1]

| $millions | 2019/20 | 2020/21 | 2021/22 | 2022/23 | 2023/24 |
|---|---|---|---|---|---|
| Net Debt - Prelims | 61,459 | 68,098 | 72,492 | 72,969 | 70,462 |
| Net Debt - Prelims Update | 62,271 | 69,993 | 75,733 | 77,644 | 76,454 |
| **Difference** | **812** | **1,895** | **3,241** | **4,675** | **5,992** |
| Net Debt % of GDP - Prelims | 19.5% | 20.6% | 20.9% | 20.1% | 18.5% |
| Net Debt % of GDP - Prelims Update | 19.7% | 21.1% | 21.7% | 21.2% | 19.9% |
| OBEGAL - Prelims | (370) | (646) | 790 | 3,191 | 5,165 |
| OBEGAL - Prelim Update | (824) | (254) | 1,544 | 3,982 | 6,073 |
| **Difference** | **(454)** | **392** | **754** | **791** | **908** |

The final fiscal forecasts are due to be completed on Monday 25 November. In addition to the changes modelled in Table 3, there are a number of other items that we are aware of that are likely to influence our final forecasts. Some items worth particular note are:

- benefit expense forecasts will be updated to reflect our final economic forecast and the most recent actual data;
- finance cost forecasts will be updated to reflect additional funding requirements and our final economic forecast;

[1] The Prelims Update numbers in the this table only reflect the impact of the additional Capital investments, final tax revenue forecasts and the flow through to debt servicing cost which has been modelled from the Fiscal Strategy Model. In addition, the net debt to GDP ratio is calculated using our nominal GDP from our final HYEFU economic forecast.

- the top-down adjustment will need to be reassessed for final forecasts received from departments and recent Government decisions (e.g. additional capital investment);
- s9(2)(f)(iv)
- 
- the Government Superannuation Fund (GSF) liability will be updated and will reflect the continued drop in discount rates since 30 June 2019.

**Presentation of the additional capital investment**

The Capital package will be included as an unallocated contingency in our fiscal forecasts. Table 4 provides a mock-up of the proposed disclosure in the notes to the forecast financial statements. The numbers in Table 4 are based on the preliminary fiscal forecasts. In addition to the disclosures in the forecast financial statements, we will also need to consider our coverage in the other HYEFU chapters. It is highly likely we will be discussing the package at an aggregated level rather than any breakdown by sector in our chapters.

*Table 4: – Mock-up of the notes to the financial statements*

| | 2020 Forecast $m | 2021 Forecast $m | 2022 Forecast $m | 2023 Forecast $m | 2024 Forecast $m | Post-2024 Forecast $m | Total Forecast $m |
|---|---|---|---|---|---|---|---|
| **Forecast New Capital Spending (annual)** | | | | | | | |
| Unallocated contingencies | 652 | 1,522 | 1,728 | 1,632 | 1,710 | 4,299 | 11,543 |
| Forecast new spending for Budgets 2020 - 2023 | 123 | 980 | 1,838 | 2,256 | 1,821 | 2,206 | 9,224 |
| **Total forecast new capital spending** | **775** | **2,502** | **3,566** | **3,888** | **3,531** | **6,505** | **8,767** |
| Forecast new capital spending (cumulative) | **775** | **3,277** | **6,843** | **10,731** | **14,262** | | |

**Managing the operating expense implications for the Capital package**

The Capital package will have consequential impacts on operating expenses. The operating impacts will most likely relate to depreciation expenses on the new assets and any new services provided from the new assets. At this stage, the extent of the operating impact is difficult to quantify without knowing the details of the underlying assets forming the Capital package. For example, depreciation expense on assets could be spread over 3 to 200 years of its life depending on the type of asset. The majority of the Capital package is expected to be invested into roading projects. Based on 30 June 2018 information the deprecation expense on state highways (excluding land) was just above 1% of the overall value of the network.

From our understanding of the Capital package, our sense is the impact on operating expenses each year is likely to be minimal. From what we know, assets will be mostly long-term in nature and are unlikely to result in extending services provided by the Government. As a result, we would recommend that initially operating expenses are managed within existing baselines or existing funding arrangements (e.g. hypothecated revenue).

It is likely some sectors may find it harder than others to manage operating costs within existing baselines (e.g. health). If this is the case, any consequential operating costs could be managed against Budget allowances. If there is, more certainty of costs ahead of Budget 2020 a tagged contingency could be set up and then drawn down as projects are approved. An alternative to this option would be to fund any increased operating costs outside of allowances, however doing so would result in a directly reduction to OBEGAL.

**Next Steps**

There will be an opportunity to discuss this note at Budget Matters on Tuesday 19 November.

Kamlesh Patel, Team Leader, Fiscal Reporting, s9(2)(k)
Jayne Winfield, Manager, Fiscal Reporting, s9(2)(f)(iv)

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# Treasury Report: HYEFU 2019 Specific Fiscal Risks Draft Chapter

| | | | |
|---|---|---|---|
| **Date:** | 20 November 2019 | **Report No:** | T2019/3733 |
| | | **File Number:** | BM-2-9-2-2-2019-6 |

## Action Sought

| | Action Sought | Deadline |
|---|---|---|
| Minister of Finance<br>(Hon Grant Robertson) | **Agree** to exclude certain risks under s 26V of the Public Finance Act<br>**Note** the risks to be published in the chapter<br>**Inform** the Treasury of any feedback or other matters that should be considered for inclusion as Specific Fiscal Risks | 25 November 2019 |

## Contact for Telephone Discussion (if required)

| Name | Position | Telephone | | 1st Contact |
|---|---|---|---|---|
| Jessica Jenkins | Graduate Analyst, Budget Management | s9(2)(k) | N/A<br>(mob) | ✓ |
| Alex Harrington | Manager, Budget Management | | s9(2)(g)(i) | |

## 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 (attached)

# Treasury Report: HYEFU 2019 Specific Fiscal Risks Draft Chapter

## Executive Summary

This report outlines the Specific Fiscal Risks (SFRs) that will be published in the 2019 Half Year Economic and Fiscal Update (HYEFU), and seeks your agreement to exclude certain risks under s 26V of the Public Finance Act (PFA). We are available to discuss the contents of this report and the attached draft SFR Chapter with your office. We request your feedback on the chapter and agreement to exclude risks under s 26V by Monday 25 November.

**Purpose of Chapter**

The SFR chapter outlines material risks that may have an impact on the fiscal outlook but are not certain enough in timing or amount to include in the forecasts. Risks disclosed in the SFR chapter cover potential policy changes, cost pressures and cost variances. Risks are included in the chapter when they amount to more than $100 million over the forecast period, and have a 20% to 50% likelihood of occurring.

The SFR chapter also discloses the government's contingent liabilities and assets, however these have not been included in this report. They will be sent across separately with the final HYEFU chapters in the week of 2 December.

**Approach**

The SFR chapter takes a transparent approach to the disclosure of risks. Risks are disclosed to the fullest extent possible, regardless of how they can be managed. This is done to improve transparency and not pre-judge future decisions by the government. The overview section of the chapter outlines that the government has a number of mechanisms to manage these risks, with the expectation that government commitments and cost pressures will be managed through Budget allowances and/or baseline prioritisation.

## Recommended Action

We recommend that you:

a **note** that the Specific Fiscal Risks Chapter outlines risks to the fiscal outlook presented in the Treasury's Half Year Economic and Fiscal Update;

b **note** the new risks in the Half Year Economic and Fiscal Update, as set out at paragraph 12 of this report;

c **provide** feedback on the attached chapter to the Treasury by Monday 25 November;

d **inform** the Treasury of any other matters you consider should be included in the Chapter by Monday 25 November;

e **agree** to exclude the following risks under s 26V of the Public Finance Act 1989:

s9(2)(b)(ii)

s9(2)(f)(iv)

f **note** the risks that have expired since the Budget Economic and Fiscal Update, as set out in paragraph 18 of the report; and

g **note** the Treasury is still completing a final review of this chapter and a final version (including the section on contingent liabilities and assets) will be sent across in the week beginning 2 December, alongside the other chapters in the Half Year Economic and Fiscal Update.

Alex Harrington
**Manager, Budget Management**

Hon Grant Robertson
**Minister of Finance**

# Treasury Report: Treasury Report: HYEFU 2019 Specific Fiscal Risks Draft Chapter

## Purpose of Report

1. This report outlines the Specific Fiscal Risks (SFRs) intended for publication in the upcoming 2019 Half Year Economic and Fiscal Update (HYEFU). A draft of the SFR chapter is attached. We request your feedback on the chapter and agreement to exclude risks under s 26V by Monday 25 November.

2. This report covers the following:

   a information on the process and criteria for publishing risks in the chapter; and

   b risks to be withheld from publication.

## Process and Criteria for Specific Fiscal Risks

3. The purpose of the SFR chapter is to disclose fiscal risks which are likely to have a material impact on the fiscal forecasts but are not certain enough in timing or quantum to include in the fiscal forecasts. The nature of these risks can be positive or negative, and relate to either capital or operating activities.

4. Section 26U of the Public Finance Act 1989 (PFA) requires each Economic and Fiscal Update (EFU) to incorporate "all Government decisions and other circumstances that may have a material effect on the fiscal and economic outlook" to the fullest extent possible.

5. You are required to sign a Statement of Responsibility in the week beginning 2 December stating that:

   a you have communicated to the Secretary to the Treasury:

      i all policy decisions with material economic and fiscal implications that the Government has made before the day on which the forecasts are finalised (25 November for this EFU).

      ii all other circumstances with material economic or fiscal implications that you are aware of before that day; and

   b the disclosures in the EFU are consistent with Part 2 of the PFA, except for matters that are withheld under s 26V where disclosure might cause serious harm to the New Zealand Government or economy.

6. The Secretary to the Treasury is required to sign a Statement that she has supplied an EFU to the Minister of Finance that incorporates the fiscal and economic implications of those decisions and other circumstances. The Statement also certifies that the EFU has been prepared by the Treasury using its best professional judgement.

7. A specific fiscal risk is disclosed in the chapter if it meets the following criteria:

   a *Risk must be material* – likely to have a fiscal impact of more than $100 million over the forecast period; and

   b *Risk must be possible* – the matter might be approved or the risk might occur within the forecast period (i.e. there is a 20% to 50% chance of the matter being approved or occurring). Matters with a greater than 50% chance of being approved or occurring and that can be quantified for particular years with reasonable certainty are included in the fiscal forecasts.

8. The process for disclosure of SFRs is as follows:

   a Agencies submit SFRs with a likely fiscal impact of more than $10 million in any given year and a reasonable likelihood of materialising over the forecast period. The purpose of the lower threshold is to ensure all potential risks are captured, to provide oversight of risks that may become material in future.

   b SFRs are reviewed and signed off by Treasury Vote teams.

   c Risks are reviewed by an internal Treasury Risk Committee to ensure a consistent approach has been taken in the identification of risks for publication and determine whether there are any additional risks which have not been captured by the process.

9. There is a degree of judgement involved in determining which risks meet the materiality threshold for publication in the chapter, particularly given the uncertainty around the timing and quantum of some risks. These judgements are tested by the Risk Committee in the preparation of the chapter to ensure consistency across all portfolios.

## Risks Published in the Chapter

10. The risks in the chapter are categorised as:

    a **Policy changes:** potential decisions likely to be taken by the government related to both new policy and existing policy settings.

    b **Cost pressures:** changes in demand or pricing which impact the cost of delivering services under existing policy settings. This category also includes variances to the costs of policies included in the fiscal forecasts.

    c **Cross-portfolio risks:** general risks which are relevant to multiple portfolios.

11. We are still completing our final review of the chapter, and we will inform you of any significant changes that are made to the content in the attached chapter.

## New Risks

12. New risks disclosed in this Update's chapter are as follows:

| | Portfolio | Title | Potential impact |
|---|---|---|---|
| **Policy Changes** | Education | Education Workforce Strategy | Uncertain, but estimated by Ministry of Education (MoE) to be around $100 million across the forecast period. |
| | s9(2)(f)(iv) | | |
| | Housing | Progressive Home Ownership | s9(2)(f)(iv) |
| | s9(2)(f)(iv) | | |
| | Revenue | Purchase Price Allocation | |
| | Transport | Upper North Island Supply Chain Strategy (UNISCS) – Working Group Recommendations | |
| **Cost Pressures** | Arts Culture and Heritage | New Zealand Screen Production Grant – Domestic | s9(2)(b)(ii) |
| | Education | School Transport Services | The potential impact is unquantifiable at this stage, however MoE estimates it to be greater than $100 million over the forecast period, s9(2)(b)(ii) |
| | Police | Firearms Reform Programme | s9(2)(f)(iv) |
| | Social Development | Quarterly Employment Survey Redevelopment Impact on New Zealand Superannuation and Veteran's Pension | The Ministry of Social Development estimates a cost of $901 million across the forecast period (if the new Quarterly Employment Survey is 2% higher). |
| | Veterans | Accounting Treatment of Veteran's Disability Entitlements | s9(2)(f)(iv) |
| **Cross Portfolio** | Implementing a Living Wage in the Public Sector | | Unquantifiable at this stage. |
| | Possible Response to the Referendum on End of Life Choice | | Unquantifiable at this stage. |

13. Many of these new risks have been submitted as risks previously, but a recent announcement or event has pushed them over the materiality threshold for publication.

14. You have received a separate Aide Memoire (T2019/3653) on the new Social Development Quarterly Employment Survey Redevelopment risk. The Aide Memoire discussed the upper-end increase of 3% to give a sense of the potential maximum impact on OBEGAL. The draft SFR for publication refers to an increase 0-2%, which MSD views as a more likely bound for the increase, given information available at this stage.

15. The Living Wage risk was recently added by the Treasury, after we learned of several living wage-related budget bids. The wording of the description is subject to change, and we are happy to receive your feedback on the current description.

## Changed & Unchanged Risks

16. A number of risks that were published at BEFU had changed in nature. The narrative generally provides the reason for the change in status, however it is worth noting the following points which are not reflected in the risk narratives:

    a **Work-related Gradual Process Disease and Infection**
    The substance of this risk remains the same as at BEFU, however the quantum of the risk has increased by $500 million due to liability increasing over time. These numbers have been updated in the description.

    b **Early Learning Action Plan**
    A Cabinet Paper on the Plan is expected to go to Cabinet on 3 December 2019. Should any announcements follow, the description may need to be updated.

17. Several risks remain unchanged in nature, but the descriptions have been rewritten for accuracy:

    a **Delivery of the Government's Public Media Objectives**
    While the quantum and likelihood of this risk remains unchanged from BEFU, the description has been updated to say "The Government has committed to, and is currently considering options for, strengthening New Zealand public media." This change was made following the recent leak regarding the possibility of creating a new media entity.

    b **Extension of the Fees-free Tertiary Education Policy**
    The narrative has been updated, and removes the reference (as in the BEFU published narrative) to specific expansion years, and the possibility of bringing forward the third year. The new narrative is consistent with the Speech from the Throne intention to make the first three years fees-free in future parliamentary terms. While this is a small change, and has been agreed with MoE, you may wish to communicate this to the Minister of Education's office.

    c **DHB Sustainability**

    This risk description is largely similar to that published at BEFU, however it removes reference to a combined deficit figure because it is too early in the financial year to comment on the likely year-end deficit position. s9(2)(b)(ii) [redacted]

## Expired Risks

18. The following risks have been expired since BEFU because the risks have either materialised, are no longer material, or have been sufficiently captured by another risk:

| Portfolio | Title | Reason for expiry |
|---|---|---|
| Customs | Tobacco Excise Proposed Change | The tobacco excise will increase by 10% on 1 January 2020. This has been included in tax revenue forecasts. |
| Education | School and Early Childhood Education Funding Review | Decisions about the future direction of the previous Government's Review of Education Funding Systems were taken by Cabinet in May 2018. This included expanding previous work on replacing deciles to look more broadly at how wider system settings should address equity. s9(2)(f)(iv) |
| Greater Christchurch Regeneration | Canterbury Earthquake Recovery Residential Red Zone (RRZ) | The Crown has signed the Global Settlement Agreement with the Christchurch City Council. The expenses involved, including those related to the RRZ, are included in the fiscal forecasts. |
| Health | Dunedin Hospital | This risk has been expired as funding for this project is now in the fiscal forecasts. |
| Police | Firearms Buyback Scheme | The firearms amnesty and buy-back ends on 20 December 2019. While there remains a risk that the volume and type of firearms and parts surrendered may differ from expectations, the risk to forecasts is unlikely to be significant. |

## Risks to Withhold from Publication

19. Section 26V(1) of the PFA states that you may determine a matter be excluded from the EFU if disclosure would:

    a prejudice the substantial economic interests of New Zealand;

    b prejudice the security or defence of New Zealand, or the international relations of the government;

    c compromise the government in a material way in negotiation, litigation or commercial activity; or

    d result in a material loss of value to the government.

20. In making this determination, s 26V(2) requires you to consider whether the exclusion could be avoided, either by making a decision before the forecasts are finalised, or by disclosing the risk without publishing the quantum of the associated impact.

21. We recommend the following risks be withheld from publication under s 26V of the PFA, and do not consider that the exclusions could be avoided under s 26V(2):

s9(2)(b)(ii)

s9(2)(b)(ii)

## Next Steps

22. If you have any further information on matters that should be considered for inclusion as SFRs, or any questions or comments on the risks in the chapter, please raise them with us through your office by Monday 25 November.

23. You will receive a final version of the chapter (alongside other chapters in the HYEFU) in the week beginning 2 December. The final version will include a section concerning Contingent Liabilities and Assets, which will be signed off separately.

**From:** Catherine Manning [TSY]
**Sent:** Monday, 25 November 2019 6:50 PM
**To:** ^Parliament: Talei Pasikale
**Subject:** Final fiscal forecasts - HYEFU 19

**Follow Up Flag:** Follow up
**Flag Status:** Flagged

[SEEMAIL][SENSITIVE]

Hi Talei

Today we have finalised the fiscal forecasts for HYEFU 2019. They are based on the final economic forecasts (completed on 11 November). The table below shows the key fiscal indicators and the changes since the preliminary fiscal forecasts.

| | Forecast | | | | |
|---|---|---|---|---|---|
| $ billion, June years | 2019/20 | 2020/21 | 2021/22 | 2022/23 | 2023/24 |
| OBEGAL - final HYEFU 19 | (0.9) | 0.1 | 1.8 | 4.1 | 5.9 |
| OBEGAL - prelim HYEFU 19 | (0.4) | (0.6) | 0.8 | 3.2 | 5.2 |
| Total Change | (0.5) | 0.7 | 1.0 | 0.9 | 0.7 |
| Residual Cash - final HYEFU 19 | (5.2) | (8.0) | (5.6) | (2.2) | 0.9 |
| Residual Cash - prelim HYEFU 19 | (4.3) | (6.5) | (4.5) | (0.9) | 2.2 |
| Total Change | (0.9) | (1.5) | (1.1) | (1.3) | (1.3) |
| Net Debt - final HYEFU 19 | 62.5 | 70.6 | 76.1 | 77.7 | 76.3 |
| Net Debt - prelim HYEFU 19 | 61.5 | 68.1 | 72.5 | 73.0 | 70.5 |
| Total Change | (1.0) | (2.5) | (3.6) | (4.7) | (5.8) |
| % of GDP, June years | | | | | |
| Net Debt - final HYEFU 19 | 19.6 | 21.0 | 21.5 | 20.9 | 19.6 |
| Net Debt - prelim HYEFU 19 | 19.5 | 20.6 | 20.9 | 20.1 | 18.5 |

The operating balance before gains and losses (OBEGAL) beyond the current year has improved since the preliminary fiscal forecasts primarily due to

- improved tax forecasts largely owing to the capital investment package, and
- improved ACC forecasts owing to discount rates being updated which has resulted in a reduction in insurance expenses.

For the 2020/21 year the fiscal forecasts are now showing an OBEGAL surplus of $57 million which has changed from the deficit position forecast in the preliminary fiscal forecasts.

Residual cash and net debt are both showing a weaker track when compared to the preliminary fiscal forecasts. This is owing to the additional capital expenditure arising from the capital investment package and is offset partially by additional tax receipts expected (consistent with the tax revenue increase). Net core Crown debt is now forecast to be 21.5% of GDP in 2021/22.

The fiscal forecasts include an updated nominal GDP track as a result of Statistics NZ 21 November annual national accounts release. Nominal GDP is $3.3 billion and $4.2 billion higher in the March 2018 and 2019 years. This was too late to be included in the final economic forecasts.

A Treasury Report discussing the final fiscal forecasts in more detail will be sent to your office later this week. Any questions please contact myself or Jayne Winfield.

Kind regards
Catherine

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**Catherine Manning | Senior Government Reporting Accountant | Te Tai Ōhanga – The Treasury**
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Visit us online at https://treasury.govt.nz/ and follow us on Twitter, LinkedIn and Instagram

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# Treasury Report: Half Year Economic and Fiscal Update 2019 Final Fiscal Forecasts

| | | | |
|---|---|---|---|
| **Date:** | 28 November 2019 | **Report No:** | T2019/3832 |
| | | **File Number:** | BM-1-2-3-2019 |

## Action sought

| | Action sought | Deadline |
|---|---|---|
| Minister of Finance<br>(Hon Grant Robertson) | **Note** the Treasury's 2019 Half Year Update final fiscal forecasts.<br>**Refer** this report to the Associate Ministers of Finance | 11 December 2019 |

## Contact for telephone discussion (if required)

| Name | Position | Telephone | | 1st Contact |
|---|---|---|---|---|
| Catherine Manning | Senior Government Reporting Accountant, Fiscal Reporting | s9(2)(k) | n/a<br>(mob) | ✓ |
| Jayne Winfield | Manager,<br>Fiscal Reporting | | s9(2)(g)(ii) | |

## Minister's Office actions (if required)

**Return** the signed report to Treasury.

If agreed, **refer** a copy of this report to the Associate Ministers of Finance.

Note any feedback on the quality of the report

**Enclosure**: No

# Treasury Report: Half Year Economic and Fiscal Update 2019 Final Fiscal Forecasts

## Executive Summary

This report provides a summary of the Treasury's final fiscal forecasts (2019/20 – 2023/24) in for inclusion in the *2019 Half Year Economic and Fiscal Update* (*Half Year Update*). The fiscal forecasts completed on 25 November capture the final economic forecasts (completed on 12 November) and other significant information that has become available since completing the 2019 *Budget Economic and Fiscal Update (Budget Update)* forecasts. Since the preliminary fiscal forecasts the most significant change is the decision around delivering a capital investment package to be announced in the 2020 Budget Policy Statement which is now included in these forecasts. This has had a positive impact on core Crown tax revenue, while residual cash deficits and net core Crown debt have increased as a result.

At the *Budget Update* in the near-term we expected that OBEGAL surpluses would narrow and net core Crown debt would rise. This was a result of tax revenue growth remaining relatively flat, while core Crown expenses growth rose, reflecting the impact of past spending decisions. As with the preliminary fiscal forecast, the final fiscal forecasts follow a similar trend as the *Budget Update*, however the softer forecasts for economic growth, a stronger wage outlook and a lower interest rate track have meant the expected drop in OBEGAL from 2018/19 to 2019/20 is greater than previously expected, with a deficit of $0.9 billion now forecast for the 2019/20 fiscal year. In the near-term, the stronger starting position of net core Crown debt arising from the 30 June 2019 results has somewhat softened the impact from the weaker fiscal outlook.

The economic conditions mentioned above are expected to continue across the rest of the forecast period. As a result, tax revenue forecasts have been revised down, benefit expenses are now expected to be higher and the cost of future ACC claims has increased. In addition to the new capital investment package, there have been increases in some items that are managed outside of Budget allowances that have adversely influenced the fiscal outlook (e.g. s9(2)(j) on-sold properties).

**Table 1** – Summary of key fiscal indicators

| Year ended 30 June | Actual | | Forecast | | | |
|---|---|---|---|---|---|---|
| | 2018/19 | 2019/20 | 2020/21 | 2021/22 | 2022/23 | 2023/24 |
| **$ billion** | | | | | | |
| Total Crown OBEGAL | 7.3 | (0.9) | 0.1 | 1.8 | 4.1 | 5.9 |
| Core Crown residual cash | (0.7) | (5.2) | (8.0) | (5.6) | (2.2) | 0.9 |
| Net core Crown debt | 57.7 | 62.5 | 70.6 | 76.1 | 77.7 | 76.3 |
| Total Crown operating balance | 0.3 | 0.4 | 3.6 | 5.8 | 8.5 | 10.9 |
| **% of GDP** | | | | | | |
| Total Crown OBEGAL | 2.4% | (0.3%) | 0.0% | 0.5% | 1.1% | 1.5% |
| Core Crown residual cash | (0.2%) | (1.6%) | (2.4%) | (1.6%) | (0.6%) | 0.2% |
| Net core Crown debt | 19.0% | 19.6% | 21.0% | 21.5% | 20.9% | 19.6% |
| Total Crown operating balance | 0.1% | 0.1% | 1.1% | 1.6% | 2.3% | 2.8% |

Overall, the fiscal outlook is weaker than at the *Budget Update.* An OBEGAL deficit is expected in the current year before returning to a surplus in 2020/21 and reaching $5.9 billion in 2023/24. Residual cash deficits are expected up until 2022/23 before returning to a surplus in the last year of the forecast. Net core Crown debt is expected to slowly rise, peaking at 21.5% of GDP in 2021/22, before falling to 19.6% at the end of the forecast period.

s9(2)(f)(iv)

**Recommended Action**

We recommend that you:

a. **note** the Treasury's 2019 *Half Year Update* final fiscal forecasts

b. **note** that overall the fiscal outlook is weaker than that at the *Budget Update*

c. **note** that you will be receiving the *Half Year Update* chapters on Monday 2 December 2019

d. **refer** this report to:

- Hon Dr David Clark, Associate Minister of Finance
  *Refer/not referred*
- Hon David Parker, Associate Minister of Finance
  *Refer/not referred*
- Hon Shane Jones, Associate Minister of Finance
  *Refer/not referred*
- Hon James Shaw, Associate Minister of Finance
  *Refer/not referred.*



Jayne Winfield
**Manager, Fiscal Reporting**

Hon Grant Robertson
**Minister of Finance**

# Treasury Report: Half Year Economic and Fiscal Update 2019 Final Fiscal Forecasts

## Purpose of Report

1. This report outlines the final fiscal forecasts (for the five years 2019/20 to 2023/24) completed on 25 November 2019 and outlines the key risks and assumptions underpinning these forecast. The report is broken into the following sections:

- Final Fiscal forecast;
- Changes since the preliminary fiscal forecasts;
- Changes since the *Budget Update*;
- Summary of Key Risks; and
- Summary of Key Fiscal Assumptions

## Final Fiscal Forecasts

2. The table below sets out the key fiscal indicators for the *Half Year Update* fiscal forecasts:

**Table 2** – Key fiscal indicators

| Year ended 30 June | 2019 Actual | 2020 Forecast | 2021 Forecast | 2022 Forecast | 2023 Forecast | 2024 Forecast |
|---|---|---|---|---|---|---|
| **$ billion** | | | | | | |
| Core Crown tax revenue | 86.5 | 88.7 | 94.3 | 99.2 | 104.8 | 110.5 |
| Core Crown expenses | 87.0 | 93.8 | 98.8 | 102.0 | 106.3 | 109.2 |
| Total Crown OBEGAL | 7.3 | (0.9) | 0.1 | 1.8 | 4.1 | 5.9 |
| Core Crown residual cash | (0.7) | (5.2) | (8.0) | (5.6) | (2.2) | 0.9 |
| Net core Crown debt | 57.7 | 62.5 | 70.6 | 76.1 | 77.7 | 76.3 |
| Total borrowings | 110.2 | 122.2 | 126.9 | 137.6 | 138.8 | 145.3 |
| Total Crown operating balance | 0.3 | 0.4 | 3.6 | 5.8 | 8.5 | 10.9 |
| Net worth attributable to the Crown | 139.8 | 139.6 | 143.4 | 149.4 | 158.1 | 169.2 |
| **% of GDP** | | | | | | |
| Core Crown tax revenue | 28.4% | 27.7% | 28.0% | 28.0% | 28.2% | 28.4% |
| Core Crown expenses | 28.6% | 29.3% | 29.4% | 28.8% | 28.6% | 28.1% |
| Total Crown OBEGAL | 2.4% | (0.3%) | 0.0% | 0.5% | 1.1% | 1.5% |
| Core Crown residual cash | (0.2%) | (1.6%) | (2.4%) | (1.6%) | (0.6%) | 0.2% |
| Net core Crown debt | 19.0% | 19.6% | 21.0% | 21.5% | 20.9% | 19.6% |
| Total borrowings | 36.2% | 38.2% | 37.7% | 38.9% | 37.3% | 37.3% |
| Total Crown operating balance | 0.1% | 0.1% | 1.1% | 1.6% | 2.3% | 2.8% |
| Net worth attributable to the Crown | 45.9% | 43.7% | 42.6% | 42.2% | 42.5% | 43.5% |

***GDP revisions – scaled GDP***

3. The fiscal forecasts include an updated nominal GDP track as a result of Statistics NZ 21 November annual national accounts release. Nominal GDP is $3.3 billion and $4.2 billion higher in the March 2018 and 2019 years. As this release was published after the economic forecasts were finalised, this was too late to be included in the final economic forecasts but has been incorporated into the fiscal forecasts ratios in line with best practice.

***Accounting standard changes resulting in restatements***

4. Two new accounting standards - PBE IPSAS 39: *Employee Benefits* and PBE IPSAS 35: *Consolidated Financial Statements* have come into effect for the Crown from 1 July 2019. As a result of these changes there is a requirement to restate comparative figures in the Crown's financial statements, both for actuals and forecasts. For the *Half Year Update* this means that the June 2019 Actuals and the Previous Budget comparators have been restated in a number of areas, resulting in differences from the previously published documents.

5. Refer to Annex One for a table showing a reconciliation between previously published documents and the restated amounts shown in the *Half Year Update* for the key fiscal indicators impacted.

## Changes Since the Preliminary Fiscal Forecasts

6. Overall, when compared to the preliminary fiscal forecasts, OBEGAL has improved by $2.7 billion across the forecast, worsening in the current year, but improving in all other years. In 2020/21 we had previously forecast a deficit of $646 million but we are now forecasting a surplus of $57 million. This improvement is primarily owing to an improved tax and a change in ACC forecasts due to updated discount rate information changing the ACC valuation.

7. The capital investment package is the main driver for the changes since the preliminary fiscal forecasts. This has increased capital expenditure, which is now expected to be $49.9 billion, an increase of $8.7 billion. Core Crown tax is forecast to be lower in the current year by $0.5 billion before increasing in the outyears resulting in a $2.6 billion improvement since the preliminary fiscal forecasts. This improvement in the tax forecasts is largely a result of the inclusion of the capital investment package and a higher interest rate track.

8. Since the preliminary fiscal forecasts, the valuation of the Government Superannuation Fund (GSF) retirement liability has been updated. In addition to the new valuation, the GSF liability is now required to be presented in accordance with an updated accounting standard. While the new accounting standard did not change the Crown's net liability it does change where some of the movements in the liability are recorded in the accounts. A portion of the movement which previously was recorded against pension expenses is now being recorded against finance costs. This change has resulted in a minor increase in overall finance costs each year.

## Changes since the Budget Update

9. The *Budget Update* was published on 30 May 2019. Since then, there have been a number of changes that have impacted the fiscal outlook. Table 3 summarises the changes in the key fiscal indicators since the *Budget Update*.

**Table 3** – Key fiscal indicators compared to the *Budget Update*

| Year ended 30 June | | Actual | | | Forecast | | |
|---|---|---|---|---|---|---|---|
| **$ billion** | | **2018/19** | **2019/20** | **2020/21** | **2021/22** | **2022/23** | **2023/24** |
| OBEGAL - *Half Year Update* 2019 | | 7.3 | (0.9) | 0.1 | 1.8 | 4.1 | 5.9 |
| OBEGAL - *Budget Update* 2019 | | | 1.3 | 2.1 | 4.7 | 6.1 | .. |
| | Total Change | | (2.2) | (2.0) | (2.9) | (2.0) | |
| Residual Cash - *Half Year Update* 2019 | | (0.7) | (5.2) | (8.0) | (5.6) | (2.2) | 0.9 |
| Residual Cash - *Budget Update* 2019 | | | (4.2) | (4.3) | (0.6) | 1.2 | .. |
| | Total Change | | (1.0) | (3.7) | (5.0) | (3.4) | |
| Net Debt - *Half Year Update* 2019 | | 57.7 | 62.5 | 70.6 | 76.1 | 77.7 | 76.3 |
| Net Debt - *Budget Update* 2019 | | | 64.7 | 69.2 | 69.9 | 68.5 | .. |
| | Total Change | | 2.2 | (1.4) | (6.2) | (9.2) | |
| **% of GDP** | | | | | | | |
| Net Debt - *Half Year Update* 2019 | | 19.0 | 19.6 | 21.0 | 21.5 | 20.9 | 19.6 |
| Net Debt - *Budget Update* 2019 | | | 20.4 | 20.7 | 19.9 | 18.7 | .. |

10. Overall, most *key* fiscal indicators are weaker than forecast at the *Budget Update.* On average OBEGAL and residual cash are lower in each year of the forecasts and weaker by around $2.3 billion and $3.3 billion per annum respectively. Net debt is $9.2 billion higher by 2022/23.

11. In summary, the most significant movements are due to economic factors, the new capital investment package, additional costs from items managed outside of Budget allowances and weaker forecast results from Crown entities. Tables 5 and 6 provide a more detailed breakdown of the movements in OBEGAL and net core Crown debt since the *Budget Update.*

### *Weaker economic factors have reduced tax revenue growth*

12. Core Crown tax revenue is forecast to be cumulatively $3.1 billion lower than the *Budget Update* over the four-year[1] period up to 2022/23 mainly owing to a weaker economic outlook. Nominal GDP forecasts reduced the tax revenue forecast by $4.0 billion with changes to interest rate forecasts reducing the forecasts of RWT on interest by $2.1 billion. Partially offsetting these effects, the underlying strength (relative to the *Budget Update*) in tax revenue in the year to June 2019 added $3.0 billion to the forecast.

13. Forecasts for RWT and GST have decreased while revenue from source deductions, other persons and corporate tax have increased. Table 4 below summarises the movements by tax type since the *Budget Update.*

14. Tax receipts follow a similar trend to tax revenue and are cumulatively lower by $3.5 billion compared to the *Budget Update*.

[1] The 2023/24 year was not forecast in the *Budget Update.*

**Table 4** – Reconciliation of the change in core Crown tax revenue

| Year ending 30 June<br>$billions | 2020<br>Forecast | 2021<br>Forecast | 2022<br>Forecast | 2023<br>Forecast | Total<br>Change |
|---|---|---|---|---|---|
| **Movement in core Crown tax owing to:** | | | | | |
| Source deductions | 0.2 | 0.1 | 0.3 | 0.4 | 1.0 |
| Other persons tax | (0.1) | 0.3 | 0.2 | 0.2 | 0.6 |
| Corporate tax | (0.1) | - | 0.2 | 0.2 | 0.3 |
| Goods and services tax (GST) | (0.5) | (0.7) | (0.6) | (0.6) | (2.4) |
| Resident withholding tax (RWT) on interest | (0.2) | (0.6) | (1.0) | (1.1) | (2.9) |
| Other taxes | 0.2 | 0.1 | (0.1) | 0.1 | 0.3 |
| **Total movement in core Crown tax revenue** | **(0.5)** | **(0.8)** | **(1.0)** | **(0.8)** | **(3.1)** |
| *Plus Budget's* tax base | 89.2 | 95.1 | 100.2 | 105.6 | |
| **Core Crown tax revenue at *Half Year Update*** | **88.7** | **94.3** | **99.2** | **104.8** | |
| **as a % of GDP** | **27.7%** | **28.0%** | **28.0%** | **28.2%** | |

***At the same time, higher wage growth and weaker economic outlook increase benefits***

15. Social assistance expenses have increased by $2.2 billion over the forecast since the *Budget Update*. This increase mainly relates to New Zealand Superannuation payments, Jobseeker Support and Emergency Benefits and the Supported Living Payment. The increase reflects higher recipient numbers and a higher wage growth track that contributed around $1.6 billion and $0.7 billion respectively to the overall increase.

16. This higher wage growth track compared to the *Budget Update* has impacted on most benefit types. The upward revision to the expected wage level has the largest impact on New Zealand Superannuation, owing to the large volume of people receiving the payment.

17. Actual recipient numbers for the Jobseeker Support and Emergency Benefit (such as emergency housing) and the Supported Living Payment are tracking above what was expected at the *Budget Update*. In addition, the softening in economic conditions in the near-term have also resulted in an expected lift in recipient numbers. Overall, the increase in recipient numbers from these two benefit types have increased expenses by around $1.0 billion over the forecast period.

***Lower interest rates have also resulted in increased costs for ACC***

18. ACC is expecting higher insurance claims costs then previously forecast. The ACC liability and insurance costs are particularly sensitive to discount rates (used to value the lifetime cost of all existing and forecast claims in today's dollars). ACC's updated forecast is based on the 30 June 2019 valuation and has been updated for 31 October 2019 discount rates. Between the *Budget Update* and 31 October discount rates have fallen.

19. As a result of the lower discount rates, the lifetime cost of forecast claims are now higher in present value terms than the same claims forecast at *Budget Update* (based on February discount rates). The increase in forecast claims costs are partially offset by the increase in levy revenue forecast based on the current funding policy, resulting in a total reduction in OBEGAL of $1.3 billion across the four-year period.

20. The total reduction in OBEGAL from ACC does not flow through to residual cash or net core Crown debt as ACC is outside of the core Crown.

***However, lower interest rates have had a minimal impact on net finance costs***

21. The weaker fiscal outlook has resulted in an increase to net core Crown debt, net finance costs on borrowings are actually expected to be lower across the four-year period compared to the *Budget Update, however this change has been offset by the accounting standard change to GSF expenses*. Overall, net finance costs have increased over the four-year period by $0.3 billion. The level of financial assets held by the Crown are expected to reduce in order to fund the increase in the cash shortfall, which has resulted in a reduction in interest revenue, however this has been more than offset by lower debt servicing costs now forecast due to lower yields on new debt being issued at a lower interest rate. The current low interest rate environment has reduced the yields on new issued bonds, however the coupon rates paid on some of these issued bonds remains unchanged, therefore the cash impact of net finance costs are higher than previously expected.

***There has been an increase in some costs managed outside of Budget allowances***

22. s9(2)(j)

23. Cabinet has agreed to compensate homeowners for the repair costs of eligible on-sold Canterbury properties. The costs from this decision were not managed against Budget allowances, therefore have directly impacted OBEGAL and net core Crown debt (T2019/2916 dated 23 September refers).

***Overall SOE and Crown entity results are weaker***

24. SOE and Crown entity forecast results have come in weaker than forecast at the *Budget Update*. Of these, the largest changes were in relation to ACC (discussed above), DHBs and KiwiRail:

- The DHBs are forecasting deficits across each year of the forecast ($0.2 billion in the current year, increasing by $0.2 billion each year to reach $1.3 billion in 2022/23). These forecast deficits have increased from 2020/21 with an overall increase in the deficits of $1.4 billion since the *Budget Update*.
- Updated forecasts for KiwiRail also show a weaker outlook than previously forecast by $0.7 billion across the forecast period. This is due to higher depreciation expenses now being forecast, owing to the increase in the value of the rail network, from the change in the valuation approach adopted in the 2019 fiscal year.

***Reforecasting by agencies has marginally impacted the fiscal outlook***

25. Some agencies have changed the timing of expenditure (both operating and capital), which overall have had a positive impact on OBEGAL but increased net core Crown debt of $0.1 billion and $0.4 billion respectively in total across the four-year period. These timing changes were mainly relating to spending from the Ministry of Transport, Ministry of Education and the Ministry of Housing and Urban Development.

***The stronger starting position has somewhat softened the impact of the weaker fiscal outlook on net core Crown debt***

26. The results from 30 June 2019 have meant that there is a stronger starting position for net core Crown debt heading into the current fiscal year. As a result, this improvement has partially offset the additional residual cash shortfall expected since the *Budget Update*.

***Assumed uptake of the 'Fixed Price Option' under the Emissions Trading Scheme (ETS) has also improved net core Crown debt***

27. ETS receipts have increased by $2.2 billion across the forecast owing to an expectation that more ETS participants will take up the 'fixed price option' where they can pay the Government $25 for each unit they are liable to surrender to meet their ETS obligations. This has resulted in an improvement in net core Crown debt from the *Budget Update*.

28. Although, the uptake of the Fixed Price Option has improved net core Crown debt it has also increased the Government's obligation under the ETS, which will need to be settled in the future. By the end of the forecast period, it is forecast to reduce net core Crown debt by around 0.6% of GDP.

**Table 5** – Changes to OBEGAL since the *Budget Update*

| Year ending 30 June<br>$billions | 2019/20 | Forecast<br>2020/21 | 2021/22 | 2022/23 | Total change |
|---|---|---|---|---|---|
| **OBEGAL - *Budget Update 2019*** | **1.3** | **2.1** | **4.7** | **6.1** | |
| **Economic factors** | | | | | |
| Core Crown tax - forecasting changes | (0.6) | (0.8) | (1.0) | (0.8) | **(3.2)** |
| Social assistance forecasting changes | (0.3) | (0.5) | (0.6) | (0.8) | **(2.2)** |
| **Other factors** | | | | | |
| Canterbury on-sold property compensation | (0.3) | - | - | - | **(0.3)** |
| Net core Crown finance costs | (0.2) | - | - | (0.1) | **(0.3)** |
| ACC results | (0.7) | (0.3) | (0.4) | 0.1 | **(1.3)** |
| DHB results | 0.1 | (0.3) | (0.5) | (0.7) | **(1.4)** |
| KiwiRail results | (0.1) | (0.2) | (0.2) | (0.2) | **(0.7)** |
| Other changes | (0.1) | 0.1 | (0.2) | 0.5 | **0.3** |
| *Total changes since the Budget Update* | **(2.2)** | **(2.0)** | **(2.9)** | **(2.0)** | **(9.1)** |
| **OBEGAL - *Half Year Update 2019* - Final** | **(0.9)** | **0.1** | **1.8** | **4.1** | |

**Table 6** – Changes to net core Crown debt since the *Budget Update*

| Year ending 30 June<br>$billion | 2019/20 | Forecast<br>2020/21 | 2021/22 | 2022/23 |
|---|---|---|---|---|
| **Net core Crown debt - *Budget Update 2019*** | **64.7** | **69.2** | **69.9** | **68.5** |
| Opening balance | (2.6) | (2.6) | (2.6) | (2.6) |
| **Economic factors** | | | | |
| Core Crown tax receipt forecasts | 0.8 | 1.8 | 2.8 | 3.5 |
| Social assistance forecasting changes | 0.3 | 0.8 | 1.4 | 2.2 |
| **Other Factors** | | | | |
| ETS fixed price option | (0.5) | (1.0) | (1.6) | (2.2) |
| Phasing changes | (0.8) | (0.1) | 0.6 | 0.4 |
| Net finance costs | 0.1 | 0.1 | 0.2 | 0.5 |
| Canterbury on-sold property compensation | 0.2 | 0.2 | 0.3 | 0.3 |
| Change in capital investment | 0.5 | 3.1 | 5.1 | 7.1 |
| Gains and losses | (0.3) | (0.2) | (0.1) | - |
| Other changes | 0.3 | (0.7) | 0.1 | (0.1) |
| **Total changes** | **(2.2)** | **1.4** | **6.2** | **9.2** |
| **Net core Crown debt - *Half Year Update 2019*** | **62.5** | **70.6** | **76.1** | **77.7** |

## Summary of Key Risks

29. Along with the inherent uncertainty regarding forecasts, there are some known risks to the fiscal forecasts:

- The fiscal forecasts do not reflect economic data received after the economic forecasts were finalised on 12 November 2019, with the exception of the GDP revision.
- s9(2)(f)(iv)
- Kāinga Ora have included borrowings in accordance with their existing agreement with the Minister of Finance ('the borrowing protocol'); we are aware that an increase to the approved level of borrowings in this protocol is going to be requested shortly. We have included a specific fiscal risk in the *Half Year Update* regarding this.

## Summary of Key Fiscal Assumptions

30. The fiscal forecasts are based on the final economic forecasts (completed on 12 November 2019), information provided by individual entities coupled with central adjustments made by the Treasury for items which are not captured in individual entity forecasts. Summarised below are some of the key assumptions worth noting that have required some degree of judgement by the Treasury in finalising these fiscal forecasts.

### Consistency of assumptions

31. The final economic forecasts that were completed on 12 November 2019 were provided to agencies whose forecasts are underpinned by key economic indicators to ensure consistency of assumptions. Discount rates and CPI assumptions are also centrally set by the Treasury for use in key asset and liability valuations (e.g. ACC claims liability, GSF liability and student loans valuation).

### Top-down adjustment

32. The top-down adjustment is a central adjustment to expenditure forecasts (both operating and capital) to reflect departments' tendency to use appropriations (upper spending limits) rather than best estimates when preparing their forecasts. The level of the central top-down adjustment is dependent on the quality of forecasts received from departments. Based on our analysis, the central top-down adjustments included in the Half Year Update forecasts are set out in Table 7 and the Budget Update in Table 8.

**Table 7** – Top-down adjustment assumed for the 2019 *Half Year Update*

| $millions | 2019/20 | 2020/21 | 2021/22 | 2022/23 | 2023/24 |
|---|---|---|---|---|---|
| Operating | 1,200 | 925 | 675 | 575 | 575 |
| Capital | 800 | 600 | 400 | 300 | 250 |
| **Total** | **2,000** | **1,525** | **1,075** | **875** | **825** |

**Table 8** - Top-down adjustment assumed for the *2019 Budget Update*

| $millions | 2019/20 | 2020/21 | 2021/22 | 2022/23 |
|---|---|---|---|---|
| Operating | 1,400 | 500 | 500 | 500 |
| Capital | 950 | 550 | 250 | 150 |
| **Total** | **2,350** | **1,050** | **750** | **650** |

33. We have adjusted these amounts since the *Budget Update*, reducing the operating adjustment in the current year, and increasing the adjustment in the outyears. The decrease in the current year is reflective of two things: an increase due to the size of the expense transfers into 2019/20, more than offset by entities' forecasting large underspends in the current year and with some of these moving into the next financial year. The operating top-down adjustment is unchanged since the preliminary fiscal forecasts.

34. The decrease in the current year is reflective of two things, an increase due to the size of the expense transfers, more than offset by MBIE forecasting large underspends in the current year with some of these moving into the next financial year.

35. Generally the top-down adjustment in the current year (2019/20) and the next year are higher than the other years in the forecast period to compensate for expenses being transferred in from previous years. This was the case for both operating and capital, where expense transfers have occurred from 2018/19.

s9(2)(j)

## Annex One – Accounting Standard restatements

| | Forecast June 2020 (per BEFU 19) $m | IPSAS 39 GSF $m | IPSAS 35 NZSF $m | Forecast June 2020 restated (per HYEFU 19) $m | Change $m |
|---|---|---|---|---|---|
| Core Crown revenue | 96,427 | - | (76) | 96,351 | (76) |
| Core Crown expenses | 93,262 | 139 | 2 | 93,403 | 141 |
| OBEGAL | 1,313 | (139) | (78) | 1,096 | (217) |
| Operating Balance | 4,680 | (139) | (3) | 4,538 | (142) |
| Net worth | 140,748 | - | (131) | 140,617 | (131) |

| | Actuals June 2019 (per June FSG) $m | IPSAS 39 GSF $m | IPSAS 35 NZSF $m | Actuals June 2019 restated (per HYEFU 19) $m | Change $m |
|---|---|---|---|---|---|
| Core Crown revenue | 93,625 | - | (151) | 93,474 | (151) |
| Core Crown expenses | 87,022 | 144 | (125) | 87,041 | 19 |
| OBEGAL | 7,508 | (144) | (17) | 7,347 | (161) |
| Operating Balance | (2,274) | 2,615 | (48) | 293 | 2,567 |
| Net worth | 146,313 | - | (141) | 146,172 | (141) |

## Annex Two – Historical Time Series

| June years | 2009 Actual | 2010 Actual | 2011 Actual | 2012 Actual | 2013 Actual | 2014 Actual | 2015 Actual | 2016 Actual | 2017 Actual | 2018 Actual | 2019 Actual | 2020 Forecast | 2021 Forecast | 2022 Forecast | 2023 Forecast | 2024 Forecast |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| $millions | | | | | | | | | | | | | | | | |
| **Revenue and expenses** | | | | | | | | | | | | | | | | |
| Core Crown tax revenue | 54,681 | 50,744 | 51,557 | 55,081 | 58,651 | 61,563 | 66,636 | 70,445 | 75,644 | 80,244 | 86,468 | 88,692 | 94,278 | 99,216 | 104,824 | 110,499 |
| Core Crown revenue | 59,191 | 55,757 | 57,199 | 60,428 | 63,805 | 67,093 | 72,213 | 76,121 | 81,782 | 6,554 | 93,474 | 95,797 | 101,592 | 106,526 | 112,735 | 117,659 |
| Core Crown expenses | 63,711 | 63,554 | 70,099 | 68,939 | 69,962 | 71,174 | 72,363 | 73,929 | 76,339 | 80,576 | 87,041 | 93,776 | 98,765 | 102,012 | 106,261 | 109,233 |
| **Surpluses** | | | | | | | | | | | | | | | | |
| Total Crown OBEGAL | (3,893) | (6,315) | (18,396) | (9,240) | (4,414) | (2,802) | 414 | 1,831 | 4,069 | 5,534 | 7,347 | (943) | 57 | 1,752 | 4,061 | 5,924 |
| Total Crown operating balance | (10,505) | (4,509) | (13,360) | (14,897) | 6,925 | 2,939 | 5,771 | (5,369) | 12,317 | 8,396 | 293 | 422 | 3,561 | 5,755 | 8,496 | 10,876 |
| **Cash position** | | | | | | | | | | | | | | | | |
| Core Crown residual cash | (8,639) | (9,000) | (13,343) | (10,644) | (5,742) | (4,109) | (1,827) | (1,322) | 2,574 | 1,346 | (710) | (5,154) | (7,973) | (5,550) | (2,231) | 911 |
| **Debt** | | | | | | | | | | | | | | | | |
| Gross debt[1] | 43,356 | 53,591 | 72,420 | 79,635 | 77,984 | 81,956 | 86,125 | 86,928 | 87,141 | 88,053 | 84,449 | 89,575 | 91,390 | 99,560 | 98,836 | 102,642 |
| Gross debt incl RB settlement cash and bank bills | 50,973 | 58,891 | 77,290 | 84,168 | 84,286 | 88,468 | 93,156 | 93,283 | 92,620 | 95,437 | 90,930 | 96,498 | 98,313 | 106,483 | 105,759 | 109,565 |
| Net core Crown debt (incl NZS Fund)[2] | 5,633 | 12,549 | 23,969 | 33,475 | 34,428 | 34,174 | 30,862 | 32,102 | 23,619 | 19,460 | 14,060 | 14,590 | 17,632 | 17,117 | 12,274 | 3,939 |
| Net core Crown debt[2] | 17,119 | 26,738 | 40,128 | 50,671 | 55,835 | 59,931 | 60,631 | 61,880 | 59,480 | 57,495 | 57,736 | 62,526 | 70,639 | 76,071 | 77,681 | 76,335 |
| Total borrowings | 61,953 | 69,733 | 90,245 | 100,534 | 100,087 | 103,419 | 112,580 | 113,956 | 111,806 | 115,652 | 110,248 | 122,161 | 126,917 | 137,643 | 138,760 | 145,324 |
| **Net worth** | | | | | | | | | | | | | | | | |
| Total Crown net worth | 99,515 | 94,988 | 80,887 | 59,780 | 70,011 | 80,697 | 98,236 | 95,521 | 116,472 | 135,637 | 146,172 | 145,786 | 149,420 | 155,264 | 163,817 | 174,879 |
| Total net worth attributable to the Crown | 99,068 | 94,586 | 80,579 | 59,348 | 68,071 | 75,486 | 86,454 | 89,366 | 110,532 | 129,644 | 139,782 | 139,620 | 143,402 | 149,387 | 158,057 | 169,156 |
| **Nominal expenditure GDP (revised actuals)** | 189,525 | 196,761 | 205,852 | 215,183 | 218,827 | 236,732 | 244,997 | 257,602 | 274,738 | 293,075 | 304,357 | 319,804 | 336,400 | 354,114 | 371,532 | 389,192 |
| % GDP | | | | | | | | | | | | | | | | |
| **Revenue and expenses** | | | | | | | | | | | | | | | | |
| Core Crown tax revenue | 28.9 | 25.8 | 25.0 | 25.6 | 26.8 | 26.0 | 27.2 | 27.3 | 27.5 | 27.4 | 28.4 | 27.7 | 28.0 | 28.0 | 28.2 | 28.4 |
| Core Crown revenue | 31.2 | 28.3 | 27.8 | 28.1 | 29.2 | 28.3 | 29.5 | 29.5 | 29.8 | 2.2 | 30.7 | 30.0 | 30.2 | 30.1 | 30.3 | 30.2 |
| Core Crown expenses | 33.6 | 32.3 | 34.1 | 32.0 | 32.0 | 30.1 | 29.5 | 28.7 | 27.8 | 27.5 | 28.6 | 29.3 | 29.4 | 28.8 | 28.6 | 28.1 |
| **Surpluses** | | | | | | | | | | | | | | | | |
| Total Crown OBEGAL | (2.1) | (3.2) | (8.9) | (4.3) | (2.0) | (1.2) | 0.2 | 0.7 | 1.5 | 1.9 | 2.4 | (0.3) | 0.0 | 0.5 | 1.1 | 1.5 |
| Total Crown operating balance | (5.5) | (2.3) | (6.5) | (6.9) | 3.2 | 1.2 | 2.4 | (2.1) | 4.5 | 2.9 | 0.1 | 0.1 | 1.1 | 1.6 | 2.3 | 2.8 |
| **Cash position** | | | | | | | | | | | | | | | | |
| Core Crown residual cash | (4.6) | (4.6) | (6.5) | (4.9) | (2.6) | (1.7) | (0.7) | (0.5) | 0.9 | 0.5 | (0.2) | (1.6) | (2.4) | (1.6) | (0.6) | 0.2 |
| **Debt** | | | | | | | | | | | | | | | | |
| Gross debt[1] | 22.9 | 27.2 | 35.2 | 37.0 | 35.6 | 34.6 | 35.2 | 33.7 | 31.7 | 30.0 | 27.7 | 28.0 | 27.2 | 28.1 | 26.6 | 26.4 |
| Gross debt incl RB settlement cash and bank bills | 26.9 | 29.9 | 37.5 | 39.1 | 38.5 | 37.4 | 38.0 | 36.2 | 33.7 | 32.6 | 29.9 | 30.2 | 29.2 | 30.1 | 28.5 | 28.2 |
| Net core Crown debt (incl NZS Fund)[2] | 3.0 | 6.4 | 11.6 | 15.6 | 15.7 | 14.4 | 12.6 | 12.5 | 8.6 | 6.6 | 4.6 | 4.6 | 5.2 | 4.8 | 3.3 | 1.0 |
| Net core Crown debt[2] | 9.0 | 13.6 | 19.5 | 23.5 | 25.5 | 25.3 | 24.7 | 24.0 | 21.6 | 19.6 | 19.0 | 19.6 | 21.0 | 21.5 | 20.9 | 19.6 |
| Total borrowings | 32.7 | 35.4 | 43.8 | 46.7 | 45.7 | 43.7 | 46.0 | 44.2 | 40.7 | 39.5 | 36.2 | 38.2 | 37.7 | 38.9 | 37.3 | 37.3 |
| **Net worth** | | | | | | | | | | | | | | | | |
| Total Crown net worth | 52.5 | 48.3 | 39.3 | 27.8 | 32.0 | 34.1 | 40.1 | 37.1 | 42.4 | 46.3 | 48.0 | 45.6 | 44.4 | 43.8 | 44.1 | 44.9 |
| Total net worth attributable to the Crown | 52.3 | 48.1 | 39.1 | 27.6 | 31.1 | 31.9 | 35.3 | 34.7 | 40.2 | 44.2 | 45.9 | 43.7 | 42.6 | 42.2 | 42.5 | 43.5 |

1 Excludes Reserve Bank settlement cash and bank bills.
2 Excludes advances.

**From:** Jess Jenkins [TSY]
**Sent:** Thursday, 28 November 2019 5:04 PM
**To:** ^Parliament: Talei Pasikale
**Cc:** Struan Little [TSY]; Paul Helm [TSY]; Alex Harrington [TSY]; Jayne Winfield [TSY]
**Subject:** SFRs Update

[IN-CONFIDENCE]

Hi Talei,

Following our conversation on Tuesday, The MoF's feedback on the SFRs chapter has been integrated, and the final (but pre-proof reader) version will come across tomorrow with the other chapters.
Hopefully the office will also be happier with the consistency and clarity of the chapter this time round. For now, I'd like to flag with you some specific changes of note in response to MoF's questions:

- The following risks have been **removed**:
  - s9(2)(f)(iv)
  - ***Implementing a State Sector Living Wage***

- The following **new risks** have been included, with materiality and wording agreed with agencies and Vote Teams:
  - ***Decommissioning of the Tui Oil Field (New) (Cost Pressure)***

    The Tui oil field operator, Tamarind, entered voluntary administration on 11 November 2019. It is likely that if Tamarind is liquidated, there will be no funds available to meet its obligations to fully decommission the oil field. The Crown may be required to meet the full costs of decommissioning the Tui Field, which are estimated at $US100 million or more. A portion of decommissioning costs could materialise as early as 2020, with the remaining costs of decommissioning the field expected to materialise over the next two to five years.

  - ***Infrastructure Funding and Financing to Improve Housing Affordability (New) (Policy Change)***

    The Infrastructure Funding and Financing Bill 2019 (the Bill) is expected to be introduced into the House of Representatives by the end of 2019. The purpose of the Bill is to enable a multi-year levy to be imposed on beneficiaries of infrastructure projects by Order in Council as part of the Infrastructure Levy Model. Under the Model the Levy will be collected by a Special Purpose Vehicle to service finance raised to cover the costs of the infrastructure. The fiscal forecasts make no provision for use of the Model. The impact of the Model will depend on the passing of the Bill into law, the final design of the Model, and the nature and extent of projects funded by the Model.

- At MoF's request, the wording of the following risks have been **amended**:
  - ***Quarterly Employment Survey Redevelopment (New)***

    Statistics NZ is redeveloping the Quarterly Employment Survey, which will change the way average wages are calculated from the current approach. There are several ways in which the new survey will differ, and the exact impact of this is uncertain. Current estimates indicate redevelopment would be likely to increase costs to the Crown by roughly $135 million per percentage point increase, per annum, from 2021/22 at the earliest.

- ***2023 Census Costs (Changed)***

  The next Census is due to take place in 2023. Statistics NZ has indicated that the funding required to deliver the Census will be sought through Budget 2020. This initiative will be supported by a detailed business case in late 2019, followed by an implementation business case for the preferred option in early 2020.

- ***Possible Responses to the 2020 Referenda on Cannabis Law Reform and End of Life Choice (Changed)***[1]

  The Government has committed to holding referenda on legalising the use of cannabis and end of life choice at the 2020 general election. The cost of conducting the referendums has been provided in the forecasts. However, there could be associated impacts on the Government's operating balance should current legal frameworks change as an outcome of the referenda.

-

- The **School Transport Risk** has been confirmed by the Vote Team as material, and the various components of the risk have been clarified further. You'll note this includes both Daily Bus Services, and Specialised School Transport Assistance.

  - ***School Transport Services (New)***

    The budget for School Transport Services for 2019/20 is $200 million. The cost of Daily Bus Services makes up over half of this allocation, and the Ministry of Education will be going to market shortly for the tender of provision of these services which could impact the contract total. In addition, the combination of a demand increase by 14% in Specialised School Transport Assistance and indexation increases will likely lead to further cost increases. To the extent that these pressures cannot be managed within existing baselines, additional funding is likely to be required.

Please let me know if there are any further comments on any of the above, or in relation to the chapter tomorrow.

Thanks!

Jess

TE TAI ŌHANGA
THE TREASURY

**Jessica Jenkins** (she/her) **| Graduate Analyst, Budget Management | Te Tai Ōhanga – The Treasury**
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[1] This risk previously related to only the referendum on cannabis law reform.

**From:** Catherine Manning [TSY]
**Sent:** Thursday, 5 December 2019 5:05 PM
**To:** 'Talei Pasikale'
**Cc:** Jayne Winfield [TSY]
**Subject:** RE: Treasury Report_ Half Year Economic and Fiscal Update 2019 Final Fiscal Forecasts.DOC

[SEEMAIL][SENSITIVE]

Hi Talei

MBIE have come back to us and said that their forecast underspends relate to PGF and grants expenditure:

- $0.5b of PGF is appropriated for 19/20 but is expected in 20/21 instead.
- $0.4b of other expenditure of which most are grants. MBIE have said they expect that the main drivers will be science related appropriations such as the Endeavour Fund, Catalyst Fund and National Science Challenges which they are forecasting to underspend in the 2019/20 year.

MBIE have said they look at their 2018/19 actual underspends to come up with these forecast underspends.

I'm not in the office tomorrow (I don't work Fridays), but if you have further questions, please contact Jayne.

Kind regards
Catherine

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**From:** Talei Pasikale <Talei.Pasikale@parliament.govt.nz>
**Sent:** Thursday, 5 December 2019 11:48 AM
**To:** Catherine Manning [TSY] <Catherine.Manning@treasury.govt.nz>
**Cc:** Jayne Winfield [TSY] <Jayne.Winfield@treasury.govt.nz>
**Subject:** RE: Treasury Report_ Half Year Economic and Fiscal Update 2019 Final Fiscal Forecasts.DOC

Kia ora Catherine

Further to Budget Matters discussion on Tuesday afternoon, does Treasury have any more details on the MBIE underspends (re para 34)?

Thanks, Talei

**Talei Pasikale**, Economic Advisor | **Office of Hon Grant Robertson** s9(2)(k)

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**From:** Catherine Manning [TSY] [mailto:Catherine.Manning@treasury.govt.nz]
**Sent:** Tuesday, 3 December 2019 12:28 PM
**To:** Talei Pasikale <Talei.Pasikale@parliament.govt.nz>
**Cc:** Jayne Winfield [TSY] <Jayne.Winfield@treasury.govt.nz>
**Subject:** Treasury Report_ Half Year Economic and Fiscal Update 2019 Final Fiscal Forecasts.DOC

[SEEMAIL][SENSITIVE]

Hi Talei – copy of the TR attached

Kind regards
Catherine

TE TAI ŌHANGA
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**From:** Alex Harrington [TSY]
**Sent:** Friday, 6 December 2019 3:14 PM
**To:** ^Parliament: Talei Pasikale
**Cc:** @Budget Team; Struan Little [TSY]; Paul Helm [TSY]; @OE analysts [TSY]; Avril Gillan [TSY]; ^Parliament: Sebastian Doelle; ^Parliament: Daniel Cruden
**Subject:** Budget Matters Agenda (10 December 2019)
**Attachments:** 4219282_Budget Matters Agenda (10 December 2019).DOCX

[IN-CONFIDENCE]

Kia ora Talei

Please find attached the agenda for Budget Matters on Tuesday 10 December. There are no further accompanying papers or attachments.

Ngā mihi
Alex

TE TAI ŌHANGA
THE TREASURY

**Alex Harrington** (he/him) **| Manager, Budget Management | Te Tai Ōhanga – The Treasury**
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# BUDGET MATTERS

**Tuesday 10 December 2019**
**4:00 – 4:45 pm in the Beehive, 7.6 EW**

## A G E N D A

**1. Read-out from Budget Ministers meeting**

Objective: To discuss the Budget Ministers meeting on Monday 9 December and confirm any further work or next steps

Attachments: None

**2. HYEFU/BPS preparation**

Objective: An opportunity to discuss anything further that is needed ahead of the HYEFU/BPS being released at 1pm on Wednesday 11 December

Attachments: None

**3. Implications of the proposed amendments to the Pay Equity Bill**

Objective: To give you a short oral briefing on the implications of the proposed amendments on the objectives of the Bill, legislative timeline, and state sector pay equity bargaining

Attachments: None. A joint Treasury/SSC report will follow later in the week.

***Indicative forward agenda for the following Budget Matters***

*No more Budget Matters meetings scheduled until 2020.*

**To:** ^Parliament: Talei Pasikale
**Subject:** New Risks since MoF Draft for BMatters discussion

Hi Talei,

As discussed, the following risks are being discussed for inclusion in the chapter

### *Petroleum Decommissioning*

Future potential fiscal impacts for the Crown are likely to include royalties and taxes that are to be refunded to the companies. The effects will depend on when Participants decide to commence the decommissioning process. Any tax rebates and royalty rebates will adversely impact the Crown's fiscal position (as these rebates are not forecast currently). The rebates are based on when decommissioning expenditure is incurred by the entities who have the current producing permit and licence. Based on current market prices and operator's current decommissioning plans/time line the anticipated effect of this over the next 5 years will be a reduction n in royalty revenue and an increase expenditure relating to the rebate of past royalties and taxes paid and based on when decommissioning expenditure is incurred.

**Infrastructure Funding and Financing to improve housing affordability - being run by vote team**
Ministers are considering a new model to provide financial support to unlock local government financing constrains and thereby enable a more responsive supply of infrastructure to improve housing affordability. An infrastructure levy would pass the cost of financing to the beneficiaries whenever a development under the model occurs. Enabling legislation would be required. The fiscal forecasts make no provision for this model, the impact of which would depend on its final design, and the nature and extent of projects approved under the model.

Jess

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