BUDGET
2022

BUDGET POLICY STATEMENT

15 December 2021

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Te Kāwanatanga o Aotearoa
New Zealand Government

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FOREWORD

Budget 2022 is being written in the continuing shadow of the COVID-19 pandemic. Around the world as countries seek to open up, a fourth wave of the virus is taking hold and the Omicron variant has emerged. In New Zealand we are managing our transition to a new framework to minimise the effects of COVID-19 and protect our population as vaccination rates increase and we seek to reduce restrictions.

The Government's strategy has proven to be a successful approach to managing the pandemic. We have had one of the lowest mortality rates in the world. At the same time the economy has been resilient with strong growth and low unemployment, although particular sectors and regions have been impacted by restrictions.

Since the pandemic began the Government has provided an unprecedented level of economic support to keep New Zealanders connected to their jobs. Both the Wage Subsidy Scheme and the Resurgence Support Payment have provided critical support to employers and workers. As both border measures and domestic restrictions evolve, economic support measures will become targeted to those most in need and tailored to their circumstances.

Budget 2022 will continue to make progress towards the goals the Government set at the start of the current Parliamentary term. These are:

1. Continuing to keep New Zealand safe from COVID-19
2. Accelerating the recovery and rebuild from the impacts of COVID-19
3. Laying the foundations for the future, including addressing key issues such as our climate change response, housing affordability and child poverty.

Within these overarching goals, and as part of our wellbeing approach, the Government has identified two policy areas that will be a particular focus for Budget 2022: embedding the health reforms; and making progress towards our emissions reduction goals.

COVID-19 has highlighted how vital a joined-up and prepared health system is for protecting New Zealanders. Under the reforms announced earlier this year, district health boards will be replaced with one national organisation (Health New Zealand), a new Māori Health Authority will be established and a dedicated Public Health Agency will be created.

Through Budget 2022 the Government will make significant further investments in establishing these new entities on a sustainable footing and beginning the delivery of the health system shifts envisaged through reform.

To make progress in addressing climate change from a Government perspective, a new approach to the Budget process is required as we make significant investments across multiple budgets. To drive this, the Government is establishing a Climate Emergency Response Fund (CERF) which will be allocated towards initiatives that help us meet our climate change objectives.

For Budget 2022, the CERF will focus on initiatives and programmes aimed at delivering the emissions reductions outlined in the Government's first Emissions Reduction Plan.

The fiscal strategy continues our balanced approach by managing debt prudently and reducing the deficits caused by COVID-19, while growing the economy sustainably and investing in important public services like health and education. Net core Crown debt and the OBEGAL (operating balance before gains and losses) are both stronger than has been previously forecast in total across the four years to 2024/25, reflective of a stronger economy and a balanced approach to investment by the Government.

The ongoing uncertainty around COVID-19 and volatility in the global economy mean the current short-term intentions and long-term objectives remain fit for purpose, so they have therefore not changed since the *2021 Fiscal Strategy Report*.

The Government is committed to setting new fiscal targets at Budget 2022 with the expectation that the global economic outlook and conditions will stabilise.

HON GRANT ROBERTSON
Minister of Finance

15 December 2021

NEW ZEALAND'S WELLBEING OUTLOOK

The Labour Government is committed to achieving its policy goals using a wellbeing approach. This aims to improve New Zealanders' living standards by taking an intergenerational view to tackling long-term challenges. It also means looking beyond traditional measures of success, such as gross domestic product (GDP), and towards broader indicators of wellbeing.

The Treasury's **Living Standards Framework** recognises that human, environmental, social, and physical and financial capital needs to be developed and sustained in order to achieve wellbeing. A complementary framework is being developed to sit alongside, **He Ara Waiora**, which draws on a te ao Māori perspective. Each framework provides a distinct contribution to understanding New Zealand's wellbeing outlook.

These frameworks invite us to consider the distributional impacts of policies on different groups and the environment. This is achieved by working in the spirit of kotahitanga (unity) with those most affected by policy changes, and by considering the intergenerational impacts of the choices we make to support our tiakitanga (stewardship) and mana whanake (intergenerational prosperity).

LIVING STANDARDS FRAMEWORK: THE FOUR CAPITALS

Budget 2022 is being developed based on the 2018 version of the Living Standards Framework. Future budgets will use the new version of the Living Standards Framework, announced by the Treasury in October 2021. The new version will inform decision-making in future Budgets by better reflecting what matters for child wellbeing, and the different ways in which culture contributes to wellbeing. It is also more compatible with wellbeing as understood in te ao Māori and by Pacific peoples, improving alignment with He Ara Waiora and Pacific wellbeing frameworks such as Fonofale.

HUMAN CAPITAL: OUR PEOPLE AND SKILLS

Human capital includes our skills, knowledge and physical and mental health, which affect areas like employment, income, housing, and social connections.

The Government's ongoing response to COVID-19 has played a significant role in protecting New Zealanders' lives and livelihoods. The continued analysis of economic and wellbeing data gathered since the start of the pandemic shows the success of New Zealand's approach to mitigating the impacts of COVID-19 relative to those of other countries.

Labour market

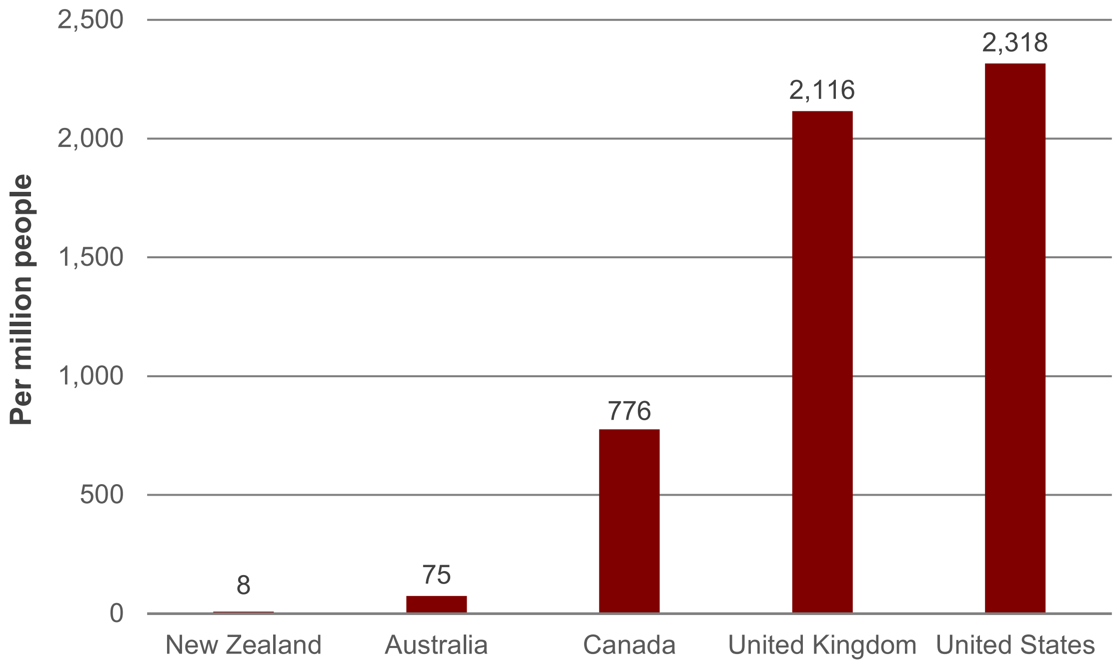
Border restrictions have had an impact on our human capital, decreasing net migration and impacting the availability of skills in some sectors. Those already disadvantaged in the labour market are typically most at risk from further disadvantage from economic shocks. They include young people, women, and Māori and Pacific peoples. However, owing to the country's strong economic recovery, disproportionate distributional impacts of COVID-19 have been less significant than expected.

The labour market has recovered to pre-pandemic levels according to nearly every indicator, with an unemployment rate of 3.4 per cent for the September 2021 quarter (compared to 4.2 per cent for the same period in 2019) and underutilisation of 9.2 per cent (compared to 10.4 per cent for the same period in 2019).[1] Despite significant improvement, pre-existing inequities persist, with unemployment rates for young Māori and Pacific workers and young people still twice the rate of that for European New Zealanders and middle-aged workers. Unemployed people have reported lower levels of overall life satisfaction, lower mental wellbeing and higher levels of loneliness than the general population.[2]

Health

COVID-19 continues to represent a clear and acute threat to New Zealanders' physical wellbeing. The Government's ongoing public health response, including the vaccination campaign, is helping to mitigate this threat, but the pandemic is increasing pressure on the physical and mental wellbeing of New Zealanders. Looking across the COVID-19 pandemic, there has been a relatively limited impact on physical health outcomes in New Zealand. We have seen a low mortality rate, relatively low hospitalisation rates, and declines in cases of other respiratory diseases.

Figure 1 – Confirmed COVID-19 deaths



Source: John Hopkins University CSSE COVID-19 Data. As of 20 November 2021

1 *Labour market statistics: September 2021 quarter.* Stats NZ, November 2021.

2 *Wellbeing statistics: March 2021 quarter.* Stats NZ, May 2021.

88 per cent of New Zealanders report they are in good health. This is much higher than the OECD average of 69 per cent and one of the highest scores across the OECD.[3] The pandemic is also affecting the mix of healthcare demand in our communities. Repeated lockdowns, while effective in mitigating the transmission of COVID-19, have suppressed other illnesses, such as respiratory syncytial virus (RSV), which has led to larger outbreaks when Alert Levels have decreased. Lockdowns have also disrupted the provision of elective and other non-urgent surgeries, and delayed some diagnoses. There is significant work underway on how we manage these in the coming years.

These outcomes are not distributed evenly across population groups. While Asian New Zealanders (90.3 per cent) and European New Zealanders (88.6 per cent) reported the highest proportion of adults with good or very good health in 2020/21, Māori (82.1 per cent) and Pacific peoples (81.7 per cent) have reported worse rates.[4] The gap in reported health between Māori and Pacific peoples and the rest of the population has widened in the past two decades.[5] Addressing these outcomes is one of the objectives of the health and disability system reforms, which include the establishment of a Māori Health Authority, with the power to directly commission health services for Māori.

There has been a general decline in the reported mental health of New Zealanders since the mid-2000s. The proportion of people reporting high psychological stress sometime in the past four weeks has increased to 9.6 per cent, and the proportion with mood and/or anxiety disorders has risen from 12 per cent in 2006 to 21.5 per cent in 2020/21. COVID-19 is further increasing pressure on the mental health of New Zealanders with around half of people being strongly or somewhat worried about the health of their family members and 21 per cent strongly or somewhat worried about getting COVID-19 themselves.[6]

Distributional challenges are also present in mental health. In general, Māori report levels of psychological distress that are almost twice as high (15.9 per cent) as, and suicide rates 80 per cent higher than, those of other New Zealanders. The rate of reported psychological distress is higher for females (11.8 per cent) than for males (7.3 per cent). Our youngest age group (15 to 24 years old) experience the highest rate of psychological distress, while the oldest groups (65 to 74, and 75-plus) have the lowest (below 5 per cent).[7] Since 2015, much of the overall rise in psychological distress has been driven by the 15 to 24 age group.[8]

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3 *New Zealand.* OECD Better Life Index. Retrieved 24 November 2021 from https://www.oecdbetterlifeindex.org/countries/new-zealand/

4 *2020/21 New Zealand Health Survey.* Ministry of Health, December 2021.

5 *Living Standards Framework Dashboard.* Retrieved 24 November 2021 from https://lsfdashboard.treasury.govt.nz/wellbeing/

6 *Provisional monthly results on COVID-19 impacts: 2020/21 New Zealand Health Survey.* Ministry of Health, July 2021.

7 *2020/21 New Zealand Health Survey.* Ministry of Health, December 2021.

8 *Living Standards Framework Dashboard.* Retrieved 24 November 2021 from https://lsfdashboard.treasury.govt.nz/wellbeing/

Moving to the next phase in our pandemic response

The Government's COVID-19 elimination strategy has proven to be a successful approach to managing the first phase of the pandemic. We have had one of the lowest mortality and hospitalisation rates in the world. At the same time the economy has been resilient, even though particular sectors and regions have been impacted by restrictions. Our high vaccination rates have enabled us to move to the next phase in our response, with a focus on minimisation and protection.

With the arrival of the Delta variant we have needed to change our strategy. The COVID-19 Protection Framework is based on a minimisation and protection approach backed by high vaccination rates. It brings us a world in which we are freer to move and live with less disruption and offers the stability businesses need to plan for the future. It introduces a new flexible three-level approach to managing COVID-19 in the community:

- **Green** is when COVID-19 is across New Zealand, including sporadic imported cases. Community transmission is limited and COVID-19 hospitalisations will be at a manageable level. The health system will be ready to respond, including with primary care, public health, and hospitals.
- At **Orange** there will be community transmission, with pressure on our health system. The whole of the health system is focussing its resources, but can continue to manage primary care, public health, and hospitals. There may also be an increasing risk for at-risk people.
- At **Red** action is needed to protect at-risk people and protect our health system from an unsustainable number of hospitalisations.

Economic support measures like the Wage Subsidy Scheme and the Resurgence Support Payment have provided critical support to both employers and workers during the first phase of the pandemic. As both border measures and domestic restrictions evolve, economic support measures will become targeted to those most in need and tailored to their circumstances.

The Government will facilitate a community-based welfare response to support New Zealand to transition to the COVID-19 Protection Framework. This will enable a regionally-led, whole-of-government response, and will provide support for housing needs, food parcels and other wellbeing items to ensure people can safely self-isolate at home.

As part of our work to reconnect New Zealanders with the rest of the world, changes to border measures will continue to be rolled out through the first half of 2022:

- Fully vaccinated Kiwis and other eligible travellers will be able to travel from Australia to New Zealand, undertaking self-isolation when entering New Zealand, from 11.59pm on 16 January 2022.
- Fully vaccinated Kiwis and other eligible travellers will be able to travel from the rest of the world to New Zealand, undertaking self-isolation when entering New Zealand, from 11.59pm on 13 February 2022.
- All fully vaccinated individuals will be able to travel to New Zealand from 30 April 2022 onwards, with the re-opening staged over time.

Arrivals who do not meet vaccination requirements and those from Very High-Risk countries will continue being required to complete seven days in managed isolation, followed by three days of home isolation. Further details of the reconnecting strategy are being developed, and the whole strategy will remain under constant review.

Education

The Government has invested heavily in supporting education, skills, and training as the economy recovers from COVID-19, to ensure students stay connected to their education and training institutions while unemployed people and those looking to retrain can access tertiary education.

Education attainment at the upper-secondary level has been improving and is nearing the OECD median. In 2020, 81 per cent of New Zealanders aged between 25 to 64 had the equivalent of at least NCEA Level 2, compared to 68 per cent in 2004. Tertiary education rates are also increasing, with 36 per cent of New Zealanders having at least a bachelor's degree in 2020, compared to 24 per cent in 2004. While education outcomes for Māori and Pacific students have improved, there continue to be significant differences between these groups and the rest of the population. The proportion of Māori and Pacific peoples aged 25 to 64 with at least an upper-secondary school qualification was 66 per cent for both groups in 2020, up from 57 per cent and 52 per cent in 2008 respectively.[9]

Despite this general improvement in qualification attainment, results as measured by the Programme for International Student Assessment (PISA) have decreased. Our mean scores for reading, mathematics, and science declined from 524 in 2006 to 506 in 2015 and 503 in 2018. There are distributional differences here too, with Māori (460) and Pacific (438) students having significantly lower scores than European (519) and Asian (521) students in 2018.[10]

School attendance has declined since 2015, particularly for disabled learners and learners from socio-economically disadvantaged backgrounds. This problem is influenced by in-school, home, and community factors. While work is underway to address the structural causes of this downward trend, our immediate concern is that poor attendance will be further worsened by COVID-19.

Time away from school during Alert Levels 4 and 3, particularly in Auckland, has had consequent impacts on engagement, learning and achievement. Following previous lockdowns, Ministry of Education data showed that most of the negative impacts of COVID-19 on attendance was concentrated on primary-school aged students, especially those in Years 1 and 2. These impacts will be felt most by the most disadvantaged students and will exacerbate existing inequities in the education system.[11]

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9 *Living Standards Framework Dashboard.* Retrieved 24 November 2021 from https://lsfdashboard.treasury.govt.nz/wellbeing/

10 *Living Standards Framework Dashboard.* Retrieved 24 November 2021 from https://lsfdashboard.treasury.govt.nz/wellbeing/

11 *He Whakaaro: How COVID-19 is affecting school attendance.* Ministry of Education, December 2020.

The Government has made significant investments targeted at improving New Zealand's human capital. These have included:

- the **Wage Subsidy Schemes**, which have paid out $18 billion between March 2020 and November 2021 to enable firms and workers to pay and stay connected to their workers during Alert Levels 4 and 3. At their peak, the subsidies supported around 1.76 million workers.
- a $486 million **initial investment in health and disability reforms** and the establishment of the interim Health New Zealand and Māori Health Authority, and an investment of more than $2 billion in supporting the **national response to COVID-19 across the health sector and implementing the COVID-19 vaccine rollout.**
- continuing work on **overhauling the welfare system** and addressing other recommendations from the Welfare Expert Advisory Group. The Government has committed to bringing forward the review of the Working for Families tax credits, currently on the medium-term welfare overhaul work programme.
- **lifting weekly benefit rates** by between $32 and $55 per adult in total over July 2021 and April 2022, in line with a key recommendation from the Welfare Expert Advisory Group.
- **increasing Working for Families from April 2022,** lifting the Family Tax Credit by $15 per week per eldest child and $13 per week for subsequent children; lifting the Best Start payment to $65 per week; and increasing the Orphan's Benefit, Unsupported Child's Benefit and Foster Care Allowance by $5 per week.
- an **increase in student loans** and allowances of $25 a week from April 2022.
- a $30 million **extension of the Student Hardship Fund** to keep students engaged in study during heightened Alert Levels.
- addressing a long-term imbalance in **funding for vocational education** with an additional $279.5 million over three years.
- the **Reform of Tomorrow's Schools**, to provide front line support closer to schools.
- **redeveloping the NCEA qualifications**, ensuring that 150,000 students who study NCEA every year have the appropriate skills and knowledge to seek further education or employment, either in New Zealand or overseas.
- establishing the **Apprenticeship Support Programme**, a cross-agency response to help employers retain and bring on new apprentices while dealing with the effects of COVID-19. This includes schemes like the **Mana in Mahi** programme, which supports those most disadvantaged in the labour market into sustainable work, and the **Apprenticeship Boost Initiative**, which has supported over 35,000 apprentices in their first and second year.

NATURAL CAPITAL: OUR ENVIRONMENT

Natural capital covers all aspects of the natural environment that support life and human activity, such as land, soil, water, plants and animals, minerals, and energy resources. It therefore has a significant impact on life satisfaction outcomes and serves as a catalyst for other variables relevant to wellbeing, like health outcomes and social connections.

The Government will continue to take action against environmental degradation. However, there is further work to be done on implementing these changes in an efficient and equitable manner.

Environmental quality

While New Zealanders on average enjoy a high level of environmental quality, there are long-standing challenges that are no less pressing in the wake of COVID-19. Our native freshwater species, habitats, and ecosystems are under threat and continue to decline due to the way we use our land and water resources.

Around half of New Zealand's land is used to produce agricultural and forestry products for export, with approximately 15 per cent of land being particularly good for food production. Expanding urban centres are encroaching on this highly productive land, and this is encouraging producers to adopt more intensive land management approaches to maintain productivity. Native vegetation continues to be removed in some regions, including the West Coast and Southland. About 25 per cent of the total area of native vegetation cover in New Zealand is on land used for sheep and beef farming, with only 3 per cent of this land permanently protected by conservation covenants.[12]

More intensive agriculture and urban expansion, combined with the conversion of native forests and wetlands, can increase pollution in our freshwater and marine environments. These changes have a cumulative impact on the environment, putting our native species at risk and reducing the benefits New Zealanders receive from nature.[13] These risks will be amplified by the effects of climate change.

Climate change

In June 2021 He Pou a Rangi, the Climate Change Commission, submitted its advice to the Government on its first three emissions budgets and a direction for its Emissions Reduction Plan for 2022 to 2025. This advice demonstrated that while current policy settings will reduce emissions and move us closer to our climate change targets, significant further action is required to meet them.

There continue to be short-run improvements in several natural capital measures owing to the COVID-19 pandemic. In the year ended March 2021, New Zealand emitted its lowest amount of greenhouse gasses in seven years, with the largest reductions coming from the transportation, postal and warehousing industries.[14] These reductions will be temporary, as the need for lockdowns declines and border restrictions are lifted.

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[12] *Our Land 2021*. Ministry for the Environment, November 2021.

[13] *Our Freshwater 2020*. Ministry for the Environment, April 2020.

[14] *Greenhouse gas emissions (industry and household): March 2021 quarter.* Stats NZ, August 2021.

The long-term impacts on New Zealand's natural capital of economic and behavioural changes as a result of the COVID-19 pandemic are uncertain. For example, a long-term shift in tourism behaviour could lead to enduring emissions reductions. Tourist activity generates approximately 7 per cent of New Zealand's greenhouse gas emissions, primarily via air and land-based travel.[15] However, the biggest generators of emissions in New Zealand are the agricultural and transport sectors where the impacts of COVID-19 have been relatively low or are expected to be short-lived. Permanent reductions to the emissions profile of these sectors will come from concerted and coordinated efforts by the Government and industry.

The Government has made significant commitments to protect our natural capital. These include:

- **recapitalising New Zealand Green Investment Finance:** in Budget 2021, $300 million was allocated to recapitalise New Zealand Green Investment Finance so that it could continue to invest in support of climate change mitigation, with a particular focus on decarbonising public transport, waste, and plastics.
- **its international climate commitments:** ahead of the 26th Conference of the Parties in Glasgow (COP26) in November, the Government announced a $1.3 billion increase in international climate finance for developing countries under the Paris Agreement over four years (2022 – 2025). The Government has also committed to halving New Zealand's greenhouse gas emissions (compared to 2005 levels) by 2030.
- **Protecting and preserving Kauri:** $28 million to finalise and implement a National Pest Management Plan to manage the threat of kauri dieback.
- **Jobs for Nature:** this is a $1.22 billion investment programme to create 11,000 nature-based jobs.
- **Emissions Reduction Plan:** the Government is currently developing its first Emissions Reduction Plan, to respond to the recommendations made by He Pou a Rangi, the Climate Change Commission, in its 2021 report. This will be released by 31 May 2022.
- **tackling on-farm emissions:** the Government is backing initiatives that help to reduce the costs to farmers and growers of lowering their emissions profiles, including $37 million toward a national integrated farm planning system and $24 million toward agricultural greenhouse gas mitigation research and development.
- **the Clean car package:** the Government has introduced a feebate scheme to help accelerate the decarbonisation of New Zealand's vehicle fleet.

[15] *Greenhouse gas emissions (industry and household): Year ended 2019.* Stats NZ, July 2021.

SOCIAL CAPITAL: OUR CONNECTIONS

Social capital includes the social connections, attitudes, norms, and institutions that contribute to societal wellbeing, for instance, through giving us a sense of belonging.

New Zealand enjoys a strong sense of community and high levels of civic participation. The OECD's Better Life Index reports that 96 per cent of New Zealanders believe they know someone they could rely on in a time of need, higher than the OECD average of 89 per cent. New Zealand's voter turnout was 80 per cent at last year's election, also higher than the OECD average of 68 per cent.[16]

The strength of New Zealand's social capital has continued to be a major contributor to the success of our COVID-19 response. During the Delta outbreak, Google Mobility data showed that most New Zealanders supported staying home to save lives, and this led to reductions in workplace mobility and corresponding increases in residential mobility comparable to the periods during heightened Alert Level restrictions in 2020. As a result, restrictions kept the outbreak to a manageable level while the vaccine rollout continued. However, domestic restrictions and border measures have negatively impacted on social capital, separating families and making it difficult for some New Zealanders to return home from overseas.

Trust in institutions

In addition to their support for staying home to save lives, New Zealanders' trust in people and institutions has been demonstrated by our high COVID-19 vaccination rates. Having as many New Zealanders as possible vaccinated slows the spread of COVID-19 and significantly reduces the proportion of people who contract the disease needing hospital care. On 16 October 2021, Super Saturday saw communities come together in novel and creative ways to boost our vaccination rates. More than 130,000 doses were administered, with more than 2.5 per cent of the population receiving jabs in a single day. New Zealand's high vaccination rate will support our economic recovery as we look to reconnect with the world.

An important consideration for maintaining and building trust in institutions will be how we manage the uneven impacts of the crisis for different population groups and generations. While the wellbeing supplement to the Household Labour Force Survey found that trust in most institutions was high, it was lower for Māori (which may be reflected in the slower vaccine uptake among younger Māori than in other groups) and those with disabilities.[17] There is also evidence that younger New Zealanders already have less trust in each other than older New Zealanders.[18]

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[16] *New Zealand.* OECD Better Life Index. Retrieved 24 November 2021 from https://www.oecdbetterlifeindex.org/countries/new-zealand/

[17] *Measuring inequality for disabled New Zealanders: 2018.* Stats NZ, October 2020.

[18] *Who do we trust in 2019?.* Institute for Governance and Policy Studies, June 2019.

Social cohesion and safety

While many areas of New Zealand's social capital are strong, there are some persistent challenges. Māori, Asian New Zealanders and Pacific peoples are more likely to report having experienced discrimination than the general population.[19] A survey undertaken by the Human Rights Commission found that Māori and ethnic Chinese respondents had been particularly vulnerable to experiences of discrimination since the start of the COVID-19 pandemic.[20]

The 2019-2020 New Zealand Crime and Victims Survey reported that more than three-quarters of adults perceived their overall safety as high. However, New Zealand women felt much less safe than men. As reported by the OECD, New Zealand has the second-highest gender gap in feelings of safety, only behind Australia.[21]

Nearly half of all homicides and reported violent crimes in New Zealand are family violence related. In 2020, 2.1 per cent of New Zealanders aged 15 and over said they had been victims of family violence in the previous 12 months. Positively, this represented a decline from 2.3 per cent on 2019. However, rates remain significantly higher than the general population for both women (3.3 per cent) and Māori (4.7 per cent), although the rate for Māori dropped from 6.1 per cent in 2019.

Community support

The strengths of iwi and other community organisations have been highlighted in the response to COVID-19, and the ways in which communities, marae and hapū supported the wellbeing of their whānau. Community-led support has helped whānau access information, financial resources, testing and vaccination.

In addition to a $45 million package in Budget 2020 for Whānau Ora providers to provide tailored responses for Māori communities during the pandemic, in September 2021 the Government announced $38 million of funding to support whānau Māori and Māori health providers in their ongoing work in responding to COVID-19. In October, a further $120 million was provided to create the Māori Communities COVID-19 Fund to fast-track vaccination efforts. These investments followed engagement with the Māori health and disability sector, which demonstrated that providers were struggling to support the COVID-19 response with their current resources. Budget 2021 also saw $380 million ring fenced for infrastructure to enable housing for Māori from the $3.8 billion Housing Acceleration Fund.

The Government has also made extra support available to community organisations to help them share COVID-19 vaccination information within their communities, and to encourage vaccine uptake. A $2 million community fund was also established during the Delta outbreak to provide support to organisations working to improve outcomes for women and girls adversely affected by COVID-19.

The full impact of COVID-19 on our communities may not be known for some time, but the Government remains committed to lifting children out of poverty and supporting communities in three key areas: increasing incomes for families; reducing housing costs and other pressures on low-income households; and changes to support the wider wellbeing of families.

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[19] *Wellbeing statistics: March 2021 quarter.* Stats NZ, May 2021.

[20] *Te Kaikiri me te Whakatoihara I Aotearoa I te Uruta COVID-19.* Human Rights Commission, February 2021.

[21] *How's Life? 2020.* OECD, March 2020.

FINANCIAL AND PHYSICAL CAPITAL: OUR BUILT AND FINANCIAL ASSETS

Financial and physical capital refers to assets owned by households, companies and the Government that range from cars and databases to financial assets such as cash and shares.

The head start New Zealand had in its economic recovery as a result of the elimination strategy meant it recovered faster and stronger than expected in the year to June 2021, with real GDP increasing by 5.1 per cent. The strong health response was also the best economic response, as it allowed our economy to open faster than those of many of our peers. Although the reintroduction of higher Alert Level restrictions in August 2021 is likely to lead to a sizeable fall in real GDP in the September quarter, the experience of 2020 suggests the economy will rebound quickly again.

The Government's fiscal position remains strong, with New Zealand's Government debt forecast to remain at levels that are sustainable. This has enabled continued support to mitigate the impacts of the higher Alert Level restrictions introduced in August 2021 on businesses and workers. Net core Crown debt is forecast to be 30.2 per cent of GDP in 2025/26. This is significantly lower than forecast for most advanced economies and will reduce the intergenerational inequity of high public debt.

Firms and supply chains

While strong economic conditions in late 2020 and throughout 2021 helped to boost firm resilience in aggregate, border restrictions and domestic public health restrictions such as social distancing requirements and capacity limits are affecting some sectors disproportionately, especially hospitality, tourism and the arts. There are pressures on small firms and sole traders in many sectors given that their buffers tend to be more limited. Supports such as the Wage Subsidy Scheme and the Resurgence Support Payments aim to mitigate some of these pressures, and in October 2021 the Government provided an additional boost to businesses in Auckland impacted by ongoing restrictions, including a $60 million package for business advice and mental health support.

Global supply chain issues are creating a difficult trading environment for many sectors and firms, as global consumer demand remains high and rising air freight prices divert cargo to sea, exceeding available shipping and port capacity. A Research New Zealand survey in June 2021 found that two-thirds of construction businesses interviewed identified three issues as affecting their ability to deliver projects on time and to budget: price increases; supplies; and material shortages and workforce shortages.[22] New Zealand also faces a challenge in maintaining air connectivity and freight capacity as the rest of the world reopens, with experience following the Global Financial Crisis suggesting that carriers may concentrate their reduced resources on lower risk, more profitable routes.

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[22] Research New Zealand, July 2021. https://www.constructionaccord.nz/assets/Construction-Accord/files/supply-chain-survey-stage-1-final-report.pdf

In addition to contributing to workforce shortages, border restrictions here and abroad are impacting on the ability of exporters to develop and maintain existing access to markets, limiting the competitiveness of those firms internationally. The Government's phased approach to lifting border restrictions safely, which will continue to be rolled out through the first half of 2022, will help address this.

Despite border restrictions and supply chain issues, the impacts of COVID-19 on individual sectors continue to be highly variable. Driven by strong performance in the primary sector, overall goods exports continue to grow, and as of October 2021 were $2.7 billion or 4.6 per cent higher than at the same point in 2019.[23]

Services exports continue to struggle as border restrictions impact on the tourism, education and hospitality industries. Despite some recovery in the quarter ending June 2021, services exports were still 43 per cent below their levels in the quarter ending December 2019 (the last quarter unaffected by border restrictions). Reopening will bring some relief to these industries, but demand for international tourism and education will likely remain below pre-pandemic levels for an extended period as a result of continued global uncertainty and reduced air connectivity.

Financial markets

New Zealand's financial system has coped well with the COVID-19 pandemic, having been supported by accommodative fiscal and monetary policy responses. Financial institutions remain robust, with strong capital and liquidity positions. This has ensured that banks and other financial institutions remain well-positioned to support the economy and wellbeing of New Zealanders. New Zealand's share market has also continued to perform well, having begun 2021 at near record-high levels on the back of strong growth as the economy rebounded quickly out of COVID-19.

Much of the momentum has been driven by strength in spending by households, with household spending in the year to March 2021 up $3.4 billion to $185.1 billion.[24] Reserve Bank of New Zealand data also shows that, in aggregate, consumers have continued to pay down non-mortgage debt. Total non-mortgage consumer lending fell from $16.8 billion in February 2020 to $13.3 billion in September 2021, a decrease of 20.8 per cent. However, this was offset by a sharp increase in household mortgage lending that accompanied rising property prices – from $279.9 billion to $323.9 billion in the same period (an increase of 15.7 per cent).

Household debt levels, in aggregate, have remained manageable because of low interest rates. However, pressure on some households' disposable income may increase, as financial conditions have been tightening due to expectations of increases in the Official Cash Rate. Stronger economic data, a tight labour market and the accelerating vaccine rollout globally have increased market confidence that economic conditions will eventually warrant higher interest rates.

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23 *Overseas merchandise trade: October 2021.* Stats NZ, November 2021.

24 While household spending was robust going into the Delta outbreak in August, there was a decrease in the September 2021 quarter with households, particularly in Auckland, limited in their ability to consume under higher Alert Level restrictions. However, spending is expected to continue recovering as restrictions ease in the months ahead.

Total business lending recovered to $120.5 billion in September 2021 after declining to $116.3 billion in December 2020.[25] This suggests confidence in the economy returning as businesses increase investment and hire more workers.

Housing

Housing market activity continues to be strong, with over 47,715 new homes consented in the year to October 2021, a 26 per cent increase on the same period in 2020.[26] Rising construction costs, issues finding skilled labour and supply chain problems risk constraining sector capacity.

Housing affordability remains a major challenge. Following the first wave of the pandemic, median house prices nationally increased by 23.4 per cent to $895,000 in the year to October 2021.[27] Census data shows homeownership rates have declined for all ages since the early 1990s, particularly for those in their 20s and 30s. In 2018, 44 per cent of people aged 25 to 29 lived in owner-occupied homes, down from 61 per cent in 1991.[28]

The percentage of households with high housing costs (greater than 30 per cent of income) has been around 30 per cent in the past decade. This impact is felt unevenly, with housing costs absorbing 45 per cent of incomes for households in the bottom quintile of the income distribution compared with 15 per cent for households in the top quintile.[29] Further, households that rent spend, on average, a higher proportion of their incomes on housing than owner-occupiers.

There are also distributional issues associated with housing quality. 2018 General Social Survey data indicated that 18.7 per cent of the housing stock required either major or moderate repairs, and that these houses are more likely to be occupied by females, and Māori and Pacific peoples than males and other New Zealanders.[30] Poor-quality housing had a material impact on life satisfaction, with 54 per cent of people who reported four key housing quality issues reporting low life satisfaction.[31]

Addressing housing issues is a major focus for the Government. In March 2021, it announced a range of initiatives to both increase supply and remove incentives for speculators in order to deliver a more sustainable housing market. The $3.8 billion Housing Acceleration Fund aims to remove a significant barrier to new housing developments by providing funding to support the building of services to new homes, such as roads and utilities. Other changes such as the extension of the bright-line test to 10 years and removing interest deductibility may be having an impact, as CoreLogic data shows first home buyers hit a record share of property purchases in the quarter ending September 2021, while the proportion of mortgaged investors in the market declined.[32] The annual number of new homes consented has been setting new records since March 2021 when the previous high (in the year ended February 1974) of 40,025 was surpassed for the first time.

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25 *Registered banks and non-bank lending institutions: Sector lending (C5)*. Reserve Bank of New Zealand. Retrieved 23 November 2021 from https://www.rbnz.govt.nz/statistics/c5

26 *Building consents issued: October 2021*. Stats NZ, December 2021.

27 Real Estate Institute of New Zealand, October 2021.

28 *Housing in Aotearoa: 2020*. Stats NZ, December 2020.

29 *Household incomes in New Zealand: trends and indicators of inequality and hardship 1982 to 2017.* Ministry of Social Development, 2018.

30 *New Zealand General Social Survey 2018.* Stats NZ, June 2019.

31 *Housing in Aotearoa: 2020.* Stats NZ, December 2020.

32 *First Home Buyer Report.* CoreLogic, November 2020.

Infrastructure

Infrastructure will play an important role in New Zealand's recovery from COVID-19 and our transition to a low-emissions and climate-resilient economy. While estimates vary, New Zealand's infrastructure deficit has been independently estimated at between $17 billion[33] and $75 billion.[34] Resolving this deficit will support higher levels of productivity and keep our economy growing. In 2017 the new Labour-led Government inherited an infrastructure spend over the previous nine years of $43.7 billion. From 2018 to 2021, $34.7 billion was invested, and we enter 2022 with a further $58.6 billion worth of infrastructure investment plans over the next five years.

Border restrictions and pressure on global supply chains present immediate challenges to the delivery of new infrastructure. This is primarily due to shortages of experienced staff, materials and supplies which are driving up prices and pushing out project timeframes. The Government is taking measures to address these issues, such as through the Apprenticeship Boost initiative, which pays up to $1,000 per month for employers to train apprentices and providing border exceptions for specialist construction workers.

The Government's infrastructure investment programme includes:

- $3 billion towards delivering over 240 community-focused **infrastructure projects** across the country, which support the construction sector and create jobs in response to COVID-19, as part of the Infrastructure Reference Group Shovel-Ready Programme established in 2020.
- increased **capital investment in health** ($870 million capital), building on the record capital investment over the previous two Budgets ($750 million through Budget 2020 and $1.7 billion through Budget 2019, plus $1.4 billion announced for the redevelopment of Dunedin Hospital). A $100 million of further capital was announced in December 2021 to upgrade ICU facilities and capacity.
- a record investment of more than $4.5 billion per year in **roads, rail and public transport infrastructure** through the National Land Transport Fund.
- **school property investment** ($634.1 million capital in Budget 2021) to help prevent overcrowding in schools and ensure students have access to quality teaching and learning environments.
- **Future of Rail investments** ($810 million capital and $449.9 million operating) to replace ageing locomotives and upgrade KiwiRail's mechanical maintenance facilities, and fund the ongoing maintenance and renewal of the rail network via the National Land Transport Fund.
- a $3.8 billion **Housing Infrastructure Fund** to increase the pace and scale of housing delivery by helping fund the critical infrastructure needed for developments.

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[33] *New Zealand*. Global Infrastructure Outlook. Retrieved 17 November 2021 from https://outlook.gihub.org/countries/New%20Zealand

[34] *Infrastructure for the long haul: A need for transparency and durability*. Sense Partners (commissioned by the Association of Consulting and Engineering New Zealand), September 2020.

HE ARA WAIORA: TE TAIAO AND TE IRA TANGATA

He Ara Waiora has been developed alongside the Living Standards Framework to understand waiora, often translated as a te ao Māori perspective on wellbeing. He Ara Waiora articulates the 'ends' or the important elements of Māori perceptions of wellbeing, which are Wairua (spirit), Te Taiao (the natural world – the environment) and Te Ira Tangata (the human domain). It also sets out the 'means', or the tikanga values or principles that help us achieve the ends (kotahitanga, tikanga, whanaungatanga, manaakitanga and tiakitanga). All these elements are seen as interrelated, and this is represented by the takarangi (connecting spiral pattern) that is overlaid on the framework.

He Ara Waiora, while being an ao Māori approach to wellbeing, has applications for all New Zealanders.

TE TAIAO

Te Taiao, the natural world, is near the centre of He Ara Waiora. This is because it represents the foundation for all life and wellbeing, and is therefore seen as an inherent good. People come from and are sustained by the natural world, with whenua (land) and other aspects of Te Taiao inextricably linked to identity. People therefore have a responsibility to look after the natural world, and in doing so cultivate wellbeing that is holistic and intergenerational.

As a result of COVID-19, some human activity harmful to Te Taiao temporarily ceased, and as we look towards recovery, we should utilise these lessons to improve our guardianship of the natural environment. For example, many businesses were forced to embrace greater digitalisation, reducing travel by air and road, thereby reducing vehicle emissions, while achieving the same economic outputs. This suggests there are more sustainable ways to operate businesses into the future while reacting to the demands of climate change. It also highlights that in order to continue to reduce emissions in this way, we need to work to establish better digital connectivity for those in the furthest reaches of New Zealand.

TE IRA TANGATA

Mana tuku iho

Mana deriving from a strong base of identity and belonging.

Mana tuku iho aligns with social capital in terms of the social inclusion, confidence and resilience that derive from community belonging and a strong sense of identity. For Māori, this is strongly linked to iwi and hapū, to place and whenua, and to an ability to connect authentically to culture, for example though the use of language. Throughout COVID-19, this has been exemplified by Māori organisations that have prioritised action in supporting communities and safeguarding their own people, including their kaumātua.

Mana tuku iho can be utilised to enhance growth by leveraging traditional knowledge and practices central to respective communities. An example is tuakana/teina (peer mentoring) models in business, social enterprise and social entrepreneurship, such as the establishment of Manaaki, a support network of business experts and advisors for businesses struggling during COVID-19.

Mana tauutuutu

Mana found in knowing and fulfilling one's rights and responsibilities to the community, and in the participation and connectedness of an individual in their community.

Mana tauutuutu has been demonstrated continually in response to COVID-19, through actions such as the delivery of food parcels and medications via services such as Whānau Ora and NGOs, and individuals sharing their resources. Having bespoke delivery models is a way of enhancing mana and of communities supporting communities, which is potentially more accessible for those who need additional assistance as it moves to a model of reciprocal care, rather than welfare or charity.

Within the health sphere, this communal sense of responsibility has supported high testing rates for COVID-19 within communities, as individuals seek to keep their communities safe. In the Pacific community, this has led to testing rates of 1.7 tests per person during the pandemic – almost double the rate of the total population.[35]

Mana āheinga

Mana in the individual's and the community's capability to decide on their aspirations and realise them in the context of their unique circumstances.

Aspirations, while linked to economic prosperity, range further than that, and include social, cultural and environmental outcomes.

In the context of the latest COVID-19 outbreak, one of the most significant aspirations for Māori communities has been around the health and broader wellbeing of the population. When resourced well and early enough, iwi and Māori providers have been effective in supporting these aspirations. In response to this, marae and iwi have mobilised to improve the vaccination rates in the community, delivering Māori-led vaccination programmes. This has been important as it has helped to overcome some delivery barriers. For example, people who face childcare issues and transport issues, elderly who are unable to attend mass vaccination events, those who are not enrolled with GPs, and those without the digital connectivity to book in a vaccination.

The new Māori Health Authority, established as part of the health reforms, will be an autonomous entity with the ability to commission services. It will undertake joint decision-making with Health New Zealand to grow kaupapa Māori services and give Māori a strong voice in the new health system. This is one way of improving the ability of Māori to realise their own aspirations in the context of healthcare.

In the economic space, COVID-19 has brought with it a focus on maintaining employment and building skills, which are strong factors in providing individuals and whānau with a greater choices and scope to fulfil aspirations. It includes enabling Māori businesses, which on average hire a larger proportion of Māori than non-Māori owned businesses.

In addition to COVID-19 economic support for businesses, the Government has provided support through a Māori trades and training fund to encourage the sustained employment, or redeployment, of the Māori labour force. Māori-led business support services have helped Māori businesses to access COVID-19 economic support and navigate a difficult trading environment.

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[35] *Testing for COVID-19.* Ministry of Health. Retrieved 24 November 2021 from https://www.health.govt.nz/our-work/diseases-and-conditions/covid-19-novel-coronavirus/covid-19-data-and-statistics/testing-covid-19

Mana whanake

Mana in the form of the power to grow sustainable, intergenerational prosperity.

The asset base of the Māori economy was estimated to be worth $68.7 billion in 2018.[36] Continuing to grow the Māori economy is key to building intergenerational sustainability and prosperity, but COVID-19 poses a risk of economic scarring. The Government is aware of and seeking to address issues in the delivery of COVID-19 supports by working with Māori leaders and delivery agencies.

Historically, Māori have been impacted more severely and for longer than other New Zealanders by financial downturns. Until 2019 the Māori unemployment rate was higher than it had been before the Global Financial Crisis. Since COVID-19 we have seen the highest rates of unemployment for wahine Māori and Pacific women compared to the rest of the population.[37] The median ages of Māori (26) and Pacific peoples (23) are significantly lower than that of the general population (38), meaning these groups are important to the overall strength of the future workforce. These age groups are also likely to suffer the lifelong consequences of labour market scarring early in their careers. It is important as we move through the recovery that we consider the specific needs of Māori and Pacific peoples to continue building their economic resilience to shocks and build intergenerational prosperity.

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[36] *Te Ōhanga Māori – The Māori Economy 2018.* Berl, January 2021.

[37] Household Labour Force Survey data.

WELLBEING OBJECTIVES

The Public Finance Act 1989 requires the Government to set wellbeing objectives through the Budget Policy Statement and explain how these are intended to support long-term wellbeing in New Zealand. These objectives are intended to be relatively enduring, which reflects that sustained investment across multiple budgets is needed to address some of New Zealand's most significant, intergenerational challenges. The wellbeing objectives are interdependent and separate from the shorter-term goals and focus areas, which are intended to support the choices and trade-offs required as part of Budget decision-making.

Our wellbeing objectives for Budget 2022 are:

1. **Just Transition** – supporting the transition to a climate-resilient, sustainable and low-emissions economy
2. **Physical and Mental Wellbeing** – supporting improved health outcomes for all New Zealanders and minimising COVID-19 and protecting our communities
3. **Future of Work** – enabling all New Zealanders and New Zealand businesses to benefit from new technologies and lift productivity and wages through innovation
4. **Māori and Pacific Peoples** – lifting Māori and Pacific Peoples incomes, skills and opportunities, including through access to affordable, safe, and stable housing
5. **Child Wellbeing** – reducing child poverty and improving child wellbeing, including through access to affordable, safe and stable housing

These objectives are enduring and continue to focus on areas the Labour-led Government identified through extensive wellbeing analysis during 2019 and 2020. This work took a collaborative and evidence-based approach, using the Treasury's Living Standards Framework and incorporating advice from sector experts and the Government's Chief Science Advisors to identify the broad areas where there are the greatest opportunities to make a difference to New Zealanders' wellbeing.

Compared to the wellbeing objectives that formed the basis of Budget 2021, our objectives have been slightly revised to reflect an increased emphasis on the need to address housing access and affordability and the ongoing but evolving impacts of COVID-19.

How the wellbeing objectives are intended to support long-term wellbeing in New Zealand

1 Just Transition – supporting the transition to a climate-resilient, sustainable and low-emissions economy

Our wellbeing objective to achieve a just transition means we will actively support a move away from fossil fuels towards a low-carbon economy in a way that will support workers, businesses, and communities to make changes to how they live and work. This protects the long-term wellbeing of New Zealanders.

Achieving a just transition protects and enhances Te Taiao while increasing financial capital through new economic opportunities. A just transition enhances social capital by ensuring the transition is fair, does not undermine social cohesion and ensures the pace of change protects and grows human capital and mana whanake.

2 Physical and Mental Wellbeing – supporting improved health outcomes for all New Zealanders and minimising COVID-19 and protecting our communities

Good physical and mental health, and timely access to care and support when they are needed are fundamental to New Zealanders' long-term wellbeing. There is ample evidence that those who suffer from poor physical and mental health find it difficult to build their own skills so that they can achieve in the workforce and engage in society. This undermines both our human and social capital, with run-on effects on financial capital. Investing in a healthier population now makes individuals more resilient and reduces future health costs.

The pandemic has presented an acute challenge to New Zealanders' physical and mental health. Ensuring the best possible access to vaccination and testing, including for rangatahi and hard-to-reach groups, will prevent further hospitalisations and enable the economy to operate without the disruption of restrictions.

3 Future of Work – enabling all New Zealanders and New Zealand businesses to benefit from new technologies and lift productivity through innovation

Innovation is the process of translating an idea or invention into a good, service, or new process, that people value. It enables the creation of new jobs and industries which in turn helps to improve productivity, lift wages and meet society's needs in new ways.

Enabling all New Zealanders to benefit from the changing nature of work requires investing to expand access to training and technology infrastructure. This improves the ability of the labour force to meet changing requirements and increases the capacity of firms to engage with increasingly dynamic markets. Adapting to the future of work adds to New Zealand's stock of human capital which improves resilience and lifts incomes, building our financial and physical capital over the long-term.

4 Māori and Pacific Peoples – lifting Māori and Pacific Peoples incomes, skills and opportunities, including through access to affordable, safe, and stable housing

An equitable recovery from COVID-19, and a just transition to a climate focused future, offers an opportunity to enhance Māori and Pacific peoples wellbeing. These demographic groups have historically been hit the hardest by economic downturns and structural adjustments and take longer than other New Zealanders to recover. Given that Māori and Pacific peoples have a lower average age than other New Zealanders, and generally experience lower levels of wellbeing, investing to lift incomes, skills and opportunities for these groups will have a significant impact on enhancing wellbeing over time.[38]

The ability for many Māori and Pacific peoples to fulfil mana āheinga and build mana whanake is impeded when health, education, housing and social welfare systems do not address multifaceted, intergenerational disadvantage. For example, Māori and Pacific peoples have lower rates of home ownership than other New Zealanders and are more likely to live in cold and damp homes. This affects health, education and economic outcomes, impacting on cultural wellbeing (including a sense of tikanga and turangawaewae) and means New Zealand is missing out on the contributions that many Māori and Pacific people could be making to our economy, society and culture.

5 Child Wellbeing – reducing child poverty and improving child wellbeing, including through access to affordable, safe and stable housing

The experiences we have as children lay the foundation for healthy development and positive wellbeing throughout our lives. Good material standards of living enable parents and caregivers to provide children with a good start in life, which has been shown to contribute to lasting wellbeing outcomes in areas like health, housing and education.

Investing in a good start in life for our children is one of the most important ways we can ensure the wellbeing of New Zealanders over the long term. It will strengthen our social and human capital, leading to better economic and financial capital outcomes. One of the keys to this is improving the housing conditions our children grow up in – improving child wellbeing requires better access to warm, dry and safe housing. This makes reducing child poverty and improving child wellbeing one of our enduring wellbeing objectives.

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38 *National ethnic population projections: 2018(base)–2043.* Stats NZ, May 2021.

FOCUS AREAS FOR BUDGET 2022

This will be our fourth Wellbeing Budget. The wellbeing approach is designed to drive investments to improve New Zealanders' living standards by tackling long-term challenges as well as addressing the pressures immediately in front of us. Wellbeing means giving people the capabilities to live lives of purpose, balance, and meaning to them.

The Public Finance Act 1989 also requires the Government to outline the overarching goals that will guide its Budget decision-making, and the policy areas it will focus on in that year. These goals and focus areas will support the Government to make the choices and trade-offs required to produce a Budget that achieves our wellbeing objectives.

Overarching goals

This Budget will be aimed at continuing to make progress against the goals the Government set at the start of the current Parliamentary term. These are:

1. Continuing to keep New Zealand safe from COVID-19
2. Accelerating the recovery and rebuild from the impacts of COVID-19
3. Laying the foundations for the future, including addressing key issues such as our climate change response, housing affordability, and child poverty.

These overarching goals have informed the design process for Budget 2022. The core of this Budget will focus on continuing to make progress on meeting the Government's manifesto commitments and addressing critical cost pressures facing key public services. We have already made significant progress on meeting these funding needs in the past year, and this Budget will continue this trend.

Alongside this, Budget 2022 will make a step change in how the Government invests to address long-term challenges. This Budget embeds new multi-year funding approaches in the areas of health and climate change. It will also pilot changes to our public finance system by establishing Natural Resources and Justice clusters, which will enable increased coordination and collaboration in these sectors.

Policy areas of focus

Within these overarching goals, the Government has identified two policy areas of focus for Budget 2022. These are:

1 Embedding health reforms

The Government has a vision for a truly national public health service that delivers for all New Zealanders and places a greater focus on primary and community care.

COVID-19 has highlighted how vital a joined-up and prepared health system is for protecting New Zealanders, and there is long-standing evidence that the DHB-based system has not delivered equitable outcomes across the country –particularly for Māori. We are now taking the steps required to reduce fragmentation, address the challenges caused by historical underfunding, and support the structures that will enable the health system to improve outcomes for all New Zealanders.

Earlier this year, the Minister of Health outlined plans to replace DHBs with one national organisation (Health New Zealand), establish a new Māori Health Authority to drive hauora Māori and commission health services directly, and create a dedicated Public Health Agency. Budget 2021 provided an initial tranche of funding to get these vital reforms underway, but there is much more to do.

Through Budget 2022, the Government will look to provide a significant further investment to establish these new entities on a sustainable footing and to begin a staged delivery of the health system shifts envisaged through reform. Budget 2022 is also significant in beginning the transition to multi-year funding for Vote Health in order to give health entities increased funding certainty and support longer-term planning for health services.

2 Addressing climate change

Climate change is one of the most pressing long-term challenges facing New Zealand. To respond effectively to the challenge, we will need to make significant investments across multiple Budgets. To address this, the Government is establishing a Climate Emergency Response Fund (CERF), which will be allocated towards initiatives that support our climate change objectives. This will be an enduring, multi-year funding mechanism, to support our transition to a low-emissions and climate resilient economy in a way that protects vulnerable communities.

In Budget 2021, we announced that the Government would be spending the proceeds of our Emissions Trading Scheme (ETS) on emissions reductions programmes from Budget 2022 onwards. The CERF is the mechanism through which we will do this, and accordingly it has been established with $4.5 billion of cash proceeds from the ETS, based on the Treasury’s forecasts of proceeds over the period from 2022/23 to 2025/26.

Our intention is that these proceeds will start as a ‘down payment’ for our climate spending; we know that more funding is required to address a complex, multi-faceted issue like climate change. We expect to review the CERF alongside the main Budget allowances, and increase the funding available as necessary to invest in high-value initiatives that will help us to achieve our climate objectives.

For Budget 2022, the CERF will focus on initiatives and programmes aimed at delivering the emissions reductions outlined in the Government's first Emissions Reduction Plan (ERP). The plan will be released by 31 May 2022. Ahead of Budget 2022, the Government has committed $800 million in new funding to increase New Zealand's support for countries most vulnerable to the effects of climate change to $1.3 billion over the four-year period from 2022 to 2025, with at least 50 per cent of that funding going to Pacific Island countries. The $800 million, plus $40 million in new funding for administration costs, has been allocated from the CERF.

For future Budgets we will look to extend the scope of the CERF to fund measures to support adaptation to the changing climate, as well as climate change mitigation. This could support the development and implementation of our National Adaptation Plan, which will be released in late 2022.

Modernising the public finance system

It has been over 30 years since the public finance system was last fundamentally reformed. While the system has worked well in many ways, and has continued to evolve, a number of issues have arisen over time:

- Public finances are under pressure, and this has increased as a result of COVID-19. There is a need to achieve greater value from baseline spending and improve fiscal management and sustainability. The system currently focuses heavily on options for new spending, with limited attention to the value gained from existing expenditure.
- The system does not adequately support joined-up work on cross-sector issues; particularly complex, intergenerational issues.
- The annual government reporting and funding cycle is short, consumes a large amount of time and effort, and can be superficial. It can be hard for departments and agencies to focus on long-term wellbeing and sustainability.

To help address these issues, the Government is piloting changes this year to modernise the system for the current context. These changes involve inter-agency collaboration, medium-term planning, and a focus on value for money.

Clusters for Budget 2022

For Budget 2022, we are piloting two clusters of agencies and Ministers covering the Natural Resources and Justice sectors. Agencies in each cluster are working together to identify priorities and develop proposals that will inform their collective efforts over the next three years. Spending reviews of each cluster are underway to assess the efficiency and effectiveness of existing spending and determine future funding requirements.

Reforms to come

As we progress through Budget 2022, we will evaluate how these clusters are working and will make decisions on the future of the cluster approach next year.

Budget allowances and the Climate Emergency Response Fund

Budget allowances

Budget allowances show how much new investment and spending is available in each Budget over the next four years. The economic backdrop for Budget 2022 remains highly uncertain amidst ongoing domestic and global COVID-19 outbreaks. The Government will continue to balance careful Budget management with prioritising investments that meet the wellbeing objectives and the Government's overarching policy goals.

The Government has set new operating allowances at $6.0 billion for Budget 2022, $4.0 billion for Budget 2023, and $3.0 billion for Budgets 2024 and 2025. Overall, by the 2025/26 fiscal year these allowance settings are expected to have an operating impact of $16.0 billion per annum.

The higher operating allowance for Budget 2022 is a one-off, reflecting substantial investment in support of the Government's significant reform programmes, including the transformation of the health system. There is a need for substantial investment to ensure that Health New Zealand and the Māori Health Authority are established on a secure and stable footing and are able to address pressing health sector needs.

Following on from Budget 2022 allowances revert back to levels of investment similar to those announced in recent Budgets.

As part of Budget 2022 the Government will be making a step change in how it invests by embedding a multi-year funding approach for some sectors. This means Budget 2022 decisions for these sectors will cover new funding for initiatives for a few years. Therefore, it is generally expected that these sectors will not receive further funding through the next few annual Budget processes.

To enable the management of multi-year funding decisions there will be scope at Budget 2022 to announce operating spending that is funded from future operating allowances outlined in Table 1, provided that the impact broadly remains within the overall operating uplift expected from operating allowances by 2025/26.

The multi-year capital allowance has been increased by $4.0 billion across the four-year forecast period. This brings the total unallocated multi-year capital allowance to $9.8 billion, or an average of $2.45 billion to be allocated per Budget in addition to $2.3 billion of pre-committed Budget 2022 initiatives.[39] The multi-year capital allowance was introduced at Budget 2019, moving away from a single-year allowance to allow for a longer-term investment approach to capital spending.

These allowances have been incorporated into the Treasury's fiscal forecasts in the *Half Year Economic and Fiscal Update* (HYEFU). The allowances are subject to change, as economic and fiscal forecasts are updated for evolving economic conditions both in New Zealand and globally.

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[39] These figures incorporate decisions as at 25 November 2021 when the Treasury's fiscal forecasts were finalised.

Table 1 – Budget allowances

$ billions	Budget 2022	Budget 2023	Budget 2024	Budget 2025
Operating allowances before pre-commitments (per year)	6.0	4.0	3.0	3.0
Multi-year capital allowance	←	9.8		→

Source: The Treasury

Climate Emergency Response Fund

Climate change is one of the most pressing long-term challenges facing New Zealand. To respond effectively to the challenge, we will need to make significant investments across multiple Budgets.

To address this, the Government is establishing the CERF, which will be allocated towards initiatives that support our climate change objectives. It will be an enduring, multi-year funding mechanism, to support our transition to a low-emissions and climate-resilient economy.

As part of Budget 2021 the Government announced it would be hypothecating the revenues from the ETS toward emissions reduction programmes. Based on updated forecasts of proceeds from the ETS, we expect Budget 2022 will allocate $4.5 billion over the forecast period to the CERF.

The CERF is a multi-year allocation that can be spent across years, which will enable the Government to manage effectively the pipeline of investments we need make in the climate transition. The fund will be able to support either operating or capital expenditure as required, provided the expenditure is time limited.

Table 2 – Climate Emergency Response Fund, after international climate finance pre-commitment[40]

$ billions	2021/22	2022/23	2023/24	2024/25	2025/26
Climate Emergency Response Fund	←		3.7		→

Source: The Treasury

Although $4.5 billion will be allocated to the CERF as part of Budget 2022, more funding may be needed to support high-value, robust initiatives that reduce emissions and increase New Zealand's climate resilience in the future. This is consistent with the advice we received from the Climate Change Commission, which shows we need to start making changes now, while recognising that the road to a low-emissions, climate-resilient productive future will be a long one.

The CERF does not represent the whole picture for climate spending. There is a range of funding mechanisms available, including existing funds like the National Land Transport Fund, and institutions like New Zealand Green Investment Finance. The Government is also committed to partnering with the private sector to meet the funding and financing challenges of the climate transition.

40 $840 million of CERF funding has been allocated toward international climate finance, as at 25 November 2021. This leaves a remainder of $3.66 billion total in the fund.

Progress update: COVID-19 Response and Recovery Fund

Context

In Budget 2020, the Government established the COVID-19 Response and Recovery Fund (CRRF). It is a temporary fiscal management tool used to support New Zealand's response and recovery from COVID-19. It was originally set at $50 billion and built on the initial $12.1 billion support package announced on 17 March 2020.

Changes since Budget 2021

In September 2021, the Government allocated a further $7 billion to the CRRF. In addition, $3 billion was made available from money previously allocated in the fund that had not been spent. As at 25 November 2021, $4.3 billion of the CRRF remains unallocated. The remaining CRRF balance will be targeted at providing further economic support, as well as building health system resilience, supporting the vaccination rollout, and strengthening border systems.

ECONOMIC AND FISCAL FORECASTS

Economic outlook and forecasts

New Zealand's economic performance has been strong since the publication of the *Budget Economic and Fiscal Update* (BEFU) 2021, reflecting that the economy has been more adaptable and resilient to the COVID-19 pandemic than previously thought. Robust demand throughout the first half of 2021 has catalysed broad-based growth, with stronger-than-expected real production GDP, tax revenues exceeding forecasts, and the unemployment rate dropping to the lowest levels since 2007.

The Delta outbreak that began in August 2021 is expected to weaken this position in the September and December quarters, though we anticipate a relatively swift recovery in activity with only a small degree of scarring as restrictions ease. Accordingly, annual real GDP growth is forecast to peak in 2023, underpinned by growth in consumption and investment that is supported by low unemployment, a strong housing market, and the gradual re-emergence of international tourism.

COVID-19 has equally impacted the supply side, offsetting the disinflationary pressures from activity disruptions. Compounded by persistent domestic demand, supply-side pressures relating to labour/skills shortages, capacity constraints, and international supply-chain disruptions will increase inflationary pressures which saw annual CPI inflation come in above forecast in the September 2021 quarter at 4.9 per cent. Similar inflation is being seen in other advanced economies. In response, the Reserve Bank of New Zealand is expected to continue tightening monetary policy to bring inflation within the 1-3 per cent target band which may also moderate house price growth over the medium term.

This increase in real activity, in combination with higher inflation, translates to nominal GDP being $21.4 billion higher by the year to June 2025 and a cumulative $78.5 billion higher over the forecast period. This is the main driver of the additional $48.6 billion in core Crown tax revenue across the four years to June 2025.

The labour market has been remarkably resilient and is expected to persist in a state of tightness, with firms reporting record-high difficulties in finding skilled labour and near record-high difficulties in finding unskilled labour in the September 2021 quarter. Unemployment is consequently expected to continue to fall to 3.2 per cent in the June 2022 quarter before rising towards 4.1 per cent by the end of the forecast period, and employment is expected to continue to exhibit quarter-on-quarter growth. Both of these will exert upward pressure on wage inflation and labour costs.

The global economic recovery has lost some momentum due to the emergence of Delta and ongoing supply-chain disruptions but the outlook remains more positive than in BEFU 2021 due to vaccinations, policy support, savings drawdowns and the reopening of economic activity. A rise in export prices is forecast to boost the terms of trade in the short term, but declining export prices alongside persistently higher import prices will lead to a lower terms of trade in the medium term compared to BEFU 2021.

The economic forecasts are dependent on some key assumptions. For example, public health restrictions and behavioural responses to COVID-19 are assumed to impact activity to an extent similar to Alert Level 2 until 1 July 2022; the international border is assumed to have a gradual and phased reopening from 1 July 2022; and potential output has been revised lower to account for ongoing disruptions and behavioural shifts related to the pandemic. A significant deviation from these assumptions – on either the upside or the downside – would change the underlying fundamentals of the forecast, as would the realisation of key risks such as the advent of a more communicable or lethal coronavirus.

Table 3 – Summary of the Treasury's Half Year Update economic forecasts

June years	2021 Actual	2022 Forecast	2023 Forecast	2024 Forecast	2025 Forecast	2026 Forecast
Real GDP growth (annual average per cent change)	5.1	0.8	4.9	2.2	2.3	2.3
Real GDP per capita (annual average per cent change)	3.8	0.1	4.1	1.2	1.2	1.1
Unemployment rate (June quarter)	4.0	3.2	3.3	3.6	3.8	4.1
Consumers Price Index (annual per cent change)	3.3	5.1	3.1	2.7	2.4	2.2
Wage growth (annual per cent change)	4.0	4.1	4.5	4.6	4.4	4.2
Current account (annual, per cent of GDP)	-3.3	-5.8	-5.4	-4.8	-4.4	-4.0

Sources: Stats NZ, the Treasury

Fiscal outlook and forecasts

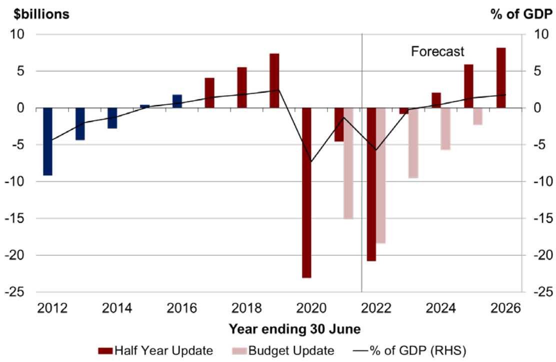
Careful management of expenses and the growing economy mean New Zealand enters the next stage of the COVID-19 response with one of the strongest fiscal positions among advanced economies.

Before the onset of the COVID-19 pandemic, the Labour-led Government ran surpluses and reduced net core Crown debt below 20 per cent of GDP, its lowest since 2011.

The Government's strong fiscal position means it has been able to support New Zealanders and businesses through the one-in-100-year global economic shock caused by COVID-19, including providing $69.1 billion for COVID-19 response, recovery and rebuild investments.

The final results for the 2020/21 fiscal year were stronger than the Treasury expected at BEFU 2021. The OBEGAL deficit of $4.6 billion in 2020/21 was $10.5 billion lower, while net core Crown debt was lower by $11.6 billion. The improvement in the results from the 2020/21 fiscal year has provided some headroom to manage the fiscal impacts from the recent Delta outbreak.

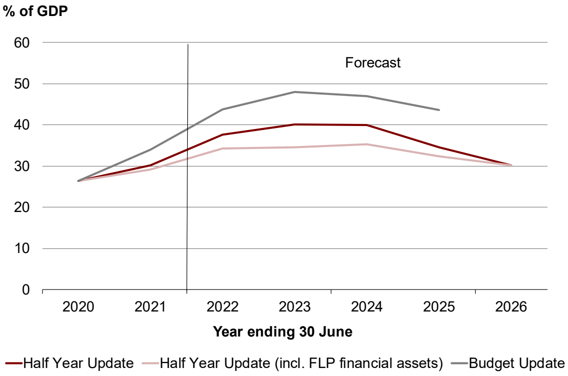
Figure 2 – OBEGAL



Source: The Treasury

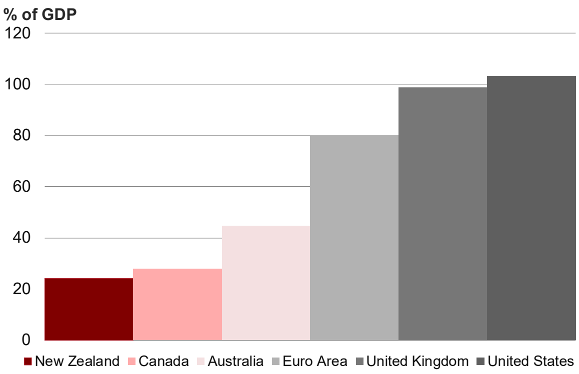
HYEFU 2021 shows a continued improvement in the fiscal outlook due to the growing economy and careful management of expenses. The OBEGAL deficit of $20.8 billion in 2021/22 is expected to be higher than at BEFU 2021, largely owing to the Government's fiscal support measures to respond to the Delta outbreak. Beyond 2021/22, a sharp recovery is expected as the temporary fiscal support measures unwind, and the economy is expected to continually grow. An OBEGAL surplus of $2.1 billion is expected in 2023/24, which grows to $8.2 billion by 2025/26, although these results could change by Budget 2022.

Figure 3 – Net core Crown debt comparison



Source: The Treasury

Figure 4 – IMF general government net debt in 2024 (forecast)



Source: IMF World Economic Outlook Database October 2021

The net core Crown debt track is now also forecast to be lower than at BEFU 2021, with a new forecast peak of 40.1 per cent in the 2022/23 year compared to 48.0 per cent of GDP at BEFU 2021. Net core Crown debt is forecast to fall to 30.2 per cent of GDP by the end of the forecast period. As discussed in BEFU 2021, the impacts of the Reserve Bank's Funding for Lending Programme (FLP) have affected the headline net debt forecasts due to the definition of net core Crown debt. Looking through the impact of financial assets from the FLP, net core Crown debt is now expected to increase to 35.3 per cent of GDP in 2023/24. The FLP is expected to be completed by the 2025/26 year and therefore will no longer impact on net core Crown debt.

The New Zealand Government's net debt position remains considerably favourable compared to other advanced economies, which went into COVID-19 with net debt averaging above 80 per cent of GDP. On an internationally comparative measure, New Zealand's net debt currently sits below that of Australia, the United Kingdom, the United States, Canada and the Euro Area and is projected to still be below in 2024 (Figure 4 refers).

Table 4 – Summary of the Treasury's Half Year Update fiscal forecasts

Year ending 30 June	2021 Actual	2022 Forecast	2023 Forecast	2024 Forecast	2025 Forecast	2026 Forecast
per cent of GDP						
Core Crown tax revenue	28.8	28.3	28.9	29.0	29.2	29.5
Core Crown expenses	31.7	35.3	30.5	30.1	29.5	29.3
Total Crown OBEGAL	(1.3)	(5.7)	(0.2)	0.5	1.4	1.8
Core Crown residual cash	(4.1)	(9.4)	(5.5)	(1.9)	3.3	2.7
Net core Crown debt	30.1	37.6	40.1	39.9	34.6	30.2
Net worth attributable to the Crown	44.6	35.1	33.4	33.6	34.8	36.4

Source: The Treasury

FISCAL STRATEGY

The Government's short-term intentions and long-term objectives for fiscal policy remain unchanged from Budget 2021

Our fiscal strategy continues to take a balanced approach to supporting current and future generations by managing debt prudently and reducing the deficit caused by COVID-19, while growing the economy sustainably and investing in important public services like health and education. Given the nature of the COVID-19 global economic shock and the need to support the economy, debt remains at prudent levels throughout the forecast period, and there remains space in the Government's fiscal strategy to respond to future shocks.

The Government's strong fiscal strategy and New Zealand's comparatively favourable debt position compared to other advanced economies mean credit rating agencies have maintained their strong ratings on New Zealand Government Bonds through COVID-19. In a ratings report, S&P Global Ratings noted that New Zealand was in a strong fiscal position before the pandemic hit and that proactive policy-making was supporting sustainable public finances and economic growth. Moody's continues to rate New Zealand Government debt at its strongest Aaa rating, while Fitch most recently retained its strong AA+ local currency rating.

Recent economic growth and careful management of government spending mean that net core Crown debt including FLP assets is now forecast to peak lower than in Budget 2021, at 35.3 per cent of GDP in 2023/24. Even at this peak, New Zealand's net debt as a percent of GDP remains lower than that of most other advanced economies based on comparable measures. OBEGAL is also forecast to return to surplus in 2023/2024. This shows an improvement since Budget 2021 and for comparison, OBEGAL did not return to surplus until the seventh year following the Global Financial Crisis.

The ongoing uncertainty around COVID-19 and volatility in the global economy mean that the current short-term intentions and long-term objectives remain fit for purpose, and have therefore not changed since the *2021 Fiscal Strategy Report* (see page 43 of that document). The Government's strategy for managing its expenditure, assets, and liabilities has also not changed since the *2021 Fiscal Strategy Report*.

Budget 2022 is expected to accord with our current short-term intentions and long-term objectives for fiscal policy by allowing net core Crown debt to rise in the short term while the Government is responding to COVID-19, and improving OBEGAL over the forecast period as economic conditions allow. The Government is committed to setting new fiscal targets at Budget 2022 with the expectation that the global economic outlook and conditions will stabilise.

Table 5 – Fiscal intentions and objectives

	Short-term intention	Long-term objective
Debt	Our intention is to allow the level of net core Crown debt to rise in the short term to fight COVID-19, cushion its impact and position New Zealand for recovery.	The Government will stabilise net core Crown debt as a percentage of GDP by the mid-2020s and then reduce it as conditions permit (subject to any significant shocks).
Operating balance	The Government will use fiscal policy to secure the economic recovery for New Zealand and reduce deficits over the forecast period as economic conditions allow.	The Government will run an operating balance consistent with meeting the long-term debt objective.
Expenses	Our intention is to ensure expenses are consistent with the operating balance objective.	The Government will ensure operating expenses support a responsible and proportionate role for the Government in maintaining a productive, sustainable and inclusive economy, consistent with the debt and operating balance objectives.
Revenue	Our intention is to ensure revenue is consistent with the operating balance objective.	The Government will ensure a progressive taxation system that is fair, balanced and promotes the long-term sustainability and productivity of the economy, consistent with the debt and operating balance objectives.
Net worth	Our intention is to use the Crown’s net worth to fight COVID-19, cushion its impact and position New Zealand for recovery. Significant risks will be transferred onto the Crown’s balance sheet through the response period.	The Government will use the Crown's net worth to maintain a productive, sustainable and inclusive economy, consistent with the debt and operating balance objectives.