

The Treasury

Advice on COVID-19 Response Information Release

December 2021

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Treasury Report: Replenishing the COVID-19 Response and Recovery Fund

Date:	2 September 2021	Report No:	T2021/2228
		File Number:	BM-2-1-2022

Action sought

	Action sought	Deadline
Minister of Finance (Hon Grant Robertson)	<p>Agree to a two-stage process for replenishing the COVID-19 Response and Recovery Fund (CRRF).</p> <p>Agree to revise the amounts included in the Imprest Supply (Second for 2021/22) Bill to accommodate the increase in the CRRF.</p> <p>Provide feedback on the attached draft Cabinet paper.</p>	3 September 2021

Contact for telephone discussion (if required)

Name	Position	Telephone	1st Contact
Gerald Lee	Senior Analyst, Budget Management	[39]	[35] ✓
Simon Duncan	Team Leader, Budget Management		

Minister's Office actions (if required)

Return the signed report to Treasury.

Note any feedback on the quality of the report

Enclosure: Yes (attached)

Treasury Report: Replenishing the COVID-19 Response and Recovery Fund

Purpose of Report

1. This report provides you with advice on replenishing the COVID-19 Response and Recovery Fund (CRRF).

Background

2. Last week, we provided you with advice on managing expected pressures on the CRRF as a result of the most recent COVID-19 resurgence [T2021/2177 and T2021/2188 refer]. In response to this advice, you:
 - agreed to refine the purpose and criteria for the CRRF towards meeting the direct costs of responding to any COVID-19 resurgences over the next year
 - indicated that you wanted to explore returning unused funding to the CRRF as part of providing additional headroom to manage COVID-19 related costs, and
 - requested further advice on replenishing the CRRF.

Costs of current resurgence

3. Since the beginning of the current resurgence on 18 August 2021, the Government has allocated just over \$2 billion of new funding from the CRRF, leaving a remaining balance as at 2 September 2021 of \$2.7 billion.
4. The largest areas of expenditure associated with the resurgence are the:
 - Wage Subsidy Scheme (WSS) which was originally estimated to cost \$2.1 billion for the first two-week payment period at Alert Level 4, comprised of \$1.4 billion of funding available in baselines and transfers from 2020/21, with \$700 million additional CRRF funding.
 - Resurgence Support Payment (RSP) which was originally estimated to cost up to \$600 million for the first two-week payment period at Alert Level 4, comprised of \$193 million of funding transferred from 2020/21 and \$407 million additional CRRF funding.
5. However, demand for these schemes has differed from initial predictions. High demand for the RSP led to a further \$300 million in CRRF funding being agreed on 27 August 2021, with the option for Joint Ministers to draw a further \$100 million if required. You will also receive advice tomorrow on further support for firms' ongoing non-wage cost pressures which could cost an additional \$700 million for grants or an uncertain amount for loans.
6. In contrast, demand for the WSS has been softer than expected and the cost of the first two-week payment period is likely to be lower than earlier estimates. This may leave a residual balance in the appropriation that can be used to manage future payments.

7. Although the trajectory of the current resurgence remains uncertain and costings are subject to change, we estimate that up to a further \$0.75 - \$1 billion of funding may need to be sought from the CRRF for the WSS over the next four weeks. This is based on a scenario where Auckland spends two weeks at Alert Level 4 while the rest of the country is in Alert Level 3, followed by two weeks of Alert Level 3 in Auckland and two weeks of Alert Level 2 in the rest of New Zealand. You will receive further advice tomorrow on detailed WSS scheme costs which incorporate data from the final day of applications for the first fortnightly payment. This paper will also seek additional funding from the CRRF for the next fortnightly payment.
8. Outside of the core economic support schemes, Treasury Vote teams are also aware of upcoming CRRF charges over the next few weeks totalling \$270 million if all agreed (although some of these proposals are likely outside the scope of the revised CRRF purpose and criteria, and not all relate to the current resurgence).
9. At the high-end, this would leave a projected balance in the CRRF of around \$1 billion by the end of the resurgence. However, there is significant uncertainty over this estimate.

Provisioning for future resurgences

Core economic support measures

10. We expect that a remaining balance of \$1 billion would be quickly exhausted in the event of a future resurgence of similar severity to the August outbreak.
11. As noted above, the largest items of expenditure associated with resurgences are the WSS and RSP. The initial funding required for these schemes in the event of a return to nationwide Alert Level 4 restrictions for two weeks would be substantially larger than the remaining CRRF.
12. Based on the costs of the two schemes in this resurgence so far, we consider that \$5 billion represents a reasonable buffer to cover the costs of economic support associated with a future outbreak similar to the current resurgence or multiple smaller outbreaks.

[33]

Fiscal and macroeconomic considerations

Fiscal headroom

16. We recently provided you with advice on available fiscal headroom in net core Crown debt that might allow for increased CRRF expenditure while remaining below the forecast track presented in the Budget Economic and Fiscal Update 2021 (BEFU 2021) [T2021/2229 refers].

[33]

Macroeconomic context

19. As part of recent advice on the economic strategy around COVID-19, we advised that macroeconomic considerations – including fiscal sustainability objectives – should be secondary when making decisions about your response to the current outbreak [T2021/2190 refers]. While there may be public communication benefits to remaining below the forecast debt track presented at BEFU 2021, this should not be a limiting factor if it becomes necessary to increase spending in order to support the health response, ensure compliance with public health measures, and enable individuals and businesses to cope at higher Alert Levels.
20. However, we also noted that supply constraints and inflationary pressures remain a risk once restrictions are eased, and current evidence suggests the economy should be well placed to bounce back. This means the potential macroeconomic impacts of further economic support measures (beyond those currently in place) should be considered and, at this stage, the CRRF should not be used purely to provide additional fiscal stimulus. This may change if the Alert Level 3 and 4 restrictions are prolonged and additional support for aggregate demand might be warranted, but there is still an opportunity cost of any spending that will limit your ability to progress other priorities.

Replenishing the CRRF

21. Based on the expected timing and potential quantum of COVID-19 related costs as well as the fiscal headroom outlined above, we recommend a two-stage process for replenishing the CRRF:
 - **Stage 1:** immediately increase the funding available in the CRRF by an additional \$10 billion.
 - **Stage 2:** re-consider the CRRF balance (including need for any further top-up) as part of the Half Year Economic and Fiscal Update (HYEFU) process.

Stage 1

22. Alongside the recent changes to the purpose and criteria for the CRRF, an immediate top-up will provide certainty to Ministers, agencies, and the public about how the fiscal impacts of COVID resurgences will be managed in the short-term. It would also provide a set envelope of funding within which new policy proposals can be prioritised (to the extent possible in resurgences).
23. We consider that an additional \$10 billion should provide sufficient funding to cover both the economic support needed for a further resurgence of similar severity to the current Auckland outbreak (or multiple smaller outbreaks), and key public health measures that may require additional funding over the next few months such as MIQ and vaccines. Based on current modelling (excluding the economic and fiscal impacts of the current resurgence), it also leaves you with fiscal headroom to increase spending further and still likely remain below the forecast track for net core Crown debt from BEFU 2021.
24. We suggest that you signal that \$3 billion of the top-up consists of previously identified unused funding in aggregate that you are returning to the CRRF from schemes such as the Small Business Cashflow Scheme and Business Finance Guarantee Scheme, (noting that this will still have a direct impact on the fiscal position). In our view, Cabinet agreement can be sought to return these funds without a formal reprioritisation process. The remaining \$7 billion will be a direct increase to the overall level of the CRRF, bringing the total to \$57 billion.

25. An increase of \$10 billion in the funding available in the CRRF would increase net core Crown debt by close to 2.5% of GDP by 2024/25. With the tightening of the CRRF criteria it is most likely that funding allocated will be focussed more on the near term, therefore will adversely impact on the operating balance before gains and losses (OBEGAL) over the next few years. The increase in funding available in the CRRF is unlikely to impact the timing of OBEGAL returning to surplus, although there could be a structural change in finance costs of approximately \$200 million per annum by 2024/25.

Stage 2

26. Through the HYEPU process, you will have the opportunity to re-consider the CRRF balance alongside updated economic and fiscal forecasts that incorporate the impact of the latest resurgence. This will allow you to take a holistic view of what level the CRRF and Budget allowances should be set at in order to fund key priorities in a manner consistent with your fiscal strategy. By this time, there will also likely be greater clarity on any further costs arising from the Reconnecting New Zealanders work programme, as well as any further reprioritisation options.

Imprest supply

27. If you agree to progress an immediate \$10 billion increase to the funding available in the CRRF, this will have implications for imprest supply. Some allowance for COVID-19 resurgence expenditure has been incorporated into the amounts in the draft Imprest Supply (Second for 2021/22) Bill (the Bill). However, if there were to be a significant increase in the CRRF impacting on the 2021/22 financial year, additional imprest supply may be required. This could be achieved by either:
- increasing the amount of imprest supply for operating expenses being sought in the current Bill by \$10 billion prior to its introduction to the House of Representatives on Wednesday 8 September 2021 (**recommended**),
 - increasing the amount of imprest supply for operating expenses being sought in the current Bill by \$5 billion prior to its introduction to the House of Representatives on Wednesday 8 September 2021 (on the assumption that a substantial portion of the new funding will impact future financial years), or
 - passing a third Imprest Supply Bill later in the financial year (as occurred in 2019/20).
28. We recommend taking a conservative approach to avoid the need for further Imprest Supply legislation. This would involve increasing the amount being sought in the Bill for operating expenses by \$10 billion. In this scenario, we suggest that Cabinet approval to the CRRF increase be sought on Monday 6 September so that it can be announced alongside the introduction of the Bill.

Alternative timing options

29. Our recommended approach to replenishing the CRRF is based on a desire to provide immediate certainty around the balance of the CRRF and align any announcements with the introduction of the Imprest Supply (Second for 2021/22) Bill.
30. However, there are other options available to if you want further time to consider the size of the increase to the CRRF. This could involve waiting to top-up the CRRF until the additional funding needs associated with the current outbreak are more certain in a few weeks, or until the size of the immediate funding requests associated with the Reconnecting New Zealanders papers in October 2021 are clearer. However, this carries the risk of further imprest supply being needed later in the year.

Next steps

31. If you agree with our recommended approach, attached is a draft Cabinet paper seeking agreement to an immediate \$10 billion increase to funding available in the CRRF. We seek your feedback on the paper so that it can be lodged on 3 September 2021 and considered by Cabinet on 6 September 2021. You could announce the increase in CRRF funding available alongside the introduction of the Imprest Supply (Second for 2021/22) Bill.
32. If you wish to take more time to consider the need for an increase to the CRRF, we can provide you with talking points to support an initial discussion at Cabinet on 6 September 2021.

Recommended Action

We recommend that you:

- a **agree** to a two-stage process for replenishing the CRRF:
 - Stage 1: immediate \$10 billion increase to the funding available in the CRRF.
 - Stage 2: re-consider the CRRF balance (including need for any further top-up) as part of the Half Year Economic and Fiscal Update (HYEFU) process.

Agree/disagree.

- b **agree** that the additional \$10 billion in funding available should comprise:
 - \$3 billion of previously allocated funding from the CRRF which is now unlikely to be used and can be returned to the CRRF, and
 - \$7 billion of new funding which will be added to the overall level of the CRRF;

Agree/disagree.

- c **agree** to increase the amount of imprest supply for operating expenses being sought in the Imprest Supply (Second for 2021/22) by \$10 billion prior to its introduction to the House of Representatives on Wednesday 8 September 2021;

Agree/disagree.

- d **provide** feedback on the attached draft Cabinet paper so that it can be lodged on 3 September 2021 and considered by Cabinet on 6 September 2021.

Simon Duncan
Team Leader, Budget Management

Hon Grant Robertson
Minister of Finance