New Zealand Budget 2019

Budget 2019 First Impressions

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- The Government has substantially increased its planned operational spending, against a backdrop of largely unchanged GDP and revenue forecasts.
- The biggest spending increases are in child poverty reduction and mental health, with relatively little focus on economic development.
- Projected surpluses are lower and net debt higher, while remaining within the Fiscal Responsibility Rules.
- Capital spending plans have been further delayed.
- We see downside risks to the Treasury's growth forecasts, which were unfazed by the weaker than expected starting point for the economy. This could have implications for the affordability of the Government's spending plans in later years.

June years	2019	2020	2021	2022	2023
OBEGAL ($bn)	3.5	1.3	2.1	4.7	6.1
Change since HYEFU	1.7	-2.8	-3.0	-2.9	-2.3
Net debt (% of GDP)	20.1	20.4	20.7	19.9	18.7
Change since HYEFU	-0.8	-0.3	0.6	0.9	1.3
Bond programme ($bn)	8	10	10	8	6
Change since HYEFU	0	2	2	1	-

The financial details of the "Wellbeing Budget" amounted to a substantial increase in operational spending over the next few years, against a backdrop of largely unchanged GDP and revenue forecasts. The net result is close to what we expected: smaller projected surpluses and more debt issuance over the coming years, while still squeaking within the Government's self-imposed fiscal responsibility rules.

Projected core Crown spending has been increased by $15bn over the next five years. The allowance for new spending in this year's Budget was increased to $3.8bn per year, with a $3.0bn allowance for next year's Budget (previously $2.4bn per year for both Budgets).

Of the five initiatives that were announced ahead of the Budget, the largest increase in spending went to addressing child poverty, followed by mental health. In contrast, areas such as building a productive nation and transitioning to a low-emissions economy received a relatively short shrift.

Surprisingly, this spending is expected to be met out of largely unchanged tax revenue projections, despite the weaker than expected starting point for the economy. The Treasury's forecasts assume that the shortfall in growth in the current fiscal year will be fully caught up in the next year. That forecast in turn partly relies on a catch-up of previous government under-spending, along with the additional spending that was announced today.

As a result of the increase in planned spending, cumulative surpluses over the next five years are expected to reach $17.7bn, down more than $9bn compared to the Half-Year Update last December.

In contrast to the operating balance, capital spending over the next five years has actually been reduced slightly, most likely reflecting ongoing delays that have pushed more planned spending beyond the five-year forecast horizon. Net capital spending in the current fiscal year is $1.3bn behind projections, and this shortfall is not expected to be fully caught up by 2023.

Net debt is forecast to rise initially, reaching 20.7% of GDP by 2021 before falling to 19.9% of GDP in 2022 – thereby fulfilling the Government's self-imposed target of reducing net debt to below 20% of GDP by that date. The long-term projections show net debt settling at just under 19% of GDP in later years. Despite the recently announced move to a more flexible target range of 15-25% of GDP in those

years, it appears that any commitment to make use of that flexibility will be left to future Budgets.

The bond programme was increased by $5bn over the next five years, with an additional $2bn of issuance in 2020 and 2021 and an additional $1bn in 2022. Inflation-linked bonds are expected to account for just $0.5bn out of the $10bn of issuance next year.

Implications

The increase in spending plans in today's Budget makes it a little more stimulatory than we expected – though that depends on that spending actually being delivered, in contrast to the persistent spending shortfalls of previous years.

We also believe that there are downside risks to the Treasury's GDP (and hence revenue) forecasts – in fact, the Treasury has actually slightly increased its nominal GDP forecasts in the later years, despite the weaker than expected starting point for the economy.

We will provide a fuller assessment of the Budget in our bulletin later today.

Market Reaction

There was limited reaction in the NZ dollar. The yield on longer term government bonds rose by 3 bps.

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