Economic Update – First Impressions.

14 May 2020

New Zealand Budget 2020.

- The Government has announced a $50bn economic recovery fund to tackle the Covid-19 pandemic, in addition to the $12.1bn package announced in March.
- The new spending that was announced today is heavily weighted towards supporting and creating jobs. The Government is aiming to return the unemployment rate to its current level of 4.2% within two years.
- Around $20bn of the package remains to be allocated within the next few years, although the fiscal projections assume that the full amount will be spent.
- Operating deficits will be close to 10% of GDP for each of the next three fiscal years.
- Government bond issuance is projected to be $190bn over the next five years, from $42bn previously. Net debt is expected to peak at over 53% of GDP from around 20% today.
- Today's announcement was more stimulatory than we expected, to the tune of around $25bn or nearly 8% of GDP. The difference largely occurs in the later years, affecting the speed of recovery rather than the depth of the downturn.
- With the Government providing more stimulus, there will be less for the RBNZ to do. This is therefore an upside surprise as far as our OCR forecast is concerned.

	2020	2021	2022	2023	2024
Economic (June years, %)					
Real GDP growth	-4.6	-1.0	8.6	4.6	3.6
Unemployment rate	8.3	7.6	5.7	5.2	4.8
CPI inflation	1.3	0.8	1.5	1.8	1.9
Fiscal (June years, %)					
Total Crown OBEGAL	-9.6	-10.1	-8.3	-4.7	-1.3
Net core Crown debt	30.2	44.0	49.8	53.6	53.6
Government bonds (June years, $ bn)					
Bond programme	25	60	40	35	30
Bonds on issue	90.2	139.1	179.1	198.4	213.0

Today's Budget delivered an economic support package that was even more massive than expected, an extraordinary response to extraordinary times. The Government has approved a $50bn fund for Covid-related response and recovery measures, in addition to the $12.1bn initial support package that was announced in March. While that $50bn does include some measures that had already been announced, such as increased funding for the wage subsidy scheme, it still amounts to an extra $40bn of stimulus over the next five years.

The Government has pledged to return the unemployment rate to its current level of 4.2% by June 2022, from an expected peak of 9.8% this year. That seems extremely ambitious, especially when most forecasts (including those of the Treasury) see the level of economic activity remaining below pre-Covid projections for many years to come.

With that goal in mind, the new spending initiatives announced today are heavily weighted towards supporting and creating jobs. The main initiatives include:

- An extension of the wage subsidy scheme for an additional eight weeks, for those firms that can show a 50% loss of revenue (previously 30%). Tourism and hospitality firms are the most likely to meet this threshold.

- An initial extra $3bn of infrastructure spending, and funding to build an extra 8,000 new homes. Further funding for both is likely in future Budgets.
- $1.6bn for trades and apprenticeship training.
- $1.1bn for jobs in environmental projects.
- An initial $400m tourism recovery fund.
- Maori and Pasifika recovery packages.

About $20bn of the fund remains to be allocated. The Finance Minister noted that this is spread over four years, and might not be allocated in the near future. However, the assumption is that the full amount will be spent.

In addition to the Covid package, the core parts of the Budget included a massive $5.6bn lift in healthcare funding, and sizeable increases for education, justice, defence, transport, community services and the arts.

The package will require a significant lift in Government borrowing over the coming years. The bond issuance programme has been expanded to $190bn over five years, compared to $42bn in the Half-Year Update in December. Net core Crown debt is expected to rise from around 20% currently to a peak of 53.6% of GDP, close to the record high that New Zealand reached in the early 1990s.

The Treasury's economic forecasts include a sharper downturn but a faster recovery compared to our forecasts. However, it should be noted that their forecasts are already dated: they were based on a total package of $35bn, whereas the full $62bn package was approved after the cut-off date for the Treasury's forecasts. (However, the fiscal forecasts incorporate the full $62bn).

Today's announcements are even more stimulatory than expected (at the cost of an even higher debt to GDP ratio). This will mean less requirement for the Reserve Bank to stimulate the economy, and is therefore an upside surprise for our OCR forecast.

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

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