2015 Budget

Taking the long view

- The 2015 Budget forecasts were much as expected, with low inflation weighing on revenue growth while allowances for new spending were unchanged.
- The operating balance is expected to scrape into surplus in 2015/16, but the profile of projected surpluses is looking increasingly slim.
- That's a particular concern for the later years of the projections, where we are less optimistic than the Treasury about the pace of economic growth as the Christchurch rebuild winds down.

Summary of Budget and Economic Forecasts

	2014	2015	2016	2017	2018	2019
	Actual	Forecast	Forecast	Forecast	Forecast	Forecast
Economic (March years, %)						
Real GDP growth	2.5	3.3	3.1	2.8	2.8	2.4
Unemployment rate	6.1	5.6	5.1	4.7	4.5	4.5
CPI inflation	1.5	0.2	1.4	2.1	2	2.1
Current account balance	-2.6	-4.1	-5.6	-4.9	-5.1	-5.3
Fiscal						
(June years, % of GDP)						
Total Crown OBEGAL	-1.3	-0.3	0.1	0.6	0.7	1.3
Net core Crown debt	25.6	25.7	26.3	25.5	24.4	22.9
(June years, $ billion)						
Core Crown revenue	67.3	71.9	74.9	78.9	83.5	87.4
Core Crown expenses	(71.5)	(73.1)	(74.9)	(77.1)	(80.8)	(83.4)

The 2015 Budget contained little in the way of surprises. As in the Half-Year Fiscal and Economic Update (HYEFU) last December, weaker than expected inflation has further eroded the tax revenue forecasts, which the government has largely taken on the chin through lower projected surpluses rather than reducing its plans for new spending. The operating balance is projected to return to surplus in the 2015/16 fiscal year, though the projected balance has continued to shrink compared to earlier forecasts and could easily be tipped into another year of deficit.

The government continues to highlight its "responsible" fiscal management. We'd agree with that assessment to the extent that the government has largely avoided the temptation to run fiscal policy in a pro-cyclical manner. The spending increases planned for the next two years are moderate, with a step-up in 2017/18 when the pace of economic growth is expected to be slowing. But we question whether the medium-term economic outlook is realistic enough, with ever-rising surpluses projected at a time when we expect the wind-down of the Christchurch rebuild to be a significant drag on the pace of growth. And that reignites our long-running question of what is being done to position the fiscal accounts to deal with longer-term challenges such as population aging. If the government were to achieve only a couple of slim surpluses before the balance started to deteriorate again, it would not reflect well on the structural position of the fiscal accounts.

On balance this is a more stimulative package than we expected on the day (notwithstanding the previously-announced measures on ACC levies and property taxation). The size of the new spending initiatives was even greater than in last year's election year Budget, and the offsetting savings measures – a new border levy and the removal of the $1000 kick-start for Kiwisaver – won't do much to dampen domestic demand. It's possible that the government chose to spend more because it could – remember that last year the Finance Minister sought advice from the Treasury on how much spending could be increased without provoking the Reserve Bank into raising interest rates. Today, the risks for interest rates if anything go in the opposite direction.

New policy initiatives

Many of the new policy initiatives covered in the Budget had already been well-signalled, including further chunky ACC levy cuts in 2015/16 and 2016/17, a tightening of capital gains tax rules around investor property, and more money to open up Crown-owned land for Auckland housing development.

The main new policy announcement was the Budget's flagship $790m Child Hardship Package, raising benefit rates for families with children, Working for Families payments, and childcare subsidies – while also raising the pressure on beneficiary parents to work.

The total amount of net new spending was unchanged from Budget 2014 and in line with the $1bn-a-year new operating allowance from the December HYEFU. But compared to Budget 2014 each side of the ledger has increased, with more spending ($6,168m of new spending initiatives over the next four years vs $5,652m last Budget) funded by reduced expenditure elsewhere. Expenditure reductions include the removal of the $1000 KiwiSaver 'kick-start' subsidy, which is estimated to save about $500m over the next four years, and a new customs and biosecurity levy, estimated to generate about $100m of revenue a year.

Economic forecasts

Since the December HYEFU, the Treasury has been surprised on the upside in terms of domestic economic activity, but on the downside for inflation. The new forecasts incorporate stronger than expected migration and house price inflation, the drop in oil prices since the half-year forecasts were put together, and interest rates that are likely to stay low for longer.

Over the next year or two the Treasury's forecasts are now fairly similar to our own, with GDP growth of a little above 3% expected over 2015/16. Where we continue to have questions is around the Treasury's forecasts in the outer years of the projection, as the Canterbury rebuild winds down. The growth forecasts hover around 2.8% through to 2017/2018, slowing to 2.4% in the last year. That strikes us as a very benign view of what a post-rebuild economic slowdown might look like. Indeed it's rather more optimistic than the Treasury's own forecasts six months ago, reflecting the more stimulatory interest rate backdrop.

That optimism suggests downside risks to the Treasury's revenue forecasts further down the track - in a context where forecasts for surpluses are already looking vulnerable. That vulnerability clearly emerged in the Treasury's economic risk scenarios. The upside scenario (featuring stronger net immigration) makes small surpluses a little larger, the downside scenario (greater weakness in the export environment) is enough to push a return to surplus out to 2018/2019.

Bond programme

The weaker fiscal position in the near term means a modest increase in the cash requirement compared to the December HYEFU. Gross bond issuance has been increased from $7bn to $8bn for the 2015/16 year, but remains unchanged at $7bn in each of the following three years.

Subject to market conditions, a new April 2033 nominal bond will be launched via syndication in the second half of this year. Inflation-indexed bonds will account for up to $2bn of the $8bn bond programme for the 2015/16 fiscal year.

Dominick Stephens
Chief Economist

Michael Gordon
Senior Economist

Westpac economics team contact details

Dominick Stephens, Chief Economist
+64 9 336 5671

Michael Gordon, Senior Economist
+64 9 336 5670

Felix Delbrück, Senior Economist
+64 9 336 5668

Satish Ranchhod, Senior Economist
+64 9 336 5669

Any questions email:
economics@westpac.co.nz

For email address changes contact:
WNZResearch@westpac.co.nz

Disclaimer

Things you should know: Each time someone visits our site, data is captured so that we can accurately evaluate the quality of our content and make improvements for you. We may at times use technology to capture data about you to help us to better understand you and your needs, including potentially for the purposes of assessing your individual reading habits and interests to allow us to provide suggestions regarding other reading material which may be suitable for you.

If you are located in Australia, this material and access to this website is provided to you solely for your own use and in your own capacity as a wholesale client of Westpac Institutional Bank being a division of Westpac Banking Corporation ABN 33 007 457 141 AFSL 233714 ('Westpac'). If you are located outside of Australia, this material and access to this website is provided to you as outlined below.

This material and this website contain general commentary only and does not constitute investment advice. Certain types of transactions, including those involving futures, options and high yield securities give rise to substantial risk and are not suitable for all investors. We recommend that you seek your own independent legal or financial advice before proceeding with any investment decision. This information has been prepared without taking account of your objectives, financial situation or needs. This material and this website may contain material provided by third parties. While such material is published with the necessary permission none of Westpac or its related entities accepts any responsibility for the accuracy or completeness of any such material. Although we have made every effort to ensure the information is free from error, none of Westpac or its related entities warrants the accuracy, adequacy or completeness of the information, or otherwise endorses it in any way. Except where contrary to law, Westpac and its related entities intend by this notice to exclude liability for the information. The information is subject to change without notice and none of Westpac or its related entities is under any obligation to update the information or correct any inaccuracy which may become apparent at a later date. The information contained in this material and this website does not constitute an offer, a solicitation of an offer, or an inducement to subscribe for, purchase or sell any financial instrument or to enter a legally binding contract. Past performance is not a reliable indicator of future performance. The forecasts given in this material and this website are predictive in character. Whilst every effort has been taken to ensure that the assumptions on which the forecasts are based are reasonable, the forecasts may be affected by incorrect assumptions or by known or unknown risks and uncertainties. The ultimate outcomes may differ substantially from these forecasts.

Transactions involving carbon give rise to substantial risk (including regulatory risk) and are not suitable for all investors. We recommend that you seek your own independent legal or financial advice before proceeding with any investment decision. This information has been prepared without taking account of your objectives, financial situation or needs. Statements setting out a concise description of the characteristics of carbon units, Australian carbon credit units and eligible international emissions units (respectively) are available at www.cleanenergyregulator.gov.au as mentioned in section 202 of the Clean Energy Act 2011, section 162 of the Carbon Credits (Carbon Farming Initiative) Act 2011 and section 61 of the Australian National Registry of Emissions Units Act 2011. You should consider each such statement in deciding whether to acquire, or to continue to hold, any carbon unit, Australian carbon credit unit or eligible international emissions unit.

Additional information if you are located outside of Australia

New Zealand: The current disclosure statement for the New Zealand division of Westpac Banking Corporation ABN 33 007 457 141 or Westpac New Zealand Limited can be obtained at the internet address www.westpac.co.nz. Westpac Institutional Bank products and services are provided by either Westpac Banking Corporation ABN 33 007 457 141 incorporated in Australia (New Zealand division) or Westpac New Zealand Limited. For further information please refer to the Product Disclosure Statement (available from your Relationship Manager) for any product for which a Product Disclosure Statement is required, or applicable customer agreement. Download the Westpac NZ QFE Group Financial Advisers Act 2008 Disclosure Statement at www.westpac.co.nz.

China, Hong Kong, Singapore and India: Westpac Singapore Branch holds a wholesale banking licence and is subject to supervision by the Monetary Authority of Singapore. Westpac Hong Kong Branch holds a banking license and is subject to supervision by the Hong Kong Monetary Authority. Westpac Hong Kong branch also holds a license issued by the Hong Kong Securities and Futures Commission (SFC) for Type 1 and Type 4 regulated activity.

Disclaimer continued overleaf.

Disclaimer continued

Westpac Shanghai and Beijing Branches hold banking licenses and are subject to supervision by the China Banking Regulatory Commission (CBRC). Westpac Mumbai Branch holds a banking license from Reserve Bank of India (RBI) and subject to regulation and supervision by the RBI.

U.K.: Westpac Banking Corporation is registered in England as a branch (branch number BR000106), and is authorised and regulated by the Australian Prudential Regulatory Authority in Australia. WBC is authorised in the United Kingdom by the Prudential Regulation Authority. WBC is subject to regulation by the Financial Conduct Authority and limited regulation by the Prudential Regulation Authority in the United Kingdom. Details about the extent of our regulation by the Prudential Regulation Authority are available from us on request. Westpac Europe Limited is a company registered in England (number 05660023) and is authorised by the Prudential Regulation Authority and regulated by the Financial Conduct Authority and the Prudential Regulation Authority. This material and this website and any information contained therein is directed at a) persons who have professional experience in matters relating to investments falling within Article 19(1) of the Financial Services Act 2000 (Financial Promotion) Order 2005 or (b) high net worth entities, and other persons to whom it may otherwise be lawfully communicated, falling within Article 49(1) of the Order (all such persons together being referred to as “relevant persons”). The investments to which this material and this website relates are only available to and any invitation, offer or agreement to subscribe, purchase or otherwise acquire such investments will be engaged in only with, relevant persons. Any person who is not a relevant person should not act or rely upon this material and this website or any of its contents. In the same way, the information contained in this material and this website is intended for “eligible counterparties” and “professional clients” as defined by the rules of the Financial Services Authority and is not intended for “retail clients”. With this in mind, Westpac expressly prohibits you from passing on the information in this material and this website to any third party. In particular this material and this website, website content and, in each case, any copies thereof may not be taken, transmitted or distributed, directly or indirectly into any restricted jurisdiction.

U.S.: Westpac operates in the United States of America as a federally licensed branch, regulated by the Office of the Comptroller of the Currency. Westpac is also registered with the US Commodity Futures Trading Commission (“CFTC”) as a Swap Dealer, but is neither registered as, or affiliated with, a Futures Commission Merchant registered with the US CFTC. Westpac Capital Markets, LLC (‘WCM’), a wholly-owned subsidiary of Westpac, is a broker-dealer registered under the U.S. Securities Exchange Act of 1934 (‘the Exchange Act’) and member of the Financial Industry Regulatory Authority (‘FINRA’). This communication is provided for distribution to U.S. institutional investors in reliance on the exemption from registration provided by Rule 15a-6 under the Exchange Act and is not subject to all of the independence and disclosure standards applicable to debt research reports prepared for retail investors in the United States. WCM is the U.S. distributor of this communication and accepts responsibility for the contents of this communication. If you would like to speak to someone regarding any security mentioned herein, please contact WCM on +1 212 389 1269. All disclaimers set out with respect to Westpac apply equally to WCM.

Investing in any non-U.S. securities or related financial instruments mentioned in this communication may present certain risks. The securities of non-U.S. issuers may not be registered with, or be subject to the regulations of, the SEC in the United States. Information on such non-U.S. securities or related financial instruments may be limited. Non-U.S. companies may not be subject to audit and reporting standards and regulatory requirements comparable to those in effect in the United States. The value of any investment or income from any securities or related derivative instruments denominated in a currency other than U.S. dollars is subject to exchange rate fluctuations that may have a positive or adverse effect on the value of or income from such securities or related derivative instruments.

The author of this communication is employed by Westpac and is not registered or qualified as a research analyst, representative, or associated person under the rules of FINRA, any other U.S. self-regulatory organisation, or the laws, rules or regulations of any State. Unless otherwise specifically stated, the views expressed herein are solely those of the author and may differ from the information, views or analysis expressed by Westpac and/or its affiliates.

For the purposes of Regulation AC only: Each analyst whose name appears in this report certifies that (1) the views expressed in this report accurately reflect the personal views of the analyst about any and all of the subject companies and their securities and (2) no part of the compensation of the analyst was, is, or will be, directly or indirectly related to the specific views or recommendations in this report.