



ECONOMIC BULLETIN

Review of New Zealand Budget 2024.



30 May 2024 | **Darren Gibbs**, Senior Economist | +64 9 367 3368 | +64 21 794 292 | darren.gibbs@westpac.co.nz

- Budget 2024 confirmed a weaker fiscal outlook than forecast in December. An OBEGAL deficit of 3.1% of GDP is forecast in the coming '24/25 year – larger than we had expected.
- Thereafter, very skinny allowances allow spending to fall as a proportion of GDP. As a result, the OBEGAL deficit declines, leading to a tiny surplus of 0.3% of GDP in '27/28.
- Given larger operating deficits and capital requirements, forecast NZGB issuance over the next 4 years has been raised by \$12bn, including a \$38bn programme in the '24/25 year. Higher short-term borrowings fund the remaining shortfall.
- NZDM has raised the caps on nominal bond lines to \$25bn from \$18bn previously, and notes that it does not expect to offer buybacks of the April 2025 bond ahead of maturity.
- Net core Crown debt is forecast to decline from 43.1% of GDP in '23/24 to 41.8% of GDP in '27/28, thus remaining above the Government's 20-40% long-term goal.
- We think that ratings agencies will remain comfortable with the outlook for the public finances given New Zealand's relatively low debt and strong governance institutions.
- The Treasury's estimate of the fiscal impulse implies that near-term fiscal policy settings are tightening less than estimated previously, but slightly more thereafter.
- Given current pressures on inflation, the RBNZ is likely to regard the reprofiling of the fiscal impulse as unhelpful (particularly in the current year), although we doubt this will be a game changer.
- The Treasury's economic forecasts are more optimistic than our own regarding inflation and near-term policy easing, allowing the Treasury to forecast an earlier recovery in growth. However, our forecasts of nominal GDP – and thus revenue are quite similar.
- Personal income tax cuts – which were exactly as campaigned on ahead of the election – were the centrepiece of the Budget 2024 policy announcements.
- We think that sustained spending restraint may well prove more difficult than assumed in Budget 2024. As a result, attainment of an OBEGAL surplus in '27/28 is far from certain.

Starting the slow grind back to surplus... but not quite yet.

In broad terms Budget 2024 provided no huge surprises, with the revised level of bond issuance in line with our sense of the midpoint of market expectations, albeit helped by additional short-term borrowing.

Markets were braced for a fiscal starting point that had worsened since the release of the Half-Year Economic and Fiscal Update (HYEFU), with the broad parameters of that deterioration laid out in the partial update that accompanied the Budget Policy Statement (BPS) in late March. At the same time, Minister of Finance Nicola Willis had made clear that Budget 2024 would set out a path back to an operating surplus – last seen in the '18/19 fiscal year – with promised tax cuts paid for by savings and other revenue initiatives. Budget 2024 begins that path, although the OBEGAL deficit in the coming '24/25 is forecast to be larger than the current year, in part reflecting the deterioration of the economy,

In this note we review the key fiscal metrics and what these mean for the Government's borrowing programme; the economic forecasts on which these forecasts are

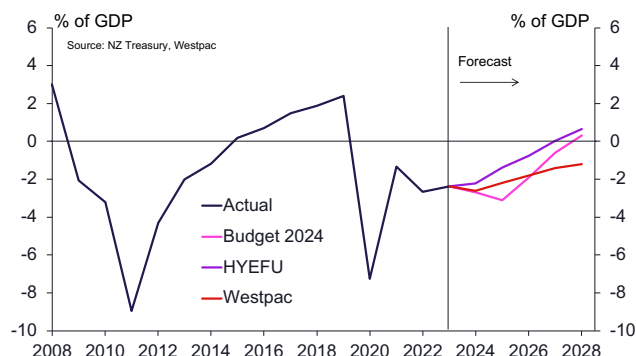
based; and how today's information might be interpreted by the RBNZ. We also note some of the key policy announcements that were made (or confirmed) in Budget 2024.

OBEGAL deficit to slowly improve from a worse starting point.

Table 1 sets out the key fiscal metrics revealed in Budget 2024, comparing these to the forecasts made in the HYEFU and to our own forecasts. An OBEGAL deficit of \$11.1bn is now forecast for the current '23/24 fiscal year, compared to \$9.3bn in the HYEFU (2.6% of GDP). The Government has set itself a smaller operating spending allowance for the coming year of just \$3.2bn. Even so, a forecast OBEGAL deficit of \$13.3bn (3.1% of GDP) in '24/25 is still larger than we had expected, reflecting both higher than expected spending and lower than expected revenue. Thereafter, the Government assumes very skinny operating allowances of just \$2.4bn in subsequent years. As a result, tight control of government spending – which is forecast to decline by over 2ppts of GDP – and a gradual pickup in revenues is expected to drive a gradual but sustained improvement in the fiscal position. Budget 2024 forecasts a deficit of \$8.5bn in '25/26, reducing thereafter until a tiny surplus of \$1.5bn is achieved in

'27/28. Compared with the HYEFU, Budget 2024 foresees a cumulative increase in the OBEGAL deficit of about \$17bn over the period through to '27/28.

Operating balance (OBEGAL), % of GDP



The economic forecasts on which these fiscal forecasts are based are discussed further below. However, in summary, the Treasury's forecasts for revenue are quite close to our own, reflecting the fact that the Treasury's forecasts for nominal GDP growth are also similar (although as discussed further below, the composition of that growth – real versus inflation – differs). The more significant risk that we see the Budget 2024 forecasts is that associated with the pressures on public spending

Table 1: Key Fiscal Metrics

	22/23	23/24f	24/25f	25/26f	26/27f	27/28f
Total spending \$bn						
Budget 2024	162	176	181	185	189	194
HYEFU	162	176	181	188	194	199
Westpac	162	176	179	185	193	202
Total revenue \$bn						
Budget 2024	153	165	168	177	187	196
HYEFU	153	167	175	185	194	204
Westpac	153	165	170	178	187	196
OBEGAL \$bn*						
Budget 2024	-9.4	-11.1	-13.3	-8.5	-3.1	1.5
HYEFU	-9.4	-9.3	-6.1	-3.5	0.1	3.4
Westpac	-9.4	-10.9	-9.2	-8.1	-6.4	-6.2
OBEGAL % of GDP*						
Budget 2024	-2.4	-2.7	-3.1	-1.9	-0.6	0.3
HYEFU	-2.4	-2.2	-1.4	-0.7	0.0	0.7
Westpac	-2.4	-2.6	-2.1	-1.8	-1.4	-1.3
Net core Crown Debt (% of GDP)						
Budget 2024	39.3	43.1	43.5	43.0	43.3	41.8
HYEFU	39.2	43.5	42.3	40.7	39.9	37.6
Westpac	39.3	44.6	44.6	44.6	45.2	44.9

* ex minority interests

Source: NZ Treasury, Westpac

that are likely to be associated with recent rapid population growth. As we wrote in our recent [Economic Overview](#), we think that maintaining such tight spending control over the entire period will be challenging. Therefore, our forecasts for spending in the final two years of the forecast period are materially higher than those in Budget 2024, so that we continue to foresee the OBEGAL balance remaining in deficit.

Bigger deficits mean more bonds.

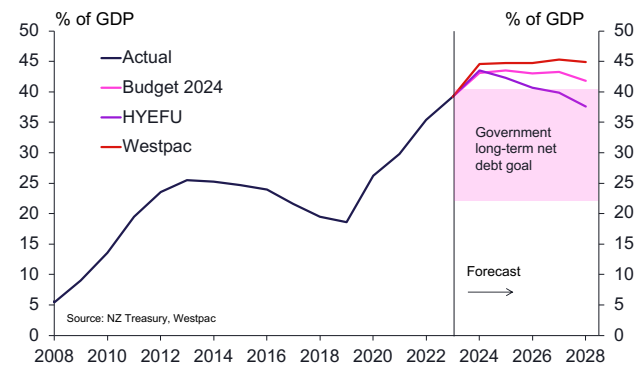
The deterioration in the underlying fiscal situation has necessitated a further increase in the Government's forecast borrowing programme (see [Table 2](#)). The funding requirement for the coming fiscal year ('24/25) has been revised up \$2bn from the HYEFU forecast to \$38bn, while the cumulative increase in the programme across the four years to 2027/28 has been revised up by \$12bn to \$164bn. Given upcoming maturities and repurchases associated with the \$5bn per year winding down of the RBNZ's Large Scale Asset Purchase programme (LSAP), the revised bond programme implies a cumulative \$68bn of net bond issuance.

According to NZ Debt Management (NZDM), short-term borrowings (Treasury Bills and Euro-Commercial Paper) at the end of '23/24 are forecast to be \$18bn. These borrowings are expected to decline to \$13bn from '24/25 onwards, although NZDM notes that a flexible approach will be taken to borrowings intra-year. The assumed long-term average level of short-term borrowings is greater than usual, thus helping to fund the circa \$17bn cumulative deterioration in the underlying fiscal position. NZDM notes that the upcoming tap syndication of the 15 May 2028 bond may prefund part of the '24/25 programme. Subject to market conditions NZDM expects three nominal bond syndications in '24/25 – two tap syndications of existing lines and one new bond line. Individual bond line caps have been raised to \$25bn from \$18bn. Gross issuance of inflation-indexed bonds is expected to be less than \$1bn. Meanwhile, NZDM says that buybacks of the 15 April 2025 bond are unlikely to be offered ahead of that bond's maturity.

Given the additional borrowing requirement, net core Crown debt is forecast to remain above the Government's new long-term goal of 20-40% of GDP though out the forecast period. From an estimated 43.1% of GDP in the current year, the Government's favoured debt measure is expected to decline only slowly to 41.8% of GDP in '27/28.

International credit ratings have remained relatively sanguine about New Zealand in recent years, noting still-low debt levels (as low as many AAA rated countries and very low compared to many AA+ rated countries), New Zealand's strong governance institutions, and forecasts pointing to an improvement in the fiscal position over time. So while Budget 2024 presents a deterioration in the fiscal outlook compared with the HYEFU, we expect that the rating agencies will give the new Government the benefit of the doubt and assume that it will deliver the declining trajectory for the deficit that's portrayed in the updated forecasts.

Net core Crown debt, % of GDP



Less near-term help for the RBNZ.

The discussion in the May *Monetary Policy Statement* (MPS) suggested that the RBNZ was predisposed to assess the fiscal stance in Budget 2024 as slightly less disinflationary than forecast in the HYEFU, and the information in today's Budget perhaps explains why.

A rough proxy of the impact of fiscal policy on aggregate demand can be obtained from the Treasury's estimate of the Total Fiscal Impulse, which is set out in [Table 3](#). The TFI is a cash-based measure of fiscal outlays and revenues, that adjusts for some items that do not directly affect aggregate demand (such as defence spending on equipment). The TFI measures the change in the fiscal stance rather whether the fiscal stance is expansionary or contractionary in an outright sense. It is important to emphasise that the TFI only provides an indication of the first-round impact of changes in discretionary fiscal policy. Budget decisions – both financial and non-financial – will also have an economic impact to the extent that they change behaviour, including on the

Table 2: NZ Government Bond Programme (\$bn)

	23/24f	24/25f	25/26f	26/27f	27/28f	Cumulative
Budget 2024	38	38	36	32	20	164
HYEFU	38	36	34	28	16	152
Difference	0	2	2	4	4	12

Source: NZ Treasury, Westpac

Table 3: Fiscal Impulse (% of Nominal Potential GDP)

	22/23	23/24f	24/25f	25/26f	26/27f	27/28f	Cumulative (23/24-27/28)
Budget 2024	-1.27	1.53	0.33	-1.91	-0.92	-2.07	-3.04
HYEFU	-1.28	2.64	-2.37	-1.58	-0.79	-1.52	-3.62
Difference	0.01	-1.11	2.70	-0.33	-0.13	-0.55	0.58

Source: NZ Treasury, Westpac

supply-side of the economy. And how the economy reacts to a given fiscal impulse – the fiscal multiplier – will depend on factors such as the state of the economic cycle.

The updated TFI estimates imply that the overall degree of looming fiscal restraint is modestly less than forecast in the HYEFU. However, the profile of that restraint is somewhat different to that estimated previously. The fiscal stance over the past year has been less expansionary than previously estimated, and the stance over the coming year – probably of greatest interest to the RBNZ given current domestic inflation pressures – is no longer estimated to be significantly tighter. The stance in '25/26 and subsequent years is now forecast to be slightly tighter than estimated in the HYEFU.

It is worth noting that the RBNZ’s view regarding the fiscal policy stance seems not to greatly take account of the Treasury’s TFI indicator. In recent years, the RBNZ has tended to focus simply on a measure of government spending (consumption plus non-market investment) as a proportion of trend GDP – a measure constructed by the RBNZ that is hard to replicate using figures provided by the Treasury – even though a lack of tax rate indexation has meant additional fiscal tightening due to fiscal drag. Given the tax changes announced in Budget 2024 (more detail on these below), the RBNZ will need to factor the extent to which they will provide a boost to consumer spending, offsetting the impact of the spending cuts confirmed in the Budget. As we noted in our preview, it is possible that well-foreshadowed tax cuts may already be influencing consumer behaviour to some degree, just as well foreshadowed cuts to government spending are likely impacting high frequency spending and confidence indicators too.

The RBNZ will formally incorporate Budget 2024 into its projections at the August MPS meeting, although comments on the impact of the Budget on the monetary policy outlook can be expected to be discussed at the July OCR review (and feature in the record of that meeting). Key judgments – such as the proportion of tax cuts that may be spent, rather than saved – will necessarily be made tentatively at first and refined as data on actual behaviour is observed. For now, our running assumption is that the RBNZ will regard Budget 2024 as somewhat unhelpful, as seemed to already be the case in the May MPS. However, regardless of how

their analysis eventually falls, we would be surprised if the RBNZ were to regard Budget 2024 as a “game changer” for monetary policy. Much will depend on how indicators of consumer and business confidence and inflation expectations evolve as the tax cuts hit.

Near-term economic forecasts downgraded as expected.

Turning to more of the detail, the key economic assumptions underpinning the fiscal outlook depicted in Budget 2024 are set out in Table 4, comparing these with the assumptions made in the HYEFU and Westpac’s own forecasts.

The Treasury’s forecasts for near-term growth in the economy have been downgraded substantially since the HYEFU and are now comparable to our own. However, the Treasury forecasts a quicker pick-up in the economy over the coming two fiscal years. This reflects the Treasury’s forecasts for inflation and monetary policy which appear notably more optimistic than our own forecasts. For example, the Treasury’s forecasts for the 90-day bill rate in June next year implies around 100bps of monetary policy easing over the period, compared to the 50bp of cuts in our own forecasts. However, other than in '25/26, the Treasury’s forecasts for nominal GDP growth are similar to our own, albeit we see a less favourable growth/inflation mix in the near term. It is worth noting that the Treasury assumes lower interest rates across the full forecast period than our own forecasts. As a result, our forecasts imply higher debt financing costs, adding further upside risk on the spending side of the Treasury forecasts.

Real GDP growth, annual average June year

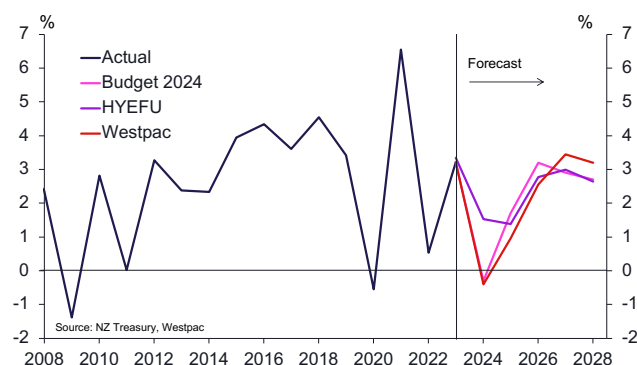


Table 4: Key Economic Assumptions (June years)

	22/23	23/24f	24/25f	25/26f	26/27f	27/28f
Real GDP growth (ann. avg.)						
Budget 2024	3.0	-0.3	1.7	3.2	2.9	2.7
HYEFU	3.2	1.5	1.5	2.8	3.0	2.7
Westpac	3.0	-0.3	0.9	2.6	3.4	3.2
Nominal GDP growth (ann. avg.)						
Budget 2024	8.7	4.4	4.2	5.6	5.3	5.0
HYEFU	8.9	6.1	4.7	5.4	5.4	5.0
Westpac	8.7	4.5	3.9	4.2	5.5	4.9
Unemployment (June qtr)						
Budget 2024	3.6	4.5	5.2	4.8	4.5	4.4
HYEFU	3.6	4.5	5.2	4.8	4.6	4.4
Westpac	3.6	4.6	5.4	5.1	4.4	4.1
CPI inflation (ann %)						
Budget 2024	6.0	3.4	2.2	2.0	2.0	2.0
HYEFU	6.0	4.1	2.5	2.2	2.0	2.0
Westpac	6.0	3.7	2.4	2.1	2.3	2.3
90-day rate (June qtr)						
Budget 2024	5.6	5.7	4.5	3.5	2.9	2.5
HYEFU	5.6	5.7	4.9	3.6	2.9	2.6
Westpac	5.6	5.6	5.0	4.0	3.9	3.9
10-yr bond rate (June qtr)						
Budget 2024	4.3	4.6	4.4	4.2	4.1	4.0
HYEFU	4.3	5.1	4.9	4.7	4.6	4.4
Westpac	4.3	5.0	4.7	4.4	4.4	4.4

Source: NZ Treasury, Westpac

Key Budget Policy Initiatives.

A key point of interest for many people in today's Budget 2024 announcement was the final configuration of the tax cuts. As expected, these have taken the form of a lift in income tax thresholds (effective from 31 July), costing \$9.8bn over the next four years:

- The \$14,000 threshold (17.5% marginal rate) has been lifted to \$15,600;
- The \$48,000 threshold (30% marginal rate) has been lifted to \$53,500; and
- The \$70,000 threshold (33% marginal rate) has been lifted to \$78,100.

These new thresholds were exactly as campaigned on by the National Party ahead of the election.

As far as spending is concerned, the Government also announced the follow key initiatives (some of which had been foreshadowed ahead of Budget 2024):

- \$3.4bn for hospital and speciality services and \$2.1bn for primary health care;

- \$1.8bn for Pharmac to purchase medicines;
- \$1.5bn to build schools;
- \$1.9bn for more frontline Corrections officers;
- \$0.4bn to support frontline policing;
- \$1.0bn increase to the National Land Transport Fund to accelerate priority projects.

CONTACT

Westpac Economics Team | westpac.co.nz/economics | economics@westpac.co.nz

Kelly Eckhold, Chief Economist | +64 9 348 9382 | +64 21 786 758 | kelly.eckhold@westpac.co.nz

Satish Ranchhod, Senior Economist | +64 9 336 5668 | +64 21 710 852 | satish.ranchhod@westpac.co.nz

Darren Gibbs, Senior Economist | +64 9 367 3368 | +64 21 794 292 | darren.gibbs@westpac.co.nz

Michael Gordon, Senior Economist | +64 9 336 5670 | +64 21 749 506 | michael.gordon@westpac.co.nz

Paul Clark, Industry Economist | +64 9 336 5656 | +64 21 713 704 | paul.clark@westpac.co.nz

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