



ECONOMIC BULLETIN

New Zealand Government Budget 2026.



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Moving closer to the promised land of fiscal balance

- Budget 2026 unexpectedly revealed a relatively robust fiscal outlook as the near-term impacts of the Iran war are offset by a tax-rich growth outlook from 2027/28.
- Following a small downward revision to the current year's forecast deficit, an OBEGALx deficit of \$11.4bn is forecast in the 2026/27 year, up from \$10.4bn in the HYEPU.
- The cumulative OBEGALx deficit in the four years to 2029/30 is around \$7bn smaller than in the HYEPU, with a not so wafer-thin surplus of \$2.6bn forecast for 2028/29 and \$6.1bn for 2029/30.
- Spending is forecast to be under control reflecting tight operating allowances, while the revenue outlook benefits from the assumption of a tax-rich growth outlook.
- The bond program is much smaller than expected - \$6 billion smaller over the forecast horizon with short term borrowings for the current year also cut \$3 billion. Markets and credit ratings agencies should cheer this outcome.
- Subject to market conditions, NZDM expects to establish a syndication for a new May 2038 bond by the end of calendar 2026. Up to \$1 billion of Inflation Indexed bonds are expected in '26/27.
- Net core Crown debt is forecast to increase from an estimated 42.4% of GDP in 2025/26 to a peak of 46.1% of GDP in 2027/28, before declining modestly in 2029/30.
- We don't expect the RBNZ will be fazed by the fiscal outlook. Government spending as a % of GDP is set to be solidly declining.
- There are possibly downside risks to the fiscal outlook given the tax-rich element of the outlook.
- Key policy initiatives announced for the first time today include a new prudential levy on a range of financial sector entities that is expected to raise \$209 million over the forecast horizon.
- The Treasury will need to publish a pre-election update, likely in early October. Pre-election fiscal manifestos from the major parties will also appear by that time.

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 fiscal 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 2026.

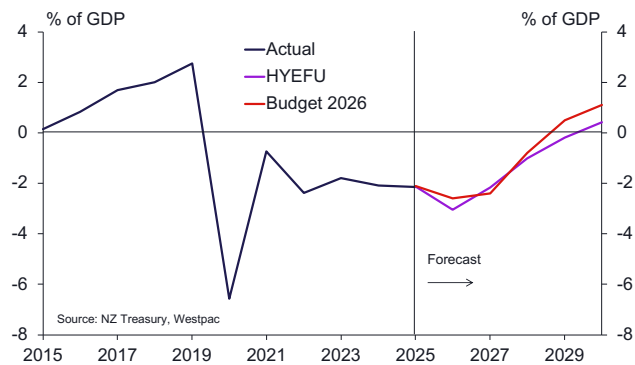
An earlier than expected return to surplus.

Table 1 sets out the key fiscal metrics in Budget 2026, comparing these to the forecasts made in the HYEPU and to our own recently updated forecasts.

An OBEGALx deficit of \$11.9bn is now forecast for the current 2025/26 fiscal year, compared to \$13.2bn in the HYEPU. That's largely due to lower-than-expected spending to date, as detailed in the fiscal accounts for the 9 months to March.

Moving forward, as announced prior to the Budget, the operating allowance for new operating spending in the coming fiscal year has been set at a very tight \$2.1bn a year (albeit up from an even skinnier \$1.3bn in Budget 2025). Thereafter, the operating allowance for future Budgets remains at \$2.4bn a year.

Operating balance (OBEGALx), % of GDP



Given the deterioration in the near-term economic outlook, the Treasury forecasts an OBEGALx deficit of \$11.4bn (2.4% of GDP) in 2026/27, compared to the \$10.4bn deficit forecast in the HYEFU. Beyond this though,

a set of relatively tax-rich economic forecasts and restrained spending growth drive a faster improvement in the operating balance compared to the HYEFU forecasts. Notably, the OBEGALx is projected to return to a surplus of \$2.6bn (0.5% of GDP) in 2028/29, a year earlier than in the HYEFU projections (and a year earlier than we thought). The traditional OBEGAL measure (which doesn't exclude ACC costs) returns to surplus a year later.

The Budget forecasts of core Crown revenue are higher across every year compared to the HYEFU, reflecting a higher level of nominal GDP and hence a larger tax base in dollar terms. These revenue forecasts were broadly in line with what we expected.

The surprise relative to our forecasts is that the core Crown spending projections were largely unchanged from the HYEFU. New spending initiatives are front-loaded to some degree, with savings found in the later years. With faster growth in the nominal economy, this means that government spending as a share of GDP declines faster than previously expected. We think that spending will ultimately prove to be higher than this in the later years, as it will be difficult for future governments to maintain this degree of spending discipline for this long.

Table 1: Key Fiscal Metrics

	24/25	25/26f	26/27f	27/28f	28/29f	29/30f
Core Crown spending \$bn						
Budget 2026	142	147	155	159	163	168
HYEFU	142	149	153	158	163	168
Westpac	142	148	155	161	169	176
Core Crown revenue \$bn						
Budget 2026	134	138	146	156	166	174
HYEFU	134	137	145	153	162	171
Westpac	134	137	144	155	166	177
OBEGALx \$bn*						
Budget 2026	-9.3	-11.9	-11.4	-4.3	2.6	6.1
HYEFU	-9.3	-13.9	-10.4	-5.1	-0.9	2.3
Westpac	-9.3	-13.2	-12.7	-7.6	-3.1	0.1
OBEGALx % of GDP*						
Budget 2026	-2.1	-2.6	-2.4	-0.8	0.5	1.1
HYEFU	-2.1	-3.0	-2.2	-1.0	-0.2	0.4
Westpac	-2.1	-2.9	-2.7	-1.5	-0.6	0.0
OBEGAL % of GDP*						
Budget 2026	-3.2	-3.3	-3.0	-1.5	-0.1	0.5
HYEFU	-3.2	-3.7	-2.7	-1.5	-0.6	0.0
Westpac	-3.2	-3.6	-3.2	-2.0	-1.0	-0.4
Net core Crown Debt (% of GDP)						
Budget 2026	41.9	42.4	45.6	46.1	45.6	44.4
HYEFU	41.8	43.3	46.0	46.9	46.9	46.1
Westpac	41.9	43.2	46.5	47.2	46.9	46.0

* ex minority interests, OBEGALx excludes ACC spending and revenues.

Source: NZ Treasury, Westpac

Table 2: NZ Government financing requirement (\$bn)

	24/25	25/26f	26/27f	27/28f	28/29f	29/30f
Budget 2026	42.6	35.0	34.0	32.0	30.0	28.0
HYEFU	42.6	35.0	34.0	34.0	32.0	30.0
Difference	0.0	0.0	0.0	-2.0	-2.0	-2.0

Source: NZ Treasury

It is worth emphasising that the error bounds around any fiscal forecast are large, especially beyond the near term, as small differences in assumptions can quickly compound to drive vastly different outcomes. For example, the Treasury’s analysis has shown that the historical 90% confidence interval around a five-year ahead forecast for revenue equates to a whopping ±\$20bn.

On that score, as usual the Treasury also published some alternative scenarios to illustrate how the fiscal outlook might evolve if the economy turns out to be stronger or weaker than the baseline economic forecast (which we discuss later in this note). In the upside scenario, oil prices retreat faster and settle at a lower level than in the central forecasts, households look through the temporary shock and maintain spending levels by dissaving, and a stronger rebound in the terms of trade boosts business profits and investment. In this scenario, the OBEGALx improves at a quicker pace, but still doesn’t return to surplus until 2028/29.

In the downside scenario the Middle East conflict is more protracted, household spending and the terms of trade are weaker, and higher inflation prompts an earlier tightening by the RBNZ. The result is a cumulative \$17bn reduction in nominal GDP over the forecast period, leading to larger operating deficits in the next three years, though still returning to a narrow surplus in 2028/29.

Regarding capital spending, as the Prime Minister announced ahead of the Budget, the net allowance for new capital spending in 2026/27 was set at \$5.7bn, up from the \$3.5bn assumption used in the HYEFU. In subsequent years the allowance for new capital spending has been maintained at \$3.5bn for Budget 2027 and Budget 2028, but has been increased to \$5.0bn for Budget 2029. We have been expecting an increase in capital spending at some point, with the Government’s Defence Capability Plan unlikely to be accommodated by the existing pool of as-yet unallocated spending. This is especially so given the pressures to invest elsewhere in the economy, including in education and transport infrastructure.

Forecast bond issuance unexpectedly reduced from 2028 onwards.

The relatively robust nominal growth outlook means that the Treasury sees a relatively “revenue rich” outlook

from 2028 onwards. This has allowed the government to bring forward by one year when they anticipate a OBEGALx surplus and correspondingly lower borrowing requirements. (see Table 2). The forecast bond programme in 2026/27 is unchanged and reduced by \$2 billion in 2027/28 onwards. Given upcoming maturities and repurchases associated with the winding down of the RBNZ’s Large Scale Asset Purchase programme (LSAP), the revised bond programme implies a cumulative \$46.5 billion of net bond issuance over the next four years.

Additionally, the relatively robust fiscal outlook is allowing a reduction in short term funding. The short-term financing program has been reduced by \$3 billion for the 2026/27 year. The composition of short-term borrowing will reflect a minimum of \$3 billion in ECP and \$3 billion of NZ Treasury bills.

The NZDMO plans a syndication of a new May 2038 nominal bond before the end of the 2026 calendar year. Less than \$1 billion of inflation indexed bonds are expected to be issued in the 2026/27 financial year.

Given the borrowing requirement, net core Crown debt is forecast to remain above the Government’s long-term goal of 20-40% of GDP throughout the forecast period. However, the relatively robust fiscal projections, including the bringing forward of the return to surplus by a year means that net debt is not expected to peak as high as expected. Net debt now peaks at just over 46% of GDP and falls after the 2027/28 year. We anticipate credit ratings agencies would welcome these projections and may take more time before considering a downgrade of the New Zealand Sovereign credit rating.

Net core Crown debt, % of GDP

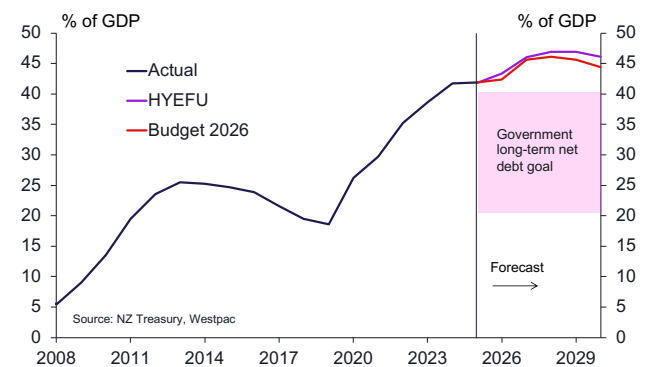


Table 3: Fiscal Impulse (% of nominal potential GDP)

	24/25	25/26f	26/27f	27/28f	28/29f	29/30f	Cumulative (25/26-29/30)
Budget 2026	-0.34	0.11	1.07	-2.01	-1.31	-0.90	-3.04
HYEFU	-0.35	1.32	-0.45	-1.82	-0.95	-0.86	-2.76
Difference	0.01	-1.21	1.52	-0.19	-0.36	-0.04	-0.28

Source: NZ Treasury

Budget unlikely to feature prominently in current RBNZ deliberations.

In judging the impact of fiscal policy, the RBNZ tends to focus on developments in Government spending as a share of GDP, which as noted is expected to decline over time. A more complete proxy of the first-round impact of fiscal policy on aggregate demand can be obtained from the Treasury's estimate of the Total Fiscal Impulse (TFI), which is set out in Table 3. The TFI is a cash-based measure of both fiscal outlays and revenues, that adjusts for some items that do not directly affect aggregate demand (such as defence spending on imported equipment). The Treasury's updated TFI estimates imply that fiscal policy had a smaller than previously expected positive impact on growth in 2025/26 that will unwind in the 2026/27 fiscal year. This reflects capital spending planned for 2026 which is now expected in the coming year. After that the Budget envisages that fiscal policy will have a contractionary impact on growth from 2027. We doubt these forecasts will change the RBNZ's views much given that government spending as a proportion of GDP is expected to decline.

Near-term economic forecasts downgraded as expected.

The key economic assumptions used by the Treasury to generate the baseline fiscal outlook are set out in Table 4. As the Minister of Finance signalled ahead of the Budget, the Iran conflict prompted a late re-write of what would have otherwise been a more favourable set of economic forecasts. Instead, the surge in world oil prices has led to a downgrade of the Treasury's GDP growth forecasts for the near term compared to the HYEFU, with a partial catch-up over the medium term once oil prices recede again. The unemployment rate is expected to peak at 5.5% this year and takes longer to decline than was assumed in the HYEFU.

While the level of real GDP is lower than previously assumed over the forecast horizon, the Treasury has upgraded its forecasts of nominal GDP – which is what matters more for their revenue projections. The Treasury assumes that the immediate spike in inflation will be only partially unwound in the future, i.e. there is a degree of second-round inflation that leaves the domestic price level permanently higher than before. That in turn leads

to higher revenue from GST, corporate tax and income tax (aided by fiscal drag as more workers are dragged into higher income tax brackets).

As always, there is a range of risks around the economic assumptions that underpin the fiscal forecasts. The obvious one is the uncertainty around how the Iran conflict plays out, including the impact on oil prices and the effects on global prices and trading partner growth. The Treasury's oil price assumptions are based on spot and futures prices as of 21 April (when the central forecast was finalised), which imply that oil prices have passed their peak and will moderate to around \$77/bbl by mid-2027. The current futures price track is higher than this, though it still implies a substantial fall in oil prices over the year ahead.

This slightly dated oil price assumption may explain the Treasury's relatively benign inflation forecasts compared to our own. Annual inflation is forecast to peak at 4.0% in the June quarter this year, easing back over the following quarters and reaching a temporary low of 1.6% in mid-2027 as fuel prices fall back. We're expecting both a higher peak in inflation in the near term and more lingering second-round effects (which actually gives us higher nominal GDP forecasts than the Treasury).

However, a different inflation outlook implies a different monetary policy response. The Budget assumes that the 90-day bank bill rate remains at just 2.8% in the June 2027 quarter, compared to around 2.5% today. This implies that RBNZ policy tightening begins almost a year later than in the RBNZ's own projections from yesterday's *Monetary Policy Statement*. Had the Treasury assumed an earlier tightening in line with the RBNZ's projections (and market expectations), both their real and nominal GDP forecasts would presumably be lower.

The Treasury's nominal GDP forecasts are also boosted a higher assumed path for the terms of trade, beyond the temporary spike in imported fuel prices. This reflects a combination of ongoing strength in export commodity prices, along with a lower assumed import price trend relative to the HYEFU. We think there's a risk that we could end up with more imported inflation than assumed – if the oil shock leads to a permanent lift in the domestic price level, it should presumably have a similar impact on the global price level.

Table 4: Key Economic Assumptions (June years)

	24/25	25/26f	26/27f	27/28f	28/29f	29/30f
Real GDP growth (ann. avg.)						
Budget 2026	-1.1	1.2	2.3	3.2	2.7	2.5
HYEFU	-1.1	1.7	3.4	2.6	2.5	2.5
Westpac	-1.1	1.2	1.8	3.2	3.7	3.2
Nominal GDP growth (ann. avg.)						
Budget 2026	3.4	4.0	5.0	6.1	5.2	4.6
HYEFU	3.8	4.2	5.4	4.9	4.8	4.7
Westpac	3.4	4.4	5.2	6.3	6.3	5.7
Unemployment (June qtr)						
Budget 2026	5.2	5.5	5.0	4.5	4.4	4.3
HYEFU	5.2	5.3	4.8	4.6	4.5	4.3
Westpac	5.2	5.4	5.3	4.6	4.2	4.0
CPI inflation (ann %)						
Budget 2026	2.7	4.0	1.6	2.1	2.1	2.0
HYEFU	2.7	2.4	2.2	2.1	2.0	2.0
Westpac	2.7	4.4	2.1	1.7	2.5	2.6
90-day rate (June qtr)						
Budget 2026	3.4	2.5	2.8	3.1	3.3	3.3
HYEFU	3.4	2.1	2.0	2.1	2.3	2.5
Westpac	3.4	2.5	4.0	4.5	4.1	4.1
10-yr bond rate (June qtr)						
Budget 2026	4.6	4.6	4.5	4.5	4.5	4.5
HYEFU	4.6	4.0	4.0	4.1	4.2	4.3
Westpac	4.6	4.9	5.1	5.1	5.1	5.1

Source: NZ Treasury, Westpac

Key Budget policy initiatives.

Finally, turning to the micro side of the Budget, which will be more important to many households and businesses, the Government announced the following policy initiatives:

- **Prudential levy on the financial industry:** The Government is implementing a new levy on deposit takers, insurers and financial market infrastructure providers. This is expected to raise \$209m in the next four years.
- **Defence:** Around \$2.3b to fund spending to increase defence force numbers, extend the life of the Anzac class frigates and HMNZS Canterbury.
- **Geopolitical risk management:** \$156m for intelligence and security services, New Zealand's aid program in the Pacific (\$110m) and \$145m for MFAT's diplomatic network.
- **Fuel resiliency:** \$150m is allocated to increase New Zealand's strategic fuel reserves and an additional \$450m contingency in the event further fuel related support is required.
- **Roading infrastructure:** \$400m for state highway resilience, \$1.8bn capital contribution for the Cambridge to Piarere expressway.
- **Health:** \$5.5b for the public health system. Bowel screening will now be available from ages 56 and higher plus hospital redevelopment in Tauranga, Hawkes Bay and Palmerston North.
- **Rail:** \$1b for Kiwirail's network improvement program.
- **Education:** \$1.6b for early education and schooling. \$470m of capital spending is allocated to redevelop up to 10 schools and purchase land for new school sites in high growth areas. The final year of fees-free tertiary education is cut, as was announced previously, to help funding education investments in other areas as well as doubling the number of trade academy places.

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