

The Treasury

Budget 2022 Information Release

August 2022

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- [38] 9(2)(j) - to enable the Crown to negotiate without disadvantage or prejudice
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Treasury Report: Budget 2022 Bilateral: Hon Stuart Nash (Economic and Regional Development)

Date:	24 February 2022	Report No:	T2022/344
		File Number:	SH-11-1

Action sought

	Action sought	Deadline
Hon Dr Megan Woods Associate Minister of Finance	Raise the talking points suggested in Annex A of this report at your meeting with Hon Stuart Nash (Economic and Regional Development) on 28 February.	28 February 2022
Hon Grant Robertson Minister of Finance	Note the contents of this report.	28 February 2022

Contact for telephone discussion (if required)

Name	Position	Telephone	1st Contact
Hannah Waine	Analyst, Regions, Enterprise and Economic Development	[39]	n/a (mob) ✓
Jean Le Roux	Manager, Regions, Enterprise and Economic Development		n/a (mob)

Minister's Office actions (if required)

Return the signed report to Treasury.
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Note any feedback on the quality of the report

Enclosure: Yes: DEV-21-MIN-0222 attached

Treasury Report: Budget 2022 Bilateral: Hon Stuart Nash
(Economic and Regional Development)

Executive Summary

This report provides you with advice ahead of your meeting with Hon Stuart Nash (Economic and Regional Development) at 5:00pm on 28 February to discuss his Budget 2022 initiatives.

We understand the focus of this discussion is likely to be the Industry Transformation Plans (ITPs) and the four ITP Budget bids in the Economic and Regional Development (ERD) portfolio. Overall, Treasury has supported several ITP bids at scale across Votes within the Ministry of Business, Innovation and Employment (MBIE). [34]

We have supported funding for programme capability, and monitoring and evaluation in the *Implementation Provision* bid.

Outside of the ITPs, the ERD bids are largely related to the future of regional economic development and supporting climate adaptation. This includes strategies to support the Government's Emissions Reduction Plan (ERP).

Recommended Action

We recommend that you:

- a **note** the advice about the Economic and Regional Development portfolio ahead of your Budget 2022 bilateral discussion with the Minister for Economic and Regional Development on 28 February.
- b **raise** the talking points suggested in Annex A of this report in your Budget 2022 bilateral discussion with the Minister for Economic and Regional Development.



Jean Le Roux
Manager, Regions, Enterprise and Economic Development

Hon Dr Megan Woods
Associate Minister of Finance

Treasury Report: Budget 2022 Bilateral: Hon Stuart Nash (Economic and Regional Development)

Purpose

1. You are meeting with the Minister for Economic and Regional Development, Hon Stuart Nash, at 5:00pm on 28 February to discuss the initiatives he has submitted for consideration through Budget 2022. This report provides you with advice and talking points to support your discussion.
2. Three annexes are attached to this report:
 - a Annex A provides a suggested agenda and talking points for your bilateral discussion with the Minister for Economic and Regional Development.
 - b Annex B provides a baseline summary for the Ministry of Business, Innovation and Employment (MBIE).
 - c Annex C provides a full list of initiatives submitted in the Economic and Regional Development portfolio, the funding sought, the Treasury Vote team assessment and recommendation, and how this is reflected in the draft Budget 2022 package.

Context for Economic and Regional Development portfolio

3. The Economic and Regional Development (ERD) portfolio is the largest in Vote Business, Science and Innovation (BSI). The Half Year Economic and Fiscal Update in December 2021 forecast approximately \$1.5 billion in operating expenditure and \$0.5 billion in capital expenditure for the 2021/22 financial year in this portfolio.
4. The forecast operating expenditure in the ERD portfolio is more than twice the actual expenditure in this portfolio in 2018/19. About \$212 million is forecast to be spent on departmental expenses, with about \$1.2 billion appropriated for non-departmental expenses. Almost \$450 million is in the Provincial Growth Fund (PGF) multi-category appropriation.
5. Forecast capital expenditure in the ERD portfolio has also increased significantly from 2018/19, from just under \$86 million actual expenditure to around half a billion in 2021/22 (\$506.61 million). A large proportion of this expenditure is related to the PGF and investment in Crown-owned companies for tourism and infrastructure.
6. At the beginning of 2021/22, almost \$700 million was appropriated for the PGF and other projects that contribute to economic development in the regions. The PGF has been consistently underspent, with approximately \$572 million in gross underspends (before expense transfers) in 2019/20 and \$143 million in 2020/21. Kānoa (previously the Provincial Development Unit) administers the PGF and the new \$200 million Regional Strategic Partnership Fund (RSPF), which was established at Budget 2021 with an initial year of funding reprioritised from the PGF.

Broader MBIE context

7. The lead agency for the ERD portfolio is the Ministry of Business, Innovation and Employment (MBIE). In 2020/21 MBIE was also the lead agency for 17 portfolios across 3 Votes (BSI, Labour Market, and Building and Construction).

8. MBIE's spending has increased significantly in recent years. In 2018/19, the agency's total operating spend was approximately \$4.5 billion. This increased to approximately \$7 billion in 2020/21. Similarly, capital expenditure increased from \$354 million in 2018/19 to \$928 million in 2020/21. This increase has mostly been in non-departmental expenses.
9. MBIE has had significant involvement in the Government's response to COVID-19. The agency led the development of New Zealand's vaccine procurement strategy and took responsibility for Managed Isolation and Quarantine (MIQ) facilities in mid-2020.
10. In addition to its role in the COVID-19 response, some of MBIE's revenue sources have been impacted by COVID-19. In Budget 2021 it received a \$86.5 million capital injection to address a third-party revenue shortfall as a result of border restrictions.
11. Minister Nash is also responsible for the Small Business and Tourism portfolios in Vote BSI. No funding has been sought through Budget 2022 for these portfolios. Tourism has received \$600 million in Budgets 2020 and 2021 to support the sector due to the impacts of COVID-19. Given underspends and the evolving nature of tourism, in his Tourism Budget 2022 letter Minister Nash noted that opportunities to reprioritise funds within the portfolio would be considered.

Budget 2021 funding for ERD

12. Total funding sought through Budget 2021 and 2022 is outlined in Table 1 below. Key initiatives are included in Table 2.

Table 1: Budget 2021 and 2022 funding for the Economic and Regional Development portfolio

	Budget 2021		Budget 2022	
	Sought	Funded	Sought	Recommended (Package)
<i>Operating (\$bn)</i>	[33]	0.256	[33]	[33]
<i>Capital (\$bn)</i>		0.020		

Table 2: Key Budget initiatives in the Economic and Regional Development portfolio

Funded in Budget 2021	Budget 2022 draft package
Accelerating and Strengthening Business Connect (\$25.2m)	Industry transformation plan implementation provision (\$50.42m recommended)
Expanding our Just Transition Support for Communities Facing Transitions (\$14.0m)	[33]
New Zealand Screen Production Grant – International (\$199.0 m)	Equitable transitions programme (\$3.6m recommended)
Regional Strategic Partnership Fund (\$66.1m - funded through reprioritisation)	Developing a circular economy and bioeconomy strategy (\$3.0m recommended)

Industry Transformation Plans (ITPs)

13. ITPs are a Government priority and manifesto commitment, and have a strong alignment with the Future of Work wellbeing objective. They are also a key lever for the Government to advance its industry strategy and broader economic strategy to deliver a high-wage, low-emissions economy. However, there are choices about the level and timing of investment in ITPs, and the relative roles of Government and industry.
14. The ITP work programme is broad in terms of scope and duration. There are currently eight ITPs, at different stages and with undetermined time horizons [33]

We expect that further funding will be sought in future Budgets, as some ITPs are still in early development phase, and the more developed ones will start to develop new action plans.

[34]

There are significant delivery risks

16. To date, \$51.4 million of funding has been allocated across the ITPs for the 2021/22 financial year (this includes in the ITPs in other portfolios and Votes within MBIE). Through the March Baseline Update (MBU) process, MBIE has requested expense transfers totalling \$14.2 million and in-principle expense transfers totalling \$16.5 million across the ITP work programme in the ERD portfolio. In our Budget 2022 assessments, we supported transferring \$12.8 million of these underspends to offset funding requested for the Implementation Provision bid.

17. Not fully funding the ITP bids may slow progress to develop and implement them. It may also have implications for the partnership approach with industry. However, underspends and labour constraints may also slow progress, regardless of the level of funding. Therefore, we recommend considering scaling or phasing of ITP funding, to manage delivery risks.

Ensuring value for money from ITPs

18. To ensure that investment in ITPs provide the best value for money, there would be benefit in considering:
 - How the programme management function (in the *Implementation Provision* bid) should have a role in identifying system issues and working with the relevant parties to either address them at a system level, or work across ITPs to address them in a more cohesive manner.
 - How the ITP programme may benefit from a specific funding framework that sets out the Government's principles for investing in ITPs. This framework could include aspects of the Government's industry and economic strategies.
 - Identifying what the transition path is for ITP initiatives to become more self-sustaining.

Supporting climate transitions

19. A priority for Budget 2022 is addressing future issues, particularly our climate change response. In Budget 2022, to align with the release of the Government's Emissions Reduction Plan (ERP), the Climate Emergency Response Fund (CERF) will be focused on emissions-reducing policies.
20. The ERD portfolio will be important in supporting the economic transition to a low-emissions economy by contributing to the development of the strategic direction and by setting specific targeted initiatives to support business through the transition. The key challenge is to ensure that initiatives are well developed and that there is the capacity to deliver them, particularly given the volume of activity in the climate space.

The future role and operational funding for Kānoa – Regional Development and Investment Unit

21. Kānoa is responsible for administering six key funds¹ worth approximately \$4.3 billion in total. Kānoa has paid \$1.92 billion worth of funding into regional economic development projects since the inception of the PGF (as at 31 October 2021).
22. Operational funding for Kānoa is not baselined and decisions about its future role and ongoing funding rely on strategic decisions for regional economic development. These include:
 - a A clear direction for regional funding to refine the institutional settings as the Crown has a number of investment institutions, some of which feature regional investment.
 - b Analysis of different funding sources to meet Kānoa's operational funding requirements comparing central funding (the current approach) with the potential to self-fund.

¹ The Provincial Growth Fund, the COVID-19 Response & Recovery Fund Infrastructure Reference Group, Regional Investment Opportunities, Strategic Tourism Asset Protection Programme (STAPP), Worker Redevelopment and the Regional Strategic Partnership

23. The Minister for Economic and Regional Development has been invited to report back before the end of 2022 on the proposed approach to re-invest returns from Crown Regional Holdings Limited (CRHL)² beyond 30 June 2023 for future regional economic development projects (refer DEV-21-SUB-0257).
24. Cabinet has agreed in principle to Kānoa's ongoing operational funding being baselined in the future subject to confirmation of funding through the Budget process (refer DEV-21-SUB-0257). Funding for the next two years of [33] is being sought through Budget 2022.

Initiatives submitted for Budget 2022

The majority of Budget bids submitted in the ERD portfolio are across three key areas; 1) Industry Transformation Plans, 2) Regional Economic Development, and 3) Climate change response. The full list of initiatives and Treasury's recommended package is in Annex C.

Industry Transformation Plans

25. ITP initiatives submitted in the ERD portfolio are:
 - a *Industry Transformation Plan Implementation Provision* [33]
- this includes programme management funding and tagged contingency for the Agritech and Advanced Manufacturing ITPs
 - b [33]
 - c
 - d
26. Of these, we have supported the **Implementation Provision** at scale. We have also supported transfers of underspends in current programmes, meaning that overall the initiatives are supported near their full scale for four years. We consider that the programme management component of this bid is critical to support effective management and delivery of the ITP work programme, although there are options to scale to the Advanced Manufacturing and Agritech contingencies. We have recommended against funding in this bid being baselined, to ensure that funding provided to the ITP programme is effectively evaluated against its objectives.
27. [33]
- 28.

² Crown Regional Holding Limited, formerly Provincial Growth Fund Limited (PGFL), is a Schedule 4A company, created in 2019 to hold PGF investments.

29. [34]

30. [33]

Other ITP initiatives in Budget 2022

31. There are ITP initiatives in other portfolios and Votes across the core, CERF and Cluster Budget processes. These should be considered alongside the ERD ITP initiatives in terms of the overall investment in the ITP work programme. They are:

Core Budget process:

- a *Implementing Actions in the Digital Technologies Industry Transformation Plan* [33] (Vote BSI – Digital Economy and Communications portfolio)
- b *Next Generation Transformation Plan for the Construction Sector Accord ('Accord 2.0')* [33] (Vote Building and Construction)

Climate Emergency Response Fund (CERF):

- c *Increasing woody biomass supply to replace coal and other carbon intensive fuels and materials* [33]
- d *Maximising carbon storage: increasing natural sequestration to achieve New Zealand's future carbon goals* [33]

Natural Resources Cluster (NRC):

- e *Primary Industry Transformation: delivering industry transformation plans in partnership with primary sectors* [33] – this covers the food and beverage, fisheries, and forestry and wood processing ITPs

Climate change adaptation

Developing a circular economy and bioeconomy strategy and the Equitable Transitions Programme [33] \$16.32 million opex respectively)

- 32. These bids are to progress a circular and bioeconomy strategy and equitable transitions strategy respectively. Both of these are recommendations from the Climate Change Commission report.
- 33. Treasury has supported both of these bids at scale. They are foundational to a high priority area and are strongly aligned with Government objectives and the LSF wellbeing domains. We support the development of both these strategies, however, we have delivery concerns.

34. The lead agencies have not been agreed yet, and it is not clear whether there have been attempts to reprioritise funds or FTEs from within baselines. The bids seek 17.5 FTEs in total which, given current labour market constraints and demands for environment and climate change policy skills, raises delivery concerns.

[33]

Regional Economic Development

The Regional Strategic Partnership Fund (RSPF) (\$55m opex and \$55 capex for 23/24)

38. Treasury supports this initiative in full to provide Kānoa with the shortfall of \$110 million for the \$200 million RSPF manifesto commitment. We consider the RSPF to be implementation ready as Cabinet has agreed on the implementation design of the RSPF (refer CAB-21-SUB-0114) and investments are beginning to be made.
39. The investments will be made in the form of grants, loans and equity and thus requires both operating and capital funding. Funding will be transferred between appropriations where necessary.

Managing the RSPF and Kānoa (Regional Economic Development & Investment Unit -
[33]

40. [33]

41. Kānoa will undertake a twice-yearly reprioritisation exercise. The first reprioritisation exercise is expected to generate approximately \$3 million. Previous reprioritisation exercises were used to provide funding for the RSPF but we are now recommending this be fully funded through Budget 2022. Ministers will need to make decisions on the use of funds identified through reprioritisation in future.

Other ERD initiatives

Operating funding for New Zealand Government to Government (NZG2G) [33]

42. NZG2G is a joint venture between the Ministry of Foreign Affairs and Trade (MFAT) and New Zealand trade and Enterprise (NZTE) that mirrors a professional services consulting firm, commercialising world class New Zealand

sector capability in education, sustainable food systems and government effectiveness, selling it to foreign governments.

43. NZG2G's operating funding runs out in July 2022. The operating funding requested is the same as previous budget bids and requires no additional FTEs. The budget bid scores highly on delivery and we support a scaled version of this bid to fund NZG2G for a time-limited three years.
44. The bid has been scaled and we recommend conducting a review into NZG2G's current funding model. Based on the revenue it is projected to generate (\$51.9m of qualified leads in sales pipeline), consideration should be given to whether NZG2G can be self-funded, and what the trade-offs are of self-funding vs the current model of seeking funding from the centre. This should be done ahead of any future Budget bid for operational funding.

Investment in a New Zealand Business Growth Fund (BGF) (\$100.5 million opex across 21/22 and 22/23)

45. This initiative would invest \$100 million in a New Zealand BGF. The BGF would be privately operated and independently managed by the commercial banks, with the Crown as a minority shareholder. The purpose of the BGF is to help SMEs grow by improving their access to finance, by providing patient-equity growth capital to New Zealand SMEs across a range of industries and locations.
46. We do not recommend funding this initiative as the problem definition regarding access to finance is not well defined and it is unclear if the stated benefits of the BGF will occur.
47. However, if you consider government intervention regarding SME access to finance necessary at this point in time, we support the BGF as the best policy tool to use. It poses low precedent and market distortions risks, and low fiscal risk for the Crown. It also does not add significant pressure on limited government resources, as this bid does not request any funding for additional FTEs.
48. We are aware that Minister Nash and the Minister of Finance have been working closely on progressing a potential BGF as outlined in the bid, including discussions with commercial banks and other stakeholders.

Funding tripartite partners to engage in the Future of Work Tripartite Forum (\$0.7 million per annum including outyears)

49. This initiative will provide funding for the equivalent of 2.5 FTEs each for the Council of Trade Unions and BusinessNZ and \$0.100m of research funding per annum to support the continuing successful operation of the Future of Work Forum and for partners to provide the necessary input into policy development.
50. [34]

51. However, if there is desire to provide funding for social partner participation at this forum, we would suggest the scaled option of providing the equivalent of 1 FTE each for the Council of Trade Unions and BusinessNZ and no funding for research (\$0.4 million per annum with outyears).

Constraints and trade-offs

52. The most significant constraint to delivery across the ERD bids is the FTE and contractor components. Across the ERD portfolio, [33]
Current labour market conditions are unfavourable for hiring, with the unemployment rate at a record low of 3.2% (December 2021 quarter). Many of

the FTEs requested have specialised skills (climate change, IT) and are highly sought after across government (policy analysts, project managers).

53. Initiatives with a material FTE component, and especially those requiring specialised skills, generally scored low on delivery. This included some high value and alignment initiatives, such as the climate-related strategies. Within the recommended Budget package we have supported 8.4 FTEs.

[38]

55. Across the ITPs, the scale of funding available is likely to be a constraint, relative to what is requested. [33]

This scale is significant in a Budget where allowances are heavily oversubscribed, meaning that trade-offs of funding across the ITP programme should be considered in decision making. [33]

Annex A: Agenda and Talking Points

General Budget 2022 talking points (5 mins)

- Pressure remains on the operating and capital allowances, meaning there will be a high bar for new spending and it is important that spending is prioritised effectively and is focused on achieving value for money.
- There are also significant public sector capacity and capability constraints – around 40 percent of initiatives are seeking additional FTEs or contractors.
- Without further prioritisation and scaling, it will be challenging to see the public sector deliver such large additional investment on top of the ongoing response to COVID-19, delivering past investments and keeping momentum on the key reform programmes underway.
- New spending is not the only lever for achieving the Government's objectives. You should consider all the levers available to you before requesting new funding, including examining baseline expenditure, ensuring that your agencies are delivering on the significant investments we have already made, and progressing non-spending initiatives such as regulatory reforms.

Economic and Regional Development talking points

Industry Transformation Plans (15 mins)

- The Implementation Provision bid includes funding for monitoring and evaluation and programme management. **How will this funding be used to deliver consistent monitoring and evaluation across the ITPs, more consistent objectives and criteria for government funding, and a long-term plan for the ITP programme, such as the time frame and strategy for reducing reliance on government funding?**
- Through the March Baseline Update (MBU) process, MBIE has requested expense transfers totalling \$14.2 million and in-principle expense transfers totalling \$16.5 million across the ITP work programme in the ERD portfolio. This raises delivery concerns for new ITP initiatives. **What capacity does MBIE have to deliver ITP initiatives funded through Budget 2022?**
- Overall, the ITP bids total a significant scale of funding requested, and we expect future ITP initiatives to be submitted in future Budgets. **How could the ITPs be scaled, phased, or non-funding levers be used (e.g. industry investment) to manage the cost while still delivering on ITP objectives?**
- [33]

What other policy tools have been considered to increase investment in manufacturing assets to support transition to a high-wage low-emission economy?

Climate adaption and CERF bids (5 mins)

- The circular and bioeconomy strategy and Equitable Transitions Programme are high value and alignment initiatives. However, they raise delivery concerns due to the number of FTEs requested and a lead agency not yet being agreed. **What role do you consider the ERD portfolio should have in delivering these (and future) climate and emissions reductions strategies? What other areas**

could be deprioritised to reallocate FTEs to deliver these strategies without additional resource?

Regional Economic Development and NZG2G (5 mins)

- [33]

We consider that reprioritisation exercises may be able to provide for a part of the shortfall now that the RSPF will be fully funded through this Budget. **Do you consider that this will allow Kānoa to continue to deliver against its objectives? How do you see Kānoa's future role in regional economic development?**

- The NZG2G has \$51.9 million of qualified leads in its sale pipeline and its operating expenses have been funded from the centre through the Budget process. We suggest a funding model review is carried out before the next Budget submission. The review should look into its funding model to explore the trade-offs, risks and benefits of the current model against a self-funded model on its operations. **Do you consider that the NZG2G can be self-funded from the revenue it generates? Are there any trade-offs or risks associated with a self-funded model?**

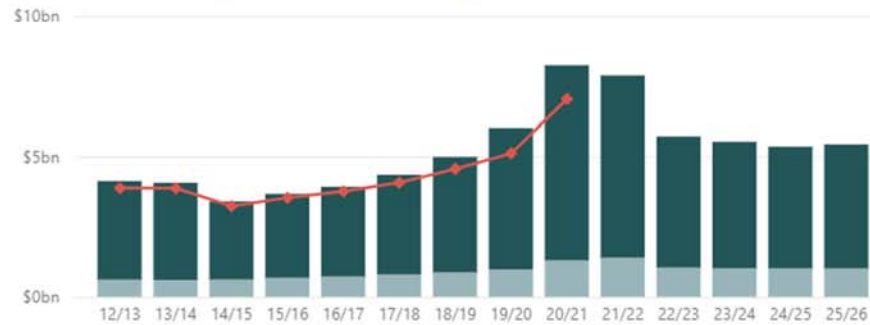
Annex B: Baseline Summary for the Ministry of Business, Innovation and Employment

Ministry of Business, Innovation and Employment

2012/2013 - 2020/2021

Operating Spending & Forecasts (Excluding Borrowing Expense)

● Departmental Operating ● Non-Departmental Operating ◆ Actuals - Year End



Capital Spending & Forecasts

● Departmental Capital ● Non-Departmental Capital ◆ Actuals - Year End



* Compound annual growth rate over the period 2012/2013 - 2020/2021

2020/2021 Key Figures



Confirmed Expense Transfers



