

The Treasury

Budget 2024 Information Release

September 2024

This document has been proactively released and is available on:

- The Budget website from September 2024 to May 2025 only at: <https://budget.govt.nz/information-release/2024>, and on
- The Treasury website from later in 2024 at: <https://www.treasury.govt.nz/publications/information-release/budget-2024-information-release>

Information Withheld

Some parts of this information release would not be appropriate to release and, if requested, would be withheld under the Official Information Act 1982 (the Act).

Where this is the case, the relevant sections of the Act that would apply have been identified.

Where information has been withheld, no public interest has been identified that would outweigh the reasons for withholding it.

Key to sections of the Act under which information has been withheld:

- [1] 6(a) - to avoid prejudice to the security or defence of New Zealand or the international relations of the government
- [23] 9(2)(a) - to protect the privacy of natural persons, including deceased people
- [25] 9(2)(b)(ii) - to protect the commercial position of the person who supplied the information or who is the subject of the information
- [27] 9(2)(ba)(ii) - to protect information which is subject to an obligation of confidence or which any person has been or could be compelled to provide under the authority of any enactment, where the making available of the information would be likely otherwise to damage the public interest
- [31] 9(2)(f)(ii) - to maintain the current constitutional conventions protecting collective and individual ministerial responsibility
- [33] 9(2)(f)(iv) - to maintain the current constitutional conventions protecting the confidentiality of advice tendered by ministers and officials
- [34] 9(2)(g)(i) - to maintain the effective conduct of public affairs through the free and frank expression of opinions
- [35] 9(2)(g)(ii) - to maintain the effective conduct of public affairs through protecting ministers, members of government organisations, officers and employees from improper pressure or harassment;
- [36] 9(2)(h) - to maintain legal professional privilege
- [37] 9(2)(i) - to enable the Crown to carry out commercial activities without disadvantage or prejudice
- [38] 9(2)(j) - to enable the Crown to negotiate without disadvantage or prejudice
- [39] 9(2)(k) - to prevent the disclosure of official information for improper gain or improper advantage
- [40] 18(c)(i) - that the making available of the information requested would be contrary to the provisions of a specified enactment

Where information has been withheld, a numbered reference to the applicable section of the Act has been made, as listed above. For example, a [23] appearing where information has been withheld in a release document refers to section 9(2)(a).

Copyright and Licensing

Cabinet material and advice to Ministers from the Treasury and other public service departments are © **Crown copyright** but are licensed for re-use under **Creative Commons Attribution 4.0 International (CC BY 4.0)** [<https://creativecommons.org/licenses/by/4.0/>].

For material created by other parties, copyright is held by them and they must be consulted on the licensing terms that they apply to their material.

Accessibility

The Treasury can provide an alternate HTML version of this material if requested. Please cite this document's title or PDF file name when you email a request to information@treasury.govt.nz.

Treasury Report: Confirming future Budget operating allowances

Date:	23 April 2024	Report No:	T2024/1091
		File Number:	MC-1-5-2-2024

Action sought

	Action sought	Deadline
Hon Nicola Willis Minister of Finance	<p>Agree to target a return on surplus no later than 2027/28 as your short-term intention for the operating balance.</p> <p>Agree, subject to Cabinet agreement to the key elements of the Phase 2 Fiscal Sustainability Programme, to reduce future Budget operating allowances to \$2.5 billion at Budgets 2025, 2026 and 2027.</p>	<p>23 April 2024 (for discussion at the Weekly Agency Meeting).</p> <p>You have options for when you make final decisions on the recommendations in this report.</p>

Contact for telephone discussion (if required)

Name	Position	Telephone	1st Contact
Sam Thornton	Senior Analyst, Macroeconomic and Fiscal Policy [39]	[35]	✓
Luke Came	Team Leader, Macroeconomic and Fiscal Policy		

Minister's Office actions (if required)

Return the signed report to Treasury.

Note any feedback on the quality of the report

Enclosure: No

Treasury Report: Confirming future Budget operating allowances

Executive Summary

This report seeks decision on the operating allowances for Budget 2025-2027. In the context of significant deterioration in the fiscal outlook since the *Half-Year Economic and Fiscal Update 2023* (HYEFU), you face difficult choices and trade-offs between your fiscal intentions and objectives and the government's other priorities. In Budget 2024, you have taken decisions to deliver the Budget 2024 package below the current operating allowance.

The Treasury recommends that you set an intention to return to surplus no later than 2027/28. Given ongoing structural deficits and repeated delays in the forecast return to surplus since Budget 2022, the Treasury places significant weight on prioritising fiscal discipline through your fiscal strategy.

To support a 2027/28 surplus target, we recommend you set allowances of \$2.5 billion per annum for the next three Budgets. Subject to Cabinet agreement to the key elements of the Phase 2 Fiscal Sustainability Programme (T2024/1102 refers refers). Our indicative final fiscal forecasts suggest these allowances (combined with a Budget 2024 package of \$3.2 billion) would result in the *Budget Economic and Fiscal Update 2024* (BEFU) forecasts showing a small surplus of \$0.7 billion in 2027/28. We note that the fiscal forecasts are not yet finalised, and there is risk that these allowances will still be too high to deliver a forecast surplus in 2027/28.

Setting the Budget operating allowances at \$2.5 billion would strengthen the medium-term fiscal trajectory and confidence in the Government's overarching fiscal strategy to put debt on a downward trajectory towards 40% of GDP. It would also support monetary policy to bring inflation back in the target band, and all else equal allow room for an earlier lowering of interest rates. However, these lower operating allowances will increase the challenge and scale of the trade-offs required to manage demands on future Budget operating allowances.

A range of alternative options exist:

- To increase the probability that the final BEFU 2024 forecasts show a surplus in 2027/28, you could lower allowances to \$2.4 billion for Budgets 2025-27. However, this will increase the delivery risks you will face in future Budgets. Allowances below \$2.4 billion are not recommended until further detail on the plans for savings are developed.
- You could state an intention to deliver a surplus in 2027/28 in your fiscal strategy, but not set operating allowances that result in a surplus in the forecasts. This would give more time to develop your approach for achieving the surplus target. The inconsistency between your strategy and the forecasts would need to be explained, with sufficient commitment made for the strategy to maintain credibility.
- You could choose not to state an intention to deliver a surplus in 2027/28, either by deferring the decision to the Budget Policy Statement for Budget 2025, or setting your intention to return to surplus after 2027/28. These options are not recommended.

We recommend you discuss the options at the Budget Ministers meeting on 24 April 2024, and confirm allowances as part of the Budget Cabinet paper on 29 April 2024.

Commitment to future allowances from your Cabinet colleagues will be critical to ensuring the deliverability of your fiscal strategy. If decisions cannot be reached in this timeframe, you could seek delegated authority from Cabinet on 29 April 2024 to make final decisions. Allowance decisions (and savings and reprioritisation decisions to support those allowances) made before Friday 3 May 2024 can be incorporated into the final fiscal forecasts.

Recommended Action

We recommend that you:

- a **agree** to target a return on surplus no later than 2027/28 as your short-term intention for the operating balance in the Fiscal Strategy Report, even if the lower allowances in recommendation b prove insufficient to show a surplus in 2027/28 in the final fiscal forecasts.

Agree/disagree

- b **agree**, subject to Cabinet agreement to the key elements of the Phase 2 Fiscal Sustainability Programme (T2024/1102 refers), to reduce future Budget operating allowances to either:

- \$2.8 billion at Budgets 2025, 2026 and 2027 (Scenario A in Table 1).

Agree/disagree

or

- \$2.5 billion at Budgets 2025, 2026 and 2027 (Scenario B in Table 1). **[Treasury recommended]**

Agree/disagree

or

- \$2.4 billion at Budgets 2025, 2026 and 2027 (Scenario C in Table 1).

Agree/disagree

Luke Came
Team Leader, Macroeconomic and Fiscal Policy

Hon Nicola Willis
Minister of Finance

_____/_____/_____

Treasury Report: Confirming future Budget operating allowances

Purpose of Report

1. This report provides further advice to support decisions on future Budget operating allowances and the surplus target and discussion on these matters at the Budget Ministers meeting on 24 April 2024.

Context

2. Treasury previously recommended you target a return to surplus no later than 2027/28 and advised you on strategies to support a return to surplus in the BEFU forecasts (T2024/872 refers). Options included reducing your Budget 2024 operating package as much as possible and reducing future Budget operating allowances.
3. You discussed options for the operating allowances and surplus target at Budget Ministers 5 on 10 April 2024. You agreed to convene a Budget Ministers meeting on 24 April 2024 (following receipt of indicative final fiscal forecasts on 23 April 2024) to consider future operating allowances and the surplus target to include in the Budget Cabinet paper for consideration on 29 April 2024.

Indicative update on fiscal outlook

4. You have received advice today from the Treasury on the updated fiscal outlook, in advance of the final fiscal forecasts on 9 May 2024 (T2024/1137 refers).
5. The updated fiscal outlook indicates a further deterioration to the OBEGAL track since the preliminary fiscal forecasts on 18 March 2024, with an OBEGAL deficit of around \$1.2 billion in 2027/28.¹ The indicative forecasts could change as we complete our quality checks of agencies forecast information, gain assurance around the rational of the material changes, and reflect any new decisions and the finalisation of our central assumptions. Accordingly, the indicative OBEGAL track could move up or down as we get closer to finalisation.
6. Further, the updated forecasts show limited progress on putting net core Crown debt as a percentage of GDP on a downward trajectory over the forecast period, peaking at 44.2 percent of GDP in 2026/27 and ending the forecast period (2027/28) at 43.4 percent of GDP, marginally higher than 2024/25.
7. The Treasury recently advised you that the fiscal impulse using the preliminary forecasts showed fiscal policy subtracting from aggregate demand from 2024/25 relative to the previous year (T2024/717). This would be broadly consistent with fiscal policy supporting monetary policy to bring down inflation. The deterioration in the OBEGAL track in the updated fiscal outlook could mean the 2024/25 fiscal impulse becomes positive (i.e. adding to aggregate demand, and hence inflation, from 2024/25 relative to the previous year).

¹ The preliminary fiscal forecasts showed an OBEGAL deficit of \$0.7 billion in 2027/28. Both the preliminary fiscal forecasts and the update you have received today assume operating allowances of \$3.25 billion in 2025 and \$3.0 billion in 2026 and 2027.

Table 1 – Indicative OBEGAL, net core Crown debt and core Crown expenses compared to the preliminary fiscal forecasts

Year ended 30 June	Forecast				
	2023/24	2024/25	2025/26	2026/27	2027/28
OBEGAL - \$billion					
BEFU 24 indicative update	(11.4)	(14.5)	(9.4)	(4.2)	(1.2)
BEFU24 preliminary fiscal forecasts	(7.9)	(8.9)	(6.6)	(3.7)	(0.7)
Total change	(3.5)	(5.7)	(2.8)	(0.5)	(0.5)
Net core Crown debt - % of GDP					
BEFU 24 indicative update	43.2	43.9	43.7	44.2	43.4
BEFU24 preliminary fiscal forecasts	42.9	42.5	41.8	42.4	41.4
Percentage point change	0.3	1.4	1.9	1.8	2.0
Core Crown expenses - % of GDP					
BEFU 24 indicative update	33.5	33.7	32.7	31.9	31.8
BEFU24 preliminary fiscal forecasts	33.4	32.9	32.7	32.1	31.7
Percentage point change	0.1	0.8	..	(0.2)	0.1

Setting your surplus target

8. The significant deterioration in the fiscal outlook since HYEFU sets a challenging context for Budget decision making. In making decisions on your operating allowances and a target date for the return to surplus, you face a competing trade-off between your fiscal strategy and your other policy objectives.
9. From the perspective of your fiscal objectives, lowering the future Budget operating allowances to help achieve a surplus in the forecast period would support medium-term fiscal sustainability, and confidence in the Government's objective to put debt on a downward trajectory towards 40 percent of GDP. Tightening fiscal policy would also support monetary policy to bring inflation back in the target band, and all else equal allow room for an earlier lowering of interest rates. While it is not strictly necessary to deliver a surplus in the forecast period to achieve your long-term fiscal objectives, a faster return to surplus would help bring down debt levels more quickly and contribute to faster macroeconomic rebalancing, reducing inflationary pressure and leading to lower interest rates.
10. As such Treasury continues to recommend setting an intention to return to a surplus no later than 2027/28 in the Fiscal Strategy Report. Tables 2 and 3 below set out options for future Budget allowances to support this recommended fiscal strategy and the implications for OBEGAL in 2027/28.
11. We recommend that this intention is set even if the final fiscal forecasts at BEFU do not show that intention being achieved. In this situation, to mitigate any risks to the credibility of the fiscal strategy, you would need to provide strong assurances at Budget 2024 to help manage market risk. These could include:
 - a reducing operating allowances for Budgets 2025, 2026 and 2027 (but no lower than \$2.4 billion);
 - b committing to implement further savings (and noting that more time is needed to identify and implement enduring savings), including initiatives outside operating allowances, ^[33] ; and
 - c committing to "banking" future upside revenue surprises.

12. Given the uncertainty in the fiscal outlook, targeting a surplus no later than 2027/28 may require further savings in future Budgets to maintain the surplus given typical forecast variations. Identifying and implementing further savings options to increase the size of the 2027/28 surplus over time would increase the likelihood of the achieving the target.
13. If your chosen lower allowances prove insufficient to show a surplus in 2027/28 in the final fiscal forecasts, and you do not wish to set an intention to return to surplus in 2027/28, the alternatives are to:
 - a defer any intention to the specific timeframe for returning to surplus until the Budget Policy Statement 2025 or later, or
 - b set your intended timeframe for returning to surplus beyond the forecast period, e.g. 2028/29 or later.
14. These alternative options would support consistency between the BEFU forecasts and your short-term fiscal strategy intentions, and would give you more time to consider options and trade-offs between the surplus target and other priorities (under option b you could bring forward your surplus target at a later date, if possible). However, Treasury does not recommend this because:
 - a option a would be inconsistent with the statements in the BPS to set the specific timeframe for returning to surplus at Budget 2024, and
 - b option b would mean further slippage to the return to surplus and the necessary rebalancing of expenses and revenue to support fiscal sustainability.

Impact of operating allowance scenarios on the surplus target

15. Tables 2 and 3 below set out the operating allowance scenarios and the indicative impact of alternative operating allowance scenarios considered at Budget Ministers 5. The Budget 2024 operating allowance has been amended to reflect the likely size of the Budget 2024 operating package.
16. Based on the updated fiscal outlook, scenario A considered at Budget Ministers 5 will likely be insufficient to show a 2027/28 OBEGAL surplus in the BEFU forecasts, despite the reduction in the expected Budget 2024 operating package. Scenario B, with allowances of \$2.5 billion from 2025 onwards, is estimated to show a small OBEGAL surplus in 2027/28 at BEFU.
17. We have included an additional scenario (scenario C) ^[34]

assuming Cabinet agrees to the Fiscal Sustainability Programme (FSP) as set out in T2024/1102.
18. As noted, further downside risks remain prior to finalising the BEFU forecasts.

Table 2 – Options for future Budget operating allowances

\$billion per annum	Operating allowances			
	Budget 2024	Budget 2025	Budget 2026	Budget 2027
Included in BEFU 24 indicative update	3.2	3.25	3.0	3.0
Scenario A	3.2	2.8	2.8	2.8
Scenario B	3.2	2.5	2.5	2.5
Scenario C	3.2	2.4	2.4	2.4

Table 3 – Impact of key fiscal indicators from the option on future Budget operating allowances

	2023/24	2024/25	2025/26	2026/27	2027/28
OBEGAL - \$billions					
BEFU 24 indicative update	(11.4)	(14.5)	(9.4)	(4.2)	(1.2)
Scenario A	(11.4)	(14.5)	(9.0)	(3.6)	(0.3)
Scenario B	(11.4)	(14.5)	(8.6)	(2.9)	0.7
Scenario C	(11.4)	(14.5)	(8.5)	(2.7)	1.0
Net core Crown debt - % of GDP					
BEFU 24 indicative update	43.2	43.9	43.7	44.2	43.4
Scenario A	43.2	43.9	43.6	44.0	43.0
Scenario B	43.2	43.9	43.5	43.8	42.6
Scenario C	43.2	43.9	43.5	43.7	42.5
Core Crown expense - % of GDP					
BEFU 24 indicative update	33.5	33.7	32.7	31.9	31.8
Scenario A	33.5	33.7	32.6	31.8	31.6
Scenario B	33.5	33.7	32.5	31.6	31.4
Scenario C	33.5	33.7	32.5	31.6	31.4

Setting your operating allowances and surplus target

19. From the perspective of your other policy priorities, you will face significant demands at future Budgets, including for cost pressures, new spending, the operating component of new capital spending, and a range of other risks that may crystallise in the future (see T2024/872 for previous advice on operating allowance demands). Moreover, a significant proportion of Budget 2025 is already formally or indicatively pre-committed (including Health sector cost pressures).
20. Lowering the operating allowances will increase the challenges and scale of the trade-offs required to manage within allowances. Budget 2024 has involved choices and trade-offs to balance fiscal objectives and the Government's policy objectives. This has included scaling and deferring some policy priorities, scaling and reprioritisation of cost pressures, and decisions to generate savings to offset existing allowances. In order to work within reduced operating allowances in future Budgets, this approach to fiscal management would need to continue, with an ongoing need to minimise out-of-cycle funding decisions to maintain headroom and flexibility for the future Budget decisions.
21. The Treasury is required to use its best professional judgment in preparing economic and fiscal updates. One of these judgments is whether the future Budget operating allowances are set at a realistic level given anticipated future expenditure. The Treasury therefore requires some assurance on how the Government intends to manage within lower future allowances, to support the inclusion in our forecasts.
22. If Cabinet agrees to the key elements of the Phase 2 Fiscal Sustainability Programme (T2024/1102 refers), we recommend you reduce future Budget operating allowances to \$2.5 billion at Budgets 2025, 2026 and 2027 (Scenario B). These allowances would likely be sufficient to forecast a small surplus at BEFU in 2027/28 but would remain subject to risks in the final forecast.

23. If you want to increase the certainty of showing a surplus in 2027/28 at BEFU, you could opt for scenario C. ^[34]

We do not recommend this option at this time as it increases the relative risk that allowances would need to be increased in future. However, scenario B keeps the option open: the allowances could be reduced further once Government develops more detail on its savings plans (including consideration of options outside OBEGAL, ^[33]

Managing within lower allowances

24. A decision to lower the operating allowances in line with any of the scenarios described above will increase the challenge and scale of the trade-offs required to manage demands on future Budget operating allowances.
25. In Budget 2024 you have taken difficult decisions to scale down or not progress some key priorities, not fund cost pressures in full and required increased reprioritisation, and secured significant savings. Continuing this approach will be critical for managing within future operating allowances, but may become more challenging over time because:
- a A significant proportion of Budget 2025 (c.\$1.5 billion) is already formally through approximately \$1.4 billion for health or tentatively pre-committed including almost \$160 million ^[33]
 - b ^[33]
 - c While you don't have a single commitment as large as the tax package to fit into new spending at future Budgets, Ministers will need to reprioritise to fund new initiatives far more than their departments are used to.
 - d New initiatives will need to be traded-off through the Budget process, with relatively little room to move between Budgets. ^[33]
 - e The savings exercise including baseline reductions undertaken for Budget 2024 has reduced much of the 'low hanging fruit' and easy savings options. Previous choices remove avenues for further investigation particularly as some options require time to be delivered ^[34]
26. On the other hand, you will have more time prior to Budget 2025 (compared to Budget 2024) to consider and develop options for savings, reprioritisation and revenue-raising, and the Government's largest manifesto commitments have already been funded. The FSP can help identify future savings options and support them into the Budget process, but substantial future savings are likely only achievable through deliberate policy changes.

Next steps and finalising your operating allowance decisions

27. We are available to discuss the advice this paper with you at the Weekly Agency Meeting on 23 April 2024.
28. You are scheduled to discuss the operating allowances and surplus target with Budget Ministers on 24 April 2024. We recommend discussing a proposal to reduce allowances as per Scenario B, supported by phase 2 of the FSP, with Budget Ministers at this meeting.
29. You have options around the timing for finalising your decisions on future Budget operating allowances:
 - a You could make decisions at the Budget Ministers meeting on 24 April 2024. Following Budget Ministers decisions, the Treasury will incorporate these into a Cabinet paper on the final Budget package and future Budget allowances for Monday 29 April 2024. You will receive an updated Cabinet paper the evening of Wednesday 24 April for your approval to lodge on Friday 26 April.
 - b You could make decisions after the Budget Cabinet paper is lodged on 26 April 2024, with the final decisions made at Cabinet. In this case we would redraft the Cabinet paper to set out options for future Budget allowances, with you orally informing Cabinet of your preferred operating allowances and surplus target at the Cabinet meeting.
 - c You could seek delegated authority from Cabinet on 29 April 2024 for you and the Budget Ministers to make final decisions on Budget allowances. Decisions about reducing allowances and savings and reprioritisation options to support this reduction can be incorporated into the final fiscal forecasts if they are made before Friday 3 May, when the fiscal forecasts will close.
30. As the fiscal forecasts are not yet finalised, it is possible the final forecasts will still not show a surplus in 2027/28, even if Scenario C is incorporated.