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2011
BUDGET

Budget Speech

19 May 2011

Budget Speech

Mr Speaker,

I move that the Appropriation (2011/12 Estimates) Bill be now read a second time.

In 2008, this Government was elected to build a more prosperous and ambitious New Zealand.

Since then New Zealand has been hit with the lingering effects of the global financial crisis, the two earthquakes and other unforeseeable setbacks.

But we have made progress regardless.

The Budgets of 2009 and 2010 helped sustain economic activity and support jobs, and protected the most vulnerable New Zealanders.

At the same time the Government has pursued a longer-term programme to lift growth. It has made major infrastructure investments, improved regulation, continued to reform and invest in science and innovation, shifted resources to frontline services and reformed the tax system.

That work continues. Today I introduce a Budget that will further strengthen the long-term performance of the economy.

It supports economic forecasts that show growth returning to its highest in over five years and 170,000 net new jobs being created by 2015.

It channels resources into key social programmes, while ensuring they are well-targeted and protect the most vulnerable.

It provides certainty that Christchurch, our second largest city, can be rapidly rebuilt.

And, despite the earthquake, it eliminates the deficit and achieves surplus by 2014/15, a year earlier than forecast in last year's Budget.

As a result, the Government's need to raise debt will greatly diminish. This year we have raised an average of $380 million of net new debt every week.

Next year that will fall by more than two-thirds to around $100 million. And from 2014/15 on we will be repaying debt.

Creating and passing through this House a Budget each year is at the heart of stable government. I want to especially thank the Government's support parties, ACT, the Māori Party and United Future, for their contributions.

Mr Speaker,

Our main task remains to return New Zealand to sustained prosperity. The economy has been underperforming since before the global financial crisis. Indeed, per capita GDP has not grown since 2004.

This Government believes that a competitive and well-balanced economy can deliver more jobs and high incomes.

Between 1990 and 2004, a 15-year period, on average the New Zealand economy grew by over 3 per cent a year, and export volumes rose by over 5 per cent a year.

On average 35,000 jobs were created every year.

So our plan is simple, and always has been.

It's about returning to conditions that allow New Zealand to focus on what it is good at doing.

It's about making sure we have a tax system that encourages work and savings, rather than providing incentives to shelter income.

It's about having an efficient public sector that doesn't crowd out the internationally-competitive parts of the economy.

It's about limiting government debt, to reduce our reliance on foreign lenders and to give us a buffer against future economic shocks.

It's about regulation that encourages enterprise and flexibility.

It's about an education system that is producing skilled workers, and those workers knowing they have a successful future here in New Zealand.

It seems simple but it's easy to get off track, as we have seen.

However, it is the only way to create permanent, worthwhile jobs for Kiwis and their families.

It's a proven formula. It works.

Mr Speaker,

Let me first address issues raised by the Canterbury earthquakes.

Christchurch is not only our second-largest city – it is also a major industrial, tourism and regional hub, and is essential to the performance of the wider economy.

The estimated combined cost of the two earthquakes to the economy is around $15 billion, which is about 8 per cent of GDP.

To put this in context, the recent earthquake off the north-east coast of Japan is estimated to have caused damage equivalent to around 3 to 5 per cent of Japan's GDP.

The Treasury's estimate of the direct impact on Crown expenses from the two earthquakes is $8.8 billion. This comprises a $3.3 billion cost to ACC and EQC, net of reinsurance, and an estimated $5.5 billion for all other costs. This includes repairing infrastructure, roads, schools and hospitals, providing temporary housing and providing the business support package.

The $8.8 billion cost is too much for Christchurch residents alone to bear.

But it is manageable within the Government's fiscal programme. New Zealand's annual GDP is around $200 billion. The Government spends around $70 billion a year and has assets of over $220 billion.

For these reasons, the appropriate response is to initially debt fund this cost. That will ensure that the burden of reconstruction is borne evenly across all regions and spread across time.

Debt funding is both the quickest and fairest way to pay for it.

Budget 2011 will provide certainty of funding for Christchurch by establishing the Canterbury Earthquake Recovery Fund.

This Fund will initially include up to $5.5 billion to meet all of the Government's earthquake-related costs, other than those funded by EQC and ACC.

The Canterbury Earthquake Recovery Fund will ensure that there is transparency and control over the cost of the earthquakes. It is expected to take several years for the final bills to arrive, after which the Fund will be wound up.

The Government will also launch a new four-year maturity Earthquake Bond for New Zealand investors. The proceeds will be directed to the Canterbury Earthquake Recovery Fund.

These arrangements mean that reconstruction of Christchurch can proceed with certainty that the Crown's contributions are fully funded.

Mr Speaker,

The OECD, the Savings Working Group and others have pointed out that we need to make the economy more competitive and lift national savings.

Currently, most businesses and households have successfully lifted their own savings. While that has hurt retailers for now, in the long term it is a good thing.

The main sector not saving is the Government.

The deficit in 2010/11 will be large, at $16.7 billion or 8.4 per cent of GDP. This includes a range of one-off costs, including the earthquakes.

The Government believes there is a strong case to eliminate the deficit faster and target a lower level of public debt. This is for a number of reasons.

The fallout from the global financial crisis of two years ago is gradually receding.

The recent fiscal expansion, which began in the mid-2000s and saw nominal spending rise 50 per cent in just five years, has placed much strain on the economy. Exports, growth and productivity have all stagnated.

Finance costs would otherwise rise unacceptably, squeezing out more worthwhile spending.

Rising debt leaves the Government vulnerable and less able to meet future shocks. Its double-A plus credit rating is on negative outlook with two rating agencies.

And productivity growth over the past decade has been less than one-sixth of that in the 1990s.

For all these reasons, stronger government finances are an essential component of moving to sustainably higher growth and job creation.

Mr Speaker,

The Budget forecasts show that, while Government spending will increase, it will do so more slowly than projected previously.

Core Crown spending is forecast to rise from $73 billion in 2011/12 to $77.1 billion in 2014/15.

The Budget identifies $5.2 billion of savings over five years that will be redirected to frontline public services and to reducing the Government's deficit.

New operating spending of around $4 billion over that period is tightly prioritised to health and education, which together receive three-quarters of total new spending.

The net result is a saving of $1.2 billion in operating spending over five years from those parts of the Budget funded by new spending allowances.

Mr Speaker,

Part of the adjustment involves examining programmes where costs have expanded rapidly, in ways that weren't anticipated, and without commensurate value to the community or taxpayers.

KiwiSaver, Working for Families, student loans and ACC are all examples where cost escalation has occurred.

The Government is committed to all of these programmes. With modest adjustments, they will emerge more effective, better targeted to those who really need them, and aligned with what the economy can afford.

Mr Speaker,

The Government has looked closely at KiwiSaver.

KiwiSaver is now well established. It has nearly 1.7 million members, and is gaining about 20,000 new members a month. KiwiSaver funds provide a pool of long-term capital which can be invested with relative certainty.

KiwiSaver balances are currently around $7.9 billion. Of this, about $3.5 billion has been directly contributed by the Government, and the balance by individuals and their employers.

In 2010/11 alone, the Government is contributing $1.2 billion.

At present, KiwiSaver's contribution to national savings is ambiguous. It helps individuals to save for their retirement.

But it means the Government is borrowing, mostly from foreigners, to contribute to private savings.

This does not lift national savings.

A better approach is to have New Zealanders actually saving for their future.

To achieve this, the Budget makes the following changes.

The default and minimum rate of member contributions will increase from 2 per cent to 3 per cent from 1 April 2013. Employees will retain the option to opt out.

The rate of employer contributions will also increase from 2 per cent to 3 per cent from 1 April 2013.

The Member Tax Credit will be reduced to 50 cents per dollar of individual contribution, with the cap halved to $521 per year from the year ending 30 June 2012. This change will be reflected in payments to KiwiSaver accounts from the second half of 2012.

The exemption from the Employer Superannuation Contribution Tax will be scrapped from 1 April 2012. This exemption is regressive, in that those on higher incomes receive larger subsidies.

Existing Kick-Start payments will remain unchanged.

The combined impact will be to see KiwiSaver inflows largely unchanged, but funded more by private savings and less from the Government. The fiscal saving to the Crown will be $2.6 billion over the next four years.

KiwiSaver remains an attractive, subsidised investment. The Government is planning to contribute $650 million next year and $2.5 billion over the next four years.

These changes put KiwiSaver funds on a sound footing. On current projections, KiwiSaver funds will total around $25 billion by 2015, and nearly $60 billion in 10 years' time.

KiwiSaver funds are well placed to participate in the Mixed Ownership Model, which I will come to shortly.

Where State-owned Enterprises raise outside equity, New Zealand investors will be at the front of the queue to invest. We expect KiwiSaver funds to become substantial long-term holders of these investments.

The decisions to lift default contribution rates, to keep KiwiSaver membership voluntary and to remove the Employer Superannuation Contribution Tax exemption were all recommendations of the Savings Working Group.

Mr Speaker,

This Budget makes changes to Working for Families to better target assistance toward lower-income families, and to put the scheme on a more sustainable footing.

Working for Families will remain essentially in its current form. The changes consist of small adjustments to the abatement threshold and abatement rate, and a gradual alignment of the over-16 rate with the 13-to-15-year-old rate.

These changes will be phased in over four steps as Family Tax Credit rates are adjusted for inflation. This is a very gradual transition which is expected, given current inflation forecasts, to take eight years.

Lower-income families and beneficiaries will be largely unaffected by these changes, and the majority will actually get an increase in their Working for Families payments after 1 April next year.

A number of families higher up the Working for Families scale, however, will receive a little less than they currently do now, or will no longer qualify. In most cases, the impacts will be small.

To put this in context, total Working for Families payments have almost doubled over the past five years, and are forecast to cost about $10.7 billion over the next four years. These changes represent about a 4 per cent trimming of the scheme.

Mr Speaker,

The Budget also makes changes to the student loans scheme.

Once again, the scheme will continue in essentially its current form.

This year, the Crown will lend almost $1.6 billion to assist students, up 50 per cent over the past five years. There are currently more than $12 billion of loans outstanding.

However, at present, for every dollar lent out the Government receives only around 55 cents back in 2011 dollar terms.

Budget 2011 tightens the lending criteria so that the scheme is better focused on those who really need assistance.

The measures tighten borrowing conditions for those aged over 55, for part-time students and for those already overdue or in default. There are a number of additional changes.

The estimated operating and capital savings over four years are $447 million. The Crown still expects to lend students a further $6.5 billion over the next four years.

Mr Speaker,

The public sector has a wider role to play in lifting productivity and national saving.

Over the past two years the Government has signalled the need for the sector to become more efficient, and has been mindful of the large increases in most budgets that have occurred in recent years.

In its first two Budgets, the Government successfully reprioritised $3.8 billion of spending into higher-priority areas.

In Budget 2011, $980 million of efficiency savings will be sought from the public sector over three years, starting from 1 July 2012.

The Government will require agencies to fund the cost of KiwiSaver, and some State sector retirement schemes for their employees. This will generate savings of $650 million. At present these contributions are centrally funded and not visible to public sector employers.

A further $330 million in back office savings will be sought from 31 core government agencies.

The savings are part of the ongoing improvement that the Government expects, and are consistent with the adjustment the households and businesses have had to make in recent years.

Mr Speaker,

One area where the benefits of cost reductions are already apparent is ACC.

Over the past two years, ACC has successfully controlled its previously run-away costs, and delivered better results from existing spending.

One immediate benefit is that the Government will need to contribute $638 million less to the non-earners' account over the next four years than previously projected.

ACC members in other accounts will also benefit, with future levies also trending lower as a result of the cost savings within the scheme.

Mr Speaker,

I now turn to the Budget's main new initiatives.

The largest share of new spending has been dedicated to improving core front-line government services.

The health sector will receive $1.7 billion of new funding over the next four years. In addition, a further $500 million of expenditure has been reprioritised within the sector.

District Health Boards will receive the bulk of this funding, including around $400 million in the next year alone.

This will fund a wide range of initiatives, including care for first-time mothers, widened access to medicines funded through DHBs, additional elective surgery, increased disability support services and training more doctors.

The Government's commitment to raising education standards remains strong, so that all young New Zealanders reach their potential.

The Budget provides an extra $1.4 billion for education, including over $100 million of new capital spending. In addition, a further $356 million has been reprioritised.

This builds on the past two years' investment in early childhood education, National Standards and the Youth Guarantee.

Early childhood education also receives an additional $550 million.

The justice sector is to receive $157 million in new funding in Budget 2011 to ensure access to justice and increase public safety.

There are significant initiatives elsewhere where a strong case was made for additional funding.

Statistics New Zealand receives $58 million of new funding to rebuild 20-year-old IT systems that will ensure the ongoing supply of important economic and social data.

The Irrigation Acceleration Fund has been expanded with $35 million of new funding over the next five years. This will help support the development of new water harvesting, storage and distribution infrastructure.

Budget 2011 provides significant capital and operational funding to strengthen delivery of school and community-based Māori language initiatives, help schools to engage better with Māori students, improve literacy and support Kura Kaupapa Māori.

Budget 2011 provides an additional $25 million over the next four years for Whānau Ora, with a further $5 million to be reprioritised from within Vote Māori Affairs.

I particularly thank the Hon Dr Pita Sharples and the Hon Tariana Turia as the Ministers responsible, together with the rest of the Māori Party.

Mr Speaker,

The Budget also includes a range of new capital spending, mostly focused on improving New Zealand's infrastructure.

The Government believes that efficient infrastructure will underpin improved productivity in a growing economy.

Budget 2011 allocates a further $942 million of capital funding to ultra-fast broadband, as Crown Fibre Holdings completes negotiations for the roll-out. This brings the total invested over the past three years to $1.4 billion.

A further $28 million has been allocated for ultra-fast broadband in schools.

The Budget includes the second $250 million tranche of the Government's intended $750 million investment over three years as its contribution toward KiwiRail's $4.6 billion turnaround plan.

And there is an additional $88 million over eight years to complete the upgrade and renewal of the Wellington Metro rail network.

Other key parts of the Government's infrastructure programme are continuing.

We continue to invest over $1 billion a year in state highway improvements, including the seven Roads of National Significance and a number of other significant regional projects.

And the investments in the new prison at Wiri, and a number of new schools, remain on target to deliver worthwhile savings to taxpayers via Public-Private Partnerships.

Mr Speaker,

These capital commitments are part of a larger programme of investment in public assets. The net value of government-owned assets is expected to increase by $34.3 billion between 2010 and 2015.

This includes a range of high-priority areas, including social infrastructure such as schools, hospitals, housing and student loans, as well as the investment in roads, rail, broadband, electricity transmission and increased investment in financial assets.

Some of this extra investment will occur within the State-owned enterprises and Crown entities. But about $21 billion will be invested in core social infrastructure and student loans.

The Government's objective is to maintain investment in core public assets without increasing debt. This highlights the need for the Government to prioritise where its capital is used.

Mr Speaker,

At present, our commercial assets present the greatest scope to change the Government's asset mix.

Earlier this year the Government announced it would explore extending the Mixed Ownership Model for some of its commercial assets.

This model frees up Crown capital, provides the companies involved with wider access to capital and imposes greater transparency and commercial discipline and reduces the need for extra government borrowing.

It also provides Kiwi investors with opportunities to put their money in solid, New Zealand-controlled companies.

It provides the opportunity for KiwiSaver funds, and large government investors like the New Zealand Superannuation Fund and ACC, to increase the proportion of their funds invested in New Zealand.

The Government therefore intends to apply the Mixed Ownership Model to Mighty River Power, Genesis Energy, Solid Energy and Meridian Energy, along with reducing its shareholding in Air New Zealand, starting in 2012.

In all cases the Crown will retain majority ownership.

The expected revenue from offering minority stakes in these five companies is between $5 billion and $7 billion.

This will therefore fund about one-third of the core Crown's increased investment in social assets in the period to 2015.

The alternative would have been to borrow more. The Government believes it is much better to reprioritise existing capital, in this case from commercial to social assets, rather than always accumulate debt.

The Government will seek a mandate in the 2011 general election before proceeding with the Mixed Ownership Model.

Mr Speaker,

The lift in private savings will benefit from a sound savings environment. Investors need both confidence to invest, and quality, reliable investments to invest in.

The collapse of the finance company sector was a major setback to confidence.

Since then, the Government has materially improved the savings environment.

This includes creation of the Financial Markets Authority, overhaul of securities law, regulation of the insurance sector and of financial advisors, and prudential supervision of non-bank deposit takers.

In terms of investment opportunities, both the issue of Earthquake Bonds, and the offer of equity to New Zealand investors under the Mixed Ownership Model, will help deepen the local capital markets.

In addition, the Debt Management Office will issue a new, long-dated, inflation-indexed bond. This reflects clearly expressed demand from long-term investors.

The local government funding agency will start operating later this year. It will be a collective vehicle, providing cheaper funding for local body projects as well as more liquid, better diversified assets for investors.

Mr Speaker,

This year the ACT Party will bring two challenging Bills to the House, which the Government will support to select committee.

The Regulatory Standards Bill seeks to improve the quality of regulatory processes. It includes a mechanism for providing transparency around the making of regulations, and an incentive mechanism to ensure compliance with the process.

The other ACT Party Bill is the Spending Cap (People's Veto) Bill. This Bill seeks to cap real per capita government spending.

In both cases the Government will give the Bill, and the submissions on it, careful consideration.

Mr Speaker,

The final elements of last year's tax package have now come into force, including tighter income definitions related to State assistance and reducing the company tax rate to 28 per cent.

This low rate of tax on businesses demonstrates that we are prepared to back them and recognise that business is the growth engine in a modern economy.

Mr Speaker,

Last year's review of the thin capitalisation rules did not include banks, which are subject to a separate regime because of their high gearing.

Having reviewed the banking sector, we have decided to lift the minimum level of non-deductible capital from 4 per cent to 6 per cent, which is more in line with international norms.

This will provide estimated revenue of $100 million over the next four years.

I thank my colleague, the Hon Peter Dunne, for his ongoing work in improving our tax system.

Mr Speaker,

The measures announced in this Budget will put both the Government's finances and the economy on a much sounder footing despite a series of adverse events and a slower economic recovery.

The projected operating deficit will fall dramatically over the next three years. It will be in significant surplus from 2014/15.

This is a year sooner than the position forecast last year.

Contributions to the New Zealand Superannuation Fund are projected to resume from 2016/17.

The debt projections have also improved.

Even absorbing the cost of the earthquakes, net core Crown debt is now projected to peak at 29.6 per cent of GDP in 2014/15 and then decline steadily.

This contrasts strongly with the outlook of ever-rising debt which the Government inherited in late 2008.

Debt would have peaked at around 27.5 per cent of GDP in the absence of the earthquakes.

Looking further ahead, continuation of current policy would see net debt eliminated entirely by 2024.

This emphasises the responsible, longer-term approach taken by this Government, which will leave future governments with choices about whether to invest, spend or reduce taxes.

It will also provide room to ride out future recessions, which surely will occur.

Our long-term fiscal objective remains to ensure that net debt remains no more than 20 per cent of GDP by the early 2020s. The current projections show this being comfortably achieved.

Mr Speaker,

Budget 2011 is about building our future.

The Prime Minister has made clear this Government's aspirations for an economy that values enterprise, rewards people for effort and encourages them to get ahead.

This is not a typical election year Budget. It is a responsible Budget appropriate to New Zealand's situation.

Budget 2011 shows how, from the depths of the global financial crisis when a decade of red ink was in prospect, and despite the devastating Canterbury earthquakes and other setbacks, the Government has laid the basis for future prosperity.

It is within sight of budget surpluses and falling public debt.

It has funded reconstruction of Christchurch, our second largest city.

It has in prospect the strongest growth for a decade.

It has materially improved the tax system.

It has placed KiwiSaver onto a sounder, more sustainable footing, and instilled a culture built on savings rather than debt.

And it will provide future New Zealanders with real choices about further lowering taxes, adding quality public services, or both.

We set a path for responsible government spending from the start of our term, and we maintain that path in this Budget.

This Budget continues to build a platform for a much stronger, more ambitious New Zealand.

Mr Speaker,

I commend this Budget to the House.