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# Pre-election Economic and Fiscal Update 2011

Hon Bill English, Minister of Finance

25 October 2011

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### Other Information

On the Treasury's website is a series of other information that contains detailed economic forecast tables and additional financial information. This information provides users of the *Pre-election Economic and Fiscal Update 2011* with further detail and should be read in conjunction with the published document. It can be accessed at:

http://www.treasury.govt.nz/budget/forecasts/prefu2011

# Statement of Responsibility

On the basis of the economic and fiscal information available to it, the Treasury has used its best professional judgement in supplying the Minister of Finance with this Economic and Fiscal Update. The Update incorporates the fiscal and economic implications both of Government decisions and circumstances as at 11 October 2011 that were communicated to me, and of other economic and fiscal information available to the Treasury in accordance with the provisions of the Public Finance Act 1989.

Gabriel Makhlouf
Secretary to the Treasury

18 October 2011

This Economic and Fiscal Update has been prepared in accordance with the Public Finance Act 1989. I accept overall responsibility for the integrity of the disclosures contained in this Update, and the consistency and completeness of the Update information in accordance with the requirements of the Public Finance Act 1989.

To enable the Treasury to prepare this Update, I have ensured that the Secretary to the Treasury has been advised of all Government decisions and other circumstances as at 11 October 2011 of which I was aware and that had material economic or fiscal implications.

Hon Bill English
Minister of Finance

18 October 2011

# Executive Summary

Real economic growth of 2.3% is forecast for the year ending March 2012 and an average growth rate of 2.9% per year is forecast for the years ended March 2012 to March 2016. The unemployment rate is forecast to fall from 6.5% in June 2011 to 4.7% in March 2016. A return to surplus in the operating balance (before gains and losses) is forecast for the year ending June 2015 and the ratio of net debt-to-GDP is forecast to peak in the same year.

These forecasts represent the outcome of judgements around likely developments in, and interactions between, five major forces that are influencing the economy:

- The world economy is slowing and concerns about sovereign debt and the stability of the banking system have unsettled financial markets. In a number of advanced countries the outlook for an upturn in growth is constrained by their need to reduce public debt to sustainable levels. We assume that European governments manage the region's debt issues and stabilise financial markets.
- Income growth in China and east Asia has increased demand and world prices for New Zealand's exports. Developments in these economies will be a major determinant of New Zealand's export performance.
- The pace and magnitude of the rebuild in Canterbury.
- The progressive withdrawal of domestic monetary and fiscal stimulus.
- The magnitude of an anticipated move away from household dis-saving.

At present, export prices are high, business confidence remains firm and the Rugby World Cup has provided some temporary support for consumption and for services exports. Partly offsetting these positive impulses, growth in the world's largest developed economies is slowing and financial market volatility has increased. We have revised down our estimates of trading partner growth and there is a significant risk that medium-term growth slows further than is built into our forecasts. The implications of even slower trading partner growth are captured in the Risks and Scenarios chapter.

The reconstruction work in Canterbury will gather momentum over 2012 and into 2013, generating higher employment and business investment, helping to insulate the economy from the impacts of slowing trading partner growth. The Treasury's estimates of damage from the Canterbury earthquakes have been revised up from $15 billion in the *Budget Economic and Fiscal Update* (*Budget Update*) to $20 billion in this *Pre-election Economic and Fiscal Update* (*Pre-election Update*) and our forecast of the scale and duration of the rebuild is also higher.

As the rebuild and broader economic recovery gather pace, spare capacity is drawn into production and monetary policy stimulus will be progressively withdrawn. Fiscal policy stimulus is also forecast to be withdrawn and operating deficits replaced by surpluses in the year ending June 2015. As capacity becomes stretched, the pace of annual average growth slows to 2.4% by the end of the five-year forecast period (Table 1).

A return to positive household saving, defined as aggregate household incomes being higher than consumption, is estimated in the year ended March 2011, for the first time in more than a decade. The rate of household saving is expected to continue to strengthen as households in aggregate move to strengthen their net asset positions. This results in more moderate consumption growth in the current upturn than was experienced in the previous cyclical upturn. In spite of this, the Treasury anticipates that the current account deficit will widen, driven by investment related to the Canterbury rebuild and partly funded by earthquake insurance payments.

The fiscal forecasts are largely in line with the *Budget Update* and continue to show a return to surplus in the year ending June 2015. Core Crown revenue increases as a percentage of GDP over the forecast period while core Crown expenses decline as a percentage of GDP. While the operating deficit continues for the next three years, this trend in revenue and expenses results in a surplus in the fourth year (Table 1).

When capital spending is deducted from operating cash flows, residual cash deficits persist throughout the forecast period. As a result, net debt rises throughout the forecast period and peaks at 29% of GDP in the year ending June 2015 before falling as a percentage of GDP. The decline in net debt as a percentage of GDP continues in the medium-term projections.

***Table 1*** – Summary of the Treasury's main economic and fiscal forecasts

| | 2011 Actual | 2012 Forecast | 2013 Forecast | 2014 Forecast | 2015 Forecast | 2016 Forecast |
|---|---|---|---|---|---|---|
| **Economic (March years, %)** | | | | | | |
| Economic growth[1] | 1.6 | 2.3 | 3.4 | 3.3 | 2.9 | 2.4 |
| Unemployment rate[2] | 6.5 | 5.8 | 5.2 | 4.9 | 4.7 | 4.7 |
| **Fiscal (June years, % of GDP)** | | | | | | |
| Operating balance[3] | -9.2 | -5.1 | -2.0 | -0.4 | 0.6 | 1.2 |
| Net debt[4] | 20.0 | 25.4 | 28.5 | 28.9 | 29.0 | 28.2 |

Notes: 1 Real production GDP, annual average percentage change
2 Percent of labour force, March quarter, seasonally adjusted
3 Total Crown operating balance before gains and losses
4 Net core Crown debt excluding the New Zealand Superannuation Fund and advances

Sources: Statistics New Zealand, The Treasury

The risks to our main forecasts are skewed to the downside. In an illustrative downside scenario, in which we assume a sharper slowdown in trading partner growth and lower terms of trade, we estimate that New Zealand's nominal GDP could be a cumulative $35 billion lower over the five-year forecast period to the year ending June 2016. We estimate that there is at least a one-in-five chance that the New Zealand economy performs worse than in this scenario.

The Crown's net worth is expected to decline in each of the next two fiscal years, before experiencing moderate growth over the remainder of the forecast period. Due to the upwards revision of the fiscal costs arising from the Canterbury earthquakes, this fall is now sharper than previously forecast in the *Budget Update*. Net worth is expected to be slightly below the current level in the year ending June 2016, at $77.2 billion, despite strong gross asset growth across the balance sheet over the forecast period.

The medium-term fiscal projections, covering the decade beyond the end of the forecasts, are similar to those included in the 2011 *Fiscal Strategy Report*. After first attaining a surplus in the year ending June 2015, the operating balance before gains and losses continues to strengthen over the projection period. Core Crown net debt steadily declines over the projection period, largely as a function of increasing surpluses being used to retire debt.

**Finalisation Dates for the Forecasts**

| | |
|---|---|
| Economic forecasts | 26 September |
| Economic data | 26 September |
| Tax revenue forecasts | 30 September |
| Fiscal forecasts | 11 October |
| Specific fiscal risks | 18 October |
| Text finalised | 18 October |

Note on 18 October the Government announced a decision to proceed with KiwiSaver auto-enrolment subject to a return to surplus. As this decision was taken after the forecasts were finalised the impacts of this policy change are not reflected in these economic forecasts. The change is included as a specific fiscal risk in chapter 4.

# 1

# Economic Outlook

## Introduction

This *Pre-election Update*, like its 2008 predecessor, has been prepared during a period of heightened uncertainty in the world economy.  The repercussions of the financial crisis that erupted in 2008 are a key source of today's uncertainty.  In many countries debt levels remain high and economic growth is weak.  Many governments face unprecedented challenges in seeking to reverse fiscal deficits, and to stabilise, and eventually reduce, their debt levels.  The global process of debt reduction has a long way to run and concerns about the sustainability of government debt, the strength of banking systems and economic growth are likely to continue to create periodic bouts of turbulence in financial markets for some time to come.

In contrast to the weak and fragile recovery in the major developed economies, growth in China and east Asia has been solid.  Income growth in the region has led to its increased importance as an export destination and has helped lift New Zealand's terms of trade to their highest level in 37 years.  Despite an easing in the short term, the terms of trade are expected to remain elevated over the forecast period, providing a significant boost to nominal GDP.  But history shows that commodity prices are volatile and, particularly in the current environment, the risks of a more significant fall than forecast here are substantial.

In New Zealand, as elsewhere, fiscal support for the economy will be withdrawn and a return to surplus is expected in the year ending June 2015.  Monetary conditions are also expected to tighten as output expands and spare capacity is used up.  However, the speed of the tightening process is conditional on the strength of world economic growth – slower world growth could delay the start of the tightening cycle.

For households in New Zealand, the rise in unemployment, combined with falls in asset prices and losses in wealth, has contributed to a change in saving behaviour: household saving is positive for the first time in more than a decade and the household debt-to-income ratio is declining.  The change in behaviour is expected to be enduring and to result in lower consumption growth relative to that experienced over the past decade.

The rebuild following the Canterbury earthquakes provides an internal driver of growth that offsets the negative impact coming from abroad.  Much of the rebuild cost is met from insurance claims, which means that progress is largely independent of the state of the world economy.  Recent information has led us to revise our estimates of the damage to

$20 billion from our initial estimate of $15 billion.  As a consequence the rebuild will be larger and take longer than assumed in the *Budget Update*.

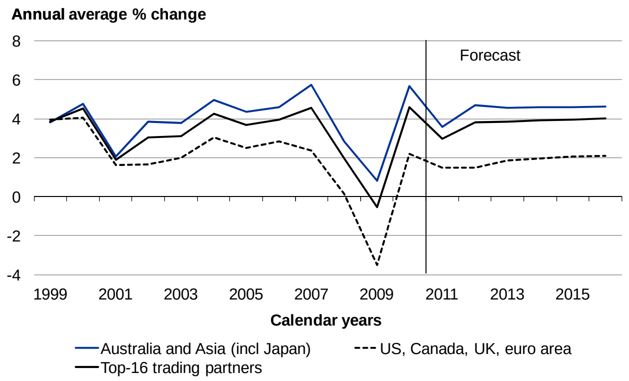
The Treasury's view of the most likely path for the economy over the forecast horizon is based on judgements around the impact of each of these forces and their interaction. However, in the current environment of heighted uncertainty, the range of plausible outcomes is wide.  The Risks and Scenarios chapter presents a view based on a weaker outlook for the world economy.

## Economic Outlook

***Trading partner growth is slowing***

In recent months the outlook for the world economy has deteriorated.  In Europe, concerns about public debt, the stability of the financial system and the slowdown in growth have generated considerable volatility in global financial markets.  Growth in the United States has also weakened and forecasts of growth in both regions have been reappraised as business confidence has faded and financial market volatility has increased.  Euro area growth is forecast to slow to 0.9% in calendar year 2012, and forecast growth in the United States of 1.8% in 2012 is up only marginally from 2011 (see box on page 9).

**Figure 1.1** – Trading partner growth




Sources:  IMF, Consensus Forecasts, The Treasury

Our forecasts assume that European governments implement measures to manage the region's debt issues and stabilise financial markets, and that additional fiscal stimulus is adopted in the United States in 2012, while recognising the need for consolidation over the medium term.  Weaker demand in these economies is expected to flow through to slower export growth in other countries.  How substantive these flow-on impacts will eventually be is difficult to gauge and there is a significant risk that trading partner growth will slow further than assumed in these forecasts.  Trading partner growth of 3.0% in the year to December 2011 is forecast, down from 4.6% last year, which was boosted by cyclical factors, such as inventory rebuilding and policy stimulus.  Despite the deterioration in the world outlook, trading partner growth is expected to rise to 3.8% in 2012.  The increase in 2012 is largely a reflection of the recovery from temporary disruptions to output in Australia and Japan early in 2011 – growth in China slows in 2012 and growth in Other Asia is steady (see Table 1.1).  The gradual recovery in the United States, United Kingdom and euro area and continued solid growth elsewhere lift trading partner growth to around 4% by 2015 (Figure 1.1).

New Zealand's trade links with Other Asia and China, in particular, have strengthened in recent years and they now take around a third of New Zealand exports.  Recent data point to an easing in activity across the region and, while further moderation is expected, the rate of expansion will likely remain solid.  Economies in this region have scope to use fiscal and monetary policies to stimulate demand, although there are risks to inflation and asset prices to be navigated.  The reasonable rates of growth expected in this region will provide opportunities for New Zealand exporters and support for commodity prices.

## Outlook for the World Economy

The outlook for the world economy is one of the main assumptions in our forecasts and also one of the major uncertainties. The greatest uncertainty is associated with the euro area sovereign debt crisis, which we expect to be resolved only gradually, with risks around key developments. The outcome of meetings of European leaders scheduled to occur between the finalisation of this text and its publication, and in the period closely following publication, could change the outlook for the euro area and the global economy. Future developments and responses will carry similar risks.

Our forecasts for economic growth in our main trading partners have been revised down from the *Budget Update* as outturns have been lower and the outlook has deteriorated (Table 1.1). While temporary factors, including natural disasters, account for some of the weaker growth to date, there is increasing acceptance that the recovery from the global financial crisis will be more protracted as household income growth is low and governments reduce debt.

***Table 1.1*** – Trading partner growth (calendar years)

| **PREFU forecasts** | **2008** | **2009** | **2010** | **2011** | **2012** | **2013** | **2014** | **2015** |
|---|---|---|---|---|---|---|---|---|
| *percent change* | *actual* | *actual* | *actual* | *estimate* | *forecast* | *forecast* | *forecast* | *forecast* |
| Australia | 2.6 | 1.4 | 2.7 | 1.7 | 3.5 | 3.2 | 3.2 | 3.2 |
| China | 9.6 | 9.2 | 10.3 | 9.3 | 8.8 | 8.7 | 8.7 | 8.5 |
| United States | -0.3 | -3.5 | 3.0 | 1.5 | 1.8 | 2.0 | 2.2 | 2.4 |
| Euro area | 0.4 | -4.3 | 1.8 | 1.5 | 0.9 | 1.5 | 1.5 | 1.5 |
| Japan | -1.2 | -6.3 | 4.0 | -0.7 | 2.3 | 1.5 | 1.4 | 1.4 |
| United Kingdom | -0.1 | -4.9 | 1.4 | 1.0 | 1.6 | 2.0 | 2.1 | 2.2 |
| Canada | 0.7 | -2.8 | 3.2 | 2.3 | 2.2 | 2.5 | 2.5 | 2.5 |
| Other Asia* | 3.2 | 0.3 | 8.3 | 5.0 | 5.0 | 5.2 | 5.1 | 5.1 |
| **Trading Partners** | **2.0** | **-0.5** | **4.6** | **3.0** | **3.8** | **3.8** | **3.9** | **4.0** |
| | | | | | | | | |
| Consensus (October) | 2.0 | -0.5 | 4.6 | 3.0 | 3.7 | 3.9 | 4.0 | 4.0 |
| IMF WEO (September) | 2.0 | -0.5 | 4.6 | 3.1 | 3.8 | 4.1 | 4.2 | 4.3 |
| Pre-Election Update Downside | 2.0 | -0.5 | 4.6 | 2.8 | 1.7 | 3.5 | 3.7 | 3.8 |
| **Budget Update 2011 (May)** | **1.9** | **-0.5** | **4.6** | **3.7** | **4.4** | **4.1** | **4.1** | **4.1** |

* South Korea, Taiwan, Hong Kong, Singapore, Malaysia, Indonesia, Thailand, Philippines, India

Sources: IMF, Consensus Economics, The Treasury

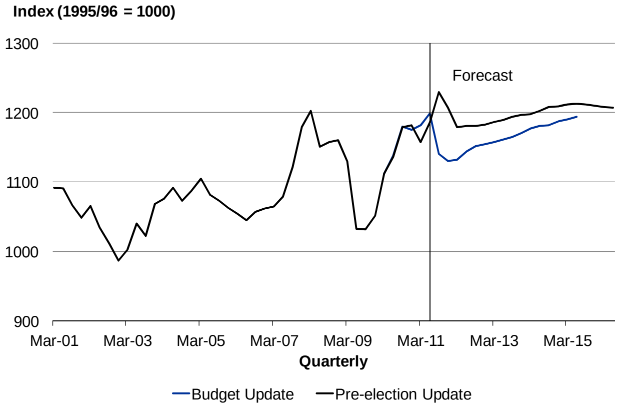
Our forecasts for trading partner growth are similar to October *Consensus Forecasts* (released after we finalised) and the IMF September *World Economic Outlook* (WEO), released just before we finalised. Our forecasts assume an orderly resolution of the euro area debt crisis, although it is acknowledged that this may take a few years to be fully resolved. Euro area growth is expected to slow to 0.9% in 2012 and to rise to 1.5% thereafter. A scenario where the euro area debt crisis is not contained is explored in the Risks and Scenarios chapter. The scenario is based on the IMF's recent WEO downside scenario, but the impact of the crisis is twice as large with trading partner output 3% below the main forecasts at the end of the period in our scenario.

The downside scenario does not envisage as sharp a downturn in the world economy as in the Global Financial Crisis (GFC) when our trading partners' output contracted. In essence, we think policy makers have learned from the GFC and are better placed to respond should financial markets become disorderly. A rapid recovery followed the GFC as authorities responded with monetary and fiscal stimulus and stocks were rebuilt. In the downside scenario presented here, growth dips to 1.7% in 2012 and remains subdued through the forecast period because authorities' ability to stimulate their economies is more limited now and households and governments still need to strengthen their financial positions.

In Australia, the terms of trade are very high, providing a substantial boost to income. Investment in the resources sector is growing strongly, contrasting with more subdued growth in the manufacturing and retail sectors of the economy. Commodity prices have fallen in recent weeks, although generally they remain high. Growth in Australia is likely to slow as the weaker outlook for developed economies flows through to Asian economies, which account for around half of Australia's exports. However, while demand growth may moderate, Australia's commodity export prices are likely to remain well supported, underpinning continued growth.

Prices for New Zealand's major export commodities increased more strongly than expected in the *Budget Update.* While they have fallen from their record highs, they have not slumped the way they did in 2008, although that is a distinct possibility, which we explore more fully in the Risks and Scenarios chapter. Our forecast of a 4% decline in the terms of trade over the coming year reflects both the weaker demand outlook and an easing of supply constraints. In the medium term, increasing emerging market incomes, combined with rising world production costs, suggest that recent gains in the terms of trade will endure (Figure 1.2).

***Figure 1.2*** – Merchandise terms of trade (SNA)

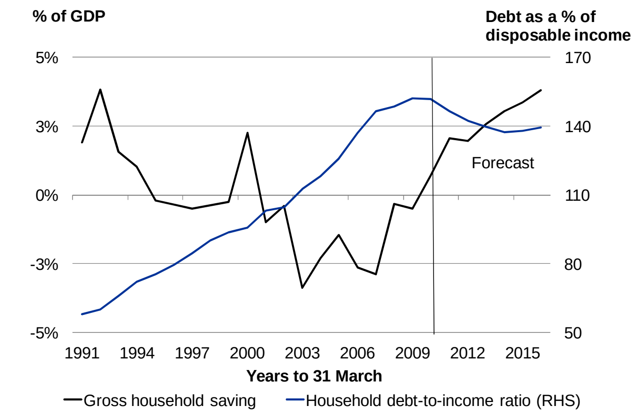



Sources: Statistics New Zealand, The Treasury

High commodity export prices have been reflected in increased profits in the agriculture sector, which have flowed through to lower agricultural sector debt. Household sector credit growth has also slowed, rising 2.0% in the past year, and with household disposable incomes growing 6.4% in the year, the household debt-to-income ratio has begun to decline (Figure 1.3). Income growth is expected to continue to exceed credit growth over the next few years, leading to further declines in this measure of household leverage.

Growth in household consumption spending has also fallen below the rate of income growth. In the year ended March 2011, the difference between income and consumption – saving – is expected to be positive for the first time in more than a decade. The change in saving behaviour is forecast to be persistent, and saving is forecast to continue rising over the forecast period. Factors behind this trend include: a desire by households to rebuild wealth lost through finance company failures and declines in financial and property values, a rise in job insecurity associated with the 2008/09 recession and changes in government policy for example, tax and KiwiSaver policies.

***Figure 1.3*** – Household saving and leverage



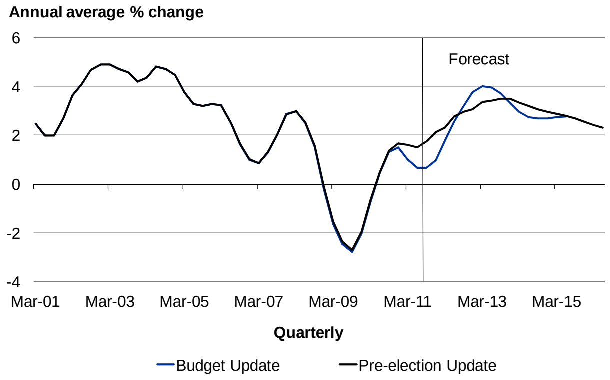

Sources: Statistics New Zealand, The Treasury

***New Zealand's economic recovery continues***

Economic activity over the first half of the year was disrupted by the Canterbury earthquake of 22 February and subsequent aftershocks. However, the economic disruption was not as severe as we had anticipated and real GDP is, at the end of the June quarter, higher than we forecast in the *Budget Update* (Figure 1.4). The increased strength in the economy is expected to persist over the second half of the year. Export prices are high, business confidence remains firm and the Rugby World Cup has provided some temporary support for consumption and for services exports. We expect growth of 2.3% in the year ending March 2012, up from 1.8% in the *Budget Update*.

In the year ending March 2013, growth rises to 3.4%, led by the construction work in Canterbury and the investment required to support it. Compared with the *Budget Update* growth is slower, reflecting the weaker world outlook and a more gradual pick-up in construction activity. The level of spare capacity in the economy is substantially absorbed by the middle of 2013 and growth moderates thereafter as economic growth returns to its sustainable or potential growth rate. Table 1.2 summarises our economic forecasts.

***Figure 1.4*** – Real production GDP




Sources: Statistics New Zealand, The Treasury

Measured in current prices, expenditure in the economy is in line with the *Budget Update* forecasts. Nominal GDP is expected to grow to $209 billion in the year ending March 2012, $2.5 billion above our *Budget Update* forecast. However, growth in the year ending March 2013 is now lower than in the *Budget Update* and GDP in current prices is $0.9 billion lower in the year ending March 2013 than it was in the *Budget Update*. In the year ending March 2015, we forecast GDP in current prices to be $0.3 billion higher than in the *Budget Update*. The cumulative impact of these revisions across the four years ending March 2015 is to raise nominal GDP by $1.7 billion.

The Canterbury rebuild will provide a significant boost to output and employment over the next few years, providing a powerful offset to the effects of the weaker world economy and, because much of the rebuild cost is met from insurance claims, there is a high degree of certainty that this activity will occur, although the precise timing of the rebuilding work is much less clear.

The earthquake rebuild is likely to take longer to begin than initially expected. This is primarily the result of continuing seismic activity in Canterbury and the implications of this activity for the reassessment of land damage and resulting building standards. So far, earthquake-related building consents remain at a low level. Nationally, the market for new houses is showing signs of a recovery from its trough. Over the past year, an estimated 12,000 to 13,000 houses were built, which is well below the 20-year average of around 22,000 houses built per year.

As well as taking longer to begin, the rebuild is expected to be larger and take longer to complete and we have revised our estimate of the extent and cost of damage up to $20 billion from $15 billion. The box on page 13 provides an update on the impacts of the

Canterbury earthquake. These revisions, combined with the cyclical rise in residential building activity, and the repair of leaky buildings, result in this sector contributing around 1.5 percentage points to GDP growth in each of the next two years to December 2013 as activity rises to its peak. A high level of activity is maintained through to the end of the forecasts.

***Table 1.2*** – Economic forecasts[1]

| (Annual average % change, March years) | 2011 Actual | 2012 Forecast | 2013 Forecast | 2014 Forecast | 2015 Forecast | 2016 Forecast |
|---|---|---|---|---|---|---|
| Private consumption | 2.0 | 2.1 | 2.2 | 2.9 | 2.9 | 2.2 |
| Public consumption | 3.8 | 1.8 | -1.5 | -0.2 | 0.5 | 0.7 |
| **Total consumption** | **2.5** | **2.0** | **1.3** | **2.2** | **2.4** | **1.9** |
| Residential investment | 2.3 | -8.4 | 37.6 | 34.9 | 14.2 | 5.5 |
| Market investment | 5.0 | 1.1 | -8.8 | 3.2 | 5.7 | 3.4 |
| Non-market investment | 7.8 | 8.9 | 9.8 | 10.3 | 4.1 | -0.3 |
| **Total investment** | **5.9** | **5.0** | **16.2** | **14.4** | **6.4** | **1.2** |
| Stock change[2] | 1.4 | -0.5 | 0.2 | 0.1 | 0.2 | 0.2 |
| **Gross national expenditure** | **4.5** | **2.1** | **4.8** | **5.4** | **3.7** | **1.9** |
| Exports | 1.9 | 2.8 | 2.3 | 1.9 | 1.7 | 1.8 |
| Imports | 10.5 | 3.6 | 6.1 | 8.0 | 4.3 | 0.7 |
| **GDP (expenditure measure)** | **1.9** | **2.0** | **3.2** | **3.3** | **2.8** | **2.4** |
| **GDP (production measure)** | **1.6** | **2.3** | **3.4** | **3.3** | **2.9** | **2.4** |
| Real GDP per capita | 0.5 | 1.5 | 2.6 | 2.4 | 1.9 | 1.5 |
| Nominal GDP (expenditure measure) | 5.7 | 5.5 | 4.7 | 5.8 | 5.1 | 4.5 |
| GDP deflator | 3.7 | 3.5 | 1.5 | 2.4 | 2.2 | 2.1 |
| Output gap (% deviation, March year)[3] | -0.7 | -0.8 | -0.2 | -0.1 | -0.1 | -0.2 |
| Employment | 1.2 | 1.8 | 1.5 | 1.5 | 1.4 | 1.3 |
| Unemployment[4] | 6.5 | 5.8 | 5.2 | 4.9 | 4.7 | 4.7 |
| Nominal wages[5] | 2.6 | 4.0 | 3.3 | 4.2 | 4.1 | 4.0 |
| CPI inflation[6] | 4.5 | 2.8 | 2.2 | 2.4 | 2.5 | 2.7 |
| Merchandise terms of trade[7] | 9.9 | 3.2 | -1.4 | 1.0 | 1.1 | 0.3 |
| Current account balance | | | | | | |
| $billion | -7.2 | -5.0 | -7.9 | -12.6 | -15.6 | -17.6 |
| % of GDP | -3.6 | -2.4 | -3.6 | -5.4 | -6.4 | -6.9 |
| Net international investment position | | | | | | |
| % of GDP | -68.7 | -68.6 | -69.1 | -70.8 | -73.8 | -77.6 |
| TWI[8] | 67.2 | 70.0 | 70.1 | 69.6 | 67.2 | 63.3 |
| 90-day bank bill rate[8] | 3.0 | 2.9 | 3.7 | 4.3 | 5.0 | 5.3 |
| 10-year bond rate[8] | 5.6 | 4.4 | 4.6 | 5.0 | 5.2 | 5.4 |

Notes:
1 Forecasts finalised 26 September
2 Contribution to GDP growth
3 Estimated as the percentage difference between actual real GDP and potential real GDP
4 Household Labour Force Survey, percent of the labour force, March quarter, seasonally adjusted
5 Quarterly Employment Survey, average ordinary-time hourly earnings, annual percentage change
6 Annual percentage change
7 System of National Accounts (SNA) basis, annual average percentage change
8 Average for the March quarter

A longer time series for these variables is provided on page 118.

Sources: Statistics New Zealand, Reserve Bank of New Zealand, The Treasury

## Economic and Fiscal Impacts of the Canterbury Earthquakes

This box summarises the economic and fiscal impacts of the Canterbury earthquakes that have been incorporated in the *Pre-election Update*, particularly the changes since the *Budget Update*.

### Disruption to economic activity has been less than anticipated ...

Activity has been more resilient to the earthquakes than we expected. Real GDP rose 0.9% in the March quarter against our *Budget Update* expectation of a 0.3% fall. The impact was also less than for the natural disasters in Australia and Japan, where real GDP fell around 1% in the March quarter. But these disasters were different in nature from the Canterbury earthquakes and, crucially, affected exports. Goods exports were affected little by the Canterbury earthquakes as the primary and manufacturing sectors were relatively unscathed. Tourism and international education were affected significantly, but the full impact was not picked up in GDP until the June quarter. The smaller amount of disruption also meant less of a bounce back in subsequent quarters.

### ... but damage estimates are higher, partly owing to continuing aftershocks ...

Our estimate of the damage caused by the earthquakes in Canterbury has increased to $20 billion from $15 billion in the *Budget Update*. The bulk of the upward revision occurred for residential dwellings and reflects higher estimates of damage in the February event and the inclusion of damage from aftershocks since the *Budget Update*, particularly those on 13 June. As in the *Budget Update*, this remains a working assumption with much uncertainty.

***Table 1.3*** – Estimates of the damage caused by earthquakes (NZ$ billion)

| | Residential | Commercial | Infrastructure | Total |
|---|---|---|---|---|
| *Budget Update* | 9.0 | 3.0 | 3.0 | 15.0 |
| *Pre-election Update* | 13.0 | 4.0 | 3.0 | 20.0 |

Source: The Treasury

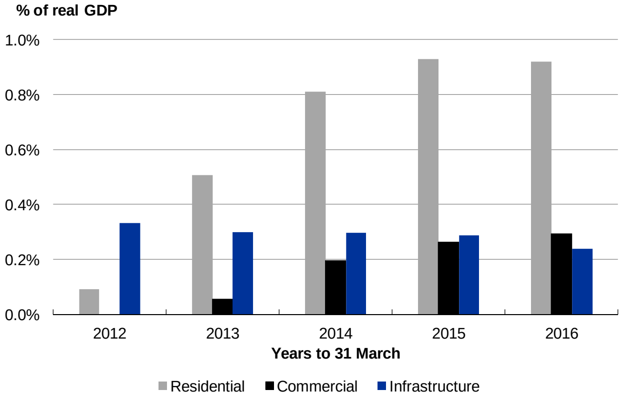
The damage estimates represent damage on property, contents and infrastructure valued at current prices. They do not include business disruption or additional costs from inflation, insurance administration or rebuilding to higher standards than existed before the earthquakes. These costs are important and their inclusion could lift the total cost to $30 billion or more. For example, incorporating inflation raises these estimates by over 20% within the forecast period, with a peak in residential construction cost inflation of around 7% per annum in 2013. The Balance of Payments estimate of $12.5 billion in reinsurance claims includes the impact of the wider insurance costs. These estimates may be revised higher over time as more information comes to hand. Adding the Balance of Payments estimate to the $7.5 billion from EQC's liability already gives an insurance cost of around $20 billion. Compared to the *Budget Update*, the treatment of reinsurance has been changed by Statistics NZ from the current to the capital account.

### ... and the amount of rebuilding will be higher, although somewhat delayed

We now assume investment related to the earthquakes will not start in earnest until the second half of 2012. This represents a delay of six to nine months compared with the *Budget Update*. The delay is the result of a further significant earthquake on 13 June and continuing seismic activity, which in turn has implications for the reassessment of land damage and building code requirements.

Higher damage estimates flow through to more investment in the forecast period, but this investment is less than it could have been owing to this delay, the nature of the extra damage (some of it is to land), and the capacity of the building industry.

***Figure 1.5*** – Canterbury rebuild profile



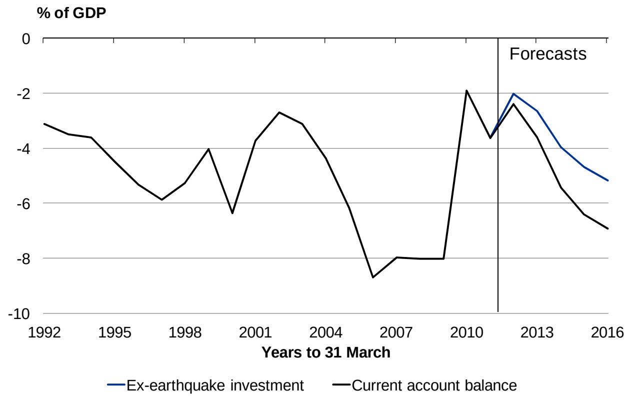

Source: The Treasury

## Wider impacts on the economy

Investment related to the earthquakes contributes around 2 percentage points of the rise in gross national investment from around 20% of GDP in the March 2011 year to over 26% of GDP in the March 2016 year. Although gross national saving is also expected to rise, it is not expected to keep pace with investment. The excess of investment over saving is reflected in the annual current account deficit widening to 6.9% of GDP in the March 2016 year.

Excluding earthquake-related investment, the current account deficit would rise to about 5% of GDP. Beyond 2016, when the rebuilding in Canterbury winds down, and assuming the exchange rate depreciates as in our forecasts, the current account deficit would be expected to return to more sustainable levels of around 4% of GDP.

***Figure 1.6*** – Current account balance




Sources: Statistics New Zealand, The Treasury

## Fiscal impacts

The Canterbury earthquakes will continue to have a significant impact on the Government's fiscal position over the next few years. At the time of the *Budget Update* the estimated total cost (including Earthquake Commission (EQC) insurance costs) was $8.8 billion spread over the next six years. A large portion of this expenditure ($3.2 billion) was unallocated, pending future decisions or additional costs of current obligations or decisions.

The costs of insurance have increased and are reflected in higher payments to foreign reinsurers and a larger current account deficit. There may also be a long-term impact on the level of economic activity as a result of the earthquake (eg, lower services exports and the diversion of resources into the construction sector).

The estimated total net cost to the Crown is now estimated to be $13.5 billion (Table 1.4). The majority of the increase since the *Budget Update* is in relation to insurance costs incurred by the EQC.

***Table 1.4*** – Forecast earthquake expenses (impact on the operating balance before gains and losses)

| Year ending 30 June<br>$million | 2011<br>Actual | 2012<br>Forecast | 2013<br>Forecast | 2014<br>Forecast | 2015<br>Forecast | 2016<br>Forecast | Total<br>Forecast | *Budget*<br>*Update* |
|---|---|---|---|---|---|---|---|---|
| Local infrastucture | 160 | 883 | 128 | 128 | 128 | 128 | 1,555 | *1,162* |
| State-owned assets | 46 | 16 | 15 | - | - | - | 77 | *85* |
| Welfare support and emergency services | 363 | 116 | 27 | 27 | 21 | - | 554 | *521* |
| AMI insurance contingency | 335 | - | - | - | - | - | 335 | *500* |
| Red Zone properties | 653 | 194 | - | - | - | - | 847 | *-* |
| Other costs | 36 | 1,336 | 115 | 58 | 62 | 7 | 1,614 | *-* |
| Yet to be allocated | - | 270 | 120 | 45 | 45 | 45 | 525 | *3,239* |
| **Canterbury Earthquake Recovery Fund** | **1,593** | **2,815** | **405** | **258** | **256** | **180** | **5,507** | ***5,507*** |
| EQC | 7,471 | 225 | 156 | 125 | - | - | 7,977 | *3,050* |
| ACC | 7 | - | - | - | - | - | 7 | *181* |
| Other SOEs and CEs | 16 | - | - | - | - | - | 16 | *40* |
| **Total Crown** | **9,087** | **3,040** | **561** | **383** | **256** | **180** | **13,507** | ***8,778*** |

Source: The Treasury

Costs in relation to the Canterbury Earthquake Recovery Fund are still expected to reach $5.5 billion. Although significant expenditure uncertainties remain, a number of expenditures have now been identified and estimated (eg, the purchase of Red Zone properties), reducing the amount set aside as “yet to be allocated”. As a result, no additional funding is required in the *Pre-election Update* (Table 1.5).

***Table 1.5*** – Funding sources

| Year ending 30 June<br>$million | 2011<br>Actual | 2012<br>Forecast | 2013<br>Forecast | 2014<br>Forecast | 2015<br>Forecast | 2016<br>Forecast | Total<br>Forecast | *Budget*<br>*Update* |
|---|---|---|---|---|---|---|---|---|
| Absorbed by reprioritising within baselines | 156 | 381 | - | - | - | - | 537 | *537* |
| Budget 2010 contingency | 64 | 135 | - | - | - | - | 199 | *199* |
| Budget 2011 | 1,373 | 2,299 | 405 | 258 | 256 | 180 | 4,771 | *4,771* |
| **Canterbury Earthquake Recovery Fund** | **1,593** | **2,815** | **405** | **258** | **256** | **180** | **5,507** | ***5,507*** |
| EQC | 7,471 | 225 | 156 | 125 | - | - | 7,977 | *3,050* |
| ACC | 7 | - | - | - | - | - | 7 | *181* |
| Other SOEs and CEs | 16 | - | - | - | - | - | 16 | *40* |
| **Total Crown** | **9,087** | **3,040** | **561** | **383** | **256** | **180** | **13,507** | ***8,778*** |

Source: The Treasury

The timing of expenditure has also changed since the *Budget Update*. Earthquake spending for the year ended June 2011 was $1.2 billion less than forecast. It is now expected that these expenses will occur over the forecast period.

The forecasts for the Canterbury Earthquake Recovery Fund include a number of pending decisions and possible eventualities that may result in additional costs to the Crown and the Fund being exceeded. Examples of these risks are outlined in the Fiscal Risks chapter (page 57). To the extent that costs exceed those included in these forecasts, there will be an adverse impact on the fiscal position.

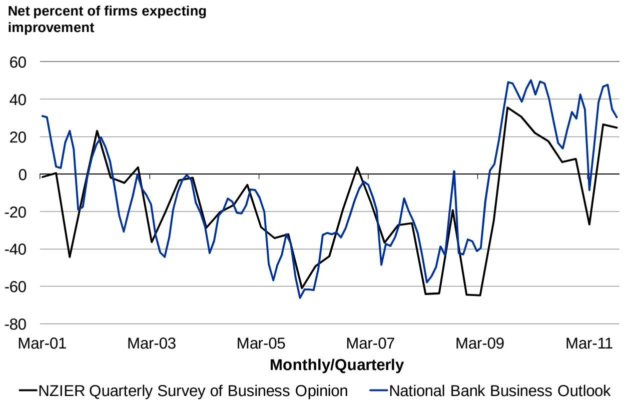
***Employment will continue to expand …***

Employment grew 1.7% in the year ended June 2011 and is expected to continue expanding at a similar pace over the year ahead. The recovery in the economy, combined with reconstruction in Canterbury, helps the unemployment rate to fall from a little under 6% at the start of 2012 to under 5% by the end of 2013. As the degree of spare capacity in the labour market reduces and firm profitability returns to more normal levels, wage growth is also expected to recover, rising from the current rate of around 3% per year to around 4% per year from 2014.

***… and business confidence remains positive***

Measures of business confidence have eased recently, although confidence remains high, suggesting that firms think the impact on New Zealand's growth from the weaker world economy may be mild (Figure 1.7). The recovery in business confidence from the lows of the 2008/09 recession has been reflected in higher business investment and business credit growth. Provided that downside risks to the world economy do not transpire and undermine confidence, business investment is expected to increase 8.9% in the year ending March 2012.

***Figure 1.7*** – Business confidence



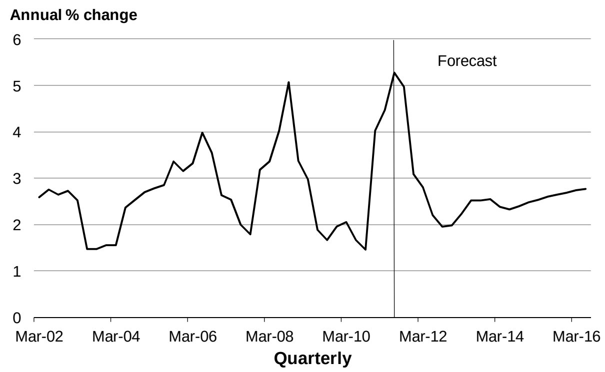

Sources: NZIER, ANZ/National Bank

Strong exporter incomes and the expected increase in both residential and non-residential construction help to sustain business investment growth of around 10% per year until 2014, when construction activity peaks. As the impulse from the earthquake fades, investment growth slows.

***Inflation expected to ease***

Annual Consumers Price Index (CPI) inflation likely peaked at 5.3% in the June 2011 quarter (Figure 1.8). Although CPI inflation is expected to ease in the September 2011 quarter, high food price inflation, rising insurance and house-building costs contribute to a still-elevated annual inflation rate of 5.0% in the quarter. In the December 2011 quarter the one-off impact from the GST increase falls out of the annual CPI calculation and inflation is forecast to fall to 3.1%. Over 2012 inflation eases further reflecting the impacts of the stabilisation and subsequent easing of international prices for food and the more general effects of the rise in the exchange rate over the middle of 2011. The weakening in tradables inflation provides some offset to rising domestic sources of inflation associated with a general tightening in capacity across the economy and inflationary

***Figure 1.8*** – Consumers Price Index

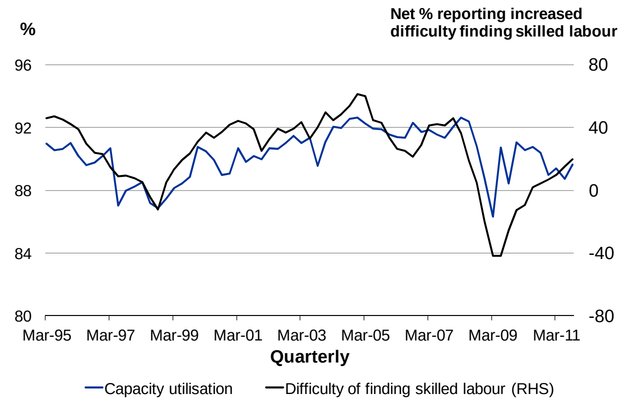



Sources: Statistics New Zealand, The Treasury pressures from the construction sector in particular. Towards the end of the forecast horizon, the falling exchange rate contributes to rising inflation.

***Spare capacity will be absorbed …***

Most indicators of resource utilisation show that spare capacity in the economy has fallen from its recessionary highs but that resource utilisation remains below its normal or average level. For example, survey measures of capacity utilisation and difficulty finding skilled labour produced by the New Zealand Institute of Economic Research (NZIER) have risen but remain below historical averages (Figure 1.9). Similarly, the level of unemployment has fallen but is still relatively high. Other measures of spare capacity in the economy, such as the output gap used in these forecasts, also show the economy's resources are less than fully employed.

***Figure 1.9*** – Capacity measures




Source: New Zealand Institute of Economic Research

Slack in the economy is drawn in over the next two years or so as growth picks up. Labour demand will increase, but initially increased output will be reflected more in the intensity of capital and labour use, rather than in hours worked or employment. Labour productivity (measured using hours worked) is forecast to grow 2.2% in the year to March 2013 but to slow thereafter, as firms take on more staff and output growth slows, in part a reflection of growth in the relatively labour-intensive construction sector. Over the forecast period labour productivity grows at an average rate of 1.5% per year.

Estimates of how fast the economy can grow without running into resource constraints depend on judgements around growth in the capital stock and whether the economy can supply labour to the parts of the economy that need it. Over the forecast period we judge the sustainable or potential growth rate of the economy to be around 2.5% per year or around 1.5% per year on a per capita basis.

***… leading to tighter monetary conditions …***

These judgements around spare capacity and potential growth inform our assessment of inflationary pressure in the economy and the pace at which monetary stimulus is withdrawn, but other factors are also important. For example, the period of easier monetary conditions following February's earthquake has been extended as global financial and economic risks have increased. The pace at which interest rates rise over the forecast period is conditional on the outlook for inflation – a larger slowdown in the world economy would likely see a longer period of low interest rates (the Risks and Scenarios chapter provides further detail). Also important is our assumption that price rises induced by the Canterbury rebuild do not cause a material shift in medium-term inflation expectations. There are some initial signs of rising inflation in the construction industry, which we forecast to increase to around 7% over the next two years or so, and there is a risk that competition for labour and materials between construction-related industries and other parts of the economy generates greater inflationary pressures than assumed here.

### *… and tighter fiscal policy*

Fiscal policy has also been supporting activity in the recovery from the 2008/09 recession and in the aftermath of the Canterbury earthquakes. The government's fiscal plans, announced in the 2011 *Budget*, see this support progressively unwound. Over the next few years, government revenue growth outstrips expense growth and the operating balance deficit narrows and is replaced by surpluses in the year ending June 2015. The withdrawal of fiscal stimulus helps to moderate the inflationary pressures arising from greater resource utilisation and allows for a more gradual pace of monetary tightening.

In the national accounts, the reduction in fiscal stimulus is reflected in a falling share of government consumption in GDP and, as a result of changes to government transfers, slower private consumption growth. The level of government consumption spending has been boosted by a number of one-off expenditure items in recent quarters, including the Canterbury earthquake, imports of spare parts for the Airforce and costs associated with the reorganisation of local government structures in Auckland. These one-offs, combined with data revisions, result in weaker public consumption growth going forward than forecast in the *Budget Update.*

### *New Zealand dollar to remain high*

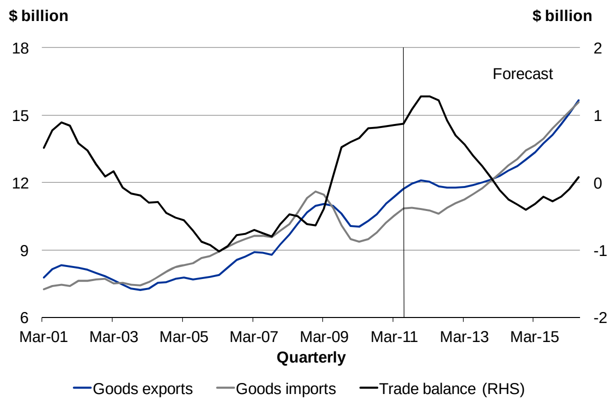
The New Zealand dollar has come off its recent peaks as growing uncertainty in the world economy has led markets to reassess New Zealand's growth prospects, but it remains high relative to most of New Zealand's post-float experience. Credit rating agencies have also reconsidered the sustainability of New Zealand's international debt position and the subsequent downgrade of New Zealand's foreign currency credit rating contributed to a further weakening in the currency. However, the economic outlook for New Zealand is more positive than in many advanced economies, which is expected to provide support for the New Zealand dollar over 2012 and 2013.

### *Long-run interest rates lower*

The credit rating downgrades, which occurred after these forecasts were finalised, also increased long-term interest rates, which impact directly on government debt servicing expenses. We estimate the downgrade increased long-term yields by around 15 basis points. This relatively muted impact likely reflects the backdrop of downgrades in a number of countries in recent months. Despite the downgrades, long-term interest rates in New Zealand and around the world have fallen since the *Budget Update*, reflecting the weaker world economy. Long-term bond yields remain close to their average rate over the past three months or so, suggesting that our forecast for 10-year bond rates of 4.4% in the December quarter, rising to 5.4% by March 2016 remains broadly appropriate.

### *Current account deficit to widen*

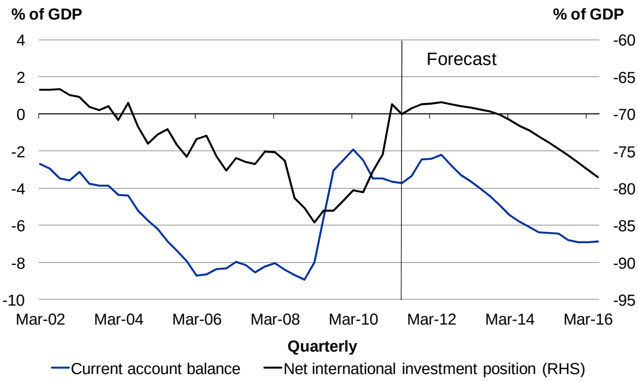
***Figure 1.10*** – Exports and imports




Sources: Statistics New Zealand, The Treasury

The high exchange rate, combined with weaker export demand, is expected to result in export receipts falling in the year ending March 2013 compared to the March 2012 year. At the same time, the domestic recovery, driven by the rebuild in Canterbury, is forecast to increase import payments. As a consequence, the surplus on the goods balance in the Balance of Payments is forecast to become a small deficit in the year ending March 2014, contributing to a current account deficit of 5.4% of GDP in that year. The deficit on the goods balance begins to reverse after March 2015, as the falling exchange rate boosts export receipts (Figure 1.10). However, the current account deficit continues to widen, reaching 6.9% of GDP in March 2016, driven by increasing debt servicing costs as international interest rates rise and profit outflows increase (Figure 1.11).

***Figure 1.11*** – Current account and net IIP




Sources: Statistics New Zealand, The Treasury

The widening of the current account deficit is reflected in the rising net liability position, which increases from 68.7% of GDP in March 2011 to 77.6% of GDP in March 2016 (Figure 1.11). However, in contrast to the period of high current account deficits in the mid-2000s, household and national saving is forecast to rise. The wider deficit and larger net debtor position therefore reflect higher investment spending, driven by the rebuild in Canterbury and by businesses, rather than consumption spending by households. The deficit is expected to stabilise as the Canterbury rebuild winds down.

Goods export volume growth slowed to 2.5% in the year ended June 2011 from the recovery-driven 6.5% in the previous year. At the same time services exports, including tourism, have been declining, with a significant drop in visitor numbers in the wake of the Canterbury earthquakes. Total export volume growth is expected to rise from 1.5% in the year ended June 2011 to 2.8% in the year ending March 2012, reflecting stronger commodity goods volumes and a rise in tourism from the Rugby World Cup. Further out, export volume growth, particularly for non-commodity goods and tourism, is restrained by the weaker world outlook.

Goods import volumes grew 11.6% in the year ended June 2011 driven by the recovery in business investment. However, import growth has trended lower over the first six months of the year and is expected to continue to weaken over the next few quarters before rising as the earthquake rebuild gets underway. Services imports have also been growing strongly, up 6.3% in the year ended June 2011, reflecting in part the high number of overseas trips taken by residents. Overall, real import volume growth is expected to ease to 3.6% in the year ending March 2012 but to rise to 8.0% in the year ending March 2014 as the Canterbury rebuild draws in imports.

The strength in import volume growth relative to exports means that net exports do not make a positive contribution to GDP growth until the final year of the forecasts.

**Economic Forecast Assumptions**

*Earthquake* – Details of the economic and fiscal impacts are discussed in the box on page 13 in chapter 1.

*Trading partner growth* – The economies of New Zealand's top-16 trading partners are expected to grow 3.0% in 2011, 3.8% in both 2012 and 2013, 3.9% in 2014 and 4.0% per annum thereafter. These are a cumulative 2% lower than in the Budget forecasts and similar to growth rates in the *Consensus Forecasts* report for October 2011.

*Global inflation and interest rates* – Annual inflation in the G3 countries (United States, Japan, euro area) falls from 2.0% in the June 2011 quarter to 1.5% in the December 2012 quarter and remains close to this rate over the forecast period. Short-term interest rates in the G3 begin to rise from their current rate of 0.6% in late 2013, reaching 2.4% in the June quarter 2016. G3 long-term interest rates begin to rise from their current rate of 1.9% in late 2012 to 3.1% in the June 2016 quarter.

*Oil prices* – The average price of West Texas Intermediate (WTI) oil rises from around US$87/barrel in the December 2011 quarter to US$93 in the June 2016 quarter. This projection is based on a monthly average of futures prices from the New York Mercantile Exchange recorded on 19 September 2011.

*Terms of trade* – The merchandise terms of trade, as measured in the System of National Accounts (SNA), are estimated to fall 4% over the year to September 2012 as commodity export prices fall from recent highs. The terms of trade remain higher than in the *Budget Update* owing to a higher starting point and offsetting weakness in merchandise import prices.

*Monetary conditions* – The New Zealand dollar Trade Weighted Index (TWI) exchange rate falls from 72.0 in the September 2011 quarter to 70.0 in the December quarter, holding there throughout 2012 and 2013. From 69.6 in March 2014, the TWI falls to 62.3 in the June 2016 quarter. Ninety-day interest rates are forecast to rise from 2.8% in the September 2011 quarter to 5.3% by the end of the forecast period.

*External migration* – The net inflow of permanent and long-term migrants of 2,300 in the year ending August 2011 becomes a net outflow of 1,000 in the year ending March 2012 as a result of the recent rise in departures to Australia (where labour market conditions have been stronger) and the impact of the Canterbury earthquakes. Additional activity related to the earthquake rebuild supports a rebound in net migration to 15,000 in the year ending March 2014 before settling at our long-run assumption of 10,000 in the year ending March 2016.

# 2

# Fiscal Outlook

## Introduction

### *Table 2.1* – Fiscal forecasts

| **Year ending 30 June<br>$billion** | **2011<br>Actual** | **2012<br>Forecast** | **2013<br>Forecast** | **2014<br>Forecast** | **2015<br>Forecast** | **2016<br>Forecast** |
|---|---|---|---|---|---|---|
| Core Crown revenue | 57.6 | 61.2 | 65.7 | 70.4 | 74.8 | 79.2 |
| Core Crown expenses | (70.5) | (74.5) | (71.6) | (72.9) | (75.6) | (78.0) |
| Net surpluses/(deficits) of SOEs and CEs | (5.5) | 2.5 | 1.4 | 1.5 | 2.2 | 2.0 |
| **Total Crown OBEGAL** | **(18.4)** | **(10.8)** | **(4.4)** | **(0.9)** | **1.5** | **3.1** |
| Net retained surpluses of SOEs, CEs and NZS Fund | 5.1 | (3.0) | (1.5) | (1.6) | (2.3) | (2.0) |
| Non-cash items and working capital movements | 4.0 | 4.5 | 0.3 | 1.3 | 0.6 | 1.2 |
| **Net core Crown cash flow from operations** | **(9.3)** | **(9.3)** | **(5.7)** | **(1.3)** | **(0.2)** | **2.3** |
| Net purchase of physical assets | (1.5) | (2.1) | (1.6) | (1.4) | (1.4) | (1.6) |
| Advances and capital injections | (2.5) | (1.9) | (2.2) | (2.2) | (2.5) | (2.2) |
| Forecast for future new capital spending | - | (0.2) | (0.5) | (0.7) | (0.8) | (0.9) |
| Balance sheet funding of new capital spending | - | - | 0.1 | 0.6 | 0.8 | 0.8 |
| **Core Crown residual cash deficit** | **(13.3)** | **(13.6)** | **(9.9)** | **(5.0)** | **(4.1)** | **(1.6)** |
| Opening net debt | 26.7 | 40.1 | 53.8 | 63.2 | 67.8 | 71.3 |
| Core Crown residual cash deficit | 13.3 | 13.6 | 9.9 | 5.0 | 4.1 | 1.6 |
| Other valuation changes in financial assets and financial liabilities | 0.1 | 0.1 | (0.5) | (0.4) | (0.5) | (0.4) |
| **Closing net debt** | **40.1** | **53.8** | **63.2** | **67.8** | **71.3** | **72.5** |
| **As a percentage of GDP** | **20.0%** | **25.4%** | **28.5%** | **28.9%** | **29.0%** | **28.2%** |

A glossary and longer time series for these variables is provided on pages 113 and 117 respectively.

Source: The Treasury

While core Crown expenses[1] are expected to exceed core Crown revenue for the majority of the forecast period, the gap between them reduces, due in part to the expenditure constraints announced at the last *Budget Update*. As a result, core Crown revenue begins to exceed expenses by the year ending 30 June 2016.

1 Core Crown expenses represent the operating expenses of government entities listed on page 77 but exclude expenses of State-owned enterprises and Crown entities. Losses are also excluded.

When forecast surpluses from State-owned enterprises (SOEs) and Crown entities are added, total Crown operating deficits are forecast to persist for the first three years of the forecasts with the total Crown operating balance before gains and losses (OBEGAL) moving into surplus in the year ending June 2015.

Core Crown operating cash flows represent the cash impact of the operating deficit (or surplus). These cash flows exclude the surpluses retained by SOEs, Crown entities and the New Zealand Superannuation (NZS) Fund and non-cash items such as depreciation. Core Crown operating cash flows remain in deficit but decline for most of the period, reaching an operating cash surplus in the year ending June 2016 (a year later than the operating surplus).

When the forecast capital investments are included (eg, purchasing assets, making advances to students), cash deficits decline over the forecast from $13.6 billion in the year ending June 2012 to $1.6 billion by the year ending June 2016.

These cash deficits are funded by an increase in net debt which is forecast to rise from 20.0% of GDP at June 2011 and stand at 28.2% at June 2016 (after peaking at 29.0% in 2015).

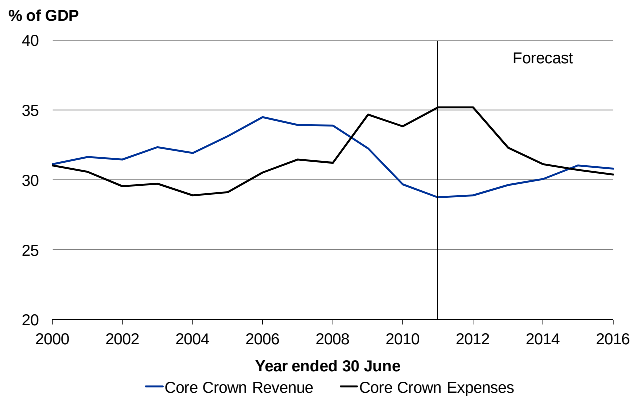
# Short-term Outlook

***Core Crown revenue increases while expenses decline as a percentage of GDP over the forecast period***

Core Crown revenue is forecast to increase over the forecast period, reaching 30.8% by the end of the forecast period compared to 28.7% in the 2011 financial year just past.

Tax revenue makes up roughly 90% of total core Crown revenue. Other sources of income include interest income, revenue from the Emissions Trading Scheme and levies such as Child Support revenue.

***Figure 2.1*** – Core Crown revenue and expenses




Source: The Treasury

The expected increase in core Crown revenue as a percentage of GDP is therefore predominantly in relation to core Crown tax revenue which is forecast to increase from 26.2% of GDP in the year ending June 2012 to 27.8% by the end of the forecast period.

Tax revenue is expected to grow at an average of 6.5% per year between the years ending June 2012 and June 2016. This increase is underpinned by growth in the nominal economy of around 5.0% per year. The main drivers of tax revenue growth are:

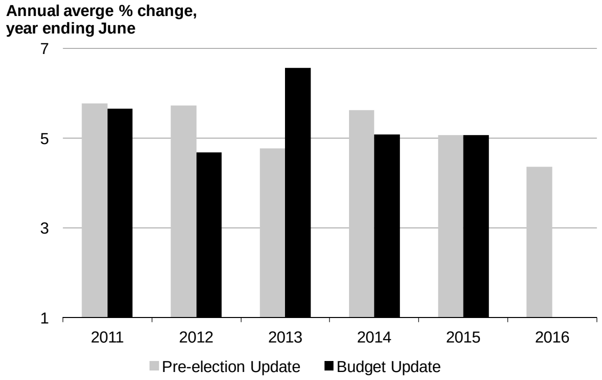
- higher levels of employment and rising wages result in tax from source deductions growing at around 7% per year
- the higher GST rate is applied to the full year to June 2012, boosting GST by 10% in that year. Growth in GST remains above 7% in the years ending June 2013 and 2014, as growth in the economy exceeds its long-run average, and

- after several years of declining revenue, corporate tax revenue bounces back in the year ending June 2012. Growth in the year ending June 2013 slows, reflecting the impact of the first full year of a lower corporate tax rate and the impact of large tax losses built up through the 2008/09 recession being unwound. Revenue growth slows, however, over the June 2015 and 2016 years as the pace of economic growth slows.

Compared to the *Budget Update*, the Treasury's macroeconomic forecasts for the *Pre-election Update* have softer growth in nominal GDP in the year ending June 2013 with growth returning, albeit from a lower base, in subsequent years (Figure 2.2).

The weaker nominal economic growth rate in 2013 reflects slower growth in employee compensation and in consumption and flows through to lower estimates of growth in PAYE and GST tax revenue. Although growth in these tax drivers increases in subsequent years, the growth rates are not significantly higher than in the *Budget Update* and the lower tax revenue in the year ending June 2013 is not recovered within the forecast period.

***Figure 2.2*** – GDP in current prices (expenditure measure)




Sources: Statistics New Zealand, The Treasury

The profit measures of operating surplus (for corporate) and entrepreneurial income (for other businesses) have also been revised down for the year ending June 2013, with peaks in activity now occurring a year later in the year ending June 2014. However, both measures have been strengthened in the current year ending June 2012.

Overall, compared to the *Budget Update*, core Crown tax forecasts have increased for the year ending June 2012 by $0.3 billion, but forecasts have been revised downwards in all subsequent years (Table 2.2).

***Table 2.2*** – Core Crown tax revenue

| **Year ending 30 June**<br>**$billion** | **2012**<br>**Forecast** | **2013**<br>**Forecast** | **2014**<br>**Forecast** | **2015**<br>**Forecast** | **2016**<br>**Forecast** |
|---|---|---|---|---|---|
| Pre-election Update | 55.5 | 59.2 | 63.6 | 67.6 | 71.5 |
| Budget Update | 55.2 | 59.9 | 64.4 | 68.5 | |
| **Increase/(decrease)** | **0.3** | **(0.7)** | **(0.8)** | **(0.9)** | |

Source: The Treasury

In line with established practice, Inland Revenue has also prepared a tax revenue forecast, which, like the Treasury's tax forecast, is based on the Treasury's macroeconomic forecasts. The two sets of forecasts differ from each other because of the different modelling approaches used by the agencies, and the various judgements and assumptions made by the forecasting teams in producing their forecasts. The Inland Revenue forecasts are in the Treasury and Inland Revenue Tax Forecasts section of the Additional Information chapter of *Pre-election Update 2011* published online only at http://www.treasury.govt.nz/budget/forecasts/prefu2011.

Core Crown expenses are forecast to decline as a percentage of GDP compared to the previous *Budget Update,* even including costs associated with the Canterbury earthquakes.

Earthquake costs to the Crown were $1.2 billion below forecast in the June 2011 financial year. However, these costs are now expected to be recognised in the current forecast period. Total earthquake costs (excluding EQC insurance costs) are estimated to remain largely within the forecast amounts included in the *Budget Update* (refer page 15).

Excluding these one-off earthquake costs, core Crown expenses are forecast to decline as a percentage of GDP across the forecast period from 34.2% in the year ending June 2011 to 30.3% by June 2016. This decrease reflects the reduction in new spending over this period that was announced in the *Budget Update*.

By June 2016, core Crown revenue is expected to exceed core Crown expenses by $1.2 billion.

### *Core Crown expenses[2] increase in nominal terms*

While core Crown expenses are forecast to decline as a percentage of GDP, they are expected to increase in nominal terms (Table 2.3).

***Table 2.3*** – Growth in core Crown expenses since 2010 (pre-earthquake)

| **Year ending 30 June**<br>**$billion** | **2012**<br>**Forecast** | **2013**<br>**Forecast** | **2014**<br>**Forecast** | **2015**<br>**Forecast** | **2016**<br>**Forecast** |
|---|---|---|---|---|---|
| **Movements in expenditure** | | | | | |
| *New spending* | | | | | |
| Budget 2010 decisions | 1.1 | 1.1 | 1.1 | 1.1 | 1.1 |
| Budget 2011 decisions | 0.4 | (0.2) | (0.3) | (0.3) | (0.3) |
| Budget 2012 allowance | - | 0.8 | 0.8 | 0.8 | 0.8 |
| Budget 2013 allowance | - | - | 0.8 | 0.8 | 0.8 |
| Budget 2014 allowance | - | - | - | 1.2 | 1.2 |
| Budget 2015 allowance | - | - | - | - | 1.2 |
| *Existing policies* | | | | | |
| Increases in New Zealand Superannuation costs | 1.3 | 1.9 | 2.5 | 3.3 | 4.2 |
| Increase in other social assistance | 0.3 | 0.4 | 0.3 | 0.3 | 0.4 |
| Emissions Trading Scheme | 1.1 | 0.3 | 0.3 | 0.6 | 0.9 |
| Debt impairments | 0.5 | 0.5 | 0.7 | 0.7 | 0.7 |
| Finance costs | 1.4 | 1.5 | 1.6 | 2.0 | 2.0 |
| *Short-term expenses* | | | | | |
| Canterbury earthquakes | 2.8 | 0.4 | 0.3 | 0.3 | 0.2 |
| Other movements | 1.6 | 0.9 | 0.8 | 0.8 | 0.8 |
| **Increase in core Crown expenses** | **10.5** | **7.6** | **8.9** | **11.6** | **14.0** |
| Baseline expenses (June 2010) | 64.0 | 64.0 | 64.0 | 64.0 | 64.0 |
| **Core Crown expenses** | **74.5** | **71.6** | **72.9** | **75.6** | **78.0** |

Source: The Treasury

2 Core Crown expenses represent the operating expenses of government entities listed on page 77 but exclude expenses of State-owned enterprises and Crown entities. Also excluded are gains and losses.

When costs associated with the Canterbury earthquakes are excluded, the main components of the increase in expenses are social assistance expenses (predominantly NZS), future allowances for new operating spending, costs associated with the Emissions Trading Scheme, and finance costs relating to the increase in gross debt.

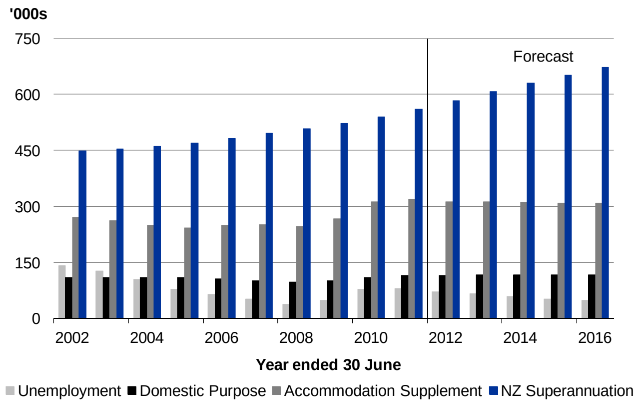
At each Budget the Government announces expenditure initiatives. In the last *Budget Update* saving initiatives were of a greater value than the estimated cost of new initiatives. As a result, net savings were forecast over the forecast period. The forecasts in this *Pre-election Update* include an allowance for future spending initiatives based on the Government's net new operating allowances for new spending over the forecast period.

New Zealand Units issued under the Emissions Trading Scheme are expected to increase as new sectors enter the scheme. These expenses are partially offset by revenue associated with the surrender of New Zealand Units by emitters. Note 20 of the Forecast Financial Statements provide further details of the scheme.

Social assistance expenses are forecast to increase by $3.7 billion over the five years of the forecast period compared to the year ending June 2011. The majority of this increase is in relation to NZS which is expected to increase by $3.6 billion over that period.

This expected increase in social assistance expenses is due to growth in both the number of recipients (Figure 2.3) and the effect of wage and CPI indexation.

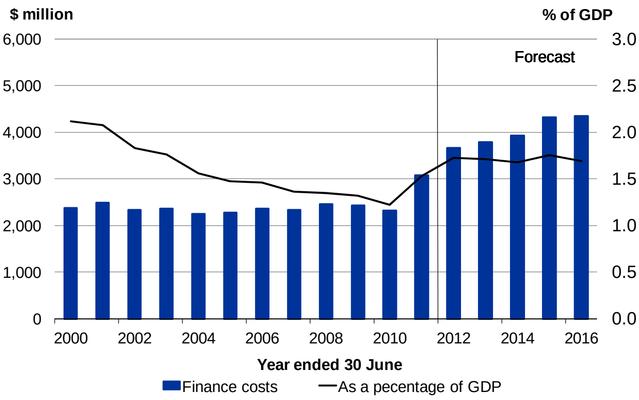
***Figure 2.3*** – Beneficiary numbers




Source: The Treasury

Finance costs are estimated to increase over the next few years (Figure 2.4) resulting from an increase in gross debt (discussed later in the chapter). Finance costs are forecast to increase from $3.7 billion in the June 2012 financial year to $4.3 billion in the year ending June 2016.

***Figure 2.4*** – Finance costs




Source: The Treasury

While debt financing costs increase over time, they are forecast to be much lower than expected at the last *Budget Update*. For example, the *Budget Update* forecast finance costs of $5.3 billion in the year ending June 2015. Our estimate for that year has fallen to $4.3 billion in the current forecasts, primarily driven by a reduction in the forecast interest rates.

The credit rating downgrades, which occurred after the interest rate forecasts were completed, are not expected to have a material impact on debt financing costs (long-term yields are expected to increase by around 15 basis points).

Cash raised from debt issuance that is not immediately required to meet cash demands is invested in financial assets. Therefore, while finance costs increase over the forecast period, this is partially offset by an increase in interest revenue from the invested assets (Table 2.4).

***Table 2.4*** – Core Crown net interest income

| **Year ending 30 June** <br> **$billion** | **2012** <br> **Forecast** | **2013** <br> **Forecast** | **2014** <br> **Forecast** | **2015** <br> **Forecast** | **2016** <br> **Forecast** |
|---|---|---|---|---|---|
| Core Crown interest revenue | 1.1 | 1.3 | 1.3 | 1.6 | 1.7 |
| Core Crown finance costs | (3.7) | (3.8) | (3.9) | (4.3) | (4.3) |
| **Core Crown net finance costs** | **(2.6)** | **(2.5)** | **(2.6)** | **(2.7)** | **(2.6)** |

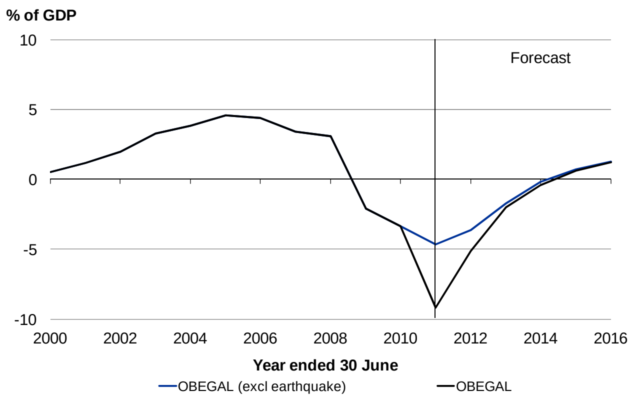
Source: The Treasury

### *The Crown is still forecast to return to surplus by June 2015*

When core Crown forecasts are combined with the forecasts for SOEs and Crown entities, the total Crown is expected to return to surplus in the year ending June 2015 as also forecast in the *Budget Update* (Figure 2.5).

The operating deficit[3] is expected to fall from 9.2% of GDP in the June 2011 year to 5.1% of GDP in the June 2012 year. Excluding the cost of the earthquakes to the Crown, the deficit is estimated to be 3.7% of GDP in the year ending June 2012 compared with 4.6% in the previous financial year.

***Figure 2.5*** – Total Crown operating balance before gains and losses




Source: The Treasury

The June 2015 surplus has increased slightly from $1.3 billion in the *Budget Update* to $1.5 billion in these forecasts. Forecast reductions in tax revenue, the recently announced reduction in ACC levies, and the forecast impact of the introduction of the agriculture sector in 2015 to the Emissions Trading Scheme are expected to be offset by a faster-than-expected decline in unemployment benefits, an increase in the EQC levy and a reduction in forecast interest rates.

When forecast net gains are included, the total Crown operating balance (including gains and losses) is forecast to reach a surplus of $1.6 billion (0.7% of GDP) in the year ending June 2014. These net gains arise predominantly from forecasts of investment returns by the Crown's financial institutions (eg, the NZS Fund).

Operating balance forecasts for the year ending June 2012 include actuarial losses of $2.3 billion on the ACC claims liability and the Government Superannuation Fund pension liability, reflecting a decrease in the discount rates since 30 June 2011 that is used to calculate these long-term liabilities.

3 Operating balance before gains and losses.

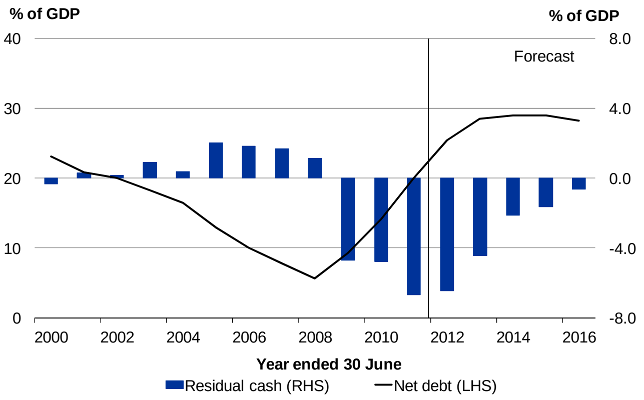
### *Cash deficits persist, resulting in increasing net debt*

While the Crown returns to surplus[4] in the year ending June 2015, residual cash deficits, although reducing, remain across the forecast period.

Operating cash does reach surplus by June 2016, but when capital spending is included, residual cash remains in deficit by $1.6 billion (or 0.6% of GDP) in that year.

Capital spending includes providing funding to the Earthquake Commission to cover the estimated cash shortfall of $490 million in the year ending June 2015.

***Figure 2.6*** – Net Core Crown debt




Source: The Treasury

The resulting residual cash deficits represent the amount the Crown has to fund, either by raising debt or reducing financial assets and they result in an increase in net debt.

The reducing cash deficits result in net debt rising in nominal terms but decreasing as a percentage of GDP from a peak of 29.0% at June 2015 to 28.2% by June 2016. This decline continues into the medium-term projections (page 38).

The profile for net debt is forecast to remain similar to the picture outlined in the *Budget Update*. As a result, the borrowing programme run by the New Zealand Debt Management Office (NZDMO) remains largely unchanged (Table 2.5).

The forecasts include the redemption of non-market domestic bonds held in the Earthquake Commission's Natural Disaster Fund (NDF). In addition, repayments of market domestic bonds are expected in the first two years of the forecasts and in the year ending June 2015.

***Table 2.5*** – Net increase in domestic bonds

| **Year ending 30 June** <br> **$billion** | **2012** <br> **Forecast** | **2013** <br> **Forecast** | **2014** <br> **Forecast** | **2015** <br> **Forecast** | **2016** <br> **Forecast** | **5 year** <br> **Total** |
|---|---|---|---|---|---|---|
| Cash proceeds from issue of domestic bonds (market) | 15.4 | 12.8 | 10.0 | 7.8 | 4.8 | 50.8 |
| Repayment of domestic bonds (market) | (7.6) | (11.0) | - | (10.0) | - | (28.6) |
| Net increase in domestic bonds (market) | 7.8 | 1.8 | 10.0 | (2.2) | 4.8 | 22.2 |
| Cash proceeds from issue of domestic bonds (non-market) | 0.4 | 0.1 | - | - | - | 0.5 |
| Repayment of domestic bonds (non-market) | (1.7) | (0.6) | (0.9) | (0.1) | - | (3.3) |
| Net increase in domestic bonds (non-market) | (1.3) | (0.5) | (0.9) | (0.1) | - | (2.8) |
| **Net cash proceeds from bond issuance** | **6.5** | **1.3** | **9.1** | **(2.3)** | **4.8** | **19.4** |

Source: The Treasury

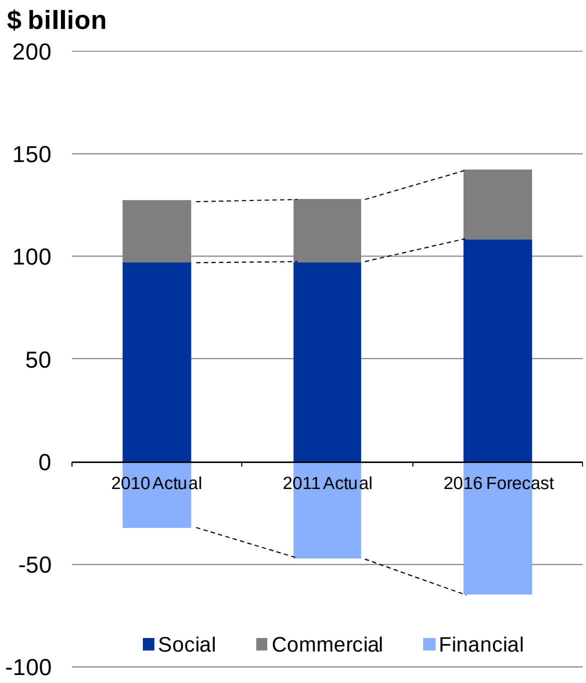
4 Operating balance before gains and losses.

# Crown's Balance Sheet Outlook

***Net worth is forecast to remain below current levels over the forecast period***

Continuing the trend from the past year, the Crown's net worth is expected to fall to a low of $65.9 billion in 2013, before recovering slightly over the remainder of the forecast period. By 2016, net worth is forecast to be $77.2 billion, $3.7 billion below 2011 levels (Figure 2.7 and Table 2.6).

**Figure 2.7** – Portfolio net values 2010, 2011 and 2016




Source: The Treasury

The forecast continuation of fiscal deficits in each of the next three years is the main factor behind this decline in net worth. Core Crown borrowings are forecast to grow from $76.8 billion to $94.9 billion over the period. This is expected to drive a fall in the value of the financial portfolio, the only portfolio to experience a decline in net value, from -$47.2 billion to -$64.9 billion.[5] The fall is sharper than previously forecast in the *Budget Update* owing to the run down of the NDF as a result of the upwards revision of EQC costs arising from the Canterbury earthquakes. The use of NZDMO assets built up to meet Government bond maturities in the 2012 and 2013 fiscal years further contributes to the decline in the value of the financial portfolio.

Meanwhile, the social and commercial portfolios are both forecast to experience small net growth over the next five years.

The social portfolio is forecast to grow consistently, from $97.3 billion to $108.5 billion, representing portfolio growth of 11.5%. This is largely unchanged from the previous forecasts. This net growth is driven by a $9.7 billion increase in assets from continued investment in physical assets in priority social areas, particularly health, education and state highways. Expected net growth in the student loan book also contributes.

The commercial portfolio is also forecast to experience consistent growth, driven by the reinvestment of positive operating returns offsetting growth in liabilities. Of the $11.2 billion increase in commercial liabilities, $7.7 billion is attributable to forecast growth in Kiwibank deposits. The Crown's net commercial interests are expected to increase from $30.8 billion to $33.7 billion by 2016, or by 9.4%. This growth takes no account of a

[5] The 'social portfolio' consists of the assets and liabilities held primarily to provide public services or to protect assets for future generations; the 'financial portfolio' reflects assets and liabilities held by the Crown to finance or pre-fund government expenditure; while the Crown's 'commercial portfolio' consists of the portfolio of companies held with purely commercial objectives. For more details, see the *Investment Statement of the Government of New Zealand 2010* /www.treasury.govt.nz/budget/2010/is.

possible reduction in the Crown's commercial ownership from the proposed extension of the Mixed Ownership Model.[6]

Commercial assets and liabilities across the forecasts are slightly higher than those in the *Budget Update*, reflecting the inclusion of AMI Insurance in the Crown's accounts and small upwards revisions across the portfolio.

***Table 2.6*** – Forecast portfolio assets and liabilities, 2011 to 2016

| $billion | 2011 Actual | 2012 Forecast | 2013 Forecast | 2014 Forecast | 2015 Forecast | 2016 Forecast | Change between 2011 and 2016 |
|---|---|---|---|---|---|---|---|
| ***Assets by Portfolio*** | | | | | | | |
| Social | 113.6 | 115.1 | 116.9 | 119.2 | 121.0 | 123.3 | 9.7 |
| Commercial | 58.1 | 60.7 | 63.1 | 66.3 | 69.4 | 72.1 | 14.1 |
| Financial | 73.5 | 69.8 | 62.0 | 67.5 | 66.0 | 72.0 | -1.5 |
| **Total Assets** | **245.2** | **245.6** | **242.0** | **253.0** | **256.4** | **267.4** | **22.2** |
| ***Liabilities by Portfolio*** | | | | | | | |
| Social | 16.4 | 17.7 | 15.9 | 15.6 | 14.9 | 14.8 | -1.5 |
| Commercial | 27.2 | 29.6 | 31.8 | 34.1 | 36.5 | 38.4 | 11.2 |
| Financial | 120.7 | 130.0 | 128.4 | 135.8 | 133.5 | 136.9 | 16.2 |
| **Total Liabilities** | **164.3** | **177.3** | **176.0** | **185.5** | **184.9** | **190.2** | **25.9** |
| **Total Net Worth** | **80.9** | **68.3** | **65.9** | **67.5** | **71.5** | **77.2** | **-3.7** |

Note that numbers may not add exactly due to rounding

Source: The Treasury

### *However, there will still be significant asset growth across the balance sheet*

While overall net worth is expected to remain below current levels by 2016, the Crown's assets are forecast to grow by gross $76.1 billion over the period to $267.4 billion after asset reductions (Table 2.7).

Table 2.7 shows that:

- Of the $76.1 billion of gross asset growth, roughly half will occur in physical assets, known as "property, plant and equipment" (PPE). Including the companies currently being considered as candidates for the Mixed Ownership Model, SOEs are the largest source of this PPE investment, contributing 40.0%. Crown entities are forecast to be the next largest investors in PPE, driven largely by investments in the road network by the New Zealand Transport Agency (NZTA). Departments are expected to undertake 22.0% of gross PPE investment over the period.
- Within non-PPE-related assets, growth in the asset portfolios held by the Crown Financial Institutions (CFIs) is the largest driver.[7] This arises from the projected value growth of existing assets and the reinvestment of returns, and contributes over a quarter of all gross asset growth. Growth in student loan advances is expected to remain largely steady across the forecasts, representing $8.2 billion by 2016.

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6 The Government has announced its intention to offer partial ownership of certain State-owned enterprises to private investors if it is re-elected. This is often referred to as the "Mixed Ownership Model". As there is insufficient information to forecast individual transactions, there are no estimates of sale proceeds, selling costs, foregone dividends or ownership changes in these forecasts.

7 The 'Crown Financial Institutions' consist of the NZS Fund, Accident Compensation Corporation (ACC), EQC, National Provident Fund and the Government Superannuation Fund.

- $3.0 billion of new capital spending is expected over the forecast period. This reflects the assumption of a capital allowance of $900 million per Budget spread over five years. This expenditure has been included as a non-PPE addition as the exact nature of the investment is yet to be determined.
- Gross asset growth will be offset by asset reductions and other changes of $53.9 billion. This is due mainly to depreciation, an unwinding of financial assets held by the NZDMO and the RBNZ, and a reduction in the EQC's assets as claims from the Canterbury earthquakes continue to be paid out. Repayments and revaluations of existing loans are expected to offset previously mentioned additions to the student loan book by $6.0 billion, resulting in a net increase in the student loan book of $2.2 billion.
- The net increase in Crown assets over the next five years is forecast to be $22.2 billion.

***Table 2.7*** – Summary of forecast asset movements, 2011 to 2016

| **$billion** | **2011 Actual** | **2012 Forecast** | **2013 Forecast** | **2014 Forecast** | **2015 Forecast** | **2016 Forecast** | **5-Year Total** |
|---|---|---|---|---|---|---|---|
| ***Forecast Growth in Assets*** | | | | | | | |
| PPE additions: | | | | | | | |
| Departments | 1.5 | 2.3 | 1.7 | 1.3 | 1.2 | 1.5 | 8.0 |
| Crown entities | 2.5 | 3.0 | 2.7 | 2.6 | 2.6 | 2.8 | 13.8 |
| SOEs | 2.7 | 3.4 | 2.9 | 3.0 | 2.7 | 2.6 | 14.5 |
| Total PPE additions | 6.6 | 8.7 | 7.3 | 6.8 | 6.6 | 6.9 | 36.3 |
| Non-PPE additions: | | | | | | | |
| Student loans additions | 1.6 | 1.6 | 1.6 | 1.7 | 1.7 | 1.7 | 8.2 |
| CFI asset investment growth | 7.7 | 3.2 | 3.7 | 4.4 | 4.6 | 5.1 | 21.0 |
| Kiwibank mortgages | 1.1 | 1.5 | 1.5 | 1.6 | 1.6 | 1.6 | 7.7 |
| Forecast new capital spending | 0.0 | 0.2 | 0.5 | 0.7 | 0.8 | 0.9 | 3.0 |
| Total non-PPE additions | 10.4 | 6.4 | 7.3 | 8.3 | 8.6 | 9.2 | 39.8 |
| **Gross additions to assets** | **17.0** | **15.1** | **14.6** | **15.1** | **15.2** | **16.1** | **76.1** |
| ***Forecast Reductions in Assets*** | | | | | | | |
| PPE reductions: | | | | | | | |
| Depreciation on PPE | (3.7) | (4.0) | (4.2) | (4.3) | (4.3) | (4.4) | (21.2) |
| Balance sheet funding for new capital | 0.0 | 0.1 | (0.1) | (0.6) | (0.8) | (0.8) | (2.3) |
| Non-PPE reductions: | | | | | | | |
| RBNZ and NZDMO activity | 5.6 | (7.8) | (9.9) | 3.4 | (5.5) | 1.7 | (18.0) |
| Student loans other changes | (0.9) | (1.1) | (1.1) | (1.2) | (1.2) | (1.3) | (6.0) |
| Reduction in EQC assets | 3.3 | (2.8) | (2.7) | (2.8) | (1.0) | 0.1 | (9.1) |
| Other changes in assets | 0.6 | 0.9 | (0.3) | 1.3 | 1.1 | (0.3) | 2.7 |
| **Net change in assets** | **21.9** | **0.4** | **(3.6)** | **11.0** | **3.4** | **11.1** | **22.2** |
| **Closing total Crown assets** | **245.2** | **245.6** | **242.0** | **253.0** | **256.4** | **267.4** | |

Note that numbers may not add exactly due to rounding

Source: The Treasury

### *This will be funded from a range of sources*

The Crown funds its asset growth from various sources, both from activity carried out within the core Crown and from dedicated sources outside it. Core Crown activity effectively reflects revenue raised from a mixture of taxation, additional borrowing, SOE dividends, and other sovereign revenue. Of the $76.1 billion of gross asset growth forecast for the next five years, $20.3 billion is expected to be funded directly from this activity (Table 2.8). The remaining $55.9 billion is forecast to be funded from sources outside the core Crown, including the reinvestment of CFI asset returns, road-user levies collected by the NZTA, and the retained operating surpluses of SOEs.

***Table 2.8*** – Summary of forecast funding sources, 2012 to 2016

| **$billion** | **2012 Forecast** | **2013 Forecast** | **2014 Forecast** | **2015 Forecast** | **2016 Forecast** | **5-Year Total** |
|---|---|---|---|---|---|---|
| Funding sourced from core Crown activity: | | | | | | |
| Used to purchase PPE | 3.2 | 2.7 | 2.1 | 2.1 | 2.4 | 12.5 |
| Used for budget capital allowances | 1.0 | 0.3 | 0.2 | 0.1 | 0.1 | 1.7 |
| Funding for new capital spending from existing resources [1] | 0.2 | 0.5 | 0.7 | 0.8 | 0.9 | 3.0 |
| Used for issuing student loans | 0.7 | 0.7 | 0.6 | 0.6 | 0.5 | 3.1 |
| **Total funding from core Crown activity** | **5.2** | **4.1** | **3.6** | **3.5** | **3.8** | **20.3** |
| Other funding sources: | | | | | | |
| Student loan repayments | 0.9 | 0.9 | 1.0 | 1.1 | 1.2 | 5.1 |
| Proceeds from asset disposals | 0.3 | 0.2 | 0.3 | 0.3 | 0.3 | 1.4 |
| Hypothecated revenue for roading | 1.2 | 1.2 | 1.3 | 1.5 | 1.7 | 6.9 |
| Financial and operating returns from CFIs | 3.8 | 2.6 | 2.7 | 2.7 | 3.1 | 14.9 |
| Valuation gains/(losses) on CFI investments | -0.6 | 1.1 | 1.7 | 1.8 | 2.0 | 6.1 |
| Borrowing by SOEs | 1.2 | 1.2 | 0.9 | 0.6 | 0.3 | 4.0 |
| Operating surpluses generated by SOEs | 1.8 | 1.7 | 2.0 | 1.9 | 2.2 | 9.8 |
| Kiwibank deposits | 1.5 | 1.5 | 1.6 | 1.6 | 1.6 | 7.7 |
| **Total funding from other sources** | **9.9** | **10.5** | **11.5** | **11.6** | **12.3** | **55.9** |
| **Total funding** | **15.1** | **14.6** | **15.1** | **15.2** | **16.1** | **76.1** |

Note that numbers may not add exactly due to rounding

[1] Funded from existing assets and increased returns on commercial assets

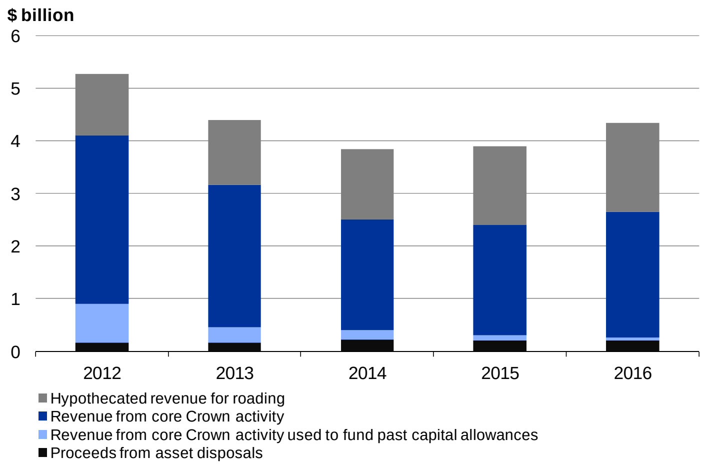
Source: The Treasury

Separating the sources of funding into those for PPE growth and those for all other non-PPE-related growth presents a clearer picture of which areas of the balance sheet are expected to rely largely on core Crown funding and which are predominantly self-funded.

Figures 2.8 and 2.9 present the funding sources for forecast PPE investment, as carried out by departments, Crown entities, and SOEs:

- Of the $21.7 billion of PPE investment forecast for departments and Crown entities over the next five years, 63.7% is expected to come from the core Crown (Figure 2.8). Of this, $12.5 billion will fund new PPE spending, while $1.4 billion will be used to fund PPE expenditure committed to in previous years' Budgets. Hypothecated revenue, principally road-user levies collected by the NZTA, contributes $6.9 billion over the five years, or 31.8%. The remaining 4.5% is from the disposal of assets within departments and Crown entities.

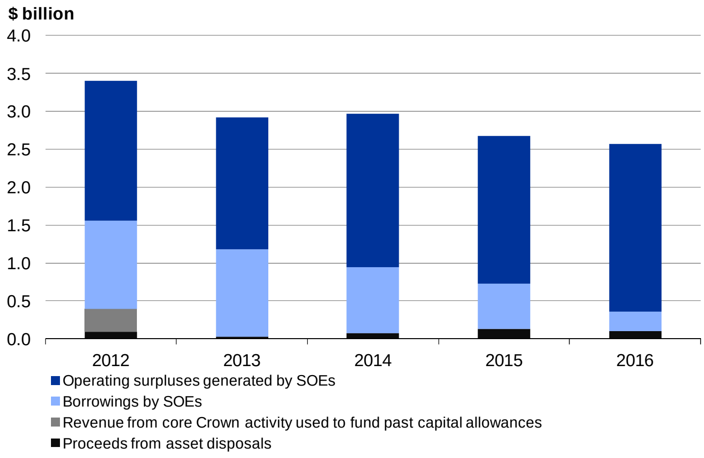
***Figure 2.8*** – Forecast PPE funding sources, 2012 to 2016: Departments and Crown entities




Source: The Treasury

- SOE PPE investment is expected to be largely funded independently of the core Crown (Figure 2.9). Capital allocations from the Crown provide only 2.1% of funding for PPE investment, used to fund commitments made in previous Budgets. The main recipient for this funding is KiwiRail's 'Turnaround Plan'. The remainder of SOE PPE expenditure is forecast to be funded from SOE operating surpluses (67.2%), SOE borrowing (27.8%), and asset disposals within SOEs (2.9%).

***Figure 2.9*** – Forecast PPE funding sources, 2012 to 2016: SOEs



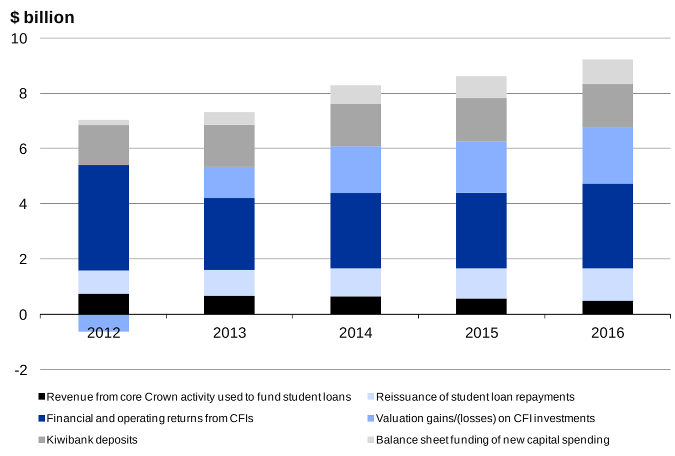

Source: The Treasury

Figure 2.10 presents the forecast funding sources for non-PPE growth. Despite the deterioration in the financial portfolio mentioned earlier, the gains and returns earned from CFI financial assets are expected to be relatively strong beyond 2012, as financial market conditions recover. These financial returns are forecast to fund all asset growth in the CFIs over the next five years, excluding the EQC. It is now expected that Crown operating surpluses will be sufficient to resume contributions to the NZS Fund in the year ending June 2018, a year later than forecast in the *Budget Update.* As this lies beyond the forecast period, no injections of core Crown funding into the NZS Fund occur in the forecasts.

As discussed elsewhere, it is expected that $3.0 billion of funding will be required for new capital spending in future Budgets. The current Government policy is to fund new capital spending initiatives for the next five budgets from its existing balance sheet rather than borrowing to fund these investments. The Government will source funding from alternative sources such as increased returns from existing investments, reprioritisation of planned capital spending, as well as the partial divestment of assets such as SOEs. New spending is not forecast to increase total assets but, rather, to replace existing assets. In total, $4.5 billion of capital spending is expected to be funded ($900 million per Budget for the next five Budgets), once out-years are included.

Of the remaining growth in non-PPE-related assets, growth in the student loan book is expected to be funded from $5.1 billion of student loan repayments, and the remaining $3.1 billion from core Crown revenue. Meanwhile, growth in Kiwibank loans is assumed to be entirely funded through an associated growth in Kiwibank deposits.

***Figure 2.10*** – Forecast Non-PPE funding sources, 2012 to 2016




Source: The Treasury

## Fiscal Forecast Assumptions

The fiscal forecasts are based on assumptions and judgements developed from the best information available on 11 October 2011, when the forecasts were finalised. Actual events are likely to differ from some of these assumptions and judgements. Furthermore, uncertainty around the forecast assumptions and judgements increases over the forecast period. The Canterbury earthquakes add further uncertainty to the economic and fiscal forecasts.

The fiscal forecasts are prepared on the basis of underlying economic forecasts. Such forecasts are critical for determining revenue and expense estimates. For example:

- A nominal GDP forecast is needed in order to forecast tax revenue.
- A forecast of CPI inflation is needed because social assistance benefits are generally indexed to inflation.
- Forecasts of interest rates are needed to forecast finance costs, interest income and discount rates.

A summary of the key economic forecasts that are particularly relevant to the fiscal forecasts is provided in the table below (on a June-year-end basis to align with the Government's balance date).

***Table 2.9*** – Summary of key economic forecasts used in fiscal forecasts

| | 2011/12 | | 2012/13 | 2013/14 | 2014/15 | 2015/16 |
|---|---|---|---|---|---|---|
| **June years** | **Budget forecasts** | **PREFU forecasts** | **PREFU forecasts** | **PREFU forecasts** | **PREFU forecasts** | **PREFU forecasts** |
| Real GDP (P) (ann avg % chg) | 2.5 | 2.8 | 3.4 | 3.2 | 2.8 | 2.3 |
| Nominal GDP (E) ($m) | 209,178 | 211,773 | 221,864 | 234,325 | 246,189 | 256,939 |
| CPI (annual avg % change) | 3.4 | 3.2 | 2.2 | 2.4 | 2.5 | 2.7 |
| Govt 10-year bonds (ann avg %) | 5.7 | 4.5 | 4.5 | 5.0 | 5.2 | 5.4 |
| 5-year bonds (ann avg %) | 5.0 | 3.6 | 3.9 | 4.7 | 5.0 | 5.3 |
| 90-day bill rate (ann avg %) | 2.9 | 2.9 | 3.6 | 4.2 | 4.9 | 5.3 |
| Unemployment rate (ann avg %) | 5.9 | 6.0 | 5.3 | 5.0 | 4.8 | 4.7 |
| Employment (ann avg % change) | 1.3 | 1.7 | 1.4 | 1.5 | 1.4 | 1.2 |
| Current account (% of GDP) | -4.5 | -2.2 | -4.0 | -5.8 | -6.5 | -6.9 |

In addition, there are a number of other key assumptions that are critical in the preparation of the fiscal forecasts.

<table>
<tr><td>Government decisions</td><td>Incorporate government decisions up to 11 October 2011.</td></tr>
<tr><td>Tax revenue</td><td> Tax policy changes announced and enacted by the Government will take place as planned and will affect tax revenue and receipts as calculated and agreed by Inland Revenue and the Treasury. The surge in other persons tax refunds and company tax refunds over the last few years was largely a result of the recession. The forecasts assume that refunds will return to pre-recession trends as the economic recovery gets underway. Utilisation of corporate tax losses to offset future taxable profits will retard the growth of corporate tax up to and including the June 2013 year. Earthquake-related GST refunds will provide a boost to GST refunds throughout the forecast period. GST receipts from earthquake-related spending will provide a temporary boost to gross GST, mostly from 2012 onwards. The total net effect of these two elements will be offset, ignoring any additional spending over and above the insurance claims that may occur. The current unusually large margin between 90-day interest rates and 6-month term deposit rates will be maintained throughout the forecast period, which has a positive influence on resident withholding tax on interest income. </td></tr>
<tr><td>Earthquake costs</td><td>Expenditure (accrual measure) is forecast based on estimates on when key decisions will be taken.  The timing of cash payments is based on estimates of when actual spending will take place. Refer page 15 for further discussion.</td></tr>
<tr><td>Operating allowance</td><td> Net $800 million in Budget 2012 and 2013. Net $1.19 billion from Budget 2014 growing at a rate of 2% per annum for subsequent Budgets. </td></tr>
<tr><td>Capital allowance</td><td> $900 million in Budget 2012 onwards as follows:
<table>
<tr><th>Year ended 30 June<br>$billion</th><th>2011/12<br>Forecast</th><th>2012/13<br>Forecast</th><th>2013/14<br>Forecast</th><th>2014/15<br>Forecast</th><th>2015/16<br>Forecast</th><th>Outside the<br>forecast<br>period</th><th>Total</th></tr>
<tr><td>Budget 2012</td><td>0.1</td><td>0.4</td><td>0.2</td><td>0.1</td><td>0.1</td><td>-</td><td>0.9</td></tr>
<tr><td>Budget 2013</td><td>-</td><td>0.1</td><td>0.4</td><td>0.2</td><td>0.1</td><td>0.1</td><td>0.9</td></tr>
<tr><td>Budget 2014</td><td>-</td><td>-</td><td>0.1</td><td>0.4</td><td>0.2</td><td>0.2</td><td>0.9</td></tr>
<tr><td>Budget 2015</td><td>-</td><td>-</td><td>-</td><td>0.1</td><td>0.4</td><td>0.4</td><td>0.9</td></tr>
<tr><td>Budget 2016</td><td>-</td><td>-</td><td>-</td><td>-</td><td>0.1</td><td>0.8</td><td>0.9</td></tr>
</table>
Funding for new capital spending will be sourced from the existing balance sheet rather than borrowing. </td></tr>
<tr><td>Investment rate of returns</td><td>Incorporate the actual results to 31 August 2011.  Beyond this time, gains on financial instruments are based on long-term benchmark rates of return for each portfolio.</td></tr>
</table>

<table>
<tr><td>Finance cost on new bond issuances</td><td>Based on 5-year rate from the main economic forecasts and adjusted for differing maturity.</td></tr>
<tr><td>Top-down adjustment</td><td>A top down adjustment is made to compensate for departments who tend to forecast upper spending limits (appropriations) rather than best estimates.<br><br>Top-down adjustment to operating and capital as follows:<br><br><table>
<tr><th>Year ending 30 June<br>$billion</th><th>2012<br>Forecast</th><th>2013<br>Forecast</th><th>2014<br>Forecast</th><th>2015<br>Forecast</th><th>2016<br>Forecast</th></tr>
<tr><td>Operating</td><td>1.1</td><td>0.3</td><td>0.1</td><td>0.1</td><td>0.1</td></tr>
<tr><td>Capital</td><td>0.4</td><td>-</td><td>-</td><td>-</td><td>-</td></tr>
</table></td></tr>
<tr><td>Borrowing requirements</td><td>The forecast cash deficits will be met by reducing financial assets and issuing debt.</td></tr>
<tr><td>Property, plant and equipment</td><td>For the purposes of the forecast financial statements, no revaluations of property, plant and equipment are projected beyond the current year. Valuations as recorded for the 2011 annual financial statements and any additional valuations that have occurred up to 31 August 2011 are included in these forecasts.</td></tr>
<tr><td>Student loans</td><td>The carrying value of student loans is based on a valuation model adapted to reflect current student loans policy. As such, the carrying value over the forecast period is sensitive to changes in a number of underlying assumptions, including future income levels, repayment behaviour and macroeconomic factors such as inflation and discount rates used to determine the effective interest rate for new borrowers. Any change in these assumptions would affect the present fiscal forecast.</td></tr>
<tr><td>Government Superannuation Fund and ACC liabilities</td><td>The Government Superannuation Fund and ACC liabilities included in these forecasts have been valued as at 30 June 2011 adjusted for the 31 August 2011 discount rate. Both liabilities are valued by projecting future cash payments, and discounting them to present value. These valuations rely on historical data to predict future trends and use economic assumptions such as inflation and discount rates. Any change in actual payments or economic assumptions would affect the present fiscal forecast. For example, if the discount rate decreases, the value of the liabilities would increase.<br><br>The Government Superannuation Fund's assets are offset against the gross liability and have been updated to reflect market values. The value of assets over the forecast period reflects long-run rate of return assumptions appropriate to the forecast portfolio mix.</td></tr>
</table>

| | |
|---|---|
| Emissions Trading Scheme (ETS) | The forecasts have been prepared in accordance with current government ETS policies. Details of current climate change policies are listed at: www.mfe.govt.nz/issues/climate/policies-initiatives.<br><br>The carbon price assumption for the ETS is based on estimates of the current certified emission reduction (CER) carbon price from Point Carbon, and is €10.40 with an exchange rate of 0.5907 (a carbon price of NZ$17.61) over the forecast period.<br><br>The economic models used to project agriculture and energy activity assume an international carbon price of NZ$25 per tonne to 2012 and NZ$50 to 2020.<br><br>The forecast assumes a 63% uptake of post-1989 foresters into the ETS over Commitment Period One (CP1).<br><br>Revenues and the associated expenses arising from the agriculture sector entering the ETS are included from the June 2015 financial year.<br><br>It is assumed the ETS has no fiscal impact on debt or cash flows, as the net cash impact from the ETS and international obligations is highly uncertain. |
| Kyoto position | The Kyoto position included in the fiscal forecasts reflects the Government's obligation for CP1, from 2008 to 2012. It does not include any future potential reduction of the position through the transfer of units offshore through the forestry sector, or any future changes to the position through transactions under the ETS.<br><br>The carbon price assumption for the Kyoto position is based on estimates of the current assigned amount unit (AAU) carbon price from Point Carbon, and is €7.63 with an exchange rate of 0.5907 (a carbon price of NZ$12.92) over the forecast period. |
| NZS Fund contributions | No contribution is assumed in the forecast period. |

# Medium-term Projections

The preceding parts of this chapter have focused on the fiscal forecasts to the year ending June 2016. This section concentrates on the medium-term fiscal projections, covering the subsequent decade up to and including the year ending June 2026.

At each *Economic and Fiscal Update*, the Treasury produces post-forecast projections of key economic and fiscal variables, such as nominal GDP and net debt. The projections arise from the forecasts, but there are fundamental differences between them. Forecasts are based on comprehensive modelling of economic and fiscal conditions, including the relationships between the two and the impacts of existing or proposed policies. Projections, in contrast, are potential paths of economic and fiscal variables beyond their end-of-forecast values, largely based on historical averages while reflecting existing policy settings. In particular, projections move towards, and then maintain, an assumption of an economy that is growing on trend and free from cycles. Projections also contain no policy responses, beyond those already in existence or to which there is a future commitment, to mitigate unfavourable outcomes or to strengthen positive trends.

### *Updated medium-term projections*

In order to produce post-forecast fiscal variables it is necessary to project forward the economic variables which inform them. For example, tax revenue grows in line with nominal GDP, once a stable economy is attained. The two economic variables that play the biggest roles in fiscal projections are nominal GDP and the rate of inflation, as measured by changes in the CPI.

CPI inflation gradually returns to 2% per year from its end-of-forecast value. This reflects the mid-point of the Reserve Bank's Policy Targets Agreement, which is to keep the CPI-measured annual inflation rate inside a 1% to 3% band.

The CPI inflation projection is added to the projection of real GDP growth to produce the nominal GDP growth projection. This means that there is an implicit assumption that other drivers of nominal GDP, such as the terms of trade, remain at the levels attained at the end of the forecasts.

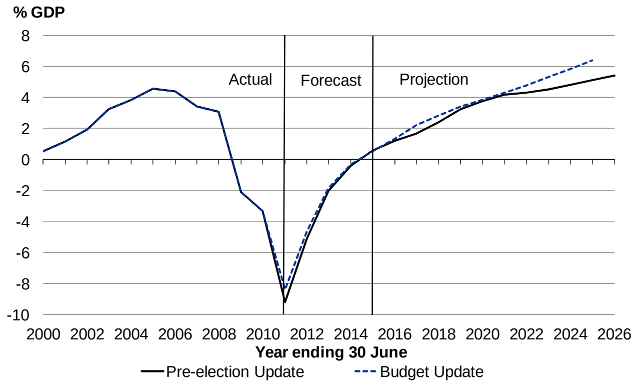
Over the projections, nominal GDP trends down from 5% annual growth in the year ending June 2017 to around 4% per year from the year ending June 2020 onwards. There are a number of factors contributing to this slowing: CPI inflation trending down to 2% per year; economic activity and the labour market returning to more normal levels as the earthquake rebuild winds down; and the aging population slowing growth in the labour force.

The medium-term fiscal projections for the *Pre-election Update* are similar to those produced for the 2011 *Fiscal Strategy Report*. The full recovery of the economy from the impacts of the Global Financial Crisis, as well as those of the Canterbury earthquakes, is still expected to be attained around the end of this decade. The total Crown operating balance before gains/(losses) returns to surplus at the same time, the year ending June 2015, and strengthens beyond that at a relatively similar rate. Core Crown net debt peaks in the forecasts and declines along a path similar to that depicted in the 2011 *Fiscal Strategy Report* projection.

The improvements in the fiscal position over the forecast period, which sees a surplus first achieved in the year ending June 2015, continue into projected years (Figure 2.11). Two factors are primarily responsible for the surplus improving over the projection period.

Firstly, the growth of all core Crown expenses, except for welfare transfers and debt-financing costs, is restricted to the size of the projected allowances for new operating spending. The annual increment to the operating allowance used in the first projected year, the year ending June 2017, is $1.239 billion. In later projected years this amount is increased by 2% per year. As this level of controlled expenditure growth is lower than both historical averages and nominal GDP growth, it plays a major role in maintaining expenses below revenue levels in the projections.

***Figure 2.11*** – Total Crown operating balance before gains/(losses) or OBEGAL

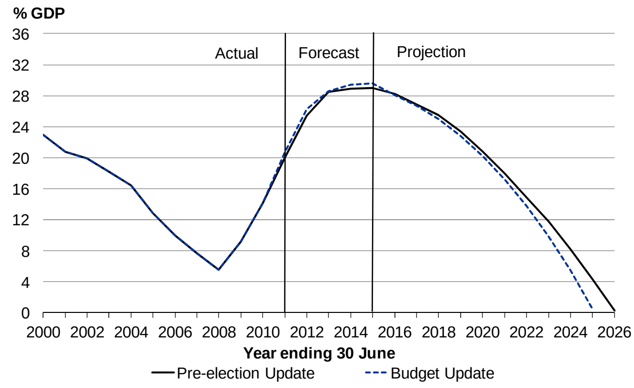



Source: The Treasury

The second factor is strengthening tax revenues, produced by an economy returning to trend and incorporating fiscal drag for the first five projected years. Even after tax recovers to an assumed stable ratio to nominal GDP, based on history, it then grows in line with GDP. As already indicated, this is faster than the driver of most expenses.

While the operating balance before gains/(losses) is the main indicator of fiscal flows, net core Crown debt (excluding the financial assets of the NZS Fund and advances) is the key indicator of the public sector's fiscal stocks. Figure 2.12 depicts net debt to nominal GDP, showing that it peaks at 29% in the year ending June 2015 before steadily declining over the projection period. The attainment of surpluses from the year ending June 2015 onwards enables some of the debt stock to be retired, which in turn helps surpluses to increase by reducing debt-financing costs.

***Figure 2.12*** – Net core Crown debt (excluding NZ Superannuation Fund and advances)

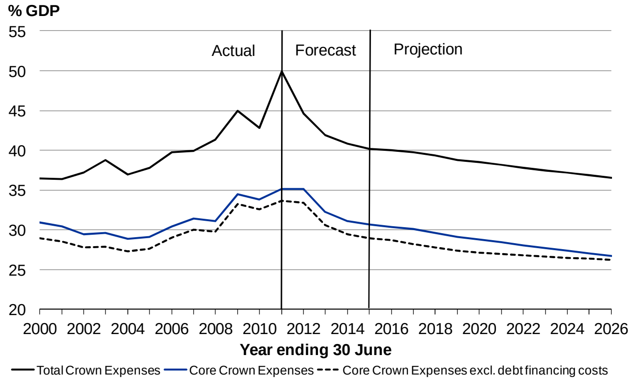



Source: The Treasury

Figure 2.13 shows that core Crown expenses, which spike in the fiscal year just completed mainly owing to one-off costs associated with the earthquakes, are forecast to decline. By the last year of the *Pre-election Update* forecasts they have returned to levels of GDP more like those seen before the Global Financial Crisis. Much of this reduction, which extends into the decade of projections, is owing to reduced operating allowances, relative to their pre-crisis levels, and restricting their growth to 2% per year. Falling debt-financing costs also play a part, as seen by the reduction in the gap between the expenditure measures with and without these costs. By the year ending June 2026 the two lines are only half a percentage point of GDP apart.

While overall expenses are declining, this is not true of all individual spending classes. In particular, gross (of tax) expenditure on NZS increases from 4.4% of nominal GDP in the year ending June 2011 to 6.1% by the end of the projection period, the year ending June 2026. The chief driver of this expense is recipient numbers, with the "65 and over" population expected to grow nearly four times more quickly than the total population over this period.

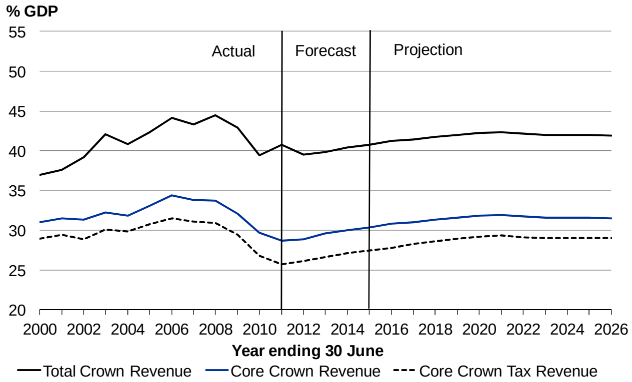
***Figure 2.13*** – Expenses




Source: The Treasury

As the economy recovers, so do tax revenues and other income sources, such as returns on financial assets. This is shown in Figure 2.14. As well as the boosts to tax from more people in employment, companies returning to profit and higher spending, fiscal drag also plays a role. This refers to the case where tax grows faster than the income that generates it, particularly when a taxpayer's income moves into a higher tax bracket. Fiscal drag is only modelled for the first five years of projections, in order to keep the tax-to-GDP ratio around average historical levels. This can be seen where the total Crown revenue line levels out from the year ending June 2021 onwards.

***Figure 2.14*** – Revenue




Source: The Treasury

# Long-term Projections

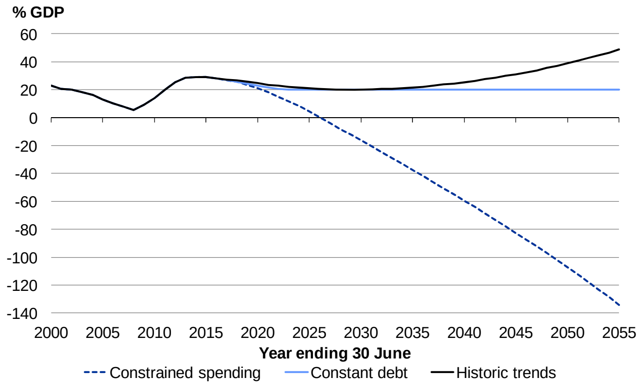
At least every four years the Treasury is required, by legislation, to produce a Statement of the Long-term Fiscal Position. The last Statement was published in October 2009 and can be sourced from the Treasury website at http://www.treasury.govt.nz/government/longterm/fiscalposition.

While a full update of the entire Statement will not be published before late 2012, the fiscal projections have been updated for a *Pre-election Update* base. Three alternative sets of policy assumptions have been modelled in Figures 2.15 and 2.16. These are:

- *Constrained spending* scenario – This assumes core Crown expenses, excluding welfare transfers (which include NZS) and debt-financing costs, derive their growth from projected operating allowances out to the year ending June 2026. In other words, this projection mimics the medium-term projections out to this point. From the year ending June 2027 onwards, the spending classes that derive their growth from the operating allowances, such as health, education and justice, are allowed to revert to historic growth patterns. This means that underlying drivers of their growth, such as labour costs and non-demographic demand factors, return to values that more closely resemble the averages of the past 20 years. Demographic demand reflects the size of their recipient groups over the projected years. In some areas, such as education, this may not be as strong as in the past. In other areas, especially health, the impacts of an aging population drive the growth of projected spending even faster than in recent history.
- *Historic trends* scenario – In this scenario, historic growth drivers for expense classes that derive their growth from the operating allowances in the forecasts are assumed from the beginning of the projections, the year ending June 2017. This is sometimes referred to as a “bottom-up” approach to modelling expenditure growth, in contrast to the “top-down” approach of imposing operating allowance caps. *Historic trends* represents the standard approach followed by most governments in producing long-term fiscal projections.
- *Constant debt* scenario – Both the *Constrained spending* and *Historic trends* scenarios use debt as the residual of their modelling. By this it is meant that revenue, expenses, assets and non-debt liabilities are all modelled, and borrowings are the outcome of combining these under the normal accounting rules. Those two scenarios differ only in the way in which expense growth is projected. By contrast, the *Constant debt* scenario constrains debt to a targeted level of nominal GDP, and expenses are the residual in the modelling. Net core Crown debt is gradually reduced from its end-of-forecast position to 20% of nominal GDP, and then the expense classes that are subject to the operating allowances are constrained to keep net debt at this ratio.

The *Historic trends* scenario follows a similar path to that depicted in the *Fiscal Strategy Report* published with the 2011 *Budget Update*. As was the case in that projection, the net debt track gradually declines to around 20% of nominal GDP before starting to lift again from around the year ending June 2030. This rising net debt track is a fundamental “warning signal” in long-term fiscal projections. Unless ongoing deficits are addressed by changes to fiscal policy settings, the relationship between deficits, borrowings and debt-financing costs will cause the debt track to rise quite rapidly. In other words, the extra borrowings needed to fund an operating deficit increase the stock of debt. This, in turn, increases the level of debt-financing costs generated, which add to the operating deficit. In the absence of any response to this situation, the debt stock and the financing costs it generates continue to supplement each other and the net debt track accelerates upward.

***Figure 2.15*** – Core Crown net debt under three long-term scenarios



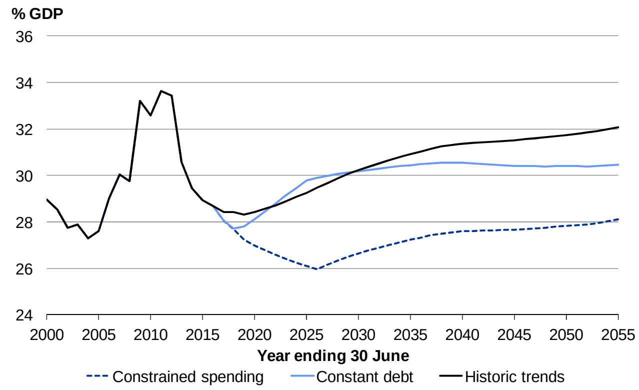

Source: The Treasury

The *Constrained spending* scenario does more than flatten debt, with net debt quickly going negative. This equates to a situation where publicly-held financial assets are in excess of gross debt levels. It is important to note that this scenario is based on the assumption that the Government maintains the tight fiscal strategy outlined in the 2011 *Fiscal Strategy Report*.

Figure 2.16 shows the three tracks of core Crown expenses, excluding debt-financing costs, which correspond to the three net debt scenarios in Figure 2.15.

The *Constant debt* expense path is in line with recent history. However, the composition of future public spending would need to be different under this scenario. NZS nearly doubles as a share of nominal GDP over the projections, rising to just under 8% of nominal GDP by the year ending June 2055. This would mean that at least some other spending areas would have to be reduced from their current ratios to GDP, if a total ratio of just over 30% were to be maintained.

***Figure 2.16*** – Core Crown expenses excluding debt-financing costs under three long-term scenarios




Source: The Treasury

*Historic trends* expenses rise to ratios nearing those of the current earthquake-induced position. However, the rising debt track that corresponds to this implies that this expenditure track would, all other things being equal, produce an unsustainable fiscal position.

The expense track aligned to *Constrained spending* sees expenses fall to levels not seen in recent history. Achieving this track will require ongoing fiscal constraint, especially when it is taken into account that NZS will be close to twice the ratio of GDP that it was when such overall ratios of expenditure to GDP were last achieved.

# Annex: Assumptions for Medium-term Projections

The assumptions for the medium-term economic and fiscal projections are outlined in this section. The full assumptions can be found in the 2011 *Fiscal Strategy Report*, at http://www.treasury.govt.nz/budget/2011/fsr.

***Table 2.10*** – Summary of economic and demographic assumptions*

| June Year[8] | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | ….. | 2026 |
|---|---|---|---|---|---|---|---|---|---|---|---|
| | Forecasts | | | | | Projections | | | | | |
| Labour force | 1.0 | 0.7 | 1.2 | 1.2 | 1.2 | 1.0 | 0.8 | 0.8 | 0.5 | | 0.4 |
| Unemployment rate** | 6.0 | 5.3 | 4.9 | 4.7 | 4.7 | 4.6 | 4.5 | 4.5 | 4.5 | | 4.5 |
| Employment | 1.6 | 1.4 | 1.5 | 1.4 | 1.2 | 1.1 | 0.9 | 0.8 | 0.5 | | 0.4 |
| Labour productivity growth*** | 1.4 | 2.1 | 1.7 | 1.4 | 1.1 | 1.2 | 1.4 | 1.5 | 1.5 | | 1.5 |
| Real GDP | 2.8 | 3.4 | 3.2 | 2.8 | 2.3 | 2.4 | 2.3 | 2.3 | 2.0 | | 2.0 |
| Average hours worked per week**** | 33.2 | 33.2 | 33.2 | 33.2 | 33.2 | 33.2 | 33.2 | 33.2 | 33.2 | | 33.2 |
| Consumers Price Index (annual % change) | 2.2 | 2.5 | 2.3 | 2.6 | 2.8 | 2.6 | 2.4 | 2.2 | 2.0 | | 2.0 |
| Government 5-year bonds (average % rate) | 3.6 | 3.9 | 4.7 | 5.0 | 5.3 | 5.4 | 5.5 | 5.5 | 5.5 | | 5.5 |
| Nominal average hourly wage | 3.6 | 3.5 | 4.1 | 4.2 | 4.1 | 3.8 | 3.8 | 3.7 | 3.5 | | 3.5 |

* Annual average % change unless otherwise stated.

** Level of unemployment (average for year ending June).

*** Hours worked measure.

**** Total hours worked ÷ total number employed.

Sources: The Treasury, Statistics New Zealand

Two economic variables have had their medium-term, stable assumptions changed since the 2011 *Fiscal Strategy Report*. These are the Government 5-year bond rate and the average hours worked per week.

The medium-term, stable assumption for the Government 5-year bond rate has been lowered from the 6% annual value used at the *Fiscal Strategy Report* to 5.5%. Forward interest rates, five and ten years ahead, are now more than 50 basis points lower than they were prior to the Global Financial Crisis. The *Pre-election Update* forecasts reflect this, with lower 5-year bond rates than the *Budget Update* forecasts in every year. The change in the bond rate comes through a lower nominal risk-free rate, owing to lower real growth and inflation rate expectations in safe-haven economies. Since the crisis, and more

[8] Note that the economic forecasts in the *Pre-election Update* are based on a March year.

recently with continued global financial turmoil, forecasters have been revising down long-run forecasts for growth and inflation in advanced economies.

In the long-term projections the Government 5-year bond rate is gradually returned to 6%, reaching this rate by the year ending June 2031 and then remaining at this rate in later years. This reflects the assumption that many of the conditions impacting on the Government bond yield curves may not persist beyond the next decade.

The average hours worked per week has had its medium-term, stable assumption lowered from the 33.6 hours per week used at the 2011 *Fiscal Strategy Report* to 33.2 hours per week. The value in the final year of the *Pre-election Update* forecasts, the year ending June 2016, is 33.2 hours per week, meaning that the new assumption is in place from the first projected year. The change reflects a declining average in recent years, as well as the assumption that an aging population is likely to lead to a lower future value. The next decade, and beyond, will see a greater percentage of the workforce reach the age of eligibility (currently 65) for NZS. Many of these workers will not retire completely, but are likely to switch from full-time to part-time employment or at least reduce their hours of work.

### *Transition of economic variables from the end of forecast*

The stable values assumed for a number of key economic variables, in medium-term projections, reflect their expected levels or growth in a New Zealand economy that is growing on trend and is free from cycles. While such conditions rarely occur, and are temporary when they do, they are appropriate to apply in projections. This is because they occur far enough into the future that it would be difficult, and subject to significant error margins, to predict the onset and duration of any economic perturbations.

Up until mid-2008 the five-year forecast period was generally sufficient for the effects of current cycles and shocks to have worked their way through the economy. This meant that key economic variables could be assumed to be at trend growth rates or levels by the final year of the forecasts. The impact of the Global Financial Crisis meant that it was no longer valid to assume the economy would fully recover within the five-year horizon of the forecasts. Consequently, for a number of variables, transitions back to trend values over the early years of projections became necessary, and this is still the case at the *Pre-election Update*.

Six economic variables are adjusted from their end-of-forecast values. All except the Government 5-year bond rate contribute to the projection of nominal GDP, which is both a driver of a number of important fiscal variables, such as tax revenue, and the underlying deflator of key fiscal indicators.[9] The other five variables are:

- aggregate labour force growth
- CPI inflation
- unemployment rate
- average hours worked, and
- labour force productivity growth.

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9 Most graphs of fiscal indicators, such as core Crown net debt, show the variable as a percentage of nominal GDP. This makes points at various times easier to compare.

For all but aggregate labour force growth, the transition involves selecting a medium-term stable assumption and a rate at which it is approached from the end-of-forecast value. The stable assumption is based on historical data, making allowance for any factors that could alter future values, such as the Policy Targets Agreement with CPI inflation. The rate of adjustment is determined by estimating a plausible path of recovery.

The aggregate labour force growth is not brought to a constant, stable rate. The transition used in this case is to make adjustments in the early projected years to reflect a period of economic rebuilding. When these adjustments dissipate, all growth in later years is aligned to Statistics New Zealand's labour force projections. Historical values of the aggregate labour force participation rate are used to gauge the appropriate adjustments.

***Table 2.11*** – Summary of fiscal assumptions

| | |
|---|---|
| **Tax revenue** | Linked to growth in nominal GDP. Source deductions (mainly PAYE tax on salary and wages) is projected using employment growth and nominal average hourly wage growth. The latter is multiplied by a fiscal drag elasticity of 1.35 for the first five years of projections. The two other major tax categories, corporate tax and other taxes (dominated by GST), are gradually returned from their end-of-forecast values to long-term constant ratios to GDP. Source deductions is also returned to a long-term GDP ratio after fiscal drag modelling ceases. The use of long-term stable tax-to-GDP ratios is to ensure that tax revenue projections are neither higher nor lower than would be expected when the economy is performing at its potential. All tax categories change at a rate of 0.2% of GDP per year, with final ratios-to-GDP of 11.2% for source deductions, 4.5% for corporate tax and 13.0% for other taxes. The long-term ratios are based on historical data, taking into account tax rate and policy changes that could affect them. Once the long-term ratios are reached the tax types remain at them in later projected years. |
| **New Zealand Superannuation (NZS)** | Demographically adjusted and linked to net wage growth, via the "66% wage floor". The latter refers to the net (after-tax) weekly NZS rate for a couple being constrained to lie between 66% and 72.5% of net average weekly earnings. As tax on average weekly earnings, being a part of overall PAYE, increases due to fiscal drag, the net average weekly earnings do not grow as quickly as the gross earnings. |
| **Other benefits** | Demographically adjusted and linked to inflation. |
| **Health, education, justice and other core Crown expense classes** | All growth assumed to come from a share of projected allowances for new operating spending. |
| **Debt-financing costs** | A function of debt levels and interest rates. |
| **Operating allowance** | $1.239 billion in the first projected year, the year ending June 2017. This is based on a $1.19 billion allowance for new operating spending, set for the year ending June 2015, grown at 2% per year from that year. |
| **Capital allowance** | $0.918 billion in the first projected year, the year ending June 2017. Budgets 2012 through to 2016 inclusive assume a $900 million allowance for new capital spending. From Budget 2017 onwards, which coincides with the first projected year, the allowance is assumed to grow at 2% per year. |
| **Surplus DMO financial assets** | $0 billion. |

| | |
|---|---|
| **NZS Fund** | Contributions to the Fund are suspended until they restart in the year ending June 2018. When contributions begin again they are calculated by a methodology consistent with the NZS and Retirement Income Act 2001.[10] |
| **Emissions Trading Scheme (ETS)** | The fiscal impact of the ETS depends on several highly uncertain factors, most notably future carbon prices and New Zealand's emissions targets from future international climate change agreements. The ETS has no impact on debt in the projected years, including and beyond the year ending June 2017. This is because a policy of full recycling of revenue is assumed. Net revenue (the value of credits received after free allocation of credits to participating industries and after meeting future emissions liabilities) is assumed to be recycled back to the public through fiscally equivalent, unspecified tax reductions or spending increases. |
| **Future emissions liabilities** | The Kyoto liability included in fiscal forecasts reflects the government's obligation for Commitment Period One, which is for the period 2008-2012. Projections do not incorporate a quantitative estimate of any net emissions liability that may eventuate from New Zealand's obligations under future international climate change agreements. |

Source: The Treasury

10 The 2011 *Fiscal Strategy Report* provides details on contributions over the forecast and projection periods and more information is available at http://www.treasury.govt.nz/government/assets/nzsf/contributionratemodel

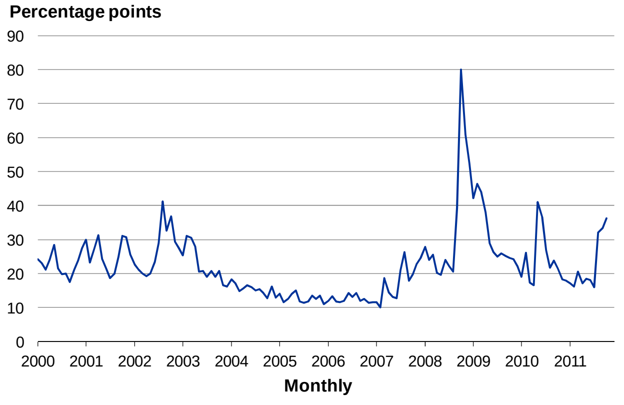
# 3

# Risks and Scenarios

## Introduction

The forecasts presented in the Economic and Fiscal Outlook chapters were produced in some of the most volatile economic and market conditions since the height of the Global Financial Crisis. The Chicago Board Options Exchange Volatility Index – a measure of volatility in the S&P500 index and generally considered to be a proxy for international financial market conditions – rose significantly during the September 2011 quarter and remains elevated.

***Figure 3.1*** – Chicago Board Options Exchange Volatility Index (VIX)




Source: Chicago Board Options Exchange (A higher number means more market volatility is expected over the next 30-day period.)

Against this backdrop, the first part of this chapter outlines key risks to the economic outlook, before presenting a plausible downside alternative scenario for the New Zealand economy. It then focuses on the established channels between the risks facing the real economy and the Crown's fiscal position.

## Economic Risks

### *Global outlook is highly uncertain ...*

Internationally, the biggest uncertainty is over how fast, or even if, policymakers and governments can stabilise financial markets. Our main forecasts assume that the global economy "manages through" in the near term, based on a reasonably orderly resolution of the ongoing sovereign debt problems in the euro area combined with the adoption of additional fiscal stimulus measures in the United States. However, the risks to this view are skewed to the downside. A failure on the part of governments to contain the crisis in the euro area could, in particular, cause a severe disruption to global funding markets.

In contrast to late 2008, there is limited room for policymakers in developed economies to cut official interest rates if such a situation were to occur again. Furthermore, differences of opinion over appropriate policy responses have come to the fore, particularly over fiscal settings in the United States. With private deleveraging set to continue in much of the world, we expect a prolonged period of sub-potential growth in the global economy.

***... posing risks to New Zealand's economy***

The risks to New Zealand from the global economy are threefold. If international activity turns out to be weaker than we have built into our main forecasts, this would reduce demand for our exports. Given the need for sizeable medium-term fiscal consolidation in much of the developed world – not least the United States – there is a great deal of uncertainty over the pace of global growth ahead. And while Asian economies appear to be relatively better placed, policymakers there – particularly in China – face their own challenges from persistently strong inflation and high-valued housing markets.

Our main forecasts assume that the terms of trade decline modestly in the near term but remain high relative to historical standards over the five-year forecast period. Should the terms of trade, in contrast, fall much further and reach their 30-year average, a sharp drop in incomes for agricultural producers would flow through into weaker domestic demand, less income for investment and debt repayment, and a significantly wider current account deficit. Lower commodity prices could also impact on New Zealand goods and services providers that export to Australia, which would also experience a cut in its national income from international commodity sales.

On the financial side, a drop in confidence and pick-up in global risk-aversion would be expected to reduce the availability, and raise the cost, of credit for New Zealand. In light of the recent downgrades to New Zealand's sovereign credit rating by international ratings agencies Fitch and Standard & Poor's, there is a risk that markets would demand a higher risk premium for New Zealand's debt in the future. That said, there is room for the Reserve Bank to provide liquidity as needed, and, if the outlook for inflation permits, to facilitate easier monetary conditions to help domestic borrowers adjust.

***The economy faces existing challenges as well ...***

The domestic economy faces other risks as well. Private consumption growth is expected to be held back by weak house price growth and households' aggregate desire to reduce their debt-to-income ratios to more comfortable levels. Given the wider potential for much tighter conditions in global funding markets, the risk is that the degree of household consolidation could be more intense than expected, with households seeking to move to an even lower level of debt than we have forecast. While this might bring forward the rebalancing that the economy needs in the long run, such a scenario would involve weaker domestic activity in the near term. At present, the risk of a large-scale increase in borrowing by households, reflecting an increased willingness by banks to lend, seems small. However, if this were to occur, it would drive a stronger economy in the near term, but would not prevent the inevitable household rebalancing further out.

***... including ongoing uncertainty over the timing of the Canterbury rebuild ...***

As outlined earlier this year, the timing and extent of the Canterbury earthquake rebuild is difficult to forecast. If significant extra seismic activity causes further damage, the risk that the cost of rebuilding exceeds the current $20 billion estimate factored into our main forecasts would clearly rise, as would the risk that the rebuild would be slower and overall economic activity lower in the short term. Conversely, if seismic activity and insurance-related issues that are currently delaying the process were to be rectified sooner than assumed, the rebuild could gather pace more quickly. Accordingly, residential and non-residential construction, imported goods and employment would all be stronger than in the main forecasts. As a result, we would expect wages in and around the rebuild area to come under upward pressure, as well as prices for some goods – particularly housing goods and services. On top of this, a more rapid rebuild could boost wider confidence in the economy, providing a lift to consumer spending and business investment.

***... and risks from non-economic events***

There are also non-economic risks that may impact on the economy, particularly climatic conditions here and abroad. Poor weather and droughts have adversely affected domestic agricultural production in the past and remain a residual risk. Equally, weather-driven supply shocks in New Zealand's competitor countries also pose risks to the price of New Zealand's exports. There are other inherent risks from a range of environmental events as well, including the potential for biosecurity issues to hit the agricultural sector and the impact of one-off events such as the recent *Rena* shipping incident in the Bay of Plenty.

***There are upside risks, but these are small at present***

The discussion up to now has centred on the negative risks facing the economy, but there are also some positive risks – albeit small at present. Possible factors this time around include the terms of trade holding up higher than forecast and/or a quicker and more decisive resolution to the problems in the euro area (as opposed to the "manage through" assumed in the main forecasts). In addition, a weaker exchange rate profile than we forecast would be expected to provide a competitive boost to New Zealand-based exporters.

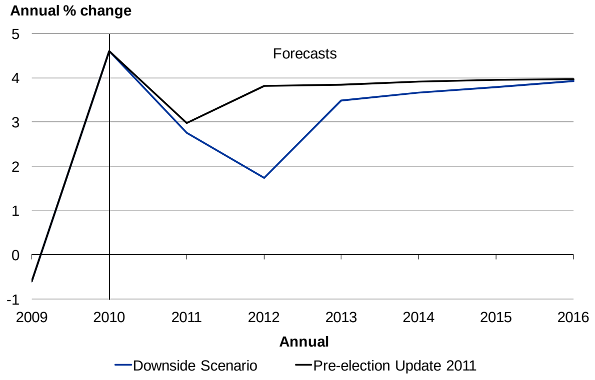
## Downside Scenario

With the balance of probabilities around our main forecasts skewed heavily to the downside, this section presents a downside scenario based on the risks discussed earlier in this chapter. To be clear, the following is just one possible outturn based on a set of risks. It should be considered an illustrative outcome rather than a 'worst case' scenario. The main drivers of this downside scenario are:

- European leaders do not manage to contain the ongoing sovereign debt challenges in the euro area, leading to a significant spike in global risk-aversion and an associated increase in market funding costs.
- With little scope for fiscal and monetary policy in the developed world to step in as it did in 2008, a protracted global recession ensues. The United States and euro area economies contract by 1.5% and 2.0% respectively in the 2012 calendar year, and stage relatively weak recoveries thereafter. Monetary policy around the globe stays supportive for longer.
- An increase in funding costs triggers housing market corrections in a number of Asian economies, exacerbating their economic downturns. Annual Chinese GDP growth slows to 6% in 2012 (versus an average of over 10% per year in the past decade).

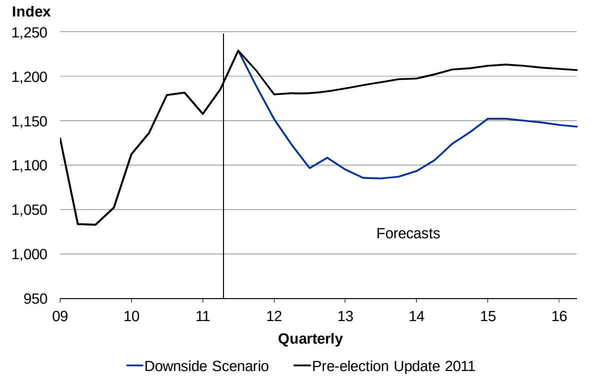
In this scenario, aggregate output in New Zealand's trading partners is approximately 3% lower than the main forecasts in the year ending March 2016. The cumulative loss of trading partner growth over five years is 13.5% of one year's annual GDP. In a deliberate effort to capture the downside risks to the global economy at present, this magnitude is around twice as severe as the IMF's downside scenario from its September 2011 *World Economic Outlook*.

***Figure 3.2*** – Trading partner growth



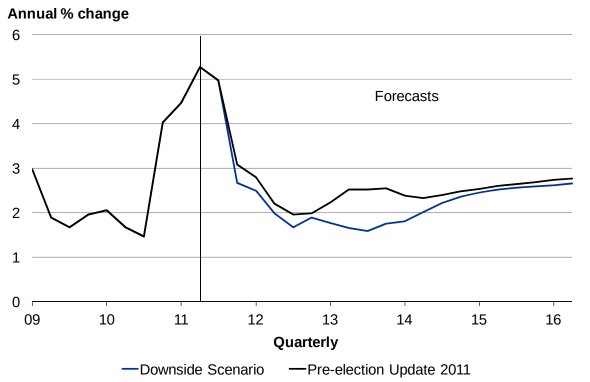

Source: The Treasury

***Figure 3.3*** – Merchandise terms of trade (SNA)



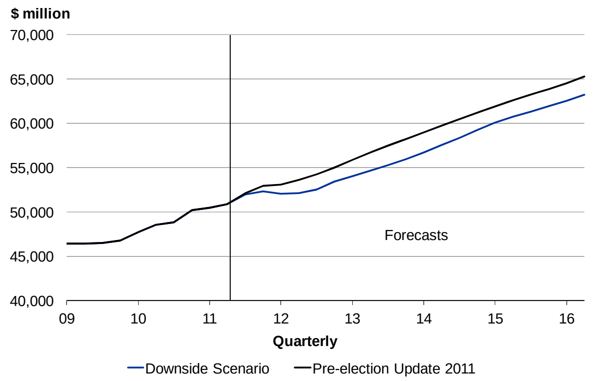

Source: The Treasury

***Figure 3.4*** – Inflation




Source: The Treasury

***Figure 3.5*** – Nominal GDP




Source: The Treasury

The impact on New Zealand of this downside scenario primarily comes through lower demand for our goods and services exports (including inbound tourism), and also lower prices for our key commodity exports – particularly dairy, meat and forestry products. The terms of trade fall sharply, down 7.0% in the year ending March 2013, largely reflecting lower prices for export commodities, and remain below levels incorporated into the main forecasts throughout the forecast period. That said, given their high starting point, the terms of trade remain around 9% higher than their long-run average during the five-year forecast period.

Lower export receipts flow through to a more rapid deterioration in the current account balance in this downside scenario. The current account deficit widens to 4.6% of GDP in the year ending March 2013 (compared with 3.6% in the main forecasts) and to 7.9% by the year ending March 2016 (compared with 6.9%). The exchange rate drops sharply and undershoots in the near term, although in a world of weak monetary settings it does not fall as far as in previous recessions. In this scenario, the trade-weighted exchange rate falls to 63.4 by the middle of the 2012 calendar year – more than 9% lower than in the main forecasts but still higher than the average since 2000 – before regaining some lost ground in 2013. In the near term at least, slower global growth outweighs any competitive boost from a weaker currency.

Lower terms of trade would also hit consumer and business confidence. The levels of both consumer spending and market investment remain below their main tracks throughout the forecast period. The latter is held back by a lack of availability, and the higher cost of credit, reflecting the disruption to global funding markets – another key headwind in this downside scenario.

As in the main forecasts, the Canterbury rebuild is a sizeable mitigating factor in this downside scenario. Residential investment is hit in the near term but recovers as reconstruction funded largely by insurance flows gathers pace over the coming years. While unemployment rises to 6.8% in the mid-2012 calendar year in the scenario – 1.2 percentage points higher than the main forecasts – rebuilding activity helps to bring the rate back down towards the end of the forecast period.

However, the overall impact of weaker economic activity in the short run results in the inflation rate being lower throughout the forecast period, coming in at 1.8% in the March 2013 and 2014 years. Accordingly, short-term interest rates are lower than in the main forecasts. The combination of weaker domestic demand and lower terms of trade means that nominal GDP is a cumulative $35 billion lower through to the year ending June 2016 in the downside scenario. A comparison of the downside scenario with the main forecasts for the key economic variables is given in Table 3.1.

### *Government's fiscal position deteriorates as a result*

Tax revenue in this scenario is lower than in the main forecasts because of weaker growth in the economy. However, the relationship between the performance of the economy and tax revenue is very imprecise. In addition to the negative impact forecast by our model, we have lowered tax revenue by a further cumulative $4 billion over the forecast period in the downside scenario. This adjustment is intended to emphasise the downside risks facing the economy at present and the extra uncertainty that this means for tax revenues (note that GDP is lower in the scenario but so is the ratio of tax to GDP).

Overall, core Crown tax revenue in the scenario is a cumulative $14.5 billion lower through to the year ending June 2016. In contrast to the main forecasts, the total Crown operating balance before gains and losses remains in deficit throughout the forecast period, registering a deficit of 0.5% of GDP in the year ending June 2016 compared with a 1.2% of GDP surplus in the main forecasts. Accordingly, core Crown net debt in the downside scenario rises to 35% of GDP in the year ending June 2016 (from 20% of GDP in 2011) – some 7% of GDP higher than in the main forecasts.

### *Other downside risks not captured in the scenario*

As noted earlier, the downside scenario sets out one plausible scenario of a downside event and should be considered more of an illustrative outcome than a 'worst case'. Overall, historic forecasting performance suggests that there is at least a one-in-five chance of an outcome worse than that captured in the downside scenario. Indeed, there are a number of risks for the economy over and above those captured in the scenario. Specifically, if a variety of factors conspired to result in the exchange rate not depreciating as we expect in the downside scenario, New Zealand would have less of a cushion from the weaker global economy. Meanwhile, to the extent that a stronger exchange rate leads to wider current account deficits than in the downside scenario, New Zealand's external liabilities and potential vulnerabilities would be still higher. Conversely, should the exchange rate depreciate more than we expect in the downside scenario, this would help to cushion the export sector further.

***Table 3.1*** – Summary of key economic variables for main forecasts and scenario

| March years | 2011 Actual | 2012 Forecast | 2013 Forecast | 2014 Forecast | 2015 Forecast | 2016 Forecast |
|---|---|---|---|---|---|---|
| **Real GDP (annual average % change)** | | | | | | |
| **Main forecast** | **1.6** | **2.3** | **3.4** | **3.3** | **2.9** | **2.4** |
| Downside scenario | | 1.7 | 2.5 | 3.6 | 3.2 | 2.6 |
| **CPI inflation (annual % change)** | | | | | | |
| **Main forecast** | **4.5** | **2.8** | **2.2** | **2.4** | **2.5** | **2.7** |
| Downside scenario | | 2.5 | 1.8 | 1.8 | 2.4 | 2.6 |
| **Unemployment rate[1]** | | | | | | |
| **Main forecast** | **6.5** | **5.8** | **5.2** | **4.9** | **4.7** | **4.7** |
| Downside scenario | | 6.5 | 6.3 | 5.8 | 5.1 | 4.7 |
| **Nominal GDP (expenditure measure, $billion)** | | | | | | |
| **Main forecast** | **198** | **209** | **219** | **231** | **243** | **254** |
| Downside scenario | | 207 | 212 | 223 | 235 | 246 |
| **Current Account Balance (% of GDP)** | | | | | | |
| **Main forecast** | **-3.6** | **-2.4** | **-3.6** | **-5.4** | **-6.4** | **-6.9** |
| Downside scenario | | -2.9 | -4.6 | -6.2 | -7.4 | -7.9 |

1 March quarter, seasonally adjusted

Source: The Treasury

## General Fiscal Risks

The discussion up to this point has focused on the main near-term economic risks. The rest of this chapter focuses on the links between the inherent risks to the performance of the economy and the Crown's fiscal position.

Table 3.2 provides some rules of thumb on the sensitivities of the fiscal position to changes in specific variables. For example, if for some reason nominal GDP growth is 1 percentage point slower than we have forecast each year up to the year ending June 2016, we would expect tax revenue to be around $3.5 billion (1.4% of GDP) lower than forecast as a result. The sensitivities are broadly symmetric, ie, if nominal GDP growth is 1 percentage point faster each year than we expect, we would expect tax revenue to be around $3.5 billion *higher* than forecast instead.

### *Fiscal sensitivities*

***Table 3.2*** – Fiscal sensitivity analysis

| **Year ending 30 June ($ million unless stated)** | **2012 Forecast** | **2013 Forecast** | **2014 Forecast** | **2015 Forecast** | **2016 Forecast** |
|---|---|---|---|---|---|
| **1% lower nominal GDP growth per annum on** | | | | | |
| Tax revenue | (549) | (1,171) | (1,876) | (2,650) | (3,492) |
| (% of GDP) | (0.3) | (0.5) | (0.8) | (1.1) | (1.4) |
| **Revenue impact of a 1% decrease in growth of** | | | | | |
| Wages and salaries | (240) | (510) | (812) | (1,153) | (1,532) |
| (% of GDP) | (0.1) | (0.2) | (0.3) | (0.5) | (0.6) |
| Taxable business profits | (96) | (225) | (370) | (526) | (687) |
| (% of GDP) | (0.0) | (0.1) | (0.2) | (0.2) | (0.3) |
| **Impact of 1% pt lower interest rates on** | | | | | |
| Interest income[a] | (116) | (117) | (54) | (87) | (34) |
| (% of GDP) | (0.1) | (0.1) | (0.0) | (0.0) | (0.0) |
| Expenses[a] | (84) | (291) | (378) | (516) | (573) |
| (% of GDP) | (0.0) | (0.1) | (0.2) | (0.2) | (0.2) |
| Overall operating balance | (32) | 173 | 325 | 429 | 540 |
| (% of GDP) | (0.0) | 0.1 | 0.1 | 0.2 | 0.2 |

a New Zealand Debt Management Office holdings only.

Source: The Treasury

### *Revenue risks*

One of the major sources of uncertainty about the fiscal position arises from the inherent uncertainty about future tax revenue. The amount of tax revenue that the government accrues in a given year is closely linked to the performance of the economy.

Figure 3.6 plots our main tax revenue forecast, along with confidence intervals around those forecasts based on Treasury's historical tax forecast errors.[11] The outermost shaded area captures the range (+/- $5 billion in the final year) within which actual tax forecasts would typically fall for 80% of the time.[12] The tax revenue forecast from the downside scenario is also plotted. Tax revenue in the downside scenario is clearly much lower than in the main forecast, but based on average historical forecast errors, there is still a one-in-five chance that tax revenue over the forecast period comes in even weaker than shown here in the downside scenario. Furthermore, with uncertainty currently greater than usual and risks skewed to the downside, the probability of tax revenue undershooting the downside scenario is currently considered to be higher than one in five.

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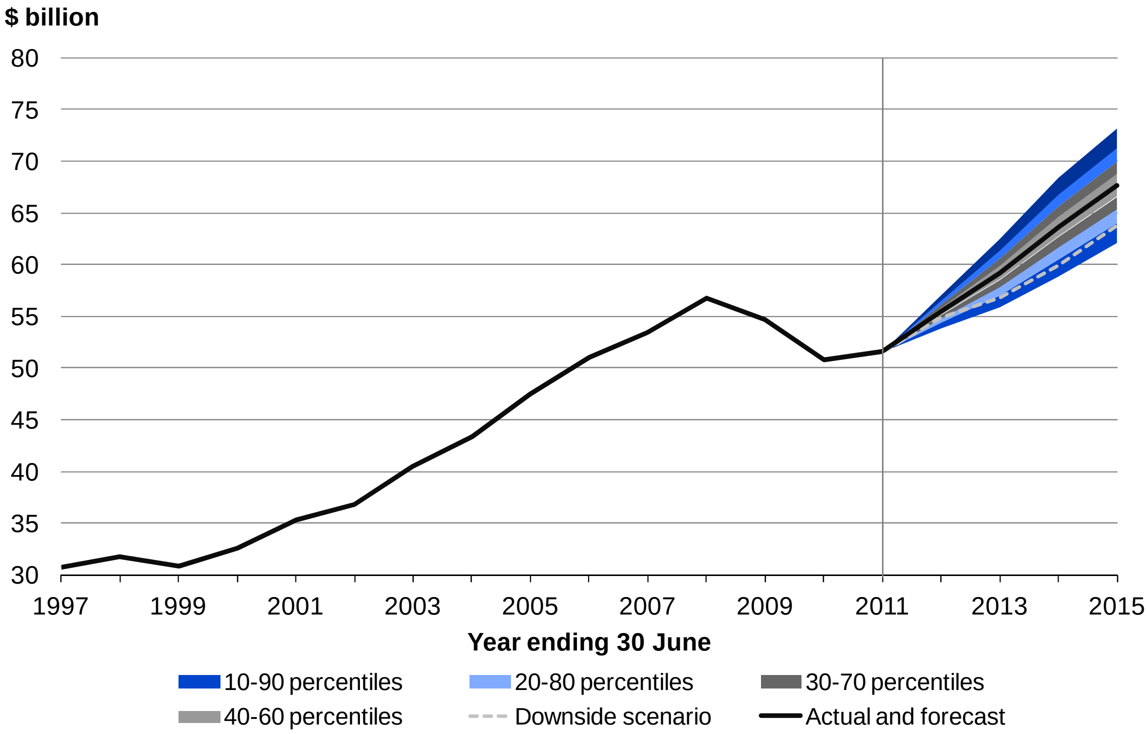
11 A full summary of the methodology and critical assumptions is included in *Treasury Working Paper 10/08*. Standard deviation assumptions used for 0-, 1-, 2- and 3-year ahead forecasts are 2.4%, 4.7%, 6.3% and 6.8% of the actual respectively. These are interpolations of the *Budget Update* forecast estimates, adjusting for the timing of the *Pre-election Update* forecast.

12 Recent Treasury analysis shows that a shock that has a significant and persistent impact on economic growth can result in tax revenues coming in significantly below the outermost shaded area. See Fookes, C (2011), "Modelling shocks to New Zealand's fiscal position," *Treasury Working Paper 11/02.*

***Figure 3.6*** – Core Crown tax revenue uncertainty




Source: The Treasury

### *Expenditure risks*

One-off and unexpected expenditure shocks can have a large impact on the Crown's operating balance in the year that they occur. Persistent errors in forecasting the cost of various programmes (ie, policies that end up costing more than the Government allows for) can also have substantial ongoing effects on the fiscal position.

There is also considerable uncertainty with regard to the performance of the economy on Crown expenditures too. This uncertainty largely relates to the operation of the so-called automatic stabilisers. For example, if the economy performs better (worse) than expected in a given year, official expenditures on social programmes may be lower (higher) than planned, and tax revenues higher (lower).

Meanwhile, the destructive seismic events of recent years have underlined the inherent exposure of the Crown's fiscal position to exogenous shocks on the capital side. The Government's fiscal position would be impacted if another catastrophic earthquake were to occur or if the costs associated with the recent events exceed the updated estimates. The ageing population also presents risks to the medium-term fiscal position, particularly to the extent that demographic forecasts may prove to be too low or high.

### *Balance sheet risks*

In addition to the primary risks facing the public finances, the Crown's balance sheet faces risks on a number of fronts too.[13] One of the main risks in this regard is to the net worth of the Crown's financial assets from movements in financial markets – particularly relating to interest and exchange rates and equity prices. Examples of these funds include the NZS Fund and the Accident Compensation Scheme (ACC). The Crown Ownership Monitoring Unit estimates that the Crown's overall financial portfolio has an asset beta of 0.45 relative to global equity markets. This means that if the MSCI World Equity Index were to fall (rise) by 10%, the value of the Crown's investments would be expected to fall (rise) by 4.5%.

The Crown also faces liquidity risk, and in extreme instances could potentially encounter difficulty in meeting financial obligations as they fall due. However, the bulk of research suggests that such a scenario is very unlikely and the Government has liquid buffers to help cope with such events.

### *Funding risks*

As noted in the Economic Outlook chapter, while our main forecasts were finalised before the recent downgrades of New Zealand's credit rating by Standard & Poor's and Fitch, the market reaction since then means that our forecasts for interest rates in the near term are still appropriate. For now, New Zealand is on a stable outlook with all three major credit ratings agencies and the Crown holds the top Aaa foreign currency rating from Moody's and stable AA foreign currency ratings from Standard & Poor's and Fitch.

Nonetheless, in the absence of a marked improvement in the external position, New Zealand may be more likely to be singled out in the funding markets in the future. All things being equal, any further deterioration in the ratings outlook could serve to raise debt-servicing costs for the Crown as well as borrowing rates for households and businesses.

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[13] For a more detailed discussion see the Crown's *Investment Statement 2010* as well as the *Supplement to the Investment Statement 2010*.

# 4

# Specific Fiscal Risks

The most significant economic risks have been identified in Chapter 3. The Statement of Specific Fiscal Risks is a requirement of the Public Finance Act 1989 and sets out all pending government decisions and other circumstances known to the Government at the finalisation of the fiscal forecasts that may have a material effect on the fiscal and economic outlook, but are not certain enough in timing or amount to include in the fiscal forecasts. It is not possible to identify every possible risk and disclosure is also subject to legal requirements and materiality thresholds, which are described after the Statement of Specific Fiscal Risks.

## Overview of Specific Fiscal Risks

Specific fiscal risks can be positive or negative and can affect revenue or spending. The links between external events and spending are indirect because new policies that change spending and revenue usually require a decision by the Government and approval from Parliament. The approach taken in this chapter is to disclose those pending policy decisions and key areas of uncertainty that may have a material effect on the fiscal outlook. The specific fiscal risks are categorised into:

- **Pending policy decisions affecting revenue:** Changes to tax policy or ACC levies could reduce or increase government income.
- **Pending policy decisions affecting expenses:** Costs of policy proposals could increase or decrease expenses depending on decisions taken, and they are risks to the extent that they cannot be managed within baselines or budget allowances.
- **Pending capital decisions:** Capital investment decisions are risks to the extent that they cannot be managed within balance sheets or budget allowances.
- **Matters dependent on external factors:** The liability of the Government for costs is sometimes dependent on external factors such as the outcome of negotiations or international obligations.

Some key examples of the risks disclosed in this chapter are outlined below:

- government decisions relating to the recommendations of the Welfare Working Group and the redesign of business processes at Inland Revenue
- specific policies that may have flow-on costs that are not accounted for within allocated funding, such as early childhood education funding, but are not likely enough to include in the forecasts

- explicit guarantees that give assurance to the public and businesses about the Crown's planned response to specific events are recognised as risks; the largest current guarantee relates to the Extended Deposit Guarantees Scheme with a total value of $1.3 billion, and
- generic cross-government risks such as the renegotiation of collective employment agreements that could have material costs and flow-on effects to remuneration in other sectors.

General cost pressures, such as those associated with an ageing population, are not recognised as specific fiscal risks.

The new risks that have been added since the *Budget Update* include:

- how the Government will respond to the Waitangi Tribunal report on the Wai 262 claim
- a change in the legal interpretation of when work-related gradual process disease and infection claims should be recognised may have an impact on the fiscal position, and
- the response to the *Rena* cargo ship grounding on Astrolabe reef.

The costs of individual natural disasters, and other major events, are not recognised as specific fiscal risks in advance as they usually occur infrequently and their timing cannot be predicted. Once a disaster does occur, a number of choices arise about how to respond and when potential liabilities are recognised. Specific risks are disclosed at this point based on the range of possible responses.

In Budget 2011 the Government established the Canterbury Earthquake Recovery Fund (CERF). The CERF is $5.5 billion and this is an estimate of the core Crown's costs of earthquake recovery. There are a large number of earthquake-related risks that, if they occur, may exhaust the capacity of the CERF. These risks include government commitments where the final cost is not yet known and policy options where decisions have not yet been taken. The risks have been aggregated and are not quantified because it is unclear which risks will be realised and what the scale of these risks would be.

In addition to the obligations and policy choices for the Government, the disasters in Canterbury and elsewhere have placed pressure on private sector insurers. As a result, the cost of insurance premiums is likely to increase over the next five years with potential flow-on effects to the Crown. The potential Earthquake Commission impact has now been recognised as a separate risk.

The final part of the chapter contains a current list of contingent liabilities, which are likely costs that the Crown will have to face if a particular event occurs. Typically, contingent liabilities consist of guarantees and indemnities, legal disputes and claims on uncalled capital. The largest quantified contingent liabilities are to international financial organisations and mostly relate to uncalled capital and promissory notes.

# Statement of Specific Fiscal Risks

## Summary Table

The matters listed below are disclosed as specific fiscal risks because they meet the rules for disclosure outlined at the end of the chapter. Full descriptions of the risks listed below are set out in the next section.

| Specific fiscal risks as at 18 October | Status | Value of risk |
|---|---|---|
| **Pending policy decisions affecting revenue** | | |
| ACC – Levies | Changed | Unquantified |
| Finance – Mixed Ownership Model | Unchanged | Unquantified |
| Revenue – Apportionment Rules for Mixed-Use Assets | Changed | Unquantified |
| Revenue – Income-Sharing Tax Credits | Unchanged | $500 million per annum |
| Revenue – Potential Tax Policy Changes | Changed | Unquantified |
| Revenue – Salary Trade-Offs | Changed | Unquantified |
| Services funded by Third Party Revenue | Changed | Unquantified |
| **Pending policy decisions affecting expenses** | | |
| Climate Change – Review of the Emissions Trading Scheme | Changed | Up to $585 million operating expenses |
| Education – Early Childhood Education Funding | Changed | Unquantified |
| Education – Upward Adjustment for School Operating Funding | Unchanged | Unquantified |
| Government Response to Wai 262 | New | Unquantified |
| Housing – Reform of Social Housing | Changed | Unquantified |
| Revenue – KiwiSaver Auto-Enrolment | New | $350 to $550 million operating expenses |
| Revenue – Transformation and Technology Renewal | Changed | Unquantified |
| Reviews of Public Services | Unchanged | Unquantified |
| Social Development – Welfare Working Group Recommendations | Changed | Unquantified |
| State Sector Employment Agreements | Unchanged | Unquantified |
| **Pending capital decisions** | | |
| Agriculture and Forestry – Investment in Water Infrastructure | Changed | Unquantified |
| Departmental Capital Intentions | Unchanged | Unquantified |
| Finance – Crown Overseas Properties | Unchanged | $150 million capital expenditure |
| Transport – Support for New Zealand Railways Corporation | Changed | Unquantified |

| Specific fiscal risks as at 18 October | Status | Value of risk |
|---|---|---|
| **Matters dependent on external factors** | | |
| ACC – Non-Earners' Account | Changed | Unquantified |
| ACC – Work-related Gradual Process Disease and Infection | New | Unquantified |
| ACC, Education, Health, Social Development – Caregiver Employment Conditions | Changed | Unquantified |
| Canterbury Earthquake – AMI Support Package | Changed | Unquantified |
| Canterbury Earthquake – EQC | New | Unquantified |
| Canterbury Earthquake – Exceeding the CERF | Changed | Unquantified |
| Climate Change – Finance for Developing Countries | Unchanged | Unquantified |
| Climate Change – International Climate Change Obligations | Unchanged | Unquantified |
| Climate Change – Kyoto Protocol Obligations | Unchanged | Unquantified |
| Communications – Potential Impairment in Value of Broadband Investment | Changed | Unquantified |
| Defence Force – Asset Valuations | New | Unquantified |
| Defence Force – Future Operationally Deployed Forces Activity | Changed | $10 to $30 million operating expenses per annum |
| Energy – Crown Revenue from Petroleum Royalties | Unchanged | Unquantified |
| Finance – Entities in Receivership under Crown Retail Deposit Guarantee Scheme | Unchanged | Unquantified |
| Finance – Extended Crown Retail Deposit Guarantee Scheme | Changed | Unquantified |
| Finance – Government Commitments to International Financial Institutions | Changed | Unquantified |
| Health – Payment of Family Caregivers | Unchanged | Unquantified |
| Revenue – Cash Held in Tax Pools | Unchanged | Unquantified |
| Transport – Response to the MV Rena Grounding | New | Unquantified |
| Treaty Negotiations – Treaty Settlement Forecast | Unchanged | Unquantified |
| Treaty Negotiations – Relativity Clause | Unchanged | Unquantified |

## Statement of Specific Fiscal Risks

***Pending policy decisions affecting revenue***

*ACC – Levies (Changed, Unquantified)*

Changes in tax settings, economic factors and ACC's financial performance affect ACC's expenses and levy income. If ACC's performance as a result of any of these factors is different from what is forecast, ACC may increase or decrease levies. An increase or decrease in levies has a flow-on impact on total Crown revenue with a corresponding impact on the operating balance before gains and losses.

*Finance – Mixed Ownership Model (Unchanged, Unquantified)*

The Government is considering applying the type of Mixed Ownership Model that is currently used for Air New Zealand to Genesis Energy, Meridian Energy, Mighty River Power and Solid Energy, and further reducing the Crown's shareholding in Air New Zealand. The final amount and timing of any cash proceeds, the flow-on effects for future dividend streams and any implementation costs are uncertain.

*Revenue – Apportionment Rules for Mixed-Use Assets (Changed, Unquantified)*

An issues paper has been released on the apportionment rules that apply to tax deductions for assets which are used to earn income and which are also partly used for private purposes. Any changes to those rules will have a positive impact on tax revenue.

*Revenue – Income-Sharing Tax Credits (Unchanged, Quantified)*

The Government has introduced legislation to establish an income-sharing tax credit. If passed as introduced, the legislation will allow couples with children under the age of 18 to pool their earnings for income tax purposes if they meet certain criteria. If implemented, the changes will reduce tax revenues by $500 million per annum once the scheme is fully operational. The Finance and Expenditure Committee has reported back recommending that the significant fiscal cost of the package be addressed before the Bill proceeds further.

*Revenue – Potential Tax Policy Changes (Changed, Unquantified)*

The tax policy work programme announced by the Government includes a number of items which are under consideration, including:

- the tax treatment of charitable giving
- the imputation system
- amortisation of capital-raising costs
- the international tax review
- the GST treatment of cross-border business activities
- the tax treatment of hybrid instruments
- the dividend review, and
- the review of specified minerals rules.

The Government aggregates the revenue impacts of most tax policy changes, and measures on the work programme are expected to be revenue-neutral or positive in aggregate.

*Revenue – Salary Trade-Offs (Changed, Unquantified)*

The Government is reviewing the tax treatment of employee benefits traded off for salary, including the treatment of car parks. Any changes are expected to result in an increase in tax revenues.

*Services funded by Third Party Revenue (Changed, Unquantified)*

A wide range of government activities are funded through third party fees and charges. Demand for these services can vary, which has a direct effect on revenue. There is a risk that changes will be required to the way services are delivered, which could result in costs to the Crown.

***Pending policy decisions affecting expenses***

*Climate Change – Review of the Emissions Trading Scheme (Changed, Quantified)*

A statutory review of the ETS was published on 15 September 2011, which included recommendations to change the ETS settings with an estimated fiscal cost of up to $585 million between 2013 and 2020, calculated at a $25 carbon price. These estimates are subject to change, based on emissions forecasts and the carbon price. There are other recommendations that have not yet been quantified fully by officials, as well as potential savings that could be used to achieve a fiscally neutral outcome.

*Education – Early Childhood Education Funding (Changed, Unquantified)*

Rising demand for Early Childhood Education (ECE) services and increased costs associated with inflation have the potential to raise the costs of Government subsidies to ECE services.

*Education – Upward Adjustment for School Operating Funding (Unchanged, Unquantified)*

The Government has increased school operating grants in Budget 2011 to help meet increased costs associated with inflation. A risk remains that similar cost pressures will need to be addressed in future years.

*Government Response to Wai 262 (New, Unquantified)*

The Waitangi Tribunal released its report on the Wai 262 claim on 2 July 2011. The report focuses on the protection of Māori culture and identity, with a particular focus on mātauranga Māori and associated taonga. The Tribunal's recommendations are directed towards a number of Government agencies individually, as groups and across sectors. The Government is currently considering the Tribunal's report and recommendations to fully understand their implications (including any fiscal implications).

*Housing – Reform of Social Housing (Changed, Unquantified)*

The Government has decided to change the policy settings for social housing. This includes increasing third party providers of social housing, increasing the effectiveness of financial assistance and focusing Housing New Zealand Corporation on providing social housing to those with the greatest housing need. Plans for implementation remain under development, but potentially represent a significant fiscal risk to the Crown. However, there may be offsetting financial benefits to the Crown if significant gains in efficiency are achieved.

*Revenue – KiwiSaver Auto-Enrolment (New, Quantified)*

In Budget 2011 the Government announced its intention to consult on the design of a one-off KiwiSaver auto-enrolment exercise to increase the number of KiwiSaver members. The Government has recently announced that it intends to proceed with auto-enrolment in 2014/15 subject to returning to surplus as planned. Depending on the timing, design features and take-up rate, an auto-enrolment exercise is likely to entail a one-off cost for kick-start payments to new members and ongoing additional costs for the Member Tax Credit. These costs could be in the order of $350 to $550 million over the first four years after the auto-enrolment took place.

*Revenue – Transformation and Technology Renewal (Changed, Unquantified)*

Inland Revenue is exploring options that will fundamentally change the way it manages its processes and data, in order to deliver smarter, modern services for less. Technology renewal is a key enabler to support Inland Revenue's future business model and focuses on sustaining current systems (ie, minimising known risks within existing technology), through to significant business process and technology changes. Any changes could impact tax revenue collections and/or have material administrative costs to implement.

*Reviews of Public Services (Unchanged, Unquantified)*

The Government has initiated a series of reviews to improve the effectiveness and efficiency of public services. Reviews may recommend, or result in, changes to service delivery and/or free up resources for reprioritisation within Votes or be used to meet pressures in other areas.

*Social Development – Welfare Working Group Recommendations (Changed, Unquantified)*

The Government is considering its response to the recommendations of the Welfare Working Group. Many of the recommendations would result in large upfront costs if adopted. The Government will make policy and funding decisions over the next year.

*State Sector Employment Agreements (Unchanged, Unquantified)*

A number of large collective agreements are due to be renegotiated in the short-to-medium term. As well as direct fiscal implications from any changes to remuneration, the renegotiation of these agreements can have flow-on effects to remuneration in other sectors. The Government has signalled an expectation of restraint given the current economic environment.

***Pending capital decisions***

*Agriculture and Forestry – Investment in Water Infrastructure (Changed, Unquantified)*

In Budget 2011 the Government established a funding programme to support potential irrigation development projects to an investment-ready stage. The Government intends to consider investing up to $400 million of equity for the construction and operation of water harvesting, storage and off-farm distribution infrastructure as part of Budget 2013. The proposal will provide detailed advice on the key investment principles and the provision of a clear separation in the Crown's role in supporting scheme development and investment decisions.

*Departmental Capital Intentions (Unchanged, Unquantified)*

The Government requires 15 capital-intensive agencies to identify their capital spending intentions over the next 10 years based on current policy settings and certain demographic and inflation assumptions. The difference between capital intentions and currently available funding is material but the Government expects that these intentions will be managed back through a range of measures such as prioritisation, changes to asset utilisation, alternative methods of service delivery and changes to policy settings. Departmental capital intentions are risks to the extent that they cannot be managed through these mechanisms or funded through existing funding sources.

*Finance – Crown Overseas Properties (Unchanged, Quantified)*

The Government holds New Zealand House in London on a long-term lease from the Crown Estate (UK). Depending on the Government's future intentions for this building, an upgrade may be required. Preliminary cost estimates for this upgrade total $150 million over the period 2012/13 to 2014/15.

*Transport – Support for New Zealand Railways Corporation (Changed, Unquantified)*

The Government has agreed in principle to support a 10-year strategy for the New Zealand Railways Corporation (NZRC, trading as KiwiRail Group) to achieve a commercially viable rail network. A total of $750 million in capital over the years to 2012/13 is forecast as the Crown contribution towards the strategy, but its disbursement will be dependent on the approval of suitable business cases and demonstrable progress towards objectives. Budgets 2010 and 2011 provided $500 million in capital towards the strategy. KiwiRail will be submitting a case for the third tranche of the $750 million as part of Budget 2012.

KiwiRail has signalled that completing the strategy will require $243 million in 2013 and $90 million in 2014. These costs are consistent with the $1.1 billion expected over the life of the plan, but are not yet funded.

KiwiRail also has $442 million in debt to the Crown maturing in the forecast period, all of which may need to be refinanced. In Budget 2011 $250 million was refinanced and $180 million falls due in 2012/13.

***Matters dependent on external factors***

*ACC – Non-Earners' Account (Changed, Unquantified)*

Changes in tax settings, economic factors and ACC's financial performance affect the Crown's liability for claims by non-earners. This is most evident in changes in discount rates that affect the Outstanding Claims Liability. If ACC's performance is different from what is forecast as a result of any of these factors, the amount required to cover the costs of non-earners' claims for that year may be more or less than needed, resulting in unplanned savings or costs to the Crown.

*ACC – Work-related Gradual Process Disease and Infection (New, Unquantified)*

The Department of Labour, in conjunction with the ACC, is seeking Crown Law advice to clarify the legal interpretation of when Work-related Gradual Process Disease and Infection claims should be recognised: at the date that someone first presents to a health provider with an injury (ACC's current interpretation) or the date that a person is first exposed to the injury-causing event. If the interpretation is the latter, ACC would need to recognise the additional liability.

*ACC, Education, Health, Social Development – Caregiver Employment Conditions (Changed, Unquantified)*

On 12 September 2011 the Government approved a negotiated settlement for sleepover providers whose service contracts are funded from Vote Health. The Government will contribute to the employers' payment of backpay and increased wages but the increased service cost to Health has only been partially funded. There is also a risk that this decision will have implications for other Crown-funded services, resulting in flow-on costs in ACC, Education and Social Development.

*Canterbury Earthquake – AMI Support Package (Changed, Unquantified)*

The net cost to the Crown of the AMI Support Package is currently estimated to be $335 million. The two main risks around this estimate are the ultimate cost of claims related to the Canterbury earthquakes (around which there is still considerable uncertainty) and the level of proceeds from the sale of the remaining good AMI business. Although the risks could be positive or negative, the reported claims liability estimates are based on the 75th percentile of the Appointed Actuary's estimated distribution of claims and therefore include a significant contingency against further deterioration.

*Canterbury Earthquake – EQC (New, Unquantified)*

The Crown faces increased risk relating to the Earthquake Commission's (EQC) disaster cover because the Natural Disaster Fund (NDF) is expected to be depleted after settling current Canterbury earthquake claims. The Government is liable to meet any deficiency in the EQC's assets required to fund future claims under section 16 of the Earthquake Commission Act 1993.

The deficiency in the EQC's assets as a result of the Canterbury earthquakes is estimated at $490 million and the core Crown's net debt has increased to allow for this shortfall. The estimated amount is based on a number of forecast assumptions, including:

- an actuarial estimate of the EQC's outstanding claims liability at 30 June 2011 (net of reinsurance recoveries)
- expected future levy income, and
- forecasts of ongoing operational costs, including reinsurance.

There is a high degree of uncertainty regarding the final cost of claims and reinsurance recoveries, which means the extent to which the EQC's assets are deficient is also highly uncertain. Measures to manage the risk associated with the deficiency in the short term, such as the purchase of additional reinsurance, may have a fiscal impact.

Future earthquakes or other natural disasters would increase the Crown's liability under section 16.

Given the significant impact of the Canterbury earthquakes on the Commission and its NDF the EQC may be reviewed, which could have a fiscal impact.

*Canterbury Earthquake – Exceeding the CERF (Changed, Unquantified)*

The Christchurch Earthquake Recovery Fund (CERF) was established in Budget 2011 to meet the Crown's costs of the Canterbury earthquakes. There are a number of pending decisions and possible eventualities that result in a risk that the CERF may be exceeded. These include:

- Land decisions – many properties are still classified as orange or white. Further decisions on land zoning and associated Government policies have yet to be made. These may increase costs to the Crown. There is also a risk that the forecast net cost to the Crown of current Crown offers is understated, mainly due to uncertainty about the extent of recoveries from insurance.
- Demolition and rockfall – the costs of demolition and mitigating rockfall risk are highly uncertain. The Crown may be required to provide a contribution towards costs not met by other parties.
- Infrastructure – not all damage to infrastructure has been fully assessed. There is a risk that the damage is greater than currently expected, which would increase the costs to the Crown.
- Contribution to Council costs – cost-sharing arrangements are yet to be finalised. There is a risk that the Crown share is greater than forecast, which would increase the costs to the Crown. This includes any potential Crown contribution towards the Central Business District Plan costs.

*Climate Change – Finance for Developing Countries (Unchanged, Unquantified)*

There is an international expectation that developed countries, including New Zealand, contribute finance to developing countries to support adaptation to, and mitigation of, the effects of climate change. Developed countries have committed to mobilising $US100 billion per year by 2020 to address the needs of developing countries. This would come from a wide variety of sources, both public and private.

*Climate Change – International Climate Change Obligations (Unchanged, Unquantified)*

The Government is currently taking part in international negotiations for a post-2012 international climate change agreement. Currently no rights or obligations are included in the fiscal forecasts for any post-2012 agreement because of the high levels of uncertainty. Any agreement could have significant financial implications, and will need to be recognised at the time.

*Climate Change – Kyoto Protocol Obligations (Unchanged, Unquantified)*

The fiscal impact of the Government's Kyoto Protocol obligations (2008 to 2012) is currently uncertain. An increase in New Zealand's net emissions or the future transfer of emission units offshore could reduce the net Kyoto position significantly. Increased allocation to emitters or increased participation by foresters under the ETS would negatively impact the Government's ETS position. The fiscal impact of any changes is dependent on the carbon price. The Government may also need to purchase emission units to meet its obligations, which would have a corresponding impact on net debt.

*Communications – Potential Impairment in Value of Broadband Investment (Changed, Unquantified)*

The Government has committed to capitalise Crown Fibre Holdings with $1.345 billion so that it can invest with private partners in a new network delivering “ultra fast” broadband services. Crown Fibre Holdings has entered into contracts with several partners. Given the nature of the investments made, it is possible that the full value of the investments will not be recovered. The fiscal forecasts include a provision for this impairment, but the final amount of the impairment may vary from this provision.

*Defence Force – Asset Valuations (New, Unquantified)*

The New Zealand Defence Force is undertaking a wide-ranging review and implementing actions to improve its business as a result of the recent Defence White Paper. The work is expected to test assumptions around asset valuations and operating norms, which may lead to changes to valuations and have an impact on the operating balance.

*Defence Force – Future Operationally Deployed Forces Activity (Changed, Quantified)*

New Zealand Defence Force personnel are deployed overseas on peace-keeping and United Nations missions. Deployments come with the risk of unforeseen events happening that could incur large costs – for example, the loss of a major military asset in a hostile environment. In addition, maintaining existing deployment levels would result in increased annual operating funding being required. The magnitude of both of these is estimated to be between $10 million and $30 million annually (but could potentially exceed this), subject to any decisions to change existing deployments.

*Energy – Crown Revenue from Petroleum Royalties (Unchanged, Unquantified)*

The Crown Revenue from Petroleum Royalties is very dependent upon the US dollar value per barrel of oil and the exchange rate. Movements up or down in either of these variables could result in a significant decrease or increase in the Crown revenue. The overall impact for the Crown could therefore be negative or positive. In addition, the Government is currently reviewing the regulatory, royalty and taxation arrangements for petroleum as part of the Petroleum Action Plan. Although the outcomes of this review are still uncertain, any changes to policies in this area could have a significant impact on future revenue from petroleum royalties.

*Finance – Entities in Receivership under Crown Retail Deposit Guarantee Scheme (Unchanged, Unquantified)*

Eight entities that were guaranteed under the original Deposit Guarantee Scheme and one that was guaranteed under the extended scheme are now in receivership. The Crown recognises its obligations under the schemes as liabilities and its rights of recovery from the receivers as assets. While the reported assets represent the receivers’ best prudent estimates of likely recoveries from the receiverships, the eventual return to the Crown is uncertain and dependent upon the value that can be realised from these entities’ assets.

*Finance – Extended Crown Retail Deposit Guarantee Scheme (Changed, Unquantified)*

There are three financial institutions participating in the extended Retail Deposit Guarantee Scheme, which ends on 31 December 2011. These entities have deposits totalling $1.3 billion covered by the guarantee and are listed on the Treasury website. This is the maximum exposure and does not include any offset resulting from the recovery of the remaining assets of financial institutions in the event the guarantee is called upon. The entities participating in the extended scheme are currently assessed as unlikely to default and therefore no provision is considered necessary in relation to the amount guaranteed by the Crown under the extended guarantee. While this represents a best estimate of the expected outcome, a range of outcomes is possible if entities default, including eventual loss to the Crown.

*Finance – Government Commitments to International Financial Institutions (Changed, Unquantified)*

The forecast level of government commitments to international financial institutions is subject to change, depending on the Government's response to any changed financial plans on the part of these institutions. The risk of government commitments to the International Monetary Fund being called has increased due to the Global Financial Crisis and recent world events, including in the Euro area.

*Health – Payment of Family Caregivers (Unchanged, Unquantified)*

The Human Rights Tribunal and High Court have ruled that the Ministry of Health's policy of not employing family members to provide care to disabled relatives is in breach of section 19 of the New Zealand Bill of Rights. Leave has been granted to appeal to the Court of Appeal.

*Revenue – Cash Held in Tax Pools (Unchanged, Unquantified)*

Funds held in tax pools are recognised as an asset to the Crown. There is a risk that funds held in these pools, over and above a customer's provisional tax liability, may be withdrawn, resulting in an unquantified cash loss to the Crown.

*Transport – Response to the MV Rena Grounding (New, Unquantified)*

On Wednesday 5 October the cargo ship *MV Rena* was grounded on the Astrolabe Reef. The grounding resulted in New Zealand's largest marine oil spill. The *Rena* has a number of containers with hazardous substances in them. Some containers have fallen into the sea and more may also fall. Maritime New Zealand (MNZ) must maintain a reserve to fund an initial response to an oil pollution event and at 30 June 2011 this stood at $3.5 million. The fiscal forecasts also include an additional $12.1 million that the Government has approved for MNZ to fund the clean-up. Under the Maritime Transport Act 1994, some costs of a clean-up can be sought from the polluter. The total cost of the clean-up, salvage response and the contribution of the polluter are not yet known, and therefore additional funding may be required.

*Treaty Negotiations – Treaty Settlement Forecast (Unchanged, Unquantified)*

The fiscal forecasts include provision for the cost of future Treaty settlements. There is a risk that the timing and amount of the settlements could be different from what is forecast. It is not possible to reliably estimate the value of this difference.

*Treaty Negotiations – Relativity Clause (Unchanged, Unquantified)*

The Deeds of Settlement negotiated with Waikato-Tainui and Ngāi Tahu include a relativity mechanism. The mechanism provides that, where the total redress amount for all historical Treaty settlements exceeds $1 billion in 1994 present-value terms, the Crown is liable to make payments to maintain the real value of Ngāi Tahu's and Waikato-Tainui's settlements as a proportion of all Treaty settlements. The agreed relativity proportions are 17% for Waikato-Tainui and approximately 16% for Ngāi Tahu. There is a risk that the timing and the amount of the expense for the relativity payments may differ from that included in the fiscal forecasts.

## Risks Removed Since the 2011 BEFU

The following risks have been removed since the *Budget Economic and Fiscal Update*:

| **Expired risks** | **Reason** |
|---|---|
| Defence Force - Sale of Skyhawks and Aermacchi Trainers | Decision taken to dispose of Skyhawks and Aermacchi Trainers element does not meet materiality threshold |
| Housing - Weathertight Homes | No longer material |
| Justice - Legal Aid | Some decisions taken, no longer material |
| Revenue - Child Support | No longer material |
| Revenue - Student Loans Redesign | Decision taken |
| Social Development – ServiceLink | Project scaled back, no longer material |
| State Services – KiwiSaver Contribution | Decision taken, risk now managed within departments |

## Criteria and Rules for Inclusion in the Fiscal Forecasts or Disclosure as Specific Fiscal Risks

The Public Finance Act requires that the Statement of Specific Fiscal Risks sets out all government decisions, contingent liabilities or contractual obligations known to the Government and subject to specific requirements that may have a material effect on the economic or fiscal outlook.[14]

The criteria and rules set out below are used to determine if government decisions or other circumstances should be incorporated into the fiscal forecasts, disclosed as specific fiscal risks or, in some circumstances, excluded from disclosure.

## Criteria for Including Matters in the Fiscal Forecasts

Matters are incorporated into the fiscal forecasts provided they meet the following criteria:

- The matter can be quantified for particular years with reasonable certainty.
- A decision has been taken, or a decision has not yet been taken but it is reasonably probable[15] the matter will be approved, or it is reasonably probable the situation will occur.

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[14] The Statement of Specific Fiscal Risks is a requirement set out in sections 26Q and 26U of the Public Finance Act 1989.

[15] For these purposes “reasonably probable” is taken to mean that the matter is more likely than not to be approved within the forecast period (by considering, for example, whether there is a better than 50% chance of the matter occurring or being approved).

Additionally, any other matters may be incorporated into the forecasts if the Secretary to the Treasury considers, using his best professional judgement, that the matters may have a material effect on the fiscal and economic outlook and are certain enough to include in the fiscal forecasts.

## Rules for the Disclosure of Specific Fiscal Risks

Matters are disclosed as specific fiscal risks if:

- the likely cost is more than $100 million over five years, and either
- a decision has not yet been taken but it is reasonably possible[16] (but not probable) that the matter will be approved or the situation will occur, or
- it is reasonably probable that the matter will be approved or the situation will occur, but the matter cannot be quantified or assigned to particular years with reasonable certainty.

Additionally, any other matters may be disclosed as specific fiscal risks if the Secretary to the Treasury considers, using his best professional judgement, that the matters may have a material effect (more than $100 million over five years) on the fiscal and economic outlook but are not certain enough to include in the fiscal forecasts.

## Exclusions from Disclosure

Matters are excluded from disclosure as specific fiscal risks if they fail to meet the materiality criterion (ie, are less than $100 million over five years), or if they are unlikely[17] to be approved or occur within the forecasting period.

Additionally, the Minister of Finance may determine that a matter be included in the fiscal forecasts or a specific fiscal risk not be disclosed, if such disclosure would be likely to:

- prejudice the substantial economic interests of New Zealand
- prejudice the security or defence of New Zealand or international relations of the Government
- compromise the Crown in a material way in negotiation, litigation or commercial activity, or
- result in a material loss of value to the Crown.

If possible, the Minister of Finance should avoid withholding the matter either by making a decision on it before the forecasts are finalised, or by disclosing it as an unquantified risk.

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16 For these purposes "reasonably possible" is taken to mean that the matter might be approved within the forecast period (by considering, for example, whether there is a 20% to 50% chance of the matter occurring or being approved).

17 For these purposes "unlikely" is taken to mean that the matter will probably not be approved within the forecast period (by considering, for example, whether there is a less than 20% chance of the matter occurring or being approved).

## Contingent Liabilities

Contingent liabilities are:

- costs that the Crown will have to face if a particular event occurs, or
- present liabilities that are unable to be measured with sufficient reliability to be recorded in the financial statements (unquantifiable liabilities).

Typically, contingent liabilities consist of guarantees and indemnities, legal disputes and claims, and uncalled capital. The contingent liabilities facing the Crown are a mixture of operating and balance sheet risks, and they can vary greatly in magnitude and likelihood of realisation. In general, if a contingent liability were realised, or the amount becomes sufficiently reliable to record as a liability, it would reduce the operating balance and net worth and increase gross sovereign-issued debt. However, in the case of contingencies for uncalled capital, the negative impact would be restricted to gross sovereign-issued debt.

Where contingent liabilities have arisen as a consequence of legal action being taken against the Crown, the amount shown is the amount claimed and thus the maximum potential cost. It does not represent either an admission that the claim is valid or an estimation of the amount of any award against the Crown.

Only contingent liabilities involving amounts of over $10 million are separately disclosed. Contingent liabilities less than $10 million are included in the “other quantifiable contingent liabilities” total. Comparatives have been adjusted where appropriate to align with the disclosure of new “material” contingent liabilities. The total amount of prior years’ contingent liabilities remains unchanged.

Contingent liabilities have been stated as at 30 June 2011, being the latest set of published contingent liabilities.

Details of each of the following contingent liabilities can be accessed from the Treasury website at http://www.treasury.govt.nz/budget/forecasts/prefu2011.

## Quantifiable Contingent Liabilities

| **Guarantees and indemnities** | **Status**[18] | **($ million)** |
|---|---|---|
| Air New Zealand – letters of credit and performance bonds | Unchanged | 34 |
| Cook Islands – Asian Development Bank loans | Unchanged | 12 |
| Indemnification of receivers and managers – Terralink Limited | Unchanged | 10 |
| Ministry of Transport – funding guarantee | Unchanged | 10 |
| Other guarantees and indemnities | Unchanged | 12 |
| | | **78** |
| **Uncalled capital** | | |
| Asian Development Bank | Unchanged | 2,995 |
| Bank for International Settlements | Unchanged | 23 |
| European Bank for Reconstruction and Development | Unchanged | 12 |
| International Bank for Reconstruction and Development | Unchanged | 991 |
| Other uncalled capital | Unchanged | 12 |
| | | **4,033** |
| **Legal proceedings and disputes** | | |
| Health – legal claims | Unchanged | 18 |
| Tax disputes | Unchanged | 281 |
| Other legal proceedings and disputes | Unchanged | 32 |
| | | **331** |
| **Other quantifiable contingent liabilities** | | |
| Air New Zealand partnership | Unchanged | 77 |
| Crown Health Financing Agency | Unchanged | 24 |
| Inland Revenue Department – unclaimed monies | Unchanged | 55 |
| International finance organisations | Unchanged | 1,254 |
| Kyoto Protocol units | Unchanged | 997 |
| New Zealand Export Credit Office – export guarantees | Unchanged | 132 |
| NZTA – Auckland City Council | Unchanged | 10 |
| Reserve Bank – demonetised currency | Unchanged | 23 |
| Other quantifiable contingent liabilities | Unchanged | 127 |
| | | **2,699** |
| **Total quantifiable contingent liabilities** | | **7,141** |

18 Relative to reporting in the *Financial Statements of the New Zealand Government for the year ending 30 June 2011*.

## Unquantifiable Contingent Liabilities

| Guarantees and indemnities | Status |
|---|---|
| Air New Zealand | Unchanged |
| Airways Corporation of New Zealand | Unchanged |
| AsureQuality Limited | Unchanged |
| At Work Insurance Limited | Unchanged |
| Bona Vacantia property | Unchanged |
| Building Industry Authority | Unchanged |
| Civil Defence Emergency Management – New Zealand Local Authorities | Unchanged |
| Contact Energy Limited | Unchanged |
| Deposit Guarantee Schemes | Unchanged |
| Electricity Corporation of New Zealand Limited | Unchanged |
| Genesis Energy – financial guarantees | Unchanged |
| Genesis Energy – letters of credit and performance bonds | Unchanged |
| Housing New Zealand Corporation | Unchanged |
| Indemnities against acts of war and terrorism | Unchanged |
| Justices of the Peace, Community Magistrates and Disputes Tribunal Referees | Unchanged |
| Landcorp Farming Limited | Unchanged |
| Maui Partners | Unchanged |
| Meridian Energy – letters of credit and performance bonds | Unchanged |
| National Provident Fund | Unchanged |
| New Zealand Railways Corporation | Unchanged |
| Persons exercising investigating powers | Unchanged |
| Public Trust | Unchanged |
| Reserve Bank of New Zealand | Unchanged |
| Synfuels-Waitara Outfall Indemnity | Unchanged |
| Tainui Corporation | Unchanged |
| Canterbury Earthquakes: | |
| Earthquake Commission | Unchanged |
| Land Zones | Unchanged |
| Civil Defence Emergency Management – Canterbury Local Authorities | Unchanged |
| Properties acquired under the Canterbury Red Zone Support Package | Unchanged |

## Unquantifiable Contingent Liabilities (continued)

| **Other unquantifiable contingent liabilities** | |
|---|---|
| Abuse claims | Unchanged |
| Accident Compensation Corporation litigations | Unchanged |
| Air New Zealand litigation | Unchanged |
| Environmental liabilities | Unchanged |
| Family caregivers | Unchanged |
| Kordia Group Limited | Unchanged |
| Maui Contracts | Unchanged |
| Rugby World Cup 2011 | Unchanged |
| Television New Zealand | Unchanged |
| Treaty of Waitangi claims | Unchanged |
| Treaty of Waitangi claims – settlement relativity payments | Unchanged |
| Westpac New Zealand Limited | Unchanged |

| **Contingent assets** | |
|---|---|
| Legal proceedings and tax disputes | Unchanged |
| Suspensory loans to integrated schools | Unchanged |

# 5

# Forecast Financial Statements

These forecasts have been prepared in accordance with the Public Finance Act 1989.

They are based on the accounting policies and assumptions that follow. As with all such assumptions, there is a degree of uncertainty surrounding them. This uncertainty increases as the forecast horizon extends.

The forecasts have been prepared in accordance with the Statement of Responsibility and reflect the judgements and information known at the time they were prepared. They reflect all government decisions and circumstances communicated to 11 October 2011.

The key assumptions that underpin the preparation of the Forecast Financial Statements are outlined on pages 33 to 36.

# Statement of Accounting Policies

## Significant Accounting Policies

These forecast financial statements have been prepared in accordance with the accounting policies that are expected to be used in the comparable audited actual financial statements of the Government.

These forecast financial statements comply with generally accepted accounting practice (GAAP) as required by the Public Finance Act 1989 and have been prepared in accordance with *Financial Reporting Standard 42: Prospective Financial Statements*.

All forecasts use the accrual basis of accounting. Forecasts have been prepared for the consolidated financial statements of the government reporting entity, which includes all entities controlled by the Government (as defined by applicable financial reporting standards).

The specific accounting policies are reproduced in full on the Treasury's website at http://www.treasury.govt.nz/publications/guidance/reporting/accounting.

## Changes in Accounting Policies

All policies have been applied on a consistent basis during the forecast period. There have been no changes in accounting policies during the period.

## Forecast Policies

These forecast financial statements have been prepared on the basis of the Treasury's best professional judgement.

Actual financial results for the periods covered are likely to vary from the information presented. Factors that may lead to a material difference between information in these forecast financial statements and the actual reported results in future years are set out in the chapter on Fiscal Risks on pages 57 to 74.

Key forecast assumptions used are set out on pages 33 to 36.

# Government Reporting Entity as at 11 October 2011

These forecast financial statements are for the government reporting entity as specified in Part 3 of the Public Finance Act 1989. This comprises Ministers of the Crown and the following entities:

## Core Crown

**Departments**

| | |
|---|---|
| Agriculture and Forestry | Land Information New Zealand |
| Building and Housing | Māori Development |
| Canterbury Earthquake Recovery Authority | New Zealand Customs Service |
| Conservation | New Zealand Defence Force |
| Corrections | New Zealand Police |
| Crown Law Office | New Zealand Security Intelligence Service |
| Culture and Heritage | Office of the Clerk of the House of Representatives |
| Defence | Pacific Island Affairs |
| Economic Development | Parliamentary Counsel Office |
| Education | Parliamentary Service |
| Education Review Office | Prime Minister and Cabinet |
| Environment | Science and Innovation |
| Foreign Affairs and Trade | Serious Fraud Office |
| Government Communications Security Bureau | Social Development |
| Health | State Services Commission |
| Inland Revenue | Statistics New Zealand |
| Internal Affairs | Transport |
| Justice | Treasury |
| Labour | Women's Affairs |
| **Offices of Parliament** | **Others** |
| Controller and Auditor General | New Zealand Superannuation Fund |
| The Ombudsmen | Reserve Bank of New Zealand |
| Parliamentary Commissioner for the Environment | |

## State-owned enterprises

| | |
|---|---|
| AMI Insurance Limited* | Mighty River Power Limited |
| Air New Zealand Limited* | New Zealand Post Limited |
| Airways Corporation of New Zealand Limited | New Zealand Railways Corporation |
| Animal Control Products Limited | Quotable Value Limited |
| AsureQuality Limited | Solid Energy New Zealand Limited |
| Electricity Corporation of New Zealand Limited | Terralink Limited (in liquidation) |
| Genesis Power Limited | Transpower New Zealand Limited |
| Kordia Group Limited | |
| Landcorp Farming Limited | *Subsidiaries of SOEs are consolidated by their parents and not listed separately in this table* |
| Learning Media Limited | |
| Meridian Energy Limited | * *included for disclosure purposes as if they were an SOE* |
| Meteorological Service of New Zealand Limited | |

## Crown entities

- Accident Compensation Corporation
- Alcohol Advisory Council of New Zealand
- Arts Council of New Zealand Toi Aotearoa
- Broadcasting Commission
- Broadcasting Standards Authority
- Career Services
- Charities Commission
- Children's Commissioner
- Civil Aviation Authority of New Zealand
- Commerce Commisson
- Crown Health Financing Agency
- Crown Research Institutes (8)
- District Health Boards (20)
- Drug Free Sport New Zealand
- Earthquake Commission
- Electricity Authority
- Electoral Commission
- Energy Efficiency and Conservation Authority
- Environmental Protection Authority
- External Reporting Board
- Families Commission
- Financial Markets Authority
- Government Superannuation Fund Authority
- Guardians of New Zealand Superannuation
- Health and Disability Commissioner
- Health Quality and Safety Commission
- Health Research Council of New Zealand
- Health Sponsorship Council
- Housing New Zealand Corporation
- Human Rights Commission
- Independent Police Conduct Authority
- Law Commission
- Maritime Safety Authority of New Zealand
- Mental Health Commission
- Museum of New Zealand Te Papa Tongarewa Board
- New Zealand Antarctic Institute
- New Zealand Artificial Limb Board
- New Zealand Blood Service
- New Zealand Film Commission
- New Zealand Fire Service Commission
- New Zealand Historic Places Trust (Pouhere Taonga)
- New Zealand Lotteries Commission
- New Zealand Productivity Commission
- New Zealand Qualifications Authority
- New Zealand Symphony Orchestra
- New Zealand Teachers Council
- New Zealand Tourism Board
- New Zealand Trade and Enterprise
- New Zealand Transport Agency
- New Zealand Venture Investment Fund Limited
- New Zealand Walking Access Commission
- Office of Film and Literature Classification
- Pharmaceutical Management Agency
- Privacy Commissioner
- Public Trust
- Radio New Zealand Limited
- Real Estate Agents Authority
- Retirement Commissioner
- School Boards of Trustees (2,481)
- Social Workers Registration Board
- Sport and Recreation New Zealand
- Standards Council
- Takeovers Panel
- Te Reo Whakapuaki Irirangi (Te Māngai Pāho)
- Te Taura Whiri i te Reo Māori (Māori Language Commission)
- Television New Zealand Limited
- Tertiary Education Commission
- Tertiary education institutions (29)
- Testing Laboratory Registration Council
- Transport Accident Investigation Commission

*Crown entity subsidiaries are consolidated by their parents and not listed separately in this table*

## Organisations named or described in Schedule 4 of the Public Finance Act 1989

- Agriculture and Marketing Research and Development Trust
- Asia New Zealand Foundation
- Crown Fibre Holdings Limited
- Dispute Resolution Services Limited
- Fish and Game Councils (12)
- Health Benefits Limited
- Leadership Development Centre Trust
- Learning State Limited
- National Pacific Radio Trust
- New Zealand Fish and Game Council
- New Zealand Game Bird Habitat Trust Board
- New Zealand Government Property Corporation
- New Zealand Lottery Grants Board
- Ngāi Tahu Ancillary Claims Trust
- Pacific Co-operation Foundation
- Pacific Island Business Development Trust
- Research and Education Advanced Network New Zealand Limited
- Reserves Boards (23)
- Road Safety Trust
- Sentencing Council
- Te Ariki Trust
- The Māori Trustee

# Forecast Statement of Financial Performance

## for the years ending 30 June

| | Note | 2011 Actual $m | 2012 Previous Budget $m | 2012 Forecast $m | 2013 Forecast $m | 2014 Forecast $m | 2015 Forecast $m | 2016 Forecast $m |
|---|---|---|---|---|---|---|---|---|
| **Revenue** | | | | | | | | |
| Taxation revenue | 1 | 51,128 | 54,690 | 54,957 | 58,571 | 62,885 | 66,869 | 70,642 |
| Other sovereign revenue | 1 | 5,281 | 5,808 | 5,563 | 5,731 | 6,118 | 6,366 | 6,951 |
| **Total revenue levied through the Crown's sovereign power** | | **56,409** | **60,498** | **60,520** | **64,302** | **69,003** | **73,235** | **77,593** |
| Sales of goods and services | | 15,084 | 16,078 | 16,825 | 17,314 | 18,426 | 19,164 | 19,941 |
| Interest revenue and dividends | 2 | 2,570 | 3,051 | 2,814 | 3,308 | 3,688 | 4,259 | 4,537 |
| Other revenue | | 7,500 | 3,106 | 3,478 | 3,563 | 3,698 | 3,778 | 3,816 |
| **Total revenue earned through the Crown's operations** | | **25,154** | **22,235** | **23,117** | **24,185** | **25,812** | **27,201** | **28,294** |
| **Total revenue (excluding gains)** | | **81,563** | **82,733** | **83,637** | **88,487** | **94,815** | **100,436** | **105,887** |
| **Expenses** | | | | | | | | |
| Transfer payments and subsidies | 3 | 22,172 | 22,926 | 22,580 | 23,175 | 23,686 | 24,540 | 25,591 |
| Personnel expenses | 4 | 19,088 | 19,149 | 19,536 | 19,773 | 19,967 | 20,219 | 20,490 |
| Depreciation and amortisation | 5 | 4,682 | 4,631 | 4,562 | 4,797 | 4,931 | 4,988 | 5,067 |
| Other operating expenses | 5 | 35,829 | 37,792 | 40,685 | 35,782 | 36,180 | 36,720 | 37,505 |
| Interest expenses | 6 | 3,596 | 4,685 | 3,959 | 4,464 | 4,901 | 5,389 | 5,458 |
| Insurance expenses | 7 | 14,592 | 3,138 | 3,751 | 4,140 | 4,405 | 4,298 | 4,841 |
| Forecast new operating spending | 8 | - | 463 | 473 | 1,094 | 1,788 | 2,932 | 3,959 |
| Top-down expense adjustment | 8 | - | (310) | (1,100) | (300) | (100) | (100) | (100) |
| **Total expenses (excluding losses)** | | **99,959** | **92,474** | **94,446** | **92,925** | **95,758** | **98,986** | **102,811** |
| **Operating balance before gains/(losses)** | | **(18,396)** | **(9,741)** | **(10,809)** | **(4,438)** | **(943)** | **1,450** | **3,076** |
| Net gains/(losses) on financial instruments | 9 | 4,619 | 1,973 | (4) | 1,588 | 2,055 | 2,062 | 2,132 |
| Net gains/(losses) on non-financial instruments | 10 | 79 | 172 | (2,064) | 191 | 170 | 176 | 185 |
| **Total gains/(losses)** | | **4,698** | **2,145** | **(2,068)** | **1,779** | **2,225** | **2,238** | **2,317** |
| Net surplus from associates and joint ventures | | 237 | 303 | 276 | 284 | 294 | 286 | 308 |
| **Operating balance (including minority interest)** | | **(13,461)** | **(7,293)** | **(12,601)** | **(2,375)** | **1,576** | **3,974** | **5,701** |
| Attributable to minority interest | | 101 | - | - | - | - | - | - |
| **Operating balance** | 11 | **(13,360)** | **(7,293)** | **(12,601)** | **(2,375)** | **1,576** | **3,974** | **5,701** |

*The accompanying notes and accounting policies are an integral part of these Statements.*

# Forecast Statement of Financial Performance (continued) – Functional Expense Analysis

## for the years ending 30 June

| | 2011 Actual $m | 2012 Previous Budget $m | 2012 Forecast $m | 2013 Forecast $m | 2014 Forecast $m | 2015 Forecast $m | 2016 Forecast $m |
|---|---|---|---|---|---|---|---|
| **Total Crown expenses** | | | | | | | |
| **By functional classification** | | | | | | | |
| Social security and welfare | 25,324 | 26,353 | 26,047 | 27,182 | 28,054 | 28,961 | 30,335 |
| GSF pension expenses | 311 | 311 | 210 | 307 | 387 | 442 | 474 |
| Health | 13,068 | 13,787 | 13,809 | 13,676 | 13,594 | 13,597 | 13,597 |
| Education | 12,406 | 13,005 | 13,052 | 12,987 | 12,957 | 13,116 | 13,336 |
| Core government services | 5,515 | 5,440 | 7,018 | 4,300 | 4,395 | 4,366 | 4,287 |
| Law and order | 3,567 | 3,745 | 3,823 | 3,750 | 3,724 | 3,737 | 3,748 |
| Defence | 1,778 | 1,872 | 1,856 | 1,876 | 1,827 | 1,825 | 1,823 |
| Transport and communications | 8,402 | 8,584 | 8,943 | 8,939 | 9,192 | 9,448 | 9,733 |
| Economic and industrial services | 18,818 | 7,758 | 8,884 | 8,413 | 8,766 | 8,626 | 9,120 |
| Primary services | 1,603 | 1,700 | 1,710 | 1,652 | 1,654 | 1,656 | 1,639 |
| Heritage, culture and recreation | 3,437 | 3,327 | 3,898 | 3,015 | 3,039 | 3,329 | 3,704 |
| Housing and community development | 1,655 | 1,119 | 1,158 | 1,082 | 1,094 | 1,177 | 1,213 |
| Other | 479 | 635 | 706 | 488 | 486 | 485 | 485 |
| Finance costs | 3,596 | 4,685 | 3,959 | 4,464 | 4,901 | 5,389 | 5,458 |
| Forecast new operating spending | - | 463 | 473 | 1,094 | 1,788 | 2,932 | 3,959 |
| Top-down expense adjustment | - | (310) | (1,100) | (300) | (100) | (100) | (100) |
| **Total Crown expenses excluding losses** | **99,959** | **92,474** | **94,446** | **92,925** | **95,758** | **98,986** | **102,811** |

*Below is an analysis of core Crown expenses by functional classification. Core Crown expenses include expenses incurred by Ministers, Departments, Offices of Parliament, the NZS Fund and the Reserve Bank, but not Crown entities and State-owned enterprises.*

| | 2011 Actual $m | 2012 Previous Budget $m | 2012 Forecast $m | 2013 Forecast $m | 2014 Forecast $m | 2015 Forecast $m | 2016 Forecast $m |
|---|---|---|---|---|---|---|---|
| **Core Crown expenses** | | | | | | | |
| **By functional classification** | | | | | | | |
| Social security and welfare | 22,005 | 22,935 | 22,560 | 23,252 | 23,829 | 24,471 | 25,536 |
| GSF pension expenses | 305 | 302 | 201 | 298 | 377 | 433 | 464 |
| Health | 13,753 | 14,353 | 14,350 | 14,330 | 14,239 | 14,233 | 14,224 |
| Education | 11,650 | 12,257 | 12,269 | 12,205 | 12,099 | 12,227 | 12,420 |
| Core government services | 5,563 | 5,564 | 7,138 | 4,390 | 4,474 | 4,450 | 4,368 |
| Law and order | 3,382 | 3,555 | 3,635 | 3,539 | 3,511 | 3,509 | 3,510 |
| Defence | 1,809 | 1,911 | 1,903 | 1,917 | 1,867 | 1,866 | 1,864 |
| Transport and communications | 2,281 | 2,378 | 2,468 | 2,128 | 2,079 | 2,136 | 2,025 |
| Economic and industrial services | 2,609 | 2,235 | 2,529 | 1,922 | 1,855 | 1,876 | 1,906 |
| Primary services | 706 | 755 | 783 | 705 | 688 | 686 | 663 |
| Heritage, culture and recreation | 1,966 | 1,947 | 2,490 | 1,542 | 1,494 | 1,738 | 2,084 |
| Housing and community development | 876 | 333 | 400 | 313 | 313 | 328 | 281 |
| Other | 479 | 635 | 706 | 488 | 486 | 485 | 485 |
| Finance costs | 3,066 | 3,714 | 3,655 | 3,789 | 3,921 | 4,313 | 4,345 |
| Forecast new operating spending | - | 463 | 473 | 1,094 | 1,788 | 2,932 | 3,959 |
| Top-down expense adjustment | - | (310) | (1,100) | (300) | (100) | (100) | (100) |
| **Total core Crown expenses excluding losses** | **70,450** | **73,027** | **74,460** | **71,612** | **72,920** | **75,583** | **78,034** |

*The accompanying notes and accounting policies are an integral part of these Statements.*

# Forecast Statement of Comprehensive Income

## for the years ending 30 June

| | 2011 Actual $m | 2012 Previous Budget $m | 2012 Forecast $m | 2013 Forecast $m | 2014 Forecast $m | 2015 Forecast $m | 2016 Forecast $m |
|---|---|---|---|---|---|---|---|
| Revaluation of physical assets | (443) | - | - | - | (1) | - | - |
| Effective portion of changes in the fair value of cash flow hedges | (252) | 3 | 7 | (1) | 1 | 4 | - |
| Net change in fair value of cash flow hedges transferred to operating balance | 17 | - | 1 | 1 | - | - | 1 |
| Net change in fair value of cash flow hedges transferred to the hedged item | 95 | (7) | (21) | (2) | - | - | - |
| Foreign currency translation differences for foreign operations | (37) | (6) | 6 | 24 | - | - | - |
| Valuation gain/(losses) on investments available for sale taken to reserves | (1) | 6 | 3 | 8 | 10 | 13 | 14 |
| Other movements | 1 | 50 | - | 2 | 1 | (3) | (1) |
| **Other comprehensive income for the year** | **(620)** | **46** | **(4)** | **32** | **11** | **14** | **14** |
| **Operating balance (including minority interest)** | (13,461) | (7,293) | (12,601) | (2,375) | 1,576 | 3,974 | 5,701 |
| **Total comprehensive income** | **(14,081)** | **(7,247)** | **(12,605)** | **(2,343)** | **1,587** | **3,988** | **5,715** |
| **Attributable to:** | | | | | | | |
| - minority interest | (74) | - | - | - | - | - | - |
| - the Crown | (14,007) | (7,247) | (12,605) | (2,343) | 1,587 | 3,988 | 5,715 |
| **Total comprehensive income** | **(14,081)** | **(7,247)** | **(12,605)** | **(2,343)** | **1,587** | **3,988** | **5,715** |

*The accompanying notes and accounting policies are an integral part of these Statements.*

# Forecast Statement of Cash Flows

## for the years ending 30 June

| | 2011 Actual $m | 2012 Previous Budget $m | 2012 Forecast $m | 2013 Forecast $m | 2014 Forecast $m | 2015 Forecast $m | 2016 Forecast $m |
|---|---|---|---|---|---|---|---|
| **Cash flows from operations** | | | | | | | |
| **Cash was provided from** | | | | | | | |
| Taxation receipts | 50,418 | 53,959 | 54,070 | 57,810 | 62,231 | 66,168 | 69,872 |
| Other sovereign receipts | 4,693 | 4,878 | 4,884 | 4,722 | 4,784 | 4,867 | 5,221 |
| Sales of goods and services | 14,899 | 16,046 | 16,424 | 17,159 | 18,363 | 18,941 | 19,664 |
| Interest and dividend receipts | 2,682 | 2,594 | 2,602 | 3,001 | 3,291 | 3,785 | 3,992 |
| Other operating receipts | 2,990 | 4,536 | 5,164 | 5,728 | 4,333 | 4,164 | 3,771 |
| **Total cash provided from operations** | **75,682** | **82,013** | **83,144** | **88,420** | **93,002** | **97,925** | **102,520** |
| **Cash was disbursed to** | | | | | | | |
| Transfer payments and subsidies | 22,172 | 23,435 | 23,089 | 23,265 | 23,782 | 24,634 | 25,685 |
| Personnel and operating payments | 55,152 | 59,108 | 62,029 | 60,788 | 59,999 | 59,746 | 57,952 |
| Interest payments | 3,107 | 4,583 | 4,100 | 4,903 | 5,085 | 5,748 | 5,748 |
| Forecast new operating spending | - | 463 | 623 | 944 | 1,788 | 2,932 | 3,959 |
| Top-down expense adjustment | - | (310) | (1,100) | (300) | (100) | (100) | (100) |
| **Total cash disbursed to operations** | **80,431** | **87,279** | **88,741** | **89,600** | **90,554** | **92,960** | **93,244** |
| **Net cash flows from operations** | **(4,749)** | **(5,266)** | **(5,597)** | **(1,180)** | **2,448** | **4,965** | **9,276** |
| **Cash flows from investing activities** | | | | | | | |
| **Cash was provided from/(disbursed to)** | | | | | | | |
| Net purchase of physical assets | (5,996) | (7,852) | (7,841) | (6,656) | (6,305) | (5,939) | (6,343) |
| Net purchase of shares and other securities | (8,405) | 5,831 | (2) | 3,862 | (9,249) | (2,205) | (9,223) |
| Net purchase of intangible assets | (600) | (532) | (582) | (446) | (407) | (345) | (345) |
| Net repayment/(issues) of advances | (1,003) | (2,039) | (1,673) | (2,229) | (2,075) | (2,061) | (1,739) |
| Net acquisition of investments in associates | 173 | (137) | (30) | (10) | (1) | (1) | (1) |
| Forecast new capital spending | - | (242) | (192) | (452) | (651) | (800) | (900) |
| Balance sheet funding of new capital spending | - | 100 | (50) | 125 | 560 | 790 | 835 |
| Top-down capital adjustment | - | 170 | 350 | - | - | - | - |
| **Net cash flows from investing activities** | **(15,831)** | **(4,701)** | **(10,020)** | **(5,806)** | **(18,128)** | **(10,561)** | **(17,716)** |
| **Net cash flows from operating and investing activities** | **(20,580)** | **(9,967)** | **(15,617)** | **(6,986)** | **(15,680)** | **(5,596)** | **(8,440)** |
| **Cash flows from financing activities** | | | | | | | |
| **Cash was provided from/(disbursed to)** | | | | | | | |
| Issues of circulating currency | 234 | 219 | 89 | 218 | 229 | 240 | 252 |
| Net issue/(repayment) of Government stock[1] | 21,088 | 4,774 | 10,312 | 4,603 | 13,125 | 1,293 | 8,384 |
| Net issue/(repayment) of foreign-currency borrowings | 1,809 | (6,639) | (7,720) | (549) | (702) | (1,199) | (1,143) |
| Net issue/(repayment) of other New Zealand dollar borrowings | 81 | 11,390 | 12,454 | 2,843 | 3,829 | 5,316 | 1,413 |
| **Net cash flows from financing activities** | **23,212** | **9,744** | **15,135** | **7,115** | **16,481** | **5,650** | **8,906** |
| **Net movement in cash** | **2,632** | **(223)** | **(482)** | **129** | **801** | **54** | **466** |
| **Opening cash balance** | 7,774 | 9,103 | 9,801 | 9,185 | 9,261 | 10,009 | 10,010 |
| Foreign-exchange gains/(losses) on opening cash | (605) | 6 | (134) | (53) | (53) | (53) | (53) |
| **Closing cash balance** | **9,801** | **8,886** | **9,185** | **9,261** | **10,009** | **10,010** | **10,423** |

Note 1: Net issue of Government stock is after elimination of holdings by entities such as NZS Fund, ACC and EQC. Further information on the proceeds a repayments of Government stock ("domestic bonds") is available in note 22.

*The accompanying notes and accounting policies are an integral part of these Statements.*

# Forecast Statement of Cash Flows (continued)

## for the years ending 30 June

| | 2011 Actual $m | 2012 Previous Budget $m | 2012 Forecast $m | 2013 Forecast $m | 2014 Forecast $m | 2015 Forecast $m | 2016 Forecast $m |
|---|---|---|---|---|---|---|---|
| **Reconciliation between the net cash flows from operations and the operating balance** | | | | | | | |
| **Net cash flows from operations** | **(4,749)** | **(5,266)** | **(5,597)** | **(1,180)** | **2,448** | **4,965** | **9,276** |
| *Items included in the operating balance but not in net cash flows from operations* | | | | | | | |
| **Gains/(losses)** | | | | | | | |
| Net gains/(losses) on financial instruments | 4,619 | 1,973 | (4) | 1,588 | 2,055 | 2,062 | 2,132 |
| Net gains/(losses) on non-financial instruments | 79 | 172 | (2,064) | 191 | 170 | 176 | 185 |
| **Total gains/(losses)** | **4,698** | **2,145** | **(2,068)** | **1,779** | **2,225** | **2,238** | **2,317** |
| **Other non-cash items in operating balance** | | | | | | | |
| Depreciation and amortisation | (4,682) | (4,631) | (4,562) | (4,797) | (4,931) | (4,988) | (5,067) |
| Write-down on initial recognition of financial assets | (807) | (806) | (798) | (779) | (794) | (794) | (803) |
| Impairment on financial assets (excl. receivables) | 105 | 85 | 79 | 149 | 142 | 135 | 124 |
| Decrease/(increase) in defined benefit retirement plan liabilities | 358 | 377 | 475 | 392 | 320 | 273 | 251 |
| Decrease/(increase) in insurance liabilities | (13,179) | 1,269 | 2,460 | 2,086 | 1,697 | 303 | (1,770) |
| Other | 238 | 307 | 281 | 284 | 293 | 290 | 308 |
| **Total other non-cash Items** | **(17,967)** | **(3,399)** | **(2,065)** | **(2,665)** | **(3,273)** | **(4,781)** | **(6,957)** |
| **Movements in working capital** | | | | | | | |
| Increase/(decrease) in receivables | 6,605 | (1,081) | (1,532) | (2,877) | (683) | (157) | 127 |
| Increase/(decrease) in accrued interest | (599) | 356 | 353 | 745 | 580 | 833 | 835 |
| Increase/(decrease) in inventories | 149 | 70 | 11 | 99 | 29 | 33 | (10) |
| Increase/(decrease) in prepayments | 39 | (3) | 4 | (12) | 39 | (1) | 2 |
| Decrease/(increase) in deferred revenue | (46) | 62 | 164 | 30 | 20 | (2) | (6) |
| Decrease/(increase) in payables/provisions | (1,490) | (177) | (1,871) | 1,706 | 191 | 846 | 117 |
| **Total movements in working capital** | **4,658** | **(773)** | **(2,871)** | **(309)** | **176** | **1,552** | **1,065** |
| **Operating balance** | **(13,360)** | **(7,293)** | **(12,601)** | **(2,375)** | **1,576** | **3,974** | **5,701** |

*The accompanying notes and accounting policies are an integral part of these Statements.*

# Forecast Statement of Changes in Net Worth

## for the years ending 30 June

| | 2011<br>Actual<br>$m | 2012<br>Previous<br>Budget<br>$m | 2012<br>Forecast<br>$m | 2013<br>Forecast<br>$m | 2014<br>Forecast<br>$m | 2015<br>Forecast<br>$m | 2016<br>Forecast<br>$m |
|---|---|---|---|---|---|---|---|
| **Opening net worth** | 94,988 | 85,519 | 80,887 | 68,282 | 65,939 | 67,526 | 71,514 |
| Operating balance (including minority interest) | (13,461) | (7,293) | (12,601) | (2,375) | 1,576 | 3,974 | 5,701 |
| Net revaluations | (443) | - | - | - | (1) | - | - |
| Transfers to/(from) reserves | (278) | 53 | 7 | 1 | 2 | 1 | (1) |
| (Gains)/losses transferred to the Statement of Financial Performance | 17 | - | 1 | 1 | - | - | 1 |
| Other movements | 84 | (7) | (12) | 30 | 10 | 13 | 14 |
| **Total comprehensive income** | **(14,081)** | **(7,247)** | **(12,605)** | **(2,343)** | **1,587** | **3,988** | **5,715** |
| Transactions with minority interest in Air New Zealand | (20) | - | - | - | - | - | - |
| **Closing net worth** | **80,887** | **78,272** | **68,282** | **65,939** | **67,526** | **71,514** | **77,229** |

*The accompanying notes and accounting policies are an integral part of these Statements.*

# Forecast Statement of Financial Position

## as at 30 June

| | Note | 2011 Actual $m | 2012 Previous Budget $m | 2012 Forecast $m | 2013 Forecast $m | 2014 Forecast $m | 2015 Forecast $m | 2016 Forecast $m |
|---|---|---|---|---|---|---|---|---|
| **Assets** | | | | | | | | |
| Cash and cash equivalents | 12 | 9,801 | 8,886 | 9,185 | 9,261 | 10,009 | 10,010 | 10,423 |
| Receivables | 12 | 21,690 | 16,709 | 18,798 | 15,922 | 15,239 | 15,081 | 15,395 |
| Marketable securities, deposits and derivatives in gain | 12 | 49,056 | 43,034 | 42,497 | 33,836 | 38,441 | 35,430 | 38,735 |
| Share investments | 12 | 14,248 | 16,095 | 18,443 | 20,695 | 22,300 | 24,504 | 26,958 |
| Advances | 12 | 20,567 | 22,433 | 22,181 | 24,228 | 26,345 | 28,484 | 30,501 |
| Inventory | | 1,308 | 1,380 | 1,320 | 1,419 | 1,448 | 1,481 | 1,471 |
| Other assets | | 1,996 | 1,662 | 1,946 | 1,959 | 1,958 | 1,965 | 1,986 |
| Property, plant and equipment | 14 | 114,854 | 121,186 | 119,067 | 121,919 | 124,174 | 126,129 | 128,397 |
| Equity accounted investments[1] | | 9,301 | 9,613 | 9,689 | 9,867 | 10,036 | 10,263 | 10,494 |
| Intangible assets and goodwill | 15 | 2,394 | 2,714 | 2,597 | 2,662 | 2,717 | 2,705 | 2,680 |
| Forecast for new capital spending (net) | 8 | - | 142 | 242 | 569 | 660 | 670 | 735 |
| Top-down capital adjustment | | - | (270) | (350) | (350) | (350) | (350) | (350) |
| **Total assets** | | **245,215** | **243,584** | **245,615** | **241,987** | **252,977** | **256,372** | **267,425** |
| **Liabilities** | | | | | | | | |
| Issued currency | | 4,254 | 4,598 | 4,361 | 4,579 | 4,808 | 5,048 | 5,300 |
| Payables | 17 | 11,099 | 9,603 | 12,303 | 11,968 | 12,630 | 12,955 | 13,631 |
| Deferred revenue | | 1,674 | 1,371 | 1,510 | 1,481 | 1,460 | 1,463 | 1,469 |
| Borrowings | | 90,245 | 101,383 | 101,237 | 103,850 | 115,136 | 115,530 | 118,893 |
| Insurance liabilities | 18 | 39,314 | 30,533 | 38,272 | 36,185 | 34,488 | 34,185 | 35,955 |
| Retirement plan liabilities | 19 | 10,156 | 8,895 | 10,581 | 10,189 | 9,869 | 9,596 | 9,344 |
| Provisions | 20 | 7,586 | 8,929 | 9,069 | 7,796 | 7,060 | 6,081 | 5,604 |
| **Total liabilities** | | **164,328** | **165,312** | **177,333** | **176,048** | **185,451** | **184,858** | **190,196** |
| **Total assets less total liabilities** | | **80,887** | **78,272** | **68,282** | **65,939** | **67,526** | **71,514** | **77,229** |
| **Net worth** | | | | | | | | |
| Taxpayer funds | 21 | 18,188 | 14,463 | 5,631 | 3,322 | 4,934 | 8,933 | 14,661 |
| Property, plant and equipment revaluation reserve | 21 | 62,690 | 63,614 | 62,646 | 62,582 | 62,546 | 62,518 | 62,490 |
| Other reserves | 21 | (299) | (207) | (303) | (273) | (262) | (245) | (230) |
| **Total net worth attributable to the Crown** | | **80,579** | **77,870** | **67,974** | **65,631** | **67,218** | **71,206** | **76,921** |
| Net worth attributable to minority interest | | 308 | 402 | 308 | 308 | 308 | 308 | 308 |
| **Total net worth** | | **80,887** | **78,272** | **68,282** | **65,939** | **67,526** | **71,514** | **77,229** |

Note 1: Tertiary education institutions constitute most equity accounted investments.

*The accompanying notes and accounting policies are an integral part of these Statements.*

# Forecast Statement of Borrowings

## as at 30 June

| | 2011 Actual $m | 2012 Previous Budget $m | 2012 Forecast $m | 2013 Forecast $m | 2014 Forecast $m | 2015 Forecast $m | 2016 Forecast $m |
|---|---|---|---|---|---|---|---|
| **Borrowings** | | | | | | | |
| Government stock | 46,018 | 52,145 | 52,630 | 53,262 | 62,322 | 59,073 | 61,454 |
| Treasury bills | 7,028 | 7,707 | 8,997 | 8,613 | 8,543 | 8,474 | 8,415 |
| Government retail stock | 261 | 270 | 258 | 258 | 258 | 258 | 258 |
| Settlement deposits with Reserve Bank | 6,276 | 6,736 | 5,429 | 5,429 | 5,429 | 5,429 | 5,429 |
| Derivatives in loss | 2,767 | 1,559 | 2,638 | 2,377 | 2,126 | 2,055 | 2,017 |
| Finance lease liabilities | 1,176 | 1,492 | 1,556 | 1,463 | 1,512 | 1,704 | 1,721 |
| Other borrowings | 26,719 | 31,474 | 29,729 | 32,448 | 34,946 | 38,537 | 39,599 |
| **Total borrowings** | **90,245** | **101,383** | **101,237** | **103,850** | **115,136** | **115,530** | **118,893** |
| Total sovereign-guaranteed debt | 67,765 | 74,900 | 76,415 | 76,327 | 85,143 | 83,248 | 84,788 |
| Total non-sovereign-guaranteed debt | 22,480 | 26,483 | 24,822 | 27,523 | 29,993 | 32,282 | 34,105 |
| **Total borrowings** | **90,245** | **101,383** | **101,237** | **103,850** | **115,136** | **115,530** | **118,893** |
| **Net debt:** | | | | | | | |
| Core Crown borrowings[1] | 76,885 | 83,195 | 84,636 | 84,762 | 93,271 | 92,086 | 94,878 |
| Add back NZS Fund holdings of sovereign-issued debt and NZS Fund borrowings | 405 | (231) | (872) | (777) | (883) | (972) | (1,105) |
| **Gross sovereign-issued debt[2]** | **77,290** | **82,964** | **83,764** | **83,985** | **92,388** | **91,114** | **93,773** |
| Less core Crown financial assets[3] | 65,400 | 59,728 | 61,028 | 53,855 | 59,987 | 57,946 | 61,708 |
| **Net core Crown debt (incl. NZS Fund)[4]** | **11,890** | **23,236** | **22,736** | **30,130** | **32,401** | **33,168** | **32,065** |
| Add back NZS Fund holdings of core Crown financial assets and NZS Fund financial assets[5] | 16,159 | 19,068 | 18,171 | 19,371 | 21,097 | 22,871 | 24,759 |
| **Net core Crown debt (excl. NZS Fund)[4]** | **28,049** | **42,304** | **40,907** | **49,501** | **53,498** | **56,039** | **56,824** |
| Core Crown advances | 12,079 | 12,568 | 12,916 | 13,650 | 14,277 | 15,285 | 15,710 |
| **Net core Crown debt (excl. NZS Fund and advances)[6]** | **40,128** | **54,872** | **53,823** | **63,151** | **67,775** | **71,324** | **72,534** |
| **Gross debt:** | | | | | | | |
| Gross sovereign-issued debt[2] | 77,290 | 82,964 | 83,764 | 83,985 | 92,388 | 91,114 | 93,773 |
| Less Reserve Bank settlement cash and bank bills | (6,470) | (6,800) | (5,585) | (5,585) | (5,585) | (5,585) | (5,585) |
| Add back changes to DMO borrowing owing to settlement cash[7] | 1,600 | 1,600 | 1,600 | 1,600 | 1,600 | 1,600 | 1,600 |
| **Gross sovereign-issued debt excluding Reserve Bank settlement cash and bank bills[4]** | **72,420** | **77,764** | **79,779** | **80,000** | **88,403** | **87,129** | **89,788** |

**Notes on borrowings**

Total borrowings can be split into sovereign-guaranteed and non-sovereign-guaranteed debt. This split reflects the fact that borrowings by State-owned enterprises and Crown entities are not explicitly guaranteed by the Crown. No other debt of State-owned enterprises and Crown entities is currently guaranteed by the Crown.

1. Core Crown borrowings in this instance includes unsettled purchases of securities (classified as accounts payable in the Statement of Financial Position).

2. Gross sovereign-issued debt (GSID) represents debt issued by the sovereign (the core Crown) and includes any government stock held by the NZS Fund, ACC and EQC.

3. Core Crown financial assets exclude receivables.

4. Net core Crown debt represents GSID less financial assets. This can provide information about the sustainability of the Government's accounts, and is used by some international agencies when determining the creditworthiness of a country.

5. Adding back the NZS Fund assets provides the financial liabilities less financial assets of the core Crown, excluding those assets set aside to meet part of the future cost of New Zealand Superannuation.

6. Net core Crown debt (excluding NZS Fund and advances) excludes financial assets which are held for public policy rather than treasury management purposes.

7. The Reserve Bank has used $1.6 billion of settlement cash to purchase reserves that were to have been funded by the NZDMO borrowing. Therefore, the impact of settlement cash on GSID is adjusted by this amount.

*The accompanying notes and accounting policies are an integral part of these Statements.*

# Statement of Actual Commitments

## as at 30 June 2011

| | As at 30 June 2011 $m | As at 30 June 2010 $m |
|---|---|---|
| **Capital commitments** | | |
| Specialist military equipment | 369 | 422 |
| Land and buildings | 701 | 849 |
| Other property, plant and equipment | 7,032 | 6,370 |
| Other capital commitments | 408 | 224 |
| Tertiary Education Institutions | 413 | 302 |
| **Total capital commitments** | **8,923** | **8,167** |
| **Operating commitments** | | |
| Non-cancellable accommodation leases | 2,909 | 2,862 |
| Other non-cancellable leases | 3,171 | 3,230 |
| Non-cancellable contracts for the supply of goods and services | 5,520 | 6,254 |
| Other operating commitments | 7,415 | 7,634 |
| Tertiary Education Institutions | 366 | 304 |
| **Total operating commitments** | **19,381** | **20,284** |
| **Total commitments** | **28,304** | **28,451** |
| **Total commitments by segment** | | |
| Core Crown | 22,129 | 20,983 |
| Crown entities | 12,925 | 13,811 |
| State-owned enterprises | 10,410 | 11,238 |
| Inter-segment eliminations | (17,160) | (17,581) |
| **Total commitments** | **28,304** | **28,451** |

# Statement of Actual Contingent Liabilities and Assets

## as at 30 June 2011

| | As at 30 June 2011 $m | As at 30 June 2010 $m |
|---|---|---|
| **Quantifiable contingent liabilities** | | |
| Guarantees and indemnities | 78 | 106 |
| Uncalled capital | 4,033 | 2,310 |
| Legal proceedings and disputes | 331 | 414 |
| Other contingent liabilities | 2,699 | 3,535 |
| **Total quantifiable contingent liabilities** | **7,141** | **6,365** |
| **Total quantifiable contingent liabilities by segment** | | |
| Core Crown | 6,884 | 6,050 |
| Crown entities | 173 | 171 |
| State-owned enterprises | 84 | 144 |
| Inter-segment eliminations | - | - |
| **Total quantifiable contingent liabilities** | **7,141** | **6,365** |
| **Quantifiable contingent assets by segment** | | |
| Core Crown | 702 | 570 |
| Crown entities | 2 | 2 |
| **Total quantifiable contingent assets** | **704** | **572** |

*The accompanying notes and accounting policies are an integral part of these Statements.*

More information on contingent liabilities (quantified and unquantified) is outlined in the Fiscal Risks chapter.

# Notes to the Forecast Financial Statements

| | 2011 Actual $m | 2012 Previous Budget $m | 2012 Forecast $m | 2013 Forecast $m | 2014 Forecast $m | 2015 Forecast $m | 2016 Forecast $m |
|---|---|---|---|---|---|---|---|
| **NOTE 1: Revenue collected through the Crown's sovereign power** | | | | | | | |
| **Taxation revenue (accrual)** | | | | | | | |
| **Individuals** | | | | | | | |
| Source deductions | 20,857 | 21,165 | 21,304 | 22,739 | 24,334 | 26,052 | 27,825 |
| Other persons | 3,791 | 4,342 | 4,290 | 4,426 | 4,633 | 4,804 | 5,028 |
| Refunds | (1,679) | (1,656) | (1,616) | (1,531) | (1,499) | (1,444) | (1,458) |
| Fringe benefit tax | 462 | 430 | 440 | 458 | 482 | 512 | 542 |
| **Total individuals** | **23,431** | **24,281** | **24,418** | **26,092** | **27,950** | **29,924** | **31,937** |
| **Corporate tax** | | | | | | | |
| Gross companies tax | 6,687 | 7,978 | 8,025 | 8,278 | 8,826 | 9,238 | 9,462 |
| Refunds | (197) | (400) | (260) | (284) | (299) | (326) | (338) |
| Non-resident withholding tax | 467 | 508 | 427 | 478 | 536 | 589 | 630 |
| Foreign-source dividend w/holding payments | - | 1 | - | - | - | - | - |
| **Total corporate tax** | **6,957** | **8,087** | **8,192** | **8,472** | **9,063** | **9,501** | **9,754** |
| **Other direct income tax** | | | | | | | |
| Resident w/holding tax on interest income | 1,704 | 1,665 | 1,646 | 1,874 | 2,251 | 2,645 | 3,069 |
| Resident w/holding tax on dividend income | 195 | 209 | 207 | 287 | 470 | 487 | 498 |
| Estate and gift duties | 2 | - | - | - | - | - | - |
| **Total other direct income tax** | **1,901** | **1,874** | **1,853** | **2,161** | **2,721** | **3,132** | **3,567** |
| **Total direct income tax** | **32,289** | **34,242** | **34,463** | **36,725** | **39,734** | **42,557** | **45,258** |
| **Goods and services tax** | | | | | | | |
| Gross goods and services tax | 23,484 | 26,007 | 25,626 | 27,437 | 30,466 | 31,628 | 32,594 |
| Refunds | (9,776) | (10,965) | (10,557) | (11,202) | (13,080) | (13,232) | (13,312) |
| **Total goods and services tax** | **13,708** | **15,042** | **15,069** | **16,235** | **17,386** | **18,396** | **19,282** |
| **Other indirect taxation** | | | | | | | |
| Road user charges | 1,016 | 1,049 | 1,073 | 1,142 | 1,223 | 1,297 | 1,367 |
| Petroleum fuels excise - domestic production | 872 | 886 | 921 | 938 | 979 | 1,016 | 1,055 |
| Alcohol excise - domestic production | 623 | 665 | 712 | 746 | 777 | 812 | 849 |
| Tobacco excise - domestic production | 220 | 251 | 210 | 219 | 212 | 206 | 207 |
| Petroleum fuels excise - imports[1] | 575 | 668 | 640 | 651 | 679 | 706 | 733 |
| Alcohol excise - imports[1] | 229 | 250 | 245 | 257 | 268 | 280 | 292 |
| Tobacco excise - imports[1] | 924 | 1,005 | 956 | 996 | 965 | 940 | 944 |
| Other customs duty | 188 | 130 | 178 | 172 | 167 | 156 | 144 |
| Gaming duties | 214 | 223 | 224 | 227 | 229 | 233 | 238 |
| Motor vehicle fees | 172 | 168 | 168 | 166 | 169 | 173 | 176 |
| Energy resources levies | 36 | 38 | 38 | 36 | 36 | 36 | 36 |
| Approved issuer levy and cheque duty | 62 | 73 | 60 | 61 | 61 | 61 | 61 |
| **Total other indirect taxation** | **5,131** | **5,406** | **5,425** | **5,611** | **5,765** | **5,916** | **6,102** |
| **Total indirect taxation** | **18,839** | **20,448** | **20,494** | **21,846** | **23,151** | **24,312** | **25,384** |
| **Total taxation revenue** | **51,128** | **54,690** | **54,957** | **58,571** | **62,885** | **66,869** | **70,642** |
| **Other sovereign revenue (accrual)** | | | | | | | |
| ACC levies | 3,586 | 3,882 | 3,686 | 3,433 | 3,564 | 3,702 | 3,836 |
| Fire Service levies | 312 | 309 | 309 | 309 | 315 | 321 | 333 |
| EQC levies | 88 | 89 | 103 | 240 | 272 | 275 | 277 |
| Other miscellaneous items | 1,295 | 1,528 | 1,465 | 1,749 | 1,967 | 2,068 | 2,505 |
| **Total other sovereign revenue** | **5,281** | **5,808** | **5,563** | **5,731** | **6,118** | **6,366** | **6,951** |
| **Total sovereign revenue** | **56,409** | **60,498** | **60,520** | **64,302** | **69,003** | **73,235** | **77,593** |

Note 1: Customs excise-equivalent duty.

# Notes to the Forecast Financial Statements

| | 2011 Actual $m | 2012 Previous Budget $m | 2012 Forecast $m | 2013 Forecast $m | 2014 Forecast $m | 2015 Forecast $m | 2016 Forecast $m |
|---|---|---|---|---|---|---|---|
| **NOTE 1 (continued): Receipts collected through the Crown's sovereign power** | | | | | | | |
| **Taxation receipts (cash)** | | | | | | | |
| **Individuals** | | | | | | | |
| Source deductions | 20,699 | 21,066 | 21,212 | 22,643 | 24,234 | 25,948 | 27,721 |
| Other persons | 4,386 | 4,765 | 4,897 | 5,002 | 5,164 | 5,309 | 5,484 |
| Refunds | (2,463) | (2,394) | (2,342) | (2,350) | (2,270) | (2,206) | (2,180) |
| Fringe benefit tax | 457 | 424 | 439 | 457 | 481 | 511 | 541 |
| **Total individuals** | **23,079** | **23,861** | **24,206** | **25,752** | **27,609** | **29,562** | **31,566** |
| **Corporate tax** | | | | | | | |
| Gross companies tax | 7,588 | 8,369 | 8,603 | 8,864 | 9,524 | 9,866 | 10,063 |
| Refunds | (772) | (799) | (918) | (913) | (922) | (927) | (933) |
| Non-resident withholding tax | 462 | 508 | 427 | 478 | 536 | 589 | 630 |
| Foreign-source dividend w/holding payments | (1) | 1 | - | - | - | - | - |
| **Total corporate tax** | **7,277** | **8,079** | **8,112** | **8,429** | **9,138** | **9,528** | **9,760** |
| **Other direct income tax** | | | | | | | |
| Resident w/holding tax on interest income | 1,701 | 1,664 | 1,645 | 1,873 | 2,250 | 2,644 | 3,068 |
| Resident w/holding tax on dividend income | 196 | 208 | 206 | 286 | 469 | 486 | 497 |
| Estate and gift duties | 2 | - | - | - | - | - | - |
| **Total other direct income tax** | **1,899** | **1,872** | **1,851** | **2,159** | **2,719** | **3,130** | **3,565** |
| **Total direct income tax** | **32,255** | **33,812** | **34,169** | **36,340** | **39,466** | **42,220** | **44,891** |
| **Goods and services tax** | | | | | | | |
| Gross goods and services tax | 22,162 | 25,135 | 24,370 | 26,502 | 29,526 | 30,712 | 31,640 |
| Refunds | (9,177) | (10,394) | (9,896) | (10,643) | (12,526) | (12,680) | (12,761) |
| **Total goods and services tax** | **12,985** | **14,741** | **14,474** | **15,859** | **17,000** | **18,032** | **18,879** |
| **Other indirect taxation** | | | | | | | |
| Petroleum fuels excise - domestic production | 869 | 886 | 921 | 938 | 979 | 1,016 | 1,055 |
| Tobacco excise - domestic production | 181 | 251 | 210 | 219 | 212 | 206 | 207 |
| Customs duty | 2,005 | 2,053 | 2,019 | 2,076 | 2,079 | 2,082 | 2,113 |
| Road user charges | 1,015 | 1,049 | 1,073 | 1,142 | 1,223 | 1,297 | 1,367 |
| Alcohol excise - domestic production | 625 | 665 | 712 | 746 | 777 | 812 | 849 |
| Gaming duties | 216 | 223 | 225 | 227 | 229 | 233 | 238 |
| Motor vehicle fees | 171 | 168 | 168 | 166 | 169 | 173 | 176 |
| Energy resources levies | 36 | 38 | 38 | 36 | 36 | 36 | 36 |
| Approved issuer levy and cheque duty | 60 | 73 | 61 | 61 | 61 | 61 | 61 |
| **Total other indirect taxation** | **5,178** | **5,406** | **5,427** | **5,611** | **5,765** | **5,916** | **6,102** |
| **Total indirect taxation** | **18,163** | **20,147** | **19,901** | **21,470** | **22,765** | **23,948** | **24,981** |
| **Total taxation receipts** | **50,418** | **53,959** | **54,070** | **57,810** | **62,231** | **66,168** | **69,872** |
| **Other sovereign receipts (cash)** | | | | | | | |
| ACC levies | 3,612 | 3,804 | 3,712 | 3,422 | 3,446 | 3,504 | 3,831 |
| Fire Service levies | 312 | 309 | 309 | 309 | 315 | 321 | 333 |
| EQC levies | 88 | 88 | 135 | 270 | 273 | 275 | 278 |
| Other miscellaneous items | 681 | 677 | 728 | 721 | 750 | 767 | 779 |
| **Total other sovereign receipts** | **4,693** | **4,878** | **4,884** | **4,722** | **4,784** | **4,867** | **5,221** |
| **Total sovereign receipts** | **55,111** | **58,837** | **58,954** | **62,532** | **67,015** | **71,035** | **75,093** |

# Notes to the Forecast Financial Statements

| | 2011 Actual $m | 2012 Previous Budget $m | 2012 Forecast $m | 2013 Forecast $m | 2014 Forecast $m | 2015 Forecast $m | 2016 Forecast $m |
|---|---|---|---|---|---|---|---|
| **NOTE 2: Interest revenue and dividends** | | | | | | | |
| ***By type*** | | | | | | | |
| Interest revenue | 2,142 | 2,569 | 2,272 | 2,695 | 3,003 | 3,503 | 3,713 |
| Dividends | 428 | 482 | 542 | 613 | 685 | 756 | 824 |
| **Total interest revenue and dividends** | **2,570** | **3,051** | **2,814** | **3,308** | **3,688** | **4,259** | **4,537** |
| ***By source*** | | | | | | | |
| Core Crown | 2,169 | 2,134 | 2,039 | 2,667 | 2,674 | 2,942 | 3,057 |
| Crown entities | 1,234 | 768 | 1,325 | 1,244 | 1,446 | 1,642 | 1,857 |
| State-owned enterprises | 801 | 1,021 | 828 | 1,006 | 1,212 | 1,328 | 1,447 |
| Inter-segment eliminations | (1,634) | (872) | (1,378) | (1,609) | (1,644) | (1,653) | (1,824) |
| **Total interest revenue and dividends** | **2,570** | **3,051** | **2,814** | **3,308** | **3,688** | **4,259** | **4,537** |
| **NOTE 3: Transfer payments and subsidies** | | | | | | | |
| New Zealand Superannuation | 8,830 | 9,575 | 9,597 | 10,235 | 10,824 | 11,590 | 12,449 |
| Domestic Purposes Benefit | 1,757 | 1,895 | 1,840 | 1,909 | 1,958 | 2,014 | 2,073 |
| Unemployment Benefit | 943 | 1,029 | 860 | 825 | 752 | 694 | 665 |
| Invalid's Benefit | 1,306 | 1,347 | 1,327 | 1,340 | 1,351 | 1,372 | 1,401 |
| Family tax credit | 2,139 | 2,178 | 2,131 | 2,125 | 2,075 | 2,038 | 2,054 |
| Accommodation supplement | 1,197 | 1,264 | 1,199 | 1,218 | 1,232 | 1,247 | 1,276 |
| Sickness Benefit | 743 | 782 | 770 | 797 | 819 | 847 | 879 |
| Student allowances | 620 | 627 | 634 | 580 | 532 | 511 | 507 |
| Disability allowances | 409 | 411 | 403 | 394 | 398 | 403 | 411 |
| Other social assistance benefits | 2,691 | 2,637 | 2,590 | 2,605 | 2,608 | 2,627 | 2,647 |
| **Total social assistance grants** | **20,635** | **21,745** | **21,351** | **22,028** | **22,549** | **23,343** | **24,362** |
| **Subsidies** | | | | | | | |
| KiwiSaver subsidies | 1,042 | 656 | 685 | 634 | 603 | 638 | 670 |
| **Other transfer payments** | | | | | | | |
| Official development assistance | 495 | 525 | 544 | 513 | 534 | 559 | 559 |
| **Total transfer payments and subsidies** | **22,172** | **22,926** | **22,580** | **23,175** | **23,686** | **24,540** | **25,591** |
| **NOTE 4: Personnel expenses** | | | | | | | |
| Core Crown | 5,996 | 6,021 | 6,011 | 5,956 | 5,979 | 6,040 | 6,084 |
| Crown entities | 10,410 | 10,440 | 10,724 | 10,924 | 11,005 | 11,120 | 11,241 |
| State-owned enterprises | 2,695 | 2,697 | 2,811 | 2,903 | 2,993 | 3,069 | 3,175 |
| Inter-segment eliminations | (13) | (9) | (10) | (10) | (10) | (10) | (10) |
| **Total personnel expenses** | **19,088** | **19,149** | **19,536** | **19,773** | **19,967** | **20,219** | **20,490** |
| **NOTE 5: Depreciation, amortisation and other operating expenses** | | | | | | | |
| Core Crown | 39,157 | 40,197 | 42,824 | 37,854 | 37,603 | 37,813 | 38,111 |
| Crown entities | 17,905 | 18,390 | 18,433 | 18,141 | 18,423 | 18,580 | 18,383 |
| State-owned enterprises | 9,567 | 10,560 | 10,993 | 11,284 | 12,027 | 12,428 | 12,981 |
| Inter-segment eliminations | (26,118) | (26,724) | (27,003) | (26,700) | (26,942) | (27,113) | (26,903) |
| **Total depreciation, amortisation and other operating expenses** | **40,511** | **42,423** | **45,247** | **40,579** | **41,111** | **41,708** | **42,572** |

# Notes to the Forecast Financial Statements

| | 2011 Actual $m | 2012 Previous Budget $m | 2012 Forecast $m | 2013 Forecast $m | 2014 Forecast $m | 2015 Forecast $m | 2016 Forecast $m |
|---|---|---|---|---|---|---|---|
| **NOTE 6: Interest expenses** | | | | | | | |
| ***By type*** | | | | | | | |
| Interest on financial liabilities | 3,545 | 4,592 | 3,914 | 4,405 | 4,832 | 5,314 | 5,385 |
| Interest unwind on provisions | 51 | 93 | 45 | 59 | 69 | 75 | 73 |
| **Total interest expenses** | **3,596** | **4,685** | **3,959** | **4,464** | **4,901** | **5,389** | **5,458** |
| ***By source*** | | | | | | | |
| Core Crown | 3,066 | 3,714 | 3,655 | 3,789 | 3,921 | 4,313 | 4,345 |
| Crown entities | 248 | 272 | 266 | 280 | 307 | 309 | 305 |
| State-owned enterprises | 1,027 | 1,392 | 1,129 | 1,361 | 1,641 | 1,745 | 1,883 |
| Inter-segment eliminations | (745) | (693) | (1,091) | (966) | (968) | (978) | (1,075) |
| **Total interest expenses** | **3,596** | **4,685** | **3,959** | **4,464** | **4,901** | **5,389** | **5,458** |
| **NOTE 7: Insurance expenses** | | | | | | | |
| ***By entity*** | | | | | | | |
| ACC | 2,979 | 3,042 | 2,307 | 3,567 | 3,854 | 4,114 | 4,408 |
| EQC | 11,776 | 78 | 427 | 373 | 300 | (105) | 130 |
| Other | (163) | 18 | 1,017 | 200 | 251 | 289 | 303 |
| **Total insurance expenses** | **14,592** | **3,138** | **3,751** | **4,140** | **4,405** | **4,298** | **4,841** |
| **NOTE 8: Forecast new spending and top-down expense adjustment** | | | | | | | |
| **Forecast new operating spending** | | | | | | | |
| Unallocated new spending from Budget 2011 | - | 463 | 473 | 294 | 188 | 141 | (46) |
| Forecast new spending for Budget 2012 | - | | - | 800 | 800 | 800 | 800 |
| Forecast new spending for Budget 2013 | - | - | - | - | 800 | 800 | 800 |
| Forecast new spending for Budget 2014 | - | - | - | - | - | 1,191 | 1,191 |
| Forecast new spending for Budget 2015 | - | | - | - | - | - | 1,214 |
| **Total forecast new operating spending** | **-** | **463** | **473** | **1,094** | **1,788** | **2,932** | **3,959** |
| **Operating top-down adjustment** | **-** | **(310)** | **(1,100)** | **(300)** | **(100)** | **(100)** | **(100)** |

Unallocated new spending from Budget 2011 represents expenses included in Budget 2011 that have yet to be allocated.

Forecast for future new spending indicates the expected spending increases from future Budgets.

| | 2012 Forecast $m | 2013 Forecast $m | 2014 Forecast $m | 2015 Forecast $m | 2016 Forecast $m | Post-2016 Forecast $m | Total Forecast $m |
|---|---|---|---|---|---|---|---|
| **Forecast new capital spending (annual)** | | | | | | | |
| Unallocated new spending from Budget 2011 | 92 | 2 | 1 | - | - | - | 95 |
| Forecast new spending for Budget 2012 | 100 | 350 | 200 | 150 | 100 | - | 900 |
| Forecast new spending for Budget 2013 | - | 100 | 350 | 200 | 150 | 100 | 900 |
| Forecast new spending for Budget 2014 | - | - | 100 | 350 | 200 | 250 | 900 |
| Forecast new spending for Budget 2015 | - | - | - | 100 | 350 | 450 | 900 |
| Forecast new spending for Budget 2016 | | | | | 100 | 800 | 900 |
| Balance sheet funding of new capital spending | 50 | (125) | (560) | (790) | (835) | (1,600) | (3,860) |
| **Total forecast new capital spending** | **242** | **327** | **91** | **10** | **65** | **-** | **735** |
| **Forecast new capital spending (cumulative)** | **242** | **569** | **660** | **670** | **735** | | |
| **Capital top-down adjustment (cumulative)** | **(350)** | **(350)** | **(350)** | **(350)** | **(350)** | | |

Unallocated new spending from Budget 2011 represents capital spending from Budget 2011 that has yet to be allocated.

Forecast for future new spending indicates the expected capital spending increases from future Budgets.

These forecasts assume that, instead of borrowing to fund this new capital spending, the Government will source funding from alternative sources such as increased returns from existing investments, reprioritisation of planned capital spending, as well as the partial divestment of assets such as State-owned enterprises. The portion of funding yet to be allocated is referred to "Balance sheet funding of new capital spending".

# Notes to the Forecast Financial Statements

| | 2011 Actual $m | 2012 Previous Budget $m | 2012 Forecast $m | 2013 Forecast $m | 2014 Forecast $m | 2015 Forecast $m | 2016 Forecast $m |
|---|---|---|---|---|---|---|---|
| **NOTE 9: Gains and losses on financial instruments** | | | | | | | |
| ***By source*** | | | | | | | |
| Core Crown | 4,116 | 1,546 | 36 | 1,477 | 1,960 | 1,992 | 2,040 |
| Crown entities | 1,058 | 688 | 32 | 280 | 225 | 212 | 241 |
| State-owned enterprises | (281) | (68) | (86) | 19 | 65 | 59 | 59 |
| Inter-segment eliminations | (274) | (193) | 14 | (188) | (195) | (201) | (208) |
| **Net gains/(losses) on financial instruments** | **4,619** | **1,973** | **(4)** | **1,588** | **2,055** | **2,062** | **2,132** |
| **NOTE 10: Gains and losses on non-financial instruments** | | | | | | | |
| ***By type*** | | | | | | | |
| Actuarial gains/(losses) on GSF liability | (574) | - | (900) | - | - | - | - |
| Actuarial gains/(losses) on ACC outstanding claims | 996 | - | (1,418) | - | - | - | - |
| Other | (343) | 172 | 254 | 191 | 170 | 176 | 185 |
| **Net gains/(losses) on non-financial instruments** | **79** | **172** | **(2,064)** | **191** | **170** | **176** | **185** |
| ***By source*** | | | | | | | |
| Core Crown | (588) | (8) | (834) | (3) | (6) | (9) | (10) |
| Crown entities | 931 | (1) | (1,429) | (14) | (41) | (36) | (32) |
| State-owned enterprises | (264) | 180 | 199 | 207 | 217 | 221 | 226 |
| Inter-segment eliminations | - | 1 | - | 1 | - | - | 1 |
| **Net gains/(losses) on non-financial instruments** | **79** | **172** | **(2,064)** | **191** | **170** | **176** | **185** |
| **NOTE 11: Source of operating balance** | | | | | | | |
| Core Crown | (9,267) | (10,350) | (14,010) | (4,318) | (457) | 1,261 | 3,237 |
| Crown entities | (3,143) | 2,533 | 538 | 1,633 | 1,558 | 1,997 | 1,720 |
| State-owned enterprises | 327 | 981 | 1,097 | 1,184 | 1,407 | 1,612 | 1,738 |
| Inter-segment eliminations | (1,277) | (457) | (226) | (874) | (932) | (896) | (994) |
| **Total operating balance** | **(13,360)** | **(7,293)** | **(12,601)** | **(2,375)** | **1,576** | **3,974** | **5,701** |
| **NOTE 12: Financial assets** | | | | | | | |
| Cash and cash equivalents | 9,801 | 8,886 | 9,185 | 9,261 | 10,009 | 10,010 | 10,423 |
| Tax receivables | 7,104 | 6,788 | 7,348 | 7,121 | 7,085 | 7,136 | 7,309 |
| Trade and other receivables | 14,586 | 9,921 | 11,450 | 8,801 | 8,154 | 7,945 | 8,086 |
| Student loans (refer note 13) | 7,460 | 7,822 | 7,932 | 8,407 | 8,869 | 9,286 | 9,647 |
| Kiwibank mortgages | 11,495 | 13,493 | 12,950 | 14,474 | 16,036 | 17,611 | 19,186 |
| Long-term deposits | 2,259 | 2,047 | 2,402 | 2,234 | 2,250 | 2,777 | 2,977 |
| IMF financial assets | 2,168 | 2,528 | 2,346 | 2,515 | 2,515 | 2,516 | 2,350 |
| Other advances | 1,612 | 1,118 | 1,299 | 1,347 | 1,440 | 1,587 | 1,668 |
| Share investments | 14,248 | 16,095 | 18,443 | 20,695 | 22,300 | 24,504 | 26,958 |
| Derivatives in gain | 5,415 | 2,394 | 4,188 | 3,176 | 2,521 | 2,124 | 1,649 |
| Other marketable securities | 39,214 | 36,065 | 33,561 | 25,911 | 31,155 | 28,013 | 31,759 |
| **Total financial assets** | **115,362** | **107,157** | **111,104** | **103,942** | **112,334** | **113,509** | **122,012** |
| **Financial assets by entity** | | | | | | | |
| NZDMO | 29,928 | 20,413 | 23,314 | 13,482 | 16,904 | 11,762 | 13,253 |
| Reserve Bank of New Zealand | 17,909 | 17,628 | 16,752 | 16,728 | 16,746 | 16,365 | 16,557 |
| NZS Fund | 18,687 | 19,543 | 18,872 | 20,036 | 21,674 | 23,263 | 24,997 |
| Other core Crown | 19,116 | 17,694 | 19,110 | 19,266 | 19,804 | 20,638 | 21,223 |
| Intra-segment eliminations | (9,165) | (6,769) | (7,538) | (6,574) | (5,933) | (4,781) | (4,746) |
| **Total core Crown segment** | 76,475 | 68,509 | 70,510 | 62,938 | 69,195 | 67,247 | 71,284 |
| ACC portfolio | 21,569 | 23,742 | 24,548 | 27,108 | 29,891 | 32,891 | 36,234 |
| EQC portfolio | 9,305 | 6,168 | 6,495 | 3,831 | 1,038 | 62 | 171 |
| Other Crown entities | 8,831 | 6,343 | 8,284 | 8,081 | 8,255 | 7,922 | 8,052 |
| Intra-segment eliminations | (3,314) | (1,532) | (3,426) | (3,432) | (3,439) | (2,945) | (2,953) |
| **Total Crown entities segment** | 36,391 | 34,721 | 35,901 | 35,588 | 35,745 | 37,930 | 41,504 |
| **Total state-owned enterprises segment** | 20,241 | 19,624 | 20,789 | 21,847 | 23,472 | 25,658 | 27,736 |
| Inter-segment eliminations | (17,745) | (15,697) | (16,096) | (16,431) | (16,078) | (17,326) | (18,512) |
| **Total financial assets** | **115,362** | **107,157** | **111,104** | **103,942** | **112,334** | **113,509** | **122,012** |

# Notes to the Forecast Financial Statements

| | 2011 Actual $m | 2012 Previous Budget $m | 2012 Forecast $m | 2013 Forecast $m | 2014 Forecast $m | 2015 Forecast $m | 2016 Forecast $m |
|---|---|---|---|---|---|---|---|
| **NOTE 13: Student loans** | | | | | | | |
| Nominal value (including accrued interest) | 12,070 | 12,909 | 12,981 | 13,861 | 14,721 | 15,522 | 16,265 |
| Opening book value | 6,790 | 7,325 | 7,460 | 7,932 | 8,407 | 8,869 | 9,286 |
| Amount borrowed in current year | 1,564 | 1,590 | 1,588 | 1,617 | 1,650 | 1,653 | 1,673 |
| Less initial write-down to fair value | (713) | (707) | (698) | (679) | (693) | (693) | (702) |
| Repayments made during the year | (802) | (834) | (852) | (940) | (1,010) | (1,089) | (1,184) |
| Interest unwind | 484 | 534 | 532 | 576 | 612 | 645 | 673 |
| (Impairment)/reversal of impairment | 125 | (110) | (110) | (110) | (110) | (110) | (110) |
| Other movements | 12 | 24 | 12 | 11 | 13 | 11 | 11 |
| **Closing book value** | **7,460** | **7,822** | **7,932** | **8,407** | **8,869** | **9,286** | **9,647** |
| **NOTE 14: Property, plant and equipment** | | | | | | | |
| ***By class of asset*** | | | | | | | |
| **Net carrying value** | | | | | | | |
| Land (valuation) | 16,372 | 16,892 | 16,774 | 16,981 | 17,099 | 17,438 | 17,673 |
| Buildings (valuation) | 24,539 | 25,232 | 25,514 | 25,841 | 25,829 | 25,389 | 25,433 |
| Electricity distribution network (cost) | 2,690 | 3,553 | 3,267 | 3,845 | 4,299 | 4,518 | 4,590 |
| Electricity generation assets (valuation) | 14,439 | 14,915 | 15,208 | 15,603 | 16,043 | 16,634 | 17,260 |
| Aircraft (excluding military) (valuation) | 1,805 | 2,587 | 2,048 | 2,268 | 2,593 | 2,771 | 2,944 |
| State highways (valuation) | 25,126 | 26,504 | 25,842 | 26,679 | 27,648 | 28,686 | 29,890 |
| Rail network (valuation) | 12,749 | 12,755 | 12,986 | 13,100 | 13,191 | 13,227 | 13,163 |
| Specialist military equipment (valuation) | 3,331 | 3,377 | 3,271 | 3,167 | 2,986 | 2,789 | 2,582 |
| Specified cultural and heritage assets (valuation) | 8,133 | 8,559 | 8,169 | 8,199 | 8,223 | 8,248 | 8,277 |
| Other plant and equipment (cost) | 5,670 | 6,812 | 5,988 | 6,236 | 6,263 | 6,429 | 6,585 |
| **Total property, plant and equipment** | **114,854** | **121,186** | **119,067** | **121,919** | **124,174** | **126,129** | **128,397** |
| ***By source*** | | | | | | | |
| Core Crown | 29,549 | 30,595 | 30,121 | 30,198 | 30,082 | 29,986 | 30,191 |
| Crown entities | 48,480 | 50,949 | 50,148 | 51,488 | 52,485 | 53,521 | 54,728 |
| State-owned enterprises | 36,825 | 39,642 | 38,798 | 40,233 | 41,607 | 42,622 | 43,478 |
| Inter-segment eliminations | - | - | - | - | - | - | - |
| **Total property, plant and equipment** | **114,854** | **121,186** | **119,067** | **121,919** | **124,174** | **126,129** | **128,397** |
| ***Schedule of movements*** | | | | | | | |
| Cost or valuation | | | | | | | |
| Opening balance | 123,941 | 131,282 | 126,601 | 135,184 | 142,025 | 148,361 | 154,402 |
| Additions (refer below for further breakdown) | 6,644 | 8,628 | 8,673 | 7,316 | 6,812 | 6,566 | 6,903 |
| Disposals | (1,283) | (287) | (371) | (292) | (374) | (463) | (405) |
| Net revaluations | (2,471) | - | 50 | - | - | - | - |
| Other | (230) | (240) | 231 | (183) | (102) | (62) | (88) |
| **Total cost or valuation** | **126,601** | **139,383** | **135,184** | **142,025** | **148,361** | **154,402** | **160,812** |
| Accumulated depreciation and impairment | | | | | | | |
| Opening balance | 10,611 | 14,349 | 11,747 | 16,117 | 20,106 | 24,187 | 28,273 |
| Eliminated on disposal | (832) | (73) | (109) | (73) | (63) | (88) | (66) |
| Eliminated on revaluation | (1,884) | - | - | - | - | - | - |
| Depreciation expense | 3,727 | 4,032 | 3,952 | 4,169 | 4,288 | 4,338 | 4,405 |
| Other | 125 | (111) | 527 | (107) | (144) | (164) | (197) |
| **Total accumulated depreciation and impairment** | **11,747** | **18,197** | **16,117** | **20,106** | **24,187** | **28,273** | **32,415** |
| **Total property, plant and equipment** | **114,854** | **121,186** | **119,067** | **121,919** | **124,174** | **126,129** | **128,397** |
| ***Additions - by functional classification*** | | | | | | | |
| Transport | 2,807 | 2,685 | 2,401 | 2,338 | 2,535 | 2,418 | 2,462 |
| Economic | 1,200 | 2,573 | 2,115 | 1,856 | 1,808 | 1,747 | 1,766 |
| Education | 648 | 865 | 886 | 801 | 724 | 728 | 727 |
| Health | 617 | 605 | 992 | 508 | 394 | 344 | 344 |
| Defence | 258 | 726 | 690 | 509 | 199 | 144 | 103 |
| Other | 1,114 | 1,174 | 1,589 | 1,304 | 1,152 | 1,185 | 1,501 |
| **Total additions to property, plant and equipment[1]** | **6,644** | **8,628** | **8,673** | **7,316** | **6,812** | **6,566** | **6,903** |

Note 1: These additions do not include any purchases which may result from the allocation of the net forecast for new capital spending (separately disclosed in the Statement of Financial Position).

# Notes to the Forecast Financial Statements

| | 2011 Actual $m | 2012 Previous Budget $m | 2012 Forecast $m | 2013 Forecast $m | 2014 Forecast $m | 2015 Forecast $m | 2016 Forecast $m |
|---|---|---|---|---|---|---|---|
| **NOTE 15: Intangible assets and goodwill** | | | | | | | |
| ***By type*** | | | | | | | |
| Net Kyoto position[1] | 291 | 444 | 282 | 282 | 282 | 282 | 282 |
| Goodwill | 485 | 484 | 442 | 431 | 452 | 452 | 452 |
| Other intangible assets | 1,618 | 1,786 | 1,873 | 1,949 | 1,983 | 1,971 | 1,946 |
| **Total intangible assets and goodwill** | **2,394** | **2,714** | **2,597** | **2,662** | **2,717** | **2,705** | **2,680** |
| ***By source*** | | | | | | | |
| Core Crown | 1,157 | 1,498 | 1,335 | 1,391 | 1,429 | 1,428 | 1,414 |
| Crown entities | 430 | 500 | 516 | 531 | 518 | 493 | 471 |
| State-owned enterprises | 807 | 716 | 746 | 740 | 770 | 784 | 795 |
| Inter-segment eliminations | - | - | - | - | - | - | - |
| **Total intangible assets and goodwill** | **2,394** | **2,714** | **2,597** | **2,662** | **2,717** | **2,705** | **2,680** |

Note 1: The New Zealand Government has committed under the Kyoto Protocol to ensuring that New Zealand's average net emissions of greenhouse gases from 2008 to 2012 (the first commitment period of the Kyoto Protocol, or CP1) are reduced to 1990 levels, or to take responsibility for the difference. New Zealand can meet its commitment through emissions reductions and use of the Kyoto Protocol flexibility mechanisms such as Joint Implementation, the Clean Development Mechanism, and offsetting increased emissions against carbon removed by forests.

To assist New Zealand in meeting its Kyoto Protocol commitments, an Emissions Trading Scheme (ETS) was established (refer note 20). These two initiatives should be looked at together when understanding New Zealand's international climate change obligations. The asset reported in these financial statements could be significantly reduced if international units are transferred offshore through foresters participating in the ETS. This, combined with other ETS variables, has a significant impact on the Government's net fiscal position from the Kyoto Protocol, which will crystallise when the first Kyoto commitment period is settled up post-2012.

These financial statements report on the New Zealand Government's international climate change obligations for the first commitment period, but not for future commitment periods which are currently being negotiated.

The latest Net Position estimate for 2011 can be found on the Ministry for the Environment's website: www.mfe.govt.nz/issues/climate/greenhouse-gas-emissions/net-position

| | 2011 Actual $m | 2012 Previous Budget $m | 2012 Forecast $m | 2013 Forecast $m | 2014 Forecast $m | 2015 Forecast $m | 2016 Forecast $m |
|---|---|---|---|---|---|---|---|
| **NOTE 16: NZS Fund** | | | | | | | |
| Revenue | 518 | 551 | 590 | 641 | 670 | 709 | 743 |
| Less current tax expense | 872 | 367 | (20) | 403 | 441 | 482 | 527 |
| Less other expenses | 169 | 172 | 171 | 184 | 202 | 216 | 235 |
| Add gains/(losses) | 3,518 | 1,215 | (425) | 1,066 | 1,584 | 1,698 | 1,842 |
| **Operating balance** | **2,995** | **1,227** | **14** | **1,120** | **1,611** | **1,709** | **1,823** |
| Opening net worth | 15,656 | 18,668 | 18,652 | 18,672 | 19,801 | 21,422 | 23,143 |
| Gross contribution from the Crown | - | - | - | - | - | - | - |
| Operating balance | 2,995 | 1,227 | 14 | 1,120 | 1,611 | 1,709 | 1,823 |
| Other movements in reserves | 1 | 6 | 6 | 9 | 10 | 12 | 14 |
| **Closing net worth** | **18,652** | **19,901** | **18,672** | **19,801** | **21,422** | **23,143** | **24,980** |
| ***Comprising:*** | | | | | | | |
| Financial assets | 18,687 | 19,543 | 18,872 | 20,036 | 21,674 | 23,263 | 24,997 |
| Financial liabilities | (1,161) | (674) | (1,436) | (1,461) | (1,462) | (1,432) | (1,436) |
| Net other assets | 1,126 | 1,032 | 1,236 | 1,226 | 1,210 | 1,312 | 1,419 |
| **Closing net worth** | **18,652** | **19,901** | **18,672** | **19,801** | **21,422** | **23,143** | **24,980** |
| **NOTE 17: Payables** | | | | | | | |
| ***By type*** | | | | | | | |
| Accounts payable | 7,337 | 6,161 | 8,541 | 8,206 | 8,468 | 8,343 | 8,519 |
| Taxes repayable | 3,762 | 3,442 | 3,762 | 3,762 | 4,162 | 4,612 | 5,112 |
| **Total payables** | **11,099** | **9,603** | **12,303** | **11,968** | **12,630** | **12,955** | **13,631** |
| ***By source*** | | | | | | | |
| Core Crown | 6,997 | 6,371 | 7,085 | 6,818 | 7,291 | 7,457 | 7,923 |
| Crown entities | 5,587 | 4,663 | 6,314 | 6,286 | 6,300 | 6,346 | 6,531 |
| State-owned enterprises | 4,779 | 4,917 | 5,406 | 5,537 | 5,853 | 6,013 | 6,201 |
| Inter-segment eliminations | (6,264) | (6,348) | (6,502) | (6,673) | (6,814) | (6,861) | (7,024) |
| **Total payables** | **11,099** | **9,603** | **12,303** | **11,968** | **12,630** | **12,955** | **13,631** |

# Notes to the Forecast Financial Statements

| | 2011 Actual $m | 2012 Previous Budget $m | 2012 Forecast $m | 2013 Forecast $m | 2014 Forecast $m | 2015 Forecast $m | 2016 Forecast $m |
|---|---|---|---|---|---|---|---|
| **NOTE 18: Insurance liabilities** | | | | | | | |
| ***By entity*** | | | | | | | |
| ACC liability | 26,939 | 27,687 | 29,025 | 30,388 | 31,896 | 33,574 | 35,415 |
| EQC property damage claims | 10,570 | 2,785 | 7,616 | 4,884 | 2,054 | 144 | 145 |
| AMI liability | 2,082 | - | 1,560 | 835 | 452 | 371 | 289 |
| Other insurance liabilities | (277) | 61 | 71 | 78 | 86 | 96 | 106 |
| **Total insurance liabilities** | **39,314** | **30,533** | **38,272** | **36,185** | **34,488** | **34,185** | **35,955** |

**ACC liability**

**Calculation information**

PricewaterhouseCoopers Actuarial Pty Ltd have prepared an independent actuarial estimate of the ACC outstanding claims liability as at 30 June 2011. This estimate includes the expected future payments relating to accidents that occurred prior to balance date (whether or not the associated claims have been reported to, or accepted by, ACC) and also the expected future administrative expenses of managing these claims.

The key economic variables that impact on changes to the valuation are the long-term Labour Cost Index (LCI), average weekly earnings and the discount rate. Discount rates were derived from the yield curve for New Zealand Government bonds. For these forecast statements, the claims liability has been updated for the latest discount rates as at 31 August 2011. The equivalent single effective discount rate, taking into account ACC's projected future cash flow patterns, is a short-term discount rate of 5.15% and a long-term discount rate of 6%.

Other key variables in each valuation are the forecast increases in claim costs over and above the economic variables above, and the assumed rate at which long-term claimants will leave the scheme over the period. This assessment is largely based on scheme history.

**Presentation approach**

The projected outstanding claims liability is included within total liabilities. ACC has available to it a portfolio of assets that partially offset the claims liability. The assets (less cross-holdings of NZ Government stock) are included in the asset portion of the Crown's overall statement of financial position.

| | 2011 Actual $m | 2012 Previous Budget $m | 2012 Forecast $m | 2013 Forecast $m | 2014 Forecast $m | 2015 Forecast $m | 2016 Forecast $m |
|---|---|---|---|---|---|---|---|
| **Gross ACC liability** | | | | | | | |
| Opening gross liability | 26,997 | 26,761 | 26,939 | 29,025 | 30,388 | 31,896 | 33,574 |
| Net change | (58) | 926 | 2,086 | 1,363 | 1,508 | 1,678 | 1,841 |
| Closing gross liability | **26,939** | **27,687** | **29,025** | **30,388** | **31,896** | **33,574** | **35,415** |
| **Less net assets available to ACC** | | | | | | | |
| Opening net asset value | 16,745 | 20,236 | 20,233 | 22,380 | 24,957 | 27,735 | 30,762 |
| Net change | 3,488 | 2,926 | 2,147 | 2,577 | 2,778 | 3,027 | 3,233 |
| Closing net asset value | **20,233** | **23,162** | **22,380** | **24,957** | **27,735** | **30,762** | **33,995** |
| **Net ACC reserves (net liability)** | | | | | | | |
| Opening reserves position | (10,252) | (6,525) | (6,706) | (6,645) | (5,431) | (4,161) | (2,812) |
| Net change | 3,546 | 2,000 | 61 | 1,214 | 1,270 | 1,349 | 1,392 |
| Closing reserves position (net liability) | **(6,706)** | **(4,525)** | **(6,645)** | **(5,431)** | **(4,161)** | **(2,812)** | **(1,420)** |

# Notes to the Forecast Financial Statements

| | 2011 Actual $m | 2012 Previous Budget $m | 2012 Forecast $m | 2013 Forecast $m | 2014 Forecast $m | 2015 Forecast $m | 2016 Forecast $m |
|---|---|---|---|---|---|---|---|
| **NOTE 19: Retirement plan liabilities** | | | | | | | |
| Government Superannuation Fund | 10,152 | 8,891 | 10,574 | 10,182 | 9,862 | 9,589 | 9,337 |
| Other funds | 4 | 4 | 7 | 7 | 7 | 7 | 7 |
| **Total retirement plan liabilities** | **10,156** | **8,895** | **10,581** | **10,189** | **9,869** | **9,596** | **9,344** |

The net liability of the Government Superannuation Fund (GSF) was calculated by the Government Actuary as at 30 June 2011. The liability arises from closed schemes for past and present public sector employees as set out in the Government Superannuation Fund Act 1956. A Projected Unit Credit method is used to calculate the liability as at 30 June 2011, based on membership data as at that date. The funding method requires the benefits payable from GSF in respect of past service to be calculated and then discounted back to the valuation date.

For these forecast financial statements, the net GSF liability was updated for the latest discount rates derived from the market yield curve for New Zealand Government bonds as at 31 August 2011.

Other principal long-term financial assumptions were an inflation rate, as measured by the Consumer Price Index, of 2.6% for 2012 decreasing to 2.5% in 2013 (unchanged from 30 June 2011) and an annual salary growth rate, before any promotional effects, of 3% (unchanged from 30 June 2011).

The 2011/12 projected increase in the net GSF liability is $422 million, reflecting an increase in the GSF liability of $282 million and a decrease in the GSF assets of $140 million.

The increase in the GSF liability of $282 million includes an actuarial loss between 1 July 2011 and 31 August 2011, of $700 million owing to movements in the discount rates. The remaining $418m reduction is due to expected benefits paid to members (reduces the liability) and current service cost and interest unwind (increases the liability).

The decrease in the value of the net assets of GSF of $140 million includes a loss of $200 million reflecting the updated market value of assets at 31 August 2011. The balance of $60 million is the total of the expected investment returns and contributions received, offset by the benefits paid to members.

The changes in the projected net GSF liability from 2011/12 onwards reflect the net of the expected current service cost, interest cost, investment returns and contributions.

| | 2011 Actual $m | 2012 Previous Budget $m | 2012 Forecast $m | 2013 Forecast $m | 2014 Forecast $m | 2015 Forecast $m | 2016 Forecast $m |
|---|---|---|---|---|---|---|---|
| **GSF net defined benefit retirement liability** | | | | | | | |
| **GSF liability** | | | | | | | |
| Opening GSF liability | 12,881 | 12,497 | 13,311 | 13,593 | 13,259 | 12,997 | 12,777 |
| Net projected change | 430 | (321) | 282 | (334) | (262) | (220) | (201) |
| Closing GSF liability | **13,311** | **12,176** | **13,593** | **13,259** | **12,997** | **12,777** | **12,576** |
| **Less net assets available to GSF** | | | | | | | |
| Opening net asset value | 2,945 | 3,229 | 3,159 | 3,019 | 3,077 | 3,135 | 3,188 |
| Investment valuation changes | 336 | 180 | (15) | 189 | 196 | 196 | 199 |
| Contribution and other income less pension payments | (122) | (124) | (125) | (131) | (138) | (143) | (148) |
| Closing net asset value | **3,159** | **3,285** | **3,019** | **3,077** | **3,135** | **3,188** | **3,239** |
| **Net GSF liability** | | | | | | | |
| Opening unfunded liability | 9,936 | 9,268 | 10,152 | 10,574 | 10,182 | 9,862 | 9,589 |
| Net projected change | 216 | (377) | 422 | (392) | (320) | (273) | (252) |
| Closing unfunded liability | **10,152** | **8,891** | **10,574** | **10,182** | **9,862** | **9,589** | **9,337** |

# Notes to the Forecast Financial Statements

| | 2011 Actual $m | 2012 Previous Budget $m | 2012 Forecast $m | 2013 Forecast $m | 2014 Forecast $m | 2015 Forecast $m | 2016 Forecast $m |
|---|---|---|---|---|---|---|---|
| **NOTE 20: Provisions** | | | | | | | |
| Provision for ETS credits | 612 | 1,241 | 1,492 | 1,387 | 1,113 | 813 | 473 |
| Provision for National Provident Fund guarantee | 983 | 925 | 918 | 850 | 794 | 743 | 692 |
| Provision for employee entitlements | 3,050 | 2,919 | 2,990 | 3,073 | 3,019 | 3,018 | 3,109 |
| Provision for Canterbury Red Zone support package | 1,039 | - | 610 | - | - | - | - |
| Provision for weathertight services financial assistance package | 567 | 687 | 556 | 392 | 209 | 52 | 6 |
| Other provisions | 1,335 | 3,157 | 2,503 | 2,094 | 1,925 | 1,455 | 1,324 |
| **Total provisions** | **7,586** | **8,929** | **9,069** | **7,796** | **7,060** | **6,081** | **5,604** |
| ***By source*** | | | | | | | |
| Core Crown | 5,351 | 6,433 | 6,833 | 5,571 | 4,551 | 3,661 | 2,917 |
| Crown entities | 1,770 | 1,705 | 1,734 | 1,755 | 1,771 | 1,775 | 1,783 |
| State-owned enterprises | 1,028 | 882 | 945 | 927 | 955 | 1,014 | 1,042 |
| Inter-segment eliminations | (563) | (91) | (443) | (457) | (217) | (369) | (138) |
| **Total provisions** | **7,586** | **8,929** | **9,069** | **7,796** | **7,060** | **6,081** | **5,604** |

**Provision for ETS credits**

The Emissions Trading Scheme (ETS) was established to encourage reduction in greenhouse gas emissions. The ETS creates a limited number of tradable units (the NZ Unit) which the Government can allocate freely. The allocation of NZ Units creates a provision (and an expense if allocated for free). The provision is reduced, and revenue recognised, as NZ Units are surrendered to the Crown by emitters. Emitters can also use international Kyoto Units to settle their emission obligation, which might occur where obligations exceed the number of allocated NZ Units. In the ETS transition period to the end of 2012, emitters can also use the NZ$25 price option to settle their emission obligation.

Until the end of 2012, the Government's net position regarding its climate change obligations will be determined by the net Kyoto position and the provision for ETS credits. After 2012, the net position will depend on any future international climate change commitments.

The carbon price used to calculate the ETS provision is assumed to remain constant over the forecast period and is based on the estimated current carbon price of €10.40 with an exchange rate of 0.5907 (a carbon price of NZ$17.61).

The carbon price for the ETS provision has been determined by the Ministry for the Environment based on international market transactions that have occurred in the certified emission reduction (CER) markets. Currently, the CER market has been determined to be the most relevant market to use for determining the carbon price for NZ Units and the calculation of the provision for ETS credits. As the market for NZ Units develops the basis for determining this carbon price will be reviewed.

The ETS impact on the fiscal forecast is as follows:

| | | | | | | | |
|---|---|---|---|---|---|---|---|
| Revenue | 322 | 379 | 298 | 485 | 669 | 956 | 1,328 |
| Expenses | 860 | 692 | 1,178 | 380 | 395 | 656 | 988 |
| **OBEGAL** | **(538)** | **(313)** | **(880)** | **105** | **274** | **300** | **340** |

# Notes to the Forecast Financial Statements

| | 2011 Actual $m | 2012 Previous Budget $m | 2012 Forecast $m | 2013 Forecast $m | 2014 Forecast $m | 2015 Forecast $m | 2016 Forecast $m |
|---|---|---|---|---|---|---|---|
| **NOTE 21: Net worth attributable to the Crown** | | | | | | | |
| Taxpayer funds | 18,188 | 14,463 | 5,631 | 3,322 | 4,934 | 8,933 | 14,661 |
| Property, plant and equipment revaluation reserve | 62,690 | 63,614 | 62,646 | 62,582 | 62,546 | 62,518 | 62,490 |
| Investment revaluation reserve | 58 | 69 | 61 | 69 | 79 | 92 | 106 |
| Cash flow hedge reserve | (310) | (223) | (323) | (325) | (324) | (320) | (319) |
| Foreign currency translation reserve | (47) | (53) | (41) | (17) | (17) | (17) | (17) |
| **Total net worth attributable to the Crown** | **80,579** | **77,870** | **67,974** | **65,631** | **67,218** | **71,206** | **76,921** |
| **Taxpayer Funds** | | | | | | | |
| Opening taxpayer funds | 31,087 | 21,720 | 18,188 | 5,631 | 3,322 | 4,934 | 8,933 |
| Operating balance excluding minority interest | (13,360) | (7,293) | (12,601) | (2,375) | 1,576 | 3,974 | 5,701 |
| Transfers from/(to) other reserves | 461 | 36 | 44 | 66 | 36 | 25 | 27 |
| **Closing taxpayer funds** | **18,188** | **14,463** | **5,631** | **3,322** | **4,934** | **8,933** | **14,661** |
| **Property, plant and equipment revaluation reserve** | | | | | | | |
| Opening revaluation reserve | 63,593 | 63,600 | 62,690 | 62,646 | 62,582 | 62,546 | 62,518 |
| Net revaluations | (443) | - | - | - | (1) | - | - |
| Transfers from/(to) other reserves | (460) | 14 | (44) | (64) | (35) | (28) | (28) |
| **Closing property, plant and equipment revaluation reserve** | **62,690** | **63,614** | **62,646** | **62,582** | **62,546** | **62,518** | **62,490** |
| **Investment revaluation reserve** | | | | | | | |
| Opening investment revaluation reserve | 59 | 63 | 58 | 61 | 69 | 79 | 92 |
| Valuation gain/(losses) on investments available for sale taken to reserves | (1) | 6 | 3 | 8 | 10 | 13 | 14 |
| **Closing investment revaluation reserve** | **58** | **69** | **61** | **69** | **79** | **92** | **106** |
| **Cash flow hedge reserve** | | | | | | | |
| Opening cash flow hedge reserve | (143) | (219) | (310) | (323) | (325) | (324) | (320) |
| Transfer into reserve | (279) | 3 | 7 | (1) | 1 | 4 | - |
| Transfer to the Statement of Financial Performance | 17 | - | 1 | 1 | - | - | 1 |
| Transfer to initial carrying value of hedged item | 95 | (7) | (21) | (2) | - | - | - |
| **Closing cash flow hedge reserve** | **(310)** | **(223)** | **(323)** | **(325)** | **(324)** | **(320)** | **(319)** |
| **Foreign currency translation reserve** | | | | | | | |
| Opening foreign currency translation reserve | (10) | (47) | (47) | (41) | (17) | (17) | (17) |
| Movement arising from translation of foreign operations | (37) | (6) | 6 | 24 | - | - | - |
| **Closing foreign currency translation reserve** | **(47)** | **(53)** | **(41)** | **(17)** | **(17)** | **(17)** | **(17)** |

# Notes to the Forecast Financial Statements

| | 2011 Actual $m | 2012 Previous Budget $m | 2012 Forecast $m | 2013 Forecast $m | 2014 Forecast $m | 2015 Forecast $m | 2016 Forecast $m |
|---|---|---|---|---|---|---|---|
| **NOTE 22: Reconciliation of core Crown operating cash flows to residual core Crown cash** | | | | | | | |
| **Core Crown cash flows from operations** | | | | | | | |
| Total tax receipts | 51,454 | 55,084 | 54,801 | 58,629 | 63,325 | 67,297 | 71,112 |
| Total other sovereign receipts | 646 | 645 | 693 | 686 | 715 | 731 | 743 |
| Interest, profits and dividends | 1,817 | 1,469 | 1,462 | 1,938 | 1,840 | 1,996 | 2,005 |
| Sale of goods and services and other receipts | 2,094 | 2,496 | 2,895 | 2,238 | 2,087 | 2,051 | 2,035 |
| Transfer payments and subsidies | (22,226) | (23,448) | (23,103) | (23,308) | (23,825) | (24,677) | (25,728) |
| Personnel and operating costs | (40,433) | (42,107) | (43,101) | (41,293) | (39,785) | (40,291) | (39,569) |
| Finance costs | (2,637) | (3,493) | (3,450) | (3,995) | (3,934) | (4,512) | (4,446) |
| Forecast for future new operating spending | - | (463) | (623) | (944) | (1,788) | (2,932) | (3,959) |
| Top-down expense adjustment | - | 310 | 1,100 | 300 | 100 | 100 | 100 |
| **Net cash flows from core Crown operations** | **(9,285)** | **(9,507)** | **(9,326)** | **(5,749)** | **(1,265)** | **(237)** | **2,293** |
| Net purchase of physical assets | (1,524) | (1,863) | (2,133) | (1,616) | (1,379) | (1,350) | (1,617) |
| Net increase in advances | (1,242) | (879) | (1,125) | (952) | (813) | (1,162) | (553) |
| Net purchase of investments | (1,292) | (1,261) | (1,160) | (1,222) | (1,428) | (1,297) | (1,638) |
| Contribution to NZS Fund | - | - | - | - | - | - | - |
| Forecast for future new capital spending | - | (242) | (192) | (452) | (651) | (800) | (900) |
| Balance sheet funding of new capital spending | - | 100 | (50) | 125 | 560 | 790 | 835 |
| Top-down capital adjustment | - | 170 | 350 | - | - | - | - |
| **Residual cash** | **(13,343)** | **(13,482)** | **(13,636)** | **(9,866)** | **(4,976)** | **(4,056)** | **(1,580)** |
| ***Financed by:*** | | | | | | | |
| Other net sale/(purchase) of marketable securities and deposits | (4,791) | 6,733 | 6,517 | 8,701 | (4,405) | 4,456 | (1,880) |
| **Total operating and investing activities** | **(18,134)** | **(6,749)** | **(7,119)** | **(1,165)** | **(9,381)** | **400** | **(3,460)** |
| ***Used in:*** | | | | | | | |
| Net (repayment)/issue of other New Zealand dollar borrowing | (1,835) | 8,295 | 9,521 | 194 | 733 | 2,971 | (616) |
| Net (repayment)/issue of foreign currency borrowing | 1,661 | (6,871) | (7,773) | (547) | (700) | (1,197) | (1,141) |
| Issues of circulating currency | 234 | 219 | 89 | 218 | 229 | 240 | 252 |
| Decrease/(increase) in cash | (861) | (1) | (1,250) | (2) | - | (145) | 146 |
| | **(801)** | **1,642** | **587** | **(137)** | **262** | **1,869** | **(1,359)** |
| **Net cash inflow/(outflow) to be offset by domestic bonds** | **(18,935)** | **(5,107)** | **(6,532)** | **(1,302)** | **(9,119)** | **2,269** | **(4,819)** |
| **Gross cash proceeds from domestic bonds** | | | | | | | |
| Domestic bonds (market) | 19,468 | 13,635 | 15,422 | 12,773 | 10,030 | 7,833 | 4,819 |
| Domestic bonds (non-market) | 270 | 187 | 448 | 122 | 36 | - | - |
| **Total gross cash proceeds from domestic bonds** | **19,738** | **13,822** | **15,870** | **12,895** | **10,066** | **7,833** | **4,819** |
| Repayment of domestic bonds (market) | - | (7,602) | (7,602) | (10,957) | - | (9,955) | - |
| Repayment of domestic bonds (non-market) | (803) | (1,113) | (1,736) | (636) | (947) | (147) | - |
| **Net cash proceeds from domestic bonds** | **18,935** | **5,107** | **6,532** | **1,302** | **9,119** | **(2,269)** | **4,819** |

# Forecast Statement of Segments

| | Core Crown | Crown entities | State-owned enterprises | Inter-segment eliminations | Total Crown |
|---|---|---|---|---|---|
| | 2011 | 2011 | 2011 | 2011 | 2011 |
| | Actual | Actual | Actual | Actual | Actual |
| | $m | $m | $m | $m | $m |
| **Statement of Financial Performance for the year ended 30 June 2011** | | | | | |
| **Revenue** | | | | | |
| Taxation revenue | 51,557 | - | - | (429) | 51,128 |
| Other sovereign revenue | 1,275 | 5,080 | - | (1,074) | 5,281 |
| Sales of goods and services | 1,443 | 14,680 | 12,510 | (13,549) | 15,084 |
| Interest revenue and dividends | 2,169 | 1,234 | 801 | (1,634) | 2,570 |
| Other revenue | 1,106 | 17,042 | 935 | (11,583) | 7,500 |
| **Total revenue (excluding gains)** | **57,550** | **38,036** | **14,246** | **(28,269)** | **81,563** |
| **Expenses** | | | | | |
| Social assistance and official development assistance | 22,227 | - | - | (55) | 22,172 |
| Personnel expenses | 5,996 | 10,410 | 2,695 | (13) | 19,088 |
| Other operating expenses | 39,161 | 32,670 | 9,727 | (26,455) | 55,103 |
| Interest expenses | 3,066 | 248 | 1,027 | (745) | 3,596 |
| Forecast for future new spending and top-down adjustment | - | - | - | - | - |
| **Total expenses (excluding losses)** | **70,450** | **43,328** | **13,449** | **(27,268)** | **99,959** |
| **Operating balance before gains/(losses)** | **(12,900)** | **(5,292)** | **797** | **(1,001)** | **(18,396)** |
| Total gains/(losses) | 3,530 | 1,989 | (545) | (276) | 4,698 |
| Net surplus/(deficit) from associates and joint ventures | 103 | 160 | (26) | - | 237 |
| Attributable to minority interest in Air NZ | - | - | 101 | - | 101 |
| **Operating balance** | **(9,267)** | **(3,143)** | **327** | **(1,277)** | **(13,360)** |
| **Expenses by functional classification** | | | | | |
| Social security and welfare | 22,005 | 3,945 | - | (626) | 25,324 |
| Health | 13,753 | 11,467 | - | (12,152) | 13,068 |
| Education | 11,650 | 9,176 | 23 | (8,443) | 12,406 |
| Transport and communications | 2,281 | 2,117 | 6,203 | (2,199) | 8,402 |
| Other | 17,695 | 16,375 | 6,196 | (3,103) | 37,163 |
| Finance costs | 3,066 | 248 | 1,027 | (745) | 3,596 |
| Forecast for future new spending and top-down adjustment | - | - | - | - | - |
| **Total Crown expenses (excluding losses)** | **70,450** | **43,328** | **13,449** | **(27,268)** | **99,959** |
| **Statement of Financial Position as at 30 June 2011** | | | | | |
| **Assets** | | | | | |
| Cash and cash equivalents | 6,087 | 2,773 | 1,425 | (484) | 9,801 |
| Receivables | 11,376 | 8,999 | 3,576 | (2,261) | 21,690 |
| Other financial assets | 59,012 | 24,619 | 15,240 | (15,000) | 83,871 |
| Property, plant and equipment | 29,549 | 48,480 | 36,825 | - | 114,854 |
| Equity accounted investments | 30,093 | 7,979 | 197 | (28,968) | 9,301 |
| Intangible assets and goodwill | 1,157 | 430 | 807 | - | 2,394 |
| Inventory and other assets | 1,691 | 378 | 1,290 | (55) | 3,304 |
| Forecast for new capital spending and top-down adjustment | - | - | - | - | - |
| **Total assets** | **138,965** | **93,658** | **59,360** | **(46,768)** | **245,215** |
| **Liabilities** | | | | | |
| Borrowings | 76,827 | 5,123 | 23,099 | (14,804) | 90,245 |
| Other liabilities | 27,207 | 45,105 | 9,021 | (7,250) | 74,083 |
| **Total liabilities** | **104,034** | **50,228** | **32,120** | **(22,054)** | **164,328** |
| **Total assets less total liabilities** | **34,931** | **43,430** | **27,240** | **(24,714)** | **80,887** |
| **Net worth** | | | | | |
| Taxpayer funds | 19,531 | 17,098 | 9,574 | (28,015) | 18,188 |
| Reserves | 15,400 | 26,332 | 17,323 | 3,336 | 62,391 |
| Net worth attributable to minority interest in Air NZ | - | - | 343 | (35) | 308 |
| **Total net worth** | **34,931** | **43,430** | **27,240** | **(24,714)** | **80,887** |

# Forecast Statement of Segments (continued)

| | Core Crown 2012 Forecast $m | Crown entities 2012 Forecast $m | State-owned enterprises 2012 Forecast $m | Inter-segment eliminations 2012 Forecast $m | Total Crown 2012 Forecast $m |
|---|---|---|---|---|---|
| **Statement of Financial Performance for the year ended 30 June 2012** | | | | | |
| **Revenue** | | | | | |
| Taxation revenue | 55,451 | - | - | (494) | 54,957 |
| Other sovereign revenue | 1,445 | 5,391 | - | (1,273) | 5,563 |
| Sales of goods and services | 1,457 | 14,803 | 14,178 | (13,613) | 16,825 |
| Interest revenue and dividends | 2,039 | 1,325 | 828 | (1,378) | 2,814 |
| Other revenue | 773 | 13,229 | 1,074 | (11,598) | 3,478 |
| **Total revenue (excluding gains)** | **61,165** | **34,748** | **16,080** | **(28,356)** | **83,637** |
| **Expenses** | | | | | |
| Social assistance and official development assistance | 22,593 | - | - | (13) | 22,580 |
| Personnel expenses | 6,011 | 10,724 | 2,811 | (10) | 19,536 |
| Other operating expenses | 42,828 | 21,991 | 11,185 | (27,006) | 48,998 |
| Interest expenses | 3,655 | 266 | 1,129 | (1,091) | 3,959 |
| Forecast for future new spending and top-down adjustment | (627) | - | - | - | (627) |
| **Total expenses (excluding losses)** | **74,460** | **32,981** | **15,125** | **(28,120)** | **94,446** |
| **Operating balance before gains/(losses)** | **(13,295)** | **1,767** | **955** | **(236)** | **(10,809)** |
| Total gains/(losses) | (798) | (1,397) | 113 | 14 | (2,068) |
| Net surplus/(deficit) from associates and joint ventures | 83 | 168 | 29 | (4) | 276 |
| Attributable to minority interest in Air NZ | - | - | - | - | - |
| **Operating balance** | **(14,010)** | **538** | **1,097** | **(226)** | **(12,601)** |
| **Expenses by functional classification** | | | | | |
| Social security and welfare | 22,560 | 4,101 | - | (614) | 26,047 |
| Health | 14,350 | 12,009 | - | (12,550) | 13,809 |
| Education | 12,269 | 9,421 | 23 | (8,661) | 13,052 |
| Transport and communications | 2,468 | 2,148 | 6,670 | (2,343) | 8,943 |
| Other | 19,785 | 5,036 | 7,303 | (2,861) | 29,263 |
| Finance costs | 3,655 | 266 | 1,129 | (1,091) | 3,959 |
| Forecast for future new spending and top-down adjustment | (627) | - | - | - | (627) |
| **Total Crown expenses (excluding losses)** | **74,460** | **32,981** | **15,125** | **(28,120)** | **94,446** |
| **Statement of Financial Position as at 30 June 2012** | | | | | |
| **Assets** | | | | | |
| Cash and cash equivalents | 6,193 | 2,291 | 850 | (149) | 9,185 |
| Receivables | 9,485 | 7,749 | 3,487 | (1,923) | 18,798 |
| Other financial assets | 54,832 | 25,861 | 16,452 | (14,024) | 83,121 |
| Property, plant and equipment | 30,121 | 50,148 | 38,798 | - | 119,067 |
| Equity accounted investments | 31,283 | 8,167 | 437 | (30,198) | 9,689 |
| Intangible assets and goodwill | 1,336 | 516 | 746 | (1) | 2,597 |
| Inventory and other assets | 1,643 | 344 | 1,317 | (38) | 3,266 |
| Forecast for new capital spending and top-down adjustment | (108) | - | - | - | (108) |
| **Total assets** | **134,785** | **95,076** | **62,087** | **(46,333)** | **245,615** |
| **Liabilities** | | | | | |
| Borrowings | 84,635 | 5,282 | 25,105 | (13,785) | 101,237 |
| Other liabilities | 29,247 | 44,934 | 8,937 | (7,022) | 76,096 |
| **Total liabilities** | **113,882** | **50,216** | **34,042** | **(20,807)** | **177,333** |
| **Total assets less total liabilities** | **20,903** | **44,860** | **28,045** | **(25,526)** | **68,282** |
| **Net worth** | | | | | |
| Taxpayer funds | 5,524 | 18,530 | 10,394 | (28,817) | 5,631 |
| Reserves | 15,379 | 26,330 | 17,308 | 3,326 | 62,343 |
| Net worth attributable to minority interest in Air NZ | - | - | 343 | (35) | 308 |
| **Total net worth** | **20,903** | **44,860** | **28,045** | **(25,526)** | **68,282** |

# Forecast Statement of Segments (continued)

| | Core Crown 2013 Forecast $m | Crown entities 2013 Forecast $m | State-owned enterprises 2013 Forecast $m | Inter-segment eliminations 2013 Forecast $m | Total Crown 2013 Forecast $m |
|---|---|---|---|---|---|
| **Statement of Financial Performance for the year ended 30 June 2013** | | | | | |
| **Revenue** | | | | | |
| Taxation revenue | 59,195 | - | - | (624) | 58,571 |
| Other sovereign revenue | 1,728 | 5,302 | - | (1,299) | 5,731 |
| Sales of goods and services | 1,434 | 14,790 | 14,627 | (13,537) | 17,314 |
| Interest revenue and dividends | 2,667 | 1,244 | 1,006 | (1,609) | 3,308 |
| Other revenue | 712 | 13,149 | 1,037 | (11,335) | 3,563 |
| **Total revenue (excluding gains)** | **65,736** | **34,485** | **16,670** | **(28,404)** | **88,487** |
| **Expenses** | | | | | |
| Social assistance and official development assistance | 23,217 | - | - | (42) | 23,175 |
| Personnel expenses | 5,956 | 10,924 | 2,903 | (10) | 19,773 |
| Other operating expenses | 37,856 | 22,082 | 11,481 | (26,700) | 44,719 |
| Interest expenses | 3,789 | 280 | 1,361 | (966) | 4,464 |
| Forecast for future new spending and top-down adjustment | 794 | - | - | - | 794 |
| **Total expenses (excluding losses)** | **71,612** | **33,286** | **15,745** | **(27,718)** | **92,925** |
| **Operating balance before gains/(losses)** | **(5,876)** | **1,199** | **925** | **(686)** | **(4,438)** |
| Total gains/(losses) | 1,474 | 266 | 226 | (187) | 1,779 |
| Net surplus/(deficit) from associates and joint ventures | 84 | 168 | 33 | (1) | 284 |
| Attributable to minority interest in Air NZ | - | - | - | - | - |
| **Operating balance** | **(4,318)** | **1,633** | **1,184** | **(874)** | **(2,375)** |
| **Expenses by functional classification** | | | | | |
| Social security and welfare | 23,252 | 4,590 | - | (660) | 27,182 |
| Health | 14,330 | 11,896 | - | (12,550) | 13,676 |
| Education | 12,205 | 9,488 | 23 | (8,729) | 12,987 |
| Transport and communications | 2,128 | 2,173 | 6,818 | (2,180) | 8,939 |
| Other | 15,114 | 4,859 | 7,543 | (2,633) | 24,883 |
| Finance costs | 3,789 | 280 | 1,361 | (966) | 4,464 |
| Forecast for future new spending and top-down adjustment | 794 | - | - | - | 794 |
| **Total Crown expenses (excluding losses)** | **71,612** | **33,286** | **15,745** | **(27,718)** | **92,925** |
| **Statement of Financial Position as at 30 June 2013** | | | | | |
| **Assets** | | | | | |
| Cash and cash equivalents | 6,093 | 2,432 | 886 | (150) | 9,261 |
| Receivables | 9,082 | 5,756 | 3,094 | (2,010) | 15,922 |
| Other financial assets | 47,763 | 27,400 | 17,867 | (14,271) | 78,759 |
| Property, plant and equipment | 30,198 | 51,487 | 40,233 | 1 | 121,919 |
| Equity accounted investments | 32,473 | 8,332 | 481 | (31,419) | 9,867 |
| Intangible assets and goodwill | 1,391 | 531 | 740 | - | 2,662 |
| Inventory and other assets | 1,652 | 345 | 1,420 | (39) | 3,378 |
| Forecast for new capital spending and top-down adjustment | 219 | - | - | - | 219 |
| **Total assets** | **128,871** | **96,283** | **64,721** | **(47,888)** | **241,987** |
| **Liabilities** | | | | | |
| Borrowings | 84,761 | 5,228 | 27,993 | (14,132) | 103,850 |
| Other liabilities | 27,513 | 43,564 | 8,325 | (7,204) | 72,198 |
| **Total liabilities** | **112,274** | **48,792** | **36,318** | **(21,336)** | **176,048** |
| **Total assets less total liabilities** | **16,597** | **47,491** | **28,403** | **(26,552)** | **65,939** |
| **Net worth** | | | | | |
| Taxpayer funds | 1,210 | 21,266 | 10,730 | (29,884) | 3,322 |
| Reserves | 15,387 | 26,225 | 17,330 | 3,367 | 62,309 |
| Net worth attributable to minority interest in Air NZ | - | - | 343 | (35) | 308 |
| **Total net worth** | **16,597** | **47,491** | **28,403** | **(26,552)** | **65,939** |

# Forecast Statement of Segments (continued)

| | Core Crown 2014 Forecast $m | Crown entities 2014 Forecast $m | State-owned enterprises 2014 Forecast $m | Inter-segment eliminations 2014 Forecast $m | Total Crown 2014 Forecast $m |
|---|---|---|---|---|---|
| **Statement of Financial Performance for the year ended 30 June 2014** | | | | | |
| **Revenue** | | | | | |
| Taxation revenue | 63,635 | - | - | (750) | 62,885 |
| Other sovereign revenue | 1,946 | 5,471 | - | (1,299) | 6,118 |
| Sales of goods and services | 1,444 | 15,191 | 15,657 | (13,866) | 18,426 |
| Interest revenue and dividends | 2,674 | 1,446 | 1,212 | (1,644) | 3,688 |
| Other revenue | 729 | 12,987 | 1,119 | (11,137) | 3,698 |
| **Total revenue (excluding gains)** | **70,428** | **35,095** | **17,988** | **(28,696)** | **94,815** |
| **Expenses** | | | | | |
| Social assistance and official development assistance | 23,727 | - | - | (41) | 23,686 |
| Personnel expenses | 5,979 | 11,005 | 2,993 | (10) | 19,967 |
| Other operating expenses | 37,605 | 22,578 | 12,276 | (26,943) | 45,516 |
| Interest expenses | 3,921 | 307 | 1,641 | (968) | 4,901 |
| Forecast for future new spending and top-down adjustment | 1,688 | - | - | - | 1,688 |
| **Total expenses (excluding losses)** | **72,920** | **33,890** | **16,910** | **(27,962)** | **95,758** |
| **Operating balance before gains/(losses)** | **(2,492)** | **1,205** | **1,078** | **(734)** | **(943)** |
| Total gains/(losses) | 1,954 | 184 | 282 | (195) | 2,225 |
| Net surplus/(deficit) from associates and joint ventures | 81 | 169 | 47 | (3) | 294 |
| Attributable to minority interest in Air NZ | - | - | - | - | - |
| **Operating balance** | **(457)** | **1,558** | **1,407** | **(932)** | **1,576** |
| **Expenses by functional classification** | | | | | |
| Social security and welfare | 23,829 | 4,902 | - | (677) | 28,054 |
| Health | 14,239 | 12,205 | - | (12,850) | 13,594 |
| Education | 12,099 | 9,449 | 23 | (8,614) | 12,957 |
| Transport and communications | 2,079 | 2,214 | 7,099 | (2,200) | 9,192 |
| Other | 15,065 | 4,813 | 8,147 | (2,653) | 25,372 |
| Finance costs | 3,921 | 307 | 1,641 | (968) | 4,901 |
| Forecast for future new spending and top-down adjustment | 1,688 | - | - | - | 1,688 |
| **Total Crown expenses (excluding losses)** | **72,920** | **33,890** | **16,910** | **(27,962)** | **95,758** |
| **Statement of Financial Position as at 30 June 2014** | | | | | |
| **Assets** | | | | | |
| Cash and cash equivalents | 6,312 | 2,693 | 1,152 | (148) | 10,009 |
| Receivables | 9,208 | 5,210 | 2,738 | (1,917) | 15,239 |
| Other financial assets | 53,675 | 27,842 | 19,582 | (14,013) | 87,086 |
| Property, plant and equipment | 30,082 | 52,485 | 41,607 | - | 124,174 |
| Equity accounted investments | 33,612 | 8,502 | 518 | (32,596) | 10,036 |
| Intangible assets and goodwill | 1,429 | 518 | 770 | - | 2,717 |
| Inventory and other assets | 1,644 | 346 | 1,456 | (40) | 3,406 |
| Forecast for new capital spending and top-down adjustment | 310 | - | - | - | 310 |
| **Total assets** | **136,272** | **97,596** | **67,823** | **(48,714)** | **252,977** |
| **Liabilities** | | | | | |
| Borrowings | 93,270 | 5,294 | 30,531 | (13,959) | 115,136 |
| Other liabilities | 26,849 | 42,282 | 8,291 | (7,107) | 70,315 |
| **Total liabilities** | **120,119** | **47,576** | **38,822** | **(21,066)** | **185,451** |
| **Total assets less total liabilities** | **16,153** | **50,020** | **29,001** | **(27,648)** | **67,526** |
| **Net worth** | | | | | |
| Taxpayer funds | 757 | 23,905 | 11,328 | (31,056) | 4,934 |
| Reserves | 15,396 | 26,115 | 17,330 | 3,443 | 62,284 |
| Net worth attributable to minority interest in Air NZ | - | - | 343 | (35) | 308 |
| **Total net worth** | **16,153** | **50,020** | **29,001** | **(27,648)** | **67,526** |

# Forecast Statement of Segments (continued)

| | Core Crown 2015 Forecast $m | Crown entities 2015 Forecast $m | State-owned enterprises 2015 Forecast $m | Inter-segment eliminations 2015 Forecast $m | Total Crown 2015 Forecast $m |
|---|---|---|---|---|---|
| **Statement of Financial Performance for the year ended 30 June 2015** | | | | | |
| **Revenue** | | | | | |
| Taxation revenue | 67,644 | - | - | (775) | 66,869 |
| Other sovereign revenue | 2,047 | 5,618 | - | (1,299) | 6,366 |
| Sales of goods and services | 1,431 | 15,246 | 16,367 | (13,880) | 19,164 |
| Interest revenue and dividends | 2,942 | 1,642 | 1,328 | (1,653) | 4,259 |
| Other revenue | 722 | 13,167 | 1,123 | (11,234) | 3,778 |
| **Total revenue (excluding gains)** | **74,786** | **35,673** | **18,818** | **(28,841)** | **100,436** |
| **Expenses** | | | | | |
| Social assistance and official development assistance | 24,584 | - | - | (44) | 24,540 |
| Personnel expenses | 6,040 | 11,120 | 3,069 | (10) | 20,219 |
| Other operating expenses | 37,814 | 22,591 | 12,715 | (27,114) | 46,006 |
| Interest expenses | 4,313 | 309 | 1,745 | (978) | 5,389 |
| Forecast for future new spending and top-down adjustment | 2,832 | - | - | - | 2,832 |
| **Total expenses (excluding losses)** | **75,583** | **34,020** | **17,529** | **(28,146)** | **98,986** |
| **Operating balance before gains/(losses)** | **(797)** | **1,653** | **1,289** | **(695)** | **1,450** |
| Total gains/(losses) | 1,983 | 176 | 280 | (201) | 2,238 |
| Net surplus/(deficit) from associates and joint ventures | 75 | 168 | 43 | - | 286 |
| Attributable to minority interest in Air NZ | - | - | - | - | - |
| **Operating balance** | **1,261** | **1,997** | **1,612** | **(896)** | **3,974** |
| **Expenses by functional classification** | | | | | |
| Social security and welfare | 24,471 | 5,184 | - | (694) | 28,961 |
| Health | 14,233 | 12,208 | - | (12,844) | 13,597 |
| Education | 12,227 | 9,604 | 23 | (8,738) | 13,116 |
| Transport and communications | 2,136 | 2,201 | 7,312 | (2,201) | 9,448 |
| Other | 15,371 | 4,514 | 8,449 | (2,691) | 25,643 |
| Finance costs | 4,313 | 309 | 1,745 | (978) | 5,389 |
| Forecast for future new spending and top-down adjustment | 2,832 | - | - | - | 2,832 |
| **Total Crown expenses (excluding losses)** | **75,583** | **34,020** | **17,529** | **(28,146)** | **98,986** |
| **Statement of Financial Position as at 30 June 2015** | | | | | |
| **Assets** | | | | | |
| Cash and cash equivalents | 6,739 | 2,374 | 1,046 | (149) | 10,010 |
| Receivables | 9,302 | 5,048 | 2,798 | (2,067) | 15,081 |
| Other financial assets | 51,206 | 30,508 | 21,814 | (15,110) | 88,418 |
| Property, plant and equipment | 29,986 | 53,521 | 42,622 | - | 126,129 |
| Equity accounted investments | 34,966 | 8,671 | 519 | (33,893) | 10,263 |
| Intangible assets and goodwill | 1,428 | 493 | 784 | - | 2,705 |
| Inventory and other assets | 1,657 | 345 | 1,484 | (40) | 3,446 |
| Forecast for new capital spending and top-down adjustment | 320 | - | - | - | 320 |
| **Total assets** | **135,604** | **100,960** | **71,067** | **(51,259)** | **256,372** |
| **Liabilities** | | | | | |
| Borrowings | 92,085 | 5,728 | 32,793 | (15,076) | 115,530 |
| Other liabilities | 26,087 | 42,111 | 8,436 | (7,306) | 69,328 |
| **Total liabilities** | **118,172** | **47,839** | **41,229** | **(22,382)** | **184,858** |
| **Total assets less total liabilities** | **17,432** | **53,121** | **29,838** | **(28,877)** | **71,514** |
| **Net worth** | | | | | |
| Taxpayer funds | 2,022 | 27,116 | 12,163 | (32,368) | 8,933 |
| Reserves | 15,410 | 26,005 | 17,332 | 3,526 | 62,273 |
| Net worth attributable to minority interest in Air NZ | - | - | 343 | (35) | 308 |
| **Total net worth** | **17,432** | **53,121** | **29,838** | **(28,877)** | **71,514** |

# Forecast Statement of Segments (continued)

| | Core Crown 2016 Forecast $m | Crown entities 2016 Forecast $m | State-owned enterprises 2016 Forecast $m | Inter-segment eliminations 2016 Forecast $m | Total Crown 2016 Forecast $m |
|---|---|---|---|---|---|
| **Statement of Financial Performance for the year ended 30 June 2016** | | | | | |
| **Revenue** | | | | | |
| Taxation revenue | 71,468 | - | - | (826) | 70,642 |
| Other sovereign revenue | 2,484 | 5,766 | - | (1,299) | 6,951 |
| Sales of goods and services | 1,426 | 14,876 | 17,123 | (13,484) | 19,941 |
| Interest revenue and dividends | 3,057 | 1,857 | 1,447 | (1,824) | 4,537 |
| Other revenue | 724 | 13,313 | 1,163 | (11,384) | 3,816 |
| **Total revenue (excluding gains)** | **79,159** | **35,812** | **19,733** | **(28,817)** | **105,887** |
| **Expenses** | | | | | |
| Social assistance and official development assistance | 25,633 | - | - | (42) | 25,591 |
| Personnel expenses | 6,084 | 11,241 | 3,175 | (10) | 20,490 |
| Other operating expenses | 38,113 | 22,923 | 13,282 | (26,905) | 47,413 |
| Interest expenses | 4,345 | 305 | 1,883 | (1,075) | 5,458 |
| Forecast for future new spending and top-down adjustment | 3,859 | - | - | - | 3,859 |
| **Total expenses (excluding losses)** | **78,034** | **34,469** | **18,340** | **(28,032)** | **102,811** |
| **Operating balance before gains/(losses)** | **1,125** | **1,343** | **1,393** | **(785)** | **3,076** |
| Total gains/(losses) | 2,030 | 209 | 285 | (207) | 2,317 |
| Net surplus/(deficit) from associates and joint ventures | 82 | 168 | 60 | (2) | 308 |
| Attributable to minority interest in Air NZ | - | - | - | - | - |
| **Operating balance** | **3,237** | **1,720** | **1,738** | **(994)** | **5,701** |
| **Expenses by functional classification** | | | | | |
| Social security and welfare | 25,536 | 5,509 | - | (710) | 30,335 |
| Health | 14,224 | 11,803 | - | (12,430) | 13,597 |
| Education | 12,420 | 9,780 | 23 | (8,887) | 13,336 |
| Transport and communications | 2,025 | 2,194 | 7,711 | (2,197) | 9,733 |
| Other | 15,625 | 4,878 | 8,723 | (2,733) | 26,493 |
| Finance costs | 4,345 | 305 | 1,883 | (1,075) | 5,458 |
| Forecast for future new spending and top-down adjustment | 3,859 | - | - | - | 3,859 |
| **Total Crown expenses (excluding losses)** | **78,034** | **34,469** | **18,340** | **(28,032)** | **102,811** |
| **Statement of Financial Position as at 30 June 2016** | | | | | |
| **Assets** | | | | | |
| Cash and cash equivalents | 6,920 | 2,506 | 1,149 | (152) | 10,423 |
| Receivables | 9,578 | 5,145 | 2,628 | (1,956) | 15,395 |
| Other financial assets | 54,786 | 33,853 | 23,959 | (16,404) | 96,194 |
| Property, plant and equipment | 30,191 | 54,729 | 43,478 | (1) | 128,397 |
| Equity accounted investments | 36,415 | 8,839 | 520 | (35,280) | 10,494 |
| Intangible assets and goodwill | 1,414 | 471 | 795 | - | 2,680 |
| Inventory and other assets | 1,678 | 346 | 1,473 | (40) | 3,457 |
| Forecast for new capital spending and top-down adjustment | 385 | - | - | - | 385 |
| **Total assets** | **141,367** | **105,889** | **74,002** | **(53,833)** | **267,425** |
| **Liabilities** | | | | | |
| Borrowings | 94,877 | 5,691 | 34,712 | (16,387) | 118,893 |
| Other liabilities | 25,811 | 44,157 | 8,573 | (7,238) | 71,303 |
| **Total liabilities** | **120,688** | **49,848** | **43,285** | **(23,625)** | **190,196** |
| **Total assets less total liabilities** | **20,679** | **56,041** | **30,717** | **(30,208)** | **77,229** |
| **Net worth** | | | | | |
| Taxpayer funds | 5,262 | 30,143 | 13,042 | (33,786) | 14,661 |
| Reserves | 15,417 | 25,898 | 17,332 | 3,613 | 62,260 |
| Net worth attributable to minority interest in Air NZ | - | - | 343 | (35) | 308 |
| **Total net worth** | **20,679** | **56,041** | **30,717** | **(30,208)** | **77,229** |

# 6

# Core Crown Expense Tables

| ($million) | 2007 Actual | 2008 Actual | 2009 Actual | 2010 Actual | 2011 Actual | 2012 Forecast | 2013 Forecast | 2014 Forecast | 2015 Forecast | 2016 Forecast |
|---|---|---|---|---|---|---|---|---|---|---|
| Social security and welfare | 16,768 | 17,877 | 19,382 | 21,185 | 22,005 | 22,560 | 23,252 | 23,829 | 24,471 | 25,536 |
| GSF pension expenses | 645 | 690 | 655 | 328 | 305 | 201 | 298 | 377 | 433 | 464 |
| Health | 10,355 | 11,297 | 12,368 | 13,128 | 13,753 | 14,350 | 14,330 | 14,239 | 14,233 | 14,224 |
| Education | 9,269 | 9,551 | 11,455 | 11,724 | 11,650 | 12,269 | 12,205 | 12,099 | 12,227 | 12,420 |
| Core government services | 4,816 | 3,371 | 5,293 | 2,974 | 5,563 | 7,138 | 4,390 | 4,474 | 4,450 | 4,368 |
| Law and order | 2,699 | 2,894 | 3,089 | 3,191 | 3,382 | 3,635 | 3,539 | 3,511 | 3,509 | 3,510 |
| Defence | 1,517 | 1,562 | 1,757 | 1,814 | 1,809 | 1,903 | 1,917 | 1,867 | 1,866 | 1,864 |
| Transport and communications | 2,405 | 2,244 | 2,663 | 2,345 | 2,281 | 2,468 | 2,128 | 2,079 | 2,136 | 2,025 |
| Economic and industrial services | 1,595 | 2,889 | 2,960 | 2,839 | 2,609 | 2,529 | 1,922 | 1,855 | 1,876 | 1,906 |
| Primary services | 438 | 541 | 534 | 507 | 706 | 783 | 705 | 688 | 686 | 663 |
| Heritage, culture and recreation | 844 | 1,107 | 1,002 | 1,281 | 1,966 | 2,490 | 1,542 | 1,494 | 1,738 | 2,084 |
| Housing and community development | 255 | 260 | 297 | 306 | 876 | 400 | 313 | 313 | 328 | 281 |
| Other | 68 | 254 | 118 | 80 | 479 | 706 | 488 | 486 | 485 | 485 |
| Finance costs | 2,329 | 2,460 | 2,429 | 2,311 | 3,066 | 3,655 | 3,789 | 3,921 | 4,313 | 4,345 |
| Forecast for future new spending | .. | .. | .. | .. | .. | 473 | 1,094 | 1,788 | 2,932 | 3,959 |
| Top-down expense adjustment | .. | .. | .. | .. | .. | ( 1,100) | ( 300) | ( 100) | ( 100) | ( 100) |
| **Core Crown expenses** | **54,003** | **56,997** | **64,002** | **64,013** | **70,450** | **74,460** | **71,612** | **72,920** | **75,583** | **78,034** |

Source: The Treasury

## ***Table 6.1*** – Social security and welfare expenses

| ($million) | 2007 Actual | 2008 Actual | 2009 Actual | 2010 Actual | 2011 Actual | 2012 Forecast | 2013 Forecast | 2014 Forecast | 2015 Forecast | 2016 Forecast |
|---|---|---|---|---|---|---|---|---|---|---|
| Welfare benefits | 15,435 | 16,288 | 17,366 | 18,961 | 19,781 | 20,456 | 21,198 | 21,764 | 22,588 | 23,610 |
| Social rehabilitation and compensation | 163 | 199 | 336 | 331 | 119 | 81 | 112 | 112 | 112 | 112 |
| Departmental expenses | 845 | 850 | 1,092 | 1,130 | 1,127 | 1,123 | 1,105 | 1,098 | 1,100 | 1,093 |
| Child support impairment | 183 | 193 | 205 | 371 | 281 | 421 | 505 | 525 | 339 | 390 |
| Other non-departmental expenses[1] | 142 | 347 | 383 | 392 | 697 | 479 | 332 | 330 | 332 | 331 |
| **Social security and welfare expenses** | **16,768** | **17,877** | **19,382** | **21,185** | **22,005** | **22,560** | **23,252** | **23,829** | **24,471** | **25,536** |

Note 1: Other non-departmental expenses in the 2011 forecast include costs associated with the Canterbury earthquakes.

Source: The Treasury

## *Table 6.2* – New Zealand Superannuation and welfare benefit expenses

| ($million) | 2007 Actual | 2008 Actual | 2009 Actual | 2010 Actual | 2011 Actual | 2012 Forecast | 2013 Forecast | 2014 Forecast | 2015 Forecast | 2016 Forecast |
|---|---|---|---|---|---|---|---|---|---|---|
| New Zealand Superannuation | 6,810 | 7,348 | 7,744 | 8,290 | 8,830 | 9,597 | 10,235 | 10,824 | 11,590 | 12,449 |
| Domestic Purposes Benefit | 1,468 | 1,478 | 1,530 | 1,693 | 1,757 | 1,840 | 1,909 | 1,958 | 2,014 | 2,073 |
| Unemployment Benefit | 613 | 458 | 586 | 930 | 943 | 860 | 825 | 752 | 694 | 665 |
| Invalid's Benefit | 1,132 | 1,216 | 1,260 | 1,303 | 1,306 | 1,327 | 1,340 | 1,351 | 1,372 | 1,401 |
| Family Tax Credit | 1,699 | 1,897 | 2,062 | 2,168 | 2,139 | 2,131 | 2,125 | 2,075 | 2,038 | 2,054 |
| Accommodation Supplement | 877 | 891 | 989 | 1,154 | 1,197 | 1,199 | 1,218 | 1,232 | 1,247 | 1,276 |
| Sickness Benefit | 573 | 582 | 613 | 710 | 743 | 770 | 797 | 819 | 847 | 879 |
| Disability Allowance | 270 | 278 | 390 | 411 | 409 | 403 | 394 | 398 | 403 | 411 |
| Income-Related Rents | 434 | 465 | 512 | 522 | 553 | 587 | 623 | 663 | 705 | 705 |
| In Work Tax Credit | 461 | 563 | 584 | 595 | 585 | 564 | 558 | 528 | 503 | 499 |
| Child Tax Credit | 44 | 11 | 6 | 4 | 3 | 2 | 2 | 1 | 1 | 1 |
| Special Benefit | 106 | 71 | .. | .. | .. | .. | .. | .. | .. | .. |
| Benefits paid in Australia | 71 | 58 | 50 | 45 | 40 | 37 | 22 | 19 | 16 | 13 |
| Paid Parental Leave | 122 | 135 | 143 | 154 | 154 | 162 | 171 | 180 | 191 | 211 |
| Childcare Assistance | 139 | 150 | 159 | 178 | 188 | 183 | 181 | 178 | 182 | 189 |
| War Disablement Pensions | 122 | 134 | 125 | 137 | 135 | 133 | 130 | 125 | 122 | 117 |
| Veteran's Pension | 143 | 161 | 176 | 179 | 178 | 177 | 174 | 170 | 168 | 166 |
| Other benefits | 351 | 392 | 437 | 488 | 621 | 484 | 494 | 491 | 495 | 501 |
| **Benefit expenses** | **15,435** | **16,288** | **17,366** | **18,961** | **19,781** | **20,456** | **21,198** | **21,764** | **22,588** | **23,610** |

Source: The Treasury

## *Table 6.3* – Beneficiary numbers

| (Thousands) | 2007 Actual | 2008 Actual | 2009 Actual | 2010 Actual | 2011 Actual | 2012 Forecast | 2013 Forecast | 2014 Forecast | 2015 Forecast | 2016 Forecast |
|---|---|---|---|---|---|---|---|---|---|---|
| New Zealand Superannuation | 495 | 508 | 522 | 540 | 561 | 584 | 608 | 630 | 652 | 673 |
| Domestic Purposes Benefit | 100 | 97 | 101 | 110 | 114 | 115 | 116 | 117 | 117 | 117 |
| Unemployment Benefit | 52 | 37 | 48 | 78 | 80 | 70 | 66 | 58 | 52 | 48 |
| Accommodation Supplement | 251 | 245 | 267 | 312 | 320 | 312 | 312 | 310 | 308 | 308 |
| Invalid's Benefit | 78 | 82 | 86 | 88 | 88 | 87 | 87 | 86 | 85 | 85 |
| Sickness Benefit | 48 | 48 | 50 | 58 | 60 | 60 | 61 | 62 | 62 | 63 |

Source: Ministry of Social Development

## *Table 6.4* – Health expenses

| ($million) | 2007 Actual | 2008 Actual | 2009 Actual | 2010 Actual | 2011 Actual | 2012 Forecast | 2013 Forecast | 2014 Forecast | 2015 Forecast | 2016 Forecast |
|---|---|---|---|---|---|---|---|---|---|---|
| Departmental outputs | 180 | 206 | 206 | 211 | 199 | 202 | 201 | 201 | 201 | 201 |
| Health services purchasing | 9,614 | 10,503 | 11,354 | 12,077 | 12,530 | 13,224 | 13,159 | 13,083 | 13,086 | 13,086 |
| Other non-departmental outputs | 99 | 97 | 98 | 106 | 120 | 121 | 117 | 111 | 111 | 111 |
| Health payments to ACC | 425 | 463 | 667 | 691 | 849 | 752 | 804 | 795 | 786 | 778 |
| Other expenses | 37 | 28 | 43 | 43 | 55 | 51 | 49 | 49 | 49 | 48 |
| **Health expenses** | **10,355** | **11,297** | **12,368** | **13,128** | **13,753** | **14,350** | **14,330** | **14,239** | **14,233** | **14,224** |

Source: The Treasury

## *Table 6.5* – Health services purchasing

| ($million) | 2007 Actual | 2008 Actual | 2009 Actual | 2010 Actual | 2011 Actual | 2012 Forecast | 2013 Forecast | 2014 Forecast | 2015 Forecast | 2016 Forecast |
|---|---|---|---|---|---|---|---|---|---|---|
| Payments to District Health Boards | 8,547 | 9,312 | 10,038 | 10,670 | 11,133 | 11,703 | 11,659 | 11,644 | 11,659 | 11,659 |
| National disability support services | 755 | 834 | 889 | 930 | 971 | 1,035 | 1,020 | 1,020 | 1,019 | 1,019 |
| Public health services purchasing | 312 | 357 | 427 | 477 | 426 | 486 | 480 | 419 | 408 | 408 |
| **Health services purchasing** | **9,614** | **10,503** | **11,354** | **12,077** | **12,530** | **13,224** | **13,159** | **13,083** | **13,086** | **13,086** |

Source: The Treasury

## *Table 6.6* – Education expenses

| ($million) | 2007 Actual | 2008 Actual | 2009 Actual | 2010 Actual | 2011 Actual | 2012 Forecast | 2013 Forecast | 2014 Forecast | 2015 Forecast | 2016 Forecast |
|---|---|---|---|---|---|---|---|---|---|---|
| Early childhood education | 617 | 860 | 1,030 | 1,184 | 1,340 | 1,353 | 1,414 | 1,469 | 1,521 | 1,575 |
| Primary and secondary schools | 4,325 | 4,552 | 4,936 | 5,157 | 5,354 | 5,521 | 5,608 | 5,499 | 5,602 | 5,735 |
| Tertiary funding | 3,322 | 3,266 | 4,564 | 4,465 | 3,991 | 4,273 | 4,191 | 4,145 | 4,127 | 4,133 |
| Departmental expenses | 875 | 828 | 888 | 898 | 923 | 1,047 | 981 | 977 | 969 | 969 |
| Other education expenses | 130 | 45 | 37 | 20 | 42 | 75 | 11 | 9 | 8 | 8 |
| **Education expenses** | **9,269** | **9,551** | **11,455** | **11,724** | **11,650** | **12,269** | **12,205** | **12,099** | **12,227** | **12,420** |

| Places | 2007 Actual | 2008 Actual | 2009 Actual | 2010 Actual | 2011 Actual | 2012 Forecast | 2013 Forecast | 2014 Forecast | 2015 Forecast | 2016 Forecast |
|---|---|---|---|---|---|---|---|---|---|---|
| Early childhood education[1] | 123,196 | 133,863 | 142,014 | 155,108 | 159,995 | 166,807 | 172,895 | 179,823 | 185,638 | 192,135 |

Note 1: Full-time equivalent based on 1,000 funded child hours per year based as at 1 July.

Sources: Ministry of Education, The Treasury

## *Table 6.7* – Primary and secondary education expenses

| ($million) | 2007 Actual | 2008 Actual | 2009 Actual | 2010 Actual | 2011 Actual | 2012 Forecast | 2013 Forecast | 2014 Forecast | 2015 Forecast | 2016 Forecast |
|---|---|---|---|---|---|---|---|---|---|---|
| Primary | 2,141 | 2,262 | 2,484 | 2,622 | 2,731 | 2,815 | 2,870 | 2,821 | 2,892 | 2,974 |
| Secondary | 1,682 | 1,761 | 1,898 | 1,972 | 2,051 | 2,121 | 2,142 | 2,083 | 2,104 | 2,143 |
| School transport | 125 | 131 | 152 | 160 | 163 | 173 | 178 | 186 | 193 | 199 |
| Special needs support | 263 | 278 | 290 | 297 | 310 | 316 | 320 | 313 | 316 | 322 |
| Professional development | 104 | 108 | 101 | 95 | 90 | 87 | 88 | 87 | 87 | 87 |
| Schooling improvement | 10 | 12 | 11 | 11 | 9 | 9 | 10 | 9 | 10 | 10 |
| **Primary and secondary education expenses** | **4,325** | **4,552** | **4,936** | **5,157** | **5,354** | **5,521** | **5,608** | **5,499** | **5,602** | **5,735** |

| Places | 2007 Actual | 2008 Actual | 2009 Actual | 2010 Actual | 2011 Actual | 2012 Forecast | 2013 Forecast | 2014 Forecast | 2015 Forecast | 2016 Forecast |
|---|---|---|---|---|---|---|---|---|---|---|
| Primary[1] | 479,230 | 475,820 | 474,630 | 473,431 | 474,149 | 480,477 | 485,321 | 491,068 | 499,160 | 505,442 |
| Secondary[1] | 277,619 | 277,582 | 280,062 | 281,095 | 281,999 | 279,588 | 278,831 | 277,599 | 276,550 | 275,310 |

Note1: These are snapshots based as at 1 July for primary year levels (years 1 to 8) and 1 March for secondary year levels (years 9 to 13). These numbers include special school rolls but exclude health camps, hospital schools and home schooling.

Sources: Ministry of Education, The Treasury

## *Table 6.8* – Tertiary education expenses

| ($million) | 2007 Actual | 2008 Actual | 2009 Actual | 2010 Actual | 2011 Actual | 2012 Forecast | 2013 Forecast | 2014 Forecast | 2015 Forecast | 2016 Forecast |
|---|---|---|---|---|---|---|---|---|---|---|
| Tuition | 1,962 | 2,172 | 2,287 | 2,398 | 2,354 | 2,370 | 2,381 | 2,367 | 2,372 | 2,373 |
| Other tertiary funding | 339 | 452 | 522 | 489 | 429 | 461 | 441 | 443 | 441 | 441 |
| Tertiary student allowances | 382 | 386 | 444 | 570 | 620 | 634 | 580 | 532 | 511 | 507 |
| Initial fair value change in student loans | .. | .. | .. | .. | .. | .. | .. | .. | .. | .. |
| Student loans | 639 | 256 | 1,311 | 1,008 | 588 | 808 | 789 | 803 | 803 | 812 |
| **Tertiary education expenses** | **3,322** | **3,266** | **4,564** | **4,465** | **3,991** | **4,273** | **4,191** | **4,145** | **4,127** | **4,133** |

| Places (year) | 2007 | 2008 | 2009 | 2010 | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 |
|---|---|---|---|---|---|---|---|---|---|---|
| Estimated funded places[1] | 225,652 | 225,836 | 234,230 | 239,978 | 238,721 | 244,339 | 242,533 | 242,633 | 242,687 | 242,723 |
| Actual delivered places[1] | 230,319 | 229,224 | 246,041 | 250,440 | | | | | | |

Note 1: Tertiary places are the number of equivalent full time (EFT) students in: student achievement component; adult and community education; and youth guarantee programmes. Note that historical place numbers have been revised so will differ from previous published EFU numbers. Place numbers are based on calendar years rather than fiscal years.

Sources: Ministry of Education, The Treasury

## *Table 6.9* – Core government service expenses

| ($million) | 2007 Actual | 2008 Actual | 2009 Actual | 2010 Actual | 2011 Actual | 2012 Forecast | 2013 Forecast | 2014 Forecast | 2015 Forecast | 2016 Forecast |
|---|---|---|---|---|---|---|---|---|---|---|
| Official development assistance | 330 | 362 | 458 | 435 | 495 | 544 | 513 | 534 | 559 | 559 |
| Indemnity and guarantee expenses | .. | .. | 992 | 7 | 319 | 29 | 37 | 43 | 48 | 48 |
| Departmental expenses | 1,402 | 1,557 | 1,668 | 1,324 | 1,492 | 1,648 | 1,673 | 1,622 | 1,605 | 1,589 |
| Non-departmental expenses | 237 | 277 | 117 | 236 | 471 | 589 | 548 | 582 | 602 | 615 |
| Tax receivable write-down and impairments | 2,479 | 701 | 1,654 | 590 | 1,010 | 1,104 | 1,068 | 1,112 | 1,157 | 1,157 |
| Science expenses | 163 | 168 | 179 | 191 | 174 | 121 | 120 | 121 | 124 | 124 |
| Other expenses[1] | 205 | 306 | 225 | 191 | 1,602 | 3,103 | 431 | 460 | 355 | 276 |
| **Core government service expenses** | **4,816** | **3,371** | **5,293** | **2,974** | **5,563** | **7,138** | **4,390** | **4,474** | **4,450** | **4,368** |

Note 1: Other expenses in the forecast period include costs associated with the Canterbury earthquakes.

Source: The Treasury

## *Table 6.10* – Law and order expenses

| ($million) | 2007 Actual | 2008 Actual | 2009 Actual | 2010 Actual | 2011 Actual | 2012 Forecast | 2013 Forecast | 2014 Forecast | 2015 Forecast | 2016 Forecast |
|---|---|---|---|---|---|---|---|---|---|---|
| Police | 1,086 | 1,198 | 1,326 | 1,349 | 1,393 | 1,406 | 1,401 | 1,395 | 1,397 | 1,398 |
| Ministry of Justice | 454 | 367 | 379 | 372 | 397 | 470 | 462 | 455 | 457 | 457 |
| Department of Corrections | 662 | 787 | 829 | 903 | 956 | 1,033 | 1,014 | 1,014 | 1,014 | 1,014 |
| NZ Customs Service[1] | 12 | 12 | 12 | 13 | 120 | 138 | 147 | 148 | 148 | 148 |
| Other departments | 48 | 79 | 80 | 102 | 237 | 101 | 73 | 75 | 72 | 72 |
| **Department expenses** | **2,262** | **2,443** | **2,626** | **2,739** | **3,103** | **3,148** | **3,097** | **3,087** | **3,088** | **3,089** |
| Non-departmental outputs | 354 | 326 | 380 | 399 | 261 | 399 | 367 | 358 | 362 | 362 |
| Other expenses | 83 | 125 | 83 | 53 | 18 | 88 | 75 | 66 | 59 | 59 |
| **Law and order expenses** | **2,699** | **2,894** | **3,089** | **3,191** | **3,382** | **3,635** | **3,539** | **3,511** | **3,509** | **3,510** |

Note1: Previously the majority of NZ Customs Service expenses were classified as core government services.

Source: The Treasury

## *Table 6.11* – Defence expenses

| ($million) | 2007 Actual | 2008 Actual | 2009 Actual | 2010 Actual | 2011 Actual | 2012 Forecast | 2013 Forecast | 2014 Forecast | 2015 Forecast | 2016 Forecast |
|---|---|---|---|---|---|---|---|---|---|---|
| NZDF core expenses | 1,459 | 1,517 | 1,697 | 1,747 | 1,736 | 1,808 | 1,868 | 1,818 | 1,817 | 1,809 |
| Other expenses | 58 | 45 | 60 | 67 | 73 | 95 | 49 | 49 | 49 | 55 |
| **Defence expenses** | **1,517** | **1,562** | **1,757** | **1,814** | **1,809** | **1,903** | **1,917** | **1,867** | **1,866** | **1,864** |

Source: The Treasury

## *Table 6.12* – Transport and communication expenses

| ($million) | 2007 Actual | 2008 Actual | 2009 Actual | 2010 Actual | 2011 Actual | 2012 Forecast | 2013 Forecast | 2014 Forecast | 2015 Forecast | 2016 Forecast |
|---|---|---|---|---|---|---|---|---|---|---|
| New Zealand Transport Agency[1] | 1,874 | 1,966 | 1,562 | 1,778 | 1,696 | 1,799 | 1,767 | 1,817 | 1,822 | 1,827 |
| Departmental outputs | 113 | 137 | 83 | 63 | 65 | 67 | 65 | 65 | 65 | 65 |
| Other non-departmental expenses | 221 | 104 | 170 | 58 | 105 | 233 | 188 | 137 | 131 | 104 |
| Asset impairments | 47 | .. | 320 | .. | .. | .. | .. | .. | .. | .. |
| Rail funding | 142 | 24 | 507 | 418 | 386 | 338 | 83 | 36 | 93 | 3 |
| Other expenses | 8 | 13 | 21 | 28 | 29 | 31 | 25 | 24 | 25 | 26 |
| **Transport and communication expenses** | **2,405** | **2,244** | **2,663** | **2,345** | **2,281** | **2,468** | **2,128** | **2,079** | **2,136** | **2,025** |

Note 1: Since 2008/09 funding has been provided to New Zealand Transport Agency (NZTA). From 2004/05 to 2007/08 funding was provided to Land Transport NZ. Prior to 2008/09, all NZTA funding was recognised as operating expenditure. However, from 2008/09 some funding is now classified as capital, resulting in a reduction to operating expenditure.

Source: The Treasury

## *Table 6.13* – Economic and industrial services expenses

| ($ million) | 2007 Actual | 2008 Actual | 2009 Actual | 2010 Actual | 2011 Actual | 2012 Forecast | 2013 Forecast | 2014 Forecast | 2015 Forecast | 2016 Forecast |
|---|---|---|---|---|---|---|---|---|---|---|
| Departmental outputs | 546 | 603 | 389 | 382 | 420 | 436 | 413 | 417 | 415 | 415 |
| Employment initiatives | 207 | 186 | 185 | 220 | 214 | 230 | 197 | 198 | 198 | 198 |
| Non-departmental outputs | 873 | 822 | 809 | 927 | 756 | 808 | 596 | 553 | 545 | 544 |
| Reserve electricity generation | 16 | 81 | 20 | 23 | 9 | 113 | .. | .. | .. | .. |
| KiwiSaver | .. | 1,102 | 1,281 | 1,024 | 1,042 | 685 | 634 | 603 | 638 | 670 |
| Research and development tax credits | .. | 37 | 154 | .. | .. | .. | .. | .. | .. | .. |
| Other expenses | (47) | 58 | 122 | 263 | 168 | 257 | 82 | 84 | 80 | 79 |
| **Economic and industrial services expenses** | **1,595** | **2,889** | **2,960** | **2,839** | **2,609** | **2,529** | **1,922** | **1,855** | **1,876** | **1,906** |

Source: The Treasury

## *Table 6.14* – Employment initiatives

| ($ million) | 2007 Actual | 2008 Actual | 2009 Actual | 2010 Actual | 2011 Actual | 2012 Forecast | 2013 Forecast | 2014 Forecast | 2015 Forecast | 2016 Forecast |
|---|---|---|---|---|---|---|---|---|---|---|
| Training incentive allowance | 29 | 27 | 30 | 19 | 11 | 16 | 14 | 15 | 15 | 15 |
| Subsidised work | 88 | 67 | 63 | 109 | 112 | 122 | 90 | 90 | 90 | 90 |
| Employment support for the disabled | 86 | 88 | 88 | 88 | 87 | 88 | 89 | 89 | 89 | 89 |
| Other employment assistance schemes | 4 | 4 | 4 | 4 | 4 | 4 | 4 | 4 | 4 | 4 |
| **Employment initiatives** | **207** | **186** | **185** | **220** | **214** | **230** | **197** | **198** | **198** | **198** |

Source: The Treasury

## *Table 6.15* – Primary service expenses

| ($ million) | 2007 Actual | 2008 Actual | 2009 Actual | 2010 Actual | 2011 Actual | 2012 Forecast | 2013 Forecast | 2014 Forecast | 2015 Forecast | 2016 Forecast |
|---|---|---|---|---|---|---|---|---|---|---|
| Departmental expenses | 342 | 354 | 360 | 352 | 354 | 394 | 372 | 370 | 372 | 375 |
| Non-departmental outputs | 80 | 109 | 89 | 136 | 160 | 223 | 197 | 182 | 176 | 149 |
| Biological research[1] | .. | .. | .. | .. | 167 | 105 | 106 | 102 | 102 | 102 |
| Other expenses | 16 | 78 | 85 | 19 | 25 | 61 | 30 | 34 | 36 | 37 |
| **Primary service expenses** | **438** | **541** | **534** | **507** | **706** | **783** | **705** | **688** | **686** | **663** |

[1] Biological research was previously classified as an economic and industrial services expense.

Source: The Treasury

## *Table 6.16* – Heritage, culture and recreation expenses

| ($ million) | 2007 Actual | 2008 Actual | 2009 Actual | 2010 Actual | 2011 Actual | 2012 Forecast | 2013 Forecast | 2014 Forecast | 2015 Forecast | 2016 Forecast |
|---|---|---|---|---|---|---|---|---|---|---|
| Community grants | 7 | 7 | 8 | 8 | 8 | 7 | 7 | 7 | 7 | 7 |
| Emissions Trading Scheme | .. | .. | 17 | 80 | 860 | 1,178 | 380 | 395 | 656 | 988 |
| Departmental outputs | 357 | 392 | 426 | 415 | 433 | 556 | 511 | 504 | 490 | 490 |
| Non-departmental outputs | 411 | 469 | 467 | 637 | 481 | 516 | 503 | 489 | 491 | 494 |
| Other expenses | 69 | 239 | 84 | 141 | 184 | 233 | 141 | 99 | 94 | 105 |
| **Heritage, culture and recreation expenses** | **844** | **1,107** | **1,002** | **1,281** | **1,966** | **2,490** | **1,542** | **1,494** | **1,738** | **2,084** |

Source: The Treasury

## *Table 6.17* – Housing and community development expenses

| ($ million) | 2007 Actual | 2008 Actual | 2009 Actual | 2010 Actual | 2011 Actual | 2012 Forecast | 2013 Forecast | 2014 Forecast | 2015 Forecast | 2016 Forecast |
|---|---|---|---|---|---|---|---|---|---|---|
| Housing subsidies | 25 | 28 | 37 | 44 | 68 | 67 | 58 | 51 | 55 | 43 |
| Departmental outputs | 134 | 141 | 148 | 140 | 136 | 137 | 129 | 140 | 148 | 110 |
| Other non-departmental expenses | 96 | 91 | 112 | 122 | 672 | 196 | 126 | 122 | 125 | 128 |
| **Housing and community development expenses** | **255** | **260** | **297** | **306** | **876** | **400** | **313** | **313** | **328** | **281** |

Source: The Treasury

# Glossary of Terms

### *ACC insurance liability*

The gross obligation for the future cost of ACC claims incurred prior to balance date. The net ACC liability is the gross liability less the asset reserves held to meet these claims.

### *Baselines*

The level of funding approved for any given spending area (eg, Vote Education). All amounts within baselines are included in the forecasts.

### *Consumer Price Index (CPI)*

Statistics New Zealand's official index to measure the rate of change in prices of goods and services purchased by households.

### *Contingent assets*

Potential assets dependent on an uncertain event occurring.

### *Contingent liability*

Costs that the Crown will have to face if a particular uncertain event occurs, or present liabilities that are unable to be measured with sufficient reliability to be recorded in the financial statements (unquantified contingent liabilities). They typically comprise guarantees and indemnities, legal disputes and claims, and uncalled capital.

### *Core Crown*

A reporting segment consisting of the Crown, departments, Offices of Parliament, the Reserve Bank and the NZS Fund. For a list of all entities included in this segment, refer to the Government Reporting Entity.

### *Core Crown expenses*

The day-to-day spending (eg, public servants' salaries, welfare benefit payments, finance costs and maintaining national defence etc) that does not build physical assets for the Crown. This is an accrual measure of expenses and includes items such as depreciation on physical assets.

### *Core Crown revenue*

Consists primarily of tax revenue collected by the Government but also includes investment income, sales of goods and services and other revenue.

### *Corporate tax*

The sum of net company tax, non-resident withholding tax (NRWT) and foreign-source dividend withholding payments (FDWP).

### *Current account (Balance of Payments)*

A measure of the flows of income between New Zealand and the rest of the world. A net inflow to New Zealand represents a current account surplus, a net outflow a deficit. The current account balance is commonly expressed as a percentage of GDP.

### *Cyclically adjusted or structural fiscal balance*

An estimate of the fiscal balance (eg, operating balance before gains and losses) adjusted for short-term fluctuations of actual GDP around trend GDP. The estimate provides a picture of the underlying trend fiscal position and helps measure the effects of policy decisions. Because it is based on a number of assumptions and is sensitive to new information, the estimate is subject to some uncertainty.

### *Demographic changes*

Changes to the structure of the population such as the age, gender or ethnic make-up.

### *Domestic bond programme*

The amount and timing of additional government bonds expected to be issued or redeemed in the next financial year.

### *Excise duties*

A tax levied on the domestic production of alcohol, tobacco and light petroleum products (CNG, LPG and petrol).

### *Financial assets*

Any asset that is cash, an equity instrument of another entity (shares), a contractual right to receive cash or shares, or a right to exchange a financial asset or liability on favourable terms.

### *Fiscal impulse*

A summary measure of how changes in fiscal policy affect aggregate demand. To isolate discretionary changes, fiscal impulse is calculated on a cyclically-adjusted basis and excludes net interest payments. To better capture the role of capital spending the indicator is derived from cash flow information.

### *Fiscal intentions (short-term)*

Indications of the Government's intentions for operating expenses, operating revenues, and the impact of its intentions on the operating balance, debt and net worth over (at least) the next three years. These intentions are required under the Public Finance Act 1989 (PFA).

### *Fiscal objectives (long-term)*

The Government's long-term goals for operating expenses, operating revenue, the operating balance, debt and net worth, as required by the PFA. The objectives must be consistent with the defined principles of responsible fiscal management as outlined in the PFA and must cover a period of (at least) 10 years.

### *Forecast new capital spending*

An amount provided in the forecasts to represent the balance sheet impact of capital initiatives expected to be introduced over the forecast period.

### *Forecast new operating spending*

An amount included in the forecasts to provide for the operating balance impact of policy initiatives, changes to demographics, and other forecasting changes expected to occur over the forecast period.

### *Gains and Losses*

Gains and losses typically arise from the revaluation of assets and liabilities, such as investments in financial assets and long-term liabilities for ACC and the Government Superannuation Fund. These valuation changes are reported directly as a movement in net worth (eg, asset revaluation reserves) or indirectly through the Statement of Financial Performance. The impact of gains and losses on the operating balance can be volatile, therefore the operating balance (before gains and losses) indicator can provide a more useful measure of underlying stewardship.

### *GDP deflator*

An index of changes in the general price level in the economy. It is calculated as the ratio of nominal GDP to real GDP.

### *Gross domestic product (GDP)*

A measure of the value of all goods and services produced in New Zealand. Changes in GDP measure growth or contraction in economic activity or output. GDP can be measured as the actual dollar value of goods and services at today's prices (nominal GDP), or excluding the effects of price changes over time (real GDP).

### *Gross domestic product (expenditure)*

The sum of total final expenditure on goods and services in the economy.

### *Gross national expenditure (GNE)*

A measure of total expenditure on final goods and services by New Zealand residents.

### *Gross sovereign-issued debt (GSID)*

Includes all debt issued by the sovereign (the core Crown). It therefore includes Government stock held within the Crown (eg, by the NZS Fund, ACC and EQC).

### *Labour force participation rate*

Measures the percentage of the working-age population in work or actively looking for and available for work.

### *Labour productivity*

Measures output per unit of labour input (where labour inputs might be measured as hours worked or the number of people employed).

### *Line-by-line consolidation*

A term used to refer to the general approach to the presentation of the Crown financial statements. It means that the individual line items for revenues, expenses, assets and liabilities in the Crown financial statements include all departments, Offices of Parliament, the Reserve Bank, SOEs, Crown entities and other entities controlled by the Government.

### *Marketable securities*

Assets held with financial institutions. These assets are held for both cash flow and investment purposes, and include any funds the Government has invested in the International Monetary Fund.

### *Monetary conditions*

Aggregate monetary conditions measure the degree to which short-term interest rates and the exchange rate either support or restrict economic growth.

### *Monetary policy*

The Reserve Bank implements its monetary policy decisions by adjusting its Official Cash Rate (OCR) in an effort to maintain stability in general level of prices within a defined annual CPI target range.

Tightening monetary policy means raising the OCR in order to moderate aggregate demand pressures and reduce inflationary pressures. Easing monetary policy has the reverse effect.

### *Net core Crown cash flow from operations*

Operating balance (before gains and losses) less retained items (eg, net surplus of SOEs, Crown entities and NZS Fund net revenue) less non-cash items (eg, depreciation).

### *Net core Crown debt*

Represents GSID less core Crown financial assets (excluding advances and financial assets held by the NZS Fund). Advances and financial assets held by the NZS Fund are excluded as these assets are less liquid and/or they are made for public policy reasons rather than for the purposes associated with government financing. Net core Crown debt provides information about the sustainability of the Government's accounts, and is used by some international rating agencies when determining the creditworthiness of a country.

### *Net international investment position (NIIP)*

Measures the net value of New Zealand's international assets and liabilities at a point in time.

### *Net worth*

Total assets less total liabilities (also referred to as the Crown balance). The change in net worth in any given forecast year is largely driven by the operating balance.

### *New Zealand equivalents to International Financial Reporting Standards (NZ IFRS)*

The reporting and measurement framework under which these forecast financial statements are prepared. These standards are approved by the External Reporting Board in New Zealand, based on requirements of the international financial reporting standards issued by the International Accounting Standards Board, adjusted where appropriate for entities that are not profit-oriented.

### *Operating balance*

The residual of revenues less expenses plus surpluses from SOEs and Crown entities. It includes gains and losses not reported directly as a movement against net worth.

### *Operating balance before gains and losses*

The impact of gains and losses on the operating balance can be volatile so the operating balance before gains and losses can provide a more useful measure of underlying stewardship.

### *Output gap*

The difference between actual and potential GDP. Potential GDP is the level of output an economy can sustain without acceleration of inflation.

### *Productivity*

The amount of output (eg, GDP) per unit of input.

***Projections***

Projections of the key fiscal indicators beyond the five-year forecast period. The projections are based on long-run economic and fiscal assumptions. For example, the projections assume no economic cycle and constant long-run interest, inflation and unemployment rates.

***Residual cash***

The level of money the Government has available to repay debt or, alternatively, needs to borrow in any given year. Residual cash is alternatively termed “Cash available/(shortfall to be funded)”.

Residual cash is equal to net core Crown cash flow from operations excluding NZS Fund activity less core Crown capital commitments (eg, contributions to NZS Fund, purchase of assets, loans to others).

***Settlement cash***

This is the amount of money deposited with the Reserve Bank by registered banks. It is a liquidity mechanism used to settle wholesale obligations between registered banks and provides the basis for settling most of the retail banking transactions that occur every working day between businesses and individuals.

***Specific fiscal risks***

A category of government decisions or circumstances which may have a material impact on the fiscal position. They are not included in the main forecasts because their fiscal impact cannot be reasonably quantified, the likelihood of realisation is uncertain and/or the timing is uncertain.

***System of National Accounts (SNA)***

SNA is a comprehensive, consistent and flexible set of macroeconomic accounts which meets the needs of government and private sector analysts, policy-makers and decision-takers.

***Tax revenue***

The accrual, rather than the cash (“tax receipts”) measure of taxation. It is a measure of tax due at a given point in time, regardless of whether or not it has actually been paid.

***Top-down adjustment***

An adjustment to expenditure forecasts to reflect the extent to which departments use appropriations (upper spending limits) when preparing their forecasts. As appropriations apply to the core Crown only, no adjustment is required to SOEs or Crown entity forecasts.

***Total borrowings***

Represents the Government’s total debt obligations to external parties and can be split into sovereign-guaranteed debt and non-sovereign-guaranteed debt. Non-sovereign-guaranteed debt represents the debt obligations of SOEs and Crown entities that are not explicitly guaranteed by the Crown.

***Tradable/non-tradable***

There is no official definition of the tradable sector. In this document the tradable sector is that part of the economy particularly exposed to foreign competition. It includes primary, manufacturing and tourism industries. Non-tradable output is estimated as a residual of total real GDP.

***Trade-weighted index (TWI)***

A measure of movements in the New Zealand dollar against the currencies of our major trading partners. The currencies comprise the US dollar, the Australian dollar, the Japanese yen, the euro and the UK pound.

***Unit labour costs***

Wages and other costs associated with employment per unit of output.

***Year ended***

Graphs and tables use different expressions of the timeframe. For example, 2011/12 or 2012 will generally mean “year ended 30 June” unless otherwise stated.

# Time Series of Fiscal and Economic Indicators

## Fiscal Indicators

| June Years | 2000 Actual | 2001 Actual | 2002 Actual | 2003 Actual | 2004 Actual | 2005 Actual | 2006 Actual | 2007 Actual | 2008 Actual | 2009 Actual | 2010 Actual | 2011 Actual | 2012 Forecast | 2013 Forecast | 2014 Forecast | 2015 Forecast | 2016 Forecast |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| $ millions | | | | | | | | | | | | | | | | | |
| **Revenue and Expenses** | | | | | | | | | | | | | | | | | |
| Core Crown revenue | 34,946 | 37,842 | 39,945 | 43,440 | 46,219 | 51,045 | 55,735 | 58,211 | 61,819 | 59,482 | 56,216 | 57,550 | 61,165 | 65,736 | 70,428 | 74,786 | 79,159 |
| Core Crown expenses | 34,829 | 36,559 | 37,513 | 39,897 | 41,882 | 44,895 | 49,320 | 54,003 | 56,997 | 64,002 | 64,013 | 70,450 | 74,460 | 71,612 | 72,920 | 75,583 | 78,034 |
| **Surpluses** | | | | | | | | | | | | | | | | | |
| Total Crown OBEGAL | 594 | 1,422 | 2,471 | 4,366 | 5,573 | 7,075 | 7,091 | 5,860 | 5,637 | (3,893) | (6,315) | (18,396) | (10,809) | (4,438) | (943) | 1,450 | 3,076 |
| Total Crown operating balance | 1,405 | 1,208 | 2,286 | 1,621 | 7,309 | 5,931 | 9,542 | 8,023 | 2,384 | (10,505) | (4,509) | (13,360) | (12,601) | (2,375) | 1,576 | 3,974 | 5,701 |
| **Cash Position** | | | | | | | | | | | | | | | | | |
| Core Crown residual cash | (386) | 349 | 216 | 1,217 | 520 | 3,104 | 2,985 | 2,877 | 2,057 | (8,639) | (9,000) | (13,343) | (13,636) | (9,866) | (4,976) | (4,056) | (1,580) |
| **Debt** | | | | | | | | | | | | | | | | | |
| Gross debt[1] | 36,580 | 37,194 | 36,650 | 36,617 | 36,017 | 35,478 | 33,903 | 30,647 | 31,390 | 43,356 | 53,591 | 72,420 | 79,779 | 80,000 | 88,403 | 87,129 | 89,788 |
| Gross debt incl RB settlement cash and bank bills | 36,580 | 37,194 | 36,650 | 36,617 | 36,017 | 35,478 | 35,867 | 36,805 | 37,745 | 50,973 | 58,891 | 77,290 | 83,764 | 83,985 | 92,388 | 91,114 | 93,773 |
| Net core Crown debt (incl NZS Fund)[2] | 25,895 | 24,908 | 24,773 | 22,647 | 19,902 | 13,324 | 6,302 | 1,620 | (2,676) | 5,633 | 12,549 | 23,969 | 35,652 | 43,780 | 46,678 | 48,453 | 47,775 |
| Net core Crown debt[2] | 25,895 | 24,908 | 25,388 | 24,531 | 23,858 | 19,879 | 16,163 | 13,380 | 10,258 | 17,119 | 26,738 | 40,128 | 53,823 | 63,151 | 67,775 | 71,324 | 72,534 |
| **Net Worth** | | | | | | | | | | | | | | | | | |
| Total Crown net worth | 12,605 | 15,450 | 22,825 | 28,012 | 39,595 | 54,240 | 83,971 | 96,827 | 105,514 | 99,515 | 94,988 | 80,887 | 68,282 | 65,939 | 67,526 | 71,514 | 77,229 |
| **Nominal GDP** | 112,588 | 119,991 | 127,511 | 134,659 | 145,200 | 154,376 | 161,890 | 172,060 | 183,325 | 185,449 | 189,359 | 200,291 | 211,773 | 221,864 | 234,325 | 246,189 | 256,939 |
| % GDP | | | | | | | | | | | | | | | | | |
| **Revenue and Expenses** | | | | | | | | | | | | | | | | | |
| Core Crown revenue | 31.0 | 31.5 | 31.3 | 32.3 | 31.8 | 33.1 | 34.4 | 33.8 | 33.7 | 32.1 | 29.7 | 28.7 | 28.9 | 29.6 | 30.1 | 30.4 | 30.8 |
| Core Crown expenses | 30.9 | 30.5 | 29.4 | 29.6 | 28.8 | 29.1 | 30.5 | 31.4 | 31.1 | 34.5 | 33.8 | 35.2 | 35.2 | 32.3 | 31.1 | 30.7 | 30.4 |
| **Surpluses** | | | | | | | | | | | | | | | | | |
| Total Crown OBEGAL | 0.5 | 1.2 | 1.9 | 3.2 | 3.8 | 4.6 | 4.4 | 3.4 | 3.1 | (2.1) | (3.3) | (9.2) | (5.1) | (2.0) | (0.4) | 0.6 | 1.2 |
| Total Crown operating balance | 1.2 | 1.0 | 1.8 | 1.2 | 5.0 | 3.8 | 5.9 | 4.7 | 1.3 | (5.7) | (2.4) | (6.7) | (6.0) | (1.1) | 0.7 | 1.6 | 2.2 |
| **Cash Position** | | | | | | | | | | | | | | | | | |
| Core Crown residual cash | (0.3) | 0.3 | 0.2 | 0.9 | 0.4 | 2.0 | 1.8 | 1.7 | 1.1 | (4.7) | (4.8) | (6.7) | (6.4) | (4.4) | (2.1) | (1.6) | (0.6) |
| **Debt** | | | | | | | | | | | | | | | | | |
| Gross debt[1] | 32.5 | 31.0 | 28.7 | 27.2 | 24.8 | 23.0 | 20.9 | 17.8 | 17.1 | 23.4 | 28.3 | 36.2 | 37.7 | 36.1 | 37.7 | 35.4 | 34.9 |
| Gross debt incl RB settlement cash and bank bills | 32.5 | 31.0 | 28.7 | 27.2 | 24.8 | 23.0 | 22.2 | 21.4 | 20.6 | 27.5 | 31.1 | 38.6 | 39.6 | 37.9 | 39.4 | 37.0 | 36.5 |
| Net core Crown debt (incl NZS Fund)[2] | 23.0 | 20.8 | 19.4 | 16.8 | 13.7 | 8.6 | 3.9 | 0.9 | (1.5) | 3.0 | 6.6 | 12.0 | 16.8 | 19.7 | 19.9 | 19.7 | 18.6 |
| Net core Crown debt[2] | 23.0 | 20.8 | 19.9 | 18.2 | 16.4 | 12.9 | 10.0 | 7.8 | 5.6 | 9.2 | 14.1 | 20.0 | 25.4 | 28.5 | 28.9 | 29.0 | 28.2 |
| **Net Worth** | | | | | | | | | | | | | | | | | |
| Total Crown net worth | 11.2 | 12.9 | 17.9 | 20.8 | 27.3 | 35.1 | 51.9 | 56.3 | 57.6 | 53.7 | 50.2 | 40.4 | 32.2 | 29.7 | 28.8 | 29.0 | 30.1 |

1 Excludes Reserve Bank settlement cash and bank bills
2 Excludes advances

# Economic Indicators

| **March Years** | **2000** | **2001** | **2002** | **2003** | **2004** | **2005** | **2006** | **2007** | **2008** | **2009** | **2010** | **2011** | **2012** | **2013** | **2014** | **2015** | **2016** |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| Annual average % change | Actual | Actual | Actual | Actual | Actual | Actual | Actual | Actual | Actual | Actual | Actual | Actual | Forecast | Forecast | Forecast | Forecast | Forecast |
| Private consumption | 3.3 | 1.4 | 2.7 | 4.8 | 6.2 | 4.5 | 4.4 | 2.5 | 3.3 | -1.1 | 0.3 | 2.0 | 2.1 | 2.2 | 2.9 | 2.9 | 2.2 |
| Public consumption | 5.8 | -2.1 | 4.2 | 1.4 | 4.9 | 4.6 | 4.9 | 4.1 | 5.0 | 4.2 | 0.2 | 3.8 | 1.8 | -1.5 | -0.2 | 0.5 | 0.7 |
| **TOTAL CONSUMPTION** | 3.8 | 0.6 | 3.0 | 4.0 | 5.9 | 4.6 | 4.5 | 2.8 | 3.7 | 0.1 | 0.3 | 2.5 | 2.0 | 1.3 | 2.2 | 2.4 | 1.9 |
| Residential investment | 19.5 | -13.3 | 2.0 | 23.6 | 14.9 | 2.6 | -5.1 | -1.4 | 3.8 | -23.2 | -13.0 | 2.3 | -8.4 | 37.6 | 34.9 | 14.2 | 5.5 |
| Non-market investment | 13.0 | -13.8 | 21.9 | 10.7 | 15.7 | 11.0 | 5.9 | -7.0 | -7.9 | 15.6 | -5.6 | 5.0 | 1.1 | -8.8 | 3.2 | 5.7 | 3.4 |
| Market investment | 7.4 | 7.3 | 6.9 | 2.8 | 13.0 | 11.9 | 11.3 | -1.5 | 9.4 | -3.3 | -10.1 | 7.8 | 8.9 | 9.8 | 10.3 | 4.1 | -0.3 |
| **TOTAL INVESTMENT** | 10.9 | -0.1 | 6.8 | 8.0 | 13.6 | 8.8 | 6.6 | -2.2 | 6.3 | -7.7 | -9.5 | 5.9 | 5.0 | 16.2 | 14.4 | 6.4 | 1.2 |
| Stock change (contribution to growth) | 1.2 | -0.3 | 0.1 | -0.1 | 0.2 | 0.3 | -0.5 | -0.7 | 0.6 | 0.2 | -2.2 | 1.4 | -0.5 | 0.2 | 0.1 | 0.2 | 0.2 |
| **GROSS NATIONAL EXPENDITURE** | 6.4 | 0.2 | 3.8 | 4.7 | 7.6 | 5.8 | 4.5 | 1.0 | 4.8 | -1.4 | -3.7 | 4.5 | 2.1 | 4.8 | 5.4 | 3.7 | 1.9 |
| Exports | 7.4 | 6.3 | 3.0 | 7.8 | 1.1 | 4.8 | -0.2 | 2.9 | 3.4 | -3.0 | 4.8 | 1.9 | 2.8 | 2.3 | 1.9 | 1.7 | 1.8 |
| Imports | 11.3 | -0.7 | 4.0 | 7.2 | 12.7 | 12.5 | 4.2 | -1.6 | 10.4 | -4.3 | -9.4 | 10.5 | 3.6 | 6.1 | 8.0 | 4.3 | 0.7 |
| **EXPENDITURE ON GDP** | 5.2 | 2.4 | 3.5 | 5.0 | 4.0 | 3.6 | 3.3 | 2.2 | 2.8 | -0.9 | 0.8 | 1.9 | 2.0 | 3.2 | 3.3 | 2.8 | 2.4 |
| **GDP (production measure)** | 5.4 | 2.5 | 3.6 | 4.9 | 4.4 | 3.8 | 3.2 | 0.9 | 3.0 | -1.5 | -0.7 | 1.6 | 2.3 | 3.4 | 3.3 | 2.9 | 2.4 |
| - annual % change | 6.5 | 0.8 | 4.6 | 4.6 | 5.3 | 2.6 | 2.4 | 1.7 | 2.3 | -3.5 | 1.8 | 1.6 | 2.5 | 3.7 | 3.1 | 2.8 | 2.2 |
| Real GDP per capita | 4.8 | 1.9 | 2.7 | 3.0 | 2.4 | 2.4 | 2.1 | -0.4 | 1.9 | -2.4 | -1.8 | 0.5 | 1.5 | 2.6 | 2.4 | 1.9 | 1.5 |
| Nominal GDP (expenditure basis) | 6.0 | 5.7 | 7.5 | 5.1 | 6.9 | 7.1 | 5.6 | 5.0 | 7.7 | 1.9 | 1.2 | 5.7 | 5.5 | 4.7 | 5.8 | 5.1 | 4.5 |
| GDP deflator | 0.8 | 3.2 | 3.9 | 0.2 | 2.8 | 3.3 | 2.3 | 2.8 | 4.7 | 2.9 | 0.4 | 3.7 | 3.5 | 1.5 | 2.4 | 2.2 | 2.1 |
| Output gap (% deviation, March year average) | 0.6 | 0.1 | 0.1 | 1.0 | 1.4 | 1.7 | 2.1 | 1.1 | 2.8 | 0.7 | -0.7 | -0.7 | -0.8 | -0.2 | -0.1 | -0.1 | -0.2 |
| Employment | 1.9 | 2.0 | 2.9 | 2.8 | 3.0 | 3.6 | 2.8 | 2.2 | 1.3 | 0.9 | -1.3 | 1.2 | 1.8 | 1.5 | 1.5 | 1.4 | 1.3 |
| Unemployment (% March quarter s.a.) | 6.5 | 5.5 | 5.3 | 5.0 | 4.3 | 3.9 | 4.0 | 3.9 | 3.9 | 5.1 | 6.1 | 6.5 | 5.8 | 5.2 | 4.9 | 4.7 | 4.7 |
| Wages (average ordinary-time hourly, ann % change) | 1.7 | 3.2 | 3.7 | 2.3 | 3.5 | 3.6 | 5.4 | 4.7 | 4.7 | 5.4 | 1.0 | 2.6 | 4.0 | 3.3 | 4.2 | 4.1 | 4.0 |
| CPI inflation (ann % change) | 1.5 | 3.1 | 2.6 | 2.5 | 1.5 | 2.8 | 3.3 | 2.5 | 3.4 | 3.0 | 2.0 | 4.5 | 2.8 | 2.2 | 2.4 | 2.5 | 2.7 |
| Merchandise terms of trade (SNA basis) | 0.2 | 3.4 | 4.0 | -5.6 | 4.3 | 3.5 | -2.0 | -1.1 | 8.5 | -0.1 | -7.5 | 9.9 | 3.2 | -1.4 | 1.0 | 1.1 | 0.3 |
| Current account balance - $billion | -7.1 | -4.4 | -3.4 | -4.1 | -6.2 | -9.4 | -14.0 | -13.5 | -14.6 | -14.8 | -3.6 | -7.2 | -5.0 | -7.9 | -12.6 | -15.6 | -17.6 |
| Current account balance - % of GDP | -6.4 | -3.7 | -2.7 | -3.1 | -4.4 | -6.2 | -8.7 | -8.0 | -8.0 | -8.0 | -1.9 | -3.6 | -2.4 | -3.6 | -5.4 | -6.4 | -6.9 |
| TWI (March quarter) | 54.1 | 50.5 | 51.6 | 60.6 | 66.9 | 69.6 | 68.3 | 68.8 | 71.9 | 53.7 | 65.3 | 67.2 | 70.0 | 70.1 | 69.6 | 67.2 | 63.3 |
| 90-day bank bill rate (March quarter) | 6.0 | 6.4 | 5.0 | 5.8 | 5.5 | 6.9 | 7.6 | 7.8 | 8.8 | 3.7 | 2.7 | 3.0 | 2.9 | 3.7 | 4.3 | 5.0 | 5.3 |
| 10-year bond rate (March quarter) | 7.3 | 6.0 | 6.7 | 6.0 | 5.9 | 6.0 | 5.7 | 5.9 | 6.3 | 4.6 | 5.9 | 5.6 | 4.4 | 4.6 | 5.0 | 5.2 | 5.4 |