  

CHiLD POVERTY ACTION GROUP

CPAG'S analysis of the 2020 Government budget

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CPAG's ANALYSIS of the 2020 BUDGET

Each year, shortly after the Government's Budget is published, Child Poverty Action Group provides its analysis of some of the details contained in various budget papers. This analysis seeks to do two things – to critically examine budget figures in order to gain an appreciation of the Budget's implications for children and to publish this analysis as an alternative interpretation to that offered by mainstream media.

The analysis offered here attempts to take a longer-term, bigger picture view of the Budget. While those preparing the Budget may have a longer-term perspective, this is seldom presented in Budget papers. Instead these papers have a medium term – four-year timeframe, and generally offer no assessment of the recent past. As an alternative CPAG's analysis attempts to frame the Budget on a ten-year horizon involving the four forthcoming years covered by Budget forecasts, the current financial year and the last five.

This analysis also attempts to examine budgets – past and present, in light of inflation, economic growth and population growth. Such an examination provides further insights into the real – inflation adjusted, effects of the Government budgets and the likely future demand for public services arising from population and economic growth.

In this analysis we have used Treasury's own Budget projections of inflation and economic growth in order to calculate the impacts of inflation on the real value of budgets and the share of future GDP which these budgets represent. For estimates of per-capita budgets we have used Statistics New Zealand's population forecasts and in particular the 95th percentile estimates of the medium population growth scenario.

The observations and insights offered here are not seen as being a complete critique of the Budget and political choices behind it. Rather, we hope that it can offer readers an alternative perspective of these priorities and choices – an alternative to that of mainstream media with its pre-occupation on the interests and concerns of private sector businesses.

Given the extraordinary nature of the 2020 Budget many of the comparisons with past spending trends and priorities are not particularly relevant. What comparisons with the past do illustrate is just how extraordinary the spending parameters of this Budget are and how much they determine our immediate future as a nation. In considering the scale of additional spending proposed in the 2020 Budget it is important not to forget the various social and economic challenges we faced prior to the COVID-19 pandemic. Challenges such as enduring inequality, a shortage of decent, affordable housing and of course child poverty remain with us. We should be asking and certainly CPAG asks- what are we doing to address these challenges as part of national efforts to rebuild our economy after COVID-19? The analysis offered here attempts to consider this question.

We welcome your feedback on this paper especially any suggestions for improving on this initiative next year.

ECONOMIC & FINANCIAL FORECASTS

Economic forecasting is never easy, but this is especially so following an economic shock which as most are, was unanticipated. The economic shock caused by the COVID-19 is unprecedented in New Zealand's modern economic history as was the scale of the shutdown designed to suppress the coronavirus disease. The resulting recession is similarly unprecedented so it is impossible to predict the scale and nature of the economic downturn.

In response to such uncertainty Treasury have developed a number of economic scenarios which are based on various sets of economic impacts[1]. These impacts included the extent of the shutdown to control the virus along with possible impacts on New Zealand's main trading partners. The best fitting of Treasury's scenarios is Scenario 1a. This scenario matches the extent of the Level 4 and Level 3 shutdown and assumes that Government will provide a $20 billion fiscal stimulus to re-start the economy. In many respects the 2020 Budget is the beginning of this stimulus package.

The economic parameters developed under Scenario 1a appear to have been carried forward into the 2020 Budget. A summary of these parameters or assumptions are reported in Table 1.

In effect Treasury is anticipating a sharp V-shaped recession rather than a U shaped one which occurred following the GFC. In this V-shaped recovery, it is expected that there will be sharp fall in the level of economy activity followed by an equally steep recovery. For example, Treasury is suggesting that the economy will grow (in real terms) at the rate of 8.6% during the year to March 2022 and 4.6% the following year. This growth is not seen to be inflationary – presumably because of surplus capacity, and will more or less return employment levels to their pre-COVID-19 levels by mid-2024.

The presumption of this sharp V-shaped recovery is important for the economic and social wellbeing of New Zealanders. An extended U-shaped recovery, such as that from the GFC recession between 2008 and 2014, will result in tens of thousands of workers being unemployed for years with the resulting economic and social costs. In addition, the decline being anticipated during the COVID-19 recession is much deeper than that during the GFC when unemployment peaked at 6.8% of the workforce in December 2012[2].

Table 1: Key economic assumptions of the 2020 Budget

Year ending March	2020	2021	2022	2023	2024
Real GDP growth	*-4.6%*	*-1.0%*	*8.6%*	*4.6%*	*3.6%*
Unemployment rate	*8.3%*	*7.6%*	*5.7%*	*5.2%*	*4.8%*
CPI inflation	*1.3%*	*0.8%*	*1.5%*	*1.8%*	*1.9%*
Current account (as % of GDP)	*-2.0%*	*-5.7%*	*-4.2%*	*-3.8%*	*-3.6%*

A summary of forecasts of Government finances from the 2020 Budget is offered in Table 2. This table outlines clearly the sharp decline in the Government's financial fortunes which will arise, mainly as a result of significant increases in core Crown expenditure. This expenditure is expected to rise by more than 30% during the current financial year to $113 billion and remains at similar levels for the whole forecast period. Aggravating the consequent deficits are small falls in tax revenues during the 2019-20 and 2020-21 fiscal years. These deficits sit around $28 billion between 2020 and 2023 before falling to a modest $5 billion on 2023-24. These deficits are financed through a massive blow-out in core crown debt which grows more than three-fold between 2020 and 2024 to $200 billion.

Table 2: Key financial forecasts from the 2020 Budget - *$billions*

Year ending June	2019	2020	2021	2022	2023	2024
Core Crown tax revenue	*86.5*	*82.3*	*80.1*	*87.3*	*96.5*	*102.1*
Core Crown expenditure	*87.0*	*114.0*	*113.5*	*119.8*	*118.6*	*113.0*
OBEGAL[3]	*7.4*	*(28.3)*	*(29.6)*	*(27.2)*	*(16.5)*	*(4.9)*
Net core Crown debt[4]	*57.7*	*88.9*	*129.5*	*163.6*	*188.7*	*200.8*

The sharp increase in spending during 2020 is almost entirely a result of the Government's response to the COVID-19 shutdown. The extend of this spending and some associated tax revenue reductions are reported in Table 3. During the 2019-20 financial year these related COVID-19 related costs amounted to $14 billion with a further $5 billion of unallocated spending for the COVID-19 response and recovery funding (CRRF). In total and by the end of the four-year forecast period yet to be allocated spending on the COVID-19 recovery may exceed $39 billion. This money is in effect a war chest for Government to direct toward responses which will maintain economic activity during the recession and potentially re-shape the economy toward the Government's goal of building an economy which is prosperous, sustainable and inclusive.

As discussed below the 2020 Budget offers little in additional spending which will reduce rates of child poverty outside of credible efforts to expand the construction of public housing. This large unallocated fund may at some time be directed toward programmes which more directly address child poverty however.

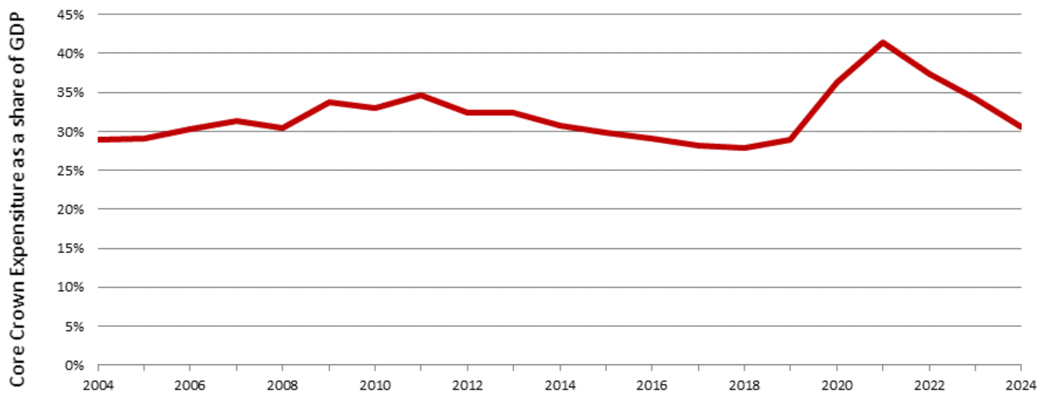
Table 3: COVID-19 decisions included in the fiscal forecasts reducing OBEGAL - *$billions*[5]

Year ending June	2020	2021	2022	2023	2024	
Reduction in tax revenue (tax policy changes)	1.2	2.0	0.8	(0.2)	0.5	**4.3**
Increase in social assistance expenditure	0.3	0.9	0.6	0.6	0.6	**3.0**
Increase in other operating expenditure	14.1	0.3	0.1	0.1	0.1	**14.7**
	15.6	3.2	1.5	0.5	1.2	**22.0**
Unallocated COVID-19 CRRF	4.9	9.8	14.8	9.8	-	**39.3**
Total COVID-19 Government Response	**20.5**	**13.0**	**16.3**	**10.3**	**1.2**	**61.3**

BUDGET SETTINGS

The COVID-19 pandemic has quickly put aside the Government's self-imposed Fiscal Responsibility rules. Included in these rules was requirement to budget for core Crown spending to be around 30% of GDP. Clearly the rules were to be applied on an averaged basis across an economic cycle and circumstances such as we now face were exempted from these conditions. Figure 1 illustrates the extent to which this 30% rule has been abandoned now. By 2022 core Crown expenditure is expected to exceed 40% of GDP. Part of this change is however due to an expected fall in GDP of almost 6% between 2020 and 2022. Of some note however is fact that core Crown expenditure reached 35% of GDP at the height of the GFC recession so there is nothing unusual about expenditures reaching such levels during recessions.

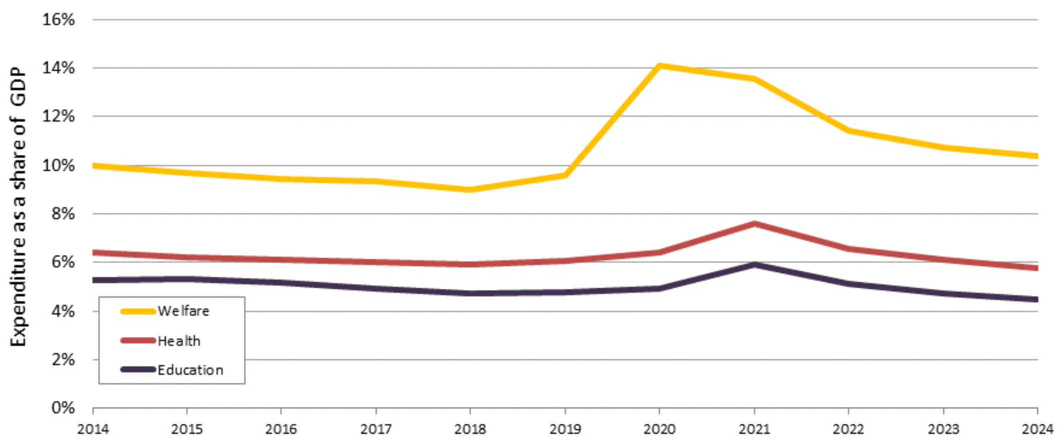
Figure 1: Core Crown expenditure as share of GDP – 2010 to 2020



Public spending on health, education and welfare accounts for around 70% of core Crown expenditure. This share falls to 62% in the 2021-2022 year on account of COVID-19 recession related spending – which as noted above is mostly not yet allocated.

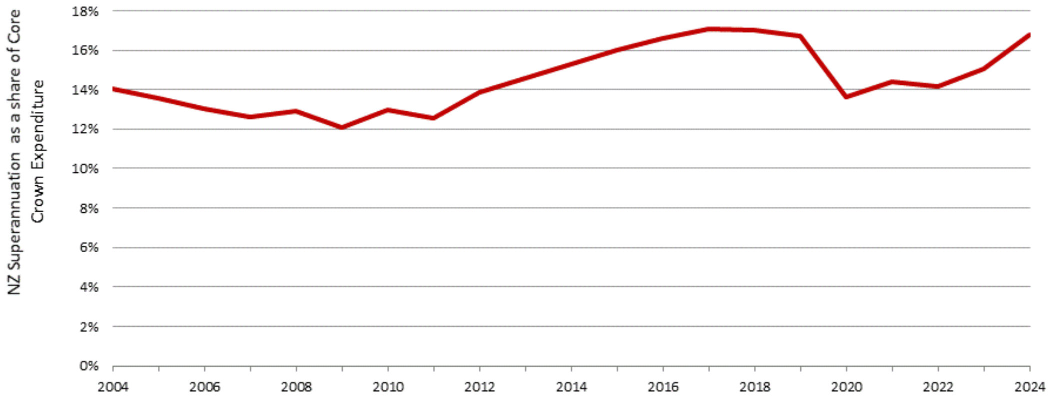
Spending on health, education and welfare as a share of GDP is reported In Figure 2. Across all three portfolios spending as a share of GDP rises over the next two years – in the case of welfare spending from a long-term trend value of 10% to 14%. Much of this increase is due to expect additional demand for welfare support on account of rising unemployment. These increases overall indicate the Government's additional commitment to spending in these core areas of public service during the recession.

Figure 2: Main areas public spending as shares of GDP - 2014 to 2024



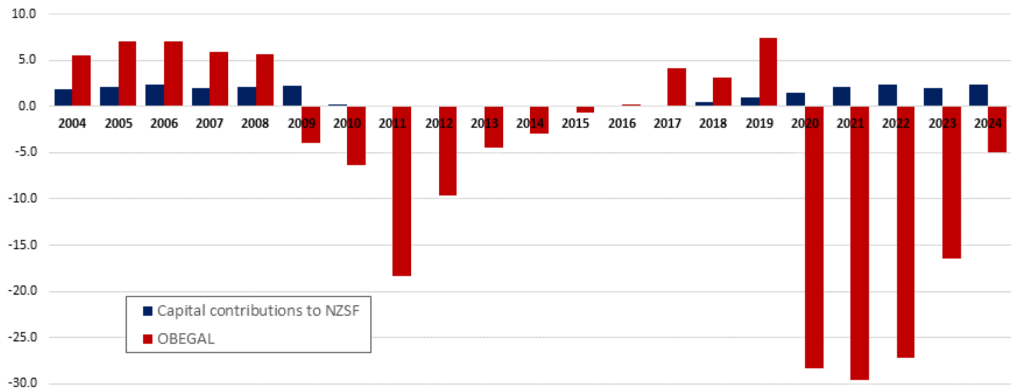
Governments have consistently but quietly made a commitment to funding our tax funded retirement income programme – New Zealand Superannuation. As baby boomers reach retirement the cost of this programme continues to grow as a share of core Crown expenditure and as a share of GDP. Between 2009 and 2017 NZ Superannuation rose from 12% of core expenditure to 17% before plateauing. As a result of the rapid growth in Government spending the share going toward NZ Super is forecast to fall to around 14% by 2022 before climbing again beyond this date. This relationship is illustrated in Figure 3.

Figure 3: Spending on NZ Superannuation as a share of core Crown expenditure - 2014 to 2024



Of some surprise in the 2020 Budget is the Government's decision to continue to allocate capital to the New Zealand Superannuation Fund despite running deficits of almost $80 billion over the next four years. Over the four years to June 2024 Government expects to contribute almost $9 billion while it borrows money to do so. Figure 4 illustrates a 20-year relationship between contributions to the NZ Superannuation Fund and Government's operating position. Typically, it has been the case the contributions are only made to the Fund at times when Government generates a surplus. This contribution has been around 20% of these surplus. For the entire period of the GFC recession and recovery no contributions were made to the fund.

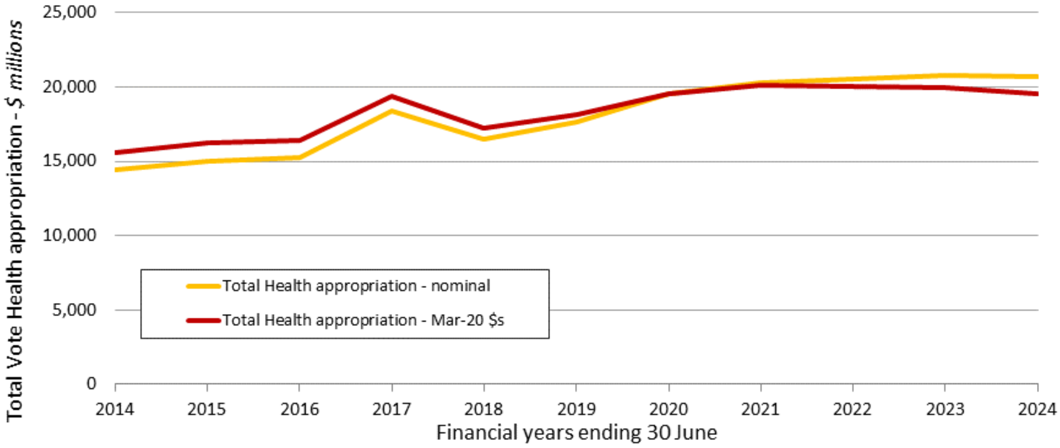
Figure 4: Contributions to New Zealand Superannuation Fund and OBEGAL – 2004 to 20204



HEALTH

Spending on public health services is budgeted to increase by just under 4% in nominal terms between 2019-20 and 2020-21 or by $770 million to $20.3 billion. Although modest, this increase comes on the back of a 10% or $1.8 billion increase in the previous year. Changes in nominal and real health sending are reported in Figure 5. Spending beyond 2022 is forecast to remain steady at about $20.5 billion annually. This represents a small real decline of 3% between 2022 and 2024.

Figure 5: Total public health budget – 2014 to 2024

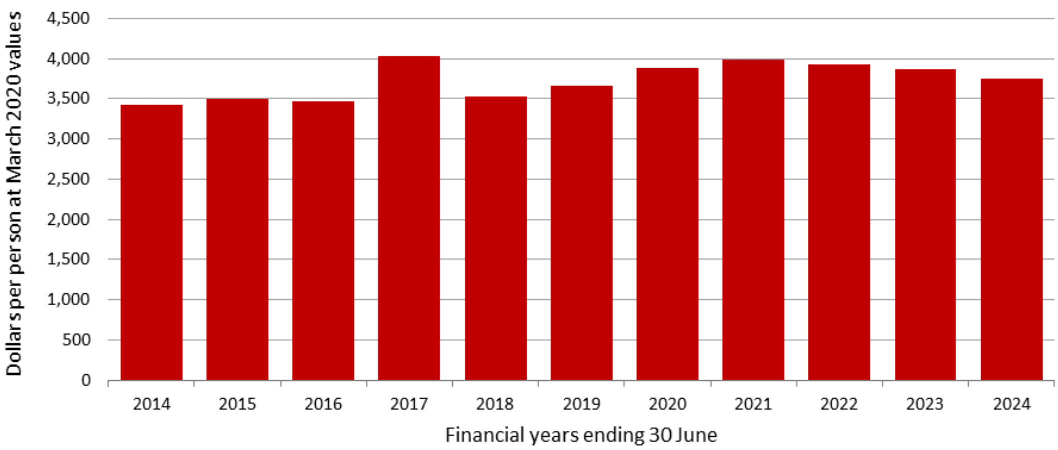


Of the total public health budget, about 75% or $15.3 billion is allocated to 19 district health boards. Budgets allocated to DHBs rose by $1 billion between 2019-20 and 2021-22 or by 6.5%.

As a share of GDP, public spending on health reached 6.2% in 2020 and is set to rise to 7.4% by 2021 before falling back to an expected 5.6% of GDP by 2024. While there is a planned increase in public health spending between 2020 and 2021 the increasing share of GDP is due to an expected decline in GDP of almost 6%.

Figure 6 reports real per-capita spending on public health services between 2014 and 2024. This shows a per-capita increase from just under $3,700 in 2018-2019 to $3,900 in 2019-2020 to almost $4,000 per head in 2020-2021. By 2024 the real per-capita spend is forecast to fall just over $3,700 again.

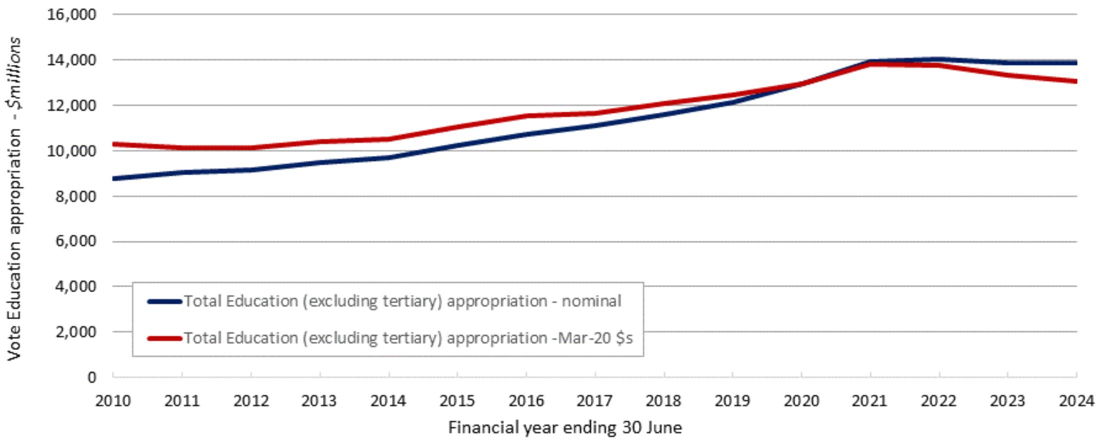
Figure 6: Real per-capita spend on public health – 2014 to 2024



EDUCATION

Total expenditure on early childhood education and compulsory education is forecast to increase by $900 million between 2019-2020 and 2020-2021 or by 7.6% to $13.9 billion. Beyond 2021 spending is forecast to remain at around $14 billion which in inflation adjusted terms represents a small real decline of about 5% through to 2024. Real and nominal spending trends on public education (excluding tertiary) are reported in Figure 7 for the period 2014 to 2024.

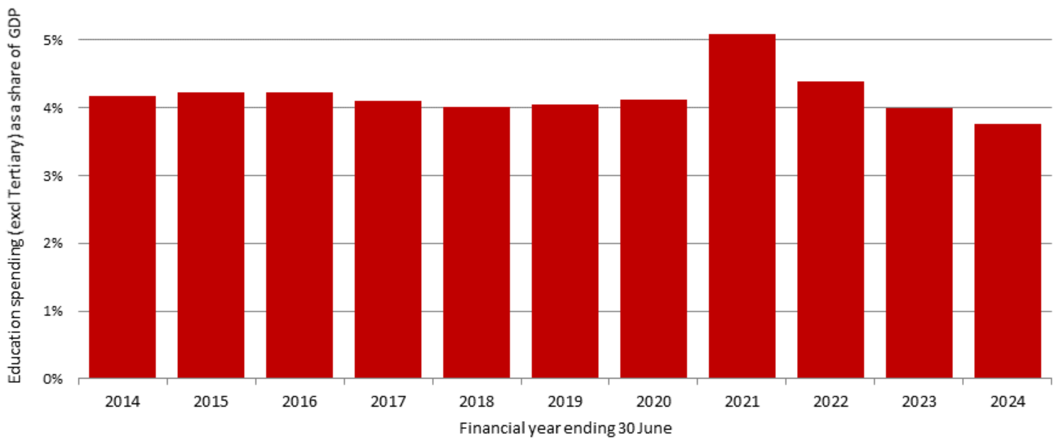
Figure 7: Total education budgets - 2014 to 2024



This fairly solid budget increase immediately followed by static budgets subsequently, means of course that in per-capita terms and as a share of GDP public education spending fades in later years. As a share of GDP, education spending is at 4.1% in 2019-20 and grows to 5.1% in 2020-2021 on the back of an expected contracting economy. Beyond this as a share of GDP, the education spend shrinks to 3.8% by 2024.

In per-capita terms the increase between 2019-2020 and 2020-2021 represents an increase from just over $2,500 per person to almost $2,700 but this shrinks to approximately $2,450 by 2024. This trend is illustrated in Figure 8.

Figure 8: Real per capita spend on education (excluding tertiary) **– 2014to 2024**



Early learning or pre-school education accounts just over $2 billion of the education spend. Spending in this area is set to rise by 5.5% in nominal terms between 2020 and 2021 to sit at $2.14 billion – an overall increase of $110.%. Changes in budget categories for primary and secondary education make year on year comparisons between 2020 and 2021 unreliable. During the 2020-2021 financial year primary education will receive a total allocation of $3.87 billion while secondary education receives $2.81 billion.

INCOME SUPPORT

Rising demand for welfare benefits is expected as a consequence of the COVID-19 recession where the total number of adults receiving a working age benefit may grow by almost 60% between 2019 and 2021. This is an increase of about 170,000 people of whom about 158,000 will be receiving a Jobseeker's payment. Alongside, this the uptake of the Accommodation Supplement is expected to grow by perhaps 140,000 people to more than 430,000. Forecasts for the number of people receiving a benefit or NZ Superannuation payment are reported in Table 4

Table 4: Numbers of people receiving benefits 2019 to 2024 *(000's of people)*

Year ending June	2019	2020	2021	2022	2023	2024
New Zealand Superannuation	767	795	821	847	874	901
Jobseeker Support and Emergency Benefit	139	166	297	246	202	180
Supported living payment	95	96	97	99	101	103
Sole parent support	59	61	70	74	73	70
All working age benefits	293	323	464	419	376	353
Accommodation Supplement	295	322	431	404	376	362

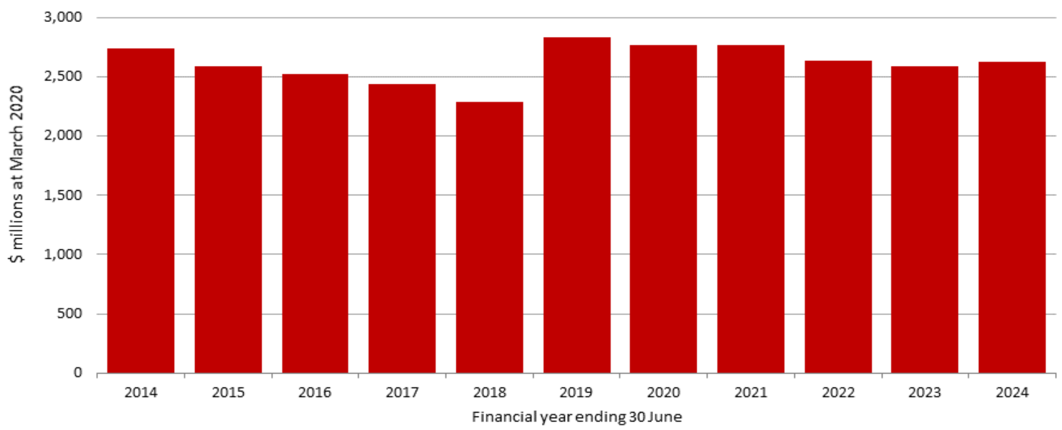
This increased demand will see the total cost of the various income support budgets rise from $26.7 billion in 2018-2019 to $32.9 billion in 2019-2020 and to $34.2 billion by 2020-2021. This is a nominal increase of 28% and a real increase of 24%. The most significant increase is the $2.1 billion expansion in the Jobseeker payments budget between 2020 and 2021, to $4.5 billion. Almost unnoticed in the scale of these changes is the inexorable increases in the NZ Superannuation budgets which continue to grow at around $900 million each year.

Table 5: Summary of benefits and income support programmes - *$nominal millions*

Year ending June	2019	2020	2021	2022	2023	2024
New Zealand Superannuation	14,562	15,516	16,346	16,941	17,859	18,983
Housing subsidies	2,614	3,028	3,813	3,840	3,742	3,700
Working age benefits	4,525	5,253	7,905	7,260	6,801	6,659
Working for Families credits	2,766	2,768	2,792	2,695	2,696	2,787
Other benefits	2,222	6,293	3,346	3,142	3,159	3,218
Total all benefit expenses	26,689	32,858	34,202	33,878	34,257	35,347

Figure 8 illustrates real changes in the total budget allocated to Working for Families programmes. Following a substantial increase of around 26% or $570 million between 2018 and 2019, the value of the programme is expected to decline gradually without any major review of payment rates or thresholds. Between 2020 and 2024, and in inflation adjusted terms, this decline is possibly around $140 million or about 5% of the value of the programme.

Figure 9: Changes in the real costs of Working for Families – 2014to 2024



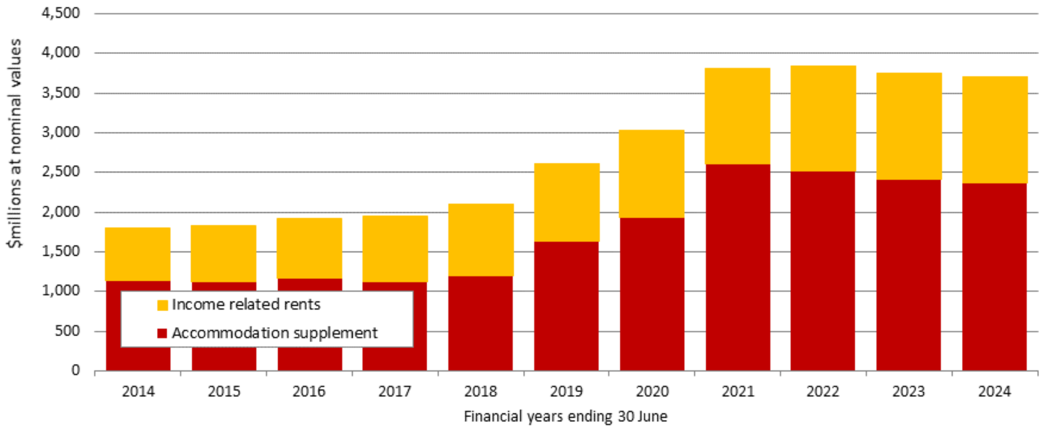
HOUSING

Housing is something of a success story in the 2020 Budget with the Minister of Housing Dr Megan Woods announcing that Government is planning to build an additional 8000 housing units over the next four years[6]. These additional units will comprise 6,000 public or other social housing units and 2,000 transitional units. These numbers are in addition the existing public housing building programme of 6,400 units and commitment to build 1000 transitional housing as part of the Government's emergency housing response. In total these figures suggest that Government, mainly through its housing and urban development agency Kainga Ora, may be building upward of 3,600 units per year for the next four years.

In addition to this house building activity, Government has also extended its commitment to the provision of emergency housing with an annual budget of $150 million. A modest increase in support for first time homeownership is also anticipated through the First Home scheme which has a budget of $110 million for 2020-2021 – an increase of almost $20 million on a year earlier.

Total spending on housing subsidies is expected to reach $3.8 billion during 2020-2021 which is a 26% increase over the previous year. The bulk of this increase ($670 million extra) is for payment of additional Accommodation Supplement subsidies and emergency housing grants and is due to an expected increase in demand arising with rising unemployment. A further $120 million is being allocated into income related rents in part to account for the increasing numbers of public and social housing tenancies. Trends in housing subsidy expenditures are reported in Figure 10.

Figure 10: Spending on housing subsidies – 2014 to 2024 – *($s nominal)*



CONCLUSIONS

This 2020 Budget has for the first time reported on progress toward child poverty reduction targets. This is a welcome innovation and adds significantly to the credibility of the wellbeing approach which is now the basis of Government's budget setting process. The results reported are provisional and tentative but still encouraging. The report acknowledges that any impact of the Government Families Package, which was introduced in mid-2018, will not yet be showing up in survey results which measure progress toward these targets. The report also acknowledges the complexity in understanding what the COVID-19 recession will do to children and to the numbers of children living in relative poverty or material hardship.

The risks which the COVID-19 recession pose for children's welfare is of concern for CPAG as it is no doubt for many other New Zealanders. Regrettably there is little in the 2020 Budget which addresses these risks. There is for example nothing to reflect the inadequate incomes offered by the working age benefits as perhaps as many 170,000 adult New Zealanders and their children join the dole queues created by the COVID-19 recession. There is nothing either to address the need for various welfare band aids such as emergency income grants, emergency housing options and State supported food banks as responses to the poverty and material hardship facing tens of thousands of New Zealand families.

A great deal is being banked on the prospect that the COVID-19 recession will be short and sharp and that the Government's massive efforts to assist the recovery will be effective in quickly turning the economy around. We hope so and we applaud the Government for its audacity in dealing with this challenge at the scale it has. The flexibility which is built into the level of unallocated budgets is warranted and useful as if can allow for well-considered policy innovations to be applied as the extent and nature of need emerges during the recovery. Such innovation, should in our opinion, be focused on the needs of the most vulnerable including many of our children.

ENDNOTES

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[1] Treasury (2020) *Treasury Report T2020/973 Economic Scenarios*. Available at https://treasury.govt.nz/publications/tr/treasury-report-t2020-973-economic-scenarios-13-april-2020

[2] Statistics New Zealand – Household Labour Force Survey

[3] Operating balance before gains and losses and excluding minority interest – BEFU 2016 p.96

[4] This figure excludes NZS Fund assets

[5] BEFU 2020 Table 2.2

[6] https://www.beehive.govt.nz/release/8000-more-public-houses-be-delivered