ANZ Research

NZ Pre-election Economic & Fiscal Update Preview

8 September 2020

Contact

Miles Workman for more details.

Deja-PREFU

Summary

- Pushing out the election date has provided the Treasury time to incorporate renewed lockdown measures into the economic and fiscal forecasts. This will dampen the rebound from the first lockdown, as it has in our economic outlook.
- However, there's a lot more than that for the Treasury to incorporate into the outlook since the May Budget, including fiscal and monetary policy decisions, the economy's vigorous rebound out of the first lockdown, a weaker global economy, and likely a reassessment of the Treasury's medium-term economic assumptions (that were largely unchanged at Budget and sitting on the optimistic side of things).
- Overall, we expect to see a stronger starting point for the economy and some fiscal indicators, but more than likely a slightly slower recovery.
- Pre-election Updates are intended to inform the public and the incoming Government about the state of the books ahead of the election. They are not a platform for fiscal policy announcements. Accordingly, we don't expect any.
- Changes to New Zealand Debt Management's (NZDM) bond issuance guidance should be relatively minor. The Budget Update forecasts showed the Treasury is expected to hold a substantial buffer of financial assets over the forecast horizon. We think it would be premature for NZDM to conclude that it won't be needed.

Key points

The Treasury will open up the Government's books on 16 September ahead of the General Election (scheduled for 17 October), with the publication of the Pre-election Economic and Fiscal Update (PREFU).

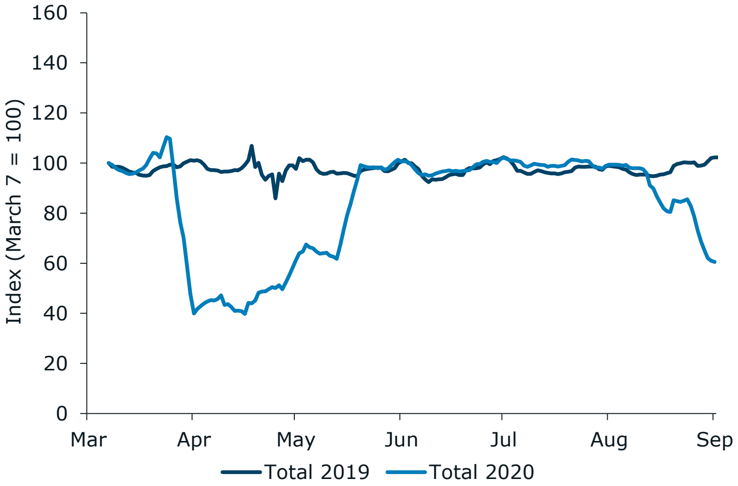
The PREFU will outline the Treasury's take on the economic and fiscal situation, and how they expect this to unfold over the next four years or so. Pushing out the election has given the Treasury the chance to review its economic and fiscal forecasts in light of renewed lockdown restrictions.

While the election result could bring changes to policy settings, the Treasury's forecasts will assume that Government decisions taken at the time of forecast finalisation will be carried through the forecast period. Any changes to policy after the election will be included in December's Half-Year Update.

A stronger starting point, but more than likely a slower recovery

Reflecting the vigorous rebound in the timely data following the first lockdown, we expect the Treasury to upgrade its forecast for Q2 GDP (-23.5% q/q at Budget). And they won't have to wait long to see if they're right. These data are published the following day at 10:45am. But as figure 1 shows, renewed lockdown measures are going to hamper the Q3 rebound.

Figure 1. ANZ card spending



Source: ANZ

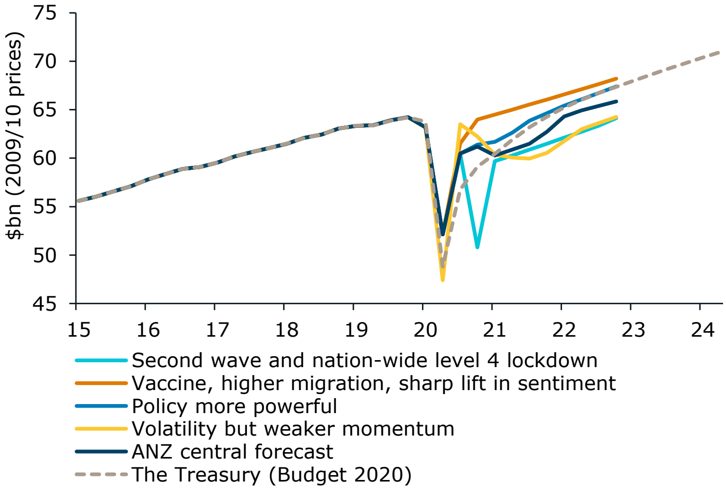
But there is a lot more for the Treasury to incorporate into the outlook than renewed lockdown restrictions:

- There are fiscal and monetary policy developments, which have both landed on the more stimulatory side versus what was assumed in the May Budget Update's central outlook.
- Conversely, there's likely to be a number of assumption changes that could weigh on the medium-term outlook, such as the length of time our borders remain closed, and the speed limit of the economy (potential GDP), given very weak business investment and low net migration.
- Then there's the fact that the global slowdown is looking worse than previously assumed. Although New Zealand's commodity prices are proving relatively resilient so far, this will weigh on expected domestic incomes, investment and sentiment more broadly.

Overall, we think the stronger starting point for GDP will be met with a slightly weaker medium-term outlook, but perhaps not significant enough to see a material deterioration in the fiscal outlook compared to the Budget Update.

However, it's worth noting that in this extremely uncertain environment, all forecasts will be wrong to some degree. The Treasury will once again communicate this clearly and lean on its scenarios (possibly not too dissimilar to our own, figure 2) to demonstrate how things could evolve from here.

Figure 2. GDP forecasts and ANZ scenarios

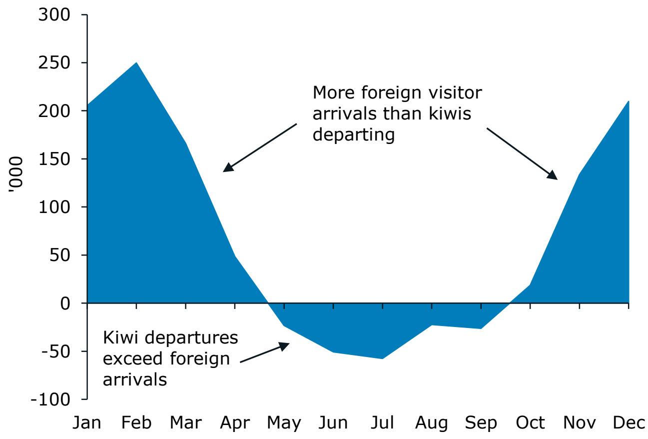


Source: Stats NZ, ANZ Research

Near term, the data is going to be volatile and subject to significant revisions. But it's the medium-term implications of this crisis that really matter – especially from a fiscal and monetary policy perspective. While some of the timely data has surprised a number of forecasters (including us and the Treasury) on the upside, it's worth remembering that there's a long way to go.

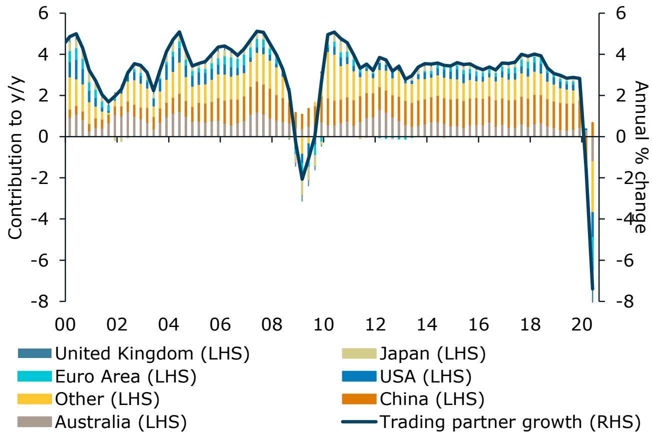
The initial lockdown (and now, renewed measures) is just one part of this shock. There's still the persistent impacts of a closed border (which will be felt much more acutely in the months ahead when net visitor arrivals would normally be lifting rapidly, figure 3), and the very sharp and synchronised global slowdown (figure 4) that will impact export earnings, investment and confidence more broadly. So far we've primarily experienced the impacts of the initial lockdown, but unfortunately the strong bounce out of that doesn't mean we've dodged the looming significant national income shock. International tourism was as big a foreign exchange earner as the dairy industry. And it's gone up in smoke.

Figure 3. Average net visitor arrivals to NZ, 2016-2019



Source: Stats NZ, ANZ Research

Figure 4. Trading partner growth



Source: Stats NZ, Macrobond, ANZ Research

Combined with the fact that the economy is yet to be weaned off an unprecedented amount of temporary support measures (such as the wage subsidy and mortgage relief), we think the Treasury are likely to conclude – as we do – that recovery over the medium term will be a little slower than assumed in May's Budget Update.

A few tweaks to the fiscal outlook

The starting point for the Government's books will be a little stronger than expected at the Budget Update, but it hasn't been one-way traffic for the Government's key fiscal indicators.

In the 11 months to May, core Crown tax revenue was almost $1.5bn ahead of forecast, consistent with a sharper-than-expected bounce in activity from lockdown. Expenses were tracking very close to forecast, despite the Budget forecasts being finalised before a number of decisions were taken. An OBEGAL deficit of $16bn was $1.6bn narrower than forecast. But at $78.7bn, net core Crown debt was $1.3bn higher than forecast, owing mostly to higher-than-forecast repurchase losses on the RBNZ's Large Scale Asset Purchase programme (LSAP). Broadly speaking, the RBNZ's LSAP is expected to cause an initial increase in net debt, but that's expected to unwind over time.

Like the broader economic outlook, there is a lot of information to incorporate into the fiscal outlook since the Budget figures were finalised in May. But we expect most of this will be around timing and allocation rather than wholesale changes to the fiscal stance. Forecast net core Crown debt is likely to peak close to 55% of GDP once again, with an OBEGAL deficit close to 10% of GDP in the 2021 fiscal year, with narrowing deficits thereafter.

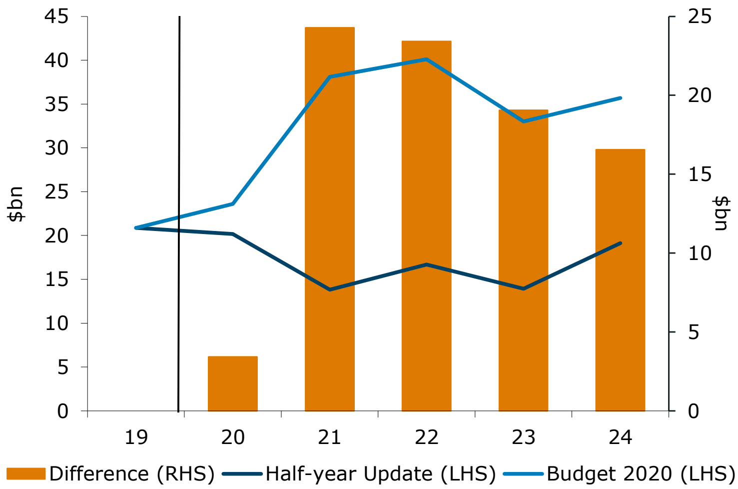
The $14bn unallocated portion of the COVID Response and Recovery Fund (CRRF) is likely to be treated like it was at the Budget, as operational spending. It would be premature to take it out now, given uncertainty around the outlook for both the virus and the economy. In our view, this money (and possibly more) will be needed to facilitate the recovery even if virus risks are contained in a relatively timely manner.

On the spending and tax side, we don't expect any new policy announcements. The PREFU is a Treasury document (not the Government of the day's) and is not intended as a platform for the incumbent Government to electioneer from. Rather, the PREFU is about informing the voter about the state of the books ahead of the election and ensuring that the incoming Government isn't met with any major surprises when they take office after the election.

Little change to the bond programme

Before the recent virus flare-up, we would have said risks were skewed towards a small downgrade to issuance guidance. NZ Debt Management has had a little more cash come in the door via syndication than expected, the forecast buffer of financial assets held by the Treasury at Budget was suitably large (figure 5), and tax revenues have been a touch better than expected.

Figure 5. Financial assets held by the Treasury



Source: The Treasury

However, the return of COVID in the community is a good reminder that this crisis is very unpredictable. We think NZDM will conclude that the prudent thing to do is maintain issuance guidance broadly in line with that signalled at the Budget Update until there is more clarity around the economic and fiscal outlook. They'll also want to be ready for any possible changes to policy settings after the election. Indeed, NZDM have a preference for stability in their guidance, and will want to avoid flip-flopping at this early stage.

Table 1. Bond issuance guidance

	Jun-21	Jun-22	Jun-23	Jun-24	Total
Budget Update	60	40	35	30	165

We don't expect a materially lower bond programme, but against the backdrop of the RBNZ upsizing the LSAP and moving to a tactical approach to bond purchases, the outlook for bonds is better. And while the RBNZ hasn't taken the liberty of flexing the pace of weekly purchases in recent weeks by as much as it did in April, we do expect the RBNZ's ongoing commitment to do what it takes and its "least regrets" approach to ultimately succeed in driving the NZGB curve lower. Some further flattening is likely in coming weeks as global bond yields decline on the prospect of easier policy elsewhere too. In 2021, we expect the OCR to fall below zero. And as we approach that OCR cut in April, we would expect the NZGB curve to bull-steepen as short bonds gravitate towards the OCR, outperforming longer bonds. To be clear, we expect longer bond yields to fall – but for the magnitude of the fall to be less.

All up, the PREFU should come and go with little fanfare, and changes to the forecasts are likely to be immaterial compared to the degree of forecast uncertainty that surrounds them.

Other than providing a near-term distraction, the election doesn't change our view of how fiscal settings are likely to evolve at a macro level from here (regardless of what the Government looks like on the other side). There will come a time when the very expensive temporary support measures are withdrawn (or expire) and the Government's focus becomes more about facilitating the economic recovery than limiting the initial damage caused by lockdowns. But to really get bang for buck on the recovery front, virus risks will first need to be contained.

Then of course there are the politically charged questions of who will pay for all this, how, and when. That's a discussion that's going to continue well after the next electoral term expires, and it'll take some pretty brave politicians to tackle issues like NZ Super affordability, and other intergenerational inequality issues. Indeed, fiscal consolidation is a story for another day but a story that we think will be told eventually. And it'll be a ripping yarn with plenty of drama and some gripping battles.

Contact us

Meet the team

We welcome your questions and feedback. Click here for more information about our team.

Sharon Zollner
Chief Economist

Follow Sharon on Twitter
@sharon_zollner

Telephone: +64 27 664 3554
Email: sharon.zollner@anz.com

General enquiries:
research@anz.com

Follow ANZ Research
@ANZ_Research (global)

David Croy
Senior Strategist

Market developments, interest rates, FX, unconventional monetary policy, liaison with market participants.

Telephone: +64 27 432 2769
Email: david.croy@anz.com

Susan Kilsby
Agricultural Economist

Primary industry developments and outlook, structural change and regulation, liaison with industry.

Telephone: +64 21 633 469
Email: susan.kilsby@anz.com

Liz Kendall
Senior Economist

Research co-ordinator, publication strategy, property market analysis, monetary and prudential policy.

Telephone: +64 27 240 9969
Email: elizabeth.kendall@anz.com

Miles Workman
Senior Economist

Macroeconomic forecast co-ordinator, fiscal policy, economic risk assessment and credit developments.

Telephone: +64 21 661 792
Email: miles.workman@anz.com

Kyle Uerata
Economic Statistician

Economic statistics, ANZ proprietary data (including ANZ Business Outlook), data capability and infrastructure.

Telephone: +64 21 633 894
Email: kyle.uerata@anz.com

Natalie Denne
PA / Desktop Publisher

Business management, general enquiries, mailing lists, publications, chief economist's diary.

Telephone: +64 21 253 6808
Email: natalie.denne@anz.com

Important notice

This document is intended for ANZ's Institutional, Markets and Private Banking clients. It should not be forwarded, copied or distributed. The information in this document is general in nature, and does not constitute personal financial product advice or take into account your objectives, financial situation or needs.

This document may be restricted by law in certain jurisdictions. Persons who receive this document must inform themselves about and observe all relevant restrictions.

Disclaimer for all jurisdictions: This document is prepared and distributed in your country/region by either: Australia and New Zealand Banking Group Limited (ABN11 005 357 522) (**ANZ**); or its relevant subsidiary or branch (each, an **Affiliate**), as appropriate or as set out below.

This document is distributed on the basis that it is only for the information of the specified recipient or permitted user of the relevant website (**recipients**).

This document is solely for informational purposes and nothing contained within is intended to be an invitation, solicitation or offer by ANZ to sell, or buy, receive or provide any product or service, or to participate in a particular trading strategy.

Distribution of this document to you is only as may be permissible by the laws of your jurisdiction, and is not directed to or intended for distribution or use by recipients resident or located in jurisdictions where its use or distribution would be contrary to those laws or regulations, or in jurisdictions where ANZ would be subject to additional licensing or registration requirements. Further, the products and services mentioned in this document may not be available in all countries.

ANZ in no way provides any financial, legal, taxation or investment advice to you in connection with any product or service discussed in this document. Before making any investment decision, recipients should seek independent financial, legal, tax and other relevant advice having regard to their particular circumstances.

Whilst care has been taken in the preparation of this document and the information contained within is believed to be accurate, ANZ does not represent or warrant the accuracy or completeness of the information Further, ANZ does not accept any responsibility to inform you of any matter that subsequently comes to its notice, which may affect the accuracy of the information in this document.

Preparation of this document and the opinions expressed in it may involve material elements of subjective judgement and analysis. Unless specifically stated otherwise: they are current on the date of this document and are subject to change without notice; and, all price information is indicative only. Any opinions expressed in this document are subject to change at any time without notice.

ANZ does not guarantee the performance of any product mentioned in this document. All investments entail a risk and may result in both profits and losses. Past performance is not necessarily an indicator of future performance. The products and services described in this document may not be suitable for all investors, and transacting in these products or services may be considered risky.

ANZ expressly disclaims any responsibility and shall not be liable for any loss, damage, claim, liability, proceedings, cost or expense (Liability) arising directly or indirectly and whether in tort (including negligence), contract, equity or otherwise out of or in connection with this document to the extent permissible under relevant law. Please note, the contents of this document have not been reviewed by any regulatory body or authority in any jurisdiction.

ANZ and its Affiliates may have an interest in the subject matter of this document. They may receive fees from customers for dealing in the products or services described in this document, and their staff and introducers of business may share in such fees or remuneration that may be influenced by total sales, at all times received and/or apportioned in accordance with local regulatory requirements. Further, they or their customers may have or have had interests or long or short positions in the products or services described in this document, and may at any time make purchases and/or sales in them as principal or agent, as well as act (or have acted) as a market maker in such products. This document is published in accordance with ANZ's policies on conflicts of interest and ANZ maintains appropriate information barriers to control the flow of information between businesses within it and its Affiliates.

Your ANZ point of contact can assist with any questions about this document including for further information on these disclosures of interest.

Country/region specific information: Unless stated otherwise, this document is distributed by Australia and New Zealand Banking Group Limited (**ANZ**).

Australia. ANZ holds an Australian Financial Services licence no. 234527. For a copy of ANZ's Financial Services Guide please click here or request from your ANZ point of contact.

Brazil, Brunei, India, Japan, Kuwait, Malaysia, Switzerland, Taiwan. This document is distributed in each of these jurisdictions by ANZ on a cross-border basis.

Cambodia. This document is distributed in Cambodia by ANZ Royal Bank (Cambodia) Limited (**ANZ Royal Bank**). The recipient acknowledges that although ANZ Royal Bank is a subsidiary of ANZ, it is a separate entity to ANZ and the obligations of ANZ Royal Bank do not constitute deposits or other liabilities of ANZ and ANZ is not required to meet the obligations of ANZ Royal Bank.

European Economic Area (EEA): ***United Kingdom.*** ANZ is authorised in the United Kingdom by the Prudential Regulation Authority (**PRA**) and is subject to regulation by the Financial Conduct Authority (**FCA**) and limited regulation by the PRA. Details about the extent of our regulation by the PRA are available from us on request. This document is distributed in the United Kingdom by Australia and New Zealand Banking Group Limited ANZ solely for the information of persons who would come within the FCA definition of "eligible counterparty" or "professional client". It is not intended for and must not be distributed to any person who would come within the FCA definition of "retail client". Nothing here excludes or restricts any duty or liability to a customer which ANZ may have under the UK Financial Services and Markets Act 2000 or under the regulatory system as defined in the Rules of the Prudential Regulation Authority (**PRA**) and the FCA. ANZ is authorised in the United Kingdom by the PRA and is subject to regulation by the FCA and limited regulation by the PRA. Details about the extent of our regulation by the PRA are available from us on request.

Fiji. For Fiji regulatory purposes, this document and any views and recommendations are not to be deemed as investment advice. Fiji investors must seek licensed professional advice should they wish to make any investment in relation to this document.

Hong Kong. This publication is issued or distributed in Hong Kong by the Hong Kong branch of ANZ, which is registered at the Hong Kong Monetary Authority to conduct Type 1 (dealing in securities), Type 4 (advising on securities) and Type 6 (advising on corporate finance) regulated activities. The contents of this publication have not been reviewed by any regulatory authority in Hong Kong.

India. If this document is received in India, only you (the specified recipient) may print it provided that before doing so, you specify on it your name and place of printing.

Myanmar. This publication is intended to be general and part of ANZ's customer service and marketing activities when implementing its functions as a licensed bank. This publication is not Securities Investment Advice (as that term is defined in the Myanmar Securities Transaction Law 2013).

Important notice

New Zealand. This document is intended to be of a general nature, does not take into account your financial situation or goals, and is not a personalised adviser service under the Financial Advisers Act 2008 (**FAA**).

Oman. ANZ neither has a registered business presence nor a representative office in Oman and does not undertake banking business or provide financial services in Oman. Consequently ANZ is not regulated by either the Central Bank of Oman or Oman's Capital Market Authority. The information contained in this document is for discussion purposes only and neither constitutes an offer of securities in Oman as contemplated by the Commercial Companies Law of Oman (Royal Decree 4/74) or the Capital Market Law of Oman (Royal Decree 80/98), nor does it constitute an offer to sell, or the solicitation of any offer to buy non-Omani securities in Oman as contemplated by Article 139 of the Executive Regulations to the Capital Market Law (issued vide CMA Decision 1/2009). ANZ does not solicit business in Oman and the only circumstances in which ANZ sends information or material describing financial products or financial services to recipients in Oman, is where such information or material has been requested from ANZ and the recipient understands, acknowledges and agrees that this document has not been approved by the CBO, the CMA or any other regulatory body or authority in Oman. ANZ does not market, offer, sell or distribute any financial or investment products or services in Oman and no subscription to any securities, products or financial services may or will be consummated within Oman. Nothing contained in this document is intended to constitute Omani investment, legal, tax, accounting or other professional advice.

People's Republic of China (PRC). This document may be distributed by either ANZ or Australia and New Zealand Bank (China) Company Limited (**ANZ China**). Recipients must comply with all applicable laws and regulations of PRC, including any prohibitions on speculative transactions and CNY/CNH arbitrage trading. If this document is distributed by ANZ or an Affiliate (other than ANZ China), the following statement and the text below is applicable: No action has been taken by ANZ or any affiliate which would permit a public offering of any products or services of such an entity or distribution or re-distribution of this document in the PRC. Accordingly, the products and services of such entities are not being offered or sold within the PRC by means of this document or any other document. This document may not be distributed, re-distributed or published in the PRC, except under circumstances that will result in compliance with any applicable laws and regulations. If and when the material accompanying this document relates to the products and/or services of ANZ China, the following statement and the text below is applicable: This document is distributed by ANZ China in the Mainland of the PRC.

Qatar. This document has not been, and will not be:

- lodged or registered with, or reviewed or approved by, the Qatar Central Bank (**QCB**), the Qatar Financial Centre (**QFC**) Authority, QFC Regulatory Authority or any other authority in the State of Qatar (**Qatar**); or
- authorised or licensed for distribution in Qatar,

and the information contained in this document does not, and is not intended to, constitute a public offer or other invitation in respect of securities in Qatar or the QFC. The financial products or services described in this document have not been, and will not be:

- registered with the QCB, QFC Authority, QFC Regulatory Authority or any other governmental authority in Qatar; or
- authorised or licensed for offering, marketing, issue or sale, directly or indirectly, in Qatar.

Accordingly, the financial products or services described in this document are not being, and will not be, offered, issued or sold in Qatar, and this document is not being, and will not be, distributed in Qatar. The offering, marketing, issue and sale of the financial products or services described in this document and distribution of this document is being made in, and is subject to the laws, regulations and rules of, jurisdictions outside of Qatar and the QFC. Recipients of this document must abide by this restriction and not distribute this document in breach of this restriction. This document is being sent/issued to a limited number of institutional and/or sophisticated investors (i) upon their request and confirmation that they understand the statements above; and (ii) on the condition that it will not be provided to any person other than the original recipient, and is not for general circulation and may not be reproduced or used for any other purpose.

Singapore. This document is distributed in Singapore by the Singapore branch of ANZ solely for the information of "accredited investors", "expert investors" or (as the case may be) "institutional investors" (each term as defined in the Securities and Futures Act Cap. 289 of Singapore). ANZ is licensed in Singapore under the Banking Act Cap. 19 of Singapore and is exempted from holding a financial adviser's licence under Section 23(1)(a) of the Financial Advisers Act Cap. 100 of Singapore.

United Arab Emirates (UAE). This document is distributed in the UAE or the Dubai International Financial Centre (**DIFC**) (as applicable) by ANZ. This document does not, and is not intended to constitute: (a) an offer of securities anywhere in the UAE; (b) the carrying on or engagement in banking, financial and/or investment consultation business in the UAE under the rules and regulations made by the Central Bank of the UAE, the Emirates Securities and Commodities Authority or the UAE Ministry of Economy; (c) an offer of securities within the meaning of the Dubai International Financial Centre Markets Law (DIFCML) No. 12 of 2004; and (d) a financial promotion, as defined under the DIFCML No. 1 of 200. ANZ DIFC Branch is regulated by the Dubai Financial Services Authority (**DFSA**) ANZ DIFC Branch is regulated by the Dubai Financial Services Authority (**DFSA**). The financial products or services described in this document are only available to persons who qualify as "Professional Clients" or "Market Counterparty" in accordance with the provisions of the DFSA rules.

United States. Except where this is a FX- related document, this document is distributed in the United States by ANZ Securities, Inc. (**ANZ SI**) which is a member of the Financial Regulatory Authority (**FINRA**) (www.finra.org) and registered with the SEC. ANZSI's address is 277 Park Avenue, 31st Floor, New York, NY 10172, USA (Tel: +1 212 801 9160 Fax: +1 212 801 9163). ANZSI accepts responsibility for its content. Information on any securities referred to in this document may be obtained from ANZSI upon request. This document or material is intended for institutional use only – not retail. If you are an institutional customer wishing to effect transactions in any securities referred to in this document you must contact ANZSI, not its affiliates. ANZSI is authorised as a broker-dealer only for institutional customers, not for US Persons (as "US person" is defined in Regulation S under the US Securities Act of 1933, as amended) who are individuals. If you have registered to use this website or have otherwise received this document and are a US Person who is an individual: to avoid loss, you should cease to use this website by unsubscribing or should notify the sender and you should not act on the contents of this document in any way. Non-U.S. analysts: Non-U.S. analysts may not be associated persons of ANZSI and therefore may not be subject to FINRA Rule 2242 restrictions on communications with the subject company, public appearances and trading securities held by the analysts. Where this is an FX-related document, it is distributed in the United States by ANZ's New York Branch, which is also located at 277 Park Avenue, 31st Floor, New York, NY 10172, USA (Tel: +1 212 801 916 0 Fax: +1 212 801 9163).

Vietnam. This document is distributed in Vietnam by ANZ or ANZ Bank (Vietnam) Limited, a subsidiary of ANZ.

This document has been prepared by ANZ Bank New Zealand Limited, Level 26, 23-29 Albert Street, Auckland 1010, New Zealand, Ph 64-9-357 4094, e-mail nzeconomics@anz.com, http://www.anz.co.nz