ANZ Research

NZ Insight: Coalition policy announcements

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Preliminary thoughts on the new Government's policy mix

Summary

- Coalition negotiations have resulted in a few policy tweaks versus the working assumptions underlying our Post-election Update note.
- Compared to National's fiscal plan, there is a little less revenue generation (no foreign buyers tax), but that's likely to be offset by deeper spending cuts.
- What we've seen today does not appear to be a game-changer for macroeconomic policy settings and therefore the RBNZ. But we think there is scope for deeper spending cuts in time.
- The proposed changes to the monetary policy framework were as anticipated, but at the margin may be seen as hawkish.
- The Treasury will incorporate today's announced policy mix into December's Half-Year Update, providing us with our first official estimate of what it all means.

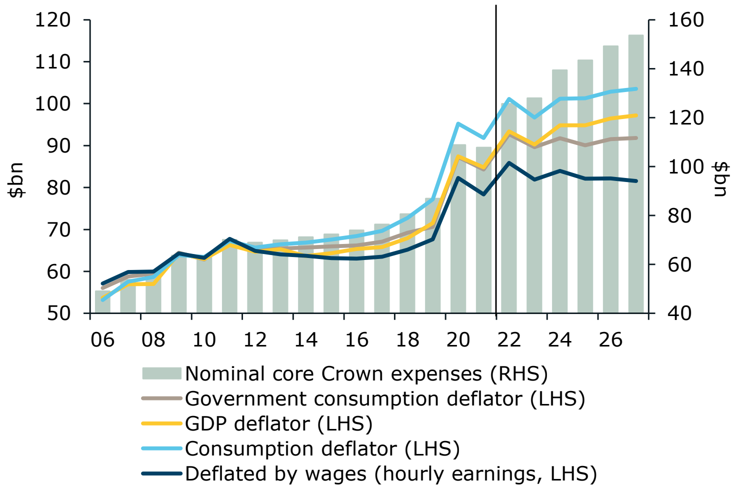
The coalition agreement between National, ACT and NZ First has yielded a slightly different policy mix than that signalled in National's fiscal plan. However, the changes do not appear to be game changers for the macroeconomic outlook compared to our previous understanding.

The next cab off the rank will be the Treasury's take on all this, which will be published in the upcoming Half-Year Update (date yet to be confirmed). We'll publish our Half-Year Update Preview after the monthly fiscal statements for the four months to October have been released (5 December). This will attempt to incorporate the fiscal staring point, potential tweaks to the Treasury's economic outlook, and signalled policy changes, arriving at a view of what it all means for NZDM's bond issuance guidance. This note just briefly discusses some of the economic impacts and risks to fiscal settings associated with today's announcements.

For context, as we discussed in this Insight, despite the economy becoming extremely capacity constrained, the previous Government opted to maintain a significantly larger Government sector in the post-pandemic era, putting upward pressure on both inflation and interest rates. It really doesn't matter which deflator you use, the Pre-election Update forecast showed that after adjusting for rising costs, government spending was still projected to be $15-$20bn higher per year in the Pre-election Update forecast compared to 2019 (pre-pandemic) (figure 1, over).

National's fiscal plan, by comparison, signalled spending cuts to the tune of around $8bn over four years – peanuts compared to previous increases. Therefore, it would not be a surprise to see deeper spending cuts in time. However, this may not be a story for the upcoming Half-Year Update, as it could take time for Ministers to work out where deeper cuts could be made. Budget 2024, with its usual back and forth between departments and Ministers, could be a likelier candidate for signalling larger spending cuts (if there is political appetite).

Figure 1. Estimates of real Govt spending.



Source: The Treasury, ANZ Research

We won't attempt to quantify the macroeconomic impacts of any policies announced today, with many still needing to be fleshed out. But for starters, let's split them into developments that could be perceived as 'hawkish' or 'dovish' for the monetary policy outlook, and then chuck in some other notable policy changes for completeness.

Policies that could be seen as 'hawkish'

Here we include policy changes that could be interpreted by the market as making the RBNZ more likely to respond in a more aggressive fashion to inflation being above the band, either now or in the future. Note, however, that most of these changes were well anticipated, limiting the likely market reaction.

- **Amend the RBNZ Act to remove "supporting maximum sustainable employment" from the RBNZ's economic objectives.** This was well signalled and anticipated, with the only new information being confirmation that they will bring about the change via changing the Act and not just watering down the employment mention in the Remit. In our view, this addition has not made any meaningful difference to policy settings in the time it has been in there. It's essentially a different lens on the same job, and it is more likely to change the RBNZ's communications than its monetary policy decisions. But to the extent that as unemployment rises there could be a *perceived* tension between "supporting maximum sustainable employment" and fighting inflation, removing it does arguably slightly smooth the path for holding rates high for longer if the RBNZ deems it appropriate.

- **Take advice on introducing specific time targets for returning inflation to target.** It seems unlikely that the Treasury would advise eliminating the useful flexibility provided by the current "medium term" terminology.

- **Take advice on removing the Treasury observer at the Monetary Policy Committee, and returning to a single decision maker.** It's not clear what advantages these changes would bring about, but they should be seen in the context of the suite of changes aimed at increasing the sole focus on inflation stability. If the committee is disbanded, markets are possibly more likely to play the man than the ball when it comes to monetary policy.

- **Restore interest deductibility for residential property investors more quickly than indicated.** National's initial plan was 50% this year and next, 75% in 2025/26, and back to 100% in 2026/27. The new, faster plan is a 60% deduction in 2023/24, 80% in 2024/25, and 100% in 2025/26. All else equal, this increases the value of an investment property immediately. On the other hand, it might take a bit of heat out of rents, to the extent that landlords have been attempting to claw back their higher net expenses. Win some, lose some for the RBNZ.
- **Income tax cuts.** As expected, at first glance. "Tax relief will be progressed as set out in National's Tax Plan, but will not include a repeal of the foreign buyer's residential property ban, with income tax reductions coming into force from 1 July 2024." National says its "tax package will continue to be funded through a combination of spending reprioritisation and additional revenue measures," along with policy changes that "will help offset the loss of revenue from that change".
- **$1.2bn Regional Infrastructure Fund**, analogous to the Provincial Growth Fund, to be administered by NZ First's Shane Jones.
- **Infrastructure: 13 new roads of national significance** to go ahead. But this will be offset by stopping spending on other infrastructure such as the Auckland light rail project. Given very long lead times for this kind of spending, let's hope some stability and predictability is achieved via the new National Infrastructure Agency – chopping and changing is enormously costly. "Institute long-term city and regional infrastructure deals, allowing PPPs, tolling and value capture rating to fund infrastructure."
- **Rewrite the Credit Contracts and Consumer Finance Act** "to protect vulnerable consumers without unnecessarily limiting access to credit." All else equal this represents an easing of credit conditions, though it's impossible to quantify at this stage. Prior reform of the Act means a lot of the initial impact on credit availability has already unwound.
- **Migration:** there doesn't appear to be any discomfort with the number of immigrants entering the country, though NZ First has a number of requirements aimed at ensuring the mix of migrants better meets New Zealand's needs. Migration policy changes include more RSE workers, a 5-year renewable parent visa, removal of median wage requirements from the skilled migrant category visa, and making it easier for family members of visa holders to work in NZ. Insofar as the RBNZ estimates that net migration on balance has a "low positive" impact on inflation (with demand-side impacts slightly outweighing the disinflationary impacts on wages), on balance these changes belong in the hawkish category.

Developments that could be seen as 'dovish'

Here we list announced policies that all else equal could (or at least might be perceived to) contribute to less contractionary monetary policy than otherwise.

- **The end of National's plan to allow foreign buyers back into the housing market.** It was very unclear what impact this change would have had, but it's fair to say a potential upside risk for house price inflation has been removed. In addition, this policy was meant to fund income tax cuts to the tune of around $700m per year, so spending cuts may need to be a little deeper than signalled. There is certainly scope to cut spending by more; the hard part will be reviewing existing baselines to find it.

- **Cuts to core public service employment:** This remains unquantified: "expenditure reduction targets to be set for each agency, informed by the increase in back office head count at that agency since 2017." This theme was well anticipated and it's hard to say if this is over and above the spending cuts National's plan has already signalled.
- **Fair pay agreements regime to be repealed** "by Christmas 2023". It's not clear that these have had any meaningful impact on wage growth as yet. But perhaps at the margin an upside risk has been eliminated.
- **Expand 90-day trials** to all businesses, increasing the flexibility of the labour market.

Other policies

- **Replace fees-free first year tertiary education with fees-free third year.** This should reduce spending in time.
- **Drop National's plan to increase the retirement age beyond 65.** This is not a win for New Zealand, with the affordability of the current set-up highly questionable in the long run. When the necessary changes are finally made (either increasing/broadening the tax system to pay for an aging population and/or lifting eligibility for NZ Super), they will need to be sharper. But the change has no immediate implications.
- **Make the Medium Density Residential Standards (MDRS) optional** for councils and introduce financial incentives for councils to enable more housing.
- **Repeal the Clean Car Discount.** This will show up in the CPI but is too small to warrant inclusion in the "hawkish" list.
- As expected, **repeal Natural and Built Environment Act 2023 and the Spatial Planning Act 2023 by Christmas, and replace the RMA** "with new resource management laws premised on the enjoyment of property rights as a guiding principle."
- Work with Auckland Council to **implement congestion charging**. Sorry cost of living. But these things really work and can be offset by low-income subsidies.
- **Tenancy changes:** introduce no-reason 90-day tenancy terminations, reduce notice periods. This increases the attractiveness of residential investment property (by reducing risk), which is a small positive for house prices, all else equal, but on the other hand it might see more rental stock hit the market, if some properties are currently vacant, which could be a small negative for rents.
- **Agriculture**: various, including reviewing methane targets, reversing ban on live animal exports, ceasing implementation of new Significant Natural Areas, improving farm environment plans, enabling offsetting sequestration against on-farm emissions, liberalising genetic engineer laws, repealing NPS on Freshwater Management, stopping the review of the Emissions Trading Scheme. We have published a separate note on the agriculture sector changes.
- **Repeal ban on offshore oil & gas exploration.** It might well prove very difficult to entice explorers here to be honest.

- **Immediate stop-work** on three waters, Auckland light rail, Let's Get Wellington Moving, income insurance, industry transformation plans, Lake Onslow pumped hydro. Not much new news here.
- Investigate reopening **Marsden Point refinery**. One suspects they'll find it would be very expensive, but national fuel security issues are real and it's good to see a commitment to robust analysis of this issue.

All up, there's a lot to digest here. In the near term, as we have recently accounted for in our forecasts, it's all consistent with a slightly different compositional mix of economic activity going forward (ie a smaller government sector and a larger private sector), but not an obvious game changer for overall aggregate supply and demand and thus our estimates of inflation pressure and the outlook for interest rates. While there are a few small upside risks to demand in the near term (ie via housing and possibly even migration), these are offset by downside risks to government spending.

Longer term, getting infrastructure settings right is a big one for the longer-term productive capacity of the country. Infrastructure decisions need to be less political and more based on sound cost-benefit analysis. And they need to be locked in. Chopping and changing key infrastructure projects between Governments (or even within them, as we've seen recently) is very costly. Let's hope the Government's plan achieves the much-desired stability and predictability that will allow the sector to scale up with confidence regarding the pipeline, aiding delivery.

From a fiscal outlook perspective, today's agreements do not provide a lot of additional information around what it means for the operating balance and pressure on bond issuance. But we'll have more to say in our Half-Year Update Preview. Lastly, changes to the RBNZ's mandate are not a game changer, but at the margin may make the comms easier around holding rates high for longer, should the RBNZ deem that necessary.

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