



Challenges and Choices

Welfare Working Group Forum
9-10 June 2010
Paul Rodway, The Treasury

Roadmap

- Background on why we look at the fiscal position several decades ahead
- NZ's long-term fiscal future – challenges and choices
- NZ needs to debate about tradeoffs we face, what does govt do, what do individuals do



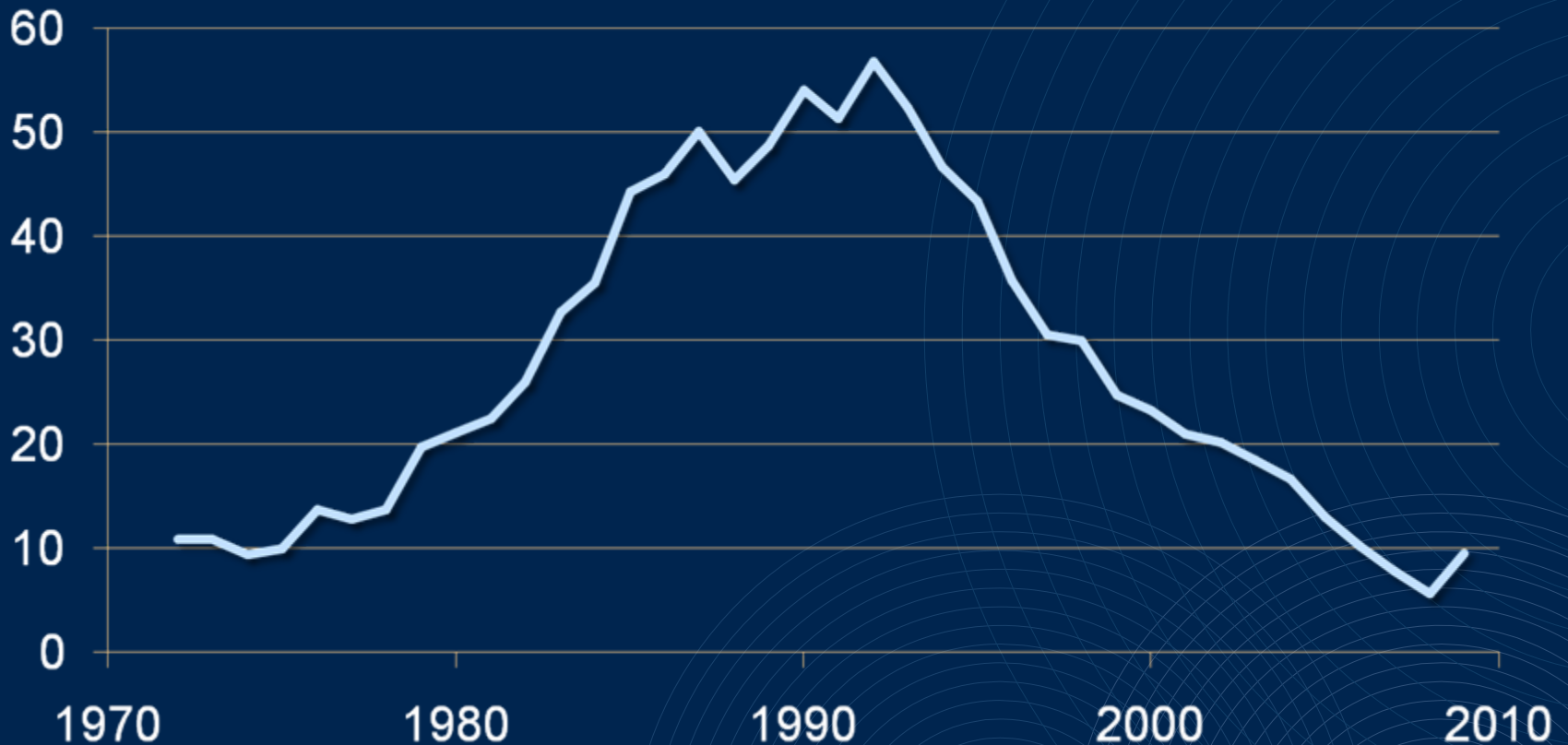
Fiscal context

- Public Finance Act (1989, amended 2004)
- Fiscal Responsibility Act (1994)
- Increasing forecast horizons
- Transparency and accountability basis



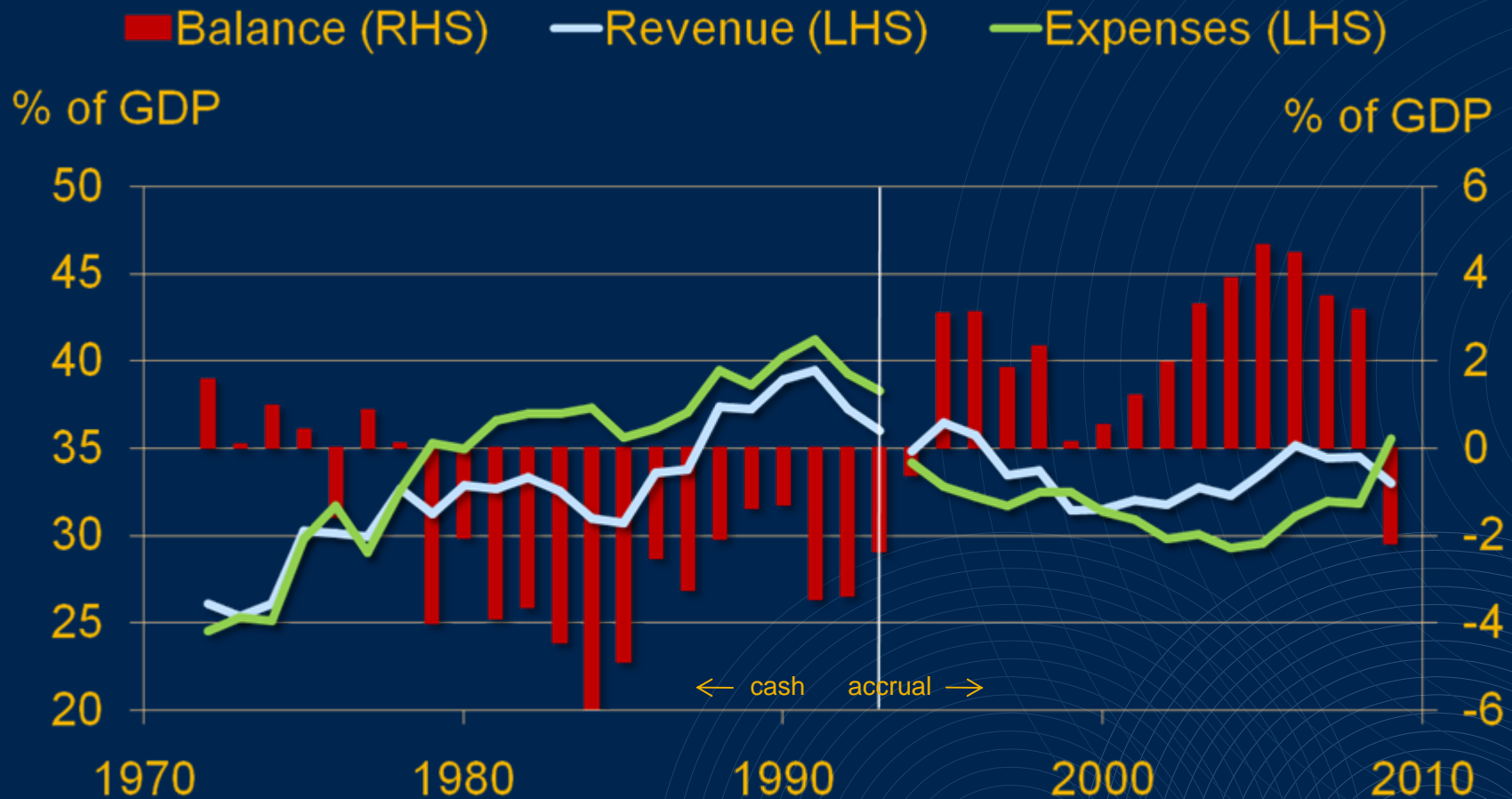
NZ's net public debt

% of GDP



Source: The Treasury

Revenue, expenses and the fiscal balance



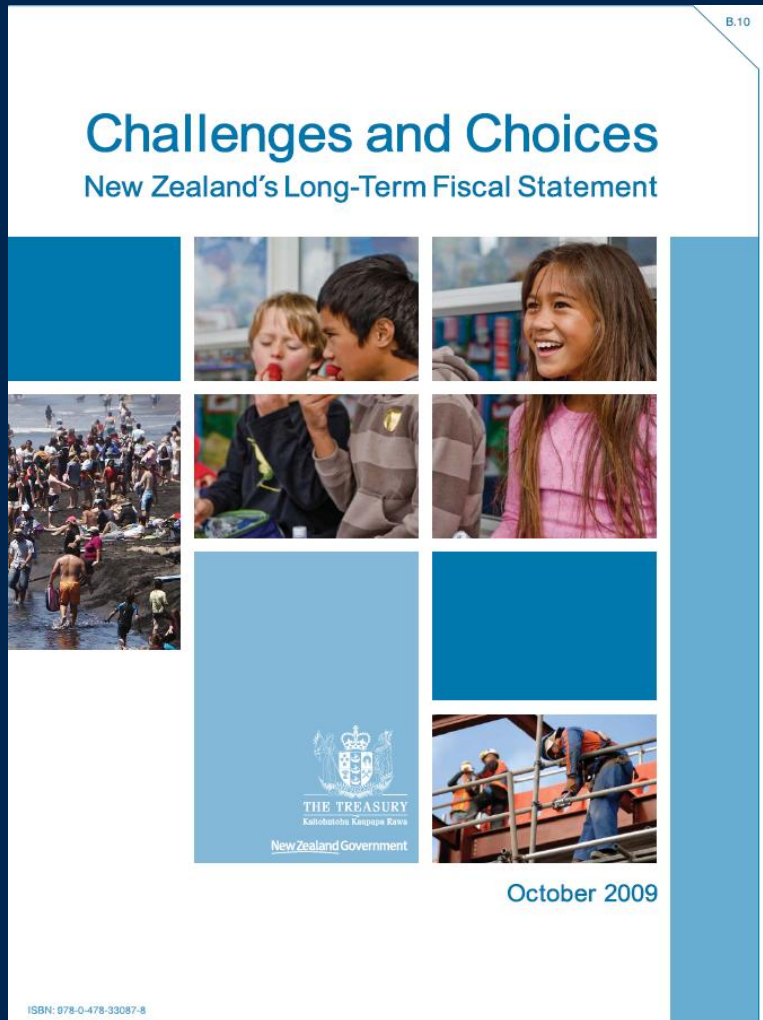
Source: The Treasury

Long-term fiscal reporting

- Explores future taxes, spending and government debt under current policy settings
- Done by most OECD countries
- Intergenerational implications



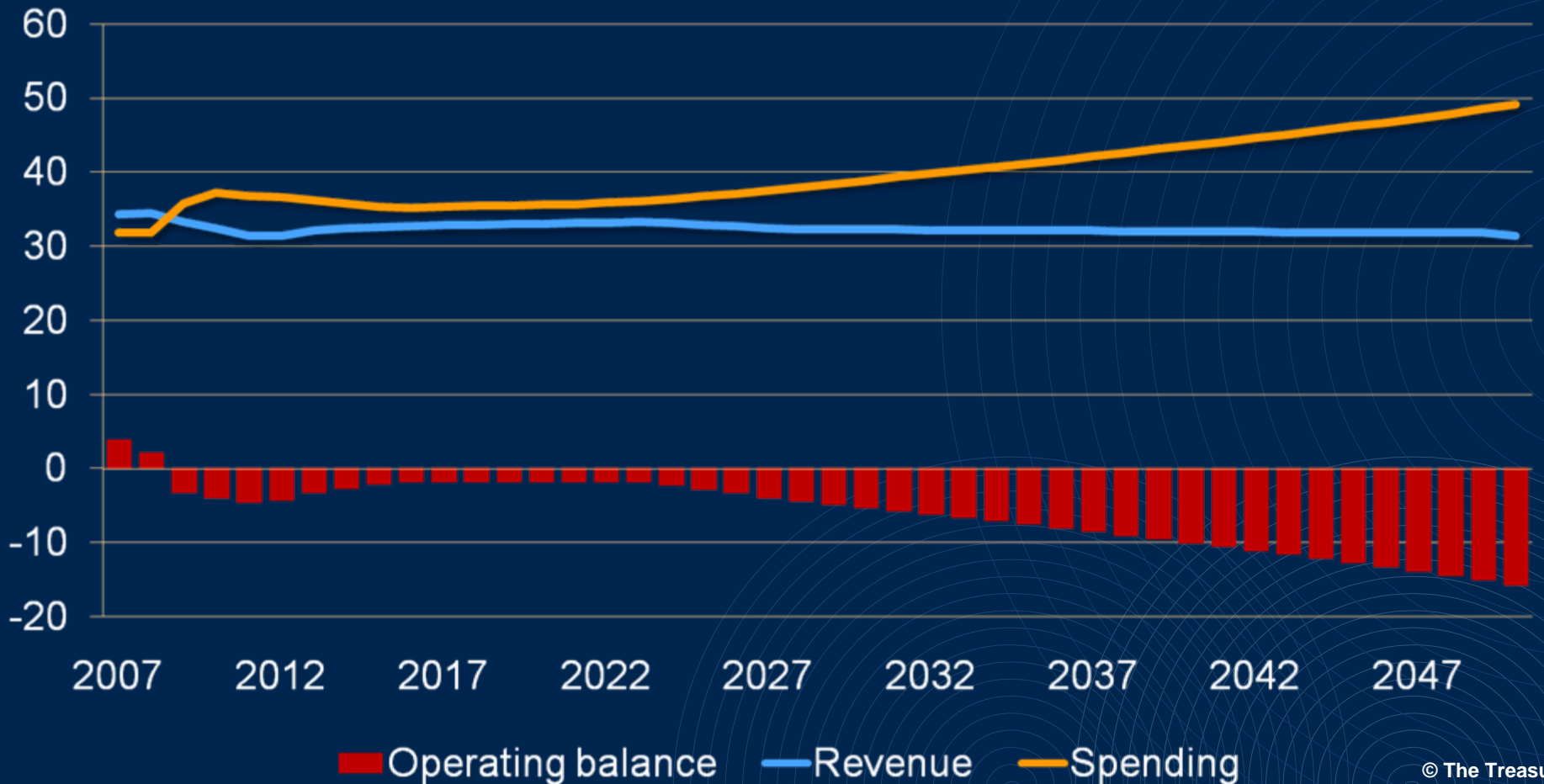
NZ's Long-Term Fiscal Statement



- Treasury must prepare every 4 years
- Look out 40 years
- Projection not forecast
- Seeks to generate discussion and debate
- Present policy options, not specific advice

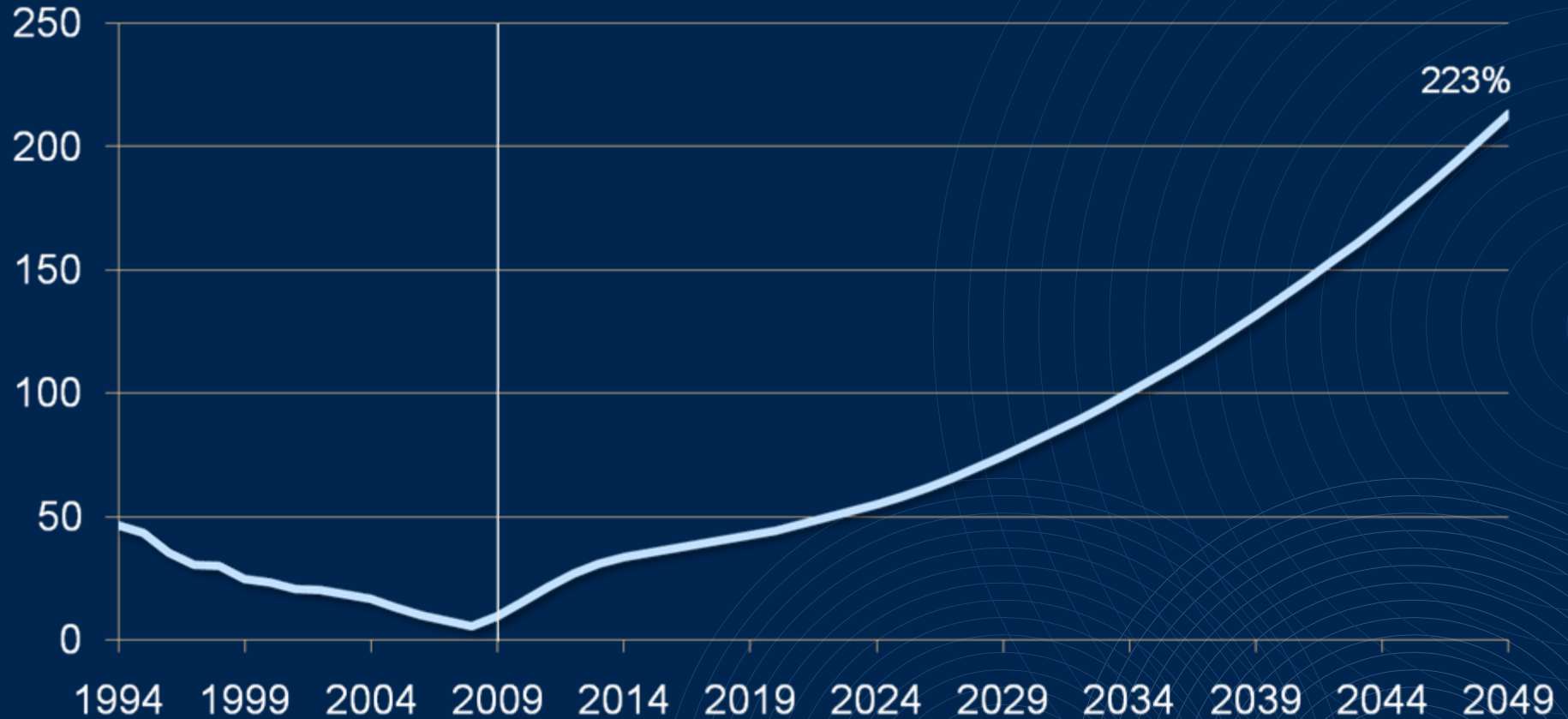
Historic trends projection – revenue, expenses and operating balance

% of GDP



Net public debt

% of GDP



Drivers of rising debt

- Future spending outstrips revenue
- Growth in spending is driven by:
 - Demographic change (ageing population)
 - Cost growth (links to real wage growth)
 - Demand for volume/scope increases
 - Compounding effects of increasing debt

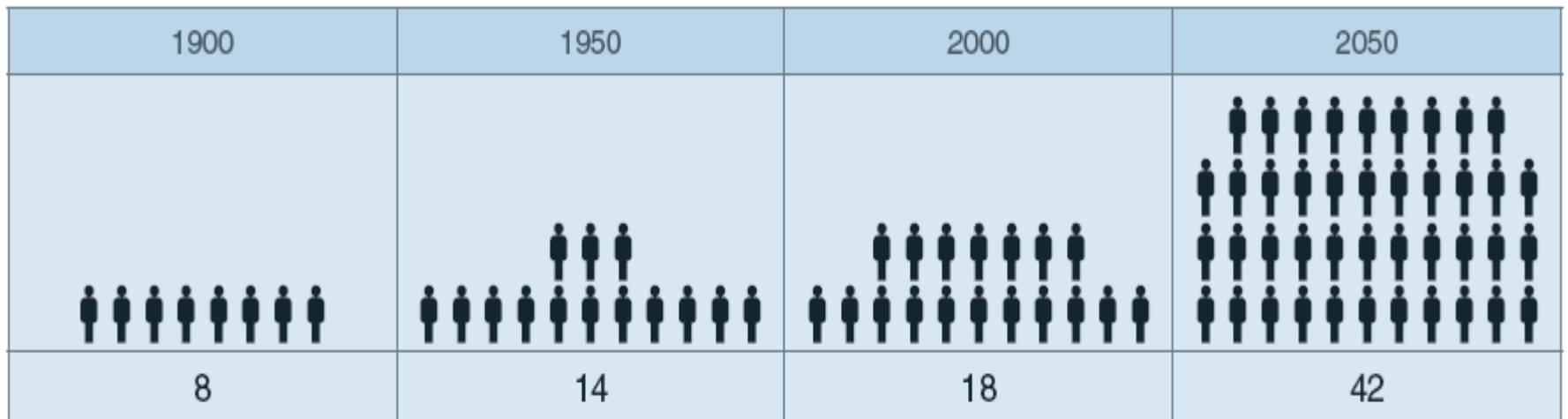


Demographic changes

- NZ facing a change to a permanently older population
- Longer lives, smaller families
- Baby boomers accelerate the transition

Ratio of over-65s to working age population doubles

People 65 and older for every 100 aged between 15 and 64



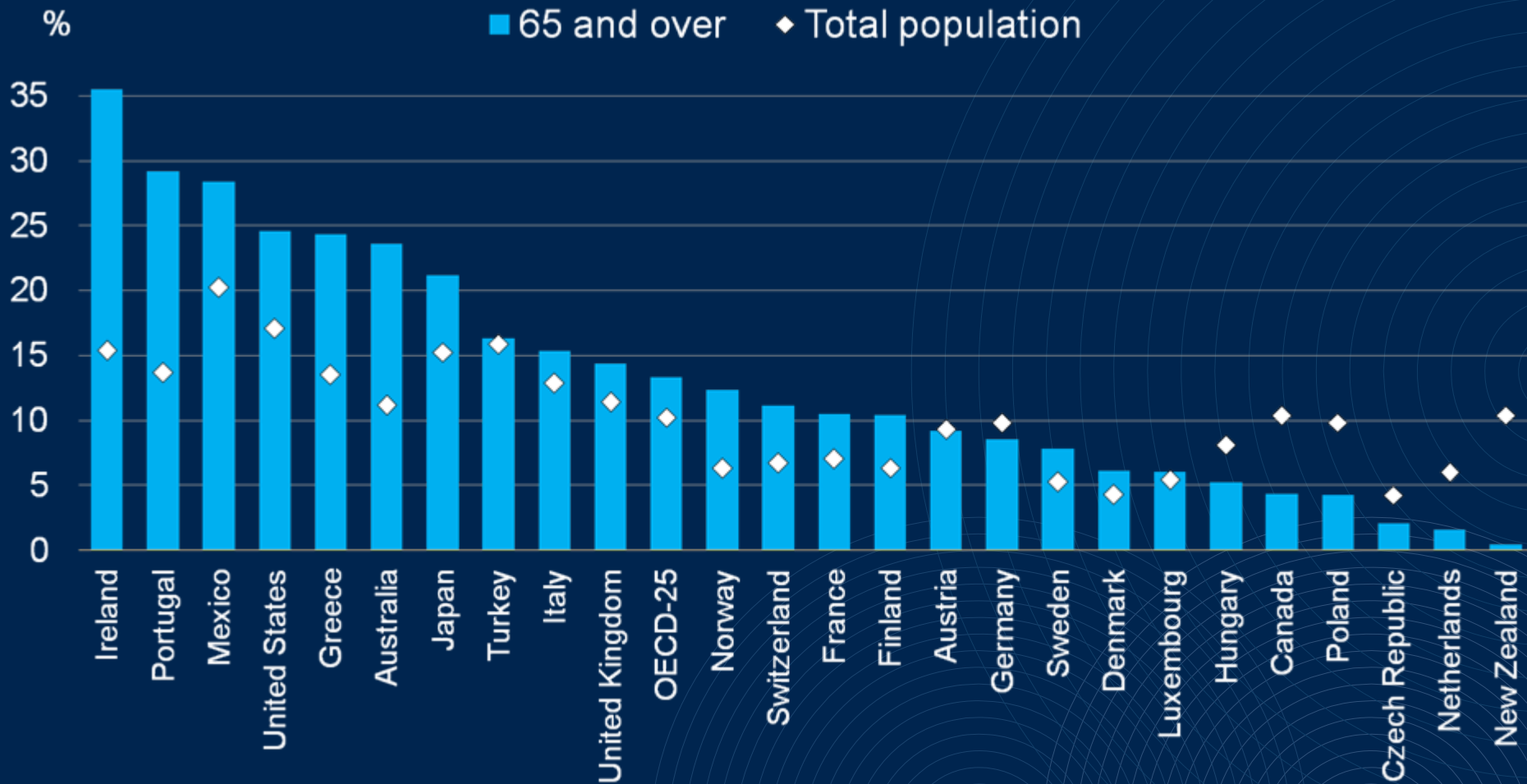
Superannuation

- 522,000 people receiving NZS now. This is projected to grow to 1.3 million in 2050
- Super is indexed to wages (and hence economic growth pushes up the cost)
- NZ's public pension system is unique in the OECD, particularly in its universality

Life expectancy and pension age

	1898	1977	1990	2009	2030	2050
Life expectancy	60	74	76	80	83	85
Pension age	65	60	60	65	65	65

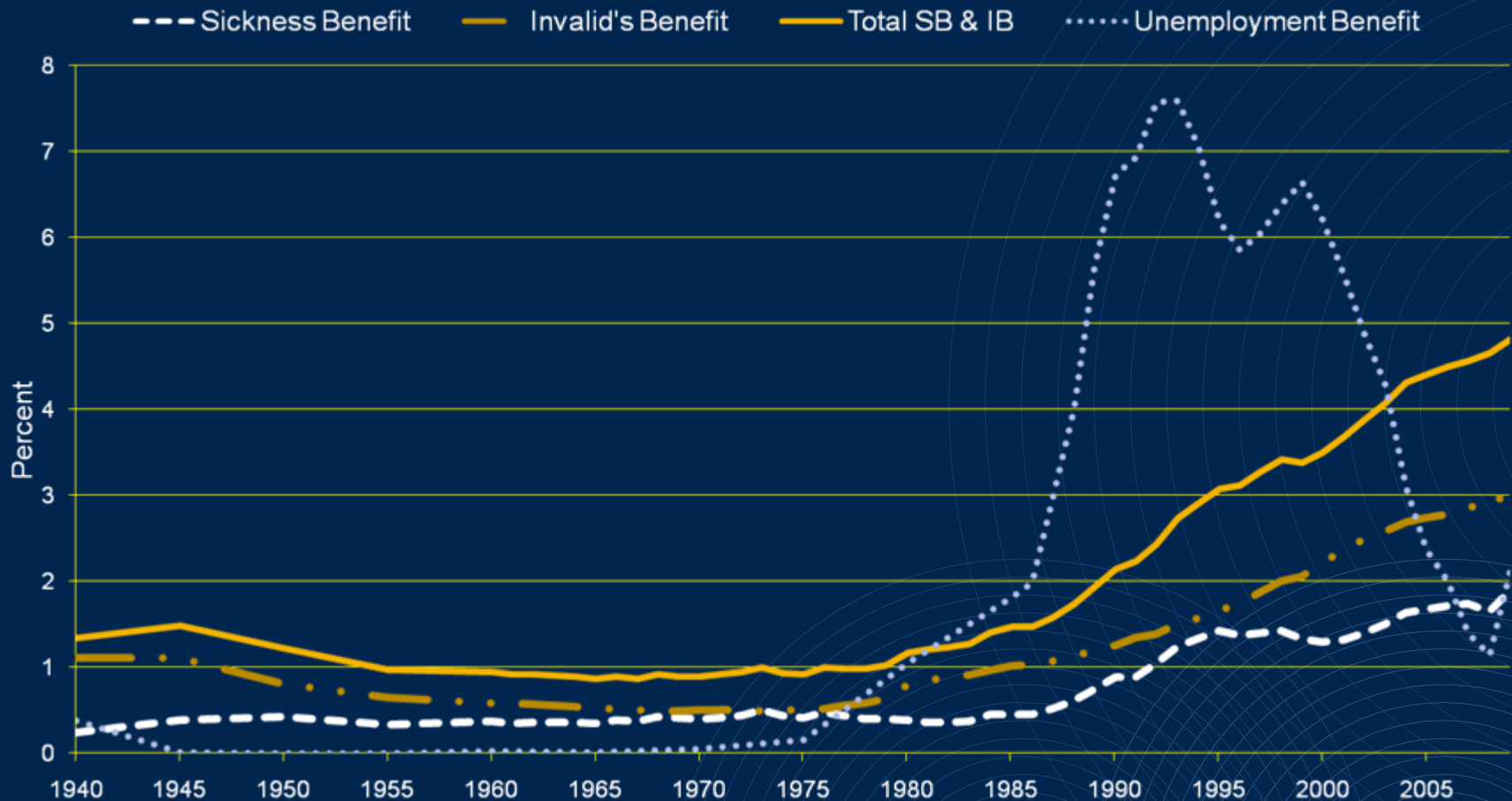
Poverty rates



Welfare benefits

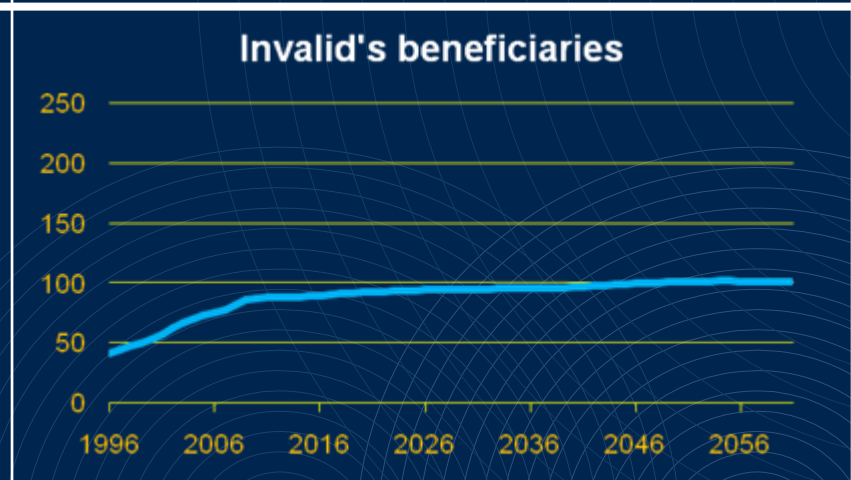
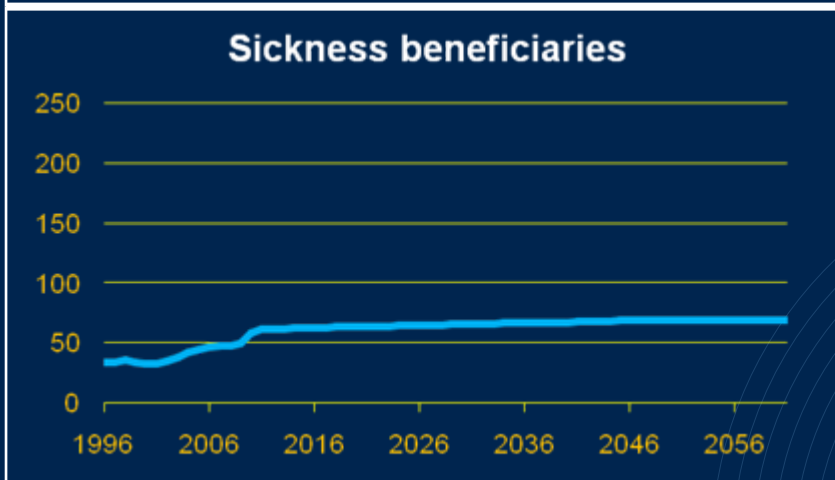
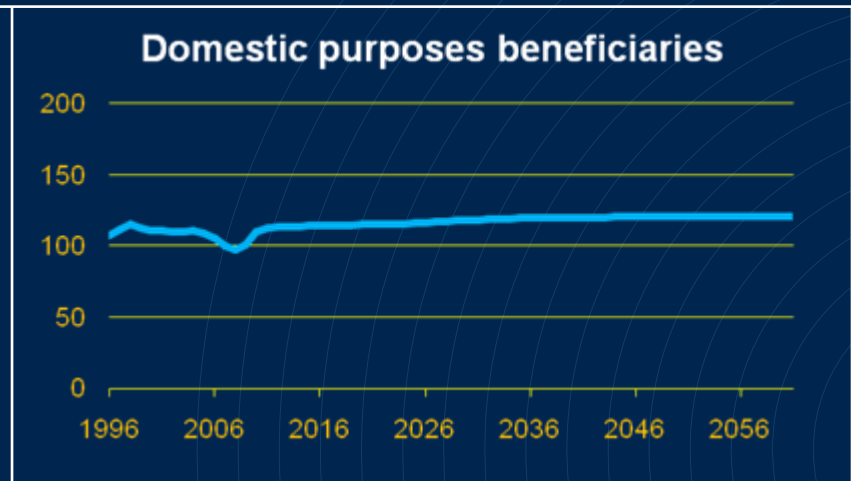
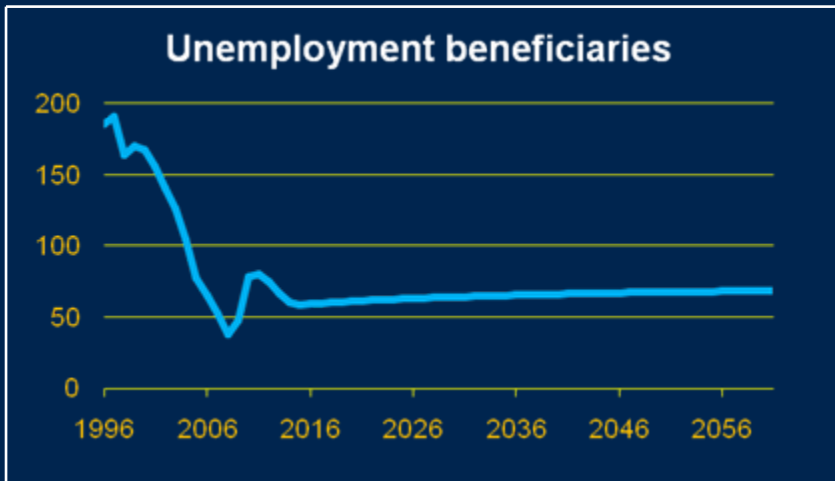
- Largest: UB, DPB, SB, IB, AS
- Income tested
- Grow by inflation - in history, in practice
- Assume fixed proportions of age groups
- Main cost drivers
 - Inflation indexing
 - Population growth and ageing

SB, IB, UB numbers (% pop 15-64)

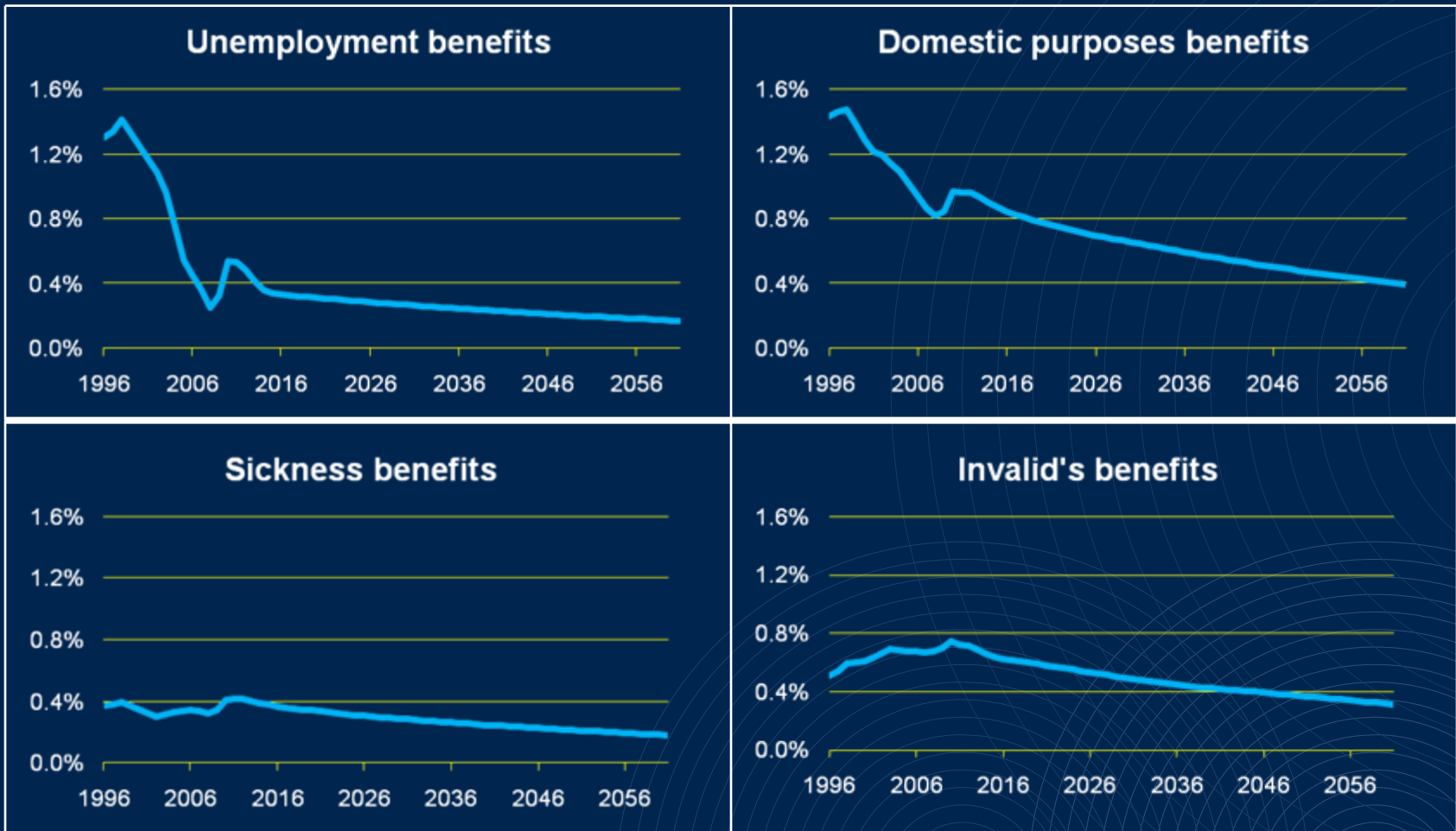


Source: MSD, 2009 Statistical Report and MSD, 'Key Facts' Statistics

Beneficiary numbers, thousands



Welfare costs as share of GDP



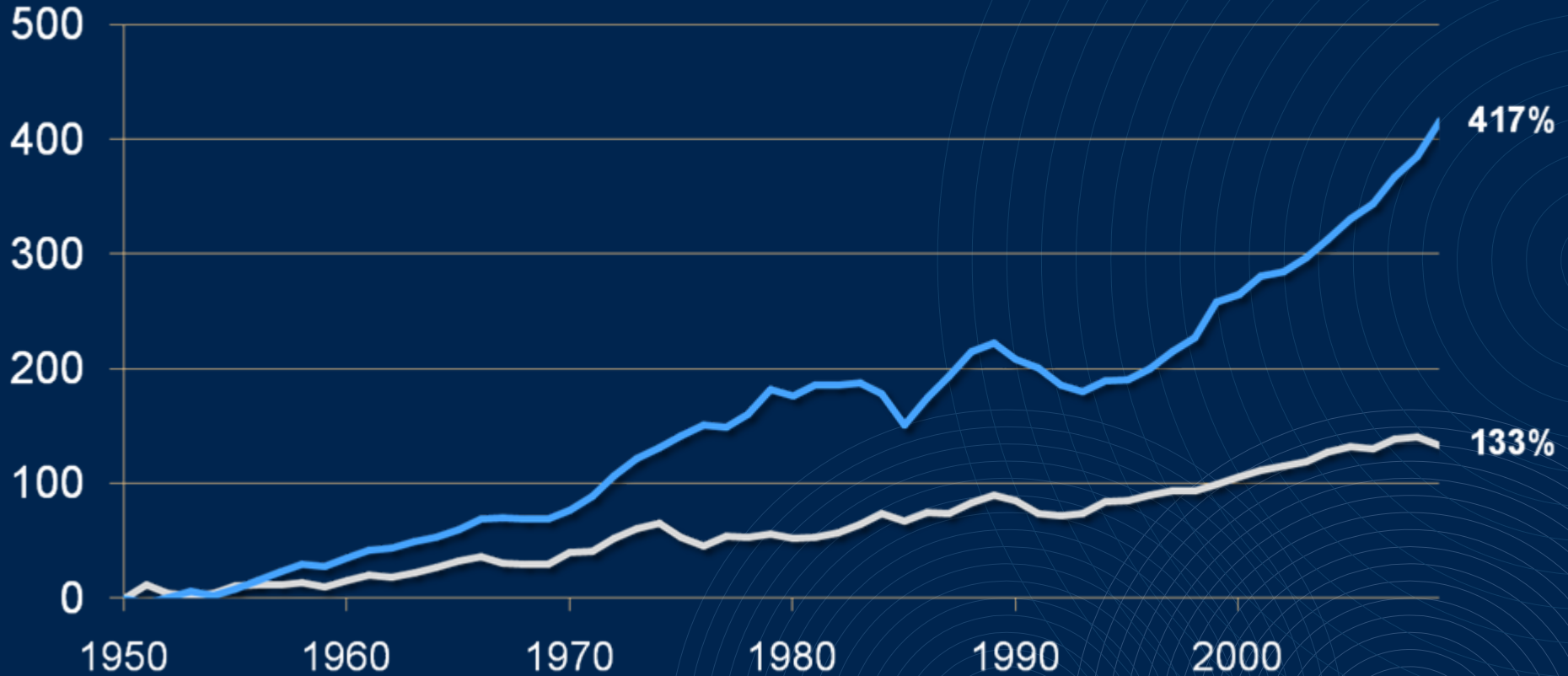
Health care

- Spending as a share of national income projected to increase by 50% by 2050
- Main drivers
 - Ageing
 - Income growth → demand
 - Technology

Health spending and income

Cumulative %
change

—GDP —Health

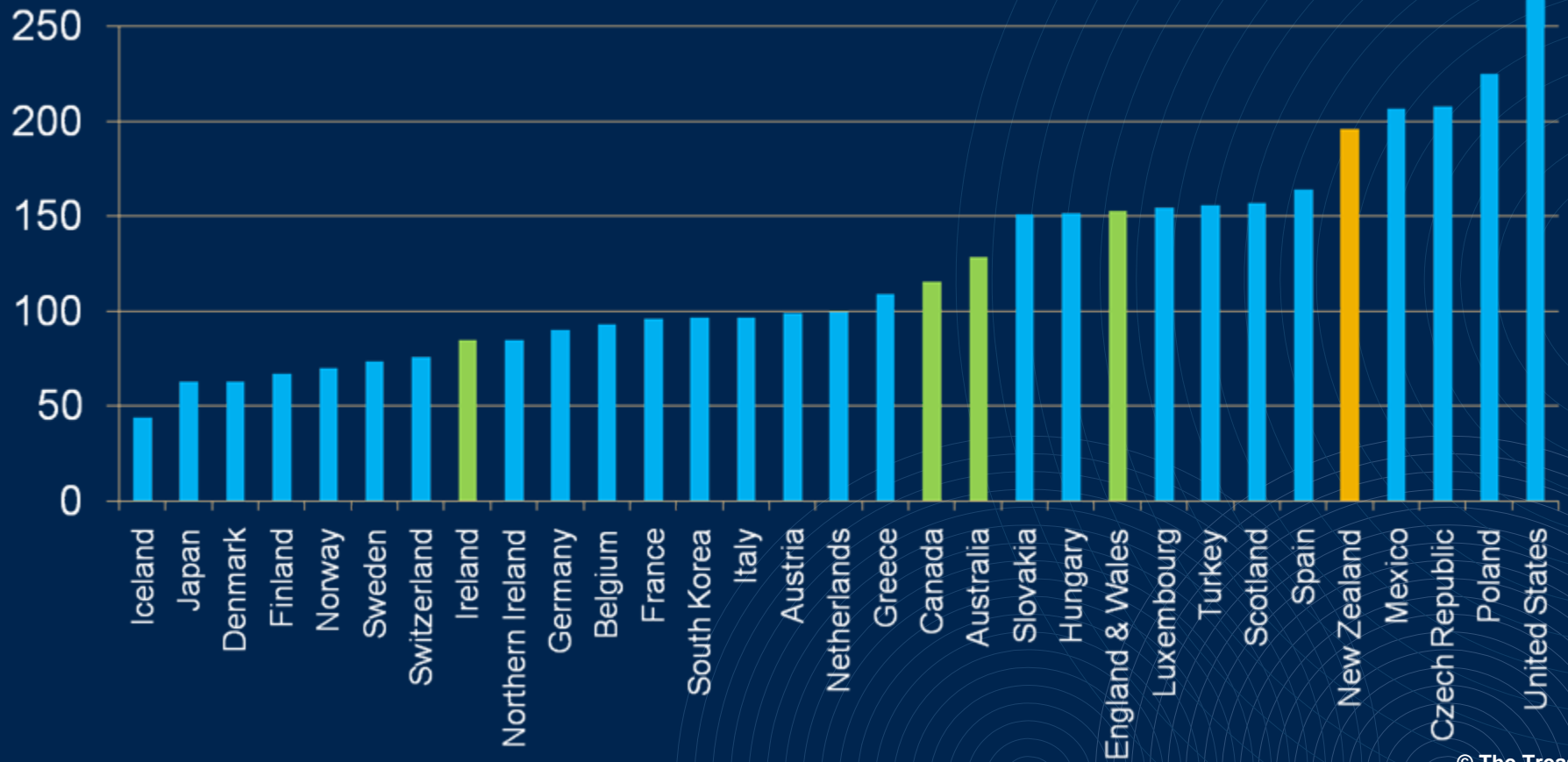


Justice

- Spending in the justice sector doubled from 1994 to 2009
- Recorded crime rates have been broadly stable over the same period
- Justice sector agencies form a "pipeline" in which policy in one part of the system can have a major impact on the other parts

Imprisonment rates

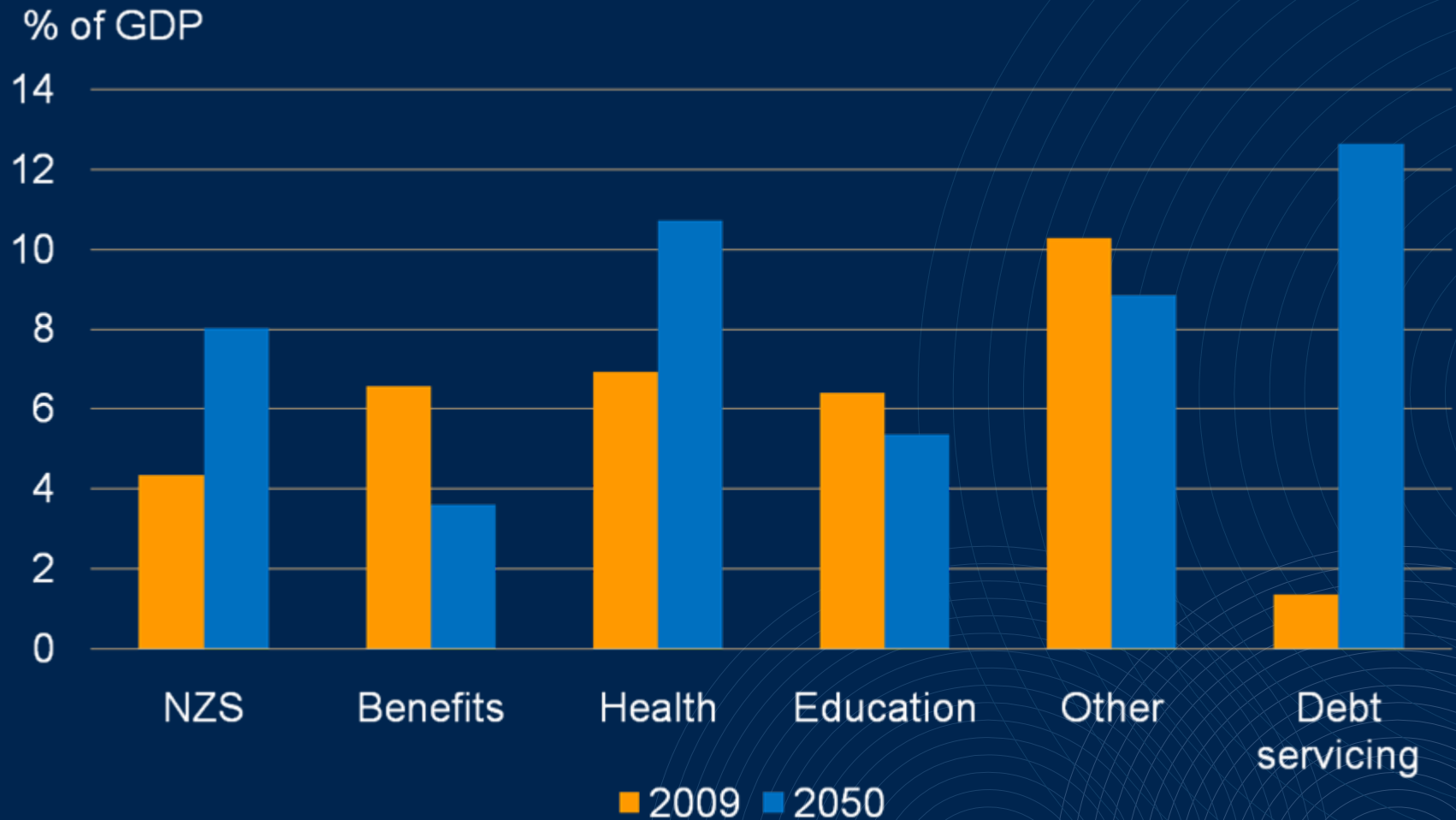
Per 100,000 of population



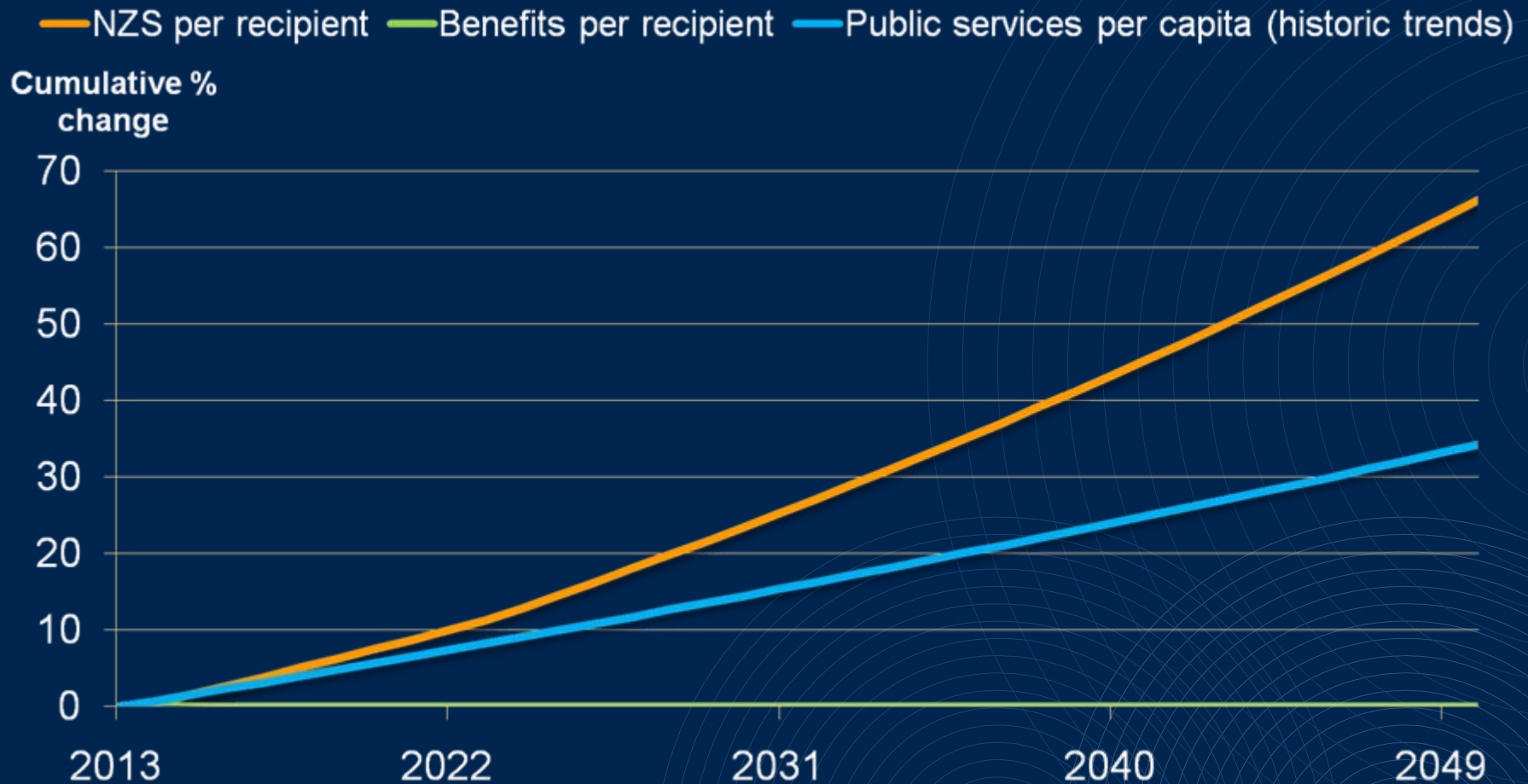
Costs of imprisonment

- It costs just over \$90,000 a year to keep a person in prison
- This compares with:
 - \$18,000/year for home detention
 - \$7,000/year for community detention

Spending changes



What the average NZer receives

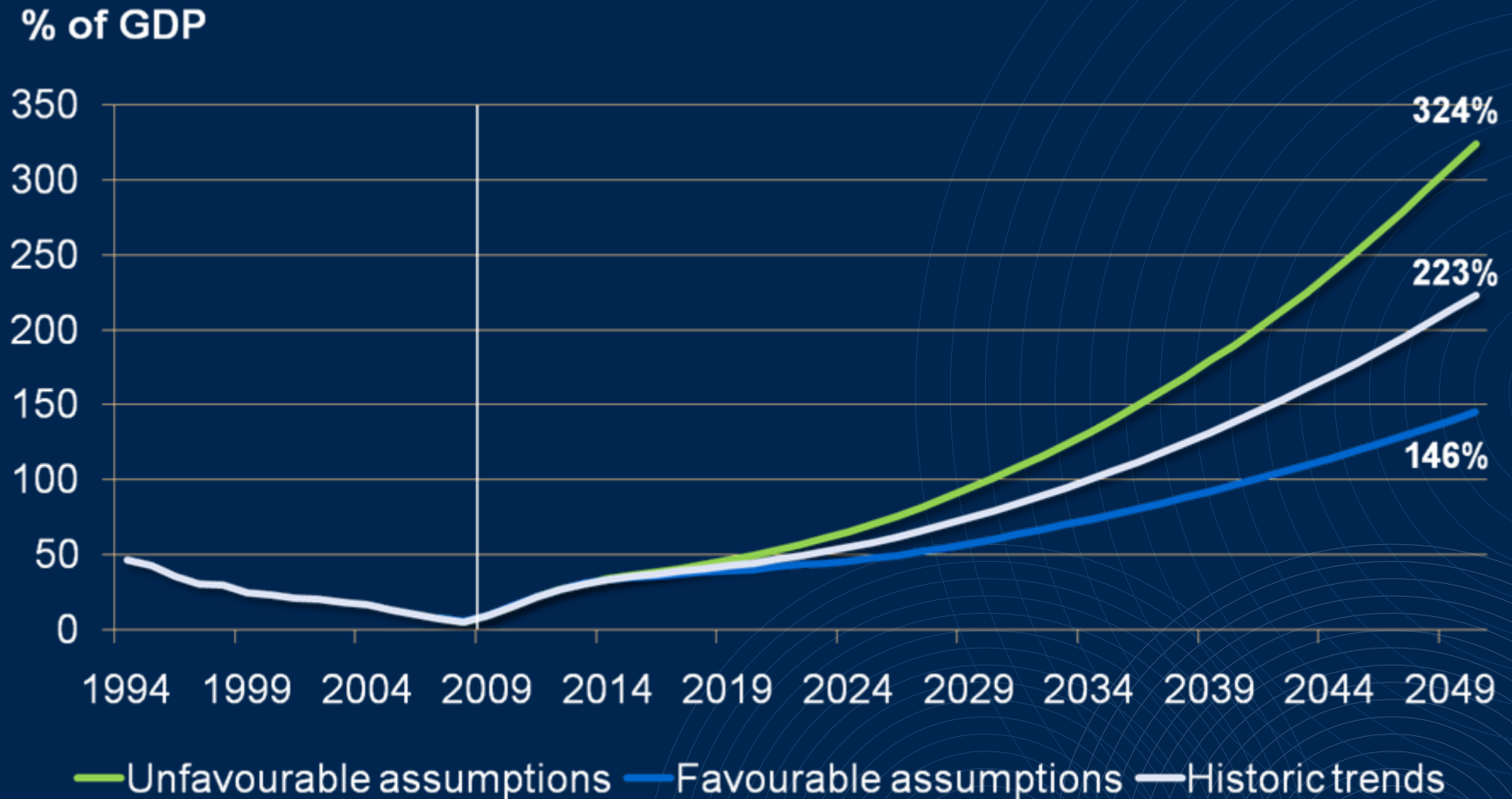




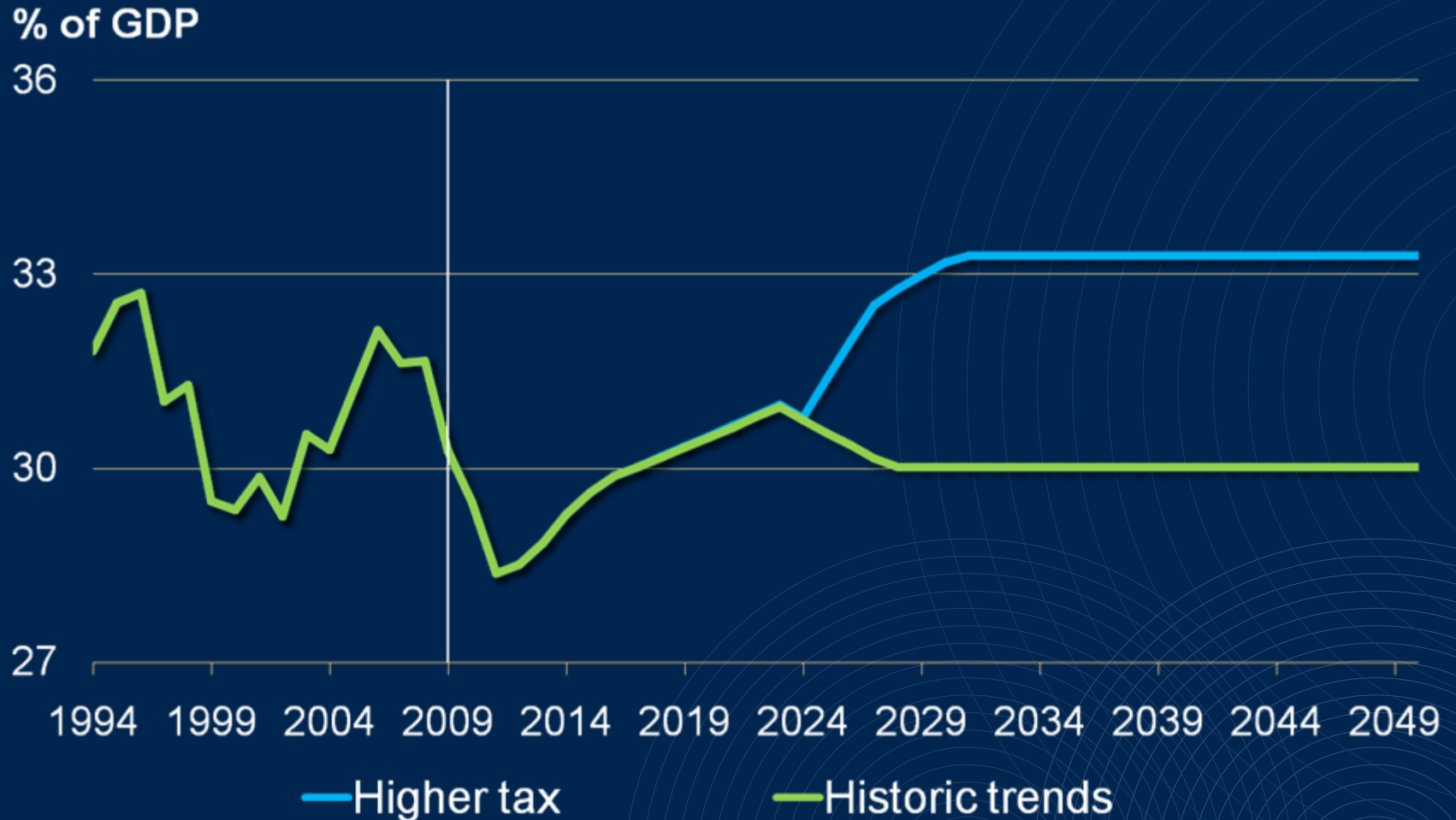
Choices

- Economic growth
- Tax
- Spending
 - Health
 - Justice
 - Education
 - Benefits
 - Superannuation

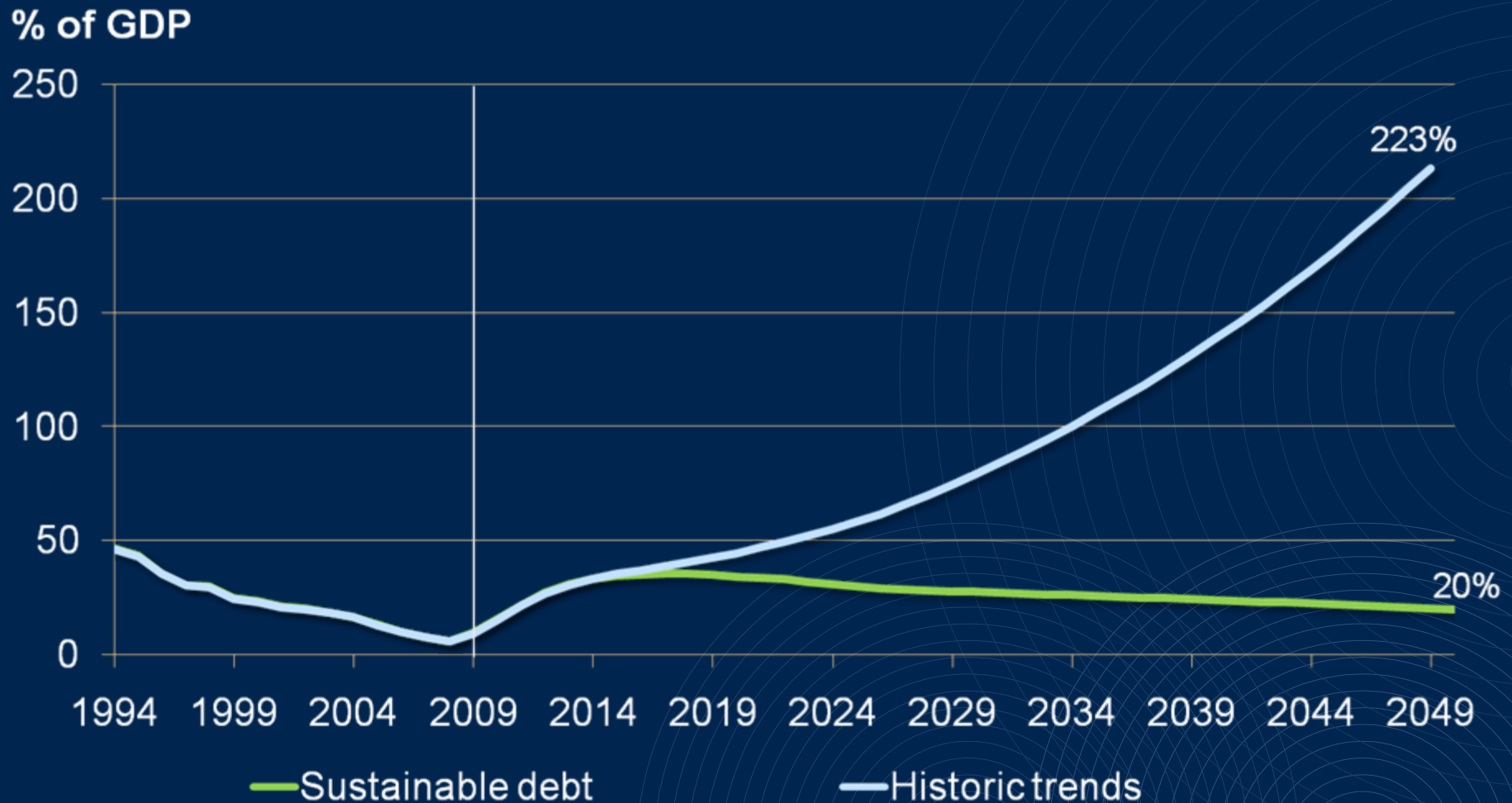
Higher growth helps, but is not a solution



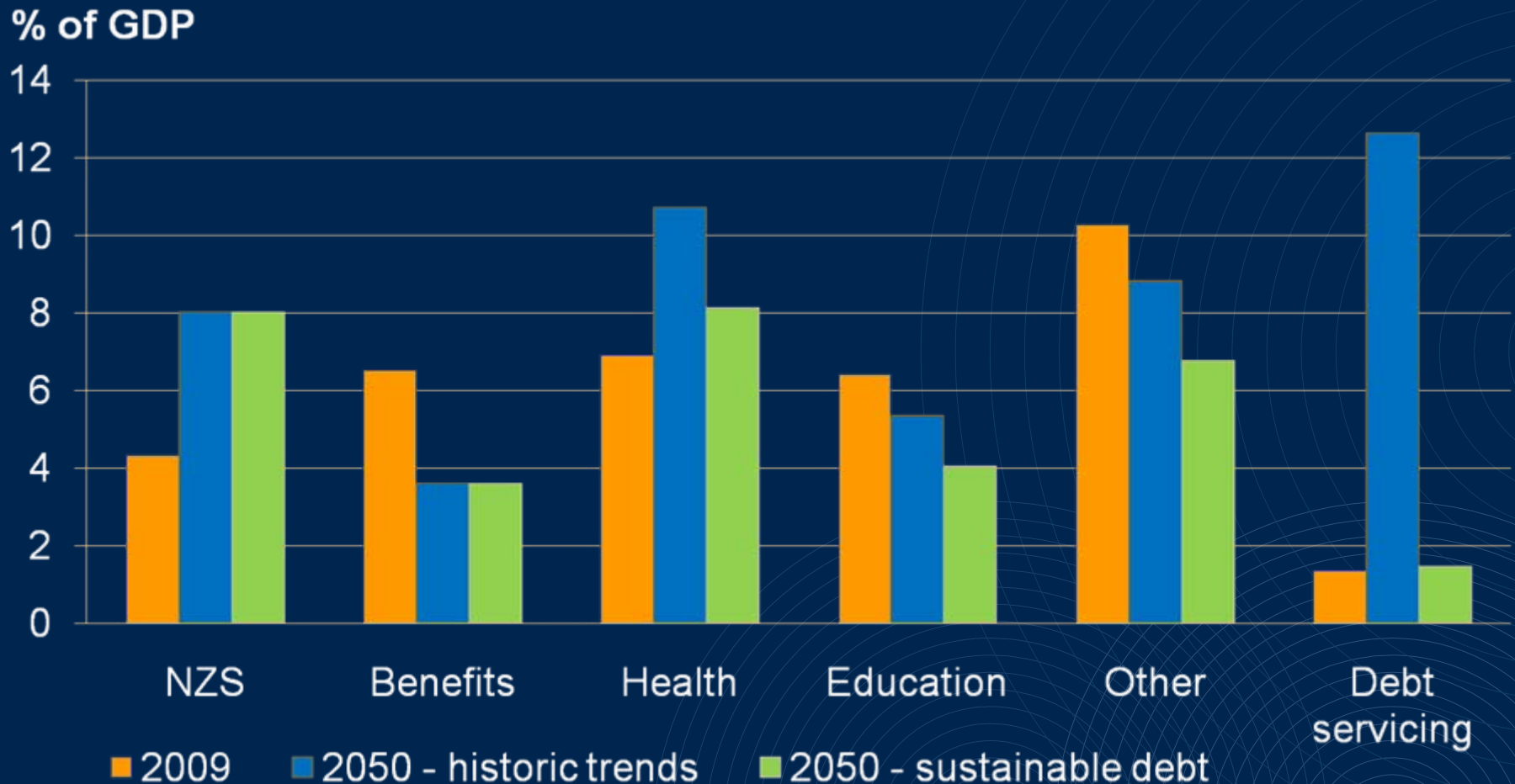
What role could tax play?



Net public debt – two scenarios



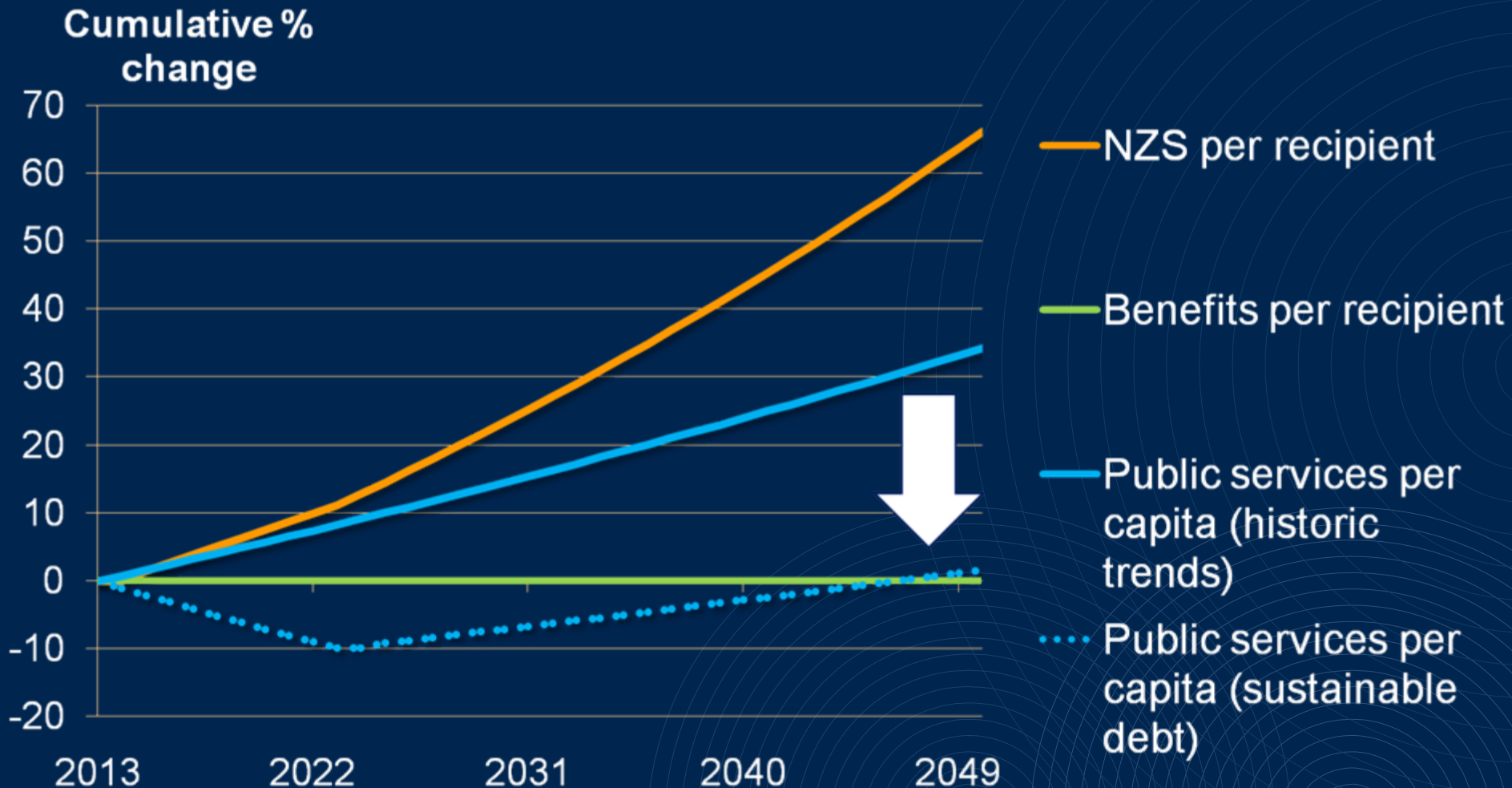
Sustainable debt: spending changes



Pressure points

- High growth areas:
 - Health
 - NZS
- Lower growth path but concerns about credibility:
 - Education (Will the demographic dividend be cashed out?)
 - Benefits (Is CPI indexation sustainable? Will SBIB growth slow)
 - Justice (Low base, but fast growth over last decade)
 - Core public sector (Fat to be trimmed?)
 - Capital (Allowance profile realistic?)
- Off balance sheet risks:
 - Climate change?
 - Implicit liabilities?

What the average Kiwi receives



More choices

- Other options for reaching sustainable fiscal position
- Conclusions to guide debate around these choices



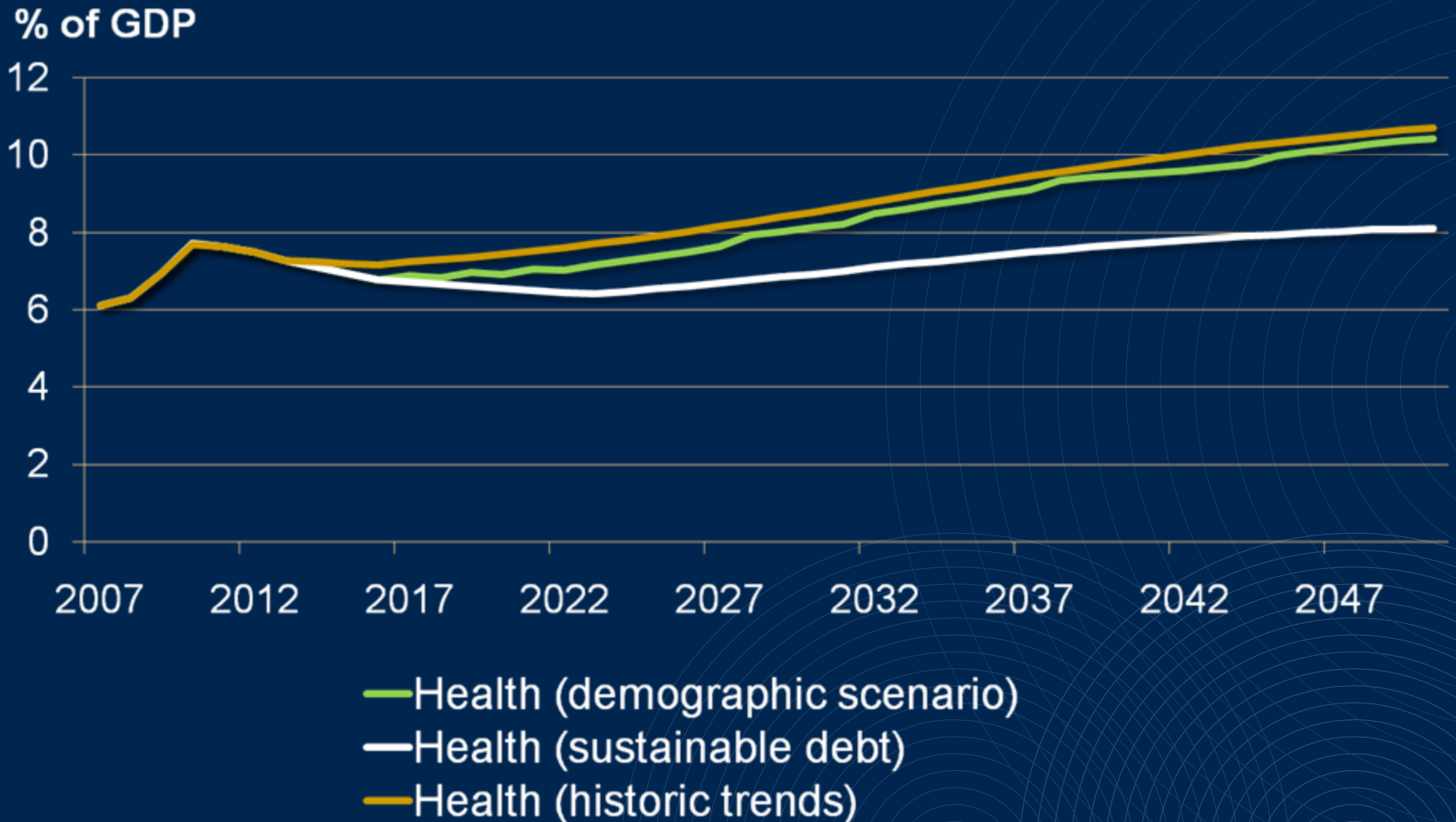
Alternate illustrative scenarios

- ‘Public sector productivity’ scenario
 - Cutting low-value programmes
 - Double public sector productivity
- ‘Rebalancing’ scenario
 - Raise taxes
 - Index pension age to life expectancy
 - Reduce growth in benefit spending
 - Gains from these changes are redistributed to other spending areas

'Demographic' scenario

- Index pension age to longevity
 - Raise from 65 to 67 by 2023
 - Reaches 69 by late 2040s
- Pension payments indexed to CPI + 1%
- Use fiscal savings for public health funding

'Demographic' scenario



General conclusions

- Make early changes
- Keep debt under control
- Encourage labour force participation
- Focus on growth
- Keep spending under control
 - Reprioritise existing spending
 - Set a high threshold for new spending
 - Secure a cost-effective mix of price, volume, quality
 - Look at institutional arrangements
 - Manage public expectations