Hon Bill English

Minister of Finance

Pre-Budget Speech to the Wellington Employers' Chamber of Commerce

St James Theatre, Wellington

Tuesday 15 April 2014

Good afternoon. It's a pleasure to be with you again today.

I would like to thank John and Raewyn and their team at the Wellington Employers' Chamber of Commerce for inviting me to speak to you again this year.

I also want to acknowledge the Chamber's work in promoting the Wellington business community and in grappling with issues affecting businesses in the capital city.

It's great to see measures of business confidence in Wellington rising.

I recently attended the 20th anniversary of Infratil, a Wellington-based company built on managing airports and electricity companies better than governments can.

Infratil has exported its expertise to other markets and diversified to other businesses, creating more jobs in Wellington.

Many people are unaware that Meridian Energy's head office is in Wellington.

Today the recently-floated company is valued at $4 billion and it could develop along a similar track to another large Wellington company, Todd Energy, by diversifying offshore and creating more jobs in Wellington.

Alongside burgeoning technology-driven companies, these companies are providing a firm foundation for Wellington's economic success.

In exactly one month, I will present the National-led Government's sixth Budget.

Over our previous Budgets, we've spent in excess of our revenue.

This has protected the most vulnerable families from the domestic recession and the GFC, it has maintained living standards and it has supported the renewal of our second-largest city after the earthquakes.

It has also lifted net government debt from $10 billion in 2008 to around $60 billion this year.

As the economy improves, and we return to surplus, we will begin repaying that debt.

The Budget next month will show growing surpluses over the next four years, starting with a small surplus in 2014/15.

At the same time, we've set out on a longer-term path to repair the damage to our economy caused by excessive borrowing, consumption and spending under the previous Labour government.

So together with households and businesses, we're rebuilding the economy's capacity to deliver more jobs and higher incomes over the next decade.

And we're starting to see positive results.

Employment is rising across the board, wages on average are increasing ahead of the cost of living and consumer and business confidence has lifted.

So the Government has shifted its focus from managing our way out of recession to managing a growing economy.

In particular, we're aiming for sustainable growth - the kind of longer-term growth that can deliver consistently more jobs and higher incomes.

A short, sharp uplift would lead only to disappointment if we did not work on the longer-term economic fundamentals of investment, skills and productivity.

The Government is taking a long-term view, because some of the factors driving the economy today will peak over the next few years.

Export prices are likely to return closer to normal levels, housing supply will eventually catch up and the Christchurch rebuild will peak and eventually slow.

And the New Zealand economy faces ongoing global risks, including uncertainty about the performance of our two largest and linked trading partners, China and Australia.

Against the background of a growing economy, we have the opportunity to lock in the gains New Zealand has earned over the last six years.

That will mean more investment, better skills and a growing export base – all flowing into higher incomes and more jobs.

This year is likely to see a political debate between a determined Government and complacent opposition parties who already believe today's good times are permanent.

And they think we can go on an immediate taxpayer-funded spend-up.

We paid the price of complacency in the years up to 2008.

Until the mid-2000s, New Zealand generally enjoyed a period of low inflation and relatively high growth.

Complacency then led to a rapid pick-up in government spending, policy that undermined competitiveness, soaring house prices and an unprecedented increase in household debt.

By 2008, households faced mortgage rates of almost 11 per cent and business rates exceeded 9 per cent.

Inflation exceeded 5 per cent and, by 2008, the export sector had shrunk significantly since the early 2000s, smothering our earning capacity.

The high cost of capital brought an end to investment and job growth and by early 2008 - well before the global financial crisis - New Zealand was in recession.

We can avoid those problems this time round.

While some increase in interest rates is an inevitable consequence of a growing economy, we need to do everything we can to ensure they don't rise too sharply in the next few years.

A lower interest rate cycle will mean less pressure on households with debt, more investment in productive businesses and less pressure on the exchange rate for our exporters.

It is in that context that we will present the Budget next month.

Budget 2014 will build on our success so far.

You will see the Government continuing to be careful with its spending. And we will lay out an ongoing programme to lock in the benefits of sustainable growth.

If governments make large cash injections into the economy when house prices are already high and economic growth is building, interest rates will rise sharply.

We won't make that mistake.

National's new spending over the last five and a half years has slowed considerably compared with new spending by the previous government - and public services have improved.

Opposition parties' answer to every problem is more government spending, despite clear evidence that high rates of government spending have little or no impact.

This was noted by the Salvation Army in its State of the Nation report in 2008. They noted that large increases in spending over the previous five years seemed to have contributed very little to New Zealand's social progress.

We don't need large lumps of new spending to get better results for our communities.

The Budget next month will be about thoughtful targeted spending, not a spend-up. It will invest in better healthcare, more effective education, safer communities and less welfare dependency.

This Government has taken time to improve the quality of government spending, rather than just cut costs.

We have invested significantly more in areas where we can make a positive difference.

Where possible, we've reprioritised spending out of areas that were not delivering results and we've used that money more effectively.

This has resulted in falling crime rates, fewer sole parents, reduced welfare dependency and higher levels of educational achievement.

In welfare alone, we are investing hundreds of millions of dollars up-front to support more people off welfare and into work, training or education.

We're finding we can improve people's lives and reduce spending pressure if we really understand who we are dealing with.

For example, there is a group of around 2,000 six- to nine-year olds who had the worst start in life. They will cost taxpayers $750 million if we do nothing to prevent them getting into trouble.

We've only recently been able to measure this figure.

The information creates a moral and financial imperative to act more effectively in the interests of these children and the wider community through the Children's Action Plan.

In another example, the number of young mothers on a main benefit has fallen from more than 4,200 in December 2009 to fewer than 2,600 in December 2013.

The Government has invested in each of them to make sure they have access to a supervising adult who can provide some stability in their lives.

Because of that investment, they have better lives and it's good for the Government's books when they succeed.

That's why we're confident we can maintain responsible fiscal policy over the next three years and at the same time improve results from public services.

That will include debt repayment, resuming contributions to the New Zealand Super Fund, and replenishing the Crown's balance sheet.

It will also allow us to invest a little more in priority public services – providing that doesn't push up interest rates or restrict our ability to get debt down.

We will have more to say about the Government's future framework for fiscal policy in the Budget.

But, as the Prime Minister confirmed two weeks ago, the Government will stick to its $1 billion Budget allowance for the 2014/15 financial year.

This is the responsible thing to do.

Imagine the effect on interest rates – and the rest of the economy – of a return to the $3 billion-plus annual Budget allowances we saw under the previous government from 2005 to 2008.

By containing government spending, we will help to restrict interest rate increases. This makes a significant and positive contribution to family budgets.

Every one percentage point movement in mortgage interest rates is worth around $40 a week - or $2,000 a year - for a family with a $200,000 mortgage.

So when you hear politicians promising to ramp up spending to pay for expensive election promises, you should remember that this would come at a significant cost to households and businesses.

We know from experience up to 2008 that runaway government spending was one driver of high interest rates.

The other driver was runaway house prices.

The Productivity Commission has noted that the biggest issue is the limited supply of new houses when demand is growing.

House prices doubled between 2001 and 2007, and prices have resumed their upwards march in most areas since the GFC.

There are a number of reasons for this, but there is little doubt that planning processes and rules are important drivers of land and housing costs.

It is now difficult to build some types of affordable housing in our least-affordable cities.

To take a couple of examples, planning rules in Auckland require apartments to be at least 40 square metres.

And balconies are now required to be 8 square metres.

These two rules alone add around $80 per week to the rent.

A range of other rules set minimum subdivision size, ceiling heights, bedroom size and even the width of your front door. All of these push up the cost of housing.

Local body planners and councillors are not aware of the wider social and economic effects of their complex rules and processes.

I see three major consequences.

First, higher house prices created by excessive planning rules put pressure on interest rates, reducing business investment, lowering productivity and hitting household budgets.

And housing supply that is unresponsive to demand causes price volatility and the risk of a severe correction.

Second, as the cost of housing consumes a greater proportion of income, pressure goes on councils and the Government for greater assistance.

Around 40 per cent of households that are renting receive accommodation support from the Government. This will increase if housing becomes less affordable.

The third consequence is that rising house prices drive inequality.

Inequality in New Zealand has been flat since 2004, but the situation could have been better had housing been more affordable.

That is why we’re working with councils to ensure New Zealanders have access to more affordable housing.

We have signed a Housing Accord with the Auckland Council, and this is already delivering results.

And we’re working to sign more accords with councils in Christchurch, Tauranga, Queenstown and the Wellington region.

We’re reforming the social housing system to bring in community housing groups, increase competition and get social houses where they are needed the most.

We’re reforming the Resource Management and Local Government Acts to cut red tape and reduce costs.

And we’re continuing to invest around $2 billion annually in accommodation support for Kiwi households.

So we’re making steady progress to deliver more affordable housing to more New Zealanders.

It takes time to change the way councils make decisions on housing and for developers to get more projects up and running.

That’s why it’s important that we continue to focus on every measure that can reduce the cost of housing over the next few years.

Before finishing today, I want to highlight the opportunity we have to lock in the benefits of sustainable and broad-based economic growth.

Despite our good progress, we still have much more to do to improve New Zealand’s economic growth and to support higher incomes across the board.

Containing government expenditure and improving housing supply are steps along the way.

The Budget will also set out the next stage of the Government’s wider programme to continue building on our competitiveness so we can lock in the gains for households and businesses.

As I said earlier, this is not the time to think about putting our feet up.

A third-term National-led Government will build on the momentum we’ve achieved across our programme.

Quarterly GDP or current account statistics are not, in themselves, what matter to families. Jobs, higher incomes and opportunities to get ahead are what really matter.

Everyone’s situation is different and many families are still finding times are challenging.

But the benefits of a sustainably growing economy are tangible and meaningful. Let me give you an example.

Over the past two years, as economic momentum has picked up, the average full-time wage has increased from $51,700 a year to $54,700 – an increase of $3,000.

Looking ahead, in the Budget next month Treasury will forecast annual GDP growth of between 2 per cent and 4 per cent a year out to 2018.

Based on that growth, Treasury’s preliminary Budget forecasts show the average wage will rise further to around $62,200 a year in four years’ time.

This would mean an increase of another $7,500 by 2018.

So, if you take that six-year period as a whole, the average wage will have gone up by $10,500, or around 20 per cent, compared to inflation of just over 12 per cent over the same period.

The Budget forecasts will also show around 170,000 more people working by 2018. Together with a falling unemployment rate, this will build on the 66,000 jobs created in the past year alone.

That's what a sustainably growing economy actually means for hard-working New Zealanders.

And that's why it's important that we remain focused on our programme of considered and consistent change over time.

Under John Key's leadership, this Government, alongside households and businesses, has managed New Zealand through some of the most significant challenges we've seen in generations.

Providing we stay the course, we will have a faster-growing, more sustainable economy. Wages will continue to increase faster than the cost of living and tens of thousands more jobs will be created every year.

We will provide more elective operations, we will help more New Zealanders off welfare and into work, and the crime rate will continue to fall.

We're on track to surplus next year and larger surpluses in subsequent years, which will give us choices. And we'll soon be able to start reducing debt and investing a bit more in priority public services.

The alternative is to put all of this at risk at the election and radically change direction.

We've already had a taste of what that change of direction would involve: a combination of high government spending, economic experiments from the 1970s and a lack of focus on what really matters.

That is a backward-looking policy prescription, particularly when New Zealanders' impressive resilience is starting to pay dividends.

We now have the opportunity to significantly improve New Zealand's economic fortunes and provide a better future for New Zealand families.

We are making good progress, but there is a lot more to be done.

Providing we stick to our plan, I’m confident that we will build the brighter future New Zealanders deserve.

Thank you.