29 September 2026

Fiscal consolidation apparent

- **Smaller deficits, bigger surpluses forecast**
- **Structural deficit reduced to 1.0% of GDP**
- **Net debt peak forecast lowered**
- **Stronger nominal economy supports tax revenue**
- **Expenses as share of economy forecast to fall**
- **Debt programme reduced**

Key forecasts

The core fiscal deficit (OBEGALx) is forecast to reduce to 1.4% of GDP in the June year 2027.

The deficit is forecast to decline to 0.2% in the June year 2028 before returning to a 0.8% of GDP surplus in Fiscal 2029, lifting to 1.4% of GDP in Fiscal 2030, and to 2.0% of GDP in Fiscal 2031.

Net debt rises to 43.7% of GDP in the year ended June 2027 and to a peak of 43.9% of GDP in Fiscal 2028. It then reduces to 39.5% in Fiscal 2031.

Bond programme lowered by $4.0b for Fiscal years 2027, 2028, 2029, and lowered by $3.0b in Fiscal 2030.

Treasury forecast the economy to grow 2.3% in the year ended June 2027 and then lift 2.9% the year after. Growth is expected to average 2.6% per annum in the three years thereafter.

Starting point

We discussed in our preview that the projected track to surplus by 2028/29 may well be from a smaller starting point. This was not only because the fiscal deficit was already running ahead of the Budget plan as we noted but also because we had detected more confidence coming from Finance Minister Willis in the lead up to today's PREFU.

The latter was further enhanced when she was recently quoted as saying that 'our Government is making great progress on fixing the books, smaller deficits, bigger surpluses, less debt'. With that sort of rhetoric heading into today's PREFU, it is no surprise to see such things in today's accounts.

The Minister of Finance has proudly announced a smaller-than-Budget deficit of 1.9% of GDP in the year to June 2026. The Budget had forecast a deficit of 2.6% of GDP for that year. The final audited Government accounts for that year are due on 8 October, although one would think that they would be close to the unaudtied accounts presented in today's PREFU.

The smaller deficit than forecast at Budget is a result of higher than forecast tax revenue, lower than forecast expenses, as well as favourable results from Crown Entities and State Owned Enterprises.

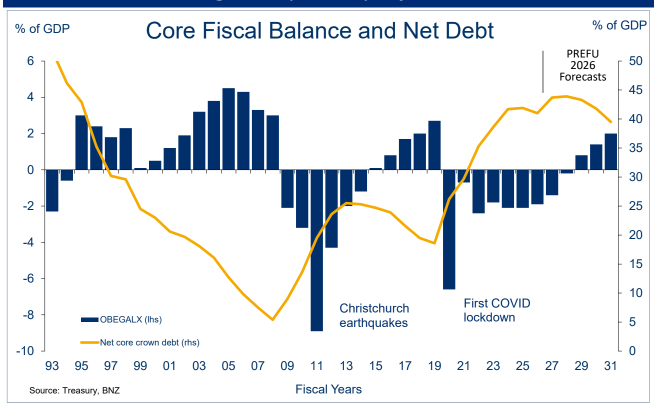
Stronger than forecast tax revenue outturns have been supported by stronger than expected nominal GDP.

Fiscal outlook

The stronger nominal economy starting point has flowed through to the fiscal forecasts. The fiscal track is firmer across the forecast horizon largely driven by upwards revisions to revenue, driven by a stronger tax base, and downward revisions to expenses.

A core operating deficit of 1.4% of GDP is now forecast for the year ended June 2027 and forecast to shrink to 0.2% of GDP in the following year. These figures are respectively 1.0% and 0.6% smaller than projected in the Budget. Smaller deficits and then larger surpluses are projected.

Smaller deficits, larger surpluses projected



As expected, the forecast OBEGALx surplus for 2028/29 remains. It is now forecast to be 0.8% of GDP, a larger surplus than the 0.5% of GDP surplus forecast at Budget 2026. The surplus is expected to grow further to 2.0% of GDP in 2030/31.

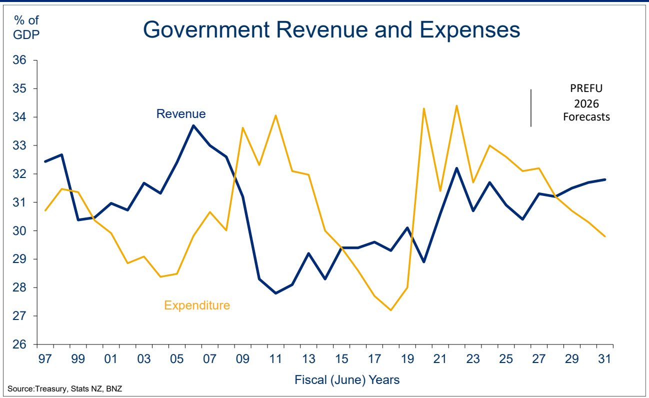
This improvement now means that the forecast peak in net debt is lower and falls faster than previously projected. Net core Crown debt now peaks at 43.9% of GDP in the year to June 2028, before falling to 39.5% of GDP in the year to June 2031. The Budget projected a peak in net core Crown debt at 46.1% of GDP in the year to June 2028.

Importantly, some of the deficit reduction is more than cyclical in nature. The cyclically adjusted, or structural, deficit has reduced to 1.0% of GDP in Fiscal year 2026 from 2.5% in Fiscal year 2024. It is projected to reach (a tiny) surplus in Fiscal year 2028, one year ahead of the forecast OBEGALx surplus and one year ahead of the structural surplus forecast in Budget 2026.

Core Crown revenue is projected to rise from 31.3% of GDP in Fiscal year 2027 to 31.8% of GDP in Fiscal year 2031. Core Crown expenses are forecast to ease from 32.2% in Fiscal year 2027 to 29.8% of GDP in Fiscal year 2030.

The reduction in expenses to GDP reflects future operating allowances and the profile of past Budget packages, with savings that increase over the latter part of the forecast period. Budget operating allowances remain at $2.4 billion per annum over the forecast period.

Revenue and expenses as a share of the economy



Source:Treasury, Stats NZ, BNZ

Rating agencies

The debt rating agencies should be happy with this set of outcomes and forecasts. Agencies had been giving New Zealand credit for the fact that the government was focusing on targeting fiscal balance. However, moves to negative credit watch were based on concerns that the surplus target was being delayed and looked increasingly untenable. Had their concerns played out moves from negative watch to a full donwgrade were possible. At Budget 2026, it looked like the Government had probably done enough to delay that proposition. Today's set of fiscal accounts is a further clear move in that direction.

The question is whether the economic forecasts on which this analysis is based, and the assoicated fiscal forecasts are credible? And, will they survive the election? On the latter it is important to note that both major parties remain committed to returning the books to surplus.

Economic outlook

With regard to the economic forecasts, we think there is some risk that growth ends up lower than Treasury is currently picking. The differences to our own forecasts are relatively small.

Treasury sees the economy growing 2.3% in the year ended June 2027 rising to 2.9% in fiscal 2028 and 2.7% the year after. Our forecasts for the same period are 2.0%, 2.8% and 2.7% respectively. The RBNZ's equivalent forecasts are 1.9%, 2.8%, and 2.9%.

We are quick to note, however, that it is unwise to be critical of anyone's forecasts in the current environment. There are simply too many moving parts and even slight changes in assumptions about key variables, such as oil prices, can have disproportionate impacts on outcomes. Economic forecasts for the PREFU were finalised on 21 August, ahead of the most recent spike in oil prices.

Additionally, to the extent that we think there are downside risks to Treasury's growth forecasts (and the Treasury openly acknowledged risks are tilted to the downside) there are upside risks to its inflation outlook.

The Treasury forecast annual inflation to ease to 1.9% in the June year 2027. Our current inflation forecast for the same period is 2.8%.

Given that it is the nominal economy that produces tax revenue then it may well be that higher inflation completely offsets lower growth in the revenue stakes.

Another support to nominal growth is the NZ dollar tracking significantly lower than assumed by Treasury. The Treasury assumed a TWI between 66.5 and 67.7 from June 2026 to June 2027. It currently sits around 64.5.

As it is, Treasury noted that oil prices are around USD$15/bbl higher than assumed at forecast finalisation. This would suggest upside risks to inflation forecasts and downside risks to growth expectations.

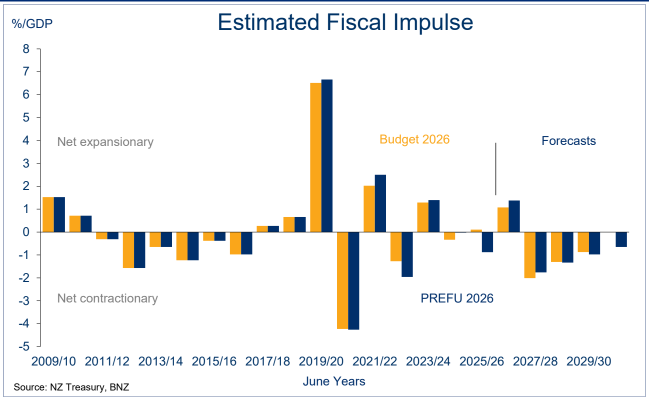
All that said, the risks are clear and will need to be monitored closely.

Implication for the RBNZ

For the central bank there should be little in today's announcement that will dissuade them from their projected broad course of action of pushing the OCR higher. The fiscal impluse is still forecast to turn contractionary. Although, compared to Budget 2026 forecasts, the fiscal impulse is expected to be more expansionary in Fiscal year 2027 and then less contractionary over the following two fiscal years. At the margin this is a touch more stimulatory (or less contractionary) than the RBNZ had factored in, although it follows a more contractionary Fiscal 2026 than expected.

Be that as it may, Treasury has a marginally more aggressive interest rate track than the Reserve Bank. Treasury has lifted its interest rate forecasts. The 90-day bank bill rate is forecast to be at 3.5% in June 2027 and reach a peak of 3.8% in June 2029 and June 2030 before easing to 3.6% the following year. This track implies the OCR pushes up to 3.5%, at a minimum. In its September MPS, the RBNZ projected the OCR averaging 3.07% in Q2 2027 lifting to 3.28% by the end of its forecast horizon in Q3 2029.

Fiscal policy to turn contractionary

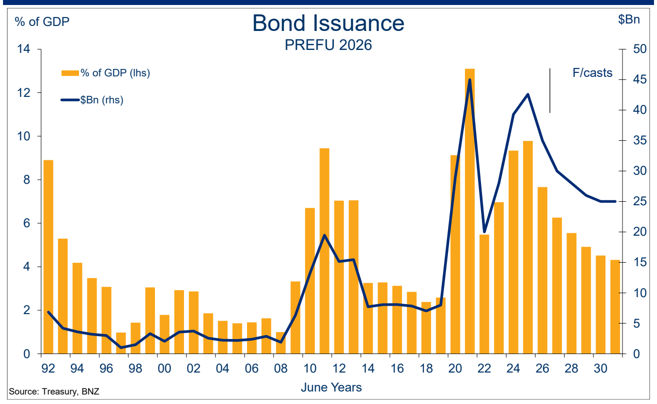


The debt programme

The most interesting thing from the PREFU for financial markets will be the fact that New Zealand Debt Management reduced the bond programme, by $4.0 billion per annum in each of the June years 2027, 2028 and 2029, with a $3.0 billion reduction in the June year 2030.

The current, Fiscal year 2027, bond programme has been reduced to $30.0 billion from $34.0 billion forecast at Budget 2026.

Bond programme reduced



Additionally, short term borrowings on issue have been reduced by $5.0 billion in the June year 2027 and reduced by $2.0 billion in the June year 2028.

The $15.0 billion bond programme reduction across the forecast horizon reflects a reduction in forecast cash requirements.

This reduction in the bond programme is not a complete surprise. We had warned of that possibility given that the cash deficit had been running smaller than Budget forecasts.

Market reaction saw a mild richening of bond-swap spreads to the tune of around 2 basis points across the curve. The market seemingly wary of any forecast given the pending election.

What next?

The election adds uncertainty to the medium-term fiscal path. What will be interesting is what the improved fiscal position will allow political parties, of all stripes, to announce in the lead up to the November 7 General Election.

No matter who is holding the Government benches after the election, there will be policy changes that have not been taken into account in this set of forecasts, although it is important to reiterate that both major parties remain committed to returning the books to surplus.

The good news is that today's fiscal accounts continue to make New Zealand's fiscal position look remarkable against a global deterioration.

PREFU 2026	2022	2023	2024	2025	2026	2027	2028	2029	2030	2031
	actual	actual	actual	actual	f/cast	f/cast	f/cast	f/cast	f/cast	f/cast
(June years, % of GDP)										
Core Crown Revenue	32.2	30.7	31.7	30.9	30.4	31.3	31.2	31.5	31.7	31.8
Core Crown Expenses	34.4	31.7	33.0	32.6	32.1	32.2	31.2	30.7	30.3	29.8
OBEGAL	-2.7	-2.4	-3.1	-3.2	-2.4	-1.8	-0.6	0.4	1.1	1.5
OBEGALX	-2.4	-1.8	-2.1	-2.1	-1.9	-1.4	-0.2	0.8	1.4	2.0
Gross Debt	32.6	33.8	41.8	46.8	49.9	50.7	51.1	50.7	49.0	46.2
Net Core Crown Debt	35.3	38.6	41.7	41.9	41.0	43.7	43.9	43.3	41.8	39.5
Domestic Bond Programme ($NZm)	20,000	28,000	39,300	42,600	35000	30,000	28,000	26,000	25,000	25,000
(June years)										
Real GDP (annual average % change)	0.5	4	1.1	-1.1	1.6	2.3	2.9	2.7	2.6	2.5
Consumer Price Index (annual % change)	7.3	6	3.3	2.7	4.1	1.9	2.0	2.1	2.1	2.0
Unemployment rate (June qtr)	3.3	3.7	4.7	5.2	5.6	5.2	4.7	4.4	4.3	4.3
90-day Bank Bill Yield (March qtr. av.)	2.2	5.6	5.6	3.4	2.6	3.5	3.7	3.8	3.8	3.6
Trade Weighted Index (March qtr. av.)	72.2	70.9	71.4	69.1	66.5	67.7	68.7	69.3	69.8	70.1

Economic Forecasts	BNZ						Treasury (PREFU 2026)						
(Annual average % change, June years)	**2025 Actual**	**2026 Fcast**	**2027 Fcast**	**2028 Fcast**	**2029 Fcast**	**2030 Fcast**	2025 Actual	2026 Fcast	2027 Fcast	2028 Fcast	2029 Fcast	2030 Fcast	2031 Fcast
Private consumption	0.4	1.3	1.3	2.6	2.8	2.9	0.6	1.0	1.8	2.7	2.9	3.1	3.0
Public consumption	-1.0	4.1	-0.1	1.1	0.2	0.0	-0.8	4.7	1.1	0.4	0.2	0.2	0.3
Residential investment	-12.2	0.4	6.6	1.0	2.5	3.1	-12.1	-1.8	7.0	10.6	5.2	3.4	2.5
Business investment	-2.5	2.8	4.9	4.2	5.3	5.5	-2.4	1.6	1.9	6.2	4.8	3.6	2.9
Exports	3.3	6.1	5.2	3.6	3.6	4.5	3.0	5.7	2.8	0.7	2.1	2.3	2.3
Imports	1.6	6.8	3.2	2.7	3.7	4.9	2.0	6.1	0.0	2.4	2.8	2.6	2.3
GDP (expenditure measure)	**-0.8**	**2.2**	**2.4**	**2.8**	**2.7**	**2.7**	**-0.8**	**2.1**	**2.6**	**3.0**	**2.7**	**2.6**	**2.4**
GDP (production measure)	**-1.1**	**1.7**	**2.0**	**2.8**	**2.7**	**2.7**	**-1.1**	**1.6**	**2.3**	**2.9**	**2.7**	**2.6**	**2.5**
Employment	-1.0	0.3	1.8	2.7	2.3	2.4	-1.0	0.3	1.6	2.3	1.9	1.6	1.4
Unemployment	5.2	5.6	5.4	4.9	4.8	4.4	5.2	5.6	5.2	4.7	4.4	4.3	4.3
CPI inflation	2.7	4.1	2.6	2.2	2.4	2.3	2.7	4.1	1.9	2.0	2.1	2.1	2.0
Current account balance													
- % of GDP	-3.6	-3.2	-4.8	-3.7	-3.3	-3.1	-3.8	-4.0	-3.5	-2.7	-2.6	-2.5	-2.4
TWI (June qtr avg)	69.2	66.5	65.0	68.4	70.6	72.0	69.1	66.5	67.7	68.7	69.3	69.8	70.1
90-day bank bill rate (June qtr avg)	3.4	2.6	4.0	3.8	3.8	3.8	3.4	2.6	3.5	3.7	3.8	3.8	3.6

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