

Paul Glass: The real size of Govt debt in NZ, stripped of accounting tricks

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We are now literally borrowing money for petrol that our kids will have to repay. The Government's fuel subsidy will cost a total of about \$2b, which will effectively be debt funded.
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OPINION

There is no such thing as "government" money when it comes to spending. Governments get their funding from taxpayers either directly through taxes or through debt, which taxpayers must service and eventually repay.

In New Zealand, the three largest sources of tax revenue for the Government are individuals (35 per cent), GST (22 per cent) and corporate tax (17 per cent).

Over the last 30 years in NZ, governments, of both flavours, have taken a prudent approach to debt that recognises that we are a small and volatile trading nation, subject to frequent natural disasters, dependent on primary products, exposed to biological risks (think Covid, foot-and-mouth disease, Psa etc) and have a highly indebted household sector.

Successive governments had driven NZ government debt down to less than 20 per cent of GDP. That prudent approach to debt all changed with the current government which, through its two terms, has spent taxpayer money at a rate unmatched in NZ's history. And unfortunately, looking at economic and social outcomes, so much of that expenditure, which has fuelled our rise in debt, appears to have been wasted.

In 2017, NZ's government debt stood at \$112 billion or \$65,000 per household.

Today, excluding an accounting trick that I'll touch on later, that debt is \$224b or \$115,000 per household.

That's a scary number when matched against the size of our tax base and when you realise that around half of NZ households don't pay any net tax (after benefit payments are included). That government debt is on top of net household debt which sits at about \$174,000 per household.

In the 2017 election, National received 44 per cent of the vote followed by Labour on 37 per cent and NZ First on 7 per cent. In possibly a portent of what was to follow, in order to secure power, Labour's first step was to offer \$3b (\$1700 from every household in NZ) of taxpayer money to NZ First for its pet project, the Provincial Growth Fund.

That was a staggering amount of money which history will show has been largely wasted, but what has followed is far worse. When the global pandemic hit, something called the Covid Relief Fund was established. The fund doesn't exist in any real way, it is just an accounting allocation within the Government's books, which gives the impression that somehow there is free money that can be spent. And spent it has been – so far about \$70b in total.

Additionally, much of this money has been spent on pet projects that have nothing whatsoever to do with Covid, but it has been a useful tool for shielding payments from scrutiny.

Yes, this current Government has had to deal with Covid (likewise previous governments had to deal with the GFC and the Christchurch earthquake) but the amount of wastage has been massive and the urgency to get on top of issues has been lacking.

The second Auckland lockdown, which could have been avoided if more urgency was shown on getting vaccines sorted, and if our largest city hadn't been used as the main provider of MIQ facilities, is estimated to have cost \$8b alone.

Consultants are now costing well over \$1.2b per annum in addition to the army of Wellington bureaucrats whose numbers have swelled by close to 15,000 additional people.

Debt levels matter when things go wrong. NZ doesn't pay its own way in the world and runs a perennial deficit with the rest the world, as measured by our Current Account.

Last year our Current Account deficit blew out to a staggering \$34b for the 12-month period ended December 31, 2022, far worse than even during the GFC (\$15b in 2008). This deficit with the rest of the world needs to be funded from foreign capital and consequently we need to be viewed as a safe place to put money. Which means we must have low government debt levels.

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Comparisons between our government debt levels and that of other developed nations can be quite misleading because of our high household debt levels, which are now close to 100 per cent of GDP.

Last year, the Government restated - and reduced - NZ's headline net debt ratio by including the large assets (about \$100b) held by the NZ Superannuation Fund and other Crown entities.

This accounting trick significantly reduced NZ's Net Debt to GDP ratio by about 20 percentage points (for example, if our net debt ratio was previously shown as 30 per cent it would now be 10 per cent) and is misleading at best. NZ, like most nations, has massive unfunded liabilities in a number of areas including infrastructure, health, education and retirement, which do not appear in our debt calculations.

Higher debt levels also mean that debt servicing becomes a significant factor when interest rates rise, as they inevitably do. This debt servicing can become a significant drag on the economy.

Sovereign debt crises are fortunately relatively rare events, but they do happen. When the global focus goes on government debt, which it will do again, NZ needs to be in very strong shape.

NZ doesn't have the luxury of digging commodities out of the ground like Australia or being a reserve currency like the US.

Once a government loses fiscal discipline, it is hard to stop.

Rather than tightening our belts we just borrow more. Core government expenditure has blown out from \$76b pa. in 2017 to an extraordinary \$130b this year, and growing.

We are now literally borrowing money for petrol that our kids will have to repay. The Government's fuel subsidy will cost a total of about \$2b, which will effectively be debt-funded. The interest cost on this debt will also need to be serviced.

To put this additional expenditure in context, Pharmac's total annual budget is only about \$1.2b.

Imagine the good we could be doing if our expenditure was more targeted.

Also, inevitably the Government will use higher debt levels as an excuse to raise even more taxes. It is much easier to tax people more than cut wasteful expenditure.

But if we look at tax take relative to GDP, on 2021 data NZ sits at 33.8 per cent vs Australia at 28.5 per cent and the US at 26.6 per cent.

The NZ Government currently runs a deficit, or spends more than it earns. Consequently, every dollar it spends above what it receives is borrowed. The level of debt is now so high that it will not be repaid by us but rather mortgaged against our kids.

If only we had spent a greater proportion of this additional debt on infrastructure, NZ would have assets we could now benefit from rather than the creaking system we have.

Going into an election year, when the temptation for low-quality vote-winning spending will be high, it would be helpful if every tax dollar spent went under the scrutiny of "Are we happy to borrow this money from our children?" because that is effectively what we are doing.

A government addicted to spending and power is very dangerous indeed.

• **Paul Glass is executive chairman of Devon Funds.**