



**GOVERNMENT OF SAMOA**

**FISCAL STRATEGY STATEMENT  
BUDGET 2009/2010**

**MINISTRY OF FINANCE**

**29 MAY 2009**



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# **FISCAL STRATEGY STATEMENT**

## **BUDGET 2009/2010–2011/2012**

### **REPORTING REQUIREMENTS**

The Public Finance Management Act 2001 specifies principles of responsible fiscal management and sets out reporting requirements on the Minister of Finance and the Ministry of Finance. The reporting requirements include, under Section 18, the budget address, and a statement of the projection of estimated revenues and expenditures for the budget year and the two following years – the forward estimates. The reporting requirements also include, under Section 19, the Fiscal Strategy Statement to be submitted to the Legislative Assembly as part of the budget address.

The Fiscal Strategy Statement includes an assessment of the extent to which the budget statement is consistent with the Statement of Economic Strategy (SES), now called “Strategy for the Development of Samoa” (SDS), an explanation of the reasons for any significant differences between the current economic and financial situation of the State and the information and intentions in the SDS, projections of movements in economic and fiscal data which demonstrate intended progress towards achieving the SDS objectives, and the significant assumptions on which the projections are based.

The SDS must be published no later than 31 May of the year the statement becomes effective, and an update report (the SDS Update) must be published no later than half way through the period covered by the SDS. At present, the SDS is for a period of four years — *Strategy for the Development of Samoa, 2008/09–2011/12: Ensuring Sustainable Economic and Social Progress*.

### **ECONOMIC AND FISCAL OBJECTIVES**

Last year, the government presented the Statement on Forward Estimates and the Fiscal Strategy Statement for the first time as required under the Public Finance Management Act 2001. At that time, there were already signs of considerable uncertainty unfolding in the global economy, with external pressures from the high prices of fuel and foodstuffs impacting the local economy. These were taken into account in the preparation of the first forward estimates and fiscal strategy. At that time, the economy was at its strongest performance in the past decade with GDP posting a 6.1% growth. What has changed since is the rapid weakening of economic performance as the impact of the global recession take effect.

The exact magnitude of the impact of the weak economy on the fiscal position, and the extent to which it represents a long-lasting structural change remain uncertain. The forward estimates for the next three years without adjustment to policy settings, show that the projected increases in debt and declines in the State’s net worth, are outside of the range considered prudent in the medium term. Additionally, the accumulation of cash deficits will put macroeconomic stability at risk if not managed prudently over the medium term. In this context, while managing our way through the economic turmoil at present, the government will monitor vigilantly in the short

term the fiscal risks that exist and where appropriate adjust its policy settings and set new fiscal objectives.

In the long term, the government will maintain a long-term perspective for managing prudently risks around our fiscal position while focusing on growth and productivity improvements in the private and public sectors.

The existing medium to long term fiscal targets therefore remain valid and are re-confirmed here. As previously noted, these targets pose no change in policy settings in the the next three years:

- (a) constraining aggregate current expenditures within the range of 35-38% of gross domestic product (GDP) over the forward estimates cycle, to ensure there is sufficient liquidity in the economy to allow the private sector to grow and provide employment opportunities for the next generation;
- (b) keeping net public debt outstanding at less than 40% of GDP so as:
  - (i) to constrain future growth in debt servicing that could preclude increasing the level of service delivery expenditures in the budget;
  - (ii) not to dissipate the gains made by the Government in bringing the level of debt in Samoa from its previously high level to one that is the envy of most, if not all, of the countries in the Pacific region; and
- (c) constraining expenditures in relation to personnel costs to the range of 30-32% of total current expenditures in the year in question, to ensure the intended efficiency dividend associated with the implementation of performance budgeting is directed to increased service delivery, rather than to an increase in the size of the ministries.

In addition to these long term objectives, the SDS 2008-2012 establishes the following fiscal policy target:

- (d) Budget balance maintained in the range of -3.5% and +3.5% of GDP (except where larger deficits involve borrowing at concessional rates to fund growth-promoting infrastructure projects).

The objectives of the fiscal strategy are consistent with the following principles of responsible fiscal management in the Public Finance Management Act:

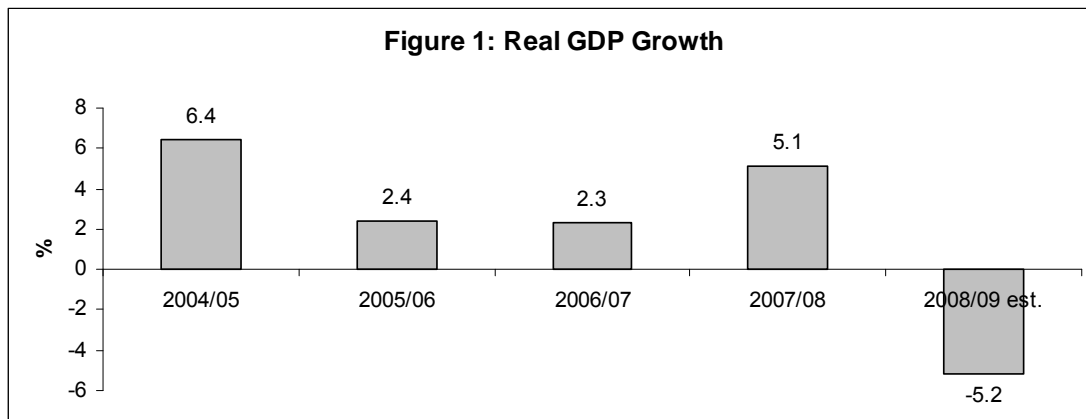
- (a) Managing total State debt at prudent levels so as to provide a buffer against factors that may impact adversely on the future levels of total State debt in the future;
- (b) Ensuring that within any borrowing programme the total overall expenditures of the State in each financial year are not more than its total overall receipts (inclusive of borrowings) in that financial year;
- (c) Achieving and maintaining levels of the State's net worth that will provide a buffer against factors that may impact adversely on the future of the State's net worth;
- (d) Managing prudently the fiscal risks facing the State;

- (e) Pursuing policies that are consistent with a reasonable degree of predictability about the level and stability of the tax rate for future years;
- (f) That the policies stipulated in the SDS 2008-2012 and those fiscal policies approved by Cabinet are in agreement with the fiscal limit that will be applied to the current and future expenditures on ministries and government projects.

## REVIEW OF FISCAL AND ECONOMIC PERFORMANCE IN THE LAST 5 YEARS, 2004/05–2008/09

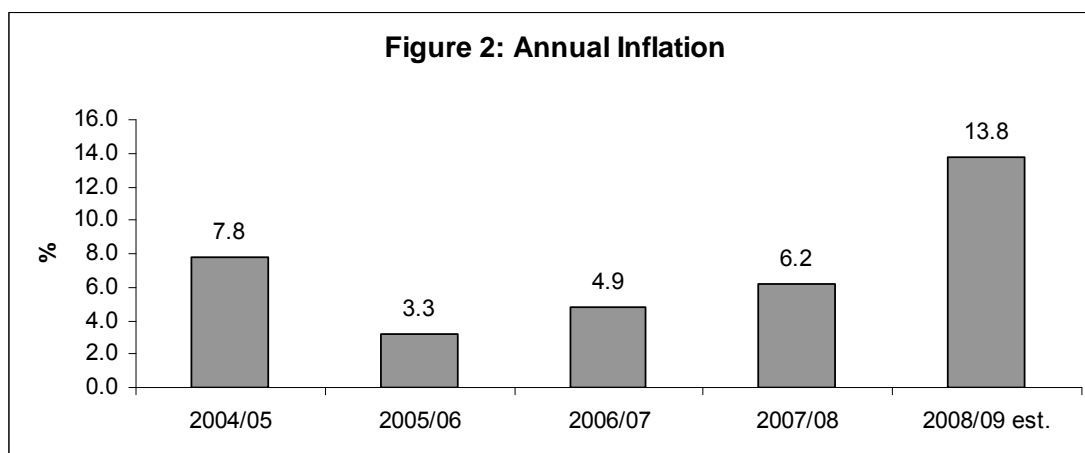
Economic growth in 2004/05–2008/09 fluctuated from year to year, as shown in Figure 1. In 2004/05 and 2007/08, growth exceeded the SDS target rate of 3.0-4.0% per annum. In the intervening years of 2005/06 and 2006/07 growth were at slower rates. The key drivers of growth in 2004/05–2007/08 were the construction sector and various services sectors which benefited from tourism growth (commerce, hotels and restaurants, transport and communications and finance and business services).

In the context of a deteriorating international economic environment, real GDP is estimated to have dropped substantially in 2008/09. In the first half of the year, there was a contraction of 7.6% compared to the same period of 2007/08, led by a downturn in other manufacturing that resulted from production cutbacks by Yazaki. Economic activity also fell in the construction sector following the 2007 South Pacific Games, and in food and beverages manufacturing, agriculture, fishing and commerce. On the expenditure side, consumption fell as price rises outpaced income. Remittances in the first half of 2008/09 were 2.7% higher than the level recorded in the first half of 2007/08, but the inflation rate approached 14%. Private investment continued to drop back to the peak of 2006/07, and exports fell due largely to declines in Yazaki and fish exports. Tourism receipts rose 12.2% in the first half of 2008/09 on the corresponding period the year before, but their purchasing power dropped slightly. Government spending increased, mainly as a result of higher development expenditure; and imports fell due to lower domestic demand. Falls in consumption, private investment and exports outweighed the increase in government spending, and the drop in exports and remittances outweighed the decline in imports.



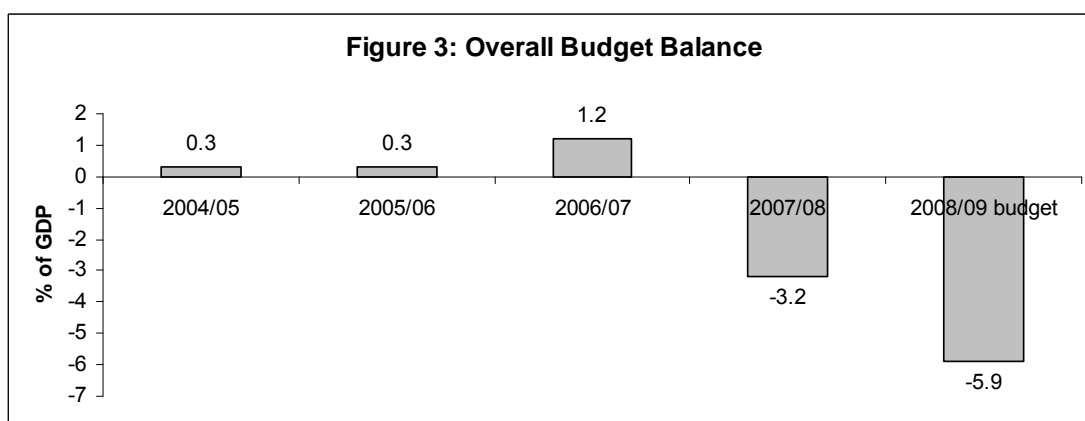
Source: Samoa Bureau of Statistics

The targeted annual inflation rate of 3.0–4.0% was exceeded in 2004/05–2008/09, except for 2005/06 (Figure 2). Domestic food shortages following cyclone Heta contributed to high inflation at the beginning of the period, and higher import prices for food and oil were the main causes of the rapid acceleration in inflation at the end of the period. Inflation in the 12 months to February 2009 reached 13.3% for the overall Consumer Price Index, 20.5% for food items and 5.8% for non-food items.

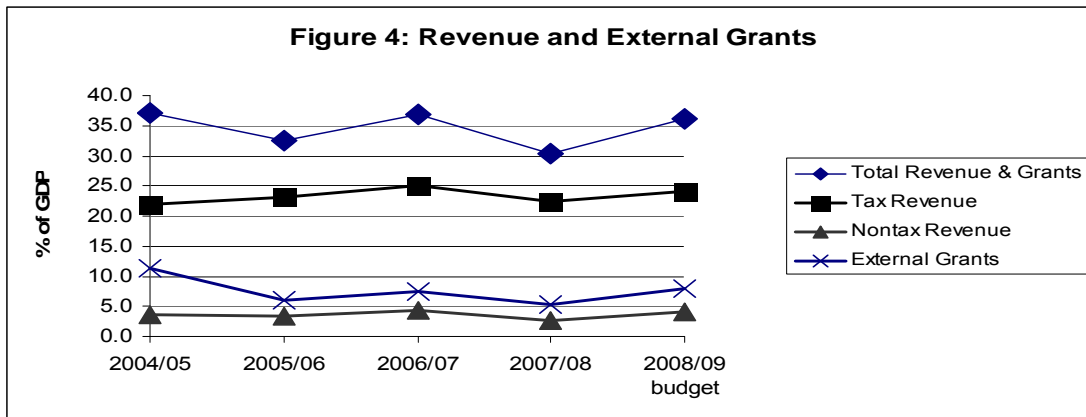


Source: Samoa Bureau of Statistics

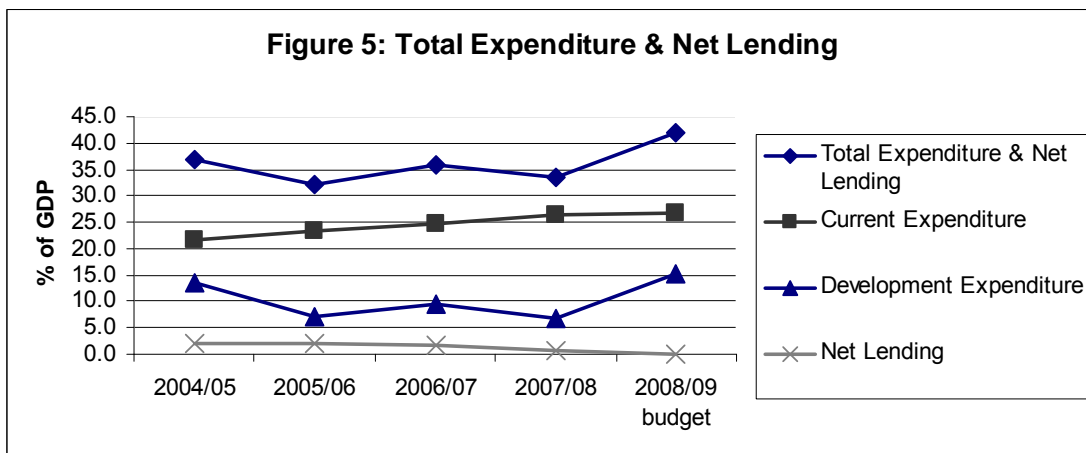
The overall budget balance remained within the target range of 3.5% of GDP for most of 2004/05–2008/09, as shown in Figure 3. In 2008/09, the estimated budget balance was outside the range as a result of a decision to increase capital spending in development projects in public and social infrastructure, including large education and health investments. Tax and non-tax revenue remained fairly steady as a percentage of GDP during 2004/05–2008/09, while external grants declined from the relatively high level recorded in 2004/05 (Figure 4). Total expenditure and net lending remained relatively steady until a rise in 2008/09, when planned development expenditure increased substantially (Figure 5). Current expenditure rose as a share of GDP, with increases in public service wage rates contributing to this expansion, while net lending fell. Current expenditures by function expressed as percentages of total current expenditures (Figure 6) revealed an increase in social services in 2006/07 (i.e. education current expenditure surge in 2006/07 due to South Pacific Games activities) and then returned to 2005/06 level in 2008/09, general services reduced in 2006/07 but now back to 2005/06 level in 2008/09 and economic services increased steadily throughout and closer to 30% in 2008/09.



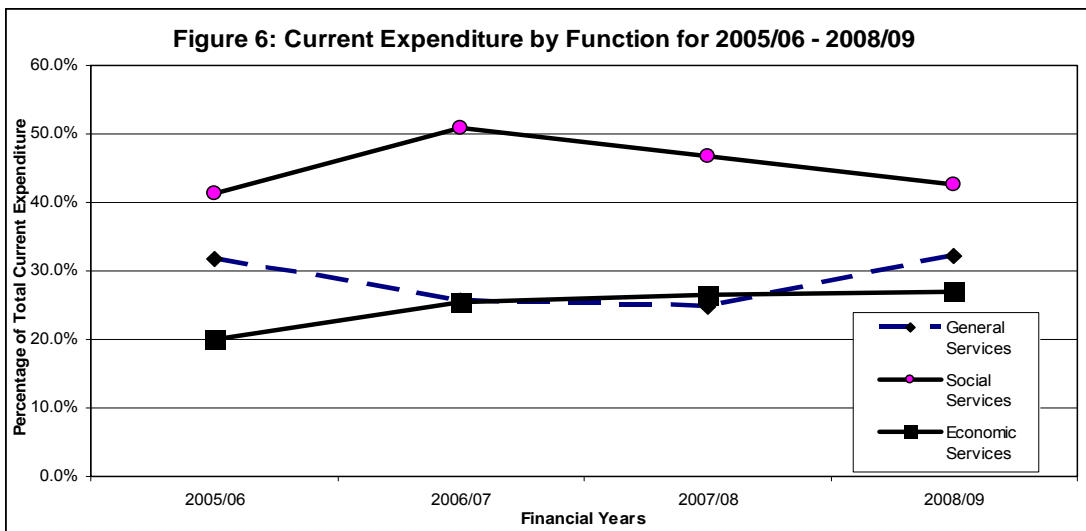
Source: Samoa Bureau of Statistics



Source: Samoa Bureau of Statistics



Source: Samoa Bureau of Statistics



Source: Samoa Bureau of Statistics

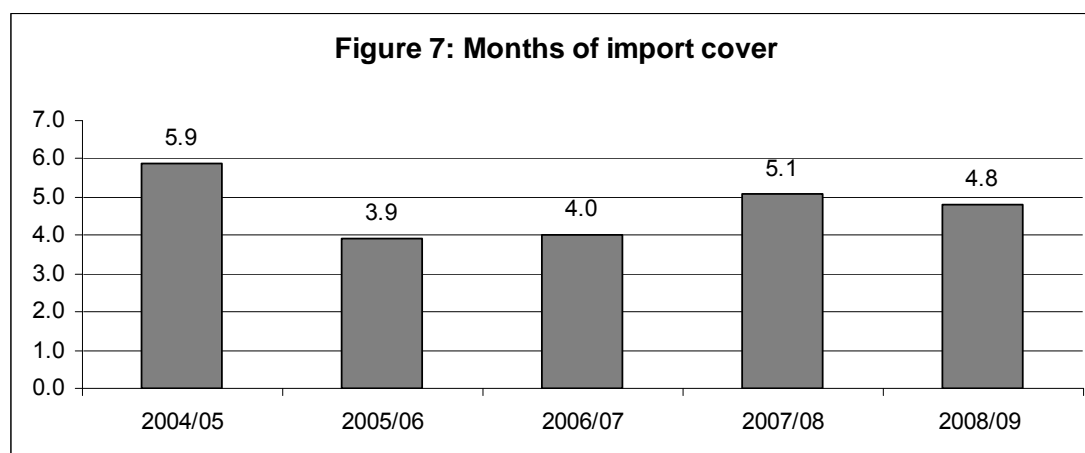
Note: All figures are actual expect 2008/09 which is an appropriated budget figure.

1/ Includes domestically financed development expenditure

2/ Other include Residual: unexplained

3/ Current Expenditure excludes Loan and grant funded expenditure

The import cover of official foreign reserves generally remained in the target range of 4.0-6.0 months throughout 2004/05–2008/09 (Figure 6), thus underpinning exchange rate stability. Some decline in import cover was unavoidable in 2005/06, given a substantial increase in the current account deficit that resulted from the construction boom around the South Pacific Games and increased private credit and consumption. Similarly, a deterioration in the current account caused some loss of import cover in 2008/09.



**Source:** Central Bank of Samoa Bulletin

**Note:** data are for the end of the fiscal year, except for 2008/09, which is the March 2009 figure.

## FISCAL PERFORMANCE IN 2008/09 <sup>1</sup>

The 2008/2009 Budget anticipated an overall deficit of 5.9% of GDP, as shown in Figure 3, with total revenue and grants estimated to rise by 15.8% on the actual 2007/08 level, and total expenditure and net lending estimated to rise by 22.0%. A current surplus of 1.5% of GDP was expected.

Fiscal operations for the first half of the financial year 2008/2009 generated an overall deficit of \$36.2 million, or 5.1% of GDP, which was \$5.8 million below the pro-rata estimate, and which was externally financed (Appendix Table A.1). The current account surplus was \$14.9 million, or 2.1% of GDP, which was above the pro-rata estimate.

These budget outcomes largely reflected shortfalls in development and current expenditure of \$9.7 million and \$8.3 million, respectively. There were delays in implementation of several major loan-funded public investment projects, and expenditures on general administration and social services were below the estimated levels. In contrast, expenditure on works, transport and infrastructure and net lending were above the pro-rata estimates.

Total revenue and grants in the first half of 2008/09 were 1.7% below the pro-rata estimate because of a shortfall in non-tax revenue collection of \$8.6 million, which reflected low collection in the property and investment income category. Tax revenue was above the pro-rata estimate by 1.3% as a result of improved collections of VAGST on imports and sales, excise tax and stamp duty and licenses. These improvements more than offset shortfalls in the collection of domestic excise, import duty and income tax. External grants were in line with the level estimated in the budget.

## ECONOMIC AND FISCAL OUTLOOK

The 2009/10 budget has been formulated in the context of the worst world economic recession since the Great Depression of the 1930s. It is forecast that in 2009 the economies of Samoa's major trading partners will contract—the United States by -2¾%, New Zealand by -2% and Australia by -1½%—and that in 2010 there will be little growth on average. A return to stronger growth is not expected until 2011. Simultaneously, the recession will reduce world inflation. Oil prices have fallen (by about 60% in US dollars in the year to March 2009); and food prices are down (by about 30% in US dollars in the year to March 2009). Inflation is forecast to drop in Samoa's major trading partners.

Against this background of world recession, declining inflation, and a return to world growth, the outlook for Samoa in 2009/10 and the subsequent four years is one of further economic contraction.(Table 1). Consumption is forecast to grow as remittance flows and incomes rise. Private investment is forecast to grow again as confidence improves; and exports are expected to increase as world growth brings rising tourism. Government spending will fall as high levels of development expenditure declines, while imports will start to grow again as domestic spending rises. Inflation is forecast to stabilise at low levels.

In 2009/10, real GDP is forecast to fall by 0.8% as lower private consumption, private investment and exports outweigh a rise in government spending. Consumption is forecast to drop 4.1% due to falls in earned incomes and remittances, including a drop in remittances resulting from the closure of a tuna cannery in American Samoa in September 2009. Private investment is forecast to be 5.0% lower as the global financial crisis makes it harder to borrow overseas, business confidence falls and construction returns to previous average levels. Government spending will be 12.7% higher as development expenditure stays at high levels and recurrent expenditure increases slightly. Exports are forecast to fall 2.5% as the world recession is assumed to hit tourism, other services exports and goods exports particularly hard. Imports increase by 1.1% as domestic demand increases slightly.

Inflation is forecast to drop to 1½% in 2009/10 and to rise to 4% in the following four years. World oil prices are expected to stabilise at levels far below the peak price of \$US140 a barrel. Food prices have fallen from the 2008 peak and are forecast to remain at lower levels, and prices for other commodities and services are forecast to grow at about 4%.

**Table 1: Growth of GDP Expenditure Components (constant 2002 prices)**

	2008/09	2009/10	2010/11	2011/12	2012/13	2013/14
<b>Consumption</b>	-4.3%	-4.1%	-1.2%	1.7%	3.2%	4.1%
<b>Private Investment</b>	-28.6%	-5.0%	6.3%	5.4%	5.5%	5.6%
<b>Government</b>	23.4%	12.7%	-7.6%	-5.4%	1.4%	1.5%
<b>Exports</b>	-10.8%	-2.5%	-0.3%	2.4%	3.0%	3.0%
<b>Imports</b>	-2.0%	1.1%	-4.6%	-0.6%	3.4%	4.1%
<b>Gross Domestic Product</b>	-4.9%	-0.8%	-0.6%	1.1%	2.9%	3.2%

Source: Ministry of Finance.

Externally-induced economic recession in 2009/10 and slow growth in 2010/11 and 2011/12 severely limit growth in Government revenue, while at the same time creating pressure to further increase spending from the levels of 2008/09, in order to boost GDP. However, it is not possible to responsibly finance large increases in spending from domestic sources, when tax revenue is expected to fall further in 2009/10 and when a money financed deficit would compromise macroeconomic stability. The decline in purchasing power of tax revenue in 2008/09–2011/12 underlines the difficulty of maintaining, let alone improving, public service delivery.

Donor assistance to finance some of an increase in expenditure would help mitigate the effects of the world recession on GDP, without putting undue pressure on the balance of payments or fuelling inflation.

The medium-term macroeconomic framework is presented in Table 2. The budget targets and their implications are as follows:

1. Budget balance as a percentage of Gross Domestic Product is above the target and presents a challenging situation where both current expenditures and development expenditures are expected to peak in 2009/10 and then reduce thereafter. The total current revenue is also expected to reduce by 2% and will remain at that level as external grants peak and then reduce thereafter. This situation is expected given the implications of the global crisis we are currently facing on our remittances, tourism and imports. This also provides cases of the need for more funding to support the budget to cover for current expenditures in the medium term, the need to prioritise and reduce current expenditures in the medium term or raise more revenue.
2. Current expenditure as a percentage of Gross Domestic Product is expected to be 26% in 2009/10 which is well below the target of 35%-38%. Despite the current expenditure being below target for the medium term, we expect that the level of current expenditures to GDP will reach the target as the economy recovers from the global crisis in the not so distant future.
3. Personnel costs as a percentage of total current expenditure is just below the target and expected to remain below the target in the medium term;
4. Disbursed Outstanding Debt as a percentage of Gross Domestic Product is slightly above the target and is expected to increase above the target in the medium term given the need to borrow to finance the shortfalls of revenue from the global crisis;

**Table 2: Macroeconomic Framework 2008/09 – 2011/12**

	Target	2008/09	2009/10	2010/11	2011/12
Real GDP (% change)	<b>3.0-4.0%</b>	-4.9%	<b>-0.8%</b>	-0.6%	1.1%
Inflation (%)	<b>3.0-4.0%</b>	13.8%	<b>1.5%</b>	4.0%	4.0%
Budget Balance (% of GDP)	<b>In range of -3.5-+3.5%</b>	-7.0%	<b>-10.6%</b>	-8.7%	-8.0%
Current Expenditure (% of GDP)	<b>35-38%</b>	36.2%	<b>26.3%</b>	25.6%	24.2%
Personnel Costs (% of total expenditure)	<b>30-32%</b>	36.9%	<b>29.0%</b>	29.0%	29.0%
Disbursed Outstanding Debt (% of GDP) <sup>1</sup>	<b>Less than 40%</b>	42.1%	<b>41.0%</b>	49.0%	51.0%
Current Account Balance (% of GDP)		-12.4%	<b>-16.4%</b>	-14.1%	-11.7%
Import Cover (months)	<b>4.0-6.0</b>	4.8	<b>5.3</b>	5.4	5.2
Nominal GDP (\$ million)	1,452.7	1,532.0	<b>1,564.9</b>	1,616.2	1,698.1

**Source:** Ministry of Finance

1. This debt consists entirely of concessional loans that are mostly financed by the Asian Development Bank and the World Bank. These loans have low interest rates and generous grace periods.

<b>Appendix Table A.1 : Samoa - Financial Operations of Central Government, 2005/06-2008/09</b>										
									Provisionals	Pro-rata
\$ million	Actuals	Actuals	Actuals	Actuals	Budget	Jul-Dec	Jul-Dec	Jul-Dec	Jul-Dec	Jul-Dec
	04/05	05/06	06/07	07/08	08/09	2005/06	2006/07	2007/08	2008/09	2008/09
<b>Total Revenue and Grants</b>	<b>408.4</b>	<b>395.1</b>	<b>487.6</b>	<b>441.1</b>	<b>510.8</b>	<b>183.7</b>	<b>222.8</b>	<b>225.9</b>	<b>251.2</b>	<b>255.4</b>
Total Revenue	283.0	323.2	389.2	364.2	400.1	147.8	173.6	187.4	195.8	200.1
Tax	242.2	281.0	331.1	325.5	340.6	130.9	152.8	170.9	174.6	170.3
Non Tax	40.9	42.2	58.1	38.7	59.6	16.9	20.8	16.5	21.2	29.8
External Grants	125.4	71.8	98.5	76.9	110.7	35.9	49.2	38.5	55.3	55.3
<b>Total Expenditure &amp; lending minus repay'ts.</b>	<b>405.4</b>	<b>391.7</b>	<b>472.3</b>	<b>487.7</b>	<b>594.8</b>	<b>187.7</b>	<b>236.1</b>	<b>263.8</b>	<b>287.3</b>	<b>297.4</b>
Current expenditure	236.6	281.9	327.6	383.6	378.4	129.3	164.0	209.8	180.9	189.2
Development expenditure	147.8	86.1	123.7	96.2	216.1	42.4	58.1	48.6	98.3	108.0
Net Lending	21.0	23.7	21.1	7.8	0.4	16.1	14.0	5.4	8.1	0.2
<b>Current surplus/deficit (-)</b>	<b>46.5</b>	<b>41.4</b>	<b>61.6</b>	<b>-19.4</b>	<b>21.8</b>	<b>18.6</b>	<b>9.6</b>	<b>-22.4</b>	<b>14.9</b>	<b>10.9</b>
<b>Overall surplus/deficit (-)</b>	<b>3.1</b>	<b>3.3</b>	<b>15.4</b>	<b>-46.6</b>	<b>-84.0</b>	<b>-4.0</b>	<b>-13.3</b>	<b>-37.9</b>	<b>-36.2</b>	<b>-42.0</b>
<b>Financing.</b>	<b>-3.1</b>	<b>-3.3</b>	<b>-15.4</b>	<b>46.6</b>	<b>84.0</b>	4.0	13.3	37.9	36.2	42.0
External financing (net)	15.8	6.2	7.6	11.8	91.5	2.2	7.4	6.2	39.5	45.7
Disbursement	27.6	19.2	21.5	28.5	105.4	8.1	14.0	14.5	47.9	52.7
Amortization	11.8	13.0	13.9	16.7	13.9	5.9	6.6	8.3	8.4	7.0
Domestic financing (net)	-18.9	-9.5	-22.9	34.8	-7.5	1.8	5.9	31.7	-3.3	3.8
Banking System	-18.7	11.0	-11.2	11.9	0.0	1.5	-4.5	28.5	0.6	0.0
Nonbanks and others	-0.2	-20.5	-11.7	22.9	-7.5	0.3	10.5	3.2	-3.9	0.0
<b>GDP</b>	<b>1099.5</b>	<b>1215.1</b>	<b>1322.7</b>	<b>1452.7</b>	<b>1413.5</b>	<b>613.5</b>	<b>647.4</b>	<b>748.7</b>	<b>709.4</b>	<b>709.4</b>
(In % of GDP)										
Total revenue and grants	37.1	32.5	36.9	30.4	36.1	30.0	34.4	30.2	35.4	36.0
Of which:										
Tax and non tax revenue	25.7	26.6	29.4	25.1	28.3	24.1	26.8	25.0	27.6	28.2
Expenditure and net lending	36.9	32.2	35.7	33.6	42.1	30.6	36.5	35.2	40.5	41.9
Current expenditure	21.5	23.2	24.8	26.4	26.8	21.1	25.3	28.0	25.5	26.7
Development expenditure	13.4	7.1	9.3	6.6	15.3	6.9	9.0	6.5	13.9	15.2
Current balance	4.2	3.4	4.7	-1.3	1.5	3.0	1.5	-3.0	2.1	1.5
<b>Overall balance</b>	<b>0.3</b>	<b>0.3</b>	<b>1.2</b>	<b>-3.2</b>	<b>-5.9</b>	<b>0.7</b>	<b>2.1</b>	<b>5.1</b>	<b>5.1</b>	<b>5.9</b>
External financing (net)	1.4	0.5	0.6	0.8	6.5	-0.4	-1.1	-0.8	-5.6	-6.4
Domestic financing (net)	-1.7	-0.8	-1.7	2.4	-0.5	0.2	-0.7	3.8	0.1	0.0

Source: Samoa Bureau of Statistics and Ministry of Finance.