FA'AVAE I LE ATUA SAMOA

GOVERNMENT OF SAMOA

FISCAL STRATEGY STATEMENT
2018/2019 BUDGET

MINISTRY OF FINANCE

MAY 2018

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FISCAL STRATEGY STATEMENT
2018/19 BUDGET

I. REPORTING REQUIREMENTS

The Public Finance Management Act 2001 stipulates the principles of responsible fiscal management as well as the reporting requirements associated with the presentation of the budget. The reporting requirements include, under Section 18, the budget address, and a statement of the projected estimated revenues and expenditures for the budget year and the two forward years. 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 "Strategy for the Development of Samoa" (SDS), an explanation of the reasons for any significant differences between the current economic and financial situation and the targets set out in the SDS.

The 2016/17-2019/20 SDS is for a period of four years with the theme; "*Accelerating Sustainable Development and Broaden Opportunities for All*".

II. REVIEW OF FISCAL AND ECONOMIC PERFORMANCE IN THE LAST 5 YEARS, 2012/13 TO 2016/17

Economic Performance

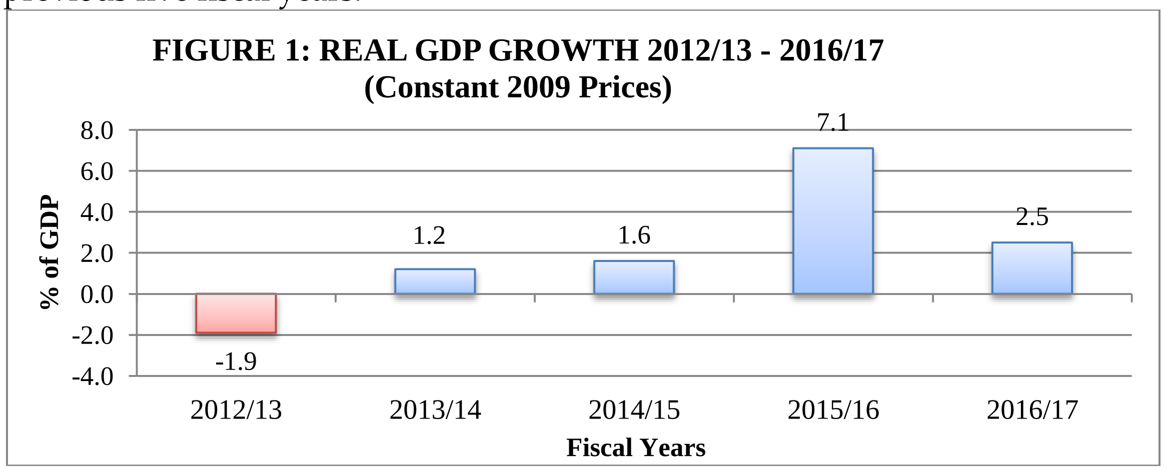
The economy recorded a 1.9 percent in FY2012/13 due to the unfavorable impacts of Cyclone Evan which hit Samoa in December 2012. However, this was reversed as a result of recovery efforts following the cyclone, preparations for the UN Small Island Developing States (SIDS) Conference and the construction of major hotels (Return to Paradise Resort, Taumeasina Island Resort, Sheraton Samoa Aggie Greys Resort and Sheraton Samoa Aggie Greys Hotel and Bungalows) which led to a positive 1.2 percent growth in FY2013/14.

This positive trend continued into FY2014/15 when the economy grew by 1.6 percent largely as a result of continued recovery works and continuation of SIDS related construction as well as preparations for the Commonwealth Youth Games and the All Blacks/Manu Samoa game which Samoa hosted. This in turn, boosted tourism, commerce, transport, communication, electricity and water sectors.

In FY2015/16, the economy grew strongly registering a 7.1 percent growth rate - its strongest growth rate over the previous five years. This was driven mainly by the sharp improvement in the Fishing industry with the entrance of the newly established Apia Deep Sea Fishing Ltd which also boosted fish exports. As well, the opening of two major tourism developments; Sheraton Samoa Aggie Greys Hotel and Taumeasina Island Resort as well as ongoing Government infrastructural projects (rehabilitation of the aviation infrastructure, enhancing and upgrading of roads, ports infrastructure, etc) all contributed to this growth.

Growth in FY2016/17 eased off to a more normal trend registering a 2.5 percent marking the completion of the three year cyclone recovery program, tailing off of major construction works as well as the slowdown in other industries including Fishing, Accommodation and Restaurants.

Figure one (1) below further illustrates the real GDP growth rates over the previous five fiscal years.



Source: Ministry of Finance and Samoa Bureau of Statistics

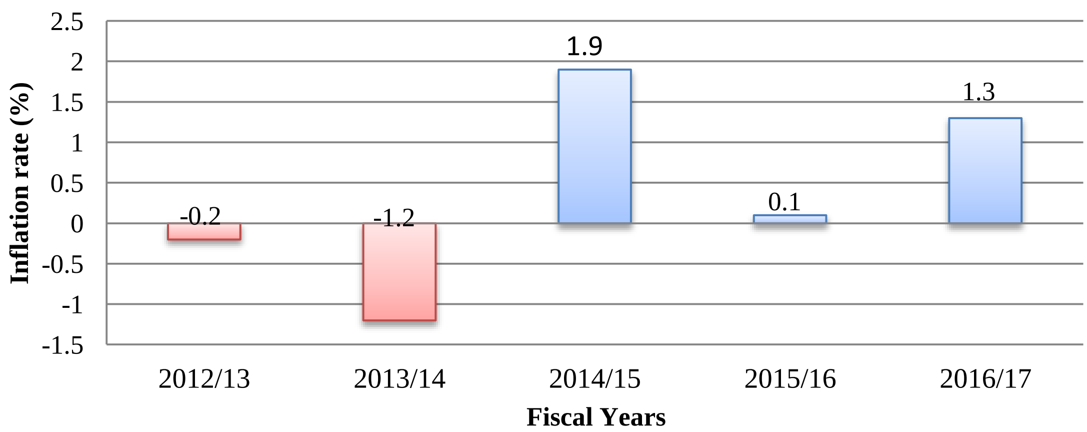
Inflation

Figure 2 presents the annual inflation rate from FY2012/13 to FY2016/17. Inflation remained well below the medium term target range of 3.0 – 4.0 percent over the five year period.

The fall in prices of international food and oil in FY2012/13 caused a 0.2 percent inflation rate which translated to reductions in the domestic prices of food, non-alcoholic beverages, housing, water, electricity, gas and other fuels. A similar trend was experienced in FY2013/14 when inflation rate registered a 1.2 percent due to continuing decreases in international oil prices.

In FY2014/15, the inflation rate gradually increased reaching 1.9 percent driven largely by the rise in prices of health products, restaurants, hotels, clothing and footwear. It eased in FY2015/16 to 0.1 percent followed by a marginal increase to 1.3 percent in FY2016/17 due to the gradual rise in global oil prices.

FIGURE 2: ANNUAL INFLATION 2012/13 - 2016/17

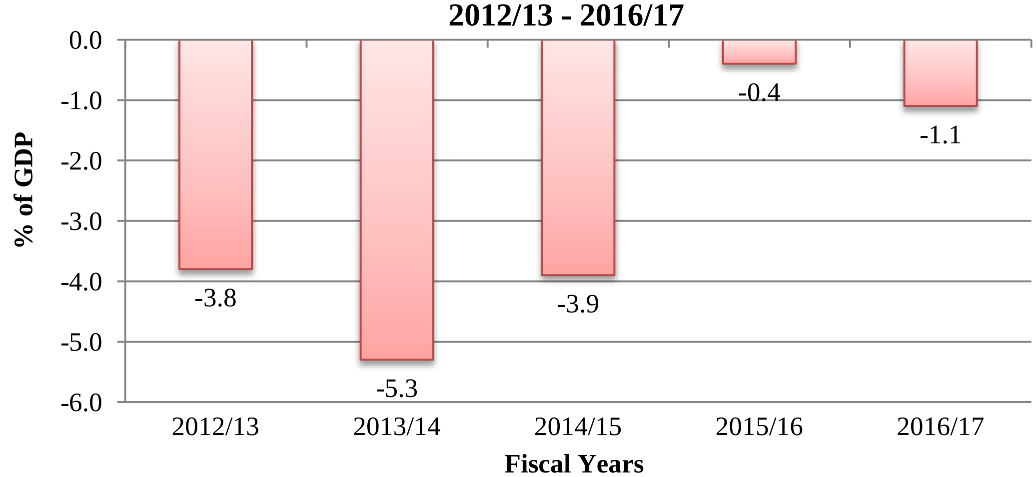


Source: Ministry of Finance and Central Bank of Samoa

Budget Balance

The fiscal deficit as a percentage of GDP was well managed within the five year period recording a marked improvement from 3.8 percent in FY2012/13 to 0.4percent in FY2015/16. This was achieved mainly as a result of the commitment to rein in spending and tailing off of rehabilitation works. A slight increase to 1.1 percent in FY2016/17 was caused mainly by the implementation of major Government infrastructural investment projects.

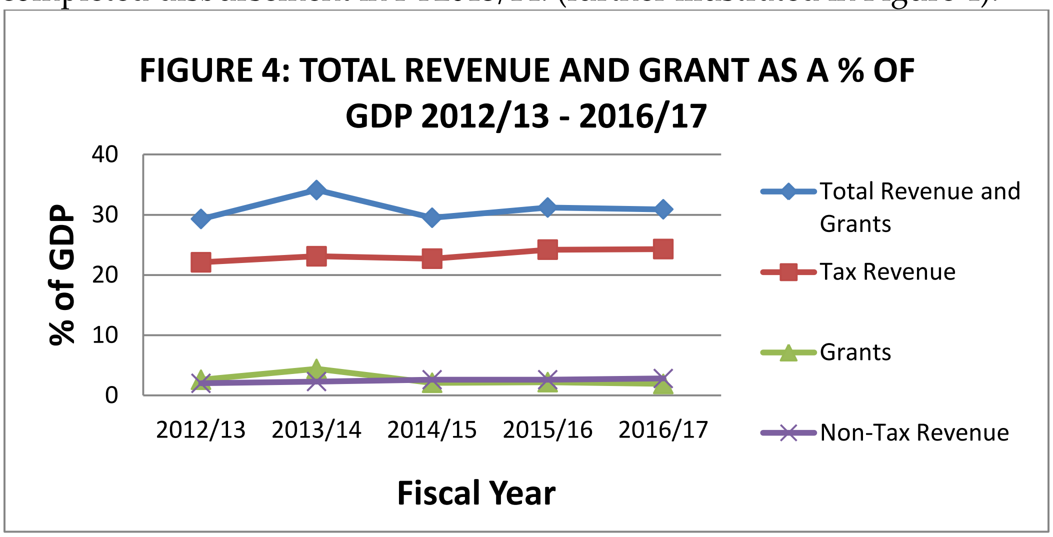
FIGURE 3: BUDGET BALANCE AS A % OF GDP 2012/13 - 2016/17



Source: Ministry of Finance and Samoa Bureau of Statistics

Revenue and Grants

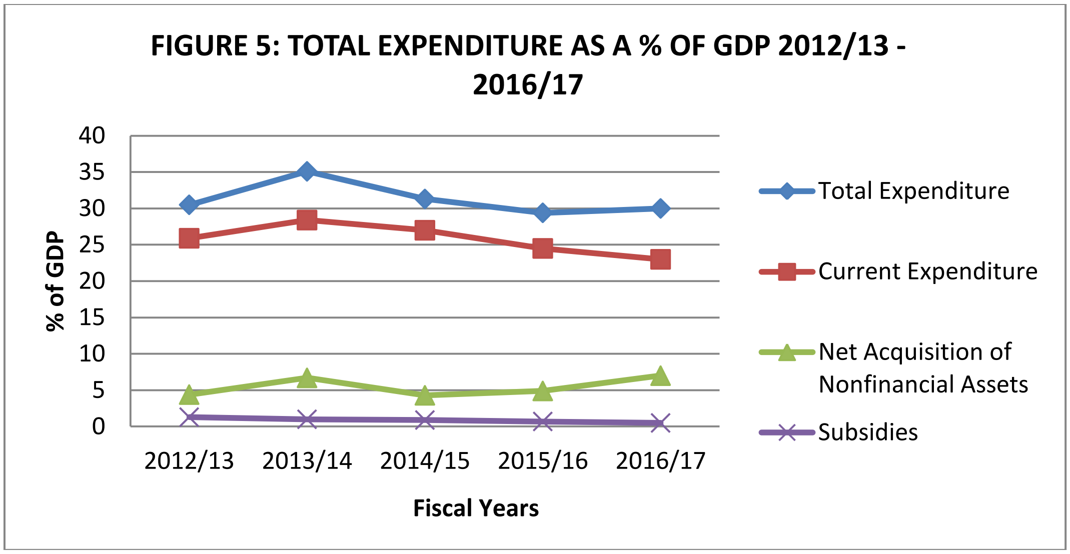
Tax Revenue increased gradually from 22.1 percent to 24.2 percent of GDP from FY2012/13 to FY2015/16. In FY2016/17, it increased slightly to 24.3 percent. **External Grants** as percentage of GDP peaked in FY2013/14 at 4.4 percent largely as a result of increased funding from external assistance for the three year cyclone recovery program. It dropped to 2.1 percent in FY2014/15 followed by 2.2 percent in FY2015/16 and 1.9 percent in FY2016/17. **Other Revenue** increased consecutively over three years from FY2012/13 to FY2014/15, remained constant in FY2015/16 and slightly picked up again in FY2016/17 to stand at 2.8 percent of GDP. Overall total **Revenue and Grants** recorded a steep drop in FY2014/15 as a direct result of the drop in External Grants when Samoa's cyclone recovery funds completed disbursement in FY2013/14. (further illustrated in Figure 4).



Source: Ministry of Finance and Samoa Bureau of Statistics

Expenditures

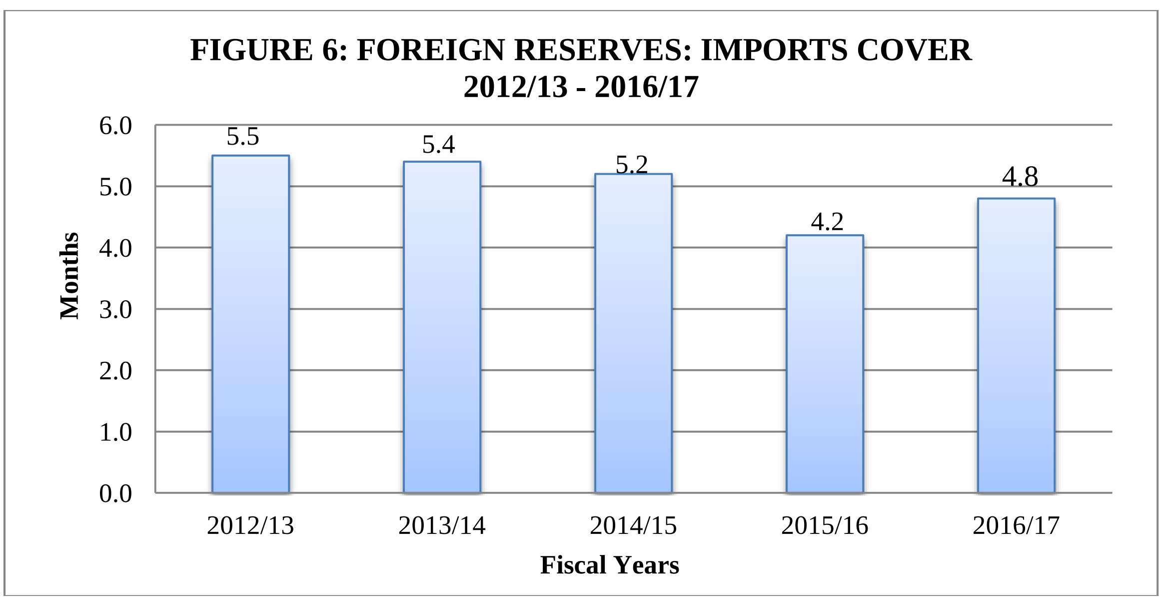
Current Expenditure as percentage of GDP dropped from FY2013/14 to FY2016/17. This drop was due to Government imposing a 10 percent productivity dividend across all ministries and corporations and a 3 percent dividend for education and health agencies. **Net Acquisition of Nonfinancial Assets** saw a gradual increase from FY2014/15 to FY2016/17 as shown in Figure 5 below. The increase was largely due to the impacts of major Government development projects under the cyclone recovery program as well as on-going projects such as the aviation project, the Parliament house, the construction of the Leonē Bridge, transport sector projects and the new Prison facility. These developments are major factors for the slight increase in **Total Expenditure** in 2016/17.



Source: Ministry of Finance and Samoa Bureau of Statistics

Foreign Reserves

Official foreign reserves remained within the 4 – 5 months range during the previous five years. This was largely driven by an increase in the amount of grants and loans on concessional terms to support tropical cyclone recovery efforts and the different activities relating to the hosting of the SIDS Conference in 2014. Reserves dropped to 4.2 months in FY2015/16 and slightly improved to 4.8 months in FY2016/17 due to the tailing off of major developments and events.



Source: Ministry of Finance and Central Bank of Samoa

Public Debt

Total public debt as percentage to GDP stood at 49 percent which is below the target threshold of 50% in FY2016/17, as a number of major projects were at their final stages, such as SACEP and Health Sector projects as well as Government's stringent monitoring of its debt position. Prior to FY2016/17, debt as a percentage of GDP exceeded the threshold largely as a result of the new borrowings in 2014 for the Airport Terminal rehabilitation projects as well as other concessional credit funding for the reconstruction work following Cyclone Evan. Debt Service as percentage of GDP remained below 3 percent from 2012/13 to 2014/15, however it exceeded the target rate of 3 percent in FY2015/16 and FY2016/17 due to new loans commencing repayments.

Table 1: Official Public Debts

Years	**2012/13**	**2013/14**	**2014/15**	**2015/16**	**2016/17**
Official Public Debts (million tala)	990.4	1,015.5	1,126	1,080	1,047
Official Public Debts as % of GDP (Target below 50%)	54	54	58	53	49
Total Debt Servicing (million tala)	38.8	46.2	53.9	66.5	66.6
Debt Servicing as % of GDP (Target 2% - 3%)	2.1	2.5	2.8	3.2	3.1

Source: Ministry of Finance

III. ECONOMIC OBJECTIVES

Fiscal Policy

To ensure macroeconomic stability is achieved in the medium to long term, Government will continue to maintain the following fiscal targets and objectives:

a) Aggregate current expenditure to be maintained within a range of 35 – 38 percent of GDP over the forward estimate cycle, to ensure liquidity in the economy is sufficient to foster private sector growth and employment;
b) Public Debt outstanding to be kept below 50 percent of GDP in the medium term;
c) Personnel costs as a percentage of total current expenditure to be constrained to a range of 40 – 45 percent so as to reflect Government's

commitment to improve service delivery associated with the implementation of performance budgeting;

d) Budget Deficit to be maintained at a rate not more than 3.5 percent of GDP;
e) Improve performance of State Owned Enterprises (SOE) to avoid extra burden on Government budget through default loans;
f) Improve compliance in revenue collection;

To maintain economic growth at a positive level, the Government will continue to put in place sound policy measures that will underpin macroeconomic stability. These measures will have the impact of cushioning the economy from future exogenous shocks and generating fiscal space to be allocated to priority sectors. Government will also reprioritize expenditures to areas that generate high returns and more employment. Emphasis will also be given to improve the efficiency and cost-effectiveness of public services delivered through Government agencies and SOEs.

In the medium term, the Government's position remains on tightening expenditure and focus on quality spending. On the debt level, Government is committed to achieving the threshold of 50 percent of GDP.

Monetary Policy

Fiscal consolidation will be supported by an accommodative monetary policy stance. This policy mix is currently consistent with the low inflation environment and more upbeat prospects for growth. In addition, this balances the desire to support economic activity whilst rebuilding fiscal buffers to handle external shocks and natural disasters. While the current level of the exchange rate is broadly in line with current economic conditions, the main challenge is to maintain gross foreign reserves in the short to medium term to a comfortable level (of around 4.0 – 6.0 months of imports), especially taking into account the risk of natural disasters.

On the monetary policy side, the outlook for commercial bank lending to the private sector, based on the assumption of continuing easing monetary policy stance in the next 3 years, is a steady and incremental growth in lending by commercial banks in general in FY2017/18/ to FY2018/19 from strong growth in FY2016/17 as commercial banks look to reassess their lending activities by prioritising well securitised portfolios while reducing their credit exposure overall. Credit growth rate is however, expected to pick up again in subsequent years (FY2019/20 onwards). As a result of strong external flows, the growth rate of broad money supply is expected to rise in 2017/18 but is expected to gradually fall in 2018/19 as domestic credit growth stabilises and inflow of net foreign assets return to its steady state.

In this regards, the Central Bank will

i. continue with easing monetary policy stance and to ensure that both commercial banks' deposit and lending rates are kept at low levels;
ii. adequately provide liquidity to support commercial banks and their operations;
iii. continue to assist local money transfer operators (MTOs) in finding sustainable avenues to remit funds back to Samoa and lastly;
iv. to continue to promote financial stability and develop the financial system consistent with the domestic absorptive capacity and demand.

IV. ECONOMIC AND FISCAL OUTLOOK

Global Economic Outlook

The International Monetary Fund's (IMF) World Economic Outlook (WEO) Update in April 2018 noted that a global economic growth in the medium term will be strong. This was based on the collective outlook of advanced economies as a group that it will continue to expand above their potential growth rate for the current and the next year. It is also reported that Aggregate growth in emerging markets and developing economies is projected to firm further. Global growth is therefore expected to grow at around 3.9 percent in 2018 and 2019. This is mainly due to the rapid growth in the Euro area, Japan, China and the United States. In the medium term, global growth is projected to decline at around 3.7 percent.

For Samoa's main trading partners, Australia, New Zealand and Fiji, their economies are expected to grow at around 3.1 percent, 2.9 percent and 3.5 percent respectively in the medium term. This will definitely have a positive impact on Samoa's trade with them.

Samoa Economic Outlook

Over the medium term, growth remains robust and is projected to **moderate to 1.8 percent in FY2017/18**, due to the negative impact of the closure of the Yazaki Samoa manufacturing plant in August 2017.

Growth is expected to **rebound to 3.3 percent in FY2018/19**, as the two new businesses occupying the old Yazaki Samoa building scale up operations and several infrastructure projects, including new bridges, road extensions, the new terminal building are completed and preparations for Samoa's hosting of the

Pacific Games. In addition, the expected positive impact from the Tui-Samoa Cable already commissioned will add value to the communication sector and will also generate opportunities for the private sector to grow. Health and Education are also expected to benefit from this Cable which allows delivery of e-Health and e-Education.

In FY**2019/20, growth is projected to increase to 3.7 percent**, driven by tourism related sectors as Samoa hosts the Pacific Games in July 2019. It is then expected to slowdown in **FY2020/21 at around 3.5 percent** mainly from the Apia Waterfront project which will support the tourism development.

<u>Forward Estimates: Revenue & Expenditure</u>

Total Revenues is expected to improve in the medium to long term as we move into the implementation of revenue measures and improving compliance. **Total Expenditure** on the other hand, in line with the implementation of the fiscal consolidation it is forecasted to remain constant in real terms over the medium term.

The macroeconomic targets and its implications are as follows (further illustrated in Table 2):

1) The Fiscal Deficit will remain at 3.5 percent of GDP in FY2018/19 and over the medium term. Notwithstanding that target, the Government will continue with its fiscal consolidation strategy to ensure the economic fundamentals support macroeconomic stability;

2) Raising total revenues will be a key component of the fiscal consolidation exercise. This will be achieved through the implementation of the revenue reforms already underway. As well, focus will concentrate on improving compliance which will be enhanced with the arrival of the scanner;

3) Total current expenditure as a percentage of GDP is expected to remain below the target rate;

4) Total public debt level as a percentage of GDP is projected to maintain below the 50% threshold in supporting the fiscal consolidation. This is due to the strong coordination, monitoring and new policy initiatives by Government to help lessen the burden put on the financing needs.

Table 2: Macroeconomic Framework FY2017/18 – FY2020/21

	Target	2017/18	2018/19	2019/20	2020/21
Real GDP (% change)	3.0%-4.0%	1.8	3.3	3.7	3.5
Budget Balance (% of GDP)	Deficit: Not more than 3.5% of GDP	-3.5	-3.4	-3.3	-3.2
Total Current Expenditure (% of GDP)	35%-38%	23.7	21.6	21.2	22.1
Personnel Costs (% of total current expenditure)	40% - 45%	47.5	48.4	47.6	47.8
Official Public Debts as % of GDP	Less than 50%	47.4	44.1	38.8	34.7
Debt Servicing (% of GDP)	2% - 3%	3.4	3.5	3.3	3.3
Nominal GDP ($ billion tala)		2.27	2.38	2.54	2.66

Source: Ministry of Finance

1. This debt consists largely of concessional loans;
2. Personnel costs and Total Current Expenditures are GFS estimates from Budget Division.

V. PUBLIC DEBT - LONG TERM PROJECTIONS

Total public debt to GDP ratio for FY2016/17 was 49.1 percent, which is below the target of 50 percent. This is a result of the fiscal consolidation with the focus in quality spending and improved revenue collection through improved compliance. In the medium term, the debt to GDP ratio is expected to remain below the target threshold as the Government continues with the budget consolidation measures. In addition, grants from development partners will continue which will finance major infrastructure projects such as roads, Matautu port, Vaisigano Catchment project and the Vaisigano Bridge.