GOVERNMENT OF SAMOA

FISCAL STRATEGY STATEMENT BUDGET 2013/2014

MINISTRY OF FINANCE

30 MAY 2013

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FISCAL STRATEGY STATEMENT
BUDGET 2013/14 – 2015/16

I. REPORTING REQUIREMENTS

The Public Finance Management Act 2001 specifies principles of responsible fiscal management and sets out reporting requirements for 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 – 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 "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, 2012/13-2015/16: Boosting Productivity For Sustainable Development.*

II. ECONOMIC AND FISCAL OBJECTIVES

Samoa"s economic growth has been volatile but recovering slowly after a series of external shocks over the past several years, which includes the global economic crisis, a devastating tsunami in 2009 and a strong tropical cyclone in December 2012. Despite these setbacks, government has continued to pursue a broad based macroeconomic policy mix through prudent fiscal measures and an accommodative monetary policy. Economic growth in 2010/11 and 2011/12, saw continued slow growth averaging 1.7% per annum and a projected pre-cyclone growth of 2.3% for 2012/13. However, cyclone Evan in December 2012inflicted substansive damage disrupting economic activities and therefore set back the projected growth for 2012/13 to only 1.3%.

The need to stimulate economic activities as well as rebuilding after tropical cyclone Evans over the next financial year forms the basis for an expansionary fiscal stance in 2013/14. The recovery and reconstruction activities over is intended to provide an economic stimulus. At the same time, maintain an accommodative stance to ensuresufficient credit to the private sector, containing inflation and managing reserves to underpin a competitive exchange rate.

In addition, the preparation to host the Small Islands Developing States (SIDS) global conference in 2014 will also provide a short term boost to the domestic economy.

Agriculture and tourism offer great potential for growth in domestic consumption, exports and employment creation.

To ensure macroeconomic stability in the medium to long term, Government will continue to pursue the achievement of the following fiscal targets:

a) Aggregate current expenditure to be maintained within a range of 35 – 38% of GDP over the forward estimate cycle, to ensure liquidity in the economy is sufficient to foster private sector growth and employment;
b) Net Public Debt outstanding to less than 50% of GDP;
c) Personnel costs as a percentage of total current expenditure to be constrained to a range of 40 - 41% so as to reflect government‟s commitment to improve service delivery associated with the implementation of performance budgeting;
d) Budget Balance to be maintained at the rate of 3.5% of GDP.
e) Prioritize spending for cyclone recovery in accordance with the Cyclone Recovery Framework as well as work plans submitted by each sector;
f) Improved performance of SOE‟s to avoid extra burden on Government budget through default loans;
g) Promote greater efficiencies in revenue collection.

III. REVIEW OF FISCAL AND ECONOMIC PERFORMANCE IN THE LAST 5 YEARS, 2008/09 TO 2012/13

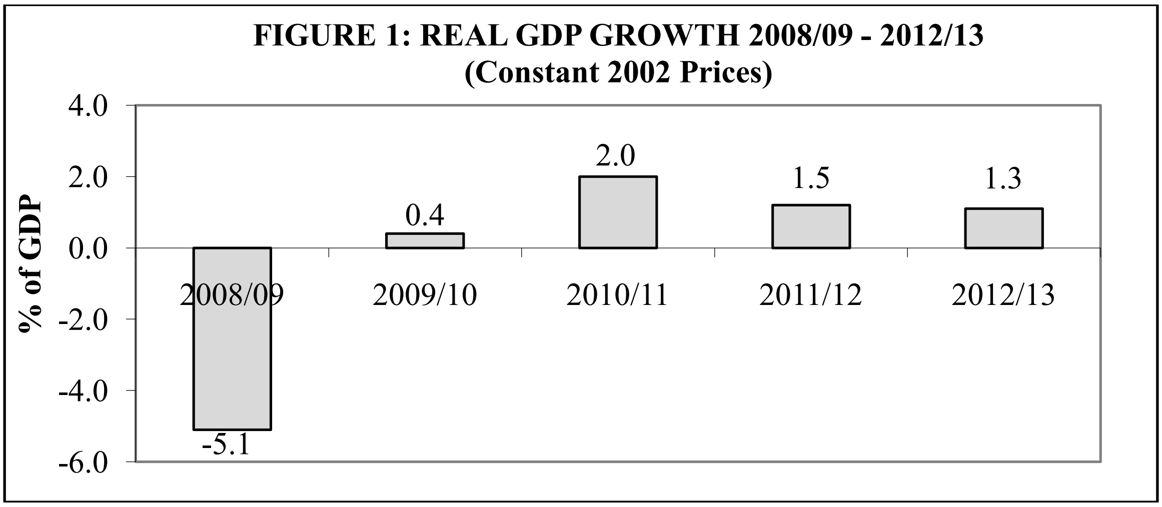
Samoa‟s economy experienced a sharp downturn of -5.1% in 2008/09 as a result of the global financial crisis adversly affecting tourism, manufacturing and remittances. In particular, Yazaki production of automotive wire harnessing declined throughout this period driven by the drop in demand for vehicles caused by the impact of global recession.

Economic growth improved slightly to 0.4% in 2009/10 boosted by reconstruction work following the tsunami of September 2009. The reconstruction works on infrastructure, tourism and housing cushioned the economy to some extent from the adverse impact of the global financial crisis. The widening and maintenance of roads, improvements to drainage and sanitation and several building construction also contributed to economic growth throughout this period.

In 2010/11, economic growth increased further to 2.0%. This was largely driven by continued reconstruction works following the tsunami. . Growth in other industries such as commerce, transport & communication and hotels & restaurants also contributed.

Economic growth rate slowed-down to 1.5% in 2011/12 as reconstruction work tailed off. However, construction of the national hospital as well as the preparation for the celebration of Samoa‟s 50th independence anniversary leveled the downward trend.

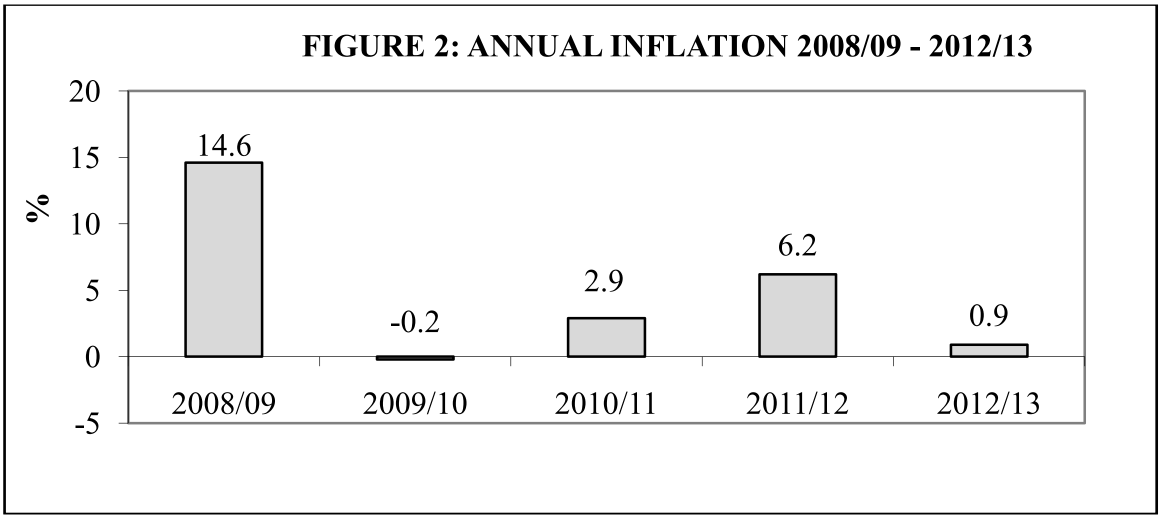
Following the devastation caused by cyclone Evan, economic growth is projected to be only about 1.3% in 2012/13. This revised projected rate is down from pre-cyclone forecast of 2.3%.



Source: Ministry of Finance and Samoa Bureau of Statistics

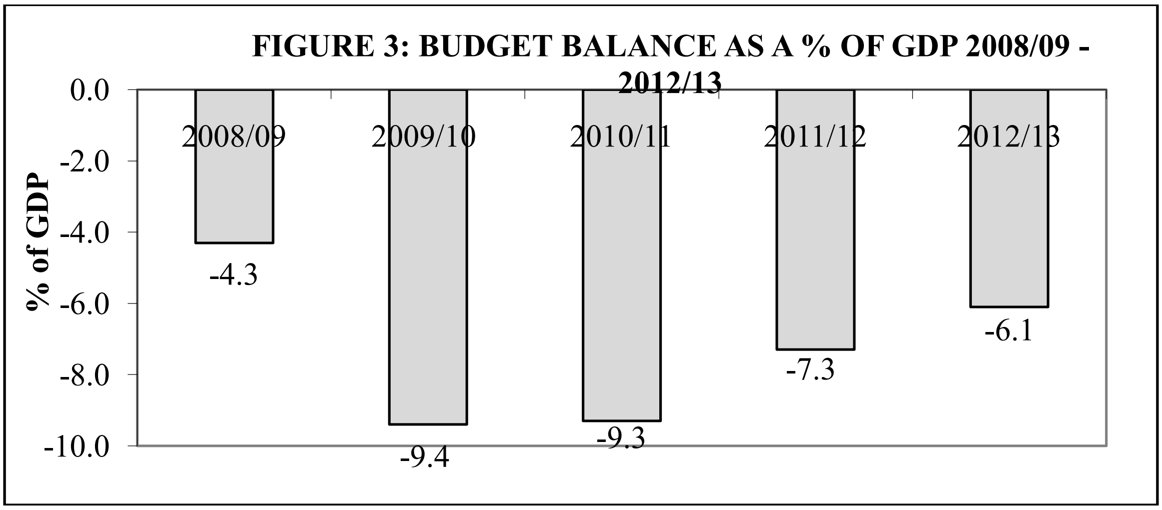
The annual inflation trend in Figure 2 shows that the target rate of 3% to 4% has been largely exceeded. The high inflation rate of 14.5% in 2008/09 reflected the rise in world food and fuel prices, and remitted into domestic prices. In 2009/10, inflation dropped to -0.2% due to a decline in world food prices. The overall increase in the annual inflation rate in 2010/11 was largely driven by the increase in electricity prices, which was caused by rising fuel prices, as well as an increase in water rates. Both of these increases filtered through to household consumption expenditure. In 2011/12, annual inflation rate rose to 6.2%. This was largely influenced by the decline in the supply of agricultural products at the Fugalei market coupled with the continuing increase in fuel prices.

Annual average inflation rate stood at 1.2% at end March 2012/13. This represented a decline of 4.4 percentage points from end March 2011/12. This result was driven by the decline in the „housing, water, electricity, gas and other fuels", „food and non alcoholic beverages" and „transport" components. Inflation is projected to drop to 0.9% at end 2012/13 as the effects of imported food prices and oil prices have dissipated.



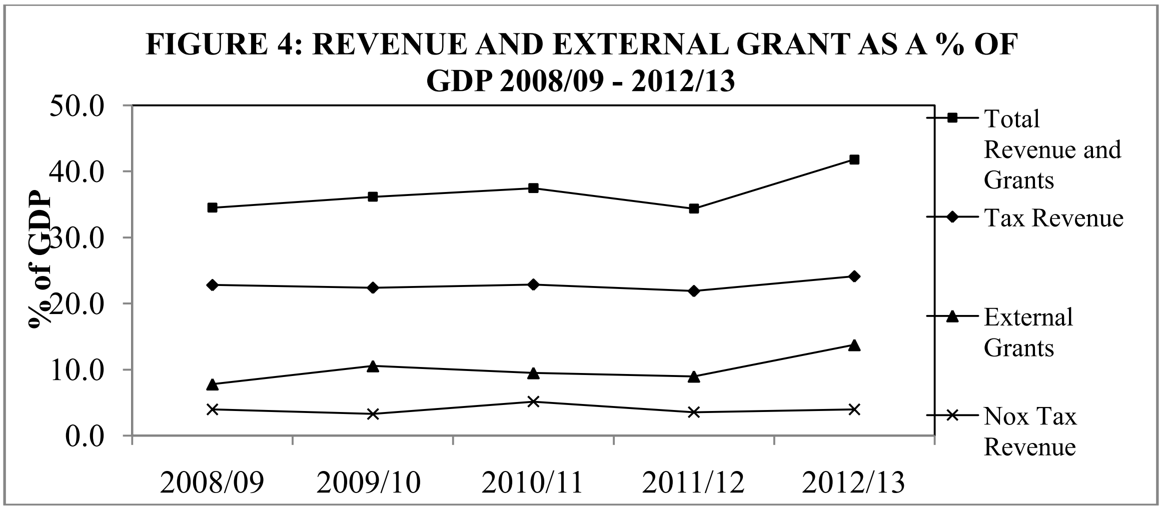
Source: Ministry of Finance and Samoa Bureau of Statistics

The overall budget deficit of 4.3% of GDP in 2008/09 was well above the target level of 3.5%. The overall deficit increased considerably in 2009/10 and 2010/11 (to 9.4% and 9.3% respectively) as a result of the fiscal stimulus implemented in response to the global economic crisis and the tsunami reconstruction spending. These were largely funded by grants and loans on concessional terms mainly from World Bank, ADB, Japan, EU, New Zealand, Australia and China. The winding down of the tsunami linked rehabilitation efforts led to decline in the overall budget deficit to 7.3% and 6.1% in 2011/12 and 2012/13 respectively.



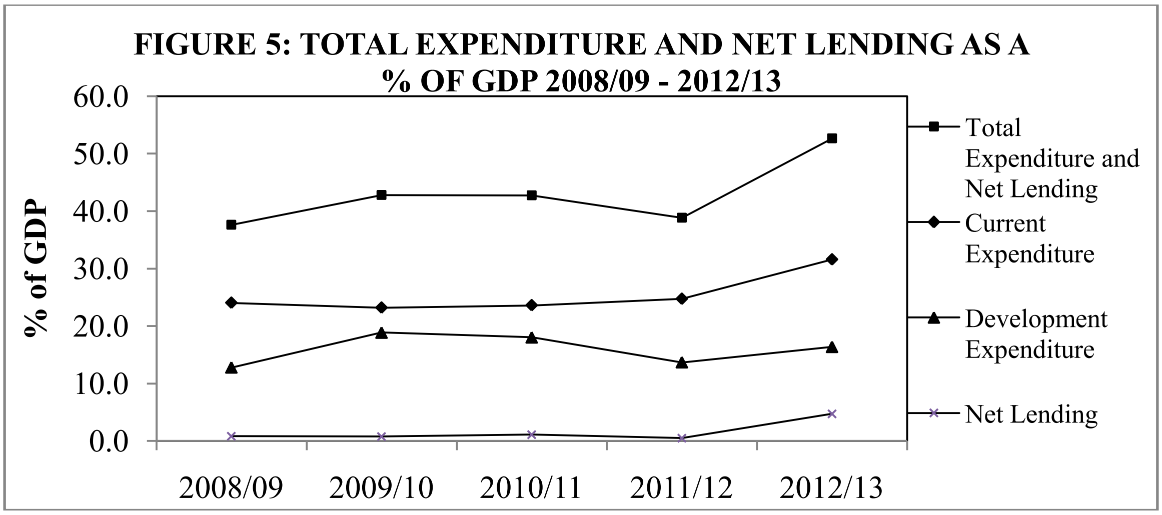
Source: Ministry of Finance and Samoa Bureau of Statistics

Tax Revenue as a percentage of GDP remained around 22% from 2008/09 to 2010/11, before dropping slightly in 2011/12 but has gradually increased in 2012/13. Non Tax Revenue as a percentage of GDP continued to vary each year between 2008/09 and 2012/13, increasing in some years and falling in others. External grants as a percentage of GDP increased from 2008/09 to 2009/10, gradually declined in 2010/11 to 2011/12 before a strong increase in 2012/13 for the cyclone recovery program.



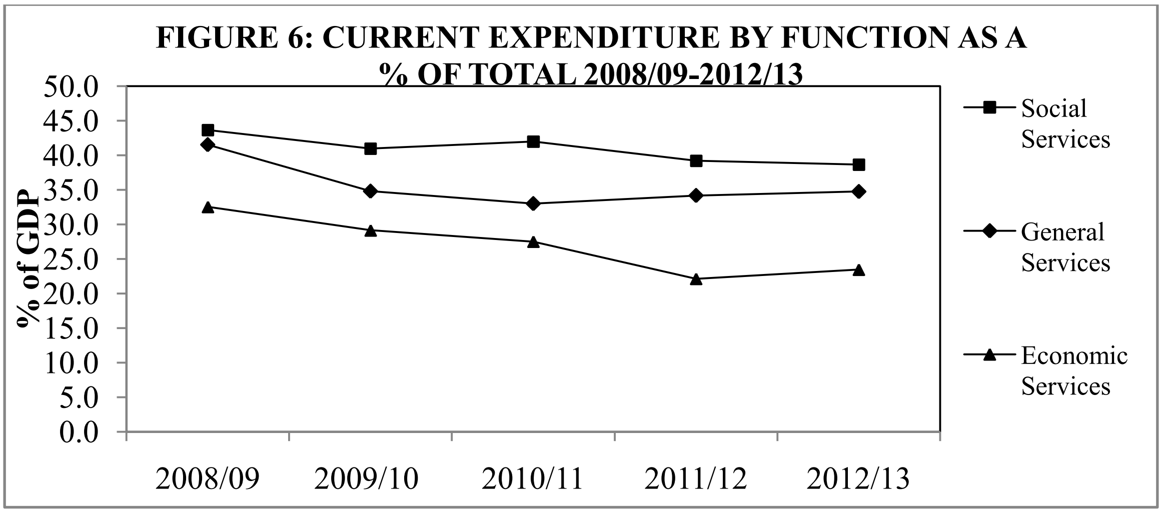
Source: Ministry of Finance and Samoa Bureau of Statistics

Current expenditure as percentage of GDP declined steadily from 2008/09 to 2009/10 as government reduced recurrent budget in the face of the global economic situation. The two natural disasters in 2009 and 2012 contributed largely to the growth of current expenditure throughout to 2012/13. Development expenditure as percentage of GDP increased from 2008/09 to 2009/10 due to the tsunami rehabilitation efforts as well as to counter the impacts of the global financial crisis. Development expenditure declined from 2009/10 to 2011/12 as a result of the completion of tsunami reconstruction works. However, the reconstruction programme for the cyclone has resulted in development expenditure increasing in 2012/13.



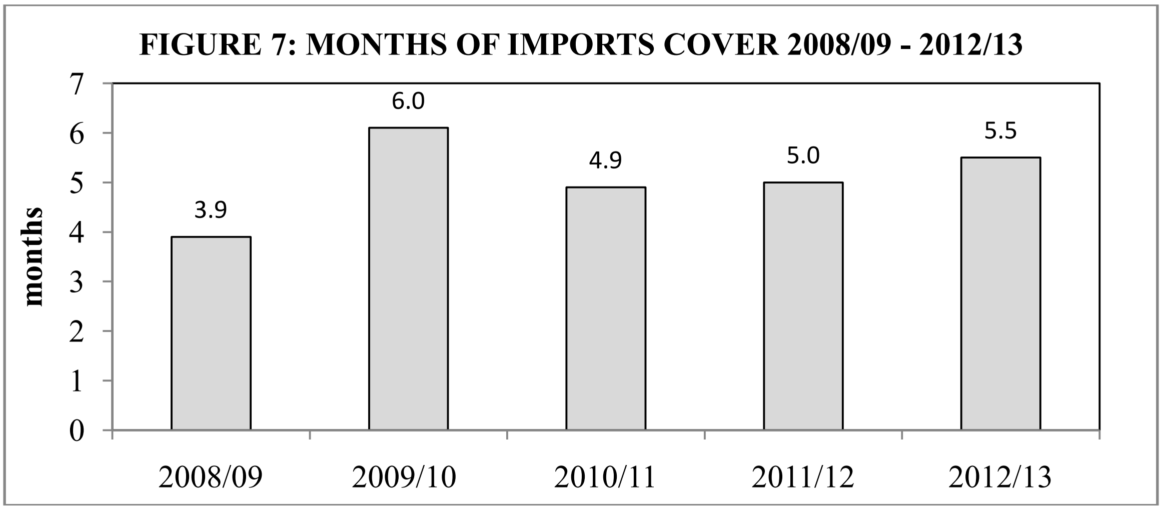
Source: Ministry of Finance and Samoa Bureau of Statistics

Current expenditure by function showed that allocations to social services declined from 2008/09 to 2009/10, increased slightly to 2010/11 then declined again to 2012/13. General services expenditure declined from 2008/09 to 2010/11 then steadily increased up to 2012/13. Expenditure on economic services had recorded a downward trend from 2008/09 to 2011/12 and is expected to increase in 2012/13.



Source: Ministry of Finance and Samoa Bureau of Statistics

Official foreign reserves in 2008/09 were below the target of 4.0 to 6.0 months of import cover. However, import cover was largely within target from 2009/10 to 2012/13.



Source: Ministry of Finance and Samoa Bureau of Statistics

External Debt

Official external debt as a percentage of GDP had remained below the target of 50.0% of GDP from 2008/09 to 2010/11. It increased slightly in 2011/12 to 55% due to the continuation of the Power Sector Project, Education Sector Programme (ESP) Phase II, National Hospital Center Phase I as well as the budget support loans from the Asian Development Bank (ADB) and World Bank. Official external debt as a percentage of GDP will increase to 59% by end 2012/13 primarily as a result of the completion of the National Hospital Center Phase I, the implementation of the National Highway Broadband project and parts of the cyclone recovery programme.

Table 1: Official External Debts

Years	2008/09	2009/10	2010/11	2011/12	2012/13
Official External Debts (Million Tala)	591.3	657.4	737.8	864.6	919.8
Total Debt Servicing	23.2	24.4	20.8	27.7	25.9
Official External Debts as % of GDP	41	45	49	55	59

Source: Ministry of Finance and Samoa Bureau of Statistics

IV. ECONOMIC AND FISCAL OUTLOOK

The International Monetary Fund (IMF) stated in its World Economic Outlook edition in April 2013 that global economic prospects have improved again but the road to recovery in the advanced economies will remain unstable. World output growth is forecast to reach 3.3% in 2013 and 4.0% in 2014. In advanced economies, activity is expected to gradually accelerate, starting in the second half of 2013.

Samoa‟s major trading partners, New Zealand economy is set to expand at only a modest pace with constraints expected from weak external demand, a strong currency, high household indebtedness and fiscal consolidation. The Australian economy is projected to expand by roughly 3.3% in 2013 and 2014, which would be slightly below potential. The US economy has continued to recover. Activity has been expanding at a pace just slightly ahead of potential, while the labour market has recovered very slowly. The housing market has shown signs of a turnaround, but its contribution to overall GDP growth remains small.

Domestically, the Samoan economy is expected to grow by 1.3% in 2012/13 due to the impact of the cyclone devastation. For 2013/14, the economy is expected to rebound to 3.5% as the recovery and reconstruction works takes hold. The preparations for the United Nation Small Island Developing States (SIDS) conference at the beginning of 2014/15 will also contribute to the economic recovery. However, the projections for 2014/15 and 2015/16 are expected to be slower at the rate of 1.2% and 1.6% respectively, as the rehabilitation works tail off. Over the medium term, GDP is expected to stabilize at around 2.5%per annum.

Domestic consumption is projected to decline by 4.2% in 2012/13 from an increase of 1.4% in 2011/12. This is largely the result of the severe impact of the cyclone on agriculture, tourism, commerce and manufacturing. The forecast for 2013/14 is an increase of 1.7% as a result of recovery in these sectors. 2014/15 is expected to increase by 6.4% as a result of increased in economic activities for hosting the Small Island Developing States (SIDS) conference 2014. A slower pase of 3.0% is expected in 2015/16.

Private investment is anticipated to remain positive throughout the medium term. Business investment is expected to hold up in the near term in a number of sectors including energy, tourism, commerce, agriculture, manufacturing and communication. Construction will also be boosted by the rebuilding program.

Exports is expected to increase by 1.0% in 2012/13 following an increase of 4.6% in 2011/12. Exports is currently projected to increase by 2.9% in 2013/14, 4.4% in 2014/15 and 3.5% in 2015/16 as the result of the recovery and reconstruction works over the same period. The SIDS conference in 2014 is expected to contribute to a projected growth of 4.4% during this period.

Imports is forecast to increase by 3.8% and 8.3% in 2012/13 and 2013/14 respectively. This growth is expected to be fueled by the rehabilitation works as demand for building materials will increase. The other contributing factor will be the considerable amount of spending on the SIDS meeting. Imports in 2014/15 is anticipated to decline by 0.6% reflecting the winding down of the recovery effort for the cyclone reconstruction. Further ahead, imports are projected to grow by 1.7% in 2015/16.

Government expenditure is forecast to significantly increase to 15.3% and 11.3% in 2012/13 and 2013/14 due to the recovery and rehabilitation work. However, in 2014/15 and 2015/16, government expenditure is projected to decline considerably by 18.9% and 6.0% respectively, as reconstruction winds down.

In 2013/14, inflation is projected to be around 1.5% due to projected declines in world commodity prices barring any other major shock from unfavorable weather conditions. Inflation is forecast to be around 3 - 4.0% from 2014/15 to 2015/16.

Table 2: Growth of GDP Expenditure Components (constant 2002 prices)

	2012/13	**2013/14**	**2014/15**	**2015/16**
Consumption	-4.2	1.7	6.4	3.0
Private Investment	16.1	14.2	16.8	5.9
Government	15.3	11.3	-18.9	-6.0
Exports	1.0	2.9	4.4	3.5
Imports	3.8	8.3	-0.6	1.7
Gross Domestic Product	1.3	3.5	1.2	1.6

Source: Ministry of Finance

The macroeconomic target rates and its implications are as follows:

1) The budget deficit target identified in the Strategy for the Development of Samoa (SDS) is 3.5% of GDP. Though government envisions fiscal expansion in 2013/14, budget deficit will decline to around 4.7% as a result of tremendous support from our development partners in terms of opting to provide more grants than loans to assist with the rebuilding efforts. The government will continue to seek out grant funding for development work rather than loans.

2) The total current expenditure as a percentage of GDP is anticipated to grow just above the target. This is driven mainly by the expansionary stance to rebuild before it declines below the target rate in the outer years.

3) Personnel cost as percentage of total current expenditure is projected to be just below the target range over the medium term. The current fiscal year is anticipated to drop as most of the current expenditure will be directed to rebuilding.

4) The external debt level as a percentage of GDP will remain high in the medium term mainly relating to the need to rebuild as well as to stimulate economic growth. The bulk of the external debt is highly concessional provided by multilateral financial institutions as well as bilateral. The government will continue to maintain prudent control over any new borrowings, and ensuring that any new borrowings must have at least a 35% grant component.. The government intends to reduce the debt to sustainable levels within five to ten years.

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Table 3: Macroeconomic Framework 2012/13-2015/16

	Target	2012/13	2013/14	2014/15	2015/16
Real GDP (% change)	3.0%-4.0%	1.3%	3.5%	1.2%	1.6%
Inflation (%)	3.0%-4.0%	0.9%	1.5%	4.0%	4.0%
Budget Balance (% of GDP)	Deficit: Not more than 3.5% of GDP	-6.1%	-4.7%	-4.9%	-1.3%
Total Current Expenditure (% of GDP)	35%-38%	35.4%	38.9%	31.3%	29.2%
Personnel Costs (% of total current expenditure)	40% - 41%	37.6%	32.5%	38.9%	38.3%
Disbursed Outstanding Debt (% of GDP)[1]	Less than 50%	59.4	62.6	64.9	63.3
Current Account Balance (%of GDP)		-3.3%	-6.5%	-3.1%	-1.3%
Import Cover (months)	4.0-6.0	5.5	5.2	5.4	5.6
Nominal GDP ($ million)		1,575.2	1,676.4	1,727.7	1,792.4

Source: Ministry of Finance

1 This debt consists entirely of concessional loans that are mostly financed by the Asian Development Bank and China

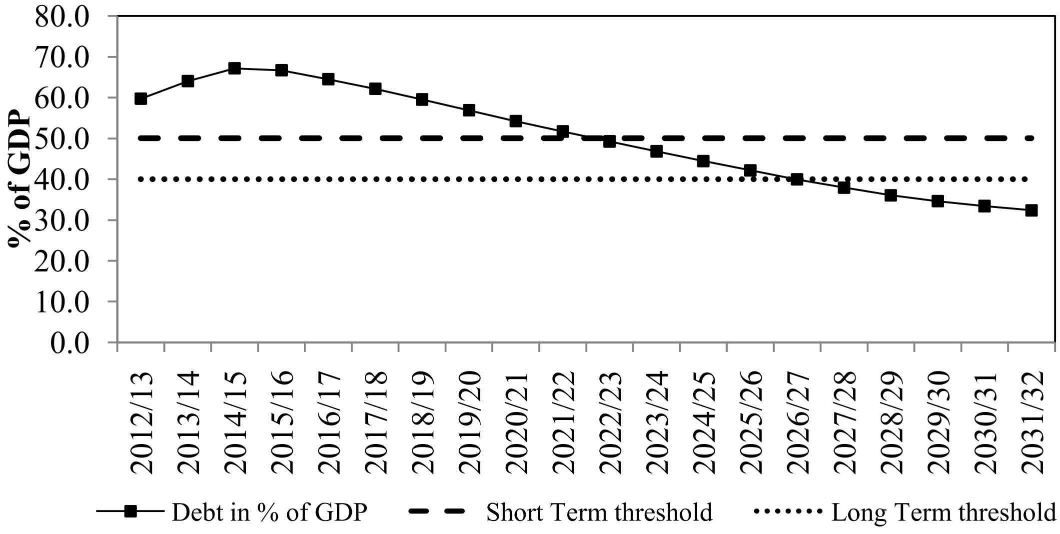
2 Personnel costs as a % of current expenditure include wages and salaries of all ministries and public beneficiary bodies, previously reflected as part of grants to SOEs in FY2011/12

V. EXTERNAL DEBT - LONG TERM PROJECTIONS

The government intends to pursue a programme of fiscal consolidation in the medium to long term. At the same time, there is a need to maintain a programme of public sector investment as the base for renewed economic growth. As a consequence the level of external debt as a percentage of GDP will continue to climb above the threshold of 50% over the medium term. The investments envisaged with the additional borrowing will be aimed at the development of the priority areas identified in the SDS. All the projects will be carefully appraised to ensure that they are economically viable and contribute positively to economic growth. Any projects that cannot be shown to have a sound economic rate of return will not be implemented. Within this framework the government has reviewed and implemented its Medium Term Debt Strategy to ease the debt burden over the medium to long term.

A sector wide approach to investment has been put in place to ensure a more efficient and cost effective allocation of expenditure in order to address specific issues related to each sector. A Public Expenditure Review covering the last ten years is ongoing to assist in reprioritizing spending to key areas for the benefit of everyone. The government as part of its ongoing Public Finance Management Reform Plan is striving to ensure the efficiency and effectiveness of the government systems. This will help the efficient allocation of resources, improve services and enhance the collection of government revenue. Non-tax reform has started to ensure cost recovery in the service being provided and to raise revenue to finance development.

FIGURE 8: NOMINAL VALUE OF PUBLIC EXTERNAL DEBT AS PERCENTAGE OF GDP



Source: Ministry of Finance