GOVERNMENT OF SAMOA

FISCAL STRATEGY STATEMENT BUDGET 2014 / 2015

MINISTRY OF FINANCE
MAY 2014

TABLE OF CONTENTS

FISCAL STRATEGY STATEMENT
BUDGET 2014/15 – 2016/17

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 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.

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

The Samoan economy experienced a relatively shallow recession in the second half of FY2012/13 as a consequence of the significant damage caused by cyclone Evan in December 2012. The impact of the cyclone hindered economic recovery from effects of the 2009 tsunami and the global financial crisis. However, events expected to boost economic growth in the near future include the preparations for the Small Island Developing States (SIDS) conference in September FY 2014/15 and the Commonwealth Youth Games (CYG) in FY 2015/16.

In pursuit of higher rates of economic growth, the government will continue to put in place sound macroeconomic policy measures that will underpin macroeconomic stability. These measures will have the dual impact of cushioning the economy from future exogenous shocks as well as to injecting spending into various sectors to trigger economic activity. Government will also reprioritize expenditures to areas that generate high returns and more employment as well as improving the efficiency and cost-effectiveness of public services delivered through government agencies.

Although short-term growth will be driven by the preparations for the SIDS meeting and CYG, it is unlikely to have a lasting impact on growth trend. Looking forward, it is essential for the economy to establish a steady positive trend to support employment creation and revenue growth. Government policies to reinvigorate agriculture production, agri-processing and boosting tourism are critical to achieving the medium-term fiscal objectives.

The overall objective of fiscal consolidation will be to maintain a steadily improving fiscal balance in the medium term. In terms of external debt, the government aims to ensure that the external debt ratio will decline in the medium term towards the target rate of no more than 50% of GDP.

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% 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 at less than 50% of GDP;
c) Personnel costs as a percentage of total current expenditure to be constrained to a range of 40 - 45% so as to reflect government's commitment to improved service delivery associated with the implementation of performance budgeting;
d) Budget Balance to be maintained at a rate not below 3.5% of GDP;
e) Improved performance of SOE's to avoid extra burden on Government budget through default loans;
f) Promote greater efficiencies in revenue collection.

III. REVIEW OF FISCAL AND ECONOMIC PERFORMANCE IN THE LAST 5 YEARS, 2009/10 TO 2013/14

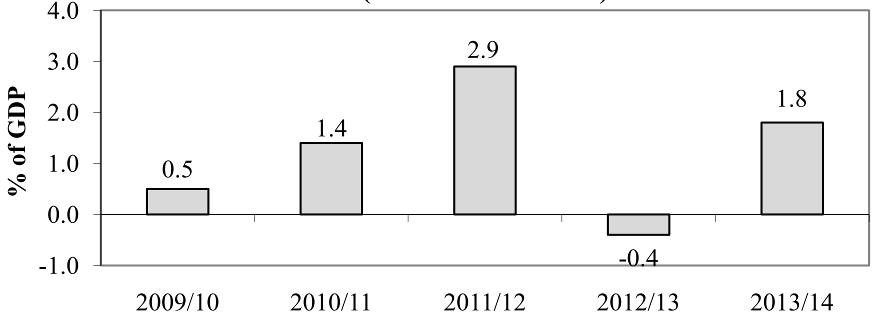
Although Samoa's economy was further impacted by the devastation of the tsunami in the first quarter of FY2009/10 on top of the global financial crisis, the economic growth rate improved to a positive 0.5% in 2009/10. This result was largely influenced by the reconstruction efforts following the tsunami. There was also a substantial increase in the import right hand drive vehicles and an increase in the number of businesses engaged in telecommunication services. These also contributed to the growth during this period.

The economic growth rate increased to 1.4% in FY2010/11. The continuation of the tsunami reconstruction work contributed strongly to this result. The construction of the new government building, the new hospital and the widening and the maintenance of roads also contributed to the improved growth rate. The commerce industry also showed positive growth during this period.

In FY2011/12, economic growth rate increased further to 2.9%. The construction industry continued to contribute strongly to this growth as the result of the ongoing construction of the new hospital and the maintenance of roads for the celebration of Samoa's 50th independence anniversary. Other industries that contributed positively to the growth were Commerce and Finance and Business Services.

With the completion of some of the major construction works and the adverse impact of cyclone Evan, the economy contracted by 0.4% in 2012/13. The cyclone had a particularly back impact on the tourism, agriculture and housing sectors of the economy. The economy is forecast to increase by 1.8% in 2013/14 as the economy continues to recover from cyclone Evan boosted by the preparations for SIDS conference in 2014/15 and CYG in 2015/16.

FIGURE 1: REAL GDP GROWTH 2009/10 - 2013/14
(Constant 2002 Prices)

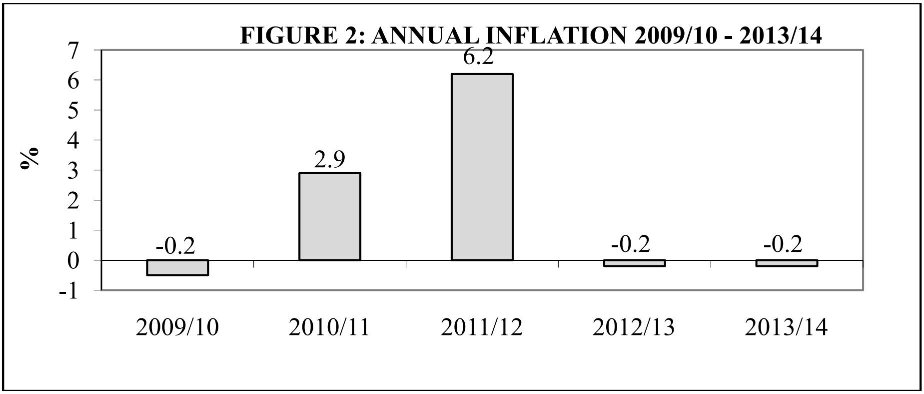


Source: Ministry of Finance and Samoa Bureau of Statistics

Figure 2 shows the annual average inflation rate from FY2009/10 to FY2013/14. Over this period the rate of inflation has been highly volatile ranging from a low of -0.2% in 2009/10 to a high point 6.2% in FY2011/12. In FY2010/11 the annual average inflation rate was 2.9%, an increase caused by the rise in electricity prices as a result of upward movements of fuels prices from overseas. At end June FY2012/13, inflation rate had declined again to negative 0.2%.

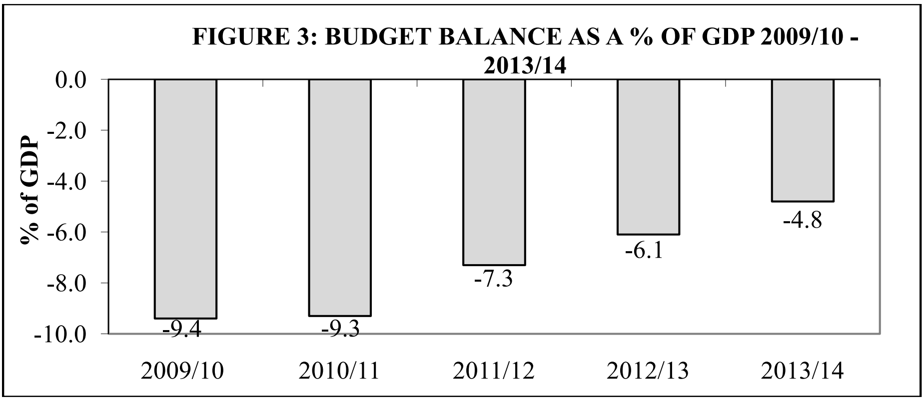
The decline in FY2012/13 was attributable to a fall in international food and oil prices and lower domestic prices recorded for some food items. Local produce prices were noticeably lower as supplies recovered from the impact of cyclone Evan. Prices for electricity and clothing & footwear were also lower over the period compared to the previous year. Although the rate has been highly volatile the average annual rate of the period as a whole was 1.7%.

The annual average rate of price inflation stood at negative 1.2% at end April 2013/14. This represents a drop of 1.8 percentage points in the rate of price inflation when compared to the annual average inflation rate of 0.6% at end April 202/13. The decline is attributed to a fall in clothing and footwear prices, lower domestic prices recorded for some food items, notably local produce as supplies recovered from the impact of cyclone Evan. Inflation is estimated to stand at negative 0.2% at end June 2013/14 as local food prices continue to decline.



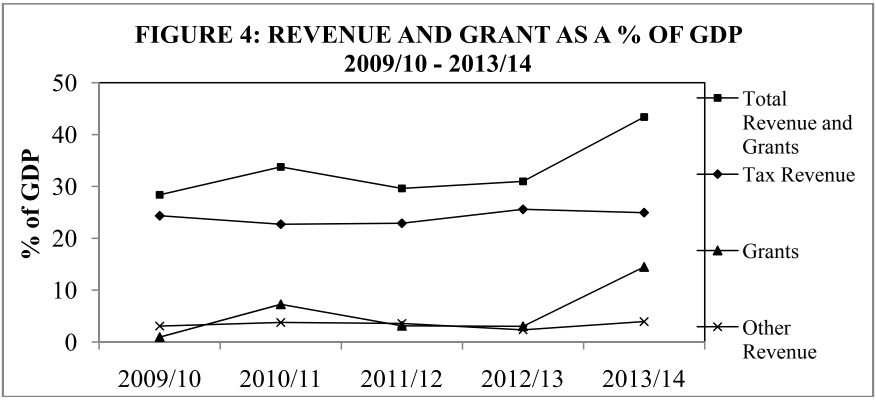
Source: Ministry of Finance and Samoa Bureau of Statistics

The overall budget deficits increased in FY 2009/10 and FY2010/11 to its highest level ever in response to the impacts of the global economic crisis and the need to fund the reconstruction and rehabilitation following the tsunami devastation. The deficit was reduced in FY2011/12 to FY2013/14 as the economy recovered from the external shocks and natural disasters. Financing the deficit was made easier for the government as external budget support funds were converted to grants by World Bank and the Asian Development Bank (ADB).



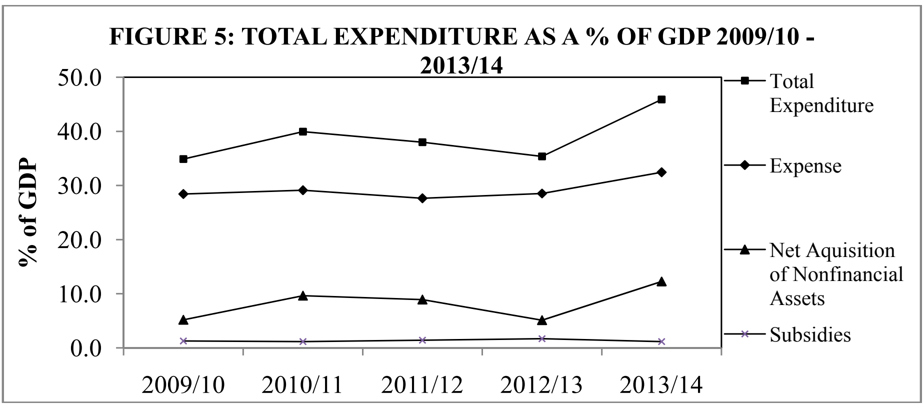
Source: Ministry of Finance and Samoa Bureau of Statistics

Tax Revenue remained at about 23% of GDP between FY2009/10 through FY2011/12, then increased to 26% in FY2012/13 and declined to 25% in FY2013/14. Other revenue increased in FY2010/11 and FY2011/12, but declined in 2012/13. It then increased again in FY2013/14 to stand at about 4% of GDP. External grants increased from 1% in FY2009/10 to 7% in FY2010/11 and then fell to 3% in FY2011/12 through FY2012/13. In FY2013/14 external grants increased to the equivalent of 14% of GDP as World Bank and Asian Development Bank converted loans to 100% grant funding.



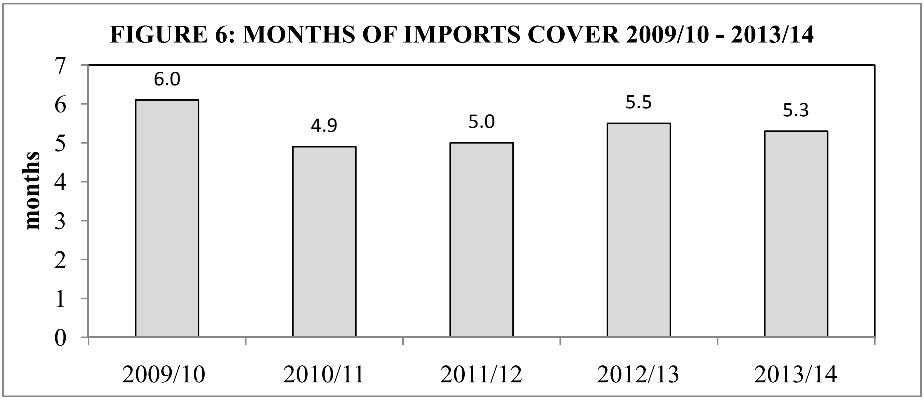
Source: Ministry of Finance and Samoa Bureau of Statistics

Expense (current expenditure) as percentage of GDP increased from 2009/10 to 2010/11 then declined in 2011/12. Expense as percentage of GDP increased in 2012/13 for the rehabilitation work of the cyclone devastation. Net Acquisition of Nonfinancial Assets (development expenditure) increased from 2009/10 to 2010/11 due to the tsunami rehabilitation efforts as well as to counter the impacts of the global financial crisis. Net Acquisition of Nonfinancial Assets declined from 2010/11 to 2012/13 as the result of the completion of tsunami reconstruction projects. However, the reconstruction programme for the cyclone devastation has resulted in development expenditure increasing in 2013/14.



Source: Ministry of Finance and Samoa Bureau of Statistics

Official foreign reserves have been in the target range of 4.0 to 6.0 months of import cover over the whole period from 2009/10 to 2013/14.



Source: Ministry of Finance and Samoa Bureau of Statistics

EXTERNAL DEBT

Official external debt as a percentage of GDP was below the target of 50.0% of GDP from 2009/10 to 2010/11. It increased 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. The level of official external debt as a percentage of GDP increased to 59% at end June 2012/13 as a result of the completion of the National Hospital Center Phase I, the implementation of the National Highway Broadband project and funding for the cyclone recovery programme. The external debt level is anticipated to increase further to 60% of GDP by end FY2013/14 driven by the continuation of the National Highway Broadband Project, the Samoa Medical Centre Phase 2 project, the Power Sector expansion project and the continuation of the cyclone rehabilitation work.

Table 1: Official External Debts

Years	2009/10	2010/11	2011/12	2012/13	2013/14
Official External Debts (Million Tala)	695.5	737.7	825.0	935.5	976.7
Total Debt Servicing	24.3	26.5	27.6	32.6	36.3
Official External Debts as % of GDP	48	49	55	59	60

Source: Ministry of Finance and Samoa Bureau of Statistics

IV. ECONOMIC AND FISCAL OUTLOOK

The International Monetary Fund (IMF) World Economic Outlook edition in April 2014, stated that the global activity has broadly strengthened and is expected to improve further in 2014 – 2015, with much of the impetus coming from advanced economies. Looking ahead, global growth is projected to strengthen from 3.0 percent in 2013 to 3.6 percent in 2014 and 3.9 percent in 2015. In advanced economies, growth is expected to increase to about 2.3% in 2014-2015, an improvement of about 1.0 percentage point compared with

2013. In emerging markets and developing economies, growth is projected to pick up gradually from 4.7 percent in 2013 to about 5.0% in 2014 and 5.3 percent in 2015.

For Samoa's major trading partners, the New Zealand economy is expected to grow by 2.7% in the 2014 and 3.6% in the 2015, driven mainly by the Canterbury rebuilding and recovery in domestic demand. The Australian economy is in the midst of a major transformation, moving from growth led by investment in resource projects to broader-based drivers of activity in the non-resource sectors. GDP is forecast to remain weak, growing by only 3 percent in 2014-15 before strengthening to 4.8 percent in 2015-16. A major impulse to global growth has come from the United States whose economy grew at 3.3 percent in the second half of 2013 and a projected annual growth of 2.8% in 2014-2015.

On the latest revised estimates of GDP, the Samoan economy experienced negative growth of 0.4% in FY2012/13 compared to a revised positive growth rate of 2.9% in FY2011/12. However, the growth outlook indicates an increase of 1.8% for FY2013/14. This is largely driven by the continued recovery of the economy as a result of post cyclone spending. Economic activity is also forecast to benefit from the preparations for the global Small Island Developing States (SIDS) conference to be held in Samoa later in 2014. Growth is projected to increase further to 2.4% in 2014/15 largely due to the impact of the SIDS conference on tourism, commerce, transport, communication and restaurants industries. Construction will also be boosted in 2014/15 by the construction of roads and bridges as well as the preparations for the Commonwealth Youth Games (CYG) in 2015. GDP growth rate is expected to stabilise around 2.6% for the remaining two years of the forecast period to FY 2016/17.

Domestic consumption is forecast to increase by 3.6% in 2013/14. This increase is expected to be driven by the continued recovery from the cyclone as well as the 3% increase in public service wages and salaries implemented in February of 2013/14. The SIDS conference is expected to contribute to the 5.2% increase in domestic consumption expenditure in 2014/15. Looking further ahead to the Commonwealth Youth Games in 2015/16, projections for growth in annual consumption expenditure will remain between 4% to 5% in the latter part of the forecast period.

Private investment is projected to remain positive as the improved GDP growth rate underpins business confidence. The commissioning of new hotels in Apia in the coming two years will further sustain private investment.

Government spending estimated to increase by 8.1% in 2013/14 as a result of cyclone reconstruction works, the cost of the public service wage/salary increase and the cost of preparations for the SIDS meeting. Government expenditure is projected to increase by a further 9.4% in 2014/15 for the SIDS conference and the CYG preparations. With the completion of these major international events, Government expenditure is anticipated to decline by 7.1% in 2015/16 and by a further 5.7% in 2016/17.

Exports are expected to increase by 1.6% in 2013/14 as the agriculture industry recovers from cyclone Evan. This is a significant upturn from the negative growth of 2.6% in 2012/13. Exports are forecast to increase by a further 3.0% in 2014/15 as the World Bank/Samoa Agriculture Competitiveness Enhancement Project (SACEP) and Asian Development Bank (ADB) agriculture sector projects come on stream. The SIDS meeting, the CYG as well as the expansion of the tourism industry are also expected to contribute to a continued improvement in export revenues. Exports are forecast to increase further in 2015/16 by 4.0% and 4.8% in 2016/17 as a result of ongoing improvements in the tourism sector and the agriculture sector.

Imports projections are largely driven by the components of domestic demand (consumption, private investment and government expenditure). Therefore, imports are expected to increase by 9.4% in 2013/14 and by 12.0% in 2014/15. This trend will ease to 9.6% and 10.1% in 2015/16 and 2016/17 respectively.

Annual average inflation rate is forecast to stand at 0.9% at end of June 2014/15. In the last two years of the forecast period the rate is expected to return to its long-run average rate and is projected to be approximately 1.6% and 2.1% in 2015/16 and 2016/17 respectively.

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

	2013/14	2014/15	2015/16	2016/17
Consumption	3.6	5.2	4.3	5.0
Private Investment	8.6	8.9	10.3	10.4
Government	8.1	9.4	7.1	5.7
Exports	1.3	3.0	4.0	4.8
Imports	9.4	12.0	9.6	10.1
Gross Domestic Product	1.8	2.4	2.7	2.6

Source: Ministry of Finance

The macroeconomic target rates and its implications are as follows:

1) A budget deficit of 4.2% of GDP is projected for FY2014/15, this follows from the deficit of 4.8% of GDP in the current fiscal year 2013/14. These deficits are both above the target of 3.5% of GDP stipulated in the SDS 2012-2016. With low growth rates in other sectors, the continuing cyclone recovery expenditure and public investment for the SIDS meeting and CYG will provide the needed stimulus for the economy. The budget deficit is projected to reach the target rate of 3.5% of GDP as the economy continues to expand over the medium term.

2) Total current expenditure as a percentage of GDP is expected to be within the target range in FY2013/14. However, expenditure is projected to fall below the target range in FY2014/15 as reconstruction works come to an end.

3) Personnel cost as percentage of total current expenditure are forecast to be above the target range over the medium term. The increase in personnel cost is due to the increase in salary effective in 2013/14.

4) External debt is projected to remain above the target rate of 50.0% of GDP, but is expected to decline slowly over the medium term. Additional debt will only be incurred for projects that provide positive economic benefits for the economy and for priority areas in the SDS 2012-2016.

Table 3: Macroeconomic Framework 2013/14-2016/17

	Target	2013/14	2014/15	2015/16	2016/17
Real GDP (% change)	3.0%-4.0%	1.8%	2.4%	2.7%	2.6%
Inflation (%)	3.0%-4.0%	-0.2%	0.9%	1.6%	2.1 %
Budget Balance (% of GDP)	Deficit: Not more than 3.5% of GDP	-4.8%	-4.2%	-2.0%	-1.2%
Current Expenditure (% of GDP)	35%-38%	36.0%	30.8%	27.2%	25.9%
Personnel Costs (% of current expenditure)[2]	40%-45%	37.9%	43.9%	46.4%	46.5%
Disbursed Outstanding Debt (% of GDP)[1]	Less than 50%	60.1%	59.2%	56.9%	53.6%
Nominal GDP ($ million)		1,569.9	1,658.9	1,765.0	1,851.6

Source: Ministry of Finance

1. This debt consists largely of concessional loans.
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

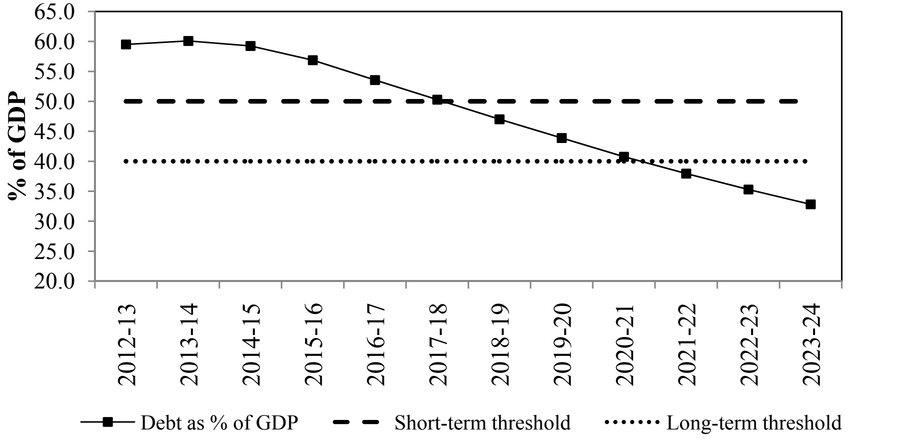
The government will endeavour to control the level of external debt with the objective of gradually bringing it down to the target level of no more than 50% of GDP in the long term. The government will ensure that spending for different sectors of the economy will be focused on generating economic activities and growth in order to achieve the target fiscal balance. The reprioritization of spending will help avoid unnecessary expenditure and will aim to provide benefits to all sectors of the economy. The only projects that will be implemented are the ones that provide clearly defined economic benefits. Government will strongly encourage the use of local labor in public investment projects so that the benefits of employment created as a result will be enjoyed by local labourers.

Non-tax reform has commenced with the goal of implementing a user-pays principle for public services, with due attention being paid to the "ability-to-pay" for lower income persons and families. In addition, government will strengthen compliance within ministries to ensure collection of revenues for public services.

The government will continue to implement structural reforms to make the public service more cost-effective and a sector wide approach has been in place to ensure the efficient allocation of resources to address issues within sectors. A Public Expenditure Review has been implemented for the purpose of reprioritizing spending to essential areas of the economy.

The implementation of the Medium Term Debt Strategy together with the above strategies will no doubt ease the debt burden over the medium to long term.

FIGURE 7: NOMINAL VALUE OF PUBLIC EXTERNAL DEBT AS PERCENTAGE OF GDP



Source: Ministry of Finance