Government of Tuvalu

2012 Budget Speech

By the Hon Lotoala Metia

Minister of Finance and Economic Development

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Salutations

1. Honorable Speaker to the House of Parliament, Hon Prime Minister and your good wife, Honourable Members of Parliament and your good wives, Representative of the EKT, Ambassador of the Republic of China to Tuvalu, Pule Fenua o Funafuti and Community Leaders, Ulu Aliki, Tupu, Pule o Kaupule on the Outer Islands, Permanent Secretaries and senior government Officials, General Managers of Public Corporations, representatives of the private sector and NGOs, Distinguished Guests, Fellow Tuvaluans.

Introduction

2. In accordance with Section 165 of the Tuvalu Constitution, I am honoured to present to Parliament the Government's 2012 Estimates of Recurrent Revenue and Expenditure.

3. Honorable members, the 2012 National Budget continues the adjustment of Government policy and spending to cope with the lingering impacts of the Global Financial Crisis (GFC). Uncertainty continues to surround the global economy. In an increasingly interconnected world Tuvalu cannot avoid these impacts.

4. The 2012 National Budget is a budget of restraint. It is a budget for the times - for the difficult circumstances we face. These difficult circumstances have been largely beyond our control. This budget continues to address these problems so that we can cope with these difficult times. However, we also look to our development partners to work cooperatively with us to deal with these difficult circumstances.

Challenges

5. Mr Speaker and Honourable members let me first outline some of the challenges we face. As most of you are aware, our fiscal policy relies heavily on the Tuvalu Trust Fund. Over the 25 years of its life the Fund has served us well. It has provided us with income to maintain a level of Government services that we could not otherwise have enjoyed. However, the Fund was hit hard by the GFC. It has recovered well but it will be at least another year, more likely two, before we can expect any distribution.

6. In recent years our expenditures have been too high. In 2011 we started to cut costs. In the 2012 Budget we take further steps to reduce spending. Our revenues have been hit by the strong Australian dollar since a majority of our revenues are in US dollars. Tax and public enterprise reforms have failed to yield the expected benefits.

7. In preparing the 2012 National Budget we have looked closely at how to reduce our deficit. We have adopted a prudent approach that involves both reductions in expenditures and increases in revenues. The Government is also committed to continuing economic reforms at a sensible and achievable pace. We must ensure that our reforms are understood and appropriate to our circumstances.

8. But there are also positives. These include improvements in tax administration, increased .tv revenues and commitments from our development partners to provide budget support.

9. Honourable members, let me now take a few moments to review our recent economic performance. The performance of the economy in recent years has reflected the problems

globally. The International Monetary Fund (IMF) estimated that the economy contracted by 1.7% in real terms (after allowing for price rises) in 2009 and a further 0.5% in 2010. While growth is expected to resume in 2011 it is expected to be a slow recovery with 1.0% growth this year and 1.4% in 2012.

10. Inflation remains low. Price levels have increased only modestly with inflation at 1.0% in the year to August 2011. This follows two years of falls from the high prices experienced in early 2009. Part of the reason for this low inflation has been the strength of the Australian dollar. Because many of the goods we import, such as fuel and rice, have international prices set in US dollars, these price rises have been contained. With the Australian dollar remaining at high levels, above parity with the US dollar, this should keep prices low. But if the Australian dollar falls we will likely experience price rises and renewed inflation.

Tuvalu Trust Fund and CIF

11. Honorable Members, it is well known that the Tuvalu Trust Fund has suffered from the impacts of the GFC. The slow recovery in global financial markets means that although the TTF remains well managed its value is still below the value at which it will provide a distribution. At 30 September 2011 the market value of the TTF was $115.1m. The maintained value (capital contributions adjusted for inflation) was 127.5m. This means that the TTF will have to grow by 10.7% (in real terms) in the next year to provide a distribution. Based on history and the current conditions of financial markets this is not considered likely. As such the Government does not anticipate any distribution from the TTF until 2013 for the 2014 Budget.

12. At the same time the balance of our Consolidated Investment Fund (CIF) has fallen from $7.4m in September 2010 to $3.1m at the end of September 2011. So far in 2011 we have drawn down $4.5m, which is in line with the sustainable drawdown from the CIF. This has resulted in the low CIF balance, since there have been no distributions from the TTF and continued deficits in our national budgets. It is a problem that this Government is seeking to address.

The Budget Setting

13. The Government has many social obligations that compete for our limited financial resources. Health, Education and Law and Order are our core concerns. But there are other commitments including the outer-islands, the environment and our productive sectors such as agriculture and fisheries that require our continued support.

14. In preparing the framework we have to make a number of assumptions to project forward to the new year and beyond. We make a range of assumptions about economic growth, exchange rates and inflation, among other things. It would take too much time to go through these, but the key assumptions are:

- Economic growth in 2011 is forecast at 1.0% and increasing to 1.4% in 2012, and although IMF have not made forecasts for 2013 and 2014 we have used the same rate for those years;
- Inflation is assumed to be 0.5% in 2012 before increasing to 2.6% in 2013 and again in 2014;
- The 2012 Budget assumes an exchange rate of one US dollar equal to 90 Australian cents and this has been applied to our US dollar revenue items in the Budget; and
- There will be no distribution from the TTF until at least 2013 for the 2014 Budget.

Recent fiscal performance

15. Honourable members, it is fair to say that the Government's recent fiscal performance has been mixed. Despite a 2011 Budgeted balance of negative $1.6m our projections for the outturn of the Core Budget Balance indicate a $2.7m deficit, with our reserves falling to around $5.0m.

16. The projected increase in the 2011 deficit has a number of contributing factors. On the expenditure side under spending on staffing costs and Special Development Expenditures was more than offset by over spending on the Tuvalu Medical Treatment Scheme, Travel and Communications, and Fuel and Oil. On the revenue side there were shortfalls on the .tv licensing agreement and the Marine Department. The strong A$ also impacted on our Republic of China grants.

2012 Budget

17. Honourable Members, the 2012 National Budget that I present today continues our tradition of fiscal prudence and investment for the future. As I have already mentioned we are aware of the difficulties we face with little or no income from our Trust Fund. We have taken a number of steps to rein in expenditure. But we are also mindful of the need for us to continue to invest in the core services and support the local economy in these difficult times.

Te Kakeega II Review

18. The recently conducted review of the Te Kakeega II reinforced many of the priorities of Government. I will present the preliminary report of the Te Kakeega II review later in this session of Parliament. However, the basic outcome reinforced many of the existing strategies. Where new strategies were proposed we will look at these in detail and adjust the budget as required to reflect the changing priorities of the people. Where the priorities were reconfirmed we will continue to focus on priorities of education and health.

19. Mr Speaker, the recent fiscal performance combined with the lack of distributions from the Tuvalu Trust Fund means that the Government will start the 2012 Budget year in a precarious financial position - with projected cash reserves of $5.0m and no distribution expected until the 2014 Budget at the earliest. This means that on current projections the remaining reserves will need to last through 2012 and 2013. The Government therefore needs to reduce expenditures and find other sources of revenues to fund its core services.

20. Honourable Members, the Appropriation Bill will seek Parliament's approval of $28.2m in core expenditures. When statutory expenditure is included the 2012 Budget expenditure increase to $29.2m. This is made up of $27.0m in recurrent expenditure and $2.2 million in Special Development Expenditures (or SDEs). This is a decline of 12.2% from budgeted core expenditure levels in 2011.

21. Budgeted recurrent spending will fall from $28.0m in 2011 to $27.0m in 2012, which represents a 3.5% decline. However, SDE spending has fallen by more than half from $5.3m in 2011 to $2.2m in 2012. This is where the main decline in expenditures has come from since most SDE spending, which are one-off items, can usually be deferred with no major impact.

22. In addition, the Government has moved to cut scholarship spending dramatically in 2012 with no new awards funded. After discussions with our development partners we anticipate an increase in external support for scholarships in 2012 in order to maintain a reasonable level of scholarships for Tuvaluans. This does not indicate any lessening of priority to the education sector but rather a re-focusing on basic, secondary and vocational education which remain the education priorities of Government as outlined in the Te Kakeega II.

23. Total domestic revenues for 2012 are estimated at $19.6m, which represents a 2.3% decline from the 2011 Budget of $20.1m. This was due mainly to a reduction in dividends and interest as a result of a reduction in dividends and a reduction in interest from the CIF as yields fall and the balance is drawn down. This has offset increases in both Company Tax and .tv revenues after the Government successfully concluded an extension of the .tv licensing agreement.

24. With respect to our biggest revenue items, fishing licenses and our grant from the Republic of China (Taiwan) we retain our estimates near last year's levels. Fishing licenses are anticipated to again yield $5.6 million while the recurrent grants from our good friends the Republic of China (Taiwan) will decline to $4.5 million because of expectations on exchange rates.

Expenditure, Revenue, Deficit, Financing, Budget Support

25. The 2012 National Budget forecasts a budget deficit of $5.1m, which, on current projections, will exhaust our reserves by the end of 2012. This results from expenditures of $29.2m against revenues of $24.1m made up of $19.6m in domestic revenues and $4.5m in grants.

26. Given that the Government's reserves are projected to be around $5.0m at the beginning of 2012, the Government will look to the help of our development partners to support and maintain our essential services. We recognize that there will need to be reforms to encourage and increase efficiencies in Government and in the economy. But as I have already said we are keen to pursue these reforms at a sustainable rate and fully aware of the implications of these reforms.

Budget main points

27. Mr Speaker we have taken some initial steps in this process during this budget. Let me outline some of these initiatives and key points of the 2012 National Budget briefly now.

Tuvalu Medical Treatment Scheme

28. One of the major areas of concern in our spending has been the Tuvalu Medical Treatment Scheme. This Scheme including the domestic referral scheme from the outer-islands has experienced major overruns in recent years. In order to try and bring these costs under control the Government has agreed that no caretakers will be funded under the new policy. Only exceptional cases will be entitled to caretakers such as blind, wheelchair patients and patients aged 13 years or younger.

Training and Scholarships

29. As mentioned earlier the Government recognized that the Government-funded scholarship program was unsustainable. It was also limiting the best use of the generous scholarship assistance from our development partners. As such, the Government has decided that no new awards, either in-service or pre-service, will be funded by the Government in 2012. While this might seem drastic it will allow the Government to focus its education and training budget on its Te Kakeega II stated priorities of basic and vocational education. In fact, this year the Government is beginning to make explicit allocation for vocational education under TVET support as the Government increases its emphasis in this area.

Outer-Islands projects

30. Despite the reductions in spending the Government is keen to support the island communities in their development efforts. As such the 2012 National Budget includes $1.2m for outer-island projects. This reinforces our commitment to these communities that we have continued

for a number of years now and demonstrates the high priority we place on maintaining and sustaining these communities.

Tuvalu Consumption Tax

31. Mr Speaker, the difficult situation that we find ourselves in makes it necessary to make some difficult decisions. One such decision is the decision to increase the Tuvalu Consumption Tax (or TCT) from 3% to 4% as of 1 January 2012. This coincides with a decline in import tariffs in line with our commitments made under the Pacific Island Counties Trade Agreement (PICTA). This decision was not done lightly and was debated at length. As a consequence, the increase has been kept to a minimum so as to minimize the impact on the community.

Development Partners

32. I would like to take this opportunity to once again thank our good friend the Republic of China (Taiwan) and the assistance they provide to the Government. In the current year they agreed to provide their grant assistance entirely as budget support. This provides the Government with much greater flexibility in its financial management. Direct budget support grant assistance in 2012 is US$5.0m ($4.5m), which allows us to fund a range of key projects in the Budget.

33. The 2012 Budget also anticipates a significant amount of Development Assistance from our other development partners. We thank the Japanese Government in providing the recently completed AM Project and the upcoming upgrade for Motufoua as well as the range of assistance such as health clinics, provision of free fuel and environmental projects. Australia and New Zealand will continue to provide a wide range of support in areas such as technical advice, support to our scholarship programs, the Tuvalu Trust Fund, education and health sectors, among other things. The European Union is also providing extensive assistance in 2011 under its Water and Sanitation and Waste Management Projects under their EDF 10 assistance. There are many other donors such as Cuba, Republic of Korea, and India that are providing valuable assistance in critical areas for Tuvalu. We will also receive a wide range of assistance from regional and multilateral agencies such as the CROP agencies, UN agencies, ADB, as well as our new partners in the International Monetary Fund and the World Bank for their forthcoming assistance. We thank all our development partners for this assistance.

Concluding Remarks

34. Mr. Speaker, Hon Members of Parliament, we face the 2012 National Budget with many concerns. However, we have started to seriously address some of the key issues to make it through the difficulties. Some may not be happy with the pace of reform and may wish for more to be done more quickly. But we need to proceed with caution and care. Our decisions affect people's lives. They are not mere numbers on a piece of paper.

35. So far Tuvalu has survived the global turmoil with little direct impact on people's lives. This budget, though including some hard decisions, aims to continue to minimize the impact on the community. This has meant a re-focusing on core areas of Government – Education and Health.

36. However, we have also tried to maintain many other key programs in areas such as law enforcement, agriculture and fisheries to ensure that people are safe and have the opportunity to live productive lives and fulfill the goals we set out in the Te Kakeega II.

37. Te Kakeega II is our roadmap to a better future. We have stopped and assessed our development this year and found much progress but also areas in need of improvement. But I

know with the willingness to work together we can achieve the Te Kakeega II goal of achieving a "healthy, educated and prosperous Tuvalu" in line with the spirit enshrined in our motto – "Tuvalu mo te Atua".

38. Finally I would like to take this opportunity to express my appreciation to everyone involved in the preparation of the 2012 National Budget, particluarly to members of the Development Coordinating Committee, Ministries, the Core Budget Team and the staff of the Planning and Budget Department. All these efforts have contributed to what I believe is another excellent achievement. I express my sincere gratitude to you all.

39. However, much of the hard work is still ahead. We need to work harder and smarter to get the most out of our limited resources for the benefit of our people. For this I ask our Heavenly Father to help us to make wise judgments, strengthen our hand, and guide our way in the year ahead.

40. I now commend the 2012 Budget to the Parliament.

41. Tuvalu mo te Atua.