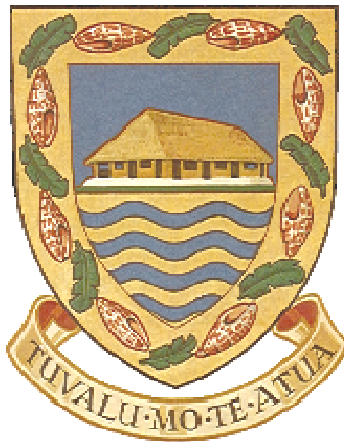


2011 National Budget Speech



**By the Honourable Lotoala Metia
Minister of Finance and Economic Development**

14th April, 2011

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Delivered to Parliament 14 April 2011

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, 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 honored to present the 2011 Estimates of Recurrent Revenue and Expenditure of the Government to Parliament.
3. Honourable Speaker and Members, the 2011 Budget that I present to you today plots a course to navigate the continuing uncertain outlook for Tuvalu. It also continues to invest in the local communities and essential services. While times remain difficult, the Government believes that we can negotiate these difficult times and minimize the impact on the community from the loss of revenues experienced in recent years. This Budget reinforces our commitment to maintain Government services for all Tuvaluans while ensuring sustainable Government finances.
4. The world economy continues to recover slowly from the impact of the Global Financial Crisis (GFC) of 2008. But Tuvalu still faces a long period during which we must watch our financial situation very carefully. Only through careful management of public finances will we be able to survive and prosper in the long run.

2011 Budget Setting

5. Honourable members let me take a few moments to set the scene for this year's budget. As mentioned the GFC has faded from view but we are still living with the impact. The foundation of a budget strategy is the Tuvalu Trust Fund and the value of the Fund was hit badly by the GFC. The Fund is still recovering and still has some way to go before we can expect a distribution.
6. In recent years the economy has struggled due to the impact of the GFC. In November 2010 the Government received the first Article IV visit of the International Monetary Fund since we became members in June last year. For the analysis of this visit the IMF concluded that the Tuvalu economy had struggled through 2009 with real GDP contracting by 1.7%. GDP growth was estimated to be weak again through 2010 growing by only 0.2%. The forecast for GDP in 2011 was for no growth with GDP remaining flat.
7. There were a number of reasons for this disappointing performance. Despite an initial positive impact from the fall in the value of the A\$ in 2008 and 2009 which tended to increase national income this was offset by a declining number of seafarers and a lack of local construction projects. The steady appreciation of the A\$ in recent times has

subsequently had a negative impact on national income from remittances, grants and .tv revenues. These have all had an impact on overall economic activity.

8. The immediate outlook remains uncertain. The AU\$ has exceeded parity with the US\$ and continues to appreciate placing pressure on our US\$ revenues and remittances. Food and fuel prices are rising again which will have an impact on the Government and household budgets. Despite this inflation in Tuvalu, as measured by the Funafuti Consumer Price Index shows overall price levels remain flat for now with no increase in the overall price level in Tuvalu.

Tuvalu Trust Fund

9. As mentioned the Tuvalu Trust Fund suffered significantly in the aftermath of the GFC. It is slowly recovering the loss of value but the market value still remains substantially below the levels needed to provide a distribution. The market value of the Fund was \$110.6 million at the end of December 2010 but this is still well below the maintained value of the Fund estimated at \$119.7 in December 2010. At this rate of recovery, there is unlikely to be any distribution for the 2012 Budget but the Government could expect a modest distribution for 2013 Budget.

Recent fiscal performance

10. Honourable Speaker, the 2010 budget year was a particularly difficult one for reasons already explained. The original budget anticipated a deficit of \$7.7 million. After the passage of a number of supplementary appropriations during 2010 the final estimated deficit has risen to around \$10.4 million. This resulted in the Government requiring to drawdown \$9.0m from the Government's Consolidated Investment Fund (CIF). The result was that the Government's reserves comprising the balances of General Account at the NBT and the CIF fell from around \$15.9m to around \$7.1m by the end of 2010.
11. Overall revenues came in slightly above expectations at \$25.5m as opposed to the budget of \$24.9m due largely to an outperformance in fishing licenses, which were originally budgeted at \$5.6m but reached \$7.6m. This offset the underperformance experienced in tax collections because of difficulties experienced implementing tax reforms. Finally a number of Government charges also fell short of expectations leading to a significant shortfall in "Other Charges".
12. The increase in the deficit was largely the result of a number of areas of overspent and later covered by supplementary appropriation. The Tuvalu Medical Treatment Scheme (TMTS) continues to experience budget overruns. In 2010 the Budget of \$1.5m reached \$2.1m. This does not reflect the full extent of the total bills incurred in 2010; a special allocation of \$0.6m is included in the 2011 Budget to clear these unpaid bills.
13. Meanwhile staffing costs fell well short of budget by almost \$1.0m as has been the case in recent years. The Government is trying to more accurately estimate salary levels to ensure that this shortfall does not occur in the future as it ties up valuable funds that could be better used elsewhere.
14. The main area of overspending resulted from SDE spending with the passage of the supplementary appropriation bill in April 2010. However, a number of these expenditures were unavoidable including the need to cover guarantees granted to the now insolvent

Air Fiji. Also the Government provided funds for undertaking remedial works at the Tuvalu Maritime Training Institute (TMTI) and it is hoped that the Government will recoup a proportion of these costs from the contractor involved. The overall impact on SDE expenditure was that the original estimated SDE budget of \$3.8m increased to around \$6.5m thereby explaining the increase in the deficit.

15. The Government understands that this was a one-off event to ensure a foundation on which to re-establish fiscal stability in public finances. As such the Government has placed at the centerpiece of the 2011 Budget an effort to reduce the Government deficit and protect Government reserves.

2011 Budget

16. Honourable Members, the 2011 National Budget that I present today is a tough but fair budget. It continues our tradition of fiscal prudence and investment in our communities. This Government is aware of the difficulties that face us over the next few years with limited income expected from the TTF. But we are also mindful of the need for us to continue to invest for the future and support the local economy in these difficult times.
17. In presenting the 2011 Budget I will seek Parliament's approval of \$33.3 million in core expenditures. This is made up of \$28.0 million in recurrent expenditure and \$5.3 million in Special Development Expenditures (or SDEs). On top of this we estimate we will also receive around \$30.7 million in development assistance in 2011 from our development partners. All this expenditure is being directed to the priorities set out in Te Kakeega II.
18. Total recurrent revenues for 2011 are estimated at \$29.7 million, which represents a significant increase from 2010. This is due to an anticipated increase in grants, dividends and .tv revenues.
19. With respect to our biggest revenue items, fishing licenses and our ROC Grant we retain our estimates near last year's levels, though the ROC grant is boosted by a generous one-off grant from the ROC. Fishing licenses are anticipated to again yield \$5.6 million while the recurrent grants from our good friends the Republic of China will increase to \$6.5m. We are also anticipating revenues from our agreement to license the marketing of our .tv top level domain to remain increase to \$2.85m, with the possibility of additional increases in the level of this revenue stream.
20. Here I must raise a note of caution. Many of our revenues – fishing licenses, Republic of China Grant and .tv revenues – are denominated in US dollars. This makes the Government's revenues extremely sensitive to the changes in the Australian dollar – US dollar exchange rate. We started the budget process making a conservative assumption that the exchange rate will be around AU\$0.95 to the US\$ over the year. Even now this may be optimistic. This is an area where the Ministry will be vigilant in reviewing exchange rates and if our revenues are anticipated to fall then there may need to be some adjustments to our expenditure levels.

Financing the Budget

21. With revenues forecast at \$29.7m and core expenditures of \$33.3 million the 2011 Budget anticipates a deficit of only \$3.5 million¹. This figure needs to be balanced against the sustainable financing available from the CIF, which in 2010 is \$4.7 million. The resulting adjusted surplus is approximately \$1.2 million.
22. As a result the Government will meet its stated macroeconomic goal in Te Kakeega II that budget deficits should not exceed 2-3% of GDP. The reduction in the deficit is in an effort to preserve the Government's reserves, especially the balances in the CIF. The Government's reserves will further be boosted during the year by an anticipated one-off grant from the European Unions Vflex Facility of 1.5m Euro or about \$2.0m. This will support the Government's budget during 2011, which will mean the Government will likely drawdown less from the CIF.
23. As a consequence the CIF Government reserves over the year will only fall from \$7.1m to about \$5.8m. This should place the Government in a position to maintain services not just in 2011 but for most of 2012. The Government though will need to reassess this situation during its preparations for the 2012 National Budget to ensure the spending levels are kept at levels that will allow for the Government to maintain a reasonable level of services through 2012 without incurring too much debt.

Budget highlights

24. Mr Speaker, I do not intend to outline the whole budget here today. But I would like to identify the highlights and some new initiatives. Let me now briefly list some key aspects of the 2011 Budget.

Wage Increase for Public Servants

25. Mr Speaker the Government realizes that cost of living pressures are presenting challenges to Tuvalu households. We also recognize that many households contain government employees. In order for households to cope better with cost of living pressures the Government has agreed to increase all public service salaries by 3% from 1 July 2011. While this may not be a large increase we have had to balance this against the fiscal requirements of the Budget and the need for prudence.

Island Communities

26. Mr Speaker, a constant theme of our Government has been the support of the Island Communities. In the 2010 Budget we provided \$1.8m for a range of community projects that are helping to support community infrastructure. In 2011 we reinforce this emphasis. Island Communities will benefit from another grant of \$1.2 million for island community projects to build on the investments made in 2010. These funds will target key projects to support island communities and identified by island communities but managed through the Ministry of Home Affairs.

¹ Note that the MTFE in the Budget papers reports a deficit of \$3.3 million. There was a minor error in the XB grants which caused the deficit in the MTFE to be out by \$0.2m.

Republic of China

27. Mr Speaker and Honourable Members, I would like to take this opportunity to once again thank our good friend the Republic of China for the assistance they provide to the people of Tuvalu. This assistance has been critical to the Government being able to maintain health and education services through out the nation as well as continuing our support for island communities. For this we are truly grateful.
28. During the recent trip by the Prime Minister to Taipei, the ROC agreed to provide a one-off grant of US\$1.5m on top of the annual grant of US\$5.0m. This assistance is greatly appreciated especially in light of the financial difficulties that we know Taipei is also facing. We also look forward to concluding the agreement with the ROC for the continuation of this generous funding assistance until 2014.

Debt Position

29. Honorable Speaker, the debt situation of the Government remains a concern but with the assistance of the Asian Development Bank we will pay down a significant proportion of our outstanding liabilities this year. The Government retains a liability for Outer-Island Suspense Accounts with NBT incurred as far back as 2005. The Government is nearing the release of a US\$2.0m grant (or \$1.9m) from the ADB. The Government has completed a range of reforms in the areas of public enterprises, banking and debt management.
30. During this session we will pass the Banking Commission Act to ensure best practice in Banking Supervision and Regulation. These acts will ensure the release of this grant that will then be dedicated to pay down the Outer-Island Suspense Account debt at NBT and place the Government and the NBT on a much firmer financial footing. This will improve the development of new ADB Programs for Tuvalu in 2011.

Ministry of Foreign Affairs, Environment, Trade, Labour and Tourism

31. Mr Speaker, the 2011 National Budget creates a new Ministry – the Ministry of Foreign Affairs, Environment, Trade, Labour and Tourism. This new Ministry pulls together a range of areas critical to Tuvalu's long term well being. The Ministry will manage our expanded overseas representation, which now extends from Suva to Auckland, New York to Brussels. Because of our unique circumstances and the challenges we face as a nation our foreign representation is inextricably linked to our environmental concerns thereby justifying the inclusion of the Department of Environment under the new Ministry. Also through our foreign representation we can continue to press our trade, labour and tourism concerns with great effect to help open avenues to generate increased foreign exchange for Tuvalu.

Education and Health

32. Honourable members, ensuring high quality health and education services for the people of Tuvalu are a core activity of Government. This Government is committed to ensuring adequate funding for these services. The Ministry of Education, Youth and Sports Budget for 2011 has increased by 6.0% to \$6.5m to be the largest Ministry with 19.6% of the Government spending. At the same time the Government has also been able to increase the Health Budget by 19.2% to \$4.9m in 2011. This represents 14.7% of the overall

Government spending. This reinforces the priority that the Government places on Education Health as outlined in Te Kakeega II.

Development Assistance

33. The 2011 Budget also anticipates a significant amount of Development Assistance forthcoming from our development partners. This year the Government anticipates development assistance of \$30.7 million. The list of projects anticipated for 2011 are contained in the Public Sector Investment Program contained in the 2011 Program Estimates. The largest project in this Program is the AM Project to upgrade the ability of Radio Tuvalu to broadcast throughout the nation on the AM Band. We thank the Japanese Government for their generous assistance in this area as well as the range of assistance in many other critical areas such as health clinics, provision of free fuel and environmental projects.
34. Our partners from Australia and New Zealand will continue to provide a wide range of support in areas such as technical advisers, support to our scholarship programs, the Tuvalu Trust Fund, education and health sectors among other things. This assistance is greatly appreciated and much needed. The European Union is also providing extensive assistance in 2011 under its Water and Sanitation and Waste Management Projects under their EDF 10 assistance.
35. 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

36. Mr. Speaker, Hon Members of Parliament, our financial management in recent years has provided many benefits for the nation. It has also shielded us from the worst global financial crisis in living memory. We are not resting on our achievements but building on them in this budget. Our reforms of the tax system, banking, financial management and public enterprises will build a strong foundation for economic development. Our work in the social sector provides for equitable opportunities for all. We believe this is the basis of a happy and prosperous Tuvalu.
37. We are not trying to do everything. We are targeted in our approach to the nation's development. We focus on our priorities set out in Te Kakeega II. The initiatives I have outlined today are only part of the work that we continue to do. Our ongoing programs in education, health, law enforcement, agriculture and fisheries are also keys to steady progress and will continue to underpin Tuvalu's well being.
38. Te Kakeega II is our roadmap to a better future. But we must occasionally stop and take stock and so in 2011 we have started to review our progress. The Government will also benefit from the Peer Review of Tuvalu's development process sponsored through the Cairns Compact. This an opportune time to review our goals as we approach the 2015 deadline for achieving the TK II and Millennium Development Goals. Te Kakeega II has

served us well but it can always be improved. We look forward to hearing the views of all Tuvaluans during the review.

39. Complementing the review of the TK II we have also reviewed the goals and objectives of the Ministries to ensure that they are clear about what they are doing and that their budgets are linked to these goals. The Planning and Budget Department has been working with Ministries to ensure that 2011 Budget Program Descriptions provide the link between the Te Kakeega and the National Budget.
40. Finally I would like to take this opportunity to express my appreciation to everyone involved in the preparation of the 2011 National Budget. My thanks go to my Cabinet colleagues, members of the Development Coordinating Committee, Ministries, the Core Budget Team and the staff of the Planning and Budget Department. It was demanding work but the commitment and hard work has paid off. It has been a mighty effort.
41. But there is much hard work ahead and difficult decisions to be made as we cope with these difficult times. For this I ask God to help us to make wise judgments, strengthen our hand, and guide our way through the difficult times we face.
42. I now commend the 2011 Budget to the Parliament.
43. Tuvalu mo te Atua.