

BUDGET SPEECH 2018

DELIVERED ON 5 DECEMBER 2017 ON THE FIRST READING
OF THE APPROPRIATION BILL 2018

BY

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LEAVING NO ONE BEHIND

Introduction

Honourable Speaker, it is my greatest pleasure to present to this House the 2018 Budget. In a little under two years in office, this Government has relished the great honour of delivering progress to the people of Kiribati – a service this Budget continues to deliver. We remain committed to serving and delivering on our commitments and we have worked tirelessly to implement the promises made to the people of Kiribati in *Te Motinnano*.

Honourable Speaker, in this short span of time, I am pleased to inform this House that we have made significant headways in accomplishing most of our key commitments, which include: doubling the copra price subsidy, providing free education up to Form 6, increasing support to Churches, recognising the important role of Mayors and Councillors (provision of salary), improved electricity distribution in South Tarawa at reduced costs to households, and major investments to improve sea and air transportation through the provision of new vessels for the Kiribati Shipping Services Limited (KSSL) and the Dash 8 for Air Kiribati. We believe that these policies will contribute to supporting our long-term vision that we live in a wealthy, healthy and peaceful nation.

Mr Speaker, these are just a few of our achievements and I must say that all of these have been achieved without compromising our fiscal sustainability. Indeed, even with

the new \$30 million investment in the Outer Islands Infrastructure Program, other Supplementary Budgets and the Revised 2017 Budget estimate all financially supported through our cash surpluses.

Mr Speaker,

The importance of the 2018 Budget cannot be understated. While our revenues have grown, they still pale in comparison to the many challenges we face as a nation. Public spending remains the single largest contributor to our economy and therefore the Budget is the key policy platform for delivering development to our people. Without sustainable finances, our challenges such as our vulnerability to climate change and our dependence on foreign fishing vessels are factors beyond our control. For this reason, the Budget must meet the twin goals of fiscal sustainability and inclusive economic development.

We strongly believe that we must take charge of our own destiny in a sustainable manner, ensuring that not only our finances are sustainable, but that **no one is left behind**. This is a central tenet of our development aspirations through the *Kiribati Vision 20* (or KV20) and the Kiribati Development Plan, which are consistent with our commitment that we will serve and deliver on the promises we have made to our people.

The Economic Outlook

Mr Speaker, the budget is the primary tool of economic management. Therefore one cannot separate the budget from the national economy, especially in Kiribati, where public spending is one of the key determinants of growth.

At a global level, the International Monetary Fund has noted that we are currently experiencing an 'upswing' in world growth. Global output is estimated to have increased by 3.6 percent in 2017, with a small upward revision in almost all non-US economies. Importantly, while strong growth in the Asia-Pacific region continues, particularly from China, international price pressures remain relatively low. In particular, let us hope that the continued restraint on oil prices continues despite of some signs of oil producers trying to reduce excess supply.

Based on a recent IMF report on Kiribati, our economy grew an estimated 3.1 percent in 2017, driven by the growth in fishing revenues and development partner projects. While some of these projects are coming to their natural conclusion in 2018 and 2019, there are a number of new projects coming online which will continue to support growth going forward. For 2018, the IMF estimates Kiribati to grow at 2.3 percent in real terms.

Price growth has been relatively muted, with the IMF estimating that inflation for 2017 will be around 2.2 percent, a slight increase on the 1.9 percent experienced in 2016 due to increasing import costs. Going forward, the IMF expects Kiribati to experience inflation in line with our major trading partners, notably Australia, with inflation to be an estimated 2.5 percent in 2018.

Our fishery also remains strong, with recent estimates of 2017 fishing revenue remaining at or above \$150 million.

For the 2018 fiscal setting, these healthy macroeconomic indicators are great news to us but as always, these forecasts come with risks.

Mr Speaker, we are an island nation. While we are so far away from the major economic centres, we cannot consider ourselves as separate to the currents of global markets. We are exposed in three ways.

Firstly, our fishery, which is our major environmental asset and primary source of revenue, is not something we have direct control over: Wherever the fish go, the fleets will follow. While we have established the Phoenix Islands Protected Area and the Vessel Day Scheme to try and ensure that this asset is sustainable into the future, we cannot deny that changes in climate, currents, or global fishing markets will impact upon the fishery's performance. Any change in the performance of the fishery has a major impact on our revenue, and hence, our ability to engage in economic development. We must recognise that while there has been a stepped change in fishing revenue, we must remain prudent about our expectations in any given year – we simply cannot afford to be overly optimistic about things beyond our control.

Secondly, the RERF – our major financial asset – is exposed to the volatility of international markets. In some years the returns will be good, while in others it may

be lower. It is crucially important that we manage the RERF in a way that benefits both current and future generations and we must be in a position to look through these fluctuations and focus on long-term growth. We have done this by continuing a balanced portfolio of assets to limit volatility, and we remain committed to reaching the \$1 billion RERF target by 2020 as outlined in the KV20, as a way of ensuring that the nation will always have access to this resource in times of need. We recognise that the RERF and cash reserve provide an important safety net for the nation's finances should external factors work against us. For this reason, we have included the impact of our decisions on our cash balances in the Budget as a way of showing the nation that we are serious about ensuring our wealth is protected.

And thirdly, while it is prudent for us to continue to use the Australian dollar, exchange rate volatility can affect everything from fishing revenue, RERF performance, and the cost of imports.

Mr Speaker, we must accept that while we can try to limit these risk factors they are largely outside of our control.

In order to be in a position where we can withstand any external shock, including climate change, we must increase the ability of our people to respond. As outlined in the KV20 and the KDP, the best way to do this is to not only raise our level of prosperity through continued economic growth, but to do so in an inclusive manner. To allow us accomplish this, our finances must be sustainable both now and in years to come. **It is therefore why we accord this as our priority to build a fiscal framework ensuring that no one is left behind.**

2018 BUDGET

Honorable Speaker, allow me at this juncture to share the details of our 2018 budget.

Expenditure

Total expenditure for 2018 is estimated at \$195.7 million, a \$31.6 million increase compared to the 2017 Budget, but a \$22.6 million decline from the Revised 2017 figures (which includes \$54.2 million in Supplementary expenditures). Of the \$195.7

million, \$7.5 million is statutory expenditure, meaning that the resultant Appropriation Bill is for a total spending of \$188.2 million.

Mr Speaker, if we break down the budget by category of expenditure, the distribution is as follows: \$80.5 million or 41.1% of the total budget is allocated for Ministries' personal emoluments; \$33.3 million or 17.0% allocated for Ministry operations; \$30.9 million or 16.7% for subsidies and grants; \$49.3 million or 25.2% for the local contribution to development; and \$1.7 million or 0.9% for total debt servicing.

However, these high-level figures do not do justice to the internal prioritisation of the budget. Taken together, the 2017 and 2018 Budgets contain three major areas of increased spending that align to our theme of **no one is to be left behind**:

Investing in Our Human Capital.

Following on from the success in 2017 of free schooling up to Form 6, the 2018 Budget provides \$2.7 million to ensure that every I-Kiribati has access to basic education. The creation of education pathways is an important element of inclusive growth, so the Government is spending \$2.9 million of its own resources to increase the availability of tertiary scholarships for those seeking further education and a further \$1.6 million for the student loan scheme. In total, these measures direct around \$7.2 million towards ensuring free or affordable access to educational opportunities for all I-Kiribati.

These contributions come as additional to the \$5.6 million that will be spent on the newly named Ministry of Employment and Human Resources, which hosts Kiribati Institute of Technology, the Marine Training Centre and the School of Nursing and Health.

The largest expenditure in the education sector is of course the Ministry of Education, whose recurrent budget of \$27.6 million in 2018 is a \$4.6 million increase on the 2017 level – the largest increase out of all the Ministries, demonstrating the commitment of this Government to investing in our nation's future leaders.

It would be remiss of me not to point out also the significant spending increases in the health sector as well. Not only has this Government increased the funding available to health referrals to \$2.6 million in 2018 (an \$800,000 increase on the 2017 Budget), but the Ministry of Health and Medical Services will also receive an

additional \$3.8 million dollars in 2018, bringing the total recurrent budget for the Ministry to \$23.6 million.

Together, health and education remain the key investment priorities for this Government, with a combined \$11.2 million *increase* to the funding of the two sectors overall. For the Ministry of Health and Ministry of Education alone, the \$8.4 million increase in funding in 2018 represents almost half of the total increase in ministry recurrent expenditure, and brings the combined ministry expenditure to \$51.2 million, 45 percent of total recurrent spending across all Ministries.

This demonstrates the importance of investing in the nation's human capital, which is critical to sustain development gains and accomplishment of the KV20 aspirations.

Investing in the Outer Islands

The copra price guarantee is of course a popular topic of public discussion. Aimed specifically at boosting economic activity and cash incomes in the outer islands, this Government is continuing to support the \$2-per-kilo price. It has now been more than a full year of implementing the new price, giving us more confidence in our ability to forecast just how large the increase in production has been. From around \$7.95 million in 2015, the Copra Price Scheme has expanded to an estimated \$30.6 million in 2017. One does not need to be an expert in mathematics to see that the doubling of the copra price has more than doubled copra production, despite logistical difficulties. Going forward, we expect modest growth from the now-higher level of production, with the Copra Price Scheme being an estimated \$31.1 million in 2018.

This program continues to have a material impact on the livelihoods of those in the outer islands, and has enabled dramatic increases in disposable income and household investment. Reflecting its importance to human capital investments in the outer islands, the Government has decided to move the Copra Price Scheme to the Local Contribution to Development.

The annual copra program is also paired up with significant infrastructure investments in the outer islands. While these investments may take some time to be fully implemented, by allocating \$30 million to the Outer Islands Infrastructure program in 2017 Supplementary Budgets, the Government has created a pipeline of projects that will be rolled out over the coming years in conjunction with a further \$40

million from the World Bank and Asian Development Bank. Together with development partner investments in telecommunications and Government investments in new shipping vessels for KSSL and the Dash 8 for Air Kiribati, this Government is committed to bringing our nation closer together – again on the basis of our modus operandi that **no one is left behind**.

Public Service Performance

There is a great demand for the Public Service to raise its standard and I must also say it is about time Government drive this high quality service delivery and performance reform in the public service.

A new and major component of the 2018 Budget is the upgrading of civil servants' salaries which will be effective from 1 January 2018. This initiative bodes well with the Government's commitment to put in place a robust incentive structure that would serve to boost productivity and the quality of outputs of its workforce. Additionally, this will also ensure that salaries are commensurate with cost of living thereby protecting the workers' purchasing power in real terms. The last salary upgrade for the public service was done in 2010 i.e. almost 10 years ago. To this end, the Government is providing a 30 percent increase to all public-sector salaries from 1 January 2018 as the centre piece of the 2018 Budget.

From 2018, this Government will be implementing tougher performance standards on all public servants in an effort to improve service delivery to the public. However, Kiribati public servants are amongst the lowest paid in the Pacific, and we cannot expect continual improvements in performance without offering the appropriate financial incentive. In order to ensure that our public servants receive compensation that is in line with what we are expecting of them, it is both necessary and appropriate that public sector pay scales be adjusted accordingly.

Being a general increase, the impacts on Ministry spending are broad-based and expected to generate dramatic improvement on public service morale. This will also give us all the mandate to ask more of our public servants to deliver better services to our citizens. Together with our customer service focus, our aim is to create a public service where performance is both expected and rewarded. For existing positions, this policy will cost a combined \$13.1 million across all agencies.

This measure is a central part of the Government's plans for improved public services. The ambitious targets set out in the KV20 will not be achieved if the Public Sector does not lift its performance accordingly. It is therefore crucial, Mr Speaker, that we take the next step in providing appropriate incentive and performance structures.

Government has also approved an Establishment Register Multi-Year Framework that provides a mechanism for the assessment of workforce requirement against Government's priorities, capability, capacity, efficiency level and impact of performance.

Other improvements include expanding the coverage of our oversight bodies, with the creation of the Leadership Commission to oversee the implementation of the Leaders Code of Conduct, improved transparency and inclusiveness of the Budget process through the inclusion of representatives of civil society and the private sector on the Government's Budget Committee, and investing an estimated \$3.1 million of the ADB's budget support in an upgraded Financial Management Information System.

REVENUE

The estimated total revenue for 2018 from all sources is \$204.3 million, which is an increase of 21.4% over the 2017 Budget figure, although significant revisions to revenue estimates in 2017 (mainly from fishing licenses) means that the 2018 Budget is an estimated 10.7% decline on the revised 2017 outcome. At this juncture, I would like to personally commend the Tax Office for its sterling progress in the collection of tax arrears in 2017, which has further boosted 2017 tax revenues above previous forecasts.

For 2018, total estimated revenue is made up of \$135.9 million (67.0%) from fishing revenue; \$44.8 million (22.1%) from taxation; and \$8.4 million (4.2%) from other Ministry sources.

It is important, Mr Speaker, that the figures presented in the Budget are a complete picture of the financial position. It is for this reason that for the first time, the 2018

Budget also includes an estimate of the interest earned in interest bearing cash accounts. For 2018, estimate interest earnings are \$1.3 million, a slight increase from the revised 2017 estimate.

In addition to this, there is an additional \$12.8 million in budget support from Economic Reform Taskforce (ERT) members: the World Bank, ADB, New Zealand, and Australia and additional support from Taiwan of \$1 million. I would like to personally thank each development partner involved in the ERT: the World Bank, the Asian Development Bank, New Zealand, and Australia for their continued support in the reform efforts, and for having the confidence in the Government's progress on ERT actions to directly contribute to our Budget systems and priorities. I would also like to thank Taiwan for the responsiveness of its development program to our priorities, including the offer to provide direct budget support.

Mr Speaker, let me now turn to the fishing license revenue figures for 2018 and beyond. In consultation with the Ministry of Fisheries and Marine Resources Development, the Ministry of Finance and Economic Development, and the IMF, the Government thinks that it is prudent to increase the long-term expectation of what annual fishing license revenue will be. For the 2018 Budget we estimate this figure to be \$130 million a year, which is slightly below the five-year average, and well below the recent highs experienced in 2015 and 2017 – it is still a conservative estimate. The annual Budget should be the main policy document of the Government taking into account our best estimate of expected revenues, thereby allowing the Government the time to feed all spending priorities through the annual Budget process at the same time. Supplementary Budgets are a less ideal platform for these decisions, as they spread decision making across the whole year. The Government firmly believes that the \$130 million target still favours a conservative view of the likely fishery performance, and provides us the opportunity to plan expenditures across the whole of 2018 and beyond.

Given our heavy reliance on fisheries revenue which is highly volatile and seasonal, it is important that we accelerate effort to bolster up and diversify our revenue base by identifying new sources of revenues to protect our bottom-line against major exogenous shocks. This is what we will be undertaking to do over the course of the next three, targeting air space and bunkering as potential revenue producers.

FISCAL POSITION AND CASH RESERVES

Mr Speaker, I would like to draw Members' attention to Table 1(b) of the Budget Book. This table sets out the fiscal position in a format more closely aligned to the internationally accepted Government Financial Statistics (or GFS). While this is not a full GFS framework, this new table gives a much greater level of detail than the previous Medium Term Fiscal Framework (still shown at Table 1(a)). This is one of the more significant improvements to the Budget Book, and brings us more in line with international best-practice. It also demonstrates this Government's commitment to improved transparency by showing the impact of the fiscal balance on cash reserves or debt levels.

According to this format, the operating balance (which excludes capital purchases or asset sales) is in a surplus of \$17.0 million. Once capital purchases are taken into account, **our fiscal balance in the 2018 Budget is a surplus of \$9.1 million.**

Looking at the forward estimates, the fiscal surplus is estimated to rise to \$10.9 million in 2019 and \$11.2 million in 2020, before falling to \$5.8 million in 2021 due to the scheduled conclusion of some of the development partners' current budget support programs.

This is a very healthy position for the Budget to be in.

Below the fiscal balance in Table 1(b), Members can see the division of the surplus across the various financing items and Government cash accounts. \$0.5 million is taken up by scheduled debt repayments on existing debts, mainly to the ADB (the details of which can be found at Appendix 6), \$1.3 million in interest earnings is retained in the Cash Reserve Account, and \$7.3 million is deposited into the Operational Account.

Mr Speaker, I would like to note that all major cash balances increase across the medium term, demonstrating our clear commitment to fiscal sustainability.

Table 1(b) also shows the projected value of the RERF over the coming years. Members will note with interest that if current market trends continue, the Government is firmly on track to reaching the KV20 target for the RERF of \$1 billion

by 2020. From the RERF report soon to be tabled in this House, Members will be able to see that there have been dramatic improvements in the performance of the portfolio, with 22.15% growth in the equities portfolio balanced against 1.0% growth in the fixed income. This has resulted in an overall increase in the RERF of 7.6% or \$65.5 million so far in 2017.

Mr Speaker, as I reported in my maiden budget speech, this Government is keen to explore ways of ensuring that the RERF benefits all generations. Once we have achieved the short-term target of \$1 billion, it is our intent to pursue changes that would allow the RERF to become an endowment fund that would provide a rules-based income stream for each and every generation from 2020 onwards.

CONCLUDING REMARKS

Mr Speaker, in closing I wish to acknowledge the continued support of our development partners in the many spheres of our development. As a small island nation with limited resources that can be exploited as a basis for sustained economic growth, we simply cannot shoulder our development burden alone. We will continue to rely and work with our development partners in a true spirit of partnership and cooperation as we forge ahead on our development journey. In this respect, we have been so privileged to have benefited until now from the generous contributions and support from our key development partners without which we would not have been where we are now. To all, kam bati n rabwa, thank you very much.

Last, but not least, I wish to sincerely thank my hard working and dedicated staff who have toiled tirelessly in putting together the budget book - and not forgetting of course the line Ministries for their equally valued support and contributions.

Let us all work together to propel our nation forward in an inclusive manner, making sure no one is left behind and with the ultimate goal that we live in a healthy, wealthy and peaceful nation. Together, we can do it.

With these remarks, Mr Speaker, I now beg to move that the 2018 Appropriation Bill be read the first time.

Thank you.