

BUDGET SPEECH 2016

DELIVERED ON 2 MAY 2016 ON THE FIRST READING
OF THE APPROPRIATION BILL (NO. 1) 2016

BY

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***Fostering inclusive growth through a more equitable distribution
of resources and the broadening of income-generating
opportunities***

Introduction

Honourable Speaker, I am pleased to present to this House and Kiribati the 2016 Budget, the very first budget of this newly elected Government. This Budget, Mr Speaker, is presented at a critical juncture. It comes against the backdrop of the recently completed presidential election in which the people of Kiribati voted overwhelmingly in favour of a change in government. The outcome of this election effectively handed over the baton of leadership to the Tobwaan Kiribati Party's presidential candidate, and now President of the Republic of Kiribati, His Excellency Taneti Maamau. This Budget therefore, Mr Speaker, marks the beginning of an era of the Tobwaan Kiribati Party, to lead Kiribati for the next four years or so under the leadership of His Excellency the President and his Cabinet ministers.

Honourable Speaker, a change over in government presents challenges and opportunities. As a successor government, we are both inheritors and

innovators. We are inheriting - whether for good or bad - what was left for us by the previous government. At the same time, we are presented with an opportunity to innovate solutions and new ideas that we believe will propel Kiribati to a higher level.

Mr Speaker, no one government is perfect. We all have our ups and downs. It would be remiss of this government, therefore, not to recognize the good work that the previous government has done for the people of Kiribati during their twelve years in government. And for that, Honourable Speaker, may I respectfully ask the Honourable Members of this House to give a round of applause in recognition of that good work. *(Thank you)*.

Budgetary Process

Honourable Speaker, the 2016 Budget is the product of the hard work and collaboration amongst all ministries and stakeholders. It is only right therefore, Mr Speaker, that I begin my presentation by thanking the staff of my Ministry for their dedication and hard work in formulating this budget. The support and cooperation from Line Ministries is gratefully acknowledged also.

The formulation of the 2016 Budget, Mr Speaker, was done taking into account (i) the financial capability of the government, thereby ensuring that we live within our means; (ii) the need to make sure that essential public services are not compromised; and (iii) the all-important objective of leading Kiribati to a path of sustained economic growth and prosperity.

Economic Outlook

Mr Speaker, the budget process must consider also the prevailing economic environment as this could have significant bearing on our economic performance, and indeed on our budgetary planning and allocation process.

According to the International Monetary Fund (IMF), the world economy is increasingly at risk of stalling. The IMF downgraded its growth forecast on the world economy for this year to 3.2%, down by 0.2 percentage point from its projection issued in January. This is only marginally above the 3% rate the IMF has previously considered a technical recession globally. China's slowdown, weak commodity prices and the continuing struggling of most of the developed countries to escape the legacies of the financial crisis are ascribed as the main causal factors for this economic stagnation. The IMF is worried such stagnation could further stifle investment, smother wage growth, curb employment and push government debt to unsustainable levels in some countries.

The continuing sluggish performance of the global economy has spill-over effects on us and the Pacific region at large. According to the Asian Development Bank (ADB) report launched early this year, Pacific economies, including Kiribati, face lower growth and tighter fiscal conditions this year due to low commodity prices and severe cyclones.

Based on the IMF's report, Kiribati's economy grew by 3.0% in 2015 driven by spending on infrastructure projects to upgrade a road and improve sanitation, which were funded by the World Bank, ADB and Australia. Higher fishing license revenues that enabled increased government spending also contributed to growth. The IMF believes that economic growth in the coming years will be modest but steady at 2.7 per cent in 2016 and 2.0 per cent in 2017. I believe that these figures will rise with the stimulus that the Government will be providing through the higher Copra Price Subsidy and free education to Form 4, 5 and 6 students, thus providing additional spending power for the people of Kiribati.

Inflation is forecast to remain subdued. In the March quarter 2016, the Retail Price Index rose by only 1.2 per cent compared with the same quarter a year ago. In 2015 the rise was 0.6 per cent and 2.1 per cent in

2014. The IMF forecasts inflation to remain low at 0.7 per cent in 2016 and 1.8 per cent in 2017.

Achieving fiscal sustainability is a major challenge for Kiribati, and indeed this government. Kiribati is heavily dependent on fishing revenues which account for 67% of total revenue. The expected significant decline in fishing revenues in 2016, as will be explained later, demands that we take decisive steps to manage our programs and expenditure priorities well to avoid an unsustainable and costly fiscal overrun. And this is exactly what this 2016 Budget is doing, as I will now discuss.

The 2016 Budget

Mr Speaker, the total recurrent budget for 2016 is \$149.1 million. This is inclusive of statutory expenditures totalling \$5.5 million. Therefore, the net amount to be appropriated by this House is \$143.6 million.

As Honourable members are aware, there is also a Development Budget amounting to \$152.5 million that I will present on Tuesday (i.e., tomorrow). To keep to tradition, I will focus for now on the Recurrent Budget and therefore subsequent references to the term 'budget' in this speech refer to the Recurrent Budget, unless otherwise stated.

Mr Speaker, let me first go through the estimated expenditures for 2016.

Estimated Expenditure

As stated earlier, the total estimated expenditure for 2016 is \$149.1 million. This is an increase of over 9% over the 2015 budget. Supplementary Estimates for expenditure in 2015, including a supplementary appropriation that I will present on Wednesday to cover the contingency warrants issued by the previous government also in December of last year, brought total budget for 2015 to \$136.5 million.

Mr Speaker, the biggest spending ministries are the Ministry of Education with a share of \$22.3 million, the Ministry of Health \$21.17 million, and Police & Prisons \$7.7 million. Together, these three ministries take up 34% of the total budget, with the other 66% distributed amongst the remaining nineteen ministries/departments. This skewed distribution of the budget is consistent with the present government's strategic priorities on education, health, and law and order.

I should point out, Mr Speaker, that one of the reasons for the increase in the Ministry of Health's budget this year is the inclusion of debts of the Ministry which have been outstanding since 2010, totalling \$2.4 million. It is a matter of concern to this government, Mr Speaker, that these outstanding debts were not cleared by the previous government.

Mr Speaker, if we break down the budget by category of expenditure, the distribution is as follows: \$61.7 million or 41% of total budget for Ministries' personal emoluments; \$30.6 million or 21% of total budget for Ministries' operations; \$40.96 million or 27% of total budget for subsidies and grants; \$14.8 million or 10% of total budget for local contribution to development; and \$1.15 million or 1% of total budget for debt servicing.

Mr Speaker, it important to note that this year we have increased the operating budgets of Ministries by 5 per cent. This is done with a view to boosting the operating capabilities of Ministries. Until now, the operating budgets of ministries have been subjected to very tight provisions, stifling their operational efficiencies and effectiveness. Personal emolument also registered increases arising from the addition of annual increments and increased leave grants introduced by the previous government.

Debt servicing is another component of the budget that becomes increasingly important. Annual debt payments for loans outstanding in 2016 are expected to amount to \$1.15 million. At present, Kiribati has total debt of \$48.7 million at the end of 2015 based on the loans that the

previous government entered, the major ones being (i) Asian Development Bank Loan for US\$10.2 million to finance Sanitation, Public Health Environment project (SAPHE) which will conclude in 2038; (ii) Asian Development Bank Loan for US\$10.71 million to support the Kiribati Road Rehabilitation project, which will conclude in 2042; (iii) Asian Development Bank Loan for US\$6.6 million for the South Tarawa Sanitation Improvement Sector Project, which will conclude in 2043; and (iv) International Cooperation and Development Fund (Taiwan) Loan (A\$20,227,983) for the repair and upgrade of Bonriki International Airport, which will conclude in 2043.

Mr Speaker, one of the most important, but often neglected, budget items is Maintenance for government buildings and infrastructure. For 2016, the provision for maintenance is \$811,595 which is small relative to the existing stock of public assets. Historically, the provision for maintenance hovers around \$685,000. We regard maintenance of buildings and infrastructure as critically important for sustained development and we will seek to beef up provision for this specific budget item in the coming years to a level proportionate with its important role and the need of the nation.

Let me now, Mr Speaker, turn to the much awaited component of the budget – Subsidies and Grants. As Honourable Members of this House are well aware, this government made commitments to the people of Kiribati that it will, amongst others, increase the price of copra from \$1 to \$2 a kilogram, offer free education from Forms 4, 5 and 6, and double its support to churches from \$500,000 to \$1 million. It is my greatest pleasure to inform this House and Kiribati, Mr Speaker, that all these three commitments are now being fulfilled and duly included in this budget for implementation. Of course, we have other commitments beside these three but we defer their implementation for now pending the completion of detailed studies on them that are underway. Note that the

support to churches referred to above will be paid out from the development fund.

The copra and free education subsidies cause a rise in the budget for subsidies and grants to \$40.96 million in 2016, compared with the revised estimate of \$29.2 million in 2015. The cost of doubling the copra price amounts to \$17.2 million in 2016, compared to \$7.95 million in 2015. The free education policy for Forms 4, 5 and 6 is expected to cost \$2.6 million in 2016 and \$2.7 million in 2017. Other rises in grants are attributable to the increases in Senior Citizens' benefit to \$2.9 million, as compared to \$2.04 million in 2015.

Mr Speaker, the early implementation of both the copra and free education subsidies is necessary. One of the main benefits of the increase in copra price is that it will discourage urban migration from the outer islands to Tarawa and at the same time encourage the unemployed on Tarawa to go back to their respective islands to earn income. This will help reduce pressure on South Tarawa and prevent other social problems associated with over-population. In essence, the copra subsidy will serve as a powerful incentive especially for people in the outer islands to use their resources more productively for their own benefits.

Our policy for free education for Forms 4, 5 and 6 will also be of great benefit to the people in the outer islands and the unemployed. Free education means a level playing field such that everyone has equal opportunity and access to quality education regardless of whether their parents are employed or not. Therefore, through this free education policy, higher education is no longer the exclusive privilege of the rich and employed as has hitherto been the case. Improved access to higher education enhances the marketability of I-Kiribati people to compete for employments locally and overseas.

Mr Speaker, the burning question that I'm sure the public want to ask is: *does this government have the money to finance all these expenditures and commitments?* The short answer, Mr Speaker, is YES it has. Let's look at the revenue side of the Budget to prove that.

Estimated Revenue

The estimated total revenue for 2016 from all sources is \$150.9 million, Mr Speaker. This is made up of \$101.4 million (67% of total revenue) from fishing revenue (licence fees & transshipment, etc); \$32.9 million (22% of total revenue) from taxation; and \$16.6 million (11% of total revenue) from other sources which include budget support from the World Bank, ADB and New Zealand of \$10.45 million for which this government is deeply grateful. I can assure these donors that the economic reform program as agreed with the previous government as one of the requirements for this extra-budgetary support will be continued by this government

Mr Speaker, Honourable members will notice a significant drop in revenue from fishing licence fees this year when compared to last year. 2015 registered a record amount of \$197.8 million, compared to \$100 million estimated for this year – a decline of 49%. Several factors account for this decline, including (i) the withdrawal of the EU fishing fleets; (ii) the reduction in the number of fishing days allocated to the US fishing boats; (iii) the uncertainty of the movements of the Australian dollar; and (iv) the end of the El Nino effect which has caused higher volumes of tuna in Kiribati waters since the beginning of 2015. The El Nino effect is expected to come to an end in the first half of 2016. This may have some effect on the number of fishing vessels in 2016. Based on these factors and the

advice of the Ministry of Fisheries, the forecast for fishing license revenue in 2016 is around \$100 million.

Taxation revenue in 2016 is expected to reach \$32.9 million. This contrasts with the preliminary estimate of \$35 million in 2015. The major reason for the drop in taxation revenue is the expected decline in VAT collections from \$14.5 million in 2015 to \$12.2 million in 2016. This is due to the previous Government's decision to cease VAT collections on State Owned Enterprises. All other areas of taxation are expected to rise or be near the same levels as in 2015.

Mr Speaker, let me take this opportunity to talk a bit on the RERF – Kiribati's biggest and single most important financial asset. At the end of December 2015, the RERF stood at \$756.3 million. International markets performed poorly in the first quarter of 2016 and the value of the RERF at the end of March dropped to \$744.2 million – a decline of 1.6%. Current forecasts are that global growth will resume in 2017 and we may see a sustainable rally in equities and an end to the recent cycle of back and forth moves experienced for most of the last 15 months. We expect, therefore, that the RERF will more than recoup its lost value within a relatively short period of time.

Honourable members will be interested to know that following a review of the performance of the RERF, new asset managers have been appointed in 2016, replacing the former fund managers – HSBC and NIKKO. The new fund managers are BlackRock and Northern Trust, both based in the US. BlackRock manages 50% of the RERF in equities while Northern Trust the other 50% in fixed income. This review of the RERF was one of the conditions for budget support from donors in 2015. The Government will pursue reform options to strengthen the governance of the RERF.

Mr Speaker, this government is not in support of the current policy which tends to encourage the perpetual building up of the RERF without much

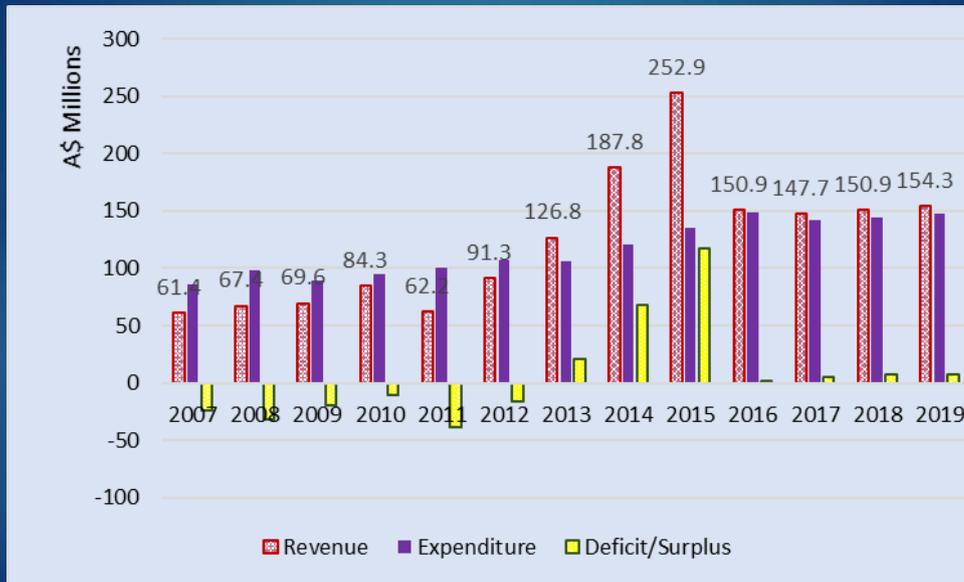
regards to distribute its pay-offs more evenly between generations. In our view, the RERF is an asset of Kiribati and therefore it should belong to every I-Kiribati and not the future generations only. Accordingly, this government will develop a policy that will ensure a more equitable distribution of the income from the RERF between generations while protecting the capital growth of the fund.

Overall Fiscal Position

All in all, Mr Speaker, the revenue situation for 2016 as outlined above is strong enough to enable the government to meet its commitments and expenditures as per the 2016 Recurrent Budget. Against the budgeted total expenditure of \$149.1 million above, there will be an expected budget surplus of \$1.8 million. Given this surplus, it is unlikely that there will be drawdown in 2016 from the reserve fund (RERF) to finance the budget. This is consistent with the policy of this government to limit drawdowns from the RERF on the basis that the RERF should be strictly a “lender of last resort” and should be utilised mainly for development purposes. It should be noted that our forecast for the fisheries revenues was based on the worst-case scenario and we are cautiously optimistic that fishing revenues for 2016 will surpass the amount estimated in this budget.

It is reassuring, Honourable Speaker, that despite the expected decline in revenues from fisheries and taxation, coupled with the implementation of copra and free education subsidies, the overall budget is in surplus, albeit small. The medium term fiscal framework which forecasts surpluses for the ensuing three years as per chart below provides added assurance.

TREND: Revenue/Expenditure/Deficits/ Surpluses



The Way Forward

Despite the positive fiscal position for 2016 as depicted above, this government will not rest on its laurels. We cannot rely on fishing revenues alone given its volatile and cyclical nature. We need to diversify and broaden our revenue sources to protect the government's bottom-line from shocks and unexpected shortfalls from fisheries.

Some of the new revenue sources that we will be exploring during our term include the imposition of access fees for the use of Kiribati's airspace by international airlines; imposing charges on multi-national firms (telecommunication companies in particular) for the use of our EEZ for their cables; tourism development especially in the Line & Phoenix group; and of course engineering a better return from our fisheries through joint ventures and/or better deals with the DWFNs.

On the expenditure side, we need to review and control certain expenditure items that are wasteful and non-productive. These include overseas travels; Kiribati's membership in certain international organisations; and subsidies to non-performing State-Owned Enterprises (SOEs), including subsidy to Fiji Airways. In so doing, we undertake to ensure that the operational efficiency of the public service and the effective delivery of essential services and programmes are not compromised.

This Government is determined to continue with the economic reform program which is starting to reap benefits for the country. We need to instil in SOE's a more commercial outlook so that they are a benefit to the community and not a drain on our finances. Public financial management requires improvements and the public sector needs to provide efficient and effective delivery of programs and services.

We will undertake to ensure that the management of the debt of the country does not get beyond our control. We will do this through strong policies to guide the level of indebtedness and only undertake concessional loans for the Government when really needed.

For the information of this House, Mr Speaker, the Government will soon launch a new Kiribati Development Plan (KDP) for the four years from 2016-19 in the first half of 2016. This plan will emphasise the Government's priorities for development including income generation programs to improve prosperity, better and cheaper education for our students, a healthier community and more job opportunities at home and abroad. The mission of this KDP is to promote better education, better health and inclusive sustainable economic growth and development through the implementation of higher education standards, the delivery of safe, quality health services and the application of sound economic policies. The Plan will focus on the following six key priority areas (KPAs):

Human Resources Development, Economic Growth and Poverty Reduction, Health, Environment, Governance, and Infrastructure.

Concluding Remarks

This 2016 budget that I have just presented embodies the government's spending priorities in line with its economic and strategic objectives, and how it will mobilise resources to finance them. It is the single most important policy instrument of the government, especially in Kiribati's case where alternative policy instruments, such as monetary policy, are relatively ineffective as tools to influence the economy in a desired way. It is imperative, therefore, that it is done properly but, more importantly, that it is sustainable.

The forecast for surpluses to continue over this year and the next three years as outlined above attests to the sustainability of the budget. At this level of aggregate spending, the Government will be able to meet its financial obligations without necessarily passing the burden to future generations, or the next government for that matter.

Mr Speaker, it would be ungracious of me to end this speech without thanking all our development partners for their invaluable and continued support to Kiribati over the years without which Kiribati would not have been at the stage it is in now. As a small developing island nation with limited resources, we simply cannot shoulder our development responsibilities alone. This government is therefore very grateful for all this assistance that our development partners have provided to date, and looks forward to the continuation and further strengthening of that relationship and cooperation into the foreseeable future.

With these remarks, Mr Speaker, I respectfully move that the 2016 Appropriation Bill be now read the first time.

Thank you, Honourable Speaker.