CAYMAN ISLANDS
GOVERNMENT

2018
Strategic Policy Statement

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Introduction

Mister Speaker, It is my distinct privilege to rise today and speak to the Government's 2018 Strategic Policy Statement or SPS.

The SPS outlines the Government's medium term fiscal plans, broad strategic outcomes and policy priorities for the next three financial years which cover the period 1 January 2018 to 31 December 2020. The SPS will also guide the preparation of the detailed 2018 – 2019 budget for the coming budget period which covers the 2018 and 2019 financial years and will be presented to this Honourable Legislative Assembly in October.

This SPS is the first one to be prepared following the 2015 and 2017 legislative amendments to the Public Management and Finance Law which shifted the Government's financial year from 1 July – 30 June period to a 1 January – 31 December period and changed our budgeting cycle from an annual one to once every two years.

Fiscal Strategy

The Government's medium term fiscal strategy, upon which this SPS has been developed, is centered on the following three guiding principles:

1. **Substantial operating surpluses each year;**

2. **No new fees or taxes levied on the public; and**

3. **No new borrowings apart from refinancing an element of the 2009 Bond.**

These guiding principles represent this Government's commitment to manage the financial affairs of the Government in a manner that achieves long term stability and sustainability.

Substantial operating surpluses each year

Managing the Governments' Operating Expenditure in a way that maintains healthy Operating Surpluses is a central guiding aim in our financial management strategy. Doing so enables the Government to use the cash generated by these surpluses to build and maintain reserves and fund its capital investment programme. This SPS sets out a clear plan for the Cayman Islands Government to do that.

Maintaining Operating Surpluses are a key component of ensuring compliance with the Principles of Responsible Financial Management and the Framework for Fiscal Responsibility set out in the Public Management Law. This SPS keeps the Cayman Islands Government firmly on the path of compliance with this important legislation.

No new fees or taxes levied on the public

Every Government derives its revenues from some form of taxation. The challenge for us is to find the right level of taxation to generate the revenues necessary to deliver the services and infrastructure required to service the needs of the people without stifling economic activity and negatively impacting quality of life for citizens and residents.

This Government has made the bold decision not to seek to introduce any new revenue measures at this stage. This was not an easy decision but was done in an effort to keep the tax burden as low as possible in an effort to keep the cost of living and cost of doing business as low as we can.

We will instead focus efforts on maximizing collection on the existing rates of fees by strengthening enforcement efforts and improving the ease of payment through E-Government initiatives and business process improvements.

No new borrowings apart from refinancing an element of the 2009 Bond

During the SPS period the Government will pursue a debt management strategy which seeks to aggressively pay down the outstanding Core Government Debt; and not incur any new borrowings except in 2019 when we are planning to borrow $130.65 million in order to refinance half of the 2009 Bond which matures in November 2019.

This borrowing will be specifically for this purpose and no loan proceeds will be used to finance operating activities or capital investments.

Mister Speaker, the Government has learned from its experience with the 2009 Bond that future borrowings are best structured as amortizing instruments with regular principal payments being made over the life of the debt as doing so smooths out cash-flows and reduces interest expense.

Broad Strategic Outcomes

In addition to our fiscal strategy, this SPS is centered around the eight Broad Strategic Outcomes which the Government has agreed will guide our policy actions over this term, these Outcomes are:

1. **A Strong Economy to Help Families and Businesses**
2. **Achieving Full Employment – Jobs for All Caymanians**
3. **The Best Education Opportunities for All Our Children**
4. **Reducing Crime and the Fear of Crime**
5. **Access to Quality, Affordable Healthcare**
6. **Stronger Communities and Support for the Most Vulnerable**
7. **Ensuring Caymanians Benefit from a Healthy Environment**
8. **Stable, Effective and Accountable Government**

Economic Forecasts

Turning now to the Economy, Mister Speaker, the Cayman Islands is blessed to have a strong, stable and moderately expanding economy. This Government is focused on ensuring that that our economy is on a path towards long-term sustainability in a way that brings maximum prosperity and opportunities for our people.

In our effort to support sustainable economic growth, we will continue the major economic policy interventions introduced during the past administration such as: reduced import duties; lower business licensing fees; development concessions; extended support to small businesses and other initiatives geared towards achieving greater economic diversification and increased employment opportunities for our people.

Over the next three financial years the Economics and Statistics Office has forecast that our economy will grow steadily, in-line with forecasts for the world's major economies, the source markets for our major economic pillars.

Economic growth as measured by the Real Gross Domestic Product (GDP) is expected to grow by 2.4% in 2018; 2.3% in 2019; and 2.0% in 2020. These forecasts are underpinned by the assumption that the three key sectors of the Cayman Islands economy: Financial Services; Tourism; and Business services will all continue to evolve and maintain their global competiveness.

In addition, economic growth will be directly influenced by several large construction projects from the private and public sectors including:

- new Hotel construction and redevelopment of existing Hotel properties along the Seven Mile Beach Corridor;
- development of a new hotel and condominiums in Beach Bay, Bodden Town;
- redevelopment of the George Town Cargo and Cruise Berthing port;
- Completion of the new John Gray High School;
- Construction of a new Long Term Residential Mental Health Facility;
- Procurement of the new Integrated Solid Waste Management System (ISWMS); and
- Completion and opening of the redeveloped and expanded passenger terminal at the Owen Roberts International Airport.

This diverse mix of projects from the public and private sectors demonstrate confidence in the economic potential of the islands and will help to strengthen our core infrastructure and position the Cayman Islands for long-term sustainable growth.

Over the next three years, economic growth will create additional jobs and keep the unemployment rate well below the 4% level. Unemployment rates are forecast to be 3.6% in 2018; 3.4% in 2019; and 3.5% in 2020.

Economic growth and increased levels of employment means that the consumption of goods and services will increase, this in turn places upward pressure on the rate of inflation (as measured by changes in the Consumer Price Index) which is expected to increase by 2.3% in 2018; 2.6% in 2019; and 2.4% in 2020.

Given our near total reliance on imported goods, inflation in Cayman is largely driven by external factors, as prices in the source markets increase so do our retail prices locally.

To help manage the impact of inflation the Government has taken the decision to leave in place the significant import duty reductions implemented in the last administration, most notably:

- **Reduced Import Duty of 25 cents per gallon down from 75 cents per gallon on fuel used by Caribbean Utilities Company for the generation of electricity;**

- **Reduced Import Duty of 20% down from 22% for licensed traders on consumer goods for retail sale; and**

- **Reduced Import Duty of 15% on building materials.**

By keeping in place these import duty reductions the Government is doing its part to keep retail prices low thereby keeping the cost of living for households and the cost of doing business as low as possible and stimulating consumption

Financial Forecasts

Mister Speaker, I will now highlight the financial forecasts which are contained in the SPS document.

However, before I do so, I need to spend a few moments to explain how the numbers in the SPS are different than those of previous SPS documents and the current 2016/17 Budget.

One of the most significant Amendments to the PMFL was to change the Government's financial year from a 1 July – 30 June period, to a 1 January – 31 December period.

As of 1 January 2018 our financial years will match the calendar, as a result the numbers you see in the SPS document for the 2018, 2019 and 2020 financial years are not directly comparable to those shown for the 2016/17 financial year which was a transitionary fiscal period covering 18 months of activity between 1 July 2016 and 31 December 2017.

Operating Revenue Forecasts

The Government's main revenue streams are directly tied to the level of consumption and rate of economic growth; generally speaking as the economy grows so do revenues.

In line with our overall fiscal strategy, the Government does not plan to introduce any major new revenue measures during the next three financial years.

Mister Speaker, the SPS forecasts that the Government's revenues will be approximately $717.9 million in 2018; $694.4 million in 2019 and $730.2 million in 2020.

These numbers are based on stable, conservative growth on our core operating revenue base plus the addition of one-off transfers to General Revenues being cash assets of Liquidated Entities which are forecast to be $19 million in 2018; $3.1 million in 2019 and $30 million in 2020.

Operating Expenditure Forecasts and Targets

Mister Speaker, the Government will continue to focus on controlling growth in operating expenditure, increases will only be allowed where they can be afforded and will be restricted to high priority areas. We will continue to challenge Government Agencies to seek to avoid increases by improving operational efficiencies.

Core Government Operating expenses are forecast to be $636.458 million in 2018; $640.364 million in 2019; and $639.855 million in 2020.

This Government is committed to restricting operating expenditure below the levels of our operating revenues in order to keep generating operating surpluses. Over the SPS period, increased operating expenditure will be used to fund a number of important initiatives including but not limited to:

- Enhancements to Policing and Public Safety by the hiring of additional Police Officers and Fire Officers along with the provision of enhanced training and support;

- The implementation of an enhanced Work Permit system which improves transparency on available jobs, increases accountability for employers and maximizes employment opportunities for Caymanians;

- Increased support for the Financial Services industry by enhanced Financial Services policy functions and improved regulatory services provided by the Cayman Islands Monetary Authority in order to keep pace with evolving international regulatory requirements;

- Enhanced tourism marketing to high value source markets and launch of new air service routes by Cayman Airways to new strategic tourism markets;

- Continued enhancement of public education services by improving services for addressing students with special needs; strengthening of core curriculum across primary and secondary schools for science, technology, mathematics and literacy; and increasing funding for overseas scholarships for advanced, specialized tertiary education;

- Increased monthly Ex-Gratia payments made to seamen, veterans, and persons receiving poor relief payments;

- Improved services and support to our elderly, disabled and other vulnerable persons in our society;

- Increased funding to the Cayman Islands National Insurance Company (CINICO) for the continued provision of health insurance services to its clients;

- Implementation of the Integrated Solid Waste Management System;

- Improvements to our vital mosquito control programme thereby mitigating risks to public health from mosquito borne diseases; and

- The implementation of an expanded Conditional Release Programme to better enable prisoners to successfully reintegrate into society as productive citizens following release from incarceration and to lower the rates of recidivism.

Capital Investment Forecasts

Mister Speaker, over the SPS period, planned capital investments are forecast to total some $309.3 million and will be spread over the three years as follows: $101.2 million in 2018; $103.3 million in 2019; and $106.9 million 2020.

These investments will be directed to support debt servicing obligations and operations of our SAGC's as well as the development of key infrastructure by the Core Government, such as:

1. completion of the new John Gray High School;

2. completion of the redevelopment and expansion of the passenger terminal at the Owen Roberts International Airport;

3. remediation of the George Town landfill and implementation of the Integrated Solid Waste Management System (ISWMS);

4. Construction of the Long Term Residential Mental Health Facility; and

5. Upgrades to our road network.

Compliance with Principles of Responsible Financial Management

Mister Speaker, maintaining compliance with the Principles of responsible financial management is another core element of this Government's fiscal strategy.

For the next three financial years we are forecasting that the Government will maintain compliance with the main Principles of Responsible Financial Management with a one-off non-compliance in 2019, which I will explain shortly.

Operating Surplus: The PMFL requires that the Government maintain a positive Operating Surplus. Over the next three years, the Core Government is forecast to remain in compliance with this requirement with Operating Surpluses forecast to be $81.497 million in 2018; $54.068 million in 2019 and $90.375 million in 2020.

These surpluses are critical to generating cash which will be used to pay off debt, maintain cash reserves and fund capital investments into both Core Government and our Statutory Authorities and Government Companies (SAGC's).

Over the SPS period, our SAGC’s combined are forecast to record net losses of $12.0 million in 2018; $12.1 million in 2019; and $14.4 million in 2020. These losses are driven primarily by preliminary estimates from CINICO of their actuarially assessed premiums. Given the limited time to review the submission from CINICO the Government has made a significant provision in its operating expenses for a premium increase to CINICO. As we go through the detailed budgeting phase this matter will be closely analyzed and addressed.

<u>Debt Service Ratio:</u>

The PMFL requires that annual Entire Public Sector debt service costs (interest and principal) not be greater than 10% of Core Government Revenues. The SPS forecasts indicate that the Debt Service ratio will be 8.9% in 2018; 48.2% in 2019; and 9.2% in 2020.

The spike to 48.2% in 2019 will bring the Government into non-compliance with this ratio during that year. However, it is important to point out that this “non-compliance” is a direct result of the planned repayment and refinancing the 2009 Bullet Bond that matures in November 2019. This is a one-off event and the Debt Service is expected to fall to approximately 9.1% in 2020.

Net Debt Ratio:

The PMFL requires that the Government's Net Debt not exceed 80 per cent of Core Government's Operating Revenues. Net Debt is calculated as the total amount of outstanding Core Government Debt plus the risk-weighted debt of Statutory Authorities and Government Companies (SAGC's) less the liquid assets of Core Government.

The Government is forecast to be in full compliance with this requirement over the next three financial years, with the Net Debt Ratio forecast to be 21.5% in 2018; 18.2% 2019; and 9.2% in 2020. This significant reduction places Government well below the maximum allowed limit of 80%, and is consistent with the Government's overall strategy of debt reduction and no new incremental borrowing.

Cash Reserves:

The PMFL requires that the Government have liquid cash reserves of not less than 90 days of estimated executive expenses.

This ratio is calculated at the point in the financial year when Government's liquid cash reserves are expected to be at their lowest, typically the 31 December of each year.

Over the period, the Government is forecast to maintain full compliance with this Principle as allowable liquid cash reserves – for the purposes of the ratio calculation – are expected to be $305.8 million (or 175.3 days) in 2018; $161.0 million (or 91.7 days) in 2019; and then be $170.0 million (or 97 days) in 2020.

The reduction in Cash reserves in 2019 reflects the planned Bond payment of some $130.65 million from our cash reserves.

Conclusion

Mister Speaker, the 2018 Strategic Policy Statement provides a strategic overview of the Governments financial resources and how they are likely to be allocated over the next three years. It is not a detailed Budget - that will come when I present the 2018 – 2019 Budget in October of this year.

As Legislators we must be cognizant of the need to balance the needs and wishes of the people today with our responsibility to make things better for future generations of Caymanians.

This SPS gives us a path to firmly maintain control over our finances while providing the resources necessary to address our critical needs; upgrade our infrastructure; modernize our public services; enhance services to the most vulnerable among us; improve our public education systems; create more opportunities for Caymanians; grow reserves to build our financial resilience; support stable, sustainable economic growth; protect our natural environment and overall build a stronger Cayman Islands.

Thank you, Mister Speaker.