Speech on Government's

2008/9 Strategic Policy Statement

Delivered by the Honourable Financial Secretary Kenneth Jefferson, JP, to the Legislative Assembly 30th November 2007.

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Part 1: Introduction

Thank you, Madam Speaker.

I rise in support of the Government Motion No. 6 /07-08.

Madam Speaker, the Honourable Leader of Government Business has provided an excellent overview of the 2008/9 Strategic Policy Statement (the "SPS") from a policy and strategic perspective. I would now like to highlight the main features of the economic forecasts, financial forecasts and long-run financial projections contained in the SPS.

Part 2: Economic Forecasts

Current Economic Conditions

Section 3 of the SPS provides the forecast economic position of the Cayman Islands for the period 2008/9 to 2010/11. These forecasts were prepared by the Economics and Statistics Office within the Portfolio of Finance and Economics.

Due to the continued recovery in the tourism industry and stable growth in the financial and business services sectors, the economy grew by 4.6% in 2006 compared to 6.5% post-Ivan growth in 2005. In comparison to the global economic growth of 5.4%, Cayman is only slightly lower by 0.8%.

The unemployment rate was 2.6% in 2006, however, for the first half of 2007 the unemployment rate changed marginally to 3.0% — consistent with the moderation of construction activities.

Consumer prices rose on average by 0.8 percent in 2006 compared to 7.3 percent in 2005. The slower pace in 2006 resulted from declining housing cost which followed the increase in housing supply in the post-Ivan period. However, in the first half of 2007, the average inflation rate stood at 3.7 percent compared to zero percent average inflation in the same period of 2006. This recent upward pressure was influenced by higher prices for personal goods and services, food and household equipment.

Overall, the latest economic data for 2006 and the nine-month period to September 2007 continue to show that the Cayman Islands' economy has rebounded from the effects of Hurricane Ivan. The data also sets the foundation for the economic forecasts for the next three years, which I will now discuss.

Economic Forecasts for the Next Three Years

The Economics and Statistics Office forecasts an economic growth of 3.1% in 2008/9, 3.0% in 2009/10 and 2.8% in 2010/11.

Employment levels are foreseen to rise from 35,520 in 2008/9 to 35,876 and 36,253 in 2009/10 and 2010/11 respectively. The unemployment rate is forecasted at 3.6% in 2008/9, and 3.7% in both 2009/10 and 2010/11.

The inflation rate, which is highly influenced by inflation rates in the United States of America, is forecasted at 3.3% in 2008/9, 3.1% in 2009/10 and 3.0% in 2010/11.

The balance of payments current account is forecasted at 18.5% of GDP in 2008/9, 18.0% in 2009/10, and 17.7% in 2010/11.The 2006/7 Strategic Policy Statement sets a surplus of $24.5 million as a target. The financial statements in the Annual Plan and Estimates indicate that the forecast surplus for the 2006/7 financial year is $32.5 million: it therefore exceeds the target set in the Strategic Policy Statement.

The Cash Flow Statement indicates $115.1 million will be used for the purchase or development of Executive Assets and $14.3 million for investments into Statutory Authorities and Government Companies is forecast to occur during the 2006/7 year.

Part 3: Aggregate Financial Targets for fiscal years 2008/9 to 2010/11The Executive

As with every SPS, Government's finite resources must be prioritized to meet the most essential needs of these Islands. The SPS for 2008/9 was not an exception. The Government went to considerable lengths to ensure that the financial targets — which are specified in this SPS — are not only robust, affordable and sustainable over the medium- and long-term but, that they are also in compliance with the Principles of Responsible Financial Management. These Principles are specified in the Public Management and Finance Law (the "PMFL") and requires the Government to be fiscally prudent.

Honourable Members will see from Section 4 of the SPS that the Government has forecasted Core Government operating revenue at $539.2 million in 2008/9, $552.5 million in 2009/10 and $564.7 million in 2010/11.

Core Government operating expenses are forecasted at $489.5 million in 2008/9, $516.5 million in 2009/10 and $537.9 million in 2010/11.

Operating surpluses are forecasted to be $49.7 million in 2008/9, $36.0 million in 2009/10 and $26.8 million in 2010/11.

On the balance sheet, net worth is expected to increase steadily over the forecasted period. Aggregate borrowing (which is the balance outstanding at the end of the period) is also expected to increase over the forecast period, however, as outlined by the Honourable Leader of Government Business, the anticipated borrowing levels remain within the limits prescribed by the Principles of Responsible Financial Management.

Net operating cash flows are targeted to remain at healthy positive levels which reflect the expected operating surpluses targets and a deliberate fiscal strategy to use part of the cash arising from operating surpluses to finance the Government's capital programme over the next three fiscal years.

Targeted net investing cash flows of $199.3 million in 2008/9, $103.4 million in 2009/10 and $72.3 million in 2010/11, reflect the Government's capital expenditure programme which includes three new high schools, one primary school, new government offices and improved road infrastructure. The decline in investing cash flows between 2008/9 and 2010/11 indicates that the majority of the Government's capital plans will be carried out by the end of the 2009/10 fiscal year.

The net financing cash flows reflect the Government's anticipated borrowing programme over the three-year period.

The targeted closing cash balance for all years satisfies the level of cash reserves required by the Principles of Responsible Financial Management.

Overall, the financial targets indicate an affordable fiscal position over the three-year forecast horizon.

Part:4 Longer-Term Financial Projections

To prove that the financial parameters set for the next three years are sustainable over a longer-period, a set of longer-term financial projections have been developed by Government. These projections, which are contained in Section 5 of the SPS, are for the seven financial years from 2011/12 through to 2017/18.

These projections, taken together with the three-year forecasts, provide a ten-year indicative fiscal track for the Government. This is long enough for the financial implications of policy decisions involving the end of the three-year target period to be fully reflected.

It is important to note that projections are not the same as forecasts. There are many uncertainties involved in looking-out over a longer-term period, and these uncertainties are too great to be able to prepare robust forecasts of likely financial activity. However, it is possible to project future revenues, expenditures and balance sheet activity on the basis of actual activity to date, the three-year targets contained in the 2008/9 SPS, current government policy, and assumptions as to future economic variables. The longer-term projections in Section 5 have been prepared on this basis.

The value of projections is not the precise position they show but rather the trend that they indicate.

The financial projections indicate that the three-year target track is sustainable over the ten-year projection period. The projections show sustained operating surpluses. More importantly, the cash flow projections show that these operating surpluses are sufficient to finance the new borrowings to be entered into over the forecast period.

Madam Speaker, recently there have been a few incorrect remarks made about the level of Government debt — those remarks put the level of debt at approximately $1 billion. Such an amount is incorrect.

Table 4, on page 17 of the SPS just Tabled, shows that the level of Government debt is expected to be approximately $244 million — which is considerably less than the incorrect $1 billion figure.

I suspect that commentators may have made the mistake of adding together the borrowing appropriations that are granted by the Legislative Assembly each year in arriving at the incorrect $1 billion figure. It is not usual for Government to borrow the full amount of its borrowing appropriation.

As an example, in the financial year ended 30th June 2007, Government had the authority from the Legislative Assembly to borrow $94 million: during that year Government only borrowed $23 million.

The projections show that new borrowings to fund the Government's planned capital programme, are affordable.

The projections show that starting 2011/12, the Government's fiscal position will allow capital expenditure of at least $61.0 million per annum. In other words, the capital expenditure and borrowing programme planned for the next three years still allows future governments enough capacity to incur sizeable amounts of capital expenditure over the medium to long-term.

Part 5: Conclusion

Madam Speaker, strong economic growth over the past year together with a projected increase in employment levels and a decrease in inflation rates in 2007, confirms the resilience and strength of Cayman's economy. As specified in the 2008/9 Strategic Policy Statement, the Government practises fiscal prudence and complies with responsible financial principles that are stipulated in the Public Management and Finance Law. I, therefore, support the Government Motion No 6/07-08 and I respectfully ask all Honourable Members to do the same.

Thank you, Madam Speaker.