

# Budget Policy Statement 2011

## 1. Statement of Responsibility

The following Budget Policy Statement is made with reference to and in accordance with sections 9 and 10 of the Public Finance and Economic Management (PFEM) Act number 6 of 1998.

Section 9 requires the Government to:

- Specify its economic and financial policies, including those relating to key economic and fiscal variables; and
- State the discipline it will adhere to in its economic and financial dealings.

Section 10 requires the Government to:

- State its **long term objectives** for fiscal policy in terms of major economic and fiscal variables;
- Specify the main **strategic priorities** guiding the preparation of the budget;
- Indicate the Government's **targets** for fiscal and economic variables; and
- Provide an assurance that the long term objectives outlined in the statement are:
  - Consistent with the Principles of Responsible Fiscal Management laid down in section 22 of the PFEM Act; and
  - Consistent with the previous year's Budget Policy Statement – that is, policies have remained consistent over time or, otherwise, justifications have been made for their departure.

Pursuant to section 10, the Government confirms that the fiscal policy objectives, strategic priorities and intentions are consistent with the Principles of Responsible Fiscal Management specified in section 22 of the PFEM Act of 1998 and that there is broad consistency with the 2010 Budget Policy Statement.



**Honourable Sela Molisa**  
Minister of Finance &  
Economic Management



**Georges Maniuri**  
Director General  
Ministry of Finance &  
Economic Management

## 2. Economic and Financial Policies

The PFEM Act of 1998 specifies the principles of responsible fiscal management. These require that the Government pursues budget policies that:

- Ensure that the Government's borrowing is kept at manageable levels;
- Maintain public assets in good condition;
- Manage fiscal risks prudently;
- Maintain stable and predictable tax rates.

The Government's highest priority for Budget 2011 is to maintain Vanuatu's economic growth and the well-being of all ni-Vanuatu, in a way that is financially sustainable and does not jeopardize future economic growth.

The Government will achieve this by sound management of public finances and by following fiscally responsible policies. Section 22 of the PFEM Act requires that the Government adheres to a set of defined principles of responsible fiscal management. These are set out in the box opposite.

### **Principles of Responsible Fiscal Management**

1. Reducing, and then managing, total State debt at prudent levels so as to provide a buffer against factors that may impact adversely on the level of total State debt in the future, by ensuring that, unless such levels have been achieved, the total overall expenditures of the State in each financial year are less than its total overall receipts in the same financial year;
2. Achieving and maintaining levels of State net worth that provide a buffer against factors that may impact adversely on the State's net worth in the future;
3. Managing prudently the fiscal risks facing the State; and
4. Pursuing policies that are consistent with a reasonable degree of predictability about the level and stability of tax rates for future years.

## 3. Budget Policies

Government's Budget Policies come from the application of the "Principles of Responsible Fiscal Management" section 22 of the PFEM Act of 1998. The Budget Policies consist of:

1. Budget Priorities for 2011;
2. Economic and Fiscal Targets for 2011; and
3. Long Term Fiscal Objectives

#### ***a) Budget Priorities for 2011***

As a matter of careful consideration, the Government has selected for the four year duration, priority areas set forth in the Planning Long and Acting Short (PLAS) matrix. In 2011, the Government will continue to pursue its existing policies which are set out as follows:

- Better access to primary education and strengthening of youth development;
- Strengthening accountability and transparency in public offices and institutions;
- Ensuring equitable and sustainable development of land;
- Providing reliable and accessible infrastructure services;
- Supporting the productive sectors;
- Offering quality health care;
- Decentralisation and institutional strengthening;
- Political stability; and
- Strengthening security and the rule of law.

The Government will continue to implement policies that improve the business environment, with particular emphasis on issues constraining growth prospects. As part of this program, the Government will resort to continue its reform of state-owned enterprises and utilities.

#### ***(b) Fiscal Policies***

The Government's high priority for 2011 is to manage its budget in a way that promotes economic growth and the distribution of that growth to all the communities of Vanuatu. The Government will continue to implement policies that encourage private sector led growth and will ensure that state-owned enterprises are as productive as possible in the long-run.

#### ***(c) Fiscal Position in 2011***

According to the last International Monetary Fund (IMF) world economic update, the economic recovery in most advanced economies has got off to a stronger start than earlier anticipated but is occurring at differing rates across the globe. In most emerging and developing economies activity is expected to be vigorous, driven by buoyant internal demand. More importantly, Vanuatu's Major Trading Partners have weathered the global economic crisis relatively well and are forecasted to maintain positive growth over the medium term.

Vanuatu's economy continued to recover but at a much slower pace than initially forecasted according to recent partial indicators. Private sector credit has slowed recently, tourist arrivals have weakened and the data on construction and consumption suggest a softening. All of these factors would lead to lower than anticipated inflows in government receipts. In line with these developments, economic growth projections were recently downgraded - to 4.1 per

cent in 2010 and by 3.7 per cent in 2011. Nonetheless growth is expected to remain above trend.

***(d) Budget Management***

Budget 2011 will be consistent with the principles of fiscal responsibility as defined by section 22 of the PFEM Act. The Government will continue to commit itself towards achieving a balanced budget in 2011.

***(e) Government Debt and Borrowing***

The Government will continue to ensure that public debt remains at a manageable level during 2011 and successive years and will restrict any new borrowings, unless for productive purposes to reflect current policy directions. The Government will ensure that external and domestic borrowings are limited to the financing of capital investment projects which generate future capacity to repay the loans bequeathed upon future generations.

***(f) Revenue and Taxes***

The Government's priority for revenue is to increase coverage and strengthen the administration of existing taxes; this includes the more remote areas of the country. There will also be focus on the effective implementation of new changes to excise duties, exemptions and previous changes relating to taxes on land and other assets. To meet these goals, the Government has recently allocated additional funds to the Department of Customs and Inland Revenue for further recruitment and purchasing of Asycuda software to reinforce the administration of government receipts. The ongoing initiative of the Government opening up offices of customs, finance and statistics in the provinces will also help improve administration.

***(g) Expenditure Programme Policies***

The Government's priorities for expenditure programmes are to continue to enhance funding for the provision of essential services and to ensure that expenditure remains within the budgeted amount. The Government will also be directing greater attention to expenditure productivity to ensure maximum value of public funds. To this end identifying efficiency gains, eliminating unproductive expenditures, and enforcing strict fiscal discipline and punitive measures are all part of the Governments efforts to achieve greater quality, efficiency and accountability of service.

#### ***4. New Policy Proposals***

Each year the Government sets aside funds for New Policy Proposals that are consistent with the Government's policy priorities.

New Policy Proposals that fall within the policy areas identified at 3 (a) will only be considered for funding in 2011 if they are:

- Well researched and fully developed proposals to reinforce the Government's key policies and programs;
- Within the capacity of the Ministry to implement over the suggested time frame;
- Able to expand and develop the economic capacity and growth rate of the country; and
- Sustainable within future recurrent funding.

Budget 2011 will include donor funded New Policy Proposals that have been developed to implement government policy priorities such as access to primary education. This will ensure that donor funding is channelled through the Government of Vanuatu Budget Management System (VBMS) and is in line with Government funding. Merging the two funding streams will result in a significant efficiency gain. Further, the integration of the budget process will enable the Government to better manage the recurrent cost implications and hence improve the financial sustainability of capital investment in essential public services.

#### ***5. Economic and Fiscal Targets for 2011***

In preparation for unforeseen shocks to the domestic economy, the Government will continue to pursue policies towards achieving a balanced budget in 2011. The economic growth rate for 2011 is forecasted to be 3.7 per cent in real terms, while the inflation rate is projected to be within the range of 3.0 to 4.0 per cent.

<b>Budget Targets for 2011</b>	<b>Long term fiscal objectives</b>
<b>Budget balance</b> Balanced Budget	Recurrent balance is positive over the medium-term
<b>Revenue</b> Recurrent revenue is forecast to be at least 19.0 per cent of GDP	There is a broad revenue base with sufficient revenue to meet the Budget Balance objective
<b>Expenditure</b> Recurrent expenditure is forecast to be 19.0 per cent of GDP	Expenditures are consistent with the Budget Balance objective
<b>Debt</b> Public debt remains at manageable level	Debt maintained at prudent levels so its share in GDP remains below 40.0 per cent

<b>Economic Growth</b> Growth forecast at 3.7 per cent	Annual economic growth rate averages at least more than population growth rate (2.6 per cent)
<b>Inflation</b> Inflation forecast at 3.0 – 4.0 per cent	Annual inflation rate remains below 4.0 per cent

## ***6. Conclusion***

Preparation for the Budget 2011 will be based on existing government policies and priorities. The budget will be prepared in line with the “Principles of Responsible Fiscal Management” and the long term fiscal objectives of the Government.

There remains uncertainty as to the performance of domestic consumption and private investment. This presents a challenge to revenue forecasts and expenditure policies in Budget 2011. The balance of risks to the near term outlook is on the downside. The Government will continue to be guided by fiscal prudence and will ensure that spending pressures in 2011 are controlled.