



GOVERNMENT OF KIRIBATI  
MINISTRY OF FINANCE & ECONOMIC DEVELOPMENT

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## Fiscal Strategy for the 2023 Budget Executive Summary

The Fiscal Strategy outlines the major parameters used to develop the 2023 Budget. This includes the ceilings to be applied to Ministry operating and personnel budgets.

The overall aim of the 2023 Fiscal Strategy is to demonstrate commitment to responsible fiscal management, by resolving legacy debt and providing for funding gaps and policy priorities, as well as enhancing value for money in the delivery of Government services, thereby supporting improved economic resilience and inclusive economic growth.

For 2023, the Government will continue to implement the Medium-Term Fiscal Strategy (MTFS) introduced in 2022, and seek to grow net worth, reduce debt, and adopt a fiscal stance consistent with economic conditions that supports delivery of services and development projects. Reforms will be pursued to improve expenditure efficiency and mobilize revenue.

Economic conditions are expected to be subdued in 2023, with the IMF April 2022 World Economic Outlook (WEO) forecasting growth of 2.3 per cent and inflation of 3.3 per cent in 2023. This context suggests that Government should continue to stimulate the recovery, including through provision of social protection payments, whilst improving program administration and expenditure efficiency. Inflationary pressures are expected to put pressure on Ministry outlays and project costs, as well as impact on consumption related revenues.

The fiscal estimates for 2023 build on the 2021 outcomes. The preliminary final budget outcome for 2021 is a small surplus of **\$5.03 million**, compared to an expected deficit of **\$25.4 million**. The outcome is better than expected, and reflects stronger fisheries and taxation revenue collections than anticipated. Outlays were also generally lower than expected.

Reflecting strong historic revenue performance, the base case forecast for revenue in 2023 is **\$325.3 million**, a **7 per cent** increase on the 2022 Budget estimate. This reflects fishing revenue estimates based on historic performance, and increases in tax revenues reflecting recent average growth rates. A RERF dividend of **2 per cent** is proposed, consistent with the 2022 Budget assumption. This is for planning purposes, and may not necessarily be used – the actual dividend will depend on 2022 RERF performance.

Taking account of the economic outlook, base case departmental budget ceilings have been uplifted by **3.5 per cent** to take account of inflationary pressure on operational and staff costs. Measures to support the COVID-19 recovery will continue, including Copra Subsidy and SFU payments. However, proactive policy action is required to improve the targeting and efficiency of these schemes with a view to improving their long run affordability.

Similar to the 2022 process, expenditure proposals above the ceiling will be considered through a New Program Proposal (NPP) process and prioritized should fiscal space be identified. Cash reserves will be used to meet any funding gaps.

There are two options proposed for the Local Contribution to the Development Fund (LCDF). Option A is the no policy change option, and includes no new measures beyond explicit recognition of the provision for RERF projects, consistent with the Withdrawal Policy. Option B includes new measures to cover unfunded Government policy commitments and address fiscal pressures.

Option B would facilitate meeting Government budget priorities that include maintaining the COVID-19 response and supporting the recovery; investing in improved Government payment administration and service delivery, including a new Integrated Financial Management Information System (IFMIS) and related legal reforms; addressing legacy Government payment arrears and debt to improve the financial viability of State-Owned Enterprises; invest in urgent maintenance of electricity, water and sewerage infrastructure; deliver on outstanding Manifesto Commitments, including the non-government leave grant; progress financial sector reform to support private sector development, and mobilize revenue, as well as provide for unfunded projects.

Option A total expenditure is estimated at of **\$326.3 million, 7 per cent (\$21.1 million)** higher than 2022. Option B has expenditure of **\$362 million, 19 per cent (\$56.9 million)** higher than the 2022 Budget estimate.

Both LCDF expenditure base case estimates lead to an expected budget deficit. The base case balance estimate for Option A is a deficit of **\$957 thousand**, and for Option B, a deficit of **\$36.7 million**. For both options, fiscal responsibility ratios continue to be met.

Cash reserves as at 13 May 2022 were \$175.9 million, providing 6 months of expenditure cover. It is proposed to take the opportunity of the strong cash reserves position to use Option B as the base case, and address fiscal pressures and risks to improve longer term fiscal resilience. This is consistent with providing some fiscal stimulus to support the COVID-19 recovery. The final size of the deficit will depend on Government decisions as part of the budget process.

There are inherent risks in the estimates related to the assumptions that underpin them. Sensitivity analysis indicates the potential impact of these risks. In all cases, if the risks eventuate, fiscal responsibility ratios can be maintained.

# **Fiscal Strategy for the 2023 Budget**

## **Introduction**

The Fiscal Strategy outlines the major parameters the Government will use to develop the 2023 Budget. This includes the ceilings to be applied to Ministry operating and personnel budgets.

The Fiscal Strategy must ensure that the top priorities of Government can be met in a sustainable way, without compromising the delivery of essential services or the budget in the long run – particularly in an environment where extremely volatile fishing revenues can lead to significant risks.

The 2023 Budget will be framed within the Government’s Medium Term Fiscal Strategy (MTFS). This strategy establishes high level goals to achieve macro-economic stability in the medium term, consistent with the aspirations in the Kiribati 20 Year vision (KV20), for Kiribati to be healthy, wealthy, and safe, with people at the center.

The 2023 Budget also needs to take account of economic conditions and fiscal pressures, including the impact of inflation on operational and project costs, the need to address Ministry and State-Owned Enterprises (SOEs) payment arrears and overdue debts, increases in international subscriptions that must be paid through the year, and the costs of projects and policy initiatives that have been agreed but not funded.

The Fiscal Strategy includes an overview of the MTFS, 2021 budget performance, the economic outlook, 2023 Budget priorities, base case forecasts to underpin the proposed fiscal settings for 2023, sensitivities and risks.

Publication of the 2023 Fiscal Strategy reflects the Government’s commitment to improved public financial management and transparency. Publication is consistent with global best-case practice, and is recommended under the International Monetary Fund’s (IMF) Public Expenditure and Financial Accountability framework.

## **Medium Term Fiscal Strategy (MTFS)**

KV20 articulates long term goals related to achieving macro-economic stability, including implementing policy settings that will increase Gross Domestic Product (GDP), fisheries revenue contributions, the private sector’s share of GDP and protect the real value of the Revenue Equalization Reserve Fund (RERF) over the long-term.

The goal of the MTFS is to achieve macro-economic stability and build a resilient, wealthy, healthy and secure nation, through responsible fiscal management by:

1. Growing financial net worth over the medium term, through prudent management of the RERF and cash balances and reducing debt. Where new debt is considered, it must be concessional, with at least a 35 per cent grant component;
2. Achieving budget balance over the medium term consistent with economic conditions and inclusive economic growth, with the aim to fully fund Government consumption and investment from current revenue by:
  - a. Revenue mobilization and diversification
  - b. Improving the efficiency and effectiveness of expenditure (value for money) and government investment
3. Investing in productivity enhancing social and economic infrastructure consistent with KV20 priorities and a proactive climate change response, with the aim to support future sources of growth and improved allocative efficiency; and
4. Structural reforms to diversify the economy and build resilience, with the aim to facilitate a vibrant private sector and create meaningful jobs.

This strategy is supported by the achievement of two fiscal responsibility ratios, to mitigate fiscal sustainability risks:

1. Departmental expenditure not to exceed 50 per cent of total expenditure; and
2. Maintenance of liquidity cash buffers of at least three months expenditure.

### **Performance against the MTFS**

The MTFS was adopted in 2021 for the 2022 Budget. A brief assessment of performance against the strategy to date includes the following.

- Net worth increased, with no new debt in 2021 or 2022, and a RERF 31 December 2021 balance of **\$1.4 billion**, equivalent to **490 per cent of GDP** and **\$11,417** per capita.
- The 2022 Budget targeted a modest surplus, with a proposed RERF drawdown consistent with the Withdrawal Policy. The 2021 preliminary budget outcome is for a small surplus balance. Fiscal responsibility ratios were met.
- Revenue mobilization reforms are in train, including a revised Income Tax Act and administration improvements.
- Key expenditure risks are being mitigated by investment in a new Integrated Financial Management Information System (IFMIS), updated financial administration

procedures and reforms to how social protection payments are administered, as well as work to improve the governance and performance of SOEs.

- Investments in social and economic infrastructure are being pursued with donor support, including investment in water, sanitation, outer island transport infrastructure and renewable energy generation.
- Structural reforms in the financial sector are being progressed to improve financial intermediation and financial inclusion.

## 2021 Preliminary Budget Outcome

The preliminary final budget outcome for 2021 is a small surplus of **\$5.03 million**, compared to an expected deficit of **\$25.4 million**, as shown in Table 1. If the RERF dividend is excluded, the outcome would be a deficit of **\$34.9 million**.

**Table 1: Preliminary 2021 Budget Outcome**

Item	2019 Actual \$	2020 Actual Consolidated \$	2021 Budget Revised \$	2021 Preliminary Actual \$	Share of Budget %
<b>Total Recurrent Revenue</b>	<b>285,258,217</b>	<b>248,870,320</b>	<b>279,472,655</b>	<b>295,394,080</b>	<b>106%</b>
<b>Total Domestic Revenue</b>	<b>284,758,222</b>	<b>241,862,015</b>	<b>265,500,677</b>	<b>285,044,765</b>	<b>107%</b>
Fisheries revenue	226,307,228	184,068,815	165,496,000	168,979,738	102%
Taxation revenue	49,440,666	51,649,018	49,996,724	65,352,479	131%
Investment revenue	2,294,377	1,752,240	5,000,000	4,545,808	91%
RERF Dividend			40,000,000	40,000,000	100%
Other Ministries Revenue	6,715,951	4,391,942	5,007,953	6,166,740	123%
<b>Total donor budget support</b>	<b>499,995</b>	<b>7,008,305</b>	<b>13,971,978</b>	<b>10,349,315</b>	<b>74%</b>
<b>Total Recurrent Expenditure</b>	<b>246,464,771</b>	<b>239,130,584</b>	<b>304,889,601</b>	<b>290,367,555</b>	<b>95%</b>
Departmental Expenditure	117,501,796	115,432,195	138,666,865	135,806,640	98%
Other Government expenditure	33,007,180	56,349,746	113,750,220	105,337,286	93%
Debt servicing	2,845,228	3,409,452	3,681,768	3,520,588	96%
Local Contribution to Development Fund	93,110,567	63,939,191	48,790,748	45,703,041	94%
<b>Recurrent Balance</b>	<b>38,793,446</b>	<b>9,739,736</b>	<b>(25,416,946)</b>	<b>5,026,525</b>	<b>-20%</b>
<b>% of GDP</b>	<b>15%</b>	<b>4%</b>	<b>-9%</b>	<b>2%</b>	
<b>Recurrent Balance (Excl RERF Dividend)</b>	<b>38,793,446</b>	<b>9,739,736</b>	<b>(65,416,946)</b>	<b>(34,973,475)</b>	<b>53%</b>
<b>% of GDP</b>	<b>15%</b>	<b>4%</b>	<b>-24%</b>	<b>-13%</b>	
Cash Reserves	140,277,833	251,230,806	184,744,357	166,983,422	
FRR: Dept Exp as % of total (<50%)	48%	48%	45%	47%	
FRR: Cash reserves in exp months ( 3 months)	7	13	7	7	
NOTE: 2020 and 2021 Actuals reflect unaudited figures and may change. 2022 as at July 2021 and 2021 at 13 May 2022					

The outcome is better than expected, and reflects stronger fisheries and taxation revenue collections than anticipated. Outlays were also generally lower than expected

## **2023 Budget Strategy and Ceilings**

The proposed 2023 Budget base case settings take account of the medium-term strategy and how it can be achieved in light of expected economic conditions, fiscal risks and Government policy priorities to be delivered in 2023.

### ***Economic Outlook***

The Government uses IMF economic forecasts to underpin the economic assumptions used to develop budget estimates.

According to the latest IMF World Economic Outlook (April 2022), the global economic recovery is expected to moderate, reflecting the impact of the war in Ukraine and continued uncertainty relating to the COVID-19 pandemic, impacting commodity prices and supply chains, feeding into higher fuel and food prices.

Global growth is projected to slow from an estimated 6.1 per cent in 2021 to 3.6 per cent in 2022 and 2023.

Beyond 2023, global growth is forecast to decline to about 3.3 percent over the medium term. War-induced commodity price increases and broadening price pressures have led to 2022 inflation projections of 5.7 percent in advanced economies and 8.7 percent in emerging market and developing economies. Multilateral efforts to respond to the humanitarian crisis, prevent further economic fragmentation, maintain global liquidity, manage debt distress, tackle climate change, and end the pandemic are considered essential. Risks to the outlook continue to be on the down-side with the continued evolution of the COVID-19 pandemic, and global political instability.

For Kiribati, the slow border re-opening and continued travel restrictions remain a brake on growth. The COVID-19 outbreak in the first quarter of 2022 will also have set back recovery.

The IMF estimates for Kiribati, have been downgraded since the last economic outlook in October 2021. The IMF now expects that Kiribati GDP increased by 1.5 per cent in 2021, but will slow to 1.1 per cent in 2022, lifting to 2.8 per cent in 2023 as vaccination rates increase and containment measures ease (leading to increased labor mobility and port activity), and investment projects move forward.

The modest global outlook should support positive RERF returns, albeit at lower levels than achieved in 2021. Fishing revenues are also expected to moderate all other things being equal.

Economic conditions suggest that continued Government outlays can be justified to support the COVID-19 recovery, such as the Copra Subsidy and Support for the Unemployed (SFU) payments. However, proactive policy action is required to improve the targeting and efficiency of these schemes with a view to improving their long run affordability.

Risks for Kiribati are skewed to the downside and relate to the potential impact of another COVID-19 outbreak, the duration of containment measures that limit labor mobility, port activity, and project progress, as well as the impact of global economic conditions on RERF performance and fishing demand.

Inflation is expected to peak at 5 per cent in 2022 before falling back to 3.3 per cent in 2023. This reflects higher commodity costs from the Ukraine conflict as well as supply chain constraints and higher shipping costs from COVID-19. These are expected to be temporary and to have worked themselves through by 2023.

Inflationary pressures are expected to put pressure on Ministry outlays and project costs, as well as impact on consumption related revenues.

The IMF's nominal GDP estimate is \$311 million for 2023.

## **2023 Budget Priorities**

The following priorities are expected to inform the 2023 Budget setting:

- Continued commitment to fiscal responsibility and implementation of the medium-term fiscal framework. With subdued economic conditions, the fiscal settings will need to reflect a more stimulatory stance, and a small recurrent deficit.
- COVID-19 response and recovery – investment in health infrastructure, vaccination roll out, quarantine facilities and economic recovery measures, including support for addressing cost of living pressures and continuation of SFU payments and Copra Subsidy at current levels.
- Strengthening Government payment administration and service delivery, including social protection payment administration, and investment in a new integrated financial management information system (IFMIS) and related legal reforms.
- Addressing Government payment arrears to SOEs and between SOEs to support SOEs to be more efficient and effective in delivering services, and to improve their underlying financial viability, and more broadly improve fiscal resilience by addressing legacy debt and supporting future macro-economic stability.

- Investment in productivity enhancing infrastructure, including in electricity, water, sanitation and transport, across the country, and for high priority projects that have been approved, but funding not yet secured.
- Provision for Government Manifesto Commitments that have not yet been funded or implemented, including the non-government leave grant.
- Revenue mobilization through reforms to taxation administration and RERF withdrawals consistent with the Withdrawal Policy.
- Implementation of financial sector reform, supporting improved financial intermediation and financial inclusion.

The overall aim is to ensure that as part of the commitment to responsible fiscal management, legacy debt and funding gaps are addressed, and service quality continues to improve, enhancing value for money in the delivery of Government services, supporting improved economic resilience and inclusive economic growth.

## **2023 Budget Assumptions**

The key assumptions in formulating the 2023 Budget baseline estimates include:

- 2023 economic conditions will be consistent with the IMF forecast of 3.6 per cent global growth, 2.8 per cent Kiribati growth, and 3.3 per cent inflation;
- Fishing revenue estimates will be consistent with historic performance;
- RERF dividends will be consistent with the RERF Withdrawal Policy, and a return consistent with the long run average of 7 per cent;
- Revenue volatility will be managed by accessing cash reserves;
- There will be significant policy changes from current settings – this includes the introduction of Leave Grants for non-ER posts, and the continuation of a Copra Subsidy of \$4 a kilo, and SFU payments of \$50 a month;
- Kiribati will be largely COVID-19 free and containment measures will be progressively eased as vaccination rates increase, enabling employment and economic activity to increase and projects to restart and progress.
- Borders will re-open by August 2022, and travel restrictions will be removed enabling free flow of people and goods supporting economic activity, assuming transport connectivity issues can be overcome;

- Donor budget support payments are conditional on meeting fiscal responsibility and economic reform commitments, as articulated in the Economic Reform Taskforce (ERT) Matrix.

The base case estimates are summarized in the table at **Attachment A**. These estimates reflect assumptions at a point in time, and are subject to change.

## **Revenue Estimates**

The starting point of the 2023 Budget is to forecast a realistic revenue envelope that provides a ceiling for expenditure.

The modest global outlook should support positive RERF returns, albeit at lower levels than achieved in 2021. Fishing revenues are also expected to moderate all other things being equal. Inflation should boost consumption related revenues.

A key challenge is the assumption around fishing revenues. Historically, fisheries forecasting has tended to significantly under-estimate expected fishing revenues. In 2020, fishing revenues out-performed the estimate by nearly a quarter, resulting in an overall surplus, rather than the expected deficit. However, 2021 revenues, whilst exceeding the original estimate, did not perform as strongly, reflecting the impact of the COVID-19 pandemic and travel restrictions limiting export opportunities.

The proposed 2023 Budget base case is for a realistic estimate of fishing revenues, consistent with historic revenue levels (three-year actual average). There is likely to be some upside potential in this estimate, as 2023 collections to March 2022 are strong.

The RERF Withdrawal Policy enables Government to plan for orderly RERF withdrawals to support economic development priorities. Dividends can only be drawn down where the fund's real rate of return was over 5 per cent in the previous year, and revenue can only be used for development projects approved by Cabinet. This rule protects the real value of the fund over time, consistent with KV20 objectives.

For the purposes of the Fiscal Strategy, RERF revenue estimates are based on the implementation of the RERF Withdrawal Policy, and an assumption that real returns will be **7 per cent** (equivalent to the long run estimated RERF return with the 50:50 investment strategy) and therefore **2 per cent, or \$26.6 million**, will be available to draw down.

This **2 per cent** must be hypothecated to development projects identified by Cabinet. Projects need to support investment in building human, social or economic capital, rather than consumption. In 2022, the RERF dividend included in the Budget was directed towards human

capital through expenditure on education related grants and subsidies. This has to be remained for 2023 with the inclusion of the infrastructure maintenance project.

The dividend revenue accrues to the Consolidated Fund (No 1 Account), and must be appropriated to be able to be spent.

The RERF dividend estimate assumes that **\$23 million** dividend will be paid in 2022, consistent with the 2022 Budget. If this is not the case, and the full amount of available dividend is drawn down (**\$80.6 million**) then the estimate for the available dividend for 2023 will be reduced by **\$2.8 million**.

In 2021, tax revenues performed very strongly, supported by the flow through of Government recovery measures, including the SFU and Copra Subsidy payments. This is expected to continue through 2022 and 2023, assuming no policy change. To improve the accuracy of the estimate for tax revenues, the forecast assumes that tax revenues will continue to grow at the average rate achieved over the past two years.

Outyears for all estimates, except the RERF are escalated by an inflation assumption of 3 per cent.

Overall, the proposed base case revenue funding envelope is **\$325.3 million**, a **7 per cent** increase on the 2022 Budget estimate. The detail of the estimate is at **Attachment B**.

### **Expenditure Estimates**

For 2023, reflecting the economic outlook, base case departmental budget ceilings have been uplifted to take account of expected increases in operational and staff costs. Measures to support the COVID-19 recovery will continue, including Copra Subsidy and SFU payments. It is also proposed to take the opportunity of the strong cash reserves position to address fiscal pressures and risks, including to address Government policy priorities such as Leave Grants for non-ER posts, resolve Ministry and SOE payment arrears and legacy debt, as well as cover unfunded decisions and make provision for urgent and unavoidable expenditure.

Similar to the 2022 process, expenditure proposals above the ceiling will be considered through a New Program Proposal (NPP) process and prioritized should fiscal space be identified. Cash reserves will be used to meet any funding gaps.

The detail of the base case expenditure estimates is at **Attachment C**. The key elements are as follows.

- The departmental expenditure ceiling has been increased by **3 per cent** from the 2022 Budget to reflect the impact of inflationary pressures on operational costs, and to

ensure staff pay increments and establishment changes are met. The base case ceiling for departmental expenditure is **\$146.5 million**. Outyears are escalated by 3 per cent inflation.

- Grants, subsidies and other commitments have been reviewed and are broadly maintained at the 2022 level, except for an increase in international commitments related to a requirement to make a one-off subscription payment related to Kiribati's membership for the World Bank due in 2023, the increase in subsidy for Kiritimati Air services and the inclusion of the election cost, thus inflating outyears expenditure levels. The base case provision for this is **\$71.5 million**, a **10 per cent** increase on 2022.
- Debt servicing is held at the same level as 2022 in all years. It is proposed that there be no new debt agreed, and that proactive action be taken to reduce arrears and legacy debts.

Two options are proposed for projects that might be included in the LCDF:

- Option A (no policy change) would include allocations for continuing projects and COVID-19 response and recovery measures (including Copra Subsidy and SFU payments). A provision of **\$104.2 million**, 11 percent more than 2022.
- Option B (addressing pressures) would build on Option A and include additional allocations for addressing known fiscal pressures with a view to mitigating fiscal risks. This would include allocations for Government Manifesto commitments, addressing legacy arrears and debts, investment in the IFMIS and new Financial Supervisory Authority, the introduction of leave grants for non-ER posts, as well as provision for unfunded policy decisions and urgent and unavoidable payments. The total estimate for this option is **\$139.9 million**, **49 per cent** higher than 2022.

The total base case for expenditure depends on which option is chosen:

- Option A leads to total expenditure of **\$326.3 million**, **7 per cent (\$21.1 million)** higher than 2022.
- Option B has expenditure of **\$362 million**, **19 per cent higher (\$56.9 million)** than the 2022 Budget estimate.

## **Fiscal Balance**

The overall base case fiscal balance position will depend on the option chosen for the LCDF but both options lead to a deficit position. For both options, fiscal responsibility ratios continue to be met

Cash reserves as at 13 May 2022 were **\$175.9 million**, providing **6 months** of expenditure cover. This is significantly above the fiscal responsibility ratio target of three months cover.

With continued uncertainty in economic conditions, and the fiscal capacity inherent in the strong cash reserve balances, it is recommended that Government take the opportunity now to address legacy debts and repair SOE balance sheets to support their ongoing viability (Option B). This will improve overall fiscal resilience and support long run macro-economic stability.

The proposed deficit base case is consistent with providing some fiscal stimulus to support the COVID-19 recovery. The final size of the gap between revenues and expenditures will depend on Government decisions as part of the budget process.

### **Risks and Sensitivities**

The base case estimates rest on assumptions related to economic activity, expenditure and revenue, especially expected fishing revenues and donor direct budget support payments.

**Attachment D** provides the results of the sensitivity analysis, showing the impact on budget balance, cash reserves and cash reserve cover of changes in key assumptions related to revenue and expenditure.

A key result of the analysis indicates that if the fishing revenue estimate is 10 per cent higher than expected, the budget would return to surplus by 2025. In all other scenarios, the budget would remain in deficit. This suggests that more proactive action to mobilize revenues and reduce expenditures is required. The cash cover fiscal responsibility ratio is achieved in all scenarios.

Fishing revenues tend to be highly volatile, and there is a risk that they may under or over perform expectations. Tax revenue performance will reflect underlying economic conditions, and any policy changes through the year. Policy changes will need to be costed and considered in the context of the revenue impact. Risks will be mitigated by regular monitoring of collections and improvements to forecasting methodologies.

Donor support payments are conditional on meeting economic reform milestones, with an estimated \$17.4 million potentially at risk (5 per cent of total revenue). The reforms are targeted at mitigating fiscal risks and include reforms to public financial management, including improved reporting, expenditure management and a new IFMIS as well as revenue mobilization initiatives. They also encompass improved SOE management, building climate change resilience and supporting financial sector reform.

A further risk relates to the quality of expenditure, and the long-term sustainability of transfer payments, such as the Copra Subsidy and SFU payments. It is proposed to undertake more analysis to consider opportunities to improve the efficiency and effectiveness of transfer payments in meeting Government objectives. This may include options to target payments to those most in need, or alternative more efficient delivery mechanisms.

Lack of expenditure discipline or emerging fiscal pressures present another risk to the base case estimates. This risk can be mitigated by a rigorous 2023 Budget process that includes review of departmental expenditure to determine opportunities for reallocation.

The economic outlook assumption is also a risk, and foreign exchange volatility may also impact on the estimates. The healthy cash reserves buffer will support and manage these risks.

To mitigate the impact of all of these risks on the budget settings, it will be important to review and revisit assumptions as the budget process progresses.

## Attachment A: Aggregates and forward estimates

Item	2022 Budget \$	2023 Estimate \$	2024 Estimate \$	2025 Estimate \$	2026 Estimate \$
<b>Total Recurrent Revenue</b>	<b>305,178,279</b>	<b>325,305,157</b>	<b>335,002,413</b>	<b>345,062,457</b>	<b>355,449,458</b>
<b>Total Domestic Revenue</b>	<b>287,781,643</b>	<b>307,908,521</b>	<b>317,605,777</b>	<b>327,665,821</b>	<b>338,052,822</b>
Fisheries revenue	200,000,000	189,379,931	195,061,329	200,913,169	206,940,564
Taxation revenue	54,322,769	79,443,878	81,827,194	84,282,010	86,810,470
Investment revenue	5,000,000	6,405,480	6,597,645	6,795,574	6,999,441
RERF Dividend	23,000,000	26,593,532	27,851,338	29,218,749	30,652,338
Other Ministries Revenue	5,458,874	6,085,700	6,268,271	6,456,319	6,650,009
<b>Total donor budget support</b>	<b>17,396,636</b>	<b>17,396,636</b>	<b>17,396,636</b>	<b>17,396,636</b>	<b>17,396,636</b>
<b>Total Recurrent Expenditure</b>	<b>305,131,607</b>	<b>362,015,001</b>	<b>336,714,822</b>	<b>342,371,759</b>	<b>342,840,660</b>
Departmental Expenditure	142,589,796	146,458,771	149,365,891	152,353,527	155,400,924
Other Government expenditure	64,817,420	71,500,555	64,370,990	66,273,981	63,870,990
Debt servicing	4,090,104	4,090,104	4,055,383	4,021,693	3,946,188
Local Contribution to Development Fund	93,634,287	139,965,571	118,922,558	119,722,558	119,622,558
<i>Copra Subsidy</i>	40,000,000	45,000,000	45,000,000	45,000,000	45,000,000
<i>Unemployment Benefit</i>	32,400,000	32,400,000	32,400,000	32,400,000	32,400,000
<i>Other Projects and Grants</i>	21,234,287	62,565,571	41,522,558	42,322,558	42,222,558
<b>Recurrent Balance</b>	<b>46,672</b>	<b>(36,709,844)</b>	<b>(1,712,409)</b>	<b>2,690,698</b>	<b>12,608,799</b>
<b>% of GDP</b>	<b>0%</b>	<b>-12%</b>	<b>-1%</b>	<b>1%</b>	<b>4%</b>
Cash Reserves	166,983,422	175,962,363	174,249,954	176,940,651	189,549,450
FRR: Dept Exp as % of total (<50%)	47%	40%	44%	44%	45%
FRR: Cash reserves in exp months ( 3 months)	7	6	6	6	7
Expenditure as share of GDP	104%	116%	103%	100%	96%
Departmental Expenditure as share of GDP	48%	47%	46%	45%	44%
Tax revenue as share of GDP	18%	26%	25%	25%	24%

## Attachment B: Revenue

REVENUE	2019 Actual \$	2020 Actual \$	2021 Budget \$	2021 Actual \$	Share of Bud %	2022 Budget \$	2022 Revised \$	2023 Proposed \$	Chg on 2022 B %
<b>Tax Revenue</b>									
Personal income tax	12,788,846	12,364,642	10,713,584	13,554,961	127%	12,500,000	12,500,000	14,659,691	17%
Company tax	8,703,249	9,702,665	12,052,782	12,693,142	105%	12,452,782	12,452,782	16,259,915	31%
Excise tax	7,799,943	8,619,710	8,369,987	10,687,165	128%	8,369,987	8,369,987	13,016,967	56%
VAT	20,148,628	20,962,001	18,860,371	28,417,211	151%	21,000,000	21,000,000	35,507,306	69%
<b>Total Tax revenue</b>	<b>49,440,666</b>	<b>51,649,018</b>	<b>49,996,724</b>	<b>65,352,479</b>	<b>131%</b>	<b>54,322,769</b>	<b>54,322,769</b>	<b>79,443,878</b>	<b>46%</b>
<b>Non Tax Revenue</b>									
Fishing licence revenue	210,641,961	170,736,450	160,000,000	161,057,420	101%	193,067,000	193,067,000	180,811,944	-6%
Fish transshipment fees	14,504,567	12,004,312	4,500,000	7,481,672	166%	6,000,000	6,000,000	8,091,428	35%
Other Fishing Revenue	1,160,700	1,328,052	996,000	440,647	44%	933,000	933,000	476,559	-49%
<b>Total Fishing Revenue</b>	<b>226,307,228</b>	<b>184,068,815</b>	<b>165,496,000</b>	<b>168,979,738</b>	<b>102%</b>	<b>200,000,000</b>	<b>200,000,000</b>	<b>189,379,931</b>	<b>-5%</b>
Dividends	2,082,002	539,833	3,500,000	4,535,812	130%	3,500,000	3,500,000	4,905,480	40%
Interest Income	212,375	1,212,407	1,500,000	9,996	1%	1,500,000	1,500,000	1,500,000	0%
RERF dividend			40,000,000	40,000,000	100%	23,000,000	23,000,000	26,593,532	16%
<b>Investment Revenue</b>	<b>2,294,377</b>	<b>1,752,240</b>	<b>45,000,000</b>	<b>44,545,808</b>	<b>99%</b>	<b>28,000,000</b>	<b>28,000,000</b>	<b>32,999,013</b>	<b>18%</b>
<b>Other revenue</b>	<b>6,715,951</b>	<b>4,391,942</b>	<b>5,007,953</b>	<b>6,166,740</b>	<b>123%</b>	<b>5,458,874</b>	<b>5,458,874</b>	<b>6,085,700</b>	<b>11%</b>
<b>Total Non-Tax Revenue</b>	<b>235,317,556</b>	<b>190,212,996</b>	<b>215,503,953</b>	<b>219,692,286</b>	<b>102%</b>	<b>233,458,874</b>	<b>233,458,874</b>	<b>228,464,643</b>	<b>-2%</b>
<b>Total own source revenue</b>	<b>284,758,222</b>	<b>241,862,015</b>	<b>265,500,678</b>	<b>285,044,765</b>	<b>107%</b>	<b>287,781,643</b>	<b>287,781,643</b>	<b>307,908,521</b>	<b>7%</b>
World Bank			6,849,315	6,849,315	100%	6,849,315	6,849,315	6,849,315	0%
ADB			-	-		3,424,658	3,424,658	3,424,658	0%
NZMFAT		2,500,000	2,500,000	2,500,000	100%	2,500,000	2,500,000	2,500,000	0%
AusDFAT	499,995	500,000	1,000,000	1,000,000	100%	1,000,000	1,000,000	1,000,000	0%
EU		4,008,305	3,622,663	-	0%	3,622,663	3,622,663	3,622,663	0%
<b>Total Budget Support</b>	<b>499,995</b>	<b>7,008,305</b>	<b>13,971,978</b>	<b>10,349,315</b>	<b>74%</b>	<b>17,396,636</b>	<b>17,396,636</b>	<b>17,396,636</b>	<b>0%</b>
<b>Total Revenue</b>	<b>285,258,217</b>	<b>248,870,320</b>	<b>279,472,656</b>	<b>295,394,080</b>	<b>106%</b>	<b>305,178,279</b>	<b>305,178,279</b>	<b>325,305,157</b>	<b>7%</b>

## Attachment C: Expenditure

EXPENDITURE	2020 Actual \$	2021 Revised \$	2021 P Actual \$	Share of Bud %	2022 Budget \$	2023 (A) No NPPs \$	2023 (B) Priority NPPs \$	(A) Chg on 2022 %	B) Chg on 2022 %
PE	...	101,033,815	97,358,854	96%	103,433,712	105,932,224	105,932,224	2%	2%
Operating Costs	...	37,633,050	38,447,787	102%	39,156,084	40,526,547	40,526,547	4%	4%
<b>Departmental expenditure</b>	<b>115,432,195</b>	<b>138,666,865</b>	<b>135,806,640</b>	<b>98%</b>	<b>142,589,796</b>	<b>146,458,771</b>	<b>146,458,771</b>	3%	3%
<b>Other government expenditure</b>	<b>56,349,746</b>	<b>113,750,220</b>	<b>105,337,286</b>	<b>93%</b>	<b>64,817,420</b>	<b>71,500,555</b>	<b>71,500,555</b>	10%	10%
<b>Debt Servicing</b>	<b>3,409,452</b>	<b>3,681,768</b>	<b>3,520,588</b>	<b>96%</b>	<b>4,090,104</b>	<b>4,090,104</b>	<b>4,090,104</b>	0%	0%
<b>Local contribution to Development Fund</b>	<b>63,939,191</b>	<b>48,790,748</b>	<b>45,703,041</b>	<b>94%</b>	<b>93,634,287</b>	<b>104,212,519</b>	<b>139,965,571</b>	11%	49%
<i>Copra Subsidy</i>	...	...	...	...	40,000,000	45,000,000	45,000,000	13%	13%
<i>Employment benefit</i>	...	...	...	...	32,400,000	32,400,000	32,400,000	0%	0%
<i>Manifesto commitments (leave grant)</i>	...	...	...	...	-	-	20,000,000	0%	0%
<i>Arrears resolution</i>	...	...	...	...	-	-	10,000,000	0%	0%
<i>New Financial Sector Supervisor</i>	...	...	...	...	-	-	1,000,000	0%	0%
<i>IFMIS</i>	...	...	...	...	-	-	1,500,000	0%	0%
<i>Provision for unfunded decisions</i>	...	...	...	...	-	-	3,253,052	0%	0%
<b>Total Expenditure</b>	<b>239,130,584</b>	<b>304,889,601</b>	<b>290,367,555</b>	<b>95%</b>	<b>305,131,607</b>	<b>326,261,949</b>	<b>362,015,001</b>	7%	19%
<b>Total Revenue</b>	<b>248,870,320</b>	<b>279,472,656</b>	<b>295,394,080</b>	<b>106%</b>	<b>305,178,279</b>	<b>325,305,157</b>	<b>325,305,157</b>	7%	7%
<b>Balance</b>	<b>9,739,736</b>	<b>(25,416,946)</b>	<b>5,026,525</b>	<b>-20%</b>	<b>46,672</b>	<b>(956,792)</b>	<b>(36,709,844)</b>	>100%	>100%
<i>Balance as share of GDP</i>	4%	-9%	2%		0%	0%	-12%		
<i>Expenditure as share of GDP</i>	91%	110%	105%		104%	105%	116%	(56,883,394)	
<i>FRR1: Dept Exp as share of total (&lt;50% target)</i>	48%	45%	47%		47%	45%	40%		
<i>FRR2: Months of expenditure cover (3 m target)</i>	13	7	7		7	6	6		
<i>Cash reserves estimate (13/5/22)</i>	251,230,806	184,744,357	166,983,422		166,983,422	175,962,363	175,962,363		
Note reserves estimate for 2023 is based on estimate at 13 May 2022 adjusted for 2022 balance									

## Appendix D: Sensitivity Analysis

Item	2022 Budget \$	2023 Estimate \$	2024 Estimate \$	2025 Estimate \$	2026 Estimate \$
<b>Sensitivity Analysis - impact on balance/reserves</b>					
<b>A1 Low case Fisheries revenue (10% less) balance impact</b>	(19,953,328)	(55,647,837)	(21,218,542)	(17,400,619)	(8,085,258)
Cash reserve estimate impact	147,030,094	120,314,526	153,031,411	159,540,032	181,464,192
Cash reserve months	6	4	5	6	6
<b>A2 High case Fisheries revenue (10% more) balance impact</b>	20,046,672	(17,771,851)	17,793,724	22,782,015	33,302,855
Cash reserve estimate impact	187,030,094	158,190,513	192,043,677	199,722,666	222,852,305
Cash reserve months	7	5	7	7	8
<b>B No Donor Budget Support balance impact</b>	(17,349,964)	(54,106,480)	(19,109,045)	(14,705,938)	(4,787,837)
Cash reserve estimate impact	149,633,458	121,855,883	155,140,908	162,234,713	184,761,613
Cash reserve months	6	4	6	6	6
<b>C No RERF Dividend (return &lt; 5%) balance impact</b>	(22,953,328)	(63,303,376)	(29,563,748)	(26,528,051)	(18,043,540)
Cash reserve estimate impact	144,030,094	112,658,987	144,686,206	150,412,600	171,505,911
Cash reserve months	6	4	5	5	6
<b>D Expenditure 5% higher balance impact</b>	(15,209,908)	(54,810,594)	(18,548,150)	(14,427,890)	(4,533,234)
Cash reserve estimate impact	151,773,514	121,151,769	155,701,803	162,512,761	185,016,216
Cash reserve months	6	4	6	6	6
<b>E Copra Subsidy reduced by 50% balance impact</b>	20,046,672	(14,209,844)	20,787,591	25,190,698	35,108,799
Cash reserve estimate impact	187,030,094	161,752,519	195,037,544	202,131,349	224,658,249
Cash reserve months	7	5	7	7	8
<b>F SFU recipients reduced by 50% balance impact</b>	16,246,672	(20,509,844)	14,487,591	18,890,698	28,808,799
Cash reserve estimate impact	183,230,094	155,452,519	188,737,544	195,831,349	218,358,249
Cash reserve months	7	5	7	7	8
Rate of growth in expenditure	0%	19%	-7%	2%	0%
Rate of growth in revenue	9%	7%	3%	3%	3%

The budget estimates rest on assumptions related to economic activity, expenditure and revenue, especially expected fishing revenues, donor direct budget support payments, RERF returns and expected dividends, as well as the maintenance of expenditure restraint.

The table above includes estimates on the impact on the overall balance for scenarios, where the underlying assumption may not hold. The impact is shown of a change in the assumption on the overall balance, cash reserves estimate, and the amount of cash reserve expenditure cover.

A key result of the analysis indicates that if the fishing revenue estimate is 10 per cent higher than expected, the budget would return to surplus by 2025. In all other scenarios, the budget would remain in deficit. This suggests that more proactive action to mobilise revenues and reduce expenditures is required. The cash cover fiscal responsibility ratio is achieved in all scenarios.

This sensitivity analysis of assumptions includes the following scenarios:

- A. Fishing revenue:
  - A1 low case: Fishing revenues are 10 per cent lower than expected. The impact is that revenue decreases and the overall position deteriorates.
  - A2 high case: Fishing revenues are 10 per cent higher than expected. The impact is that revenue increases and the overall position improves, moving into surplus in 2025.
- B. No Donor Budget Support: Donors do not pay budget support, due to non-achievement of economic reform milestones. The impact is that revenue decreases and the overall position deteriorates.
- C. No RERF Dividend: rates of return on RERF do not exceed the 5 per cent benchmark for withdrawal of a dividend, as outlined in the RERF Withdrawal Policy. Therefore, no dividend can be drawn down. The impact is that revenue decreases and the overall position deteriorates. Expenditure on RERF projects is expected to occur, reflecting that an appropriation was approved.
- D. Expenditure high case: expenditure exceeds the forward estimates by 5 per cent. The impact is that expenditure is increased and the overall position deteriorates.
- E. Copra Subsidy reduction: the Copra Subsidy is reduced from \$4 a kilo to \$2 a kilo. The impact is that expenditure on the measure is reduced, and the overall position improved.
- F. Support for the Unemployed: the number of recipients of the payment is reduced by half from 53,000 to 26,500. The impact is that expenditure on the measure is reduced and the overall position improved.

Cash reserves are assumed to be available to cover the volatility in the balance. The capacity to do this is assessed using an estimate of how many months expenditure the reserves are able to cover. In nearly all scenarios the fiscal responsibility ratio of three months reserve cover is met. The only exception relates to the Scenario C in 2026.