

# **BUDGET PRESENTATION 2004/05**

*on*

*Thursday, April 15, 2004*

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## **A: INTRODUCTION**

1. All budget presentations important. This is my eleventh and has special significance for a host of reasons.
2. Was a very difficult calendar and fiscal year.
3. Gratitude to
  - (a) Family/Friends
  - (b) Ministers of State
  - (c) Constituents/Region III
4. Place on record gratitude to Financial Secretary, all the Deputy Financial Secretaries and Technical Staff at the Ministry, Governor, Deputy Governors and staff of the BOJ, Director Generals STATIN and PIOJ, Executive Director of the FSC and all members of the Revenue Agencies.
5. Have tabled wide array of data sets – equivalent in range, quality and timeliness to that available anywhere else in the world. Once certain standards have been established must be maintained or exceeded. As such, analysts and creditors at home and abroad watch expectantly each month for data on inflation movements, interest rates, as well as the level of subscription to Government issues.
6. There is room for improvement but I am proud of our officers.
7. These results impact on (a) interest rates and (b) whether or not debt issues subscribed. Expenditure financed by revenues plus loans but of vital importance - loans at what cost.
8. We have tabled enough information to provide the basis for informed discussion on all aspects of the economy and the society. The availability of these data sets allows for a significant change in my

presentation this year. It is necessary to review last year and to present, as we usually do, the macro-economic targets for the medium-term. However, focus will be on the fiscal targets and concrete steps being taken to expand the economic output.

## **B: YEAR IN REVIEW**

1. Whilst the Budget Debate is about the planned expenditure for fiscal year 2004/2005 and the way in which this would be funded, much of the issues which arose in reviewing fiscal year 2003/2004 had their genesis before.
2. As such in discussing the period it is useful to look at the challenges and set backs, as well as the successes/achievements for the 15 month period – January 03 to March 04.
3. The first six months of the calendar year i.e. Q4 of 02/03 and Q1 of 03/04 “difficult”, to put it euphemistically. The first signs of wider than projected fiscal deficit had emerged and difficulties emerged both domestically and externally which made economic management challenging.
4. Period started with uncertainty related to a possible war in Iraq. In February of 03, we were forced to purchase FE from the NIR to pay down a Euro bond which had matured thus simultaneously diminishing the NIR and raising questions about the ability to maintain a stable exchange rate system.
5. These uncertainties fed on themselves, leading to intense instability in the FE market and devaluation where the exchange rate bottomed out at J\$70 to (US)\$1.
6. The Administration took action, involving intervention, a significant hike in interest rate and an offer of unlimited indexed bond which restored order to the system. The rate has remained at about the same level (just of J\$60:US\$1) since that intervention.
7. This side of the House was intrigued by the fact that during a recent debate, Opposition Spokesman on Justice opined that, the intervention to stabilize and reverse the deterioration in the FE market was ill advised.
8. The size and range of goods and services affected by the tax package also contributed to the difficulties in the first half of the calendar

year. Several changes/adjustments were made and the delays in finalizing the set of measures itself contributed to the uncertainty.

9. In any event any tax package equivalent to 3.5% of GDP must have severe impact on the population as disposable income would have been reduced.
10. The combination of devaluation and the tax package led to movements in the CPI not seen in over seven years.
11. Externally, downgrade of our bonds by the rating agencies increased the difficulty in accessing resources externally, thus forcing almost total reliance on domestic financing.
12. The inevitable results were of higher interest rates and the need to increase short-term issues. Managing in that scenario posed extreme challenges.
13. **Successes/Positives:** Despite all the above challenges, as significant as they were, simultaneously there were significant positives in the real economy. We will focus on three - agriculture, bauxite alumina and tourism.
14. **Agriculture:** Rebounded – six major natural shocks (floods and drought) between 1999 and 2003. Grew by 5.7% in 2003.
15. **Bauxite/Alumina:** During calendar 2003, the bauxite alumina sector was operating at close to maximum capacity and demand on the world market for alumina pushed prices beyond original projection.
16. **Tourism:** The tourism sector had perhaps its greatest year ever with records being established in long-term visitors, cruise ship passengers as well as total visitor expenditure. The recovery of the industry had not only positive results in terms of the viability of properties but also contributed to greater stability in the foreign exchange market and improvement in the balance of payments.
17. The growth in these sectors of the real economy, were major contributors to the overall economic performance. Perhaps more importantly, these were not one-off occurrences. They were simply

laying the basis for the growth in the medium-term about which I will have more to say.

18. With the improvements in the real economy we turned our attention in Q3 to restoring confidence in the country on the part of external creditors, particularly those in Europe. This was achieved initially through tele-conferences, but finally by a major tour through the financial capitals of Europe.
19. We discovered to our surprise that here was widespread confidence in Jamaica's economic future but creditors, both past and prospective, felt that we had tended to neglect Europe focusing too much on North America. It is an error we will not repeat.
20. The positive response in Europe was occurring in spite of the impact of the difficulties in Argentina on creditors in Europe. Useful to elaborate on this point.
21. The fact is that whilst in North America most of the bonds issued by a country such as Jamaica are purchased by institutions, in many European countries e.g. Italy and Germany, the purchasers are individuals, oft times, pensioners who buy and hold. As such when one utilizes part of one's pension to purchase an Argentine bond and down the road when that bond matures, there is no payment forthcoming, this translates not simply into a lower profit margin for a financial institution, but into financial melt down of individuals and families.
22. There are two critical lessons here for Jamaica. The first is that despite the cost, the decision to intervene through FINSAC and protect savers, holders of insurance policies and pension funds was the correct one. The second lesson is that our history of never renegeing on our debt obligations, regardless of the fiscal pressures has helped us to establish a niche in the external capital market.
23. People who buy our bonds know that when the time comes for us to repay we will. It differentiates us from many other countries and lays the basis for us to confound critics and the analysts with the successful Euro issue in February.

24. That successful Euro issue of €200 million (approximately (US)\$250 million following the (US)\$100 million loan obtained from BNS in December simultaneously reflected a change in market perception and confidence and impacted on both positively. Everything is indeed everything.
25. The additional resources have helped to accelerate the downward movement in interest rates domestically and have provided the Central Bank with resources to further stabilize the foreign exchange market.
26. Hence, for the first three months of 2004 (Q4 of 03/04) there has been a “gelling” of positive outcomes which have re-enforced each other. There was the performance in tourism, mining and agriculture. There is stability in the FE market, there was a reduction in domestic interest rates and perhaps most critical, there has been very good fiscal performance.

## C: THE FISCAL

1. The members of this House and the general public may wonder why the Administration has placed so much emphasis on the attaining of fiscal targets for 03/04 and indeed for the medium-term. The Prime Minister and I have, on several occasions, reiterated that the target of eliminating the fiscal deficit during fiscal year 05/06 remains and will be met.
2. To achieve this target, the critical element is to attain a primary surplus of the order of 12% and above, over a three-year period. In my last meeting with the former Managing Director of the IMF, Mr Köhler, now the German President, he questioned the feasibility of our attaining our fiscal targets as he felt it would not be possible for a country to achieve them and maintain social stability.
3. Many others felt like he did and many analysts confidently asserted that we had no option but to go the route of Argentina and re-structure our debt.
4. The only question, they argued, was whether we would seek to work with our creditors or do it unilaterally. I told Mr Köhler and all other creditors – Jamaica will honour its debt obligations.
5. Whilst attainment of the targeted primary surplus is indeed difficult, the plain fact is that short of some country either writing off significant debt or giving us significant grants, we have no option but to eliminate the fiscal deficit in our quest to bring down interest rates. There is no option.
6. There were times during the fiscal year when both the level of revenues collected as well as the level of expenditure occasioned by the higher than projected interest payments caused concern amongst our creditors about the fiscal targets.
7. In fact, in December 2003, my presentation to members of the Trade union leadership showed that unless there were tight management of the budget we could be headed for a deficit equivalent of 10% of GDP in 2003/04 and a worsening situation

thereafter. This was the document which got into the hands of the Leader of the Opposition and which he gave great publicity, locally and internationally.

8. At that stage we felt it necessary to provide to the public a revised projection of the expected deficit. We announced that rather than the target of 5%-6% of GDP, we expected to end the fiscal year with a deficit of 6.9% of GDP. Whilst this represented a missing of the original target, it was significantly different from Mr Seaga's 10% of GDP.
9. That projection of 10% of GDP sent shivers through the market and forced us to redouble our efforts. Everyone should be judged in terms of what is expected of them and what the final outturn is. The budget as presented last year projected revenues of \$147 billion the outturn was \$151.4 billion. The budget of last year projected expenditure of \$171.4 billion, the outturn was \$179.6 billion. Simply translated we spent \$8.2 billion more than projected.
10. However, domestic interest costs were \$11 billion more than we had budgeted for. Put another way, had domestic interest rates not been raised because of the problems which I have outlined above, our expenditure levels would have been on target. Furthermore, we could have used the additional amount spent on interest to deal with the capital projects and clear outstanding obligations.
11. But back to the fiscal numbers. The fiscal deficit for fiscal year 2003/04 in dollar terms was \$28.2 billion. This converts to a fiscal deficit as a percentage of GDP of 5.8%. We have made the target of a deficit of 5-6% of GDP.
12. There is a clear message for our creditors at home and abroad. Judge us in terms of our performance and we expect that the reward will be lower interest rates thus allowing us to dedicate more sums to address the social and economic needs of our people.
13. I now turn to an issue concerning the fiscal accounts which arose during the discussions at the Standing Finance Committee on the way in which expenditure for fiscal year 2003/2004 was financed.

The Opposition Spokesman on Justice asked about “advances” made by the Central Bank to Central Government, specifically during December 2003.

14. The specific answer to his question is that the Bank of Jamaica made no “advances” to the Central Government in December 2003 or at any time during FY 03/04. In fact, the last time that the BOJ made any such advance to the Central Government was in 1992.
15. The question posed is so important that it is imperative that we place firmly on the record of the House the facts about the financial relationship between the Bank of Jamaica and the Central Government. I have indicated that the last time advances were made by the BOJ to the Central Government was in 1992.
16. Up until 1992 the BOJ acted as banker to the Central Government with Central Government’s revenue and expenditure accounts maintained in the Bank of Jamaica.
17. As the Government’s banker, the BOJ provided advances to the Central Government when resources were inadequate to cover expenditure.
18. Ministries and departments could draw cheques on their Expenditure Clearing Accounts held at the BOJ, as the central Bank would honour those cheques regardless of whether there were adequate resources in the accounts.
19. This resulted in large amount of funds leaving the Central Bank to fund Central Government expenditure, financed by “advances” from the Central Bank to Central Government. The law required that such advances be cleared within three months of the end of the fiscal year, from the revenues.
20. The reality was that these overdrafts were carried forward from year to year, not only contributing to inflation but also creating a situation which impaired the balance sheet of the BOJ.
21. In 1992 the Government took the decision to control the build up of advances to Central Government by the BOJ and, as a first step,

a decision was taken to establish banking relationships with the commercial banks. However, the Consolidated Fund, the Debt Accounts and some revenue accounts were still maintained at the Central Bank.

22. Since 1992 there have been no advances from the BOJ to Central Government. From time to time, the BOJ invests in GOJ's instruments on commercial terms similar to those offered to any other institution or retail investor. These instruments, carrying market interest rates, are freely tradable securities and are used by the BOJ in its conduct of monetary policy. The securities are either sold outright by the BOJ or used to back the Bank's reverse repos.
23. The maintenance of the Consolidated Fund in the BOJ still posed challenges for liquidity management. Consequently in 1998 Consolidated Fund accounts were opened in the commercial banking sector.
24. In February 2003 when it became apparent that we would not be able to raise funds on the external capital market and there was the need to repay a bond issue of €200 million, the Central Bank paid the debt from the NIR. In turn the BOJ was compensated by the Government with LRS' at prevailing market interest rates.
25. Over the course of the financial year 2003/2004, the GOJ paid to the BOJ \$7.55 billion in principal and \$6.4 billion in net interest for its holdings of GOJ securities. At the same time, the BOJ's investments in GOJ securities totalled \$18.47 billion.
26. I sincerely hope that this clarifies the financial relationship between the Central Bank and the Central Government.

## **D: MEDIUM TERM**

1. Normally, what is presented here are the major macro-economic projections for the medium-term. The comparison of the targets established for fiscal year 03/04 against the actual outturn as at March 31, 2004 is instructive. GDP growth at 2.1% was within the range, the NIR was significantly above the target. The primary surplus, as a percentage of GDP was on target and the deficit was within the range of 5%-6% of GDP. Our only deviation in terms of macro-economic target was in terms of the inflation result.
2. This year as has been done for the past several years, the outline for the next three years will be presented but first we need to spend some time on what I consider the most significant development which will impact on the medium-term - the signing of a Memorandum of Understanding between the Government of Jamaica and the major trade unions representing public sector workers.
3. It is useful for us to indicate the path leading to this historic development. Last year in the month of November, I decided to have a series of exchanges with critical partners to indicate the present state of the economy and the prospects for the future. The meeting with the trade union leadership was by far the most productive as their first request was for full information prior to any decision on the way forward.
4. We responded to their request for information indicating several important aspects about the fiscal, including the increasing percentage taken up by interest payments, and wages and salaries. Furthermore, we demonstrated that wages and salaries, in real terms, had improved compared to inflation, as a percentage of total expenditure and even in US dollar terms.
5. The presentation also indicated that unless we were able to obtain some understanding, the prospects were for the deficit to grow. Given that this was untenable, the only option which the Government would have at that stage would be for severe cuts in employment.

6. The sensible option which was expressed by both sides would be to find a way to protect employment and simultaneously curb the rate of growth of wages and salaries. Furthermore, there was an acceptance that there had to be adjustments within the public sector to bring about greater efficiency levels.
7. We worked throughout the Christmas period and through January leading to the historic signing on Monday, February 16. Subsequently, the MOU has been signed by the JTA and we confidently expect that within the near future the other unions and groupings representing public sector workers will be on board.
8. Three final comments are in order. The first is that the maturity demonstrated by the leadership of these unions must be publicly recognized. Whilst all the leadership contributed, Senator Dwight Nelson has been the critical factor in guiding the process and he and his colleagues must be saluted.
9. The second is that whilst we will have hic-cups from time to time, all of us who signed the MOU are committed to ensuring its success. Furthermore, we are convinced that it has laid the basis for a new era in the socio-economic architecture of this country.
10. The third point to be made is that this historic agreement has given credibility to the Government's fiscal targets not only for fiscal year 2004/05 but also for 2005/06 when we plan to eliminate the deficit.
11. In terms of the macro-economic targets for 2004/05, we project inflation of 9%, GDP growth of 2.5%, NIR as at March 31, 2005 of (US)\$1.3 billion, a primary surplus of 13.7% of GDP and a deficit of between 3% and 4% of GDP.
12. The achievements of the last fiscal year gave creditability to these targets and should provide creditors with the assurance that our target of eliminating the deficit in the next fiscal year 2005/06 will be met.

### Social Targets

13. Whilst I have stressed the absolute necessity of meeting the fiscal targets, let me hasten to state that we do not view this target as an end in itself. Governments do not exist simply to meet fiscal targets. Governments are elected to respond to the needs of the people and so our commitment to working to develop the human resources and to raise standards of living is in no way diminished by our commitment to make the fiscal targets.
14. Anyone who would try to posit the one against the other is engaged in a fool's game. There is a famous Politician/Statesman, who shall remain nameless, who introduced us to the phrase "it takes cash to care".
15. The reality is that for a very long time in the future we need to support expenditure in providing a Social Safety Net and investing in the social services by being able to convince creditors, domestic and foreign, that the money they lend to us will be repaid. Simply put, we can only increase the investments in the social services if we demonstrate, not by words, but by deeds, that we will be careful in managing the resources at our disposal and that we will pay our debts. In other words, attainment of the fiscal targets is not an enemy of the social targets but is a needed platform on which our social objectives will be met.
16. In terms of this social objective we have worked with our international development partners in producing a medium-term socio-economic policy framework anchored on the macro-economic targets. This document, in addition to demonstrating the usual macro-economic targets also articulates the development objectives, the priorities and strategies for the social sectors.
17. The draft document will be put out for public scrutiny to allow for a full round of consultations and once endorsed by Cabinet, it will be available to monitor performance against targets.
18. This development represents a continuation of our effort to ensure that our performance is monitored against the targets which have

been established, not only in the economic sectors but in the social sectors.

### Debt

19. The issue of the debt has been the focus of much discussion/deliberation over many years. It is a fact that both the stock of debt and the debt to GDP ratio are not in a situation where we can be comfortable. However, whilst agreeing on this point, there are some simplistic derivations which need to be dismissed.
20. The first is that one cannot condemn the level of indebtedness and at the same time seek to demand additional expenditure in virtually every area.
21. The second point is that debt is not a bad thing in itself. When people take mortgages to purchase a home - that is regarded as a positive. Similarly, a student who borrows from the SLB or from a bank to invest in higher education has incurred debt in order to increase his/her value added; that is good debt. For those who rail against the debt and demand that we should borrow no more, the obvious question is - what programmes, what projects or which employees would be sacrificed. No developing country which has aspirations for improving human development or providing citizens with improved physical infrastructure can do so solely on the basis of tax revenues.
22. The critical mix is to ensure that expenditure levels do not depart so significantly from revenues that your creditors become skittish.
23. Therefore, even as we seek to slow the rate of growth of the debt stock, we cannot have it all ways. We cannot demand greater expenditure, less taxation and less debt.

### Energy Cost

24. One major factor which can impact on the medium-term, over which we have virtually no control, is the cost of oil.
25. This matter has for reasons which we all know, and both major political parties can take equal blame in this matter, has not to date benefited from rational discourse.

26. Jamaica has gasoline prices which rival the lowest in the region even when we produce not one gallon. Whilst the price of gasoline is often seen in terms of the additional revenue brought to the Consolidated Fund through taxes, there is an even more threatening implication. It relates to the impact on the balance of payments. The original forecast for the country's balance of payment for the fiscal year 2004/05 assumed an average oil price of (US)\$30 per barrel which would give us an oil bill of just under (US)\$850 million and a current account deficit of (US)\$885 million – approximately 10% of GDP.
27. If oil prices average (US)\$33.40 per barrel for the year, this would lead to oil imports costing an additional (US)\$69 million which would move the Current Account deficit to (US)\$950 million – approximately 10.6% of GDP.
28. If OPEC decides to reduce supplies and crude oil prices average (US)\$35 per barrel for the fiscal year, the fuel bill could climb to over (US)\$950 million – (US)\$110 million above the original forecast and the Current Account deficit could move to 11% of GDP.
29. I have put this information out as there is need for the country, beginning with the members of this Honourable House, to initiate serious dialogue on our energy bill. Whilst conservation measures must be promoted, the reality is that these will not be enough to address the difficulty which I have outlined.
30. Neither tourism, nor bauxite, nor any other export sector can grow at a rate to compensate for the possible increases in our import bill which I have outlined.
31. From time to time I receive letters from ordinary Jamaicans which contain gems of wisdom. A few months ago I received one such letter which posited the dilemma we face in a very pragmatic, down to earth way. The writer indicated that whilst Jamaica produces not one gallon of oil there have been and can always have the possibility of riots if we sought to move the price of a litre of gasoline up by any margin.

32. At the same time, Jamaica which produces all the water it could ever need, imports bottled water from diverse sources.
33. Compare the prices of a litre of bottled water and a litre of gasoline.
34. Mr Prime Minister, if there is one issue which could totally derail our b.o.p. position in the medium term, it is the cost of imported energy. This question provides the members of the House the opportunity to work jointly on a realistic energy policy which take cognizance of the potential damage of a sharp price movement on every aspect of national life.

## **E: ECONOMIC EXPANSION**

1. As I have indicated, this presentation focuses on two main issues. Firstly, the non-negotiable requirement that the fiscal targets are met and secondly, that the economy continues on its growth path at an accelerated rate.
2. It is to the second question that we now turn. Last year - calendar and fiscal - two critical sectors – tourism and bauxite/alumina performed at levels which provided the basis for the recovery in the real economy.
3. What is more exciting is that these are not one-off occurrences as the investment plans for the medium-term suggest that these sectors will reach unprecedented levels in our history in the medium-term. Furthermore, the increased economic activity is multi-sectoral, covering goods producing sectors, tourism as well as the IT sector.

### Tourism

4. In 2003, the number of stop-over arrivals was in excess of 1,350,000 – the highest number ever. Cruise ship arrivals reached 1,132,000 an increase of 31% over 2002. It was the first time that Jamaica had received over one million cruise ship passengers.
5. In the first two months of 2004 stop-over arrivals increased by just under 8% which is the target for the year and the projections are that we will have another year of strong growth.
6. During the course of this calendar year, at least 800 new hotel rooms will come on stream with the RIU hotel in Negril and Sandals Whitehouse providing the majority of those rooms.
7. Sandals Whitehouse, of which the Government is the majority owner, is the first major resort to be established on the South Coast and we confidently expect it to be a catalyst for future tourism development on that side of the island.
8. The new properties will generate in excess of 1,200 new jobs.

9. But this is only the beginning. Later this year construction will begin on four new hotel properties being developed by a Spanish hotel chains. They will be situated at Rose Hall in St James, Oyster Bay in Trelawny, Peartree Bay in St Ann and Mammee Bay also in St Ann.
10. Iberostar will be constructing 3 hotels with a total number of rooms of 950 at Rose Hall.
11. AM Resorts will be constructing 4 hotels with a total of 1,400 rooms at Oyster Bay. Grupo Pinero will be constructing 3 hotels with a total of 1,800 rooms at Peartree Bay and RIU will be constructing 3 hotels, a total of 850 rooms at Mammee Bay.
12. The total investment will be in the range of (US)\$550 to (US)\$600 million excluding the cost of land acquisition. Five thousand rooms will be constructed over a 5-year period.

#### Bauxite/Alumina

13. The Bauxite/alumina sector had strong performance last year with respect to alumina output, total bauxite production, foreign exchange earnings and new investments.
14. Alumina output reached 3.84 million tonnes, the highest ever by Jamaica. Bauxite production was 13.44 million tonnes, the second highest in our history and the highest in 29 years.
15. Gross foreign exchange earnings increased by 8.6% equaling (US)\$775 million.
16. Both JAMALCO and Alpart undertook expansions during the year with investments totaling (US)\$150 million. The JAMALCO expansion increased capacity by 250,000 tonnes and during the first half of this year, Alpart's expansion will lead to increased capacity of 150,000 tonnes.
17. This increase in capacity of 400,000 tonnes per annum will increase foreign exchange earnings by (US)\$80 million per annum.

18. In the first quarter of 2004, alumina production increased by 12.1% compared to the corresponding period for 2003 and bauxite output increased by 8.2%. Gross foreign exchange earnings are projected to increase by over 20% to approximately (US)\$950 million for 2004.
19. Responding to the prospects of robust growth in world demand, as well as Jamaica's improved competitive position, ALCOA has announced its plans to further expand the JAMALCO plant by 1.4 million tonnes.
20. This project will involve total capital investments of (US)\$690 million of which (US)\$300 million will be spent in Jamaica. Over 2,500 construction jobs will be created.
21. When completed this expansion will generate additional gross foreign exchange earnings of over (US)\$300 million per annum.
22. In our discussions with the Executives of ALCOA they have raised the question of whether the country will be able to provide the goods and services needed to ensure that the construction activity proceeds apace. Diverse business opportunities will arise including provision of food services, accommodation, transportation, banking services, equipment hireage, steel fabrication, engineering services.
23. This investment is a direct result of various steps which have been taken by the Government to foster macro-economic stability and to reform the fiscal arrangements of the industry to enhance competitiveness.
24. The landmark MOU between the bauxite companies, the trade unions and Government has helped to bring stability to the industrial relations in the sector.
25. An interesting bottleneck which could arise is the availability of enough skilled workers to meet the needs of the construction in bauxite/alumina and tourism, simultaneously.

26. Whilst we have identified the significant and firm programmes for expansion in the two traditional sectors, it is imperative that at each step we continue to foster new entrepreneurs whether they be involved in the established sectors or in new areas.
27. I now turn to two new initiatives being spearheaded by the EXIM Bank. The first relates to a new loan facility for the Information Communication and Technology (ICT) sector. EXIM will provide an \$80 million pool of funds to the sector for software development, receivables financing, working capital and the purchasing of capital equipment. The interest rate on these loans will be 12% per annum.
28. There are two components to the programme. There is a short-term working capital facility named YES – Young Entrepreneurial Scheme focusing on young and upcoming entrepreneurs in the sector who are either domiciled at the Technology Innovation Centre at the University of Technology or engaged in similar type businesses elsewhere in Jamaica.
29. Each borrower is initially eligible for a loan limit of \$½ a million but repeat borrowers may access additional financing but not exceeding an overall limit of \$1 million.
30. The second component is whereby the EXIM Bank has made a medium-term facility of \$60 million available, to established ICT companies registered and operating in Jamaica. Loan limit is \$15 million repayable over five years.
31. A second important programme which will be facilitated through EXIM Bank relates to the on-lending of approximately (US)\$8.4 million to exporters. The programme will be jointly executed by EXIM and the JEA.
32. The loans will be made to companies approved by the JEA, assessed as being capable of reaching agreed targets for exports, job creation and investment. Loans will only be provided to companies that are in good standing in terms of tax payments.

33. The loan ceiling will be a maximum of (US)\$300,000 per borrower and will be for a period of four years inclusive of a one year moratorium. The interest rate will be 7%.

#### DBJ

34. Mr Speaker, I wish to say something about the work of the DBJ, which falls under the aegis of the Ministry of Finance and Planning.
35. During the FY 03/04, the DBJ approved loans totaling (J)\$1,350 million and (US)\$27.7 million. Main sectors – Agriculture (J)\$263 million; Agro-industry (J)\$284 million; Manufacturing (J)\$445 million and Tourism (J)\$210 million and (US)\$27 million.
36. Approvals for manufacturing a most pleasant surprise. Hopefully, a clear sign of recovery.
37. DBJ not just for big farmers, manufacturers and hoteliers. During the year, the tillage service, done in collaboration with Ministry of Agriculture, RADA and the JAS was launched. Provides low-cost tillage services to small farmers.
38. A first tranche of \$10 million was made available to the JAS, through MINAG, to introduce a sustainable marketing facility for local produce.
39. The Cocoa Rehabilitation Project has so far been accessed by 200 cocoa farmers with a total acreage of 715 acres.

#### Sugar

40. Throughout history, countries are invariably faced with the rise, maturation and then decline of what were formally lead sectors in an economy. The situation is no different for Jamaica and in fact, one of the difficulties we face is that the economy of the year 2004 is significantly different from that which obtained in 1980, a mere 24 years ago.
41. Even whilst recognizing that in certain instances the decline of an industry is inevitable, there are some industries where it is possible, if correct decisions are taken – use of technological

advances, new production methodologies and better management systems - to restore what would seem to be an industry which was on death's bed.

42. Too often there is a tendency for pundits to speak of the inevitable decline or death of an industry but only rarely would these pundits indicate what should replace it. The sugar industry is one such sector.
43. Books have been written, many theses have been produced, speaking about the inevitable death of the industry in Jamaica. However, there are 29 members of this Honourable House who would face serious difficulties, were the industry to go under.
44. This industry cannot be pigeon-holed. It is agriculture, it is manufacturing. It employs those with minimal skills; it employs those with the highest level of technological and scientific training – engineers, chemists, computer experts.
45. Consider what Lionel Town would be like if Monymusk were closed. Or what would happen to Central and Western Westmoreland if Frome went under.
46. Jamaica cannot afford to write off the sugar industry and it is for that reason that the Government took the decision to invest significant amounts in the five State-owned factories. The positive results have begun to emerge.
47. To be accurate, some of these results have come from external occurrences over which we had no control, e.g. movement of the Euro vs the US dollar, but even if this occurred and there was no improvement in terms of production, those positive shocks would come to naught. The SCJ in this crop has produced by the end of March, 86,000 tonnes – approximately 12,000 tonnes more than at the same period last year. It has also recorded a 25% increase in cane yields per hectare and a 22% increase in hectares planted in canes.
48. Based on the performance through to the end of March, the company is confident it will achieve its production target for the

crop despite the serious problems resulting from illicit fires. To date such fires have resulted in losses amounting to approximately \$135 million.

49. Furthermore, it is projected that the five factories will, for the first time, make an operating profit this year, moving from an operating loss of over \$500 million last year.
50. But we recognize that in certain instances not all the lands owned by the estates are suitable for cane and we have begun a diversification project. The projects to be initiated this year include 150 hectares of papaya at Hampden, 50 hectares of vegetables and 40 hectares of cotton at Monymusk.
51. We all know that one of the less positive features about sugar production - a factor which has influenced reactions - relate to the poor living conditions of many of the workers in the sector. This Administration has sought, through innovative means, to improve housing conditions. Over 180 hectares of land have been set aside to provide housing solutions for employees.
52. An initiative about which we are particularly proud, is one undertaken at the St Thomas factory, where in collaboration with Food for the Poor, decent housing is being provided for 75 families. This will be a model community with individual housing units and with each family having assigned sanitary facility. It will also have in place a modern sewage disposal facility, roads, electricity and a recreational area.

#### Road Infrastructure

53. To complement the expansion in various areas of the economy, the Government has embarked on a programme of infrastructure development unprecedented in the country's history.
54. Segment I of the North Coast Highway has totally transformed the travel dynamics between Negril and Montego Bay. Segment II currently under construction will do the same for the Montego Bay to Ocho Rios journey.

55. As soon as certain contractual issues are resolved, work will begin on Segment III from Ocho Rios to Port Antonio. The development work on Segment II and III has been a major factor in influencing the decisions for the significant new investments in tourism in the parishes of St Ann and Trelawny.
56. To complement the development of the North Coast Highway is Highway 2000. The second section between Bushy Park and Mandela is scheduled to be completed and opened by October of this year. This will be followed by the section which will include a new Causeway and joined to the Mandela via the Dyke Road. The target date is to complete that section by December 2005.
57. The final section – Sandy Bay to Williamsfield – has a projected completion date of August 2008.

Water

58. In drive to put NWC on path to viability, have met with Minister and Chairman to examine financial situation.
59. NWC owes Ministry of Finance just under \$875 million. At the same time NWC is owed \$540 by various Government Departments and Ministries. Decision taken to set off the amount owed to the NWC, by the amount owed to Finance – leaving a balance of \$335 million.
60. This amount owed will be used to facilitate several water and sewerage projects.

## **F: FINANCING THE BUDGET**

1. First we need to summarize the budget which calls for an expenditure of \$328.2 billion. Recurrent expenditure is \$187.6 billion of which interest payments account for \$96.3 billion (51.3%). Capital expenditure is \$140.6 billion of which amortization accounts for \$132.16 billion (94%).
2. Debt servicing therefore accounts for \$228 billion. Put another way, of the total budget of \$328 billion, only \$100 billion is left to pay teachers, nurses, doctors, policemen, run the business of Government and do some projects.
3. Once again, we see the importance of trimming the deficit, reducing interest payments and providing us with the flexibility to do the things needed and demanded by the population.
4. In looking at the way to finance the budget this year, several factors had to be taken into consideration. The first is that we presented a major tax package last year and this was compounded by depreciation in the value of the currency. This impacted on inflation. As I have said on previous occasions, increased inflation is itself another tax package. Secondly, there is the reality of the MOU where workers in the public sector have committed themselves to “hold strain” for two years as their contribution to addressing the fiscal problem.
5. A third important point is that there is a Tax Policy Review Committee which was established a year ago under the chairmanship of Mr Joseph M Matalon. This committee comprises representatives of a broad cross section of interest groups, private sector, trade unions, the accounting profession and ordinary citizens. The work of that committee is being informed by technical analysis provided by a team from Georgia Tech led by Professor Roy Bahl, who carried out much the same work for the last comprehensive review of our tax system some 20 years ago.
6. I have been bombarded with proposals for adjustments to the tax system and we have taken the policy decision that, rather than

seeking to tinker at this stage of the game, all such proposals should be submitted to the Tax Policy Review Committee and will go into the mix which would inform the recommendations they submit in their final report in October.

7. One of these proposals for change has come from the PSOJ/JMA and it relates to the 2% Custom User Fee which was imposed last year. I need not review the circumstances which led to the imposition of this Custom User Fee (CUF). Suffice to say that after a rocky start, it has worked very well realizing revenues of just under \$4billion.
8. The proposal which has been advanced is partly based on the view that the CUF has not attained the objective of “punishing” those who operate outside of the tax net. Against that background it has been proposed that the present non-refundable 2% should be replaced by 2.5% charge which could be used as a credit against income tax obligations.
9. This proposal has certain attractive features but as I have indicated, I intend to refer it to the Tax Policy Review Committee such that the response would be incorporated in a total comprehensive assessment.
10. However, there are additional reasons why we would not seek to make the change at this time. The first is that the present system is working. Secondly, within the context of the MOU the Government cannot take a chance on moving the fee from 2% to 2.5%.
11. I have been assured by those who advocate the change that, in a competitive environment, those who intend to use the fee as a tax credit would have no incentive to increase their prices. Whilst I accept that the argument would hold for many, I could say with little fear of contradiction that there will be those who may be tempted to use the excuse of the increase in the “up-front” charge as an excuse for moving prices.
12. So my formal response to those who have proposed the change is to submit the proposal to the Tax Policy Review Committee.

### Property Taxes

13. Property taxes should cover costs of solid waste management and street lighting. Not possible at present. Must be raised.
14. However, still not satisfied that the system is at an acceptable level of efficiency. Not friendly to the willing taxpayer. Will give personal attention to moving it to the appropriate level.
15. Pay what you paid last year.
16. I have spoken earlier about the high cost of energy and the need to encourage conservation. My colleague, the Minister of Commerce, Science & Technology has raised with me the fact that the policy of taxing solar water heaters flies in the face of our commitment to energy conservation. I wish to announce that effective June 1, 2004 these taxes/duties will be changed as follows:
  - a. Caricom manufactured – no GCT/no duties;
  - b. Extra regional – no GCT – duties as per Caricom agreement.
17. Last year in our attempt to reduce the number of areas which were exempted from GCT, we applied it to health insurance premiums as is done in most countries with a VAT. A combination of interest groups including the providers of health insurance and the trade unions have protested.
18. We recognize the validity of these protests and so effective June 1, 2004, the GCT will no longer be applied to health insurance premiums. However, there is an important message to all concerned. There is need for greater efficiency both in terms of the firms, the doctors, and pharmacists in terms of the costs which are passed on to clients/patients.
19. Our decision to remove the GCT has a cost as it implies diminishing revenues. Now the ball is in the court of all other elements in the equation. The Government and the workers will be watching to see how these costs move and the justification provided.

20. We all know the size of the expenditure budget. Now let us turn to how it will be funded. We intend to borrow a total of \$153 billion that leaves a gap of \$175 billion. We expect to receive grants totaling \$4.3 billion, the bulk of which will come from the European Union. We project capital revenue at \$2.5 billion which is significantly less than the outturn for the last fiscal year where there were significant inflows due to divestment.
21. We project non tax revenue at \$10.2 billion of which a significant portion will come from the Custom User Fee, as well as approximately (US)\$6 million from the sale of the cellular licence to AT&T. We project \$155 billion as tax revenue. This represents an increase of 17% compared to the outturn of \$131 billion for 2003/04. For those who believe this is an optimistic projection, the increase FY 03/04 compared to FY 02/03 was 27.4%. Furthermore, this represents the average rate of increase for the last six fiscal years.
22. We project to collect this based on improvements in our administration as well as in terms of certain legislative amendments, to make the various tax collection machinery more efficient. Simply put, there will be no new taxes. There is no tax package.

## **G: CONCLUSION**

1. In my presentation this afternoon, I have provided details on how the expenditure budget which was tabled just over two weeks ago will be financed for fiscal year 2004/2005. As is obvious, this expenditure budget retains very strong controls in terms of fiscal constraints. But we have gone at lengths to indicate that unless we can hold fast our commitment to reduce and eliminate the fiscal deficit, the objective of reducing interest rates and promoting economic growth on a sustained basis, will remain out of reach.
2. Despite the tight year which we have experienced, there are very few persons either within this Honourable House or out of Jamaica who could have anticipated that we would have been in this position at this time, this year.
3. We are here with a dollar which has been stable for close unto a year. We are here with foreign reserves higher than they were a year ago. We are here with our external bond prices trading at levels, in certain instances, never before reached. We are here in a situation where there are several external financial institutions seeking to take us to the market.
4. But perhaps most important, we are here in a situation where in terms of ongoing investments and those which will be coming on stream within the year and within the medium-term, we are poised for a period of sustained economic expansion.
5. The projects are flowing from the pipeline and there are more still in the pipeline.
6. This has not come about overnight, or by chance. The fact is that this Administration over 15 years has taken certain strategic decisions aimed at fundamentally changing the economy. Some of these decisions involved short-term adjustments, whereby we abolished price controls and liberalized various aspects of the economy. Some of the results of these changes had negative impact but they had to be done.

7. There was a second set of changes which are much more subtle and hence, have not received immediate attention although their impact will be longer lasting. The financial sector has been thoroughly modernized and the regulatory system guiding it is being brought up to world class standards. Very few persons could look at the financial sector now and compare it with that which obtained 15 years ago.
8. There are other changes which we have made in terms of reducing the scope of Governmental activity and bringing private sector investments in to several areas once thought to be exclusive State province. Hence, investments in the tele-communications industry, the power sector, in the physical infrastructure such as airports and roads are now being undertaken by the private sector. We have also put in place the regulatory environment to give investors confidence that their returns on investments will not be determined by arbitrary decision-making.
9. Whilst we have not got everything right, we have demonstrated that some of what were seen as intractables in the past can be tackled successfully. Although 2003 was not a good year for inflation, the record of seven consecutive years of price increases below 10% demonstrates that we know how to deal with that problem.
10. But above and beyond those achievements, there is a new mood in the country particularly amongst an emerging class of young domestic investors. They monitor the activities of Government which provide them with the signal for their own investment decisions.
11. It is this group of business people who have been the driving force behind Partners for Progress. Their activities have changed the mood in the business community and facilitated interaction with Government and the trade union movement in ways which will redound to the national good.
12. That is why it is imperative that the Government must stick to its commitment to reduce and eliminate the fiscal deficit.

13. It is only by so doing that the sustainable downward path for interest rates will be achieved. This new era is going to call for new thinking, not just from Government, but from the financial institutions. As Government paper becomes less attractive, there must be a willingness by these institutions to provide support for projects, whether they are for expansion of for new ventures. Whether they are to produce goods or for services.
14. There is also a need for entrepreneurs to be willing to subject their proposals and their accounts to the most rigorous scrutiny.
15. For entrepreneurs there are clear incentives for taking your company public.
16. But this new mood is not simply reflected in the actions of the owners of capital. The initiative taken by the leaders of the trade unions representing public sector workers to sign the historic MOU with the Government demonstrates that labour is fully on board. This is no empty expression of national commitment. We are talking about dollars and cents.
17. And this Administration will not betray the historic vote of confidence given by the labour movement in terms of their contribution to the way forward. We recognize, as all should that there can be no period of sustained economic growth or social stability unless the workers are fully involved.
18. Despite the constraints, we are going to work to improve the social sectors.
19. The SIF Programme is but one example of that commitment to ensure that those who are most deprived are not forgotten as the economy expands.
20. The attainment of the fiscal deficit is a necessary condition towards the objective which we intend to reach. The objective is that, with reduced interest rates, debt servicing will consume a smaller percentage of total expenditure thus allowing us to concentrate on social and physical infrastructure. I must repeat – failure to make our target will be punished with a reduction in available credit,

increased interest rates and so less to spend on addressing the needs of those at the bottom of the socio-economic ladder.

21. But to get to that point we have to demonstrate to our creditors, domestic and external, that we are serious about living within our means. The task before us is a challenging one, but as we demonstrated last year, we are more than equal to any obstacle which can be placed in front of us.
22. This has not been an easy budget to construct – neither on the expenditure nor the revenue side. We have had to operate within tight constraints.
23. But within those constraints, we have tried to retain the confidence of our creditors, even whilst protecting the most disadvantaged. We have protected jobs, whilst getting the workers to contribute to fiscal restraint. At the same time the prospects for significant growth in the economy have not been this good for years. There are projects flowing from the pipeline.
24. In my last meeting with the public sector union leaders, I promised a Budget consistent with the MOU. We believe we have kept our commitment. We have –
  - (1) Kept property taxes where they were last year
  - (2) Rolled back the GCT on health insurance premiums
  - (3) Opened up new opportunities for new entrepreneurs in the ICT sector
  - (4) Given exporters a new loan facility with a 7% interest rate, and
  - (5) Imposed no new tax package.
25. There is room for all groups, all sectors, and individuals to contribute in this exciting period. Let us unite and move forward with confidence – as one nation.