

---

2006/2007 JAMAICA BUDGET OPENING PRESENTATION

Dr. The Hon Omar Davies  
Minister of Finance & Planning  
Thursday, April 26, 2006

---

<b>A:</b>	<b>INTRODUCTION.....</b>	<b>2</b>
<b>B:</b>	<b>REVIEW OF CALENDAR YEAR 2005 AND FISCAL YEAR 2006.....</b>	<b>4</b>
<b>C:</b>	<b>MEDIUM TERM.....</b>	<b>8</b>
<b>D:</b>	<b>HIGHLIGHTS OF EXPENDITURE.....</b>	<b>15</b>
<b>E:</b>	<b>FINANCING THE BUDGET .....</b>	<b>18</b>
<b>F:</b>	<b>CONCLUSION .....</b>	<b>22</b>

A: INTRODUCTION

1. Protocol
  - (a) Family
  - (b) Constituency
2. Thanks to officials
  - (i) FS, DFS's, all officials Ministry of Finance and Planning. Already indicated the achievement of preparing Estimates of Expenditure in line with the new configuration of Government. Although some divisions/departments more integrally involved, virtually all officers, at all levels contribute.
  - (ii) Thanks to Heads and officials of Bank of Jamaica, STATIN, PIOJ.
  - (iii) Must speak to quality of staff in the public sector and the "batting strength" (totally dissimilar to current West Indies team.) Few would recognize that much of the top hierarchy of the Ministry of Finance in place today reflects a change from a year ago – Financial Secretary, 4 Deputy Financial Secretaries, Director General for Tax Administration. In the midst of generalized criticism about inefficiency of the public sector, I know of few organizations local or foreign which could effect such a smooth transition in so many critical positions.
3. Must express gratitude to former Prime Minister, the Most Hon P J Patterson. This represents my 13<sup>th</sup> consecutive budget presentation but it is my first without him as Prime Minister. Members of this House have already paid a moving tribute to him but there are few who would realize how vital his studied insight into all issues has been in terms of guiding all members of his team.
4. I certainly have benefited.
5. I made reference to "the team" and must also publicly place on record, appreciation for the contributions of four colleagues here who are no longer in the Cabinet – Minister of Foreign Affairs and Foreign Trade, Minister of Health, Minister of Development, Minister of Water and Housing, Minister of Information.
6. Each contributed in his own unique way.
  - (i) KD – Security/Foreign Affairs
  - (ii) John – Health/NHF
  - (iii) Paul – Pipeline and
  - (iv) Danny – Labour/Water & Housing/Parliament
7. Must also take this opportunity to formally congratulate the new Prime Minister. In fact, the country and our democratic system of government should feel proud at

the manner in which the succession has proceeded in an orderly manner. Few countries in the world can claim to be able to do likewise. It is a powerful signal to all at home and abroad.

8. I now turn to outlining the structure of my presentation. First I will present a review of major highlights of Calendar 2005 as well as Fiscal Year 2005/06. Whilst data are available in general for 2005 in certain areas the same is not true for Fiscal Year 05/06.
9. I will discuss the medium term both in terms of macro-economic targets but also I wish to spend some time focusing on the social issues. Essentially, what are the priority objectives, which we as a country should aim at on both the social and economic fronts for the medium term? Thirdly, the medium term preview provides the appropriate context to assess specific areas of expenditure as reflected in the Estimates tabled just over two weeks ago and which has been reviewed by the Standing Committee. I will then address the matter of financing the budget and then wrap up the presentation.

**B: REVIEW OF CALENDAR YEAR 2005 AND FISCAL YEAR 2006**

1. Our review of both calendar year 2005 and fiscal years 2005/2006 is facilitated once again by a comprehensive set of available documentation. Again, congratulations are due to all the agencies involved in preparing them.
2. Whilst it has been said before, it bears repeating that both the calendar year and the fiscal year have been extremely challenging with “shocks” from nature as well as from world economic developments. These “shocks” have to be assessed against the background that the country was in the process of recovering from Hurricane Ivan which had devastated the island in September 2004.
3. I need not remind members that 2005 was characterized by an unprecedented numbers of hurricanes, virtually continuous rainfall and even when we were spared, the impact on the US had indirect negative effects on us.
4. Added to this was the impact of the unprecedented increase in petroleum prices.
5. The summary result was that the domestic economy was disrupted for an extended period lasting from September 2004 to November 2005. Most badly hit was agriculture, which recorded a decline of 7.3%, following a decline of roughly 9% in 2004. Also hit was the manufacturing sector, which declined by 3.4%, a sharp reduction, compared to a growth of 4.2% in 2004.
6. On the positive side, construction and installation grew by 7%. Electricity and water by 4.1%; mining and quarrying by 2.8%. The overall result was growth of 1.4%.
7. Inflation – Inflation for the calendar and fiscal year was 12.9% and 11.4 % respectively. Again the “unusual” developments, particularly during the period June to October contributed to the rapid increase in inflation. Of special significance was the increase in the price of domestic foodstuff which pushed up overall prices. This clearly related to the impact of the inclement weather on domestic agriculture.
8. Of significance is that subsequently – in the period October to March -cumulative inflation was only 1.1%.
9. The reduction in the second half of the fiscal year has provided the basis for the expectation that single digit inflation will be achieved for both calendar year 2006 and fiscal year 2006/2007.

10. Balance of Payments (BOP) – The estimated current account deficit for the fiscal year is approximately (US)\$925 million or 9% of GDP.
11. The deficit represents an increase of (US)\$320 million relative to the previous year and is primarily due to the deterioration in the merchandise trade balance. A major contribution to this deterioration was the increase in the oil import bill. In 2005, the oil bill grew from (US)\$943 million to (US)\$1,335 million, an increase of 41.5%.
12. The increase in the oil import bill could not be compensated for by the expansion in exports, particularly bauxite and alumina.
13. At the same time, the healthy level of the NIR which stood at just under (US)\$2.1 billion at the end of March allowed the country to withstand the various shocks to the BOP.
14. Questions have been raised about the “cost” to the country of maintaining the NIR at this level. Such a discussion can now take place from the comfortable and secure position of having the present NIR cushion. Despite the shocks, the loss of foreign exchange earnings from tourism for the period and the sharp reduction in earnings from export agriculture, such as sugar and bananas, there was never any question about the country’s ability to meet its external obligations. Therefore, in any attempt to assess the “cost” of maintaining the NIR, it is imperative that simultaneously the benefits are also taken into account.
15. From the perspective of the Administration, this discussion on the relative “merits” of having a robust NIR, does not take into account the constant threat to the BOP of any of the number of “shocks” over which we have no control.
16. Tourism – Despite the negative effects of the various hurricanes/storms/floods there was growth in the tourism sector, both in terms of arrivals as well as visitor spending. Stopover arrivals in Jamaica increased by 4.5% and earnings grew to \$11.55 billion, an increase of 6.5% from the previous year.
17. Even better news is that for this new winter season, (I have data on airport arrivals for the period December 15 to April 21) total arrivals amounted to just over 630,000 persons – a 16.8% increase over the corresponding period for the previous year.
18. Debt – The issue of the size of the country’s debt has received considerable attention and continues to do so. At the end of March 2006, total public debt stood at \$847 billion an increase of 11.5% over the total at the end of March 2005.
19. The debt to GDP ratio declined from 138.25% to 131.5%.

20. Today I have tabled, as I normally do during this Debate, a Ministry Paper detailing the debt management strategy to be pursued during this Budget year. What is clear is that this strategy has continued to retain the confidence of creditors, local and external. Evidence is demonstrated by the fact that despite the shocks which the economy experienced during the years, the country successfully placed a 20 year Bond in October 2005 at a 9.2% interest rate. This was bettered by a 30-year Bond placed in February 2006 with an interest rate 8.5% per annum.
21. The interest rates on Jamaican Bonds, although not at the level which we would desire, still remain significantly lower than those faced by countries with similar macro economic indicators, reflecting confidence in the management of the economy.
22. In terms of domestic interest rates, despite the challenges faced during the year there was overall decline. The results of the auction conducted yesterday showed another decline (albeit slight) in the rates.
23. The Fiscal Deficit – It is well known that the Government had placed high priority on the attainment of a balanced budget during fiscal year 2005/2006. For a host of reasons, it became apparent by the third quarter of the year that it would not be possible to achieve this target.
24. Several factors influenced our inability to meet the target. An important one was the impact on economic production by the natural disaster shocks. The impact, starting in 2004, was far greater than anticipated, affecting economic activities in all sectors, and particularly in rural Jamaica. This led to a decline in revenue inflows. At the same time, there was the need for increases in expenditure, occasioned by the need to respond to infrastructure, as well as the special pay adjustment for public sector workers in light of the higher than projected inflation levels.
25. As such, the overall deficit was of the order of 3.3%.
26. Employment /Unemployment – The unemployment rate in the 4th quarter of 2005 was 10.9% compared to 11.4% in 2005. While this percentage provides the comparisons which have been cited over the years, the Administration recognizes the need for social intervention programmes aimed at bringing about more rapid reduction in unemployment levels, particularly for the youth and for women. The Prime Minister will be speaking to such interventions in greater detail.
27. As regards the measurement of poverty, the Survey of Living Conditions (SLC) for 2005 provides us with the positive result that poverty declined to 14.8% in 2005 down from 16.9% in 2004. Each geographic region showed a reduction in poverty levels in 2005 compared to 2004. What is interesting is that “rural

towns” have a lower poverty level than the Kingston Metropolitan Area or the rural areas.

28. In terms of policy we are now at the stage where the SLC data which are available on an annual basis, should now be used to direct interventions in a more focussed way to address both the objective of poverty reduction as well as unemployment and under-employment. This will be a central objective of the Administration’s policy in the medium term.

C: MEDIUM TERM

1. I have already provided an assessment of developments during Calendar 2005 and in some instances where data availability permits, of Fiscal Year 05/06. There are several issues which can be highlighted. One which is of special interest and significance is the moderation in price movements over the past six months. Cumulative inflation over that period was 1.1%. Last time this occurred was between October 2000 and March 2001.
2. That development and certainly others over the last five years should provide us with the basis for analytic assessment of what targets we should set ourselves for the medium term in both the economic and social spheres.
3. The Budget debate provides us with a special opportunity for such a discourse. As the duly elected representatives of the people, we have an unique responsibility and opportunity in this debate to not only review the last fiscal year and preview the present one, but also and perhaps more important, to advance for public discussion our views on what should be national targets and objectives for the medium term.
4. At this juncture I would wish to speak directly to the role of the Opposition in such an assessment. It takes two to make a meaningful debate. There are clear objectives/obligations of an Opposition in our system of Government. Perhaps the main one is to democratically seek to remove the Government from office. Hence it is expected that the spokespersons will seek to identify weaknesses in policies and in project implementation which will demonstrate to the public at large, and the electorate in particular, why a change in the Administration would be to the benefit of the nation.
5. However, even whilst recognizing this obvious obligation, we must seek a way to have the Opposition become more involved in guiding the development of national policy. A great deal of focus has been placed on facilitating this involvement through constitutional change. Whilst the efforts to date must be commended and must be continued, the actual results have been disappointing.
6. Even as we continue with those efforts there are practical steps which we should put in place to facilitate dialogue and involvement. The major onus must be on the governing party, to facilitate this involvement but at the same time, there should be a willingness on the part of the Opposition to respond constructively.
7. At the practical level I have sought to share with the Opposition, in particular with the previous and present Leaders of the Opposition, information for which there is no legal requirement to provide. I have also sought to ensure that external financial institutions are given the opportunity to interface with them. This is a



- practice I believe we should broaden such that whatever constitutional change may eventually come about, access to information and involvement in proposed policy changes can be facilitated even before the relevant legislation is passed.
8. I can identify immediately prospects for this greater involvement/collaboration in new pensions legislation.
  9. As regards the medium term outlook, the Administration has already taken concrete steps to move beyond solely concentration on macro economic variables. As such, we have developed a medium term social and economic programme which for the past several years has formed the basis of discussions with our development partners.
  10. The discussion of social policy has been facilitated by the fact that Jamaica's data collection on social variables is one of the most advanced – anywhere in the world as reflected in a range of publications e.g. – the annual Survey of Living Conditions (SLC) and the Economic and Social Survey.
  11. For the medium term let me begin with the macro-economic programme. This has been circulated and there are no real surprises, although the major caveat would be “subject to shocks, related to national disasters or prices of imported commodities” – oil being the best (or worst) example.
  12. Certain realities have to be faced. To begin, the world is significantly more competitive and at the same time there is less concessional help forthcoming from bilateral and multi-lateral sources. Consider the following data on grant receipts. Last fiscal year grant inflows amounted to (US)\$11.3 million. In fact, only once in the last four fiscal years 2004/05 has grant flows exceed (US)\$20 million. That figure was related to assistance for Post-Ivan recovery.
  13. Also instructive is the gradual removal of special trade facilities, most notable those related to bananas and now sugar.
  14. Therefore, the major lesson is that from an economic perspective, we are increasingly on our own and this will be the norm for the future. As such there are certain non-negotiables related to managing the fiscal accounts, controlling inflation, reducing the debt ratios and maintaining stability in a liberalized foreign exchange system.
  15. Let me pause to comment on the objectives of a liberalized foreign exchange system. I have made various presentations in this House in several debates addressing the question of the fixed as opposed to market-driven foreign exchange system. I must confess that I thought the argument had been settled, but I am told that there continues to be interest in the issue.

16. It seems that the disaster in Argentina, once cited as the perfect model which should be copied by all, has not been sufficient to explode the myth that fixing the exchange rate will cure all ills. One would have thought that the resilience and efficiency of our own system as demonstrated by the stability maintained last year in face of unprecedented oil prices, in face of successive storms, hurricane, and floods would have represented adequate proof of the stability of our home grown, tried and tested model.
17. Since we are often more impressed with external view points, than those generated domestically, let me cite a study of precisely this issue carried out by two leading economists – Guillermo Calvo – Chief Economist at the IDB and Prof. Frederic Mishkin of Columbia University.
18. After reviewing the various options in terms of exchange systems available to a country the conclusion of these noted scholars was - **(GO TO PAGE 28 OF PAPER).**
19. Let me now turn to the social imperatives for the medium term. They include a reduction of unemployment, continued reduction of the levels of poverty, increased emphasis on broadening access to education and training and strengthening the social security system, including reforming the pensions industry.
20. Even as we speak of the social agenda, let it be clearly understood that the country's ability to respond to deficiencies which I have just outlined, must be dependent on continued maintenance of macro-economic stability and more important the sustained generation of additional investments. The flow from the pipeline must continue.
21. How will such investments be generated? Logically, investments will come from three broad areas: from domestic private sector, from foreign direct investments and finally from the resources of the State itself.
22. The policies which are developed for each of those potential sources of investments must be custom built. For the domestic private sector there is need for recognition by the State of the varying requirements of sub-sectors and there must also be a clear distinction between social welfare as opposed to the encouragement of business enterprises.
23. The development of the appropriate policies to facilitate increased investments by the domestic private sector must first be based on technically sound macro-economic programmes as well as continuing dialogue to identify the problems of specific sub-sectors. However, it is simply not possible for any sector to be subsidized in perpetuity, regardless of perceived social benefits.

24. As regards encouraging foreign direct investments, the results of the past few years have been encouraging and instructive. It is clear that consistency of policies including the articulation of coherent medium term targets, has raised the country's credibility and credit-worthiness in the eyes of foreign investors. This is reflected in the unprecedented level of investment inflows in tourism, bauxite/alumina, and infrastructure.
25. Our task is to continue to provide the reassurance to foreign investors in order to facilitate sustained investment even whilst moving to the second issue of ensuring that the benefits of these investments flow through the system and more members of the society can identify with the benefits of these investments.
26. Let us desist from posing the false dichotomy - the irrelevant either, or - between large foreign investments and the seeming absence of immediate benefits to those at the bottom of the economic ladder – the unemployed youth, small domestic producers including farmers.
27. Respectfully, while we treasure good corporate citizenship, this is not the main responsibility of the private investor – domestic or foreign. It is our responsibility to develop these linkages.
28. This logically takes us to the role of the State. I would wish to suggest that there are three critical roles to be identified by the State in terms of facilitating economic growth and employment creation. In the first instance, there are some investments which are so “lumpy” that they often need the presence of the State either on its own or as a joint venture partner. Our role in the bauxite/alumina industry under successive Administrations is one such example.
29. A second area would be in terms of the State initiating developments in a region or sector either on its own or in collaboration with the private sector. The State's involvement in many tourism projects, most recently Sandals Whitehouse - is a good example. Despite the problems which are associated with this venture - and there have been problems – this investment will, in the long run, serve as the catalyst for the opening up of a complementary tourism product uniquely suited for the South Coast.
30. The question which then arises is what is a permissible loss to be absorbed by the State for either a sector or a specific project? Clearly, regardless of how attractive a project is, there must be a limit set on the loss which can be absorbed by the State. We need to take the debate to this level.
31. Examples – NW Manley and Negril. Edward Seaga and Ocho Rios; PJ Patterson with highway infrastructure.

32. There is yet a third role for the State in terms of investments and employment generation. The fact is that Jamaica, not unlike several other countries, is caught in a transition whereby a significant percentage of the labour force is not equipped to meaningfully contribute to a rapidly changing economic structure. The sugar industry is the most blatant example but the same applies to several other sectors.
33. Even as we speak a looming problem is that progress on construction projects will be constrained by the unavailability of adequate numbers of skilled workmen even whilst there remain significant numbers of unemployed or under employed. A complement to this is a situation where new “lumpy” investments have spin-offs in terms of demands for goods and services which cannot be supplied by local individuals or small enterprises.
34. What then is the role of the State in such activities? It includes aggressively increasing training at all levels. Not just for the young but for adults who need to retool or to have their skills upgraded. There is also the need to recognize that in the interim, the State will have to allocate some resources for employment activities which are not demonstrably viable in a strict financial sense. The Lift Up Jamaica Programme is a case in point.
35. Such programmes, often ridiculed, represent enlightened self-interest on the part of society. Recent paper by Barry Chevannes arguing that unemployment is a major cause of “disorder”. – (QUOTE CHEVANNES)
36. The important issue is to ensure that to as great an extent as possible, we set targets for the transition from unskilled to semiskilled and from semiskilled to skilled.
37. My deliberate attempt to establish for the medium term a socio-economic framework is derived from the clear experience, not just in Jamaica, but from other countries faced with the same challenges, of the need for a common national perspective of the way forward – a “social pact” as it were.
38. This pact must recognize that for a host of reasons, including the competing demands from different sectors, as well as the continued existence of a too-onerous debt burden that the resources available for social intervention are limited. It is within this context that I will briefly speak of the MOU which expired at March 31, and our hopes for a successor agreement.
39. The two-year agreement which expired on March 31 was a significant development for the labour movement and for the maturation of the relationship with the main employer of labour - the State. For too many, this MOU was seen simply as a wage freeze. For those involved in the process there was always a deeper recognition that, although our other objectives and targets were not all met, this agreement transcended a wage pact.

40. Respect is due to the labour leaders who recognized the importance of the agreement and the potential for development of the workers who they represent. The union leaders were provided with an unprecedented opportunity to interface on a monthly basis with the leadership of Government, not simply to discuss issues related to conditions of service, but perhaps more important, issues of social and economic policy.
41. These interactions were not superficial but of substance and brought about a greater understanding on both sides of the table of the issues impacting on national development. The gains made over that two-year period were significant and must not be abandoned.
42. There are some challenges and this is a natural expectation in a democratic society, but the Administration is very confident that as in the case of the other challenges which we faced and overcame during the first MOU, that these will also be overcome and a successor agreement will be entered into.
43. The final issue which I wish to place on the table for further consideration for the medium term relates to social security - in particular pensions. One of the most significant pieces of legislation completed during the last parliamentary year related to that which will now provide the regulatory framework for the industry.
44. This new legislation will provide the Government, through the FSC, with the ability to monitor the management of pension funds to ensure that such funds are invested wisely and that the workers are protected. For, in the final analysis, we are talking about their hard-earned resources which have been invested to protect them when their working days are over.
45. Few persons realize that prior to the passage of this legislation, the only laws governing pension funds related to the tax concessions from which such funds benefit. There was no mandatory registration of the funds or screening of those charged with managing them. Hence there could be no definitive response to questions posed about the industry e.g. – what precisely is the size of the industry? The recently passed legislation puts us in a position to speak definitively and to take appropriate actions to protect the interest of the workers.
46. I have just last week met with the major stakeholders in the sector in order to ensure their full involvement in the additional changes which must take place in the legislation; these changes include vesting and portability.
47. The Leader of the Opposition in his contribution to the recent debate spoke to the need for the biggest pension fund of all – the National Insurance Fund - to be subject to the same level of transparency and accountability being demanded of private funds. We are at one. The Administration's objective is to ensure that as

we move forward to broaden and strengthen the legislation, these discussions will benefit from the consideration of a joint Parliamentary Committee which will provide the recommendations for hopefully, unanimous adoption by both Houses of Parliament. As such, I hope that the passage of this new legislation will be a primary objective for the new legislative year.

48. I have used this opportunity in looking at the medium term to challenge the speakers from the Opposition and indeed those in the public and in the media, who speak on national issues to take the debate to another level. Let us depart from the “same old, same old”. We have the opportunity and the obligation to address the challenges our country face with analytic rigor with the objective of pragmatic solutions.

**D: HIGHLIGHTS OF EXPENDITURE**

1. The data indicate that the planned expenditure on capital for FY 06/07 is \$28.9B - significant increase over the allocation for last FY.
2. To be precise the numbers contained in the estimates overstate actual work which will be carried out during the year as included in these figures are payments under deferred financing schemes. Such projects have long been completed but our agreement with the Auditor General is that the sums are placed in the Expenditure Budget during the year when the payments are actually made.
3. For example under the Ministry of Education's capital budget, there are sums totaling approximately \$1B for payments - \$350M for schools constructed in Western Jamaica and \$640M for schools constructed in St Catherine.
4. It is not possible to discuss expenditure in all ministries. Will focus on Education, National Security and Housing, Transport & Works.
5. **Education**  
A significant addition to the capital budget for this Ministry – an allocation of \$3.6B representing the balance of NHT funds (\$5B) not spent in 05/06. A range of programmes, the biggest relates to expenditure of \$2,650M to facilitate rehabilitation and upgrading of schools as well as rehabilitation of both primary and secondary facilities.
6. This is a significant expenditure but is urgently needed to bring the facilities island-wide up to acceptable standards.
7. This is an appropriate juncture to place on the table once more the issue of a need for additional resources of similar magnitude over the medium term to facilitate the transformation in the education system to which we all say “Aye.
8. The decision last year to transfer \$5B from the NHT to facilitate this process resulted in some controversy. Although the transfer took place, the agreement was that this would be a one-off activity.
9. I take this opportunity to signal to members that the Government is formally examining the present range of payroll regulated deductions – from both employers and employees with two objectives. The first is to respond to the valid criticisms that the present system is overly complicated and the varied requirements represent a major cost to firms to be compliant. As such the first order of business is to simplify the system and reduce the associated costs of compliance.

10. The second objective is to provide flexibility in terms of allocation of the resources depending on the particular priority in the nation at a given period. And so, if the consensus is that for the next ten years the education and training system is in need of additional resources, there should be the ability to make this reallocation without the controversy of last year.
11. It makes no sense for one sector to be cash rich whilst another needing additional resources is starving.
12. The first draft of the study on rationalization has been prepared. It has not been considered by Cabinet, but the Leader of the Opposition was interviewed by the consultant and is in possession of the first report.
13. A priority aspect of the new legislative year must be to address implementation of recommendations aimed at achieving the two objectives listed above. Let me assure all contributors – employees and employer that the Administration is of the view that the present level of deductions is adequate. There is no plan to increase the total amount.
14. A final point which I wish to make in terms of education is to support the position articulated by my colleague Minister recently in terms of the level of subsidy being provided at the tertiary level. The objective of the country must be to provide increased access to quality tertiary education to as many qualified students as possible. At present the State absorbs up front, 80% of the cost of tertiary training. It is not possible to simultaneously increase access and to increase the level of subsidy. The resources just do not exist.
15. The obvious question is, will students from the lowest income groups be denied access because of the need to meet a part of their tuition cost? The answer is absolutely not!!
16. It is within that context that we need to expand the activities of the Students' Loan Bureau. Last year I was able to negotiate with the deposit taking institutions a concessionary loan of \$1,750M to the SLB which facilitated the reduction of interest rates on new loans to 12%.
17. We have examined the situation and I am pleased to inform colleagues and the public that effective September 1, the interest rates on old loans will also be reduced to 12%.
18. It is imperative to note that for students from poor families grants are also available to supplement these loans.
19. Problem which I have encountered as an MP – reluctance of many low income families to borrow from the SLB.



## **20. National Security**

- The whole society is united around the commitment to reduce the levels of crime and violence. To date 2006 represents a major improvement over 2005. We are certainly not where we need to be, but the progress is encouraging.
21. It is apparent however, that to take the fight against crime and violence to another level, there is need to rapidly improve the technological capabilities of our crime fighting institutions. Contained in the Capital A estimates is a sum of \$1,500B for the Ministry of National Security of which nearly \$1.1B will be dedicated to the acquisition of modern technology.
22. There is a sum of \$721.5M for the purchase of digital radio and digital microwave network for the Jamaica Constabulary Force. It goes without saying that the communications network available to crime fighters must be superior to that available to the criminals.
23. In addition, there is a sum of \$353.5M for automated palm and finger printing system and an integrated ballistic information system.

## **24. Ministry of Housing, Transport & Works**

- This is indeed a “super ministry” with responsibility for continuing the expansion and modernization of the country’s infrastructure network. This is needed to simultaneously respond to the demands of our own citizens as well as to provide the basis to attract more foreign investments.
25. In terms of water, I wish to highlight two projects. The first is the major Rural Water Supply to which \$610M has been allocated. This will address projects at Shettlewood in St James, Milk River in Clarendon and Christiana/Spaulding in Manchester and Clarendon. There will also be the commencement of civil works for the laying of pipes for the Hope Bay/St Margaret’s Bay scheme.
26. The second scheme which I wish to highlight is the Kingston Metropolitan Area Water Supply Scheme for which an allocation of \$1,135M has been made. This scheme is partially financed by the Japanese and the objective is to boost the supply for South East St. Catherine and the Kingston Metropolitan Area.
27. In terms of transportation, the North Coast Highway Improvement will receive nearly \$2.250M. This will address both the segments from Montego Bay to Ocho Rios and the new segment from Ocho Rios to Port Antonio.
28. Also to be noted is the allocation of \$25M for continued construction of the state-of-the-art, world class Transportation Centre at Half Way Tree which has been facilitated by the bilateral support from the Belgian Government.

E: FINANCING THE BUDGET

1. Useful for me to summarize the main parameters of this budget for Fiscal Year 06/07. It is cast within the context of the medium term economic framework which has been circulated.
2. As such, the expenditure budget calls for spending of \$358 billion with amortization accounting for \$117.6 billion and recurrent and capital programmes \$240.5 billion. A significant positive in the budget for this fiscal year is the growth of capital expenditure which is just under \$29 billion up from \$15.5 billion in 2005/06.
3. Before going to the heart of the matter which is how this budgeted expenditure will be financed there are some preliminary issues which need to be addressed. The first relates to the fact that although a start has been made, there still is a way to go in terms of implementing various proposals from the Matalon Tax Reform Committee. It is very often the approach to cite the “give back” proposals and ask when they will be implemented without, at the same time, addressing those aspects of the Committee’s report which would lead to a more rational system.
4. As regards “give backs” the significant increases in the tax threshold were undoubtedly justified but nonetheless, costly. They translate directly into revenue loss of approximately \$2.2 billion to taxpayers, with those at the bottom of the income ladder gaining more in relative terms.
5. There are other important steps to be taken including a rationalization of the complex web of incentives granted to various sectors and sub-sectors. Our ability to rationalize company income tax is to a large extent hindered by this web.
6. It is a firm commitment to address this rationalization not only within the context of the Jamaican tax system, but also from the perspective of our participation in the CSME. We are in the process of obtaining assistance from a multilateral institution to carry out the required work needed to inform policy changes in this area.
7. Another point which should be appreciated is the reduced level of grant funding from which the country benefits. In the last fiscal year, grants amounted to (US)\$11.3 million. In 02/03 it was (US)\$18.13 million and 03/04 (US)\$9.8 million. Simply put, increasingly we will be on our own with the budget to be financed mainly from our own resources.
8. One dilemma which we face in seeking to rationalize the tax system is the objective of simplification which facilitates greater equity and ease in auditing. On the other hand, there are special cases deserving special consideration. One

such example is that related to application of GCT to services associated with funerals. The Member from Central St Catherine made an impassioned presentation on this matter during my appearance before the Standing Finance Committee. I promised her I would re-examine the issue. I am pleased to inform the House that effective June 1, 2006 funeral expenses of \$100,000 and under will be zero-rated, for GCT purposes.

9. A similar plea has come from the agriculture sector and even whilst we seek to simplify the system we are cognizant of the impact on those who work in this sector, which has taken a tremendous beating over the past two years. As such, with effect from June 1, items falling in the following groups will once more be zero-rated.

### GO TO DATA

#### 10. Revenue and Grants

The projected revenue and grants for FY 2006/07 of \$222.2B represents an increase of 19.0% over FY 2005/06 and is disaggregated as follows:

	2005/06 (in billions of dollars)	2006/07	Change %
<b>Revenue &amp; Grants</b>	186.7	222.2	19.0
Tax Revenue	162.6	195.0	20.0
Non-tax Revenue	11.8	12.8	8.8
Bauxite Levy	3.1	3.9	24.9
Capital Revenue	8.5	6.8	-19.9
Grants	0.7	3.7	414.9

11. Tax revenue, which comprises about 87% of total revenue, is forecast to grow by 20% over the previous fiscal year. This growth is underpinned by the projected growth in the economy, to be augmented by aggressive revenue enhancement measures.
12. The revenue enhancement measures will reflect a menu of administrative and legislative initiatives geared toward improving the tax system, reducing the incidence of non-compliance and boosting collections.
13. Have noted almost unanimous view – widen the net, go after delinquents. Government's prime responsibility but all have a role to play. Special appeal to private sector entities and special interest groups.
14. Leading financial institutions has voluntarily laid out rules governing relationship with clients. Must be demonstrably tax compliant. Ask others to follow that lead.

### **15. Administrative/Compliance Measures**

Achievement of the programmed fiscal deficit of 2.5% of GDP in 2006/07 will require the tax authorities to adopt an aggressive approach toward increasing tax revenue collections. To this end Tax Administration will be undertaking special projects aimed at:

- (i) auditing and assessing very large companies and
- (ii) collection, through a concerted and carefully managed programme, of a significant portion of the large portfolio of tax arrears, known to exist on taxpayer accounts.

### **16. Forensic and Other Large Audits**

The audit coverage of very large firms has up to now been extremely inadequate, partly because empowering legislation is weak in some areas, but also because the skills of the tax auditors have been unequal to the requirements of these complex and technically demanding audit examinations.

17. The tax administration has secured international help to provide guidance on the audits of some targeted companies, beginning in April 2006. Although the entire audit process will take some time, given the taxpayers' rights of objection and appeal against assessments, it is nevertheless envisaged that some collections will result from the special audit effort during FY 2006/07.

### **18. Arrears Collections**

The collection of taxpayer arrears is one of the most challenging aspects of the work of any tax administration. Tax arrears in Jamaica are known to have grown to several tens of billions of dollars, but prior to FY 2004/05, efforts to collect them have not been very successful. During the last five months of FY 2005/06, the tax authorities designed and implemented a project aimed at collecting \$5.0B of these arrears.

19. The programme involved a special collections group of just about 100 officers who were exposed to special training in arrears collections and in reconciling taxpayer accounts on the tax administration computerized systems. The group was divided into four teams covering the four tax administration regions in the island, and produced weekly collections reports for a project coordinator in the office of the Director General, Tax Administration, who had overall management responsibility for the project. During the five-month period from November to March, the project collected a total of \$5.6B in arrears of company and individual income taxes, PAYE, education tax and general consumption tax.
20. The administrative arrangements for, and management of, the collection exercise which was so successful on this special project, are now being implemented as part of the general compliance process within the Inland Revenue Department.

21. These measures, alongside the elasticity of the tax system should ensure achievement of the targeted \$195.0B in tax revenue.

**22. Non-tax Revenue**

Non-tax revenue is projected at \$12.8B, 8.5% above collections in FY 2005/06. The estimate for non-tax revenue amounts to 1.7% of GDP, which is marginally below the 1.8% in 2005/06. This estimate includes receipts from the sale of a fourth cellular license.

**23. Bauxite Levy**

The bauxite/alumina industry is expected to remain quite buoyant in FY 2006/07, which should result in significant levy inflows. Projections are for a 25% increase in levy receipts over FY 2005/06 to \$3.9B. Underlying these estimates is further growth in bauxite production and world aluminium price.

**24. Capital Revenue**

Capital revenue estimates of \$6.8B are \$1.7B (20%) less than collections in the previous fiscal year. The forecast for capital revenue includes expected inflows from the divestment of Government's shares in Jamaica Public Service Company Limited (JPSCo).

**25. Loan Receipts**

The revenue forecast outlined above of \$222.2B and the \$358.2B expenditure budget approved by Parliament leaves a financing gap of \$136.0B. In February 2006 the GOJ raised US\$250M which amounts to (J)\$16.26B, on the international capital market as part of the financing plan for the FY 2006/07 budget.

26. Of interest to note that neither the US\$ nor the J\$ equivalent has been touched to date – due to buoyancy of revenue collection to which reference has been made.

27. Accounting for the pre-financing receipt leaves a gap of \$119.7B, which will be covered by loan receipts. The estimate is for external loans of \$7.9B from multilateral/bilateral sources that are associated with capital projects. Domestic borrowing of \$111.9B will be utilized to finance the deficit and amortization.

28. The fact that there are no “bullet” external amortization payments in 2006/07 makes the case for minimal external borrowing during the year. This forecast for domestic loans represents a reduction from the \$130.9B raised in FY 2005/06 and bodes well for reduction in interest rates in 2006/07.

29. In summary, the expenditure budget of \$358.2B will be financed by revenues of \$222.2B and loans of \$136B. There is no tax package. There are no new taxes!!

F: CONCLUSION

1. As I had noted at the beginning of my Presentation, this debate on the fiscal budget for 2006/2007 is taking place at a significant point in our country's history. It is taking place against the backdrop of us having to face the challenges, some domestic and others from nature and international events, beyond our control.
2. We can only make general assumptions about future "shocks" and their intensity. That we were able to come through fiscal year 2005/2006 and calendar year 2005, in the manner we did, is an attribute to the resilience of our people and the economy.
3. We have presented our expenditure budget which is significant for a host of reasons. The reduced size, in real terms, compared to last year's budget demonstrates our continued commitment to fiscal prudence.
4. It is no secret that our debt ratio remains too high and that we have been diverted from our path towards elimination of the deficit in 2005/06.
5. Any one who has toured the country knows that there are significant infrastructure needs which have to be addressed. We have been fortuitous in that, there is no major one-off (bullet) external debt payment to be made this year. This has given us some "fiscal space" to address areas needing support.
6. We know that no ministry, or department has received all they would wish. This is the nature of budgeting in a country such as ours, where demands invariably exceed available resources.
7. Nonetheless, we have presented a budget which will be financed with no new taxation. Rather, we intend to focus on increasing the equity of the taxation system by going after those individuals and companies who have accumulated significant arrears or who consistently pay less than they should. We accept that as government, we must demonstrate the commitment to increasing the equity of the system. Everyone advises that this is what we should do. I sincerely hope that we hear no protest when we "walk the walk".
8. But there are fundamentals which the country must face in the medium term. The steps which this Administration has taken, in terms of managing the economy, have all been geared towards preparing the country for a new era - an era of fewer breaks, fewer concessions and reduced grant financing. An era of increased competition as preferential trade regimes are eliminated.

9. This Administration has no doubt that the country is capable of meeting the challenges which face us today and will face us in the medium term.
10. At the same time, let us not fool ourselves and pretend that there are simply “no pain” answers to difficult challenges. Adopting a policy of a fixed exchange rate does not address the fundamental issues of lower than desired levels of productivity, whether it is in the private or public sector.
11. Adopting a fixed exchange rate system is not sustainable, unless simultaneously fiscal prudence is exercised.
12. Pandering to unreasonable demands for increased wages is not possible unless other services are slashed or significant additional taxes are imposed.
13. We certainly do not believe that we have successfully addressed all the issues but make no mistake, significant progress has been achieved. We have taken on the multilaterals, and defined our own macro-economic programme. Very few thought it would have been possible for us to have maintained the commitment to ending our borrowing relationship with the IMF. Now they assess our programme on the basis of mutual respect and we have even become the “best of friends”.
14. Our technicians and our policy makers have developed and implemented our own set of policies and they have shown positive results. We have a stable foreign exchange system and adequate reserves to see us through times of trouble. 2004 and 2005 provided us with ample proof of this.
15. The credibility of our programme has simultaneously attracted record levels of foreign direct investment in bauxite/alumina, in infrastructure and in tourism, even whilst private capital has extended the maturity period of our Bonds to 30 years at the best market interest rates we have even been able to obtain.
16. But there remain problems which we need to address on both the social and economic fronts. I list five.
  - i) We must continue with significant investments in the education and training system to bring our labour force to the point where it is capable of providing the value-added needed for this new phase of the economic development. We are convinced that under the leadership of the Minister, the Ministry of Education and the Transformation Team are up to the challenge.
  - ii) We must continue relentlessly to fight against crime and violence, not simply to reassure foreign investors or tourists, but more important, to provide a civilized environment for our own people. It is clear that the

initiatives which have been put in place (by both the present and former Ministers of National Security) are bearing fruits. We are not yet where we wish to be - but progress is being made.

- iii) We need to work with our micro and small businesses to better equip them not only to provide for the domestic economy but more importantly to reap some of the benefits to be derived from the demand of goods and services occasioned by the large investments which are taking place.
- iv) We will have to facilitate the transition in the agriculture sector, utilizing modern techniques to meet the demand for local consumption, to supply the expanding tourism sector as well as to fulfill our export obligations.
- v) We will have to work with our domestic financial institutions to reorient their focus from the purchasing of safe government paper to supporting investments in the real economy. In previous years we have spoken about this being a challenge for the future. The future is now.

17. Mr. Speaker, I have deliberately structured my contribution to this Debate in order to set the stage for a more meaningful exchange. However, let us not ignore certain realities.

- i) The Country is benefiting from unprecedented levels of FDI.
- ii) Inflation is trending down – 1.1% over the last six months.
- iii) Poverty levels are trending down.
- iv) The foreign exchange market is stable and the reserves are adequate.
- v) There was growth in the economy last year – despite the challenges.

18. As I close, I do not seek to dictate to the Opposition the form or content of their contributions to this Debate. However, I have deliberately thrown out the challenge that they will seek to use this opportunity to present alternative solutions to the challenges we face those advanced by the Administration. We need to take the Debate to another level. We need to unite around the issues where we share common objectives and methodologies. This cannot be beyond us. Our beloved country deserves no less.