GRENADA

Medium-Term Fiscal Framework: 2019-2021

Ministry of Finance, Planning, Economic and Physical Development

November 2018

I, Ophelia Wells- Cornwall, Acting Permanent Secretary, Ministry of Finance, attest to the reliability and completeness of the information presented in the Medium-term Fiscal Framework 2019-2021 and its compliance with the Fiscal Responsibility Legislation No. 29/2015 as amended.

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Mrs. Ophelia Wells- Cornwall

Permanent Secretary (Ag.)

1. RECENT ECONOMIC PERFORMANCE

Preliminary estimates based on data for the first nine months of 2018 indicate that the economy will continue along a positive trajectory in 2018 with projected growth of approximately 5.2 percent. Growth in 2018 is fueled primarily by the Construction and Tourism sectors, and supported by robust activity in the Transport and Retail Trade sectors. Average inflation, as measured by the CPI, was 0.6 percent for January to June 2018[1] compared to the same period in 2017. However, this is expected to increase in the latter part of the year with projected increases in international food and oil prices. The unemployment rate has been provisionally estimated at 20.9 percent, down from 23.6 percent in 2017.

Grenada's fiscal accounts continue to improve in 2018. A Primary Surplus (including Grants) of $ 199.6 million (6.2 percent of GDP) is provisionally estimated, making 2018 the fourth consecutive year that the primary surplus has been achieved. An Overall Balance after Grants of $136.3 million (4.2 percent of GDP) is estimated. The healthy fiscal performance was underpinned by enhanced compliance and enforcement in the Inland Revenue Department and the Customs & Excise Department, as well as Government's deliberate efforts to reduce its discretionary expenditure. Vibrant economic activity also contributed to the strong fiscal outturns. Public debt is estimated at 62.7 percent in 2018, a reduction of 6.2 percentage points relative to ratio at end-2017.

Table 1: Primary and Overall Balance after Grants 2017 vs 2018

	2017	2018	Variance	
	$m	$m	$m	%
Primary Balance after Grants	172.6	199.6	27.0	15.6
Overall Balance after Grants	91.6	136.3	44.7	48.8

Source: MOF

In the external sector, the current account deficit is estimated to widen on account of higher import values due to a rise in fuel prices. With respect to monetary developments, liquidity levels remained elevated and domestic credit growth is expected to accelerate in 2018. Overall, the financial system remains stable and sound.

[1] The latest period for which data are available.

2. MEDIUM-TERM MACROECONOMIC OUTLOOK

Grenada's medium-term economic prospects are positive. Real GDP growth (at market prices) is projected to average 4.0 percent over the period 2019-2021. Growth will be carried by public infrastructure development, as well as the expected continuation of the relatively strong performances in the Services Sector, particularly, construction, tourism, and education services. Meanwhile, inflation is estimated to edge up in in the short term on account of rising international oil prices, as well as possible increases in the prices of imported products should international trade wars escalate. Over the medium term however, inflation is expected to moderate with expansions in global oil production and the anticipated easing in trade tensions. The unemployment rate is expected to continue declining with increased economic activity, but it is likely to remain in double digits until reforms to address structural rigidities take root.

2.1 Medium-term Fiscal Policy Objectives

The Government's Medium-term Fiscal Framework (MTFF) 2019-2021 is framed to ensure compliance with the Fiscal Responsibility Law (FRL) No. 29/2015 (as amended in 2017). It is also framed to support the Government's Medium-term Agenda (MTA). The objective of the MTA is to anchor medium-term development planning and strategic interventions to accelerate inclusive, job-rich growth, as well as poverty reduction.

In relation to fiscal policy, the primary objective for the medium term is debt reduction. Accordingly, the Government will continue to deploy revenue and expenditure strategies such that primary surpluses are generated to keep public debt on a firm downward trajectory in the MTFF period.

With respect to revenue, the strategy is aimed at enhancing compliance, enforcement and administration, all with a view to building up Government's revenue base to be able to comfortably finance its expenditure plans on a sustained basis. Recurrent revenue is projected to reach $853.8 million in 2021, a 9.4 percent increase relative to the 2019 estimate. As a percentage of GDP, recurrent revenue is projected to average 23.1 percent over the period 2019-2021. Meanwhile, Grants are projected to average 3.7 percent of GDP over the medium term.

In relation to expenditure, the strategy will continue to focus on promoting greater efficiency in public spending to be consistent with the FRL's primary expenditure rule. More emphasis will be placed on improving the execution of the public sector investment programme and providing sufficiently for recurrent operating costs. Specifically, delays in project implementation, which increase gestation periods and cost overruns will be seriously addressed, as well as the manner in which projects are selected, prioritised and managed. Furthermore, expenditure control systems will be strengthened by upgrading procedures, processes and policies and reinforcing accountability and compliance mechanisms. In particular, Finance Officers will be given constant high-level attention and monitoring. Finally, priority will also be given to containing the growth of recurrent administrative costs by efficiently executing public sector reform so that cost efficiencies are maximised in the delivery of public services. A pay and grade exercise will be conducted to help inform any future changes to the wage bill. Accordingly, recurrent expenditure is projected to be to $636.8 million (17.2 percent of GDP) in 2021, a decrease of less than one percent when compared to the 2019 estimate of $637.8 million (18.9 percent of GDP). Capital expenditure is projected to average around 4.4 percent of GDP over the medium term and total expenditure as a percent of GDP is projected at 24.7, 21.9 and 20.7 for 2019, 2020 and 2021 respectively.

Based on the projected outruns for revenue and expenditure, Government's fiscal surpluses will be maintained over the medium term, with the overall surplus and primary surplus averaging 4.3 and 6.3 percent of GDP respectively in 2019-2021. Accordingly, public debt is forecasted to be on a persistent downward trajectory over the medium term, falling below its FRL's target of 55.0 percent of GDP in 2020.

Appendix 1presents the MTFF 2019-2021. The assumptions underlying the MTFF projections are at Appendix 2.

3. CONSISTENCY OF THE MTFF WITH THE FISCAL RESPONSIBILITY LEGISLATION

The following explicit fiscal rules and debt target are stipulated in Sections 7 and 8 of the FRL:

1. *Primary Expenditure Rule:* the rate of growth of the primary expenditure[2] of the Central Government and of every covered public entity, shall not exceed 2.0 percent in real terms in any fiscal year, when adjusted by the preceding year's inflation rate.

2. *Wage Bill Rule:* the ratio of expenditure on the wage bill shall not exceed 9.0 percent of GDP.

3. *Primary Balance Rule:* the targeted primary balance shall be a minimum of 3.5 percent of GDP.

4. *Contingent Liabilities Rule:* contingent liabilities arising from, as a result of, or in connection with Public-Private Partnerships (PPPs) shall not exceed 5.0 percent of GDP.

5. *Public Debt Target*: the total stock of public sector debt shall not exceed 55.0 percent of GDP.

Table 2 shows that the MTFF 2019-2021 is in compliance with the requirements of Sections 7 and 8 of the FRL.

[2]Calculated as Total Expenditure less Interest Payments.

Table 2: Compliance Matrix

	2019		2020		2021	
	Fiscal Rule	Projected	Fiscal Rule	Projected	Fiscal Rule	Projected
Growth of Real Primary Expenditure less capital grants (Annual % change)	2.0%	2.0%	2.0%	2.0%	2.0%	1.8%
Wage Bill (% of GDP)	9.0%	8.1%	9.0%	7.6%	9.0%	7.4%
Primary Balance (% of GDP)	3.5%	6.0%	3.5%	6.2%	3.5%	6.7%
Contingent Liabilities related to PPPs (% of GDP)	5.0%	0.0%	5.0%	0.0%	5.0%	0.0%
Debt Anchor: 55% of GDP*						
Public Debt (% of GDP)		56.5%		50.6%		44.7%
Notes: * the FRL does not stipulate a year in which the 55% is to be reached.						

Source: MOF

4. RISKS TO THE MEDIUM-TERM ECONOMIC OUTLOOK

A mix of upside and downside risks can affect Grenada's positive macroeconomic outlook. On the upside, Grenada's economic improvement and the investor confidence that it is likely to engender, together with potential upside surprises such as a faster-than-anticipated economic growth in Grenada's main trading partners, especially in the United States, augur well for the outlook. Additionally, the country's oil and natural gas discovery bodes well for the medium-to-long-term outlook.

On the downside, the projected growth in the economies of Grenada's main trading partners is tenuous and vulnerable to setbacks with increasing risks of protectionism, the potential escalation of trade wars in advanced economies and low productivity, as well as ageing population especially in the Euro Area. These global headwinds pose potential downside risks for Grenada, through lower tourist arrivals, remittances and foreign direct investment. Rising international oil prices is also a significant risk to the economic outlook, more so in the short term. Additionally, the cessation of oil refining by Trinidad's State-owned company –Pertrotrin-which was the main exporter of fuel to Grenada, can cause short-run disruptions that might increase the local price of fuel, as well as cost of production, with negative consequences for economic activity.

The fiscal outlook in particular can also be affected should the strong inflows to the National Transformation Fund (NTF) as well as external grants from development partners not continue over the medium term. Furthermore, fiscal risks can also materialise should state-owned enterprises (SOEs) fail to remain within their funding constraints or should there be calls on the Central Government's resources where SOEs cannot service their obligations. Capacity and institutional constraints also pose risks to the execution of the capital budget as envisaged in the MTFF. Pension reform, as well as the implementation of the National Health Insurance, if not properly managed, can also pose significant risks to public finances.

Finally, but by no means least, Grenada's vulnerability to natural hazards is an inherent risk; indeed, adverse effects of climate change can significantly affect agricultural output (in particular) over the medium term. Table 3 summarizes the main downside risks and mitigation measures. The Medium-term Fiscal Framework can be adversely affected should any of the downside risks materialise.

Table 3: Risk Summary

Risk Type	Risk Description	Source of Risk	Risk Rating	Measures to Manage/Mitigate Risks
Operational	Macroeconomic	Heightened global economic uncertainties and rising oil prices and trade tensions.		Continue to implement reforms to build economic resilience, boost competitiveness, productivity and growth. Additionally, continue to build fiscal buffers by strengthening Government's cash position and increasing savings.
		Lower-than-expected NTF inflows and grants from development partners.		Continue to exercise fiscal prudence to contain discretionary expenditure, prioritise strategic capital investments and improve revenue administration and collection. Additionally, further strengthen country-readiness systems to enhance the preparation of critical pre-investment work.

		Capacity and institutional constraints affecting project implementation		Continuous capacity building in project management and greater coordination among implementing ministries should help mitigate this risk.
		Cost associated with pension reform and NHI.		The respective ongoing processes must be guided by the parameters of the FRL to prevent any major fiscal fallout. In relation to both initiatives, it is crucially important that they be carried out in a phased and fiscally-sound manner.
		Operations of SOEs.		Ensure that up-to-date audited financial statements are submitted in a timely manner and closely monitor management performance within the SOEs to ensure that they pursue their respective stipulated mandates in the most cost -efficient and cost-effective manner.
Other	Natural Disasters	Hurricanes, tropical storms, and flooding.		Continue efforts to strengthen internal capacity to build resilience to natural hazards. NTF Regulations require 40.0percent of the monthly receipts to be set aside for arrears clearance, debt reduction and natural disaster relief. Given the downward trajectory of the debt stock, this arrangement should allow for a progressively larger share of NTF resources to be available for disaster relief. Additionally, the successful negotiation of the inclusion of natural disaster clauses in the debt restructuring agreements will allow for a specified moratorium in debt service following a qualifying natural disaster.

				Further, as a member of the Caribbean Catastrophe Risk Insurance Facility, Grenada stands to benefit from insurance payments in the aftermath of a qualifying natural disaster.

Key	
	High Risk
	Medium Risk

Appendix 1: Medium-Term Fiscal Framework 2019 - 2021

Grenada Fiscal Projections

In millions of Eastern Caribbean Dollars

	2019		2020		2021	
	Projected	as a % of GDP	Projected	as a % of GDP	Projected	as a % of GDP
TOTAL REVENUE AND GRANTS	964.2	28.5	932.2	26.2	949.0	25.7
CURRENT REVENUE	780.4	23.1	821.5	23.1	853.8	23.1
Tax revenue	726.5	21.5	764.7	21.5	794.8	21.5
Taxes on Income	157.4	4.7	165.7	4.7	172.2	4.7
Taxes on Property	28.0	0.8	29.5	0.8	30.5	0.8
Taxes on Domestic Goods & Consumption	156.8	4.6	165.1	4.6	171.6	4.6
Taxes on International Trade & Transacti	384.3	11.4	404.5	11.4	420.4	11.4
Non - Tax Revenue	53.9	1.6	56.8	1.6	59.0	1.6
Grants	183.7	5.4	110.7	3.1	95.2	2.6
TOTAL EXPENDITURE & NET LENDING	834.2	24.7	780.9	21.9	766.0	20.7
CURRENT EXPENDITURE	637.8	18.9	637.7	17.9	636.8	17.2
Personal Emoluments,Wages, Allowances & social contributions	275.4	8.1	272.2	7.6	272.5	7.4
Goods and Services	124.8	3.7	126.1	3.5	125.1	3.4
Interest Payments	72.0	2.1	67.7	1.9	64.9	1.8
Transfers	165.6	4.9	171.7	4.8	174.3	4.7
Net Lending	0.0	0.0	0.0	0.0	0.0	-
Capital Expenditure	196.4	5.8	143.2	4.0	129.2	3.5
Current Balance (before Grants)	142.7	4.2	183.8	5.2	217.0	5.9
Overall Balance (after Grants)	129.9	3.8	151.3	4.3	183.0	4.9
Primary Balance (before Grants)	18.2	0.5	108.3	3.0	152.6	4.1
Primary Balance (after Grants)	201.9	6.0	219.0	6.2	247.9	6.7
Memo item						
GDP (Nominal market prices)	3,381.5		3,559.4		3,699.2	
Real GDP growth (%)	4.2		3.9		3.9	

Source: MOF

Appendix 2: Baseline Medium-Term Fiscal Assumptions

CATEGORIES	2019	2020	2021
Recurrent Revenue	All categories of tax and non-tax revenue are assumed to grow in line with projected GDP. A policy decision on the reduction in the Peronal Income Tax and Corporate Income Tax rates were also factored into the projections		
Recurrent Expenditure			
Personal Emoluments, Wages, Salaries and Allowances	Assumes that the agreement beween the Government and the Unions for salary increase of 4% will stand	Projected to be consistent with the fiscal rule	
Social contributions to employees			
Goods & Services	Projected to be consistent with the fiscal rule		
Current transfers			
Interest payment	External and domestic interest rate payment reflects the conditions stated in the contractual agreements		
Grants			
Budgetary	Budgetary grants are equal to the expected inflow from donor agen		
Capital	Captial grants will be fully covered		
Capital expenditure & Net Lending	Assumes that it will average 4.4 percent of GDP based on the project implementation schedule		

Source: MOF