

# GOVERNMENT OF THE CAYMAN ISLANDS



**2008/2009**

## **Strategic Policy Statement**

**For the financial year ending 30 June 2009**



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## **1. Introduction**

### **Purpose of the Strategic Policy Statement**

This Strategic Policy Statement (SPS) sets out the policy and financial parameters the Government intends to use to prepare its Budget for the 2008/9 financial year.

In accordance with the requirements of the Public Management and Finance Law (2005 Revision) (PMFL), the SPS is strategic and high level in nature. It does not allocate resources to individual expenditure items or specify the particular initiatives the Government intends to pursue; rather the role of the SPS is to outline, for consideration and approval by the Legislative Assembly, the strategic parameters on which the Budget will be based. Detailed information will be contained in the Annual Plan and Estimates (the Budget) for 2008/9 when that is presented to the Legislative Assembly in April 2008.

### **Content of the SPS**

The content of the SPS reflects the requirements of the PMFL.

Section 2 outlines the Government's outcome goals for the next three years. These goals, which are set at a broad level, establish the policy direction for the Government over the period. They will be used by the Government to determine specific policy priorities for the Budget.

Section 3 contains an overview of the expected medium term economic position for the Cayman Islands relative to the global economic outlook.

Section 4 establishes the aggregate financial targets that the Government has established for 2008/9 and the subsequent two financial years.

Section 5 contains long term financial projections for the Core Government for the period 2011/12 through 2017/18. These projections are more indicative than absolute in nature and provide a sense of the Government's expected performance over the long term.

Section 6 sets out the indicative allocations to each Minister and Official Member for the 2008/9 Budget, together with indicative planning allocations for the following two years. These allocations are to be used as the basis for Ministers and Official Members and their Ministries/Portfolios to establish their operating and capital budgets for the 2008/9 financial year.

### **The Government's Strategic Approach**

The Government's strategic focus continues to be based on delivering the commitments made in the People's Progressive Movement (PPM) manifesto; and the importance of taking a medium and long term perspective to government finances.

The Government is fully committed to delivering on its campaign promises. These include improving the level and quality of education and health services, investing in essential road infrastructure, implementing strategies based on the lessons from Hurricane Ivan, combating crime, and continuing support for Tourism and Financial Services as the twin pillars of our economy. The parameters contained in this SPS reflect the continuation of that policy path.

The longer-term projections show that the financial targets established for 2011/12 to 2017/18 are affordable, sustainable, and allow compliance with the Principles of Responsible Financial Management over the longer term.

The publication of these long-run projections reflects the PPM Government's continued commitment to responsible, open and honest government.

## 2. Government's Outcome Goals

### Broad Outcomes

The PPM Government has established eleven broad outcome goals which have guided its policy actions since coming into office in May 2005. These broad outcomes remain unchanged for the 2008/9 to 2010/11 forecast period and are as follows:

- *Deal with the Aftermath and Lessons from Hurricane Ivan;*
- *Address Crime and Improve Policing;*
- *Improve Education and Training;*
- *Rebuild the Health Service;*
- *Address Traffic Congestion;*
- *Embrace Cayman Brac and Little Cayman;*
- *Conserve the Environment;*
- *Strengthen Family and Community;*
- *Support the Economy;*
- *Open, Transparent, Honest and Efficient Public Administration; and*
- *Sound Fiscal Management.*

These broad outcome goals indicate the Government's policy priorities and serves as a guide to how the government allocates its resources.

### Specific Outcomes

The specific outcomes the Government intends to target to achieve the eleven broad outcomes are summarised in Table 1.

*Table 1: Specific Outcomes and Key Policy Strategies*

<b>Broad Outcome</b>	<b>Specific Outcomes and Key Policy Strategies</b>
<b>Broad Outcome Goal: 1</b> <i>Deal with the Aftermath and Lessons from hurricane Ivan</i>	<ul style="list-style-type: none"> <li>• Provision of improved emergency shelter facilities</li> <li>• Improved capacity to respond to disasters and other emergency situations</li> <li>• Creation of a disaster tolerant central information technology infrastructure</li> <li>• Infrastructure to deal with storm water drainage</li> <li>• Improved enforcement of building control standards</li> </ul>
<b>Broad Outcome Goal: 2</b> <i>Address Crime and Improve Policing</i>	<ul style="list-style-type: none"> <li>• Provision of various courts to deal with drugs, family and commercial issues</li> <li>• Modernization of Court systems</li> <li>• Improvement to prison infrastructure</li> <li>• Enhanced capability to combat crime</li> </ul>
<b>Broad Outcome Goal: 3</b> <i>Improve Education and Training</i>	<ul style="list-style-type: none"> <li>• Produce a National Human Capital Development strategy</li> <li>• Promotion of a life-long learning initiative</li> <li>• Improvement to educational services</li> <li>• Continued construction of three new high schools</li> <li>• Construction of a new George Town Primary School</li> <li>• Provision of learning communities</li> <li>• Continued enhancement of the Civil Service College</li> </ul>
<b>Broad Outcome Goal: 4</b> <i>Rebuild the Health Services</i>	<ul style="list-style-type: none"> <li>• Improvement to public health services</li> <li>• Enhanced wellness programme for all citizens</li> <li>• Provision of a long term mental facility</li> <li>• Improved services at Government hospitals and clinics</li> </ul>
<b>Broad Outcome Goal: 5</b> <i>Address Traffic Congestion</i>	<ul style="list-style-type: none"> <li>• Completion of the East-West Arterial Highway</li> <li>• Continued road improvements such as widening and surface upgrades</li> <li>• Extension to the Linford Pierson Highway</li> <li>• Completion of the Esterley Tibbetts Highway</li> </ul>
<b>Broad Outcome Goal: 6</b> <i>Embrace Cayman Brac and Little Cayman</i>	<ul style="list-style-type: none"> <li>• Improvements to playfields, ramps and jetties</li> <li>• Continue supporting tourism in the Cayman Brac and Little Cayman</li> <li>• Improve the landfill in Cayman Brac</li> <li>• Improvements to roads in Cayman Brac and Little Cayman</li> <li>• Extension of the UCCI and the Civil Service College to Cayman Brac</li> </ul>
<b>Broad Outcome: 7</b> <i>Conserve the Environment</i>	<ul style="list-style-type: none"> <li>• Implementation of a National Conservation Law</li> <li>• Planning and implementation of a terrestrial system of protected areas</li> <li>• Pursue Waste to Energy initiatives</li> <li>• Landfill improvements and expansion</li> <li>• Expansion of the recycling efforts</li> <li>• Improved beautification programme</li> </ul>

<p><b>Broad Outcome: 8</b> <i>Strengthen Family and Community</i></p>	<ul style="list-style-type: none"> <li>• Improvements to community facilities</li> <li>• Cemetery expansion and development</li> <li>• Upgrading of Sports facilities</li> <li>• Development and enhancement of parks and beaches</li> <li>• Development of a National Sports Council</li> <li>• Enhanced care for persons with disabilities</li> <li>• Provision of additional facilities to accommodate the elderly</li> <li>• Provision of a therapeutic youth facility</li> <li>• Provision of transitional housing for released prisoners</li> <li>• Build capacity to respond to the National Assessment of Living Conditions (NALC)</li> </ul>
<p><b>Broad Outcome: 9</b> <i>Support the Economy</i></p>	<ul style="list-style-type: none"> <li>• Support a diversified agricultural sector.</li> <li>• Improvement and enhancement of Government Offices Infrastructure</li> <li>• Implementation of an integrated tourism marketing and product development strategy</li> <li>• Continued support of the Go-East Initiative</li> <li>• Implementation of strategies to increase tourist arrivals from Europe and Canada</li> <li>• Implementation of an affordable housing initiative</li> <li>• Continued support to first time Caymanian home owners</li> <li>• Promote and facilitate appropriate long-term foreign and local investment in the Cayman Islands</li> <li>• Conduct a National Census</li> <li>• Increased surveillance by key financial regulatory bodies</li> </ul>
<p><b>Broad Outcome: 10</b> <i>Open, Transparent, Honest and Efficient Public Administration</i></p>	<ul style="list-style-type: none"> <li>• Implementation of the Freedom of Information Law</li> <li>• Continued support of constitutional reform</li> <li>• Continued support for the Office of the Complaints Commissioner</li> </ul>
<p><b>Broad Outcome: 11</b> <i>Sound Fiscal Management</i></p>	<ul style="list-style-type: none"> <li>• Control growth in operating expenditure of core Government</li> <li>• Continue to manage the government finances in full compliance of the Public Management and Finance Law</li> </ul>



### 3. Economic Overview

#### *Introduction*

This section outlines the forecasted economic position of the Cayman Islands for the period 2008/2009 to 2010/11. It includes a brief review of the global economic situation and the country's performance from January 2006 to September 2007 to provide the context for the Cayman Islands' macroeconomic forecasts. These forecasts are a key determinant of the Government's Aggregate Financial Targets, which are outlined in Section 4.

#### *World Economic Position*

##### **Overview<sup>1</sup>**

In 2006, global economic growth was estimated at 5.4 percent, an improvement on the 4.8 percent recorded in 2005. Global growth originated predominantly from productivity increases in most advanced economies, supported by strong domestic demand. Strong consumption demand led the growth in the United States of America (US), Canada and Japan. Gross domestic product (GDP) of the US grew by 2.9 percent amidst adjustments in the housing market. The Euro area recorded the highest growth (2.8%) in six years, as the German, French, and Italian domestic markets expanded at healthy rates in 2006.

World output was estimated to have increased in the first half of 2007. Global growth for the whole year of 2007 is projected at 5.2 percent amidst adjustments in the financial markets of advanced economies, and inflationary concerns among some emerging market and developing countries. The global growth is 0.3 percentage points higher than was projected in April 2007 by the IMF. The major upward revisions have been for emerging markets and developing countries, particularly, China, India, and Russia. On the other hand, economic prospects of the US were revised downward.

##### **US Economy**

The US is the main source of consumption goods and production materials for the Cayman Islands, as well as a key market for the country's service sectors. The local market is also highly susceptible to interest rate policies in the US due to the currency board system which pegs the value of the local currency to the US dollar. By extension, US interest rate are a main determinant of local interest rates and thus, of the overall macroeconomic performance of the Cayman Islands. The Federal Reserve revised the Federal funds rate downwards by 0.5 percent to 4.75 percent in September 2007. This is the rate that commercial banks use for lending among themselves and is expected to influence adjustments in lending rates.

In 2006, US economic growth deteriorated to 2.9 percent from the 3.1 percent in 2005. Strong growth was noted in the second quarter of 2007, an improvement over the sluggish growth in the first quarter. GDP growth is expected to be aided by favourable net exports associated with the weakening US dollar. Notwithstanding this, the downturn in the housing market which negatively impacts disposable income is expected to cause a lower GDP growth forecast for 2007 of 1.9 percent compared to the forecast of 2.2 percent in April 2007.

##### **Other Countries**

Other advanced economies are expected to turn in mixed GDP growth in 2007. The Euro area is forecasted to have GDP growth of 2.5 percent in 2007, slightly lower than the 2.8 percent recorded in 2006. In the United Kingdom, growth is projected to improve to 3.1 percent in 2007 from 2.8 in 2006.

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<sup>1</sup> This assessment is based on the World Economic Outlook (International Monetary Fund, October 2007).

**Table 2: Comparative Macroeconomic Forecasts (%)**

	2006			2007			2008		
	Cayman Islands	U.S.	Global	Cayman Islands	U.S.	Global	Cayman Islands	U.S.	Global
Real GDP Growth	4.6	2.9	5.4	3.8	1.9	5.2	3.2	1.9	4.8
Inflation (Consumer Price Index)	0.8	3.2	2.3 <sup>a</sup>	3.6	2.7	2.1 <sup>a</sup>	3.3	2.3	2.0 <sup>a</sup>
Unemployment Rate	2.6	4.6	5.6 <sup>a</sup>	3.2	4.7	5.3 <sup>a</sup>	3.5	5.7	5.5 <sup>a</sup>

Sources: IMF World Economic Outlook (October 2007) for US and global data; Cayman Islands Government Economic and Statistics Office for the Cayman Islands data.

<sup>a</sup> For advanced economies only

### *Cayman Islands Economy*

#### **Out-turns for 2006 and January to September 2007**

Economic performance in 2006 was bolstered by recovery in the tourism industry and stable growth in the financial and business services sectors. Estimated GDP grew by 4.6 percent compared to the 6.5 percent post-Ivan growth in 2005.

In 2006, total visitor arrivals increased by 11.7 percent, due to strong growth in air arrivals. The latter recovered by 59.3 percent while cruise arrivals increased by 7.3 percent. During the first half of 2007, total visitor arrivals grew by 3.3 percent as air arrivals strengthened by 8.4 percent while cruise arrivals rose by 2.6 percent.

The construction sector was a key driver of the economic growth in 2006. The value of building permits increased in 2006 by 32.8 percent while those of project approvals also moved upward by 22.8 percent. In the first three quarters of 2007, the value of building permits fell by 6.0 percent, while the value of project approvals declined by 22.0 percent.

The financial services industry maintained its resilience throughout 2006. With the exception of the banking and trust licenses which dropped by 4.6 percent, increases were recorded in insurance company licenses (1.1%), mutual funds (14.5%), stock exchange listings (15.2%) and company registrations (20.2%). During the first three quarters of 2007, mutual funds increased by 16.0 percent over the comparative period in 2006 while registration of new companies grew by 15.7 percent. Additionally, insurance licences increased by 3.3 percent, stock market listings by 25.7 percent while banks and trust registrations declined by 3.1 percent.

In 2006, the unemployment rate improved to 2.6 percent. For the first half of 2007, the unemployment rate stood at 3.0 percent as employment declined slightly with the moderation of construction activities.

Consumer prices rose on average by 0.8 percent in 2006 compared to 7.3 percent in 2005. The slower pace in 2006 resulted from declining housing costs which followed the increase in housing supply in the post-Ivan period. However, in the first two quarters of 2007, the average inflation rate stood at 3.7 percent compared to zero percent average inflation in the same period of 2006. This recent upward pressure was influenced by higher prices for personal goods and services, food and household equipment.

The fiscal balance further strengthened in 2006. The core government recorded a current surplus of \$116.1 million (or 5.7% of GDP) in 2006 from \$87.5 million (or 4.5% of GDP) in 2005. This performance was

bolstered by buoyant revenue increases from taxes on international trade and transactions of 8.8 percent, and from domestic taxes on goods and services of 12.9 percent.

The revenue increase occurred amidst a downward adjustment in imports. After the influx of reconstruction materials and consumer goods immediately after hurricane Ivan, merchandise imports declined in 2006 by 9.0 percent to reach \$906.1 million. Imports were dominated by consumption goods as capital and intermediate goods slackened off. In the first six months of 2007, however, imports rebounded by 17.8 percent compared to the same period in 2006 to settle at \$535.7 million. Part of the increase may be attributed to price increases particularly for food as global food prices for these imports have recently been on the rise.

In 2006, a preliminary estimate of the current account of the balance of payments reveals a deficit of approximately CI\$387.9 million, or 19.1 percent of GDP. This is, however, an improvement from the deficit of CI\$611.3 million (31.7% of GDP) in 2005. The improvement was largely due to significant growth in total visitor expenditures coupled with a lower level of imports during the year.

### **Estimates for the Financial Year 2007/8**

Real growth of estimated GDP for the Cayman Islands in 2007/8 is projected to ease to approximately 3.5 percent, down from 4.2 percent in 2006/7. The projection takes into account a 3.2 percent GDP growth for 2008.

Growth in 2007/8 is expected to be fuelled by strong performance of the financial and business service sectors. Meanwhile, the key risk to the forecasted growth is the softening of demand for tourism services as the growth prospect of the US economy, a major market, has been recently adjusted downward. The projected GDP growth incorporates this risk.

Inflation is expected to rebound to 3.5 percent in 2007/8, from 2.2 percent in 2006/7 resulting mainly from pressures on food prices, and personal goods and services. The key risk to local inflation is the upward trend of global food prices due to rising demand in developing countries including China and India.

Consistent with the moderation of growth projections, unemployment is projected at 3.4 percent for 2007/8, from 2.9 percent in 2006/7. This projection takes into account a 3.2 percent unemployment rate for 2007.

For the financial year 2007/8, the deficit on the current account of the balance of payments is expected to improve slightly to 19.0 percent of GDP. This takes into account the risk of a softening in receipts from tourism.

### ***Economic Forecasts for Financial years 2008/9 to 2010/11***

#### **Real GDP**

Over the next three financial years, economic growth in the Cayman Islands is expected to moderate following the downscaling in the economic prospects of its key markets, mainly the US. Barring external shocks, GDP growth is forecasted at 3.1% in 2008/09, 3.0% in 2009/10 and 2.8% in 2010/11 (See Figure 1).

#### **Employment Level and Unemployment Rate**

Given the above forecast growth path of the economy, employment levels is expected to be 35,520 in 2008/9, 35,876 in 2009/10 and 36,253 in 2010/11 (See Figure 2). The corresponding unemployment rate is forecasted at 3.6% in 2008/9, with 3.7% in both 2009/10 and 2010/11 (See Figure 3).

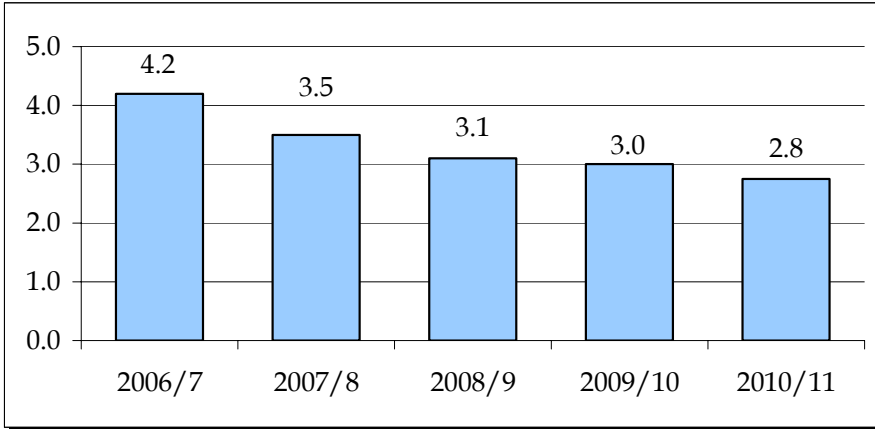
#### **Inflation**

Domestic inflation remains highly influenced by US inflation. Based on moderate inflation forecasts for the US, the local inflation forecasts for 2008/09 is 3.3%, 3.1% in 2009/10 and 3.0% in 2010/11 (See Figure 4).

#### **Current Account**

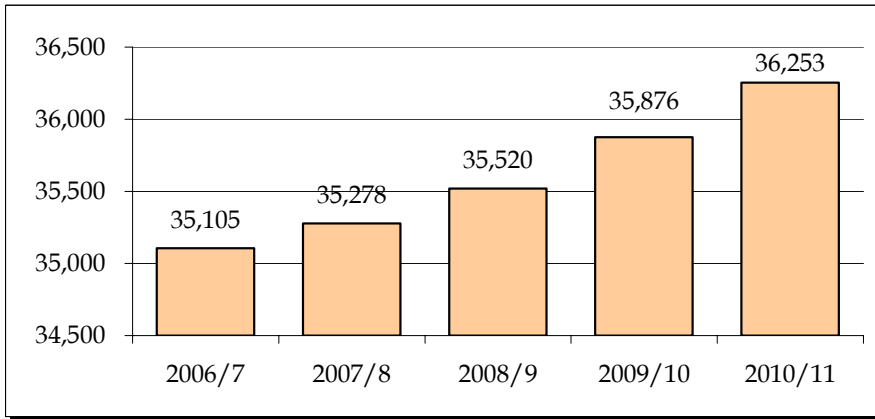
The current account of the balance of payments is forecasted at 18.5% of GDP in 2008/9, 18.0% in 2009/10, and 17.7% in 2010/11 (See Figure 5).

**Figure 1: Cayman Islands' Real GDP Growth Forecasts (in %)**



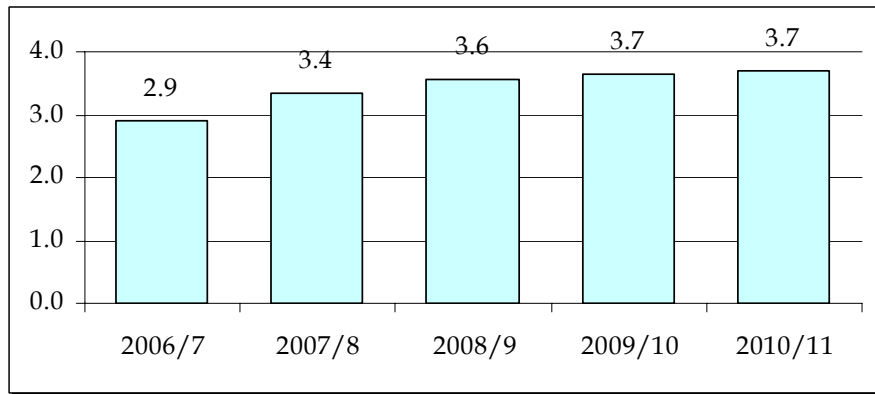
Source: Cayman Islands Government (Economics and Statistics Office)

**Figure 2: Cayman Islands' Employment Forecasts**



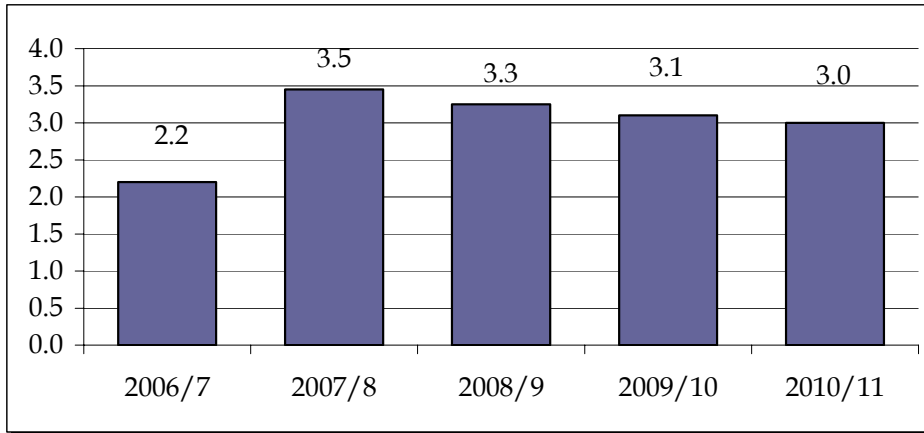
Source: Cayman Islands Government (Economics and Statistics Office)

**Figure 3: Cayman Islands' Unemployment Rates (%)**



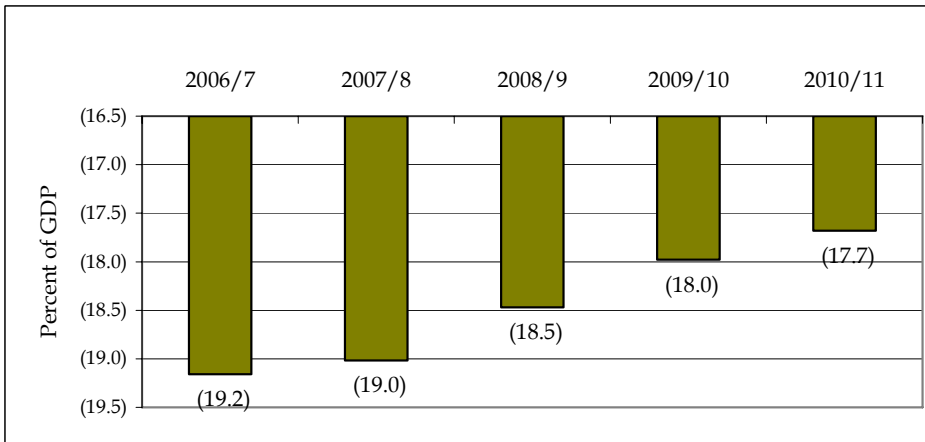
Source: Cayman Islands Government (Economics and Statistics Office)

**Figure 4: Cayman Islands Inflation Rate Forecasts (%)**



Source: Cayman Islands Government (Economics and Statistics Office)

**Figure 5: Cayman Islands' Current Account of the Balance of Payments**



Source: Cayman Islands Government (Economics and Statistics Office)

*Significant Assumptions Underlying the Economic Forecasts*

**Economic Growth**

- Growth of the US will soften in 2008 as compared to projections as of April 2007 while global economic growth is almost stable.
- In tourism, global air arrivals are assumed to grow by 4.0% annually which is greater than the 2.0% forecasted for the region by the World Tourism Organization (WTO) for 2007. Air arrivals to the Cayman Islands are assumed to grow at 4.6% in 2007 and 3.0% to 3.1% in 2008 to 2011.
- The financial services sector is sufficiently resilient to withstand global financial shocks.

**Employment / Unemployment**

- The domestic economy grows as forecasted.
- There are no major impediments to the supply of labour to meet the demand in the economy.

**Inflation**

- Forecasts are based on current CPI basket; rebasing is expected to be undertaken in the latter months of the fiscal year 2007/8 which could result to revisions in forecasts.
- The US Federal funds rate policy remains proactive or reactive to inflation data, and continues to influence local prime lending rates.
- Domestic demand is not subject to any major external shock.

**Current Account**

- Growth of imports is dependent on economic growth forecasts.
- Growth of receipts from services exports assumes modest growth in tourism services, business and financial services.

**Date Economic Forecasts Were Finalized**

The economic forecasts were finalized on October 30, 2007 and take into account economic data and information available as of that date.

## 4. Aggregate Financial Targets

### Introduction

In addition to achieving the Government's broad policy objectives, the Budget must comply with the Principles of Responsible Financial Management (the Principles) specified in the PMFL. Accordingly, the SPS is required to specify the aggregate financial targets for the Core Government on which the Budget will be based, and show that those targets comply with the Principles.

This section specifies the aggregate financial targets for the Core Government established by Cabinet for the 2008/9 Budget and the planning targets for the 2009/10 and 2010/11 Budgets. The targets for 2009/10 and 2010/11 provide a planning guide for the Government and will be updated in subsequent SPS documents in light of changes to the financial position of the government and/or policy priorities.

This section also outlines the fiscal strategy rationale on which the aggregate financial targets are based as well as explaining how the targets comply with the Principles.

### The Government's Fiscal Strategy

The Government's fiscal strategy continues to be the same as that outlined in the 2007/8 SPS. It consists of three elements: fiscal responsibility; the need to address the country's social and economic infrastructure needs; and economic management considerations.

#### *Strategy 1: Fiscal Responsibility*

As outlined in Section 2, one of the Government's outcome goals is sound fiscal management. The Government recognises that this is the bedrock upon which investor confidence in these Islands is built. It is also critical to the long term financial health of the country that the Government continues to manage its finances in a sound and controlled manner.

Accordingly, the Government is fully committed to the Principles. Compliance with the Principles is therefore the first, and perhaps most important, element of the Government's fiscal strategy. It is, and will continue to be, a key driver of the Government's financial decision-making.

#### *Strategy 2: Addressing Social and Economic Infrastructure Needs*

In addition to maintaining fiscal control, the Government also recognises that the social and economic infrastructure of the country needs to be improved. In particular, there are important infrastructure needs in the education, transportation and government administration sectors. These needs have both capital and operating requirements and their magnitude is considerable. The future of the country requires them to be addressed and the Government is doing so.

Accordingly, the second element of the Government's medium term fiscal strategy is to generate the cash flows necessary to finance priority capital and operating infrastructure needs. The Government's approach to achieve this is three-fold.

*Source 1: Keep a tight rein on operating expenditure.* Controlling operating expenditure helps generate operating surpluses that can then be used to finance new capital or operating needs. Expenditure is being controlled through two means. The first, is the active prioritisation of expenditure demands, and the second, is requiring ongoing efficiency improvements in government agencies. This approach has been adopted as a key element of the Government's expenditure management strategy since the 2005/6 budget process and has been used in the 2006/7 and 2007/8 budget process and again in the establishment of the aggregate targets that form part of this 2008/9 SPS.

*Source 2: Ensure Public Authorities are Financially Sustainable.* This will involve working with Statutory Authorities and Government Companies – particularly the loss-making ones like Cayman Airways Limited, the Health Services Authority and the Cayman Turtle Farm – to develop financially stable business operations. The ultimate goal in this regard is to achieve an overall break-even position for the public authority sector. Fully achieving this goal will take some time but significant progress is being made towards reforming these entities to be more financially stable.

*Source 3: Undertake New Borrowing.* The Government's third financing strategy is new borrowing. The size of the new infrastructure needs is beyond the ability of the government to finance them from the first two sources. In addition, many of the necessary infrastructure investments (such as new schools, new Government accommodation building and new roads infrastructure) will have long-term benefits for several generations. In these circumstances, it is therefore appropriate for the government to borrow to finance these projects as, not only does this spread the financing costs, it also helps to match the costs and benefits over time.

The Government has established two important rules that are applied when determining the amount of new borrowing: borrowing must be within the limits established by the Principles; and the timing of capital expenditure is to be managed so as to minimise borrowing levels. The Government established these rules to ensure that the total amount of borrowing is maintained within serviceable limits and does not become an excessive burden on future generations of Caymanians. These caveats continue to be an important part of the Government's overall fiscal strategy.

### ***Strategy 3: Economic Management Considerations***

The third element of the Government's fiscal strategy relates to economic management. In determining the level of operating revenues, operating expenses, and capital expenditures, it will consider not only the need to comply with the Principles, and the need to address social and economic infrastructure needs, but also the economic impact these levels will have. In doing so, the Government will give due consideration to the PPM manifesto commitments to support the ongoing economic development of these Islands, particularly the twin pillars of tourism and financial services.



## Aggregate Financial Targets for 2008/9 – 2010/11

### Targets

The aggregate financial targets for the Core Government established by Cabinet for 2008/9 and the subsequent two financial years are provided in Table 4.

**Table 4**  
**Aggregate Financial Targets for Core Government**

Financial Measure	2007/8	2008/9	2009/10	2010/11
	Revised Budget \$000s	Target \$000s	Target \$000s	Target \$000s
<b>Operating Targets</b>				
Operating Revenue	530,717	539,181	552,458	564,689
Operating Expenses	(490,024)	(489,482)	(516,473)	(537,903)
Surplus Before Extraordinary Items	40,693	49,699	35,984	26,786
Extraordinary Items	(4,000)	-	-	-
Surplus (Deficit) After Extraordinary Items	36,693	49,699	35,984	26,786
<b>Balance Sheet Targets</b>				
Borrowing (balance outstanding at year-end)	243,847	374,652	422,818	444,899
Net Worth	536,071	585,742	621,726	648,512
<b>Cash Flow Targets</b>				
Net Operating Cash Flows	63,059	71,305	63,552	55,659
Net Investing Cash Flows	(119,916)	(199,267)	(103,353)	(72,273)
Net Financing Cash Flows	69,751	128,905	48,166	22,081
Net Movement in Cash	12,894	943	8,365	5,467
Closing Cash Balance	114,584	115,527	123,892	129,359

### Basis for the Targets

The targets in this 2008/9 SPS have been derived from a thorough forecasting exercise involving all Ministries and Portfolios. This has allowed the Government forecasts to more accurately reflect the expected financial impact of Government's policy priorities. As part of the forecasting exercise, operating revenues and expenses as well as capital investment forecasts were updated. These forecasts were reviewed to ensure that they are sustainable over the medium term, particularly in relation to capital expenditure and financing, and also that they are consistent with the Principles of financial management.

The Government's longer-term financial projections for the period 2011/12 to 2017/18 were also updated as part of the process of developing the targets (see Section 5). This was to ensure that the three year forecasts are sustainable, particularly in relation to capital expenditure and financing, and also that they are consistent with the Principles of Responsible Financial Management in the short, medium and long term.

### *Explanation of the Targets*

The aggregate targets fall into three groups: operating targets, balance sheet targets and cash flow targets.

#### *Operating Targets*

The operating targets reflect the three main numbers from the operating statement: operating revenue, operating expenses and operating surplus/deficit. The surplus/deficit is the key operating measure.

A healthy operating surplus is targeted throughout the three -year forecast period. These surpluses are consistent with the Government's fiscal strategy outlined above and will be used to fund essential social and economic infrastructure projects contained in the capital program.

#### *The Balance Sheet Targets*

The balance sheet reports the assets and liabilities of the core government and the difference between them is termed "net worth". Net worth can be thought of as the amount the citizens of the Islands have invested in the government and is equivalent to shareholder funds in a company.

The balance sheet targets reflect the two main measures important to measure a government's financial position: borrowings and net worth.

Aggregate borrowing (i.e. the balance outstanding at the end of the period) is targeted to increase over the forecast period. This is consistent with the Government's fiscal strategy (see the fiscal strategy discussion above) and will be used to fund the development of new infrastructure. The borrowing levels targeted comply with the Principles throughout the forecast period. The longer-term projections show that these levels of borrowing are sustainable (see Section 5).

Net worth is targeted to increase steadily over the period. This is consistent with increases in the operating surplus targets over the three years.

#### *Cash Flow Targets*

The cash flow targets relate to the three categories that make up the cash flow statement: operating cash flows (operating receipts and payments), investing cash flows (equity injections and the purchase or construction of assets) and financing cash flows (borrowing).

Net operating cash flows are targeted to remain at healthy positive levels. This reflects the operating surplus targets and is a deliberate fiscal strategy as these cash surpluses will be used to partially finance the Government's capital programme, thereby reducing the borrowing requirement.

In line with the Government's policy priorities, substantial net investing cash flows are targeted throughout the forecast period in order to fund the capital expenditure programme for the next three years, including new schools, a new Government Office Building and improved road infrastructure.

The net financing cash flows reflect the Government's anticipated borrowing programme over the period. This level of financing is consistent with the Government's fiscal strategy outlined above.

The cash position is targeted to be 90 days which reflects the requirement of the PMFL for the Government's cash reserves to be no less than 90 days of executive expenditure in 2008/9, 2009/10, 2011/12 and all subsequent financial years. The targeted closing cash balances for each of the three years satisfy the level of cash reserves required by the Principles of Responsible Financial Management.

## Compliance with Principles of Responsible Financial Management

Table 5 summarises the extent to which the aggregate financial targets comply with the Principles. The table shows that the targets comply with all the Principles in each year of the forecast period.

**Table 5**  
*Compliance with Principles of Responsible Financial Management*

<b>Principle</b>	<b>Degree of Compliance</b>
<p><b>Operating surplus:</b> should be positive</p> <p>(Operating surplus = core government operating revenue – core government operating expenses)</p>	<p><b>Complies in all years</b></p> <p>2008/9 : \$49.699 million 2009/10 : \$35.984 million 2010/11 : \$26.786 million</p>
<p><b>Net Worth:</b> should be positive</p> <p>(Net worth = core government assets – core government liabilities)</p>	<p><b>Complies in all years</b></p> <p>2008/9 : \$585.742 million 2009/10 : \$621.726 million 2009/11 : \$648.512 million</p>
<p><b>Borrowing:</b> Debt servicing cost for the year should be no more than 10% of core government revenue</p> <p>(Debt servicing = interest + other debt servicing expenses + principal repayments for core government debt and self financing loans)</p>	<p><b>Complies in all years</b></p> <p>2008/9 : 7.9% 2009/10 : 8.7% 2010/11 : 9.0%</p>
<p><b>Net Debt:</b> should be no more than 80% of core government revenue</p> <p>(Net debt = outstanding balance of core government debt + outstanding balance of self financing loan balance + weighted outstanding balance of statutory authority/government company guaranteed debt - core government liquid assets)</p>	<p><b>Complies in all years</b></p> <p>2008/9 : 68.8% 2009/10 : 74.4% 2010/11 : 75.7%</p>
<p><b>Cash Reserves:</b> should be no less than estimated executive expenses for:</p> <ul style="list-style-type: none"> <li>• 90 days in 2008/9</li> <li>• 90 days in 2009/10</li> <li>• 90 days in 2010/11</li> </ul> <p>(Cash reserves = core government cash and other liquid assets)</p>	<p><b>Complies in all years</b></p> <p>2008/9 : 90 days 2009/10 : 90 days 2010/11 : 90 days</p>
<p><b>Financial risks:</b> should be managed prudently so as to minimise risk</p>	<p><b>Complies in all years</b></p> <ul style="list-style-type: none"> <li>• Insurance cover exists for key assets and major potential liabilities.</li> <li>• Hurricane preparedness strategy in place</li> </ul>

## **5. Longer-Term Financial Projections**

### **Introduction**

The Government has developed a set of longer-term financial projections to help guide the setting of the three year fiscal targets and assessing their impact over the long term.

### **Projections are not Forecasts**

It is important to note that projections are not forecasts. There are many uncertainties involved in projecting over a longer-term period and these uncertainties are too great to be able to prepare robust forecasts of likely financial activity. However, it is possible to project future revenues, expenditure, balance sheet activity etc. on the basis of actual activity to date, the three-year forecasts/targets, current government policy, and assumptions as to future economic factors. The longer-term projections have been prepared on this basis.

With this type of long term projections there is an increase in the probability of variance of a result over time therefore, the value in such projections is not in the precise result but rather in the trend that they indicate. For example, projections that show a declining surplus over time would be an indication of an unsustainable financial position.

### **Projections Assumptions**

The projections have been prepared on the basis of the following assumptions:

- Revenue grows at 2.5 % per annum during the projection period and this results from economic factors rather than new revenue measures. This rate is less than the projected long-run GDP growth forecasts of 2.8% p.a.;
- Operating expenditure grows at 3.0% per annum during the projection period;
- Government continues to finance its borrowings at current rates and terms;
- Current government policies, including existing levels of economic and social support; and
- No external shocks to the Cayman economy.

**Table 6**  
*Longer-Term Projections*

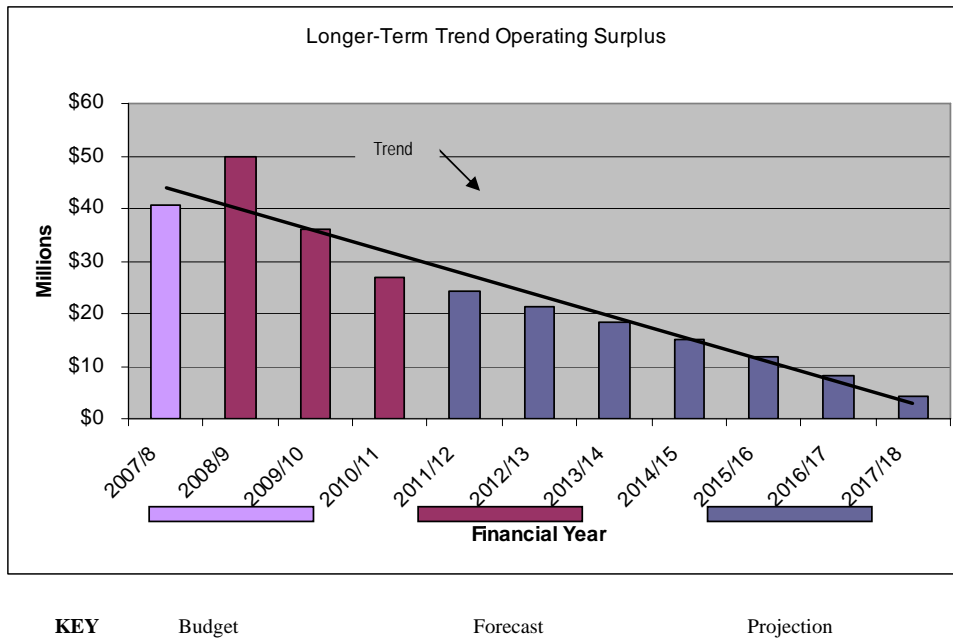
Fiscal Measure (Millions)	2007/8	2008/9	2009/10	2010/11	2011/12	2012/13	2013/14	2014/15	2015/16	2016/17	2017/18
	Revised Budget	Target	Target	Target	Projection	Projection	Projection	Projection	Projection	Projection	Projection
Operating Surplus	40.693	49.699	35.984	26.786	24.183	21.370	18.385	15.184	11.765	8.084	4.182
Net Worth	536.071	585.770	621.755	648.541	672.724	694.094	712.479	727.663	739.428	747.511	751.693
Executive Capital Investment Expenditure	140.661	197.014	101.113	70.139	64.000	63.000	62.000	61.000	60.000	59.000	58.000
New Borrowing (during the fiscal year)	88.900	154.100	76.600	52.000	48.000	51.000	53.000	56.000	59.000	63.000	66.000
Borrowing (balance outstanding at year-end)	243.847	374.652	422.818	444.899	461.840	480.525	499.907	520.878	543.339	568.133	594.175
Cash Balance	114.584	115.527	123.892	129.359	133.223	137.909	142.226	146.878	151.575	156.928	161.662

**Overview of the Projections**

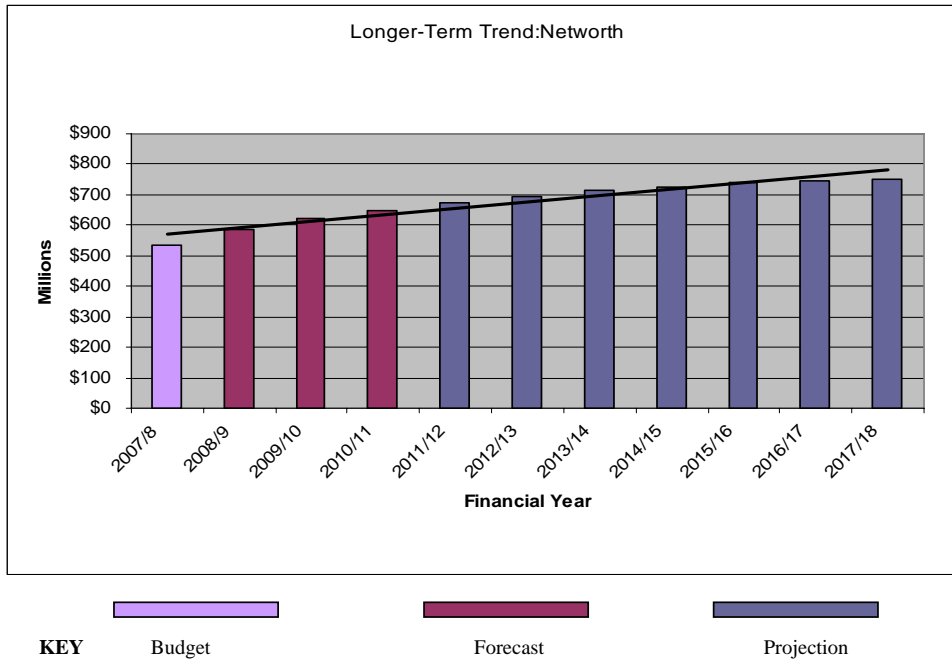
Table 6 and Figures 4 to 12 provide the financial projections for the periods 2007/8 to 2017/18. In summary the projections show:

- Net surplus position in each of the projected fiscal years. These projections are conservative in nature and assume moderate growth to revenue over the period along with continued prudent controls over operating expenditures.
- There is also a steady increase in the Government’s projected net worth position. This is reflective of the continued surplus position being forecasted and is a positive indicator of the financial health of the Government (see Figure 4).
- The Government intends to borrow \$282.7 million over the next 3 financial years in order to finance its planned capital programme (see Figure 7). This borrowing is affordable over the medium and long term as our financial position is projected to remain fully compliant with the Principles of Responsible Financial Management throughout that period. Looking further ahead, the projections allow for an average annual capital budget of \$61 million for 20011/12 to 2017/18 which will be financed by an average borrowing of \$56.6 million per year.
- Cash reserves will grow in tandem with the operating expenditures allowing the Government to always maintain a minimum of 90 days of executive expenditures at the end of each financial year as required under the Public Management and Finance Law (2005 revision).

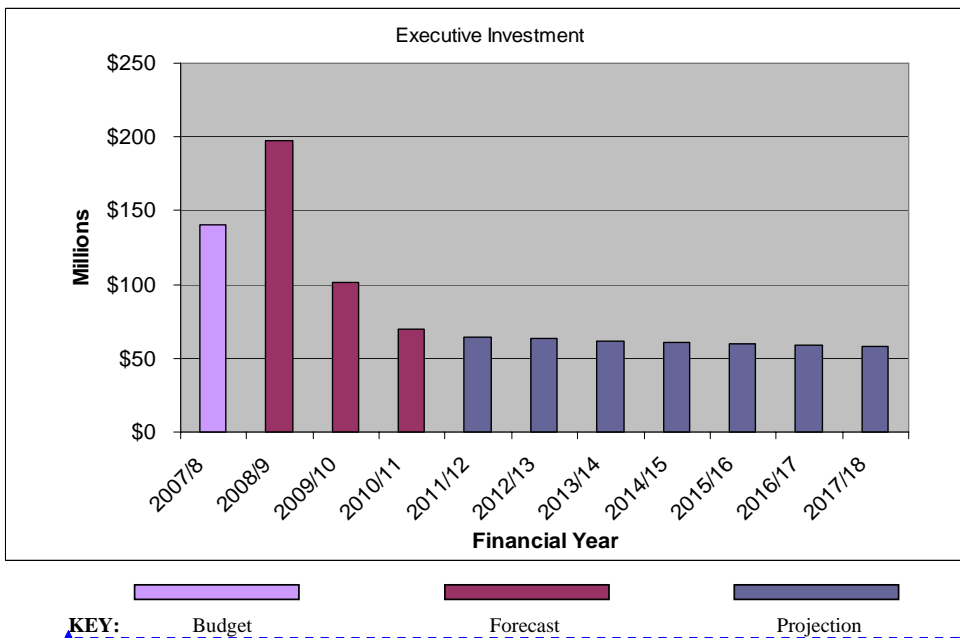
**Figure 4**  
**Longer-Term Trend: Operating Surplus**



**Figure 5**  
**Longer-Term Trend: Net Worth**



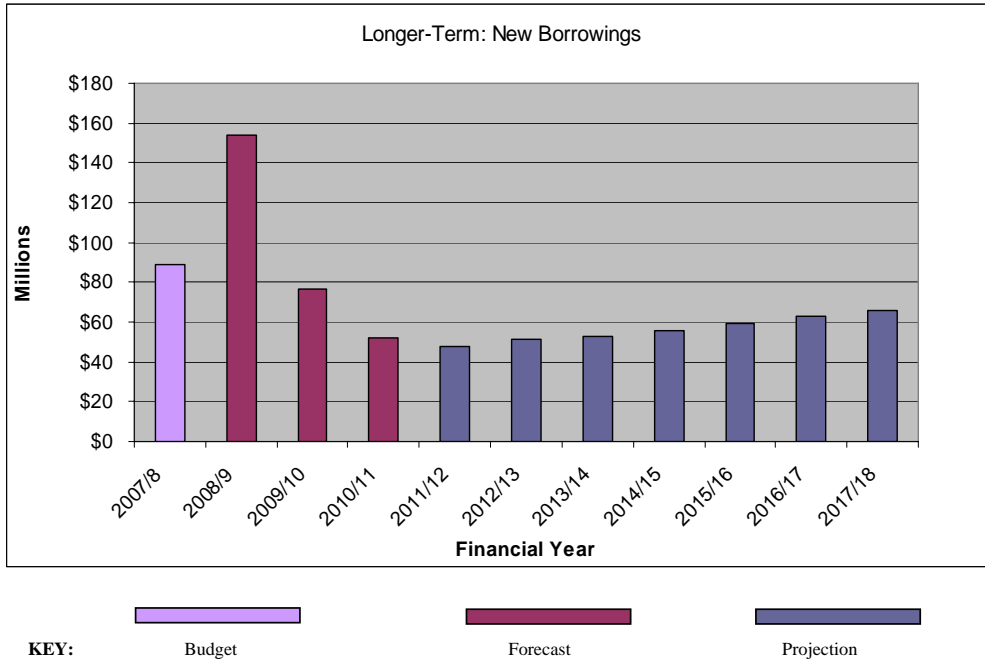
**Figure 6**  
**Longer-Term Trend: Executive Capital Investment Expenditure**



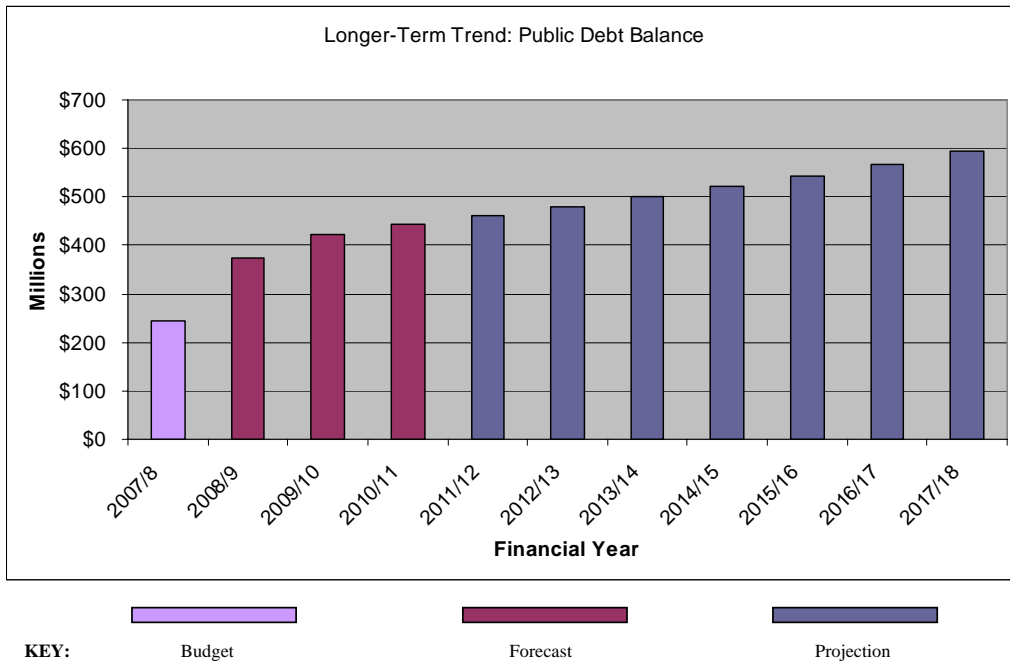
**KEY:** Budget Forecast Projection

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**Figure 7**  
**Longer-Term Trend: New Borrowing**

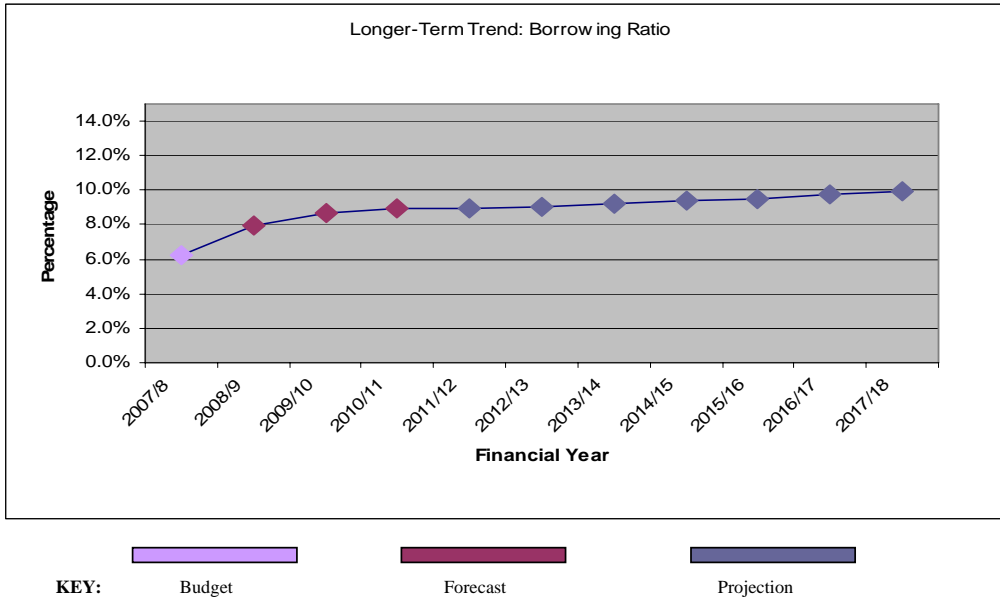


**Figure 8**  
**Longer-Term Trend: Public Debt Balance**

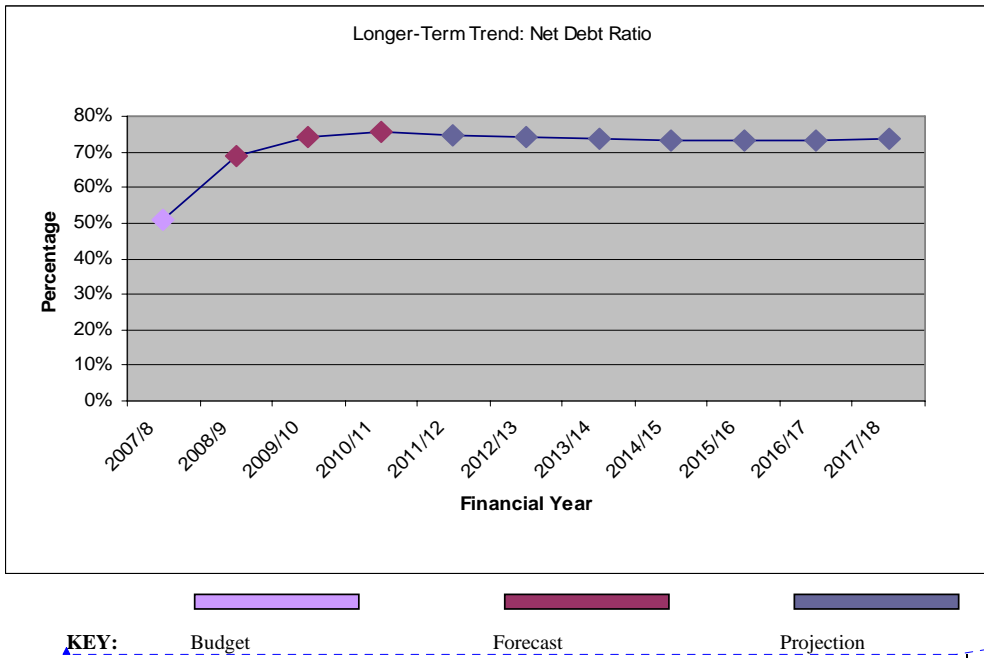




**Figure 9**  
**Longer-Term Trend: Borrowing Ratio**

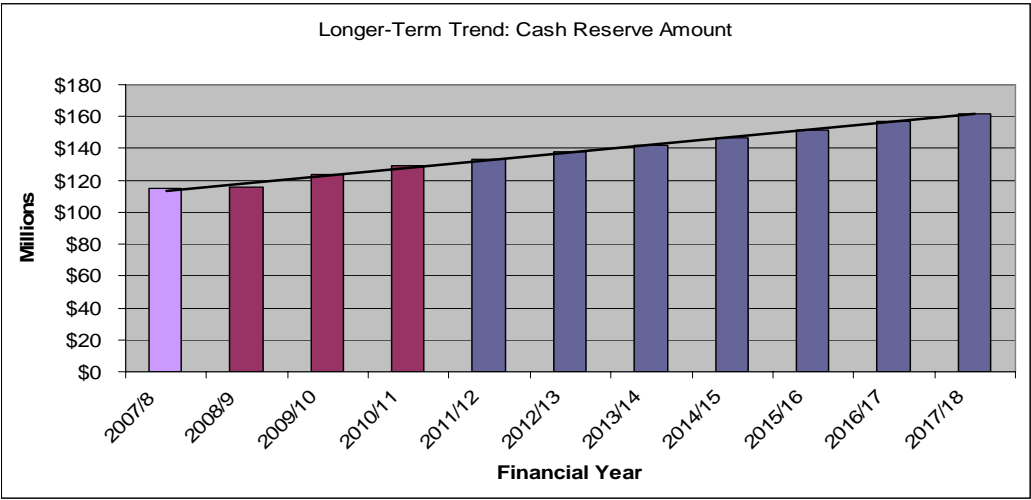


**Figure 10**  
**Longer-Term Trend: Net Debt Ratio**



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**Figure 11**  
**Longer-Term Trend: Cash Reserves Amount**



**KEY:**



Budget



Forecast



Projection

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## 6. Financial Allocations

### Introduction

In accordance with the requirements of the PMFL this section specifies the indicative financial allocations to individual members of Cabinet for the 2008/9 Budget. These allocations are used as the basis for Ministers and Official Members and their Ministries/Portfolios to establish their outputs and detailed budgets for the 2008/9 financial year.

### Operating Allocations

The aggregate financial targets set out in Section 4 establish the operating limits for the core government for the 2008/9 financial year. These include the total operating expenses for the forecast year.

Operating expenses are made up of two broad categories of expenses:

- Expenses of ministries and portfolios which are funded by revenue earned by them from sources other than Cabinet; and
- Executive expenses, being expenses incurred by the Cabinet in funding the outputs they are purchasing from ministries, portfolios, statutory authorities, government companies and non-governmental output suppliers, the cost of transfer payments and various other miscellaneous executive expense items.

Although the overall level of Government expenses is important for the financial management of the government as a whole, executive expenses are the focus of budget allocations. This is because executive expenses represent the amount Cabinet has to spend on buying outputs or funding other interventions.

Table 7 provides the indicative allocations of executive operating expenses to each Minister or Official Member for the forecast period. These allocations represent the amount available for each Minister or Official Member to purchase outputs from their ministries, statutory authorities and government companies, and other third parties (Non-Governmental Output Suppliers) and to fund transfer payments or other executive operating expenses for which the member of Cabinet is responsible.

### Capital Allocations

The aggregate financial targets set out in Section 4 also establish a limit for capital expenditure.

As with operating expenditures, this target is comprised of two amounts:

- Investing cash flows (asset purchases) funded by ministries and portfolios from their own resources, namely the cash generated from the inclusion of depreciation in their output prices; and
- Executive investing cash flows, being the investing cash flows controlled directly by Cabinet.

The executive investing cash flow is the focus of the budget allocations because it represents the amount that Cabinet has at its disposal limit to spend on capital.

Table 8 provides the indicative capital (or investment) allocations to each Minister or Official Member for the forecast period. This allocation can be used to fund one of three capital items: equity investments into ministries, portfolios, statutory authorities and government companies; acquisition or replacement of executive assets; or loans-made.

**Table 7**  
**Executive Operating Expenditure Allocations**

<b>Cabinet Member</b>	<b>2008/9 \$000</b>	<b>2009/10 \$000</b>	<b>2010/11 \$000</b>
Chief Secretary	76,751	79,260	81,845
Head of the Civil Service	13,043	14,045	15,287
Attorney General	8,421	8,720	9,028
Financial Secretary	73,993	89,449	98,327
Leader of Government Business	7,105	7,719	8,376
Minister of District Administration, Planning, Agriculture and Housing	33,750	34,883	35,895
Minister of Communications, Works and Infrastructure	18,545	19,161	19,797
Minister of Health and Human Services	71,370	73,724	76,705
Minister of Education, Training, Employment, Youth, Sports and Culture	93,801	110,333	113,710
Minister of Tourism, Environment, Investment and Commerce	61,048	63,650	66,432
Public Accounts Committee (Audit Office)	750	875	881
Oversight Committee of the Legislative Assembly (Complaints Commissioner)	985	1,017	1,050
Attorney General for Chief Justice (Judicial Administration)	9,474	10,098	10,759
<b>Total Executive Operating Expenditure Allocations</b>	<b>469,036</b>	<b>512,934</b>	<b>538,092</b>

**Table 8**  
**Executive Investment Allocations**

<b>Cabinet Member</b>	<b>2008/9 \$000</b>	<b>2009/10 \$000</b>	<b>2010/11 \$000</b>
Chief Secretary	19,656	7,125	4,125
Head of the Civil Service	300	0	0
Attorney General	120	120	120
Financial Secretary	4,326	3,034	2,765
Leader of Government Business	1,500	740	440
Minister of District Administration, Planning, Agriculture and Housing	33,686	26,705	23,605
Minister of Communications, Works and Infrastructure	24,328	13,872	21,502
Minister of Health and Human Services	13,714	8,655	6,393
Minister of Education, Training, Employment, Youth, Sports and Culture	85,600	33,800	7,000
Minister of Tourism, Environment, Investment and Commerce	9,784	2,602	2,520
Public Accounts Committee (Audit Office)	0	0	0
Oversight Committee of the Legislative Assembly (Complaints Commissioner)	0	0	0
Attorney General for Chief Justice (Judicial Administration)	4,000	4,460	2,170
<b>Total Executive Investment Allocations</b>	<b>197,014</b>	<b>101,113</b>	<b>70,640</b>

## 7. Conclusion

This Strategic Policy Statement establishes the policy and financial framework on which the 2008/9 budget will be prepared.

The policy goals and financial parameters outlined in this document clearly reflect a continuation of the policies established by the PPM Government. Those policies are based around eleven broad outcomes which include: supporting the economy; improving education and training; strengthening the family and community; addressing traffic congestion; and embracing Cayman Brac and Little Cayman.

The financial targets set out in this SPS allow for the funding of various interventions to progress the key policy initiatives relating to these outcomes. Particularly the targets provide for delivery of a capital development programme which includes additional schools, new Government Office Accommodation, enhanced Public Safety and disaster response capabilities, continued improvement to the country's road network infrastructure and other significant assets. This capital programme will be funded by a combination of operating surplus and borrowings over the three year forecast period.

At the same time the financial targets reflect the Government's fiscal strategy: be fiscally responsible; acquire the resources necessary to address the country's social and economic infrastructure needs; and support the ongoing economic development of the country. Updated long-run fiscal projections continue to show that the targets are sustainable beyond the forecast period and therefore remain affordable.

This Strategic Policy Statement shows that the Government remains focussed and committed to delivering on its manifesto commitments. It shows that the Government is continuing with the policy direction it has established since coming into office, and it shows that the Government is continuing to manage the country's finances diligently, responsibly and transparently.

**Hon. D. Kurt Tibbetts, JP**  
**Leader of Government Business**

29th November, 2007