



Government of the Cayman Islands

MEDIUM TERM FISCAL STRATEGY: 2013 - 2017

15 August 2013

Foreword

The Government of the Cayman Islands (the "Government") is of the firm view that the Cayman Islands' economy has shown a high degree of resilience to rebound from the effects of the 2008 global recession. Overnight tourist arrivals have shown steady growth, cruise tourism is poised for growth, and the construction sector is showing signs of recovery. Our financial services industry, which remains a key pillar of our economy, also continues to grow providing employment opportunities for Caymanians as well as stable Government revenues.

Notwithstanding lingering uncertainties in the global economy, and despite certain policy actions by the previous Administration which could be considered less than helpful, the Cayman Islands remain on a positive economic trajectory. The current position requires careful management and sound policies to prevent economic shocks which could be damaging to future progress.

Compliance with the Public Management and Finance Law will require a contraction in Public Sector spending over the short to medium term. The Government must therefore increasingly refocus its efforts towards facilitating economic growth by promoting a climate that allows the private sector to flourish.

To grow, the private sector requires access to the best talent, and the Government must assist by providing Caymanians with access to higher education and training. The Government must also encourage continued investment and restoration of investor confidence through open, honest, fair and transparent governance and the avoidance of restrictive tax measures.

On 2nd August 2013, Ministers and Members of the Cabinet held a high level strategic meeting with senior management in the Civil Service. This meeting discussed a financial framework which will allow the Government to comply with the fiscal responsibility requirements of the *Public Management and Finance (Amendment) Law 2012*. In summary, participants were advised of Government's intended policy actions to:

- Decrease expenditures, reduce debt, and improve cash balances;
- Support the private sector as the engine for economic growth;
- Implement economic and social policies more efficiently;
- Enhance the living conditions of poor communities by more effective means; and
- Improve the immigration system based on lessons learned from the recent past.

The message was well received with the Elected Government and the Civil Service sharing a commitment to work hand in hand to achieve what is required for the Country to prosper.

On 14th August 2013, a similar meeting was held with Statutory Authorities and Government owned companies. The meeting yielded several positive results with ideas shared for various cost saving initiatives and opportunities for greater synergies among the wider Public Sector.

This document further details those Plans and covers the current Administration's term in Office. It updates the state of the Cayman Islands economy, highlights the challenges the Islands face, and outlines Government's commitment in meeting those challenges.

The Government holds steadfast to the view that severe austerity measures will not be the prescription that restores the Country's financial health. Flexibility must be allowed to enable the Government to address its domestic affairs through policies and strategies that are harmonious to our unique set of circumstances as a small-island economy.

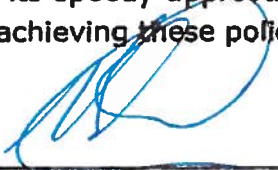
The people of the Cayman Islands have shown tremendous resilience during the recent difficult economic times. Where others have faltered, we have held steadfast. Our debt is declining; our credit ratings has been reconfirmed; revenues are growing; expenditures are reducing, and we are producing Surplus budgets; and growing cash reserves.

It shows that, if provided with the required flexibility to manage its affairs, the Government can be successful and achieve its objectives.

This Government is committed to sound fiscal management and good governance. It is committed to the rule of law; and to the continued restoration of public finances to sustainable levels.

This medium term fiscal strategy outlines a robust set of Plans to achieve these objectives. They are sufficiently aggressive to meet the fiscal targets yet moderately weighted to account for future potential risks.

I now therefore commend this document to the United Kingdom's Government and ask for its speedy approval to enable our Government to immediately get to work on achieving these policy objectives.



Hon. Marco Archer
Minister for Finance & Economic Development
15th August 2013

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1.

BACKGROUND

On the 23rd November 2011 the Cayman Islands Government signed a Framework for Fiscal Responsibility (the "FFR") agreement with the United Kingdom. The FFR was subsequently incorporated into the Public Management and Finance Law (the "PMFL") on the 15th November 2012. The overarching objective of the FFR is to promote prudent fiscal management by enforcing adherence to six Principles of Responsible Financial Management. These Principles are:

- Operating Surplus should be positive;
- Net-Worth should be positive;
- Debt Servicing costs should not exceed 10% of core Government's revenue;
- Net Debt ratio should not exceed 80% of core Government revenue;
- Liquid-Assets should be sufficient to meet 25% (or 90 days) of estimated executive expenses at Government's lowest cash point during its fiscal year; and
- Financial Risks should be managed prudently.

Due to existing global financial conditions, the Government could not immediately comply with all six Principles at the time they were established. The amendment to the PMFL therefore established a target compliance date of 30th June 2016 when all six Principles must be met.

The 2012-13 Budget was the first budget prepared in the context of the FFR. **Table 1** on the next page shows the actual (but unaudited) operating performance relative to that Budget. It shows that whilst policy decisions were made not to pursue certain planned Revenue Measures (which were considered potentially harmful), measures were also taken to reduce operating expenditures.

When those expenditure reductions are added to the reduced capital spend, as shown in **Table 2**, the result is a mere \$2.5 million variance from the closing cash target established in the original 2012/13 Budget.

The cash target is the most important measure, for it is the aspect that is carried forward to future years to enable compliance with the Net Debt and Cash Reserve requirements in 2015-16.

Based on the \$2.5 million cash underperformance in Year 1 (or 2012/13), the Government now proposes to reduce the planned operating expenditures for Year 2 (or 2013/14) shown in the original 3-year Plan by \$3.0 million. This allows the Government to remain within the fiscal frame that was first agreed.

Table 1 2012-13 Estimated Performance Relative to Budget

CAYMAN ISLANDS GOVERNMENT SUMMARY STATEMENT OF FINANCIAL PERFORMANCE <i>All figures stated in 000s and in CI Dollars</i>			
	2012/2013	2012/2013	
	Preliminary Actual	Initial Full Year Budget	Variance
<u>Operating Revenues</u>			
Coercive Revenue	559,168	590,559	(31,391)
Sales of Goods & Services	58,390	58,682	(292)
Investment Revenue	303	213	90
Donations	407	-	407
Extraordinary Revenues	-	-	-
Other Revenue	136	-	136
Total Operating Revenue	618,404	649,454	(31,050)
<u>Operating Costs</u>			
Personnel Costs (includes Salaries, Wages, Health-Care Costs and "normal" Pension Expense)	221,623	233,985	-12,362
Past Service Pension Expense	16,888	16,900	(12)
Total Personnel Costs	238,511	250,885	12,374
Supplies and Consumables	78,383	87,773	9,390
Leases	7,168	7,511	343
Depreciation	25,013	25,006	(7)
Litigation Costs	1,134	454	(680)
Outputs from Public Authorities	114,445	108,460	(5,985)
Outputs from Non-Governmental Organizations	24,712	18,955	(5,757)
Transfer Payments	31,403	32,816	1,413
Other Operating Expenses	4,187	4,359	172
Financing Expense	33,187	32,841	(346)
Sub-total : Operating Expenses of Core Government	558,143	569,060	10,917
Operating Expenses of Core Government	558,143	569,060	10,917
(Gains)/losses on foreign exchange transactions	(1,920)	17	1,937
(Gains)/losses on non-financial instruments	(22)	-	22
Total Net Operating Expenses of Core Government (Accruals-based Amounts)	556,202	569,077	12,875
Net Surplus/(Deficit) of Core Government	62,203	80,377	(18,174)
Surplus/(Deficit) of Statutory Authorities and Government Owned Companies	1,658	1,875	(217)
Net Surplus/(Deficit) of Entire Public Sector	63,861	82,252	(18,391)

Table 2 - 2012-13 Capital Transactions and Cash Balances

CAYMAN ISLANDS GOVERNMENT SUMMARY STATEMENT OF FINANCIAL PERFORMANCE <i>All figures stated in 000s and in CI Dollars</i>			
	2012/2013	2012/2013	
	Preliminary Actual	Initial Full Year Budget	Variance
Total Net Operating Expenses of Core Government (Accruals-based Amounts) - as shown previously	556,202	569,077	12,875
Capital Transactions			
Equity Investments (in Gov't Ministries, Portfolios and Offices, and to Statutory Authorities and Gov't Companies)	40,872	43,528	2,656
Executive Assets (e.g. road development, payment for land purchases and construction of buildings)	7,782	13,975	6,193
Total for Capital Transactions (Accruals-based Amounts)	48,654	57,503	8,849
Total of: Net Operating Expenses and Capital Transactions (Accruals-based Amounts)	604,855	626,580	21,725
Cash Balances			
Operating Cash Balances	20,665	22,278	(1,613)
Restricted Cash Balances	96,605	97,442	(837)
Total Cash Balances	117,270	119,720	(2,450)
Borrowing Balance at end of each year	573,050	573,358	(408)

2.

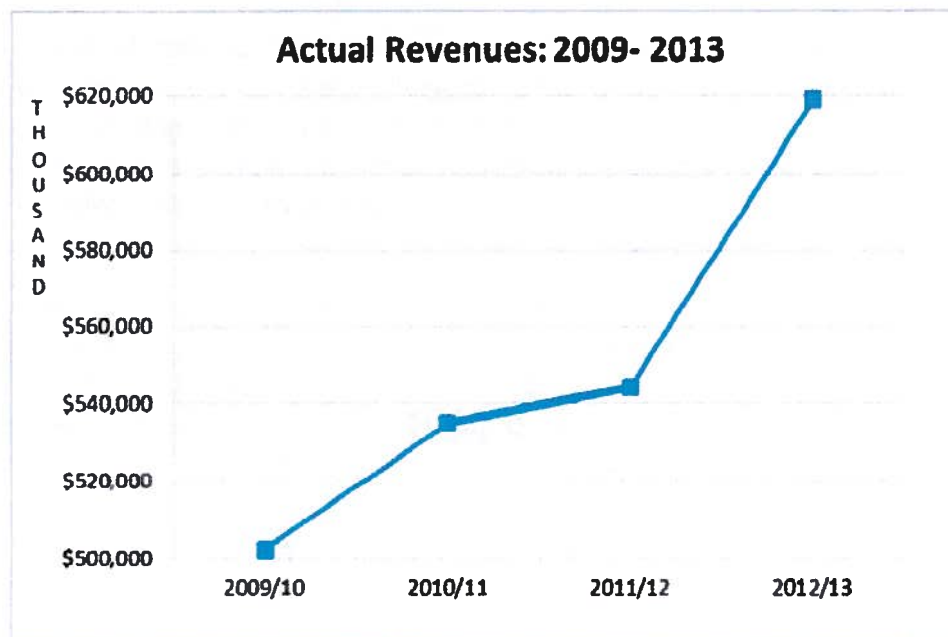
RECENT FISCAL PERFORMANCE

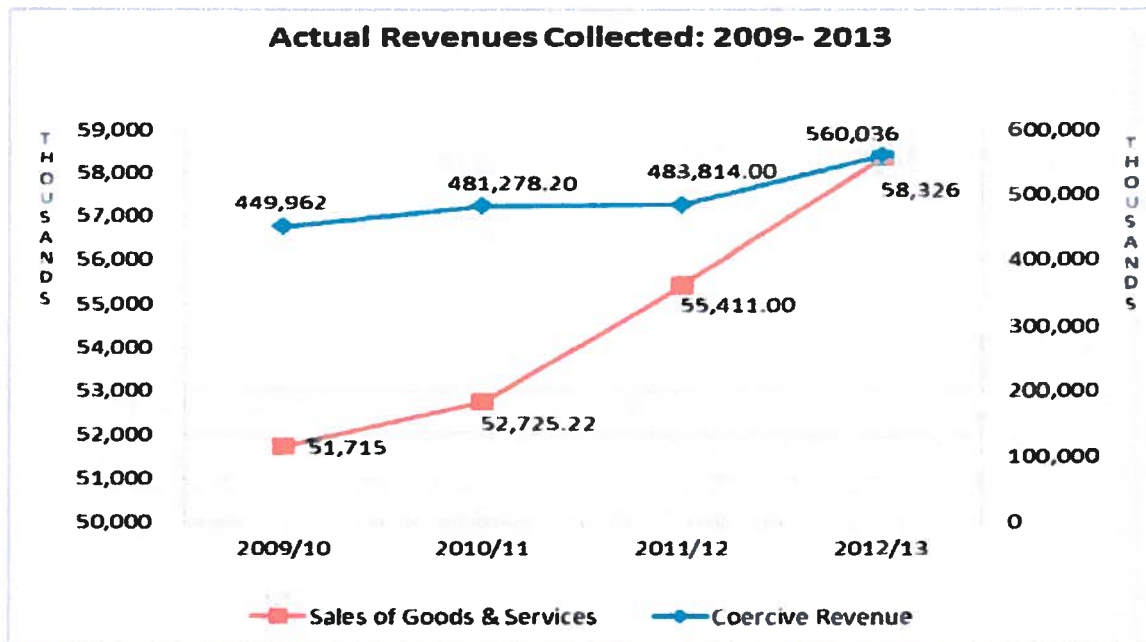
In brief

- Recent performance shows the ability of the economy to generate additional revenue; and
- Whilst revenue grew by 24% over the past 4 years, the expected (revenue) growth for the 2013/14 fiscal year is set at a modest 3.5%.

Revenues

Since 2009, Government revenue has shown tremendous growth. Total revenue grew by 24% between 2009 and 2013. This increase resulted from new measures and growth in the local economy.





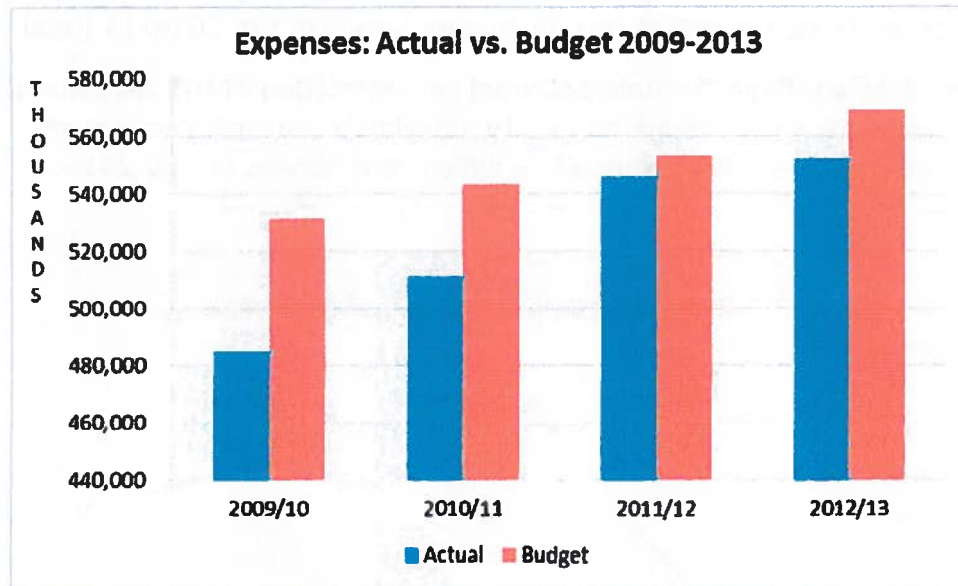
The 2013/14 fiscal year is expected to generate revenues of \$640 million, compared to \$619 million earned in the 2012/13 fiscal year. This represents a very modest growth expectation of 3.5% and includes a single new Revenue Measure for Directorship fees which is being budgeted at \$6.0 million.

The Directorship fee was deferred from the 2012/13 Budget to allow further industry consultation. Now that those consultations have been concluded, the Government feels comfortable introducing this Measure which is expected to generate approximately \$8.0 million per annum. However, a risk weighting of 25% was applied (in line with previous directives from the FCO) which reduces the budgeted amount to \$6.0 million in 2013/14.

With the exception of the single measure discussed above, all other revenue changes result from either the full year impact of measures implemented after the start of the 2012-13 fiscal year, or through natural growth in existing revenue streams. It should also be noted that the projections were adjusted to remove "outliers" (such as the Stamp Duty from the sale of a major hotel) in 2012/13 fiscal year's performance.

Expenses

Overall expenses have been below budget in each of the four fiscal years as shown below. Traditionally, the largest areas for under expenditure have been in personnel costs.



Whilst the Civil Service has been effective in keeping costs down - quite often the overspent areas related to policy. These included purchase of outputs from Non-Government Output Suppliers, Transfer Payments and Support to Statutory Authorities and Government Owned Companies.

The Progressives intend to do its part going forward in ensuring that the policy measures taken do not reduce or cancel the efforts of the Public Service in reducing overall costs. That means that policies will be equitable, transparent and properly managed to remain within levels the Country can afford.

Debt

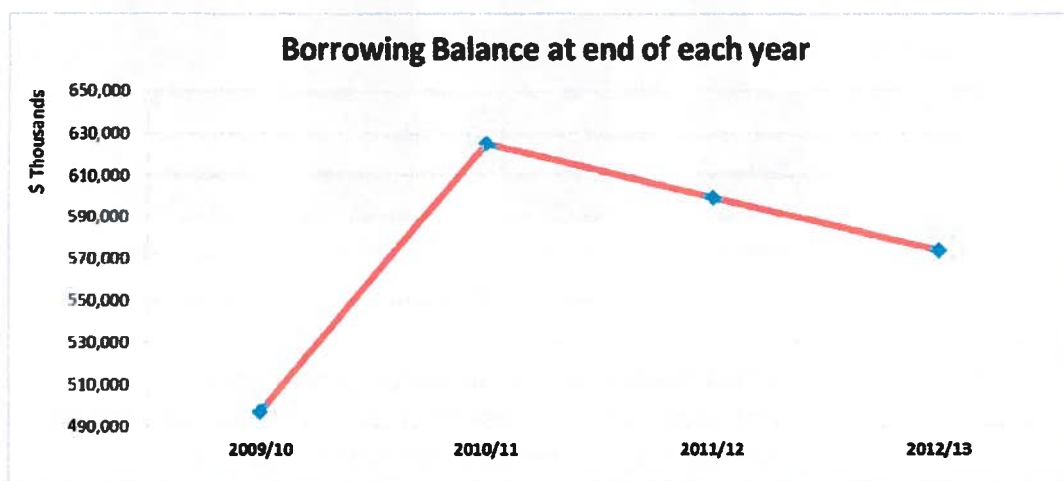
The Cayman Islands Government has met and will continue to meet all its debt servicing obligations. As the graph on the next page shows, Core Government debt peaked at approximately \$625 million at the end of 2011 and has been declining thereafter. The Government proposes, at a minimum, to further reduce Core Government debt by approximately \$71.2 million before the end of June 2016.

The Government is cognizant of the US\$312 million bond which matures in 2019 and acknowledges the limited scope for retirement upon maturity.

Therefore, the Government will explore opportunities to renegotiate the terms of that bond with a view to potentially place half the existing principal on a amortizing program while setting aside funds to retire the remaining half on maturity.

Opportunities are also being explored among the wider public sector for potential early retirement of certain smaller bonds in the 2014/15 fiscal year.

Further debt strategies include potential re-negotiation of the repayment terms associated with an existing loan facility carrying a principal repayment obligation of \$15.4 million annually – which commences in July 2016.



3.

THE ECONOMIC CONTEXT

In brief

- Gross Domestic Product (GDP) is projected to increase by 2.0% for calendar year 2013, and 2.6% for calendar year 2014.
- Inflation is projected at 2.1% for calendar year 2013, and 2.2% for calendar year 2014.
- Unemployment is projected at 6.0% by end of calendar year 2013, and 5.8% by end of calendar year 2014.

GDP Growth

For the calendar year ended 2012, the local economy grew by 1.6%. The key sectors showing recovery were:

- Construction;
- Wholesale and retail trade;
- Hotels and restaurants;
- Financial and insurance services (New Partnership, insurance licences and stock exchange listings);
- Transport; and
- Storage and communication services.

Real GDP growth, whilst modest, is poised to continue in the short run, with projections showing a 2.6% increase by the end of calendar year 2014. This expansion is expected from private sector stimuli via construction projects such as Cayman Narayana University Medical Center and Cayman Enterprise City.

This will be aided by the commencement of certain Public Sector projects such as the redevelopment of the Owen Roberts Airport, and potential construction of a modern Cruise Berthing Facility.

The Cayman Islands' economy is most impacted by performance in the United States economy. For 2014, the U.S. Congressional Budget Office expects GDP growth of 3.4% and for the economy to grow at an average rate of 3.6% thereafter until 2018.

Inflation

The average inflation rate in 2012 was 1.2%. This is a direct result of higher prices in clothing and footwear, food and non-alcoholic beverages, and alcohol and tobacco.

The gradual economic recovery in the rest of the world is currently leading to higher food and fuel prices. As such, inflation in 2013 is expected to rise to 2.1% due to those increases along with greater demand for construction materials.

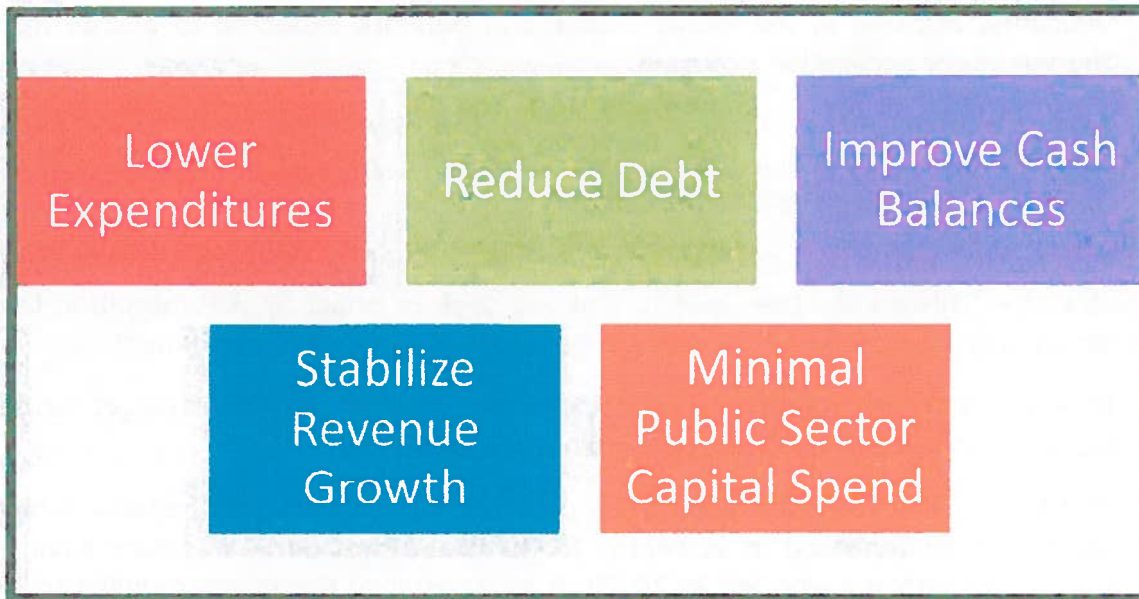
Balance of Payments

By the end of 2012, the Country's Current Account Deficit was estimated to have narrowed by 2.5% to \$467.0 million (or 18.1% of GDP). This is mainly due to an increased inflow of funds through higher visitor expenditure. Also, workers remittances were marginally higher as foreign employment increased.

The Current Account Deficit is forecasted to increase to over 19% of GDP throughout 2014, based on the premise that outflows (such as imports of goods for the new private sector projects), will outperform inflows (primarily financial and tourism receipts).

4.

FISCAL STRATEGY



Lower Expenditures:

The Government proposes to cut a total of \$22.5 million (or 4%) in annual Operating Expenditures over the 2013/14 and 2014/15 fiscal years. In 2015/16, the Government proposes a less than 1% increase in Operating Expenditures.

It is not realistic to expect that Operating Expenditures in the Public Sector can continue to decrease in perpetuity – as inflation is expected to continue over the medium term and Public Sector staff are paid at 2007 salary levels.

Personnel Costs- Estimated Personnel costs for the 2012/13 fiscal year are \$238.5 million. This amount includes approximately \$16.9 million in Past Service Pension Liability payments.

In line with the 2009 Constitution, Members in the Legislative Assembly increased from 15 to 18 following the May 2013 General Elections. This will add approximately \$1.0 million in Personnel costs to the 2013/14 budget. The additional cost comes from salaries, healthcare, pension, and the need for personal assistants for additional Ministers.

The Government also plans to introduce a voluntary separation program which requires funding of approximately \$1.2 million. Those two factors would effectively add approximately \$2.2 million in Personnel Costs to the level incurred in the 2012/13 fiscal year; however, the Government proposes to fund those increases from efficiencies and seek to reduce overall Personnel Costs a further \$1.0 million below the 2012/13 estimated actual.

These savings will be achieved through more effective management of overtime, attrition in the Public Sector and benefits expected to accrue from the voluntary separation program.

Since the start of the 2013/14 fiscal year, the Government has issued policy Instructions which require that there be no net growth in Personnel Costs during the period of the interim budget.

Moving forward, the Government will implement a "managed vacancies" strategy. This means the Government will seek to enact an Appropriation Law which only funds 99% of the current positions in the Core Government.

As attrition occurs, managers will have to first meet their savings target for net personnel reduction before replacements are approved.

In addition, the voluntary separation program will be a one-off expense which would not be repeated in 2014/15. In 2014/15, the full year salary savings from those persons who left in 2013/14 as a result of the program will also be realized.

Supplies and Consumables – Estimated Supplies and Consumables costs for 2012/13 is \$85.5 million (inclusive of leases).

Included in this sum are: Electricity, \$9.6 million; Insurances, \$8.0 million; Leases, \$7.2 million; Advertising, \$6.2 million; Professional Fees, \$4.1 million; Transportation, \$3.2 million; Vehicle Fuel, \$2.7 million; Telephone charges, \$2.6 million; Security Services, \$2.4 million; Janitorial, \$2.2 million; Building maintenance, \$2.0 million; Official Travel, \$1.8 million; Insecticides, \$1.7 million; Marketing services, \$1.7 million; paper, printing and other office supplies, \$1.3 million; spare parts, \$1.2 million; and freight and shipping, \$1.2 million.

To support the development of a business case for a modern Cruise Berthing Facility, the Government is expected to spend approximately \$2.0 million in professional fees, during 2013/14, for independent advice as required by the amended PMFL.

The Government proposes to fund this increase and increases for other policy measures through efficiency gains and to further reduce Supplies and

Consumables by a net of \$3.0 million in the 2013/14. This would be a 3.5% decrease from the 2012/13 actual expenditure level for this category.

Opportunities to effect this reduction will be most prevalent in official travel, professional fees, electricity, advertising, leases, and the provision of certain services such as janitorial and security.

Outputs from Statutory Authorities – The Government believes that active management is necessary for the entire Public Sector and not just the Core Government. In this regard, the Government will be seeking opportunities to reduce the level of output/subsidy to Statutory Authorities and Government Owned Companies, as well as mandating efficiency gains in their operations.

The Government met with the Agencies representing the largest expenditures in the wider Public Sector on 14th August 2013 and outlined its policies for improved performance. These policies include furthering opportunities for third party revenues and more comprehensive management of certain Public Sector Costs such as healthcare.

The Government will seek to transfer certain Public Sector risks to the Agency best able to manage those risks. In recent years, the Government has encountered significant volatility in the cost of sending indigents overseas for tertiary care at various health facilities. Working with CINICO, the Government will now seek to insure this group of individuals at a predefined premium rate which will add greater certainty to the budget process and reduce the amount actually incurred in 2012/13.

Finally, the Government will seek to first rationalise certain Statutory Authorities and Government Owned Companies and then seek to establish shared back office functions (such as accounting, HR, IT, and secretarial).

Non-Government Output Suppliers – This area of expenditure is estimated at \$24.7 million for the 2012/13 fiscal year. Principal Items Include: Medical care at various overseas institutions for indigents, \$14.3 million; Legal Aid services, \$2.3 million; Rental Assistance payments, \$1.6 million; Private Schools subsidy, \$1.5 million; and the local care of indigent and disabled persons, \$1.3 million.

With the introduction of the Children's Law and the Bill of Rights, the Judicial Administration estimates that Legal Aid will be as high as \$3.0 million for the 2013/14 fiscal year, which would otherwise increase the costs in this category.

The provision of healthcare cost incurred by the Government is approximately \$100 million per annum. As part of a wider strategy, the Government intends to better leverage this healthcare buying power to affect a \$2.5 million

decrease in the cost of sending indigents overseas on an annual basis for tertiary care (see discussion under Outputs from Statutory Authorities).

The provision of Legal Aid is a Constitutional requirement; the Government therefore does not perceive opportunities for significant savings in the short term from this category. Instead the Government will focus its efforts on examining the criteria associated with other programs such as rental assistance to see where savings can be realized to offset this anticipated increase.

Transfer Payments – For the 2012/13 fiscal year, the Government supported several social programs and incurred an estimated cost of \$31.4 million in Transfer Payments. This includes Scholarships; Financial Assistance to the poor as well as to Seamen and Veterans; promotion of Nation Building; and student enrichment support services.

The Government immediately cancelled the non-education components of the Nation Building Program which will save the public purse approximately \$2.5 million in the 2013/14 fiscal year.

The Government believes there are further savings opportunities and intends to carry out a full scale review on other social benefit programs such as Pre-school grants (the Government introduced reception year in 2012/13 which should reduce demand in this area), financial assistance vouchers (as the economy continues to rebound), and scholarships (to promote greater equity among recipients).

Financing Cost: Based on the existing debt portfolio and associated interest rates, as well as the lower expected costs associated with overdraft facilities, the Government is estimated to spend approximately \$1.7 million less on financing cost in 2013/14 than in 2012/13. The Financing Cost estimate for 2013/14 does not take into account any possible reduction in interest costs that may result from a refinancing of the Government's existing debt portfolio. The estimated reduction of \$1.7 million to the 2012/13 expenditure level is based on existing and known interest rates.

Summary of lower expenditures – The calculated savings from the above measures, if fully realized, will reduce Public Sector costs by approximately \$20 million in the 2013/14 fiscal year. The cost reduction entered in the "ratio reckoner" is \$12.5 million. This allows for a risk factor of close to 40% and improves the chances that the Government will remain within the fiscal parameters.

Reducing Public Sector Debt – The Government intends to continue reducing public sector debt for the duration of the 4-year Plan. This means:

- Regular principal payments will be made on existing amortizing loans;
- At least US\$10 million in bonds will be retired before 2015/16;
- Future operating overdrafts will be minimized or eliminated; and

The Government will also explore opportunities to obtain more favourable interest rates on its existing loan portfolio through refinancing options. Where such considerations provide evidence of reduced public sector interest cost, the Government will seek to take those opportunities with a view towards paying any interest saved towards the principal balance.

Importantly, the Government does not propose to enter into any new long term borrowings over the duration of the Plan. Rather, the Government will seek to generate the required cash for infrastructure development and other capital costs from its operating surpluses unless there is a clear business case that suggests otherwise.

Improve Cash Balances – Preliminary results shows that the Government closed the previous fiscal year (2012/13) with aggregate core Government bank balances of approximately \$117.9 million. This was an improvement of \$26.6 million over the previous year (2011/12) which opened with \$91.3 million in aggregate cash balances, on the 1st July 2012.

The Government's Plan shows a forecast cash balance of approximately \$340.7 million by the compliance deadline of 30th June 2016 (see Appendix A). This will be achieved through stable revenues and reductions in operating and capital expenditures.

The Government will also introduce policies to improve the performance of its 25 Statutory Authorities and Government Owned Companies to begin accruing greater benefits from their performance. To this extent, the Government will be seeking approximately \$6.5 million in dividend payments in each of the fiscal years for the duration of the Plan.

Stable Revenue – The Government's revenue outlook is stable and is not dependent on any material new or unproven Measures. The only Measure the Government intends to introduce is a Directorship fee which was first proposed in 2012/13, but was delayed to allow for further industry consultation. Now that those consultations have been completed, the Government feels confident introducing this Measure in the 2013/14 fiscal year. Further, this Measure will not have an inflationary effect on the local economy and has been risk weighted by reducing the calculated amount by 25%.

Table 3 Material Changes to revenue 2012-13 vs. 2013-14

Revenue Description	2012/13 Actual In 000s	13-14 Forecast In 000s	Variance In 000s
Cruise Ship Departure Charges			2,809
	8,531	11,340	
Environmental Protection Fund Fees			1,508
	5,427	6,935	
Other Import Duty & Charges			1,238
	84,607	85,845	
Directorship Fees	0	6,000	6,000
Motor Vehicle Charges			2,040
	10,512	12,552	
Partnership Fees			2,830
	23,319	26,149	
Tourist Accommodation Charges			5,384
	14,105	19,489	
Work Permits Fees			4,599
	53,641	58,240	
Total	200,142	226,550	26,408

Table 3 shows the material changes to the forecast revenue in 2013/14.

Cruise Ship Departure Taxes

Revenue from Cruise Ship Departure taxes is expected to increase by \$2.8 million for the 2013/14 fiscal year. The Port Authority has projected growth of 400,000-500,000 cruise passengers due to major cruise liners adding ships to the Caribbean route which would include Grand Cayman. These cruise lines set their itineraries well in advance adding a certain element of certainty to the forecast.

Environmental Protection Fund Fees

Environmental Protection Fund Fees is forecast to increase by \$1.5 million in the 2013/14 fiscal year. This is due to anticipated growth in airline and cruise ship passenger arrivals.

Other Import Duty and Charges

Other Import Duty and Charges is forecast to increase by \$1.2 million. This equates to a 1.5% increase and is well below the anticipated economic growth. The Government is also rationalizing the system of duty waivers to improve the levels of collection and eliminate abuses. This will translate into increased amounts coming into the Government's coffers on an annual basis.

Directorship Fee

As earlier outlined, this is the only new revenue measure proposed for 2013/14.

Motor Vehicle Charges

Motor Vehicle Charges are expected to generate additional revenue of \$2.0 million due to:

- Amendment made to the Traffic Law and Regulations effective September 2012, which increases revenue collections by increasing motor vehicle fees and charges, and reclassifying vehicles into different categories; and
- Increase in number of vehicles imported during the 2012/13 financial year based on reports received by major car dealers in the Cayman Islands.

Partnership Fees

Partnership Fees are based on anticipated growth and recent activities in the industry.

Tourist Accommodation Charges

Tourist Accommodation tax is forecast to increase by \$5.3 million. This increase anticipates growth in the number of tourist air arrivals by 4% as well as an increase in the Tourism Accommodation Tax rate from 10% to 13%. The law took effect in the last six months of the 2012/13 financial year – 2013/14 will benefit from a full year of charges.

Work Permit Fees

Work Permit Fees are forecast to increase by \$4.6 million. This is based on an anticipated growth of 0.6% in imported labor for 2013/14 fiscal year. The Government also intends to make legislative and policy changes that will result in a reclassification of Exempted Term Limit holders who will fall under the work permit category.

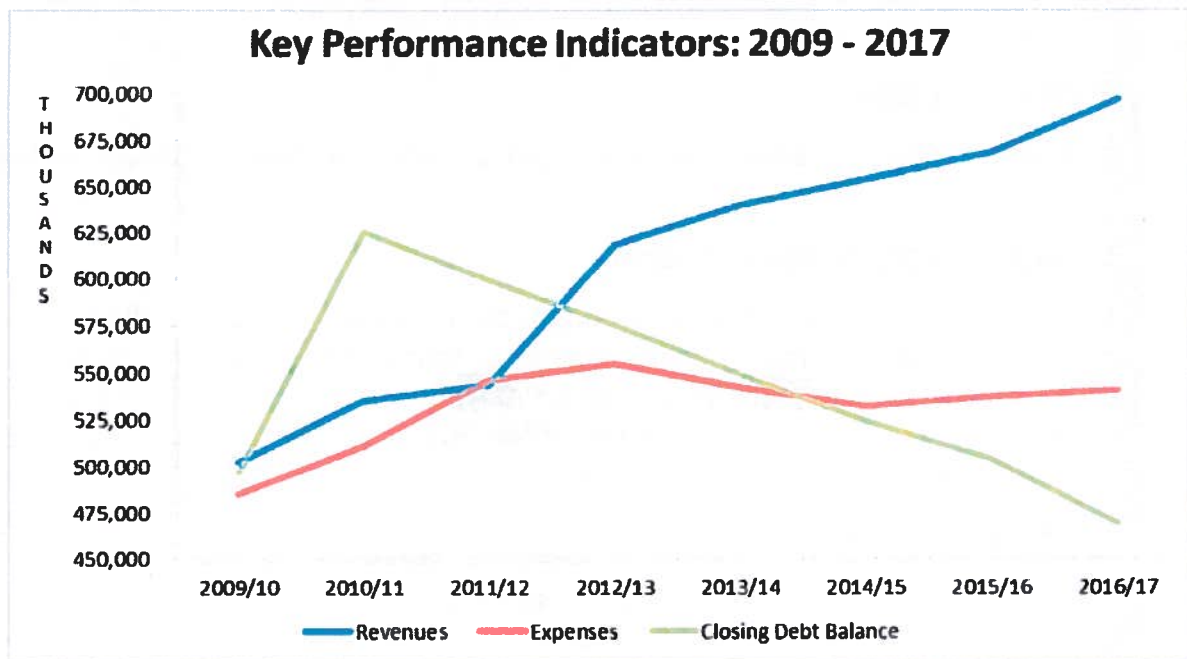
Minimal Public Sector Capital spend – Statutory Authorities and Government Owned Companies require approximately \$22 million per annum in capital injection over the medium term to meet various existing loan repayment obligations. The Government is committed to all Public Sector Agencies meeting their debt obligations and has planned accordingly.

In 2013/14, the Government is required to make certain payments in respect of work done in prior years. These included retention payment on the new

Government Administration Building as well as payment for works carried out on other projects but not previously settled. To meet these requirements, the Government has made provisions of approximately \$5 million.

Except for the two factors listed previously, the Government proposes to restrict capital spend in all other areas to \$25 million per annum for the next 3 fiscal years. This amount is expected to cover plant expansion programs mandated by the new Constitution, road maintenance and upgrades, completion of on-going projects, and replacement or purchase of plant and equipment for service delivery in the Public Sector.

This restricted capital spend is to enable the Government the best opportunity to meet the cash levels required under the PMFL by the 2015/16 deadline.



5.

ECONOMIC STRATEGY

The Government will be taking a multi-faceted approach towards economic growth in the short to medium term.

In brief

- Lower the cost of operations for small businesses;
- Encourage and facilitate new pillar industries;
- Enhancing immigration policies;
- Partner with the private sector for needed infrastructure;
- Redevelop Owen Roberts International Airport;
- Explore the development of a modern Cruise Berthing facility; and
- Improve health and wellness for all citizens

Lower the cost of operations for small businesses

The Government will introduce policies and other economic measures to encourage entrepreneurship and lower the cost for small businesses. As an interim measure and to inspire investor confidence, the Government is committing to no new inflationary revenue measures in the short to medium term.

With continued growth in numbers, the Government will also seek to lower work permit costs for small businesses and explore further opportunities to revisit certain fees implemented under the previous UDP administration. This will be done with a view of rolling back those fees considered inflationary once public finances have stabilized and the baseline revenue targets are being met.

Encourage and facilitate new pillar industries

Whilst the Cayman Islands' existing business model has served it well over the past 40 years, the Government recognizes the need to diversify the economic base to create further opportunities for Caymanians and add an extra layer of economic safeguard. The Government will therefore support initiatives such as health tourism and the expansion of the Special Economic Zone. The Government will also pursue other possibilities with local and international

investors to expand the economic base in a socially harmonious and sustainable manner.

Enhancing immigration policies

Immigration is a key and sensitive issue among the local community. The Government recognizes the need for international talent to augment our Caymanian workforce and will seek to implement policies which are conducive to harmonious growth.

Specific policies include rescinding the “key employee” provision and extending the term limit to 10 years. This will avoid a precipitous fall in work permit numbers by extending the time period for approximately 1,500 employees who would normally have had to leave the Islands in October 2013. Those persons will now have an opportunity to apply for permanent residency and further policies will be put in place to ensure that those departing will do so in a phased manner thereby reducing shock to the local economy.

Process changes to the work permit approval system will also be introduced. Routine granting of work permits will be done by the Immigration Department thereby speeding the approval process as applicants will no longer need to wait for the Work Permit Board to meet and consider applications.

This will provide the Government, businesses and those in the expatriate community, greater certainty in their medium term planning.

Partner with the private sector for needed infrastructure

With the current restrictions on borrowing, major infrastructure projects such as a Cruise Berthing Facility will only be possible in the short term through partnerships with private sector developers. In pursuing these development opportunities, the Government is committed to open, transparent and robust processes which deliver value for money and which accrues maximum benefits for the people of the Cayman Islands.

With the welcome shift in economic activities towards the eastern Districts, the Government intends to work closely with private sector developers for the expansion of the East West Arterial highway. This expansion is necessary to facilitate further development of certain major projects such as the Narayana University Medical Center, a five-star Conrad Hotel in Beach Bay and a \$360 million golf, residential, and commercial project in Frank Sound.

The Government will also work towards solutions for sustainable waste management, national housing, IT infrastructure and Transportation.

Redevelop Owen Roberts International Airport

Tourism remains a key pillar of the local economy. The Government is committed to the enhancement of our Tourism product through the redevelopment of the Owen Roberts International Airport.

This will entail an expansion of current capacity, improvements to airfield safety, improvement to the terminal and enhancement to the passenger experience through greater processing efficiency.

This project will be funded from existing cash reserves held by the Airports Authority in the short run and may develop into a public private partnership for future expansion phases.

Develop a modern Cruise Berthing Facility

Work on the development of a modern Cruise Berthing facility is underway via the development of a business case. Cruise berthing is seen as a major requirement to improve the Cayman Islands competitive standing in the cruise tourism industry and improve recently declining visitor numbers.

It is also seen as a catalyst towards revitalizing downtown George Town and restoring some of the declining fortunes experienced in recent years. The Government intends to ensure that maximum benefits accrue to the residents of the Cayman Islands from any berthing facility by restricting any accompanying new upland development as part of that project.

The process is proceeding in accordance with international best practices. If the business case demonstrates an economically viable project which is in the best interest of the people of the Cayman Islands, the Government intends to move forward with the start of construction by the end of 2014.

The Government understands that any crystallization of a PPP arrangement to develop the facility will have to be done within the confines of the PMFL fiscal ratios.

Improve health and wellness for all citizens

Almost 20% (approximately \$100 million in 2012/13) of the national budget is directed towards Public Sector healthcare costs. It is a growing problem which the Government recognizes and intends to take measures to address over the short to medium term.

The Government intends to address this key issue by incentivising lifestyle changes, introducing policies with greater focus on preventative and primary healthcare, thereby minimizing the incidences of chronic illness.

The Government will also review the current healthcare model to determine whether it is optimal for the Cayman Islands. The current situation involves a

profitable insurance sector, increasing healthcare costs and a Government hospital which is incurring annual losses primarily from bad debts and the inability to collect from uninsured or underinsured patients.

6.

Conclusion

The Government is in firm command of its fiscal affairs. It is ready and able to take the Country forward in achieving the goals outlined in the PMFL.

As a Government, we have a mandate to put forward a Plan and a position which we believe is in the best interest of our people. Understandably, the United Kingdom Government is keen to avoid any unnecessary contingent liability.

Differences of opinion are a normal part of any relationship, and there will be times when we may not agree on the most effective means of achieving our various objectives. However, when such differences arise, the Government believe that it is important that we address them with mutual respect for the views of each party and that we never lose sight of the common objective which is the continued prosperity of the people of the Cayman Islands.

The Government must have a stable framework in which to operate, when such a framework is agreed with the United Kingdom Government, it should remove a certain level of annual uncertainty regarding the national budget as long as the Government demonstrates that it remains on a fiscally prudent path.

It should also be recognized that arbitrary mandates without sound economic analysis or an appreciation for conditions in the local economy may be counterproductive to proper fiscal management.

In most successful business partnerships, risk is transferred to the party best placed to manage those risks. Therefore, when the Elected Government and the senior management within the Cayman Islands Public Service carefully develop a Plan based on experience, informed through stakeholder consultation and developed for our unique set of circumstances, such a Plan should be viewed with the credibility it deserves.

It must also be recognized that such decisions are more than just simple numbers on a spreadsheet; they affect the lives of our citizens on a very personal level and could be the difference between a child getting a college education or a sick person getting access to needed medical care.

This *Medium Term Fiscal Strategy* sets out the Government's view of the fiscal and economic dimensions of these imperatives.

Government recognises that choices have to be made within prudent fiscal limits as shaped by the current circumstances, while laying the foundations on which to build future budgets. However, we are confident in our abilities to manage the domestic economic affairs of the Country and believe the Plan laid out in this document is achievable, credible and prevents economic shocks which could be damaging to our recovery.



Hon. Marco Archer
Minister for Finance & Economic Development
15th August 2013

Appendix A

**Cayman Islands Government
Fiscal Frame Calculator**
All figures in 000s and Cayman Islands Dollars

	Prelim Results	SPS Forecast				
	2012/13	2013/14	2014/15	2015/16	2016/17	
Operating Revenue	618,403	640,000	654,000	668,000	697,000	
Total Operating Revenue (A)	618,403	640,000	654,000	668,000	697,000	
Depreciation	25,013	25,440	25,940	25,940	25,940	
Financing Expenses	33,187	31,474	29,703	28,621	27,258	
(Profit)/Loss of Statutory Authorities/Government Companies	(1,658)	(1,901)	(2,902)	(2,902)	(2,902)	
Other Operating Expenses	498,000	487,000	479,259	485,060	489,911	
Total Operating Expenses (B)	554,542	542,013	532,000	536,719	540,207	
Net Operating Profit (A - B)	63,861	97,987	122,000	131,281	156,793	

	Prelim Results	SPS Forecast			
	2012/13	2013/14	2014/15	2015/16	2016/17
Cashflow from Operating Activities	99,705	121,526	145,038	154,319	179,831
Net Cashflow from Operating Activities (C)	99,705	121,526	145,038	154,319	179,831
Purchase of property, plant and equipment	(31,270)	(30,000)	(25,000)	(25,000)	(35,000)
Equity Injection In Statutory Authorities/Government Companies	(22,025)	(22,000)	(22,000)	(22,000)	(22,000)
Net Proceeds from Dividends/Investments	6,464	6,500	6,500	6,500	6,500
Net Cashflow from Investing Activities (D)	(46,831)	(45,500)	(40,500)	(40,500)	(50,500)
Repayment of Borrowings	(26,304)	(26,362)	(25,374)	(19,921)	(19,545)
Net cash flows from financing activities (E)	(26,304)	(26,362)	(25,374)	(19,921)	(19,545)
Net increase/(decrease) in cash and cash equivalents (C + D + E)	26,570	49,664	79,164	93,898	109,786
Add Cash and cash equivalents at beginning of period	91,346	117,916	167,580	246,744	340,642
Gross Cash and Cash Equivalents at end of period	117,916	167,580	246,744	340,642	450,428
Less Restricted Cash Balances (Excluding General Reserves)	(52,532)	(56,032)	(59,532)	(62,532)	(65,532)
Net Operating Cash	65,384	111,548	187,212	278,110	384,896

Cayman Islands Government
Fiscal Frame Calculator
All figures in 000s and Cayman Islands Dollars

	Prelim Results	SPS Forecast			
	2012/13	2013/14	2014/15	2015/16	2016/17
Opening Debt Balance	601,794	575,490	549,128	523,754	503,833
Less Principal Repayments	(26,304)	(26,362)	(25,374)	(19,921)	(19,545)
Closing Debt Balance	575,490	549,128	523,754	503,833	484,288

DEBT SERVICE RATIO	Prelim Results	SPS Forecast			
	2012/13	2013/14	2014/15	2015/16	2016/17
Debt Service					
Core Government Financing Expenses	33,187	31,474	29,703	28,621	27,258
Core Government Principal Repayments	26,304	26,362	25,374	19,921	19,545
Statutory Authorities/Government Companies Debt Service Cost	19,610	18,331	49,178	15,870	11,733
Total Debt Service (F)	79,101	76,167	104,255	64,412	58,536
Total Operating Revenue (A)	618,408	640,000	654,000	668,000	697,000
Debt Service Ratio (F/A)	12.8%	11.9%	15.9%	9.6%	8.4%

Target: FFR 2015/16 <= 10%

NET DEBT SERVICE RATIO	Prelim Results	SPS Forecast			
	2012/13	2013/14	2014/15	2015/16	2016/17
Core Government Debt Balance	575,490	549,128	523,754	503,833	484,288
Plus Weighted Balance of Statutory Authorities/Government Companies Debt	87,550	78,809	70,372	57,622	50,352
Total Debt	663,040	627,937	594,126	561,455	534,640
Less Gross Cash and Cash Equivalents at end of period	(117,916)	(167,580)	(246,744)	(340,642)	(450,428)
Net Debt (G)	545,124	460,357	347,382	220,813	84,211
Total Operating Revenue (A)	618,408	640,000	654,000	668,000	697,000
Net Debt Ratio (G/A)	88.2%	71.9%	53.1%	33.1%	12.1%

Target: FFR 2015/16 <= 80%

LIQUID ASSET RATIO**	Prelim Results	SPS Forecast			
	2012/13	2013/14	2014/15	2015/16	2016/17
Estimated Executive Expenditure	554,542	542,013	532,000	536,719	540,207
Estimated Executive Expenditure per day (H)	1,519.3	1,485.0	1,457.5	1,470.5	1,480.0
Liquid Opening Cash Balance (Opening Cash Balance Less Restricted Balances)	36,814	61,884	108,048	184,212	275,110
Less Estimated decline in cash between July and December	(66,000)	(50,000)	(45,000)	(40,000)	(40,000)
Estimated Liquid Assets (I)	(27,186)	11,884	63,048	144,212	235,110
Number of Days Cash Reserves (I/H)	(17.9)	8.0	43.3	98.1	158.9

Target: FFR 2015/16 >= 90 days

Notes

**Notional calculation based on estimated intra-year lowest cash balance relative to the end of the year.