GOVERNMENT OF GRENADA

Compliance Assessment Report: Supplementary Budget 2020

Submitted To:

The Parliament

Submitted By:

The Minister of Finance, Planning, Economic and Physical Development

In Fulfillment of Section 12 (1) (2) (d) of the Fiscal Responsibility Act No. 29 of 2015, as Amended

April 2020

Table of Contents

1.0 Introduction

This Compliance Assessment Report to Parliament is in fulfillment of Section 12 (1) (2) (d) of the Fiscal Responsibility Act No. 29 of 2015, as amended (FRA), which stipulates that,

> *"The Minister of Finance shall prepare and submit to Parliament, along with the presentation of the annual and any supplementary budget, a statement showing the progress made towards compliance with the fiscal rules and targets under sections 7 and 8, in the relevant financial year."*

More specifically, Section 12 (2) (d) requires that the following information be provided in the Compliance Assessment Report:

a) The manner in which the annual budget or supplementary budget laid before Parliament complies with the fiscal rules and targets, and reflects improvement required for full compliance.

Compliance is to be assessed for the following explicit rules and targets that are stipulated in Sections 7 and 8 of the FRA:

1. **Primary Expenditure Rule**: the rate of growth of the primary expenditure[1] of the Central Government, and of every covered public entity[2], shall not exceed 2.0 percent in real terms in any fiscal year, when adjusted by the preceding year's inflation rate.
2. **Wage Bill Rule**: the ratio of expenditure on the wage bill shall not exceed 9.0 percent of GDP.
3. **Primary Balance Rule**: the targeted primary balance shall be a minimum of 3.5 percent of GDP.
4. **Contingent Liabilities Rule**: contingent liabilities arising from, as a result of, or in connection with Public-Private Partnerships shall not exceed 5.0 percent of GDP.
5. **Public Debt Target**: the total stock of public sector debt shall not exceed 55.0 percent of GDP.

---

[1] Calculated as Total Expenditure less Interest Payments.

[2] In the absence of a consolidated Public Sector fiscal account (i.e. both Central Government and Public Entities), primary expenditure only includes expenditure of the Central Government.

As stipulated in the Act, the following are exempted from the fiscal rules and targets:

i. Grants made to the Government for the financing of capital expenditures in Grenada and the associated expenditures.
ii. Any capital expenditures made from or under the National Transformation Fund.

2.0 Context: 2020 COVID-19 Supplementary

The COVID-19 is a global health pandemic of enormous proportions. Its impact and effects have delivered a decisive and pronounced economic shock to countries worldwide, Grenada not being spared. The direct impact on Grenada's economy to date has been significant with job losses (precise amount being estimated) because of the closure of hotels, the departure of over 3,000 SGU students, and the negative ripple effects, the stalling of construction activity and the decline in general economic/business activity. In-house analysis of the Ministry of Finance has preliminarily estimated a contraction of 12.9% in real GDP in 2020.

Cabinet at its meeting on April 6th, 2020, approved a stimulus package of expenditure measures aimed primarily at cushioning the effect of the economic fallout due to COVID-19. The measures include payroll and income support to affected businesses and individuals respectively, as well as other measures to help mitigate the impact of COVID-19 such as small-scale community-based PSIP projects to provide short-term employment.

Table 1 presents the estimated cost of the COVID-19-related expenditure stimulus package.

Table 1: Estimate Expenditure - Stimulus and Supplementary

Fiscal Category	Original Budgeted Amount (EC$M)	Estimated Cost of Stimulus Measures (EC$M)	Vote	Total Supplementary (EC $M)
Current Transfers	163.1	40.0 (payroll & income support, small business & hotelier support, contribution to Subsidy and support to other severely impacted groups)	Ministry of Finance, Planning, Economic & Physical Development	40.0
Goods & Services	121.5	10.0 (COVID-19 related health expenditure)	Ministry of Health, Social Security & International Business	10.0
Total		50.0		50.0

Source: Ministry of Finance

Table 2 presents the revised fiscal estimates for 2020. A primary balance of 0.1% of GDP is estimated compared to the original budgeted estimate of 6.4% of GDP. The revised fiscal includes estimates of the COVID-19 stimulus expenditure measures, revised estimates of revenue and grants and contingencies for possible expenditure overruns. The revised revenue estimates reflect the significant contraction in nominal GDP. Capital expenditure has been scaled down relative to the original Budget because of the anticipated slowdown in major PSIP projects over the period March-June, as well as delayed starts to originally-planned projects. However, it is assumed that small-scale community-based projects will be rolled out during the three-month period, the expenditure for which will be had from a reallocation within the capital budget. Capital grants have also been lowered consistent with the scaling back of capital expenditure.

In accordance with Section 12 (2) (d) of the FRL, details of the 2020 COVID-19 Supplementary Budget are set out in Table 2.

y

		Estimates
	2020	
	Budget	**COIVD-19 Fiscal**
	EC$M	
Total Revenue & Grants	**1,015.6**	**820.1**
Total Revenue	**797.0**	**688.5**
Tax Revenue	**739.4**	**637.6**
Taxes on Income & Profits	**152.3**	**126.7**
Personal Income Tax	72.6	61.6
Corporate Income Tax	69.9	57.2
Withholding Tax	9.9	7.9
Taxes on Property	**30.1**	**23.4**
Property Tax	15.1	11.2
Inheritance Tax	0.0	0.0
Property Transfer Tax	15.0	12.2
Taxes on Domestic Goods & Services	**159.1**	**141.3**
VAT	130.2	114.4
Excise Tax	2.9	2.4
Stamp Duty	4.2	3.8
Annual Stamp Tax	20.9	20.0
Embarkation tax	0.1	0.1
Gaming Tax	0.7	0.6
Taxes on International Transactions	**397.9**	**346.1**
Import Duty	88.7	78.3
Petrol Tax	68.7	55.0
Customs Service Charge	65.3	58.0
Environemental Levy	13.1	11.6
Miscellaneous Customs Revenue	1.3	1.1
VAT	134.8	119.4
Excise Tax	26.1	22.7
Non-tax Revenue	**57.6**	**50.9**
Total Grants	**218.6**	**131.6**
o/w: Capital Grants	*201.8*	*115.2*
Total Expenditure	**859.0**	**883.2**
Primary Expenditure	**792.0**	**817.5**
Recurrent Expenditure	**633.7**	**739.3**
Employee Compensation	282.2	280.4
Goods & Services	121.5	151.2
Interest Payments	67.0	65.7
Current Transfers	163.1	242.0
Capital Expenditure	**225.3**	**143.9**
Current Account Balance (excluding Grants)	163.3	(50.8)
Overall Balance	156.6	(63.1)
Primary Balance (including Grants)	223.6	2.6
Memo Items		
GDP (nominal)	3,475.3	2,825.3
Real GDP, Market Price (% Change)	4.2	(12.9)
Inflation	1.0	1.82
Primary Expenditure less Grants ($m)	590.2	702.4
Primary Expenditure less Grants (%)	2.0	21.6
Primary balance (as a % of GDP)	6.4	0.1
Public Debt (% of GDP)	53.7	58.3

3.0 Compliance with Fiscal Rules and Targets

The additional COVID-19 expenditure, the estimated contraction in GDP and lower revenue translate to breaches in three of the four fiscal rules and a deviation of the public debt-to-GDP ratio from its target as shown in Table 3.

Table 3: Compliance Matrix

Fiscal Variable	**Fiscal Rules**	**2020 COVID-19 Supplementary**	**Compliance**
Primary Balance, After Grants (percent of GDP)	**3.5%** (not less than)	0.1%	No
Wage Bill (percent of GDP)	**9.0%** (not exceeding)	9.9%	No
Primary Expenditure less Capital Grants (real percent change)	**2.0%** (not exceeding)	21.6%	No
PPP-related Contingent Liabilities (percent of GDP)	**5.0%** (not exceeding)	0.0%	Yes
Public Debt (percent of GDP)*	**55.0%**	58.3%	Deviation from target

Source: Ministry of Finance
**Central Government plus Government Guaranteed.*

4.0 Suspension of Fiscal Rules and Targets for the Fiscal Year 2020

Section 10 (1) and (2) of the FRL, which deals with Escape Clause states, "*the Minister may by Order suspend, for a period not exceeding one fiscal year, fiscal rules, targets and corrective measures under sections 7 and 8, where– (a) a natural disaster, public health epidemic, or war as a result of which a state of emergency has been declared by the Governor-General pursuant to section 17 (1) of the Constitution; (b) real GDP experiences a decline of two percent in a given fiscal year or a cumulative decline equal to or greater than three percent over two consecutive fiscal years; (c) the Eastern Caribbean Central Bank has certified in writing that a financial sector crisis has occurred, or is imminent, and the Minister estimates that the fiscal costs of such crisis, including the costs of any related recapitalisation of banks by the Government after all possible private sector solutions have been explored, is likely to equate or exceed four percent of* GDP."

Given the impact of, and Government's response to the COVID-19 crisis, two of the three criteria required for invoking the Escape Clause have been met: (i) a State of Emergency was declared by the Governor-General on March 25th 2020; and (ii) GDP is preliminary estimated to contract by 12.9% in 2020. The economic impact of COVID-19 is broad based, but the main assumptions for the pronounced decline in GDP estimated for 2020 are; a 50% decline in Tourism value added, 20% reduction in private education, and a 15% decrease in private construction activity as well as wholesale and retail trade.

As Table 3 shows, three of the four fiscal rules are estimated to be breached, while the Public debt-to-GDP ratio is expected to deviate from its target. These estimated breaches are justified because they are solely as a result of the impact of COVID-19 on key macro-economic variables particularly GDP, revenue and expenditure.

It is therefore necessary that the fiscal rules and targets under Sections 7 and 8 of the FRL be suspended for the fiscal year 2020 in accordance with Section 10 (1) and (2) of the FRL to allow the Government to cushion the acute impact of COVID-19 on the economy and society. Indeed, the non-adherence to the fiscal rules and targets within the current context is justified given the severity of the crisis and the potent expenditure measures it necessitates to address its impact and effects.

5.0 Recovery Plan for Fiscal Rules and Targets

Section 10 (4) and (5) of the FRL states, "*Where the Minister has suspended any fiscal rule, target or corrective measure established under section 7 or 8, the Minister shall immediately prepare and lay before the Houses of Parliament for approval a recovery plan memorandum pursuant to subsection (5). The recovery plan memorandum under subsection (4) shall set out the measures proposed to secure compliance with the fiscal rule, target or corrective measure at the expiration of the period for which Parliament approves the suspension of a fiscal rule, target or corrective measure established under section 7 or 8, including the size and nature of the revenue and expenditure measures.*"

Further, Section 10 (6) and (7) states, "*Subject to subsection (7), in the fiscal year immediately following the period for which fiscal rules and targets are suspended pursuant to this section, the Minister shall implement the measures approved by Parliament under the recovery plan* *memorandum to ensure full compliance with the fiscal rules and targets under sections 7 and 8. Where the Minister determines that resumption of the application of fiscal rules, targets or corrective measures at the expiration of the period stipulated in an Order made pursuant to subsection (1) would be unduly harmful to the public finances and macroeconomic or financial stability, the Minister may make a second Order to extend the period for which such fiscal rules and targets are suspended under this section by a period not exceeding one fiscal year."*

Table 4 sets out the preliminary fiscal projections for the years 2021 & 2022, which show some fiscal improvement on the following main assumptions: (i) GDP growth will rebound in 2021 underpinned mainly by a pickup in construction activity as well as wholesale and retail trade and a return of activity at SGU, with the related positive spin offs on ancillary services; (ii) modest increase in total revenue, consistent with the projected positive GDP growth; and (iii) restrained expenditure growth particularly in current transfers.

	Projections	
	2021	2022
	Proj.	Proj.
	EC$M	
Total Revenue & Grants	**896.5**	**903.2**
Total Revenue	**727.4**	**760.7**
Tax Revenue	**672.7**	**703.4**
Taxes on Income & Profits	**123.7**	**129.3**
Personal Income Tax	66.2	69.2
Corporate Income Tax	49.0	51.2
Withholding Tax	8.5	8.9
Taxes on Property	**25.2**	**26.3**
Property Tax	12.1	12.6
Inheritance Tax	0.0	0.0
Property Transfer Tax	13.1	13.7
Taxes on Domestic Goods & Services	**151.9**	**158.8**
VAT	122.9	128.6
Excise Tax	2.6	2.7
Stamp Duty	4.1	4.3
Annual Stamp Tax	21.5	22.5
Embarkation tax	0.1	0.1
Gaming Tax	0.6	0.6
Taxes on International Transactions	**372.0**	**389.0**
Import Duty	84.2	88.0
Petrol Tax	59.1	61.8
Customs Service Charge	62.3	65.2
Environemental Levy	12.5	13.0
Miscellaneous Customs Revenue	1.2	1.2
VAT	128.3	134.1
Excise Tax	24.4	25.5
Non-tax Revenue	**54.7**	**57.2**
Total Grants	**169.1**	**142.5**
o/w: Capital Grants	*151.5*	*123.9*
Total Expenditure	**862.0**	**851.7**
Primary Expenditure	**797.1**	**791.2**
Recurrent Expenditure	**678.7**	**693.1**
Employee Compensation	291.7	303.3
Goods & Services	153.5	155.9
Interest Payments	64.9	60.5
Current Transfers	168.7	173.4
Capital Expenditure	**183.3**	**158.6**
Current Account Balance (excluding Grants)	48.7	67.5
Overall Balance	34.5	51.4
Primary Balance (including Grants)	99.4	111.9
Memo Items		
GDP (nominal)	3,036.0	3,174.8
Real GDP, Market Price (% Change)	5.8	2.8
Inflation	1.57	1.81
Primary Expenditure less Grants ($m)	645.6	667.3
Primary Expenditure less Grants (%)	(9.9)	1.8
Primary balance (as a % of GDP)	3.3	3.5
Public Debt (% of GDP)	60.9	63.7

It must be underscored that given the evolving nature of the COVID-19 crisis and the immense uncertainty about how long it would persist, at this stage, the projections and assumptions are tentative at best. As shown in Table 4, the primary balance rule and the wage bill rule are marginally breached in 2021, while the primary expenditure rule is adhered to. The wage bill rule is breached solely because of subdued growth in nominal GDP. In 2022, both the primary balance and primary expenditure rules are adhered to, but wage bill rule remains marginally breached, while the public debt-to-GDP ratio deviates further from its target.

Therefore, it might become necessary for an extension of the recovery period beyond the one year stipulated in the FRL, following a review of the projections in June 2020.