Sovereign: Jamaica

Assessment of the Budget and Revenue Measures

The Government of Jamaica (GOJ) is programming to spend $852.6 billion in fiscal year (FY) 2020/21. This is $6.4 billion or 0.7% lower than the estimated final spending during the previous fiscal year. Above the line expenditure amounts to $660.2 billion of which the lion share goes to recurrent spending ($582.2 billion or 88.2%) and the remainder on capital spending ($74.2 billion or 11.2%). Revenue inflows of $675.1 billion is expected to cover programmed above the line spending resulting in a fiscal surplus of $14.9 billion or 0.7% of GDP. When interest payments are added to the fiscal surplus a primary balance surplus of $147.5 billion or (6.5% of GDP) is generated.

Below the line outflows of $163.4 billion is envisaged with the larger share $155.2 billion being amortization of debt. Below the line inflows amount to $151.7 billion of which loans account for $143.6 billion and other inflows $8.1 billion. With total overall inflows (above and below the line items) at $826.9 billion and overall expenditure at $852.6 billion an overall deficit of $25.8 billion is programmed.

Table 1: Summary Medium-term Budget

	Actual 2017/18	Actual 2018/19	Estimate 2019/20	Estimate 2020/21	Estimate 2021/22	Estimate 2022/23	Estimate 2023/24
Revenue & Grants	**560,773.6**	**628,985.2**	**645,259.1**	**675,093.1**	**700,451.9**	**738,032.8**	**778,726.7**
Tax Revenue	496,894.6	542,919.4	557,536.1	603,785.2	639,476.5	675,426.2	713,615.5
Grants	5,614.4	10,547.0	4,718.1	4,337.3	4,087.9	4,327.9	5,576.7
Expenditure	**552,050.1**	**604,597.5**	**645,022.3**	**660,225.8**	**670,871.7**	**690,744.7**	**720,379.8**
Recurrent	505,244.0	538,393.2	572,911.7	586,022.6	591,305.2	605,395.7	627,678.2
Programmes	176,779.5	209,079.7	220,170.5	232,071.7	229,932.5	238,433.7	246,252.5
Compensation	193,283.5	200,125.3	213,610.1	221,296.6	233,361.4	244,979.5	257,178.5
Wages & Salaries	178,366.3	183,505.5	196,109.3	204,282.0	214,496.1	225,220.9	236,482.0
Interest	135,181.0	129,188.1	139,131.1	132,654.2	128,011.3	121,982.5	124,247.2
Capital Expenditure	46,806.0	66,204.3	72,110.6	74,203.3	79,566.5	85,349.0	92,701.6
Fiscal balance	**8,723.4**	**24,387.7**	**236.8**	**14,867.3**	**29,580.2**	**47,288.1**	**58,346.9**
Loans	**207,133.0**	**114,180.1**	**95,810.7**	**143,602.9**	**108,180.2**	**73,889.6**	**51,148.5**
Amortization	**232,289.9**	**132,990.1**	**178,526.4**	**155,189.7**	**142,083.7**	**138,982.7**	**115,634.9**
Other Inflow (inc'ds PCDF)	**11,400.1**	**27,894.9**	**87,790.7**	**8,193.0**	**4,323.3**	**17,804.9**	**6,139.5**
Other outflow (inc'ds BOJ recap)	**14,260.6**	**35,164.5**	**35,522.9**	**37,260.8**	**-**	**-**	**-**
Overall Balance	**(19,293.9)**	**(1,691.9)**	**(30,211.1)**	**(25,787.3)**	**-**	**-**	**-**
Primary Balance	**143,904.4**	**153,575.8**	**139,367.9**	**147,521.5**	**157,591.5**	**169,270.6**	**182,594.1**
Total Payments	**798,600.6**	**772,752.1**	**859,071.6**	**852,676.3**	**812,955.4**	**829,727.4**	**836,014.7**

Sources: Ministry of Finance & Planning and JMMIR

What do the numbers communicate and are they credible?

Revenue

Revenue & Grants at $852.6 billion represents 29.6% of GDP, which is relatively in line with the three year average. Tax revenue at $603.8 billion is 26.5% of GDP and is also relatively in line with the three year average. Revenue & Grants and Tax Revenue are expected to grow by 4.6% and 8.3%, respectively. The Tax Revenue numbers appear credible, but it may be very challenging for it to grow at the programmed rate given a combination of expected low inflation and weak nominal GDP growth. The government of Jamaica (GOJ) is forecasting nominal GDP to rise by 5.7%. **With Revenue & Grants and Tax Revenue buoyancy of 1.01 and 1.04, respectively, net of the revenue measures (See Revenue Measures), we project growth in both components of 4.4% and 7.2%, respectively. This is relatively in line with figures presented in the budget**. However, our projections did not take account of likely fallout in GDP growth, domestic consumption and visitor arrivals.

In the event of revenue shortfalls and under normal economic conditions the tax authority can ramp up compliance measures in order to bring revenue in line with budget. However, these are extraordinary times and compliance efforts may not yield the desired result. Given the prevailing global and domestic economic conditions, we envisage weaker than expected upward adjustments in revenues and the risk is elevated (**See Risk to Budget**).

Expenditure

Overall expenditures is slated to increase by $15.2 billion or 2.4%, which in real terms is lower than the estimated spending in the previous period given inflation of more than 4%. The amount being expended on wages & salaries, $204.3 billion, has finally hit the 9% of GDP target. This is one of the main pillars of the agreements which were inked with the International Monetary Fund (IMF) under the nearly decade long economic assistant programme.

The GOJ is expected to spend $132.6 billion on interest of which the domestic portion is $109.2 billion and the foreign portion is $34.4 billion. As the debt level continues to fall, interest payments as a percentage of overall revenue and GDP are falling commensurately. In FY 2010/11 interest payments relative to revenues and GDP were 40.1% and 10.8%, respectively, and is expected to fall to 19.6% and 5.8% in 2020/21, respectively.

Capital expenditure at $74.2 billion (3.3% of GDP) represents a significant increase when compared to previous years. For example in FY 2013/14 the GOJ expended $37.7 billion (2.5 of GDP) on capital. Provisions are made in the current budget for the Southern Highway Improvement Project; Montego Bay by-pass; rural water project and construction of the Western Children and Adolescent Hospital. These and other projects will help to improve the country's infrastructure and stimulate growth in the Construction sector. What is also commendable in addition to the nominal spending on capital is the execution rate (capital outlay relative to budget). In previous years the ratio of spending relative budget was below 80%, and fell to as low as 60% in some periods. It has since risen to more than 90% and is expected to remain elevated over the medium term. Capacity constraint in the public and private sectors is one of the main cause for delays in project execution.

Debt Issuance and Market Impact

The GOJ will be active in loans market as it seek to take up $155.2 billion to help cover amortization of $143.6 billion. The net flow to the market is $11.6 billion which does not compared favourably to the $82.7 billion that went back to the market during the previous fiscal year. The GOJ will be visible in the domestic capital market this fiscal year as $109.2 billion will be sought to cover amortization of $111.0 billion.

GOJ activities in the domestic capital market will put pressure on liquidity levels. However, we do not anticipate a rise in local interest rates. We expect the Bank of Jamaica (BOJ) to intervene in the market to help stabilize liquidity levels and prevent upwards interest rate adjustments. The BOJ will be incentivized to act accordingly because of the low risk associated with rising inflation. Expected slower than planned adjustment in domestic GDP is also another reason that will prod the Bank to act to help steer the economy from falling into recession.

Allocation by Ministries: Non-debt Recurrent and Capital Spending

Outside of the Ministry of Finance & Public Service, priority is being given to four ministries –Health; National Security, Education, Youth and Information; and Economic Growth and Job Creation - in the Budget (See Table 1) which account for 57% and 59% of the Non- debt recurrent and –capital spending, respectively. The overall spending on these ministries is in keeping with the Vision 2030 objectives and the mandate of the government to among other things boost economic growth and reduce employment. Relative to estimated spending in FY2019/20 the outlay on non-debt recurrent increased by $8.1 billion (3.0%) and while spending on capital decline by $4.3 billion (8.9%).

Table 2: Synopsis of Budgetary Allocation

	Non-Debt Recurrent Spending	% of total	% Change vs. FY 2019/20	Capital Spending	% of total	% Change vs. FY 2019/20
Ministry of Health	74,140.3	15.1%	5.5%	3,903.6	5.3%	12.5%
Ministry of National Security	78,006.3	15.9%	2.2%	15,953.8	21.5%	-19.7%
Ministry of Education, Youth and Information	117,073.0	23.9%	4.6%	1,480.5	2.0%	18.3%
Ministry of Economic growth and Job Creation	11,464.2	2.3%	-18.1%	22,355.9	30.1%	-4.3%
sub-total	*280,683.8*	*57.2%*	*3.0%*	*43,693.8*	*58.9%*	*-8.9%*
Total Budget	**490,629.1**	**100%**	**4.5%**	**74,203.2**	**100%**	**2.9%**

Sources: JMMBIR

Debt Levels

Debt-to GDP is estimated to fall to 91.5% at the end of FY 19/20 compare to 94.4% at the end of FY 2018/19. With programmed fiscal surpluses and positive real GDP growth the debt is estimate to reach 67.8%, which is within reach of the 60% that is targeted by end FY 2025/26. The projected path of the debt is relatively in line with our forecast, as such we are fairly confident that the debt target can be achieved within the time frame promulgated under the Debt Act.

Risks to the Budget

The 2020/21 budget and medium-term fiscal framework are cast at a time when there are global headwinds that could have far reaching negative impact on the global economy. We expect sharp reduction in tourist arrivals and a slowdown in remittance flows occasioned by reduction in GDP growth in source countries – United States of America (USA), the United Kingdom (UK) and Canada. The coronavirus outbreak (COVID-19) in China which has subsequently spread to other parts of the world could disrupt the global supply chain. It has already forced some governments, including the USA, to impose travel restrictions to help curtail the spread of the virus. For countries such as Jamaica we anticipate reduction in tourism and remittance flows.

The price of oil envisage in the budget is US$54.88 per barrel, based on West Texas Intermediate (WTI) price. At the time of writing oil price had tumbled to US$31.4 per barrel, or 43.3% lower than programmed. Oil price has declined due to a combination of increased supplies arising from the failure of The Organization of Petroleum Exporting Countries (OPEC) and Russia to reach agreement on further supply cuts, as well as concern regarding lower demand occasioned by expected slowdown in the global economy. We expect that global demand for goods and services will remain subdued throughout 2020. Given this outlook commodity prices, including oil, are likely stay depressed throughout the period. This is likely to translate into lower inflation and improved terms of trade for import-dependent economies.

Under the above mentioned scenario we envisage weaker inflation and nominal/real GDP growth for Jamaica over the next year, at least. Thus we expect significant fallout in the Special Consumption Tax (SCT), from which the lion share is derived from the tax on fuel; reduction in travel tax; and lower than planned GCT collections. **The expected net impact on the fiscal accounts are a shift from a fiscal surplus to fiscal deficit and deceleration in the pace of reduction in debt-to-GDP**.

Revenue Measures

The GOJ has reduced taxation to the general public to the tune of $18.0 billion bringing the cumulative tax reduction since FY 2019/20 to $32 billion (1.4% of GDP). The Tax measures for FY 2020/21 are summarized in Table 3. The reduction in taxation is welcome, as the country has had to grapple with several years of increased taxation to help then GOJ meet fiscal targets. The net impact of GCT on the average household is likely to be low, given relatively subdued spending at the individual household level. However at the aggregate level the tax cut is significant and will help to boost consumption in the economy.

The ad valorem Asset Tax was first implemented in FY 2012/13 at a rate of 0.14% of the value of taxable assets for specified regulated entities. During FY 2014/15 it was increased to 0.25% and remain at these levels. Adjustment was made in FY 2019/20 where it non-financial institution were no longer required to continue make payments. The Asset Tax is extremely burdensome on businesses, which are already facing heavy taxation. It negatively affected the investment decision and caused suboptimal allocation of capital, as the tax has no bearing on income generated. The net result of the Asset Tax is that some projects with low cash yield in early years, but which are highly profitable are scaled down or put on hold. The reduction in the Asset Tax rate is commendable, and hopefully the tax will be eliminated in the near future.

Table 3: Revenue Measure

Revenue Measures	Revenue foregone (J$ billion)
Reduction in the Standard general Consumption (has low GCT) rate from 16.5% to 15%	13.968
Reduction in the Asset Tax rate from 0.250% to 0.125%	3.020
New Income Tax credit for companies (regulated and unregulated) with annual sales/revenues less than or equal to $500 million	1.010
Total	**17.998**

Sources: Ministry of Finance and Planning and JMMBIR

Opinion

Given resource constraints and the many issues that are facing the country, the budget is crafted to help the sovereign balance the economic growth agenda while at the same time meet critical fiscal targets to engender long-term fiscal and debt sustainability. Having assessed the numbers these are the positive highlights: i) continued fiscal discipline to meet debt-to-GDP target of 60%; ii) increased capital spending over the medium term; iii) and fiscal surpluses, which indicates space to withstand shocks.

Reduction in the debt while not an end in and of itself is beneficial to the sovereign and the domestic financial markets. In fact, one of the reasons cited for the sovereign's low credit ratings is the high debt levels which indicate significant challenge in meeting debt payment in the event of shocks. Some overseas entities are restricted from engaging in capital market transactions in Jamaica because of the sovereign's low credit ratings. The push to improve the credit profile, if realized could open up the local markets to greater levels of external capital flows that could help accelerate growth.

Increased capital outlay to improve dilapidated infrastructure complements the overall harmonious economic environment, which can engender greater levels of domestic investments. Given the prevailing global economic environment and the risk associated with weather-related shocks, downturn in domestic economic activities resulting thereof could negatively affect revenue collections. Ten years ago such a scenario would have posed serious downside risks, because of elevated fiscal deficit and debt burden. Increased borrowings by the GOJ occasioned by revenue fallout reverberated in capital markets in the form of rising interest rates owing to the crowding out effect. In an environment of fiscal surpluses, the impact of revenue slippages are likely to have a lower impact on the domestic capital market.

While we welcome the budget and the medium-term posture of the fiscal authority we note with concern the migration of trained public sector workers and the high murder rate. We are cognizant of the fiscal constraints, but the delivery of a proper health care and a first world education system will be imperil if means are not found to retain the services of highly trained and technical personnel. The issue goes beyond salary, as some persons have cited among other things poor working conditions and vindictive behaviour of senior personnel as their reasons for leaving the public service.

On the issue of murders, we are well aware that this serious matter goes beyond hard policing as factors such as mental health, broken family structure and an under-resourced and fully stretched legal system feature prominently in the metrics of variables that impact criminal behaviour and the murder rate. We believe that a place to start to help cauterize the problem is to view the prevailing issue as a mental health problem, and address it as a public health crises. There is a template that is already in place from Honduras which can be adopted and fine-tuned to suit the Jamaica landscape.

There are elevated risks to the budget owing to the outbreak of COVID-19 and the attendant impact on expected GDP growth and revenues. Given the spending profile relative to revenue, we are expecting that the finance minister will present a Supplementary Budget before the end of the financial year to address expected lower than planned revenue intake and additional spending to help contain the spread of the virus.