Cayman Islands Business Environment Update

Keynote Address by the Honourable Chris Saunders, JP
Deputy Premier and Minister for Finance & Economic Development

Wednesday, 12 May 2021 at 10 am
Grand Cayman Marriott Beach Resort

Opening

Good Morning Colleagues. It is my distinct pleasure to speak at this conference and to share the current state of and, prospects for Cayman's economy with you. I thank Mr. Ric Agrella and Mrs. Sheree Ebanks for extending the invitation to me – which is my first official engagement since being appointed as the Deputy Premier, Minister for Finance & Economic Development and Minister for Border Control & Labour.

Today, I want to highlight that despite the closure of our borders and our curtailed Tourism industry, Cayman's economy is well on the road to recovery. Although the hotel, restaurant, transport, storage and communication sectors are projected to contract this year, they will partially recover in 2022 while the financing, insurance and business services sectors show resilience and are projected to continue to expand in 2022.

As the labour-intensive construction and tourism sectors recover, the unemployment rate will continue to decline over the next two years while inflation is projected to increase marginally.

Preliminary indicators suggest that Caymans' economy contracted in real terms by 6.5% in 2020, a sharp decline relative to the growth of 3.8% for 2019. Cayman's economy is expected to recover partially in the current 2021 year, albeit without any meaningful contribution from tourism as international demand remains subdued. However, progress made internationally to inoculate the world population against the COVID-19 virus bodes well for future demand. Barring any further domestic or global shock, "knock on wood", the economy is expected to record growth of 3.2 percent in 2021 before accelerating to 6.3 percent in 2022.

The ***hotels and restaurant*** sector is estimated to have contracted by just under 77% in 2020. The sector is projected to further contract by just over 38% in 2021 before recovering partially. The contractions are in-line with reductions in the sector's operations and are consistent with the closing of our borders and the fallout in major tourist markets.

I would like to recommit that this Government remains committed to rebuilding the sector and by extention our economy, in a safe way for our

residents. We will maintain the existing Global Citizen Concierge programme in an effort to continue the provision of temporary support in the sector over the short term.

The ***transport, storage and communication*** sector is estimated to have contracted by over 14% in 2020. The sector is projected to contract further by 3% in 2021.

The ***financing and insurance*** sector is estimated to have contracted by just under half (0.4%) a percent in 2020. The sector showed some resilience in the pandemic with full services largely maintained throughout. The sector is projected to expand by 3% for 2021 and around 2% in 2022.

The ***business services sector***, which is comprised mainly of legal and accounting services, also remained relatively robust during the crisis. The sector contracted by 3% in 2020, and is expected to grow by 5% in 2021 and around 2% in 2022. This forecast is however clouded by the recent addition of Cayman to the Financial Action Task Force (FATF) grey list and existential threat of being placed on the European Union blacklist. These are areas which Government will continue to navigate with the continued assistance of the Association and other key stakeholders in the industry.

In every crisis there is an opportunity and I believe this crisis has provided us here in the Cayman Islands with the opportunity to restructure and rebuild our economy in a more resilient, sustainable and community-driven way. The Cabinet continues to have discussions with key stakeholders on stimulus measures to boost growth in some sectors. Some of these measures will be included in the Strategic Policy Statement that is currently being developed.

Employment

The unemployment rate rose to 5.2% of the labour force in 2020, in line with the contraction in GDP. This was further aggravated by the collapse of the tourism and transportation sectors which are labour-intensive sectors. Notwithstanding, the rise in the unemployment rate was moderated by the transient nature of some element of the expatriate labour force with unemployed expats leaving the Islands and leaving the labour force. Over the near term the demand for labour is expected to track the GDP growth forecasts with new employment expected from the recovery of labour-intensive industries such as construction and tourism. The unemployment rate in 2021 and 2022 is projected at 4.8% and 4.5%, respectively.

This Administration has commited to refocussing and prioritising Caymanian employment as part of our mandate. This should assist in sustaining the local economy in the short-term by maintaining disposable income and spending locally.

Inflation

The consumer price index (CPI) inflation rate fell to an average of 1.0% for 2020. This was due to reduced pressures on both imported and domestic inflation from the contraction in demand both locally and internationally. Average inflation for 2021 and 2022 is projected at 1.6% and 1.7%, respectively. The relative stability in the forecast for inflation is premised on the expectation of international demand remaining generally subdued over the near term.

Financial Performance and Position of the Government

The impact of the pandemic, along with the prior Adminstration's response to ensuring the health and safety of the people of the Cayman Islands and stimulating the local economy, has had a significant impact on the Government's financial performance and forecast financial results for 2021.

Operating Revenue

By the end of March 2021, Core Government's Operating Revenue totalled $404 million, which was 11% more than the 3-month budget projected.

Postive variances were seen in Mutual Fund Administrator Licence Fees; Exempt Companies Fees; Private Fund Fees; and Stamp Duty on Land Transfers. When combined they accounted for $61 million more than what was budgeted for the first quarter.

However, significant negative variances were seen in:

1. Cruise Ship Departure Charges, which were down year-to-date budget, by $3.0 million or 100%;

2. Other Import Duties were down, against the year-to-date budget, by $3.7 million or 11%;

3. Partnership Fees were down by $2.6 million or 5%;

4. Securities Investments Business Licence Fees were down by $3.3 million or 29%;

5. Tourist Accommodation Charges were down by $14 million or 99%; and

6. Work Permit Fees were down, compared to the year-to-date budget, by $2.7 million or 15%.

Operating and Financing Expenditures

For the three-month period ended 31 March 2021, Core Government's Operating and Financing Expenses totalled $208 million or 6% more than the year-to-date budget:

1. Personnel Costs totaled $90.5 million or 3% less than the year-to-date budget;

2. Supplies and Consumables, excluding Operating Leases, totaled $22 million or 32% less than the year-to-date budget;

3. Outputs from Statutory Authorities and Government Owned Companies totaled just over $34 million and were in line with the anticipated year-to-date budget;

4. Outputs from Non-Governmental Output Suppliers totaled $9.4 million or 29% more than the year-to-date budget. The increase in expense was primarily due to the funding of tertiary medical care for indigents, seamen and veterans;

5. Transfer Payments totaled $34 million or 194% more than the year-to-date budget. The increase in expense was primarily due to overages in spending on scholarships, the monthly stipend to Caymanian tourism workers and support and assistance to Caymanian-owned businesses.

Operating Surplus

For the three-month period ended 31 March 2021, Core Government's Operating Surplus totalled $196 million or 16% more than the year-to-date budget.

It is important to note that a significant proportion of Core Government's Operating Revenue is earned during the first quarter of each financial year – which is when financial services fees are due. Historically, revenue levels taper off as the year progresses.

As such, the Operating Surplus of $196 million is not expected to be maintained as the year progresses. In fact, Core Government is forecast to end the 2021 financial year with an Operating Deficit of $98 million, unless corrective action is taken by Government. The Entire Public Sector is projected yo have a Deficit of $157 million for 2021, again, unless corrective action is taken.

The PACT Government is not comfortable with being in an Operating Deficit position and over the upcoming weeks we will be looking at ways in which the Government can bring this number down.

Bank Balances and Debt Balance

At the end of the first quarter, Core Government's closing bank balances totalled $611 million while Core Government debt balances stood at just under $244 million.

The Debt balance continues to decline with scheduled principal repayments being made. With the Islands' GDP estimated to be CI$4.75 billion at 31 December 2020, its Debt to GDP ratio would be a very favourable 5.1% - one of the lowest in the world. In comparison, Japan has a debt-to-GDP ratio of over 200% and the UK has a ratio of 100% indicating that our local Government has debt under control and, it is very prudent with respect to borrowing.

Compliance with Principles of Responsible Financial Management

As I previously mentioned, for the 2021 financial year, forecasts show that Core Government will comply with all but one of the Principles of Responsible Financial Management:

1. Core Government is forecast to have an Operating Deficit of $98 million – whereas the Government is required to maintain an Operating Surplus. This projection can be reduced as a result of Government's planned intervention with expenditure-reduction proposals.

The Government will however be in compliance with the remaining Principles:

1. Net Worth ratio – where net worth is forecast to be positive at $1.4 billion;

2. Debt Servicing Cost - which includes both interest and principal payments – and is forecast to be 7.8 % – which is within the 10% threshold;

3. Net Debt – the ratio between Government's total debt and bank balances - will be 24% - which is less than the maximum 80% threshold; and

4. Cash Reserves are forecast to be at 95.2 days of Operating Expenditures – which is slightly above the 90-day legal threshold.

As a result of breaching compliance with the Operating Surplus Principle, as required by the Public Management and Finance Act, the Government is now required to get written approval from the Foreign Commonwealth and Development Office before:

1. the Strategic Policy Statement is finalised;

2. any public borrowing or any refinancing of public borrowing is undertaken;

3. proceeding with any project with a lifetime value of more than $10 million;

4. using public assets as collateral as part of any arrangement with a party external to the Government;

5. the hypothecation of any revenue stream; and any

6. divestment of public assets.

The amount of time that the Government has to become fully compliant with the Principles is three (3) years or much longer period of time as can be agreed with the UK Government. The Ministry of Finance aims to obtain the approval of the Foreign Commonwealth and Development Office by the end of June of this year.

Conclusion

The PACT Government is committed to improving the quality of life of our people, building our country and creating a strong and diverse economy.

The PACT Government is committed to addressing good governance and to finding employment for Caymanians.

The forecast Operating Deficit and forecast breach of one of the Principles of Responsible Financial Management is not a financial situation that we are comfortable being in. Having to seek the UK Government's approval on key financial matters is not ideal and is not where we want to be.

Over the upcoming months, the PACT Government will be reviewing ways in which we can improve public finances to pre-pandemic levels.

We will be reviewing ways in which we can reduce the cost of living, continue to support programmes to micro and small businesses and of course, assess when would be the most appropropriate time to re-open our borders safely.

As the Honourable Premier said at the swearing-in ceremony for Parliament, the PACT Government is committed to buiding a community

that is rich in our culture and heritage and building an economy that makes Cayman one of the best places to live and work on this planet.

Thank you.