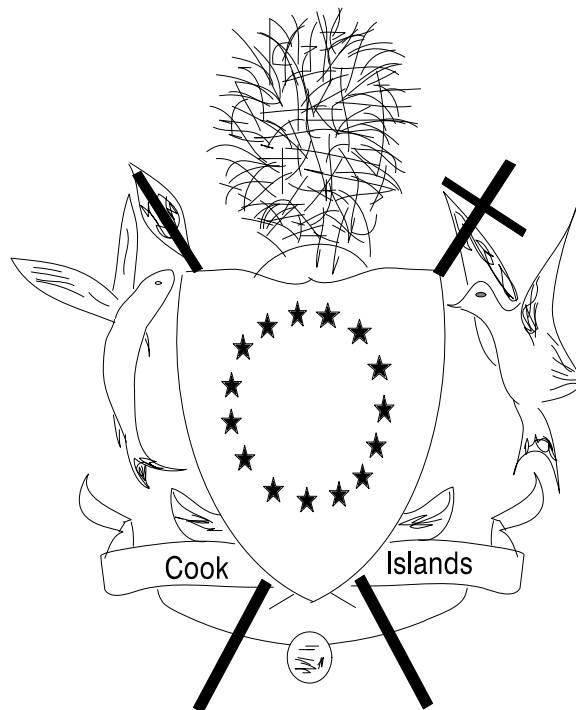

The Cook Islands

BUDGET POLICY STATEMENT

2011/2012



Government of the Cook Islands

31 March 2011

**COOK ISLANDS GOVERNMENT
BUDGET POLICY STATEMENT
2011/2012
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31 March 2011

STATEMENT OF RESPONSIBILITY

I have read the Financial Secretary's Statement of Responsibility and concur with her regarding the preparation of the Budget Policy Statement 2011/2012.

This Budget Policy Statement (BPS) is prepared in accordance with Section 11 of the Ministry of Finance and Economic Management Act 1995-96, which states that the Minister of Finance shall no later than the 31st day of March cause a Budget Policy Statement to be published.

I have reached the conclusion that no comprehensive fiscal forecast is possible with the meaning of section 19(a) of the Ministry of Finance & Economic Management Act 1995-96 (Cook Islands) without disclosure of the anticipated adjustments to appropriations that will be incorporated in the Appropriation Amendment Bill 2010, of which include non discretionary expenditure items. Section 22(2) requires me, as matter of law, to report the above in the Fiscal Update before 31 March 2011.

In accordance with Section 30(2) of the Ministry of Finance and Economic Management Act 1995-96, the Minister of Finance and the Financial Secretary shall prepare and sign a Statement of Responsibility for the financial statements. I accept the overall responsibility for the integrity of the Budget Policy Statement 2010-11 and its compliance with the Ministry of Finance and Economic Management Act 1995-96.

A handwritten signature in black ink, appearing to read 'Mark Brown', with a long horizontal stroke extending to the right.

Honorable Mark Brown
Minister of Finance



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31 March 2011

STATEMENT OF RESPONSIBILITY

This Budget Policy Statement (BPS) is prepared in accordance with Section 11 of the Ministry of Finance and Economic Management Act 1995-96, which states that the Minister of Finance shall no later than the 31st day of March cause a Budget Policy Statement to be published.

In accordance with Section 30(2) of the Ministry of Finance and Economic Management Act 1995-96, the Minister of Finance and the Financial Secretary shall prepare and sign a Statement of Responsibility for the financial statements.

The integrity of the disclosures and consistency with the requirements of the Ministry of Finance and Economic Management Act 1995-96 are warranted in relation to financial statements included within this Budget Policy Statement.

As Financial Secretary, I accept full responsibility for the integrity of the information provided.

Kia Manuia.

A handwritten signature in black ink, appearing to read 'Priscilla'.

Priscilla Maruariki

Acting Financial Secretary

BUDGET POLICY STATEMENT 2011-12

1.0 INTRODUCTION

On 17 November 2010, our people made the decision for change by electing a new Government. Recognising this, Government, is committed to making sure that this change happens by honouring the pledges that we have made prior to taking office. However, we are mindful that doing so will be a challenge. We have inherited an extremely constrained economy where our current surpluses are minimal, and our net worth is outside the range of what this Government considers prudent.

During the term of past Government, the economy was constrained. If we are to achieve our national vision where our people are “To enjoy the highest quality of life consistent with the aspirations of our people, and in harmony with our culture and environment”; we must bring balance back to our economy.

Budget 2011-2012 marks the start of a new development phase with the upcoming Economic Development Summit and the launch of our country’s second National Sustainable Development Plan. Our second National Sustainable Development Plan will highlight the social, economic, environmental and cultural outcomes that our people desire. In pursuing these outcomes, this Government is ready to forge a new growth path and to work tirelessly to build a future in which all Cook Islanders can take pride and share in the benefits that will be accrued in the future.

This Budget is critical as it will set the scene and define the directions going forward. Given our current economic situation, Government’s most urgent task is to put in place measures that will boost the economy in the short to medium term, while at the same time, build the conditions for long term and sustainable economic growth. The focus of this approach is on sustainability and the outcomes over the immediate, medium and longer term, not only in economic terms, but also to ensure that economic development yields the sustainable outcomes in the social, environmental and cultural dimensions in the years to come.

Government recognises that if this is to happen, we must concentrate on building a more vibrant economy capable of producing high returns within a sustainable framework. We need to be more innovative in everything that we do so that the disadvantages of our size, spread and isolation from markets are more than compensated for by the difference we are able to bring to our products and processes.

Our economy needs to be transformed to meet the needs of our people. The first step towards this transformation is to change the role of government in the economy. If we are to develop an economy capable of adapting quickly and being recognised as innovators, government policy making and implementation must also reflect new attitudes.

The Government is therefore committed to following a policy direction that is:

- Active

- Collaborative
- Sustainable and
- Focused

This Government has a vision for the economy which is innovative, exciting, and challenging, but we also appreciate that all the wisdom on economic policy does not rest only with the government. We must work together with the private sector and the community to look at aspects of what needs to be done.

In doing so, we have carefully analysed the past, scrutinized the extensive public consultations related to the review of the NSDP conducted in the past year, engaged the Economic Development Summit Taskforce to conduct further consultations and have called for public submissions to formulate our development directions going forward.

This Budget Policy Statement draws upon these consultations in setting out Government's:

- 1) Medium Term Fiscal Policy
- 2) Budget 2011-2012 Key Strategic Priorities
- 3) Intentions for Budget 2011-2012

1.1 MEDIUM TERM FISCAL POLICY

The Ministry of Finance and Economic Management Act 1995-96 ("the Act") requires Government to state or reaffirm Government's long-term objectives for fiscal policy in its Budget Policy Statement.

The Act sets out the long term principles to ensure that the Government manages and sustains a healthy macroeconomic environment for the Cook Islands. These principles as set out in the Act are as follows:

- Ensuring that unless Crown debt is at prudent levels, operating expenses will be less than operating revenues (Government will run an operating surplus)
- Achieving and maintaining levels of Crown net worth that provide a buffer against factors which may impact adversely on net worth in the future
- Managing prudently the fiscal risks facing the Crown
- Pursuing policies that are consistent with a reasonable degree of predictability about the level and stability of tax rates for future years

Government must pursue its policy objectives in accordance with these principles. These principles are quantified in the Fiscal Responsibility Ratios, setting parameters on government's macroeconomic flexibility. These ratios and trends are discussed in the Fiscal Update section of this publication.

Reflecting the principles of fiscal responsibility quantified and assessed through the 'Fiscal Responsibility Ratios' developed by the Ministry of Finance & Economic Management in 2010, Government will operate within the following fiscal limitations.

- Size of governments pocket
 - Maintaining taxation to GDP ratio of 25% to control the size of governments operating expenditures and limiting the withdrawal of resources away from the private sector
- Expenditure control
 - Continuing to maintain recurrent expenditures within operating revenues to keep within affordability
 - Keeping cost of the public service within 40% of total revenue to ensure that significant sums are flexible for development programs
- Prudence
 - Undertake new borrowings within the country's debt carrying capacity, within 35% of nominal gross domestic product
 - Debt servicing costs for new and existing debt levels are kept within 5% of total revenue noting that the value of debt servicing is expected to increase over the medium term.
 - the rate of debt accumulation will be balanced across the country's debt carrying capacity and the cost of debt servicing

In response, government will undertake the following strategies:

- Review the current major tax mix with a focus on meeting government economic development priorities whilst keeping within appropriate levels and improving revenue collection.
- Running a balanced budget by providing for necessary one off initiatives funded through efficiencies gained in other areas of government operations whilst maintaining a focus on economic investments that generate short and long term returns.
- Managing governments economic investment requirements financed through new debt within the national debt carrying capacity of 35% of nominal gross domestic product. Government seeks to only take on debt where the investment clearly brings about much needed boost to the economy that in turn will cover debt servicing costs.
- Actively engage with donor partners to align development assistance to national priorities, with General Budget Support being the preferred mechanism of delivery

managed through the adoption of the first Cook Islands Aid Policy. This will be complemented by the Public Expenditure Financial Accountability which will demonstrate the strength of government's financial management systems to manage general budget support from donors.

- Continue to put funds into the reserve trust fund building a buffer to protect the net worth of the Crown, whilst at the same time put in place a trust fund mechanism for response, mitigation and adaptation measures that are required as a result of adverse impacts of Climate Change and natural disasters

It is imperative that government continues to pursue its policy objectives based on the principles of responsible fiscal management.

This short to medium term fiscal policy is underpinned by the longer term fiscal policy captured in the Act and is intended to guide investment decisions over the 2011-12 Budget focusing on sustainable and innovative economic investments.

1.2 KEY STRATEGIC PRIORITIES

Although successive Governments in their own ways have advanced our economic development, feedback received from the public has indicated that the right framework to grow and allow the economy to flourish continues to be lacking. Budget 2011-2012 provides the opportunity and platform for government to build the framework for the economy that our people desire. A framework that will in the coming fiscal year, focus on propelling our economy into a higher growth and development trajectory. This will allow us in the outer years to provide resources to invest in further improvements to our peoples' wellbeing. With this in mind, Budget 2011-2012 will focus on the following broad strategic directions:

1. Energise and grow the economy by supporting our key economic drivers and advancing on innovation in potential areas of growth;
2. Enable enterprise by establishing the environment conducive for existing businesses to grow and for new businesses to start, stay and thrive in our communities;
3. Reduce the cost of doing business and cost of living, and increase the disposable incomes of our people;
4. Re-orientate the public sector to better support and respond to the needs of the economy; and
5. Develop infrastructure that will support economic growth underpinned by environmentally sustainable practices.

1.3 GOVERNMENTS INTENTIONS FOR BUDGET 2011-2012

1. Energise and grow the economy by supporting our key economic drivers and advancing innovation in potential areas of growth

Tourism

This Government's recent agreement towards subsidising key airline routes demonstrates its commitment towards tourism as our primary economic driver. However, if the anticipated results are to be achieved, our tourism product needs to be enhanced. Therefore Budget 2011-2012 will:

- See the commencement of the implementation of our Destination Development Strategy which will harness the potential of our culture, creativity and environment in offering our visitors that truly unique Cook Islands experience. Programmes to be developed and implemented in our Pa Enua (Outer Islands) must recognise the uniqueness of each island.
- Provide an alternative port for cruise ships in Rarotonga.

It is Government's view that its investment in tourism together with that of the industry will increase visitor spending and ensure that the benefits ensued are spread across our communities.

Financial Services

Our Financial Services sector has the potential to increase its contribution to the economy. However, it requires a legislative framework and marketing that will improve the attractiveness of our jurisdiction. Therefore Budget 2011-2012 will support initiatives that:

- Update existing legislation and create legislation for new services and products that will add value to our competitiveness as a jurisdiction.
- Increase marketing efforts internationally to raise the profile of the jurisdiction and diversify our client base.

Marine Resources

The Ministry of Marine Resources has recently made good progress in improving the economic return from our fisheries and marine resources as evidenced by the recent implementation of the bone fishing initiative in Aitutaki. However, there remains untapped potential in this area. Therefore Budget 2011-2012 will support initiatives that:

- Expand and diversify offshore fishing via designated and exploratory licence arrangements.
- Support and rejuvenate levels of pearl production in Manihiki lagoon
- Strengthen marine eco-tourism links in all islands
- Improve the management of our non-living marine resources
- Support small scale fisheries and aquaculture initiatives to conserve our resources and culture, promote healthy nutrition and substitute imports.

Agriculture

Government recognises the potential for agriculture to improve its impact on the economy particularly through the revitalisation of agriculture in the Pa Enua and import substitution. However, much work is needed to establish the economic viability of revitalising agriculture in our southern group islands. Therefore Budget 2011-2012 will support initiatives that:

- Re-examine and determine the way forward for agriculture in the Cook Islands and the appropriate role of government in its development, including the focus towards growing southern group contribution to the economy, and the working relationships between Growers Associations and other key stakeholders.

- Support the adoption of biological and organic agriculture.

Culture and Creative Industries

Government recognises the potential for economic growth from our Culture and Creative Industries. Budget 2011-2012 will therefore support initiatives that will allow this sector to grow through:

- Establishing the right policy environment to encourage innovation and creativity
- Strengthening linkages between culture and creative industries and other key drivers of the economy.
- Actively promoting our cultural heritage

Research and Development

Government is mindful that the cornerstone of innovation is research and development. To build an innovative economy, Budget 2011-2012 will support research and development initiatives that improve our products and processes and thus, economic return from the key drivers of our economy particularly in the areas of tourism, financial services, marine resources, agriculture, culture and creative industries. Additionally, research and development in other critical areas that support the economy such as social practises and environmental development especially with regard to climate change will also be encouraged.

2. Enable enterprise by establishing a conducive environment for existing business to grow and for new business to start, stay and thrive in our communities

Policy, Legislation and Regulation

It is this Governments desire that our economy must be private sector led. However, government plays the critical role of establishing the policy, legislative and regulatory frameworks that promote competition, innovation, and investment; and also protects consumers and employees. Government will ensure safety, security oversight and surveillance of the aviation and maritime systems, in compliance with international transport regulations. Therefore, Budget 2011-2012 will support initiatives that develop or strengthen the policy, legislative and regulatory frameworks in the following areas:

- Culture and Creative industries
- Agriculture and Horticulture
- Fisheries and Marine Resources
- Foreign Investment to attract appropriate investors and new money into the economy
- Competition and consumer protection
- Labour Relations
- Immigration (including visas for overseas students and retirees)
- Superannuation Scheme
- Transport
- Trade and Commerce
- Support local contractors in implementing infrastructure projects
- Renewable energy projects
- Telecommunications

- Ports and Airports

Taxation

Government recognises that the tax regime of the country also has an impact on enabling enterprise. Therefore Budget 2011-2012 will:

- Examine our taxation regime and explore options which will enable economic development and also improve our people's livelihoods both in Rarotonga and in the Pa Enua.

Telecommunications

The Government is well aware that telecommunications will play an increasing role in shifting from a service economy to a knowledge economy. The Government therefore recognises that existing and future telecommunications needs must be addressed. Budget 2011-2012 will focus on clearly articulating policy that:

- Ensures that the consumer is provided with a telecommunications service that is fair, of high quality, affordable and fast.
- Will review all aspects of the telecommunications industry with a view to determine the model that provides best service.

3. Reduce the cost of doing business and cost of living, and increase the disposable income of our people

Cost of finance

The cost of finance is a major burden for both existing businesses and potential entrepreneurs. Assistance in alleviating this burden is essential. Therefore, Budget 2011-2012 will support initiatives that:

- Identifies options that will provide relief for businesses with a priority to reducing interest rates.
- Identify and put into place mechanisms that will allow for the provision of finance at lower interest rates on development terms and conditions.
- Actively collaborate with the financial institutions to establish mechanisms that allow the Cook Islands to have some influence on its domestic monetary policies.

Cost of Energy

High energy costs impact on the cost of doing business and the cost of living in the Cook Islands. This Government is committed to energy independence in the long term by harnessing our potential for renewable energy. Therefore, Budget 2011-2012 will support initiatives that reduce energy costs and vigorously pursue the utilisation of renewable energy through:

- Developing an integrated and comprehensive energy policy that covers fossil fuels, renewable energy and transport.
- Supporting renewable energy initiatives such as Te Aponga Uira's 100% renewable energy programme.
- Exploring the provision of incentives to encourage the use of renewable energy in households and reduce energy costs.
- Engaging actively with our development partners to support our efforts in renewable energy.

Increasing disposable incomes

The Government is committed to increasing the disposable income of our people. Therefore, Budget 2011-2012 will:

- Examine the impacts of an incremental increase in the minimum wage and identify and implement the best options for such an increase.

4. Re-orientate the public sector to better support and respond to the needs of the economy

Managing government's external relations

Government's agenda for development is an ambitious one and our strategic objectives cannot be achieved through our own hard work alone. Over the coming year, it will be important for Government to continue to intensify bilateral and multilateral efforts to promote cooperation and partnerships with other governments and organisations in support of our development initiatives, including promoting opportunities for the private sector, reducing the international costs of doing business for our private sector, and addressing climate change, renewable energy and other Cook Islands concerns.

While continuing to strengthen our relations with New Zealand and other regional countries and territories, special effort will be made to intensify our relations with European and Asian partners. In consultation with the private sector and other stakeholders, Government will also adopt the Cook Islands' first formal trade policy.

Government will also adopt a progressive immigration policy and enact immigration legislation that would introduce new economic development initiatives supporting our overall development strategies. Those new initiatives will be assisted by the introduction of a new border and immigration application management system this financial year.

Improving service delivery, accountability and transparency

Government is determined to improve service delivery, accountability, and transparency in the public service. To this end, it has begun the comprehensive functional review of the entire public sector. However, Government has also identified problematic areas that must be addressed sooner rather than later. These reviews will look at establishing the best solutions to improve service delivery to achieve not only our economic aspirations but also the overall development outcomes that our people expect on both Rarotonga based outputs and governance structures in the outer islands.

As a critical step to improving accountability and transparency, Government will in the 2011-2012 fiscal year work towards ensuring that financial audits of all its agencies are up to date.

Budget 2011-2012 will seek to improve our planning and budgeting processes by strengthening linkages at the national, sectoral and agency levels and integrating cross-cutting development issues into our processes of policy development and implementation. In doing so, we are committed to integrate cross cutting priority issues such as gender, climate change, and disaster risk management into planning and budgeting processes. It is anticipated that this will result in more robust and balanced policy directions.

In addition, Government has identified the need for better economic forecasting and statistical analysis to justify, drive and achieve the results that are desired for economic and social development, as well as to improve monitoring and evaluation. Therefore, Budget 2011-2012 will support initiatives that will lead to this end.

Building resilience to climate change

Government acknowledges climate change as one of the biggest threat to the long term survival of our islands. In order that our country can build the adaptive capacity required to address climate change effectively, Budget 2011-2012 will establish a designated climate change division to better coordinate programmes that target the climate change related vulnerabilities of our communities.

Develop infrastructure that will support economic growth

Government recognises the role of infrastructure development in accelerating and supporting economic growth as it is often the most significant investment in any budget. Our endeavours in this area must be consistent with Government's vision for high yield investments whilst taking into consideration the impacts on our environment. Budget 2011-2012 will progress on the following infrastructure developments:

- Improve the project planning and implementation for all infrastructure projects
- Re-examine key findings of the Preventative Infrastructure Master Plan including a governance framework
- Completion of policies and updating of relevant legislation and regulations
- Strengthening waste, recycling and sanitation policies and delivery mechanisms
- Advance medium to long term planning for investment in the water sector, including upgrade of existing intake systems
- Improve the strategic and operational management of our assets
- Implement the road and water program
- Implementing renewable energy initiatives
- Implement the upgrade of Mauke and Mitiaro harbours under Cyclone Recovery and Reconstruction Program and
- Identify required ICT improvements.

Other considerations for Budget 2011-2012

Human Resource Development

Government recognises that economic and social development must go hand in hand. Just as economic growth is important to achieving and sustaining good social outcomes, human and social capital are vital to sustainable development. Government is therefore committed in Budget 2011-2012 to continue on improving educational outcomes in our schools, vocational training and tertiary level through sustaining the implementation of the Education Master Plan with a particular emphasis on building a culture of enterprise and financial literacy in collaboration with other key stakeholders including BTIB, Chamber of Commerce and the private sector, and the Banking sector.

1.4 CONCLUSION

The new government has inherited some challenges since coming into office. However it has made a commitment to working together with all our stakeholder partners to set this country on the path to prosperity.

Early in its tenure, your government has demonstrated its ability to be bold and decisive through its commitment to supporting our tourism industry initiative to underwrite critical airline tourism links.

We will redirect our resources into our priorities. The forthcoming Economic Summit will be a platform through which the government will seek a mandate from our people to pursue identified priorities.

We are committed to working closely with all our development partners to align our combined efforts and resources to achieving the national priorities of the Cook Islands. We have a shared appreciation for the role of investment and enterprise in underpinning growth; and we share a common commitment to improve service delivery and build a strong and competitive economy.

Government can achieve its aspirations, through the implementation of prudent economic policies intended to ensure continuous stability and stimulate growth within an environment of good governance.



Honourable Mark Brown

Minister of Finance

1.0 ECONOMIC UPDATE

This Economic Update is intended to provide an overview of the economic performance of the Cook Islands economy focused on the current fiscal year 2010-11 and the outlook going forward. Given new data available (December quarter 2010), this is an update of the analysis provided at the time of the Half Year Economic & Fiscal Update (HYEFU) published in December 2010. Commentary is held constant where data and anecdotal evidence remains the same as at the time of the HYEFU.

As per previous Economic Updates, this update will provide an overview of trends and movements in Gross Domestic Product, and key industries inclusive of tourism, marine resources, agriculture, trade and banking & finance.

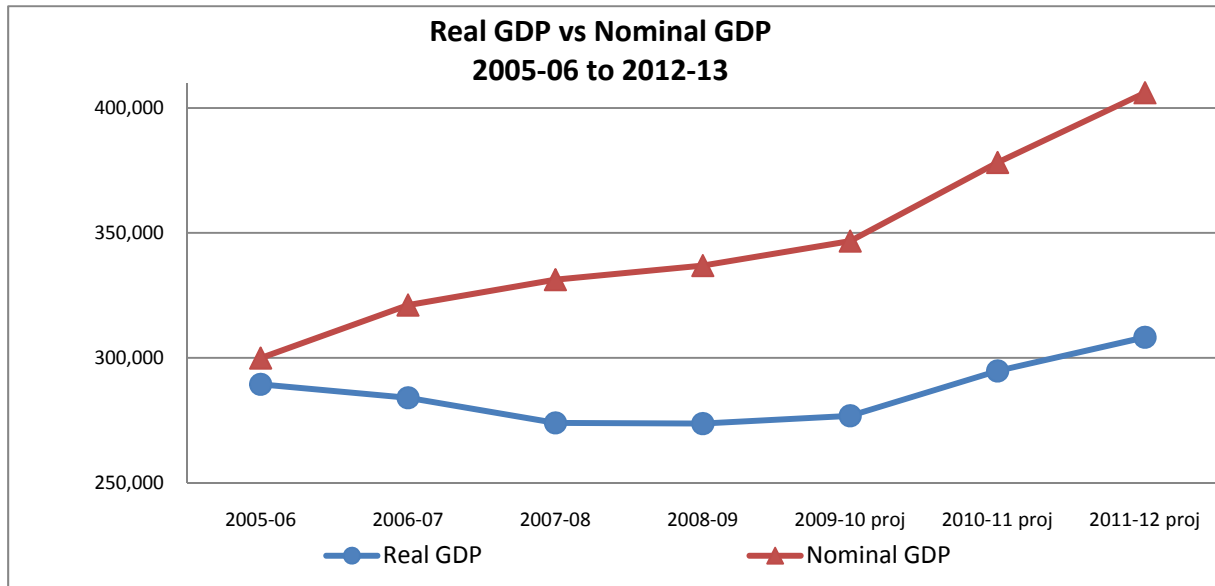
Despite recent natural disasters in a number of of the Cook Islands tourism markets, visitor arrivals have continued to exhibit strong consistent growth rates over the past quarter keeping in line with projections made at the time of the HYEFU. It is expected that this trend will continue over the medium to long term in conjunction with the recent commitment to increase support by Government to the Tourism industry.

Price rises measured through the Consumer Price Index (CPI) have been revised downward to reflect minimal movements over the first three quarters in the current fiscal year, however the full reflection of global increases in oil prices, given the lag in hitting the Cook Islands economy, is mirrored in the upward revision of CPI movement in the outer years. Revisions to CPI have been reflected in the growth rates for nominal projections on GDP, trade and banking and finance.

In general, the Cook Islands economy has returned to positive growth following a period of contraction to 2009, however there are increased risks to sustainability of solid growth given recent natural disasters and oil price rises beyond our control. The heavy reliance on global markets for imported products and tourism demand causes the Cook Islands to be vulnerable to slight shifts in global markets. Therefore any negative impacts flowing through the global markets will see the Cook Islands revisit its projections to adjust accordingly.

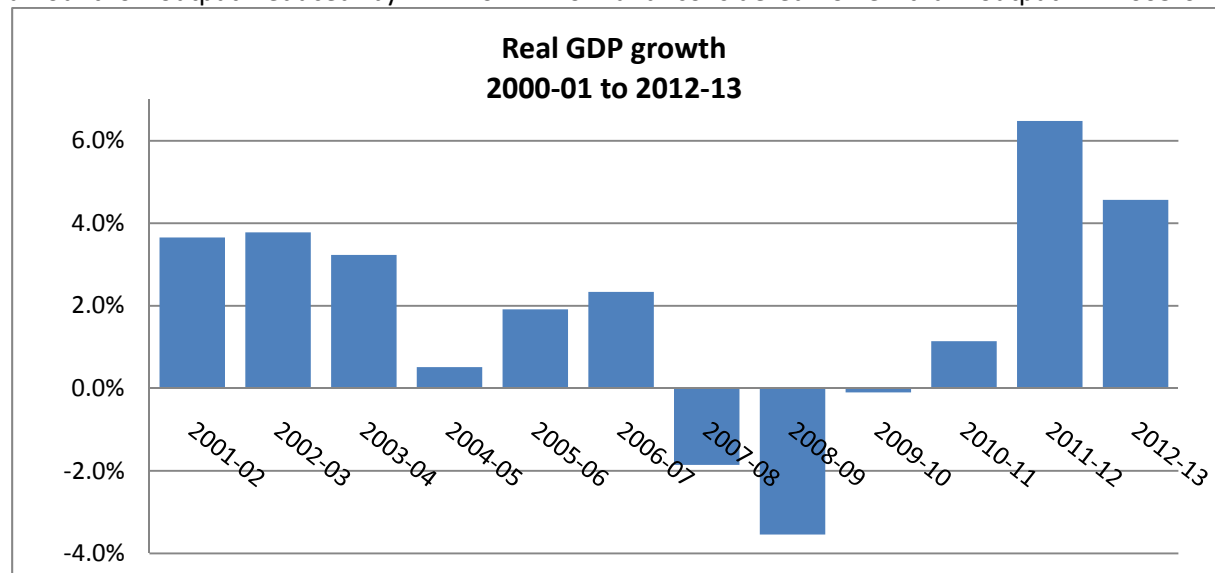
1.1 Gross Domestic Product

Gross Domestic Product (GDP) is used as an indicator to assess the performance of an economy over time. It measures the NZD value of the output of the economy. A growing economy in real terms indicates higher economic activity translating into higher incomes and subsequently taxation for the Government¹. GDP is an annual statistic and thus only gets updated once a year. Over the year performance in the tourism, marine, trade, banking and agriculture provide an insight into economic activity.



Real GDP

After a period of relatively stable growth, the economy contracted over 2007-08 to 2009-10. The amount of output reduced by NZD10.1million and considered lower than output in 2003-04



predominantly due to the impacts of the global economic crisis on general demand for the economy's output and the continual increase in the value of imports as an outflow.

The estimated value of real GDP in 2010-11 is NZD276.8million. Without a change in fiscal policy or rapid turn-around in global demand, it would be expected that growth within the economy in real terms would be minimal.

As reported in the HYEPU, Government has made a policy decision to significantly increase support to growing the tourism industry through underwriting airline linkages to Sydney, Los Angeles and Nadi underpinned by marketing funds (Tourism Growth Strategy).

Given the economy is largely based on tourism which has strong flow on effects to all other sectors, it is estimated that growth in the outer years will improve significantly. As such, based on visitor arrivals and revenue collections to date, growth at year end 2010-11 is estimated at 1.1%, with 6.5% and 4.5% in the outer years reflecting the full impact of the Tourism Growth Strategy.

Nominal GDP

The Nominal Gross Domestic Product measures the value of all the goods and services produced in an economy expressed in current prices.

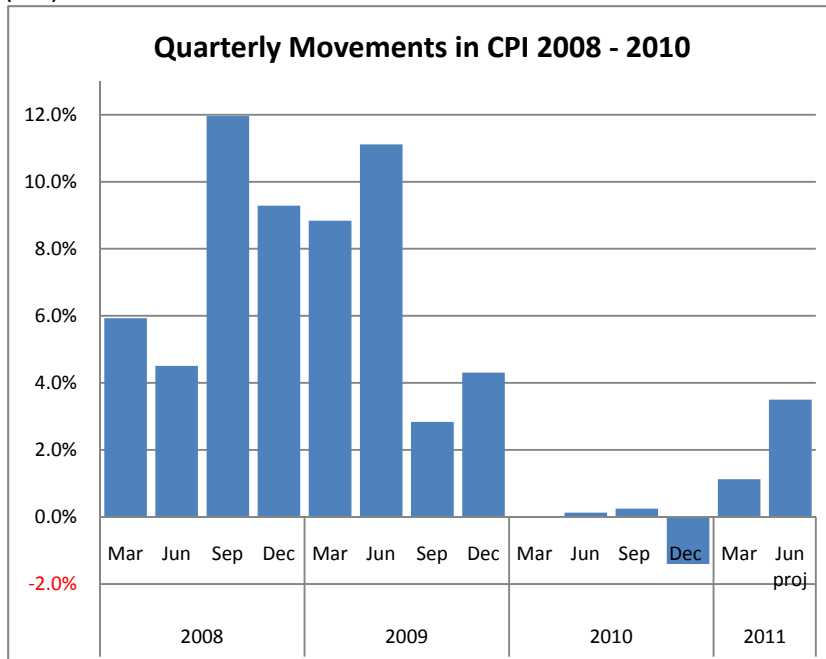
The rate of inflation has been revised since the HYEPU to account for movements in price to date and the expectation of higher oil prices from June quarter 2011. The economy is expected in nominal terms to grow at 2.0% revised downwards from 2.9% in December 2010. It is expected that growth in the outer years will be 11.0% and 6.6% reflecting the catch up in the upward movement in the global oil prices in 2011-12 and 2012-13. Noting this, the significant increase in 2011-12 is due to a bounce-back from a low base.

Table 1.0: Economic Indicators

Economic Indicators					
	2008-09	2009-10	2010-11	2011-12	2012-13
	<i>Actual</i>	<i>Actual</i>	<i>Estimate</i>	<i>Proj.</i>	<i>Proj.</i>
Economic Activity					
Nominal GDP (\$'000)	331,300	336,900	343,566	381,249	406,558
% Change	3.2%	1.7%	2.0%	11.0%	6.6%
Real GDP (at Constant 2006 Prices, \$'000)	274,000	273,700	276,800	294,800	308,200
% Change	-3.5%	-0.1%	1.1%	6.5%	4.5%
Inflation					
Consumer Price Index (base Dec. 2006 = 100)	115.7	117.7	118.8	124.4	127.9
% Change	10.3%	1.8%	0.9%	3.5%	3.0%
Construction/Capital Investment					
Commercial Building Approvals (\$'000)	12,200	3,310	2,806	3,114	3,320
Residential Building Approvals (\$'000)	11,958	8,488	9,643	10,701	11,411
Productive Sector Indicators					
Visitor Arrivals	96,900	99,500	104,100	117,619	125,577
% Change	1.4%	2.7%	4.6%	13.0%	6.8%
Estimated Visitor Expenditures (\$'000)	174,500	179,100	208,100	235,200	251,200
Pearl Exports (\$'000)	1,750	1,570	1,850	1,570	1,570
Fish Exports (\$'000)	2,700	3,130	4,040	4,160	4,280
External Sector					
Merchandise Trade Balance (\$'000)	(240,500)	(344,100)	(349,700)	(388,900)	(415,000)
Services Trade Balance (\$'000)	241,500	247,300	277,600	312,400	333,400
Exchange Rate (US\$ per NZ\$, December 2010)	0.639	0.685	0.756	0.756	0.756
Financial Sector (at end of financial year)					
Private and Public Enterprise Deposits (\$'000)	226,800	221,600	226,000	250,800	267,500
Private and Public Enterprise Loans (\$'000)	297,300	288,700	294,400	326,700	348,400

1.2 Consumer Price Index (CPI)

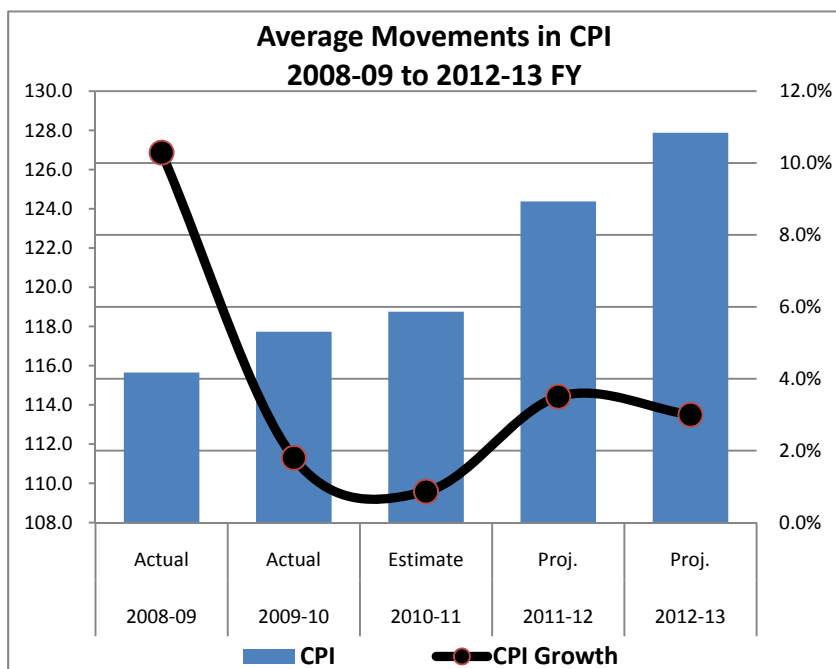
General price increases are measured within the Cook Islands economy by the Consumer Price Index (CPI).



On a quarterly basis movements in price over the first three quarters of the fiscal year to March 2011 have been slight indicating an average movement in price of -0.4%. Despite slight upward movements in the prices of food, apparel and tobacco & alcohol groups, downward movements in the cost of transport, specifically international travel, have pushed overall price downward.

The last quarter of the fiscal year (quarter on quarter in previous year) is expected to hit a high inflation of around 3.5% to reflect heavy movements in the price of oil in the global markets. This is given a lag effect of the global increase in oil prices in the Cook Islands economy of 1-2 quarters.

The effects of the significant movements in the price of oil on the global market is expected to be reflected in 2011-12 where CPI projections will be rebounding off a much lower base from 2010-11. It is expected that the implications of the oil price rise will be wide spread and will hit the pockets of



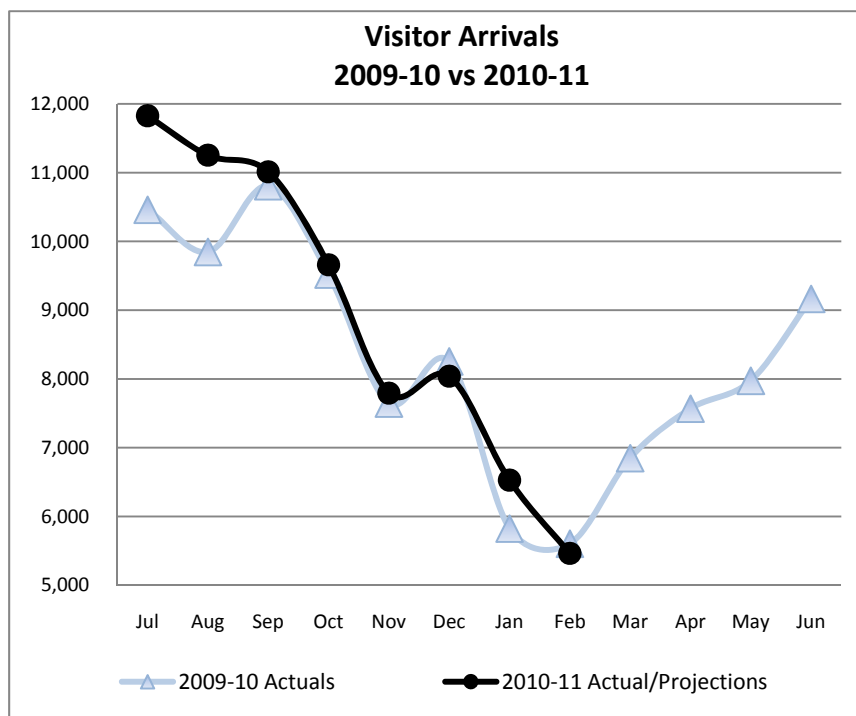
both businesses and households and may force more concerted consideration towards renewable energies and cost savings measures.

At the time of the HYEFU2010 CPI was projected to increase by 1.8%, however given the year to date movements in price and despite an expected increase in the June quarter 2011, the average increase in CPI for 2010-11 is projected to be downgraded to 0.9%. Going forward, prices are

expected to quickly push upwards in the outer years by 3.5% and 3.0% respectively, reflecting a catch up in the upward movement in oil prices globally.

1.3 Tourism

As the main driver of economic activity in the Cook Islands, investment in the Tourism industry has been a priority over the last year to stimulate economic activity within the sector and the flow of benefits across the wider economy.



Activity in the tourism industry is measured by the number of visitor arrivals on a monthly basis and assessed in comparison to earlier estimates and compared to previous year's performance.

Arrivals from July 2010 to February 2011 are 5.3% up over the same period of the previous year and are in line with projections made at the time of the HYEPU in December 2011, despite a

slight fall in February 2011. This fall is largely driven by the New Zealand market and is assumed to reflect a flow on impact in response to from the Christchurch earthquake in February 2011. This is expected to be temporary noting that marketing campaigns have been put in place in the New Zealand market in an effort to pull up numbers over the short term given February to May are the seasonal lows.

The trend in the Australian market continues to show consistently increasing visitor arrivals. Cook Islands Tourism Corporation will be rolling out a significant marketing campaign in this market aimed at encouraging people to opt for short term travel continuing on through the year, resulting in the spreading out of seasonal flows and supporting the direct link to this market via Sydney.

Although there is an expectation of higher fare prices given rising oil costs, the marketing campaigns have been orientated towards the higher yield passengers to mitigate this risk.

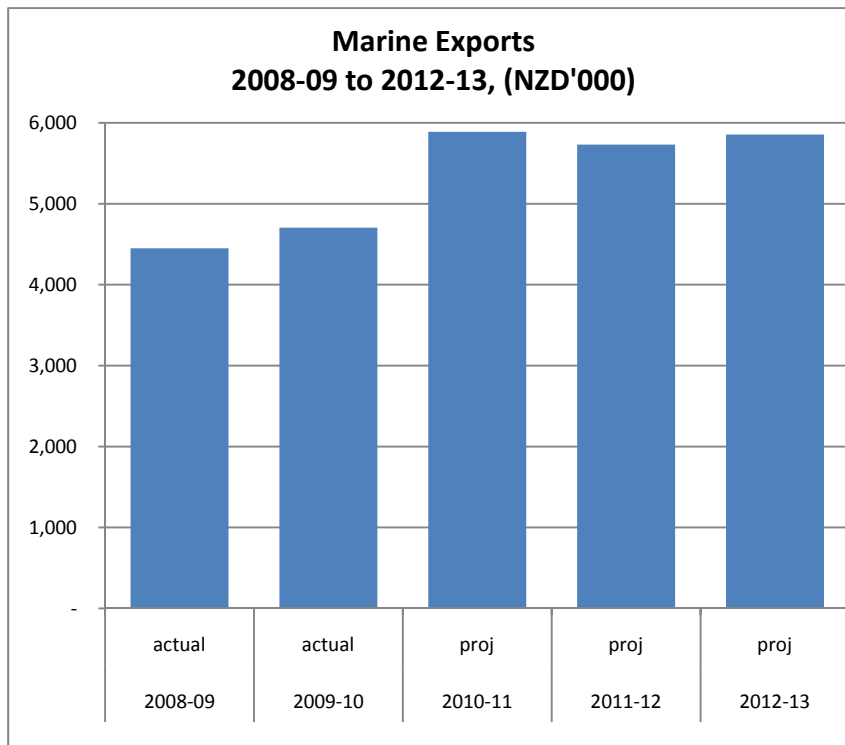
The full effect of the marketing under the Tourism Growth Strategy initiatives and direct flight guarantees is expected to be reflective in very significant gains of 13.0% in 2011-12 and 6.8% in 2012-13.

In supporting the industry the Cook Islands Tourism Corporation is currently working with the industry to review the 'Tourism Accreditation Scheme', in redefining goals and objectives and developing a system that accommodates this. The Cook Islands Tourism Corporation is also due to launch revitalised website which is both comprehensive and informative providing travellers with a

tool that is user friendly, efficient and cost cutting in finding an accredited products and experience in the Cook Islands.

In acknowledging oil price rises and the management of this risk to visitor arrivals, projections for 2010-11 going forward remain as reported at the time of the HYFEU in 2010.

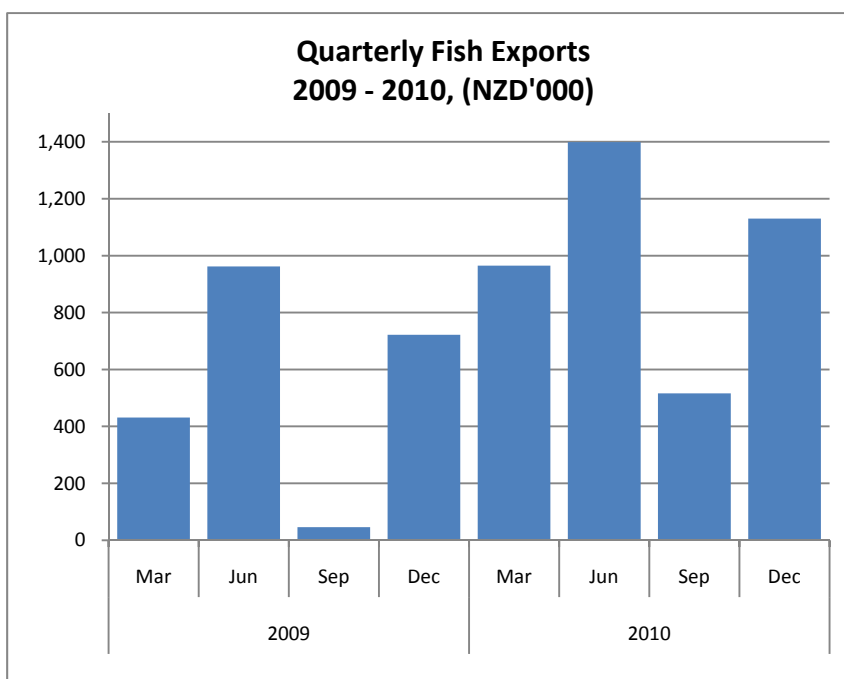
1.4 Marine Resources



The Marine sector in the Cook Islands is made up of mainly tuna fisheries and pearls. The most recent measure of the Marine sector’s contribution to GDP is for 2009 where it is estimated to have a combined value of NZD7.5million.

Exports of marine produce are also assessed on a quarterly basis. The most recent statistics value marine exports in 2010 at \$5.6million, indicating a slight turnaround in activity in the two years mainly driven by growth in fisheries.

1.4.1 Fishing



The Cook Islands fishing industry continues to be serviced by the Northern and Southern fleets, consisting of 34 and 4 licensed vessels respectively. The Northern fishery lands the majority of its catch in Pago Pago with the remaining dispersed in smaller markets in Japan, Thailand and Brazil.

The Cook Islands exports around \$3.6million worth of products to Japan, which is inclusive of fresh

fish and pearls. The industry is confident that despite the natural disasters and the recovery in Japan, exports will continue or be rerouted to other markets.

For 2010 the Ministry of Marine Resources (MMR) has revised its catch estimates upwards from the northern fishery from 4,000 metric tonnes (mt) as reported at the time of the HYEFU to 6,000 – 8,000 mt and is expected to exceed the catch estimates in 2009. This is also reflected in the December quarter 2010 export of fish valued at \$1.1million pushing up overall projections of exports of fish from \$3.6million to \$4.0million in 2010-11.

In an effort to further increase fisheries exports from Rarotonga, the MMR is putting in place a rebate scheme to encourage the larger distant water fishing nations currently operating in the northern fishery to invest resources into onshore processing in Rarotonga. Progress of this initiative will be assessed over 2011-12.

As reported in the HYEFU in December 2010, MMR continues to seek the Cook Islands accreditation to the European Union market. Access to this provides the Cook Island with the benefits of a higher value fishery and quality recognition. The current status indicates that the Cook Islands is already in a good position to meet the first criteria required to certify that its fish exports are compliant against illegal, unreported or unregulated (IUU) certification. The second criteria in regards to food and safety has much work still to be done for the Cook Islands to be accredited by the European Union as the competent food safety authority and there remains about 80% more of the criteria that needs to be fulfilled.

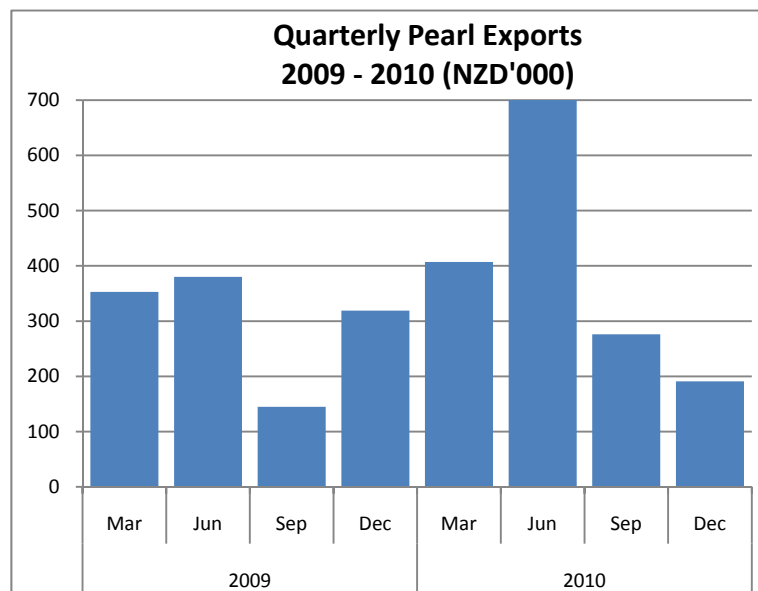
As reported in the HYEFU in December 2010, the MMR will regulate and license a sports fishery for the bonefish on Aitutaki and Manuae. This was expected to be launched in February 2011 at the time of the HYEFU, this has now been extended to April 2011. Industry expectations drawn from the business case suggest a potential contribution of \$2.5million to the Cook Islands economy, however this will be assessed over time.

Overall, forecasts for fishing exports remains positive and estimates for 2010-11 are expected to increase over estimates at the time of the Half Year Economic & Fiscal Update 2010. This is a result of recent growth gained through the December 2010 exports. In the outer years exports are expected to grow in line with growth in nominal GDP discounted for increases domestic consumption to reflect higher visitors and associated demand as a result of the Tourism Growth Strategy.

1.4.2 Pearl

Cook Islands pearls are sold both domestically and via export markets. It is difficult to quantify the size of the domestic market. Therefore performance of the industry is assessed by examining export trends over time. Pearl exports make up around 22% of total exports.

Since the time of the Half Year Economic & Fiscal Update 2010, recent quarterly data for December 2010 value total exports for 2010 at



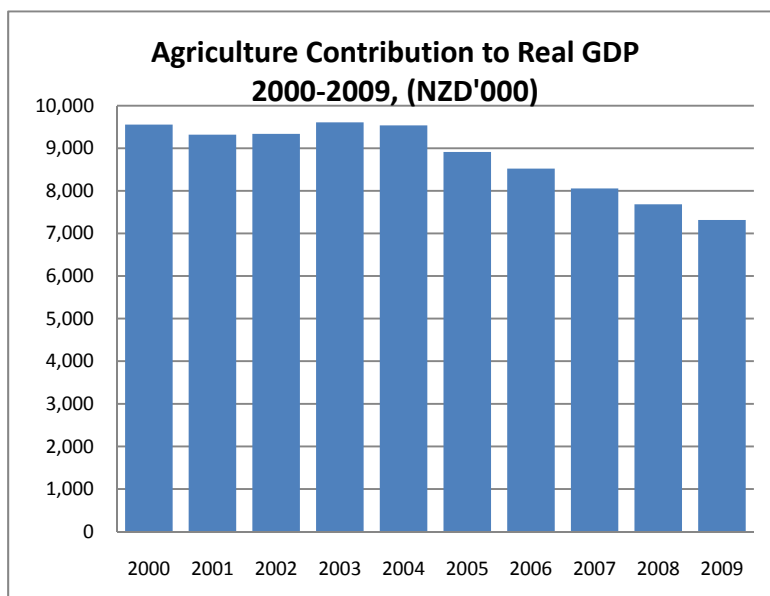
\$1.6million, slightly lower than expected at the time of the last update, however still 31.6% higher than 2009. Estimates of the value of exports over the 2010-11 financial year have also been revised downward from \$2.0million to \$1.8million, yet again still estimated to come in 17.8% above 2009-10.

As reported in the Half Year Economic & Fiscal Update 2010, without any new investments to stimulate production, pearl farming and production is expected to remain flat over the medium term. The availability of funds to assist farmers with capital investments and cash flows is required to sustain growth. Access to inputs is limited which has been the main driver behind a huge portion of inactive licensed farmers. Unless something is done about this, a high proportion of farmers will remain inactive in pearl farming and production.

At present, the Cook Islands Pearl Authority in cooperation with the MMR have jointly submitted a proposal to an external party to seek support for revitalising the long term viability of the Cook Islands Pearl Industry by implementing key marketing, production, and capacity building initiatives. This proposal is still in the process for consideration since the release of the Half Year Economic & Fiscal Update 2010. Progress will be confirmed at the time of the Budget Estimates in June 2011. In the event this funding is secured, pearl production is expected to significantly improve which should result in increased production, increased exports and increased economic benefits to the Cook Islands and those directly involved in the industry.

1.5 Agriculture

The agriculture sector is made up of a large informal sector and thus its total contribution to the economy is difficult to quantify. The supply and demand for produce is predominantly based in Rarotonga.



As demonstrated in the Half Year Economic & Fiscal Update in December 2010, GDP data indicate agriculture contribution to the economy in real terms and in 2009 was NZD7.3million accounting for only 2.7% of GDP, however declining overtime. The majority of produce is consumed domestically with only a minor volume being exported overseas.

Export Market

In 2010, NZD1.1million worth of agricultural products were exported to markets in Japan, Hawaii, New Zealand and Australia. The products are pawpaw, noni and maire eis contributing \$25,000, \$971,000 and \$58,000 respectively.

Noni continues to be the largest agriculture export, however the total proportion of noni exports has declined constantly over the past 2 years. In 2010 almost 100% of total noni were exported to

Japan, with declines in other smaller scale markets including Chile. Given the recent impacts of the natural disasters in Japan and on its economy, demand for noni exports will cease over the coming months and will directly impact suppliers who rely on this export market.

Japanese importers have advised the Cook Islands to halt exports to Japan for a period of 3 months, a potential loss in export revenue of around \$0.3million based on the average over the last 3 years for the March quarter. However, demand following this timeframe remains uncertain. Advice from the industry suggests that at this stage there is limited flexibility to sell surplus produce in other markets.

Given the product is slow to perish if stored appropriately the impact on the individual grower is expected to be a cash flow issue if alternative markets are not found and cannot be attracted through lower pricing.

The Ministry of Agriculture and the Cook Islands Noni Marketing Group (responsible for consolidating the sale and marketing of Cook Islands noni products) are positive that the Japanese market will bounce back after the halt period and are currently advising growers on how to manage over this period.

Domestic Market

As reported in the Half Year Economic & Fiscal Update 2010 fresh fruit and vegetables remain the main agricultural produce traded on the domestic market. Surplus demand is met through imported produce from overseas markets.

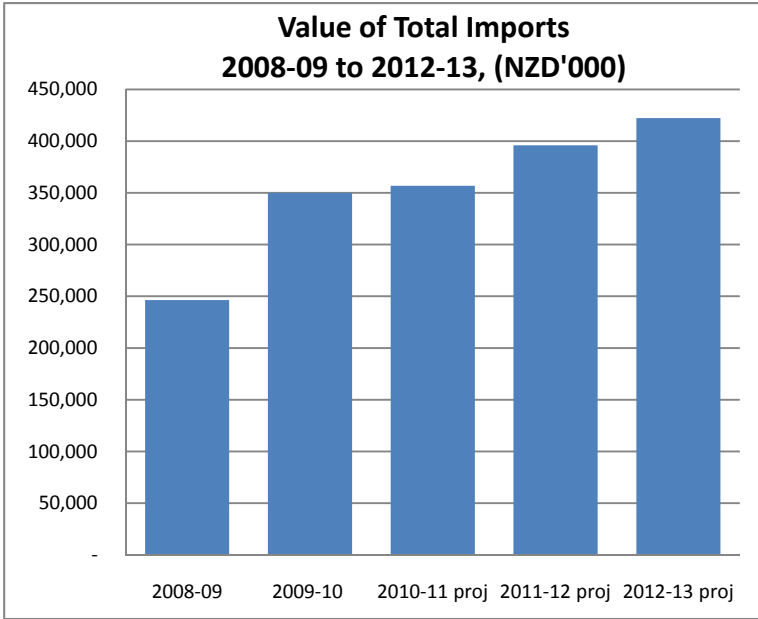
Further growth in demand for fresh produce is expected to come from the tourism industry under the Tourism Growth Strategy. There is potential to strategically increase production to cater for the expectation of increased demand and reduce the import substitution gap. If concentrated efforts are not made to increase domestic supply, reliance on imported produce will deepen and limit the spread of economic returns to the agriculture industry from a higher number of visitors under the Tourism Growth Strategy.

The existing program to expand supply in the Southern Group islands under the Te One Kura project with an overall objective of import substitution is intended to be re-examined including the role of Government in the agriculture sector. Difficulties with the project include appropriate infrastructure, business cases and organisation. Until the private sector re-orientates itself to fill the gap of import substitution, projections are that growth in imported produce will increase in line with growth in the economy.

1.6 Exports and Imports

Imports

The import leakage for the Cook Islands is estimated at around 58%, so for every \$1 spent in the Cook Islands, \$0.58 cents leaks out of the economy. This is because of the Cook Islands heavy reliance on imported products to meet local demand including demand driven by the tourism industry. The Cook Islands imported a total of \$408million worth of merchandise in 2010.



Import volumes were predominantly made up of minerals, oil (36.7%), machinery, transport and equipment (17.4%) and miscellaneous manufactured goods (14.4%). Over 50% of all products are imported from New Zealand followed by other suppliers in Fiji and Australia.

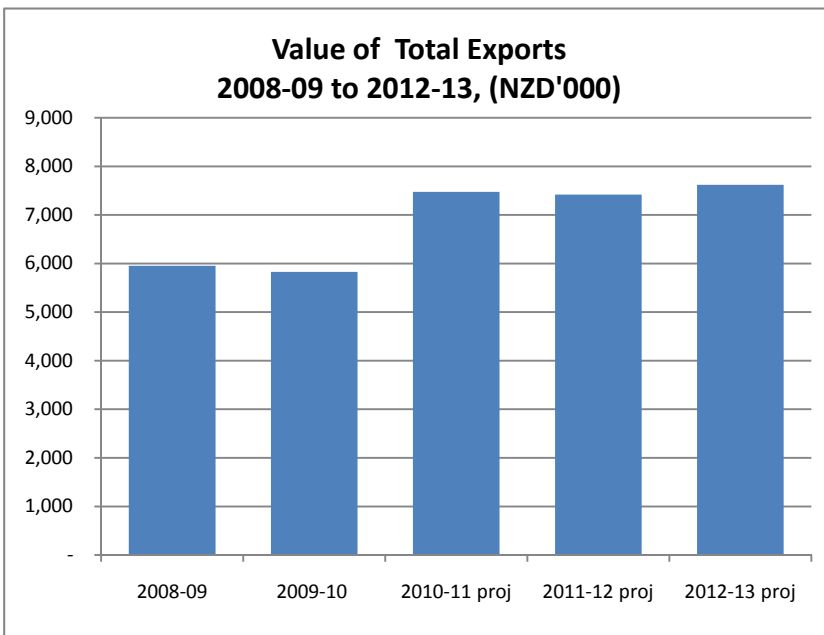
As per section 1.2 (Consumer Price Index) of this Economic Update, projected rises in the cost of oil will be translated into higher freight costs expected to cause the value of imports to significantly rise in the June

quarter 2010-11 and on to the first three quarters of 2011-12.

Projections for imports in 2010-11 will continue to be in line with nominal GDP. The expected increase in visitor numbers as a direct consequence of the Tourism Growth Strategy will place heavier demand for imported produce. A market gap presents itself and moves to fill this demand through local produce which will relieve some pressure on the deepening of the trade deficit through import substitution potentially pulling down the import leakage.

Exports

As in previous updates the main exports out of the Cook Islands is predominantly fish, pearls and agricultural products. In 2010 contributions to total exports were as follows; fish 58.1% (\$4.0million), black pearls 22% (\$1.6million) and agricultural products 14.7% (\$1.1million). Total exports in 2010 exceeded 2009 levels by 62.9%.



The trend in each of the export industries are discussed in detail in sections 1.4.1 (Fish), 1.4.2 (Pearl) and 1.5 (Agriculture) of this update. Consolidating these statements, it is expected that fish and pearl exports will continue to grow moderately over the remainder of the financial year but may be limited by domestic consumption, whilst agriculture exports will be halted over the June quarter in 2011 given the impacts of the Japanese

natural disaster on the demand for noni exports estimated to set back the industry by around \$0.3million.

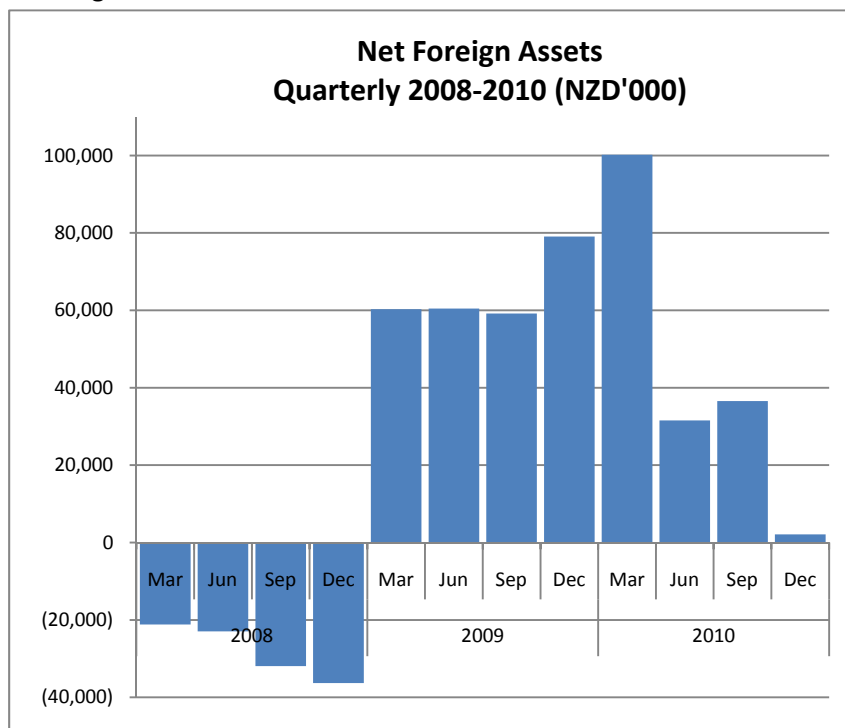
Total exports for 2010-11 is expected to be 23.5% above 2009-10 given the balancing out of the one off impact of non export of fish in the September 2009 quarter, the one off increase in pearl exports due to a delayed harvest, and despite the temporary halt on noni exports to Japan. In 2011-12 exports are estimated to be reduced by -1.0% mainly reflecting the removal of the one off increase in pearl exports in 2010-11. Going forward growth is expected to grow with movements in real GDP.

Balance of Trade (BOT)

Balance of Trade as of December quarter 2010 indicates a significant deficit of -\$108.3million. This is 2.6% deeper than the September 2010 quarter and significantly higher than the December quarter in 2009. Based on current projections, BOT for the year ending June 2011 is estimated to come in at a deeper deficit of -\$349.4million and will grow in line with the trend in nominal GDP in the outer years.

1.7 Banking and Finance

The main indicators of activity in the Cook Islands banking sector include the movements in net foreign assets, loans and savings levels over time. Given that the Cook Islands does not have a sovereign Reserve Bank and conducts its commercial activities in New Zealand Dollar, it does not



operate monetary policy and therefore does not manage the pace of demand through interest rates.

Since the HYEPU in December 2010 the net foreign assets (NFA) in the Cook Islands banking sector has significantly decreased from NZD36.5million in September 2010 to NZD2.1million in December 2010 indicating a decline in gross foreign assets due to a decrease in balances held with banks and finance institutions abroad.

Deposits

Deposits in the December quarter 2010 is NZD185.7million, a decrease of -17.5% below the September quarter 2010 and -17.1% below 2009 levels predominantly due to decreases in demand and term deposits by -25% and -17.7% respectively.

Loans

The December quarter continues to record a decline in total loans and advances since June 2009 mirroring trends in construction. Total loans and advances were recorded at NZD295.4million in the December quarter 2010 reflecting a -0.3% decline in loan stocks over the previous quarter across the majority of industries continuing to reflect limited focus towards development investments..

Going forward, as the economy picks up, loans and deposits are also expected to grow in line with growth in nominal GDP.

Financial Services Industry

The financial services sector is a composition of various services including international company registrations, trusts, partnerships and limited liability companies.

First established in 2009-10, the Financial Services Development Authority (FSDA) purpose is to market the Cook Islands as an international jurisdiction and to act as a point of contact between the government and the industry. As per the Budget Policy Statement 2011-12, it is noted that there is potential to further improve the contribution of financial services to the economy. Progressing the development of marketable products and the jurisdiction will assist in improving returns from this industry.

In reference to the recent natural disasters, the financial services industry has noted that New Zealand, Australia and Japan accounts for a small portion of clients which means that any negative impact on the industry will be minimal or non-existent.

It is important to note that often where there are major world events that negatively impact a region's economy, people become more aware of the need to arrange personal and financial planning. The services that are offered in the Cook Islands become more attractive as a 'safe harbour' for people which may mean an increase in business from these countries.

Housing and Construction

The trends and movements in the construction industry is measured by the building approvals from both residential and commercial properties which indicates investor confidence within the economy.

Total investments in the December quarter 2010 amounted \$3.7million of which residential and commercial investments accounted 76% and 24% respective of the total value. The total number of investments have declined by -10.5% over the December quarter of the previous year.

Going forward it is expected that the construction industry will grow moderately in line with nominal GDP in the outer years.

1.8 Assumptions Underlying the Economic Forecast

The assumptions underlying the economic forecasts are outlined within each of the individual sections in the Economic Update. It is noted that all data is now updated and based on rebased GDP data at 2006 prices.

The key assumptions are as follows:

- Real GDP is expected to grow by 1.1% in 2010-11 and to increase significantly by 6.5% and 4.5% in the two outer years reflecting projections at the time of the Half Year Economic & Fiscal Update in December 2010. This is a significant increase from the growth rates reported at the time of the Pre Election Economic & Fiscal Update in October 2010. The Government of the Cook Islands adopted a 3 year intensive program to rapidly expand air services links underpinned by additional marketing dollars focused on the tourism industry. These growth rates are net of a discounting factor of 2.0 percentage points and will be revised as assumptions for the Tourism Growth Strategy is reviewed and real data is collected. Underlying growth will continue to be dependent on the rate of growth in the global economy.
- Consumer price index is projected downwards to 0.9% in 2010-11, then increase to 3.5% in 2011-12 and 3.0% in 2012-13 going forward reflective of a catch up in the upward movement in oil prices globally.
- Nominal GDP will therefore grow by around 2.0% in 2010-11 and increase in the outer years by 11.0% and 6.6% reflecting a revision of inflation since the HYEUFU2010.
- In the short term, these variables are assumed to depart from their medium term paths in line with current economic conditions.

The above assumptions are based on past growth rates and economic predictions for regional and world growth in 2010-11 and the out years.

In terms of sector assumptions:

- Visitor arrivals remain at the same growth rates projected at the time of the HYEUFU in which visitor arrivals is expected to grow by 4.6% in 2010-11. In line with Government current strategy and resource commitment towards the Tourism industry, visitor arrivals are then forecasted to grow 13.0% in 2011-12 and 6.8% in 2012-13.
- With limited new investments towards the pearl industry, underlying growth in exports is expected to maintain its current levels. The value of pearl exports is expected to increase by 17.8% in 2010-11, exports are then expected to return to the 2009-10 level and remain flat in the outer years until such a time where development funds are accessible by the industry.
- Fish exports are projected to grow by 28.9% over 2009-10 levels, given 2009-10 stocks were bought for domestic consumption during large sporting events hosted by the Cook Islands, a one off impact, and is expected to grow by 3.0% in the out years.
- Agriculture exports of noni are assumed to be zero in June quarter 2011 following the halt in exports to Japan as a result of the natural disasters and response. It is assumed that after this quarter the market will return back to the prior levels.
- Other exports, imports, bank deposits and bank loans and advances are all expected to increase in line with growth in nominal GDP over the medium term.

2.0 FISCAL UPDATE

2.1 Overview

The purpose of the Fiscal Update is to provide necessary revisions to fiscal forecasts that underpinned the Half Year Economic & Fiscal Update in December 2010 (HYEFU), and as a result provide an analysis for fiscal responsibility and a revised set of accounts for 2010-11, 2011-12 and 2012-13.

In updating the fiscal forecasts, the following factors and have been considered

- year to date assessment of revenues and expenditure patterns against original Budget Estimates 2010-11 (July), and
- the incorporation of adjustments in estimates to be included in the Appropriation Amendment for 2010-11

In 2010-11 (current fiscal year) generally both revenues and expenditures are tracking closely to that projected at the time of the Budget Estimates 2010-11 (July) and therefore those items that are not affected by policy shifts are expected to come in on budget at year end. Overall revenue has been revised upwards by \$0.7million in 2010-11 mainly reflecting increases to fishing license fees and other smaller movements in other revenues. Expenditures are expected to be increased by \$1.0million in operating expenditures, but an overall reduction in investment activities by \$9.4million mainly reflecting the deferment of loan funds and its associated expenditures to 2011-12.

Combined, these items have a net effect on the operating balance of -\$0.4million and on the overall budget balance of +\$0.5 million at year end. These items are discussed in more detail under Section 1.2 of this update.

As discussed in the Half Year Economic & Fiscal Update in December 2010 and at the front end of this publication, to control the impacts of fiscal policy on fiscal and macroeconomic stability, the Government of the day must operate within the fiscal responsibility principles outlined in the MFEM Act as follows:

- Ensuring that unless Crown debt is at prudent levels, operating expenses will be less than operating revenues (Government will run an operating surplus)
- Achieving and maintaining levels of Crown net worth that provide a buffer against factors which may impact adversely on net worth in the future
- Managing prudently the fiscal risks facing the Crown
- Pursuing policies that are consistent with a reasonable degree of predictability about the level and stability of tax rates for future years.

The Ministry of Finance and Economic Management quantifies these principles through the Fiscal Responsibility Ratios as reported in each publication since the Budget Estimates 2010-11. The below table shows the benchmarks of these ratios and performance in 2009-10 and expectations for 2010-11 based on revised forecasts:

Table 2.10 : Fiscal Responsibility Ratios

	Type	Purpose	Benchmark	2009-10	2010-11	2010-11	Comment
				Estimate	Budget	Estimate	
				\$m	\$m	\$m	
A Fiscal Envelope Ratio							
1	Tax Revenue to GDP	Sets the revenue boundary and ensures government limits the diversion of resources away from the private sector	25%	25%	25%	25%	Current levels are appropriate. Note that there has been no policy shift in the tax regime in 2010-11. Budget Policy is to review the taxation regime and will be guided by this limitation.
B Expenditure Control Ratios							
2	Personnel to Total Revenue	Controls expansion in the size of the public service	40%	42%	43%	42%	Concerning and will require policy action over the medium term. Budget Policy to review the size of the public service will be guided by this limitation.
3	Operating Balance	As required under the MFEM Act	0	-2,672	600	1,007	Current levels are appropriate. However levels must be tracked closely over the medium term in terms of sustainability to include the management of donor funds given the moves to general budget support.
C Prudential Ratios							
4	Debt Servicing to Total Revenue	Measures ability to service debt	5%	4%	3%	3%	Current levels are appropriate. However this must be tracked closely as new loans are considered including the purpose of the loan to generate economic activity to repay debt.
5	Budget Overall Deficit as % of GDP	Moderate the rate of debt accumulation	+/-2%	-2.8%	-1.9%	-1.8%	Current levels as per the 2010-11 budget are appropriate given the balance of expenditure in 2009-10 was financed through reserve fund rather than increased borrowings. However this must be tracked closely when new loans are considered.
6	Debt to GDP ratio	Measures the level of debt relative to national income	35.0%	18%	20%	17%	Current levels are appropriate and will improve over time. However this must be tracked closely when new loans are considered.

In this context, in 2010-11 government is generally managing decisions within the fiscal responsibility limitations.

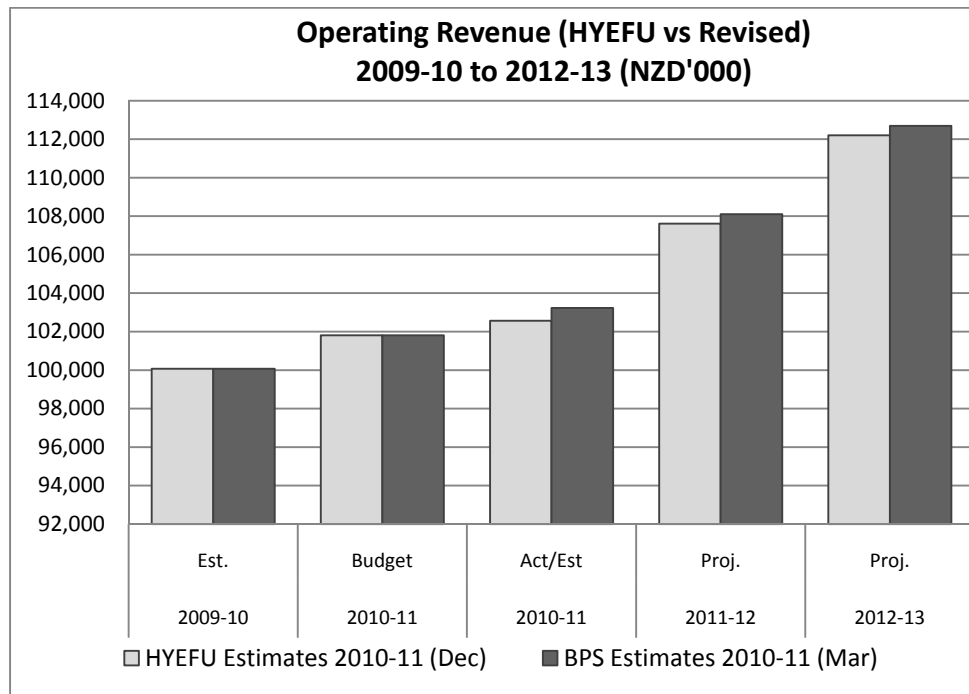
Table 2.2 : Fiscal Indicators

Fiscal Indicators					
NZD'000	2009-10	2010-11	2010-11	2011-12	2012-13
	Act.	Budget	Est.	Proj.	Proj.
Statement of Financial Performance					
Taxation Revenue	83,762	83,893	84,223	92,577	97,235
Other Revenue	6,321	6,970	7,576	5,543	5,576
Ministry Trading (net revenue)	5,413	5,148	5,155	5,271	5,271
Interest and Dividend	4,575	5,797	6,274	4,708	4,608
Total Operating Revenue	100,071	101,808	103,227	108,099	112,690
Total Revenue as % of GDP	30%	30%	30%	28%	28%
Tax Revenue as % of GDP	25%	25%	25%	24%	24%
Personnel	41,685	43,559	43,559	43,176	43,012
as % of Total Revenue	42%	43%	42%	40%	38%
Total Operating Expenditure	102,743	101,208	102,220	107,677	109,929
as % of GDP	31.0%	30.0%	29.8%	28.2%	27.0%
as % of Operating Revenue	102.7%	99.4%	99.0%	99.6%	97.5%
Operating Balance	- 2,672	600	1,007	422	2,762
as % of GDP	-0.8%	0.2%	0.3%	0.1%	0.7%
Non Operating Balance (million)	(6,474)	(7,160)	(7,201)	(7,349)	(8,080)
Overall Surplus/(Deficit)	(9,146)	(6,560)	(6,194)	(6,928)	(5,318)
as % of GDP	-2.8%	-1.9%	-1.8%	-1.8%	-1.3%
Statement of Financial Position					
Assets (\$m)	304.4	316.6	313.3	325.1	328.6
Liabilities (\$m)	126.6	134.3	131.0	136.6	133.4
Crown Balance (\$m)	177.8	182.4	182.3	188.6	195.2
as % of GDP	53.7%	54.1%	53.1%	49.5%	48.0%
Statement of Borrowings					
Net Crown Debt, end of FY (\$m)	58.2	66.7	57.2	66.0	64.4
as % of GDP	17.6%	19.8%	16.6%	17.3%	15.8%
Loan Repayment Reserves Held (\$m)	22.0	20.5	20.5	18.6	16.8
Debt Servicing (\$m)	4.0	3.2	3.1	3.4	4.1
as % of Total Revenue	4.0%	3.2%	3.0%	3.1%	3.7%
Memo item: Nominal GDP (\$m)	331.3	336.9	343.6	381.2	406.6

2.2 Operating Statement

The Operating Statement reflects the financial performance of government and discusses general trends and revisions of forecasts for operating revenues, operating expenditures and the resultant operating balance.

2.2.1 Operating Revenue



Operating Revenues are made up of taxation receipts (81.6%), other revenues collected on behalf of the crown (7.3%), ministry trading revenue (5.0%) and interest and dividend receipts (6.1%). These are used to finance the operating cost of government, with surpluses used for investing activities (where apparent).

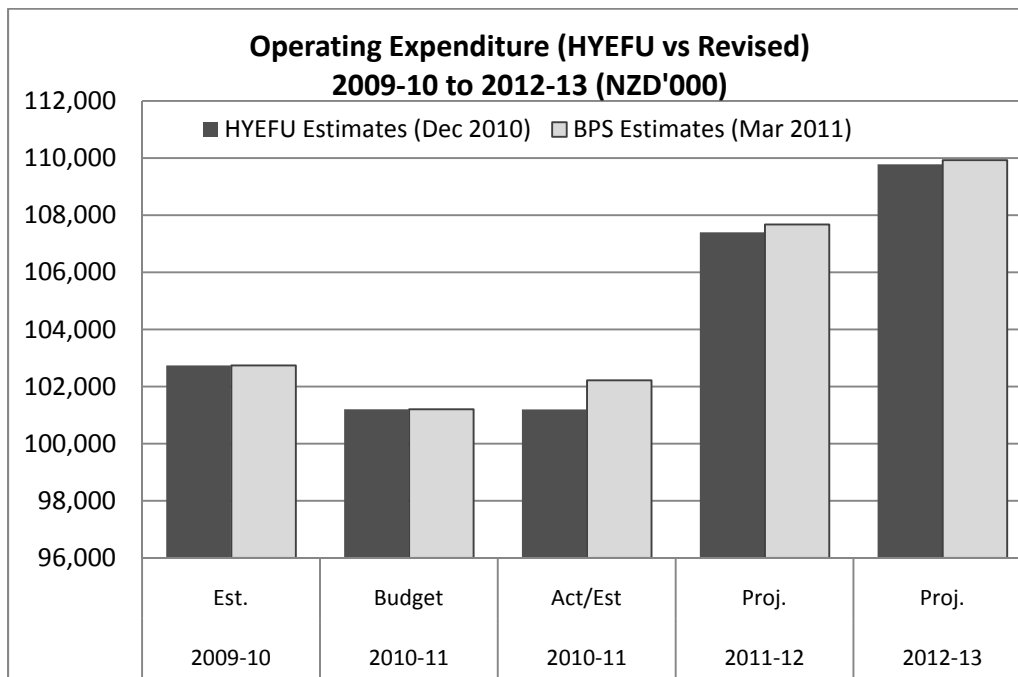
At the time of the HYEUFU in December 2010, Operating Revenues were expected to come in at year end at \$102.6 million. Since this time Government has reviewed and updated its revenue estimates upwards to \$103.2million. This is a \$1.4million increase on estimates at the time of the original Budget Estimates passed in August 2010 and a \$0.7million increase over the HYEUFU estimates.

The upward revision of revenue estimates since the HYEUFU is predominantly due to upward revisions to fishing license collections due to an increase in the level of fees charged raising approximately \$0.6million additional revenues, higher revenues received under the existing upper air space management agreement \$0.1million, along with slight fluctuations in other revenues. Although there are fluctuations over the year, the overall increase over the previous year is expected to be 3.2%. These estimates have been used as the basis for the preparation of an Appropriation Amendment 2010-11 for Parliament consideration.

Going forward, base growth in operating revenues is expected to continue in line with nominal GDP reflecting the Tourism Growth Strategy and slight adjustments to outer year revenues from the midterm review.

2.2.2 Operating Expenditure

Operating expenditure refers to government expenditure on delivery of government’s core outputs by the public service, payments on behalf of the crown, and other operating expenditures.



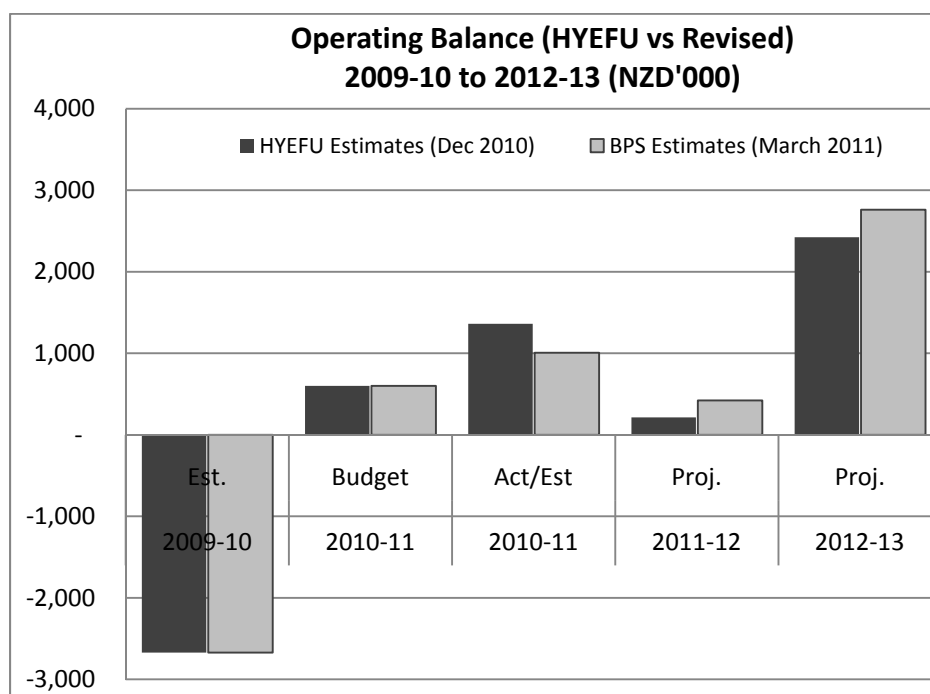
Operating expenditures were estimated at \$101.2million for 2010-11 at the time of the Budget Estimates in July 2010. This was estimated to remain as budgeted at the time of the HYEFU in December 2011. Given the desire of the current Government to table an Appropriation Amendment in 2010-11, operating expenditure estimates as at March 2011 have been revised upwards to \$102.2million, around +\$1.0million.

The intent behind the adjustments reflected in these estimates is to allow the payment of fixed non-discretionary items, whilst also accommodating the necessary adjustments to the appropriation to ensure Governments initiatives are sufficiently appropriated. These adjustments in expenditure is funded through identified year to date savings in existing appropriations and surplus revenues received by the Crown since the principal Act was passed. The estimates will also allow for the removal of capital expenditures that will be deferred to the next financial year while institutional arrangements within the infrastructure sector are strengthened. Specific details of the adjustments to estimates will be released on the tabling of the Appropriation Amendment 2010-11 in April 2011.

Going forward estimates are projected to grow with nominal GDP largely reflective of growth in the tourism industry underpinned by the Tourism Growth Strategy.

2.2.3 Operating Balance

The Operating Balance is the balance of operating revenues minus operating expenditure, as prescribed by the MFEM Act. Given the analysis provided in sections 2.2.1 and 2.2.2, the operating balance in 2010-11 is estimated to increase from \$0.6million at the time of the original budget estimates in August 2010 to \$1.0million, reflecting the upward revisions to revenues and the provision of new expenditures through savings in other expenditure items. Going forward, with the upward revision to operating revenues over the medium term due to changes in licensing fees and other adjustments, it is expected that based on existing commitments, the 2011-12 operating balance will be \$0.4million; after removing the impacts of one off expenditure and revenue items, increases in the outer years will grow in line with nominal GDP.



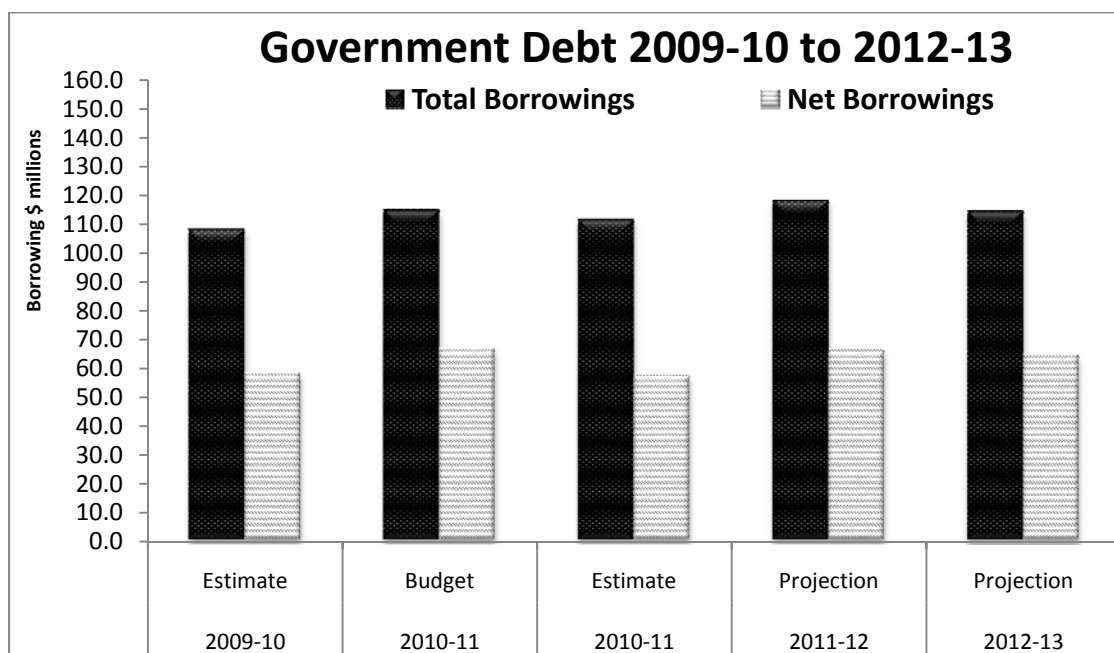
2.3 Debt

Total gross government debt is estimated at \$111.5 million or 32.5% of GDP for the fiscal year ending 30 June 2011. This is an amendment to the \$114.8 million initially reported in the HYEFU.

The downward revision of the debt level in 2010-11 (reduction of \$3.3 million) is the net result of an increase in an existing loan commitment in 2010-11 and the deferment of an economic loan to 2011-12 net of. The increased on the existing loan is \$6.2 million that is currently under negotiation with the Asian Development Bank (ADB). This is a supplementary loan request in

addition to the original ADB Rarotonga Harbour Ports Authority loan (\$26.8 million) to finance the project funding shortfall. The reasons for the cost underestimation were volatility in the cost of construction materials; the relative isolation of the project site, and volatile market conditions making cost estimation difficult. Offsetting this is the reduction of \$9.5 million being the delay in the signing off of the second tranche of the ADB Economic Recovery Support Program Loan (ERSP) initially intended for 2010-11. This funding source will be re-appropriated through the 2011-12 fiscal year and aligned to outcomes of the Economic Summit to be held in April 2011.

Net debt is at \$57.2 million (16.6% of GDP) and considered well within the fiscal responsibility benchmark of 35% as outlined in the Fiscal Responsibility Ratios. This percentage is expected to slightly increase in 2011-12 to accommodate for the second tranche of the ADB ERSP loan, and then reduce over the outer years as growth in the economy improves and repayments of existing debt continue, despite reductions in debt reserves in outer years.



Loan Reserves

Government also holds loan reserves which have been built up over the years from the repayments of on lent loans to State Owned Enterprises (SOEs). Government loan reserves will stand at \$20.5 million by June 2011. This is a drawdown of \$1.5 million in 2010-11 to finance SOE loan repayments. Loan reserves will continue to slowly reduce in the outer years as repayments are made on loans that were on-lent to SOEs.

Net Debt to GDP

The Fiscal Responsibility Ratio states that net debt to GDP should not exceed 35%. The intention of this ratio is to control and set a limit on the level of net debt (debt carrying capacity) and measure this against national income. Based on this ratio, the current debt carrying capacity of the Cook Islands is \$120.3 million (net of loan reserves). This has been

revised upwards since the Budget Estimates 2010-11 (July) given the rebasing of the GDP statistic. As above, current levels are within fiscal responsibility principles outlined in the MFEM Act.

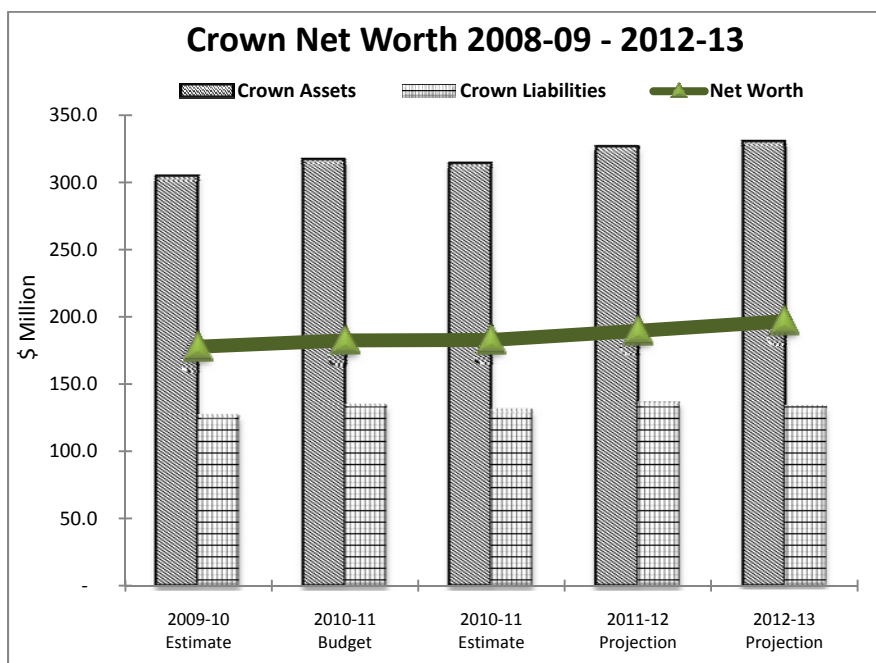
In the unlikely event that there are no future borrowings, this Fiscal Responsibility Ratio will improve with anticipated growth in GDP and repayment of existing debt in the outer years.

Although debt to GDP is well below the threshold, attention needs to be drawn to the ability of government to fund the associated operating expenses (including interest payments and maintenance costs of existing and new loans/projects) from operating revenue generated.

While there are demands for upgrading infrastructure to facilitate sustainable economic growth and social activities, future debt levels must be approached cautiously. All borrowing proposals must be made under transparent processes as required by the MFEM Act 1995-96, evidenced by well researched business cases and funded through a user pays system where possible. The fiscal responsibility ratios will assist Government to manage the growth in debt prudently¹.

2.4 Net worth

Government's net worth is the difference between Crown assets and Crown liabilities. Government's net worth simply gives a snapshot of government's ability/inability to service all its creditors. There are currently no clear guides to determining an optimal level of public sector net worth; however analysing the government's net worth and what causes it to change can lead to understanding the need for better policies.



Government's net worth is revised downward from the original 2010-11 Budget Estimates of \$182.4 million to \$182.3 million. This is a net movement of \$0.4 million reflecting the increase

¹ PEEFU, October 2010

in the operating surplus of \$0.6 million as per the original Budget Estimate to \$1.0 million reflecting additional revenues and revisions to expenditures expecting to be reflected through an Appropriation Amendment 2010-11. Offsetting this is the reduction in the aid funded assets of \$0.5million as a result of the reduction of aid flows of \$5.0million, of which \$0.5million was expected to be asset purchases.

From the above graph, Crown’s net worth will continue to increase in the outer years as long as there is an estimated operating surplus. Also a major contributor to the forecast upward trend is the injection to the Crown’s asset from aid donor funding. It is estimated that an annual average of 10% of donor funding is capital asset.

2.5 Aid Flows

Total aid contributions by donor partners were budgeted at \$39.5 million at the time of the original Budget Estimates 2010-11. This has been reduced to \$34.5 million, which accounts for 14% decrease of aid funding level since the Budget Estimates 2010-11 and as last reported in the Half Year Economic & Fiscal update in December 2010.

Various funding modalities are being explored with General Budget Support (GBS) being preferred mechanism of delivery, managed through the national appropriation. The adoption of the revised Cook Islands Aid Policy as stated in the front end of this publication defines Governments commitments to the efficient and effective use of Official Development Assistance and outlines actions required to achieve this preferred modality. An integral part of the move towards GBS is the Public Expenditure Financial Accountability (PEFA) to be conducted in 2011. The PEFA will test the strength, define failings and provide guidance on remedial measures guiding Governments continuing efforts to attain robust national financial management framework with in turn provides confidence to the donors for direct national budget support.

The allocation of 2010-11 funding by sector is as follows:

Sector	Budget 2010-11	Estimate 2010-11	Variance
Infrastructure	14,769,143	14,769,143	0
Economic	10,546,784	5,546,784	-5,000,000
Social	8,651,670	8,651,670	0
Governance	1,752,429	1,799,857	47,428,
Environment	1,686,071	1,686,071	0
Law & Order	1,442,640	1,442,640	0
Other	664,000	664,000	0
Grand Total	39,512,736	34,560,165	5,047,428

The changes in the 2010-11 programme is predominantly due to the following

- The reduction in aid funds in the Economic Sector is a result of the removal of Food and Agriculture Organisation (FAO) program of \$5 million (\$US3.5million) which will support Food Security initiatives managed and driven by the Ministry of Agriculture. It is intended that the program will be re-introduced to the 2011-12 budget process.
- The adjustment in the Indian Grant Fund of \$47,428 increasing the total amount to \$518,857 has been appropriated as new money being available in the current financial year 2010-11.

Other notable donor assistance expected to be provided under the aid program for 2010-11 include the following

- The Pacific Environment Community (PEC) Fund supported by Japan and the Pacific Adaptation Strategy Assistance Programme (PASAP) fund supported by Australia are the first concrete programs to be delivered in-country related to climate change.
- Technical assistance from the Asian Development Bank (ADB) is progressing on institutional review and reform in both the Infrastructure Sector and the Public Service. Some outcomes from these are anticipated to include strengthen the delivery of both the New Zealand and European Union (EU) funded sanitation projects.
- The Cook Islands is one of 23 countries participating in the Paris Declaration Evaluation, a global evaluation of aid effectiveness. This evaluation has been completed and the report was presented at the Bali PDE meeting in early December 2010. The findings provided an indication of the effectiveness of aid from annual donor allocations. This will contribute to global evaluation of aid effectiveness as well as provide valuable insight into the way aid is applied to meeting the needs of the country.
- The United Nations Development Program (UNDP) will shortly review its efforts in consolidating United Nations (UN) programs within the United Nations Development Assistance Framework (UNDAF) concept to reduce the UN fragmented approach.
- As reported in the HYEPU, NZAID and AusAID's harmonised aid program remains our largest inclusive of a \$6 million carry forward of under spending from the 2009-2010 increasing NZAID's aid allocation from \$17 million to \$23 million 2010-11. It is noted that \$20 million was allocated to various projects and \$3 million is currently being distributed to government programs.
- As reported in the HYEPU a total of 6.8 billion yen (US\$66 million) was allocated by Japan as a Pacific Environment Community (PEC) Fund to 14 countries that are members of the Pacific Islands Forum. The funds will be managed by the Pacific Islands Forum Secretariat. An estimate of USD4 million has been allocated to the Cook Islands and these are to fund initiatives in solar energy generation and water desalination.

The Aitutaki Recovery Committee had identified a shortfall in funding due to increasing labour cost. The previous Government had requested to the New Zealand Government for an additional \$0.9 million to cover the funding gap. A Letter of Variation (LoV) has recently been signed between New Zealand and Cook Islands Government for approved funding to cover the shortfall of \$0.9 million. The funds are not new money and are included within the indicative \$23 million forward aid program.

Government has appropriated additional funds of \$0.07 million required as Governments contribution towards the completion of the Pukapuka Cyclone Shelter co-funded by European Union. A further \$0.15 million has been allocated to the Pukapuka project by the Flex Funds administered by Foreign Affairs. The total value of this project is \$4.0 million.

The Aid Management Division, responsible for coordinating aid flows to the Cook Islands, is continuously engaging with donor partners to align development assistance to national priorities, with General Budget Support being the preferred mechanism of delivery managed through the adoption of the first Cook Islands Aid Management Policy as stated in the front end of this publication. This will be complemented by the Public Expenditure Financial Assessment (PEFA) to be conducted in 2011 which will demonstrate the strength of government's financial management systems to manage and undertake general budget support from donors.

The Cook Islands Government continues to seek improvements in aid coordination within limited resource allocations with a focus on changing business towards having more control over the priority programs for aid donor expenditure aligned to national goals. This has included strengthening the relationship between the Ministry of Foreign Affairs and Immigration (MFAI) and the Ministry of Finance and Economic Management (MFEM) in relation to the European Union program.

2.6 Specific Fiscal Risk

The total quantifiable contingent liabilities are estimated at \$21.2million in 2010-11. This is made up of the following:

Guarantees and Indemnities

- The Government of the Cook Islands has accepted the commercial risk such that in the event that the Rarotonga/Los Angeles flight incurs a loss, Government will share these losses up to \$5.0 million. As per the appropriation, Government estimates that the maximum payout in 2010-11 will be \$3.5million, with the balance recognised as a contingent liability.
- Under a second agreement with Air New Zealand, the Government of the Cook Islands has accepted the commercial risk such that any losses incurred by Air New Zealand in respect to the service provided on the trial flight from Sydney to Rarotonga during the term of agreement shall be met by the Government of the Cook Islands. Given this liability was appropriated in the budget at \$2.5million, it is not recognised above as a contingent liability. The loss has been realised at slightly less than \$1.0million and is well within the appropriation provided. Savings in this appropriation have been transferred to marketing of the next round of airline subsidies. It is anticipated that contingent liabilities for the new Sydney, Los Angeles and Fiji flight will be included in the 2011-12 Budget Estimates.
- The settlement with Apex Agencies Limited (operating as TOA Petroleum, TOA) dated 11 December 2009 provided a guaranteed minimum EBITA (Earnings Before Interest, Tax,

Depreciation and Amortisation) of \$1,200,000 per annum. Thus if TOA makes a profit of less than \$1.2million in a given year (or even a loss) the Crown will make a top up payment to \$1.2million. That is the Crown's potential liability could exceed \$1.2million in a given year. An estimate of the potential liability has not been made although \$1.2 million has been included in the appropriation for 2011-12.

Uncalled Capital

- Government also holds NZ\$6.7 million in uncalled capital shares comprising of \$3.9 million in the Asian Development Bank and \$2.8 million in the Bank of the Cook Islands.

Legal Proceedings & Disputes

- Total quantifiable risk to government under legal proceedings & disputes is \$16.2 million.
- \$14.5 million relates to contingency in recognition of the lawsuit filed against the Government regarding its shipping policy in October 2002. However it is not anticipated that any payment will be made on this claim.
- Legal claim of \$0.6 million against the Health Department for medical negligence (2010). The Government will be filing a Statement of Defence disputing the allegation.
- Legal claim of \$0.6 million against the Ministry of Transport for public misfeasance (2010). Statement of Defence have been filed disputing the allegation.
- \$0.5 million relates to other small legal proceedings and dispute cases against the Crown.

2.7 Assumptions Underlying the Fiscal Projections

Various assumptions must be made to forecast government's fiscal position and performance in the outer years.

Operating Revenues are forecasted on the basis of growth in the economy adjusted for one off considerations.

While growth in neighbouring countries is expected to be moderate in 2010, growth in the Cook Islands over the medium term has been revised upwards to reflect expected returns from the recently adopted Tourism Growth Strategy. As a result, Real GDP growth is expected to edge upwards to increase by:

- 1.1% in 2010-11,
- 6.5% in 2011-12 and
- 4.5% in 2012-13.

Reflecting adjustments to CPI, Nominal GDP is expected to grow by

- 2.0% in 2010-11
- 1.1% in 2011-12
- 6.6% in 2012-13

The assumptions made that underpin the economic impacts of the Tourism Growth Strategy is that each additional tourist will

- Stay an average of 10 days¹
- Spend approximately NZD223 per day²
- Such expenditures have a multiplier effect of 1.8²
- Every NZD1 in general consumption generates \$0.42 in GDP³
- Every NZD1 in GDP generates on average \$0.25 in taxation

These assumptions haven been reviewed by the Ministry of Finance & Economic Management with technical assistance from the Asian Development Bank.

Growth in prices measured through movements in the Consumer Price Index is expected to be not as high as estimated at the time of the HYEPU in 2010-11, but reflect growth in the outer years as a result of price increases in global oil prices, as follows:

- 0.9% in 2010-11
- 3.5% in 2011-12
- 3.0% in 2012-13

Actual receipts may differ if growth in the economy varies from projections. Economic outlooks by both the OECD and the World Bank indicate positive growth in the major countries in the world including the USA and Europe including a tailing off of unemployment rates following the impacts of the Global Economic Crisis.

Natural disasters on Japan, Christchurch and Brisbane are estimated to have a slight yet temporary impact on the Cook Islands economy, more so in March and June quarter 2011.

Operating Expenditure movements in the outer years is based on actual commitments to movements through the Medium Term Budgeting Framework.

Level of borrowings is based on average exchange rates in December 2010.

2.8 Statement of Accounting Policies

There have been no changes since the Half Year Economic & Fiscal Update 2010. There are no major changes to accounting policies anticipated in the foreseeable future.

¹ Cook Islands Tourism Corporation, 2010

² Airbiz, Berl Economics: Cook Islands Tourism Corporation, Economic Impact of Seasonal : Sydney — Rarotonga Route, Final Report November 2010

FINANCIAL UPDATE

as at 30 June 2011

The forecast financial estimates of the Crown as set out in the following pages.

Statement of Financial Performance

Statement of Financial Position

Statement of Cash Flows

Statement of Borrowings

Revenue Levied on Behalf of the Crown

Statement of Fiscal Risks

Schedule 14
STATEMENT OF FINANCIAL PERFORMANCE
For the years ending 30 June

	2009-10 Estimate \$m	2010-11 Budget \$m	2010-11 Estimate \$m	2011-12 Projection \$m	2012-13 Projection \$m
REVENUE					
Revenue Levied Through the Crown's Sovereign Power	83.8	83.9	84.2	92.6	97.2
Other Crown Revenue	6.3	7.0	7.6	5.5	5.6
Sales of Goods & Services (Ministry Trading Revenue)	5.4	5.1	5.2	5.3	5.3
Interest and Dividends	4.6	5.8	6.3	4.7	4.6
Total Revenue From Crown Funded Activities	100.1	101.8	103.2	108.1	112.7
EXPENDITURE					
Crown Funded Activities	102.7	101.2	102.2	107.7	109.9
Total Expenditure From Crown Funded Activities	102.7	101.2	102.2	107.7	109.9
Net Operating Surplus/(Deficit)	(2.7)	0.6	1.0	0.4	2.8

Schedule 15

STATEMENT OF FINANCIAL POSITION

As at 30 June

	2009-10 Estimate Estimate \$m	2010-11 Budget Budget \$m	2010-11 Estimate Estimate \$m	2011-12 Projection Projection \$m	2012-13 Projection Projection \$m
Assets					
Cash & short term deposits	24.5	26.1	26.5	28.7	31.9
Loan Reserves	22.0	20.5	20.5	18.6	16.8
Trust accounts	2.0	2.4	2.4	2.8	3.3
Inventory	1.1	1.2	1.2	1.2	1.5
Debtors & receivables	4.4	4.6	4.6	4.6	4.6
Tax Receivables	9.0	9.0	9.0	9.7	10.5
Banking Investment Portfolio	-	-	-	-	-
Advances to public enterprises & other authorities	27.9	27.6	33.8	33.5	33.2
Investment in public enterprises & other authorities	103.2	103.2	103.2	103.2	103.2
Fixed assets	110.4	122.1	112.2	122.8	123.6
Total Assets	304.4	316.6	313.3	325.1	328.6
Liabilities					
Creditors and Payables	13.9	14.5	14.5	13.5	13.8
Trustee Liabilities	4.5	5.0	5.0	5.0	5.2
Borrowings	108.1	114.8	111.5	118.1	114.4
Banking customer deposits	-	-	-	-	-
Total Liabilities	126.6	134.3	131.0	136.6	133.4
Crown Balance	177.8	182.4	182.3	188.6	195.2

Schedule 16

STATEMENT OF CASH FLOWS

For the years ending 30 June

	2009-10 Estimate \$m	2010-11 Budget \$m	2010-11 Estimate \$m	2011-12 Projection \$m	2012-13 Projection \$m
Operating Activity Cash Flows					
Cash provided from:					
Taxation & levies	83.8	83.9	84.2	92.6	97.2
Collection of prior year tax arrears	4.2	0.0	-	(0.7)	(0.8)
Other	16.1	17.5	18.6	15.1	15.3
Ministry Trading Revenue	5.4	5.1	5.2	5.3	5.3
Interest on Funds/Dividends	4.6	5.8	6.3	4.7	4.6
Other Revenue	6.1	6.6	7.2	5.1	5.4
	104.1	101.4	102.8	107.0	111.7
Cash applied to:					
Ministry operating costs to produce outputs	60.8	60.8	60.6	62.5	62.6
Ministry Gross Expenditure	63.7	64.0	63.8	66.0	66.1
Less Depreciation	(2.9)	(3.2)	(3.2)	(3.5)	(3.6)
Other Crown expenses	36.6	31.7	32.9	36.6	38.4
	97.4	92.5	93.5	99.2	101.0
Net Operating Activity Cash Flows	6.7	8.9	9.3	7.8	10.7
Investing Activity Cash Flows					
Cash provided from investing activities	0.1	0.3	0.3	0.3	0.3
Subsidiary Loan Repayments	0.1	0.3	0.3	0.3	0.3
Cash applied to investing activities	28.7	13.9	4.5	14.0	4.4
Ministry capital	1.9	13.9	4.5	13.9	4.4
Ports	26.8	-	-	-	-
CIIC	-	-	-	-	-
Contingency	-	0.1	0.1	0.1	0.1
Net Investing Activity Cash Flows	(28.6)	(13.7)	(4.2)	(13.7)	(4.2)
Financing Activity Cash Flows					
Cash provided from financing activities	26.8	11.1	1.5	11.4	1.9
Cash applied to financing activities	4.7	3.0	2.9	3.2	3.9
Loan repayments	3.2	2.6	2.5	2.7	3.4
Loan Reserves	1.1	-	-	-	-
Reserve Trust Fund	0.4	0.4	0.4	0.5	0.5
Net Financing Activity Cash Flows	22.1	8.1	(1.4)	8.2	(2.0)
Net cash movements	0.2	3.3	3.7	2.3	4.5
Add opening cash & deposits	23.9	24.2	27.5	31.1	33.5
Closing Cash & Deposits	24.2	27.5	31.1	33.5	37.9

Schedule 18

REVENUE LEVIED ON BEHALF OF THE CROWN

For the year ending 30 June

	2009-10 Estimate \$m	2010-11 Budget \$m	2010-11 Estimate \$m	2011-12 Projection \$m	2012-13 Projection \$m
Tax Type					
Income Tax	22.3	22.5	22.5	24.7	25.9
Company Tax	10.4	9.7	9.7	11.1	11.6
Import Levies	10.9	10.9	10.9	11.9	12.5
Value Added Tax	34.4	35.0	35.0	38.0	39.9
Departure Tax	5.7	5.8	6.1	6.9	7.3
Total Taxation Revenue	83.8	83.9	84.2	92.6	97.2

Schedule 17

STATEMENT OF BORROWINGS

As at 30 June

	2009-10 Estimate \$m	2010-11 Budget \$m	2010-11 Estimate \$m	2011-12 Projection \$m	2012-13 Projection \$m
Debt	108.1	114.8	111.5	118.1	114.4
Total Borrowings	108.1	114.8	111.5	118.1	114.4
Assets held against Debt					
Advances to public enterprises	27.9	27.6	33.8	33.5	33.2
Loan reserves	22.0	20.5	20.5	18.6	16.8
Net Borrowings	58.2	66.7	57.2	66.0	64.4

Schedule 19

STATEMENT OF FISCAL RISKS

Guarantees and Indemnities	1,500,000
Uncalled Capital	4,500,000
Legal Proceedings & Disputes	15,213,184
TOTAL QUANTIFIABLE CONTINGENT LIABILITIES	21,213,184

Guarantees and Indemnities relate to the following:

The Government of the Cook Islands has accepted the commercial risk such that any losses incurred by Air New Zealand in respect to the service provided on the trial flight from Sydney to Rarotonga during the term of agreement shall be met by the Government of the Cook Islands. Given the trial has ended, the estimated pay out is \$0.9million. This is to be funded through the appropriation at 2.5million and therefore not recognised above as a contingent liability.

Under a second agreement with Air New Zealand, the Government of the Cook Islands has accepted the commercial risk such that in the event that the Rarotonga/Los Angeles flight incurs a loss, Government will share these losses up to \$5million. As per the appropriation, Government estimates that the maximum payout in 2010-11 will be \$3.5million with the balance recognised as a contingent liability.

The settlement with Apex Agencies Limited (operating as TOA Petroleum, TOA) dated 11 December 2009 provided a guaranteed minimum EBITA (Earnings Before Interest, Tax, Depreciation and Amortisation) of \$1,200,000 per annum for a period of 8 years. Thus if TOA makes a profit of less than \$1.2million in a given year (or even a loss) the Crown will make a top up payment to \$1.2million. That is the Crown's potential liability could exceed \$1.2million in a given year. An estimate of the potential liability has not been made.

Uncalled capital relates to shares in the Asian Development Bank and in the Bank of the Cook Islands

Legal Proceedings and Disputes relates to the Shipping Case and other smaller cases against the Crown