

Proactive Release

Date: 10 January 2022

The following Cabinet paper and related Cabinet minute have been proactively released by the Minister of Foreign Affairs

Title	Reference
<i>Supporting Short and Medium Term Economic Recovery in the Cook Islands</i>	CAB-21-MIN-0439 ERS-21-MIN-0038

Some parts of this information release would not be appropriate to release and, if requested, would be withheld under the Official Information Act 1982 (the OIA). Where this is the case, the relevant sections of the OIA that would apply have been identified. Where information has been withheld, no public interest has been identified that would outweigh the reasons for withholding it.

Key to OIA redaction codes:

- 6(a): to avoid prejudicing the international relations of the New Zealand Government;
- 6(b)(i): to protect the passing of information from another government on a confidential basis;
- 7(b)(ii): to avoid prejudicing the relations of the self-governing State of the Cook Islands;
- 7(b)(iii): to avoid prejudicing the relations of the self-governing State of Niue;
- 9(2)(g)(i): to protect the free and frank expression of opinions by departments.



Cabinet

Minute of Decision

This document contains information for the New Zealand Cabinet. It must be treated in confidence and handled in accordance with any security classification, or other endorsement. The information can only be released, including under the Official Information Act 1982, by persons with the appropriate authority.

Report of the Cabinet External Relations and Security Committee: Period Ended 29 October 2021

On 1 November 2021, Cabinet made the following decisions on the work of the Cabinet External Relations and Security Committee for the period ended 29 October 2021:

ERS-21-MIN-0038 **Supporting Short- and Medium-Term Economic Recovery in the Cook Islands** CONFIRMED
Portfolio: Foreign Affairs

Michael Webster
Secretary of the Cabinet



Cabinet External Relations and Security Committee

Minute of Decision

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Supporting Short- and Medium-Term Economic Recovery in the Cook Islands

Portfolio Foreign Affairs

On 26 October 2021, the Cabinet External Relations and Security Committee:

- 1 s7(b)(ii) and the suspension of tourism in August 2021 has interrupted the economic recovery;
- 2 **noted** that the Cook Islands is not currently able to receive support from any other like-minded multilateral or bilateral partners;
- 3 **noted** that the Government of the Cook Islands requires short-term budget support for government cash reserves, s7(b)(ii)
- 4 **agreed** that NZ\$20 million from within existing aid programme resources be provided as a grant to the Government of the Cook Islands, within the current financial year, to support government cash reserves;
- 5 **agreed** that:
 - 5.1 NZ\$40 million from within existing aid programme resources be allocated to infrastructure investment to support the medium-term economic recovery of the Cook Islands;
 - 5.2 this funding will be provided as a contribution to the New Zealand-Cook Islands Infrastructure Trust Fund;
- 6 **noted** that the total proposed funding referred to above is NZ\$60 million, and that this quantum of proposed expenditure requires Cabinet approval;
- 7 **noted** that this funding will be sourced from within the existing International Development Cooperation (IDC) appropriation, and that no new funding is sought.

Janine Harvey
Committee Secretary

Present: (see over)

Present:

Rt Hon Jacinda Ardern (Chair)
Hon Grant Robertson
Hon Kelvin Davis
Hon Andrew Little
Hon David Parker
Hon Nanaia Mahuta
Hon Poto Williams
Hon Kris Faafoi
Hon Peeni Henare

Officials present from:

Office of the Prime Minister
Department of the Prime Minister and Cabinet
Officials Committee for ERS

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Office of the Minister of Foreign Affairs

Cabinet

Supporting short- and medium-term economic recovery in the Cook Islands

Proposal

- 1 This paper seeks Cabinet approval to allocate NZ\$60 million from existing International Development Cooperation (IDC) programme resources as grant support for the short- and medium-term economic recovery of the Cook Islands. This grant would bring the total level of Aotearoa New Zealand's fiscal crisis budget support for the Cook Islands to \$132 million over three financial years.
- 2 The funding for this proposal is sourced from within the existing IDC appropriation and no new funding is sought. The quantum of proposed expenditure requires Cabinet approval.

Relation to government priorities

- 3 The proposed expenditure reflects our whanaungatanga and our constitutional obligations to the Cook Islands to support effective self-governance, improved economic resilience, and delivery of core public services in the context of shared citizenship.
- 4 The proposed expenditure also aligns with the Government's policy framework for the Cook Islands, Niue, and Tokelau, recognising the unique characteristics of our relationships with these countries: stewardship, commitment, and interdependence.
- 5 By supporting a medium-term return to economic and social resilience in the Cook Islands, the proposed funding would align with the approach set out in the papers 'New Zealand's Pacific Engagement: From Reset to Resilience' and 'New Zealand's Pacific Engagement: Moving from COVID-19 Response to Recovery and Longer Term Resilience', which Cabinet approved on 4 October.
- 6 These papers set out Aotearoa New Zealand's approach to engagement with the Pacific. This engagement is steered by our desire for a peaceful, stable, prosperous, and resilient region in which Aotearoa New Zealand collaborates with others as a true partner. A significant impact of ongoing economic stress in the Cook Islands is likely to be migration to New Zealand. This has been the pattern in previous economic crises and would undermine the country's resilience. Providing economic support which avoids or mitigates this outcome would embody the new Pacific approach.

Executive Summary

- 7 The economic impacts of the COVID-19 pandemic on the Cook Islands have been amongst the most significant in the Pacific region, with GDP falling by an estimated 32 percent in the first fifteen months of the pandemic.
- 8 The temporary resumption of two-way quarantine-free travel between Aotearoa New Zealand and the Cook Islands between May and August 2021 will have contributed to government revenue and private-sector incomes. However, the recent suspension of tourism following the movement to Alert Level 4 in Aotearoa New Zealand places the Cook Islands once again at risk of fiscal crisis.
- 9 s6(b)(i)
- 10 In light of this, I consider that the following additional grant financing should be provided to the Cook Islands, from existing aid programme resources:
- NZ\$20 million to support government cash reserves in the short term; and
 - NZ\$40 million to provide support for infrastructure investment, to generate medium-term economic growth and a return to economic resilience.
- s6(b)(i)
- 11 The proposed grant financing recognises that the Cook Islands is not able to draw on support from any other like-minded bilateral or multilateral partners at this time. In the absence of further grant support from Aotearoa New Zealand, there is a genuine risk of a fiscal crisis occurring within the current calendar year.

Background

The economic impacts of COVID-19 in the Pacific have been severe and the outlook is negative

- 12 COVID-19 has had a profound impact on the Pacific, particularly for countries that are tourism-dependent, as countries throughout the region closed their international borders to limit or prevent the spread of the virus.
- 13 Since the beginning of the pandemic, Aotearoa New Zealand has been responding to the economic situation in the Pacific, including with direct budget support to mitigate the risks of fiscal crises.
- 14 The Cabinet paper 'New Zealand's Pacific Engagement: Moving from COVID-19 Response to Recovery and Longer Term Resilience' set out five resilience pillars that will guide the aid programme's engagement with the Pacific region. These pillars are economic and fiscal resilience; climate change and disaster resilience; governance resilience; social resilience; and intergenerational and cultural resilience. The paper makes clear that alongside long-term investment, we will also need to provide short term support to deal with the immediate impacts of COVID-19. One such example is fiscal crisis financing.

- 15 Cabinet is also today considering a package of further economic support to Fiji, which is managing a worsening COVID-19 outbreak, with severe economic impacts and negative implications for the budget deficit and for levels of government debt.
- 16 While Cook Islands and Fiji have been the immediate focus of our current economic support efforts, s6(a)
s6(a)
- 17 s6(a)
- 18 While economic support has been provided for a number of countries in the Pacific, the region's economic outlook remains negative, and there are significant downside risks. s6(a)
s6(a)
- 19 MFAT continues to monitor the economic situation in the Pacific, in coordination with Australia, the Asian Development Bank (ADB), the World Bank and the International Monetary Fund. s6(a)
s6(a)
- 20 s6(a)
- 21 s6(a)
- MFAT
- will continue to provide advice and assessments to Ministers on the support required for the region.

The Cook Islands economy has been especially affected by COVID-19

- 22 Border closures during the pandemic, while successful in keeping the virus out of the country, have had a severe negative impact on economic activity. The Cook Islands is heavily dependent on the tourism industry, with the CIG estimating that 65 percent of pre-pandemic economic activity had been directly derived from tourism, with another 20 percent from related industries.

23 The ADB calculates that GDP fell by 32 percent in the Cook Islands between March 2020 and June 2021, due directly to the economic impacts of the COVID-19 pandemic. The 2020/21 budget deficit is calculated at -26.6 percent, or NZ\$105.5 million.

24 Prior to the COVID-19 pandemic the Cook Islands had enjoyed two decades of economic growth and strong budget management. When the economic impacts of COVID-19 were first registered, the Cook Islands initially financed its economic response from its own Stabilisation Fund of NZ\$56.7 million. However, the severity of the economic downturn exhausted these funds.

25 s6(a)

s7(b)(ii)

26 Aotearoa provided an additional NZ\$3 million in support to Tokelau at the beginning of the COVID-19 pandemic, to support the country's immediate expenditure priorities. s9(2)(g)(i)

Fisheries revenue exceeded its forecast amount in the 2020/21 financial year by NZ\$6.1 million, and as a result, Tokelau returned a budget surplus in 2020/21 of NZ\$2.7 million.

27 In addition, Tokelau will be a recipient of substantial additional resources through the recently announced funding for climate finance. This, along with existing development activities in Tokelau, s9(2)(g)(i)

28 s7(b)(iii)

Aotearoa New Zealand has to date provided NZ\$19 million in additional budget support to Niue, which has primarily been disbursed as wage subsidies and other supports provided to businesses and households to mitigate the economic impacts of the pandemic.

29 s7(b)(iii)

¹ Following the economic disruption caused by the COVID-19 pandemic, this target ceiling for the debt-to-GDP ratio has now been raised to 50 percent, with a 'hard' ceiling of 65 percent.

30 s7(b)(iii)

31

Analysis

Aotearoa New Zealand has been a crucial partner to the Cook Islands...

- 32 Recent feedback from the Secretary of the CIG’s Ministry of Finance and Economic Management noted that Aotearoa New Zealand’s economic support of the Cook Islands during the COVID-19 pandemic has been “both timely and absolutely essential”.
- 33 Aotearoa New Zealand has provided NZ\$72 million in additional budget support to the Cook Islands in four tranches since the beginning of the COVID-19 pandemic. This sequence of support has responded to the needs of the Cook Islands as they have emerged over the course of the pandemic.
- 34 The additional budget support that Aotearoa New Zealand has provided to the Cook Islands in response to COVID-19 has been well used, consistent with the CIG’s fiscal prudence and sound financial management of the past two decades.
- 35 Funding provided by Aotearoa New Zealand has primarily been channelled into supporting the CIG’s Economic Response Plan (ERP), which was enacted rapidly in response to the pandemic. Elements of the ERP include:
- Wage subsidies for employees of firms that have lost income as a result of the pandemic, particularly in the tourism sector;
 - Financial support for sole traders, many of whom operate in the tourism sector or adjacent industries; and
 - Top-ups for existing social protection payments, such as the aged pension, disability pension and supports for households living in extreme poverty.
- 36 In addition, NZ\$2 million has been added to an existing IDC programme activity that provides adaptation grants and advisory support to small- and medium-sized businesses, mainly in the Cook Islands’ tourism sector.
- 37 Feedback received on the ERP in Rarotonga from private-sector representatives indicates that it has been highly successful, and has prevented widespread business closures in the tourism sector. The wage support measures in the ERP have further been credited with avoiding large-scale emigration of the Cook Islands’ working-age population to Aotearoa New Zealand during the COVID-19 pandemic.

... but further support is required as tourism is suspended once again

- 38 The resumption of tourism arrivals from Aotearoa New Zealand from 17 May until its suspension on 16 August 2021 (Cook Islands time) had seen the Cook Islands

economy begin to make progress on a tourism-led economic recovery. Tourism arrivals had exceeded initial estimates for this period, and were approaching 65 percent of pre-pandemic levels.

39 However, the current suspension of two-way quarantine-free travel following Aotearoa New Zealand's move to Alert Level 4 in August 2021 has interrupted this recovery, with negative implications for government revenues and cash reserves.

40 The CIG has recently reintroduced the wage subsidies and sole trader grants that had been in place during the initial border closure in 2020-2021, s6(b)(i)

41 s6(b)(i)

42 Aotearoa New Zealand provided grant support to the Cook Islands of NZ\$30 million in July 2021, on the basis of the ongoing economic impacts of COVID-19. We understand that this funding will be used to support cash reserves and government expenditures over the August to October period.

43 s6(b)(i)

44 While the two-way quarantine-free travel arrangement between New Zealand and the Cook Islands has been suspended due to community transmission of COVID-19 in New Zealand, the CIG has indicated that travel could resume if the rate of community transmission in New Zealand returns to a low level. The trajectory of the current New Zealand outbreak has increased uncertainty about when this will occur. The impact of the *Reconnecting New Zealanders* framework on border settings between New Zealand and the Cook Islands is not yet known. There is potential for it to increase the stringency of requirements and therefore impact on tourism levels. We will work to identify and mitigate impacts on tourism where possible.

The Cook Islands has no current alternatives for support

45 The Cook Islands has few alternative financing options. It is not a member of the World Bank, United Nations, or the International Monetary Fund. Further, it is not eligible to receive Official Development Assistance allocations from other bilateral partners following its graduation from OECD DAC eligibility in January 2020.

46 s6(a)

s6(a)

47

48

Support for the short term: Cash reserves to support immediate needs

49 While Aotearoa New Zealand has provided substantial grant financing to the Cook Islands during the COVID-19 pandemic to date, the latest disruption to the tourism-led recovery means that the Cook Islands is once again in need of grant support to sustain government cash reserves.

50 I now propose to provide an additional NZ\$20 million to support the Cook Islands, from within existing IDC allocations, to assist the CIG to manage the economic impacts of the suspension of tourism once again.

51 s7(b)(ii)

This contribution will bridge the gap in financing between our most recent grant support, and the upcoming loan from the ADB that is scheduled to be considered in December 2021.

52 s7(b)(ii)

The risk of Cook Islanders emigrating to Aotearoa New Zealand would increase further, and if this occurred it would worsen the economic recovery prospects of the Cook Islands.

53 MFAT officials are continuing to monitor the economic recovery of the Cook Islands, including projections for government cash reserves. s6(b)(i)
s6(b)(i)

s7(b)(ii)

Support for the medium term: Investing in infrastructure

54 s6(b)(i)

The CIG has identified public infrastructure investment as its preferred means of generating a return to economic resilience in the medium term.

55 I am now proposing to provide an additional NZ\$40 million from existing IDC programme resources as grant support for infrastructure investment, to be transferred this financial year.

56 Of this amount, NZ\$20 million will be drawn from the aid programme's Strategic Initiatives Development Fund (SIDF), and NZ\$20 million from existing country-programme allocations.

57 Public infrastructure investment will inject capital into the economy to generate GDP growth, replacing private capital that has been redirected to debt payments. Infrastructure projects will also generate employment opportunities that can be expected to assist in retaining workers in-country, and reduce the risk of emigration.

58 The possibility of outward migration of the labour force of the Cook Islands, whose residents share citizenship with Aotearoa New Zealand, is an ongoing risk for the Cook Islands' medium-term recovery. Following economic instability in 1996, the Cook Islands experienced a population decline of almost 17 percent. Renewed significant outward migration would diminish the Cook Island's workforce and have a negative impact on Cook Islands' medium- to long-term economic resilience.

59 I have determined that NZ\$40 million is an appropriate amount as a basis for giving a degree of medium-term certainty to CIG for undertaking detailed planning and design work for infrastructure projects. As the economy begins to return to resilience in the medium term and domestic resources become available, it is my expectation that the CIG will begin to provide financing to its domestic infrastructure pipeline from within the CIG budget, as resources allow.²

60 The proposed amount of funding is also considered to be within the absorptive capacity of the Cook Islands, s6(b)(i)

61 s7(b)(ii)

² The ADB has also indicated that additional lending may be available for infrastructure investment as resources become available in the 2023/24 financial year.

s7(b)(ii)

Grant financing remains the preferred modality of the aid programme.

62 I propose to channel this funding through the existing Cook Islands-New Zealand Infrastructure Trust Fund, for which the New Zealand High Commission in Rarotonga sits on the Steering Committee. This partnership-focused mechanism ensures that we participate in strategic decisions on investments that are a priority for the Cook Islands, have a role in the high-level oversight over the use of funds including ensuring climate resilience is explicitly considered and a human rights based approach is applied, and can facilitate access to technical assistance where CIG requests this.

63 In April 2021, \$20 million in budget support was provided as a grant to the Cook Islands, to support government cash reserves and macroeconomic stability.

s7(b)(ii)

64 Since April 2021, the CIG has approved a new National Infrastructure Investment Plan, prepared with technical assistance from the Pacific Region Infrastructure Facility (of which MFAT is a member). The Plan will guide infrastructure investments over the next 10 to 15 years. The Plan notes the significant environmental challenge for the Cook Islands that is posed by inadequate sanitation, which is expected to be exacerbated by the return of tourism in a COVID-19 recovery context. The Plan reaffirms the CIG's commitment to a piped reticulated solution (such as MTVKTV) as the only viable long-term option to deal with the sanitation impacts of the concentration of tourism accommodation on the southern side of Rarotonga.

65 The CIG's Ministry of Finance and Economic Management has advised MFAT that it sees MTVKTV as a critical project for stimulating the economy. It is making progress in negotiations with landowners on land for treatment and disposal and much of the ground work has already been done in terms of feasibility and environmental impact assessments. Access to funding is a barrier to progressing detailed design and construction.

s7(b)(ii)

s7(b)(ii)

Implementation

66 The proposed package of support recognises the need for both short-term flexibility and medium-term certainty in order to generate a sustained economic recovery.

67 If approved, the proposed NZ\$20 million in support for cash reserves will be earmarked for expenditures that meet the most immediate short-term needs, such as the CIG's existing wage subsidy and small trader grant, social protection payments, and expenditure on core public services.

- 68 If approved, the proposed NZ\$40 million in funding for infrastructure investment will be disbursed through the existing jointly governed Cook Islands-New Zealand Infrastructure Trust Fund.
- 69 The CIG has met Aotearoa New Zealand's accountability expectations regarding public financial management, including reporting and progress towards bringing audit reports up to date. The Government has also undertaken to provide quarterly summary reporting, and has been reporting on progress against outputs in the ERP.
- 70 The Development Sector Committee, jointly governed by Cook Islands and Aotearoa New Zealand officials, and the annual Joint Ministerial Forum will also be key mechanisms for monitoring and dialogue on outcomes achieved through our support.

Financial Implications

- 71 This proposal will cost NZ\$60 million and will be transferred this financial year. The funding will be drawn from two sources: the Strategic Initiatives Development Fund (SIDF) of the IDC appropriation³; and the existing resources from the Cook Islands country allocation.
- 72 The breakdown of the proposed funding will be as follows:

Amount	Purpose	Source
NZ\$20 million	Support for short-term cash reserves	SIDF
NZ\$20 million	Support for medium-term infrastructure investment	SIDF
NZ\$20 million	Support for medium-term infrastructure investment	Cook Islands core country programme allocation

The proposal does not require new funding. MFAT does not anticipate exceeding the IDC threshold in the current financial year as a consequence of this funding decision.

Legislative Implications

- 73 There are no legislative implications from this proposal.

Impact Analysis

- 74 There are no regulatory, climate, or population implications arising from this proposal.

Human rights

- 75 s7(b)(ii)

It will contribute to the realisation of human rights in the Cook Islands by enhancing the CIG's ability to self-implement human rights such as the right to

³ The total funding available under the SIDF at the start of the triennium was NZ\$188 million. The SIDF balance will fluctuate over the course of the triennium, as it operates as a revolving fund to enable flexible and responsive management of allocations.

social security, adequate standard of living, food security, housing, education, health, economic empowerment, and good governance.

- 76 This is consistent with Aotearoa New Zealand's focus on human rights in development cooperation contributing to reducing inequality and enhancing well-being, stability, and security. Promoting human rights and social inclusion across the Pacific is integral to New Zealand's International Human Rights Action Plan, as well as our commitment in the 2030 Sustainable Development Goals to leave no one behind: kua tētahi e whakarērea.

Consultation

- 77 The Treasury have been consulted and are comfortable with the proposed approach.

Communications

- 78 Following approvals and agreement with the Government of the Cook Islands, I propose to make an announcement on this support, in line with a communications plan developed by officials.

Proactive Release

- 79 I intend to proactively release this Cabinet paper following Cabinet consideration, subject to necessary redactions including to preserve our relations with the Government of the Cook Islands, and any sensitive information that has been shared with Aotearoa New Zealand.

Recommendations

- 80 I recommend that Cabinet:
- 1 s7(b)(ii) and the suspension of tourism in August 2021 has interrupted the economic recovery.
 - 2 **Note** that the Cook Islands is not currently able to receive support from any other like-minded multilateral or bilateral partners.
 - 3 **Note** that the Government of the Cook Islands requires short-term budget support for government cash reserves, s7(b)(ii)
 - 4 **Agree** that NZ\$20 million from within existing aid programme resources be provided as a grant to the Government of the Cook Islands, within the current financial year, to support government cash reserves.
 - 5 **Agree** that NZ\$40 million from within existing aid programme resources be allocated to infrastructure investment to support the medium-term economic recovery of the Cook Islands. This funding will be provided as a contribution to the New Zealand-Cook Islands Infrastructure Trust Fund.
 - 6 **Note** that the total proposed funding from this Cabinet paper is NZ\$60 million.

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- 7 **Note** that the quantum of proposed expenditure requires Cabinet approval.
- 8 **Note** that the funding for this proposal is sourced from within the existing IDC appropriation and no new funding is sought.

Authorised for lodgement

Hon Nanaia Mahuta

Minister of Foreign Affairs

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Minister of Foreign Affairs

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