



COMMONWEALTH OF THE BAHAMAS

2005/2006

BUDGET COMMUNICATION

Presented to the Honourable House of Assembly

By

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Acting Prime Minister

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Acting Minister of Finance

On

Wednesday, 25th May, 2005

2005/06 BUDGET COMMUNICATION

In the absence of the Rt. Hon. Prime Minister and Minister of Finance, I have the honour of presenting the 2005/06 Budget Communication to this Honourable House of Assembly. I am sure that at this time especially, the prayers of this Honourable House are for his full and speedy recovery to return to take his rightful place.

I can assure this Honourable House that this Communication is presented with the Prime Minister's full approval. He would, of course, be here to present it in person but for the concerned advice of his doctors that he

should take time to give himself the opportunity of proper convalescence.

In the preparation of this Budget Communication I am sure that the Prime Minister and my Minister colleagues would wish me to acknowledge the work of the Minister of State for Finance, Senator James Smith, and the staff of the Ministry of Finance.

Before delivering this Communication I wish to thank Almighty God for bringing me to this place and time, and pray that He will assist me, His humble servant, in delivering this Budget Communication to this Honourable House and to the Nation.

INTRODUCTORY COMMENTS

Consistent with the new Rules of Procedure of this Honourable House, in order to focus attention on the key policy issues in the 2005/06 Budget, I am aiming for conciseness in the oral dimension of this Budget Communication. Consequently, the 2005/06 Budget Communication will focus on matters of national strategic importance. The details of these matters will be dealt with by the Ministers and Parliamentary Secretaries concerned with particular Ministries and other agencies in the course of their contributions to the Budget Debate.

However, I do want to stress that this procedure does not mean that conciseness is being attained at the expense of comprehensiveness in the 2005/06 Budget Communication. On the contrary, this Budget Communication and the Annexes attached to it enable the budget documentation to be more expansive and comprehensive in coverage than the documentation for previous budgets.

BUDGET DOCUMENTATION

The innovative features of the documentation are threefold.

Firstly, the full economic background to the Budget by the Ministry of Finance, the Central Bank of The Bahamas and other economic

agencies is set out in Annex A. Hitherto, the Communication contained only a brief summary.

In relation to the Central Bank of The Bahamas, I would like to take this occasion to express the nation's appreciation to the Governor of the Central Bank, Mr. Julian Francis, who is retiring to take up the prestigious position of Chairman of the Grand Bahama Port Authority. As Governor, Mr. Francis was closely involved in the development of the Central Bank's regulatory functions. I am sure that I am reflecting the views of all Members of this Honourable House when I express our deep appreciation to Mr.

Francis for his work. I am sure that I can add that he takes with him our sincerest wishes that he will have a similar outstanding record of achievement at the Grand Bahama Port Authority which is one of the most important entrepreneurial enterprises in the Bahamian economy.

Mr. Francis will be succeeded as Governor by the Deputy Governor, Mrs. Wendy Craig, who also has a record of distinguished service to the Bank. I am sure that we all wish her well in her new role as Governor.

In this context I wish to mention that the Government is establishing a committee that is representative of all of the financial

regulatory institutions, namely the Ministry of Finance, the Central Bank, the Registrar of Insurance, the Securities Commission, and the Registrar General, to consider options for consolidating these agencies into one or more regulatory organizations. The heads of each of the regulatory institutions will serve on the committee which will meet under the chairmanship of the Minister of State for Finance. I am pleased to announce that the former Minister of Finance, Sir William Allen, has agreed to be available to participate in the work of the committee. This gesture is a demonstration of the non-partisan approach to dealing with a sector, the financial services

sector, which is of such importance to our economy.

The second innovative feature of the budget documentation for 2005/06 arises from up-to-date national accounts data from the Department of Statistics being available. The data are presented where appropriate in the Tables in Annex B. This is a major advance over previous years where only provisional data were available for many years and the Ministry of Finance had to rely either on projections made by the International Monetary Fund, the IMF, or on various methods to project the movement of the national accounts on the basis of indicators. In

fact, the recent IMF Article IV Consultation Mission was able to rely on the national accounts data from the Department of Statistics for the years 1989 to 2004, rather than being obliged to prepare its own estimates.

On this matter I would like to say that the IMF Report will be published in early July following consideration by the IMF Executive Board. On the basis of discussions which the Mission had in Nassau, there is every reason for assuming that the Mission generally approves the policy thrust of the Government in targeting key fiscal indicators and putting in place appropriate fiscal policies to realize

these indicators. I will deal with these matters later in this Communication. It might be added that the IMF assessment is in accord with the A ratings of the Bahamian economy, which is implied by the A3 rating of the sovereign debt of The Bahamas by Moodys, and the equivalent rating by the other major Rating Agency, Standard and Poor's.

The Department of Statistics is to be congratulated on the production of the national accounts data the details of which it will publish shortly. In preparing the national accounts data for the years 1989 to 2004, the Department of Statistics has had the strong support of the Ministry of Finance and of the

Central Bank of The Bahamas, together with the expertise and experience of a resident specialist from Statistics Canada, and technical assistance from the IMF. In complimenting the Department of Statistics I wish also to acknowledge the invaluable contributions of these organizations and personnel.

It is intended to install this updating of the national accounts data as an annual process, so that The Bahamas will have available, as in 2005, up-to-date national accounts data at all times. To assist with this process, the Ministry of Finance will ensure that the

Department of Statistics receives whatever technical assistance is required.

The third innovative feature of the documentation for the 2005/06 Budget is the inclusion of a summary Table setting out Multi-Annual Budget Forecasts. Again, this is an advance from previous Communications where the focus was on the annual fiscal position. The Table projects the public finances for the two fiscal years after 2005/06, namely 2006/07 and 2007/08, on the basis of present trends and policies. The necessarily tentative basis of the projections is explained in the notes to the Table. The purpose is to provide some indication, howsoever tentative,

of the medium-term strategic framework of the public finances in underpinning the stability and sustainable growth of the Bahamian economy. Such a framework is useful in highlighting that commitments are only made when the full implications are analysed. Experience elsewhere demonstrates how unwise it can be to make major commitments prematurely, without analyzing in depth the economic and fiscal ramifications. I am sure that the Bahamian public and the international community will appreciate and endorse the Government's philosophy on this matter.

In summarizing these improvements and innovations in the presentation of the Budget Communication, I trust that they will assist in making the oral presentation as concise as possible for the convenience of this Honourable House and of the Bahamian public, while providing substantial additional valuable economic and fiscal information as Appendices to the Communication.

2005/06 and Medium - Term Economic

Outlook

The Government and the community are interested in economic growth because economic growth provides more and better jobs for Bahamians. There is the extra benefit

that as employment and incomes rise, Government revenue increases and this enables the Government to spend more on providing a wider range of essential services.

The Economic Background in Appendix A indicates that the Bahamian economy commenced to grow strongly in 2004, when the growth rate was 3% in real terms. As Table I indicates, the projections made by the recent IMF Article IV Mission suggest that strong growth, of 3.5%, will occur in 2005, largely as a result of the volume of investment projects coming on stream. Moreover, there is every likelihood that these strong rates of growth will be sustained in the years after 2005

because of the timing of further productive capital inflows some of which have already been approved and will come on stream in those years. An important consideration in this respect is the outlook for the global economy. We cannot take a benign global outlook totally for granted. The recent meeting of the Ministers of Finance on the International Monetary and Financial Committee of the IMF cautioned that while the global outlook is still very good, rising imbalances, high oil prices, and the prospect of rising global interest rates suggest that the balance of risks is more negative.

Nevertheless, in the case of the Bahamian economy, while we heed these cautionary remarks on the global economic outlook, the growth of the Bahamian economy, which commenced in 2004, could continue for the rest of this decade.

The commencement of a period of strong growth is due in very large measure to the success of the Government's investment policy. The Government has been very active and vigilant in promoting the attractions of The Bahamas for high-quality investment. It is important to emphasise that there is great international and regional competition in attracting this kind of high-quality productive

international investment. Therefore, it was crucial for the Government to pursue, with the utmost vigor, the aim of promoting the attractiveness of The Bahamas as an ideal investment location. Otherwise, some of the investment could have been diverted to other international and regional tourism destinations.

Furthermore, the Government has been equally concerned to promote investment by Bahamian entrepreneurs. The establishment of a Venture Capital Fund is evidence of this policy. In the 2004/05 Budget \$1million was made available and this has been augmented by a further \$1million in the 2005/06 Budget.

As the Fund succeeds and develops the Government will provide additional resources.

OPPORTUNITIES AND CHALLENGES

The sustained strengthening of the Bahamian economy will present the Government and people of The Bahamas with opportunities and challenges. Indeed, one could use these words interchangeably because to avail of the opportunities means to accept the challenges which the opportunities present.

One of the challenges is to ensure that the capital structure, both physical and human, is in place to accommodate the expected economic growth, and to maximize its

potential benefits to the Bahamian people in both the short-term and the medium-term. Other challenges can be met as the economic growth comes on stream.

It is important to distinguish between the two different sets of challenges and opportunities. In the first instance, commitments may have to be made in anticipation of the revenues arising. Anticipation is essential so as to equip the economy, in terms of both human and infrastructural capital, to maximize the benefits of growth. In the second set of challenges, those challenges which a buoyant economy can address, the task is to wait until

the revenues are flowing before undertaking expenditure commitments.

NATIONAL INFORMATION AND
COMMUNICATIONS FRAMEWORK

I stated that one of the challenges is to ensure that our human and physical capital structure is in place to accommodate and then maximize the benefits of the upsurge in the economy.

As regards human capital, by which we mean people who are educated well enough to hold good jobs, the Ministry of Finance is commissioning Canadian technical assistance to develop a National Information and Communications Framework, in short an NIC

Framework. The technical assistance is being sought from an expert agency of the Canadian Government, entitled *Consulting and Audit Canada*, CAC. This agency has extensive and successful experience in providing technical assistance in this matter to many other countries.

The NIC Framework which will be developed is intended to enable The Bahamas to develop as a nation that maximizes the power, reach, versatility and innovation of information and communications technology. The Framework will provide on-line access to healthcare, education, and government services such as land registration and land use

policy, and will be a driving force in developing e-commerce in The Bahamas. I might also mention that the land use and administration programme is assisted by the Inter-American Development Bank, IDB.

Increased levels of e-commerce will enable Bahamian companies to compete in the global marketplace, and the development of a vibrant and entrepreneurial information technology sector will create employment, encourage diversification, and boost investor confidence. A National Information and Communications Technology Policy paper will be published in due course. This Paper will integrate with the *Policy Statement on Electronic Commerce and*

the Bahamian Digital Agenda published by the Ministry of Finance in January, 2003.

The Framework also envisages the transformation of the Bahamas Telecommunications Company, BTC, into a state-of-the-art communications leader. This transformation process is already the subject of intense work with the assistance of international consultants. The transformation will enhance the current operations of BTC, as well as preparing BTC for graduation into a privatized entity at the cutting edge of technological development in communications.

As regards physical infrastructure, BTC is proceeding urgently with the project to develop a fibre-optic cable linkage to provide all of the inhabited islands of The Bahamas with reliable and efficient connection. This project is of paramount importance to enable hotels and other facilities to develop in the inhabited Family Islands and to provide each Island with diversified economic opportunities. As necessary, the highest priority is being given to developing other necessary infrastructure in the Family Islands such as airports, roads and utilities.

DISASTER MANAGEMENT AND RECOVERY

A further crucial dimension of this matter is to ensure that each inhabited Island in The Bahamas is enabled to cope with natural disasters such as hurricanes and flooding. This means ensuring that the physical capital is as strong as possible to withstand the most severe weather but also ensuring that the response to emergencies is immediate, orderly, and effective in restoring economic and social life to pre-storm levels. To this end, priority is being given to the development of an emergency response organization with the administrative capacity to mobilize as required in an immediate, orderly and effective

manner. The prodigious efforts made to deal with the recent disasters notably in Grand Bahama and Abaco are an enormous tribute to everyone concerned. However, we can move forward by assimilating the lessons learned from these recent disasters into the development of a modern high-powered and highly professional organization authorized, staffed and equipped to respond systematically to emergencies. Work is ongoing on developing this organization and proposals in this regard will be submitted to Parliament in due course. Valuable assistance is being provided by the *Inter-American Development Bank, IDB, and the Economic Commission for Latin America*

and the Caribbean, ECLAC, in this and related matters.

FISCAL MANAGEMENT

As the Bahamian public has been made aware, expert advice is that we would do well to limit the ratio of Government Debt to GDP to as near as possible to 30% of GDP so as to avoid the problems which would arise from a ratio significantly in excess of that level. These problems are for instance, those which would arise from a sharp and severe downturn in the global economy. If such an event were to arise, it could drastically reduce tourism revenues and therefore Government revenues; in such circumstances additional taxation to

bridge the gap between revenue and expenditure would be unwarranted, imposing as it would, a heavier burden on an economy already deflated. Reducing expenditure would mean cutting back on employment in the public sector paid for out of the Consolidated Fund. Experience elsewhere shows that when the ratio of Government debt to GDP moves significantly above 40%, the scope for further Government borrowing is severely constrained. In those circumstances the only options available to a Government might be the painful taxation and expenditure options. In other words, fiscal deficits arise if we spend more than we earn in revenues, and if this situation

continues for long enough we build up massive borrowing problems.

Circumstances are quite different if the ratio of Government debt to GDP is closer to 30%. There would be much greater scope to avoid these drastic remedies because there would be the capacity to borrow until the economic situation improves and until revenues recover so as to again close the gap between revenue and expenditure. This is what transpired in 2001 and 2002.

To bring the ratio of Government debt to GDP to as close as possible to 30%, revenues must consistently attain the level of 20% of GDP. At that level, we can also provide the

level of resources which we need for ongoing public expenditure while containing the fiscal deficit. For example, if the ratio of revenue to GDP achieved is, say, 19%, the amount of revenue foregone by not realizing the 20% mark is some \$60million. To put this \$60million in context, it is two-thirds of the combined annual subsidies paid to Bahamasair, the Water & Sewerage Corporation and the Broadcasting Corporation of The Bahamas; it is about one-half of the combined amount spent on the Royal Bahamas Police Force and the Royal Bahamas Defence Force; and it is about one-half of the amount which we spend on

public hospitals. Therefore, 1% of GDP is not a trivial amount.

Successive governments have tried to attain the ratio of Government revenue to GDP of about 20%. At that level, we could enjoy a reasonable level of public services without introducing taxation to pay for them. We could maintain living standards in The Bahamas well above that of many other countries in the Region, and make the Bahamian economy one of the most competitive in the Region.

However, the ratio of Revenue to GDP of 20% is becoming increasingly hard to achieve because of the narrowness of our revenue system, heavily dependent as it is on Customs

revenues and the non-taxation of services. Thus, the expansion of essential public services has resulted in fiscal deficits emerging which have been met by borrowing. As a result, the level of Government Debt to GDP has risen inexorably since the year 2000.

In recognition of this issue, in the 2005/06 Budget the Government is aiming to contain the ratio of Government debt to GDP to under 38%. By this step, the Government is continuing the process commenced in 2002/03 of controlling the fiscal deficit so as to bring the ratio of Government debt to GDP down to about 30% within a 5 year period.

Of course, a major challenge is to ensure that the revenues are properly collected. To meet that requirement we must have in place appropriate revenue instruments and structures.

As regards revenue instruments, we must have in place the most efficient possible revenue system operating the most appropriate tax 'handles'. For example, we must be able to plot and monitor all features of imports so as to ensure that the appropriate Customs Duties are paid. In the case of the Customs Department, the Trade Information System, TIMS, is now operational and there has already been an improvement in

collections and administration. Other major revenue agencies are also being reviewed in order to implement improvements.

But we must be able to go further in the sense that some of our taxes are linked with economic activities which might be transformed into new forms which our existing tax 'handles' do not touch. For example, if the renting out of investment properties such as apartments and homes, is not picked up by the present tax handle, the hotel room occupancy tax, an important taxable stream is not paying its fair share of the tax burden.

Measures were taken in 2004/05 to strengthen revenue administration and these

are being continued, where appropriate, in 2005/06 and augmented by additional specific measures. These include the following:-

- The introduction of cash receipting systems, to replace manual receipting of revenue, and thereby reduce leakages of revenue.**
- The introduction of the use of major credit cards in all revenue Agencies, to facilitate the payment of fees and taxes due to Government.**
- Improvement to the assessment process for real property tax, by bringing more properties onto the assessment register.**

- **The exemption on owner occupied properties was increase from \$100,000 to \$250,000; however, to avail of this concession, homeowners have to pay arrears or enter into a satisfactory arrangement with the real property tax office.**
- **Compile revenue statistical data to provide increased transparency of the revenue numbers.**
- **Amend the Stamp Act to close the loopholes and improve administration of the revenue collection process.**
- **Establish a new category of trained officers to act as Compliance Officers, to**

undertake review and analytical work in connection with revenue administration, in the areas of Hotel Room Tax, Stamp Tax, Business Licence and Ticket Tax.

- **Amend the Casino Act, to provide for payment of casino tax to the Gaming Board to facilitate better supervision of the timely payment of casino taxes.**

REVENUE REFORM

Even with significant improvement in revenue administration, the task of reaching and sustaining the ratio of Government revenue to GDP of 20% would be difficult. This conclusion suggests that within the next 5 to 10 years, The Bahamas may have to radically

change its revenue system. The pressures to do so come from two distinct forces, one international and the other domestic.

I have already outlined the position whereby the consistent attainment of a ratio of revenue to GDP of 20% seems to be increasingly difficult to achieve, primarily because of the structure and narrow tax base of our revenue system. Nevertheless, we are continuing to move to enhance the administration of our existing revenues until this process is exhausted. At some point in the medium-term firm consideration will have to be given to how best to reform our present system.

In the case of the international forces, within the context of the World Trade Organisation there will be pressure on The Bahamas to reduce and simplify its Customs Duties. The reduction in Customs Duties would mean finding a satisfactory replacement to yield the same level of revenues.

There is national consensus that The Bahamas should not adopt an income tax system. Therefore, reform of the revenue structure would mean the implementation of a Value-Added Tax, VAT, or a similar tax. This Government has no intention of introducing such a tax now or in the near future. Indeed,

no government would be able to implement a VAT at short notice. This is because a VAT is a complex measure requiring careful planning and preparation, extending over several years, and would involve considerable consultation with those likely to be affected such as businesses and ordinary Bahamians. It would also involve the preparation of legislation to give effect to it.

In recognition of the fact that it would be useful to explore all aspects of a possible VAT for implementation at some future date when the necessity and desire for change materialises, the Ministry of Finance is continuing to commission reports on

operational aspects of a VAT. However, I can assure the House that there are no plans to implement a VAT now or in the immediate future.

PUBLIC SERVICE REFORM

Clearly there will be heightened concentration on the importance of training by the Bahamian public and the Public Service for the eventual transition to a VAT and for the implementation of the National Information and Communications Framework. In the case of the Public Service, this heightened concentration on training forms an important element of Public Service Reform. To ensure that the Framework is

implemented resulting in e-government and that the revenues, including VAT, are properly collected and accounted for, means that we must have in the public sector a highly disciplined, motivated and trained workforce. Every member of the Public Service will be encouraged to participate and there will be no redundancies and cutting back on the Public Service. Public Service Reform does not involve such measures but aims to increase productivity and improve the quality of service to the public.

The Government considers that it is crucial to ensure a climate of good industrial relations in our economy. The lead in this

regard falls to the public sector. Incomes expectations are high, especially in light of the imminent inflow of major investment projects.

In view of what has been said in relation to revenue failing short of the 20% target, it is important to urge restraint and the expectations on incomes should be tempered until the target is achieved. A climate of harmonious industrial relations in the public sector is important to the Government and the Nation. The Government is presently reviewing its responses to the proposals on labour issues by the public sector unions and staff associations. The Government is pleased that the proposals encompass salary and non-salary

matters which will assure industrial harmony throughout the public sector.

In order to assist in our responses to the proposals, we expect to commission a study by an international expert on the orderly and equitable evolution of public sector pay and other benefits in the medium-term. The study would also include the actuarial costing of the pensions and other benefits arising.

The Government is also interested in requests from some of the staff associations and public sector representatives to examine the issue of leap frogging whereby a pay increase granted to one group and not to another results in anomalies which cause

dislocations in the service. The idea is to further study this issue with a view to establishing transparent principles so that increased demands by one group will not be met without regard to the principles applied to another group.

It is important that there be a link between public sector pay and productivity and to the enhancement of the competitiveness of the economy. Of course, in view of what has been said about the fiscal situation, it is crucial that any pay increases have regard to the capacity of the Consolidated Fund to meet the increases without additional taxation. The proposals

from the public sector unions and associations indicate a willingness to consider all of these issues.

Accordingly, the Minister of Foreign Affairs and the Public Service will be contacting the public sector unions to discuss the matter further. In this context, the Ministry of Finance has in its budgeting provided some funding in anticipation of pay increases for public servants and related groups, following comprehensive and harmonious negotiations. The budget provision also provides for increases in pensions for retired public servants.

The continuation of a climate of industrial relations harmony throughout the public sector is essential in attracting investment to the economy, and in enabling the private sector to expand and enhance employment opportunities.

I wish to emphasise that in order to demonstrate commitment to moderation in incomes and benefits, it is not proposed to increase the pay and benefits of Ministers, Ministers of State, Parliamentary Secretaries and Members of Parliament and Senators.

TRADE ISSUES

The process of preparing for negotiating entry on acceptable terms into the World

Trade Organisation is continuing. Similarly, the discussions on the Free Trade Area of the Americas may resume shortly, and the Bahamian teams are ready to participate as before. It is the intention to bring any agreement which emerges to Parliament for approval but at the present rate of progress of the discussions, that date is some time away.

The Caribbean Single Market and Economy, CSME, is the subject of considerable attention with a great deal of heat and not a lot of light being brought to the matter. The Government has no intention of committing to any international or regional grouping which could or would be damaging to the interests of

The Bahamas. The Bahamas has derogations from any aspects of the CSME which would be contrary to our interests. The primary advantage of the CSME to The Bahamas is the avoidance of isolation in international and regional discussions on economic issues. In these trade issues, the appropriate Ministers will deal thoroughly with these matters during their contributions to the Budget Debate.

PUBLIC EXPENDITURE MANAGEMENT

The enhanced revenue stream in the medium-term will permit us to develop and improve essential Government services in line with sustainable revenue growth. As the prosperity of our society and economy grows it

is crucial to ensure that we develop as an inclusive society whereby no person, no community or no social group, should perceive themselves to be excluded from the improvement in our economic welfare. In that regard, we must pay particular attention to the weak and elderly, to those with special needs, to disadvantaged youth, and to isolated communities. Social problems can fester in any environment where a particular group may feel overlooked or disadvantaged. Therefore, everyone must be made to feel that they are participating in the development of our polity, our society and our economy. If we do not address the issues at their root, the inclusion

of all in the welfare of our nation, we will have to spend enormous resources later in endeavouring to put in place remedial measures to deal with the problems which emerge. This leads to consideration of the Government's fiscal programme for 2005/06.

2005/06 FISCAL PROGRAMME 2005/06

The 2005/06 Budget provides for a number of important expenditure commitments and a number of significant revenue measures with modest cost implication.

The total for Recurrent Expenditure is \$1,214 million, which is an increase of \$39 million or 3% over the 2004/05 Budget. More

importantly, it is \$64million or 5.5% over the 2004/05 Projected Outturn. Therefore, Recurrent Expenditure shows a significant increase in real terms, that is well in excess of the rate of inflation.

The single major component of the increase is the provision in the Ministry of Finance Estimates for pay increases for public servants and related groups, arising from the present negotiations, as well as some increase in benefits for retired public servants. Another important increase is for the improvement in insurance arrangements for the Royal Bahamas Police Force, the Royal Bahamas Defence

Force and the other Law Enforcement Officers.

The distribution of Recurrent Expenditure is as follows:

- Debt Interest and Redemption is \$188million or over 15% of total Recurrent Expenditure of \$1,214million.**
- The Department of Education is \$157 million or 13% of the total; the Ministry of Education receives \$32million or 3% of the total; the College of The Bahamas receives almost \$20million plus fees which amounts to over 2%; the Bahamas Vocational and Technical Institute receives almost \$5million and the**

Department of Archives receives \$2million. The combined education area is therefore, \$216million or 17.8% of the total.

- The Public Hospitals Authority receives \$128million or 11% of the total; the Department of Environmental Health receives \$26million or 2%; the Department of Public Health receives \$21million or 2%; and the Ministry of Health receives almost \$10million or almost 1%; thus \$185million or 15% of Recurrent Expenditure is on Health.**
- The Ministry of Tourism receives \$78million or 6.4% of the total.**

- **The Department of Public Service receives almost \$72million or 6% of the total, mainly for pensions, rents, and the insurance for Police, Defence, and other Law Enforcement Officers. The total amount for this insurance programme for Law Enforcement Officers is \$8million.**
- **The Royal Police Force receives \$94million or almost 8%; the Royal Bahamas Defence Force receives \$34million or 3%; Prisons receives almost \$17million or almost 1.5%; the Ministry of National Security receives almost \$1million; thus, the combined amount for these security services is**

\$146million or almost 12%. As stated, the provision for insurance of Law Enforcement Officers is in the Department of Public Service Estimates amounting to \$8million.

- The Ministry of Labour and Immigration, the Department of Labour and the Department of Immigration receive \$19million or almost 2%.The Department of Social Services receives \$24million or 2%; the Ministry of Social Services and Community Development receives \$3million; the provisions for the Simpson Penn Centre for Boys and the**

Willamae Pratt Centre for Girls are about \$1million each.

- **The Ministry of Youth, Sports & Culture receives over \$15million or almost 1.5%.**
- **The Ministry of Agriculture, Fisheries and Local Government and the related Departments receive \$34million or 3% of the total.**
- **The Office of the Attorney General receives almost \$9million; the Judicial Department also receives almost \$9million; the Court of Appeal and Magistrates Courts receive almost \$8million; overall the legal system receives \$25million or 2%.**

- **The Post Office receives almost \$8million, and the Port Department receives \$6million.**
- **The Ministry of Transport and Aviation receives almost \$8million, the Road Traffic Department receives almost \$6million, the Department of Civil Aviation receives \$9million, and the Department of Meteorology receives over \$2million; the Airport Authority receives \$3million.**
- **The Ministry of Works and Utilities and the Department of Works receive over \$23million.**

- **The Ministry of Finance receives \$44million, of which \$24million is the global amount for negotiated pay settlements for the Public Service, and \$2million is for pensions adjustments for retired public servants; Customs receives \$23million, the Treasury over \$8million and the Department of Statistics receives over \$3million.**
- **The Ministry of Foreign Affairs and the Public Service receives over \$16million.**
- **The Ministry of Housing and National Insurance and the Department of Housing receive almost \$5million. The Estimates for this Ministry provide for**

the creation of the new Department of Urban Renewal which receives a budget of almost \$2million in 2005/06. The success of the urban renewal programme is one of the highest priorities of the Government, and as required, additional resources will continue to be committed to the success of the programme. The new Department will play a critical role in coordinating the input of the many Government agencies into the programme. The expenditure allocations for the inputs of these other agencies is provided for in their 2005/06 Estimates.

- **The Ministry of Trade & Industry receives \$4million.**
- **The Ministry of Financial Services and Investments receives almost \$4million.**

The vital elements of Government, the Office of the Governor General, the Senate and House of Assembly, the Department of the Auditor General, Cabinet Office and the Offices of the Prime Minister and of the Deputy Prime Minister are also provided for.

As regards Capital Expenditure, the total is \$165million, which is an increase of \$17million over the 2004/05 Budget or over 25% over the 2004/05 Projected Outturn.

The major components of the increase over 2004/05 are

- The Ministry of Works and Utilities is receiving an allocation of almost \$56million or 33% of the total for Capital Expenditure.**
- The Ministry of Education is receiving an allocation of almost \$19million which is an increase of over 11% over 2004/05.**
- The Royal Bahamas Police Force is receiving \$7million which is an increase of \$2.6million or nearly 60% over 2004/05. This increase is primarily for the new Police Communications System.**

- **The Royal Bahamas Defence Force is receiving almost \$5million which is an increase of 14% over the 2004/05 allocation.**
- **The Department of Local Government which is receiving an allocation of \$2.3million which is over 20% more than in 2004/05.**
- **The Ministry of Youth, Sports and Culture which is receiving \$3.5million which is an increase of almost 60% over 2004/05.**
- **Sundry Capital Expenditure provides Government financing for Bahamasair, the Water and Sewerage Corporation, and**

the Broadcasting Corporation of The Bahamas.

- **Major increases are also provided for Prisons, Foreign Affairs, Customs, Social Services & Community Development, Post Office, Civil Aviation, Post Office, Port, Agriculture & Fisheries, Department of Environmental Health Services, the Ministry of Health, and the Public Hospitals Authority.**

The 2005/06 Budget provision for Recurrent Revenue is \$1,145million, an increase of \$93million or 9% over the 2004/05 Budget. Revenue performance in this current calendar year, 2005, is tending to improve and

it may be possible to achieve the 2004/05 Budget target. The reason for projecting an increase of 9% over 2004/05 is because of the strengthening of the economy, with growth in current terms of over 5%, and the heightened emphasis being given to concrete and specific improvements in revenue administration.

The significant concessions being made in 2005/06 are :-

- The rate of Customs Duty on Electric Generating Sets is being reduced from 35% to 10% in order to assist in meeting emergencies caused by hurricanes and storms when electricity to households and businesses is disrupted.**

- **In order to encourage the use of alternative sources of energy for heating, the Customs Duty on Solar Panels and related parts is being made duty free, from the existing rate of 35%.**
- **So as to encourage the use of helmets by persons riding motor-bikes and scooters, the Customs Duty on safety head gear is being eliminated, from the existing rate of 35%.**
- **The Customs Duty on certain paper used by commercial printers is being reduced from 35% to 15%.**
- **The rate of Customs Duty on visual teaching aids often personally purchased**

by teachers to assist in the classroom is being eliminated, from the present rate of 35%.

It is intended to pursue the improvement of all of our national airports so as to raise them to the highest standards required. Accordingly, a variety of Air Navigational Fees and related charges in the Family Islands are being increased to more realistic levels to meet part of the cost. In addition, it is intended to implement Passenger Facility Fees at major airports as part of the cost recovery exercise.

CONCLUSION

The Rt. Hon. Prime Minister has given me the privilege of presenting the 2005/06 Budget Communication. The Communication sets out the strategic path which the Government intends to follow in 2005/06. I intend to deal in more detail during the course of the Debate with the police, defence and prisons services for which I am responsible, My colleague Ministers will undoubtedly wish to deal in detail with the matters for which they are responsible.

The 2005/06 Budget, like all of the Budgets introduced by this Government, is intended to create the conditions whereby

Bahamians of all social classes can enjoy a reasonable, secure and happy standard of living, whereby families and persons in crisis can receive suitable assistance to ease their pain and their problems, and where everyone participates in the quality which we can all have. In this regard, I wish to once again refer to the importance which the Government attaches to Urban Renewal as is evident in the commitment of additional resources in 2005/06 and the creation of the new Department. I wish at this point to pay tribute to all involved in the urban renewal project, and to the many businesses and church and

other voluntary organizations who are supporting the project.

I believe that I am speaking for the Rt. Hon. Prime Minister and my colleagues in Government when I say that in our capacity as Ministers, we endeavour to meet the criterion of good governance which the Seventeenth Century poet John Milton stated as follows:-

“..when complaints are freely heard, deeply considered, and speedily reformed, then is the utmost of civil liberty attained.”

I am deeply grateful to the Almighty in enabling me to deliver this Communication

and I pray that He will soon restore the Prime Minister to us.

With that, Mr. Speaker, I have the honour to commend the 2005/06 Budget to the deliberations of this Honourable House.

ECONOMIC BACKGROUND

INTRODUCTION

1. It is estimated by the Department of Statistics that the economy grew by 3.0% in real terms ¹(4.2% in current prices) in 2004. In 2005 the economy is projected to grow by about 3.5% in real terms (about 5.4% in current prices) arising from actual and expected capital investment inflows, and this should result in a further decrease in the rate of unemployment. Trends in the international environment remain generally supportive of the outlook with an expected strengthening in tourism and foreign investment activity. The Bahamas should continue to experience mild inflation, however with some increased pressures from the elevated and uncertain international trend in oil prices. Domestic financial sector developments and policies remain supportive of orderly development of the economy.

2. In examining recent developments and prospects for the Bahamian economy this analysis first reviews the elements of the international economic environment which have the most direct impact on domestic trends. This is followed by an analysis of the domestic environment, including policies and trends affecting the financial sector.

INTERNATIONAL ECONOMIC DEVELOPMENTS

3. In its April 2005 World Economic Outlook the IMF, estimated that despite some retrenchment in industrial production and a slowdown in world trade, the pace of global output expansion increased to 5.1% 2004 from 4% in 2003. With the outlook more broadly improved, world growth is expected to level off at 4.3% in 2005 and at 4.4% in 2006.

4. The US economy is projected to continue to grow by about 3.6% in real terms in 2005, and the global economic outlook continues to improve. The accelerated level of growth during 2004 generated increased domestic price pressures. As a result, the Federal Reserve began to gradually tighten interest rates, and this process is expected to continue during 2005. The interest rate increases, alongside higher energy costs are expected to result in more stable annual growth,

¹ Unless otherwise stated, in the Analysis the figures for growth in GDP are expressed in real terms

projected at 3.6% in 2006, compared to the exceptional level of 4.4% in 2004. Expectations of rising interest have slowed the rate of depreciation in the US dollar during 2004. However the dollar is expected to remain weak relative against the Euro and other major currencies, as financial markets respond negatively to the record federal budget and trade deficits in the US, which are expected to persist over the medium term. On the positive side, the depreciation of the US \$ vis-à-vis other major currencies should maintain a significant competitive advantage for The Bahamas' tourism product relative to destinations such as European destinations whose currencies appreciate against the US\$.

5. There may be moderate easing of geopolitical tensions and reduced terrorism concerns among the traveling public and the general restoration of business and consumer confidence. However, as is pointed out in the communiqué from the recent meeting of Finance Ministers of the major countries on the IMF's International Monetary and Financial Committee, the major economies still face significant challenges from high energy costs, with resulting increased inflation expectations, which could exert a drag on private sector growth. However, although higher energy costs are expected to persist over the medium term these have already been factored into the positive projections for the global economy.

DOMESTIC ECONOMIC DEVELOPMENTS

6. As stated above, the Department of Statistics estimates that during 2004, growth in the Bahamian economy strengthened to 3.0%, compared with 1.9% in 2003 and 1.4% in 2002. The acceleration arose primarily from modest annual increases in real private sector consumption, steady growth in Government expenditures and a healthy pickup in business and residential investments. As the economy recovers from hurricanes Frances and Jeanne, tourism and foreign investment inflows strengthened. Accordingly, growth of 3.5% is projected during 2005 and to stabilize at about that level in the medium term. As a result, the average unemployment rate should continue to fall.

TOURISM

7. There was some disruption to tourism primarily in Grand Bahama because of the hurricanes. However, the impact was felt after the more profitable first half of the visitor season and the hotel infrastructure in New Providence were spared significant damage. The recovery and reconstruction of damaged infrastructure and facilities in Grand

Bahama and the Family Island is proceeding urgently.

8. With the United States providing a majority of the visitors, total arrivals rose by 8.9% to a record 5 million in 2004, as compared with gains of 4.3% and 5.3% in 2002. Air arrivals, which include stopover activity, increased by 1.5% to 1.5 million visitors. Sea arrivals, reflecting the continued robustness of the cruise sector, rose by 12.3% to 3.6 million.

9. The growth in cruise visitors plus the pricing gains and room room night sales in stopovers boosted tourism earnings by an estimated 4% to over \$1.8 Billion in 2004. As regards hotel sector performance, the Ministry of Tourism's survey of large properties, indicates that room revenues recovered by 3.4% last year following a 6.1% decline in 2003. In particular occupied room nights among these properties rose by 1.7% and the average nightly room rate rose by 1.7% to just over \$151.

10. There were however distinct differences in tourism's contribution among the major destinations of the Bahamas. Both stopover and cruise activity strengthened in New Providence. While the disruption from the severe damage to the hotel properties resulted in decreased industry earnings for Grand Bahama, the Family Islands still recorded some increase in total sector earnings owing to the contributions from increased stopover capacity in islands like Exuma which escaped major damage.

11. Data for the first quarter of 2005, indicate that tourism is continuing to expand, characterized, in the stopover sector, by robust pricing and hotel room occupancy levels, particularly for New Providence. In the Family Islands, the evidence suggest a completed recovery from capacity and other setbacks during September to December 2004; however seasonal activity in the Grand Bahama hotel sector was still depressed.

12. The outlook for tourism remains positive for the medium-term, and has taken on more certainty since 2004, as external factors, including the weak US \$ are supporting stronger visitor demand. Moreover, increased external confidence in the sector is resulting in major inflows of foreign investments into resort developments; these inflows are supporting significant upgrade and expansion in capacity. In line with the increased inflows into the tourism sector, The Bahamas is experiencing a steady increase in direct airlift, including low fare-carriers from North America; furthermore, it is expected that by the summer of 2005 there will be increases in airlift from Europe. The Government is also giving priority to the upgrade of key ports of entry

in New Province and the Family Island, ensuring that comprehensive attention is given to infrastructure needs.

FINANCIAL SECTOR

13. The financial services sector provides important employment benefits to Bahamians in the domestic and international financial services and related professional sectors. The domestic financial sector is vital for also ensuring an orderly and sustainable intermediation of domestic financial savings.

14. As to employment and structural trends, indications are that conditions were stable to moderately improved during 2005. The banking sector continued to adjust to the Central Bank's physical presence requirements with a further number of institutions deciding to windup operations that were being managed through local agents. This and the ongoing consolidation of some operations resulted in a further reduction in the number of banks and trust companies licensed to operate from or within the Bahamas to 266 in 2004, from 284 in 2003 and 284 in 2002. As at the end March 2005 the number of licenses had decreased further to 262. However, total employment among banks, which corresponds more to physical presence, increased during 2004 to more than 4,300, and banks' total expenditures in the economy rose above \$400 million.

15. The insurance industry's contribution is more concentrated in the domestic sector. There was an increase in the number of domestic companies and agents to 132 in 2004 from 127 in 2003, and in the number of external insurers to 29 from 26. Based on the Central Bank's survey, average salaries among local insurance operations are within the \$40,000 to \$45,000 range. Indications are that there was no net loss of employment in 2004.

16. The 19 registered credit unions continued to experience strong Balance Sheet growth, providing stable employment for 105 persons during 2004. Although offering competitive compensation packages relative to the rest of the financial sector, average salary expenses per worker are significantly lower, as a result a of a considerable number of part-time jobs in the sector.

17. In the securities industry, prospects also improved during 2004, with total value of assets under management remaining above the \$100 Billion level for the second consecutive year. However, employment decreased, owing to the relocation of an important operation outside of this jurisdiction. Indications are also that, although average employee compensations are still the most attractive in the financial services

sector, these softened during 2005, owing to a reduction in the share of non-Bahamians in the workforce.

CONSTRUCTION

18. Comprehensive data on construction, as compiled from building permits and the Ministry of Work's monitoring of building starts and completion, are not yet available for 2004. However, the sector is expected to show strengthening relative to 2003, given the increased support from foreign investments and the steady financing of domestic housing developments. Arising from the impact of the investment inflows and other factors, the outlook for the sector is distinctly positive.

19. In the domestic sector, total mortgage commitments for new construction and repairs to existing structures rose by 27.9% to 1,175 during 2004, with the corresponding value higher by 43.2% to \$130.9 million. Some 95% of these approvals and the corresponding strengthening were attributed to residential loan approvals. On the residential side mortgage disbursement, which also included financing of non-construction activities, increased by 4.3% to \$299.3 million and commercial loan disbursements nearly doubled to \$25.4 million. In line with disbursements, growth in total outstanding mortgages strengthened by 11.2% to \$1,863.4 million in 2004, with residential claims accounting for 91.3% of the total. The average interest rate on local residential mortgages decreased during the year to 8.8% from 9.0% in 2003, and was stable for commercial loans at 9.6%.

AGRICULTURE AND FISHERIES

20. Indications are that both agriculture and fisheries production decreased during 2004, mainly as a result of the hurricanes. The agricultural sector also suffered a set back from the outbreak of citrus canker in Abaco. However, production and export estimates were only available for fisheries activity. These indicate that, for the first half of 2004, the most recent period for which data on fisheries landings were available, the total domestic catch decreased in volume by 5.5% and value by 10.2%. For the year, earnings from fisheries exports declined by 16.9% to \$90.4 million, with crawfish shipments, which accounted for 97.5% of receipts, decreased by 17.0% to \$88.2 million.

INFLATION

21. The Bahamas experienced modest consumer price inflation during 2004. Although higher energy costs continued to be experienced, these exerted more of their initial effect on domestic prices in 2003. Since

the beginning of 2005, however, households have experienced some re-intensification of these pressures, particularly in electricity costs and gasoline.

22. With a marginal decrease in average housing costs (0.1%), the most heavily weighted component of the Retail Price Index, average consumer price inflation in The Bahamas declined to 0.9% in 2004, from 3.0% in 2003. Some average cost decline was also estimated for recreation & entertainment services, while the average price increase also declined for furniture & household items and for medical care & health.

FOREIGN INVESTMENT AND THE BALANCE OF PAYMENTS

23. The Bahamas has entered another strong cycle of foreign investment, with a more balanced distribution of attention throughout The Bahamas. In the short-term, job creation prospects for the construction sector are considerable, with both the Atlantis Phase III and the BahaMar Cable Beach redevelopment likely to stretch the sector's capacity. Foreign exchange inflows will also be boosted during the construction phase, as it is estimated that about one-third of the costs associated with large scale projects directly impact the economy, either through wages or other payments to local contractors and suppliers.

24. The Central Bank's balance of payments estimates indicate that during 2004, net private foreign investment inflows to The Bahamas rose considerably to \$430.5 million from \$313.3 million in 2003. The majority of the net flow, some \$346.5 million compared to \$229 million in 2003 were channeled into productive enterprises. The remaining \$84 million in net inflows funded net real estate purchases, mainly in the second homes market.

25. As a result of these increased foreign inflows, and increased local consumption and housing investments, there was a widening in the merchandise trade deficit to \$ 1.34 Billion in 2004. The Current Account Deficit, which is more broadly defined to take account of the trade balance and net earning from services such as tourism, and which normally also increases under these conditions, was instead reduced during 2004. This was due to the significant inflows from re-insurance claims settlement to the Bahamas following the hurricanes, conservatively estimated at about \$200million. Over the next few years, as investments remain at a high level, the Current Account Deficit is expected to increase in both absolute terms and as a percentage of GDP.

CAPITAL MARKETS

26. The improvement in the economy contributed to an increase in investor confidence and activity in the domestic capital markets. The volume of securities traded on the Bahamas International Securities Exchange (BISX) nearly doubled to 8 million shares during 2004, with the value significantly higher at \$24.3 million from \$7.5 million in 2003. The BISX All Share Price Index appreciated by 19.7% to 1,039.4 points, a marked rebound from the narrowed decline of 2.0% in 2003. Similarly, valuations represented in the broader Fidelity Capital Market Index (Findex), which captures over-the-counter trading, recovered by 14.9% to 423 points, from a loss of 0.6% in the previous year. Total market capitalization on BISX rose by 17.2% to \$1.9 Billion, and was inclusive of the Kerzner International Bahamian Dollar Depository Receipts (BDRs) sold to the public during July 2004.

27. A number of important initiatives are being considered to accelerate the development of the local capital markets. One of these is the eventual inclusion of Government debt securities among instruments issued and openly traded in the capital markets, provided that this does not increase the cost of Government debt financing, and this would establish a benchmark for the pricing and issuance of private debt securities. Consideration is also being given to measures to ensure the self-sustaining operating viability of BISX. Finally, consideration is being given to the further gradual liberalization of Exchange Controls, including those on certain portfolio investments.

PAYMENTS SYSTEM MODERNIZATION

28. Modernization of the payments system is vital to ensuring that commercial transactions in the domestic economy are settled as efficiently as possible and that full advantage is taken of modern technology to facilitate commerce. Led by the Central Bank, The Bahamas payments system modernization initiative reached an important milestone in May 2004 with the start up of the Bahamas Interbank Settlement System (BISS), for real time gross payments settlements (RTGS) among the clearing banks and the Central Bank. This infrastructure is also accommodating large value payments processed on behalf of banks' clients and the public sector.

29. The final phase of the payments systems modernization initiative, the establishment of the Automated Clearing House, is on schedule for completion during the second half of 2005. The ACH infrastructure will facilitate settlement of low value retail payments (less than \$50,000), and is expected to speed up the development of domestic electronic commerce by accommodating the settlement of non-cash

transactions that are denominated in Bahamian dollars. As the two largest originators of small-value payments it is expected that the Government and the National Insurance Board will be the largest users of the ACH network.

MONEY AND CREDIT DEVELOPMENTS

30. Domestic monetary and credit trends evolved along a strongly sustainable path during 2004. Enhanced foreign currency inflows supported accelerated growth in bank deposits and were more than adequate to fund domestic credit growth. These inflows therefore still permitted a substantial buildup in external reserves and bank liquidity.

31. Although the credit restraint policy imposed by the Central Bank in 2001 remained in place until August 2004, it was evident that the first half buildup in external reserves and liquidity were reflected in steady strengthening in the real sectors of the economy. The Central Bank however, timed the relaxation of its credit policies with indications that asset quality in the local banking system was improving, as evidenced from a gradual decline in the share of bank loans to the private sector that were encountering repayment difficulties. While banks have been permitted to resume growth in their private sector loans, they are required to do so within prudential parameters established by the Central Bank in August 2004, which mandate a minimum equity contribution of 15% from borrowers towards most new personal loans granted, and which limit the resulting total debt service ratio from loans taken on, to a range of 40% to 45% of ordinary monthly income.

32. Most of the expansion in credit during 2004 occurred prior to the relaxation of the lending restriction, with the timing of the hurricanes slowing the lending enthusiasm during the last four months of 2004. Growth in bank credit to the private sector firmed to \$244 million or 6.8% in 2004 from \$ 250 million or 0.6% in 2003. Although residential mortgages continued to attract a large share of the net lending, flows for consumer purposes also rebounded during 2004. These trends continued during the first quarter of 2005, now also incorporating resumed emphasis on lending for businesses activities.

33. As economic conditions, and the outlook for external reserves and bank liquidity continued to improve, in February, 2005, the Central Bank reduced the Discount Rate by 0.5 % to 5.0% and, a day later, commercial banks reduced the Prime Lending Rate by a similar amount to 5.50%. This latter reduction benefits existing loans with interest rates linked to Prime, such as mortgages and businesses facilities, and permits all new facilities including consumer loans to benefit from

lower rates. The Government also benefits because the interest paid on the bulk of its B \$ debt (including Registered Stocks) is linked to Prime. Lower interest rates are expected to stimulate increased borrowing and domestic spending, by qualifying more marginal borrowers to meet the repayment requirements for loans. For households with existing mortgages, the interest savings also free up financial resources that can be used for other activities.

34. The record accumulation in external reserves continues during 2005 but at a slower pace than in 2004. During 2004, reserves increased by 37.9% to \$667.8 million by end December, and were equivalent to 21.7 weeks of non-oil import cover, compared to 16.6 weeks at the end of 2003. During the first quarter of 2005 balances experienced seasonal growth to \$718.6 million at end-March, attesting to continued support from private sector foreign currency inflows. In addition, the net proceeds to the Government and Hotel Corporation of The Bahamas from the sale of the Cable Beach properties further boosted balances to nearly \$800 million as of mid-May, 2005.

NATIONAL DEBT

35. The increase in Public Sector Debt slowed during 2004. Growth in the Government's Direct Debt was \$161.3 million or 8.3% to \$2,101.0 million in 2004. The increase in the National Debt, which takes into consideration the Government Guaranteed borrowings of the Public Corporations, was also slowed to \$ 130.7 million or 5.1% for a stock of \$2,533.3 million. During 2003, the National Debt rose by 8.8%.

36. The total foreign currency debt of the Government and Public Corporations is closely monitored by international observers, as on the repayment side it represents a required use of foreign exchange earnings. Growth in the debt is justified, if it supports increases in the productive capacity within the economy, and if the servicing burden from principal repayment and interest costs does not unduly constrain the economy's access to foreign exchange for other beneficial purposes. Both as a percentage of GDP and relative to the share of export earnings used for debt servicing, the Bahamas continues to have a relatively low foreign currency debt burden. During 2004 the growth in the public sectors' foreign currency debt decreased by \$40.4 million or 6.8% for an end-December stock of \$557.5 million. This compared to an increase of just in excess of this amount in 2003. The amount of the foreign currency debt owed by Government decreased marginally to \$287.6 million, while the Public Corporations' liabilities fell to \$269.9 million from \$305.8 million. The debt service as percentage of exports of services decreased slightly to 3.6% in 2004, and is expected to decrease

further in 2005 as foreign exchange earnings grow.

ECONOMIC OUTLOOK

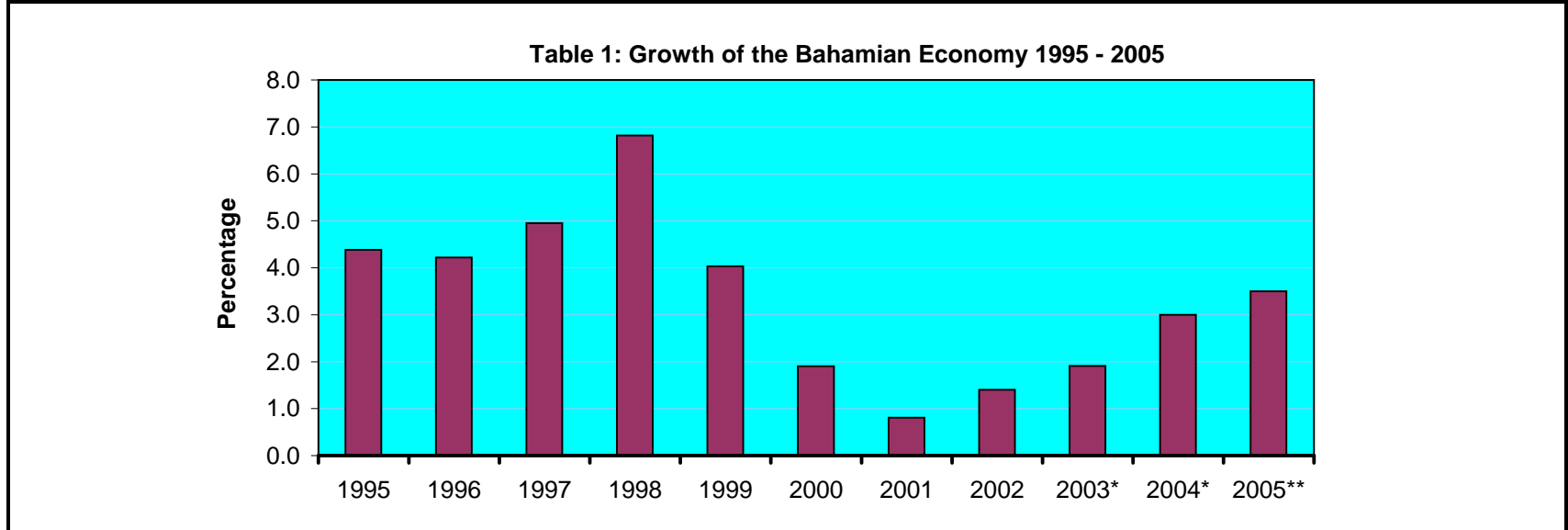
37. Growth in the Bahamian economy is expected to strengthen during 2005 and to remain robust over the medium term. While tourism continues to be main force propelling the expansion, the foreign investment inflows are expected to significantly impact the construction sector in the short-term. Over the medium term the new tourism and related facilities will provide an important boost in tourism sector capacity and permanent jobs, and will more evenly distributed throughout the islands of the Bahamas as a result of Government policy in this regard. With other sectors of the economy also expected to record stable to increased output, this should will sustain a favourable climate for the evolution of the public sector's finances.

38. However, there are the usual downside risks, because the openness of the Bahamian economy means that it is inherently vulnerable to negative external shocks. Furthermore, the tourism and infrastructural capital stock is exposed to potential hurricane damage that could severely disrupt foreign exchange earnings. In that regard, the intention of the Government to have in place an organizational structure capable of mobilizing at the highest levels of efficiency to deal with disaster recovery is of crucial importance. At the macro-economic level, domestic monetary and fiscal policies will maintain a medium to long-term perspective of increasing the diversity and resilience of the economy, and ensuring that increased priority is given to savings and investments including containing fiscal deficits.

Table I. Growth of the Bahamian Economy 1995 - 2005

	1995	1996	1997	1998	1999	2000	2001	2002	2003*	2004*	2005**
GDP(Current Prices) (\$Millions)	3429	3609	3842	4283	4704	5004	5131	5400	5502	5735	6043
Growth-Current Prices(%)	5.2	5.3	6.4	11.5	9.8	6.4	2.6	5.2	1.9	4.2	5.4
Growth-Constant Prices(%)	4.4	4.2	5.0	6.8	4.0	1.9	0.8	1.4	1.9	3.0	3.5
Consumer Price Index (%)	2.1	1.4	0.5	1.3 (a)	1.3 (a)	1.6(a)	2.0	2.2(a)	3.0(b)	0.9	1.8

Source: Department of Statistics
(a) GDP deflator is higher in those years
(b) GDP deflator is lower in those years
* Department of Statistics preliminary or provisional estimates
** IMF Projections



**Table II - Budget Performance
\$millions**

	1996/97	1997/98	1998/99	1999/00	2000/01	2001/02	2002/03	2003/04	2004/05 Budget	2004/05 Projected Outturn	2005/06 Budget
1. Recurrent Expenditure	778	808	837	866	930	986	1035	1091	1175	1150	1214
2. Recurrent Revenue	698	780	822	943	973	875	918	959	1052	1030	1145
3. Recurrent Deficit (1 minus 2)	80	28	15	83	43	111	117	132	123	120	69
4. Capital Expenditure	140	117	124	139	133	138	127	116	148	130	165
5. Capital Revenue	3	1	0	0	1	0	0	0	11	11	7
6. Capital Deficit (4 minus 5)	137	116	124	139	132	138	127	116	137	119	158
7. TOTAL DEFICIT (3 plus 6)	217	144	139	56	89	249	244	248	260	239	227
8. Debt Redemption	84	79	74	41	75	85	60	85	97	97	55
9. GFS Deficit (7 minus 8)	133	65	65	15	14	164	184	163	163	142	172
10. GDP (current prices)	3726	4062	4493	4854	5068	5266	5451	5618	5889	5889	6208
11. GFS Deficit as % of GDP	3.6	1.6	1.4	0.3	0.3	3.1	3.4	2.9	2.8	2.4	2.8

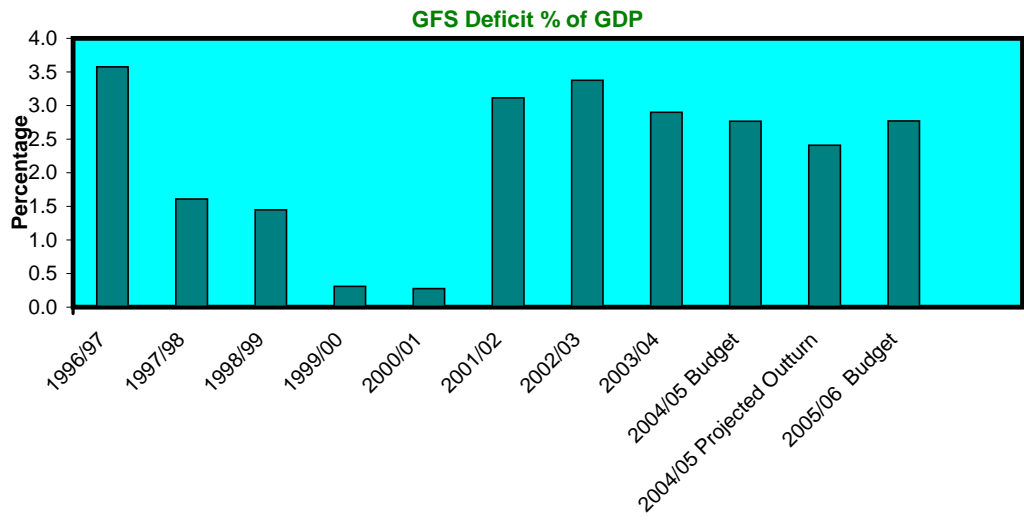
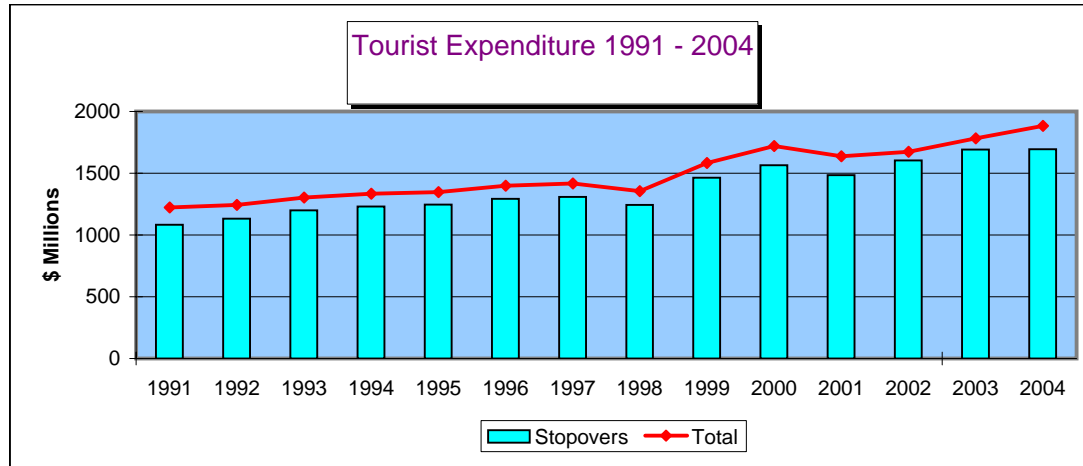
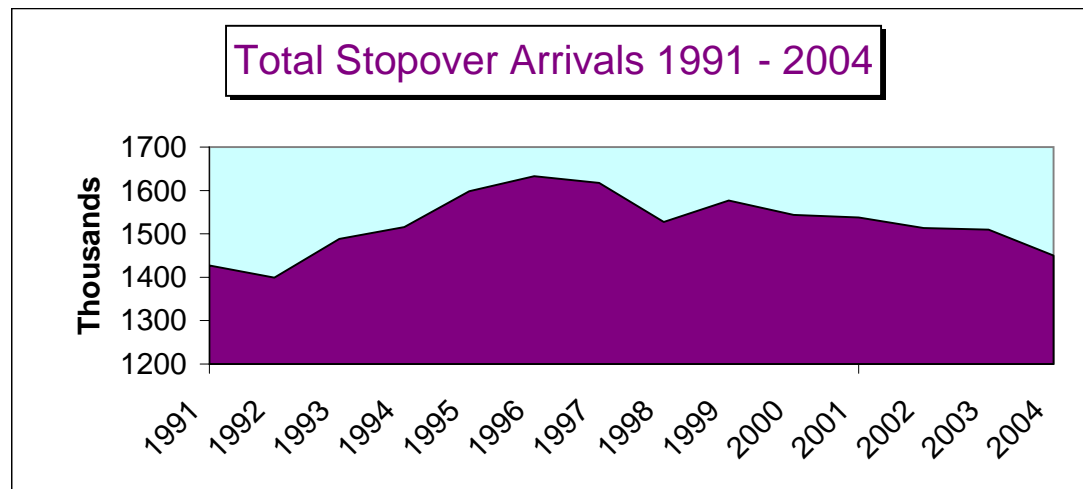


Table III. Tourist Expenditure and Arrivals 1991 - 2003

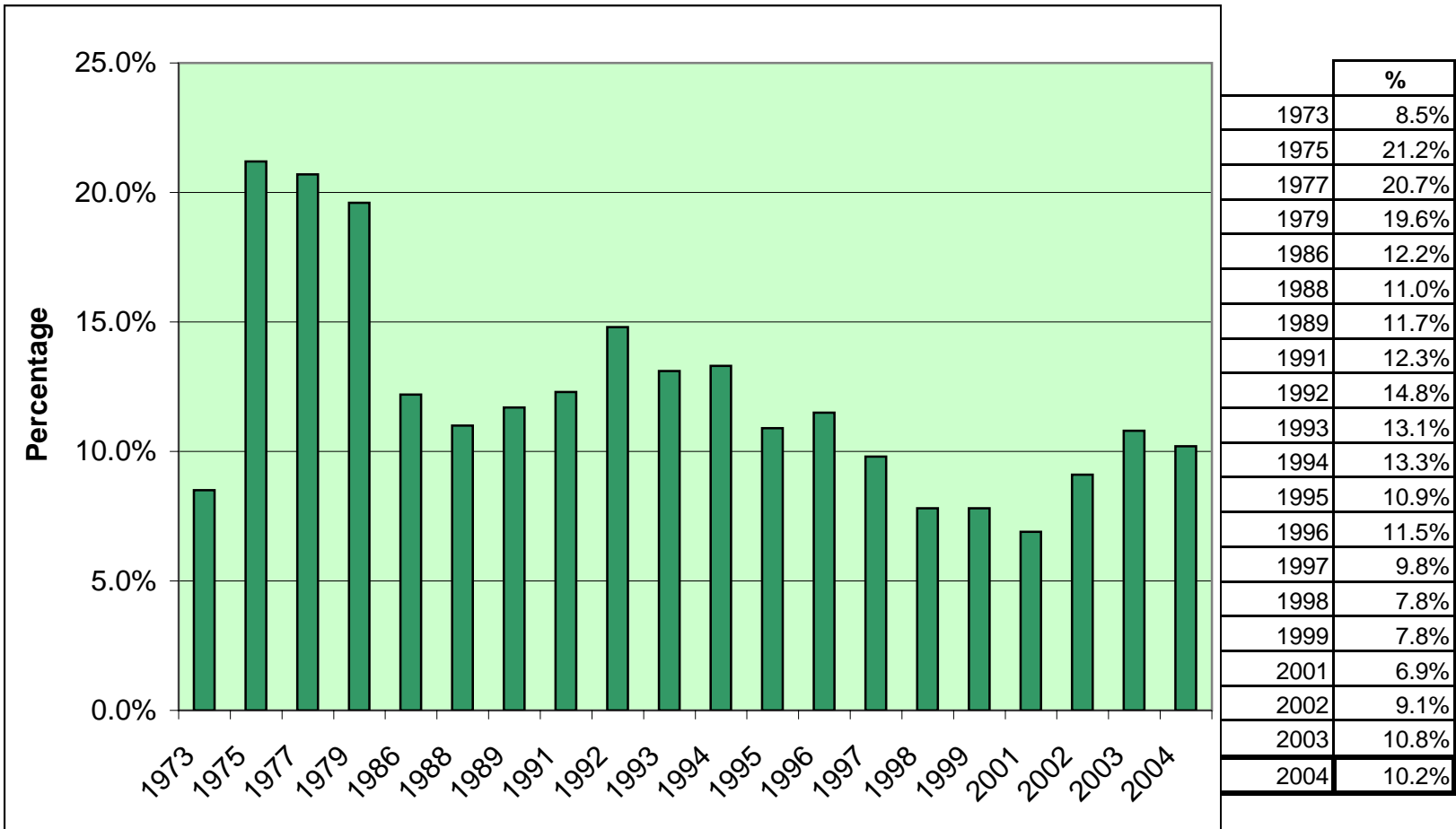


*Source: Central Bank and Ministry of Tourism



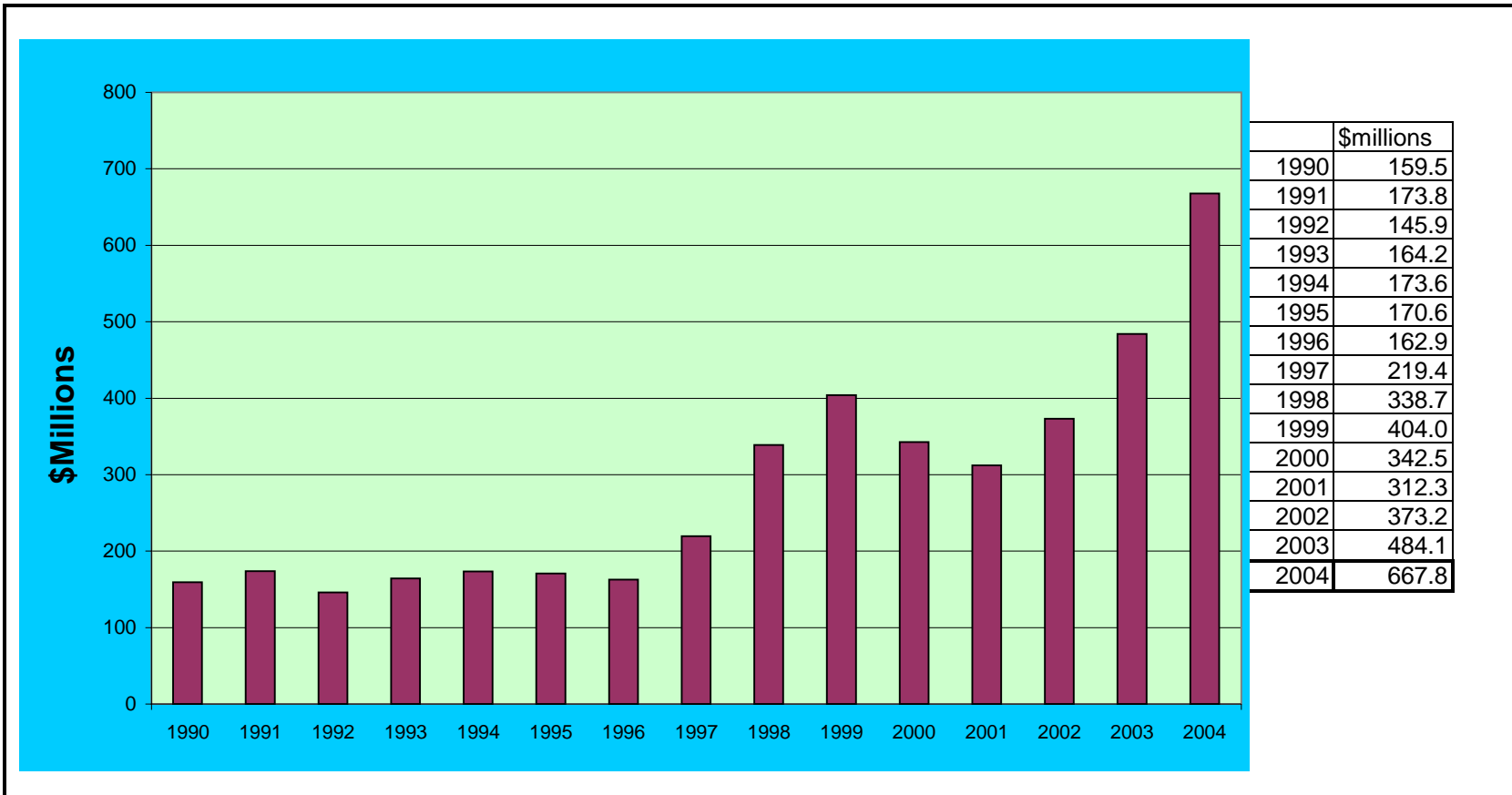
*Source: Central Bank and Ministry of Tourism

Table IV. Unemployment Rates 1973-2004



Source: Department of Statistics

Table V Total External Reserves 1990 - 2004



Source: Central Bank Quarterly Statistical Digest, February 2005

Table VI. National Debt

\$ millions	1996	1997	1998	1999	2000	2001	2002	2003	2004
(1) Direct Charge	1,235	1,377	1,431	1,513	1,514	1,604	1,807	1,940	2,100
(2) Government Guaranteed Debt	314	332	349	374	365	359	399	461	422
(3) National Debt(1+2)	1,549	1,708	1,780	1,887	1,879	1,963	2,206	2,401	2,522
GDP(\$millions)	3609	3842	4283	4704	5004	5131	5400	5502	5735
As % of GDP									
(1) Direct Charge	34%	36%	33%	32%	30%	31%	33%	35%	37%
(2) Government Guaranteed Debt	9%	9%	8%	8%	7%	7%	7%	8%	7%
(3) National Debt(1+2)	43%	44%	42%	40%	38%	38%	41%	44%	44%

National Debt

Legend: (1) Direct Charge, (2) Government Guaranteed Debt, (3) National Debt(1+2)

As % of GDP

Legend: (1) Direct Charge, (2) Government Guaranteed Debt, (3) National Debt(1+2)

Source: Central Bank Quarterly Statistical Digest February 2005

Table VII. Growth of the Bahamian and US Economies 1996 - 2005

Annual percent change in real terms

	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005*
Bahamas	4.2	5.0	6.8	4.0	1.9	0.8	1.4	1.9	3.0	3.5
United States	3.7	4.5	4.2	4.4	3.7	0.8	1.9	3.0	4.4	3.6

Source: US - IMF World Economic Outlook, April 2005

Bahamas - Department of Statistics

* IMF Projections

Table VII Growth of the Bahamian and US Economies 1996 - 2005

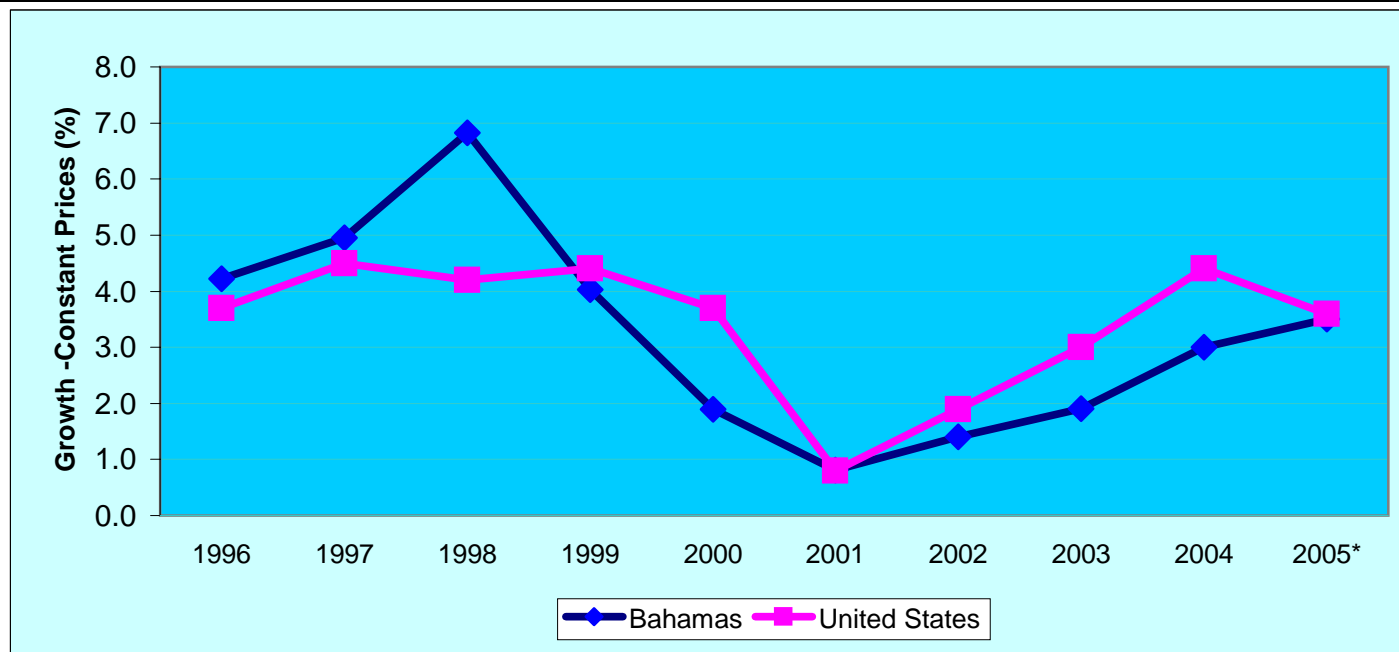


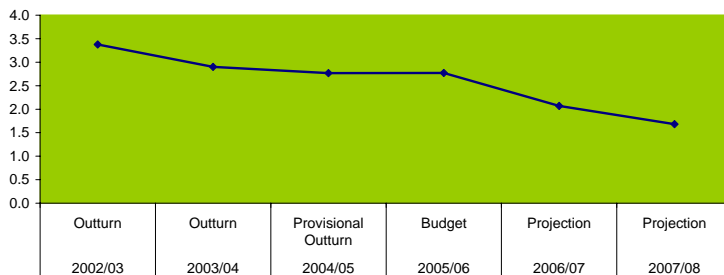
TABLE VIII

BUDGET PROJECTIONS 2006/07 AND 2007/08

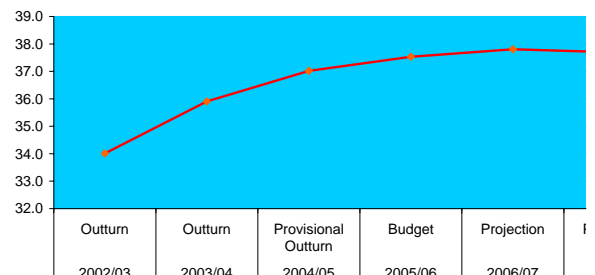
\$ million

	2002/03 Outturn	2003/04 Outturn	2004/05 Provisional Outturn	2005/06 Budget	2006/07 Projection
	(1)	(2)	(3)	(4)	(5)
1. RECURRENT EXPENDITURE	1035	1091	1175	1214	1280
2. RECURRENT REVENUE	918	959	1052	1145	1220
3. RECURRENT DEFICIT (1.minus 2.)	117	132	123	69	60
4. CAPITAL EXPENDITURE	127	116	148	165	165
5. CAPITAL REVENUE	0	0	11	7	0
6. CAPITAL DEFICIT (4. minus 5.)	127	116	137	158	165
7. TOTAL DEFICIT (3. plus 6.)	244	248	260	227	225
8. DEBT REDEMPTION	60	85	97	55	90
9. GFS DEFICIT (7. minus 8.)	184	163	163	172	135
10. GDP (current prices)	5451	5618	5889	6208	6520
11. GFS DEFICIT as % of GDP	3.4	2.9	2.8	2.8	2.1
12. Government Debt as % of GDP	34.0	35.9	37.0	37.5	37.8
13 Government Debt - end-June FY \$ million	1854	2017	2180	2330	2465
14. Ratio of Recurrent Revenue to GDP %	16.8	17.1	17.9	18.4	18.7

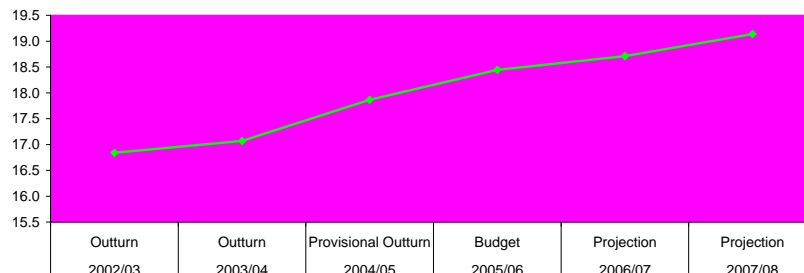
GFS Deficit as % of GDP



Government Debt as % of GDP



Ratio of Recurrent Revenue to GDP



Notes on Multi-annual Projections

1. *The purpose of these Multi-annual Projections is to provide a ‘snap-shot’ of the evolution of the public finances over the next 2 to 3 years based on the continuation of existing policies and on assumptions about the macroeconomic environment. The Projections are not intended as the ‘vision’ of the evolution of the public finances nor as immutable commitments, for the reasons set out in the following paragraphs.*

2. *The Government of The Bahamas targets the following three key closely related fiscal indicators:-*

- *The “GFS Deficit” (basically the difference between total government expenditure, excluding debt redemption, and total revenue, excluding borrowing), as an approximation of the addition which the Budget makes to Government Debt.*
- *The ratio of Government Revenue to GDP because it is below the level of 20% which is deemed the minimum level necessary to finance the current level of Government services.*
- *The level of Government Debt prior to, and after the Budget. Government policy is to place an absolute ceiling of 40% on the ratio of Government Debt to GDP, and as far as possible to reduce the level to about 30% of GDP.*

3. *Targeting these indicators has enabled the Bahamian economy to remain stable and meet economic and social challenges arising from such events as the 1990 Gulf Crisis, the slowdown in the global economy in 2000, the terrorism attacks of 11 September, 2001, and the current generally unsettled external environment.*

4. *In view of the openness of the Bahamian economy with corresponding sensitivity of the government revenue base to external macroeconomic developments, government policy is to maintain as much flexibility in expenditure commitments as is consistent with careful planning of major expenditures. Thus, all major projects and expenditures are carefully monitored and new commitments are only brought forward either in response to requirements to complement and induce major private sector investment inflows, or as major existing projects are completed. (High levels of productive private sector investment are the major dynamo of growth in the Bahamian economy.) The public sector investment programme is, therefore, the corpus of*

ongoing government investment expenditure with new or additional projects introduced as scope arises.

5. The projections assume GDP growth in current prices of 5% in each year. The projections also assume that Recurrent Revenue will grow in 2006/07 and 2007/08 by about 7.5% because of the increased buoyancy arising from the investment inflow and the coming on stream of the revenue administration enhancement measures. Recurrent Expenditure is assumed to grow incrementally as in the recent past. Finally, Capital Expenditure is assumed to basically plateau. No provision is made in the calculations for the privatization of BTC and Bahamasair; in the case of BTC, privatization would provide a capital inflow which would enable reduction in the ratio of Government Debt to GDP; in the case of Bahamasair, privatization could result in a significant reduction in the considerable capital transfers made in the budget to Bahamasair thereby reducing the GFS Deficits (and the resulting Government debt to GDP ratio).

6. However, as stated, the main purpose of the projections is illustrative and a different 'mix' of assumptions would, of course, produce different results.

**Ministry of Finance
May, 2005**

Table IX

EXPENDITURE ON THE GROSS DOMESTIC PRODUCT
at Current Market Prices

		(B\$ millions)							
Line	Item	1989F	1990F	1991F	1992F	1993F	1994F	1995F	1996F
1	Government final consumption expenditure	415.27	407.12	440.58	427.27	397.99	482.68	476.20	516.87
1.1	Collective Consumption Expenditure	248.35	243.60	267.31	251.11	232.02	298.77	286.42	323.53
1.2	Individual Consumption Expenditure	166.91	163.52	173.27	176.16	165.97	183.91	189.78	193.35
2	Private final consumption expenditure	1914.52	1989.06	2051.09	2008.33	2061.84	2131.06	2333.91	2513.24
3	Gross capital formation	964.52	931.27	913.33	866.21	721.66	842.80	948.29	1100.52
3.1	Change in stocks	86.62	119.90	122.75	53.81	62.04	54.85	76.00	101.35
3.2	Gross fixed capital formation	877.90	811.37	790.59	812.40	659.62	787.95	872.29	999.17
3.2.1	Residential construction	166.52	158.59	151.04	153.85	110.40	124.32	124.01	156.13
3.2.2	Other construction	294.08	278.52	265.01	271.44	236.74	283.94	234.98	224.50
3.2.3	Machinery/equipment	417.30	374.26	374.54	387.11	312.48	379.69	513.31	618.54
4	Exports of goods and services	1648.32	1714.73	1585.17	1562.18	1606.81	1662.79	1699.04	1733.68
5	Less: Imports of goods and services	1750.51	1771.67	1716.35	1592.26	1589.08	1739.67	1883.08	2086.69
6	Expenditure on GDP - before Staistical Discrepancy	3192.11	3270.51	3273.83	3271.74	3199.23	3379.66	3574.37	3777.62
7	Statistical Discrepancy	-129.63	-104.81	-162.67	-162.58	-107.37	-120.98	-145.01	-168.21
8	EXPENDITURE ON GROSS DOMESTIC PRODUCT	3062.48	3165.71	3111.16	3109.16	3091.86	3258.67	3429.36	3609.40
	GDP NOMINAL GROWTH RATE		3.37	-1.72	-0.06	-0.56	5.40	5.24	5.25
	F: Final								
	R: Revised								

Source: Department of Statistics

Table IX (continued)

EXPENDITURE ON THE GROSS DOMESTIC PRODUCT
at Current Market Prices

		(B\$ millions)							
Line	Item	1997F	1998F	1999F	2000F	2001F	2002F	2003R	2004PL
1	Government final consumption expenditure	578.48	592.40	642.26	680.38	730.40	770.39	785.00	810.50
1.1	Collective Consumption Expenditure	359.33	360.88	405.03	416.44	444.17	480.62	488.70	505.11
1.2	Individual Consumption Expenditure	219.15	231.52	237.23	263.94	286.22	289.76	296.30	305.39
2	Private final consumption expenditure	2673.78	3016.15	3253.98	3359.76	3621.04	3589.36	3763.83	3991.20
3	Gross capital formation	1418.67	1708.03	1698.88	1929.99	1779.94	1682.72	1732.45	1848.03
3.1	Change in stocks	144.50	207.13	153.75	200.67	176.23	136.57	142.38	166.49
3.2	Gross fixed capital formation	1274.17	1500.91	1545.13	1729.32	1603.72	1546.15	1590.07	1681.54
3.2.1	Residential construction	197.48	278.02	198.15	242.97	229.33	276.90	344.26	349.29
3.2.2	Other construction	315.93	412.35	521.61	544.41	506.55	521.43	438.92	460.17
3.2.3	Machinery/equipment	760.77	810.54	825.36	941.93	867.83	747.83	806.90	872.07
4	Exports of goods and services	1750.23	1793.52	2130.81	2361.09	2163.49	2370.74	2322.14	2471.44
5	Less: Imports of goods and services	2491.44	2699.86	2826.52	3172.13	3000.44	2862.67	2981.26	3290.94
6	Expenditure on GDP - before Staistical Discrepancy	3929.72	4410.25	4899.41	5159.09	5294.43	5550.54	5622.16	5830.23
7	Statistical Discrepancy	-88.23	-127.59	-195.21	-155.39	-162.98	-150.47	-119.96	-95.63
8	EXPENDITURE ON GROSS DOMESTIC PRODUCT	3841.50	4282.66	4704.19	5003.70	5131.45	5400.06	5502.20	5734.60
	GDP NOMINAL GROWTH RATE	6.43	11.48	9.84	6.37	2.55	5.23	1.89	4.22
	F: Final								
	R: Revised								
	PL: Preliminary								

Source: Department of Statistics

Table X - Ratio of Recurrent Revenue to GDP
\$millions

	1996/97	1997/98	1998/99	1999/00	2000/01	2001/02	2002/03	2003/04	2004/05 Budget	2004/05 Projected Outturn	2005/06 Budget
Recurrent Revenue	698	780	822	943	973	875	918	959	1052	1030	1145
GDP (current prices)	3726	4062	4493	4854	5068	5266	5451	5618	5889	5889	6208
Recurrent Revenue % of GDP	18.7%	19.2%	18.3%	19.4%	19.2%	16.6%	16.8%	17.1%	17.9%	17.5%	18.4%

Recurrent Revenue as % of GDP

