

2006/07 BUDGET

COMMUNICATION

Mr. Speaker:

**I have the honour to present the 2006/07
Budget Communication.**

INTRODUCTION

**Before entering office in May, 2002, my
Party worked hard to earn the trust of the
Bahamian people. Since May, 2002, my
Government has remained true to its principles
and commitments. We have worked tirelessly to
prove ourselves worthy of the trust reposed in us
by the people of our country. Our dedication to
the interests of the Bahamian people is there for
all to see. Our achievements include the
introduction of a tourism anchor project to
virtually every significantly inhabited Family**

Island; we are arranging the supply of potable water to each and every Island; we are providing the telecommunications links throughout The Bahamas which will enhance the security of The Bahamas by providing a sound communications infrastructure in the event of national emergencies such as hurricanes; the telecommunications infrastructure will also enable every Bahamian to benefit from e-government, from the internet, and from distance learning; we are on the threshold of transforming the tourism and transportation sectors of New Providence; we are working diligently to aid the restoration of Grand Bahama and we have provided \$8million in the 2006/07 Budget for that purpose; we are placing enormous emphasis on all aspects of urban renewal to deal especially with the problems of disadvantaged youth, the elderly, the sick and

the poor; we are putting in place ambitious but achievable programmes and strategies to move aggressively to attack the problems of crime and illegal immigration which together constitute the greatest source of worry and anxiety for the Bahamian people; we are improving our educational system with special emphasis on vocational training and the development of the College of The Bahamas, and the introduction of much-needed reforms and innovations in our primary and secondary school systems; as evidence of our deep commitment to providing housing for lower income families, we have built more than 1,366 new homes in the first four years of our administration which is already more than the previous administration built in its entire two terms in office; we are enabling our health care system to raise the standard of delivery of essential health services; and we are

laying the foundations for an appropriate system of National Health Insurance which promises to be one of the most important instruments of social and health care reform in our nation's history.

Make no mistake about it, Mr. Speaker. My Government's record is clear. It is as unequivocal as it is undeniable. We can lay claim to an exemplary record in managing the economy since entering office in 2002. Moreover, we have secured the future economic prospects of The Bahamas, prospects which are unrivalled in this Region and without precedent in the economic history of our country.

Each of the Ministers in my Government during the course of the Budget Debate will be pleased to enlarge on the proud record of his or her portfolio and to back up my words.

THE SUCCESS OF OUR ECONOMIC AND
SOCIAL PROGRAMME

The Tables in Annex B to this Communication show very clearly and undeniably how my Government steered the Bahamian economy from the stagnation of 2001/02 to the present situation where the economic prospects of The Bahamas are unprecedented. These are similar to the Tables in Annex B of the 2005/06 Budget Communication.

Every single indicator in the Tables in Annex B shows positive results. And lest we forget, it was brought about by my Government even before it has completed its first term.

Economic Growth

Looking through the information one can see that economic growth is increasing steadily each year and will be 5.8% in 2006 as compared with

2.3% in 2002 when we entered office, or 0.8% in the previous year, 2001.

The recent IMF Mission projects a growth rate for the fiscal year 2005/06 of 4.7%, for the calendar year 2006 of 5.8%; and for the fiscal year 2006/07 of 6.5%. These overlapping projections strongly suggest that the growth rate of the Bahamian economy started to accelerate in the latter part of 2005 and will continue to accelerate through the whole of 2006. Infact, the IMF projections show a growth rate of 6.7% for 2007/08 so it is clear that the IMF accept the acceleration of the economy right through the next two fiscal years at least. These projections are given in the IMF's Aide-Memoire which I will elaborate upon later in this Communication.

The positive turnaround in the economy which has been achieved and continues to be achieved by my Government arises from my

Government's success in attracting productive investment in tourism projects in virtually every major Island of The Bahamas, and from my Government's careful stewardship of this economic expansion the likes of which are without precedent. The projected volume of inward investment is at least \$8Billion over the next few years. In relation to the size of the economy, this is a scale of inward investment without parallel anywhere in the world. The volume of investment is well in excess of the 2005 GDP of The Bahamas of \$5.9Billion. A special additional table is included in Annex B of the Communication which summarises the Central Bank data on these capital investment inflows. The capital inflow will further strengthen in 2006 and 2007 with the BahMar project and the construction of two new hotels in New Providence, and the acceleration of the

investment projects envisaged for the major inhabited Family Islands.

I might add that throughout The Bahamas we are upgrading airports to meet the upsurge in international traffic arising from the major new tourism projects coming on stream. In particular, Nassau International Airport, soon to be Sir Lynden Pindling International Airport, is being placed under private sector management and the whole airport complex is to be developed to the highest international standards. This will be a self-financing project and the end-result will be an international airport of which Bahamians can be truly proud.

The advance of our tourism sector is borne out by the fact that in 2004 the number of visitors exceeded 5 million for the first time in our history. The year 2005 saw further increase in that number, and all the indications are that

2006 will be even better. Moreover, it is not only the numbers but the expenditure and room rates which are being generated which are also increasing. Indeed, since a number of the new projects include major upmarket projects in New Providence and the Family Islands, these projects will further boost expenditure and room rates throughout The Bahamas.

This Budget Communication could not be complete unless I mentioned the planned relocation of our commercial port to the southwestern end of New Providence, and the attendant redevelopment of Bay Street into a tourism Mecca of world class standards. This is an undertaking of colossal proportions but with the public/private sector partnership that we have forged is well on its way to becoming a reality.

The scale of the projected investment in the tourism projects, and in the infrastructure which is required to support them, is such that it calls for major changes in the culture and performance of the public sector. A major challenge for the public sector, and particularly for Permanent Secretaries and the heads of the major utilities Corporations and the senior management in the Ministries and Corporations, is to ensure that the required public services - utilities, security services, education, transportation, housing and health services - are in place in a timely manner to meet the needs in each community and in each project arising from the investments.

The Office of the Prime Minister is providing the strategic planning and coordination function on this issue. The development of this function is rightly seen as a major aspect of Public Sector

Reform, and special training seminars and workshops are planned to ensure the success of this function.

In order to lessen demands on the Treasury and to demonstrate good corporate governance on the part of investors, our investment policy requires partnership in joint provision or joint financing by the public and private sectors of the facilities and services which each anchor project and the community concerned may require. This policy also places greater pressure for efficiency and effectiveness in the delivery of public services.

This approach is exemplified by the position in relation to Mayaguana where Government and the I-Group are accepting joint responsibility for providing the major new and additional public services and facilities needed to make the resort development project a success and enable the

people of Mayaguana to enjoy the benefits of the project and to grow into a prosperous, socially balanced community.

Again, the implementation of the policy will make exceptional demands on the management of the public sector. I am confident that these demands will be adequately met.

Fiscal Deficit

Mr. Speaker:

Returning to the indicators in Annex B to this Communication, the GFS Deficit is firmly under control and we have placed it on a declining trajectory. The GFS Deficit will be 1.9% in 2006/07 as compared with 3.1% in 2001/02. Thus, the deterioration in the ratio of Government debt to GDP has been arrested and has commenced on the glide path to return towards the 30% level within the medium-term.

The improvement in the public finances does not arise from austerity in expenditure but in growing the economy so that the response is revenue buoyancy. In fact, during our four years in office we have not made any increases in taxation. Indeed, we have accomplished the very opposite by reducing taxation, the most significant reduction being that arising from increasing the threshold for Real Property Tax in the 2002/03 Budget or to put it differently, extending exemption from Real Property Tax to many more people than before. In consequence, very many families on modest incomes have been relieved of the burden of this Tax.

We have certainly tightened revenue administration, and we have increased some fees by modest amounts for Government services but these are not instances of taxation. On the contrary, these are fees for services and the

increases were intended to go towards meeting, at least in part, the costs of providing the services.

We have certainly closed any tax loopholes which we have detected, primarily in relation to Stamp Duty because we see no reason why tax evasion and avoidance should be countenanced at the expense of compliant taxpayers. But the major impulse to the correction of the public finances has come from the growth in the economy giving rise to substantial revenue buoyancy.

Tourism

Again, continuing with the review of the indicators in Annex B, the tourism industry is already doing well and visitor arrivals and expenditure are taking off and exceeding the levels last achieved during the mid-1990's. When the new tourism anchor projects in the

Family Islands come on stream over the next few years, and the transformation of New Providence is completed, our tourism industry will be the most formidable and successful in the Region. In that regard I wish to again emphasise that my Government will be doing everything possible to aid the recovery of Grand Bahama.

Unemployment

Unemployment is declining and will decline dramatically further when the major tourism projects reach full steam. In this regard, it is our intention to expand the Urban Renewal Programme to ensure that our young people are given all of the means necessary to achieve remunerative and personally satisfying employment. To that end we intend to use a manpower survey approach, drawing on the expertise of the Department of Statistics, to assess the employment needs of presently

unqualified young people, and then put in motion vigorous programmes to equip them with the education, skills and training they need to take up the employment opportunities coming on stream.

Our young people have so much to gain, and we as a nation have so much to gain too, from their fullest participation in society. The Government is doing everything possible to provide them with opportunities, and it is up to these young people to avail of these opportunities.

The Urban Renewal Programme has a crucial role to play in enabling the identification of young people at risk. If they are not reached through this Programme or through other initiatives involving the Government and voluntary organizations, there would be the danger that they would lose hope and become

entrapped in anti-social behaviour, and perhaps ultimately in crime. Thus, an important effect of the Programme is to move young people away from a life which would bring them ultimately into conflict with the forces of law and order.

Let us not be under any illusions as to just how important our work in this regard really is. No less a person than His Grace Archbishop Drexel Gomez has described the Urban Renewal Programme as very possibly the most important social programme ever undertaken by any Government since Independence. The Programme has won enthusiastic acclaim throughout our Region and around the world. It is transforming our communities and rebuilding lives one by one. It is bringing hope where there was only despair. I sincerely hope that those who were critical of the Programme, because of their failure to understand its import, and the impact

it is having on aiding people to reconstruct their lives and neighbourhoods, will now acknowledge their error and endorse the Bahamian and international acclaim to which I have referred.

On this issue, let us recall the memorable words of the late Rev. Martin Luther King:-

“When an individual is no longer a true participant, when he no longer feels a sense of responsibility to his society, the content of democracy is emptied...when the social system does not build security but induces peril, inexorably the individual is impelled to pull away from a soulless society. This produces alienation – perhaps the most pervasive and insidious development in contemporary society.”

The goal of my administration is to enable everyone to succeed, or if they fail initially, to have more than one chance to succeed. I know

how important this is because I myself am a living testimony to the redemptive power of the second chance.

In the case of those who, for reasons of age or handicap or illness, must be more fully supported in their endeavours, we are developing social policies which address their predicament. It is imperative that we do so because we cannot have a partitioned society where some succeed handsomely while others simply fall behind. We must have an integrated society where all are given the opportunity to share equitably in the fruits of our economic development and to develop themselves to their full potential. In particular, we simply must make every effort to involve our young people in our society, who might otherwise be at risk, to make them feel part of our society and to show them the way forward and to provide them with the motivation

and the skills they will need to survive and prosper.

It is my hope that through the Urban Renewal Programme we can identify those in need or those who feel alienated, and bring the resources of our society, both public and private, to bear in helping them. But, in the final analysis, the ultimate responsibility rests with people themselves to avail themselves of the opportunities presented for education and skills training.

External Reserves

Mr. Speaker:

Continuing with the review of the economic indicators, it will be noted that the Bahamian currency is strong as never before, because the External Reserves of the Central Bank have rebounded from \$312million in 2001 to almost \$600million today. As explained in the *Economic*

Background in Annex A to this Communication,
the strength of the External Reserves has
permitted the Central Bank to relax certain
exchange controls, further evidence of the
growing strength of the economy.

Interest Rates

Annex A to this Communication sets out the
Economic Background to the Budget. A reading
of this Annex will reveal that the benefits of our
policies are apparent in the availability of
employment opportunities, the expansion of
essential services without the need for additional
taxation, the improvement in pay and conditions
throughout the economy, the increase of over
16% in the amount of residential mortgages in
2005, and the reduction of 4 basis points on
interest rates. And even with all that we are only
at the take-off position in relation to the
economy.

**Confirmation by International Rating Agencies
and the IMF**

Any objective observer would be bound to agree that my Government team has brought the Bahamian economy from its low point of 2001/02, when all of these indicators were negative, to the present stage where the Bahamian economy has already reached take-off point into what could be, the longest, highest and most sustainable economic expansion of our history.

Indeed, there are objective observers who have confirmed the evidence of our achievements, and of the economic potential which we are releasing. These observers are the two Rating Agencies, Moodys and Standard and Poors, which have continued to give investment grade ratings to The Bahamas. In the case of Moodys, the rating for The Bahamas is the

highest among the independent countries in the Hemisphere excluding the North American giants, the United States and Canada. In the case of Standard and Poors, the rating for The Bahamas is equaled by only one other country in this Region, excluding the two North American giants.

In further confirmation of the excellence of the Government's management of the economy I would direct the attention of Honourable Members to the Aide-Memoire of the recent IMF Staff Visit which I am tabling along with this Communication.

By way of background to this Aide-Memoire, The Bahamas is on a 24 month cycle for IMF Article IV Consultation Missions. The last such Mission was in 2005, and the Report is available on the internet. In every other year to the year in which the Consultation Missions occur, the

IMF makes what is termed a “Staff Visit”. This Visit provides an opportunity for the IMF staff to obtain an update from many sources, including the banking and financial sector, the Chamber of Commerce as well as from the Ministry of Finance and the Central Bank, on the rapidly changing economic and fiscal developments in The Bahamas.

Just as importantly, the Visits are valuable for providing an opportunity for discussion between the technicians in the Ministry of Finance and the Central Bank and the IMF Staff on these developments. The Aide-Memoire prepared by the IMF staff provides their views on a number of key issues.

Needless to say, the institutional conservatism, which is the hallmark of the IMF, is reflected in the Aide-Memoire. Nevertheless, as I have said, even the IMF projects growth in

2006/07 to be 6.5%, in 2007/08 to be 6.7%, in 2008/09 to be 5.6% before tapering off later as the horizon lengthens and uncertainties can arise. Thus, even the IMF agrees with the Government's optimism about the expansion of the Bahamian economy.

I might add that on most crucial issues the thinking of my Government is very close to that of the IMF. Such differences as there may be are not substantial and relate more to matters of practicality and timing rather than to policy disagreements. In this regard I am drawn to the comments of Mr. Haruhiko Kuroda, the President of the Asian Development Bank, in his interview with the IMF quarterly magazine, *Finance and Development*. Mr. Kuroda said:-

"I think that ... although economic theory may provide some insight, some framework, good policies may require something that

goes beyond just economic theory or analysis – some practical judgment, some good sense.”

It is this practical judgement which my Government brings to these matters. For this reason my Government consults widely, thereby taking into account the technical and other advice given to Government from many sources, including Ministries and Departments, other Government agencies, the private sector and the international organizations such as the IMF and the Inter-American Development Bank. No one person or organization has all the answers, although some like to think that they do, and that is why the broadest consultation is advisable on all key issues.

I might mention, in the particular context of the importance which my Government attaches to consultation, that there will be no

commitment to enter into trade agreements – regional, hemispheric or global – without the fullest consultation within The Bahamas.

Nor will there be any major changes in the revenue system of The Bahamas without the fullest prior consultation. My Government is not contemplating any such changes but, in view of the recommendation in the IMF Aide-Memoire regarding a VAT, a perennial recommendation of the IMF, I think it is necessary to set the record straight.

Importance of consultation

The hallmark of my Government is consultation, rather than impulsive decision-making, and the record demonstrates the soundness of this approach, in signal contrast, I might add, to the costly mistakes which are made when there is a rush into decisions without adequate preparation, without adequate

consultation, and without adequate care, prudence and proper planning.

A further attribute of my Government is caution in ensuring that each step forward is based on solid ground so as to better withstand any setback that may occur from external economic shocks or meteorological factors. Our economy is small and open. Therefore, we must be sensible in recognizing the intrinsic risks which we, in The Bahamas, face at all times. In this context one has to be mindful of the advice of the noted American economist Richard Cooper who said:-

“Governments typically behave as if positive shocks are permanent, and negative shocks are temporary.”

In exercising prudence in economic matters we are simply being sensible and responsible in our own interests. Even major economies can be

blown off course by an unexpected and unforeseeable economic chain of events. That is why, for example, within the European Monetary Union there is such insistence on careful macroeconomic management. Therefore, it behoves a small open economy such as ours to exercise the same level of care as is exercised by much larger economies.

My Government has not made nor will it make, promises which would undermine the economy and put at risk the future of every Bahamian. Every promise which we have made we have either fulfilled or we are determined to implement with care and prudence as our economy grows and is capable of providing the necessary financial resources.

There can be no disputing the information in Annexes A and B. This information is based, in the main, on published sources such as IMF

reports, Central Bank Reports, and Department of Statistics reports. Thus, it is information which is, or will be, easily accessible to the public via the internet. The information in the Annexes is irrefutable evidence of my Government's successful management of the economy and public finances, and of our restoration of the robust growth prospects of The Bahamas.

As mentioned in the 2005/06 Budget Communication, the Department of Statistics is now able to follow the internationally accepted standard for producing estimates of national income data. The recent IMF Staff Visit and the 2005 IMF Article IV Mission had confidence in the Department's work and used the data. In fact, the national accounts data were also crucial to the work of the consultants preparing the

report on the impact of tourism in the Bahamian economy.

LOOKING AHEAD

Mr. Speaker:

***The Speech From The Throne* earlier this year set out the Government's considerable achievements in its current first term in office. More importantly, however, it also maps out the policies which my Government is committed to following now and in the period immediately ahead to further enhance the economic and social security of the Bahamian people.**

The Bahamian people know our capabilities, and they know that our success to date places us within closer reach of the goals set out in the *Speech From The Throne*. I believe that the Bahamian people will agree that our record to date is a record of impressive achievement in a

remarkably short period of time. We are confident that our record is such that the Bahamian people will consider us worthy of their continued trust, support and confidence, as we make ready to propel The Bahamas forward in our second term in office.

FISCAL PERFORMANCE 2005/06

Turning to fiscal performance in 2005/06, the provisional outturn is for a GFS Deficit of 2.4%, compared with the figure of 2.8% in the Budget. The summary data is in Annex B, Table II to this Communication. This projected outturn is not very different from the projection in the IMF Aide-Memoire of 2.5%.

Revenue performance

The most striking point about budget performance in 2005/06 is the strength of Recurrent Revenues. These amount to

\$1,212million which is an increase of \$67million over the 2005/06 Budget Estimates of \$1,145million, and an increase of almost 15% over 2004/05 Outturn. The increase is attributable to three factors. Firstly, the growing strength of the economy which generated substantial revenue buoyancy, particularly in Customs revenues and Stamp Duty on both imports and property transfers; secondly, the closure of revenue loopholes especially under the Stamp Act which gave rise to all manner of tax avoidance schemes; and thirdly, the general tightening and overall improvement of revenue administration. An example of the latter is the implementation in the Customs Department of the TIMS, the *Trade Information Management System*, which is a useful tool in identifying situations where Customs revenue might be at risk.

Recurrent Expenditure

Recurrent Expenditure projected outturn at \$1,225million is very close to the original Budget Estimates of \$1,214million. It will be recalled that the 2005/06 Budget Estimates included most of the cost of the general Public Service pay award. The 2006/07 Recurrent Expenditure Estimates make provision for settlement of the teachers' award on the same basis as that award as well as for the Public Service pay award due on 1 July, 2006.

Capital Expenditure

The projected outturn for Capital Expenditure is \$175million, which is an increase of \$10million over the 2005/06 Budget Estimates. The increase is mainly attributable to increased allocations for Bahamasair, the Water & Sewerage Corporation, and the Broadcasting Corporation of The Bahamas. A Supplementary

Appropriation Bill is being tabled in relation to these additional allocations.

2006/07 FISCAL PROGRAMME

Expenditure Priorities

In terms of share of Recurrent Expenditure, it is clear that the major priorities are :-

- **firstly, the services which provide security for persons, property and our national frontiers; more specifically, these services encompass the Police, the Defence Force, the Immigration, and Customs Departments, and the Judicial System; and**
- **secondly, the measures which provide employment opportunities and which seek to integrate every Bahamian more fully into society;**

these measures encompass education and training, urban renewal, disaster relief, housing and the whole spectrum of social and health care services provided by the State.

2006/07 Recurrent Expenditure Allocations

Turning to the 2006/07 Recurrent Expenditure Estimates, these amount to \$1,386million. This is an increase of \$172million, or over 14% over the 2005/06 Recurrent Estimates. The increase of \$172million comprises:-

- An increase of \$56million for debt servicing, principally an enhanced provision for Debt Redemption.**
- A provision of \$14million for the pay award for the Public Service due on 1 July, 2006.**

- **A provision of \$5million for Increments due in 2006/07.**
- **An amount of \$40million arising from additional expenditure in 2005/06 which adds to the expenditure base in 2006/07. Examples are the additional allocations in 2005/06 of \$6million to the Public Hospitals Authority, \$8million for the National Emergency Management Agency, \$4.5million for the Royal Bahamas Police Force, \$4.6million for Customs overtime, and \$3.6million for the Department of Education.**
- **Major increases in provisions for all of the security services, education and health services.**

The major Recurrent Expenditure provisions in 2006/07 are:-

- **An increase of 15.4% for the Royal Bahamas Police Force.**
- **An increase of 18.9% for the Royal Bahamas Defence Force.**
- **An increase of 13% for the Immigration Department.**
- **An increase of 7.1% in the provision for Prisons.**
- **An increase of 13.1% for the Judicial Department, an increase of 12.6% for Magistrates Courts and an increase of 10.8% for the Court of Appeal; following the usual practice established over many years, some of these expenditures can be met by savings on the Heads concerned or on other Heads of Recurrent Expenditure; however, when such savings are unlikely to be realized,**

Supplementary Appropriations will be presented to this Honourable House for approval.

- **An increase of 21.3% for the Office of the Attorney General and Ministry of Legal Affairs.**
- **An increase of 10.2% for the Department of Social Services and Community Development.**
- **An increase of 11.4% in the provision for the Public Hospitals Authority.**
- **An increase of 9.8% for the combined educational heads.**
- **A provision of \$8million for the National Emergency Management Agency.**
- **A provision of \$2.45million for Urban Renewal.**

- **An increase of 53.8% in the provision for Mail Boat Service Contracts.**
- **An increase of 15.8% in the provision for the Department and Ministry of Public Works.**

Pay policy

In the 2005/06 Budget Communication, the importance of the orderly evolution of public sector salaries and wages was explained. Every responsible Government has to be concerned about this issue. It is important for the reasonable remuneration claims of all public servants to be recognized. About one-half of Recurrent Revenue is required to meet Public Service salaries and other remuneration. It is equally important that the Public Service accepts the implementation of measures to improve productivity so that pay increases are merited by productivity. As foreshadowed in the 2005/06

Budget Communication, an international expert has been engaged to provide advice on this issue.

2006/07 Capital Expenditure Allocations

The priorities in Recurrent Expenditure are also reflected in the 2006/07 Capital Expenditure Estimates. The major increases are as follows:-

- An increase of 22% for the Royal Bahamas Police Force.**
- An increase of 51.1% for the Royal Bahamas Defence Force.**
- An increase of 77.4% for Prisons.**
- An increase of 7% for Customs.**
- An increase of 24.4% for Education.**
- An increase of 4.8% for the Public Hospitals Authority.**

Adequate allocations are made across the board for every Head of Recurrent Expenditure. As I

said early in this Communication, each Minister of my Government will be pleased to place on record the achievements of his or her portfolio and to account for the expenditure allocations made for the Heads for which he or she is responsible.

Recurrent Revenue 2006/07

Mr. Speaker:

Turning to Recurrent Revenue in 2006/07, I am happy to advise that arising from the projected growth in the economy and improvements in revenue administration, there is no increase in taxation in this Budget. This means that my PLP Government has managed the public finances so prudently that we are able to reduce the GFS Deficit, improve essential public services, and improve pay and conditions in the Public Service, and achieve these objectives without any increase whatsoever in

taxation. We have ensured that our economic growth strategy generated the additional revenues which we needed.

Thus, the Recurrent Revenue Estimates for 2006/07 amount to \$1,345million which is an increase of 11.1% over the 2005/06 Provisional Outturn \$1,212million.

The IMF Aide-Memoire to which I referred earlier makes a number of suggestions as to additional revenue measures but these need further consideration before they can – or need – be implemented. They may be implemented in a later Budget but they are not included in this Budget.

Revenue changes

Indeed, in this Budget I am making a number of changes in taxation, in some cases significant reductions, and in others total elimination of the

taxation. Let me repeat for all to hear: NO NEW TAXES.

Indeed, I am reducing the 35% Customs Duty on Hurricane Shutters to 15%. I am also reducing the Customs Duty on stone coaled metal roofing shingles from 35% to 10%. These reductions are aimed at facilitating Bahamians taking precautions against storm damage or quickly repairing storm damage.

I am reducing various rates of duty, ranging from 25% to 40%, on items connected with solar equipment to a uniform 19%. This is an environmentally friendly measure.

I am also reducing the duty on gas powered water heaters by 5% to align it with that on electric powered heaters.

I am reducing the duty on soy milk from 45% to 15% to align it with that on fresh milk.

I am correcting the anomaly whereby loose stones and pearls can be classified under two tariff heads one of which carries a 35% duty and the other a zero rate. All will now be zero-rated.

I am also amending the Business Licence Act to provide that companies which pay excises under the Spirit and Beer Manufacture Act would be exempt from Business Licence Fee.

Revenue administration

The Ministry of Finance is continuing with its action plan to bring about improvements in revenue administration throughout the various revenue agencies. In this regard progress is well in hand in implementing a system designed to remove all manual receipting and to replace this with a cash receipting system whereby all receipts will be generated by computers. In addition acceptance of credit cards so as to bring greater flexibility and convenience to the public

when paying fees and charges, has been introduced in a number of revenue collection agencies. These efforts will continue for all agencies.

The Revenue Compliance Unit of the Ministry of Finance which was foreshadowed in my previous Budget Communication is about to begin its work. It is intended that this Unit will play a pivotal role in ensuring compliance in the payment of fees and charges due to the government, and thereby reducing leakages in the system. The work of this Unit will be focused initially on the areas of hotel room tax, stamp tax, business licence fee, road traffic fees and property tax. In addition, the analytical work to be undertaken by the Unit will provide the Ministry of Finance, and thereby the Government, with statistical data on which

informed policy decisions with regard to revenue matters can could be taken.

The government will move amendments to existing legislation to secure the collection of revenue due to Government when a business ceases operating, or when a business undertakes a change in equity ownership or when the business is sold. This will include changes to the Business Licence Act, Hotels Act, Passenger Tax Act and the Insurance Act, among others.

The reporting and collection procedures of all revenue agencies are being reviewed so as to maximize the use of information technology. This will bring improved collection of revenues, and generate data on revenue performance which can be analysed to further improve revenue policy and administration.

Business climate

The Government is committed to improving the business climate of The Bahamas because we know that a better investment climate pays off in good and sustainable business and employment opportunities for Bahamians. A great deal is being accomplished in this regard by streamlining Government administration, and through the development of e-government. Indeed, my Government is committed to the sensible diversification of the economy, as is evident from the establishment of the Domestic Investment Board. I agree with the IMF that there would appear to be a potential for the development of a domestic food sector. The Government would welcome proposals on this matter provided such proposals are viable and sustainable.

Of course, while inward capital investment by its sheer magnitude is a major engine of growth in our economy, my Government recognizes the crucial importance of encouraging investment by Bahamian entrepreneurs not only as a significant and increasing growth factor, but also as a means of Bahamians exercising control over their own economic destiny.

Therefore, concurrently with these externally financed investments, we are putting in place the domestic investment architecture, through the Domestic Investments Board, to encourage our own Bahamian citizens to develop businesses linked with, or even independent of, the anchor investments throughout The Bahamas. I believe that our own entrepreneurs are fully capable of providing a great percentage of the goods and services required by the anchor

investments and the new communities that will be created in consequence.

My Government will be ensuring that the various agencies – the Domestic Investments Board, the Bahamas Development Bank, the Bahamas Agricultural and Industrial Corporation, and the Venture Capital Fund – will fully support the development and enhancement of Bahamian entrepreneurs.

BUILDING AN EQUITABLE SOCIAL
PLATFORM

Mr. Speaker:

Our economic strategy is not an end in itself. Rather it is the means by which we build a strong economy as the lynchpin of a just and equitable social order.

The vision of my Government is that a strong economy, based on an equitable spread of

employment and entrepreneurial opportunities, allied with a sound public financial system will secure the attainment and preservation of a just and equitable social order in our country.

My vision is to have in place a social platform on which every Bahamian can stand with security, and where none fall below the level of social comfort provided by the platform. As our economy progresses and budgetary resources become available we shall be able to raise this social platform year after year. At every juncture, however, we will be mindful of the intrinsic risks facing a small open economy, and we will exercise care so that we proceed at the pace of our economic development and never outstrip it. Other countries have had sad experiences of moving too fast and allowing social programmes to outpace the economic means of paying for them. This has resulted in the misery of

economic adjustment programmes and attendant social dislocation. We must avoid this pitfall at all costs.

The platform of which I speak consists of meaningful employment opportunities, adequate housing, security of person and property, access to affordable health care, access to necessary social facilities and services, and educational and training opportunities.

In this context, I would like to emphasise that my Government is particularly concerned with the issue of affordable housing for lower and middle income families. This will continue to be a major priority of my Government. The coming months and years will witness a vigorous continuation of the Government's housing programme to complement the impressive achievements already attained in our first four

years, which I have referred to earlier in this Communication.

My Government is also concerned with ensuring that suitable housing is available to young Bahamian professional couples. To that end the Government intends to obtain suitable land in New Providence and the Family Islands to provide sites for housing for middle-income families.

CONCLUSION

Mr. Speaker:

My Government is committed to the empowerment of the Bahamian people in all spheres of life. Empowerment means providing the environment, the means and opportunities, and, as far as possible, the motivation for the Bahamian people to exercise control over their own destiny. Empowerment is at the other end of

the spectrum from a dependency culture. In this regard, I would like to quote the great Nineteenth Century British philosopher and parliamentarian John Stuart Mill who provided timeless advice on the role of government in a liberal democracy such as ours:-

“A good government will give all its aid in such a shape, as to encourage and nurture any rudiments it may find of a spirit of individual exertion. It will be assiduous in removing obstacles and discouragements to voluntary enterprise, and in giving whatever facilities and whatever direction and guidance may be necessary: its pecuniary means will be applied, when practicable, in aid of efforts rather than in suppression of them, and it will

call into play its machinery of rewards and honours to elicit such efforts.”

My Government has achieved a great deal - if I may say so, a very great deal - in four short years. One can visualize the achievements yet to come. My vision is that the Bahamian people will continue to face the challenges of globalisation with confidence and ambition, and that under the leadership of a Progressive Liberal Party Government they will continue to build a society in which everyone has the opportunity to serve, to participate and to fulfil his or her dreams and ambitions for a better life.

My ambition in this regard finds its most poignant expression in the absolute imperative that we lift up and give a second chance to all those in our society who may have fallen through the cracks or fallen by the wayside.

We must measure our success in terms of how well we manage to lend a helping hand to those of whom I speak. They have the talent. They have the ambition. All they need is a second chance and it will always be the business of my Government to see to it that a second chance is given to all those who are in need of it.

We are well on our way, Mr. Speaker, and with God's continual blessings and the continued support of the Bahamian people we will make our way forward into the future, knowing that our best days are still ahead, and that though the present times be bright, the future that beckons us is brighter still.

ECONOMIC BACKGROUND

INTRODUCTION

Preliminary estimates from the Department of Statistics (DOS) indicate that the Bahamian economy grew by 3.7% in nominal terms during 2005, despite global oil price pressures and the devastating hurricanes. Growth was supported by increased levels of foreign investment, strong consumer spending, robust expansion in construction activity and firming tourism output.

For 2006, the Bahamian economy is expected to grow further by 5.8%, led in part by sustained output in the tourism sector, foreign investment in tourism related infrastructure, and residential construction activity. Indications are that global oil prices will continue to firm; however, the sharp increases noted in 2005 should be tempered somewhat this year. Consequently, inflation is expected to be relatively moderate.

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, followed by an analysis of the domestic environment, including policies and trends affecting the financial sector.

INTERNATIONAL ECONOMIC DEVELOPMENTS

The International Monetary Fund (IMF) in its April 2006 World Economic Outlook estimates that global output growth eased to 4.8% from 5.3% in 2004, primarily attributed to escalating oil prices amid persistent Middle East geopolitical tensions and natural disasters. The price of oil grew to its highest levels

during the year, as the Organization of Petroleum Exporting Countries' (OPEC) increased output levels, failed to compensate for growth in global demand, especially among the Asian economies. As a result, many developed countries recorded an overall weakening in their current account positions. Given these developments, labor markets in developed countries remained subdued, while several central banks implemented rate tightening policies in an effort to mitigate the effects of higher prices.

Initial data suggest that economic growth in the United States declined to 3.5% from 4.2% in 2004, mainly due to a falloff in inventory investment and reduced consumer and federal government expenditure. Led by considerable employment gains in professional and business services, and health care and leisure & hospitality industries, the average unemployment rate in the US decreased to 4.9% from 5.4% in 2004. US average consumer prices increase to 3.4%, from 2.7% in 2004. Meanwhile, the positive outlook projected for the US economy, coupled with higher domestic interest rates, contributed to an appreciation in the United States' dollar against major currencies during 2005.

With respect to other major world economies, economic growth in the Euro-zone for 2005 is estimated at 1.3% compared to 2.1% in 2004. In the United Kingdom, the expansion in economic activity slackened to 1.8% from 3.2% in the previous year. Japan's output improved slightly to 2.8% from 2.3% a year earlier, reflecting higher exports and private consumption.

The outlook is for global growth to slow slightly through early 2006, and pick up modestly in the following months as central banks adopt relatively accommodative monetary policies. With respect to the US, the economic expansion is not expected to be as strong as in 2005; however, the increase in activity is still forecast to be the highest among the G-7 countries.

In the commodities market, the IMF has raised its forecast for oil price increases in 2006, reflecting the consensus that the present supply constraints and consumption demand pressures alongside geopolitical tensions, will continue to bid up fuel costs. Since the start of the year, the US dollar has depreciated against many of the major currencies. Market sentiments indicate that the favourable interest rate differential for the US dollar observed during 2005 is likely to be reversed in 2006, as the Federal Reserve ends its rate increases in contrast to the tightening bias posture assumed by other central banks, such as the ECB.

DOMESTIC ECONOMIC DEVELOPMENTS

In 2005, increased consumer spending, construction activity and tourism related foreign direct investment supported further strengthening in the Bahamian economy. Gains were also recorded in the tourism sector, as room revenues advanced and favorable economic conditions in the United States supported a marginal increase in visitor arrivals. Inflation remained contained, despite a general rise over the previous year's level. In light of buoyant economic conditions and a more liberal lending environment following the removal of credit restrictions, bank credit accelerated resulting in a contraction in liquidity and external reserve levels. The fiscal situation benefited from the generally healthy level of economic activity, as the corresponding growth in tax receipts facilitated a reduction in the comparative fiscal deficit for the first half of FY2005/06. On the external side, however, the rise in import demand combined with higher global oil prices caused the current account deficit to expand significantly, which was financed in large measure from foreign investment inflows.

TOURISM

Following the devastation of the 2004 hurricane season, tourism activity during 2005 showed some

strengthening, principally as a result of growth in the US economy and firming in room rates. The overall performance of the industry for the year was sustained by a 4.4% improvement in air arrivals which eclipsed the 0.5% weakening in cruise visitors.

By ports of entry, arrivals to New Providence were up marginally by 0.1%, as an 11.6% increase in air traffic was dampened by the 5.5% fall-off in the more dominant sea arrivals. Visitor count for the Family Islands reflected gains in both air and sea components, by 2.9% and 10.8%, respectively. Although registering some improvement in the final quarter, total arrivals to Grand Bahama fell by 11.2%, with air and sea visitors weakening by 20.6% and 5.9%, respectively.

Hotel sector performance indicators signalled an increase in the overall tourism output, supported by price appreciation and higher room night sales. The Ministry of Tourism's survey of large properties indicated that growth in hotel room revenue strengthened to 9.2% from 4.1% in 2004, with increases in New Providence, Grand Bahama and the Family Islands of 9.1%, 7.8%, and 15.7%, respectively. Occupied room nights improved by 4.6%, and average nightly room rates advanced by 4.4% to \$156.56. Overall, hotel occupancy rates rose to 70% from 66% in 2004.

Preliminary information for the first two months of 2006, indicate a weakening in tourism output, as total visitor arrivals contracted by 5.2%. This outcome reflected negative developments within the cruise sector, with arrivals from this category declining by 8.7%. However, the higher value-added air arrivals rose by an estimated 3.9%.

FINANCIAL SECTOR

Banking, insurance and investment funds activity for 2005, suggest that the financial sector experienced healthy balance sheet trends and stable employment conditions. Mainly owing to the Central Bank's physical presence requirement which was adopted for the banking sector in 2001, the number of licensed banks and trust companies in the financial market fell by 16 to 250 during 2005. The number of public licensees decreased by 8 to 149, as did the number of restricted and non-active operations to 101.

As at 30 June 2004, all licensees which had not met the Central Bank's physical presence requirements were obligated to have established a presence in The Bahamas. The sole exception related to those licensees which had entered into special managed arrangements approved by the Central Bank. In keeping with this requirement, 205 licensees operated through physical presence at end-2005, compared to 213 at end-2004. An additional 42 institutions continued to operate under restrictive management arrangements approved by the Central Bank, while 3 institutions implemented measures to ensure compliance with the regulations. Indications are that employment in the sector remained close to 2004's level of 4,366.

Data from the Office of the Registrar of Insurance Companies for 2004 highlighted further growth in the industry. The number of licensed insurance operations in The Bahamas increased by four (4) to 195 at end-2005, the number of companies operating in the domestic sector totaled nine (9), the number of domestic broker and agents and external operators totaled 89 and nine (9), respectively. Moreover, total assets at end-2004 exceeded \$552 million and were mainly concentrated among life and health insurance companies.

Data from the Securities Commission indicated that the total number of active investment funds

operating from or within The Bahamas fell by 185 to 653 at end-June 2005, compared to the previous year, with assets under management totaling an estimated US\$164.1 billion.

CONSTRUCTION

Key indicators of construction activity suggest a significant improvement in output during 2005, fuelled by robust growth in residential mortgage lending activity as well as foreign investments in tourism-related projects. Prospects for 2006 are equally encouraging for both residential and commercial construction investments, based on outstanding commitments.

Mortgage commitments for new construction and repairs totaled 1,883 valued at \$229.1 million as compared to 1,175 in 2004 at a corresponding value of \$131.0 million. The residential component accounted for the majority (96.3%) of disbursements, valued at \$214.5 million, which was 71.9% higher than the previous year's total. Commercial drawdowns, valued at \$14.6 million, more than doubled and accounted for 3.7% of total commitments.

Outstanding mortgages for 2005 increased by 15.9% to \$2,159.4 million. Residential lending, at 91.5% of the total, rose by 16.1% in 2005, whereas commercial loans outstanding advanced by 13.9% and accounted for the remaining 8.5% of the aggregate. Interest rate conditions remained favourable as both commercial and residential average loan rates fell by 4 basis points each to 9.2% and 8.4%, respectively.

INFLATION

Domestic price inflation increased to 2.2% from 1.0% in 2004, owing to pressures in the global oil market as well as local factors. Cost increases were registered for medical care & health (3.4%), food &

beverages (3.2%), education (3.2%), and housing (2.6%) – the most heavily weighted category—and lesser increases for other goods and services (1.9%), and furniture & household operation (1.3%). Cost declines were noted for clothing & footwear (2.2%) items.

Initial data suggests a continuation of the trend in the first quarter of 2006, as the rate of inflation advanced to 2.1% for the twelve-month period ending March from 1.1% in the comparable period of 2005. Growth mainly reflected higher food & beverages, housing and other goods & services costs.

UNEMPLOYMENT

The rate of unemployment rate for 2005 was stable at 10.2%. This was largely the result of a reduction in unemployment in other parts of The Bahamas being offset by an increase in unemployment in Grand Bahama from 9.3% in 2004 to 11% in 2005. Thus, in 2005 the jobs generated from the reconstruction effort offset the jobs lost due to the closure of the Royal Oasis. The position is reflected in the stable labour force participation rate of 74.7% in 2005.

AGRICULTURE, FISHERIES AND INDUSTRY

Agriculture and fisheries was affected by the 2004 hurricane season, where the total output for this sector declined from the historically high levels of 2003. Industry was also affected by the 2004 hurricane season, most notably electricity production which was marginally lower than 2003. Overall the modest growth in the industry sector was limited by the 2004 hurricane season.

FOREIGN INVESTMENT AND THE BALANCE OF PAYMENTS

The Central Bank's balance of payments estimates showed that the current account deficit deteriorated significantly in 2005, due to higher prices for imported

fuel, and robust growth in consumer and business demand, which boosted non-oil imports.

Preliminary data indicate an expansion in the trade deficit by an estimated 13.9% to \$1,626.2 million, following the 7.3% increase in 2004. Volatility in the global oil market reinforced a 43.7% increase in the oil import bill to \$525.2 million, with double digit gains across all products.

The expansion in the current account deficit was partially financed by growth in the capital and financial account, as sustained foreign investment in tourism infrastructure, second homes and timeshares elevated the estimated surplus on the capital and financial account by 38.3% to \$429.5 million.

CAPITAL MARKETS

The strength of the Bahamian economy during the year fostered improved investor sentiment as evidenced by increased trading values on the Bahamas International Securities Exchange (BISX). Although the volume of securities traded declined by 15.9% to 6.7 million shares, the value rose by \$12.8 million or 49.8%. The BISX All Share Price Index rallied by 30.0% to 1,350.7 points, outpacing the 19.7% expansion in 2004. Consequently, BISX market capitalization expanded by 34.8% to \$2.6 billion and, in the absence of any new private capital offerings during the year, the number of publicly traded companies on the Exchange remained unchanged at 19. Similarly, valuation represented in the broader Fidelity Capital Market Limited's Index (Findex), which also captures over-the-counter trading, rose by 28.4% to 551.9 points from 14.9% in 2004. There were 27 securities trading locally, including four (4) over-the-counter instruments and four (4) mutual funds.

PAYMENTS SYSTEMS MODERNISATION

The Central Bank and the Clearing Banks' Association continued to collaborate in an ongoing project aimed at modernizing the domestic payments system by, inter alia, the establishment of more secure and efficient operational systems that would offer additional services to the public.

The first leg of the Payments System Modernization Initiative (PSMI) was achieved with the implementation of the Real Time Gross Settlement System (RTGS) in May 2005, for large and time sensitive transactions. During 2005, the RTGS had a daily average of 76 transactions from seven clearing banks and the Central Bank, valued at an estimated B\$31.53 million.

The process to establish an automated clearinghouse (ACH), designed to eliminate manual cheque clearing and to provide for other payment services, was considerably aided by the creation of working groups to define and oversee the project. Additionally, World Bank experts were engaged to further support the activity of the working groups and to assist in reviewing the "Vision Statement" and service requirements. Following revised targets, the automation of the cheque clearing system is now scheduled to commence by end-June 2006 and the implementation of direct debit and credit payment services by end-December 2006.

During the year, the Central Bank, in consultation with other strategic financial sector partners, finalized revisions to its exchange control regime. These measures involved the liberalization of various capital account restrictions designed to increase investment opportunities available to Bahamians in the global market, and deepen domestic capital markets while simultaneously allowing temporary and permanent residents to participate more meaningfully in the country's financial markets. The consultations culminated in the issuing of a press release by the Bank,

outlining the liberalization measures in January of this year.

MONEY AND CREDIT DEVELOPMENTS

Following the August 2004 elimination of the credit restrictions imposed on local banks and the decision to lower the discount rate, which gave rise to a reduction in commercial banks' prime lending rate, domestic demand increased as consumers responded to the more favorable lending and economic environment. Consequently, liquidity levels declined as domestic credit advanced significantly. However, despite the rapid growth in loans, indications are that there was an improvement in domestic banks' asset quality during 2005 as the rate of arrears for both commercial and residential mortgages declined while the arrears rate for consumer loans rose marginally.

Growth in domestic credit more than doubled to \$672.3 million (12.9%) compared to \$253.2 million (5.1%) in 2004. Bahamian dollar lending firmed by 12.7% up from 7.4% in 2004, while domestic foreign currency credit, which was primarily utilized for tourist-related projects, rebounded by 14.1% from the preceding year's 9.9% fall-off. Private sector credit recorded strengthened growth of 14.2% (\$614.3 million) in comparison to 6.0% (\$244.8 million) in 2004. Specifically, the addition to the Bahamian dollar component at \$518.1 million (13.1%) was almost twice the preceding year's level, while foreign currency claims recovered by \$96.2 million (25.2%) from the 7.2% reduction in 2004.

Amid increased domestic credit and higher oil prices, external reserves contracted by \$89.0 million (13.3%) to \$578.8 million, reversing the \$183.5 million (37.9%) gain in 2004. However, reserves witnessed a record month-end peak of \$792.9 million in May, and at year's end, were equivalent to an estimated 19.5 weeks of non-oil merchandise imports compared to 23.3 weeks at end-2004. For the first three months of 2006, the

reserve buildup of \$59.1 million was slightly higher than for the comparative period of 2005, benefiting from improvements in the tourism sector and ongoing foreign investment flows.

In interest rate developments, the weighted average loan and deposit rates contracted by 93 basis points to 10.34% and 61 basis points to 3.22%, respectively. Moreover, the average rate on commercial mortgages fell by 107 basis points to 8.10%; for overdrafts, by 81 basis points to 10.86%; for consumer loans, by 74 basis points to 12.22% and for residential mortgages, by 73 basis points to 8.08%. With regard to deposits, the average savings rate decreased by 31 basis points to 2.26%, with lower returns on fixed deposits of 3.13%–3.62% in comparison with 3.69%–4.46% in 2004.

NATIONAL DEBT

On a calendar year basis, the rate of growth in the Direct Charge on Government slowed to 6.5% (\$137.3 million) from 8.4% (\$161.7 million) in 2004. Bahamian dollar debt advanced by 7.5% in 2005, compared to growth of 10.1% in the previous year, while the level of foreign currency debt remained relatively unchanged.

The Government's contingent liabilities increased by 13.1% (\$57.6 million) to \$497.5 million in 2005, compared to a decline of 5.9% (\$27.7 million) in the previous year. The expansion was attributable to additions to the guaranteed debt of the Bahamas Mortgage Corporation, and the Airport Authority, together with the \$24 million new debt issue of the Clifton Heritage Authority.

Public corporations' debt rose by \$31.8 million (5.6%) to \$599.0 million, in contrast to a contraction of \$37.8 million (6.2%) in 2004. The advance was solely on account of growth in Bahamian dollar debt of \$43.8 million (15.1%), as the foreign currency component declined by \$11.9 million (4.3%) to \$264.7 million.

Taking into account guaranteed debt of the public corporations, National Debt advanced by \$194.9 million (7.7%) to \$2,732.7 million at end-December 2005, some \$60 million more than in the previous year. However, continued improvements in the economy led to a further reduction in the debt service ratio as a percentage of exports of goods and services and as a percentage of government revenue, from 3.4% and 2.7% to 2.8% and 1.9%, respectively in 2005.

ECONOMIC OUTLOOK

The outlook for the Bahamian economy in 2006 is strongly positive as ongoing foreign direct investment and sustained tourism demand will result in enhanced and sustainable economic growth. Employment levels will also improve as more jobs are created in the construction and tourism sectors.

Nonetheless, a small open economy such as The Bahamas always remains vulnerable to global economic shocks such as upward movements in the price of oil, a major downturn in global economy, and weather-related shocks.

Notes on Multi-annual Projections 2006/07 to 2008/09

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 environment¹. The Projections are not intended as the 'vision' of the evolution of the public finances nor as immutable commitments, and are subject to margins of error. The following paragraphs explain some of the issues involved.

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 for a considerable number of years it was below the level of 20% 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 to reduce the level to about 30% of GDP² in the medium-term so as to leave 'fiscal*

¹ Forecasting is inherently fraught with difficulty because the future is unpredictable; as Macbeth states (I,iii)

If you can look into the seeds of time
And say which grain will grow and which will not,
Speak then to me

(quoted in Hendry and Ericsson: Understanding Economic Forecasts)

² The Contingent Liabilities (Government Guaranteed Debt of the Public Corporations, Bahamasair, and other public authorities) component of the National Debt is also carefully monitored particularly the components (such as borrowings by the loss-making Public Corporations) which require or may

space' to meet unforeseen and unforeseeable shocks.

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, severe hurricane damage in recent years, 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 and to the volume of direct foreign investment, 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 inflows³, 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 need and scope arise.

5. The projections for GDP growth are the projections in the IMF Aide-Memoire prepared by the recent Staff Visit. The projections assume GDP growth in current prices of 6.5% in 2006/07, 6.7% in 2007/08 and 5.6%

require funding for servicing the debt from the Consolidated Fund. For the purposes of these projections it is assumed that there is no change in policy as regards borrowing by the loss-making entities.

³ The projections for Capital Expenditure assume, *inter alia*, that Government policy is to limit the capital expenditure of Government; this policy is based on requiring joint public/private sector provision, or equivalent financing, in relation to the major tourism projects coming onstream; in many instances these projects require the provision of new or enhanced facilities and services which would normally be solely provided or funded by Government.

in 2008/09. (It is not clear why the growth rate in 2007/08 could be projected to slacken in that year, given that the likely volume of direct investment expenditure in that year is likely to be at least as great as in 2007/08. Therefore, a growth rate of 6.7% would appear to be more likely in 2008/09 than the lower projection of 5.6%.) The projections also assume that Recurrent Revenue will grow in 2007/08 and 2008/09 by 8% in each year (which is a little above the growth rate of the economy) because of the expected increased revenue buoyancy arising from the massive direct capital 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 plateau⁴. 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 of Government Debt; in the case of Bahamasair, privatization could result in a significant reduction in the considerable capital transfers made in the budget to Bahamasair.

6. The projections would result in the GFS Deficit being reduced to 1.1% in 2008/09, and the ratio of Government Debt to GDP being reduced to 36.3%.

7. 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, 2006

⁴ See previous footnote.