



COMMONWEALTH OF THE BAHAMAS

2008/2009 MID-YEAR BUDGET STATEMENT

ON THE SIX MONTHS ENDING 31st DECEMBER 2008

Presented to the Honourable House of Assembly

by

**The Rt. Hon. Hubert A. Ingraham, M.P.
Minister of Finance**

on

Wednesday, 25th February, 2009

INTRODUCTION

I have the honour to present the Mid-Year Budget Statement for the six-month period ending December 31, 2008.

The deteriorating global financial and economic crisis, with devastating effects on all economies, places an enormous challenge on Governments to provide leadership. Leadership to overcome this crisis is being provided by the United States and the other major economies. At this time, the global economy is not yet responding but it is clear from the statements made by the leaders of the major economies that they will persist with strong reflationary initiatives until the global economy responds.

My Government has responded to the leadership challenge before it, and it will continue to do so, in order to lead The Bahamas back to sustained prosperity as the global environment improves. Moreover, to the maximum extent possible within the limitations imposed by the external

environment, my Government is taking all the initiatives within its own power and discretion to maintain the economy independently of the global environment.

This is the context within which this Mid-Year Budget Statement is being presented.

This Statement fulfills, again this year, the commitment that I made to this Honourable House and to the Bahamian people in the 2007/08 Budget Statement, to demonstrate transparency, accountability and orderly budgeting. To that end, this Statement sets out:

- the economic background of the fiscal year to date;**
- the fiscal performance during the first six months of the current fiscal year; and**
- any proposed additions or variations to expenditure.**

ENHANCING GOOD GOVERNANCE

Strengthened Accountability

I begin by emphasizing the very high priority that my Government attaches to continuing to enhance good governance for the benefit of all Bahamians. This Statement is but one of a number of initiatives that we have, and will be implementing to strengthen good governance.

The introduction of this Statement into the budgetary process represents a fundamentally important element of good governance; it obliges the Government to report to Parliament on the progress that it is making, at the mid-point of the fiscal year, in achieving the goals and objectives that it presented in the Budget Statement. Through the Statement, Ministers report to Parliament and to the Bahamian people on the achievements being realized to date in their portfolios and, if necessary, request any additional resources that may be

required to permit them to attain the goals established at the beginning of the fiscal year. In this open and transparent way, this Honourable House has access to the facts and information required to examine the use and management of public funds and Ministers are accountable for answering questions on these critically important issues.

The preparation and presentation of the Mid-Year Statement is driving home to public officials the paramount importance of sound husbandry of public monies, through prudent financial management procedures and controls.

Modernizing Financial Administration

As we move forward and to further enhance good governance, it is vitally important to modernize our public financial administration and strengthen transparency, accountability and integrity in the collection and disbursement of public funds.

Towards this end, the Ministry of Finance is preparing a White Paper containing a number of proposals for the

modernization of financial administration taking account of developments since the Financial Administration and Audit Act was enacted in 1973. The White paper will be made available to Members of Parliament, senior officials and the public for review and comment. At the present time, while we expect the process of public consultations to be exhaustive, we do also expect it to be timely. As such, it is our intention to table a revised and modernized Financial Administration and Audit Bill during the course of this calendar year.

The template for the administration of public funds contained in the Financial Audit and Administration Act of 1973 is no longer adequate and or appropriate for present day Bahamas.

Improving the Efficiency of Government

A third key component of our strategy to strengthen good governance is the set of various initiatives that we have taken to improve the efficiency of Government operations and services to the public. We strive to reduce the burden on

citizens and businesses by streamlining bureaucratic procedures, reducing cumbersome application processes for permits, licences and registrations, eliminating unnecessary red tape as well as putting in place modern technologies for transacting with Government.

More specifically, in line with my Government's expressed commitment to Public Sector Reform, we launched a Service Improvement Programme in May 2008 which included six pilot agencies, namely: the Department of Public Service, the Registrar General's Department, Building Control, the Road Traffic Department, the Department of Physical Planning and the Passport Office. Initially, a survey was conducted to obtain the views of the public and employees with respect to the performance of these agencies. The findings confirm the widely held view that these agencies are highly bureaucratic and not very responsive to the needs of their customers and employees.

In response, Service Improvement Teams were established in each agency and tasked with the responsibility, in line with the survey results, of drafting Service Improvement Plans and Service Charters for their respective departments.

In order to further effect service improvement, the Department of Public Service has developed a number of initiatives, including a manual entitled “Code of Quality Customer Service” that will be given to each public officer. The pilot agencies’ Service Improvement Plans and Charters, as well as the new initiatives of the Department of Public Service are now being implemented.

Our task does not, of course, end there. We are fully committed to ensuring that improvements in public service and ethical conduct pervade each and every agency and department of Government. Reforms will be incrementally implemented throughout the Public Service.

Already, important reforms have been initiated in three critical areas, namely Immigration, the Police Force and Customs. In all three, we have streamlined the organizational and administrative structures and all will strive to modernize their processes and procedures to improve effectiveness, efficiency and service to the public.

With respect to Immigration, improvements have been mandated in all areas of operations that bear on applications for nationality, residency status and work visas. Renewed and sustained attention is to be given to policing and enforcing our immigration laws.

In Customs, new staffing and modern management systems are being introduced including a shift system that will greatly reduce if not eliminate high overtime payments. Lower overtime charges will provide clear benefits to citizens in the form of lower costs of imported products and will also contribute to the enhancement of the competitiveness of our tourism industry. As well, the entire spectrum of Customs

operations is under review to improve efficiency and service, and to capitalize on the introduction of modern technologies throughout the organization.

THE ECONOMIC CONTEXT

The Global Economic Outlook

Prior to reviewing the evolution of public finances in the first six months of the current fiscal year, I begin with a brief overview of the global economic environment, followed by a discussion of recent economic developments in The Bahamas and the near-term outlook.

We presently face the most challenging global economic environment that the vast majority of Bahamians have ever witnessed. One of the distinguishing features of this environment is not only the degree to which world economic conditions and the outlook have deteriorated, but also how quickly that has occurred. Another is the uncertainty surrounding the depth and likely duration of the global

economic crisis. What is especially daunting is that the responses or answers necessary to address these conditions have so far eluded world leaders in both the public and private sectors.

When I presented the 2008-09 Budget Statement to this Honourable House some nine months ago, prospects for real economic growth in the U.S., our dominant tourism and investment market, were still relatively buoyant, as evidenced by statements at that time by the G-7 Group of countries and the Board of the U.S. Federal Reserve System; and this despite the fact that the sub-prime credit crisis had already surfaced in 2007.

Of course, we now know that any signs of optimism that might have existed at that time have since dissipated and been replaced by predictions of unprecedented economic weakness around the globe.

Of equal if not greater concern to policymakers in all countries is the fact that conditions have recently continued to

worsen, seemingly at an accelerating pace. At the heart of current difficulties is the fact that an insidious feedback loop has developed between the crisis in financial markets and the real economy. Declining wealth for many, rising unemployment and a high level of uncertainty have adversely affected consumer and business demand and confidence. At the same time, disruptions in credit markets have reinforced the downward trend in spending.

In the space of under three months, between November 2008 and January 2009, the IMF has revised its forecast for global economic growth in 2009 downward to $\frac{1}{2}$ of a percentage point, down fully by 1.75 percentage points. Any recovery in 2010 is expected to be modest at best, with the timing and pace of the recovery depending critically on strong policy actions.

Projections for growth in the advanced economies have been sharply reduced. In the United States, real growth is now

expected to come in at -1.6% in 2009, down from +1.1% in 2008.

The outlook in 2009 for the other major economic regions is similar: the Euro Area economy is forecast to contract by 2%, this year, while that of Japan is expected to shrink by 2.6%. In China, some 70,000 factories have closed leaving millions without jobs.

It is clear that current depressed economic conditions and near-term prospects will present a huge challenge for governments and central banks around the world. The IMF estimates that a diverse array of policies will be required on the part of the major countries to address each and every component of the current crisis in order to support sustained economic recovery. Besides measures to stimulate demand, initiatives will critically be required to stabilize and unclog credit markets.

Domestic Economic Developments

It goes without saying that small open economies such as ours simply cannot and will not avoid being negatively impacted by this global economic and financial maelstrom. We have already felt the effects of a slowing world economy, and especially, rapidly deteriorating conditions in the U.S., where the unemployment rate rose in January 2009 to its highest level in 16 years. Almost 600,000 jobs were lost in the U.S. in January alone and 3.6 million since December 2007. More strikingly, about one-half of the total job losses occurred in the last three months.

The effects on Bahamian economic performance and prospects are evident and stark. At the time of the 2008-09 Budget Statement, we forecasted real economic growth of 2% in 2008 and 2.5% in 2009. I might add that these were, at the time, very modest and prudent projections, in comparison to the IMF forecasts for The Bahamas economic performance for those two years. The IMF projection for real growth in the

Bahamian economy in 2008 and 2009 was 4% and 3.8% respectively.

Domestic economic conditions were lackluster in 2008, especially so during the second half of the year. It was during the third quarter of 2008 that the negative effects of the global financial and economic crisis became entrenched in tourism and in anticipated foreign direct investment activities. After expanding 2.8% in 2007 and 4.6% in 2006 preliminary indications are that real GDP in 2008 was at best flat. Staffing reductions, largely concentrated in the tourism sector, and a stalled pace of job creation in the foreign investment-supported construction sector suggest an upward trajectory in the unemployment rate from the mid-year estimate of 8.7% in 2008.

The usual tracking of unemployment rates on an annual basis will not assist in better informing our interventions to address job losses. Hence, the Department of Statistics has undertaken a Supplemental Labour Force Survey in New

Providence and Grand Bahama, the results of which will become available sometime in mid-March as opposed to the end-of-year tracking results.

Based on data for calendar year 2008 the value of construction starts was ahead of that for the year 2007 in spite of reduced support from foreign investments, including an estimated one-fourth slowdown in net real estate purchases, which stimulate second homes development.

The value of building construction starts in 2008 of \$418.6 million was more than double the value of building starts in 2007 for a positive difference of \$219.4 million.

Some of the major projects that we had expected to support domestic growth have been stalled by the global financial crisis. As a consequence, the Government is implementing a public sector infrastructure stimulus programme to create jobs and cushion the effect of some of the job losses in other parts of the economy.

In essence, we will accelerate planned works to improve roads, docks and airports; expand school and community recreational facilities; and construct and refurbish Government offices.

The Government is arranging a loan of two hundred million dollars (\$200 million) from a consortium of banks which will provide funding for the stimulus programme and offset revenue shortfall in fiscal 2008/09. Legislation seeking the authority for this loan will shortly be placed before Parliament.

The progressive weakening in tourism activity has coincided with the deepening of the economic malaise in the United States economy, which accounts for over 80% of the total visitor count. During 2008, total visitor arrivals fell by 4.6% to 4.4 million relative to the same period in 2007, with the respective falloffs in air and sea traffic of 6.4 % and 3.8%. By country of origin, stopover visitors from the U.S. fell by 7.3%, and outweighed the combined net gains from other countries of

8%. Notably, given the respective strength of their currencies early in the year, stay-over traffic from Canada and Europe improved by 14.4% and 7.4%, respectively—representing a combined 14.3% of the total.

Hotel room revenues at properties surveyed by the Ministry of Tourism rose by 5.8% during the first nine months of 2008. This was due to a 9.4% increase in the average nightly room rate to \$220.58, which offset a 3.3% decrease in occupied room nights. The average room occupancy rate declined more significantly to 56.8% from 64.2%, also a result of the 9.2% rise in available room nights.

Some 1,200 jobs were eliminated in the hotel sector during 2008, and another 300 in 2009, and work weeks and work hours for many employees in the hotel sector have been reduced.

The other pillar of our services economy is facing a renewed threat from the major industrial countries as offshore financial jurisdictions again become the focus in the search for

solutions to the global financial crisis. Honourable Members will be aware that EU Heads of Government meeting in Berlin, Germany on Sunday past agreed that the extraordinary international crisis called for an overhaul of the international financial system including a new system of regulations for all financial markets, products and participants.

They again placed blame for the international financial crisis on ‘offshore jurisdictions’ or “tax havens” as they call us, where non-transparent business is carried out and promised to prepare a “toolbox of sanctions to be applied against such tax havens” which is to be presented to a summit of the Group of 20 developed countries meeting in London on 2 April.

We have a vested interest in protecting our financial services sector and so we will redouble efforts to ensure that we follow international best practices and cannot be correctly identified as an uncooperative jurisdiction.

As for other economic indicators, domestic inflation—measured by the change in the average Retail Price Index—

rose to 4.5% in 2008 up from 2.5% in 2007, influenced by the pass-through effects of the rising international price for oil, food and other commodities.

The pace of domestic credit expansion slackened to an estimated \$370.1 million in 2008 from \$691.4 million in 2007 – a decrease of \$321.3 million. Commercial banks registered a further deterioration in loan quality during 2008, as private borrowers experienced increased difficulties in servicing their obligations. The proportion of private sector Bahamian dollar loans in payment arrears of 30 days or more rose to 12.4% from 9.3% at end-December 2007.

During 2008, external reserves rose by \$108.8 million (24.0%), compared to a decline of \$45.5 million (9.1%) in 2007. The improved year-end position corresponded to an estimated 14.8 weeks of non-oil imports, higher than the 10.0 weeks at end-2007.

In light of the gravity of the global financial and economic situation the Bahamian economy will likely experience a modest contraction in 2009.

2008/09 BUDGET PERFORMANCE

In the 2008-09 Budget Statement a GFS Deficit of 2.1% of Gross Domestic Product was projected for this fiscal year. The GFS Deficit is measured as total government expenditure excluding debt redemption minus government revenues excluding borrowings. It provides a measure of the impact of the budgetary situation on the level of Government borrowing.

Since returning to Office, my Government has stated that it is committed to pursuing sound macroeconomic and fiscal policies that ultimately result in eliminating the GFS Deficit of 2.1% in 2005/06 and 2.5% in 2006/07 and progressively reducing the rate of Debt to GDP. This remains a cornerstone of our strategy to strengthen the fundamentals of our economy

and improve the standard of living of Bahamians. This was clearly our policy in the five years from 1997 to 2002 and we embarked upon that course again with the 2007/08 budget in which the GFS deficit fell from 2.5% to 1.7%.

However, as might be expected, the global and domestic economic environment and outlook do not now admit to a reduction in the GFS Deficit. In the circumstances of stagnant revenue growth, increased public expenditure and the difficulties and hardship being imposed on our economy and workers, my Government believes that the most appropriate course of action in the near-term is to absorb the current weakness in revenue and not to counter it with reductions in current expenditure. As such, there will be slippage from the 2.1% projected deficit GFS deficit in 2008-09 to a ratio which exceeds the 3% reached following the events of 9/11.

Because of the prudent policies The Bahamas is well-placed with a low level of Government Debt to GDP, one of the lowest in the Caribbean. As a result, we can cushion the effects

of the international turbulence upon our citizens, especially those in the lower income brackets without compromising our commitment to fiscal prudence. Honourable Members will recall that, in a recent address to this House, I described in detail the numerous tax exemptions and reductions and the social assistance measures that have been introduced by my Government.

However, it will be important for us to maintain steadfast vigilance over public finances in order to maintain our relatively favourable debt position going forward. In the near term, that means that the stimulus that we provide must be cyclical in nature and not lead to an increase in the Government's structural fiscal deficit. Over time, as global conditions recover and our economy resumes more buoyant growth, we will need to return to strong discipline over recurrent expenditures as well as an ongoing determination to properly collect all revenues rightfully due to Government

such that the path to our overall fiscal targets is securely restored.

In this Statement, we are making adjustments to Recurrent and Capital Expenditures but, importantly, we are committed to remain within the total expenditure limits already approved by Parliament for expenditure in fiscal 2008/09.

The Mid-Year Progress Report being circulated with this Mid-Year Budget Statement shows the progress for the first 6 months of the 2008-09 fiscal year, that is for the period 1st July to 31st December 2008 of Recurrent and Capital Expenditure and Recurrent Revenue. The purpose of the data is to enable this Honourable House to assess the progress made to date through the 2008-09 Budget across the whole range of Government spending and revenue.

The totals for expenditure and revenue for the first six-month period of the fiscal year must be viewed with caution as there are seasonal and other timing factors in play which will

only be eliminated when accounts are closed following the conclusion of the fiscal year. Accordingly, allowance must be made for these factors in analyzing the data.

Recurrent Expenditure

The data for the first six months of the 2008-09 Fiscal Year reveal that actual Recurrent Expenditure was \$72.8 million below the forecast.

The Supplementary Recurrent Expenditure provided for in this Mid-Year Budget Statement, amounting to \$30 million and Capital Expenditure amounting to \$15.6 million will be accommodated through reallocation of expenditure between Ministries, Departments and Agencies. I expect that notwithstanding these supplemental appropriations the total expenditure will remain within the level already approved by Parliament.

Recurrent Revenue

Total revenue collections for the first six months of the fiscal year amounted to \$626.5 million, down \$51.6 million

(7.6%) from the forecast. Despite this level of revenue weakness relative to forecast, it is noteworthy that total collections over the first six months of 2008-09 were largely in line with collections over the first six months of 2007-08. That in itself is remarkable in light of the economic environment that I set out above.

The principal revenue shortfalls from forecast occurred in respect of Import and Export Duties, which were \$39.1 million, lower than forecast. Other shortfalls occurred in Excise Tax, at \$18.1 million and Tourism Tax, at \$11.3 million. Modest gains over forecast were recorded in Real Property Tax, at \$7.1 million, Immigration fees, at \$8.7 million and Stamp Tax, at \$5.4 million.

Capital Expenditure

In the first six months of the 2008-09 fiscal year, Capital Expenditure amounted to \$92.4 million, up only slightly (\$1.8 million) from the forecast of \$90.6 million.

In my Mid-Year Budget communication last year I stated that the capital transfers to deficit-generating Public Sector entities was an unsustainable situation which needed to be addressed. I am pleased to report that Bahamasair is being held to its allocation of \$28 million in the budget, and so is the Broadcasting Corporation to its \$11.7 million allocation. Restructuring of the Water and Sewerage Corporation which accounts for \$11 million of the \$15.6 million of the Supplementary Capital funding being sought today will be undertaken so as to improve the efficiency in this corporation.

CONCLUSION

At the time of my address to the nation on the economy in early November, I recalled the October, 2008 advice of the IMF to Government's planning strategies to respond to the still emerging economic and financial crisis. That advice recommended that Governments develop various scenarios and plan responses to them. In that way, as the crisis develops,

appropriate and feasible responses would be at hand and careful consideration could be given to implementation.

It is obvious that there can be no broad single-stroke response to this global crisis but, rather, measured and incremental responses must be available as the crisis develops.

At the commencement of this Statement I outlined the global financial and economic crisis which is the background to these mid-year 2008/09 budget developments and challenges in our economy. My Government and our institutions with financial and economic responsibility – the Central Bank and the Ministry of Finance – are monitoring developments closely and providing data and analysis which is enabling my Government to ensure that the Bahamian economy takes maximum advantage of the turnaround, as and when it occurs.

We anticipate a visit by an IMF Article IV Consultation Mission by the end of March which can provide views on global developments and provide objective and independent assessment on the outlook for the Bahamian economy. As

initiated by a previous administration headed by me, the Report of the IMF Mission will be published. That Report will provide guidance on whether the global economic outlook is responding to the initiatives of the major economies.

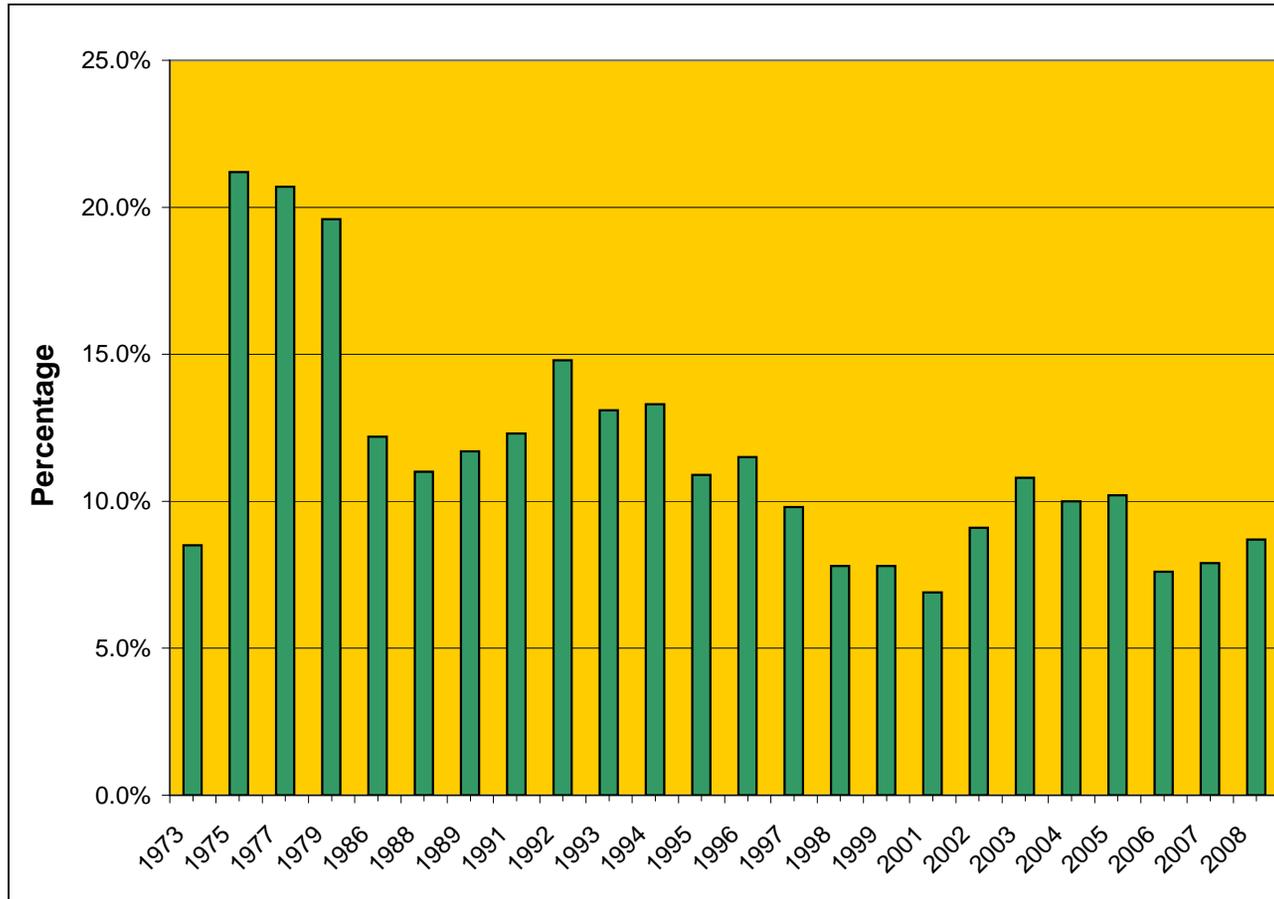
The Government is ensuring, with every means in its power, that the Bahamian economy is not stagnating beyond the level of the burden imposed by the global crisis.

I draw the attention of Members of this Honourable House to the tables and graphs included in the Statement which provide data on Unemployment Rates 1973-2008, Total External Reserves 1990-2008, Growth of the Bahamian and US Economy 1996-2008, Ratio of Foreign Direct Investment to GDP, and National Debt 1993-2008p.

I thank the Members of this Honourable House for their patience, and I have the Honour to present the Statement and the associated Bills.

25th February, 2009

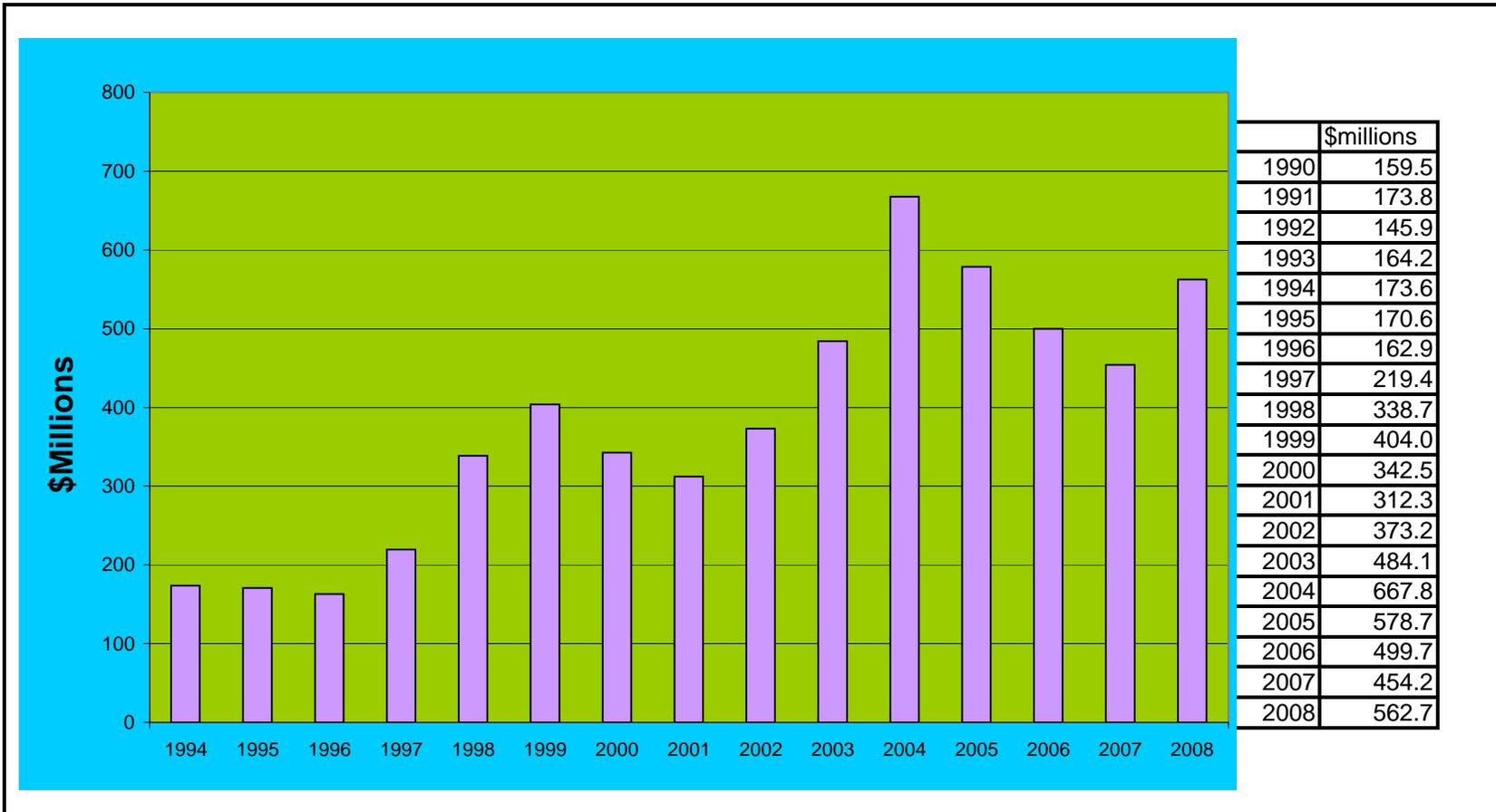
Table I - Unemployment Rates 1973-2008



	%
1973	8.5%
1975	21.2%
1977	20.7%
1979	19.6%
1986	12.2%
1988	11.0%
1989	11.7%
1991	12.3%
1992	14.8%
1993	13.1%
1994	13.3%
1995	10.9%
1996	11.5%
1997	9.8%
1998	7.8%
1999	7.8%
2001	6.9%
2002	9.1%
2003	10.8%
2004	10.0%
2005	10.2%
2006	7.6%
2007	7.9%
2008	8.7%

Source: Department of Statistics

Table II - Total External Reserves 1990 - 2008



Source: Central Bank Quarterly Statistical Digest, February 2009

Growth of the Bahamian and US Economy 1996 - 2008

Annual percent change in real terms

	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008
Bahamas	5.3	6.1	7.7	3.3	4.3	-0.3	2.1	-2.4	-0.2	3.3	4.6	2.8	2.0
United States	3.7	4.5	4.2	4.4	3.7	0.8	1.6	2.5	3.6	3.1	2.9	2.2	1.6

Source: Department of Statistics; IMF World Economic Outlook October 2008

Table III - Growth of the Bahamian and US Economy 1996 - 2008

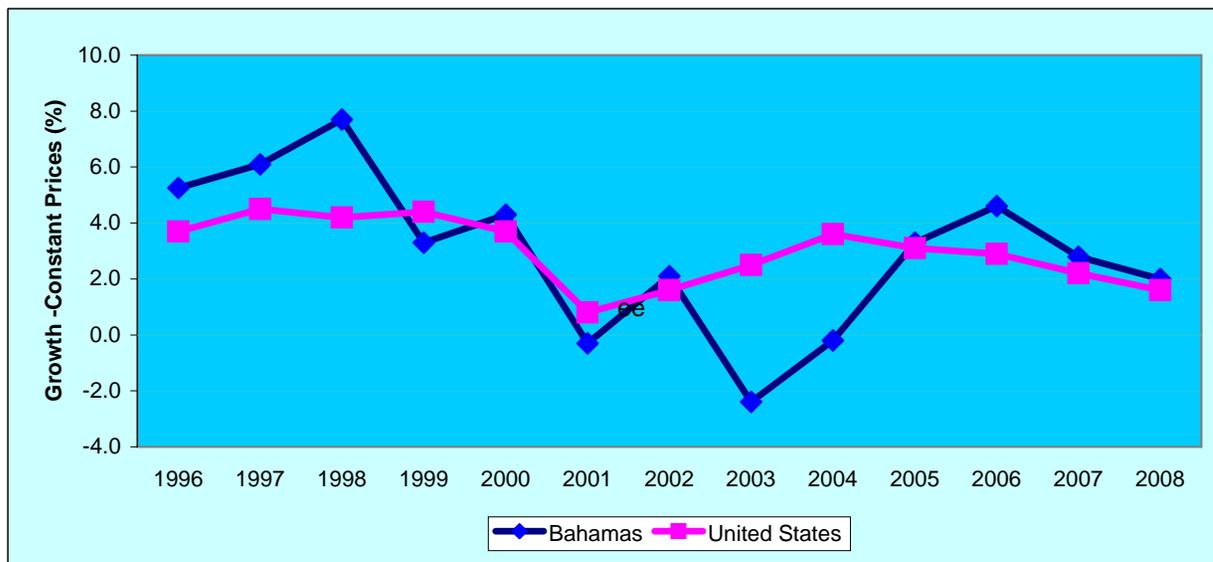
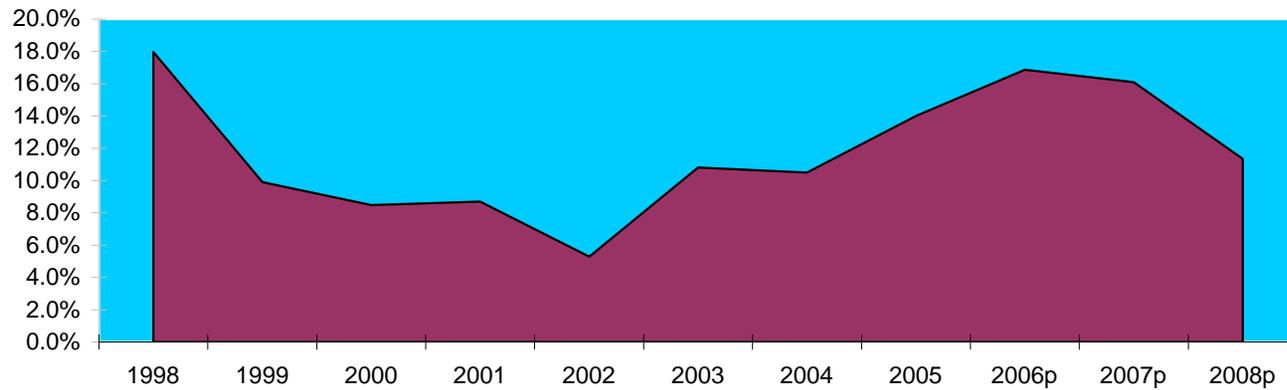


Table IV - Ratio of Foreign Direct Investment (FDI) to GDP
B\$ millions

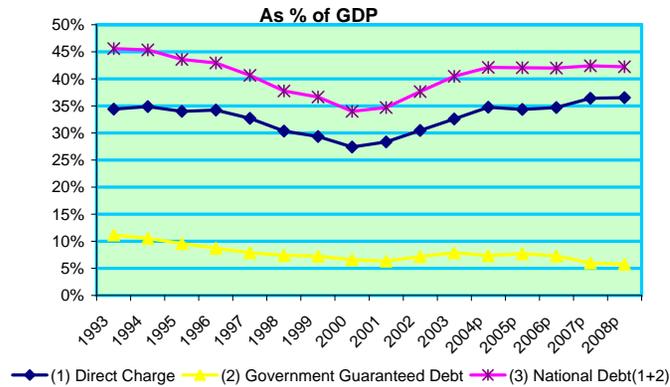
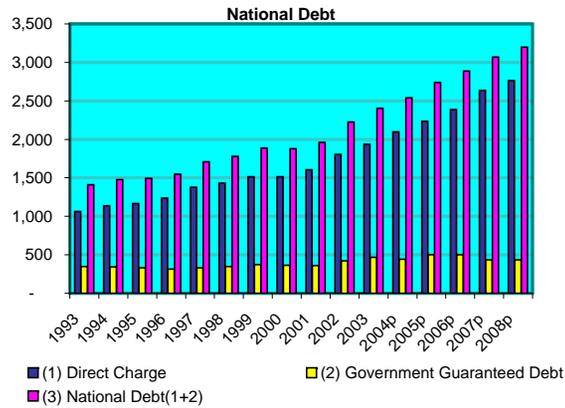
	1998	1999	2000	2001	2002	2003	2004	2005	2006p	2007p	2008p
Foreign Direct Investment	847.0	510.3	469.1	492.6	312.4	641.7	632.4	911.5	1,159.4	1,163.6	858.3
GDP(Current Prices)	4,714	5,150	5,528	5,659	5,912	5,942	6,032	6,509	6,876	7,234	7,572
FDI as % of GDP	18.0%	9.9%	8.5%	8.7%	5.3%	10.8%	10.5%	14.0%	16.9%	16.1%	11.3%



Source: The Central Bank of The Bahamas

Table V - National Debt

\$ millions	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004p	2005p	2006p	2007p	2008p
(1) Direct Charge	1,065	1,136	1,166	1,235	1,377	1,431	1,513	1,514	1,604	1,802	1,936	2,098	2,235	2,386	2,635	2,764
(2) Government Guaranteed Debt	346	343	329	314	332	349	374	365	359	423	468	442	502	501	435	436
(3) National Debt(1+2)	1,410	1,479	1,495	1,549	1,708	1,780	1,887	1,879	1,963	2,225	2,404	2,540	2,737	2,887	3,070	3,200
GDP(\$millions)Revised	3092	3259	3429	3609	4205	4714	5150	5528	5659	5912	5942	6032	6509	6876	7234	7572
As % of GDP																
(1) Direct Charge	34%	35%	34%	34%	33%	30%	29%	27%	28%	30%	33%	35%	34%	35%	36%	37%
(2) Government Guaranteed Debt	11%	11%	10%	9%	8%	7%	7%	7%	6%	7%	8%	7%	8%	7%	6%	6%
(3) National Debt(1+2)	46%	45%	44%	43%	41%	38%	37%	34%	35%	38%	40%	42%	42%	42%	42%	42%



Source: Central Bank Quarterly Statistical Digest February 2009