COMMUNICATION

BY

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DEPUTY PRIME MINISTER

AND

MINISTER OF FINANCE

DEBATE ON THE

2018 FISCAL STRATEGY REPORT

WEDNESDAY, 6th FEBRUARY 2019

OPENING STATEMENT

ON THE

2018 FISCAL STRATEGY REPORT

I. Introduction

Mr. Speaker,

In opening the debate on the 2018 Fiscal Strategy Report (FSR), I want to begin by reiterating the central point made by the Prime Minister when the FSR was tabled in the House. This document, which is mandated by the new Fiscal Responsibility Act 2018, does indeed stand as another historic achievement in the implementation of our Government's drive to fundamentally transform both public financial management and the public finances of our nation.

Later in my presentation I will go over the contents of the report in detail, including information about our macroeconomic outlook, fiscal forecasts, risk mitigation strategies and many other technical details.

But before we get carried away with the technical analysis, I want to make sure people understand what this debate is really about; what is the point of talking about a Fiscal Strategy Report and why should people care. It's important to put this in context because this exercise is new and historic for the Parliament and for the Bahamian public.

This document is all about how we plan to spend the people's taxpayer dollars. And I can assure you, **Bahamians want to know about that**!

In fact, every man and woman, on every island, wants to know, and deserves to know, **where their tax dollars go**. Everyone wants to know and, quite frankly, has a right to know, **how and why we make our decisions about the country's finances**.

As a Government, we might have the power to levy taxes, but we don't have a right to spend the people's money without appropriate public scrutiny and accountability. The former administration never learned that lesson, but today, we are going to show them better than we could tell them.

This Government promised to operate in the light of day, for better or worse, with full transparency, and we are setting that standard for all others to follow.

Today we will formally present and debate the Government's 2018 Fiscal Strategy Report, a public document that guides the creation of the annual budget.

Here is the reality: It costs a lot of money to run the country, and over the past few years, successive governments have had to introduce new taxes to build sustainable revenues to meet the demands. But, the former government taught us a painful and instructive lesson: It doesn't matter how much money you have – in fact, you could have a trillion dollar windfall – but, **if you cannot manage the money, it will never be enough**. **If you can't manage the money, you'll find yourself having more and doing less**. This is the people's frustration today: Why does the government have to cut back when it's making more money now than ever before?

Simply put, a country can't operate from strength when it is drowning in debt; it can't control its future when it can't pay its bills; it can't uplift its people if it can't stand on its own two feet. The country must stand upright and strong in its financial footing to deliver the tangible benefits and quality services that the people deserve.

Even our neighbours in the region have discovered, if we do not arrest the upward spiralling of the debt burden, our interest payments on debt alone will continue to take up more of our revenue dollars, leaving us unable to devote those dollars to areas that could actually stimulate growth in our economy, improve public infrastructure and government services, and provide jobs for Bahamians.

It's no different from an ordinary person working to manage their money: When money is flowing on a regular and consistent basis, and you have financial stability that gives you the freedom to think about the future. When you can comfortably pay your bills; and you are not ducking people you owe, you have enough flexibility to take care of your needs and to invest in your wants and dreams. But, when bills are piling up and the debt collectors are calling, money come, money go. You have less freedom, less flexibility, less choice. In fact, other people start dictating the terms of your life. They remove you from the head of your own table.

Many Bahamians can relate to the feeling of ducking someone who you owe money to, when you know you cannot pay. When someone is so deep in debt or their spending habits are so out of control, not even a steady income or a pay increase can help. The money will fly out so fast it would feel like the pay increase never even happened. Instead you feel trapped, out of control, and filled with regret, when you think about all the things you **should have** done and **did not do**; all of the things you should **not** have done and **you did**.

In times like these, sometimes you just have to look yourself in the mirror, (and if I may use a colloquial expression), you have to check yourself. **And in simple terms, our fiscal strategy is to put the government in check and to keep the government in check.**

In other words, we will balance the budget; restore order to public finances and strength to the Bahamian people.

When we came to government the first thing we had to do was acknowledge that the country's financial affairs were in shambles; that we could not live in the land of denial and flam out way to success. To deliver for the people we had to put first things first and get the country back on its feet: Standing upright and strong. That meant getting the Government's expenses under control; that meant putting a plan in place to balance the budget; that meant putting money aside, little by little, for those rainy days.

Further, we had to put safeguards in place to limit the fiscal damage any one government could cause. In a functioning system, tax payers should not have to work harder to make up for the mistakes of public financial mismanagement. So, we are putting tremendous effort into building systems of transparency and accountability. We are putting laws in place to limit the Government's spending; to require regular reporting; and to ensure there is public scrutiny.

By putting the government in check, we are setting ourselves up to deliver a stronger economy, more meaningful benefits and quality services to the Bahamian people now and in the future.

With that being said, I want to stress at the onset that this debate is not taking place in a vacuum. The rationale and the aspiration of the FSR are created in the context of the Fiscal Responsibility Act. It is that landmark piece of legislation that states what information should be in the FSR, that it should be published in November; that it should be debated by Parliament; and many other requirements. It is in the context of the landmark fiscal responsibility legislation that the government strategically committed to:

- ➢ Openness, transparency and proper and accurate fiscal planning and reporting
- ➢ Achieving and maintaining a balanced budget
- ➢ Keeping the growth in expenditure in check
- ➢ Reducing the debt burden; and
- ➢ Facilitating consistent public scrutiny of the public finances and its ability to act as a check on the tendency for the burden of government to grow in an ad hoc way.

For the benefit of this House and Bahamian citizens I will walk you through the requirements of the law and the contents of the 2018 Fiscal Strategy Report, explaining, more specifically, how our fiscal strategy and its strict adherence to fiscal discipline will benefit the Bahamian people.

In a nutshell, the simple benefit is this: no strategy means no results. You may have heard the saying, "a man without a plan plans to fail", and that is precisely what would happen if this government did not have a strategic plan for how it would remediate its fiscal woes. An established fiscal strategy – and the report that documents same - ensures that we have the proper foundation for economic growth and stability over the long term, by setting a plan for eliminating the fiscal deficit and reducing the debt burden to a sustainable level.

When we get our fiscal affairs in order, we create room for spending to be used for capital needs, such as infrastructure, that creates jobs for individuals. In fact, a three year capital expenditure plan is currently in the works, that seeks to take a hard look at capital projects that are already developed, those in the pipeline, and those not yet developed to see how best we can accommodate them into our medium term plan, with the aim of garnering fruitful, and sustainable improvements in national productivity and economic growth.

Our model of good governance stands in stark contrast to the approach of the previous administration. Indeed they incessantly talked a good game about the critical need to curtail and eventually eliminate the deficit and reduce the debt burden to lower, more desirable levels. However, their promise to strengthen fiscal transparency and accountability, as well as their well-laid plans to reduce the fiscal deficit, invariably and miserably failed to materialize. As a result, under their watch, the overall fiscal position was in persistent deficit, leading to unsustainable levels of Government debt and posing serious consequences for our economic stability.

II. The Fiscal Responsibility Act

Mr. Speaker,

Our approach to enhancing fiscal responsibility, both in legislative terms as well as in concrete terms was first exemplified by our actions in the 2018/19 Budget.

The fiscal plan laid out in the 2018/19 Budget Communication contains the concrete measures needed to secure the elimination of the fiscal deficit by 2020/21 and to put the debt burden on a clear downward track to more sustainable levels.

And, in order to secure these fiscal gains, we developed and introduced the Fiscal Responsibility Act, as I referenced earlier, that came into effect on October 1st of last year. The Act provides a strong, depoliticized institutional framework for fiscal policy—so as to ensure that no future Government ever again engages in flagrantly irresponsible fiscal policies that could once more threaten the future prosperity of our nation. To this end, the Act contains legally binding fiscal rules that place limits on the annual fiscal balance and the debt-to-GDP ratio.

The Act provides for regular and explicit fiscal reporting for public and parliamentary scrutiny and also an independent mechanism for assessment of compliance with the fiscal responsibility principles and objectives and for the provision of advice. To that end, the Act provides for the establishment of an independent, private sector Fiscal Responsibility Council (FTC) that will be responsible for assessing the Government's compliance with the general principles, fiscal responsibility principles and fiscal objectives of the Act and advising on fiscal and budgetary matters of the Government. The FRC is to be established in July 2019, in time to review and assess the 2019/20 Budget.

I fully expect it to be a very active and constructive participant in the FSR review process beginning with the second FSR in November of 2019.

In order to enhance fiscal transparency and accountability on a timelier basis, the Government has also initiated the publication of quarterly fiscal performance reports, with the most recent report—the second of its kind—having been published last week for the first half of the 2018/19 fiscal year. We produce these reports not because there is a law that compels us to do so. We produce these reports because it is simply right to keep Bahamian tax payers informed on how their government is earning and spending their money.

Mr. Speaker,

Without overstating the case, this new quarterly fiscal report is yet another historic milestone on our march toward enhanced, transparent and accountable fiscal management in The Bahamas. We have committed to providing this information in formats that are accessible and understandable to all Bahamians. The enhanced communications we have adopted at the Ministry of Finance have made this possible.

III. The Fiscal Strategy Report

Mr. Speaker,

Under the Act, the preparation of an annual Fiscal Strategy Report (or FSR) is intended to guide the preparation of the annual Budget and must provide information on:

- the long term macroeconomic forecast;
- the assumptions and methodologies underpinning such a forecast; and
- medium term fiscal forecasts setting out actual, estimated and projected values for key fiscal variables for the two previous years, the current year, and the next three years.

The FSR incorporates information on the fiscal policies for the medium term, including the expenditure policy and the profile of capital expenditure; the revenue policy; the policy on the fiscal balance and the debt management policy. The FSR provides as well an assessment of the extent to which the fiscal performance of the Government is consistent with the fiscal responsibility principles and the fiscal objectives in the Act. Finally, the FSR discusses quantified risks to the forecast and risk management intentions.

The FSR is to be presented to Cabinet no later than the 1st Tuesday of November of each fiscal year. Once approved by Cabinet, and no later than the 3rd Wednesday of November, the Minister must submit the FSR to Parliament and to the Fiscal Responsibility Council (FRC). It must also be published at that point.

Parliament is then to debate the FSR and inform the Minister no later than the 31st day of January of any recommendations on the report. The Minister may amend the FSR, as applicable, and table it in Parliament, and then publish it on the Government website. The FSR will then set the parameters for the preparation of the annual Budget.

In this regard, this year's FSR highlights areas in which the analytical capabilities of the Ministry of Finance will need to be significantly strengthened in the period ahead. The Ministry of Finance is, for example, in the process of strengthening its internal analytical capabilities in macroeconomic and fiscal modeling and forecasting. This initiative, together with planned enhanced collaboration with key agencies, such as the Department of Statistics and the Central Bank of The Bahamas, will enhance the Ministry's ability to more fully satisfy the reporting and forecasting requirements of the Act in respect of future Fiscal Strategy Reports.

It should also be noted that the budgetary data presented in the FSR are prepared using a modified cash basis of accounting and guided by International Public Sector Accounting Standards (IPSAS). The data is also presented using the new chart of accounts introduced on July 1, 2018, which prepares for the eventual conversion of the accounting presentation to the IPSAS accrual basis. The Government is committed to moving to the accrual method of accounting and has commenced a comprehensive public financial management institutional strengthening initiative which includes the implementation of new budgeting and accounting software and standards, and the supportive systems.

The 2018 FSR is divided into four (4) sections in compliance with legislative requirements, as follows:

1. a report on economic and fiscal performance in the most recently completed fiscal year, namely 2017/18;
2. a macroeconomic and fiscal forecast for the current and next three fiscal years;
3. the proposed fiscal policy for the next three fiscal years, including key Budget priorities; and
4. an analysis of risks and mitigation strategies.

There is also a discussion of debt management policy in Annex A.

Briefly, the FSR notes that, in 2017/18, the economy performed in line with the forecast presented at the time of that year's Budget. However, it also reveals that fiscal performance in 2017/18 was somewhat weaker than budgeted, with the GFS deficit posting a slippage to a level of $415 million relative to the forecast of $320 million. The deficit equated to an estimated 3.3 per cent of GDP, compared to the forecasted 2.6 per cent. That, however, is still a sharp improvement from the $661 million budgetary shortfall in 2016/17, which represented 5.5 per cent of GDP. We will review these details again in the context of the Mid-Year Budget review.

Mr. Speaker,

Notwithstanding the fact that the details of the current and most recent budget outturn will be addressed during the mid-term budget, I do want to speak briefly on the $95 million overrun against the original budget forecast. We acknowledge that our forecasting for expenditure patterns and our budgetary management should have allowed us to pick this up when we presented the budget in May.

However Mr. Speaker, the reality is that this poor forecasting is not a new phenomenon. When we examine the last five budget years of the previous administration, we see the same exact pattern. The former Minister of Finance came to Parliament during the Budget debate with a forecasted budget deficit - and invariably the final deficit number would end up being larger – usually much larger. For example, this is what has transpired over the last five budget cycles:

- In Fiscal Year 2013/14 the former Minister of Finance during the budget debate projected a deficit of $462 million and the deficit ended at $488 million - for a slippage of $31 million against the projection.
- In 2014/15, during the Budget debate the projection given was for a $198 million deficit, and the end result was $381 million deficit for a slippage of $183 million.
- In 2015/16, the projection was a $150 million deficit and the outturn was a $310 million deficit, for a slippage of $160 million

- In 2016/17, the projected deficit was $500 million at budget time and the final deficit was $661 million, for a delta of $161 million.

- This past May, I had had projected a deficit of $310 million, but ended at a deficit of $415 million for slippage of $105 million against the May projection.

Again, I want to make clear that this is not a comparison between the original budget forecasts and the end result. These are the slippages based on projections given during a budget speech that is done 10 months into the fiscal year when forecasts should be fairly solid.

Mr. Speaker, I can bet that Members opposite will seek to make great hay out of the most recent slippage - of course conveniently forgetting that during their most recent term in office the very same thing happened every single year. They lived it and did not see fit to comment on it at the time. Worse, they did not see fit to correct these chronic shortcomings.

But we are different from them Mr. Speaker. We have recognized the challenges that we have both in budget forecasting and in expenditure management and we are owning up to it. For many, many years, what has happened is that there is an end of year rush to meet spending commitments that ought to have been better planned throughout the year. Further, there are postings and settlements that ought to be accounted for in forecasts and were not. This has been the state of play for some time. And the net result of this is that our forecasts end up being meaningless. But I am pleased to inform this House that – like with so many other things – this administration is fixing it.

To this end, Mr. Speaker, this government continues to give priority focus to strengthening public financial management arrangements, so as to deal effectively with the fiscal risks posed by the government not discharging its payment obligations in a timely manner. Simply put, we are endeavoring to pay our bills on time.

We have taken responsive and targeted initiatives to identify, report on, and clear arrears, and implemented steps to strengthen expenditure controls so as to avoid an accumulation of new arrears. This fiscal year, we have begun monthly agency budget meetings, to assess developments with respect to budgeted spending. We have implemented better control and recording of payment commitments, as well as more effective cash management and forecasting. We will shortly be introducing the requirement for of monthly spending plans by agencies. In combination, these measures are intended to ensure that the Government remains on top of what is happening and they support confidence in our fiscal policy stance. Going forward, when we make these kinds of forecasts during the budget debates when the fiscal year would have been more than three quarters complete, all can be assured that – barring the truly unforeseen – the forecasts will prove much more accurate.

Moving on to the macroeconomic and fiscal forecasts for the current period through 2021/22: The forecasts in the FSR largely correspond to the positions set out in the 2018/19 Budget Communication. That projection incorporated the various policy measures announced in the Budget, including those geared to securing the attainment of the fiscal objectives in the Act, and it now serves as the so-called "status quo" fiscal outlook going forward for the purposes of planning for the 2019/20 Budget. The macroeconomic forecast for The Bahamas has been updated to take into account the October 2018 release of the IMF World Economic Outlook, which remained unchanged in the most recent IMF update released just last week. Of note, the rate of real economic growth has now been shaded down only slightly in both 2018 and 2019, by 0.2 per cent and 0.1 per cent, respectively. Real growth in 2018 is forecast at 2.3 per cent and, in 2019, at 2.1 per cent. This largely reflects somewhat softer projected growth in the U.S. However, forecasted inflation this year and next is now somewhat higher than previously projected. As a result, the growth of nominal GDP is now expected to be higher in both 2018 and 2019 than had been projected in the May Budget.

The Budget fiscal projection was extended to 2021/22 by assuming that:

- primary recurrent expenditure grows by 2.5 per cent that year, the same rate as in the two previous fiscal years; and
- recurrent revenue remains around the 20 per cent level of GDP attained in 2018/19.

As well, the FSR asserts that it is the intention of the Government, as an overriding guiding principle, to maintain the level of recurrent expenditure at no more than 20 per cent of GDP through the medium term fiscal planning horizon.

In addition, the medium-term forecast incorporates a modest enhancement in capital expenditure in line with the priority that the Government attaches to strengthening and expanding public infrastructure in support of stronger economic growth.

On the basis of these planning assumptions, it may be seen that a further small budget surplus, amounting to 0.1 per cent of GDP, is projected for 2021/22. This follows a deficit of 1.8 per cent of GDP in 2018/19, a deficit of 0.8 per cent in 2019/20 and a surplus of 0.1 per cent in 2020/21. As a result, the debt-to-GDP ratio declines steadily from its peak of 57.8 per cent of GDP in 2017/18 to 52.4 per cent of GDP in 2021/22.

As for the section of the FSR dealing with Budget priorities and the fiscal strategy for the next three fiscal years, it makes clear that the priorities for the 2019/20 Budget will necessarily need to be framed such as to respect and reinforce the actions and positive results of the 2018/19 Budget. These priorities will also continue to be inspired by the Government's 2017 Manifesto and the Speech from the Throne (SFT), both of which delineated the full policy agenda over the course of the mandate. The key themes of that agenda are as follows:

- Promoting investment and entrepreneurship
- Investing in Digital Government initiatives both to galvanize citizen and private sector engagement and secure operational efficiencies
- Enhancing the growth of the tourism sector throughout the archipelago

- Investing in enhanced education and training
- Investing to improve and strengthen the health care system
- Supporting renewable energy and securing environmental sustainability
- Ensuring safe and secure communities
- Promoting the self-sufficiency of the State-Owned Enterprises
- Expansion of social services and assistance and revitalization of heritage communities
- Promotion of growth opportunities for the Grand Bahama economy

In addition, the 2019/20 Budget will need to address the other fiscal pressures that are on the horizon, as described in the last Budget. These include:

- the need for further reform of the tax system, to cover the elimination of distortions in the import tax regime to better align The Bahamas' tax system with international best practice; to achieve convergence with EU and OECD requirements, including the removal of so-called ring-fencing, and to ensure that any incentives or preferential treatment is linked to significant activity in The Bahamas.
- the need for ongoing modernization of the major tax agencies—including Customs and Real Property Tax.
- the need to implement the required reductions to Customs/Excise duties upon accession to the World Trade Organization, likely beginning in 2020 upon the completion of negotiations and the passage of requisite legislation.
- the desirability of reviewing and assessing the adequacy and effectiveness of the current tax concession regime.
- addressing critical public infrastructure needs to support stronger economic growth and desirable advances in productivity, and the role to be played by PPPs in meeting these needs.

- ➢ the establishment of a Disaster Relief Fund, over the medium-term horizon, to mitigate against fiscal risks posed by weather-related events.
- ➢ addressing the issue of public sector pension reform, which poses a major burden on the sustainability of the public finances.

The FSR reiterates the Government's firm commitment to the implementation of some $100 million in duty and excise reductions in the context of the three-year fiscal strategy that was set out in the 2018/19 Budget. These reductions will be designed to advance the objective of rebalancing the tax burden between the provision of goods and services and reduce the attendant distortionary impacts. They will also accommodate the reductions in import taxes attendant upon accession to the WTO.

As I mentioned, the framing of the next Budget will need to address several important policy and fiscal pressures, central of which is the need to further implement the key priorities in the Government's socio-economic growth strategy. In that context, it will be noted that the medium term fiscal outlook set out in the FSR does provide the Government with some much-needed fiscal room to manoeuver, relative to the legally mandated fiscal objectives in the Act. Indeed, the law stipulates that annual deficits shall not exceed 0.5 per cent of GDP as of 2020/21 and beyond. As such, should the Government so choose, it could avail itself of that fiscal room to finance high priority policy initiatives. It also bears noting that, even with annual deficits of 0.5 per cent of GDP, should the Government so choose, the debt-to-GDP ratio would still continue to decline steadily, though more gradually, toward the long-term goal of 50 per cent of GDP. For planning purposes, the FSR states that the Government will seek to attain that objective by the 2024/25 fiscal year.

IV. CONCLUSION

Mr. Speaker,

In closing, I would simply reiterate the truly ground-breaking and historic nature of the 2018 Fiscal Strategy Report that we have before us. I firmly believe that this annual document will serve to greatly enhance the transparency and accountability of this and future Governments in respect of the management of the fiscal affairs of our nation.

It is important Mr. Speaker that persons do not seek to analyse the FSR by what it is not. It is not a document on economic policy that speaks to or lays out the government's economic plan. That will be the temptation of some – to point out with great fanfare that there is no discussion of the specifics of an economic plan. That is not what an FSR is about. The law that gives life to the FSR lays out very specifically what is to be in the report. It is to speak principally to the government's budgetary and financial plans and how these plans impact the deficit and debt. It is on this basis that the FSR should be assessed.

Indeed, the overriding objective of the FSR is to open up the Budget process in order to strengthen the development of responsible fiscal policies and promote the attainment of better outcomes going forward. As the Fiscal Responsibility Act makes clear, Parliament has a vital role to play in this regard. Accordingly, I look forward to a vigorous and healthy debate on this year's FSR in the period ahead.

As for the Government's fiscal strategy itself, **we are going to restore order to public finances and strength to the Bahamian people.** By putting the government in check and keeping the government in check. That means no more runaway trains leading the country to the fiscal brink. All governments will have to plan ahead, as we are; they will have to be transparent, as we have demonstrated; and they will have to accountable to the people every step of the way.

The Bahamian people are tired of the mismanagement. They are tired of having to wait for their basic needs to be met. They are tired of having to put their dreams on hold because the government cannot get it together. **We recognised this on day one and decided to look in the mirror and say, let's put the government in check.**

The Bahamian people deserve to know what abundance looks like, what prosperity feels like. Now imagine a Government committed to delivering a surplus, which means, not having **just enough**, but having **more than enough** to invest in the basic needs of the people, **AND** their hopes and dreams.

Ultimately, that is the fiscal **vision** underpinning our fiscal strategy. In the future we envision a government in surplus; a government with more than enough to freely invest in all of its people, across each and every island.

We are not close to a surplus as yet, but the steady march forward will continue and must continue.

If you eat right in the first place you don't have to worry about going on an insufferable diet. If you get your annual checkups and stay on top of your health you don't have to worry about crippling medical bills getting sick from something preventable. The lesson here is to put first things first, and our strategy is to do just that: We are going to restore order to public finances and strength to the Bahamian people.

As I sit Mr. Speaker, I want to congratulate my team at Finance and at DIR in particular, on the fantastic and laudable improvements being reported in the efficiency of the business license process this year. Turnaround times have been improved from application to issuances of licenses to as little as 24 hours in some cases and most within 48 hours. Indeed a remarkable improvement on the two weeks to four week runaround period of the past. I want to recognize them and thank them for the creativity and commitment they have shown thus far, and to let them know, the public has taken note and singing their praises. Keep it up!