Keynote Address

by the Hon. K. Peter Turnquest, Deputy Prime Minister and Minister of Finance

National Conclave of Chambers of Commerce in The Bahamas

Thursday, 14 June 2018

"The Bahamas: A Global Enterprise"

[PROTOCOL]

Good Morning,

I extend my sincere thanks to the National Conclave of Chambers of Commerce in The Bahamas for the invitation to address you today. This is a timely occasion to meet with the business community and all of the stakeholders present, as the country undergoes this period of change and transformation.

The Chambers of Commerce in The Bahamas have always played an important role in supporting private sector growth, and you continue to do so today. I congratulate you on all of your continued initiatives and look forward to the projects you will undertake in the latter half of this year.

Your theme - "*The Bahamas: A Global Enterprise"* - is also timely given the current discussions about The Bahamas' ascension into the World Trade Organisation. Many of you, no doubt, have participated in the public consultations with the Ministry of Financial Services, which would have given you an opportunity to share your views on key negotiating points for the government's accession. Consultations continue for those of who have not yet participated.

The Government is aligned in its thinking that the country must regard itself as a global entity. Not only because of the global strength we have in our two primary export markets - tourism and financial services - but also because of global trade liberalization, and the market disruptions of digital technology. In no sector can we afford to be insular in our thinking or practices. As employees, as entrepreneurs, as business owners, and as a government, we must see ourselves as global participants and must strive to be globally competitive.

Given our fiscal state of affairs, we simply cannot have a discussion about The Bahamas as a global enterprise without speaking about the Government getting its fiscal house in order; without speaking about the Government's fiscal consolidation plan and socio-economic transformation agenda. So, I will utilise my time today to speak about both, and how they relate to one another.

THE BOTTOM LINE

There is no doubt that our country is facing extraordinary and challenging circumstances, due to the state of our public finances. And, to the extent that we permit the past practices of fiscal indiscipline and fiscal mismanagement to continue, and not take decisive steps to alter the current course, we run the certain risk of undermining the stability and viability of the Bahamian economy.

Far from being an exaggeration, our fiscal realities have been signaled by the international multilateral institutions and credit rating entities as worrisome trends that need to be corrected. Debt levels have been continuously climbing for the past ten years—increasing by 160%

between 2008 and 2017. At $1.09 billion, debt service today is 8.3% of GDP. Just last year, interest on the debt increased by $89 million.

If left unaddressed, these trends have the potential to trigger further credit downgrades, which would increase borrowing costs for The Bahamas, severely hamper the economic prospects for local businesses, and make the economy less competitive and attractive to investors.

We are not the first country to find itself in this circumstance – with millions in government arrears, massive levels of debt, growing interest rates, and a bond rating at junk status – and we will probably not be the last. But we have the benefit of observation, analysis and the opportunity to make strategic changes that will place our economy on a more positive track.

It was not long ago that The Bahamas experienced its own sovereign credit rating downgrade. Under the previous administration, The Bahamas went through four downgrades to the point where our credit rating went to what is commonly referred to as JUNK status. We were a country that, as late as 2011, could boast of an A3 rating by Moody, which is in the upper echelon of investment grades. Now we have been relegated to the remedial classes - with a negative outlook by some other agencies.

And to be sure, it is not just about the embarrassment and hit to our reputation that this junk status has brought. It has real financial implications. The most recent downgrade in 2017 triggered margin calls on certain derivative transactions the government had engaged in to hedge currency and interest rate risks on its debt.

As a country intent on improving its competitiveness in the global community, The Bahamas simply can't afford to have more downgrades on account of a weak fiscal position. This is a price none of us can afford to pay.

We have studied what happens to countries that delay their inevitable day of reckoning for political expediency: Their economic woes snowball into a full-blown economic crisis; they face currency devaluations and crippling borrowing costs. We have watched how government inaction has only quickened the crawl towards a fiscal point of no return. We have seen how the failure to act decisively and with determination has forced countries to bow at the feet of international debt collectors and credit rating agencies.

This Government has no intention of leading The Bahamas down that path, and we are prepared to make responsible choices, no matter how politically unpopular, to avoid such a fate. The corrective actions we are undertaking with the 2018/19 fiscal plan might be hard and painful and require shared sacrifice, but they are necessary. And they are made on our terms, not by the dictates of external actors, whose mercy we must subject ourselves to.

As I mentioned earlier, our economy is not in an economic crisis today. In fact, our economy is in a state of economic recovery, which is confirmed by data from the Central Bank, the Department of Statistics and reports from the International Monetary Fund. Last year the economy grew by 1.4 per cent on the back of the much-awaited opening of the Baha Mar resort and a stronger U.S. economy.

The most recent IMF report noted that without resolute implementation of structural reforms, medium-term growth would be subdued. The Government's cost containment efforts last year improved our fiscal balance, but our fiscal deficits remain above debt-stabilizing levels. Without policies to ensure fiscal sustainability, The Bahamas risks losing its economic gains.

I hope I have set the context for the government's fiscal decisions in clear terms because addressing these matters goes to the heart of our global competitiveness and economic prosperity. They sit at the foundation of our fiscal plan.

BUDGET DECISIONS

To address the state of fiscal affairs, the government attached critical priority to fiscal consolidation and took the decision to raise additional revenue through increased taxation as well as enhanced revenue collection measures.

On the expenditure side, we intend to continue our trend of **fiscal constraint**. In the budget, 24 of the 53 Heads, excluding interest payments, saw reductions in their budget allocations, and 3 were given an increase under 1.5 per cent. For the expenditure allocations, we focused on the areas of highest priority within our **socio-economic transformation agenda**: investing in new initiatives to advance inclusive growth, social progress, economic empowerment, environmental sustainability, public sector reform and modernization.

We appreciate that we have to get the cost of government down, but that cannot happen overnight, without causing major disruption and possibly pushing the economy into recession. We have started that process, and our digital government projects will assist greatly in that effort. In the budget, we allocated $8 million for "**Digital Bahamas**" to transfer more government services online, to streamline government processes and improve the ease of doing business. With monies coming in faster to meet government expenditures we can reduce our reliance on overdrafts and other short-term borrowing facilities.

We are also building training programs to help transition the civil service and contract workers off the public register. The **Central Government's wage bill** is the single largest recurrent expenditure at $793 million.

The government is currently the largest employer in the country, but as we improve the competitiveness of the workforce and reduce the size of government, we hope to change this, and place the responsibility for job creation, innovation and GDP growth where it belongs, on the private sector. Our **economic driver equation is upside down** and we need to correct it. The government should take its rightful place as a regulator of the economic space, providing the enabling environment for a healthy private sector and as a service provider of last resort, rather than an employer.

This too takes time: It requires structural adjustments and it also requires a cultural shift. I am confident that together we can overcome, fix the wrongs and build a better, stronger and efficient government machinery, but it does take patience, discipline and sacrifice. Our $2.6 million investment in full-scholarships for BTVI students will advance this effort by raising the skill level while increasing the competitiveness of the Bahamian workforce.

The incentives offered to the business community, we hope, will also stimulate new investments and job creation. The **Commercial Enterprises Act** is already seeing success in driving new foreign direct investment, or FDI, and job creation. The multi-million dollar investment of GIBC Digital in Grand Bahama will have an estimated economic impact of over $10 million in the first year, creating 50 new jobs. Further, GIBC has expressed plans to expand its Bahamian operations to over 150 employees and build a state-of-the-art, sustainable Data and AI center within three years, bringing an economic impact of $50m by 2020.

Then there is the **Economic Empowerment Zones Bill, which, when enacted,** will first be applied to the Over the Hill community to bring rejuvenation and economic empowerment to this neglected area. In the budget, we allocated $5 million to foster a culture of entrepreneurship so more Bahamians can create their own jobs. This will empower micro, small and medium-sized enterprises, who continue to be the backbone of the business community. This effort is in collaboration with the Chamber of Commerce who we know will work with the Government to ensure the project's success. We call on the various chambers to educate their stakeholders about the government's initiatives that will empower them.

The Government is also working to improve the performance and revenue yield of **state owned agencies**, or SOEs, reducing the cost to government over time. Twenty-three (23) SOEs account for 15% of the government's total expenditure. This is unacceptable. In light of the critical priority being attached to fiscal consolidation, such a drain on the public finances must clearly be rationalized. The Government has already directed each SOE to move toward a cost-recovery operating model, which might include a mix of revenue enhancement initiatives, as well as measures to reduce expenditures in-line with industry benchmarks. The SOEs are now articulating strategies that we expect will take them to this optimized point within 3 to 5 years.

Can more be done to rationalize expenditures, reduce the cost of government, and support job growth? Yes, of course, but we believe we have made a good start, and our efforts continue. The budget is not just about taxes, no matter how controversial the government's taxes might be. The Government has implemented a range of measures on the expenditure side to improve efficiencies, reduce costs and to transfer those responsibilities that belong with the private sector to the private sector.

With the achievement of a balanced budget in three years, we can start to repay the massive debt we have, invest more in job creation activities and infrastructure, lower the overall tax burden and address the myriad of social and civic issues we face.

On the revenue side, moving to significantly enhance the revenue yield of our tax system was not done capriciously but rather out of a deep sense of responsibility for righting the ship of state and restoring the fiscal health of the Government.

I only need five numbers to explain our fiscal state of affairs:

1. **7.2 billion:** Total debt.
2. **$381 million**: Cost of interest payments on the debt for the upcoming fiscal year. That means, 14% of total revenue goes towards interest payments: In other words, 14 cents out of every dollar earned.
3. **$360 million:** Accumulated arrears from successive governments. We uncovered these after several budget calls this year, and in the budget we published a transparent list of the various large and small contractors. And just to remind you, last year we had to repay a separate $400 million in unpaid bills incurred by the former administration alone.
4. **$76 million:** Previously under-budgeted commitments that were also uncovered in our thorough budget review.

Previous governments have been artificially under-budgeting for contractual commitments, which means vital programs were under funded, and some vendors were simply not paid.

- A $4 million government food program, for example, only had a budget of $2.5 million.
- A $6 million commitment for immigration related software and hardware to support the passport office was never specifically budgeted for.
- A $10 million commitment for software and hardware upgrades to modernize the Department of Inland Revenue was never specifically budgeted for.

Our fiscal state of affairs has been building from years of fiscal hocus-pocus and hide the debt. Simply put, the chickens have come home to roost and unless we were willing to risk another downgrade to total crap bonds, with our ability to borrow in crisis evaporating, we had to address the problem.

I would love to pull the magic rabbit out of the hat or push the liabilities further down the road but that is simply not possible or responsible. Further, with interest cost eclipsing $381M we just cannot afford any more large borrowings.

These were the options:

1. Cut discretionary spending (which I just spoke to earlier)
2. Borrow more to meet the fiscal gaps, which was not an option
3. Continue false under-budgeting, which was not an option; or,
4. Enhance the revenue yield to more appropriate levels

As you can see, we were constrained by a set of choices that necessitated our adoption of a judicious and balanced approach of increased taxation as well as enhanced revenue collection measures, paired with our other fiscal consolidation efforts.

We considered all of the user fees and services that have not been adjusted for many years and reassessed those. We looked at immigration and port fees, which barely cover the cost of operations at this point. We looked at Real Property Tax, particularly the tax on foreign-owned vacant land; licensing fees on large commercial vehicles and an increase in other user fees. In total, we came up with about **$100m from non-VAT revenue sources**.

We considered VAT rates from 10% to 12% and ultimately fell on the 12% number as it gives us the best chance of arresting the slide, fixing the imbalance and funding priority modernization and infrastructure projects—that will bring cost savings and economic return and produce the desired balanced budget in three years, giving consideration to economic hiccups and other unplanned events. The **VAT increase** is expected to generate an additional $400 million in revenue.

In the context of tax reform, the government has already expressed its desire to explore further restructuring away from narrow-based and distortionary taxes. Accordingly, we have commissioned Deloitte to undertake a detailed assessment of the appropriateness of, and options for, **alternative forms of Business Tax** in The Bahamas, the revenues from which could, as an option, serve to replace the fees now collected in respect of Business License. At this stage, this is simply exploratory work geared to obtain an empirically based assessment of tax options and to canvass the views of a full range of Bahamian stakeholders. This study is just underway and I emphasize that no policy commitment has been made to the introduction of any alternate form of tax at this juncture.

I appreciate that many of these revenue-generating measures are unpopular. In fact, that might be the understatement of the day. But we are in this together as we only have one Bahamas and we must adapt to be successful together. While the business community has been resistant to these changes, we are calling on you all to embrace the notion of shared sacrifice so that we can restore the public finances to a healthy state on a durable and sustainable basis. A healthy public financial position will redound to the benefit of all Bahamians.

THREE-YEAR FISCAL PLAN

What we envisage is a three-year fiscal strategy, that will allow us to both deal with the assorted fiscal pressures that we face in 2018/19 and beyond and meet our deficit targets each year. In the budget, additional revenue from VAT and other taxes will be used to pay off the build up of unpaid bills and other identified contractual obligations, and draw a line in the sand that puts the practices of the past behind us.

We have also committed that as the hundreds of millions of old arrears and obligations are finally paid off over the next three years, the Government will give back to consumers, in the form of Customs duty and Excise tax reductions, on the order of $100 million, bringing down the cost of imported goods to the benefit of Bahamians throughout the country. This will line the country up for its efforts to participate in the World Trade Organisation (WTO) framework.

FISCAL RESPONSIBILITY

The budget adopts an approach to the management of the fiscal affairs of the nation in a responsible, transparent and accountable way. In fact, through the proposed **Fiscal Responsibility legislation**, the government is creating a legally-binding framework for responsible fiscal management as well as effective parliamentary and public scrutiny of the fiscal performance of the Government.

Going forward, the government would have to articulate and commit to a fiscal framework that caps the size of government to manageable limits to avoid an unchecked growth in Government spending that could over time undermine the economic stability of the country.

This law comes with legally mandated fiscal restraints, including caps on government spending, and debt ceilings and mandates to maintain a sustainable fiscal balance.

All of these fiscal consolidation efforts are critically needed to properly support The Bahamas as a global enterprise. We cannot be competitive if we do not have a strong fiscal position, if the state of public finances does not instill confidence in the business community and within the investment market. It is in our best interest to demonstrate we are a strong, stable jurisdiction. This also gives us strength at the negotiating table.

GLOBAL ENTERPRISE

Our country is small, but we have a very open economy that is heavily involved in, and reliant on, transactions with the rest of the world.

In 2017, our exports of goods and services represented some 34 per cent of Gross Domestic Product (GDP) while imports of goods and services accounted for 42 per cent of GDP.

While we have typically run a Current Account Deficit with the rest of the world, foreign direct investment and other capital inflows have more often than not been adequate to finance that deficit.

In 2017, our surplus on Capital and Financial Account amounted to over 20 per cent of GDP.

With our pending accession to the World Trade Organization, it can be expected that our interactions with the world economy will only increase further. This means we must aggressively tackle our weaknesses in the **ease of doing business** to strengthen our position as a true global enterprise.

All will know that we have not fared favourably in the annual country rankings of the ease of doing business developed by the World Bank. Indeed in the latest 2018 rankings, which are based on data as of mid-2017, we placed 119th out of 190 countries, with an even worst showing in respect of trading across borders with a 157th ranking.

Responding to this demand, the Government established a private sector led Committee to develop recommendations for improvements in the ease of doing business in this country. The Ministry of Finance also formed a cross-agency committee to examine how to make the business license application process faster, easier and more efficient.

The ultimate goal of the Committee was to streamline the entire business license process to allow much faster approval times through greater use of digital platforms that would support integration of systems between agencies for complete online service.

Our focus has been on making the system faster, easier and better. To that end, we are making the Business License system:

- Faster—by shortening the time required to secure both new and renewed licenses;

- Easier—stress-free and more citizen centered by fostering greater inter-agency cooperation to facilitate the acquisition of licenses; and

- Better—through improved service delivery via a single point of contact.

Upon completion in early 2019, the new system will also include the seamless integration of systems between agencies and complete online services, including the submission of applications and the reservation of business names through the Office of the Registrar General.

The Government is also implementing recommendations from the Ease of Doing Business Committee in:

- Promoting the Development of MSMEs
- Economic Diversification through the Digital and Blue Economies

With respect to **the Digital Economy**, we want to develop a sector strategy that involves both public and private stakeholder, encouraging Bahamian firms to incorporate digital technologies into their business strategy and create innovative technology-based business models. FinTech is an area of great potential, as it capitalizes on our strength in the financial services sector and the ICT sector, a major growth market.

To support the Digital Economy, the Government recognizes the need to improve the existing ICT infrastructure and legal and institutional framework in order to promote investment, as well as to use digital solutions to improve productivity in all economic sectors.

With respect to **the Blue Economy**, for small island states such as The Bahamas, articulating a strategy around our blue economy also enables identification and diversification into many other new and emerging ocean-based activities and sectors, including marine aquaculture, seabed mining, maritime safety and surveillance, marine biotechnology, marine security offshore wind energy, ocean renewable energy and deep-sea oil and gas production.

You may have also heard about our plans to develop an **Airplane Registry Industry**, incentivized by the elimination of duty on airplanes. We are trying to encourage aircraft leasing companies and corporate jet fleets to come to The Bahamas registry. By creating this registry, the country should see an increase in economic activity in the leasing, surveying, financing and insurance sectors, to support the registry, as well as job opportunities to service, repair, fuel and maintain the aircrafts. Once on the registry, we can charge owners up to $5,000 a year. These aircrafts need to be maintained and inspected, which means high quality jobs can be created from this registry

WTO PARTICIPATION

The Bahamas is the only country in the Western Hemisphere that is not a member of the WTO. The Bahamas cannot defend its own trade interests in the WTO if it does not have a seat at the table. Goods and Services offers were submitted by The Bahamas to the WTO for negotiations in 2013. The offers have been revised as a result of those negotiations and are currently the subject of industry consultations before being resubmitted to the WTO for a further round of negotiations with trading partners.

By joining the WTO, Bahamian businesses will have a more secure and predictable basis for business expansion. Without the security of legally binding agreements, there are no limits on trade restrictions or prohibitions being imposed by a country on Bahamian goods and services in foreign markets. This puts Bahamian goods and services at a disadvantage vis-à-vis its competitors who are members of the WTO and have the benefit of international trade rules that limit the imposition of trade restrictions on the import or export of their goods and services.

By joining the WTO, small countries enjoy the benefits that all WTO Members grant to each other, based on principles of non-discrimination and transparency. Small countries, like The Bahamas, can participate fully in the multilateral trading system as decisions are made by consensus and each Member has an equal right to challenge another member's practices in the

WTO dispute settlement procedures. Coalition building can also help small countries increase their bargaining power in negotiations or in creating new trade rules.

Modernization through domestic reforms undertaken in the process of accession, as well as transparency and predictability of the rules-based multilateral trading system, can also help to create a competitive and favourable business environment for all private sector operators, domestic and foreign.

Export-oriented operators can also benefit from access to the markets of all WTO Members on a most-favoured nation (MFN) basis. Hence, the greatest benefits of accession arguably go to SMEs and consumers, who are typically not able to lobby/negotiate on their own behalf.

CONCLUSION

There are many opportunities for The Bahamas to expand its participation in the global economy in traditional sectors, such as tourism and financial services, but also in broader areas that can support the economy's diversification. The planned accession to WTO will facilitate this expansion, and the Government is playing its role to make the necessary provisions and conduct the relevant stakeholder consultations.

But in light of the extraordinary and challenging circumstances we faced this year, given our fiscal state of affairs, we determined that all of our efforts, economic growth and diversification, could be undermined if we allowed the past practices of fiscal indiscipline to continue; if we did not take up the responsibility to put the country's fiscal house in order.

We need to ensure that we have fiscal headroom in the event of economic shocks; we need to ensure that we are able to negotiate from a position of strength, and that we can be selective about the types of investments we elicit when participating in the global economy.

The Government fully appreciates the sacrifice that the increase in the VAT rate and other taxes will represent for our citizens. But we only have one Bahamas and we are in this together.

The decisions we made are to strengthen The Bahamas' fiscal position and therefore our global value proposition. It is a three year commitment we are asking from the Bahamian people, at the end of which we will have a balanced budget and be on a certain path towards greater debt sustainability.

We must demonstrate that we have a stable and sustainable economy to instill confidence in current and future investors.

We must modernize to make it easier to do business in The Bahamas.

We must innovate to remain on the competitive edge.

We must diversify to create new opportunities to thrive in our economy.

We must lift up vulnerable communities and create inclusive growth.

And, we must collectively shoulder the burden of nation building, and adapt to be successful together.