



GOVERNMENT OF BARBADOS

FINANCIAL STATEMENT

AND

BUDGETARY PROPOSALS

2009

PRESENTED

BY

HON. DAVID THOMPSON

PRIME MINISTER AND MINISTER OF FINANCE

Monday 18<sup>th</sup> May, 2009

Mr. Speaker, I rise to present this Financial Statement in the year of Our Lord 2009 cognizant that acute challenges face our country and confront the world. To paraphrase Charles Dickens, these times are, *“the best of times, the worst of times; the age of wisdom, the age of foolishness; the epoch of belief, the epoch of incredulity; the season of light, the season of darkness; the spring of hope, the winter of despair...”*

I take comfort from the fact that the vast majority of Barbadians, judging from the tone and focus of their submissions, suggestions and counseling, are fully aware and appreciative of the nature of my task, created in large measure by circumstances not of our making.

Political friends and foes alike agree that, just as was the case in 1986 and even more so in 1991, this Democratic Labour Party has been dealt, financially-speaking, a ‘bad hand’. We have also inherited a multiplicity of national ills and a veritable cauldron of economic and social problems of a national, regional and international character.

Ninety per cent of our citizens and residents alive today would not have experienced a global economic downturn of the scope and magnitude of that which currently engulfs the world and which has placed small, open, vulnerable economies such as Barbados in a proverbial tailspin.

Economies in our Caribbean region are foundering in a morass of declining values and markets for their exports, tight fiscal positions and weak administrative capability for implementing national and regional decisions.

Nationally, we devised an attractive political, social and economic agenda in 2008 which tackles the main domestic challenges but is very much influenced by a hostile external environment.

There are no sure-footed policies that can be pursued, simply because we are walking an uncharted path; not having a reliable concept of how long or how severe the international economic and financial upheaval will last.

We have chosen as a government to pursue a road less traveled as we seek to bring some creativity and ingenuity to our task. Our policies will not find favour with everyone – some for narrow political reasons - others because their natural stance in times of difficulty is merely blame allocation.

Estimates ranging from 12 to more than 36 months in relation to the length of the recession are compounded by experts differing – even widely and dramatically - on what lies ahead for industrialized as well as developing countries.

What we do know, Mr. Speaker, is that those countries displaying encouraging signs of coping, note I did not say recovery but merely coping, are those that have been able to unite their best minds and brains around the problem and rally their populations towards a common sense of purpose. They work like a team, pursuing a goal, pulling together, managing internal conflict and keeping their eyes on the prize.

The one thing that Barbados starts with is our Social Partnership. Our next step is to create a **Team Barbados** strategy and work together to achieve our goals.

Of equal significance is the questionable success and effectiveness various strategies, including so-called “stimulus packages” crafted with the declared intent of arresting turbulence and decay.

This economic virus, similar in nature to the H1N1 virus, commonly known as Swine Flu, has spread with great efficiency from continent to continent. And while some economies in the developed world may have discovered and accessed the financial know-how and capability over the past eighty years since the last major economic upheaval of this type, none has as yet come up with the economic vaccine to both prevent as well as fend off the symptoms.

As a nation and as a people, we can tinker with systems and re-order priorities, but the options for economic planners in a country like Barbados, at this particular time, are few. There is also a tendency to believe that what is afflicting us is a cycle and that it is in fact predictable and measureable based on past experience.

That however is not my view. It is always easy to work backwards from a crisis and attribute factors and exigencies to its occurrence. But when you are in the middle of a major economic upheaval, it is necessary to frankly appreciate that there are things that we simply do not know and that only hindsight can explain.

That was my experience in 1992 when I first came into the Ministry of Finance. There has been a tendency for us to stay in the box and give greater credence to trends, forecasts, external predictions and stories of doom and gloom. The qualities that lead to change - risk taking, innovation, creativity and bravado - don't come in a box.

We must, as a small nation, appreciate that there are things that we do not know. Therefore we have to test, adapt, review and constantly be creative in applying solutions. Who could have known in 1961 the spectacular results that free Secondary Education would have wrought for our society?

In 1991, do we remember that every prediction from every quarter was that the Barbados dollar would be devalued?

I am always inspired by the Biblical advice, *“Now faith is being sure of what we hope for and certain of what we do not see.”* (Hebrews 11:1)

This government will do nothing reckless. But we will not fold our arms and do nothing either.

We must not be arrogant about the gifts that God has given us and we should acknowledge that there are some things that we do know: Anyone traveling to Europe or the United States and browsing the shopping malls or having enlightened discussions with persons of varying social and professional backgrounds, would understand clearly why our tourism sector in Barbados and the region, is under threat.

The persons we are wooing to this region are themselves victims of the economic downturn. Many of them were employed at General Motors, at various financial establishments that have gone belly up, in state agencies that have been downsized, in multinational companies that have exported their jobs to Central and Latin America.

This past week alone, 63 000 jobs were lost in the United States of America! This has nothing to do with the more than 15, 000 that were axed by British Telecoms earlier last week.

Many potential visitors to Barbados are this evening in London and Washington working in jobs over which dark clouds hover. In this environment, the prudent head of household adopts a posture of wait and see.

We are also competing against tourist destinations and chain enterprises in competing destinations that can absorb prolonged losses. How, for example, do we respond to a situation where airline, hotel, car rental and holiday attraction rates in some tourist cities in Europe and the US have been slashed by as much as 75 per cent for an indefinite period?

Sand, sea and sun are as commonplace today as is satellite television and amusement parks. How do you convince a family of the merits of passing up a \$1,000 vacation at home or close to home in preference to the same experience in Barbados that will cost them approximately six times as much?

These are the real and serious issues that confront us as a nation going forward in this period of global economic uncertainty.

And how also do you remain profitable as an attractive financial services sector, when the source of your revenue and profits are being offered free of cost by your competition, in an effort to thrive and survive?

How do you promote and protect your local agriculture sector, when alternative sources of produce, with cheap labour and greater resources, land and otherwise, can deliver the said product to our shores for a fraction of what it cost us to produce it here?

How do you guarantee the maintenance of high paying, quality jobs in the manufacturing sector, when that which you produce can be fetched from low cost suppliers in countries paying slave wages for less than the cost of your raw materials?

These are not abstract or esoteric questions. These are the realities.

This is no attempt to mitigate the impact of hard or maybe unpopular decisions that will have to be made. This is the gravity of the situation that confronts us as a nation today and these are the challenges we have to overcome.

I said earlier that hope was being engendered in societies where the better minds and more fertile brains are uniting and rallying around the national flag.

In the United States of America, President Obama's load in the first six months was made much lighter as a result of the cooperative and conciliatory approach of John McCain and other persons of influence seated across the political divide. That is not to say that he did not have other powerful critics.

In the United Kingdom, Opposition Leader David Cameron is doing well in the polls because he is not seeking to undermine or tear down the positives that Gordon Brown is seeking to put forward.

It is, in fact, a strategy that the Westminster political system seldom fostered in the past but the intelligence, sagacity and awareness of patriotic citizens is greater and they are not easily fooled by harmful posturing and political high-wire stunts.

In other words, the language of hope is easier to convey to the populace when all sectors and quarters of influence are focused and united in their resolve.

There comes a time in the life of a leader - whether it be business, religion, trade unionism or politics - where and when the national good must supersede all considerations. I humbly submit that now is the time for that awareness and maturity to manifest itself in our approach to problem solving.

We need as leaders in our various fields of endeavor to inspire the population. Barbados' successful navigation of the economic challenges we confront, depends squarely on our capacity to rally the country behind widely accepted and embraced objectives.

The optimum value and impact of any policy will be realized, only if and when the wider society subscribes to and pursues that objective.

In that regard, the timing of this Financial Statement is opportune, for we need as a nation to take stock of the trajectory of our actions, given the dynamic nature of events around us.

This presentation is but a guide to how we intend to approach challenges in the short and medium term.

One of the hallmarks of our tenure to date has been our capacity and indeed the deliberate manner in which we responded to situations; were they the oil and fuel crisis, the burgeoning cost of vital commodities as a result thereof, our practical and commonsense approach to issues of migration or our prioritization of certain social services that have enabled vulnerable groups to cope with the crisis and lead dignified lives.

The government which I have the honour to lead does not believe it has a monopoly on good ideas or that any position it takes is etched in stone. We have been and will continue to be flexible. No good idea, from whatever source, will be frowned upon.

The impact of drainage in Barbados will be minimized this year, I am sure, because we benefitted from the input and wisdom of senior folks, many of who, never crossed the door of a secondary school, far less a college or university.

Our communities will be infused with greater democratization as over 400 men and women will be inducted into 30 Community Councils to have a greater say in their own lives.

We have quietly and without fanfare democratised the Cabinet System by establishing four Cabinet Committees – Economic Policy, Social Policy, Infrastructure and Governance – to engender greater participation in Cabinet decisions by giving Public Officers, representatives of Statutory Corporations and Stakeholders to the opportunity to help explain, augment, prioritise and critique draft Policy Papers before they reach the full Cabinet. In some cases, the Committees have been given power to decide matters which do not need to go to the full Cabinet.

This Financial Statement is therefore made cognizant of the fact that further changes and amendments to all areas of policy will have to be made as we go along.

As I said previously, we are navigating an uncharted path. No one knows what lies beyond the bend. In fact, we have not yet even seen the bend.

Our actions and approaches will not be characterized by arrogance or conceit. If we make mistakes, we will take stock, reverse them and get on the correct path. If we under-do, or over-do in any regard, we will correct that as well.

What we will not do is fail to take hard or unpopular decisions for fear of partisan, political or other fall out. What we also will not become is wrong and strong, in our approach to problem solving.

We therefore come to the nation today, fortified in the knowledge that Barbadians know and understand the environment and the limitations with which we operate.

We are confident that our people will not expect more of us than we can reasonably give and, at the same time, that they will not expect us to give without taking...a little something.

After all, Mr. Speaker, the national cake has gotten no bigger. To lengthen the top we are forced sometimes to shorten the bottom. To protect the weak and vulnerable we are forced sometimes to borrow or take a little from the slightly better off.

In the final analysis there is one Barbados, and it is the duty of economic planners to seek out and safeguard the interest of all inhabitants.

It is against the backdrop of that reassurance and understanding, Mr. Speaker that I now set forth, in greater detail, the international, regional and domestic economic environment, in which this presentation is made.

### **The Economic Picture - International Perspective**

The escalation of the US financial crisis in September 2008 has led to a severe downturn in the global economy evident in an unprecedented contraction in global activity and trade. Global GDP contracted by an alarming 6¼ percent (annualized) in the fourth quarter of 2008, a swing of 10.25 percentage points from 4.0 percent growth a year earlier!

In addition, financial markets continued to face persistent liquidity shortages, thereby placing pressure on financial institutions. Within such a context, these financial sector shocks are expected to further retard growth within the developed economies, despite the substantial policy stimulus packages that are currently being implemented.

These developments will have severe economic, financial and investment ramifications for small open economies like Barbados. By any measure, the current financial and economic crisis represents by far the deepest and most pervasive post-World War II recession.

Within the USA, GDP growth contracted by 6.3 percent in the fourth quarter of 2008 and by 2.6 percent at the end of the first quarter of 2009. This pushed the unemployment rate up to 8.5 percent. It is projected that growth will fall by 2.8 percent in 2009 and remain at zero in 2010.

In the UK, one of our major markets, economic growth fell by 4.1 percent during the first quarter of 2009 compared with positive growth of 0.4 percent for the corresponding period in 2008. Overall, it is expected that growth will fall by 4.1 percent in 2009 with marginal positive growth in 2010.

In Canada, which is also a major trading partner, real GDP is expected to decline by about 6.5 percent for the first quarter of 2009, as against the 1.6 percent growth in the same period in 2008. It is projected that the real decline will be 2.5 percent in 2009 but that growth will return in 2010 at 1.2% for that year.

The impact of the crisis on developing and emerging economies such as China and India has also now been felt. China's economy grew by 6.1 percent in the first quarter of 2009, the worst first quarter performance in nearly two decades. Similarly, India's economy grew by 7.9 percent in the first quarter of 2009, down from 9.2 percent for the corresponding period in 2008.

On a more positive outcome, we are seeing some drop in oil and commodity prices. These reductions have helped to dampen some of the inflationary pressures felt last year. However, there are growing fears of deflation within advanced economies due to declines in per capita consumption and investments.

### **Regional Perspective**

As in other emerging regions, the Latin America and Caribbean regions are facing their own challenges as evidenced by reduced capital inflows, lower revenues from exports, tourism and remittances. This is not good news for Barbados the Caribbean countries are among our major trading partners.

It is expected that growth in the Caribbean region will fall by 0.2 percent in 2009 with a fairly strong recovery of 1.5% predicted for 2010. In most of the Caribbean countries the growth outlook for 2009 is down. Nonetheless, most of these countries should see some recovery by the end of 2010.

## **International Outlook**

The global economic outlook, according to the IMF, is for world output to decline by 1.3 percent in 2009, with some recovery in 2010, growing by 1.9 percent. It is expected that international financial markets will take longer to recover than previously envisaged despite interest rate cuts and large fiscal stimulus packages.

The economies of emerging and developing countries are expected to face greater pressures as access to capital declines and revenues from exports fall.

In the face of these challenges, countries will widen their fiscal deficits as many of them will have to use countercyclical actions to ensure some level of macroeconomic stability in the short to medium term. However, these deficits will have to be rolled back once the global recovery starts.

It is expected that the global economy will recover gradually in 2010. However this will depend on the ability of the industrial countries to heal their financial sectors quickly.

## **Domestic Economic Review**

Mirroring the global economic slowdown, the Barbados economy grew by 0.7 per cent in 2008. The pass through effects of higher oil and commodity prices combined with the lower tourism receipts have contributed to the overall decline in real output growth. This growth was however above the GDP growth rate registered in the last recessionary period when real GDP declined by 2.6 percent in 2001.

As a result of the protracted downturn within the global economy, GDP during the first quarter of 2009 fell by an estimated 2.8 percent, mirroring but not as bad as the 5.1 percent decline in the first quarter of 2002. The combination of lower capital inflows and increased outflows by the private sector pushed the capital and financial account into a deficit, forcing the net international reserves to fall by \$48.3 million.

Real value-added in the traded sector declined by 1.1 per cent during 2008. This outturn was attributed to a fall off in tourism value-added which fell by an estimated 1.7 percent, after recording an increase of 3.1 percent in 2007.

Preliminary data for the first quarter of 2009 revealed that tourism activity continues to decline, as value added to this sector fell by approximately 6.2 percent, reflective of a fall-off in arrivals from major source markets.

This performance is however above the 8.4 percent decline witnessed in 2002, a period that was affected by September 11<sup>th</sup> events and declines in global growth.

After two previous consecutive declines in the first quarter for sugar output levels, sugar production increased by approximately 11.9 percent during the first quarter of 2009. This outturn reversed the decline in sugar production which during 2008 fell by 9.0 percent or 31.6 thousand tonnes.

Output from non-sugar agriculture and fishing grew moderately by 1.1 percent during the first quarter of 2009 following a 3.7 percent increase registered during 2008.

Manufacturing output recorded a 6.6 percent decline during the first quarter of 2009. This outturn was attributed largely to declines in the production of food, non-metallic products and garments. The sub-sectors which registered marginal to moderate increases were chemical, beverage and tobacco and electronics.

The international business and financial services sector continued to exhibit moderate growth despite the challenges posed by the world financial and economic crisis.

During 2008, there were 579 new licenses issued compared with 764 in 2007, representing a 13.9 per cent decrease. New registrants to the international business companies (IBCs) stood at 481 while the number of New Societies with restricted liabilities (SRLs) licensed were 83.

During the first two months of 2009, preliminary data showed that new licenses approved for IBCs were 50 compared with 117 for the corresponding period of 2008, four (4) for SRLs compared to 35 and none for offshore banks and exempt management companies.

Reflecting a fall-off in new commercial and residential real estate activity, output in construction continued its downward trend in the first quarter of 2009 registering a 4.6 percent decline, after recording an overall decline of 3.4 percent in 2008.

Given the downturn in both the traded and non-traded sectors, unemployment levels at the end of 2008 started an upward trend recording 8.1 percent, a 0.7 percentage point increase over the 7.4 percent recorded in 2007.

During the first quarter of 2009, the unemployment level is anticipated to be above the 7.9 percent recorded during the first quarter of 2008. However, these levels are below the 10.4% level recorded in 2002, and in each of the years 2004 of 12.6%, 2005 (13%) and 2006 (11%).

The slowing of global economic activity and the pass-through effects of lower oil and international commodity prices contributed to inflation rates moderating during the last quarter of 2008 and the first quarter of 2009. At the end of 2008, the average rate of inflation stood at 7.3 per cent compared with 4.7 percent at the same period of 2007.

On a point-to-point basis, the rate of inflation continued to decline gradually from the peak of 11.2 percent reached in September 2008, falling to 7.6 at the end of February 2009.

In the financial sector, total deposits of commercial banks, including foreign currency deposits, fell by an estimated 1.3 percent to \$8,934.9 million at the end of December 2008. The level of savings deposits however grew by 9.3 percent or \$255.2 million to \$3,666.5 million during the review period. This expansion was attributed to major increases in the accounts of private individuals which rose to \$3,383.1 million, some 92.3 percent of total savings deposits.

Saving deposits by financial institutions fell by 20.9 percent while savings by business firms fell by 0.5 percent. Deposits by financial institutions also fell by 20.9 percent while savings by business firms fell by 0.5 percent.

In line with the fall in economic activity witnessed during 2008, credit to the non-financial institutions grew by only 0.3 percent during the first quarter of 2009, compared with 2.5 percent in the corresponding period one year prior. Deposit growth also slowed to 0.4 percent from 3.6 percent in the first quarter of 2008.

There was also further fall-off of the liquid asset ratio which recorded 8.7 percent at the end of February 2009. This outcome is indicative of reduced holdings of cash by the commercial banks, as the excess cash to deposit ratio decreased from 2.3 percent at the end of 2008 to 1.5 percent at the end of March 2009.

On the balance of payments, the external current account has started to show signs of improvement during the first quarter of 2009, as a deficit of \$16.9 million was registered compared to \$24.4 million in the corresponding period of 2008. This outcome is largely attributed to lower levels of retained imports, reflecting the sharp fall in petroleum prices on the international market.

Consistent with global economic trends during a recession, net long term investment fell by 66.1 percent to \$495.1 million in 2008 compared to \$1,460.9 million in 2007.

During the first quarter of 2009, the capital and financial account continued to exhibit declines, as a deficit of \$31.4 million was registered. This outturn in the capital and financial account balance was attributed to additional debt service payments, repatriation of profits and large tourism-related outflows.

The performance of the Barbados economy during the remainder of 2009 and into 2010 is predicated on the performance of the global economy, which is projected to contract in 2009.

This occurrence will see Barbados's major trading partners experiencing significant contractions within their economies which will create negative spill-over effects for the Barbados economy. Within such a context, real output of the Barbados economy is forecast to fall by between 2.0 and 2.5 percent in 2009 - much the same as in 2001 - as a result of further contractions within both the traded and non-traded sectors.

In particular, reduced growth within Barbados' major source markets (the UK and US) will negatively affect the outturn for tourism activity which is projected to decline by 4.5 percent by the end of 2009.

Based on the dampened economic activity within the economy, the rate of unemployment will be expected to rise while the pass through effects of lower oil and international commodity prices should result in lower inflation rates of around 4.0 to 5.0 percent.

The external current account is projected to show signs of improvement by the end of 2009 due to declines in the value of retained imports resulting from dampened demand and lower international commodity prices. Given the fall-off in net capital inflows resulting from lower foreign investment into the Barbados economy, the surplus on the capital and financial account is projected to be less than the figure recorded in 2008.

## **FISCAL SITUATION**

The 2008-2009 Estimates of Revenue and Expenditure were approved by Parliament in March 2008 and were formulated to achieve a fiscal deficit of 2.2% of GDP at market prices.

The Estimates projected current revenue on the cash basis of \$2,692.5 million, current expenditure excluding amortization of \$2,631.5 million and capital expenditure of \$235.4 million to give a fiscal deficit of \$174.4 million.

Preliminary information received from the Accountant General indicates that current revenue for the fiscal year was \$2,535.6 million, a decrease of \$6.8 million or 0.3% less than the amount collected for the same period last year.

The decrease in current revenue was mainly as a result of a decrease in Taxes on Incomes and Profits, which declined by \$59.2 million or 6.4% due to the global economic crisis which negatively impacted corporation taxes. Value Added Tax collected is also \$13.6 million less than that collected for 2007-2008.

Preliminary information also indicates that current expenditure less amortization was \$2,700.4 million, an amount of \$141.6 million or 5.5% above that recorded for the corresponding period last year. This increase can be attributed in part to the additional funds provided for the Barbados Tourism Authority and the Tourism Industry Relief Fund to assist the Tourism Industry during the economic crisis, the Special Road Improvement Project, the electricity and diesel subsidies and other increased subventions provided during the financial year.

Capital expenditure was \$214.2 million, \$24.8 million or 10.4% less than for the corresponding period of 2007-2008.

Based on the decline in revenue and the increased expenditure to stimulate activity in the economy, it is expected that the fiscal deficit for 2008-2009 will be 5.1% of GDP, substantially above the fiscal deficit of 3.7% recorded for 2007-2008 and the 2.2% originally targeted for 2008-2009 but below the 5.4% recorded for 2002-2003.

### Central Government Debt

At March 31, 2008 Central Government debt outstanding totalled \$5,762.1 million consisting of \$4,260 million or 73.9% in local debt and \$1,502.1 million or 26.1% in foreign debt.

By comparison, at March 31, 2009 the debt outstanding was \$6,198.2 million made up of domestic debt of \$4,738.0 million and foreign debt of \$1,460.2 million.

## Our Major Challenge for 2009 - 2010

The performance of the Barbados economy over the first three months of 2009 confirmed the expectations of a very difficult year. Output fell by an estimated 2.8%, marking not only a reversal of the 3.2% growth averaged between 2003 and 2008, but also one of the most pronounced contractions since the 1991/1992 recessions.

Value-added in both the traded and non-traded sectors have fallen (5.2% and 2.1%, respectively) and unemployment rates have started to rise again (7.6% at the end of 2008 compared to 6.7% one year earlier).

At the same time, net capital inflows have decreased, resulting in losses on the net international reserves (NIR) of the monetary authorities to the tune of \$36.4 million at May 6<sup>th</sup> 2009. With the downturn in economic activity and the reduction in net capital inflows, domestic deposit accumulation has been relatively sluggish, which, when coupled with waning demand, has led to stagnant private sector credit growth.

The expectations for the remainder of 2009 are not dissimilar. With the latest revision to the IMF's forecasts suggesting an even deeper recession in the United States, Barbados is facing the possibility of dampened economic activity well into 2010.

Even with the US\$100 million loan proceeds expected from the Trinidad and Tobago capital market, declining net capital inflows could continue to erode the NIR, leading to an estimated year-end loss possibly in the region of \$100 million.

The only positive sign so far has been an ease in inflationary pressures, as indicated by the downward trend in the point-to-point rate of inflation since September 2008.

Having said all of that, both the monetary and fiscal authorities have been trying to mitigate wherever possible the negative spill-off from the severe slowdown in global economic activity. Due to the financial origins of this current crisis, the Central Bank has been paying particularly close attention to developments within the domestic financial system and responding appropriately.

The Central Bank lowered the domestic interest rate environment by gradually reducing its minimum deposit rate, with a view to reducing the operational costs of businesses through consequential reductions in the lending rates. The minimum deposit rate now stands at 3.00%, 225 basis points below the rate that prevailed at the onset of the crisis in early to mid-2007.

As a further signal of the intended direction of interest rates, the Central Bank lowered the rate that liquidity-strapped institutions pay on borrowings from the Central Bank on two occasions, first in late 2008 and again in early 2009, to its current level of 8%. Effective June 1, 2009, the discount rate will be reduced further to 7%.

The reductions in the Central Bank's minimum deposit rate together with changes to the discount rate were relatively successful, particularly in signalling the direction of lending rates at commercial banks.

Liquidity concerns also played a major role in dictating the direction of monetary policy. The liquidity constraints internationally, as well as emerging concerns domestically, not only were a determining factor in lowering the discount rate, they also prompted the Central Bank to fast track its plans to introduce a reserve requirement for institutions licensed under Part III of the Financial Institutions Act, 1997.

The reserve requirement for Part III institutions was introduced in early 2009 and the institutions to which it relates have started to comply with the requirement. The Central Bank also added to its suite of instruments with the introduction of a repurchase facility, which can be used to provide liquidity for institutions that are short in cash but have eligible securities on their books.

The Barbados Deposit Insurance Corporation also has the full support of the Central Bank in carrying out its role of assisting with the protection of depositors should an eligible institution become financially distressed.

Activity within the banking sector has generally reflected the macroeconomic downturn. In the first four months of 2009, deposits grew by a mere 1.7% while credit increased by an even smaller margin of 0.3%, and non-performing loans are on the rise.

Even though the Bank has succeeded in lowering interest rates, the weak demand for loans has outweighed the impact of this relatively attractive borrowing climate. Furthermore, despite the positive spread maintained between domestic interest rates and U.S. interest rates, the global credit squeeze has effectively limited foreign capital inflows, thus further dampening deposit accumulation.

In 2008 the Central Bank continued the process of gradual liberalisation of exchange controls with the expectation that these amendments would provide an opportunity for Barbados to attract more foreign capital inflows as well as facilitate the rights of establishment and other conditions under the CSME.

Changes have also been made to address the needs of the small business sector given that the slowing economic conditions, and the potentially negative effects on small business development, point to a greater urgency to review the support schemes that provide both technical and financial assistance to the sector.

The Central Bank therefore revised the conditions for access to the Credit Guarantee Scheme for Small and Medium-Sized Businesses and to the Industrial Credit Fund to make them more accessible. The Central Bank will continue to monitor the effectiveness of these funds and make any necessary amendments as it strives to address the needs of small businesses.

Recommendations as to how Government should attempt to revive the economy have been provided by the Special Working Group in “Barbados Short and Medium Term Action Plan” as well as by the Central Bank in its “Policy Recommendations to Stimulate Output at the Sectoral Level”.

Despite the fact that the on-budget fiscal deficit has generally been improving (with the exception of 2008), the central government debt-to-GDP ratio rose from 59.6% in 1999 to 83.2% in 2008. Given the increasing tendency of government guarantees, which expanded from approximately \$387.1 million to \$729.0 million between 2004 and 2005, total public sector debt rose from 65.3% of GDP in 1999 to 98.7% of GDP in 2008.

Based on the projection for the fiscal deficit, central government debt is expected to increase from the 83.2% of GDP estimated at the end of 2008 to 87.2% in 2009, which would contribute to a total public debt that is expected to be in the region of 102.3% of GDP by the close of the year.

Government has tended to rely very heavily on domestic sources of financing in recent times. Consequently, the build-up in external debt has not been as significant as that of domestic debt, and the increase in the country's external exposure has been limited to some extent.

In 2009, a change in the composition of financing is expected; with the US\$100 million loan proceeds from the Trinidad and Tobago market, the deficit is anticipated to be financed equally by both domestic and foreign entities. In 2010, it is highly probable that the deficit will again be largely financed by domestic sources, as it is expected that the majority of any foreign borrowing will be used to facilitate the repayment of the US\$100 million bullet loan in June 2010.

This high level of public debt is a major cause for concern, particularly since it brings into question the sustainability of our fiscal policy. In 2008, Barbados recorded a total debt-to-government revenue ratio of 339.4% and an external debt-to-government revenue ratio of 124.2%.

In 2009, these ratios are forecast to rise even higher in light of planned government borrowing from external sources as well as a falloff in government revenues. Furthermore, even though in general the focus is on external debt sustainability, the rapid growth in domestic debt has received increased scrutiny from the international community.

Our strategy will be to generate a primary surplus of at least 5.9% of GDP from 2011 onwards. If this stance is maintained, the central government debt-to-GDP ratio should be just below 70.0% by the end of 2018. Government will limit additional foreign debt wherever possible.

## **CHALLENGES FOR BARBADOS**

As you can appreciate from what I have just said, the challenges for **Team Barbados** are, without a doubt, phenomenal.

Mr. Speaker, the best and only possible successful way for us to meet the challenges of this era is if we see ourselves as a national team facing a major competitive match that when the whistle is blown and it is over will see us promoted into a higher league or relegated.

We have the talent, we have talked the talk for a while and understand the strategy - although we naturally second-guess it - and we know the teams we are competing with and those that wish to catch up with us.

Right now all teams are facing a similar crisis. Are we going to be promoted or relegated?

In my government's view, for us to win this critical match and move up, there are some vital things we have to do:

**Protecting our Foreign Exchange Earnings and Aiming for Growth:**

We have to protect our earnings of foreign exchange as much as we can and, despite the current decline in the economies of our major tourist and international business markets, we should also aim for growth. If we aim for growth and do not achieve quite what we aim for, we are still likely to do better than if we simply aim to retain what we have. This has to be achieved by a combination of strategies.

The **Team Barbados** marketing efforts must be more focused on:

- (1) appreciating those who have played with and supported us in good and bad times and asking them, as persons who have been part of the Barbadian business experience, to “*hit the road*” with Team Barbados;
- (2) getting new players and supporters - visitors and investors - to commit to Barbados;
- (3) tailoring marketing efforts and resources to the results that we want and not on doing and spending on something because we have done it all the time.

We must also be clear as to what we are marketing. We are not just marketing hotels and sand and sea or tax breaks, we are marketing “*the Barbados experience*” which includes all that the entire Team Barbados has to offer in terms of our environment, our friendly people, our international business services, our high quality of life, our cultural services, our tourism experience, our educational standards, our infrastructure, our history, our reputation and our good name. What Team Barbados is marketing is Barbados – a country that wants to succeed and do even better.

We must maintain our presence in the marketplace and make our marketing more impactful and efficient. We have increased the Budgets of the Tourism Authority and Invest Barbados significantly for the task.

We have streamlined the corporate structure of the BTA and increased the mandate of Invest Barbados to include the Diaspora and launched the Team Barbados concept in our foreign Missions under the CIEX mandate.

The results have been encouraging even though there is still too much territoriality in our Missions where institutional mandates are too compartmentalized. A team must play as a team and players must be focused and competent but, most of all, adaptable. We must find the basis for working together, irrespective of any differences, in these difficult times.

We must encourage our Diaspora Networkers to help in marketing our country. Many Barbadians living overseas ask me, *“how can I help?”* Every Barbadian everywhere and anyone interested in the success of our country anywhere must be brought into the Team Barbados Network. We must use every conceivable device including formal and informal communications like facebook, blogs, you tube and so on to invite visitors and investors to see Barbados as their place of opportunity and enjoyment.

We have spent considerable time visiting and interacting with the Diaspora in London, Manchester, Cuba, Jamaica, Miami and Orlando, Houston, Toronto, Montreal and Ottawa, Cayman Islands and Panama. They need to know the game plan for Team Barbados.

**Achieving Stability, Productivity and Efficiency:** We also have to keep the economy as stable as possible within the significant fiscal constraints that bind us and within the context of what is happening all around us in the region and in the world.

Seeking to keep the economy stable will be partly accomplished by the earlier focus on limiting the decline in our foreign exchange earnings, on achieving greater efficiency and the elimination of waste in the public sector, on keeping our enterprises going and on providing strong and flexible safety nets.

We have to improve the sustainability of our fiscal position and so reduce the level of annual government borrowing and with it the burden being placed on future generations of Barbadians to service such debt. Our fiscal position also needs to improve, once the current economic crisis has ended, if we are to maintain our debt ratings.

Our concern for the debt ratings is because downgrades in the ratings will mean that future borrowings by Barbados on the international capital markets would be at significantly higher interest rates and so make our overall debt more expensive. Further, a downgrade could mean that some institutions that are able to buy our international bonds may now find that the lower-rated bonds do not qualify for their portfolios and so our access to foreign private capital markets could be reduced. The history of fiscal deficits over the last ten years is as follows and I include them for comparison:

<b><u>Financial Year</u></b>	<b><u>Fiscal Deficit</u></b>
1999-2000	1.4%
2000-2001	1.8%
2001-2002	3.8%
2002-2003	5.4%
2003-2004	2.4%
2004-2005	2.6%
2005-2006	1.5%
2006-2007	2.1%
2007-2008	3.7%
2008-2009	5.1%

In relation to our ratings, the Standard and Poor's rating was maintained at BBB+ but the outlook was changed from stable to negative.

The ratings from Moody's are not yet completed but in a recent Press Release Moody's said, *"Moody's Investors Service has placed Barbados' government bond ratings on review for possible downgrade to assess the credit impact of further deterioration in the country's debt metrics in the coming years. The review affects both the A3 local currency and the Baa2 foreign currency government bond ratings. The A1 foreign currency country ceiling for bonds, and the Baa2 foreign currency country ceiling for deposits are also under review.*

***"Barbados' key debt metrics have been deteriorating in recent years and are now at levels that compare poorly with other countries in the Baa rating category,"*** said Moody's Vice President - Senior Analyst Alessandra Alecci. ***"Such deterioration was observed prior to the onset of the global crisis, suggesting structural elements as part of the cause."***

*One of those elements is a persistent increase in government expenditures, including those off-budget, as revenues have remained at roughly the same level in terms of GDP. Since Moody's last rating action in 2000, Barbados' public debt stock has more than doubled, and relative to revenues, it has increased significantly. By the end of 2010, it could exceed 100% of GDP, up from 65% in 1999.*

***“Given that the government intends to undertake countercyclical fiscal policies from an already relatively weak fiscal position, and taking into account the anticipated impact of the recession on debt dynamics,”*** said Alecci, ***“a further worsening of debt metrics is likely in the coming years.”*** Barbados’ external liquidity has traditionally been weak and the country’s external debt metrics have tended to be worse than peers due to persistently large current account deficits, which have, in some years, required financing from foreign-exchange reserves. While the level of external debt is moderate, international liquidity is poor as measured by some of Moody’s key indicators.

*Despite near-term negative developments, Moody’s has no concerns about the government’s ability to finance its short-term needs, highlighting Barbados’ current investment-grade status. The majority of Barbados’ public debt is denominated in local currency and held by local commercial banks and public institutions, thereby reducing rollover risk.*

*In addition, the government has a sinking fund that can comfortably cover this year’s amortizations. Further, the country has successfully faced worse episodes of adverse macroeconomic conditions without compromising its commitment to the pegged exchange rate regime in place for over 30 years. A high GDP per capita and high-quality institutions also support of Barbados’ investment-grade ratings, noted the analyst.*

***“Factors that could eventually lead Barbados to lose its investment-grade ratings include unwillingness and inability to reverse the fiscal deterioration as expenditures could remain ‘sticky,’ and a loss of competitiveness in key industries, particularly tourism, which would prevent the economy from staging a meaningful recovery,” said Alecci.***

***”A reversal of the deteriorating trend in debt metrics will be key to Barbados’ ratings trajectory going forward,” said Alecci. This is particularly relevant given Barbados’ policy constraints due to the pegged exchange rate regime.”***

This is something that, in Opposition, we constantly warned the then government about. No heed was paid to our concerns and we are now faced with a stark, disturbing reality of the chickens coming home to roost.

Again, by comparison I include the movements in Standard and Poor’s ratings and outlook over the last ten years:

1. 1999: rating change to A- in good economic times.
2. 2004: rating DOWNGRADE from A- to BBB+, stable outlook in good economic times.
3. 2005: rating maintained at BBB+ but outlook changed from stable to negative in good economic times.

4. 2008: rating maintained at BBB+ but outlook changed from negative to stable when international predictions by IMF and others were still fairly positive for world economic growth.
5. 2009 April: rating maintained at BBB+ but outlook changed from stable to negative in the worst economic times in eighty years!

The long-standing concern of rating agencies relates to the history of increases in government borrowing over the last ten years and, of course, debt to GDP ratios which are as follows:

<u>Financial</u> <u>Year</u>	<u>Debt</u> <u>Outstanding</u> <u>(\$M)</u>	<u>Debt/GDP</u> <u>ratio</u>
1999-2000	2,885.1	58.2
2000-2001	3,225.6	63.0
2001-2002	3,784.5	74.1
2002-2003	3,975.6	76.5
2003-2004	4,211.8	78.1
2004-2005	4,472.1	79.4
2005-2006	4,742.6	78.9
2006-2007	4,911.0	77.0
2007-2008	5,762.1	84.5
2008-2009	6,198.2	82.8

What this means for all of us is simple to explain but to reverse the trend is quite difficult to actually achieve especially in this fiscal year. Our challenge is to narrow the fiscal gap by ensuring that government spending does not grow faster than the rest of the economy or by increasing government revenue faster than growth in the economy or by both measures at different periods of time.

The objective is to reach the fiscal deficit target and the debt ratio target that will ensure the country can continue to borrow when it needs to for critical projects and that its companies can enjoy world class debt ratings and competitiveness.

This will mean, among other things, that we have to remove subsidies to operations which are commercial or supposed to break even. Government itself will have to be leaner and more efficient. We will also have to maintain capital spending in the economy in order to lay the infrastructural foundations for the country to produce more in the future.

The increase in investment will also help enhance productivity of the economy so that the products and services we provide to our residents and to the rest of the world, including our visitors, are more competitive than they currently are and more attractive than those offered by our competitors in the region and around the world.

Another important challenge for Team Barbados in both the public and private sectors is to raise our service levels throughout the economy, particularly in all those areas that interact directly with the public or on which the public depends. We simply have to raise productivity in government and business.

While this challenge will partly be addressed by commissioning better technology, implementing better systems and delivering more and better training, we will not raise the level of productivity in our country until we all believe that we must and are motivated to give a full day of efficient and effective work for the wages to which we have agreed and until management and supervisors, business owners and workers representatives, government ministers and parliamentarians are prepared to deal firmly with those who refuse to give the level of work for which they are being paid.

While we press for growth wherever we can, we will seek earnestly and as a priority in this Financial Statement to help existing enterprises keep their doors open. Business enterprises are the ones with the responsibility and capacity to exploit the growth opportunities that may initially be generated by government's efforts.

Government, as part of Team Barbados, will market the country's tourism industry and facilitate new international business legislation, but it is hotels, other tourism enterprises and people that will have to fashion the packages and deliver the services to the tourists.

It is the private practitioners in the legal and accounting services, as part of Team Barbados, who have to provide high quality advice and structure the arrangements within the existing legislation and persuade investors to use those arrangements in Barbados.

### **Expanding our Social Safety Net**

The final, but very significant challenge for Team Barbados, is to make sure that the social safety net that we have in the country is sufficiently strong and flexible to ensure that our people, especially the most vulnerable among us, do not slide back into deep poverty.

Four of the biggest challenges here will be Jobs & Training, Health and Housing.

I have specifically placed jobs under this heading because we recognise that the protection of jobs is not only an economic initiative but in times of economic challenges, it is a social issue. Our Social Partnership programme to save jobs is the key initiative in this Financial Statement.

### Saving Jobs

What we are witnessing at this time is that many actors in the Social Partnership, as part of their national commitment, have maintained levels of employment in their businesses in circumstances where they would otherwise lay-off workers. Such a strategy – though desirable – has eaten into their cash flow, compromised their inventory and is not sustainable in a prolonged economic recession. We fully understand this.

I have agreed to make available to eligible employers experiencing cash flow problems the equivalent of a loan from the National Insurance Scheme, which is one year's deferment of employer contributions to the Scheme.

Employers must however have been compliant as at June 30, 2009 and give a commitment to maintain current employment levels for the period of the facility. This arrangement will become effective July 1, 2009 and the amount of the loan will be repayable over a five year term at a 3% rate of interest.

The National Insurance Scheme will not be put in a worse position by this measure since I propose to have the legislation changed to enable the Unemployment Fund to pay over to the National Insurance Fund the difference between what the NIS would otherwise have earned on these employer contributions and what the NIS actually earns on the scheme.

My view is based on the position that this scheme would reduce the number of employees who would otherwise become unemployed and draw on the Unemployment Fund.

It is better for employees because they maintain all of their employment rights and their job and their income does not decline. Employers benefit because their cash-flow requirements should be eased and they can maintain their commitments to the Social Partnership. The economy and the whole society benefit because job levels are maintained.

Additionally the Unemployment Fund itself benefits for it is better in this environment for the Unemployment Fund to disburse funds to prevent unemployment than to have to pay unemployment benefits.

Changes in the relevant legislation will be required to facilitate this innovative Employment Stabilisation Scheme and to ensure that this loan to employers ranks equally with other unpaid NIS contributions if the employer closes the business afterwards.

This measure is expected to cost the Unemployment Fund approximately \$34 million over six years.

### Waivers of Penalties and Interest

As a consequence of the current economic crisis, government has already introduced a programme of relief to employers and self-employed persons by way of a waiver of interest and penalties in respect of outstanding National Insurance, Income Tax, Land Tax and Value Added Tax.

The terms of this programme offer a waiver of half of the total interest and penalty owed in respect of outstanding contributions or taxes.

To qualify, persons must enter into an agreement with the relevant Government entities and the arrears must be settled within the agreed period.

## Training

The Importance of Training and Retraining cannot be overemphasized in an environment of job losses and recession. This is the ideal time for new skills to be acquired and for down-time to be used to enhance skills.

Economic recovery rests on the adaptability of our workforce and government is committed to expanding and extending training opportunities.

Under the NIS Regulations that apply to Unemployment Benefits, a person shall not be treated as unemployed unless he satisfies the Director that he is unemployed, capable and available for work or that he is unemployed and he is following a course of instruction or training under a scheme approved by the Board.

The National Insurance Board has approved the following courses as appropriate and a fund of \$10 million has been established for Retraining and for a stipend to be paid to beneficiaries of training when their benefits expire: Air-conditioning and Refrigeration, Auto-body repairs, Auto Mechanics, Basketry, Bobcat Operation, Carpentry, Computer Applications, Cupboard Construction, Electrical Installation, Garment Making, Tailoring, Household Accessories, Cookery, Heavy Duty Truck Driving, Horticulture/Landscaping, Housekeeping, Machinist Fitter, Masonry, Plumbing, Screen Printing, Sign Making, Steel Bending and Fixing, Skid Steer Loader/Backhoe, Tiling, Tractor Operation, Upholstery, Welding (all at the Barbados Vocational Training Board).

Accounts Technology/Administration, Animal Husbandry, Catering, Computer Maintenance, Crop Husbandry, Office Administration, Office Technology, Electrical Wiring, Electrical Installation, Aesthetics (Nail Care and Skin Care), Garment Making, Geriatric Studies, Landscaping and Horticulture, Maritime Operations, Painting and Decorating, Small Engine Repairs, Tourism Craft and Upholstery (at the Samuel Jackman Prescod Polytechnic).

### Housing

At the same time as protecting jobs, we have to meet some basic social needs that have not been adequately met, such as housing.

The National Housing Corporation has resumed its task of housing the nation through its Rental, Loans and Sales portfolio. During the financial year, 2008 to 2009 the National Housing Corporation commenced the construction of fifty six (56) rental units at a cost of \$15.0 million at the Country Park Towers and these are scheduled for completion by May 2010.

For the current financial year 2009 to 2010 the Corporation has identified five (5) other areas where one hundred and three (103) units will be constructed as follows:

- Twenty (20) units costing \$4,500,000.00 at Tweedside Road, St. Michael.
- Thirty-six (36) units costing \$10,500,000.00 at Eckstein Village, St. Michael.
- Three (3) infill units costing \$600,000.00 at Sayes Court, Christ Church. To date construction has started.
- Twenty four (24) units costing \$4,500,000.00 at Haggatt Hall, St. Michael.
- Twenty (20) units costing \$3,700,000.00 at Fordes Road, Clapham, Christ Church.

During the period April 2008 to March 2009, one hundred and sixty four (164) loans were approved totalling \$8.6 million.

Under the free transfer of tenancy programme, tenants who occupied the units for twenty (20) years or more as at January 16<sup>th</sup>, 2008 qualified for the free transfer of their units. 2,104 tenants have qualified for ownership of their units, and to date 1,852 have signed the agreement and are no longer paying rent.

For the period April 2008 to March 2009, one hundred and fifty five (155) lots were conveyed under the Sites and Services Programme. The National Housing Corporation has also identified an additional 392 lots for sale, comprising 187 middle income lots and 205 low income lots.

During the financial year 2009 to 2010, the National Housing Corporation proposes to develop thirty seven (37) acres of land to provide two hundred and twenty four (224) residential lots and fifteen (15) commercial lots.

To date the National Housing Corporation has commenced construction in 6 developments to produce 247 houses. At this date 91 houses have been completed while 156 are at various stages of completion. In addition, during the 2009 to 2010 financial year the National Housing Corporation is projecting to complete 572 houses and to provide 426 lots. The NHC needs time to dservice and rev up its engines

The Cabinet on March 19<sup>th</sup> 2009 approved the Rent-to-Own Housing Policy which has as its main objective the opportunity for low income earners to become property owners. The eligibility criteria to qualify for the rent-to-own programme are as follows:

- (i) persons must be working for not more than \$3,000.00 per month and are financially unable to service a mortgage;
- (ii) persons must not own property elsewhere;
- (iii) persons must be first time home owners;
- (iv) persons should not have benefitted previously from any public sector housing programme;
- (v) persons' rental payment must be up to date.

The Airlie Heights Development which consists of sixteen (16) two (2) bedroom duplexes is being used as a pilot project for the Rent to Own Housing Policy for Public Sector Landlords. Each unit is 520 square feet, costs \$135, 570.00 and has approximately 2,000 square feet of land.

One of the major concerns of Barbadians is access to decent affordable housing and land ownership. The increased demand for housing and land makes it critical that land utilization is maximized. Affordability therefore becomes a major challenge to the Government whilst satisfying the lower and middle income strata.

The “Zero Lot Line” concept of land utilization is a land maximization solution for middle and lower income housing provision that allows more families to be housed on an individual parcel of land. It also provides an opportunity for homeowners to purchase housing without incurring the high cost of large land lots. Land yield will therefore be expected to increase by 50% as home placement would increase from the current eight (8) to ten (10) per acre of residential development to between twelve (12) and sixteen (16) per acre.

Land at Coverley, Christ Church is being used as a Pilot Project where fifty (50) houses are being constructed using the “Zero Lot Line Concept”. The Project includes the construction of roads and infrastructure as well as the necessary financing up front for the housing development.

### Health and the Queen Elizabeth Hospital

The Ministry of Health has identified as a high priority area Chronic Non Communicable Disease and its potential devastating impact on the population.

These disorders which include diabetes, hypertension, cancers, cardiovascular disease and stroke have the potential to reverse much of the public health gains made over the last 50 years.

We must have a national strategy to get Barbadians exercising and moving coupled with strategies that include health promotion and education, surveillance, risk factor reduction and the adoption of fiscal and other monetary measures that will have a national impact.

Chronic non-communicable diseases affect more than 30% of our population over the age of 40 years and while we have a relatively commendable tertiary care system much of the emphasis needs to be on primary prevention.

We now understand that 80% of these disorders can be preventable. As a result the Ministry of Health took the unprecedented step to have a multi-disciplinary and mutli-sectoral approach to tackling these disorders.

Some companies both large and small have already put in place work-site wellness programmes that satisfy minimum criteria as established by the Ministry of Health and we encourage more to do the same. Numerous studies in industrialized countries have attributed improved morale, increased productivity and decreased absenteeism to worksite wellness programmes.

The workplace can be an environment in which people are afforded the opportunity to learn about health, to participate in physical exercise and to have the experience of eating healthy foods.

The Ministry of Health, the Ministry of Economic Affairs, Empowerment, Innovation, Trade, Industry and Commerce and particularly the Barbados National Standards Institute will need to collaborate to develop standards and protocols for unhealthy food, taking into account acceptable international recommendations.

The development of internationally recognised standards is preferred over increased taxation on these unhealthy food products. In addition to addressing the issue of food content there should be wider discussion regarding food labelling and processing. Citizens need to be provided with simple but accurate information so as to assist them in making wholesome and healthy choices that will contribute to their health and longevity.

The concept of Team Barbados is not only limited to economic development, it has relevance in all aspects of our lives. I have asked my dear wife Mrs. Mara Thompson to head a voluntary National Task Force to facilitate a major national exercise initiative to get Barbadians moving and shortly, I will also be reviewing a package of tax incentives for Gym memberships and equipment.

The other main concern of Barbadians is the Queen Elizabeth Hospital.

I am proposing that a Special Purpose Vehicle be established specifically for the purpose of the designing, financing and major renovation of the existing Hospital and/or construction of the extension to the existing Hospital and/or a new Hospital rather than under the project management of the Ministry of Health.

The work on planning for this project should start immediately. The Ministry of Health should establish a small Task Force to immediately consult with major stakeholders as a matter of priority to ensure the fullest possible consultation to resolve the outstanding issues.

### Charities

During my presentation of the Financial Statement and Budgetary Proposal to Parliament in July 2008, I announced that the Government would be embarking on innovative methods to capture international funds in support of social and economic development.

This is in keeping with the Bible injunction, *"Give, and it will be given to you. A good measure, pressed down, shaken together and running over, will be poured into your lap. For with the measure you use, it will be measured to you."* (Luke 6:38)

This proposal was based on the philosophy that investing private capital for public return should be a new approach to development financing in Barbados.

The Ministry of Finance having recognized the important contribution that philanthropic giving can make to the social and economic development of Barbados, commissioned a study which concluded that the only tax efficient method of giving in Barbados using the Covenant for three years or more, was overly bureaucratic because the covenant form, being a legal document, has to be signed and witnessed by both the donor and the recipient charity.

It also has to be registered with the Registrar of Corporate Affairs and Intellectual Property (CAIPO) or the Registration Department; it must then be submitted to the Inland Revenue Department for approval and registration. This is very often a time consuming process for the charity concerned. This long bureaucratic process has been identified in the report as the reason why many charities in Barbados do not actively seek to raise funds by means of covenant.

The Inland Revenue Department has therefore made the following recommendations:

- I. Covenant Rules should be abolished. In place of covenants, official donation receipts should be allowed.
- II. Section 85 (1) of the Income Tax Act should be expanded to include other organizations or entities which can be included in a Schedule to the Act.
- III. Small organizations should not be required to prepare and file legal documents with CAIPO in order to be a benevolent organization. A letter from the appropriate Ministry that the organization is an approved organization should be sufficient.
- IV. Both Cash donations and property should be allowed for tax purposes.
- V. Large donations of over \$1 million should be carried forward for five years and there should be a restriction on the amount that can be claimed each year.

Additionally, it is my intention to permit large one-off donations to Specially Scheduled Charities with a major public purpose like the Queen Elizabeth Hospital project or the Constituency Councils project to be written off in one year since such donations will reduce the Charities' dependence on government.

I concur with the conclusions and recommendations of the Study as well as the comments of the Inland Revenue Department. Therefore, the Income Tax Act Cap 73 will be amended in accordance with the recommendations of the Commissioner of Inland Revenue.

### Creative Economy

There is no longer a need for debate about the potential of the Culture Sector to contribute to the national economy and to the strengthening of our communities. The creative industries now constitute a new and economically significant dynamic in world trade.

As we seek to identify strategies for managing our response to the current global economic situation, there is a clear need for further diversification in our economy. The cultural sector is an obvious candidate for development in this regard, as it offers many opportunities for employment and revenue generation by way of goods, services, and Intellectual Property Rights.

Over the past decade, the Caribbean music industry has become increasingly aware of the value of audio visual products, both as marketing tools and as merchandise. The potential of the film industry is being successfully exploited outside of the USA and in Europe.

Barbadian talent is already being successfully marketed internationally, although not primarily for the benefit of the local economy.

A new regime of incentives, concessions, credits and exemptions is therefore proposed, for the benefit of cultural practitioners, and approved corporate, governmental and other entities, as a means of facilitating the requisite investment and capitalization for cultural projects, including those designed for heritage development and preservation.

These measures have previously been applied for the strategic development of the manufacturing and tourism sectors. It is now anticipated that the new regime, which will be encapsulated in a new Bill for Cultural Industries, will include import duty reductions and corporation or income tax relief for approved projects.

## Business Facilitation

Many a small business in Barbados has gone out of existence through and while waiting on government to pay its bills. Small businesses rejoice on receiving government contracts but then cringe as they wait seemingly forever on draw-downs, even though their work is complete or ahead of schedule. Adequate representation has been made for and on behalf of such enterprises.

Accordingly, it is proposed that a window facilitated by the Central Bank of Barbados of up to \$15 million be established whereby persons owed outstanding monies by government, and with proof of having satisfactorily completed their work can receive up to 90 per cent “advances” from that institution through factoring of the small businesses trade receivables with the commercial banks who then discount these advances with the Central Bank.

In this regard such enterprises can benefit from an ease in the pressure on their cash flow, easily meet pay roll expenses and restock and retool their operations and become eligible for other consideration.

There is no justifiable reason why such payments are often delayed. Much of this can be placed squarely at the feet of traditional bureaucracy despite the introduction of the Smart Stream System.

An internal Committee of Permanent Secretaries has been established to investigate why such payment delays occur both in terms of contracts for goods and services and government's temporary employees. The Committee will make recommendations which should eliminate such delays.

This is all in an attempt to assist the cash flow of the small businessman or woman and ensure job retention in these difficult times.

It is the intention of the Government to merge the operations of some of Government's Funding Agencies such as FundAccess, the Enterprise Growth Fund Ltd, the Industrial Investment Employment Fund and the Innovation Fund in order to bring a better and faster response to the needs of the diverse clients.

## Financial Services Commission

The Barbados Financial Services Commission (FSC) will be launched in the first quarter of 2010. Government has carefully reviewed the proposals for this new entity and has agreed that its establishment is critical and should be at the forefront of this country's efforts to ensure the sustainability of its financial services industry.

Working alongside the Central Bank, which will retain regulatory oversight for the banking sector, the FSC will be responsible for all non-banking activities in Barbados regardless as to the source of investment and will thus exercise jurisdiction over domestic and international non-financial business activity.

This is as appropriate a time as any to point out that the meltdown in the international financial system and the contagion which followed has had its impact in the Caribbean with the principal casualty being CL Financial Limited in Trinidad and Tobago. The difficulties in its Trinidad and Tobago operations have impacted on the operations of Clico Holdings (Barbados) Limited and its financial subsidiaries here – Clico Mortgage and Finance, Clico International Life Insurance and Clico International General Insurance.

In the United States, the response to the crisis has been to use taxpayer funds to bail out the troubled entities and in Trinidad a similar course has been adopted. There has been no bail out in Barbados. Rather, we have sought to engineer a private sector solution as a means of maintaining confidence in our financial system and aimed at saving jobs, pensions and investments.

I had earlier announced that Insurance Corporation of Barbados Limited had expressed an interest in Clico's subsidiaries and was involved in talks with that entity aimed at acquiring those assets. Those talks had apparently broken down and each party gave a version of why the breakdown had occurred.

To avoid any uncertainty and achieve government's objectives, a Memorandum of Understanding (MOU) has now been signed between the Government of Barbados and Clico by which the sale of the financial subsidiaries of Clico Holdings has been removed from the control of Clico Holdings and placed in the hands of a government-controlled Oversight Committee of six persons – four appointed by government (which will include the Solicitor General, the Permanent Secretary, Ministry of Finance and the Central Bank of Barbados) and two by Clico Holdings.

In the interim, the Committee will be responsible for the approval of expenditure and such decisions as relate to the financial subsidiaries of Clico Holdings.

We have chosen this route rather than the lengthy and cumbersome route of Judicial Management under the Insurance Act.

I also wish to state that ICBL has expressed a willingness to return to the table and this company along with any other reputable companies interested in purchasing will be given the opportunity to submit bids to the Oversight Committee.

The government of Barbados has been in constant communication with the government of Trinidad and Tobago and other regional governments in this matter.

The Regional College of Regulators will meet on Tuesday in Guyana and work continues in the process of finding a regional solution to the CL Financial issue.

## International Business

Barbados welcomes and supports multilateral activity aimed at rebuilding the failed international financial markets, based on stronger international cooperation in matters of tax information exchange. In fact, for many years Barbados has quietly been expanding its network of tax treaties based not only on securing competitive withholding rates on dividends, interest and royalties but ensuring effective means of communication between our respective Inland Revenue Departments.

I am pleased to confirm that the accelerated expansion of tax treaty network will stand alongside the specific measures I will address shortly.

The International Trust Act will be amended to allow for the creation and regulation of Private Trust Companies. Legislative changes will include a clear definition of “trust business” so as to better define the spectrum of services which Service Providers offer under the banner of trust services and the central registration of all International Trusts; guidelines on the licensing of trust companies and identification of the principals involved in the transaction.

In 2007 the Government introduced certain changes to the Income Tax which were designed to create opportunities for Barbados to be used as an attractive jurisdiction for the creation of holding companies.

Amendments will now be made to Property Transfer Tax Act and Stamp Duty Act to include a transfer to a non resident of Barbados of shares of a company, whose assets consist wholly of foreign shares, foreign securities and other foreign assets and whose income is derived solely from sources outside of Barbados.

It should be noted that the proposed changes to the Acts contemplate that the exemptions will apply to transfers by both Barbadian and non-Barbadian resident shareholders. With regard to exchange controls, it is imperative that “holding companies” benefit from similar exemptions to those enjoyed by International Business Companies and Regular Barbados Companies which conduct “international business” only.

The Income Tax Act provides that an individual, who is resident but not domiciled in Barbados, is taxable on income derived from local sources and on foreign income that is remitted or deemed remitted to Barbados. We will amend the Income Tax Act to reduce **the effective rate** of income tax that such individuals would be required to pay on their foreign income and to enable an individual who becomes domiciled here also, to claim the foreign currency earnings credit in respect of his income derived from outside Barbados.

The proposed incentive would potentially increase the amount of personal income tax revenues generated for the Government.

Further, it is proposed that dividends derived by Barbadian resident companies, including companies licensed to operate in the international business sector should be exempt from tax in Barbados on dividends derived from a “substantial shareholding” in an overseas company.

With the objective of enhancing the attractiveness of Barbados as a holding company jurisdiction, an exemption from withholding tax in respect of dividends paid by a resident company to non resident shareholders out of foreign source income earned by the company will be granted.

### Shipping

The Shipping (Incentives) Act will be amended to include game/sports fishing. I will extend customs duty-free concessions to fishing, rods and reels, safety equipment such as life rafts, satellite tracking systems, flares, fire extinguishers; lifejackets; satellite navigational systems, depth sounders; VHS, SSB and AM Radios, to any company engaged in commercial shipping and boating in the tourist industry (including game/sports fishers) from ten to fifteen years.

The Shipping Corporations Act was enacted in 1996, with a view of providing incentives associated with the formation of shipping corporations established to own, manage and operate ships. This Act has attracted little clientele.

Dr. Trevor Carmichael was commissioned by the Barbados Ships' Registry to review the Act. He proposed a number of amendments to the Shipping Corporations Act, which would, inter alia:

- (a) Permit the incorporation of shipping corporations that are offshore (in terms of requisite authority) and that are domestic.
- (b) Remove the restriction that a Director may not be a resident of Barbados.
- (c) Amend the purposes of the Act to include, e.g. the registration of incorporated and unincorporated bodies for expanded shipping activities. (The main focus is to enable the incorporation of a company to operate bareboat charters, allow for the registration of external companies under the Act as well as the registration of a company owning a ship registered in another jurisdiction.)
- (d) Enable a shipping incorporation incorporated in another jurisdiction to be registered as an External Corporation under the Act.

The Act will be amended to facilitate these proposals.

## Taxation

Government's fiscal elbow-room is extremely limited. Many representations have been made to me regarding concessions that should be given here and there. Regrettably, many of these proposals cannot be accommodated this year. As I have explained, we have to "hold tight" wait for the winds of international misfortune to calm and see some clearing in the sky. A complete review of our tax policy and incentive and competitive framework is underway and a full strategy will be announced in due course.

## VAT on Automobiles

The automobile industry, particularly the new vehicle business, is currently witnessing a 43% decline in sales. It is anticipated that this decline will continue unless the Government intervenes to assist in sustaining this sector.

The automobile dealers have also revealed that there has been a decline in new vehicle sales as a consequence of increased cost when the environmental levy was equalized on both new and used vehicles, the appreciation of other currencies against the US dollar and also due to a rise in manufacturing costs.

As a consequence of the foregoing the Government has decided to reduce the effective excise tax payable on vehicles falling under the following tariff headings, by increasing the rebate payable to dealers on the importation of new vehicles from 15% to 20%;

These new rates will become effective July 1, 2009.

### VAT on Building Materials

Due to the rising cost of land and building materials, the cost of constructing a home is a problem for potential low income home owners. I have therefore decided to increase the value of the qualifying amount for a refund of VAT on building materials from \$150,000 to \$200,000 on a house costing not more than \$400,000 for first time home owners who reside in their homes. There will therefore be no maximum family income limit below which first time homeowners will have to qualify.

The removal of VAT from the construction materials on this proposal would cost the Government approximately \$2.4 million.

In addition, I propose to remove the VAT on locally produced art and craft sold in locations such as the Grantley Adams International Airport and the Port to allow local art & craft to become more price-competitive.

### In-Bond Scheme

The phasing out of the in-bond scheme commenced on 1<sup>st</sup> May 2009. From that date, all companies registered on the in- bond scheme will have their bond liability coverage reduced from 30% to 5%. This will assist considerably with operators in the Duty Free Sector.

### Water

The level of revenue generated from existing water rates is insufficient to cover the costs of providing water and wastewater services. More importantly, it is not enough to maintain the existing level of service provision. Hence, it has become necessary to seek an increase in the rates.

The rates in existence today came into effect January 1, 2005. The existing rates have been structured to take into consideration the consumer's ability to pay (affordability) and to encourage careful use of Barbados' water resources (conservation).

Barbados is a water-scarce country and consequently water shortages are becoming a problem with the continued growth in demand. Moreover, the amount of water available for development has become very limited. The Barbados Water Authority has had to resort to desalination to address the problem of water scarcity.

The financial picture for BWA for 2009-2010 is distressing. The BWA is not generating sufficient funds to finance its operating budget, the capital programme, the debt service costs on the \$150 million loan nor the Pension Plan.

For a long time, our water mains have needed replacement, and more recently we have needed to increase the amount of potable water available. It is a massive undertaking but it has to start some time. Now is that time.

Too much money is wasted on pumping water of which a great deal (30% - 60%) is wasted through leaky drains, leaving residents without an adequate water service. We will this year begin the process of relaying these mains. It will take a long time to complete the job but the longest journey begins with the first step.

Additionally, the need for more potable water will be met by commissioning a Reverse Osmosis plant to provide five million gallons per day more. The BWA has been instructed to seek private partners for this project as well as the mains replacement programme to ensure that this BWA improvement programme is efficiently and expeditiously executed and financed.

This programme will cost approximately \$50 million per year for the next several years. But without it, our people continue to be deprived of adequate water service, our efforts to house the population are frustrated and our attempts at expanding our tourism and real estate industries are stymied.

The BWA has very little flexibility in reducing its costs. Approximately \$80 million of BWA's operating budget is comprised of costs that cannot easily be reduced without significantly reducing the level of service.

Let me here itemize some of those costs:

<b>Summary of key expenditures:</b>	<b>Expenditure</b>	<b>% of Total Expenditure</b>	<b>% of Total Revenues</b>
Salaries & Wages	\$ 29,454,384.26	29%	34%
Desalinated water	\$ 12,960,000.00	13%	15%
Electricity	\$ 25,200,000.00	25%	29%
Depreciation	\$ 11,657,312.10	12%	13%
<b>TOTAL</b>	<b>\$ 79,271,696.36</b>	<b>79%</b>	<b>90%</b>

The projected financial position for the next three years indicates that BWA's costs will continue to outstrip revenues resulting in operating losses and cash deficits. The accumulated net-loss position is projected at \$121M and the accumulated cash deficit at \$25M.

These statistics show that this is not a one off situation but will continue well into the future, under the existing tariffs.

The BWA has put in place a number of measures to reduce expenditures and to increase revenues. Some of these initiatives can be implemented expeditiously, while others require additional study to determine feasibility within the current operating environment. The key strategies include cost reducing and revenue enhancing measures.

To ensure that BWA is a financially viable entity and is in a position to undertake the major capital works programme that its development plan envisages, a change in tariff has been requested.

The increase as recommended by some analysts was in the vicinity of 100 percent of existing rates. I consider this high and not practical in the current economic environment.

Water is too vital a commodity, to be priced beyond the reach of any citizen of household. I have asked for a sharpening of pencils and also for a reasonable and equitable structure that will ensure and safeguard access to and affordability by the most vulnerable. The Welfare Department and other Social Care facilities will assist the most vulnerable in the payment of their bills.

All rates will definitely have to be increased by July 1, 2009.

### Gun Licenses

Mr. Speaker the current annual license fee on a firearm in Barbados is \$75. The cost of processing, documenting and maintaining these records is more than the \$75. I propose to introduce a two-tiered licensing system whereby, effective immediately, the first time cost of licensing a firearm is \$500 and the annual Renewal License Fee is \$200 per licensed firearm.

## Drivers License

Currently, there is the anomaly, indeed, the inequitable scenario where senior citizens, who are beyond regular salary and wage earning years, pay more at the end of a three year period for the renewal of a driver's license than do persons who comprise the workforce. This is because retirees are granted only one year renewals, and this is after supplying annual medical reports, the acquisition of which incur additional cost.

I am satisfied that the hassle is not worth the effort. Accordingly, effective January 1<sup>st</sup>, 2010 the cost of annual renewal of Driving Licenses to persons 65 years and older shall be reduced from \$50 to \$25 at the time of renewal.

## Projects

We have done what can prudently be done to keep people gainfully employed.

In central government, we have extended the duration of the programme to keep our verges and drains clean so as to prevent or relieve the flooding that occurs in some areas when it rains.

Our road repairing programme has been intensified and spread further around the country including the constituencies previously neglected such as St. John, St. Philip North, St. Lucy and St. Andrew.

Work is also due to start this year on junction improvement in the Warrens area in order to increase the capacity of that road system to carry the volume of traffic traversing that junction as a result of the commercial development there, and so to reduce the congestion in the area and increase the productivity of the country.

The National Insurance Board has seized this current economic situation to position itself to improve the financial return it earns on the pension funds it manages on behalf of the people of Barbados. At the same time, the Government of Barbados will use this opportunity to provide improved accommodation for some of its employees whose work places leave much to be desired.

As a result, NIS is having constructed for it two buildings at Warrens at a total cost of approximately \$105 million over two years and providing almost two hundred thousand square feet of usable office space that Government has agreed to rent on a long term basis. One building has already started and the documentation for the second is now complete, the site hoarded up and the project ready to commence.

Apart from improving working conditions, Government will then be able to repair vacated buildings properly, or demolish those buildings and use them in joint ventures with private partners to generate future income streams for Government.

The National Insurance Board through these investments will get nearer to the target for real estate in its investment portfolio without having to take as high a risk as the NIB would have to take if it depended on rentals solely from the private sector.

By making these investments, NIB will also be increasing the return it makes on its money since the returns on real estate are typically better than on long term government bonds or bonds of equivalent rating or on deposits held in the commercial banks, trust companies and mortgage houses.

The NIB is also nearing the point when it will be ready to commence construction on a third office building also for lease to Government but this time to accommodate the operations of the Caribbean Examinations Council.

Once again, this will be a very substantial building and current expectations are for construction on that building to start in the fourth quarter of this year.

Work is also due to start within the next few months on a substantial rebuild of the Lodge School. The tenders are in and are currently being evaluated.

Mr. Speaker, there are other projects under active planning and near to start of implementation. The programmes that I have just mentioned will together provide capital spending in the economy outside of central government spending of approximately \$100 million per year or nearly 1.5% of gross domestic product and, along with the expanded housing capital works programme, will go a long way towards restoring employment levels in the construction industry and the rest of the economy.

To protect the reserves in this capital works environment I have described, Government's foreign currency borrowing already approved by this House will be available.

Mr. Speaker, I come finally to matter of further increases in taxes and other impositions. There has been speculation over the additional revenue it would require to meet anticipated increases in expenditures and to achieve the fiscal objectives earlier outlined.

I believe firmly that Barbadians understand and appreciate the gravity of the crisis confronting us. We cannot as individuals and we cannot as a country live beyond our means.

We must cut and contrive. I believe there is more we can do to cut out wastage. We need to begin in the public service!

Strong recommendations were made to me for a one-off increase in the Value Added Tax. Indeed, a convincing argument for a three per cent increase in the VAT was made and seriously considered. However, I do not believe that the citizens of Barbados can bear such at this time. I am aware of the warning signals and I am cognizant of the concerns that will be articulated by rating agencies, the World Bank, International Monetary Fund and other relevant bodies.

However, I also know the strain that workers in Barbados are under and the load they are already carrying and more will not be asked of the tax paying and the consumer public of Barbados than that which they can reasonably bear.

## **Conclusion**

My moving a resolution in support of this Financial Statement will trigger three days of intense debate and discussion both in this Chamber and around Barbados. It's the perfect occasion and opportunity for us to bring into effect the 'Team Barbados' concept and approach.

I note with interest that the Opposition has promised to advance constructive policies and ideas for the forward movement of our country. I welcome that commitment to taking the high road in this debate.

As I said earlier, no plausible idea or suggestion will be discarded or frowned upon. Our position is that any and all ideas advanced for grappling with and surmounting current challenges will be embraced and pursued, no matter the source. This is a time for us to put Barbados first!

I have presented a Financial Statement for the times, in which I have set forth the challenges, minimized the potential fallout, while remaining fiscally responsible.

It is a strategy that should calm fears, guide us through the storm and brace us for the imperceptible.

This Financial Statement has remained true to the Government's pledge of open and transparent government; that is caring, responsive and real.

We have not ducked the issues or wilted under pressure. We have relayed and portrayed the situation as is, in the hope and with the confidence that Barbadians will respond with the tenacity for which they are known.

“Do not be anxious about anything, but in everything, by prayer and petition, with thanksgiving, present your requests to God. And the peace of God, which transcends all understanding, will guard your hearts and your minds ...” (Philippians 4:6-7)

I have confidence in our people.

I have confidence in our country.

I have confidence in this Honorable House.

That is why I unreservedly commend this Bill for consideration.

## **APPENDIX**

Revised Rates of Excise Tax on Automobiles:

<u>Tariff Heading</u>	<u>Current Excise Tax</u>	<u>New rate</u>
87.03	31.95	26.95
87.03	49.35	44.35
87.03	61.34	56.34
87.03	78.73	73.73
87.03	105.00	100.00
87.04	47.77	42.77
87.04	65.16	60.16