

Pre-Budget Report

IN ADVANCE OF FISCAL YEAR
2021 - 2022



GOVERNMENT OF BERMUDA
Ministry of Finance

Chapter 1

Purpose of the 2021/22 Pre-Budget Report

What Is a Pre-Budget Report?

A Pre-Budget Report (PBR) is a policy statement issued by the government prior to the release of its budget. It defines the priorities for the next budget in a medium-term framework covering external developments and internal strategies. The PBR should clearly state the government's economic and fiscal policy challenges as well as its objectives and intentions in the medium term.

Bermuda's economy, like most other small open economies, is highly vulnerable to external events, underlining the need for financial and fiscal prudence. This vulnerability is compounded by continuing budget deficits and a high level of government net debt, which now stands at \$2.972 billion.

There are a number of actions that the government needs to address regarding the problems the island faces. Furthermore, it is important that stakeholders and citizens understand these vulnerabilities, have the opportunity to give their views, and are aware of the factors driving the government's fiscal policy decisions. The government should be accountable for developing strategies to cope with both domestic and international turbulence, and the strategies adopted should be transparent and open to criticism and comment. The government should also be accountable for their execution.

Greater transparency and public participation in the budget process [are] more likely to yield spending priorities that serve the best interests of society as a whole... The regular release of information can provoke public debate and encourage accountability. Budget information is important not just for accountability to the public but also for internal management purposes.

Holding the government fiscally accountable requires the production and dissemination of budget information from the formulation stage, through approval, execution, and evaluation (or oversight). Yet around the world today, citizens and legislatures frequently lack at least some basic information about government decisions and actions at every stage of the budget process.¹

¹ Harika Masud and Jason M. Lakin, "What the Open Budget Survey 2010 Tells Us about the Global State of Transparency", Yale Journal of International Economics, Winter 2011, p. 65.

Purpose of the Pre-Budget Report

The objective of the PBR is to increase public awareness of a government's fiscal and budget policy objectives, and to establish a benchmark for evaluating the conduct of fiscal and budget policy.

The PBR also serves to **educate** the public and encourage debate on the budget strategy and how effectively it copes with current economic and social priorities. The PBR is intended to provide an opportunity for stakeholders, such as business and social groups, to understand and comment on options for the next budget. This can give stakeholders confidence that the administration's budget policies are grounded in longer-term fiscal and budget strategies.

From the government's perspective, the scope for public misunderstanding of the (eventually chosen) budget strategy is reduced due to a greater public appreciation of the nature of the trade-offs facing the government.

Pre-Budget submissions by such groups, whom respond to the PBR, can also **alert** the government to unforeseen pitfalls and alternative policy options as well as improve the quality of the budget. They may even pre-empt embarrassing policy back-flips after the budget has been handed down, when previously invisible problems come to the fore.

The PBR will also improve the budget preparation process for the **line ministries** in the current budget year as well as in forward years by imparting a clearer knowledge of the government's strategies.

Finally, a PBR increases the **accountability** of present and future governments for effective fiscal policy management. This is at two levels:

- The government can be held accountable for the extent to which the fiscal strategy it proposes in the PBR conforms to the principles of sound fiscal management.
- The government can be held accountable at the end of the fiscal year for the extent to which the realised fiscal outcome conforms to the strategy it proposed for that year in the PBR.

Principles of Good Fiscal Policy

Fiscal policy should be directed at ensuring that prosperity reaches all segments of Bermuda's society while having a sustainable medium-term framework. To date, Bermuda's economy has not worked for all Bermudians, and this government was elected to change the status quo and ensure all Bermudians have an opportunity for prosperity.

To meet these objectives, this government's fiscal strategy will be framed in accordance with the following principles of sound fiscal management.

- Prudent management financial risks faced by the government.
- Ensure fiscal policies contribute to enhancing the government's fiscal position.
- Pursue fiscal policies consistent with a reasonable degree of stability and predictability.
- Maintain the integrity of the tax system.
- Ensure policy decisions are constructive and have a positive impact on future generations.

The management of public finances has taken on greater significance with the onset of COVID-19. At the earliest possible stage, countries are tasked with charting a path towards resuming normal application of fiscal policies, striking a balance between the objective of restoring fiscal sustainability and not jeopardizing growth.

The government maintains that the uncertainty of these times should not deter efforts to promote and invest in the diversification of our economy. Bermuda's effective management of the Coronavirus and rigorous testing regime has provided an avenue for growth which the government will continue to capitalize on. These growth opportunities will improve our ability to reduce our deficit and increase employment in not only existing industries but new and innovative sectors as well.

However, it is important to note that while diversification is a major priority, the government must put stability first, avoiding any risk that could impact the island's sterling reputation or the sustainability of the public finances.

Risks Facing the Bermuda Economy

In their reports, the Fiscal Responsibility Panel (FRP) highlighted a number of risks to Bermuda's economy. These risks, among others, underscore the need for financial and fiscal prudence, and the government has considered these risks when framing the 2021/22 budget.

Some of the threats noted by the FRP are as follows:

- *Risks From Slowing Global Growth.* The pandemic has fundamentally altered the external environment facing Bermuda. The IMF projects that the world economy will shrink by 4.4% in 2020, and then recover by 5.2% in 2021 taking output slightly above that of 2019 -- two lost years of global growth, with limited catch-up thereafter.
- *Insurance Industry Risks.* Bermuda's (re)insurance industry is exposed to losses from extreme weather events and natural catastrophes elsewhere. To date, the Bermuda-based (re)insurance sector has proven to be well capitalised, paying claims related to increasing extreme weather and natural catastrophe events, as well as benefiting from investment returns, higher premiums and increased insurance penetration. The Bermuda Monetary Authority (BMA) and the UK's Prudential Regulatory Authority (PRA) conducted a joint stress test of (re)insurers in 2019, supplementing this with an additional exercise focusing on COVID-19-related losses in 2020. The conclusions, published in June 2020, found that (re)insurers remained resilient to extremely adverse scenarios.

- *Risk From Corporate Tax.* Bermuda's status, with respect to the EU's blacklist of non-cooperative tax jurisdictions, has also been resolved for the moment, following Bermuda's implementation of measures (primarily relating to economic substance for collective investment funds). Bermuda is now fully compliant and has been moved to the "white list." Progress has also been made with respect to OECD standards on corporate taxes, the Base Erosion and Profit Sharing (BEPS) Pillar 2, as Bermuda joins the OECD Multilateral Competent Authority agreement to automatically exchange tax information. However, further pressure on this front is inevitable, principally from countries heavily reliant on corporate tax revenues seeking to ensure taxation reflects economic presence. This raises medium-term concerns about the potential impact on Bermuda's attractiveness as a base for international corporates. In short, Bermuda has responded flexibly and appropriately to a variety of international regulatory pressures and issues over previous years. However, such pressures will not diminish, particularly in respect of taxation, and may well intensify, as other governments seek to rebuild their public finances.
- *Impact of Global Warming and Climate Change.* While the pandemic and the associated uncertainties overshadow other risks, that does not mean they should be ignored. Climate change continues to be a major and growing threat, with 2020 seeing several extreme weather events. Bermuda is vulnerable both directly, given its geographical position and low-lying land, and indirectly, because of the importance of the insurance and reinsurance sector to the economy of the island.
- *Effects of an Ageing Population, Declining Workforce, Underfunded Public Sector Pension Funds and Escalating Health Care Costs.* This remains a certainty, not just a risk, which will result in serious medium and longer-term pressures on public spending and challenges to growth. It will also make it more difficult to deal with a large debt overhang.

Chapter 2

Economic and Fiscal Performance

Covid-19 has caused a severe economic shock in all directly affected economies.

Global Economy

According to the IMF's October 2020 World Economic Outlook (WEO), the global contraction is not as severe as previously anticipated. Global growth is forecasted at negative 4.4% in 2020, increasing to positive 5.2% in 2021 (the 2020 contraction has been upgraded from 6.0%-7.6% in the June report and global growth in 2021 has been upgraded from 2.8%-5.2% in the same report). The revision reflects more optimistic second quarter GDP data, mainly in advanced economies.

Global trade began recovering in June as lockdowns were eased. China's contribution to the recovery was important with their exports recovering from large declines earlier in the year, supported by an early restart of activity and a strong increase in demand for medical supplies and equipment to assist the shift to remote working.

However, the lasting effects to the global economy from the pandemic recession can be witnessed in labor market indicators and inflation outcomes. According to the International Labour Organization, the global reduction in work hours in the second quarter of 2020 compared with the fourth quarter of 2019 was equivalent to the loss of 400 million full-time jobs. Global inflation results have witnessed prices of items such as medical supplies and commodity prices increase, while the effects of weak aggregate demand appear to have outweighed the impact of supply interruptions. In general, inflation in advanced economies remains below pre-pandemic levels. In emerging markets and developing countries however, inflation declined sharply in the initial stages of the pandemic but has since picked up in some countries.

Although economic activity began to improve sooner than expected (after lockdowns were scaled back in May and June), the IMF states that many countries have delayed reopening. With the COVID-19 pandemic continuing to spread, some countries are reinstating partial lockdowns to protect the susceptible population. For many countries, sustaining economic activity and helping individuals and firms most in need, while ensuring that debt remains sustainable, is a daunting task. This job is made more difficult

due to the fact that there are already high levels of public debt due to the spending needs triggered by the crisis combined with reduced revenue levels. However, governments must continue to combat the health crisis and mitigate the downturn while being prepared to adjust policy strategy as the pandemic and its impact on economic activity and society evolve.

US Economy

Based on information provided by the OECD Economic Outlook 2020, the US economy is recovering following a significant decline in GDP and dramatic rise in the unemployment rate in the first half of 2020 brought on largely due to the COVID-19 pandemic. The unemployment rate is expected to gradually decline but will remain elevated compared to the pre-pandemic period. This is a reflection of the activity in sectors such as hospitality and transportation continuing to be impacted by the pandemic and impediments to cross-sectional labour reallocation. Once a general rollout of an effective vaccine occurs, this should allow an easing of containment measures and strengthen confidence in the economy which will enhance the recovery.

As a result of the impact of COVID-19 and the measures put in place to minimize the pandemic's effect, real GDP in the US is anticipated to contract by 3.7% in 2020, before rising by 3.2% in 2021 and 3.5% in 2022. The anticipated economic growth in 2021 will undoubtedly have a positive impact on Bermuda's economy. With vaccines on the horizon and economic growth, the US will significantly assist Bermuda's economic recovery in 2021 and beyond as they are Bermuda's largest trading partner and source of the vast majority of visitors to the island.

Bermuda Economy

Bermuda's economy exhibited a marginal increase in 2019 of 0.5% based on constant market prices (real GDP). The largest value increases, in real terms, were recorded in the construction and real estate activities sectors. In contrast, the financial and insurance activities sector recorded the largest decline in value.

The economic impact of the pandemic public-health measures, required to suppress COVID-19, caused severe reductions in the Bermuda economy during the first half of 2020 and beyond.

Based on figures released by the Department of Statistics, GDP fell by an average of 9.3% in real terms in the first 2 quarters of 2020. This decline was primarily driven by declines in expenditure on durable goods and services. Durable goods spending fell due to fewer

purchases of motor vehicles and furniture. Spending on services experienced declines for travel-dependent services such as accommodation and air transport.

Bermuda Economy 2020: Economic Review

Summary Economic Indicators: Economic Review 2020

- The year to date (September) average inflation as measured by the Consumer Price Index was 0.0% and the 12-month average rate was 0.2%. The primary causes of inflation during the last twelve months were increased costs in health insurance of 1.7% in April and increases in the average costs of various food items throughout the year.
- Total retail sales for the first eight months of 2020 decreased by 4.5% or \$33.4 million to register at \$713.8 million. Apparel stores exhibited the largest decline in sales followed by motor vehicle stores and service stations sales. In all three categories, decreased demand led to fewer sales year over year.
- Total value of new construction projects started for the first six months of this year fell by 41.3% from \$73.4 million to \$30.3 million.
- The estimated value of construction work put in place was \$58.0 million, a reduction of 57.5%. The majority of the decline can be attributed to an 88.7% decrease in work performed on roads, bridges and the airport and the fact that work on hotels and guest houses was nonexistent in the first 2 quarters of 2020.
- Based on preliminary estimates from the Office of the Tax Commissioner, employment income for the first 9 months of 2020 fell by \$194.2 million to \$2.528 billion, a decrease of 7.1% when compared to the first 9 months of 2019.
- Imports decreased by 27.5% over the first two quarters of the year to register at \$437 million. Broken down by quarter, there was an increase of 10.6% in the first quarter followed by a decline of 50.3% in the second quarter. The majority of the decrease can be attributed to an \$87.2 million or 62.4% fall in the imports of machinery due in large part to Belco's imports for a new generator last year. The other category that contributed significantly to the decline in the level of imports was finished equipment.
- Air arrivals during the first three quarters of 2020 plunged by 85.2% while the number of cruise passengers fell by 97.9% over the same time period. Total visitor arrivals were down by 93.7% versus a year ago.
- Total air visitor spending in the first nine months fell by \$277.2 million or 84.6% settling at \$50.3 million.

- 503 new international companies and partnerships were registered in Bermuda during the first nine months of 2020 representing a 5.7% increase when compared to the 2019 registrations of 476.
- Bermuda's Balance of Payments over the first two quarters of 2020 recorded a surplus on the current account of \$453 million, which was \$100 million greater than the corresponding surplus in 2019. The increase in the current account surplus was due in large part to a \$167 million reduction in the deficit of the goods account and a \$49 million increase in business services. Transport and investment income also contributed to growth with reductions in their balances of \$36 million and \$35 million respectively. These amounts were partially offset by a \$194 million decline in the balance on the travel account.
- Based on figures released by the Bermuda Monetary Authority, Bermuda's money supply grew by 5.5%, or \$195 million, year over year at the end of the second quarter of 2020. The money supply increased mainly due to a \$0.1 billion or 2.9% increase in local consumer deposits in the second quarter.
- The banking sector's total assets increased by 12.9% or \$2.7 billion at the end of June 2020. The growth was driven by increases in investment holdings which advanced by 15.2% or \$1.4 billion.
- Loans & advances increased by 9.9% or \$0.8 billion over the second quarter of 2020 while customer deposits grew by 13.7% or \$2.5 billion for the same time period.

The above mentioned economic data clearly illustrates the severe economic shock that COVID-19 has had on the Bermuda economy and the economic performance for the first 6 months of calendar year 2020 was as expected.

However, the government's COVID-19 Fiscal Plan has provided timely and targeted fiscal stimulus to various components of our economy, as needed. The government has taken urgent, and appropriate action to reduce hardship and prevent business failures. Without these stimulus measures the overall economic contractions in 2020 would be a lot worse.

In addition, the international business sector, in particular the insurance sector, has remained resilient during 2020 despite the pandemic. This sector will continue to be the main driver of our economy.

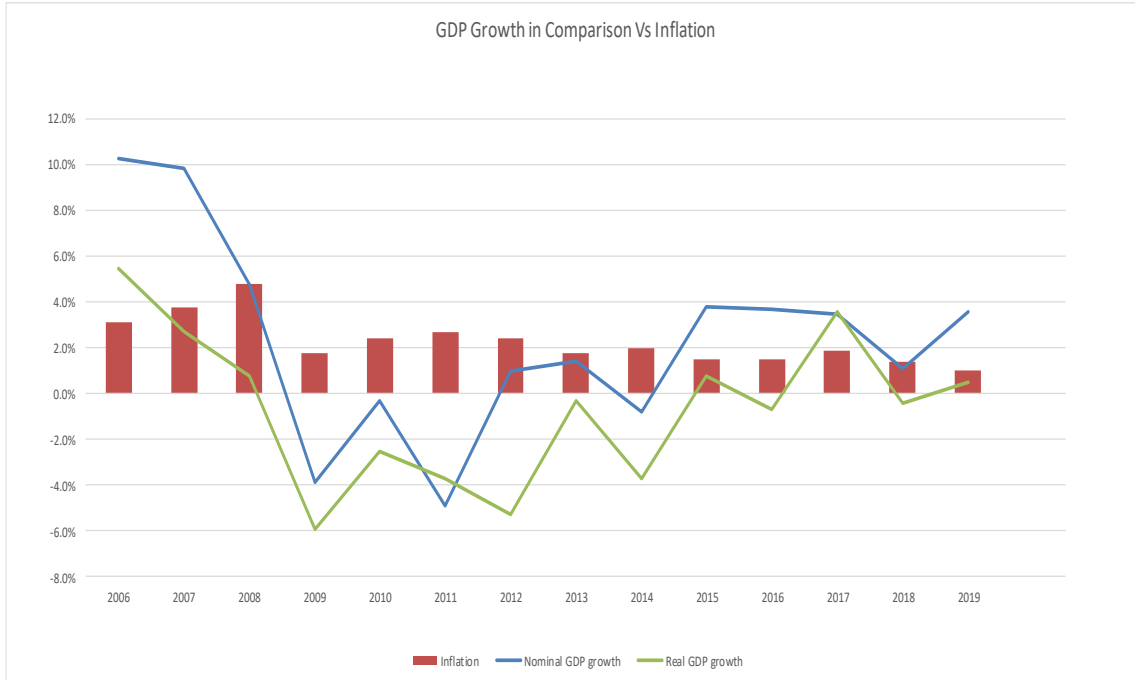
Overall, the Bermuda insurance market has adapted well to COVID-19-related restrictions and was able to continue to service policyholders in a nearly seamless manner. No major operational or solvency matters were experienced highlighting the resilience of our

market. The COVID-19 pandemic has only affected the profit and losses of insurance providers rather than their solvency, which should allow for the market to withstand the impact of the pandemic, even if an above average 'catastrophe' season occurs. Furthermore, the COVID-19 pandemic may have some potentially positive effects with respect to the Bermuda insurance market if new insurance business lines develop and existing insurance business lines grow. In addition, there has also been a significant growth in the long-term insurance sector.

We are still facing much uncertainty, and in particular, there is the risk that the economic impact of the pandemic may be even more severe and longer lasting than currently anticipated.

With contraction in many of the key economic data, such as visitor arrivals and spending, imports, construction activity, consumer spending and employment income expected to continue, but at a lesser level of contraction than in the first 6 months of this calendar year, the Ministry of Finance expects GDP in 2020 to be in the range of negative 7% to 9%.

Throughout the economic disruption caused by COVID-19, the government has and will continue to make a concerted effort to stimulate domestic spending and maintain employment levels in Bermuda through the implementation of timely and targeted measures, with some of these measures being recently announced in our Speech from the Throne.



Credit Ratings

The government currently holds long-term foreign currency credit ratings of “A+” (stable outlook) from Standard and Poor’s (S&P) and “A2” (stable outlook) from Moody’s Investor Services (Moody’s).

During the government’s recent debt issue in August 2020, S&P Global Ratings issued a report on 12 August 2020 that affirmed Bermuda’s 'A+' long-term sovereign credit and senior unsecured debt ratings, its 'A-1' short-term rating, and its 'AA+' transfer and convertibility assessment on the territory. The outlook remains stable.

The headline and beginning of the report read as follows:

“Bermuda ‘A+/A-1’ Ratings Affirmed; Outlook Stable S&PGR Affirms Bermuda’s ‘A+/A-1’ Ratings With Stable Outlook

The stable outlook reflects our expectation that Bermuda’s moderate net general government debt burden, favorable external position (including current account surpluses) and political stability will help contain the negative impact of a sharp GDP contraction in 2020 and set the stage for economic recovery in coming years. We expect GDP to decline by 7% in 2020 and recover by 5% in the following year. The recession may result in a general government deficit of 3.7% of GDP this year. We assume that a

combination of GDP growth, recovering revenues, and a commitment to advance towards fiscal balance will contain future fiscal deficits, and stabilize the government's net debt burden."

The public should accept the outcome of this report as an independent and objective endorsement of the government's fiscal and economic policies which are aimed at keeping the population safe and the economy strong during this global pandemic.

Debt Concern

Public debt levels and deficits have hit records during the pandemic. Many experts argue it is a sound means to fund the recovery. Since 2009, Bermuda's national net debt has increased by \$2.5 billion. At the end of September 2020, total net government debt outstanding was \$2.9 billion, which was \$600 million beneath the present statutory debt ceiling of \$3.5 billion. The Ministry of Finance regards this level of debt as a serious challenge. Similarly to many small countries and territories, Bermuda's economy is extremely susceptible to outside events. The following vulnerabilities are common to many small islands including Bermuda:

- A high level of openness means they are heavily exposed to shocks in global markets;
- A narrow resource base and small domestic market prevent small economies from diversifying to a vast assortment of activities, making them more susceptible in terms of trade shocks;
- When one prevailing activity declines, it has a major impact on the economy, which is the case in Bermuda in which the insurance sector continues to be dominant;
- Government revenues are volatile;
- High degree of susceptibility to natural disasters; and
- Capital markets tend to view small countries as riskier than larger countries.

The above vulnerabilities emphasize the need to maintain lower debt levels than larger countries, and also points to the urgent need to diversify Bermuda's economy.

With our recent borrowings, the annual debt service cost is currently \$127.2 million, claiming 13.6 cents of every dollar of revenue that the government takes in. This level of debt service displaces spending in critically important areas such as education, social services and national security. We must focus on achieving better value from the dollars we expend as our ability to incur additional indebtedness will become increasing

constrained. This underlines the urgent need to balance the budget and eventually pay down on our debt.

In comparable jurisdictions with similar economic challenges, they have been forced, by external forces, to take actions to reduce deficits and put into legislation formal **fiscal rules** to help them reduce both deficits and debt levels.

Despite the pandemic, the government remains committed to the objective of halting the increase in our net debt and subsequently working to reduce debt, in order to attain target ratios for debt to revenue and debt service to government revenue of less than 80% and 10% percent, respectively. It is necessary to note that it will not be possible to achieve these goals without a diversified and growing economy which, in turn, will not only produce balanced economic growth, but also benefits all Bermuda residents.

Application of Fiscal Rules, Targets and Policies

Strengthening fiscal frameworks, in particular **numerical fiscal rules**, emerged as a key response to the fiscal legacy of the global financial crisis. In their recent report, the FRP recommended that the government put in place a fiscal framework with clear rules to ensure fiscal sustainability over the longer term.

What is a fiscal rule?

A fiscal rule imposes a long-lasting constraint on fiscal policy through numerical limits on budgetary aggregates.

What is the objective of a fiscal rule?

Rules aim at correcting distorted incentives and containing pressures to overspend, in particular in good times, so as to ensure fiscal responsibility and debt sustainability.

Providing a credible medium-term anchor has been the pervasive motive for adopting or strengthening fiscal rules policy after the crisis experience.

Types of Fiscal Rules

Four main types of fiscal rules can be distinguished based on the type of budgetary aggregate that they seek to constrain:

1. Debt rules set an explicit limit or target for public debt in percent of GDP.
2. Budget balance rules constrain the variable that primarily influences the debt ratio and are largely under the control of policy makers.
3. Expenditure rules set limits on total, primary, or current spending.
4. Revenue rules set ceilings or floors on revenues and are aimed at boosting revenue collection and/or preventing an excessive tax burden.

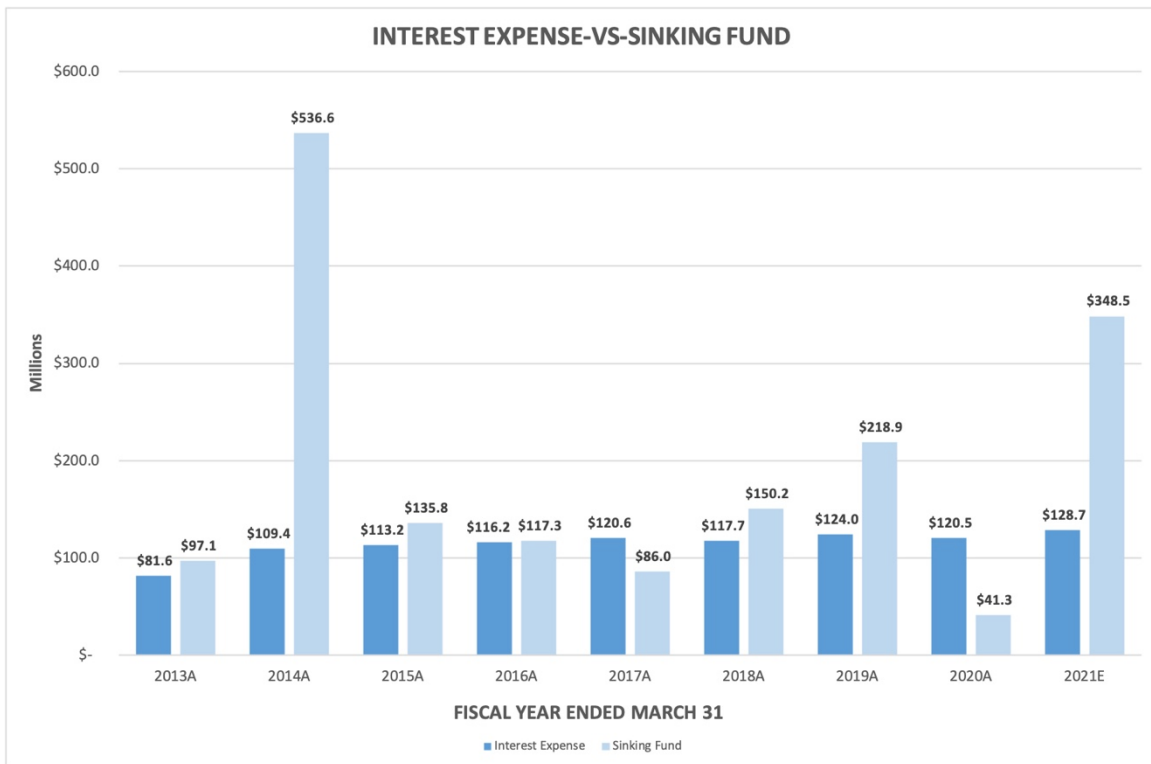
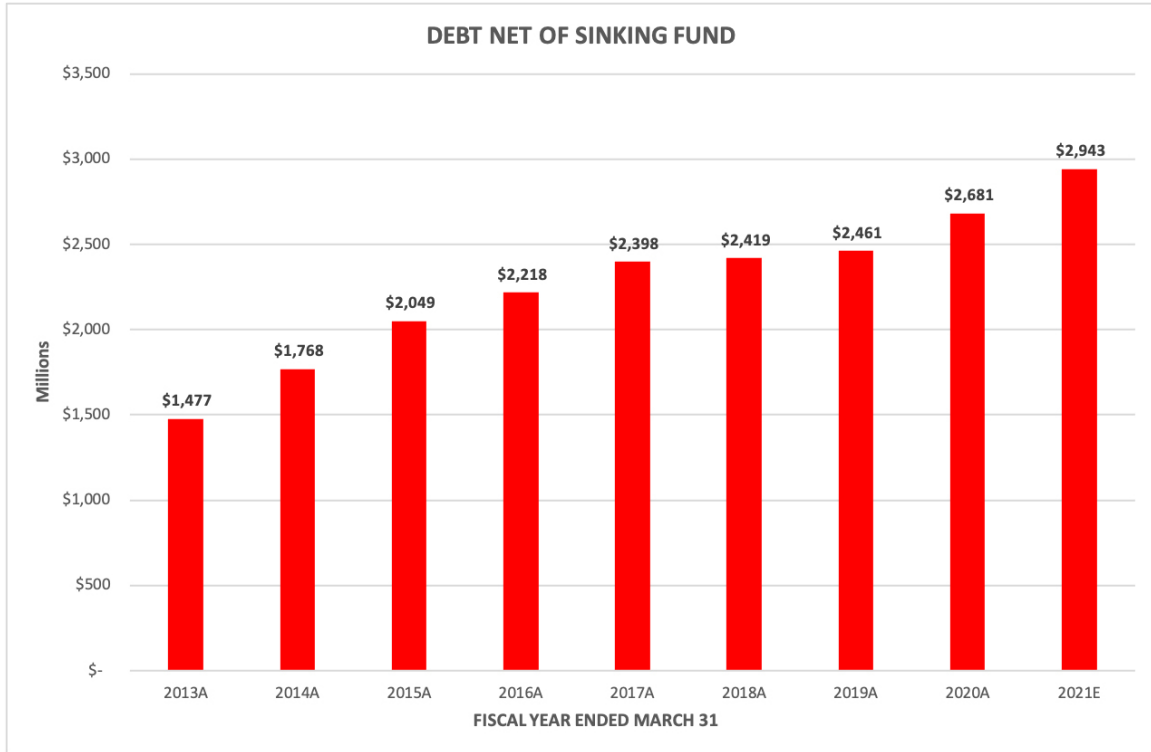
Bermuda's fiscal policy framework is governed by the Constitution, which is amplified in several pieces of legislation, including the Public Treasury (Administration and Payment) Act 1969, the Audit Act 1990, the Government Loans Act 1978, Appropriation Acts and several tax laws which gives the government several powers and responsibilities to collect taxes and fees.

The government has also set up debt-related targets, or rules, that are appropriate for an economy the size of Bermuda's. The government has recognized the desirability of achieving a net debt/revenue ratio that would not exceed 80% and a debt service cost/revenue ratio that would be below 10%. These are targets we would work towards over the medium term.

No explicit fiscal rules are entrenched in the legislation, except with respect to the debt ceiling in the Government Loans Act and annual appropriation Bills.

Fiscal rules and targets are useful to achieve fiscal discipline and by extension, longer term fiscal policy goals. However, even if they are legislated, they should allow some flexibility especially to deal with unforeseen/extraordinary circumstances such as this current economic crisis.

With the above mentioned in mind, the government is considering the recommendation of the FRP to put in place a fiscal framework with clear fiscal rules.



2019/20 Actual Fiscal Review

The total revenue raised by the Consolidated Fund (CF) for fiscal 2019/20, was \$1.086 billion, representing a decrease of \$14.1 million (1.3%) from fiscal 2018/19's total revenue of \$1.100 billion. This was \$32.1 million or 2.9% lower than original budget estimate of \$1.118 billion. The decreases from estimates were primarily attributable to lower collections in customs duties and stamp duty. The most significant generators of revenues for fiscal 2019/20 were Payroll Taxes, accounting for \$465.0 million or 42.8% of total revenue (2018/19 – \$467.5 million or 42.9%) and Customs Duty, accounting for \$221.9 million or 20.4% (2018/19 – \$226.1 million or 20.8%).

Current expenses for fiscal 2019/20 were \$1.392 billion (2018/19 – \$1.187 billion). This was \$204.1 million or 17.2% higher than 2018/19 due to non-recurring items consisting of the valuation provision against the Caroline Bay project; and first time provisions for doubtful collection of amounts due to the CF by other government funds. These amounts were partially offset by net decreases in other expenses.

The three largest components of recurring current expenses were employee costs, grants and contributions, and interest on debt. Total employee costs were \$558.5 million or 40.1% of total expenses (2018/19 – \$550.1 million or 46.3%). Included in this amount is \$78.1 million of non-cash retirement benefits expense. Grants and contributions were \$324.0 million or 23.3% of total expenses (2018/19 – \$319.2 million or 26.9 %) and interest on debt was \$120.5 million or 8.7% of expenses (2018/19 – \$124.0 or 10.4 %).

Total current expenditure on a modified cash basis was \$1.052 billion (2018/19 – \$1.109 billion), which was \$5.4 million more than adjusted budget estimates (2018/19 – \$7.9M less). This overage was primarily due to the following:

- A strategic decision to provide financial support of \$3.0 million to secure winter air service from New York and Boston;
- Subsidy funding of \$7.8 million for the Bermuda Hospital Board as part of the block grant provided to the hospital in relation to the healthcare reform;
- Above budget spends in the Ministries of Public Works and National Security;
- Unbudgeted COVID-19 expenditures; and
- Interest and facility fee costs of \$3.9 million in relation to the borrowing incurred to make good on the Caroline Bay guarantees;

These amounts were offset with savings in materials and supplies, repairs and maintenance, energy, transport and other expenditure line items.

Total capital account cash expenditure was \$67.1 million, which was \$2.4 million higher than the original budget estimate. This increase was due to a delay in the receipt of new buses and additional grant funding provided to the National Sports Centre to resurface the track in anticipation of the CARIFTA games being held in Bermuda in April 2020.

Total capital and current account cash expenditure for 2019/20 was \$1.118 billion, which was \$7.8 million or 0.7% higher than the original budget estimate of \$1.111 billion.

The all-inclusive result from government operations (both current and capital) on an accounting accrual basis for the year ending March 31, 2020, was a deficit of \$346.1 million, \$222.8 million higher than the prior year's deficit of \$123.3 million. This increase was due to extraordinary items relating to valuing the Caroline Bay project and first time provisions for doubtful collections of amounts owed to the CF by other public sector funds or organizations.

There are many non-appropriated expenses included in this figure. If we strip those away, along with the non-recurring items related to the Caroline Bay project, the modified cash all-inclusive results from government operations (on the same basis that is shown in the Budget Book) show a deficit of \$32.5 million. This compares to a surplus of \$7.4 million that was originally budgeted. Therefore, the overall deficit was up by \$39.9 million when compared to the original estimate. The increased deficit is primarily a result of lower than budgeted revenues as COVID began to have a negative impact on revenues in the last quarter of 2019/20. During this fiscal year, the government has continued to prudently manage discretionary current and capital expenditures.

Financial Assets

Financial assets consist of assets available to discharge existing liabilities or to finance future operations. Financial assets decreased by \$12.4 million or 4.1% from last year to \$286.1 million at the end of 2020. Cash decreased by \$397 thousand as a result of the operating, investing, capital, and financing activities shown in the Statement of Cash Flow. Accounts receivable were \$3.1 million higher than the prior year.

The net amount due from government funds and agencies decreased by \$15.1 million or 22.8% from last year. The decrease was due to a provision for doubtful recoveries of \$22.9 million established in 2020, primarily relating to collection uncertainty of a receivable of \$41.5 million from the Government Employees Health Insurance Fund. This was offset by increases and decreases in amounts due from and to other government funds and agencies.

In September and October 2019, the government purchased the lenders' rights in the Tranche B and C loans made to Caroline Bay Limited (formerly Morgan's Point

Limited), George's Bay Limited (GBL) and its subsidiaries for a total of \$168.5 million. The government also purchased an aggregate of 1,500 Class B Non-Voting Participating Common Shares, \$0.01 par value of (GBL). The Government exercised this option, following a formal demand on the guarantee, (as opposed to direct repayment of the guaranteed loans) in order to avail itself of all legal remedies available to the lenders.

In December 2019, the government undertook to settle \$11.1 million outstanding contractors' balances owed by GBL for work performed. In March 2020, the government successfully petitioned the courts to appoint provisional liquidators to implement a corporate restructuring and wind up GBL. The government has a secured claim against the Caroline Bay project assets of GBL as recourse for the Tranche B secured debt and an unsecured claim relating to the Tranche C debts. There is a high level of uncertainty related to the assets of GBL and the cost which will be associated with recovering those assets. While not concluding a nil value to the assets, as there are number of tangible assets which have value, there is uncertainty relating to the expected return which the government may receive after GBL assets are written down or where costs have been incurred to facilitate a sale.

Due to accounting requirements regarding the valuation uncertainty, the government has recorded a nominal value of \$1,000 on the Statement of Financial Position. This is not reflective of the eventual positive return that the government expects it will obtain from the Caroline Bay project, however, that expected return cannot currently be quantified.

Liabilities

Liabilities, consisting of debts or other monetary obligations owing at year-end and to be settled in the future, increased by \$317.1 million from last year to \$4.5 billion. The most significant liability, unmatured debt, increased by \$219.7 million from the prior year mainly due to the establishment of a \$200 million credit facility to facilitate the purchase of the George's Bay Limited lenders in fiscal 2019/20. By year-end, \$187.4 million was drawn on the facility.

Pension and other employee future benefits increased by \$78.1 million due to current year Pensions and Retirement Benefits Expense. Other changes to liabilities included an increase of \$19.3 million in accounts payable and deferred liabilities attributable to an \$18.2 million rise in deferred revenue due primarily to an agreement entered into with a cruise line. The transaction established that the cruise line provided the government with \$15 million in exchange for primary birthing rites for its ships. Under the agreement, use of the \$15 million was restricted to the purchase of two tugboats

(i.e. not available for general expenditure) and is recorded as a deferred amount in the financial statements.

Six-Month Fiscal Performance for 2020/21

The headline numbers for the 2020/21 National Budget, were: a revenue target of \$1.122 billion; current expenditure of \$1.057 billion, including debt service of \$121.4 million; capital expenditure of \$85.0 million; leading to a projected deficit of \$19.8 million.

The public-health measures required to safeguard the health of residents have caused a severe economic shock in the Bermuda economy. The economic impact of COVID-19 has also had a severe knock-on effect on the 2020/21 fiscal performance. The combination of lower fiscal revenues, and higher public spending, will cause the projected 2020/21 budget deficit of \$19.8 million to increase significantly.

Total revenues for the first half of fiscal 2020/21 were \$462.8, \$82.6 million, or 15.1% below the same period last fiscal year. This was due to lower collections in all tax types other than Land Tax, Vehicle Licences & Registration, and Financial Services Tax.

Of significance:

- Payroll taxes were down by \$6.5 million or 2.6%;
- Customs Duty was down by \$31.4 million or 26.2%;
- Passenger Taxes were down by \$26.2 million or 100%; and
- All Other Receipts down by \$10.2 million or 28.3%.

Due to the easing of restrictions, including the opening of our borders, the revenue collections in the second fiscal quarter of this year showed an improvement of just over \$19.5 million when compared to the first fiscal quarter. The Ministry expects revenue collections to continue to improve with increased economic activity.

Current expenditures, excluding debt service and COVID-19 related expenditures, for the six months ending September 30, 2020, are \$35.9 million or 7.7% **lower** than the corresponding prior period ending September 2019. This was due to most expenditure types being down when compared to 2019 as a result of the government's remote working policy.

Of significance:

- Salaries and Wages were down by \$5.7 million or 2.8%;
- Employer Overhead was down by \$6.5 million or 16% due to Government suspending matching contributions into the pension funds;
- Energy costs were down by \$2.2 million or 31%;

- Travel was down by \$1.5 million or 91%; and
- Professional Services were down by \$1 million or 6%.

Significant public resources have been directed to strengthen the healthcare sector and support affected workers and economic sectors.

During the first half of this fiscal year, the government spent \$78.8 million in COVID-19 related expenditures. The majority of this expenditure - \$57.6 million - is connected to the Government's Unemployment Benefit in which we paid benefits to over 10,000 persons. We have also spent just over \$21 million for other COVID-19 related matters to keep Bermuda safe and secure. This included costs related to the following:

- To purchase PPE;
- To provide for COVID-19 testing;
- To embody the Bermuda Regiment;
- To provide for quarantine facilities;
- To provide for enhanced cleaning contracts;
- To provide grant funding for the BEDC Business Sustainability & Continuity Funding Programme;

In this \$21 million, is an amount of \$5.8 million paid to the Bermuda Airport Authority to honour the airport minimum revenue guarantee with Skyport.

When factoring in these COVID-19 related unbudgeted expenses, the total current account expenditure was \$506.7 million, a \$42.9 million, or 9.2%, increase compared to the period ended September 30, 2019.

Total current expenditures, including COVID-19 expenses and excluding debt service, for the six months ended September 30, 2020, are higher than the 2020/21 fiscal year original half-year budget estimate of \$467.8 million.

Capital expenditures for the six months ending September 2020 are \$3.4 million lower than the six months ending September 2019. This decrease was mainly due to the government delaying the start of some capital projects due to COVID-19.

Interest expenses and related facility fees are tracking \$6.1 million higher than in 2019. This is due to higher debt levels after the government's capital raise of \$1.35 billion at historically low rates. This borrowing provides liquidity to the government in support of the impending economic recovery over the next two to three years.

Excluding debt service, the government recorded a \$71.4 million current account deficit for the first six-month period ending September 30, 2020, compared to a \$50.7 million surplus for the same period in 2019.

The all-inclusive deficit was \$135.8 million compared to a deficit of \$7.6 million in 2019. The above-mentioned capital raised financed this deficit.

Net debt at the end of September 2020 stood at \$2.94 billion.

**2020/21 BUDGET PERFORMANCE
FOR THE 6 MONTHS ENDING 30TH SEPTEMBER, 2020**

REVENUE

	2020/21		SEPT 2020/21 (\$000)	SEPT 2019/20 (\$000)	DIFFERENCE (\$000)
	ORIGINAL ESTIMATE	REVISED ESTIMATE			
	(\$000)				
CUSTOMS DUTIES	235,000	183,300	88,375	119,822	(31,447)
PAYROLL TAX	467,000	396,950	245,635	248,386	(2,751)
INTERNATIONAL COMPANIES	66,490	59,706	3,732	3,925	(193)
FOREIGN CURRENCY PURCHASE TAX	26,250	22,313	9,532	12,909	(3,377)
LAND TAX	85,500	72,675	39,199	36,731	2,468
HOTEL OCCUPANCY TAX	10,000	1,500	234	6,160	(5,926)
VEHICLE LICENCES & REGISTRATION	31,060	29,507	14,397	13,441	956
PASSENGER TAX	25,200	-	-	26,371	(26,371)
TRANSPORTATION INFRA. TAX	11,100	-	-	-	-
STAMP DUTY	24,567	20,613	9,287	11,251	(1,964)
CIVIL AVIATION RECEIPTS	17,300	15,570	7,785	8,000	(215)
FINANCIAL SERVICES TAX	12,000	10,200	5,471	5,165	306
TELECOMMUNICATION RECEIPTS	17,876	16,982	8,491	8,677	(186)
IMMIGRATION RECEIPTS	18,367	15,612	5,569	8,476	(2,907)
ALL OTHER RECEIPTS	74,461	69,144	25,084	36,040	(10,956)
TOTAL	1,122,171	914,072	462,791	545,354	(82,563)

EXPENDITURE

	2020/21		SEPT 2020/21 (\$000)	SEPT 2019/20 (\$000)	DIFFERENCE (\$000)
	ORIGINAL ESTIMATE	REVISED ESTIMATE			
	(\$000)				
Current Account Expenditure	935,566	862,566	427,861	463,787	(35,926)
Unemployment Benefit	-	58,000	57,600	-	57,600
COVID-19 Expenditure	-	67,200	21,220	-	21,220
Capital Account Expenditure	85,008	93,000	27,493	30,853	(3,360)
Interest on Debt	121,400	128,750	64,375	58,275	6,100
Sinking Fund Contribution	-	-	-	-	-
TOTAL	1,141,974	1,209,516	598,549	552,915	45,634

DEFICIT	(19,803)	(295,444)	(135,758)	(7,561)
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Revised Budget for 2020/21

COVID-19 impacts have made the 2020/21 budget presented in February in the House of Assembly outdated.

Revenue

The original revenue budget estimate for 2020/21 was \$1.122 billion. COVID-19 has and is continuing to have a significant impact on government revenues due to reduced economic activity in many sectors of the economy and the loss of most tourism-related taxes and levies. The Ministry's revised revenue estimate for 2020/21 is \$914.1 million, a reduction of \$208 million, or 18.5%.

This estimate assumes that revenues based on cruise ship related tourism fall to zero, while revenues from most broadly-based taxes fall by 10% - 22%.

The primary reasons for the mentioned decrease in revenue are due to:

- A decrease in Payroll Tax from \$467.0 million to \$396.9 million, representing a \$70.0 million or 15% reduction;
- A decrease in Customs Duty from \$235.0 million to \$183.3 million representing a \$51.7 million or 22% reduction; and
- A decrease in Cruise Ship Departure taxes and the Transport Infrastructure tax from \$36.3 million to 0, representing a \$36.3 million or 100%

Expenditures

Current Account

In the February Budget Statement, the original current account expenditure (before debt service) in 2020/21 was estimated at \$935.6 million.

Based on submissions by Ministries and Ministry of Finance projections, unbudgeted COVID-19 expenditures for this fiscal year are estimated to be \$125.2 million and consist of the following:

UNBUDGETED COVID-19 EXPENDITURES

(\$000)	
COVID-19 MINISTRY EXPENDITURES	22,000
UNEMPLOYMENT BENEFIT	58,000
SUPPLEMENTAL UNEMPLOYMENT BENEFIT	3,000
FINANCIAL ASSISTANCE	2,000
QUANGO'S ASSISTANCE:	
BEDC	12,000
WEDCO	3,500
GOLF COURSES	3,700
BAA - AIRPORT REVENUE GUARANTEE	21,000
TOTAL EXTRAORDINARY EXPENSES	125,200

The management of public finances has taken on greater significance with the onset of COVID-19. As a result, the Ministry of Finance COVID-19 Fiscal Plan calls for a re-examination and reduction of lower priority budget expenditures to ensure that spending needed for COVID-19 matters are maintained and the deficit is contained. Accordingly, savings have been identified in the following areas:

- Continuing the freeze on the funding of vacant posts that are not required to address COVID-19 or to protect Bermuda's national interests;
- Continuing the ban on non-essential government travel; and
- Reducing all discretionary spending, including grants, consultancy, training, materials and supplies, clothing and uniforms, etc.

To reduce the deficit further, other temporary payroll or government employee overhead savings were identified. Savings have also been identified in several discretionary areas such as grants, consultants, travel, repairs and maintenance, etc. Additionally, to reduce the deficit further, other temporary payroll or government employee overhead savings have been identified and implemented as the government has been in negotiations with the Unions on this matter. At this time, the four largest unions representing over 80% of public sector employees have agreed to the government's cost-saving measures.

To date, just over \$73 million in savings have been identified which are broken down as follows:

(\$000)	
SALARY	15,900
WAGE	4,100
VACANT POSTS	8,000
EMPLOYER OVERHEAD:	
PSSF Contribution (Employer)	19,167
MMPF Contribution (Employer)	833
Social Insurance Contribution (Employer)	6,000
OTHER DEPARTMENTAL OPERATIONAL EXPENSES	19,000
TOTAL CURRENT ACCOUNT EXPENDITURE SAVINGS	73,000

When factoring in the unbudgeted COVID-19 expenditures and savings that have been identified, the revised current account expenditure is **\$987.8 million**, which is \$52.2 million or 5.3% higher than the original estimate.

Capital Expenditures

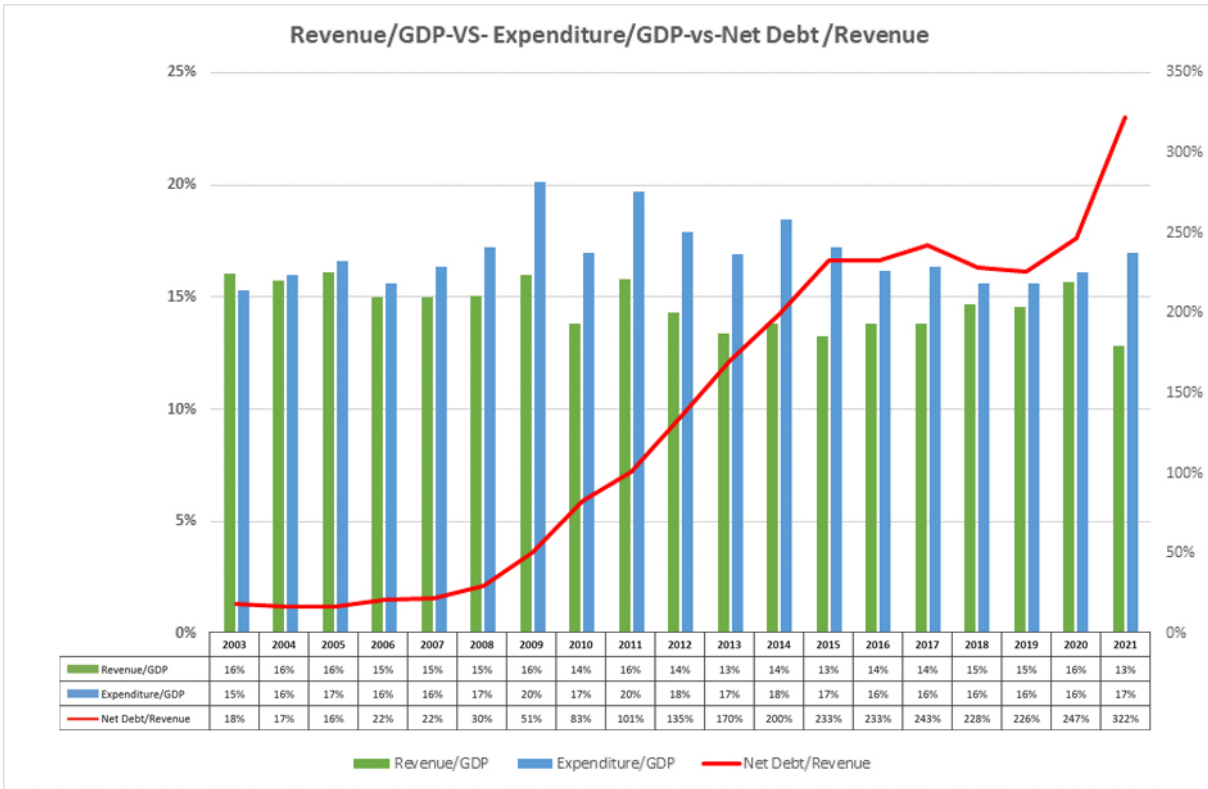
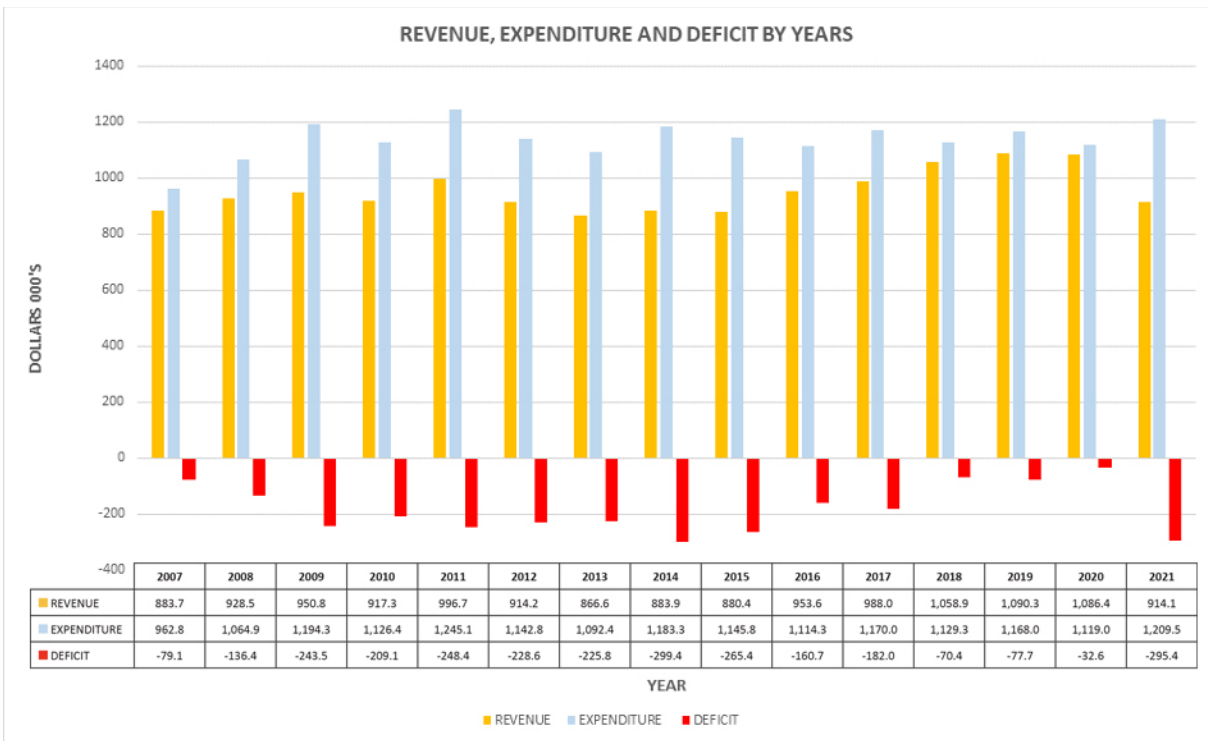
The original capital expenditure component of the 2020/21 Budget was set at \$85.0 million.

Although, when we first encountered the Covid-19 pandemic we made the decision to delay some capital projects that had not commenced, we have revised our approach to support essential capital projects and support certain additional projects. These capital projects will support our economic recovery, provide employment for Bermudians, and improve our quality of life.

In total, the Ministry is providing up to \$93 million in capital development up \$8 million from the \$85 original budget.

**2020/2021 REVISED BUDGET
FOR THE TWELVE MONTH PERIOD ENDED MARCH 31**

(\$000)	ORIGINAL ESTIMATE	ADJUSTMENTS	REVISED
REVENUE	1,122,171	(208,099)	914,072
CURRENT ACCOUNT EXPENDITURE:			
SALARY	353,545	(15,900)	337,645
WAGE	69,407	(4,100)	65,307
VACANT POSTS		(8,000)	(8,000)
EMPLOYER OVERHEAD:			
PSSF Contribution (Employer)	28,750	(19,167)	9,583
MMPF Contribution (Employer)	1,250	(833)	417
Social Insurance Contribution (Employer)	9,000	(6,000)	3,000
OTHER DEPARTMENTAL OPERATIONAL EXPENSES	473,614	(19,000)	454,614
TOTAL CURRENT ACCOUNT EXPENDITURES	935,566	(73,000)	862,566
BUDGET SURPLUS (DEFICIT) BEFORE DEBT SERVICE	186,605	(135,099)	51,506
INTEREST ON DEBT AND OTHER RELATED FEES	121,400	7,350	128,750
CAPITAL EXPENDITURE	85,000	8,000	93,000
BUDGET SURPLUS (DEFICIT)	(19,795)	(150,449)	(170,244)
EXTRAORDINARY EXPENSES:			
COVID-19 EXPENDITURES	-	22,000	22,000
UNEMPLOYMENT BENEFIT	-	58,000	58,000
SUPPLEMENTAL UNEMPLOYMENT BENEFIT	-	3,000	3,000
FINANCIAL ASSISTANCE	-	2,000	2,000
QUANGO'S ASSISTANCE:			
BEDC	-	12,000	12,000
WEDCO	-	3,500	3,500
GOLF COURSES	-	3,700	3,700
BAA - AIRPORT REVENUE GUARANTEE	-	21,000	21,000
TOTAL EXTRAORDINARY EXPENSES	-	125,200	125,200
ADJUSTED BUDGET SURPLUS (DEFICIT)	(19,795)	(275,649)	(295,444)



Chapter 3

The Government's Fiscal Strategy for 2021/22

Framing the 2021/22 Budget

The key factors which will impact upon the framing and composition of the 2021/22 Budget include:

- Uncertainty due to the impact of the COVID-19 crisis on the economy and the government's fiscal position;
- Economic Recovery Measures;
- Government's 2020 General Election Campaign Platform and the 2020 Speech From The Throne;
- Economic considerations;
- Taxation sensitivities;
- Continuing deficits, high debt levels and the debt ceiling;
- Continuation of Zero Based Budgeting that will include a Public Service Value Assessment to provide for a better-quality portrayal of the range of services delivered by the Government of Bermuda;
- Feedback from the Pre-Budget Report in advance of fiscal year 2021/2022;
- Risks facing the country, and
- The implementation of the Government's fiscal strategy; which is to reduce net debt and fully balance the budget by 2023/24.

These factors are vital to the role of the government in terms of determining high policy priorities and establishing a baseline budget allocation.

Preparing the 2021/22 Budget will be challenging given the unprecedented uncertainties in the context of the COVID-19 pandemic. In 2020, the government has taken unprecedented policy actions to redirect existing resources towards health and social support measures. These actions have required unbudgeted COVID-19 expenditures of approximately \$125 million for the current fiscal year. COVID-19 has also had a significant impact on government revenues and the Ministry estimates that revenue yields for 2020/21 will contract by about 18.5% or \$208.1 million. After factoring in the impact of COVID-19, and various austerity measures taken by the government, the revised deficit for 2020/21 is estimated at \$295.4 million. This level of deficit is unsustainable.

At the end of this fiscal year total gross government debt outstanding, will stand at \$3.35 billion.

Based on the Ministry's macroeconomic impact model, it is estimated that real GDP, as a result of COVID-19, could potentially contract by 7% to 9% using a moderate scenario in calendar year 2020. Under this scenario real GDP should stabilize in 2021 with growth returning in 2022.

Given the current economic circumstances and uncertainty, due to COVID-19, it would be imprudent to anticipate an overly aggressive increase in revenues for 2021/22. On the contrary, there are likely to be further appeals for government tax relief due to the pandemic. Ministry of Finance's most optimistic forecast is for revenue growth of between 7.5% - 10% which would be mainly driven by post COVID-19 economic recovery, minor fee increases and the new Travel Authorization Fee. On this basis, total revenue of between \$970 million to \$990 million might be anticipated in 2021/22. This amount represents an increase of up to \$80 million over the revised revenue target for 2020/21. Included in this amount are fees related to the newly introduced Travel Authorization Fee in accordance with the Quarantine (COVID-19) (NO. 3) Amendment (NO.4) Order 2020 of \$8 million. Additionally, since the biennial government fee increase was not conducted last year, Ministries will review fees under their remit to ensure there is reasonable cost recover for the service offered.

Controlling government expenditure has been, and still remains a focus of the government. In the Government's 2017 Election Platform there was a call for increased Government efficiency in order to control government expenditure, as opposed to across-the-board cuts. In this regard, in order to determine high policy priority programmes the Budget Office reintroduced Zero Based Budgeting (ZBB) in the last fiscal year. Policy prioritization at the start of the budget process will facilitate a better alignment of the allocation of limited resources with government's overall policy initiatives and objectives.

The ZBB exercise in developing 2020/21 estimates was able to capture critical data in order to examine all services provided by the government. In order to improve on the quality of the data provided the ZBB form has been refined further to ensure all services are clearly identified and the characteristics of those services can be correctly analysed. The ZBB data will ultimately provide an inventory of all services provided across the government to both its internal and external beneficiaries. This will be a shift from functional to service-centric budgets.

In an effort to meet the expenditure target, as required by the Government's Medium Term Expenditure Framework, various payroll related measures are proposed in the 2021/22 Budget. These include:

- Removing funding for lower priority vacant public sector posts; and
- Offering the early retirement eligibility plan to employees aged 55 years.

Other factors that the Government must take into consideration are as follows:

- Government debt levels and the debt ceiling;
- Excess Funds from the recent debt issuance;
- Austerity measures taken by the Government that will continue in the 2021/22 fiscal year;
- Ongoing COVID-19 obligations required for health, social support, and economic recovery measures;
- Other commitments of the government.

The Ministry of Finance proposes to set the total current account appropriation, less debt service and COVID-19 expenditures at between \$875 - \$903 million; \$60.6 or \$32.6 million below the budgeted expenditure approved in 2020/21.

This level of spending will enable the government to execute on its priorities of educating our children, providing healthcare and security for our citizens and assistance to the less fortunate. It will also allow us to provide targeted investments to assist with our economic recovery in a fiscally prudent and responsible manner. Bermuda has responded well to the immediate challenges of COVID-19, and therefore, the 2021/22 budget will be focused on rebuilding our economy.

This government's economic plan has always been rooted in growing the twin pillars that have served the Bermuda economy well: financial services and tourism.

Other areas of focus in this plan include; diversifying the Bermuda economy in an effort to attract companies in growing industries; implementing measures to reduce the cost of living and doing business in Bermuda; making the government more efficient; and reducing regulations and bureaucracy to stimulate investment while promoting competition in the Bermuda economy.

Continuing with these principles will ensure that our economy recovers and grows, as it did before the pandemic.

It is important that the scope of our economic recovery plan be broad-based covering both measures to sustain economic activity and structural reforms including immigration. Policy measures will target our most critical and prospective economic sectors and will involve the following:

- Supporting the recovery of tourism & business travel;
- Supporting and expanding international business;
- Encouraging business development and economic diversification - Bermuda's emerging Tech Sector and advanced financial regulatory framework will be capitalized on as opportunity.

Based on the latest submissions by Ministries and Ministry of Finance estimates, continuing COVID-19 expenditures are estimated at between \$20-\$25 million for fiscal year 2021/22. These amounts will be provided as a contingency and will cause the total current account appropriation to increase to between \$895 - \$928 million.

The government remains committed to balancing the budget. However, if unrealistic targets are established and not met, this undermines the credibility of the government pertaining to public commitments on cost control. Actual comparable current account expenditure for the last seven years is as follows:

(\$000)	Fiscal Year Ended March 31,							
	2013	2014	2015	2016	2017	2018*	2019	2020
Fiscal Year								
Current Expenditure	998.8	970.9	935.1	902.2	914.3	892.9	921.2	931.4
Percentage change	-	-2.79%	-3.69%	-3.52%	1.34%	-2.34%	3.17%	1.11%

* Includes one-off \$25 million reduction in Bermuda Hospital Board Subsidy and the Government's pay award to public officers, which cost the government approximately \$9 million.

As shown above, current account costs have been reduced materially over the years without layoffs of workers in the public sector. It has become increasingly difficult to implement further cost reductions under the current government structure.

Based on the original 202/21 budget, 52.4% (\$490.6 million) of the current account expenditure (excluding debt service) represents employee costs and 33.4% (\$312.9 million) relates to grants and contributions.

This means that 85.9% (\$803.5 million) in total is spent on these 2 cost items. Accordingly, there are very few other expenditure types that can be reduced and have a material impact on the level of spending without reducing the level of services.

The plan for capital outlays should also be prioritized and remain within the range of \$60 - \$70 million. This level of spending will maintain the country's infrastructure and create jobs.

Uncertainty is inherent in budget preparation, however, for fiscal year 2021/22 it is much higher than usual because of increased volatility in revenues and uncertain expenditure needs due to COVID-19. Therefore, the government must strike the correct balance between providing flexibility on uncertain spending needs, without undermining budget credibility.

If the mentioned budget measures are implemented, the projected deficit for 2021/22 could be in the range of \$126.5 million - \$155.5 million compared to an estimated deficit of \$295.4 for fiscal year 2020/21.

In setting the overall strategy for the upcoming budget, governments should recognize and adapt to the exceptional degree of macroeconomic uncertainty and its impact on revenues and opt for a prudent approach.

The tables below show two illustrative fiscal scenarios. They represent possible outcomes based on the fiscal strategy that the government selects.

STRATEGY 1

	ORIGINAL ESTIMATE 2020/21 (\$000)	COVID-19 ESTIMATE 2020/21 (\$000)	ORIGINAL ESTIMATE 2021/22 (\$000)
Revenue and Expenditure Estimates			
Revenue	1,122,171	914,072	970,000
Current Account Expenditure (excl. debt service)	(935,566)	(862,566)	(903,003)
COVID-19 Contingency	0	(125,200)	(25,000)
Current Account Balance (excl. debt service)	186,605	(73,694)	41,997
Interest on Debt	(121,400)	(128,750)	(127,500)
Surplus (Deficit) Available for Capital Expenditure	65,205	(202,444)	(85,503)
Capital Expenditure	(85,008)	(93,000)	(70,000)
Budget Surplus (Deficit)	(19,803)	(295,444)	(155,503)

STRATEGY 2

	ORIGINAL ESTIMATE 2020/21 (\$000)	COVID-19 ESTIMATE 2020/21 (\$000)	ORIGINAL ESTIMATE 2021/22 (\$000)
Revenue and Expenditure Estimates			
Revenue	1,122,171	914,072	980,000
Current Account Expenditure (excl. debt service)	(935,566)	(862,566)	(889,003)
COVID-19 Contingency	0	(125,200)	(22,500)
Current Account Balance (excl. debt service)	186,605	(73,694)	68,497
Interest on Debt	(121,400)	(128,750)	(127,500)
Surplus (Deficit) Available for Capital Expenditure	65,205	(202,444)	(59,003)
Capital Expenditure	(85,008)	(93,000)	(67,500)
Budget Surplus (Deficit)	(19,803)	(295,444)	(126,503)

Policy Options Under Consideration for 2021/22 Budget

The following are **considerations** for inclusion in next year's budget. One of the main objectives of a pre-Budget statement is to provide a document that elicits discussion from stakeholders. Prior to finalising the budget, the government will hold public forums and meetings with stakeholders and discuss the ideas outlined below.

Payroll Tax

Continue to provide Payroll Tax relief to troubled sectors during the pandemic

The government has implemented several emergency measures to assist businesses that have a pressing need for financial relief as a result of this pandemic. We have provided short-term relief from payroll tax to assist the restaurant, bar, hotel and taxi sectors. The fiscal implications of these actions will be a reduction of government revenue, however, this relief has eased some of the pressure on these sectors and especially lessens the pain being experienced by many Bermudians who work in these sectors. To maintain employment levels in these sectors, the government will be considering extending this relief during the upcoming budget session.

Incentive for Job Creation

In 2018, the government amended the Payroll Tax Act 1995 to legislate the Government's "**tax incentives to grow jobs**" programme, the objective of this programme was simple: to have more jobs based in Bermuda, providing more opportunities for Bermudians who are looking for work or who may want to progress in their careers.

This legislation specifically provided payroll tax relief for the tax periods from 1 April 2018 to 31 March 2021 for employers who increased their total number of full-time employees when compared to the total as at March 31, 2018. The relief is for the employer portion of payroll tax and is only applied against new additional employees hired between April 1st 2018 and March 31 2021. Initially, this proposal was for exempt undertakings and any other employer with a payroll exceeding \$1,000,000 that are liable to payroll tax at the standard rate and are not receiving other payroll tax relief.

International Company Fees

The Registrar of Companies (ROC) is actively going through a transitional period. The breadth and depth of the ROC's regulatory responsibilities is wide and has been increasing

in recent years, with Economic Substance being a new addition from 2019. Fulfilling these responsibilities will require short term investment and a higher cost base going forward. Without this investment, e.g. in digitisation, the government believes that Bermuda will fall behind competitive jurisdictions and the perceived value-for-money that Bermuda offers will be eroded. Accordingly, the ROC has completed a holistic review of the Department's corporate fee structure. This review included a comparative fee analysis between Bermuda and other competitive jurisdictions. The ROC will start consultation with key stakeholders on this fee structure in advance of any amendments to fees.

Biennial Fee Increase

Since the biennial Government fee increase was not conducted last year, Ministries will review fees under their remit to ensure there is reasonable cost recover for the service offered. Some of the fees to be reviewed are court and boat mooring fees amongst others.

Customs Duty

The Retail Shops (Temporary Customs Duty Relief) Act 2008 provides a zero rate of customs duty on imported capital goods intended for the renovation and refurbishment of retail shops. This exemption has been in effect since April 1, 2008 and many properties have benefited from the Act. This relief expires on March 31st 2021. To continue to assist retailers, the government is considering extending this relief for a further 5 years and is also considering extending the scope of goods that are receive under the Act.

Land Tax

The Land Valuation Department has postponed their quinquennial revaluation of land, after which a 2020 Draft Valuation List was to be produced. The List was to be published on 31st December, 2020 and come into effect for land tax purposes on 1st January, 2021.

Accordingly the 2015 Valuation List will remain in force for 10 years, Land Tax revenue is secure and not affected and rates and bands will remain as is.

The government emphasises that the policy options listed above are for discussion purposes and that no decisions on any of the above for the 2021/22 budget have been made. During the months of January and February, the government will hold public meetings on the above policy options to encourage public debate and discussion on the priorities for the 2021/22 budget. The government welcomes feedback on this report, as we look to involve as many as possible in the Open Budgeting Process.

Historical Economic and Fiscal Information

As of or for fiscal year ended March 31 (except as specified)

	2010/11	2011/12	2012/13	2013/14	2014/15	2015/16	2016/17	2017/18	2018/19	2019/20
Bermuda's economic data										
Nominal GDP	6,312.7	6,378.2	6,465.7	6,413.90	6,654.50	6,899.90	7,142.30	7,224.30	7,484.1	6,941.5
Nominal GDP growth (%)	-4.9%	1.0%	1.4%	-0.8%	3.8%	3.7%	3.5%	1.1%	3.6%	-7.3%
Population	63,193	62,408	61,954	61,777	61,735	63,791	63,892	63,973	64,027	64,055
Population growth	-0.4%	-1.2%	-0.7%	-0.3%	-0.1%	3.3%	0.2%	0.1%	0.1%	0.0%
GDP per capita	99,896	102,202	104,363	103,823	107,791	108,164	111,787	112,927	116,890	108,368
Inflation	2.7%	2.4%	1.8%	2.0%	1.5%	1.5%	1.9%	1.4%	1.75%	1.00%
Real GDP growth (%)	-3.7%	-5.3%	-0.3%	-3.7%	0.8%	-0.7%	3.6%	-0.4%	0.5%	-8.50%
Unemployment	6.0%	8.0%	7.0%	9.0%	7.0%	6.0%	6.0%	5.2%	5.2%	5.2%
Government profit and loss data										
Revenues	996.7	914.2	866.6	883.9	880.4	953.6	988.0	1,058.9	1,090.3	1,086.4
Expenditures	1,245.10	1,142.80	1,092.45	1,183.30	1,145.80	1,114.3	1,170.0	1,129.3	1,168.0	1,119.0
Surplus (deficit)	-248.4	-228.6	-225.9	-299.4	-265.4	-160.7	-182.0	-70.4	(77.7)	(32.6)
Interest expense	56.3	67.6	81.6	109.4	113.2	116.2	120.6	117.7	124.0	120.5
Sinking fund	18.3	25.7	30.8	37.6	47.7	52.2	58.4	62.1	64.2	-
Government balance sheet data										
Total debt	1,088	1,351	1,574	2,305	2,185	2,335	2,484	2,568.9	2,680.0	2,722.2
Sinking fund balance	85.5	114.7	97.1	536.6	135.8	117.3	86	150.2	218.9	41.3
Net debt	1,002.0	1,236.3	1,476.9	1,768.4	2,049.2	2,217.7	2,398.0	2,418.70	2,461.10	2,680.90
Guarantees	210.8	207.3	278.6	515.4	519.1	698.5	541.4	533.5	567.5	421.1
Government cash flow data										
Capital expenditures	121	59.5	63.5	65.4	49.8	43.7	76.7	56.6	58.6	67.1
Loan proceeds	264	264	223	731	(120)	150	149	84.9	111.1	42.2
Increase in sinking fund	21	29.2	-17.6	439.5	-400.8	-18.5	-31.3	64.2	68.7	-177.6
Net increase in debt	243.1	234.3	240.6	291.5	280.8	168.5	180.3	20.7	42.4	219.8
Government financial ratio data										
Debt service ratio	7.5%	10.2%	13.0%	16.6%	18.3%	17.7%	18.1%	17.0%	17.3%	11.1%
Net debt/GDP	15.9%	19.4%	22.8%	27.6%	30.8%	32.1%	33.6%	33.5%	32.9%	38.6%
Surplus (Deficit)/GDP	-3.9%	-3.6%	-3.5%	-4.7%	-4.0%	-2.3%	-2.5%	-1.0%	-1.0%	-0.5%

Chapter 4

COVID-19

Actions taken by the Government

Since December 2019, infections attributable to COVID-19 have been reported around the world. On March 11, 2020, the World Health Organization (the “WHO”) characterized the COVID-19 outbreak as a pandemic. Measures to mitigate the spread and intensity of the outbreak have been undertaken by governments around the world, including mandatory quarantines, travel restrictions, social distancing and curtailment or suspension of economic and other forms of activity.

The Bermuda Government adopted several measures in response to the COVID-19 outbreak aimed at preventing mass contagion and overcrowding of Bermudian health service facilities, which included placing severe restrictions on business and economic activity, and movement of people.

The government has been successful in addressing this health crisis, in turn allowing the economy to reopen, while protecting the population.

During this period, the government has supported the functioning of essential sectors, provided resources for people hit by the crisis, and taken steps to limit excessive economic disruption by providing support to businesses.

The government has taken decisive measures to support the economy and its citizens during this period.

The Government’s COVID-19 - Fiscal Plan has provided timely and targeted fiscal stimulus to various components of our economy, as needed. The government has taken urgent, and appropriate, action to reduce hardship and prevent business failures. Some of the actions taken include the following:

Ministry of Finance COVID-19 Fiscal Plan		
POLICY INITIATIVE	DESCRIPTION	\$AMOUNT
Debt ceiling	Raised Debt Ceiling to \$2.9 billion	\$150M addt'l
Borrowing Capacity	Available Government borrowing	\$220M
Emergency COVID-19 Funding	Executed \$20 million & \$150 million credit facilities	\$170M
Debt ceiling	Raised Debt Ceiling to \$3.5 billion	\$600M addt'l
Emergency COVID-19 Funding	Issued \$1.35 billion of Senior Notes	\$450M new
Emergency COVID-19 Funding	Additional Ministry Funding for COVID-19 Expenditures	\$22M
Unemployment Benefit		\$58.5M
Supplemental Unemployment Benefit		\$1.5M
Increase Financial Assistance		\$2.5M
Business Sustainability & Continuity Funding Prog.	Govt/BEDC Financial Support to SMEs	\$12M
Assistance to other Quangos	WEDCO and Golf courses	\$7.2M
National Pension Scheme	Voluntary Withdrawal from Private pension plan	Up to \$12K
National Pension Scheme	Suspension of Employee and Employer contributions	
Social Insurance	Suspension of Employee and Employer contributions	
Tax Relief:		
Payroll Tax , Corporate Service Tax,	Extension of filing deadline for businesses	
Payroll Tax	Short-term relief for restaurant and bar sector 0% rate	
Payroll Tax	Short-term relief for hotel sector 0% rate	
Land Tax	Short-term relief for hotel sector 50% of rate	\$1.2M/YEAR
Government Fee Regulations/Penalties	Fees may be waived or differed upon request	
Customs Tariff	Duty relief for PPE and supplies	\$2M Duty Relief
Customs Tariff	Duty deferment retailers/commercial importers	
Payroll Tax	Short-term relief for Taxi Operators 50% of Tax	\$0.3M
Other COVID Related Cost:		
Airport Revenue Guarantee		\$21M

Without these stimulus measures the overall economic contractions would be far worse.

Chapter 5

Conclusion

Commitment to Budget Transparency

This PBR represents a step forward in the preparation of budgets and the formulation of budget policy in Bermuda. To meet international best practice for budget transparency, the International Budget Partnership recommends that governments publish eight budget reports during the budget cycle. The documents and the government's commitments are below:

- 1. Pre-Budget Report:** This document is the government's fifth PBR. It is recommended that this document be issued at least one month prior to the Budget Statement to allow adequate time for public feedback to assist in budget policy formulation.
- 2. Budget Statement:** The government issues budget statements annually. This practice is a matter of custom and will continue.
- 3. Citizens' Budget:** A Citizens' Budget is a non-technical presentation that "can take many forms but its distinguishing feature is that it is designed to reach and be understood by as large a segment of the population as possible". A Citizens' Budget is a simplified summary of the budget designed to facilitate discussion. The government has issued a guide to the budget in the past and will issue this document with the 2021/22 Budget Statement.
- 4. Enacted Budget:** The Enacted Budget is the appropriations bill which is passed by the legislature annually, as required by the Bermuda Constitution.
- 5. In-year Reports:** The government currently issues quarterly fiscal performance reports and will continue to do so.
- 6. Mid-year Review:** The government currently issues a Mid-year Review and will continue to do so.
- 7. Year-end Report:** The government does issue financial statements once they have been audited as per the Bermuda Constitution. The government also provides highlights of the financial statements by way of a Ministerial Statement in the House of Assembly. The government commits to developing and releasing a more comprehensive report by way of a Financial Statement Discussion and Analysis document at the same time as its annual financial statements.
- 8. Audit Report:** The Auditor General currently issues an Audit Report annually.

It is the aim of the government to provide all of these reports during the coming budget cycle and 2021/22 fiscal year. In publishing this document and conforming to international standards of budget transparency, this government reaffirms its commitment to good governance.

Feedback

The government invites and welcomes feedback on this document. In addition to electronic communication, the government will hold public meetings in January and February 2021 to discuss the principles laid out in this document and to solicit public feedback.

Comments can be emailed to: openbudget@gov.bm



GOVERNMENT OF BERMUDA

Ministry of Finance