



2017

Barbados

Budget

Commentary

May 30, 2017

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Managing Partner's Message



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On May 30, 2017, The Financial Statement and Budgetary Proposals were delivered to the Honourable House of Assembly by The Hon. Christopher P. Sinckler MP, Minister of Finance and Economic Affairs.

KPMG is delighted to be able to present our post-budget commentary on Barbados' 2017 Financial Statement and Budgetary Proposals.

The proposals concentrated on measures designed to extract liquidity from the system, curb consumer spending and dampen demand for imported goods, all geared towards the preservation of our foreign reserves and the management of our debt position.

In this post budget commentary on the fiscal measures announced by The Honourable Minister we offer our analysis for your consideration.

We hope that our remarks stimulate discussion on how this budget affects us as individuals and our country as a whole. We are once again reminded that the success of our economy depends on the cooperation of the Government, the Private Sector and the wider community.

Please contact us should you require clarification on any of the matters discussed in this document.

Carol Nicholls
Managing Partner
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Executive Summary

The Right Experience
The Right People
The Right Relationships

Executive Summary



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In commencing his May 2017 Financial Statement and Budgetary Proposals, the The Hon. Christopher P. Sinckler MP, Minister of Finance and Economic Affairs drew a comparison to similar economic circumstances 25 years ago, the sacrifices that were required and the courage and leadership of then Prime Minister Lloyd Erskine Sandiford. The Minister admitted that *"the state of our economy is not yet where it should be"*, and that while there has been some progress, the country now needs to enter a phase where growth is faster and higher.

Historically the Barbados government has made significant expenditures on social services – including education, healthcare, water, public transportation, sanitation, community development services and social welfare – but the country must now strike a balance between maintaining the social and economic fabric of society, and observing fiscal prudence.

While there was modest growth of 1.6% and 2% at the end of 2016 and quarter one of 2017, respectively, the fiscal deficit remained at (6%) of GDP at the end of quarter one of 2017. Concomitantly, international reserves stood at approximately \$705.4 million reflecting an import reserve cover of 10.7 weeks at the end of quarter one. However, this was still below the 12 week benchmark.

The Minister went on to outline various initiatives that will be launched in the coming months including:

- the launch of the duty free zones initiative;
- amendment to the Housing Incentives Act (reflecting additional concessions for developers of low income housing); and
- amendment of the Special Development Areas Act.

Continued deficit and cost of financing

Despite a number of growth initiatives in recent years, the biggest challenges facing the country and constraining growth are the fiscal deficit and the low foreign exchange reserves. Efforts to contain non-interest expenditure have been relatively successful, but interest expense has grown cumulatively by \$4.2 billion over the past seven years, driven almost exclusively by the high deficit financing.

For the current fiscal year, government anticipates a number of challenges in financing the deficit, especially given the objective of planned reduction in Central Bank financing.

Compounding this fact, is that servicing of this growing level of debt has been eroding the level of foreign reserves. More importantly, the deficit has been further impacted by the mix of financing between domestic and foreign.

Over the last few years, Barbados has also been experiencing a number of credit agency downgrades (see Economic Dashboard, page 6). This has essentially impacted the mix of fiscal deficit financing and the cost of financing the deficit itself.

There has been a skew towards more expensive local financing when compared to the historical mix of cheaper US dollar financing along with Barbados dollar financing. As such, the weighted average historical cost of financing was lower than current levels.

Executive Summary

National Fiscal, Economic and Social Development Restructuring and Enhancement Programme

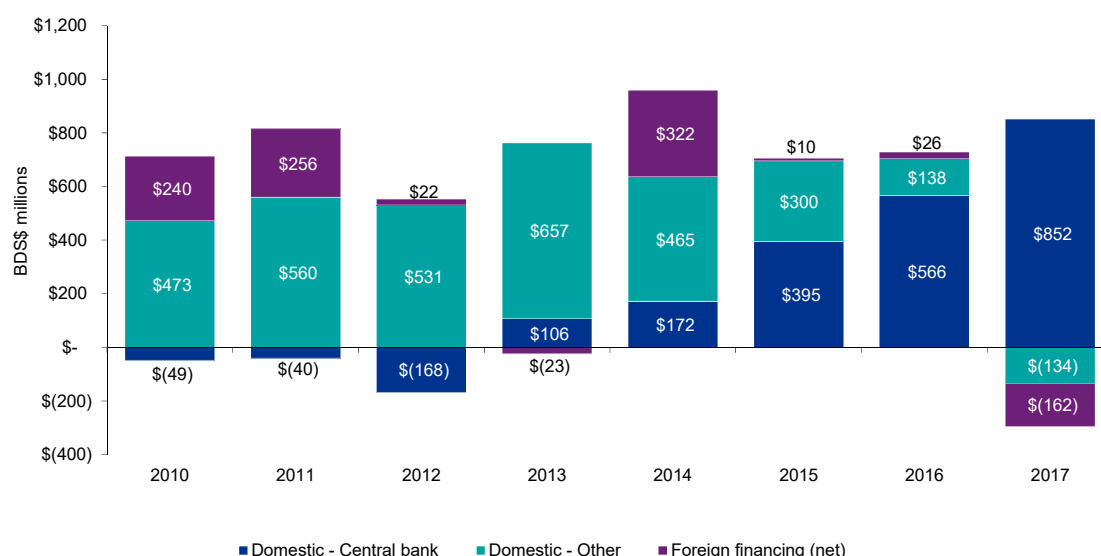
The Minister continued to highlight that the above noted Programme will be published in the coming weeks along with other proposals. Key items included are noted below:

- boosting foreign exchange earnings;
- implementing productive sector reform by reducing the cost of doing business in critical sectors;
- instituting a Competitiveness Awareness Commission and Operational Unit;
- implementing a new national energy policy;
- implementing fiscal consolidation through: Public Financial Management reform including the passage of the Financial Management and Audit (State Owned Enterprises or "SOEs") Act;
- reforming SOEs, including: mergers, operational consolidation and divestment;
- completing tax policy reform and tax administration upgrade;
- stabilising debt growth and reduction through fiscal reform, debt management and debt profiling; and
- reforming key social sectors such as: health, education, sanitation, social care and environmental protection.

With this in mind, the **objectives of the specific measures** of the budget mirror the above Programme while considering the following specific factors:

- protecting the level of foreign reserves;
- completing the fiscal consolidation process by achieving a balanced budget on the current account with at a surplus of at least 5% for three fiscal periods;
- reducing the net financing requirement for government and by extension reducing the need for Central Bank financing;
- slowing the growth of the national debt and over time reducing it to below 100% of GDP;
- placing Barbados on a path to regaining a healthy credit rating that would permit the country to retain the option of accessing the international capital markets for reasonable financing in the near future; and
- strengthening investor confidence.

Financing Mix



Executive Summary

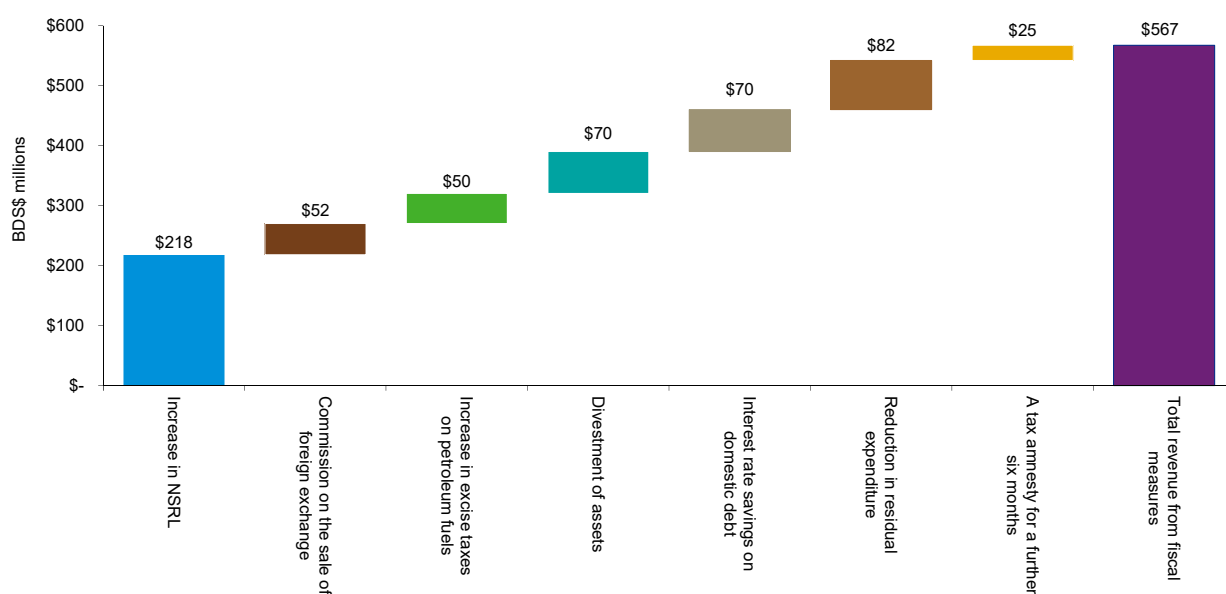
Summary of revenue and expenditure budgetary measures

The chart below outlines the proposed measures as outlined by the Minister of Finance in the May 30, 2017 budget. We discuss these in more detail on the following pages.

The measures are expected to reduce the fiscal deficit by \$567 million, through a combination of increased revenues, expenditure savings and divestment proceeds – this would lead to a small fiscal surplus of \$4.4 million, and reduce the Central Bank financing requirement by \$640 million, to only \$87 million. In addition, the government anticipates that the measures will dampen imports, reduce the demand for foreign currency, and stem the decline in foreign exchange reserves.

We note that the increase in the rate of the National Social Responsibility Levy (“NSRL”) and the commission on the sale of foreign exchange as proposed, represent over 50% of the total revenue to be generated during fiscal 2017-2018.

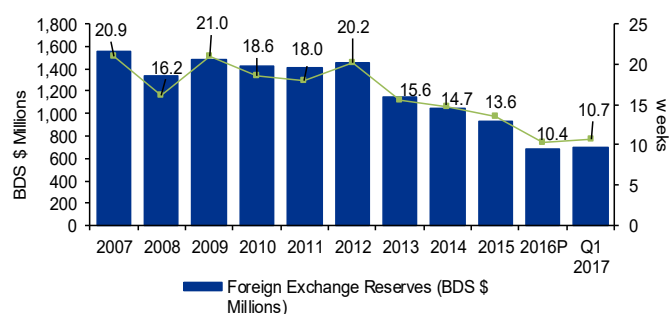
Revenue and expenditure budgetary measures



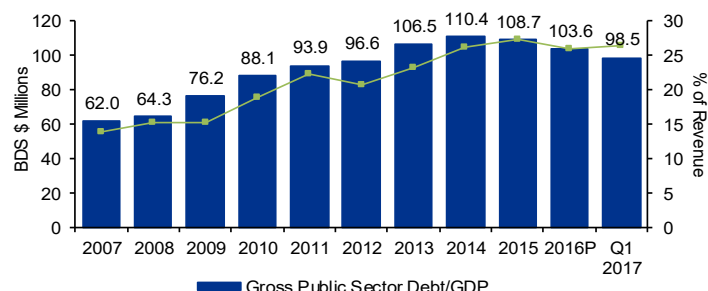
Source: The Financial Statement and Budgetary Proposals - 2017

Executive Summary

Foreign Exchange Reserves and Cover



Gross Government Debt/ GDP and Government Interest Payments (as a % of revenue)



Economic Dashboard												
	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016P	Q1 2017
Economic Indicators												
Real Growth (%)	5.7	1.7	0.3	-4.0	0.3	0.8	0.3	-0.6	0.1	1.0	1.6	2.0
Inflation (%)	7.3	4.0	8.1	3.6	5.8	9.4	4.5	1.8	1.8	-1.1	1.3	na
Foreign Exchange Reserves (BDS \$ Millions)	1,194.1	1,549.9	1,343.3	1,477.4	1,423.7	1,414.8	1,457.7	1,144.1	1,052.4	927.0	681.1	705.4
Foreign Exchange Reserves, cover weeks	16.0	20.9	16.2	21.0	18.6	18.0	20.2	15.6	14.7	13.6	10.4	10.7
Average unemployment (%)	8.7	7.4	8.1	10.0	10.3	11.2	11.5	11.6	12.3	11.3	9.9	na
Summary of Government Operations												
Revenue as a % of GDP	29.8	31.5	28.6	28.2	25.3	25.6	29.3	28.4	26.7	27.7	29.3	30.3
Expenditure as a % of GDP	32.9	35.4	38.7	33.0	32.5	34.3	33.7	36.9	37.7	35.8	37.5	36.4
Fiscal Deficit as a % of GDP	-2.7	-3.4	-4.9	-4.8	-7.3	-8.8	-4.4	-8.5	-11.0	-8.1	-8.2	-6.0
Public Debt												
Gross Public Sector Debt/GDP	59.5	62.0	64.3	76.2	88.1	93.9	96.6	106.5	110.4	108.7	103.6	98.5
Government Interest Payments (as a % of revenue)	14.7	13.9	15.3	15.3	18.8	22.3	20.7	23.2	26.1	27.2	25.9	26.3
Ratings												
Standard & Poor's	BBB+	BBB+	BBB+	BBB	BBB-	BBB-	BB+	BB+	B	B	B-	CCC+
Moody's	Baa2	Baa2	Baa2	Baa3	Baa3	Baa3	Ba1	Ba3	B3	B3	Caa1	Caa3

Source: Central Bank of Barbados Press Conference on Barbados' Current Economic Performance - May 9, 2017

Note: P - provisional
Note: na - not available



Budget Commentary

Key:



Positive



Negative



Both Positive and Negative

Tax Services

Anticipate. Innovate. Deliver.

Budget Commentary

Commission on Foreign Exchange Transactions



Proposal/ key changes

The Minister stated that as at March 2017, the foreign exchange import cover stood at 10.7 weeks and proposed that a broad-based foreign exchange commission be charged on all sales of foreign currency at a rate of 2%.

This will extend to inter alia, all wire transfers, credit card transactions and over the counter sale of foreign currencies.

Anticipated additional revenues were noted as being \$140 million for a full financial year and \$52.5 million for the remaining nine months of the current fiscal year.

Timing

Effective July 1, 2017

Our view

This measure will further impact businesses in a country that already has exchange controls on foreign currency transactions. This will result in a widespread increase in prices.

No exemptions for special scenarios such as payments for educational and medical purposes have been mentioned.

Who is affected

All persons seeking to transact business in foreign currency; importers of goods and consumers in general.

National Social Responsibility Levy



Proposal/ key changes

The NSRL rate is to be increased from 2% to 10%. Designed to finance the cost of health care, the Minister stated that the revenues raised have come close to the targets set. Based on the 2016 budgetary proposals the NRSL was set to raise \$60.8 million.

Additional revenues are now anticipated to be \$292 million for a full financial year and \$218 million for the remaining nine months of the current fiscal year.

Timing

Effective July 1, 2017.

Our view

Again this proposal will further increase the cost of doing business and will negatively impact the purchasing power of consumers.

While this measure is likely to be unpopular, its imposition may be justified to address important social objectives.

However the Minister has not indicated whether the funds raised will be used solely to meet health care objectives and to maintain a clean environment as originally envisaged, but noted that the revenues raised may fund other critical areas of social service provisioning.

Who is affected

Importers and businesses immediately; ultimately all consumers.

Budget Commentary

Tax Amnesty



Proposal/ key changes

The Minister proposes a tax amnesty on VAT and Land Tax for the period June 1, 2017 to November 30, 2017.

Taxpayers will benefit from a waiver of penalties and interest on taxes owing to the Barbados Revenue Authority and the rules as previously imposed should apply (as republished by the Barbados Revenue Authority).

Proceeds from this initiative are to directly assist with the liquidation of income tax refunds owed to taxpayers by the BRA.

The previous proposal provided for a waiver of payments of penalties, interest and other charges, where the taxpayer settled the outstanding principal on or before the prescribed date of February 15, 2017.

Timing

June 1, 2017 to November 30, 2017.

Our view

Based on experience with the previous amnesty, this measure should achieve favourable results.

The Minister has not specifically mentioned corporation tax and individual income tax in the proposal.

Who is affected

Entities and individuals who are in arrears.

Excise Tax on Gasoline and Diesel Fuels



Proposal/ key changes

The Minister proposes to increase the excise tax:

Excise Tax	Increase \$	From \$	To \$
Gasoline	0.25	0.74	0.99
Diesel	0.24	0.20	0.44
Retail Price	Increase \$	From \$	To \$
Gasoline	0.05	3.00	3.05
Diesel	0.10	2.15	2.25

Timing

Effective June 1, 2017.

Our view

This will result in an increase in prices, especially in sectors heavily dependent on fuel.

Who is affected

All consumers.

Budget Commentary

VAT



Proposal/ key changes

The Minister proposes that the Barbados Revenue Authority, Ministry of Finance and Economic Affairs, Treasury Department and Central Bank of Barbados collaborate and design a VAT factoring programme to attend to the issue of arrears in VAT refunds.

No further details were provided.

Timing

Details of the programme are to be revealed in the near future with the hope of commencement before October this year.

Our view

This program is an initiative to alleviate the backlog of VAT refunds and in so doing, improve the cash flow of businesses who have been experiencing delays in receiving their VAT refunds. It is a welcome initiative if implemented in the short-term.

Who is affected

VAT registrants who are due refunds.

Duty Free Zones



Proposal/ key changes

The Minister proposes to launch the duty free zones across a number of locations in Barbados.

This measure was proposed in the 2016 budgetary proposals to facilitate the creation of duty free shopping zones in Barbados to enable Barbadians and visitors alike to make purchases in foreign currency only. Possible areas were noted as City of Bridgetown, Holetown, Hastings/Worthing and the two main ports of entry.

No further details were provided.

Timing

August 2017.

Our view

This proposal would serve to increase economic activity in these areas. However, this may lead to a reduction in sales for merchants who operate outside of these proposed exclusive zones.

Who is affected

Visitors and locals.

Budget Commentary

Tax Administration



Proposal/ key changes

The Minister proposed to establish a special task force unit within the Barbados Revenue Authority for the purpose of establishing a national tax administration registration initiative.

This measure is geared towards bringing into the tax net, persons operating businesses, the self employed, professionals, sole traders, and artisans not already registered.

Timing

Definitive timeline not provided.

Our view

This measure should ensure that government does not rely only on existing taxpayers (most of whom are employed persons), to shoulder the tax burden, but will broaden the tax base.

The ability to generate additional tax revenue is contingent upon these additional taxpayers having the capacity to generate earnings.

Who is affected

Individuals, professionals and self employed persons.

State Assets



Proposal/ key changes

The Minister proposed to raise the revenue through a divestment programme which will include the following:

- Sale of **Barbados National Terminal Company Ltd.** – this is an ongoing matter which requires the approval of the Fair Trading Commission to effect net proceeds of \$70 million.
- Sale of the **Hilton Hotel at Needham's Point** currently under the portfolio of Needham's Point Holding Ltd. – Government expects to receive no less than \$100 million as net proceeds from the sale.

The Minister also spoke to the construction of the Sam Lord's Castle resort to be operated by Wyndham – an investment in the range of US\$250 million with borrowings from EXIM Bank of China.

Timing

Fiscal year 2017- 2018.

Our view

We welcome the government's initiatives as they relate to the generation of foreign currency and the reduction of the fiscal deficit. While there may be long term gains to be made from obtaining dividends from a now profitable Hilton, we recognise that the government is seeking more immediate inflows of foreign exchange.

The government needs to mitigate all risks associated with the completion of the transactions in a timely manner.



KPMG

Caricom

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Our Practice Information

KPMG Globally

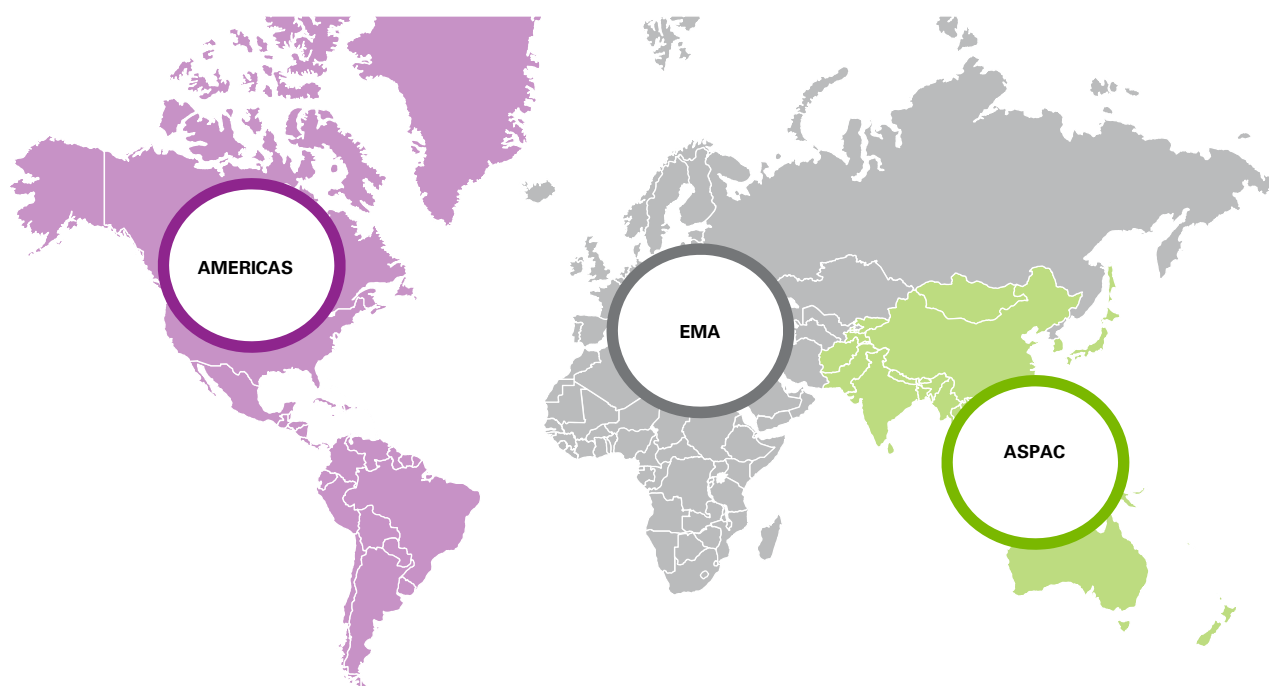
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Global capability and consistency are central to the way we work. By providing global organizations with the same quality of service and behavior around the world, we can work with them wherever they choose to operate.

Our industry focus helps KPMG people to develop a rich understanding of clients' businesses and the insight, skills, and resources required to address industry-specific issues and opportunities.

Our history spans three centuries and features a number of significant mergers, leading to the merger of Peat Marwick International and Klynveld Main Goerdeler, and their individual member firms, in 1987. Today, KPMG is a truly global organization, with operations in 152 countries and territories.

KPMG's global network is arranged into three operating regions – the Americas; Europe-Middle East-Africa (EMA); and Asia-Pacific (ASPAC).



Our Practice Information

KPMG Regionally

Our regional governance entity, called KPMG Caricom, was formed in 2004, with members comprising the KPMG member firms in the Barbados and the Eastern Caribbean and Trinidad and Tobago.

KPMG Caricom is a member of KPMG Islands Group, a regional network of KPMG member firms all of which have similar cultures and operating environments, providing audit, tax and advisory services with more than 2,000 professionals to deliver value to clients in:

Antigua and Barbuda	The Bahamas
Barbados	Bermuda
British Virgin Islands	Cayman Islands
Gibraltar	Guernsey
Isle of Mann	Jamaica
Jersey	Malta
Saint Lucia	Saint Vincent and the Grenadines
Trinidad and Tobago	Turks and Caicos Islands





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