

Bermuda Budget Release 2005

“.....a Budget that will indelibly mark the record of our tenure as the Government of Bermuda that deftly balanced stability with innovation in this brave new world of change and challenges.”

The Hon. Paula A. Cox, J.P. M.P. began the delivery of her second budget with the above statement. She concluded with “Our future success will depend on our continued resilience, our continued prudence, and the courage to make bold steps in furthering the ‘Social Agenda’. This means that every one of us must be involved as we build our nation: A Bermuda for Everyone ... Everyone for Bermuda.”

This was the theme of the budget which essentially saw no significant tax increase, a fine tuning of employment tax for small businesses, confirmation of stamp duty relief already announced,

and continued initiatives to stimulate tourism.

The major change is an increase in the debt ceiling and continued capital projects which account for 91% or \$125 million of capital asset investment leaving \$12 million for new capital projects.

The budget contemplates ongoing major capital projects, including the areas of education and seniors’ care. While attention to the Social Agenda will provide long-term benefits, the short-term consequence is an increase of the debt by \$85 million to \$216 million - which appears to approach record high levels.

It is noteworthy that employment levels continue to increase significantly in the areas of international business and the construction sector. Government appears to have maintained employee levels at rates not exceeding those of the general economy.

The Finance Minister can be commended for the budget that has applied limited tax changes to fund the ongoing spending initiatives. Caution is warranted that expenditures on existing and future capital programs may contribute to exacerbate existing inflationary pressures through increasing wage scales and increases in the costs of living.

Economic Performance

The original estimated revenue for 2004/05 of \$693.9 million has been revised upwards to a figure of \$738.5 million (an increase of 6.4%). Similarly the projected revenue for 2005/06 has been estimated at approximately \$750.5 million (an increase of 1.6% on the Revised 2004/05 figures). The major revenue sources contributing to this favourable outcome were payroll tax (\$24.0m), stamp duties (\$11.6m) and customs duty (\$2.7m).

In line with the increasing revenues current account expenditures are rising. However, the expenditure rates (excluding debt servicing costs and sinking fund contributions) are rising at a higher rate, with percentage increases of over 5% between 2003/04 and 2004/05 and a percentage increase of approximately 6.6% anticipated between 2004/05 and 2005/06. The scale of the increases reflects the additional resources that the Government has deployed to realise the goals and objectives of the 'Social Agenda'.

Preliminary estimates of GDP growth in 2004 indicate a better than anticipated expansion of nearly 3 per cent following the 2.1 per cent increase in GDP in 2003.

The overall employment level has increased by 1.5% in 2004 compared with a flat performance in 2003. The increase represented an additional 573 jobs bringing the total to 38,259. The international business sector continued to show strong growth with a 8.3% increase compared with 5.3% in 2003. The construction, hospitality and public sectors posted increase in employment levels (8.6%, 3.3 and 3.8% respectively) Declines were recorded in the wholesale (1.5%), retail (2.3%) and most significantly, local manufacturing that showed a reduction of 5.5%.

During 2004 consumer price inflation averaged 3.6% compared to 3.2% in the prior year. The price increases were driven by higher sustained increases in oil prices, healthcare increases and higher education costs for private schools. The inflation increases in Bermuda paralleled the developments in the United States as the upward pressure of prices continues to be a factor for both countries. The weak dollar and continuing high oil prices driving up the cost of Bermuda's imports from the main

trading partners could result in inflation reaching 4.0% in 2005.

The Main Tax Effects

Payroll Taxes

- New tiered system for small/medium businesses for payroll between \$200,000 to \$1million. Top rate remains at 13.5%.
- Social Insurance contributions to be increased by 4.75% with effect from August 2005.

Property

- No ARV increases.
- Elimination of stamp duty/estate tax on the primary family home-stead with respect to deceased estates.
- Residents in the municipal area of St. George's will not be required to pay property taxes to the Corporation in 2005/6.

Senior

- Further pension increase of 3.5% in August 2005.
- No land tax for seniors over 65 occupying their own homes.

Household

- No bus/ferry fare increases.
- No vehicle license fee increases.

Social

- New community areas programme.
- Customs duty relief on imported capital goods for recognised national sporting bodies, and clubs and community organisations for renovating/refurbishing or constructing sports facilities.

Focus on Tourism

'The outlook for tourism in 2005 is positive and exciting

The 2005/06 budget focuses on a business-like tourism strategy supported by a budget of \$37 million, a similar level to the previous year.

Key concepts:

To increase tourism's economic impact as it relates to on-island expenditure and public sector revenue

To grow the number of visitor accommodations and direct air access gateways

To increase the number of Bermudians employed in the hospitality sector

To develop and diversify the tourism product

Specific goals include increasing air arrivals to 400,000 over the next 3 years, increasing average visitor spending by 7 per cent and increasing visitor 'complete satisfaction' indicators by 10 per cent. Strategies include continued work to decrease airfares, the development of new geographic markets in Europe and South America and positioning Bermuda as a year-round destination.

Proposed Sunday opening hours were cited as being of benefit to tourist initiatives, and small businesses in the tourism industry will benefit from the new tiered payroll tax structure. In addition, cruise ship passenger arrival tax rates have been decreased from a flat \$60 to \$20 per day per passenger to encourage 1 day cruise ship visits.

The Queen's Warehouse in St. George's will be restored as the World Heritage Visitors Centre to revive cultural tourism in St. George's.

Social Agenda

Government continues to stress their Social Agenda to enhance the well-being and welfare of all Bermudians through the sustainable development of our economy and community.

Healthcare

- Health and wellness clinics for seniors in Somerset, Warwick, Pembroke and St. George's; community-based home assessments for seniors and assistance with home modifications for seniors to provide for independent living.
- Integration of the National Drug Commission as a department of the Ministry of Health.
- Funds are allocated to establish a Women's Treatment Facility to enable on-island rehabilitation.

Culture

- Continuing funding for "Grass Roots Programme"

- Funding for 500th Anniversary of Bermuda, \$1 million over 4 years to St. George's Foundation to assist with World Heritage Visitor's Centre.
- Provision of customs duty relief on imported capital goods for recognized national sporting bodies or clubs engaged in renovating sports facilities for the community.

Education

- A grant to the National Training Board to assist with the implementation of the Tech Quest 2000 Project to provide technical skills to unemployed individuals.
- Establishment of a Mature Student Further Education Fund.
- Expansion of the Child Development Services to ensure cohesive services for children from birth to end of Primary One.

Housing

- Affordable housing for Bermudia families.

- 160 units are planned in Pembroke, Sandy's and St. George's.
- Emergency housing units are planned with the assistance of a gift of \$1million from Bank of Bermuda/ HSBC Group.

Environment

- Continuation of the Community Areas Program (CAP) to upgrade local environments and to stimulate community spirit.

Other Programs

- Pledge to set aside \$1 million as a Bermuda Birthright Fund to be set aside for tomorrow's retirees.
- Work to continue on St. George's Residential Care Facility and the Senior Secondary School.
- Work to start on Hamilton Police Station and Lefroy House refurbishment.

Impact on Business

Bermuda businesses are facing increased external economic challenges due to the continued weakness in the US dollar against the currencies of Bermuda's trading partners. This has the effect of increasing imports resulting in higher prices for businesses and households with potential of annual inflation reaching 4%.

Regulation is a key area of focus to ensure that Bermuda's reputation as a major player in the global financial services arena is maintained. Bermuda companies have not yet been subject to legal suits in the investigations into the insurance sector in New York but it is believed that this will have an impact on the future number of incorporations of large re-insurance companies in Bermuda.

The economic outlook for Bermuda remains buoyant and the momentum is expected to be maintained in 2005. The number of planned construction projects will ensure that the construction sector will remain robust. Interest rates are expected to remain at historically low levels .

The Public Housing Act will be amended allowing all stores to open between 1pm and 6pm on public holidays, other than Christmas Day and Good Friday.

The Government continues to work towards stimulating new start up businesses and assisting small businesses in managing and containing costs. The key concessions in this area relate to amendments to the Payroll Taxes Act and the Customs Tariff Act.

Payroll amendments:

- A tiered structure (based on payroll costs)
 - Upto \$200,000 – 7.25%
 - \$200,000 - \$500,000 – 10.75%
 - \$500,000 - \$1,000,000 – 12.75%
 - \$1,000,000m + - 13.5%

Customs amendments:

- Amendment to Customs Procedural Code to give relief to small business promotional and marketing strategies
- Zero rate of duty on all imported equipment supplies and machinery by registered farmers.
- Reduction in the rate on fresh greenery to 22.25%
- Reduction in raw form of PVC goods, such as window shutters, to 10%

The Government has extended the customs relief for capital imports used in renovations, refurbishments and new restaurant developments to March 31, 2009.

Economic Figures

“...It is our challenge and our opportunity to continue to do all we can as Government to ensure that the economy works for the people of Bermuda.....”

The economic figures in this table have been adjusted to reflect actual figures for the prior years. Percent changes relate to original estimate. Please note that the Government now uses current market prices for GDP calculations.

The following highlights significant components of the 2005/2006 budget:			
	04/05 Revised \$m	05/06 Est \$m	% Change
Revenues	738.5	750.5	1.6
Current Account Expenditures (Excluding Debt and Sinking Fund)	654.4	697.7	6.6
Capital Expenditures	110.4	137.0	24.1
Budget Surplus	(37.5)	(97.7)	160.8
Debts and Guarantees	131.4	216.3	64.5
The economic figures in the table below have been adjusted to reflect actual figures for prior years			
	2003	2004	2005
Population (Estimate)	62,000	62,000	62,000
GDP (at constant market prices (1996), \$b)	4.0	4.1	4.2
GDP per Capita (\$)	63,973	65,892	67,704
% Change	3.9	3.0	2.5-3.0
	03/04	04/05	05/06
Current Account (\$)			
Revenue	705.5	738.5	750.5
Expenditure (Excluding Debt and Sinking Fund)	621.8	654.4	697.7
Balance	83.7	84.1	52.8
Current Account Expenditure per Capita (\$)	10,028.9	10,554.1	11,252.5
% change	11.2	5.2	6.6
Capital Expenditure (\$m)	82.2	110.4	137.0
Capital Expenditure per Capita (\$)	1,326.6	1,780.8	2,210.2
% Change	16.2	34.2	24.1

% changes relate to revised estimate/actual as appropriate

This briefing is intended as a general guide to the Budget 2005. It is not intended to be comprehensive and should not be used as a basis for decisions. For that purpose advice should be obtained which takes into account all the client's circumstances.

Every effort has been made to ensure the accuracy of the information contained herein. In view of its purpose the reader will appreciate that we, the Bermuda firm, are unable to accept liability for any errors or omissions which may arise.

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