حكومة مملكة البحرين

Government of Bahrain

Update of the Fiscal Balance Program

البحرين

BAHRAIN

Overview

The Fiscal Balance Program was launched in 2018 with the overall objective to achieve a fiscal balance by 2022 through 6 initiatives:

1. Public expenditure reductions
2. A voluntary retirement scheme for government employees
3. Balancing the Elecetricity & Water Authority (EWA) expenditures and revenues
4. Streamlining the distribution of cash subsidies
5. Targeting inefficient operational government expenditures
6. Simplifying government processes and increasing non-oil revenues

Progress on the Implementation of the Fiscal Balance Program Initiatives

As of the end of Q3 2021, significant progress has been made across all six initiatives of the Fiscal Balance Program, as described below:

1 Public expenditure reductions

Seven government task forces were established to oversee all operational purchase requests across different spending categories in order to achieve cost reduction targets, in addition to revising operational cost spend policies. The task forces reviewed 21,264 purchase requests since their inception and until the end of Q3 2021 with the aim of maintaining the operational expenditures level as stated in the state budget.

2 A voluntary retirement scheme for government employees

The scheme was successfully completed with 8,214 government employees now retired, representing 18% of the public sector workforce, and achieving a cost saving of BD130 million per annum.

3 Balancing the Electricity & Water Authority’s (EWA) expenditures and revenues

A fiscal transformation plan proposed by EWA has been approved. In 2018 EWA had an allocated budget of BD 189mn; and with fiscal balance expected to be achieved by 2022, the balance has been factored into the 2021/2022 State Budget.

4 Streamlining the distribution of cash subsidies

Previously, social programs that involved cash subsidies comprised of multiple allowances typically disbursed by multiple entities. These cash subsidies have now been consolidated through one central government financial subsidies system to be made towards eligible citizens which is an important part of ensuring fairness and improving quality of life.

5 Targeting inefficient operational government expenditures

The Ministry of Finance and National Economy was restructured with the addition of a Debt Management Office and several new Directorates including a Central Government Procurement Directorate, which has successfully completed a number of central purchasing tenders, and a Central Efficiency Directorate. In addition, all finance directors across all Government entities now report to the Shared Financial Services directorate of the Ministry.

6 Simplifying government processes and increasing non-oil revenues

The VAT implementation commenced from 1 January 2019 at a rate of 5%. As of the end of Q3 2021, over 19,000 companies and government owned entities were registered, with high compliance rates of over 97% recorded in relation to VAT return submission and VAT collection.

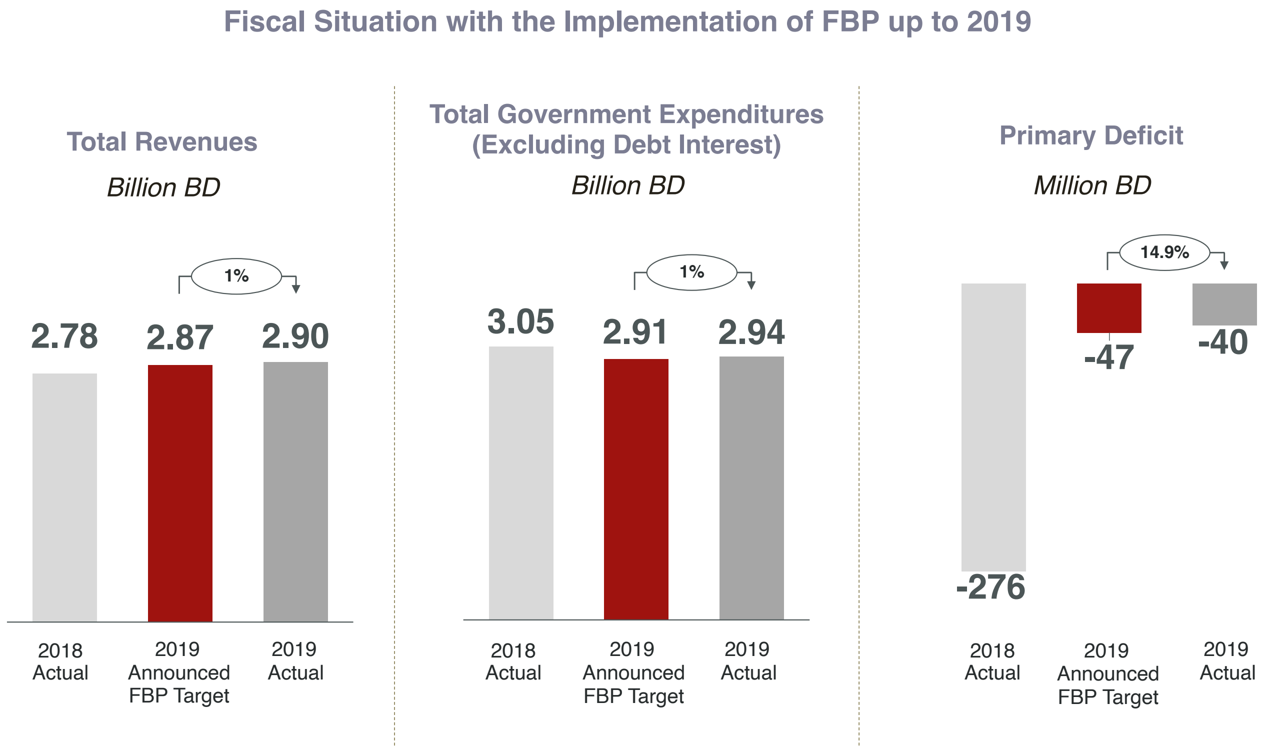
In addition, the Government has implemented a number of programs aimed at simplifying and improving its services including:

- The updates to the Commercial Registration Portal (SIJILAT) & Building Permits Approval system (BENAYAT), which witnessed significant enhancements including integration with additional government entities, further simplifying and streamlining of application processes, and revising content to feature up to date licensing requirements
- Launching the government service centres evaluation program “Taqyeem” which aims to enhance the performance of public services by emphasizing the importance of innovation within government work streams to ensure optimal performance and service delivery excellence
- The formation of the Legislation Development Committee which oversees the drafting of new legislation
- Overhaul of the legal system with a focus on digital transformation, with the transitioning of services across the various litigation steps to electronic services, the implementation of the case management system in commercial courts and the review of legislation to mirror best practice
- The adoption of the Digital Government Strategy that applies digital technologies extensively to improve government services delivery
- Documenting and publishing all government services procedures on online portals, and introducing in place service level agreements (SLAs) to ensure the quality of the government services offered, with ongoing reviews of established SLAs.

Lower international oil prices and the economic impact of the Coronavirus (COVID-19) pandemic have impacted the results for the financial year 2020 and for the first half of 2021. The government remains committed to achieving fiscal balance and has made significant progress on the implementation of the Fiscal Balance Program. In addition, a number of new initiatives have been identified to achieve fiscal balance in the medium term.

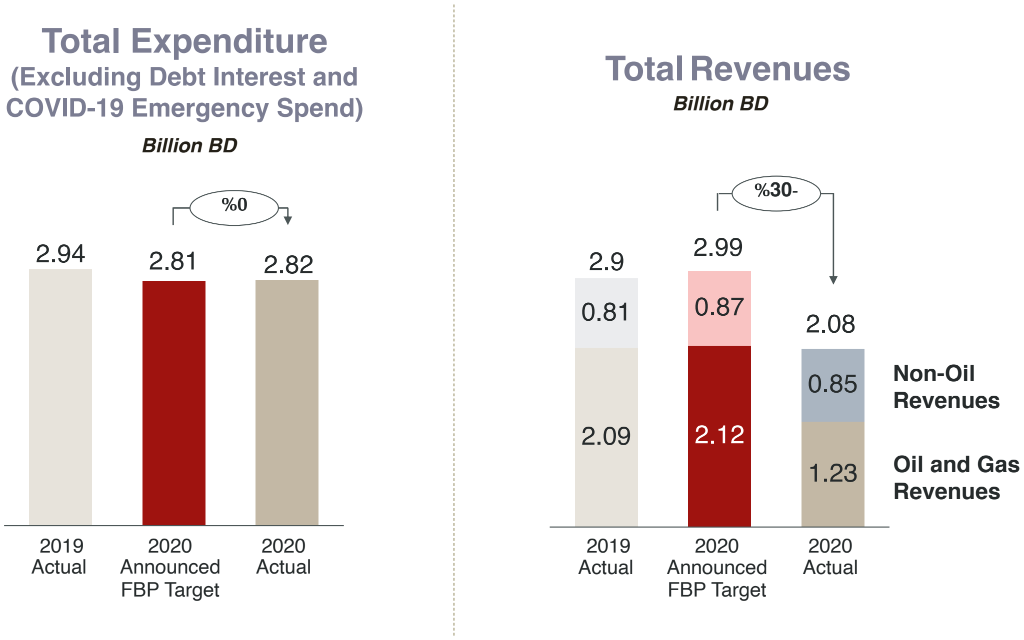
Fiscal Situation - 2019 to end of Q3 2021

With the implementation of the Fiscal Balance Program initiatives, the Kingdom of Bahrain has made significant progress in reducing its primary deficit during the fiscal year 2019:



The Kingdom's commitment to the fiscal balance program enabled it to absorb the COVID-19 emergency spend into the approved 2021/2022 state budget, with minimal overspend in both 2020 and the first half of 2021. However, oil and gas revenues were significantly impacted by the decrease in global oil prices and the impact of the COVID-19 pandemic on economic activity domestically and internationally.

Control Government Expenditure during COVID-19 pandemic



If no additional measures are taken, the fiscal situation is expected to improve slightly; driven by the recovery in the economy and commodities prices. However, the total deficit is expected to remain high, reaching BD1.3 billion in 2021 and BD1.1 billion in 2022.

Revised Forecasts

Considering the period impacted by the COVID-19 pandemic and the lower oil and gas prices, the Government plans to further cut spending and increase non-oil revenues with the aim of achieving:

Overall fiscal balance by 2024, a 2-year extension of the original Fiscal Balance target

The revised targets and the additional measures follow the same principles of the Program launched in 2018, namely:

Government started with addressing its own fiscal challenges and reducing its operational costs

Maintaining social support to citizens most in need

Continuing to provide government services in an efficient manner

Furthermore, the revised targets are based on a commitment to further build on the achievements to date and to deliver the savings from all initiatives previously announced under the Program.

In addition, the Kingdom of Bahrain is taking the necessary steps to comply with international best practices in combating base erosion and profit shifting, while maintaining the Kingdom's position as an attractive destination for foreign direct investment, given that the Kingdom of Bahrain is among the countries in the "comprehensive framework of the OECD / G20 on Base Erosion and Profit Shifting (BEPS), which joins the statement on a two-pillar solution to address the tax challenges arising from the digitization of the economy as of August 31, 2021". The framework is expected to enter into force in 2023 and pledges to guarantee a minimum corporate income tax of 15% globally.

The main initiatives of the revised plan include:

Expenditure Rationalization Measures:

- **Reducing recurrent non-manpower expenditure**
- **Reducing project spend**
- **Reducing manpower expenditure**
- **Streamlining the distribution of cash subsidies to citizens**

Revenue Enhancement Measures:

- **Increasing Government owned entities annual contributions**
- **Adjusting commodities prices and prices of services provided to companies**
- **Introducing new Government services revenue initiatives**
- **Increasing the VAT to 10%**

Expenditure Rationalization Measures:

Reducing recurrent non-manpower expenditure

Further spending cuts of government recurrent expenditure will be conducted to maximize efficiency of spending.

Reducing project spend

Project spending will be reviewed and prioritized without impacting major projects.

Reducing manpower expenditure

Government entities will be restructured in order to streamline resources and increase manpower efficiency.

Streamlining the distribution of cash subsidies to citizens

Following the consolidation of the multiple cash subsidies programs which allowed thorough analysis to be conducted, the Government will work with the Legislative Authority to enhance the efficiency of support for eligible citizens.

Revenue Enhancement Measures:

Increasing Government owned entities annual contributions

The increase planned from 2023 will include the annual contributions paid by the Oil and Gas Holding Company (nogaholding), Bahrain Mumtalakat Holding Company, Eskan Bank and the Telecommunications Regulatory Authority, as well as the introduction of contributions from the Bahrain Tourism & Exhibitions Authority.

Adjusting commodities prices and prices of services provided to companies

Establishing a mechanism to review and adjust commodities prices and prices of the services provided to companies on a periodic basis to ensure they are in line with market price.

Introducing new Government services revenue initiatives

Non-oil revenue growth is expected to be driven by a newly established Revenue Development Taskforce that the Government set up, including the introduction of new fees for services currently provided and the introduction of a number of new services.

Increasing the VAT to 10%

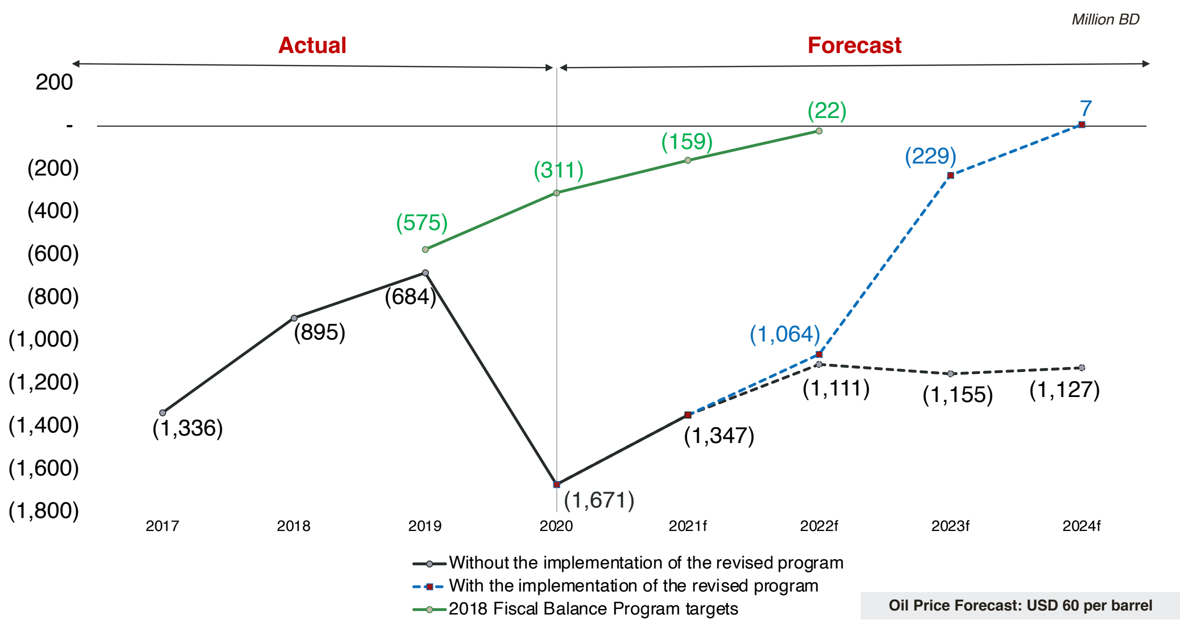
The Government has approved a draft bill to double the value-added tax to 10%, and has sent the relevant legislation to parliament for approval to amend the value-added tax rate, currently at 5%, from 1 January 2022. Existing VAT exemptions on certain sectors, basic food commodities and +1,800 government services will remain.

Key Performance Indicators

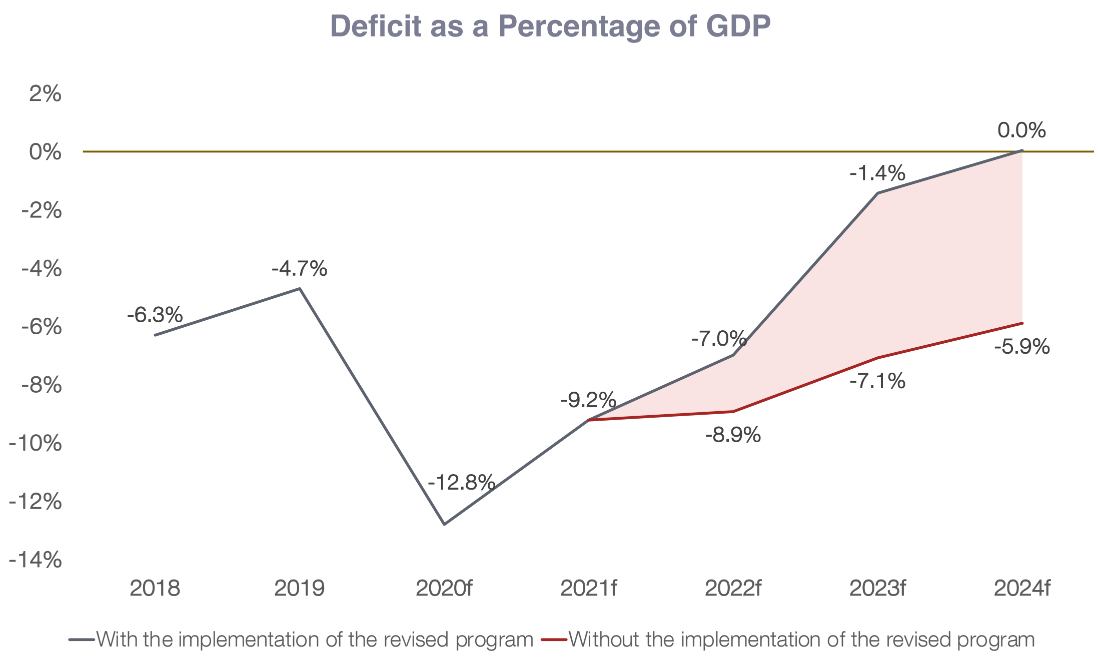
The Government has set revised targets to regularly assess its performance and the effectiveness of implementing the initiatives under the updated Fiscal Balance Program (FBP).

The implementation of the FBP in 2018 aimed to reduce overall fiscal deficits by 2022. However, due to the decrease in oil prices in 2020 and the Covid-19 pandemic, deficits reached BD 1.67 billion in 2020. It is forecasted to move towards a positive trajectory continuously starting from 2021 until achieving fiscal balance by 2024.

Overall Fiscal Deficit

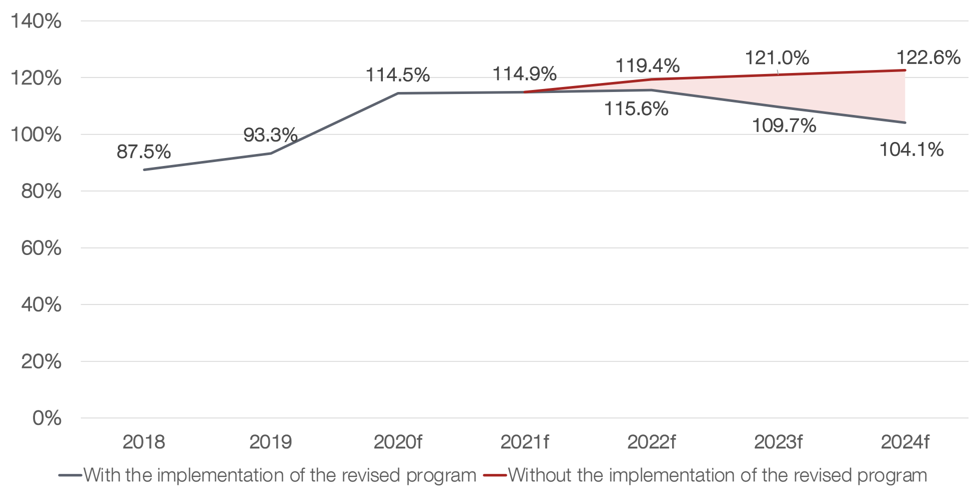


Significant progress was made to reduce budget deficits, with the deficit to GDP percentage reaching 6.3% and 4.7% in 2018 and 2019, respectively. However, the decrease in oil prices at the start of 2020 and the COVID-19 pandemic caused the deficit to GDP ratio to reach 12.8% in 2020, thus requiring the FBP to be revised to ensure a positive trajectory towards fiscal balance by 2024.



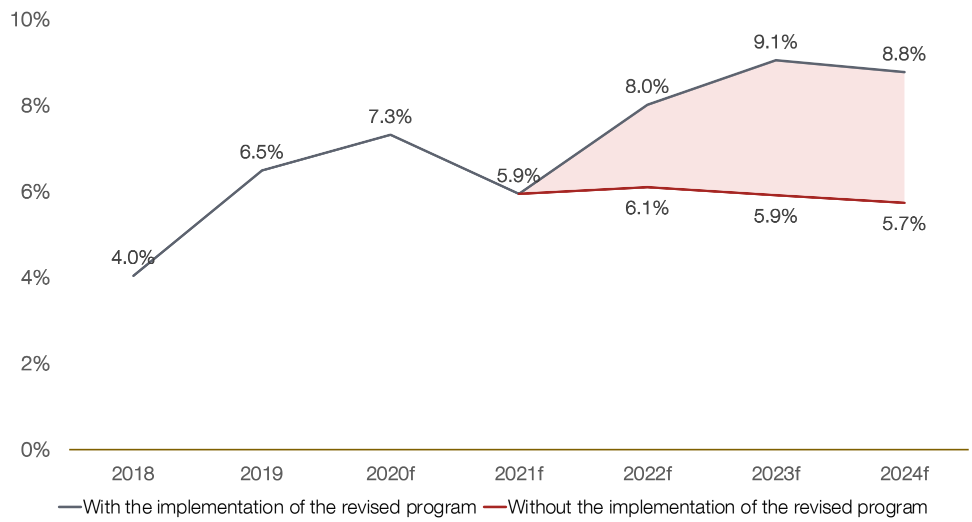
Debt as a percentage of GDP continued to grow, albeit at a slower pace, increasing from 87.5% in 2018 to 93.3% in 2019. The events of 2020 have led the debt to GDP ratio to increase to 114.5% in 2020 and the ratio is expected to increase further to 114.9% by year end of 2021. A key target of the Fiscal Balance Program is stabilizing the debt to GDP ratio before moving on a downward trajectory.

Debt as a Percentage of GDP

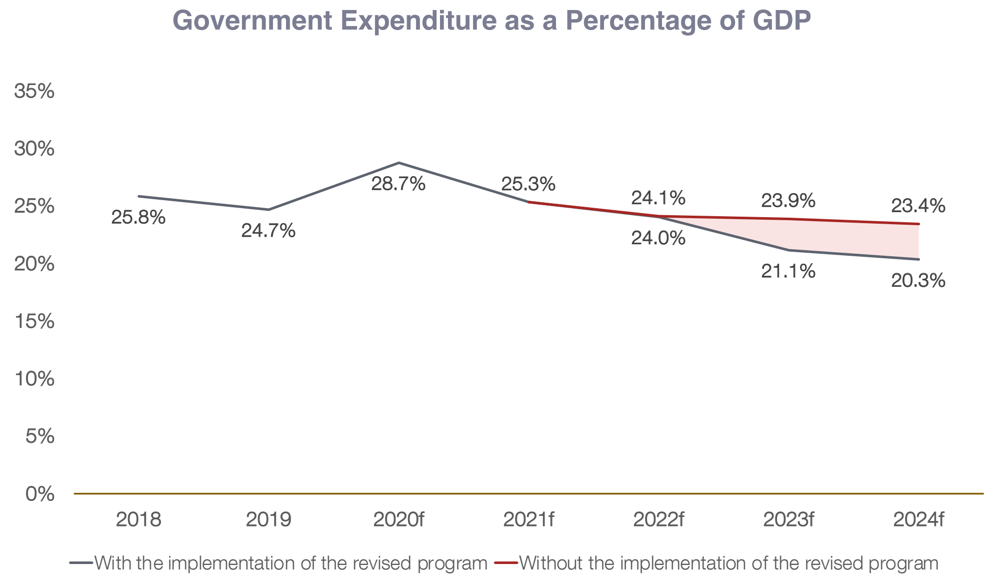


The launch of the Fiscal Balance Program has boosted the growth of the ratio of non-oil revenue to non-oil GDP. The implementation of the VAT from 1 January 2019 increased the non-oil revenue by 66% in 2019 compared to 2018, and the increase in the rate is expected to drive the revenue further up. The contribution of non-oil sectors to GDP has been steadily increasing. Despite a slight decrease expected in the year 2021, the ratio is expected to increase from 2022 onwards.

Non-oil Revenue as a Percentage of Non-oil GDP



Government spending decreased from its peak in 2015 of 30.4% of GDP, with further reductions achieved following the implementation of several initiatives between 2015 and 2017 and the launch of the Fiscal Balance Program in 2018. Government expenditure as a percentage of non-oil GDP has remained stable around 25%, albeit with a small increase in 2020 due to COVID-19 emergency spending, and is expected to reduce around 20% by the year 2024.



Increasing non-oil revenue was a key pillar of the Fiscal Balance Program when it was launched in 2018 and is also significant for the success of the revised Program. The contribution of non-oil revenues to recurrent government expenditure has been on an upward trajectory and the reliance on the oil sector is expected to continue to decrease.