COMMONWEALTH OF THE BAHAMAS

2021

MEDIUM-TERM DEBT MANAGEMENT STRATEGY FY2022/23 TO FY2024/25

PREPARED BY THE DEBT MANAGEMENT OFFICE
MINISTRY OF FINANCE

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LIST OF ABBREVIATIONS AND ACRONYMS

CREDITORS

CDB	Caribbean Development Bank
EEC	European Economic Community
IBRD	International Bank for Reconstruction and Development (World Bank)
IDB	Inter-American Development Bank
IMF	International Monetary Fund

CURRENCIES

BSD	Bahamian Dollar
CHF	Swiss Franc
CYN	Chinese Yuan Renminbi
EUR	Euro
GBP	British Pound Sterling
SDR	Special Drawing RIghts
USD	United States Dollar

OTHERS

ATM	Average Time To Maturity
ATR	Average Time To Re-fixing
ComSec	Commonwealth Secretariat
DOD	Disbursed and Outstanding Debt
GBE	Government Business Enterprise
GDP	Gross Domestic Product

DEFINITIONS

Average Time to Maturity (ATM)	A measure of the weighted average time to maturity of all principal repayments in the portfolio. A longer ATM implies lower financing risk, and vice versa.
Average Time to Refixing (ATR)	A measure of the weighted average time until all principal repayments in the debt portfolio become subject to a new interest rate.
Gross Domestic Product	The market value of all final goods and services produced within a country in a given period. The GDP is determined using data for production, expenditures, or income, and is presented in current or constant prices.
Refinancing Risk	The possibility that a borrower cannot refinance its debt by borrowing to repay existing debt.
Weighted Average Interest Rate (WAIR)	The weighted average interest rate on outstanding debts is determined by the value of the debt as a percentage of the total outstanding amount.
Yield Curve	A graph that plots the structure of interest rates, at a set point in time, of government securities with different maturities, ranging from the 3-months T-bills to the 30 year bonds. It enables investors to compare yields offered on short, medium and long-term government paper.

NOTES

Fiscal Year	The Bahamas' fiscal year runs from July 1 to June 30.
Reporting Currency	The domestic currency of The Bahamas is the Bahamian Dollar which is pegged to the USD at 1:1. Unless otherwise stated, all values are in Bahamian Dollar equivalents.
Coverage	The Medium-term Debt Management Strategy includes only central Government existing debt and projected borrowings.
Classification	For the purposes of the MTDS, debt is classified by currency and not residency.
Source	The source of all tables and figures is the Ministry of Finance. Statistics on GDP and prices are obtained from the Bahamas National Statistical Institute and the respective projections, from the International Monetary Fund (IMF). Projections for international reserves are also from the IMF.

FORWARD

Prudent management of debt is essential to the Government's ability to achieve fiscal sustainability and build resilience to withstand exogenous shocks, like severe weather-related events and health pandemics, contribute to stable long-term economic growth, and protect The Bahamas' creditworthiness among investors.

As part of the reporting requirements under the Public Debt Management Act, 2021 ("the PDMA"), the Government is mandated to publish a medium-term debt management strategy. This strategy outlines the Government's plans to achieve the optimal debt portfolio, based on a ranking of the cost and risk tradeoffs of alternative strategies. It operationalizes the Government debt management objectives—key among which is the sourcing of financing needs at the lowest possible cost over the medium-term, consistent with a prudent degree of risk.

The FY2022/23 – FY2024/25 Medium-term Debt Management Strategy ("the MTDS") is the first report on the Government's debt management strategy under the PDMA. It is being prepared against the backdrop of the recent Hurricane Dorian and the COVID-19 health pandemic which triggered a sharp rise in the fiscal deficit, the debt levels, and an unprecedented contraction in economic activity.

The Government recognizes the importance of sound fiscal policies and strong macroeconomic growth to placing the debt on a sustainable, downward trajectory. Consequently, the MTDS is anchored on the Government's medium-term fiscal framework, as set out in the 2021 Fiscal Strategy Report which frames the Government's economic policy reforms and fiscal consolidation measures over the medium-term. Through a combination of these macro-fiscal policies, the fiscal deficit is forecasted to converge to the target 0.5% of GDP by FY2024/25 which will facilitate a reduction in funding requirements and the level of debt accumulation.

The Government is committed to improving public debt management and The Bahamas' creditworthiness. The publication of the FY2022/23 – FY2024/25 MTDS, which has been approved by the Cabinet and is to be debated in Parliament, reinforces the Government's commitment to promote clarity, transparency and accountability in these operations.

I extend my sincere appreciation to the Financial Secretary and the Debt Management Office team for their efforts in the preparation of this inaugural debt management report, and for their commitment to the implementation and oversight of the selected debt management strategy.

Hon. Philip E. Davis
Prime Minister and Minister of Finance

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ACKNOWLEDGMENT

The FY2021/22 – FY202024/25 Medium-term Debt Strategy ("the MTDS") is the first formal exercise by the Government to devise a medium-term debt management strategy for The Bahamas. The MTDS will play a critical role in guiding debt management operations over the medium-term and, through the operationalization of the debt management objectives, assist the Government in achieving the goal of debt sustainability.

The MTDS has been prepared by the Debt Management Office ("the DMO") of the Ministry of Finance and outlines the Government's preferred strategy, which seeks to balance the cost and risk of both the existing public debt portfolio and alternative borrowing mixes.

The design and completion of this MTDS exercise would not have been possible without the invaluable contribution and collaboration of various stakeholders. I would like to recognize the efforts of the DMO team, and the Central Bank of The Bahamas Debt Management Unit, the Research Department, for their committed engagement to this exercise.

Finally, I extend special gratitude to the team at the Commonwealth Secretariat's Debt Management Unit, which provided technical assistance and capacity building support to The Bahamas team. This was critical in navigating the MTDS framework and Analytical Tool developed by the World Bank and the International Monetary Fund, which was used to analyze the various debt management strategies.

Having analyzed the cost risk tradeoffs of alternative strategies, the Ministry of Finance, via the DMO, is committed to implementing the debt management objectives, as outlined in the Public Debt Management Act, 2021 and the selected preferred strategy.

In keeping with the Government's commitment to transparency, the MTDS report is available on the Government's website at www.bahamas.gov.bs.

Simon Wilson
Financial Secretary

EXECUTIVE SUMMARY

The Public Debt Management Act, 2021 ("the PDMA), which was enacted in March 2021 and came into force on July 1, 2021, sets out the framework for effective debt management in The Bahamas. The PDMA requires the formulation and execution of a medium-term debt management strategy, having due consideration to the macroeconomic and financial market conditions, the availability of financing from various creditors, and vulnerabilities that could impact future borrowing requirements and debt service costs.

The Medium-Term Debt Management Strategy is a plan aimed at achieving the desired debt portfolio consistent with the debt management objectives. It guides the Government's borrowing decisions to fund its overall fiscal deficit, within the context of its cost and risk objectives.

The FY2022/23 – FY2024/25 Medium-term Debt Management Strategy ("the MTDS") has been prepared at a time when The Bahamian economy is recovering from the impact of two significant exogenous shocks in FY2019/20—Hurricane Dorian and the COVID-19 pandemic. The combination of border closures and severe containment measures to address the health-related concerns of the virus gave rise to a sharp contraction in economic growth, by an estimated 8.4% in FY2020/21, and a deterioration in the jobless rate to an IMF estimated peak of 25.6% in 2020. On the fiscal front, revenue losses and unplanned expenditures to fund the emerging social and economic needs resulted in a spike in the overall deficit to 13.6% of GDP from a year-earlier 7.1%. The medium-term outlook, which is significantly dependent on the recovery underway in tourism, envisages a rebound in real GDP to an estimated 3.2% in FY2022/23 and an average 3.1% over the three-year MTDS horizon.

Government debt grew at a relatively accelerated pace in recent years, moving from 58.0% of GDP in FY2017/18 to a high of 100.4% of GDP in FY2020/21. This development primarily reflected the impact of sustained fiscal deficits stemming from the sharp contraction in revenues and extraordinary spending to address the recent two external shocks.

In recent years, financing of the deficit has tilted more towards foreign currency borrowings, by way of sovereign bond issuances, syndicated loans, as well as increased access to multilateral debt. At end-September 2021, foreign currency debt constituted a larger 44.9% of the outstanding debt, up from 36.4% at end June-2018. Nevertheless, the portfolio's exposure to foreign exchange risk is minimal as the bulk of the debt is in Bahamian Dollars and most of the foreign currency risk is denominated in USD to which the Bahamian Dollar is pegged.

The FY2022/23 – FY2024/25 MTDS was formulated on an evaluation of the cost and risks of four (4) alternative debt strategies which were feasible under the prevailing domestic and international financial market conditions. These included increasing/reducing the proportion of external debt, increasing/reducing the tenor of the debt portfolio and the use of liability management operations. The selected strategy is one that would minimize the cost and risks of financing the fiscal deficits under both the baseline economic projections and shocks to the baseline. Certain benchmarks for the cost and market risk indicators, consistent with the Government's debt management objectives, were also established during the process, which pertained to: (i) foreign currency (FX) risk; (ii) interest rate risk; and (iii) refinancing risk.

The optimum debt strategy selected through this process seeks to extend average time to maturity, provide higher borrowing through fixed interest rate instruments, increase the share of domestic borrowings, and incorporate liability management operations while also balancing the cost. The financing mix under the selected FY2022/23 – FY2024/25 MTDS will include 41% of net borrowing from foreign sources and 59% of the financing from domestic sources. However, in terms of gross financing, foreign/domestic financing mix will be 28% and 72%, respectively.

1

Introduction

1.1 Background

The Public Debt Management Act, 2021 ("the PDMA") establishes the legal framework governing Government debt management activities in The Bahamas. Section 11 of the PDMA provides that the Debt Management Office, Ministry of Finance, should formulate a debt management strategy with medium-term focus that would guide the Government's borrowing policies and debt management operation and aim at achieving the debt management objectives. It further provides that the debt management strategy should be submitted to Cabinet for approval.

1.2 Objectives

The objectives of public debt management, as prescribed in Clause 4 of the PDMA, are to:

- ensure that financing needs and debt service obligations are met in a timely manner at the lowest possible cost over the medium to long-term, consistent with a prudent degree of risk;
- support the development of an efficient government securities market; and
- ensure that the public debt is managed consistent with the general principles of responsible fiscal management, the fiscal responsibility principles and the fiscal objectives in the Fiscal Responsibility Act, 2018 ("the FRA").

The FY2022/23 – FY2024/25 MTDS is the first to be prepared by the Debt Management Office, Ministry of Finance ("the DMO"), outlining the Governments' plan to meet its financing requirements at the lowest possible cost, while stabilizing the debt level over the year. The MTDS is in line with the Government's budget, and macroeconomic assumptions guiding the medium-term fiscal strategy in the 2021 Fiscal Strategy Report ("the FSR") and the Revised Budget for FY2021/22.

Minimizing the costs and risk of government debt activities is key to achieving debt sustainability and managing fiscal risks; and developing an efficient government bond market is critical to diversifying the source of budgetary financing over the medium-term.

Linking the debt sustainability objectives with the FRA's general principles of responsible financial management (i.e., accountability, intergenerational equity, responsibility, stability, transparency and inclusive growth) underscores the Government's commitment to good governance and fiscal discipline, as a means of achieving improved efficiency and effectiveness in public finance management and increased confidence of investors, creditors and other stakeholders in public sector decision making. It also brings a more strategic and long-term perspective to these activities. These good governance concepts are simultaneously reinforced by the Government's requirement to ensure that debt management practices are consistent with the overarching goals of achieving and maintaining a sustainable fiscal balance, prudent levels of public debt and prudently managing fiscal risks.

1.3 Scope of the MTDS

The scope of the MTDS comprises the central Government debt portfolio managed by the DMO, which covers the Government's foreign currency and Bahamian Dollar debt. For the purposes of the MTDS, and to capture the portfolio risks more accurately, debt is classified by currency as opposed to residency. That is, throughout the document, external debt captures all foreign currency denominated debt while domestic debt captures Bahamian dollar denominated debt. The MTDS has been developed based on the outstanding debt portfolio of the Government as at September 30, 2021, and the planned issuance of securities and other financing instruments during the balance of FY2021/22.

In keeping with the statutory requirements, the time horizon for this MTDS is three years, beginning with the upcoming budget year (FY2022/23) and the subsequent two fiscal years (FY2023/24 and FY2024/25).

1.4

Legal and Institutional Framework for the MTDS

a. Legal Framework

Public debt management operations in The Bahamas are governed by the PDMA and the Fiscal Responsibility Act, 2018 ("the FRA") which, together, reinforce the Government's commitment to fiscal and debt sustainability, and to accountability and transparency in fiscal operations.

Clause 11 of the PDMA mandates that the DMO develop and publish a medium-term debt management strategy that sets out the roadmap to achieve the objectives of public debt management for the upcoming budget year and at least two subsequent financial years. The MTDS is intended to guide the Government's borrowing policies and debt management operations and should be based on a detailed assessment of the costs and risks of alternative borrowing strategies and consider the Government's fiscal policy, the annual budget, the fiscal strategy report, the macroeconomic environment, market conditions and other relevant factors.

The FRA, which provides the overarching legislation under which the Government seeks to achieve fiscal consolidation, established the numerical long-term ceiling on Government debt at 50% of GDP—a level deemed consistent with this objective. As specified in the 2021 Fiscal Strategy Report (FSR), pursuit of the fiscal consolidation goal will ensure gradual convergence towards this debt anchor, by the revised target date of FY2030/2031.

In keeping with international best practice, the Government intends to review the FY2022/23 – FY2024/25 MTDS on an annual basis, with projections carried forward on a rolling basis for the subsequent three years.

b. Institutional Arrangements

Public debt management operations in The Bahamas come under the charge of the DMO in the Ministry of Finance and include responsibilities covering front office (resource mobilization/negotiations and investor relations), middle office (preparation of the MTDS reports, risk management and debt analysis), and back office (recording and reporting of debt statistics) activities.

In an exception to the front office activities, the issuance of domestic government securities and related activities (e.g., preparing the prospectuses for the issue of government securities and the announcements and the results of issuances as well as acting as paying agent for debt servicing obligations) will continue to be undertaken by the Central Bank of The Bahamas ("the Central Bank"), as the Government's fiscal agent, in collaboration with the DMO. The fiscal agency activities also include the transitory assistance currently provided by the Central Bank with maintaining Government's debt statistics in the Commonwealth Meridian debt recording and management system.

The Ministry of Finance continues to enhance the existing institutional arrangements for debt management. These include building the DMO team to the optimal size required by the organizational structure, providing exposure to capacity building initiatives in debt management and increasing the use of analytical tools.

c. Background to the Medium-Term Debt Strategy

i. Macro-Economic Conditions

During FY2019/20, The Bahamas was confronted with an unprecedented scale of economic, social, and health challenges emanating from the twin exogenous shocks—Hurricane Dorian in September 2019 and the COVID-19 pandemic which was first detected in The Bahamas in March 2020. Nationwide lockdowns and the imposition of other containment measures to curtail the spread of the COVID-19 virus triggered an abrupt halt in tourism, the major foreign exchange earner and employer, alongside a disruption in general business activity.

On a calendar year basis, real GDP contracted sharply by an estimated 14.5% in 2020, compared with a small gain of 0.7% in 2019. The unemployment rate also deteriorated, to an IMF estimated 25.6%, as a significant proportion of the workforce was either furloughed, laid-off or had their work week reduced because of the widespread closure of businesses.

Inflationary pressures were relatively mild, benefitting from the decline in global oil prices. For 2020, the rise in average consumer prices was almost flat at 0.04%, compared with 2.49% in 2019.

Financial sector developments featured a strong build up in domestic bank liquidity, which is a key source of funding for the Government's debt issuances. This development partly reflected weakness in domestic credit, amid increased stress in private sector credit quality indicators stemming from the adverse impact of COVID-19 on employment conditions. Liquidity growth also benefitted from the Government's recent foreign currency borrowings, which contributed to a boost in external reserves of $624.1 million to $2,382.2 million at end-December 2020—the equivalent of approximately 43.7 weeks of import cover.

In the external sector, the estimated deficit on the current account deficit widened sharply, to $2,330.1 million in 2020 from $359.2 million in 2019. This was primarily explained by the reversal in the services account balance, to a deficit of $132.5 million from a year-earlier $2,637.0 million surplus, amid the COVID-19 induced collapse in tourism activity.

Because of the adverse impact of the COVID-19 health crisis and Hurricane Dorian on economic growth, the fiscal deficit and debt levels, The Bahamas' sovereign credit ratings were downgraded on several occasions over the past 18 months. In the latest rating actions, Moody's Investors Services downgraded The Bahamas' long-term issuer and senior unsecured ratings, by one notch, to Ba3, on September 17, 2021, and maintained the negative outlook. On November 12, 2021, S&P Global Ratings also lowered The Bahamas' credit rating to B+. However, the outlook was upgraded to stable, given the positive pace of the economic recovery following the relaxation of the COVID-19 restrictions made possible partly by the global and domestic vaccination programmes.

ii. Fiscal Developments

Fiscal operations came under intense pressure during FY2020/21, as the Government experienced a marked decline in revenue receipts during the peak of the COVID-19 crisis and elevated spending to fund the extraordinary health, social and economic support initiatives.

Notwithstanding the sharp contraction in revenue intake during the first half of the fiscal year, fiscal performance in the second half benefitted from the strengthening rebound in tourism and general business activity, amid the increase in the global COVID-19 vaccination uptake and the progressive loosening of the containment measures.

Estimated revenue receipts, at $1,872.7 million (18.9% of GDP) for FY2020/21, surpassed the budget target by $110.1 million or 6.3%—although positioning $226.3 million (10.8%) below the FY2019/20 yield. Recurrent expenditures of $2,851.3 million (28.8% of GDP) exceeded the budget by $277.0 million, as

Government spent an estimated $268.5 million or 2.7% of FY2020/21 GDP to meet the extraordinary COVID-19 assistance programmes. These new spending demands were partially facilitated through cuts in non-priority current outlays, together with a reduction in capital spending of $146 million (28.3%) from the budgeted level to an estimated $369.5 million for FY2020/21.

Consequent on these developments, the Government's overall fiscal operations recorded a deficit of $1,348.1 million in FY2020/21, for an elevated 13.6% of GDP. Although only $20.9 million above the target deficit for FY2020/21, the outcome was a sharp deterioration from the estimated $799.0 million deficit for FY2019/20, which represented 7.1% of GDP.

The overall budget deficit was financed from both foreign (63.8%) and Bahamian Dollar (36.2%) sources.

1.5 Key developments in the Domestic Bond Market

Traditionally, the domestic bond market is the main source of financing for the fiscal deficit, although it is not developed nor deep enough to fully support Government budgetary requirements in all market conditions. During FY2020/21, and into the current fiscal year, the pre-existing vulnerabilities of the domestic market were exposed, as macroeconomic conditions became more challenging and the Government's borrowing needs were enlarged. Given the rather narrow investor base and limited absorptive capacity of the domestic market, the Government was constrained to increase reliance on external funding to meet the gap, reduce concentration risks in the domestic market and to support external stability, given the adverse impact of COVID-19 on tourism inflows.

The development of the bond market remains a strategic objective of the Government, from the perspective of broadening investor participation, limiting foreign exchange risk in the debt portfolio and establishing a yield curve that serves as a reference for access to financing for private and other public sector initiatives.

Several recent developments sought to advance this objective.

July 2018	The Government commenced reopening of existing bonds to help establish them as true benchmarks.
August 2019	The Government migrated its portfolio of bonds to the Bahamas International Securities Exchange (BISX).
July 2020	Trading commenced on Government paper listed on BISX—positioning the Government to obtain more efficient market-determined pricing of its securities.
July 2020	Prior to the finalization of the Public Debt Management legislation, the Government passed the Bahamas Registered Stock (Amendment) Act, 2020 which allowed for the elimination of physical securities; and the Central Bank, in its role as fiscal agent for the Government's securities, increased its reliance on electronic communications and settlements. This included a shift to an all-digital process for Bahamas Registered Stock ("BGS") offerings and settlements.
July 2020	The Central Bank launched the Bahamas Government Securities Depository ("the BGSD").
July 2020	The BISX trading platform and dematerialized holdings were integrated with the BGSD for more efficient record keeping around securities ownership, and transfers of ownership. The Central Bank engaged with commercial banking partners to enhance access to online and mobile banking for wire transfers, particularly for increase in daily transactional limits to settle government security purchases. Further enhancements are underway to these processes—to include an online BRS initial public offer portal for the public.

The Government will continue to foster the development of the domestic market with increased focus on liquidity, transparency, secondary market trading, settlement mechanisms and investor diversification. In this context, several important plans underway include the introduction of an online auction for the BISX broker dealers and commercial banks, and the concurrent carve out of a non-competitive bidding scheme for small, individual investors in government bonds—to bring greater cost and administrative efficiency to the issuance process.

2

Review of Existing Debt Portfolio

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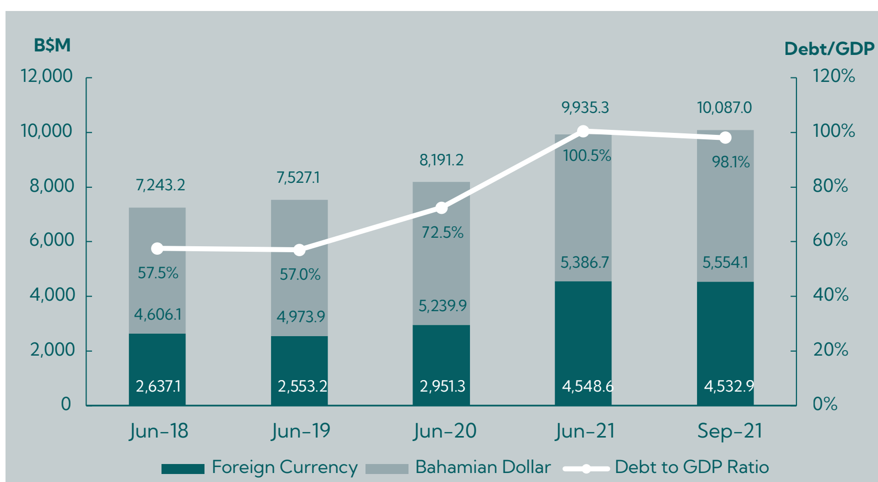
2.1

Composition of Outstanding Government Debt

The Government's debt comprises debt denominated in foreign currency and Bahamian Dollars. Figure 1 shows the trend in Government debt for the review period.

Figure 1: Government Debt Portfolio



At end-September 2021, the total Government debt is estimated at $10,087.0 million, equivalent to an estimated 98.1% of the annualized nominal gross domestic product (GDP). The portfolio comprised $4,532.9 million (44.9%) in foreign currency debt and $5,554.1 million (55.1%) in Bahamian Dollar debt.

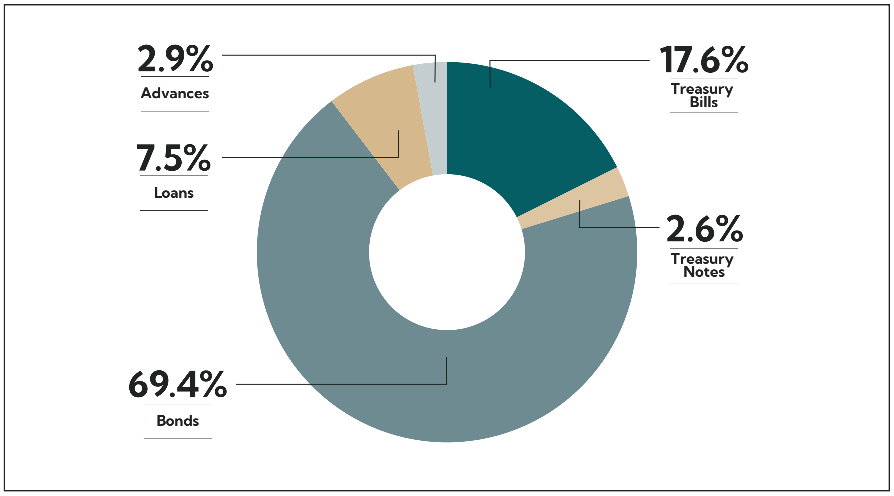
Reflecting the extraordinary spending demands and revenue losses associated with Hurricane Dorian and the COVID-19 health pandemic, Government debt rose sharply, by an average annual rate of 11.4% or an aggregate of $2,408.2 million over the three fiscal years to June 2021. Correspondingly, the estimated debt to GDP ratio firmed, from a relatively stable 57.5% in FY2017/18 to 72.5% in FY2019/20 and peaked at 100.5% in FY2020/21.

2.2 Bahamian Dollar Debt

Bahamian Dollar denominated debt grew steadily over the review years, from $4,606.1 million at end-June 2018 to $5,554.0 million at end-September 2021—for an aggregate gain of $947.9 million. This evolution, however, culminated in a 7.5% reduction in the Bahamian Dollar debt's share of total debt, to 55.1% at end-September 2021.

As shown in Figure 2, the breakdown of the $5,554.1 million stock of domestic debt by creditor at end-September 2021 comprised bonds (69.4%), Treasury bills (17.6%), Treasury notes (2.6%), commercial loans (7.5%) and advances from the Central Bank (2.9%).

Figure 2: Creditor Composition of Bahamian Dollar Debt, at end-September 2021



a. Government Securities

i. Bonds

Domestic market conditions have generally favoured Government bond issuances, supported by the ongoing buoyancy in banking sector liquidity and the persistent lack of stable alternative investment opportunities. Typically, the Government has issued bonds to refinance maturing bonds, and with net increases secured over the review years.

Holdings of domestic bonds are highly concentrated in the private sector grouping, which captures individuals, credit unions, trust and mutual funds, and businesses. This sector held 50.9% of the $3,852.8 million bond stock at end-September 2021, compared with the 40.0% accounted for at end-June 2018. With this outcome, there has been a consequential decline in the share held by commercial banks, from the peak 31.1% at end-June 2018 to 23.4% at end-September 2021, they remain the single largest holder of Government bonds. Public corporation's share of bonds also trended lower, to 14.7% from 17.1% at end-June 2018; and a similar abatement was observed for the Central Bank's share, of 9 basis points to 6.0% at end-September 2021. Meanwhile, the respective proportions for insurance companies and other financial institutions were relatively stable at 4.2% and 0.8%.

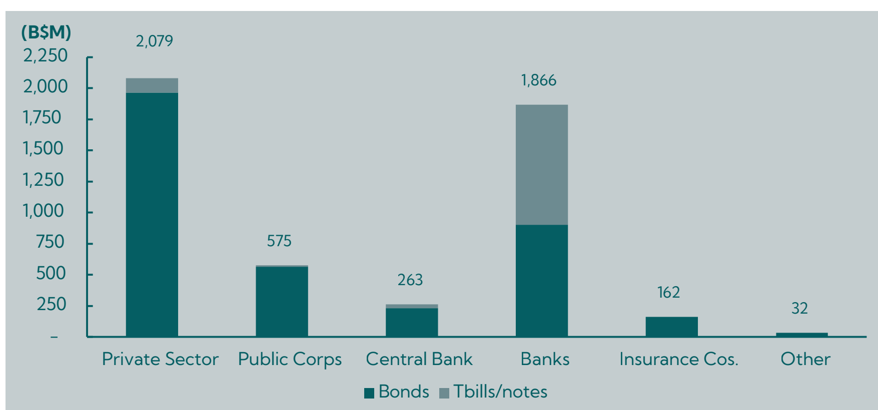
Based on the maturity structure, more than two-thirds (76.6%) of the bonds were in the over 15 years' bucket, contrasting with 11.4% in the over 5- to 10-year bucket. Of the remaining 12.0% of the bond portfolio, 5.7% was held in maturities of 1 year and less, and the over 1 to 5 year and the over 10 to 15 year maturity tranches held almost equivalent shares, of 3.2% and 3.1%, respectively.

ii. Treasury Bills and Notes

Treasury bills and notes feature a mix of 30-, 91- and 182-day tenors, with an average life of approximately 3.6 months. Of the aggregated $1,124 million outstanding at end-September 2021, the bulk was issued at 91-day maturities (77.9%), followed by the 182-day (21.9%) and the 30-day tenors (0.2%).

Commercial banks have been consistently the largest holder of these securities, with a share of 85.9% at end-September 2021, as Government securities also qualify as regulatory liquid assets. The next largest share was accounted for by the "Other" category (10.4%)—primarily the broker/dealers, followed by much smaller proportions for the Central Bank (2.8%) and the public corporations (0.9%).

Figure 3: Total Government Securities, end-September 2021



In recent years, the Government sought to reduce the refinancing/rollover risk in the portfolio posed by the short-term Treasuries, by converting portions to longer dated bonds.

2.3 Foreign Debt

At end-September 2021, the creditors of foreign currency debt comprised private capital markets (54.6%), multilateral sources (24.9%), financial institutions (19.1%) and bilateral agencies (1.4%).

a. Private Capital Markets

As shown in Table 1, international bond issuances, which held steady at $1,650.0 million through end-September 2020, increased to $2,475.0 million in FY2020/21—all of which were issued at fixed rates of interest. In October 2020, the Government completed an offering in of $600 million of 8.95% notes due 2023, which was reopened in December 2020 and an additional $225.0 million was issued.

Table 1: Government International Bond Issuances

Issue	Coupon	Issue Date(s)	Maturity Date(s)
USD$200 million	6.625%	May-2003	May-2033
USD$100 million	7.125%	Apr-2028	Apr-2038
USD$300 million	6.950%	Nov-2009	Nov-2029
USD$300 million	5.750%	Jan-2014	Jan-2024
USD$750 million	6.00%	Nov-2017	Nov-2026|Nov-2027|Nov-2028
USD$825 million	8.95%	Oct-2020|Dec-2020	Oct-2030|Oct-2031|Oct-2032

Future redemptions for the external bonds are partially managed via discretionary sinking funds established by the Government. At end-September 2021, the accumulated value of the sinking funds for the US$100 million, the US$200 million and the US$750 million bond issues stood at $192.4 million.

b. Multilateral Debt

The share of multilateral debt obligations, which are contracted at concessional terms (comparatively lower cost and longer tenor than commercial debt) recorded a sharp increase, from 8.0% of the foreign currency debt stock at end-June 2018 to 24.9% at end-September 2021. Growth was paced by a more than threefold rise in indebtedness to the largest holder, the IDB, which moved from $189.1 million at end-June 2018 to $650.8 million at end-September 2021—based on several new policy-based loans. However, the IDB's share was sharply reduced to 57.6% of the total multilateral debt, reflecting the Government's sourcing of a 182 million SDR facility (USD250.9 million) from the IMF under the Rapid Financing Instrument and an exceptional $100 million development policy loan from the World Bank (The Bahamas formally graduated from the World Bank in 1989.)—both of which assisted with meeting the extraordinary economic and social demands arising from the COVID-19 pandemic. Borrowings from the CDB were also higher—at $121.3 million at end-September 2021 from a low of $22.4 million in FY2018—as the Government sought to support the recovery from the widespread destruction caused by Hurricane Dorian.

c. Bilateral Debt

The single holder of bilateral debt is the Export-Import Bank of China, with an outstanding balance of $65.2 million on the three credit facilities at end- September 2021.

d. Financial Institutions

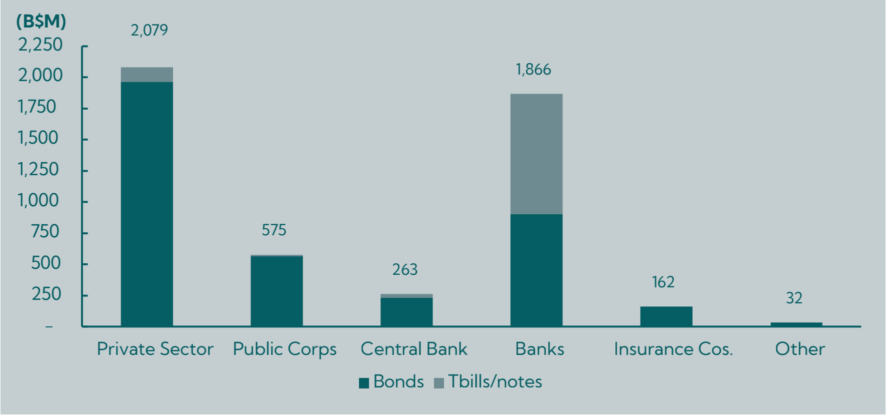
Debt owing to financial institutions in foreign currency totaled $863.3 million at end-September 2021, representing an increase of $174.0 million over end-June 2018. This reflected the net impact of scheduled loan runoffs and the new $246 million bridge facility obtained in July 2020, to assume an equivalent liability previously held by the Bahamas Electricity Corporation. Through end-September 2021, this loan, which was recently extended to January 2022, was being serviced by the Bahamas Power and Light Company ("the Company") under a separate agreement with the Government, pending the Company's decision regarding long-term funding arrangements.

2.4 Debt Service Payment

As depicted in Figure 4, total debt service fluctuated during the past four years, declining from $1,616.3 million in FY2017/18 to $1,130.0 million in FY2018/19, before firming and peaking at $1,785.0 million for FY2020/21.

On the external side, the rise in interest cost to $205.5 million for FY2020/21 reflected the impact of the increased debt stock and less favourable borrowing conditions in the international bond market. Scheduled principal payments were also spiked by the incidence of several refinancing operations relative to interim financing obtained during the fiscal year.

Figure 4: Government Debt Service



Domestic debt service trends reflected the combination of firming interest rates on Government securities and increased issuances. Similarly, the steady accretions in the principal component were associated with the higher volume of refinancing activities in the context of an elevated debt stock.

2.5

Cost and Risk Analysis of the Debt Portfolio

The Government's debt portfolio has inherent risks related to market volatility, given changes in interest and foreign exchange rates, and there is also the risk associated with debt refinancing. The basic cost and risk indicators for the portfolio, at end-September 2021, are presented in Table 2.

a. Cost Indicators

The cost of the existing debt portfolio, based on the implied weighted average interest rate (WAIR), was 4.8% at end-September 2021. The higher WAIR on the foreign currency debt of 5.3% was driven by the dominance of the fixed rate USD bonds in the portfolio, which carried a weighted average interest rate of 7.2%. This outcome, however, was softened by the favourable impact of concessionary multilateral and bilateral credits in the portfolio relative to commercial borrowings, which tilted the WAIR on the loan segment lower to 3.1%.

On the domestic side, Government bonds carried a WAIR of 4.7% at end-September 2021, with approximately 53.0% of the outstanding portfolio being issued at fixed rates of interest and having a WAIR of 4.9%, compared with the 4.5% WAIR for the variable rate bonds. Treasury bills and notes bore a combined WAIR of 2.7%, while commercial loans in Bahamian Dollars had a combined WAIR of approximately 4.8%—comprising 4.6% for the fixed rate debt and a slightly higher 4.9% for variable rate debt. Advances, which are linked to the 90-day Treasury bill rate, bore a WAIR of 2.7%.

Total interest payment on the debt portfolio of $422.4 million for FY2020/21 represented an estimated 22.6% of Government revenue and 4.3% of GDP.

The present value of the debt at end-September 2021 was significantly lower, at $9.775 billion (95.0% of GDP), due to the growing importance of concessional and semi-concessional debt in the existing debt portfolio.

Table 2: Cost and Risk Indicators of Existing Debt, at end-September 2021

Risk Indicators		Foreign Debt	Bahamian Dollar Debt	Total Debt
Nominal Debt (in millions of BSD)		4,532.9	5,554.1	10,087.0
Nominal Debt as % of GDP		44.1	54.0	98.1
Present Value Debt as % of GDP		41.5	53.6	95.0
Cost of Debt	Interest as % of Government Revenue	9.3	10.9	20.2
	Interest as % of GDP	1.9	2.3	4.2
	Weighted Avg. Interest Rate (WAIR)	5.3	4.2	4.8
Refinancing Risk	ATM (years)	7.0	7.5	7.3
	Debt maturing in 1 yr. (% of Total)	7.7	34.3	22.3
	Debt Maturing in 1 yr. (% of GDP)	3.4	18.5	21.9
Interest Rate Risk	ATR (years)	5.0	5.1	5.0
	Debt refixing in 1 yr. (% of Total)	40.8	68.7	56.1
Foreign exchange risk	Fixed rate debt (% of total)	60.7	62.2	61.5
	Non-USD F/C Debt (% of total debt)	12.6	-	5.4

b. Risk Indicators

i. Refinancing/Rollover Risk

Rollover/refinancing risk shows the vulnerability of the portfolio to higher refinancing costs for maturing debt obligations within a specified period or, in extreme cases, the inability to rollover the debt. Refinancing risk is a key risk in Government's existing debt portfolio, with the average time to maturity (ATM) placed at 7.3 years at end-September 2021.

Given the short-term nature of the Treasury bills and notes, refinancing risk was skewed towards the domestic portfolio, which had an ATM of 7.5 years and 34.3% of the portfolio maturing within 1 year.

Refinancing risk of the foreign debt revealed an ATM of 7.0 years at end-September 2021, reflecting the characteristics of a portfolio more concentrated in instruments with commercial relative to concessionary terms. Only 7.7% of the foreign debt portfolio is maturing within 1 year, providing the Government with time to develop and execute refinancing initiatives.

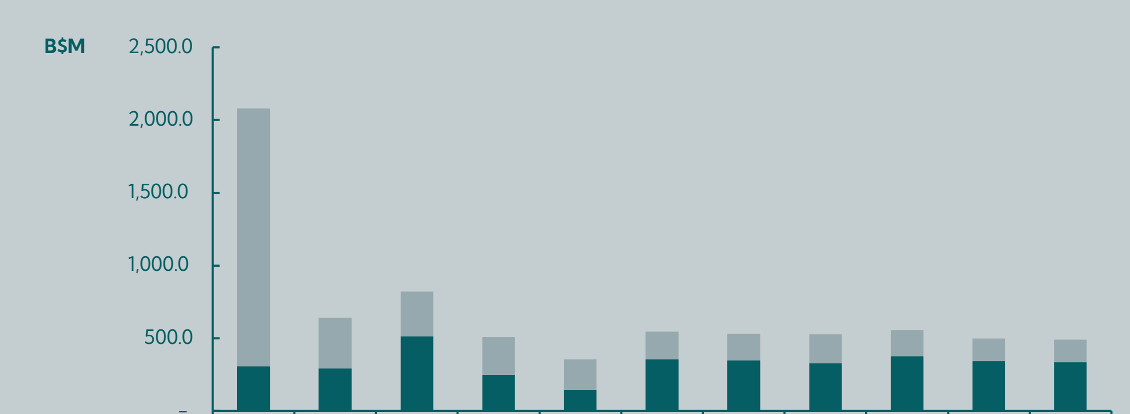
ii. Redemption Profile

Figure 5 depicts the amortization of the outstanding debt and the risk inherent in the structure of the debt. Aside from the short-term domestic Treasuries, the redemption profile of the Government's debt portfolio was reasonably paced.

The distribution of the forecasted redemptions between 2023 and 2032 is indicative of the dominance of the domestic bonds in the debt portfolio. Bonds are primarily held by commercial banks, the public corporations and institutional investors, who tend to refinance issues, amid the lack of a steady stream of alternative investment instruments in the domestic space.

The redemption profile for foreign currency debt is relatively lengthy and smooth, reflecting the longer maturity and amortizing structure of the multilateral and bilateral credits. The projected spikes are linked to the foreign bond redemptions, which dominate the existing debt portfolio.

Figure 5: Redemption Profile of Government Debt, as at end-September 2021



	2022	2023	2024	2025	2026	2027	2028	2029	2030	2031	2032
Bahamian Dollar	1,769.3	348.1	309.0	259.4	208.1	191.2	180.9	199.4	179.2	155.2	155.0
Foreign Currency	309.5	293.4	514.4	249.1	148.2	356.1	349.3	330.5	378.0	344.0	337.2

iii. Interest Rate Risk

Interest rate risk relates to the changes in debt service cost arising from variability in market interest rates. The Average Time to Re-fixing (ATR) is a measure of the weighted average time until all the principal payments in the debt portfolio are subject to a new interest rate.

The Bahamas' debt portfolio has an overall ATR of 5.0 years, with 56.1% of the total debt subject to a change in interest rate in one year.

Interest rate risk is mainly inherent in the domestic debt portfolio. Although the ATR is only slightly higher at 5.1 years, a significant 68.7% of the debt is subject to refixing in one year due to the prevalence of the short-term Treasury bills and notes. The ATR for the external debt was also not significantly different, at 5.0 years, but with a lower 40.8% of the debt refixing in one year. Further, the proportions of fixed rate debt for both foreign currency and Bahamian Dollar debt were 60.7% and 62.2%, respectively.

iv. Exchange Rate Risk

Foreign exchange risk is the risk that The Bahamas' debt position will deteriorate due to changes in the value of the Bahamian Dollar relative to other currencies. As illustrated in Table 3, The Bahamas remains minimally exposed to foreign exchange risk. At end-September 2021, approximately 55.1% of the debt portfolio was contracted in Bahamian Dollars.

Consistent with the increased borrowings from the multilaterals and the international bond issuances, the share of debt denominated in United States Dollars, to which the Bahamian dollar, is pegged, grew to 39.5% at end-September 2021 from 28.8% at end-June 2018 and a low of 27.5% at end-June 2020. Debt denominated in SDRs, for which the USD is also the dominant currency, accounted for 2.5% of the total debt, with lower shares for the CHF (1.7%), CNY (0.6%), and EUR (0.6%). To help mitigate residual currency risk in the portfolio posed by CHF and CYN denominated debt, the Government has in place several foreign currency swap arrangements.

Table 3: Currency Distribution of Government Debt at end-September 2021

Currency	B$M	% Share
Bahamian Dollars	5,554.1	55.1
US Dollars	3,983.3	39.5
IMF SDRs	257.0	2.5
Swiss Francs	168.9	1.7
Chinese Yuan	65.2	0.6
Euros	58.5	0.6
Total	10,087.0	100.0

Review of Existing Debt Portfolio

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3.1 Macroeconomic Assumptions

The FY2022/23 – FY2024/25 MTDS is anchored on the financial and medium-term macroeconomic forecasts in the 2021 FSR and Revised Budget for FY2021/22, which articulate the Government's policy framework for achieving the goal of fiscal consolidation and debt sustainability (see Table 4). Through a combination of economic and fiscal reform policies, the Government intends to move progressively towards achieving the fiscal and debt to GDP targets, of 0.5% and 50%, respectively.

Over the medium-term, the macroeconomic environment appears positive for The Bahamas, following the reopening of the economy in November 2020, after an extended lockdown period to stem the spread of COVID-19.

Table 4: Baseline Macroeconomic Assumptions

		Actuals			Budget	Forecasts		
	Unit	2018/19	2019/20	2020/21P	2021/22	2022/23	2023/24	2024/25
Total Revenue	**B$ M**	2,426.4	2,099.2	1,872.7	2,338.8	2,700.3	3,057.8	3,428.3
Total Expenditure	**B$ M**	2,641.4	2,898.2	3,220.8	3,197.4	3,115.5	3,255.1	3,356.4
Recurrent Expenditure	**B$ M**	2,418.0	2,526.0	2,851.3	2,879.2	2,679.3	2,790.1	2,866.9
of which: Interest Pmts	**B$M**	329.7	344.7	422.4	482.5	505.8	565.8	578.0
Capital Expenditure	**B$M**	223.4	372.2	369.5	318.2	436.2	465.0	489.5
Overall Fiscal Balance	**B$M**	(215.0)	(799.0)	(1,348.1)	(858.6)	(415.2)	(197.3)	71.9
Primary Fiscal Balance	**B$M**	114.7	(454.3)	(925.7)	(376.1)	90.6	368.5	649.9
GDP (Real)	**B$M**	11,267.1	10,486.0	9,606.7	10,682.0	11,020.8	11,418.3	11,702.9
GDP (Nominal)	**B$M**	13,205.0	11,301.0	9,895.0	11,573.0	12,462.0	13,268.0	13,985.0
GDP (Nominal) Growth	**%**	5.7	(14.4)	(12.4)	17.0	7.7	6.5	5.4
GDP (Real) Growth	**%**	1.7	(6.9)	(8.4)	11.2	3.2	3.6	2.5
Total Revenue	**% of GDP (Nominal)**	18.4	18.6	18.9	20.2	21.7	23.0	24.5
Total Expenditure	**% of GDP (Nominal)**	20.0	25.6	32.5	27.6	25.0	24.5	24.0
Recurrent Expenditure	**% of GDP (Nominal)**	18.3	22.4	28.8	24.9	21.5	21.0	20.5
Capital Expenditure	**% of GDP (Nominal)**	1.7	3.3	3.7	2.7	3.5	3.5	3.5
Overall Balance	**% of GDP (Nominal)**	(1.6)	(7.1)	(13.6)	(7.4)	(3.3)	(1.5)	0.5
Primary Balance	**% of GDP (Nominal)**	0.9	(4.0)	(9.4)	(3.2)	0.7	2.8	4.6

Note: FY GDP data derived from quarterly GDP series compiled by the Bahamas Statistical Institute; forecasts based on IMF annual GDP data.

Generally, the medium-term macroeconomic outlook points to a continued strengthening of the economic recovery underway since the second half of 2020. This is grounded in expectations for a continuation of the stronger than earlier anticipated rebound of the dominant tourism activity to pre-pandemic levels, and supported by prospective positive yields from the Government's economic policy initiatives aimed at increasing foreign direct investment (FDI) and improving the competitiveness of the economy, through more business friendly conditions. Growth in real GDP growth is forecasted to improve to around 6.9% in FY2021/22 from the steep 8.4% fall-off in FY2020/21, and moderate to 5.8% in FY2022/23 before leveling-off to 2.6% in FY2024/25.

With the steady recovery in tourism, the services account on the balance of payment is forecast to return to a surplus position and the capital account is expected to benefit from healthy levels of FDI. Together, these developments are projected to deliver positive outcomes for the overall balance of payments, as measured by the change in the international reserves position, and therefore support stability in the exchange rate.

Price conditions are expected to tighten somewhat in FY2022/23 and FY2023/25, under the impact of the persistence of the ongoing supply chain disruptions—although with consumer price inflation remaining in the lower single digits. Based on the latest projections produced by the IMF in the October 2021 World Economic Outlook, the expectation is for The Bahamas' average consumer price gains to firm to around 2.5% in 2022 and 2023, before stabilizing at 2.0% in 2024 and 2025.

Fiscal policy remains an important facet of the Government's strategy for maintaining stability in macroeconomic conditions through its growth positive initiatives and steady progress towards the achievement of the fiscal consolidation and debt targets.

As set out in the 2021 FSR, the Government is targeting an overall fiscal deficit of $415.2 million or 3.3% of GDP for FY2022/23, improving to $263.7 million in FY2023/24 and achieving near balance in FY2024/25, with the overall deficit narrowing to $67.9 million or 0.5% of GDP—which is the fiscal target established in the FRA. Regarding revenue projections, the Government has articulated its intent to introduce enhanced revenue administrative measures, aimed at increasing the tax base by minimizing leakages and to pursue tax policy reforms to strengthen revenue collections over the medium-term. Through effective implementation of these initiatives, total revenue is expected to progressively improve, from a projected 20.2% of GDP in FY2021/22 to 24.5% of GDP in FY2024/25.

On the spending side, recurrent outlays are forecasted to decline by 4.9% in FY2022/23 to approximate 22.0% of GDP and hold steady at this level through the remaining two years to FY2024/25, as spending levels normalize after the exceptional pressures imposed by COVID-19 and Hurricane Dorian. Similarly, the policy for capital expenditure is to maintain these outlays at 3.0% of GDP throughout the medium-term, as the Government also intends to leverage public private partnerships to achieve its infrastructure goals.

3.2 Risks Associated with the Macroeconomic Indicators

The FY2022/23 - FY2024/25 Government debt management strategy is based on the above mentioned macroeconomic assumptions. However, occurrences of exogenous shocks emanating from the external economic environment and events, like natural disasters (that are not factored into these assumptions) could cause deviations from the targets aimed to be achieved by the strategy. Weaker than anticipated global recovery, a resurgence and persistence of the COVID-19 pandemic and the occurrence of a natural disaster, which would all have adverse spillover effects for the fiscal outcome.

To illustrate, a slowdown in global economic growth could adversely impact both the economic growth projections and anticipated yields from revenue mobilization initiatives, with consequential adverse implications for the fiscal deficit, as well as projections of borrowing requirements, debt levels and debt servicing costs.

Likewise, any setback to tourism performance, from unanticipated adverse developments with the COVID-19 pandemic a severe weather event, like a hurricane, could exert pressure on external inflows and, therefore, the external reserves position. The resultant outcome could cause a shift in the Government's funding strategy more towards foreign currency borrowings to support the external position, amid the concomitant threats to growth projections. Further, any downsides in global commodity prices would present marked risks to the growth and external account forecasts.

On the domestic side, the lack of fiscal and economic policy reforms, aimed at improving the revenue yield, containing expenditures and boosting economic growth, could stall the attainment of the fiscal targets, with adverse implications for creditworthiness, access to credit markets, debt levels and debt servicing costs.

3.3 Indicative Benchmark and Target

For the efficient management of the Government debt, it is important to identify risks inherent in the debt portfolio and to establish corresponding quantitative targets for the risk indicators. These targets help to communicate the debt management objectives more clearly, in terms of cost and risk factors, and facilitate a more sustainable and predictable debt strategy, independent of political or other exogenous impacts inherent to the debt portfolio. Quantitative targets also allow for clear comparisons with the actual outcomes of the underlying indicators. However, because of unanticipated exogenous shocks and changes in market conditions create uncertainty and risks, which often give rise to the potential need for quick responses by the debt management, these indicators are normally defined in ranges. The key debt portfolio risks for The Bahamas are foreign exchange, interest rate and refinancing risks and the objective of the debt management strategy is managing these risks within prudent levels.

The indicative benchmark and target for key risk indicators are summarized below.

a. Foreign Currency Risk Benchmark

The currency and interest rate composition of debt, as well as its maturity structure, are important determinants of debt vulnerability. Therefore, external (FX) debt will be maintained at 30 percent (+/-5%) of total debt. Foreign currency borrowings are targeted at financing Government's capital expenditures, refinancing the global bond issuances, and achieving policy action reforms designed to promote private sector-led growth, secure improvements in the policy, legal, and institutional framework for state-owned entities, public-private partnerships, fiscal management, and the business and investment climate and build resilience to climate change, including emergency and disaster response.

b. Interest Rate Risk Benchmark

The debt strategy will place emphasis on stabilizing debt service costs by increasing the share of fixed rate debt in total debt portfolio to keep average time for refixing greater than or equal to 5 years.

c. Re-Financing Risk Benchmark

The debt strategy would seek to ensure a stable and affordable maturity structure to reduce refinancing risk exposure by maintaining an ATM of greater than or equal to 6.5 years.

4

Modelling of the Medium-Term Debt Strategy

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In formulating the FY2022/23 – FY2024/25MTDS, cost and risks of several alternative debt strategies were assessed, both under the baseline economic projections and shocks to the baseline. These plausible strategies were developed by increasing/reducing the tenor of the domestic securities, increasing/reducing the proportion of foreign currency debt in the portfolio and factoring a liability management operation. An optimal strategy was then selected based on cost and risk outcomes as well as its impact on development of the domestic bond market.

Consistent with the medium-term fiscal strategy of the Government, the FY2022/23 – FY2024/25 MTDS was developed to fund the net deficit plus principal payments over the next three fiscal years. Various debt strategies were analyzed under the baseline macroeconomic and financing assumptions and with different shock scenarios, involving interest rate, exchange rates, and a combined interest rate and exchange rate shock.

4.1 Baseline-Pricing Assumptions and Description of Shock Scenarios

For the FY2022/23 – FY2024/25 MTDS, it is assumed that the bulk of the foreign currency denominated debt will be contracted in USD.

a. Pricing Assumptions

The baseline projections used for the terms and pricing of the foreign currency denominated debt (see Table 5) are as follows:

- The BSD is assumed to remain pegged to the USD at the current 1:1 ratio. The projected cross currency rates were drawn from the implicit exchange rate used in the IMF's October 2021 World Economic Outlook (WEO).
- Loans from multilateral sources are priced at an average fixed rate of 1.43% and floating rates (reference rate plus a margin) of up to 1.11%, with a 25-year tenor and 5-year grace period.
- Loans from bilateral sources are priced at an average fixed rate of 2.0%, with a 20-year tenor and 5-year grace period.

- Commercial loans are assumed to be contracted at both fixed interest rates at the prevailing market rates and floating debt at a reference rate plus a margin with a maturity of 8 years, including a grace period of up to 6 years.
- The pricing of International Capital Market bonds is based on the prevailing sovereign bond yield curve for June 2021, with an average tenor and grace period of 11 years.
- For floating rate external debt instruments, LIBOR forward rates were used, as published on the Bloomberg portal.

The terms and pricing assumptions for the BSD denominated financing under the baseline scenario are as follows:

- Commercial borrowings are contracted in BSD—for fixed interest rates, at the prevailing market rates and floating rates, at a reference rate plus a margin, with an up-to 8-year tenor and 2-year grace period.
- Domestic market securities financing comprises bonds, Treasury notes and Treasury bills. Treasury bills/notes are assumed to be issued up to 1-year maturities, while the other securities are expected to be issued with maturities and grace periods of up to 30 years. A portion of the Treasury bills are assumed to be converted to 10-year fixed rate bonds.
- For the Bahamian dollar (BSD) denominated domestic debt instruments, the yield curve was projected by fitting the Nelson Siegel Method on published yields of the Central Bank and deriving forward yields from the fitted curve.

Table 5: Baseline Pricing Assumptions

Financing Source	Interest Rate Type	Maturity (Yrs.)	Grace (Yrs.)	Currency Type	Average Interest Rate
Multilateral Loans	Fixed	25	5	FX	1.43
Multilateral Loans	Variable	25	5	FX	1.80
Bilateral Loans	Fixed	20	5	FX	2.00
USD Commercial Loans	Variable	8	6	FX	Reference + Margin
USD Commercial Loans	Fixed	8	6	FX	Prevailing Market Rates
USD Bonds	Fix	11	11	FX	Prevailing Market Rates
USD Bonds	Variable	11	11	FX	Reference + Margin
Other USD Loans	Variable	1	1	FX	Reference + Margin
Liability Management	Fixed	10	10	FX	Prevailing Market Rates
BSD Commercial Loans	Fixed	8	2	BSD	Reference + Margin
BSD Commercial Loans	Variable	8	2	BSD	Prevailing Market Rates
BSD Bonds	Fixed	17	17	BSD	Prevailing Market Rates
BSD Bonds	Variable	20	20	BSD	Reference + Margin
BSD 10 yr. Bonds (Incl. converted T-bills)	Fixed	10	10	BSD	Prevailing Market Rates
BSD 7 yr. Bonds	Fixed	7	6	BSD	Prevailing Market Rates
BSD 3 yr. Bonds	Fixed	3	2	BSD	Prevailing Market Rates
BSD T-Bills/Notes	T-bills	1	1	BSD	Prevailing Market Rates
Other BSD Short-Term Debt	Fixed	1	1	BSD	Prevailing Market Rates

b. Shocks

The shocks to the baseline projects are detailed below.

- **Foreign exchange rate shocks.** The extreme risk scenario for exchange rates modelled a 10% depreciation shock to the non-USD baseline exchange rate projections, applied in FY2022/23 and maintained through the period of analysis.
- **Interest rate shock.** The extreme risk scenario for interest rates assumes a stand-alone interest rate shock of 200 basis points over the baseline interest rate projections for floating rate instruments, each year in the projection period, allowing a parallel shift or change in the yield curve.
- **Combination shocks.** The combination shock models a moderate risk scenario for interest rates in conjunction with a moderate risk scenario for exchange rates. For the interest rate shock, a 100-basis point increase over the baseline projections was applied to floating rate instruments, each year in the projection period. The moderate exchange rate shock assumed a 7.5% depreciation applied to the non-USD in FY2022/23.

4.2 Description of Alternative Debt Management Strategies

Four (4) financing strategies are considered during the MTDS process to inform the financing of the fiscal deficit and guide medium-term borrowing over the three-year period FY2022/23 – FY2024/25.

Each strategy considers a distinctive financing mix, comprising debt instruments from both domestic and foreign sources. The foreign financing includes bonds and loans ranging from concessional to commercial terms, while the domestic financing considers loans, bonds, treasury notes, treasury bills and advances.

- **Strategy 1 (S1-Status quo):** The strategy follows the status quo and assumes that the Government would follow the pre-COVID-19 borrowing pattern. In net terms, the strategy assumes new financing of 5% of gross financing needs over the medium-term, of which, 20% represents net foreign, and 80% represents net domestic financing over the medium-term. In terms of gross borrowing, foreign and domestic financing accounts for 28% and 72%, respectively.

» **Strategy 2 (S2):** The objective of this strategy was to reduce refinancing risks by lengthening the ATM of the portfolio, while at the same time balancing cost. Some liability management operations were also modelled in this strategy. The strategy assumes new financing of 9% of gross financing needs over the medium-term, of which, 75% represents net foreign financing and 25% represents net domestic financing. The financing mix for the gross foreign and domestic financing was 32% and 68% respectively.

» **Strategy 3 (S3):** This strategy also seeks to address interest rate risk by borrowing at more fixed interest rates, while still aiming to extend average time to maturity and balancing cost and engaging in liability management activities. The proposed net borrowing is expected to be 13%, of which 59% represents net borrowing from foreign sources and 41% from domestic sources. In terms of gross financing, the strategy assumes a foreign/domestic financing mix of 28% and 72%, respectively.

» **Strategy 4 (S4):** The strategy seeks to gradually address FX risk by only issuing debt denominated in BSD and USD. The strategy assumes a net new financing of 10%, including a mix between foreign and domestic financing, of 43% and 57%, respectively. The gross financing for this strategy assumes a foreign/domestic mix of 28% and 72%, respectfully.

4.3 Baseline Projection and Alternative Strategies

Table 6 presents new financing and the gross borrowing by financing source from the alternative strategies the Government considered for the period ending FY2024/25. Each alternative strategy presented different combinations of borrowing instruments, thereby resulting in the various debt compositions at the end of the strategy period (see Table 7).

Table 6: Gross Borrowing by Instrument under Alternative Strategies (In % of Gross Financing Needs by end-FY2024/25)

Gross Financing Source by Interest Rate Type	Total Gross Borrowing (FY2022/23- FY2024/25) as a % of Gross Financing Needs			
	S1	S2	S3	S4
FX Multilateral Loans (Fixed)	0	0	0	0
FX Multilateral Loans (Floating)	5	9	9	9
FX Bilateral Loans (Fixed)	-	-	-	-
USD Commercial Loans (Floating)	13	15	9	12
Non-USD Commercial Loans (Floating)	-	-	4	-
USD Commercial Loans (Fixed)	2	2	2	2
USD Bonds (Fixed)	1	-	-	1
USD Bonds (Floating)	2	1	-	-
Other USD Loans (Floating)	2	2	2	2
USD Liability Management (Fixed)	4	4	4	4
BSD Commercial Loans (Floating)	3	1	5	3
BSD Commercial Loans (Fixed)	4	2	-	-
BSD Bonds (Fixed)	5	13	14	14
BSD bonds (Floating)	5	-	-	-
BSD 10 yr. Bonds (Incl. converted T Bills) (Fixed)	-	2	5	3
BSD 7 yr. Bonds (Fixed)	0	0	1	1
BSD 3 yr. Bonds (Fixed)	0	1	0	2
BSD T-Bills/Notes (Fixed)	43	39	39	40
Other Short Term BSD Debt (Fixed)	11	9	9	9
Foreign Financing	**28**	**32**	**28**	**28**
Domestic Financing	**72**	**68**	**72**	**72**
Net Financing Source by Interest Rate Type	**Total Net Borrowing (FY2022/23- FY2024/25) as a % of Gross Financing Needs**			
	S1	**S2**	**S3**	**S4**
Net Foreign Financing	1	7	8	4
Net Domestic Financing	4	2	5	6
Total Net Financing	5	9	13	10
Of which: Net Foreign/Domestic Financing Mix	20/80	75/25	59/41	43/57

Table 7: Composition of Debt Portfolio by Instrument under Alternative Strategies (In % of Outstanding Portfolio as at end-FY2024/25)

Outstanding by instrument	Sep-2021	FY2021/2022	As at End FY2024/25			
	Current	Projected	S1	S2	S3	S4
Multilateral Loans (Fixed)	0	0	0	0	0	0
Multilateral Loans (Floating)	11	10	10	12	13	13
Bilateral Loans (Fixed)	1	1	0	0	0	0
USD Commercial Loans (Floating)	7	10	10	11	7	9
Non-USD Commercial Loans (Floating)		2	0	0	2	0
USD Commercial Loans (Fixed)	2	2	2	2	1	1
USD Bonds (Fixed)	24	22	22	21	21	21
USD Bonds (Floating)	0	0	1	1	0	0
Other USD Loans (Floating)	0	2	2	2	2	2
Liability Management (Fixed)	0	3	3	3	3	3
BSD Commercial Loans (Floating)	3	0	2	1	3	2
BSD Commercial Loans (Fixed)	1	1	3	2	0	0
BSD Bonds (Fixed)	20	2	17	23	23	23
BSD Bonds (Floating)	18	19	14	11	11	11
BSD 10 yr. Bonds (Incl. converted T Bills) (Fixed)		16	0	1	3	2
BSD 7 yr. Bonds (Fixed)		0	0	0	1	1
BSD 3 yr. Bonds (Fixed)		0	0	1	0	2
BSD T-Bills/Notes (Fixed)		0	11	8	8	8
Other Short-term BSD Debt (Fixed)		10	3	2	2	2
Foreign	**44.9**	**52**	**50**	**51**	**49**	**49**
Domestic	**55.1**	**48**	**50**	**49**	**51**	**51**
Total	**100**	**100**	**100**	**100**	**100**	**100**

The outcomes of cost and risk trade-offs of the various alternative strategies reflect a balance between costs and risks and are used to inform the choice of the optimal strategy. Table 8 and Figure 7 show the cost and risk characteristics of the debt portfolio under alternative strategies considering the underlying assumptions.

Table 8: Cost and Risk Indicators under Alternative Strategies

Cost and Risk Indicators		Sep-21	FY2021/22	As at End FY2024/25				Long-term Targets
		Current	Projected	S1	S2	S3	S4	
Nominal debt as % of GDP		98.1	97.7	84.7	84.7	84.7	84.7	<50%
Present value debt as % of GDP		95.0	95.8	83.0	82.4	82.4	82.4	
Interest payment as % of GDP		4.2	4.4	4.1	4.1	4.1	4.1	
Implied interest rate (%)		4.9	4.5	4.7	4.7	4.7	4.7	<5%
Refinancing Risk	Debt maturing in 1 yr. (% of total)	22.3	26.0	19.1	16.0	15.4	16.4	
	Debt maturing in 1 yr. (% of GDP)	21.9	24.7	16.2	13.6	13.1	13.9	
	ATM External Portfolio (yrs.)	7.0	5.8	5.5	5.8	5.9	6.0	
	ATM Domestic Portfolio (yrs.)	7.5	7.3	7.2	7.0	7.1	6.9	
	ATM Total Portfolio (yrs.)	7.3	6.6	6.4	6.4	6.5	6.4	>6.5yrs
Interest Rate Risk	ATR (yrs.)	5.0	4.6	3.8	4.0	4.3	4.2	>5yrs
	Debt refixing in 1 yr. (% of total)	56.1	61.2	55.7	50.1	46.7	47.3	
	Fixed rate debt incl. T-bills (% of total)	61.5	57.3	59.0	61.7	65.0	65.3	
	T-bills (% of total)	11.1	10.0	10.6	8.3	8.0	8.5	
FX Risk	Non-USD FX debt as % of total	5.4	0.0	0.7	0.7	0.7	0.7	
	FX debt as % of total debt	44.9	49.0	49.6	50.9	49.0	49.1	30%

Overall, the cost and risk indicators analyzed under each strategy improved over the medium-term. Both the nominal and Present Value (PV) of debt to GDP ratios across all the alternative strategies are lower than the levels in September 2021, which indicates the Government's commitment to fiscal consolidation over the medium-term and interim progress towards achieving the long-term debt target set out in the FRA. As shown in Table 8, under current market conditions, Strategy 3 (S3) is more feasible, produced better performance under stressed conditions and therefore has greater benefits to debt management objectives. When taken overall, S3:

- presents the lowest overall risk for similar cost as the other alternative strategies.
- minimizes overall refinancing risk by stabilizing the portfolio's ATM and reducing the stock of debt maturing in one year as a percentage of total debt and GDP.
- lowers overall interest rate risk by reducing the stock of debt refixing in 1 year as a percentage of total debt, scales down the amount of short-term debt refixing in one year and stabilizes the ATR. Although S4 performed marginally better when the fixed rate debt as a percentage of total was considered; S3 displayed a better overall performance in managing interest rate risk, having less short-term debt.
- reduces overall FX risk by curtailing the amount of non-USD denominated debt as a percentage of total debt.
- reduces the debt to GDP ratio in both present value and nominal terms when compared to the current and projected ratios.
- reduces the cost of debt in terms of interest payments as a percent of GDP and the implied interest rate.
- aligns with the gradual approach towards achieving long-term debt targets.

The redemption profiles for alternative strategies by end-FY2024/25 are shown in Figure 6. Although all strategies extend the maturity of debt by reducing the stock of short-term debt, including Treasury bills to varying degrees, the remaining balance of this debt is due in the FY2025/2026. The high maturities of foreign debt observed between financial year ended 2030 and 2033 are mainly associated with the upcoming retirement of bonds previously issued. However, the Government has taken the proactive risk management approach of establishing and funding sinking funds to assist in redeeming these upcoming bond repayments.

Figure 6: Redemption Profiles for Alternative Strategies (End-FY2024/25)

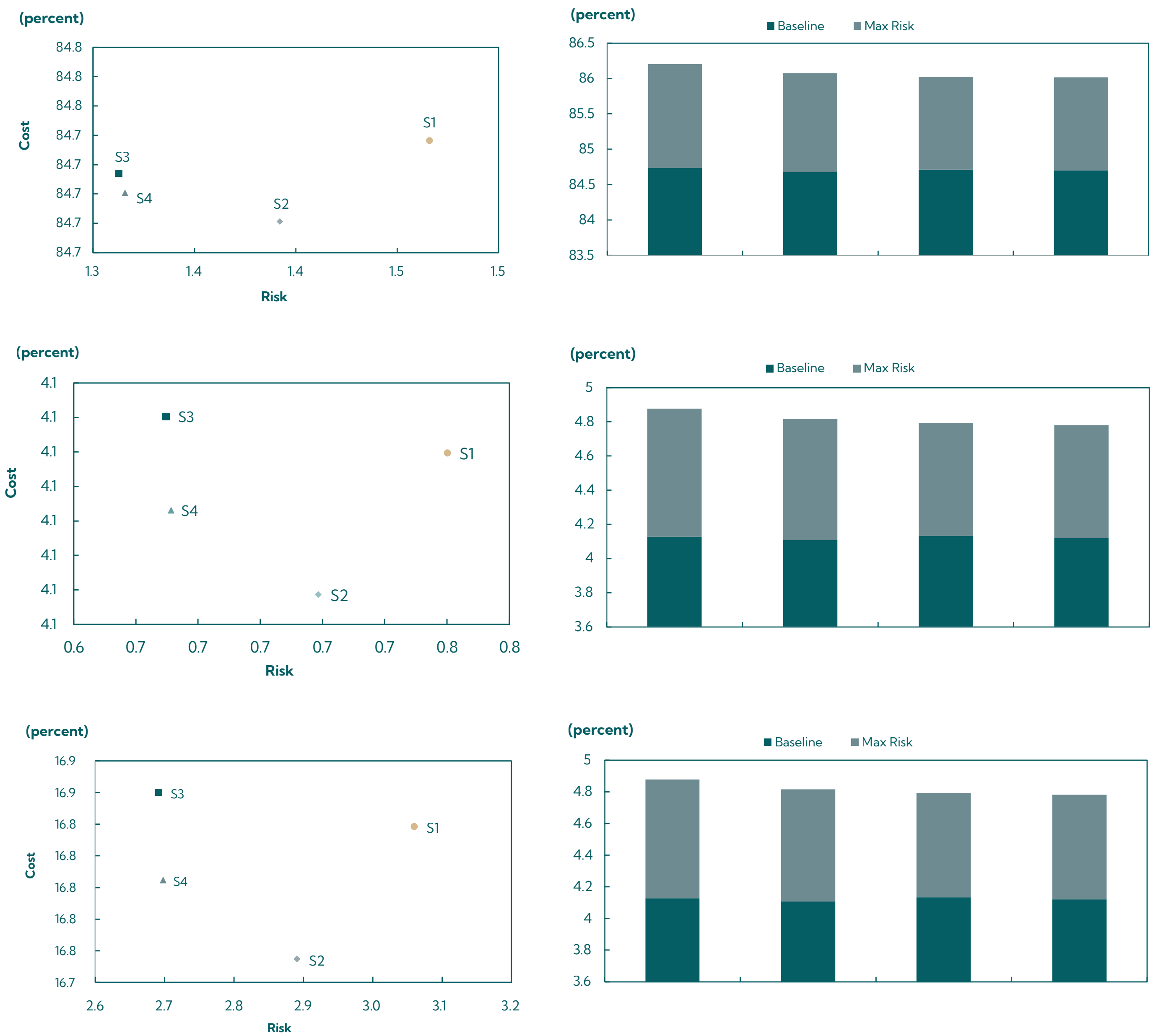
4.4

Effect of Shocks on the Costs and Risks Characteristics of Debt

Baseline pricing and shock scenario analysis considered the following indicators: Present Value of Debt/GDP, interest payments/revenues, interest payments/GDP and total debt service/GDP (see Figure 7). The outcome of the analysis indicates the extent of risk associated with each strategy under the baseline and shock scenarios. Risk measures estimate the potential unexpected increase in debt service payments produced by an unanticipated shift in market variables, namely, changes in interest or exchange rates. In a deterministic setting, risk is measured as the difference between the cost over the period under a shock scenario and the baseline cost.

Strategy 3 presents the lowest overall cost and risk combination across all indicators under a shocked scenario.

Figure 7: Cost-Risk Representation of Alternative Borrowing Strategies



5

Optimal Debt Management Strategy

List of Tables

To summarize, the Government intends to pursue Strategy 3 (see details in Table 9) for the following reasons:

- S3 presents the best overall performance when compared to September 2021 and the financial year end June 2022 (projected);
- S3 performs the best in achieving the debt management objective by reducing cost and risk when compared to the other alternative strategies;
- S3 was more resilient to shocks, as measured by the lowest cost and risk combinations across all indicators under a shocked scenario (see Figure 7); and
- S3 is more feasible, given current market conditions and the ongoing pandemic; and presents a more gradual approach towards the long-term target by minimize costs and reduce risk over the medium-term.

Table 9: Selected Strategy Details

Indicators	Financial Year ended		
	2023	2024	2025
Primary Deficit/(Surplus)	(91)	(369)	(651)
Interest on Existing Debt	506	446	401
Amortization on Existing Debt	2,860	852	901
Interest on New Debt	–	120	177
Amortization on New Debt	–	1,319	1,437
Gross Financing Needs	**3,276**	**2,368**	**2,266**
Financed by:			
FX Multilateral Loans (Fixed)	0	0	0
FX Multilateral Loans (Floating)	189	260	252
FX Bilateral Loans (Fixed)	–	–	–
USD Commercial Loans (Floating)	330	124	244
Non-USD Commercial Loans (Floating)	150	–	150
USD Commercial Loans (Fixed)	71	26	26
USD Bonds (Fixed)	–	–	–
USD Bonds (Floating)	–	–	–
Other USD Loans (Floating)	25	50	50
USD Liability Management (Fixed)	150	150	–
Total Foreign Financing	916	610	722
BSD Commercial Loans (Floating)	206	80	70
BSD Commercial Loans (Fixed)	–	–	–
BSD Bonds (Fixed)	634	249	190
BSD Bonds (Floating)	–	–	–
BSD 10 yr. Bonds (Incl. converted T Bills) (Fixed)	235	235	225
BSD 7 yr. Bonds (Fixed)	121	125	110
BSD 3 yr. Bonds (Fixed)	1,079	1,019	949
BSD T-Bills/Notes (Fixed)	55	50	–
Other Short-Term BSD Debt (Fixed)	30	–	–
Domestic Financing	**2,360**	**1,758**	**1,543**
Total Gross Financing	**3,276**	**2,368**	**2,266**

6

Debt Sustainability

The Bahamas' 2020 Debt Sustainability Analysis included in the IMF Country Report following the 2020 Article IV Consultation indicated that the public debt, at its then current level of 81.3% of GDP (end-December 2020) was sustainable and expected to remain sustainable over the medium-term. However, like most economies, the impact of the global COVID-19 crisis, combined with local natural disasters, like Hurricane Dorian, have increased risks to debt sustainability.

Despite the pandemic, The Bahamas has implemented several key Public Financial Management (PFM) reforms to support debt sustainability. This includes the FRA, which was passed in 2021 to, among other objectives, guide the formulation and implementation of fiscal objectives for debt. The long-term debt and fiscal objectives, as outlined in the FRA, are to reduce these indicators to no more than 50% and 0.5% of GDP, respectively.

The Government's medium-term fiscal strategy outlines a path for a gradual, sustained and orderly achievement of the fiscal balance target, by end-FY2024/25. Accordingly, in addition to the underlying projected primary surpluses, the financing combination of the selected medium-term debt strategy (S3) is expected to gradually bring the Government closer to the long-term debt target.

7

MTDS Implementation, Monitoring, Review and Reporting

The recommended strategy will be implemented through the annual borrowing plan that delivers the Government gross funding needs over the medium-term. The borrowing plan will outline the timing, currency and potential terms of the expected securities to be issued and the anticipated loan disbursements per creditor.

The mix of the borrowing instruments will be aligned to the FY2021/22 MTDS objectives as previously outlined above. Specifically, the major financing instruments will be loans and bonds of medium to long term tenor, mainly contracted in BSD and USD, and a preference for fixed interest rates to reduce risks (refinancing, interest rate and FX risks) in the debt portfolio. The strategy will also gradually reduce the stock of treasury bills and other short-term debt to curtail refinancing risks. Under this strategy, liability management operations will be employed as part of the risk management activities to achieve the preferred debt portfolio structure.

7.1 Implementation, Monitoring and Review

The domestic debt issuance program will be reviewed on a quarterly basis by the DMO, which will also engage market participants and other relevant stakeholders. Further, the assumptions in the strategy will be compared with the outcomes of the macroeconomic environment, including the fiscal deficits, general price levels (exchange, inflation and interest rates) at the end of FY2023/24—or earlier, depending on market conditions. The assumptions may be adjusted, as appropriate, based on the outcome of this exercise during the annual review.

Similarly, the actual borrowing and the cost risk indicators will be assessed against the projections under the selected strategy to gauge progress towards the long-term targets outlined in the document. Priority focus will be given to ensuring the achievement, at the earliest, of the 30% target for the ratio of foreign debt to total debt. In this context, and consistent with the key debt management objective of securing debt at the lowest cost and prudent degree of risk, the Government will continue to monitor market absorption metrics for domestic securities and leverage opportunities for a higher level of domestic issuances relative to foreign currency debt.

Special attention will also be given to contingent liabilities to evaluate and address any changes in these risks. The resulting public debt structure will inform the revision of the budget provisions and management of associated debt costs and risks.

The annual review of the strategy will be communicated through regular debt management reports. The quarterly Public Debt Bulletins will also be published as part of best practices in debt transparency. The implementation outcome of the FY2022/23 strategy will inform the update of the FY2023/24 MTDS, with a view to achieving continuous improvement in debt management and sustainability.

It is recognized that accurate forecasts of Government's cash flows are required for effective implementation of the debt management strategy. In keeping with the requirements of the PFMA, the Government's intent to implement a Treasury Single Account (TSA) will provide for more optimal utilization and management of cash resources, and improved fiscal, debt management and monetary policy coordination which could positively impact the government's debt servicing cost.

7.2 *Reporting*

Consistent with good practices in debt transparency, and to ensure compliance with the PDMA, the FY2022/23 – FY2024/25 MTDS is being submitted to the Minister for review and forwarding, along with his recommendations, to the Cabinet for approval, with or without amendments. The approved debt management strategy is to be tabled in the House of Assembly at the same time as the Fiscal Strategy Report and, thereafter, the FY2022/23 – FY2024/25 MTDS is to be published.

MEDIUM-TERM DEBT MANAGEMENT STRATEGY FY2022/23 TO FY2024/25

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