

## BAHAMAS

### 1. General trends

The Bahamian economy continued to recover in 2012, with a marginal increase in growth to 1.8% from 1.7% in 2011. The impetus for growth came mostly from tourism and construction activity. Nevertheless, the narrowness of the recovery constrained its impact on the labour market, leading to only marginal gains in employment. Inflation declined from 3.2% in 2011 to 2.0% in 2012 December-to-December as the cost of transport, communication and recreation and culture fell.

Two headwinds continue to challenge the economy and could undermine the strength and duration of the recovery. The first is the unsustainable fiscal position of the government; the second is weak domestic private sector investment and the related issue of poor bank credit quality. The fiscal deficit expanded to 5.6% of GDP in fiscal year 2011/2012, up from 4.6% of GDP in fiscal year 2010/2011, reflecting a decline in revenue in the face of higher expenditure. This trend has continued in the first half of 2012/2013.

Public sector debt has spiked since the recession and is now at levels (over 60% of GDP) that could hurt growth. The government has embarked on a fiscal consolidation programme designed to improve expenditure management, to achieve debt sustainability in the medium-term and to introduce a 15% VAT by July 2014. Domestic private sector activity remained weak, partly linked to caution in lending by commercial banks owing to high non-performing loans. The current account deficit widened from 13.8% of GDP in 2011 to 17.8% of GDP in 2012, partly reflecting increased imports for construction projects and a smaller surplus on the services account due to higher payments for construction and transportation services.

Economic activity was expected to have been flat in the first quarter of 2013 compared with the same period in 2012. This stemmed from a decline in tourism value added that was expected to be offset by increased construction activity. Tourist arrivals by air, which include the high value-added stopover segment, contracted by 3.4% after growing by 11.2% in the same quarter of 2012. Construction was buoyed by the Baha Mar project and public infrastructure works. The fiscal deficit expanded due to higher government spending, driven by capital expenditure. The current account deficit most likely widened, reflecting higher imports of construction materials and household goods that offset sluggish growth in exports.

Growth is expected to strengthen to 3.0% in 2013, underpinned by a continued recovery in stopover tourism and construction activity with spillovers into the wholesale and retail sector. Nevertheless, actual growth will depend on the strength of the recovery in the United States. The fiscal deficit is expected to be contained to around 6.5% of GDP, as the government strives to contain expenditure and strengthen revenue collections. The current account deficit is projected to widen in 2013, as the uptick in activity fuels higher demand for imports, especially for construction projects, which will offset growth in tourism receipts.

## 2. Economic policy

### (a) Fiscal policy

Fiscal management remains the principal challenge for the Bahamas. The government implemented a fiscal stimulus package and acted as employer of last resort to combat the adverse effects of the global crisis. As a result, the fiscal deficit jumped from 1.8% of GDP in fiscal year 2007/2008 to 5.6% of GDP in fiscal year 2011/2012. Similarly, public debt rose from 44% of GDP in 2008 to 61% of GDP in 2012.

Fiscal policy was again expansionary in fiscal year 2011/2012, as the government maintained spending on a number of projects, including the airport improvement project and major road works aimed at nurturing the recovery and reducing hardship for citizens. The fiscal deficit increased to 5.6% of GDP in 2012 from 4.6% in 2011. Total expenditure expanded by 5.2% to 17.0% of GDP, driven by an 18.9% rise in capital spending. The surge in capital spending, 3.8% above budget, was associated with significant road and other infrastructure works and substantial cost overruns on these projects. Other outlays went towards the government's acquisition of land and the acquisition of a new government headquarters building. Current spending was contained due to lower domestic debt interest payments on account of the lowering of the prime lending rate in the previous year, as government consumption was higher. Growth in revenues receded, owing to lower receipts from taxes on international trade, which reverted to trend following a one-off surge in the stamp tax from the sale of an oil refinery in the previous year. Non-tax revenues were buoyed by the payment of deferred interest on bond investments and proceeds from the sale of government property. Public sector debt increased from 61.8% of GDP in calendar 2011 to 67.2% of GDP in calendar 2012, reflecting increased borrowing by the central government and public corporations.

The worsening fiscal situation continued into the first half of fiscal year 2012/2013. The deficit expanded by 106.3 million Bahamian dollars (B\$) to 6.3% of GDP. Fiscal deterioration stemmed from a 7.2% contraction in revenue in the face of 5.8% growth in spending. Capital spending continued to surge with substantial expenditure on major roads and other infrastructure. Revenues contracted by 6.0% as excise tax collections normalised after the payment of arrears in the previous year. Non-tax proceeds rose in line with higher receipts from public enterprises.

With a continuation of the trend growth in spending, alongside dampened revenues, the government is likely to overshoot its deficit target of 6.5% of GDP for 2012/2013. However, the government has embarked on a programme to rein in capital spending and improve revenues. Key short-term measures include a review of customs fees to bring them in line with the cost of providing the service, a property tax amnesty beginning in March 2013 to encourage citizens to pay on time, improved execution and reprioritisation of capital projects, and upgrading of the tax administration infrastructure to strengthen collections. In the medium to longer term, reform measures include the 15% VAT slated for July 2014. Expenditure reform will focus on steady reduction in spending by 0.5% of GDP starting in 2013/2014 to 2016/2017. This would entail prudential expenditure management, cuts in waste and improved prioritisation of spending. Efforts by the government to set up a national lottery and allowing gambling by locals, partly as a means of raising revenue to aid in fiscal consolidation, were rejected in a referendum in early 2013.

## **(b) Monetary and exchange rate policy**

Monetary policy was neutral in 2012 since, with the economy on the path to recovery, the central bank did not adjust its policy rates. Nevertheless, the bank monitored developments in the international and domestic economy for pressure points that could affect the fixed exchange rate.

Domestic credit grew by 2.1%, directed to the public sector, as credit to the private sector was flat. Banks increased their holdings of government paper in an environment where rates of return on other investments remained very low. Growth in credit to the private sector has averaged less than 1.0% over the last three years and, despite the recovery, private investment remains weak amid slim profit margins and uncertainty about future prospects. During the year, credit increased to the distribution (B\$ 45 million), transport and manufacturing sectors but was offset by reduced flows to other sectors including tourism and professional services.

Growth in the broad money supply (M2) slowed to 0.4%, reflecting the marginal pickup in economic activity. Savings deposits increased marginally, but time deposits contracted by 4.1% due in part to a significant decline in interest rates that they attracted. Liquidity in the banking system remained elevated due both to sluggish private sector credit demand and to increased discretion by banks in lending as a result of high loan losses. In this environment, the weighted average interest rate spread widened by 51 basis points. The average deposit rate moderated by 61 basis points to 2.02%, while the loan rate fell by 10 basis points to 10.88%. Bank credit quality deteriorated amid continued high levels of unemployment, which affected the ability of creditors to service their loans. Private sector loan arrears rose by 3.5% to B\$ 1.251 billion, while non-performing loans increased by 6.3%. Banking sector profitability weakened, with net income falling by 26.5%, reflecting lower interest income.

The central bank has embarked on a programme to strengthen regulatory oversight of the financial system. Important measures include the full roll-out of its risk based supervision framework (RBSF), which the bank hopes to entrench as standard practice, and a credit bureau to provide a formal, secure mechanism for exchanging credit information in an effort to reduce the incidence of non-performing loans.

## **3. The main variables**

### **(a) The external sector**

Imports picked up as activity continued to recover, contributing to a widening of the current account deficit to 17.8% of GDP in 2012 from 13.8% of GDP in 2011. The goods deficit expanded by 11.5% to B\$ 2.376 billion, driven by an 11.9% (US\$ 353.2 million) expansion in imports, which offset the 13.1% (US\$ 108.9 million) growth in exports. Non-oil imports and building materials and equipment were boosted by the large foreign investment-based projects and government infrastructure works. Higher import volume and prices led to a 13.1% increase in payments for oil imports.

The services account surplus narrowed by 7.5% to B\$ 1.215 billion due to higher payments for construction services related to foreign hotel construction and increased payments for transportation services. These more than offset the 3.6% increase in travel-related receipts, associated with the recovery in the tourism sector and higher receipts for government services. The income account deficit deteriorated by B\$ 64 million as a result of higher profit repatriations by non-banks.

The surplus on the capital and financial account improved by 4.7%, buoyed largely by government borrowing of B\$ 180.0 million and loan financing for infrastructure projects. Commercial banks significantly scaled back their short-term capital outflows. Meanwhile, net foreign direct investment contracted sharply (33.3%) to B\$ 444.8 million. This mainly reflected a return to trend in equity investments, which had surged in 2011 on account of the government's sale of its majority shareholding in Bahamas Telecommunications Company (BTC) and a fall in real estate purchases. The new government had announced plans to re-nationalize BTC, but this is not expected to occur in the short term. International reserves declined by 5.8% to US\$ 816 million, covering around four months of non-oil merchandise imports.

### **(b) Economic activity**

The economy continued to recover, growing by 1.8% in 2012. Activity was buoyed by increased tourist arrivals, especially the high value-added air arrivals, dynamic growth in construction and higher value added in transport and communications. Total visitor arrivals increased by 6.3% to 5,940,170, boosted by a 7.1% rise in air arrivals and a 6.1% increase in sea arrivals. This growth reflected the recovery in major markets and aggressive marketing campaigns, including incentive programmes. Information from a sample of hotels indicated that room revenue rose by 4.0% in 2012, surpassing the almost 3% gain in 2011. However, this stemmed from an increase in the average occupancy rate, as the average daily room rate fell by 3.0% to B\$ 229.2, reflecting discounting by some hotels to attract visitors.

Construction activity surged 24.3%, propelled by foreign investment-funded hotel construction including the Baha Mar resort and Albany Hotel. These were complemented by significant public sector capital works, including a number of roads and the airport. Nevertheless, domestic private construction remained weak, reflecting high unemployment and debt deleveraging by private individuals. This was reflected in a 28.1% contraction in total mortgage loans for new construction and repairs. Moreover, mortgage commitments indicate that the challenges facing domestic private construction are expected to last into the medium term. In the offshore financial services sector, the number of licensed banks and trust companies declined by 10 to 268. Nevertheless, activity in the sector remained buoyant. The sector has overhauled its regulation, prudential oversight mechanisms and risk assessment systems to make them compliant with international standards.

On the expenditure side, gross domestic investment rebounded strongly to grow by 10.5%, bolstered by public infrastructure investment. Nevertheless, consumption expenditure declined by 1.5% following marginal growth in 2011, as consumer confidence remains weak in the face of the narrow recovery.

### **(c) Prices, wages and employment**

Inflation fell from 3.2% in 2011 to 2.0% in 2012 December-to-December. Transport prices fell despite the volatility in international fuel prices. Prices in the communication and recreation and culture sub-sectors also moderated. Meanwhile, price increases were recorded for clothing and footwear, food and beverages and medical care and health. Domestic fuel costs rose in line with higher international oil prices. The average price of gasoline and diesel rose by 5.4% and 6.2%, respectively, leading to an increase in the Bahamas Electricity Corporation's fuel charge.

Wages remained largely stable in 2012, as the government sought to contain its current costs. The modest increase in wage costs came largely from the payment of increments to civil servants. Improved economic conditions contributed to marginal gains in employment. As a result, unemployment fell from

15.9% in 2011 to 14.7% in 2012. Nevertheless, unemployment among the 15-24 age cohort, including university graduates, remained exceedingly high, at over 30%. Unemployment was lower among females than males.

Table 1  
BAHAMAS: MAIN ECONOMIC INDICATORS

	2004	2005	2006	2007	2008	2009	2010	2011	2012 a/
<b>Annual growth rates b/</b>									
Gross domestic product	0.9	3.4	2.5	1.4	-2.3	-4.2	1.0	1.7	1.8
Per capita gross domestic product	-0.6	1.9	1.0	0.0	-3.7	-5.5	-0.3	0.4	0.6
Gross domestic product, by sector									
Agriculture, livestock, hunting, forestry and fishing	-6.8	-9.9	-8.2	-7.3	2.9	3.7	4.4	-9.2	-9.0
Mining and quarrying	6.4	-5.0	15.3	-11.7	26.2	-3.3	9.2	-20.7	-8.4
Manufacturing	9.6	-5.6	10.8	-12.6	-7.3	-6.0	9.9	-1.8	16.4
Electricity, gas and water	5.1	5.3	-2.3	3.7	9.4	-2.6	-5.4	7.3	-9.2
Construction	-16.9	33.0	20.4	-34.7	28.7	-10.2	27.7	-3.6	24.3
Wholesale and retail commerce, restaurants and hotels	3.0	10.0	2.3	8.7	-4.4	-2.8	-1.6	7.4	0.5
Transport, storage and communications	3.6	5.3	2.7	-11.2	-7.4	4.4	-8.2	6.4	9.8
Financial institutions, insurance, real estate and business services	2.2	1.5	-3.5	11.5	-2.1	-6.7	3.0	2.3	-2.4
Community, social and personal services	3.5	-1.4	-3.5	3.8	-3.3	-6.0	3.2	0.5	0.0
Gross domestic product, by type of expenditure									
Final consumption expenditure	-1.8	7.4	2.8	1.0	-2.2	-8.0	-0.1	0.1	-0.2
Government consumption	-3.2	3.1	1.8	-0.2	7.2	3.9	-0.3	3.5	1.9
Private consumption	-1.5	8.2	3.0	1.3	-3.8	-10.3	-0.1	-0.7	-0.7
Gross capital formation	-5.1	24.7	22.0	-2.6	-9.3	-9.4	1.2	8.7	20.6
Exports (goods and services)	11.7	-2.1	1.9	-1.4	-2.2	-3.2	1.3	6.3	5.7
Imports (goods and services)	3.5	14.3	12.2	-3.7	-5.9	-12.2	-0.4	7.5	13.0
<b>Millions of dollars</b>									
Balance of payments									
Current account balance	-307	-305	-1 031	-954	-872	-809	-813	-1 091	-1 452
Goods balance	-1 429	-1 763	-2 033	-2 154	-2 243	-1 825	-1 888	-2 132	-2 376
Exports, f.o.b.	477	549	694	802	956	711	702	834	942
Imports, f.o.b.	1 907	2 312	2 727	2 956	3 199	2 535	2 591	2 966	3 318
Services trade balance	1 013	1 611	1 206	1 433	1 488	1 155	1 312	1 314	1 215
Income balance	-141	-159	-165	-186	-78	-152	-235	-236	-300
Net current transfers	251	6	-39	-47	-39	14	-3	-36	10
Capital and financial balance c/									
Net foreign direct investment	274	563	706	746	860	497	872	667	445
Other capital movements	217	-347	246	162	120	565	-14	448	932
Overall balance	183	-89	-79	-46	109	253	45	24	-75
Variation in reserve assets d/	-183	89	79	46	-109	-253	-45	-9	75
Other financing	0	0	0	0	0	0	0	-15	0
Other external-sector indicators									
Net resource transfer (millions of dollars)	349	57	787	723	903	909	623	864	1 077
Gross external public debt (millions of dollars)	285	287	289	273	384	703	711	799	1 037

Table 1 (concluded)

	2004	2005	2006	2007	2008	2009	2010	2011	2012 a/
<b>Employment</b>	<b>Average annual rates</b>								
Labour force participation rate	75.7	76.3	75.1	76.2	76.3	73.4	...	72.3	...
Unemployment rate e/	10.2	10.2	7.6	7.9	8.7	14.2	...	15.9	14.0
<b>Prices</b>	<b>Annual percentages</b>								
Variation in consumer prices (December-December)	1.9	1.2	2.3	2.8	4.6	1.3	1.4	3.2	2.0
Nominal deposit rate f/	3.8	3.2	3.4	3.7	3.9	3.8	3.4	2.6	2.1
Nominal lending rate g/	11.2	10.3	10.0	10.6	11.0	10.6	11.0	11.0	10.8
<b>Central government h/</b>	<b>Percentajes of GDP</b>								
Total revenue	14.7	15.9	16.8	18.2	17.0	17.7	22.0	20.1	18.4
Tax revenue	13.0	14.2	15.1	15.2	13.7	14.2	16.4	16.2	15.6
Total expenditure	16.1	16.5	18.2	19.9	21.4	22.8	24.2	25.7	24.7
Current expenditure	14.8	14.9	16.1	17.1	18.2	19.6	20.8	20.7	20.4
Interest	1.7	1.5	1.6	1.7	1.9	2.3	2.7	2.3	2.3
Capital expenditure	1.3	1.6	2.1	2.8	3.2	3.2	3.3	5.0	4.3
Primary balance	0.2	0.8	0.0	0.1	-2.5	-2.8	0.6	-3.3	-3.9
Overall balance	-1.5	-0.7	-1.6	-1.6	-4.4	-5.1	-2.1	-5.7	-6.2
Public debt	...	35.5	36.2	36.9	37.4	44.1	45.7	50.2	54.5
<b>Money and credit</b>	<b>Percentages of GDP, end-of-year stocks</b>								
Domestic credit	73.7	76.6	84.7	89.4	95.9	102.8	107.1	108.4	106.6
To the public sector	12.5	12.3	13.5	14.6	16.6	18.5	23.8	24.0	25.2
To the private sector	61.2	64.3	71.2	74.7	79.3	84.3	83.3	84.4	81.4
Monetary base	9.0	7.6	7.1	8.1	7.8	8.9	10.5	11.2	11.0
Money (M1)	62.3	62.7	64.6	67.8	71.8	77.1	78.5	80.2	77.4
M2	61.0	60.8	62.6	65.4	69.4	74.2	75.6	77.5	74.7
Foreign-currency deposits	1.4	1.9	2.0	2.4	2.4	3.0	2.8	2.6	2.6

**Source:** Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official figures.

a/ Preliminary figures.

b/ Based on figures in local currency at constant 2006 prices.

c/ Includes errors and omissions.

d/ A minus sign (-) indicates an increase in reserve assets.

e/ Includes hidden unemployment. Nationwide total.

f/ Weighted average rate of deposit rates.

g/ Weighted average of lending and overdraft rates.

h/ Fiscal years, from July 1 to June 30.

Table 2  
**BAHAMAS: MAIN QUARTERLY INDICATORS**

	2011				2012				2013	
	Q.1	Q.2	Q.3	Q.4	Q.1	Q.2	Q.3	Q.4	Q.1	Q.2 a/
Goods exports, f.o.b. (millions of dollars)	166	204	178	181	203	190	214	220	...	...
Goods imports, c.i.f. (millions of dollars)	727	862	897	924	1 022	868	864	893	...	...
Gross international reserves (millions of dollars)	975	1 076	979	897	890	928	757	816	793	811 b/
Consumer prices (12-month percentage variation)	2.6	3.6	3.4	3.2	2.9	2.2	1.8	2.0	1.2	...
Average nominal exchange rate (Bahamas dollars per dollar)	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00
Nominal interest rates (annualized percentages)										
Deposit rate d/	3.2	2.9	2.3	2.2	2.2	2.1	1.9	1.8	1.9	1.7 b/
Lending rate e/	11.2	11.1	11.0	10.6	10.3	11.0	11.2	11.1	10.9	10.8 b/
Monetary policy rates	5.3	5.0	4.5	4.5	4.5	4.5	4.5	4.5	4.5	4.5 b/
Domestic credit (variation from same quarter of preceding year)	2.9	-0.2	0.0	0.4	2.1	6.6	5.1	3.4	2.4	-0.1 b/
Non-performing loans as a percentage of total credit	10.7	10.7	11.4	13.0	13.1	13.3	13.4	13.9	14.2	14.3 f/

**Source:** Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official figures.

a/ Preliminary figures.

b/ Figures as of May.

c/ Figures as of January.

d/Weighted average rate of deposit rates.

e/ Weighted average of lending and overdraft rates.

f/ Figures as of April.