



Monthly Economic and Financial Developments September 2007

In an effort to provide the public with more frequent information on its economic surveillance activities, the Central Bank has decided to release monthly reports on economic and financial sector developments in The Bahamas. The Bank monitors these conditions as part of its monetary policy mandate, to assess whether money and credit trends are sustainable relative to levels of external reserves required to protect the value of the Bahamian dollar and, if not, the degree to which credit policies ought to be adjusted. The main data source for this surveillance is financial institutions' daily reports on foreign exchange transactions and weekly balance sheet statements. Therefore, monthly approximations may not coincide with calendar estimates reported in the Central Bank's quarterly reports. The Central Bank will release its "Monthly Economic and Financial Developments" report on the Monday following its monthly Monetary Policy Committee Meeting.

Future Release Dates:

2007: December 3rd

1. Domestic Economic Developments

Indications are that the expansion in the Bahamian economy moderated somewhat during September, amid a leveling off in foreign investment inflow and tourism activity. Strengthened seasonal demand for foreign currency also contributed to a fall-off in both bank liquidity and external reserves.

Total visitor arrivals fell by 7.0% during the first seven months of 2007, in comparison to the previous year, due to contractions in both the air and sea segments, by 8.0% and 6.5%, respectively. All of the major ports registered declines, with the largest decrease noted for the Family Islands of 8.6% to 0.8 million visitors. Similarly, travelers to the Grand Bahama market fell by 8.3% to 0.4 million, and arrivals to New Providence weakened by 5.9% to 1.6 million.

On the fiscal side, the deficit for the first two months of FY2007/08 stood at \$23.2 million, in contrast to a \$0.4 million surplus in the corresponding period of FY2006/07. This outturn reflected a 7.7% rise in expenditure, as current and capital outlays firmed by 4.1% and 25.0%, respectively. Moreover, total revenue moderated by 3.4%, occasioned by a 5.4% contraction in tax receipts which overshadowed the growth in non-tax revenue.

Inflation for the twelve months ending September moved higher vis-à-vis last year by 0.8 percentage points to 2.42%, owing to continuing price pressures from higher fuel costs. The most significant increases were recorded for other goods and services (4.62%), furniture & household operation (3.98%), food and beverages (3.82%), and recreation & entertainment services (3.35%).

2. International Developments

Based on the September edition of the IMF's "World Economic Outlook", the global economy expanded by a robust 5% in the first half of 2007, mainly reflecting positive developments in China and India, and expectations are for an additional 4.75% advance in the July to December period. However, several risks remain to this outlook, including the adverse impact of the United States mortgage crisis on the global financial system and continuing concerns over oil price induced inflation. Consequently, a number of central banks have adopted a cautious "wait and see" approach to monetary policy, with the exception of the Federal Reserve, which loosened monetary policy to stimulate aggregate demand in the United States' economy.

Conditions in the United States real estate sector continued to be negative during the review month. Housing starts fell by 10.2% to an annual rate of 1.19 million units, the lowest level in over a decade, and building permits contracted by 7.3% to a yearly rate of 1.23 million units. However, other sectors of the economy showed signs of improvement, as the trade deficit narrowed by \$1.4 billion to \$57.6 billion in August, with the decline in the US dollar contributing to the \$0.6 billion expansion in exports, while imports waned by \$0.8 billion. Retail sales in September rose by 0.6% over the previous month. The unemployment rate was relatively unchanged at 4.7%, as gains in non-farm employment of approximately 110,000 negated accretions to the labour force. In response to an appreciable deterioration in financial market conditions during September and the fear that there would be some spill over into the wider economy, the Federal Reserve reduced the federal funds rate for the first time in four years, by 50 basis points to 4.75%. The discount rate was also lowered by a similar magnitude to 5.25%.

The robust growth observed in the Chinese economy during the first half the year continued unabated in the third quarter, as increased investments, retail sales and exports propelled the rise in GDP over the nine month period to 11.5%. Correspondingly, the country's trade surplus rose by 69% to \$185.7 billion, resulting in foreign exchange reserves strengthening by over 45.1% on a year-on-year basis to a record \$1.43 trillion. Buoyed by the rapid rise in foreign and domestic investments, consumer price inflation, on a point-to-point basis, firmed by 5.2% in August. The Central Bank continued its policy of reducing the level of monetary accommodation during the review month, increasing the benchmark deposit and lending rates by 0.27 percentage points each, to 3.87% and 7.29%, respectively. In addition, the Bank raised the commercial banks' reserve requirement ratio by 0.5 percentage points.

Preliminary data for Japan showed industrial production in August rising by 3.4% on a monthly basis, following a rebound in auto manufacturing in the aftermath of the July earthquake. In addition, the trade surplus strengthened by more than 13.7% from the previous month to ¥892.2 billion, as the 2.4% contraction in imports offset the marginal fall in exports. Average prices in August rose by 0.5% on a monthly basis, but declined by 0.2% over the previous year. Given these developments, the Bank of Japan decided to maintain its benchmark interest rate at 0.5%.

Despite the dislocation in the financial sector in September, caused by the uncertainty surrounding the solvency of a major mortgage lender, indications are that the UK economy continued to strengthen. Preliminary data for the three months ended August revealed that industrial production advanced by 0.4% relative to the previous quarter, and retail sales were 1.3% higher supported by heightened non-food related purchases. The August trade deficit narrowed by £0.5 billion to £4.1 billion, reflecting an improvement in the goods deficit to £6.9 billion from a revised £7.4 billion a month earlier. The unemployment rate steadied at 5.4% in the three-months to August, while consumer prices increased by 1.8% in September, buoyed by higher costs for food products. Meanwhile, in light of the uncertainty surrounding the impact of the financial sector crisis on the wider economy, the Bank of England maintained its main interest rate at 5.75% in September.

Revised second quarter GDP estimates for the euro area showed total output increasing by 0.3%, although 0.5 percentage points lower than the expansion registered in the previous quarter. However, increased production of non-durable consumer goods supported a higher expansion in industrial production of 1.2% in August vis-à-vis 0.7% a month earlier. The unemployment rate was unchanged on a monthly basis at 6.9%; while increased costs for housing, transport and food products led to inflation rising by 0.4 percentage points to 2.1%. At its September meeting, the ECB kept its key interest rates unchanged in the wake of growing uncertainty surrounding the global financial markets.

In September, ongoing geopolitical tensions, combined with production disruptions in the Gulf of Mexico, elevated oil prices by 9.3% above the previous mark to \$78.84 per barrel. Production expanded by 0.24 million barrels per day (mb/d) to 30.6 mb/d, amid a rebound in oil production from Iraq and, in an effort to ensure adequate crude supplies to meet the demand of the upcoming winter season, OPEC agreed to boost its production by 0.5 mb/d beginning November 1st, 2007. Given volatile crude oil prices, uncertainty in the financial markets and a depreciating US dollar, investors increased their demand for safer investments. As a result, the price of gold rose by 10.4% to \$743.60 per ounce and silver firmed by 14.0% to \$13.77 per ounce.

