



2018 ANNUAL REPORT
& Statement of Accounts
for the year ended December 31, 2018



MISSION

To foster an environment of monetary stability conducive to economic development, and to ensure a stable and sound financial system through the highest standards of integrity and leadership.

VISION

To promote a leading financial services industry within the framework of dynamic monetary policy developments, modernized payment systems, sound management strategies and capacity building.

VALUES

Our commitment to fulfilling our Mission is embodied in our Core Values of:

- Objectivity
- Confidentiality
- Integrity
- Excellence
- Teamwork
- Empowerment
- Initiative

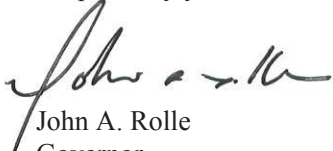


April 22, 2019

Dear Deputy Prime Minister:

In accordance with Section 32(1) of the Central Bank of The Bahamas Act, 2000, I have the honour of forwarding to you, on behalf of the Board of Directors, the Annual Report of the Bank for the year 2018. Included with this Report is the Annual Statement of Accounts of the Bank for the year.

Respectfully yours,



John A. Rolle
Governor

The Hon. K. Peter Turnquest
Deputy Prime Minister & Minister of Finance
Office of the Prime Minister
Cecil Wallace-Whitfield Centre
West Bay Street
Nassau, N.P., Bahamas

ABOUT THE BANK

Under the Central Bank of The Bahamas Act, 2000 (the Act), the Bank is mandated to promote and maintain monetary stability and balance of payments conditions, conducive to the orderly development of the economy; in collaboration with other financial institutions, to promote and maintain adequate banking services and high standards of conduct and management therein; and to advise the Minister of Finance on any matter of a financial or monetary nature referred by him [the Minister] to the Bank for its advice.

MONETARY POLICY

In its monetary role, a primary objective of the Bank is to ensure adequate support for the fixed parity of the Bahamian dollar against the United States' currency. To attain this objective, the Bank has to maintain adequate foreign reserves against the stock of its demand liabilities, and ensure that the demand for foreign exchange, stimulated principally by domestic credit expansion, does not exceed the pace at which the economy earns foreign exchange from real sector activities. In alignment to this goal, the Bank has statutory responsibility for the prudent management of the country's foreign currency reserves.

The Bank's administration of exchange controls is also closely linked to the fixed exchange rate policy objective. Capital controls, which have undergone gradual relaxation in recent years, restrain the movement of capital by residents; however, there are no restrictions on current payments.

PUBLIC DEBT & SINKING FUND MANAGEMENT

The Bank provides front, middle and back office services to the Government and its agencies, in activities involving debt issuance and administration, and the management of several sinking fund arrangements.

PAYMENTS

The Bank's involvement in the payments system is also integral to its overall mandate to promote the stability of, and confidence in the financial system. In carrying out its oversight function, the Bank seeks to ensure, *inter alia*, that the payments infrastructure functions smoothly, efficiently and fairly in the interest of all participants and users; that it minimizes and controls risks; and that the level of product innovation and development is adequate for the needs of the economy.

CURRENCY

The Bank meets the currency needs of the public by arranging for the procurement, storage and issuance of Bahamian banknotes and coins, as well as maintaining the quality of currency in circulation. Banknotes deemed as unfit are withdrawn from circulation and replaced.

FINANCIAL STABILITY

Prudential oversight of regulated entities is a critical part of the infrastructure to maintain high standards of service, conduct and management in the banking sector. A combination of off-site examinations, on-site inspections, and market intelligence, informs the risk-based assessments that are used to monitor the soundness of supervised financial institutions. Stress testing is undertaken to gauge resilience to key economic and financial shocks.

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FOREWORD

The Bahamian economy strengthened during 2018. The performance of the tourism sector propelled this outcome, as demand growth closely matched the expansion in airlift and high-end hotel room capacity, following the completion of the phased opening of the Baha Mar Resort. Growth in vacation rental demand (onshore stay in non-resort facilities) was also strong. In addition, a number of small to medium-scale foreign investment projects undergirded activity in the construction sector.

In this environment, the number of employed persons trended upwards, as businesses continued to on-board new staff. Nevertheless, gains in the labour force resulting from a reduction in the number of previously discouraged workers—combined with new job seekers—led to an uptick in the unemployment rate. Further, with an upward adjustment in the value added tax (VAT) rate by 4.5 percentage points on the 1st July to 12.0%, and gains in international oil prices, domestic price pressures firmed mildly, but with inflation staying below 2.5% over the year.

Fiscal sector developments were dominated by the implementation of the Government’s Fiscal Responsibility Act. This framework aligns with public finance and governance reforms, that should lead to a reduction in the deficit to GDP ratio to no more than 0.5% by FY2020/21 and the Government’s debt ratio to within 50% of GDP over the long-term. Overall, the deficit decreased in FY2017/18, as lower capital spending resulted in a decline in aggregate expenditures. This trend persisted into the first half of FY2018/2019, with the VAT-related increase in tax revenue, outstripping the modest growth in expenditure.

Even with the decrease in external reserves to \$1,196.3 million from \$1,417.4 million in 2017, the average import cover stayed well above international benchmarks. The reduction was largely because of the public sector’s reversal to a net reliance on domestic currency financing, as opposed to the sizeable foreign currency borrowing in 2017. Private sector demand for foreign currency also strengthened, both for trade and investment payments; however, these were closely matched by robust gains in private sector foreign currency inflows.

Given the improving economic conditions and the healthy external balances, the Bank decided to maintain its accommodative monetary policy stance. The Monetary Policy Committee (MPC) therefore focused its attention on identifying further Exchange Control liberalisation measures, to reduce the administrative burden on the public and


improve the “ease of doing business”. The Committee also endorsed proposals to increase the access of certain low-risk groups to commercial banking services, and the access of non-residents to Bahamian dollar deposit accounts.

In the area of supervision, the Bank maintained its active surveillance and regulatory agenda, particularly as it related to Basel II and III implementation. Guided by the results of the Caribbean Financial Action Task Force’s (CFATF) Mutual Evaluation Report (MER), the Bank strengthened its efforts in the area of combating money laundering, terrorism and proliferation financing. In this regard, the Bank adopted a more granular model to assess AML/CFT risks. Revised versions of the AML/CFT Guidelines were released to align with the revamped legislation passed in 2018. These initiatives also progressed through intensive collaboration with domestic regulators, and increased outreach to supervised financial institutions (SFIs).

Other important supervisory initiatives, included the transition of the credit unions to a risk-based oversight framework, similar to banks. In conjunction with other domestic regulators—preparations also concluded for the IMF’s Financial Sector Assessment Programme (FSAP) mission, which was conducted in early 2019. The last FSAP mission to The Bahamas was in 2012, which yielded generally positive results for the country and informed critical elements of the regulatory reform agenda since then.

Deepening the Bank’s efforts to modernize and improve access to domestic financial services—particularly among Family Island residents—“Project Sand Dollar” was launched in 2018 to develop and introduce a digital version of the Bahamian dollar. This initiative should allow both residents and visitors to seamlessly access digital payment services, promote interoperability across private providers of payment services, and enable more access to traditional banking services.

The Bank’s continued progress towards its strategic goals is being achieved through our talented, dedicated and industrious staff; we also benefit from an incredibly engaged Board of Directors. I therefore extend sincere appreciation to the Bank’s staff and the Directors. Together, we all look forward to sustaining these endeavours.



John A. Rolle
Governor



DIRECTORS AND SENIOR OFFICIALS

AT DECEMBER 31, 2018



DIRECTORS

Pictured from left: Mr. Derek Rolle, Deputy Governor; Mr. Robert Adams; Mr. John A. Rolle, Chairman; Mr. Thomas Dean; Mr. L. Edgar Moxey.



SENIOR OFFICIALS

Pictured standing from left: Mr. Errol L. Bodie, Manager, Information Technology; Mr. Alwyn Jordan, Manager, Research; Ms. Deborah Ferguson, Manager, Human Resources; Ms. Karen Rolle, Deputy Inspector, Banking Supervision; Mrs. Cleopatra Davis, Manager, Banking; Mr. Charles Littrell, Inspector, Banking Supervision; Mrs. Tamieka V. Watson, Manager, Exchange Control; Mr. Ricardo Barry, Chief Security Officer; Mr. Ian B. Fernander, Manager, Administration. Seated from left: Mr. Keith T. Jones, Manager, Finance; Mrs. Nakeisha Burrows, Manager, Internal Audit; Mr. John A. Rolle, Governor; Mr. Derek Rolle, Deputy Governor; Mrs. Rochelle A. Deleveaux-McKinney, Legal Counsel & Board Secretary.



2018 AT A GLANCE

- ◆ The domestic economy sustained its growth trajectory in 2018, expanding by an estimated 2.3%¹, following a gain of 1.4% in the prior year. This outcome was supported by improvements in tourism sector output, and ongoing stimulus from foreign investment-led construction activity.
- ◆ Average consumer prices firmed modestly during the year, reflecting the pass-through effects of the 4.5 percentage point rise in the VAT rate on 1st July to 12.0%.
- ◆ Employment gains were sustained in 2018, as hotels and other smaller-scaled businesses continued to on-board staff; although the unemployment rate rose to 10.7% from 10.1%, as the growth in the active labour force outpaced job gains.
- ◆ The fiscal deficit to GDP ratio narrowed to an estimated 3.3% in FY2017/2018, from 5.6% in the prior period, underpinned by a capital spending-led reduction in aggregate expenditure, which outstripped the decrease in total revenue.
- ◆ At end-December, the Government's Direct Charge to GDP ratio edged-down to an estimated 58.9%, from 59.0% in 2017. In addition, the National Debt to GDP ratio stood at an estimated 64.6% at end-December, a decrease of 0.2 percentage points over the twelve-month period.
- ◆ External reserves contracted by \$221.1 million to \$1,196.3 million at end-December 2018, with the import cover ratio narrowing to an estimated 17.5 weeks, compared to 21.9 weeks in 2017.
- ◆ The Central Bank sustained its efforts to gradually liberalize exchange controls, by unveiling a series of measures in February 2018, which targeted both current and capital account transactions.
- ◆ In February, the Credit Reporting Act was passed in Parliament and the selection process for the credit bureau restarted. The associated regulations were finalized for gazetting in January 2019.
- ◆ The Bank unveiled its revised proposals with respect to the Basel II and III supervisory framework for its licensees, which focused on applying a more proportioned approach, based on the size and complexity of banks operating within and from within this jurisdiction.
- ◆ In June 2018, the Bank issued binding guidance on a simplified approach to customer due diligence (CDD) for Bahamian domestic accounts, in an effort to encourage more financial inclusion for low risk customers. Exchange control restrictions on non-residents' access to Bahamian dollar deposit accounts, were also relaxed in August 2018.

¹ IMF's April 2018 Forecast.



STRATEGIC FOCUS FOR 2019

Improve the Monetary Policy Framework

- Strengthen the macro-economic surveillance framework with quarterly forecasts.
- Enhance the financial stability analysis, with forward looking assessments of risks and vulnerabilities, and improved surveillance of non-bank financial activities.
- Improve data quality and coverage, through strengthened forecasting and estimation methodologies; expanded surveys of real sector activities and increased use of secondary data, including public finance.
- Transition to the IMF's Balance of Payments Methodology (BPM 6) compilation format for international trade and financial data; and produce data on The Bahamas' International Investment Position (IIP).
- Pursue further gradual liberalisation of the Exchange Control regime, while maintaining foreign exchange market and exchange rate stability.

Strengthen Supervisory and Regulatory Systems

- Continue to implement the Basel III framework for SFIs, using proportionality principles that achieve a more efficient, simplified, yet internationally compliant outcome for The Bahamas.
- Further strengthen AML/CFT supervision, through sustained capacity building; and broad engagement and collaboration with industry stakeholders, policy makers, regulators and standards setting bodies.
- Strengthen and expand supervisory oversight of credit unions, retail payment service providers and other non-bank SFIs.
- Promote passage of legislation to strengthen the crisis management system and bank resolution framework.

Promote Payment Systems and Financial Markets Infrastructure Development

- Support sustained public debt market and debt management reform by, *inter alia*, completing the establishment of the Centralised Securities Depository (CSD) for Government debt, and promoting the passage of modernized legislation for public debt management.
- Deepen payment systems modernisation, through the piloted introduction of a digital version of the Bahamian dollar, and promote direct participation of systemic non-bank financial institutions, and high-volume public sector retail payments originators in the Automated Clearing House (ACH) and Real Time Gross Settlement System (RTGS).

Strengthen External Relations, Public Education and Financial Inclusion Efforts

- Complete the redevelopment of the Bank's website, to improve the ease of navigation and provide the public with more comprehensive information.
- Leverage the membership in the global Alliance for Financial Inclusion (AFI), to achieve improved financial inclusion outcomes across SFIs and propose a national financial inclusion strategy for the Government's consideration.
- Execute the next round of financial literacy outreach.
- Conclude the licensing process for the credit bureau and promote increased public awareness about the bureau.

Enhance Operational Efficiency and Corporate Governance

- Promote passage of the Central Bank of The Bahamas Bill, 2019, with provision for increased transparency, operational independence and restrained provisions on lending to the Government.
- Strengthen the Central Bank's enterprise risk management systems, including for business continuity, cyber & information security and strategic planning & execution.
- Advance the Bank's IT modernisation project, initiating procurement of new financial management and human resources solutions.
- Continue work to secure the necessary real estate, to begin construction of a new Central Bank Headquarters and a new Currency Operations Centre.





OUR OPERATIONS

GOVERNANCE & ACCOUNTABILITY

The Bank's corporate governance framework, as outlined in the Central Bank of The Bahamas Act, 2000 (the Act), prescribes, *inter alia*, the roles and responsibilities of the Board of Directors, the Governor and the Deputy Governor.

BOARD OF DIRECTORS

The Board of Directors has overall responsibility for policy and oversight of the Bank's management and operations, including strategic planning, financial and accounting practices and procedures, risk management and succession planning.

Appointed by the Governor General, on the advice of the Minister of Finance, the Board is comprised of the Governor (Chair) and up to four independent directors. During 2018, Mr. L. Edgar Moxey, Mr. Robert Adams and Mr. Thomas Dean, were all re-appointed to serve as Directors from 1st July 2018 to 30th June 2019.

As required under the Act, each Director must sign a declaration of secrecy in relation to the affairs of the Bank, and is indemnified by the Bank against personal, civil or criminal liability, in respect of their actions done in good faith while carrying out their statutory duties.

There is statutory provision for the appointment of two Deputy Governors, who may attend Board meetings, but are only eligible to vote in cases where—in the absence of the Governor—one chairs the Board Meeting. Currently, only one Deputy Governor has been appointed and three Directors form a quorum.

The Board met on twelve occasions in 2018. The Board's agenda included discussions on domestic and international economic and financial conditions, their implications for the external reserves, the Bank's Strategic Plan for 2016-2020; de-risking and measures to enhance the Bank's supervisory oversight of the country's anti-money laundering and countering the financing of terrorism frameworks; and the status of proposed legislative amendments impacting the Bank's operations. Deliberations were facilitated by various management briefs and reports.

ACCOUNTABILITY & TRANSPARENCY

The Bank is mandated, by statute and best business practices, to ensure a high degree of transparency, which facilitates accountability. In compliance with these

responsibilities, the Bank furnished the Minister of Finance with a report of its activities for 2018, which was subsequently laid before Parliament. Monthly balance sheet information was also provided to the Minister and published in the Gazette.

During the year, the Governor maintained scheduled monthly meetings with the Minister of Finance and provided the Minister with special periodic communications, both written and verbal, on industry related matters, as they emerged. These meetings help to facilitate and maintain coordination between monetary and fiscal policy, and provide an opportunity to keep the Government informed of the Bank's performance in meeting its statutory obligations.

Information on domestic economic and financial developments was published in the Bank's Monthly Economic and Financial Development (MEFD) reports, Quarterly Economic Reviews (QER) and Quarterly Statistical Digests (QSD). These publications, along with other announcements, notices and press releases, were made available to the public via the Bank's website².

In other activities aimed at promoting accountability and transparency, the Governor and senior officers of the Bank gave official speeches on various topics, including domestic economic conditions and prospects, developments in the regulatory and supervisory space, exchange control liberalization measures, and updates on strategic projects.

RISK MANAGEMENT

Risk management is an integral part of the management function, involving the identification, evaluation and prioritization of risks, in order to promote the making of sound business decisions. The Bank's approach to risk management is based on sound central banking principles and a robust governance structure.

Internal Audit

As a part of the Bank's risk management structure, the Internal Audit Unit (IA), supports both the Audit Committee of the Board of Directors and Management, in evaluating the adequacy and effectiveness of the Bank's system of internal controls, risk management and governance processes. The operations of IA are steered by a Board-approved Internal Audit Charter and a risk-driven

² www.centralbankbahamas.com



Annual Audit Plan. To maintain independence, the Head of IA reports functionally to the Audit Committee and administratively to the Governor.

As part of its 2018 work programme, IA completed a review of its own governance processes. This exercise was implemented to enhance both the relevance and value-added contribution to the Bank. The Unit also completed and issued internal audit and special project reports, which focused on strengthening several of the Bank’s critical processes.

The Unit also examined the Bank’s financial operations, maintenance & contract management procedures, information technology and information security programmes, in addition to other key operational functions. The core aim of these reviews is to enhance existing internal controls and strengthen operational efficiency. The effectiveness with which departments discharge their core duties was also evaluated, including, but not limited to, the risk-based supervision process and examinations, human resources, facilities surveillance and physical access. In addition, the IA Unit supported various working committees of the Bank during the review period, which were geared towards encouraging and sustaining a stronger internal control and compliance environment.

Information Security

The Bank has a maturing information security programme, spearheaded by the Information Security Unit (ISU). An Information Security Steering Committee, comprising heads of departments, provides strategic oversight to the programme. In 2018, the ISU continued to strengthen the information security programme, in line with best international standards, and to monitor the IT and physical work environment to identify risks and vulnerabilities that require active remediation. Automated tools were deployed to scan and monitor the IT environment, enabling continuous real time security alerts and increasing compliance to quickly detect and identify security threats.

The Bank’s information security awareness programme, which promotes responsible, safe and accountable behaviour of staff, intensified during the year. The staff now undergo training, particularly to reduce institutional vulnerability to physical and cyber information threats. The Bank’s fifth annual Information Security Awareness Month and Fair, which was held in June 2018, featured both local and international exhibitors, exposing both staff and public invitees to these issues. Moreover, the Bank launched its e-learning platform, thereby enrolling all staff in a continuous, mandatory cyber and information security training regime.

BANKING OPERATIONS

Currency Operations

The Bank’s currency operations include both a circulation and an active numismatic component, with the circulation programme maintaining an aggressive anti-counterfeiting element.

Circulated notes and coins are regularly updated for security and aesthetic reasons. In particular, the Bank issued the new Counter Resistant Integrated Security Product or CRISP Evolution (CE) \$20 banknote on 27th September, 2018, marking the third release in the new banknote family. The Bank also launched a redesigned 15¢ coin, which completed the redesign of the family of circulation coins.

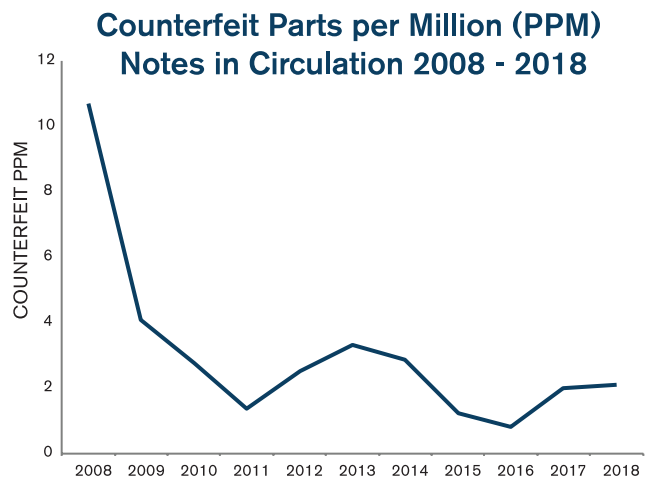
The Bank will continue its release of banknote denominations with the CE \$1/2, CE \$3 and CE \$50 banknotes in 2019 (See: Table 1). The new CE \$5 and CE \$100 banknotes are scheduled for release in 2020 and 2021, respectively. These notes will contain both aesthetic and security enhancements, pioneering the pairing of the Durasafe® substrate and RAPID® on the CE \$50 bill and Durasafe and MOTION SURFACE™ security stripe on the CE \$100 bill.

Table 1: Bank Note Security Tiers

DENOMINATION	PUBLIC CONSUMPTION
\$1/2, \$3	Novelty
\$1, \$5	Low Value
\$10, \$20	Transactional
\$50, \$100	Value Storage

Source: Central Bank of The Bahamas

In addition to regularly scheduled anti-counterfeit detection workshops in New Providence and Grand Bahama, the Bank facilitated targeted training sessions for large merchants and retailers in New Providence. These seminars supplement online tools to provide public guidance

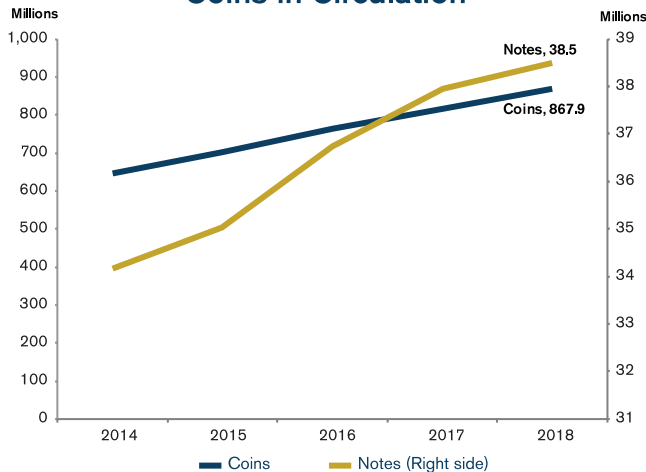


on how to authenticate genuine banknote features, with the latest being the launch of a mobile banknote app in September 2018. The Bank intends to expand its outreach to other islands in the coming year, and to upgrade the mobile app. The Bank has already engaged with representatives from The Bahamas Alliance for the Blind and Visually Impaired, to participate in validating suitable visually-impaired recognition features on the currency.

Given the number of built-in security features, detected incidences of counterfeiting of the Bahamian currency remained low, at less than 1.0 parts per million (ppm) of banknotes in 2018.

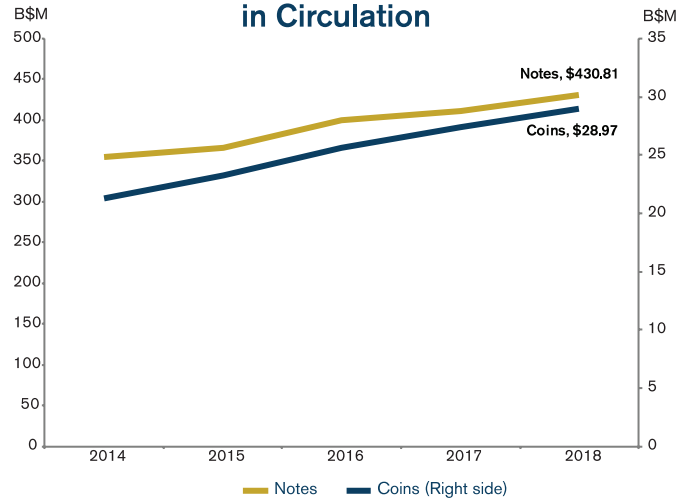
The Bank continued to see an increase in the demand for Bahamian banknotes and coins. However, the volume of \$1 bills issued declined by 45%, in line with the improved durability of the 2017 CRISP Evolution issue, the increasing dispensing of higher face value notes through ATM machines and lessening over-the-counter withdrawals at commercial banks. Similarly, the demand for circulation coins rose—more specifically the 1¢—a trend that is expected to continue until stocks of this denomination are depleted in early 2020. The graphs show the movements in the volume and value of Bahamas notes and coins over the past five years.

Quantity of Notes and Coins in Circulation



In the numismatic programme, the Bank completed its Islands of The Bahamas \$10 Silver Proof Coin series, with the release of its Inagua coin in May 2018, followed by a five-coin collectors set in July 2018, which included the 2014 Aerial View, 2015 Exuma, 2016 Nassau, 2017 Bimini, and 2018 Inagua coins. Each of the coins was minted in fine silver, with the obverse showcasing the Coat of Arms of The Bahamas and the reverse, the cultural image most synonymous with that Island. The coins each have a limited mintage of 500 pieces, with the exception of the Nassau coin, of 1,000 pieces; and the five-coin set, limited to 75.

Value of Notes and Coins in Circulation



On 3rd December 2018, the Bank released its first gold coin in over a decade, the limited edition 1.1 ounce \$250 Gold Proof Atlantic Blue Marlin Coin, which was produced by the Royal Mint. The coin, on its reverse side, has a modern image of the blue marlin fish, and on its obverse, the Coat of Arms of The Bahamas.

Public Debt Administration (Domestic)

The Bank continued in its role as Registrar and Transfer Agent for Government and public corporations' securities; although private financial institutions still manage several issues. The Bank also sustained its efforts to modernize the public debt management infrastructure, by assisting with the preparation of the legal reform proposals and ongoing development of the market framework.

During the year, the securities outstanding for the Clifton Heritage Authority and The Bridge Authority remained at \$24.0 million and \$29.0 million, respectively. In addition, following a maturity of \$5.0 million, outstanding instruments of the Education Loan Authority declined to \$62.0 million. Outstanding bonds of the Bahamas Development Bank and the Bahamas Mortgage Corporation closed the year lower at \$41.0 million and \$160.0 million, following maturities of \$2.0 million and \$5.0 million, respectively.

In June 2018, the Bank introduced a Bahamas Registered Stock (BRS) Initial Public Offering Calendar. This initiative formed part of an overarching framework to improve the public debt management infrastructure and to better inform the investing community about opportunities to purchase BRS. As at end-December 2018, the value of BRS outstanding stood at \$3.3 billion, an increase of \$89.0 million over the prior year. The Bank facilitated nine Initial Public Offerings (IPOs), which totalled \$499.0 million, with maturities of \$410.0 million. Over the year, the Bank also facilitated one secondary market offering totalling \$9.0 million.



Box 1: MONETARY POLICY IN 2018

The Bank's Monetary Policy Committee (MPC), which meets on a monthly basis, is chaired by the Governor and encompasses several Heads of Departments and other technicians. The overall objective of the MPC is to advise and assist the Governor in formulating policy measures to promote monetary and financial stability. The monthly surveillance analysis of the MPC is summarized in a report, which is disseminated to the public within five days of each meeting. In recent years, the MPC's analysis has been extended to include a quarterly presentation, which typically provides a more in-depth review of economic developments over the year.

During 2018, the MPC's monthly deliberations focused on analyzing key developments that occurred throughout the international and domestic environment. Discussions were conducted against the backdrop of several important domestic economic and financial themes, several of which have persisted over an extended period. Specifically:

- The ongoing modest pace of domestic economic growth, reflecting the gains in the tourism sector, as Baha Mar completed the opening of all of its properties during the year.
- The improvement in the labour market, following the on-boarding of new staff by Baha Mar and other smaller-scale businesses.
- The high level of bank liquidity, in an environment of persistent weakness in credit demand.
- The further improvement in banks'

credit quality indicators, mainly reflecting loan restructuring activities, enhanced debt collection efforts and the modest growth in the domestic economy.

- Financial inclusion, as it pertains to the streamlining requirements for the opening of bank accounts to ensure that certain vulnerable groups have access to regulated payment and other financial services in the country.

In evaluating the external risks to the domestic economy, the MPC noted several important trends. On the positive side, the sustained growth in the United States' economy favoured continued gains in domestic tourism output, as well as foreign investment activity. However, several headwinds remained, including the prolonged trade war between the United States and its major trading partners, the potential adverse economic effects from the Federal Reserve raising interest rates and the uncertainties surrounding "BREXIT". The MPC also assessed pressures on external reserves from higher global oil prices, amid supply cuts from several major producers.

In the context of the Bank's mission to maintain adequate levels of external reserves to support the fixed exchange rate regime, the Committee sustained its close monitoring of two key external reserve adequacy indicators; namely, the ratio of external reserves to base money and the import reserve cover. In the absence of significant one-off transactions, reserve trends featured the traditional build-up in external balances in early 2018, during the winter tourist period, followed by a

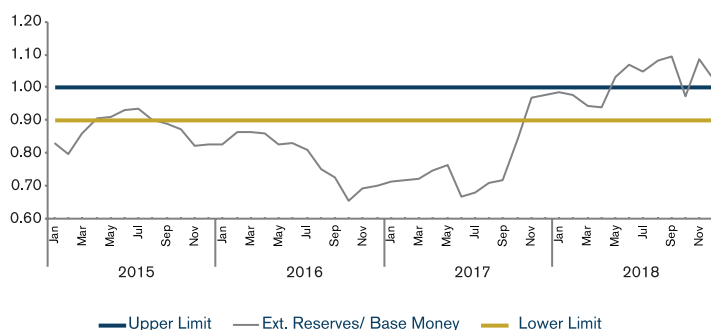
drawdown in balances in the latter six months, as foreign currency demand to facilitate import and other current payments expanded. As a consequence, the ratio of reserves to base money trended upwards from January, to exceed the higher end of its 90% - 100% benchmark range, at 103% by May 2018. The indicator remained above the range over the ensuing months, peaking at 109.5% in September. The indicator then fell in the latter half of the year, to a low of 102.6% at end-December, 2018.

Similar trends were noted with regard to the more broadly tracked indicator, external reserve coverage in weeks of annual current year's merchandise imports. Specifically, the ratio rose from 21.9 weeks at the end of 2017, to a peak of 24.8 weeks in the first quarter of 2018, before declining to 23.2 weeks in the following three-month period. The ratio continued to trend downwards in the latter half of the year, falling to 19.1 weeks at end-September and then to 17.5 weeks by year-end—although remaining well above the international benchmark of 12.0 weeks.

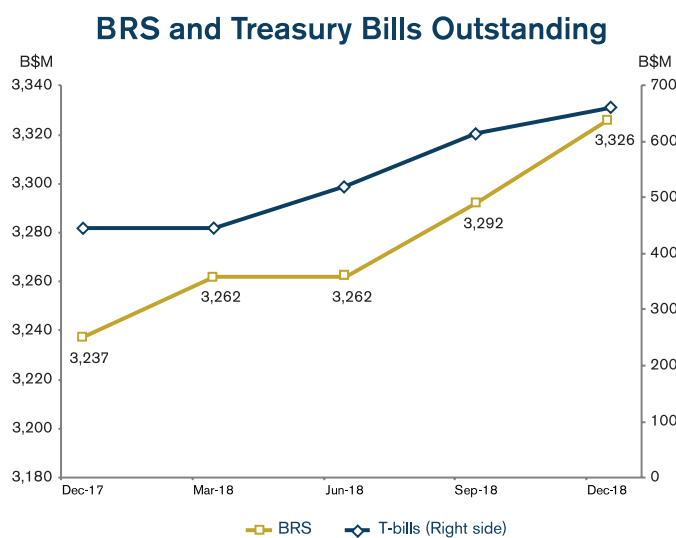
The MPC also sustained its monitoring of banking sector soundness and stability indicators. Specifically, the Committee acknowledged the elevated levels of liquidity in the banking system—mainly reflecting banks' conservative lending stance and consumers' efforts to deleverage—with the Central Bank's focus on absorbing some of the excess cash balances through sales of its holdings of Government debt. However, financial stability concerns were muted, given that banks' average capital levels remained robust—well in excess of the required target and trigger ratios of 17.0% and 14.0%, respectively. Moreover, banks sustained their efforts to improve their balance sheets by reducing their non-performing loans (NPLs), through the sale of delinquent mortgages to non-bank entities, combined with ongoing loan restructuring activities.

Given the robust levels of external reserves, modest economic growth, and weak consumer credit demand, the MPC decided to maintain its neutral policy stance throughout 2018. ◆

Ratio of External Reserves to Base Money



With regard to shorter-term instruments, the value of outstanding Treasury bills (T-bills) increased by \$215.0 million, to close the year at \$660.0 million. T-bill taps raised \$251.0 million in new financing, with retirements amounting to \$36.0 million. During the year, the investment community shifted more towards the longer-dated 182-day T-bills, versus the 91-day T-bills, resulting in changes in the average tender rates. The average tender rate for 91-day T-bills closed the year at 1.5368%, and 182-day at 1.8364%, compared the respective 1.7904% and 2.0188% in 2017. The chart illustrates the year-over-year movement in outstanding T-bills and BRS.



During the year, the Bank provided assistance to the Government in drafting the Public Debt Management Act (PDMA). It is anticipated that the PDMA will be completed and tabled in Parliament in 2019. This work, which engaged a broad spectrum of stakeholders, is expected to lead to the revamping of the public debt management infrastructure, providing more structure and accountability, that aligns with international best practices. The framework would also promote efficiencies related to dematerialization, optimized debt management strategies and strengthened oversight of public enterprises' debt operations.

DIGITAL CURRENCY INITIATIVE

The Bank intensified its financial inclusion and payment systems modernisation plans in 2018, targeting a piloted introduction of a digital version of the Bahamian dollar by 2020. This innovation would also promote the interoperability of seamless connectivity between private providers of electronic payments solutions. In order to affect this change, the Bank established an E-solutions Unit in the Banking Department, to focus on developing this payment platform.

This initiative has been branded as “Project Sand Dollar.” Emphasis is on providing a technology solution that

meets the needs of an archipelagic geography, with more enabled access to banking services and inclusivity across population segments, including undocumented persons. The Bank is closely engaged with the Government, to promote the development of a national digital identity infrastructure, which is an essential complement to a mobile retail payments infrastructure, and also allows for expanded access to domestic financial services, that would comply with stringent international AML/CFT standards.

Payments and Business Innovations

The Bank implemented several initiatives aimed at improving its payment systems and network resilience. The Bank partnered with SWIFT³, under a SWIFT Alliance Managed Operations initiative, to improve the system's responsiveness and reduce network downtime. The SWIFT network was also upgraded to the latest software release, thereby providing enhanced protection for critical infrastructure, and an attestation to the Bank's compliance with all of the 2018 mandatory security controls. These attestations provide assurances and comfort for all counterparties, with whom the Bank transacts inside the SWIFT network.

In November 2018, the Bank launched the Bahamas Government Securities Depository (BGSD). The BGSD platform, was developed through a collaborative effort, which included the Bahamas International Securities Exchange (BISX), domestic broker dealers, the Government, the service provider MontranTM and other stakeholders. This project underscores the Bank's sustained role in supporting the development of The Bahamas' financial market infrastructure, benefiting from technical assistance from the Commonwealth Secretariat. It seeks to promote greater efficiency, transparency and accessibility in the Government securities' market; and to achieve a seamless and open market for the purchase and sale of Government securities. A second and more user-friendly version of the platform, is expected to be launched in the second quarter of 2019, providing direct access to key capital market firms and commercial banks.

PAYMENT & SETTLEMENT SYSTEMS

Oversight

The Bank, through its Payments Unit, sustained its efforts to strengthen the oversight of the domestic payment and settlement systems, while ensuring the efficiency, reliability and security of the infrastructure. Quarterly meetings were held with members of the Bahamas Automated Clearing House (BACH) and the ACH, which processes small-value transactions of less than \$150,000. These meetings considered collateral and settlement issues of the commercial banks, internal audits and any other

3 The Society for Worldwide Interbank Financial Telecommunications.



significant developments that emerged. Similar meetings were held with key stakeholders of the Central Bank-owned Bahamas Inter-Bank Settlement System (BISS), the RTGS, which facilitates real time settlement of large value payments greater than \$150,000. Deriving from such discussions was feedback on operational efficiency, as well as the ongoing development of the BISS.

Following the release of the Payment Instruments (Oversight) Regulations, 2017, and corresponding General Information and Application Guidelines for Providers of Electronic Retail Payments Instruments and Electronic Money Products, the Bank issued one license for the provision of electronic payment services. Some of the goals of the Bank in the payments arena, are to reduce the dependency on the use of cash in the domestic economy, accelerate financial inclusion initiatives and promote the more efficient provision of services by non-deposit taking institutions.

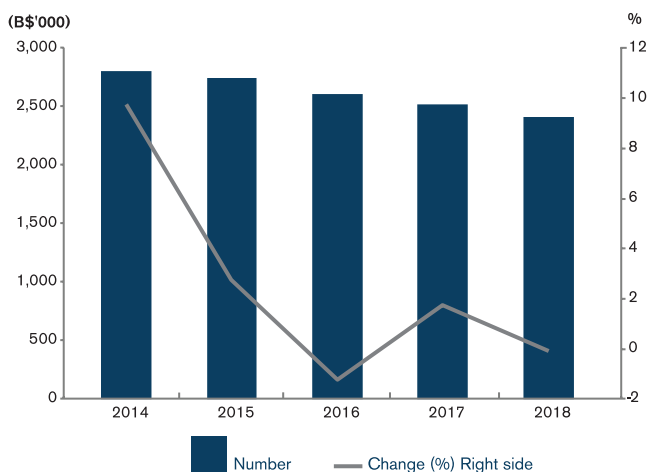
Market Developments

Despite some recent annual fluctuations, data continued to reveal increasing volumes of domestic electronic payment transactions in The Bahamas. This reflects the supporting role of the ACH and RTGS in settlements, and efforts by commercial banks to promote greater use of online banking and ATMs in place of in-branch services.

Real Time Gross Settlement (RTGS)

The seven participating clearing banks processed, in addition to direct interbank transactions, X9 (cheques) and NACHA (direct credits) payments, over the BISS-RTGS, in seven daily settlement windows, between 8:15 a.m. and 4:45 p.m. These also, in many instances, summarize net clearance of ACH payments. Over the review year, the volume of these transactions increased significantly by 24.9% to 115,068. The corresponding value of the transactions rose by 2.5% to \$30.0 billion.

Cheques Cleared



Cheques

As rapid technological developments and increasing use of electronic payment methods continue to drive the payments industry, the use of cheques remains on a downward trend—with the exception of large value transactions. The number of processed instruments declined by 4.2% to 2.4 million, after a 3.5% contraction in 2017. Similarly, the related value of these payments fell slightly by 0.1% to \$7.1 billion, in contrast to a 1.8% expansion to \$7.2 billion in the previous year.

NACHA Payments

Payments processed by the BACH, in accordance with the globally accepted National Automated Clearing House Association (NACHA) format, trended upwards over the review year. The volume of these transactions expanded by 12.6% to 2.9 million, with a corresponding growth in the value, by 22.2% to \$3.4 billion.

Retail Payments Services

In keeping with global trends, the use of technology remains a driving force of developments in the payments landscape in The Bahamas. As a result, an increase in the volume of electronic payments was observed in 2018, notwithstanding the fact that cash still remains a significant medium for transactions.

Automated Teller Machines (ATMs)

ATMs are installed throughout the country, with various locations extending from inside commercial bank branches, to areas of high customer transit, such as supermarkets and gas stations. A number of machines—specifically those placed in high tourist traffic areas—are configured to dispense both Bahamian and US currency. During the year, the number of ATMs in operation increased by 5.5% to 382, following a 10.0% decline to 362 in 2017, as commercial banks shifted many of their basic products to online facilities. Correspondingly, the volume of transactions rose by 13.2% to 11.5 million, from 10.2 million transactions a year ago. In contrast, the value of these transactions decreased by 7.8% to \$1.9 billion, from \$2.1 billion last year.

Debit cards

Debit cards with international brands, such as Visa and MasterCard, which allow both domestic and foreign currency transactions, have replaced “non-branded” products. The number of such card transactions grew by 23.3% to 14.0 million in 2018, with the associated value firming at a moderated pace of 2.6% to \$1.7 billion.

Credit cards

These cards are issued by the local commercial banks and are also generally internationally branded, by either Visa or MasterCard. Most personal cards carry limits which range from \$500-\$5,000, \$5,000-\$10,000 and



over \$10,000; however, select high net worth individuals can negotiate even greater limits. In 2018, the number of cards in circulation rose further by 10.2% to 286,340, extending the 15.3% gain recorded in the previous year. However, with growing debit card use, the related value of unpaid balances contracted by 2.3% to \$249.1 million. The growth in new accounts was concentrated in cards with limits of under 5,000, which increased by 12.0%, even though outstanding balances fell by 5.2% to \$102.1 million. For cards with credit limits of \$5,000-\$10,000, the number of these accounts decreased, by 2.7% to 21,597, and the associated unpaid balances, by 4.1% to \$66.5 million. In contrast, the number of cards with limits of over \$10,000, rose by 1.4% to 13,544 and with growth in unpaid accounts by 3.4% to \$80.5 million.

Internet Banking

Commercial banks provide an increasing range of Internet banking services to customers, with some banks levying a fee for this convenience. The Central Bank's 2018 payments survey, revealed that the number of total users—inclusive of residential, business, public sector and other users—increased by 15.9% to 105,273 accounts, compared to 90,838 accounts at end-2017.

Instances of Payment Fraud

The Central Bank began compiling data on the number of fraud cases in 2017, as part of a heightened focus on consumer protection. A preliminary analysis of the Bank's 2018 payments survey, showed that there were 3,507 reported cases of fraud processed by commercial banks for cheques, debit and credit cards, valued at \$7.8 million. Disaggregated by type, cases involving debit cards accounted for 59.5% of the total at 2,086, with an associated value of \$3.2 million; this reflects in part exposure to a major "card skimming" scheme that affected one domestic entity in August. Cheque fraud represented 14.6% of the aggregate number of cases at 514, for a corresponding value of \$2.5 million (32.5% of the total value). Further, the number of cases involving credit cards stood at 907, which constituted 25.9% of the total and an associated value of \$2.0 million. The survey revealed that expectedly, over 75% of fraud cases were reported in New Providence, given that the majority of the banks' customer accounts reside in the capital.

FOREIGN RESERVES MANAGEMENT

During the year, external reserve balances fell by approximately 15.6% to \$1.2 billion, when compared to 2017. In particular, there was a net reversal of public sector debt financing towards domestic sources, following both refinancing and net new borrowings in foreign currency in 2017. The public sector was therefore a significant net user of foreign exchange, leading the drawdown in reserves, in spite of expanded net inflows through the private sector.

The Bank continued to actively manage the reserve balances through a structured strategy that involved low risk investments in term and overnight deposits at correspondent banks. This approach helps to avail the Bank of liquidity and provide a modest income. In early 2018, the Board approved revised Investment Policy Guidelines (IPG) for the reserves, to renew the authorised outsourcing of some investment services to professional managers. Under this framework, the Bank on-boarded Allianz Global Investors as an external asset manager in October 2018. It is expected that in addition to enhanced yields, the Bank will benefit from significant knowledge transfer. Still, having regard to containing the risk exposures of the foreign reserves, the amended policy also widens the range of investment grade instruments that can be held by the Bank, in keeping with evolving international benchmarks of acceptable foreign reserve assets.

The Bank's Investment Committee (IC), remains responsible for implementing the investment mandates of the Bank, and supervising the external asset managers, with the Board charged with the periodic review of performance against the IPG. In early 2018, the committee added two new members, in order to draw on a wider array of knowledge and expertise from within the Bank. The IC meets weekly to review investment proposals, both domestic and foreign, with a view to analyzing and approving the requests in accordance with global market conditions.

During the year, the Bank maintained its statutory compliance with its Key Performance Indicators (KPIs). Specific to the reserves, these include the requirement that the ratio of foreign reserves to demand liabilities is a minimum of 50 percent; and that held foreign securities with maturities of five or more years, never exceed 20% of the reserves portfolio. The remaining KPIs impose restrictions on exposures to medium and longer-term debt of The Bahamas Government.

DORMANT ACCOUNT ADMINISTRATION

The Bank administered dormant accounts, in accordance with provisions in the Banks and Trust Companies Regulation Act, 2010. These are balances with banks on which no customer activity has occurred for at least seven years. They are required to be transferred from the institutions to the Central Bank for safe keeping, until the account holders are presented to claim the funds. As at 31st December 2018, the Bank maintained custody of 41,459 dormant facilities, with balances totalling \$108.8 million, denominated in eight currencies (See: Table 2). Balances in United States dollars and Bahamian dollars, together accounted for a dominant 89.1% of the total, while the Australian dollar, Canadian dollar, Swiss franc, Euro, British pound and Hong Kong dollar, accounted for the remaining 10.9%.



Table 2: Dormant Account Balances

Currency	Account Balances 2018 (\$'000)	No. of Accounts 2018	% of Total Balances (2018)
Australian \$	70.5	2	0.1
Bahamian \$	36,176.1	33,732	33.3
Canadian \$	5,821.6	424	5.4
Swiss Franc	1,602.3	16	1.5
Euro	2,649.6	36	2.4
UK (Sterling)	693.5	111	0.6
Hong Kong \$	1,046.4	1	1.0
US\$	60,694.8	7,137	55.8
TOTALS	108,771.5	41,459	100

Source: Central Bank of The Bahamas

During the year, the Bank continued to promote proposed reforms to the dormant account framework, which culminated in the Banks and Trust Companies Regulations (Amendment) Act (BTCRA), 2018, being passed in Parliament in December 2018, and brought into force in February 2019. The Amendment introduced additional assets to be defined as dormant, including custody accounts, contents of safety deposit boxes, money orders and credit card balances. An equally important reform allows the Government to receive ownership of specific categories of dormant funds transferred to the Central Bank and held for ten years. Low-value accounts of \$500 or less would immediately cede to the Government, on transfer to the Central Bank. In accordance with the Act, as at end-December 2018, an estimated \$40.95 million in dormant funds was due to be remitted to the Government against the applicable 10-year custodial period expiration.

In 2019, the Bank will introduce additional governance oversight structures for dormant account administration. This will include increased public disclosures regarding assets in custody, and public awareness campaigns around funds recovery and ways to minimise lapses into account inactivity status. The Bank has also committed to developing an automated enquiry tool to help the public to search for suspected dormant assets.

EXCHANGE CONTROL ARRANGEMENTS

During 2018, the Exchange Control Department (ECD) supported the Bank's statutory mandate, to monitor the demand for foreign exchange, while attending to the public's approval needs and ensuring the prudent management of external reserves.

The Bank, in its role as Controller of the Exchange, persisted with its efforts towards the further gradual liberalization of exchange controls over the review period. In this regard, the measures implemented during

the year included: granting Authorized Dealers and Money Transmission Businesses (MTBs) increased delegated authority for current payments, expanding the amount of funds that residents can acquire at the official rate for investment in property abroad and upwardly adjusting the amount that Temporary Residents can borrow in Bahamian dollars for owner-occupied residences. Recent liberalisation measures are summarised in Box 2.

Residents continued to make outward capital investments through the Investment Currency Market (ICM), at the reduced premium bid and offer rates, of 5.0% and 2.5%, respectively. In 2018, sales activity amounted to \$42.3 million, four times the \$10.9 million recorded in 2017, while redemptions totalled \$8.0 million, compared to nil in the prior year.

The Bahamas Depository Receipt (BDR) programme, which facilitates residents' investments in foreign securities, experienced modest participation during the year, as the number of licensed broker dealers increased by one, for a total of seven; however, only four entities participated in the programme. Of the \$35.0 million allocated for the facility in 2018, some \$13.7 million was drawn, compared to \$16.4 million in the prior year.

In terms of foreign exchange requests, in excess of \$3.4 billion was approved in 2018, of which annual current account payments accounted for the majority, at \$2.3 billion, while capital approvals totalled \$1.1 billion. Approvals for oil payments continued to dominate current account transactions, at \$709.2 million, followed by factor income payments (\$570.6 million), other services (\$494.0 million), non-merchandise insurance (\$196.9 million), travel (\$157.1 million), non-oil imports (\$127.7 million), and transfer payments (\$55.1 million). Capital approvals were dominated by loan repayments, which totalled \$906.2 million, while other capital and share purchases accounted for significantly smaller shares of \$125.6 million and \$22.6 million, respectively.

Authorized dealers and authorized agents, along with MTBs, remained important intermediaries in the administration of exchange controls. At end-2018, the number of authorized dealers (commercial banks) and agents (resident trust companies) remained at eight each. The Central Bank also continued to provide the requisite training and advice to authorized dealers, authorized agents and MTBs, to ensure that their reporting submissions were compliant with the delegated framework and to maintain the integrity of the reporting system, which is necessary for the proper analysis of the balance of payments accounts.



Box 2: CAPITAL ACCOUNT LIBERALISATION MEASURES

During the year, the Central Bank continued with its gradual relaxation of the exchange control regime, while preserving the economy's capacity to maintain adequate supplies of foreign exchange for trade-related payments, and ensuring safeguards around the stability of the Bahamian dollar exchange rate.

Effective 1st February 2018, the following measures were implemented:

- Residents who previously had funds held in foreign currency denominated deposits and/or investment assets outside of The Bahamas, were required to apply to the Central Bank to either obtain approval to maintain these accounts or to repatriate either the assets or their proceeds to The Bahamas, with no penalties imposed on these regularized accounts. The owners of the deposit facilities would then be allowed to use the resources to finance domestic transactions, without restriction.
- Without prior reference to the Central Bank, Bahamian-owned businesses were granted approval to maintain operating deposit accounts in foreign currency of up to \$100,000 at

domestic commercial banks. These accounts are required to be funded exclusively from revenues earned in foreign currency and are to be used strictly for making payments abroad. Central Bank approval will continue to be required for accounts, which retain more than \$100,000 in foreign currency revenues.

- The buying and selling rates for the ICM were reduced from 12.5% and 10.0%, to 5.0% and 2.5%, respectively. In December, the Bank concluded the second part of this reform, announcing the framework to allow direct sale and redemption of investment currency through authorized dealers (commercial banks). The arrangements took effect on 1st January, 2019, allowing for the transfer of a portion of the premium on sales to commercial banks, while retaining with the Central Bank, the full liability for premium on ICM redemptions (capital repatriated to The Bahamas).
- The Central bank granted greater autonomy to authorized dealers to vet account signatories and discontinued its annual approval process for individual

signatories on foreign currency accounts and annual renewals to maintain such facilities.

- The Authorized Agent delegation has been amended to allow Authorized Agents to offer foreign currency trading services to Bahamians¹.
- Subsequent to the February liberalization reforms, in August, 2018, the Bank amended Exchange Control policies to allow commercial banks to establish Bahamian dollar deposit facilities for non-resident individuals, without prior Exchange Control approval, when balances on such facilities are proposed at B\$50,000 or less. Under this new policy, the exchange control stipulation for banks to ascertain the work permit status of account holders to open accounts no longer applies. The reform supports the financial inclusion initiative, which introduced streamlined customer due diligence requirements that supervised financial institutions should follow when establishing low-risk relationships under revised AML/CFT Guidance issued in June, 2018. ♦

¹ For a complete listing of liberalization measures, please see the central bank's website at: www.centralbankbahamas.com

ECONOMIC ANALYSIS, STATISTICS AND RESEARCH

The Bank, through its Research Department, plays an important role in providing the public with comprehensive, accurate and timely information on domestic economic and financial developments. During the year, the Department sustained its publication of the Monthly Economic and Financial Developments (MEFD) report, the Quarterly Economic Review (QER), the Quarterly Statistical Digest (QSD) and the Annual Report. In addition, the Financial Stability Report (FSR) for 2017, which analyzed developments in the financial sector and provided an assessment of the potential risks to stability from both internal and external factors, was published in June 2018.

In the March 2018 edition of the QER, the Department also published findings from the annual survey on the “Gross Economic Contribution of The Financial Sector to the Economy” for 2017. Further, the information compiled for the quarterly Bank Lending Conditions Survey (BLCS), was disseminated to the public via the quarterly MPC presentations.

During the year, the Department played a pivotal role in the implementation of the International Monetary Fund's (IMF) Enhanced General Data Dissemination System (e-GDDS), which allows the public to access key reports on the economy through one portal and facilitates the dispersion of economic and financial data to various



international institutions, via the machine readable Statistical Data and Metadata Exchange (SDMX) format. Further, in line with its mandate, the Department provided economic and financial data to a variety of regional and international bodies.

In 2018, research projects undertaken by staff focused on an array of topical issues, which were presented at the Department’s internal roundtable forums and at external conferences. The papers included: *“The Effectiveness of Countercyclical Policies in The Bahamas”*, *“The Importance of Financial Inclusion in The Bahamas”*, *“An Analysis of the Commercial Enterprise Act”*, *“Forecasting Methodologies”*, *“Excess Liquidity in The Bahamas’ Banking Sector”*, *“Measuring the Level of Dollarization of the Bahamian Economy”*, *“Optimal Monetary Policy Framework in an Environment of Excess Liquidity”*, and *“The Impact of Credit Rating Downgrades on the Cost of Government Borrowing”*. In addition, some members of staff presented their research work at the regional annual Monetary Studies Conference, which was held in Barbados in November and at the Research Review Seminar hosted by the Central Bank of Trinidad & Tobago in June. At these events, staff from the Department shared papers entitled, *“An Analysis of the Relationship Between Non-Performing Loans and Macroeconomic Indicators in Selected Caribbean Countries”*, *“Is Government Borrowing Crowding Out Private Sector Credit in The Bahamas?”* and *“Policy Options for Debt Sustainability in The Bahamas”*.

During the year, staff also participated in a myriad of external training events. These included workshops on financial integration, hosted by the Alliance for Financial Inclusion (AFI) and the Bank of Ghana, and a Monetary Policy Workshop, facilitated jointly by the IMF, CEMLA and The Central Bank of Colombia.

The Department continued to play an important role in the Bank’s outreach programme, with staff facilitating regular presentations to primary and high schools, as well as college students on the role and functions of the Central Bank. Staff also fielded several requests from members of the public to provide presentations on various economic topics.

PRUDENTIAL SUPERVISION & REGULATION

The Central Bank’s supervisory responsibilities cover a range of licensed activities under the Banks and Trust Companies Regulations Act, 2000 and various subsequent amendments, the Payments System Act, 2012, the Credit Union Act, 2015, and the Credit Reporting Regulations Act, 2018.

During the year, the number of bank and trust company licensees decreased by 11 to 231 (See: Table 3). In total, 6 licenses were issued (2 public banks, 2 public trusts and

2 restricted nominee trusts) and 17 entities ceased to carry on business (consisting of 4 public banks, 4 restricted nominee trusts and 9 non-active nominee trusts). Of the 231 licensed entities, 219 maintained a full physical presence in The Bahamas, while the remaining 12 operated via approved management agreements. Approximately 43% of the total licensees originate from G-10 countries.

The total number of private trust companies (PTCs) rose by 15 to 136 at end-2018. The Bank approved the registration of 24 PTCs, while removing 9 from the register. Meanwhile, financial and corporate service providers, that act as registered representatives (RRs), remained at 5, while 2 additional licensees advised the Bank of their intentions to act as RRs of PTCs, increasing the number to 23.

In other groupings, licensed non-bank MTBs remained at 5, while related agents increased by 8 to 20. Also, the number of financial co-operative credit unions stayed at 10, inclusive of the Bahamas Cooperative League Limited. The Bank also licensed the first standalone retail payment service provider, with at least one other application under consideration.

Applications processed and approved for regulated functions and positions totalled 428—the majority of which were linked to new appointments of officials. In keeping with prescribed “fit and proper” requirements, the Bank reviewed and approved the appointment of 168 directors, 158 money laundering reporting officers (MLROs) and executive officers and 84 senior officials/officers. In other administrative activities, 32 outsourcing applications were approved, as licensees took further decisions to streamline operational overhead and benefit from economies of scale.

Table 3: Regulated Entities

	2016	2017	2018
Banks and Trusts	248	242	231
Banks & Trusts	62	55	54
Banks	31	30	29
Trusts	155	154	148
Non-Licensee RRs	5	5	5
Licensee RRs	19	21	23
PTC (Registered)	121	121	136
Non-Bank MTBs	3	5	5
Non-Bank MTAs	11	12	20
Cooperative Credit Unions	10	10	10
Retail Payment Service Providers	--	--	1
Memo Items:			
Assets of Domestic Banks (B\$Bill)	18.53	19.08	17.43
% change	-36.0%	2.9%	-8.6%
Assets of Int'l Banks (B\$Bill)	165.03	168.45	166.10
% change	-29.1%	2.1%	-1.4%

Source: Central Bank of The Bahamas



Supervisory and Regulatory Developments

During the year, the Bank continued to follow very closely the policy agenda of international standard setting bodies, such as the Basel Committee, the Financial Action Taskforce (FATF), the Organization for Economic Co-operation and Development (OECD) and the Financial Stability Board (FSB). In particular, the Basel Committee focused on its ongoing evaluation of post-crisis reforms, much of which is embodied in the Basel III framework. The Committee continued to explore the role of proportionality in the Basel framework, while emphasizing the importance of implementing the post-crisis reforms in a full, timely and consistent manner.

The Bank, through its Supervision Department, unveiled its revised proposals with respect to Basel II and III implementation, taking a more proportionate measure, based on the size and complexity of banks operating within and from within this jurisdiction. The proposals and the resulting feedback, will guide the development of a draft capital regulation document in 2019.

On the AML/CFT front, the Government developed an aggressive legislative agenda to enhance the financial sector's legal, supervisory, regulatory and enforcement regimes, in the wake of international pressure. The agenda primarily addressed the legal, regulatory, supervisory and enforcement framework gaps identified in the CFATF's Recommendations from the 2017 MER, the National AML/CFT Risk Assessment, the OECD Global Forum on Tax Matters and the European Union's Code of Conduct Group's concerns. In June 2018, the Bank issued binding guidance information regarding a simplified approach to customer due diligence (CDD) for Bahamian domestic accounts. This approach encourages more financial inclusion for low risk customers, and greater focus on source of wealth documentation for high-risk clients. In addition, in August 2018, the Bank released the revised version of its AML/CFT Guidelines. These Guidelines were amended to align with the compendium of new legislation passed in 2018.

Given the ongoing pressure that banks faced in maintaining correspondent banking relationships (CBRs) with international counterparties, the Bank continued to monitor such developments in 2018, to determine if the loss of CBRs has had any destabilizing impact on financial institutions or the system at large. The results of the Bank's AML Survey in 2018, revealed that the majority of banks continued to be insulated from the threats of de-risking; although a growing minority have faced some challenges. Overall, much of the sector has felt the impact of the heightened monitoring by correspondent banks, which has become the "new normal".

In terms of mutual evaluation, The Bahamas was found to be "Largely Compliant" in the Global Forum's Phases 2

and 3 Peer Review Reports, published in 2013 and 2018, respectively. These reviews focused on the availability of beneficial ownership information, access to beneficial ownership data and information exchange. Historically, the Bank's SFIs were operating from a reasonably sound base, as they maintain beneficial ownership information on their clients and client structures. Their internal registers are verified and confirmed through the Bank's examination process. In the context of the financial sector at large, the Government sought to address the OECD's concerns with the passage of the Register of Beneficial Ownership Act, 2018. This legislation, establishes a secure and searchable database of the ownership details for all legal entities registered in The Bahamas, with the "Competent Authority", same being the Registrar General's Office. The database will only be accessible by a designated person from a secure location in The Bahamas.

Overall, 2018 ushered in a wave of supervisory and regulatory developments in the face of threats of The Bahamas being blacklisted by the European Union and to strengthen the jurisdiction's AML/CFT regime to address the gaps identified in the MER.

Supervisory Effectiveness

Building upon the Bank's decision in the prior year to commence continuous supervision of the AML/CFT regime, in 2018, the Bank shifted its strategic focus towards more effective intervention and refining administrative processes, where feasible.

Effective Supervisory Intervention

The Bank's supervisory actions are classified into three categories:

- **Directives**, which address the most urgent and serious matters;
- **Requirements**, which are not as serious or urgent as Directives, but which are sufficiently serious that the Bank is prepared to deploy its statutory powers in an effort to achieve the required result; and
- **Expectations**, which cover matters where an SFI, should consider improving some aspect of its risk management.

The core determinant on whether or not the Bank is effective in achieving its prudential mission, is its ability to rapidly and effectively resolve directives and requirements. From 1st January to 30th September 2018, the stock of outstanding directives was reduced from 26 to 8. No new directives were necessary during this period. Of the remaining 8 directives, as of 30th September 2018, 7 were classified as making satisfactory progress, while 1 was progressing more slowly by comparison. It is worth noting that SFIs are generating a substantial rate of closed



requirements and are generally on track with outstanding requirements.

AML/CFT versus Other Supervisory Interventions

From March 2018, the Bank measured the split between AML/CFT and other supervisory interventions. For the period in which AML/CFT supervision was the primary focus, the number of new AML/CFT matters was much greater than the number of new financial soundness or other issues; this pattern should continue during 2019. In addition, the introduction of the new administrative monetary penalties (AMP) regime for money laundering/terrorist financing breaches in 2018, may pre-empt a surge in new issues.

Procedural Improvements

From January 2018, the Department’s examination process was changed, with the major reform focusing on reducing the timeline from the examination visit, to the issuing of the Report of Examination (RoE). The RoE summarizes the examination’s findings, and commonly defines supervisory interventions, such as Directives and Requirements. Shortening the time between visits and the issuing of the RoE, reduces the time taken by SFIs to correct identified deficiencies. During the year, all on-site examinations resulted in RoEs being issued within 20 business days of the visit—which is the performance benchmark. Prior practice sometimes led to RoEs not being issued in final form for several months after the examination; therefore, the Bank considers this to be a material improvement in the supervisory practice.

In addition to supervision and examination, the Bank reviewed applications from SFIs to grant various authorizations and approvals, the largest of which related to the consideration of candidates for “approved persons” positions. Table 4 outlines the Bank’s success since 2017 in materially reducing the average time taken to process an “approved persons” application. Much of that reduction has arisen from streamlined internal approval processes. Further, in the latter half of the year, the Bank began to see the benefits of more engagement with the industry and provided more guidance on authorization forms and procedures.

Overall 2018 has proven to be a highly satisfactory year for supervisory effectiveness, as the Bank met the major challenge of moving to continuous supervision of AML/CFT risks. In addition, metrics associated with process efficiency, and even more importantly, effectiveness of interventions also improved.

AML/CFT Supervision

Following the migration from periodic to continuous oversight of money laundering/terrorist financing (ML/TF) risks of SFIs in late 2017, the Bank worked to further develop its AML/CFT supervisory framework. At the beginning of 2018, the Bank received responses from an AML/CFT survey, which was issued to banks, trust companies, credit unions and MTBs. The survey focused on various areas of AML/CFT, including governance, Money Laundering Reporting Officer/Compliance Officer (MLRO/CO) functions, training, policies and procedures, cash transactions, clientele, and the composition of transactions. The submitted responses gave the Bank an improved perspective upon which to continue to enhance the AML/CFT supervision of SFIs under its remit. The summary results from the survey of the banking and trust sector were released on 20th April 2018.

In addition, the Bank incorporated a more granular assessment model of the ML/TF risk within its risk-based super-

Table 4: Applications for Approved Persons

	Mar-17	Jun-17	Sep-17	Dec-17	Mar-18	Jun-18	Sep-18
Applications	22	9	14	9	25	27	17
Follow-up	55%	56%	64%	33%	72%	44%	29%
Average Days - if Followed-up	84.8	68.8	37.1	31.0	24.2	27.4	26.6
Average Days - if Complete	23.4	19.0	14.6	10.7	8.4	10.5	10.8

Source: Central Bank of The Bahamas

visory framework (RBSF). This model gave the Bank the opportunity to attain a detailed, baseline view of the ML/TF risk of its SFIs, on an individual basis. The Bank performed AML/CFT focused risk assessments on 75 public SFIs and 9 co-operative credit unions. In the future, the Bank intends to develop and launch an updated version of its AML/CFT supervisory regime, based upon consultations with, and information received from SFIs over the year. It is envisioned that this regime will involve greater engagement with the industry and other external parties.

On a national level, representatives from the Bank continued to actively participate in The Bahamas’ Identified Risk Steering Committee (IRSC); formerly the National Task Force. The IRSC currently meets on a weekly basis to discuss AML/CFT work within the jurisdiction, and to address deficiencies noted in The Bahamas’ 2017 MER, on AML/CFT effectiveness.

Risk Based Supervisory Framework

Following the Bank’s introduction of the “ever-greening” concept in 2017, further enhancements to the RSBF continued in 2018, with greater emphasis being placed on assessing ML/TF risks. Given this focus on an in-depth review of SFIs’ ML/TF risks, the number of full/



simplified risk assessments completed in 2018 declined relative to the previous year. As at 31st December 2018, three SFIs were “ever-greened”, six full/simplified risk assessments were completed, while 11 assessments were at various stages of completion. The Bank intends to continue its “ever-greening” reviews and commence its new cycle of SFIs’ risk assessments for 2019. The Bank is also in the process of developing an automated RBSF for co-operative credit unions, which will be rolled-out in 2019.

Data Analytics

To enhance and streamline data compilation and regulatory surveillance processes, the Bank made some key changes to the reporting suite of forms for co-operative credit unions and MTBs; reporting forms are also expected to be completed for registered representatives in 2019. These enhancements will allow for the efficient and consistent collection of data from all reporting SFIs within the Bank’s Online Reporting and Information Management System (ORIMS). Further, through the development of automated tools and revised templates, the Bank has also streamlined the process for Supervisors to perform prudential analyses and reviews of financial data.

Examination Programme

On-site Examinations

Over the course of 2018, the Bank conducted a total of 22 on-site examinations (See: Table 5). The examinations conducted included:

- 4 full scope safety and soundness examinations, 2 of which were for international firms and 2 for MTBs;
- 4 limited scope reviews of commercial banks’ risk management frameworks in the areas of AML/CFT, operational risk, and corporate governance;
- 5 special AML focused examinations of international firms, including a request by the home regulator of a local subsidiary;
- 9 limited scope reviews of international firms, where several risk areas, including AML compliance, credit and corporate governance were examined, in addition to validating the effectiveness of the remedial work undertaken to close gaps identified during the previous examinations.

As a result of this process, 20 examination reports—including two outstanding from 2017—were completed. No reports were issued to SFIs for two of the special AML examinations; however, internal reports were generated for supervisory purposes. As at December 2018, two reports, although drafted, were yet to progress to final format, but are expected to be issued within the target timeframe. Reports for all examinations undertaken in 2018 were issued within the required 20 workday timeframe.

Table 5: On-site Examinations Conducted

	2016	2017	2018
Examinations			
Domestic Licensees	4	4	6
Other Licensees	15	14	11
Follow-up /Special Focus/ Regulator Initiated	4*	0	5**
Discovery Reviews	8*	11*	0
Financial Credit Unions	4	1	0
Total	35	30	22
Reports			
Finalized Reports	27	22	18
Reports in Progress	5	2	2
Total	32	22	20

Source: Central Bank of The Bahamas

* No report to SFI required, internal report generated for supervisory purposes.

** Internal Report generated for supervisory purposes for 2 of the examinations.

In 2018, the Examination Unit also undertook four joint examinations with the Securities Commission of The Bahamas (SCB), three of which were special AML focused reviews, which utilized the *Protocol for the Joint On-site Examinations by the Central Bank and the Securities Commission of The Bahamas* (the Protocol); this was revised in January 2012.

Off-site Surveillance and Monitoring Activities

International Supervised Financial Institutions

At the end of 2018, the number of Central Bank SFIs totalled 216 banks and trust companies, compared to 219 at end-2017, representing some 96.4% of the total number of SFIs operating from within The Bahamas. Collectively, the international SFIs maintained an asset base of US\$166.1 billion as at end-2018, comprising primarily investments and market placements. The asset base stood at approximately US\$168.5 billion at the end of 2017, which indicated a slight decline from 2016. For 2018, the makeup of the SFIs continued to be primarily subsidiaries or branches of larger international/global entities.

With The Bahamas signing onto the OECD’s Multilateral Competent Authority framework for the Common Reporting Standards on automatic tax information exchange on 13th December 2017, there continued to be marginal declines in customer deposits in 2018, as international clients took advantage of relevant tax amnesty programmes. Further, businesses operating models were re-engineered, which impacted the strategic plans of international SFIs’ ownership structure and human capital.

Throughout 2018, the Bank continued to utilize its primary supervisory tools to monitor and supervise the international firms via AML/CFT risk analyses, financial analyses, prudential meetings, discovery review meetings,



annual meetings with internal auditors (local and international) and on-site examinations. Further, collaborations were held annually with local financial industry stakeholders and home regulators.

International SFIs continued to reduce costs by way of outsourcing, via service level agreements (SLAs), both internationally and locally (home SFIs). In some cases, there were greater demands for global regulatory requirements, compliance initiatives, as well as other regulatory reforms, which has caused parent banks of SFIs to continually examine and rationalize their offshore businesses. In some cases, the end results were either a restructured or a reduced business presence within The Bahamas. SLAs were largely concentrated to back office administration, wealth management, human resources, internal audit, business continuity and IT general maintenance and support.

Domestic Banks and Trust Companies

During the year, the number of commercial banks remained unchanged at 8, inclusive of 3 locally owned banks, one US and four Canadian-based banks. Another 8 banks and trust companies are also authorized to provide services in the domestic market. These concentrate on a limited book of fiduciary services, with the more substantive activities targeting international clients. As at year-end, the total assets of banks and trust companies stood at B\$17.4 billion, which represented a decrease of B\$1.7 billion (or 8.6%) since year-end 2017. The four Canadian banks continued to account for approximately two-thirds of the total domestic banking assets. During 2018, commercial banks' branch networks increased by 9 to 76.

The Bank maintained its enhanced monitoring of commercial banks, to detect and address any emerging risk issues, given their systemic importance, via its RBSF. Through the formal risk assessment process, several of the commercial banks' risk ratings were updated to reflect the Bank's view of the key risks impacting their operations. The process primarily encapsulates an assessment of the institution's key business risks and control environment and is supplemented with the analysis of financial and non-financial regulatory returns and periodic risk management meetings with senior management and independent risk and control functions. Supervisory cooperation and communication, via supervisory colleges, regional teleconferences and other bilateral exchanges, played a pivotal part in the ongoing monitoring of the commercial banks during the course of the year.

Credit Risk Reviews

During 2018, the Bank continued with its oversight of credit risk in the domestic banking system, monitoring the top 20 non-performing loans (NPLs) of each commercial bank. Half-yearly and ad hoc meetings were held with senior bank executives, to discuss strategies deployed to

reduce their NPL levels and the resulting outcomes. The predominant elements of the supervisory monitoring, included periodic reviews of the credit risk structure, that is collateral and other based lending, specific provisions, performing and non-performing trends, concentration and diversification of the credit risk portfolio, underwriting processes and the overall performance of the credit portfolio.

In November 2018, the Bank facilitated training for all commercial banks, credit unions and insurance companies, on the draft Credit Reporting Regulations, 2018. The training was conducted by the International Finance Corporation (IFC) and focused on the "Supervision of the Credit Bureau and the Role of the Information Providers/Users". It is anticipated that with the establishment of the credit bureau, more comprehensive credit information will be provided to lenders and it will lead to the development of a credit scoring mechanism for borrowers, which will facilitate improved credit risk management by commercial banks and other credit providers and also increase high quality borrowers' access to credit.

The industry's NPLs continued on a downward trend, declining by 8.9% or \$50.5 million in 2018. This reduction was primarily as a result of distressed asset sales in the residential and commercial real estate property portfolios of certain domestic banks. More broadly, some domestic banks continued to provide concessions to existing customers through debt consolidation and restructuring.

Stress Testing

Credit risk stress testing is conducted periodically for commercial banks by updating the Bank's model using forecasted macro-economic variables. The stresses are designed to assess the resilience of the domestic sector as a whole (or top-down stress testing) and individual banks (bottom-up testing) to extreme, but plausible stressed scenarios. Using varying growth rates, along with forecasted macro-economic indicators, the aggregate position of the balance sheet and income statement is forecasted for the industry for three years. The forecasted NPLs are subject to shocks of 100%, 150% and 200% for each of the three years, the impact of which flows through to the statement of income, with increases (or decreases) in expenses relative to loss interest income and provisions for impaired loans, ultimately impacting the level of capital.

The results of the consolidated credit risk stress tests conducted in 2018, consistently showed that at all levels of shock, which reduced capital levels up to 10.1%, no new capital injection was required. Capital levels remained comfortably above the trigger and target ratios of 14% and 17%, respectively, at an average capital to risk-weighted assets of 31.3% to 35.6%, thus negating any short to medium risks to financial stability.



At varying levels of shocks to the NPLs, the earnings of banks would be negatively impacted, as a result of increases in provisioning levels and the loss in interest income. The banks would therefore be expected to partially counter the impact of the same by seeking other non-interest income sources.

Interest and Liquidity Shocks

Interest rate stress tests calculate a proxy measure of the impact on the consolidated and individual capital of commercial banks of shifts in yields on the Bahamian currency and foreign currency on the net balance sheet valuation of the SFIs. The assumed change in the yield was 100 basis points for Bahamian currency and 200 basis points for foreign currency. The results continued to show that commercial banks are less susceptible to interest rate risk in their banking books, given the infrequent change in the Bahamian dollar Prime lending rate and the continued robust level of eligible capital, among other factors.

Liquidity risk stress tests are based upon commercial banks' liquidity gap analysis captured in maturity ladders and cashflow forecasting, based upon specific inflow and outflow assumptions, that are expected to occur in a liquidity stress scenario. These test results continued to indicate that banks' risk to near-term depletion of liquidity is negligible, due to the high level of liquidity across the banking system, bolstered by banks continued conservative stance to lending. Generally, banks have the capacity to withstand sudden shifts in their deposit base without encountering liquidation challenges.

Capital Adequacy

Despite periodic dividend payments to shareholders, commercial banks' capital levels remained robust. At end-December 2018, the capital-to-risk-weighted ratio stood at 32.29% and the common equity to tier 1 capital-to-risk weighted ratio stood at 29.93%, well above the established regulatory target and trigger ratios of 17.0% and 14.0%, respectively.

Credit Unions

During the annual meetings with the credit union sector, key regulatory expectations and practices were discussed, including corporate governance, credit risk management, AML/KYC initiatives, inclusive of the Deposit Insurance Corporation's (DIC) coverage, AMPs, the impact on capital of transitioning to Basel III and other relevant topics affecting the sector. The sector meanwhile transitioned towards a risk-based supervision approach. This new framework provides for the application of an enhanced supervisory focus on the inherent risk monitoring within this group of SFIs; similar to the application to banks and trust companies. The operations of these SFIs also continued to be monitored through: risk assessments, analysis of financial returns utilizing

key PEARLS⁴ standard ratios, onsite examinations, remediation efforts and AML/KYC assessments, which form part of the supervisory programme.

At end-2018, the total assets among the 10 registered entities stood at \$449.0 million, for an average growth rate of 6.6% over the past five years. The membership covered 43,880 persons, compared to the 42,186 persons recorded a year earlier.

Money Transmission Businesses

The regulatory and supervisory regime for MTBs and MTAs, is designed to ensure adherence to regulatory and statutory filing requirements. In 2018, the Department commenced a programme comprised of an on-site facility visit and presentations from the five MTBs, with a focus on their AML/KYC regime and technology systems capability. It is envisioned that this programme will continue as a part of the supervisory agenda going forward. MTBs are continuously devising strategies to remain competitive within the market by, *inter alia*, engaging in strategic partnerships to facilitate money transfers within remote Family Island locations, while also expanding their product offerings in an effort to grow their customer base.

Basel II and III Implementation Programme

During 2018, the Bank consulted with the industry by way of four discussion papers, which proposed to simplify the Bahamian Basel II and III frameworks, consistent with the proportionality principles set out by the Basel Committee. It is also in keeping with the development of prudential policies and regulations that balance safety, efficiency and competitiveness in the Bahamian banking system, while promoting financial system stability. The Bank expects that the introduction of a simplified approach would reduce regulatory compliance costs, relative to the current capital regime, and in line with the typical international implementation of Basel III.

The proposals issued covered the areas below.

- **Capital Requirements:** this paper proposes an optimal capital regime for the Bahamian banking system that is consistent with the proportionality principles set out by the Basel Committee.
- **Minimum Disclosures:** outlines an approach to implement Pillar 3 Disclosures (regulatory capital and risk exposures), that optimises the accessibility, consistency and comparability of banks' financial information, without imposing any additional regulatory burden or costs.

⁴ PEARLS measure key areas of a credit union's operations. The word stands for: Protection, Effective financial structure, Asset quality, Rates of return and costs, Liquidity and Signs of growth.



- **Domestic Systemically Important Banks:** provides a framework that would ensure that banks identified as systemically important in The Bahamas, are subject to more intense supervisory oversight and have greater capacity to absorb losses.
- **Liquidity Coverage Ratio (LCR) and Net Stable Funding Ratio (NSFR):** outlines the proposed approach to implement the LCR and NSFR, detailing what qualifies as High Quality Liquid Assets (HQLA), the calculation and requirements for the LCR and NSFR, and the Bank's approach to implementing enhanced liquidity monitoring tools.

The Bank intends that its Basel II and III frameworks will be fully implemented during 2020.

Supervisory Policy and Guidance

The Bank issued a number of guidance notes in 2018. The first two guidance notes listed were jointly issued by the Bank, the Securities Commission of The Bahamas, the Insurance Commission of The Bahamas, and the Gaming Board For The Bahamas. A major guidance note was also revised, following the amended suite of AML/CFT legislation. The domestic regulators will continue to find opportunities to issue consistent guidance across jointly regulated industries.

Guidance Notes and Policies

- **Guidance Note on the Sound Management of Risks Related to Financial Crime in The Bahamas (August 2018):** covers risk management approaches for AML/CFT and other financial crimes and acts as a guide to Bahamian financial entities, to improve industry practices.
- **Guidance Note on Proliferation and Proliferation Financing (August 2018):** raises awareness of risks and vulnerabilities with regard to proliferation and proliferation financing.
- **Board Engagement Policy for Supervised Financial Institutions (July 2018):** describes the Bank's supervisory framework for engaging more closely with the boards of SFIs, based on a risk-based approach.
- **Guidance Note on Streamlined Requirements for Account Opening, Provision of Financial Services and Customer Identification (June 2018):** clarifies the Bank's policy in relation to customer due diligence procedures for the purpose of account opening, and general customer identification and indicates which documents can be used to verify customers' identities.
- **Guidelines for Licensees on the Prevention of Money Laundering and Countering the Financing of Terrorism (Revised, August 2018):** revised the version first issued in May 2009 and previously updated

in May 2017. These achieve alignment with AML/CFT reforms under the Proceeds of Crime Act, 2018, the Financial Transaction Reporting Act, 2018, the Anti-Terrorism Act, 2018, the Financial Transactions Reporting Regulations, 2018 and the Financial Transactions Reporting (Wire Transfers) Regulations, 2018.

Legislative Initiatives

Various legislative reforms under the Bank's direct remit progressed during 2018, with the Parliamentary approvals concluded for the dormant accounts reform and the credit bureau (See: Box 3).

Crisis Management

In 2018, the Bank continued its vigorous surveillance of the domestic systemically important banks (D-SIB), with increased prudential supervisory oversight of this grouping, aimed at ensuring that firms remained sound and resilient within the financial system, in order to better withstand negative consequences in the face of crises. The Bank either commenced or targeted measures aimed at enhancing crisis management preparedness, including improving early detection and intervention tools; strengthening legal underpinnings of the resolution regime, and bolstering the technical operations and resources of the deposit insurance framework.

Early detection measures include the annual preparation of a financial stability report and the Bank's prudential supervisory toolkit. In this regard, pre-emptive interventions are aligned with the Bank's Ladder of Supervisory Intervention, and the robust risk-based approach to tailoring the frequency, intensity and specific nature of engagement with D-SIBS. Proposed legislative reforms to the resolution regime will grant full administrative resolution powers to the Bank, to facilitate expedited orderly bank resolutions, under the sole direction of the Bank, rather than through the courts. In addition to the domestic focus on deposit insurance, the Central Bank also continued to collaborate with the Caribbean Group of Banking Supervisors (CGBS), on a draft regional financial crisis management plan, and a draft CARICOM plan to harmonize regional deposit insurance frameworks.

Regulatory Cooperation

The Bank cooperates with both domestic and international regulators on areas that advance the overarching national objectives of improving the effectiveness of the Bahamian supervisory regime, while also meeting various international obligations.

On the domestic front, senior staff from the Bank participated in the work of the Group of Financial Service Regulators (GFSR), which comprises the five domestic regulators for banks and trust companies, the securities industry, insurance companies, credit unions and financial



Box 3: 2018 LEGISLATIVE REFORMS

- **The Credit Reporting Act, 2018**, was passed by Parliament in February 2018. This Act establishes a legal and regulatory framework to support a national credit reporting system. A credit bureau is an essential part of the financial sector infrastructure, as it promotes more efficient lending, enhanced financial stability prospects and greater inclusion.
- **The Draft Credit Reporting Regulations, 2018**, was subsequently Gazetted in [February 2019] to provide the remaining oversight framework for the credit bureau regime.
- **The Draft Central Bank of The Bahamas Bill, 2018**, submitted for Government approval, will consolidate and modernize the legal framework for the Central Bank of The Bahamas, in line with evolved best international practices. The proposed reforms seek to strengthen and clarify the existing provisions relative to the objectives and functions and legal environment of the Bank, statutory limits on Central Bank lending to the Government; and increased transparency around operational independence.
- **The Banks and Trust Companies Regulations (Amendment) Act, 2018**, introduced an amended framework for dormant accounts administration. It expands the range of assets and accounts held at financial institutions that would be transferred to Central Bank custody, after a seven-year period of inactivity. New provisions also allow for ownership of the assets to transfer to Government ownership after being unclaimed for a further 10 years.
- **The Draft Bank and Trust Companies (Administrative Monetary Penalties) (Amendment) Regulations, 2018**, will simplify the existing administrative penalties regime, by introducing a fixed rate penalty for erroneous financial returns, and will allow for flexibility in terms of the amount of penalty imposed on a SFI for late and erroneous filings. Penalties imposed under the existing regulations totalled \$361,500 in 2018, compared to \$595,500 in 2017. Breaches since 2016 have commonly been classified under 18 different categories—the most active being late or erroneous filing of the Daily B\$ Position, Weekly Interim Reports, and Quarterly Unaudited Financial Statements.
- **The Draft Bahamas Public Debt Management Bill, 2018**, will consolidate and amend the law relating to the management of Public Debt in The Bahamas and provide for the governance aspects, high level policy objectives and institutional arrangements for the prudent management of the Government's debt, the making of guarantees and loans, the receiving of grants, and to provide for matters connected therewith or ancillary thereto.

and corporate service providers. In 2018, the GFSR executed the flagship inaugural AML Risk Management Conference, held at the Baha Mar Resort on September 17 and 18. More than 400 persons from a cross-section of the financial services industry attended the event, which promoted awareness of the national strategy for AML/CFT risk management, industry issues, and planned reforms stretching into 2019. The GFSR's members also jointly developed AML/CFT-related guidance notes, and executed other public outreach, including an annual AML publication. An information-focused AML website is targeted for launch in 2019.

At the regional and international levels, senior staff of the Bank Supervision Department attended the Group of International Financial Centres Supervisors' discussions, which were held in London and Abu Dhabi, respectively, the latter as part of the biennial International Banking Supervisors' Conference 2018. More generally, the Bank Supervision Department participated in regulatory colleges in the Caribbean and Canada for the domestic systemically important banks and an international trust company.

Further, engagement with home-consolidated regulators of SFIs continued to be facilitated through the annual regulatory letters. This is a proactive measure to ascertain

Table 6: 2018 Requests for Cooperation

Country	Requests Received from Foreign Regulators
Antigua	1
Jersey	1
Korea	1
Luxembourg	2
Malta	1
Peru	2
Singapore	1
St. Kitts	1
Switzerland	3
Trinidad & Tobago	1
Total Requests	14

Source: Central Bank of The Bahamas



the risk areas identified within the group entity, and to gauge whether any impact would be transmitted to the established operations within The Bahamas. Information with respect to specific regulatory issues or financial, operational and environment risk factors, are exchanged through the various Memorandums of Understanding (MOUs) in force with foreign supervisors.

In 2018, the Bank received and responded to 14 information requests from 10 foreign regulatory authorities (See: Table 6).

DEPOSIT INSURANCE CORPORATION

The Bank has the statutory responsibility to oversee the Deposit Insurance Fund (the Fund) for Bahamian dollar deposits in the banking system in The Bahamas. The Deposit Insurance Corporation (DIC), insures Bahamian dollar deposits up to a maximum of \$50,000 for any single depositor in each of its 11 member institutions. These entities do not hold equity positions in the DIC.

The DIC assesses the depository institutions, an annual premium equal to one-twentieth of one percent (0.05%) of deposits, averaged over liabilities as at 31st March and 30th September of the preceding year. Based on average total insurable Bahamian dollar deposits in domestic banks of \$6.3 billion in 2018, relative to \$5.8 billion in the previous year, premiums levied and collected in 2018 amounted to \$3.2 million, in comparison to \$2.9 million in 2017. Factoring net earnings, the accumulated assets of the Fund increased by approximately \$5.7 million to \$56.4 million, with \$52.5 million invested in Bahamas Government securities. At end-2018, approximately 82.3% of Bahamian dollar denominated accounts held balances of less than \$5,000, with 10.7% of deposit accounts ranging between \$5,000 and \$25,000, and 2.6% of deposit accounts ranging between \$25,000 and \$50,000.

In 2018, the DIC continued its public awareness campaign, aimed at bolstering confidence in this safety net mechanism. In this regard, social media outreach expanded, while outreach through traditional media channels increased. The DIC also encouraged member institutions to intensify customer-targeted education programmes about the scheme.

In the area of staffing, the Bank increased the number of full-time personnel dedicated to the DIC, in keeping with the overall strategy of institutional strengthening. In addition, consultation progressed around bringing credit unions under the scheme, and assessments coalesced around the adequacy and soundness measures, as part of a medium-term strategy to target a higher level of funding resources for the DIC. Further, the DIC employed crisis simulation scenarios, to help identify gaps in the contingency planning and preparedness around potential distress or failures within financial institutions.

INFORMATION TECHNOLOGY

In the area of Information Technology (IT), the Bank continued to focus on improving operational efficiency, system availability and mitigating cyber security risks, all against the backdrop of a planned systems modernization initiative. During the year, the major projects completed included several upgrades and enhancements to core systems that support the Bank's mandate, such as SWIFT and RTGS. The Bank's telephone system was also upgraded to ensure improved resiliency and efficiency. Improvements were also made to the institution's document capture and imaging solution, resulting in shortened application turnaround times in the Bank Supervision and Exchange Control Departments.

In light of an uptick in cyber-related incidents worldwide, core systems in the Bank were strengthened, internal controls reviewed and enhanced, and staff were trained to identify and mitigate information security vulnerabilities and risks. The incident management process was also reviewed and revised to enhance service delivery and strengthen overall systems availability. In support of this initiative, the Bank also augmented its systems monitoring capacity, by acquiring a cloud-based monitoring solution, which allows comprehensive monitoring of internal and external information assets and comprehensive executive reporting.

FACILITIES MANAGEMENT AND HEALTH & SAFETY IN THE WORKPLACE

The Bank conducts its business from the Main Building, situated between Market Street on the west and Frederick Street on the east, and the leased Trimark Building, located on the north of the main building. Another leased property in Freeport, Grand Bahama, is used to conduct exchange control-related business. The Bank also owns three protected historical buildings, namely, the Great House, which serves as the staff cafeteria; Balcony House, a two-storied period building presently managed by the Antiquities, Monuments and Museums Corporation (AMMC) as a museum; and Verandah House, formally used as a training facility by the Bahamas Institute of Financial Services (BIFS), and now converted into a gym for employees.

The Bank focused on various projects in 2018, to maintain workplace safety and enhance its facilities. Progress was also made against medium-range efforts to create new, modern facilities for the Bank's operations. In the first quarter of 2018, an Urban Plan and Architectural Concept Design Competition was launched to identify design concepts for a new headquarters, to be constructed at the Royal Victoria Gardens site in the City of Nassau. The winning design was submitted by Mr. Jason Lorandos of Architekton Design Studio Bahamas Ltd. The design is being fine-tuned to meet all of the Bank's requirements,



with Mr. Lorandos formally engaged to provide professional services for the project, in line with the Bank's requirements, which were laid out ahead of the design competition⁵.

Medium-range plans also include a separate constructed facility for the Bank's currency operations, apart from the new headquarters. The Bank is acquiring additional real estate for this purpose and also expects to advance this project in 2019.

During the year, the Bank also entered into a lease agreement with Poinciana (SPV) Limited, for space in the former UBS Building on East Bay Street, New Providence, for its Business Continuity Planning operations, and as a secondary IT site. Occupancy is anticipated to be completed in the second quarter of 2019.

To alleviate constraints on staff and the public, the Bank has also pursued a lease with the Anglican Diocese to develop a track of property on Market Street north of Gaol Alley for extra parking. Work is scheduled to commence on the site during the first quarter of 2019.

As part of its green initiative, the Bank sustained its efforts to carefully monitor its energy consumption. Although core usage has fallen, intensive construction works and repairs on-site, still resulted in an overall slight 0.5% rise in electricity use in 2018. Further, the total energy bill increased by 9.6%, due almost entirely to the rising fuel surcharge. Overall, total utility costs—including water & sewerage, electricity, cable and telecommunications—rose by 10.7% in 2018, when compared to the prior year.

STAFF COMPLEMENT AND RELATIONS

The staff complement increased by 2 to 247 in 2018. There were 28 employee separations, including 8 resignations, 6 terminations, and a combination of 13 retirements and end of fixed-term contracts; one active employee became deceased. This elevated the turnover rate by almost 4.0 percentage points to 11.3% (See: Table 7). During the year, there were 30 new hires, with 48 internal placements among existing staff, inclusive of 39 promotions and 9 lateral transfers. These changes mainly reflected the restructuring efforts of the Bank Supervision Department, which continued to strengthen its supervisory function for both financial soundness and AML/CFT risks. In addition, placements filled the need for new and specialised competencies in other key areas, such as the Research Department. At the end of the year, 30 vacancies existed across the Bank.

⁵ Parliamentary approval for the Bank to acquire the Royal Victoria Gardens property from the Public Treasury, commenced in December 2018, and the process was concluded in February 2019.

Table 7: Workforce Metrics

	2016	2017	2018
Staff Complement	246	245	247
Gender Distribution (%)			
Male	33.7	32.3	34.0
Female	66.3	67.8	66.0
Turnover Rate (%)*	6.2	7.4	11.3

Source: Central Bank of The Bahamas
* Includes staff who retired during the period

Of the total employee count, 174 were non-management, 61 were middle management, and 12 were executive management. The female to male ratio remained at almost 2:1.

As to the average tenure, some 26.3% of the staff have served for more than 20 years, 26.7% for more than 10 years, and 47.0% for 10 years or less. At the annual Long Service Award Ceremony, held on 23rd January 2019, 13 employees were recognized for the milestones achieved in 2018, regarding their continuous service to the Bank; for 30 years of service (9 individuals), 20 years (2 individuals), and 10 years of service (2 individuals.)

Employee Relations

On an ongoing basis, the Bank encourages communication with staff through departmental monthly meetings, a monthly Open Management Meeting for all managers, and weekly management meetings for Department Heads. In pursuit of more open communication with all staff, the Bank initiated general staff meetings, the first of which was held on 18th June 2018 in the Bank's Art Gallery. At this meeting, the Governor provided key information regarding the Bank's strategic goals and plans and engaged staff in active discussions regarding the current challenges and the future of the organization; feedback from the participants was generally very positive.

The Bank continues to foster employee engagement and promotes the well-being of staff. In this regard, sponsored events during the year included: the annual Family Fun Day, the Health and Wellness Week, the annual Christmas Party for employees, the annual Christmas Party for children of employees and monthly social gatherings. The Bank also sponsored employee participation in the biennial Caribbean Central Bank Games, held in St. Kitts & Nevis, from March 28 – April 02, 2018. The Special Activities Committee promoted team spirit in 2018, by encouraging quarterly competitive and fun activities among staff members. The events also provided an opportunity for staff to support charitable organizations. In addition, the Bank's new gym at Verandah House has been fully embraced by staff, as a major aspect of its healthy lifestyle programme.



With regard to team building, the Cultural Committee organized a session called “UnWind”, which afforded staff the opportunity for workplace camaraderie and a venue to produce ceramic art. Moreover, in October 2018, the Bank hosted the inaugural Cultural Arts Festival, featuring work of local craft persons and artisans. The event also featured music, food offerings, as well as a Junkanoo rush, and was touted as very successful.

It should be noted that 95% (135) of staff members comprise the non-management and the mid-management bargaining units. As the industrial agreement with the mid-management staff represented by the Bahamas Communications and Public Managers Union (BCPMU) expired in January 2019, negotiations are expected to be concluded during the coming year. The Industrial Agreement with other staff represented by the Union of Central Bankers (UCB), expires 31st December 2020.

In addition to the negotiations, the Bank continued to engage in open and constructive communications with both unions through separate quarterly meetings. During these forums, the unions were given updates on Bank matters and each union had the opportunity to table their queries and concerns. In particular, discussions ensued with relevant staff on the proposed “wind-up” of the Bank’s Retirement Plan (Defined Benefit Pension Plan). In sessions held during the year, the Governor outlined the Bank’s intent, timeline and the process for executing this matter.

Staff Development and Training

In 2018, the Bank continued to provide relevant training and development opportunities to ensure that staff members have the technical competencies needed to fulfil the Bank’s mandate. Learning experiences were made available through a combination of in-house, local and overseas training. A summary of the training is shown in Table 8.

Table 8: Summary of Training Developments

	In- House	Local	Overseas	Total
First Quarter	55	61	13	129
Second Quarter	44	24	53	121
Third Quarter	36	23	25	84
Fourth Quarter	33	13	36	82
TOTAL PARTICIPANTS	168	121	127	416

Source: Central Bank of The Bahamas

In-House Training

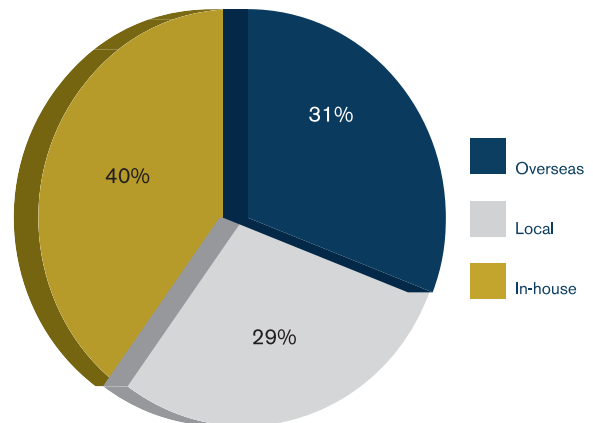
In-house training included the continuation of the Spanish Language Course with the completion of the third module. Specialized training on Firewall 8.0 Essentials-Configuration and Management, was also held for IT staff, while a Certified Procurement Fraud Control Specialist Training Course was conducted for participants

from various departments. A First Aid/CPR course was facilitated for new and renewal certifications.

Twenty-seven staff participated in an intensive 3-day Retirement Seminar Roadmap to a Golden Retirement, which addressed topics such as: Emotional Preparedness for Retirement, Staying Engaged after Retirement, Investment Options and Financial Planning. The participants were also afforded a one-on-one opportunity to sit with a financial planner. As the Bank accelerates its efforts to become an ISO Certified organization, 16 staff members—representing all departments in the Bank—participated in two intensive training courses, which were 2-modules each and one week in length, namely: ISO 31000-Enterprise Risk Management and ISO 27001-Information Security Management.

During the year, two Induction Training workshops were held to impart critical information about the Bank, its vision, mission, values, policies, benefits and opportunities for recently on-boarded staff. Later in the year, supervisory and middle managers of various departments participated in a Performance Management refresher workshop.

Employee Training (2018)



Local Training

Local and online training programmes included a wide range of technical courses to broaden competencies and skills. The Bank, along with other financial industry associates, hosted The Bahamas 2018 AML/CFT Risk Management Conference. Staff also attended several major local conferences, highlighted by the Americas’ Central Securities Depositories’ Association (ACSDA) Conference, hosted by the Bahamas Central Securities Depository; the Association of Supervisors of Banks of the Americas’ (ASBA) Annual Assembly, hosted by the Bank; The Bahamas Blockchain & Cryptocurrency Conference, organised by the Bank; the Institute of Internal Auditors (IIA) Awareness Month (Bahamas Chapter); and the Institute of Chartered Accountants



of the Caribbean (ICAC) Caribbean Conference of Accountants. Selected staff members participated in BICA's Accountants Week 2018 event; the 28th Annual Bahamas Society for Human Resources Managers (BSHRM) Conference and Business Expo, and the Caribbean Association of Banks Conference.

Other local seminars and training provided exposure to AML/CFT issues, current economic trends, human resources competencies, financial market analysis, public policy, financial technology, and international tax cooperation matters.

Representation and training at overseas conferences, meetings and seminars increased during the year. Such participation ensures that the Bank stays engaged in the global regulatory and supervisory arena, and improves its capacity to respond constructively to emerging trends.

Several conferences and meetings were hosted by key stakeholders, including: the Bank for International Settlements (BIS); the central banks of Aruba, Barbados, Curacao, Jamaica, Ghana, Trinidad & Tobago and Samoa; the European Central Bank; and the Federal Reserve Banks of Atlanta, Chicago, and New York. Selected staff also participated in training coordinated by the Association of Certified Fraud Examiners (ACFE), the Global Alliance for Financial Inclusion (AFI), the IMF's Caribbean Regional Technical Assistance Centre (CARTAC), the Centre for Monetary Studies of Latin America and the Caribbean (CEMLA), the Caribbean Financial Action Task Force (CFATF), and the IMF. Thematic issues covered, related to cyber fraud, financial inclusion strategies, banking supervision, payment and settlement systems, monetary policy and central banking operations.

Through its Continuing Education Programme, the Bank supports staff who wish to pursue tertiary level education and professional certifications. In 2018, nine staff members received approvals for studies mainly related to AML, while one staff member was granted an In-Service Award scholarship to pursue a Master's degree in Actuarial Science.

COMMUNITY INVOLVEMENT AND OUTREACH

In 2018, the Bank continued its educational and career outreach to primary, secondary school and college-level students. This covered attendance at career fairs hosted by the C.V. Bethel Senior High School and C.C. Sweeting Senior High; and nine in-house presentations to visiting students on the History, Role and Importance of the Central Bank. Ten students from four high schools also received work experience exposure, as part of their respective school's development programmes.

Over the summer, 17 students were recruited to the Bank's 6-week long Summer Employment Programme and placed

in various Departments throughout the organisation. The Junior Professionals Summer Programme (JPSP) paralleled this process, for three students over an eight-week period. It is designed to attract and develop high-performing university students, about to enter their final year, specializing in studies that would satisfy the entry-level requirements for permanent positions within the Bank.

Community Relations

The Bank's wide range of community and civic activities are headlined by the art programme that spotlights and promotes development of local talent. The art programme for 2018 commenced in May, after the on-boarding of a new curator. The first exhibition, on 16th May, under the caption "*Happy Birthday Nettie*", was a retrospective of trailblazing hotelier and intuitive folk artist, Ms. Nettica Symonette, on the occasion of her birthday. Next followed the Sue Bennet William's After School Music and Art Classes (ASMAC) 25th Annual Exhibition; and exhibitions, which showcased works by the ISSA WYBE group, and new age artist Ms. Jodi Minnis, who presented her first showcasing of oil painting and photographs entitled "*INTIMACY*".

The Central Bank's third Annual Staff Art Exhibition, held in August, displayed the individual reproductions of staff from its "*Unwind, Teambuilding with Ceramics*" workshop held in June.

The Gallery year concluded with the awards night for the 35th Annual Competitions for the Open and High School Art categories held on 4th October and 8th November, respectively. In the Open Category, Mr. Richardo Barrett was awarded the winning prize for his piece "*The Dragon and Flamingo, Who's da boss?*" Ms. Jada Lightbourne of Queen's College, was the winner of the 2018 High School Competition with her piece entitled "*Conch n Grits*". The Best Sculpture Award was presented to Mr. Drenay Rahming of C.V. Bethel Senior High.

The Central Bank remains committed to the development of the visual arts in The Bahamas.

2018 FINANCIAL HIGHLIGHTS

The financial position of the Bank is influenced by external reserve developments, which are impacted by real sector performance, global (mainly US) interest rates and the Government's financing activities. In addition, changes in interest rates and demand for Government Securities, affect the level of income generated by the Bank's domestic debt holdings.

The Bank's financial statements for the year ended 31st December 2018, along with comparable figures for 2017, are presented on pages 47 to 120 of this report.

During 2018, the Bank's total assets contracted by \$111.8 million (5.9%) to \$1,772.0 million. Contributing to



this outturn was a \$221.1 million (15.6%) reduction in external assets—which comprised 67.5% of the total—to \$1,196.3 million, following a significant Government borrowing supported expansion in the prior year. A breakdown by category, showed that cash and deposit balances declined by \$322.8 million (46.2%) to \$375.8 million, while the Reserve Tranche with the IMF fell marginally by \$0.6 million (2.3%) to \$26.8 million. In a partial offset, the Bank’s total government securities portfolio grew by \$55.9 million (9.1%) to \$670.5 million; although the onboarding of a new investment manager during the year meant that the marketable securities portfolio went from a zero balance in 2017 to a total of \$101.8 million in the review year, while securities held to maturity, fell by \$45.9 million (7.5%) to a \$568.8 million. In addition, allocations from the IMF’s Special Drawing Rights (SDRs), increased by \$46.4 million (60.4%) to \$123.2 million.

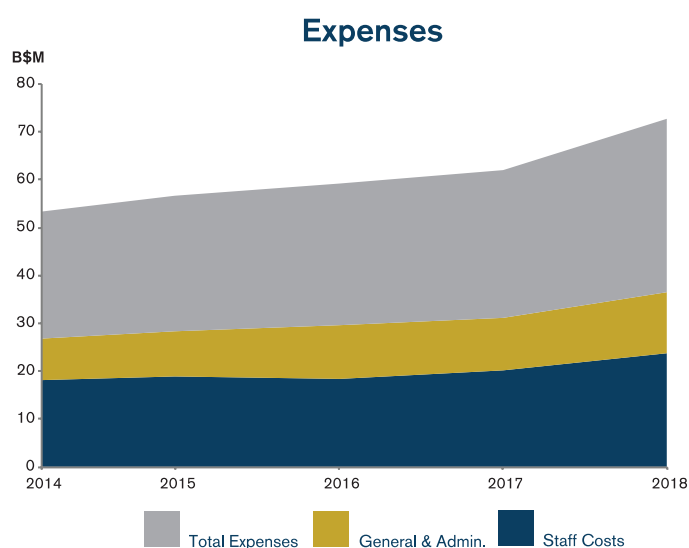
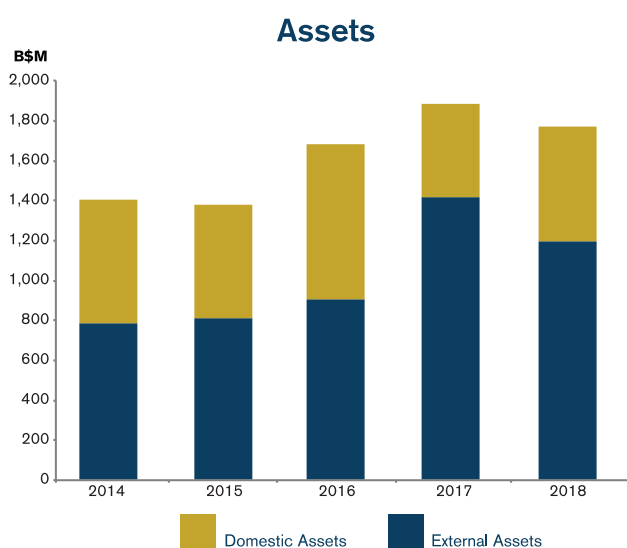
Total domestic assets of the Bank rose by \$109.4 million (23.5%) to \$575.7 million in 2018, led by an increase in T-bill holdings. Specifically, the Bank’s T-bill portfolio advanced by \$148.6 million to \$155.7 million, a reversal from a marked decline in the prior year, associated with a combination of maturities and sales to the commercial banks. Similarly, gains were recorded for retirement benefit assets and property plant & equipment, of \$2.2 million (39.1%) to \$7.9 million and \$1.5 million (12.3%) to \$13.8 million, respectively, while more muted increases were noted for cash on hand and Bridge Authority bonds. In contrast, the Bahamas Registered Stock (BRS) holdings fell by \$25.5 million (9.3%) to \$249.0 million and short-term Government debt contracted by \$15.0 million (11.1%) to \$120.4 million. The remaining domestic assets decreased by a combined \$2.5 million (8.0%) to \$28.4 million.

The Bank’s total demand liabilities fell by \$132.0 million (8.7%) to \$1,389.3 million, owing in large measure to a contraction in commercial banks’ deposits, by \$219.6 million (21.7%) to \$791.7 million, following an expansion in the prior year, when Government repaid outstanding advances. Conversely, deposits by the Bahamas Government and related agencies rose more than two-fold, by \$52.0 million to \$96.2 million, while currency in circulation grew by \$21.3 million (4.9%) to \$459.9 million. Similarly, accounts payable more than doubled to \$29.0 million from \$11.1 million, while the liabilities associated with the ICM edged-up by \$0.3 million (3.1%) to \$9.0 million.

The income generated by the Bank rose by \$9.8 million (23.5%) to \$51.5 million, supported by a rise in investment income—which accounted for a combined 84.7% of the total—by \$4.5 million (11.6%) to \$43.6 million. Specifically, buoyed by the rise in interest rates and invested assets, returns on foreign investments grew by \$12.0 million (63.6%), offsetting the \$7.4 million (38.7%) decrease in interest income on domestic investments. In addition, earnings from “other miscellaneous” sources firmed by \$1.1 million (18.6%) to \$6.9 million and interest on loans stabilized at \$1.0 million.

The Bank’s total expenses increased by \$1.8 million (5.7%) to \$32.8 million in 2018, mainly reflecting higher general and administrative spending, which grew by \$1.6 million (18.8%). Similarly, staffing costs edged-up by \$0.1 million (0.6%) to \$20.3 million, while depreciation expenses were relatively flat.

Against this backdrop, the Bank registered total comprehensive income of \$22.0 million for 2018, a gain of \$10.1 million (84.9%), relative to the prior year.







OUR ENVIRONMENT

INTERNATIONAL ECONOMIC DEVELOPMENTS

Despite the uncertainty caused by the on-going trade disputes between the United States and its major trading partners, and the partial US Government shutdown in the latter half of the year, indications are that the global economy maintained its modest pace of growth during 2018, expanding by approximately 3.1%, following a 3.7% gain in the previous year. Against this backdrop, employment conditions continued to gradually improve, while inflation stayed relatively subdued. Nevertheless, the major stock markets registered broad-based declines, reflecting in part uncertainties over the United Kingdom's "BREXIT" deal impasse. Given the softness in economic growth, most major central banks maintained their accommodative monetary policy stance. The exception was the Federal Reserve, which continued with its programme to "normalize" rates over the near-term.

Among the developed markets, real GDP growth in the United States quickened to 2.9% from 2.2% in 2017, attributed to gains in consumer spending, non-residential fixed investments, exports, federal Government spending and private inventory investments. In contrast, the pace of economic expansion in the United Kingdom slowed by 40 basis points to 1.4%, owing in large measure to declines in the construction, production and service sectors. Similarly, real output growth in the euro area softened by 60 basis points to an estimated 1.8%, as the region's two largest economies showed signs of weakness. In Asia, China's expansion tapered to 6.6% from 6.8% in the prior period, as trade tensions with the United States impacted industrial production and exports. In addition, output

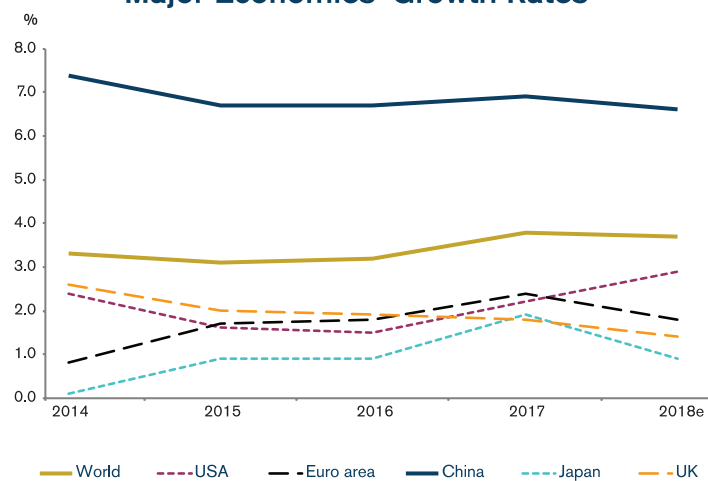
growth in Japan narrowed by 1.2 percentage points to 0.7%, explained by a slowdown in export growth, particularly to other Asian markets.

Labour market conditions in the major economies continued to improve during 2018. Specifically, in the United States, the unemployment rate declined by 50 basis points to 3.9%, with notable job gains occurring in the health care, food service, construction and manufacturing sectors. In addition, the United Kingdom's unemployment rate fell by 30 basis points to 4.1% during the year, as the number of employed persons grew by an estimated 444,000 over 2017. Despite the lacklustre economic performance, the jobless rate in the euro area decreased by 70 basis points to 7.9% at end-December—the lowest rate recorded since October 2008. Further, the major Asian economies continued to experience extremely tight labour market conditions, as the unemployment rates in Japan and China narrowed by 40 and 10 basis points to 2.4% and 4.9%, respectively.

Global inflationary pressures remained well contained in 2018, reflecting the dampened consumer demand conditions and the decline in international oil prices in the latter months of the year. Specifically, annual inflation in the United States decreased to 1.9% from 2.1% in the prior year, largely associated with a significant reduction in energy prices, mainly gasoline and fuel. Similarly, in Europe, inflation in the United Kingdom softened by 90 basis points to 2.1%, attributed to lower petrol and airfare prices, while the euro area's annual inflation rate firmed to 1.6% from 1.4%, owing mainly to higher services, energy, food and alcohol & tobacco costs. Inflation in Asia also remained relatively mild, as reductions in food, housing and transportation & communication costs, contributed to Japan's average annual price gains moderating to 0.3%, from 1.1% in the previous year. Further, China's annual inflation rate edged-up by 30 basis points to 1.9%, due in part to higher food costs.

Primary commodity prices recorded some strengthening in 2018, reflecting to some extent, supply constraints. In the energy market, average crude oil costs firmed by 31.6% to US\$72.36 per barrel over the year, underpinned by major exporters' efforts to limit production, as well as geopolitical concerns regarding major producers in the Middle East and South America. However, on a point-to-point basis, average costs contracted by 21.5% to US\$52.28 per barrel at end-December 2018, over the prior year. In the precious metal markets, the average price of silver

Major Economies' Growth Rates



fell by 9.1% to \$15.64 per troy ounce, while the average cost of gold stabilised at \$1,266.1 per troy ounce.

Buoyed by the sustained growth in the United States' market, along with an increase in investors' demand for relatively safe assets, the US dollar appreciated against most other major currencies in 2018. The dollar strengthened by 8.5% versus the Canadian dollar, to CAD\$1.36. Similarly, the dollar increased relative to the British Pound, by 6.0% to £0.78, the Chinese Yuan, by 5.7% to CNY6.88, the euro, by 4.7% to €0.87, and the Swiss Franc, by 0.8% to CHF 0.98. In contrast, the dollar weakened vis-à-vis the Japanese Yen, by 2.7% to ¥109.70.

Reflecting in part investors' concerns over the major economies' trade disputes, the lack of progress in the United Kingdom's "BREXIT" negotiations and the partial US Government shutdown at the end of the year, the major stock market indices recorded board-based contractions. Specifically, in the United States, the Dow Jones Industrial Average (DJIA) and the S&P 500 indices moved lower by 5.6% and 6.2%, respectively. Similarly, in Europe, declines were posted for Germany's DAX (18.3%), the United Kingdom's FTSE 100 (12.5%) and France's CAC 40 (11.0%). Asian bourses also registered losses, with China's SE Composite plunging by 24.6%, while Japan's Nikkei 225 index weakened by 12.1%.

Major countries recorded mixed outcomes in their external trade balances. In the United States, the goods and services deficit deteriorated by \$68.8 billion (12.4%) to an estimated \$621.0 billion—the highest since 2008. Notably, imports of mainly capital and consumer goods grew by 7.5%, outpacing the 6.3% advance in exports of largely industrial materials and capital products. In addition, the United Kingdom's trade deficit grew by £8.4 billion to a projected £32.3 billion, underpinned by a £7.2 billion rise in services imports, which overshadowed the £0.6 billion gain in service-based exports. Further, Japan registered an estimated trade deficit of ¥1.2 trillion—the first in three years—as imports rose by 9.7%, outweighing the 4.1% expansion in exports. The euro area's trade surplus narrowed by €40.7 billion (17.3%) to €194.2 billion, as the 6.2% growth in imports, eclipsed the 3.7% rise in exports, while China's surplus also fell sharply to US\$351.8 billion—the lowest since 2013—from US\$421.4 billion in 2017. This reflected a 15.8% increase in imports of primarily raw materials and commodities, which outstripped the 9.9% growth in exports of mainly finished metals.

Amid on-going trade tensions and concerns over a potential slowdown in global economic growth, most of the major central banks either maintained or enhanced their accommodative monetary policy stances in 2018. In Europe, the Bank of England retained its key policy rate

at 0.75% and sustained its £435.0 billion asset purchase programme. Similarly, the European Central Bank kept its key policy interest rates at historic lows and left its asset purchase programme at €30 billion per month. In Asia, the Bank of Japan kept its Government bond purchase programme unchanged, in order to retain 10-year yields at 0.0% and continued with its policy of applying a -0.1% short-term interest rate on balances in current accounts held by financial institutions at the Bank, in a bid to encourage lending. Further, the People's Bank of China maintained the reserve requirement ratio for both large and small-scale SFIs at 17.0% and 15.0%, respectively, and injected US\$74.0 billion into the banking system, in an effort to stimulate domestic demand. In contrast, faced with an environment of improving economic and labour market conditions, combined with relatively low inflation, the Federal Reserve continued to "normalize" its policy rate, by adjusting the target range for the federal funds rate upwards by an additional 100 basis points to 2.25%-2.50% by December.

OVERVIEW OF DOMESTIC ECONOMIC DEVELOPMENTS

Buoyed by gains in tourism sector output and support from foreign investment-led construction activity, preliminary indications are that the domestic economy sustained its growth in 2018, above the estimated 1.4% expansion of 2017. Employment continued to increase; although the jobless rate edged slightly higher, as the general rise in the labour force outpaced job gains. Domestic inflation rose modestly, reflecting the pass-through effects of the 4.5 percentage point hike in the VAT rate and growth in global oil prices in prior periods.

In the fiscal sector, the overall deficit decreased considerably in FY2017/18, as a capital-led reduction in aggregate expenditure, outpaced the falloff in total revenue. Similar trends were noted in the first half of FY2018/19, as the deficit narrowed, due to the VAT-related gain in revenues, which overshadowed the growth in total expenditure. Financing for the deficit was obtained primarily from domestic sources and comprised both long and short-term debt.

At end-December, the ratio of the Direct Charge on the Government to GDP was relatively stable at 58.9%, in comparison to the previous year. Further, the National Debt—inclusive of Government loan guarantees to the public sector—stood at an estimated 64.6% of GDP, down slightly from 64.8% at end-December 2017.

Monetary sector developments in 2018 featured a slowdown in the growth of bank liquidity and the banking system's net foreign assets, as domestic credit expansion contrasted with a decline in the deposit base. Amid this environment of heightened net foreign currency demand,



the stock of external reserves fell to an estimated 17.5 weeks of the current year's total merchandise imports, relative to 21.9 weeks in the prior period; although remaining well above the 12.0 weeks international benchmark.

Reflecting in part entities' intensified debt collection and loan restructuring efforts, and momentum from growth in the economy, banks' credit quality indicators improved during the year. Total net profits also rose, owing to lower provisioning for loan losses and higher fee-based income. In addition, the weighted average interest rate spread narrowed in 2018, as the decrease in the average loan rate, eclipsed the softening in the associated deposit rate.

In the external sector, the estimated current account deficit widened during 2018, vis-à-vis the prior year, due mainly to higher net income outflows, an import-led deterioration in the merchandise trade deficit and a rise in current transfer outflows, which eclipsed the improvement in the services account surplus. In addition, the surplus on the capital and financial account decreased sharply, owing primarily to a marked reduction in debt-financed inflows. Specifically, the public sector's transactions reversed to a net outflow, from a significant net receipt in the prior period, when Government issued its US\$750.0 million external bond. Private loan proceeds also contracted relative to 2017.

REAL SECTOR

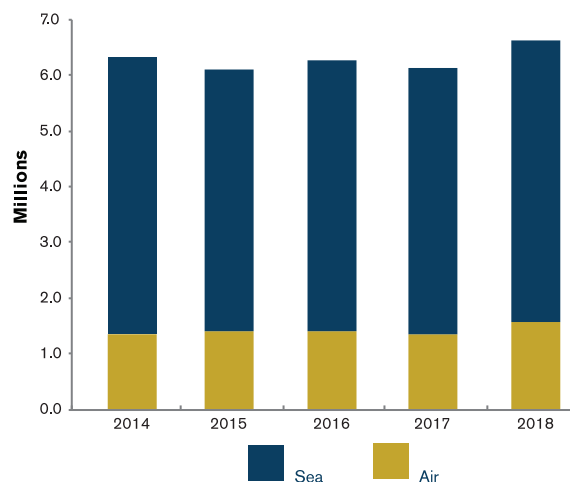
Tourism

Output in the tourism sector strengthened at a healthy, accelerated pace during 2018. Expanded airlift and demand matched the growth in high-end hotel room capacity, following the completion of the phased opening of the multi billion-dollar Baha Mar resort.

Data provided by the Ministry of Tourism, showed that total visitor arrivals firmed by 7.9% to 6.6 million in 2018 (See: Table 9). This was the strongest growth recorded in eight years, and a reversal from a 2.1% decline in the prior period. Air arrivals strengthened by 16.7% to 1.6 million—the highest pace of growth since 2008—reversing the prior year's 4.0% reduction. In addition, the high volume sea component—at 76.5% of the total—rose by 5.5% to 5.1 million, vis-à-vis a 1.5% decline a year earlier.

Disaggregated by first port of entry, overall visitors to New Providence grew by 4.1% to 3.8 million, exceeding the prior period's 1.2% gain. With the addition of high-end room capacity, air arrivals rebounded by 19.2%, from a 3.6% contraction last year. In a partial offset, sea traffic fell by 1.5%, compared to a 3.2% gain in 2017. Similarly, visitors to Grand Bahama increased by 9.1% to 0.7 million, vis-à-vis a 26.6% hurricane-related fall in the previous period. The outcome reflected gains in both sea and air passengers, by 9.6% and 5.4%, respectively, a reversal

Tourist Arrivals



from declines of 23.5% and 43.8% in the preceding year. Further, visitors to the Family Islands strengthened by 14.9% to 2.2 million, extending 2017's 2.6% expansion, buoyed by increases in both the air and sea segments, by 10.6% and 15.7%, following the prior period gains of 14.2% and 0.8%, respectively.

In line with the improvement in the stopover visitor segment, hotel sector indicators trended upwards during the review year, as preliminary data from a sample of large properties in New Providence and Paradise Island, revealed that total room revenue climbed by 34.0%, following a flat performance in 2017. Underpinning this outturn, total room nights sold rose by 28.0%, following a mere 1.0% uptick in the prior period, while the average occupancy rate firmed by 1.0 percentage point to 61.7%, in contrast to a 6.8 percentage point decrease in 2017. With the addition of medium to high-end rooms to the pool, the average daily room rate (ADR) rose by 4.7% to \$250.57, vis-à-vis a 0.8% decline in the prior year.

Construction

During the review year, activity in the construction sector was sustained by a number of small to medium-scale foreign investment-related projects. In addition, domestic private sector investment, as represented by residential and commercial building activity, showed modest signs of improvement.

As an indicator of domestic activity, total mortgage disbursements for new construction and repairs—as reported by commercial banks, insurance companies and the Bahamas Mortgage Corporation—increased by 11.6% to \$121.5 million in 2018, a turnaround from the prior period's 3.4% contraction. A breakdown of the components, showed that the dominant residential segment grew by 9.2% to \$111.8 million, reversing the previous year's 5.0% reduction. In addition, disbursements for the much smaller commercial component expanded by 50.6% to \$9.6 million, extending the year-earlier gain of 32.7%.

Nevertheless, domestic construction activity is still likely to be subdued over the near-term, as recorded mortgage commitments, an indicator for new buildings and repairs, remained divergent from disbursement trends. These declined in number by 22.2% to 397 and in value by 27.5% to \$41.8 million. The residential approvals—at 99.7% of the total—contracted in number, by 21.9% to 396 and in value, by 25.2% to \$41.8 million. In addition, commercial approvals fell in number to one from three, with a corresponding falloff in value to under \$0.1 million, from \$1.7 million in the prior period.

In terms of interest rates, the average financing cost for commercial credit declined by 2.4 percentage points to 6.26%, while the corresponding residential mortgage rate fell by 54 basis points to 7.04%.

Employment

Buoyed by the expansion in economic activity, employment conditions continued to gradually improve in 2018, benefiting from the on boarding of new staff at tourism facilities. According to the Department of Statistics' Labour Force Survey, the number of persons employed grew by 3.4% to 210,560. However, a 4.0% expansion in the labour force to 235,695 persons, related to the entrance of new job seekers and previously discouraged workers, resulted in the unemployment rate firming by 60 basis points, on an annual basis, to 10.7%, as at November 2018.

A breakdown by the major job markets, showed that the jobless rate in New Providence, which comprised the bulk—69.4% of the total labour force—rose by 40 basis points to 11.0%. In contrast, outcomes in the other major centres were more favourable, with the unemployment rates in Grand Bahama and Abaco decreasing by 20 basis points and 90 basis points to 11.9% and 7.7%, respectively. At the end of the period, the jobless rate for females stood at 11.3%, 1.3 percentage points higher than the corresponding rate for males.

Prices

Reflecting mainly the hike in the VAT rate and higher fuel costs, the Retail Price Index for The Bahamas firmed to 2.3% in 2018 from 1.5% in the prior period. Underlying this outturn, accretions to average costs accelerated for transport, by 2.6 percentage points to 4.6%; restaurant and hotels, by 1.8 percentage points to 4.1%; recreation & culture, by 1.7 percentage points to 2.9%; and health, by 1.4 percentage points to 2.1%. Further, following reductions in 2017, average prices firmed for food and non-alcoholic beverages, by 2.4%; miscellaneous goods and services, by 2.4% and furnishing, household equipment & routine household maintenance, by 0.9%. Moreover, the decrease in clothing & footwear, costs eased to 0.9%, from 1.2% a year earlier. In a modest

offset, the rate of inflation slowed for housing, water, gas electricity and “other” fuels—the most heavily weighted component—by 1.2 percentage points, to 2.4% and for alcoholic beverages, tobacco & narcotics, by 1.1 percentage points to 0.6%. In addition, average prices contracted for communication, by 1.4%, after firming by 3.4% in the previous year. Further, the average cost decline for education quickened to 0.6%.

Amid the rise in global oil prices, domestic energy costs firmed over 2018. Specifically, the average per gallon cost for both gasoline and diesel rose by 11.1% and 15.6% to \$4.74 and \$4.45, respectively, following gains of 8.9% and 10.6% in the previous year.

Table 9: Selected Economic Indicators (%)

	2016	2017	2018
Real GDP	(1.7)	1.4	2.3*
Unemployment Rate (Nov.)	11.6	10.1	10.7
Hotel Occupancy**	67.5	60.7	61.7
Total Arrivals	2.5	(2.1)	7.9
Mortgage Disbursements	(3.4)	(0.4)	11.6
Inflation	(0.4)	1.5	2.3
National Debt/GDP Ratio	59.6	64.8	64.6*

SOURCE: Central Bank of The Bahamas

*2018 GDP estimates derived from IMF's data.

** Data from The Bahamas Hotel and Tourism Association and The Ministry of Tourism for Nassau and Paradise Island properties.

FISCAL OPERATIONS

FY2017/18 Performance

Following the implementation of measures to strengthen revenue collections and curtail expenditure growth, Government's overall deficit contracted by \$254.4 million (38.0%) to \$414.9 million in FY2017/18 (See: Table 10); although remaining \$93.6 million (29.1%) above budgetary projections. The outturn largely reflected a capital-related reduction in total spending by \$280.9 million (10.3%) to \$2,449.0 million, which was \$11.4 million (0.5%) lower than the estimated expenditure. Conversely, total revenue decreased by \$26.5 million (1.3%) to \$2,034.1 million; approximately \$105.0 million (4.9%) below the budgeted amount.

Expenditure

Current spending—at 89.0% of total outlays—declined by \$159.2 million (6.8%) to \$2,180.4 million; approximately \$51.5 million (2.3%) less than budget estimates. In terms of the components, consumption outlays decreased by \$99.3 million (8.0%) to \$1,144.3 million, underpinned by a falloff in purchases of goods & services, which overshadowed higher personal emoluments.



Table 10: Fiscal Indicators (B\$ Millions)

	FY2014/15	FY2015/16	FY2016/17	FY2017/18	FY2018/19	
	Actual	Actual	Actual	Actual	Approved Estimates	Preliminary ¹ Outturn
Government Revenue	1,701.5	1,929.6	2,060.5	2,034.1	2,650.9	1,010.3
as % of GDP	15.4	16.3	17.2	16.3	20.4	7.8
Government Expenditure	2,083.5	2,240.0	2,729.9	2,449.0	2,888.5	1,184.6
as % of GDP	18.9	19.0	22.7	19.7	22.2	9.1
Surplus/(Deficit)	(382.0)	(310.4)	(669.3)	(414.9)	(237.6)	(174.3)
as % of GDP	(3.5)	(2.6)	(5.6)	(3.3)	(1.8)	(1.3)

SOURCE: Ministry of Finance
Compiled according to the IMF's Government Finance Statistics Format.
¹ July - December, 2018

Similarly, transfer payments decreased by \$60.0 million (5.5%) to \$1,036.1 million. This captured reduced general subsidies, including disbursements to the National Health Insurance (NHI) Scheme and the impact of the reallocation of several expenditure items to other accounts. In addition, transfers to public corporations and payments abroad to non-profit institutions contracted. Conversely, gains were recorded for transfers to households and interest payments on debt.

Capital outlays contracted sharply by almost one-third, (\$121.5 million) to \$268.7 million, but still exceeded the budget estimates by approximately \$37.9 million (16.4%). Underlying this outturn, spending on infrastructure was nearly halved to \$146.0 million from \$272.0 million in the prior fiscal year, as allocations returned to trend levels following the prior period's post-hurricane rebuilding efforts. In contrast, asset acquisitions rose by \$4.5 million (3.8%) to \$122.7 million, due mainly to spending on "other" assets, including equity acquired from a public corporation. However, both land purchases and other equity investments declined.

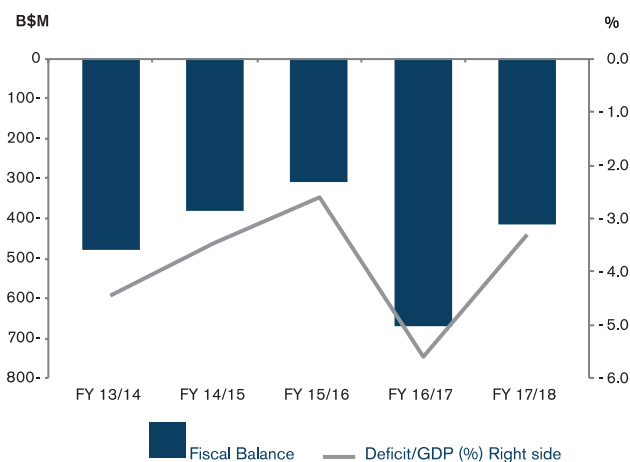
Revenue

Tax revenue—which comprised 90.0% of total collections—decreased by \$5.9 million (0.3%) to \$1,830.7 million, resulting in a \$110.9 million (5.7%) shortfall when compared to the budget estimates. An analysis of the sub-components, showed that receipts from taxes on international trade & transactions contracted by \$38.7 million (6.6%) to \$544.0 million, attributed mainly to declines in both excise and import taxes. Similarly, business and professional license fees declined by one-fifth to \$151.3 million, due primarily to a considerable decrease in income from general business license fees. Providing some offset, VAT receipts expanded by \$42.3 million (6.6%) to \$680.3 million. In addition, selective taxes on services improved by almost a third to \$37.2 million, as income from gaming taxes strengthened. Further, departure taxes and motor vehicle taxes also firmed, with more

moderate gains revealed for property taxes and non-trade stamp taxes.

Non-tax receipts decreased by \$23.3 million (10.4%) to \$200.6 million, but stood \$5.3 million (2.7%) higher than budget estimates. This outturn reflected in large measure a halving in income from dividend and other "miscellaneous" sources to \$24.9 million.

Fiscal Indicators



Financing

Financing for the deficit during FY2017/18, was obtained primarily from external sources, including a US\$750.0 million external bond. Additional resources included \$619.3 million in short-term bridging foreign currency loans, which were repaid from the bond proceeds. Domestic funding totalled \$617.7 million and comprised a combination of long-term bonds (\$492.0 million), Treasury bills (\$111.7 million) and loans & advances (\$14.0 million).

First Six Months of FY2018/19

During the first half of FY2018/19, the Government's overall deficit narrowed by \$79.6 million (31.3%) to \$174.3 million, vis-à-vis the same period of last year.



Contributing to this outturn was a VAT-related \$129.5 million (14.7%) improvement in total revenues to \$1,010.3 million, which outpaced the \$49.9 million (4.4%) rise in aggregate spending to \$1,184.6 million.

Revenue

Total tax receipts expanded by \$117.1 million (14.9%) to \$902.0 million, as VAT collections strengthened by \$81.2 million (25.5%) to \$399.5 million, reflecting the impact of the 4.5 percentage point upward adjustment in the rate to 12.0%. In addition, stamp taxes more than doubled to \$107.7 million, as the Government replaced the VAT on real estate sales with the tariff structure that predated the introduction of VAT. Property taxes and business & professional license fees also expanded. However, there were reductions for motor vehicle taxes, levies on international trade and transactions and gaming taxes.

Non-tax revenue moved higher by \$12.3 million (12.8%) to \$108.2 million, led by an increase in receipts from the sale of goods & services from an uptick in immigration fee collections. In addition, income from fines, forfeits & administrative fees, and revenue from the sale of Government land, rose modestly.

Expenditure

The growth in total expenditure reflected in large measure a \$94.0 million (9.4%) increase in current outlays to \$1,097.6 million. This outturn resulted in part from a \$44.4 million (25.0%) expansion in the use of goods & services to \$222.2 million, led by a notable rise in spending for special financial transactions and rent. Further, subsidies increased by \$28.1 million (20.0%) to \$168.7 million, as outlays for health sector activities expanded. Similarly, “other” payments grew by \$19.3 million (23.7%) to \$101.0 million, reflecting a gain in transfers to non-financial public enterprises, as contingent liabilities were settled. Also of note, expenses increased for public debt interest payments, pensions & gratuity payments and social assistance benefits. However, the wage bill declined.

In contrast, capital expenditure contracted by \$44.1 million (33.6%) to \$86.9 million, mainly attributed to a \$46.9 million (41.6%) reduction in the acquisition of non-financial assets to \$65.7 million, reflecting a significant decrease in outlays for “miscellaneous” assets. Spending for fixed assets also fell by \$1.4 million (2.5%) to \$54.0 million, owing to a decrease in acquisitions of “other” structures. In a modest offset, outlays for the use of goods & services firmed, while capital transfers increased incrementally.

Financing

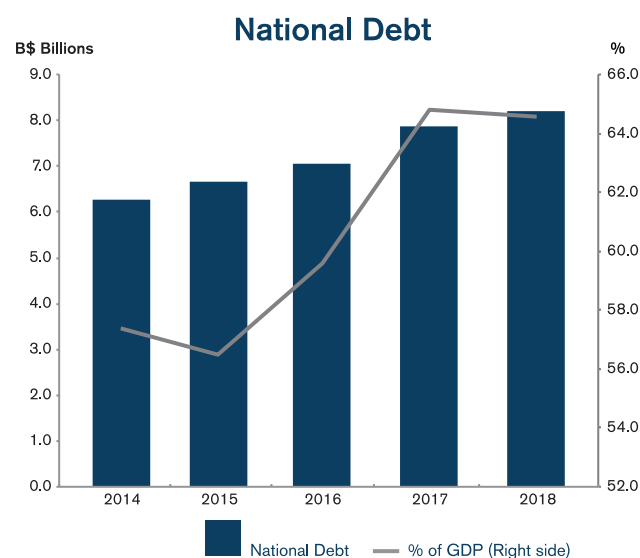
Budgetary financing for the six-month period, was obtained predominately from domestic sources, led by long-term bond issuances (\$314.0 million), loans and advances

(\$205.0 million) and Treasury bills & notes (\$153.9 million), while external debt drawdowns accounted for a mere \$4.5 million in funding. Debt repayments for the period totalled \$416.0 million, the majority of which (\$373.9 million), was utilized to repay Bahamian dollar obligations.

National Debt

During the calendar year, the Government’s Direct Charge rose by \$317.3 million (4.4%) to \$7,497.3 million, a slowdown from the previous period’s \$864.5 million (13.7%) expansion. Consequently, the ratio of the Direct Charge to GDP fell by 10 basis points to approximately 58.9% (See: Table 11). Bahamian Dollar denominated debt—at 65.4% of the total—expanded by \$341.2 million (7.5%) to \$4,905.1 million. In contrast, foreign currency claims fell by \$24.0 million (0.9%) to \$2,592.2 million. An analysis by holder, showed that commercial banks held the largest share of Bahamian dollar debt (40.4%), followed by the private sector (36.8%) and public corporations (12.0%). The Central Bank and other local financial institutions accounted for smaller shares of the outstanding debt at 10.6% and 0.2%, respectively.

Government’s contingent liabilities increased by \$18.1 million (2.6%) to \$722.3 million, mainly reflecting a rise in the guaranteed obligations of two utilities. As a result, the National Debt, which includes contingent liabilities, grew by \$335.3 million (4.3%) to \$8,219.6 million, a significant slowdown from the \$834.1 million (11.8%) expansion recorded in the prior year. Similarly, the National Debt to GDP ratio decreased by 20 basis points to an estimated 64.6%, following a 5.2 percentage point increase to 64.8% in 2017.



Foreign Currency Debt

During 2018, public sector foreign currency debt declined by \$10.7 million (0.3%) to \$3,473.5 million, as



new drawings reverted to trend levels of \$220.0 million, following a sharp increase to \$1,347.1 million in the prior year, related to external bond and loan drawdowns. Similarly, amortization payments fell by \$328.8 million (60.3%) to \$216.9 million. The Government's debt obligations—which constituted 74.6% of the aggregate—declined by \$24.0 million (0.9%) to \$2,592.2 million, while the public corporations' segment, rose by \$13.3 million (1.5%) to \$881.3 million.

Foreign currency debt service payments contracted by \$260.7 million (37.3%) to \$437.8 million, owing in large measure to a \$357.4 million (61.0%) reduction in payments by Government to \$228.6 million. In contrast, outlays by public corporations rose by \$96.7 million (85.9%) to \$209.2 million. Adjusting for refinanced principal, the 2018 servicing level was \$393.7 million, compared to \$248.5 million in the prior year. The 2018 debt service as a share of exports was estimated at 9.2%, compared to 6.5% in 2017 on an adjusted basis. For the Government, debt service relative to revenue reached 10.6%, vis-à-vis an adjusted 6.6% in 2017.

A breakdown by creditor profile, showed that private capital markets held the majority of foreign currency debt (47.5%), followed by non-resident investors (32.5%); inclusive of international financial institutions and insurance firms. The residual shares were held by banks (9.6%), multilateral institutions (8.1%) and bilateral agencies (2.3%). Meanwhile, the average maturity of foreign currency debt shortened to 9.3 years, compared to 11.0 years in the prior year. By currency, the bulk of the debt (85.3%) was denominated in US dollars, while the Swiss Franc, euro, and Chinese Yuan accounted for significantly smaller proportions of 6.6%, 5.9% and 2.3%, respectively.

Public Sector F/C Debt Service

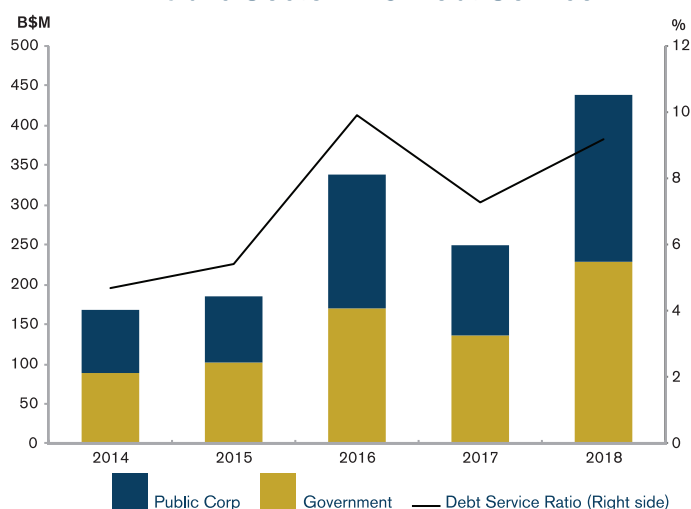


Table 11: Debt Indicators

	2016p	2017p	2018p
(B\$ Millions)			
A. Total F/C Debt	2,646.8	3,484.2	3,473.5
i) External Debt	2,373.0	3,233.9	3,170.2
ii) Internal F/C Debt	273.8	250.4	303.4
B. National Debt	7,050.2	7,884.3	8,219.6
i) Direct Charge	6,315.6	7,180.1	7,497.3
Percent of GDP			
A. Total F/C Debt	22.4	28.6	27.3
i) External Debt	20.0	26.6	24.9
ii) Internal F/C Debt	2.3	2.1	2.4
B. National Debt	59.6	64.8	64.6
i) Direct Charge	53.3	59.0	58.9

SOURCE: Treasury Accounts, Treasury Statistical Printouts and Public Corporations' Quarterly Reports
*2018 GDP estimates derived from the IMF's data

MONEY, CREDIT AND INTEREST RATES

Monetary Sector

Monetary developments during 2018 culminated in a decline in bank liquidity, as an expansion in domestic credit contrasted with a reduction in the deposit base. These trends underscored the public sector's switch to domestic financing, and a corresponding net usage of foreign currency resources, which also largely explained the contraction in external reserves. Commercial banks' credit quality indicators improved during the year, as the ameliorating economic environment, on-going debt restructuring and loan write-offs, reduced overall loan delinquencies. Banks' profitability also strengthened, attributed to lower provisioning for loan losses and a rise in fee-based income. In terms of interest rates, the average spread narrowed, as the decline in the average lending rate, outweighed the softening in the average deposit rate.

Liquidity

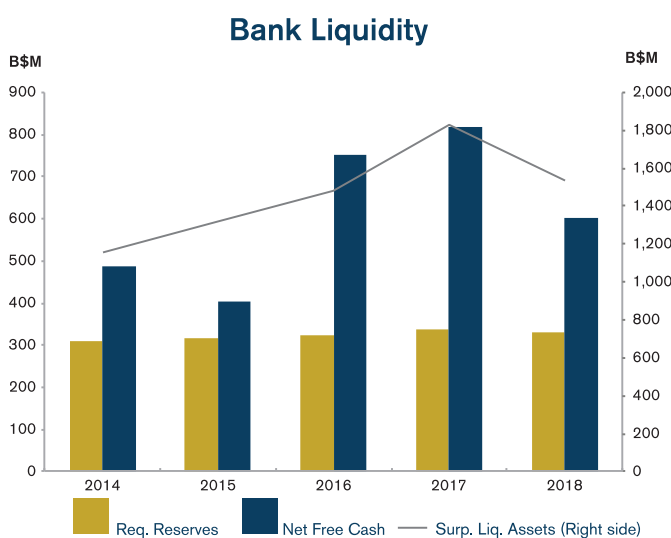
Banking sector liquidity remained at elevated levels in 2018, with average net free cash balances—a narrow measure of liquidity—growing by \$93.8 million (12.7%) to \$835.1 million, in comparison to an \$89.4 million (13.7%) build-up in the previous year. An analysis of the yearly trends, indicated that balances rose steadily during the first five months of the year, reaching a peak of \$1,036.6 million in May, before declining over the remaining months to close the year at \$602.5 million. This equated to a lower 9.3% of Bahamian dollar deposits, compared with 12.3% in the prior year.



Excess liquid assets, a broader measure of liquidity—which includes holdings of Government securities—averaged \$1,826.4 million per month, 13.9% higher than over the previous year and peaked at \$1,995.2 million in April, before decreasing over the remainder of the year. At year-end, overall liquidity stood at \$1,533.2 million, for a contraction of 16.1%, a reversal from last year’s 23.4% expansion. Further, the value of excess liquid assets exceeded the statutory requirement by 137.4%, down from 161.9% in 2017.

Money Supply

The overall money supply (M3), contracted by \$55.7 million (0.8%) in 2018, vis-à-vis the prior year’s \$107.2 million (1.6%) gain, for an aggregate stock of \$6,981.6 million. A breakdown of the various components, revealed that the expansion in narrow money (M1), slowed to \$75.3 million (2.8%), from \$193.4 million (7.9%) in 2017. Gains in demand deposits softened to \$57.4 million (2.4%), from \$181.4 million (8.3%), outweighing quickened growth in currency in active circulation to \$17.9 million (6.1%), from \$12.1 million (4.3%) in the previous period.



Broad money (M2) decreased by \$53.9 million (0.8%), a turnaround from a \$140.7 million (2.1%) growth in the prior year, associated with a private sector-led reduction in fixed deposits. Specifically, the falloff in fixed balances accelerated to \$185.6 million (6.8%), from \$128.4 million (4.5%) in the preceding year. In addition, gains in savings deposits slackened to \$56.3 million (4.1%), from \$75.6 million (5.8%) in 2017. Conversely, the decrease in foreign currency deposits slowed to \$1.7 million (0.6%), from \$33.5 million (10.9%) in the previous period, as the falloff in private sector placements was offset by growth in public sector deposits.

As a proportion of the overall money stock (M3), Bahamian dollar fixed deposits comprised the largest

share (36.6%), followed by demand and savings balances at 34.6% and 20.4%, respectively. In addition, currency in active circulation and foreign currency deposits represented significantly smaller shares, of 4.4% and 3.9%, respectively.

Domestic Credit

The growth in domestic banks’ credit in 2018, was attributed to lending to the Government, reflecting increases in loans & advances, as well as holdings of Treasury bills. Conversely, credit to the private sector contracted; although a slowdown from the prior year’s reduction.

Following a \$290.1 million (3.2%) falloff in the prior period, total domestic credit grew by \$80.1 million (0.9%) in 2018, with 95.5% of the total denominated in Bahamian dollars. Specifically, net claims on the Government rose by \$156.3 million (6.6%), a reversal from a \$168.4 million (6.6%) reduction in 2017 (See: Table 12). In contrast, the expansion in claims on the rest of the public sector slowed to \$13.3 million (2.8%), from \$66.2 million (16.3%) in the prior period.

The reduction in credit to the private sector continued, but at a moderated pace of \$89.5 million (1.5%), compared to \$187.9 million (3.0%) in 2017, when one entity swapped a portion of its NPLs for debt securities issued by a Government-owned SPV. The dominant personal loans category, representing 79.2% of the total, declined further by \$124.0 million (2.4%), vis-à-vis \$62.4 million (1.2%) in the prior year. More muted reductions occurred for agriculture (\$3.0 million), “miscellaneous” purposes (\$1.9 million), tourism (\$1.4 million), entertainment & catering (\$0.3 million) and mining & quarrying (\$0.3 million). In contrast, credit gained for distribution (\$15.9 million), manufacturing (\$6.3 million), professional & other services (\$5.9 million), transport (\$5.4 million) and construction (\$4.3 million); with more muted increases occurring for credit to private financial institutions (\$2.1 million) and fisheries (\$0.7 million).

A further disaggregation of the personal loan category, showed that the decline in consumer credit widened to \$105.1 million (4.5%), from \$49.1 million (2.1%) in the previous year, while the falloff in housing loans steadied at \$13.3 million (0.5%) and the contraction in overdrafts extended to \$5.4 million (9.1%).

A disaggregation of consumer credit, revealed significant net repayments for debt consolidation (\$28.9 million), “miscellaneous” purposes (\$23.1 million), private cars (\$17.7 million), land purchases (\$13.7 million), and home improvement (\$11.9 million), while more modest declines occurred for education and credit cards of \$10.0 million and \$5.8 million, respectively. Conversely, net lending increased for travel by \$5.4 million, medical by \$0.7 million and taxis & rented cars by \$0.2 million.



Table 12: Flow of Bank Credit (B\$ Millions)

Destination	Outstanding	Absolute		Outstanding
	as at 2016	2017	Changes 2018	as at 2018
Destination				
Government (net)	2,551.4	(168.4)	156.3	2,539.2
Central Bank	716.6	(326.5)	80.5	470.6
Domestic Banks	1,834.8	158.1	75.7	2,068.6
Rest of Public Sector	406.3	66.3	13.3	485.8
Central Bank	8.9	(0.9)	(0.3)	7.7
Domestic Banks	397.4	67.1	13.6	478.1
Private Sector	6,170.8	(187.9)	(89.5)	5,893.4
Domestic Banks	6,170.8	(187.9)	(89.5)	5,893.4
Consumer	2,371.4	(49.1)	(105.1)	2,217.2
Mortgages	2,716.9	(12.4)	(13.9)	2,690.6
Other Loans	1,082.5	(126.4)	29.5	985.6
Financing				
Liabilities (Net of Government)	6,930.1	107.2	(55.6)	6,981.7
Currency	280.5	12.1	17.9	310.5
Total Deposit liabilities	6,649.6	95.2	(73.5)	6,671.2
Demand deposits	2,426.0	153.4	57.9	2,637.3
Savings deposits	1,315.2	75.3	53.6	1,444.0
Fixed Deposits	2,908.4	(133.5)	(185.0)	2,589.9
International reserves	904.0	513.5	(221.1)	1,196.3
Other net external liabilities	(225.4)	(39.6)	7.5	(257.4)
Capital and surplus	2,760.2	110.0	(86.3)	2,783.9
Other (net)	116.8	(14.7)	(10.4)	91.7

SOURCE: Central Bank of The Bahamas

Interest Rates

The weighted average interest rate spread on domestic banks' loans and deposits narrowed by 25 basis points to 10.50% during 2018. This reflected a 41 basis point decline in the average loan rate to 11.34%, which outpaced the 16 basis point decrease in the associated deposit rate to 0.84%.

On the lending side, declines were recorded for the average overdraft rate by 48 basis points to 10.15%, residential mortgages, by 35 basis points to 5.41%, and consumer loans, by 12 basis points to 13.49%. Conversely, the average rate for commercial mortgages rose by 72 basis points to 7.59%.

In the context of the persistent liquidity overhang, interest rates across the majority of the deposit categories contracted. Specifically, the average rate paid on savings balances fell by 9 basis points to 0.64%, while the average range on fixed maturities eased to 0.60%-1.26%,

from 0.64%-1.61% in the prior period. Further, the average rate on demand balances remained unchanged at 0.27%.

In other interest rate developments, the average 90-day T-bill rate decreased by 14 basis points to 1.69%, while the Central Bank's Discount rate and the commercial banks' Prime rate remained at 4.00% and 4.25%, respectively.

Net Foreign Assets

The banking system's net foreign assets contracted by \$214.5 million (18.6%) to \$938.1 million in 2018, a turnaround from the \$474.0 million (69.9%) growth in the prior year, while commercial banks' net foreign liabilities declined by \$7.5 million (2.8%) to \$257.4 million and the Central Bank's external reserves decreased by \$221.1 million (15.6%) to \$1,196.3 million. The latter contrasted with a \$513.5 million (56.8%) accumulation a year earlier, which included the receipt of net proceeds from the Government's external borrowings.

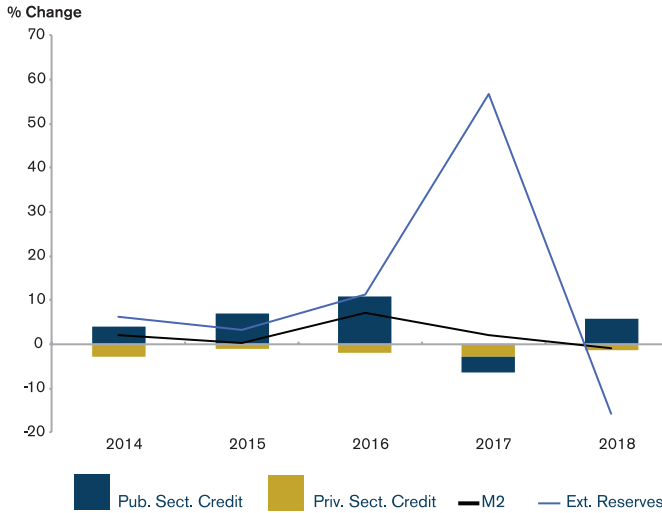
An analysis of the monthly foreign reserve trends, revealed a net accumulation in January, from proceeds of the Government's US\$50.0 million equivalent external loan. A steady rise followed, to a peak of \$1,694.2 million in April, in line with seasonal net tourism inflows. Seasonally elevated foreign currency demand in the latter half of the year, pushed balances to a low of \$1,196.3 million at end-December. Still,

the average monthly balances were further improved by \$415.5 million (39.6%), compared to a gain of \$88.1 million (9.2%) in the prior year.

An analysis of the underlying foreign currency transactions, revealed that the Central Bank recorded a net sale of \$296.5 million, vis-à-vis a net purchase of \$487.6 million in 2017, as the \$908.9 million contraction in total purchases to \$1,127.8 million, outweighed the \$124.9 million falloff in gross sales to \$1,424.3 million. Specifically, the Bank's transactions with the Government reversed to a net sale of \$43.2 million, from a net purchase of \$724.1 million a year earlier. Further, the Bank's net sale to public corporations—primarily for fuel imports and debt service—grew by \$105.4 million (34.4%) to \$412.0 million, partly reflecting higher global oil prices. However, the net purchase from commercial banks more than doubled to \$158.7 million, from \$70.1 million in 2017.



Monetary Developments



At end-December, the stock of reserves stood at an estimated 17.5 weeks of the current year’s total merchandise imports, relative to 21.9 weeks in the previous year and above the international benchmark of 12.0 weeks. After accounting for the statutory requirement to maintain reserves equivalent to 50% of the Bank’s demand liabilities, “useable” reserves fell by \$148.7 million to \$521.6 million.

BANKING SECTOR PERFORMANCE

Credit Quality

Banks’ credit quality indicators have been on an improving trend over the last five years, assisted by entities’ sales of NPLs, aggressive collection and debt restructuring efforts, as well as the modest growth in the economy. During 2018, total arrears decreased by \$75.0 million (8.5%) to \$809.8 million—the lowest level since 2008—following the previous year’s \$125.8 million (12.5%) contraction. Correspondingly, the ratio of arrears to total private sector loans contracted by 1.2 percentage points to 14.3%, after a 1.7 percentage point decline in 2017.

The decrease in total delinquencies was led by NPLs, which fell by \$50.5 million (8.9%) to \$517.0 million, albeit lower than the sell-off induced \$161.6 million (22.2%) reduction in 2017. As a result, the ratio of NPLs to total private sector loans narrowed further by 78 basis points to 9.1%. Similarly, the short-term (31-90 day) component, contracted by \$24.5 million (7.7%) to \$292.9 million, a turnaround from the prior year’s increase of \$35.8 million (12.7%), with the attendant ratio declining by 37 basis points to 5.2% of total private sector loans.

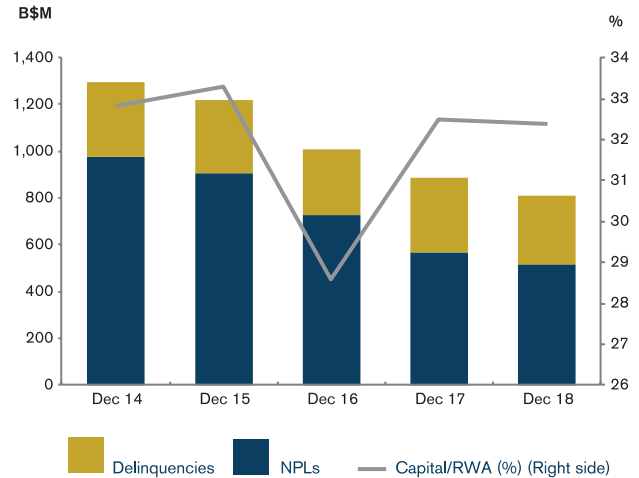
An analysis by loan type, showed that mortgage arrears fell by \$34.7 million (6.5%) to \$499.4 million, vis-à-vis a \$13.1 million (2.5%) increase in the prior year. The associated ratio to corresponding loans declined by 1.2 percentage points to 18.8%. Similarly, consumer loan

delinquencies, which were almost unchanged in the prior year, decreased by \$29.0 million (11.2%) to \$229.3 million, while the relevant loan ratio fell by 79 basis points to 10.2%. In addition, commercial delinquencies decreased by a lesser \$11.3 million (12.2%) to \$81.1 million, after the prior period’s \$139.6 million (60.2%) contraction, when one entity sold a portion of its non-performing portfolio to a non-bank firm. As a consequence, the corresponding delinquency ratio narrowed again, by 2.4 percentage points to 10.4%.

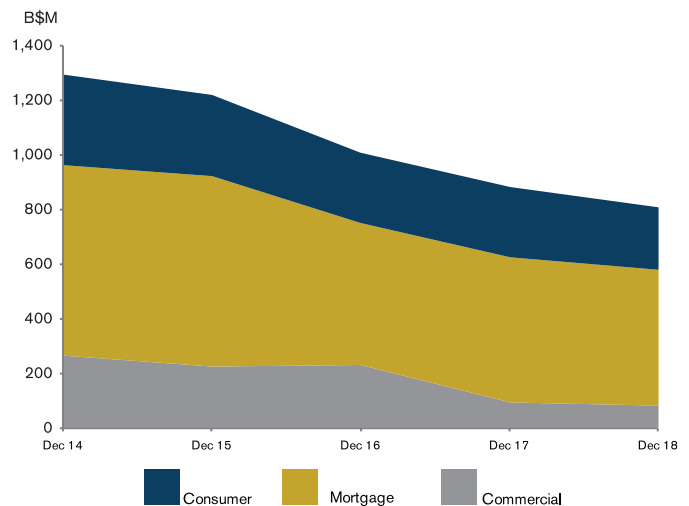
Capital Adequacy and Provisions

Banks maintained their conservative stance with regard to capital, and at end-2018, the ratio of capital to total risk weighted assets stood 20 basis points lower at 32.3% (See: Table 13). This remained well above the prudentially prescribed target and trigger ratios of 17.0% and 14.0%, respectively. Further, banks increased their provisions for bad debts, by \$14.9 million (3.5%) to \$438.5 million, a turnaround from 2017’s contraction of

Private Sector Loan Arrears



Private Sector Arrears by Loan Category



\$91.2 million (17.7%). As a result, the ratio of provisions to total private sector loans firmed by 18 basis points to 7.0%. Similarly, the ratios of provisions to both NPLs and arrears advanced by 10.2 and 6.3 percentage points, to 84.8% and 54.2%, respectively.

Meanwhile, in line with conservative practices, commercial banks also wrote-off a total of \$125.3 million in delinquent loans, while recoveries amounted to \$21.0 million.

Bank Profitability

Domestic banks' profitability improved during the twelve months to September 2018—the latest data available—owing in large measure to higher fee income and lower provisioning for bad debts. In particular, the net interest margin contracted by \$14.7 million (2.8%) to \$518.7 million, as interest receipts fell by \$25.6 million (4.3%) to \$577.3 million, outstripping the \$11.0 million (15.8%) decrease in interest expense to \$58.6 million. In a slight offset, earnings from commission & foreign exchange services increased by \$1.2 million (4.5%) to \$29.2 million; however, the gross earnings margin declined by \$13.4 million (2.4%) to \$547.8 million, extending the \$5.6 million (1.0%) falloff in 2017.

Banks' operating costs grew by 3.0% (\$11.0 million) to \$374.1 million, attributed to an increase in non-staff outlays—including professional services, Government fees and maintenance—by 5.4% (\$9.7 million). Similarly, staffing costs rose slightly by 0.9% (\$1.4 million), while occupancy expenditures edged-down by 0.3%. Accordingly, the net earnings margin contracted by 12.3% (\$24.4 million) to \$173.7 million, following a

5.2% (\$10.8 million) reduction in 2017. However, banks' results from their “non-core” operations reversed significantly to a \$46.5 million net profit, vis-à-vis a net loss of \$8.5 million in the previous year. Underlying this performance, provisions for bad debts and depreciation costs, decreased by 32.0% (\$40.1 million) and 10.3% (\$1.6 million). In addition, income from “other” fee-based services grew by 10.0% (\$13.3 million), reflecting in part the increase in rates on several categories of fees, as well as the introduction of new charges over the year by some entities.

Given these developments, the banking sector's net profits grew by \$30.5 million (16.1%) to \$220.3 million, a reversal from a decline of \$21.7 million (10.2%) during the corresponding period of 2017.

Corresponding to these trends, the gross earnings margin ratio fell by 21 basis points to 5.31%, as the 22 basis point decline in the interest margin ratio to 5.03%, overshadowed the 1 basis point increase in the commission & forex income ratio to 0.28%. Further, the net earnings margin decreased by 27 basis points to 1.68%, owing in part to a 5 basis point increase in the operational cost ratio to 3.63%. In contrast, after accounting for positive contributions from fee income and lower bad debt costs, the net income ratio strengthened by 27 basis points to 2.14%.

CAPITAL MARKET DEVELOPMENTS

Domestic capital market activity reflected in part the improvement in economic conditions during the review year. The volume of shares traded on the Bahamas International Securities Exchange (BISX), increased sharply by 66.1% to 8.5 million; although the corresponding value declined by 6.2% to \$41.8 million. Reflecting overall valuation gains, the BISX All Share Index—a market capitalization weighted index—rose by 2.2% to 2,109.45 points, lower than the 6.5% growth in 2017. Further, the market capitalization of listed firms expanded slightly by 0.9% to \$5.4 billion, after a 6.4% increase in 2017. During the year, the number of publicly traded securities on the exchange fell by one to 51, and comprised 19 common shares, 13 preference shares and 19 debt tranches.

INTERNATIONAL TRADE AND PAYMENTS

Preliminary data on the external account for 2018, showed that the current account deficit deteriorated by an estimated \$190.3 million (12.6%) to \$1,699.0 million (See: Table 14), underpinned by a sharp increase in net income outflows, and a widening in the merchandise trade deficit. In addition, the capital and financial account surplus narrowed significantly by \$814.6 million (52.3%) to \$744.2 million, mainly reflecting a reversal in net public sector transactions to a net repayment from a net external bond-related receipt in 2017.

Table 13: Commercial Banks' Financial Soundness Indicators¹

	2016	2017	2018
Capital Adequacy			
Regulatory capital/RWAs*	28.6	32.5	32.3
Regulatory Tier 1 capital/RWAs*	27.0	29.0	31.2
Asset Quality			
NPLs/private sector loans	12.3	9.9	9.1
NPLs to capital	28.1	21.0	21.0
Earnings & Profitability			
Return on assets	2.0	1.8	2.3
Return on equity	7.9	6.8	8.5
Liquidity			
Liquid assets to total domestic assets	25.9	29.0	26.8

SOURCE: Central Bank of The Bahamas
 *Risk Weighted Assets
¹ Year-end data



The estimated merchandise trade deficit grew by \$114.0 million (4.5%) to \$2,651.9 million. In particular, a \$198.8 million (6.4%) rise in imports to \$3,307.2 million, outstripped the \$84.8 million (14.9%) growth in exports. Specifically, net payments for fuel purchases rose by \$186.9 million (32.8%) to \$757.2 million, linked to higher import volumes. In a modest offset, net non-oil imports declined by \$16.8 million (0.8%) to \$2,107.3 million. As to imported fuel costs, the average price per barrel of jet fuel increased by 34.4% to \$90.53; propane, by 19.2% to \$55.34; motor gas, by 13.0% to \$89.03; gas oil, by 12.8% to \$75.31 and aviation fuel, by 10.4% to \$155.47.

The estimated surplus on the services account strengthened by \$272.0 million (18.8%) to \$1,717.2 million. This outturn reflected an expansion in net tourism receipts by \$328.0 million (12.5%) to \$2,953.1 million, reflecting the surge in stopover visitors, while the winding-down of the Baha Mar project contributed to net construction service outflows falling sharply by \$75.4 million (63.5%) to \$43.3 million. Further, net inflows from offshore companies' local expenses moved higher by \$4.7 million (3.6%) to \$134.8 million and net outflows for royalty and license fees edged-down, by \$3.9 million (27.5%) to \$10.3 million. In a modest offset, net payments for transportation services expanded by \$65.0 million (16.9%) to \$448.4 million, due to a reversal in port & airport charges to a net disbursement, vis-a-vis a net inflow in the prior year, combined with higher net outflows for passenger and air & sea freight services. In addition, net payments for other "miscellaneous" services rose by \$43.9 million (7.6%) to \$617.8 million. Further, net outflows for insurance services firmed by \$39.9 million (35.0%) to \$153.9 million. Meanwhile, the net outflows for Government services contracted by \$8.8 million (8.3%) to \$97.0 million.

The estimated deficit on the income account nearly doubled to \$693.2 million from \$360.7 million in 2017, largely attributed to an above trend rate of private sector profit repatriations. Notably, net investment income outflows widened to \$635.3 million from \$321.9 million, with private sector interest and dividend payments more than doubled at \$499.0 million, as repatriations by both commercial banks and non-bank entities, expanded by \$148.2 million and \$103.7 million, respectively. Similarly, net outflows for the official transactions' category grew by \$61.5 million (82.2%) to \$136.3 million, explained by the two-thirds (\$61.7 million) rise in the Government's net interest payments, as opposed to nearly stable earnings on the Central Bank's net investments. In addition, the net

TABLE 14: Balance of Payments Summary (B\$ Millions)

	2016p	2017p	2018p
I. CURRENT ACCOUNT	(710.8)	(1,508.6)	(1,699.0)
i) Merchandise Trade (net)	(2,150.2)	(2,537.9)	(2,651.9)
Exports	481.4	570.5	655.3
Imports	2,631.6	3,108.4	3,307.2
of which: Oil	433.6	570.3	757.2
ii) Services (net)	1,564.3	1,445.2	1,717.2
Travel	2,745.3	2,625.2	2,953.1
Other	(1,181.0)	(1,180.0)	(1,235.9)
iii) Income (net)	(439.9)	(360.7)	(693.2)
iv) Current Transfers (net)	315.1	(55.2)	(71.1)
II. CAPITAL AND FINANCIAL ACCOUNT	778.0	1,558.8	744.2
i) Capital Account (Transfers)	(13.8)	(26.1)	(20.7)
ii) Financial Account	791.8	1,584.9	764.9
of which: Direct Investment	390.4	461.1	486.0
III. NET ERRORS AND OMISSIONS	24.8	459.9	737.0
IV. CHANGES IN EXTERNAL RESERVES¹	(92.0)	(510.0)	217.7

SOURCE: Central Bank of The Bahamas
¹() = increase.

repatriation of employee earnings moved higher by \$19.1 million (49.3%) to \$57.8 million.

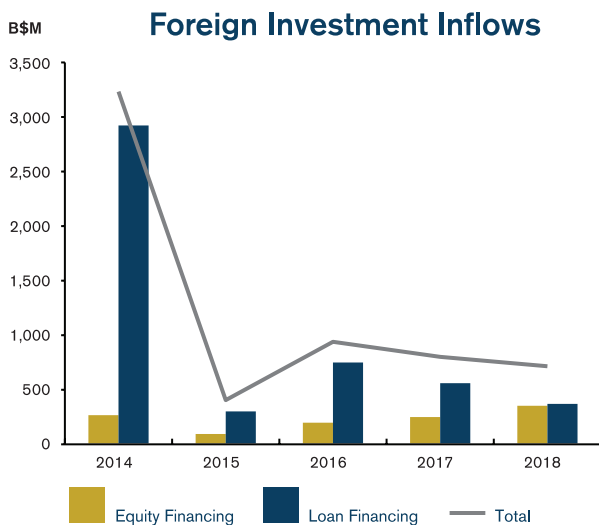
Net current transfer outflows expanded by \$15.9 million (28.8%) to \$71.1 million. This was due in large measure to a reversal in private, non-remittance related transfers to a \$19.6 million net outflow, from a \$54.4 million net receipt a year earlier, when residual proceeds from the 2016 hurricane were received. In contrast, net workers' remittance payments contracted by \$41.8 million (18.7%) to \$181.8 million, while the Government's net receipts grew by \$16.4 million (14.4%) to \$130.4 million.

The decrease in the surplus on the capital and financial account was primarily due to a sharp reduction in "other", mostly debt financing inflows, by \$1,006.4 million to \$290.6 million. This reflected a reversal in net public sector debt transactions to a net repayment of \$49.8 million, vis-à-vis a net receipt of \$804.9 million in 2017, when Government issued its external bond. Further, private sector loan-based financing inflows decreased by \$108.0 million to \$337.8 million and domestic banks' net short-term inflows narrowed by \$20.8 million to \$5.6 million. In a modest offset, net direct investment inflows rose by \$24.9 million to \$486.0 million, amid a \$48.8 million increase in net equity investment inflows to \$271.0 million,



which outweighed the \$23.9 million decline in net inflows from real estate transactions to \$215.0 million. Similarly, residents' net portfolio outflows under the Bahamian Depository Receipt (BDR) programme, decreased by \$5.0 million to \$11.7 million, while capital transfers lessened by \$5.5 million to \$20.7 million, due solely to a reduction in the migrant component.

After making the relevant adjustments for net errors and omissions, the overall balance—which is equivalent to the change in the Central Bank's external reserves—recorded a deficit of \$217.7 million, a reversal from a \$510.0 million surplus in 2017.



Projected improvement in the sector's credit quality indicators should also persist, reflecting in part heightened debt collection efforts and loan restructuring initiatives. Banks are also projected to maintain robust levels of capital, thereby mitigating any risk to financial stability.

The external reserves outlook is also modestly positive, with balances expected to remain above international benchmarks. However, outcomes remain contingent on the balance of supply and demand factors in the foreign exchange earning sectors, with robust tourism receipts, balanced against the on-going outflow needs for public sector debt service, fuel imports and rising private sector imports. Given more liberal exchange control policies, private portfolio investment needs are also likely to be elevated.

Although the overall assessment is relatively positive, downside risks remain, including the potential adverse effects on global growth from the on-going trade dispute between the United States and its major trading partners. In addition, the high level of bank liquidity could have an adverse impact on external reserves, if utilized to fund excessive consumer credit growth over the short-term. In this context, the Central Bank's gradual reduction in its holdings of Government debt, is targeted at reducing this liquidity overhang. The implementation of the credit bureau, should also provide context for more sustainable lending practices over the medium-term.

DOMESTIC ECONOMIC OUTLOOK FOR 2019

The Bahamian economy should expand further during 2019, with improved economic conditions in key external markets and increased high-end hotel capacity, accommodating projected growth in tourism. Moreover, sustained activity in the construction sector is expected to benefit from both new and on-going foreign investment projects throughout the archipelago. Given this outlook, employment conditions should continue to gradually improve; while inflation is likely to stay contained, despite the continued marginal pass-through from the VAT rate increase.

On the fiscal front, efforts to reduce the deficit and the related debt indicators, will continue to depend heavily on the effectiveness of measures to strengthen revenue administration; with the enacted fiscal responsibility legislation providing a governance framework to strengthen expenditure controls.

The monetary sector is forecasted to feature sustained highly liquidity levels, as banks maintain their conservative lending policies and households deleverage further.





THE CENTRAL BANK OF THE BAHAMAS

Financial Statements
for the Year Ended December 31, 2018





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REPORT OF THE AUDITORS TO THE BOARD OR DIRECTORS OF THE CENTRAL BANK OF THE BAHAMAS

Opinion

We have audited the accompanying financial statements of The Central Bank of the Bahamas (the "Bank"), which comprise the statement of financial position as at 31 December 2018, and the statement of comprehensive income, statement of changes in equity and reserve and statement of cash flows for the year then ended and notes to the financial statements, including a summary of significant accounting policies.

In our opinion, the accompanying financial statements present fairly, in all material respects, the financial position of The Central Bank of the Bahamas as at 31 December 2018 and its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards (IFRSs) and the Central Bank of The Bahamas Act, 2000 as amended.

Basis for Opinion

We conducted our audit in accordance with International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the Auditors' Responsibilities for the Audit of the Financial Statements section of our report. We are independent of the Bank in accordance with the International Ethics Standards Board for Accountants' Code of Ethics for Professional Accountants (IESBA Code) together with the ethical requirements that are relevant to our audit of the financial statements in The Bahamas, and we have fulfilled our other ethical responsibilities in accordance with these requirements and the IESBA Code. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Key Audit Matter

Key audit matters are those matters that, in the auditors' professional judgment, were of most significance in the audit of the financial statements as at 31 December 2018. These matters were addressed in the context of the audit of the financial statements as a whole, and in forming the auditors' opinion thereon, and the auditor does not provide a separate opinion on these matters. We have determined the matters described below to be the key audit matters to be communicated in our report.

Classification of Bahamas Government Registered Stocks

The Bank assessed the classification and measurement of its financial assets upon the adoption of IFRS 9. Based on the Bank's assessment, the Bahamas Government Registered Stocks previously classified as loans and receivables and measured at amortised cost have been classified as financial assets at fair value through other comprehensive income (FVOCI). As per transitional provision of IFRS 9, the comparative periods have not been restated and the effect of the remeasurement of Bahamas Government Registered Stocks in the amount of \$2,277,217 was presented as an adjustment to the beginning General Reserve balance as shown on the statement of changes in equity and reserves.

Other Matter

The financial statements of the Bank for the year ended 31 December 2017 were audited by other auditors whose report dated 13 April 2018, expressed an unqualified opinion on these financial statements.



Other Information

Management is responsible for the other information. The other information comprises of information presented in The Central Bank of the Bahamas' complete Annual Report 2018 (but does not include the financial statements and our auditors' report thereon).

Our opinion on the financial statements does not cover the other information and we do not express any form of assurance conclusion thereon.

In connection with our audit, of the financial statements, our responsibility is to read the other information identified above and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

Responsibilities of Management and Those Charged with Governance for the Financial Statements

Management is responsible for the preparation and fair presentation of the financial statements in accordance with IFRSs and the Central Bank of the Bahamas Act, 2000, as amended, and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, management is responsible for assessing the Bank's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the Bank or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Bank's financial reporting process.

Auditors' Responsibilities for the Audit of the Financial Statements

Our objectives are to obtain reasonable assurance about whether the financial statements, as a whole are free from material misstatement whether due to fraud or error, and to issue an auditors' report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

A further description of the auditors' responsibilities for the audit of the financial statements is located in an Appendix to this report. This description forms part of our auditors' report.

The engagement partner on the audit resulting in this independent auditors' report is Clifford Culmer.

**Chartered Accountants
Nassau Bahamas
5 April 2019**



APPENDIX TO THE AUDITORS' REPORT

Detailed Description of Our Responsibilities

As part of an audit in accordance with ISAs, we exercise professional judgment and maintain professional skepticism throughout the audit. We also:

- Identify and assess the risk of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Bank's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Bank's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Bank to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide those charged with governance with a statement that we have complied with relevant ethical requirements regarding independence, and to communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

From the matters communicated with those charged with governance, we determine those matters that were of most significance in the audit of the financial statements of the current period and are therefore the key audit matters. We describe these matters in our auditors' report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

The Central Bank of The Bahamas
(Established under the laws of the Commonwealth of The Bahamas)

Statement of Financial Position
As at December 31, 2018
(Expressed in Bahamian dollars)

	Note	2018 \$	2017 \$
ASSETS			
EXTERNAL ASSETS			
Cash and deposits with banks	5 3	375,760,906	698,535,734
Foreign Government Securities	6	568,768,827	614,662,080
Marketable Securities	7	101,761,419	-
International Monetary Fund:	8		
Bahamas Reserve Tranche		26,821,805	27,464,827
Special drawing rights – holdings		123,190,711	76,784,418
		<u>1,196,303,668</u>	<u>1,417,447,059</u>
DOMESTIC ASSETS			
Cash on hand	3	37,828	32,190
Bahamas Government Treasury bills	15	155,736,831	7,169,543
Advances to Bahamas Government	10	120,367,448	135,360,600
Bahamas Government Registered Stocks	11	249,036,288	274,511,585
Loans to Bahamas Development Bank	12	2,509,158	2,759,867
Bahamas Development Bank bonds	9	4,049,834	4,091,984
Bridge Authority bonds	13	493,487	491,351
Clifton Heritage Authority bonds	14	638,069	638,069
Currency inventory		10,827,049	11,582,274
Retirement benefit asset – Employees	30	7,921,180	5,692,780
Receivables and other assets		10,331,083	11,751,054
Property, plant and equipment	4	13,761,612	12,255,430
		<u>575,709,867</u>	<u>466,336,727</u>
TOTAL ASSETS		<u>1,772,013,535</u>	<u>1,883,783,786</u>

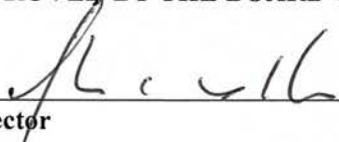
The accompanying notes are an integral part of these financial statements.



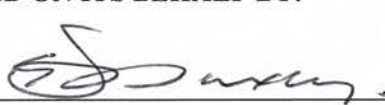
The Central Bank of The Bahamas
Statement of Financial Position (Continued)
As at December 31, 2018
(Expressed in Bahamian dollars)

	Note	2018 \$	2017 \$
LIABILITIES			
DEMAND LIABILITIES			
Notes in circulation	16	430,888,855	411,120,706
Coins in circulation		28,970,923	27,396,830
Deposits by commercial banks	17	791,668,258	1,011,246,639
Deposits by Bahamas Government and Bahamas Government agencies		96,155,504	44,152,152
Deposits by international agencies	18	255,302	255,217
Accounts payable and other liabilities		29,002,444	11,110,160
Investment Currency Market payable		9,007,273	8,736,314
Health insurance subsidy benefit for retirees	31	3,190,276	3,112,941
Retirement benefit liability - Governors and Deputy Governors	32	144,362	4,188,009
		<u>1,389,283,197</u>	<u>1,521,318,968</u>
OTHER LIABILITIES			
International Monetary Fund: Special drawing rights allocation	8	173,347,897	177,399,213
		<u>173,347,897</u>	<u>177,399,213</u>
TOTAL LIABILITIES		<u>1,562,631,094</u>	<u>1,698,718,181</u>
EQUITY AND RESERVES			
Authorised and fully paid capital	19	3,000,000	3,000,000
Exchange equalisation account	19	10,811,110	10,143,882
Contingency reserve		750,000	750,000
Other reserves		10,389,415	10,389,415
Building fund	19	30,680,403	20,680,403
Fair Value Reserve	19	1,369,020	-
General reserve	19	152,382,493	140,101,905
		<u>209,382,441</u>	<u>185,065,605</u>
TOTAL EQUITY AND RESERVES		<u>209,382,441</u>	<u>185,065,605</u>
TOTAL LIABILITIES, EQUITY AND RESERVES		<u>1,772,013,535</u>	<u>1,883,783,786</u>

APPROVED BY THE BOARD OF DIRECTORS AND SIGNED ON ITS BEHALF BY:



 Director



 Director

5 April 2019

 Date

The accompanying notes are an integral part of these financial statements.



The Central Bank of The Bahamas

Statement of Comprehensive Income For the Year Ended December 31, 2018 (Expressed in Bahamian dollars)

	Note	2018 \$	2017 \$
INCOME			
Interest income:	20		
Foreign investments		30,850,307	18,857,304
Domestic investments		11,744,171	19,157,402
Loans		1,003,968	1,050,841
		<u>43,598,446</u>	<u>39,065,547</u>
Interest expense		<u>(1,640,107)</u>	<u>(921,557)</u>
Net interest income		41,958,339	38,143,990
Net foreign exchange gain/(loss)		667,228	(4,052,958)
Net trading gains on Bahamas Government			
Registered Stocks		155,436	1,781,256
Realised gain on Marketable Securities		12,238	-
Unrealised gain Marketable Securities		1,553,425	-
Gain on sale of Foreign Government Securities		238,719	-
Other income		<u>6,887,037</u>	<u>5,809,081</u>
Total income		<u>51,472,422</u>	<u>41,681,369</u>
EXPENSES			
Staff costs	21	20,256,324	20,142,188
General and administrative	21	10,382,028	8,741,643
Depreciation	4	<u>2,177,020</u>	<u>2,163,178</u>
Total expenses		<u>32,815,372</u>	<u>31,047,009</u>
NET INCOME		<u>18,657,050</u>	<u>10,634,360</u>
OTHER COMPREHENSIVE INCOME			
<i>Items that will or may be reclassified to net income</i>			
Valuation gain on Bahamas Government			
Registered Stock		1,369,020	-
<i>Items that will not be reclassified to net income</i>			
Actuarial gain on defined benefit pension			
plan for employees		1,812,912	1,301,634
Actuarial gain/(loss) on group insurance subsidy		46,364	(52,920)
Actuarial gain on defined pension			
plan benefit for Governors and Deputy Governors		<u>154,273</u>	<u>39,417</u>
Total other comprehensive income		<u>3,382,569</u>	<u>1,288,131</u>
TOTAL COMPREHENSIVE INCOME		<u>22,039,619</u>	<u>11,922,491</u>

The accompanying notes are an integral part of these financial statements.



The Central Bank of The Bahamas
Statement of Changes in Equity and Reserves
For the Year Ended December 31, 2018
(Expressed in Bahamian dollars)

	Authorised & Fully Paid Capital \$	Exchange Equalisation Account \$	Contingency Reserve \$	Other Reserves \$	Building Fund \$	General Reserve \$	Total \$
Balance at January 1, 2017	3,000,000	14,225,479	750,000	10,389,415	10,680,403	134,097,817	173,143,114
Comprehensive income							
Net income	-	-	-	-	-	10,634,360	10,634,360
<i>Other comprehensive income</i>							
Allocation to building fund (Note 19)	-	-	-	-	10,000,000	(10,000,000)	-
Appropriation of foreign exchange gain (Note 2 (b) ii)	-	(4,081,597)	-	-	-	4,081,597	-
Actuarial gain on defined benefit pension plan for employees (Note 30)	-	-	-	-	-	1,301,634	1,301,634
Actuarial gain on health insurance subsidy benefit for retirees (Note 31)	-	-	-	-	-	(52,290)	(52,290)
Actuarial gain on defined benefit pension plan for Governors and Deputy Governors (Note 32)	-	-	-	-	-	39,417	39,417
Total comprehensive income	-	(4,081,597)	-	-	10,000,000	6,004,088	11,922,491
Balance at December 31, 2017	3,000,000	10,143,882	750,000	10,389,415	20,680,403	140,101,905	185,065,605

The accompanying notes are an integral part of these financial statements.



The Central Bank of The Bahamas
Statement of Changes in Equity and Reserves (Continued)
For the Year Ended December 31, 2018
(Expressed in Bahamian dollars)

	Authorised & Fully Paid Capital \$	Exchange Equalisation Account \$	Contingency Reserve \$	Other Reserve \$	Building Fund \$	Fair Value Reserve \$	General Reserve \$	Total \$
Balance at January 1, 2018	3,000,000	10,143,882	750,000	10,389,415	20,680,403	-	140,101,905	185,065,605
Adjustment on transitional application of IFRS 9 (Note 11)	-	-	-	-	-	-	2,277,217	2,277,217
Balance at January 1, 2018, as restated	3,000,000	10,143,882	750,000	10,389,415	20,680,403	-	142,379,122	187,342,822
Comprehensive income								
Net income	-	-	-	-	-	-	18,657,050	18,657,050
<i>Other comprehensive income</i>								
Allocation to building fund	-	-	-	-	10,000,000	-	(10,000,000)	-
Appropriation of foreign exchange gain (Note 2 (b) ii)	-	667,228	-	-	-	-	(667,228)	-
Valuation gain on Bahamas Government Registered Stocks	-	-	-	-	-	1,369,020	-	1,369,020
Actuarial gain on defined benefit pension plan for employees (Note 30)	-	-	-	-	-	-	1,812,912	1,812,912
Actuarial gain on health insurance subsidy benefit for retirees (Note 31)	-	-	-	-	-	-	46,364	46,364
Actuarial gain on defined benefit pension plan for Governors and Deputy Governors (note 32)	-	-	-	-	-	-	154,273	154,273
Total comprehensive income	-	667,228	-	-	10,000,000	1,369,020	10,003,371	22,039,619
Balance at December 31, 2018	3,000,000	10,811,110	750,000	10,389,415	30,680,403	1,369,020	152,382,493	209,382,441

The accompanying notes are an integral part of these financial statements.



The Central Bank of The Bahamas

Statement of Cash Flows For the Year Ended December 31, 2018 (Expressed in Bahamian dollars)

	Note	2018 \$	2017 \$
CASH FLOWS FROM OPERATING ACTIVITIES:			
Net income		18,657,050	10,634,360
Adjustments for non-cash items:			
Discount earned on marketable securities - net	6	(987,749)	(1,031,764)
Premium earned on BGRS - net		-	(15,300)
Depreciation	4	2,177,020	2,163,178
Loss on disposal of property, plant and equipment - net	4	269,110	83,573
Interest income		(42,610,697)	(38,018,483)
Gain on sale of Marketable Securities		(238,719)	-
Unrealised gain on Marketable Securities		(1,553,425)	-
Interest expense		1,640,107	921,557
(Increase)/Decrease in operating assets			
Currency inventory		755,225	(3,558,430)
International Monetary Fund		2,437,951	(5,495,996)
Deposits with banks – with original contractual maturities greater than three months		(25,000,000)	(100,000,000)
Retirement benefit asset		(415,488)	(327,371)
Receivables and other assets		1,419,971	55,864
Increase/(Decrease) in operating liabilities			
Notes in circulation		19,768,149	11,045,545
Coins in circulation		1,574,093	1,748,806
Deposits by commercial banks		(219,578,381)	144,927,100
Deposits by Bahamas Government and Bahamas Government agencies		52,003,352	16,292,234
Deposits by international agencies		85	(57)
Investment Currency Market payable		270,959	953,514
Health insurance subsidy benefit for retirees		123,699	108,189
Retirement benefit liability – Governors and Deputy Governors		(3,889,374)	(50,025)
Accounts payable and other liabilities		17,892,284	5,160,639
International Monetary Fund		(4,148,272)	9,928,493
Net cash (used in)/from operating activities		(179,433,050)	55,525,626
CASH FLOWS FROM INVESTING ACTIVITIES:			
Purchase of foreign government securities	6	(111,676,227)	(69,919,317)
Proceeds from maturities/redemptions of foreign government securities	6	158,000,000	7,000,000
Purchase of marketable securities	7	(106,566,727)	-
Proceeds from sales of marketable securities	7	7,070,246	-
Purchase of property, plant and equipment	4	(3,952,893)	(1,640,246)
Proceeds from sale of property, plant and equipment		581	20,474
Purchase of Bridge Authority bonds	12	(2,100)	(5,300)
Purchase of Bahamas Government Registered Stocks	11	(8,295,060)	(54,163,200)
Proceeds on sales/maturities of Bahamas Government Registered Stocks	11	37,250,092	150,909,400
Repayments of loans by Bahamas Development Bank	12	250,000	800,000
Purchase of Bahamas Government Treasury bills	15	(642,975,803)	(1,095,088,890)
Proceeds from the sales/maturities of Bahamas Government Treasury bills	15	494,570,346	1,311,294,313
Advances to Bahamas Government	10	(30,000,000)	-
Repayments from Bahamas Government	10	45,000,000	-
Interest received		40,316,441	39,360,989
Net cash (used in)/from investing activities		(121,011,104)	288,568,223



The Central Bank of The Bahamas

Statement of Cash Flows For the Year Ended December 31, 2018 (Expressed in Bahamian dollars) (Continued)

	Note	2018 \$	2017 \$
CASH FLOWS FROM FINANCING ACTIVITIES:			
Purchase of SDRs	7	(48,060,684)	-
Interest paid		<u>(1,543,151)</u>	<u>(769,879)</u>
Net cash used in financing activities		<u>(49,603,835)</u>	<u>(769,879)</u>
NET (DECREASE)/INCREASE IN CASH AND CASH EQUIVALENTS		(350,047,989)	343,323,970
CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR		<u>542,827,395</u>	<u>199,503,425</u>
CASH AND CASH EQUIVALENTS AT END OF YEAR	3	<u>192,779,406</u>	<u>542,827,395</u>

The accompanying notes are an integral part of these financial statements.



The Central Bank of The Bahamas

Notes to the Financial Statements December 31, 2018

1. General Information

The Central Bank of The Bahamas (the “Bank”) is established as a body corporate, under the Central Bank of The Bahamas Act, and was continued under the Central Bank of The Bahamas Act, 2000 (the “Act”). The Act establishes the structure, governance and funding of the Bank. The Bank’s principal business is the provision of Central Banking facilities for the Commonwealth of The Bahamas. In accordance with the Act, it is the duty of the Bank to promote and maintain monetary stability and credit and balance of payments conditions conducive to the orderly development of the Bahamian economy; in collaboration with the financial institutions, to promote and maintain adequate banking services and high standards of conduct and management therein; and to advise the Minister on any matter of financial or monetary nature referred by him to the Bank for its advice. Its main place of business is located at Frederick Street, Nassau, Bahamas.

2. Summary of Significant Accounting Policies

The principal accounting policies adopted in the preparation of the financial statements are set out below. These policies have been consistently applied to all the years presented, unless otherwise stated.

(a) Basis of preparation

i) Compliance with IFRS

The financial statements are prepared in accordance with International Financial Reporting Standards (IFRS).

ii) Historical cost convention

The financial statements have been prepared under the historical cost convention except for financial instruments that are measured at fair value, as disclosed in the accounting policies below. Historical cost is generally based on the fair value of consideration given in exchange for assets.

The preparation of financial statements in conformity with IFRS requires the use of certain critical accounting estimates. It also requires management to exercise judgment in the process of applying the Bank’s accounting policies. Estimates and judgments are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. Actual results could differ from those estimates. The areas involving a higher degree of judgment or complexity, or areas where assumptions and estimates are significant to the financial statements, are disclosed in Notes 2 (d), (m), 29, 30 and 31.



The Central Bank of The Bahamas

Notes to the Financial Statements

December 31, 2018

(Continued)

2. Summary of Significant Accounting Policies (Continued)

(a) Basis of preparation (continued)

iii) New standards, amendments and interpretations adopted by the Bank

Standards and amendments and interpretations to published standards that became effective for the Bank's financial year beginning on January 1, 2018 were either not relevant or not significant to the Bank's operations and accordingly did not have a material impact on the Bank's accounting policies or financial statements.

IFRS 9 Financial instruments

IFRS 9 *Financial Instruments* (IFRS 9) addresses the classification, measurement and recognition of financial assets and financial liabilities, and replaces the guidance in IAS 39 *Financial Instruments: Recognition and Measurement* (IAS 39) that relates to the classification and measurement of financial instruments. IFRS 9 retains but simplifies the mixed measurement model and establishes three primary measurement categories for financial assets: amortised cost, fair value through profit or loss and fair value through other comprehensive income. The determination is made at initial recognition, and the basis of classification depends on the Bank's business model for managing its financial assets and the contractual cash flow characteristics of the financial asset. In addition, IFRS 9 requires the impairment of financial assets to be calculated using an expected credit loss model that replaces the incurred loss impairment model required by IAS 39.

For financial liabilities, there are no changes to classification and measurement, except for the recognition of changes in own credit risk in other comprehensive income for financial liabilities designated at fair value through profit or loss.

The Bank assessed the classification and measurement of its financial assets upon the adoption of IFRS 9. The classification of financial assets under IFRS 9 was generally based on the business model in which the financial assets were managed and its contractual cash flow characteristics. Based on the Bank's assessment, the Bahamas Government Registered Stocks previously classified as loans and receivables and measured at amortised cost have been classified as financial assets at fair value through other comprehensive income (FVOCI). As per transitional provision of IFRS 9, the comparative periods have not been restated and the effect of the remeasurement of Bahamas Government Registered Stocks was presented as an adjustment to the beginning General Reserve balance.



The Central Bank of The Bahamas

Notes to the Financial Statements

December 31, 2018

(Continued)

2. Summary of Significant Accounting Policies (Continued)

(a) Basis of preparation (continued)

IFRS 9 Financial instruments (continued)

Adoption of IFRS 9 did not have a significant impact on the Bank's other financial assets and financial liabilities.

IFRS 9 replaces the 'incurred loss' model in IAS 39 with an 'expected credit loss' (ECL) model. The new impairment model applies to financial assets measured at amortised cost and debt instruments at FVOCI. There were no significant 12-month ECL on financial assets since these consist primarily of cash and securities issued or guaranteed by Foreign Governments or the Bahamas Government.

IFRS 15 Revenue from contracts with customers

IFRS 15 *Revenue from Contracts with Customers* (IFRS 15) deals with revenue recognition and establishes principles for reporting useful information to users of financial statements about the nature, amount, timing and uncertainty of revenue and cash flows arising from an entity's contracts with its customers. Revenue is recognised when a customer obtains control of a good or service and thus has the ability to direct the use and obtain the benefits from the good or service. The standard is effective for annual periods beginning on or after January 1, 2018, and replaced IAS 18 *Revenue* and IAS 11 *Construction Contracts* and related interpretations.

Adoption of IFRS 15 did not have a significant impact on the Bank's financial statements as the Bank's main revenue pertains to interest income and gains from its financial assets.

iv) New standards, amendments and interpretations not yet adopted by the Bank

With the exception of the following standards, amendments or interpretations, the application of new standards and amendments and interpretations to existing standards that have been published but are not yet effective are not expected to have a material impact on the Bank's accounting policies or financial statements in the financial period of initial adoption.



The Central Bank of The Bahamas

Notes to the Financial Statements

December 31, 2018

(Continued)

2. Summary of Significant Accounting Policies (Continued)

(a) Basis of preparation (continued)

IFRS 16 Leases

IFRS 16 “Leases” set out the principles for the recognition, measurement, presentation and disclosure of leases. All leases result in the lessee obtaining the right to use an asset at the start of the lease and, if lease payments are made over time, also obtaining financing. Accordingly, IFRS 16 eliminates the classification of leases as either operating lease or finance lease as is required by IAS 17 and, instead, introduces a single lessee accounting model. Lessees will be required to recognise: (a) assets and liabilities for all leases with a term of more than 12 months, unless the underlying asset is of low value; and (b) depreciation of lease assets separately from interest on lease liabilities in the income statement. IFRS 16 substantially carries forward the lessor accounting requirements in IAS 17. Accordingly, a lessor continues to classify its leases as operating leases or finance leases, and to account for those two types of leases differently.

The Bank has not yet assessed the full impact of adopting IFRS 16, which is effective for annual periods on or after January 1, 2019.

(b) Foreign currency translation

i) Functional and presentation currency

Items included in the financial statements are measured using the currency of the primary economic environment in which the Bank operates. The financial statements are presented in Bahamian dollars (B\$), which is the Bank’s functional and presentation currency.



The Central Bank of The Bahamas

Notes to the Financial Statements

December 31, 2018

(Continued)

2. Summary of Significant Accounting Policies (continued)

(b) Foreign currency translation (continued)

ii) Transactions and balances

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the date of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at year-end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognised as a part of net income in the statement of comprehensive income. Translation differences on monetary financial assets and liabilities carried at fair value are part of the fair value gain and losses. The net foreign exchange gain/(loss) in the Bank's assets and liabilities arising from movements in foreign exchange rates is included in the statement of comprehensive income and, in accordance with Sections 32(2)(a) and 32(2)(b) of the Act, the gain/(loss) is appropriated from the general reserve to an exchange equalisation account within equity and reserves.

(c) Financial assets

Financial assets represent a contractual right to receive cash or another financial asset or to exchange financial assets or financial liabilities with another entity under conditions favorable to the Bank.

The Bank classifies its financial assets in the following categories: fair value through profit or loss (FVTPL), fair value through other comprehensive income (FVOCI) and financial assets held at amortised cost. The Bank classifies its financial assets based on both the Bank's business model for managing those financial assets and the contractual cash flow characteristics of the financial assets. Financial assets are not reclassified subsequent to their initial recognition unless the Bank were to change its business model for managing financial assets, in which case all affected financial assets would be reclassified on the first day of the first reporting period following the change in the business model.

i) Financial assets at fair value through profit or loss

This category has two sub-categories: financial assets held for trading, and those designated at fair value through profit or loss at inception. A financial asset is classified into the financial assets at fair value through profit or loss category at inception if acquired principally for the purpose of selling in the short term, if it forms part of a portfolio of financial assets in which there is evidence of short-term profit-taking, or if so designated by management. Any financial assets not held in one of the other business models are measured at fair value through profit and loss.



The Central Bank of The Bahamas

Notes to the Financial Statements

December 31, 2018

(Continued)

2. Summary of Significant Accounting Policies (continued)

(c) Financial assets (continued)

i) Financial assets at fair value through profit or loss (continued)

Financial assets designated as at fair value through profit or loss at inception are those that are managed and whose performance is evaluated on a fair value basis, and are intended to be held for an indefinite period of time but may be sold in response to needs for liquidity or changes in interest rates, exchange rates or equity prices. Information about these financial assets is provided internally on a fair value basis to the Investment Management Committee. Financial assets classified as at fair value through profit or loss consist of Marketable Securities which are managed by a third party and the International Monetary Fund asset balances which have been so designated by management.

ii) Financial assets at fair value through other comprehensive income

Financial assets are classified and measured at fair value through other comprehensive income once held in a business model whose objective is to collect contractual cash flows and selling financial assets. These financial assets are non-derivatives that are either classified in this business model or are not classified as financial assets at amortised cost or financial assets at fair value through profit or loss. Changes in the carrying amount of these monetary financial assets relating to foreign currency rates and interest income calculated using the effective interest method are recognised in the statement of comprehensive income. Other changes in the carrying amount of financial assets at fair value through other comprehensive income are recognised through other comprehensive income.

Bahamas Government Treasury bills and Bahamas Government Registered Stocks are measured at fair value through other comprehensive income.

iii) Financial assets held at amortised cost

A financial asset is measured at amortised cost if it meets both of the following conditions and is not designated as at FVTPL:

- the asset is held within a business model whose objective is to hold assets to collect contractual cash flows; and
- the contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interests.



The Central Bank of The Bahamas

Notes to the Financial Statements December 31, 2018 (Continued)

2. Summary of Significant Accounting Policies (continued)

(c) Financial assets (continued)

iii) Financial assets held at amortised cost

Accounts set out below are classified as financial assets held at amortised cost:

- Foreign Government Securities
- Advances to Bahamas Government
- Loans to Bahamas Development Bank
- Bahamas Development Bank bonds
- Bridge Authority bonds
- Clifton Heritage Authority bonds
- Employee loans and other receivables

Subsequent to initial recognition these assets are measured at amortised cost using the effective interest rate method, less any impairment.

The effective interest method is a method of calculating the amortised cost of a debt instrument and of allocating interest income over the relevant period. The effective interest rate is the rate that exactly discounts the estimated future cash receipts (including all fees paid or received that form an integral part of the effective interest rate, transaction costs and other premiums or discounts) through the expected life of the debt instrument, or (where appropriate) a shorter period, to the net carrying amount on initial recognition.

Regular-way purchases and sales of financial assets are recognised on the trade date – the date on which the Bank commits to originate, purchase or sell the asset. Financial assets are initially recognised at fair value plus transaction costs, except financial assets carried at fair value through profit or loss where such costs are expensed as incurred. Financial assets are derecognised when the rights to receive cash flows from the financial assets have expired or when the Bank has transferred substantially all risks and rewards of ownership.

Financial assets at fair value through profit or loss are subsequently carried at fair value. Fair value is based on quoted prices for securities traded in active markets (e.g. international securities exchange) or valuation techniques, including recent arm's length transactions, discounted cash flow analyses and other valuation techniques commonly used by market participants, for securities not traded in active markets.

Gains or losses arising from sales and changes in fair value of financial assets other than those at FVOCI are recognised as a part of net income in the statement of comprehensive income in the financial period in which they arise.



The Central Bank of The Bahamas

Notes to the Financial Statements

December 31, 2018

(Continued)

2. Summary of Significant Accounting Policies (continued)

(d) Impairment of financial assets

The Bank assesses its financial assets measured at amortised cost and debt instruments at FVOCI for ‘expected credit loss’ (ECL).

The Bank measures loss allowances at an amount equal to lifetime ECL, except for the following, for which they are measured as 12-month ECL:

- debt securities that are determined to have low credit risk at the reporting date; and
- other financial instruments on which credit risk has not increased significantly since their initial recognition.

The Bank considers a debt security to have low credit risk when its credit risk rating is equivalent to the globally understood definition of ‘investment grade’ and is issued or guaranteed by a Foreign Government or the Bahamas Government. The Bank does not apply the low credit risk exemption to any other financial instruments.

12-month ECL are the portion of ECL that result from default events on a financial instrument that are possible within the 12 months after the reporting date. Lifetime ECL are the ECL that result from all possible default events over the expected life of the financial instrument.

ECL are a probability-weighted estimate of credit losses. They are measured as follows:

- financial assets that are not credit-impaired at the reporting date: as the present value of all cash shortfalls (i.e. the difference between the cash flows due to the entity in accordance with the contract and the cash flows that the Bank expects to receive)
- financial assets that are credit-impaired at the reporting date: as the difference between the gross carrying amount and the present value of estimated future cash flows;

At each reporting date, the Bank assesses whether financial assets carried at amortised cost and debt financial assets carried at FVOCI, are credit-impaired. A financial asset is ‘credit-impaired’ when one or more events that have a detrimental impact on the estimated future cash flows of the financial asset have occurred.



The Central Bank of The Bahamas

Notes to the Financial Statements

December 31, 2018

(Continued)

2. Summary of Significant Accounting Policies (continued)

(d) Impairment of financial assets (continued)

Loss allowances for ECL are presented in the statement of financial position as follows:

- financial assets measured at amortised cost: as a deduction from the gross carrying amount of the assets;
- debt instruments measured at FVOCI: no loss allowance is recognised in the statement of financial position because the carrying amount of these assets is their fair value. However, the loss allowance is disclosed and is recognised in the fair value reserve.

(e) Property, plant and equipment

Property, plant and equipment, other than land, are recorded at historical cost less accumulated depreciation. Historical cost includes expenditure that is directly attributable to the acquisition of the items.

Subsequent costs are included in the asset's carrying amount or are recognised as a separate asset, as appropriate, only when it is probable that future economic benefit associated with the item will flow to the Bank and the cost of the item can be measured reliably. All other repairs and maintenance are charged to the statement of comprehensive income as part of net income during the financial period in which they are incurred.

Land is not depreciated. Depreciation on other assets are calculated using the straight-line method to allocate cost (net of residual values) over the rate of estimated useful lives as follows:

	Rate
Buildings & renovations	2% - 20%
Office equipment	20% - 33%
Computer software	20% - 50%
Office furniture & fittings	20%
Other fixed assets	20% - 33%

Included in Other fixed assets are Artworks which the Bank does not depreciate.



The Central Bank of The Bahamas

Notes to the Financial Statements

December 31, 2018

(Continued)

2. Summary of Significant Accounting Policies (Continued)

(e) Property, plant and equipment (continued)

The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at each balance sheet date. Assets that are subject to depreciation are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount. The recoverable amount is the higher of the asset's fair value less costs of disposal and its value in use.

Gains and losses on disposals are determined by comparing proceeds with the carrying amount and are recognised in the statement of comprehensive income as a part of net income.

(f) Financial liabilities

Financial liabilities are any liabilities that are contractual obligations to deliver cash or another financial asset to another entity or to exchange financial assets or financial liabilities with another entity under conditions that are potentially unfavorable to the Bank; or a contract that will or may be settled in the Bank's own equity instrument. Financial liabilities are classified as either financial liabilities at fair value through profit or loss (including financial liabilities held for trading and those designated at fair value through profit or loss) and financial liabilities at amortised cost.

i) Financial liabilities at fair value through profit or loss

A financial liability is classified as held for trading if it is acquired or incurred principally for the purpose of selling or repurchasing it in the near term or if it is part of a portfolio of identified financial instruments that are managed together and for which there is evidence of a recent actual pattern of short-term profit-taking or if so designated by management. Financial liabilities designated as at fair value through profit or loss at inception are those that are managed and whose performance is evaluated on a fair value basis, and are intended to be held for an indefinite period of time but may be extinguished in response to needs for liquidity or changes in interest rates or exchange rates. Information about these financial liabilities is provided internally on a fair value basis to the Investment Management Committee. Financial liabilities classified as at fair value through profit or loss consist of the International Monetary Fund liability balance and has been so designated by management.



The Central Bank of The Bahamas

Notes to the Financial Statements

December 31, 2018

(Continued)

2. Summary of Significant Accounting Policies (continued)

(f) Financial liabilities (continued)

i) Financial liabilities at fair value through profit or loss (continued)

Financial liabilities at fair value through profit or loss are initially recognised and subsequently measured at fair value with any gains or losses recognised in the statement of comprehensive income. Fair value is computed using quoted market prices.

ii) Other financial liabilities at amortised cost

Other financial liabilities are initially recognised at fair value and subsequently measured at amortised cost using the effective interest rate method, where applicable.

The Bank derecognises financial liabilities when, and only when, the Bank's obligations are discharged, cancelled or they expire.

(g) Provisions

Provisions are recognised when the Bank has a present legal or constructive obligation as a result of past events, it is more likely than not that an outflow of resources will be required to settle the obligation, and the amount has been reliably estimated.

The amount recognised as a provision is the best estimate of the consideration required to settle the present obligation at the end of the reporting period, taking into account the risks and uncertainties surrounding the obligation. Where a provision is measured using the cash flows estimated to settle the present obligation, its carrying amount is the present value of those cash flows.

When some or all of the economic benefits required to settle a provision are expected to be recovered from a third party, a receivable is recognised as an asset if it is virtually certain that reimbursement will be received and the amount of the receivable can be measured reliably.



The Central Bank of The Bahamas

Notes to the Financial Statements

December 31, 2018

(Continued)

2. Summary of Significant Accounting Policies (Continued)

(h) Currency inventories

Bank notes and coins are recorded at cost upon receipt of stock and are placed into inventory. They are subsequently expensed when issued into circulation.

(i) Numismatic coins

Numismatic coins, which are specially minted or packaged as collectors' items and are not issued for monetary purposes, are not included in coins in circulation. Any profit or loss arising from the sale of these coins is included in the statement of comprehensive income.

(j) Investment currency market payable

The Bank maintains a market in investment currency, prescribed for facilitating direct investment and foreign currency securities acquisitions outside The Bahamas. The investment currency attracts a deposit of 5.0% (2017:10%). Such deposits are treated as financial liabilities, recognised initially at fair value and subsequently measured at amortised cost. The financial liabilities are derecognised when repaid to investors and funds are repatriated to the country.

The purchase of investment currency attracts a 2.5% surcharge to facilitate the transaction. This fee is recognised upon completion of the investment currency purchase and is recognised in 'Other income' in the statement of comprehensive income.

(k) Income and expense recognition

The Bank recognises income when it is probable that future economic benefits will flow to the Bank and the amount of income can be reliably measured. Income is measured at the fair value of the consideration received or receivable. Interest income is accounted for on an accrual basis using the effective interest method.

The effective interest method is a method of calculating the amortised cost of a financial asset or liability and of allocating interest expense over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash payments through the expected life of the financial asset or liability, or (where appropriate) a shorter period, to the net carrying amount on initial recognition of the financial asset or liability.

Other income and expenses are recognised on the accrual basis.



The Central Bank of The Bahamas

Notes to the Financial Statements

December 31, 2018

(Continued)

2. Summary of Significant Accounting Policies (Continued)

(l) Leases

The Bank is the lessee

The leases entered into by the Bank are operating leases. The total payments made under operating leases are charged to the statement of comprehensive income as a part of net income on a straight-line basis over the period of the lease. When an operating lease is terminated before the lease period has expired, any payment required to be made to the lessor by way of penalty is recognised as an expense in the financial period in which termination takes place.

(m) Employee benefits

The Bank's employees participate in a defined benefit and a defined contribution pension plan.

Defined Benefit Plan

The Bank's retirement plan has a contributory defined benefit plan with participants being permanent employees who have been employed on or before December 31, 2013 and have not attained age 55. The cost of providing such benefits is determined using the projected unit credit method, with actuarial valuations being carried out at each statement of financial position date. The defined benefit obligation is calculated annually by independent actuaries. Remeasurements are recognised in other comprehensive income when they occur. Past service cost is recognised immediately in the period of a plan amendment or curtailment. Contributions are made by employees at 5% of basic salary and the difference by the Bank, which amounted to 18.8% (2017: 18.8%).

The asset or liability amount recognised in the statement of financial position represents the present value of the defined benefit obligation and the current service cost at the end of the reporting period less, the fair value of plan assets.

Any asset arising as a result of this calculation is considered a surplus in the defined benefit plan which is fully recoverable by the Bank.



The Central Bank of The Bahamas

Notes to the Financial Statements

December 31, 2018

(Continued)

2. Summary of Significant Accounting Policies (Continued)

(m) Employee benefits (continued)

Defined Benefit Plan (continued)

Employees who join the Bank on or after January 1, 2014 participate in the defined contribution plan. The Bank pays fixed contributions, equivalent to 10% of each member employee's salary, into the Plan which is administered by a third party. These contributions are expensed in the period in which the employees rendered the services entitling them to the benefits. In addition, each member also contributes 5% of their salary. The Bank has no legal or constructive obligations to pay further contributions if the Plan does not hold sufficient assets to pay all employees the benefits relating to employee service in the current and prior periods.

The contributions are recognised as employee benefit expense in the statement of comprehensive income in the period when they are due. The Bank has no further payment obligations once the recognised contributions have been paid.

Health insurance subsidy for retirees

The Bank pays a portion of the group life and health insurance (GLHI) premium for retirees who elect to remain covered by the Bank's GLHI policy after retirement. The expected costs of these benefits are accrued over the period of employment using the same accounting methodology as used for defined benefit pension plan. Remeasurement gains and losses arising from experience adjustments and changes in actuarial assumptions are charged or credited to equity in other comprehensive income in the period in which they arise. These obligations are valued annually by independent qualified actuaries. The amount recognised in the statement of financial position represents the present value of the retirement benefit obligation.

Defined Benefit Plan for Governors and Deputy Governors

Governor's and Deputy Governors participate in a non-contributory defined benefit plan which pays a lifetime pension if ten (10) or more years are served in either or both positions. The cost of providing such benefits is determined using the projected unit credit method, with actuarial valuations being carried out at each statement of financial position date. The defined benefit obligation is calculated annually by independent actuaries. Remeasurements are recognised in other comprehensive income when they occur. Past service cost is recognised immediately in the period of a plan amendment or curtailment. The plan is financed on a pay-as-you-go basis.

The liability amount recognised in the statement of financial position represents the present value of the defined benefit obligation at the end of the reporting period.



The Central Bank of The Bahamas

Notes to the Financial Statements

December 31, 2018

(Continued)

2. Summary of Significant Accounting Policies (Continued)

(n) Cash and cash equivalents

For the purpose of the statement of cash flows, cash and cash equivalents comprise cash on hand and at bank and deposits that have original contractual maturities of three months or less.

(o) Taxation

Under the current laws of The Bahamas, the country of domicile of the Bank, there are no income, capital gains or other corporate taxes imposed. The Bank's operations do not subject it to taxation in any other jurisdiction.

(p) Fiduciary items

No account is taken in these financial statements of assets held or liabilities incurred by the Bank in a fiduciary capacity.

3. Cash and Deposits with Banks

Cash and cash equivalents per the statement of cash flows comprise the following:

	2018	2017
	\$	\$
External Assets		
Cash on hand	4,000	4,000
Cash in vault	652,247	467,035
Cash and deposit with banks	<u>375,104,659</u>	<u>698,064,699</u>
	375,760,906	698,535,734
Domestic Assets		
Cash on hand	<u>37,828</u>	<u>32,190</u>
	375,798,734	698,567,924
Less: Deposits with banks with original contractual maturities greater than three months	<u>(183,019,328)</u>	<u>(155,740,529)</u>
	<u>192,779,406</u>	<u>542,827,395</u>



The Central Bank of The Bahamas

Notes to the Financial Statements December 31, 2018 (Continued)

4. Property, Plant and Equipment

	Land	Buildings & Renovations	Office Equipment	Computer Software	Furniture & Fittings	Other Fixed Assets	Total
	\$	\$	\$	\$	\$	\$	\$
COST							
As at January 1, 2018	2,452,938	14,901,106	8,440,891	11,742,617	784,850	286,959	38,609,361
Additions	-	1,834,869	1,314,446	585,087	82,941	135,500	3,952,893
Disposals/Retirement	-	(21,199)	(1,832,498)	-	(5,358)	-	(1,859,055)
As at December 31, 2018	2,452,938	16,714,776	7,922,839	12,327,704	862,433	422,509	40,703,199
ACCUMULATED DEPRECIATION							
As at January 1, 2018	-	8,761,140	7,121,118	9,683,326	631,724	156,623	26,353,931
Charge for the year	-	442,848	555,733	1,052,753	60,933	64,753	2,177,020
Disposals/Retirement	-	(21,199)	(1,562,807)	-	(5,358)	-	(1,589,364)
As at December 31, 2018	-	9,182,789	6,114,044	10,736,079	687,299	221,376	26,941,587
NET BOOK VALUE							
As at December 31, 2018	2,452,938	7,531,987	1,808,795	1,591,625	175,134	201,133	13,761,612
COST							
As at January 1, 2017	2,452,938	15,060,801	7,959,896	11,114,648	700,766	319,769	37,608,818
Additions	-	296,700	604,582	627,969	92,210	18,785	1,640,246
Transfer	-	-	4,476	-	(4,476)	-	-
Disposals/Retirement	-	(456,395)	(128,063)	-	(3,650)	(51,595)	(639,703)
As at December 31, 2017	2,452,938	14,901,106	8,440,891	11,742,617	784,850	286,959	38,609,361
ACCUMULATED DEPRECIATION							
As at January 1, 2017	-	8,723,357	6,695,552	8,616,386	568,568	122,546	24,726,409
Charge for the year	-	433,515	531,453	1,066,940	70,536	60,734	2,163,178
Disposals/Retirement	-	-	3,730	-	(3,730)	-	-
Transfer	-	(395,732)	(109,617)	-	(3,650)	(26,657)	(535,656)
As at December 31, 2017	-	8,761,140	7,121,118	9,683,326	631,724	156,623	26,353,931
NET BOOK VALUE							
As at December 31, 2017	2,452,938	6,139,966	1,319,773	2,059,291	153,126	130,336	12,255,430



The Central Bank of The Bahamas

Notes to the Financial Statements December 31, 2018 (Continued)

5. External Assets

External assets comprise those assets defined by Section 18(1) of the Act. The Act also requires that the value of external assets shall not at any time be less than 50% of the value of the aggregate of the notes and coins in circulation and other demand liabilities of the Bank. At year end, external assets represented 86.1% (2017: 93.2%) of such liabilities.

6. Foreign Government Securities

Section 18(1) of the Act requires that marketable securities issued or guaranteed by foreign governments, which mature beyond 5 years, shall at no time constitute more than 30% in value of the Bank's external assets. At December 31, 2018, marketable securities held by the Bank, which mature after 5 years, constituted 23.27% (2017: 22.03%) of the Bank's external assets. The Ministry of Finance is in the process of amending the Act consistent with the Bank's current operating profile, which is expected to increase the allowed percentage above.

The movement in Foreign Government Securities classified as financial assets held at amortised cost (2017: held-to-maturity) are as follows:

	2018	2017
	\$	\$
Beginning balance	611,001,834	547,050,753
Purchases at nominal value	111,500,000	70,000,000
Discount on purchases	176,227	(80,6833)
Redemptions/maturities	(158,000,000)	(7,000,000)
Gain on redemption/maturities	238,719	-
Discount earned	1,126,311	1,044,887
Amortised premium	(138,562)	(13,123)
Total	<u>565,904,529</u>	<u>611,001,834</u>
Add: Accrued interest	2,864,298	3,660,246
Ending balance	<u>568,768,827</u>	<u>614,662,080</u>

These securities bear interest at rates varying between 1.375% and 4.75% (2017: 1.125% and 3.375%).

7. Marketable Securities

These represent securities that are externally managed by a third party.



The Central Bank of The Bahamas

Notes to the Financial Statements

December 31, 2018

(Continued)

7. Marketable Securities (Continued)

The movement in marketable securities classified as financial assets at fair value through profit or loss are as follows:

	2018	2017
	\$	\$
Beginning balance	-	-
Purchases	106,566,727	-
Sales	(7,070,246)	-
Unrealised gain	1,553,425	-
Total	101,049,906	-
Add: Accrued interest	711,513	-
Ending balance	101,761,419	-

8. International Monetary Fund

Background

The International Monetary Fund (IMF) is an organisation of 188 countries, working to foster global monetary cooperation, secure financial stability, facilitate international trade, promote high employment and sustainable economic growth, and reduce poverty around the world. The Bahamas was admitted as a member of the IMF on August 21, 1973.

Quota, Subscriptions and Reserve Tranche

Each IMF member country is assigned a quota, or contribution, that reflects the country's relative size in the global economy. Quotas are denominated in Special Drawing Rights (SDRs), the IMF's unit of account, which is essentially a specified basket of four (4) major international currencies (i.e., the U.S. Dollar, Japanese Yen, Euro, and Pound Sterling).

As of December 31, 2018, The Bahamas was assigned a quota of SDR 182,400,000 (2017: SDR 182,400,000) which represents 0.04% (2017: 0.04%) of the total quota allocated by the IMF.



Notes to the Financial Statements
December 31, 2018
(Continued)

8. International Monetary Fund (Continued)

Quota, Subscriptions and Reserve Tranche (continued)

A member's quota determines that country's financial and organizational relationship with the IMF which includes:

- Determining the maximum amount of financial resources the member is obliged to provide to the IMF via its subscription;
- Determining a member's voting power in IMF decisions; and
- Establishing the maximum amount of financing a member can obtain from the IMF.

The Reserve Tranche Position (RTP) represents that proportion of the required quota of currency that each IMF member country must provide to the IMF, but can designate for its own use. The RTP was purchased from the Government of The Bahamas in 1976 and can be encashed on demand in order to meet a balance of payments financing need. This reserve asset is established when a member pays its initial subscription into the IMF at the predetermined amount of SDR or freely usable currency. The IMF designates freely usable currencies as those widely used to make payments for international transactions and are traded in the principal exchange markets.

The Bahamian dollar is designated as an unusable currency which permits the Bank to pay the non-reserve portion of the quota in the form of promissory notes. Subsequent to its initial subscription into the IMF, the Bank has increased the IMF subscriptions of The Bahamas by issuing, non-negotiable, interest-free promissory notes which are payable if the IMF requires an emergency loan. Payment of the promissory notes will give rise to an equal and opposite receivable from the IMF. These promissory notes were issued by the Bank and the Government of The Bahamas on behalf of the Bank, in the Bahamian dollar equivalents of SDR 43,346,071 and SDR 114,884,493 (2017: SDR 43,280,648 and SDR 114,711,096) respectively. The promissory notes form, in substance, part of a loan commitment to the IMF and as such are not recognised on the statement of financial position.



The Central Bank of The Bahamas

Notes to the Financial Statements December 31, 2018 (Continued)

8. International Monetary Fund (Continued)

Quota, Subscriptions and Reserve Tranche (continued)

The IMF reserve tranche represents the difference between the members quota and the sum of promissory notes and subscription payments in local currency paid to the IMF as noted below:

	2018		2017	
	SDR	\$	SDR	\$
Quota	182,400,000	253,680,382	182,400,000	259,762,084
Subscription payments in promissory notes	(158,230,564)	(220,065,734)	(157,991,744)	(225,001,452)
Subscription payments in local currency	(4,884,156)	(6,792,843)	(5,122,976)	(7,295,805)
Reserve tranche	19,285,280	26,821,805	19,285,280	27,464,827

The movement in the reserve tranche during the year are as follows:

	2018		2017	
	SDR	\$	SDR	\$
Beginning balance	19,285,280	27,464,827	19,285,280	25,925,814
Purchase of SDRs	-	-	-	-
Currency movement	-	(643,022)	-	1,539,013
Total	19,285,280	26,821,805	19,285,280	27,464,827

SDR Holdings and SDR Allocation

The IMF may allocate SDRs to member countries in proportion to their IMF quotas. SDRs allocated is treated as a liability in the financial statements of a member, with an equal asset initially being recorded in the form of SDR Holdings.

Members can hold their SDRs as part of their international reserves or sell part or all of their SDR holdings. Members can exchange SDRs for freely usable currencies (and vice versa) among themselves and with prescribed holders; such exchange can take place under a voluntary arrangement or under designation by the IMF. Revaluation differences of SDR assets and liabilities are reported in net foreign exchange gains/losses account in the statement of comprehensive income.

IMF members can also use SDRs in operations and transactions involving the IMF, such as the payment of interest on and repayment of loans, or payment for future quota increases.

Consequently, a member's SDR Holdings (asset) and SDR Allocation (liability) can be different at a point in time.

The IMF pays interest at the SDR interest rate on the amount that a member's net holdings exceed their cumulative allocations. Conversely, if a member's SDR holdings are below its allocation, it incurs a net interest obligation.



The Central Bank of The Bahamas

Notes to the Financial Statements December 31, 2018 (Continued)

8. International Monetary Fund (Continued)

SDR Holdings and SDR Allocation (continued)

Interest on SDR holdings and allocations are received/paid quarterly. The SDR interest rate is determined weekly on each Friday and is based on a weighted average of representative interest rates on three months debt in the money markets of the basket of five (5) SDR international currencies.

SDR Holdings

	2018		2017	
	SDR	\$	SDR	\$
Beginning balance	53,832,786	76,665,114	54,084,961	72,708,131
Purchases	34,556,353	48,060,684	-	-
Remuneration and other charges	-	-	(252,175)	(674,773)
Currency movement	-	(1,794,929)	-	4,631,756
Total	88,389,139	122,930,869	53,832,786	76,665,114
Add: Accrued interest		259,842		119,304
Ending balance		123,190,711		76,784,418

SDR Allocation

	2018		2017	
	SDR	\$	SDR	\$
Beginning balance	124,413,351	177,181,312	124,413,351	167,252,819
Currency movement	-	(4,148,272)	-	9,928,493
Total	124,413,351	173,033,040	124,413,351	177,181,312
Add: Accrued interest		314,857		217,901
Ending balance		173,347,897		177,399,213

In accordance with a resolution of the Board of Governors of the IMF, effective December 11, 1978, The Bahamas became a participant in the Special Drawing Rights Department of the IMF, receiving a total allocation of SDR 10,230,000 between 1979 and 1981. A general allocation took effect on August 28, 2009 and a special allocation on September 9, 2009 and increased the Bank's allocations to SDR 124,413,351.

The interest rate, which is the same on both SDR Holdings and allocation, varied between 0.764% and 1.103% (2017: 0.287% and 0.7439%) during the period.



The Central Bank of The Bahamas

Notes to the Financial Statements December 31, 2018 (Continued)

9. Bahamas Development Bank Bonds

The movement in the Bahamas Development Bank bonds is as follows:

	2018	2017
	\$	\$
Balance	4,000,000	4,000,000
Add: Accrued interest	<u>49,834</u>	<u>91,984</u>
Total	<u>4,049,834</u>	<u>4,091,984</u>

These bonds bear interest at the Bahamian dollar prime rate of 4.25% (2017: 4.25%) with \$2,000,000 maturing on August 1, 2025 and November 1, 2025, respectively.

10. Advances to Bahamas Government

Sections 28(3) and 28(4) of the Act require that advances to the Government, which may be outstanding at any one time, shall not exceed the lesser of either (a) 10% of the annual average ordinary revenue of the Government over the three preceding years, for which the accounts have been laid before Parliament, or (b) the estimated ordinary revenue of the Government for the year.

At the year end date, advances to the Government were 7.89% (2017: 9.52%) of the lesser of such revenues.

The movements in advances for the year are as follows:

	2018	2017
	\$	\$
Beginning balance	134,657,052	134,657,052
Additional advances	30,000,000	-
Repayments	<u>(45,000,000)</u>	<u>-</u>
	119,657,052	134,657,052
Add: Accrued interest	<u>710,396</u>	<u>703,548</u>
Ending balance	<u>120,367,448</u>	<u>135,360,600</u>



The Central Bank of The Bahamas

Notes to the Financial Statements

December 31, 2018

(Continued)

10. Advances to Bahamas Government (Continued)

The advances, which are repayable on demand, are as follows:

Rate	2018 \$	2017 \$
0.356%	4,069,444	19,069,444
0.395%	20,000,000	20,000,000
0.483%	5,000,000	5,000,000
0.512%	5,000,000	5,000,000
0.540%	60,000,000	60,000,000
0.638%	20,000,000	20,000,000
0.840%	5,587,608	5,587,608
	<u>119,657,052</u>	<u>134,657,052</u>

11. Bahamas Government Registered Stocks

Effective January 1st, 2018 The Bahamas Government Registered Stocks were classified as financials at fair value through other comprehensive income upon the adoption of IFRS 9. The Bahamas Government Registered Stocks were previously classified as Loans & Receivables measured at amortised cost. The movements in Bahamas Government Registered Stocks are as follows:

	2018 \$	2017 \$
Beginning balance	271,713,400	368,444,300
Adjustment on transitional application of IFRS 9	<u>2,277,217</u>	<u>-</u>
Adjusted beginning balance	273,990,617	368,444,300
Purchases	8,295,060	54,163,200
Market value adjustment	1,369,020	-
Discounts carried	-	31,814
Premiums amortised	-	(16,514)
Redemptions/maturities	<u>(37,250,092)</u>	<u>(150,909,400)</u>
Total	246,404,605	271,713,400
Add: Accrued interest	<u>2,631,683</u>	<u>2,798,185</u>
Ending balance	<u>249,036,288</u>	<u>274,511,585</u>

Bahamas Government Registered Stocks bear interest at rates ranging between 3.50% and 6.00% (2017: 3.00% and 5.40%).



The Central Bank of The Bahamas

Notes to the Financial Statements

December 31, 2018

(Continued)

12. Loans to Bahamas Development Bank

This balance is comprised of two Government Guaranteed loan facilities made available in accordance with Section 29(1)(f) of the Act.

The movement in loans to Bahamas Development Bank are as follows:

	2018	2017
	\$	\$
Beginning balance	2,750,000	3,550,000
Repayments	<u>(250,000)</u>	<u>(800,000)</u>
Total	2,500,000	2,750,000
Add: Accrued interest	<u>9,158</u>	<u>9,867</u>
Ending balance	<u>2,509,158</u>	<u>2,759,867</u>

The loans bear interest at 2.00% (2017: 2.00%), with \$2,500,000 maturing on October 28, 2024.

13. Bridge Authority Bonds

The movements in the Bridge Authority bonds are as follows:

	2018	2017
	\$	\$
Beginning balance	484,100	478,800
Purchases	<u>2,100</u>	<u>5,300</u>
Total	486,200	484,100
Add: Accrued interest	<u>7,287</u>	<u>7,251</u>
Ending balance	<u>493,487</u>	<u>491,351</u>

These bonds bear interest at rates ranging from 1.00% to 1.63% (2017: 1.25% to 1.63%) per annum over the Bahamian dollar prime rate with \$447,900, \$14,300 and \$24,000 maturing on March 24, 2019, 2024 and 2029, respectively.

14. Clifton Heritage Authority Bonds

These bonds, which mature on May 20, 2025, bear interest at 5.25%. The balance of the Clifton Heritage Authority bonds is made up as follows:

	2018	2017
	\$	\$
Balance	634,600	634,600
Add: Accrued interest	<u>3,469</u>	<u>3,469</u>
Total	<u>638,069</u>	<u>638,069</u>



The Central Bank of The Bahamas

Notes to the Financial Statements

December 31, 2018

(Continued)

15. Bahamas Government Treasury Bills

Bahamas Government Treasury bills are discounted at rates ranging between 99.55% and 99.63% (2017: 99.45% and 99.47%) maturing 91 to 182 days from acquisition.

	2018	2017
	\$	\$
Beginning balance	7,167,773	223,373,196
Purchases	642,975,803	1,095,088,890
Redemptions/maturities	(494,570,346)	(1,311,294,313)
Total	<u>155,573,230</u>	<u>7,167,773</u>
Add: Discount earned	163,601	1,770
Ending balance	<u>155,736,831</u>	<u>7,169,543</u>

16. Notes in Circulation

In accordance with the Act, the Bank has the sole authority to issue banknotes for circulation in The Bahamas. A breakdown, by denomination, is presented below.

Notes	2018	2017
	\$	\$
0.50	772,514	767,305
1.00	24,666,843	24,285,623
3.00	2,026,296	2,016,801
5.00	11,978,945	11,917,775
10.00	18,872,740	18,510,170
20.00	54,215,500	61,348,800
50.00	141,702,200	123,722,200
100.00	176,571,800	168,470,000
Other bank notes	82,017	82,032
	<u>430,888,855</u>	<u>411,120,706</u>

17. Deposits by Commercial Banks

Deposits by commercial banks include current account balances deposited as statutory reserves in accordance with Section 19 of the Act. The remaining funds deposited in the current account are used to facilitate settlement and to effect foreign currency transactions.

The present level of the statutory reserves applicable to commercial banks is 5% of total Bahamian dollar deposit liabilities, of which at least 4% must be placed on deposit with the Bank. These deposits are interest free and are repayable on demand, subject to maintenance of minimum balances required by the Act.



The Central Bank of The Bahamas

Notes to the Financial Statements

December 31, 2018

(Continued)

18. Deposits by International Agencies

The Bank is designated as the fiscal agency for the Commonwealth of The Bahamas. Deposits by international agencies include deposits in Bahamian currency by the World Bank, the International Monetary Fund and the Inter-American Development Bank. These deposits are interest free and are repayable on demand.

19. Equity and Reserves

Capital management - The Bank's objectives when managing capital, which consists of total equity and reserves on the statement of financial position, are:

- To comply with the capital requirements outlined in Sections 6 and 7 of the Act;
- To safeguard the Bank's ability to continue as a going concern in its provision of Central Banking facilities for The Bahamas; and
- To maintain a strong capital base to support the development of the Bahamian economy.

Capital adequacy and the use of regulatory capital are monitored by the Bank's management, and in accordance with the guidelines established by the Act.

At December 31, 2018, and 2017, the Bank's paid up capital was equal to the authorised capital of \$3,000,000.

To comply with section 32(2)(a) of the Act, the table below presents the performance of the Bank excluding from the calculation any profit or loss arising from any revaluation of any assets or liabilities of the Bank occasioned by any change in the value of the currency of The Bahamas or any foreign currency.

	2018 \$	2017 \$
Net income	18,657,050	10,634,360
Appropriation of foreign exchange (gain)/loss	<u>(667,228)</u>	<u>4,081,597</u>
Net income per the Act	17,989,822	14,715,957
Other comprehensive income	<u>3,382,569</u>	<u>1,288,131</u>
Total comprehensive income stated in accordance with the Act	<u><u>21,372,391</u></u>	<u><u>16,004,088</u></u>



The Central Bank of The Bahamas

Notes to the Financial Statements

December 31, 2018

(Continued)

19. Equity and Reserves (Continued)

Exchange equalisation account - Under the terms of Sections 32(2)(a) and 32(2)(b) of the Act, this account represents the net foreign exchange gain or loss arising from the revaluation of foreign currency monetary assets and liabilities of the Bank at the date of the statement of financial position.

Building fund - This account represents a reserve for construction of a new premises.

Fair value reserve – This represents the accumulated gain on the market value of financial assets classified at fair value through other comprehensive income.

General reserve - Section 7(2) of the Act requires that, at the end of any year where the amount in the general reserve exceeds twice the authorised capital of the Bank or 15% of its demand liabilities, whichever is greater, the excess shall be paid to the Consolidated Fund, unless the Minister of Finance determines otherwise.

The balance of the general reserve at the year-end amounted to \$152,382,493 (2017: \$140,101,905) equivalent to 11% (2017: 9%) of demand liabilities.

20. Income

	2018	2017
	\$	\$
<i>Interest on foreign investments</i>		
Demand deposits	4,818,321	1,045,526
Fixed deposits	7,335,895	3,099,850
Foreign Government and marketable securities	17,696,361	14,314,522
Interest Income on SDR	999,730	397,406
	<u>30,850,307</u>	<u>18,857,304</u>
<i>Interest on domestic investments</i>		
Bahamas Development Bank bonds	170,000	170,110
Bahamas Government Registered Stocks	10,998,383	14,329,383
Bridge Authority bonds	26,852	26,635
Bahamas Government Treasury bills	518,792	4,601,113
Clifton Heritage bonds	30,144	30,161
	<u>11,744,171</u>	<u>19,157,402</u>
<i>Interest on loans</i>		
Loans to Bahamas Development Bank	53,233	65,401
Government advances	710,397	703,548
Staff	240,338	281,892
	<u>1,003,968</u>	<u>1,050,841</u>
<i>Interest expense on IMF allocation</i>	<u>(1,640,107)</u>	<u>(921,557)</u>



The Central Bank of The Bahamas

Notes to the Financial Statements December 31, 2018 (Continued)

20. Income (Continued)

	2018	2017
	\$	\$
<i>Gains/(losses) on investments</i>		
Net foreign exchange gain/(loss)	667,228	(4,052,958)
Realised gain on Marketable Securities	12,238	-
Unrealised gain on Marketable Securities	1,553,425	-
Gain on Sale of Foreign Government Securities	238,719	-
Net trading gain on Bahamas Government Registered Stocks	155,436	1,781,256
	<u>2,027,046</u>	<u>(2,271,702)</u>
<i>Other income</i>		
Allocated bank license fees	3,700,000	3,700,000
Bank statutory fines	251	88,780
Commission on foreign currency sales	1,183,323	953,152
Premium on Investment Currency Market	1,106,407	238,729
Other	897,056	828,420
	<u>6,887,037</u>	<u>5,809,081</u>
Total income	<u>51,472,422</u>	<u>41,681,369</u>

21. Expenses

	2018	2017
	\$	\$
<i>Staff costs</i>		
Salaries, wages and gratuity	15,014,657	14,529,163
Defined benefit plan	1,235,549	1,331,381
Group insurance plan	1,322,676	1,419,211
Staff training	752,262	509,120
National insurance	488,859	466,951
Health insurance subsidy	264,417	239,810
Responsibility allowance	217,500	202,650
Former Governors' retirement benefit	298,635	893,799
Defined contribution plan	297,169	238,663
Other	364,600	311,440
	<u>20,256,324</u>	<u>20,142,188</u>



The Central Bank of The Bahamas

Notes to the Financial Statements December 31, 2018 (Continued)

21. Expenses (Continued)

	2018	2017
	\$	\$
<i>General and administrative</i>		
Currency	1,540,499	1,813,934
Professional fees	3,193,718	2,129,647
Utilities	1,052,476	868,435
Repairs and maintenance	1,038,155	965,246
Rent	536,303	505,251
Insurance	202,417	182,420
Cash shipment	285,191	254,008
Subscription and membership fees	133,948	128,286
Stationery and office supplies	61,298	89,346
Directors' remuneration	57,950	49,898
Other	2,280,073	1,755,172
	<u>10,382,028</u>	<u>8,741,643</u>

22. The Deposit Insurance Corporation

During 1999, in accordance with Section 5(1) of the Protection of Depositors Act, 1999, the Bank has made an initial capital contribution of \$500,000 in the Deposit Insurance Corporation (DIC). This represents 100% of the paid-up portion of the capital of DIC, which was established to manage the Deposit Insurance Fund set up to protect deposits placed with member institutions.

In the opinion of the Directors, the Bank is not exposed, or has rights, to variable returns from its involvement with the DIC and does not have the ability to affect its returns. Consequently, the Deposit Insurance Corporation is not treated as a subsidiary in these financial statements.

Considering the substance of this transaction, this contribution does not meet the recognition criteria as an investment and was subsequently derecognised.



The Central Bank of The Bahamas

Notes to the Financial Statements

December 31, 2018

(Continued)

23. Commitments & Contingencies

(a) Contingencies

The Bank is party to claims in the normal course of business, which are at various stages of the judicial process. The Bank is defending all such claims and is of the opinion that the outcomes, which cannot presently be determined, will not adversely affect its operations or financial position.

(b) Commitments

i) Leases

The Bank leases office space with lease terms of between three to five years. At year-end, the Bank was committed to the following payments:

	2018	2017
	\$	\$
Not later than one year	394,834	351,643
Later than one year but not later than five years	941,423	1,012,346

ii) Printing of Currency

The Bank also commits to order currency from several minters and printers. At year-end, the Bank was committed to the following payments for currency:

	2018	2017
	\$	\$
Not later than one year	2,933,500	53,470
Later than one year but not later than five years	2,894,980	3,565,556



The Central Bank of The Bahamas

Notes to the Financial Statements December 31, 2018 (Continued)

24. Concentration of Assets and Liabilities

	2018	2017
EXTERNAL ASSETS		
<i>Geographic Region</i>		
North America	62.11%	72.00%
Europe	4.07%	21.55%
Other	33.82%	6.45%
	<u>100.00</u>	<u>100.00</u> %
<i>Industry</i>		
Financial Sector	100.00%	100.00%
DOMESTIC ASSETS		
<i>Geographic Region</i>		
Bahamas	100.00%	100.00%
<i>Industry</i>		
Government Sector	100.00%	100.00%
DEMAND LIABILITIES		
<i>Geographic Region</i>		
Bahamas	100.00%	100.00%
<i>Industry</i>		
Financial Sector	92.81%	96.62%
Government Sector	7.19%	3.38%
	<u>100.00</u> %	<u>100.00</u> %
OTHER LIABILITIES		
<i>Geographic Region</i>		
North America	100.00%	100.00%
<i>Industry</i>		
Financial Sector	100.00%	100.00%

Section 29(1)(c) of the Act requires that the total amount of Government issued or guaranteed securities held at any time by the Bank, which mature beyond five (5) years after their date of issue, shall not exceed 20% of the demand liabilities of the Bank. At the statement of financial position date, such securities held by the Bank, which matured beyond five years after their date of issue, was 18.02% (2017: 11.28%) of demand liabilities. The Ministry of Finance is in the process of amending the Act consistent with the Bank's current operating profile, which is expected to increase the allowed percentage above.

The Act further requires that any holdings of Government issued or guaranteed securities should not have maturities extending beyond 20 years from the date of their acquisition. The Bank held no securities maturing beyond 20 years, at either December 31, 2018 or 2017.



The Central Bank of The Bahamas

Notes to the Financial Statements December 31, 2018 (Continued)

25. Related Party Transactions

Related parties comprise i) Government ministries and departments; ii) Government corporations and agencies; iii) entities controlled by the Government; iv) entities in which the Government has a significant ownership interest; and v) key management personnel. Transactions that the Bank has with such related entities are disclosed on the statement of financial position and accompanying notes. The amounts and terms of these transactions are discussed and agreed upon by the parties.

The Bank provides certain services to the Government of The Bahamas, in accordance with its mandate under Sections 26 to 29 of the Act. These services include but are not limited to:

- Act as banker to the Government or any public corporation;
- Act as the agent of the Government in the management of the public debt;
- Make temporary advances to the Government;
- Open accounts for, accept deposits from, and collect money for or on account of, the Government or any public corporation; and
- Buy, hold and sell securities issued or guaranteed by the Government

The Bank's senior officials and directors are regarded to be its key management personnel.

The following balances and transactions relate to key management personnel:

(a) Compensation:

	2018	2017
	\$	\$
Senior officials' salaries and short-term benefits	1,828,633	1,526,662
Directors' remuneration	57,950	49,898
Post-employment benefits	<u>128,420</u>	<u>124,851</u>
	<u>2,015,003</u>	<u>1,701,411</u>



The Central Bank of The Bahamas

Notes to the Financial Statements

December 31, 2018

(Continued)

25. Related Party Transactions (continued)

(b) Other assets include secured loans to employees totaling \$7,896,892 (2017: \$9,207,535) net of provision for bad debt totaling \$378,699 (2017:\$351,691), of which the following relates to key management personnel:

	2018	2017
	\$	\$
Beginning of the year	871,444	966,456
Advances during the year	9,200	42,350
Repayments during the year	<u>(121,244)</u>	<u>(137,362)</u>
End of the year	<u>759,400</u>	<u>871,444</u>

(c) Post-employment pension obligation and other benefits:

	2018	2017
	\$	\$
Defined contribution pension plan for Employees	162,970	109,738
Defined benefit pension plan for Employees	2,402,913	2,175,120
Defined benefit pension plan for Governors and Deputy Governors	401,751	230,674
Gratuity	<u>34,856</u>	<u>4,422</u>
End of the year	<u>3,002,490</u>	<u>2,519,954</u>

26. Fiduciary Assets and Liabilities

Section 24 of the Act authorises the Bank to accept unclaimed customer deposits that are required to be transferred to it by a bank in The Bahamas in accordance with the Banks and Trust Companies Regulation Act, pay interest on money deposited and pay out money to any person entitled thereto. At December 31, 2018 the Bank held assets consisting of bank accounts in respect of the unclaimed customer deposits of \$108,771,515 (2017: \$100,077,726). These amounts are excluded from the statement of financial position.

The Insurance Commission of the Bahamas granted the Bank custody of unclaimed insurance from registered insurance companies in the amount of \$2,003,574 (2017: \$1,526,088) which are excluded from the statement of financial position.

Additionally, the Bank holds various sinking funds with an external broker on behalf of The Government which totaled \$72,004,836. These funds are also excluded from the statement of financial position.

To manage fiduciary risk, the Bank generally takes a conservative approach in its fiduciary undertakings.



The Central Bank of The Bahamas

Notes to the Financial Statements December 31, 2018 (Continued)

27. Financial Instruments

Categories of Financial Instruments

	Amortised Cost \$	Fair Value Through Profit or Loss \$	Fair Value Through Other Comprehensive Income \$	Total Carrying Amount \$
December 31, 2018				
EXTERNAL ASSETS				
Cash and deposits with banks	375,760,906	-	-	375,760,906
Foreign Government Securities	568,768,827	-	-	568,768,827
Marketable securities	-	101,761,419	-	101,761,419
International Monetary Fund:				
Bahamas reserve tranche	-	26,821,805	-	26,821,805
Special drawing rights - holdings	-	123,190,711	-	123,190,711
DOMESTIC ASSETS				
Cash on hand	37,828	-	-	37,828
Bahamas Development Bank bonds	4,049,834	-	-	4,049,834
Advances to Bahamas Government	120,367,448	-	-	120,367,448
Bahamas Government Registered Stock	-	-	249,036,288	249,036,288
Loans to Bahamas Development Bank	2,509,158	-	-	2,509,158
Bridge Authority Bonds	493,487	-	-	493,487
Clifton Heritage Authority Bonds	638,069	-	-	638,069
Bahamas Government Treasury Bills	-	-	155,736,831	155,736,831
Employee loans and other receivables	8,187,757	-	-	8,187,757
Total	1,080,813,314	251,773,935	404,773,119	1,737,360,368



The Central Bank of The Bahamas

Notes to the Financial Statements December 31, 2018 (Continued)

27. Financial Instruments (Continued)

Categories of Financial Instruments (continued)

	Fair Value Through Profit or Loss \$	Other Financial Liabilities \$	Total Carrying Amount \$
December 31, 2018			
DEMAND LIABILITIES			
Notes in circulation	-	430,888,855	430,888,855
Coins in circulation	-	28,970,923	28,970,923
Deposits by commercial banks	-	791,668,258	791,668,258
Deposits by Bahamas Government and Bahamas Government agencies	-	96,155,504	96,155,504
Deposits by International agencies	-	255,302	255,302
Accounts payable and other liabilities	-	29,002,444	29,002,444
Investment Currency Market payable	-	9,007,273	9,007,273
OTHER LIABILITIES			
International Monetary Fund: Special drawing rights allocation	173,347,897	-	173,347,897
Total	<u>173,347,897</u>	<u>1,385,948,559</u>	<u>1,559,296,456</u>



The Central Bank of The Bahamas

Notes to the Financial Statements

December 31, 2018

(Continued)

27. Financial Instruments (Continued)

Categories of Financial Instruments (continued)

	Loans & Receivables (amortised cost)	Fair Value Through Profit or Loss	Held-to- Maturity (amortised cost)	Available-for- Sale	Total Carrying Amount
	\$	\$	\$	\$	\$
December 31, 2017					
EXTERNAL ASSETS					
Cash and deposits with banks	698,535,734	-	-	-	698,535,734
Marketable securities issued or guaranteed by foreign governments	-	-	614,662,080	-	614,662,080
International Monetary Fund:					
Bahamas reserve tranche	-	27,464,827	-	-	27,464,827
Special drawing rights - holdings	-	76,784,418	-	-	76,784,418
DOMESTIC ASSETS					
Cash on hand	32,190	-	-	-	32,190
Bahamas Development Bank bonds	4,091,984	-	-	-	4,091,984
Advances to Bahamas Government	135,360,600	-	-	-	135,360,600
Bahamas Government Registered Stock	274,511,585	-	-	-	274,511,585
Loans to Bahamas Development Bank	2,759,867	-	-	-	2,759,867
Bridge Authority Bonds	491,351	-	-	-	491,351
Clifton Heritage Authority Bonds	-	-	638,069	-	638,069
Bahamas Government Treasury Bills	-	-	-	7,169,543	7,169,543
Employee loans and other receivables	9,784,592	-	-	-	9,784,592
Total	1,125,567,903	104,249,245	615,300,149	7,169,543	1,852,286,840



The Central Bank of The Bahamas

Notes to the Financial Statements December 31, 2018 (Continued)

27. Financial Instruments (Continued)

Categories of Financial Instruments (continued)

	Fair Value Through Profit or Loss \$	Other Financial Liabilities \$	Total Carrying Amount \$
December 31, 2017			
DEMAND LIABILITIES			
Notes in circulation	-	411,120,706	411,120,706
Coins in circulation	-	27,396,830	27,396,830
Deposits by commercial banks	-	1,011,246,639	1,011,246,639
Deposits by Bahamas Government and Bahamas Government agencies	-	44,152,152	44,152,152
Deposits by International agencies	-	255,217	255,217
Accounts payable and other liabilities	-	11,110,160	11,110,160
Investment Currency Market payable	-	8,736,314	8,736,314
OTHER LIABILITIES			
International Monetary Fund: Special drawing rights allocation	177,399,213	-	177,399,213
Total	177,399,213	1,514,018,018	1,691,417,231

28. Fair Value Measurements

Fair value of financial instruments

Below is a comparison of the carrying value and the fair value of the Bank's financial instruments, other than those with carrying value that approximates its fair value.

	2018		2017	
	Carrying Value \$	Fair Value \$	Carrying Value \$	Fair Value \$
FINANCIAL INSTRUMENTS				
Foreign Government Securities	568,768,827	572,175,261	614,662,080	617,020,047
Bahamas Government Registered Stocks (at fair value in 2018)	-	-	274,511,585	276,830,251
Loans to Bahamas Development Bank	2,509,158	3,154,075	2,759,867	3,539,415
Bridge Authority bonds	493,487	500,705	491,351	509,559
Clifton Heritage Authority bonds	638,069	665,910	638,069	661,404
TOTAL	572,409,541	576,495,951	893,062,952	898,560,676



The Central Bank of The Bahamas

Notes to the Financial Statements

December 31, 2018

(Continued)

28. Fair Value Measurements (continued)

Fair value of financial instruments (continued)

- i) It is the Directors' opinion that the carrying value of other assets and liabilities approximate their fair value due to the short-term maturities of these investments.
- ii) Investments in Bahamas Development Bank bonds yield market-based interest rates resulting in its carrying value approximating its fair value.
- iii) Advances to Bahamas Government and deposits by commercial banks, international agencies, Bahamas Government and government agencies are considered due on demand. Thus, in the absence of any impairment on the financial assets, the carrying amount approximates the fair value.

Fair value hierarchy and measurements

The Bank ranks its investment securities based on the hierarchy of valuation techniques required by IFRS, which is determined based on whether the inputs to those valuation techniques are observable or unobservable. Observable inputs reflect market data obtained from independent sources; unobservable inputs reflect the Bank's market assumptions. These two types of inputs lead to the following fair value hierarchy:

Level 1 – Quoted prices (unadjusted) in active markets for identical assets or liabilities.

Level 2 – Inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (that is, as prices) or indirectly (that is, derived from prices).

Level 3 – Inputs for the asset or liability that are not based on observable market data (unobservable inputs).

This hierarchy requires the use of observable market data when available. The Bank considers relevant and observable market prices in its valuations where possible.



The Central Bank of The Bahamas

Notes to the Financial Statements

December 31, 2018

(Continued)

28. Fair Value Measurements (Continued)

Fair value hierarchy and measurements (continued)

The level in the fair value hierarchy within which the fair value measurement is categorized in its entirety is determined on the basis of the lowest level input that is significant to the fair value measurement in its entirety. For this purpose, the significance of an input is assessed against the fair value measurement in its entirety. If a fair value measurement uses observable inputs that require significant adjustment based on unobservable inputs, that measurement is a Level 3 measurement. Assessing the significance of a particular input to the fair value measurement in its entirety requires judgment, considering factors specific to the asset.

The determination of what constitutes ‘observable’ requires significant judgment by the Bank. The Bank considers observable data to be that market data that is readily available, regularly distributed or updated, reliable and verifiable, not proprietary, and provided by independent sources that are actively involved in the relevant market.

The fair value of financial instruments traded in active markets is based on quoted market prices at the statement of financial position date. A market is regarded as active if quoted prices are readily and regularly available from the exchange, dealer, broker, industry group, pricing service or regulatory agency, and those prices represent actual and regularly occurring market transactions on an arm’s length basis. These instruments are included in Level 1.

Financial instruments that trade in markets that are not considered to be active but are valued based on quoted market prices, dealer quotations or alternative pricing sources supported by observable inputs are classified within Level 2. These include government debt securities and other securities with observable inputs.

Financial instruments classified within Level 3 have significant unobservable inputs, as they trade infrequently. Level 3 instruments include unlisted securities that have significant unobservable components, including equity securities.



The Central Bank of The Bahamas

Notes to the Financial Statements December 31, 2018 (Continued)

28. Fair Value Measurements (Continued)

Fair value hierarchy and measurements (continued)

The following table categorizes into three levels the inputs to measure fair value of financial instruments:

Financial assets and liabilities that are measured at fair value on a recurring basis

	Fair value measurements as at December 31, 2018			Total \$
	Level 1 \$	Level 2 \$	Level 3 \$	
FINANCIAL ASSETS				
Financial assets at fair value through profit or loss				
Marketable Securities	101,761,419	-	-	101,761,419
International Monetary Fund:				
Bahamas reserve tranche	26,821,805	-	-	26,821,805
Special Drawing rights - holdings	123,190,711	-	-	123,190,711
Financial assets at fair value through Other Comprehensive income				
Bahamas Government Treasury bills	-	155,736,831	-	155,736,831
Bahamas Government Registered Stock	-	249,036,288	-	249,036,288
FINANCIAL LIABILITIES				
Financial liabilities at fair value through profit or loss				
International Monetary Fund:				
Special drawing rights allocation	173,347,897	-	-	173,347,897



The Central Bank of The Bahamas

Notes to the Financial Statements December 31, 2018 (Continued)

28. Fair Value Measurements (Continued)

Fair value hierarchy and measurements (continued)

Financial assets and liabilities that are measured at fair value on a recurring basis (continued)

	Fair value measurements as at December 31, 2017			Total \$
	Level 1	Level 2	Level 3	
	\$	\$	\$	
FINANCIAL ASSETS				
Financial assets at fair value through profit or loss				
International Monetary Fund:				
Bahamas reserve tranche	27,464,827	-	-	27,464,827
Special Drawing rights - holdings	76,784,418	-	-	76,784,418
Available-for-sale financial assets				
Bahamas Government Treasury bills	-	7,169,543	-	7,169,543
FINANCIAL LIABILITIES				
Financial liabilities at fair value through profit or loss				
International Monetary Fund:				
Special drawing rights allocation	177,399,213	-	-	177,399,213

Level 3

The Bank does not have a level three classification at December 31, 2018 and 2017.

There were no transfers between levels in the year.

Financial assets and liabilities that are not measured at fair value on a recurring basis.

	Fair value measurements as at December 31, 2018			Total \$
	Level 1	Level 2	Level 3	
	\$	\$	\$	
FINANCIAL ASSETS				
Cash and deposits with banks	375,798,734	-	-	375,798,734
Financial assets held at amortised cost				
Bahamas Development Bank bonds	-	4,049,834	-	4,049,834
Advances to Bahamas Government	-	120,367,448	-	120,367,448
Loans to Bahamas Development Bank	-	2,509,158	-	2,509,158
Bridge Authority bonds	-	493,487	-	493,487
Employee loans and other receivables	-	8,187,757	-	8,187,757
Foreign Government Securities	568,768,827	-	-	568,768,827
Clifton Heritage Authority bonds	-	638,069	-	638,069



The Central Bank of The Bahamas

Notes to the Financial Statements December 31, 2018 (Continued)

28. Fair Value Measurements (Continued)

Fair value hierarchy and measurements (continued)

Financial assets and liabilities that are not measured at fair value on a recurring basis (continued)

	Fair value measurements as at December 31, 2018			Total \$
	Level 1	Level 2	Level 3	
	\$	\$	\$	
FINANCIAL LIABILITIES				
Other financial liabilities				
Notes in circulation	430,888,855	-	-	430,888,855
Coins in circulation	28,970,923	-	-	28,970,923
Deposits by commercial banks	-	791,668,258	-	791,668,258
Deposits by Bahamas Government and Bahamas Government agencies	-	96,155,504	-	96,155,504
Deposits by international agencies	-	255,302	-	255,302
Accounts payable and other liabilities	-	29,002,444	-	29,002,444
Investment Currency Market payable	-	9,007,273	-	9,007,273

	Fair value measurements as at December 31, 2017			Total \$
	Level 1	Level 2	Level 3	
	\$	\$	\$	
FINANCIAL ASSETS				
Cash and deposits with banks	698,567,924	-	-	698,567,924
Loans and receivables				
Bahamas Development Bank bonds	-	4,091,984	-	4,091,984
Advances to Bahamas Government	-	135,360,600	-	135,360,600
Bahamas Government Registered Stocks	-	274,511,585	-	274,511,585
Loans to Bahamas Development Bank	-	2,759,867	-	2,759,867
Bridge Authority bonds	-	491,351	-	491,351
Employee loans and other receivables	-	9,784,592	-	9,784,592
Held-to-maturity investments				
Foreign Government Securities	614,662,080	-	-	614,662,080
Clifton Heritage Authority bonds	-	638,069	-	638,069

FINANCIAL LIABILITIES

Other financial liabilities

Notes in circulation	411,120,706	-	-	411,120,706
Coins in circulation	27,396,830	-	-	27,396,830
Deposits by commercial banks	-	1,011,246,639	-	1,011,246,639
Deposits by Bahamas Government and Bahamas Government agencies	-	44,152,152	-	44,152,152
Deposits by international agencies	-	255,217	-	255,217
Accounts payable and other liabilities	-	11,110,160	-	11,110,160
Investment Currency Market payable	-	8,736,314	-	8,736,314



The Central Bank of The Bahamas

Notes to the Financial Statements

December 31, 2018

(Continued)

28. Fair Value Measurements (Continued)

Fair value hierarchy and measurements (continued)

Financial assets and liabilities that are not measured at fair value on a recurring basis (continued)

The fair value of the financial assets and liabilities disclosed under level 2 and 3 above have been determined considering, amongst other factors, discounted cash flows, with the most significant input being the Bahamian prime rate as the discount rate. The Bahamian dollar Prime rate was reduced by 0.50% effective January 2017, and prior to this change Prime rate had not experienced any changes since the year ended December 31, 2011.

29. Risk Management

The Bank's activities expose it to a variety of financial risks and those activities involve the analysis, evaluation, acceptance and management of some degree of risk or combination of risks. Taking risk is core to the financial business, and the operational risks are an inevitable consequence of being in business. The Bank's aim is therefore to achieve an appropriate balance between risk and return and minimise potential adverse effects on the Bank's financial performance. From this perspective, the Bank considers certain non-financial assets and liabilities in its overall risk management assessment.

The most important types of risks are credit risk, liquidity risk, market risk and operational risk. Market risk includes currency risk and interest rate risk.

The Bank's risk management policies are designed to identify and analyse these risks, to set appropriate risk limits and controls, and to monitor the risks and adherence to limits by means of reliable and up-to-date information systems. The Bank regularly reviews its risk management policies and systems to reflect changes in markets, products and emerging best practices.

Risk management is carried out by the investment and monetary policy committees under policies approved by the Board of Directors. The committees identify, evaluate and hedge financial risks in close co-operation with the Bank's operating units. The Board provides written principles for overall risk management, as well as written policies covering specific areas, such as foreign exchange risk, interest rate risk, credit risk and financial instruments.



The Central Bank of The Bahamas

Notes to the Financial Statements December 31, 2018 (Continued)

29. Risk Management (Continued)

Credit risk

The Bank takes on exposure to credit risk, which is the risk that a counterparty will cause a financial loss for the Bank by failing to discharge an obligation. Significant changes in the economy, or in the health of a particular segment that represents a concentration in the Bank's portfolio, could result in losses that are different from those provided for at the statement of financial position date. Credit exposures arise principally in loans and advances, debt securities and other bills in the Bank's asset portfolio. The Investment Committee monitors credit risk management and control, and regular reports are provided to the Board of Directors. The Directors do not consider that the Bank is exposed to any significant credit risk because its financial assets consist primarily of cash and securities issued or guaranteed by the United States Governments or The Bahamas Government. Accordingly the Bank has not established a provision for its financial assets. Maximum credit exposure at the year end approximates the carrying value of all assets.

Exposure to credit risk

The credit quality of financial assets that are neither past due nor impaired can be assessed by reference to external credit ratings or to historical information about counterparty default rates.

	2018	2017
	\$	\$
Cash and deposits with banks		
Aaa	202,143,811	218,092
Aa2	56,001,935	33,774,567
A1	86,454,207	261,438,414
Aa1	20,391,928	22,089,466
Aa3	10,112,778	94,255,610
A2	-	-
A3	-	-
Ba2	-	33,059,022
Ba3	-	253,229,528
Baa3	-	-
	<u>375,104,659</u>	<u>698,064,699</u>
Bahamas Development Bank Bonds		
Baa3	4,049,834	4,091,984
Advances to Bahamas Government		
Baa3	120,367,448	135,360,600
Bahamas Government Registered Stock		
Baa3	249,036,288	274,511,585
Loans to Bahamas Development Bank		
Baa3	2,509,158	2,759,867
Bridge Authority Bonds		
Baa3	493,487	491,351



The Central Bank of The Bahamas

Notes to the Financial Statements

December 31, 2018

(Continued)

29. Risk Management (Continued)

Credit risk (continued)

Exposure to credit risk (continued)

	2018	2017
	\$	\$
Receivables and Other Assets	8,187,757	9,784,592
Bahamas Government Treasury Bills		
Baa3	155,736,831	7,169,543
Foreign Government Securities		
Aaa	568,768,827	614,662,080
Marketable Securities		
Aaa	101,761,419	-
Clifton Heritage authority bonds		
Baa3	638,069	638,069
International Monetary Fund		
Bahamas reserve tranche	26,821,805	27,464,827
Special drawing rights - holdings	123,190,711	76,784,418
	<u>150,012,516</u>	<u>104,249,245</u>
	<u>1,736,666,293</u>	<u>1,851,783,615</u>

Market risk

The Bank takes on exposure to market risk, which is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market prices. Market risks arise from open positions in interest rate, currency and equity products, all of which are exposed to general and specific market movements and changes in the level of volatility of market rates or prices such as interest rates, credit spreads, foreign exchange rates and equity prices. The Bank's exposure to market risk is from its financial investment portfolios.

The market risks arising from the Bank's activities are monitored by the Investment Committee and the Monetary Policy Committee. Regular reports are submitted to the Board of Directors and operating units.

Currency risk

Apart from the Bank's assets and liabilities with the IMF, which are denominated in SDRs, its exposure to foreign currency risk is limited. The only other significant foreign currency is US dollar, on which there is no exposure because the Bahamian dollar and the US dollar are pegged 1:1. The Bank manages any other foreign currency exposure using internal hedging techniques, by matching assets and liabilities wherever possible.

The following table presents the carrying amounts of the Bank's financial assets and liabilities by currency:



The Central Bank of The Bahamas

Notes to the Financial Statements December 31, 2018 (Continued)

29. Risk Management (Continued)

Currency risk (continued)

*(BSD equivalent)

As of December 31, 2018	B SD	USD*	GBP*	EUR*	Other*	SDR*	Total
Financial Assets							
Cash and deposits with banks	37,828	375,733,778	192	6	26,930	-	375,798,734
Foreign Government Securities	-	568,768,827	-	-	-	-	568,768,827
Marketable Securities	-	101,761,419	-	-	-	-	101,761,419
International Monetary Fund:							
Bahamas reserve tranche	-	-	-	-	-	26,821,805	26,821,805
Special drawing rights - holdings	-	-	-	-	-	123,190,711	123,190,711
Domestic financial assets	541,018,872	-	-	-	-	-	541,018,872
Total financial assets	541,056,700	1,046,264,024	192	6	26,930	150,012,516	1,737,360,368
Financial Liabilities							
Notes in circulation	430,888,855	-	-	-	-	-	430,888,855
Coins in circulation	28,970,923	-	-	-	-	-	28,970,923
Deposits by commercial banks	791,668,258	-	-	-	-	-	791,668,258
Deposits by Bahamas Government and Bahamas Government agencies	96,155,504	-	-	-	-	-	96,155,504
Deposits by international agencies	-	255,302	-	-	-	-	255,302
Accounts payable and other liabilities	29,002,444	-	-	-	-	-	29,002,444
Investment Currency Market payable	9,007,273	-	-	-	-	-	9,007,273
International Monetary Fund:							
Special drawing rights allocation	-	-	-	-	-	173,347,897	173,347,897
Total financial liabilities	1,385,693,257	255,302	-	-	-	173,347,897	1,559,296,456
Net on-balance sheet position	(844,636,557)	1,046,008,722	192	6	26,930	(23,335,381)	178,063,912



The Central Bank of The Bahamas

Notes to the Financial Statements December 31, 2018 (Continued)

29. Risk Management (Continued)

Currency risk (continued) *(BSD equivalent)

As of December 31, 2017

Financial Assets	BSD	USD*	GBP*	EUR*	Other*	SDR*	Total
Cash and deposits with banks	32,190	698,535,500	5	65	164	-	698,567,924
Foreign Government Securities	-	614,662,080	-	-	-	-	614,662,080
International Monetary Fund: Bahamas reserve tranche	-	-	-	-	-	27,464,827	27,464,827
Special drawing rights - holdings	-	-	-	-	-	76,784,418	76,784,418
Domestic financial assets	434,807,591	-	-	-	-	-	434,807,591
Total financial assets	434,839,781	1,313,197,580	5	65	164	104,249,245	1,852,286,840
Financial Liabilities							
Notes in circulation	411,120,706	-	-	-	-	-	411,120,706
Coins in circulation	27,396,830	-	-	-	-	-	27,396,830
Deposits by commercial banks	1,011,246,639	-	-	-	-	-	1,011,246,639
Deposits by Bahamas Government and Bahamas Government agencies	44,152,152	-	-	-	-	-	44,152,152
Deposits by international agencies	-	255,217	-	-	-	-	255,217
Accounts payable and other liabilities	11,110,160	-	-	-	-	-	11,110,160
Investment Currency Market payable	8,736,314	-	-	-	-	-	8,736,314
International Monetary Fund: Special drawing rights allocation	-	-	-	-	-	177,399,213	177,399,213
Total financial liabilities	1,513,762,801	255,217	-	-	-	177,399,213	1,691,417,231
Net on-balance sheet position	(1,078,923,020)	1,312,942,363	5	65	164	(73,149,968)	160,869,609



The Central Bank of The Bahamas

Notes to the Financial Statements

December 31, 2018

(Continued)

29. Risk Management (Continued)

Currency risk (continued)

Sensitivity of BSD compared to foreign currencies reflected in these financial statements is as follows:

	<u>Average Rate</u>		<u>Year-end Spot Rate</u>	
	2018	2017	2018	2017
USD1	1.0000	1.0000	1.0000	1.0000
GBP 1	1.3312	1.2900	1.2791	1.3503
EUR 1	1.1784	1.1300	1.1447	1.1910
SDR 1	1.4142	1.4055	1.3908	1.4154

Special Drawing Rights (SDRs), the IMF's unit of account, is essentially a specified basket of five (5) major international currencies (i.e., the U.S. Dollar, Euro, Japanese Yen, Pound Sterling and Chinese Renminbi). The weightage of each currency is as follows:

<u>Currency</u>	<u>Weight</u>
USD	41.73%
EUR	30.90%
JPY	10.92%
GBP	8.09%
CNY	8.33%
	<u>100.00%</u>

At December 31, 2018, if BSD had weakened/strengthened by 10% against SDR with all other variables held constant, comprehensive income for the year would have been BSD 12,319,071 (2017: BSD 7,496,305) higher/lower, mainly as a result of foreign exchange gains/losses on translation of SDR-denominated financial assets and liabilities.

Interest rate risk

Cash flow interest rate risk is the risk that the future cash flows of a financial instrument will fluctuate because of changes in market interest rates. Fair value interest rate risk is the risk that the value of a financial instrument will fluctuate because of changes in market interest rates. The Bank takes on exposure to the effects of fluctuations in the prevailing levels of market interest rates on both its fair value and cash flow risks. Interest margins may increase as a result of such changes but may decrease or create losses in the event that unexpected movements arise. The level of mismatch of interest rate repricing that may be undertaken by the Bank is monitored frequently by the Investment Committee and the Monetary Policy Committee.



The Central Bank of The Bahamas

Notes to the Financial Statements December 31, 2018 (Continued)

29. Risk Management (Continued)

Interest rate risk (continued)

Certain of the Bank's financial assets and liabilities are exposed to interest rate risk. Foreign Government securities carry an average yield of 2.23% (2017: 1.48%); however, if these securities had a reduced average yield of 2.16% (2017: 1.39%), derived from their varying yields at the lower end of the spectrum, income for the year and equity at year end would have been reduced by \$556,997 (2017: \$502,070). Had the yield been tilted towards the higher end of the spectrum, to 2.23% (2017: 1.39%), income for the year and equity at year end would have increased by \$556,997 (2017: \$502,070).

In respect of all variable interest bearing instruments, if interest rates had been 50 basis points higher, with all other variables remaining constant, the increase in equity and net operating results for the year would amount to approximately \$807,274 (2017: \$890,455), arising from variable rate instruments. If interest rates had decreased by 50 basis points, the decrease in equity and net operating results for the year would amount to approximately \$(807,274) (2017: \$(890,455)).

	December 31, 2018	December 31, 2017
	\$	\$
Fixed Rate Instruments		
Financial assets	1,221,187,573	1,362,661,691
Financial liabilities	-	-
Variable Rate Instruments		
Financial assets	503,949,062	479,783,347
Financial liabilities	173,347,897	177,399,213

Liquidity risk

Liquidity risk is the risk that the Bank is unable to meet its payment obligations associated with its financial liabilities when they fall due, and to replace funds when they are withdrawn. The consequence may be the failure to meet obligations to repay depositors and fulfill commitments to lend.

The Bank manages its foreign liquidity risks through appropriate structuring of its foreign investment portfolios to ensure that the maturity profiles of foreign assets sufficiently match those of foreign commitments. This is monitored and managed on a regular basis. In addition, the Bank's foreign investment portfolio comprises mainly short-term, highly liquid investment instruments.



The Central Bank of The Bahamas

Notes to the Financial Statements December 31, 2018 (Continued)

29. Risk Management (Continued)

Liquidity risk (continued)

The Bank's liquidity risk management process, as carried out within the Bank, includes:

- Day-to-day funding, managed by monitoring future cash flows to ensure that requirements can be met, inclusive of replenishment of funds as they mature. The Bank maintains an active presence in global money markets to enable this to happen;
- Maintaining a portfolio of highly marketable assets that can easily be liquidated as protection against any unforeseen interruption to cash flow;
- Monitoring statement of financial position liquidity ratios against internal and statutory requirements; and
- Managing the concentration and profile of debt and financial instrument maturities.

The table below analyses financial assets and liabilities into relevant maturity groupings based on the remaining period to the contractual maturity dates as of the statement of financial position date and represent undiscounted cash flows.



The Central Bank of The Bahamas

Notes to the Financial Statements December 31, 2018 (Continued)

29. Risk Management (Continued)

Liquidity risk (continued)

Period of maturity As of December 31, 2018	Up to 1 month \$	1 to 3 months \$	3 months to 1 year \$	1 to 5 years \$	Over 5 years \$	Total \$
Financial Assets						
Cash and deposits with banks	25,556,470	40,823,611	309,418,653	-	-	375,798,734
Marketable securities issued or guaranteed by foreign governments	-	-	117,076,107	315,780,298	237,673,841	670,530,246
International Monetary Fund:						
Bahamas reserve tranche	26,821,805	-	-	-	-	26,821,805
Special drawing rights – holdings	123,190,711	-	-	-	-	123,190,711
Bahamas Development Bank bonds	-	-	-	-	4,049,834	4,049,834
Advances to Bahamas Government	120,367,448	-	-	-	-	120,367,448
Bahamas Government Registered stock	-	5,353	16,784,494	79,543,054	152,703,387	249,036,288
Bahamas Government Treasury Bills	-	45,705,096	110,031,735	-	-	155,736,831
Loans to Bahamas Development Bank	-	-	-	-	2,509,158	2,509,158
Bridge Authority bonds	-	454,582	-	38,905	-	493,487
Clifton Heritage Authority bonds	-	-	-	-	638,069	638,069
Receivables and other accounts	-	-	1,904,335	1,913,903	4,369,519	8,187,757
Total financial assets	295,936,434	86,988,642	555,215,324	397,276,160	401,943,808	1,737,360,368



The Central Bank of The Bahamas

Notes to the Financial Statements December 31, 2018 (Continued)

29. Risk Management (Continued)

Liquidity risk (continued)

Period of maturity As of December 31, 2018	Up to 1 month \$	1 to 3 months \$	3 months to 1 year \$	1 to 5 years \$	Over 5 years \$	Total \$
Financial Liabilities						
Notes in circulation	430,888,855	-	-	-	-	430,888,855
Coins in circulation	28,970,923	-	-	-	-	28,970,923
Deposits by commercial banks and Bahamas Government	791,668,258	-	-	-	-	791,668,258
Deposits by International agencies	96,155,504	-	-	-	-	96,155,504
Accounts payable and other liabilities	255,302	-	-	-	-	255,302
Investment Currency Market payable	29,002,444	-	-	-	-	29,002,444
International Monetary Fund: Special drawing rights allocation	9,007,273	-	-	-	-	9,007,273
	173,347,897	-	-	-	-	173,347,897
Total financial liabilities	1,559,296,456	-	-	-	-	1,559,296,456
Net on-balance sheet position	(1,263,360,022)	86,988,642	555,215,324	397,276,160	401,943,808	178,063,912



The Central Bank of The Bahamas

Notes to the Financial Statements December 31, 2018 (Continued)

29. Risk Management (Continued)

Liquidity risk (continued)

Period of maturity As of December 31, 2017	Up to 1 month \$	1 to 3 months \$	3 months to 1 year \$	1 to 5 years \$	Over 5 years \$	Total \$
Financial Assets						
Cash and deposits with banks	543,963,708	65,187,315	89,416,901	-	-	698,567,924
Foreign Government Securities	-	-	-	302,738,213	311,923,867	614,662,080
International Monetary Fund:						
Bahamas reserve tranche	27,464,827	-	-	-	-	27,464,827
Special drawing rights – holdings	76,784,418	-	-	-	-	76,784,418
Bahamas Development Bank bonds	-	-	-	-	4,091,984	4,091,984
Advances to Bahamas Government	135,360,600	-	-	-	-	135,360,600
Bahamas Government Registered stocks	-	127,211	395,910	100,312,237	173,676,227	274,511,585
Bahamas Government Treasury Bills	-	7,169,543	-	-	-	7,169,543
Loans to Bahamas Development Bank	-	-	-	-	2,759,867	2,759,867
Bridge Authority bonds	-	-	-	453,905	37,446	491,351
Clifton Heritage Authority bonds	-	-	-	-	638,069	638,069
Employee and other receivables	230,437	3,753	48,573	2,766,681	6,735,148	9,784,592
Total financial assets	783,803,990	72,487,822	89,861,384	406,271,036	499,862,608	1,852,286,840



The Central Bank of The Bahamas

Notes to the Financial Statements December 31, 2018 (Continued)

29. Risk Management (Continued)

Liquidity risk (continued)

Period of maturity As of December 31, 2017	Up to 1 month \$	1 to 3 months \$	3 months to 1 year \$	1 to 5 years \$	Over 5 years \$	Total \$
Financial Liabilities						
Notes in circulation	411,120,706	-	-	-	-	411,120,706
Coins in circulation	27,396,830	-	-	-	-	27,396,830
Deposits by commercial banks	1,011,246,639	-	-	-	-	1,011,246,639
Deposits by Bahamas Government and Bahamas Government agencies	44,152,152	-	-	-	-	44,152,152
Deposits by International agencies	255,217	-	-	-	-	255,217
Accounts payable and other liabilities	11,110,160	-	-	-	-	11,110,160
Investment Currency Market payable	8,736,314	-	-	-	-	8,736,314
International Monetary Fund: Special drawing rights allocation	177,399,213	-	-	-	-	177,399,213
Total financial liabilities	1,691,417,231	-	-	-	-	1,691,417,231
Net on-balance sheet position	(907,613,241)	72,487,822	89,861,384	406,271,036	499,862,608	160,869,609



The Central Bank of The Bahamas

Notes to the Financial Statements December 31, 2018 (Continued)

29. Risk Management (Continued)

Operational risk

Operational risk is the risk of loss arising from systems failure, human error, fraud or external events. When controls fail to perform, operational risks can cause damage to reputation, have legal or regulatory implications, or lead to financial loss. The Bank cannot expect to eliminate all operational risks, but it endeavours to manage these risks through a control framework and by monitoring and responding to potential risks. Controls include effective segregation of duties, access, authorisation and reconciliation procedures, staff education and assessment processes, such as the use of internal audit.

30. Retirement Benefit Plans

Defined Contribution Plan

	2018	2017
	\$	\$
Amount recognised as an expense (Note 21)	297,169	238,663

Defined Benefit Plan

The movements in the contributory defined benefit obligation over the year are as follows:

	2018	2017
	\$	\$
Present value of obligation at start of year	54,181,841	53,273,856
Interest cost	2,677,447	2,606,904
Current service cost	1,970,408	2,034,655
Benefits paid	(5,384,938)	(2,271,556)
Actuarial (gain)/loss on obligation due to experience	(981,223)	237,203
Actuarial loss on obligation due to demographic assumption changes	1,506,010	-
Actuarial gain on obligation due to financial assumption changes	(2,281,552)	(1,699,221)
Present value of obligation at end of year	<u>51,687,993</u>	<u>54,181,841</u>
Fair value of plan assets at start of year	59,874,621	57,337,631
Interest income	3,026,432	2,862,747
Contributions paid – both employees’ and employer’s	2,043,856	2,122,923
Benefits paid	(5,384,938)	(2,271,556)
Administrative costs	(6,945)	(16,740)
Return on plan assets, excluding interest income	56,147	(160,384)
Fair value of plan assets at end of year	<u>59,609,173</u>	<u>59,874,621</u>



The Central Bank of The Bahamas

Notes to the Financial Statements December 31, 2018 (Continued)

30. Retirement Benefit Plans (Continued)

Defined Benefit Plan (continued)

The amount recognised as an asset in the statement of financial position in respect of the Bank's contributory defined retirement benefit plan is as follows:

	2018 \$	2017 \$
Present value of funded obligations	51,687,993	54,181,841
Fair value plan assets	<u>(59,609,173)</u>	<u>(59,874,621)</u>
	<u>(7,921,180)</u>	<u>(5,692,780)</u>

Summary of plan investments, in accordance with IAS 19 is as follows:

	2018 \$	2017 \$
Cash	872,727	2,400,890
Interest receivable	709,120	678,974
Bahamas Government Registered Stocks	56,770,235	55,659,335
Other bonds	849,421	446,272
Equity securities	700,000	700,000
Accounts payable	<u>(292,330)</u>	<u>(10,850)</u>
Total	<u>59,609,173</u>	<u>59,874,621</u>

The expense recognised in the statement of comprehensive income in respect of the Bank's contributory defined retirement benefit plan is as follows:

	2018 \$	2017 \$
Current service cost	1,547,547	1,593,495
Administrative cost	6,945	16,740
Net interest income	<u>(348,984)</u>	<u>(255,843)</u>
	<u>1,205,508</u>	<u>1,354,392</u>
Remeasurements recognised in OCI	(1,812,912)	(1,301,634)



The Central Bank of The Bahamas

Notes to the Financial Statements December 31, 2018 (Continued)

30. Retirement Benefit Plans (Continued)

Defined Benefit Plan (continued)

Movements in the net assets recorded in the statement of financial position are as follows:

	2018 \$	2017 \$
Net assets at beginning of year	(5,692,780)	(4,063,775)
Net expense recognised in net income	1,205,508	1,354,392
Employer contributions	(1,620,996)	(1,681,763)
Remeasurements recognised in OCI	(1,812,912)	(1,301,634)
	<u>(7,921,180)</u>	<u>(5,692,780)</u>

The Bank intends to contribute approximately 18.9% of gross payroll to the plan during 2019 (2018: actual 18.9%).

Principal actuarial assumptions used at the statement of financial position date are as follows:

	2018	2017
Discount rate	5.50%	5.20%
Expected rate of salary increase at age 18	4.00%	4.00%
Expected rate of salary increase at age 59	4.00%	4.00%
Cost of living adjustment for active employees	1.25%	1.25%

The actual return on plan assets during the year was \$3,082,578 (2017: \$2,702,363).

Sensitivity and other results

The benefit obligation as at year-end is distributed as follows:

	2018 \$	2017 \$
Pensioners	14,678,734	13,583,810
Vesting actives	34,452,589	39,530,802
Deferred actives	-	-
Unvested actives	2,556,670	1,067,229
	<u>51,687,993</u>	<u>54,181,841</u>

The pensioner liability of \$14,678,734 (2017: \$13,583,810), includes \$1,990,960 (2017: \$2,605,283) relating to assumed cost of living adjustments.



The Central Bank of The Bahamas

Notes to the Financial Statements

December 31, 2018

(Continued)

30. Retirement Benefit Plans (Continued)

Sensitivity and other results (continued)

The liability for actives of \$34,452,589 (2017: \$39,530,802), includes \$1,962,291 (2017: \$1,346,535) relating to assumed cost of living adjustments and \$7,807,528 (2017: \$7,317,097) relating to assumed future salary increases.

The following table illustrates the changes or sensitivity of the benefit obligation as at December 31, 2018 for 1% changes in discount rate and salary increases.

	2018		2017	
	1% Increase \$	1% Decrease \$	1% Increase \$	1% Decrease \$
Discount	(6,903,383)	8,684,854	(7,420,950)	9,366,230
Future salary increases	2,050,259	(1,855,040)	2,331,289	(2,105,627)

If all members lived one year longer than projected, the liability at year-end would be \$52,678,666 (2017: \$55,304,406).

If the discount rate remained at 5.2% and mortality remained unchanged, the benefit obligation would be \$52,463,535 (2017: No change in discount rate).

The weighted average duration of the defined benefit obligation at December 31, 2018 is 14.9 years (2017: 15.3 years).

31. Health Insurance Subsidy Benefit for Retirees

The movement in the health insurance subsidy for retirees over the year is as follows:

	2018 \$	2017 \$
Present value of obligation at start of year	3,112,941	2,951,833
Interest cost	158,214	144,297
Current service cost	106,203	95,692
Benefits paid	(140,718)	(131,801)
Actuarial (gain)/loss on obligation due to experience	(44,335)	27,035
Actuarial loss/(gain) on obligation due to financial assumption change	118,441	(76,506)
Actuarial (gain)/loss on obligation due to demographic assumption change	(120,470)	102,391
Present value of obligation at end of year	<u>3,190,276</u>	<u>3,112,941</u>
Contribution paid – employees’ and employers’ contributions	140,718	131,801
Benefits paid	(140,718)	(131,801)
	<u>-</u>	<u>-</u>



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Notes to the Financial Statements December 31, 2018 (Continued)

31. Health Insurance Subsidy Benefit for Retirees (Continued)

The expense recognised in the statement of comprehensive income in respect of the health insurance subsidy benefit for retirees is as follows:

	2018 \$	2017 \$
Current service cost	106,203	95,692
Net interest cost	<u>158,214</u>	<u>144,297</u>
	<u>264,417</u>	<u>239,989</u>
Remeasurements recognised in OCI	(46,364)	52,920

Movements in the net liability recorded in the statement of financial position are as follows:

	2018 \$	2017 \$
Net liability at beginning of year	3,112,941	2,951,833
Net expense recognised in net income	264,417	239,989
Employer contributions	(140,718)	(131,801)
Remeasurements recognised in OCI	<u>(46,364)</u>	<u>52,920</u>
	<u>3,190,276</u>	<u>3,112,941</u>

Principal actuarial assumptions used at the statement of financial position date are as follows:

	2018	2017
Discount rate	5.50%	5.20%
Rate of Medical Subsidy Increases	0.00%	0.00%

Sensitivity and Other Results

The benefit obligation as at year-end comprises:

	2018 \$	2017 \$
Pensioners	1,671,425	1,474,690
Actives	<u>1,518,851</u>	<u>1,638,251</u>
Total	<u>3,190,276</u>	<u>3,112,941</u>



The Central Bank of The Bahamas

Notes to the Financial Statements December 31, 2018 (Continued)

31. Health Insurance Subsidy Benefit for Retirees (Continued)

Sensitivity and Other Results (Continued)

The following table illustrates the changes or sensitivity of the benefit obligation as at December 31, 2018 for 1% changes in discount rate.

	2018		2017	
	1% Increase \$	1% Decrease \$	1% Increase \$	1% Decrease \$
Discount rate	(352,966)	432,776	(354,508)	436,157

If all members lived one year longer than projected, the liability would be \$3,259,292 (2017: \$3,187,982).

If the discount rate remained unchanged from 5.2% and mortality assumption remained unchanged the benefit obligation would decrease by \$5,000.

The weighted average duration of the defined benefit obligation at December 31, 2018 is 12.2 years (2017: 12.6 years).

32. Retirement Benefit Plan for Governors and Deputy Governors

The movements in the non-contributory defined benefit obligation over the year are as follows:

	2018 \$	2017 \$
Present value of obligation at start of year	4,188,009	4,277,451
Interest cost	210,431	202,841
Current service cost	189,747	188,384
Benefits paid	(282,500)	(441,250)
Actuarial (gain)/loss on obligation due to experience	(92,856)	48,214
Actuarial loss on obligation due to demographic assumption change	146,450	-
Actuarial (gain) on obligation due to financial assumption change	(126,931)	(87,631)
Present value of obligation at end of year	4,232,350	4,188,009
Fair value of plan assets at start of year	-	-
Expected return on plan assets	101,544	-
Contributions - Employer	4,188,009	441,250
Benefits paid	(282,500)	(441,250)
Actuarial gain on plan assets	80,935	-
Fair value of plan assets at end of year	4,087,988	-



The Central Bank of The Bahamas

Notes to the Financial Statements

December 31, 2018

(Continued)

32. Retirement Benefit Plan for Governors and Deputy Governors (Continued)

The amount recognised as a liability in the statement of financial position in respect of the Bank's non-contributory defined retirement benefit plan for governors and deputy governors is as follows:

	2018	2017
	\$	\$
Present value of funded obligations	4,232,350	4,188,009
Fair value of plan assets	(4,087,988)	-
	<u>144,362</u>	<u>4,188,009</u>

The expense recognised in the statement of comprehensive income in respect of the Bank's non-contributory defined retirement benefit plan for governors and deputy governors is as follows:

	2018	2017
	\$	\$
Current service cost	189,747	188,384
Net interest expense	<u>108,888</u>	<u>202,841</u>
	<u>298,635</u>	<u>391,225</u>
Remeasurements recognised in OCI	(154,273)	(39,417)

Movements in the net liability recorded in the statement of financial position are as follows:

	2018	2017
	\$	\$
Net liability at beginning of year	4,188,009	4,277,451
Net expense recognised in net income	298,635	391,225
Employer contributions	(4,188,009)	(441,250)
Remeasurements recognised in OCI	<u>(154,273)</u>	<u>(39,417)</u>
	<u>144,362</u>	<u>4,188,009</u>



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Notes to the Financial Statements December 31, 2018 (Continued)

32. Retirement Benefit Plan for Governors and Deputy Governors (Continued)

Principal actuarial assumptions used at the statement of financial position date are as follows:

	2018	2017
Discount rate at end of year	5.50%	5.20%
Salary increase (p.a.)	3.50%	3.50%
Cost of living adjustment for pensioners (p.a.)	3.50%	3.50%

Sensitivity and other results

The benefit obligation as at year-end is distributed as follows:

	2018	2017
	\$	\$
Pensioners	3,830,599	3,957,335
Actives - Vested	-	-
Actives - Unvested	<u>401,751</u>	<u>230,674</u>
	<u>4,232,350</u>	<u>4,188,009</u>

The pensioner liability of \$3,830,599 (2017: \$3,957,335) includes \$976,747 (2017: \$1,051,927) relating to assumed cost of living adjustments, and \$976,747 (2017: \$1,040,621) relating to assumed future salary increases.

The liability for actives of \$401,751 (2017: \$230,674) includes \$108,222 (2017: \$58,329) relating to assumed cost of living adjustments and \$158,874 (2017: \$98,227) relating to assumed future salary increases.



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Notes to the Financial Statements

December 31, 2018

(Continued)

32. Retirement Benefit Plan for Governors and Deputy Governors (Continued)

The following table illustrates the changes or sensitivity of the benefit obligation as at December 31, 2018 for 1% changes in discount rate and salary increases.

	2018		2017	
	1% Increase \$	1% Decrease \$	1% Increase \$	1% Decrease \$
Discount	(395,571)	471,635	(395,464)	471,268
Future salary increases	22,128	(21,072)	452,922	(387,389)

If all members lived one year longer than projected, the liability at year-end would be \$4,389,536 (2017: \$4,358,283).

The weighted average duration of the defined benefit obligation at December 31, 2018 is 10.2 years (2017: 10.3 years).

33. Comparative figures

Presentation of certain comparative balances has been re-stated in order to conform with the current year's presentation.





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