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QUARTERLY OVERVIEW OF DOMESTIC ECONOMIC DEVELOPMENTS

SEPTEMBER 2006

This summary is an early release, excerpted from the upcoming issue of the Central Bank's Quarterly Economic Review for the Quarter ended September 2006. The full text of the Economic Review will be released on 12 January 2007.

The Bahamas
Review of Domestic Economic Developments for Third Quarter 2006

Indications are that the strengthening in the Bahamian economy observed in the first half of the year was maintained during the third quarter, reinforced by a continuation of strong consumer demand. Construction output also expanded as bank lending supported increased housing investments; however, weakness in both air and sea arrivals suggested a softening in tourism output. In the fiscal sector, extraordinary gains in tax revenues supported a turnaround in the overall balance, to a modest surplus for the first quarter of FY2006/07. Monetary developments featured sustained expansion in credit and a concomitant tightening in bank liquidity and decline in external reserves. On the external side, the estimated current account deficit widened, mainly linked to a decline in tourism inflows; however, the capital and financial account surplus improved, on account of increased funding of tourism related investments by overseas and domestic sources.

Reflecting the strong pace of credit expansion, net free cash balances of the banking system contracted by 7.4% to $171.2 million during the third quarter, which represented a smaller 3.6% share of Bahamian dollar deposit liabilities compared to 6.4% last year. Broader surplus liquid assets also narrowed by 15.1% to $163.8 million, for a reduction in the excess over the statutory minimum, to 20.5% from 33.1% a year-earlier. The weighted average interest rates for deposits and loans were only marginally higher at 3.31% and 9.93%, respectively, resulting in a slight up-tick in the average loan-to-deposit rate spread to 6.62%. Meanwhile, the 90-day Treasury bill rate and benchmark rates—Central Bank's Discount rate and commercial banks' Prime—were all unchanged at 0.69%, 5.25% and 5.50%, respectively.

The overall money supply (M3) contracted at a slower pace of 1.5% compared to 2.1% in 2005, placing the overall stock at $5,078.6 million. Developments included a 16.2% decline in residents' foreign currency deposits, consequent on public sector withdrawals to meet operational expenses, and a 7.8% fall-off in demand deposits. In contrast, currency in active circulation, fixed and savings deposits rose by 0.4%, 1.2% and 1.0%, respectively.

Buoyed by healthy economic conditions and a relatively low interest rate environment, domestic credit expansion was sustained during the review quarter. Total claims outstanding firmed by 3.6% to $6,525.0 million, compared to modest growth of 0.8% last year. The uptrend was associated with extended gains in private sector credit of 4.4% relative to 2.6% a year ago. The Bahamian dollar component increased by 4.6%, up from 3.8% in 2005, and private sector foreign currency credit by 1.9%, in contrast to a 7.5% contraction a year-earlier. Residential mortgages, personal overdrafts and consumer credit rose by 4.7%, 6.6% and 3.9%, respectively. Conversely, claims on the public sector were marginally reduced by 0.2%, as the 0.9% decline in net credit to Government offset the 1.1% rebound in claims on the public corporations.

In the fiscal sector, preliminary estimates of Government's budgetary operations for the first quarter of FY2006/07 showed a surplus of $3.7 million, a turnaround from a deficit of $20.3 million in the previous year. Total revenue improved by 20.3% to $326.9 million, as tax receipts gained 21.5% to $305.8 million, supported by a 38.8% surge in non-financial stamp taxes associated with real estate transactions. Developments were reinforced by a 17.3% advance in non-tax earnings to $21.1 million. Total expenditure expanded by 10.7% to $323.3 million, explained by an 8.6% increase in current outlays to $283.3 million, a 14.6% hike in capital investments to $30.3 million and a more than doubling in net lending to public corporations to $9.7 million. Budgetary financing for the first quarter of FY2006/07 included a $100.0 million Registered Stock issue and short-term advances from the Central Bank of $15.0 million. Borrowings, alongside total debt amortization of $36.3 million, which was almost entirely denominated in Bahamian dollars, resulted in a 3.5% quarterly rise in the Direct Charge on Government to $2,396.7 million. Inclusive of a 2.0% ($10.2 million) reduction in guaranteed borrowings of the public corporations, the National Debt expanded by an estimated $70.1 million (2.5%), placing the outstanding stock at $2,893.1 million.

Tourism developments during the review quarter were marked by a 8.5% downturn in visitor arrivals to 1.04 million, which reversed last year's growth of 3.5%. In particular, air traffic fell by 7.0% to 333,737 vis-à-vis a 12.8% gain in 2005; and sea arrivals, which accounted for 67.8% of visitors, decreased by 9.2% to 702,789. Port of entry data revealed that New Providence, which received 60.3% of the quarter's arrivals, recorded a fall-off of 9.4%, as air and sea visitors declined by 7.1% and 10.7%, respectively. A similar pattern was observed in Grand Bahama, where traffic was reduced by 24.5%, based on downturns in both air and sea arrivals, of 9.5% and 30.5%, respectively. Benefiting from an upswing in sea traffic, visitors to the Family Islands rebounded by 2.9% from last year's 0.5% downturn.

In the construction sector, output continued to benefit from elevated residential mortgage lending activity. Data collected from banks, insurance companies and The Bahamas Mortgage Corporation revealed that the value of total mortgage disbursements for the third quarter increased by 11.3% to $179.5 million. The bulk was earmarked for residential projects, which experienced an increase of 15.4% to $165.6 million, while commercial activities fell by 21.9% to $13.9 million. The number of mortgage commitments for new construction and repairs, a forward looking indicator, contracted by 36.9% to 335, with a corresponding 35.3% decrease in value to $39.4 million. Residential loan approvals declined in number by 36.5% to 323, with a similar abatement in value to $35.9 million, while commercial loan commitments fell in number by 45.5% to 12 and in value by 23.4% to $3.4 million. Meanwhile, total outstanding mortgages advanced by 18.3% to $2,432.8 million, with comparable percentage expansions in both the residential and commercial components. In terms of interest rates, average residential and commercial rates declined by 1 and 2 basis points, to 8.1% and 8.8%, respectively.

Fisheries data for the third quarter of the year featured a decline in export volumes of 35.0% to 1.0 million pounds, with a corresponding fall-off in earnings of 41.1% to $16.8 million, when compared with the same period last year. Crawfish export receipts, which accounted for 97.0% of total sales, slackened by 40.9% to $16.3 million, with a 33.9% drop in volume. A similar pattern was observed for the first nine months of 2006, as fisheries export volumes decreased by 28.3% to 2.8 million pounds, while receipts were reduced by 31.7% to $41.5 million.

During the review quarter, consumer price inflation, measured by changes in the average Retail Price Index, moderated to 2.11% from 2.29% in the comparable 2005 period, primarily influenced by decelerations in average costs of transport & communication and education services. For the twelve-months through September, inflation also narrowed to 1.59% from 2.05%, attributed to declines in average prices for transport & communication and recreation & entertainment services.

In the external sector, the current account deficit widened by $160.8 million to $425.2 million in the third quarter of 2006. Weakness in tourism receipts, combined with increased outflows for other services, construction, insurance and government services, led to a contraction in the services account surplus by 59.0% to $89.7 million. Also, the merchandise trade deficit deteriorated by 8.5% to $486.6 million alongside the 30.4% decline in inflows from net current transfers to $6.3 million, which offset the 20.7% reduction in net foreign income remittances to $34.6 million.

The capital and financial account's estimated surplus expanded to $244.0 million from $147.6 million in 2005, mainly reflecting domestic banks' funding of tourism related projects and other net foreign investment inflows. However, net direct investment inflows (net equity and net real estate inflows) were reduced by $51.7 million to $139.8 million. Portfolio investment net outflows amounted to $6.3 million, compared to a negligible balance a year ago.