Release Date: 15 June 2005

QUARTERLY OVERVIEW OF DOMESTIC ECONOMIC DEVELOPMENTS

MARCH 2005

This summary is an early release, excerpted from the upcoming issue of the Central Bank's Quarterly Economic Review for the Quarter ended March 2005. The full text of the Economic Review will be released on 21 June 2005.

The Bahamas
Review of Domestic Economic Developments for First Quarter 2005

Indications are that the Bahamian economy continued to strengthen during the first quarter of 2005, in a climate of subdued inflation. Increased construction stimulus, from intensifying foreign investment inflows, residential investments and hurricane repairs, outweighed the comparative decrease in tourism output, which remained constrained mainly by the reduced capacity in Grand Bahama. While the fiscal outlook was improved, expenditure growth outpaced the rise in revenue, resulting in a widening in the budget deficit for the third quarter of FY2004/05. Financial sector trends featured accelerated expansion in domestic credit, which trailed growth in the monetary aggregates, for further improvement in bank liquidity. In the context of the Central Bank's more accommodative policy stance, interest softened broadly, albeit with some widening in the average loan-to-deposit rate spread. On the external side, the estimated current account deficit widened, partly on account of an increase in the oil import bill. Meanwhile, a more than two-fold hike in net private foreign investments underpinned a significant boost in the surplus on the capital and financial account.

Following a shift of surplus resources into Treasury bills, net free cash balances of banks decreased by 14.8% to $231.5 million at end-March 2005; however, with liquidity constituting a larger 5.5% of Bahamian dollar deposit liabilities, compared to 4.8% last year. Broader surplus liquid assets, which reflected support from foreign currency inflows, increased by 13.3% to $263.4 million, exceeding the statutory minimum by 38.1%, relative to the year-earlier ratio of 37.3%. The stable outlook for external reserves growth and continued buoyancy in liquidity, led to the Central Bank's decision in February to reduce the Discount Rate, by 50 basis points to 5.25%. This was followed by an equivalent reduction in Prime by commercial banks to 5.50%. Reflecting these trends, the weighted average interest rate on loans and deposits softened by 20 and 31 basis points, to 10.64% and 3.44%, respectively, with the corresponding average spread widened by 11 basis points to 7.20%. Meanwhile, the average 90-day Treasury bill rate decreased by 7 basis points to 0.18%.

Healthy growth in private sector deposits supported an almost stable rate of monetary expansion (M3) of 4.4%, compared to 4.6% in 2004, and placed the overall stock at $4.62 billion vis-à-vis $4.19 billion in 2004. Accretions to demand deposits firmed to 11.6% from 14.1%, nearly offsetting moderated savings and fixed deposit gains of 4.4% and 0.7%, relative to 4.7% and 2.2% respectively, in 2004. Although currency in active circulation decreased by 0.6%, resident foreign currency balances recovered by a third.

While trailing money growth, domestic credit expansion accelerated to $132.6 million (2.5%) from $70.8 million (1.4%) the previous year, resulting in outstanding claims of $5.36 billion. Firmer growth in net claims on the public sector (10.5%) was led by a more than doubled increase in net credit to Government of 16.8% ($92.0 million), with marginally rebounded credit to the public corporations of 0.4%. The pace of private sector credit expansion was steadied at 0.9%, with moderate firming in Bahamian dollar claims (1.2%) outpacing a downturn in foreign currency credit (2.4%). Personal loans, the largest share of private claims (71.2%), grew at a more tempered pace (0.4%), encompassing softening in residential mortgages growth (3.0%) and an unchanged level of consumer loans. However, net lending was resumed for claims against most business and other private sector activities.

On the fiscal front, the estimated deficit for the March quarter of FY2004/05 widened to $33.2 million from $24.2 million in the year-earlier period. Total revenue rose by 0.4% to $254.3 million, trailing the 3.6% expansion in expenditure to $287.5 million. On the revenue side, the 19.1% strengthening in tax receipts, was nearly offset by the significant shift in the timing of flows, which reduced non-tax revenue by more than half, and the absence of capital revenue, as compared to a significant inflow in 2004. Expenditure trends included increases in both current outlays (4.5%) and net lending to the public corporations (28.1%), which masked a reduction in capital outlays (20.0%). Budgetary financing during the quarter was sourced from an increase in outstanding Treasury bills of $13.1 million, and in advances from the Central Bank of $5.7 million. After principal repayment of $20.4 million, mainly on domestic debt, the Direct Charge on Government declined by 0.1% to $2,099.6 million. Nevertheless, a 0.7% increase in the guaranteed liabilities of the public corporations to $435.2 million, caused the National Debt to rise by 0.1 % to $2,534.9 million.

Capacity constraints, which remained concentrated in Grand Bahama following the September 2004 hurricanes, contributed to a decline in tourism earnings during the first quarter of 2005. First quarter visitor arrivals fell by 3.0% to 1.35 million, following robust growth of 13.3% in 2004. Both air and sea arrivals contracted, by 4.2% and 2.5%, from the year-earlier advances of 7.9% and 15.7%, respectively. In addition to some falloff in cruise earnings, indications are that stopover spending also declined. The Ministry of Tourism's survey indicate that the average nightly room rate gains among large hotel properties, of 9.4% to $177.88, was partly offset by a 6.1% decrease in nightly room sales, consequently constraining estimated room revenue growth at 2.8% from 10.9% in the first quarter of 2004. While both New Providence and the Family Islands operated with less rooms and the Family Islands experience reduced room sales, the capacity constraint was most marked by the one third fewer rooms in Grand Bahama, as a major hotel remained closed since September 2004.

Construction sector activity was significantly strengthened during the first quarter, as stimulus from foreign investments intensified, and local building expenditures remained firmly supported by re-insurance claim inflows and mortgage lending for both residential and commercial developments. Data collected from banks, insurance companies and the Bahamas Mortgage Corporation revealed that the value of quarterly mortgage disbursements, mainly against residential developments, increased by 14.5% to $86.0 million. More forward looking, the value of local commitments for new construction and repairs more than doubled to $47.1 million, with residential loan approvals accounting for 96.8% of the total. In line with these trends, outstanding mortgages at quarter's end were 11.5% higher than the previous year, with residential claims elevated by 12.2% to $1,747.0 million and commercial claims, by 3.9% to $164.0 million.

When compared to the same period in 2004, consumer price inflation, measured by changes in the average Retail Price Index, stabilized at 0.1 % during the first quarter. Declines in average costs on clothing & footwear and housing, and subdued increases in average costs on food & beverages, medical care & health and education were counter-balanced by a comparatively firmer uptrend in the other components in the Index. During the 12 months through March 2005, average inflation eased to 0.9% from 2.5% in 2004, paced by reduced average costs on housing, clothing & footwear and recreation & entertainment services. The annual cost increase softened for most other items in the Index.

In the external sector, the estimated current account deficit widened to $76.2 million from $12.9 million in the first quarter of 2004. An elevated oil bill extended the trade deficit by 3.3% to $363.7 million, while a decrease in net tourism receipts led the contraction in the services account surplus by 18.2% to $290.0 million. The income account recorded an approximate doubling in the net outflow to $50.9 million, owing to increased net repatriation of private sector earnings, concentrated in the banking sector. Meanwhile, continued insurance settlements related to the September 2004 hurricanes boosted net current transfer receipts to $48.4 million from $9.0 million in 2004.

The estimated surplus on the capital and financial account widened to $128.5 million from $49.0 million in 2004. Within this, estimated net private investment inflows were boosted to $167.8 million from $66.4 million, with net direct equity inflows elevated to $71.9 million from $18.9 million; net real estate sales, to $24.3 million from $19.9 million and net loan financing, to $71.6 million from $27.6 million. Meanwhile, the public sector's net external debt repayment narrowed to $2.6 million from $7.8 million, and the banking system recorded a net short-term outflow of $25.3 million, in contrast to an approximately balanced outcome in 2004.