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QUARTERLY OVERVIEW OF DOMESTIC ECONOMIC DEVELOPMENTS

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This summary is an early release, excerpted from the upcoming issue of the Central Bank's Quarterly Economic Review for the Quarter ended September 2003. The full text of the Economic Review will be released on December 16 2003.

The Bahamas
Review of Domestic Economic Developments for 3rd Quarter, 2003

Preliminary indicators suggest that the Bahamian economy weakened during the third quarter, both in comparison to the same period last year and the output strengthening noted during the first half of 2003. This outturn was primarily due, in combination, to a decrease in tourism expenditures, owing to the delayed recovery in leisure spending among households in the United States, the primary market, and softness in the construction sector, where financing for domestic projects slackened. The outlook for both sectors, however, has significantly improved since the end of the third quarter, as firming employment trends in the continued sectoral broadening of the economic expansion in the United States were expected to stimulate increased growth in The Bahamas' tourist sector by the onset of the 2004 winter season. Meanwhile, the anticipated start of significant foreign investment projects in the hotel sector should boost construction output in 2004.

As regard other developments, although mild firming continued to be noted in the annual inflation rate, the quarterly comparisons indicated more recent softening. The fiscal situation reflected the cumulative improvement in the economy since 2002, with strengthened tax collections partly contributing to a reduction in the overall budget deficit for the first quarter of FY2003/04. In the financial sector, quarterly developments were dominated by the $200 million external bond issue, which financed a reduction in the banking system's net claims on Government, a decrease in the system's net foreign liabilities. The added buoyancy in liquidity conditions underpinned further softening in average interest rates. On the external side, the estimated current account deficit widened moderately, underscored by decreased net services receipts; albeit, capital and financial inflows were boosted by the net Government's external borrowing.

For the September quarter, net free cash balances of the banking system rose by 9.3% to $138.9 million, though corresponding to a slightly reduced 3.7% of Bahamian dollar deposits. Broader surplus liquid assets increased more vigorously, by 19.6% to $177.3 million, exceeding the statutory minimum by a wider 29.6% margin, as compared to 21.7% in 2002. Although weighted average interest rates softened as a consequence, the 5 basis points drop in the deposit rate to 3.81% as opposed to a 2 basis points easing on the lending side to 12.15%, caused the average spread to widen by 3 basis points to 8.34%. The average 90-day Treasury bill rate also decreased by 28 basis points to 1.74%, while benchmark rates—the Central Bank's Discount Rate and commercial banks' Prime—were maintained at 5.75% and 6.00%, respectively.

Given a stronger buildup in private sector balances, relative to a net shift of public corporation's funds from fixed to demand balances, the money supply (M3) recovered marginally during the review period, by 0.4% to $4.0 billion, in contrast to the previous year's contraction of 0.6% to $3.9 billion. Demand balances growth accelerated to 3.0% from 0.5%, while savings, mainly in the hands of private individuals, rebounded by 0.5%. With strengthened expansion in business balances, the reduction in fixed deposits was steadied at 0.1%, while the contraction in the currency component was slightly abated to 3.1%.

Led by the Government's repayment of the $125.0 million foreign currency loan obtained from local banks in June and July 2002, domestic credit contracted by $124.9 million (2.6%), to an-end quarter stock of $4.8 billion, opposing growth of 1.7% in 2002. In particular, after advancing by 3.3% in 2002, net claims on Government decreased by $18.4 million (27.5%), inclusive of net Bahamian dollar repayments of $56.9 million (10.5%), primarily met through the balance of proceeds from the bond issue. Meanwhile, growth in the banking sector's claims on the rest of the public sector slowed to 1.5% from 6.5% last year. Private sector credit expansion at $56.2 million, 1.4% vis-à-vis 1.2% in 2002, was due solely to resumed expansion in foreign currency claims (4.7%), as the Bahamian dollar uptrend slackened to $38.3 million (1.1%). The latter was largely explained by lessened gains in residential mortgages (1.6%), which overshadowed faster growth in consumer credit (1.0%). Total claims relative to most other private sector activities increased moderately.

In the fiscal sector, the estimated deficit for the first quarter of FY2003/04 narrowed to $23.1 million from $28.1 million in the year-earlier period. Revenue collection increased by 4.1% to $213.7 million, supported by the 3.8% gain in tax collections and higher non-tax yields (8.2%) which were linked to fee increases approved in the Budget. Meanwhile, reduced expenditure growth at 1.4% to $236.8 million, resulted from scaled back capital investments (55.0%) and decreased net lending to public corporations (23.7%), which offset an accelerated current spending increase of 7.4%. Budgetary financing for the quarter included the $200.0 million external bond, a $75.0 million domestic bonds issue and $2.8 million from other external sources. Debt amortization of $203.3 million was paced by the $125.0 million foreign currency loan repayment to local banks. Consequently, the Direct Charge on Government rose by 4.0% to $1,929.0 million. After a 4.2% reduction in contingent liabilities to $16.5 million, the National Debt grew by 2.6% to $2,301.7 million (7.2%), which was approximately $153.9 million (7.2%) above the September 2002 level.

In the tourism sector, output growth weakened during the third quarter, compared to the same period last year, with moderated cruise visitor gains occurring alongside a reduction in stopovers. Following the 11.5% rebound in 2001, visitor gains slowed to 1.5% as sea arrivals, which mirror cruise trends, rose by a lesser 2.3% to 0.72 million, as compared to the 18.2% boost last year. Air visitors, at 0.34 million, were approximately unchanged vis-à-vis 2002's decline of 0.3%. As regard the main destinations, rebounds in both air and sea arrivals underpinned an upturn in traffic to New Providence (1.8%), while the Family Islands capitalized on 2002's gains, particularly in the cruise sector, with arrivals further increased by 8.0%. Grand Bahama, however, recorded a 9.5% downturn in arrivals, on account of both air and sea visitors. The comparative decline in industry earnings during the quarter was led by a 4.4% reduction in estimated hotel room revenues, vis-à-vis weak onshore activities, particularly in New Providence. Although hotel average room rates firmed by 1.8% to $146.64 per night, occupied room nights decreased by 6.0%, as the average room occupancy rate softened to 57.5% from 63.7% last year.

While forward looking indicators foreshadow significantly elevated construction output for 2004 from new foreign investment projects, reduced mortgage lending contributed to decreased outlays on locally initiated projects during the third quarter. Growth in total mortgages outstanding among banks, insurance companies and the Bahamas Mortgage Corporation slackened to $18.2 million (1.1%) from $68.8 million (4.7%) in 2002. This was largely due to reduced lending for new construction and repairs of residential dwellings. In particular, total mortgage commitments, mainly for residential construction, decreased in numbers to 185 from 220 in 2002, and in value by 44.8% to $20.6 million.

Consumer price inflation, measured by changes in the average Retail Price Index, softened during the third quarter, to 0.3% from 0.8% in the comparable 2002 period. This was largely due to average cost decreases on recreation & entertainment services and "other" goods & services. However, the annual inflation rate for the 12 months through September firmed to 2.9% from 2.3% in 2002, paced by accelerated average cost increases for recreation & entertainment services, "other" goods & services, medical care & health, furniture & household operations, transport & communication and housing.

In the external sector, preliminary estimates suggested a widening in the current account deficit to $111.6 million from $68.7 million last year. Increased net import demand extended the trade deficit to $228.2 million from $211.2 million, while net invisible inflows decreased by 20.1% to $154.1 million, due to reduced net travel receipts (11.4%) and decreased local expenditures by offshore companies, following elevated restructuring activities in 2002. Some offset to these was provided by the narrowing in net income outflows, by 26.1% to $44.8 million, reflecting decreased remittances by banks and private companies. However, net current transfer receipts narrowed to $7.4 million from $10.3 million, owing to a reduction in net government inflows.

The estimated surplus on the capital and financial account widened to $114.4 million from $99.0 million in 2002, mainly on account of the $198.4 million net external borrowing by the Government, relative to a net repayment of $3.5 million last year. The $125.0 million domestic foreign currency loan repayment connected with this, caused a shift in the banking system's position to a net short-term outflow of $99.9 million from a net inflow of $58.6 million in 2002. Net private foreign investment inflows decreased to $30.4 million from $55.5 million, despite a $5.1 million increase in net equity inflows to $22.9 million, as net foreign real estate sales tapered to $1.5 million from $13.6 million and net loan proceeds, to $6.8 million from $25.1 million. The rest of the public sector recorded a further net external debt repayment of $5.8 million.