The Central Bank of The Bahamas

Quarterly Economic Review

March, 2000

Vol. 9, No.1

The Quarterly Economic Review is a publication of The Central Bank of The Bahamas, prepared by The Research Department for issue in March, June, September and December. It replaces the former Quarterly Review which was last published for March 1992. All correspondence pertaining to the Economic Review should be addressed to:

The Manager
Research Department
The Central Bank of The Bahamas
P. O. Box N-4868
Nassau, Bahamas

QUARTERLY ECONOMIC REVIEW

Volume 9, No. 1
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CONTENTS

REVIEW OF ECONOMIC AND FINANCIAL DEVELOPMENTS

DOMESTIC ECONOMIC DEVELOPMENTS

Preliminary indicators for the first quarter of 2000 suggest continued expansion in the Bahamian economy. Tourism and foreign investment related inflows supported further growth in bank liquidity and a reduction in the financial system's net foreign liabilities, amid sustainable domestic credit expansion. Fiscal sector developments were highlighted by a robust revenue performance, which outpaced expenditure gains to secure an improvement in the overall deficit. Price trends remained favourable, despite the quarterly firming in average consumer prices which was partly associated with the recent hike in oil prices. In the external sector, the moderately widened current account deficit, linked mainly to increased domestic demand, continued to be financed by the capital and financial account which remained in substantial surplus.

In the financial sector, excess reserves of the banking system rose by 19.3% to $96.6 million. However, firmer private credit expansion was a key factor behind the 12.2% decline in the surplus on liquid assets to $130.5 million, which exceeded the statutory minimum by 24.9% as against a higher 30.8% in 1999. Within this context, the average spread between lending and deposit rates softened; the weighted average deposit rate was down by 16 basis points to 3.92%, while the weighted average lending rate fell by 45 basis points to 11.36%, primarily due to lower rates on residential mortgages and consumer loans. As regard other key interest rates, the 90-day Treasury bill rate was virtually unchanged at 0.96%, while the Central Bank's Discount Rate and commercial banks' Prime remained at 5.75% and 6.00%, respectively.

Broadbased growth in deposits supported a 3.2% expansion in the money supply (M3) to $3,352.9 million, which was incrementally below the year-earlier advance of 3.3% but surpassed the slowed growth in domestic credit of 1.9%. Credit developments were largely reflective of a 3.8% net repayment on the public sector's domestic liabilities to the banking system as the Central Bank sold its Treasury bill holdings to the National Insurance Board. This turnaround significantly countered accelerated private sector credit growth of 3.2% vis-à-vis 2.2% a year ago, and was related to increased lending for housing and consumer durables and recourse to overdraft facilities.

Tourism performance, although restrained by a decline in air arrivals, benefited from steadily increasing average room rates, resulting in a 19.8% boost in hotel room revenues. Total arrivals rose by 8.7% to 1.1 million visitors, as an appreciable 16.1% hike in sea arrivals (65% of total arrivals) offset the 2.7% falloff in air traffic. Analyzed by domestic destinations, New Providence and the Family Islands recorded respective declines in air arrivals of 3.5% and 13.2%, in contrast to strengthening positions achieved in 1999. Conversely, growth in air traffic to Grand Bahama firmed to 8.1% from 3.5% last year. The favourable performance of sea arrivals comprised an improvement of 26.1% for New Providence and 10.8% for the Family Islands, but a 5.1% drop for Grand Bahama. As regards other key tourism measures, weakness in air arrivals was compensated by significant estimated gains in stopover expenditures, as evidenced by the 15.0% hike in the average hotel room rate to $169.69 per night and the 4.2% growth in the number of room nights sold. The average hotel occupancy rate, however, declined to 71.0% from 72.3%, mainly due to a further 6.0% increase in room inventory, which paced slightly ahead of growth in rooms sold.

Steady investments in both housing and commercial projects during fourth quarter 1999—the most recent period for which data are available—confirmed the continuing positive contribution of construction activity to economic output. In particular, the value of construction permits—a reliable indicator of future activity—more than doubled to $177.4 million, corresponding to higher planned housing and commercial investments. Valuations on building starts also strengthened by 8.9% to $39.5 million. In this regard, approximately 81.7% of the total represented housing units, which appreciated by 12.2% to $32.2 million. Completion estimates, heavily weighted by commercial activity, fell to $78.3 million from

$364.4 million in 1998, when Sun International's project on Paradise Island was a significant positive factor.

On the inflation front, the average Retail Price Index firmed by 0.3% during the first quarter, in contrast to a 0.1% contraction a year ago. This was led by a significant oil price propelled upturn in transportation and communication costs (0.5% from a 2.3% contraction last year) and broadbased firming in average price advances for food & beverages and medical care & health. Consumer price inflation, annualized for the 12 months through March, stabilized at 1.4%, with ongoing tuition hikes influencing another sizeable but smaller advance in education costs of 11.9% as compared to 14.5% a year earlier. Both this and the accelerated housing cost increase (0.7%) were counterbalanced by less intense firming in average prices for food & beverages and most other items in the Index.

The fiscal outturn for third quarter FY1999/00 benefited from robust growth in revenue receipts, which underpinned a significant narrowing in the overall deficit to $15.0 million from $24.1 million in the third quarter of FY1998/99. Reflecting accelerated domestic import demand, revenue collections increased by 14.2% to $230.1 million, with the 16.7% gain in tax income largely concentrated in import duties. On the expenditure side, the 8.6% advance to $245.1 million included respective hikes in both recurrent (8.9%) and capital (15.0%) spending. Outlays for tourism services and social benefits registered the strongest gains on the recurrent side, while the increase in capital spending was largely explained by capital transfers to public corporations and infrastructural investments. Conversely, budgetary support of public corporations in the form of loans (net) declined by 7.8%. Alongside short-term advances from the banking system, fiscal operations were financed by net foreign currency borrowings of $1.5 million, which placed the Government's Direct Charge higher by an equivalent amount at $1,513.8 million. Taking into account a marginal decrease in Government Guaranteed Debt, the National Debt rose by $1.3 million to $1,867.9 million for the quarter and was some 4.1% above the year-earlier level.

External sector developments featured a 13.8% estimated widening of the current account deficit to $131.7 million. In particular, a 6.8% hike in imports pushed the visible trade deficit 6.5% higher to $333.3 million, while the surplus on the services account was 1.1% lower at $229.4 million. Apart from a general increase in import demand, the trade deficit was also inflated by the sharp rise in average fuel prices, while the surplus on net invisible flows was slightly reduced, as a net increase in non-tourist related outflows countered the net improved surplus on the travel account. The current account balance also benefited from lower net income outflows (10.6%) and a boost in current net transfer receipts (28.0%).

As regards the capital account, the threefold increase in net direct foreign investments to $40.0 million was offset by a near halving of other net investment inflows to $43.6 million, largely explained by continuing but smaller scale tourist-related developments. In addition, public sector loan receipts were $6.1 million lower at $3.2 million, given reduced central government borrowing activities. Consequent on these transactions and a more modest decline in bank's short-term net foreign currency exposure, the overall capital and financial account posted a reduced surplus of $80.9 million vis-à-vis $99.3 million last year. The overall balance of payments surplus, measured by changes in external reserves, stood at $46.3 million which was some 36.3% below the year-earlier outturn.

FISCAL OPERATIONS

According to provisional estimates, fiscal operations for the third quarter of FY1999/00 registered a marked decline in the overall deficit, to $15.0 million from $24.1 million in the comparable FY1998/99 period. Supported by continued buoyancy in economic activity, revenue collections strengthened by 14.2% to $230.1 million, to outpace the 8.6% increase in total outlays to $245.1 million.

REVENUE

Revenue growth was largely derived from broad-based gains in tax collections of $30.5 million (16.7%) to $213.9 million, representing 92.9% of total inflows. Non-tax receipts, at 7.1% of the total, declined by $1.9 million (10.5%) to $16.2 million.

In the context of favourable economic conditions, tax revenue featured strong growth in levies on international trade and transactions of $132.8 million (19.2%), with import duties improving by 23.8% to $106.2 million and stamp tax from imports, by 7.9% to $25.0 million. Selective taxes on services—comprising gaming and hotel occupancy taxes—strengthened by almost a third to $14.9 million, and departure taxes by 22.0% to $15.4 million. In addition, property taxes rose by 9.1% to $8.3 million, while stamp taxes on financial and other transactions firmed incrementally to $19.0 million.

Government Revenue By Source
(January - March)

	FY98/99p		FY99/00p	
	B$M	%	B$M	%
Property tax	7.6	3.8	8.3	3.6
Selective Services tax	11.3	5.6	14.9	6.5
Bus. & Prof. Lic. fees	17.1	8.5	15.8	6.9
Motor Vehicle tax	2.4	1.2	7.3	3.2
Departure tax	12.7	6.3	15.4	6.7
Import duties	85.8	42.5	106.3	46.2
Stamp tax from imports	23.1	11.5	25.0	10.9
Export tax	2.4	1.2	1.4	0.6
Stamp tax from exports	-	-	0.1	-
Other stamp duty	18.9	9.4	19.0	8.3
Other Tax revenue	2.2	1.1	1.3	0.5
Fines, forfeits. etc.	12.2	6.0	13.4	5.8
Income	5.8	2.9	2.7	1.2
Other non-tax rev.	0.2	0.1	0.1	-
Capital Revenue	-	-	-	-
Grants	-	-	-	-
Less: Refunds	0.2	0.1	0.9	0.4
Total	201.5	100.0	230.1	100.0

The fall-off in non-tax collections was principally explained by a near halving in income from public enterprises and other sources to $2.7 million. Conversely, proceeds from fines, forfeitures & administrative fees were higher by $1.2 million (10.1%) at $13.4 million.

Expenditure

The $19.4 million (8.6%) increase in total expenditure comprised growth in recurrent spending of 8.9% to $205.8 million and in capital outlays of 15.0% to $27.8 million. Net lending to the public corporations, however, fell by 7.8% to $11.5 million. On a proportional basis, recurrent spending constituted 84.0% of total expenditure; capital outlays, 11.3% and net lending to the public corporations, 4.7%.

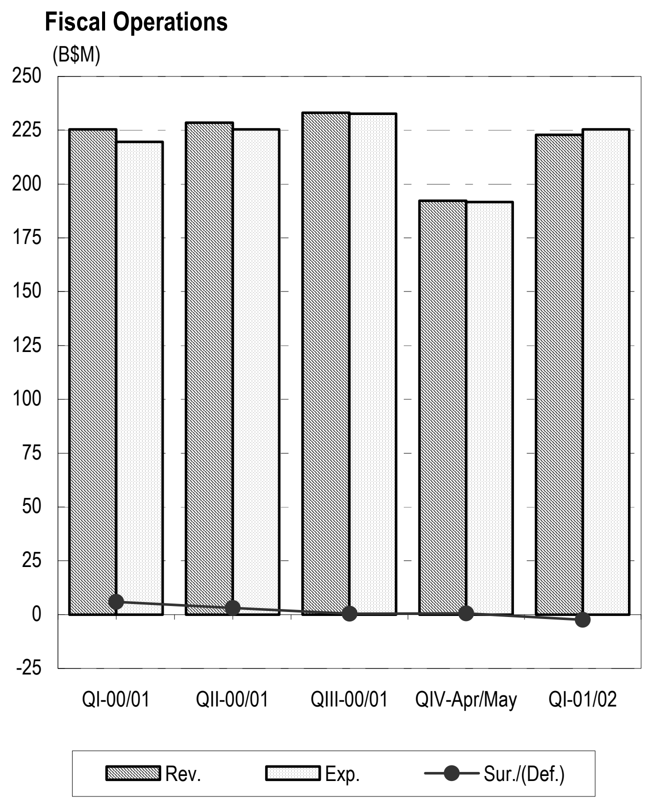
The economic classification of recurrent outlays continued to reflect notable shifts in the various categories associated with the transfer of several health departments to the newly constituted Public Hospitals Authority. In particular, estimated government consumption declined by 8.5% to $126.9 million, but was more than offset by the 56.9% ($28.6 million) hike in transfer payments to $78.8 million. The latter included relatively stable interest payments of $25.9 million and a hike in subsidies—including payments to the Authority—to $23.4 million from $3.7 million last year. Transfers to households—mainly public pensions and gratuities—rose by 57.5% to $16.0 million, while transfers to non-profit institutions were lower by 85.2% at $9.7 million.

On a functional basis, the strongest gains in recurrent expenditures were recorded in economic services of $6.1 million (24.4%) and in social benefits & services of $4.2 million (34.2%). Disbursements for education were also up by 6.6%; for health, by 6.5% and for public order and safety, by 4.8%. On a proportional basis, general public services absorbed 23.8% of recurrent outlays, followed by education (20.1%), health (16.1%), economic services (15.2%) and interest on government debt (12.6%).

The $3.6 million hike in total capital outlays was explained mainly by increased capital transfers to public corporations of $2.8 million to $3.3 million and higher spending on infrastructure works of $1.8 million to $10.0 million. Education related investments were also raised by $1.1 million to $4.3 million, contrasting with fairly stable expenditures for health ($2.5 million) and general public services ($4.1 million).

Financing and National Debt

Budgetary financing during the review quarter was accommodated through recourse to short-term advances from the banking system alongside external borrowings of $6.5 million. Debt repayment amounted to $5.1 million, with 64.5% applied to internal foreign currency liabilities and 30.9% to external obligations. Consequently, the Direct Charge on Government rose by $1.4 million to $1,513.8 million.



Bahamian dollar debt represented 91.0% of the total Direct Charge, with public corporations holding the largest share (46.2%), followed by banks (28.8%), private and institutional investors (20.7%) and the Central Bank (4.3%). By maturity profile, approximately 83% of the Direct Charge represented long-term indebtedness, of which 24.8% is to be retired within the next five years; 26.8% within 5-10 years; 26.2% within 10-15 years and 22.2% within 15-20 years.

Based on a $0.1 million net repayment on the public corporations' guaranteed debt to $354.1 million, the quarterly increase in the National Debt was placed at 0.1%, for an outstanding stock of $1,867.9 million vis-à-vis $1,794.4 million at end-March 1999.

PUBLIC SECTOR FOREIGN CURRENCY DEBT

During the first quarter of 2000, public sector foreign currency debt rose by $2.2 million (0.6%) to an estimated $377.2 million. Borrowings of $12.3 million comprised disbursements from existing loan facilities for various capital development projects. Foreign currency debt service, which decreased further to $15.9 million from $16.4 million in 1999, included $10.0 million in principal repayments and $5.9 million in interest charges. Debt service as a proportion of exports of goods and non-factor services declined to 2.8% from 3.0% in the corresponding 1999 period. Meanwhile, the Government's debt service represented a reduced 2.3% of total revenue relative to 3.2% last year, signaling stronger collections vis-à-vis declining debt service outlays.

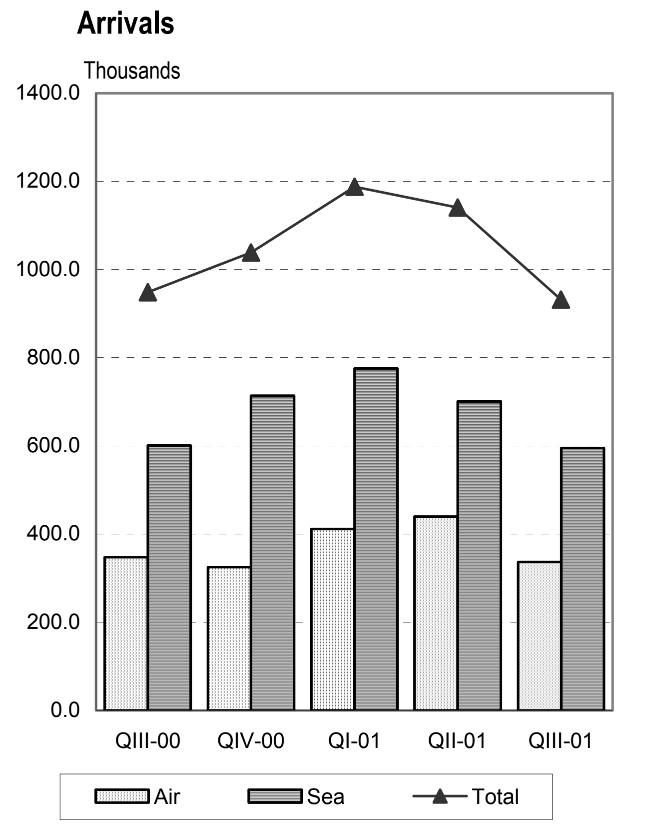
Foreign currency debt was denominated primarily in US dollars and featured an estimated weighted average age span of 10 years. By debtor profile, the largest share of outstanding liabilities was owed to multilateral institutions (56.4%), followed by commercial banks (23.6%), private capital markets (13.2%) and bilateral and offshore financial institutions (6.8%).

REAL SECTOR

TOURISM

First quarter estimates of tourism activity suggest continued growth in output, linked principally to competitive pricing of facilities alongside healthy increases in cruise visitors, as the weakness in air arrivals was partly linked to Y2K related travel concerns.

After a robust 13.1% recovery in 1999, total visitor arrivals strengthened further by 8.4% to 1.1 million, reinforced primarily by a 15.5% hike in sea arrivals to 714,950. Air arrivals contracted by 2.7% to 384,999. An analysis of activity by ports of entry shows increased cruise ship calls to New Providence and the Family Islands supporting healthy gains of 26.1% and 10.8% in sea visitor arrivals, respectively. However, air traffic to these destinations fell by 3.5% and 13.2%, respectively. Although Grand Bahama experienced persistent weakness in sea arrivals of 5.1%, air arrivals recorded an encouraging hike in growth to 8.1% from 3.5% last year.



Partial indicators of visitor spending highlight the industry's enhanced competitiveness from gains in the pricing of hotel room facilities. Moreover, growth in occupied room nights suggests that some of the weakness in air traffic was offset by longer vacation stays, as both available hotel room nights and occupied nights increased by 6.0% and 4.2%, respectively. As a result, average hotel occupancy was only marginally lower at 71.0%. Meanwhile, average room rates were boosted by 15.0% to $169.69 per night, with room revenues up 19.8%. New Providence led with double digit gains in both room revenues (19.2%) and average room rates (18.9%); Grand Bahama registered an 11.5% hike in average room rates and Family Island properties, a 7.9% gain.

Construction

Recently released estimates of construction activity for the fourth quarter of 1999 confirmed earlier indications of the significant contribution of housing investments to construction output during 1999, and of the positive outlook for activity during 2000. Boosted values for permits granted reflect rebuilding efforts following the destruction caused by Hurricane Floyd, along with another round—although of a reduced scale—of tourist-related developments, which continue to sustain a high level of employment in the sector.

Construction Activity
(October - December)

	1998	1999	% Δ
Building Permits			
Number	598	694	16.1
Value (B$M)	88.3	177.4	100.9
Building Starts			
Number	263	248	-5.7
Value (B$M)	36.3	39.5	8.8
of which: Residential	28.8	32.3	12.2
Commercial	7.5	7.2	-4.0
Public	--	--	--
Building Completions			
Number	416	364	-12.5
Value (B$M)	364.4	78.3	-78.5

Compared to the final quarter of 1998, the value of construction starts advanced by 8.9% to $39.5 million, despite a 5.7% reduction in the number of units to 248. The key factor was the 12.2% hike in residential valuations to $32.2 million, as commercial starts contracted in value by 3.8% to $7.2 million, despite an incremental increase in the number of projects.

The number of building completions fell by 52 (12.5%) to 364 units, with the estimated value sharply lower at $78.3 million from $364.4 million in 1998, which reflected the extraordinary boost in value associated with the completion of Phase II of the Atlantis Resort project on Paradise Island. Correspondingly, although the number of commercial completions increased by 1 to 45, the respective value contracted sharply to $46.1 million from $319.4 million in 1998. Housing completions also fell by 14.3% to 318 units and the assessed value by almost a third to $31.2 million.

Data on building permits issued signaled healthy future growth in both residential and commercial investments, with aggregate value more than doubled to $177.4 million and corresponding to a 16.1% gain in number to 694 units. In particular, valuations on residential approvals strengthened by 70.4% to $97.5 million and the associated number of units by 16.3% to 584. Equally significant, the estimated value of commercial permits more than doubled to $79.1 million, alongside a 17.6% advance in the number of units to 107. Although public sector permits were almost halved to 3, their estimated value firmed to $0.8 million.

PRICES

Consumer price inflation, measured by average variations in the Retail Price Index, firmed by 0.3% for the first quarter, and contrasted with a marginal easing of 0.1% in the same period last year. Most notable, the rate of increase in food & beverage costs accelerated to 1.4% from 0.2% and for medical care & health, to 1.3% from 0.7% in 1999. Under the impact of higher oil prices, the transport & communications index rebounded by 0.5% relative to a 2.3% contraction in 1999, with a similar up-trend in average prices for clothing & footwear by 0.2% following an equivalent decline a year ago. Partially off-setting declines were registered in average costs for recreation & entertainment services (1.2%) and other goods & services (1.8%), which represented substantial easings from the comparative year-earlier period.

On an annual basis through March, the rate of increase in average consumer prices was stable at 1.4%, amid offsetting trends in the various components. In particular, modest firming in price increases for housing and furniture & household operations at 0.7% and 1.4% respectively, contrasted with a significantly slowed advance in the food and beverage component at 0.1% from 1.9% in 1999. Also notable were more tempered increases for

Average Retail Price Index
(Annual % Changes)

		1999		2000	
Items	Weight	Index	%	Index	%
Food & Beverages	138.3	106.7	1.9	106.9	0.1
Clothing & Footwear	58.9	105.2	1.7	106.0	0.7
Housing	328.2	101.8	0.1	102.5	0.7
Furn. & Household	88.7	103.0	0.9	104.5	1.4
Med. Care & Health	44.1	105.1	2.5	107.1	1.9
Trans. & Comm.	148.4	100.9	-0.3	100.8	-0.1
Rec., Enter. & Ser.	48.7	106.6	3.4	109.7	2.9
Education	53.1	109.5	14.5	122.6	11.9
Other Goods & Ser.	91.6	101.0	0.1	102.5	1.5
ALL ITEMS	1000	103.4	1.4	104.8	1.4

recreation & entertainment costs (2.9%), clothing & footwear (0.7%) and medical & health care (1.9%). Meanwhile, ongoing hikes in tertiary level tuition occasioned another sizeable but reduced increase in average education costs of 11.9% as opposed to 14.5% last year, and the transportation & communications index fell further by 0.1% as compared to 0.3% in 1999.

MONEY, CREDIT AND INTEREST RATES

OVERVIEW

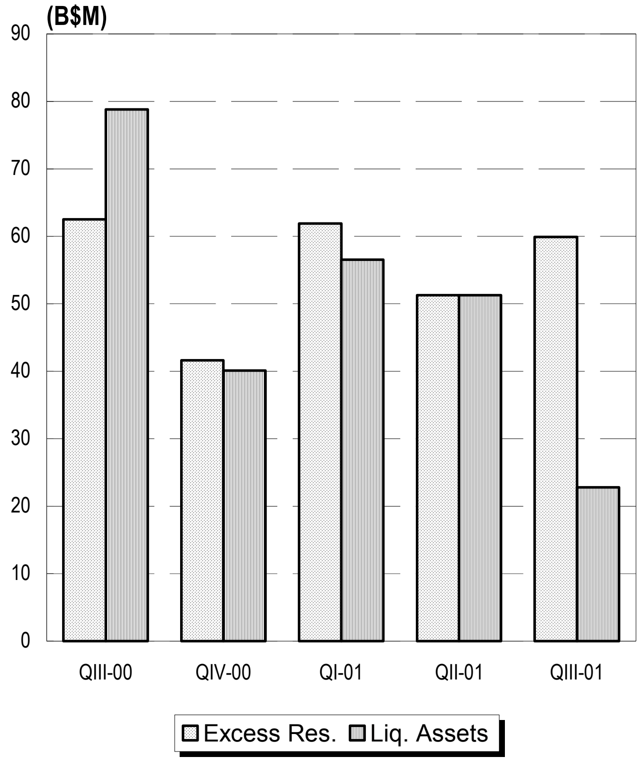
Growth in the money and credit aggregates moderated from the corresponding 1999 period, although the rate of increase in the money supply continued to pace ahead of domestic credit expansion. Conditions remained supportive of further improvements in the financial system's net foreign assets and liquidity levels, but quarterly gains were reduced, amid more accelerated growth in private sector credit and decreased net foreign currency inflows. The average interest rate spread between banks' loans and deposits narrowed during the quarter, due to some tightening of deposit rates and further softening in lending rates.

Banks' earnings indicators for the final quarter of 1999, the latest period for which data are available, show a decrease in profitability ratios. Effective interest spreads narrowed, whereas the operating cost ratio stabilized.

LIQUIDITY

During the review quarter, net free cash reserves of the banking system grew by $15.7 million (19.3%) to $96.6 million and represented 3.0% of Bahamian dollar

Liquidity



deposit liabilities compared with 1.9% in 1999 when excess reserves were only $54.6 million. In the context of increased deposit liabilities, the broader surplus liquid asset measure narrowed by $18.2 million (12.2%) to $130.5 million, exceeding the statutory minimum by a lesser 24.9% as against 30.8% in 1999.

Deposits and Money

The accumulation of deposit balances by private individuals underpinned most of the quarterly expansion in the monetary aggregates. In particular, growth in narrow money (M1) slackened to 2.3% from 4.7% a year ago, with gains in demand deposits lower at 4.4% from 7.4% and currency in circulation recording a stronger decline of 6.7% vis-à-vis 5.5% in 1999.

Broad money (M2) expansion also receded to 3.0% from 3.4% in 1999, as growth in savings balances eased to 4.3% from 5.2%. Conversely, fixed deposits posted a firmer advance of 2.8% as against 2.5% a year earlier. Residents' foreign currency deposits were higher by 20.0%, reversing the marginal 1.5% downturn posted in 1999. Consequently, overall money (M3) grew by $105.3 million (3.2%) to $3,352.9 million, not significantly changed from the year-earlier 3.3% advance.

Inclusive of balances held by Government, the Bahamian dollar deposit base stood at $3.2 billion at end-March 2000. The largest shares were held by private individuals (58.4%) and business firms (22.2%), followed by the combined balances of private financial institutions and other private depositors (10.4%) and the public sector (9.0%).

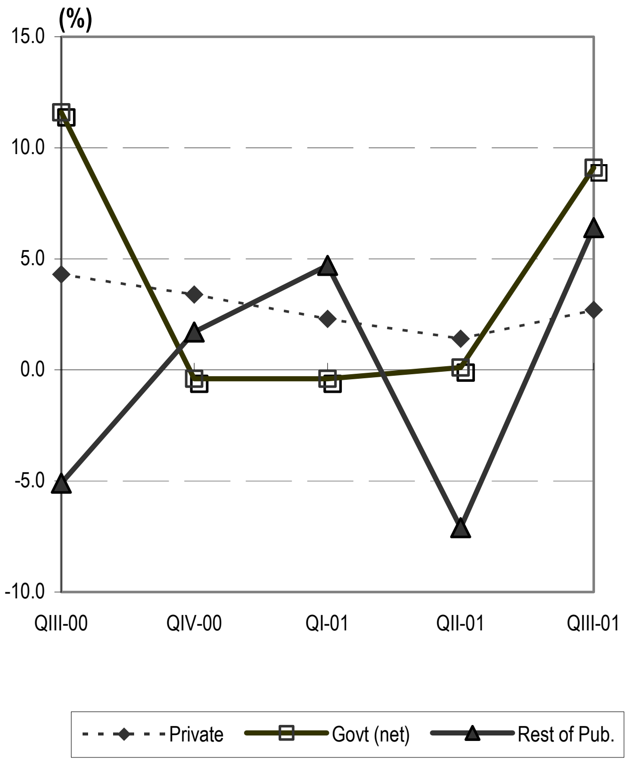
An analysis of deposits by range of values revealed that the largest concentration of depositors (91.1%) were those with average account balances of less than $10,000, which combined for a less proportionate 12.0% of the banking system's financial savings. In contrast, approximately 71.4% of resources were held by the 2.4% of depositors with balances in excess of $50,000. The next largest accumulation of deposits (5.2%) was held by savers with deposits within the $10,000 - $30,000 range (10.5%) and the remainder (1.3%), among depositors whose balances were in the $30,000 - $50,000 range (6.1%).

Domestic Credit

Growth in overall domestic credit eased to 1.9% from 2.2% in the first quarter in 1999, as the public sector's strong net repayment position significantly mitigated the appreciably higher advance in private sector credit. For the public sector, a 3.8% net repayment contrasted with the year-earlier growth of 2.2%. Specifically, net credit to Government, which advanced by 7.2% in 1999, contracted by 3.1% as the National Insurance Board acquired virtually all Treasury bills held by the Central Bank. Meanwhile, the banking system's claims on the rest of the public sector declined further by 5.6%, albeit at a moderated pace from last year's 14.6% fall-off.

Private sector credit expansion moved higher to $99.4 million (3.2%) from $61.4 million (2.2%) in 1999, largely attributed to increased recourse to overdraft facilities alongside accelerated lending for housing and consumer durables. On a currency basis, the firming was evident in both Bahamian dollar and foreign currency claims at 2.7% and 6.4% vis-à-vis respective year-earlier hikes of 2.0% and 3.4%. In this regard, local currency claims represented a slightly reduced 77.8% of the total increase.

Changes in Credit



Although personal loans' share of private credit slackened to 65.3%, growth was appreciably higher at $60.2 million (2.9%) from $7.9 million (0.4%) last year. In particular, overdraft balances registered renewed growth of 17.5%, following the year-earlier contraction of 38.4%. Growth in consumer credit more than doubled to 1.6% from 0.7% and housing loans (mainly mortgages) rose at a strengthened 4.3% pace from 3.3% in 1999.

Within the consumer credit category, notable growth was recorded for private cars (4.9%), taxis and rented cars (6.9%), land purchases (2.3%), debt consolidation (0.8%), medical (2.5%) and miscellaneous purposes (3.8%). Categories posting net repayments included travel (6.9%), education (1.5%), home improvement (0.9%) and credit cards (4.1%).

Distribution of Bank Credit By Sector
End-March

	1999		2000	
	B$M	%	B$M	%
Agriculture	17.1	0.6	11.4	0.3
Fisheries	7.6	0.3	5.8	0.2
Mining & Quarry	19.1	0.6	16.7	0.5
Manufacturing	64.2	2.1	88.4	2.6
Distribution	203.8	6.6	150.9	4.3
Tourism	200.6	6.5	223.6	6.4
Enter. & Catering	19.7	0.6	25.7	0.7
Transport	27.2	0.9	47.1	1.4
Public Corps.	105.3	3.4	149.1	4.3
Construction	165.4	5.3	243.7	7.0
Government	86.2	2.8	84.6	2.4
Private Financial	7.3	0.2	3.0	0.1
Prof. & Other Ser.	134.6	4.4	129.7	3.7
Personal	1918.7	62.1	2121.6	60.9
Miscellaneous	112.0	3.6	180.8	5.2
TOTAL	3088.8	100.0	3482.1	100.0

Sectoral analysis of private credit also indicated noteworthy quarterly gains for manufacturing (40.9%), tourism (4.1%), transport (4.6%), construction (1.9%) and miscellaneous purposes (5.5%). Meanwhile, net repayments were recorded for mining and quarrying (4.6%), distribution (6.4%) and private financial institutions (20.8%).

Commercial Banks

During the review quarter, commercial banks' deposit liabilities to the private sector increased by 4.4%, outstripping the 3.1% advance in lending to the sector. This, combined with a 1.8% decline in net claims on the public sector, accommodated a 4.9% reduction in commercial banks' net foreign liabilities.

On a proportional basis, commercial banks' share of total banking sector deposit liabilities was placed at 97.8%, with the bulk (90.9%) owing to the private sector. Approximately 60.0% of deposits was held as fixed balances, 22.2% as demand and 17.8% as savings.

Other Local Financial Institutions

The OLFIs' external exposure switched to a net foreign liabilities position of $12.1 million from a net foreign assets position of $2.1 million last quarter. In this regard, growth in private sector domestic deposits slackened to 4.8% from 8.7% last year, to trail firmer credit expansion of 6.3%. Mortgages led the increase in credit, expanding by 8.6% to $72.7 million, and represented 81.6% of total loans.

A broader analysis of deposit liabilities showed that the majority was held in fixed deposits (89.2%), followed by demand deposits (7.0%) and savings (3.8%).

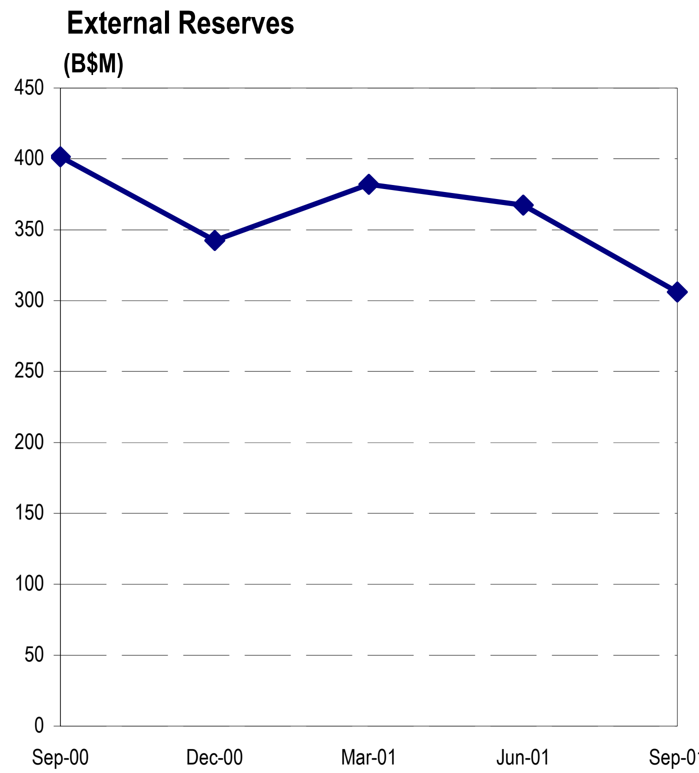
CENTRAL BANK

During the review quarter, the Central Bank's net claims on Government fell by 20.6% to $55.4 million, following the sale of Government paper to the National Insurance Board. Meanwhile, external reserves recorded a healthy gain of $46.4 million (11.5%) to $450.4 million—although below the more robust strengthening of $72.8 million (21.5%) registered last year when growth in net inflows to the banking system were stronger amid milder consumer credit expansion.

Underlying external reserves movements, the Bank's total foreign currency sales rose by 21.1% to $110.9 million, while total purchases fell by 8.8% to $144.8 million. A 29.9% reduction in the net purchase from commercial banks to $70.2 million was reinforced by the increased net sale to the public sector of 10.3% to $36.3 million.

INTEREST RATES

Interest rate movements during the review quarter featured lower average lending rates, particularly for residential mortgages and consumer lending. In the context of moderately higher deposit rates, the estimated interest rate spread between deposits and loans narrowed to 7.44% from 8.05%. In particular, the weighted average rate of interest on deposits rose by 16 basis points to 3.92%, while the weighted average lending rate fell by 45 basis points to 11.36%.



Firming on the deposit side, which was strongest on the upper end of the maturity spectrum, was underscored by the higher average band on fixed deposits of 3.92%-4.59% as compared to 3.72%-4.35% in the previous quarter. Meanwhile, average lending rates were primarily influenced by declines in the more heavily weighted rates on residential mortgages (22 basis points lower at 9.06%) and consumer loans (13.26% vis-à-vis 13.53%). Conversely, the average commercial mortgage rate rose to 9.63% from 9.20% and the rate on overdrafts, to 10.52% from 10.10%.

Official rates—the Central Bank’s Discount Rate and commercial banks’ Prime—were unchanged at 5.75% and 6.00%, respectively. The rate on 90-day Treasury bills was virtually stable at 0.96%, and there were no primary activities in long-term government securities during the quarter.

BANK PROFITABILITY

The most recent data on bank profitability for the quarter ended December 1999, indicate a $5.4 million (19.6%) decrease in domestic banks' net income over the corresponding 1998 period. This outturn primarily reflected a significant increase in non-staff related operating costs—including Y2K computer expenses—which contrasted with almost stable net interest income.

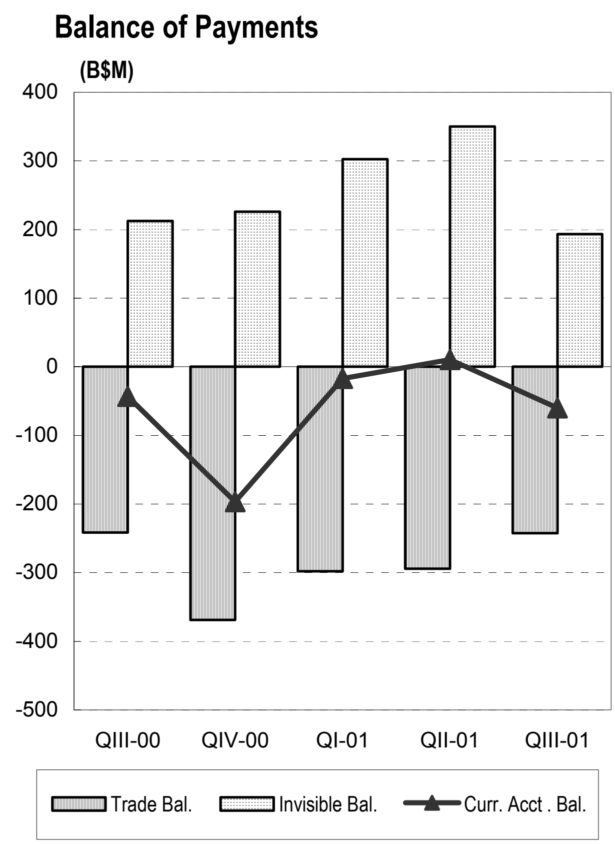
Against the background of steady increases in balance sheet aggregates, however, profitability, relative to average assets (the return on assets ratio), slackened to 2.04% from 2.87% in the final quarter of 1998. In particular, the net interest margin decreased to 5.10% from 5.69%, and the contribution from commissions and foreign exchange income was reduced to 0.52% from 0.59% in 1998. Conversely, operating costs, as a fraction of average assets, stabilized at 3.77%.

INTERNATIONAL TRADE AND PAYMENTS

Preliminary indications are that the first quarter deficit on the current account of the balance of payments expanded by an estimated 13.8% to $131.7 million. Although exports grew by 7.9%, strengthened demand for durable goods imports and higher oil prices caused the trade deficit to expand by 28.4%, while net invisible receipts fell by 1.1%, in the wake of higher net remittances for non-tourism related external services.

The merchandise trade deficit widened to an estimated $333.3 million, as total imports rose by 6.8% to $442.7 million to offset the 7.9% gain in exports to $109.4 million. In line with rising growth trends and higher levels of consumer confidence, non-oil imports grew by 3.2% to $388.1 million and the sharp increase in fuel prices pushed the oil bill appreciably higher by 42.7% to an estimated $54.1 million. In particular, the per barrel prices for motor gasoline and jet fuel surged to $63.67 and $36.53 from $20.52 and $18.00, respectively. Likewise, the per barrel cost of gasoline oil was almost doubled at $34.14, while bunker 'c' fuel costs firmed by 29.2% to $37.04 per barrel and aviation gasoline, by 19.7% to $82.32 per barrel.

Net invisible inflows decreased marginally by $2.6 million (1.1%) to $229.4 million during the review quarter. Although net tourism receipts improved by an estimated $20.1 million (5.9%) to $363.1 million, a significant offset was provided by the $10.2 million (38.7%) decrease in offshore companies' local expenses. Other offsets included higher net payments for transportation services ($5.3 million); Government's net external payments ($3.2 million) and "other" net payments—inclusive of foreign construction services and credit card remittances—($2.7 million).



On the income side, net factor remittances fell by 10.6% to $39.0 million. Net repatriation of investment income declined by 14.1% to $29.7 million, as against only slightly increased workers' net remittances of $9.2 million.

Net inflows under transfers improved to $11.2 million from $8.7 million last year, as the increase in Government's net receipts (20.7%) was reinforced by the marginally lower net private sector outflow of $0.4 million.

The estimated surplus on the capital and financial account narrowed to $80.9 million from $99.3 million in the first quarter of 1999. While migrants' capital transfers remained in a small deficit of $2.7 million, net investment inflows under the financial account decreased to $83.6 million from $101.8 million in 1998, still benefiting from investment flows to the hotel sector.

Disaggregation of the financial account reveals that net foreign direct investment flows were higher at $40.0 million vis-à-vis $13.6 million in 1999. Private equity flows, at $35.6 million, advanced by more than three-fold and net real estate investments rose by a third to $4.3 million. In a strong offset, however, net private loan inflows contracted to $47.1 million from $77.0 million in 1999. Moreover, the public sector's net foreign currency borrowings subsided to $3.2 million from $9.3 million in 1999, while banks recorded a net outflow of short-term capital of $6.7 million as compared to 1999's net inflow of $1.9 million.

In the context of these developments, and after adjusting for possible errors and omissions, the overall payments balance—measured by the increase in the Central Bank's external reserves—recorded a surplus of $46.3 million in the first quarter of 2000. This, however, was considerably less than last year's $72.8 million surplus.

INTERNATIONAL ECONOMIC DEVELOPMENTS

Global economic output improved further during the opening quarter of 2000, as the growth momentum remained strong in both the United States and Europe and a recovery appeared evident in Japan. Economic conditions supported progress in fiscal consolidation efforts in most major industrial countries, but tighter labour markets combined with higher energy prices for a broadbased increase in average inflation, which prompted a further series of official interest rate hikes. Despite firming credit conditions, major equity market indices recorded modest appreciations, with strong gains in technology stocks broadly offsetting the negative response of "old economy" stocks. In currency developments, the euro and other major currencies continued to depreciate steadily against the United States dollar, on account of the relatively more robust US economy. Developments on external sector accounts remained mixed, amid the varying growth outcome among the major industrial economies.

In the United States, the longest economic expansion on record continued at a brisk annualized rate of 5.4%, although moderating from the revised 7.4% posted in 1999 Q4. Despite higher interest rates imposed by the Federal Reserve, both consumer spending and business investment remained exceptionally strong, and exports continued to strengthen. Germany's real GDP rose by an estimated 2.7%, following the preceding quarter's 3.2% gain, as rising domestic demand and sustained export growth were reinforced by the significantly weakened euro. In the United Kingdom, indications are that the expansion slowed significantly to an annualized 1.2% rate from the previous quarter's 3.1%, as sterling's appreciation vis-à-vis the euro constrained exports to countries within the European Monetary System. Preliminary indications are that the Japanese economy expanded by a robust 11.0% annualized rate in the first three months of 2000, the best quarterly performance in over 25 years. In addition, for the fiscal year to March the economy recorded its first positive 12-month growth in more than two years of 0.4%, albeit slightly below government's growth target of 0.6%.

Labour market developments in the major economies were underscored by continued job gains in Europe's two largest economies and persistent tightness in the United States and the United Kingdom. In particular, Germany's jobless rate fell to an average 10.1% from 10.4% in the preceding three months and average French unemployment, to 10.2% from 10.8%. Although the United States' average jobless rate stabilized at 4.1%, the monthly rate declined to a 30-year low of 4.0% in March. Employment growth in the United Kingdom also secured a reduction in the claimant unemployment rate to 4.0% from 4.1% last quarter. In contrast, the Japanese average unemployment rate rose to 4.8% from 4.6% in the previous quarter.

Amid substantial increases in energy costs and tightening labor markets, consumer price inflation accelerated in most of the major industrial countries during the review quarter. In the United States, the first significant sign of capacity constraints was reflected in a rise in annualized inflation to 4.0% from 2.9% in the previous quarter. A weakened currency was a factor within the European Monetary System, where inflation firmed to 2.9% from 1.8% in the fourth quarter of 1999, with Germany's rate accelerating to 2.8% from 1.5%. In the United Kingdom, the quarterly rise in average consumer prices slackened on an annual basis to 1.7% from 2.6%.

Deflationary pressures persisted in Japan, where the decline in average consumer prices abated to 0.4% from 0.9% last quarter, due largely to the appreciation of the Yen and ongoing weakness in consumer demand.

In foreign exchange markets, the United States dollar strengthened steadily against all major currencies, partly associated with the upward revisions to US growth prospects and favourable movements in interest rate differentials. In particular, the dollar rose by 4.6% and by 4.4% against the Deutschemark and Swiss Franc to DM2.03 and SF1.66, respectively. The dollar also appreciated by 0.7% against both the Canadian dollar and pound sterling to C$1.45 and £0.63, respectively and by 3.3% vis-à-vis the Yen, to ¥105.49. In contrast, the euro, which continued to experience widespread depreciation, weakened against the dollar by 5.0% to €1.05, bringing the total depreciation since its 1999 debut to more than 21%.

Commodity market price developments were mixed during the quarter. Oil prices surged to a high of $34.13 per barrel in early March, before retreating to $26.90 as OPEC eased production restraints. Conversely, the price of gold lost additional value, closing 4.1% lower at $276.75 per ounce.

Global equity markets recorded increased volatility in the first quarter, influenced by strong investor demand for high technology, media and telecommunication stocks, which rallied at the expense of more established "old economy" stocks. In this regard, the United States' tech-heavy Nasdaq composite advanced by 12.4% versus a more modest rally in the broader S&P 500 index of 2.0%. With investors factoring an eventual slowing of the United States' economy because of higher interest rates, the Dow Jones Industrial Average (DJIA) and the United Kingdom's FTSE-100—both principally comprised of "old economy" stocks—declined by 5.0% and 5.5% respectively during the quarter. Adding to the strong gains achieved last quarter, technology and internet stocks pushed France's CAC-40 index higher by 5.5% and Germany's Dax and Japan's Nikkei 225 indices up by 9.2% and 7.4% respectively.

On the monetary front, concerns that the strong growth momentum would present upside risks to price stability occasioned another round of interest rate tightening among major industrial economies. The Federal Reserve Board increased short-term rates for the fifth time since June 1999, hiking both the federal funds and the discount rates by 25 basis points, on two successive occasions, to 5.50% and 6.00%, respectively. The European Central Bank (ECB) also raised its repurchase rate on two occasions by a total of 50 basis points to 3.50%, and the Bank of England increased its official short-term rate by 25 basis points to 6.00%. Conversely, the Bank of Japan maintained its zero interest rate policy.

Apart from Japan, the major economies continued to make progress on the fiscal front, due largely to stronger revenue growth amidst improving economic activity. In the United States, indications are that the federal surplus for fiscal year 2000, which began in October 1999, will substantially exceed last year's $123.6 billion. In the first three months of FY2000, an estimated surplus of $112.2 billion was recorded compared to $59.7 billion in the same period last year. Within the context of a fiscal surplus expected to nearly double last year's £7.0 billion, the United Kingdom's Chancellor of the Exchequer made his budget statement on March 21, which included increases in government consumption and investment. In contrast, while Japan's continued use of fiscal stimulus seems to have had a negligible positive effect on the economy in the second half of 1999, it substantially boosted the deficit for the fiscal year to above 11.0% of GDP.

On the external side, the evolution of current accounts continued to mirror differences in growth rates among the major industrial economies. In the United States, the estimated trade deficit widened, pacing above the fourth quarter's annualized $365.89 billion, with the demand for imports still surpassing strengthening exports. Meanwhile, the continued appreciation of the pound sterling, particularly in relation to the euro, hindered the United Kingdom's exports to Europe, causing the trade deficit to widen further vis-à-vis 1999 Q4, to $48.6 billion on an annual basis. Conversely, currency weakness and boosted net exports expanded the respective trade balance surplus of Germany and Japan above the previous quarter's $64.4 billion and $120.8 billion. Indications are that Japan's current account surplus widened to an estimated annualized $135.7 billion from $103.5 billion in the previous quarter and Germany's deficit improved to $16.4 billion from $30.8 billion.

STATISTICAL APPENDIX

(Tables 1-16)

STATISTICAL APPENDIX

The following symbols and conventions are used throughout this report:

1. **n.a. not available**
2. **-- nil**
3. **p = provisional**
4. **Due to rounding, the sum of separate items may differ from the totals.**

GROSS ECONOMIC CONTRIBUTION OF BANKS AND TRUST COMPANIES IN THE BAHAMAS, 1999

INTRODUCTION

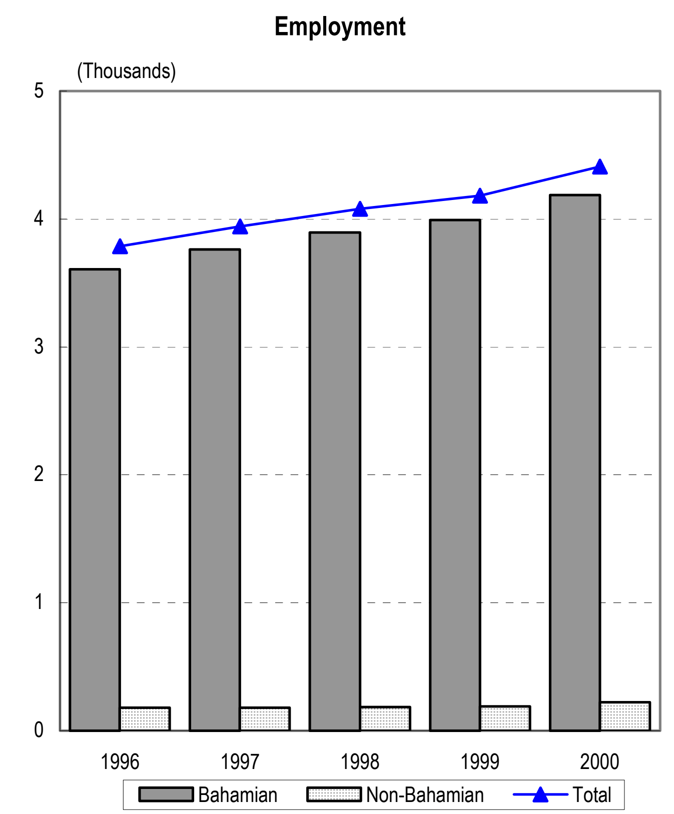
Results from the 1999 survey of the **Gross Economic Contribution of Banks & Trust Companies** confirm the banking sector's ongoing strong contribution to the Bahamian economy, through steady growth in employment and expenditures. This year's assessment was significantly shaped by the sharp boost in Y2K related capital and administrative outlays and growth in the number of physical operations. The economic importance of the banking sector to the Bahamian economy is underscored by the fact that banks account for just over half of the financial sector's estimated 15.0% direct contribution to GDP. With the intensification of global competition for financial services, the task of preserving and expanding upon the opportunities remains a tremendous challenge for The Bahamas. Indeed, both private and public sector efforts are focused on maintaining a well regulated and supervised environment for financial institutions, yet providing the flexibility and ease required of the modern day investor. Considerable resources have been channeled into staff training and key infrastructural supports, such as telecommunications.

Banking and trust operations were undertaken by 415 licensed institutions, 3 less than in 1998. In particular, the number of public banks and trust companies fell by 6 to 276, non-active licences declined by 1 to 16 whereas restricted licences rose by 4 to 123. In line with the domestic authorities' desire to secure greater domestic value added from banking operations, the number of public institutions with a physical presence rose to 199 from 193 in 1998. A further breakdown of public institutions shows that 191 were Bahamian incorporated and 65 were euro-currency branches of foreign banks and trust companies. The remaining 20 were authorized dealers and agents operating within the domestic sector, of which 7 were commercial banks; 2, savings and loans institutions and 11, trust companies.

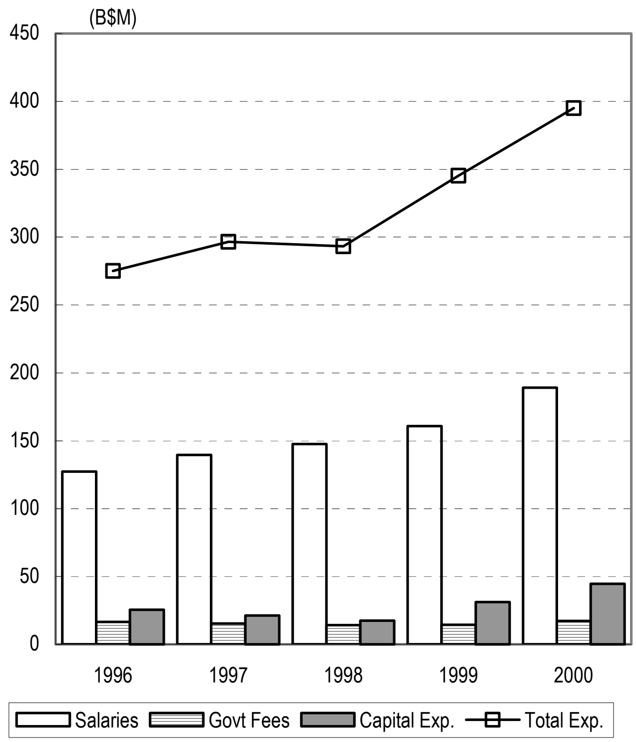
The asset base of the banking system is estimated to be in excess of $230 billion, with the bulk of activity concentrated in the offshore sector. Off-balance sheet activity, although not directly measured, is placed at an equally significant level. Banks' domestic assets approximated $4.4 billion, which were less than 2.0% of the consolidated resources, but approached 100% of The Bahamas' GDP.

OVERALL TRENDS IN EMPLOYMENT

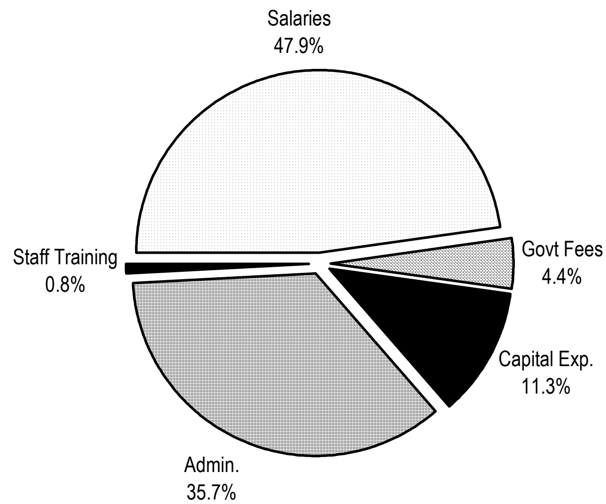
Employment growth in the banking sector continues to be influenced by the increased use of technology and the competitive consolidations both across offshore jurisdictions and among financial institutions. During 1999, total employment rose by 65 (1.6%) to 4,145 indivuals, as compared to a stronger net increase of 138 positions (3.5%) in 1998, and average gains of 3.1%. in the five years through 1998. Employment growth was almost entirely concentrated in the Bahamian workforce, which rose further by 66 (1.7%) to 3,961 persons and accounted for 95.6% of the total employment. Meanwhile, the expatriate labour complement was one less at 184.



Expenditure



Expenditure Components (% of Total)



EXPENDITURES

As regards expenditures, banks recorded significantly expanded outlays in the economy during 1999, corresponding to a broadbased increase in operating costs and aggressive investments in office premises and Y2K compliant technology. Total expenditures advanced by $48.9 million (16.7%) to $342.1 million, constrasting with a marginal decline of 1.1% in 1998. The increase was also stronger than the previous five-year average uptrend of 6.7% .

On a proportional basis, banks' operational expenses—inclusive of salaries, government fees, training and administrative costs—comprised 90.9% of total outlays, which was below the 92.1% average posted during 1994-1998. Correspondingly, the share absorbed by capital expenditures on new premises, renovations and the acquisition of fixed assets rose above-trend to an expanded 9.1% share in 1999, relative to 7.9% over the previous five years.

Total operational outlays grew significantly by $35.2 million (12.7%) to $311.0 million in 1999, for a marked strengthening vis-à-vis an almost level position in 1998 and less robust healthy average yearly gains of 7.4% during the prior five years. A key factor was the 20.9% hike in administrative costs to $134.9 million, largely associated with outlays on Y2K computer related preparations. Salaries, which represented an estimated 46.5% of banks' total expenses, also rose by 7.9% to $159.2 million, exceeding both the 1998 advance of 5.8% and the 1994-1998 average growth of 7.1% per annum. Gains partly reflected the increase in total employment, but the estimated 6.2% rise in average salaries to $38,408 was also significant. This capped average annual increases of 3.9% in the five years through 1998, and paced ahead of inflation, which has correspondingly averaged 1.4% per annum.

Direct training outlays by banks rose at a healthy pace of 10.2% to $2.7 million in 1999, in line with the average annual rate of increase observed since 1994. In this regard, most local training initiatives take advantage

of programs offered at The College of The Bahamas and the Bahamas Institute of Bankers.

The Government's estimated direct benefit from the sector's presence in The Bahamas, in the form of revenue receipts, was stable at $14.2 million and accounted for 4.6% of banks' operational outlays. Licence fees still represented the largest revenue component at $8.1 million (56.8%), followed by other receipts such as import duties and stamp and real property taxes, at a combined $3.9 million (27.4%). Meanwhile, company registration and work permit fees constituted the remaining $2.2 million (15.8%). On a cumulative basis, total revenues paid to government since 1994 amounted to some $90.7 million.

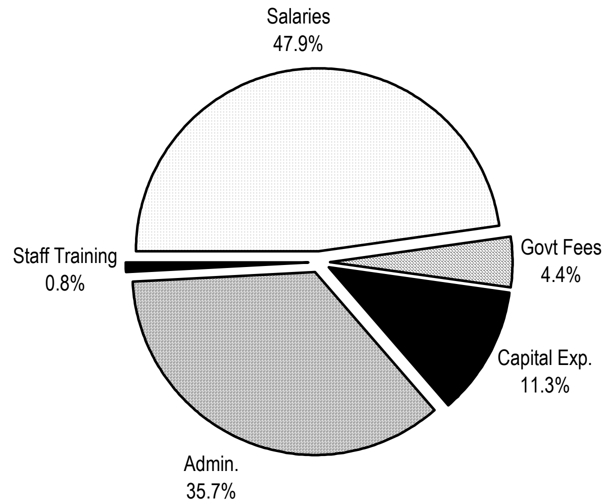
In addition to construction of office premises, the elevated level of capital investments among banks in 1999 was strongly influenced by information systems' upgrades to ensure Y2K compliance and related contingency requirements. In particular, financial institutions' total capital spending almost doubled to $31.2 million from $17.4 million in 1998. Reflecting technology upgrades, outlays on fixed assets rose to $19.9 million from $11.2 million in 1998. Meanwhile, expenditures on new office premises increased almost four-fold to $9.2 million. Banks also boosted real estate purchases modestly, but expended a reduced amount on renovations.

Domestic vs. Offshore

Disaggregation of the banking sector's economic contribution into domestic and offshore components reveals that, while there is some overlapping of offshore and local operations, the retail, labour intensive nature of the local operations still accounts for the predominant share of the domestic banks' expenditures in the economy.

During 1999, total employment in the domestic sector rose by 25 (0.8%) to 3,203 positions. This outturn primarily reflected an overall increase in the number of Bahamians by 32 (1.0%) to 3,155, to contrast with a decline in expatriate staff by 7 to 48. The corresponding ratio of Bahamians to non-Bahamians rose to 66:1 from 57:1 in 1998.

Expenditure Components (% of Total)



In the offshore sector, with the higher concentration of expatriate staff, total employment rose by 40 (4.4%) to 942 persons—a development linked to the increase in physical offices located in the jurisdiction. Both local and foreign staff registered respective gains of 34 and 6, to 806 and 136. Meanwhile, expatriates continued to represent a larger 14.4% of the offshore workforce, compared to a sizeably reduced 1.5% in the domestic sector.

Average salary comparisons are consistent with earlier observations, which evidenced premium compensation in the offshore sector relative to the domestic, given the greater concentration of skills as well expatriate management in the former. The respective average annual compensation for both domestic and offshore employees rose by 4.0% to $35,279 and $49,045, widening the earnings gap vis-à-vis 1998. Nevertheless, indications are that the improved profitability of domestic operations allowed salaries in the sector to increase at a faster average annual rate of 4.4% during 1994-1998 as compared to average hikes of 2.4% per annum in the offshore sector.

Following 1998's 4.1% contraction, domestic institutions' total expenditures rebounded strongly by 15.5% to $219.2 million in 1999, and represented 64.1% of the sector's total expenditures. In light of Y2K related expenditures, this uptrend also paced strongly ahead of the five year average annual growth of 6.9% through 1998. The upturn in operational costs was estimated at 12.6%, placing outlays at $203.2 million, with administrative costs rebounding by 20.0%. Reflecting licence fee increases for commercial banks, Government fees paid by domestic institutions rose sharply by 43.1% to $6.5 million. Salary payments advanced further by 6.8%, following a 5.7% boost in 1998, with direct expenditures on training only incrementally reduced. Meanwhile, capital spending, which comprised an increased 7.3% of the 1999 expenditures, rose sharply to $15.9 million from $9.3 million, almost entirely reflecting Y2K related investments. This contrasted with a negative average annual growth of 4.8% over the previous five years.

Among the offshore banks, a near doubling in capital spending to $15.2 million also influenced the 18.9% boost in aggregate spending to $122.9 million in 1999. The uptrend also paced significantly ahead of the previous five-year average annual growth of 6.3%. Apart from investments in technology, growth in the capital budget reflected ongoing construction of new office premises. Operational expenses, which advanced at an accelerated pace of 13.1% to $107.7 million, also was influenced by Y2K related increases in administrative outlays. Corresponding to faster employment growth relative to domestic banks, offshore salary payments grew at a comparatively stronger pace of 10.7%, and direct training expenses were boosted by 42.4%. The offshore banks' contribution to Government however, fell by 19.9% to $7.7 million, reflecting a small reduction in license fees paid and a decline in import duty payments.

Other Developments in the Financial Sector

As The Bahamas intensifies its efforts to attract more physical operations to the jurisdiction, growth in employment and other direct benefits to the economy are expected to continue over the medium term, notwithstanding ongoing consolidations brought on by technology and heightened competition. Such growth prospects augur well for the increasingly diverse character of the offshore financial sector, with direct spin-off benefits to the banking sector from activities such as international business companies (IBC) registration and management and mutual funds management. During 1999, IBC registration rose by 18.4% to 100,092 entities. While the amount of assets under management fell by 3.8% to $84.5 billion because of portfolio adjustments, the number of mutual funds being managed rose further to 596 from 584 in the previous year.

Domestic banking operations were affected by the passage of the Protection of Depositor Act in September 1999, providing for a deposit insurance scheme for resident Bahamian dollar deposits up to a maximum of $50,000. Initial funding of the Deposit Insurance Corporation (DIC) was sourced from equal $0.5 million contributions from the Central Bank and domestic banks, alongside a government-guaranteed bond issue of $6.75 million. These proceeds assisted with the payout to depositors of Gulf Union Bank (Bahamas) Limited (in liquidation). Under the terms of the Act, premium contributions to the DIC are assessed at the rate of 0.005% of institutions' resident Bahamian dollar deposits−averaged over the end of March and September of the previous year.

Another development that is expected to have a positive impact upon the banking sector, particularly offshore, is the recent establishment of The Bahamas International Stock Exchange (BISX). Most of the technical and legislative hurdles surrounding the operations of the Exchange were resolved during the first quarter of 2000, and the domestic side of operations commenced shortly thereafter. It is expected that offshore operations on BISX will start before the end of 2000. As for domestic banks, the inauguration of BISX's local operations presents both competitive opportunities and challenges, as more large and medium sized firms are expected to use this medium to raise capital.

The ensuing years will present many challenges to offshore banking in The Bahamas as the jurisdiction defends its reputation as a legitimate well-regulated center in the wake of initiatives launched by the Organization for Economic Cooperation and Development (OECD) and the Financial Stability Forum (FSF). These initiatives are targeted at the majority of offshore centers and seek to provide for more open information sharing arrangements, particularly in taxation matters. The Bahamian authorities have restated their commitment to ensuring that anti-criminal and other supervisory efforts are continually strengthened, and to take the necessary steps to ensure that the offshore sector continues to enjoy its positive international stature.

SURVEY OF PRIVATE PENSION PLANS IN THE BAHAMAS (1997 & 1998)

INTRODUCTION

Private pension schemes in The Bahamas represent an important source of domestic savings, alongside resources managed by banks, insurance companies and the National Insurance Board. Based on the latest surveys conducted by the Central Bank of The Bahamas for 1997 and 1998, aggregate savings in these arrangements continued to accumulate at a strengthening pace, benefiting from the general buoyancy in economic conditions. Growth has been favoured by firmer rates of return on invested assets, significant employment gains, which led to an increase in the number of participants—especially in the tourism sector—and a rising income base from which schemes are partially funded. On course to surpass the $600 million mark by the end of 2000, pension fund resources were equivalent to approximately 16.7% of GDP in 1998 as compared to an estimated 11.3% in 1992, and represented some 14.4% of banks' 1998 domestic asset. The only other significant concentrations of domestic savings are with the National Insurance Board, whose domestic assets approached $908 million in 1998, and insurance companies, which control more than $300 million in mortgages and other assets.

The significance of privately funded pension schemes lies in their ability to allow participants to accumulate significant supplementary savings toward retirement, facilitate a more efficient management of such assets and provide a stable pool of investment resources for productive economic activities. The importance of these institutional investors will undoubtedly become more evident as domestic capital markets continue to deepen.

In view of the increased investment risks associated with such developments, emphasis is already being placed on providing a proper regulatory framework for domestic pension schemes. The existing plans have generally been established as trust arrangements, where the funds are kept separate from the respective companies' assets. The appointed trustee boards either rely on in-house administration of funds or secure the services of external managers. In this regard, survey results show that most plans were administered by insurance companies (42.5%), while a comparable number was managed in-house (41.5%). The other plans are administered by banks, trusts and other entities. As to financial controls, about three quarters of local plans are audited on an annual basis, and actuarial assessments are regularly relied on to ensure the long-term financial solvency of schemes.

As such, the proposed legislation is generally expected to institutionalize existing administrative arrangements, which conform, in most instances, to international norms for pension fund management. Nevertheless, the increase in transparency and efficiency that is expected to result from this process should provide a sound base for future growth and development of the sector.

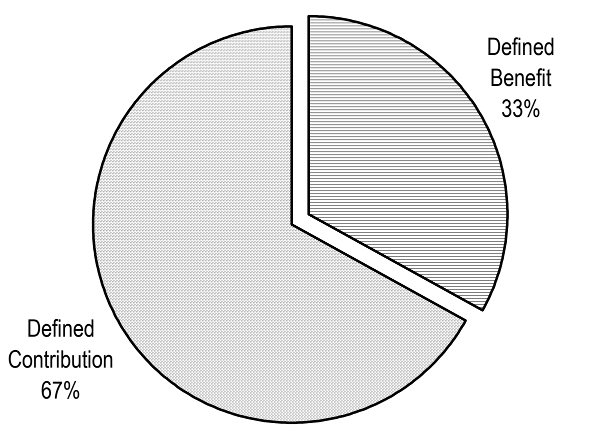
EVOLUTION AND PROFILE OF PRIVATE PENSION SCHEMES

While historical evidence dates the use of pension arrangements by The Bahamas Government to as early as 1862, the first private plans were not established until the early 1960's, influenced in many instances by labour unions, which sought to secure higher retirement incomes for their members. Indeed, some of the older private pension arrangements were in the highly unionized communications & utilities sector. Also significant was the increased use of plans by business firms to make employment opportunities more attractive.

Existing plans in The Bahamas fall into three categories: defined benefit, defined contribution and provident fund schemes. Defined benefit plans guarantee their participants the payment of a specified periodic retirement benefit. From an actuarial standpoint, these plans are required to maintain a present-value balance between future benefits (liabilities) payable under the schemes, relative to accumulated and expected future contribution (assets) receipts. A fully funded plan maintains an actuarial balance between assets and liabilities; an arrangement is said to be under funded if it has potentially greater future liabilities, and overfunded if it has potentially greater future assets.

Under a defined contribution plan, periodic benefit payments to retirees depend entirely on the total net value of contributions made into the respective participants' accounts. For provident fund schemes, which also link benefits to contributions, the main distinction vis-à-vis defined contribution schemes is that an employee's retirement benefit is disbursed in a lump sum amount. Because of similarities, the analysis that follows groups together these two types of plans.

Pension Funds By Type (1998)



The 1998 Survey was sent to 125 plans of which responses were received from 106. Where possible, consolidated estimates were made for non-respondents based on broad sector trends. Of the 106 responses received for 1998, approximately 71 were defined contribution (or provident) schemes and 35 were defined benefit plans. However, defined benefit plans encompassed some 86.7% of all pension fund participants, reflecting the presence of several large arrangements within the tourism (hotels & restaurants) and communications & utilities sectors. Among the 35 defined benefit plans, 14 were identified as being over-funded by an aggregate \$14.3 million; 11 were under-funded by \$45.9 million and 10 were adequately funded.

Survey results show that the majority of funds were established during the last two decades. Specifically, 46 schemes were started during the 1980s and 42 others during the 1990s, compared to 7 in the 1960s and 11 in the 1970s. With the establishment of new schemes, the data also reveals a notable shift in preference towards defined contribution arrangements, mainly related to the increasing use of such plans by smaller companies. In particular, while only 22.2% of all plans in existence up through 1979 were classified as defined contribution, the respective ratio increased to 54.7% and 67.0% when extended to the end of 1989 and 1998.

Employee participation was compulsory in approximately half of the plans. In this regard, the smaller defined contribution schemes had fewer incidences of compulsion (approximately 40.9%) compared to almost three quarters for the defined benefit schemes.

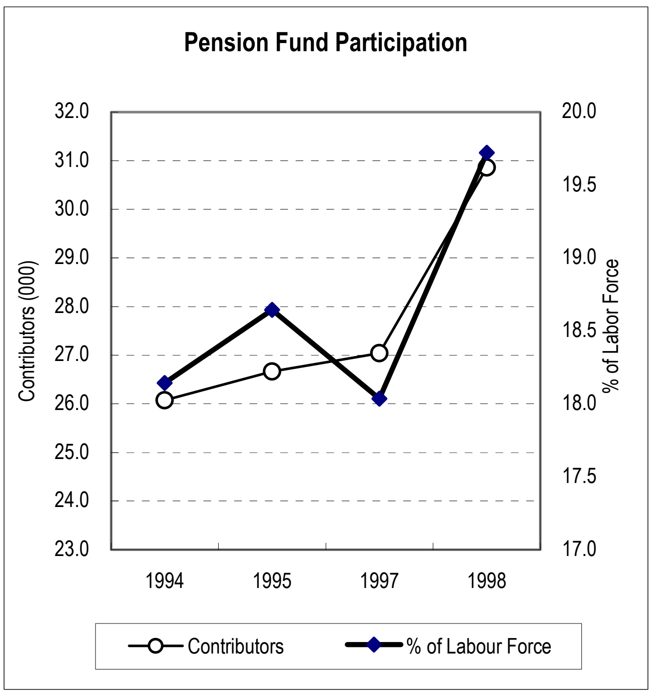
CONTRIBUTION RATES

There does not appear to be any institutional or sectoral pattern for contribution rates for pension schemes surveyed. Under the most common arrangement, contributions equate to 10% of the participant's salary, and the cost is shared equally between the employer and employee. However, on an industry wide basis, the average employer's contribution exceeded the employee's. For defined contribution plans, the respective rates were 6.2% and 4.3% compared to 5.6% and 2.5% for defined benefit schemes. The data also contained considerable variance in contribution rates from plan to plan. For employees, contribution rates ranged between 2.0% and 10.0%, while employer payments ranged between 1.0% and 22.0% of paid salary.

PARTICIPATION

Indications are that pension schemes cover less than 20% of the Bahamian workforce, as compared to approximately 25% around the beginning of the decade. Nevertheless, some recovery has been noted relative to the low points of the recent recession, with the coverage ratio moderately higher at 19.7% in 1998, compared to

18.0% in 1997 and 1994's low of 18.1%. Regarding the total number of participants, coverage rose moderately by 1.4% to 27,039 persons during 1995 - 1997, and more vigorously by 14.1% to 30,857 persons in 1998. Growth between 1995 and 1997 was mainly concentrated among defined contribution plans and during 1998 among defined benefit plans. On a sectoral basis, just over half of the gain through 1997 was underpinned by the increase in financial sector participants, while strengthening hotel sector employment accounted for some four-fifths of the advance in 1998.



The hotel & restaurants sector maintained by far the largest share of pension fund participant—19,401 or 62.9% of the total in 1998. This was followed by the communications & utilities sector (mainly the public corporations) at 3,800 (12.3%) and the financial sector, at 3,150 (10.2%).

Pensioners and Benefit Payouts

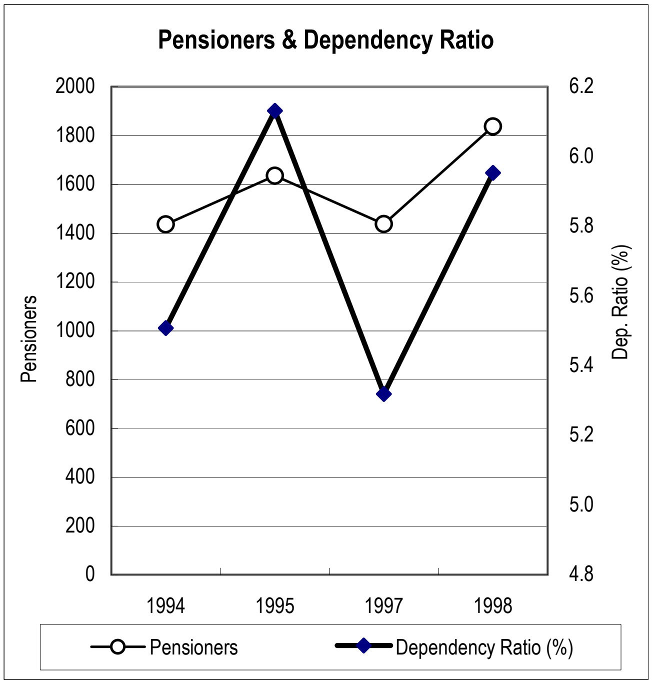
Despite the notable increase in participants in pension schemes, the ratio of pensioners to active participants for 1998 rose to approximately 1:17 from the 1997 ratio of 1:19. Along with the relative increase in beneficiaries, the dependency ratio firmed to 6.0% in 1998 from 5.3% in 1997. Attributing to these trends was the 27.8% advance in the number of pensioners to 1,837, mainly corresponding to increased hotel sector retirees. This was matched by a similarly strong advance in the aggregate value of annual pension benefits to $11.0 million from $8.5 million in 1997.

Asset Size and Disposition

Local estimates of pension resources understate the total vested interest of the Bahamian workforce, as there is a significant level of participation in the globally managed plans of foreign multinational and offshore financial institutions. In such instances, these contributions are generally funded from resources from outside The Bahamas and invested externally as a part of the global consolidated scheme.

In respect of reported data in the two years through 1997, the value of domestic pension fund assets grew by an inflation-adjusted rate of 14.8% to $500.7 million, and further by 11.5% to $564.9 million in 1998. Comparatively, the real growth rates in the banking sector's domestic assets were more accelerated at 23.1% between 1995 and 1997, and at 12.4% in 1998. Meanwhile, the National Insurance Fund, the largest single accumulation of domestic savings, totalled $907.6 million in 1998, growing at a comparatively slower rate of 13.5% and 5.9% in both periods.

An analysis of assets based on the types of pension funds revealed that just over four-fifths of the aggregate ($463.7 million) was concentrated among defined benefit plans, with the remaining $101.1 million held by defined contribution schemes. In contrast to previous years, the growth in assets was more significantly influenced by increased workforce coverage as opposed to hikes in contributions, as evidenced by the marginal decline in the average level of savings per participant to $18,306 in 1998 from $18,517 in 1997. Meanwhile, the distribution of the asset base was strongly correlated with the length of time that funds had been in existence. In particular, the 18 plans established during the 1960s and 1970s amassed savings of $306.6 million (54.3% of the total), compared to an estimated $258.3 million among the 88 plans established since 1980.



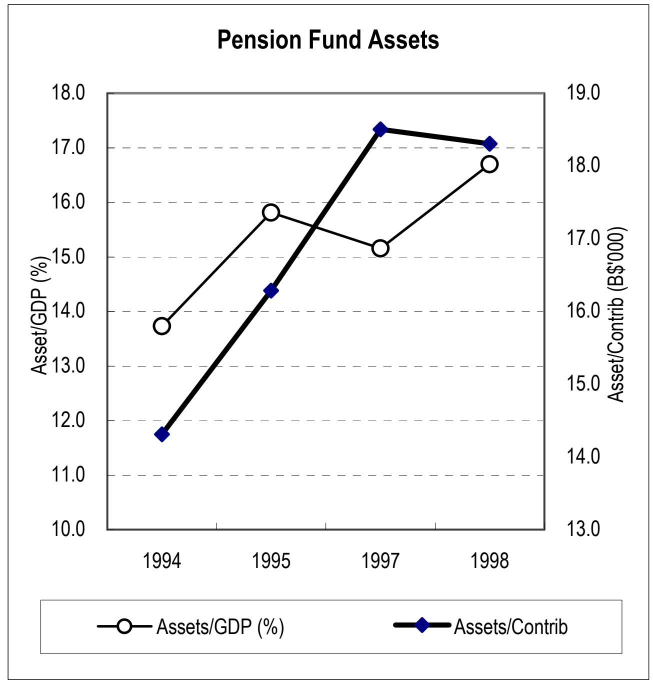
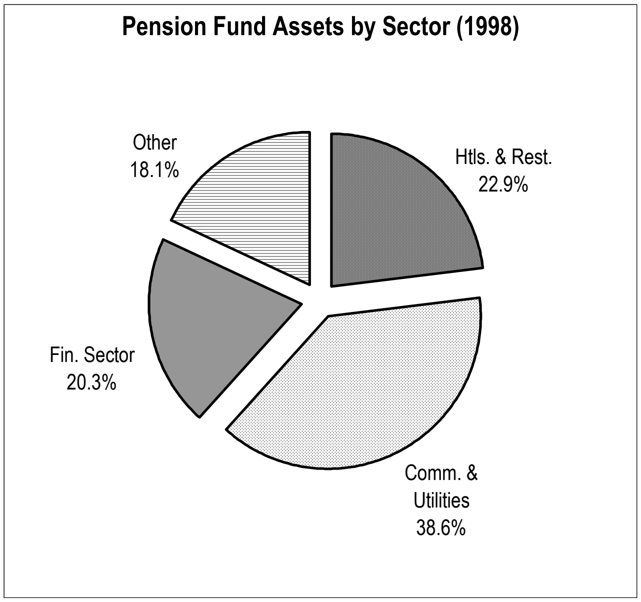


Table 1 shows that, as at end-1998, plans in the communications & utilities sector held the largest proportion of the asset base at $218.3 million (38.6%), despite accounting for only 12.3% of total participants. The next two largest shares were concentrated in the hotel & restaurants and financial sectors at $129.6 million (22.9%) and $114.7 million (20.3%), respectively. The remaining sectors, including manufacturing, transportation and distribution, combined for some 18.1% of total assets.

The portfolio distribution of pension assets for 1995 - 1998 is shown in Table 2. Of particular note is the steady increase in investment in Bahamas Government Registered Stocks (BGRS), bank deposits and equities, contrasting with reduced shares in mortgages and other investments vis-à-vis 1995 levels. In 1998, Government bonds represented the largest share of holdings at $188.3 million (33.3%), followed closely by bank deposits at $177.1 million (31.4%). The comparative 1995 shares were lower at 29.8% and 27.4%, respectively. While this distribution largely reflects the low risk and high liquidity features of these instruments, it is also indicative of the limited domestic investment opportunities. Nevertheless, local retirement schemes have approximately doubled their investments in private instruments (bonds, stocks and mutual funds, largely held outside The Bahamas by the external schemes) to $87.8 million (or a 15.5% share of the aggregate portfolio vis-à-vis 10.2% in 1995), while maintaining a low share of investments in employers' business at $4.5 million (0.8%). Conversely, the portfolio allocation for mortgages declined to $58.9 million (10.4%) in 1998 from $86.1 million (19.8%) in 1995.

As for the locational distribution of investments, some $504.8 million (89.4%) was invested inside The Bahamas, with $60.0 million (10.6%) held externally—inclusive of externally funded schemes. Of these external investments, approximately $24.6 million (41.0%) was held in equities, $12.6 million (21.0%) in government securities, $9.1 million (15.2%) in mutual funds, $7.5 million (12.4%) in bank deposits and $6.1 million (10.2%) in other investments.



The trend of diversifying assets mainly into bank deposits, government securities and equities is also apparent in the sectoral breakdown shown in Tables 3A and 3B. When compared to 1997, the communications & utilities sector recorded slightly expanded asset shares in both government securities (40.1%), bank deposits (27.9%) and equities (5.2%) at end-1998. Plans in the hotel & restaurants sector placed slightly less emphasis on government securities (26.6%), while increasing holdings in bank deposits (38.2%) and equities (23.4%). Meanwhile, financial sector schemes had reduced investment proportions in government bonds (35.5%), but a greater share of placements in deposits (32.7%) and a stable share allocated to equities (13.7%).

Among plan types, defined benefit plans showed stronger preference for government securities at 36.9% of the respective combined portfolio in 1998, versus a 17.0% share among defined contribution plans (Table 2). Similarly, defined benefit plans invested a comparatively larger share of average assets in mortgages and equities. Both of these configurations suggest a more aggressive investment strategy among defined benefit schemes. Nevertheless, both defined benefit and defined contribution plans accumulated significant resources in bank deposits (at 30.4% and 35.8%, respectively), albeit defined contribution schemes placed proportionately more of their assets in loans and other investments.

As regard average rates on pension fund assets, yields firmed slightly to 6.87% in 1998, remaining above the 6.71% averaged in 1995. In this regard, the defined benefit plans enjoyed higher yields than the other plans, estimated at 7.07% in 1998 versus an average of 6.78% among defined contribution plans. Both rates, however, were higher relative to the 1995 respective levels of 6.62% and 6.75%.

Conclusion and Outlook

As the economy continues to expand, both the level of labour force participation and the number of pension funds in existence are expected to grow at a healthy pace. This poses new questions about the safety of these resources and their impact on labour force mobility. To address these concerns the Government has already circulated a draft of the proposed Occupational Retirement Scheme Act, which will establish a registry for domestic pension funds under the supervision of the Registrar of Insurance Companies. The Bill provides for close supervision of pension fund management, with particular regard to their actuarial soundness, and it proposes to establish prudential guidelines for the investment of fund assets. Perhaps the most significant feature of the proposed legislation is the proposed transferability of vested interest between schemes as workers change jobs. Recognizing the important role that pension funds will play in a more active domestic capital market, such measures will strengthen the management infrastructure of pension funds, while maintaining confidence in the system and ensuring the efficient use of such resources for national development.