



Gross Economic Contribution of the Financial Sector in
The Bahamas (2008)

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GROSS ECONOMIC CONTRIBUTION OF THE FINANCIAL SECTOR IN THE BAHAMAS (2008)

INTRODUCTION

This report summarizes the results of the Central Bank's 2008 survey on the gross economic contribution of the financial sector to The Bahamas. Data on the banking sector's involvement in the economy have been collected from as early as 1977. Over the past eight years, the Bank has sought to expand its coverage to capture the contribution of other financial sector entities, including insurance companies, credit unions, mutual fund administrators and financial and corporate services providers.

Despite the adverse domestic and international developments, which particularly impacted The Bahamas' financial sector during the latter half of 2008, indications are that the sector, which accounts for at least 15% of the gross domestic product (GDP), recorded an increased contribution to the economy in 2008. Gains were noted in employment, and salaries and other expenditures, particularly within the banking sector. Less comprehensive data indicate that developments in several areas of the non-bank financial sector paralleled those among banks and trust companies, with increased value added observed, particularly among credit unions, insurance companies and providers of corporate and financial services (mainly international business companies (IBC) activities).

The bulk of the operating and investment expenditures collected in the survey impact the private sector, with some expenses reflecting payments to Government, mostly for licence and work permit fees, and import taxes. The Government also earns revenue from stamp taxes on financial transactions which, combined with licensing fees, decreased by 16.4% to \$111.1 million in 2008, mainly corresponding to a drop in the volume of transactions, particularly among domestic banks and insurance companies. The component of revenues derived from license fees was further augmented at a healthy pace of 25.1% to \$33.2 million, underpinned by the continued rebound in international business companies (IBCs) activities.

BANKING SECTOR

A PROFILE OF THE SECTOR

Banks and trust companies account for the largest portion of the financial sector's contribution to the economy, registering modest firming in employment and expenditure levels within both domestic and international operations during 2008. The number of institutions licensed to operate from or within The Bahamas increased by 26 to 271. This corresponded to a boost in the number of restricted licenses by 35 to 130, relative to reductions in non-active licensees to 10 from 12, and in public licenses—which provide the bulk of the employment—to 131 from 138. Of the total licensees, 20 institutions provided services to the domestic sector, inclusive of 8 commercial banks and 12 other local financial institutions—the latter with a focus primarily on trust operations.

During 2008, assets of international banks and trust companies advanced by 24.0% (\$97.4 billion) to an estimated \$503.0 billion. This corresponded to an observed international pattern benefitting Caribbean financial centres during 2008, as resources flowed out of the US credit markets.¹ However, indications are that the value of fiduciary assets under management (mainly offshore) contracted for the second consecutive year, owing to both a decline in deposits and lowered valuations on portfolios invested in capital market instruments.

On the domestic side, buoyed by increased lending to the private sector and augmented holdings of Government debt, total assets rose by \$697.5 million (8.3%) to \$9.1 billion, an incremental slowing from the advance of 8.9% in 2007. Institutions operated with a network of 110 branches, an increase of two since 2007. Due to higher expenditures—particularly bad debt provisions—domestic banks' net earnings contracted by 10.4% (\$32.1 million) to \$275.3 million, for a reduced 2.74% of average assets compared to 3.05% a year earlier.

¹ Source: Bank For International Settlements, Quarterly Review, June 2009.

Table A: Government Revenues from Financial Sector Activities (B\$ Million)

Period	2003	2004	2005	2006	2007	2008
A. Stamp Taxes on Transactions	51.6	43.8	66.4	78.9	108.3	84.3
Gross Insurance Premium Tax	10.9	7.9	18.1	22.0	18.2	21.3
Mortgages	5.9	6.9	12.2	16.3	42.4	21.3
Other Banking Transactions	34.7	28.9	36.0	40.3	47.5	41.6
Instruments & Bonds	0.1	0.1	0.1	0.1	0.2	0.2
B. Licence & Registration Fees	23.6	25.1	23.8	23.6	28.1	34.8
International Business Companies (IBCs)	15.0	15.7	14.7	13.5	15.2	21.3
Banks and Trust Companies	6.8	7.7	7.2	8.4	11.1	11.6
Insurance Companies, Brokers & Agents	0.2	0.1	0.4	0.3	0.2	0.3
Financial & Corp. Svcs. Providers <u>1/</u>	0.04	0.04	0.05	0.04	0.10	0.10
Investment Funds <u>2/</u>	1.5	1.6	1.4	1.4	1.5	1.5
C. Total Revenues	75.2	68.9	90.2	102.5	136.4	119.1

Sources: Bahamas Government's Treasury Department, Securities Commission of The Bahamas.

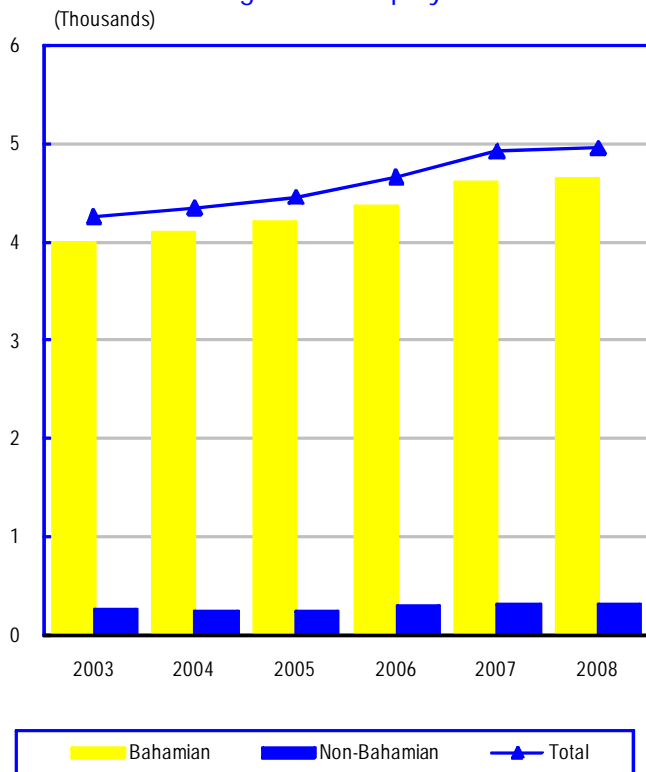
Notes: 1/ Central Bank Estimates for 2008.

2/ Amounts collected by the Securities Commission.

EMPLOYMENT

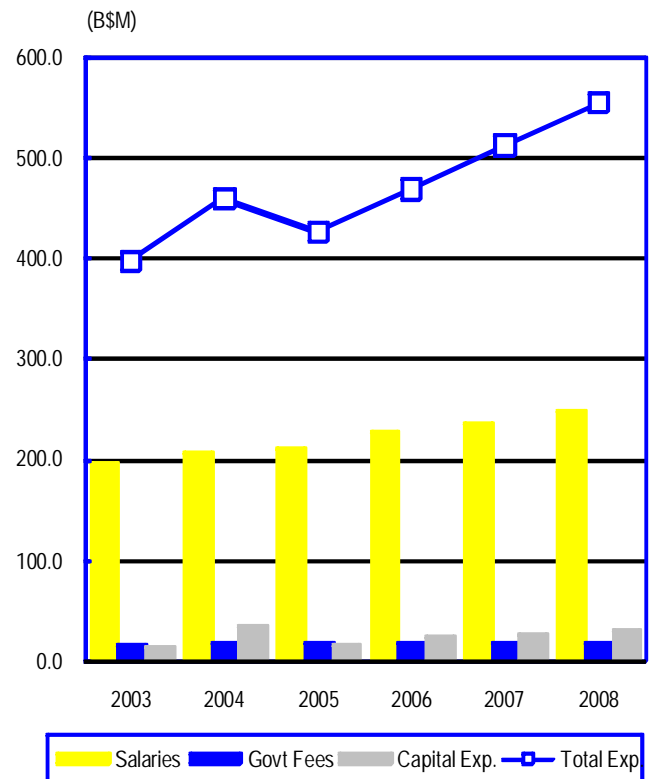
Preliminary estimates showed employment in the banking sector grew at a slowed pace of 0.6% (31) to 4,954 persons, compared to a gain of 5.6% (261 positions) in 2007. This corresponded to a 0.7% (31 positions) rise in the number of Bahamians employed to 4,637; albeit, lagging the previous year's 5.4% gain and the average yearly increase of 155 jobs (3.7%) over the adjoining five years. In contrast, the number of expatriate workers in the sector remained at 317, after a 7.8% hike in 2007. Given these developments, the respective shares of Bahamian and expatriate employees were unchanged, at 93.6% and 6.4% of the total workforce.

Banking Sector Employment



Operational costs, which comprised 94.2% of total expenditures, trended higher by 7.5% to \$521.0 million, ahead of the average yearly increase of 6.2% during the adjoining five years. Inclusive of bonuses, the dominant salaries component rose by 5.9% to \$286.5 million, moderately below 2007's gain of 6.3%.

Banks' Local Expenditure



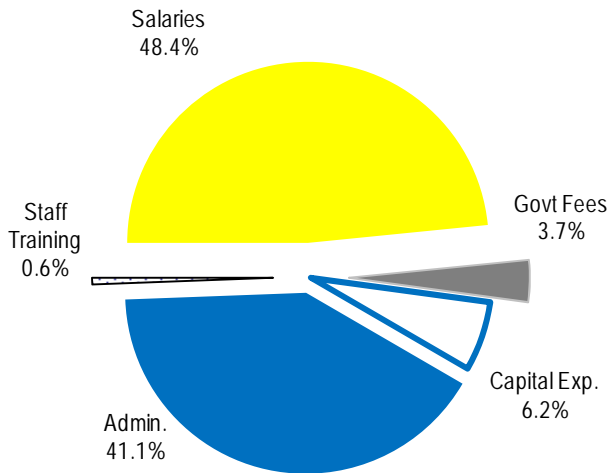
Adding bonuses, the average annual employee compensation advanced by 5.3% to \$57,839 in 2008, with a 6.2% increase in Bahamians' pay, contrasting with a 0.6% reduction for non-Bahamians. Excluding bonuses, the average base salary improved by 4.6% to \$50,488 per annum, extending the previous year's 0.7% rise and an average annual 1.1% increase observed from 2003 to 2007. The average base salary for expatriate workers, mainly in selected top level management positions, rose by 7.1% to \$115,591; and the corresponding estimate for Bahamians, by 4.2% to \$46,012. Conversely, direct spending on staff training narrowed by 3.2% to \$3.0 million, vis-à-vis an upturn of 11.2% in 2007.

EXPENDITURES

Higher salary payments, administrative costs and increased capital spending underpinned a rise in the banking sector's gross expenditures by 8.2% to \$553.1 million in 2008. This lagged the 9.2% increase registered in 2007, but was ahead of the 6.5% average growth between 2003 and 2007.

After a 3.5% uptrend in 2007, direct fees paid to Government rose further by 3.6% to \$19.3 million, attributable largely to increased outlays for customs duties, work permits and license fees. Other administrative costs rose by 10.2% to \$212.1 million, offsetting the 2.9% falloff in 2007.

Banks' Expenditure Components
(% of Total)



DOMESTIC VERSUS INTERNATIONAL BANKING

It is useful to separately analyse the expenditure trends and patterns of the domestic and the international banking and trust operations. Domestic operations provide more staff intensive, retail services, which account for the bulk of the incurred expenses; albeit, in most cases alongside significant international business. The international licensees specialize in more skills-intensive wealth management operations, providing private banking services for high net worth clients—in many instances depending on operational resources based outside The Bahamas.

Employment growth in both domestic and international operations slowed in 2008, a consequence of the softer business environment. Among domestic licensees, employment rose by 0.7% (25 persons) to 3,791 vis-à-vis a 5.9% rise in 2007. Similarly, jobs in the international sector grew by 0.5% (6 persons) to 1,163 at end-2008, after a stronger gain of 4.7% in 2007. As a result, domes-

tic banks' share of total sector employment steadied at 76.5%.

As to nationalities, net employment opportunities for Bahamians in local banks were tempered during 2008, to 29 positions (0.8%) compared to an annual average increase of 171 positions (4.9%) during the previous two years. Moreover, the foreign workforce fell for the first time in six years, by 4 persons (6.7%) to 56. Correspondingly, the ratio of Bahamians to non-Bahamians employed within local banks firmed to 66:1 from 61:1 a year ago. In the international sector, employment growth was registered for both Bahamians and expatriates, of 2 (0.2%) and 4 (1.6%), respectively; albeit, tempered from the respective increases of 31 (3.6%) and 21 (9.0%) in 2007. However, the ratio of Bahamians to non-Bahamian in international operations remained at 3.5:1.

During 2008, total expenditures for domestic banks advanced by 11.3% to \$342.7 million, led by gains in operating costs, of 10.2% to \$319.2 million, and salary expenses, of 9.0% to \$182.5 million. Partly driven by utilities expenses, administrative costs also rose by 13.3% to \$125.6 million; however, both Government fee payments and staff training costs decreased slightly. Local banks also recorded a 28.3% increase in capital outlays to \$23.5 million, extending last year's growth of 12.7% and the 11.5% average yearly increase over the five years through 2007. Included in this were higher renovation expenses and outlays for new buildings.

In the international sector, total spending strengthened by 3.9% (\$7.9 million) to \$210.4 million, as operational and capital costs firmed by 3.8% and 6.2% to \$201.9 million and \$8.5 million, respectively. At 51.5% of operational outlays, employee compensation grew by 1.7% to \$104.0 million; while Government fees moved higher by 7.4% (\$0.8 million) to \$10.2 million, inclusive of incrementally higher payments for licence and work permit fees. Under investments, increased outlays were registered for new premises and office equipment and furniture, which outweighed a reduction in renovation expenditures.

In a continuation of the 14.3% average annual increase of the preceding five years, capital outlays strengthened by 21.6% to \$32.1 million, exceeding the 3.4% advance noted in 2007. Of particular note were significantly increased investments on new premises (at \$9.1

TABLE C. GROSS ECONOMIC CONTRIBUTION OF BANKS AND TRUST COMPANIES

Period	2003p	2004p	2005p	2006p	2007p	2008p	2003p	2004p	2005p	2006p	2007p	2008p
	DOMESTIC						OFFSHORE					
A. TOTAL EMPLOYMENT	3,208	3,275	3,424	3,557	3,766	3,791	1,045	1,068	1,027	1,105	1,157	1,163
1. Non-Bahamians	43	45	49	58	60	56	222	206	192	236	257	261
2. Bahamians (of which:)	3,165	3,230	3,375	3,499	3,706	3,735	823	862	835	869	900	902
i) Local Banking	2,602	2,689	2,824	2,964	3,146	2,989	3	2	2	5	0	0
ii) Offshore Banking	101	151	85	79	83	115	483	521	531	548	569	566
iii) Trust Administration	291	243	267	287	293	293	164	150	188	207	207	206
iv) Other	171	147	199	169	184	338	173	189	114	109	124	130
	DOMESTIC						OFFSHORE					
	(B\$ Millions)											
B. TOTAL OPERATIONAL COSTS	225.4	260.8	253.7	274.6	289.6	319.2	156.0	163.8	154.6	168.0	194.4	201.9
(1+2+3+4)												
1. Salaries ¹⁾	129.5	133.7	142.5	150.0	167.4	182.5	66.4	74.2	68.6	73.5	102.3	104.0
2. Government Fees	6.7	7.6	8.8	8.8	9.3	9.2	9.7	11.3	9.2	9.2	9.4	10.2
i) Licence	2.8	2.9	4.9	4.4	5.1	5.1	3.9	4.1	4.7	4.0	4.6	4.7
ii) Company Registration	0.7	0.7	0.7	0.7	0.9	0.7	0.7	0.7	1.2	1.8	1.5	1.2
iii) Work Permits	0.5	0.6	0.6	0.6	0.6	0.4	1.8	1.8	1.8	2.1	2.1	2.3
iv) Other Government Fees	2.7	3.4	2.6	3.1	2.8	2.9	3.4	4.7	1.5	1.4	1.2	1.9
3. Staff Training	1.3	1.3	1.5	1.5	2.1	1.9	1.1	1.1	1.2	1.4	1.0	1.1
4. Other Administrative Costs	87.9	118.2	100.9	114.3	110.8	125.6	78.9	77.2	75.5	83.9	81.7	86.5
C. CAPITAL EXPENDITURE²⁾	11.9	28.0	12.5	16.3	18.3	23.5	3.6	6.7	5.1	9.2	8.0	8.5
D. TOTAL EXPENDITURE (B+C)	237.2	288.9	266.2	290.9	308.0	342.7	159.6	170.5	159.7	177.2	202.5	210.4
E. AVERAGE SALARY (B\$/000)³⁾	40,352	40,838	41,618	42,172	41,559	43,125	63,512	69,434	66,838	66,472	70,031	74,488

Source: The Central Bank of The Bahamas

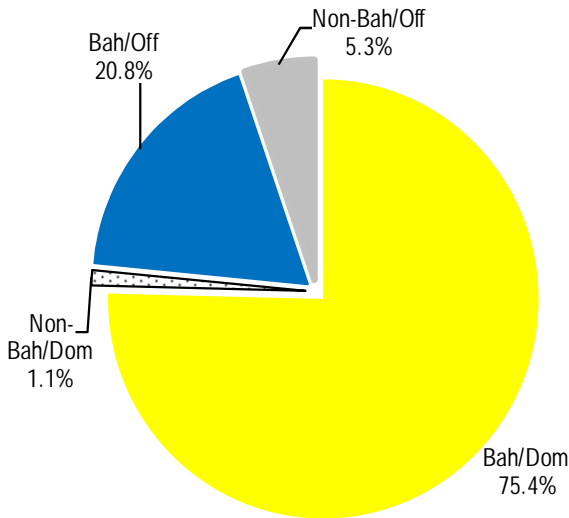
¹⁾ Includes bonuses

²⁾ Includes construction, renovation expenses and other fixed assets.

³⁾ Excludes bonuses

million), led by expansion in domestic banks' branch networks and marginally higher spending on office equipment and furniture, of 1.7% to \$15.1 million. Together, these outweighed a reduction in renovation expenditures, by 1.1% to \$6.8 million, and investments in land and other fixed assets, by a combined 11.6% to \$6.1 million.

Employment: Domestic & Int'l Banks (2008)



Compensation differentials favour jobs in the international sector, which require a greater concentration of specialized skills relative to the domestic banking operations. However, larger bonus increases in domestic operations narrowed the total average annual compensation relative to offshore banks, by an estimated \$2,684. Notably, the 8.3% rise in domestic banks' average pay to \$48,140 outpaced the 1.3% advance in the average total pay within international banks to \$89,424. Conversely, average base salaries, excluding bonuses, rose faster in the international sector, by 6.4% to \$74,488 per annum, compared to an increase of 3.8% to \$43,125 per annum within domestic operations.

OTHER FINANCIAL SECTOR ACTIVITIES

Indications are that the economic contribution from non-bank financial sector activities also registered gains during 2008, despite the deterioration in economic conditions in the latter half of the year.

INSURANCE SECTOR

Based on data from the Office of the Registrar of Insurance Companies, the number of licensed operations rose by 5 to 168 in 2008, after a significant consolidation in 2007. In particular, the number of domestic insurance companies remained at 54, while local brokers and agents increased by 3 to 83 and external insurers, by 1 to 20. Although comprehensive estimates were not available, indications are that the domestic sector's operational expenditures rose at a more tempered pace during 2008, supporting total employment in excess of 1,500 persons. Bahamians continued to occupy the majority of positions (98.3%), with non-Bahamians assuming a small number of highly specialized, technical and managerial posts. The domestic sector also experienced some boost in capital spending, related to the expansion of premises and purchase of office equipment. Meanwhile, average compensation for full-time employees in the insurance sector, at nearly \$45,000 per annum, remained competitive against those in domestic banks.

Data from the Government's finance statistics revealed that, although insurance companies and brokers directly paid total licence fees of under \$1.0 million in 2008, their underwriting activities generated an estimated \$11.5 million in gross premium taxes, compared to \$9.1 million in 2007. The mortgage lending operations of domestic insurers also generate stamp revenues; however, the share in the total is not expected to differ significantly from the sector's overall participation in mortgage lending, estimated at 6.2% of the market in 2008.

CREDIT UNIONS

As credit unions continued to expand their customer base, estimated assets rose by 3.0% to \$244.6 million in 2008; albeit, slowed from an increase of 9.9% in 2007. Total expenditures for the year firmed by an estimated 4.8% to \$6.9 million, supported by a 16.0% hike in administrative outlays to \$3.0 million. Marginal increases were noted for staff training and utilities expenses, while employee compensation and Government fees were unchanged at \$2.8 million and \$0.1 million, respectively. The estimated capital expenditures of credit unions were slightly reduced to \$0.3 million in 2008.

Although the number of persons employed by credit unions declined by 2 to 108 in 2008, staffing has remained relatively stable over the last five years. Given

Table D: Other Selected Financial Sector Statistics

	Unit	2004	2005r	2006p	2007p	2008p
Investment Funds Administrations						
Licensed Mutual Funds	Number	838	699	723	782	867
Licensed Administrators						
Asset Under Management	Number B\$ Billions	59 163.4	59 175.2	61 204.7	65 297.6	66 n/a
Insurance Companies and Agents						
Domestic Companies and Agents	Number	191	190	205	163	168
Total Domestic Assets	Number B\$ Millions	152 986.59	155 1,234.64	169 1,374.97	144 n/a	148 n/a
Average Annual Salaries	B\$	42,120	44,024	44,425	45,225	45,007
Operating Costs / Total Expenditures	%	94.6	91.9	94.8	94.1	94.9
External Insurers						
	Number	39	35	36	19	20
Credit Unions						
Number of Unions	Number	19	17	16	18	20
Total Assets	B\$ Million	170.2	190.4	216.1	237.4	244.6
Employment	Number	105	105	106	110	108
Average Annual Salaries	B\$	27,602	28,293	28,594	26,555	26,880
Total Expenditures	B\$ Million	7.99	6.87	6.18	6.61	6.93
Operating Costs / Total Expenditures	%	72.9	81.7	89.5	92.8	95.0
Bahamas International Securities Exchange (BISX)						
Securities Listed	Number	19	19	19	19	23
Shares Traded	Thousands	7,996	6,724	5,251	4,770	4,623
Market Capitalization	B\$ Billion	1.90	2.60	3.20	3.98	3.03

Sources:

The Central Bank of The Bahamas, Bahamas International Securities Exchange (BISX),
The Securities Commission of The Bahamas and The Registrar of Insurance Companies.

the part-time nature of some engagements, despite being competitive with jobs in the rest of the domestic financial sector, the average earned compensation stood at \$26,880 in 2008, advancing by 1.2% since 2007.

INVESTMENT FUNDS INDUSTRY

Data from the Securities Commission indicated that the number of active investment funds registered in The Bahamas rose by 85 (10.9%) to 867 in 2008. Data was not available on the net asset value of funds, which stood at \$298 billion in 2007; albeit, the increase in the number of funds is expected to have countered some of the valuation declines in the existing portfolios that were impacted by the global financial crisis. During 2008, the number of investment fund administrators, the direct sources of employment within the sector, increased by 1 to 66. Administrators collectively managed the assets of 800 registered funds, an increase of 42 since 2007. Given these trends, it is expected that employment conditions stabilized during 2008, with average salaries remaining competitive against those in the international banking sector.

INTERNATIONAL BUSINESS COMPANIES (IBCs)

The incorporation and management of IBCs generate revenue and support employment within the banking sector and among financial and corporate services providers (FCSPs)—mainly legal and accounting firms. IBC activities increased for the second consecutive year, with the revenues collected by government firms by 40.1% to \$21.3 million in 2008, following an increase of 12.1% in 2007 and a downturn over both 2005 and 2006. Trends included both registration of new companies and the resumption of fee payments by some previously inactive registrants. Based on these trends, it is estimated that the number of active, fee paying IBCs rose further, to more than 50,000 in 2008. The projected private sector benefits from incorporation and company maintenance services surpassed \$50.0 million, from an estimated \$42.3 million in 2007.

CAPITAL MARKET DEVELOPMENTS

During the year, the deterioration in the economy and depressed investor confidence led to a sharp downturn in the domestic equity market, with contractions in both share valuations and trading volumes. Developments were highlighted by a 17.2% depreciation in the Bahamas International Securities Exchange's (BISX) All

Share Price Index, compared to a 23.3% gain in 2007. Similarly, the total market capitalization of the companies listed on the Exchange fell by 23.9% to \$3.0 billion. The Fidelity Capital Market Limited's Findex—which includes over the counter trading—declined by 11.0% to 834.8 points, following a 26.4% advance in 2007. On an adjusted basis, net of a significant ownership shift, the value of the shares traded on BISX fell by 3.1% to 4.6 million; however, the total cost of the securities exchanged rose by 11.7% to \$31.6 million.

During the year four (4) new tranches of medium term debt and one (1) preference share issue were listed on the BISX, bringing the number of publicly traded securities to 24, including 19 companies.

CONCLUSION AND OUTLOOK

Results from the above analysis suggest that the Bahamian financial services sector remained resilient during 2008, in the face of the global economic downturn and turbulent financial markets developments. Notwithstanding, as the adjustments to these events set in, the pace at which business opportunities expand in the short-to-medium term could slow. Neither the domestic nor the international sectors experienced any destabilising effects from the 2008 upheaval. However, the impact on the local economy continues to accumulate, owing to real sector adjustments in tourism and foreign investments, which have adversely affected balance sheet growth and led to escalated credit risks among economically affected households. Greater attention to risk mitigation rather than business growth is therefore expected to weigh more heavily on domestic banks' short-term strategies. Medium-term adjustments are also anticipated in the international sector, as licensees adopt a more cautious approach to operational initiatives amid developing countries' ongoing determination of regulatory responses to the global financial challenges.

The Bahamas' policy response is expected to feature expanded international cooperation, through tax information exchange agreements (TIEAs) and other information sharing arrangements with countries other than the United States. Enhanced supervisory and regulatory efforts will be maintained to preserve the ongoing stability of both the domestic and international sectors, inclusive of imminent enabling legislation that would strengthen the oversight of the insurance sector.