



## **“A Bahamas Future Built on Central Banking?”**

**Speech by**

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**(As prepared for delivery)**

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### **1 Introduction**

I want to start by first thanking the Counsellors Limited for the invitation to speak here today.

The Business Outlook has become a staple in The Bahamas, as a forum for intelligent discourse on important economic and development matters. Both private and public stakeholders value this opportunity for engagement, as it sets the tone for rest of the year.

Before I get into my presentation, I should mention that the Central Bank is celebrating its Golden Jubilee this year, marking 50 years of service to an independent Commonwealth. I am excited about all that the Bank has planned for the commemorations and I trust that you will celebrate and deliberate with us—when the opportunities arise— as we reflect on the past five decades and make our intentions clear on what we would like to see in the decades to come.

Turning to the topic at hand, the Central Bank certainly has a role to play in supporting economic growth and stability, both now and in the future. My presentation will focus on the

Bank's role and functions, as well as how it has evolved over time to meet the demands of a maturing small open economy. It will also highlight some critical aspects of how this contribution can be shaped for the future. Part of that journey, while recognizing the constraint of operating in a small open economy, will involve continuing to strike a balance in our approach to monetary and financial sector policies, between a diminished reliance on administrative tools and allowing for increased market driven outcomes.

## 2 Evolving to Our Present State of Central Banking in The Bahamas

Although the Bahamian experience with Central Banking is more modern, it encapsulates centuries of evolution around how such institutional arrangements should be structured; and many of the stern, frequently unpleasant lessons around financial sector turbulence, and international economic relations--especially of the 20th Century and early 21st Century. The Central Bank of The Bahamas was established in 1974, with core mandates that can be conveniently condensed into three areas

- i. First, responsibility for monetary policy, geared towards preserving the exchange rate peg.
- ii. Second, through supervision and regulation, ensuring the stability and orderly functioning of the domestic banking system (and credit unions)—and ensuring the stable, reputable conduct of international banking and trust services.
- iii. Third, ensuring the efficient and orderly functioning of the domestic payments system, which covers the Bank's responsibility as sole issuer of currency, and facilitator of the clearance of payments among banks and other supervised entities.

While the Bank does not have any explicit economic growth mandate or target, through successfully carrying out its core objectives, it lays a vital foundation to support growth.<sup>1</sup>

When the Central Bank was established, The Bahamas already operated a fixed exchange rate system, which had existed prior to, and even after the dissolution of the UK's Sterling Area to which the islands belonged as a colony. The exchange control regulations which the Bank took over, encapsulated controls on both long- and short-term capital transactions; and payments for imports of goods and services. Capital controls also became embedded into how we viewed and administered our national investment policy.

Coming out of the inflation experiences of the 1970s and 1980, and the banking and financial crises, up to the mid-2000s, central banking emphasis round the world shifted broadly away from targeting the exchange rate to targeting inflation as a better anchor for monetary policy; and the emphasis on financial stability was further heightened. While central banks use interest rates as a signal and key tool to manage such outcomes; with the financial stability mandate they also target areas such as variability in the access to credit--both in terms of the lending supply capacity within financial institutions and qualification standards applicable to borrowers. In this context, the relatable policy variables in The Bahamas include the personal debt-service burden and equity requirements for loans. In other financial systems the prudential authorities also increase or decrease the capital and liquidity requirements for

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<sup>1</sup> This is encapsulated in the Bank's mission statement, which is "to foster an environment of monetary stability conducive to economic development and to ensure a sound and stable financial system."

banks, as the stability risks from lending rise or fall. On a structural basis, The Bahamas also has examples of the progressive longer-term reforms to improve the credit environment and financial stability constructs, namely: the credit bureau, deposit insurance, and over the medium term the collateral assets registry is forthcoming.

If one observes the current posture of monetary policy globally today, it should be clear too, that over a short or medium term perspective, central banks are often prepared to sacrifice growth in order to keep inflation under control. But inflation targeting still has an objective of supporting better longer-term growth potential, as both price stability and financial stability have positive impacts on the savings and investment decisions that affect potential growth.

What is the equivalent for The Bahamas? We maintain a fixed exchange rate. Being successful, in this regard means that we have to preserve credibility around the adequacy of foreign reserves that protect the peg. Moreover, the stability of the exchange rate allows The Bahamas to import the low inflation rate success of the US, our main trading partner. This also influences the attractiveness of the country to foreign direct investment, as investors care about avoiding exchange rate losses; and they care about the safety of lending to the our country in foreign currency. The in depth dialogue that the Central Bank of The Bahamas regularly has with potential investors to The Bahamas, is commonly about how, especially around reforms to exchange controls, the security of the peg is being preserved.

In the space of regulations and banking supervision, keeping pace with evolving international standards has also guided the Central Bank's economic contribution. For The Bahamas, this has been about remaining a transparent player in the global arena, while ensuring that the application of standards continued to secure a contribution of international financial services to the economy; and that domestic commerce was not cutoff from access to international payments. Nevertheless, the progress achieved particularly in terms of international tax transparency is still having a consolidating impact on our international banking sector. There are promising signs of growth in Latin American markets, but this is still overshadowed by downside effect of business that is returning to Europe. To a significant extent, The Bahamas has also experienced some strains on the ease of banking from our AML risk management frameworks; although recently there have very notable strides made to simplify the due diligence requirements for low-risk users of banking and payment services.

### 3 Towards a Future of Central Banking in The Bahamas

As we look to how central banking could evolve in tailored ways for The Bahamas, a starting point would be to consider how the various mandates of the Central Bank support economic growth, and how the mandates could motivate policies to raise potential growth; and better situate The Bahamas to adapt and become more resilient in the face of climate change risks. While maintaining monetary and financial stability are still the top priorities, some of the very important future emphasis that I would like to highlight embrace inclusive and accelerated digital transformation in domestic financial services; becoming more attuned to climate change risks; confronting issues that impact banking sector competition and efficiency; and keeping exchange control administration continuously in the mix.

### 3.1 Payments System Modernisation

Continued and accelerated modernisation of payments—with an emphasis on digitisation—is about making the economy more efficient, and making access to financial services more inclusive; as well as about boosting resiliency in the face of more frequent and more destructive hurricanes. In this regard, the Central Bank’s Payments System Modernization Initiative (PSMI) began in the early 2000s, addressing upgrade of the clearing processes for wholesale (RTGS) and retail payments (ACH). Now the emphasis is to continue to develop and increase adoption of our digital currency (CBDC), the “SandDollar”.

Today, 11 CBDCs have been launched, including two in the Caribbean, with 21 other pilots ongoing, and an additional 33 said to still be in the development phase. According to the Atlantic Council<sup>2</sup>, there are over 130 countries which represent 98% of global GDP exploring a CBDC, with 19 of the G20 countries in the advanced stage of such developments.

Work is also underway to improve the general payments infrastructure and progress The Bahamas to a fast payments system. It is not a quest to eliminate cash—but to reduce dependence on the instrument and gradually phase out physical cheques. Fast payment systems are gaining traction as alternatives to credit and debit card transactions, as they allow for real time settlement of transactions between users. According to the World Bank, such systems are being explored in six of the seven continents. This represents more than 70 countries worldwide across a mix of advanced, emerging market, and developing countries.

While our local initiatives have been focused on domestic payments at the outset, we are also preparing for the coordinated global push to improve cross-border infrastructures, which will help to decrease the time associated with clearing international transactions and assist with reducing transaction costs for such transfers. In fact by 2027, the G20 has set ambitious target for the cross-border retail payments, which would deliver on such benefits. The outcomes only be realized on the same scale for The Bahamas, if there is a significant improvement in the access to and speed of local retail payments; and if the retail payments in general look more like fast payments.

### 3.2 Addressing Climate Change Risk and Green Finance

The second work stream that I would like to highlight, which has been garnering global interest and effort is addressing climate change risk and green finance. While there is an element of ensuring that there is transparency around how the supply of green financing is incentivized, accessed, as well as disclosed; the Bahamian domestic interest would also centre around ensuring that capital or exchange control policies support private sector access to green finance.

Managing climate change risks also matters for the prudential safety and soundness of the Bahamian financial system. In this respect, the Central Bank’s work plan is to improve its stress-testing frameworks, which measure the exposure of domestic banks to climate change and, where necessary, tweak regulations to better ensure that risk are adequately managed.

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<sup>2</sup>Atlantic Council - <https://www.atlanticcouncil.org/cbdctracker/>

Our stress testing models already assume that severe changes in non-performing loans (NPLs) could correlate with very destructive hurricanes. Now, the granularity in this type of analysis is expected improve, with more tailored institution level understanding of exposure risks, and consequently more tailored regulatory oversight on a lender by lender basis, if necessary.

The financial stability risks from climate change also pose looming concerns about private sector under-insurance against hurricanes. This risk management gap, is expect to gain broader national attention, once the Bahamian domestic Financial Stability Council is convened later this year. In particular, The Bahamas' needs outcomes that reduce the private sector's recovery dependence on government assistance; and outcomes that increase the public sector's capacity to restore public infrastructure following major setbacks.

### 3.3 Regulatory Sandboxes

The third innovation I want to highlight is adopting the use of regulatory Sandboxes. The Central Bank is exploring how such frameworks could support the introduction of nascent financial technologies. This is important in the context of how to enable faster access to digital payments platforms; as well as to how The Bahamas ultimately enables, regulated, but more open access to digital banking platforms. The regulatory sandbox can be an effective supervisory tool to allow firms to foster product innovations, in the market place, with the right safeguards in place. The Central Bank is exploring the use of this instrument to establish the legislative and policy conditions, application requirements, and bespoke supervisory provisions under which participating stakeholders could introduce innovations to consumers. We are targeting some initial constructs for sandboxes before the end of 2024.

### 3.4 Additional Considerations for The Bahamas' Central Bank

Before I conclude I want to touch on two additional work stream considerations for the Central Bank of The Bahamas. These are competition in banking, and exchange controls— issues that receive much attention and often times contention.

On financial sector competition, it is important to recognize that the domestic financial market space is still very small. Efficiency concerns will not be resolved by simply increasing the number of banking players or other providers. Rather, we expect that more aspects of services delivery would be addressed, including quality, efficiency and cost, as The Bahamas moves towards an internationally benchmarked consumer financial protection regime. This is a current focus of the Central Bank. In addition, we foresee that additional investments would be needed in the payments space to lower access costs; and that agency banking or similar services could be a route to more efficiently extend the reach of services to all communities. The Central Bank along with financial services providers are also vested stakeholders in strengthening the quality and reach of telecommunications infrastructure, so that digital services delivery is inclusive for all communities of The Bahamas.

### 3.5 Exchange Controls

Finally on exchange controls, the Central Bank expects to continue to push for reforms that improve the benefits that the economy receives on capital transactions; keeping the process sustainable and not undermining our ability to maintain the fixed exchange rate system. Administratively, it is about continuing to streamline how both domestic and foreign individuals receive approvals, where necessary; and continuing to afford commercial banks

more delegated authority to approve forex transactions, without recourse to the Central Bank. We are also continuing to look for simplification that would speed up how commercial banks onboard foreign investor enterprises for deposit accounts.

While it is underappreciated, the average member of the public, even small businesses, have virtually no need to interact with the Central Bank to conduct forex transactions. In addition, most residential real estate transactions, no longer experience exchange control friction during the conveyance process; and establishing Bahamian dollar deposits accounts to meet local property maintenance expenses is, in most cases, unhindered by the need for any exchange control approvals. On a forward looking basis, the Central Bank will continue to streamline the ease at which investment transactions are processed for exchange control purposes, and minimise the duplication of efforts, that could arise when The Bahamas Investment Authority is the principal approving authority.

#### 4 Concluding Remarks

To conclude, the Central Bank's practice is to ensure that there is an innovative approach to policy and regulations that support The Bahamas' medium and long-term growth interests. This includes keeping pace with the global regulatory requirements that affect the ease of doing business and international sector, while supporting domestic financial stability in its multifaceted dimensions. At the same time, the Bank will continue to provide the monetary policy oversight needed to help deliver on the credibility of the fixed exchange rate system. There is also a strong imperative to strengthen resiliency and risk management frameworks for climate change. In this regard, it must be recognized that resilience is also impacted by how inclusivity ties in with more digital supply of financial services. In the meantime, greater efficiency in financial services, also of necessity, depends on how we continue to improve the public infrastructure, through which services are provided, including for payments.

Although I have not stressed it, this is a collaborative and consultative process, with the government, industry and all users of financial services as the vested stakeholders.