



**Monetary and Financial Sector Policies: Strengthening the Medium-Term
Prospects**

by

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**Opening Remarks:
Bahamas Economic Outlook**

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Introduction

It is a pleasure for me to bring remarks to this third Economic Outlook conference, organized by Royal Fidelity. The perspectives that this event provides, remind us that our economy is globally connected, and that the progress that we achieve is driven by how we position domestic policies to take advantage of global opportunities. In this regard, I would like to like to speak briefly to the monetary and financial sector as regard both near-term prospects and key reforms that can benefit the economy over the medium-term.

A major challenge for our country is achieving stronger growth. Underperformance is a critical factor constraining the sovereign credit rating of The Bahamas. It is a structural challenge that can be surmounted most, through planning and execution, such as has been proposed in the National Development Plan.

Monetary Policy and Exchange Control

The Central Bank's statutory role is to ensure that enabling conditions exist within the financial sector to favour economic growth and development. It is closely tied to upholding the stability of our currency.

Having exchange controls supports this framework. Provided that the rest of our monetary policies are consistent, the controls help to insulate the economy against foreign exchange shortages that would force the exchange rate peg to be abandoned. The framework also allows the Central Bank to manage the adequacy of the stock of foreign reserves, which by law can never fall below 50 percent of the value of currency liabilities of the Central Bank¹.

The focus of monetary policy in this setting is to manage any added demand for imports and the use of foreign exchange which arise from the lending activities of commercial banks.

Currently the outlook for The Bahamas is for improved economic performance over this year and the medium-term. Included in this is essential expansion in foreign exchange earnings capacity in

¹ These so called "demand liabilities" of the Central Bank include the stock of Bahamian dollar currency issued by the Central Bank, plus deposits placed at the Central Bank by commercial banks and the public sector which can be withdrawn and converted to cash.

the tourism sector; prospects for tourism growth tied to US markets in particular, and discounted oil prices from the relative highs of the last half decade. These all point to the prospects for stronger net foreign exchange inflows.

This is why the Central Bank undertook to lower interest rates at the close of 2016. The economy has the capacity for a gradual increase in domestic demand which can be accommodated without a drawdown in external reserves. Indeed the outlook remains stable to incrementally firm for external reserves in 2017, with conditions healthier in 2018, once the full operational impact of Baha Mar starts to take hold.

It is the risk of depletion or inadequacy of foreign reserves that would stir concerns--including fears of devaluation. At the end of 2016, the reserves stood at \$902 million, equivalent to about 3 months of imports and to about 70% of the currency or potential currency liabilities of the Central Bank. This stock is literally the residual of the more than \$5 billion in foreign exchange that flow through the domestic Banking system each year,² with roughly the same amounts flowing out to pay for imports or investments made abroad.

Over the medium-term the Central Bank would like to see the external reserve ratios improve, fuelled by strengthening economic growth, either in the foreign exchange earning sectors or in activities that help the economy conserve better on the use of foreign exchange. This brings some of the present exchange control reform proposals into focus. These will consider increased access to foreign currency credit financing for local firms in targeted sectors that would strengthen the net foreign exchange earnings potential of The Bahamas. The Government will receive these proposals for consideration in February.

Public Debt Governance

Another focus which revised Central Bank legislation will tackle is strengthening the governance around the Bank's lending to government. This and other modernisation reform have already

² An even larger quantity of foreign currency denominated transactions flows through the GDP accounts and are captured in the balance of payments statistics. These represent payments made outside The Bahamas either for investment ownership changes between non-residents or for investment goods imported into The Bahamas. Also, some foreign exchange circulates within the economy and pays for imports but never passes through commercial banks.

been endorsed by the Bank and the Government, in a framework that we anticipate will be open to public consultation later this year. It will complement work already begun to introduce a market based framework for pricing new debt, and provide more flexible tools to manage bank liquidity.

Safeguarding financial sector stability and preserving confidence in banks also serve the interest of the economy.

Credit Quality and Market Reforms

Our domestic banks are well capitalized by international standards, which is key to both stability and confidence. Most of the threat to their capital erosion since 2008 has been from the accumulation of non-performing loans (NPLs) that ate into interest earnings potential and forced them to make significant write-offs. NPLs are now decreasing, under improving economic conditions that are putting more delinquent borrowers in position to service their loans. Banks have also restructured significant credit, particularly mortgages, to make them more affordable and they have identified several hundred households who qualify for assistance under the Government's mortgage relief program. There has also been almost \$130 million in non-performing residential mortgages sold to other private sector firms that are similarly restructuring or resolving the facilities.

At the end of 2016 the NPL rate had therefore fallen to 12.3% of private sector loans, compared to 15.1% at the end of 2015 and a peak of above 16% in mid-2014.

A key reform that would promote healthier credit markets in the medium and longer-term is the passage of the already drafted credit bureau legislation. It is expected to be considered soon, after Parliament takes up the mortgage relief or Home Owners Protection Bill.

Financial Inclusion and Payments System Modernisation

The Central Bank is also formulating reforms which would promote financial inclusion and reach deeper into the consumer segment of the banking system. Such initiatives would also be positioned to support improvement to the anti-money laundering (AML) profile of The

Bahamas, and help to reduce risks of compromised access to correspondent banking networks that facilitate vital international payments.

The strategy involves promoting a sustained reduction in the use of cash in local transactions over the medium-term, and increasing the ease of access of all persons to accounts in the banking system. Regulations will soon be issued to facilitate licensing of non-bank providers of e-payments solutions, with enhancements following that would position the local economy to adopt or participate more broadly in FinTech solutions.

These initiatives will also bring public education and non-price based regulations which promote consumer protection more to the forefront.

Other Strategic Focuses

Ladies and gentlemen, the Central Bank has just mapped out a new Strategic Plan that will guide our work through 2020. It touches on matters such as I have just mentioned, more generally on areas where our interventions could have positive structural impact; and on how the Bank can help support overall improvements in the business environment.

The Bank also intends to promote more informed and constructive dialogue on monetary and financial sector policies. These must be couched within a deeper appreciation of how the sustainability of our exchange rate regime is preserved. Such dialogue, I am aware, will also touch on whether we can effect stable changes to our regime.

Conclusion

Again, it is commendable that Fidelity and its partners have assembled this panel of experts to discuss the economic outlook, and particularly its international dimensions. While The Bahamas is on the receiving end of many of these developments, reforms continue to be within our reach to capitalize further on the opportunities that are presenting themselves.

I trust that today's presentations, and the discussions around them will sharpen the focus on these issues. The Central Bank stands ready to be more engaged with the public on these matters and we look forward to doing so in our various communications, publications and forums.