



## Gross Economic Contribution of the Financial Sector in The Bahamas (2006)

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## GROSS ECONOMIC CONTRIBUTION OF THE FINANCIAL SECTOR IN THE BAHAMAS (2006)

### INTRODUCTION

The Central Bank has compiled annual data on the gross economic contribution of the financial sector to the Bahamian economy, dating back to 1973. The current exercise focuses primarily on an analysis of the licensing, employment and expenditure trends of banks and trust companies operating in The Bahamas and summarises important developments in the insurance sector, investment funds industry and capital markets over the review period. To provide a more comprehensive sectoral assessment, efforts are ongoing to obtain greater specificity with respect to the contribution of corporate and financial service providers.

As the second pillar of the Bahamian economy, the financial sector contributes, on average, an estimated 15%-20% of the Gross Domestic Product (GDP). A combination of factors continue to support The Bahamas' success in financial services, principal among which are the diverse pool of skilled professionals, a commitment to remain up-to-date in the provision of financial products, and strong emphasis on ensuing compliance with international standards and regulations. Traditionally, banking and trust activities account for the largest share of the sector, with domestic banks offering retail banking services, and international institutions specializing primarily in wealth and portfolio management.

### BANKING SECTOR

The 2006 survey data indicates that the financial sector continued to contribute positively to the growth of the Bahamian economy, as evidenced by sustained improvements in employment, salaries and capital investments by banks and trust companies.

During the year, the total number of banks and trust companies licensed to operate from or within The Bahamas declined by 2 to 248 compared to the previous year, with public bank and trust licensees reduced by 6 to 143, while restricted and non-active licenses increased by 4 to 105. Public institutions included 90 Bahamian incorporated entities, 31 euro currency branches of foreign banks and trust companies, and 22 domestic banks. Of the

latter, 9 were Authorized Agents and Dealers (commercial banks), and 13 Authorized Agents, which primarily provide trust and wealth management services. The number of entities licensed to operate under the Central Bank's physical presence policy rose by 2 to 215, while the remaining 33 licenses functioned under restrictive management agreements with the approval of the Central Bank.

Preliminary data for the first nine months of 2006 on the asset base of international banks and trust companies indicated an improvement of \$35.6 billion (11.7%) to \$339.4 billion at end-September 2006. Total assets of the domestic banks expanded by 12.1% to \$7.8 billion; and profits were up by 27.9% to \$300.8 million. Consequently, the sector experienced an improvement in its average return on assets ratio, from 3.57% in 2005 to an estimated 4.02% in 2006.

### EMPLOYMENT

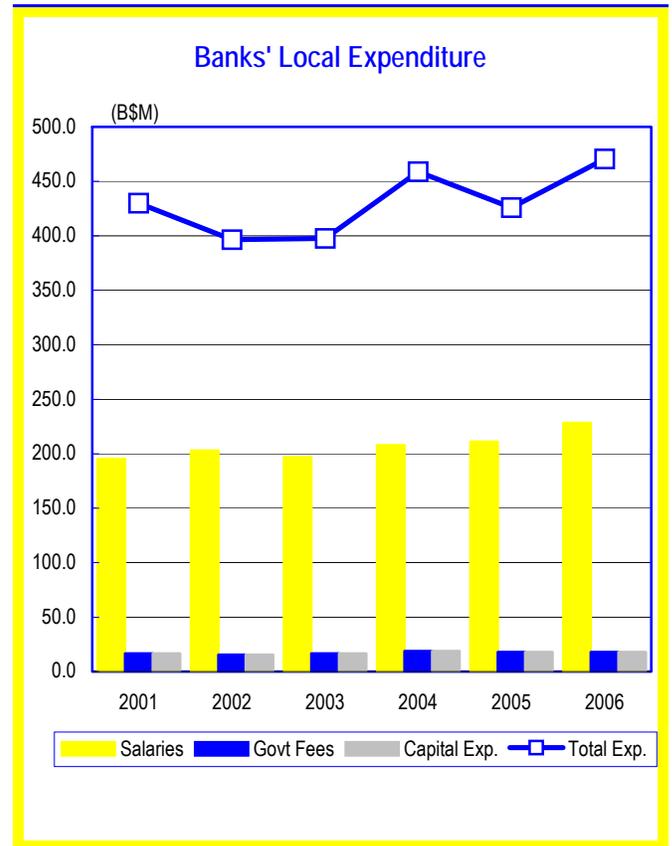
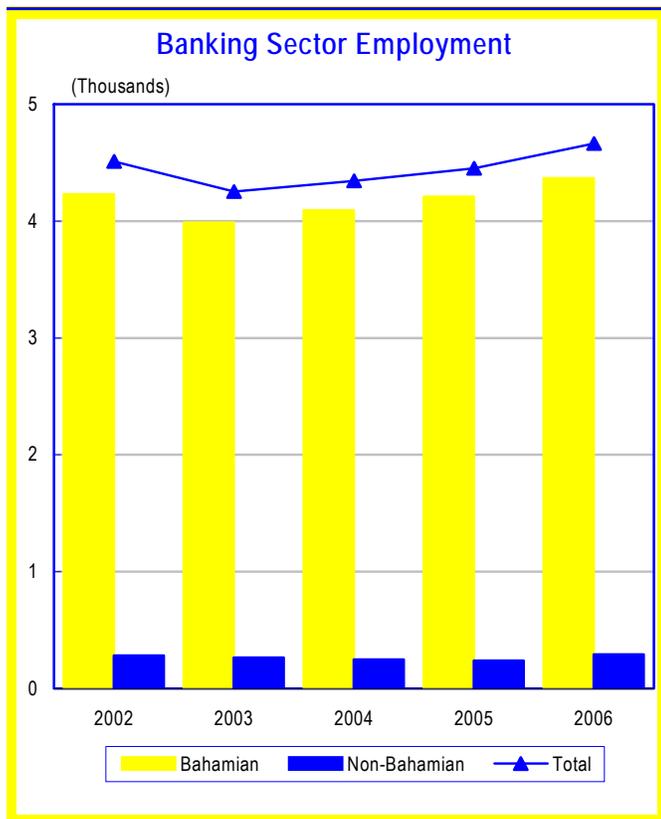
Reflecting the continued recovery in the banking sector, the total number of persons employed rose for the third consecutive year, by 211 (4.74%) to 4,662 in 2006. Specifically, the number of Bahamians employed increased by 158 (3.8%) to 4,368 and accounted for 93.7% of the total workforce. The number of expatriate employees rose by 22% (53) to 294, to represent 6.3% of the workforce, a turnaround from the 4.0% decrease registered in 2005. This development reflected expansions in banking operations, as the range of services provided to clients increased, coupled with continued efforts by the sector to comply with the Central Bank's physical presence requirements. Moreover, employment growth supported the industry's pressing need for high-skilled, bilingual employees, for both front and back end office functions.

### EXPENDITURE

Higher operational costs and capital expenditures elevated banks' total spending in 2006 by 10.5% (\$44.6 million) to \$470.5 million. This outturn completely reversed 2005's decline of 7.2% (\$32.9 million), and was significantly above the average outlay of \$421.7 million over the past five years.

Following 2005's 3.7% contraction, operational expenditures strengthened by 9.0% to \$445.0 million, although accounting for a slightly reduced 94.6% of total outlays. Administrative costs rose by \$19.4 million to \$195.9 million, reversing the \$18.4 million decline in 2005. This was largely explained by generally higher wages and employment levels, which boosted salary expenses by 8.1% to \$228.2 million—outpacing both the previous year's increase of 1.6% and the 2.0% average growth for the five years through 2005. Reflecting a return to the upward trend observed over the 2000–2004 period, the average salary paid to employees rose by 3.2% to \$48,958, in contrast to a 0.9% decline in 2005, which followed on a general fall in the number of persons employed in the offshore sector. Expenditures related to staff training were marginally increased to \$2.8 million, and Government fees stabilized at \$18.0 million.

ises, as the number of bank branches rose by 16 (16.8%) to 111. In contrast, renovation expenses declined by 6.6%.



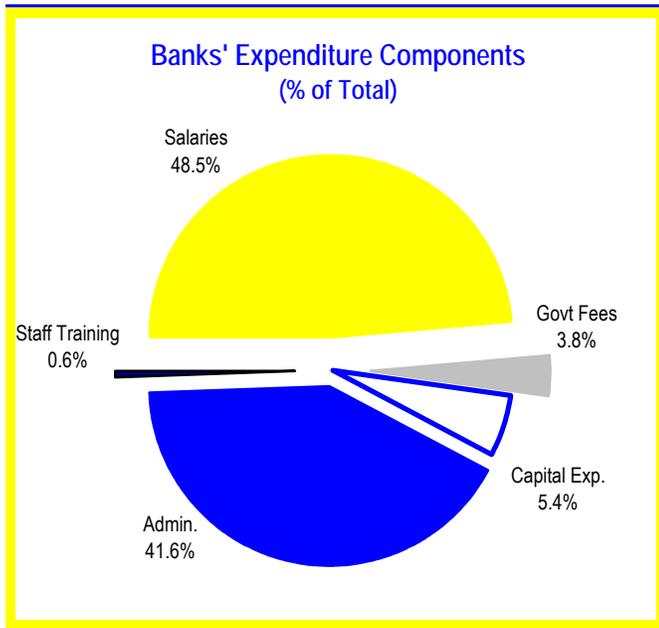
Capital spending escalated by 45.0% to \$25.5 million, a rebound from the 49.4% contraction recorded during 2005. In particular, investments in land and office equipment purchases rose strongly by 61.3%, along with a 28.4% expansion in investments related to new prem-

#### DOMESTIC VERSUS INTERNATIONAL BANKING

The disaggregation of banking institutions into domestic and offshore operations allows for the comparison of the more labor intensive, retail banking operations of the domestic sector with the generally more skill intensive, high value-added services of the international banking sector.

Reflective of efforts by banks to expand their market presence and increase the range of services provided, employment within domestic banks and trust companies rose by 3.9% (133) to 3,557. Employment growth in the offshore sector was comparatively stronger at 7.6% (78 persons) to 1,105. Consequently, domestic entities' share of total employment in the banking sector fell marginally by 0.6 percentage points to 76.3%. The number of Bahamians employed in the domestic sector rose by 124 persons to 3,499, and expatriate employment, by

9 to 58. As a result, the ratio of Bahamian to non-Bahamian employees fell from 69:1 in 2005 to 60:1.

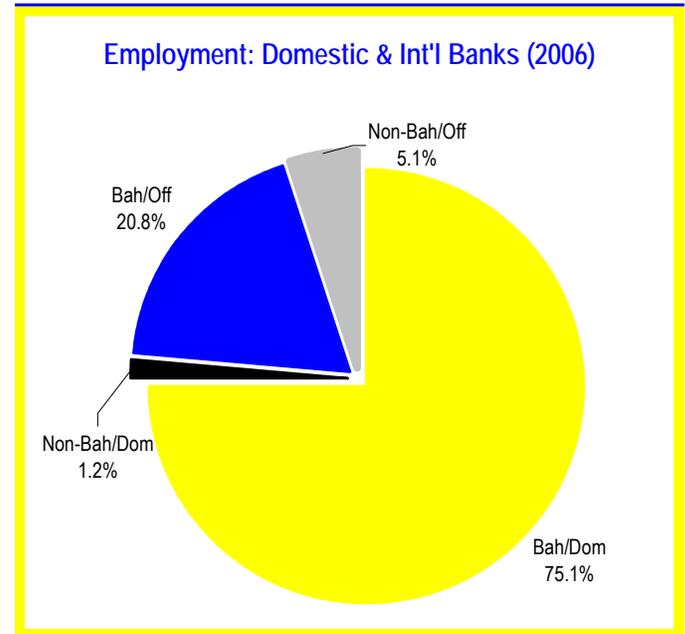


In the offshore sector, Bahamian employment was up by 4.1% to 869 persons, behind the 22.9% hike in non-Bahamian employment to 236. However, the ratio of Bahamians to non-Bahamians was unchanged at 4:1.

Total expenditures by domestic banks and trust companies recovered strongly by \$26.0 million (9.8%) to \$292.1 million during 2006, compared to an average annualized growth of 0.9% for the previous five years and a decline of 4.2% in 2005. Much of the increase was concentrated in operational expenses, which grew by \$22.2 million to \$275.9 million, as salary disbursements and other administrative costs rose by some \$11.0 million each to \$153.6 million and \$111.9 million, respectively. Outlays for Government fees at \$8.8 million and staff training at \$1.5 million were on par with the previous year's levels. Capital investments increased by \$3.8 million to \$16.3 million, reflecting outlays for land (\$1.5 million) and office furniture and equipment (\$2.6 million); however, renovation expenses declined by 7.4% to \$2.4 million.

On the offshore side, the 11.7% expansion in total spending to \$178.3 million was broadly-based among the major expenditure categories, and represented a reversal from the 1.9% decline registered in the five years ending

2005. Buoyed by growth in salary expenses (8.7%), staff training (12.1%) and other administrative (11.2%) costs, total operational payments were 9.4% higher at \$169.1 million. In addition, capital investments almost doubled to \$9.2 million, based on increased outlays for land, equipment and furnishings and new premises, which negated a 4.5% decrease in renovation expenses to \$1.11 million.



In 2006, the spread between offshore and domestic average salaries narrowed by an estimated \$908 to \$24,312, as the 3.8% rise in domestic banking average salaries to \$43,195 outpaced the 1.0% expansion in offshore sector salaries to \$67,507.

## OTHER FINANCIAL SECTOR ACTIVITIES

### INSURANCE SECTOR

Statistics compiled by the Central Bank and the Registrar of Insurance Companies indicate that the insurance industry continued to perform well during 2006, with the total number of insurance companies advancing by 15 to 205. Among the major categories, companies operating locally rose by 14 to 169 and external insurers firmed by 1 to 36.

Provisional data from the Central Bank's survey reveal that the sector employed approximately 1,391 persons, a slight 1.8% downturn from the previous year, as Bahamian employees (98.3% of the total) contracted by



**TABLE B. GROSS ECONOMIC CONTRIBUTION OF BANKS AND TRUST COMPANIES**

| Period   | 2001p                 | 2002p  | 2003p  | 2004p  | 2005p  | 2006p  | 2001p           | 2002p  | 2003p  | 2004p  | 2005p  | 2006p  |
|--|-----------------------|--------|--------|--------|--------|--------|-----------------|--------|--------|--------|--------|--------|
|  | <b>DOMESTIC</b>       |        |        |        |        |        | <b>OFFSHORE</b> |        |        |        |        |        |
| <b>A. TOTAL EMPLOYMENT</b>                     | 3,371                 | 3,309  | 3,208  | 3,185  | 3,424  | 3,557  | 1,215           | 1,201  | 1,045  | 1,181  | 1,027  | 1,105  |
| 1. Non-Bahamians                               | 44                    | 44     | 43     | 38     | 49     | 58     | 242             | 239    | 222    | 214    | 192    | 236    |
| 2. Bahamians (of which:)                       | 3,327                 | 3,265  | 3,165  | 3,147  | 3,375  | 3,499  | 973             | 962    | 823    | 967    | 835    | 869    |
| i) Local Banking                               | 2,740                 | 2,675  | 2,602  | 2,689  | 2,824  | 2,964  | 3               | 3      | 3      | 2      | 2      | 5      |
| ii) Offshore Banking                           | 59                    | 103    | 101    | 136    | 85     | 79     | 533             | 524    | 483    | 555    | 531    | 548    |
| iii) Trust Administration                      | 318                   | 251    | 291    | 206    | 267    | 287    | 167             | 171    | 164    | 190    | 188    | 207    |
| iv) Other                                      | 210                   | 236    | 171    | 116    | 199    | 169    | 270             | 265    | 173    | 220    | 114    | 109    |
|  | <b>(B\$ Millions)</b> |        |        |        |        |        |                 |        |        |        |        |        |
| <b>B. TOTAL OPERATIONAL COSTS</b><br>(1+2+3+4) | 231.9                 | 230.1  | 225.4  | 250.2  | 253.7  | 275.9  | 149.4           | 146.8  | 156.8  | 177.6  | 154.6  | 169.1  |
| 1. Salaries                                    | 124.9                 | 129.9  | 129.5  | 126.4  | 142.5  | 153.6  | 70.3            | 72.9   | 67.1   | 82.8   | 68.6   | 74.6   |
| 2. Government Fees                             | 6.7                   | 6.4    | 6.7    | 7.4    | 8.8    | 8.8    | 9.8             | 9.1    | 9.7    | 11.6   | 9.2    | 9.2    |
| i) Licence                                     | 3.0                   | 3.2    | 2.8    | 2.8    | 4.9    | 4.4    | 4.9             | 4.1    | 3.9    | 4.2    | 4.7    | 4.0    |
| ii) Company Registration                       | 1.2                   | 0.7    | 0.7    | 0.7    | 0.7    | 0.7    | 1.4             | 2.1    | 0.7    | 0.7    | 1.2    | 1.8    |
| iii) Work Permits                              | 0.5                   | 0.4    | 0.5    | 0.6    | 0.6    | 0.6    | 1.8             | 1.9    | 1.8    | 1.9    | 1.8    | 2.1    |
| iv) Other Government Fees                      | 2.0                   | 2.2    | 2.7    | 3.3    | 2.6    | 3.1    | 1.7             | 1.0    | 3.4    | 4.8    | 1.5    | 1.4    |
| 3. Staff Training                              | 1.2                   | 1.3    | 1.3    | 1.3    | 1.5    | 1.5    | 1.0             | 1.6    | 1.1    | 1.2    | 1.2    | 1.4    |
| 4. Other Administrative Costs                  | 99.1                  | 92.5   | 87.9   | 115.1  | 100.9  | 111.9  | 68.3            | 63.2   | 78.9   | 82.1   | 75.5   | 83.9   |
| <b>C. CAPITAL EXPENDITURE I/</b>               | 25.4                  | 13.2   | 11.9   | 27.8   | 12.5   | 16.3   | 23.3            | 6.1    | 3.6    | 7.2    | 5.1    | 9.2    |
| <b>D. TOTAL EXPENDITURE (B+C)</b>              | 257.3                 | 243.3  | 237.2  | 277.9  | 266.2  | 292.1  | 172.7           | 153.0  | 160.3  | 184.8  | 159.7  | 178.3  |
| <b>E. AVERAGE SALARY (B\$/000)</b>             | 37,064                | 39,250 | 40,352 | 39,699 | 41,618 | 43,195 | 57,876          | 60,717 | 64,214 | 70,082 | 66,838 | 67,507 |

**Source: The Central Bank of The Bahamas**

I/ (includes construction, renovation expenses and other fixed assets)

22 to 1,367; while non-Bahamians were lower by 3 at 24. Companies' aggregate expenditure advanced marginally by 0.28%, to \$116.4 million, reflecting a \$3.0 million rise in operational outlays to \$110.4 million. In contrast, other "miscellaneous" capital expenditures and payments for renovation expenses softened by \$1.08 million and \$1.6 million, to \$5.1 million and \$0.9 million, respectively.

#### *CREDIT UNIONS*

Preliminary estimates from the Department of Cooperative Development revealed that total assets in the sector strengthened by 14.2% to \$201.0 million.

Meanwhile, partial results from the Central Bank's 2006 survey, point to a marginal reduction in total expenditure by \$0.7 million to \$6.2 million. This outturn reflected a slowdown in fixed asset acquisitions, following substantial capital investments in office equipment and furniture in 2005. Consequently, total spending on fixed assets fell by nearly 50.2% to \$0.6 million. Moreover, despite a 2.0% expansion in salary payments to \$3.0 million, decreased outlays for "miscellaneous" administrative expenses resulted in total operational expenditures contracting by 1.4% to \$5.5 million.

Data on employment showed that the number of workers in the industry was virtually unchanged at 106; while the increased use of full time resources resulted in average salaries firming by 1% to \$28,594 per person.

#### *INVESTMENT FUNDS INDUSTRY*

Based on information compiled by the Securities Commission of The Bahamas, the number of active mutual funds under management rebounded to 725 in 2006 from 699 in 2005. Correspondingly, asset valuations firmed by US\$29.8 billion to US\$205.0 billion. A net increase of four (4) investment fund administrators brought the total to 63 by end-2006.

#### *CAPITAL MARKETS DEVELOPMENTS*

Buoyed by the general improvement in economic conditions, which strengthened investor confidence, the BISX All Share Price Index appreciated by 24.1% to 1,676.2 points in 2006, following a 30% expansion in 2005. A healthy 34.5% to 742.2 points gain was also registered in the broader Fidelity Capital Market Index (FINDEX)—which captures over-the counter trading—compared to 28.4% in 2005. The total market capitaliza-

tion of shares traded on BISX rose by 20.9% to \$3.2 billion; however, the volume of shares traded on the Exchange declined by 21.9% to 5.3 million, with value correspondingly lower by an equivalent percentage to \$28.7 million.

In other capital market developments, Kerzner International Ltd. (KZL) completed its "going-private" transaction on August 28, 2006. All issued and outstanding shares were cancelled and repurchased at a cash price of \$81.00 per share. Consequently, the Bahamian Dollar Receipts (BDRs) of KZL, which commenced trading on the Exchange in July 2004 at a ratio of ten BDRs for each KZL share, were repurchased at a price of \$8.09 per share, representing a capital appreciation of 57.4% over the initial \$5.14 listing price. Despite the withdrawal of KZL from the Exchange, the listing of Consolidated Water Company in January 2006 left the number of companies registered on BISX at 19. Regarding mutual funds, Fidelity Bank Limited listed its second mutual fund, Fidelity Prime Income Fund Ltd, in December of 2006.

#### **RECENT REGULATORY DEVELOPMENTS**

Aside from an ample pool of skilled labor, other important features of a successful and competitive financial sector are its regulatory framework and product offerings, transparency and the level of sophistication. During 2006, the Central Bank of The Bahamas, in consultation with local financial service providers, continued efforts to enhance the regulatory infrastructure under its supervision and to ensure industry compliance with local and international standards. In this regard, several pieces of legislation proposed by the Bank were brought into effect. Among these were the Banks & Trust Companies (Large Exposures) Regulations 2006, which define large exposures as generally those which are greater than or equal to 10% of a licensee's capital base. These regulations prescribe the maximum permissible single exposure and the maximum permissible exposures to related parties of licensees. They also limit a licensee's aggregate large exposure, describe the conditions under which large exposures may be allowed and include penalties for non-compliance.

Public private partnership continues to figure prominently in initiatives to improve the competitiveness of the industry. As an example, at the start of 2005 steps were taken to lay out the infrastructure for the operation of

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Private Trust Companies (PTCs). This involved collaboration between the Central Bank and a number of agencies including, the Bahamas Financial Services Board (BFSB), the Association of International Trust Companies (AIBT) and the Society of Trust and Estate Practitioners (STEP). As a result, in 2006 amendments were made to the Central Bank of The Bahamas Act, 2000 and the Banks and Trust Companies Regulation Act, 2000, to facilitate the operation of Private Trust Companies (PTCs). These companies, which do not conduct business with the general public, are normally used to administer the assets of high net worth families, and are subject to a more moderate supervisory framework than trust companies that offer services to the public, including exemption from the licensing requirements of the Banks and Trust Companies Regulation Act, 2000. Though exempt from licensing, PTCs are required to have resident Registered Representatives, which are also the Central Bank's primary point of contact for supervision of PTCs. They provide the services of secretary, director or other administrative services to PTCs and are subject to know-your-customer and record keeping compliance measures under the new legislation.

There was also an evaluation exercise carried out by the Caribbean Financial Action Task Force (CFATF), to assess the local financial services industry along with its

regulatory bodies, with the objective of measuring their compliance with the Financial Action Task Force's (FATF) 40 Recommendations on Money Laundering and nine Special Recommendations on the Financing of Terrorism. The results of this exercise are expected to be disseminated in 2007.

In other regulatory developments, the Bank Supervision Department of the Central Bank issued five new guidelines and two consultative papers during the year. It also proposed amendments to the Banks and Trust Companies (License Application) Regulations, 2002 and responded to thirty-three regulatory requests from foreign regulators.

## CONCLUSION

The review of the financial sector's activities revealed a trend of continued strengthening, as improvements noted in 2005 were extended into 2006. The outlook for the sector remains optimistic, as institutions continue to employ high caliber individuals and strive to maintain a competitive advantage over other jurisdictions. In this vein, the Central Bank will continue to collaborate with domestic and international agencies to fine-tune, adopt or develop regulatory mechanisms and initiatives to ensure that the sector remains properly regulated.