MPC Press Briefing

Remarks by John Rolle, Governor

26 July, 2019

Welcome to the Central Bank's quarterly economic briefing. These coincide with the conclusion of our monthly Monetary Policy Committee meeting, which assess whether, given trends and the outlook, any adjustments are necessary to policies affecting money and credit trends, and whether the outlook for the external reserves are within the safe bounds that would uphold the value of the Bahamian currency. This quarter the Central Bank also relaunched its survey on current business conditions. Today, the Central Bank is also publishing its latest financial stability report.

Overall, the indicators continue to show strengthening in the Bahamian economy since 2018. This mainly reflects growth in stopover tourism. While the showing in the vacation rental market is a strong factor, improvement in the hotel segment was the most dominant factor. In particular, the industry absorbed the room capacity boost from Baha Mar, both increasing the average room occupancy rates and securing higher average daily room rates. The 2020 outlook is for further growth in tourism, but at a slower pace, since hotel room inventories will not increase by the same magnitudes as in the past 12 months.

A steady, modest inflow of foreign investments is also providing economic stimulus, particularly to construction. Most of these investments are occurring in the tourism sector, in resort and residential facilities and in cruise-line attractions.

The foreign exchange sector activities, just mentioned, have had positive impact on financial sector indicators and the strength of The Bahamas' external reserves. Seasonal growth in the reserves in the first half of 2019 was at double the pace of gains recorded in the first half of 2018. At the end of June, the external reserves were just above $1.5 billion, very close to the same level as in 2018. Driving this performance, there was a more than doubling in the net amount of net foreign exchange purchased by commercial banks from the private sector, that were subsequently sold to the Central Bank. A part of this though, was also that the private sector's spending on imports appeared to be reduced in comparison to 2018. The subdued spending on imports would have reflected continued reduction in total credit to the private sector, which is an important financer of imports. Another probable factor, not directly measured, was that the VAT rate change increased the cost of imports.

The constrained lending environment is a continued reflection of the high rates of credit delinquencies from which commercial banks are recovering. The Central Bank is prompting these institutions to take more aggressive steps to reduce the delinquency rate, making their balance sheets stronger, much faster, before another recession happens. This would include approaches such as recognition of higher losses on loans that are in default; taking more discounted views on the value of foreclosed mortgaged properties, and taking more persistent efforts to selloff repossessed properties.

Turning to the outlook, beyond the ever present risks from severe hurricanes, uncertainties from ongoing international trade disputes and the Brexit challenges facing Europe, the Bahamian economy is expected continue to grow over the next few years. The domestic banking sector will continue to experience high levels of liquidity, and the foreign reserves of the central bank are expected to continue increase at a mild pace. When the medium-term credit delinquency rates are taken into account, the Banking sector is only expected to begin to recover its total lending to the private sector at a gradual pace.

Taking this assessment into account, the Central Bank has decided to maintain its accommodating posture for private sector credit growth. Our posture, however continues to assume sustainable outcomes in how large public and private sector financing operations are executed. For large scale transactions, either involving debt or equity operations, a prudent inclusion of foreign currency flows would be essential so as not to divert Bahamian credit from households and the smaller commercial borrowers.

Our financial stability report, being released today, also puts some focus on the sustainability of monetary policies. We note that there are no pressing risks to financial stability, but there are vulnerabilities that need to be tackled. One is the Central Bank's assessment that it is in the Bahamas' interest to manage a gradual reduction in surplus capital from within the banking system. Capital levels are comfortably in excess of our minimum requirements and more than adequate to absorb extreme, surprise loses that the average bank might encounter from severe shocks. Continuing to tolerate such excesses, in the Central Bank's view, would only increase the medium-term likelihood that lending institutions would take on riskier activities to generate comfortable returns on these surpluses. Unwinding would involve a multi-year outflow of dividends by foreign banks that must be factored into our projections for healthy external reserves balances.

At the same time the Central bank is tasked with managing a gradual reduction in bank liquidity, as these surpluses could potentially fuel too rapid a pace of credit growth in the future, which could eat into the external reserves. Our stated approach is to continue to selloff the Central Bank's holding of Government debt, which would reduce the excess liquidity in the system. Also, we continue to progress the establishment of the credit bureau that would generate information to help banks make sound lending decisions.

Returning to the economic assessment, the Central Bank's latest of survey of business conditions, uncovered varied feedback from the private sector on how the economy performed in recent months. Most surveyed business noted higher cost in their operations but stable to improved operating conditions. The outlook held by most firms was for stable to further improved conditions over the remainder of 2019, with lowered inflation expectations, and healthier employment outcomes than in the first half of 2019.

The Central Bank continues to monitor the economic environment, and will adjust its policy stance as necessary, in the interest of preserving the Bahamian dollar fixed exchange rate arrangements and managing financial stability risks.