Monthly Economic and Financial Developments (MEFD)

March 2023

Remarks by the Governor
01 May 2023

Preliminary indications are that the Bahamian economy continued to expand at a healthy pace in the first quarter of 2023. However, with stopover visitor volumes being closer to full recovery from the pandemic, the pace of growth was, as expected, strongly moderated in comparison to the same period of 2022. Alongside the tourism impetus, The Bahamas benefitted from continued foreign direct investments mostly attracted to real estate and tourism developments. In the public sector, the government's revenue recovered further, although deficit reduction efforts were also paced by the recovery in government spending. In the meantime, the latest data continued to show elevated consumer price inflation, passing through from higher costs on imported fuel and other goods and services. While the economic outlook is still positive on balance, downside risks are elevated, with the war in Ukraine adding to the headwinds from central banks efforts to bring down inflation in the major economies.

Although there have not been any recent official estimates of the unemployment rate, the estimate is still projected to be higher than it was before the pandemic started. However, the unemployment rate would also have fallen significantly from elevated setback, projected in excess of 20 percent during parts of 2020 and 2021. The prospects for further reduction in the employment rate will depend on the speed at which the economy grows after 2023, catering both to the surplus of new labour that accumulated during the recession and workers who were only temporarily unemployed.

As regard tourism, the recovery trend during the first quarter still conveyed elements of pent-up travel demand. Taking average pricing increases into account, the stopover industry's seasonal earnings are projected to have already fully recovered, even though visitor volumes still have a small amount of capacity to regain. For 2023, balanced against downside risks, tourism earnings are also expected to exceed pre-pandemic estimates on a calendar year basis. As to visitor head count, comparing season with season, it is estimated that at the end of the first quarter, based on air arrival trends, stopover visitor volumes were approximately recovered to about 97 percent of their 2019 levels–which would have been the pre-COVID high. The cruise sector, which completed this seasonal recovery in mid-2022, experienced further exceptionally stronger gains, with no signs of levelling off since the rebound from COVID-19.

The tempered pace of growth was captured in the foreign exchange markets trends. In particular, total private sector inflows through commercial banks grew by almost 10 percent in the first quarter, compared to a more accelerated recovery-paced gains of almost two-thirds in 2022. Other than tourism's impact, the outcome also points to potentially slowed contribution from other foreign exchange earning activities, such as collectively real estate and foreign direct investments.

In the meantime, foreign exchange outflows through the private sector, mainly an indicator of domestic demand for imports of goods and services, rose by about 20 percent in the first quarter of 2023, compared to the recovery-propelled boost of 37% in 2022. Because private sector outflows grew faster than inflows, it led to reduced net sales of foreign exchange from commercial banks to the Central Bank.

While this helped moderate the seasonal buildup in external reserves, the transactions with the public sector had the greater impact. In particular, in the first quarter, the Central Bank made a net sale of foreign currency to the public sector, as compared to the net purchase in excess of $300 million in 2022, which was timed with the bulk of the previous fiscal year's external borrowing activities.

As of the beginning of May, the external reserves measured approximately $2.7 billion, still a healthy position. On a seasonal basis, these balances are expected to peak later in the year, before being drawdown over the closing months of the year. The reserves are expected to end 2023 below their closing levels of 2022. This is in keeping with stronger private sector demand for imports of goods and services, some of which could be driven by expanded private sector credit.

As regard to credit, bank lending to the private sector remains constrained overall. Based on the latest lending condition survey through the second half of 2022, the volume of requests for loans has increased, but new lending was still pacing slower than debt repayment. Hence, even over the first quarter of 2023, total private sector contracted. However, the contraction was more moderated than in 2022, still holding out prospects for more incremental increase in total credit by the end of 2023. In the meantime, the domestic banks continued to record healthy reduction in the credit delinquency rate over the first quarter of the year. Continued reduction in the delinquency rate, along with increased use of the credit bureau, is expected to further improve the environment for lending.

Turning to the outlook, the Central Bank expects that growth in the economy will moderate closer to 4 percent in 2023, after regaining about 14.4 percent in 2022, according to the Bahamas National Statistical Institute. Correlated with this would also be more moderated changes in bank liquidity, healthy evolution of the external reserves and room for further reduction in the government's budget deficit. The domestic environment is expected to be able to support both increase lending to the private sector and allow the government to increase its reliance on local borrowing to finance the deficit.

However, the downside side risks to the economy are still significant. These include external pressures that are contributing to elevated inflation and which, in the case of fuel, could make both travel and accommodations more expensive for tourists. Likewise, central bank-led increases in interest rates in the US and other major economies could have recessionary impact in these economies, further limit travel and increase the cost of financing for foreign direct investments. COVID-19 disruption risks also linger in the background.

In this environment, the Central Bank's monetary policy position is to continue to be accommodating for lending to the private sector. Although this increases the potential for net foreign currency outflows, it is still projected to leave the external reserves in a healthy position overall, and therefore maintain solid support for the Bahamian dollar fixed exchange rate. As regard to other foreign exchange market policies, the Central Bank will maintain a very measured approach to investment currency reforms, while favouring increased administrative efficiencies in processes governing trade payments, and both inward and outward direct investments.