GRAY/10/3983

October 26, 2010

Statement by Mr. Bergo and Mrs. Alfredsdottir on The Bahamas
(Preliminary)
Executive Board Meeting 10/102
October 27, 2010

We thank staff for a well-written report and Mr. Hockin and Mr. Rolle for their informative Buff. We share the main conclusions of staff's assessment and will thus limit our remarks to only a few points.

The global financial crisis has hit the Bahamian economy rather adversely due to the high dependence on tourism and financial services. Consequently, GDP has fallen, unemployment risen, budget and external deficits have widened, and FDIs have shrunken. However, according to staff the medium-term outlook appears to be satisfactory, returning to a trend growth rate of about 2 ½ percent for 2012.

Fiscal Policy

The authorities have maintained spending in line with the budget in order to mitigate the demand shock. We note, nevertheless, that the budget balance has been in a negative territory for an extended period and this trend has been exacerbated in the downturn. This is a matter of concern and should be addressed as soon as the authorities believe that actions taken will not unduly depress demand. We also note that government debt is now projected to approach 55 percent by 2015. We note that tax reform is being initiated and improvements in tax administration are expected to improve revenue. Nevertheless, we agree with staff that additional, and bolder, measures may be necessary to improve the fiscal position

We agree with staff on the need for greater fiscal transparency, not least with respect to the SOEs. Also, we underline the importance of strengthening macroeconomic and financial statistics and, specially, government finance statistics and national accounts.

Monetary Policy

We agree that the fixed exchange rate continues to provide an adequate nominal anchor. On reserve cushion, we tend to agree with staff that an even larger reserve could help to mitigate the impact of large negative shocks. *Could staff please comment on what levels of reserve they believe are appropriate?* We welcome the intensified monitoring of asset quality by the CBOB and the safeguarding capital buffers in the banking system as described in the Buff.

Financial Sector

The banking system appears to be normalizing but risk remains. On that front, staff especially draws attention to NPLs which have increased significantly in the downturn. *We are concerned about the proportion of NPLs in private sector credit; could staff comment on the outlook and prospective developments?* We agree with authorities and staff that the deterioration in the banks' loan portfolio warrants close monitoring and we strongly support increasing the intensity of on-site inspections and monitoring.