

THE CENTRAL BANK OF THE BAHAMAS

MONETARY POLICY IN A SMALL, OPEN,  
DEPENDENT ECONOMY: THE CASE OF  
THE BAHAMAS

by

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MONETARY POLICY IN A SMALL, OPEN DEPENDENT  
ECONOMY: THE CASE OF THE BAHAMAS.

Monetary policy plays a very important role in economic growth and development, and central banks, as agents of the Government, are empowered with various tools of monetary and credit control which can be applied singly or in combination to achieve certain policy objectives. These objectives incorporate not only the conventionally accepted goal of influencing the level, but also the direction of economic activity. The policy in financially advanced economies is to view the control of the money stock as the proximate objective of monetary policy, with the underlying assumption being that the expansion in the rate of growth of the money stock leads to increases in nominal income, employment and the price level. The appropriate policy under these circumstances, therefore, is to choose a desired rate of growth for the money supply which is consistent with the targets for output, employment and prices. This underlies the monetarist approach as expounded by Milton Friedman.

This approach, however, has little or no relevance for a small, open, dependent economy where the money stock is not an exogenous variable that can be manipulated by the monetary authorities, but rather an endogenous variable determined by the balance of payments, the level of economic activity, the monetary base and the asset preference of commercial banks and the non-bank public. In such economies, therefore, any attempts by the monetary authorities to control the money stock would be beset with difficulties. This paper will review the Central Bank's experience in the use of monetary policy instruments over the period 1979 to 1985,

with a view to highlighting the objectives of monetary policy in the Bahamas and the limitations surrounding its use.

The structure of the paper will be as follows: In Section I, we will discuss the basic philosophy underlying monetary policy in the Bahamas; and the real, monetary and institutional factors which tend to complicate the task of conducting monetary policy. Section II will outline the various tools of monetary and credit control at the Central Bank's disposal. Section III will review monetary and credit developments in the late seventies, which led to the adoption of certain monetary policy measures in late 1979 and 1980. Section IV will discuss developments leading up to the various policy measures that were taken since 1980. In Section V, some concluding comments will be made on the limitations of monetary policy in a small, open dependent economy like the Bahamas.

## Section I

The formulation and conduct of monetary policy is a reflection of the economic and financial system in which it operates. In advanced economics, for example, monetary policy is used primarily to control inflation, on the assumption that there is a strong correlation between growth in the money supply, credit and inflation. However, in the case of a small open, dependent economy, the success with which monetary policy can be used to effect growth and stability is very limited. In these economies, monetary policy decisions are dictated, by and large, by external forces. In the case of the Bahamas, monetary policy decisions are heavily influenced by developments in the United States, the major trading partner. Indeed, having regard to the strong trade and financial ties that exist between the Bahamas and the United States, any attempts by the Bahamian authorities to pursue an independent monetary policy based on domestic considerations alone would be most imprudent.

In the exercise of monetary policy, the Central Bank is mindful of the need to maintain both internal and external stability. However, the ability to achieve the former is very limited since inflation is primarily "imported" and hence, is largely outside the control of the authorities. The task of achieving internal stability is further complicated by the fact that there is little scope for manipulating the prices of consumer and producer goods as domestic production is low. There is, however, some room for influencing the price of services, particularly tourism through wages and wage settlements. The extent to which this is done can and does have a significant impact on overall costs and

and prices owing to the dominance of the tourist sector. Recognizing the limited use to which monetary policy can be successfully applied to achieve internal stability, and having regard to the economy's strong reliance on external trade, and hence its extreme vulnerability to external vagaries, the Bank focuses mainly on the external balance. Monetary policy, therefore, is primarily geared towards protecting the country's international reserves.

The success of any monetary policy is determined in the final analysis by the monetary authorities ability to control the monetary base, hence influencing the liquidity of commercial banks and their ability to expand credit. The monetary base may be analyzed from the 'source' or the 'use' side. The net source base, that is, the supply of reserve money, is defined as the net foreign assets of the Central Bank; net credit to the Government and commercial banks by the Central Bank; and other assets of the Bank. The uses or the demand for the base are the net liabilities of the Central Bank, defined as currency in active circulation and commercial bank reserves. It is determined by the demand for cash of the non-bank public and the derived demand for required reserves and excess reserves of commercial banks.

The unpredictable influences on foreign exchange receipts and the, by and large, uncontrollable impact of the fiscal budgetary deficit on the source base makes the task of controlling the money stock very difficult, if not possible in the case of The Bahamas. The inflow of foreign exchange is not under the direct control of the Central Bank since foreign exchange receipts or losses depend ultimately on developments in the real sector, in this case the tourist sector which is the major source of the foreign exchange

component of the monetary base. Foreign exchange inflows from tourism are generally unstable, particularly in the short run, since tourist expenditure depends on movements in real incomes in developed economies, in our case primarily the United States.

In a small, open, dependent economy like the Bahamas, excess credit expansion will jeopardise currency stability as it encourages increased expenditure, which leads directly to a loss of foreign reserves as imports increase. The Central Bank may, therefore, attempt to influence foreign exchange reserves hence, reserve money by regulating credit. However, there is a limit to which a restrictive credit policy can be used to protect the balance of payments because of the implications for growth. Money and credit play a crucial role in economic activity and increases in both aggregates should reflect and be consistent with a country's growth objectives. Too little credit would reduce output and employment, hence developing countries like the Bahamas, must be careful not to be too restrictive in their credit policies.

There are certain monetary factors which can frustrate the Central Bank's attempt to control the supply of high powered money, such as, Government expenditure and the public's demand for cash. Central Banks have no real control over Government credit which is determined by budgetary operations. While the Bahamas is no exception, The Central Bank Act does place a statutory limit on credit to Government. The Act stipulates that loans and advances to Government cannot exceed ten (10) per cent of Government's average ordinary revenue which is defined as the average revenue over the most recent three (3) years. This provides an

important instrument of control as Central Bank credit to Government, either through direct advances or purchases of Government securities, is a key determinant of reserve money. Government expenditure increases the monetary base either by expanding currency in circulation and/or deposits.

The impact of Government's budgetary operations on reserve money is compounded by the fact that the Government also holds deposits with commercial banks, as well as with the Central Bank. A drawdown of Government deposits with commercial banks decreases reserve money, while a build-up increases it. The initial impact of a government's registered stock issue, and the manner in which the Central Bank arranges for its financing through non-inflationary means. When an issue is floated, this has the immediate impact of decreasing reserve money, as the proceeds are kept on deposit with the Central Bank. The drawdown of these funds will depend, in large measure, on the speed with which Government's capital development projects are implemented. If projects are delayed, the funds will remain effectively sterilized at the Central Bank, thus exerting pressure on commercial bank liquidity. The Central Bank cannot transfer any part of these deposits to commercial banks to ease this pressure without Government's approval. It can, of course, accommodate commercial banks by making direct advances to them against Government securities. However, subsequent drawdowns by Government of deposits held with the Central Bank may create excess liquidity and increase commercial banks' ability to lend at a time when the Central Bank may be pursuing a policy of credit restraint.

Reserve money is also influenced by several institutional factors peculiar to The Bahamas, one of which relates to the dualistic feature of commercial banking operations. There are ten commercial banks in the Bahamas, all of which are branches of international banks. The duality in their operations relates to the fact that they simultaneously conduct domestic and offshore banking business. These banks are direct sources of reserve money because they have access to foreign exchange which can be sold to the Central Bank for domestic currency. They are allowed to deal in foreign currency against Bahamian dollar within specified limits, and they are permitted to bring in funds from abroad to make loans in Bahamian dollars or in foreign currency with Exchange Control approval. In fact, a substantial proportion of the domestic portfolio of these banks consists of foreign currency loans and advances to residents. Of course, the extent to which banks will avail themselves of external funding will depend in part on the spread between the external cost of funds and the return that the funds yield locally; and partly on their open position.

On the open position, commercial banks are required to maintain a position in Bahamian dollars vis-a-vis foreign currency of \$500,000 long or short. This means that they can deal in foreign currency up to the limit where their Bahamian dollar assets (liabilities) do not exceed their Bahamian dollar liabilities (assets) by more than \$500,000. A long position occurs where Bahamian dollar assets exceed liabilities and any excess over this limit must be sold to the Central Bank for foreign currency to bring the 'open' position in line. Conversely, if Bahamian dollar liabilities exceed assets



How is the  
\$5m limit set  
by policy?  
So it can be  
waived, or is  
it written in the  
law requires  
and stay

(i.e., a short position) by more than \$500,000, this would require a sale of foreign currency for Bahamian dollar assets. This ensures that commercial banks do not bring in too much foreign resources to fund their domestic loan operations. If they were to do so, this would be reflected in an excessive long position and they would then be forced to surrender the excess Bahamian dollar assets to the Central Bank for foreign currency. This quantitative limit imposed by the Bank effectively controls the extent to which commercial banks' foreign borrowing can influence reserve money, and hence their ability to extend credit at a time when the Central Bank may be operating a tight monetary policy. It also limits the extent to which the country can increase its foreign liabilities, which constitute a direct claim on external reserves, in the short run.

A further institutional constraint on the effectiveness of monetary policy in the Bahamas is the National Insurance Board, which was created in 1974 to provide national social insurance benefits. The substantial surplus that this public corporation accumulates annually constitutes a direct source of reserve money, since a sizeable proportion of this surplus is held on deposit with commercial banks. The Board's surplus is now in excess of \$200 million, which makes it a dominant force in the system. Presently, an informal agreement exists between the Central Bank and the Board whereby, to accommodate the Bank's monetary policy objectives, the Board has agreed not to place funds with commercial banks without prior consultation with the Bank. The Board also holds sizeable deposits with the Central Bank. In order to prevent heavy downward pressure on interest rates from the placement of large

deposits by the National Insurance Board during periods of high liquidity, when rates are already low, the Board is encouraged to hold their surplus funds at the Central Bank. When liquidity is low, the Bank advises the Board to place deposits at selected commercial banks, or the Bank itself places them on the Board's behalf.

From the foregoing, it is clear that it is virtually impossible to effectively control the monetary base in an economy like the Bahamas owing to the inability to accurately predict the components of the source base. The task of successfully conducting monetary policy through controlling the monetary base is made even more difficult in the Bahamas because of the other peculiar features discussed above. Having regard to this, therefore, the Central Bank has adopted a more direct and unconventional approach towards the formulation and application of monetary policy. \*

Section II

The Bank attempts to influence the level of money and credit by managing liquidity rather than by frequently adjusting interest rates. However, while The Bank does not set targets for the level of interest rates, it seeks to ensure that rates are kept at a level consistent with the main monetary policy objective of protecting the balance of payments.

To facilitate the conduct of monetary policy, the Central Bank has at its disposal all the traditional instruments of monetary

and credit control, namely, variable reserve ratio; variable liquid assets ratio; discount rate; selective credit control; open market operations and moral suasion. The Bank is empowered to vary the statutory reserve ratio between 5 per cent and 20 per cent and to allow different ratios for different classes of commercial banks. However, the ratio was set at 5 per cent of Bahamian dollar deposit liabilities in July 1974, and has not been changed to date. The liquid assets ratio may be varied between 10 per cent and 30 per cent, but has been fixed at 20 per cent of demand deposits and 15 per cent of time and savings deposits, and borrowings since July 1974.

Loans and advances are made to commercial banks against the security of government registered stocks at the prevailing bank rate for a period not greater than the maturity date of the security or 93 days, whichever is longer. From time to time, a surcharge may be imposed for heavy and/or frequent borrowing. The amounts of any loans or advances to commercial banks cannot exceed 85 per cent of the market value of the security at the date of its acquisition by the Bank. Treasury bills are rediscounted at a rate of  $\frac{1}{2}$  of a percentage point above the average market rate of discount of treasury bills.

The authorities have opted not to exercise the power of selective credit control, and the absence of well-developed money and capital markets severely limits the extent to which open market operations can be effectively used. Moral suasion is widely used, and is undoubtedly the most effective tool in a small system such as ours. Ultimately, the choice of instrument depends on the prevailing economic, monetary

and financial conditions and the particular objective that is being sought. In the final analysis, the Bank prefers to use the direct approach rather than quantitative controls, as it is felt that such measures could prove to be disruptive and counter-productive.

### Section III

The sluggish growth in private sector demand for credit in the mid-seventies, as shown in Table I, reflects a sharp fall-off in private sector investment. The year 1977 saw a turnaround, with private sector credit increasing by \$13.7 million in Bahamian dollars. In an attempt to further stimulate private demand for credit and having regard to the strong growth in external reserves, the Central Bank agreed to a  $\frac{1}{2}$  percentage point reduction in the prime rate in April, 1979 from 9.5% to 9.0%.<sup>1</sup> As seen from Table I, this move coincided with the rise in Eurodollar rates. During the period 1976 - 1978 (III), Eurodollar rates were persistently lower than the rates on Bahamian dollar loans, with the differential getting progressively narrower from year to year. The lower rates on foreign currency loans encouraged the growth of businesses with a high or potentially high foreign exchange earning capacity.

The proportion of foreign currency loans to total loans and advances was relatively stable up to 1978 (II), when it rose to 40.6% from 35.8% in 1976 (IV). The shift in credit from foreign currency to Bahamian dollars started in 1978 (III) and gained momentum

in 1979, as the interest rate differential between Eurodollar rates and local rates widened. The impact of the lowering of the prime rate on the distribution of credit outstanding became increasingly evident by 1979 (II), with Bahamian dollar credit advancing by 8.2% to \$224.7 million, from \$207.7 million at end - 1978. Foreign currency credit over the same period declined by 9.8% to \$108.2 million. The shift to Bahamian dollar credit intensified further as the interest rate spread increased, in the wake of monetary measures taken by the Federal Reserve Board to protect the value of the dollar, which fell almost uninterruptedly on the major foreign exchange markets since June, 1979. The Federal Reserve Board increased the discount rate from 9.5% to 11.5% in July and 12.0% in October, 1979. Residents took advantage of the increased interest rate spread to pay off their foreign liabilities in advance, by increasing their Bahamian dollar liabilities. By the end of 1979, Bahamian dollar loans moved up by 28% over 1978, while foreign currency loans fell by 19%.

The authorities were of the view that the widening interest rate spread would be a temporary phenomenon, as it was anticipated that rates abroad would fall. It was also envisaged that the unfavourable impact of the credit expansion on the balance of payments would be cushioned somewhat by growth in domestic economic activity. Consequently, no action was taken and market forces were allowed to operate freely. However, subsequent developments in the fiscal area created a further squeeze on commercial bank reserves, which were already feeling the pressure from the expansion in Bahamian dollar credit. In June 1979, the Government floated a \$40.0 million Registered Stock issue to finance its capital deve-

lopment expenditure. However, so as not to compete with the private sector for the limited supply of skilled manpower and other real resources, the Government delayed the implementation of its projects. Consequently, proceeds of the stock issue were left on deposit with the Central Bank. This, coupled with the sharp expansion in Bahamian dollar credit, exerted severe pressure on reserve money and commercial bank liquidity (See Table II), as commercial banks financed much of the expansion in credit by drawing down their excess reserves. Excess reserves declined to an unprecedented low of \$5.6 million (1.5% of Bahamian dollar deposit liabilities) in late November, 1979, thus drastically reducing commercial banks ability to create credit at a time when the demand for credit is usually at a seasonal high. The authorities sought to deal with this situation in a manner that would have the least disruptive effect on the banking system.

The Central Bank, in consultation with the Government, transferred \$6.5 million from the Government's Registered Stock Account at the Bank to those commercial banks that did not qualify for a direct loan owing to a lack of adequate collateral. The rate charged for these deposits was the prime rate. The Central Bank also made a direct advance of \$2.0 million to commercial banks against Government securities at 1% above the prime rate, up from the usual  $\frac{1}{2}$  percentage point. This was designed to give a direct signal to banks that they should be more selective in their credit policy. By the end of the year, commercial bank excess reserves, as shown in Table II, stood at \$9.6 million (2.9% of Bahamian dollar deposit liabilities), which was still low by historical standards. Net free reserves, defined as excess reserves less Central Bank

advances and Government special deposits, declined to the dangerously low level of \$1.1 million or 0.3% of Bahamian dollar deposit liabilities.

At the end of 1979, several banks were forced to sell treasury bills to the Central Bank to meet their statutory reserve requirements. The impact of the expansion in Bahamian dollar credit and the freezing of Government deposits at the Central Bank on commercial banks liquidity was particularly acute at this time of the year when excess reserves is usually at a seasonal low. The seasonal pattern of excess reserves up to 1979 is shown in Chart I. Commercial banks usually accumulate reserves during the first half of the year as a result of heavy foreign exchange inflows from tourism. The decline in the second half of the year reflects in part a slowdown in tourist activity.

The process of substitution of Bahamian dollar liabilities for U.S. dollar liabilities peaked in the last quarter of 1979 and early 1980, when U.S. interest rates soared. As shown in Table IV, the rate differential in favour of Eurodollar rates jumped to 6.1% in 1980. Businesses were not only borrowing to repay their foreign currency debts, but also to build up their inventories as the cost of Bahamian dollar credit dropped below the expected rate of inflation. Also, with the rise in the cost of foreign credit, suppliers' credit became increasingly difficult to obtain, thus increasing the demand for Bahamian dollar credit.<sup>2</sup> Commercial banks financed this expansion in Bahamian dollar credit in part by selling government securities to the Central Bank.<sup>3</sup>

As liquidity worsened, domestic interest rates came under upward pressures. The Treasury bill rate rose late in 1979 and towards the end of the year the bank rate - the rate at which the Central Bank makes advances to commercial banks against government securities - was raised by  $\frac{1}{2}$  percentage point to 10%. In February 1980, the Bank took other measures to curb the rapid expansion in Bahamian dollar credit. Commercial banks' liquid assets position was scrutinized to ensure compliance with the statutory requirements and banks were asked to refrain from selling government securities to the Central Bank. Exchange Control approvals for prepayment of foreign currency loans were terminated and banks were encouraged to reduce loans to importers for financing inventories. Although it was anticipated that these measures would help to reduce the pressure on the foreign exchange reserves, the authorities recognized that unless the local lending and deposits rates were raised to more competitive levels to discourage further shifts in the currency mix of the public's financial assets and liabilities, the liquidity position of the commercial banks would continue to deteriorate.

Interest rates in The Bahamas remained relatively stable over the period 1976 - 1979. (See Table III). Savings deposits rates remained on average at around 4.75%, while rates on fixed deposits showed a general decline since early 1976. The prime rate remained fixed at 9.5% until April, 1979 when it was reduced to 9.0%. Being mindful of the adverse impact that an uncompetitive deposit rate could have on commercial bank resources, as savers opted to invest overseas, and as the expansion in Bahamian dollar credit continued unabated, the Central Bank moved quickly to deal



with the situation. The Bank agreed to a two percentage point increase in the prime rate in February 1980 from 9% to 11%. Concurrently, commercial banks were directed to raise the rate of interest on savings deposits by a similar amount from 4% to 6%. The bank rate was also raised at this time by  $\frac{1}{2}$  percentage point to 11%. Other deposits and lending rates also moved up.

Reflecting the impact of these policy measures taken in February 1980 and the significant fall in Eurodollar rates in April - May, the liquidity situation improved in mid-1980. However, as shown in Chart II, the seasonal improvement in the reserves position of the commercial banks during this period was less striking than in previous years. As Eurodollar rates soared again towards the end of 1980 (See Table I), liquidity tightened towards the end of the year and the demand for Bahamian dollar credit continued to grow. Deposit rates came under increasing upward pressure, and although the prime rate remained unchanged at 11%, the effective lending rates increased, in some cases quite significantly. The Central Bank moved to relieve the pressure on liquidity by making direct advances to banks against the security of Government securities.<sup>4</sup> Those banks which were not eligible to borrow from the Central Bank because of the lack of adequate collateral were forced to borrow on the interbank market. In an effort to deal with the excessive expansion in credit to the private sector, the Bank sought to discourage frequent use of its discount facilities. Consequently, in November 1980, the Bank imposed a 2% surcharge on frequent and/or heavy users of its accommodation facilities.

The persistent pressure on the country's foreign exchange

reserves particularly towards the end of the year when the demand for foreign exchange is normally at a seasonal high, became a cause for grave concern. It was observed also that commercial banks were selling much less foreign currency to the Central Bank than previously, particularly those banks which were holding most of the foreign currency accounts of residents. While Exchange Control Regulations permitted banks to deal among themselves in foreign currency, there was an understanding between the banks and the Central Bank that any foreign balances in excess of the current requirements of the holders of these accounts (mainly the hotels) should be sold to the Central Bank for Bahamian dollars. It was observed, however, that commercial banks were selling these excess balances on the interbank market at a rate above par rather than to the Central Bank.

While the Bank did not want to completely withdraw the right given to commercial banks to deal among themselves in the interbank market, it took steps to ensure that they would not abuse this privilege. With this in mind, the Bank sought to limit the amount of interbank foreign currency dealings by requiring that banks report all interbank foreign currency transactions in excess of US\$250,000 to the Central Bank. Further, in order to compete more effectively with commercial banks and increase the inflow of foreign exchange, the Bank agreed to buy U.S. dollar balances from commercial banks at a rate of US\$1.0000 = Bah. \$1.0000. Also, in order to make it more attractive for the buying banks to deal with the Central Bank, the selling rate was lowered from US\$1.0000 = Bah. \$1.0050 to US\$1.0000 = Bah. \$1.0040.

Section IV

In 1981, domestic interest rates came under considerable upward pressure as rates overseas rose sharply and as banks bid up deposit rates to attract deposits in the wake of a sharp rise in the demand for credit. The increase in credit in November reflected seasonal factors as well as purchases by Bahamians of several small foreign-owned companies. After averaging 8 - 8½%, interest rates on some fixed deposits rose to as much as 11½%. However, following a 2.7 percentage point rise in the three-month Eurodollar rate (See Table V), the interest rate differential between local lending rates and rates overseas rose markedly to 5.5% from 2.8% in 1980 (See Table IV). This widening of the interest rate spread in favour of foreign rates caused a significant shift from foreign currency credit to Bahamian dollar credit. Private sector credit in Bahamian dollars rose by 15%, while foreign currency credit fell by 10%. As Table IV reveals, the proportion of foreign currency credit to total credit dropped to 16.0% from a year earlier 19.3%. In an effort to ease the upward pressure on domestic interest rates, the Central Bank placed a ceiling of 10% on fixed deposit rates and directed commercial banks to restrict their expansion of consumer credit.

There were no fundamental changes in monetary policy during 1982. Commercial banks were encouraged to bring in foreign funds to supplement their domestic resources as Bahamian dollar credit to the private sector continued to rise, in the wake of a sharp increase in the interest rate differential in the first half of the year. In order to discourage unnecessary capital outflows relating to prepayment of foreign currency loans, the Bank tightened its Exchange

Control procedures, and in some instances applications for loan prepayments were refused. As part of its credit restraint policy, The Central Bank reinstated the 2% surcharge that was lifted in November, 1981 on frequent and excessive borrowings by commercial banks. The actual rate charged fluctuated between 10% - 12% depending on the level and frequency of borrowing. While this basic policy was maintained throughout the year, its application was flexible and depended, in large measure on the prevailing liquidity situation.

With the fall in international interest rates during the second half of the year and the concomitant lowering of the nominal differential between domestic interest rates and rates overseas from 5.5% to 2.1%, the rate of increase in Bahamian dollar credit to the private sector slowed. For the year as a whole, the rate of growth of Bahamian dollar credit to the private sector moderated to 13% from a year-earlier 15% (See Tables IV and VI). Although interest rates in the United States fell below the Bahamian dollar prime rate, foreign currency credit to the private sector fell. This indicated some uncertainty by the private sector about future trends in U.S. interest rates as apposed to the relative stability of domestic interest rates. Reflecting an increase in real interest rates, as inflation dropped to 6.1% from 11.1% in 1981, private sector deposits in Bahamian dollars rose by 14.0% as against a year-earlier 11.0% (See Table VI). However, liquidity remained tight owing primarily to a marked rise in demand for credit from the public sector, most of which originated from the non-financial public corporations.

In order to ease liquidity pressures, the Bank continued to

sterilize substantial amounts of National Insurance deposits and adopted a very selective approach in placing portions of these deposits with commercial banks, at rates varying between 9-½ and 10%.<sup>5</sup> Liquidity showed some improvement by May with the pick-up in tourism. However, commercial banks continued to seek accommodation from the Central Bank as liquidity was generally low during the year. As shown in Table VII, the level of excess reserves stood at \$9.4 million at year-end, down from a year-earlier \$10.2 million. However, net free reserves was a negative \$10.1 million, up slightly from the previous year. Net free reserves as a percentage of Bahamian dollar deposit liabilities was marginally lower from last year at a negative 2.2%.

The main thrust of monetary policy during 1983 remained that of credit restraint. In the wake of an unfavourable trend in net foreign currency purchases, the Central Bank took a decision in April to maintain domestic interest rates at a level that would allow a differential of no more than two (2) percentage points in favour of local rates compared to rates in the United States. Towards mid-year, there was some pressure from the banking system to increase interest rates, as a result of the system's adjustment to a temporary demonetization of some \$8 million following the Registered Stock issue in late April. In order to stem this upward pressure and to simultaneously maintain rates at the present levels generally, the Bank temporarily lowered the bank rate to 9% (See Table V), but reserved the option to apply a 2% surcharge for frequent and/or heavy borrowers. The use of the surcharge during the latter half of the year was flexible and depended for the most part on liquidity conditions. For the year as a whole, the interest

rate spread moved to 1.4%, in favour of the Bahamas (See Table IV).

With the fall in U.S. interest rates and the consequent shift in the interest rate differential in favour of the Bahamas, the growth in Bahamian dollar credit to the private sector eased to 8.0%, from a year-earlier 13%. The continued decline in foreign currency credit during the year reflected in part the reduction in and completion of a number of large investment projects. This moderation in Bahamian dollar credit, coupled with the full repayment of borrowings from the Central Bank brought a turnaround in the liquidity position of commercial banks. As shown in Table VII, excess reserves moved to a positive \$10.4 million or 1.9% of Bahamian dollar deposit liabilities, a sharp turnaround from the previous year's negative position.

The year 1984 saw some significant developments in external reserves, domestic credit and liquidity. International reserves rose sharply by \$39.0 million, compared with \$10.1 million in the previous year, while growth in domestic credit slowed to 5%, slightly above the rate of inflation. One possible explanation for the slowdown in credit growth may be the reduced demand for trade credit by local firms whose cash flow may have increased as economic activity pick-up. As seen in Table IV, the growth of Bahamian dollar deposits decelerated sharply to 6.0% from 14.4% in 1983. This was due in part to intense competition from the other local financial institutions whose deposits increased significantly, as they intensified their efforts to attract funds to expand their home mortgage financing.

The developments in external reserves and Bahamian dollar credit caused a further improvement in liquidity. Average excess reserves increased by \$8.9 million in 1984 to \$20.3 million. After reaching a peak of \$31.0 million in May, the absolute level of excess reserves fell to a year-end level of \$11.3 million, though up from the \$10.4 million and \$9.4 million recorded for 1983 and 1982 respectively (See Table VII). In view of the persistently high level of liquidity in the system during most of the year, the Bank continued to demonetize a substantial amount of National Insurance funds. However, as liquidity began to tighten towards the end of the year, commercial banks sought accommodation from the Central Bank. In order to restraint excessive credit expansion and hence protect the balance of payments, the Bank sought to discourage the frequent or excessive use of its short-term accommodation facilities by raising the bank rate to 9.5% from 9.0% (See Table V). Simultaneously, the rate applied to frequent or heavy borrowing was reduced to 10.0% from 11.0%. The Bank, through moral suasion, also continued its policy of encouraging commercial banks to lend more to the productive sectors and to limit credit for consumption purposes.

The trends observed in external reserves, domestic credit and liquidity continued into 1985. In the first quarter, external reserves rose by \$40.0 million, up \$30.4 million from the corresponding period last year. With the interest rate differential again moving in favour of U.S. interest rates (See Table IV), Bahamian dollar credit to the private sector rose by 9% from the same period

last year, and foreign currency credit fell by 25%. Liquidity remained high in the first quarter, with excess reserves at \$20.2 million or 3.7% of Bahamian dollar deposit liabilities (See Table VII).

These trends continued well into the second quarter. In light of the strong growth in external reserves, the high and rising levels of liquidity and the continued slowdown in credit growth, the Central Bank moved to promote economic activity by lowering interest rates. In May, the Bank dropped its bank rate by a full percentage point, from 9½% to 8½%. Commercial banks in turn, reduced their prime rate from 11% to 10% and the rate of interest on saving deposits, by an equivalent amount from 6% to 5% (See Table V).

This action was predicated on the rationale that lowering interest rates will stimulate activity in the interest-sensitive growth-oriented sectors. Reflecting the impact of the Bank's interest rate policy and excess liquidity, interest rates moved generally lower during the second quarter, and Bahamian dollar credit to the private sector rose by 9%.

#### Section V

Monetary policy is used by developed countries with varying degrees of success to effect certain policy objectives. However, while the economic and financial structure of these economies allow them a certain measure of success in the use of monetary policy, they too find that monetary policy is not a panacea. The economic



and financial problems faced by developed and developing countries are not fundamentally different, however, there are certain special circumstances in developing countries which necessitate a different approach towards economic and financial management. The scope for success in applying monetary policy to achieve growth with stability in a small, open, dependent economy is extremely limited. Indeed, the entire policy focus in such economies must necessarily be different from that of advanced economies.

Economies like the Bahamas cannot use monetary policy to achieve internal stability since the forces which determined movements in domestic prices are primarily external. The problem becomes even more acute if industrial and agricultural production is weak, as this does not allow for much control over the internal factors that influence price changes.

The success with which monetary policy may be used to effect external stability is also problematic. The structural weaknesses inherent in the Bahamian economy make it heavily dependent on external trade, as evidenced by a persistent deficit in the trade account. The fact that the Bahamas has managed to maintain a relatively high level of external reserves over the years is due more to supply factors rather than demand. Traditionally, tourist has performed well and the strong positive impact of tourist receipts on the invisibles account has been sufficient to wipe out the trade deficit and give an overall surplus in the current account. This pattern persisted up to 1980, when the current account shifted to a deficit.

The Central Bank's main policy stance has been and continues to be one of credit restraint. Through moral suasion

and its bank rate policy, the Bank encourages commercial banks to restrict growth in consumer credit and to increase loans to the productive sectors. However, the extent to which a central bank can restrict credit in an open, dependent economy like the Bahamas is seriously limited because of the strong interrelationship between the trade deficit and the level of economic activity. Indeed, in some instances, the line between loans for consumption vis-a-vis productive purposes may be clouded. Consequently, measures taken to restrict consumer loans may adversely affect producer loans and lead, in short, to an inefficient allocation of resources. It is for this reason that the Central Bank has adopted a more direct and unconventional approach in its execution of monetary policy.

Being small does have its advantages, however, in that it allows for quick and continuous feedbacks about developments and their effects on the banking system, hence facilitating timely policy response. Being mindful of the need for a co-ordinated strategy in policy formulation and execution, the Central Bank always seeks to ensure that monetary policy is compatible with fiscal policy. In its conduct of a fiscal policy, the Government has supported the Bank's efforts to maintain monetary stability and a favourable balance of payments by keeping its expenditure under control.

FOOTNOTES

1. Interest rates in The Bahamas are not subject to formal controls, but changes in the commercial bank rate and the savings deposit rate require in practice the concurrence of the Central Bank.
2. The rise in import prices, which resulted primarily from higher inflation in the United States, also contributed to the expansion in Bahamian dollar private sector credit.
3. At this time, the Central Bank's informal policy was to purchase government registered stocks from commercial banks at par. The policy was changed in 1982, at which time the Bank stood ready to buy stocks at a discount using the prime rate as the reference rate.
4. For 1980 as a whole, outstanding credit from the Central Bank to the commercial banks increased by B\$8 million, following a rise of B\$2 million in 1979. Also, the bank's holdings of Treasury bills declined by B\$6 million in 1979 and an additional B\$1.4 billion in 1980, to a level of only B\$2.6 million. Bank's holdings of other government securities denominated in Bahamian dollars increased by B\$6.2 million in 1979 as a whole (but they fell by B\$1.6 million in the last quarter of the year), followed by a decline of B\$11.3 million in 1980.
5. By end-1982, National Insurance deposits with commercial banks totalled \$11 million.

TABLE I Loans and Advances of Commercial Banks 1/

| <u>End of Period</u>               | <u>Total</u> | <u>Foreign<br/>Currency</u> | <u>Bahamian<br/>Dollars</u> | <u>Proportion<br/>of Foreign<br/>Currency Loans</u><br>% | <u>Interest<br/>Rate<br/>Spread 2/</u><br>% |
|------------------------------------|--------------|-----------------------------|-----------------------------|--|---|
| ( In millions of Bahamian dollars) |              |                             |                             |  |   |
| 1976 - IV                          | 270.3        | 96.7                        | 173.6                       | 35.8   | 4.2   |
| 1977 - I                           | 264.2        | 93.9                        | 171.6                       | 35.5   | 4.4   |
| II                                 | 274.6        | 97.0                        | 177.6                       | 35.3   | 3.9   |
| III                                | 297.5        | 115.5                       | 182.0                       | 38.8   | 3.3   |
| IV                                 | 306.6        | 119.3                       | 187.3                       | 38.9   | 2.4   |
| 1978 - I                           | 299.1        | 116.4                       | 182.7                       | 38.9   | 2.2   |
| II                                 | 319.1        | 129.5                       | 189.6                       | 40.6   | 1.7   |
| III                                | 323.3        | 127.0                       | 196.3                       | 39.3   | 0.8   |
| IV                                 | 327.8        | 120.0                       | 207.7                       | 36.6   | -1.6  |
| 1979 - I                           | 325.0        | 113.2                       | 211.8                       | 34.8   | -1.4  |
| II                                 | 332.9        | 108.2                       | 224.7                       | 32.5   | -1.6  |
| III                                | 347.4        | 107.2                       | 240.2                       | 30.9   | -2.7  |
| IV                                 | 362.1        | 96.9                        | 265.2                       | 26.8   | -5.7  |
| 1980 - I                           | 349.9        | 72.2                        | 272.7                       | 22.1   | -6.1  |
| II                                 | 360.1        | 73.3                        | 286.8                       | 20.4   | -0.2  |
| III                                | 367.2        | 72.2                        | 298.1                       | 19.7   | -1.1  |
| IV                                 | 395.1        | 76.2                        | 318.9                       | 19.3   | -6.1  |

SOURCE: Central Bank of the Bahamas and International Financial Statistics

1. Excludes loans and advances to the public sector.
2. Percentage point difference between prime rate on Bahamian dollar loans and 3-month eurodollar interest rate.

TABLE II Commercial Banks Reserve Position  
(B\$ Millions)

|  | 1975 | 1976 | 1977 | 1978 | 1979 | 1980 |
|--|------|------|------|------|------|------|
| Total Reserves   | 19.2 | 20.1 | 21.4 | 24.1 | 25.5 | 27.6 |
| Excess Reserves  | 9.5  | 9.2  | 9.4  | 10.9 | 9.6  | 8.8  |
| Borrowing from Central Bank                            | -    | -    | -    | -    | 2.0  | 10.0 |
| Placement of Government Deposits                       | -    | -    | -    | -    | -    | -    |
| Net Free Reserves                                      | 9.5  | 9.2  | 9.4  | 10.9 | 1.1  | -1.2 |
| (As a per cent of Bahamian dollar deposit liabilities) |      |      |      |      |      |      |
| Excess Reserves  | 4.9  | 4.2  | 3.9  | 4.1  | 2.9  | 2.3  |
| Net Free Reserves                                      | 4.9  | 4.2  | 3.9  | 4.1  | 0.3  | -0.3 |

SOURCE: CENTRAL BANK OF THE BAHAMAS

TABLE III Selected Interest Rates

(Quarterly average, per cent per annum)

|                                | 1         | 9          | 7           | 6          | 1         | 9          | 7           | 7          | 1         | 9          | 7           | 8          | 1         | 9          | 7           | 9          |
|--------------------------------|-----------|------------|-------------|------------|-----------|------------|-------------|------------|-----------|------------|-------------|------------|-----------|------------|-------------|------------|
|                                | Qtr.<br>I | Qtr.<br>II | Qtr.<br>III | Qtr.<br>IV | Qtr.<br>I | Qtr.<br>II | Qtr.<br>III | Qtr.<br>IV | Qtr.<br>I | Qtr.<br>II | Qtr.<br>III | Qtr.<br>IV | Qtr.<br>I | Qtr.<br>II | Qtr.<br>III | Qtr.<br>IV |
| <u>Deposit Rates</u>           |           |            |             |            |           |            |             |            |           |            |             |            |           |            |             |            |
| Savings deposits               | 4.60      | 4.60       | 4.65        | 4.73       | 4.74      | 4.74       | 4.49        | 4.74       | 4.74      | 4.59       | 4.50        | 5.20       | 4.90      | 4.50       | 4.72        | 4.46       |
| Fixed deposits                 |           |            |             |            |           |            |             |            |           |            |             |            |           |            |             |            |
| Up to 3 months                 | 7.05      | 6.89       | 6.42        | 6.52       | 6.60      | 5.56       | 5.56        | 5.69       | 5.48      | 5.71       | 4.95        | 5.06       | 5.10      | 4.87       | 4.83        | 4.62       |
| Up to 6 months                 | 7.63      | 7.03       | 6.85        | 7.00       | 6.96      | 6.16       | 6.16        | 6.11       | 5.95      | 5.99       | 5.60        | 5.66       | 5.28      | 5.48       | 5.47        | 5.12       |
| Up to 12 months                | 7.90      | 7.40       | 7.25        | 7.46       | 7.21      | 6.60       | 6.60        | 6.26       | 6.20      | 6.24       | 5.88        | 6.02       | 6.03      | 5.89       | 5.71        | 5.64       |
| Over 12 months                 | 8.21      | 7.87       | 7.62        | 7.88       | 7.78      | 7.01       | 7.00        | 6.88       | 6.73      | 6.80       | 6.25        | 6.79       | 6.17      | 6.21       | 6.28        | 6.19       |
| Prime rate                     | 9.50      | 9.50       | 9.50        | 9.50       | 9.50      | 9.50       | 9.50        | 9.50       | 9.50      | 9.50       | 9.50        | 9.50       | 9.50      | 9.00       | 9.00        | 9.00       |
| <u>Mortgages</u>               |           |            |             |            |           |            |             |            |           |            |             |            |           |            |             |            |
| Residential                    | 12.07     | 12.05      | 12.20       | 12.18      | 12.16     | 12.14      | 12.13       | 12.13      | 12.13     | 12.12      | 12.04       | 11.86      | 12.05     | 11.19      | 11.80       | 11.86      |
| Commercial                     | 12.12     | 12.11      | 11.11       | 11.10      | 11.10     | 11.11      | 11.10       | 11.11      | 11.71     | 11.75      | 11.77       | 11.83      | 12.03     | 11.86      | 11.64       | 11.53      |
| <u>Consumer Loans</u>          |           |            |             |            |           |            |             |            |           |            |             |            |           |            |             |            |
| Hire-purchase                  | 17.17     | 17.17      | 17.17       | 17.17      | 17.17     | 17.17      | 17.17       | 17.67      | 17.67     | 17.67      | 17.17       | 17.17      | 17.17     | 16.72      | 16.72       | 16.72      |
| Other                          | 16.24     | 16.20      | 16.30       | 16.26      | 16.30     | 16.32      | 16.30       | 15.82      | 15.82     | 15.79      | 15.79       | 15.49      | 15.43     | 15.04      | 15.04       | 15.04      |
| <u>Other Rates</u>             |           |            |             |            |           |            |             |            |           |            |             |            |           |            |             |            |
| Treasury Bill Rate             | 6.60      | 3.55       | 4.68        | 6.85       | 6.82      | 3.07       | 3.77        | 5.39       | 4.55      | 3.28       | 3.08        | 2.93       | 3.03      | 2.19       | 2.66        | 4.14       |
| Central Bk. Rediscount Rate    | 6.56      | 4.15       | 5.18        | 7.36       | 7.32      | 4.20       | 4.27        | 5.89       | 5.05      | 3.78       | 3.58        | 3.43       | 3.80      | 2.69       | 3.16        | 4.64       |
| U.S. Dollar Rate<br>(3 months) | 5.54      | 5.86       | 5.68        | 5.25       | 5.11      | 5.56       | 6.21        | 7.11       | 7.28      | 7.84       | 8.71        | 11.08      | 10.87     | 10.62      | 11.66       | 14.70      |

SOURCE: Central Bank of The Bahamas and International Financial Statistics

TABLE IV Loans and Advances of Commercial Banks<sup>1</sup>  
(B\$ Millions)

| End of Period | In Foreign Currency | In Bahamian Dollars | T O T A L | Proportion of Foreign Currency Loans | Interest Rate Spread <sup>2</sup> |
|---------------|---------------------|---------------------|-----------|--------------------------------------|-----------------------------------|
| 1980          | 60.1                | 318.9               | 379.0     | 19.3                                 | - 6.1                             |
| 1981          | 69.7                | 366.9               | 436.2     | 16.0                                 | - 5.5                             |
| 1982          | 63.7                | 413.5               | 477.2     | 13.0                                 | - 2.1                             |
| 1983          | 58.1                | 445.4               | 503.5     | 11.5                                 | 1.4                               |
| 1984          | 60.3                | 467.2               | 527.5     | 11.4                                 | 0.3                               |
| <u>1984</u>   |                     |                     |           |                                      |                                   |
| I             | 77.0                | 432.6               | 509.6     | 15.1                                 | 1.0                               |
| II            | 60.3                | 441.6               | 501.9     | 12.0                                 | -0.4                              |
| III           | 59.5                | 454.4               | 513.9     | 11.6                                 | 0.7                               |
| IV            | 60.3                | 467.2               | 527.5     | 11.4                                 | -2.0                              |
| <u>1985</u>   |                     |                     |           |                                      |                                   |
| I             | 57.4                | 471.3               | 528.7     | 10.9                                 | -2.0                              |
| II            | 56.9                | 481.4               | 538.3     | 10.6                                 | 1.7                               |

SOURCE: Central Bank of the Bahamas and International Financial Statistics

1. See note to Table I

2. See note to Table I

TABLE V SELECTED INTEREST RATES  
(average per cent per annum)

|                              | 1980  | 1981  | 1982  | 1983  | 1984  | First Quarter |       | Second Quarter |       |
|------------------------------|-------|-------|-------|-------|-------|---------------|-------|----------------|-------|
|                              |       |       |       |       |       | 1984          | 1985  | 1984           | 1985  |
| <u>Deposit Rate</u>          |       |       |       |       |       |               |       |                |       |
| Savings Deposits             | 6.15  | 6.58  | 6.05  | 6.08  | 6.10  | 6.09          | 6.20  | 6.09           | 5.81  |
| <u>Fixed Deposits</u>        |       |       |       |       |       |               |       |                |       |
| Up to 3 months               | 7.16  | 8.21  | 7.91  | 7.90  | 7.82  | 7.86          | 7.50  | 7.68           | 6.33  |
| Up to 6 months               | 7.39  | 8.32  | 8.16  | 8.30  | 8.00  | 8.23          | 7.97  | 7.86           | 7.02  |
| Up to 12 months              | 7.62  | 8.53  | 8.38  | 8.42  | 9.19  | 8.28          | 8.04  | 8.33           | 6.98  |
| Over 12 months               | 7.79  | 8.74  | 8.54  | 8.47  | 8.38  | 8.48          | 8.21  | 8.23           | 7.86  |
| <br>                         |       |       |       |       |       |               |       |                |       |
| Prime Rate                   | 11.00 | 11.00 | 11.00 | 11.00 | 11.00 | 11.00         | 11.00 | 11.00          | 10.00 |
| <u>Mortgage</u>              |       |       |       |       |       |               |       |                |       |
| Residential                  | 12.81 | 13.11 | 13.32 | 13.36 | 13.27 | 13.27         | 13.79 | 13.27          | 13.17 |
| Commercial                   | 12.93 | 13.13 | 13.69 | 13.90 | 13.70 | 13.70         | 14.00 | 13.70          | 13.92 |
| <u>Consumer Loans</u>        |       |       |       |       |       |               |       |                |       |
| Hire-Purchase                | 17.20 | 17.43 | 17.59 | 17.99 | 18.30 | 18.38         | 17.09 | 18.54          | 16.86 |
| Other                        | 12.77 | 13.46 | 14.25 | 14.19 | 13.94 | 13.75         | 14.44 | 14.01          | 13.23 |
| <u>Other Rates</u>           |       |       |       |       |       |               |       |                |       |
| Bank Rate                    | 11.00 | 10.00 | 10.00 | 9.00  | 9.50  | 9.00          | 9.50  | 9.00           | 8.50  |
| Treasury Bill Rate           | 7.42  | 8.98  | 8.92  | 9.20  | 6.46  | 7.71          | 7.73  | 6.41           | 4.77  |
| <br>                         |       |       |       |       |       |               |       |                |       |
| Central Bank Rediscount Rate | 7.92  | 9.48  | 9.42  | 9.70  | 6.96  | 8.21          | 8.23  | 6.91           | 5.27  |
| Euro-dollar Rate (3 months)  | 13.76 | 16.51 | 13.12 | 9.57  | 10.75 | 10.03         | 9.03  | 11.35          | 8.26  |

Source: Central Bank of The Bahamas



TABLE VI SUMMARY OF COMMERCIAL BANKS' ACCOUNTS

(B\$ Million, end of period)

|   |         |         |         |         |         | Second Quarter |         |
|---|---------|---------|---------|---------|---------|----------------|---------|
|   | 1980    | 1981    | 1982    | 1983    | 1984    | 1984           | 1985    |
| <u>Net Foreign Assets</u>                               | -91.1   | -105.6  | -76.7   | -60.8   | -52.2   | -65.7          | -76.4   |
| <u>Net claims on Central Bank</u>                       | 26.3    | 12.7    | 19.1    | 41.8    | 41.6    | 58.8           | 46.0    |
| Notes and coins   | 13.8    | 13.2    | 17.5    | 15.4    | 19.2    | 10.0           | 10.0    |
| Balances  | 22.5    | 18.5    | 21.1    | 26.4    | 22.4    | 48.8           | 36.0    |
| Central Bank credit <sup>1/</sup>                       | -10.0   | -19.0   | -19.5   | -       | -       | -              | -       |
| <u>Net Domestic Assets</u>                              | 422.8   | 478.4   | 526.5   | 555.0   | 564.3   | 546.3          | 634.4   |
| <u>Net claims on Government</u>                         | 54.4    | 84.8    | 95.3    | 117.2   | 116.4   | 123.6          | 137.1   |
| Treasury bills  | 1.0     | 8.0     | 8.5     | 13.0    | 14.0    | 8.1            | 27.3    |
| Other securities  | 42.0    | 35.4    | 32.4    | 39.5    | 41.6    | 49.5           | 58.0    |
| Loans and advances                                      | 27.7    | 47.5    | 60.2    | 72.8    | 70.8    | 73.3           | 60.6    |
| Less: deposits  | -15.9   | -6.1    | -5.8    | -8.1    | -10.0   | -7.3           | -8.8    |
| <u>Net claims on public sector <sup>2/</sup></u>        | - 6.8   | -19.7   | -4.3    | -10.7   | -25.2   | -11.5          | -9.0    |
| Loans and advances                                      | 36.8    | 22.3    | 50.7    | 33.3    | 24.9    | 26.2           | 15.0    |
| Less: deposits  | -43.6   | -42.0   | -55.0   | -44.0   | 50.1    | 37.7           | 24.0    |
| <u>Net claims on other local financial institutions</u> | 1.0     | -       | -5.2    | -6.6    | -3.2    | -8.0           | -3.5    |
| <u>Credit to private sector</u>                         | 386.7   | 443.4   | 482.4   | 509.7   | 534.9   | 508.6          | 538.3   |
| Securities  | 7.7     | 6.8     | 5.2     | 6.2     | 7.4     | 6.8            | -       |
| Loans and advances <sup>3/</sup>                        | 379.0   | 436.6   | 477.2   | 503.5   | 527.5   | 501.8          | 538.3   |
| In local currency                                       | (318.9) | (366.9) | (413.5) | (445.4) | (467.2) | (441.6)        | (481.4) |
| In foreign currency                                     | (60.1)  | (69.7)  | (63.7)  | (58.1)  | (60.3)  | (60.3)         | (56.9)  |
| Private capital and surplus                             | -38.4   | -33.6   | -38.6   | -44.6   | -54.5   | -47.0          | -17.6   |
| <u>Net unclassified assets</u>                          | 11.9    | 3.5     | - 3.1   | -10.0   | - 4.1   | -19.3          | -10.9   |
| <u>Liabilities to private sector</u>                    | 358.0   | 385.5   | 468.9   | 536.0   | 553.7   | 538.2          | 603.3   |
| <u>Demand deposits</u>                                  | 103.1   | 103.5   | 117.1   | 137.2   | 137.2   | 134.4          | 147.6   |
| In local currency                                       | (92.6)  | (96.5)  | (106.1) | (123.9) | (127.0) | (123.6)        | (136.2) |
| In foreign currency                                     | (10.5)  | (7.0)   | (11.0)  | (13.3)  | (10.2)  | (10.8)         | (11.4)  |
| <u>Savings deposits</u>                                 | 94.8    | 100.7   | 109.1   | 124.1   | 145.3   | 143.0          | 159.3   |
| In local currency                                       | (94.6)  | (100.5) | (107.8) | (123.0) | (140.9) | (138.8)        | (158.9) |
| In foreign currency                                     | (0.2)   | (0.2)   | (1.3)   | (1.1)   | (4.4)   | (4.2)          | (0.4)   |
| <u>Fixed deposits</u>                                   | 160.1   | 181.3   | 242.7   | 274.7   | 271.2   | 260.8          | 296.4   |
| In local currency                                       | (152.1) | (178.9) | (213.0) | (241.8) | (250.1) | (240.1)        | (273.2) |
| In foreign currency <sup>4/</sup>                       | (8.0)   | (2.4)   | (29.7)  | (32.9)  | (21.1)  | (20.7)         | (23.2)  |

SOURCE: Central Bank of the Bahamas

<sup>1/</sup> Includes Central Bank fixed-term deposits with commercial banks.<sup>2/</sup> Includes deposits of the National Insurance Board<sup>3/</sup> Data for 1980-81 are not comparable to those for 1982-85 owing to change in reporting format effective January 1982.<sup>4/</sup> Data for 1980-81 are not comparable to those for 1982-84. Since 1982, some nonresident deposits have been reclassified as resident deposits; these included deposits held on escrow accounts for nonresident clients and bank liabilities previously held by foreign banks.

TABLE VII Commercial Banks Reserve Position

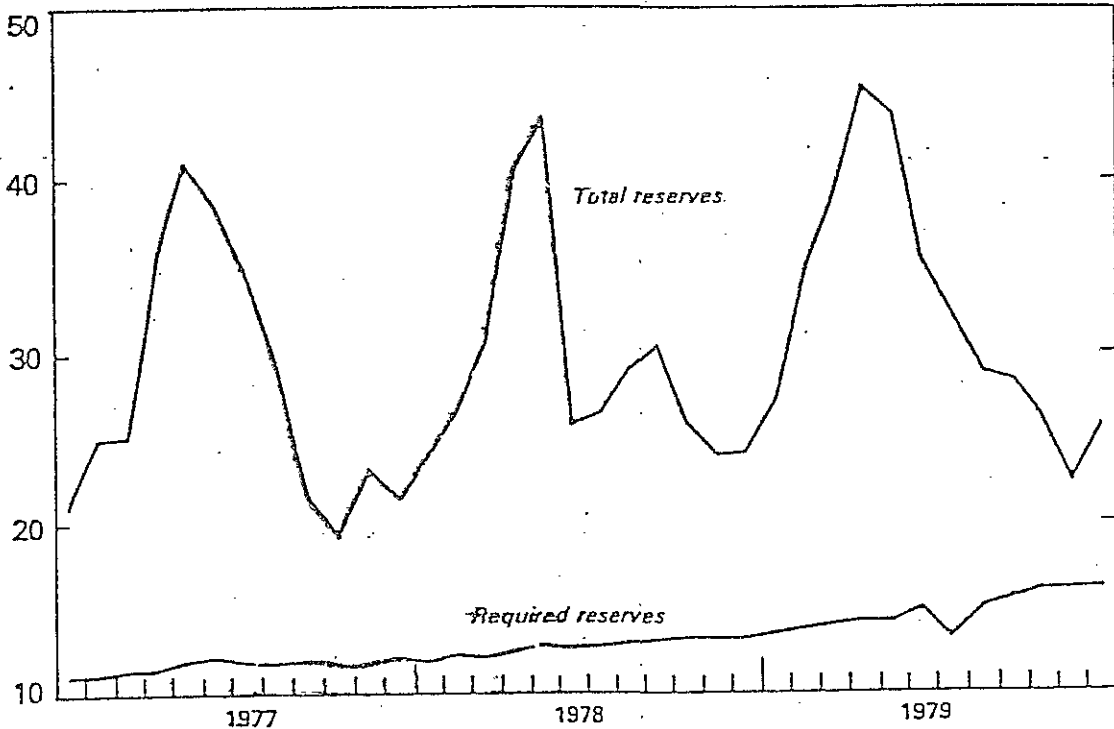
(B\$ Millions)

|   | 1981  | 1982  | 1983 | 1984 | First Quarter |      | Second Quarter |      |
|---|-------|-------|------|------|---------------|------|----------------|------|
|   |       |       |      |      | 1984          | 1985 | 1984           | 1985 |
| 1. Total Reserves                                     | 30.8  | 33.7  | 37.4 | 39.4 | 50.4          | 49.8 | 58.2           | 46.4 |
| 2. Excess Reserves                                    | 10.2  | 9.4   | 10.4 | 11.3 | 22.2          | 20.2 | 29.5           | 16.1 |
| 3. Borrowings from Central Bank                       | 19.4  | 19.5  | -    | -    | -             | -    | -              | -    |
| 4. Net Free Reserves (2-3)                            | - 8.2 | -10.1 | 10.4 | 11.3 | 22.2          | 20.2 | 29.5           | 16.1 |
| (As a percent of Bahamian Dollar Deposit Liabilities) |       |       |      |      |               |      |                |      |
| Excess Reserves                                       | 2.7   | 2.0   | 1.9  | 2.0  | 4.1           | 3.7  | 4.9            | 2.8  |
| Net Free Reserves                                     | -2.3  | -2.2  | 1.9  | 2.0  | 4.1           | 3.7  | 4.9            | 2.8  |

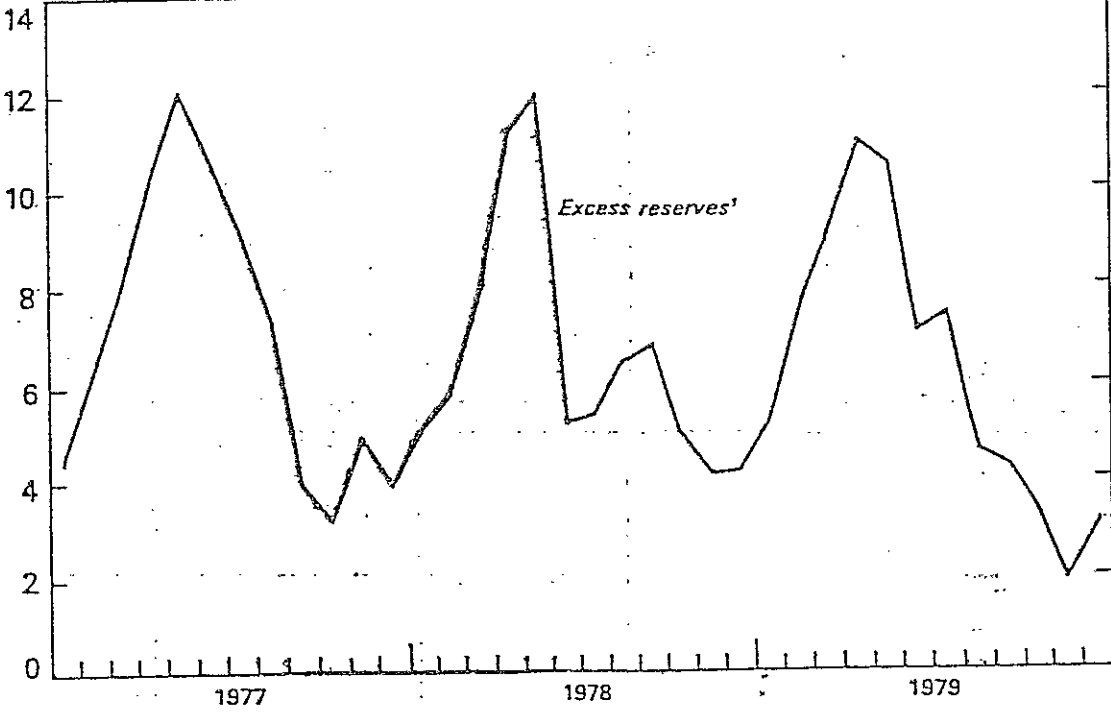
SOURCE: Central Bank of The Bahamas

# COMMERCIAL BANKS RESERVE POSITION

Millions of Bahamian dollars



Per cent

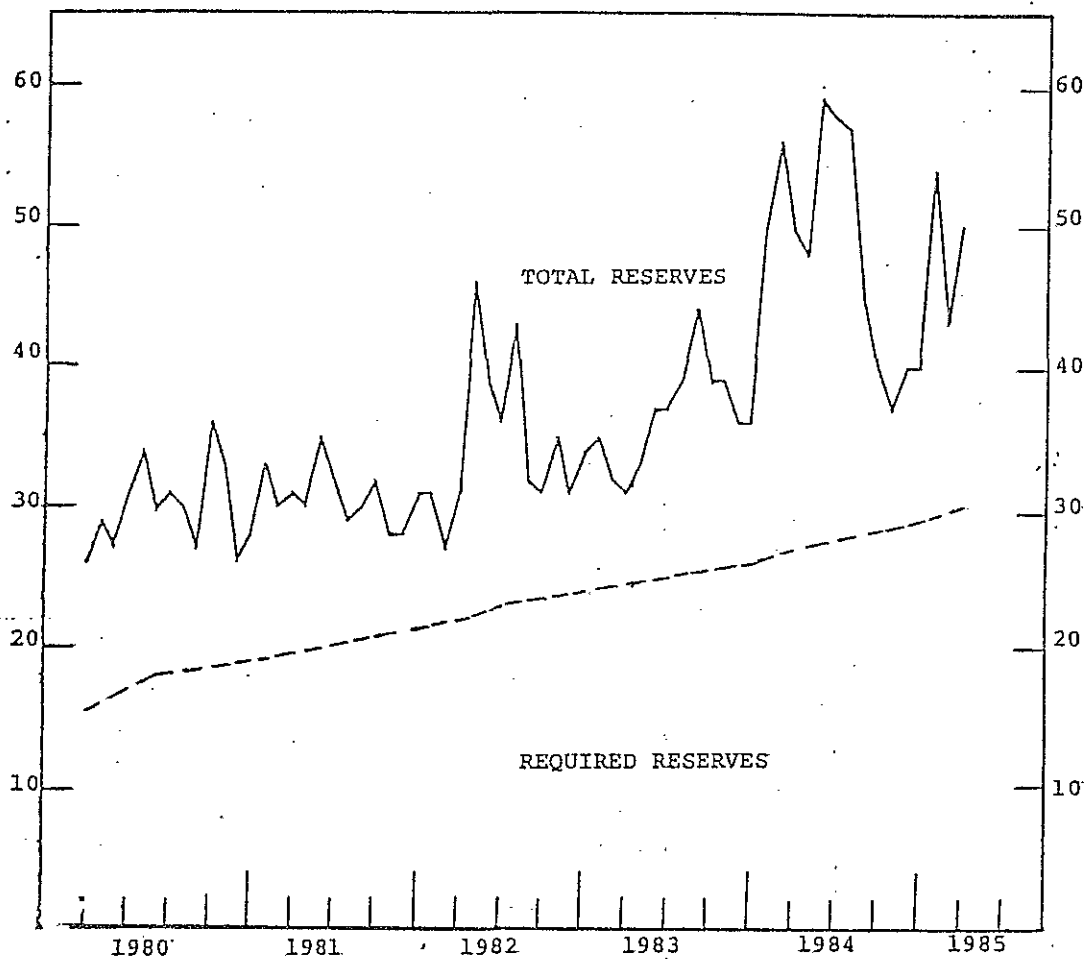


Source: Central Bank of The Bahamas.

<sup>1</sup>As per cent of Bahamian dollar deposit liabilities.

CHART II

COMMERCIAL BANKS RESERVE POSITION  
(Millions of Bahamian Dollars)



SOURCE: CENTRAL BANK OF THE BAHAMAS