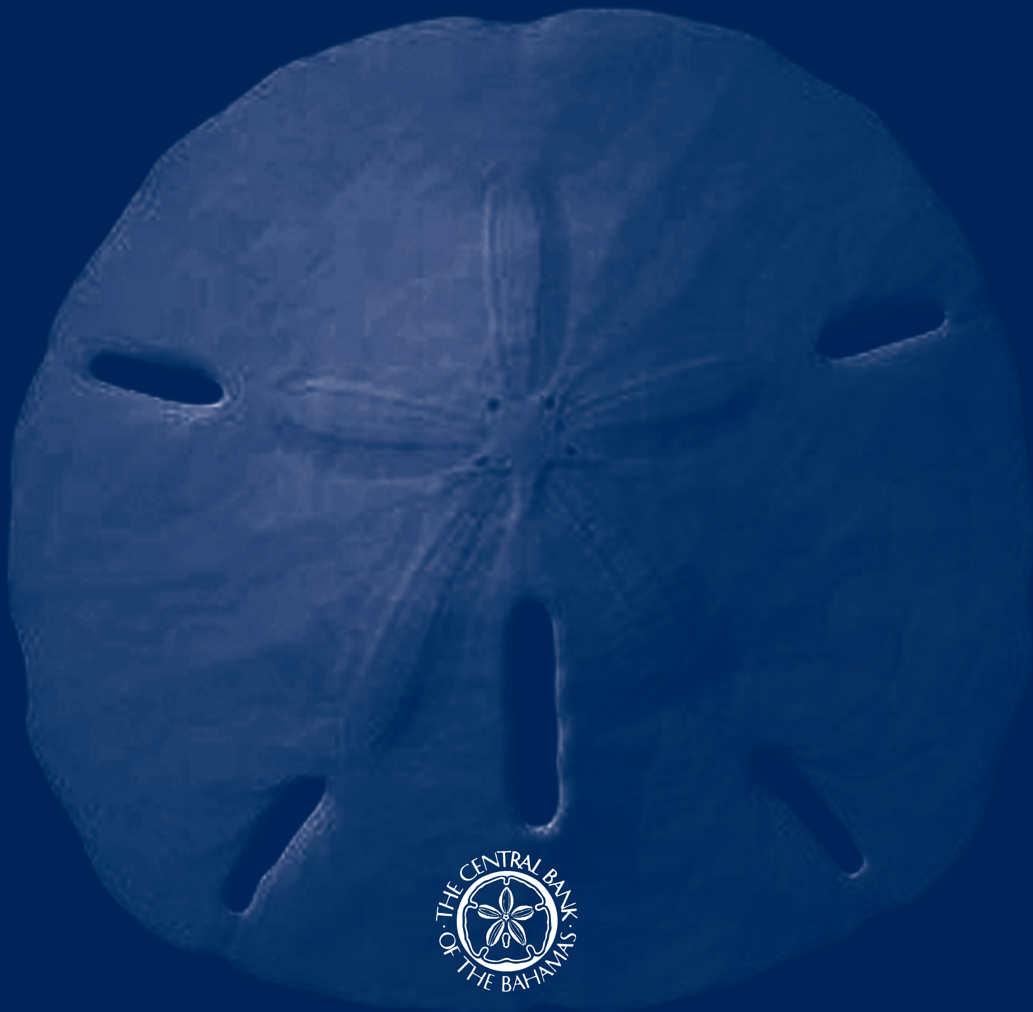
2007

The Central Bank of The Bahamas
ANNUAL REPORT
& Statement of Accounts
For The Year Ended 31 December 2007



MISSION STATEMENT

To foster an environment of monetary stability conducive to economic development, and to ensure a stable and sound financial system

DIRECTORS AND SENIOR OFFICIALS

At December 31, 2007

BOARD OF DIRECTORS

Wendy M. Craigg - Chairman

Mr Gregory Cleare

Mr Vincent Vanderpool-Wallace

Mr Michael F. Lighbourne

SENIOR OFFICIALS

Wendy M. Craigg - Governor

Michael F. Lightbourne - Deputy Governor

Bert A. Sherman - Senior Manager

Cecile M. Sherman - Manager, Banking

Sylvia L. Carey - Manager, Human Resources

Cassandra C. Nottage - Manager, Bank Supervision

Rochelle A. Deleveaux - Legal Counsel & Secretary to the Board

Gerard L. Horton - Manager, Exchange Control

John A. Rolle - Manager, Research

Keith T. Jones - Manager, Accounts

Errol L. Bodie - Manager, Information Technology

Ian B. Fernander - Manager, Administration

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16 April, 2008

Dear Prime Minister:

In accordance with Section 32(1) of the Central Bank of The Bahamas Act, 2000, I have the honour of forwarding to you, on behalf of the Board of Directors, the Annual Report of the Bank for the year 2007. Included with this Report is the Annual Statement of Accounts of the Bank for the year.

Respectfully yours,

Wendy Craigg

Wendy Craigg
Governor

The Rt. Hon. Hubert A. Ingraham
Prime Minister and Minister of Finance
Office of the Prime Minister
Sir Cecil V. Wallace-Whitfield Center
Cable Beach
Nassau, N.P., Bahamas

ECONOMIC AND MONETARY REVIEW

DOMESTIC ECONOMIC DEVELOPMENTS

Preliminary indications are that the economic growth momentum moderated in 2007, as a slowing in credit expansion and construction activity tempered the improvement in tourism output. Domestic price developments reflected the pass-through effects of higher global oil and food prices (see Table 1), while monetary conditions featured gains in bank liquidity, as a consequence of the reduced pace of credit expansion and above trend inflows in the first half of the year. For the first six months of FY2007/08, there was a deterioration in the fiscal deficit on account of higher outlays and contracted receipts. On the external front, despite deteriorations in the merchandise trade and income accounts, the estimated current account deficit improved as strengthened tourism earnings alongside higher offshore companies' local expenses and reduced outflows for construction services underpinned growth in the services account surplus. In contrast, indications are that the surplus on the capital and financial account was sharply lower, attributed primarily to a reversal in banking sector transactions to a net outflow, with a less marked reduction in private sector net inflows.

Supported by a slowdown in domestic credit growth and higher foreign inflows in the first half of the year, bank liquidity expanded by 62.3% to $190.1 million at end-December 2007, and the share of Bahamian dollar deposit liabilities rose by 1.2 percentage points to 3.6%. Average monthly liquidity firmed by 14.5% to $191.2 million, and the broader surplus liquid assets advanced by 12.4%, for a monthly average of $171.8 million. With the rise in average loan rates twice that for deposits, at 66 basis points, the weighted average interest rate spread widened by 33 basis points to 6.94 percentage points. The average 90-day Treasury bill rate also firmed by 1.79 percentage points to 2.66%; while benchmark interest rates—Central Bank's Discount Rate and the Commercial Banks' Prime—were unchanged at 5.25% and 5.50%, respectively.

TABLE 1: Selected Economic Indicators (% Change)

	2005	2006	2007
Occupied Hotel Room Nights	4.6	(1.9)	(4.4)
Total Arrivals	(4.5)	(1.0)	(2.9)
Construction Starts - Value	19.6	19.3	(31.2) *
Construction Completions - Value	16.0	12.8	3.0 *
Electricity Generation (mwh)	5.5	1.8	n/a
Retail Price Index	2.0	1.8	2.5

SOURCE: The Central Bank of The Bahamas
* YTD June 2007 vs. YTD June 2006

Buoyed by a significant build-up in residents' foreign currency deposits and increased private sector local balances, growth in money supply (M3) accelerated to 9.6% from 6.5% in 2006, placing the overall stock at $5,637.3 million. Demand deposits expanded by 2.6%, while fixed deposits and the currency component recorded extended gains of 13.1% and 10.7%, respectively. Conversely, the rate of increase for savings deposits was 4.0 percentage points lower at 4.1%.

Reflecting an abatement in consumer lending, accretions to domestic credit slowed to 10.3% from 14.3% in 2006, for an outstanding stock of $7,434.3 million. Private sector credit, which advanced by 14.4% in 2006, posted a lower gain of 9.7% as growth in housing loans, consumer credit and overdrafts slackened by 2.6, 3.7 and 39.7 percentage points to 13.7%, 10.8% and 4.5%, respectively. Accretions to banks' claims on the public sector moderated slightly to 13.2%, which was largely associated with a strengthened rise in net credit to Government of 28.0% relative to 5.4% in 2006—mainly in the form of increased holdings of Treasury bills and bonds, alongside a US$20.0 million short-term credit facility. By contrast, other public sector entities reduced their liabilities by 12.1%, following on a year-earlier sharp rise of 31.0%.

On the fiscal side, preliminary data indicated that Government's overall budget deficit for the first six months of FY2007/08 almost doubled to $99.3 million, compared to the FY2006/07 period. In the context of some slowing in the economic growth momentum, aggregate revenue receipts fell by 2.6% to $609.7 million, while total expenditure rose by 4.8% to $708.9 million. The 1.1% decline in tax receipts was primarily associated with a significant contraction in the heavily trade-weighted "miscellaneous" or unallocated receipts, which overshadowed appreciable gains in all other tax categories. Non-tax collections decreased by 16.4%, mainly on account of a timing-related decline in income from other sources. On the expenditure side, increased payments for salaries, goods & services and transfers, elevated current outlays by 6.8%; whereas capital spending contracted by 2.3%, due to declines in capital formation and transfers to non-financial public institutions.

Budgetary financing during the first six-months of FY2007/08 comprised $166.5 million in newly issued Government securities, $28.0 million in Treasury bills, a US$20.0 million short-term loan facility and $2.2 million in external funding.

For calendar year 2007, the Direct Charge on Government advanced by 10.4% to $2,630.9 million and, taking into account the 13.9% fall-off in Government's contingent liabilities, the National Debt expanded by 6.2% to $3,062.4 million at end-December, 2007.

Preliminary tourism statistics for 2007 suggested an expansion in overall output, as price improvements and gains in other hotel indicators mitigated the contraction in the number of tourists. Visitor arrivals declined by 2.9% to 4.6 million, extending the previous year's 1.0% downturn. The outcome reflected a 4.0% reduction in sea traffic to 3.1 million and a 0.4% softening in air visitors to 1.5 million. On a destination basis, visitors to New Providence weakened by 0.8%, as the 1.3% decline in sea passengers outpaced the 0.1% gain in air arrivals. In Grand Bahama, contractions in both sea (10.4%) and air visitors (5.7%) resulted in a 9.0% deterioration in overall tourists to that market. Similarly, arrivals to the Family Islands fell by 4.1%, with the 5.4% decrease in sea traffic countering the 2.2% upturn in air visitors.

Early estimates of hotel performance, obtained from a sample survey, placed revenues 8.4% higher at $403.1 million. The outcome was supported partly by the addition of new high-end hotel rooms to the outstanding stock, which elevated the average daily rate by an estimated 13.5% to $189.42 per night. A contributing factor was also the moderate firming in the average length of stay to 6.6 nights. For the New Providence market, total room revenues advanced by 11.4%, while a lower gain of 4.5% was noted for the Family Islands and a contraction of 8.3% for Grand Bahama.

Indications are that construction output moderated during 2007, as both commercial and residential mortgage lending weakened and tourism investment activity slowed in the latter half of the year. Total mortgage loan disbursements contracted by 10.5% to $544.0 million, based on reductions in both the residential (8.6%) and commercial (26.9%) components. Mortgage commitments for new construction and repairs—a leading indicator of construction activity—fell by 27.6% in number to 1,051, with a corresponding decline in value by 26.1% to $133.2 million.

Consumer price inflation, measured by changes in the average Retail Price Index, accelerated to 2.50% from 1.83% in 2006. Higher costs were registered for all categories of the Index, including a high of 5.26% for furniture & household operation, and in excess of 3.0% for food and beverages, recreation and entertainment services, transportation and communication, and medical care & health.

In the external sector, provisional data indicated an 8.9% narrowing in the current account deficit to $1,419.1 million for 2007. The outturn reflected a 24.2%

expansion in the estimated services account surplus to $1,011.9 million, buoyed by a 7.7% increase in net travel receipts, a 12.9% expansion in net receipts from offshore companies' local expenses, and a 17.8% contraction in outflows for construction services based on moderated foreign investment activity. In contrast, the deficit on the merchandise trade account expanded by 3.6% to $2,539.2 million, as accretions to both oil and non-oil imports surpassed improvements in goods sold to foreign carriers.

The capital and financial account surplus contracted by an estimated $287.1 million to $938.0 million, which was primarily associated with a $273.3 million reduction in inflows under "other" investments, as banking sector transactions were reversed, to a net outflow of $86.6 million from a net inflow of $143.1 million in 2006. Less significant were the movements in private sector transactions, with foreign direct investment inflows receding by $13.2 million to $692.6 million and other inflows, mainly in the form of loans, lower by $37.3 million at $415.7 million. The public sector registered higher net repayments of $9.9 million, compared to $3.5 million in 2006.

FISCAL OPERATIONS

FY2006/07 Performance

Preliminary data on the fiscal performance for FY2006/07 indicate a $76.4 million or 72.1% deterioration in the overall deficit to $182.5 million, which exceeded budgetary expectations by an estimated $57.2 million (45.6%). The outcome was largely associated with higher than budgeted transfers and other assistance to public sector entities, and increased outlays for education, which extended growth in total expenditure, from 9.3% in FY2005/06 to 14.6% ($193.5 million). Supported by import growth and real estate related transactions, revenue intake increased by 9.6% ($117.0 million), although considerably below the 17.5% gain in the comparable period, but just $0.5 million shy of the budget target (see Table 2).

Tax receipts, at 90.0% of total revenue, aggregated $1,205.0 million—a gain of 10.1% over FY2005/06 and 0.7% vis-à-vis the budget. Realty-related transactions contributed importantly to revenue growth. Mortgages and valuation transactions of over $250,000 elevated other "miscellaneous" stamp taxes, by 40.9% ($66.1 million), which were nearly two-thirds over the budget. In addition, a $21.2 million (62.3%) surge in commercial property tax collections underpinned a hike in property taxes of 45.1% ($24.7 million)—which was approximately 12.2% above the anticipated outcome. Although some 8.4% below budget, taxes on international trade & transactions rose by 4.4% ($28.1 million), on account of increases in import duties (4.0%) and associated stamp taxes (6.4%); whereas taxes from exports were marginally lower by 1.1% ($0.2 million). However, the overall performance of trade taxes was more improved,

TABLE 2: Government's Budget (B$'000)

	FY2004/05 Actual	FY2005/06 Actual	FY2006/07 Approved Estimates	FY2006/07 Preliminary Estimates	FY2007/08 Approved Estimates	FY2007/08 Preliminary[1] Estimates
Government Revenue	1,039,376	1,221,454	1,338,971	1,338,481	1,483,929	609,650
Government Expenditure (i+ii+iii)	1,214,903	1,327,534	1,464,321	1,520,992	1,609,289	708,939
i) Recurrent Expenditure	1,053,095	1,149,582	1,269,560	1,285,692	1,385,133	622,514
ii) Capital Expenditure	90,374	123,454	162,356	166,225	189,731	64,025
iii) Net Lending	71,434	54,498	32,405	69,075	34,425	22,400
Surplus/(Deficit)	(175,527)	(106,080)	(125,350)	(182,511)	(125,360)	(99,289)

SOURCE: Ministry of Finance
Compiled according to the IMF's Government Finance Statistics Format. [1] July - December, 2007

given the 45.4% ($6.9 million) rise in the "other tax" category, which is dominated by undistributed trade taxes. Among the remaining tax revenue items, moderate increases were registered for selected tourism services (6.3%), business and professional license (5.6%), motor vehicles (1.4%) and departure (0.6%) taxes.

Non-tax receipts grew by 6.1% ($7.7 million) to $133.6 million, which was 1.7% less than budgeted. Income from public entities and other sources was higher by 26.2% ($11.0 million) at $53.0 million—reinforced by a $25 million dividend payment from a local utility. Receipts of fines, forfeits and administrative fees declined by 2.4% to $80.1 million; and proceeds from the sale of government property lagged the previous year's level and budget estimates, by $1.3 million and $1.0 million, respectively.

On the expenditure side, recurrent outlays, which comprised 84.5% of total expenditures, rose by 11.8% to $1,285.7 million in FY2006/07, approximately 1.3% higher than budgeted. Outlays for various development contracts in the areas of environmental health, human resources and e-commerce, as well as election-related and office rental expenses, elevated purchases of goods and services by 15.7% to $270.4 million; and salary adjustments in the education and law enforcement areas underpinned a 8.6% hike in personal emoluments to $536.5 million. Transfer payments, which rose by 13.5% to $478.8 million, included a two-fold boost in the assistance to public corporations to $6.3 million and double digit gains, ranging from 11.2% to 22.5%, for all other transfers, with the exception of non-financial public enterprises which grew modestly by 0.9%. Consistent with the buildup in Bahamian dollar debt and firming in borrowing costs, interest payments advanced by 8.6% ($10.1 million).

Capital expenditures increased by 34.6% ($42.8 million) to $166.2 million, although only 2.4% higher than budgeted. Outlays for public works, inclusive of road redevelopment investments, at $53.7 million, represented a gain of 19.4%; and school repairs amplified education spending by 73.2% to $43.7 million, which represented 26.3% of total capital expenditure and exceeded the budget by 80.3%.

Financing for FY2006/07 comprised Bahamian dollar borrowings of $230.3 million, with nearly 85% ($195.3 million) secured through the sale of bonds and the remainder from Central Bank advances ($25.0 million) and Treasury bill issues ($10.0 million). In addition, external borrowings, being drawdowns on existing loans, amounted to $14.6 million. Debt repayment totaled $122.5 million, of which $91.0 million went towards Bahamian dollar obligations, $1.8 million for domestic foreign currency debt and $29.7 million for external liabilities.

2007/2008 Budget

The Budget for FY2007/08, which was approved by the House of Assembly in June 2007, emphasized the Government's commitment to strong fiscal discipline in order to achieve a recurrent budget surplus, reduce the GFS deficit-to-GDP ratio to 1.8%, and realize an improvement in the debt-to-GDP ratio to a range of 30% - 35% in five years—down from the current 38%. The Authorities also announced plans for submitting a mid-year budgetary performance review, in line with goals for improving transparency and accountability in the budgetary process.

The overall budget deficit for FY2007/08 is expected to remain relatively stable versus FY2006/07, at approximately $125.4 million, or equivalent to an estimated 1.8% of GDP. A 10.8% gain is envisaged for revenue and grants, to $1,483.9 million, while expenditures—including net lending to public corporations, are targeted to grow by 9.9% to $1,609.3 million.

On the revenue side, although no new taxes or increases in existing tax rates were proposed, additional revenue is projected to be generated from higher stamp and import tax receipts and more efficient revenue administration, which is to include ongoing rationalization of tariffs. Tax receipts are expected to advance by 13.0% to $1,351.6 million, benefiting mainly from robust growth in other "miscellaneous" stamp taxes, of 41.6% to $199.6 million, which covered anticipated increases in realty-related transactions. Similarly, taxes on property and international trade & transactions are set to strengthen by 21.0% and 11.0%, respectively, with more moderate gains for business and professional license fees (8.9%) and motor vehicle taxes (7.9%). In contrast, departure taxes are budgeted to contract by 9.9%.

The prospective yield from non-tax receipts fell by $13.9 million (10.2%) to $122.1 million, reflecting a reduction in income from other sources by 27.9% ($14.5 million), following extraordinary gains last year; and a marginal 0.3% fall-off in fines, forfeits & administrative fees. In contrast, proceeds from the sale of government property are set to firm by 61.4% to $2.2 million, and capital revenue by 54.3% to $10.0 million—the latter on account of anticipated increases in EU reimbursements.

Total expenditures are projected to rise by $145.0 million (9.9%), with current outlays, at 86.1% of the total, augmented by $115.6 million (9.1%). The latter comprised gains in personal emoluments of $33.8 million (6.1%), payments for goods and services of $31.1 million (11.3%), and subsidies & other transfers of $50.0 million (16.7%). Interest payments were relatively stable at $142.0 million, although representing a slightly reduced 10.3% of the current budget versus 11.1% a year earlier.

Budget allotments for capital expenditure were enlarged by 16.9% to $189.7 million, with provisions for capital formation and asset acquisitions rising by 12.5% and 29.5%, respectively. By functional classification, allocations for economic services are expected to advance by 3.9%, primarily due to increases in outlays for infrastructure projects. Higher provisions were also made for general public services (47.7% to $42.6 million); education (12.7% to $27.3 million); health (23.7% to $17.2 million) and defense (71.6% to $12.9 million).

First 6 months of FY2007/08

Government's budgetary operations for the first six months of FY2007/08 resulted in an almost doubling in the overall deficit, to $99.3 million vis-à-vis $50.2 million in the comparable period of FY2006/07. Reflecting the moderation in economic activity, total revenue contracted marginally by 2.6% to $609.7 million (41.1% of budget estimates), as tax and non-tax yields decreased by 1.1% and 16.4%, respectively. These trends were reinforced by a 4.8% hike in expenditures to $708.9 million, which represented 44.1% of the approved budget. Broad based growth in current spending (6.8%) overshadowed the contraction in capital outlays (2.3%).

Tax receipts, at $558.2 million (91.6% of total revenue), included a 6.4% hike in taxes on international trade & transactions to $328.8 million, although the "other tax" category, with its dominant concentration of undistributed trade taxes, registered a marked decline of 71.7% ($54.5 million) to $21.5 million. Significant contributions continued to be sourced from property taxes, which grew by 39.4% to $40.4 million; and taxes on selected tourism services strengthened by 62.1% to $17.4 million, owing to a more than two-fold gain in hotel occupancy taxes to $12.2 million. Proceeds from business and professional license taxes also expanded by 42.7% to $18.6 million, comprising higher receipts from international business companies ($2.5 million) and company fees & registrations ($1.0 million), with smaller respective gains for motor vehicle and departure taxes, of 13.0% and 2.4%.

The 16.4% reduction in non-tax revenues to $26.0 million was primarily explained by a timing-related difference in the receipt of property income, causing income from other sources to decline by 80.0% to $3.0 million. In contrast, collections of fines, forfeits & administrative fees were higher by 4.9% at $47.8 million.

Recurrent spending, which constituted 87.8% of total expenditures, was extended by $39.4 million (6.8%) to $622.5 million, led by an $11.0 million (4.2%) increase in personal emoluments and a $7.0 million (6.8%) hike in outlays for goods and services. Transfer payments were enlarged by $21.5 million (9.8%), as growth in subsidies ($14.3 million) and transfers to households ($3.0 million) overshadowed respective declines in transfers to non-profit institutions and non-financial public enterprises, of $5.5 million and $1.3 million. In addition, interest payments rose by $9.6 million (16.2%) relative to the same period a year earlier.

Capital expenditures were moderately lower by $1.5 million (2.3%) at $64.0 million, explained by decreases in capital formation (4.2%) and transfers to non-financial public enterprises (40.6%), which countered the increase in other "miscellaneous" asset acquisitions (9.5%). Net lending to public entities for budgetary support was reduced by 19.1% to $22.4 million.

Budgetary financing for the first six months of FY2007/08 comprised mainly Bahamian dollar borrowings by way of bonds ($166.5 million) and Treasury bills ($28.0 million), while external loan drawings amounted to $2.2 million. Debt repayment totaled $24.4 million, of which $21.0 million went towards retiring Bahamian dollar debt.

For calendar year 2007, the Direct Charge on Government increased by $247.2 million (10.4%) to $2,630.9 million. Bahamian dollar claims, at 89.0% of the total, rose by $247.8 million to $2,340.4 million. By creditor profile, the majority of Bahamian dollar debt was held by private institutional investors (31.5%), followed by public corporations (31.2%), commercial banks (22.3%), the Central Bank (14.9%), and Other Local Financial Institutions (0.1%).

Government's contingent liabilities contracted by 13.9% ($69.4 million) to $431.5 million at end-2007, reflecting in part refinancing and reclassification of debt by the Airport Authority ($39.8 million) as direct obligations of the Nassau Airport Development Company; and the reduction in outstanding liabilities by the Bahamas Electricity Corporation ($14.6 million). At end-2007, the National Debt, which incorporates these contingent liabilities, stood $177.8 million (6.2%) higher at $3,062.4 million—extending the comparative $147.7 million increase posted in 2006.

Table 3: Public Sector Foreign Currency Debt (B$ Millions)

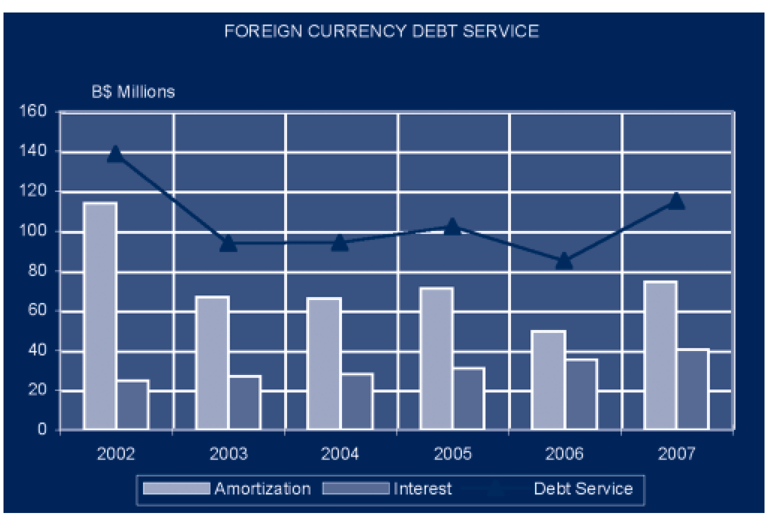
	2005p	2006p	2007p
A. EXTERNAL DEBT	337.5	334.0	324.3
i) Government	286.5	289.2	270.4
ii) Public Corporations	51.0	44.8	53.9
of which Gov't Guaranteed	50.4	44.6	38.8
B. INTERNAL F/C DEBT	215.9	299.1	314.6
i) Government	-	1.9	20.1
ii) Public Corporations	215.9	297.2	294.5
of which Gov't Guaranteed	170.8	151.8	90.8
C. TOTAL F/C DEBT	553.4	633.2	638.8
D. DEBT SERVICE RATIO	3.4	2.7	3.5

SOURCE: Treasury Accounts, Treasury Statistical Printouts and Public Corporations' Quarterly Report

Foreign Currency Debt

During 2007, public sector foreign currency debt grew by $5.7 million (0.9%) to $638.8 million at end-December (see Table 3), as the 43.1% increase in drawings to $185.0 million, slightly exceeded the three-fold rise in debt repayments—inclusive of refinancing activities—to $179.3 million. Total public corporation debt, at 54.5% of the total, rose by 1.8% ($6.3 million); whereas Government's liabilities declined marginally by 0.2%.

By creditor profile, the largest share of the foreign currency debt was held by commercial banks (50.7%), followed by private capital markets (31.3%) and multilateral institutions (16.5%). The average maturity of the debt was slightly below 11.5 years, with 97.9% of the liabilities denominated in US dollars.

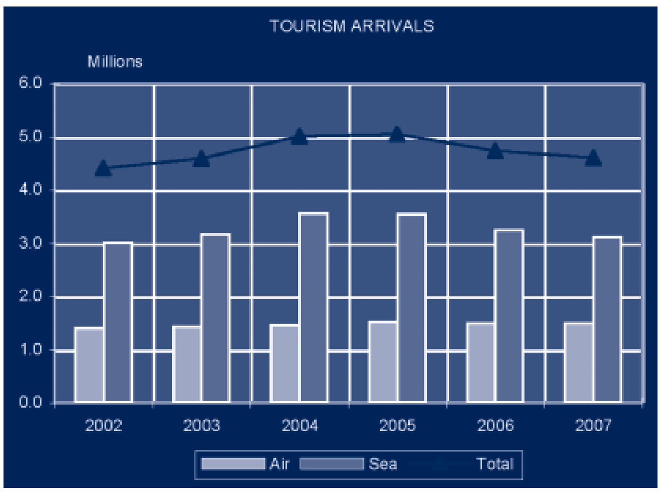


An increase in interest charges by $5.2 million (14.7%) to $40.4 million, along with the strong rise in amortization payments, boosted debt service payments to $219.7 million from $84.8 million in 2006. Consequent on higher amortization payments, the ratio of Government's foreign currency debt service to total revenue doubled to 3.8%, after stabilizing at 1.9% in the previous two years.

Tourism

Despite the negative impact of the Western Hemisphere Travel Initiative (WHTI) and weakness in key segments of the major United States market on visitor arrivals, preliminary data suggested an overall improvement in tourism output for 2007, supported by increased aggregate expenditure levels and extended length of stay indicators.

Notwithstanding signs of growth in the latter half of 2007, due in part to the adjustment of travel itineraries in the wake of Hurricane Dean, broadly sustained contractions in the first six months of the year resulted in total visitor arrivals decreasing by 2.9% to 4.6 million, compared to a 1.0% decline in 2006. Sea visitors, which account for the bulk of traffic at 67.7%, fell by 4.0% to 3.1 million; while air arrivals softened by 0.4% to 1.49 million.



Of the 1.52 million in stop-over visitors, those from the United States, at 1.26 million, represented a reduced share at 82.8%. Canadian visitors improved by 14.2%, with a corresponding gain in share of 1.2 percentage points to 6.5%. A smaller upturn of 4.1% was registered for European visitors, who accounted for a moderately higher proportion of the total at 5.6%.

TABLE 4: Change in Tourist Arrivals (%)

PORTS OF ENTRY	2005	2006	2007	2007 Market Share
Nassau/Paradise Island	(0.4)	(8.1)	(0.8)	58.9
Grand Bahama	(25.9)	(0.8)	(9.0)	12.8
Rest of Family Islands	(19.3)	17.1	(4.1)	28.3
TOTAL	**(9.7)**	**(1.0)**	**(2.9)**	**100.0**

SOURCE: The Bahamas Ministry of Tourism

By port of entry, visitors to the main New Providence market slackened by 0.8%, linked solely to a 1.3% contraction in the sea component, as air arrivals were relatively unchanged at 1.1 million. Conditions in Grand Bahama remained depressed, with the 9.0% reduction in total arrivals explained by weakness in both sea (10.4%) and air passengers (5.7%). Total visitors to the Family Islands also decreased by 4.1%, led by a 5.4% drop in sea arrivals which negated the 2.2% improvement in air visitors (see Table 4).

Despite a slight contraction in occupancy rates, preliminary data showed room revenues from the sample of large hotels for New Providence, along with a combination of large and small properties in Grand Bahama

TABLE 5: Tourism Statistics

	2005	2006	2007	% Change 2006	% Change 2007
Air Arrivals	1,514,532	1,491,633	1,486,301	(1.5)	(0.4)
Sea Arrivals	3,264,885	3,238,974	3,109,281	(0.8)	(4.0)
Total	4,779,417	4,730,607	4,595,582	(1.0)	(2.9)
Occupied Room Nights	2,270,018	2,225,939	2127490p	(1.9)	(4.4)
Hotel Occupancy	70.4%	68.4%	65.5%p	(2.2)	(2.9)
Avg. Daily Room Rate(B$)	156.56	167.00	189.20p	6.3	13.3

SOURCE: The Bahamas Ministry of Tourism
p - provisional

and the Family Islands, firming by 8.4% to $403.1 million (see Table 5). This outcome was underpinned by the launch of one high-end property during the year, along with generally appreciated average room rates for a number of entities. For the main New Providence market, total room receipts grew by an estimated 11.4%, as a 16.2% advance in average rates to $202.51 per day compensated for a 3.2 percentage point drop in occupancy levels to 73.9%. For Grand Bahama, room revenues sagged by 8.4%, reflecting a contraction in occupancy rates, from 51.7% in 2006 to 48.4%, while average daily rates declined marginally to $122.4 per night. Other indicators of activity in the sector showed mildly positive outcomes, as the average length of stay edged up, from 6.4 nights in 2006 to 6.6 nights.

Prices

Reflecting the pass-through effects of higher fuel and food costs, consumer price inflation, as measured by changes in the average Retail Price Index, increased by 2.50%, well ahead of the 1.83% for 2006 (see Table 6). The most significant price gains were noted for furniture & household operations (5.26%), recreation & entertainment services (3.78%), transport & communication (3.72%) and food & beverage (3.59%). More modest cost hikes were recorded for medical care & health, other goods and services and education, which firmed by 3.01%, 2.80% and 2.30%, respectively. Growth of less than 1% was noted for the remaining categories.

TABLE 6: Average Annual Percentage Changes in Retail Price Index, New Providence

(Oct./Nov. 1995 = 100)

Group	Weight	2005	2006	2007
Food & Beverage	138.3	3.15	4.68	3.59
Clothing & Footwear	58.9	(2.22)	1.14	0.87
Housing	328.2	2.76	1.66	0.47
Furniture & Household Operation	88.7	1.27	2.02	5.26
Medical Care & Health	44.1	3.42	1.75	3.01
Transportation & Communication	148.4	2.54	(1.97)	3.72
Recreation, Entertainment & Services	48.7	0.28	(0.15)	3.78
Education	53.1	3.33	(0.44)	2.30
Other Goods & Services	91.6	1.89	6.74	2.80
ALL ITEMS	**1,000.0**	**1.95**	**1.83**	**2.50**

SOURCE: Department of Statistics

Local automotive fuel and electricity costs also revealed the general firming in global crude oil prices. The cost of gasoline surged by 17.8% during the first half of 2007, peaking at $4.57 per gallon, before receding to $4.28 per gallon by year-end. Diesel prices in New Providence also increased steadily to a high of $3.97 per gallon in November before moving lower to $3.48 per gallon in December. After softening between January and May, by 3.1% to 9.6 cents per KWH, the fuel surcharge trended progressively higher over the remainder of the year, to approximately 13.7 cents per KWH by year-end.

Construction

Output in the construction sector continued to provide a significant stimulus to economic activity during 2007, although the momentum eased in the latter months, due primarily to the completion of a large-scale tourism investment project and softened domestic residential and commercial activity.

Partly reflecting funding constraints, amid a slowing in foreign inflows, total mortgage disbursements by banks, insurance companies and the Bahamas Mortgage Corporation fell by 10.5% to $544.0 million for 2007. Residential disbursements, which comprised 91.3% of total mortgage loans, decreased by 8.6% to $496.6 million, and commercial outlays were lower by 26.9% at $47.4 million.

The total number of mortgage commitments for new construction and repairs to existing residences, which serves as indicators of future construction activity, weakened by 27.6% to 1,051, and the value by 26.1% to $133.2 million. Residential loan commitments, at 90.2% of the total, contracted by 30.1% to $120.1 million, whereas the commercial component surged by 56.4% to $13.1 million.

Reflecting moderately tightened credit conditions in 2007, average interest rates on residential and commercial loans were higher by three (3) and one (1) basis points at 8.6% and 9.0%, respectively.

Fisheries

Preliminary data from the Department of Fisheries indicated a modest contraction in fish landings for 2007, by 27.0% in weight and 11.7% in value, to 8.1 million pounds and $80.2 million, respectively. Underlying this outturn was a reduction in both the volume and value of the crawfish catch, by 15.4% and 5.6% to 5.1 million pounds and $70.9 million. Similarly, landings of scale fish, the second largest category by weight, fell by nearly one-third in both weight and value, to 2.0 million pounds valued at $5.7 million. Conch catches were lower in weight by 56.8% at 0.8 million pounds and by 55.2% in value to $3.0 million.

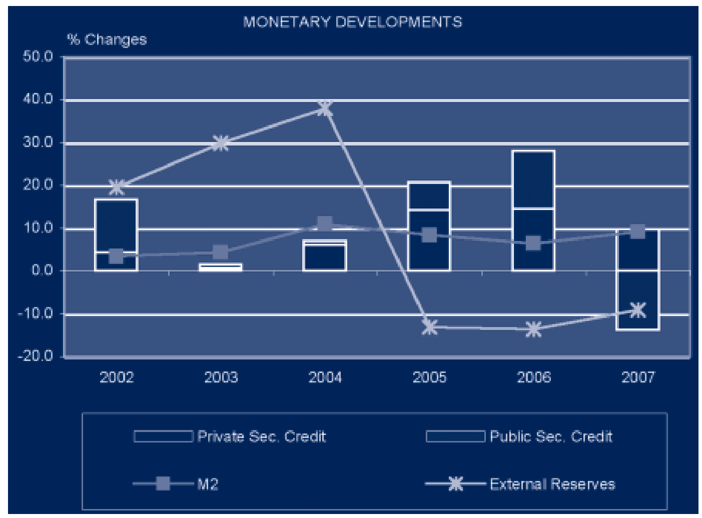
Given reductions in landings, fisheries exports for 2007 decreased by 4.3% in volume and 5.6% in value, to 5.7 million pounds and $91.1 million, respectively. Crawfish exports accounted for in excess of two-fifths of both the total weight and value, contracting by 5.3% to 4.9 million pounds valued at $86.7 million—for a drop of 6.0%. Conch meat (4.7% of total weight) increased in quantity by 7.3% to 0.3 million pounds, but fell by 0.8% in value to $1.6 million. In contrast, exports of scale fish (3.1% of the total) rose almost three-fold in volume and two-fold in value, to 0.18 million pounds and $0.4 million, respectively. Stone crab sales, at $1.5 million, were more than a third higher in both weight and value.

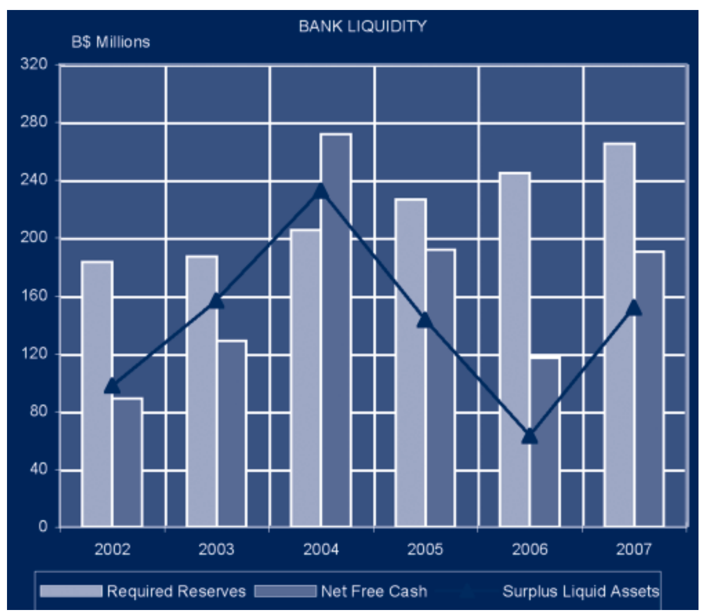
MONEY, CREDIT AND INTEREST RATES

Monetary developments during 2007 featured an improvement in overall liquidity conditions, reflecting generally favourable foreign currency inflows, linked to tourism and foreign investment activities combined with slowing, although relatively strong, credit growth. As accretions to lending costs outpaced the firming in deposit rates, the loan to deposit rate spread widened. Banks' performance indicators featured some softening in profitability during 2007, in line with the slowdown in credit growth; while a slight deterioration in asset quality indicators prompted banks to increase loan loss provisions.

Liquidity

Average monthly liquidity for 2007, as measured by banks' free cash balances, advanced by 14.5% to $191.2 million, reversing last year's 35.8% contraction to $167.0 million. The year-end position improved to $190.1 million from $117.2 million in 2006 and represented a higher share of Bahamian dollar deposit liabilities at 3.6% compared to 2.4% a year earlier. Similarly, the average monthly surplus liquid assets—a broader measure of liquidity—strengthened by 12.4% to $171.8 million, while the year-end balance more than doubled





to $151.9 million, corresponding to an expanded 17.7% of the statutory minimum vis-à-vis 7.9% in 2006. Free cash balances and surplus liquid assets attained respective peak levels in May and July, of $237.5 million and $252.0 million.

Foreign Exchange

During 2007, the Bank's net foreign currency sale declined by 29.1% to $69.0 million, benefiting from an 8.1% increase in aggregate purchases to $711.1 million, which outpaced the 3.3% rise in total sales to $780.1 million (see Table 7). Underlying this outcome were comparatively strengthened foreign currency inflows which reinforced a 28.4% hike in purchases and an 11.2% contraction in sales, for a more than three-fold boost in the net purchase from commercial banks to $189.3 million. The Bank's net sale to other customers was higher by 34.6% at $287.9 million, due mainly to elevated oil and debt payments by the public corporations. In contrast, the net purchase from Government was more than halved to $29.7 million, as sales increased by a similar magnitude to retire a US$50.0 million loan facility.

Consistent with the seasonal movements in external reserves, the first six months of the year featured the typical net purchase of foreign exchange by the Bank, although appreciably higher at $129.9 million compared with $58.2 million in 2006. For the second half of the year, the net sale expanded by 27.9% to $198.8 million, in response to increased public corporations' demands.

As a result of these transactions, the decline in external reserves moderated by $45.6 million (9.1%) to a year-end position of $454.2 million, although the average annual stock was 4.1% lower at $556.5 million. External reserves attained a comparatively higher record month-end peak of $692.4 million in May and were equivalent to an estimated 11.5 weeks of non-oil merchandise imports at end-2007, compared to 14.0 weeks at end-2006. By law, the Central Bank is required to keep, at a minimum, external reserves equivalent to 50.0% of its demand (currency and deposit) liabilities. After discounting the external balances from this amount, "useable reserves" stood lower at $104.5 million compared to $201.5 million in 2006.

Money Supply

In 2007, money supply growth intensified, amid a buildup in private sector deposits. Narrow money (M1), which accounted for 23.1% of the overall stock, rose by 3.9% to $1,300.3 million, compared with a modest 0.3% rise in 2006. Business firms and private individuals supported an expansion in demand deposits of 2.6%, in contrast to a 0.3% downturn in 2006; and the growth

TABLE 7: Central Bank Foreign Exchange Transactions (B$'000)

	Commercial Bank		Government		Other		Total		
Period	Purchases	Sales	Purchases	Sales	Purchases	Sales	Purchases	Sales	Net
Qtr.I	163,792	64,209	48,580	38,842	6,408	61,502	218,780	164,553	54,227
Qtr.II	114,180	54,676	44,480	37,151	5,204	64,625	163,864	156,452	7,412
Qtr.III	54,128	117,553	70,805	30,726	1,106	85,164	126,039	233,443	(107,404)
Qtr.IV	36,176	82,926	56,895	47,091	56,864	67,902	149,935	197,919	(47,984)
2006	**368,276**	**319,364**	**220,760**	**153,810**	**69,582**	**279,193**	**658,618**	**752,367**	**(93,749)**
Qtr.I	202,276	23,594	50,998	42,197	1,381	71,263	254,655	137,054	117,601
Qtr.II	154,302	63,686	45,425	61,281	10,509	72,894	210,236	197,861	12,375
Qtr.III	39,799	148,222	41,692	47,515	2,093	71,089	83,584	266,826	(183,242)
Qtr.IV	76,501	48,108	81,394	38,819	5,540	91,531	163,435	178,458	(15,023)
2007	**472,878**	**283,610**	**219,509**	**189,812**	**19,523**	**306,777**	**711,910**	**780,199**	**(68,289)**

SOURCE: The Central Bank of The Bahamas

in currency in active circulation accelerated to 10.7% from 3.5%.

The expansion in broad money (M2) was extended to $451.3 million (9.1%) from $299.9 million (6.4%) in 2006. Transfers to higher yielding deposits partly explained the near halving in savings growth to $38.8 million (4.1%) and the corresponding elevated gains in fixed deposits of $363.3 million (13.1%) compared to $224.9 million (8.8%) in 2006.

Reflecting an upturn in public corporations' balances, residents' foreign currency deposits rose strongly by $40.9 million (25.7%), up from $15.0 million (10.4%) in 2006. As a result, overall money (M3) growth broadened by $492.2 million (9.6%), for an end-December stock of $5,637.3 million, vis-à-vis gains of 6.5% in 2006 and 9.2% in 2005.

Bahamian dollar fixed deposits remained the largest component of the money stock (55.8%), followed by demand (19.1%) and savings (17.6%) balances. Smaller shares were accounted for by currency in circulation and residents' foreign currency deposits, of 4.0% and 3.5%, respectively. Categorized by holder, private individuals held the bulk (58.6%) of Bahamian dollar deposit liabilities; next were business firms (24.2%), the public sector (9.7%), 'others' (4.5%)—which included institutional investors—and private financial institutions (3.0%).

A further analysis of Bahamian dollar deposits by range of value and number of accounts showed that individual balances of up to $10,000 constituted some 90.3% of accounts, but only 7.7% of the aggregate value. Placements valued between $10,000 and $50,000 represented an estimated 6.7% of the accounts and 12.9% of the total value. Conversely, balances over $50,000 corresponded to a dominant 79.4% of the aggregate value, although the smallest share of the number of accounts at 3.0%.

Domestic Credit

Consequent on a slowdown in private sector credit expansion and a contraction in public corporations' net liabilities, domestic credit growth moderated to $691.4 million (10.3%) in 2007 from $843.4 million (14.3%) in 2006. The expansion in the Bahamian dollar component was only slightly lower at 13.0%, while foreign currency claims declined by 9.8%, following a 17.9% advance in 2006.

Growth in private sector credit slackened to $549.7 million (9.7%) from $715.0 million (14.4%) in 2006 (see Table 8). The sectoral distribution of credit revealed that personal loans, which constituted 74.6% of private claims, grew by 13.2% compared with 15.7% in 2006. Housing loans continued to account for the bulk of personal credit (50.5%), advancing by a reduced

TABLE 8: Flow of Credit In The Financial System (B$ Millions)

	Outstanding as at 2005	Absolute Changes 2006	Absolute Changes 2007	Outstanding as at 2007
DESTINATION				
Government (net)	642.5	34.5	189.8	866.8
Central Bank	122.0	60.5	149.8	332.3
Domestic Banks	520.5	(26.0)	40.0	534.5
Rest of Public Sector	303.3	93.9	(48.1)	349.1
Central Bank	8.3	(0.2)	(0.6)	7.5
Domestic Banks	295.0	94.1	(47.5)	341.6
Private Sector	4,953.7	715.0	549.7	6,218.4
FINANCING				
Liabilities	4,830.2	314.9	492.2	5,637.3
Currency	195.3	6.8	21.6	223.7
Demand deposits	1,167.8	14.3	45.2	1,227.3
Savings deposits	885.7	71.2	38.2	995.1
Fixed deposits	2,581.4	222.6	387.2	3,191.2
International reserves	578.8	(79.0)	(45.6)	454.2
Other net external liabilities*	(611.0)	(143.1)	86.5	(667.6)
Capital and surplus	1,302.9	179.0	175.9	1,657.8
Other (net)	265.8	(127.3)	(64.3)	74.2

SOURCE: The Central Bank of The Bahamas
* ( ) = increase

TABLE 9: Sectoral Distribution of Bank Credit (B$ Millions)

	2006		2007	
	$	%	$	%
Sector				
Agriculture	11.3	0.2	11.2	0.2
Fisheries	13.3	0.2	10.7	0.2
Mining & Quarrying	11.2	0.2	7.1	0.1
Manufacturing	51.7	0.9	52.5	0.8
Distribution	217.0	3.6	195.4	3.0
Tourism	253.7	4.2	244.8	3.7
Entertainment & Catering	59.3	1.0	47.0	0.7
Transport	22.9	0.4	24.8	0.4
Construction	412.3	6.8	460.2	7.0
Government	156.3	2.6	120.3	1.8
Rest of Public Sector	268.1	4.4	243.9	3.7
Private Financial Institutions	27.8	0.5	27.2	0.4
Professional & Other Services	156.4	2.6	149.6	2.3
Personal	4,078.0	67.2	4,618.0	70.5
Miscellaneous	332.2	5.5	340.2	5.2
TOTAL	6,071.3	100.0	6,553.0	100.0

SOURCE: The Central Bank of The Bahamas

13.7% ($281.3 million) vis-à-vis the year-earlier 16.3% ($287.8 million). Accretions to consumer credit and personal overdrafts moderated by 3.8 and 39.6 percentage points, to 10.8% ($205.3 million) and 4.5% ($3.5 million), respectively.

Consumer credit, at a relatively stable 31.5% of total Bahamian dollar credit, registered broad-based increases across all categories, with the exception of taxis and rented cars. Significant growth in net lending was noted for the miscellaneous category ($70.0 million), debt consolidation ($36.5 million) and credit cards ($30.6 million). Similarly, net credit for land purchases, private cars and home improvement firmed by $25.9 million, $19.7 million and $10.2 million, respectively, with increases of under $10 million posted for the remaining categories.

Among the other private sector components, credit expanded for construction ($47.9 million), miscellaneous ($7.9 million), transport ($1.9 million) and manufacturing ($0.9 million) (see Table 9). These contrasted with net repayments for distribution ($21.6 million), entertainment & catering ($12.3 million), tourism ($8.9 million), professional & other services ($6.8 million), mining & quarrying ($4.1 million), fisheries ($2.5 million), private financial institution ($0.5 million) and agriculture ($0.05 million).

Growth in the banking sector's net claims on the public sector narrowed by 0.4 percentage points to 13.2% ($141.7 million). A turnaround in public corporation's position to a net repayment contrasted with a sharp hike in Government's net indebtedness to the system of 28% vis-à-vis 5.4% in 2006.

Interest Rates

In interest rate developments, the weighted average spread on commercial banks' loan and deposit rates widened by 33 basis points to 6.94 percentage points in 2007, as the firming in the weighted average loan rate by 66 basis points to 10.63%, doubled the advance in the average deposit rates to 3.69%. In addition, the average 90-day Treasury bill rate advanced by 1.79 percentage points to 2.66%. However, benchmark rates—the Central Bank's Discount Rate and commercial banks' Prime—held steady at 5.25% and 5.50%, respectively.

On the lending side, average rates on overdrafts appreciated by 88 basis points to 11.44%; for consumer loans, by 74 basis points to 12.70%; commercial mortgages, by 38 basis points to 8.75% and residential mortgages, by 31 basis points to 8.16%. Regarding deposits, the average rate fell for savings by 11 basis points to 2.05%, but the rate range for fixed deposits, moved within an elevated band of 3.51% - 4.52%, vis-à-vis 3.17% - 4.18% in 2006.

Net Foreign Assets

The financial system's net foreign liabilities contracted by $40.9 million to $213.4 million in 2007 (see Table 10), in contrast to a sharp increase of $222.1 million in 2006, which was primarily associated with public sector borrowing activities. Amid debt repayments by public utilities, domestic banks' net foreign liabilities decreased by $86.5 million (11.5%) to an estimated $667.6 million. The contraction in the Central Bank's external reserves was 42.3% lower at $45.6 million (9.1%), for an end-December level of $454.2 million.

TABLE 10: Foreign Asset Position (B$'000)

	2005	2006	2007
1. THE CENTRAL BANK			
EXTERNAL RESERVES (Beginning of Year)	667,823	578,796	499,762
a. SALES TO:			
i) Commercial Banks	454,029	319,364	283,612
ii) Government	134,888	153,810	189,815
iii) Other Customers	256,036	279,193	306,637
iv) Total Sales	844,953	752,367	780,064
b. PURCHASES FROM:			
i) Commercial Banks	475,185	368,276	472,878
ii) Government	178,724	220,760	219,508
iii) Other Customers	35,057	69,582	18,717
iv)Total Purchases	688,966	658,618	711,103
c. Reserve Tranche	(775)	470	435
d. SDR Tranche	(21)	4	77
e. Other	67,756	14,241	22,922
INCREASE/(DECREASE)	(89,027)	(79,034)	(45,527)
EXTERNAL RESERVES (End of Year)	578,796	499,762	454,235
2. DOMESTIC BANKS			
NET FOREIGN ASSETS (Beginning of Year)	(563,483)	(611,037)	(754,119)
a. Foreign Exchange Transactions	(3,996)	(14,963)	975
i) Net Purchase/(Sale): Central Bank	(21,156)	(48,912)	(189,266)
ii) Net Purchase/(Sale): Other Customers	17,160	33,949	190,241
b. Changes in Local Liabilities	581,662	696,415	779,296
c. Changes in Local Assets	629,216	839,497	692,730
INCREASE/(DECREASE) (During Year)	(47,554)	(143,082)	86,566
NET FOREIGN ASSETS (End of Year)	(611,037)	(754,119)	(667,553)
3. TOTAL NET FOREIGN ASSETS (End of Year)	(32,241)	(254,357)	(213,318)

SOURCE: The Central Bank of The Bahamas

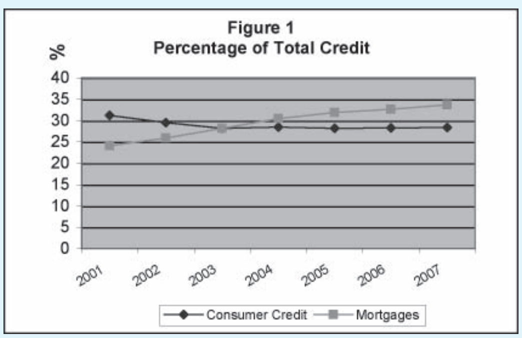
Asset Quality

Quarterly surveys indicate a modest deterioration in domestic banks' asset quality for 2007, occurring alongside slower growth in bank loans of 8.4% ($440.8 million) compared with 14.2% in 2006. Total arrears as a percentage of banks' non-Government Guaranteed loans moved higher to 9.5% from 7.7% in 2006, reflecting a significant increase in the value of outstanding loans which were 30 days past due, but had not reached the status of non-performing (over 90 days). By disaggregation, the rate of arrears for residential mortgages firmed by 3.2 percentage points to 10.4%; for commercial loans, by 1.1 percentage points to 9.2%, and for consumer loans, by 0.3 percentage points to 8.3%.

Non-performing loan facilities with 90 or more days past due payments represented a slightly higher 4.5% of the systems' loans compared to 4.2% at end-December-2006. Banks incremented their loan loss provisions by a comparatively smaller $2.5 million (2.1%) to $120.7 million at end-2007, relative to the $28.7 million rise in 2006. As a consequence, the ratio of provisions to total loans fell slightly to 2.2% from 2.3%, but narrowed as a percentage of non-performing loans, to 48.0% from 54.7% in 2006.

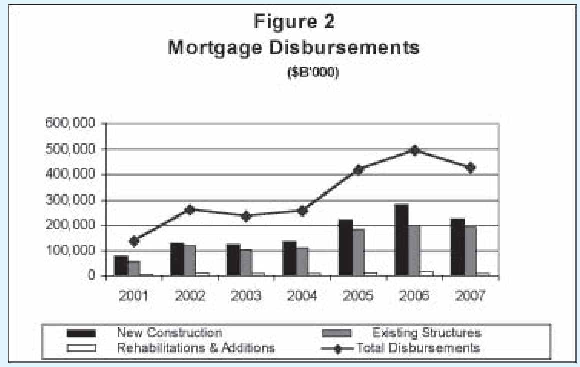
BOX 1: Trends in Commercial Bank Mortgages

Between 2001 and 2007, mortgages were the most rapidly growing component of bank credit, buoyed by relatively favourable economic conditions, increased incomes, heightened competition among commercial banks, and a stable interest rate environment. During the period in which the Central Bank's credit ceiling was in effect (September 2001 to August 2004), the value of outstanding mortgages grew at an average annual rate of 11.5% ($155.7 million) to $1,590.4 million by end-2004, surpassing the comparable 3.8% ($183.3 million) for total credit to $5,227.2 million. Following the lifting of the credit ceiling in 2004, mortgage growth accelerated to 16.3% ($303.4 million) annually, exceeding the average 10.3% ($735.7 million) increase posted for total credit. As a consequence, mortgages accounted for approximately 33.6% of total banking system loans at end-December 2007, compared to 24.1% in 2001 (see Figure 1).



The bulk of mortgage loans was for residential investments which constituted an average 90.7% of the total portfolio over the seven-year review period. Both residential and commercial segments registered strong growth, following the lifting of the credit ceiling—advancing between 2004 and 2007 by an average of 16.1% ($275.6 million) and 19.3% ($27.8 million), respectively.

Underlying these trends, annual disbursements for residential mortgages for new construction, additions and repairs rose by an average 32.4% ($21.8 million) in the four years to 2004, which was further consolidated in the three years to 2006, at a slightly higher rate of 40.7% ($61.2 million), before contracting by 20.2% ($51.4 million) in 2007. The commercial component decreased by an average 5.7% ($1.3 million) per year over the 2001 to 2004 period, but grew by an average 93.5% ($14.3 million) between 2004 and 2006, before contracting in 2007 by 21.9% ($8.9 million). Total disbursements over the last seven years amounted to $2,716.2 million and as Figure 2 shows, the majority of the outlays were channeled towards new construction (58.8% of the total). Disbursements for the acquisition of existing structures comprised the second largest category (37.5%), while allocations for rehabilitations and additions represented a much smaller share (3.7%).



Among the major domestic lenders, commercial banks provided the majority of mortgages, accounting for an average 85.2% over the seven-year period, with smaller shares held by insurance companies (9.8%) and the Bahamas Mortgage Corporation (5.0%).

Mortgage lending continued to be supported by favourable interest rate conditions and increased competition. Between 2001 and 2007, average interest rates for both commercial and residential mortgages fell by 0.12 and 0.79 percentage points, to 8.75% and 8.95%, respectively. Statistics also revealed that lending institutions have been steadily increasing the value of the loans granted as a percentage of the overall cost of the properties. For 2007, the average loan value/cost ratio for commercial loans firmed by 6.6 percentage points to 71.6%; and for residential mortgages, by 5.3 percentage points to 80.6%. Consistent with this trend, the average monthly payments on both commercial and residential mortgages expanded. In particular, commercial mortgage payments strengthened over the seven-year period by an estimated $986.7 to approximately $4,103 per month by 2007. Similarly, residential mortgage payments were higher by $146.30 at $1,295 per month.

Lending requirements and prudential norms governing access to various types of credit, including mortgages, remained unchanged during 2007. These requirements were established in conjunction with the imposition of the lending cap in 2001 and focused principally on banks' ability to assess the debt service capabilities of borrowers and to ensure that new credit will be provided only after a careful review of customers' existing levels of indebtedness, their ability to repay increased obligations and the extent to which they would be able to provide direct equity contributions to supplement existing loan financing. In this regard, the specific guidelines include: a total debt service ratio of 40%-45% of ordinary monthly income; minimum equity contributions of 15% on all personal loans, with the exception of those secured with mortgage indemnity insurance and those granted for educational and medical purposes. Dealer rebates are not counted as equity contribution for automobile loans, while the cost of insurance may be included in the loan amount, and the equity contribution must be assessed on the total loan, including insurance costs. In addition, the Bank determined that no more than 50% of tips received by service persons may be counted as income when assessing debt servicing levels.

In the wake of Hurricanes Jeanne and Francis, the Bank temporarily eased these requirements to allow greater borrowing flexibility for individuals impacted by the storms. These lending guidelines, alongside the Bank's regular monitoring of credit developments within the banking system, provide for a robust prudential environment for mortgage lending by banks.

BOX 2: Monetary Policy During 2007

The Monetary Policy Committee (MPC) was established by the incumbent Governor in 1980 to promote efficiency and transparency in the formulation and conduct of monetary policy, and to ensure a well-organized decision-making process. The MPC also formulates recommendations for the Government on fiscal and exchange control matters, and reviews supervisory issues as they impact the domestic financial system. The MPC is chaired by the Governor and its membership includes the Deputy Governor, and several department heads. While the Governor is ultimately responsible for the policies promulgated by the Bank, the Committee formally assists this process, and credibility is ensured by the consensus nature of decisions, acted upon by the Governor.

During 2007, the MPC actively monitored economic developments, along with indicators of domestic credit, liquidity and loan quality and the external reserves, to ensure that the evolution of these trends was consistent with financial sector and overall macroeconomic stability. Concomitantly, developments in the external environment—the rising cost of fuel, the US mortgage crisis, and the broader financial sector crisis, were key issues on the MPC's agenda, given the implications of higher fuel costs for domestic prices of goods and services; and the potential weakening of the US economy and global funding constraints on tourism performance and the progress of various foreign investment projects.

Under an improved external reserve performance during the first half of 2007, the Committee proceeded with the implementation of the Bahamian Depository Receipt (BDR) programme for the local broker dealers in the fourth quarter of 2007. The guidelines provided for the authorized sale of foreign currency at the official rate up to the maximum of $6.25 million per quarter. Further, in an effort to improve the efficiency of the current exchange control regime, the MPC proposed amendments to the Exchange Control regulations to allow, under delegated authority to the banks and money transmission businesses, residents' requests to transfer monetary gifts and other miscellaneous overseas payments, up to a value of $500 per transaction.

The MPC continued to liaise with the Bahamas International Securities Exchange (BISX) and the Government, in examining the implications of the proposal to transfer the secondary market for Bahamas Government Registered Stock (BGRS) to BISX. The MPC also kept abreast and, where necessary, provided input with regard to the initiative to bring Money Transmission Businesses (MTBs) under the direct supervision of the Central Bank.

In the payments arena, the Committee monitored developments by the Automated Clearing House (ACH) Task Force on the implementation of the ACH, scheduled for late-2008.

Consistent with the MPC's transparency objective, information used by the Committee in assessing the domestic economic situation and the need for change in the monetary policy stance, was disseminated to the public through the publication of its Monthly Economic and Financial Developments reports on the Bank's website.

Bank Profitability

Reflecting the build-up of deposits and slackened credit growth, bank profitability ratios moderated in the twelve-months through September 2007, the most recent period for which consolidated data are available. In particular, the net interest margin, which accelerated by 23.9% in the comparative 2006 period, grew by 9.4% to $450.3 million; however, commission and foreign exchange transactions provided an additional $7.5 million (26.7%) in income at $35.4 million, compared to a negligible rise a year earlier. Accretions to operating costs were $5.2 million lower at $14.2 million, as reductions in staff and occupancy expenses offset the growth in other "miscellaneous" operating costs. Consequently, the net earnings margin growth receded to $32.0 million (14.4%) from $60.1 million (37.0%) in 2006. "Other" income, net of depreciation and bad debt expenses declined by $0.5 million (0.9%) to $53.1 million relative to a $12.4 million (30.2%) growth in the comparative period. In this regard, depreciation costs decreased by 4.8% to $11.5 million; however, bad debt expenses were significantly higher by 49.1% at $45.0 million, as evidenced by the increase in loan-loss provisions. As a result of these developments, the net income gain was some 56.6% lower at $31.5 million.

As a percentage of average balance sheet assets, the net income ratio tapered to 3.82% from 3.90% in 2006. The gross earnings margin, the combined ratio of net interest income and commissions and fee income, narrowed by 18 basis points to 6.02%; the operating cost ratio fell by 20 basis points to 2.86%; while the contribution from other income (net of depreciation and other non-cash expenses) was lower by 9 basis points at 0.66%.

PAYMENT AND SETTLEMENT DEVELOPMENTS

Real Time Gross Settlement (RTGS) Transactions

The Bahamas Real Time Gross Settlement (RTGS) system, which was implemented in May 2004, facilitates the real time processing of high value and time critical payments between financial institutions and their customers, by mitigating the risk connected with manual or delayed payment settlement. The system facilitates, among other transactions, customer payments, inter-bank payments and cheque clearing. For 2007, the total volume of transactions from clearing banks and the Central Bank rose by 27.0% to 39,914; however, total value declined by 1.0% to $9.2 billion.

Cash

In The Bahamas, cash continued to be an essential method of making payments. Of the $333.9 million currency in circulation at end-2007, the value held in active circulation by the public rose by 10.7% to $223.7 million, but represented a relatively stable 4.1% of broad money (M2).

Cheques

Cheques have been an important payment medium in The Bahamas, particularly with the advent of cheque guarantee cards which offer some measure of security to merchants who accept this form of payment. In 2007, the total number of cheques cleared was lower by 1.5% at 3,921,951, although the value was slightly lower at $8.7 billion. In the ten years to 2007, the number of cheques cleared through the banking system rose by 10.9%.

Credit Cards

Domestic commercial banks continued to issue credit cards under the Visa and MasterCard brand names, along with the Bahamian dollar denominated card, SunCard, which was launched in 1984.

The number of cards issued over the period 2002-2007 increased by 46.2% to 135,963 in 2007, evidencing the growing popularity of this method of payment. From an outstanding level of $158.8 million in 2002, the value of credit card debt advanced by over 60% to $257.0 million at end-2007—to account for an increased 12.2% of consumer credit.

Capital Markets

During 2007, domestic capital market activity registered declines in both trading volumes and values from 2006. The volume and value of securities traded on the Bahamas International Securities Exchange (BISX) fell by 8.5% to 4.6 million and by 2.4% to $26.4 million, respectively. The benchmark BISX All Share Price Index appreciated by 23.2% to 2,066.8 points, slightly below the year-earlier growth of 24.1%. Valuation represented in the broader Fidelity Capital Market Limited's Index (Findex), which captures over-the-counter trading, grew by 26.4% to 938.3 points, down from 34.5% in 2006. However, the 24.3% gain in market capitalization on BISX to $3.9 billion exceeded the year earlier 20.8% advance.

Publicly trading companies on BISX remained at 19. Inclusive of over-the-counter instruments and mutual funds, the total number of securities listed locally increased by 1 to 29, as a result of the addition of the mutual fund, Fidelity Bahamas International Investment Fund Limited. Mutual funds now number 6, while the number of over-the-counter securities was unchanged at 4.

In other capital market developments, the BISX licensed broker dealer firms launched their Bahamian Depository Receipts (BDRs) in the final quarter of 2007. One of the firms aimed to raise total capital of $10.0 million, while the other firm's authorized capital consisted of $100,010, divided into 10,000,000 non-voting Class A common shares having a par value of $0.01 each ("Investor Shares") and 10,000 voting Class B shares having a par value of $0.001 per share (Management Shares). The funds accumulated are to be invested in foreign assets under the 2006 Exchange Control relaxation measures.[1]

INTERNATIONAL TRADE AND PAYMENTS

Preliminary data for the balance of payments in 2007 showed an improvement in the current account deficit by an estimated $137.7 million to $1,419.1 million (See Table 11). The outcome was due predominately to tourism-led gains in the services account surplus, which overshadowed deteriorations in the merchandise trade and income deficits. In contrast, the surplus on the capital and financial account receded, mainly on account of a significant reversal in commercial banks' transactions to a net outflow, and alongside a moderate reduction in "other" direct investment inflows.

Influenced by slackened growth in non-oil imports, the merchandise trade deficit rose moderately by an es-

[1] See "Relaxation of Exchange Control Restrictions on Capital Market Transactions", Central Bank of The Bahamas website: www.centralbankbahamas.com

timated 3.6% ($87.6 million) to $2,539.2 million. The slowdown in domestic demand contributed to a 16.5 percentage point moderation in non-oil import growth to 1.0% ($16.7 million). However, increased volumes combined with cost hikes underpinned a firming in the fuel import bill by 10.0% ($70.9 million). By category, the per barrel price of propane rose by 12.5% to $63.64; motor gas, by 1.4% to $90.16; aviation gas, by 13.2% to $127.60; jet fuel, by 17.6% to $101.66, bunker 'C', by 22.1% to $57.69, and gas oil, by 4.45% to $81.08. Goods procured in ports by foreign carriers expanded by 16.9% ($41.7 million).

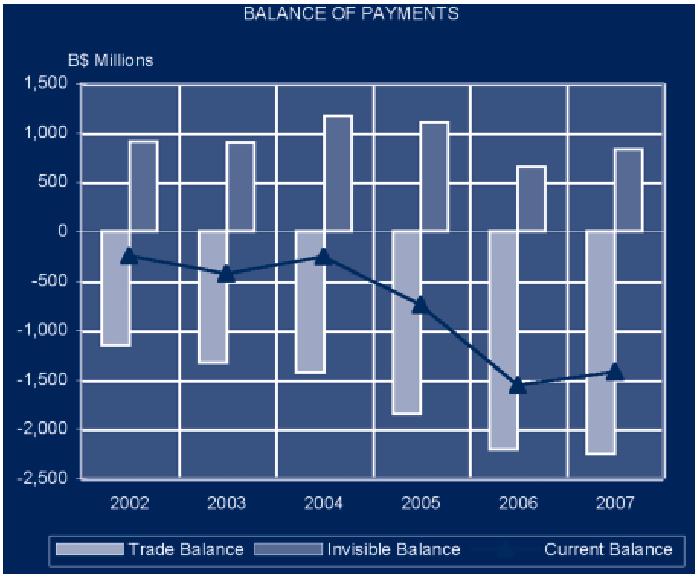
The surplus on the services account strengthened by 24.2% ($197.1 million) to $1,011.9 million, in contrast to a $406.3 million (33.3%) deterioration in 2006. Despite the fall off in total arrivals, increases in average expenditure per visit combined with lengthened average stay indicators reinforced gains in net travel receipts of 7.7% ($128.1 million) to $1,799.3 million. Reflecting the slowdown in construction activity, due in part to the completion of a major tourism project, net outflows for construction services fell by 17.8% to $176.2 million. Declines were also recorded for net insurance payments (11.6%) and Government services (34.2%); whereas revived activity in the offshore sector enlarged local spending, by 12.9% to $212.4 million. In contrast, net outflows for transportation services, other "miscellaneous" services and royalties & licence fees firmed by 5.0%, 5.9% and 11.4%, respectively.

The deficit on the income account widened by an estimated $13.2 million (6.1%) to $231.2 million, due mainly to an increase of 16.2% ($21.5 million) in dividend and interest payments. This outturn was primarily explained by a 33.9% ($43.1 million) boost in net factor outflows for non-bank private entities, as commercial bank transactions were reversed, to a net inflow of $16.3 million from a net outflow of $5.3 million in 2006. Net outward remittances of labour income fell by 8.8% ($8.1 million) to $84.7 million; while net remittances of official transactions were up marginally to $7.5 million.

TABLE 11: Balance of Payments Summary (B$ Millions)

	2005p	2006p	2007p
I) CURRENT ACCOUNT	(747.2)	(1,556.9)	(1,419.0)
i) Merchandise Trade (net)	(1,850.2)	(2,205.7)	(2,251.6)
Exports	549.0	664.9	740.3
Imports	2,399.2	2,870.6	2,991.9
ii) Services (net)	1,221.0	814.8	1,012.0
Travel	1,724.6	1,671.2	1,799.3
Transportation	(312.9)	(310.5)	(321.3)
Other	(190.7)	(545.9)	(466.0)
iii) Income (net)	(203.3)	(218.0)	(231.2)
Compensation of Employees	(73.2)	(92.8)	(84.7)
Investment Income	(130.1)	(125.2)	(146.5)
iv) Current Transfers (net)	85.3	52.0	51.8
Government	59.1	58.3	60.9
Private	26.2	(6.3)	(9.1)
II) CAPITAL AND FINANCIAL ACCOUNT	890.2	1,216.1	929.0
i) Capital Account (Transfers)	(60.4)	(63.5)	(75.7)
ii) Financial Account	950.6	1,279.6	1,004.2
1. Direct Investment	562.8	705.8	692.6
2. Portfolio Investment	—	(18.8)	(7.2)
3. Other Investment	387.8	592.6	319.3
Central Gov't Long Term Capital Flow (net)	1.2	2.7	(18.9)
Other Public Sector Capital	(9.7)	(6.2)	9.0
Banks	47.6	143.1	(86.6)
Other	348.7	453.0	415.7
III) NET ERRORS AND OMISSIONS	(232.0)	261.7	444.4
IV) CHG IN EXTERNAL RESERVES ( )=increase	89.0	79.0	45.6

SOURCE: The Central Bank of The Bahamas



Net current transfer receipts softened by $0.2 million (0.5%) to $51.8 million, following a $33.4 million contraction in 2006, which was associated with a fall off in "other sectors" transfers. Inflows attributed to the general government rose by $2.6 million to $60.9 million; however, worker remittance outflows increased by $2.8 million to $10.3 million.

Preliminary data showed a significant narrowing in the surplus on the capital and financial account, by $287.1 million to $928.9 million. Net migrant transfer outflows firmed by $12.2 million to $75.7 million. In contrast, the surplus on the financial account contracted by $274.9 million to $1,004.7 million. Other net investment inflows receded by $273.3 million to $319.3 million, as profit remittances and other repatriations led to a reversal in domestic banks' transactions, to a net outflow of $86.6 million from a net inflow of $143.1 million in 2006. The net repayment attributed to the public sector firmed by $6.4 million to $9.9 million; and "other" private sector net inflows contracted by $32.3 million to $420.7 million. Reflecting declines in net equity inflows of $115.8 million, which outpaced the $102.6 million advance in land purchases, net foreign direct investment receipts moderated by $13.2 million to $692.6 million.

After adjusting for errors and omissions and other transactions, the overall balance—as represented by the external reserves of the Central Bank—declined by $45.6 million, which was $33.4 million below the 2006 fall-off.

OUTLOOK FOR 2008

Prospects for the Bahamian economy are significantly influenced by global developments which, since August 2007, have deteriorated as the broadening effects of the US mortgage crisis precipitated a global credit crunch and dampened consumer confidence.

Generally, domestic economic conditions are expected to be relatively mild in the first half of the year, reflecting the slowing in the global economy, as well as the slackened pace of foreign direct investment activity (FDI), amid challenges imposed by the global funding constraints and housing market fall-out. With the growing weakness in the US economy which, on average, accounts for some 84% of total visitors, concerns persist about the potential adverse implications for tourism activity, in the near-term, although some mitigating effects could be derived from The Bahamas' close proximity to the US and the existing pegged exchange rate arrangement, making it a choice destination for US travelers. The outcome could also be positively influenced by the increased marketing initiatives directed towards visitors from other regions, particularly Europe and Canada, where purchasing power has improved.

However, hesitancy in FDI projects, which have boosted the growth momentum in recent years, could dampen prospects for construction activity and employment gains as well as constrain the improvement in money and credit conditions. Additional downside risks to the outlook also remain from the likely continued firming in fuel costs, with consequent implications for domestic inflation.

INTERNATIONAL ECONOMIC DEVELOPMENTS

Despite increasing headwinds originating from the United States' sub-prime mortgage crisis, global economic activity was positive for 2007. The International Monetary Fund (IMF) estimated that world output growth moderated slightly by 0.1 percentage points to 4.9% in 2007, with sound economic fundamentals in the major countries supporting improvements in labor and equity markets worldwide. However, heightened food and energy costs elevated inflationary pressures, while concerns over the weakness of the US economy led to further depreciation in the United States dollar vis-à-vis a number of major currencies. Monetary policy in the major economies during the first half of the year focused on reducing the level of monetary accommodation in order to contain inflationary pressures, following aggressive moves by several central banks to support financial markets and maintain investor confidence.

Following a weak opening quarter growth of 0.6% and then two quarters of robust real expansion averaging 4.0%, US real GDP growth slackened sharply to an annualized 0.6% in the final quarter of 2007. Consequently, the US economy posted an annual expansion of 2.2% in 2007, down from 2.9% in 2006, with the moderation attributed to reductions in residential and inventory investment, which outstripped positive contributions from increased personal consumption, exports, nonresidential building and government spending. Benefiting from improvements in investments, private consumption and the service, production and construction sectors, output growth in the United Kingdom advanced by 3.1% in 2007, up from 2.9% in 2006. Real GDP growth in the euro zone eased slightly to 2.6% in 2007 from 2.8% a year earlier, as the expansion in Germany and France softened by approximately 0.4 and 0.1 percentage points to 2.5% and 1.9%, respectively. Buoyed by business investment and export growth, economic output in Japan firmed by 1.7%. The Chinese economy expanded by a brisk 11.4% in 2007, surpassing the previous year's advance of 10.7%, and averaging 10.6% in the past five years. Strong foreign and domestic investment, net exports, industrial production and consumption expenditure continue to be the key drivers of growth.

With the exception of the United States, labor market conditions improved in several major economies, to achieve a reduction in the average jobless rate among developed countries of 0.4 percentage points to 5.1% in 2007. The United States experienced a relatively stable unemployment rate of 4.5% during the first half of the year; however, as the impact of the housing downturn spread into the broader economy, job losses in the construction and manufacturing sectors resulted in the rate of unemployment rising by 0.6 percentage points over its 2006 level to 5.0%. As favorable economic growth in the United Kingdom expanded employment opportunities in most sectors, particularly finance and business services, the jobless rate contracted to 5.2% from 5.5% in 2006. Steady economic performance within the Euro area since the upswing of 2006 also secured an improvement in the unemployment rate, by 0.6 percentage points to 7.1% in 2007. Among the main European markets, the German and French unemployment rates receded to 7.6% and 7.8%, down by 0.8 and 1.2 percentage points, respectively, from 2006. Japan's continued economic recovery contributed to a reduction in its jobless rate, to 3.8% from 4.1% in 2006. Growing external and domestic demand in China fuelled developments within the technology and manufacturing sectors, and led to a marginal 0.1 percentage point contraction in the jobless rate to 4.0%.

Price developments in most major economies mainly reflected the pass-through effects of higher global oil and food costs. In the United States, average consumer price inflation accelerated to 4.1% in 2007 from 2.5% in 2006, and was the largest annual gain since the 6.1% in 1990. However, core inflation, which strips out energy and food items, was slightly lower at 2.4% in 2007. Consumer price gains in the United Kingdom eased by 0.9 percentage points to 2.1%, as advances in food and non-alcoholic beverage costs were offset by lower average prices for gas and electricity bills. Higher average costs for food, energy, education and transportation services pushed the euro area inflation to 3.1%, up from 1.9% in 2006, with both Germany and France recording elevated inflation rates of 3.1% and 2.8%, respectively. Despite numerous attempts by China's central bank to reduce aggregate demand and curb inflation, surging prices, mainly for food and housing, resulted in average consumer price inflation accelerating by 3.3 percentage points to 4.8%. Consumer prices in Japan rose, on average, by 0.7% on a year-on-year basis, moderately lower than the 3.0% increase noted in 2006.

World commodity prices trended upwards for the sixth consecutive year, as heightened demand in rapidly growing economies, such as China and India, combined with continued depreciation in the United States dollar, resulted in appreciated prices for oil, precious metals and key non-fuel primary commodities. Since end-2006, oil prices surged by 56% to a record high of $94.92 per barrel at year-end. The advance was triggered by a combination of supply constraints caused by factors such as geopolitical tensions in the Middle East and Africa, supply disruptions, demand pressures from the fastest-growing emerging market economies, mainly China and India, and the shifting of investors' assets into oil futures. As high oil prices sparked interest in alternative grain-based energy sources, the underlying demand for grains sparked an appreciation in the average annual price of corn and wheat, by 34.3% and 32.9%, respectively. Uncertainty in the global financial markets also prompted investors to increase their demand for relatively safe assets, causing the price of gold and silver to escalate by 31.0% and 14.7%, to highs of $833.92 and $14.80 per troy ounce, respectively.

Monetary policy measures by major central banks shifted from a bias toward focusing on inflation pressures in the first half of 2007, to concerns about increasing downside risks to economic growth. To address the tightening of the global credit markets, as the financial sector restricted lending in the face of the spill-over effects of the housing crisis in the United States, central banks pursued a coordinated effort to ensure sufficient liquidity was available to financial institutions through year end. Apart from providing credit to the market, the Federal Reserve responded by cutting its discount rate by 50 basis points in August and both the key federal fund and the discount rate by 1 percentage point each in the final four months, to year-end rates of 4.25% and 4.75%, respectively. To combat inflationary concerns, the Bank of England raised its key bank rate by a total of 75 basis points during the first three quarters to 5.75%. However, as concerns emerged regarding the weakness of the economy, the Bank trimmed its policy rate in the fourth quarter by 25 basis points to 5.50%. A similar pattern was observed for the European Central Bank (ECB), which raised its key interest rates by a total of 50 basis points over the first six-months, to tackle rising inflation, although leaving rates unchanged for the remainder of the year. Facing relatively benign inflation, the Bank of Japan increased both the overnight call rate and complimentary lending facility on one occasion by 0.25 percentage points to 0.50% and 0.75%, respectively, but left key rates unchanged for the balance of the year—reinforcing the cautiously optimistic outlook for the economy. Citing concerns that the economy was overheating, the Peoples Bank of China adopted an aggressive tightening stance in order to contain inflationary pressures. Through six separate rate increases, the Bank raised the benchmark one-year deposit rate from 2.52% to 4.14% and the lending rate from 6.12% to 7.47%. The reserve requirement ratio on deposit institutions was also adjusted upward by 5.5 percentage points to 14.50% and the ratio on foreign currency deposits, by 1 percentage point to 5.00%.

Currency developments in 2007 featured the continued depreciation of the United States' dollar against other major currencies, as markets responded to concerns over the US sub-prime mortgage crisis. The dollar recorded its most significant depreciation against the Euro, weakening by 9.2% to €0.69, as the differential between US and euro zone interest rates narrowed and favorable economic conditions in the major European countries fuelled investments. Similarly, the dollar lost 7.01% against the Swiss Franc to CHF1.13. Amid mounting pressure in the United States for the Chinese authorities to revalue their currency, the Yuan appreciated by 6.51% versus the dollar during the year. With interest rates in Japan remaining the lowest among developed countries, the dollar strengthened vis-à-vis the yen by 3.45% for the first half of the year; however, during the final months of 2007, downward pressure on the dollar, stemming from the uncertainty over the outlook for the US economy, resulted in a 6.18% depreciation to ¥111.71 over the entire year. As the Bank of England continued to tighten monetary policy over the course of 2007, the pound sterling strengthened by 1.96% against the dollar to £0.50 per dollar.

Equity markets globally experienced significant volatility during most of 2007, as investors grappled with weakness in the housing industry, concerns over financial companies, and the possibility of a weaker economy. Strong global economic growth and corporate earnings, contributed to stable markets during the first half of 2007, a scenario which came to an abrupt end in August, as concerns over the extent of the economic and financial fallout arising from the US sub-prime mortgage and liquidity crises began to weigh on the markets, which registered significant corrections in the fourth quarter. However, on balance, 2007 was yet another year of positive performances. The Morgan Stanley All Country World Index, which is a measure of global trends, ended the year up 4.5% to 207.52 points. In the United States, the Dow Jones Industrial Average (DJIA), which hit several record highs and peaked at 14,164 on 9 October, gained 6.4% to close at 13,264.8 points; and the S&P 500 index finished the year up 5.5% at 1,468.36 points. Strong rallies in European equity markets during the first half of 2007 tightened since the credit crunch, with Germany's DAX still returning 22.3% to close at 8,067.32 points. The United Kingdom's FTSE 100 also moved higher by 3.8% to 6,456.90 points and France's CAC 40, by 1.3% to 5,614.08 points. Japan's NIKKEI 225 fell 1.1% to 16,111.43 points, whereas China's Shanghai SE Composite index was up a remarkable 96.7% to close at 5,261.56 points.

As export growth trended upward in most developed countries, trade balances generally improved. In the United States, despite the surge in oil imports, the declining value of the dollar improved the competitiveness of American goods and services, boosting exports and narrowing the US' goods and services deficit by 6.2% from 2006, to $711.6 billion for the twelve-months to December 2007. For the United Kingdom, the decline in the service account surplus contributed to a widening in the trade deficit, to £51.0 billion from £46.4 billion in 2006. The Euro area registered an external trade surplus of €23.0 billion in 2007, a reversal from the previous year's deficit of €14.4 billion. Buoyed by a 31% increase in the merchandise trade balance, the goods and services surplus of Japan increased by 37.2% to ¥100.8 trillion; and China's trade surplus expanded by approximately 48% to $262.2 billion, on account of robust export growth.

The 16th meeting of the International Monetary and Financial Committee (IMFC) of the Board of Governors of the International Monetary Fund was held on 20, October, 2007 in Washington, D.C. Among other issues discussed, the members noted the strength of major economies and robust growth in emerging markets; however, they acknowledged the build up in inflationary pressures, and financial market turmoil, which substantially increased the downside risks to the short to medium term global economic outlook.

OPERATIONS

BANKING

Currency Operations

The Central Bank of The Bahamas, through the Currency Division of the Banking Department, has responsibility for all aspects of currency management—including the design, minting and printing of currency necessary to maintain adequate stocks. The Bank also has responsibility for the issuance and redemption of all Bahamas banknotes and coins. An important aspect of the Division's daily efforts involves examining the quality of the currency returned to the Bank, to determine whether it should be reissued or destroyed, and recording all movements of currency into and out of circulation.

At the close of 2007, Bahamas currency in circulation totaled approximately $333.9 million, a 4.9% increase over 2006. Bahamas banknotes are issued in denominations of $0.50, $1, $3, $5, $10, $20, $50 and $100, with a circulation value of $317.1 million at end-December, 2007. Coins in circulation stood at approximately $16.8 million, for a gain of 4.4%.

Currency in Circulation (B$ Millions)

	2006	2007	% Change
Notes	$302.4	$317.1	4.86
Coins	$16.0	$16.8	4.35
Total	$318.4	$333.9	4.87

As part of its continued effort to upgrade the security of Bahamas banknotes, in December 2007 the Bank introduced the newly designed $5 banknote, the fourth denomination in the CRISP (Counterfeit Resistant Integrated Security Product) family of banknotes. The Bank plans to phase into circulation other denominations in the coming years, with the CRISP $1 banknote planned for 2008.

In addition to the new banknotes, the Bank's redesign of the coin family continued with the release of a new 10¢ coin in September. A redesigned 25¢ cent coin is scheduled for release in mid-2008.

Foreign Exchange Transactions

The Central Bank's buying and selling rates for U.S. dollars from/to commercial banks were unchanged at US$1.00 = B$1.00 and US$1.00 = B$1.0025, respectively, and at par for cash transactions. Foreign exchange rates for the quotation of Pound Sterling were obtained each business day from the international market at 9:00 a.m. and 11:30 a.m. and at other appropriate intervals, depending on the dollar value of transactions and market volatility. For Pound Sterling sales, the Central Bank maintained the policy of adding a commission of one half of one percent to the mid-rate.

The highest and lowest Pound Sterling/Bahamian dollar rates employed by the Central Bank during 2007 were as follows:-

	Buying	Selling	Date Employed
Highest	2.1053	2.1158	November 7, 2007
Lowest	1.9218	1.9314	March 5, 2007

Relations with Public Sector

As the official registrar and transfer agent for Government debt, the Bank executed functions related to overseeing and facilitating the issuance, redemption and servicing of Registered Stocks and Treasury bills, along-

Table 12: Bahamas Government Treasury Bills (B$ Millions)			
	2005	2006	2007
Bills Outstanding (End of Yr)	**192.5**	**192.5**	**230.5**
Average Price			
Tender Rate (%)	99.85	98.81	98.81
Discount Rate (%)	0.35	3.00	3.04
Re-discount Rate (%)	0.85	3.50	3.54

Source: The Central Bank of The Bahamas

side debt securities issued by the Bahamas Development Bank, Bahamas Mortgage Corporation, the Clifton Heritage Authority and the Bridge Authority.

For Treasury bills, the statutory ceiling on the maximum amount Government is permitted to borrow remained capped at 25 percent of the lesser of ordinary revenues, as provided in the most recent approved budgetary estimates, or the average revenue of the latest three years of audited accounts which have been tabled in Parliament. The issuance of an additional $38.0 million in Treasury bills (see Table 12) increased the undiscounted outstanding stock to $230.5 million for 2007, being held by the Central Bank (62.7%), commercial banks (22.1%) and public corporations (15.2%). Rediscounts totaled $77.4 million from commercial banks and from public corporations, $10.0 million. As regards prices, the tender rate was stable at 98.81% and the average discount rate was 4 basis points higher at 3.04% at end-December 2007.

Table 13: Bahamas Government Registered Stocks (B$ Millions)		
	2006	2007
Outstanding (Beginning of year)	**1,669.0**	**1,829.9**
Add: New Issues	226.6	261.8
Less: Maturities	65.7	60.0
Outstanding (End of year)	**1,829.9**	**2,031.7**
Interest Yield		
Variable Rates (Prime + Add-On)		
Prime	5.50%	5.50%
Add-On	0.03125% - 1.25%	0.03125% - 1.25%
Fixed Rates	5.75% - 9.00%	5.75% - 9.00%
Maturity Range	2007 - 2026	2008 - 2037

Source: The Central Bank of The Bahamas

During 2007, the value of Bahamas Government Registered Stocks outstanding rose by 11.0% to $2,031.7 million (see Table 13). Five bond issues, totaling $261.8 million, were arranged by the Bank; and scheduled redemptions aggregated $60.0 million. New issues featured a maximum maturity limit of 30 years, and stable effective coupon rates at a spread of 0.03125% to 1.25% above commercial banks' Prime rate.

The value of outstanding Bridge Authority bonds was unchanged at $28.0 million, bearing maturities ranging from 2014 - 2029 and variable yields of Prime plus a margin of 1.000% - 1.625% per annum. Clifton Heritage Authority bonds at $24.0 million, carry maturities spanning the years 2020 - 2035; and variable yields over Prime of 0.250% - 0.750% per annum.

Relations with Banks

In accordance with Section 19 of the Central Bank of The Bahamas Act 2000, banks are required to maintain "Statutory Reserves" against their Bahamian dollar deposit liabilities. Since established in 1974, the reserve ratio has remained at 5.0%, with a minimum 80% to be held in deposit balances at the Central Bank. In line with accretions to the Bahamian dollar deposit base, required reserves increased by 8.1% to $216.6 million at end-2007. Banks' excess balances, at $145.3 million, represented nearly 43.0% of their total deposits held with the Central Bank—exceeding the 26.0% for 2006. Banks also held balances at the Central Bank to facilitate cheque clearing arrangements, which continue to be managed by the Central Bank. Following a 0.9% hike in 2006, the volume of cheques processed in 2007 declined by 1.5% to 3.9 million, with a 0.2% decrease in the associated value to $8,697.0 million. The Bank continued to use the Society Worldwide Interbank Financial Telecommunication (SWIFT) network to transmit high speed secured messages relative to international transfer of funds.

Payment Systems

Plans toward the creation of an Automated Clearing House (ACH) continued during the year, with pilot testing and implementation expected by the fourth quarter of 2008. This electronic facility, to automate clearing of low-value payments, including cheques and direct debits, will provide improved efficiency in the local banking system through a less costly and more timely settlement process.

The Central Bank worked closely with the Clearing Banks Association (CBA) to ensure a smooth implementation of the system and its interface with the Bank's Bahamas Inter-bank Settlement System (BISS), which is required for final, irrevocable settlement.

Investment Currency Market (ICM)

The Banking Department facilitated operations under the ICM, a mechanism which provides residents with investment dollars for acquiring overseas assets, such as shares/securities and real estate. Since 16 January 2006, the premium bid and offer rates were reduced to 10.0% and 12.5%, respectively.

Despite a reduction in the rate, ICM activity was relatively moderate during 2007. From a revised opening balance of $6,083,593.73, the ICM recorded sales of $47,427.68 and purchases of $11,083.40, to end the year at $6,032,249.45.

EXCHANGE CONTROL

During 2007, the Exchange Control Department continued to monitor the impact of the liberalization measures enacted in the first quarter of 2006. Notable among the measures coming on-stream was the non-sponsored Bahamian Depository Receipt (BDR) Investment Program, under which residents are permitted to participate, via local BISX licensed broker/dealers, in foreign capital markets by purchasing foreign security-backed instruments. Activity in the BDR program commenced in the fourth quarter of 2007, with the participation of two licensed broker/dealers, each of whom received their allotment of foreign exchange from the Central Bank under the program's guidelines totaling $4.166 million. The National Insurance Board also made outward investments under the liberalization programme of $9.375 million during the year.

The Department monitored the demand for foreign exchange by the general public, which was particularly robust with regard to oil payments, and sought to identify areas for further liberalization. In the context of the latter, the Department proposed for consideration in December, a further delegation of authority to commercial banks and money transfer service providers of a new limit of $500.00 for cash gift and small miscellaneous purchases. There is currently no delegation of gift payments.

The Department focused on a number of initiatives aimed at improving operational efficiency through automation of work processes. Ongoing enhancements to the Lotus Notes Correspondence Tracking System will facilitate data processing, storage, report generation and retrieval activities across the Department's functions. Progress was also made towards automating the capture and compilation of various statistical information collected by the Department, including activity on business and client foreign currency accounts, and foreign investment flows. The Department, in collaboration with the commercial banks, commenced a review of processes and the E1 Forms banks currently use when servicing customers under delegated authority, with a view to determining changes that would provide greater ease for the institutions, their clients, and the Central Bank.

The Department also worked closely with commercial banks in rationalizing the rules governing the operation of debit card programs. Three additional institutions were granted approval to market pre-paid debit cards, bringing the total number of banks providing this service to five (5). The Central Bank increased the cash withdrawal limit on debit cards, from $500.00 per day to $1,000.00 per day, which resulted in a significant rise in reported usage for these cards.

At end-2007, the number of Authorized Dealers (commercial banks) and Authorized Agents operating domestically stood at eight (8) and fifteen (15), respectively.[2]

[2] See the Central Bank's website, www.centralbankbahamas.com for list of Authorized Dealers and Authorized Agents

RESEARCH

During 2007, the Research Department performed its critical role of data collection, and analysis to meet the needs of internal and external stakeholders. Its dissemination objective was achieved primarily through the key publications produced by the Bank, namely, the Quarterly Statistical Digest, which featured detailed statistics on money and banking, fiscal, balance of payments and real sector developments, and the economic analysis and various survey results covered in the Monthly Economic and Financial Developments Reports, the Quarterly Economic Reviews and the Annual Report. The Department completed and presented a number of papers and briefs, both domestically at the MPC and Roundtable meetings, and abroad at various international and regional fora. In addition, the Department produced its inaugural edition of the Working Paper Series for 2006, and conducted a number of training initiatives to ensure that employees effectively executed the mandate of the Department.

Economic research efforts involved the production of a number of papers which reflected research interests of staff, along with the policy needs of the MPC. In particular, two articles entitled; 'Does Capital Account Liberalization Make Caribbean Economies More or Less Susceptible to Sudden Stops' and 'Fiscal Discipline in the Achievement of Fiscal and Debt Sustainability and Growth in The Bahamas', were presented at the 39th Annual Caribbean Centre for Monetary Studies Conference held in Belize. Other papers were presented at the Department's Quarterly Roundtable forum and addressed topics such as trends in remittances in The Bahamas, the case for the use of indirect monetary policy instruments, the net worth approach to fiscal policy and an examination of the proposed National Health Insurance Scheme.

The Department facilitated two technical assistance missions during the course of the year. The first mission, conducted by a World Bank consultant, examined the feasibility of the Government's proposal to migrate the secondary market for Government Securities from the Central Bank to BISX. The second, an IMF technical assistance mission, analysed the opportunities for the use of indirect monetary policy instruments in The Bahamas, and provided a capacity building module for relevant staff of the Bank.

During the year, staff attended various in-house and external training programs to enhance their knowledge of economic matters, including survey writing and econometric workshops, and courses in Government Finance Statistics, Debt, Balance of Payments and Financial Programming.

In the coming year, the Department will continue to play a leadership role in the assessment process for the implementation of the Online Reporting System (see Information Technology). In addition, further focus will be given to building capacity in forecasting techniques, broadening the level of research and analysis on domestic developments, and enhancing the information being disseminated to the public.

BANK SUPERVISION

During 2007, the Bank Supervision Department focused on the following issues and projects, in addition to fulfilling its mandate with respect to regulation and supervision of bank and trust licensees.

- Progressing with the preparatory work required for the eventual implementation of the Market Risk Guidelines and Basel II requirements.
- Conducting consultative exercises with industry participants in policy initiatives.
- Assessing and confirming the overall safety and soundness of licensees through off-site analysis and focused onsite examinations.
- Maintenance of regular contact and interaction with directors and management of each licensee.
- Regular monitoring and review of licensees, through analysis of prudential and published reports; fit and proper reviews of proposed directors, executive officers and senior management of licensees; and processing significant changes to licensees' arrangements.
- Updating and amending the regulatory framework and the Department's supervisory processes and procedures.
- Ongoing training and development of the staff in the areas of risk-based supervision and related topics.

Domestic and international cooperation with other regulatory bodies remained an important feature of

TABLE 14: Banks and Trust Companies Licensed in The Bahamas

	PUBLIC			RESTRICTED			NON-ACTIVE			
	B&T	B	T	B&T	B (Nom)		B&T	B	T	TOTAL
December 2006	81	43	19	4	3	86	5	4	3	248
Add Licenses issued in 2007	0	1	0	0	0	4	0	0	0	5
Less Licenses revoked in 2007	3	2	0	1	0	2	0	0	0	8
Sub Totals	78	42	19	3	3	88	5	4	3	245
Licenses upgraded or downgraded	1	-1	-1	0	0	1	0	0	0	0
December 2007	79	41	18	3	3	89	5	4	3	245

B=Bank, T=Trust, T(Nom)=Nominee Trust

Note: Gross License Fees during 2007 amounted to approximately $11.24 million.

Source: The Central Bank of The Bahamas

the Department's work programme. On the local level, cooperation was accomplished through the Group of Financial Sector Regulators (GFSR), which comprises the six domestic agencies that perform regulatory functions with respect to bank and trust companies, securities firms, a domestic securities exchange, insurance companies, credit unions and financial & corporate service providers. International cooperation was also facilitated through the Bank's representation on relevant regional and international bodies and various international fora.

Licensing Activity and Physical Presence Policy

During 2007, the number of bank and trust licences was reduced by three (3) to 245 (see Table 14).

The Governor granted five (5) new licences and revoked eight (8). Of the 245 licensees, 214 operated through physical presence, one fewer than in 2006. Thirty-one (31) or two (2) less licences, of predominantly G-8 branches, maintained restrictive management arrangements approved by the Central Bank, and as permissible under international best practices in banking supervision promulgated by the Basle Committee.

Private Trust Companies

Under the framework for the approval of Registered Representatives of Private Trust Companies (PTCs), a Registered Representative is either (i) a licensee of the Central Bank or (ii) a Financial and Corporate Service Provider (duly licensed under the Financial and Corporate Services Providers Act, 2000 ("the FCSPA") whose business is limited to acting as a Registered Representative and who has been approved by the Governor to provide services to PTCs pursuant to Section 3 of the Banks and Trust Companies Regulation Act, 2000 (as amended by the Banks and Trust Companies Regulations (Amendment) Act, 2006.

During 2007, five (5) licensees advised the Governor of their intention to act as Registered Representatives of PTCs. The Governor approved two (2) Financial and Corporate Services Providers to act as Registered Representatives and seven (7) Private Trust Companies were certified by the Central Bank as qualifying for an exemption from having to obtain a trust licence pursuant to the Banks and Trust Companies Regulation Act, 2000.

TABLE 15: Onsite Examinations Conducted (2005-2007)

	2005	2006	2007
Examinations			
Domestic Licensees	4	2	3
Other Licensees	28	29	75
Follow-up /Special focus	7	7	2
Total	**35**	**36**	**77**
Reports			
Finalized Reports	41	40	41
Reports in Progress	4	2	5
Total	**45**	**42**	**46**
Follow-up Examinations Required	3	0	0

Source: The Central Bank of The Bahamas

On-site Examinations

Examinations conducted during 2007 focused primarily on licensees' safety and soundness, and also closely scrutinized licensees having restrictions placed on their business activity, e.g. restricted trust licences that confine mandates to a very limited number of client relationships or where the principal purpose is to provide shareholders or directors to corporate entities administered by those licensees.

In general, safety and soundness examinations confirmed an overall improvement in licensees' systems and controls, and timely implementation of corrective actions to address findings and recommendations of previous examinations.

The Bank's efforts to better coordinate supervisory efforts and minimize regulatory overlaps in the existing domestic regulatory regime, while at the same time fostering inter-regulatory cooperation, culminated with an agreed Protocol for Joint On-Site Examinations for jointly regulated entities with the Securities Commission of The Bahamas at end-2007. There are currently fifty-six (56) jointly regulated entities. The key objective of this programme is to streamline examination activities by coordinating:

- the planning, timing and scope of examinations;
- the reporting of examination findings and recommendations; and
- follow-up and enforcement actions, if any.

The aggregate number of on-site examinations completed during 2007 stood at eighty (80), including thirty-one (31) restricted licences (see Table 15). In cases where a group of related licensees was examined, a combined Report of Examination was issued. Although the number of consultant examiners declined by one to seven, examination resources continued to be supplemented by the secondment of permanent BSD staff members under a six-month rotation programme.

Going forward, the Department intends to employ more risk-based principles of regulation and supervision for the conduct of on-site examinations, thereby promoting greater efficiency in the use of supervisory resources. Having the benefit of seven years of on-site examination experience, the goal is to tailor the approach to one that focuses more on the risk profile of licensees, thus avoiding a prescriptive one-size-fits-all approach, while at the same time continuing to adhere to the Basel standards for effective banking supervision.

To this end, the Department is presently undertaking an exercise to refine the risk categorization of licensees, using such factors as home/host designation, the degree to which activities are outsourced, complexity of ownership, market focus etc. A part of this exercise also includes the review of the on-site examination templates and methodology, toward the production of a more comprehensive manual to govern the program. The Department intends to publish a paper in early 2008, the objective being to promote awareness and enhance transparency in the regulatory and supervisory process.

Other Domestic Supervisory Actions

The Supervisory Unit of the Department continued to carry out comprehensive analysis and assessment of the on-going financial positions of active banks and trust companies. The ability of licensees to operate as going concerns and their compliance with the Bank's requirements, regarding liquidity, solvency, and risk management, were investigated and appraised.

In October, the Department released an electronic set of reporting forms styled as "the Quarterly Reporting System" ("the QRS"). The QRS comprises the existing BSD I and II reporting forms, along with the newly added BSD III form (Capital Adequacy Statement). The QRS was formulated in-house, as an interim system to the more comprehensive Online Reporting System being pursued by the Bank, and is intended to enhance the quality of the reports submitted by licensees. Based on the inputs, the forms automatically calculate key performance ratios, assess compliance with prudential norms and calculate the risk-weighted capital adequacy ratio. To facilitate completion, licensees were provided with appropriate guidance notes on the system, and commenced utilizing the quarterly suite of forms from the final quarter of 2007.

TABLE 16: Issued Guidelines

	Document	Final Issue Date
1	General Information and Application Guidelines for Private Trust Companies and their Registered Representatives	10th January 2007
2	Business Continuity Guidelines	1st May 2007
3	Guidelines for Independent Non-Executive Directors	9th May 2007

Source: The Central Bank of The Bahamas

In keeping with its commitment to ensure appropriate corporate governance structures in, as well as 'fit and proper' management of banks and trust companies within the jurisdiction, the Department reviewed and recommended approval for the appointment of one hundred and eleven (111) directors and fifty (50) senior officers. For 2007, eighty-one (81) meetings were held with licensees to discuss prudential issues, and licensees paid thirty two (32) courtesy visits to the Bank.

The Department remained vigilant in collecting and disseminating information on instances of attempted fraud or questionable activities brought to its attention by targeted institutions, the public, or other regulatory agencies. The Bank's website was regularly updated with warning notices to the public, providing timely information on suspected fraudulent schemes and unlicensed entities purporting to be banks or trust companies. To assist in this effort, the Attorney General's Office, the Royal Bahamas Police Force, the Postmaster General, the Bahamas Telecommunications Company, the Registrar General, and other financial sector regulatory authorities were routinely advised of these matters.

To ensure timely release of information, the Bank also utilized its membership on the Attorney General's

TABLE 17: Consultation Papers

	Consultation Paper	Date Released	Final Date for Comments
1	Stand-Alone Money Transmission Business Legislation	27th February 2007	30th March 2007
2	Proposal to Amend the Banks and Trust Companies Regulation Act, 2000 Relating to the Rights and Duties of Auditors of Licensees	6th November 2006	7th February 2008
3	The Temporary Relocation of Foreign Banks and Trust Companies to The Bahamas	12th November 2007	11th January 2008
4	Proposed Amendments to the Guidelines for the Prevention of Money Laundering and Countering the Financing of Terrorism	16th November 2007	31st January 2008

Source: The Central Bank of The Bahamas

Task Force, which examines ways to assimilate warnings and resolutions issued by the United Nations and partner nations regarding terrorists and other named individuals or organizations. It is intended that an enhanced mechanism to capture such warnings and resolutions be introduced in 2008-to provide coverage for the entire financial services industry.

During 2007, the Department's quarterly letters continued to provide an avenue for ongoing dialogue between the Bank and licensees regarding developments relating to their operations, guidelines and regulations issued, as well as other important policy matters affecting the industry.

Watch List Committee

The Department has recourse to supervisory intervention in accordance with the policy guideline titled "A Guide to the Central Bank's Ladder of Supervisory Intervention" published in April 2006. An important component of the ladder of supervisory intervention is the Watch List Committee-an internal committee, chaired by the Inspector, which is mandated to continuously monitor licensees placed on the watch list, to ensure compliance with directives of the Department. Placing a licensee on the watch list is an intermediate step to more severe supervisory intervention. For 2007, the Watch List Committee continued to identify and monitor high-risk licensees, placing specific emphasis on ensuring that the safety and soundness of these licensees is restored in a timely manner. The number of licensees on the Watch List was unchanged.

New Guidelines & Other Initiatives

The Department finalized and issued three (3) guidelines over the course of 2007 (see Table 16).

The 2006 amendments to the Central Bank of The Bahamas Act, 2000 and the Banks and Trust Companies Regulation Act, 2000 (the BTCRA), as well as the introduction of the Banks and Trust Companies (Private Trust Companies) Regulations, 2007, established a unique type of trust company known as the Private Trust Company ("PTC"), which is exempt from the full range of licensing requirements otherwise applicable to trust companies operating within and from within The Bahamas. The General Information and Application Guidelines for Private Trust Companies and their Registered Representatives outline the Central Bank's policy with regard to the approval of Registered Representatives of PTCs and their ongoing regulation and supervision.

Business continuity remains an ongoing priority for the Central Bank and the quick recovery of business functions after a disruption is crucial to maintaining confidence in the financial system. Accordingly, the Bank issued Business Continuity Guidelines in May 2007, which outlined the Bank's supervisory approach to business continuity planning and the sound practices which the Central Bank expects its licences to take into consideration in formulating their business continuity plans.

The Guidelines for Independent Non-Executive Directors (INEDs), which also came into effect in May 2007, specified elements that constitute independence, outlined activities that INEDs are prohibited from performing as they might lead to a conflict of interest, and identified and discussed issues that may influence the effectiveness of INEDs on the board. The Guidelines also clarified the expectations of the Bank in relation to independent non-executive directors of its licensees ("licensees") and certain functions of their boards.

The Department embraces a transparent and consultative approach to regulation, as a means of tapping industry expertise and experience to better understand the impact of new regulations on compliance costs and to identify, upfront in the process, any unintended operational and implementation issues. Over the course of 2007, the Department issued four (4) consultation papers for industry comment (see Table 17).

All final guidelines and consultation papers are published in full on the Central Bank's website at www.centralbankbahamas.com. Following the consultative process, the Department, in conjunction with the Legal Unit, proposed several changes to existing legislation as well as the implementation of several new pieces of legislation as summarized in Box C.

BOX 3: Legislative/Regulatory Developments

I. 2007 AMENDMENTS TO EXISTING STATUTES

The Central Bank of The Bahamas (Amendment) Act, 2007(Act No. 17 of 2007) and the Banks and Trust Companies Regulation (Amendment) Act, 2007 (Act No. 21 of 2007).

These amendments broadened the powers of the Bank to share information with other domestic regulatory authorities where the Governor considers that such cooperation or information may be relevant to the functions of such other regulatory authority or as a necessary part of a framework for consolidated supervision, oversight or regulation of the financial services sector. Similar amendments were made to the governing legislation of other domestic financial sector regulatory agencies.

II. PROPOSED LEGISLATIVE CHANGES

A. To Existing Statutes

Banks and Trust Companies Regulation Act, 2000

Proposed amendments to this Act seek to inter alia:

- Bring the supervision of non-bank money transmission businesses under the authority of the Central Bank of The Bahamas;
- Set out the rights and duties of auditors of licensees with respect to disclosing to the Inspector of Banks and Trust Companies, information about licensees which is of material significance to the functions and duties of the Inspector;

B. To Existing Regulations

Draft Banks and Trust Companies (Licence Application) (Amendment) Regulations, 2008

- These draft regulations will amend the Banks and Trust Companies (Licence Application) Regulations, 2002 to revise the documentary requirements for applicants seeking to become licensees of the Central Bank. The Bank will no longer require a detailed net worth statement for applicants who seek to acquire shareholdings in licensees of less than 10% but will permit such applicants to submit net worth statements which certify that their net worth is at least five (5) times the value of the share capital to be acquired. The regulations also permit the Bank to accept, in lieu of two character references (which the regulations currently require), a letter of good standing from the home regulator of proposed licensees which have parent companies domiciled in specified categories of countries.

Draft Financial Transactions Reporting (Amendment) Regulations, 2008

- These draft regulations seek, through an amendment to regulation 8 of the Financial Transactions Reporting Regulations, 2000 (which sets out the due diligence requirements for financial institutions providing wire transfer facilities), to bring The Bahamas into compliance with the FATF's Special Recommendation VII. This recommendation requires financial institutions, including money remitters, to among other things, include accurate and meaningful originator information (name, address and account number) on funds transfers and related messages that are sent.

C. Proposed New Regulations

Draft Banks and Trust Companies (Money Transmission Business) Regulations, 2008

- These draft regulations set out the regulatory requirements for stand alone money transmission businesses incorporated in The Bahamas and include provisions for, among other things, licensing, minimum capital, reporting and record keeping requirements.

Draft Banks and Trust Companies (Temporary Business Continuity Operations) Regulations, 2008

- Create a framework for the Central Bank to permit foreign banks and trust companies to relocate to The Bahamas temporarily on the occurrence of a natural disaster in their home jurisdictions.

Basel I Status

The Department remains committed to advancing the implementation of the 1996 amendments to Basel I related to Market Risk and Netting Arrangements. Efforts have progressed to the stage where comprehensive draft Market Risk Guidelines are being examined for practicality in the Bahamian context.

The draft Market Risk Guidelines establish a de minimis threshold for applying a capital charge to market investments of 10% of total on and off-balance sheet exposures. The market risk capital charge will apply to banks with a trading book meeting the de minimis threshold based on the Basel Committee's definition of a "trading book". Based on a market risk survey conducted by the Central Bank in 2006, it would appear that only a small number of licensees would be affected by these Guidelines, as most licensees held positions for asset liability management and not for trading purposes. Detailed proposals will be published for public comment during the first half of 2008.

Update on Basel II

The implementation of Basel II remains a challenging task for all banking supervisors, and particularly so for small economies such as The Bahamas. However, there is broad acceptance that, as a vehicle which seeks to harness best practices in risk management into the regulatory process, it will enhance financial stability in The Bahamas.

Similar to other jurisdictions in the Caribbean region, The Bahamas intends to adopt at least the key elements of Basel II (including the new credit risk weightings) by 2010. In the interim, the Department will work closely with home country regulators of the more complex banks for which the Central Bank serves as host supervisor. The aim will be to ensure that the global plans of the more complex banks for implementing Basel II, as approved by their home supervisor, are not thwarted by local rules or requirements in The Bahamas. At the same time, the Central Bank will want to ensure that there is no reduction in the minimum capital requirements, which it deems appropriate to protect depositors.

The Department anticipates that banks will be allowed to use a range of approaches, as appropriate to their size and complexity, while also taking into account the approaches of their parent banks, where applicable. Also, the Department expects that, for those stand-alone banking licensees, which are solely incorporated in The Bahamas and where the Central Bank serves as home regulator, the simplified or standardized approaches will be the most suitable in the short term.

Although there are advantages to the implementation of the new Accord, the Central Bank is also mindful of important challenges related to resources and training. This underscores the Central Bank's ongoing efforts to strengthen its relations with foreign regulatory counterparties via memoranda of understanding and a regular exchange of letters with the "home country" regulators. As the Basel Committee intends to have the new capital framework applied on a consolidated basis for banking groups, its introduction will make cooperation with foreign bank supervisors even more important than at present. In particular, this will be the case where the home regulator (i.e. the regulator based in the country of the group's origin and headquarters) has to consider whether to approve credit risk, market risk or operational risk models presented at the group level, for implementation in the home and host jurisdictions. (It is likely that large complex banking groups will wish to apply one consistent model through much or all of their global operations and they will naturally look to their home regulator for approval). This application, however, will not present any particular challenges for the Central Bank, as the legislative framework allows the Central Bank to co-operate with other regulators for the purpose of promoting effective consolidated supervision.

One of the major enhancements to the legislative framework in 2000 allowed the Central Bank to facilitate the consolidated supervision of its licensees by permitting their home country supervisors to conduct on-site inspections in The Bahamas and by exchanging relevant regulatory information for specified purposes with home country supervisors—while protecting the confidentiality of individual customer information.

Generally, the Central Bank intends to take a consultative approach to the implementation of Basel II, in order to develop the optimal approach for The Bahamas—not least because of the flexibility allowed to national regulators in a number of areas.

IMF Information Dissemination and Monitoring Initiative

The year 2007 represented the second annual participation by The Bahamas in the IMF's information dissemination and monitoring initiative for international and offshore financial centres. It is the agency's intention that this framework would increase transparency in the activities of international and offshore financial centres through the dissemination of a minimum set of information and provide information for its ongoing monitoring of international and offshore financial centres.

To complete this exercise, The Bahamas provided the IMF with a comprehensive set of financial sector data covering banking, insurance, investment funds, company and trust service providers and other relevant economic indicators. The Central Bank coordinated The Bahamas' response with the aid of the Securities Commission, the Office of the Registrar of Insurance Companies and the Inspector of Financial and Corporate Services Providers.

International Regulatory Cooperation

Foreign bank regulators continued to conduct in person, or through agents, on-site examinations of Bahamian licensees owned by banks in these countries. Such examinations are allowed for the purposes of consolidated supervision, with strict protection of Bahamian confidentiality laws. In 2007, the Panamanian and Philippine banking regulators took advantage of these provisions.

The Bank continued to cooperate with its international bank regulatory network to ensure that The Bahamas is not used by undesirable parties to escape proper oversight, and equally to ensure that institutions established and based in The Bahamas comply fully with internationally accepted standards and norms of bank management. The Department received and responded to eighteen (18) requests for information from various foreign regulatory authorities, from eleven (11) countries in 2007 (see Table 18), compared with thirty-three (33) requests from 20 countries in 2006-many of which related to securities matters where the Central Bank worked closely with the Securities Commission of The Bahamas (the Commission). The decline in the number of requests received partly reflected the Commission's ability, via the Securities Industry (Amendment) Act, 2007 to directly require any financial institution (including Central Bank licensees), to provide it with any information that is necessary to the execution of its functions under the Securities Industry Act, 1999.

TABLE 18: Requests for Cooperation from Foreign Regulatory Authorities in 2007

Country	Requests	Completed	Outstanding*
British Virgin Islands	1	1	
United States	3	3	
Panama	1	1	
Guyana	1	1	
Singapore	1	1	
St Vincent & Grenadines	1	1	
Barbados	4	3	1
Luxembourg	1	1	
Argentina	1	1	
Mexico	1	1	
Cayman Islands	3	3	
Total Requests	18	17	1

Source: The Central Bank of The Bahamas

Note * in this case, data has been provided but additional "follow-up" is required and requests were still being processed at year end.

Regulatory Cooperation in The Bahamas

In 2007, the Group of Financial Service Regulators (GFSR) continued to work closely together, under the chairmanship of Mr Hillary Deveaux, Executive Director of the Securities Commission and subsequently, the Governor of the Central Bank, Mrs. Wendy Craigg, who assumed the chairmanship in June 2007.

The GFSR met on eight (8) occasions. In addition, there were a number of special focus meetings involving the common regulators of the Colina Financial Group. The Central Bank also co-ordinated work by the regulators designed to demonstrate the success of The Bahamas in meeting overseas regulatory requests for cooperation on a timely and effective basis. The Bank participated in several technical groups with fellow regulators to consider possible revisions to the statutory filings and publication of licensees' financial conditions; money transmission supervision and issues relating to the Attorney General's Task Force.

Letters to Home Regulators

The implementation of the new international capital adequacy framework (Basel II) will make cooperation with foreign bank supervisors even more important than at present. Accordingly, in 2007 the Bank Supervision Department continued the annual communication with the home regulators of licensees, an exercise which began in May 2005. The annual letters provide an overview of the operations of subsidiaries or branches to home regulators, who were encouraged to give their comments on the condition of the parent and its operations.

Membership in International and Regional Bodies

The Department actively participated in discussions relating to regional and cross-border bank supervision, and maintains active membership in the following international and regional bodies.

- Association of Banks of the Americas (ASBA)
- Offshore Group of Banking Supervisors (OGBS)
- Caribbean Group of Banking Supervisors (CGBS)
- Caribbean Financial Action Task Force (CFATF)

A number of the Department's staff also served on various technical working groups and committees within these organizations.

Human Resources and Training

Staff training remained an important priority in 2007. The staff benefited from thirteen (13) overseas and local training workshops, courses and seminars in the areas of risk-focused supervision, trust examinations, conglomerate supervision, risk management/internal controls and advanced computer operations. The various training programs were primarily facilitated by the following organizations: Financial Stability Institute; the Caribbean Group of Banking Supervisors (CGBS); the United States Federal Reserve System; Office of Superintendent of Financial Institutions (OSFI), the Caribbean Regional Technical Assistance Centre (CARTAC); the Association of Supervisors of Banks of the Americas (ASBA); and The Bahamas Institute of Financial Services (BIFS).

In-house training sessions continued with local industry experts and staff presenting topics of interest and relevance to the work of the Department. The staff also benefited from the web-based training offered by the Financial Stability Institute, in Basel Switzerland. Expectations are that this type of training will continue to be offered to staff in 2008.

Management and senior staff participated in several fora and working groups, including the Caribbean Group of Banking Supervisors Plenary, the Association of Banking Supervisors of the Americas Annual Plenary, the College of Regulators meetings with OSFI, the ASBA and CGBS' Working Group sessions on Consolidated Supervision, and The Bahamas Financial Services Board's (BFSB) Trade & Tax initiatives forum.

The training program for 2008 is expected to concentrate primarily on several key areas: credit risk analysis, bank examination and analysis, advanced risk management, Basel II components - market risk, operational risk, etc. A strong emphasis will remain on in-house training and courses and seminars offered by other agencies, both locally and overseas. The Department plans to hold at least two briefing sessions with industry professionals on topics of interest.

Work Agenda for 2008

The Department will continue to focus its efforts on improving the efficiency of operations, completing outstanding legislative amendments and supervisory guidance documents, and upgrading of employees' skills, as set out in the following projects.

- Introduction of a more risk-based approach to onsite examination and refinement of the onsite methodology.
- Ongoing training of staff in bank and credit analysis, examination techniques, and knowledge of industry products and new initiatives.
- Finalization of revised AML/CFT Guidelines, the Temporary Business Continuity Operations Regulations and the Amendments to the BTCRA regarding the rights/duties of Auditors.
- Completion of procedural and policy documents

governing Money Transmission Businesses for roll-out to the industry.
- Finalization of the Bank's definitive Market Risk Guidelines, presently being formulated with the help of an external consultant, and issuance for consultation with the industry by 30 June 2008.
- Completion of the Bank's definitive statement regarding implementation of Basel II capital requirements by 30 September 2008, to include the identification of the Country's National Discretion Items.
- Completion of the Content Manager project which will allow for electronic capture and retrieval of all incoming correspondence and internal documentation.

Deposit Insurance Corporation

The Deposit Insurance Corporation (DIC) is a strategic component of the prudential regulation and supervision of the domestic banking sector, providing coverage to fourteen (14) member institutions in 2007. The DIC insures Bahamian dollar deposits up to a maximum of $50,000 to any single depositor in each member institution. Member institutions do not hold any equity position in the DIC.

The DIC invests in Bahamas Government Registered Stocks (BGRS) and earns interest rates tied to Commercial Banks' Prime Rate. Investments at year-end 2007 amounted to $8.7 million compared to $6.4 million in 2006.

The DIC assesses member institutions at an annual premium equal to one-twentieth of one percentage point of the sum of an amount equal to the average of the sum of those deposits insured by the DIC as of March 31 and September 30, in the preceding premium year. Based on average total insurable Bahamian dollar deposits in banks of $4.4 billion during 2006 relative to $4.0 billion in 2005, premiums levied and collected in 2007 amounted to $2.2 million compared to $2.0 million in 2006. At end-2007, the accumulated assets of the Fund stood at $10.2 million, up from $7.6 million in 2006.

INFORMATION TECHNOLOGY

For 2007, the Information Technology (IT) Department focused on initiatives aimed at simplifying infrastructure and systems management, improving security, access control and business resiliency, streamlining costs and complexities of the operation, and improving access to information. As a result of these various undertakings, the Bank has experienced significant improvements in systems stability and resilience, security, controls and disaster recovery capabilities.

The Department also initiated a significant number of programs designed to upgrade access to reporting and regulatory data, including the rollout of Document Imaging in the Exchange Control and Bank Supervision Departments, ongoing Portfolio Management System enhancements, workflow systems improvements, upgrade of network security systems, continued reduction in server hardware and storage utilizing virtualization and consolidated storage equipment.

Significant progress was made towards the eventual implementation of an Online Reporting and Information Management solution for regulatory submissions and subsequent data mining and reporting. A business case document, outlining the solution requirements, was prepared and subsequently approved by the Board. The responses to the Request for Information were used to formulate the Request for Proposal. Five competitive solution providers, each with excellent track records in regulatory reporting and data warehousing, responded with proposals, to which three will be shortlisted to demonstrate their capabilities during the first quarter of 2008. The Bank anticipates engaging the successful vendor in the second quarter of 2008 to complete this project within 12 - 18 months.

The Department continued to restructure its relationship with IT providers, with the establishment of new helpdesk agreements with several key vendors which are expected to deliver savings and improve service levels to the organization.

LEGAL UNIT

During 2007, the Legal Unit continued to execute its mandate as advisor to the Bank on legal matters relating to its operations and administration, and to prepare drafts of proposed regulations and amending Acts to enable the Bank to carry out its functions.

As part of the Bahamian delegation, staff of the Legal Unit attended and participated in the CFATF Plenary XXVI and Ministerial Council XIV over the

19th - 23rd November, 2007, in San Jose, Costa Rica at which the third Mutual Evaluation Report on the Anti-Money Laundering and Combating the Financing of Terrorism (AML/CFT) regime in The Bahamas was discussed and approved. Legal Unit staff also participated in a sub-committee of the Attorney General's Task Force, which was established to identify and make recommendations on areas in the country's AML/CFT regime which needed to be enhanced.

The Legal Unit facilitated training for Bank staff and made presentations at various seminars on Private Trust Legislation and on The Bahamas' Proposal for Implementation of FATF Special Recommendation VII. The staff of the Unit attended seminars on a variety of subjects, including payment systems legal reform, prevention of money laundering and terrorist financing, insurance and private wealth management and tax and trade issues.

Members of the Unit also participated in the ongoing work of the Legal Requirements Working Group, which is mandated to make recommendations regarding the legal framework necessary to support the implementation of an Automated Clearing House (ACH) in The Bahamas and to review any legal issues arising as a result of its operation.

INTERNAL AUDIT

During 2007, the Internal Audit Unit continued its efforts to ensure that key operational areas, including currency, external reserves management and correspondent bank account reconciliations, were monitored on a continuous basis. Other key audits included a review of activities related to Government Treasury bill operations, numismatic coins and financial transactions undertaken for the public sector.

In 2008, the Unit will continue to focus on crucial areas of the Bank's operations, using risk-based auditing techniques with emphasis on strengthening internal control processes and implementing an enterprise-wide risk management program.

ADMINISTRATION

During 2007, the Administration Department managed several capital projects relating to the general upkeep of the Bank's facilities and environment.

The Balcony House Museum reopened to the public in October 2007, after a three-year hiatus, during which time repairs and refurbishments were completed. The Museum continued to be operated by the Antiquities, Monuments and Museums Corporation. Repair works were also undertaken to Verandah House, which currently accommodates the Bahamas Institute of Financial Services.

Internal development work continued on an automated Procurement & Payment System, which was implemented during the second quarter of 2007, and has greatly improved the efficiency of the Bank's processes for acquiring goods and services.

During the year, external consultants provided further enhancements and functionality to the automated Dormant Account System, and the Bank commenced a system wide audit and reconciliation of dormant accounts. The Bank accepted submission of dormant accounts from licensees totaling approximately $1.2 million and processed claims of nearly $0.3 million.

The Department provided coordination and logistical support for numerous seminars, conferences and events during the year, which included the Caribbean Group of Banking Supervisors (CGBS) Plenary meeting, held at the British Colonial Hilton Hotel in May.

The Bank's Art Gallery was the venue for six exhibitions, including debuts by a group of art teachers and the Junkanoo Association of The Bahamas. The 24th Annual Art Exhibition, which was held in November, provided an ongoing venue for promoting art development.

CORPORATE ACTIVITIES

THE BOARD

Under the Central Bank of The Bahamas Act, 2000, the Board of Directors is responsible for ensuring that appropriate policies, management and financial controls, and administrative systems are in place to allow the Bank to achieve its statutory objectives in an efficient and effective manner.

In January 2007, the Central Bank's two external Directors, Mr. Carlton Williams and Mr. Warren Rolle, were reappointed to their positions. In August, they were replaced by Mr. Gregory Cleare and Mr. Vincent Vanderpool-Wallace, both of whom served previously as Directors. In addition, Mr. Michael Lightbourne, a career banker and former central banker, was appointed to the post of Deputy Governor, effective 4th June 2007, and became a member of the Board.

During the year, amendments were proposed to the Central Bank of The Bahamas Act, 2000 to expand the size of the Board by increasing the number of the Bank's non-executive directors to four (4), and to clarify the maximum fine for contravention of licensees' statutory reserve and liquid asset ratio requirements.

OVERSEAS MEETINGS AND CONFERENCES

In January, Governor Wendy Craigg traveled to Exuma to attend the Bahamas Financial Services Board's Annual Retreat. During the months of May and November, Governor Craigg participated in the semi-annual meetings of CARICOM Central Bank Governors, which convened in Jamaica. The Governor also attended the annual meetings of the Bank for International Settlements in Basel, Switzerland, and the annual IMF/World Bank meetings held in Washington, D.C. in June and October, respectively.

STAFF TRAINING, DEVELOPMENT AND RELATIONS

In January, the Bank received the final report on the comprehensive Job Evaluation and Organizational Review & Compensation Exercise in which it had been engaged during the past several years and, based on the recommendations of the report, implemented a revised grade and salary structure. Following negotiations, the Bank and the Union of Central Bankers executed a new five-year Agreement on May 15.

During the review year, the Bank continued to provide professional growth opportunities for employees through in-house training and sponsorship in domestic and international training programmes. Enrolment in international training programmes_inclusive of courses, meetings and conferences_totalled 61, while 192 attendees were sponsored locally. In addition to local and international training, staff of the Bank participated in 14 in-house training and development workshops and seminars, including the annual Induction Training Course.

Staff-initiated Continuing Education programmes have been consistent throughout the year, and the 34 employees currently enrolled in continuing education courses benefited from tuition reimbursements and subsidies under the Staff Training Incentive Programme. Additionally, two employees are presently engaged in full-time studies—one locally and one overseas_under the In-Service Awards Programme.

At the Annual Long Service Awards Presentation Ceremony in January, the Bank recognized four employees for twenty years of service and five for ten years of service.

STAFF COMPLEMENT

As at 31 December 2007, the staff complement stood at 232, inclusive of 215 permanent and 17 contractual employees. During the year, Mr. Michael Foot, Bank Inspector, demitted office after serving a three-year contract with the Bank. Among other separations were eight (8) resignations and two (2) retirements. The Bank recruited eight (8) new employees in 2007, and was also saddened by the loss of two (2) employees.

PUBLIC RELATIONS

The Bank continued to demonstrate its support for the development of the youth of the nation by partnering with the Ministry of Education and the Lyford Cay Foundation to fund the All-Bahamian Merit Scholarship Award. As is customary, the Bank also hosted student tours of its various departments, accommodating students from a total of seven public and private educational institutions, for whom sessions on the role and function of the Central Bank were also facilitated.

ACKNOWLEDGMENT

The Board of Directors extends its sincere appreciation to all Bank staff for their continuous dedicated service during the past year.

MANAGEMENT'S REPORT

The Central Bank of The Bahamas' Financial Statements for the year ended December 31, 2007 along with comparative figures for 2006, are shown on pages 46 to 76.

Growth in total assets of $112.4 million (15.5%) was due mainly to a $158.0 million (74.5%) increase in other assets to $370.1 million, as external reserves declined by $45.5 million to $454.2 million. The Bank's holdings of Treasury bills were higher by $91.7 million, (based on rediscounting activities by commercial banks to support liquidity requirements); and the portfolio of Bahamas Government Registered Stocks rose by $56.7 million (73.1%).

Total liabilities grew by $101.2 million (16.4%), led by a $100.4 million (16.6%) hike in demand liabilities. In particular, notes in circulation were higher by 14.8 million (4.9%), and deposits by commercial banks, by $88.1 million (35.1%).

Increased holdings of domestic investments, combined with marginally higher yields on foreign assets, resulted in a $1.7 million (5.1%) gain in operating income to $34.9 million. With expenses down by $2.5 million (9.6%) to $23.7 million, there was an overall improvement in profits from operations of $4.2 million (60.4%) to $11.2 million.

The Central Bank of The Bahamas

FINANCIAL STATEMENTS

31 December 2007

PricewaterhouseCoopers
Providence House
East Hill Street
P. O. Box N-3910
Nassau, The Bahamas

PKF
Pannell House
44 Elizabeth Avenue
P. O. Box N-8335
Nassau, The Bahamas

INDEPENDENT AUDITORS' REPORT

To the Directors of the Central Bank of The Bahamas

Report on the Financial Statements

We have audited the accompanying financial statements of the Central Bank of The Bahamas, which comprise the balance sheet as of 31 December 2007, and the income statement, statement of changes in equity and reserves and cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory notes.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with International Financial Reporting Standards and the Central Bank of The Bahamas Act, 2000. This responsibility includes: designing, implementing and maintaining internal controls relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

Auditors' Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with International Standards on Auditing. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditors' judgement, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditors consider internal controls relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

Auditors' Responsibility (Continued)

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the accompanying financial statements present fairly, in all material respects, the financial position of the Central Bank of The Bahamas as of 31 December 2007, and its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards and the Central Bank of The Bahamas Act, 2000.

PricewaterhouseCoopers.
Chartered Accountants

Nassau, Bahamas
16 April, 2008

PKF
Chartered Accountants

Nassau, Bahamas
16 April, 2008

THE CENTRAL BANK OF THE BAHAMAS
BALANCE SHEET AS AT 31 DECEMBER 2007
(Amounts expressed in Bahamian Dollars)

	Notes	2007 $	2006 $
ASSETS			
PROPERTY, PLANT AND EQUIPMENT	4	14,565,722	14,604,933
EXTERNAL ASSETS	5		
Cash and deposits		59,540,754	90,606,867
Marketable securities issued or guaranteed by foreign governments	6	384,710,396	399,723,705
International Monetary Fund:	7		
Bahamas reserve tranche		9,893,418	9,418,568
Special drawing rights		90,099	13,350
		454,234,667	499,762,490
OTHER ASSETS			
Bahamas Mortgage Corporation bond	8	-	301,079
Advances to the Bahamas Government	9	73,412,547	63,037,758
Bahamas Government registered stocks	10	134,282,446	77,594,632
Loans to Bahamas Government agency	11	6,776,126	7,050,504
The Bridge Authority bonds	12	770,903	761,269
Clifton Heritage Authority bonds	13	637,973	638,075
Bahamas Government Treasury bills	14	144,098,022	52,400,690
Receivables and other accounts		10,158,879	10,386,449
		370,136,896	212,170,456
Total Assets		**838,937,285**	**726,537,879**

The notes on pages 54 to 76 form an integral part of these financial statements.

THE CENTRAL BANK OF THE BAHAMAS
BALANCE SHEET AS AT 31 DECEMBER 2007
(Amounts expressed in Bahamian Dollars)
(Continued)

	Notes	2007 $	2006 $
LIABILITIES, EQUITY AND RESERVES			
DEMAND LIABILITIES			
Notes in circulation		317,146,751	302,373,357
Coins in circulation		16,798,735	16,064,232
Deposits by commercial banks	15	339,096,999	250,960,623
Deposits by the Bahamas Government and Bahamas Government agencies		26,041,541	26,441,541
Deposits by international agencies	16	426,966	546,936
Payables and other accounts		4,274,800	3,338,072
Provision for payment into the Consolidated Fund	18	-	3,618,000
		703,785,792	603,342,761
OTHER LIABILITIES			
International Monetary Fund allocation of special drawing rights	17	16,261,326	15,485,607
EQUITY AND RESERVES			
Authorized and fully paid capital		3,000,000	3,000,000
Exchange equalization account	18	(227,646)	227,294
Contingency reserve	18	750,000	750,000
Other reserves	18	9,799,944	13,758,811
General reserves	18	105,567,869	89,973,406
		118,890,167	107,709,511
Total Liabilities, Equity and Reserves		**838,937,285**	**726,537,879**

The financial statements, as approved by the board of directors and authorized for issuance on 16 April 2008, are signed on its behalf by:

Governor   Director

The notes on pages 54 to 76 form an integral part of these financial statements.

THE CENTRAL BANK OF THE BAHAMAS
INCOME STATEMENT
FOR THE YEAR ENDED 31 DECEMBER 2007
(Amounts expressed in Bahamian Dollars)

	Notes	2007 $	2006 $
INCOME	19	34,888,001	33,192,437
EXPENSES	20	(23,707,345)	(26,222,808)
NET PROFIT FOR THE YEAR		**11,180,656**	**6,969,629**

The notes on pages 54 to 76 form an integral part of these financial statements.

THE CENTRAL BANK OF THE BAHAMAS
STATEMENT OF CHANGES IN EQUITY AND RESERVES
FOR THE YEAR ENDED 31 DECEMBER 2007
(Amounts expressed in Bahamian Dollars)

	Authorized and fully paid capital	Exchange equalization account	Contingency reserve	Other reserves	General reserves	Total
	$	$	$	$	$	$
Balance at 1 January 2006	3,000,000	154,046	750,000	13,758,811	86,695,025	104,357,882
Net profit for the year	-	-	-	-	6,969,629	6,969,629
Transfer to Consolidated Fund					(3,618,000)	(3,618,000)
Transfer of unrealized exchange gains	-	73,248	-	-	(73,248)	-
Balance at 31 December 2006	3,000,000	227,294	750,000	13,758,811	89,973,406	107,709,511
Net profit for the year	-	-	-	-	11,180,656	11,180,656
Transfer from other reserves to general reserves				(3,958,867)	3,958,867	-
Transfer of unrealized exchange losses	-	(454,940)	-	-	454,940	-
Balance at 31 December 2007	**3,000,000**	**(227,646)**	**750,000**	**9,799,944**	**105,567,869**	**118,890,167**

The notes on pages 54 to 76 form an integral part of these financial statements.

THE CENTRAL BANK OF THE BAHAMAS
CASH FLOW STATEMENT
FOR THE YEAR ENDED 31 DECEMBER 2007
(Amounts expressed in Bahamian Dollars)

	Notes	2007 $	2006 $
CASH FLOWS FROM OPERATING ACTIVITIES:			
Net profit for the year		11,180,656	6,969,629
Adjustments for non-cash items:			
Amortization of premiums on marketable securities	6	2,377,842	3,724,902
Depreciation	4	1,607,630	1,608,253
Loss on sale of property, plant and equipment		-	16,225
Interest income	19	(33,655,962)	(31,421,837)
Interest expense	20	647,375	550,976
Net cash used in operating activities before changes in operating assets and liabilities		(17,842,459)	(18,551,852)
(Increase)/decrease in operating assets:			
International Monetary Fund - Special Drawing Rights		224,120	294,223
Receivables and other accounts		395,441	596,186
(Decrease)/increase in operating liabilities:			
Notes in circulation		14,773,394	16,081,429
Coins in circulation		734,503	1,171,539
Deposits by commercial banks		88,136,376	(35,269,200)
Deposits by the Bahamas Government and Bahamas Government agencies		(400,000)	(27,350,783)
Deposits by international agencies		(119,970)	(235,770)
Payables and other accounts		936,917	559,707
Net cash from/(used in) operating activities		**86,838,322**	**(62,704,521)**

The notes on pages 54 to 76 form an integral part of these financial statements.

THE CENTRAL BANK OF THE BAHAMAS
CASH FLOW STATEMENT
FOR THE YEAR ENDED 31 DECEMBER 2007
(Amounts expressed in Bahamian Dollars)
(Continued)

	Notes	2007 $	2006 $
CASH FLOWS FROM INVESTING ACTIVITIES:			
Purchases of marketable securities	6	(27,000,000)	(30,000,000)
Proceeds from maturities of marketable securities	6	39,500,000	50,000,000
Purchases of property, plant and equipment	4	(1,568,419)	(2,215,423)
Proceeds from sale of property, plant and equipment		-	37,935
Advances (made to)/repaid by Bahamas Government	9	(10,000,000)	15,000,000
Purchase of the Bridge Authority bonds	12	(9,400)	(5,100)
Purchases of Bahamas Government registered stocks	10	(56,210,900)	(24,518,400)
Proceeds from sales and maturities of Bahamas Government registered stocks	10	192,700	20,846,200
Repayments of loan by Bahamas Government agency	11	275,000	275,000
Purchase of Clifton Heritage Authority bonds	13	-	(633,700)
Purchase of Bahamas Government Treasury bills	14	(290,344,485)	(52,214,845)
Proceeds from the sale and maturities of Bahamas Government Treasury bills	14	199,098,332	
Proceeds from the maturity of Bahamas Mortgage Corporation bond		300,000	-
Interest received		32,296,172	31,864,673
Net cash (used in)/provided by investing activities		**(113,471,000)**	**8,436,340**
CASH FLOWS FROM FINANCING ACTIVITIES:			
Payment to the Consolidated Fund		(3,618,000)	-
Interest paid		(647,564)	(528,950)
Net cash used in financing activities		(4,265,564)	(528,950)
Net decrease in cash and cash equivalents		**(30,898,242)**	**(54,797,131)**
Cash and cash equivalents at beginning of the year		90,650,144	145,447,275
Cash and cash equivalents at end of the year		**59,751,902**	**90,650,144**
Cash and cash equivalents are comprised of the following:			
Cash and deposits		59,540,754	90,606,867
Cash on hand (included in receivables and other accounts)		211,148	43,277
		59,751,902	**90,650,144**

The notes on pages 54 to 76 form an integral part of these financial statements.

1. INCORPORATION AND ACTIVITIES

The Central Bank of The Bahamas (the Bank) was established under the Central Bank of The Bahamas Act Chapter 321, and was continued under the Central Bank of The Bahamas Act, 2000 (the Act). Its main place of business is located at Frederick Street, Nassau, Bahamas. The Bank's principal business is the provision of central banking facilities for the Commonwealth of The Bahamas. In accordance with the Act, it is the duty of the Bank to promote and maintain monetary stability, and credit and balance of payments conditions conducive to the orderly development of the Bahamian economy.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The principal accounting policies applied in the preparation of these financial statements are set out below. These policies have been consistently applied with the years presented, unless otherwise stated.

(a) Basis of preparation

The Bank's financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS). The financial statements have been prepared under the historical cost convention.

The preparation of the financial statements in conformity with IFRS requires the use of certain critical accounting estimates. It also requires management to exercise its judgement in the process of applying the Bank's accounting policies. The areas involving a higher degree of judgement or complexity, or areas where assumptions and estimates are significant to the financial statements are disclosed in Note 3.

In the current year, the Bank has adopted IFRS 7 Financial Instruments: Disclosures and the amendments to IAS 1 Presentation of Financial Statements, which became effective for fiscal periods beginning on or after 1 January 2007. The impact of the adoption of IFRS 7 and the changes to IAS 1 has been to expand the disclosures provided in these financial statements regarding the Bank's financial instruments and management of capital.

The remaining standards and amendments and interpretations to published standards that became effective for fiscal periods beginning on or after 1 January 2007 were not relevant to the Bank's operations and accordingly did not impact the Bank's accounting policies or financial statements.

The application of the new standards and amendments and interpretations to existing standards that have been published but are not yet effective are not expected to have a material impact on the Bank's accounting policies or financial statements in the period of initial application.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

(b) Revenue and expense recognition

Revenues and expenses are recognized on the accrual basis.

(c) Foreign currency translation

(i) Functional currency and presentation currency

Items included in the financial statements are measured using the currency of the primary economic environment in which the Bank operates (the functional currency), namely, the Bahamian dollar. The financial statements are presented in Bahamian dollars, which is the Bank's functional and presentation currency.

(ii) Transactions and balances

Transactions in currencies other than Bahamian Dollars are converted at the rates of exchange ruling at the time of the transactions. Balances in currencies other than Bahamian Dollars at the balance sheet date are converted at the closing rate of exchange prevailing at the balance sheet date.

The net change in the Bank's assets and liabilities arising from movements in currency exchange rates is included in the income statement and, in accordance with Sections 32(2)(a) and 32(2)(b) of the Act, the unrealized portion is transferred to an exchange equalization account.

(d) Property, plant and equipment

Property, plant and equipment are recorded at cost less accumulated depreciation. Depreciation is provided in equal annual instalments so as to write off the cost of assets, other than land, over their estimated useful lives. The following rates are used:

Buildings & renovations	2% - 20% p.a.
Office equipment	20% - 33% p.a.
Computer software	33% - 50% p.a.
Office furniture & fittings	20% p.a.
Other fixed assets	20% - 33% p.a.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

(e) Financial assets

The Bank classifies its financial assets in the following categories: loans and receivables; held-to-maturity investments and available-for-sale financial assets. The classification depends on the purpose for which the financial assets were acquired. Management determines the classification of its investments at initial recognition and re-evaluates this designation at every reporting date.

(i) Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market, other than: (a) those that the Bank intends to sell immediately or in the short term; (b) those that the Bank upon initial recognition designates as available-for-sale; or (c) those for which the Bank may not recover substantially all of its initial investment, other than because of credit deterioration, which are classified as available-for-sale.

Advances to the Bahamas Government

The advances to the Bahamas Government are classified as loans and receivables originated by the Bank and not held-for-trading. These loans, which are payable on demand, are stated at amortized cost, less any provision for impairment.

Loans to Bahamas Government agency

The loans to Bahamas Government agency are classified as loans and receivables originated by the Bank and not held-for-trading. These loans, which have a fixed maturity period, are measured at amortized cost, using the effective interest rate method, less any provision for impairment.

Bahamas Mortgage Corporation bonds

Bahamas Mortgage Corporation bonds are classified as loans and receivables by the Bank and not held-for-trading and are measured at amortized cost.

Bahamas Government registered stocks

Bahamas Government registered stocks are classified as loans and receivables by the Bank and not held-for-trading and are measured at amortized cost.

The Bridge Authority bonds

The Bridge Authority bonds are classified as loans and receivables by the Bank and not held-for-trading and are measured at amortized cost.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

(e) Financial assets (Continued)

(i) Loans and receivables (Continued)

Bahamas Government Treasury bills
The Bahamas Government Treasury bills are classified as loans and receivables by the Bank and not held-for-trading and are measured at amortized cost.

Section 29(1)(c) of the Act requires that the total amount of Government issued or guaranteed securities held at any time by the Bank, which mature beyond five years after their date of issue, shall not exceed 20% of the demand liabilities of the Bank. At the balance sheet date, such securities held by the Bank which mature beyond five years after their date of issue was approximately 19.27% (2006: 13.14%) of such liabilities.

The Act further requires that any holdings of Government issued or guaranteed securities should not have maturities extending beyond 20 years from the date of their acquisition. The Bank held no such securities maturing beyond 20 years, at either 31 December 2007 or 2006.

(ii) Held-to-maturity financial assets

Held-to-maturity investments are non-derivative financial assets with fixed or determinable payments and fixed maturities that the Bank's management has the positive intention and ability to hold to maturity. If the Bank were to sell other than an insignificant amount of held-to-maturity assets, the entire category would be reclassified as available-for-sale.

Marketable securities issued or guaranteed by foreign governments
Marketable securities issued or guaranteed by foreign governments are classified as held-to-maturity investments, and are stated at amortized cost, using the effective interest rate method. Such investments are subject to review for impairment.

Clifton Heritage Authority bonds
Clifton Heritage Authority bonds are held to maturity investments, and are stated at amortized cost, using the effective interest rate method. Such investments are subject to review for impairment.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

(e) Financial assets (Continued)

(iii) Available-for-sale financial assets

Available-for-sale investments are those intended to be held for an indefinite period of time, which may be sold in response to needs for liquidity or changes in interest rates, exchange rates or equity prices.

Regular-way purchases and sales of financial assets categorized as held-to-maturity and available-for-sale are recognized on the trade-date (that is the date on which the Bank commits to purchase or sell the asset).

Financial assets are initially recognized at fair value plus transaction costs for all available-for-sale financial assets. Financial assets are derecognized when the rights to receive cash flows from the financial assets have expired or where the Bank has transferred substantially all risks and rewards of ownership.

Gains and losses arising from changes in the fair value of available-for-sale financial assets are recognized directly in equity, until the financial asset is derecognized or impaired. At this time, the cumulative gain or loss previously recognized in equity is recognized in the income statement. However, interest calculated using the effective interest method for investments classified as available-for-sale is recognized in the income statement.

The fair values of quoted investments in active markets are based on current bid prices.

(f) Impairment of assets

The Bank assesses at each balance sheet date whether there is objective evidence that a financial asset is impaired. A financial asset is impaired if its carrying amount is greater than its estimated recoverable amount. The amount of the impairment for assets carried at amortized cost is calculated as the difference between the assets carrying amount and the present value of expected future cash flows discounted at the financial asset's original effective interest rate.

If, in a subsequent period, the amount of the impairment decreases and the decrease can be related objectively to an event occurring after the impairment was recognized, the previously recognized impairment is decreased and the decrease is recognized in the income statement.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

(g) Numismatic coins

Numismatic coins, which are specially minted or packaged as collectors' items and are not issued for monetary purposes, are not included in coins in circulation. Any profit or loss arising from the sale of these coins is included in the income statement.

(h) Retirement benefit costs

The Bank's retirement plan is a contributory defined benefit plan with participants being permanent employees who join the Bank prior to age 55. The cost of providing such benefits is determined using the projected unit credit method, with actuarial valuations being carried out at each balance sheet date. Actuarial gains and losses which exceed 10% of the greater of the present value of the Bank's pension obligations and the fair value of the plan's assets are amortized over the expected average remaining working lives of the participating employees. Past service cost is recognized immediately to the extent that the benefits are already vested, and otherwise is amortized on a straight-line basis over the average period until the amended benefits become vested.

The amount recognized in the balance sheet represents the present value of the defined benefit obligation as adjusted for the unrecognized actuarial gains and losses and unrecognized past service costs, and reduced by the fair value of plan assets. Any asset arising as a result of this calculation is limited to the unrecognized actuarial losses and past service cost plus the present value of available refunds and reductions in future contributions to the plan.

(i) Fiduciary items

No account is taken in these financial statements of assets held or liabilities incurred by the Bank in a fiduciary capacity.

3. CRITICAL ACCOUNTING ESTIMATES AND JUDGMENTS

The Bank makes estimates and assumptions that affect the reported amounts of assets and liabilities within the next financial year. Estimates and judgements are continually evaluated and based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. Such accounting estimates and judgments are disclosed in Notes 2 (f) and 2 (h).

4. PROPERTY, PLANT AND EQUIPMENT

	Land	Buildings & renovations	Office equipment	Computer Software	Office furniture & fittings	Other fixed assets	Total
	$	$	$	$	$	$	$
COST							
At 1 January 2007	2,452,938	12,175,003	9,441,931	6,381,926	3,078,282	463,671	33,993,751
Additions	-	267,245	674,200	352,779	239,208	34,987	1,568,419
At 31 December 2007	2,452,938	12,442,248	10,116,131	6,734,705	3,317,490	498,658	35,562,170
ACCUMULATED DEPRECIATION							
At 1 January 2007	-	4,185,509	5,895,352	6,217,697	2,784,316	305,944	19,388,818
Charge for the year	-	399,071	876,767	148,971	119,153	63,668	1,607,630
At 31 December 2007	-	4,584,580	6,772,119	6,366,668	2,903,469	369,612	20,996,448
NET BOOK VALUE							
At 31 December 2007	**2,452,938**	**7,857,668**	**3,344,012**	**368,037**	**414,021**	**129,046**	**14,565,722**

	Land	Buildings & renovations	Office equipment	Computer Software	Office furniture & fittings	Other fixed assets	Total
	$	$	$	$	$	$	$
COST							
At 1 January, 2006	2,452,938	11,702,455	8,240,950	6,050,206	3,006,725	392,556	31,845,830
Additions	-	472,548	1,268,483	331,720	71,557	71,115	2,215,423
Disposal	-	-	(67,502)	-	-	-	(67,502)
At 31 December 2006	2,452,938	12,175,003	9,441,931	6,381,926	3,078,282	463,671	33,993,751
ACCUMULATED DEPRECIATION							
At 1 January 2006	-	3,860,066	5,149,255	5,922,808	2,602,292	259,486	17,793,907
Charge for the year	-	325,443	746,097	294,889	195,366	46,458	1,608,253
Disposal	-	-	-	-	(13,342)	-	(13,342)
At 31 December 2006	-	4,185,509	5,895,352	6,217,697	2,784,316	305,944	19,388,818
NET BOOK VALUE							
At 31 December 2006	**2,452,938**	**7,989,494**	**3,546,579**	**164,229**	**293,966**	**157,727**	**14,604,933**

5. EXTERNAL ASSETS

External assets comprise those assets defined by Section 18(1) of the Act. The Act also requires that the value of external assets shall not at any time be less than 50% of the value of the aggregate of the notes and coins in circulation and other demand liabilities of the Bank. At the year-end, external assets represented approximately 64.54% (2006: 82.83%) of such liabilities.

6. MARKETABLE SECURITIES ISSUED OR GUARANTEED BY FOREIGN GOVERNMENTS

Section 18(1) of the Act requires that marketable securities issued or guaranteed by foreign governments, which mature beyond 5 years, shall at no time constitute more than 30% in value of the Bank's external assets. At 31 December 2007, marketable securities held by the Bank, which mature after 5 years, constituted 14.68% (2006: 11.00%) of the Bank's external assets.

The movement in marketable securities is as follows:

	2007	**2006**
	$	**$**
At beginning of year	395,409,750	419,134,652
Purchases	27,000,000	30,000,000
Redemptions	(39,500,000)	(50,000,000)
Amortization of premium	(2,377,842)	(3,724,902)
End of year	**380,531,908**	**395,409,750**
Add: Accrued interest	4,178,488	4,313,955
	384,710,396	**399,723,705**

The maturity of the marketable securities is as follows:

	2007	**2006**
	$	**$**
Within 60 days	-	-
60 days to 1 year	72,829,705	45,391,263
1 to 5 years	245,183,000	299,342,813
After 5 years	66,697,691	54,989,629
	384,710,396	**399,723,705**

The fair value of these securities at the balance sheet date was $386,394,914 (2006: $386,366,849). These securities bear interest at rates varying between 2.62% and 6.50% (2006: 2.62% and 6.50%).

7. INTERNATIONAL MONETARY FUND

Bahamas Tranche

The International Monetary Fund (IMF) reserve tranche represents the amount by which The Bahamas' quota of Special Drawing Rights (SDR) with the IMF exceeds subscription payments as noted below:

	2007 SDR (millions)	2007 $	2006 SDR (millions)	2006 $
Quota	130.3	205,906,336	130.3	196,023,565
Subscription payments in promissory notes	(119.3)	(188,731,460)	(119.3)	(179,422,681)
Subscription payments in currency	(4.7)	(7,281,458)	(4.7)	(7,182,316)
Reserve tranche	**6.3**	**9,893,418**	**6.3**	**9,418,568**

The reserve tranche was purchased from the Government of The Bahamas in 1976.

Subsequent to that purchase, the Bank has funded 25% of each increase in the IMF subscriptions of The Bahamas by issuing interest-free promissory notes which are payable on demand. In the opinion of the Directors, it is not probable that an outflow of resources employing economic benefits will be required to settle these promissory notes, which total $51,678,036 (2006: $49,632,139). Consequently, this amount is regarded as a contingent liability and is not recognized in the Bank's balance sheet.

Special Drawing Rights

This amount represents SDR holdings with the IMF, is repayable on demand and bears interest at rates varying from 3.50% to 4.32% (2006: 4.31% to 5.48%).

8. BAHAMAS MORTGAGE CORPORATION BOND

This bond bears interest at a rate of 2.00% (2006: 2.00%) per annum below the Prime rate and matured in 2007.

	2007 $	2006 $
At beginning of year	301,079	300,000
Maturities	(301,079)	-
Accrued Interest	-	1,079
End of Year	**-**	**301,079**

9. ADVANCES TO THE BAHAMAS GOVERNMENT

Sections 28(3) and 28(4) of the Act require that advances to the Government, which may be outstanding at any one time, shall not exceed 10% of either the annual average ordinary revenue of the Government over the three preceding years for which the accounts have been laid before Parliament or the estimated ordinary revenue of the Government for the year, whichever is the less.

At the balance sheet date, advances to the Government approximated 5.6% (2006: 6.00%) of the lesser of such revenues. Of those advances, $19,000,000 (2006: $19,000,000) bear interest at a rate of 1.09% (2006: 1.09%), $5,969,000 (2006: $5,969,000) bear interest at a rate of 0.08% (2006: 0.08%) and $10,000,000 (2006: Nil) bear interest at a rate of 2.25% (2006: Nil). The remaining advances were interest free during both 2007 and 2006. The advances are repayable on demand.

The movement in the advances to The Bahamas Government is as follows:

	2007	**2006**
	$	**$**
At beginning of year	61,987,608	76,987,608
Additions	10,000,000	-
Repayments	-	(15,000,000)
End of year	**71,987,608**	**61,987,608**
Add: Accrued interest	1,424,938	1,050,150
End of year	**73,412,547**	**63,037,758**

10. BAHAMAS GOVERNMENT REGISTERED STOCKS

The movement in Bahamas Government Registered Stock is as follows:

	2007	**2006**
	$	**$**
At beginning of year	76,366,800	72,694,600
Purchases	56,210,900	24,518,400
Redemptions/maturities	(192,700)	(20,846,200)
End of year	**132,385,000**	**76,366,800**
Add: Accrued interest	1,897,446	1,227,832
End of year	**134,282,446**	**77,594,632**

10. BAHAMAS GOVERNMENT REGISTERED STOCKS (Continued)

Bahamas Government Registered Stocks bear interest at rates ranging between 5.53% and 8.75% (2006: 5.60% and 6.75%) and mature as noted below:

	2007	2006
	$	$
1 to 5 years	89,500	-
More than 5 years	134,192,946	77,594,632
	134,282,446	**77,594,632**

11. LOANS TO BAHAMAS GOVERNMENT AGENCY

This balance is comprised of three loan facilities made available to a Government agency in accordance with Section 29(l) (f) of the Act.

The movement in loans to Bahamas Government Agency is as follows:

	2007	2006
	$	$
At beginning of year	7,025,000	7,300,000
Repayments	(275,000)	(275,000)
End of year	**6,750,000**	**7,025,000**
Add: Accrued interest	26,126	25,504
End of year	**6,776,126**	**7,050,504**

The loans bear interest at 2.00% (2006: 2.00%) and mature as noted below:

	2007	2006
	$	$
1 to 5 years	250,000	375,000
More than 5 years	6,500,000	6,650,000
	6,750,000	**7,025,000**

12. THE BRIDGE AUTHORITY BONDS

These bonds bear interest at rates ranging from 1.00% to 1.50% (2006: 1.00% to 1.50%) per annum over the Prime rate.

The movement and maturity for the Bridge Authority Bonds are as follows:

	2007 $	2006 $
At beginning of year	748,400	743,300
Purchases	9,400	5,100
End of year	**757,800**	**748,400**
Add: Accrued interest	13,103	12,869
More than 5 years	**770,903**	**761,269**

13. CLIFTON HERITAGE AUTHORITY BONDS

The Bank is the registrar for the Clifton Heritage Authority Bonds guaranteed by The Bahamas Government. The total allotment of the bonds is $24,000,000. The maturity dates are as follows:

Maturity dates	Interest rates	Principal Amount
Due on 20 May 2025	1/2% per annum above Prime rate	B$ 8,000,000
Due on 20 May 2030	5/8% per annum above Prime rate	B$ 8,000,000
Due on 20 May 2035	3/4% per annum above Prime rate	B$ 8,000,000
		B$24,000,000

	2007 $	2006 $
At beginning of year	633,700	-
Purchases	-	633,700
End of year	**633,700**	**633,700**
Add: Accrued interest	4,273	4,375
More than 5 years	**637,973**	**638,075**

14. BAHAMAS GOVERNMENT TREASURY BILLS

As at 31 December 2007, the Bank has holdings of Bahamas Government Treasury bills totaling $143,460,999 (2006: $52,214,845) plus accrued interest of $637,023 (2006: $185,845) that mature between 4 January 2008 and 7 May 2008 and which are discounted at rates varying from 2.65% to 3.33%. Due to the short-term nature of these securities, amortized cost approximates fair value.

15. DEPOSITS BY COMMERCIAL BANKS

Deposits by commercial banks consist of current account balances deposited as statutory reserves in accordance with Section 19 of the Act.

The present level of the statutory reserves applicable to commercial banks is 5.00% of the total Bahamian dollar deposit liabilities, of which at least 4.00% must be placed on deposit with the Bank. These deposits are interest free and are repayable on demand subject to maintenance of minimum balances required by the Act.

16. DEPOSITS BY INTERNATIONAL AGENCIES

The Bank is designated as the fiscal agency for the Commonwealth of The Bahamas. Deposits by international agencies include deposits in Bahamian currency by the World Bank, the International Monetary Fund, the Inter-American Development Bank, the Caribbean Development Bank and the Commission of the European Development Fund. These deposits are interest free and are repayable on demand.

17. INTERNATIONAL MONETARY FUND ALLOCATION OF SPECIAL DRAWING RIGHTS

In accordance with a resolution of the Board of Governors of the IMF, effective 11 December 1978, The Bahamas became a participant in the Special Drawing Rights Department of the IMF, receiving a total allocation of SDR10,230,000 between 1979 and 1981. The Special Drawing Rights allocation bore interest during the year at rates varying between 3.50% and 4.32% (2006: 4.31% and 5.48%), includes accrued interest of $95,387 (2006: $95,576) and is repayable on demand.

18. EQUITY AND RESERVES

a. **Capital management** - The Bank's objectives when managing capital, which is a broader concept than 'equity' on the face of the balance sheet, are:
   - To comply with the capital requirements outlined in Sections 6 and 7 of the Act;
   - To safeguard the Bank's ability to continue as a going concern so that it can continue to provide central banking facilities for the Commonwealth of The Bahamas; and
   - To maintain a strong capital base to support the development of the Bahamian economy.

18. EQUITY AND RESERVES (Continued)

Capital adequacy and the use of regulatory capital are monitored by the Bank's management, and in accordance with the guidelines established by the Act. Provision is made in Sections 6(1) and (2) of the Act for the Paid Up portion of the authorized capital of the Bank to be increased each year by an amount from the Consolidated Fund at such times and in such amounts as the Board, with the approval of the Minister, may determine. At 31 December 2007, the Bank's paid up capital was equal to the authorized capital of $3,000,000.

b. **Exchange equalization account** - Under the terms of Sections 32(2)(a) and 32(2)(b) of the Act, this account represents the net unrealized profits or losses arising from the revaluation of foreign currency assets and liabilities of the Bank at the balance sheet date.

c. **Contingency reserve** - This reserve is maintained in accordance with the provisions of Section 7(1) of the Act.

d. **Other reserves** - In accordance with the provisions of Section 7(1) of the Act, the Bank has determined to transfer $3,958,867 from other reserves to general reserves. In 2006, an amount of $Nil was transferred from other reserves to general reserves.

e. **General reserves** - Section 7(2) of the Act requires that, at the end of any year where the amount in the general reserves exceeds twice the authorized capital of the Bank or 15% of its demand liabilities, whichever is greater, the excess shall be paid to the Consolidated Fund unless the Minister of Finance determines otherwise.

The balance of the general reserves at the year end amounted to $105,567,869 (2006: $93,591,406) equivalent to 15.00% (2006: 15.51%) of demand liabilities prior to a provision of $Nil (2006: $3,618,000) to be paid into the Consolidated Fund.

19. INCOME

	2007	**2006**
	$	**$**
Interest income	33,655,962	31,421,837
Unrealized exchange (loss)/gain	(454,940)	73,248
Other operating income	1,686,979	1,697,352
	34,888,001	**33,192,437**

20. EXPENSES

	2007	2006
	$	$
General & administrative expenses	8,572,806	13,015,732
Staff costs	12,879,534	11,047,847
Depreciation expense	1,607,630	1,608,253
Interest expense	647,375	550,976
	23,707,345	**26,222,808**

21. THE DEPOSIT INSURANCE CORPORATION

In accordance with Section 5(1) of the Protection of Depositors Act, 1999, the Bank has made an initial capital contribution of $500,000 representing 100% of the paid-up portion of the capital of the Deposit Insurance Corporation. This Corporation was established to manage The Deposit Insurance Fund, which was established to protect funds deposited with member institutions.

In the opinion of the Directors, the Bank does not have the power to govern the financial and operating policies of the Deposit Insurance Corporation so as to attain benefits from its activities. Consequently, the Deposit Insurance Corporation is not treated as a subsidiary in these financial statements.

Additionally, the Directors do not consider that the investment in the Deposit Insurance Corporation will be recoverable, and consequently the Bank has made a full provision against this investment.

22. COMMITMENTS

The Bank is committed to rent office space under an operating lease. The Bank is committed to the following future payments under the lease agreement:

Years	**$**
2008	421,397
2009	387,638
2010	89,180

23. CONCENTRATIONS OF ASSETS AND LIABILITIES

The Bank has the following concentrations of assets and liabilities:

EXTERNAL ASSETS	2007	2006
	%	%
Geographic Region		
North America	99.77	99.97
Europe	0.20	-
Other	0.03	0.03
Industry		
Financial Sector	100.00	100.00

OTHER ASSETS	2007	2006
	%	%
Geographic Region		
Bahamas	100.00	100.00
Industry		
Government Sector	100.00	100.00

DEMAND LIABILITIES	2007	2006
	%	%
Geographic Region		
Bahamas	99.94	99.99
Other	0.06	0.01
Industry		
Financial Sector	100.00	100.00

OTHER LIABILITIES	2007	2006
	%	%
Geographic Region		
North America	100.00	100.00
Industry		
Financial Sector	100.00	100.00

24. RELATED-PARTY TRANSACTIONS

The Bank could be regarded as related to state corporations such as Bahamas Electricity Corporation (BEC) and National Insurance Board (NIB). However, the only transactions that the Bank has with such related entities are purely on commercial terms.

The Bank provides certain services to the Government of The Bahamas in accordance with its mandate under Sections 26 to 28 of the Act.

The Bank's senior management personnel are regarded to be its only key management personnel.

The following transactions were carried out with related parties:

a. Compensation:	**2007**	**2006**
	$	**$**
Salaries and short-term employee benefits	1,365,517	1,394,686
Termination benefits	-	-
	1,365,517	**1,394,686**

b. Loans:	**2007**	**2006**
	$	**$**
		Note 31
Beginning of the year	837,012	964,286
Loans advanced during the year	27,352	32,900
Loan repayments received	(139,306)	(160,174)
End of year	**725,058**	**837,012**

25. CONTINGENT LIABILITIES

The Bank is party to asserted and unasserted claims in the normal course of business, which are at various stages of the judicial process. The Bank is defending all such claims and is of the opinion that the outcome, which cannot presently be determined, will not adversely affect its operations and financial statements.

In connection with the IMF subscription, the Bank has issued promissory notes which are regarded as contingent liabilities (see Note 7).

26. OFF BALANCE SHEET ITEMS

The Bank has off balance sheet items totalling $40,907,368 (2006: $37,657,946). These items, which are held in a fiduciary capacity, comprise offsetting assets consisting of bank accounts, and liabilities consisting of dormant retail customer accounts of $40,907,368 (2006: $37,657,946).

Certain dormant retail customer accounts, which are received in foreign currencies, are invested in the same currency. These currencies are converted to Bahamian Dollars at the rate of exchange prevailing at the date of accepting their funds, and listed as a memorandum account in the trial balance. Foreign currency deposits are repaid by liquidating investments in the same currency, which does not involve currency conversion.

27. FAIR VALUE OF FINANCIAL INSTRUMENTS

With the exception of marketable securities, whose fair value is as stated in Note 6, and those financial assets classified as loans and receivables with an aggregate carrying value of $359,340,044 (2006: $201,145,932) and aggregate fair value of $358,156,634 (2006: $200,828,867), the Directors consider that all of the Bank's financial assets and liabilities are carried at amounts approximating their fair value.

28. MATURITIES OF FINANCIAL INSTRUMENTS

Except as otherwise disclosed in Notes 6 to 15, the Bank's significant financial assets and liabilities mature within one year, of the balance sheet date.

29. FINANCIAL RISK MANAGEMENT

The Bank's activities expose it to a variety of financial risks and those activities involve the analysis, evaluation, acceptance and management of some degree of risk or combination of risks. Taking risk is core to the financial business, and the operational risks are an inevitable consequence of being in business. The Bank's aim is therefore to achieve an appropriate balance between risk and return and minimise potential adverse effects on the Bank's financial performance.

The Bank's risk management policies are designed to identify and analyse these risks, to set appropriate risk limits and controls, and to monitor the risks and adherence to limits by means of reliable and up-to-date information systems. The Bank regularly reviews its risk management policies and systems to reflect changes in markets, products and emerging best practices.

Risk management is carried out by the investment and monetary policy committees under policies approved by the Board of Directors. The committees identify, evaluate and hedge financial risks in close co-operation with the Bank's operating units. The Board provides written principles for overall risk management, as well as written policies covering specific areas, such as foreign exchange risk, interest rate risk, credit risk and financial instruments.

The most important types of risks are credit risk, liquidity risk, market risk and other operational risk. Market risk includes currency risk and interest rate risk.

29. FINANCIAL RISK MANAGEMENT (Continued)

Credit risk

The Bank takes on exposure to credit risk, which is the risk that a counterparty will cause a financial loss for the Bank by failing to discharge an obligation. Significant changes in the economy, or in the health of a particular segment that represents a concentration in the Bank's portfolio, could result in losses that are different from those provided for at the balance sheet date. Credit exposures arise principally in loans and advances, debt securities and other bills into the Bank's asset portfolio. The credit risk management and control are monitored by the Investment Committee and reported to the Board of Directors regularly.

The Directors do not consider that the Bank is exposed to any significant credit risk because its financial assets consist primarily of cash and securities issued or guaranteed by either foreign Governments or The Bahamas Government.

Market risk

The Bank takes on exposure to market risk, which is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market prices. Market risks arise from open positions in interest rate, currency and equity products, all of which are exposed to general and specific market movements and changes in the level of volatility of market rates or prices such as interest rates, credit spreads, foreign exchange rates and equity prices. The Bank's exposure to market risk is from its financial investment portfolios.

The market risks arising from the Bank's activities are monitored by the investment and monetary policy committees. Regular reports are submitted to the Board of Directors and operating units.

Foreign exchange risk

The Bank takes on exposure to the effects of fluctuations in the prevailing foreign currency exchange rates on its financial position and cash flows.

The Bank's exposure to foreign exchange risk is largely limited by the fact that fluctuations in the prevailing foreign currency exchange rates are for the account of the Government under the terms of Sections 32(2)(a) and 32(2)(b) of the Act.

Interest rate risk

Cash flow interest rate risk is the risk that the future cash flows of a financial instrument will fluctuate because of changes in market interest rates. Fair value interest rate risk is the risk that the value of a financial instrument will fluctuate because of changes in market interest rates. The Bank takes on exposure to the effects of fluctuations in the prevailing levels of market interest rates on both its fair value and cash flow risks. Interest margins may increase as a result of such changes but may decrease or create losses in the event that unexpected movements arise. The level of mismatch of interest rate repricing that may be undertaken by the Bank is monitored frequently by the investment and monetary policy committees.

29. FINANCIAL RISK MANAGEMENT (Continued)

Interest rate risk (Continued)

Certain of the Bank's financial assets and liabilities are exposed to interest rate risk. Marketable securities carry an average yield of 4.20% (2006: 4.46%); however, if these securities had a reduced average yield of 3.17% (2006: 3.14%), derived from their varying yields at the lower end of the spectrum, income for the year and equity at year end would have been reduced by $4,000,908 (2006: $5,382,747). Had the yield been tilted towards the higher end of the spectrum, to 4.60% (2006: 4.625%), income for the year and equity at year end would have been increased by $1,547,075 (2006: $665,245).

At 31 December 2007, should interest rates have risen by 25 basis points with all other variables remaining constant, the increase in equity and net income for the year would amount to approximately $408,764, arising from funds placed on cash and deposits (2006: $402,016).

If interest rates had decreased by 25 basis points, the decrease in equity and net income for the year would amount to approximately $408,764 (2006: $402,016).

Liquidity risk

Liquidity risk is the risk that the Bank is unable to meet its payment obligations associated with its financial liabilities when they fall due, and to replace funds when they are withdrawn. The consequence may be the failure to meet obligations to repay depositors and fulfil commitments to lend.

The Bank manages its foreign liquidity risks through appropriate structuring of its foreign investment portfolios to ensure that the maturity profiles of foreign assets sufficiently match those of foreign commitments. This is monitored and managed on a regular basis. In addition, the Bank's foreign investment portfolio comprises mainly short-term, highly liquid investment instruments.

Liquidity risk management process

The Bank's liquidity management process, as carried out within the Bank includes:

- day-to-day funding, managed by monitoring future cash flows to ensure that requirements can be met, inclusive of replenishment of funds as they mature. The Bank maintains an active presence in global money markets to enable this to happen;
- maintaining a portfolio of highly marketable assets that can easily be liquidated as protection against any unforeseen interruption to cash flow;
- monitoring balance sheet liquidity ratios against internal and regulatory requirements; and
- managing the concentration and profile of debt and financial instrument maturities.

30. CONTRIBUTORY DEFINED BENEFIT PENSION PLAN

The movement in the defined benefit obligation over the year is as follows:

	2007	2006
	$	$
Current service cost	1,365,716	1,435,571
Interest cost	1,703,810	1,601,617
Contribution by plan participants	361,668	344,995
Actuarial gain	535,090	510,854
Benefit paid	(596,830)	(979,556)
End of year	**3,369,454**	**2,913,481**

The amount recognized as an asset in the balance sheet in respect of the Bank's defined benefit contributory pension plan is as follows:

	2007	2006
	$	$
Present value of funded obligations	(29,949,990)	(28,012,384)
Fair value of plan assets	36,976,991	34,218,125
	7,027,001	6,205,741
Unrecognized actuarial gains	(3,926,543)	(3,336,723)
Net assets calculated in accordance with paragraph 54 of International Accounting Standard 19	**3,100,458**	**2,869,018**

30. CONTRIBUTORY DEFINED BENEFIT PENSION PLAN (continued)

The expense recognized in the income statement in respect of the Bank's defined benefit pension plan is as follows:

	2007	2006
	$	$
Current service cost	1,004,048	1,090,576
Interest cost	1,703,810	1,601,617
Expected return on plan assets	(2,239,286)	(2,087,072)
	468,572	**605,121**

Movements in the net assets recorded in the balance sheet are as follows:

	2007	2006
	$	$
Net assets at beginning of year	2,869,018	2,810,574
Net expense recognized in the income statement	(468,572)	(605,121)
Employer contributions	700,012	663,565
Net assets at end of year	**3,100,458**	**2,869,018**

Principal actuarial assumptions used at the balance sheet date are as follows:

	2007	2006
Discount rate	6.00%	6.00%
Expected return on plan assets	6.50%	6.50%
Expected rate of salary increase at age 18	9.00%	9.00%
Expected rate of salary increase at age 59	2.00%	2.00%
Average expected remaining working lives of employees (years)	19.00	19.00

The actual return on plan assets during the year was $2,294,016 (2006: $2,094,830).

31. CORRESPONDING FIGURES

The corresponding figures disclosed in Note 24 for loans to related parties have been restated to conform with the presentation adopted for the current year.

Additionally, in the 2006 financial statements investments in Bahamas Government registered stocks, Bahamas Government Treasury bills, Bridge Authority bonds and Bahamas Mortgage Corporation bonds were described as available-for-sale securities. These investments are now described as loans and receivables. This change does not have any financial impact on the carrying values of these investments.

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