FINANCIAL MARKET BRIEF

13th January 2017

CFAL

TOP STORY - LOCAL

A review of the Bahamas' Financial Health…was the S&P Downgrade Justified?

The Government of the Bahamas is approximately three and a half years into its 'medium-term fiscal consolidation plan' which it initiated at the beginning of the 2013/14 fiscal year (FY). The intent of the plan as articulated by the Minister of Finance and Prime Minister, Mr. Perry Christie, during the 2013/14 Budget Communication was to "eliminate the GFS Deficit and return the Government's finances to surpluses; reverse the Government's primary balance position from a deficit to a surplus; enhance economic growth and employment prospects; reform the country's tax system with the implementation of Value Added Tax (VAT) and the modernization of the real property tax system; establish a Central Revenues Agency; and reduce the burden of public debt over time". In assessing the Government's performance, as it relates to the country's fiscal position, it is important to first define fiscal consolidation. The term fiscal consolidation refers to "concrete policies aimed at reducing government deficits and debt accumulation". Notwithstanding the government's ambitious stance on improving the country's public finances, it has a long way to go in stabilizing or reducing the debt share and deficit levels and putting the country's finances on a path to improved economic health.

Standard and Poor's (S&P) more or less confirmed the Bahamas' untenable economic position when it downgraded the country's foreign and local currency sovereign credit ratings by one notch to 'BB+/B' from 'BBB-/A-3' in December. This latest downgrade by S&P has in effect reduced the Bahamas' sovereign credit rating to speculative grade or "junk" status. The rating agency also assigned a stable outlook. S&P's rationale for the ratings downgrade included "weaker than expected economic growth; slower pace in realizing benefits from fiscal consolidation plan; weaker public finances due to lower GDP growth; increased levels of external debt; double-digit unemployment, high nonperforming loans in the banking system and, high household indebtedness". The country's BB+/B sovereign ratings indicate that "it faces major ongoing uncertainties or exposure to adverse business, financial or economic conditions which could lead to the obligor's inadequate capacity to meet its financial commitment on the obligation". In essence, the Bahamas' speculative grade or "junk" status means that the country is at risk for defaulting on its debt obligations, albeit less vulnerable than other countries rated within this category. While some may disagree with S&P's assessment of the country's finances, a closer look at the economic numbers and trends may shed more light on the country's fiscal health.

We start with GDP which is perhaps the most important indicator for measuring the success of an economy. The local GDP, which is usually quoted in both real and nominal terms, is the total value of all goods and services produced within the Bahamas over a given period. In the case of the Bahamas, this economic statistic is usually assessed on an annual basis. The current nominal GDP, 2015, stands at $8.85 billion. Real GDP, however, which measures economic growth, is at $7.79 billion and has contracted 1.66% in 2015 and 0.52% in 2014. The Bahamas, as evidenced by recorded GDP numbers, is in a sustained low growth environment – the GDP growth rate has averaged 1.00% over the past 10 years and is expected to be 0.30% in 2016 and 1.20% in 2017 (S&P). This period of negative and ultra-low economic growth has placed a strain on government revenues, making it more difficult for the government to achieve its fiscal consolidation goal of eliminating the GFS Deficit and generating a primary budget surplus; and has contributed to the downgrade by S&P. Policy makers have insisted that Baha Mar's impending opening should have positively impacted growth projections and prevented the downgrade to "junk" bond status. For that, it's important to note that the future success of Baha Mar is uncertain and by all accounts Baha Mar should have officially opened in December 2014; and has consistently missed several scheduled openings since then. Notwithstanding the failure of Baha Mar to contribute to economic growth in the past, S&P did, however, change the outlook from negative to stable in anticipation of Baha Mar's 2017 opening and other smaller tourism related developments.

Let's now focus on the Bahamas' debt ratios. Over the past eight years, the Bahamas has seen a sustained deterioration in its debt ratios. With the government continuously running deficits, the Bahamas' total debt share will certainly continue to increase. In total, the Bahamas now owes $6.77B, which is equivalent to 76.49% of GDP. Less than a decade ago, in 2008, the debt to GDP ratio stood at a healthy 38.96%. This deterioration in public finances can be attributed to an equally substantial increase in the GFS deficit to GDP from 1.83% in 2008 to 4.49% in 2015, after peaking at 6.48% in 2013. The GFS deficit is the gap between government spending and transfers to public corporations and government revenues collected. While the government has made tremendous strides in reducing the GFS deficit relative to GDP from its high of 6.48% to about 3.5% for FY 2015/16, it has consistently missed its aggressive deficit targets stated in consecutive Budget Communications of 1.0% - 2.0% of nominal GDP. The Bahamas' foreign currency debt has also skyrocketed from $387.50M or 4.70% of GDP in 2008 to $1.76B or 19.88% of 2015 GDP at the end of September 2016. This growing external debt level has also negatively impacted the country's sovereign rating. The Bahamas' primary challenge in reducing its debt stock is the country's prolonged weak economic growth, and unless there is a significant boost in GDP growth, the country's debt levels will likely continue to accelerate. Improvements in the country's public debt ratio will require a bold commitment on the Government's part to implement fiscal reforms that will spur economic growth and fiscal stimulus. The focus on increased taxation while excluding fiscal austerity is not working, as unemployment remains relatively high and wage growth has stalled. To the government's credit, VAT collections have been successful, standing at $1.1 billion from January 2015 – September 2016. However, growth in overall government revenues has softened. This tapering in government revenues coupled with increased government spending (which has soared from 15.98% of GDP during FY 2005/06 to 24.05% during FY 2015/16) is hindering substantial reductions to the GFS deficit and driving debt numbers higher than projected figures.

Sovereign credit ratings have become especially important over the past decade due to the globalisation of markets and cross border investments. With the Bahamas' growing foreign debt stock, it has become increasingly important for the country's credit quality to be assessed by the major credit rating agencies. Merely proclaiming aggressive debt and deficit targets in successive Budget Communications will not favourably impact the country's sovereign debt rating. Rather, tangible results reflected in economic numbers and supported by sound economic policies will go a long way in reversing the country's sovereign debt rating decline and return it to investment grade.

WEEKLY MARKET REPORT - LOCAL

BISX INDEX	
13-Jan-17	1,922.52
Weekly %	0.08%
YTD %	-0.81%
Market Cap $	3.954B

MARKET MOVERS	
Daily Volume Avg.	27,175
Advancers	1
Decliners	1
Unchanged	33

COMPANY NAME	CLOSING PRICE	1-WEEK CLOSING PRICE	CHANGE %	52-WEEK HIGH/LOW	VOLUME
Advancers					
Commonwealth Brewery	$11.93	$11.91	0.17%	15.50/12.59	1,000
Decliners					
Consolidated Water	$2.10	$2.12	-0.94%	2.72/2.18	-

DIVIDENDS	Dividend Rate	Record Date	Payment Date
Focol Holdings Pref A& C	6.25%	30-Dec-16	11-Jan-17

Market Summary

The local market ended this week with 108,699 shares crossing the exchange with 14 trades to accumulate a value of $504,899.73. The BISX All-Share Index gained 1.55 points or 0.08 percent to end the week at 1,922.52. Year to date the Index is down 15.69 points or 0.81 percent.

This week's value and volume leader was AML Foods Ltd. (AML) moving 100,000 shares in 1 trade to accumulate a value of $438,000.00. The remaining volume this week was attributed to: Arawak Cay Port Development Ltd. (APD) - 30 shares in 1 trade, Cable Bahamas (CAB) - 400 shares in 1 trade, Commonwealth Brewery (CBB) - 1,000 shares in 4 trades, Commonwealth Bank Ltd. (CBL) - 1,100 shares in 1 trade, FamGuard (FAM) - 3,444 shares in 2 trades, Finco (FIN) - 525 shares in 2 trades and ICD Utilities (ICD) - 2,200 shares in 2 trades.

Notice

Cable Bahamas Ltd. (CAB): Ordinary shareholders dividend payments have been suspended until June 30th 2017.

EQUITY INDICES	LEVEL	1 WEEK	QTD	YTD	12 MOS.
BISX (The Bahamas)	1,922.52	0.08%	-0.81%	-0.81%	5.38%
S&P 500	2,274.64	-0.10%	1.60%	1.60%	20.33%
Dow Industrials (DJIA)	19,885.73	-0.39%	0.62%	0.62%	23.12%
NASDAQ	5,574.12	0.96%	3.55%	3.55%	23.16%
FTSE All-Share	7,337.81	1.77%	2.73%	2.73%	23.10%
S&P/TSX Comp	15,497.28	0.01%	1.37%	1.37%	27.34%
STOXX Europe 50	3,324.34	0.10%	1.03%	1.03%	8.18%
Nikkei 225	19,287.28	0.00%	0.90%	0.90%	12.48%
German DAX	11,629.18	0.26%	1.29%	1.29%	16.75%
Hang Seng	22,937.38	0.00%	4.26%	4.26%	17.50%
MSCI Emerging Markets	896.64	1.76%	3.99%	3.99%	22.90%
COMMODITIES					
Gold Spot	1,197.34	2.11%	4.34%	4.34%	9.49%
Crude Oil	57.05	-1.06%	-0.02%	-0.02%	38.04%

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