

PRIVATE SECTOR ASSESSMENT OF BAHAMAS



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The Private Sector Assessment Report for the Bahamas was authored by Guillermo R. Alborta in 2012, and was commissioned by the Inter-American Development Bank (IDB), with funding from the Compete Caribbean Program, a regional private sector development, technical assistance initiative financed by the IDB, the United Kingdom Department for International Development (DFID) and the Department of Foreign Affairs, Trade and Development Canada (DFATD), and executed in partnership with the Caribbean Development Bank (CDB) (for more information and access to the full document visit Compete Caribbean www.competecaribbean.org).

This report, based on the Private Sector Assessment Report for the Bahamas, was formatted and edited by The Economist Intelligence Unit at the request of the Compete Caribbean Program, but was not authored by The Economist Intelligence Unit, and neither The Economist Intelligence Unit, nor its affiliates, accept any liability or responsibility for the content of this report or how it has been formatted.

Executive summary

The Private Sector Assessment Report (PSAR) for the Bahamas presents an overall assessment of private-sector development and recommendations for facilitating and accelerating private investment and growth. It draws on both primary and secondary data sources. Primary data analyses were derived from interviews with key stakeholders from the domestic private and public sectors as well as interviews with regional and international agencies. A listing of the main stakeholders interviewed is documented in the original country report.¹ Secondary data were utilized to describe the state of the country at both the micro and macro levels. In addition to these specific elements of the research, the development of the PSAR was assisted by consultations organized under the Caribbean Growth Forum (CGF).²

The Bahamas PSAR evaluates the productive sector; the challenges posed by the business climate and an inadequate workforce; the promising dynamism evident in traditional and emerging sectors; and policy recommendations for priority areas. It identifies educational and workforce-skills improvements; infrastructure provision; the creation of an enabling environment for private investment; and financial support for SMEs and entrepreneurial development as key actions that are required to stimulate the Bahamian economy.

As a tourism-dependent economy, the Bahamas is reliant on regular tourist arrivals, and this renders the country vulnerable to shocks in key tourism source markets, particularly the US. According to the World Travel and Tourism Council, the outlook for the sector is positive, with forecast sustained growth in the local tourism industry of 2.6% annually in the period to 2022, and a related contribution to employment growth, with employment in the sector forecast to increase by around 23% between 2011 and 2022. However, the industry is changing, and in order to realize these forecasts the country needs to maintain an advantage in the sector over global competitors, which are steadily improving their tourism offerings.

In addition, the country needs to diversify its economic base towards the mining and manufacturing sector, which is displaying notable dynamism, as reflected in its compound average growth rate for mining and quarrying of around 7.5% a year between 2000 and 2011, and the positive change in the revealed comparative advantage of the Bahamas in non-traditional export products, such as aragonite and salt. These sectors, which are currently small but are fast-growing, represent prospects for the growth of new industries. To support diversification towards these emerging sectors, efforts should be made to implement the Road Map for the Advancement of Science and Technology

¹ The original reports can be found on Compete Caribbean's website: <https://www.competecaribbean.org>.

² The CGF is a facilitated methodology for public-private dialogue around issues central to private-sector development and growth. It brings a non-traditional approach to the greatest challenge currently faced by the region: creating sustainable and inclusive growth. The Forum also aims to facilitate an action-oriented dialogue around key policy reforms needed across three thematic areas: investment climate, skills and productivity, and logistics and connectivity. The CGF is a joint initiative by the Compete Caribbean Program, the Inter-American Development Bank, the World Bank, and the Caribbean Development Bank. It is supported by the Department of Foreign Affairs, Trade and Development Canada, the UK's Department for International Development, the CARICOM Secretariat and the University of the West Indies

and to provide related support for research and development. The agricultural sector, although limited by the country's geography and factor endowment, is also cited as a potential growth industry that has been targeted as such by the government.

Domestic and foreign companies alike have played key roles in sustaining the Bahamas' economic growth and trade performance. There is strong private-sector organization through sector-specific representative bodies, particularly in the country's mainstay sectors. The development of economic links between foreign investors and domestic sectors will be an important strategy in terms of diversifying the economy, promoting private-sector activity (particularly by small and medium-sized enterprises) and supporting employment growth.

Bahamian businesses identify an inadequately educated workforce and customs and trade regulation as the most bothersome problems facing them. Whereas issues such as crime, theft and disorder are identified by large firms as major constraints, access to finance affects medium-sized enterprises in particular, while practices within the informal sector are noted as key obstacles for smaller businesses. Moreover, infrastructure weaknesses, including inadequate supplies of electricity and water, can increase costs, disrupt production and reduce profitability for firms of any size. In addition, losses during trade or exportation are highly significant for Bahamian businesses of all sizes. Efforts are already under way to close the skills gap.

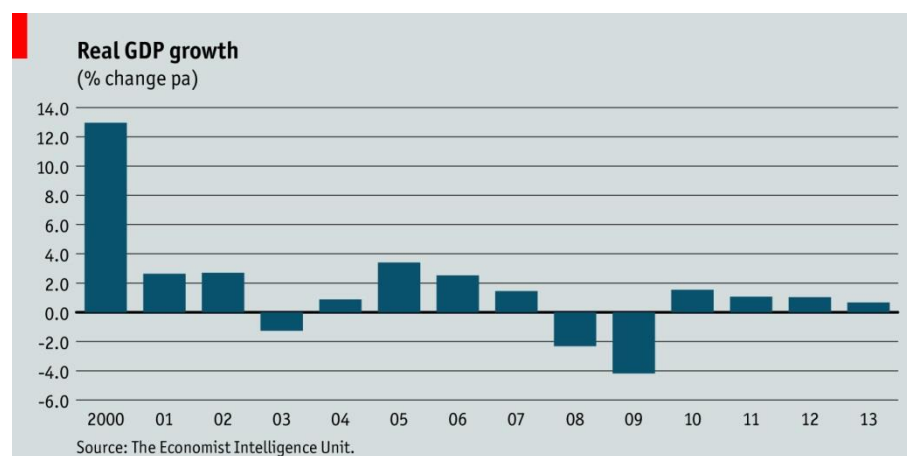
Of the many policy recommendations that could be made to improve the business environment, the PSAR emphasizes the importance of addressing the challenges of education and workforce skills, the quality of infrastructure, access to finance, innovation, and environment and land use.

I. Private sector assessment

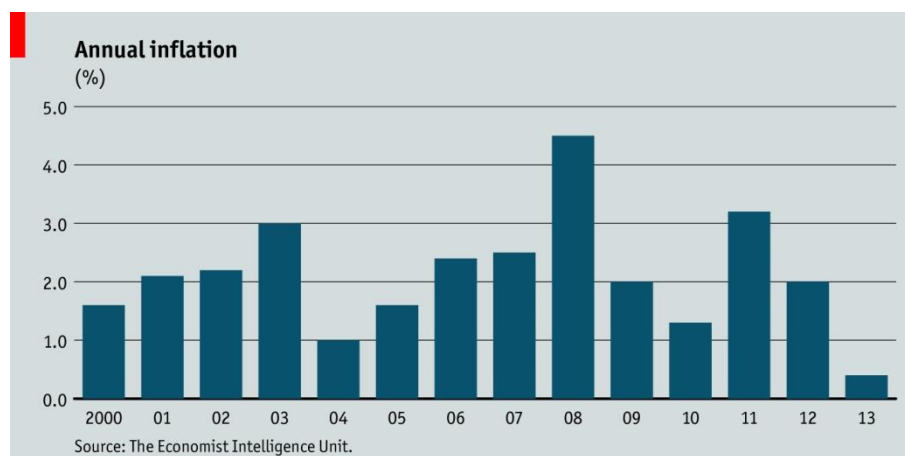
Background Private-sector development is a priority for the Bahamas' leaders, and is part of the government's latest policy document, Vision 2030: Charter for Governance—Believe in the Bahamas. In this document, the government notes the urgent need for economic change and the need for a long-term development plan. The document establishes both a short-term agenda, focusing on 12 issues that the current administration intended to address during its first 100 days after taking office in May 2012, and a long-term vision for the period to 2030 involving the explicit and vital participation of the private sector. The initial priorities relate to improving human-resources capacity through education and training, improving social-protection systems and restructuring government ministries. The role of the private sector is viewed as fundamental.

Macroeconomic overview The Bahamas is a small archipelagic island state with an open economy. Its economy has been largely dominated by two services sectors that account for roughly two-thirds of GDP and employ most of the labour force, namely tourism (and tourism-related construction) and financial services. Industrial production, manufacturing and agriculture are limited by the country's modest geographical area and factor endowment.

Figure 1



The Bahamas will continue to benefit from the openness of its economy. It is expected that the government will seek to attract visitors and investment from non-traditional, fast-growing markets in Latin America and Asia. Tourist arrivals from North American remain dominant because of the proximity of that market, while efforts to diversify economic activity have had only a weak impact, as tourism (particularly from the US) continues to dominate investment flows and government policymaking. Plans to open up the electricity industry to greater private-sector involvement, and the partial reversal of a moratorium on offshore oil drilling, signal a pragmatic approach to policymaking. Annual inflation averaged just over 2% between 2000 and 2013. The Bahamian dollar has been pegged to the US dollar at parity since 1973, and there is a strong commitment to maintenance of the peg.

Figure 2

After contracting by an average of over 3% a year in 2008-09 on the back of the global financial crisis, the Bahamian economy has since picked up, albeit weakly. Growth averaged just over 1% in 2010-13. The construction sector will continue to benefit from several large-scale tourism-related investments, most notably the Baha Mar tourism complex, the first phase of which is due to open in spring 2015. Growth will be underpinned by foreign investment in tourism-related and infrastructure projects, which will continue to boost construction activity, employment and income. The forecast pick-up in the US economy in the coming period will slowly boost arrivals and visitor spending. However, much will depend on the performance of the Baha Mar resort. Unemployment in the Bahamas, which peaked in 2010, is forecasted to continue to decline gradually, boosting domestic demand. GDP per head averaged US\$18,200 (at purchasing power parity exchange rates) in 2010-13.³

Due to the low or negative rates of economic growth recorded since 2005, unemployment has been relatively high, meaning that job creation and labour market reform is a fundamental objective. The unemployment rate increased steadily from 6.9% in 2001 to a high of 15.9% in 2011, and is estimated at 14.3% in 2014, with unemployment among young people (those aged 15-24) standing at 28%. The services sector provides the largest share of employment in the country, with women considerably more reliant on service industries for employment than men.

The Bahamas continued to post wide trade and current-account deficits in 2013. Average oil prices moderated throughout that year, and previously surging import demand, linked to major tourism-related construction projects, also ebbed (and will fall further as the massive Baha Mar resort nears completion). These trends are estimated to have narrowed the trade deficit to US\$2.2bn in 2013, although the shortfall remained large at the equivalent of 26.3% of GDP. A gradual recovery in most import segments due to economic recovery and construction work on a major new tourism venture will again force up imports again in 2014-15. The Economist Intelligence Unit forecasts that growth in imports will outpace a mild upturn in exports in the next two years, thus

³ In 2012 GDP per capita stood at US\$21,540 (PPP international currency), according to the World Bank.

preventing any further narrowing of the trade deficit, which is forecast to average just over 27.5% of GDP in 2014-15.

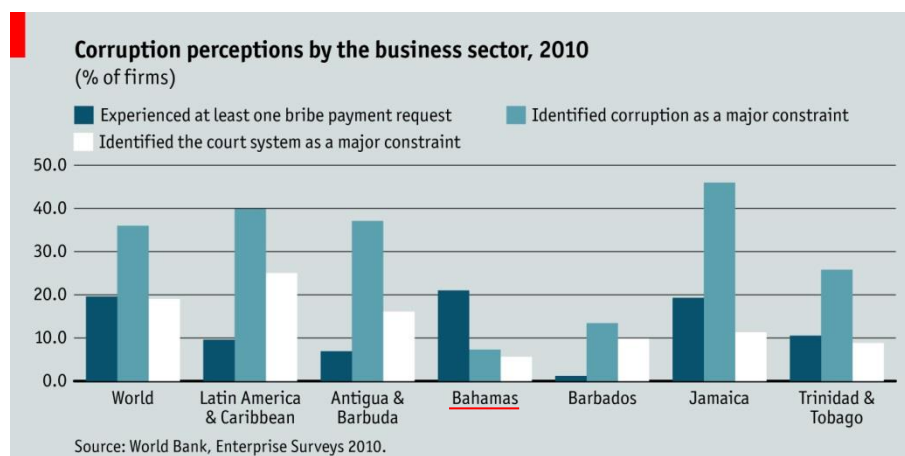
As a result of weak financial services income and a further upturn in import demand, driven by the construction sector, the current-account deficit is forecast to widen again, to the equivalent of 20.8% of GDP, in 2014. The commissioning of new tourism capacity and related services will provide a major boost to services inflows in 2015 and beyond. Remittance income from Bahamians working abroad is expected to continue its recent modest recovery in 2014-15 as job prospects in the US pick up. The combined effect of these trends will be a slight narrowing of the current-account deficit, to 19.5% of GDP, in 2015.

Institutional effectiveness

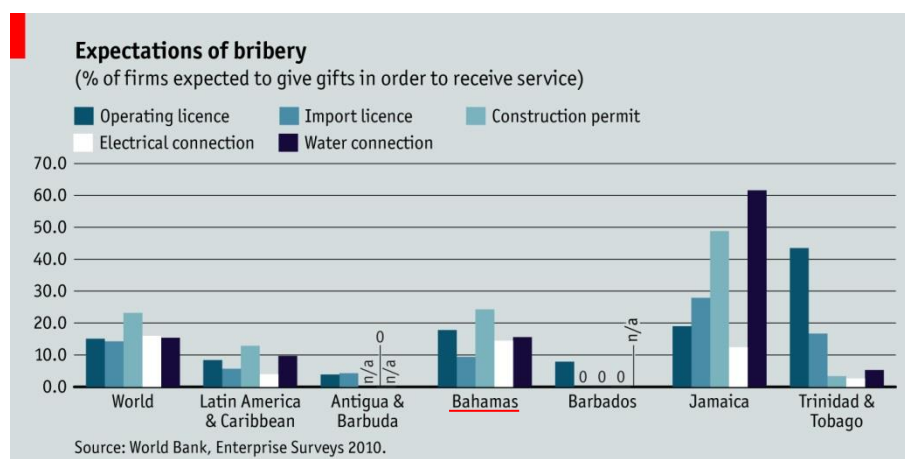
The Bahamas benefits from a stable political environment, with democratic elections held every five years as required by the constitution. While there are minor ideological differences between the two major political parties, the Progressive Labour Party, which currently leads the government, and the Free National Movement, as well as a more recent arrival on the scene, the Democratic National Alliance, all these parties are largely committed to democracy, the rule of law and the operation of free markets. However, there is a need to strengthen public institutions, and reforms should include the promotion of efficient co-ordination between government agencies and private-sector bodies.

Both domestic and foreign companies have played a key role in sustaining the country's economic growth and trade performance. The World Bank's 2010 Enterprise Survey for the Bahamas reported that senior management spent less than 5% of their time dealing with issues relating to government regulations that affect domestic and foreign companies. This figure is comparable to the responses in Antigua and Barbuda and also Barbados, but is higher than that for Jamaica. Firms in Trinidad and Tobago reported significantly higher regulatory time burdens.

In connection with institutional strength, a large proportion of enterprises have experienced bribe requests. There are concerns about the lack of transparency and the prevalence of discretionary procedures for obtaining licences and permits. Figure 3 shows perceptions of corruption in the Bahamas compared with other countries in terms of firms' experiences of bribe requests, their identification of corruption as a major constraint on doing business and their citing of problems with the court system as a major constraint.

Figure 3

Perceptions regarding gifts given to obtain permits and licences in the Bahamas are roughly on a par with the global average.⁴ The Bahamas' score is worse than the Latin American regional average or Trinidad and Tobago regarding the expectation of bribe payments to obtain construction permits and electricity and water connections. Almost 20% of the firms surveyed in the Bahamas felt that they were expected to give gifts to public officials “to get things done”—a phrase that could cover a wide range of actions. Whereas crime, theft and disorder appear to be important problems for large enterprises, medium-sized and small firms are not as concerned about these issues. On a positive note, very few firms (5.6%) claim that the judicial courts are a major obstacle to conducting business.

Figure 4

Components of the productive sector

This section addresses the current state of the private sector in the Bahamas, and provides a broad overview of major trends and the sector's primary components. A later section will discuss potential emerging growth sectors.

Overview of the sector

⁴ Average of countries surveyed for the World Bank's 2010 Enterprise Surveys.

The Bahamas is a highly entrepreneurial society with a relatively large private sector. In 2011 the private sector contributed around 80% of GDP⁵ and 78.7% of total employment⁶. In spite of the Bahamas' hyper-specialization in tourism and finance, there is export activity in a range of merchandise products. However, the level of diversification as measured by the number of different products exported is significantly lower than in comparator countries.

Tourism (consisting of the hotel and restaurant sector) and financial services (provided by commercial banks, insurance firms and other financial institutions) are the largest sectors of the economy measured in terms of their shares of GDP and employment. Both sectors are major foreign-exchange earners, and together they account for at least two-fifths of GDP directly and two-thirds indirectly. Their main indirect influence is reflected in construction, with other indirect effects observed in the wholesale and retail trade sector. In 2000 services value added accounted for 80.4% of GDP, and by 2013 the services sector's share in the economy had increased to 90.8%.

In 2013 the contribution of agriculture (including fishing) to gross value added (at market prices) stood at 1.8%, while that of manufacturing was around 3.7%; industry (including manufacturing) accounted for 6.8%. Overall economic growth in the Bahamas has been and will remain highly dependent on the performance of the services sector. However, industry and agriculture also hold significant prospects; mining, the smallest major sector, is also the fastest-growing.

In all sectors of the Bahamas' economy, a significant number of small- and medium-sized enterprises (SMEs) coexist with large domestic and international companies. (In the Bahamian context, small firms employ between one and four people, while medium-sized firms employ 10-49 and have sales below US\$250,000 annually.) According to the Bahamas Department of Statistics, in the year ending January 2011 there were an estimated 4,732 registered small and medium-sized firms on the island of New Providence (where the capital, Nassau, is situated), with firms with up to nine employees accounting for 87% of the total. The wholesale and retail trade industry accounted for the largest number of these firms, at 2,031, followed by accommodation and foodservice (493) and mining, quarrying, manufacturing, water supply, waste management and remediation, electricity activities and airconditioning supply (326 in total). The fewest registered firms were in the information and communications technology industry (43) and the arts, entertainment and recreation industry (51). On Grand Bahama there were 356 firms registered in the manufacturing sector in 2009, with an average of ten employees, with larger average company sizes of 38 employees in the general-purpose machinery subsector and 21 in the processed-meat, fish, fruit, vegetable and fats subsector. The 2011 Labour Force Report published by the Department of Statistics indicated that the four most important sectors in the Bahamas were tourism (comprising hotels, restaurants, wholesale and retail), which employed 30.7% of the labour force, financial services (consisting of financing, insurance, real-estate and other business

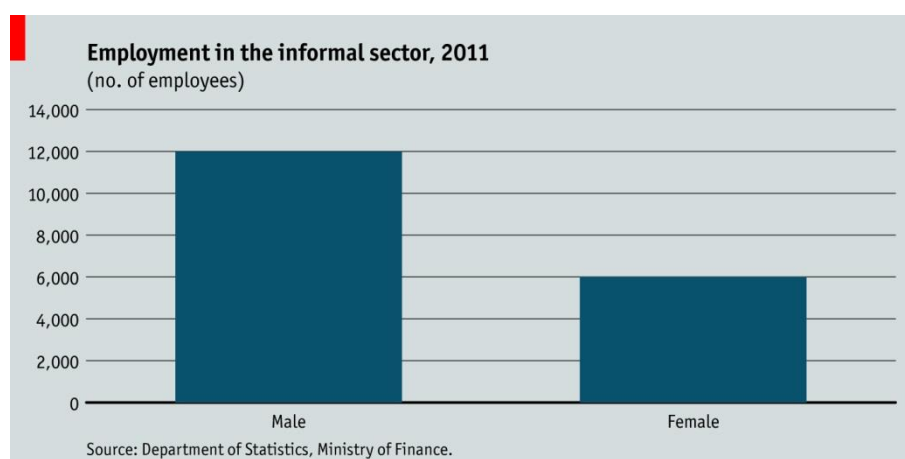
⁵ World Bank, World Development Indicators.

⁶ Bahamas Department of Statistics.

services), employing 25.4%, construction (25.1%), community, social and personal services (9.9%), manufacturing (3.2%), transport, storage and communications (2.7%) and agriculture, hunting, forestry and fishing (1.9%).

The Labour Force Report shows that female employment increased by 5.6% between 2009 and 2011, while male employment rose by 2.4%. The services sector provides the largest share of national employment, and women are considerably more reliant on services for employment than men. The construction, mining, agricultural and transport sectors predominantly employ male workers, whereas most employees in the community social services, finance, and hotel and restaurant sectors are women. Employment is evenly distributed by gender in wholesale and retail trade. Informal activities tend to be concentrated in retail. The wholesale and retail industry grew faster than any other industry between 2009 and 2011, with employee numbers rising by 16%. By contrast, the construction industry, in which male workers tend to predominate, experienced a decline of 18% in the period. Furthermore, although the majority of informal workers are male, recent trends show female participation in informal employment growing by 65% from 2009 to 2011, contrasting with an increase of only 20% in male participation. According to the Department of Statistics (DoS), in 2011 the informal sector employed 17,995 people, of whom 6,005 were women and 11,990 men (See Figure 5).

Figure 5



According to the DoS, in 2011 the informal sector grew more rapidly than the formal sector. Causes of informality on the part of companies worldwide include burdensome tax systems, rigid labour markets, high inflation and dominance of economies by agriculture. In the case of Bahamas, the current analysis suggests that a key factor determining the considerable size of the informal economy is labour market rigidities.

Agriculture and industry

The industrial sector has grown in importance to the Bahamian economy over the past two decades. In 2013 industry contributed 6.8% of gross value added (at market prices), of which manufacturing accounted for 3.9%. Major industries in the Bahamas include cement, oil-refining and transshipment, rum manufacturing, pharmaceuticals, and the manufacture of spiral-welded steel pipes. As a result of the long-standing Hawksbill Creek Agreement, the largest

segments of Bahamian industry have been established in a duty-free zone in Freeport, Grand Bahama. That city—the Bahamas' second-largest—is a base for foreign and local industrial investment in manufacturing, including chemicals and ship-refurbishment.

Other manufacturing activities in the Bahamas include the spinning, weaving and finishing of textiles; apparel; sawmilling and planting of wood; publishing; glass and glass products; metal products, tanks and steam generators; and furniture. The Bahamas has a number of notable industrial firms, including a pharmaceutical company, PFC Bahamas (Syntex), the BORCO/Vopak Terminal Bahamas oil facility, Sands Beer, the Bahamian Brewery in Grand Bahama, and the Commonwealth Brewery in Nassau, which produces the Heineken, Guinness and Kalik beer brands. Other industries include sun-dried sea salt and cruise-ship repair services.

Agriculture and fisheries together accounted for just 1.8 % of GDP in 2013.⁷ Agricultural subsectors include citrus, vegetables and poultry. Although the Bahamas exports lobster, fish and craft poultry (consisting of organic and free-range meat), most of it is not caught or raised commercially. Lobsters, crawfish and other seafood products continue to be exported to the US and the EU. There is no large-scale agriculture in the Bahamas, and most agricultural products are consumed domestically. Most agricultural production takes place in Andros, the Abacos, Eleuthera and Grand Bahama. The Bahamas imports more than US\$250m-worth of foodstuffs per year, representing about 80% of its food consumption.

The mining sector plays only a minor role in the economy. The production of salt and aragonite (a stone used in glass manufacturing) are the country's two most commercially important mineral products. One of the Bahamas' major mining operators is Morton Bahamas Salt, the only major industrial enterprise and the largest employer on the island of Inagua, where the second-largest solar saline operation in North America is located. Meanwhile, limestone sand is produced by Freeport Aggregate for the local construction industry. Aragonite is used as an input in building materials and the manufacture of cellular phones. Local operators claim that they produce some of the finest lightweight aggregate materials in the world, owing to the high quality of the limestone mined in the Bahamas.

Services The travel and tourism sector accounts for four-fifths of the Bahamas' foreign-exchange earnings. The World Travel and Tourism Council (WTTC) estimates that in 2013 the tourism industry accounted directly for 20.4% of GDP and 28.5% of total employment in the Bahamas, and that in 2014 its direct contributions to GDP and employment will rise to 28.2% and 34.3% respectively. If indirect contributions are also considered, the industry contributed 46% of GDP in 2013 and 54.5% of total employment (around 102,500 jobs) in 2011. Forecasts for the sector are positive, as the WTTC expects sustained average annual growth of 3.3% in the tourism industry in the period to 2024 and projects that the number of people employed in the sector will grow to about 125,000 by that year.

⁷ Provisional estimate from the Bahamas Department of Statistics, National Accounts Report 2013.

Between 2000 and 2011 the hotel and restaurant sector was one of the most dynamic in the Bahamas, recording consistent growth. The tourism sector is dominated by large resort hotels, which had an average occupancy rate of 51.9% in 2013, and by other hotels catering to international tourists. Small hostels and bed-and-breakfast venues mainly serve domestic tourists.

Cruise-ship visitors and daily visitors account for around two-thirds of arrivals on average but for only 11% of total tourist spending, meaning that there is a reliance on stop-over tourism. According to an IMF study on stop-over expenditure, economic conditions in tourists' countries of origin explain 45% of the variation in tourism expenditure in the Bahamas, while the relative level of local prices explains less than 6% of the variation.⁸ According to data for 2011, the travel and tourism sector makes greater contributions to GDP and employment in the Bahamas than in regional comparator countries such as Antigua and Barbuda, Barbados and Jamaica, thereby rendering the Bahamas particularly vulnerable to any fall in the number of arrivals.

The tourism industry is closely linked to the construction and related engineering services sector. Over the past decade, hotel construction projects across the Bahamian archipelago have boosted economic growth and raised employment. For instance, the construction of the Atlantis Resort and Casino on Paradise Island continues to boost tourism and other activities on New Providence. Meanwhile, the construction of the BahaMar resort project on New Providence is driving construction growth, with the US\$2.6bn facility planned to be completed by the spring of 2015.

The second-largest productive sector in the Bahamas is financial services. The largest proportion of this industry consists of offshore-transaction services, while a smaller share is contributed by domestic activity. Although commercial banking, trust-fund services and private-banking services have traditionally been the cornerstone of the country's financial industry, in the past ten years the sector has expanded significantly and now offers more sophisticated services, including wealth-management and insurance services. The attractiveness of offshore financial services in the Bahamas is closely linked to the country's advantageous tax, legal and regulatory framework, including its banking-secrecy laws and corporate tax-free status.

As of June 2012, a total of 274 financial institutions were authorized to carry out operations in or from the Bahamas. Of these, 159 were restricted under Offshore Financial Centres regulations and 115 were authorized to work as banks and trust companies. However, most of these institutions are dealers, euro-currency branches, and subsidiaries of banks and trusts that operate from outside the Bahamas and are also based outside the country. The local financial sector is composed of banks and trusts, with around ten banks serving the domestic market. The Bahamas Department of Statistics estimates the direct contribution of the financial sector to the nation's economy at 12% of GDP in 2013, with banks accounting for around 8% of GDP and insurance for around 4%.

⁸ IMF (2005), *The Bahamas: Selected Issues and Statistical Appendix*, Report No. 05/224, pp. 9-10.

II Key challenges for private sector development

The World Bank's Doing Business reports rank the Bahamas 76th out of 185 countries surveyed in 2013 and 84th out of 189 countries in 2014. The country's ranking has deteriorated steadily since 2009, when it was first included in the index.

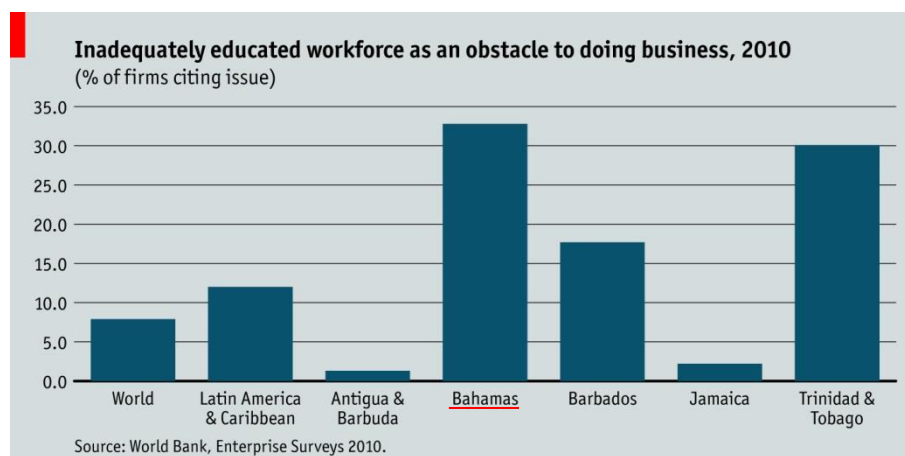
The Bahamas' business climate poses numerous difficulties for businesses, according to the 2014 Doing Business report. The country is ranked fairly highly on resolving insolvency (58th out of 189 economies), trading across borders (63rd) and paying taxes (47th). However, it receives average or below-average rankings in all other areas, and its rankings on these indicators have all deteriorated since the previous report. The Bahamas is particularly poorly ranked for registering property (179th out of 189 countries), enforcing contracts (125th) and protecting investors (130th).

According to the World Bank's 2010 Enterprise Surveys, 33% of Bahamian businesses identified an inadequately educated workforce as the biggest obstacle to doing business, while 14.2% of firms noted customs and trade regulations as the most bothersome obstacle. Responses to the surveys varied significantly depending on firm size. For example, 81% of large firms indicated that an inadequately trained workforce was a major obstacle, whereas just 19% of small firms noted it as a serious problem. In addition, 52% of large firms noted crime, theft and disorder as a major constraint, but just 18% of small firms did so. Small companies identified practices of competitors in the informal sector and customs and trade regulations as the top obstacles.

The Private Sector Assessment Report (PSAR) identifies a number of important obstacles and challenges to private-sector development, including the inadequately educated labour force, problems with access to finance, infrastructure and energy issues, customs and tariff rates, environmental issues and gender matters.

Labour force skills

Although labour market regulation and flexibility are not viewed as major constraints on the private sector according to responses to the 2010 Enterprise Surveys, firms cite the lack of skills, high wages and low productivity as concerns. Unemployment is high in the Bahamas, the workforce is deficient in the skills required by employers and there is a lack of necessary training. In an effort to alleviate the scarcity of qualified workers and to fill gaps in the availability of technological skills, almost 37% of local firms provide on-the-job training for their employees.

Figure 6

Private-sector representatives in the Bahamas noted during the Compete Caribbean consultations in November 2012 that skills shortfalls in the workforce were not effectively addressed by either private or public training institutions. According to surveyed stakeholders, the main skills that employers look for in potential employees are numeracy and literacy; personal traits such as responsibility, teamwork and good communication; and information technology (IT) skills. The lack of IT skills was highlighted by employers in financial services and insurance, while the tourism industry emphasized problems with numeracy and literacy. Due to the increasing importance of technology in numerous sectors, IT skills were mentioned across the board. In the construction industry, companies pointed to the need for more trained airconditioning and refrigeration mechanics, electricians, carpenters, plumbers and pipe fitters, operators of heavy equipment, supervisors and construction managers, again commenting on the poor basic skills of potential workers.

Access to finance

Domestic savings play a major role in the availability of credit for the Bahamian private sector. At the end of 2011 credit extended to the private sector was equivalent to around 86% of annual GDP—the highest level among the comparator countries. In terms of administrative costs and bank efficiency, the spread between the average lending and deposit interest rates in the Bahamas is the lowest among the comparators (see Figure 7). The number of firms identifying access to finance as a major obstacle to doing business varies significantly by firm size. According to the World Bank's 2010 Enterprise Surveys, only 1.9% of large firms indicated that access to finance was a major obstacle, while 12% of small firms and 18% of medium-sized firms cited it as a major difficulty. Financial issues impact firms differently at different points in their business cycles, and also depending on their size. There is a greater need for working capital for ongoing operations than for initial investments (large companies may not source the funds for initial investment locally). According to the World Bank's surveys, only 30% of all firms in the Bahamas use bank loans for working capital—one of the lowest ratios in any of the comparator countries (see Figure 8).

Figure 7

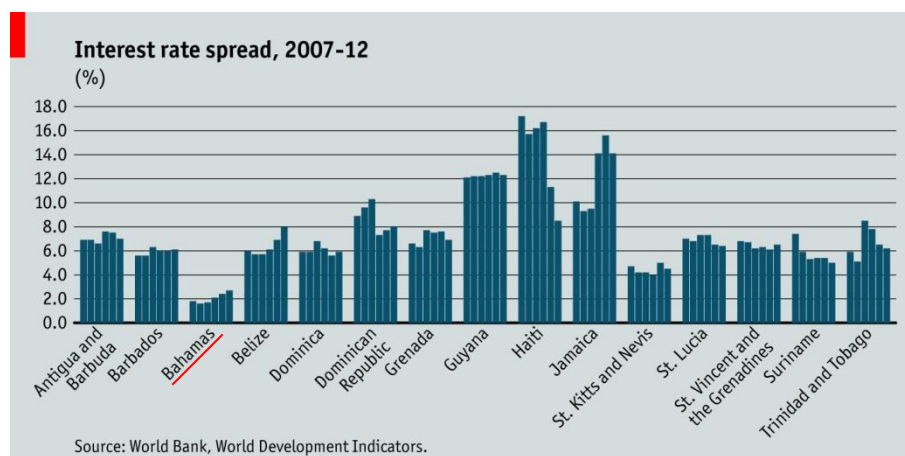
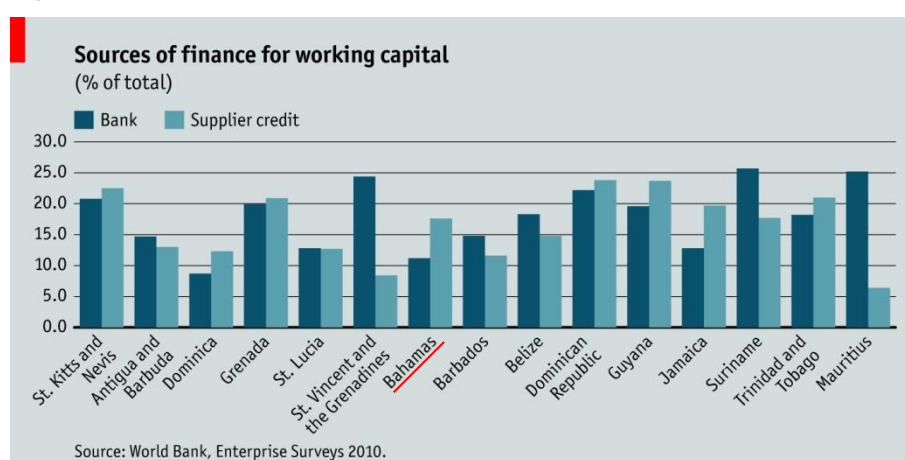


Figure 8



The level of collateral required from potential borrowers by domestic financial institutions is substantial and prohibitive. This may be a symptom of institutional limitations, such as a credit system that does not check the past creditworthiness of borrowers or effectively measure repayment risk. As a result, lending institutions lack specific information on the risks of financing ventures and are obliged to limit their exposure through high security requirements. The collateral required for business credit can reach 230% of the value of the loan for small firms, while for mid-size companies it can reach 253% and for the largest can be as high as 319%. According to the 2010 Enterprise Surveys, the Bahamas has the highest collateral requirements as a percentage of loan value in the Latin American and Caribbean region.

Infrastructure and energy

Infrastructure weaknesses, including inadequate electricity and water supplies, can increase costs, disrupt production and reduce profitability for firms of any size. There is a relatively consistent supply of electricity available to the private sector in the Bahamas, partly because a large proportion of firms own their own generators. However, there are sectors of the economy, most notably tourism, that cite electricity supply and prices as an important obstacle and constraint. The price of power in the Bahamas is close to the high Caribbean

average of 30 US cents/kWh. The heavy reliance of businesses on their own generators for electricity leads to diseconomies of scale and dependency on imports of fuel oil. The Bahamas Electricity Corporation (BEC) is a state-owned enterprise that faces challenges in terms of administrative efficiency and also in the efficient generation and distribution of electricity. In August 2013 the government announced plans to reform the country's energy sector through the restructuring of the BEC by mid-2014. However, the process has not yet been completed.

Access to telecommunications services is another bottleneck, particularly for companies operating in the tourism and financial service industries. The Bahamas Telecommunications Company recently partially privatized provision of telephone, cellular-phone and Internet services, but very little competition exists. Infrastructure-related challenges in transportation, water supply and communications place further constraints on the operational capacity of firms and exporters. Delays in obtaining public services affect different types of businesses differently. Whereas electricity connection delays are a significant problem for large companies, small firms suffer primarily as a result of fixed-line connection delays. Mid-size firms, meanwhile, might wait for three to four months to obtain a telecoms connection. Although arranging connections to water supplies is less of a problem, according to the businesses surveyed, the number of water outages per month in the Bahamas affects firms of all sizes, and is large relative to the number experienced in regional comparator countries including Barbados, Jamaica, and Trinidad and Tobago. Delays in getting connected to water supplies affect large construction companies and hotel operators particularly severely.

Customs and tariff rates

Private-sector growth and development in the Bahamas, and especially growth in services export capacity and travel services, are closely linked to international trade and customs regulations. Foreign investment, which has been directed mainly into tourism projects and financial services, has helped to stimulate economic growth. In the past five years the Bahamas has pursued new integration and liberalization arrangements, such as the Economic Partnership Agreement with the EU and the start of the process of accession to the World Trade Organization (WTO). Joining the WTO may require the Bahamas to negotiate additional agreements, and also to make adjustments in its public sector and economy. Some of the necessary reforms include changes to taxation, competition policy, intellectual property rights legislation and government procurement.

The tourism industry in the Bahamas is concerned about losing competitiveness against other markets in the Caribbean, and notably about the eventual opening up of Cuba as a tourist destination. Local firms face a myriad of additional constraints on their competitiveness. Discretionary and restrictive tax regimes and high import tariffs can negatively impact hotels, retailers and restaurants that depend on imported goods. More than 60% of all agricultural products face import tariffs ranging from 25% to 50% in the Bahamas.

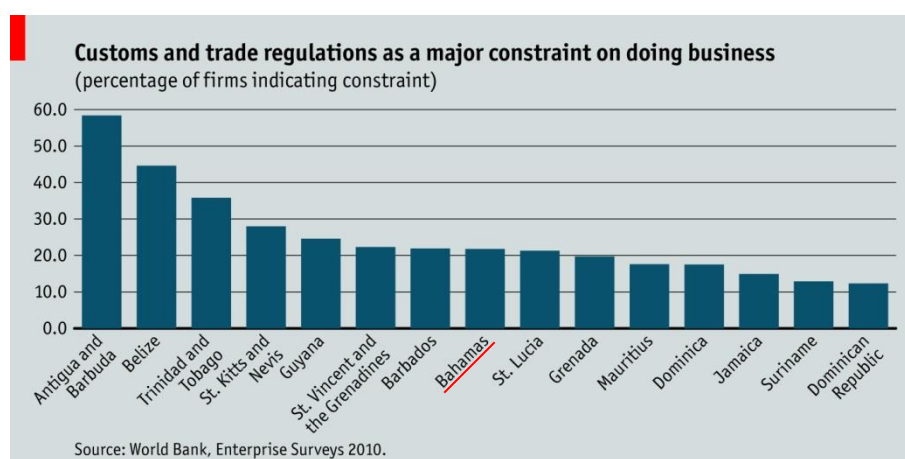
The tourism industry and the hotel sector have been willing in the past to buy local goods and services, but they are constrained by poor availability, quality

and reliability. Protectionist policies to promote local activity—such as the mandating of local participation in approved foreign investment projects, and the protection of local industries and workers via high import tariffs and restrictions on foreign ownership of businesses—have proved ineffective. According to the World Bank's 2010 Enterprise Surveys, 80% of Bahamian companies use materials or supplies of foreign origin, and customs and trade regulations are the third most important constraint on firms.

Average tariffs on all products in the Bahamas (including both agricultural and non-agricultural products) are among the highest in the Caribbean. Trade tariffs in the Bahamas are almost double those in Jamaica, and, with the exception of tariffs applied to animal and dairy products, are also nearly twice the level of those in Trinidad and Tobago. High tariffs are justified by the authorities on two counts: they provide a large share of fiscal revenue, and they protect the local market. Under the law, wholesale and retail operations may not be carried out by non-Bahamians.

The local private sector is reliant on imported supplies, and is protected by high tariffs and regulatory barriers to entry by new market participants from abroad. As shown in Figure 9, customs and trade regulations are not reported to be a major constraint on doing business in most comparator countries, with the notable exception of Antigua and Barbuda. Only one-fifth of firms consider trade regulation to be a major constraint in the Bahamas. Small firms (those with 5-19 employees) are the most concerned about such rules.

Figure 9

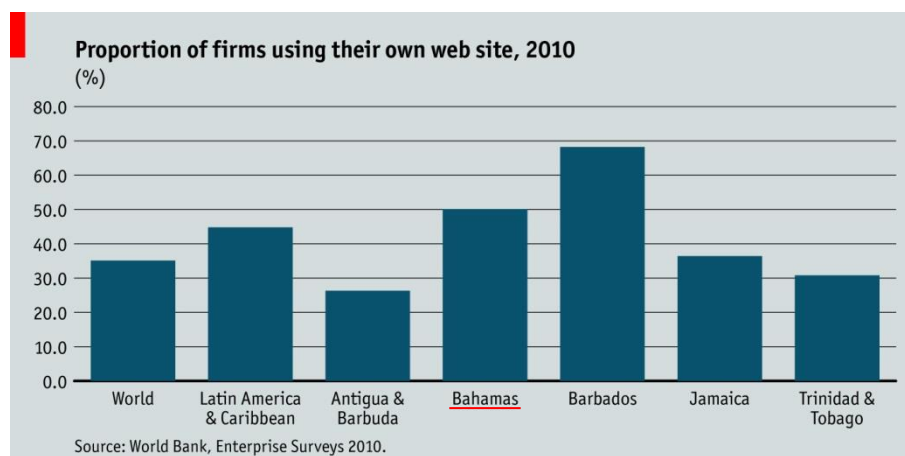


Innovation and information and communications technology

In 2003 the government established the long-term, broad-based objective of transforming the Bahamas into a digital economy as a means of generating opportunities for the local population to participate in the global economy. The Bahamas' strategy in this regard includes the use of the Internet to engage in activities such as e-commerce, e-learning, e-health and accessing government services. The government's initial commitment was to expand its wide-area network to connect all government agencies, and to accelerate the development of online processes to facilitate business. Results have also been positive with regard to information and communications technology (ICT) benchmark indicators for the private sector. Compared with the world as a whole, Latin

America and the Caribbean, and selected Caribbean countries, in the Bahamas there are relatively high levels of technology use in enterprises and access to electronic communications for business. Internet penetration has allowed most enterprises to use e-mail to interact with clients and suppliers. A significant proportion of companies are also developing a web presence by investing in their own websites.

Figure 10



Achieving complete telecoms and Internet coverage poses challenges. The Bahamas' geography presents major challenges for ICT. For instance, Cable Bahamas broadband can reach only four islands in the archipelago at present, and not every settlement has coverage even on those islands. Creating websites for private-sector firms is a challenge, due to the inconsistency of coverage and broadband accessibility. Nevertheless, despite the high start-up costs, some banks are now providing platforms for e-commerce to enable businesses to sell online and deposit the resulting funds in their accounts.

The Bahamas has a Road Map for the Advancement of Science and Technology to provide direction and guidance for the acceleration of national development in these important areas. The plan comes under the authority of the Science and Technology Committee of the Bahamas Environment, Science and Technology (BEST) Commission. The committee was established in 2001 to fill an acknowledged gap in governmental processes in terms of support, encouragement, management, and accelerating the development and growth of science and technology. However, research and development (R&D) budgets are small in the Bahamas, activity in this field is at a low level and there is only limited support for product development.

Although innovation is generally appreciated in the Bahamas as being vital in terms of creating wealth and generating sustainable returns on investment, most interviewees believe their culture to be reactive rather than proactive. This characteristic limits innovation in the country. Innovation goes hand in hand with R&D, and there are few institutions in the Bahamas that support such activities, although the College of Bahamas has the potential to do so.

Environment The Bahamas contains highly diverse terrestrial and marine habitats. The tourism industry relies heavily on the natural resources of the coastal zone. However, development in this sector, as well as urban growth and infrastructure expansion, has resulted in many physical changes to the coast. The Bahamas is a coastal country, with most of its population living within coastal zones. It is extremely vulnerable to natural disasters, and to hurricanes in particular. Given that the country's economy is based primarily on tourism, any environmental hazard can affect the wellbeing of most of the country's population, either through direct impacts (physical or economic) or via economic linkages. The combination of population growth and the increasing number of visitors is putting pressure on the Bahamas' natural resources. This has made it necessary to develop legislation, policies, strategies and management systems to preserve the country's resources.

Generally, management of environmental issues has been the responsibility of public agencies such as the Department of Environmental Health Services and the BEST Commission. The latter body evaluates and enforces policies and legislation relating to the coastal environment, the marine environment, land, tourism, water, waste management, and natural and technological hazards. In addition, within the Ministry of Tourism two units have been created to incorporate environmental management and awareness into the industry. The BEST Commission has also implemented a number of initiatives that address the vulnerability and mitigation aspects of disasters arising out of climate change, through the creation of a National Climate Change Committee.

Hotels have responded positively to the need to address environmental issues through various initiatives. Although these measures have resulted in improvements in environmental-management performance, particularly in the area of energy, there is considerable scope for further positive change. It is evident that cost is a major limiting factor in the environmental soundness of the hotel sector, and also that assistance is needed in the form of fiscal and other incentives to catalyze the widespread use of environmentally sound technologies in the sector. Incentives to spur the use of such technology are currently lacking. This is significant, in that the majority of hotels in the Bahamas are small, are usually family-owned and managed, generally operate on small budgets, and require a longer period of return on investment for projects. This is even more the case for small hotels that operate outside the main tourist destinations, such as Nassau. Funds should be made available to small hotels so that they can undertake sustainable-tourism initiatives that encourage environmentally sound and cost-efficient operations.

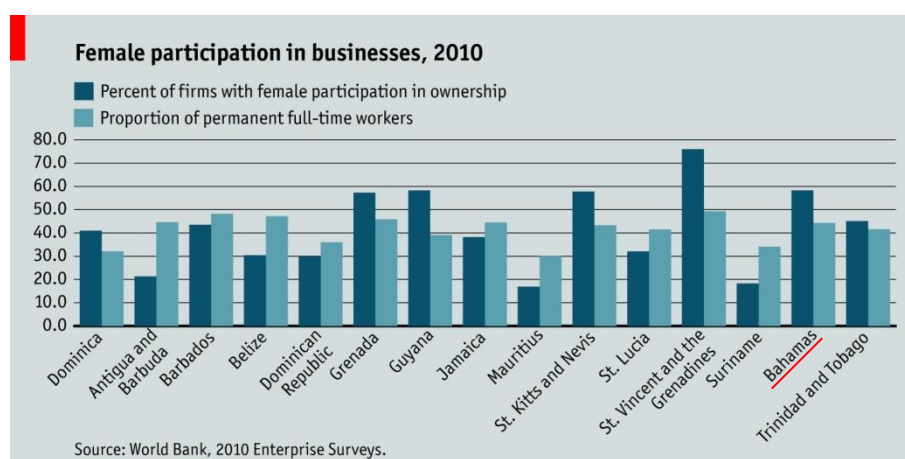
Gender The World Economic Forum's Global Gender Gap Report⁹ reveals that in 2009 and 2012 the Bahamas achieved rankings close to 1 (indicating that the country has relatively low gender-based disparities) in all areas except political empowerment. In 2013 the Bahamas was ranked 40th among 136 countries worldwide on overall gender equality. It was ranked fifth for economic

⁹ The report and index provide a framework for capturing the magnitude and scope of gender-based disparities around the world. The index benchmarks national gender gaps on economic, political, educational and health criteria, and provides country rankings that allow comparison across regions and income groups and over time.

participation, joint first for educational attainment, and also joint first for health and survival. However, it was ranked among the most gender-unequal countries for political empowerment, at 124th. Women make up only 14% of the membership of parliament, and there are currently only two women in ministerial or cabinet positions.

With regard to economic participation and opportunities, the Bahamas boasts a relatively equal distribution of males and females in terms of labour force participation, earned income, and senior officials and managers. Female participation is significantly higher in professional and technical professions. The 2013 report shows that the gender earnings gap for women is only one-third of male colleagues' earnings. Women in the Bahamas rank higher than males in literacy rates and primary- and secondary-education enrolment. There are also twice the number of female professional and technical workers participating in the labour market compared with male professionals and technical staff. As part of the Enterprise Surveys conducted by the World Bank in various Caribbean countries in 2010, gender participation was measured at the level of firms and entrepreneurial activity. The following chart shows that female participation is important for enterprises in the Bahamas and that women achieve higher participation rates there than in other Caribbean, Latin American and even high-income non-OECD countries.

Figure 11



III. Emerging sectors

The product space map for the Bahamas does not indicate obvious candidates for large or fast-growing sectors. The identification of emerging sectors is based on the industries with the greatest potential to contribute to economic growth in the future. This section provides an overview of manufacturing, mining and agriculture as small, but potentially growing, sectors.

The most recent product space maps for the Bahamas—those for 2000, 2005 and 2010—are largely similar in their reflection of a highly heterogeneous productive structure. Different products are not closely connected between the various sectors, and thus they mostly exist in relative isolation and at a low level of economic complexity. This indicates the challenges that the country will face in moving into new high-growth sectors or more complex, interrelated industries.

Traditional sectors: tourism, finance, wholesale trade and retail trade

The hotel and restaurant sector grew by an average of just 1% a year in 2010-13. Another traditional mainstay of the economy, the financial services sector, expanded by a robust average of 5.1% annually in the same period. This reflected the volatile, but relatively strong, performance of both banks and insurance firms. The insurance sector contracted by 33% in 2011, before growing by a whopping 51% in the following year. Meanwhile, real estate—the largest contributor to GDP, accounting for 20% of GDP in 2013—grew by a modest 1.8% in 2010-13.

Table 1: Bahamas: industry growth trends

	Average annual growth, 2010-13	Contribution to Gross Value Added, 2013
Agriculture & fisheries	1.0%	1.8%
Agriculture	-5.3%	0.7%
Fishing	8.6%	1.1%
Industry	2.0%	6.8%
Mining	-0.7%	0.8%
Manufacturing	3.5%	3.9%
Electricity	0.5%	1.4%
Water	4.8%	0.7%
Construction	13.4%	9.8%
Wholesale & retail activity	-3.5%	9.8%
Wholesale trade	-8.3%	1.9%
Retail trade	-2.1%	7.9%
Hotels & restaurants	1.0%	10.6%
Hotels	1.7%	7.9%
Restaurants	-0.6%	2.7%
Transport	-0.8%	3.4%
Land transport	-0.1%	0.4%
Marine transport	-0.2%	2.6%
Air	-2.3%	0.4%
Storage	5.4%	0.5%
Communication	-0.3%	4.0%
Financial intermediaries	5.1%	12.0%
Banks	5.3%	8.8%

Insurance	9.3%	3.2%
Real-estate/rent/business activity	1.8%	20.1%
Real estate	2.7%	16.5%
Other business services	-1.6%	3.5%
Public administration & defence	3.7%	6.1%
Education	0.8%	4.0%
Private education	2.9%	1.8%
Public education	-0.8%	2.2%
Health	-0.5%	3.7%
Private health	-2.1%	1.4%
Public health	0.7%	2.3%
Other community, social & personal services	0.4%	5.6%

Source: Bahamas Department of Statistics.

While large traditional sectors as hotels and restaurants and also financial services will remain important to economic growth, small non-traditional sectors may become increasingly significant in the near future.

**Potential growth sectors:
manufacturing, mining and
agriculture**

The country's productive agricultural, manufacturing and exporting base has historically focused on a very narrow range of primary commodities and goods with low value-added content. The smallest sectors in the Bahamas' economy displayed the most dynamic growth between 2000 and 2011. Mining, and particularly the production of aragonite and salt, was the fastest-growing sector in 2000-11, with a compound average growth rate of 7.5% a year in 2000-11. However, its average growth rate in the four-year period from 2010 to 2013 was negative, at -3% a year.

By 2010, the Bahamas' exports had transformed from chemical products, mounted precious stones, diamonds, precious jewellery and oxygen-function acids and derivatives to sodium chlorinate, heterocyclic compounds, warships, followed by work of arts, polystyrene and fresh, chilled, frozen or salted crustaceous and molluscs poultry. Using the Standard International Trade Classification, Revision 4 (SITC 4), in 2010 the country's exports exhibited a revealed comparative advantage (RCA) in products such as mineral tars, salt (sodium chloride), ships and boats, and polystyrene. (An RCA number above 1 for a product indicates that a country has a comparative advantage in exports of that product.) However, with the exception of ships and boats, these products account for only a small share of the total value of the country's exports. In 2008 the Bahamas exported warships worth US\$195m. Meanwhile, the value of alcoholic-beverage exports declined from US\$227m in 2008 to just US\$14m in 2010 as the category's RCA declined.

A significant number of export products have an RCA above 1. The Bahamas has increased the value of its exports (and its share of world exports) in machinery, tools and base metals, articles of iron, iron and steel, perfumes and cosmetics, works of art and optical and medical apparatus. Aggregated data show that the shares of GDP contributed by the agriculture and industrial sectors were fairly stable over the decade to 2010, with only the beverage and tobacco sector experiencing a precipitous decline.

IV Priority areas and action plan

The Bahamas Private Sector Assessment Report (PSAR) identifies a number of key challenges to private-sector development and several sectors that may drive growth in the future. Of the many policy recommendations to improve the business environment that could be included, the PSAR emphasizes the importance of solving the challenges of education and workforce skills, the quality of infrastructure, access to finance, innovation, customs, and environment and land use.

Improving education and workforce skills

The Bahamian government is already responding to the need to improve education and workforce skills. In addition to ongoing efforts to support education and training programmes and to improve labour market information; accreditation and certification; teacher training; and stakeholder consultation, private-sector representatives recommend that they be consulted regarding industry-specific curricula and invited to review training programmes. Industry and training institutions need a mechanism to improve information about labour supply and demand and to facilitate the hiring of new graduates.

Private-sector stakeholders indicated that an overall reform of the education system is required from primary to tertiary level. Changes should include improved vocational training, and expanded opportunities to obtain four-year university degrees. Moreover, additional graduate programmes are required. Training institutions should be encouraged to create venues such as job fairs to provide effective channels via which skilled workers can fill employment gaps.

Although labour regulation is not viewed as a major problem, some issues remain, including the timely grant of work permits and migration policy. With regard to migration, the available data make it difficult to distinguish clearly between immigration and emigration for policymaking purposes. The Bahamas faces a shortage of qualified construction workers, and is losing skilled professional talent through emigration.

One recommendation is to revamp immigration regulations pertaining to foreign workers. Although this is a politically sensitive issue, both public- and private-sector officials agree that the existing shortages of qualified labour will intensify unless more foreign workers are allowed to take up employment in the country. The paucity of timely labour data prevents the private sector from gaining a clear picture of how many workers are needed for each sector. For example, real-estate and infrastructure investments will increase the demand for construction workers, who will need to be sourced from abroad. Information on projected employment demand for approved investment projects could serve as a basis for revising immigration policy, with the aim of introducing more flexible, simpler and less discretionary restrictions on foreign workers.

Infrastructure provision

It has been almost a decade since the government initiated important projects and reforms pertaining to infrastructure provision. Current infrastructure inadequacies are largely due to the existence of a government monopoly in the supply of infrastructure services, and to the inadequacy of existing policies to

facilitate the effective participation of private investment. Streamlining the public sector's decision-making process regarding private investment is a top priority for the current administration. There needs to be a move away from a highly centralized, discretionary and case-by-case negotiating process towards a more policy-oriented, decentralized process. Government involvement should centre on creating and enforcing appropriate general regulations within an overall development strategy. It should also focus on complementary policies, such as reforms to establish an independent regulatory framework, and price liberalization to address the problems caused by political decisions to keep tariffs below cost level in the transportation, telecommunications, energy, and water and sewage sectors.

Two specific proposals for improvements in the organization of the public sector to address critical aspects of private-sector investment are: i) strengthening the strategic planning function, and ii) establishing a public-private partnership unit within the Office of the Prime Minister. There is significant interest in the Bahamas in the role that state-owned enterprises can play in promoting economic development through infrastructure investments, the relationship between such entities and the state as a shareholder, and the criteria used in assessing options for investing in or disposing of these enterprises.

Access to finance

With respect to access to finance for small and medium-sized enterprises (SMEs), some private firms say that they face barriers in accessing credit, but data show that there is considerable short-term liquidity in financial institutions. Moreover, public institutions exist that are dedicated to providing support for the productive sector. According to the World Bank's 2010 Enterprise Survey for the Bahamas, medium-sized companies were the most likely to identify access to finance as the main obstacle facing them and as a key factor that needed to be addressed in order to improve their ability to do business. Private-sector representatives point out that access to credit must be provided in tandem with technical support services in order to be effective.

Credit products should be comprehensive and cover all stages of businesses' financial requirements. The provision of non-financial business-support services should include business-development activities such as assistance with strategic planning, developing a sound business plan, credit negotiation and building a strong credit history. There is a need for different types of lending: for growth, for high-risk projects and for structural development. The government should have a plan in place with incentives for the provision of credit to underserved sectors and businesses. It should also identify high-growth firms that can provide jobs and support economic growth. Moreover, firms should have access to international lenders, and foreign-exchange-control processes must be streamlined at the Central Bank of The Bahamas to provide access to funds internationally at low interest rates.

Currently, neither domestic commercial banks nor offshore banks have the incentive to supply credit to domestic firms. Banks operate to maximize shareholder benefit, and will pursue product lines that they believe will turn a profit. Most commercial banks in the Bahamas do not lend unless clients have

significant collateral in the form of land or real estate. However, a large number of companies in the country have no equity that they can use as collateral for bank loans. Most Bahamian companies are small and medium-sized, and most commercial banks are not yet interested in looking at the potential benefits of such firms as a target market. Technological and creative projects are not supported financially because they are not traditional activities. Given that only a small percentage of businesses in the Bahamas survive for more than five years, non-financial support such as technical assistance for business development is urgently needed.

Capital constraints do exist in the Bahamas for a large number of private-sector entrepreneurs, and especially for SMEs, but the panel of interviewees suggested that there were certain clear principles that should guide attempts to improve the business climate in this regard:

- Credit and technical support need to go hand in hand when dealing with SMEs.
- Individuals have to become their own advocates in educating themselves about credit requirements and creditworthiness.
- Training institutions should be spearheading awareness campaigns through social media and other modern channels of communication.
- Policy revisions are essential with regard to credit bureaux and bankruptcy and foreclosure laws.

Customs and tariff rates

Key recommendations to emerge from the research focus on strengthening public institutions, such as customs services and procedures, and improving market access and clustering facilitation for potential exports. In terms of strengthening public institutions, reforms must promote efficient co-ordination between trade agencies, and need to include support for the Bahamas Trade Commission as the central conduit for consultation with the private sector on trade issues. Creating a modern and integrated customs system will be critical in order to comply with and reap the benefits of a more liberalized trading environment. Customs modernization must aim to provide a transparent and less discretionary system in terms of product valuation, nomenclature and origin of goods. Investment in information technology solutions throughout the trade cycle is necessary in order to facilitate trade flows; an example would be the creation of a single electronic window to enable firms to comply with origin, standards, and sanitary and phyto-sanitary requirements through a single platform.

An institutionalized dialogue between the public and private sectors is increasingly viewed as a fundamental element of the Bahamas' future. The development of business between foreign investors and domestic sectors will be an important strategy in terms of diversifying the economy, promoting private-sector activity (particularly among SMEs) and supporting employment growth. For instance, linking private investors to the agricultural sector through the implementation of standards and modern control techniques to improve quality will enhance the development of SMEs and clusters, and this in turn will result in greater market opportunities locally and internationally.

Effective co-ordination between the public and private sectors regarding public policy and regulation will strengthen the Bahamas' competitive position in both foreign and domestic markets. Currently, the erosion of trade preferences in the country's main export markets is a concern for many goods exporters, including prominent companies such as Polymers International, Morton Salt and Paradise Fisheries. Three of the Bahamas' top four export products to the EU—spiny lobster tails, organic chemicals containing pyrimidine, and expansible polystyrene—enjoy marked preferential margins.

Innovation Remarkable efforts have been made in the Bahamas to promote information and communications technology (ICT), and there is a general recognition that ICT can help business development. However, the country's geography presents considerable challenges for ICT and connectivity. Increasing business sophistication will eventually result in new and innovative services and products, but achieving this goal requires technical knowledge and skills, as well as entrepreneurial confidence. Some private-sector institutions, such as the Bahamas Chamber of Commerce and Employers Confederation, are working to inspire individuals and businesses to become more innovative through competitions and other approaches. Access to telecommunication value-added services, such as WiFi, have been limited for SMEs by the slow pace of growth in service coverage.

Environment and land use An important requirement for the development of the private sector is an appropriate framework for environmental regulation. Efforts are needed to develop adequate information systems and to improve the generation, compilation and processing of environmental information. This will provide an appropriate baseline to guide policy. Topics such as innovation and science and technology can be incorporated into the agenda of the Bahamas Environment, Science and Technology (BEST) Commission (which comes under the auspices of the Ministry of Education and Environment). Academic institutions are involved in promoting science and technology, but financial resources limit the results and continuity of such programmes.

Land-use policy and administration issues have a major adverse impact on agriculture and coastal management at present. Sectors such as fisheries would benefit greatly from efforts to streamline land grants, sales and concessions. Although land-registration systems aimed at replacing the current registry with a standard title system and modernizing the registration process have been seen primarily as policies that are relevant to foreign investors, they are also important to domestic marine development, the agricultural sector and fisheries exports.

Conclusions The magnitude of the reforms that are needed in the Bahamas will necessitate their implementation in a manner that helps to build broad consensus and guarantee long-term stability. There is already a general acknowledgement that there is an urgent need to achieve more public-private synergies. The government's Bahama's Vision 2030 plan has set the course for two potential forums to drive reform. The first will be the Constitutional Review Committee, through which public- and private-sector partners will be able to formulate a

long-term economic plan. The second forum is intended to be more direct or executive in nature—for example, the suggested Council of Economic Advisers. The purpose of the council would be to advise the government on major issues, and particularly those relating to economic growth and stability. A review of the country's tax system will be high on the list of matters to be referred to the council. The private sector has also called for a similar review of taxation issues at Caribbean Community (CARICOM) level.

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