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Bermuda is still in recession::

FINANCIAL RAMBLINGS from The Rock by Nathan Kowalski

Many of our clients are asking if the recession is over and when will the economic recovery begin in Bermuda?

I decided to try and figure out Bermuda's Gross Domestic Product (GDP) for the first quarter of 2010. My analysis that follows is not an attempt to get a completely accurate number for the GDP figure but an attempt to discern the general level and direction of growth in Bermuda.

Based on my preliminary analysis, it would appear Bermuda's economy continued to contract in the first quarter of 2010 by approximately 0.5 percent. The fact that Bermuda continues to contract may not be a great shock to many residents as it surely feels worse for a lot of Bermudians.

What may be interesting is the composition of this decline and what may happen going forward. It is disheartening to note Bermuda's contraction in comparison to expansions in other developed markets, especially our largest trading partner, the United States, which expanded at a 2.7 percent rate in the first quarter. Clearly, Bermuda's recovery in economic activity is lagging other regions.

My calculation uses published government data and divides GDP into its common four components in an attempt to calculate their respective growth rates: net exports, government spending, investment, and consumption.

My guesstimate for the net export figure points to approximately 0.8 percent real growth. The main contributor was exported business services.

The government sector contributed the most to positive growth in the quarter. By my estimates it helped GDP by a positive 5.2 percent.

Government involvement in the economy continues to expand while private sector growth is slowing. In fact, if government expenditures remained flat year over year, GDP would likely have been negative two percent for the quarter.

Investment activity contributed a marginal 0.2 percent with machinery orders accounting for much of this gain. The largest component by far in the calculation of GDP is the consumption component.

This component, unfortunately, has exhibited the weakest growth and slid about 2.2 percent. The continuing slump in retail sales, resident purchases abroad and the flat

employment market are constraining growth in consumption.

Of these figures, however, the consumption sector is the most subject to revision. With current statistics it is very difficult to determine.

Conversely, the net export and government figures, I feel, are very reliable. Going forward, the growth trend continues to look challenging.

Clearly the residential and commercial real estate markets are taking a turn for the worse. The glut of commercial real estate space is likely to drive rental prices in the B and C quality space lower.

Based on anecdotal evidence and a cursory review of rental websites, residential real estate rates continue to soften with a surge in listings over the past few months.

It appears unrented supply for one- and two-bedroom units continues to expand while net migration looks to be turning negative for the first time in a number of years.

The stock of residential dwelling units actually expanded 8.8 percent in the first quarter. Future building activity and construction is set to slow meaningfully as legacy commercial construction projects are completed amid a dearth of new activity.

The value of new projects started in the first quarter of 2010 was only \$17.4 million in comparison to last year's quarter of \$134.3 million. A considerable drop for sure.

All these headwinds will likely constrain growth in incomes and consumption in the future. This is evident in the continued softness for the retail sales figures which dropped in May by \$89.4 million or 3.8 per cent, the 14th consecutive monthly decline.

It's not all that clear that Bermuda will get a boost from the tourism sector either. Based on the latest consumer confidence data out of the US, travel intentions continue to slip and only 7.2 percent plan on taking a foreign vacation this year.

In fact, vacation intentions for the US as a whole, Bermuda's largest tourist contributor, are now near the cycle low set in April of 2009. Hotel investment is also likely to slow in future quarters.

The balance of payments, which contains components that feed directly into the net export figure, continues to slide.

It is conceivable that this will eventually end up being a non-contributor over the next few quarters. The only component that may help alleviate the continued slide in Bermuda growth may be the government sector.

If the hospital project commences, public works projects expand and government hiring continues, the Government may help ease the slide in growth. But Keynesian stimulus spending has its limits.

At some point Bermuda needs to find a new source for growth. Based on this cursory

analysis it is unlikely Bermuda will have real growth this year.

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