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IMF Executive Board Concludes 2019 Article IV Consultation with St. Lucia

On February 7, 2019, the Executive Board of the International Monetary Fund (IMF) concluded the Article IV consultation discussions[1] with St. Lucia and considered and endorsed the staff appraisal without a meeting.[2]

Following a slowdown in 2018 real GDP growth has picked up in 2019 supported by strong growth in tourism activities. The construction sector continued to contract in early 2019 owing to delays in public infrastructure projects but stayover arrivals grew by 7.9 in the first three quarters of the year (y-o-y). Preliminary data also point to improvement in the current account. Unemployment has declined somewhat but remains high at 18 percent while inflation remained subdued as fuel price pressures subsided.

Prudent fiscal policies and revenues from the citizenship-by-investment program (CIP) have helped stabilizing public debt as a share of GDP. The primary fiscal surplus rose to 2.1 percent of GDP in 2018 and is projected to be broadly balanced in 2019 due to a decline in CIP applications and increased public sector wages. Bank credit to the private sector shrank for a sixth consecutive year, reflecting more conservative lending practices and banks' efforts to resolve legacy NPLs, while the expansion of the credit union sector remains strong.

Near-term growth prospects are favorable, albeit with downside risks. The commencement of large public infrastructure projects, including the redevelopment of the international airport and a comprehensive road improvement program, is expected to substantially boost growth in 2020-22 but will push up public debt and weaken the external position. Nonetheless, the expected improvement in St. Lucia's connectivity could help address capacity constraints and has the potential to catalyze a more durable expansion of the tourism sector and related activities. Downside risks to the outlook include a deeper-than-expected slowdown in major source markets for tourism, energy price shocks, disruptions to global financial markets, and loss of correspondent bank relationships. St. Lucia's high vulnerability to natural disasters constitutes an ever-present risk to both growth and the fiscal outlook.

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[1] Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board.

[2] The Executive Board takes decisions under its lapse of time procedure when it is agreed by the Board that a proposal can be considered without convening formal discussions.

Executive Board Assessment

St. Lucia's near-term growth prospects are favorable, but policy adjustments will be needed to strengthen longer-term growth. The commencement of large public infrastructure projects is expected to substantially boost growth in 2020-22 but will raise public debt and weaken the external position. However, a deeper-than-expected slowdown in major source markets for tourism, energy price shocks, disruptions to global financial markets, and loss of CBR all represent downside risks. St. Lucia's high vulnerability to natural disasters constitutes an ever-present risk to both growth and the fiscal outlook. Longer-term growth continues to be impeded by the high public debt, lingering vulnerabilities in the financial system, and structural impediments to private investment. On the other hand, there is an upside that infrastructure investment could catalyze a greater-than-expected expansion of the tourism sector and related activities. While the overall external position is assessed to be broadly consistent with the level implied by fundamentals and desirable policies, St. Lucia still has considerable competitiveness challenges, particularly in its non-tourism sector, that need to be addressed.

Fiscal policies should be geared toward rebuilding policy space and ensuring public debt converges to the regional target of 60 percent of GDP by 2030. The debt-financed infrastructure investments, despite being on semi-concessional terms with long-run repayment largely covered by dedicated revenue streams, will move public debt further away from the regional target. The need to invest in climate resilience and the uncertainty over future CIP revenues pose additional challenges to public finances. Without policy adjustments, debt vulnerabilities are elevated, and public debt does not stabilize over the near term.

The government's near-term focus should be on revenue-enhancing measures and investments that build resilience to climate related shocks. In addition to limiting current spending growth (particularly the public wage bill), additional revenues should be mobilized from the proposed hotel accommodation fee, the introduction of a carbon tax, and reducing the scope of VAT exemptions. Since some of these measures will likely be regressive, they should be introduced in parallel with targeted transfers that offset the impact on poor and vulnerable households. The National Health Insurance system should also be introduced in a fiscally responsible manner. Concerted efforts are also needed to mobilize donor grants to fund investments in climate resilience. If there is over-performance of the CIP, or of other revenue sources, it should be directed toward financing a self-insurance fund to bolster the economy's resilience against natural disasters.

A fiscal rule would help anchor fiscal policy over the medium term and support consolidation efforts. To be effective, the fiscal rule should encompass a comprehensive definition of fiscal activities, including the fiscal costs of natural disasters and the lumpy expenditure associated with infrastructure investment, and should be part of a broader fiscal responsibility framework that embeds appropriate institutional and governance arrangements to ensure both the appropriate degree of flexibility as well as enforceability of the fiscal rule. The fiscal rule will also need to be carefully calibrated to strike the balance between credibly meeting the debt target over the medium-term and providing space for much-needed spending to build resilience.

To support private sector investment, measures are needed to address constraints on financial intermediation. There is scope to improve credit market efficiency by modernizing foreclosure and insolvency legislation, establishing a regional credit bureau and registry, and taking steps to allow for the greater use of movable property as loan collateral.

Emerging financial sector risks warrant a more assertive approach to regulation and supervision. The banks' rising allocation of their assets to overseas debt securities has supported bank profitability but may also expose the sector to losses if global financial market conditions deteriorate or risk premia rise. The rapid expansion of credit unions has increased the sector's macro-financial significance that warrants stronger oversight. The swift adoption of the Harmonized Co-operative Societies Act, combined with a strengthening of supervisory oversight of the non-bank financial sector, remain key policy priorities. In addition, continued efforts are needed to satisfy international taxation and AML/CFT standards.

Efforts are needed to further enhance resilience to climate change and natural disasters. Progress has been made in implementing recommendations of the CCPA. Key measures to address the remaining institutional, financing and capacity gaps include the active costing of climate projects, improving public financial management of climate financing and outlays, mobilizing private investment in mitigation and adaptation and strengthening capacity in managing climate-related investments.

Decisive and targeted reforms are needed to address supply-side impediments to long-term growth. Enhancing productivity will require a better alignment of the education system with labor market needs. There is scope to improve the business environment by enhancing access to credit and reducing electricity costs, further diversifying the economy toward higher-value exports, and increasing local content in the tourism supply chain.

St. Lucia: Selected Social and Economic Indicators, 2015–24

I. Social and Demographic Indicators

Area (sq. km)	616	Infant mortality (per thous. live births, 2018)	14.9
		Human Development Index ranking (of 189 countries, 18)	89
Population Characteristics			
Total (2018)	178,696	Gross Domestic Product (2018)	
Rate of growth (average 2011-2018)	0.9	(millions of US dollars)	1,922
Population density (per sq. km., 2018)	290.1	(millions of EC dollars)	5,189
Net migration rate (per thousand, 2018)	0	(US$ per capita)	10,755
Secondary education enrolment (percent, 18)	90	Gross National Income per Capita (US$, 2018)	10,126
Life expectancy at birth (years, 2018)	76.1		

II. Economic and Financial Indicators

					Projections					
	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024
					(Annual percentage change, unless otherwise specified)					
Output and prices										
Real GDP (at market prices)	0.2	3.2	2.6	0.9	1.5	3.2	3.0	2.4	1.5	1.5
Real GDP (at factor cost)	2.0	1.3	2.4	0.6	1.5	3.2	3.0	2.4	1.5	1.5
Consumer prices, end of period	-2.6	-2.8	2.0	2.2	2.1	2.2	2.0	2.0	2.0	2.0
Consumer prices, period average	-1.0	-3.1	0.1	2.4	2.2	2.1	2.1	2.0	2.0	2.0
Output gap (percent of potential GDP)	-1.4	0.2	0.9	-0.2	-0.9	-0.1	0.5	0.7	0.2	0.0
Unemployment rate (% annual avrg.)	24.1	21.3	20.2	20.2	...	...	...	...	...	...
Real effective exchange rate										
(annual average, depreciation -)	106.8	104.9	103.1	102.3	...	...	...	...	...	...
					(In percent of GDP, unless otherwise specified)					
Central government balance 1/										
Revenue	23.1	23.4	23.0	23.5	23.0	22.6	22.5	22.5	22.4	22.4
Taxes	20.7	20.9	20.1	20.5	20.7	20.3	20.3	20.2	20.2	20.2
Non-tax revenue	1.1	1.2	1.5	2.2	1.6	1.5	1.5	1.5	1.5	1.5
Grants	1.3	1.2	1.3	0.8	0.8	0.8	0.8	0.8	0.8	0.8
Expenditure	25.7	24.9	25.4	24.6	25.5	25.4	25.3	24.6	24.6	24.6
Current primary expenditure	18.1	17.7	17.6	18.2	18.3	17.8	17.7	17.6	17.6	17.6
Interest payments	3.5	3.4	3.3	3.2	3.2	3.2	3.2	3.1	3.1	3.1
Capital expenditure	4.1	3.8	4.5	3.2	4.0	4.4	4.4	3.9	3.9	3.9
Natural disaster (ND) annualized cost	...	...	...	...	0.7	0.7	0.7	0.7	0.7	0.7
Primary balance, excl. ND cost	0.9	1.9	0.8	2.1	0.7	0.3	0.4	1.0	1.0	0.9
Primary balance, incl. ND cost	...	...	...	...	0.1	-0.3	-0.2	0.3	0.3	0.3
Overall balance excl. ND cost	-2.5	-1.5	-2.4	-1.1	-2.5	-2.9	-2.7	-2.1	-2.1	-2.2
Overall balance, incl. ND cost	...	...	...	...	-3.2	-3.5	-3.4	-2.8	-2.8	-2.8
Public sector debt	66.1	66.2	65.5	64.3	65.5	69.1	72.6	73.7	74.1	74.1
Domestic	34.7	34.5	32.0	33.2	33.5	34.7	35.9	35.9	36.2	36.4
External	31.4	31.6	33.5	31.2	32.0	34.4	36.7	37.8	37.9	37.7
Money and credit, end of period (annual percent change)										
Broad money (M2)	5.8	2.3	0.2	3.4	3.7	5.4	5.1	4.4	3.5	3.5
Credit to private sector (real)	-5.8	-4.8	-2.0	-3.3	-1.4	-1.2	0.1	0.9	1.0	1.5
Credit to private sector (nominal)	-6.8	-7.8	-1.9	-1.0	0.7	0.9	2.1	2.9	3.0	3.5
Balance of payments										
Current account balance, *o/w:*	0.0	-7.1	-1.1	2.3	3.0	-1.3	-2.6	-0.7	-0.3	0.0
Exports of goods and services	59.1	54.0	57.2	58.6	57.7	56.6	55.9	55.1	55.2	56.0
Imports of goods and services	-50.4	-54.4	-52.7	-50.8	-49.4	-52.6	-53.2	-50.6	-50.2	-50.8
Capital account balance	0.8	0.8	0.7	0.7	0.8	0.8	0.8	0.8	0.8	0.8
Financial account balance	3.9	-4.7	-0.1	2.5	3.8	-0.5	-1.8	0.0	0.5	0.8
Direct investment	-7.8	-8.8	-3.2	-3.5	-3.9	-5.2	-5.0	-5.0	-5.0	-5.0
Portfolio investment	0.0	1.7	-3.3	3.4	2.4	3.4	3.4	3.0	2.5	2.5
Other investment	8.1	3.2	5.6	4.4	4.4	-2.2	-0.5	3.0	2.9	3.7
Net reserves assets	3.7	-0.8	0.8	-1.9	0.9	3.5	0.2	-1.0	0.0	-0.5
Errors and omissions	3.0	1.6	0.2	-0.5	0.0	0.0	0.0	0.0	0.0	0.0
Overall balance	3.0	1.6	0.2	-0.5	0.0	0.0	0.0	0.0	0.0	0.0
External debt (gross) 2/	70.7	67.4	68.8	65.9	66.7	67.9	66.4	65.2	65.5	64.0
Public	31.4	31.6	33.5	31.2	32.0	34.4	36.7	37.8	37.9	37.7
Savings-Investment balance	0.0	-7.1	-1.1	2.3	3.0	-1.3	-2.6	-0.7	-0.3	0.0
Savings	18.1	13.4	20.5	23.4	24.7	23.1	22.2	22.4	21.3	21.1
Investment	18.1	20.5	21.6	21.1	21.6	24.4	24.8	23.2	21.6	21.1
Public 3/	4.2	4.4	5.5	4.6	4.8	7.3	8.3	6.6	5.0	4.6
Private	13.9	16.1	16.1	16.5	16.9	17.1	16.6	16.6	16.6	16.6
Memorandum items:										
Nominal GDP (EC$ millions)	4,480	4,594	4,905	5,189	5,381	5,672	5,963	6,229	6,449	6,676
Net imputed international reserves										
Months of imports of goods and services	4.3	3.7	3.9	3.4	3.6	4.0	3.8	3.6	3.5	3.2
Percentage of demand liabilities	91.4	90.7	91.1	90.7	90.9	92.2	91.9	91.1	90.9	90.3

Sources: St. Lucia authorities; ECCB; UNDP HDI; and Fund staff estimates and projections.

1/ Fiscal year (April–March) basis. Fiscal balances do not include the airport project, which is implemented by a public corporation.

2/ Comprises public sector external debt, foreign liabilities of commercial banks and other private debt.

3/ Comprises investment by the central government and construction expenditures of public corporations, incl. the US$175 million airport project.