INTERNATIONAL MONETARY FUND

Staff Country Reports

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Eastern Caribbean Currency Union: 2009 Discussion on Common Policies of Members Countries—Staff Report; and Public Information Notice on the Executive Board Discussion

This staff report on common policies of member countries of the Eastern Caribbean Currency Union (ECCU) was prepared by a staff team of the International Monetary Fund in the context of the periodic regional surveillance of the ECCU. The regional perspective of such discussions is intended to strengthen the bilateral discussions that the IMF holds with members in the region under Article IV of the IMF's Articles of Agreement. The following documents have been released and are included in this package:

- The staff report for the 2009 Discussion on Common Policies of Member Countries, prepared by a staff team of the IMF, following discussions that ended on April 2, 2009, with the officials of the ECCU on economic developments and policies. Based on information available at the time of these discussions, the staff report was completed on April 30, 2009. The views expressed in the staff report are those of the staff team and do not necessarily reflect the views of the Executive Board of the IMF.

- A Public Information Notice (PIN) summarizing the views of the Executive Board as expressed during its May 15, 2009, discussion of the staff report.

The document listed below have been or will be separately released.

Selected Issues Paper

The policy of publication of staff reports and other documents allows for the deletion of market-sensitive information.

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INTERNATIONAL MONETARY FUND

EASTERN CARIBBEAN CURRENCY UNION

Staff Report for the 2009 Discussion on Common Policies of Member Countries

Prepared by the Staff Representatives for the 2009 Discussion with the Eastern Caribbean Currency Union

Approved by José Fajgenbaum and Philip Gerson

April 30, 2009

EXECUTIVE SUMMARY

- **Focus.** The mission focused on measures to address the spillovers arising from the global financial crisis, deteriorating regional growth, and increased stresses affecting the region's financial system.

- **Economic outlook.** Regional growth will contract in 2009, reflecting a collapse in tourist arrivals and construction activity, and increasing financial sector strains. As most ECCU economies are operating below potential, inflation will be constrained. Uncertainties about the length and depth of the global recession tilt risks to the downside. High public debt levels (91 percent of GDP at end-2008), in the context of a regional currency board arrangement, exacerbate the region's vulnerability to shocks, and limit the room for counter-cyclical fiscal policies.

- **Financial sector.** The financial system has increasingly come under stress, particularly through weakly supervised nonbank and offshore financial sectors, with knock-on effects to domestic banks. In response, ECCU authorities have accelerated the establishment of national Single Regulatory Units and the passage of harmonized legislation to strengthen regulation and supervision of nonbanks and offshore institutions. Credit risk, high government exposures, and liquidity risk are major threats to banking system stability.

- **Fiscal policy.** Recession-induced revenue losses and higher debt servicing costs are projected to raise the overall regional fiscal deficit to about 6.8 percent of GDP in 2009 (4⅔ percent in 2008). To maintain confidence in the credibility of the currency board arrangement, the national and regional authorities should contain fiscal slippages and operationalize the ECCB's revised fiscal benchmarks.

- **External competitiveness.** The real effective exchange rate appears broadly in line with fundamentals. Though largely financed by nondebt-creating FDI flows, elevated current account deficits (about 34 percent of GDP in 2008) pose significant risks that warrant careful monitoring.

- **Crisis preparedness.** The mission encouraged the authorities to develop further contingency plans for possible crisis scenarios, including a prolonged economic slowdown, large-scale bank runs and capital flight.

- **Fund financing.** To help mitigate the balance of payments impact of the downturn in tourism and FDI flows, St. Vincent and the Grenadines, Dominica and St. Lucia have requested financing under the Rapid-Access component of the Exogenous Shocks Facility; Grenada has requested an augmentation under its PRGF Arrangement; and St. Kitts and Nevis has requested a purchase under the Emergency Assistance for Natural Disasters Facility.

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ACRONYMS

ACP	Africa, Caribbean and Pacific
AML/CFT	Anti-Money Laundering/Combating the Financing of Terrorism
CARICOM	Caribbean Community
CARIFORUM	CARICOM countries and the Dominican Republic
CARTAC	Caribbean Regional Technical Assistance Centre
CBA	Currency Board Arrangement
CBERA	Caribbean Basin Economic Recovery Act
CCRIF	Caribbean Catastrophe Risk Insurance Facility
CDB	Caribbean Development Bank
CDF	Caribbean Development Fund
CFATF	Caribbean Financial Action Task Force
CIDA	Canadian International Development Agency
CSME	CARICOM Single Market and Economy
CTO	Caribbean Tourism Organization
CWC	Cricket World Cup
EC	Eastern Caribbean
ECCB	Eastern Caribbean Central Bank
ECCU	Eastern Caribbean Currency Union
ECSE	Eastern Caribbean Securities Exchange
ECSRC	Eastern Caribbean Securities Regulatory Commission
EDF	European Development Fund
EPA	Economic Partnership Agreement
EU	European Union
FAD	Fiscal Affairs Department
FDI	Foreign Direct Investment
FSAP	Financial Sector Assessment Program
GARFIN	Grenada Authority for the Regulation of Financial Institutions
LEG	Legal Department
LOLR	Lender of Last Resort
MCM	Money and Capital Markets Department
NBFI	Nonbank Financial Institution
NPL	Nonperforming Loan
OECD	Organization for Economic Cooperation and Development
OECS	Organization of Eastern Caribbean States
PRGF	Poverty Reduction and Growth Facility
PSIA	Poverty and Social Impact Analysis
PSIP	Public Sector Investment Program
ROC	Regional Oversight Committee
ROSC	Report on the Observance of Standards and Codes
REER	Real Effective Exchange Rate
RGSM	Regional Government Securities Market
SRU	Single Regulatory Unit
STA	Statistics Department
UIS	Unregulated Investment Scheme
VAT	Value Added Tax
WHD	Western Hemisphere Department
WTO	World Trade Organization

I. Brief Perspective

1. **The ECCU—a regional currency board arrangement—consists of eight small, open, tourism-dependent island economies that are highly vulnerable to external shocks** (Figures 1 and 2).[1] The ECCU is the world's only currency union in which members pool their foreign reserves, and the level of the exchange rate peg has not been changed in more than three decades. The exchange rate stability has helped foster a highly monetized and stable financial system.

2. **While social indicators are favorable, the region's deteriorating macroeconomic performance, poverty and crime remain concerns.** ECCU countries rank high on the United Nation's Human Development Index relative to other countries with similar income levels, with improving governance indicators (Figure 3). However, in the face of a series of negative shocks since the mid-1990s, including erosion of trade preferences, declining aid flows, adverse terms of trade movements, and natural disasters, governments have eased fiscal stances repeatedly to buffer these shocks, resulting in large fiscal deficits and very high public debt levels (Figure 4). Pockets of poverty, along with rising criminal activity, threaten both social consensus and prospects for the important tourism sector.

ECCU: Social Indicators

	Antigua and Barbuda	Dominica	Grenada	St. Kitts and Nevis	St. Lucia	St. Vincent and the Grenadines	ECCU
Poverty headcount index, 2000 1/	12	33	32	31	25	38	28.5
HDI rank (2008), of 179 countries	59	77	86	60	66	92	...
Life expectancy (years), 2006	72.7	74.1	68.4	71.2	73.4	71.3	71.9
Adult illiteracy rate (percent), 2004	14.0	12.0	4.0	2.2	5.2	11.9	8.2
Mortality rate, infant (per 1000 live births, 2006)	10.0	13.0	16.2	16.8	12.2	17.1	14.2
Gini coefficient	0.525	0.488	0.504	0.445	0.468	0.448	0.480

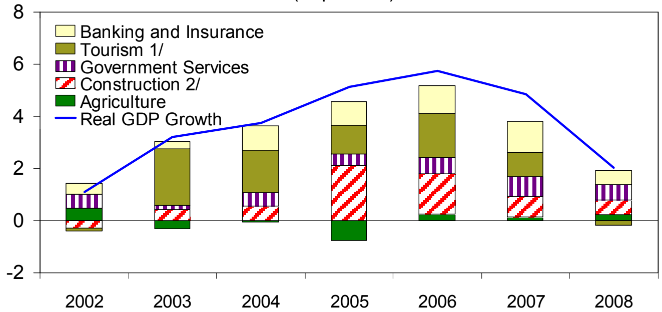
Sources: ECCB; Fund staff estimates and projections; United Nations, Human Development Report 2008; and the World Bank, WDI 2007.
1/ Percentage of population living below each country's locally-defined poverty line in 2000.

[1] The Eastern Caribbean Currency Union (ECCU) comprises six Fund members: Antigua and Barbuda, Dominica, Grenada, St. Kitts and Nevis, St. Lucia, and St. Vincent and the Grenadines; and two territories of the United Kingdom, Anguilla and Montserrat. Fund relations are summarized in the Informational Annex.

II. Recent Developments

3. **Following a period of strong growth, the region is facing a volatile and weakening external environment.** GDP growth moderated slightly from a decade high of 6⅓ percent in 2006 to about 5 percent in 2007, reflecting the unwinding of the Cricket World Cup (CWC)-related construction boom, declining stayover tourist arrivals, and the impact of Hurricane Dean. For 2008 growth declined further to 1.8 percent, given a sharply slowing global economy, declining tourist arrivals, the global financial crisis, and elevated world commodity prices.[2] ECCU members have also displayed an uneven pace of growth deceleration (Figure 5).

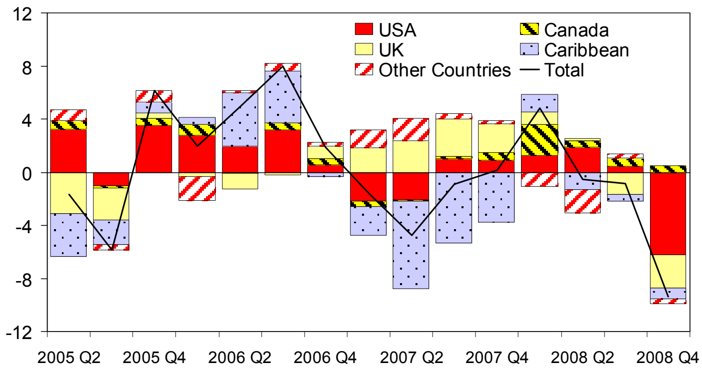
ECCU: Contribution to Real GDP Growth by Sector, 2002–08
(In percent)



Sources: ECCB; and Fund staff projections.
1/ Includes wholesale and retail trade, hotel and restaurant, air transport, and half of local transport.
2/ Includes mining and quarrying.

4. **In response to large shocks to tourism receipts and FDI, most ECCU countries have expressed interest in Fund financing.** Despite positive growth in the first half of 2008, stayover tourist arrivals fell by 5 percent in the second half, reflecting the impact of the global downturn and reduced airlift (Figure 6). This trend has continued into 2009. Beginning in the last quarter of 2008, construction of some tourism accommodation projects has been slowed or placed on hold, owing to financing difficulties and sluggish sales. To help mitigate the balance of payments impact of the downturn in tourism and FDI, St. Vincent and the Grenadines, Dominica and St. Lucia have requested financing under the Rapid-Access component of the Exogenous Shocks Facility; Grenada has requested an augmentation under its PRGF program; and St. Kitts and Nevis has requested a purchase under the Emergency Assistance for Natural Disasters Facility, in the wake of Hurricane Omar's destruction of tourism infrastructure.

ECCU: Stayover Arrivals, 2005–08
(Annual percentage change)

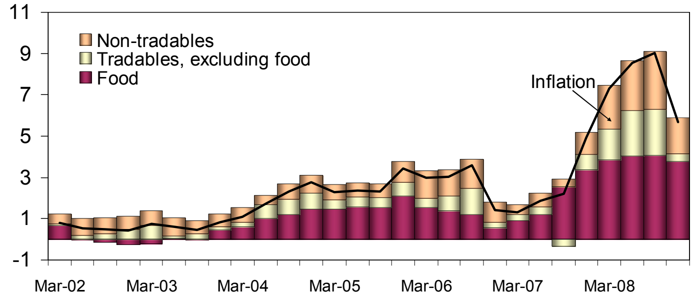


Sources: ECCB; and Fund staff estimates.

[2] The estimated growth rate would mark a regional recession in 2008, as it was less than 2.2 percent per annum, which is the growth rate that is one standard deviation below the ECCU mean rate of economic growth (4.6 percent) over the period 1965–2008.

5. **Following a strong acceleration during the first three quarters, inflation eased toward end-2008.** Inflation spiked due in large part to the global commodity price shock and the depreciation of the U.S. dollar against major currencies, which raised import prices of food and fuel (Figure 7). Inflation rose to 9 percent in the year to September 2008, compared with an annual average of 2–3 percent for the prior two decades. The ECCU authorities sought to mitigate the social implications of higher inflation, which has a disproportionately adverse impact on the poor. Temporary ameliorative measures included: the suspension of import duties and other taxes on basic consumer items; controls on retail markups and profit margins; and limited commodity price subsidies to vulnerable groups. Inflationary pressures eased toward end-2008, as world commodity prices retreated from record highs amid slowing global growth.

ECCU: Contribution to Inflation, 2002–08 1/
(Percent change)



Sources: ECCB; and Fund staff calculations.
1/ Tradables in the ECCU comprise food, alcoholic drink and tobacco, fuel and light, clothing and footwear, household and furniture equipment; non tradables include medical care and expenses, education, personal services, housing and utilities, miscellaneous and transportation and communication.

6. **Growth of monetary aggregates decelerated markedly in 2008** (Figures 8 and 9). Led by expansion in lending to the tourism, consumer durables, and construction sectors, private sector credit grew by 20 percent in 2007. By end-2008 credit growth had halved, in the context of tighter lending terms and conditions established by ECCU banks (particularly foreign-owned banks) and sluggish credit demand. As broad money growth decelerated amid the economic slowdown, both foreign and local banks relied on drawdowns of their net foreign assets to finance domestic credit provision. In particular, from September 2008 local banks picked up their pace of drawdown significantly, while foreign banks' drawdowns slowed. Despite some moderate loss of foreign reserves, reserve coverage of demand liabilities (mainly currency in circulation plus commercial banks' reserves at the ECCB) remained at about 100 percent at end-2008.

ECCU: Selected Monetary Indicators, 2004–09

	2004	2005	2006	2007	Prel. 2008	Proj. 2009
	(Annual percentage change)					
Broad money	13.2	8.4	11.6	9.7	3.0	-1.0
Net foreign assets 1/	6.8	1.2	2.0	-1.5	-7.0	-2.7
Net domestic assets 1/	6.4	7.2	9.6	11.2	9.9	1.6
Of which						
Private sector credit 1/	5.1	9.2	14.6	17.3	10.2	1.0
Currency backing ratio, in percent 2/	96.2	96.5	98.7	100.1	102.0	...

Source: ECCB.
1/ Twelve–month change in percent of broad money at the beginning of the period.
2/ Defined as ratio of the ECCB's gross foreign reserves to demand liabilities.

ECCU: Deceleration of Monetary Growth in 2008
(Percentage change)

	2008	Jan-Aug 08	Sep-Dec 08
Net foreign assets of banks	-78.2	-22.7	-55.6
Foreign banks	-60.2	-55.2	-5.0
Local banks	-25.9	6.8	-32.7
Private sector credit	10.8	6.9	3.9
Foreign banks	6.9	4.9	2.1
Local banks	14.8	10.1	4.8
Private sector deposits	3.0	4.2	-1.2
Foreign banks	1.2	2.5	-1.3
Local banks	4.3	7.1	-2.8

Sources: ECCB; and Fund staff estimates.

7. **While prudential indicators remain strong, signs of pressure have recently emerged** (Figure 10). ECCU banks appear to be reasonably capitalized and profitable. Nevertheless, the trend of improving prudential indicators began to reverse in 2008. In particular, with moderation of credit growth in a rapidly-slowing economy, banks' nonperforming loans (as a share of total loans) have crept up, while profitability, loan loss provisioning, and capital adequacy ratios have declined moderately. More worrisome is the marked decline in banks' liquidity (Figure 11). In addition, banks' government exposures remain high, and are concentrated in several state-owned local banks (Figure 12).

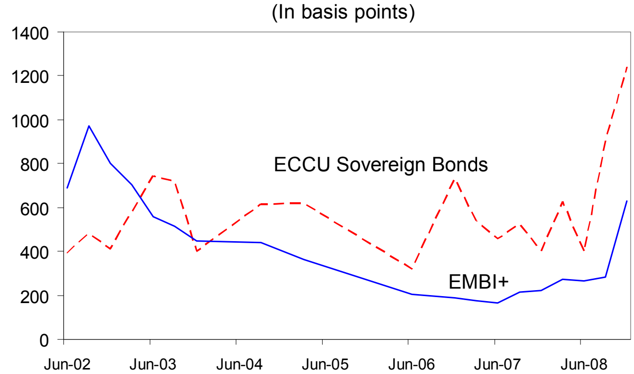
ECCU Banking System: Financial Soundness Indicators, December 2008
(In percent)

	Anguilla	Antigua & Barbuda	Dominica	Grenada	Montserrat	St. Kitts & Nevis	St. Lucia	St. Vincent & Grens.	ECCU
Capital adequacy 1/	15.5	16.9	15.0	15.1	47.7	47.3	15.6	17.9	20.1
Liquid assets/total assets	22.4	36.5	41.7	24.1	92.1	38.8	16.7	33.8	22.1
(Pre-tax) return on average assets	1.4	2.2	0.7	1.9	1.7	4.7	3.2	2.0	2.6
NPLs/total loans	8.7	14.2	7.1	3.5	5.5	5.2	6.6	3.9	7.7
Loans to households/total loans	50.7	41.6	54.6	58.4	80.0	36.1	30.5	48.9	42.3
Gross government exposure/total assets	7.7	11.8	11.9	12.7	9.8	28.2	9.7	18.4	14.3

Source: ECCB.
1/ Local banks.

8. **Liquidity conditions are tightening.** Commercial banks' excess reserves at the ECCB dropped and interbank interest rates increased toward the end of 2008. Since banks usually account for about 50 percent of the value of bids, oversubscription in the Regional Government Securities Market (RGSM) also declined sharply.[3] Nevertheless, interest rates on the RGSM have only risen slightly. In contrast, spreads on ECCU sovereign bonds in the over-the-counter repo market spiked to an unprecedented level at end-2008, signaling that ECCU governments, particularly those with high debt levels, are facing higher financing costs. In addition, as of March 2009, the Eastern Caribbean Stock Exchange index had declined by 16 percent from its peak in late 2007.

ECCU: Sovereign Bond Spreads in Trinidad and Tobago 1/
(In basis points)



Sources: Bloomberg; Caribbean Money Market Brokers; and Fund staff calculations.
1/ Spreads are computed relative to U.S. bonds of comparable maturities.

9. **The failure and subsequent intervention of Trinidad and Tobago-based CL Financial Group in January 2009 has had adverse effects on the Caribbean financial sector, through its extensive cross-border insurance, investment, and banking linkages, and exposed weaknesses in the region's regulatory framework for nonbanks.** An important source of financing for the rapid expansion of CL Financial in

[3] The RGSM is a regional, auction-based system for marketing government securities of ECCU members. The market has been in operation since November 2002, and market capitalization has grown to almost EC$922 million (7 percent of regional GDP) at end-2008.

recent years was the offer of fixed-term deposit-like financial products through the group's insurance subsidiaries operating in the ECCU—CLICO Life Insurance (CLI) and British American Insurance (BAI). These deposit accounts yielded annual interest rates far in excess of those offered by commercial banks, and not only undermined the client base for the domestic commercial banking system but, as now revealed, the higher interest rates reflected the far riskier investment activities in which their principal (CL Financial) was engaged. The collapse of CL Financial prompted 'deposit runs' on CLI and BAI branches operating in the ECCU. The combined exposure of CLI and BAI to policy and deposit holders in the ECCU amounts to about EC$2 billion (about 15 percent of ECCU GDP), against which ECCU governments would probably not be able to provide credible guarantees.[4]

10. **The ECCU's offshore financial sectors have also been adversely affected by increased scrutiny from advanced economies.** In February 2009, fraud charges were levied by the U.S. Securities and Exchange Commission (SEC) against Sir Allen Stanford and the Stanford International Bank (SIB), an offshore bank based in Antigua and Barbuda. This action also triggered a run on deposits on the Stanford-owned Bank of Antigua (BOA), a domestic commercial bank. The ECCB's initial policy response to the deposit run comprised moral suasion and the provision of emergency liquidity. Later, the ECCB intervened under its "special emergency powers" and on February 23 arranged a consortium of ECCU domestic banks and governments to form a new entity (Eastern Caribbean Amalgamated Financial Company Limited) to manage the operations of BOA, thereby ending the run on deposits.

11. **External imbalances remain elevated**. The current account deficit surged to 35 percent of GDP in 2007, financed almost fully by nondebt-creating foreign direct investment (Figure 13). The current account deficit is estimated to have remained at a similar level during 2008, as slowing construction-related imports offset falling tourism receipts and higher fuel and food imports. Reflecting sluggish private capital inflows (largely FDI), gross international reserves declined by about US$5 million to US$760 million by end-2008 (equivalent to about 3½ months of imports).

ECCU: Selected External Indicators, 2004–09

	2004	2005	2006	2007	Prel. 2008	Proj. 2009
	(In percent of GDP)					
External current account balance	-16.4	-22.4	-29.7	-34.8	-33.9	-24.2
Direct investment (net)	13.6	17.3	26.3	27.7	22.6	16.3
Gross international reserves (US$m)	632.4	600.8	696.0	764.5	759.0	687.4
	(Annual percentage change)					
Exports of goods	11.6	8.0	-2.5	4.8	12.9	-8.6
Imports of goods	5.5	18.0	17.0	13.3	4.3	-25.6
Travel (net)	12.0	3.1	0.2	1.8	-2.7	-15.7
Terms of trade (goods and services)	-4.4	-2.8	-9.7	-1.5	-14.0	...
Stayover arrivals	10.0	1.3	2.8	-1.8	-1.3	-11.6
Real effective exchange rate	-3.6	-0.9	-0.1	-2.3	1.1	...

Sources: ECCB; and Fund staff estimates.

[4] In April 2009 Ministers of Finance and central banks of the ECCU, Trinidad and Tobago and Barbados announced that a US$80 million Liquidity Support Fund will be established, designed to support the liquidity position of BAI operations in the ECCU.

12. **Limited progress has been made in fiscal consolidation.** Tax revenues have increased, benefiting from strengthened tax administration and broader tax bases (particularly owing to the introduction of VATs and market-valuation-based property taxes). Capital expenditure peaked in 2006, reflecting CWC and tourism-related investment, but has since declined, and current expenditure remained high. As a result, some fiscal consolidation was achieved during 2007, although no major progress was made in 2008.

ECCU: Selected Fiscal Indicators, 2004–09

	2004	2005	2006	2007	Prel. 2008	Proj. 2009
	(In percent of GDP)					
Revenues	26.4	26.4	27.7	28.4	28.1	26.4
Grants	2.6	3.5	3.6	2.3	2.9	2.5
Noninterest current expenditures	22.3	21.8	22.1	22.2	22.6	23.3
Interest	4.4	3.9	4.0	3.6	3.9	4.5
Capital expenditures	6.7	8.6	10.3	9.3	9.1	7.8
Primary balance (excluding grants)	-2.6	-4.0	-4.7	-3.1	-3.6	-4.7
Primary balance (including grants)	0.1	-0.5	-1.1	-0.8	-0.7	-2.2
Overall balance	-4.3	-4.4	-5.1	-4.4	-4.7	-6.8
Memorandum items:						
Public sector debt	107.3	100.5	98.4	94.5	90.6	97.9

Sources: Country authorities; and Fund staff estimates.

13. **Some success has been achieved in winding back public debt burdens, yet more needs to be done to lower vulnerabilities.** Strong economic growth since 2001, along with debt restructurings (Dominica and Grenada) and debt writedowns (Antigua and Barbuda and St. Vincent and the Grenadines) has lowered the regional debt ratio from its high of 107 percent of GDP in 2004 to 91 percent of GDP in 2008. Nonetheless, Anguilla and Montserrat are the only ECCU members with public debt levels that are currently below the ECCB's debt-to-GDP benchmark of 60 percent (to be achieved by 2020).

ECCU: Selected Indicators of Central Government Debt Burden, 2004–09

	2004	2005	2006	2007	Prel. 2008	Proj. 2009
	(In percent of current revenues)					
Interest payments	**16.7**	**14.8**	**14.6**	**12.7**	**14.2**	**17.2**
Anguilla	2.8	3.7	3.5	3.4	3.9	7.9
Antigua & Barbuda	23.0	22.1	21.5	15.2	19.7	24.3
Dominica	17.9	16.3	6.9	7.2	6.1	6.5
Grenada	25.2	8.3	8.3	8.9	9.5	12.5
Montserrat	1.6	2.8	3.4	2.7	3.5	4.5
St. Kitts & Nevis	20.8	22.1	26.6	22.5	23.8	30.5
St. Lucia	11.9	12.0	12.5	12.6	14.0	15.7
St. Vincent & the Grens.	8.6	10.8	11.0	10.4	9.7	10.5
Debt service 1/	**30.3**	**36.8**	**21.1**	**22.6**	**21.2**	**25.7**
Anguilla	3.2	4.1	3.8	3.9	4.4	9.1
Antigua & Barbuda 2/	53.4	106.6	27.6	21.8	26.8	35.1
Dominica	35.5	24.1	11.4	11.8	16.2	15.6
Grenada	40.4	12.3	13.3	14.1	15.0	18.7
Montserrat	2.0	3.1	3.7	3.0	3.8	4.8
St. Kitts & Nevis	33.2	34.9	36.9	35.0	33.3	40.7
St. Lucia	14.8	18.7	18.6	32.2	19.7	21.8
St. Vincent & the Grens. 2/	19.4	21.9	20.6	19.8	19.1	22.2

Sources: Country authorities; and Fund staff estimates.
1/ Includes only external amortization.
2/ For 2005 and 2007, the debt service incorporates amortization in relation to debt relief received by Antigua and Barbuda and St. Vincent and the Grenadines from Italy.

14. **Regional integration initiatives continue at varying speeds.** Economic integration in the Eastern Caribbean continues to gain traction. Public consultations on a draft OECS Economic Union Treaty, approved by OECS member states in May 2007, started in several jurisdictions during 2008.[5] The Economic Union is expected to be formally in place by end-2009. In November 2008 OECS Heads of Government agreed to Trinidad and Tobago joining the Economic Union by 2011. In contrast, progress in implementing the CARICOM Single Market and Economy (CSME) has been limited, partly because the participation of OECS countries is predicated on the establishment of a US$250 million Caribbean Development Fund (CDF) to support their development needs, which has not yet been made fully

[5] The Organization of Eastern Caribbean States (OECS) comprises Antigua and Barbuda, Dominica, Grenada, Montserrat, St. Kitts and Nevis, St. Lucia, and St. Vincent and the Grenadines, with Anguilla and the British Virgin Islands as associate members.

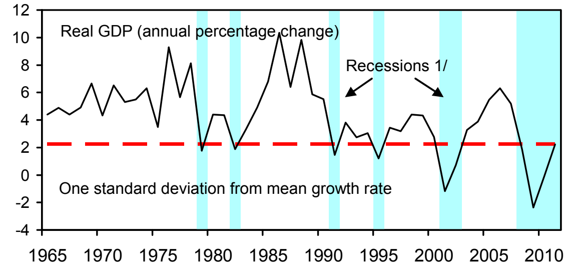
operational.[6] In October 2008 CARIFORUM countries, including all eight ECCU members, signed an Economic Partnership Agreement (EPA) with the European Union, the first among ACP regions.[7] The EPA replaced unilateral preferential access with phased-in reciprocal free trade (Box 1). CARICOM countries are also in negotiation with Canada on a Trade and Development Agreement.

III. Outlook and Risks

15. **The ECCU region is expected to fall deeper into recession in 2009.**

- *Real GDP* is expected to contract by about 2½ percent, as the tourism and construction sectors are being hit hard by the global economic downturn. A slow recovery is projected for 2010 and the medium term, predicated on a rebound of the global economy, increasing tourism demand, and utilization of the region's enhanced accommodation capacity. Compared with the 2001–02 recession, this recession is expected to be deeper and more prolonged, with the region expected to remain in recession for four years beginning in 2008.

***The recession will be deeper and longer this time around*.**



Sources: IMF, International Financial Statistics; World Economic Outlook; and Fund staff estimates.
1/ Recession is defined as growth falling below historical average minus one standard deviation.

- *Inflation* is expected to return to its long-run average of 2–3 percent per year, as the regional output gap widens and world food and energy prices retreat alongside the slowing global economy.

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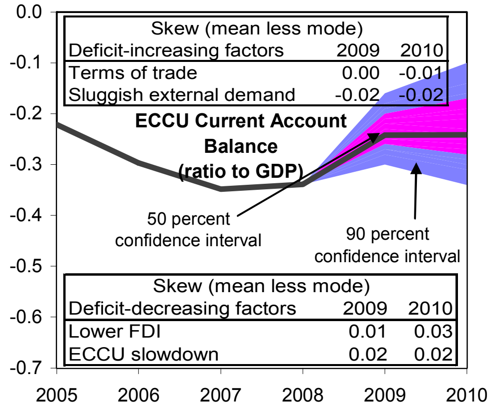
[6] The CDF, which officially started operations on November 1, 2008, is headquartered in Barbados and managed by a Board of Directors drawn from CARICOM members. CARICOM member states have contributed US$67 million, with an additional contribution of US$53 million due by mid-2009.

[7] All ECCU members (with the exception of Anguilla) are eligible to export goods covered under the Caribbean Basin Economic Recovery Act (CBERA) to the U.S. duty free. In March 2009 the World Trade Organization approved a waiver request of the U.S. on CBERA, extending trade preferences for exports of CARICOM countries to 2014.



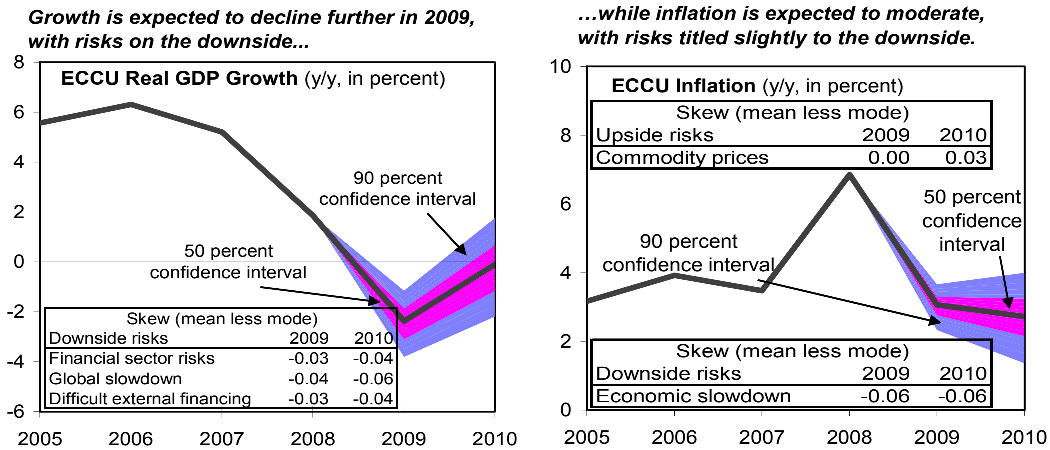
Source: Fund staff estimates.

- *External current account deficits* are projected to narrow markedly in 2009, with weaker demand for imports (owing to slowing FDI and domestic demand) and favorable movement in the region's terms of trade (underpinned by falling commodity import prices) more than offsetting the impact of continued lackluster tourism performance and declines in remittances and exports. However, the balance of payments is expected to post a larger deficit, as capital inflows are projected to decline by more than the current account deficit. Accordingly, growth of monetary aggregates is expected to continue to slow. Since the region's fiscal position is expected to deteriorate markedly in 2009, the balance of payments adjustment will reflect sharp declines in private investment and consumption (as a share of GDP).

16. **The outlook is subject to large uncertainties and downside risks.** The length and depth of the recession is particularly difficult to predict. Key influencing factors include: (i) the length and depth of the global slowdown, and the magnitude of spillovers to the ECCU region; (ii) the availability and cost of external financing for both the public and private sectors; and (iii) the severity of financial stress amid the global storm. Should these downside risks materialize, the ECCU region, as with other countries with large external and internal imbalances and limited scope for countercyclical policy responses, would be vulnerable to a much deeper and longer local recession.

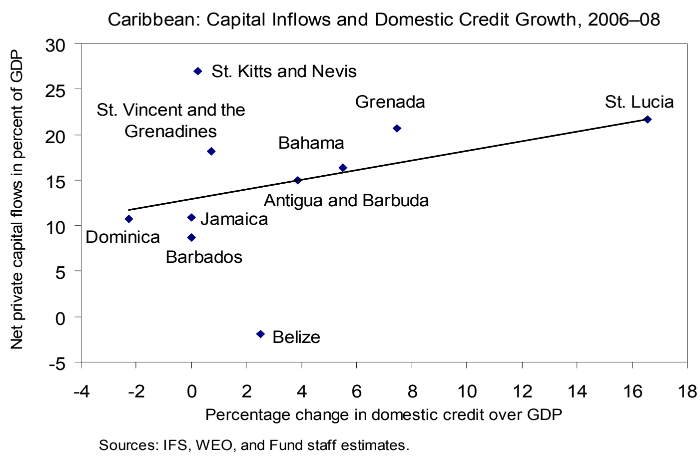
17. **A deeper and more prolonged global downturn would weigh heavily on the region's growth outlook.** Staff analysis suggests that both trend growth and business cycles in the region have been heavily influenced by the U.S. in the past—a 1 percent negative shock to the U.S. growth rate is found to translate into a decline of ½ percent in the ECCU region's growth within the first year (Box 2).[8] Potential transmission channels of slower growth in advanced economies include: (i) declining tourism receipts, particularly those derived from the U.S., which is the source of one third of the stayover tourists to the region; (ii) the region's dependence on growth-affected remittance flows; and (iii) sluggish property sales, which in turn leads to construction of tourism accommodation (hotels, condominiums and villas) being delayed or even terminated.

[8] See also Y. Sun and W. Samuel (2009), "ECCU Business Cycles: Impact of the United States," IMF Working Paper 09/71.



Source: Fund staff estimates.

18. **A sudden stop or abrupt reversal of external capital flows poses another source of risk.** Private capital flows have financed tourism construction (particularly FDI), and supported the rapid expansion of domestic credit (such as funding from foreign parent banks to local branches). A sudden stop or abrupt reversal of private capital flows would lead to a credit squeeze in the region, dampening growth further and affecting current account sustainability. With its external borrowing largely sourced on commercial terms, the ECCU public sector is also vulnerable to global credit strains, through heightened rollover risks and elevated interest costs. This vulnerability could have serious implications for fiscal and debt sustainability. Moreover, as local banks have very high government exposures, difficulties in governments' debt servicing capacity could threaten bank stability, and adversely affect the level of international reserves needed to sustain the currency board arrangement.



19. **Banking systems in the region have a strong presence of Canadian banks, which has helped limit the local impact of the global financial crisis.** In comparison with other developed-country peers, Canadian banks remain resilient due to strong supervision and regulation, stringent capital requirements, and more conservative lending practices. Nevertheless, Canadian financing conditions have tightened, with similar implications for the branches of Canadian banks operating in the ECCU.

20. **Severe financial stress would further dampen economic activity.** The region has many foreign financial institutions, including branches of foreign banks, insurance companies, and offshore banks. The recent CL Financial and Stanford Group events demonstrated that external financial shocks can be quickly transmitted to the region through such financial institutions. Furthermore, the presence of financial conglomerates and complicated ownership structures within the Caribbean increase the contagion risk across different types of financial institutions as well as across borders. Lastly, the region's social security systems have provided a stable source of deposits to banks. Should there be major impairment of social security systems' investment portfolios amid the financial storm, banking system stability could be threatened.

ECCU: The Importance of Foreign Banks
(As of end-2008; in EC$ millions)

	Foreign Banks	Local Banks	Total	Share of Foreign Banks (In percent)
Private sector deposits	4,542	6,265	10,807	42.0
Bank loans and investments 1/	6,242	8,500	14,742	42.3
Of which: Private sector credit	5,660	5,918	11,578	48.9

Sources: ECCB; and Fund staff calculations.
1/ Including domestic loans, advances, and investments.

ECCU: Cross Border Linkages of the Banking System

	Gross Claims on Other ECCU Public Sectors		Due to Other ECCU Banks		Due from Other ECCU Banks	
	Dec-04	Dec-08	Dec-04	Dec-08	Dec-04	Dec-08
	(in percent of bank assets)					
Anguilla	1.1	1.1	2.2	4.7	4.8	3.4
Antigua and Barbuda	0.6	0.5	3.5	11.4	2.2	11.5
Dominica	2.8	5.9	1.1	1.9	11.9	14.4
Grenada	1.6	1.3	2.0	3.5	5.0	4.5
Montserrat	12.4	5.4	0.8	27.3	26.4	47.2
St. Kitts and Nevis	1.9	0.1	9.1	9.4	1.5	6.8
St. Lucia	1.4	0.9	3.5	12.1	3.2	3.7
St. Vincent and the Grenadines	3.4	0.5	4.6	10.5	4.7	15.5

Sources: ECCB; and Fund staff estimates.

IV. POLICY DISCUSSIONS[9] [10]

21. **Against this background, policy discussions focused on assessing and managing near-term risks while continuing to address the region's fundamental economic issues.** Discussions with the national and regional authorities focused on four related themes:

- Ensuring the resilience of the financial system;

- Maintaining external stability and bolstering competitiveness;

[9] This report covers regional topics, highlighting the common policy issues of members of the currency union, and provides a regional perspective on economic policies relevant for Fund surveillance for which responsibility lies at the national level. Analysis of the developments and prospects of individual ECCU countries, with a focus on national fiscal and structural policies, can be found in bilateral Article IV staff reports.

[10] Discussions took place during January–March 2009 and the mission comprised, at various stages, P. Cashin (Head), K. Nassar, C. Pattillo, R. Perrelli, W. Samuel, Y. Sun, N. Wagner, and Y. Wong (all WHD). M. Savastano (WHD), M. Horgan, M. O'Sullivan, and M. Morgan (all OED) participated in key meetings. The mission visited each of the six Fund-member countries and two U.K. territories of the ECCU, and met with Prime Ministers, Chief Ministers, Ministers of Finance, senior government officials, representatives of the agricultural, financial and tourism sectors, and senior officials at the ECCB, the Caribbean Development Bank (CDB), the Caribbean Regional Technical Assistance Center (CARTAC), and bilateral donors.

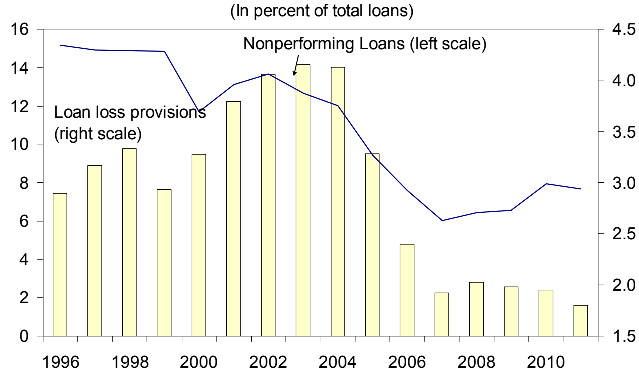
- Enhancing fiscal and debt sustainability; and
- Boosting crisis preparedness and capacity building.

22. **The authorities broadly agreed with the mission's assessment on economic outlook and risks.** To address the challenges facing the region, the mission stressed that the balance of adjustment versus financing needs to tilt heavily toward adjustment. The region has built up high public debt over the last decade—primarily through commercial borrowing—in the face of a series of external shocks, including the erosion of trade preferences and the decline of official development assistance. With its large public debt burden and tightened global liquidity, the ECCU region now has to rely more on fiscal adjustment to navigate though the current economic downturn. While agreeing on the importance of adjustment, the authorities noted that small states (such as ECCU members) warrant differentiated treatment from the international community, as adverse global developments often have disproportionate effects on them. The mission encouraged the authorities to seek more concessional resources and contingent financing lines from multilaterals and bilateral partners, in order to prepare for possible crisis scenarios.

A. Resilience of the Financial System

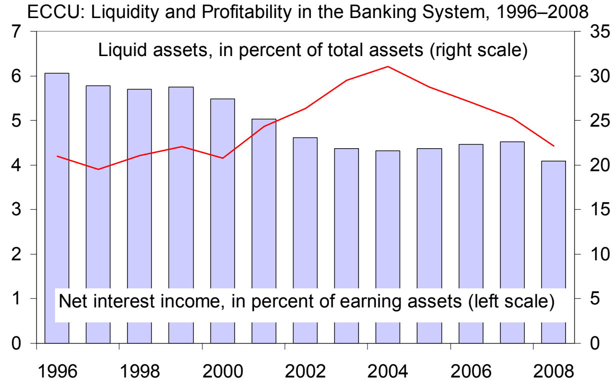
23. **The ECCB's limited lender-of-last-resort (LOLR) role under a currency board arrangement and the absence of a deposit insurance framework highlight the critical importance of closely monitoring banking risks.** The recent deposit run on the Bank of Antigua illustrated that acute liquidity problems can quickly develop, and potentially trigger bank insolvency. Waning economic growth after a period of rapid private credit growth poses another major risk to the stability of the ECCU banking system, through the deterioration of banks' asset quality. The recent deterioration in several prudential indicators does raise concerns. Stress tests confirm that key risks remain, including high government exposures, credit risk, and liquidity risk, with some local banks being particularly vulnerable (Box 3). Cross-border bank linkages in the region are relatively weak, but are increasing, particularly through common ownership structures, pointing to potential cross-country contagion risks.

ECCU: Banking Sector NPLs and Loan Loss Provisions, 1996–2008
(In percent of total loans)



Source: ECCB.

ECCU: Liquidity and Profitability in the Banking System, 1996–2008



Source: ECCB.

24. **The ECCB has stepped up efforts in banking regulation and supervision, but more needs to be done.**

- The ECCB completed 12 on-site inspections in 2008, compared with a total of four in 2007. Progress continues to be made in improving legislation, issuing prudential guidelines, and providing training in supervision. In particular, the harmonized legislation on minimum capital requirements, which empowers the ECCB to raise capital based on bank-specific risk profiles, has been passed in several ECCU jurisdictions. With CARTAC assistance, work on developing a risk-based supervisory framework, to better target on- and off-site inspection of vulnerable banks, is expected to be completed in the first half of 2009. Importantly, beginning in January 2009, all foreign bank branches are required to submit their own audited financial statements to the ECCB. Given the increasing presence of financial conglomerates in the Caribbean, the ECCB also intends to strengthen consolidated supervision (both cross-functional and cross-border). It has requested CARTAC assistance in developing a framework of consolidated supervision and had received some initial training. Lastly, the ECCB has been pursuing better cross-border regulatory cooperation and information sharing with other Caribbean central banks.[11]

- The mission urged the ECCB to increase further the scope and frequency of on-site inspections and remain vigilant on banks' liquidity and credit risks, as well as high government exposures. The ECCB also needs to strengthen follow-up and enforce remedial measures—a corrective action framework for identified weak banks should be initiated. Given banks' indirect exposure to exchange rate risk (e.g., through foreign currency loans offered to domestic residents), regulation and monitoring of foreign exchange risk should be further developed.

25. **The authorities are moving forward with strengthening regulation and supervision of the nonbank financial sector, in the wake of the CL Financial shock.**

- Anguilla, Grenada, and Montserrat are the three ECCU jurisdictions that have established single regulatory units (SRU) for nonbanks. Using these SRUs as a model, all other ECCU jurisdictions have committed to establishing national SRUs in the first half of 2009. An SRU Implementation Committee has been established at the ECCB to facilitate this process.

- The authorities are also committed to accelerating the passage of enabling harmonized legislation, including SRU Acts, Money Services Acts, Cooperatives Acts, Building Society Acts, and Insurance Acts, and to ensuring adequate staffing and training. SRUs, when fully functioning, are expected to improve supervision of the nonbank financial sector by bringing various nonbank financial entities under one supervisory umbrella. The authorities noted an urgent need for capacity building at the level of national regulators, and have sought CARTAC assistance.

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[11] The ECCB signed the Multilateral Memorandum of Understanding of CARICOM Central Banks in 2008.

- The mission welcomed ongoing efforts to develop prudential forms for gathering data from nonbank financial institutions, with a view to develop a comprehensive financial sector survey over the medium term. More generally, it is important to enhance the disclosure of information (covering both on and off-balance sheet exposures) by all financial institutions.

- The mission also recommended that SRUs and the ECCB bolster regulation and supervision of nonbank liabilities, to avoid further instances of regulatory arbitrage such as those exemplified by the bank-deposit-like 'annuity products' offered by domestic insurance companies. The mission welcomed the close collaboration of ECCU governments and the ECCB with their counterparts throughout the region in seeking a prompt and sustainable solution to the CL Financial issue, and urged them to move quickly with their proposed intervention, to help prevent asset stripping and any further deterioration of the deficits in the insurance statutory funds. The IMF has provided (and will continue to provide) technical assistance on resolution options for both traditional insurance policyholders and for investors in insurance deposit-like products.

26. **Actions have been taken against unregulated investment schemes (UIS) operating in the ECCU.** It has been determined that the Eastern Caribbean Securities Regulatory Commission (ECSRC) has the jurisdiction to act against UIS seeking to operate in the ECCU region. Following requests from both the Grenada and Dominica financial services regulators, in mid-2008 the ECSRC issued "cease and desist" orders against a UIS operating in Grenada and Dominica (which was subsequently made public) and against another UIS seeking to operate in Grenada. Other national regulators have also been investigating if similar UIS exist in their respective jurisdictions. The ECSRC is fully prepared to proceed accordingly, at the request of national regulators. The authorities noted that the fallout from domestic investment in UIS on the ECCU financial system had been very limited, as this issue had been confronted at an early stage. [12]

27. **The region's offshore financial sectors are facing serious challenges as developed country regulatory authorities move to heighten scrutiny and regulation.** While several ECCU countries have enhanced supervision of their offshore financial sectors, there has been little progress in aligning the prudential regimes of offshore banks with those of domestic banks, as recommended by the 2004 ECCU FSAP.[13] In the wake of the global financial crisis, offshore financial services are under increasing pressure as regulators in advanced economies are moving to curtail their activities through more stringent regulation.[14] Revenue from offshore financial sectors is particularly important for

[12] See also A. Carvajal, H. Monroe, C. Pattillo, and B. Wynter (2009), "Ponzi Schemes in the Caribbean," IMF Working Paper 09/95.

[13] For example, St. Kitts and Nevis is moving ahead quickly with passage of its *Tax Cooperation Act*, which will allow for the exchange of information with relevant countries to prevent the evasion of taxes by their residents through the use of local offshore companies.

[14] As of April 2009, the OECD has listed all eight ECCU members as tax havens which have committed to the internationally-agreed tax standard developed by the OECD, but have not yet substantially implemented the standard. In addition, the *Stop Tax Haven Abuse Bill* is awaiting passage in the U.S. Congress, and aims

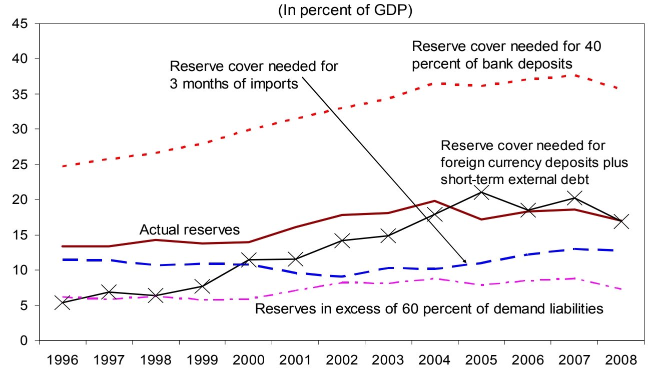
(continued)

Nevis, Anguilla, and Antigua and Barbuda. In terms of AML/CFT compliance, a new round of CFATF mutual assessment is ongoing, with the assessments for Antigua and Barbuda, St. Kitts and Nevis, St. Lucia, St. Vincent and the Grenadines completed in June 2007, September 2008, October 2008, and March 2009, respectively. Assessments for two other ECCU jurisdictions (Anguilla and Montserrat) are scheduled for 2009. The mission urged that the enforcement of AML/CFT frameworks for offshore financial services continue to be enhanced.

28. **The mission welcomed the recent establishment of a Regional Oversight Committee (ROC), comprised of the ECCB, ECSRC, and national financial regulators (SRUs).** The Committee, which meets on a monthly basis starting from 2009, provides a high-level forum for ECCU regulators to share information, discuss regulatory reforms, and coordinate responses to threats to financial stability. The mission enquired about plans for the ECCB to take the lead responsibility in supervising systemically-important near banks (credit unions and building societies) and to be closely involved in supervising offshore banks which have domestic bank affiliates, as recommended by the 2004 ECCU FSAP. The authorities indicated that regulation and supervision of nonbanks and offshore banks falls under national regulators, not the ECCB. However, the ROC will serve to enhance information exchange and cooperation among ECCB and national regulators, and close gaps in regulation and supervision of the region's financial institutions. The mission recommended that the ECCB continue to be the focal point of ensuring financial stability, taking the lead role within the ROC, and that sufficient resources be allocated to all financial regulators and supervisors.

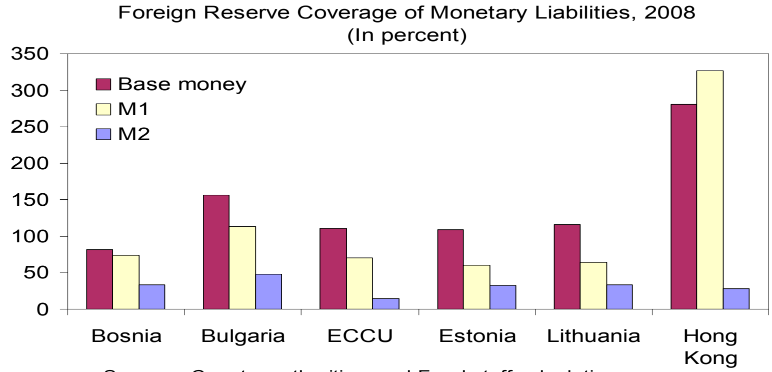
29. **Given tightened global liquidity, careful international reserve management is critical to sustain the region's currency board arrangement.** Functioning very much as a traditional currency board, the ECCB has been involved in minimal lending to member governments and banks, and has built up foreign reserve coverage over the years. Fund staff support this conservative approach, which has served the region well in maintaining exchange rate and price stability, and has limited any potential systemic impact arising from past episodes of banking stress. The ECCB agreed that an active monetary policy (including altering its limited LOLR capacity) runs the risk of undermining the region's hard-earned price and exchange rate stability (Box 4). In this context, the ECCB and commercial banks have been working on arrangements to resolve fragmentation of the interbank market (between local and foreign banks) and enhance

ECCU: Optimal Level of Reserves, 1996-2008
(In percent of GDP)



Source: Fund staff calculations.

to restrict the use of offshore tax havens and abusive tax shelters. All ECCU members except Montserrat are on the list of offshore secrecy jurisdictions in that Bill.



Sources: Country authorities; and Fund staff calculations.

interbank market efficiency. The mission enquired about plans to augment reserve coverage, as the ECCB's potential LOLR capacity is limited by the amount of reserves in excess of the minimum 60 percent requirement for backing of demand liabilities.[15] While the authorities deemed the current level of international reserves to be broadly adequate, they shared the staff's concern that reserves could be placed under pressure in an extreme scenario of large-scale bank runs and capital flight.[16] Given the need to prepare better for adverse events, the authorities agreed on the need to further explore options with multilaterals, development partners and regional central banks on the establishment of contingent lines of credit to boost reserves in any future crisis situation.

30. **Interest rate rigidities should be addressed to cope better with the current downturn.** The region has a floor rate which guarantees a minimum return of 3 percent on savings deposits held with commercial banks.[17] Staff commented that this floor represents a distortion that introduces a wedge on the cost of capital. Even though near banks (such as credit unions) are not subject to this floor, competition for deposits would make them similarly affected. The mission recommended that the floor be either removed or lowered to reduce the cost of borrowing during the current economic downturn—with a view to phasing out the floor over time. The authorities noted that the floor was instituted as a means to protect returns to small depositors, and was strongly supported by the community. They also expressed concerns about the potential adverse impact on the level of foreign reserves of removal of the deposit rate floor.

31. **The ECCB and national regulatory authorities continue to move forward with policy initiatives to deepen the region's capital markets.** Despite recent growth, both the RGSM and ECSE remain thin, illiquid, and highly segmented (Figures 14 and 15). The ECCB is keen to establish repo and secondary securities markets, but faces significant obstacles such as insufficiency of dematerialized (paperless) government securities. The ECCB's efforts thus far have focused on improving market infrastructure for securities trading and enhancing the payments and clearing system. The mission suggested formulating a medium-term market development strategy—involving the sequencing and

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[15] At end-2008, the ECCB's excess reserves (reserves exceeding the minimum requirement of backing for 60 percent of demand liabilities) amounted to about EC$850 million. Reflecting the deep monetization of the ECCU, this international reserve coverage is small relative to the banking system's private sector deposit liabilities (close to EC$11 billion).

[16] For additional details see M. Dehesa, E. Pineda, and W. Samuel (2009), "Optimal Reserves in the ECCU," IMF Working Paper 09/77.

[17] The floor was last lowered in September 2002, from 4 to 3 percent.

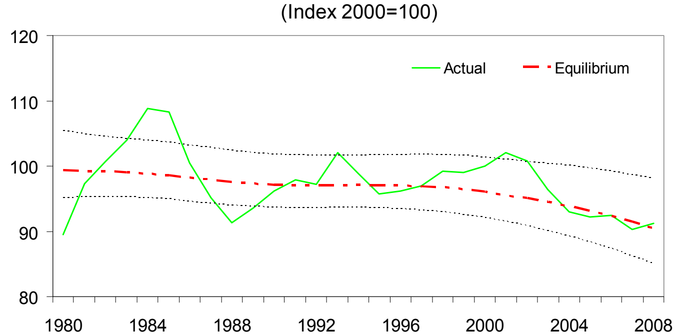
prioritization of reforms—on the basis of coordinated efforts on demand, supply, and market infrastructure. Key areas for reform include: (i) obtaining credit ratings for sovereign bonds issued by all ECCU governments, to assist in establishing pricing benchmarks and yield curves; (ii) reducing ECSE trading costs and strengthening disclosure requirements for listing on the ECSE; (iii) enhancing private credit information and markets for collateral; and (iv) simplifying the foreclosure process. The authorities noted that it would take time to deepen capital markets, especially given the lack of market makers and the predominance of a "buy and hold" mentality of investors in the region. In light of the recent liquidity crunch faced by many countries around the globe, the authorities intend to fast track the development of a repo market to enhance liquidity management in the ECCU.

B. External Stability and Competitiveness

32. **High external current account deficits remain a source of concern.** These deficits, compounded by very high public debt, render the region vulnerable to external shocks and could jeopardize the sustainability of the long-lived currency board arrangement. Key factors mitigating the concern about the sustainability of the ECCU's external position were the following:

- *FDI, a historically stable source of external flows, continues to finance the bulk of the current account deficits*. Tourism sector investment, particularly for hotel construction, remains overwhelmingly financed by FDI. Foreign borrowing (public or private) has not played and is not expected to play a major role in financing the region's current account imbalances. FDI-financed current account deficits are generally more sustainable than debt-financed deficits, and tend to adjust more gradually than deficits financed by debt or portfolio flows. As recently observed, while an adverse shift in investor sentiment may lead to a sharper than envisaged decline in foreign investment, such a decline will be reflected pari-passu in a lower current account deficit (given the high import content of construction and tourism-based activities).

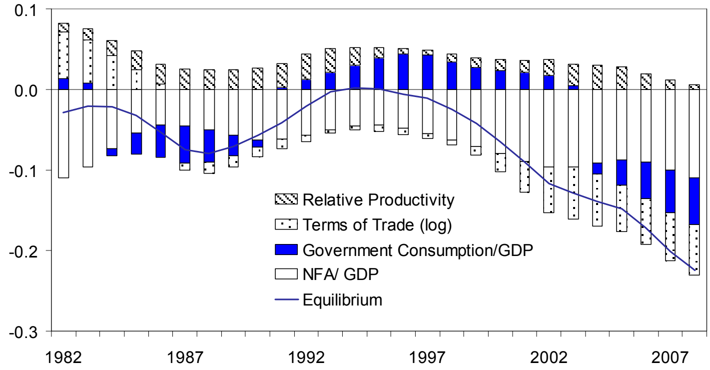
ECCU: Actual and Equilibrium REER, 1980–2008 1/
(Index 2000=100)



Sources: IMF, Information Notice System; and Fund staff estimates.
1/ The dotted lines around the equilibrium exchange rate represent 90 percent confidence intervals of the prediction.

- *The level of the real exchange rate appears appropriate*. Analysis by Fund staff suggests that the actual real exchange rate is broadly in line with its equilibrium level, reflecting the depreciation of the U.S. dollar against major currencies since 2002. Moreover, the real exchange rate (measured relative to tourism competitor-based markets) is currently at its lowest level in almost 20 years. Despite recent U.S. dollar appreciation, other measures of the real exchange rate (relative to either trade-weighted or customer-based markets) remain well below the levels seen during the 1990s and early 2000s. The equilibrium real exchange rate has also declined in recent years, reflecting the fall in the terms of trade, increased government consumption spending, and the accumulation of net foreign liabilities.[18]

ECCU: Contributions to Changes in Equilibrium Exchange Rates, 1982–2008
(In percent)

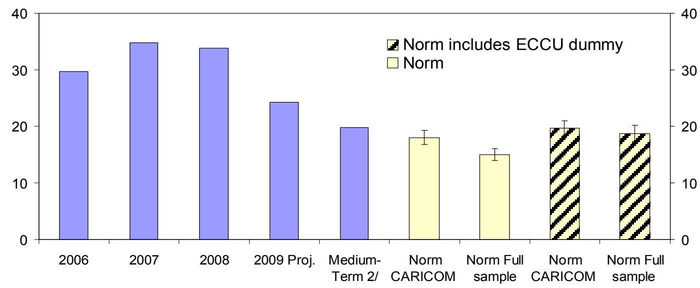


Sources: IMF, Information Notice System; and Fund staff estimates.

- *Debt sustainability analysis* indicates that the ECCU's external public debt to GDP ratio will increase moderately over the medium term (Appendix Figures 1 and 2).

33. **Medium-term current account deficits in the ECCU are broadly in line with the estimated equilibrium levels.** Using the macroeconomic balance approach, Fund staff estimates put the equilibrium current account deficit under current policies (the current account 'norm') at around 19 percent of GDP. The ECCU's projected medium-term (2014) deficit of about 20 percent of GDP is within one standard deviation of the estimated current account norm.[19] This implies that despite their numerical high levels, medium-term current account imbalances in the ECCU—largely financed by private capital flows (particularly FDI)—appear sustainable. While deficits are

ECCU: Current Account Deficit, Actual and Estimated Norms 1/
(In percent of GDP)



Source: Fund staff estimates and projections.
1/ In computing the norms, medium-term values of the fiscal balance, oil-balance, output growth, and relative income are drawn from staff projections. Band is ±1 standard error of the prediction. CARICOM sample includes ECCU countries and The Bahamas, Barbados, Belize, and Jamaica. Full sample includes 24 tourism-dependent economies as defined by Bayoumi and others (2005).
2/ Based on Fund staff estimates. Medium-term is 2014.

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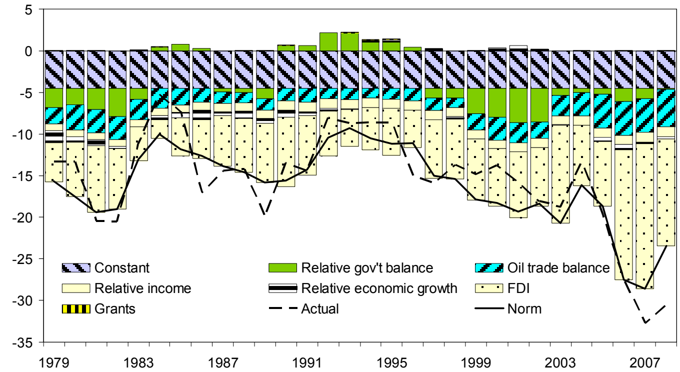
[18] Time series models linking the real effective exchange rate (REER) to measures of the ECCU region's fundamentals (productivity differentials, terms of trade, government consumption and net foreign assets) suggest that there is little evidence of overvaluation of the EC dollar. For additional details see E. Pineda, P. Cashin, and Y. Sun (2009), "Assessing Exchange Rate Competitiveness in the Eastern Caribbean Currency Union," IMF Working Paper 09/78.

[19] The panel regression (for the period 1979–2008) includes sample sets consisting of 10 CARICOM and 24 tourism-dependent countries—see E. Pineda, P. Cashin, and Y. Sun (2009).

projected to remain in excess of estimated equilibrium levels for several years, which would raise vulnerabilities, they are expected to narrow over the medium term as tourist arrivals pick up and tourism-based investment opportunities decline (implying smaller FDI flows). The authorities agreed with this assessment, noting the large import content of FDI inflows. They pointed out that high external imbalances reflect the region's gradual transition from agricultural-based to tourism-based economies, and that investment in the tourism sector is expected to improve the region's growth prospects and eventually help reduce future current account imbalances.

ECCU: Contributions to Current Account/GDP Norm, 1979-2008
(In percent)



Source: Fund staff estimates and projections.

34. **Notwithstanding the above, large external imbalances do pose risks that warrant careful monitoring.** These include:

- *Maintaining competitiveness will be key.* Since 2004 the region's share of stayover arrivals in the Caribbean has remained stagnant and the terms of trade has deteriorated by a cumulative 32 percent (Figures 16 and 17). Fiscal consolidation, critical to bolster competitiveness and assist in maintaining external stability, is to face serious tests during the current economic downturn. Moreover, given the exchange rate peg with the U.S. dollar, large movements of exchange rates among major currencies would have implications for the competitiveness of the EC dollar. Indeed, the U.S. dollar has appreciated against major currencies since August 2008.

- *Slowing capital flows in a deteriorating external environment could undermine the region's external stability*. Reflecting deleveraging, sizeable private capital flows intermediated through commercial banks in recent years are expected to retreat in 2009. This, together with slowing FDI flows (cumulatively by about 40 percent in nominal terms during 2008–09), are projected to result in a moderate loss of ECCB foreign reserves (about 1½ percent of GDP), despite a much smaller current account deficit projected for 2009. The authorities viewed FDI—the dominant source of external flows—as a sustainable and reliable source of capital flows, but shared the mission's concern that a sharp drop of capital inflows could raise pressure on foreign reserves and the exchange peg. They agreed with the need to closely monitor private sector capital flows and the ECCU's net asset position, and improve statistics in this area.[20]

[20] Data on the ECCU's overall net external asset position, and the level and structure of the stock of external assets and liabilities, are not available.

35. **The authorities stressed their commitment to maintain the currency board arrangement and the exchange rate peg with the U.S. dollar.** Noting that the EC dollar is close to its equilibrium value, they argued that the potential benefits from changing the parity were unlikely to be significant and the costs likely to be potentially substantial. Given the ECCU's high import dependence, competitiveness gains from a devaluation would be limited. In the authorities' view, the exchange rate peg has offered a strong anchor for price expectations, which have contributed to financial deepening and economic development in the region. Moreover, as public external debt is mainly denominated in U.S. dollars, a devaluation would further strain the region's already difficult debt-servicing position.

36. **In this context, structural reforms are crucial to enhance competitiveness and ensure that the recent investment boom will translate into sustainable growth.** Noting the risks posed by a slowing world economy and turbulent financial conditions, the authorities were concerned about growth prospects. Measures that could enhance competitiveness and growth potential include:

- *Improving the business climate*. Regulatory, administrative, and legal reforms are needed to help lower the cost of doing business. Indeed, most countries in the region have seen some worsening of their doing business rankings in the past few years (Figure 18). The *2008 Doing Business Indicators* identified several areas of consistent weakness, including difficulties in accessing credit and credit information; weak contract enforcement; high firing costs; and difficulties in closing businesses. The authorities indicated that the Eastern Caribbean Enterprise Fund (ECEF), an independent regional entity with a goal of capitalization of EC$100 million, is expected to be established in 2009 to provide market rate-based financing to small- and medium-sized enterprises.

- *Deepening regional integration and coordination.* Significant gains can be expected from the promulgation of the OECS Economic Union (planned for end-2009), which envisages the creation of a single economic and financial space, and strengthened cooperation in many areas to attain economies of scale. This should enhance factor, goods, and labor market flexibility in the region. Work is also ongoing to establish a regional transportation and distribution entity, to help reduce regional transportation costs. The authorities viewed regional harmonization of tax incentives as impractical, but agreed with the staff that incentives should be granted in a nondiscretionary and transparent manner based on appropriate cost-benefit analysis.

C. Fiscal Consolidation and Debt Sustainability

37. **The very high levels of public debt and debt servicing leave little room for counter-cyclical fiscal policy in the current economic downturn.** Disappointingly, regional progress in fiscal consolidation and debt reduction was limited in the recent (2003–07) economic upturn. Adverse external sector developments (particularly declines in tourist arrivals and imports) during the still-unfolding recession will lead to fiscal revenue losses. Under current policies, the region's overall fiscal position is expected to

deteriorate markedly in 2009 and to improve only moderately over the medium term; public debt would therefore rise from about 91 percent of GDP at end-2008 to about 110 percent of GDP by 2014. The staff urged the authorities to minimize fiscal slippages in the current downturn and stay on track with efforts to contain and prioritize expenditures, sustain revenue reforms, and strengthen debt management. Larger fiscal adjustment will be required in the medium term to stabilize and eventually reduce the public debt-to-GDP ratio. Any sizeable fiscal deterioration could place public sector debt back on an upward spiral, undermining the sustainability of the currency board arrangement.

38. **The authorities noted their plans to carry through with proposed revenue reforms.** Enhanced tax administration and tax reforms have led to increasing tax revenue in recent years (Figure 19). VATs have been successfully introduced in Dominica (March 2006), Antigua and Barbuda (January 2007), and St. Vincent and the Grenadines (May 2007). With CARTAC and Fund technical assistance, preparations are ongoing for introduction of VATs in Grenada (early 2010), St. Lucia (mid-2010), and St. Kitts and Nevis (late 2010). The mission stressed that, given the erosion of the corporate tax base by tax concessions, preserving the integrity of the VAT—by limiting the number of zero-rated and exempt items—is a top priority. In addition, actions need to be taken to ensure successful post-VAT implementation, including: (i) strengthening audit capability and minimizing VAT noncompliance; (ii) facilitating the absorption of VAT units into mainstream domestic tax operations; and (iii) establishing semiautonomous revenue authorities, and implementing customs reforms. Flexible fuel pricing mechanisms, which have been established in all but two (Antigua and Barbuda and St. Lucia) ECCU jurisdictions, will help preserve taxation of petroleum products and promote energy conservation (Figure 20).

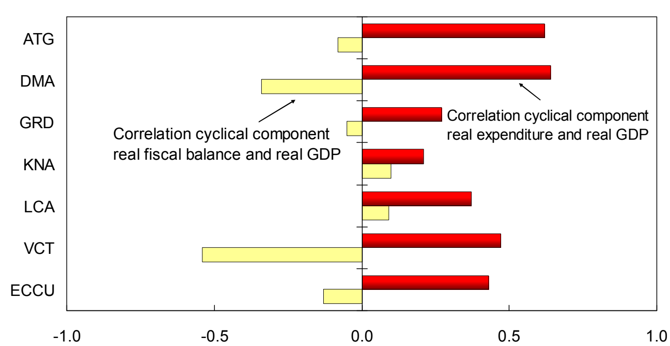
39. **Measures aimed at containing expenditures and enhancing their efficiency are critical.** Despite recent progress with revenue reforms, public expenditure remains large and inefficient (Figure 21). The staff welcomed the establishment of an OECS Public Expenditure Commission, which will follow the model of the successful OECS Tax Reform Commission, and try to forge a regional consensus on expenditure priorities and the appropriate role of government in the OECS. However, the authorities pointed to mounting social and development needs that ECCU governments are obliged to meet. The mission stressed that, with very high public debt, the governments have little fiscal leeway to maintain the role of "employer of last resort" in the current economic downturn. Instead, should fiscal revenue decline, the staff argued that ECCU governments need to be prepared to reduce expenditures, including prioritizing public investment spending and containing wage bills, to minimize fiscal slippages. Within this framework, the mission supported well-targeted social spending to mitigate the hardship caused by the economic downturn on vulnerable groups. The mission also noted that some ECCU countries have widened the coverage of social programs to ameliorate the recent effects of rising unemployment, such as the introduction of unemployment insurance in Antigua and Barbuda, higher public assistance payments in Grenada, and increases in conditional cash transfer programs in St. Lucia.

40. **The authorities saw strengthening public debt management as a priority**. They were concerned about the impact of heightened rollover risks and rising interest rates on their already difficult fiscal positions. Several ECCU countries (Antigua and Barbuda, Dominica, St. Kitts and Nevis, and St. Lucia) have received debt management technical assistance from external debt managers and/or the Fund's MCM Department, and further Fund technical assistance will be forthcoming to other ECCU countries. Enhanced debt management would allow the authorities to more closely monitor all existing public debt (including contingent liabilities of the public sector), conduct risk assessments, formulate debt strategies, and reduce debt servicing costs by retiring more expensive debt.[21]

41. **Further efforts are required to ensure the sustainability of social security systems.** Traditionally, governments in the region have used national social security funds as a captive source of financing (at below market rates of interest), which has exacerbated the impact of rapid population ageing and high emigration on the viability of the systems. As a consequence, the region's social security systems have large unfunded liabilities, which may have also been exacerbated by the systems' holdings of CIL and BAI "deposit-like" insurance products.[22] Parametric adjustments to social security schemes (e.g., increasing the retirement age and contribution rates, changing the benefits formulae), as well as greater portfolio diversification of scheme assets, are essential to ensure the long-term viability of social security systems. Staff welcomed parametric reforms already enacted in Dominica, St. Lucia, and St. Vincent and the Grenadines to bolster the sustainability of their schemes, and encouraged the authorities to address the issue of noncontributory double pensions for civil servants in several ECCU countries. The mission also noted the progress made by the OECS Social Security Commission (established by the ECCB Monetary Council in July 2008) in examining the viability of social security systems.

42. **To provide adequate discipline, the ECCB's revised fiscal benchmarks should be made operational**. In mid-2006 the ECCB Monetary Council approved revised fiscal benchmarks that require governments to achieve a public debt-to-GDP ratio of 60 percent by 2020, by integrating annual budget objectives with medium-term goals. However, there have been disappointingly few demonstrations of commitment to the revised benchmarks by ECCU member countries, with most

ECCU: Fiscal Cycles, 1983-2006



Source: J. Araujo, "Fiscal Cycles in the Caribbean", forthcoming IMF Working Paper.
Note: Antigua and Barbuda (ATG), Dominica (DMA), Grenada (GRD), St. Kitts and Nevis (KNA), St. Lucia (LCA) and St. Vincent and the Grenadines (VCT).

[21] For additional details see "A Risk Analysis of Public Debt in the ECCU: A Fan Chart Approach," by K. Nassar and C. Pattillo, Chapter V in *Eastern Caribbean Currency Union—2009 Selected Issues* (www.imf.org).

[22] See H. Monroe (2009), "Can the ECCU Afford to Grow Old?," IMF Working Paper 09/38.

countries continuing to increase their public debt (as a share of GDP). Analysis by Fund staff confirms that the region's fiscal policy is generally procyclical, with higher public expenditures during good years. In light of the ECCU's observed inability to achieve (or even move toward) the ECCB's fiscal benchmarks, staff urged the national and regional authorities to promptly establish a formal mechanism to ensure consistency between national fiscal policies and the fiscal benchmarks, in order to preserve confidence in the currency board arrangement. The mechanism should involve annual national budget targets (for the public sector overall or primary balance), placed within multiyear macroeconomic frameworks which would ensure consistency with the 2020 public debt targets. The annual budget targets should be published (to enable a comparison with actual fiscal outcomes), and allow for adverse shocks by aiming for stronger fiscal consolidation in periods of above-average growth. The mission also raised the option of enacting national Fiscal Responsibility Laws to help enforce the revised fiscal benchmarks. The authorities continued to demonstrate little appetite for an enforcement mechanism based on some system of economic penalties to assist in achieving the benchmarks. Instead, they preferred peer pressure and greater transparency of fiscal outcomes to provide credibility for the mechanism.

43. **The authorities pointed out that in the current downturn, it was necessary to strike a balance between achieving fiscal adjustment and debt sustainability, and mitigating the social pressures affecting ECCU populations with government spending.** Many of the national authorities perceived the magnitude of fiscal adjustment required to achieve the ECCB benchmarks as daunting, and neither socially nor politically feasible in their present economic circumstances. They explained that while many fiscal measures had been undertaken in ECCU countries in recent years, natural disasters, trade preference erosion, and infrastructure requirements had created social and capital spending needs that could not be deferred or curtailed (Box 5).[23] To address the debt situation, they considered that the region would need to flesh out medium-term debt strategies, seek assistance from debt advisors to conduct comprehensive reviews and management of their debt stock, as well as avail themselves of debt relief wherever possible. However, the authorities agreed with the Fund staff that fiscal adjustment must play a key role in any comprehensive debt reduction strategy.

D. Crisis Management

44. **Crisis management and preparedness are top priorities for the region.** The authorities agreed with the mission that the region's vulnerability to shocks, exacerbated by high public debt, narrow fiscal space, and the ECCB's limited role as a lender of last resort, highlights the urgency of carefully managing risks and developing national and

[23] See "Insurance Against Natural Disasters in the Caribbean," by Y. Wong, A. Lemus, and N. Wagner, Chapter VI in *Eastern Caribbean Currency Union—2009 Selected Issues* (www.imf.org).

regional contingency plans to prepare for potential future crises.[24] Main themes of these discussions were:

- Recognizing the disruptive nature of financial crises under a currency board arrangement, the authorities noted that efforts have been focused on crisis prevention and development of early warning systems. The mission encouraged the authorities to further strengthen monitoring capacity to ensure early detection and intervention, and to enhance information on macroeconomic-financial linkages.

- The ECCB has formulated contingency plans for dealing with weak and troubled banks, as evidenced by its successful leadership of the region's response to the recent run on the Bank of Antigua. The mission encouraged the authorities to expand their plans to cover banks and systemic nonbanks (such as credit unions) and to deal with systemic contingencies. The plans should be carefully communicated to the public, to help boost confidence in the financial system. Furthermore, plans should be endorsed by all ECCU members and explicitly address the issue of burden sharing (responsibilities of depositors, shareholders, national governments, and the ECCB) in the event of future financial crises.

- To ensure the sustainability of the currency board arrangement, the mission recommended focusing the ECCB's role in crisis resolution on technical assistance and moral suasion, rather than extending liquidity support to banks, nonbanks, and governments. Nevertheless, in the current environment of heightened financial risks, the mission agreed that the ECCB could continue to provide very limited LOLR support, as in the recent case of Bank of Antigua, but should establish firm limits to avoid being drawn into liquidity operations that could compromise the currency board arrangement.

- Given the difficult fiscal position of most ECCU governments, any formal guarantee of bank deposits runs the risk of being ineffective due to a lack of credibility. Moreover, given the fixed exchange rate regime, tools for containing bank runs would have to be mostly administrative in nature (e.g., early intervention of insolvent banks, deposit securitization, forced maturity extension, deposit freezes, and bank mergers). The mission also recommended that the authorities examine the efficacy of temporarily imposing capital controls in the event of large-scale capital flight.

- The burden of response to any financial sector crisis rests with national governments through the adoption of emergency fiscal and other measures. Possible fiscal responses could include a combination of expenditure cuts and deferments (including reductions in civil service wages and greater prioritization of public investment spending) and emergency revenue measures (including higher indirect taxes). Targeted social safety nets, such as use of food stamps, unemployment benefits, and public assistance payments, are needed to mitigate the hardship borne by vulnerable groups in the event of a crisis.

[24] See M. Dehesa and P. Druck (2008), "The ECCB: Challenges to an Effective Lender of Last Resort," IMF Working Paper 08/214.

E. Capacity Building

45. **Led by the ECCB, commendable progress has been made in improving the quality of economic and financial statistics and enhancing institutions.**

- A monetary ROSC was completed in 2007, and many of its recommendations have been implemented. In addition, balance of payments forms are being revised and tested to better capture trade in services (tourism), and follow the revised BPM6 methodology. The revised forms will be used for the compilation of balance of payments data, beginning in 2010. Significant progress has also been made on: rebasing the national accounts (to a common 2006 base year), to be completed by end-2009; and developing new national and regional CPI indices (based on latest household budget surveys), to be completed by end-2010. The national and regional authorities have established a data release calendar in 2009, to ensure the regular dissemination of statistical data. Work is ongoing to develop harmonized reporting by all nonbanks, including credit unions and insurance companies.

- With support from the Fund, the authorities continue to implement their initiative to establish a Regional Statistical System over the medium term. It is envisaged that the system will be established in three phases: (i) transforming Central Statistical Offices (CSOs) into statutory bodies with clearly defined functions; (ii) developing effective support to the CSOs through technical assistance and training; and finally (iii) establishing a Regional Statistical Bureau (RSB) linked to the CSOs at the national level.

46. **Further progress in capacity building is needed to improve policy analysis and design, and will require sizeable support through technical assistance.** While welcoming the progress achieved thus far, the mission noted several longstanding areas of data and institutional weakness, including: public finance and debt statistics; labor market and social indicators; public expenditure (particularly public sector investment planning); nonbank financial sector data; measures of private sector capital flows; and debt management. The mission urged the national and regional authorities to continue to work to improve statistical practices and data management, and to bolster budgetary resources devoted to these tasks. The authorities expressed their appreciation for the technical assistance provided thus far by the Fund, development partners, and particularly CARTAC (Box 6). They agreed that data and institutional deficiencies have compromised the quality of past policy analysis and design, and requested that technical assistance be continued to assist their endeavors in overcoming such deficiencies.

V. Staff Appraisal

47. **A sharply-slowing economy in the face of a hostile external environment presents major policy challenges.** Led by construction and tourism, the region enjoyed an average annual growth of about 4½ percent during 2003–07. However, the global downturn amid regional and international financial shocks in 2008 has taken a toll on economic activity, with the region expected to sink further into recession in 2009 and 2010. Key near-term risks include a deeper and more protracted global slowdown, increasing financial stress, and large retrenchment of capital inflows. To navigate through

the current economic downturn and high global volatility, the authorities need to carefully manage these risks while staying on track to address fundamental issues, particularly fiscal and debt sustainability.

48. **Safeguarding financial stability in the wake of the global crisis requires further and prompt efforts in strengthening regulation and supervision of banks and nonbanks.** The recent shocks of CL Financial Holdings and the Stanford Group highlight the urgency to bring the nonbank and offshore financial sectors under effective regulation and supervision. Credit risk, high government exposures, and liquidity risk pose major threats to the stability of the banking system. It is, therefore, crucial to intensify oversight of banks for early detection of vulnerabilities and strengthen enforcement of remedial measures. Supervision of the nonbank financial sector should also continue to be bolstered, through the planned rapid establishment of national single regulatory units in all eight ECCU jurisdictions. In addition, the increasing presence of financial conglomerates in the Caribbean underscores the need for consolidated supervision, both cross-border and cross-functional. The recent establishment of a Regional Oversight Committee, under the leadership of the ECCB, is a welcome development, which enables all ECCU financial regulators to coordinate responses to threats to financial stability.

49. **The longstanding currency board arrangement and exchange rate peg, to which the authorities remain committed, have contributed to external stability.** Staff analyses indicates that the EC dollar is close to its equilibrium level. The large ECCU current account deficit will decline over the medium term, and will continue to be largely financed by FDI. Sustained fiscal consolidation is not only fundamental to supporting external stability, but also necessary to underpin the currency board arrangement. The ECCB's approach of a nonactivist monetary policy remains appropriate, even during the current period of economic and financial difficulties. Instead, greater flexibility in interest rates should be sought to increase banks' efficiency and lower the cost of capital.

50. **Given the region's high vulnerability, crisis management and contingency planning remain top priorities.** Full-fledged contingency plans should clearly define responsibilities of relevant institutions and stakeholders—including the ECCB's limited lender-of-last-resort role—in the event of a crisis and be carefully communicated to the public. Possible fiscal responses could include a combination of expenditure cuts and postponements, and emergency revenue measures. Targeted social safety nets are needed to mitigate hardship on vulnerable groups in the event of a crisis. The authorities are also encouraged to further explore contingent financing with multilaterals and development partners, to better prepare for possible crisis scenarios.

51. **Fiscal consolidation and debt reduction should remain at the center of the region's policy agenda.** With very high public debt, there is little room for counter-cyclical fiscal policy and every effort should be made to minimize slippages during the economic downturn. Key fiscal initiatives include:

- *Revenue reforms*. The staff welcomes the progress made in revenue mobilization and encourages the remaining jurisdictions to move quickly to adopt VATs and institute more flexible mechanisms for domestic fuel pricing. The integrity of VATs needs to be preserved, by limiting exemptions and concessions.

- *Expenditure restraint*. Capital expenditures need to be better prioritized, along with implementation of civil service reform to contain the size of wage bills. These measures will create room for strengthening and focusing expenditure on social safety nets.

- *Debt management*. Ongoing efforts by the authorities to strengthen debt management capacity will be critical in seeking to enhance debt sustainability.

- *Fiscal benchmarks.* A strong and transparent link needs to be established between the setting of national fiscal policies and achievement of the ECCB's fiscal benchmarks. Such links will help strengthen fiscal discipline at the national level and boost public confidence in the sustainability of the currency board arrangement.

52. **Structural reforms need to be carried through to enhance competitiveness.** The planned OECS Economic Union provides an important opportunity to further enhance regional coordination and integration, and promote factor and product market mobility. Other priorities include improving the national and regional business climate, and increasing the flexibility of labor and product markets.

53. **Efforts to further advance the region's capacity building are well placed.** The region has made commendable progress in improving statistics on the national accounts, consumer prices, monetary aggregates, and the balance of payments, and efforts in these areas should be continued. The initiative to establish a regional statistical system is also welcome. Data deficiencies, however, continue to compromise the quality of policy analysis and design. The staff encourages the authorities to continue their efforts in capacity building—supported by technical assistance—and urges improvements in the data on the nonbank financial sector, noncentral government fiscal accounts, and debt stocks.

54. **It is proposed that the next discussion on ECCU common policies takes place in 12 months.**

Box 1. The Economic Partnership Agreement Between the Caribbean and European Union

The Economic Partnership Agreement (EPA) between the European Union (EU) and individual CARIFORUM countries (CARICOM and the Dominican Republic) was signed on October 15, 2008. This comprehensive agreement, the first between the EU and an ACP region, can yield significant benefits to participating Caribbean countries, but would require countries to improve their trade policy frameworks, including accelerating regional integration initiatives, to take advantage of the available opportunities. The EU would also need to commit to providing significant assistance to help overcome the constraints that Caribbean countries face in accessing their markets.

The EPA is a WTO plus reciprocal agreement that encompasses free trade in goods, trade in services, and provisions on Singapore issues. The trade in goods agreement envisages the immediate elimination of import duties and quotas on 98.5 percent of Caribbean goods entering the EU, while the duties of CARIFORUM countries would be reduced in phases starting in 2011, which would result in the removal of duties on 87 percent of European goods entering the Caribbean countries by 2033. Caribbean bananas are allowed immediate duty- and quota-free access to the EU market. The agreement on services proposes the liberalization of 94 percent of services sectors in the EU, while covering 65 percent of services sectors in the ECCU, 75 percent in the rest of CARICOM and 80 percent for the Dominican Republic. The agreement covers all four modes of supply of services—cross border (1 and 2), commercial presence (3), and movement of natural persons (4)—and contains potentially significant opportunities for Caribbean service providers in Europe. The agreement also includes WTO plus provisions on investment measures, government procurement, intellectual property rights, trade and customs facilitation as well as a dispute settlement mechanism.

The most significant benefits would likely come from the agreement on services. A joint study by the World Bank and OAS estimates that full implementation of the service access provisions under the EPA could result in an increase in GDP of about 2½ percent above the baseline and an increase in export supply of about 6½ percent, mainly as a result of productivity increases that would be generated by entry of European service providers in the Caribbean market. The trade agreement on the other hand is estimated to result in a marginal rise in GDP from the baseline, and an increase in export demand of about ¾ of 1 percent, particularly in vegetables, fruits, and nuts.

Estimated Benefits of the EPA for Caribbean Countries

Percentage chage from baseline	Export	GDP	Absorption	Consumption
Trade in goods (excluding sugar)	0.76	0.11	0.04	0.08
Trade in goods (including sugar)	0.81	0.15	0.18	0.27
Trade in services	6.29	2.38	4.98	6.96
Trade in goods and services	7.09	2.49	5.02	7.02

Source: World Bank and OAS, *Caribbean Accelerating Trade Integration* .

What needs to be done for the Caribbean to take advantage of the agreement? There is an urgent need to improve competitiveness in the region by reducing labor market rigidities, lowering the cost of doing business (particularly transportation costs), improving customs procedures, strengthening the legal framework, and developing a competition policy. The framework for trade policy also needs to be strengthened to make national trade policy more coherent. Accelerated implementation of many of the provisions of the revised CARICOM treaty, which have languished, like the free movement of capital, rights of establishment, and the provisions of the trade in services regime, would better equip regional firms to take advantage of opportunities under the EPA. Enhancing trade policy along with internalizing other adjustment cost could prove to be prohibitive for many Caribbean countries, particularly the ECCU, and would require significant financial assistance from the EU which could be supported under a comprehensive aid for trade package.

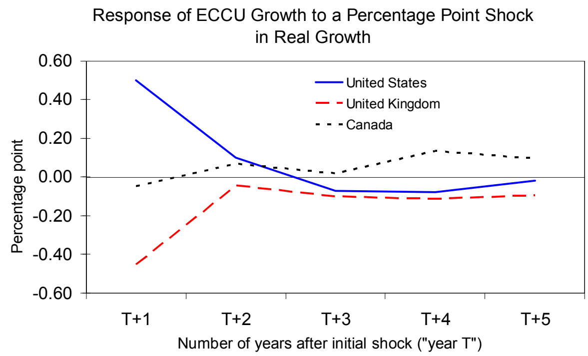
Box 2. Business Cycle Linkages between the ECCU and Major Trading Partners

Given the ECCU's currency board arrangement and its hard peg to the U.S. dollar, the vulnerability of the ECCU to external shocks remains a serious concern. The global financial crisis of 2008 has already adversely affected tourist arrivals to the ECCU, and slowed investments and remittances, thereby reducing prospective growth outcomes for the ECCU in the near term. Additional downside risks remain in view of the declining prospects for global growth in 2009, especially for the United States and Canada. As such, the dependence of the ECCU on its major trading partners remains an important issue.

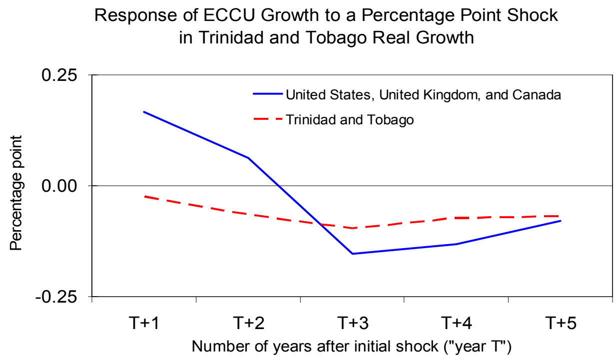
Spillovers from major trading partners to the ECCU can be estimated using the structural vector-auto regression (SVAR) methodology of Rigobon (2003).[1/] In contrast to existing SVAR approaches, this methodology estimates the size of spillovers by exploiting changes in the variability of the external shocks, a feature that is particularly ideal for the ECCU region. The estimated SVAR allows real growth in the United States, the United Kingdom, and Canada to influence the growth rate of the ECCU directly. It also constrains the ECCU to have no spillover effects on these countries, which seems sensible given that the ECCU is composed of small open economies. The model is estimated using annual real growth data for 1965–2008.

The preferred parameter estimates suggest that the United States is the main driver of ECCU growth. Specifically, after one period (year "T+1"), a 1 percentage point increase in U.S. growth increases growth in the ECCU by approximately 0.5 percentage points on average. By contrast, a similar shock to either Canadian or United Kingdom growth does not produce economically meaningful or statistically significant effects on the ECCU growth rate.

OECS member states have set themselves the goal of forming an OECS Economic Union by 2009, and Trinidad and Tobago is expected to become a member by 2011. Reformulating the SVAR to include Trinidad and Tobago and the United States, Canada and the United Kingdom as a group yields little evidence that Trinidad and Tobago is a key growth driver of the ECCU. This result probably reflects the services-oriented nature of ECCU exports and the limited consumption of these services by Trinidad and Tobago during 1965–2008.



Source: Fund staff estimates.



Source: Fund staff estimates.

[1/] Rigobon, R. (2003), "Identification through Heteroskedasticity," *Review of Economics and Statistics*, Vol. 85.

Box 3. Stress Testing the ECCU Banking System

The ECCU banking system remains well capitalized, yet local banks are burdened by persistent high government exposures and are vulnerable to credit risks. As of end-2008, locally incorporated banks' gross government exposures accounted for about one fifth of their total assets, more than triple the ratio of foreign branches. Local banks' capital adequacy ratio (CAR) stood at 20 percent, far exceeding the ECCB's 8 percent prudential requirement. However, their capital adequacy may be overstated given potential underprovisioning, as reflected in local banks' relatively low provisioning-to-NPL ratio.

ECCU: Financial Soundness Indicators, December 2008
(in percent)

	Capital Adequacy 1/	NPLs/ Total Loans 2/	Provisioning/ NPLs 2/	Gross Government Exposure/ Total Assets	Amount Outstanding by Largest Sector/Total Loans
Aggregate banking system	…	7.7	23.4	14.3	44.0
Foreign branches	…	4.5	39.2	5.4	48.7
Locally incorporated	20.1	10.2	17.9	21.1	44.2

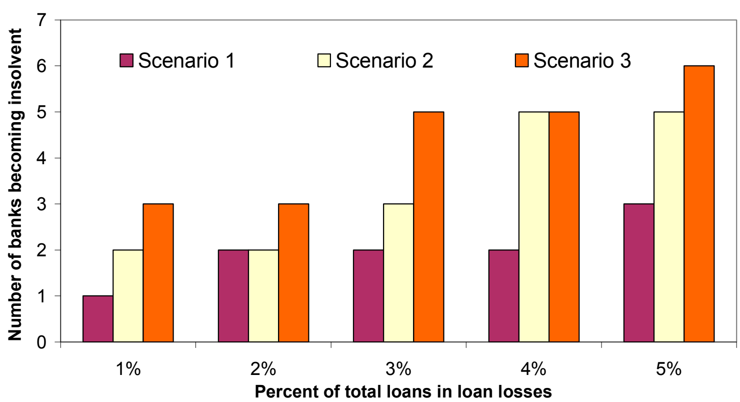
Source: ECCB.

1/ The foreign branches have consolidated capital positions with their parent banks.
2/ Non-performing loans.

Stress tests on 20 locally-incorporated banks, which have their own capital bases, reveal several major risks. Foreign branches are excluded from the stress tests as they do not have their own capital bases.

- **Credit risk and high government exposures pose the most significant challenge to the stability of the ECCU banking system.** NPLs are expected to rise in a slowing economy. Even with just a 1 percent increase of total loans in loan losses (Scenario 1), 1 of the 20 local banks would become insolvent. The number of insolvent banks rises to 3 with an additional 5 percent of total loans in loan losses. Under Scenario 2, where loan losses are compounded by a 10 percent nonrepayment in government obligations, the number of insolvent banks increases to 2 for a 1 percent rise of total loans in loan losses and 5 for a 5 percent rise of total loans in loan losses. To account for possible underprovisioning, it is further assumed that recovery rates will be lower than provisioning by 10 percent of NPLs (Scenario 3). This would lead to the insolvency of 6 local banks under the worst-case scenario.

Sensitivity Analyses, Local Banks, end-2008



Note: Scenario 1 models the impact of increased loan losses (in percent of total loans); scenario 2 adds the non-repayment of 10 percent of government exposure to scenario 1; scenario 3 incorporates the impact of underprovisioning of 10 percent of NPLs to scenario 2.

- **Liquidity risk is another major risk to banking system stability.** As of end-2008, local banks overall had net liquid assets of 34 percent of deposits, above the ECCB's 20 percent prudential requirement. However, 8 out of the 20 local banks had net liquid assets below 20 percent of deposits, with net liquid assets of two local banks being negative. With a 20 percent deposit loss, the number of local banks with net liquid assets ratios below the ECCB's prudential

Box 3. Stress Testing the ECCU Banking System (Concluded)

requirement increases to 13, 8 of which have negative net liquid assets. For the 20 local banks as a whole, the net liquid assets ratio falls by half to 17 percent. Impairment of foreign investments, which, on average, account for about 40 percent of banks' liquid assets, will also reduce local banks' liquidity and solvency. With a 50 percent loss of foreign investments, 12 banks will have net liquid asset ratios fall below the 20 percent prudential requirement, and 6 banks will become insolvent.

- **While local banks' direct foreign exchange risk is small, indirect risk could potentially be sizeable.** As of end-2008, all but two local banks had net positive open positions in foreign exchange, suggesting that most local banks would benefit from a potential EC dollar devaluation. However, a devaluation could affect banks' balance sheets indirectly through its impact on borrowers' capacity to service loans. About half of the region's public debt is external debt (mostly denominated in U.S. dollars). A large devaluation could hurt the public sector's capacity to repay, with knock-on effects to local banks which have large government exposures. Moreover, ECCU banks offer foreign currency loans to residents. To the extent that those residents cannot repay the foreign currency loans in the event of a devaluation, banks are exposed indirectly to foreign exchange risk. As information on borrowers' net open positions in foreign exchange is hard to come by, a close look is taken at the composition of foreign currency loans versus deposits in ECCU banks. For the banking system as a whole, foreign currency loans and deposits roughly match each other. Nevertheless, as of end-2008, private business' foreign currency deposits were less than half of their foreign currency loans, suggesting that potential foreign exchange risk faced by private business may indirectly affect ECCU banks.

Foreign Currency Deposits and Loans of Residents in the ECCU Banks 1/
(In millions of EC$)

	Dec-07	Jun-08	Dec-08
Public sector			
Foreign currency deposits	431.9	496.9	510.2
Foreign currency loans	126.9	109.8	109.3
Private business			
Foreign currency deposits	1,001.8	859.5	813.3
Foreign currency loans	1,577.1	1,667.3	1,754.1
Households			
Foreign currency deposits	927.7	988.8	962.4
Foreign currency loans	474.5	536.7	567.7
Nonbank financial institutions			
Foreign currency deposits	62.7	46.2	49.1
Foreign currency loans	4.1	3.7	1.9
Subsidiaries & Affiliates			
Foreign currency deposits	80.2	61.6	89.4
Foreign currency loans	5.5	24.1	4.9
Total			
Foreign currency deposits	2,504.4	2,452.9	2,424.5
Foreign currency loans	2,188.0	2,341.7	2,437.8
Memorandum items (in percent):			
Foreign currency deposits/total deposits	17.6	17.1	16.8
Foreign currency loans/total loans	17.6	17.9	17.6

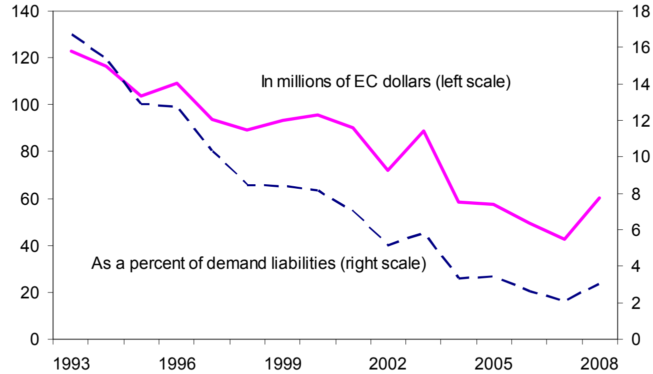
Sources: ECCB, and Fund staff estimates.
1/ Including both foreign and local banks.

- **The risk of pure interbank contagion is found to be limited**, reflecting the limited interbank market among local banks. However, there could be indirect effects should an individual bank's insolvency lead to a loss of confidence in the banking system.

Box 4. The ECCB's Monetary Instruments and Facilities

The ECCB Act (1983) stipulates that the EC dollar is pegged at EC$2.70 to US$1 and requires the ECCB to hold external reserves for its members of no less than 60 percent of its demand liabilities. However, the policy norm for the minimum reserve cover is 80 percent and has been maintained at about 100 percent in recent years. The ECCB is permitted to provide credit to its members under strictly specified limits and within the reserve cover requirements. At the beginning of its fiscal year, the ECCB allocates its global limit on domestic assets, currently 20 percent of demand liabilities, to credit to commercial banks and the participating governments (40 percent and 60 percent of the fiduciary issue, respectively) with each government having its own limit.

ECCB: Lending to Governments, 1993–2008



Source: ECCB.

The ECCB's monetary instruments and facilities are:

- **Reserve requirement.** Set at 6 percent on all deposits. Reserves are unremunerated, in local currency and are based on the average level of deposits for the week.

- **Rediscount facility for treasury bills.** The ECCB may sell to banks treasury bills it has purchased in the primary market and which can be rediscounted before their maturity date. However, the ECCB no longer sells treasury bills to banks, as this facility is being phased out. Instead, banks are encouraged to utilize the RGSM secondary market.

- **Discount rate.** This is the applicable rate at the discount window, but the ECCB has used it more to signal its views about interest rate movements. This was lowered in July 2003 to 6.5 percent.

- **The minimum savings deposit rate.** This is the only remaining interest rate control imposed by the ECCB under its general power to establish a schedule of interest rates and credit limits. It was lowered in September 2002 from 4 percent to 3 percent.

- **Lombard facility (discount window).** The ECCB may provide emergency liquidity assistance to a bank that is in distress, once the bank has exhausted other liquidity sources, for up to 90 percent of the face value of treasury bills or other securities. This facility has been used very rarely.

As in the case of Bank of Antigua, the ECCB can also exercise **special emergency powers** based on its judgment that a financial institution is in serious stress. The operation of these instruments is reviewed regularly by the ECCB's Monetary Council.

Box 5. Trade Preference Erosion and Donor Assistance

The continued erosion of trade preferences for ECCU exports to European markets, compounded by the decline in development assistance, has adversely affected the region's rural populations. Going forward, increased international competition is expected to lead to further contraction of the traditional banana sector. There is a need to continue to develop targeted social safety nets for displaced farmers and agricultural workers, involving time-bound measures such as income transfers and retraining programs, and to diversify agricultural production to meet local demand from the tourism sector.[1/]

Fund technical assistance reviewed the impact of preference erosion on poverty in the Windward Islands, through a FAD Poverty and Social Impact Analysis completed in early 2009. A major finding is that social programs in ECCU countries have evolved over time in a piecemeal fashion, which is both expensive and inefficient in targeting the needs of the most vulnerable. The mission urged the national fiscal authorities to sharpen the focus and coherence of poverty reduction initiatives, to ensure they are linked to social development programs in national budgets, consistent with overall macroeconomic and fiscal objectives.

ECCU countries continue to be frustrated with the slow disbursal of pledged assistance by traditional development partners. The authorities were particularly concerned about the EU's nondisbursal of previously committed development funds, aimed at mitigating the adverse impact of trade preference erosion and facilitating the transition out of agriculture. The mission encouraged the authorities to continue to work closely with the EU to quickly release undisbursed financial assistance (particularly from SFA sources). In a welcome development, the EU has recently disbursed long-awaited sugar transformation funds to St. Kitts and Nevis (receiving the first of two installments in December 2008), and continues to disburse from its European Development Fund (EDF) resources, with St. Kitts and Nevis, Antigua and Barbuda, St. Lucia, Dominica, and Grenada receiving grants in 2008.[2/]

ECCU: Status of EU Banana Support (Special Framework of Assistance), End-2008

	Dominica			Grenada			St. Lucia			St. Vincent and the Grens.		
	Amount Committed	Amount Disbursed	Percent Disbursed	Amount Committed	Amount Disbursed	Percent Disbursed	Amount Committed	Amount Disbursed	Percent Disbursed	Amount Committed	Amount Disbursed	Percent Disbursed
	(In € million)			(In € million)			(In € million)			(In € million)		
1999	6.5	6.0	92.7	1.0	0.9	93.3	8.5	7.4	86.8	6.1	5.4	88.0
2000	6.5	0.4	5.9	0.5	0.5	99.4	8.9	7.3	82.8	6.5	4.6	71.5
2001	6.7	6.1	91.4	0.5	0.5	99.4	9.2	6.0	65.4	6.4	3.6	56.2
2002	6.4	2.0	31.0	0.5	0.0	3.1	8.8	2.3	26.3	6.1	1.4	23.6
2003	5.9	2.2	38.0	0.5	0.4	73.5	8.0	3.2	40.0	5.9	1.9	31.5
2004	5.3	2.9	53.8	0.5	0.3	65.3	7.4	2.2	29.5	6.0	1.7	28.0
2005	4.5	1.4	31.7	0.5	0.2	44.5	6.2	0.0	0.0	4.5	0.9	20.2
2006	3.8	0.5	12.6	0.5	0.2	44.0	5.4	0.9	15.9	3.9	0.7	16.9
2007	3.3	0.0	0.0	0.5	0.0	0.0	4.6	0.0	0.0	3.3	0.0	0.0
2008	3.6	0.0	0.0	0.5	0.0	0.0	4.8	0.0	0.0	3.5	0.0	0.0
Total	**52.5**	**21.5**	**41.0**	**5.5**	**3.1**	**56.0**	**71.7**	**29.3**	**40.8**	**52.0**	**20.1**	**38.6**

Source: Delegation of the European Commission, Barbados.

[1/] Donors (principally the European Union (EU) and Caribbean Development Bank (CDB)) have offered assistance to facilitate the social and economic transformation of the ECCU economies away from (banana and sugar) agriculture, under the Special Framework of Assistance (SFA), designed for the period 1999-2008. See also M. Mlachila, P. Cashin and J. Gold, "The Macroeconomic Impact of Trade Preference Erosion on the Caribbean," Chapter III of *The Caribbean: Enhancing Economic Integration,* Bauer, Cashin, and Panth (eds.), IMF 2008.

[2/] The CDB also extended policy-based loans to St. Kitts and Nevis and St. Lucia in 2007 and 2008, respectively.

Box 6. ECCU: Technical Assistance from the Fund in 2008 and 2009

The ECCU has been an intensive user of CARTAC (backstopped by the Fund) and Fund technical assistance (TA). The following major support has been provided or envisioned in 2008–09:

Tax and customs reform: Follow-up assistance in St. Vincent and the Grenadines, Antigua and Barbuda, and Dominica to strengthen value-added tax (VAT) implementation and improve the organization and operations of tax and custom administration (FAD, CARTAC). Assistance with near-term implementation of VAT in St. Lucia, St. Kitts and Nevis, and Grenada (CARTAC, FAD, LEG). Assistance with custom reforms in Grenada, St. Vincent and the Grenadines, and St. Lucia (CARTAC). Revenue administration assessments for St. Kitts and Nevis, and St. Vincent and the Grenadines; and revenue administration follow-up assistance to Dominica (CARTAC).

Public debt management: Assistance to strengthen debt management capacity and develop medium-term debt strategy has been provided to St. Lucia and St. Kitts and Nevis in 2008, and will be extended to Dominica in the first half of 2009 (MCM).

Public finance management: Advanced internal audit training conducted for St. Vincent and the Grenadines and Grenada; revenue modeling and forecast training conducted for St. Vincent and the Grenadines, Grenada, and Montserrat; and pension reviews conducted for Montserrat, and St. Kitts and Nevis (all CARTAC).

Regional financial and capital market: Assistance to facilitate the establishment of an overnight repo facility and the functioning of the interbank market; payments and settlements (both MCM); assistance for review and preparation of new securities regulations (CARTAC).

Financial sector supervision: Assistance (since April 2008) to ECCU member countries in the development of Single Regulatory Units (SRUs) based on the specific needs of each SRU; revision of insurance laws and designing of regulatory insurance reporting forms; development of law, changes in legal framework, and training for the supervision of credit unions; development of credit bureaus in the region; and launching of a financial literary web site (all CARTAC).

Preference erosion: A Poverty and Social Impact Analysis (PSIA) of banana-exporting ECCU countries was completed in early 2009, to identify the most vulnerable groups and assist in the design of a transition strategy (FAD).

Economic and financial statistics: Ongoing assistance in compiling supply and use tables in all ECCU countries; rebasing consumer price index and national accounts (all CARTAC); assistance in the development of tourism satellite accounts (CARTAC; CARICOM Secretariat; CDB; and OECS Secretariat); and assistance in the development of a regional statistics network (STA).

Balance of payments statistics: Ongoing assistance in revising forms for compiling external sector statistics, in particular to implement the Balance of Payments and Investment Position Manual (BPM6) in 2009 (CARTAC; OECS Secretariat; STA).

Other capacity building: Completed a Regional IT Study in areas of tax, customs, treasury, expenditure and budget at the request of CIDA (CARTAC); regional training courses on IT accounting system, unregulated investment schemes, and the CARICOM Tax Treaty; a regional workshop on tax administration IT applications and systems to address the Caribbean region's medium-term needs (CARTAC, ECCB, and CARICOM); continued work in the establishment of a regional customs (ASYCUDA IT-based) service center in St. Lucia (CARTAC, and CARICOM); and review of revenue administration and public expenditure IT system (CIDA, CARTAC).

Table 1. ECCU: Selected Economic and Financial Indicators, 2004–10 1/

					Prel.	Proj.	
	2004	2005	2006	2007	2008	2009	2010
	(Annual percentage change)						
National income and prices							
Real GDP	3.9	5.6	6.3	5.2	1.8	-2.4	-0.1
GDP deflator	2.4	3.3	2.7	3.5	5.1	3.4	2.7
Consumer prices, average	2.2	3.2	4.0	3.3	6.9	3.1	2.7
Monetary sector							
Liabilities to the private sector (M2)	13.2	8.4	11.6	9.7	3.0	-1.0	2.1
	(Annual change, in percent of M2 at the beginning of the year)						
Net foreign assets	6.8	1.2	2.0	-1.5	-7.0	-2.7	-1.3
Net domestic assets	6.4	7.2	9.6	11.2	9.9	1.6	3.4
Of which							
Private sector credit	5.1	9.2	14.6	17.3	10.2	1.0	3.4
Credit to central government	-1.0	2.0	-0.2	2.3	1.4	0.2	0.0
	(In percent of GDP)						
Public sector							
Primary central government balance	0.1	-0.5	-1.1	-0.8	-0.7	-2.2	-2.2
Overall central government balance	-4.3	-4.4	-5.1	-4.4	-4.7	-6.8	-6.9
Total revenue and grants	29.0	29.9	31.3	30.7	31.0	28.9	29.0
Total expenditure and net lending	33.3	34.3	36.4	35.1	35.6	35.7	35.9
Foreign financing	3.1	-2.9	2.0	0.7	0.7	1.0	0.7
Domestic financing including arrears	1.7	4.5	6.1	3.5	3.6	5.8	6.2
Central government current account balance	-0.3	0.7	1.4	2.5	1.3	-1.6	-0.8
Total public debt (end-of-period)	107.3	100.5	98.4	94.5	90.6	97.9	103.8
	(Annual percentage change)						
External sector							
Exports, f.o.b.	11.6	8.0	-2.5	4.8	12.9	-8.6	-0.1
Imports, f.o.b.	5.5	18.0	17.0	13.3	4.3	-25.6	3.8
Stayover visitors	10.0	1.3	2.8	-1.8	-1.3	-11.6	1.4
Nominal effective exchange rate 2/							
(1990 =100) end-of-period (depreciation -)	-2.7	-0.4	0.1	-2.0	-1.0	...	...
Real effective exchange rate 2/							
(1990 =100) end-of-period (depreciation -)	-3.6	-0.9	-0.1	-2.3	1.1	...	...
Terms of trade 2/	-4.4	-2.8	-9.7	-1.5	-14.0	...	...
	(In percent of GDP)						
External current account balance	-16.4	-22.4	-29.7	-34.8	-33.9	-24.2	-24.1
Trade balance	-36.5	-40.2	-44.6	-47.1	-45.3	-31.8	-32.4
Services, incomes and transfers	20.1	17.9	14.9	12.2	11.4	7.6	8.3
Of which							
Travel	28.4	26.7	24.4	22.8	20.7	17.3	17.8
Capital and financial accounts 3/	19.5	21.9	31.9	35.9	33.5	22.4	23.6
Of which							
Foreign direct investment	13.6	17.3	26.3	27.7	22.6	16.3	17.8
External public debt (end-of period)	62.1	53.9	50.9	47.4	46.0	50.1	53.3
External debt service, in percent of goods and nonfactor services	11.5	15.4	8.1	10.7	9.1	12.1	10.9
Of which							
Interest	4.8	4.0	4.3	4.4	4.5	5.9	5.8
End-year gross foreign reserves of the ECCB							
In millions of U.S. dollars	632.4	600.8	696.0	764.5	759.0	687.4	660.8
In months of imports	4.8	3.9	3.8	3.7	3.5	4.3	4.0
In percent of broad money	20.4	17.9	18.6	18.6	17.9	16.4	15.5
Currency backing ratio, in percent 4/	96.2	96.5	98.7	100.1	102.0	...	...

Sources: Country authorities; and Fund staff estimates and projections.

1/ Includes all eight ECCU members unless otherwise noted. ECCU price aggregates are calculated as weighted averages of individual country data. Other ECCU aggregates are calculated as sum of individual country data; ratios to GDP are then calculated by dividing this sum by the aggregated GDP.

2/ Excludes Anguilla and Montserrat.

3/ Includes errors and omissions.

4/ ECCB's foreign assets as a ratio of its demand liabilities.

Table 2. ECCU: Selected Economic Indicators by Country, 2004–14

					Prel.	Proj.					
	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014
					(Annual percentage change)						
Real GDP	**3.9**	**5.6**	**6.3**	**5.2**	**1.8**	**-2.4**	**-0.1**	**2.2**	**3.5**	**3.9**	**4.1**
Anguilla	16.4	10.7	18.3	21.0	-0.5	-6.1	-3.2	0.0	3.0	4.0	5.0
Antigua and Barbuda	5.2	5.5	12.4	6.9	2.8	-4.9	-1.1	2.1	3.8	4.8	4.8
Dominica	3.0	3.3	4.0	1.5	2.6	1.1	2.0	3.0	3.0	3.0	3.0
Grenada	-5.7	11.0	-2.3	4.5	0.3	-0.7	1.0	2.9	3.4	3.6	3.9
Montserrat	4.5	-0.3	-3.8	2.8	6.2	3.0	2.5	2.0	2.0	2.0	2.0
St. Kitts and Nevis	7.3	5.2	2.5	2.9	3.2	-1.2	0.0	1.0	2.0	2.0	2.0
St. Lucia	3.8	4.4	4.9	1.7	1.7	-2.5	-0.4	1.8	3.6	4.2	4.2
St. Vincent and the Grenadines	6.8	2.6	7.6	7.0	0.9	0.1	1.2	3.8	4.3	3.9	4.1
CPI (end of period)	**2.6**	**4.2**	**2.8**	**5.7**	**5.0**	**2.4**	**2.3**	**2.6**	**2.5**	**2.3**	**2.3**
Anguilla	5.1	3.2	10.6	3.5	5.9	2.5	2.5	2.5	2.5	2.5	2.5
Antigua and Barbuda	2.8	2.5	0.0	5.2	2.3	0.7	2.5	3.4	3.0	2.5	2.5
Dominica	0.8	2.7	1.8	6.0	6.7	3.5	1.5	1.5	1.5	1.5	1.5
Grenada	2.5	6.2	1.7	7.4	5.2	2.1	2.2	2.4	2.2	2.1	2.0
Montserrat	4.0	2.9	1.0	1.2	4.5	2.5	2.0	2.0	2.0	2.0	2.0
St. Kitts and Nevis	1.7	6.0	7.9	2.1	7.6	3.5	2.2	2.2	2.2	2.2	2.2
St. Lucia	3.4	4.5	1.4	6.6	3.8	3.1	2.2	2.2	2.2	2.2	2.2
St. Vincent and the Grenadines	1.7	3.9	4.8	8.3	8.7	2.9	2.9	2.9	2.9	2.9	2.9
CPI (period average)	**2.2**	**3.2**	**4.0**	**3.3**	**6.9**	**3.1**	**2.7**	**2.6**	**2.5**	**2.3**	**2.3**
Anguilla	4.4	4.6	8.4	5.2	4.7	4.1	2.5	2.5	2.5	2.5	2.5
Antigua and Barbuda	2.0	2.1	1.8	1.4	5.6	2.4	2.5	3.4	3.0	2.5	2.5
Dominica	2.4	1.6	2.6	3.2	6.9	4.8	2.5	1.5	1.5	1.5	1.5
Grenada	2.3	3.5	4.2	3.9	8.0	2.3	2.9	2.6	2.4	2.3	2.0
Montserrat	3.1	2.7	1.9	2.7	4.9	3.5	2.3	2.0	2.0	2.0	2.0
St. Kitts and Nevis	2.2	3.4	8.5	4.5	5.4	4.2	2.8	2.2	2.2	2.2	2.2
St. Lucia	1.2	3.9	4.1	2.2	7.2	2.2	2.8	2.2	2.2	2.2	2.2
St. Vincent and the Grenadines	3.0	3.7	3.0	6.9	10.1	4.2	2.9	2.9	2.9	2.9	2.9
Private sector credit	**6.1**	**11.7**	**18.0**	**20.1**	**10.8**	**1.0**	**3.3**	**5.3**	**6.3**	**6.6**	**6.8**
Anguilla	9.2	20.6	18.5	36.9	19.0	-2.3	-0.8	2.5	5.6	6.6	7.6
Antigua and Barbuda	1.1	10.4	20.4	13.9	8.0	-0.1	3.9	7.6	8.8	8.3	8.1
Dominica	7.1	6.0	11.2	5.2	8.4	4.6	3.7	4.5	4.5	4.5	4.5
Grenada	6.8	9.2	12.5	15.1	10.9	3.0	6.6	5.8	6.0	6.0	6.1
Montserrat	3.3	18.4	15.4	22.8	15.9	9.9	4.6	4.0	4.0	4.0	4.0
St. Kitts and Nevis	8.9	7.5	11.8	13.3	13.5	4.8	7.2	3.3	4.2	4.3	4.3
St. Lucia	10.2	16.2	24.5	29.5	11.6	-10.4	1.8	4.2	5.5	6.7	4.6
St. Vincent and the Grenadines	0.9	5.5	14.3	15.0	3.0	1.4	1.9	2.7	6.8	4.7	4.0
					(Percentage growth compared to M2 at the beginning of the year)						
Net credit to public sector	**0.0**	**2.5**	**-1.5**	**0.8**	**1.4**	**0.2**	**0.0**	**-0.1**	**0.1**	**0.5**	**0.5**
Anguilla	1.8	0.7	-4.5	-0.4	2.2	2.1	2.0	1.0	2.2	1.7	1.8
Antigua and Barbuda	-1.1	-1.2	-5.2	-5.7	5.1	-1.8	-1.4	-1.8	-1.7	-0.7	-0.6
Dominica	-5.1	-1.2	-9.9	-7.0	-0.9	-0.6	-0.4	-0.5	-0.5	-0.5	-0.5
Grenada	-6.8	-0.9	-0.3	1.6	1.0	2.6	0.0	0.0	0.7	0.0	0.0
Montserrat	-7.3	8.2	3.1	2.4	4.5	7.7	0.8	0.5	-0.4	1.3	3.3
St. Kitts and Nevis	18.3	9.2	6.4	0.1	-1.9	-0.9	-2.4	-2.6	-2.7	-2.5	0.0
St. Lucia	-2.5	3.2	3.1	-20.8	25.5	0.3	-1.4	-1.0	0.0	0.6	0.1
St. Vincent and the Grenadines	2.7	7.6	0.1	2.8	2.4	5.0	4.4	6.7	2.6	3.3	3.8

Sources: Country authorities; and Fund staff estimates.

Table 3. ECCU: Selected Central Government Fiscal Indicators by Country, 2004–14 1/

(In percent of GDP)

	2004	2005	2006	2007	Prel. 2008	Proj. 2009	2010	2011	2012	2013	2014
Total revenues and grants	**29.0**	**29.9**	**31.3**	**30.7**	**31.0**	**28.9**	**29.0**	**28.9**	**29.1**	**29.1**	**29.0**
Anguilla	29.6	28.6	33.3	29.2	27.5	23.1	24.1	26.0	26.6	27.6	27.6
Antigua and Barbuda	21.6	21.8	25.1	24.3	24.0	23.2	22.8	22.8	22.8	22.8	22.8
Dominica	38.8	39.0	43.2	45.0	40.6	38.7	38.1	37.7	37.7	37.7	37.7
Grenada	30.8	34.5	33.6	27.2	31.3	26.7	28.2	28.4	28.3	28.1	27.9
Montserrat	112.8	73.9	81.0	89.6	87.4	83.7	79.3	77.4	78.6	76.7	74.9
St. Kitts and Nevis	34.3	39.4	39.4	39.5	38.9	36.6	35.8	33.0	33.5	33.5	33.4
St. Lucia	25.5	25.6	26.9	28.2	29.3	27.4	27.6	28.3	29.4	29.6	29.6
St. Vincent and the Grenadines	29.5	29.3	30.1	30.9	32.4	29.8	29.9	29.8	29.9	29.9	29.9
Current expenditure	**26.7**	**25.7**	**26.2**	**25.8**	**26.6**	**27.9**	**27.8**	**27.1**	**27.3**	**27.2**	**27.4**
Anguilla	23.3	23.1	24.7	23.3	26.6	27.3	27.9	26.3	26.4	26.0	26.0
Antigua and Barbuda	25.2	24.7	26.0	24.2	24.1	28.9	29.2	28.2	28.2	28.0	28.2
Dominica	29.5	28.9	28.8	30.1	28.1	28.2	28.1	27.9	27.9	27.7	27.6
Grenada	26.0	20.3	21.2	21.7	24.5	22.7	21.4	21.1	21.2	20.6	20.7
Montserrat	81.4	67.8	69.3	74.8	71.1	72.3	72.3	72.4	72.5	72.5	72.6
St. Kitts and Nevis	34.9	36.8	36.5	36.0	36.3	38.4	38.3	35.0	37.0	38.2	39.1
St. Lucia	21.7	21.3	21.7	22.2	22.8	23.1	23.3	23.4	23.4	23.4	23.5
St. Vincent and the Grenadines	25.9	27.1	26.4	25.6	26.6	26.2	26.5	26.5	26.7	26.8	26.9
Capital expenditure and net lending	**6.7**	**8.6**	**10.3**	**9.3**	**9.1**	**7.8**	**8.0**	**8.0**	**8.2**	**8.2**	**8.3**
Anguilla	10.4	8.9	7.3	8.1	4.7	4.0	4.0	4.5	5.0	5.0	5.0
Antigua and Barbuda	2.5	4.0	7.9	6.4	7.6	5.5	5.5	5.5	5.5	5.5	5.5
Dominica	8.3	9.0	9.9	14.3	10.5	9.5	8.8	8.3	8.2	8.2	8.2
Grenada	7.4	13.8	18.8	13.6	12.5	8.6	9.6	8.2	8.2	8.2	8.2
Montserrat	29.8	21.8	15.4	21.3	26.1	22.6	12.6	9.4	9.4	9.4	9.4
St. Kitts and Nevis	7.2	6.7	7.9	8.2	6.1	6.4	6.8	7.9	7.9	7.9	7.9
St. Lucia	7.4	10.3	11.0	8.7	11.0	10.5	11.3	12.0	13.0	13.0	13.5
St. Vincent and the Grenadines	7.1	8.0	7.5	8.9	7.5	7.5	7.5	7.5	7.5	7.5	7.6
Saving (current revenue less current expenditure)	**-0.3**	**0.7**	**1.4**	**2.5**	**1.3**	**-1.6**	**-0.8**	**0.0**	**0.1**	**0.2**	**0.0**
Anguilla	5.8	4.6	6.1	5.5	-0.3	-4.7	-3.8	-0.3	0.2	1.6	1.6
Antigua and Barbuda	-3.9	-3.8	-3.8	-0.8	-1.5	-7.5	-6.4	-5.4	-5.3	-5.1	-5.4
Dominica	1.6	2.8	5.9	2.2	3.1	2.4	2.8	3.0	3.0	3.1	3.2
Grenada	-2.2	3.8	3.7	4.4	2.4	1.5	3.8	4.5	4.5	5.0	4.9
Montserrat	-52.1	-38.0	-40.8	-46.1	-41.5	-42.8	-42.7	-42.8	-42.9	-42.9	-43.0
St. Kitts and Nevis	-1.0	-0.1	0.2	1.4	0.5	-3.5	-2.8	-2.4	-3.8	-5.1	-6.0
St. Lucia	3.8	4.0	4.9	5.9	5.2	4.0	4.0	4.6	5.7	5.9	5.8
St. Vincent and the Grenadines	2.8	0.7	2.8	3.6	3.3	1.8	1.6	1.6	1.7	1.6	1.5
Primary balance	**0.1**	**-0.5**	**-1.1**	**-0.8**	**-0.7**	**-2.2**	**-2.2**	**-1.5**	**-1.4**	**-1.3**	**-1.4**
Anguilla	-3.3	-2.4	2.4	-1.2	-2.8	-6.4	-5.4	-2.0	-1.9	-0.4	-0.4
Antigua and Barbuda	-1.2	-2.3	-4.0	-2.8	-3.2	-6.0	-6.4	-5.5	-5.5	-5.5	-5.5
Dominica	4.7	6.3	5.9	4.6	2.4	2.9	3.0	3.0	3.0	3.0	3.0
Grenada	3.4	2.4	-4.3	-5.8	-3.2	-1.6	0.0	2.0	2.1	2.3	2.3
Montserrat	2.0	-14.8	-2.7	-5.7	-8.7	-9.9	-4.3	-3.0	-1.8	-3.7	-5.6
St. Kitts and Nevis	-0.8	4.0	4.7	3.7	5.3	2.4	0.9	1.3	1.7	1.6	1.5
St. Lucia	-0.6	-3.0	-2.6	0.8	-0.6	-2.0	-2.4	-2.4	-2.2	-1.9	-2.4
St. Vincent and the Grenadines	-1.1	-2.9	-0.7	-0.6	1.2	-0.9	-0.8	-0.9	-0.8	-0.8	-0.9
Overall balance	**-4.3**	**-4.4**	**-5.1**	**-4.4**	**-4.7**	**-6.8**	**-6.9**	**-6.3**	**-6.4**	**-6.4**	**-6.7**
Anguilla	-4.1	-3.4	1.3	-2.1	-3.8	-8.2	-7.8	-4.8	-4.8	-3.4	-3.4
Antigua and Barbuda	-6.1	-6.9	-8.7	-6.4	-7.7	-11.2	-11.9	-10.9	-10.8	-10.6	-10.9
Dominica	-0.8	1.2	3.7	2.2	0.5	1.0	1.3	1.5	1.6	1.8	1.9
Grenada	-2.6	0.4	-6.4	-8.2	-5.7	-4.6	-2.9	-0.9	-1.1	-0.7	-1.0
Montserrat	1.6	-15.6	-3.7	-6.4	-9.7	-11.3	-5.6	-4.4	-3.3	-5.2	-7.1
St. Kitts and Nevis	-7.9	-4.0	-5.0	-4.8	-3.5	-8.2	-9.3	-9.9	-11.3	-12.6	-13.6
St. Lucia	-3.6	-6.0	-5.9	-2.7	-4.6	-6.2	-7.0	-7.1	-7.0	-6.8	-7.4
St. Vincent and the Grenadines	-3.6	-5.9	-3.9	-3.6	-1.7	-3.8	-4.0	-4.3	-4.2	-4.3	-4.5

Sources: Country authorities; and Fund staff estimates.

1/ Fiscal years for Dominica and St. Lucia.

Table 4. ECCU: Selected Public Sector Debt Indicators by Country, 2004–14 1/

	2004	2005	2006	2007	Prel. 2008	Proj. 2009	2010	2011	2012	2013	2014
				(In percent of GDP)							
Total public sector debt	**107.3**	**100.5**	**98.4**	**94.5**	**90.6**	**97.9**	**103.8**	**106.8**	**108.4**	**109.3**	**110.3**
Anguilla	22.4	24.0	19.4	18.5	21.6	30.8	38.9	42.7	45.3	45.9	46.2
Antigua and Barbuda 2/	135.0	110.6	106.3	102.7	92.7	108.0	120.5	128.5	134.0	137.0	139.6
Dominica	107.8	100.6	99.1	89.5	81.8	78.0	74.3	70.3	66.4	62.5	58.8
Grenada	120.5	110.3	116.7	111.5	108.6	109.1	108.5	104.3	100.4	95.2	90.4
Montserrat	11.9	10.9	9.9	9.0	17.7	27.8	31.9	34.9	36.6	40.1	45.5
St. Kitts and Nevis	194.4	196.8	188.7	181.7	177.6	186.1	192.1	196.1	200.2	206.5	213.2
St. Lucia	64.4	66.0	65.6	69.3	70.1	75.6	80.4	84.1	86.3	87.8	89.9
St. Vincent and the Grenadines	78.6	80.2	77.5	69.5	67.5	73.2	80.0	83.6	84.3	85.6	86.8
External debt 3/	**62.1**	**53.9**	**50.9**	**47.4**	**46.0**	**50.1**	**53.3**	**54.7**	**55.4**	**54.9**	**55.4**
Anguilla	7.5	6.0	4.7	4.1	6.2	8.9	11.3	13.1	13.1	12.2	11.3
Antigua and Barbuda 2/	65.7	41.1	40.6	39.5	35.8	47.7	58.4	66.5	72.6	75.8	83.0
Dominica	74.9	69.0	68.0	62.3	57.8	54.8	51.7	48.0	44.6	41.8	37.3
Grenada	88.6	78.9	81.0	78.7	79.2	78.9	79.2	76.6	73.7	69.5	65.6
Montserrat	10.1	9.2	8.4	7.7	6.7	6.0	5.4	4.9	4.4	4.0	3.5
St. Kitts and Nevis	85.0	76.4	67.4	59.3	63.3	63.1	60.2	56.2	52.2	47.1	41.4
St. Lucia	45.0	46.7	44.5	45.3	43.6	46.4	48.1	49.1	49.1	49.1	48.9
St. Vincent and the Grenadines	52.9	52.0	46.4	37.0	35.0	37.2	41.3	41.9	43.1	44.0	44.5
Domestic debt	**45.2**	**46.6**	**47.5**	**47.1**	**44.5**	**47.8**	**50.4**	**52.0**	**53.0**	**54.4**	**54.9**
Anguilla	14.9	18.0	14.7	14.3	15.4	21.9	27.6	29.6	32.2	33.7	34.8
Antigua and Barbuda 2/	69.3	69.5	65.7	63.2	56.9	60.2	62.2	62.0	61.4	61.2	56.6
Dominica	32.9	31.6	31.1	27.2	24.0	23.2	22.6	22.3	21.8	20.8	21.5
Grenada	32.0	31.4	35.7	32.8	29.3	30.2	29.3	27.7	26.7	25.7	24.8
Montserrat	1.8	1.8	1.5	1.2	11.0	21.7	26.5	29.9	32.1	36.2	42.0
St. Kitts and Nevis	109.4	120.4	121.3	122.4	114.3	123.0	131.9	139.9	148.1	159.3	171.8
St. Lucia	19.3	19.3	21.1	24.0	26.5	29.2	32.4	35.0	37.1	38.7	41.0
St. Vincent and the Grenadines	25.7	28.2	31.1	32.5	32.6	36.0	38.6	41.7	41.2	41.6	42.3
				(In percent)							
Implied interest rate on central government debt											
Anguilla	4.6	5.1	6.5	6.2	5.5	6.5	6.7	7.0	6.9	7.0	7.0
Antigua and Barbuda	3.9	4.5	4.9	3.8	5.3	5.2	4.9	4.5	4.2	4.0	4.0
Dominica	6.1	6.4	3.0	3.5	2.9	3.3	3.1	2.9	2.8	2.8	2.7
Grenada	6.2	2.1	2.0	2.3	2.7	3.2	3.1	3.3	3.8	3.7	4.3
Montserrat	3.9	7.6	9.7	8.5	5.9	4.8	4.1	4.0	4.0	3.7	3.5
St. Kitts and Nevis	5.8	6.5	6.9	6.1	6.4	7.4	6.9	7.3	8.3	8.8	8.9
St. Lucia	4.7	4.6	5.1	5.1	5.6	5.6	5.6	5.6	5.6	5.6	5.6
St. Vincent and the Grenadines	3.5	4.2	4.8	5.5	5.3	5.2	5.6	5.7	5.8	5.9	6.0
Implied interest rates on central government external debt											
Anguilla	5.7	4.2	5.6	5.7	4.1	6.5	6.5	6.5	6.5	6.5	6.5
Antigua and Barbuda	3.6	5.7	6.3	6.9	7.1	5.1	4.1	3.2	2.5	2.1	1.6
Dominica	4.9	5.1	2.9	2.6	2.6	2.7	2.6	2.5	2.4	2.4	2.3
Grenada	6.1	1.3	1.9	2.1	2.2	2.9	3.1	3.3	3.8	3.6	4.1
Montserrat	4.2	8.6	11.0	9.3	9.8	10.6	10.6	10.6	10.7	10.7	10.8
St. Kitts and Nevis	6.8	7.8	6.8	6.8	6.2	7.6	7.0	7.5	8.6	9.4	9.9
St. Lucia	5.3	5.0	5.8	6.5	7.1	7.0	6.9	6.8	6.8	6.7	6.6
St. Vincent and the Grenadines	2.4	3.1	3.7	5.2	4.8	4.3	5.0	5.0	5.1	5.4	5.6
Implied interest rates on central government domestic debt											
Anguilla	4.3	5.3	6.7	6.2	6.5	6.5	6.7	7.1	7.0	7.1	7.1
Antigua and Barbuda	4.1	3.9	4.0	1.9	4.3	5.4	5.7	5.9	6.2	6.3	7.6
Dominica	8.5	8.9	3.0	5.2	3.6	4.4	3.9	3.7	3.5	3.3	3.2
Grenada	6.4	4.0	2.3	2.9	4.1	4.1	3.2	3.2	3.9	4.0	4.7
Montserrat	2.5	2.6	2.7	3.4	3.5	3.2	2.7	2.9	3.1	3.0	2.9
St. Kitts and Nevis	4.7	5.5	6.9	5.8	6.5	7.4	6.8	7.3	8.2	8.5	8.7
St. Lucia	6.0	5.9	5.7	5.3	5.8	5.7	5.7	5.7	5.7	5.6	5.6
St. Vincent and the Grenadines	6.6	7.4	7.0	5.9	6.0	6.4	6.4	6.5	6.7	6.6	6.6

Sources: Country authorities; and Fund staff estimates.

1/ Fiscal years for Dominica and St. Lucia.

2/ The decline of public debt in 2008 reflects debt write-down by the Banco do Brazil and two statutory bodies.

3/ Includes external arrears.

Table 5. ECCU: Monetary Survey, 2004–10

(In millions of Eastern Caribbean dollars)

					Prel.	Proj.	
	2004	2005	2006	2007	2008	2009	2010
I. Monetary Survey (Consolidated Banking System)							
Net foreign assets	**2,902.0**	**3,000.6**	**3,177.9**	**3,025.6**	**2,254.1**	**1,949.2**	**1,805.4**
Net domestic assets	**5,449.7**	**6,055.0**	**6,927.2**	**8,062.5**	**9,165.5**	**9,351.1**	**9,732.7**
Net credit to the public sector	-219.2	-10.7	-148.3	-72.4	88.1	115.4	113.4
Central government	482.9	652.3	638.7	872.2	1,029.7	1,055.4	1,053.4
Nonfinancial public enterprises 1/	-702.1	-663.0	-787.0	-944.6	-941.6	-940.0	-940.0
Credit to private sector	6,599.4	7,371.1	8,697.0	10,445.8	11,577.9	11,690.0	12,073.6
Other	-930.4	-1,305.4	-1,621.4	-2,311.0	-2,500.5	-2,454.3	-2,454.3
Liabilities to private sector (M2)	**8,351.7**	**9,055.6**	**10,105.1**	**11,088.1**	**11,419.6**	**11,300.4**	**11,538.1**
Money (M1)	1,886.8	2,086.7	2,258.9	2,493.8	2,481.3	2,346.8	2,294.8
Quasi-money	6,464.9	6,968.9	7,846.2	8,594.3	8,938.3	8,953.6	9,243.3
II. Eastern Caribbean Central Bank							
Net foreign assets	**1,702.9**	**1,611.7**	**1,871.9**	**2,055.8**	**2,043.2**	**1,849.9**	**1,778.2**
Net domestic assets	**-1,216.8**	**-1,090.3**	**-1,285.9**	**-1,461.1**	**-1,430.4**	**-1,356.1**	**-1,367.2**
Net position with banks and other institutions	-1,161.7	-1,043.7	-1,172.2	-1,296.1	-1,258.6	-1,226.1	-1,237.2
Credit to government	-39.0	-14.8	-52.8	-74.9	-53.1	-50.0	-50.0
Other	-16.1	-31.8	-61.0	-90.2	-118.7	-80.0	-80.0
Liabilities to private sector	**486.1**	**521.4**	**586.0**	**594.7**	**612.8**	**493.8**	**411.0**
Currency issued	662.9	732.8	783.3	842.1	878.3	720.2	667.4
Currency held by banks	-176.8	-211.4	-197.3	-247.4	-265.4	-226.4	-256.4
III. Commercial Banks							
Net foreign assets	**1,199.0**	**1,388.9**	**1,306.0**	**969.8**	**210.9**	**99.4**	**27.2**
Net claims on ECCB	1,170.4	1,029.2	1,180.2	1,266.4	1,251.1	1,226.1	1,237.2
Net domestic credit	**5,496.1**	**6,116.1**	**7,033.0**	**8,257.2**	**9,344.8**	**9,481.1**	**9,862.7**
Net credit to the public sector	-180.2	4.1	-95.6	2.5	141.2	165.4	163.4
Central government	522.0	667.1	691.5	947.1	1,082.8	1,105.4	1,103.4
Rest of the public sector	-702.1	-663.0	-787.0	-944.6	-941.6	-940.0	-940.0
Credit to private sector	6,599.4	7,371.1	8,697.0	10,445.8	11,577.9	11,690.0	12,073.6
Other	-1,069.6	-1,259.1	-1,568.5	-2,191.1	-2,374.3	-2,374.3	-2,374.3
Liabilities to the private sector	**7,865.6**	**8,534.2**	**9,519.1**	**10,493.4**	**10,806.8**	**10,806.6**	**11,127.1**
(Percentage growth compared to M2 at the beginning of the year)							
Memorandum items of the consolidated banking system:							
Net foreign assets	6.8	1.2	2.0	-1.5	-7.0	-2.7	-1.3
Central bank	3.4	-1.1	2.9	1.8	-0.1	-1.7	-0.6
Commercial banks	3.3	2.3	-0.9	-3.3	-6.8	-1.0	-0.6
Net domestic assets	6.4	7.2	9.6	11.2	9.9	1.6	3.4
Of which							
Net credit to the public sector	0.0	2.5	-1.5	0.8	1.4	0.2	0.0
Credit to the private sector	5.1	9.2	14.6	17.3	10.2	1.0	3.4
(Annual percentage change)							
Liabilities to the private sector (M2)	13.2	8.4	11.6	9.7	3.0	-1.0	2.1
Private sector credit	6.1	11.7	18.0	20.1	10.8	1.0	3.3
Income velocity of broad money	1.09	1.10	1.09	1.08	1.12	1.15	1.15
Private sector credit/GDP (percent)	72.4	73.7	79.1	87.2	90.5	90.3	90.9
Broad money/GDP (percent)	91.6	90.6	91.9	92.6	89.3	87.3	86.8
Foreign currency deposits/GDP (percent)	12.9	14.1	16.0	16.1	13.9	13.7	13.8

Sources: ECCB; and Fund staff estimates.

1/ Includes the national insurance schemes.

Table 6. ECCU: Summary Balance of Payments, 2004–14

	2004	2005	2006	2007	Prel. 2008	Proj. 2009	2010	2011	2012	2013	2014
(In millions of U.S. dollars)											
Current account	**-552.4**	**-827.7**	**-1,207.5**	**-1,544.7**	**-1,604.6**	**-1,160.9**	**-1,188.1**	**-1,290.1**	**-1,347.9**	**-1,319.3**	**-1,222.8**
Trade balance	-1,232.8	-1,488.8	-1,814.5	-2,086.6	-2,144.7	-1,523.4	-1,595.4	-1,855.0	-2,035.0	-2,210.4	-2,430.9
Exports	342.8	370.1	360.8	378.0	426.6	390.0	389.8	404.0	422.7	444.3	469.9
Imports	-1,575.6	-1,858.9	-2,175.3	-2,464.6	-2,571.3	-1,913.4	-1,985.2	-2,259.0	-2,457.7	-2,654.6	-2,900.8
Services and income	460.4	473.1	443.1	392.6	386.8	221.2	257.9	407.3	516.2	698.0	987.3
Services	765.3	721.5	659.1	628.3	593.8	437.3	477.3	629.4	743.6	925.2	1,216.0
Transportation	-140.9	-174.4	-209.0	-236.9	-256.6	-260.4	-267.9	-281.4	-298.3	-317.0	-337.1
Travel	959.5	989.7	991.6	1,009.3	982.0	827.3	877.4	1,036.8	1,160.7	1,354.0	1,658.2
Other services	-53.4	-93.9	-123.4	-144.1	-131.5	-129.6	-132.3	-125.9	-118.8	-111.8	-105.1
Income	-304.9	-248.4	-216.0	-235.7	-207.0	-216.1	-219.3	-222.1	-227.4	-227.2	-228.7
Current transfers	220.1	188.1	163.9	149.3	153.3	141.3	149.4	157.6	171.0	193.1	220.9
Capital and financial account	**657.8**	**809.1**	**1,299.4**	**1,591.5**	**1,586.0**	**1,071.7**	**1,160.1**	**1,294.8**	**1,376.1**	**1,334.4**	**1,239.2**
Capital transfers (net)	132.1	330.1	173.8	198.2	199.8	190.0	200.0	200.0	200.0	200.0	200.0
Financial account	525.7	479.1	1,125.5	1,393.3	1,386.2	881.7	960.1	1,094.8	1,176.1	1,134.4	1,039.2
Direct investment	458.6	639.8	1,072.2	1,229.2	1,071.2	782.6	877.4	1032.4	1109.7	1085.0	994.6
Portfolio investment	72.5	31.1	21.9	-27.7	10.0	10.0	20.0	20.0	20.0	20.0	20.0
Public sector long term	46.3	-110.0	4.9	21.2	31.7	48.7	33.2	30.7	27.1	14.5	16.5
Other public sector capital	0.0	5.2	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Commercial banks	-98.8	-77.4	30.7	124.5	281.0	41.3	26.7	10.4	16.8	15.9	8.6
Other capital 1/	47.2	-9.7	-4.2	46.1	-7.7	-0.9	2.8	1.3	2.5	-1.0	-0.5
Overall balance	**105.4**	**-18.5**	**91.9**	**46.8**	**-18.6**	**-89.2**	**-28.0**	**4.7**	**28.2**	**15.1**	**16.4**
Financing	**-105.4**	**18.5**	**-91.9**	**-46.8**	**18.6**	**89.2**	**28.0**	**-4.7**	**-28.2**	**-15.1**	**-16.4**
Of which : Changes in imputed reserves (increase -)	-97.2	28.3	-93.8	-56.4	19.1	71.6	26.6	-1.4	-22.9	-10.2	-12.9
Fund financing	5.2	3.2	2.4	-4.7	8.9	17.6	1.4	-3.3	-5.3	-4.9	-4.5
(In percent of GDP)											
Current account	**-16.4**	**-22.4**	**-29.7**	**-34.8**	**-33.9**	**-24.2**	**-24.1**	**-25.0**	**-24.6**	**-22.7**	**-19.8**
Exports	10.1	10.0	8.9	8.5	9.0	8.1	7.9	7.8	7.7	7.6	7.6
Imports	-46.7	-50.2	-53.4	-55.6	-54.3	-39.9	-40.3	-43.8	-44.9	-45.7	-46.9
Services, incomes and transfers	20.1	17.9	14.9	12.2	11.4	7.6	8.3	10.9	12.6	15.3	19.5
Of which											
Travel	28.4	26.7	24.4	22.8	20.7	17.3	17.8	20.1	21.2	23.3	26.8
Current transfers	6.5	5.1	4.0	3.4	3.2	2.9	3.0	3.1	3.1	3.3	3.6
Capital and financial account	**19.5**	**21.9**	**31.9**	**35.9**	**33.5**	**22.4**	**23.6**	**25.1**	**25.2**	**23.0**	**20.0**
Of which											
Direct investment	13.6	17.3	26.3	27.7	22.6	16.3	17.8	20.0	20.3	18.7	16.1
Overall balance	**3.1**	**-0.5**	**2.3**	**1.1**	**-0.4**	**-1.9**	**-0.6**	**0.1**	**0.5**	**0.3**	**0.3**
(Annual percentage change)											
Exports	11.6	8.0	-2.5	4.8	12.9	-8.6	-0.1	3.7	4.6	5.1	5.8
Imports	5.5	18.0	17.0	13.3	4.3	-25.6	3.8	13.8	8.8	8.0	9.3
Travel (net)	12.0	3.1	0.2	1.8	-2.7	-15.7	6.1	18.2	12.0	16.7	22.5
Foreign direct investment	-17.5	39.5	67.6	14.6	-12.9	-26.9	12.1	17.7	7.5	-2.2	-8.3
Memorandum items:											
End-year gross reserves of the ECCB, US$ millions	632.4	600.8	696.0	764.5	759.0	687.4	660.8	662.3	685.2	695.4	708.3
In months of current year imports	4.8	3.9	3.8	3.7	3.5	4.3	4.0	3.5	3.3	3.1	2.9
ECCU GDP at market prices, US$ millions	3,377	3,703	4,071	4,435	4,738	4,793	4,921	5,163	5,470	5,813	6,185

Sources: ECCB; and Fund staff estimates and projections.

1/ Includes errors and omissions.

Table 7. ECCU: Selected Vulnerability Indicators, 2004–10

					Prel.	Proj.	
	2004	2005	2006	2007	2008	2009	2010
Key economic and market indicators							
Real GDP growth	3.9	5.6	6.3	5.2	1.8	-2.4	-0.1
CPI inflation, (in percent, end of year)	2.6	4.2	2.8	5.7	5.0	2.4	2.3
Interbank interest rate (in percent, end of year)	4.6	4.3	5.2	5.1	5.2	...	...
Exchange rate, EC$/US$ (end of period)	2.7	2.7	2.7	2.7	2.7	2.7	2.7
External sector							
Current account balance (percent of GDP)	-16.4	-22.4	-29.7	-34.8	-33.9	-24.2	-24.1
FDI inflows (percent of GDP)	13.6	17.3	26.3	27.7	22.6	16.3	17.8
Export growth (f.o.b)	11.6	8.0	-2.5	4.8	12.9	-8.6	-0.1
Travel (percent of GDP)	28.4	26.7	24.4	22.8	20.7	17.3	17.8
Terms of trade (12-month percentage change) 1/	-4.4	-2.8	-9.7	-1.5	-14.0	...	...
Real effective exchange rate (1990=100) 1/	93.0	92.2	92.1	90.0	90.9	...	...
Gross international reserves (in US$ billion)	0.632	0.601	0.696	0.765	0.759	0.687	0.661
Net international reserves (in US$ billion)	0.631	0.597	0.693	0.761	0.757	0.685	0.659
Total gross external public debt (percent of GDP)	62.1	53.9	50.9	47.4	46.0	50.1	53.3
Gross external financing requirement (in US$ billion) 2/	0.674	1.045	1.281	1.670	1.698	1.268	1.280
Consolidated public sector (percent of GDP)							
Overall central government balance	-4.3	-4.4	-5.1	-4.4	-4.7	-6.8	-6.9
Primary central government balance	0.1	-0.5	-1.1	-0.8	-0.7	-2.2	-2.2
Central government current account balance	-0.3	0.7	1.4	2.5	1.3	-1.6	-0.8
Public sector gross debt (end-of-period)	107.3	100.5	98.4	94.5	90.6	97.9	103.8
Public and private financial sector (in percent)							
Capital adequacy ratio (indigenous banks, Tier I capital over risk weighted assets)	16.5	17.5	18.3	18.2	18.0	…	…
NPLs/total loans	12.0	9.4	7.6	6.0	7.7	…	…
Indigenous banks	15.6	11.7	9.5	7.5	10.2	…	…
Foreign banks	7.3	6.7	5.3	4.3	4.5	…	…
Loan loss provision/NPLs	34.4	34.9	31.6	31.8	23.4	…	…
Indigenous banks	31.3	33.2	26.8	26.0	17.9	…	…
Foreign banks	44.4	38.4	42.0	43.9	39.2	…	…
Loans to agricultural sector/total loans	4.0	3.6	3.0	2.7	3.1	…	…
Loans to tourism sector/total loans	7.7	8.0	9.6	11.2	11.3	…	…
Loans to household sector/total loans	47.5	47.5	45.3	43.1	42.3	…	…
Gross government claims/total assets	15.5	15.1	14.4	13.4	14.3	…	…
Government deposits/total deposits	16.8	17.1	17.8	17.2	17.8	…	…
FX deposits/total deposits	15.4	16.0	18.0	17.6	16.8	…	…
Liquid assets/total assets	31.0	28.7	27.0	25.3	22.1	…	…
Large loans and advances/total loans	28.7	28.2	29.5	31.5	29.1	…	…
Large deposits/total deposits	22.6	22.2	23.0	23.3	21.3	…	…
Risk-weighted assets/total assets	52.4	54.1	54.9	58.4	63.1	…	…
Contingent liabilities/capital (indigenous banks)	75.1	85.4	87.0	72.8	68.3	…	…
(Pre-tax) return on average assets	1.7	2.1	2.5	2.6	2.6	…	…
(Pre-tax) return on average equity	13.6	16.1	21.5	21.3	21.3	...	...
Memorandum items:							
ECCB reserve cover (in percent) 3/	96.2	96.5	98.7	100.1	102.0	...	...
ECCB gross reserves/broad money (in percent)	20.4	17.9	18.6	18.6	17.9	16.4	15.5

Sources: Country authorities; and Fund staff estimates and projections.

1/ Excludes Anguilla and Montserrat.
2/ Defined as external current account deficit plus external amortization.
3/ Foreign assets as a percentage of demand liabilities.

Table 8. ECCU: Creditor Composition of Public Debt at End-2008 1/

(Share of total)

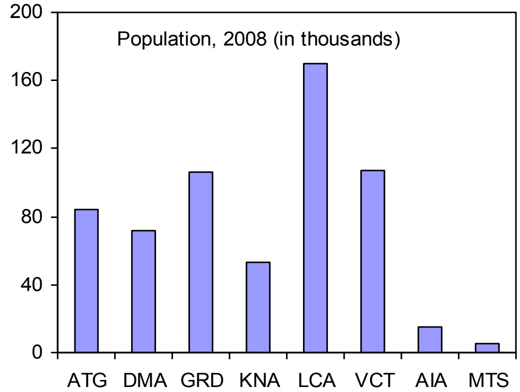
	Antigua and Barbuda	Dominica	Grenada	St. Kitts and Nevis	St. Lucia	St. Vincent and the Grenadines
External debt	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**
Central government	83.6	71.3	88.1	77.2	81.7	84.9
Multilateral	5.6	47.0	33.0	21.0	47.6	47.0
Official bilateral	24.5	10.9	15.7	12.9	4.5	16.2
Commercial	53.5	10.6	39.4	14.0	19.2	21.7
Other	0.0	2.8	0.0	29.2	10.4	0.0
Arrears, total	n.a.	0.0	0.0	0.0	0.0	0.0
Other public sector	16.4	28.7	11.9	22.8	18.3	15.1
Domestic debt	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**
Central government	94.5	94.6	82.5	77.9	93.7	59.0
ECCB	0.0	1.8	0.0	0.5	0.4	1.2
Private domestic banks	20.5	29.7	11.6	51.2	51.3	43.9
Nonbank financial institutions	0.0	11.0	0.0	3.5	8.7	0.0
Insurance funds	0.0	47.6	0.0	4.9	2.9	3.5
Other	16.1	4.6	68.9 2/	17.8	30.3	10.4
Arrears, total	57.9	0.0	1.9	0.0	0.0	0.0
Other public sector	5.5	5.4	17.5	22.1	6.3	41.0
Memorandum items:						
Public debt (percent of GDP)	92.7	81.8	108.6	177.6	70.1	67.5
Of which						
External debt	35.8	57.8	79.2	63.3	43.6	35.0
Public debt (millions of U.S. dollars)	1134.6	305.1	693.3	969.9	719.6	405.6
Of which						
External debt	438.4	215.6	506.0	345.8	447.8	210.0

Sources: ECCB; and Fund staff estimates.

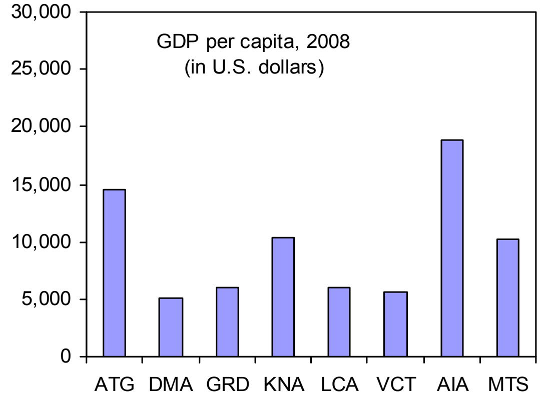
1/ Excludes Anguilla and Montserrat.
2/ No creditor breakdown is available for restructured and unrestructured domestic bonds.

Figure 1. ECCU: Key Characteristics

The economies are small...



...and at different stages of development.



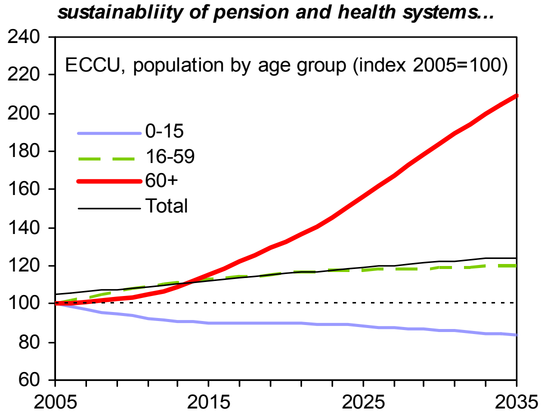
They are all vulnerable to natural disasters. .

Worldwide Incidence of Natural Disasters, 1970–2008 1/

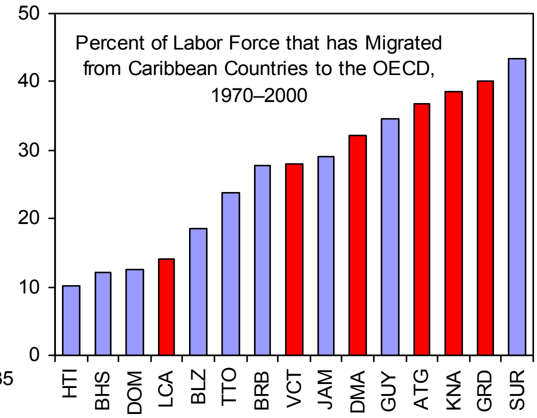
	All Recorded Disasters				
	Number of Events	Number of Events Divided by Land Area		Number of Events Divided by Population	
		Index	Rank	Index	Rank
All countries	9,278	100	95	100	95
Advanced economies	1,841	9	106	0	115
Caribbean	356	576	38	874	34
ECCU	68	938	7	2,185	11
Anguilla	5	1,500	3	4,361	2
Antigua and Barbuda	8	556	10	0	14
Dominica	11	449	15	0	8
Grenada	6	540	11	0	18
Montserrat	7	2,100	2	13,120	1
St. Kitts and Nevis	7	824	5	0	11
St. Lucia	12	592	8	0	17
St. Vincent and the Grenadines	12	942	4	0	13
Other Caribbean	288	4,023	693	0	594
Other	7,081	49	102	10	101

...and external shocks given the high degree of openness.

Rapid population aging is a challenge for the sustainabliity of pension and health systems...



...and emigration, among the highest in the world, is creating additional pressures.

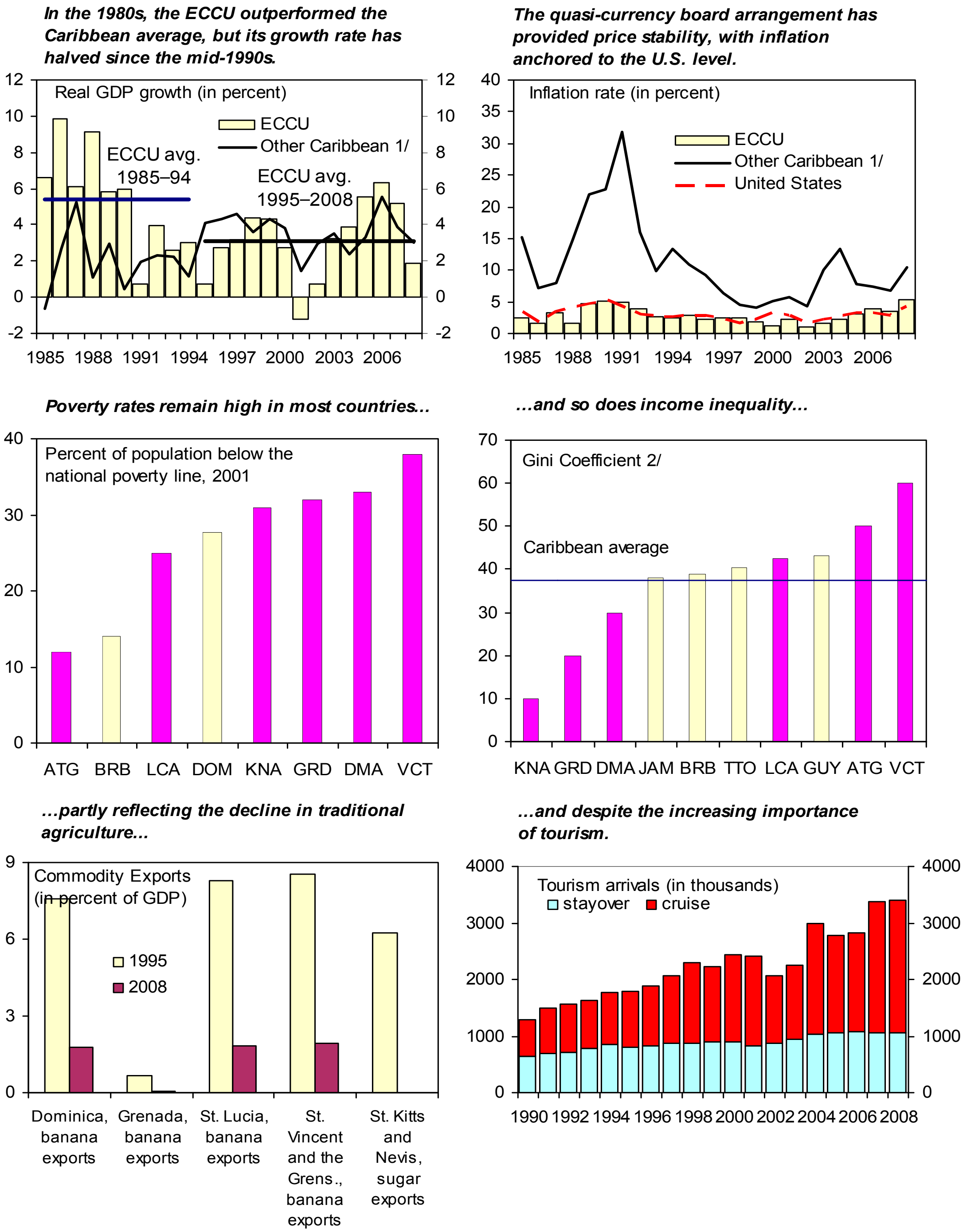


Sources: IMF, WEO; World Bank, WDI; EM-Dat; ECCB; and Fund staff calculations.

1/ The sample contains 190 countries. Simple unweighted averages are used for country groupings. Rankings are in descending order, with "1" indicating the most exposed to natural disasters.

Note: Antigua and Barbuda (ATG), The Bahamas (BHS), Barbados (BRB), Belize (BLZ), Dominica (DMA), Dominican Republic (DOM), Grenada (GRD), Guyana (GUY), Haiti (HTI), Jamaica (JAM), Montserrat (MTS), St. Kitts and Nevis (KNA), St. Lucia (LCA), St. Vincent and the Grenadines (VCT), Suriname (SUR), Trinidad and Tobago (TTO).

Figure 2. ECCU: Overview



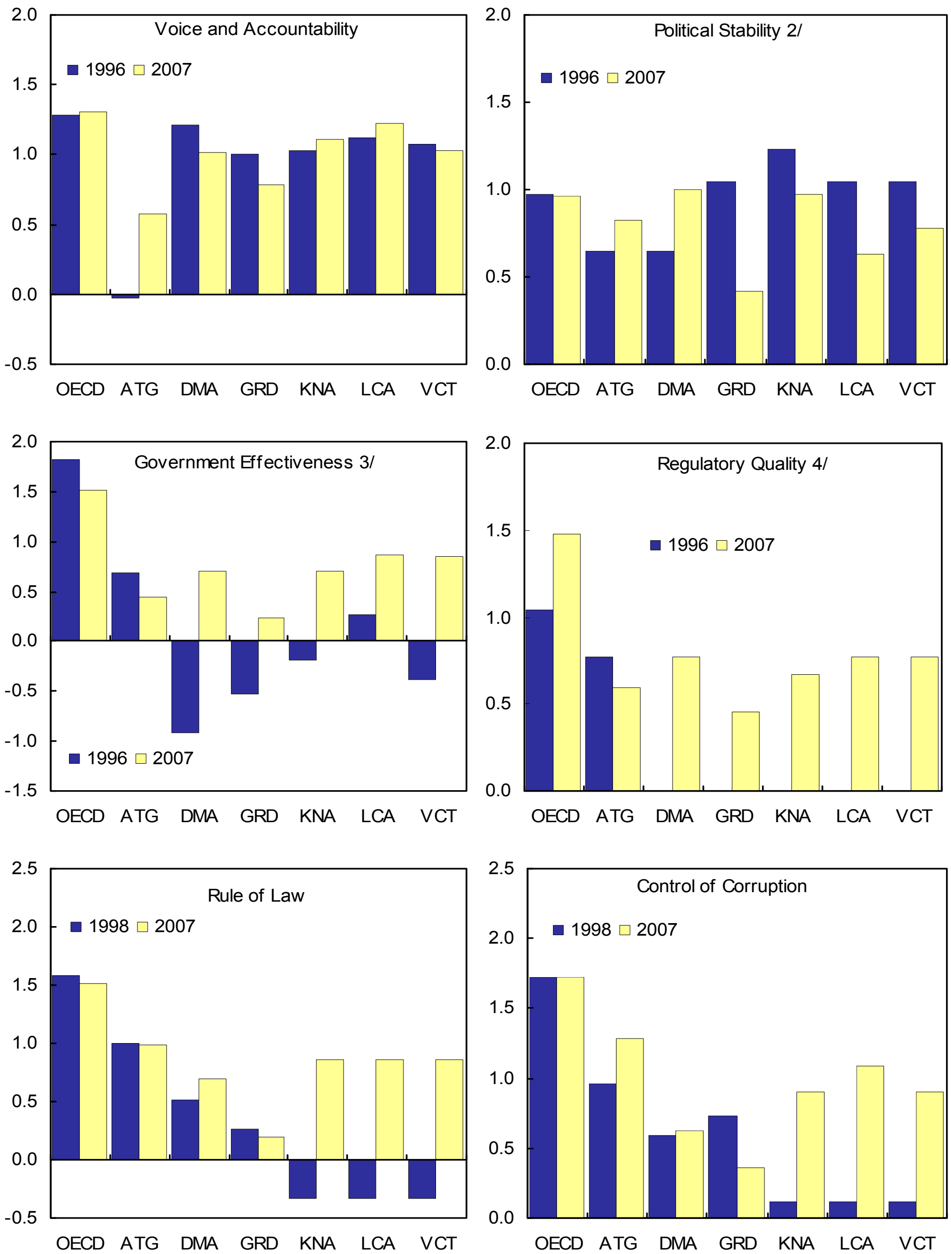
Sources: ECCB; World Bank; and Fund staff estimates.

1/ Simple average of The Bahamas, Barbados, Belize, Dominican Republic, Guyana, Haiti, Jamaica, and Trinidad and Tobago.

2/ A larger value indicates greater income inequality.

Note: Antigua and Barbuda (ATG), Barbados (BRB), Dominica (DMA), Dominican Republic (DOM), Grenada (GRD), Guyana (GUY), Jamaica (JAM), St. Kitts and Nevis (KNA), St. Lucia (LCA), St. Vincent and the Grenadines (VCT), Trinidad and Tobago (TTO).

Figure 3. ECCU: Governance Indicators 1/



Source: World Bank.

1/ The units in which governance indicators are measured follow a normal distribution with a mean of zero and a standard deviation of one in each period. Changes of the indicators over time for individual countries indicate changes in individual countries' relative positions in the sample.

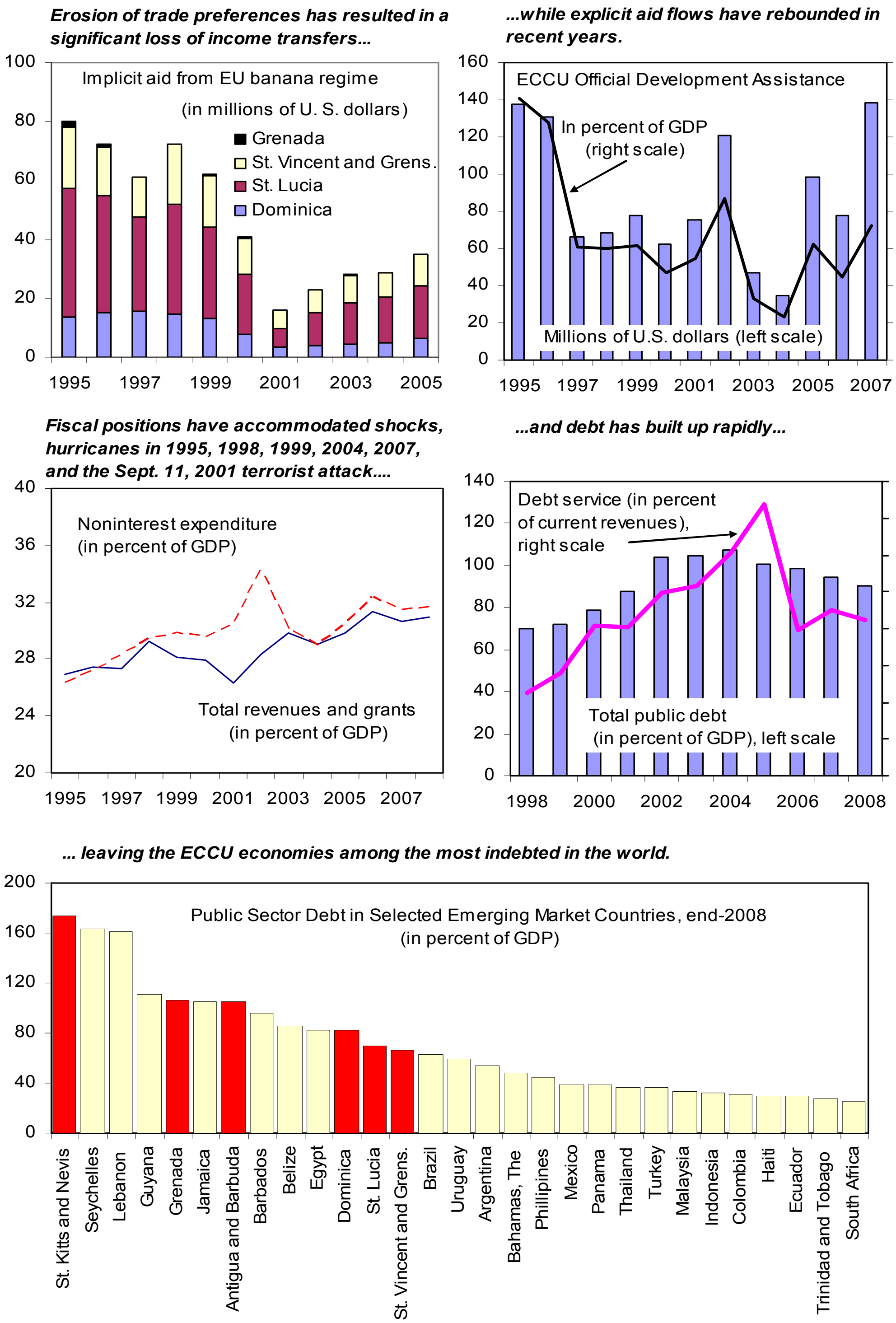
2/ Initial year for ATG (1998), DMA (1998) and KNA (2003).

3/ Initial year for ATG (1998).

4/ Initial year for ATG (1998).

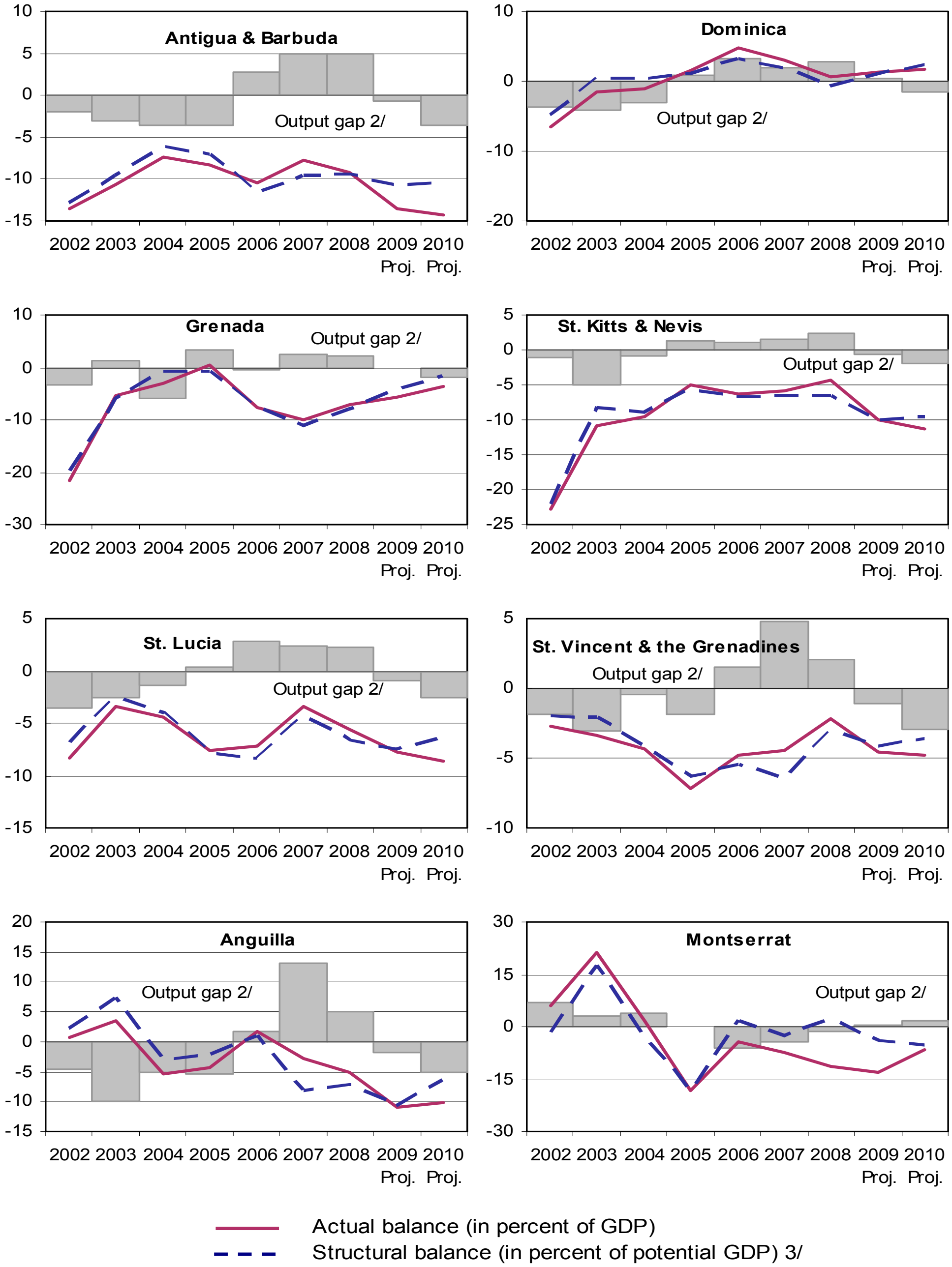
Note: Organisation for Economic Co-operation and Development (OECD), Antigua and Barbuda (ATG), Dominica (DMA), Grenada (GRD), St. Kitts and Nevis (KNA), St. Lucia (LCA), St. Vincent and the Grenadines (VCT).

Figure 4. ECCU: External Environment, 1995–2008



Sources: World Bank, World Development Indicators; IMF, International Financial Statistics; IMF, World Economic Outlook; OECD, International Development Statistics; ECCB; and Fund staff calculations.

Figure 5. ECCU: Central Government Actual and Structural Budget Balances, 2002–10 1/
(In percent of potential GDP)



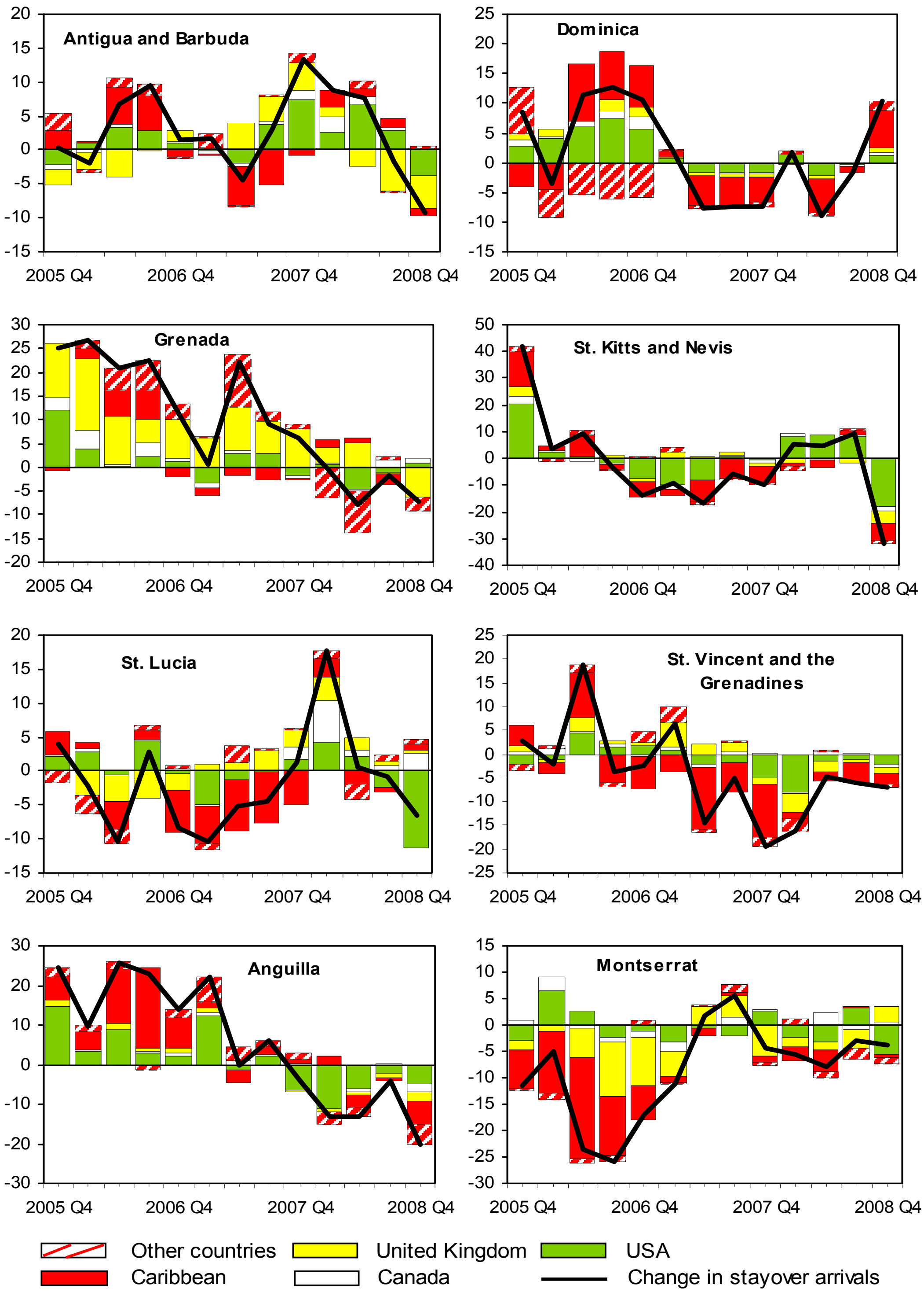
Sources: Country authorities; ECCB; and Fund staff estimates.

1/ Actual balance is the overall balance (revenue and grants less expenditure), and is expressed as a percentage of actual output. Actual output is measured as gross domestic product (GDP) at factor cost.

2/ The output gap is actual output less potential output, as a percent of potential output.

3/ Structural balance is expressed as a percent of potential output. The structural balance is the budgetary position (overall balance) that would be observed if the level of actual output coincided with potential output.

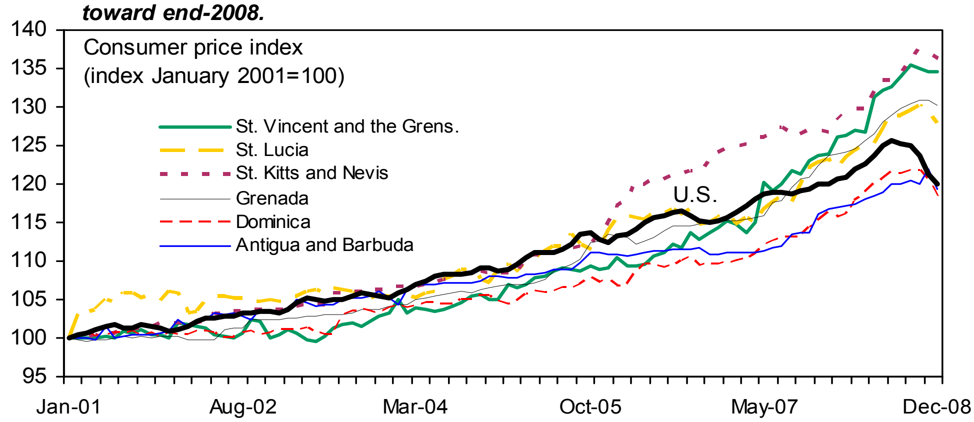
Figure 6. ECCU: Stayover Arrivals, 2005–08
(Annual percentage change)



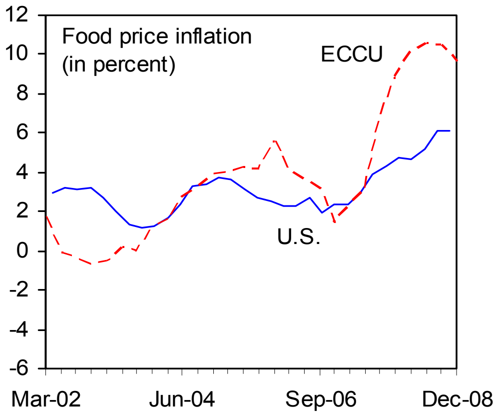
Sources: ECCB; and Fund staff calculations.

Figure 7. ECCU: Inflation Developments, 2001–08

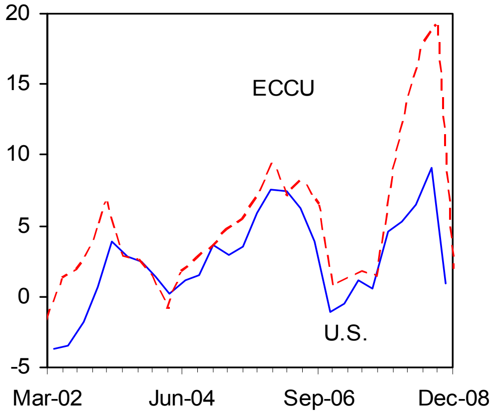
Inflationary pressures have emerged in the region since late 2007 and subsided toward end-2008.



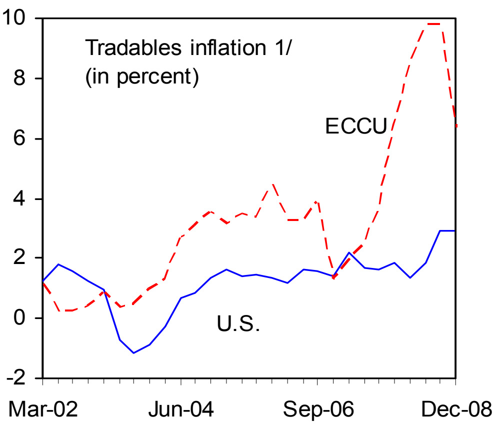
...reflecting higher world food prices...

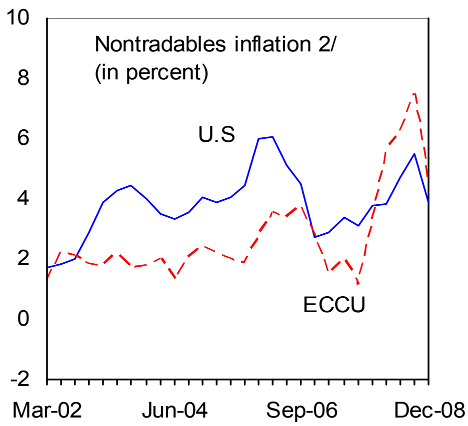


...and energy prices...



...which, along with currency depreciation, have pushed up tradables inflation.



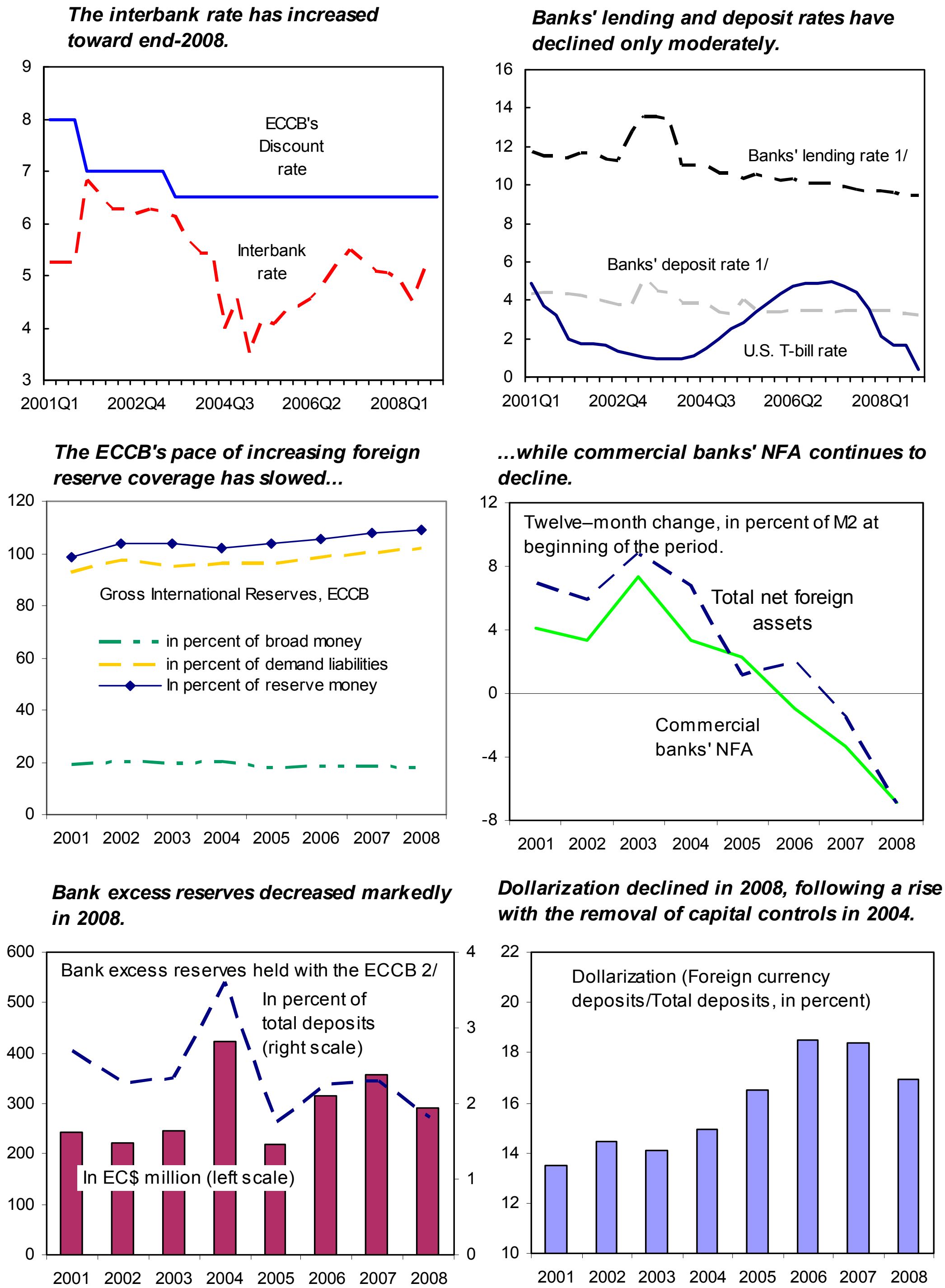


Sources: IMF, Direction of Trade Statistics; Haver; ECCB; and Fund staff calculations.

1/ Tradables are defined to include food, alcoholic beverages and tobacco, fuel and light, clothing and footwear, and household and furniture equipment.

2/ Nontradables are defined to include housing and utilities, transportation and communication, medical care and expenses, education, personal services, and miscellaneous.

Figure 8. ECCU: Monetary Developments, 2001–08



Sources: ECCB; and Fund staff calculations.

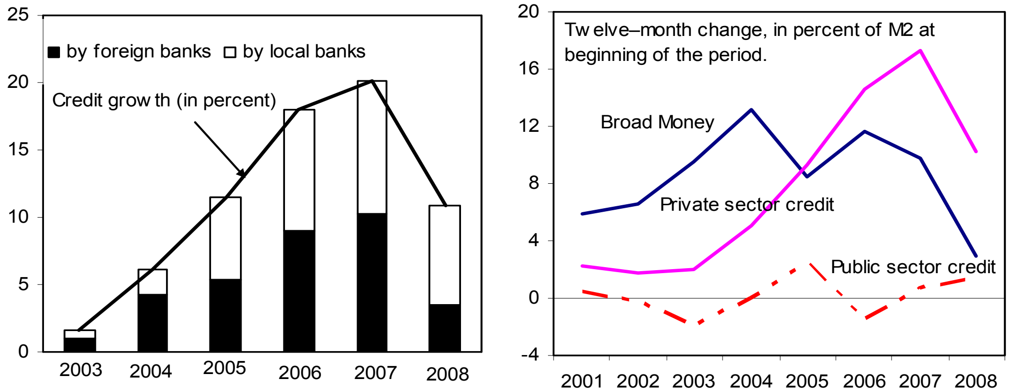
1/ There was a break in the interest rate series in 2003Q2.

2/ Excess reserves is defined as the excess of bank reserves (cash holdings and deposits of commercial banks with the ECCB) over required reserves. The current reserve requirement is 6 percent of deposits.

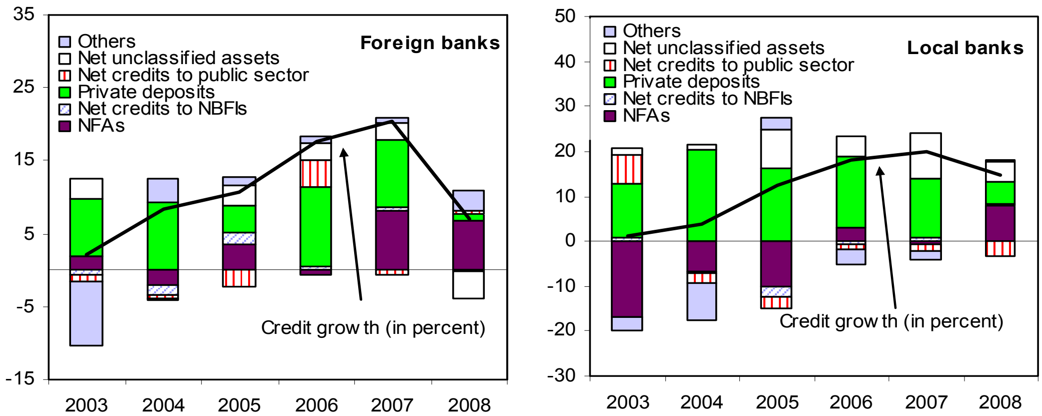
Figure 9. ECCU: Private Sector Credit Growth, 2001–08

In 2008 local banks contributed more to private credit growth...

...which has slowed markedly in 2008, following a strong acceleration since 2003.

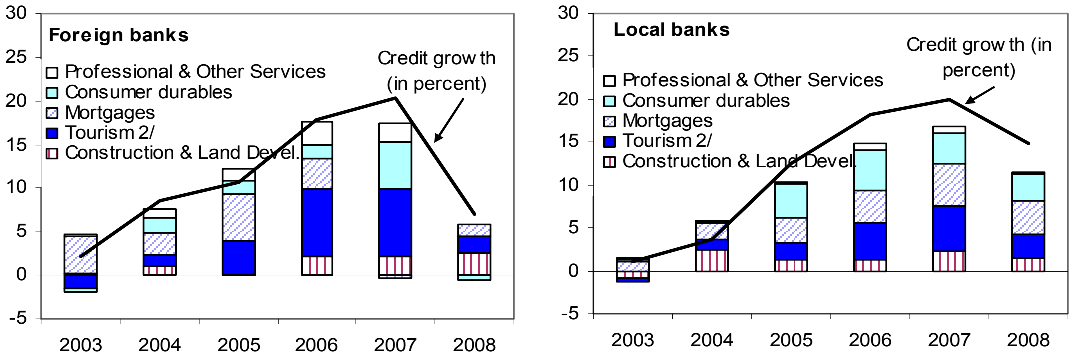


For the first time in recent years, drawdown of NFAs has become the major financing sources for both foreign and local banks in 2008.



Tourism and consumer loans accounted for most of the sharp decline in credit growth by foreign banks in 2008...

...while tourism loans accounted for most of the moderate decline by local banks.

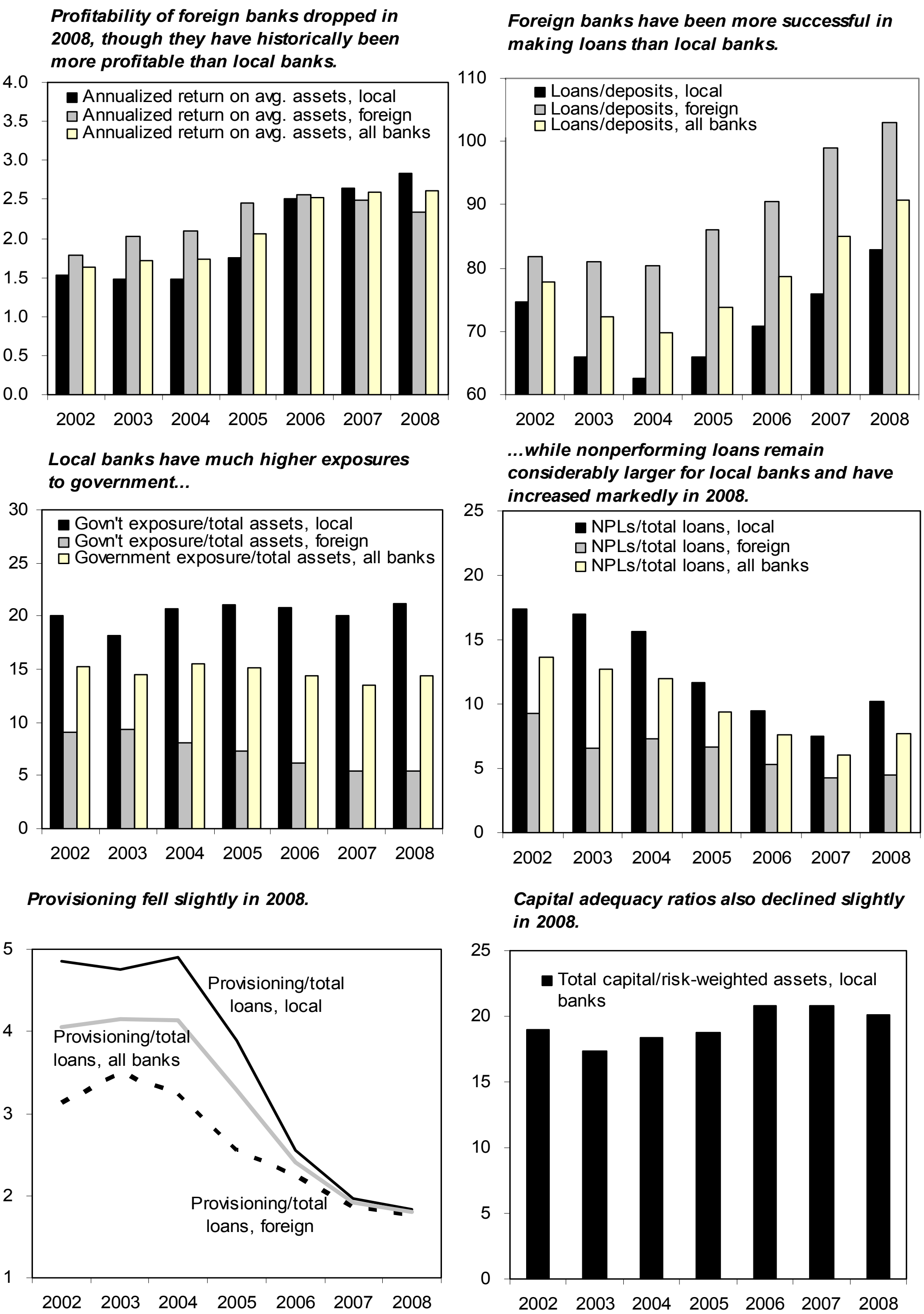


Sources: ECCB; and Fund staff calculations.

1/ Includes interbank float, reserves held with the ECCB, and other unclassified assets.

2/ Includes tourism, entertainment, and half of transport, distributive trade and professional services.

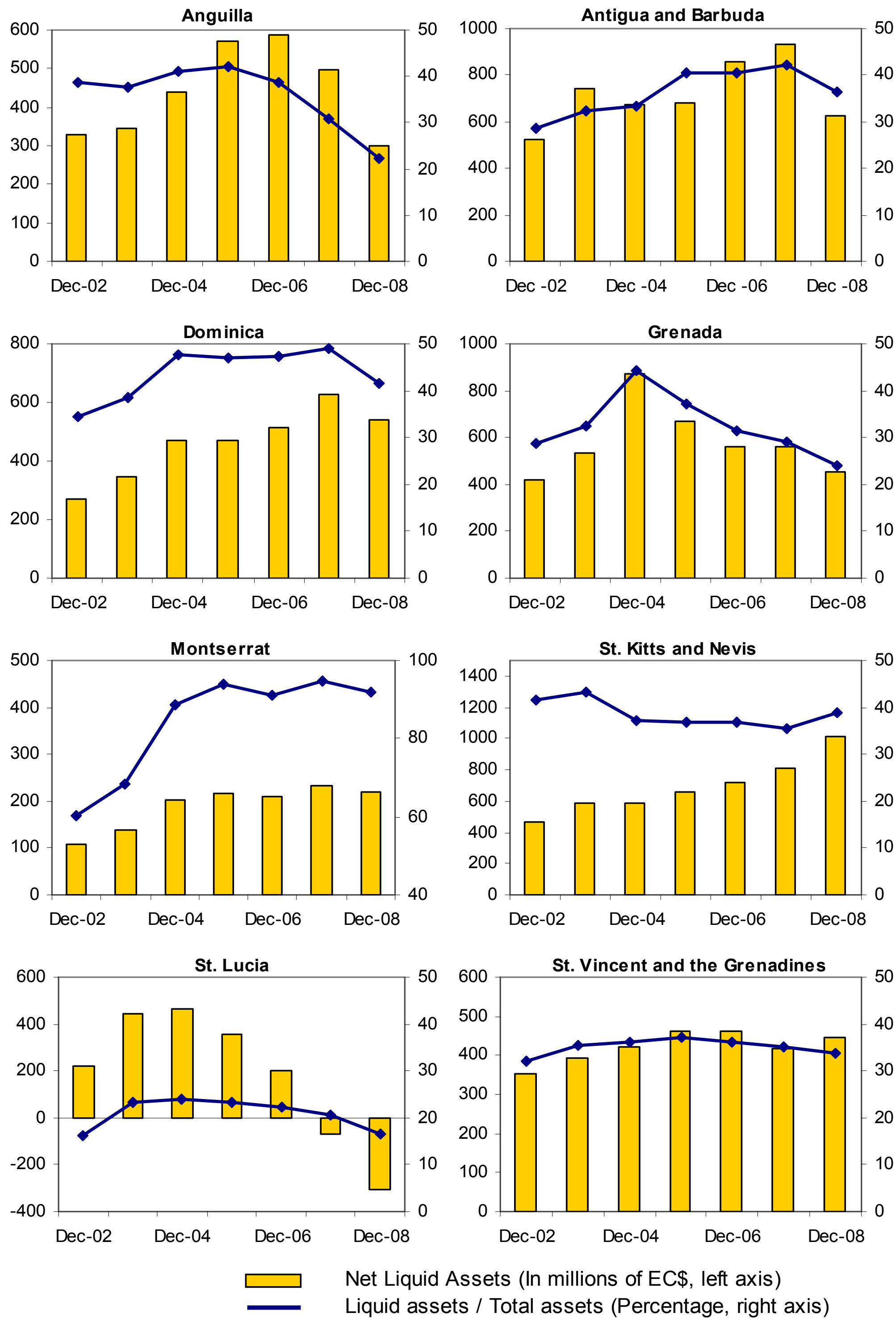
Figure 10. ECCU: Banking System Vulnerabilities, 2002–08 1/



Sources: ECCB; and Fund staff calculations.

1/ Prudential indicators are reported by commercial banks, with infrequent onsite verification by the ECCB.

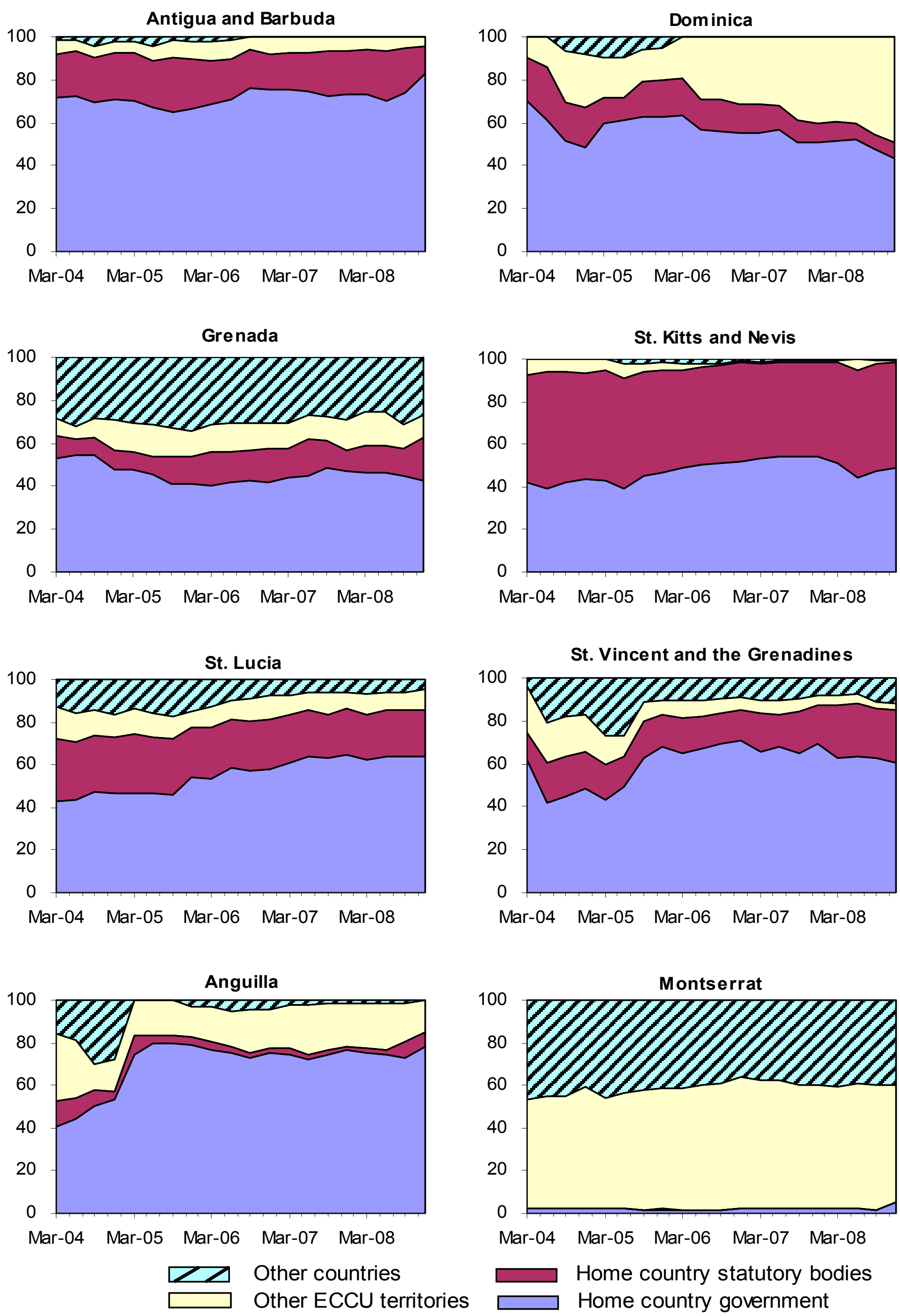
Figure 11. ECCU: Bank Liquidity, 2002–08



Source: ECCB.

Figure 12. ECCU: Decomposition of Commercial Banks' Exposure to the Public Sector, 2004–08
(In percent of public sector exposure)

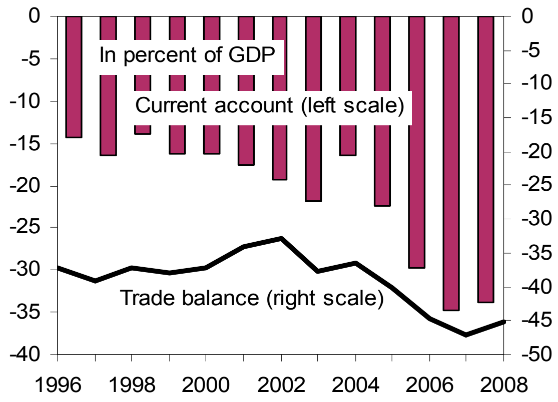
Commercial banks have large exposures to their home country public sector.



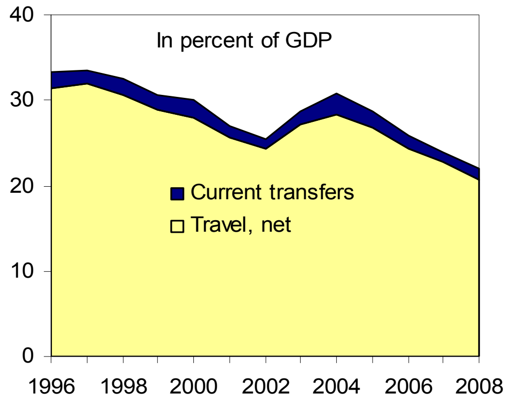
Sources: ECCB; and Fund staff calculations.

Figure 13. ECCU: Trade and Capital Account, 1996–2008

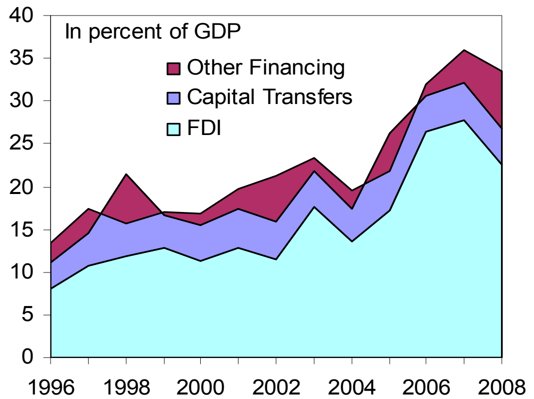
Strong imports have brought trade and current account deficits to historic highs...



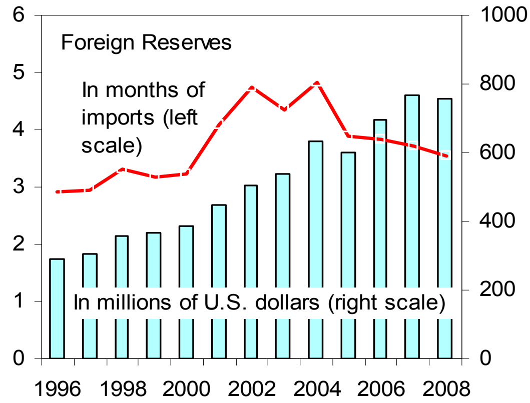
...with tourism receipts and remittances declining markedly.



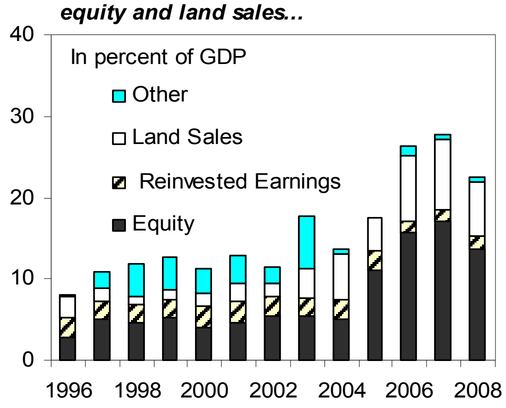
The current account was almost fully financed by FDI flows and capital transfers, though other financing also played a role in 2008.



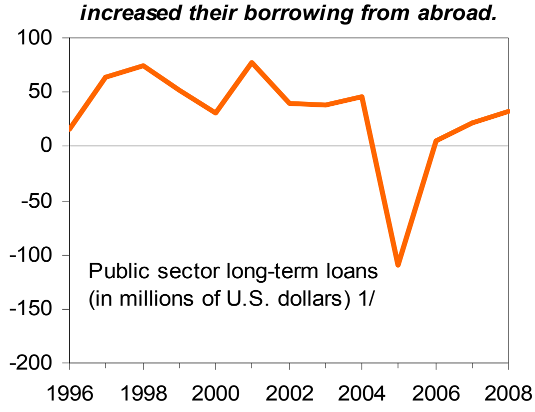
There was a small loss of foreign reserves in 2008.



FDI has been mostly in the form of equity and land sales...

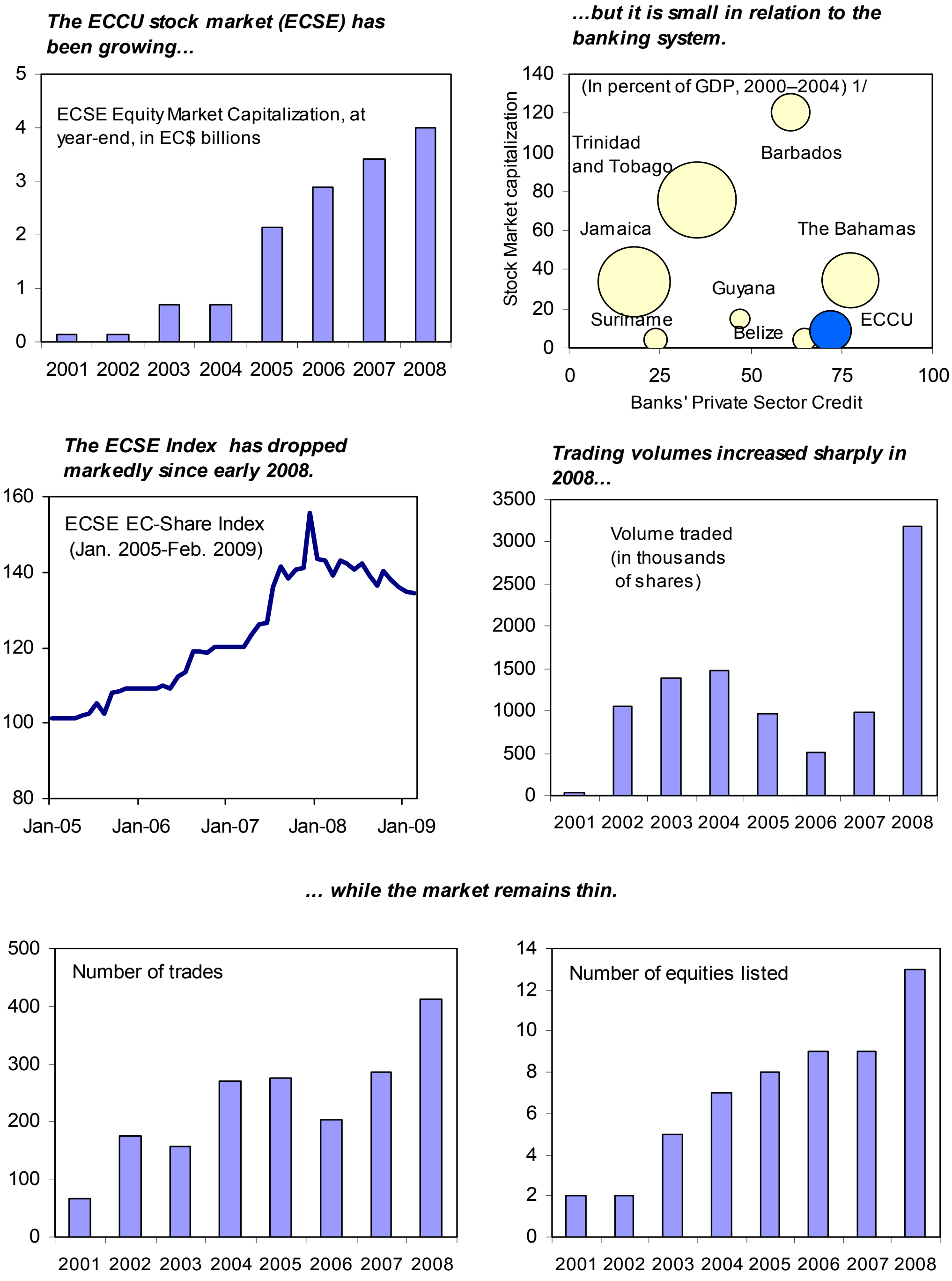


...and governments have recently increased their borrowing from abroad.



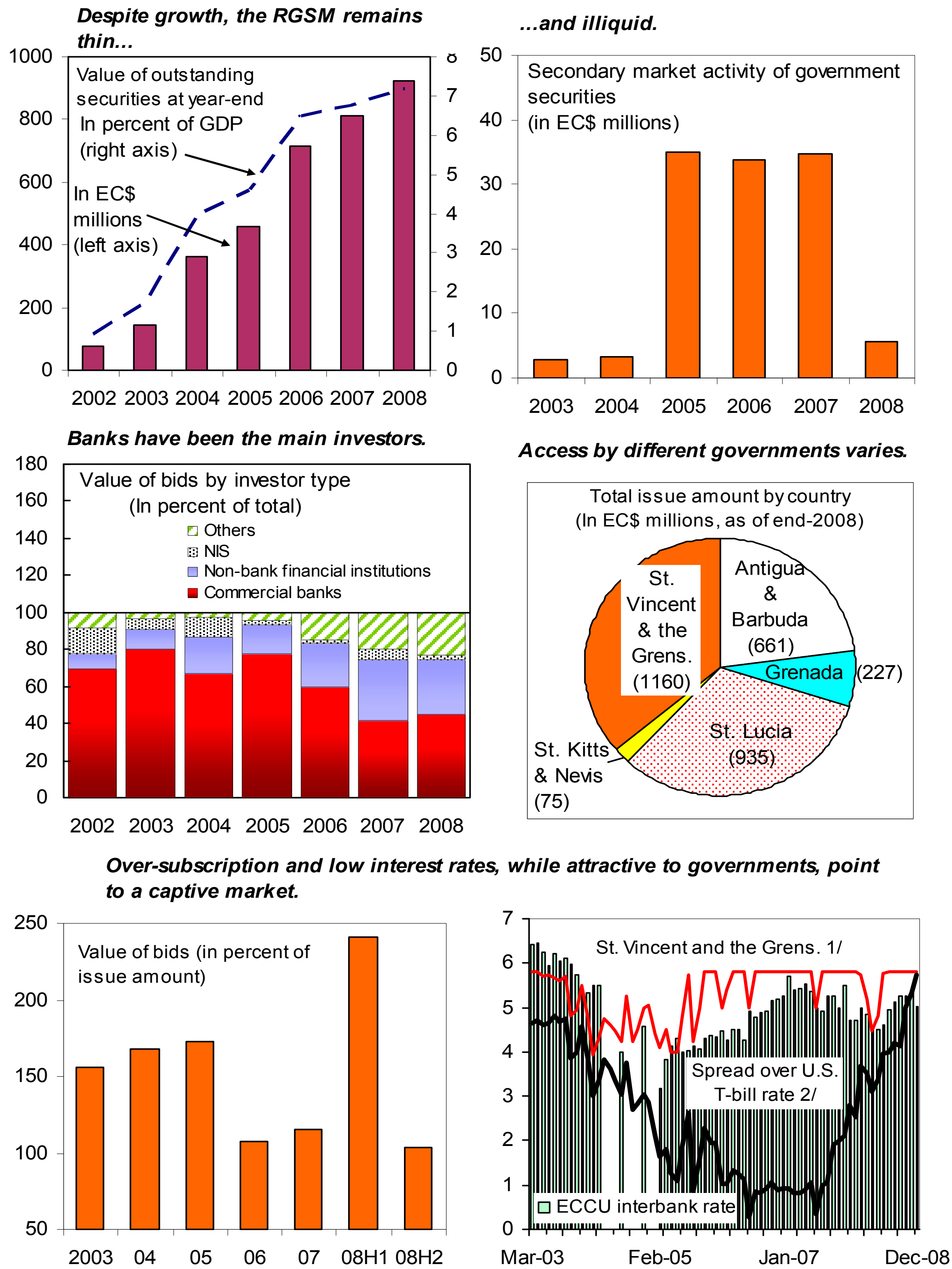
Sources: Country authorities; ECCB; and Fund staff estimates.
1/ A positive (negative) number indicates borrowing from (lending to) foreigners.

Figure 14. Eastern Caribbean Securities Exchange



Sources: Eastern Caribbean Securities Exchange (ECSE); Caribbean Trade and nvestment Report 2005; and Fund staff estimates.
1/ Size of bubble indicates country GDP in millions of U.S. dollars.

Figure 15. ECCU: Regional Government Securities Market, 2002–08

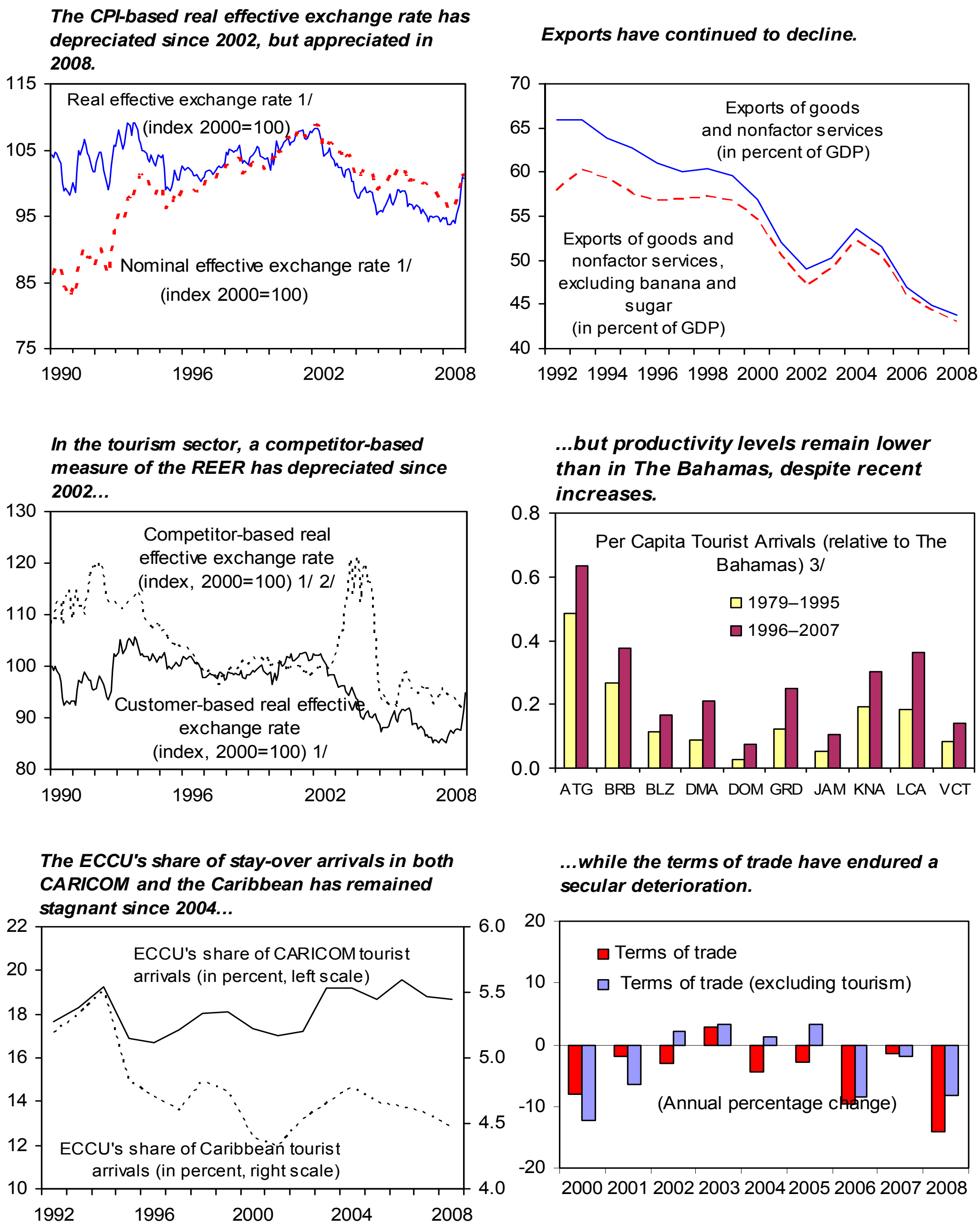


Sources: ECCB and ECSE.

1/ Interest rates on 3-month treasury bills by St. Vincent and the Grenadines. Interpolated rates for March and May 2004.

2/ Spreads on St. Vincent and the Grenadines 3-month treasury bills over U.S. interest rate on 13-week treasury bills.

Figure 16. ECCU: External Competitiveness, 1990–2008



Sources: ECCB; Caribbean Tourism Organization; Country authorities; World Travel and Tourism Council; and Fund staff estimates.

Note: Antigua and Barbuda (ATG), Barbados (BRB), Belize (BLZ), Dominica (DMA), Dominican Republic (DOM), Grenada (GRD), Jamaica (JAM), St. Kitts and Nevis (KNA), St. Lucia (LCA), and St. Vincent and the Grenadines (VCT).

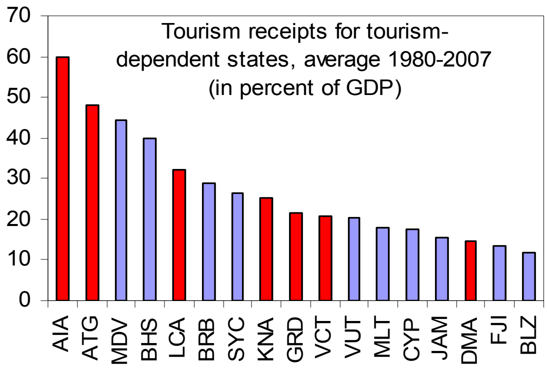
1/ An increase (decrease) indicates an appreciation (depreciation).

2/ The sharp movements in the competitor-based real exchange rate in 2002–04 were largely driven by the Dominican Republic's peso.

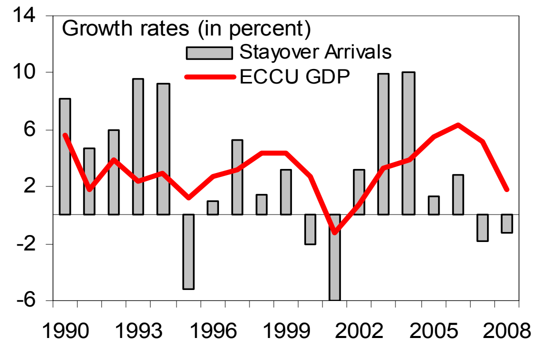
3/ A value below 1 indicates that the country's tourism sector is less productive than that of The Bahamas.

Figure 17. Tourism Performance

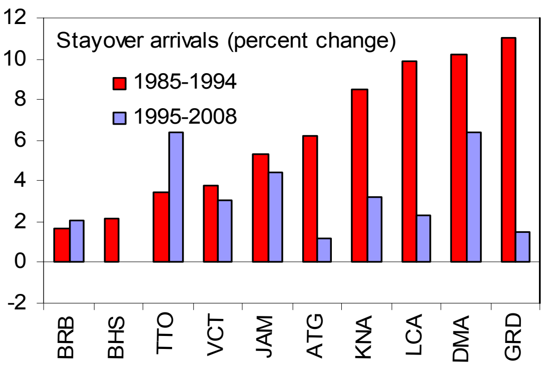
ECCU countries are among the most tourism-dependent economies in the world...



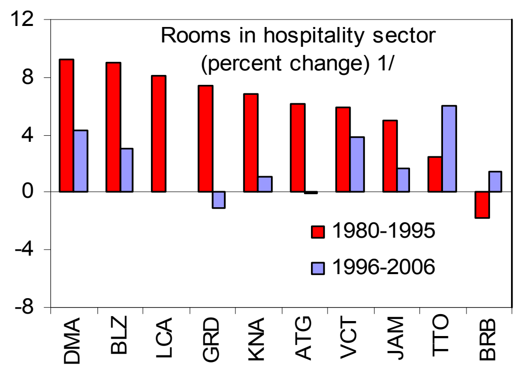
..with tourism arrivals being highly correlated with economic performance.



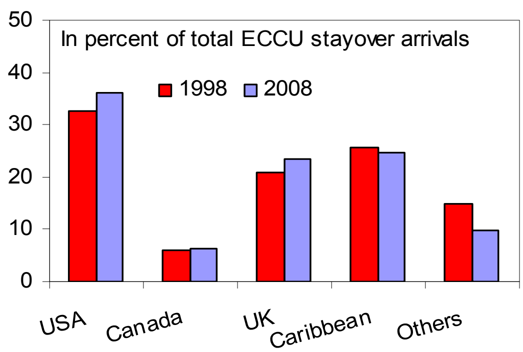
Growth in stayover arrivals to the ECCU has declined markedly in the last decade...



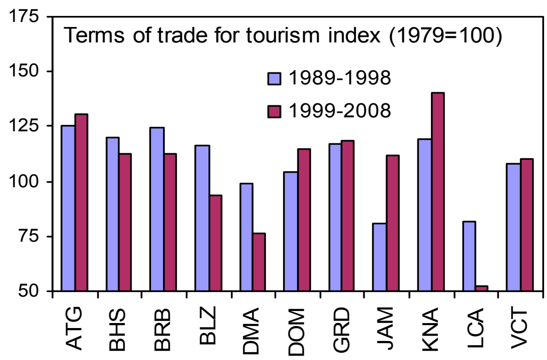
..due in part to declining growth in accommodation capacity.



The U.S. has remained the top source for tourists to the ECCU.

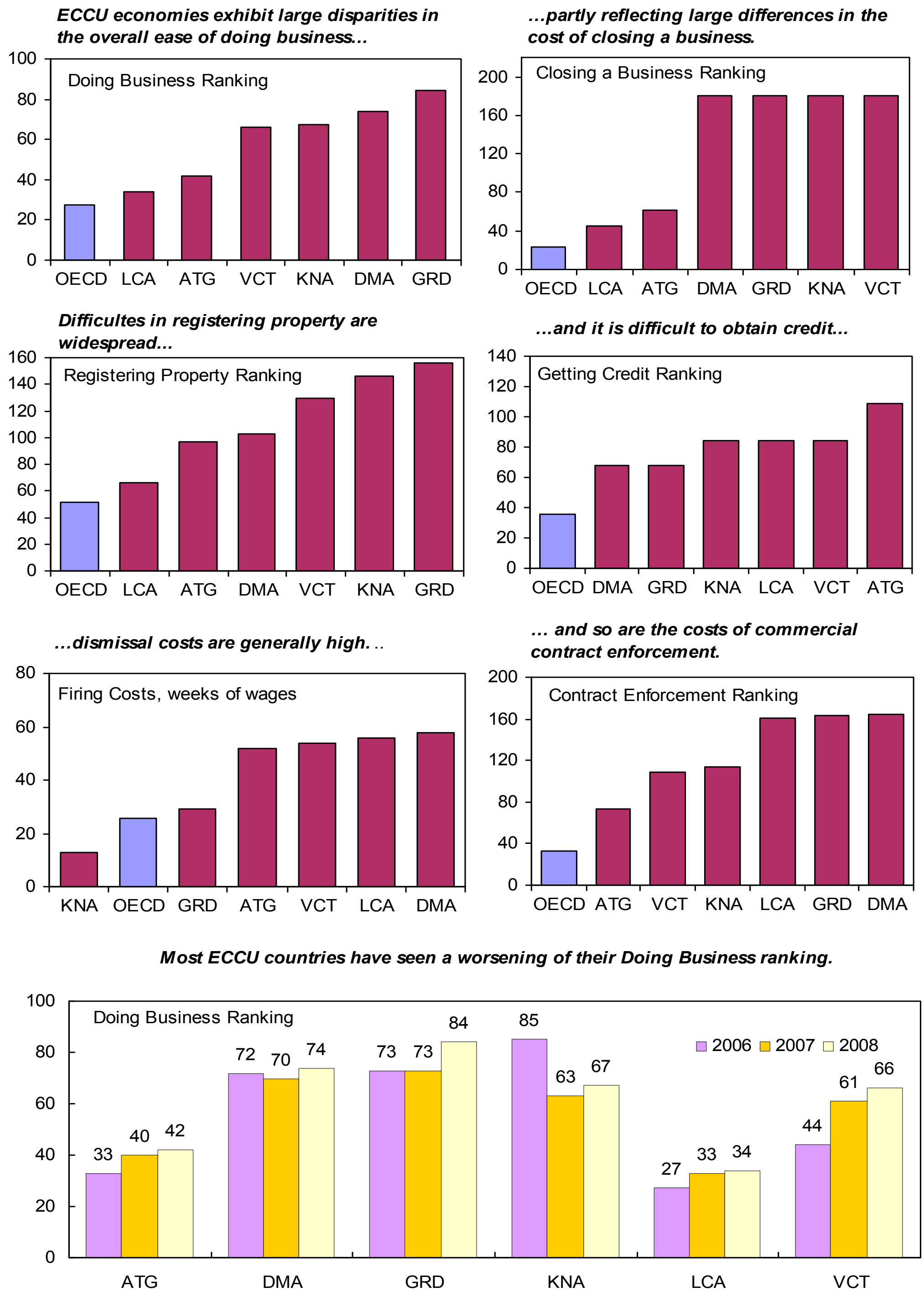


The terms of trade for tourism dropped significantly for some ECCU destinations.



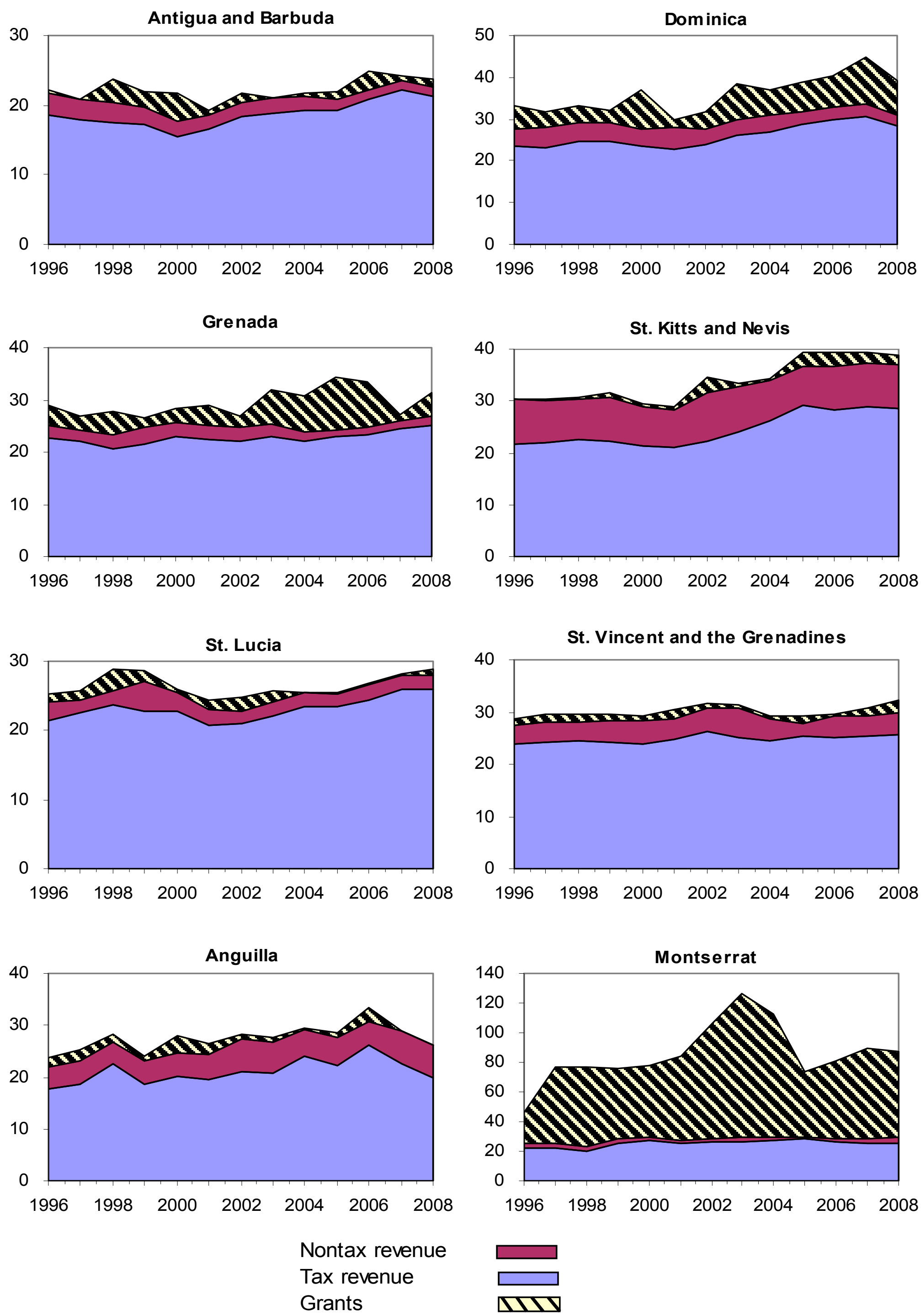
Sources: Country authorities; ECCB; and Fund staff estimates.
1/ Grenada's infrastructure was damaged in 2004 due to Hurricane Ivan.
Note: Antigua and Barbuda (ATG), Aruba (ABW), Bahamas (BHS), Barbados (BRB), Belize (BLZ), Cayman Islands (CYM), Croatia (HRV), Cyprus (CYP), Dominica (DMA), Dominican Republic (DOM), Fiji (FJI), Grenada (GRD), Jamaica (JAM), Maldives (MDV), Malta (MLT), St. Kitts and Nevis (KNA), St. Lucia (LCA), St. Vincent and the Grenadines (VCT), Seychelles (SYC), Trinidad and Tobago (TTO), Vanuatu (VUT).

Figure 18. ECCU: Doing Business Indicators, 2008 1/



Sources: World Bank, *2009 Doing Business Indicators* (2008); and Fund staff calculations.
1/ Smaller numbers represent greater ease in doing business. The 2008 rankings are across 181 countries.
Note: Antigua and Barbuda (ATG), Dominica (DMA), Grenada (GRD), St. Kitts and Nevis (KNA), St. Lucia (LCA), and St. Vincent and the Grenadines (VCT).

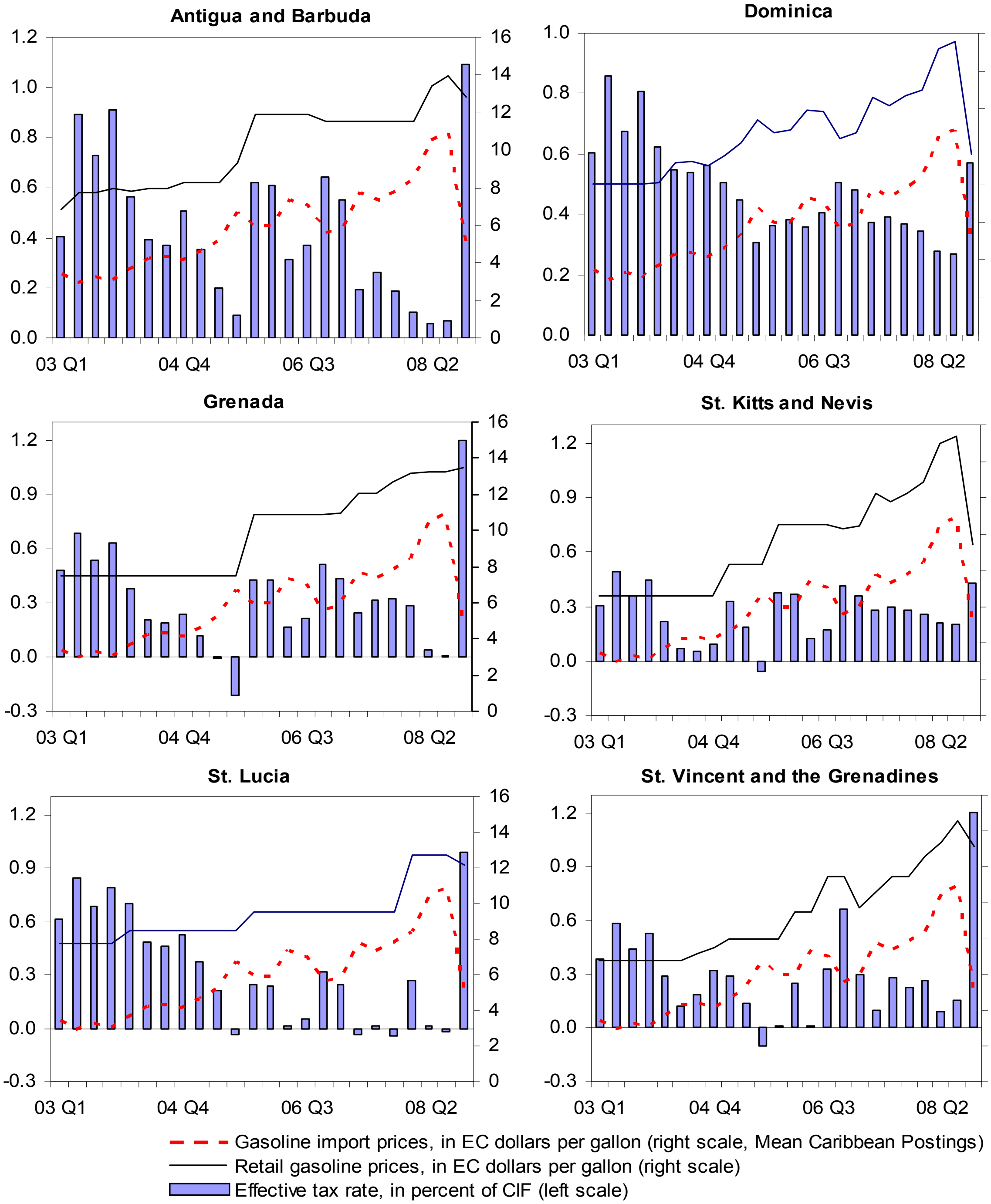
Figure 19. ECCU: Fiscal Revenue, 1996–2008
(In percent of GDP)



Sources: ECCB; Country authorities; and Fund staff calculations.

Figure 20. ECCU: Effective Gasoline Tax Rate, Gasoline Import and Retail Prices, 2003–08

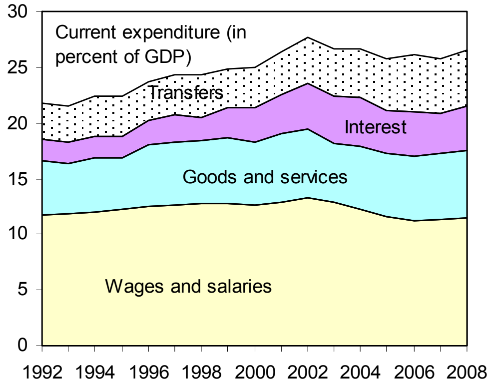
Failure to adjust retail prices to world oil price developments implies large fiscal costs.



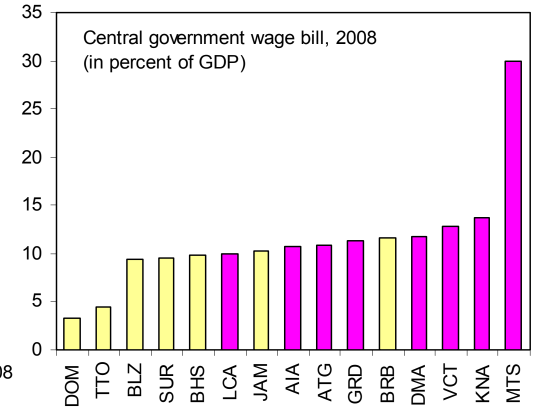
Sources: ECCB; and Fund staff estimates.

Figure 21. ECCU: Fiscal Expenditure

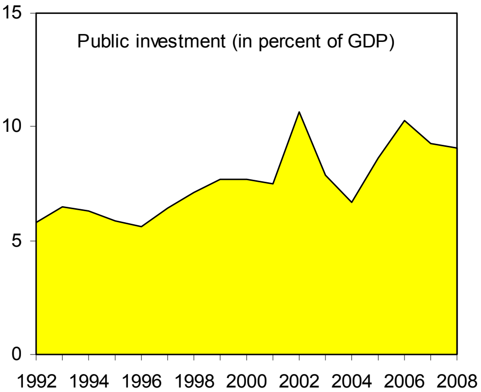
Current expenditure on goods and services, transfers, and interest payments have increased over the years.



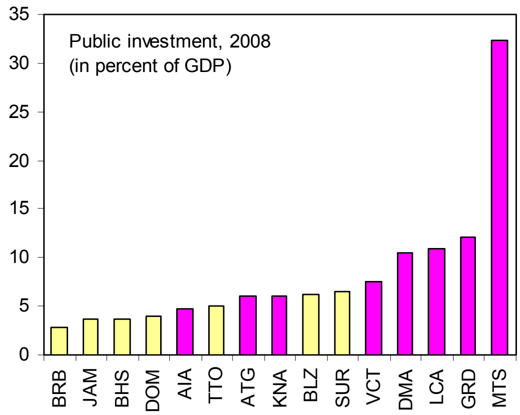
ECCU wage bills are large relative to other Caribbean countries.



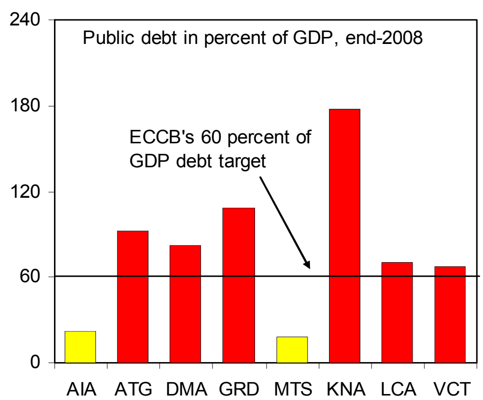
Public investment has also risen over the years...

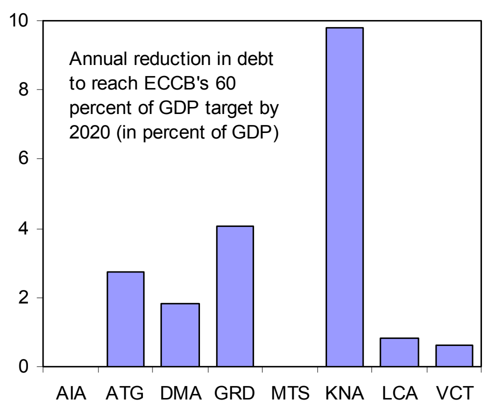


... and is large relative to other Caribbean countries.



Reducing high debt burdens will require a sustained effort in restraining expenditure.





Sources: World Economic Outlook; Country authorities; and Fund staff calculations.
Note: Anguilla (AIA), Antigua and Barbuda (ATG), Bahamas (BHS), Barbados (BRB), Belize (BLZ), Dominica (DMA), Dominican Republic (DOM), Grenada (GRD), Guyana (GUY), Haiti (HTI), Jamaica (JAM), Montserrat (MTS), St. Kitts and Nevis (KNA), St. Lucia (LCA), St. Vincent and the Grenadines (VCT), Suriname (SUR), Trinidad and Tobago (TTO).

Appendix Table 1. ECCU: Public Sector Debt Sustainability Framework, 2004–14
(In percent of GDP, unless otherwise indicated)

		Actual					Projections						
		2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	**Debt-stabilizing primary balance 1/**
1	**Baseline: Public sector debt 2/**	**107.3**	**100.5**	**98.4**	**94.5**	**90.6**	**97.9**	**103.8**	**106.8**	**108.4**	**109.3**	**110.3**	**-1.3**
	Of which : Foreign-currency denominated	62.1	53.9	50.9	47.4	46.0	50.1	53.3	54.7	55.4	54.9	55.4	
2	Change in public sector debt	2.9	-6.9	-2.0	-4.0	-3.9	7.3	5.9	3.0	1.6	0.9	1.0	
3	Identified debt-creating flows (4+7+12)	-1.9	-4.5	-3.3	-3.6	-1.6	5.9	4.4	1.4	0.3	-0.1	0.1	
4	Primary deficit	-0.1	0.5	1.1	0.8	0.7	2.2	2.2	1.5	1.4	1.3	1.4	
5	Revenue and grants	29.0	29.9	31.3	30.7	31.0	28.9	29.0	28.9	29.1	29.1	29.0	
6	Primary (noninterest) expenditure	28.9	30.4	32.4	31.5	31.7	31.2	31.2	30.3	30.5	30.4	30.5	
7	Automatic debt dynamics 3/	-1.8	-5.0	-4.4	-4.4	-2.3	3.7	2.2	-0.1	-1.0	-1.4	-1.3	
8	Contribution from interest rate/growth differential 4/	-1.8	-5.0	-4.4	-4.4	-2.3	3.7	2.2	-0.1	-1.0	-1.4	-1.3	
9	*Of which* : Contribution from real interest rate	2.0	0.5	1.4	0.3	-0.6	1.6	2.1	2.1	2.5	2.6	2.9	
10	*Of which* : Contribution from real GDP growth	-3.8	-5.5	-5.8	-4.7	-1.6	2.1	0.1	-2.2	-3.5	-4.0	-4.2	
11	Contribution from exchange rate depreciation 5/	0.0	0.0	0.0	0.0	0.0	...	...	...	...	...	...	
12	Other identified debt-creating flows	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
13	Privatization receipts (negative)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
14	Recognition of implicit or contingent liabilities	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
15	Other (specify, e.g., bank recapitalization)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
16	Residual, including asset changes (2–3) 6/	4.8	-2.4	1.3	-0.4	-2.3	1.4	1.5	1.6	1.3	1.0	0.9	
	Public sector debt-to-revenue ratio 2/	369.9	336.0	314.4	307.7	292.4	338.6	358.0	370.0	372.0	375.3	380.0	
	Gross financing need 7/	**8.5**	**9.8**	**13.4**	**10.9**	**8.8**	**11.3**	**10.9**	**10.1**	**9.7**	**9.5**	**10.1**	
	in billions of U.S. dollars	0.3	0.4	0.5	0.5	0.4	0.5	0.5	0.5	0.5	0.6	0.6	
	Scenario with key variables at their historical averages 8/						**97.9**	**99.7**	**101.5**	**103.1**	**104.4**	**105.5**	**-1.4**
	Scenario with no policy change (constant primary balance) in 2009–14						**97.9**	**103.8**	**107.6**	**110.2**	**112.1**	**113.9**	**-1.3**
	Scenario with natural disaster 9/						**97.9**	**105.9**	**113.1**	**121.6**	**124.3**	**127.1**	**1.5**
	Key Macroeconomic and Fiscal Assumptions Underlying Baseline												
	Real GDP growth (in percent)	3.9	5.6	6.3	5.2	1.8	-2.4	-0.1	2.2	3.5	3.9	4.1	
	Average nominal interest rate on public debt (in percent) 10/	4.5	4.0	4.4	4.0	4.4	5.1	4.9	4.8	5.0	5.0	5.2	
	Average real interest rate (nominal rate minus change in GDP deflator, in percent)	2.1	0.6	1.7	0.5	-0.6	1.7	2.2	2.2	2.5	2.7	2.9	
	Nominal appreciation (increase in US dollar value of local currency, in percent)	0.0	0.0	0.0	0.0	0.0	...	...	...	...	...	...	
	Inflation rate (GDP deflator, in percent)	2.4	3.3	2.7	3.5	5.1	3.4	2.7	2.6	2.5	2.3	2.3	
	Growth of real primary spending (deflated by GDP deflator, in percent)	0.5	11.3	13.9	2.5	1.9	-3.7	0.3	-0.6	4.0	3.5	4.3	
	Primary deficit	-0.1	0.5	1.1	0.8	0.7	2.2	2.2	1.5	1.4	1.3	1.4	

1/ Assumes that key variables (real GDP growth, real interest rate, and other identified debt-creating flows) remain at the level of the last projection year.
2/ Gross central government and government-guaranteed debt.
3/ Derived as $[(r - \pi(1+g) - g + \alpha\varepsilon(1+r)]/(1+g+\pi+g\pi))$ times previous period debt ratio, with r = interest rate; π = growth rate of GDP deflator; g = real GDP growth rate; α = share of foreign-currency denominated debt; and ε = nominal exchange rate depreciation (measured by increase in local currency value of U.S. dollar).
4/ The real interest rate contribution is derived from the denominator in footnote 2/ as $r - \pi(1+g)$ and the real growth contribution as -g.
5/ The exchange rate contribution is derived from the numerator in footnote 2/ as $\alpha\varepsilon(1+r)$.
6/ For projections, this line includes exchange rate changes.
7/ Defined as public sector deficit, plus amortization of medium and long-term public sector debt, plus short-term debt at end of previous period.
8/ The key variables include real GDP growth; real interest rate; and primary balance in percent of GDP.
9/ Assuming that a hurricane hits half of ECCU countries, increasing their primary deficit by three percent of GDP for 2009–11 and reducing growth to zero.
10/ Derived as nominal interest expenditure divided by previous period debt stock.

Appendix Table 2. ECCU: External Debt Sustainability Framework, 2004–14
(In percent of GDP, unless otherwise indicated)

		Actual					Projections						
		2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	**Debt-stabilizing noninterest current account 1/**
1	**Baseline: External debt 2/**	**62.6**	**54.2**	**51.1**	**47.7**	**46.1**	**50.3**	**53.7**	**55.2**	**55.8**	**55.3**	**55.8**	**-20.7**
2	Change in external debt	-0.6	-8.4	-3.1	-3.4	-1.6	4.2	3.4	1.4	0.6	-0.5	0.4	
3	Identified external debt-creating flows (4+8+9)	-4.9	-9.0	-5.5	-1.5	3.9	5.0	2.3	0.0	-1.1	-1.5	-1.7	
4	Current account deficit, excluding interest payments	13.8	20.3	27.7	32.9	31.9	22.2	22.1	22.9	22.6	20.7	17.8	
5	Deficit in balance of goods and services	13.8	20.7	28.4	32.9	32.7	22.7	22.8	23.8	23.7	22.1	19.7	
6	Exports	53.5	51.1	46.6	44.9	42.8	36.1	36.9	40.4	42.2	45.4	50.5	
7	Imports	67.4	71.8	75.0	77.8	75.5	58.8	59.7	64.2	65.8	67.5	70.2	
8	Net nondebt creating capital inflows (negative)	-17.5	-26.2	-30.6	-32.2	-26.8	-20.3	-22.0	-23.9	-24.0	-22.1	-19.3	
9	Automatic debt dynamics 3/	-1.2	-3.2	-2.5	-2.2	-1.2	3.2	2.2	1.0	0.4	0.0	-0.1	
10	Contribution from nominal interest rate	2.6	2.0	2.0	2.0	1.9	2.1	2.2	2.1	2.1	2.1	2.0	
11	Contribution from real GDP growth	-2.3	-3.2	-3.1	-2.4	-0.8	1.1	0.0	-1.1	-1.8	-2.1	-2.1	
12	Contribution from price and exchange rate changes 4/	-1.5	-2.0	-1.4	-1.7	-2.3	...	...	...	...	...	...	
13	Residual, incl. change in gross foreign assets (2–3) 5/	4.3	0.6	2.4	-1.9	-5.5	-0.8	1.1	1.5	1.7	1.0	2.1	
	External debt-to-exports ratio (in percent)	117.0	106.0	109.6	106.1	107.7	139.3	145.7	136.5	132.4	121.9	110.3	
	Gross external financing need (in billions of US dollars) 6/	**0.8**	**1.3**	**1.4**	**1.8**	**1.8**	**1.4**	**1.4**	**1.5**	**1.5**	**1.5**	**1.4**	
	In percent of GDP	23.6	34.1	33.3	40.5	37.8	28.8	28.0	28.6	28.1	25.9	22.8	
	Scenario with key variables at their historical averages 7/						**50.3**	**50.6**	**51.3**	**52.3**	**52.4**	**53.6**	**-23.0**
	Scenario with natural disaster 8/						**50.3**	**58.2**	**63.9**	**68.3**	**66.6**	**66.0**	**-21.9**
	Scenario with FDI at historical average minus one standard deviation						**50.3**	**60.0**	**69.7**	**78.5**	**77.5**	**77.4**	**-21.2**
	Key Macroeconomic Assumptions Underlying Baseline												
	Real GDP growth (in percent)	3.9	5.6	6.3	5.2	1.8	-2.4	-0.1	2.2	3.5	3.9	4.1	
	GDP deflator in US dollars (change in percent)	2.4	3.3	2.7	3.5	5.1	3.4	2.7	2.6	2.5	2.3	2.3	
	Nominal external interest rate (in percent)	4.3	3.6	4.0	4.2	4.3	4.6	4.4	4.2	4.1	3.9	3.8	
	Growth of exports (US dollar terms, in percent)	14.4	4.7	0.3	4.9	1.8	-14.8	4.7	15.0	10.5	14.5	18.5	
	Growth of imports (US dollar terms, in percent)	5.6	16.9	14.8	13.0	3.7	-21.4	4.0	13.0	8.6	9.1	10.6	
	Current account balance, excluding interest payments	-13.8	-20.3	-27.7	-32.9	-31.9	-22.2	-22.1	-22.9	-22.6	-20.7	-17.8	
	Net nondebt creating capital inflows	17.5	26.2	30.6	32.2	26.8	20.3	22.0	23.9	24.0	22.1	19.3	

1/ Long-run, constant balance that stabilizes the debt ratio assuming that key variables (real GDP growth, nominal interest rate, dollar deflator growth, and non-debt inflows in percent of GDP) remain at their levels of the last projection year.

2/ Defined as nonfinancial public sector debt. Information on private sector external borrowing is unavailable.

3/ Derived as $[r - g - \rho(1+g) + \varepsilon\alpha(1+r)]/(1+g+\rho+g\rho)$ times previous period debt stock, with r = nominal effective interest rate on external debt; ρ = change in domestic GDP deflator in US dollar terms, g = real GDP growth rate, ε = nominal appreciation (increase in dollar value of domestic currency), and α = share of domestic-currency denominated debt in total external debt.

4/ The contribution from price and exchange rate changes is defined as $[-\rho(1+g) + \varepsilon\alpha(1+r)]/(1+g+\rho+g\rho)$ times previous period debt stock. ρ increases with an appreciating domestic currency ($\varepsilon > 0$) and rising inflation (based on GDP deflator).

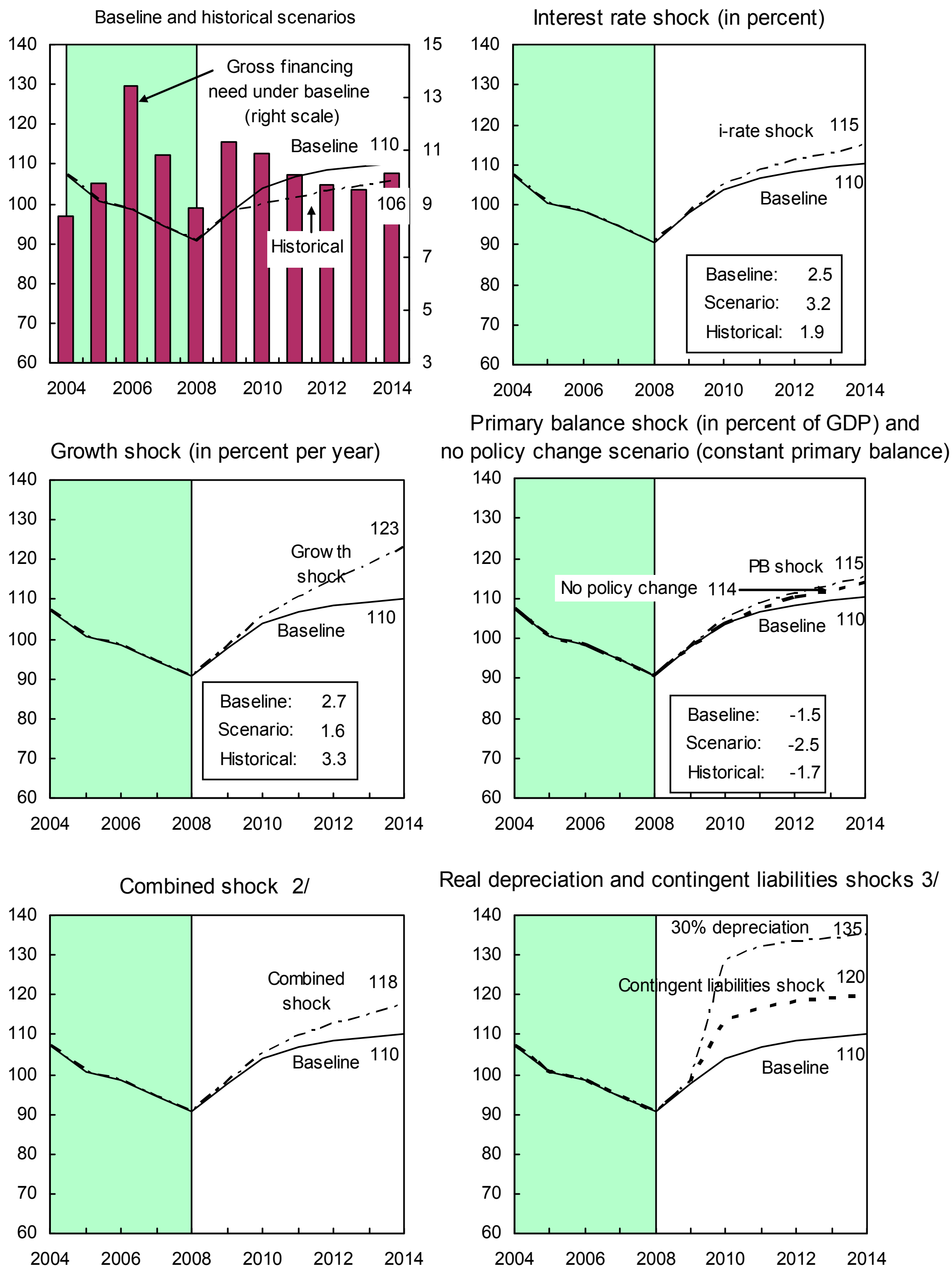
5/ For projection, line includes the impact of price and exchange rate changes.

5/ Defined as current account deficit, plus amortization on medium- and long-term debt, plus short-term debt at end of previous period.

7/ The key variables include real GDP growth; nominal interest rate; dollar deflator growth; and both noninterest current account and nondebt inflows in percent of GDP.

8/ Natural disaster impacting half of the ECCU countries, increasing the regional CA deficit by 4 percent of GDP in 2009–11, and reducing growth by an average of 1.6 percentage points for the same period. These parameters are taken from the median impact of 12 large natural disasters in the ECCU (Rasmussen, WP/04/224).

Appendix Figure 1. ECCU: Public Debt Sustainability: Bound Tests 1/
(Public debt in percent of GDP)



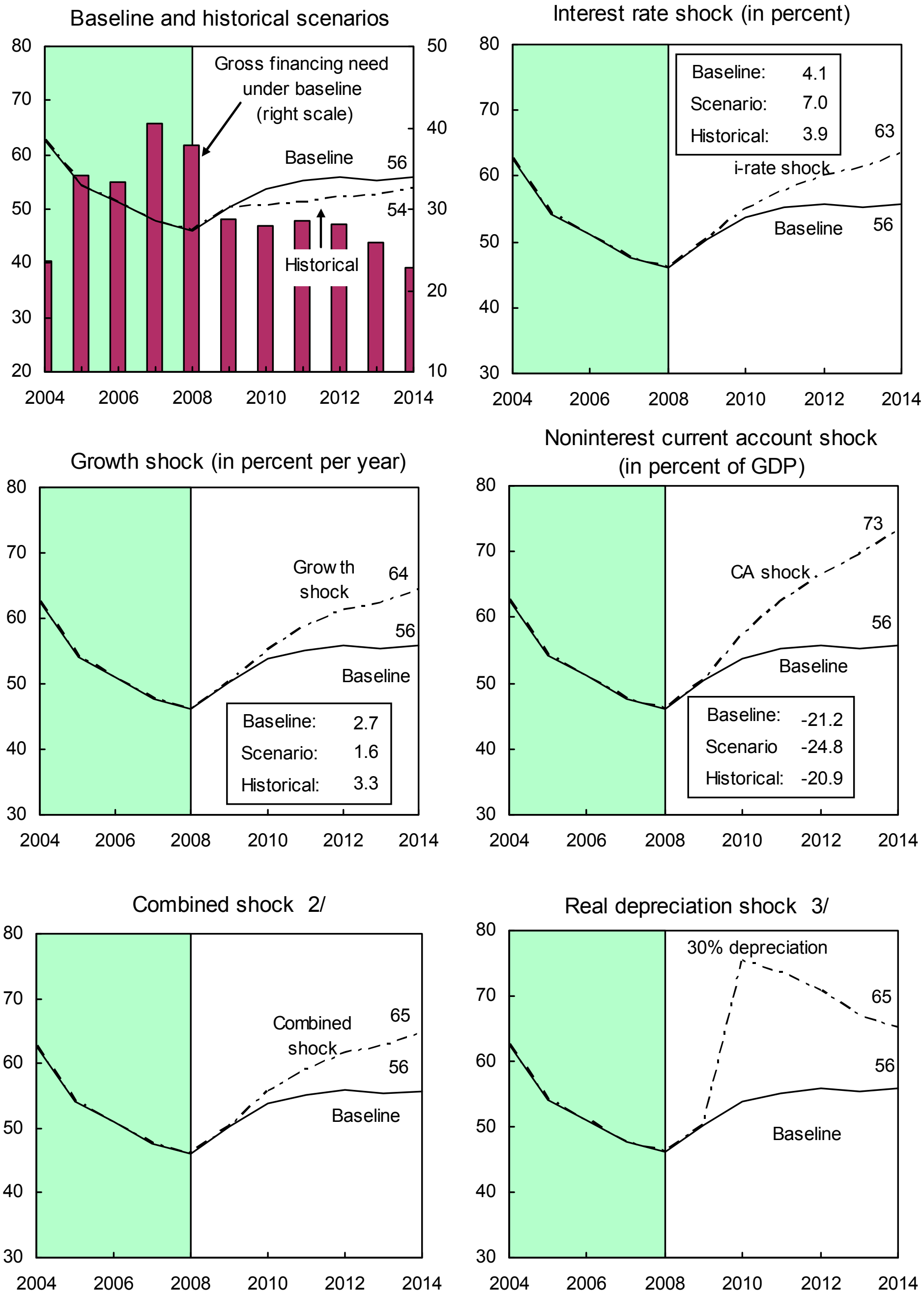
Sources: Country Authorities; and Fund staff estimates.

1/ Shaded areas represent actual data. Individual shocks are permanent one-half standard deviation shocks. Figures in the boxes represent average projections for the respective variables in the baseline and scenario being presented. Ten-year historical average for the variable is also show n.

2/ Permanent 1/4 standard deviation shocks applied to real interest rate, grow th rate, and primary balance.

3/ One-time real depreciation of 30 percent and 10 percent of GDP shock to contingent liabilities occur in 2010, w ith real depreciation defined as nominal depreciation (measured by percentage fall in dollar value of local currency) minus domestic inflation (based on GDP deflator).

Appendix Figure 2. ECCU: External Debt Sustainability: Bound Tests 1/
(External debt in percent of GDP)



Sources: Country Authorities, and Fund staff estimates.

1/ Shaded areas represent actual data. Individual shocks are permanent one-half standard deviation shocks. Figures in the boxes represent average projections for the respective variables in the baseline and scenario being presented. Ten-year historical average for the variable is also shown.

2/ Permanent 1/4 standard deviation shocks applied to real interest rate, growth rate, and current account balance.

3/ One-time real depreciation of 30 percent occurs in 2010.

ANNEX I. SUMMARY OF APPENDICES

The full appendices to this report are issued as a supplement.

Fund relations. The Eastern Caribbean Currency Union consists of eight members that have a common currency, monetary policy, and exchange system. The common currency, the EC dollar, has been pegged to the U.S. dollar at the rate of EC$2.70 since July 1976. The region has a common central bank, the Eastern Caribbean Central Bank (ECCB), which has operated like a quasi-currency board, maintaining foreign exchange backing of its currency and demand liabilities at close to 100 percent. The exchange system is free of restrictions on the making of payments and transfers for current international transactions. A safeguards assessment was completed in 2007, and concluded that the ECCB continues to have appropriate control mechanisms in place.

Relations with the World Bank Group. The Eastern Caribbean Sub-Region country assistance strategy (CAS) for FY 2006−09 supports the region's development through: (i) stimulating growth and improving competitiveness; and (ii) reducing vulnerability. Efforts in the area of growth are focused on a series of analytical and advisory activities. On reducing vulnerability, the Bank has facilitated the establishment and participation of OECS countries in the Caribbean Catastrophic Risk Insurance Facility. It has also provided financial support for improvements in the efficacy and targeting of social safety nets in the OECS. The FY 2006–09 CAS proposes a total lending envelope of US$103 million. The CAS for FY 2010−13 is expected to be presented to the Board of the World Bank in early 2010.

Relations with the Caribbean Development Bank (CDB). Between 1970–2008, the CDB approved loans of US$1,209 million to the ECCU, of which US$915 million has been disbursed as of end-2008. Most of the CDB's interventions in the OECS have been directed toward infrastructural development, related to the incidence of natural disasters in the region as well as the need to ensure infrastructure improvements for productive investments. In 2006, the CDB expanded its range of instruments to include policy-based lending, to support policy reforms and/or institutional changes at the macroeconomy-wide or sectoral level. St. Kitts and Nevis (2007) and St. Lucia (2008) have received policy-based loans in support of their reform programs.

Relations with the Caribbean Regional Technical Assistance Center (CARTAC). CARTAC's core areas of technical Assistance (TA) include public financial management, which includes tax policy and administration; public expenditure management; macroeconomic management and financial programming; financial sector supervision (including supervision of nonbanks); and economic and financial statistics. ECCU countries continue to be among the most active Caribbean countries in requesting TA and training in all of CARTAC's core areas. As in previous years, the largest areas of CARTAC involvement in the ECCU countries have been in value-added tax implementation and in building capacity to undertake improved macroeconomic management. This TA support continues to represent a significant addition to the Fund's TA to the ECCU region.

Annex II. ECCU: Analytical Work

Analytical work by Fund staff has contributed to strengthening public dialogue on key issues in the Eastern Caribbean Currency Union (ECCU).[25] Recent ECCB Monetary Council and national policy discussions have drawn on input from Fund staff, including on the response to preference erosion, monetary policy initiatives, regulation of nonbank financial institutions, and social security reform.[26] The authorities have appreciated the increased emphasis given to regional issues as well as the focus on growth and vulnerabilities—particularly high public debt levels, optimal reserves, and lender-of-last-resort activities of the central bank.

Ongoing Analytical Work (to be published as 2009 *ECCU Selected Issues* chapters and IMF Working Papers in 2008 and 2009):

- A Risk Analysis of Public Debt in the ECCU: A Fan-Chart Approach (2009 *ECCU Selected Issues* chapter)
- Insurance Against Natural Disasters in the Caribbean (2009 *ECCU Selected Issues* chapter)
- Ponzi Schemes in the Caribbean (IMF WP/09/95)
- Assessing Exchange Rate Competitiveness in the Eastern Caribbean Currency Union (IMF WP/09/78)
- Optimal Reserves in the Eastern Caribbean Currency Union (IMF WP/09/77)
- ECCU Business Cycles: Impact of the United States (IMF WP/09/71)
- Financing Universal Health Care: Lessons for the Eastern Caribbean and Beyond (IMF WP/09/61)
- Can the ECCU Afford to Grow Old? (IMF WP/09/38)
- *The Caribbean: Enhancing Economic Integration* (2008 IMF book)
- What Attracts Tourists to Paradise? (IMF WP/08/277)
- Tax Concessions and Foreign Direct Investment in the ECCU (IMF WP/08/257)
- The ECCB: Challenges to an Effective Lender of Last Resort (IMF WP/08/214)
- Measuring the Informal Economy in Latin America and the Caribbean (IMF WP/08/102)
- The Anatomy of Banking Crises (IMF WP/08/93)
- Price Dynamics in the Eastern Caribbean (IMF WP/08/90)
- Corporate Income Tax Competition in the Caribbean (IMF WP/08/77)

[25] Outreach activities traditionally include the presentation of staff's preliminary analytical work to the authorities, civil society, academics and the general public in each of the six Fund-member ECCU countries, the Eastern Caribbean Central Bank (ECCB), and at academic conferences and workshops held in the region.

[26] All Fund papers (published since 2004) on each of the six Fund-member ECCU countries are available on the ECCB website. The link is http://www.eccb-centralbank.org/Publications/imfpapers1.asp .

INTERNATIONAL MONETARY FUND

EASTERN CARIBBEAN CURRENCY UNION

Staff Report for the 2009 Discussion on Common Policies of Member Countries

Informational Annex

Prepared by the Western Hemisphere Department

April 30, 2009

Contents Page

Appendices

Appendix I: ECCU—Relations with the Fund
(As of April 3, 2009)

I. Membership Status: Not Applicable

II. Exchange Arrangement:

The Eastern Caribbean Currency Union (ECCU) comprises six Fund members: Antigua and Barbuda, Dominica, Grenada, St. Kitts and Nevis, St. Lucia, and St. Vincent and the Grenadines; and two territories of the United Kingdom, Anguilla and Montserrat. The eight ECCU members have a common currency, monetary policy, and exchange system. The common currency, the Eastern Caribbean (EC) dollar, has been pegged to the U.S. dollar at the rate of EC$2.70 per U.S. dollar since July 1976. The common central bank, the Eastern Caribbean Central Bank (ECCB), has operated like a quasi-currency board, maintaining foreign exchange backing of its currency and demand liabilities of close to 100 percent.

III. Safeguards Assessment

Under the Fund's safeguards assessment policy, the ECCB is subject to a full safeguards assessment under a four-year cycle. The most recent assessment was completed in July 2007, and concluded that the ECCB continues to have appropriate control mechanisms in place, which have strengthened since the first safeguards assessment completed in 2003. ECCB management places emphasis on good governance and sound controls, and has enhanced the bank's transparency and accountability since the last assessment, including the publications of financial statements that comply with International Financial Reporting Standards. The assessment made some recommendations to sustain the ECCB's safeguards framework going forward.

IV. Report on the Observance of Standards and Codes

The Report on Observance of Standards and Codes—Data Module, was completed for the ECCB in August, 2007, covered monetary statistics of the ECCB, and was published as IMF Country Report No. 07/289 on August 21, 2007.

The Financial System Stability Assessment for the ECCU was completed in April 2004, and examined the adherence of the domestic banking sector to the Basel Core Principles for Effective Banking Supervision.

In domestic banking supervision, assessors noted the need to strengthen the legislative framework to enhance the powers and autonomy of the ECCB and to generally beef up the enforcement process. More frequent and comprehensive on-site examinations are required particularly in light of the high levels of nonperforming loans and perceived gaps in data integrity. Implementation of a risk-based capital framework for banks should be a priority, which adequately reflects risk of public sector loans. Supervisory practices should develop further in the direction of risk-focused supervision that also takes into consideration ongoing communication with external auditors and overseas supervisors. The need to establish a more formal information exchange mechanism with the home supervisor was also identified as a priority, especially with regard to the consolidated supervision of significant regional banking groups.

Some of these concerns have been addressed: new regulatory guidelines for risk-weighting nonperforming public sector exposures went into effect in January 2006, and amendments to the uniform Banking Act have been passed and gazetted in all ECCU jurisdictions. These amendments will give the ECCB enhanced regulatory powers, particularly in regards to implementation of additional regulation and prudential guidelines.

Appendix II. OECS: Relations with the World Bank Group

(As of March 5, 2009)

World Bank Group Strategy

The World Bank Group strategy in the OECS is focused on helping these small states meet the development challenges that face them. The guiding principles of the strategy are: (a) supporting regional integration and coordination efforts; (b) partnering and harmonization in both lending and analytical work with other development partners; and (c) active pursuit of simplification and capacity building initiatives tailored to small states. The Bank will continue to take the lead on public sector reforms with a particular focus on governance, the efficiency of public spending, social expenditures (including safety nets), disaster mitigation, and environmental management.

Bank-Fund collaboration in specific areas: The World Bank Group and the IMF will continue to collaborate on the financial sector, on the medium-term structural reform agenda and in providing technical assistance on macroeconomic management issues jointly with the Caribbean Regional Technical Assistance Center (CARTAC). The Bank and the IMF will also continue to collaborate on supporting the countries of the OECS in the preparation of their Poverty Reduction Strategies (PRS).

Group strategy: The World Bank Group Management presented to its Board the Eastern Caribbean Sub-Region Country Assistance Strategy (CAS), on September 13, 2005. The World Bank Group's strategy for the four years covered by this CAS (FY2006–09) supports the sub-region's development agenda through two main pillars: (1) stimulating growth and improving competitiveness; and (2) reducing vulnerability, by promoting greater social inclusion and strengthening disaster risk management. Recognizing the OECS countries' high debt ratios, Bank activities will focus on leveraging available donor grant financing. Following the recommendations of the recently completed growth and competitiveness study for the OECS, IBRD and IDA assistance would focus on providing technical and financial assistance for interventions to support the two main pillars of the CAS. The CAS proposes a total lending envelope of US$103.4 million. An indicative Base Case lending scenario consists of about US$51.3 million in IDA resources for the four OECS blend countries (Dominica, Grenada, St. Lucia and St. Vincent and the Grenadines). This envelope includes the estimated IDA country allocations for each of the four countries during FY2006–09, and an IDA Regional allocation of US$15.2 million for two regional projects: US$12 million for Catastrophe Risk Insurance and US$3.2 million for Infrastructure and Utilities Reform. The indicative high case lending scenario consists of approximately US$52.1 million in IBRD investments and development policy operation commitments for the six OECS countries, in addition to the base case lending scenarios mentioned above. The Eastern Caribbean Sub-Region Country Assistance Strategy (CAS) for FY2010–13 is expected to be presented to the Board of the World Bank in early 2010.

Increasing competitiveness and reducing vulnerability. In addition to stabilizing macroeconomic conditions and reducing fiscal deficits and public debt levels, the OECS countries are focusing on: (i) improving the investment climate by broadening the tax base, and streamlining the investment incentive regime and making it more transparent; (ii) improving public sector performance, by raising the efficiency of public investment and improving service delivery; (iii) reducing transaction costs, by strengthening regulation and efficiency of public utilities; (iv) promoting appropriate education and skills development to take advantage of new opportunities in the global environment; and (v) reducing vulnerability, by strengthening the social protection mechanisms and strengthening disaster risk management. The OECS authorities also are targeting to expand their positive experiences with sub-regional functional cooperation (e.g., common central bank, telecommunications regulation, pharmaceutical procurement) to other areas including energy sector regulation, as a way of better allocating the region's scarce human and financial resources.

The Bank is supporting these efforts through a comprehensive series of recently completed, ongoing and planned analytical and advisory activities including the following: "Towards a New Agenda for Growth"—OECS growth and competitiveness study (2005); an OECS Skills Enhancement Policy Note (2006); a Caribbean Air Transport Report (2006); a regional study on Crime, Violence, and Development: Trends, Costs, and Policy Options in the Caribbean (2007); an OECS Private Sector Financing Study (2008); the OECS Tourism Backward Linkages Study (2008); the report "Caribbean—Accelerating Trade Integration: Policy Options for Sustained Growth, Job Creation and Poverty Reduction" (2008); a CARICOM study on Managing Nurse Migration (ongoing); and a preparatory study aimed at developing a Caribbean-wide Regional Energy Strategy (ongoing).

Managing volatility: Recent analytical work on macroeconomic vulnerabilities has shown that the frequent natural disasters in the OECS are a major cause of income insecurity and high poverty rates in the sub-region, as many households cycle in and out of poverty in tandem with these events.

Disaster Management. Despite the regularity of natural disasters, the authorities in the OECS have generally pursued reactive policy responses rather than mitigation measures. Given declining aid flows and limited institutional capacity, the countries need to move to proactive responses with greater cooperation between governments, donors and civil society at both the national and the sub-regional levels. The Bank has worked to strengthen mitigation and response planning by providing rapid response assistance to the countries in the aftermath of major catastrophes such as Hurricane Ivan with the Emergency Recovery Program in Grenada. Also, the Bank has facilitated the establishment and participation of OECS countries in the regional Caribbean Catastrophe Risk Insurance Facility **(CCRIF)**, the world's first regional catastrophe risk insurance pool.

Safety Nets. Despite relatively high per capita incomes, unemployment (estimated between 5–20 percent) and poverty levels (ranging 12–38 percent) are quite high in the OECS sub-region. However, current safety nets suffer from a plethora of uncoordinated programs, which lack appropriate targeting mechanisms and adequate coverage. These will need to be improved to address the impact of eroding trade preferences on the rural sector, emerging problems with youth-at-risk, an aging population, continued vulnerability to external shocks, and new vulnerabilities arising from the HIV/AIDS epidemic. Improvements to the efficiency and targeting of social safety nets were examined under the public expenditure reviews. The Bank has provided financial support for an ongoing **Poverty Reduction Fund** in St. Lucia, which has piloted community procurement, a **Social Protection Review** for Dominica (and technical assistance to improve social protection), and an **IDF grant** to strengthen poverty measurement in the OECS. A **Caribbean Regional HIV/AIDS** program, including Grenada, St. Kitts and Nevis, St. Lucia, and St. Vincent and the Grenadines is being implemented. The current global crisis has further augmented the needs for improving social safety nets in the region. As part of its response to the global crisis, the Bank has also started new discussions with the governments in the region to strengthen the social safety nets through improved targeting, effectiveness and coverage.

Planned Operations

The Eastern Caribbean Sub-Region Country Assistance Strategy (CAS) ends on June 30, 2009. There is presently only one regional project in preparation, namely the OECS Electricity Regulator Project. It will assist the governments of the region to enhance the efficiency of electricity provision by among other things establishing a regional electricity regulator and thus promoting a regional approach and solutions to the structural challenges. There are plans to continue to roll out the OECS Skills Enhancement for Inclusive Growth Project to Dominica and St. Vincent and the Grenadines which had previously expressed interest for the project, the objective of which is to assist the governments of the region to increase the employability of youth through the establishment of a competitive training fund for financing demand-driven training and traineeships. Other operations focused on disaster vulnerability reduction and mitigating the poverty and social impacts of the global economic crisis are also planned.

Financial Relations
(In millions of U.S. dollars)

Operations	Original Principal	Disbursed 1/	Undisbursed 1/
OECS-Telecom. and ICT Development Project (DMA,GRD,LCA,KNA,VCT)	2.70	1.36	1.52
OECS-HIV/AIDS Prevention and Control (GRD,LCA,KNA,VCT)	20.72	13.15	10.18
OECS-Education Development Project (GRD,KNA,VCT)	18.94	12.04	8.50
OECS-Catastrophe Insurance (DMA,GRD,LCA,VCT)	14.20	11.13	3.76
OECS E govt. for Regional Integration Project (DMA,GRD,LCA)	7.20	0.00	6.63
Total (regional projects)	**63.76**	**37.68**	**30.59**
Total (all projects)	**110.87**	**52.49**	**54.37**
Dominica			
OECS-Catastrophe Insurance	4.50	3.18	1.21
Growth and Social Protection Technical Assistance Credit	1.45	0.56	0.95
OECS-Telecommunications and ICT Development Project	0.54	0.26	0.33
OECS E govt. For Regional Integration Project	2.40	0.00	2.21
Total	**8.89**	**4.00**	**4.70**
Grenada			
Hurricane Ivan Emergency Project	19.77	9.80	5.95
OECS-Telecommunications and ICT Development Project	0.54	0.26	0.30
OECS-Education Development Project	9.90	5.77	3.21
HIV/AIDS Prevention and Control	4.64	2.31	2.95
OECS-Catastrophe Insurance	4.50	3.55	0.84
Public Sector Modernization Technical Assistance Credit	3.50	0.75	2.93
Grenada Technical Assistance Credit	1.86	0.00	1.77
OECS E govt. For Regional Integration Project	2.40	0.00	2.21
OECS Skills for Inclusive Growth	3.00	0.00	3.12
Total	**50.11**	**22.44**	**23.28**
St. Lucia			
OECS-Catastrophe Insurance	4.50	3.18	1.21
OECS-Skills for Inclusive Growth	3.50	0.25	3.49
OECS-Telecommunications and ICT Development Project	0.54	0.25	0.30
OECS-HIV/AIDS Prevention and Control	6.40	4.82	1.91
Disaster Management Project II	10.50	4.38	5.88
OECS E govt. For Regional Integration Project	2.40	0.00	2.21
Total	**27.84**	**12.88**	**15.00**

Financial Relations (continued)
(In millions of US dollars)

Operations	Original Principal	Disbursed 1/	Undisbursed 1/
St. Kitts and Nevis			
OECS -Telecommunications and ICT Development	0.54	0.25	0.27
OECS-Education Development Project	5.00	4.16	0.84
OECS-HIV/AIDS Prevention and Control	4.05	2.84	1.21
Total	**9.59**	**7.25**	**2.32**
St. Vincent and the Grenadines			
OECS-Catastrophe Insurance	0.70	0.57	0.12
OECS-Telecommunications and ICT Development Project	0.54	0.25	0.30
OECS-Education Development Project	6.20	1.92	4.53
OECS-HIV/AIDS Prevention and Control	7.00	3.18	4.12
Total	**14.44**	**5.92**	**9.07**

Note: DMA denotes Dominica, GRD denotes Grenada, KNA denotes St. Kitts and Nevis; LCA denotes St. Lucia, and VCT denotes St. Vincent and the Grenadines.

1/ Amounts may not add up to Original Principal due to changes in the SDR/US dollar exchange rate since signing.

Disbursements and Debt Service
(In millions of US dollars, fiscal year ending June 30)

	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009*
Total disbursements	8.84	6.08	9.43	26.56	13.75	15.25	20.72	31.14	20.98	7.15
Repayments	0.73	1.10	1.23	2.27	3.06	3.64	4.72	6.38	8.6	6.52
Net disbursements	8.11	4.97	8.20	24.29	10.69	11.62	16.00	24.73	12.37	0.96
Charges and fees	0.05	0.72	1.44	2.01	2.22	2.52	2.70	3.04	3.54	2.34

Note: Data as of March 6, 2009.

Appendix III. Caribbean Development Bank: Overview of Activities in the ECCU

The Caribbean Development Bank (CDB) has as one of its core mandates, the mobilization of resources to finance projects and programs that contribute to the development of its 18 borrowing member countries. In this regard, the CDB has played an important role in the development of the countries of the Eastern Caribbean Currency Union (ECCU). Since inception, the CDB has approved approximately US$3.3 billion to its borrowing member countries, with the OECS as a whole accounting for approximately 34.2 percent. To date, most of the CDB's interventions in the ECCU have been in infrastructural development, and is in part directly related to the incidence of natural disasters in the region, and the need to ensure adequate infrastructure support for investments in tourism and other productive sectors. Resources approved for physical and social infrastructure have, on average, accounted for 59 percent of overall lending to the sub-region, and comprised mainly of upgrading transportation and communication, educational services, power and energy, and housing. Interventions in the productive sectors account for 17.4 percent of total activity, and have focused largely on manufacturing and agriculture. Multisectoral interventions have also been an important element of the CDB's activities in the ECCU and may take the form of *inter alia* natural hazard management, lines of credit, improving social and living conditions through the Basic Needs Trust Fund (BNTF), and activities of the Caribbean Technological Consultancy Services (CTCS) Unit (which provides technical assistance to the private sector, institutional strengthening of government departments, feasibility studies, and the assessment and implementation of transactions-based taxes). In 2006, this category was expanded to include policy-based lending (PBL), which supports policy reforms and/or institutional changes, either at the macro-level or in a sector or sub-sector. Multisectoral interventions to date represented 23.6 percent of all interventions to the sub-region.

St. Lucia has been the largest recipient of CDB financing in the ECCU, accounting for approximately 25.6 percent of approvals to the sub-group. Most of the projects currently underway in St. Lucia are in the areas of physical and social infrastructure development, with interventions to improve the water supply, road rehabilitation, natural disaster mitigation and solid waste management (which forms part of a wider OECS solid waste management programme). Within the productive sectors, CDB has been involved mainly in tourism and stimulating the recovery of banana production. In 2008, the CDB approved a US$30 million PBL to St. Lucia in support of government's reform programme. The loan was to assist the Government of St. Lucia in its preventative strategy to reinforce and strengthen fiscal performance; to insulate the country as much as possible from the inherent risk associated with its openness; and to improve its responsiveness, should the risks be realized. St. Lucia also received a US$12 million loan to enhance the provision of education services, and grants totaling US$2.8 million to aid in the preparation of the PBL, poverty reduction and technical assistance through the CTCS.

Resources approved to Grenada account for 16.5 percent of total resources allocated to the sub-region. The development of physical infrastructure has been the main focus of ongoing activities in this island, with significant emphasis being placed on bridge and road improvement, the rehabilitation of schools, waste management improvement, and natural disaster management. In 2008, loans approved to Grenada amounted to US$5.7 million comprising US$3.7 million for disaster mitigation and restoration and US$2 million for a student loan. Grants approved totalled US$2.2 million for CTCS, BNTF and institutional strengthening of the Ministry of Communications.

CDB has also played an important role in helping Dominica pursue its development objectives, with funding accounting for 15.5 percent of total approvals to the ECCU. Projects underway in Dominica are in the areas of education sector enhancement, natural disaster management, waste management and the upgrading of eco-tourism sites. In addition to the CDB's capital project-related interventions, the Bank has actively assisted Dominica in its economic reconstruction effort through the provision of stabilization/structural adjustment loans. In 2008, US$9.7 million in loans was approved to assist in the rehabilitation effort following the passage of Hurricane Omar in October. Dominica also received US$2.5 million in grants for poverty reduction, education sector enhancement, operationalisation of national parks service, and assistance from CTCS.

Approvals to St. Vincent and the Grenadines amounted to US$174.7 million over the period 1970 to 2007. In 2008 US$10.4 million in loans was approved for the student loan scheme and a study on port rationalisation and development. The country also received a further US$1.8 million from the BNTF and CTCS programmes to bring the total share of CDB activity in this country to 15.5 percent. During the year the Bank finalised a country strategy with St. Vincent and the Grenadines to guide interventions over the period 2009–11. Some of the potential areas in which CDB may get involved are economic diversification, infrastructure development, human resource development, poverty reduction, disaster risk management and strengthening public sector management.

Activity in St. Kitts and Nevis has mainly been in the areas of disaster rehabilitation and natural disaster management, with some emphasis on improving the provision of education services, enhancing waste management and developing a sound macroeconomic policy framework through policy-based lending. In 2008, a student loan amounting to US$6.2 million was approved while grant assistance totalled US$0.9 million for poverty reduction and CTCS services. At end-December 2008, approvals to St. Kitts and Nevis accounted for 15.1 percent of funding to the sub-region.

CDB approvals to Antigua and Barbuda account for only 5.9 percent of sub-regional activity. Education sector enhancement has been the main focus of recent assistance along with security improvements to the air and sea ports. Antigua and Barbuda only received grant assistance in 2008, which amounted to US$0.5 million for consultancy services for the appraisal of a policy based loan, preparation for a basic education project, and CTCS services. CDB is currently in the process of preparing a country strategy paper with Antigua and Barbuda to guide its programme of assistance over the medium term.

Activity in Anguilla is also relatively small, representing 4.4 percent of total approvals since 1970. Ongoing projects in Anguilla are predominantly in natural disaster management. The year 2008 however, saw some expansion in activity with a US$18 million loan being approved for Blowing Point Ferry port development and a US$0.3 million loan for a feasibility study for the establishment of a Hospitality and Training Institute. This study also received an additional US$0.1 million in grant funding, while CTCS funding amounted to US$0.08 million.

Approvals to Montserrat have also been minimal following the dramatic reduction in economic activity in the wake of volcanic activity and the country's subsequent dependence on UK aid. Funding to Montserrat accounts for a mere 1.5 percent of total approvals to the sub-region with most of the recent work involving improvements to the education sector. Montserrat received only CTCS and BNTF grant assistance in 2008, which totalled US$l.1 million.

CDB Operations
Loans, Contingent Loans, Equity and Grants
(Net, in millions of U.S. dollars) 1/

	Approvals 1970–2007	Disbursements 1970–2007	Approvals 2008	Disbursements 2008
Anguilla	34.2	30.2	18.5	1.2
Antigua and Barbuda	71.4	49.0	0.0	6.9
Dominica	171.9	141.4	15.3	3.6
Grenada	191.6	144.9	8.0	10.3
Montserrat	17.3	10.6	1.1	0.5
St. Kitts & Nevis	176.7	121.1	6.4	15.8
St. Lucia	265.3	226.1	44.8	10.2
St. Vincent and the Grenadines	174.7	130.3	12.2	13.0
Total	**1103.1**	**853.6**	**106.2**	**61.6**

1/ All figures are net of cancellations.

Appendix IV. CARTAC: Capacity Building in the ECCU

The Caribbean Regional Technical Assistance Center (CARTAC) was established in November 2001 as a regional resource, based in Barbados, to provide technical assistance (TA) and training to beneficiary countries, currently 21[27]. CARTAC's core areas of technical assistance include public financial management, which includes tax policy and administration, public expenditure management, macroeconomic management and financial programming, financial sector supervision (including capital markets) and economic and financial statistics. It is a multi-donor project with the IMF as executing agency.[28] An active Steering Committee consisting of representatives from participating countries, donor agencies, CARICOM and the CDB, provides strategic guidance and ensures ownership and commitment.

The ECCU countries have been among the most active countries in requesting technical assistance and training in all of CARTAC's core areas. Again, the largest areas of CARTAC involvement in the ECCU countries have been in VAT implementation and in building capacity to undertake improved macroeconomic management. This technical assistance support has represented a significant addition to the Fund's technical assistance to the ECCU region. Highlights of CARTAC's technical assistance to the ECCU countries in the various core areas are provided below.

In the area of **tax and customs policy and administration**, CARTAC and FAD conducted a comprehensive review of the OECS tax systems and administrations in 2003. Most of the ECCU countries have started to implement the salient recommendations of the review. The following countries have introduced a VAT: Dominica (2006), Antigua and Barbuda (2007), St. Vincent and the Grenadines (2007), while Grenada is actively working to introduce a VAT (early 2010); St. Lucia (mid 2010); and St. Kitts and Nevis (late 2010). CARTAC is undertaking an external evaluation of its VAT program with a focus on results and outcomes of CARTAC's technical assistance. CARTAC has provided technical assistance to establish a personal income tax system in Antigua and Barbuda; significant technical assistance and training has been provided in Antigua and Barbuda, Dominica, Grenada and St. Vincent and the Grenadines, St. Kitts and Nevis and St. Lucia related to their VAT implementation. CARTAC has also undertaken full revenue assessment missions to Dominica, St. Lucia, St. Vincent and the Grenadines and St. Kitts and Nevis. In 2008, CARTAC assisted with the development of corporate strategic business plans for tax and customs departments in Grenada, St. Vincent and the Grenadines and Dominica. Training has been provided in customs valuation and risk assessment in three OECS countries in coordination with CCLEC

[27] Bermuda joined CARTAC in November, 2007 bringing the total number of members to 21.

[28] CIDA provides over 50 percent of CARTAC's total funding, with CDB, EU, Ireland, IMF, UNDP, the World Bank, and CARTAC member countries contributing the remainder.

and with support from the Canadian and U.S. Customs agencies. Oversight technical assistance has been provided to St. Vincent and the Grenadines and Grenada customs, regarding their reform programs. Antigua and Barbuda has established a customs reform program with CARTAC assistance and USAID is assisting to implement reforms including the adoption the Jamaican CASE (IT) system. CARTAC completed a significant Regional IT Study in the areas of tax, customs, treasury, expenditure and budget in ten Caribbean countries including ECCU countries at the request of the Canadian International Development Agency (CIDA) related to the development of their SEMCAR program. CARTAC will, during the remainder of 2009 and 2010: (1) continue to provide pre- and/or post-VAT technical assistance to Antigua and Barbuda, Dominica, St. Vincent and the Grenadines, Grenada, St. Lucia, and St. Kitts and Nevis; (2) undertake a full revenue administration assessment mission in Antigua and Barbuda; (3) continue to deliver targeted short-term customs oversight technical assistance to Grenada and St. Vincent and the Grenadines in their respective customs reform programs providing strategic and modernization recommendations; (4) provide customs post clearance audit training in St. Vincent and the Grenadines and St. Lucia; (5) provide customs assistance in developing new customs laws and related regulations in Grenada and Dominica; (6) provide regional training workshops with the ECCB and CARICOM on the CARICOM Tax Treaty and insurance concepts course; and (7) provide a regional workshop with ECCB on the use of a revenue authority toolkit. Further, CARTAC will continue to assist five OECS countries build their capacity in the area of collections enforcement and audit through formal training, on the job coaching, and enhanced operational manuals.

In **public finance management**, CARTAC and the ECCB assisted ECCU countries in diagnostic exercises as part of the Fiscal Machinery Project to draw up action plans to address public expenditure management weaknesses. Following up on these diagnostic assessments, CARTAC has focused on improving cash management, budgeting procedures and debt management in the ECCU countries, with both seminars and short-term missions. A review of the Treasury function in 2006 and of the Budget function in 2007, has been conducted in Antigua and Barbuda and reports presented to the Minister of Finance. Three months of technical assistance were provided to the Antigua treasury following the report in 2007 and 2008. Treasury reviews were also performed in Dominica (2007) and St. Kitts and Nevis (2008). CARTAC has funded the attachment of a budget officer from Grenada to the ECCB for the purpose of addressing Grenada's consolidated public sector accounts. Technical assistance was provided to Anguilla (2007) for the development of an annual cash management forecast model.

An analysis of St. Lucia's budget system was undertaken in 2006 and recommendations submitted to the authorities. A follow up mission was done in January 2009 with focus on program/performance budgeting. A review of St. Vincent's budget system is scheduled for mid-March 2009. Revenue forecasting and modeling workshops were held in St. Kitts and Nevis with participation from Anguilla (2007), St. Lucia (2007), Dominica (2007), St. Vincent (2008), Grenada (2008), and Montserrat (2008). A review of the internal and external audit functions was performed in Anguilla in 2007. A debt sustainability workshop was held in St. Vincent in 2008.

Pension reviews were done in Montserrat (2008) and St. Kitts and Nevis (2008). A follow-up mission to Montserrat was completed in 2008 to assist the authorities in their selection of the options for reform. CARTAC will be providing further technical assistance to implement the selected options.

CARTAC has funded Smartstream User Group meetings in 2007 and 2008 to discuss issues and problems with the software with the software company in attendance. All ECCU countries are users with the exception of Antigua which utilizes Free Balance software, Funding for IT attachments from Anguilla and Grenada to Barbados was provided to improve their financial reporting capacities.

CARTAC has also been helping in establishing an internal audit unit in St. Lucia. A training manual and a training program have been developed and were delivered in 2006 with participation from Dominica. Introduction to internal audit workshops were delivered to St. Lucia and Dominica (2006), St. Vincent and Grenada (2007) and St. Kitts and Nevis and Anguilla (2007). Advanced internal audit workshops were delivered to St. Lucia and Dominica (2007), St. Vincent and Grenada (2008) and St. Kitts and Nevis and Anguilla (2008). In order to support a coordinated regional approach to public finance reform, CARTAC has supported the establishment of the Caribbean Public Finance Management Association (CAPFA), in which the ECCU countries have been active.

At the request of the ECCB, CARTAC has provided technical assistance to the ECCU member countries in developing and implementing their own home-grown programs aimed at achieving a set of fiscal/debt targets.[29]

Over the last year, CARTAC successfully reinvented the work in the MAC area to focus on building capacity within the ministries of finance and the ECCB in macroeconomic analysis, forecasting and performance monitoring. This was a priority in light of the apparent weakening of local macro/fiscal teams in a number of countries. In 2008, CARTAC continued to organize missions across the ECCU to work with small teams to prepare macroeconomic projections under a baseline scenario; identify imbalances and formulate policy measures to address them; and prepare a framework to monitor key quarterly targets of the programme.

[29] The original targets were replaced in 2006 by a ceiling on the public sector debt/GDP ratio of 60 percent by 2020.

In the past year, the **financial sector supervision and capital markets** advisors have focused on upgrading the legislative framework for the nonbank sector. On the financial sector side, an inventory of capacity building needs was completed in late 2007 and elaborated a work plan to address the technical assistance needs over the next three years for the Caribbean region in the areas of banking, insurance, credit union, and nonbank supervision as well as the development of single regulatory units. For the banking sector, CARTAC works closely with the Caribbean Group of Banking Supervisors (CGBS) to fulfill the training needs of the region through workshops. Workshops in progress are IT Examinations for Banking Supervisors, Crisis Preparedness, and Market Risk Assessments. For country-specific banking supervision technical needs, CARTAC arranges for a consultant to work with the banking authorities on the areas of need. Most recently, the country-specific capacity building projects are implementation of the market risk capital charge under the Basel I capital adequacy requirements, implementation of Basel II, and stress-testing. For insurance supervisors, CARTAC convened an Insurance Supervision Advisory Group to identify the insurance supervisory training needs of the region as well as programs to implement those needs. As a result of the activities of the CARTAC Insurance Advisory Group, the Caribbean Association of Insurance Regulators (CAIR) was rejuvenated and instituted a number of training programs based on the IAIS Core Curriculum for Insurance Supervisors. Work is also underway in several countries to revise insurance laws and to design regulatory insurance reporting forms. Work is ongoing with the Off-shore Group of Insurance Supervisors on building capacity in the off-shore insurance supervision sector. For credit union supervisors, a model Credit Union Law has been developed and changes in the legal framework for the supervision of credit unions is well underway in several key countries. Regulatory reporting forms for credit unions are now in place for the ECCU, and specific on-site and off-site supervisory training is being conducted in various countries. In addition to these key areas of supervision, CARTAC serves the capacity building needs for the Caribbean Financial Action Task Force (CFATF) and the off-shore supervisors in the region. The development of single regulatory units in the ECCU is also a major on-going technical assistance project. Work has also begun in enhancing pension fund supervision in the region. Two other recent projects recently undertaken are the development of credit bureaus in the region and the launching of a financial literacy web site (www.financialliteracycaribbean.com). Work conducted throughout the region as well as the output is provided to all supervisory authorities through the CARTAC web site under Financial Sector Resources.

On the capital markets side, a CARTAC-sponsored attachment of ECSRC regulators to Jamaica to observe and participate in an on-site examination of a securities dealer; and CARTAC-sponsored attendance by ECSE and ECSRC staff at securities training courses in Washington, DC took place in 2008. CARTAC also sponsored the attendance of senior ECSRC regulators at a regional conference in Jamaica on unregulated investment schemes and at the annual conference of the CGSR in Barbados. CARTAC sponsored the participation of an experienced regional securities regulator from Trinidad & Tobago at a retreat for the induction of new ECSRC commissioners. A draft Financial Services Commission Act in Montserrat, sponsored by CARTAC, has been submitted to the authorities. CARTAC is currently assisting Grenada with the setting up of the Grenada Authority for the Regulation of Financial Institutions (GARFIN). CARTAC has assisted with the development of prudential reports for nonbanks in the ECCU and recently conducted training on the supervision of offshore mutual funds for St. Kitts and Nevis and St. Lucia and on the supervision of securities firms for the ECSRC.

During 2008, the CARTAC program to improve **economic and financial statistics** in the ECCU concentrated on national accounts and prices. Anguilla, Dominica, Grenada, St. Kitts and Nevis, and St. Vincent and the Grenadines were the main beneficiaries of technical assistance for strengthening national accounts statistics. Supply and use tables were completed for Dominica and St. Vincent and the Grenadines in the first quarter of the year, and progress was also made in developing supply and use tables for Grenada. At the same time, the project launched in the last quarter of 2007 to improve the measurement of tourism in the national accounts was extended to Anguilla, bringing the number of countries benefiting under the project to seven. In response to a request from the authorities, CARTAC assisted St. Kitts and Nevis in compiling separate production-based measures of GDP for the islands of St. Kitts and Nevis, and CARTAC assisted the Nevis Department of Statistics and Economic Development in building up a capability in compiling national accounts. In the areas of prices, CARTAC gave assistance to Anguilla, Antigua and Barbuda, St. Kitts and Nevis, St. Lucia and the ECCB in improving CPI compilation. Work on the development of export-import price indices (XMPIs) was initiated in St. Kitts and Nevis and continued in Anguilla. With respect to training, Grenada benefited from professional attachments for training in XMPI compilation and dissemination. In other areas of training, CARTAC mounted three regional courses between July and September, 2008. CARTAC sponsored and conducted workshops on national accounts statistics and XMPIs, while a seminar on the Coordinated Direct Investment Survey and Balance of Payments was hosted by CARTAC and conducted by the IMF. Participants from the ECCB and the eight ECCU territories attended each of the three training courses.

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IMF Executive Board Concludes 2009 Discussion on Common Policies of Member Countries of the Eastern Caribbean Currency Union

On May 15, 2009, the Executive Board of the International Monetary Fund (IMF) concluded the 2009 Discussion on Common Policies of Member Countries of the Eastern Caribbean Currency Union (ECCU).[1]

Background

In the face of a weak and volatile external environment, economic activity in the ECCU has faltered, and the ECCU has entered a recession. Led by construction and tourism, average annual growth reached 4½ percent during 2003–07. However, growth declined to 1.8 percent in 2008, and the region's real GDP is expected to contract by a further 2½ percent in 2009, reflecting a sharply-slowing global economy, declining tourist arrivals and foreign direct investment (FDI) flows, and increased financial sector stresses. Following a strong acceleration during the first three quarters of 2008 (to reach about 9 percent), inflation eased toward end-2008 amid the retreat of world commodity prices, and is projected to return to its long-run average of 2–3 percent per year in 2009.

Limited progress has been made towards fiscal consolidation. Tax revenues have increased, benefiting from strengthened tax administration and broader tax bases (particularly owing to the introduction of VATs). Capital expenditure peaked in 2006, reflecting Cricket World Cup and tourism-related investment, but has since declined, and current expenditure remained high. As a result, while some fiscal consolidation was achieved during 2007, no major progress was made in 2008. Recession-induced revenue losses and higher debt-servicing costs are projected to raise the region's overall fiscal deficit to 6.8 percent of GDP in 2009 (4⅔ percent in 2008), with public debt rising to 98 percent of GDP at end-2009 (91 percent at end-2008).

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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. At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities.

The region's financial system has not been immune to the global crisis. Growth of monetary aggregates decelerated markedly in 2008, particularly during the last quarter, and the trend of improving bank prudential indicators in recent years has started to reverse. High government exposures, credit risk, and liquidity risk present major threats to ECCU banking system stability. Shocks emanating from the collapse of CL Financial Group, a Caribbean conglomerate headquartered in Trinidad and Tobago, and the Stanford International Bank, an offshore bank based in Antigua and Barbuda, have also increased the stress in the nonbank financial sector (including the offshore financial institutions), with knock-on effects to domestic banks. Against this background, the authorities have accelerated their efforts in strengthening financial sector regulation and supervision, including through the establishment of effective national single regulatory units for nonbanks.

The current account deficit remained elevated at 34 percent of GDP in 2008, as slowing construction-related imports offset falling tourism receipts and higher fuel and food imports. The deficit is projected to contract markedly to about 24 percent of GDP in 2009, with weaker demand for imports (owing to slowing FDI and domestic demand) and favorable movement in the region's terms of trade (underpinned by falling commodity import prices) more than offsetting the impact of continued lackluster tourism performance and declines in remittances and exports. Gross international reserves are expected to fall in 2009 (by about 1½ percent of GDP), as capital inflows are projected to decline by more than the contracting current account deficit. Despite some recent real appreciation, the Eastern Caribbean dollar's real effective exchange rate is in line with its equilibrium level, and remains close to its most depreciated level in almost 20 years.

Executive Board Assessment

The Executive Board noted that the tourism-dependent ECCU region has been hit hard by the global downturn, particularly through sharply-declining tourist arrivals, remittances, and foreign direct investment. Directors considered that the ECCU economy will experience a severe contraction of uncertain length and depth and increased financing strains. Against this background, Directors supported the authorities' focus on policies to manage near-term challenges and downside risks, while continuing to address fundamental fiscal and debt sustainability issues. They also endorsed the authorities' ongoing efforts in crisis prevention, and encouraged the authorities to further enhance contingency plans for possible crisis scenarios.

Directors commended the ECCU authorities' prompt and coordinated responses to address threats to the region's financial stability emanating from the collapse of the Trinidad and Tobago-based CL Financial Group and the Antigua-based offshore Stanford International Bank. Directors also welcomed progress in strengthening regulation and supervision of the financial sector, particularly the passage of harmonized legislation governing nonbank financial institutions. Nonetheless, they recommended reinforced efforts to intensify oversight of banks, particularly through further increasing the frequency and scope of on-site inspections, and to strengthen follow-up and enforcement of remedial measures. Directors stressed that non-bank and offshore financial sectors need to be quickly brought under effective regulation and supervision, through establishing fully functioning national Single Regulatory Units. Given the increasing presence of financial conglomerates in the Caribbean, they welcomed the ongoing efforts by the ECCU authorities to strengthen cross-functional and cross-border consolidated supervision, and to enhance collaboration and information sharing. A number of Directors called for enhancing implementation of Anti-Money Laundering/Combating the Financing of Terrorism (AML/CFT) frameworks, while a few encouraged the authorities to implement the internationally agreed tax standard developed by the Organisation for Economic Co-operation and Development (OECD).

Directors considered that the currency board arrangement continues to serve the region well by fostering price and financial stability, including in the face of adverse external shocks. They observed the staff's assessment that, despite some recent appreciation, the real effective exchange rate appears to be in line with fundamentals. Nevertheless, given the deteriorating terms of trade and export performance, Directors welcomed the region's continued efforts—including through the establishment by end-2009 of the Organization of Eastern Caribbean States Economic Union—to enhance regional integration and external competitiveness.

Directors observed that the region's very large external current account deficits are narrowing, and continue to be predominantly financed by non-debt creating foreign direct investment. They cautioned that any sudden slowing of capital inflows in a deteriorating external environment could raise pressures on international reserves. Directors supported the authorities' intentions to monitor closely private sector capital flows and the ECCU's net asset position, and to enhance statistics in this area. They encouraged the authorities to improve the business climate through regulatory, administrative, and legal reforms.

Given the region's high public debt levels and currency board arrangement, Directors considered that there is little room for counter-cyclical fiscal policy during the current economic downturn. They stressed that fiscal discipline is key to underpinning external stability and maintaining credibility of the currency board arrangement. Directors encouraged the authorities to minimize the worsening in the fiscal deficit and over the medium term to reduce the public debt-to-GDP ratio. Toward those objectives, they endorsed the authorities' plans to complete tax reforms in the remaining ECCU jurisdictions, prioritize capital expenditures, contain wage bills, and enhance debt management. Fiscal credibility would be enhanced by establishing a strong and transparent link between national fiscal policies and achievement of the ECCB Monetary Council's fiscal benchmarks. Directors supported the authorities' plans to increase expenditure on targeted social safety nets, in order to mitigate the hardship on vulnerable groups during the economic downturn.

Directors commended the progress, led by the ECCB, in improving the region's statistics and institutional building. They encouraged national and regional authorities to further improve statistical practices and bolster data management, and supported the ongoing efforts to develop an integrated regional statistical system for the ECCU.

Directors agreed that the views they have expressed today will form part of their discussions in the context of the Article IV consultations for individual members of the ECCU that take place until the next Board discussion of the ECCU's common policies.

Public Information Notices (PINs) form part of the IMF's efforts to promote transparency of the IMF's views and analysis of economic developments and policies. With the consent of the country (or countries) concerned, PINs are issued after Executive Board discussions of Article IV consultations with member countries, of its surveillance of developments at the regional level, of post-program monitoring, and of ex post assessments of member countries with longer-term program engagements. PINs are also issued after Executive Board discussions of general policy matters, unless otherwise decided by the Executive Board in a particular case.

Eastern Caribbean Currency Union: Selected Economic and Financial Indicators, 2005–09 1/

	2005	2006	2007	Prel. 2008	Proj. 2009
	(Annual percentage change)				
National income and prices					
Real GDP	5.6	6.3	5.2	1.8	-2.4
GDP deflator	3.3	2.7	3.5	5.1	3.4
Consumer prices, average	3.2	4.0	3.3	6.9	3.1
	(In percent of GDP)				
Public finances					
Primary central government balance	-0.5	-1.1	-0.8	-0.7	-2.2
Overall central government balance	-4.4	-5.1	-4.4	-4.7	-6.8
Total revenue and grants	29.9	31.3	30.7	31.0	28.9
Total expenditure and net lending	34.3	36.4	35.1	35.6	35.7
Total public debt (end-of-period)	100.5	98.4	94.5	90.6	97.9
	(In percent of GDP, unless otherwise noted)				
External sector					
Current account balance	-22.4	-29.7	-34.8	-33.9	-24.2
Trade balance	-40.2	-44.6	-47.1	-45.3	-31.8
Travel	26.7	24.4	22.8	20.7	17.3
Exports, f.o.b. (annual percentage change)	8.0	-2.5	4.8	12.9	-8.6
Imports, f.o.b. (annual percentage change)	18.0	17.0	13.3	4.3	-25.6
Stayover visitors (annual percentage change)	1.3	2.8	-1.8	-1.3	-11.6
Terms of trade (annual percentage change) 2/	-2.8	-9.7	-1.5	-14.0	...
Real effective exchange rate (annual percentage change) 2/ 3/	-0.9	-0.1	-2.3	1.1	...
End-year gross foreign reserves of the ECCB					
In millions of U.S. dollars	600.8	696.0	764.5	759.0	687.4
In months of imports	3.9	3.8	3.7	3.5	4.3
In percent of broad money	17.9	18.6	18.6	17.9	16.4
External public debt (end-of-period)	53.9	50.9	47.4	46.0	50.1
	(Annual percentage change)				
Money and credit					
Net foreign assets 4/	1.2	2.0	-1.5	-7.0	-2.7
Net domestic assets 4/	7.2	9.6	11.2	9.9	1.6
Broad money	8.4	11.6	9.7	3.0	-1.0

Sources: ECCU country authorities; Eastern Caribbean Central Bank; and Fund staff estimates and projections.

1/ Includes all eight ECCU members unless otherwise noted. ECCU price aggregates are calculated as weighted averages of individual country data. Other ECCU aggregates are calculated as sum of individual country data; ratios to GDP are then calculated by dividing this sum by the aggregated GDP.
2/ Excludes Anguilla and Montserrat.
3/ End-of-period (depreciation -), 1990=100.
4/ In relation to broad money at the beginning of the period.