Caribbean Region Quarterly Bulletin

2017:II

Commodities in the Caribbean

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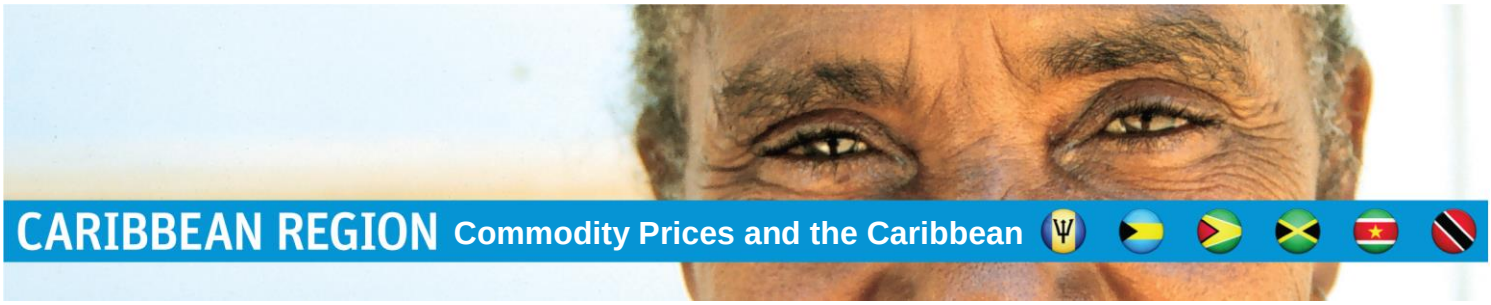
IDB Country Department Caribbean

Commodities in the Caribbean



The Challenges Continue

This edition of the Quarterly Buletin discusses recent economic developments in the Caribbean and explores the importance of commodity prices for the Caribbean.

Selected Indicators	Real Growth Rate	Annual Inflation (% end of period)	General Government Primary Balance (% of GDP)	General Government Overall Balance	Current Account balance (% of GDP)	General Government Gross Debt (% of GDP)
The Bahamas	0.0	1.0	-0.3	-3.5	-11.4	75.2
Barbados	1.6	0.3	0.1	-7.8	-4.5	145.2
Guyana	3.2	1.3	-4.5	-5.4	-3.0	46.3
Jamaica	1.7	4.0	7.0	-0.9	-3.0	115.2
Suriname	-9.0	61.0	-4.5	-6.1	-3.6	67.8
Trinidad and Tobago	-2.3	3.1	-2.9	-5.0	-10.0	60.9
CCB Average	-0.8	11.8	-0.9	-4.8	-5.9	85.1

Source: International Monetary Fund and country authorities.
Note: Year is 2016 or closest available date. Barbados debt figure includes holding of NIS.

Summary of Economic Update by Country

The new government in **The Bahamas** announced it would address increasing fiscal imbalances and a build-up in debt. In spite of large investment projects, growth remains tepid but the economy remains stable with gross international reserves forecasted to remain at stable levels and inflation projected to be lower than the previous year-end period. However, double-digit unemployment and a higher share of non-performing loans continue to constrain private credit.

The government in **Barbados** is trying to address growing vulnerabilities with an unprecedented fiscal adjustment. The intended measures, which focus on revenues but also include expenditure savings and try to address foreign exchange pressures, should lead to an adjustment of 5 percent of GDP. Economic growth was estimated at about 1.5-2 percent but could be lower as a result of the fiscal adjustment.

Gold continues to drive **Guyana's** economy through the first months of 2017. Better weather conditions in the early part of year compared to El Nino affected 2016 agricultural campaign, promises to increase yields. An expansionary fiscal policy continues amid implementation challenges. Monetary policy remains accommodative as GoG foreign currency situation seems to be stabilizing.

The **Jamaican** economy remains stable with a positive outlook. The IMF Executive Board concluded the first review under the Stand-By Arrangement (SBA) in April 2017, reporting continued strong program implementation and sustained positive economic growth, estimated at 1.7 percent for FY2016/17 with an acceleration in later years.

Suriname is still overcoming a deep recession triggered by the fall in commodity prices in 2015. The economy is still projected to contract in 2017 but improvements are likely for the current account and fiscal balances.

The economy in **Trinidad and Tobago** continues stagnant but could start recovering slowly, provided that the energy output increases and the commodity prices stabilize. Overall, the non-energy activity has stagnated since 2015 as a consequence of lower prices and volumes of oil and natural gas as well as a fiscal retrenchment. However, economic performance largely differed across sectors. Besides, as the energy prospects improve in 2017-2018, the domestic economy could slowly recover revive its growth potential.

The **Eastern Caribbean** continues the tourism-led recovery. In addition, fiscal consolidation efforts are proving successful as some countries are achieving primary surpluses.

Special Regional Report: Commodities in the Caribbean

This Caribbean Region Quarterly Bulletin explores the importance of commodities for the countries of the Caribbean. While the Caribbean includes commodity producers, most depend heavily on energy imports. The fall in oil prices was a huge relief for these countries, improving the external position, keeping prices stable and increasing the purchasing power for households. At the same time, Suriname and Trinidad and Tobago were hit hard with falls in exports, revenues and economic contractions.

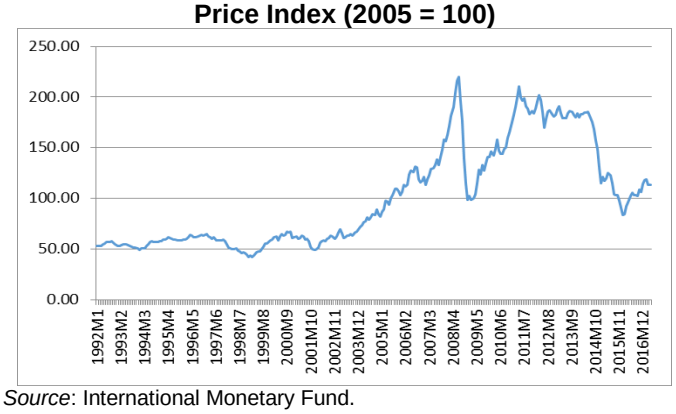
COMMODITIES IN THE CARIBBEAN: OVERVIEW

Contributor: Juan Pedro Schmid

Introduction

Commodities are central to the small and open economies of the Caribbean region. Three countries that correspond to the IDB's Caribbean Country Department – Guyana, Suriname, and Trinidad and Tobago – are commodity exporters. The other three countries – The Bahamas, Barbados, and Jamaica depend on commodity imports (as do the countries of the Organisation of Eastern Caribbean States). Interestingly, the economic performances of The Bahamas, Barbados, and Jamaica have been among the weakest in the region, while the commodity producers – Guyana, Suriname, and Trinidad and Tobago – in general performed better and benefited until recently from high commodity prices. However, the recent fall in commodity prices (Figure 1) exposed their overreliance on commodities and dampened their growth outlooks in the short to medium terms.

Figure 1. International Monetary Fund All Commodity Price Index (2005 = 100)



Source: International Monetary Fund.
Note: Includes both Fuel and Non-Fuel Price Indices.

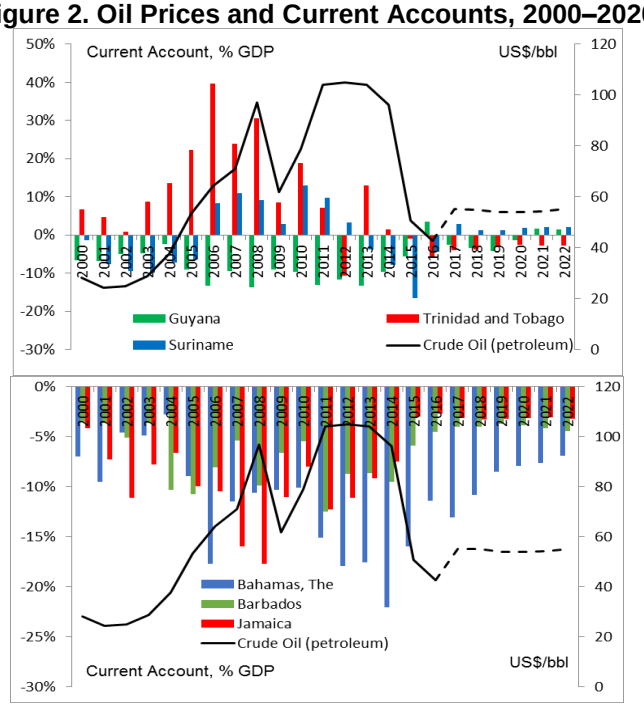
Oil is the dominant commodity in the Caribbean. In terms of exports, Suriname and Trinidad and Tobago already export crude, while Guyana is expected to become a major producer by 2020. Trinidad and Tobago also exports natural gas, while Suriname also has gold and used to mine bauxite/alumina. Guyana is the most diversified, as it relies on gold but also exports rice, bauxite, and timber, among other commodities. Other countries are niche producers. For instance, Jamaica used to be a major bauxite exporter but volumes have fallen on the back of high domestic energy prices and low world prices. In addition, Jamaica produces small quantities of coffee and some other agricultural produce.

Oil dependence is a major vulnerability for macroeconomic stability. The vulnerability of the commodity importers stems from several factors: lack of alternative energy sources, which forces them to import most energy (over 90 percent); and outdated, inefficient electricity generation, which leads to high prices by international comparison. As a result, economic growth, external sustainability, and fiscal sustainability depend on the vagaries of oil prices.

The End of the Commodity Super-Cycle and the Caribbean

The fall in commodity prices eased pressures on some Caribbean countries. While commodity producers have been facing headwinds and were forced to adjust amid lower commodity prices and the potential for an extended downturn, commodity importers were relieved (Figure 2). Lower commodity prices had beneficial effects on the external position of The Bahamas, Barbados, and Jamaica and supported the economic recovery of these countries.

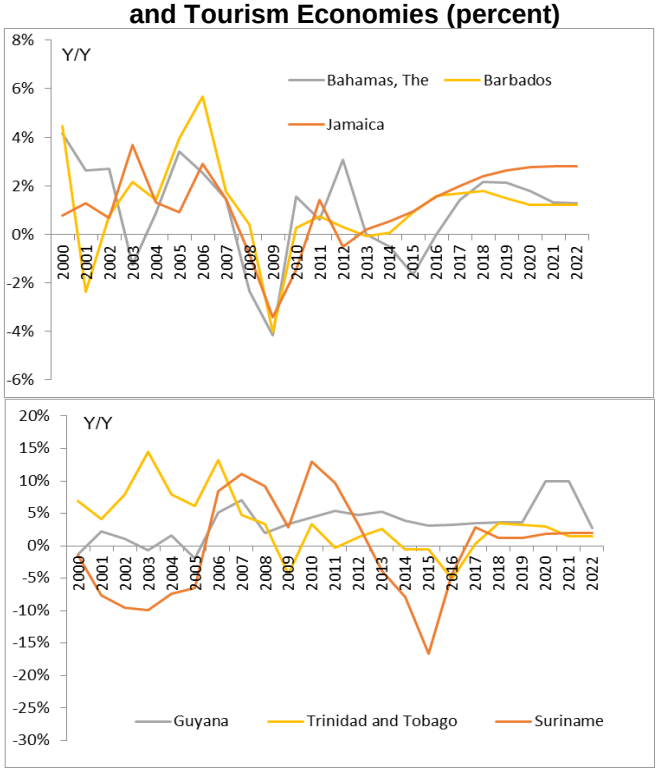
Figure 2. Oil Prices and Current Accounts, 2000–2020



Source: IDB calculations based on data from the International Monetary Fund, *World Economic Outlook.*

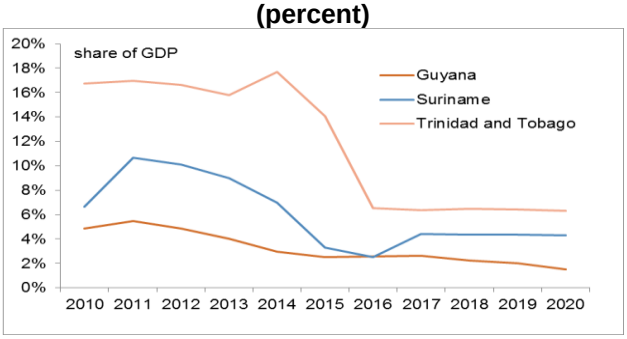
Suriname and Trinidad and Tobago were hardest hit by the end of the commodity super-cycle. Their current accounts fell into deficit while economic growth collapsed (Figure 3). In addition, fiscal challenges increased as both countries depended on commodities for their revenues (Figure 4). Both countries have started adjustments to mitigate further worsening from the outfall. Conversely, Guyana's economic performance has remained strong, as stable and increasing gold prices have compensated for the fall in other commodity prices. In addition, Guyana is still a net energy importer; and, as such, benefited from the fall in oil prices.

Figure 3. Economic Growth in Caribbean Commodity and Tourism Economies (percent)



Source: IDB calculations based on data from the International Monetary Fund, *World Economic Outlook.*
Note: Y/Y = year-over-year.

Figure 4. Commodity Revenues as a Share of GDP (percent)



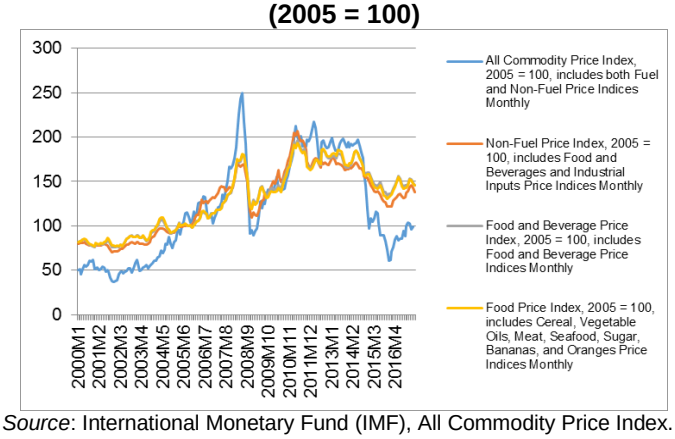
Source: International Monetary Fund.

Commodity Prices

Overall, commodity prices are still above their long-term averages. The International Monetary Fund's All Commodity Price Index increased sharply between 2005 and 2007. The global financial crisis led to a sharp decline in prices, but prices recovered quickly and remained elevated from 2011 to 2014. Commodity prices fell again in 2014. Currently, prices are close to their 2005 level (Figure 5).

Energy prices are the main driver of commodity price swings. While less volatile, non-energy commodity price indexes follow energy prices. Energy is a major input for commodity production, and energy reacts quickly to demand and supply forces, as was the case in 2014 when U.S. shale oil and gas production led to an increase in supply while demand remained constrained.

Figure 5. IMF Commodity Price Sub-Indexes (2005 = 100)

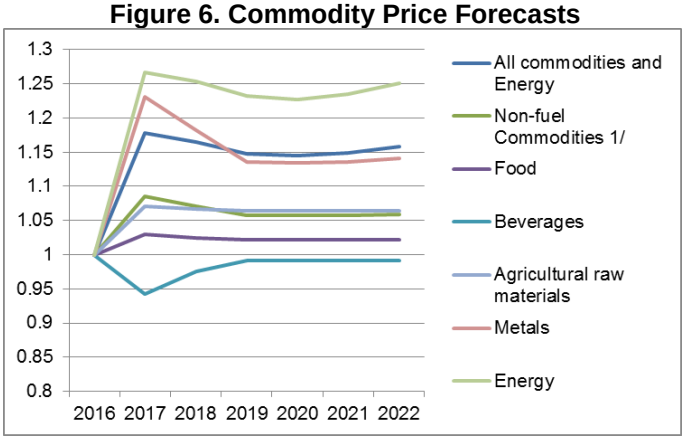


Source: International Monetary Fund (IMF), All Commodity Price Index.

Outlook

The outlook for commodity prices remains tepid. Prices of major commodities are projected to remain above 2016 levels but no major increases are projected (Figure 6).

Figure 6. Commodity Price Forecasts



Source: International Monetary Fund, All Commodity Price Index.

In terms of oil prices, forecasts are flat amid abundant supply, but important risks remain.[1] Underlying the oil price forecast is the assumption that the OPEC deal is extended, which could drive a modest rally in global oil prices. Oil prices could fall if the OPEC agreement is abandoned. A large increase in U.S. shale oil production, for instance, could undermine political will among OPEC producers to accept a loss of market share. On the upside, geopolitical risk related to tensions

[1] For a detailed outlook, see the Economist Intelligence Unit June Crude Oil Update.

between the various powers involved in the Syrian proxy conflict could push prices higher. Prices could remain under pressure over the longer term as oil production from other countries, including Canada, the United States, and Brazil, continues to increase.

Conclusion and Policy Options

Most forecasts expect commodity prices to remain low compared to the boom period from 2002–2014. The fall in prices has hit oil-exporting countries like Suriname and Trinidad and Tobago hard. Both economies are under pressure, despite some savings during the good times. This makes the task even harder for the governments to rebalance policies in response to the low energy prices – particularly their fiscal stances.

Conversely, low oil prices have benefited most other countries in the region that rely on oil and fuel imports. The effects in these countries have been especially visible on their external positions as Jamaica, Barbados, Guyana and The Bahamas have eliminated much of their double-digit current account deficit. The low oil prices offer these countries opportunities to increase buffers and improve policies to make them less vulnerable to oil price fluctuations.

The dependence on energy imports remains an important vulnerability and requires policy adjustment and investments. Most countries can exploit efficiency improvements of domestic power utilities and savings from energy efficiency investments. In addition, the lower oil prices can be used to reduce reliance on government subsidies and expand the use of renewable energy.

Diversification would shield commodity producers from price volatility. However, diversifying an economy is a slow and difficult process. In the meantime, other options could be pursued such as hedging against oil price changes.[2]

[2] Mexico is an oil producer that hedges against a decline in oil prices. Conversely, Jamaica has been hedging against oil price increases since 2015.

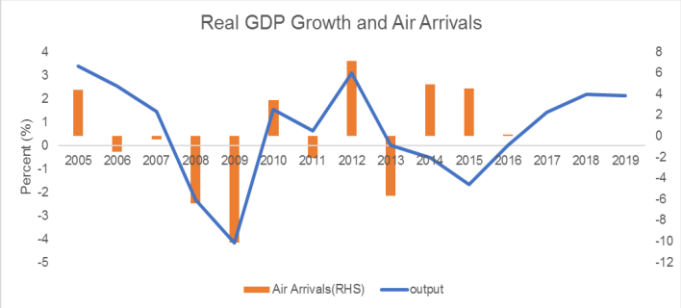
Contributor: Allan Wright

Overview

The Bahamas faces a tepid growth outlook. Growth has been averaging 0.5 percent over the past 10 years. Real GDP is projected to grow by 1.4 percent in 2017, compared to flat growth a year earlier. The International Monetary Fund's projected average medium-term growth rate for the next five years is 1.7 percent.

Large capital projects are driving medium-term growth. The Baha Mar Casino and Hotel opened on April 21, 2017 with expectations of additional direct jobs, tax revenues, and other economic impacts within the next two fiscal periods. The Freeport Container Port, Ocean Cay Hotel, Marine Park, and Williams Cay Hotel are other large capital projects expected to be growth-positive within the same period. These large capital ventures are being relied upon to make outstanding contributions to push mid-term GDP growth above 1 percent.

Figure 1: Real GDP Growth and Air Arrivals (percent)



Sources: International Monetary Fund, *World Economic Outlook* (April 2017); and Ministry of Tourism statistics.

Recent Developments

The 2017 general elections in The Bahamas took place peacefully throughout the archipelago on May 10, 2017. The Free National Movement (FNM) won 35 seats in the House of Parliament, with the Progressive Liberal Party (PLP) securing the other four seats.

The primary fiscal balance is expected to recover in 2017/18. The primary balance for 2016/17 is estimated to be -0.3 percent of GDP. However, as a result of tax revenues and increased economic activity from tourism-based infrastructure projects (Baha Mar, Freeport Container Port, Ocean Cay Hotel, Marine Park, and Williams Cay Hotel), along with current tax collections efforts, the International Monetary Fund estimates that the primary balance could improve to 0.7 percent in 2017/18.

Highlights

- *General elections were held on May 10, 2017, with the Free National Movement winning 35 of 39 seats.*
- *Public debt increased due in part to hurricane reconstruction and relief financing.*
- *Petroleum and food imports are significant contributors to the overall merchandise import bill within The Bahamas (over 13 percent of GDP).*

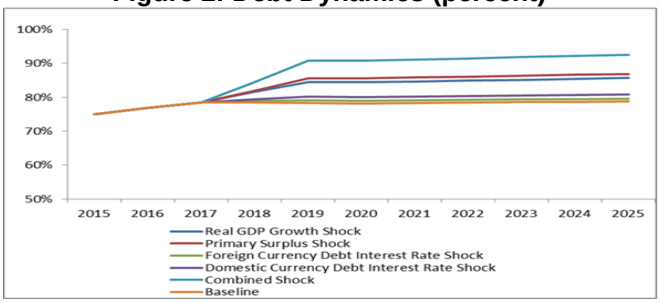
Public debt increased due in part to hurricane reconstruction and relief financing. Central government and publicly guaranteed debt is projected to increase by roughly 2.5 percentage points to 77 percent of GDP. Simulations show that The Bahamas would need to adjust the primary balance by 2.17 percentage points of GDP to stabilize its debt-to-GDP ratio. A simulation of the expected medium-term debt trajectory, subject to growth and interest rate shocks sustained over the two-year period from 2017–2018, suggests that even under adverse shocks the debt path stabilizes over time.

The Bahamas remains vulnerable to shocks. Simulations of the sensitivity of the debt trajectory, using a one standard deviation shock sustained over the two-year period from 2017–2018 suggest that under all shock scenarios the debt path stabilizes over time, though at a higher level, implying a stronger adjustment is needed to decrease debt in the medium to longer term. The Bahamas is most sensitive to declines in GDP growth, lower than projected primary surpluses or a combination of several shocks, all of which would shift the debt trajectory up (Figure 2). In contrast, The Bahamas is less sensitive to interest rates shocks, partly because interest rates have been relatively stable in the past. Simulations suggest that a one standard deviation increase keeps interest rates at levels close to the projections.

Examining the confidence in the current trajectory of the debt-to-GDP ratio using a fan chart analysis, The Bahamas' debt-to-GDP ratio (including publicly guaranteed debt) is expected to range between 70 and 85 percent of GDP over the medium to long term. The probability that the debt trajectory rose above 75 percent by end of 2017 is 95 percent, highlighting the need to

continue fiscal consolidation efforts to reverse the increasing trend.

Figure 2: Debt Dynamics (percent)

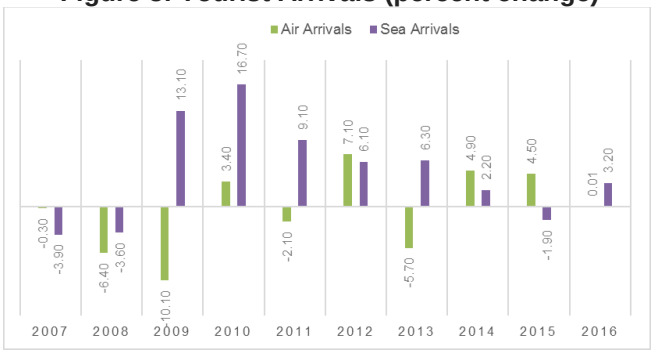


Source: IDB estimates based on data from the International Monetary Fund, *World Economic Outlook* (April 2017).

Our estimates suggest that The Bahamas' debt-to-GDP ratio would continue to rise in the short term and stabilize at 78 percent, with downside risks. The modest tourism recovery, any further delays to the comprehensive opening of the Baha Mar mega resort and its respective economic contribution, and modest fiscal consolidation (particularly on the expenditure side) are downside risks to growth over the next two to three years. Upside risks include materialization of the government's projected pipeline of tourism-related projects and respective private capital inflows. In addition, faster recovery in the tourism sector with growth in arrivals and higher spending per tourist could also contribute to growth above the baseline.

The tourism sector continued its gradual recovery from 2015. The increase in air arrivals was marginal at 0.1 percent to the end of the year. However, the largest category, sea landings, increased by 3.2 percent, resulting in overall total arrivals growing by 2.5 percent (Figure 3).

Figure 3: Tourist Arrivals (percent change)



Sources: Ministry of Tourism; and www.Tourismtoday.com

Inflation in The Bahamas, which is highly correlated with U.S. inflation, declined from 2 percent in 2015 to 1 percent as of December 2016. There is a full pass-through given The Bahamas' dependence on imports, and prices and variations follow international commodity prices. Almost 60 percent of the consumer basket is processed food, of which 95 percent is imported. An increase in petroleum prices would likely have an indirect effect on processed food prices. In 2016, price decreases of less than 7 percentage points were observed for education, housing, and transport**.**

Private sector credit had contracted by 1 percent as of December 2016. Although there is liquidity, lending has been risk-averse because of high levels of non-performing (NPL) loans, which peaked at 15.3 percent in 2014 (but subsequently declined to 11.4 percent as of December 2016). High NPL levels are due to double-digit unemployment, weaker domestic consumption, and the overhang from the global financial crisis.

Conclusion

The opening of the Baha Mar Casino and Hotel, along with the expansion in the Freeport Container Port, are expected to support real sector growth, help curb unemployment (by providing 5,000 jobs), and increase income (by over US$2 billion) once the projects come fully online within the next two fiscal periods.

Table 1: High-Frequency Macroeconomic Indicators

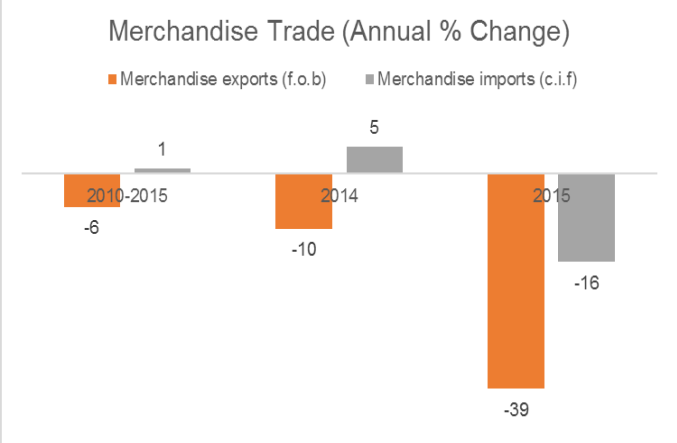
	Recent Data	Period	Prior Data	Period
Annual GDP growth (%)	0.0	2016	-1.7	2015
Tourist arrivals	2.5	Dec-16	-0.5	Jul-05
Exports (12-month growth)	1.8	Dec-16	-1.7	2015
Imports (12-month growth)	-3.0	Dec-16	2.0	2015
Private sector credit growth (%)	-1.0	Dec-16	-0.2	Sep-16
Inflation (% yoy change)	1.0	Dec-16	2.0	Jul-05
Exchange rate (end of period)	1.0	2016	1.0	2015
Unemployment rate (%)	11.6	Nov-16	14.8	Nov-15

Source: Central Bank of The Bahamas.

Introduction

According to the World Trade Organization, merchandise exports and imports account for approximately 6 and 31 percent of GDP, respectively, in The Bahamas. [1] Over the period 2010–2015, merchandise imports grew by 1 percent, but they declined by some 16 percent in 2015 as international petroleum and crude oil prices declined. During the half-decade period, exports declined by 6 percent and there was a significant loss of 39 percent in 2015 (Figure 1), in part due to a stagnant and declining market share in marine products. The Bahamas' market share in world exports fell by 5 percent for crustaceans and by 1 percent for mollusks.[2]

Figure 1:Trade (annual percent change)

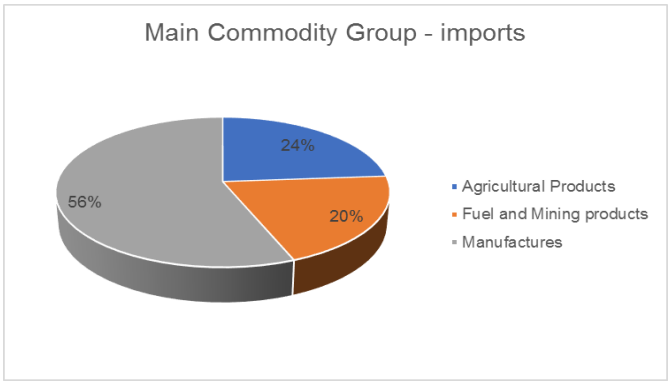


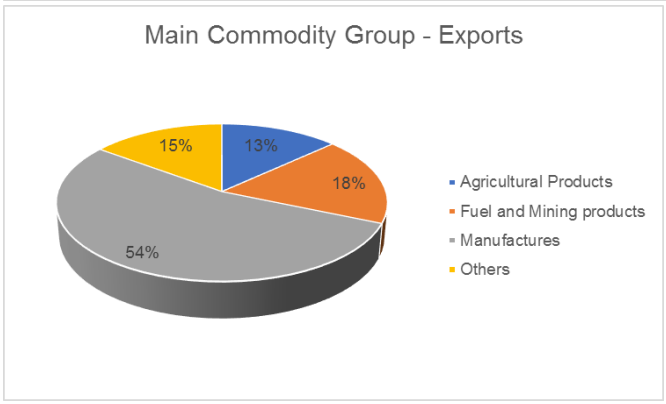
Source: World Trade Organization, 2015.
Note: c.i.f. = cost, insurance, and freight; f.o.b. = free on board.

The main commodity groups for merchandise imports and exports in The Bahamas are fuel and mining products, manufactures, and agriculatural products. More than 75 percent of imports and slightly below 72 percent of exports are concentrated in non-agricultural products (Figure 2).

Of the top imported products, petroleum oils and other crude account for over 20 percent of non-agricultural products (approximately 6 percent of total GDP), followed by motor cars and furniture and other parts at 4.2 and 2.7 percent, respectively. Leading exports as a percentage of non-agricultural products are polymers of styrene (19.6 percent), petroluem oils and other crude (15.9 percent), crustaceans (13.4 percent), heterocyclic compounds nitrogen (11.1 percent), and vessels for pleasure or sports (5 percent).

Figure 2: Imports and Exports, 2015 (percent)





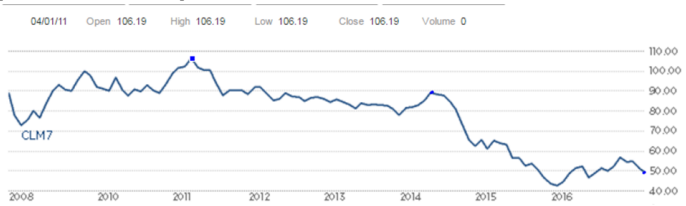
Source: World Trade Organization, 2015.

With no proven reserves of easily exploitable fossil fuel in significant quantities, The Bahamas remains highly dependent on imported petroluem oils and other crude for energy generation.[3] The inability to diversify the energy matrix has meant lost opportunities to reduce dependence on fossil fuels. Fluctuations in international prices therefore have a significant impact on current account balances and domestic prices. West Texas Intermediate (WTI) shows movements in prices from as high as US$140 per barrel (July 2008) to present levels of roughly US$50 (Figure 3).

Current lower fuel oil prices are having a positive impact on the economy. During the past five years, oil imports averaged almost 10 percent of GDP and just over a third of the trade balance. At the end of 2015, oil imports accounted for 6 percent of GDP (US$520 million). The country's external position improved and the current account deficit as a percent of GDP declined from 16 to 11 percent, largely driven by lower fuel imports (Figure 4). Expectations are that this trend will continue.

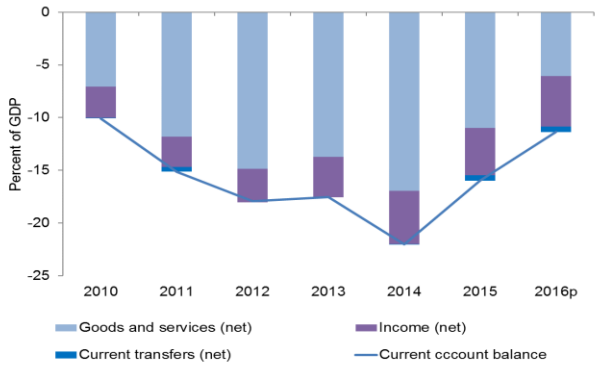
[1] http://stat.wto.org/CountryProfiles/BS_e.htm.
[2] https://comtrade.un.org.
[3] The Bahamas National Energy Policy (2013–2023).

Figure 3: West Texas Intermediate Crude Oil Prices (in U.S. dollars)



Source: http://data.cnbc.com. Electronic Jun 2017 (CLM7)

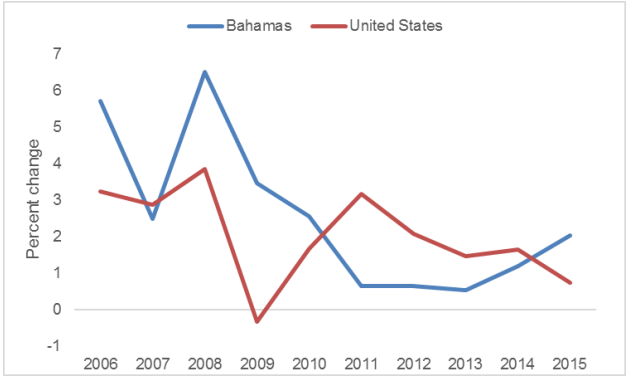
Figure 4: Current Account Balance (percent of GDP)



Source: Central Bank of The Bahamas.

Domestic prices in The Bahamas have a strong relationship with import fuel costs and U.S. inflation. Inflation rose to 6.5 percent in 2008, when oil prices were at US$140 per barrel, then declined to 2 percent in 2015 and 1 percent in 2016 (Figure 5). With low price expectations in the United States, short-term forecasts for domestic prices remain low.

Figure 5: The Bahamas and U.S. Inflation Retail Price Index (percent change)



Sources: Central Bank of The Bahamas; and the U.S. Federal Reserve Economic Database.

The Bahamas imports approximately US$599 million in goods, mostly in food, food preparations, and some alcohol-based goods representing roughly 22 percent of merchandise trade (or 7 percent of GDP). At the same time, The Bahamas exports only US$4 million in goods.[4] For the period 2010–2015, imports rose by an average of 4 percent and exports rose by 3 percent (Figure 6). The Bahamas is among the largest food importers in the Caribbean, behind only Jamaica, Trinidad and Tobago, and Haiti. The Bahamas has the second highest food-import-dependence ratio (total food imports/total food consumption) within the region at 0.92, which is 21 percentage points above the regional average.[5] This poses food security concerns for the medium term for the nation's economy.

For the period of analysis, international commodity prices mirrored the movement in fuel prices, with rising import levels until a recent moderation. Fluctuations in the small export basket of agricultural and animal products are responsible for significant movements in 2014 and 2015.

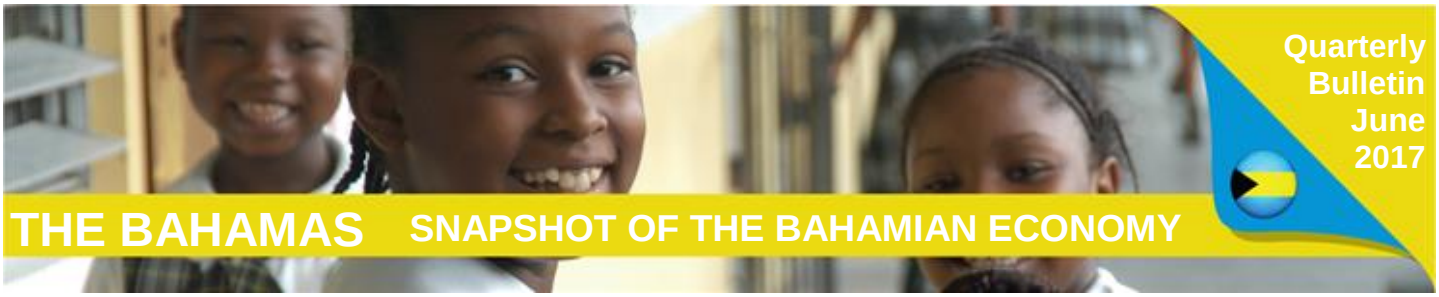
Figure 6: Agricultural Products (annual percent change)

Source: World Trade Organization, 2015.

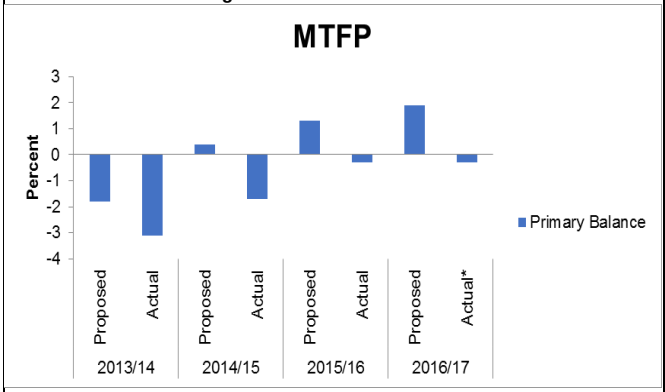
Conclusion

Petroleum and food imports are significant contributors to the overall merchandise import bill in The Bahamas (over 13 percents of GDP). The country's dependence on fossil fuels and food imports poses risks to economic sustainability and food security.

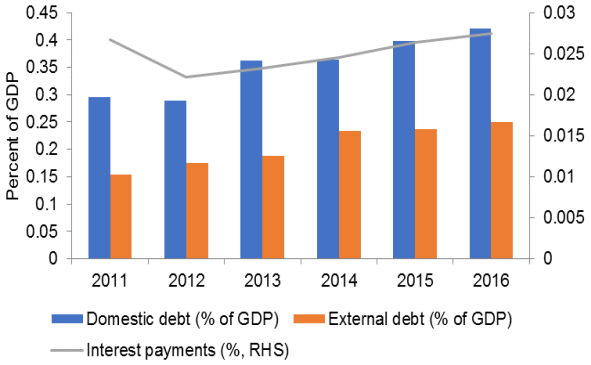
[4] http://stat.wto.org/CountryProfiles/BS_e.htm.
[5] Walters and Jones (2012). www.fao.org/3/a-i5131e.pdf



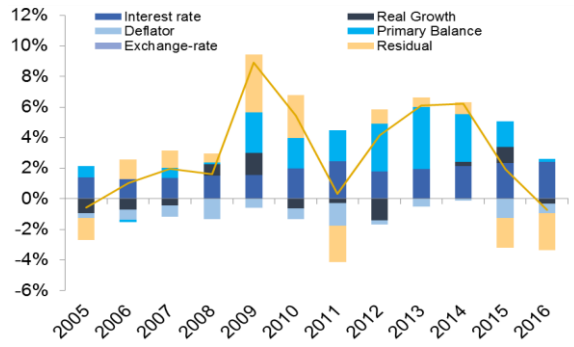
Medium-Term Fiscal Program



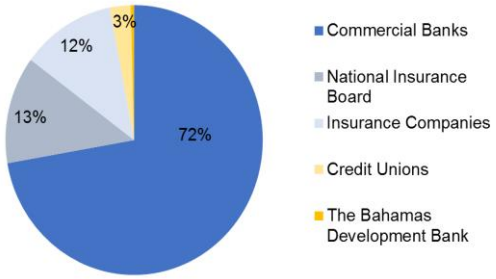
Debt



Debt Decomposition



Share of Domestic Assets



Sources: Central Bank of The Bahamas; Ministry of Tourism; and International Monetary Fund, *World Economic Outlook.*

Table 2: Selected Indicators for The Bahamas, 2012-2017

Social and Demographic Indicators (most recent year)						
GDP (US$ millions), 2017	9,345	Adult literacy				95.6
Per capita GDP (2015,US$)	23,903	Poverty rate (percent), 2014				12.8
Life expectancy at birth in years (2015)	76.1	Population (thousands), 2015				364
Rank in UNDP Development Index (2014)	55	Unemployment rate (Nov 2016)				11.6
Economic Indicators						
	2012	**2013**	**2014**	**2015**	**2016**	**2017**
(Annual percentage change, unless otherwise indicated)						
Real Sector						
Real GDP (% change)	3.1	0.0	-0.5	-1.7	0.0	1.4
Nominal GDP(% change)	6.5	1.5	1.1	2.7	2.2	3.7
Inflation (end of period)	0.7	1.0	0.2	2.0	1.0	1.6
Unemployment	14.4	15.8	14.6	13.4	14.5	13.2
(In percent of GDP, unless otherwise stated)						
External Sector						
Exports of goods and services	44.4	43.8	42.5	38.6	40.4	43
Imports of goods and services	59.3	56.3	61.3	47.1	44.1	44
FDI	6.3	4.5	2.9	1.3	2.4	2.8
Current account balance	-17.9	-17.5	-22.0	-16.0	-11.4	-12.2
Gross International Reserves (US$M)	810	742	788	812	902	854
In months of next year's imports	2.0	1.7	2.3	2.4	2.6	2.5
Central Government Operations	**2011/12**	**2012/13**	**2013/14**	**2014/15**	**2015/16**	**2016/17**
Revenue and grants	17.2	15.9	16.8	19.2	21.4	21.7
Total Expenditure	22.6	22.3	22.4	23.5	24.9	25.2
Overall balance	-5.3	-6.4	-5.6	-4.3	-3.5	-3.5
Primary balance	-3.1	-4.1	-3.1	-1.7	-0.3	-0.3
Memorandum items:						
National debt (in millions of $B)	4,362.8	4,995.7	5,590.1	6,284.5	6,653.4	7,042.4
In percent of GDP (including contingent liabilities)	55.3	60.7	65.6	72.9	75.2	76.7
Nominal GDP (in millions of B$)	7,890.0	8,399.0	8,522.0	8,618.0	8,854.0	9,177.0

Source: IMF WEO and Article IV, The Central Bank of The Bahamas, and the Department of Statistics.

Contributors: Juan Pedro Schmid and Kimberly Waithe

Overview

The government announced new fiscal measures to stop the debt build-up and to protect foreign reserves. Focusing on revenues, the measures represent an adjustment equivalent to 5 percent of GDP.

The fiscal consolidation will affect economic growth. The authorities expect economic growth to be 0.5 percent lower than projected in 2017 due to the fiscal measures, but the economic performance will also depend on external factors and reactions of the private sector.

Tourism and construction activity continue to drive economic output at the end of the first quarter of 2017. Consistent tourism demand and low international oil prices have benefited the Barbadian economy but international reserves remain under pressure in spite of a small increase to 10.7 weeks of imports.

Recent Developments

The Barbadian economy grew by 2 percent at the end of the first quarter of 2017. This out-turn is similar to the performance recorded a year earlier of 2.3 percent. The expansion was primarily due to strong tourism performance, as value-added grew by 3 percent. Long-stay arrivals rose by 4.4 percent to reach 192,000 visitors, but the length of stay declined during the quarter, limiting growth in tourist receipts to around 2.6 percent. The growth in arrivals came from the United States and Canadian markets, which rose by 16.4 percent and 11.1 percent, respectively. However, arrivals from the United Kingdom declined by 1.6 percent, as this market continues to face uncertainty and a weaker currency. Cruise passengers also grew during the quarter by around 9 percent. The nontradable sectors grew by 1.2 percent, with construction activity growing by 2 percent, buttressed by the on-going construction of Sandals Royal. Wholesale and retail and finance and other services also saw increases of 1.2 percent and 2 percent, respectively.

The country's fiscal deficit declined to an estimated 6 percent of GDP at the end of FY 2016/17. This is slightly higher than the target of 5.8 percent of GDP in the August 2016 budget, but an overall improvement from the deficit of 8.2 percent of GDP recorded a year earlier. This performance was attributed to higher tax collections, as total revenue grew by 7 percent to reach US$1,385.9 million or 30 percent of GDP. Direct tax revenue grew by 7.6 percent, boosted by increases in personal taxes (16.5 percent) and corporate taxes (6.9 percent). At the same time, indirect taxes were bolstered by increased value-added tax (VAT) receipts (10.1 percent) and the National Social Responsibility Levy (NSRL),[1] which was introduced in the 2016 budget and collected US$12.5 million. Total expenditure grew marginally by 0.2 percent to reach US$1,663.9 million or 36.4 percent of GDP. While transfers and subsidies witnessed a small decline of 0.4 percent, interest payments grew by 8.4 percent. Public debt remained elevated at an estimated 143 percent of GDP, including National Insurance Scheme (NIS) holdings, as at end-March 2017.

Highlights

- *Real GDP grew by 2 percent at the end of March 2017.*
- *The fiscal deficit fell to an estimated 6 percent of GDP at the end of FY2016/17.*
- *Reserves increased to 10.7 weeks of imports or US$352.7 million.*

The Financial Statement and Budgetary Proposals for FY2017/18 was presented to the House of Assembly on May 30, 2017. With the broad objectives to protect the level of foreign reserves, intensify the fiscal adjustment process, and stop the growth of the national debt, the government announced new fiscal measures that aim for a balanced budget or a small fiscal surplus of US$2.2 million for FY2017/18, equivalent to a primary surplus of around 7 percent of GDP. In comparison, the deficit stood at US$278 million or 6 percent of GDP, with a primary surplus of 1.9 percent of GDP at the end of FY2016/17.

Measures focus on the revenue side with new taxes and a tax amnesty for arrears. Some of the main revenue-raising initiatives announced included:

- The *National Social Responsibility Levy* is set to increase from 2 to 10 percent on all taxable imports and domestically produced goods effective July 1, 2017. It is estimated that the levy will collect US$109 million (2.3 percent of GDP) for the remainder of the fiscal year.
- A *Commission on Foreign Exchange* will be charged on all sales of foreign currency at a rate of 2 percent. This will include all wire transfers, credit card transactions, and over-the-counter sales of foreign currency. It is estimated that the commission will collect US$26 million over the remainder of this fiscal year or 0.5 percent of GDP.
- *An increase in the excise tax on gasoline and diesel,* effective June 1, 2017, will increase the prices by US 12.5 cents per litre from US 37 cents to US 50 cents for gasoline and by US 12 cents per litre from US 10 cents

[1]The NSRL was introduced on September 1, 2016.

to US 22 cents for diesel. It is estimated that the excise tax will collect US$25 million over the remainder of this fiscal year or 0.5 percent of GDP.

- *Tax amnesty* for arrears across the tax categories of the VAT and land tax will be in place for the period from June 1 to November 30, 2017. It is estimated that the amnesty will collect US$12.5 million over the remainder of this fiscal year, or 0.3 percent of GDP. In addition, the government is expected to divest the Barbados National Terminal Company Ltd. and Hilton Hotel at Needham's Point at net proceeds of US$35 million and US$50 million, respectively.

Expenditure cuts should yield 0.9 percent of GDP in savings. The Budget Speech announced a 10 percent cut across the board in the existing approved Estimates of Expenditure for FY2017/18. Spending such as debt service, salaries, and pensions is excluded from the cut, which is estimated to yield US$41 million (0.9 percent of GDP) in savings.

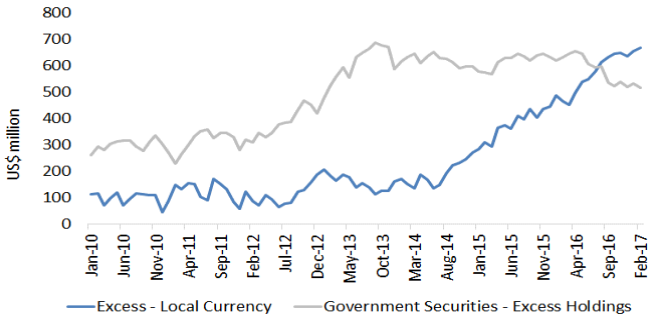
The government is seeking to re-profile part of the domestic debt. A possible debt swap with the National Insurance Scheme and the Central Bank of Barbados (CBB), which are major holders of domestic securities, could result in a possible US$35 million (0.7 percent of GDP) reduction in interest costs. However, the operation would also negatively affect both entities' balance sheets.

The external position recorded a surplus of US$21.9 million or 1.8 percent of GDP at the end of March 2017. This is relative to the surplus of US$29.2 million (2.5 percent of GDP) recorded a year earlier. Higher travel receipts (2.6 percent) were offset by an increase in retained imports of 6.6 percent, which included an increase of 13.2 percent in fuel imports. At the same time, reserves stood at US$352.7 million (10.7 weeks of imports), an increase compared with US$340.6 million at the end of December 2016. Tourism receipts contributed to this modest increase, but on-going delays in starting private sector investment projects and in the sale of government assets hampered overall growth in reserves.

Barbados' financial sector is stable and liquid, but private credit remains subdued. Excess liquidity in the banking system increased to 17 percent, compared with 10.6 percent in the first quarter of 2016, in part due to some commercial banks opting to reduce some of their holdings of government paper for cash at the CBB (Figure 1). However, credit to the nonfinancial private sector remained weak and stood at 1 percent at the end of March 2017, while domestic deposits grew marginally by 2 percent. The weighted average deposit rate edged down to 0.3 percent, while the average loan rate stood at 6.7 percent in the first quarter of 2017. This has been the trend since April 2015, when the CBB removed the minimum savings rate that stood at 2.5 percent, thus allowing commercial banks and other deposit-taking institutions to determine the rates.

The CBB has tightened monetary policy, announcing that effective June 15 commercial banks will be required to hold 15 percent of their domestic deposits in stipulated securities. This move is the first increase since 2007, when the ratio was reduced to 10 percent. Cash reserve requirements for commercial banks (5 percent) and for deposit-taking trust and finance companies and merchant banks would remain unchanged. This move reflects the government's aim to address the size of the deficit and how it is financed, and reverse the trend of increasing excess reserves mentioned above.

Figure 1. Commercial Bank Excess Reserves



Source: Central Bank of Barbados.

Outlook

Barbados remains in a vulnerable position. The growth outlook is positive but modest with estimates ranging between 1.5 and 2 percent by the end of 2017. Fiscal consolidation, while necessary for fiscal and debt sustainability, will negatively affect growth but could be offset by increased activity in tourism and construction. Tourism performance would be driven by the continued recovery across the main source markets and the additional airlift. However, growth prospects could be hampered by delays to private sector investment projects slated for 2017 and the on-going uncertainty around the weakened British pound.

High-Frequency Macroeconomic Indicators				
	Last Data	Period	Prior Data	Period
Annual GDP growth (%)	2.0	Mar-17	1.6	Dec-16
Tourism arrivals (annual % change)	4.4	Mar-17	6.3	Dec-16
Nonperforming loans (%)	8.9	2016 Q4	9.4	2016 Q3
Foreign Exchange Reserves cover,weeks	10.7	Mar-17	10.4	Dec-16
Inflation(%)	1.3	Dec-16	0.8	Nov-16
Unemployment rate (%)	9.9	2016 Q3	10.2	2016 Q2

Source: Central Bank of Barbados.

Introduction

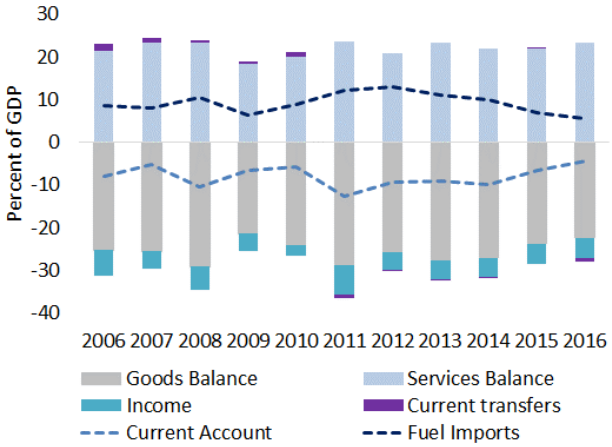
Over the last decade, fluctuations in commodity prices have had a significant impact on the Barbadian economy. Barbados is a highly open economy, with exports and imports on average equivalent to around 96 percent of GDP from 2006 to 2016. The degree of openness and the concentration on a few trading partners render the economy vulnerable to fluctuations in international commodity prices, downturns in the global demand for tourism, and policy changes abroad. Oil imports, which account for around 90 percent of energy needs, along with high and volatile energy prices, have increased the country's macroeconomic vulnerability. More recently, favourable external conditions buttressed by lower international oil prices have eased macroeconomic management.

Effect of Oil Prices

Barbados' external position has been impacted by fluctuations in international oil prices over the last decade. From 2006 to 2014, movements in oil prices increased external vulnerability. During that period, fuel imports accounted for an average of 26.4 percent of total good imports, peaking at 33.1 percent of total imports in 2012. Barbados produces some oil, but domestic demand (about 10,000 barrels per day) greatly exceeds local supply (about 1,000 barrels per day). This dependence makes the economy highly vulnerable to changes in international oil prices. At the same time, the country spent an average of US$434.7 million on fuel imports, which peaked at US$558 million (12.9 percent of GDP) in 2012. Since all refined oil products are imported, they have a negative effect on the trade balance and put pressure on the current account. From 2011 to 2014, when international oil and commodity prices rose to above US$100 per barrel, the current account deficit averaged around 10 percent of GDP, peaking at 12.2 percent of GDP in 2011 (Figure 2). However, with the recent moderation in oil prices to around US$50 a barrel, oil imports have declined to US$251 million or 5.5 percent of GDP and, subsequently, the current account deficit fell to 4.5 percent of GDP at the end of 2016.

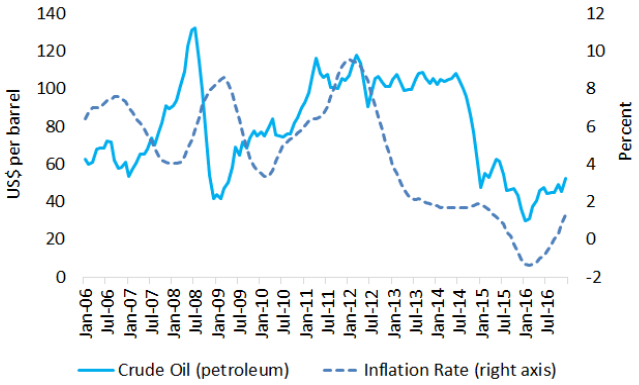
Inflation in Barbados is driven mostly by fluctuations in food and fuel prices. Given that the country imports most of its consumption, prices tend to follow those of its main trading partners, namely the United Kingdom and the United States, but with greater volatility than the variations in global commodity prices. The pass-through of imports to prices in Barbados is high and passed mostly to the consumer. During 2006 to 2012, higher global oil prices led to rising domestic prices for transportation and electricity, which are important inputs to production. This period saw an increase in inflation from 7.3 percent in 2006 to a peak of 9.4 percent in 2011, when international oil prices rose above US$100 per barrel (Figure 3). However, starting in 2013 there was a significant decline in inflation, averaging around 1 percent, owing to lower import prices.

Figure 2. Current Account Balance (percent of GDP)



Sources: Barbados Statistical Service; and the Central Bank of Barbados.

Figure 3. Inflation in Barbados and Crude Oil Prices



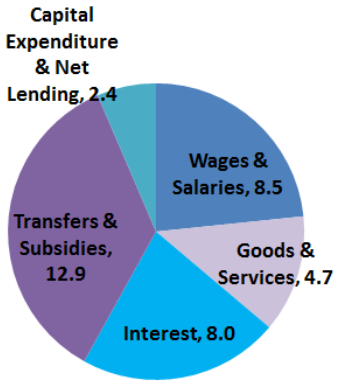
Sources: Barbados Statistical Service; and the Central Bank of Barbados.
Note: Crude oil (petroleum) represents the simple average of three spot prices: Dated Brent, West Texas Intermediate, and the Dubai Fateh.

Households and businesses have benefited from the recent moderation in fuel prices. Fuel is the largest item in the cost of production of electricity. It is estimated that around 50 percent of the electricity tariff is fuel cost, which is passed on to the final consumer.[2] The electricity bill accounts for around 15 percent of average monthly

[2] IDB Country Strategy for Barbados 2015–2018, April 2015.

income for low-income households. Over the last few years, lower fuel prices have led to a reduction in electricity tariffs. Information available from Barbados Light and Power (BL&P) indicates that through its fuel adjustment clause,[3] electricity tariffs fell by 52.8 percent, from US$ 44.5 cents/kWh in July 2014 to 21 cents/kWh in December 2016. The IMF's EBA-lite external sustainability analysis suggests that the Barbadian dollar may be overvalued by around 9.6 percent, which undermines competitiveness for the export sectors.[4] Lower energy costs and contained inflation improve the competitiveness of businesses from reduced input costs.

Figure 4. Composition of Expenditure, FY2016/17 (percent)



Sources: Ministry of Finance; and the Central Bank of Barbados.

Since Barbados is a net oil importer, its public finances are impacted by variations in international oil prices. In Barbados, fuel and electricity prices are not subsidized,[5] therefore the impact on revenues of variations in fuel prices are marginal. Gasoline, diesel, and fuel oil are imported by the Barbados National Oil Company Limited (BNOC). A value-added tax (VAT) of 17.5 percent and an excise tax[6] are charged when selling to the main retailers, Rubis West Indies Limited and Sol (Barbados) Limited. On the expenditure side, transfers are among the largest budget items, at 12.9 percent of GDP in FY2016/17 (Figure 4). Therefore, in the current environment of lower global oil prices, state-owned enterprises would benefit from lower operating costs, which could result in an improved financial position and reduced reliance on government.

Conclusion

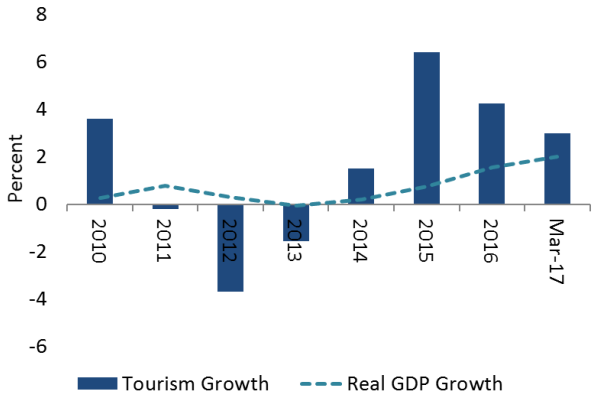
Given the adverse implications of high and volatile oil prices for the economy, pursuing initiatives geared towards renewable energy and energy efficiency is critical. The government of Barbados, in its National Sustainable Energy Policy, aims to increase the share of economically viable renewable energy in Barbados' energy mix, with an indicative target of about 29 percent of all electricity consumption to be generated from renewable sources by 2029. Moreover, as a means of reducing its dependence on fossil fuels, the government approved in 2012 a US$24.6 million Public Sector Smart Energy Program with specific objectives to install renewable energy systems in government buildings and retrofit these buildings and public lights with energy-efficient technologies; undertake a pilot project and studies to encourage the use of renewable energy; and assist with capacity-building, institutional strengthening, and public awareness in the energy sector.[7] The government also established an Energy Smart Fund through an IDB loan of US$10 million to "facilitate subsidized loans for the implementation of viable renewable energy and energy efficient projects along with grants to businesses for funding pre-investment studies, assessing the technical and financial viability of these projects."[8]

In 2016, the government approved an IDB loan of US$34 million for the Deployment of Cleaner Fuels and Renewable Energies in Barbados Program, with the main objectives to upgrade existing natural gas infrastructure and increase energy efficiency and renewable energy applications within the operations of the National Petroleum Corporation (NPC) and Barbados National Oil Company Limited (BNOCL).

[3] The fuel clause adjustment is a mechanism designed to recover the cost of fuel oil used in the generation of electricity. It adjusts the price that customers pay for each kilowatt hour of electricity as the cost of fuel used to generate electricity rises and falls.
[4] IMF Article IV, August 2016.
[5] The diesel subsidy, which was discontinued in April 2014, provided direct price support for consumption at 23 cents per litre for the manufacturing, agriculture, and fisheries sectors, as well as 08 cents per litre for public transportation.
[6] Gasoline and diesel are charged both the VAT of 17.5 percent and the excise tax, while fuel oil is charged only the VAT. In April 2014, an increase in the excise tax on gasoline of BDS$ 0.20 per litre became effective.
[7] The financing plan includes a US$17 million investment loan from the IDB and a US$7.6 million grant from the European Community.
[8] Ministry of Energy. http://www.energy.gov.bb/web/energy-smart-fund

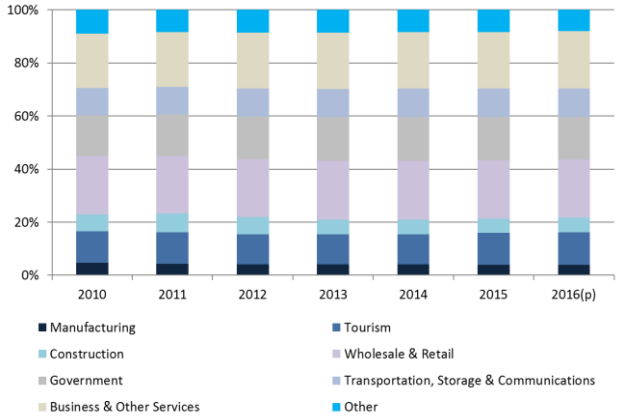
The gradual tourism recovery...

Figure A. Real growth and Tourism growth



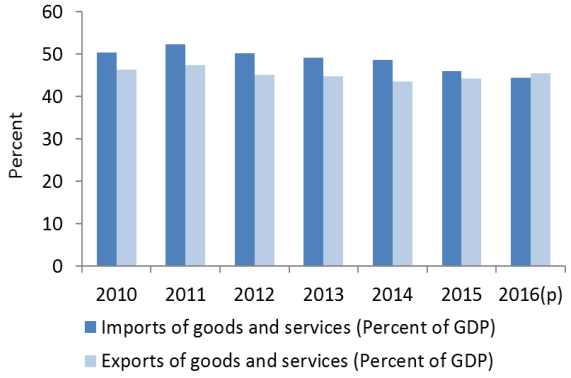
… is the driver of growth.

Figure B. Contribution to GDP (% GDP)



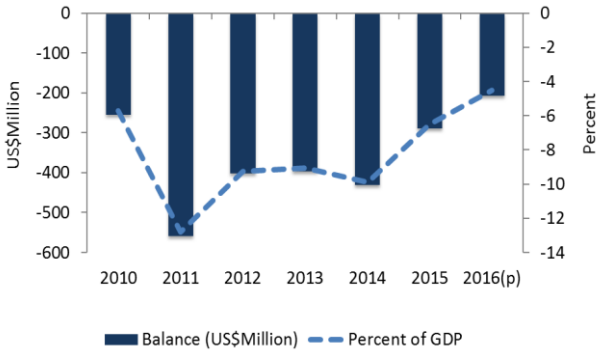
Lower oil and commodity prices...

Figure D. Exports and Imports (% GDP)



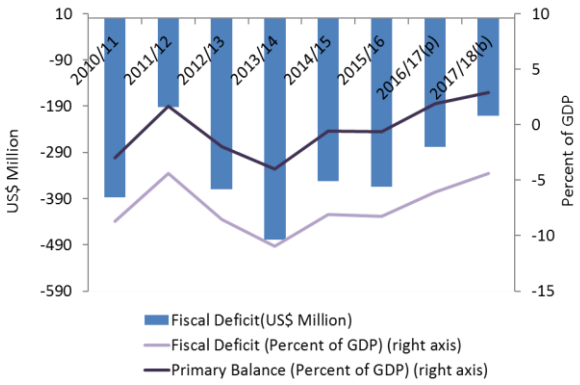
… also improved the current account balance

Figure E. Current account balance (% GDP)



But large sustained fiscal deficits…

Figure C. Revenues and Expenditures (% GDP)



…put further pressure on reserves.

Figure F. Gross reserves (US$ millions)

Sources: Central Bank of Barbados; International Monetary Fund, *World Economic Outlook* (April 2017); and the Ministry of Finance.
Note: (p) projected figures; (b) budgeted figures.

	2011	2012	2013	2014	2015	2016	2017(p)
(Annual percentage changes, unless otherwise indicated)							
Real sector							
Real GDP	0.8	0.3	-0.6	0.1	1.0	1.6	1.7
Nominal GDP	-2.0	-0.6	0.9	-0.4	1.6	3.4	2.7
Inflation (end of period)	9.4	4.5	1.8	1.8	-1.1	1.3	2.0
Unemployment	11.2	11.5	11.6	12.3	11.3	9.9	9.5
External sector							
Exports of goods and services (% change)	0.2	-5.3	0.2	-3.2	3.1	6.6	n.a
Imports of goods and services (% change)	1.9	-4.8	-1.2	-1.5	-3.9	0.2	n.a
Current account (percent of GDP)	-12.2	-8.7	-8.6	-9.4	-6.3	-4.5	-4.0
International reserves (US $millions)	707.4	728.9	572.1	526.2	463.5	340.6	352.7*
International reserves cover (weeks)	18.0	20.2	15.6	14.7	13.6	10.4	10.7*
(In percentage of GDP, unless otherwise indicated, on a fiscal year basis)							
Public sector							
Total revenue	29.3	28.4	26.7	27.7	29.3	30.3	30.7+
Total expenditure	33.7	36.9	37.7	35.8	37.5	36.4	35.1+
Central government primary balance	1.6	-2.0	-4.0	-0.6	-0.6	1.9	2.9+
Central government overall balance	-4.4	-8.5	-11.0	-8.1	-8.2	-6.0	-4.4+
Debt indicators							
General government debt	78.0	83.5	94.4	100.4	105.2	108.2	105.4*
General government debt (inclusive of NIS holdings)	105.3	113.6	127.3	134.8	140.7	145.7	143.0*
Central government debt over revenues	266.7	294.5	353.4	363.2	358.9	357.0	331.8*
External debt service as percentage of exports of goods and services	6.9	7.3	7.0	7.3	11.5	9.2	n.a

Sources: Central Bank of Barbados; International Monetary Fund, World Economic Outlook (April 2017); and the Ministry of Finance.
Note: (p) projected figures for 2017. NIS = National Insurance Scheme.
+ Budgeted figures for FY2017/18.
* Data as end March 2017.

Contributor: Mark Wenner and Dillon Clarke

Overview

Guyanese authorities estimate that the economy will grow in real terms at 3.8 percent by year-end 2017, 0.6 percent above the revised figure achieved in 2016. The two leading sectors for 2017 are expected to be mining and services. The government continues to rely on stimulus spending to increase aggregate demand, principally through an enlarged public investment program and higher levels of spending on transfers. In the first two months of 2017, GYD1.2 billion was spent, approximately 163 percent more than the same period in 2016. All categories of non-interest current expenditure have been higher, but transfers registered the largest change – 62.3 percent higher than the same period in 2016 – compared to the other two categories (wages and salaries, and purchases of goods and services). However, slowness in the execution of capital projects, ongoing weaknesses in the sugar and forestry sectors, and the generally negative public response to the expansion of value-added tax (VAT) coverage to education, water, and electricity services could affect consumer and private investment spending.

Recent Developments and Outlook

Through the early part of 2017, the mineral sector, and in particular gold, continued to stand out and is expected to the make the greatest contribution to economic growth in 2017. Gold production in both January and February exceeded corresponding levels for 2016. The two-month total came to 108,048 ounces compared to 94,432 ounces in 2016. Higher gold prices seem to be stimulating small and medium-sized mining enterprises to declare more, in contrast to the decline in declarations for the two large foreign-owned mines. Gold prices in the first two months of 2017 ranged from US$1,159.20 per ounce on January 2 to U$1,255.60 on February 28, compared to a comparable range of US$1,063.70 and US$1,230.10 in the corresponding 2016 period.

Unlike gold, bauxite production contracted by 18.3 percent in the first two months of 2017 on a year-to-year basis. Production was 229,441 metric tonnes (mt) in the first two months of 2017 compared to 280,901 mt in the previous period. The outlook for bauxite remains uncertain for the rest of the year. On one hand, consumption of aluminum, the finished product, in general is rising. On the other hand, implementation of new environmental regulations on coal-fired aluminum smelters in China, the world's largest producer and consumer of aluminum and the driver of the market, may generate downward price pressure. Aluminum consumption in the rest of the world has been generally flat dating back to 2012. In the first quarter of 2017, the average price for aluminum was US$1,851 per mt compared to US$1,514 per mt in the first quarter of 2016, representing a 22 percent price improvement largely driven by China. Guyana is a producer of high-quality calcined bauxite and should be favoured if total world demand for aluminum holds for the rest of the year.

Highlights

- *More oil discovered. On March 18, 2017, ExxonMobil successfully drilled its sixth well, Snoek, and found high-quality oil. Other sites with promising geological features similar to the oil-bearing reservoirs discovered remain to be explored by ExxonMobil in the area that its controls.*
- *Gold continues to buoy the economy as other primary sectors lag through the early part of the year.*
- *The Ministry of Finance will review tax policies and issues in time for presentation of the 2018 Budget Estimates in November in response to complaints about the expansion of value-added tax coverage.*

Agriculture, forestry, and fisheries production has had a mixed record. The sugar sector continues to underperform and is the lagging sector in the new year despite an increase in the world price**.** As of February 2017, sugar production was 29 percent off the corresponding level for 2016 (3,669 mt versus 5,151 mt), when production during the first half of the year was affected by an El Niño-related drought. So far in 2017, strike actions, suspended production at Skeldon, and the consolidation of sugar estates combine to explain the reduction in output. According to the World Bank's Commodity Outlook Report, the average world price of sugar improved from US 14 cents per pound in the first quarter of 2016 to US 18.63 cents in the first quarter of 2017. However, this is still far below the Guyanese average cost of production, which ranges from US 38 cents to US 45 cents per pound.

The Guyana Rice Development Board (GRDB) is reporting 518,667 metric tons of paddy harvested from 220,640 acres for the first crop of 2017, which is 26 percent abouve the corresponding period last year. Nonetheless, exports of the first crop have summed to 239,442 metric tons, 60,000 metric tones less than the corresponding period last year. However, the U.S. Department of Agriculture's Foreign Agricultural Services estimates milled rice[1] total production for the full year will be 560,000 mt as of June 2017, down 16 percent from the previous year. The GRDB reports that the acreage

[1] Note there is a difference between paddy, rice in the husk, and milled and polished rice without the husk which has less weight.

planted for the first crop was 225,000 acres, which is above the 180,000 acres planted for the same period last year that was affected by El Niño, and the target set of 210,000 acres. The larger planted area reflects better weather conditions in the first quarter compared to the same period last year. GRDB also notes that farmers seem to be placing a renewed emphasis on improved high-yield and aromatic varieties with high margins as a means to improve producer incomes. World rice prices, however, have declined at both the one-month level and the 12-month level. In the first quarter of 2016 Thailand 5% rice was $379 and Vietnam 5% rice was US$361.7, two benchmark grades commonly used. In the first quarter of 2017, those average prices fell to US$371.3 and US$338.5, respectively. These lower prices could affect acreage planted in the second half of the year and put pressure on both millers' and producers' rates of return. The cost of milling rice in Guyana is not as competitive as some of the major rice exporters.

In forestry, production fell to 37,074 cubic meters year-to-year to date compared to 51,052 cubic meters in February 2016. The reasons for the decline were subdued world demand and non-renewal and repossession of concessions held by two foreign companies for failing to add value to forestry operations. Fisheries production is also down. Shrimp and prawn exports fell 41.8 percent in February 2017 year-to-year.

ExxonMobil continues to add to its oil reserves. On March 18, 2017, the company safely drilled its sixth well, Snoek, and found another significant reserve of high-quality oil. However, the amount is not quantified as further assessments are ongoing. Guyana, nonetheless, seems to have added to its technically recovered reserves of 1.4 billion barrel equivalents calculated for the Liza 1, 2, 3, and Payara 1 wells. A production license was applied for in March and commercial extraction of oil from Liza 1 is expected to start sometime between mid-2020 and early 2021, with other oilfields coming online over time. The possibility of exploiting the gas found for domestic electricity generation is also emerging as a point of negotiation. This change of plan would imply laying a pipeline on the seabed from the well sites to the coast and constructing a gas-to-power conversion plant. Using natural gas would represent a lower cost option and imply lower carbon dioxide emissions compared to continued reliance on liquid fossil fuels, which are currently used for 83 percent of thermal generation of electricity.

Fiscal policy continues to be expansionary. The central government is raising even more revenue than before due to more aggressive arrears collection and excise taxes on petroleum products. But it is spending at an even faster pace, which implies increasing fiscal deficits. As of February 2017, year to date current revenues were GY$21.4 billion compared to GY$17.4 billon collected during the same period in 2016, while central government expenditure totalled GY$14 billion compared to GY$10.9 billion in the same period in 2016. But while current revenue gains outpaced current expenditures, capital expenditures were 163 percent above the previous period. The fiscal deficit in 2016 was -5.4 percent of GDP and is expected to increase to -7.4 percent in 2017.

While inflation has remained low, it has increased somewhat compared to the previous period. The cumulative 12-month inflation rate rose 3 percent from February 2016 to February, 2017. What seems to be driving higher inflation are food prices, medical care, transport, and communications. In response to criticisms of the government's recent tax policy changes, especially extending the VAT to private education tuition and fees, the Ministry of Finance has agreed to a review prior to the 2018 Budget Estimate presentation.

Monetary policy continues to be accommodative but the financial system continues to slow credit expansion as asset quality deteriorates. Money supply continues to expand. M2 increased by 4.8 percent over the 12 months ending in February. However, the financial system, concerned about lending risk, seems to prefer liquid investments and has slowed credit expansion. As of February 2017, liquidity rates, as measured by currency divided by M2, was 41 percent. The non-performing loan average for commercial banks is still high (last reported at 13.1 percent as of December 2016), and there has been negligible private sector credit growth (1.2 percent growth over the first quarter of 2016). On currency markets, as of March 2017 the official exchange rate remained at GY$206.5 to the U.S. dollar, unchanged from 2014, but parallel market rates have been reported to be slightly higher, ranging from GY$215 to GY$218.

Conclusion

Guyana's growth outlook over the medium term remains positive, but structural weaknesses and vulnerability to external shocks still loom as fiscal buffers erode. While debt-to-GDP ratios are low relative to Caribbean counterparts, protracted fiscal expansion impacts imply higher debt loads and heighten the need for fiscal consolidation, better budget creditability, and stronger institutional capacity.

High-Frequency Macroeconomic Indicators

	Most Recent Data	Period	Prior Data	Period
Annual GDP growth (%)	3.3	2016	3.2	2015
Exports (12-month growth)	19.2	2016	-1.4	2015
Imports (12-month growth)	4.4	2016	-16.7	2015
Private sector credit growth (%)	4	2016	6.2	2015
Inflation	1.3	2016	-1.8	2015
Exchange rate (end of period)	206.5	2016	206.5	2015

Source: Bank of Guyana.

Introduction

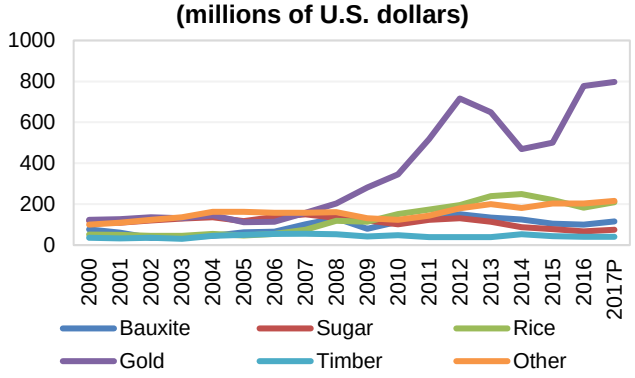
Guyana is a primary commodity exporter dependent on six products – gold, bauxite, rice, sugar, timber, and fisheries – for more than 80 percent of exports. Together, mining and agriculture constitute approximately 33 percent of GDP and account for an estimated 23 percent of the total active labour force, according to the International Labour Organization. Through backward and forward linkages, the two sectors stimulate distribution, retail, and construction service sectors. During the super-cycle commodity boom that started in 2002/03 and ended in 2013/14, Guyana benefited directly from the increase in external demand for its primary commodities. The export-led boom, combined with debt forgiveness, helped to sustain 11 years of consecutive positive real growth starting in 2006. Commodity producers, however, tend to be exposed to commodity price fluctuations that affect revenue streams and result in volatile public sector expenditure patterns. In addition, the long gestation period needed to develop mines and forestry operations can also lead to erratic flows in foreign direct investment. Investments are made when mineral and timber prices are high, but by the time the mines and concessions are operational, price and market conditions may have weakened, contributing to procyclical investment inflows. Consequently, the more open and dependent the economy is on commodities, the more likely the growth pattern of the country will be volatile. Accordingly, fiscal management in resource-rich countries tends to be more problematic.

Unlike many other commodity producers, Guyana was able to overcome volatility and maintain steady growth, especially after 2008–2009. The reasons were twofold: debt relief (US$460 million) in 2006, and the signing of a generous PetroCaribe rice-for-oil compensation arrangement with Venezuela that lasted from 2009 to 2015. Debt relief allowed government authorities to invest in more social and infrastructure spending than would have been the case. In addition, the Venezuelan premium valuation of Guyanese rice imports over world market prices stimulated the rice industry, and the generous financing helped reduce debt servicing requirements. If not for the PetroCaribe program, current account deficits would have been much higher than observed. Since the end of the commodity super-cycle and the PetroCaribe arrangement, Guyana has continued to grow due to continued strength of the gold sector and the dramatic drop in oil prices that started in mid-2014 and has reduced the share of fuel and lubricants in total imports from approximately 33 to 18 percent. Lastly, the effect of the announcement of an oil discovery in 2015 will spur an increased inflow of foreign direct investment, and economic growth is expected to increase markedly once production starts in 2020–2021.

External Accounts and Commodities

As can be seen in Figure 1, commodity exports generally moved upward after 2002, as China's rapid industrialization fuelled strong demand for all sorts of raw commodities. After 2008/09, Guyana's exports increased markedly, peaking in September 2011 when gold prices hit $1,923 per ounce. The gold-led export boom was due to flight to quality and safe assets that occurred in the aftermath of the 2007/08 global financial crisis. As housing and equity markets crashed, gold investments became a refuge. Conversely, as equity and housing markets recovered in 2012 and 2013, gold prices declined and so did Guyana's gold exports. Political and economic uncertainty in the world economy – including from Great Britain's decision in June 2016 to leave the European Union ("Brexit") – helped gold producers such as Guyana by contributing to a rebound in gold prices and in turn total export value. In addition, two large-scale and very efficient foreign-owned mines started operations in 2015 and ramped up production in 2016. These two large firms represented approximately 35 percent of declared gold production in 2016.

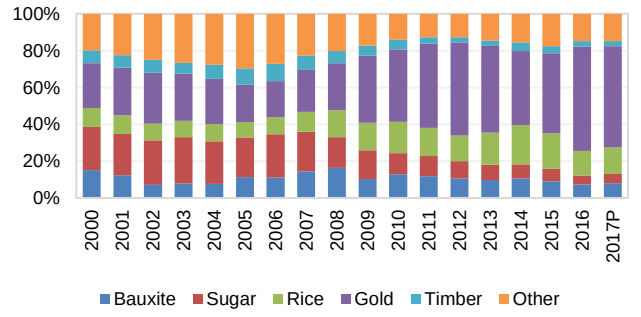
Figure 1. Evolution of Commodity Exports (millions of U.S. dollars)



Sources: International Monetary Fund, *World Economic Outlook;* and Bank of Guyana.

Figure 2 shows that gold exports have come to play an ever more dominant role in generating Guyana's export earnings since 2008. In 2017, gold is expected to constitute close to 54 percent of total exports and account for 22 percent of GDP, while sugar, the traditional mainstay, has diminished in importance and is now expected to constitute 5 percent of total exports in 2017 and approximately 2 percent of GDP. Rice, the second most important export earner over the 2009–2014 period, rose to constitute an 8 percent share of GDP but has since retreated, and in 2017 is expected to account for a 6 percent share of GDP. Bauxite and timber have downward trends as contributions to GDP as world demand has become subdued.

Figure 2. Commodity Exports (percent of GDP)

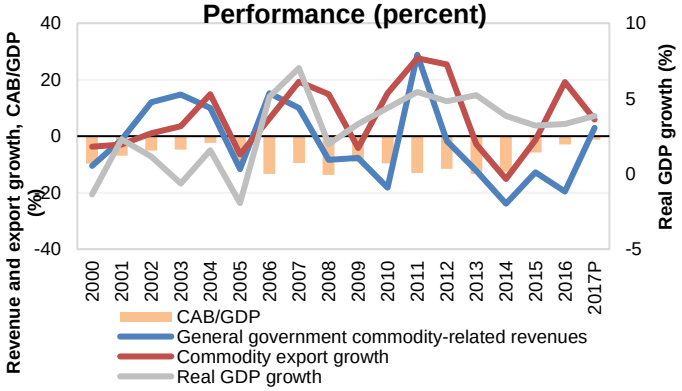


Sources: International Monetary Fund, *World Economic Outlook;* Bank of Guyana.

Fiscal Accounts

As can be seen in Figure 3, government commodity-related revenue has closely tracked commodity export growth. Likewise, the current account balance has generally improved when commodity export growth trends were upward and vice versa. The coefficient of variation (standard deviation/mean) for government commodity-related revenue for three separate periods indicates increasing variability. For the years 2000–2005, a period prior to the start of the super-cycle commodity boom and just at the start of the boom, government commodity-related revenue had a coefficient of variation of 0.46. For the years 2006–2010, a period marked by debt forgiveness, the global financial crisis, and the signing of the PetroCaribe rice-for-oil arrangement, the coefficient of variation was .48, close to the measure for the earlier period. However, for the period 2011–2016, the spread increased to 1.92, significantly higher than the two previous periods. This higher level of variation will have implications for fiscal policy.

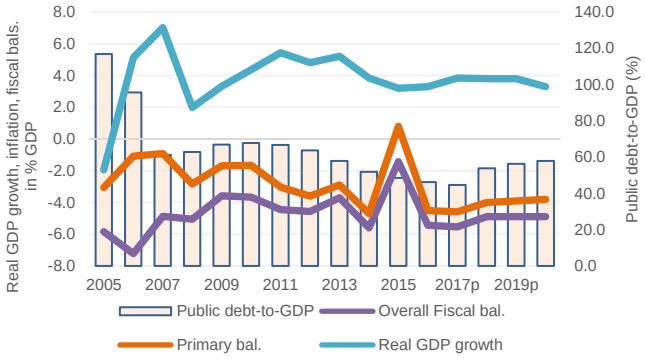
Figure 3. Commodity Export and Revenue Performance (percent)



Sources: International Monetary Fund, *World Economic Outlook;* Bank of Guyana.
Note: CAB = current account balance.

During the peak period of commodity-related government revenue capture from 2010–2012, the government continued to run fiscal deficits. As can be seen in Figure 4, the government spending pattern has been consistently procyclical. A more prudent policy would have been to reduce fiscal deficits during "boom" years and attempt to generate public savings that could then have been used for countercyclical spending during the "lean years" of low commodity prices.

Figure 4: Fiscal Balance and Public Debt Indicators (percent)



Sources: Ministry of Finance; and International Monetary Fund, *World Economic Outlook.*

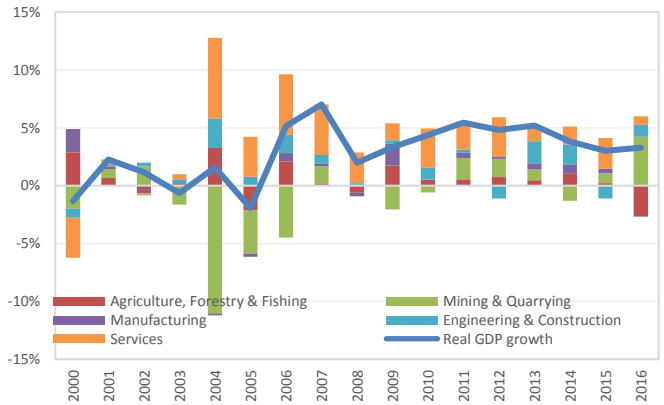
Economic Growth Effects

A decomposition of growth indicates that the mining sector has contributed to positive growth since 2010. In the mid-2000s, mining made negative contributions largely due to the closing of the large-scale Omai gold mine in 2005. The next year, gold output fell 26.5 percent. Eventually small and medium-scale miners ratcheted up production, and with the sharp rise in gold and bauxite prices thereafter, the contribution of mining to growth increased until 2014.

Outlook

Looking over the medium term, the price perspective is mixed. Gold, sugar, and coconut oil prices are expected to fall, while bauxite, rice, oil, and natural gas prices are expected to rise. Note however, that the expected increases in prices for logs, oil, and rice are moderate. In 2020 and 2021, Guyana is expected to become an oil producer. Gas will be re-injected into the wells but is not likely to be commercialized until a much later date. Coconut oil is included to represent the fortunes of non-traditional agricultural exports. At present, coconut nuts and coconut water are the third leading agricultural export.

Figure 5: Decomposition of Sectoral Contributions to Growth (percent)



Source: Ministry of Finance.

Table 2: Forecasted Prices for Commodities Relevant to Guyana

Commodity	Forecast Prices					
	Unit	2017	2018	2019	2020	2021
Gold	US$/toz	1,249	1225	1206	1187	1169
Aluminium	US$/mt	1800	1828	1856	1885	1915
Rice, Thai 5%	US$/mt	385	389	393	397	401
Sugar, world	US$/kg	0.4	0.4	0.4	0.39	0.39
Logs, Malaysia	US$/cum	275	280	284	289	294
Crude Oil,	US$/bbl	55	60	61.5	62.9	64.5
Natural Gas	US$/mnbtu	3	3.5	3.6	3.7	3.8
Coconut Oil	US$/mt	1600	1584	1567	1551	1536

Source: World Bank, Commodity Outlook Report (April 2017).

Conclusions and Policy Recommendations

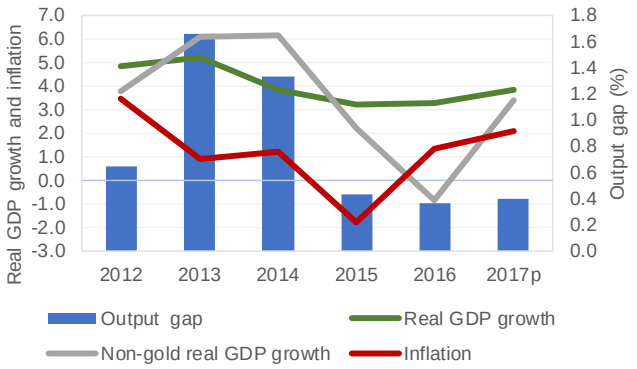
Guyana has benefited from the super-cycle commodity boom. However, as commodity prices have generally declined since 2013, the economy has become more reliant on a single commodity – gold – to sustain positive growth. Looking over the medium term to 2021, the price forecasts for main current exports and non-traditional ones show moderation (Table 2).

As a primary commodity exporter, Guyana should improve its ability to manage resource flows and build resilence. Resource-dependent governments in general tend to have procyclical spending patterns and face the prospects of large and persistent downturns when prices for their principal commodity exports collapse. This volatility can destabilize fiscal policy and weaken economic growth prospects. In addition, exchange rate appreciation and rent-seeking behaviours tend to be associated with commodity extraction. They reduce export competitiveness and foster non-transparency. To address these challenges, it would help to adopt fiscal rules and redoubt efforts to strengthen institutions.

In addition, the pace of preparations for the advent of oil and gas commercialization could quicken so that the benefits of this new bonanza can be prudently spent and distributed. At the same time, several export related challenges have to be addressed, including what to do with declining traditional export sectors, how to promote and diversify into new exports, and how to add value and sophistication to its exports.

Strong gold performance averts recession…

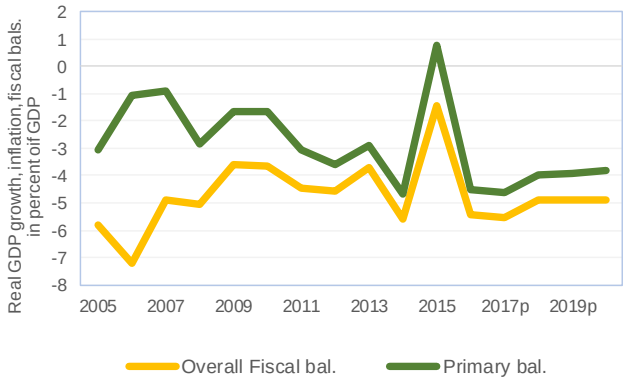
Figure a: Real GDP Growth and Inflation



Source: Ministry of Finance, and IMF WEO October 2016.

Meanwhile, authorities' fiscal expansionary policy quickly deteriorates fiscal balance.

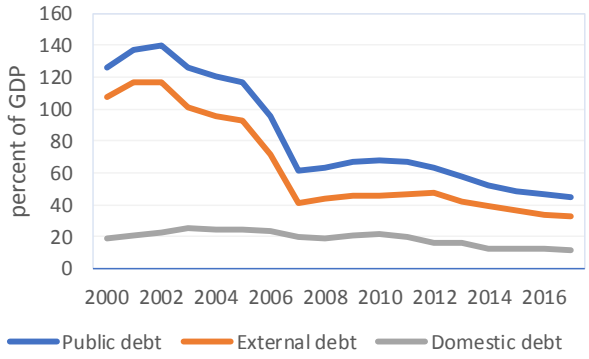
Figure b: Fiscal Overview



Source: Ministry of Finance, and IMF WEO.

However, debt-to-GDP ratios remain below historical levels.

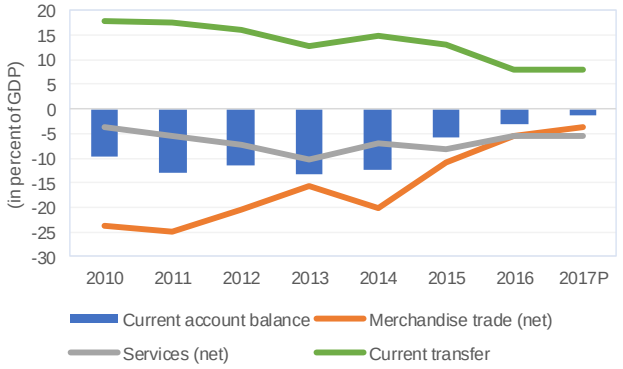
Figure c: Public Sector Debt



Source: Ministry of Finance, and IMF WEO.

High gold exports and lower import prices improved terms of trade…

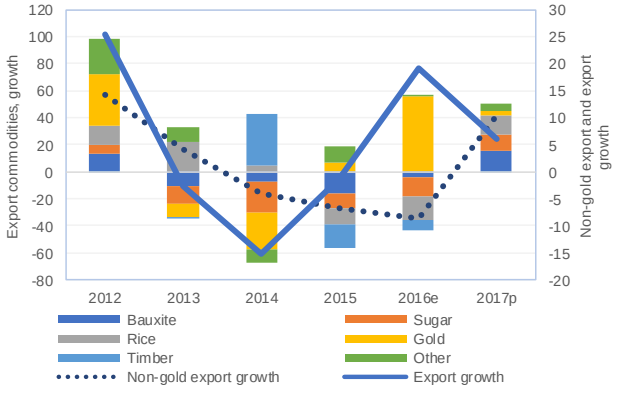
Figure d: Current Account Components



Source: Bank of Guyana and Ministry of Finance.

…despite weak performance form other export sectors.

Figure e: Export performance (annual percent change)



Source: Bank of Guyana, Ministry of Finance, and IMF.

	2013	2014	2015	2016	2017 (P)
(Annual percentage changes, unless otherwise indicated)					
Real sector					
Real GDP	5.2	3.8	3.0	2.6	3.8
Nominal GDP (GYD millions)	614100.0	635300.0	653300.0	707300.0	N/A
Inflation (end of period)	0.9	1.2	-1.8	1.3	2.5
External sector					
Exports of goods	-2.8	-15.2	-1.4	19.2	6.0
Imports of goods	-7.5	-3.0	-16.7	4.4	2.2
Current account (percentage of GDP)	-13.3	-12.5	-5.7	-3.0	-3.0
Remittances (percentage of GDP)	12.7	14.9	13.2	8.1	8.1
FDI (percentage of GDP)	7.2	8.5	4.0	4.2	3.8
(In percentage of GDP, unless otherwise indicated, on a fiscal year basis)					
Central government					
Revenue and grants	23.4	23.0	24.9	24.7	24.4
Current expenditure	19.7	21.1	22.6	24.5	24.4
Capital expenditure and net lending	8.6	8.2	4.7	6.7	7.4
Primary balance	-2.9	-4.7	0.8	-4.5	-4.6
Overall balance	-3.7	-5.6	-1.4	-5.4	-5.6
Debt indicators					
Central government debt	57.9	51.9	48.6	46.3	44.7
External public debt (end of period)	41.8	39.5	36.1	36	32.9

Source: Central Bank of Guyana, World Economic Outlook, IMF (October, 2016).

Notes: (P) denotes projected figures. FDI= foreign direct investment.

Contributor: Juan Pedro Schmid

Overview

Jamaica's economy remains stable. The Executive Board of the International Monetary Fund (IMF) concluded the first review under the precautionary Stand-By Arrangement (SBA) in April 2017, reporting continued strong program implementation and sustained positive economic growth estimated at 1.7 percent for FY2016/17 with an acceleration in later years.

Highlights

- *The IMF completed the first review under the precautionary SBA in April 2017.*
- *The macroeconomic environment remains positive.*
- *A conducive external environment, including a decline in international commodity prices, has supported Jamaica's recovery.*

Recent Developments

The SBA continues the reforms under the IMF's Extended Fund Facility (EFF). The 36-month program, amounting to SDR 1,195.3 million[1] (about US$1.63 billion), was approved by the IMF's Executive Board on November 11, 2016. Following the conclusion of the first review, accessible resources increased by SDR 126 million to SDR 426.1 million (equivalent to around US$580 million). The IMF reported strong program implementation but emphasized the importance of maintaining the reform momentum, including reducing wage costs for public sector workers. Additional reform areas include rebalancing from direct to indirect taxes, strengthening the social safety net, and reallocating public resources to infrastructure spending. These measures should facilitate economic growth, job creation, and social protection. The primary surplus is projected to remain at 7 percent of GDP for the medium term.

The new budget maintains the 7 percent of GDP primary surplus target but contains rebalancing. On the revenue side, the implementation of the JM$1.5 million income tax threshold was offset by special consumption taxes and other indirect taxes. In terms of expenditures, both capital expenditures and social expenditures increased in real terms compared to FY2016/17. Public sector salaries and interest payments continue to absorb the lion's share of the budget, accounting for 33 percent and 25 percent of total expenditures, respectively.

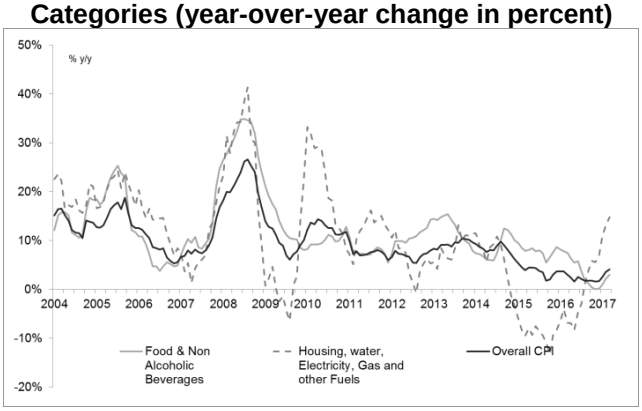
Economic Performance and Outlook

The macroeconomic environment remains favourable. Inflation reached 5 percent in April 2016 as the effects of the fall in oil prices subsided (Figure 1). However, with oil prices to remain flat, inflation is projected to remain in the lower band of the Bank of Jamaica's (BOJ) target of 4 to 6 percent.

Net international reserves of US$2.85 billion as of April 2017 were above prudential levels. Given the remaining funds from the EFF, gross international reserves at end-February 2017 amounted to US$3.4 billion, equivalent to 21.9 weeks of imports of goods and services. The precautionary SBA boosted potential reserves by another US$580 million.

The Bank of Jamaica announced it would buy back U.S. dollar-denominated instruments. The central bank had issued U.S. dollar instruments to increase reserves – so-called borrowed reserves – but decided to retire part of them early as reserves remain high. In addition, the SBA target for reserves only counts nonborrowed reserves, making the borrowed reserves ineffective to reach reserve targets.

Figure 1: Total Consumer Price Index and Main Categories (year-over-year change in percent)



Source: IDB calculations based on data from the Bank of Jamaica.

Financing of the budget will come from domestic and external sources. Jamaica is projected to require financing equivalent to 9.6 percent of GDP in the current fiscal year. Only 0.3 percent of GDP is for deficit financing, while the remainder is to amortize maturing debt. Demand for domestic GOJ debt securities vanished following the National Debt Exchange in 2013, forcing the authorities to rely more strongly on multilateral financing and external debt issuance since then. However, the government resumed domestic debt issuances in February 2016 and is projected to cover financing amounting to 3.7 percent of GDP from domestic sources.

[1] SDRs are an international reserve asset created by the IMF.

The remainder will come from multilateral and bilateral development partners, and international capital markets.

Growth is projected to accelerate. Growth for the current fiscal year FY2017/18 that will end in March 2018 is projected at 2.1 percent, following 1.7 percent in FY2016/17 and 1.1 percent the year before. The recovery should be centred on tourism and construction, but most other sectors also have a positive outlook.

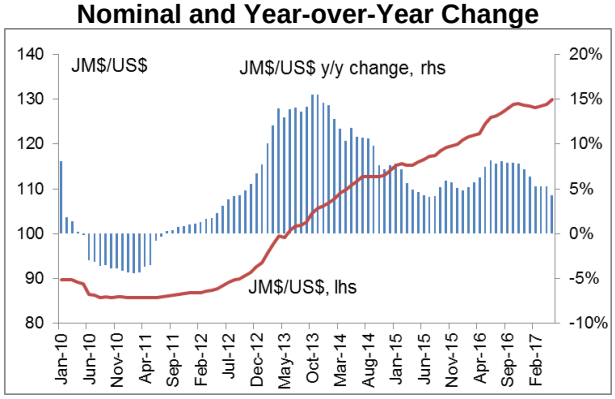
The economic impact of heavy rains in May 2017 should be low. Jamaica was hit by heavy rains in the first half of May that led to dislocation and damage to infrastructure and agriculture. The rains were potentially damaging, as they affected crops at a vulnerable time. However, only minor damage has been reported.

Unemployment continues to improve but at a slow pace. At 12.7 percent in January 2017, unemployment remained virtually the same as it was in the previous quarter (12.89 percent in October 2016) but improved compared to the same period a year earlier (13.3 percent). Encouragingly, the number of employed persons increased by 21,900 persons, equivalent to 1.8 percent of the employed workforce.

Exchange Rate Woes

Movements of the Jamaica dollar versus the U.S. dollar remain a worry for Jamaicans. The Jamaican dollar experienced rapid depreciation against the U.S. dollar from late 2011 to the end of 2014. Besides worries from the volatile economic situation, the depreciation also compensated for a decline in the competitiveness of Jamaican goods as a result of an appreciation of the currency in 2010. In line with the stabilization, an improvement in domestic confidence, and low levels of inflation, the depreciation has been slowing (Figure 2).

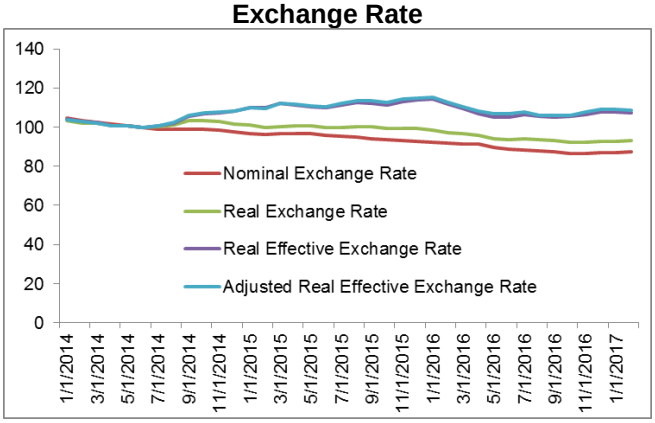
Figure 2: Jamaican Dollar/U.S. Dollar Exchange Rate, Nominal and Year-over-Year Change



Source: IDB calculations based on data from the Bank of Jamaica.

While Jamaica has gained competitiveness against the United States, other countries have gained more. The real exchange rate against the U.S. dollar declined (Figure 3), indicating that Jamaican goods have become cheaper in U.S. dollars. However, comparing the real effective exchange rate (exchange rates with all trading partners where the weights depend on the quantities exported) or the adjusted real exchange rate (the exchange rates of competitor countries that export the same goods) shows that Jamaica has lost international competitiveness.[2] The reason for this is that while Jamaica's currency depreciated against the U.S. dollar, other currencies depreciated more.

Figure 3: Jamaican Dollar/U.S. Dollar Nominal Exchange Rate, Real Exchange Rate, Real Effective Exchange Rate, and Adjusted Real Effective Exchange Rate



Source: IDB calculations based on data from the Bank of Jamaica.

Conclusion

The SBA is expected to provide a sustainable framework for the next three years. Growth in FY2017/18 and FY2018/19 is projected to accelerate further to 2.1 percent and then 2.5 percent. With stabilization in oil prices, inflation should increase from its record low levels to around 5 percent, still below historical levels. Similarly, the current account deficit is projected to remain below 4 percent (see the Snapshot below for forecasts under the SBA).

High Frequency Macroeconomic Indicators				
	Last data	Period	Prior data	Period
Real GDP Growth (y/y)	1.1	2016 Q4	2.0	2016 Q3
Inflation (y/y)	4.8	Apr-17	2.6	Jan-17
Net international Reserves (US bil)	2.8	May-17	2.6	Feb-17
Exchange Rate (end of period)	129.9	Jun-17	128.1	Feb-17
Unemployment Rate (%)	12.7	Jan-17	12.9	Oct-16

Sources: Bank of Jamaica; and Statistical Institute of Jamaica.
Note: y/y = year over year.

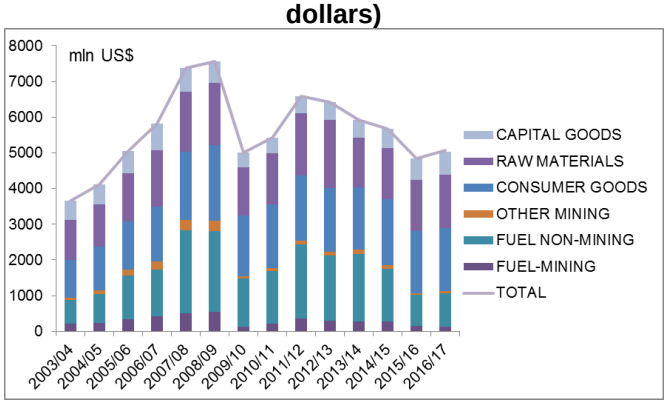
[2] For details on the AREER methodology, see Appendix C in Andrew Powell (editor) *Routes to Growth in a New Trade World,* 2017, Inter-American Development Bank, Washington, DC.

Introduction

As a small and open economy, Jamaica is highly dependent on the vagaries of commodity prices. Besides energy, Jamaica also imports a large part of agricultural produce and industrial inputs.

Jamaica used to be a major commodity exporter. Geologically, large parts of Jamaica contain bauxite, the primary ore of aluminium. This abundance made Jamaica a leading bauxite producer in the world in the 1950s through the 1970s. However, structural issues and low world prices for aluminium led to a rapid decline in production from 1980 onward. The global financial crisis was also a major blow to the industry, as Jamaica's bauxite/alumina exports declined by two-thirds from FY2007/08 to FY2009/10.

Figure 4: Jamaican Imports of Goods (millions of U.S. dollars)



Source: Bank of Jamaica.

Commodity Dependency in Jamaica

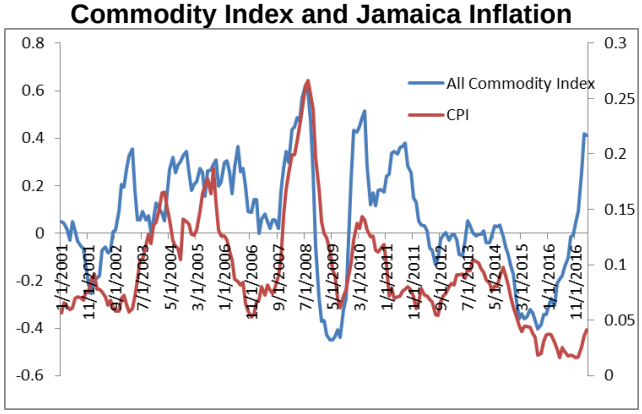
The main channels through which commodity prices affect Jamaica are the external balance of payments and inflation. Raw materials and fuel make up around half of all imports of goods, with the remainder being consumer and capital goods (Figure 4). Swings in commodity prices quickly transmit into variations in imports, with important consequences for the external situation.

Jamaica typically runs current account deficits. With high import dependence, the current account has been in deficit since the mid-1990s. Most of the variation results from fuel imports, which is also reflected in the recent decline of the current account deficit to less than 3 percent of GDP.

Jamaica imports around 20 million barrels of oil per year. The Petroleum Corporation of Jamaica and bauxite companies are the main importers of fuel into Jamaica. The import value has varied depending on price and volume, varying between 7.1 percent of GDP in 2015/16 and 22.2 percent of GDP in 2008/09. Electricity generation is the largest consumer of fuel imports.

International prices, especially for energy, are a main determinant of Jamaican inflation. Monthly inflation in Jamaica has averaged 9.5 percent since January 2001, ranging from 1.3 to 26 percent. Of this variation, around 40 percent is related to commodity price fluctuations.[3] Over this time period, two sub-periods stand out: the acceleration of commodity prices in 2007, and the recent fall in those prices starting in 2014. Inflation in Jamaica closely followed international commodity prices on both occasions (Figure 5).

Figure 5: The International Monetary Fund's All Commodity Index and Jamaica Inflation



Source: IDB calculations based on data from the Bank of Jamaica and the International Monetary Fund.
Note: CPI = Consumer Price Index.

Oil prices translate into electricity prices, affecting the competitiveness of Jamaican firms.[4] Oil price shocks are reinforced through outdated and inefficient electricity generation in Jamaica, exacerbating an already uncompetitive position.

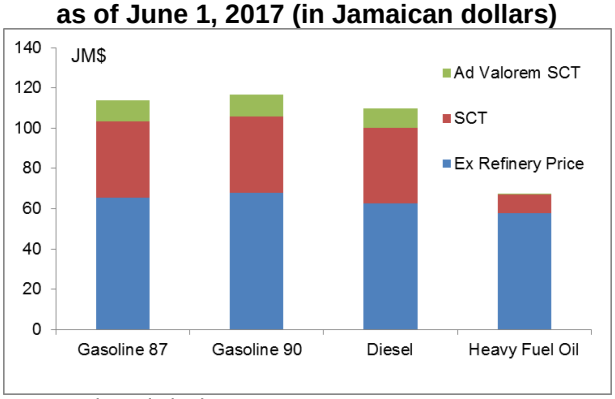
Oil price variations have fiscal consequences. While Jamaica does not subsidize energy consumption, variations in gas prices translate into variations in fuel taxes. Besides a fixed Special Consumption Tax (SCT), Jamaica also charges a 10 percent ad valorem tax, which depends on the price. However, the fixed SCT constitutes the large majority of the taxes on gas.

Jamaica has benefited from the recent fall in oil prices. The decline has supported Jamaica's adjustment program under the EFF. The year before the program,

[3] Based on a simple regression of monthly year-over-year inflation on changes in the International Monetary Fund's All Commodity Index.
[4] As per regulation, the Jamaica Public Service Company charges a Fuel and Independent Power Producer Charge and a Foreign Exchange Adjustment in addition to base charges in order to take into account the cost of buying fuel for energy generation.

FY2012/13, Jamaica's current account deficit was 10 percent of GDP, while inflation was 9.1 percent. The economy contracted in the same year by 0.8 percent. Four years later, in FY2016/17, the economy grew an estimated 1.7 percent while the current account deficit declined to 3 percent of GDP and inflation fell to 2.3 percent. Several factors are responsible for these advances, but the decline in average fuel prices from US$106.9 to US$46.3 per barrel provided support. In spite of a 25 percent increase in the volume of fuel from FY2012/13 to FY2016/17, the import bill declined by almost half, from US$2.1 billion to US$1.2 billion.

Figure 6: Petrojam Jamaica Petroleum Product Prices as of June 1, 2017 (in Jamaican dollars)



Source: Petrojam Limited.
Note: SCT = Special Consumption Tax.

Conclusions and Policy Implications

Jamaica's recent economic performance has benefited from a conducive external environment. While the world economy recovered, leading to higher remittances and tourism arrivals, commodity prices eased. As a result, demand for Jamaican products increased while its imports declined. Inflation remained low and electricity prices declined, increasing the purchasing power of Jamaicans and improving competitiveness.

Jamaica remains highly vulnerable to commodity price shocks. The country continues to depend on imports, including for most of its energy needs, and recent advances could be reversed quickly. However, the country is increasing its resilience by building economic buffers and reducing its dependence on imported energy.

External buffers have increased under the EFF/SBA. The combination of a floating exchange rate and appropriate international reserves provides a buffer against external shocks. The Bank of Jamaica can provide foreign exchange in case of an external shock (such as a spike in international prices, which would require more foreign currency for imports), while the exchange rate can adjust to lower demand for imported goods. This is an advantage compared to countries with fixed exchange rates that have to rely on reserves alone in case of insufficient foreign currency. Finally, the precautionary SBA provides a further contingency against external shocks.[5]

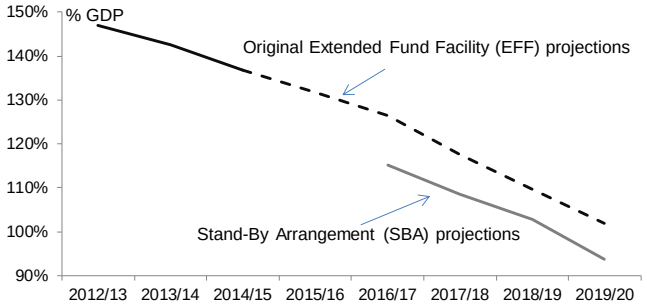
Several initiatives to reduce energy dependence are ongoing. The replacement of old diesel-based generators with new gas-based generators will reduce generation costs.[6] In addition, several initiatives continue to be implemented to increase the share of renewable energy to the targeted 20 percent of the total by 2030.[7]

[5] The SBA amount was calibrated to help absorb large shocks, which could include a rapid increase in oil prices. See Box 4 in the SBA request for such an adverse scenario. http://www.imf.org/external/pubs/cat/longres.aspx?sk=44394.0

[6] Groundbreaking for construction of a 190MW power plant at Old Harbor began in April 2017.

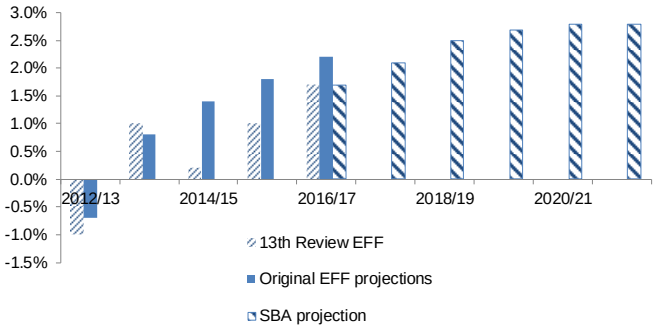
[7] See Saurabh Mahapatr, "Jamaica Will Add 150 MW of Renewable Energy Capacity This Year," *Clean Technica,* June 28, 2016. Available at: https://cleantechnica.com/2016/06/28/jamaica-will-add-150-mw-renewable-energy-capacity-year/

The Stand-By Arrangement will still focus on debt reduction …
Figure a. Debt-to GDP 2011/12 - 2019/20



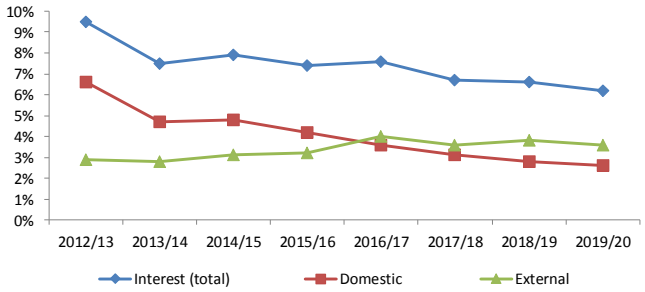
Source: International Monetary Fund (IMF)

…and continue to hope for growth acceleration
Figure b. Annual GDP Growth Rate



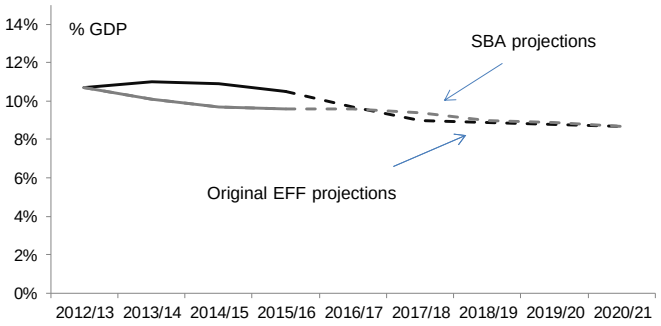
Source: Statistical Institute of Jamaica and IMF

Interest Payments are on a downward path…
Figure c. Interest Payments on Government Debt (% of GDP)



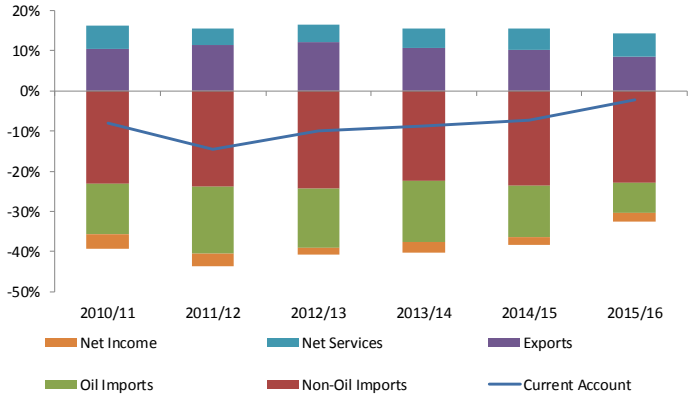
Source: International Monetary Fund.

while reduction of public sector salaries remains a target
Figure d: Public Wages and Salarias (% of GDP)



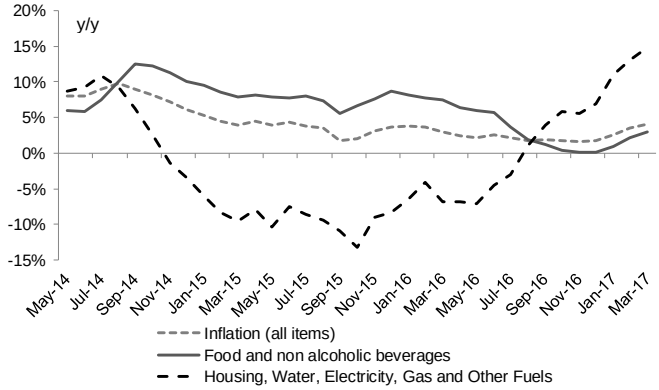
Source: International Monetary Fund.

Low oil prices helped the current account…
Figure e. Contributors to Current Account Deficit (% of GDP)



Source: Bank of Jamaica.

… and kept inflation under control
Figure f. Inflation and Its Main Components (y/y % change)



Source: Bank of Jamaica.

	2012/13	2013/14	2014/15	2015/16	2016/17 (P)
(Annual percentage changes, unless otherwise indicated)					
Real Sector					
Real GDP	-0.7	0.9	0.2	1.0	1.7
Nominal GDP	6.1	8.9	6.9	7.5	4.0
Inflation (end of period)	9.1	8.3	4.0	3.0	4.0
Exchange rate (end of period)	98.9	109.6	115.0	122.0	128.6
External Sector					
Exports of goods and services (yoy, %)	3.5	3.5	-5.0	0.3	2.2
Tourism receipts (yoy, %)	1.4	1.8	10.0	5.9	2.9
Imports of goods and services (yoy, %)	0.4	0.4	-7.3	-9.7	4.0
Current account (percentage of GDP)	-11.5	-8.4	-6.6	-1.8	-3.0
(In percentage of GDP, unless otherwise indicated, on a calendar year basis)					
Central Government					
Revenue and grants	25.8	27.2	26.3	27.0	27.9
Budgetary expenditure	29.9	27.1	26.8	27.2	28.8
Primary balance	5.4	7.7	7.5	7.1	7.0
Budget balance	-4.1	0.1	-0.5	-0.3	-0.9
Public sector balance	-4.2	0.1	0.4	1.6	-0.9
Treasury bill rate (percent, end of period)	5.8	8.0	7.0	5.8	-
Debt Indicators					
Public sector debt	146.4	141.6	124.8	120.3	115.2
Public sector debt over revenues	n.a.	516.4	491.6	445.6	412.9
Foreign currency public debt (end of period)	76.0	76.4	49.9	70.0	
International Reserves					
Net international reserves (USD Mill)	884	1303	2294	2416	2699
Gross international reserves (weeks of good and services imports)	<12	14.4	19.4	23.3	22.5

Sources: International Monetary Fund; and country authorities.
Note: P = projected; yoy = year-over-year.

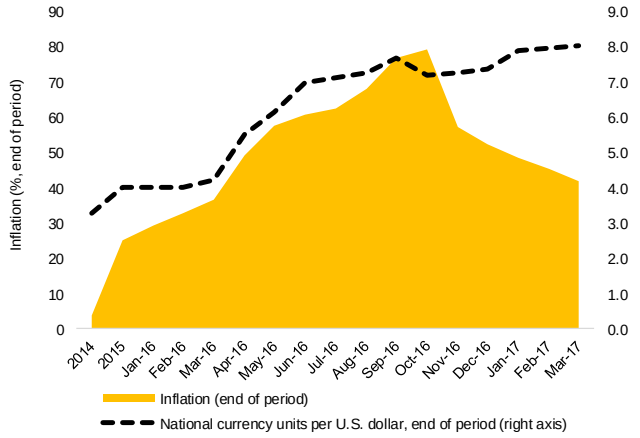
Contributor: Jeetendra Khadan

Recent Developments

Suriname is expected to record another year of economic contraction in 2017 before seeing some marginal improvement in 2018. Real GDP is projected to decline by 1.2 percent in 2017. The International Monetary Fund (IMF) projects that real economic growth of 0.8 percent will return in 2018, with growth then averaging about 1.7 percent over the period from 2019 to 2022. This outlook is largely predicated on a recovery of the mining sector, which would support growth through the medium term.

Inflation has decelerated in 2017. After spiking at 79.2 percent (year-on-year) in October 2016, inflation declined to 41.8 percent in March 2017. There has been an easing of the pass-through effect associated with the rapid decline in the value of the Suriname dollar and an increase in utility tariffs that largely contributed to the sharp increase in inflation in 2015 and 2016 (Figure 1). Renewed exchange rate stability has since helped to produce a period of sustained disinflation (Figure 1).

Figure 1. Inflation and the Exchange Rate



Source: Central Bank of Suriname.

The fiscal deficit narrowed in 2016. As a percentage of GDP, the fiscal deficit declined from 6.7 percent in 2015 to 3.3 percent at the end of 2016. This was influenced largely by a 14.5 percent decline in government expenditure and an 8.5 percent fall in government revenue. The fiscal balance, however, remains under pressure as demands by teachers for a pay increase are putting an additional burden on the country's wage bill. School salaries accounted for about 10 percent of total primary spending in 2016 (**Economist Intelligence Unit**, 2017).

The current account has shown significant improvements. After recording a deficit of 16 percent of GDP in 2015, the current account deficit declined to 4.4 percent of GDP in 2016 and is expected to report a surplus of 2.8 percent of GDP in 2017. This improvement has been largely due to an improvement in exports of goods and services, which increased by 60 percent: the trade deficit narrowed from US$85 million in 2015 to US$15 million in 2016.

Highlights

- *Suriname's economy is expected to contract by 1.2 percent in 2017.*
- *Fiscal and current account balances have markedly improved in the last year.*
- *Suriname was downgraded by Standard and Poor's Global Ratings in April 2017.*

Suriname's debt stock as a percent of GDP increased by 19 percentage points from 2015 to 2016. This was partly due to the issuance of an external government bond of US$550 million. General government debt stood at 64.6 percent of GDP in 2016, more than triple the 19 percent of GDP in 2010 (Figure 2).

The primary balance and changes in the exchange rate are the two main recent drivers of Suriname's debt. Large fiscal deficits, currency devaluation, and weak real GDP growth, driven primarily by a sharp drop in mineral revenues, have been the main causes (Figure 3). Suriname's primary fiscal deficit increased from 1.5 percent of GDP in 2010 to 4.4 percent of GDP in 2016, reaching a high of 7.8 percent of GDP in 2015. Real GDP growth declined from an average of 4.4 percent in 2001–2014 to an average of -6.6 percent in 2015–2016. Together with these factors, a currency depreciation of 127 percent from 2010 to 2016 raised the debt-to-GDP ratio by over 35 percentage points from 2014 to 2016.

Foreign reserves have recovered only marginally. New borrowing and some recovery in commodity prices have contributed to a small recovery. Recently, foreign reserves increased to US$393 million in April 2017 from US$381 million in December 2016.

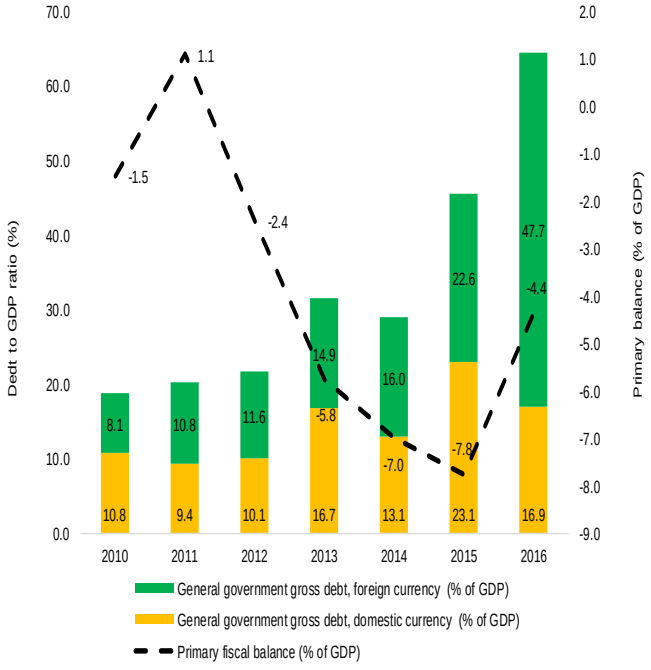
The Central Bank of Suriname has set new rules for currency credits. Reports suggest that commercial banks are now only permitted to provide foreign currency loans to companies and individuals that receive regular foreign currency income.

Suriname was downgraded by Standard and Poors (S&P) Global Ratings in April 2017. S&P lowered Suriname's long-term sovereign credit rating from B+ to B with a negative outlook. S&Ps rationale for the downgrade reflects a worsening of the country's financial

profile and economic strength as a result of a significant economic contraction in 2016 that resulted in higher government debt, a substantial currency devaluation, and high inflation.

Suriname's National Assembly passed legislation to establish a Savings and Stability Fund (SSF). The SSF is expected to receive windfall mining revenue starting in 2018. In principle, the SSF will address the problem of volatility in fiscal revenue collection. The authorities expect that the SSF's capital will reach roughly US$200 million by 2023. The Central Bank of Suriname will manage the fund for the first three years, after which time a supervisory board comprised of government, the central bank, and business and trade union representation will be established. The SSF will help to support macroeconomic stability in the longer term.

Figure 2. Suriname's Domestic and Foreign Debt (percent of GDP)



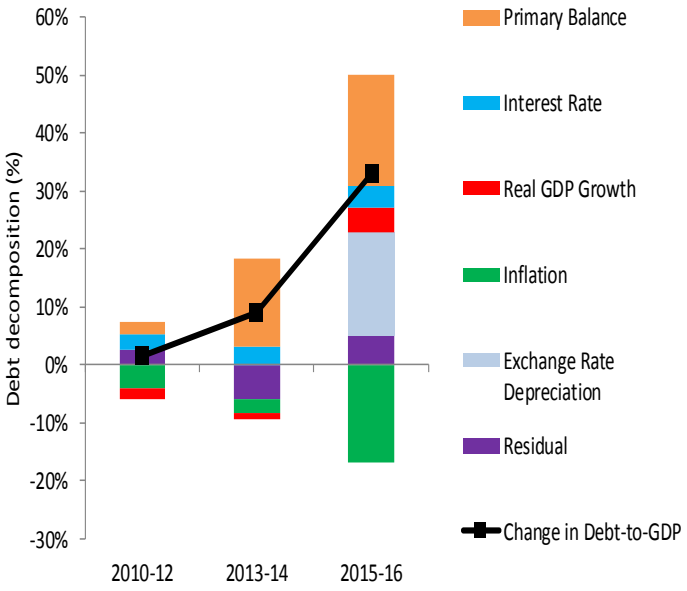
Source: Author's estimates based on data from the International Monetary Fund, *World Economic Outlook* (April 2017).

Suriname's housing sector is expected to benefit from an Islamic Development Bank loan. The Islamic Development Bank approved a US$35 million loan to support affordable housing in Suriname.

The authorities have officially announced that the IMF Stand-By Arrangement that was approved in May 2016 has ended.

Suriname aims to attract doctors and specialists to boost health care. The authorities indicate that the ratio of family doctors is 1 per 1,600 population, and for medical specialists the ratio is 1 per 2,600 population. Health authorities aim to attract Cuban doctors and specialists to reduce the former ratio to 1/1,300 and the latter to 1/2,300.

Figure 3. Debt Decomposition, by Time Periods (percent)



Source: Author's estimates based on data from the International Monetary Fund, *World Economic Outlook* (April 2017).

Looking forward, a number of challenges confront the authorities. Perhaps the main challenge relates to balancing the effects of fiscal consolidation, which is required to support macroeconomic stability, against the welfare impact of adjustments on the most vulnerable in society. In addition, the expected decline in gold prices over the medium term puts Suriname in a precarious position. Over a longer horizon, the government must follow through on its commitment to undertake institutional reforms, broad-based structural reforms to improve productivity growth, and measures to support economic activity in the non-mineral sector economy.

Table 1. High Frequency Macroeconomic Indicators

	Most Recent Data	Period	Prior Data	Period
Real GDP growth (y/y)	-10.7	2016	-2.7	2015
Inflation (end of period)	52.0	2016	25.0	2015
Gross international reserves (US$ million)	393	Apr.2017	381	2016
Exchange rate (to US$)	7.5	Mar.2017	7.4	2016
Unemployment rate (%)	8.7*	2016	8.7	2015

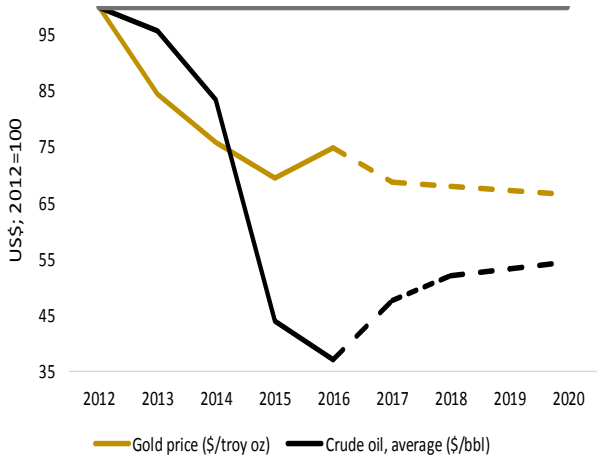
Sources : Central Bank van Suriname; General Bureau of Statistics; International Monetary Fund, *World Economic Outlook* (April 2017).

* Estimate.

Introduction

Suriname is an extreme case of a small commodity dependent economy. This South American country is well endowed with natural resources, highly dependent on international markets, and highly vulnerable to external shocks. Suriname has historically depended on the exports of a few primary commodities. As such, Suriname benefitted enormously from the commodity super-cycle of the 2000s, which resulted in one of the better periods of the country's economic history. In 2011, the exports of gold, alumina, and oil together accounted for 53 percent of GDP and roughly 40 percent of government revenues. This ended abruptly in 2015 when the risks of being commodity-dependent came to the fore, pushing Suriname into a new economic phase characterized by low growth and rapidly rising debt. This section provides an analysis of this recent commodity shock on Suriname's macroeconomic performance and the country's policy response.

Figure 4. Commodity Price Shocks

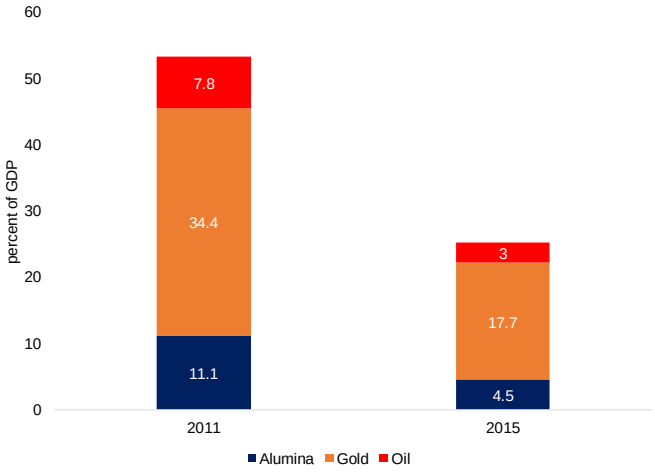


Source: World Bank Pink Sheet (2017).

The Triple Commodity Shock

Suriname experienced a triple commodity shock in 2015. The price of gold declined by 30 percent relative to 2012, oil prices declined by 56 percent relative to 2012, and alumina production came to a halt (Figure 4). Since these three commodities were the mainstay of Suriname's economy, the declines were like a "perfect economic storm." The result was a sharp drop in economic growth and rapid deterioration of the country's fiscal and external accounts. Because of the commodity shock, the contribution of exports of these three commodities to GDP declined from 53.3 percent in 2011 to 25.1 percent in 2015 (Figure 5).

Figure 5. Exports as a Percent of GDP

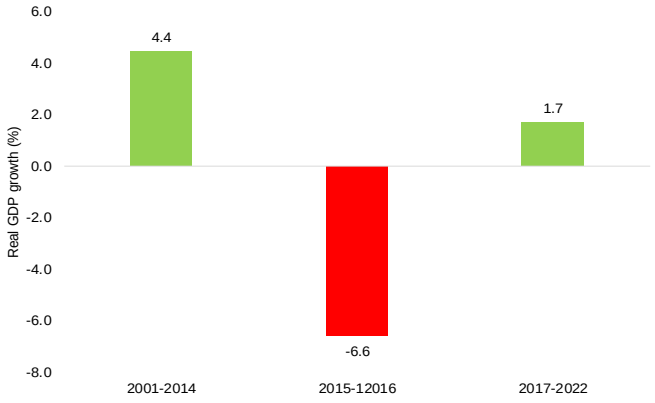


Source: IMF Article IV (2016).

Sharp Decline in Real GDP Growth

Suriname experienced a sharp decline in real GDP growth in 2015 and 2016. The country moved from being one of the fastest-growing economies in Latin America and the Caribbean over 2001–2014 to experiencing the second-largest economic decline in 2015–2016. Suriname's average growth rate for the period from 2001–2014 was 4.4 percent, the second highest in the Caribbean and fifth highest in Latin America and the Caribbean. This is no longer true. The growth momentum that was mainly propelled by the commodity super-cycle and came after decades of low and volatile growth has ended. In 2015–2016, Suriname recorded the second largest decline in real GDP growth in Latin America and the Caribbean, second only to Venezuela (Figure 6), and growth is not expected to return to pre-2014 levels at least over the medium term.

Figure 6. Real GDP Growth (percent)



Source: IMF, *World Economic Outlook,* April 2017.

Fiscal Impact of the Commodity Shock

There was a surge in commodity-related revenues and a corresponding rise in expenditure during the boom period. A substantial increase in commodity-related revenues contributed to a 464 percent increase in general government revenues from 2002 to 2015 (Figure 7). This strong revenue flow was accompanied by a sharp rise in government spending (581 percent) over the same period that increased annually by an average of 16.7 percent. The largest share of government expenditure during this period was focused on wages and salaries.

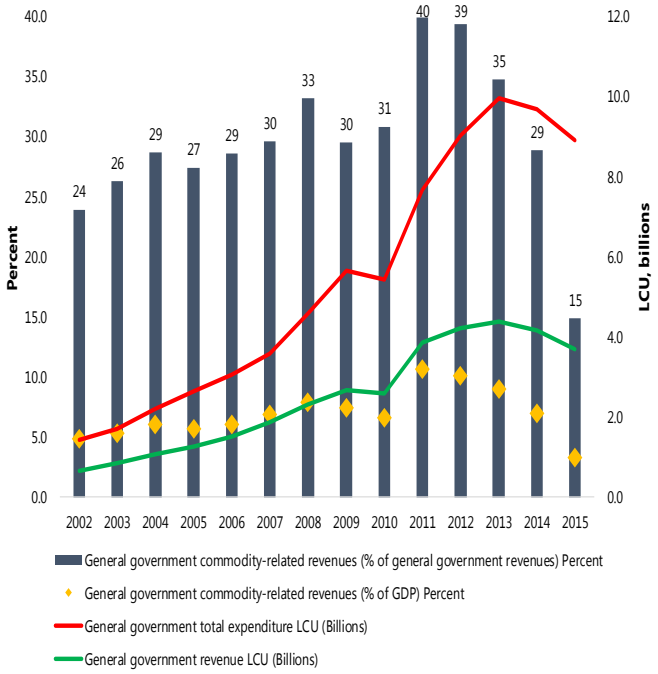
Suriname's fiscal performance deteriorated sharply after the 2015 commodity shock. While the country's fiscal performance improved during the commodity super-cycle compared to the previous eight years, it has weakened significantly since the commodity shock. Suriname had a small primary fiscal deficit averaging 0.7 percent of GDP from 2001–2014, compared to an average deficit of 2.8 percent of GDP from 1990–2000. However, the sharp decline in mineral-related revenues significantly contributed to a rapid deterioration of the fiscal accounts: commodity-related revenues increased from 24 percent of general government revenues in 2002 to a peak of 40 percent in 2011, before declining to 15 percent in 2015. This led to Suriname's primary fiscal balance moving from a small deficit over 2001–2014 to the third-largest deficit (6.3 percent of GDP) in Latin America and the Caribbean in 2015–2016.

The External Sector Shock

Suriname's current account balance worsened sharply after the commodity shock, moving from a small surplus to one of the largest current account deficits in Latin America and the Caribbean. The current account balance went from an average surplus of 0.4 percent of GDP over 2001–2014 to an average deficit of 10.5 percent of GDP in 2015–2016. The magnitude of the shock, shown in Figure 8, is largely attributed to the significant drop in mineral exports. The IMF (2016) noted that the decline in mineral exports accounted for more than the full decline, since there was an offsetting rise in non-mineral exports.

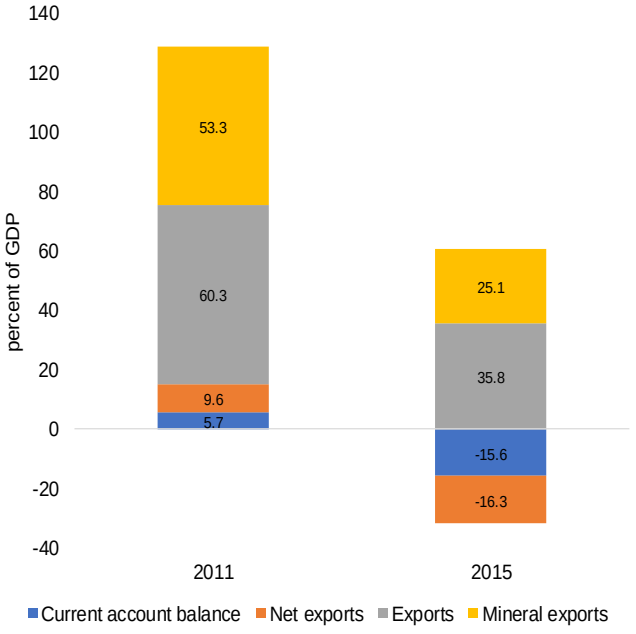
Gross reserves declined and the authorities floated the exchange rate. Gross reserves dropped from US$779 million (3.4 months of import cover) in 2013 to US$330 million (2.1 months of import cover) in 2015 due mainly to the sharp drop in net exports and the central bank's intervention to support the currency. Subsequently, the authorities devalued the currency by 21 percent in November 2015. On March 22, 2016 Suriname adopted a managed-float exchange rate system by means of currency auctions.

Figure 7. General Government Commodity-related Revenues



Source: International Monetary Fund, *World Economic Outlook* (April 2017).
Note: LCU = local currency units.

Figure 8. Current Account Balance and Net Exports (percent of GDP)



Source: International Monetary Fund, Article IV (2016).

The Fiscal Shock

Surname's debt-to-GDP ratio increased by 35.6 percentage points in three years beyond the 60 percent threshold:[1] from 29 percent of GDP in 2014 to 64.6 percent of GDP in 2016 (Figure 9). This was the largest increase in the debt ratio recorded in Latin America and the Caribbean, pushing the country's debt-to-GDP ratio over the critical debt-growth threshold. Weak growth, large fiscal deficits, and currency devaluation have been the main drivers, as discussed above.

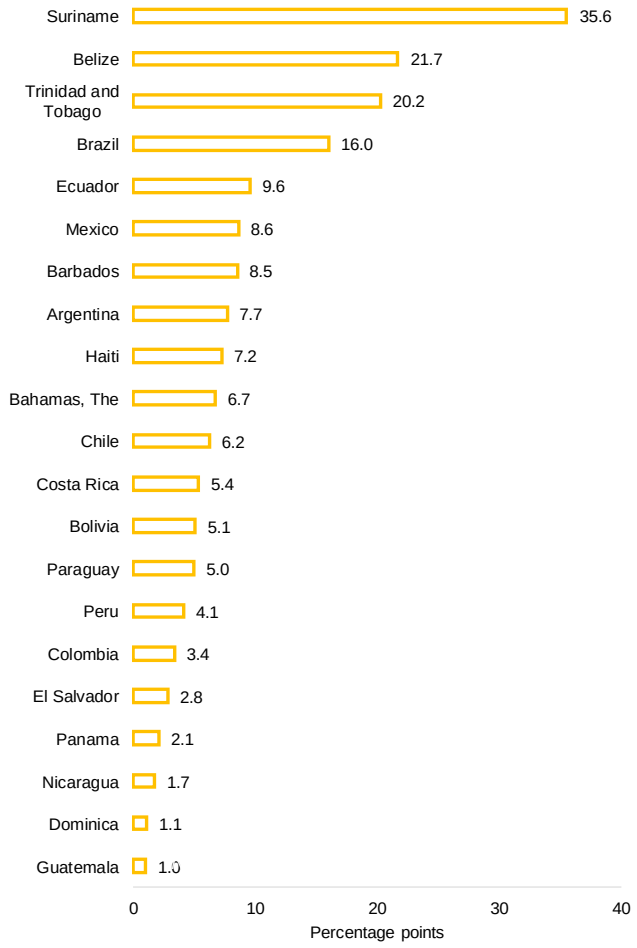
Never Let a Crisis Go to Waste: Policy Response and Reform Impact

The authorities outlined an ambitious adjustment program to restore macroeconomic stability and put the economy on a sustainable growth path, initially supported by an IMF Stand-By Arrangement. Key measures of the program include cuts to government expenditure, floating of the exchange rate, curbing monetary financing, initiating the phasing-out of electricity subsidies, and preparing for the introduction of a broad-based value-added tax in 2018. In addition to these measures, the government has committed to undertaking broad-based structural reforms to improve productivity growth and diversify the economy, and to develop a well-targeted social safety net to protect the vulnerable population from the adverse effects of adjustments (see IMF 2016 for more details).

Some improvements to the fiscal and external accounts have been realized. The fiscal and external imbalances have declined and the IMF is projecting further improvements to the macroeconomic framework over the medium term – assuming the reform agenda continues.

The current crisis presents an opportunity for policymakers in Suriname to undertake much-needed reforms. To the extent that this is achieved, Suriname can come out of this crisis stronger and more resilient to external shocks.

Figure 9. Change in the Debt-to-GDP Ratio from 2014 to 2016 (percentage points)



Source: International Monetary Fund, *World Economic Outlook* (April 2017).

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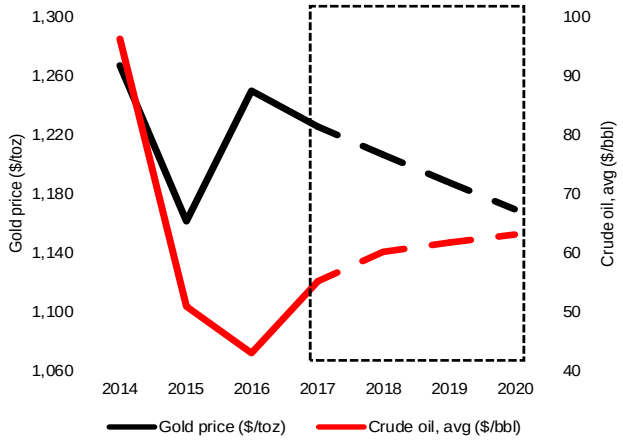
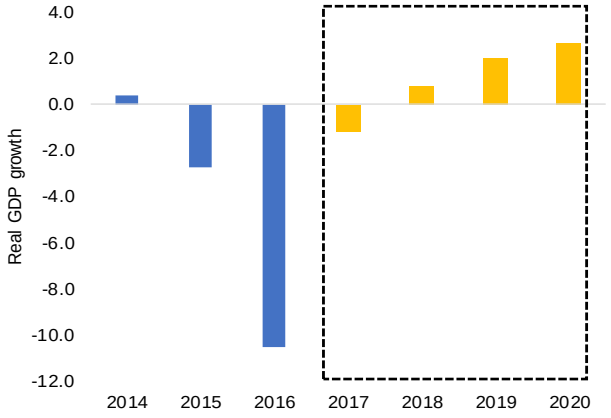
International Monetary Fund (IMF). 2016. Article IV: Suriname Request for Stand-by Arrangement—Press Release; Staff Report; and Statement by the Executive Director for Suriname. International Monetary Fund, Washington, DC.

[1] Determining whether fiscal policy is adequate requires a benchmark to decide whether debt is too high, or is forecast to become too high. One typical debt benchmark is derived from the estimated relation between debt and economic growth. The inverted "U" shape relation captures that, for a debt-to-GDP ratio lower than 30 percent, any increase has a positive marginal and average effect on economic growth. However, above that level (the turning point on the inverted U curve), any further increase has a negative marginal effect, and above 60 percent the impact (marginal and average) becomes negative. See also Ruprah, Melgarejo, and Sierra (2014).

Gold prices are on a downward path…

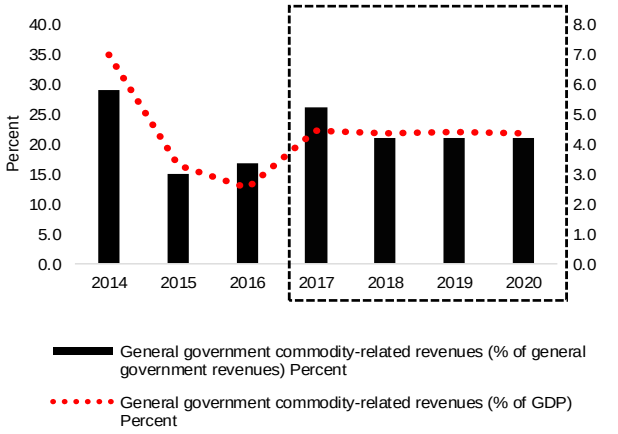


Real GDP growth to improve marginally…

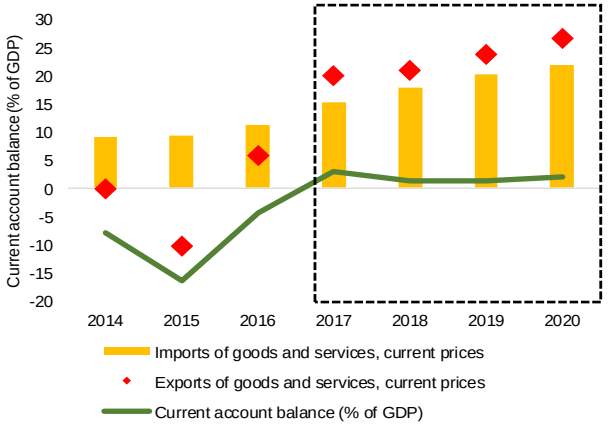


Inflation on a downward path…

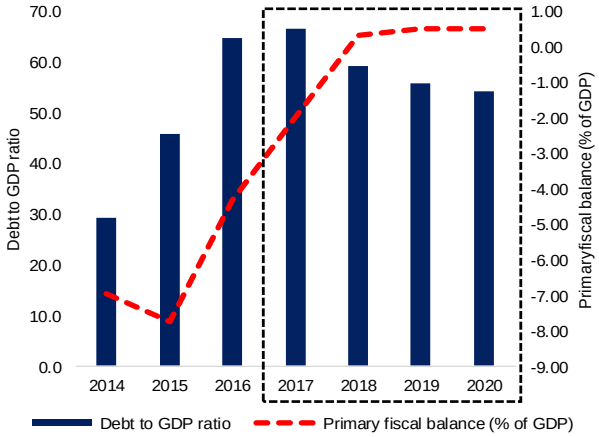
Commodity related revenues will remain depressed over the medium term…



Current account balance to improve slightly …



Debt is projected to stabalize as fiscal balance improves …



Source: International Monetary Fund, *World Economic Outlook* (April 2017).

Suriname: Selected Indicators

	2013	2014	2015	2016	2017(p)
(Annual percentage changes, unless otherwise indicated)					
Real sector					
Real GDP	2.9	0.4	-2.7	-10.5	-1.2
Nominal GDP	3.3	1.8	-3.6	33.4	28.5
Inflation (end of period)	0.6	3.9	25.0	52.4	29.9
Unemployment	6.0	7.0	8.3	11.0	9.1
Exchange rates (end of period)	3.3	3.3	4	7.5	7.6**
(In percent of GDP, unless otherwise indicated, on a calendar year basis)					
External sector					
Capital and financial account	8.3	13.1	15.2	-13.7	n.a.
Current account	-3.8	-7.9	-16.6	-4.4	n.a.
Gross international reserves (US$ millions)	779	625	330	381	n.a.
In months of imports	3.4	2.8	2.1	2.6	n.a.
Central government					
Revenue and grants	25.8	24.1	22.1	15.2	17.0
Total expenditure	32.9	32.0	31.4	20.9	21.8
Primary balance	-5.8	-7.0	-7.8	-4.4	-2.0
Overall balance	-7.1	-7.9	-9.3	-5.7	-4.8
Debt indicators					
Total government debt	31.6	29.1	45.7	64.6	66.3
External debt	14.9	16.0	22.6	47.7	54.1
Domestic debt	16.7	13.1	23.1	16.9	12.3

Sources: International Monetary Fund (2017).

Notes: (p) denotes provisional figures. World Economic Outlook, IMF (April, 2017)
**Data as at May 19, 2017. On March 22, 2016, Suriname adopted a flexible exchange rate regime.

Contributor: Juan Pradelli

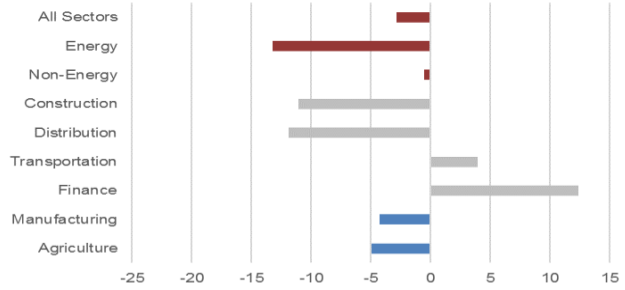
Overview

The domestic economy in Trinidad and Tobago is stagnant but could start recovering slowly provided that energy output increases and commodity prices stabilise. Overall, non-energy activity has stagnated since 2015 as a consequence of lower prices and volumes of oil and natural gas as well as a fiscal retrenchment. However, economic performance has varied widely across sectors. In addition, as energy prospects improve in 2017–2018, the domestic economy could slowly revive its growth potential.

Recent Developments and Outlook

Economic performance has been heterogeneous across sectors of activity (Figure 1). Following the collapse in commodity prices and the disruptions in energy production, the dynamics of the domestic economy has been mixed. According to Central Statistical Office data, distribution services, construction, and manufacturing—which jointly account for two-fifths of the non-energy economy—contracted by 10 percent (cumulative) in 2015–2016. These sectors have some trade linkages to the hydrocarbon industries and were largely affected by the prevailing budget austerity, including cuts in public investment. In stark contrast, finance and transport services—which also represent two-fifths of the non-energy economy—expanded by 9 percent (cumulative) in the same period. So far, the financial sector has avoided the negative repercussions of the recession on debtors' creditworthiness, while expanding its financing to the Government.

Figure 1. Sectoral GDP Growth 2015—2016
(cumulative variation in percent)



Sources: Central Statistical Office and author's calculations.

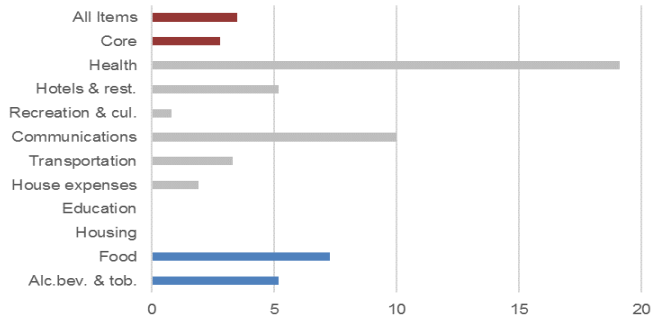
Price inflation also differed across goods and services (Figure 2). Since late 2015, there has been upward pressure on prices as a result of the ongoing currency depreciation and a number of fiscal measures (e.g., extension of the value-added tax base, higher fuel prices at the pump, higher taxes on tobacco and alcohol).

Highlights

- *The energy sector will normalize in 2017–2018 and improve conditions for other economic sectors to recover.*
- *Fiscal austerity is continuing in FY2016/17 and revenue shortfalls have led to further expenditure cuts in recent months.*
- *Monetary policy is supporting economic activity, but there are potential risks posed by the gradual normalization of U.S. Federal Reserve policy.*

The domestic economic downturn, however, contained inflation to a significant extent. For instance, food prices—the single most important component of the Retail Price Index—increased by 7 percent between September 2015 and December 2016. Such an increase is arguably lower than what the cost pressures would have caused in the absence of depressed consumption demand. Specifically, higher costs resulted from: (i) the 7 percent currency depreciation observed in that period, which passed through local prices given the importance of imported food staples; (ii) the imposition of value-added tax rates of 12.5 percent on several food items previously exempted; and (iii) the impact of higher fuel prices on the transportation of goods. Similarly, prices of housing and house expenses (including furnishings, household equipment, and routine maintenance) remained essentially stable in view of the severe contraction in construction and real estate activity.

Figure 2. Retail Price Inflation
(percent variation from Sep 2015 to Dec 2016)



Sources: Central Statistical Office and author's calculations.

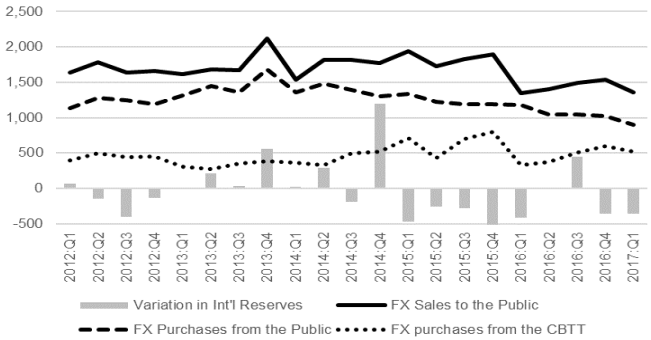
The Mid-Year Review of the FY2016/17 Budget presented in May 2017 suggests that the Government continue cutting expenditures to cope with revenue shortfalls. In the first half of FY2016/17 (October 2016 to March 2017), total revenue was TT$18.1 billion, which implied a TT$5.3 billion shortfall relative to the original budget forecast, mainly due to delays in asset-sale

transactions. To cope with lower-than-expected receipts, the Government has introduced new expenditure cuts; thus, total expenses were TT$23.5 billion, or nearly TT$3.8 billion lower than the original budget plan. In this regard, the FY2016/17 Budget aimed to freeze nominal expenditure at levels achieved through numerous cuts introduced early in 2016. The revenue loss has also led to a higher-than-expected deficit, which amounted to TT$5.4 billion and exceeded the planned figure by TT$1.5 billion. Deficit financing involved a withdrawal from the Heritage and Stabilisation Fund (US$251 million) and net borrowings from domestic sources (TT$3.7 billion).

Recent downgrades reflect the credit rating agencies' concerns about the energy outlook and the policy response, especially on the fiscal front. In April 2017, Standard & Poor's downgraded Trinidad and Tobago's long-term sovereign debt from A- to BBB+, which was the first time the rating fell since 2011. Moody's had graded sovereign bonds as Baa1 since 2006, but downgraded the rating to Baa2 in April 2015, Baa3 in April 2016, and Ba1 in April 2017, which implied the loss of investment-grade status. Both credit rating agencies have expressed concerns with regard to the effects of persistently lower energy prices, the vulnerabilities associated with narrow economic diversification, and growing external and fiscal imbalances. They also stressed that a negative outlook is warranted as long as there is uncertainty about the policy response going forward, i.e., how the policy framework will be adjusted to cope with the short-term external shock and to facilitate a long-term diversification strategy. The Government announced its intention to invite Fitch, the third major agency, to assess risk of sovereign debt.

Foreign exchange shortages persist (Figure 3). Since mid-2015, the reduced supply of hard currency from the energy companies, coupled with an increased demand for speculative and precautionary motives, have unsettled the foreign exchange market and led to international reserve losses. Back in 2013–2014, the authorized market dealers purchased a quarterly average of US$1.4 billion from the public—where those companies are the major suppliers—and only US$0.4 billion from the Central Bank; on the other hand, they sold a quarterly average of US$1.8 billion to the public—comprised of importers and investors. In 2015, when oil and natural gas prices collapsed and the Central Bank actively intervened in the foreign exchange market, the dealers' purchases were US$1.2 billion from the public and US$0.7 billion from the monetary authority—who essentially offset the shortfall from energy companies; and the dealers' sales to the public amounted to US$1.8 billion. From 2016 to the first quarter of 2017, the shortage has become acute: the dealers' purchases were only US$1 billion from the public and US$0.5 billion from the Central Bank, while the sales to the public were just US$1.4 billion. When the Central Bank stepped in, the international reserve losses were sizable: in 2015, net reserves fell from US$11.3 billion to US$9.9 billion; and further declined to US$9.1 billion at end-March 2017, despite US$1 billion in receipts from the sovereign global bond issued in mid-2016 that temporarily bolstered reserves. To contain losses, the local currency has been allowed to depreciate by 7 percent since late 2015. More recently, the Government announced its intention to identify sectors (e.g., manufacturing) that banks should prioritize when meeting demand for hard currency. Arguably, a future recovery in gas prices and exports is likely to ease market tensions and reduce shortages.

Figure 3. Foreign Exchange Market Dealers' Operations and International Reserves (in billions of U.S. dollars)



Sources: Central Bank of Trinidad and Tobago and author's calculations

Conclusion

Trinidad and Tobago must manage a severe shock to commodity prices and a temporary disruption to energy output. Ongoing projects in the natural gas sector, most notably TROC and Juniper, are expected to increase volumes produced and support downstream industries. Most projections indicate global energy prices may have stabilized, but any such projections are subject to considerable uncertainty.

High-Frequency Macroeconomic Indicators

	Latest data	Period	Prior data	Period
Real GDP Growth (%, y-o-y)	-2.3	Q4 2015	-2.0	Q3 2015
Exports (12-month growth, %)	-23.4	Q3 2015	-20.1	Q2 2015
Imports (12-month growth, %)	-17.4	Q3 2015	-19.6	Q2 2015
Private sector credit (12-month growth, %)	6.2	Q1 2016	6.1	Q4 2015
Inflation (headline, % yoy change)	3.4	Jun.2016	3.4	May.2016
Exchange rate TT$/US$ (end of period)	6.70	Jul.2016	6.66	Jun.2016
Unemployment rate (%)	3.4	Q3 2015	3.2	Q2 2015

Source: Central Bank of Trinidad and Tobago.

Commodities and Macroeconomic Performance in Trinidad and Tobago

Trinidad and Tobago's economy is centred around the extraction of oil and natural gas. Oil has been drilled for almost 100 years and was the predominant commodity produced and exported until the early 1990s. Since then, natural gas has become the cornerstone of the energy sector and supported downstream processing activities—mainly liquefied natural gas and petrochemicals for export—as well as domestic power generation. In 2011–2015, on average, the energy sector generated 38 percent of GDP and 82 percent of merchandise exports.

Hydrocarbon-related activities are major drivers of macroeconomic performance. Led by large multinational companies, the hydrocarbon extractive sector is akin to an enclave and lacks strong linkages with the domestic economy through supply chains. Nevertheless, income and foreign exchange generated do spill over through other channels where the public sector's fiscal and exchange rate policies play a key role.[1] First, taxation provides energy revenues to the Government that are ultimately spent on transfers and subsidies to state-owned enterprises, private firms, and households, thus stimulating aggregate demand, domestic economic activity, and employment. In 2011–2015, on average, nearly 45 percent of fiscal revenues were collected from those companies and funded budget expenses.[2] Second, foreign currency is supplied to the foreign exchange market; for example, an important share of energy revenues is surrendered in foreign currency and converted to local currency at the official parity. Energy-related foreign exchange inflows permit domestic firms to conduct international transactions and import capital and consumption goods that cannot be produced locally. They also affect the Government's ability to carry out its exchange rate policy, which has a significant influence on domestic production costs and prices.

While the energy sector is essential to the country's prosperity and high-income level, it also carries visible macroeconomic risks and policy challenges. As discussed in this bulletin, boom-and-bust cycles have been induced by large fluctuations in global energy prices, as well as by the normal life cycle of oil and natural gas industries. In this regard, macroeconomic vulnerabilities stem from a narrow export base and a fiscal structure heavily dependent on energy revenues. Besides, extractive activities may undermine the growth potential of non-energy tradable sectors by creating economic and institutional distortions typical of the Dutch disease phenomenon, as in the case, for example, of currency overvaluation and excessive labour costs affecting the competitiveness of domestic firms.[3]

A Historical Perspective on the Energy Sector's Performance

Global energy prices have experienced two protracted booms since Trinidad and Tobago's independence (Figure 4). Amidst geopolitical pressures in the Middle East and expansionary U.S. monetary policy, oil prices boomed in the 1973–1982 period. Measured at 2016 constant U.S. Producer Price Index (PPI) prices, the real West Texas Intermediate (WTI) oil price rose from US$10 to nearly US$80. More recently, the 2002–2015 boom occurred under quite diverse circumstances, including strong global growth until the financial crisis, the subsequent Great Recession, and the world-wide shale revolution. The real WTI oil price rose from US$40 to US$110 between 2002 and 2008, and dropped to US$80 in 2009–2010 following the financial crisis. It quickly rebounded and stabilized around US$95 in 2011–2014, but collapsed from mid-2015 to a range of US$40-US$50. Prices of natural gas and petrochemicals (ammonia, methanol, and urea) relevant to Trinidad and Tobago's exports followed a similar path. Measured at 2016 constant U.S. PPI prices, the real Henry Hub natural gas price doubled to US$10/mmbtu between 2002 and 2008, and dramatically dropped to a range of US$2-US$5/mmbtu as U.S. domestic production soared. To offset adverse conditions to sell to the U.S. market, Trinidad and Tobago actively expanded liquefied natural

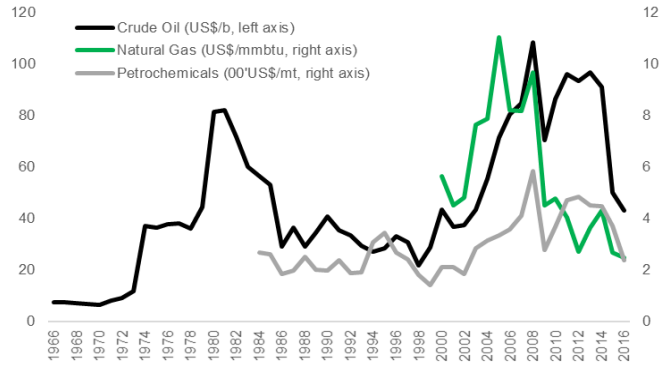
[1] On channels linking energy and non-energy sectors in Trinidad and Tobago, see Hilaire, A., A. Henry, and K. Ramlochan, 2013, *Macroeconomic Challenges: Linking Extractive Industries to the Wider Economy*, Central Bank of Trinidad and Tobago. Available at: http://www.central-bank.org.tt/sites/default/files/Macroeconomic%20Challenges%20-%20Linking%20Extractive%20Industries%20June%202013%20Template%20Recover1.pdf.

[2] On the role of fiscal policy in stimulating the non-energy economy, see the IDB's Caribbean Region Quarterly Bulletin 2016:IV at https://publications.iadb.org/handle/11319/8029.

[3] On Dutch disease in Trinidad and Tobago, see Jeetendra Khadan, 2017, *Is Oil and Gas Smothering the Private Sector in Trinidad and Tobago*? Inter-American Development Bank. Available at: https://publications.iadb.org/bitstream/handle/11319/8104/Are-Oil-and-Gas-Smothering-the-Private-Sector-in-Trinidad-and-Tobago.pdf?sequence=1.

gas exports to Latin America, Europe, and Asia, where prices remained elevated.[4]

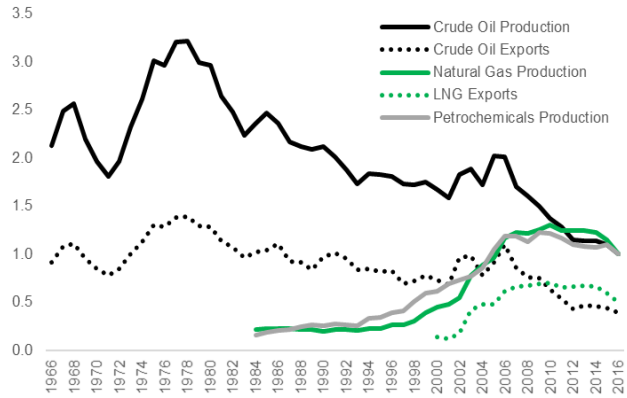
Figure 4. Commodity Real Prices



Sources: International Monetary Fund and Central Bank of Trinidad and Tobago.
Notes: Nominal prices are deflated using the U.S. Producer Price Index 2016 = 1. Petrochemicals price is a simple average of the prices of ammonia, methanol, and urea.

The energy sector's size and structure have evolved in response to the maturation of oil fields and the development of natural gas-related projects (Figure 5). At aggregate level, oil fields entered a mature stage in the 1980s and 1990s, and thus output steadily decreased from a peak of 230,000 b/d in the late 1970s to 72,000 b/d in 2016. In the same period, exports fell from nearly 100,000 b/d to 28,000 b/d. This secular trend reflects the exhaustion of non-renewable oil wealth, which proceeded despite the 2002—2015 price boom and the policy incentives to improve drilling efficiency. On the other hand, natural gas production expanded in the mid-1990s to support petrochemical projects, and further in the 2000s with the development of the liquefied natural gas (LNG) industry. Output increased fivefold from 1996—2010 and reached 4.3 billion cf/d. It stabilized around 4 billion cf/d in 2011—2014 but fell to 3.3 billion cf/d in 2016 as infrastructure upgrading and maintenance works temporarily disrupted production. In recent years, half of natural gas output fed the LNG industry and one-third supported petrochemicals.

Figure 5. Commodity Output Produced and Exported

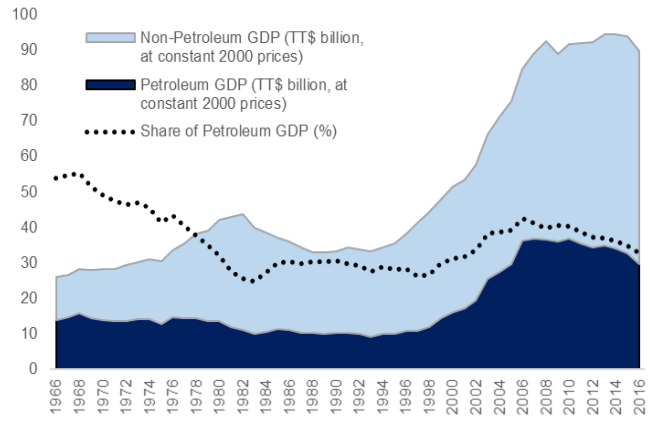


Sources: Central Bank of Trinidad and Tobago and author's calculations
Notes: Output produced is expressed as an index with 2016 = 1. Output exported, also expressed as an index, is scaled to replicate the proportion of production sold to foreign markets. Petrochemicals production includes ammonia, methanol, and urea, for which virtually all output is exported.

Hydrocarbons-related activities have largely contributed largely to the country's income and foreign exchange receipts (Figure 6 and 7). During the two energy price booms, the energy sector generated 38 percent of annual GDP at constant prices, on average; while in the non-booming period of 1983–2001 the sector's contribution never failed to exceed 25 percent. Similarly, hydrocarbons and petrochemicals represented 85 percent of total exports during both energy price booms, on average; while the share often exceeded 65 percent in 1983–2001. Foreign exchange receipts were buoyant in the last boom because high energy prices in world markets were compounded with the progress in monetizing Trinidad and Tobago's natural gas wealth. Measured at 2016 constant U.S. PPI prices, annual exports averaged US$11 billion and significantly strengthened the country's capacity to import, repay foreign debts, and build international reserves and external assets (e.g., the Heritage and Stabilisation Fund). Notably, the size and structure of energy exports reflected the underlying transformation of the hydrocarbon economy. While oil largely dominated the energy export basket until the 1990s, it represented around 45 percent during the last boom, on average. Sales of LNG and petrochemicals to foreign markets, on the other hand, increased their share of energy exports to 33 percent and 22 percent, respectively.

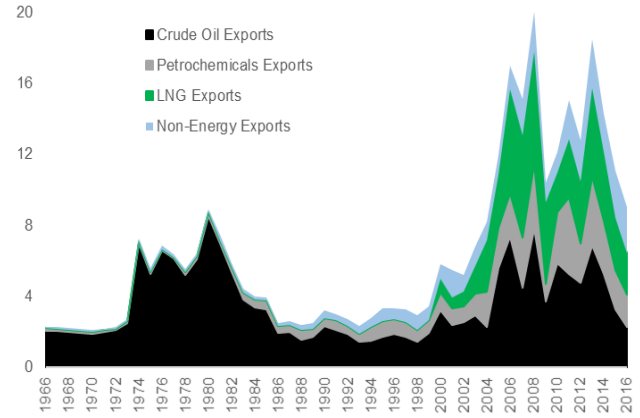
[4] For instance, the real price of Russian natural gas sold to Germany increased from US$9/mmbtu in 2010 to an average of US$11/mmbtu in 2011-2014, while the real price of Indonesian LNG sold to Japan rose from US$10/mmbtu to around US$17/mmbtu in those years.

Figure 6. Composition of Real GDP



Sources: Central Bank of Trinidad and Tobago and author's calculations

Figure 7. Composition of Real Exports

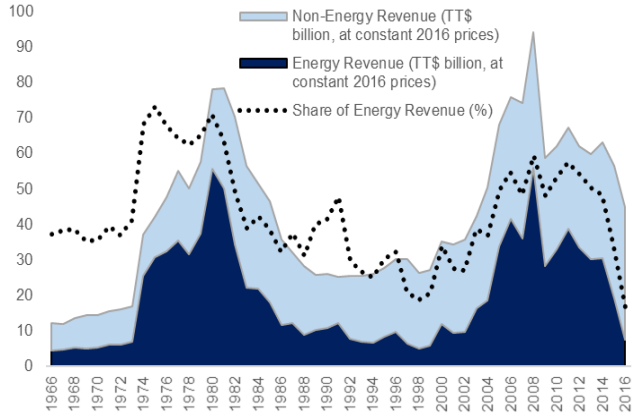


Sources: Central Bank of Trinidad and Tobago and author's calculations
Notes: Nominal export values expressed in billions of U.S. dollars and deflated using the U.S. Producer Price Index 2016 = 1. Petrochemicals exports include ammonia, methanol, and urea.

Fiscal and Growth Performance in an Energy-Dependent Economy

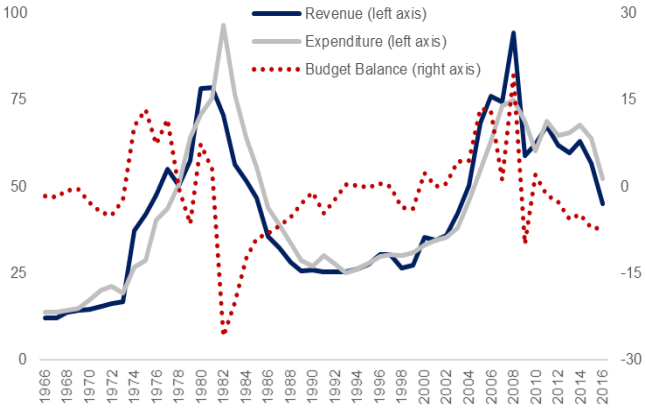
Fiscal institutions and policies underpin the linkages between the energy sector and the Government's public finances (Figure 8 and 9). A sizable (albeit volatile) source of fiscal resources results from the taxation of energy companies through the corporate income tax on hydrocarbon producers and the supplemental petroleum tax. These resources represented two-thirds of total budgetary revenues during the 1973–1982 boom, and nearly half of them in the 2002–2015 boom. In the second boom, in particular, energy revenue benefitted from rising oil and gas prices together with growing volumes of natural gas. It then increased from 10 percent of GDP in the early 2000s to nearly 20 percent in 2008, and subsequently fluctuated around 17 percent of GDP until 2014; when commodity prices collapsed, energy revenue fell to 11 percent of GDP in 2015 and further to 5 percent in 2016. As fiscal policy often aimed to share the country's natural resource wealth among citizens and stimulate the non-energy domestic economy, the buoyancy of energy revenue tended to fund an expansion of budget expenses.[5] In this context, the cycles in commodity prices and production induce cycles in public finances.

Figure 8. Composition of Real Fiscal Revenue



Sources: Central Bank of Trinidad and Tobago and author's calculations
Notes: Nominal revenues deflated using the Retail Price Index 2016 = 1.

Figure 9. Real Fiscal Revenue and Expenditure



Sources: Central Bank of Trinidad and Tobago and author's calculations
Notes: Nominal values expressed in TT$ billion and deflated using the Retail Price Index 2016 = 1.

[5] Only a few years back energy revenues were saved in the Heritage and Stabilisation Fund. International experience shows that resource-rich countries often expand government expenditures when benefitting from a windfall of resource-related fiscal revenue, and some at least partially save these resources in sovereign wealth funds or similar arrangements. On this issue, see IMF, 2012, *Macroeconomic Policy Frameworks for Resource-Rich Developing Countries*; and IMF, 2016, *Fiscal Policy: How to Adjust to a Large Fall in Commodity Prices*.

Boom-and-bust cycles in the domestic non-energy economy follow developments in the energy sector. The evolution of hydrocarbon-related activities affects the growth performance of the wider economy through the channels discussed earlier: the demand for domestic output is supported by public expenditure funded with energy revenues, and the capacity to import capital goods and technology is buttressed by the foreign exchange inflows associated with energy exports. Historically, the path of energy prices and production correlates with the pace of expansion (or contraction) of the non-energy economy. For the purpose of qualitatively appreciating such a relation, the evolution of the energy and non-energy sectors can be jointly observed over a few sub-periods in which the commodity price and output conditions evolved in particular ways (Table 1). Seven sub-periods identified are the following: the years before the first boom when the oil sector was still expanding (1966–1972); the first boom (1973–1982); the post-boom years when oil fields started maturing (1983–1995); the commencement of major natural-gas-related projects (1996–2001); the second boom with high energy prices and rapid expansion of LNG and petrochemicals (2002–2008); the brief interlude when energy prices fell and the natural gas sector virtually reached a plateau; and the continuation of the second boom until its end (2011–2015).

Table 1. Economic Performance Across Stages of Energy Sector Development

	1966-1972	1973-1982	1983-1995	1996-2001	2002-2008	2009-2010	2011-2015
Real Crude Oil Price WTI (US$/b) (1)	7.6	47.7	38.0	32.5	68.7	78.5	85.4
Crude Oil Production (000' b/d)	154.1	203.1	149.5	122.2	130.2	102.5	82.9
Crude Oil Exports (000' b/d)	66.5	87.6	67.3	52.8	64.9	49.6	33.2
Crude Oil Exports Value (US$ billion) (1)	2.0	5.9	2.2	2.1	4.7	4.8	5.1
Real Natural Gas Price HH (US$/mmbtu) (1)				5.1	8.2	4.6	3.5
Natural Gas Production (bn cf/d)	0.3	0.4	0.7	1.2	3.2	4.2	4.1
LNG Exports (mn cu m)				6.1	24.3	34.1	31.6
LNG Exports Value (US$ billion) (1)				0.7	3.8	3.4	3.7
Real Petrochemicals Price (00' US$/metric tonne) (1)			2.4	2.1	3.5	3.2	4.5
Petrochemicals Production (Index 2016=1)	0.05	0.05	0.24	0.53	0.98	1.22	1.10
Petrochemicals Exports (Index 2016=1)	0.05	0.04	0.22	0.51	0.97	1.21	1.09
Petrochemicals Exports Value (US$ billion) (1)	0.1	0.1	0.5	0.8	2.2	1.9	3.1
Real GDP Growth (%)	3.4	5.5	-0.9	7.0	8.3	-0.5	0.5
Real GDP Growth - Petroleum (%)	-0.3	-1.7	-0.7	9.5	12.1	0.3	-2.4
Real GDP Growth - Non-Petroleum (%)	4.6	7.7	-1.8	6.2	6.3	-0.9	2.3
CG Total Revenue (2)	13.9	53.3	33.2	30.6	63.0	60.5	61.7
CG Energy Revenue (2)	5.2	33.9	12.0	8.0	30.2	30.6	30.3
CG Non-Energy Revenue (2)	8.7	19.4	21.2	22.6	32.7	29.9	31.4
CG Total Expenditure (2)	16.4	51.5	38.8	31.4	54.9	64.4	66.1
CG Capital Expenditure (2)	3.6	19.8	5.5	2.5	7.9	10.5	9.2
CG Current Expenditure (2)	12.8	31.8	33.3	28.9	47.1	54.0	56.9
CG Budget Balance (2)	-2.5	1.8	-5.6	-0.8	8.0	-4.0	-4.4

Sources: Central Bank of Trinidad and Tobago and author's calculations
Notes: (1) Values in 2016 constant U.S. dollars, deflated using the U.S. Producer Price index 2016 = 1. (2) Values in 2016 constant prices, deflated using the Retail Price Index 2016 = 1.

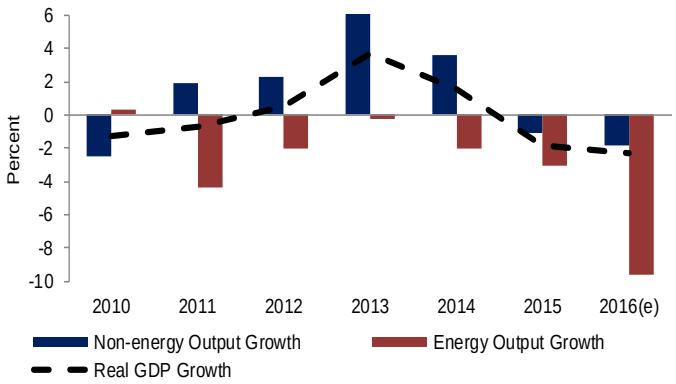
Historically, the non-energy economy benefitted from energy booms, but these spillovers have weakened at least since the global financial crisis. Performance of the non-energy economy was remarkably strong during the first boom (1973–1982) and the development of the natural gas industries (1996–2001 and 2002–2008). In those years, the average annual growth rate of non-petroleum GDP was around 6 to 7 percent, reflecting booms in construction and real estate as well as strong public and private consumption fuelling distribution and trade activity. Notably, the non-energy economy expanded at much lower rates after the global financial crisis, even during the second part of the energy boom (2011–2015). Such a growth slowdown poses concerns as to whether there are structural obstacles for the wider economy that have predominated over positive spillovers from the hydrocarbon-related activities or the fiscal policy stimuli.[6]

In the second part of the recent energy boom (2011–2015), fiscal policy resulted in unprecedented budget imbalances. Underpinning the growth of domestic economic output was always an expansionary fiscal policy funded with energy revenue. In particular, throughout the second boom (2002–2015), annual energy revenue averaged TT$30 billion in real terms, on top of a similar figure for non-energy revenue. Budget expenditure, in turn, was persistently increased until it reached an annual average of TT$66 billion in real terms in 2011–2015. As a consequence, the budget surpluses achieved in 2002–2008 turned to deficits after the financial crisis. Ostensibly, it was unprecedented that fiscal imbalances persisted even during the booming years of 2011–2015. Deficits have been further aggravated as energy prices have collapsed since mid-2015. In this context, concerns emerge as to whether fiscal policy is sustainable.[7]

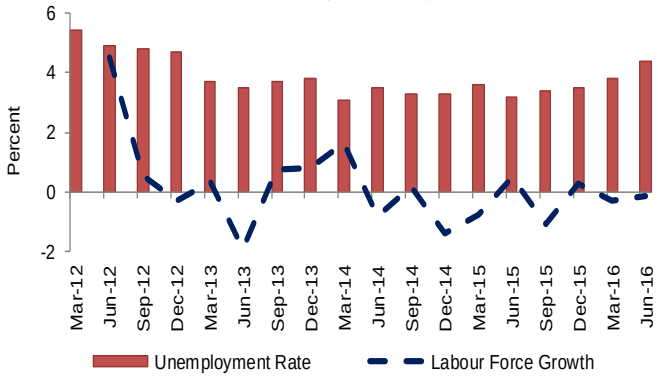
[6] On the structural obstacles currently facing the private sector operating in the non-energy economy in Trinidad and Tobago, see the IDB's Caribbean Region Quarterly Bulletin 2017:I, available at: https://publications.iadb.org/handle/11319/8210
[7] On the fiscal policy and outcomes during the second energy boom, see the IDB's Caribbean Region Quarterly Bulletin 2016:II, available at https://publications.iadb.org/handle/11319/7683

Trinidad and Tobago: A Snapshot of the Economy

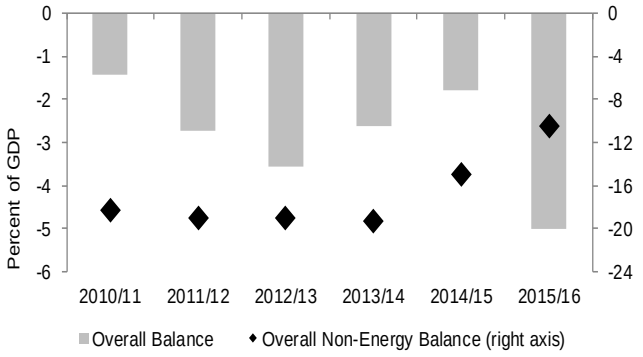
The economy entered into recession in 2015 ...



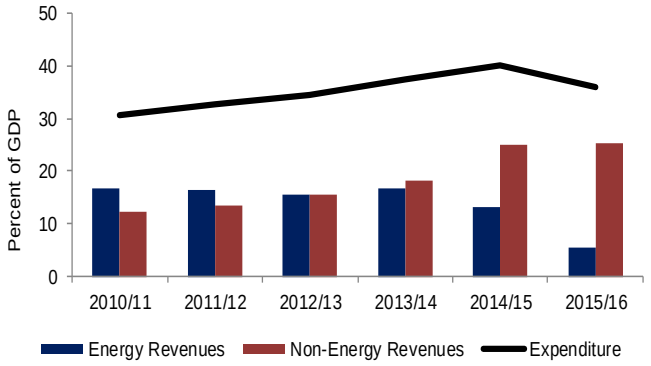
... and the labour market no longer creates jobs.



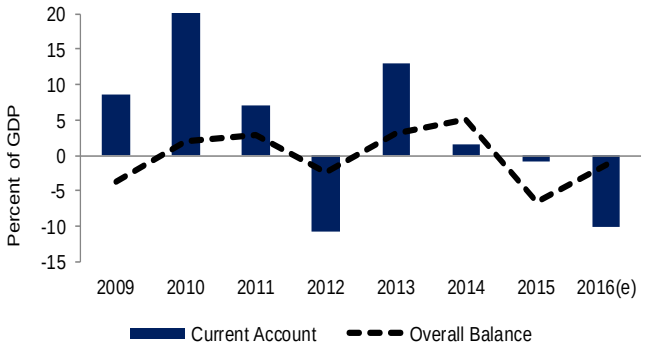
The Government's fiscal policy is geared towards consolidation ...



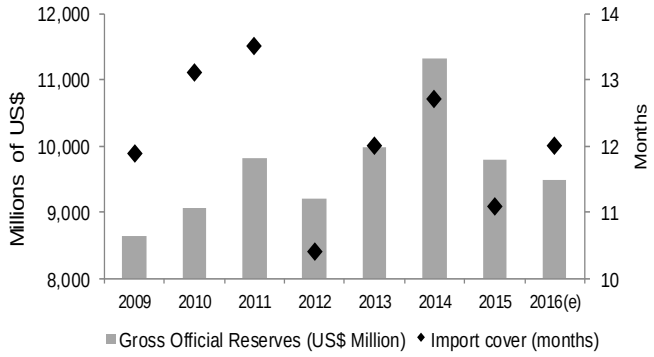
...with initiatives to boost non-energy revenue and cut expenditure.



The external position continues deteriorating ...



... which further tightens the foreign exchange market.



Source: Central Bank of Trinidad and Tobago

	2010	2011	2012	2013	2014	2015	2016
			(Annual percentage changes, unless otherwise specified)				
Real Sector and Prices							
Real GDP /1	-1.3	-0.7	0.5	3.7	1.5	-1.8	-2.3
Real GDP - Energy /1	0.3	-4.4	-2.0	-0.2	-2.0	-3.1	-9.6
Real GDP - Non-energy /1	-2.5	1.9	2.3	6.1	3.6	-1.0	-1.8
Headline Inflation	10.5	5.1	9.3	5.2	5.7	4.7	3.1
Nominal GDP (TT$ billion)	131	163	165	170	168	150	146
Nominal GDP (US$ billion)	20.6	25.4	25.7	26.4	26.2	23.4	22.5
			(In percentage of GDP, unless otherwise specified)				
External Sector /2							
Exports (merchandise)	54.6	58.8	50.3	71.0	55.6	46.1	35.6
o.w. Energy Exports	45.8	49.5	38.1	57.6	46.1	35.9	26.7
Imports (merchandise)	31.6	37.3	45.4	47.9	43.0	40.4	39.6
o.w. Energy Imports	12.9	16.9	21.8	27.1	21.3	14.1	26.7
Trade Balance (merchandise)	23.0	21.5	5.0	23.2	12.6	5.7	-4.0
Services Balance	2.4	-2.5	-2.6	-1.7	-1.8	-3.2	-3.0
Income Balance	-5.2	-12.1	-13.2	-8.6	-9.2	-3.3	-3.1
Current Transfers (net)	0.1	0.1	0.1	0.1	-0.1	-0.2	0.1
Current Account	20.3	7.0	-10.7	13.0	1.4	-1.0	-10.0
Capital and Financial Account	-18.2	-4.1	8.2	-10.0	3.6	-5.6	8.7
Overall Balance	2.0	3.0	-2.4	3.0	5.1	-6.5	-1.3
Variation in Int'l Reserves (US$ billion)	0.4	0.8	-0.6	0.8	1.3	-1.5	-0.3
			(In percentage of GDP)				
Central Government (on a FY basis) /3							
Revenue and Grants	34.0	29.2	29.8	31.0	34.8	38.1	30.8
o.w. Energy Revenues	17.6	16.9	16.3	15.5	16.7	13.2	5.4
Current Expenditure	28.9	25.5	26.9	28.9	32.4	34.8	32.6
o.w. Transfers and Subsidies	17.4	15.4	16.5	17.7	20.7	20.4	18.8
Capital Expenditure and Net Lending	5.0	5.0	5.7	5.6	5.0	5.1	3.2
Primary Balance	2.3	0.3	-1.0	-1.9	-0.8	0.5	-2.9
Overall Balance	0.1	-1.4	-2.7	-3.5	-2.6	-1.8	-5.0
Debt Indicators (on a FY basis) /3							
Net Public Sector Debt	34.7	29.7	38.9	38.4	41.8	51.0	60.9
CG External Debt	8.6	7.8	8.2	7.0	8.9	10.6	16.2
CG External Debt Service	1.8	0.6	0.7	1.2	0.6	0.7	0.9

Source: Central Bank of Trinidad and Tobago (CBTT), Central Statistical Office (CSO), and Ministry of Finance (MOF)
Notes: 1/ CBTT estimates using QGDP Index until 2015 and CSO estimates in 2016
2/ Trade and BOP data for 2011-2016 are being revised by the CSO and CBTT
3/ For instance, the figures reported in 2016 correspond to FY2015/16

Contributors: Shamar Blenman and Juan Pedro Schmid

Recent Developments[1]

Growth in the OECS moderated slightly in 2016, averaging 2.4 percent compared to 2.6 percent in 2015. According to the Eastern Caribbean Central Bank (ECCB), Antigua and Barbuda led the way with robust growth of 4.4 percent, up from 4.1 percent in 2015. Economic activity also accelerated in St. Vincent and the Grenadines, which grew at 3 percent compared to 1.6 percent in 2015. Growth remained stable at 3.6 percent in St. Kitts and Nevis. However, the rate of growth slowed in Grenada from 6.2 percent in 2015 to 1.9 percent in 2016 and in St. Lucia from 1.9 to 0.7 percent over the same period. Dominica moved from a contraction of -1.8 percent in 2015 to grow by 0.9 percent.

Tourism performance was mixed in 2016. Total visitor arrivals to the OECS declined slightly by 0.6 percent, with a 2.9 percent increase in stay-over arrivals offset by a 1.9 percent fall in cruise passengers. Total visitor expenditure remained flat at US$1,590.7 million. While only Grenada (9.7 percent), St. Kitts and Nevis (3.7 percent), and St. Vincent and the Grenadines (5.7 percent) saw increases in total visitor arrivals, all countries with the exception of St. Kitts and Nevis saw higher stay-over arrivals. However, stay-over arrivals from the United Kingdom fell by 2.5 percent across the OECS, likely related to the Brexit referendum and the depreciation of the British pound.

The fiscal situation improved in 2016. Dominica, Grenada, and St. Vincent and the Grenadines experienced fiscal deficits in 2015 but achieved surpluses in 2016, while St. Lucia realized a lower fiscal deficit in 2016. These improvements were largely driven by higher tax revenue and lower capital expenditure; however, current expenditure increased in all of the countries. Dominica's fiscal surplus of 11.5 percent of GDP was achieved primarily as a result of inflows under its Citizenship by Investment (CBI) Programme, with non-tax revenues reaching 24.5 percent of GDP in 2016, up from 5.3 percent in 2015. It is noteworthy that these inflows are volatile. Antigua and Barbuda and St. Kitts and Nevis achieved smaller fiscal surpluses in 2016, as the pace of expenditure growth outstripped the pace of revenue growth in the case of Antigua and Barbuda, while in St. Kitts and Nevis both tax revenues and non-tax revenue inflows under its CBI Programme fell.

Highlights

- *Economic growth in the OECS slowed in 2016 to 2.4 percent, compared to 2.6 percent in 2015.*
- *The fiscal situation improved in 2016.*
- *On the back of lower oil prices, inflation was low in 2016.*
- *Oil prices directly influence external sustainability, fiscal outcomes, and even economic growth.*

Current account deficits remained high in 2016. However, there was improvement in the current account in Dominica (from -8 to -7.8 percent of GDP), Grenada (from -17.7 to -17.5 percent of GDP), and St. Vincent and the Grenadines (from -21.2 to -18.9 percent of GDP). On the other hand, the current account balance deteriorated in Antigua and Barbuda (from -5.2 to -5.9 percent of GDP), St. Kitts and Nevis (from -8.5 to -14.5 percent of GDP), and St. Lucia (from -2.6 to -6.7 percent of GDP). The widening of the current account deficit in St. Kitts and Nevis in particular came as a result of lower budgetary receipts from its CBI Programme. In St. Lucia, lower exports of goods led the widening of the current account deficit.

Inflation was low in 2016. Prices fell by 3 percent in St. Lucia, 1.1 percent in Antigua and Barbuda, and 0.05 percent in St. Kitts and Nevis. This deflation was driven by a fall in the price for food and non-alcoholic beverages; housing, utilities, gas and fuels; and transport. On the other hand, there was inflation of 1.6 percent in Dominica and 1 percent in both St. Vincent and the Grenadines and Grenada. These developments were influenced by higher price indexes for housing, utilities, gas, and fuels in Dominica; transport and communication in Grenada; and food and non-alcoholic beverages and transport in St. Vincent and the Grenadines.

Credit to the private sector continued to fall across the OECS, declining by 1.3 percent in 2016 compared to a fall of 4.5 percent in 2015. However, this decline was driven by St. Lucia, where credit fell by 5 percent, with less lending to households and businesses. Lending to the private sector expanded in Dominica (2.9 percent), St. Kitts and Nevis (0.9 percent), and St. Vincent and the Grenadines (1.3 percent) but remained flat in Antigua and Barbuda (0.1 percent) and Grenada (-0.2 percent). Over the first two months of 2017, credit to the private sector in the OECS fell by 0.3 percent, representing declines in

[1] This bulletin focuses on developments in the independent countries of the OECS: Antigua and Barbuda, Dominica, Grenada, St. Kitts and Nevis, St. Vincent and the Grenadines, and St. Lucia. Figures exclude territories that are members of the OECS.

each individual country. The lack of access to finance in the OECS is reported by firms as a major challenge for business operations.

Interest rate spreads have increased since the lowering of the minimum deposit rate by the ECCB. At the time of the lowering of the minimum deposit rate from 3 to 2 percent in April 2015, the average interest rate spread in the OECS ranged from 5.9 percent in Dominica to 6.8 percent in both Antigua and Barbuda and St. Vincent and the Grenadines. By the end of December 2016, the average interest rate spread increased to a range of 6.4 percent in Dominica to 7.4 percent in Antigua and Barbuda. This comes as the fall in average lending rates has not kept pace with the fall in average deposit rates, highlighting a major reason for declining credit to the private sector throughout the OECS.

St. Lucia presented its budgetary proposals for FY2017/18. Budgeted expenditure is EC$1.513 billion, a 6.1 percent increase over the 2016/17 approved estimates, with EC$1.151 billion allocated to recurrent expenditure and EC$362 million to capital expenditure.[2] Some of the fiscal measures announced in the presentation include enactment of a Public Financial Management Bill; plans to simplify and make more progressive the personal income tax system; and an increase in the excise tax on gasoline and diesel from EC$2.50 per gallon to EC$4.00 per gallon to fund road rehabilitation and expansion of the road network. Earlier in February 2017, the value-added tax rate was reduced from 15 to 12.5 percent.

Outlook

Growth in the OECS is expected to accelerate in 2017 to between 2.4 percent (according to the International Monetary Fund - IMF) and 2.7 percent (according to the ECCB). According to the ECCB's estimates, St. Kitts and Nevis is expected to lead the way with growth of 5.4 percent; the IMF has a more cautious estimate of 3.5 percent. More moderate growth is expected in Dominica (3.1 percent), Antigua and Barbuda (2.9 percent), Grenada (2.7 percent), and St. Vincent and the Grenadines (2.2 percent). In St. Lucia, while the ECCB expects a contraction of -0.2 percent, the IMF forecasts growth of 0.5 percent.

Construction activity should continue to be robust, especially with continued reconstruction efforts and the building of a new hospital in Dominica; the building of a new secondary school and a second cruise berthing facility in St. Kitts and Nevis; and other public and private sector works among the other members.

Tourism performance is also expected to improve with additional flights to Antigua and Barbuda, St. Kitts and Nevis, and St. Lucia; new cruise ship calls in Dominica; and the expansion of hotel room stock in Grenada and St. Kitts and Nevis. However, St. Lucia's new airport tax may compromise its tourism performance.

Agriculture should also play a strong role in Dominica, St. Lucia, and St. Vincent and the Grenadines.

Fiscal balances could deteriorate in the OECS in 2017. St. Kitts and Nevis could see an overall fiscal deficit for the first time since 2010 as inflows from the CBI Programme taper off, leading to deterioration in the primary balance. Dominica could also see a reversal back to a fiscal deficit as inflows under its CBI Programme moderate. St. Lucia and Antigua and Barbuda should continue to have fiscal deficits, while in Grenada and St. Vincent and the Grenadines fiscal surpluses should stay the same.

The external current account imbalance may widen in 2017. Construction-related imports and projected rises in international oil and commodity prices may force the widening of current account deficits. In St. Kitts and Nevis, in particular, lower inflows from its CBI Programme would contribute to widening the deficit. This would be tempered by continued improvements in tourism arrivals.

Inflation will be contained 2017. Over the medium term, the Consumer Price Index is expected to follow the gradual increase in international fuel and food import prices.

High-Frequency Macroeconomic Indicators				
	Last Data	Period	Last Data	Period
Annual GDP growth (percent)	2.1	Dec-16	2.2	Dec-15
Tourism arrivals (annual percent change)	(1.0)	Jun-16	5.6	Mar-16
Inflation (end of period)	0.10	Sep-16	(0.06)	Jun-16

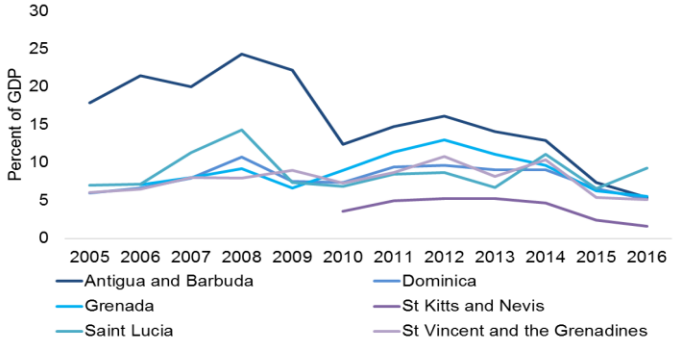
Source: Eastern Caribbean Central Bank, 2017.

[2] Exchange rate: US$1 = EC$2.7.

Introduction

The members of the OECS are heavily dependent on commodity imports and as such are vulnerable to commodity price fluctuations. Being small and with few natural resources, the countries of the OECS import their fuel for consumption. As such, from 2005–2016 fuel imports consumed a major portion of GDP throughout the OECS, ranging from 4 percent in St. Kitts and Nevis to 15 percent in Antigua and Barbuda (Figure 1). Fuel has consumed the largest share of the import bill in Antigua and Barbuda and Grenada, accounting for over 35 and 21 percent of total imports, respectively.

Figure 1: Imports (percent of GDP)



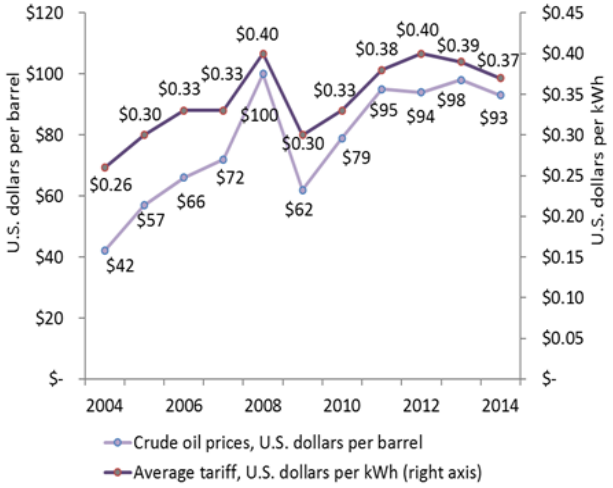
Source: Eastern Caribbean Central Bank, 2017.

External Accounts and Commodities

High international oil prices pressure external balances. As the OECS member countries are very dependent on fuel imports, rising international prices cause a widening in current account deficits throughout the union. From 2011–2014, when international oil prices fluctuated between US$70 and US$110 per barrel, current account deficits in the OECS averaged 16 percent of GDP, with oil imports accounting for 9-10 percent of GDP. Then in 2015–2016, when oil prices dipped below US$60 per barrel, current account deficits narrowed to around 11 percent of GDP, with oil imports averaging 5-6 percent of GDP.

Fuel prices affect the cost of electricity. Although there is some installed capacity for renewable energy in the OECS, electricity generation is primarily from fossil fuels. As a result of this reliance on imported petroleum products, electricity tariffs are high, as fuel costs are passed through to the end-consumer under a fuel surcharge. Figure 2 illustrates a correlation between average tariffs in the OECS and crude oil prices. Between 2000 and 2004 average electricity tariffs in the OECS were US$0.24-US$0.26 per kWh, with crude oil prices averaging between US$30 and US$42 per barrel. However, by 2008 when the price of oil rose to an average of US$100 per barrel, average tariffs in the Eastern Caribbean rose to US$0.40 per KWh. With the annual average crude oil price dipping to below US$50 per barrel in 2015–2016, average tariffs fell to US$0.28 KWh in 2016.

Figure 2. Average Tariffs (U.S. dollars per kWh) in OECS Countries and Crude Oil Prices (U.S. dollars per barrel)



Source: Castalia Strategic Advisors, 2015.

Fiscal Accounts and Commodities

Energy subsidies negatively impact the fiscal accounts. In periods of high international oil prices, governments in the OECS sought to smooth the prices of electricity and transportation fuel to reduce volatility and keep prices low. This came primarily in the form of reduced rates on consumption or excise taxes. Consequently, this results in foregone revenues for the respective governments. Di Bella et al. (2015)[3] estimated that as a result of these subsidies, foregone revenues from 2011–2013 amounted to 1.2 percent of GDP in Antigua and Barbuda; 0.9 percent in Grenada; 0.6 percent in St. Kitts and Nevis; 0.3 percent in St. Lucia; and 0.1 percent in Dominica. High international oil prices also affect public expenditure, with more of the limited budgets devoted to paying for energy consumption by the various ministries and state-owned enterprises. Lower international oil prices since 2015 would therefore have been positive for fiscal management in the Eastern Caribbean.

[3] Di Bella et al (2015), "Energy Subsidies in Latin America and the Caribbean: Stocktaking and Policy Challenges," IMF Working Paper 15/30, International Monetary Fund, Washington, DC.

PetroCaribe provided favourable financing terms when oil prices were high. All six OECS member countries signed the PetroCaribe Cooperation Agreement in June 2005, which enabled them to receive loans at concessional rates for the purchase of oil from Venezuela. St. Lucia, however, did not access financing under the agreement. In times of high oil prices, PetroCaribe financing was used to fund social public spending programs in the OECS. With oil prices low, funding has decreased, leaving these governments to reduce social spending or look elsewhere to finance it. At the end of 2014, the total outstanding PetroCaribe debt in the OECS was US$405.9 million, with Grenada being the most indebted country with debt of US$134.1 million.[4]

Economic Growth

Oil prices affect GDP. McIntyre et al. (2016) estimated the impact of oil price shocks on real GDP growth variation throughout the Caribbean.[5] They found that around 7.8 percent of real GDP variation in the OECS can be explained by oil price changes. Dominica and Grenada are the most susceptible, with an oil price shock explaining 15 percent and 14 percent variations, respectively. The variation in St. Lucia and St. Kitts and Nevis was more moderate at 7 percent and 5 percent, respectively, while the variation was low in St. Vincent and the Grenadines and Antigua and Barbuda at 3 percent and 2 percent of real GDP, respectively.

Conclusions and Policy Implications

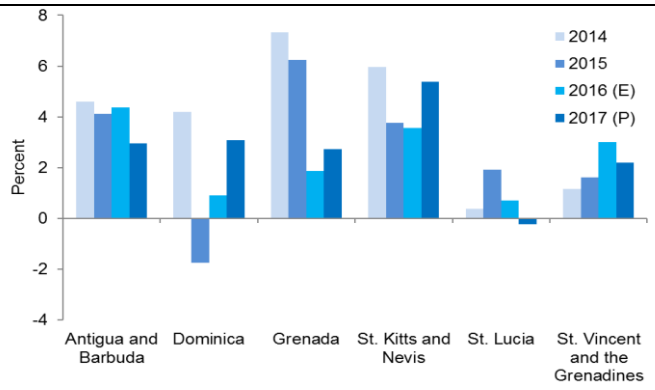
Reducing dependency on imported fossil fuels is achievable with available renewable energy potential. Geothermal energy represents the most significant potential in the Eastern Caribbean, totalling 620 megawatts.[6] Dominica is poised to benefit the most with 300 megawatts of geothermal potential. In fact, Dominica is in the most advanced stage of development, having successfully dug a production well with potential power generation capacity of 7-9MW. The government is now seeking to secure funding for construction of a geothermal plant, with the expectation that it will become operational by the end of 2019. St. Kitts and Nevis and St. Vincent and the Grenadines have begun exploratory drilling, while Grenada and St. Lucia have conducted pre-investment studies but have yet to commence exploratory drilling. Antigua and Barbuda does not have geothermal energy potential. Outside of geothermal energy, the countries of the OECS have hydro, wind, and solar photovoltaic potential that can be exploited to diversify the energy mix and reduce dependency on imported fossil fuels. The IDB and the Caribbean Development Bank have partnered with the OECS governments with a US$50 million loan for the Sustainable Energy Facility for the Eastern Caribbean to help these countries realise their renewable energy potential and improve energy efficiency.

[4] Eastern Caribbean Central Bank, “The Impact of Dismantling the Petro Caribe Agreement in the ECCU – A Case Approach,” 2015.
[5] A. McIntyre et al “Caribbean Energy: Macro-Related Challenges,” IMF Working Paper 16/53, International Monetary Fund, Washington, DC.
[6] According to the Eastern Caribbean Currency Union 2016 Article IV Consultation by the IMF.

The OECS Countries at a Glance

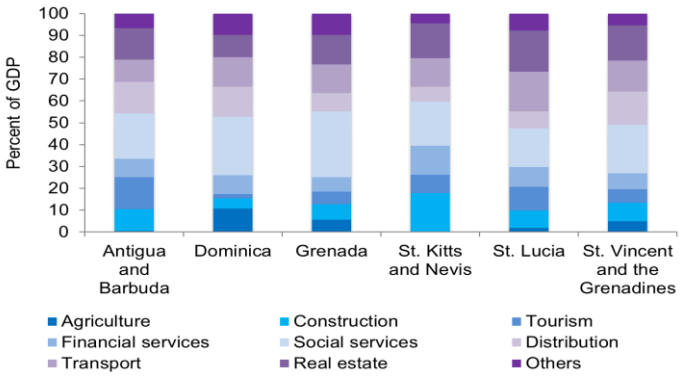
Growth is recovering in the OECS countries…

Figure a. Real GDP Growth, 2014–2017 (percent)



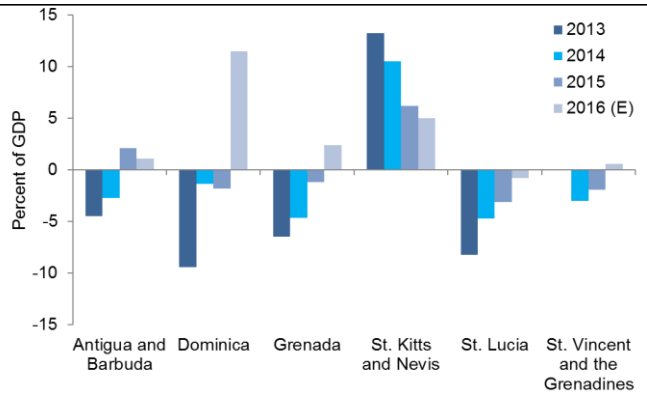
…with tourism, construction, and agriculture leading the way.

Figure b. Contribution to GDP, 2016 (percent of GDP)



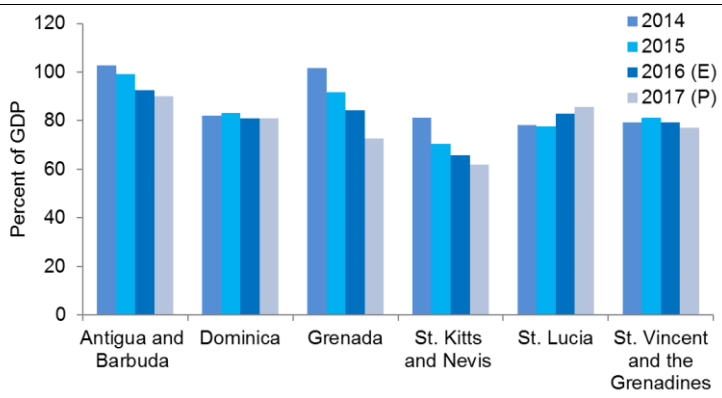
Fiscal deficits are declining…

Figure c. Fiscal Deficit, 2013–2016 (percent of GDP)



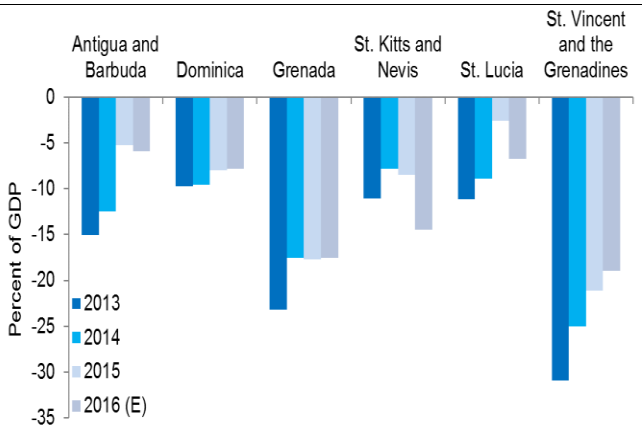
…but debt remains above 60% of GDP

Figure d. Central Government Debt, 2014–2017 (percent of GDP)



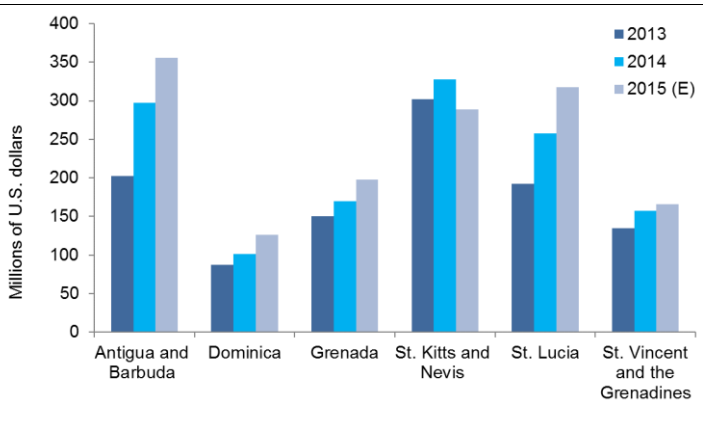
Current account deficits are high…

Figure e. Current Account Balance, 2013–2016 (percent of GDP)



…but reserves improved over time.

Figure f. Gross International Reserves, 2013–2015 (millions of U.S. dollars)



Sources: Eastern Caribbean Central Bank; and IMF, *World Economic Outlook* (April 2017).

Selected Economic Indicators for OECS Countries

	2012	2013	2014	2015	2016 (E)	2017 (P)
Antigua and Barbuda						
Annual percentage change unless otherwise indicated						
Real Sector						
Real GDP	3.8	(0.2)	4.6	4.1	4.4	2.9
Nominal GDP	6.5	(1.7)	6.6	6.4	6.9	5.5
Consumer prices (end of period)	1.8	1.1	1.3	0.9	(1.1)	…
Consumer prices (period average)	3.4	1.1	1.1	1.0	(0.5)	…
Annual percentage change unless otherwise indicated						
External Sector						
Exports of goods and services	3.2	(1.5)	3.2	6.0	1.4	1.5
Imports of goods and services	17.2	(7.5)	6.1	(24.3)	2.5	2.0
Current account (percent of GDP)	(14.8)	(15.1)	(12.5)	(5.2)	(5.9)	(9.8)
In percent of GDP						
Public Sector						
Total revenue	19.8	18.6	19.8	23.8	24.6	…
Current expenditure	20.5	21.7	20.9	20.3	20.4	…
Capital expenditure and net lending	0.6	1.3	1.6	1.4	3.1	…
Primary balance	1.1	(2.4)	(0.1)	4.6	3.9	…
Overall balance	(1.3)	(4.5)	(2.7)	2.1	1.1	…
General government gross debt	86.4	94.8	102.7	99.1	92.7	90.1
In millions of EC dollars						
Memo						
Nominal GDP at market value	3,283.3	3,228.9	3,440.7	3,660.2	3,912.7	4,126.8
Dominica						
Annual percentage change unless otherwise indicated						
Real Sector						
Real GDP	(1.1)	0.8	4.2	(1.8)	0.9	3.1
Nominal GDP	(3.0)	4.6	3.9	(2.1)	1.6	4.0
Consumer prices (end of period)	1.3	(0.4)	0.5	(0.5)	1.6	…
Consumer prices (period average)	1.4	(0.0)	0.8	(0.8)	0.3	…
Annual percentage change unless otherwise indicated						
External Sector						
Exports of goods and services	(15.7)	27.6	15.8	8.8	8.9	1.7
Imports of goods and services	(7.7)	(0.1)	14.4	5.6	9.7	2.0
Current account (percent of GDP)	(17.3)	(9.7)	(9.5)	(8.0)	(7.8)	(9.5)
In percent of GDP						
Public Sector						
Total revenue	27.7	27.9	31.8	31.0	50.6	…
Current expenditure	24.1	25.7	24.7	26.9	27.9	…
Capital expenditure and net lending	12.8	11.7	8.5	5.9	11.2	…
Primary balance	(7.6)	(7.4)	0.4	0.0	13.4	…
Overall balance	(9.2)	(9.4)	(1.4)	(1.8)	11.5	…
General government gross debt	72.4	80.1	82.2	83.0	81.0	81.0
In millions of EC dollars						
Memo						
Nominal GDP at market value	1,311.9	1,372.8	1,426.1	1,396.5	1,418.6	1,474.9

Selected Economic Indicators for OECS Countries *(continued)*

	2012	2013	2014	2015	2016 (E)	2017 (P)
			Grenada			
			Annual percentage change unless otherwise indicated			
Real Sector						
Real GDP	(1.2)	2.4	7.3	6.2	1.9	2.7
Nominal GDP	2.7	5.3	8.2	8.0	3.3	4.8
Consumer prices (end of period)	1.8	(1.2)	(0.6)	1.1	0.9	…
Consumer prices (period average)	2.4	(0.0)	(1.0)	(0.5)	1.6	…
			Annual percentage change unless otherwise indicated			
External Sector						
Exports of goods and services	(4.4)	(1.7)	15.9	6.0	4.1	5.8
Imports of goods and services	(0.4)	10.6	(5.9)	17.8	11.1	4.6
Current account (percent of GDP)	(21.1)	(23.2)	(17.5)	(17.7)	(17.6)	(18.7)
			In percent of GDP			
Public Sector						
Total revenue	20.7	20.6	24.5	24.8	27.4	…
Current expenditure	21.2	20.3	20.0	17.6	20.6	…
Capital expenditure and net lending	5.0	6.8	9.2	8.4	4.4	…
Primary balance	(2.1)	(3.4)	(1.2)	2.2	5.4	…
Overall balance	(5.5)	(6.5)	(4.7)	(1.2)	2.4	…
General government gross debt	103.3	108.1	101.8	91.7	84.4	72.6
			In millions of EC dollars			
Memo						
Nominal GDP at market value	2,159.7	2,274.9	2,461.2	2,657.0	2,743.8	2,875.4
			St. Kitts and Nevis			
			Annual percentage change unless otherwise indicated			
Real Sector						
Real GDP	(0.6)	6.2	6.0	3.8	3.6	5.4
Nominal GDP	(2.5)	7.3	7.6	3.4	4.6	6.2
Consumer prices (end of period)	0.5	0.6	(0.5)	(2.4)	(0.0)	…
Consumer prices (period average)	0.8	1.1	0.2	(2.3)	(0.8)	…
			Annual percentage change unless otherwise indicated			
External Sector						
Exports of goods and services	7.3	16.8	16.4	13.1	(7.5)	(5.9)
Imports of goods and services	(6.5)	23.3	6.3	10.9	5.2	1.0
Current account (percent of GDP)	(7.6)	(11.1)	(7.8)	(8.5)	(14.5)	(18.3)
			In percent of GDP			
Public Sector						
Total revenue	42.4	46.2	43.4	40.2	35.0	…
Current expenditure	27.6	26.3	27.2	27.0	26.7	…
Capital expenditure and net lending	3.6	6.7	5.7	7.0	3.3	…
Primary balance	17.1	17.0	13.9	8.2	6.6	…
Overall balance	11.2	13.2	10.5	6.2	5.0	…
General government gross debt	137.9	101.1	81.4	70.6	65.8	61.9
			In millions of EC dollars			
Memo						
Nominal GDP at market value	1,983.0	2,128.0	2,289.0	2,366.5	2,475.6	2,628.2

Selected Economic Indicators for OECS Countries *(continued)*

	2012	2013	2014	2015	2016 (E)	2017 (P)
			St. Lucia			
			Annual percentage change unless otherwise indicated			
Real Sector						
Real GDP	(1.4)	0.1	0.4	1.9	0.7	(0.2)
Nominal GDP	1.4	1.5	5.2	3.2	(3.7)	2.3
Consumer prices (end of period)	5.0	(0.7)	3.7	(2.6)	(3.0)	…
Consumer prices (period average)	4.2	1.5	3.5	(1.0)	(3.1)	…
			Annual percentage change unless otherwise indicated			
External Sector						
Exports of goods and services	(4.3)	3.0	5.2	12.7	(5.6)	(2.0)
Imports of goods and services	(8.4)	(1.1)	3.0	1.3	7.3	(0.9)
Current account (percent of GDP)	(13.5)	(11.1)	(8.9)	(2.6)	(6.7)	(8.8)
			In percent of GDP			
Public Sector						
Total revenue	28.7	30.2	32.8	33.9	34.5	…
Current expenditure	28.3	29.0	30.1	29.7	30.5	…
Capital expenditure and net lending	8.3	9.5	7.3	7.3	4.8	…
Primary balance	(3.6)	(3.6)	0.3	1.9	4.2	…
Overall balance	(7.8)	(8.2)	(4.7)	(3.1)	(0.8)	…
General government gross debt	74.5	77.2	78.1	77.8	82.9	85.6
			In millions of EC dollars			
Memo						
Nominal GDP at market value	2,919.9	2,921.7	2,932.5	2,989.0	3,009.9	3,002.8
			St. Vincent and the Grenadines			
			Annual percentage change unless otherwise indicated			
Real Sector						
Real GDP	1.4	1.8	1.2	1.6	3.0	2.2
Nominal GDP	2.5	4.1	0.9	1.3	4.5	3.7
Consumer prices (end of period)	1.0	-	0.1	(2.1)	1.0	…
Consumer prices (period average)	2.6	0.8	0.2	(1.7)	(0.1)	…
			Annual percentage change unless otherwise indicated			
External Sector						
Exports of goods and services	1.4	(2.8)	3.9	2.2	2.4	7.5
Imports of goods and services	6.1	6.9	1.3	8.0	6.7	(2.5)
Current account (percent of GDP)	(27.6)	(30.9)	(25.1)	(21.2)	(18.9)	(18.4)
			In percent of GDP			
Public Sector						
Total revenue	-	-	29.3	28.8	29.4	…
Current expenditure	-	-	25.9	25.8	25.5	…
Capital expenditure and net lending	-	-	6.4	5.0	3.4	…
Primary balance	-	-	(0.7)	0.3	2.6	…
Overall balance	-	-	(3.0)	(1.9)	0.6	…
General government gross debt	72.5	75.0	79.4	81.3	79.2	77.2
			In millions of EC dollars			
Memo						
Nominal GDP at market value	1,870.9	1,947.3	1,965.4	1,991.7	2,081.2	2,158.0

Sources: Eastern Caribbean Central Bank; and IMF, *World Economic Outlook* (April 2017).
Notes: (P) = projections; (E) = estimates

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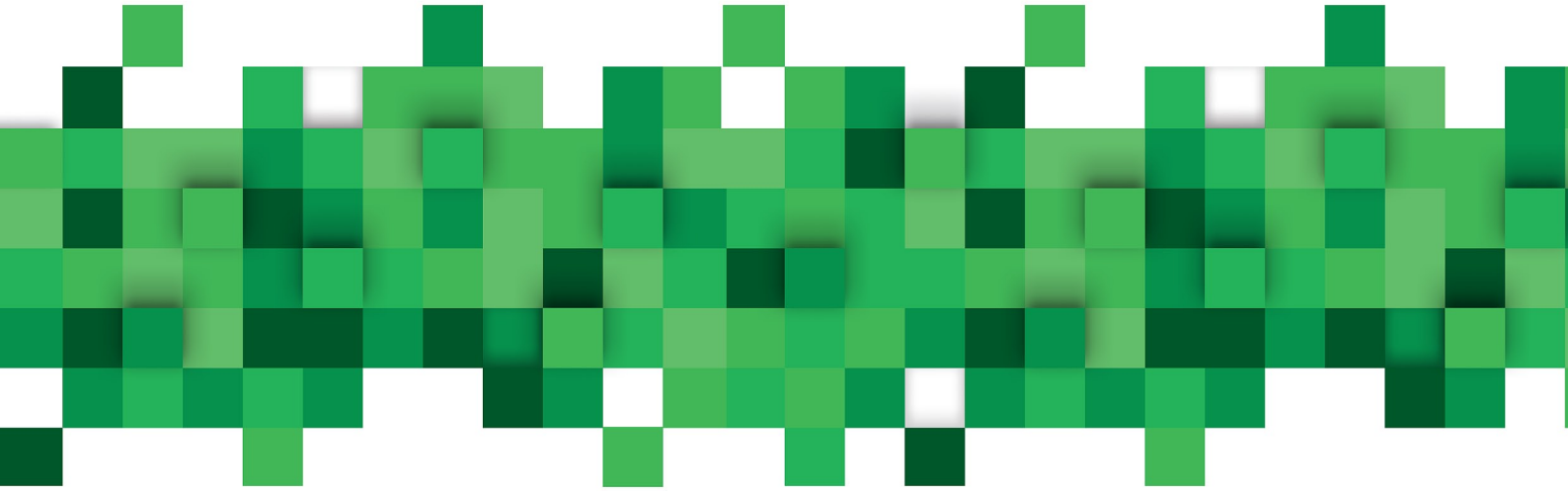

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