Caribbean Region Quarterly Bulletin

Development Challenges in the Caribbean

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Development Challenges in the Caribbean

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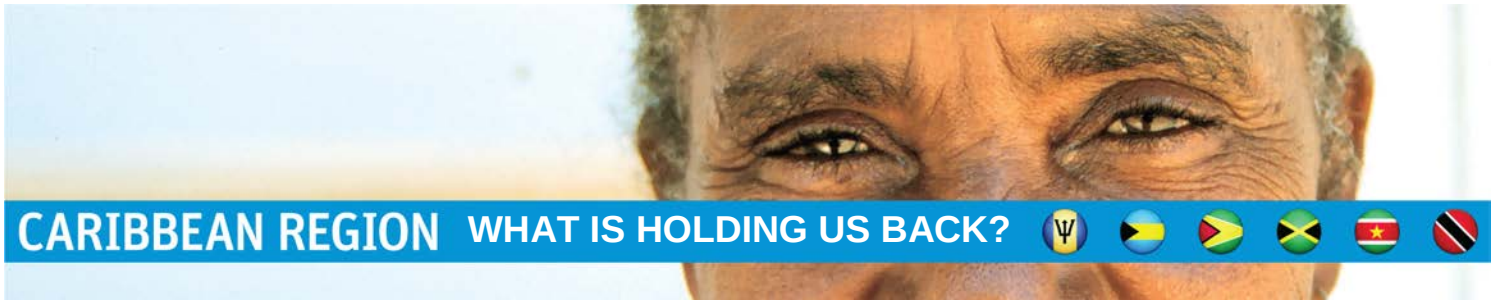


Dear Reader,

Welcome to the September 2018 *Caribbean Region Quarterly Bulletin.* The Caribbean economies are known for high debt and low growth. While this description is often accurate, the region also has huge potential, especially in the service and tourism sector. This quarterly bulleting gives an overview of the challenges that hold back growth and development and gives policy recommendations to accelerate growth, deepen socio-economic development and improve lives in the Caribbean countries.

Special Regional Report: Challenges to Development in the Caribbean

The countries that constitute the Inter-American Development Bank's Caribbean Country Department (CCB) differ in terms of languages and dialects, customs, foods, religions, and other traditions that can be traced to the diversity of the region's people, history, migration, culture, and geography. In terms of economic structure, an evident distinction is that three of the CCB countries – Guyana, Suriname, and Trinidad and Tobago – rely on commodities, while the other three CCB countries (The Bahamas, Barbados, and Jamaica) and the member countries of the Organisation of Eastern Caribbean States rely on services, with an emphasis on tourism.

In spite of these differences, several common development challenges emerge, including weak fiscal institutions, crime and violence, a sluggish private sector, weak productive development policies, skill-biased emigration, and other structural impediments. Taken together, these factors have resulted in a complex and challenging environment for promoting sustainable growth and development in the Caribbean. The situation is made more difficult by recurrent natural disasters, which are projected to increase in frequency in the future. The regional section of the Quarterly Bulletin provides a comparative overview of these issues, while the country summaries explores individual constraints to development in more depth.

The Bahamas

Developments in The Bahamas remained positive up to the period of review, with expected growth of 2.5 percent in 2018. Tourism indicators are continuing to trend upwards – for example, air arrivals were up 15 percent as at May 2018 – as foreign direct investments in private capital projects have supported the increasing level of construction-related activity within the archipelago. The fiscal balance has continued to show a cumulative deficit contraction over the first 10 months of FY2017/2018. The main contributors were declining flows in capital expenditure as the rebuilding of works following recent hurricanes has wound down, and an increase in revenues from a modest improvement in value-added-tax (VAT) receipts. Domestic energy costs rose during this period, reflecting an increase in global oil prices. Liquidity levels expanded as short-term financing of the government increased, but external reserve levels contracted from the seasonal demand for foreign currency and public sector debt repayments obligations.

The FY2018/2019 Budget Communication was approved in the final week of June. The budget include several key revenue and expenditure measures. For revenue, the government of increased the VAT from 7.5 to 12 percent while removing it from several breadbasket items, imposed a progressive tax on gaming house profits and instituted a tax on gaming house patrons, eliminated import duties on several retail and capital goods, and raised the custom exemption. Expenditures were curtailed by way of introduction of a Fiscal Responsibility Bill, the proposed establishment of an independent Fiscal Responsibility Council, a 10 percent reduction in discretionary expenditure across all government ministries, and establishment of a Disaster Relief Fund and a $13.5 million digital government initiative.

The rate of unemployment remained flat at 10 percent as of May 2018, down only slighly from 10.1 percent in November 2017, as the size of the labour force increased at a rate similar to the rate of job creation. Unemployment in the most populated island (New Providence) declined by 60 basis points to 10 percent, while in Grand Bahama the rate increased to 12.4 percent from 12.1 percent. Youth unemployment levels remained at concerning levels of 24.1 percent as of May 2018, up by 2 percentage points, and the number of discouraged workers increased by 6.9 percent.

The Central Bank of The Bahamas proposed revisions to the legislative framework for resolving problem banks. The proposed amendments will, once enacted, establish the central bank as the resolution authority for problem banks and streamline the role and powers of the Deposit Insurance Corporation.

Barbados

The Barbados Labour Party (BLP) won the 24 May 2018 election. The BLP won all 30 parliamentary seats in an historic election, making Ms. Mia Amor Mottley the first female prime minister. Shortly after, the new administration announced its plan to address high public debt levels and the country's fragile external position. The government halted payments to external commercial creditors in June 2018. It has since requested balance of payment support from the International Monetary Fund (IMF) and announced further fiscal adjustment measures in the FY2018/2019 budget. The new measures aim to increase the primary fiscal surplus to 6 percent of GDP.

The economy contracted by 0.6 of a percent in the first semester of 2018, compared to 1.5 percent growth over the same period of 2017. Tourism value-added fell by 2.3 percent in the first six months of 2018. Although tourist arrivals increased 3.4 percent from the first semester of 2017, this was not enough to offset the shorter average length of stay. The inflation rate continued to rise and stood at 4.9 percent as of the end of June 2018, compared to 3.5 percent a year earlier. A pick-up in international oil prices and the pass-through effect of revenue increases are among the factors responsible for the increasing prices.

The government's fiscal position has improved, yet remains a concern. The fiscal deficit narrowed to 4.3 percent of GDP in FY2017/2018 as a result of higher revenues and lower expenditures. Revenue collection was boosted by higher excise taxes, value-added taxes, and corporate taxes, and by National Social Responsibility Levy collections. Expenditures decreased to 32.8 percent of GDP in FY2017/2018 as a result of a moderate decrease in non-interest expenditure (reaching 25.2 percent of GDP) and lower capital expenditure (falling to 1.7 percent of GDP). Gross public sector debt remains high, at an estimated 155 percent of GDP as of the end of June 2018.

International reserves remain low. Reserves were 7.2 weeks (US$221.6 million) as of the end of June 2018. This is slightly above the 6.7 weeks at the close of 2017 and is a result of the halt of payments to international creditors in June 2018. High foreign debt servicing obligations and weak private sector capital flows remain among the main causes of the fall in international reserves.

The Central Bank of Barbados is expecting economic growth to remain at -0.5 of a percent in 2018. Further fiscal consolidation measures are expected to have dampening effects on economic growth. Going forward, the tourism and construction sectors will be the drivers of growth, and further investments in these sectors, within a low inflationary environment, will be key.

Guyana

Growth has become more broad-based. In the first half of 2018, the Guyanese economy grew in real terms at 4.5 percent, higher than the 2.5 percent recorded over the same period in 2017, on account of positive growth in the agriculture, fishing and forestry (3.4 percent) and services (8.2 percent) sectors. Despite the contractions in the usually dominant sub-sectors of rice (3.8 percent) and gold (9.1 percent), growth was driven by the livestock (29.1 percent), bauxite (33.1 percent), and construction (13.4 percent) sub-sectors, reflecting more broad-based growth. During this, period inflation remained stable at a moderate 1.3 percent. The Ministry of Finance revised the 2018 growth projection to 3.7 percent.

The central government balance was reduced to a surplus of $3.1 billion in the first half of 2018, compared to $8.3 billion in the same period in 2017, on account of increased levels of expenditure and a reduction of grants. Revenues totaled $109.2 billion as of the end of June 2018, 12.7 percent above the same period in 2017, owing to the tax amnesty and increased collections from all tax categories.

International reserves remain above prudent levels. At of the end of June 2018, gross international reserves stood at US$473.4 million, equivalent to 3.1 months of import cover.

The overall balance of payments deteriorated, with the country recording a deficit of US$139.8 million in the first half of 2018, compared to a deficit of US$46 million during the same period in 2017. The current account deteriorated from a deficit of US$79.2 million to a deficit of US$194.1 million. Despite a deteriorating current account, the capital account improved to US$71.8 million in the first half of 2018, compared to US$16.8 million over the same period in 2017.

The banking sector remains well capitalized, with a capital adequacy ratio of 29.54 percent. By March 2018, the ratio stood at 13.22 percent, compared to 12.79 percent in 2017. The ratio of gross loans to gross deposits stood at 57.84 percent as of March 2018. Private sector credit grew by 4.1 percent over the first half of 2018.

Jamaica

Policies and reforms have stabilized the Jamaican economy and restored sustainability. Progress with debt reduction, fiscal consolidation, and the accumulation of external buffers has met or exceeded commitments under the current IMF arrangement, despite slow progress on wage compression and public sector transformation. Looking forward, efforts to reinforce financial and economic management institutions—for example, the shift to inflation-targeting and the recently announced establishment of a fiscal council—should help to ensure that hard-won gains are sustained once the country graduates from the current IMF adjustment programme in 2019.

Growth is accelerating, but from a low base, and inflation is undershooting the target. Favourable weather conditions have driven a rebound in agricultural output, while external demand remains strong, supporting tourism and trade, and improving credit conditions have begun to spur domestic investment. Consequently, real GDP is projected to grow by 1.7 percent during the year ending in March 2019—up from 0.9 of a percent for FY2017/2018. Inflation was below the central bank's target range of 4 to 6 percent through the first half of 2018, driven by limited pass-through of higher import prices, the rebound in agricultural output, and weak domestic demand, despite the lowest level of unemployment in recent history (9.7 percent).

The exchange rate is depreciating in an orderly fashion, while credit conditions are improving. The central bank's easing of the policy rate over the past year to 2 percent —the lowest rate on record—coincides with the normalization of interest rates in the United States. Together, these factors have contributed to a roughly 7 percent depreciation of the Jamaican dollar against the U.S. dollar since the end of August 2017. These lower interest rates and limited government domestic financing are driving strong domestic credit growth of over 13 percent, supporting a deepening of local capital markets. Data suggest that large corporates are driving this growth, while banks thus far remain somewhat reluctant to reduce rates for small and medium-size enterprises.

Jamaica's public debt levels fell at a faster-than-expected pace over the past year, owing to fiscal prudence and lower financing costs. The public-debt-to-GDP ratio fell to 104 percent as of the end of March 2018, from over 140 percent in 2013. While this level of indebtedness remains high by international standards, the pace of debt reduction has been impressive, and current estimates suggest that if the authorities maintain their commitment to prudent policies, the country should achieve the Fiscal Responsibility Law's target of debt lower than 100 percent of GDP by the end of March 2019, a year ahead of schedule.

Suriname

Economic growth is expected to return to Suriname in 2018. The IMF estimated almost zero growth for 2017, an improvement from an average decline of -3.9 percent over 2015–2016. The IMF also projects real GDP growth of 1.4 percent in 2018.

Inflation continues to decline. The inflation rate fell to 8.6 percent in March 2018 from 9.2 percent at the end of 2017. The fall in headline inflation was largely due to sub-categories such as housing and utilities. Previously, inflation spiked to 79.2 percent in October 2016 because of higher costs for utilities and a depreciation of the exchange rate. The exchange rate has stabilized at roughly US$1/SRD7.51 since December 2016.

Fiscal deficits continue to be an area of concern. The primary fiscal deficit for 2017 was estimated at 4.2 percent of GDP, lower than the 7.4 percent of GDP reported in 2016. The overall fiscal deficit was estimated at 6.9 percent of GDP in 2017, falling from 8.9 percent of GDP in 2016.

The state oil company, Staatsolie, obtained a US$625 million syndicated loan from the international market in June 2018. Staatsolie used part of the loan proceeds to repay a loan of US$261.5 million to the government in 2016, and to purchase of the government's share in the Newmont gold mine valued at US$76 million. The government indicated that it will use the US$337.5 million it received to reduce more expensive foreign and domestic debt and to deal with recurring payments such as salaries, subsidies, debt service payments, and payment of minor remaining domestic arrears.

External debt is estimated at US$1,717 million. Suriname's total public debt as at May 2018 was estimated at 73.5 percent of 2017 GDP. External debt as a percentage of GDP was estimated at 51.3 percent of GDP and domestic debt was 22.2 percent of GDP.

Suriname recorded a smaller current account deficit in 2017. Estimates from the Central Bank of Suriname show that the current account deficit was US$1.8 million (equivalent to 0.05 percent of GDP) as of the end of 2017. This smaller current account deficit—the 2016 deficit was 3.7 percent—was due mainly to a positive goods trade balance, as exports increased by 41 percent compared to 2016.

International reserves increased to US$533.4 million in June 2018, equivalent to roughly three months of import cover. This marks an increase from the US$444.6 million in international reserves in January 2018.

Finally, the authorities increased public sector wages by 25 percent in August 2018. In addition, the minimum hourly wage was increased by 37 percent in July 2018.

Trinidad and Tobago

Trinidad and Tobago is slowly recovering from a deep economic recession. A sharp decline in energy prices and lower domestic production of oil and natural gas caused the economy to contract by 6.1 percent in 2016 and by 2.6 percent in 2017. Recently, however, the country has seen a turnaround in the energy sector on the back of new fields (e.g., bpTT's Juniper) and improved pumping technologies recently adopted in mature fields (e.g., bpTT's onshore compression project). This is expected to lead to positive economic growth. The IMF projects the economy of Trinidad and Tobago to grow by 1 percent in 2018. Growth in the non-energy sector, however, is expected to remain negative for the third consecutive year.

The government is continuing its programme of fiscal consolidation. Facing significant energy revenue shortfalls, the government of Trinidad and Tobago adopted adjustment measures in the past two fiscal years. Some key changes include tax reforms in the energy and non-energy sectors, a reduction in fuel subsidies, and the establishment of a procurement board and revenue authority. Aided by favourable conditions in the energy sector and reforms in corporate taxation, total revenue increased in the first quarter of FY2018 while expenditures fell, leading to a slight primary surplus. The mid-year review of the budget projects the overall fiscal deficit for FY2018 at 2.5 percent of GDP. Trinidad and Tobago's public-debt-to-GDP ratio decreased from 62.7 percent of GDP in September 2017 to 59.6 percent of GDP in March 2018.

Foreign reserves have continued to fall. Net official reserves declined by 11 percent (year-over-year) as of the end of July 2018. The country's net official reserves stood at US$7.7 billion or 8.5 months of import cover. Sizable investments by energy companies, tax reforms, and favourable production and price conditions in the oil and gas sector may slow the decline in foreign reserves. The increased supply of hard currency may also ease the tightness in the foreign exchange market. Anecdotal evidence suggests that local firms are facing fewer difficulties in sourcing foreign exchange to service debts with foreign suppliers.

Inflation remains subdued. Headline inflation, measured using the retail price index, was 0.9 of a percent (year-over-year) in June 2018 versus 1.5 percent in June 2017. Food prices, which increased by 1.4 percent between June 2017 and June 2018, are one of the main drivers of headline inflation. Core inflation was only 0.8 of a percent (year-over-year) and substantially below the 1.7 percent level a year earlier.

Organisation of Eastern Caribbean States Countries

Moderate real GDP growth is projected for the countries of the Organisation of Eastern Caribbean States (OECS) in 2018. Following economic growth averaging 0.7 of a percent in 2017, the Eastern Caribbean Central Bank (ECCB) projects a marginal improvement to 1.1 percent in 2018. With the exception of Dominica, economic growth in the OECS is expected to range from 1.2 percent in St. Vincent and the Grenadines to 3.9 percent in Antigua and Barbuda. This outturn is underpinned by expected robust performances in the tourism and construction sectors as well as by positive global developments in the OECS's main trading partners (United States, United Kingdom, and Canada). Growth in Dominica over the medium term could be boosted by reconstruction activity.

The region witnessed an improved tourism performance during the first three months of 2018. Total visitor arrivals to the OECS increased by 9.9 percent, with the cruise passenger segment driving this increase with growth of 10.7 percent. Moreover, total visitor expenditure grew by 22 percent to reach US$625 million. In particular, total visitor arrivals grew by around 18 percent in Antigua and Barbuda and in St. Kitts and Nevis, while Grenada witnessed an increase of 24 percent. At the same time, boosted by higher cruise ship calls, the number of cruise passenger arrivals almost doubled in St. Vincent and the Grenadines. On the other hand, tourism performance continues to be weak in Dominica following the adverse impact of the 2017 hurricane season, as the number of long-stay visitors fell by 36 percent.

Access to credit remains a challenge in the OECS. Throughout the OECS region, credit to the private sector declined by 0.6 of a percent during the first three months of 2018. However, there was some heterogeneity across the region, with an expansion of credit in Grenada (0.5 of a percent) and St. Kitts and Nevis (0.2 of a percent). On the other hand, all the other countries experienced a contraction in private sector credit ranging from -0.6 of a percent in Dominica to -1.2 percent in St. Lucia. Notably, since 2010 Antigua and Barbuda and St. Lucia have seen contractions in credit to the private sector of 26 and 17 percent, respectively, while in Grenada credit to the private sector fell by 11 percent.

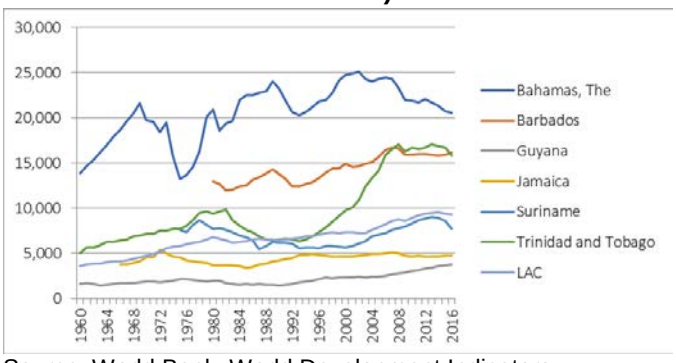
With the exception of St. Kitts and Nevis, consumer prices increased as of the end of March 2018. There were increases in the inflation rate ranging from 0.1 of a percent in Grenada to 0.5 of a percent in Antigua and Barbuda. Most of the rise in inflation was a consequence of higher prices for a number of food items and for gas and fuels. On the other hand, the inflation rate declined by 0.8 of a percent in St. Kitts and Nevis.

Contributors: Juan Pedro Schmid and Moises Schwartz

Introduction

The Caribbean is a diverse region. Countries differ in terms of languages and dialects, customs, foods, religions, and other traditions that can be traced to the diversity of the region's people, history, migration, culture, and geography. In terms of economic structure, an evident distinction is that three of the countries examined in the Quarterly Bulletins – Guyana, Suriname, and Trinidad and Tobago – rely on commodities. More than 50 percent of their exports are concentrated in their main two commodities. These countries tend to experience volatile swings in economic conditions caused by movements in world commodity prices. By contrast, the other three Caribbean countries examined here (The Bahamas, Barbados, and Jamaica) and the member countries of the Organisation of Eastern Caribbean States rely on services, with an emphasis on tourism.

Figure 1. GDP Per Capita (in constant 2010 U.S. dollars)

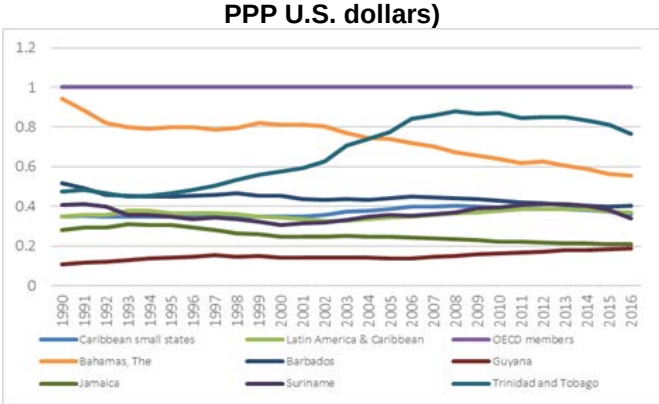


Source: World Bank, World Development Indicators.
Note: LAC: Latin America and the Caribbean.

Growth performance in the Caribbean has been disappointing. Although income levels differ across the six countries examined here, common features include relatively low economic growth during the last decade, especially for the tourism-dependent countries. As a result, income levels at constant prices have remained somewhat flat over time. As Figure 1 shows, GDP per capita levels in constant U.S. dollars in The Bahamas and Barbados are the highest in the region. However, those countries' GDP per capita levels were already higher in the 1960s than the 2017 levels for Guyana, Jamaica, and Suriname. Trinidad and Tobago is an exception, as the country experienced an acceleration in per capita GDP on the back of oil price booms in the mid-1970s and the late 1990s (with GDP per capita jumping from US$6,400 in 1993 to a peak of US$17,000 in 2013). Guyana remains the poorest country in the group even though it has been catching up from low levels (from US$1,470 GDP per capita in 1990 to US$3,800 in 2017). Jamaica's GDP per capita has also been at the lower end, and at constant prices is basically the same today as it was in 1970 (US$4,800 in 2016 compared to an average of US$4,500 in the 1970s).

The Caribbean seems to be losing out. The region in general has not been catching up with more advanced countries. For instance, Caribbean countries examined here are stagnating or falling behind compared to the member countries of the Organisation for Economic Co-operation and Development, as shown in Figure 2, which considers price differences between countries. The exception is Trinidad and Tobago, which saw improvements until 2008 but has since fallen back. In addition, although still low in comparison with OECD levels, Guyana's per capita GDP at purchasing power parity (PPP) advanced from around 10 percent of the OECD level in 1990 to 20 percent in 2016. The Bahamas, which had a per capita income level on par with the OECD in the 1990s, has seen its income per capita relative to the OECD average decline to around 60 percent. Performance in the other countries has been mostly flat, catching up in some years but reversing in others.

Figure 2. Per Capita GDP Relative to the OECD (in PPP U.S. dollars)



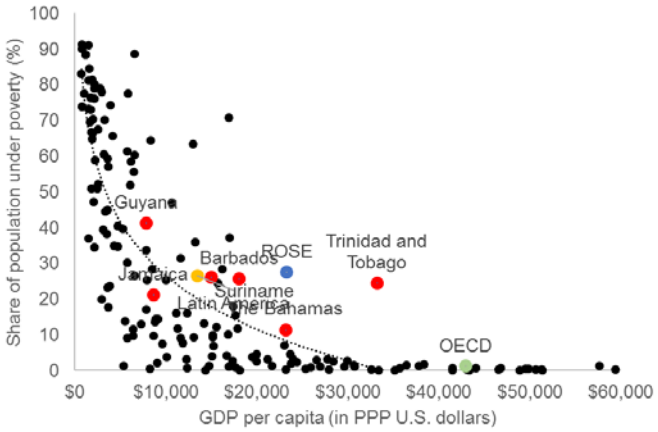
Source: World Bank, World Development Indicators.
Note: OECD: Organisation for Economic Co-operation and Development; PPP: purchasing power parity.

Poverty remains a challenge. Even though average income in the Caribbean is relatively high, deprivation remains a challenge. In addition, considering the average level of income, poverty is high in several Caribbean countries (i.e., their poverty levels lie significantly above the dotted regression line in Figure 3). The gap is largest in Trinidad and Tobago, with the highest GDP per capita in PPP in the Caribbean, but with a poverty rate (24.5 percent) well above what is observed among countries with similar GDP per capita. Barbados, Suriname, and Guyana also have elevated levels of poverty relative to their GDP per capita. Poverty rates stand at 25.7 percent

for Barbados, 26.10 percent for Suriname, and 41.2 percent for Guyana.

Common challenges for development include weak fiscal institutions, crime and violence, a sluggish private sector, weak productive development policies, skill-biased emigration, and other structural impediments. Taken together, these factors have resulted in a complex and challenging environment for promoting sustainable growth and development in the Caribbean. The situation is made more difficult by recurrent natural disasters, which are projected to increase in frequency in the future. This portion of the Quarterly Bulletin provides a regional overview of these issues, while the country summaries explores individual constraints to development in more depth.

Figure 3. Poverty versus GDP Per Capita



Source: Authors' calculations based on individual household surveys and the World Bank's 2016 World Development Indicators database.
Note: OECD: Organisation for Economic Co-operation and Development; PPP: purcahsing power parity; ROSE: rest of the small economies of the world.

Constraints to Growth and Development

Several studies have explored the reason for the Caribbean's weak growth performance. Chamon et al. (2017) provide an overview of conditions that have limited Caribbean growth, such as the debt burden, crime, migration, natural disasters, and business environments. Ruprah, Melgarejo, and Sierra (2014) explore whether the relatively small size of Caribbean countries explains their underperformance. They find that size does not account for the documented underperformance and suggest that growth is held back by rent-seeking and state capture of private elites. Sutton and Ruprah (2017) focus on crime and violence, estimating an average welfare cost of crime in the Caribbean of about 3 percent of GDP.

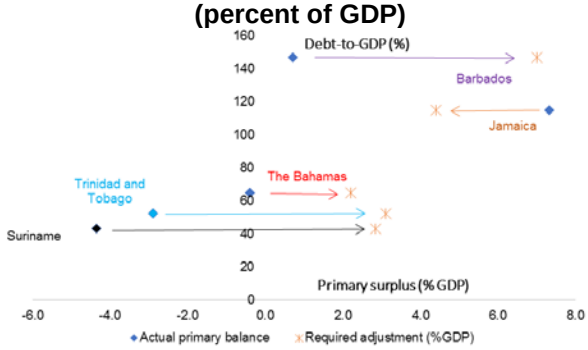
Common structural issues hamper growth and development. In general, challenges can be grouped into three areas: the public sector, the business environment, and social sectors/human development.

Public Sector

Weak public service delivery at high cost burdens the Caribbean. An obvious challenge resulting from the small size of the Caribbean countries is the lack of economies of scale for the public sector. As a result, public sector wages and salaries usually take up a large share of public expenditures. At the same time, capacity in terms of the qualifications and specialized skills that are available in the public sector is often insufficient, and public service delivery weak. Service delivery is also influenced by red tape as a result of a paper-based culture, regulatory complexity, insufficient coordination among ministries, and lack of digitalization and use of information technology solutions.

Fiscal challenges are central in the Caribbean. Debt-to-GDP ratios in CCB countries are high relative to comparable countries, especially for the tourism-dependent economies. The situation has become especially challenging in Barbados, which just started a fiscal adjustment programme and is announced to enter a programme supported by the International Monetary Fund (IMF). At the same time, Jamaica continues its fiscal consolidation efforts to further reduce its debt-to-GDP ratio. The debt-to-GDP ratio in The Bahamas had been increasing, but fiscal adjustment measures seem to have stabilized the level of debt. The challenge for the commodity-dependent countries is the volatility and resulting vulnerability from commodity price swings. Presently, at current levels most CCB countries have to adjust their fiscal balances even to just stabilize their debt-to-GDP ratios.

Figure 4. Actual and Required Fiscal Balance, 2018 (percent of GDP)



Source: Authors' calculations based on WEO.

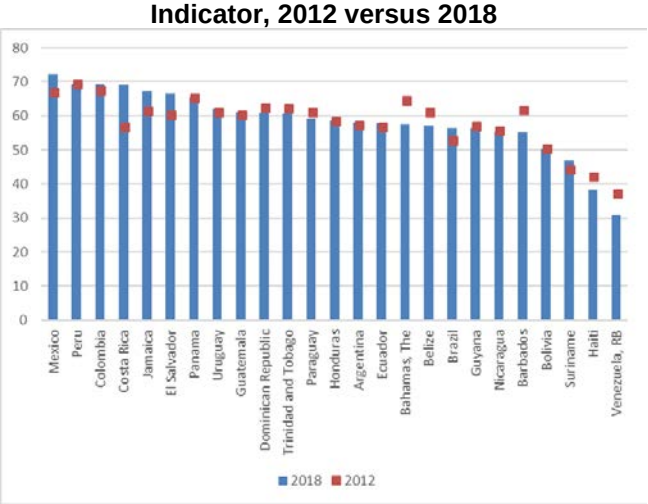
Structural fiscal imbalances have been persistent. In highlighting the fiscal and debt challenges in the Caribbean, Yartey and Turner-Jones (2014) document

that structural fiscal problems resulted in a sizable accumulation of debt in the late 1990s and early 2000s, exacerbated by the 2008 global financial crisis. Thus, Caribbean economies face high debt-to-GDP ratios, interest payments that take up a large share of revenues, and exposure to rollover risks that can feed fiscal crises. In addition, despite recent advances, fiscal institutions in the region remain weak and are not appropriate for the challenge the countries face in terms of potential for shocks, volatility, and vulnerability.

Business Environment

The small size of the countries, weak institutional frameworks, and high energy prices all constrain private sector development. Ruprah and Sierra (2016) and Khadan (2017) study the private sector and show that firms in the Caribbean underperform their peers in other regions across several dimensions, including investment, sales growth, innovative capacity, and productivity. Both studies conclude that the main constraint is a policy environment that fails to promote a dynamic and innovative private sector. They identify several areas with weak policies, including customs and trading, access to finance, crime, and the lack of a skilled workforce because of skill-biased emigration. Indeed, 71 percent of the tertiary-educated labour force in Caribbean countries has migrated to member countries of the OECD, while remittances do not compensate for the public resources invested in education and the lost productivity due to emigration (Ruprah, Melgarejo, and Sierra 2014).

Figure 5. Distance to Frontier, Doing Business Indicator, 2012 versus 2018



Source: World Bank, 2018 Doing Business Report.

The business environment is generally not conducive to growth and development. In the Caribbean, Jamaica is the best-ranked country in the World Bank's Doing Business Report at 70th, followed by Trinidad and Tobago at 102nd. Suriname is the lowest-ranked at 165th (out of 190). Jamaica, and to a lesser degree Suriname, are the only Caribbean countries examined here that have improved their business climate as measured by the distance to frontier (Figure 5).[1]

Caribbean exports are concentrated both in terms of products and markets. Most of the tourists visiting the Caribbean are from the United States, followed by Canada and the United Kingdom. These countries are also the main export markets for other exports and remittances. In the case of commodity producers, they depend on world commodity prices, which have proven to be volatile. This concentration brings risks and volatility in addition to restricting possibilities for faster economic growth.

Access to finance is a challenge for smaller firms. While financial sectors in the region have enough liquidity, conditions for accessing financing can be prohibitive. Between one-quarter and one-third of firms identify access to finance as a major or severe obstacle.[2] Similarly, collateral requirements can be prohibitive, ranging from 60 percent of the loan amount in Guyana to over 180 percent in Barbados (Compete Caribbean 2015).

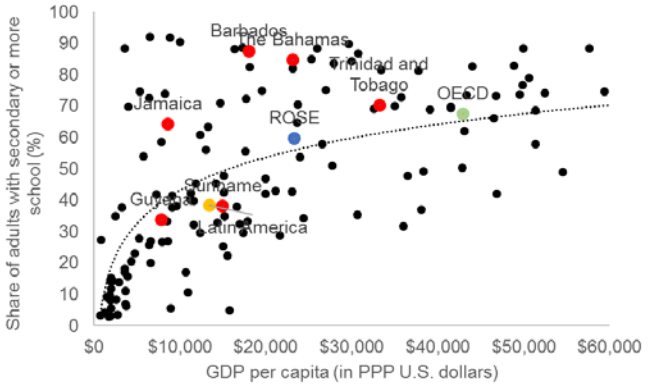
Social Development

The region has undergone a transition where coverage of social services has made important strides, but quality is lagging. Caribbean governments have invested in education and health with important results. For instance, in education, school attendance is near universal at the primary school level, although it decreases for higher school levels. In addition, there are differences in terms of learning achievements, achievements between socio-economic groups, and achievements between boys and girls (with girls performing better in education than boys). Nevertheless, indicators for education are mostly on par or above those for comparable countries.

Basic health indicators have improved. Infant mortality and life expectancy are mostly in line with Latin America (Table 1) and the level of income in the CCB countries (Figure 7). However, commodity-dependent countries fare worse, especially Trinidad and Tobago, which has weak indicators considering its high level of income.

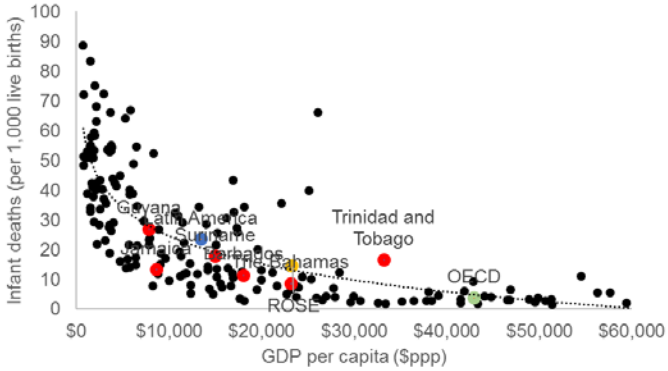
[1] Because of methodological changes, 2012 and 2018 are not strictly comparable. However, the data indicate that there were no important improvements.
[2] Trinidad and Tobago is an exception with 14 percent.

Figure 6. Educational Attainment versus GDP Per Capita



Source: Authors' calculations based on individual household surveys and the World Bank's 2016 World Development Indicators database.
Note: OECD: Organisation for Economic Co-operation and Development; PPP: purchasing power parity; ROSE: rest of the small economies of the world.

Figure 7. Infant Mortality versus GDP Per Capita



Source: Authors' calculations based on the World Bank's 2016 World Development Indicators database.
Note: OECD: Organisation for Economic Co-operation and Development; PPP: purchasing power parity; ROSE: rest of the small economies of the world.

Table 1. Health Outcomes and Health Supply

Country Name	Infant Mortality Rate (per 1,000 live births)	Life Expectancy at Birth (years)	Physicians per 1,000 population
OECD	5.93	80.12	2.86
The Bahamas	8.60	75.68	2.26
Barbados	11.40	75.91	1.81
Jamaica	13.20	75.97	0.47
ROSE	13.32	75.44	1.67
Trinidad and Tobago	16.50	70.67	1.82
Suriname	17.80	71.41	0.82
Latin America	23.04	70.93	1.25
Guyana	26.90	66.65	0.21

Source: Authors' calculations based on the World Bank's 2016 World Development Indicators database.

Note: OECD: Organisation for Economic Co-operation and Development; ROSE: rest of the small economies of the world.

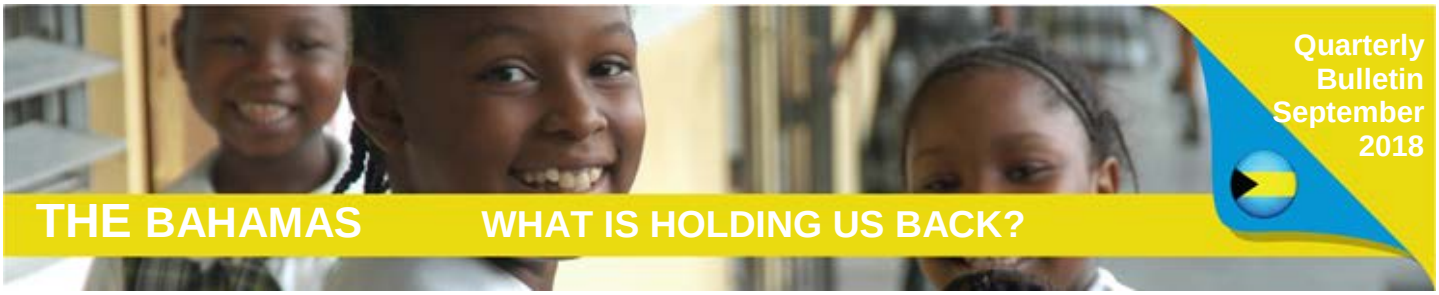
The transition to increased non-communicable diseases is a strain for the region. While the incidence of communicable diseases has decreased, the incidence of non-communicable diseases has increased, putting an important burden on health systems.

Conclusions and Policy Discussion

The Caribbean has underperformed other regions in terms of growth and development. The three tourism-dependent countries have the weakest growth performance among all IDB borrowing member countries since 1980 except for Haiti and Venezuela. At the same time, economic performance in the commodity-dependent countries has been volatile, with small buffers smoothing between booms and busts.

The weak economic performance is related to common development challenges. While each country faces idiosyncratic challenges, common constraints to growth and development emerge. For example, all countries are small, and all countries face climate risks from their geographic location in the Caribbean. But there are other similarities as well, such as issues involving competitiveness, the ease of doing business, and institutional development, all of which are usually below levels in comparator countries.

Policy suggestions are often similar. For instance, fiscal prudence and strengthening of fiscal institutions is central in all countries. Most countries would also benefit from institutional strengthening, a better business climate, and more competitive environments. This regional analysis has only provided a small overview of these and other challenges facing the region. More detailed analysis and policy recommendations can be found in the individual country summaries.



THE BAHAMAS WHAT IS HOLDING US BACK?

Contributor: Allan Wright

Overview

The economy of The Bahamas, an archipelagic nation with over 700 island and cays, depends on the principal sectors of tourism and financial services. The population of The Bahamas is estimated at 368,000, with a per capita income of approximately US$28,600, among the highest in Latin America and the Caribbean. Since the global financial crisis, the nation has experienced low growth rates and mounting levels of debt. The main reasons have been identified as subdued contributions from the tourism[1] and financial sectors, along with low levels of total factor productivity.[2] The country has been facing growing competitive challenges from within the Caribbean region in terms of international tourist arrivals since 2006, while stricter international regulatory standards have led to increases in operational costs within the financial sector, the economy's next-largest engine of growth.

Recent Economic and Social Trends

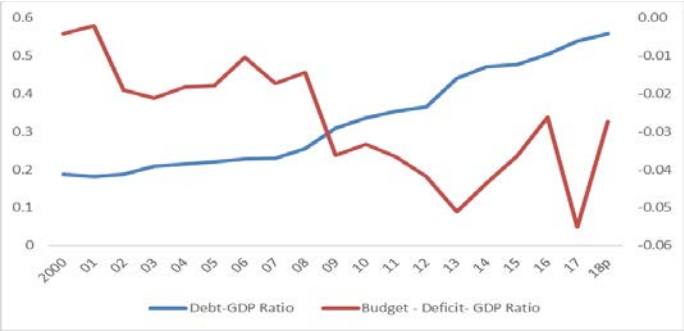
Growth in The Bahamas has been low, averaging 0.3 of a percent over the past decade, and lags Caribbean comparators. Real GDP is projected to grow by 2.5 percent in 2018 and 2.2 percent in 2019 following improvements in 2017. Stronger levels of growth are expected in the near term as a result of continued robust economic conditions in the United States and growth in foreign direct investment from the opening of the final phase of the Baha Mar luxury hotel[3] and other projects. Employment was boosted by the Baha Mar project, as some 4,000 jobs were created up to the first quarter of 2018.

Central government debt as a percentage of gross domestic product (GDP) rose from just above 30 percent after the global financial crisis to approximately 55 percent in FY2017/2018, and the central government fiscal deficit tightened as deficit levels moved up to 5.5 percent of GDP in FY2016/2017.[4] Staffing excesses and other inefficiencies of state-owned enterprises have placed an undue burden on government coffers and are estimated at some 5 percent of overall GDP. In addition, post-hurricane rebuilding and clean-up activities after several Category 5 storms impacted revenue collections and spending levels**.** A planned 10 percent reduction in expenditures, using a combination of approaches such as programme rationalization and new revenue-generating measures, were presented by the Deputy Prime Minister and Minister of Finance in the recent House of Assembly budget presentation. Those measures are designed to lead to a balancing of the country's 2018/2019 budget and achieving fiscal targets outlined in the new Fiscal Responsibility Legislation 2018 Bill.[5]

Highlights

- *Pursuing a pro-growth path for the medium term will be a challenge, especially in an environment of tight fiscal space and lower levels of external competitiveness.*
- *Disaster risks and climate change events present significant challenges.*
- *The authorities have recognized the need to adjust and reform, including measures to increase tax revenues and reduce expenditures.*

Figure 1. Central Government Debt and Deficit (percent)



Source: Central Bank of The Bahamas Reports.

External competitiveness has declined due to the appreciation of the U.S. dollar, with which The Bahamas maintains a peg. Liquidity and external reserves levels

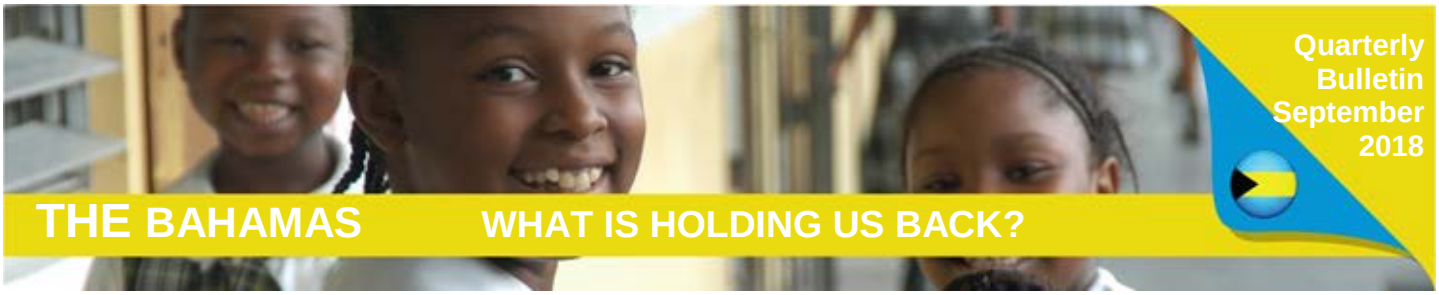
[1] According to the 2015 World Travel and Tourism Council report, The Bahamas is the 10th most tourism-dependent economy in the world. Tourism accounts directly and indirectly for 43.6 percent of GDP, 51.6 percent of total employment, and 61.5 percent of total exports. However, the country has been losing market share (-0.5 percent) in the Caribbean region in terms of international tourist arrivals since 2006.

[2] In the growth equation, technological innovation, or total factor productivity (TFP), is a contributory component, and its increase is attributed to the enhanced utilization of production inputs with the existing stock of quality capital and labor. By the application of a worldly usage of product, process, and organizational innovation, the quality, timeliness, and accessibility of public sector governance can be enhanced for the population and for the many sectors that are served by the government. The Bahamas has a TFP change of approximately 1 percent against a list of leading Caribbean economies, where deteriorating potential growth has been influenced by weak TFP growth.

[3] The Rosewood Hotel opened June 2018, while the SLS resort became operational in November 2017.

[4] The central government fiscal deficit is estimated to have reached 2.7 percent of GDP for FY2017/2018.

[5] The reduction of central government debt to 50 percent from its current level and targeting a fiscal deficit of 0.5 of a percent by FY2020/2021 were the main objectives of the legislation. The transitional periods of 2018/2019 and 2019/2020 will see targeted fiscal deficits of 1.8 and 1 percent, respectively.



have been boosted by proceeds from the government's recent bond issue.

The Bahamas' value of 0.778 on the United Nations Development Programme's Human Development Index is above the regional average for Latin America and the Caribbean (0.75) and within the high human development category. However, low growth rates over the past decade are contributing to troubling trends in social indicators. Poverty rates, though lower than regional comparators, increased during the measured period (2001–2013) from 9.3 to 12.4 percent.[6] There also appears to be regional and demographic disparities, with poverty rates in the southern-most Family Islands at 17.2 percent, almost 5 percent above the national average. For young adults and children, estimates are roughly 6 percent above the archipelago's average (18.4 percent), and female-headed households show a higher poverty rate than male-headed households (9.7 percent versus 7.9 percent).

Medium-Term Economic and Social Outlook

Pursuing a pro-growth path for the medium term will be a challenge, especially in an environment of tight fiscal space and lower levels of external competitiveness. Growth in The Bahamas for 2018, which is expected to be 2.5 percent, would be a significant improvement over previous periods, with continued improvement of 2.2 percent expected in 2019. Growth is expected to be boosted in the near to medium term as a result of the opening of the Baha Mar luxury resort and construction activity related to the US$4.2 billion project, other foreign direct investment, the contribution of tourism as measured through air arrivals (which grew by 15 percent as at May 2018), rebuilding activities following Hurricanes Matthew and Irma, and continued robust economic returns in the United States.

The government has embarked on efforts to rationalize public expenditure through a 10 percent reduction in government spending in FY2017/2018 and improved tax collection efforts. The first 11 months of FY2017/2018 have shown a decline in the deficit, driven by higher levels of collection and stabilization of expenditure after recent hurricane rebuilding expenditure. The planned introduction of fiscal responsibility legislation, in addition to current cost-cutting measures, raises hopes that the currently high levels of the budget deficit and debt burden will be gradually reduced, bringing greater credibility to the level of fiscal governance throughout the country.

Risk Factors

Current pension liabilities appear to pose a serious long-term challenge. Liabilities for government pensions, which include coverage for public entities and social security commitments, are roughly 160 percent of GDP, and some agencies, including the International Monetary Fund, indicate those commitments are currently underfunded. There appears a strong need for a contributory scheme to ease the burden that will soon be exacerbated as the retirement population grows to 41.6 per 100 workers by 2060.

Low elevation throughout The Bahamas, along with weak environmental planning, make the economy susceptible to disaster risk and climate change. Hurricanes Joaquin, Matthew, and Irma all negatively affected the archipelago in the past three years, with estimated rebuilding costs of almost US$750 million. Disaster risks and climate change events present significant challenges to the preservation of human life and to maintaining and improving economic activity while achieving fiscal and debt targets. In a tourism-based economy, climate adaptation measures can serve to reduce the vulnerability of tourism support systems such as water management, transportation, food supply, and energy, while also preserving natural attractions that are critical for the tourism industry**.**

Development Constraints

The Bahamas' developmental and growth challenges are centred on low investment and entrepreneurship driven by low returns to economic activity and high financing costs. The country is impacted by low social returns and appropriability due to a large and inefficient government sector and a private sector weakened by an inadequately trained workforce, operating within a vast geographic expanse of islands and cays with weakened infrastructure. The archipelago does have access to international finance, albeit with a weaker sovereign credit rating. Historically, however, the high cost of financing, along with elevated unemployment rates (especially among youth), have further weakened domestic consumption and demand.

Underlying low appropriability is the problem of a limited reach within the public sector. The public sector struggles to provide adequate services across the archipelagic islands, especially the southern-most Family Islands.[7] Air and maritime connectivity is particularly challenging, as are water services and sanitation. Tightening fiscal space has made this challenge even more pronounced, as growing levels of recurrent spending and transfers to state-owned enterprises have weakened

[6] Data provided by the 2013 Household Expenditure Survey.

[7] See Vision 2040, the National Development Plan for The Bahamas, available at http://www.vision2040bahamas.org/.

the government coffers of needed resources and impacted the medium–term fiscal programme targets (IMF 2016). Improvements in the efficiency of the public sector will come from better management of fiscal resources, strengthening of state institutions by revamping fiscal processes and public procurement, the use of competitive procurement methods, and the monitoring of contracts. Better governance will require better use of evidence-based policymaking through via improved data generation and dissemination (Kaufmann et al. 2005).

Low appropriability in the private sector has been impacted by an inadequately trained labour force and other market and coordination failures. In addition, the private sector faces challenges in the form of high energy costs and frequent power outages, financing access and rising costs, and low research and development expenditure (Vision 2040; World Bank 2016). Limited infrastructure quality (air and maritime connectivity), poor public services (road network and transportation services), weak protection of minority investors and property rights, rising crime and violence, and low levels of coordination between the government and the private sector to develop industries that encourage diversification and sophistication have all diminished the country's ability to mitigate its dependence on exogenous factors and improve factor productivity. The Bahamas needs to develop a framework and programmes that encourage economic incentives for diversification and intra-linkages, as well as the respective institutional capacity to implement them. Policy interventions that aid private sector growth by improving the business environment, would go a long way towards placing The Bahamas on a higher growth trajectory (Vision 2040).

Low social returns are impacting economic activity due to deficiencies in human capital (health, education, and citizen security). Despite significant per capita spending levels in education and health, The Bahamas continues to struggle with high levels of students of both genders who leave school without diplomas or certifications. Development indicators for nursing and midwifery, infant mortality, and available beds are at concerning levels, as what scarce resources are available have to cover a vast territory (World Bank 2015). Increasing murder and rape rates in recent years have meant that The Bahamas now has among the highest levels of these crimes in the Western Hemisphere (IDB 2015).

Cross-cutting public, private, and social capital are the issues of gender, environmental risk, and climate change. With rising education failure rates, especially among males, there is the indication of a beginning of a structural deficiency within the labour market. An environment and climate change study by the IDB (2016a) shows that the archipelago is susceptible to rising sea levels and storm events, including storm surges, which have damaged the country's infrastructure quality and connectivity services in past years. The low elevation of the islands and cays, with many economic and social services close to the coastline, creates a challenging issue for urban planners and policymakers. In 2016, Hurricane Matthew brought significant damage to the northern and central parts of The Bahamas (New Providence, Berry Islands, North Andros. and Grand Bahama) The damage was approximately four times greater than that incurred from Hurricane Joaquin, which impacted the southern islands the previous year (IDB 2016b).

Conclusion

The Bahamas faces important challenges. Economic growth has remained subdued since the 2008 global financial crisis. A strong dependence on tourism and on specific tourism markets, as well as vulnerability to weather-related shocks and from being a small country spread over dozens of islands, all constrain economic growth. At the same time, the debt-to-GDP ratio has been increasing, bringing fiscal challenges and a need to adjust in the short to medium term. The authorities have recognized the need to adjust and reform, including through measures to increase tax revenues and reduce expenditures. The successful implementation of public financial management reforms and adherence to the targets of the Fiscal Responsibility Legislation 2018 Bill in the near and medium terms will help reduce the wage bill, achieve greater efficiency of state-owned enterprises, and boost capital spending on key infrastructural projects, placing the economy on a sustainable path. Work is needed on reforming the public servants pension system and restricting any further escalation of the contingent liabilities of state-owned enterprises.

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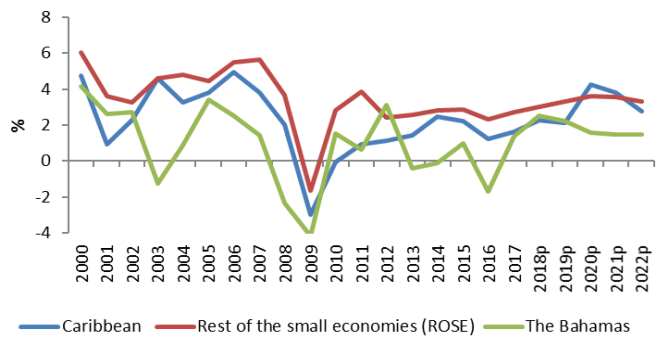
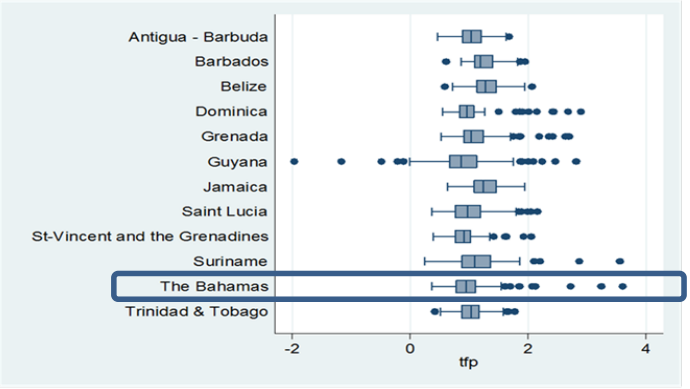
The Bahamas high per capita, but low growth rates since GFC

Figure a: Real GDP Growth (Percent)



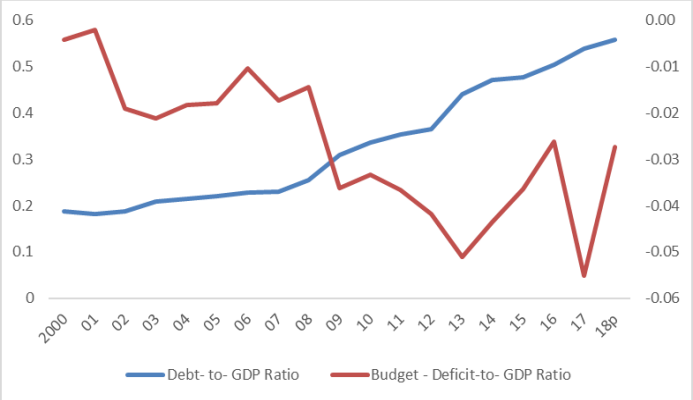
Low total factor producticity is contributing to low growth rates

Figure b: Total Factor Productivity



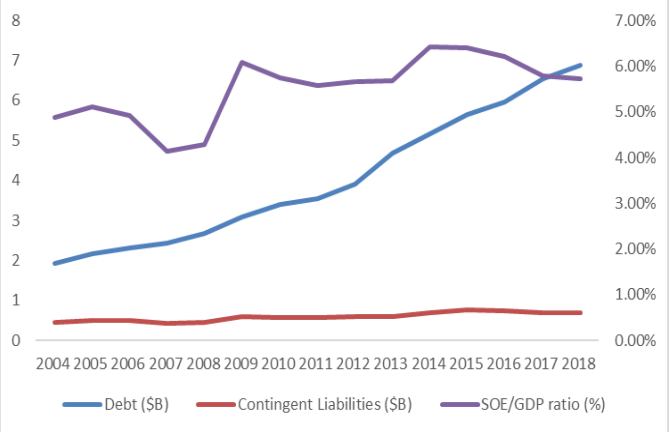
Fiscal Space is tightening

Figure c: Fiscal Space (Percent)



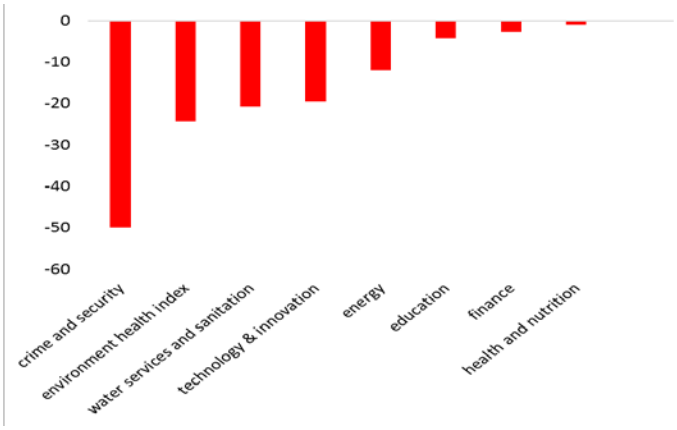
Excessive burden on fiscal position from State Owned Enterprises

Figure d: State Owned Enterprises



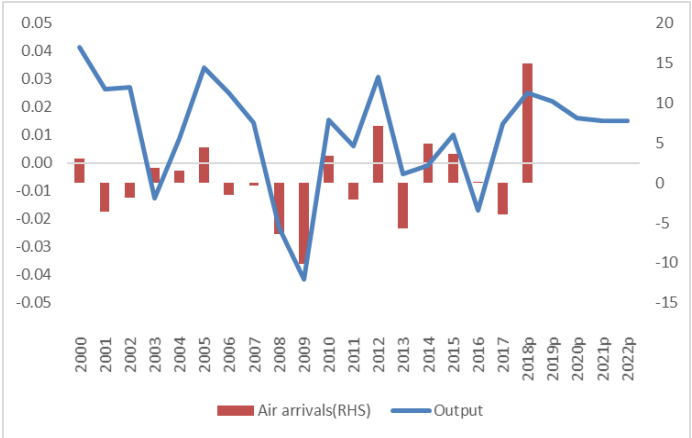
….. development gaps

Figure e:



… while tourist arrivals are recovering

Figure f: Air Arrivals and Real GDP Output (Percent)



Contributors: Laura Giles Álvarez, Juan Pedro Schmid, and Kimberly Waithe

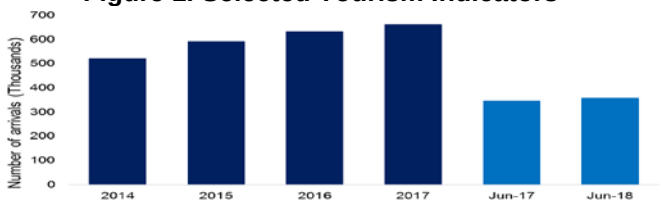
Overview

Barbados is a high-income country that has made significant social achievements but currently faces macroeconomic and fiscal challenges. With an estimated population of 280,000 and GNI per capita of US$17,830 in 2017, Barbados is classified as a high-income country. Historically, Barbados has invested in social development, as reflected in high health and education indicators. However, macroeconomic and fiscal challenges include the fact that Barbados has the highest debt level in the region at 155 percent of GDP as of the end of June 2018, as well as low levels of international reserves.

Recent Economic and Social Trends

Economic growth in Barbados has been modest in recent years. The country's real growth rate has been weak, averaging 0.3 percent since 2010. Growth temporarily increased to 2.5 percent in 2016 but fell back to only 0.1 percent in 2017.[1] During the first half of 2018, GDP growth was estimated at -0.6 percent of GDP due to weaker demand from fiscal consolidation measures, weaker performance in the construction sector, and falling tourism demand. An increasing number of tourist arrivals has not been enough to overcome declining trends in visitors' length of stay, resulting in the sector's falling value added (Figure 1).

Figure 1. Selected Tourism Indicators



	2014	2015	2016	2017	Jun-17	Jun-18
Number of arrivals (thousands)	520	592	632	661	345	357
Average length of stay (days)	5.5	5.1	4.9	4.7	4.7	NA

Source: Central Bank of Barbados.

The government's fiscal position remains a concern. The financing gap has narrowed because of fiscal consolidation efforts, yet this has been insufficient to curb debt levels. Revenues have been rising in recent years, reaching 28.5 percent of GDP at the end of FY2017/2018, while expenditures have been only slightly reduced, reaching 32.8 percent of GDP at the end of FY2017/2018 (25.2 percent of GDP for primary expenditures, which exclude interest payments). Growing revenues have been led by higher excise taxes, value-added taxes, corporate taxes, and National Social Responsibility Levy collections. Current expenditures have been stable over the past two years as a result of falling levels of spending on salaries and wages and on goods and services, counteracted by rising transfers and subsidies and interest payments. Capital expenditures reached 1.7 percent of GDP in FY2017/2018, lower than the 2.3 percent of GDP recorded in FY2016/2017. Because of these trends, in FY2017/2018 the fiscal balance narrowed to -4.3 percent of GDP and the primary fiscal balance increased to 3.3 percent of GDP.

Highlights

- *Barbados has experienced modest average growth since 2010 and persistent fiscal deficits; resulting in high debt-to-GDP ratios and low levels of international reserves.*
- *There are inherent structural weaknesses in the economy, including low levels of diversification and competitiveness, as well as a weak business climate.*
- *In contrast, Barbados performs well on social and institutional development indicators.*
- *Going forward, fiscal consolidation will be the focus for economic policy in the short term, while addressing structural constraints to unlock potential sources of growth will be key in the medium and long terms.*

Gross public sector debt grew to reach 155 percent of GDP as of the end of June 2018. This was higher than the 148.6 percent of GDP recorded at the close of 2017. International reserves reached 7.2 weeks of import cover (US$221.6 million) as of the end of June 2018. This is slightly above the 6.7 weeks of import cover recorded at the close of 2017, partly resulting from the suspensions of payments to international creditors since June 2018. This has led to more international credit rating downgrades, with Standards & Poor's further downgrading Barbados's global bonds due in 2019 and 2022 from CC to D (default) in August 2018. At the same time, higher tax collections and growing global oil prices contributed to increasing inflation rates, which reached 4.9 percent as of the end of April 2018 (compared to 4.5 and 1.5 percent at the close of 2017 and 2016, respectively).

The current account deficit has narrowed. Barbados has a historical current account deficit, largely resulting from its dependence on fuel and food imports. The current account balance has been declining in recent years – from -9.2 percent of GDP in 2014 to -3.8 percent in 2017. This

[1] As of June 2018, the methodology to calculate GDP has been updated and rebased to 2010 prices. The numbers presented in this bulletin are therefore based on provisional estimates presented in the Central Bank of Barbados' Quarterly Economic Review, January-June 2018.

trend has continued in 2018, and as the end of June 2018, the current account balance reached -1.7 percent of GDP. Behind the trend were lower external interest payments, following the halt on payments to external creditors, and a reduction in imports during the first half of the year. Going forward, projected increases in the price of fuel will likely counteract these trends.

Living standards and governance indicators in Barbados are high. Barbados performs strongly on governance and institutional indicators, ranking in the top 80th percentile on most of the World Bank's World Governance Indicators. These results are comparable to OECD countries. Regarding social sectors, Barbados is classified within the high human development category, ranking 54th out of 188 countries on the United Nations Development Programme's 2015 Human Development Index. Life expectancy and mean years of schooling stood at 75.8 years and 10.5 years, respectively, in 2015. Barbados has high levels of expenditure on public education and health, spending an average 6 percent of GDP and 4.5 percent of GDP, respectively, between 2010 and 2014. The latest Barbados Survey of Living Conditions 2016–2017 shows that income inequality and extreme poverty levels have improved since 2010. The Gini index fell from 0.43 to 0.32 and extreme poverty decreased from 6.8 to 3.4 percent between 2010 and 2016. However overall poverty increased, as household poverty rates increased from 15.1 to 17.2 percent during the same period.

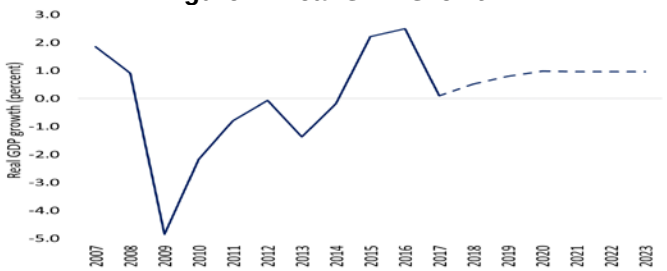
Medium-Term Economic and Social Outlook

The Central Bank of Barbados and the International Monetary Fund (IMF) forecast an economic growth rate ranging between -0.5 and 1 percent in 2018 and remaining under 2 percent in the medium-term (Figure 2). Improved macroeconomic performance is key for growth prospects in the future. The economy will remain vulnerable to changes in the price of international commodities. The prospects of increasing oil prices will likely have a negative effect on growth and contribute to rising inflation, which is expected to continue increasing in 2018. Given the public sector's macroeconomic and fiscal challenges, the private sector will have to play a bigger role to support economic growth going forward.

Risk Factors

Several factors can affect Barbados' medium-term outlook. These include the government's macroeconomic and fiscal challenges; limited access to new financing, particularly since the suspension of payments to international creditors and the recent downgrades in June and August 2018 by Standard & Poor's; higher-than-expected U.S. and domestic interest rates; the uncertainty surrounding Brexit, which can have implications for goods and tourism demand, as the United Kingdom is one of the country's key trading partners; and the incidence of natural disasters, which remains a cause of concern for medium-term economic prospects.

Figure 2. Real GDP Growth



Sources: Central Bank of Barbados; and International Monetary Fund, April2017 *World Economic Outlook.*

Development Constraints

Fiscal consolidation will likely have a negative impact on the economy. On 11 June 2018, the newly elected government presented the "mini budget," which aims at rising the primary fiscal balance to 6 percent of GDP in the next fiscal year through revenue and expenditure measures. Further reforms will also be announced and implemented over the next three years. The government has also requested balance of payments support from the IMF and is expected to commence official negotiations for an IMF programme in the next few months. This programme will most likely include both fiscal adjustment and debt restructuring measures. The scope to collect further revenues will be limited, given the already high revenue collection rates. On the expenditure side, salaries and wages and transfers will likely be the focus, particularly transfers to state-owned enterprises (SOEs).

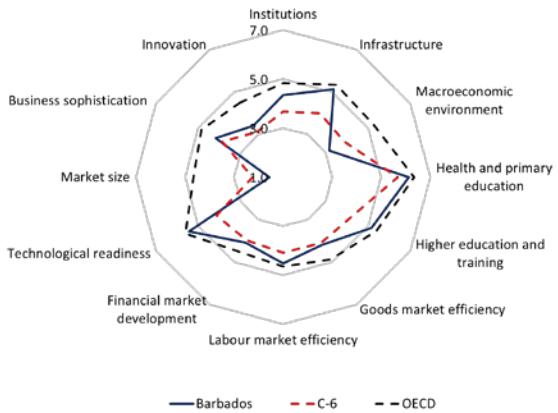
Reductions in expenditures could have negative effects on social sectors, particularly through adjustments in subsidies and transfers. The University of the West Indies and Queen Elizabeth Hospital, which are two of the greatest beneficiaries of these transfers, will be particularly vulnerable to expenditure cuts. The stock of capital will also likely be adversely affected, resulting in lower levels of investment and operation and maintenance spending. This could be particularly damaging for the tourism industry, which relies heavily on high-quality infrastructure and will be an important source of growth going forward. Other key sectors for growth that could potentially be affected by inadequate levels of infrastructure are energy, transport and connectivity, and water and sanitation.

Structural challenges that hinder growth will also have to be addressed. A development gap analysis for Barbados, following Borensztein et al. (2014), reveals negative gaps in private sector and financial as well as environmental indicators, given the country's income level. Contrastingly, Barbados scores highly on social and institutional development indicators. Based on these results, inherent structural weaknesses to the economy include:

- **A weak business environment.** An inadequate labour supply, onerous red tape, and the high tax burden are reported to be key constraints to private sector operations. Barbados ranked 132nd out of 190 countries in the 2018 World Bank's Doing Business Report.
- **High dependence on imports and low levels of diversification.** Barbados relies heavily on the tourism and financial services sectors, which accounted for approximately 50 percent of GDP in 2017, without considering tourism's indirect weight on other economic sectors. The country also presents a historical negative trade balance, depending heavily on imports of goods, particularly food and oil. This makes it vulnerable to fluctuations in external markets, particularly tourism, finance, and oil.
- **Low competitiveness.** Barbados ranked 72nd out of 138 countries on the World Economic Forum's 2016–2017 Global Competitiveness Index (Figure 3). The country's small market size, rigid labour laws, fiscal imbalances, and high trade tariffs were identified as key structural constraints to its competitiveness. If they remain unaddressed, they could negatively affect key sectors such as the financial and tourism sectors, which are key for growth going forward.
- **Climate change and natural hazards:** Being a small island state in the Caribbean, Barbados is inherently vulnerable to climate change and natural disasters, particularly given that more than half of the country's GDP is generated in areas at risk of natural hazards. The country also records high level of CO2 emissions and carbon intensity trends.

To enhance growth going forward, the government should prioritize measures that will support the country's competitiveness and business environment. A key short-term measure will be to set and commit to a structural reform programme that tackles fiscal imbalances and rising debt levels, and that boosts investor confidence. In the medium and longer terms, further structural measures could include promoting diversification in energy sources to reduce dependency in oil imports; fostering labour market flexibility and a supply of workforce skills that meets labour market demands; addressing the cost and time of government processes to reduce excessive red tape, particularly by reducing inefficiencies in state-owned enterprises; reforming legal processes; and promoting greater use of technologies to make public sector processes leaner. Finally, further investment is needed in climate change mitigation and adaptation strategies. Investing in resilient construction, comprehensive risk assessments, and early warning systems are possible adaptation steps that could be taken, whereas mitigation measures should revolve around lowering greenhouse gas emissions.

Figure 3. Global Competitiveness Index Scores by Pillar, 2016–2017



Source: World Bank, Global Competitiveness Report.
Note: The scale ranges from 0 to 7, with 0 being the worst and 7 being the best.

Conclusion

Short-term stabilization in Barbados must be followed by structural reforms. In the short run, external and fiscal imbalances are the key constraints to growth and development. In addition, the country should protect its social achievements. For the medium to long term, reforms that unlock the country's growth potential are key. Maintaining adequate infrastructure, reducing red tape, and improving the environment to invest and do business will also be critical. This will be important both throughout the fiscal consolidation process and to foster greater competitiveness, private sector development, and thus long-term growth.

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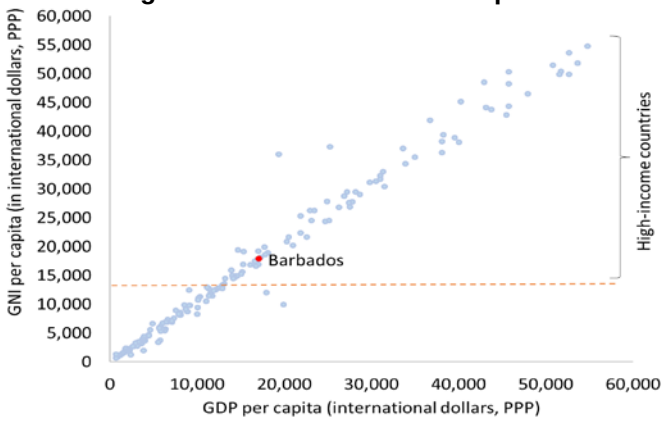
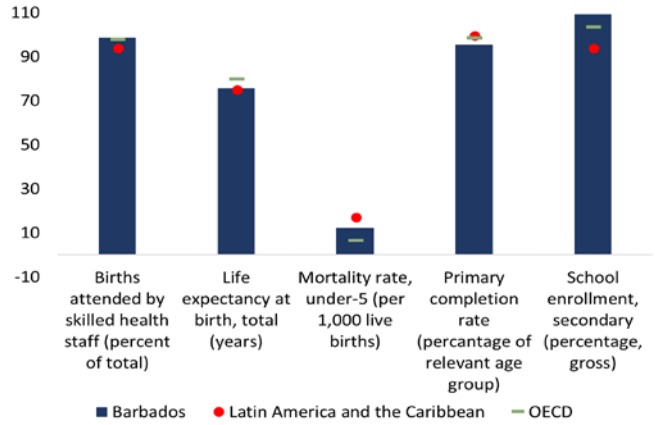
Barbados is a high-income country…

Figure a. GNI and GDP Per Capita



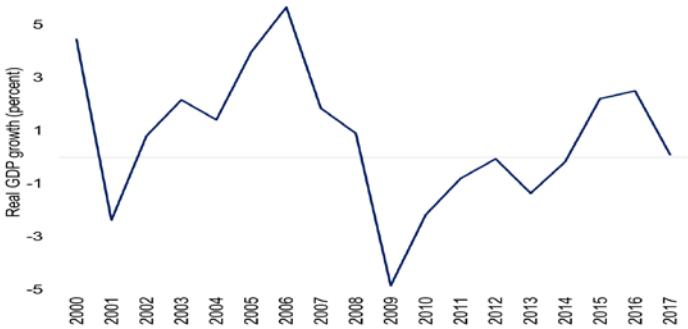
…with high scorings on social indicators

Figure b. Key Social Indicators



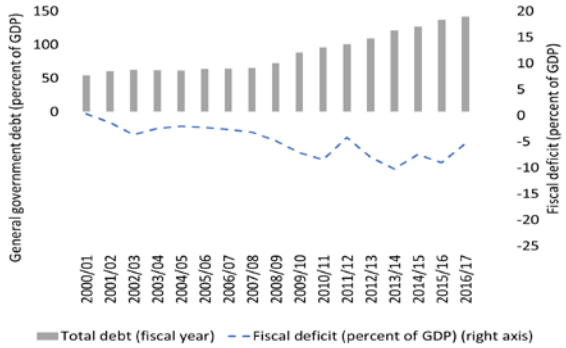
However, average real economic growth has been weak since 2010…

Figure c. Real GDP Growth



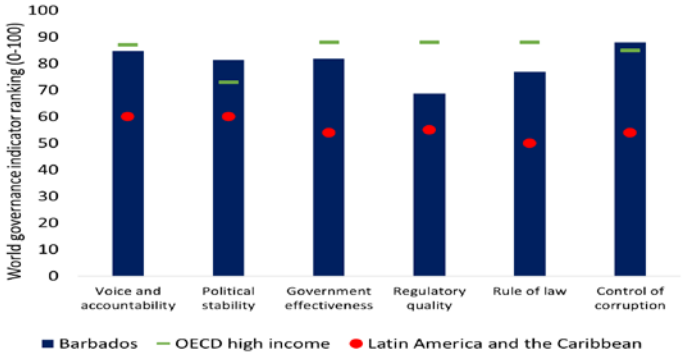
…coupled with recurring fiscal deficits and rising debt levels.[1]

Figure d. General Government Debt and Fiscal Deficit



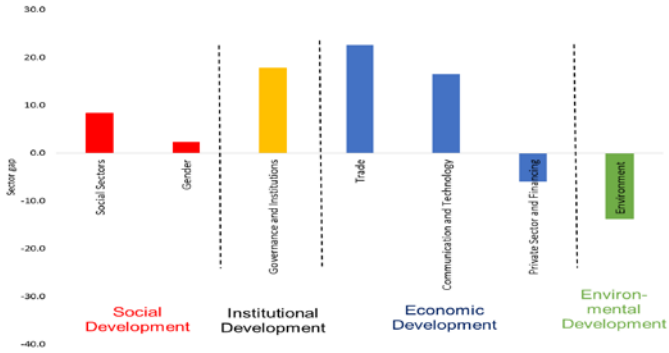
Together with high social achievements, Barbados has good governance indicators…

Figure e. World Governance Indicator Rankings



…yet development gaps prevail for private sector, financing and environmental sectors.[2]

Figure f. Sector Gaps



[1] Debt figures in this figure are taken from a harmonized series for general government debt, based on the Central Bank's First Quarter Quarterly Economic Review.
[2] The development gap is defined as the distance between the observed and the expected value of a given output indicator. In this case, it measures the distance between the output indicator for Barbados and the fitted value resulting from a linear (or quadratic) fit from a cross-country regression of such indicator on GDP per capita.
Sources: International Monetary Fund WEO, World Bank, Central Bank of Barbados and IDB.2018. Country Development Challenges for Barbados.

Contributors: Victor Gauto and Elton Bollers

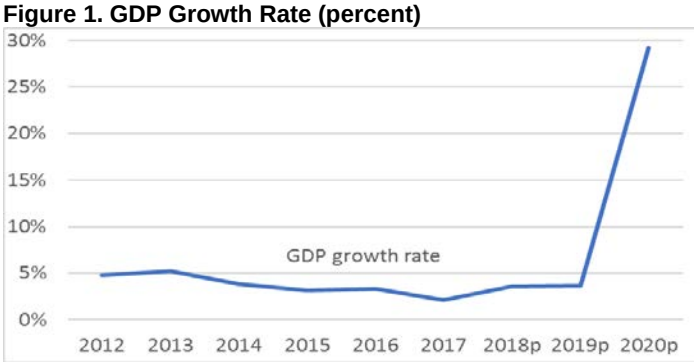
Overview

Guyana is a small coastal economy that is rich in minerals such as gold and, more recently, oil. Guyana has a population of 780,000, making it the sixth most populated country in the Caribbean. However, Guyana's GDP per capita of US$4,700 is one of the lowest in the Caribbean at 14th out of 15 countries in the region. GDP is expected to grow significantly in the medium term, as Guyana is currently transitioning into becoming an oil-producing country beginning in 2020.[1] Recoverable oil resources are currently estimated at 4 billion barrels of oil-equivalent.

Recent Economic and Social Trends

Guyana's macroeconomic situation over the last few years has been stable. The country's GDP growth averaged 3.65 percent over the last five years (Figure 1), fourth highest in the region, and the inflation rate has remained low, averaging 0.8 of a percent during the same period. International reserves remain stable at approximately 16 percent of GDP and are enough to cover 3.3 months of imports, above the three-month import cover benchmark. After more than four years, the official exchange rate increased from G$206.5/US$1 to G$208.5/US$1 in April 2018. The average fiscal balance between 2013 and 2017 was -3.7 percent, leading to relatively manageable levels of public debt on the order of 46.1 percent of GDP. The prospect of commercial oil production starting in 2020 is expected to generate significant revenues for the government, which would contribute to reducing public debt levels.

Figure 1. GDP Growth Rate (percent)



Source: International Monetary Fund, April 2018 *World* Economic Outlook.

Social trends remain mixed. Current data on poverty are not available for Guyana, but existing indicators suggest that the country underperforms its peers. According to the Guyana Labour Force Survey (2003/2017), the labour force participation rate is 68.8 percent for men and 43.6 percent for women, even though the population of working-age women is slightly higher than men. The unemployment rate of 12 percent is above the average of 8.2 percent for Latin American and Caribbean (LAC) countries. Life expectancy at birth was 66.6 years in Guyana in 2016, one of the lowest among peer countries and below the LAC average of 75.5. Guyana ranks eighth out of 14 countries in undernourishment, with 8.5 percent of the population undernourished, slightly higher than the LAC average of 6.5 percent. Rates of immunization coverage are higher than average in Guyana, reaching 97 percent of the population for some of the main vaccines (BCG, DPT1).

Highlights

- *Strengthening institutional capacity and human capital formation are among Guyana's major development priorities.*
- *Guyana's oil reserves are estimated at 4 billion barrels of oil-equivalent.*
- *The government has released its Sovereign Wealth Fund proposal.*

Maternal and infant mortality rates lag regional averages. Maternal deaths per 100,000 live births in 2015 were estimated at 229, which is higher than the LAC average of 68 and higher than the world average of 216, according to UNICEF. The infant mortality rate is 26.9 per 1,000 live births, compared to the average of 14.8 for LAC countries. Contributing to poor health indicators is inefficient public investment in healthcare, resulting in understaffing and outdated equipment, affecting the quality of service rendered. Government health expenditure as a share of GDP is estimated at 4.1 percent in 2018.

Evidence suggests that the quality of human capital is not sufficient to assure sustainable growth. School enrolment rates are close to the LAC average, with 91.5 percent of primary-school-aged children attending school, compared to the LAC rate of 94 percent. However, the secondary school enrolment rate is higher in Guyana (83 percent) than the LAC average (73 percent). Even though enrolment at the primary and secondary level is high, the quality of schooling varies. Student performance on the Caribbean Examination Councils Examination is below the Caribbean average. To compound the issue of human capital formation, Guyana has the world's seventh-highest rate of emigration, and most of the emigrants tend to be skilled and/or university-educated persons.[2]

[1] See IMF (2018). Real GDP growth is projected to be 29.8 percent in 2020.

[2] The United Nations Development Programme's 2009 Human Development Report estimated Guyana's tertiary-educated emigration rate at 78.6 percent.

Medium-Term Economic and Social Outlook

The medium-term outlook looks bright given that oil production is expected to begin in 2020. The economy is expected to grow at an average of 16.6 percent between 2018 and 2023 (IMF 2018). At the same time, government revenues are projected to increase by an average of 15.6 percent over the same period, with oil revenues representing approximately 25 percent of total government revenues. In 2028, government oil revenues are expected to exceed US$3 billion, in an economy with a current GDP of US$3.6 billion. This represents a significant structural transformation in which oil production is expected to represent more than 40 percent of GDP at the height of production (IMF 2018).

The government has made strides in strengthening the institutional and regulatory framework of the oil sector in order to establish efficient governance of the resources for the economic and social transformation of Guyana. The recently created Energy Department within the Ministry of the Presidency will be tasked with oil and gas oversight. The Petroleum Commission Bill, which has been drafted and is currently being reviewed, is scheduled for passage in 2018. This commission will be tasked with regulating the petroleum sector. The Ministry of Business has published the second draft of the Local Content Policy and is soliciting comments and suggestions prior to finalization.[3] The government recently presented its Green Paper on the Sovereign Wealth Fund in Parliament, which would set the rules for balancing and channelling oil-related revenues into budget stabilization, infrastructure development, and intergenerational savings.

These prospects make it necessary to formulate a sustainable development plan. The focus should be on improving productive capacity, continuing structural reforms leading to improved efficiency and competitiveness, diversifying the base of the economy, and protecting the environment. The plan should identify the development projects that oil-related revenues could fund in terms of infrastructure, human capital, and technology. The announced vision of the standing government is to pursue a "greening of the economy" primarily through the Green State Development Strategy, which frames the country's development vision for the next 15 years.

Risk Factors

Real GDP growth is expected to be in the 3 to 5 percent range through 2019 based on an economy transitioning into oil production, but it hinges on commodity prices and the absence of major external shocks. Guyana faces climate risks such as increased sea level rise, more irregular rainfall patterns, and greater frequency and severity of floods and droughts. These risks pose a substantial threat to the agriculture sector and livelihoods on the coastal plain. Adaptation to climate change remains insufficient, and the continued rise in average temperatures is likely to further increase the country's vulnerability. Although the government is taking steps to prepare for initial oil production, the process is gradual, and it exposes the economy to missing opportunities at the onset of that production. The political culture is polarized, which makes it difficult to craft bipartisan solutions, build consensus, and undertake structural reforms to strengthen and diversify the economy.

Development Constraints

Guyana's development and growth challenges centre on limitations in infrastructure, institutional, and human capital development, all of which contribute to low levels of investment. Gross fixed capital formation in Guyana was estimated at 17 percent of GDP in 2017, below the LAC average of 19 percent.[4] Lack of access to international capital markets and low returns on investment are influenced by low levels of productivity due to developing public sector services and infrastructure.

There is the need to strengthen the public sector. The public sector is large but faces challenges in providing public services. The effectiveness and efficiency of public spending may be compromised by structural and management inadequacies. Among the challenges for the public sector are strengthening its fiscal and public financial management capabilities, which will be required to manage the implications of oil production expected for 2020. Inadequate governance, combined with human capital and financial constraints, results in moderate to low public sector institutional effectiveness. The 2016 World Governance Indicators rank Guyana in the 42nd percentile for government effectiveness and in the 37th percentile for regulatory quality.

The quality of infrastructure could be improved. Better electricity generation and distribution is critical to sustained growth and economic diversification. Improving transport links between the coastal areas and the interior and between the country and the rest of the world will be key to sustaining growth. The investment climate for the private sector needs to be strengthened, since the government leads the economy in gross fixed capital formation. Public gross fixed capital formation is 8.6 percent of GDP,

[3] Source: Ministry of Business. Available at: http://www.business.gov.gy/wp-content/uploads/2018/05/Second-Draft-Local-Content-Policy-Framework.pdf.

[4] The data are based on the IMF's April 2018 World Economic Outlook database.

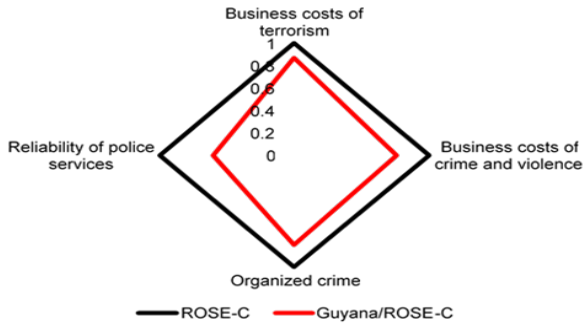
compared to the LAC average of 4.5 percent, while private gross fixed formation is 8 percent of GDP, compared to the LAC average of 16 percent. Both public and private sector monies should be leveraged to address infrastructure bottlenecks. Considering that oil revenue will compound the resources available for infrastructure development, strengthening investment management capacity will be required to translate these additional resources into greater and equitable economic growth.

Interventions to improve health sector outcomes would significantly contribute to improving human development. There are important challenges in access to healthcare, particularly in rural areas in the interior. The country's health profile is characterized by a double burden of disease: non-communicable diseases are increasing, and communicable diseases remain a challenge. Cases of malaria have dropped from 40 per 1,000 population in 2013 to 17 per 1,000 in 2016, according to WHO/UNICEF. Malaria remains endemic in the interior regions of the country, traditionally affecting mostly the north-western area and mining communities. Additionally, there continues to be a shortage of nurses and physicians in the public healthcare system. Given the country's epidemiological profile, health posts and health centres should be the gate of entry of the population into the health system. This would require upgrading and expansion of physical infrastructure and the equipment of facilities. In addition, recruitment and retention of trained workers has been a challenge. A shortage of skilled labour and infrastructure, coupled with limited accessibility, present considerable challenges to the development of adequate social services.

Crime and insecurity are detrimental to Guyana's social capital and social cohesion but seem to have improved through 2016. The homicide rate per 100,000 population was 19 in 2015, which is below the LAC average of 22 per 100,000. Trust in the police improved from a low of 35.5 percent in 2014 to 54.1 percent in 2016. However, the police force remains the least trusted institution in Guyana, according to the 2016 Latin American Public Opinion Project (LAPOP 2016). Police responsiveness, measured by the expected wait time after the police are called, made limited progress between 2014 and 2016 (LAPOP 2016).

Guyana ranks lower than the average for the rest of the world's commodity-dependent small economies with respect to the business cost of crime and terrorism (Figure 2). The operational capacity of both the Guyana Police Force and the justice system is limited by understaffing and tense relations with the community. Interpersonal trust is also low, and it is driven largely by crime and insecurity. The highest levels of trust are found in Region 2 and the hinterland, with the lowest levels in the most populated area (Region 4) (LAPOP 2016).

Figure 2. Crime and Security



Source: World Bank, Global Competitiveness Index (2015).
Note: Rose-C: rest of the small economics of the world that are commodity-dependent.

Conclusion

With the recent discovery of oil and mounting estimates of recoverable oil reserves, the medium-term economic outlook for Guyana is positive. The government's challenge will be to translate new potential resources into higher levels of human capital and infrastructure. Over the last decade the country has sustained consecutive years of positive real economic growth associated with the commodity super-cycle, but human development has lagged. Improved economic policies and stronger institutions are necessary to address the negative development gaps,[5] attract more private sector investment, create more employment opportunities, and attain higher living standards.

References

Borensztein E., S.J. Miller, G. Sánchez, and P. Valenzuela. 2014. Development Diagnostics for the Southern Cone. IDB Working Paper No. 85194. Inter-American Development Bank, Washington, DC.

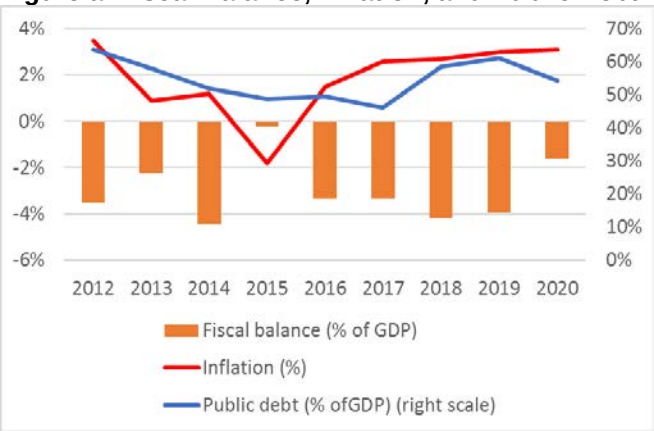
International Monetary Fund (IMF). 2018. 2018 Article IV Consultation. IMF Staff Report No. 18/220. Washington, DC.

Vanderbilt University. 2016. Americas Barometer. Latin American Public Opinion Project (LAPOP).

[5] A development gap is defined as the distance between the obtained and expected value of a development indicator for a country (Borensztein 2014). The expected value of an indicator is a linear/quadratic fit from a regression of the indicator on GDP per capita. A gap analysis was carried out using 39 indicators grouped into seven categories.

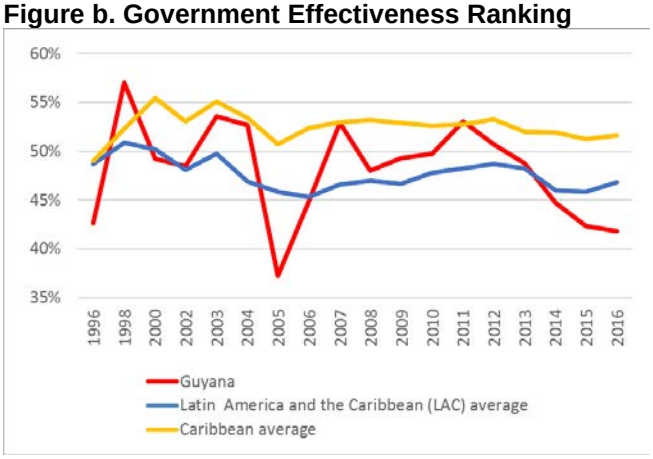
Although macroeconomic indicators remain stable…

Figure a. Fiscal Balance, Inflation, and Public Debt



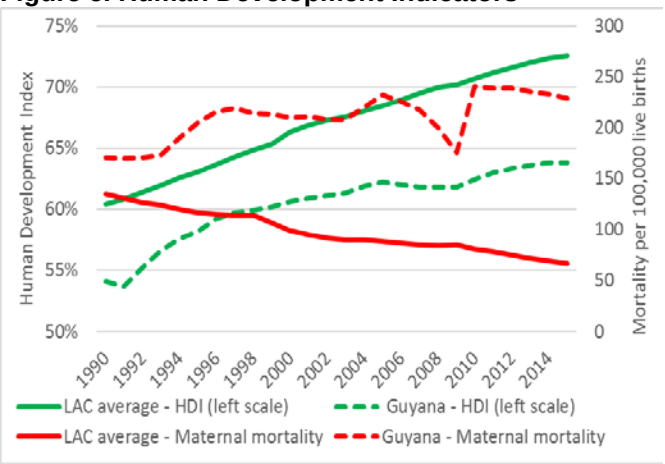
…the perception of government effectiveness declined.

Figure b. Government Effectiveness Ranking



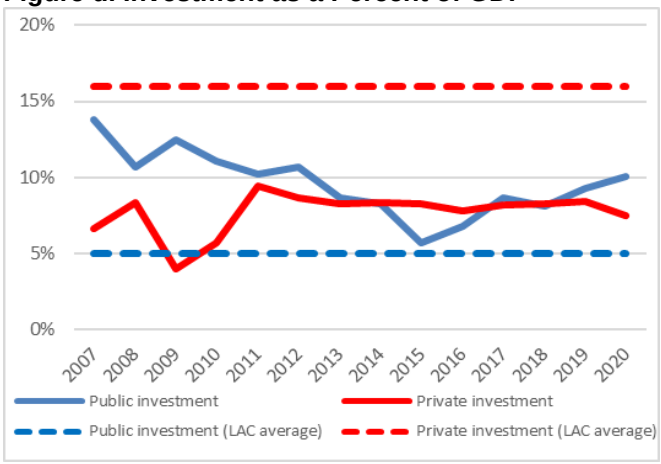
Challenges include lagging human development…

Figure c. Human Development Indicators



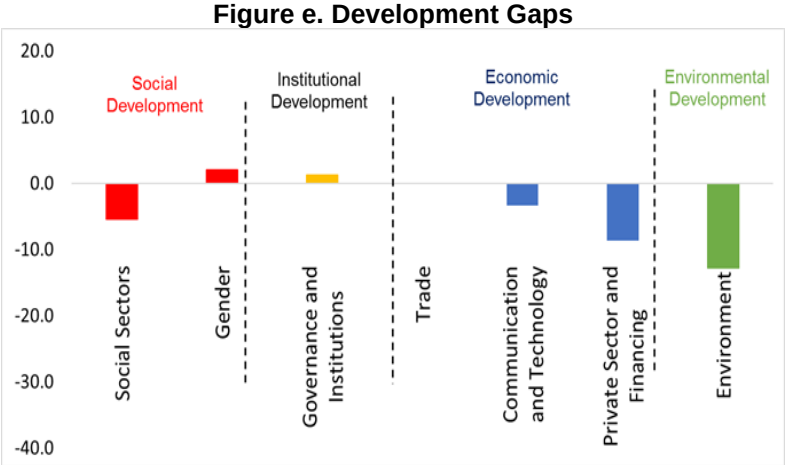
…and limited private sector investment.

Figure d. Investment as a Percent of GDP



The major developments gaps are in the environment, private sector and financing, the social sectors, communication and technology categories.

Figure e. Development Gaps



Sources: World Bank, International Monetary Fund, April 2018 *World Economic Outlook*

Contributor: Henry Mooney

Overview

From the early 1990s through 2013, Jamaica's economic performance was volatile and lacklustre. Imprudent policies and shocks contributed to rising deficits and debt, low levels of investment and innovation, and financial crises. Socio-economic conditions also suffered, as reflected in stagnant levels of per capita GDP, high unemployment, and poor outcomes on key indicators of health, education, and security.

Despite these previous challenges, Jamaica's government has succeeded in reforming both policies and institutions over the past five years. With the support of development partners, debt levels have fallen by nearly a third since 2013, inflation and interest rates are at record lows, external imbalances have narrowed, and confidence in the country's economy and policy credibility have increased tremendously. Conditions have begun to improve, with employment and business confidence at all-time highs, and credit conditions improving significantly. Looking forward, authorities will need to stay the course in terms of policy prudence and focus attention on structural reforms aimed at making development more rapid and inclusive.

Economic and Social Trends

Jamaica is a small, open economy, characterized by low growth and high debt. Since 1990, Jamaica's average real GDP growth rate has been approximately 1 percent per year. This is well below the approximately 3 percent average of other Caribbean economies (Figure 1) and the 4 percent average for Latin America and the Caribbean. Years of high deficits, public enterprise borrowing, financial sector crises, and bailouts resulted in rapid debt accumulation that has stifled growth and development. As a result, the standard of living has remained stagnant—as measured by per capita GDP—for the past five decades.

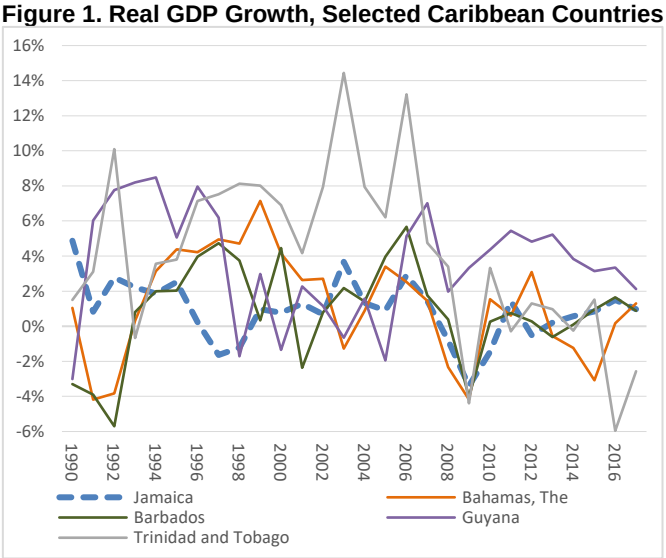
Jamaica signed a four-year Extended Fund Facility (EFF) arrangement with the International Monetary Fund (IMF) in May 2013. The primary aim of the program was to restore macroeconomic and debt sustainability, support the development of institutions and capacity, and promote structural reforms. The EFF provided a roadmap for fiscal and external sustainability aimed at reducing the debt-to-GDP ratio from 145.3 percent in FY2012/2013 to below 100 percent by FY2019/2020. This initial target is now expected to be reached a year ahead of schedule. In addition, the EFF revived the unfinished structural reform agenda embedded in previous IMF programmes.

Highlights

- *Jamaica has a long history of volatile growth, policy inconsistency, and vulnerability to exogenous shocks. Despite gains in recent years, the global financial crisis adversely affected socio-economic outcomes.*
- *Authorities have made tremendous strides towards policy reform and institutional development since 2013. This has helped reverse the trajectory of public debt, improve investment conditions, and set the stage for an acceleration of growth and the reduction of poverty.*
- *Authorities must stay the course to ensure that hard-won macroeconomic stability is maintained. Reform efforts must now turn to structural reforms aimed at restructuring the public sector to increase efficiency and public investment, improving the investment climate, deepening financial markets, and ensuring that growth is more inclusive than in the past.*

A three-year successor Stand-By Arrangement with the IMF was launched in November 2016. Jamaica's performance and policy implementation since the launch of the 2013 IMF programme has been strong, with fiscal surpluses meeting or exceeding targets, and debt reduction progressing faster than initially expected. Despite successful implementation of a number of the programme's structural measures, however, a major hurdle remains with respect to reducing the public sector wage bill, which accounts for about one-third of government revenues.

Figure 1. Real GDP Growth, Selected Caribbean Countries

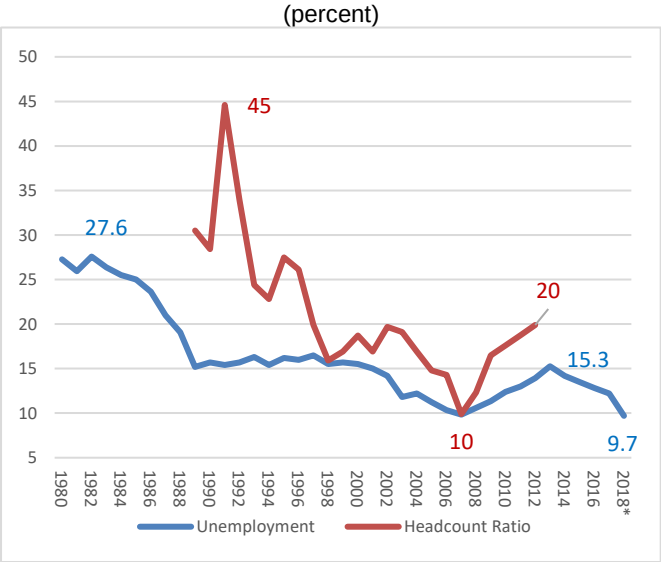


Source: World Bank, World Development Indicators.

Socio-economic indicators deteriorated following the global financial crisis. Prior to the crisis, both the rate of unemployment and the poverty headcount ratio (i.e., the proportion of the population living below country-specific poverty lines) had been steadily

decreasing, with both reaching then-historic lows of about 10 percent in 2007. Unfortunately, this trend reversed with the onset of the global financial crisis, which contributed to reductions in output, employment, and remittances from abroad. As a consequence, between 2007 and 2012 (just prior to the initiation of the 2013 IMF programme), the rate of unemployment increased by about half and the incidence of poverty doubled (Figure 2). These increases were more pronounced in urban areas, where the poverty headcount ratio quadrupled from 5 to 19 percent between 2007 and 2012. While the economic stabilization and rebound in growth ushered in by the IMF-supported programme since 2013 has helped reduce unemployment to record lows (9.7 percent as of the end of April 2018), poverty has remained stubbornly high, as represented by a headcount ratio of over 20 percent in 2015 (latest available data).

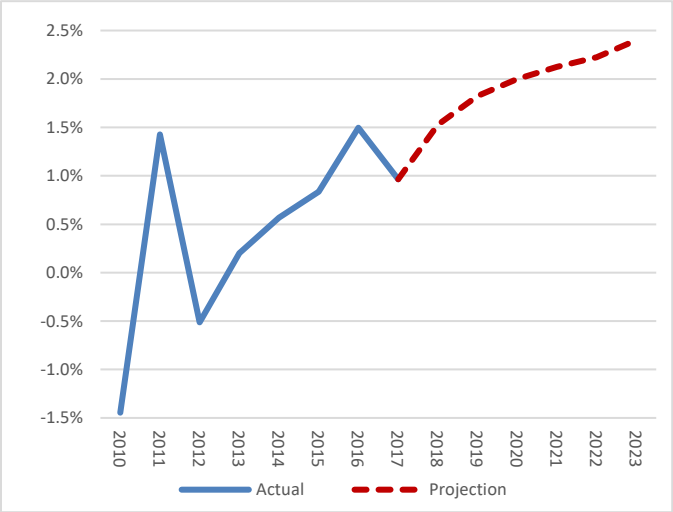
Figure 2. Unemployment and Poverty Headcount Ratio
(percent)



Sources: International Monetary Fund, April 2018 *World Economic Outlook*; and World Bank, World Development Indicators.
* Latest data from the Jamaica Statistical Institute for end-March 2018.

Growth and other measures of economic performance have improved considerably since 2013. Real GDP growth is expected to reach 1.7 percent (year-on-year) by the end of FY2018/2019, nearly double the 20-year average (Figure 3). Growth rates are now projected to accelerate to well over 2 percent per year over the medium term. In the absence of rapid increases in oil prices or other unforeseen external shocks over the medium term, this growth acceleration should be supported by low and stable inflation within the target band (4 to 6 percent)[1], in turn fostering higher rates of both savings and investment, as well as by incentives to reduce the high level of deposit dollarization—about 41 percent of deposits were denominated in foreign currency in 2018.[2] The current account deficit is projected to remain below 3 percent over the medium term, with narrowing external imbalances driven in large part by continued fiscal restraint. As both credit conditions and external and domestic investor confidence continue to improve, expectations are that private sector activity will increasingly drive growth.

Figure 3. Economic Growth Projections (Real GDP)



Sources: International Monetary Fund, April 2018 *World Economic Outlook*; and IDB staff calculations.

Development Constraints

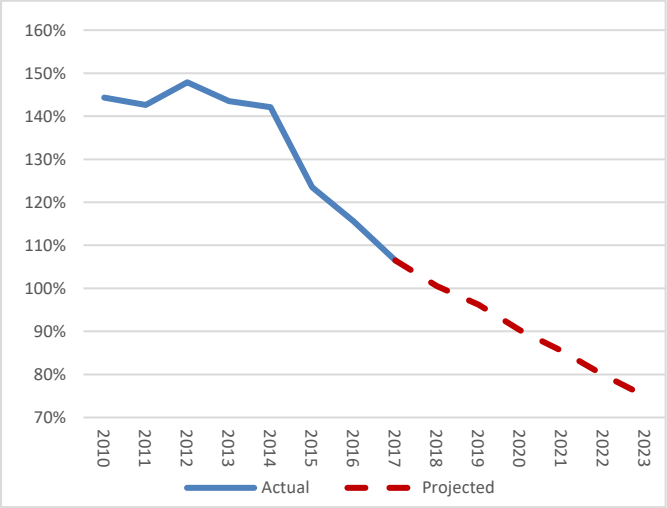
Jamaica is vulnerable to exogenous shocks, including because of its narrow export and production base and its dependence on commodity imports (e.g., food and fuel). Domestic food production is subject to frequent weather-related shocks that have contributed to output volatility and bouts of inflation. In addition, Jamaica depends heavily on remittances, which are equal to about 15 percent of GDP. Exports are concentrated, with three-quarters destined for the United States, Canada, and the United Kingdom. These countries are also home to most tourists visiting Jamaica, and the source of most remittances.

Despite tremendous progress towards debt consolidation since 2013, Jamaica remains one of

[1] The Bank of Jamaica shifted to an inflation-targeting framework in 2017. Both inflation and policy rates have fallen considerably since that time, supporting the financial sector and helping to entrench market expectations of prudent policies.
[2] Calculated as foreign currency deposits / M3 (monetary aggregate).

the world's most indebted countries. Public debt fell by nearly a third from over 145 percent of GDP in 2013 to 104 percent of GDP as of the end of March 2018 (Figure 4). Barring any change in the direction of policies or the materialization of unforeseen shocks, this trend is expected to continue.

Figure 4. Public Debt (percent of GDP)



Sources: International Monetary Fund, April 2018 *World Economic Outlook*; and IDB staff calculations.

Debt service and public wages crowd out investment in productive sectors. With two-thirds of revenues having been dedicated to substantial interest payments and salaries since the mid-1990s, infrastructure and social expenditure have been crowded out, compromising growth, productivity, and social outcomes. High public sector financing needs and the resulting increase in domestic interest rates have also crowded out domestic credit, curtailing investment and the private sector's ability to drive productivity enhancements and job creation.

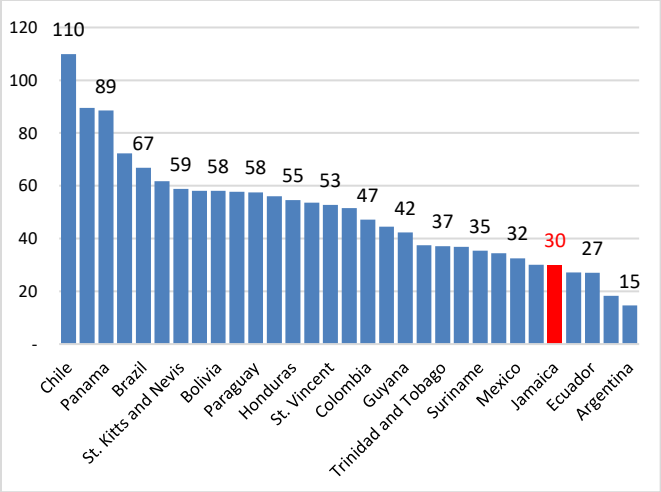
Despite encouraging recent tax reforms, further expenditure rationalization is needed. The two main expenditure items continue to be interest payments (7 percent of GDP) and public sector salaries (9.6 percent of GDP) in 2018. While debt service payments will decrease as the government makes progress towards debt reduction, the wage bill can only be reduced via public sector modernization and reforms to increase the its efficiency.

The current level of the public wage bill has been driven by several rounds of salary increases. These resulted in an increase in public sector salaries and other forms of compensation from the equivalent of 5 percent of GDP in FY1995/1996 to almost 11 percent by FY2009/2010, with much of this increase taking the form of subsidies and other non-wage payments. The magnitude of the problem is highlighted by peer comparison—public wages average about 6 percent of GDP in Europe, and 5 percent of GDP in Asia and the Pacific. Reform of state-owned entities is also crucial, as these have been a major source of debt accumulation via contingent liabilities. Similarly, public pension reforms are needed to avoid future fiscal risks.

Jamaican businesses face several challenges. Despite recent reforms, firms still struggle with red tape and excessive bureaucracy. By international comparison, Jamaica's business climate is weak in the areas of taxation, accessing electricity, resolving legal disputes, obtaining construction permits, and trading across borders. In terms of innovation, Jamaican firms struggle with gaps in the legal framework for intellectual property, as well as with weak policies and institutions for innovation.

Access to credit and a shallow financial sector are also key impediments to growth and investment in Jamaica.[3] As highlighted in Figure 5, Jamaica's ratio of domestic private credit to GDP of 30 percent in 2015 (estimated at 32 percent in 2016)—a common indicator of financial sector depth—was well below the average for middle-income countries (94 percent), Latin America and the Caribbean (49 percent), and sub-Saharan Africa (46 percent). As a consequence, the share of Jamaican firms with loans is low, and firms report that a lack of access to credit is a key impediment to investment, innovation, employment creation, and growth.

Figure 5. Domestic Credit to the Private Sector, 2015
(percent of GDP)



Sources: World Bank World Development Indicators; IMF, World Economic Outlook databases; and IDB staff calculations.

[3] For a broader discussion of related issues, see Mooney, "Jamaica: Financial Development, Access and Inclusion—Constraints and Options", 2018.

High electricity prices have also been a drag for businesses. Despite a decrease from US$0.39 to US$0.27 per KWh between 2012 and 2015, Jamaica's average electricity tariff was high when compared to other countries in the region and across the world—for example, Barbados at US$0.24 per KWh, Trinidad and Tobago at US$0.06 per KWh, and the United States at US$0.1 per KWh. Electricity generation is still dependent on inefficient diesel generators, and is subject to considerable technical losses, including from theft.

Tackling inequality, reducing poverty, and protecting those who are most vulnerable requires addressing differences in quality and access to basic services, as well as providing a social safety net. In terms of education, access has improved considerably and school enrolment has increased to a net enrolment rate of 99 percent for pre-primary education, 92.5 percent for grades 1 to 6, and 80 percent for grades 7 to 9. At the same time, social protection through Jamaica's conditional cash transfer program supports poorer households, while improving health and education outcomes for vulnerable mothers and children. However, the quality of these services and access to them varies substantially, as do outcomes in terms of health and education.

Non-communicable diseases (NCDs) have become a major financial burden in the health sector, while emerging infectious diseases threaten economic stability. Insufficient investment in infrastructure, equipment, supplies, and human resources has compromised the quality of health services—particularly the primary care system. This in turn has led to the public avoiding primary health care facilities, and to an overwhelming demand for hospital services. The challenge of providing health services is exacerbated by an increased burden from NCDs, which have surpassed communicable diseases as the main cause of mortality and morbidity.

Conclusion

Jamaica's authorities have made tremendous progress over the past five years. This includes praiseworthy success in restoring macroeconomic stability and debt sustainability. However, achieving higher and durable rates of growth has proven more challenging. Indications are that Jamaica's economy might finally be in a position to reap the benefits of lower debt and a track record of fiscal prudence, which have already spurred more rapid credit growth and improved private sector confidence. Nevertheless, Jamaica continues to face vulnerabilities that require prudent policies and reforms that can serve as the foundation for more rapid, consistent, and inclusive economic growth.

The IMF programme and parallel efforts of development partners have served as anchors for economic policies. To date, considerable effort has been made towards entrenching both prudent policies and the reform of economic institutions, including shifting from direct to indirect taxes, strengthening the social safety net, and reallocating public resources to infrastructure spending. In this context, authorities have also succeeded in strengthening monetary policy and the central bank's operational capacity as it shifts to inflation targeting, greater exchange rate flexibility, and a focus on building international reserves.

Looking forward, structural reform requirements are much more complex and uncertain than those associated with macroeconomic stabilization. The government's efforts should now aim to directly address the country's most pressing development challenges, including modernizing the public sector to enhance efficiency and reduce wage costs, supporting development of a deeper and more inclusive financial sector, and increasing levels of public investment in areas that can increase productivity and support private sector investment and expansion.

Figure a. Per Capita Gross National Income (Atlas method, current US$)

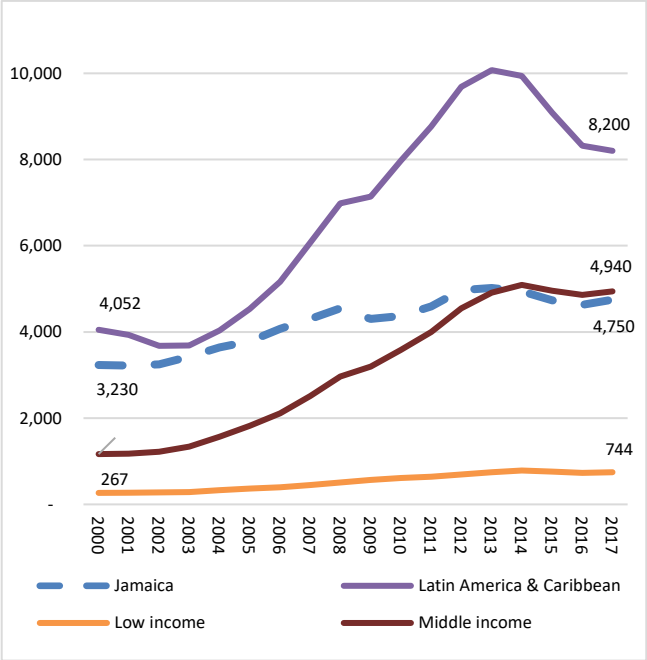


Figure c. Domestic Market Interest Rates (percent)

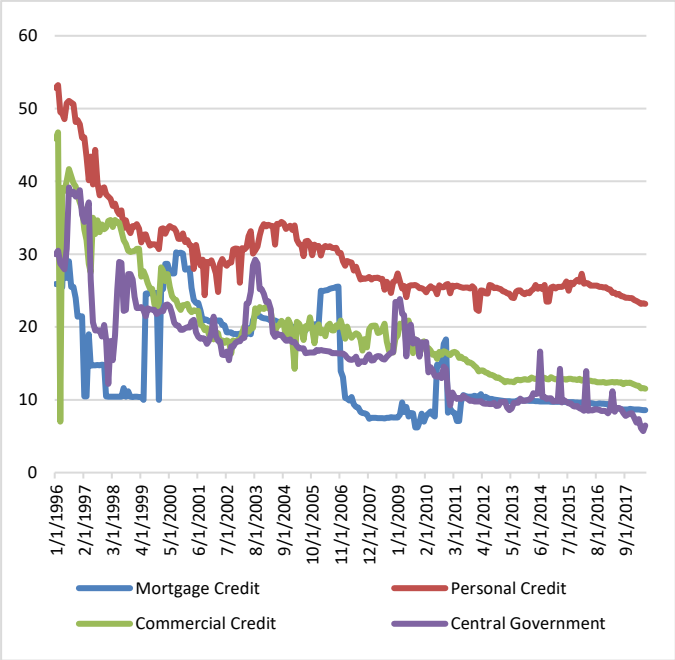


Figure b. Inflation and Exchange Rate since 1990 (percent)

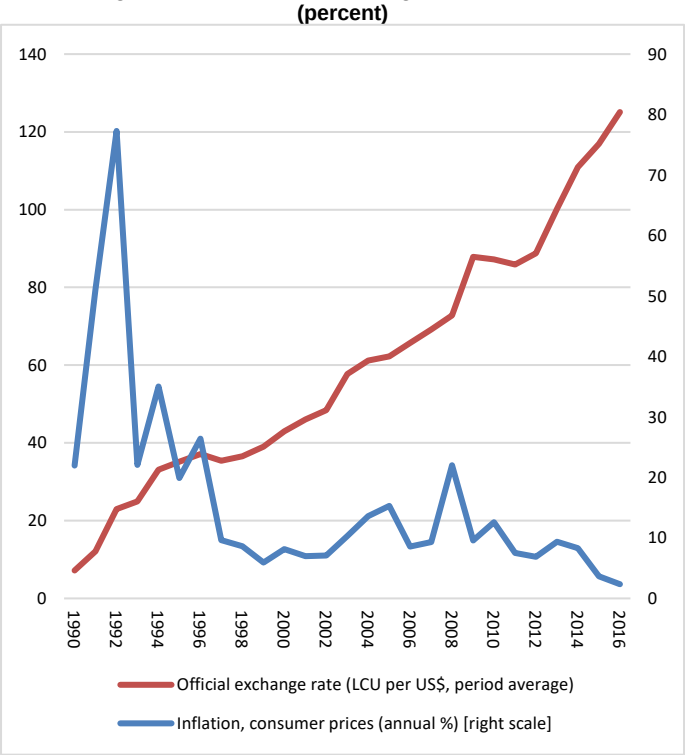
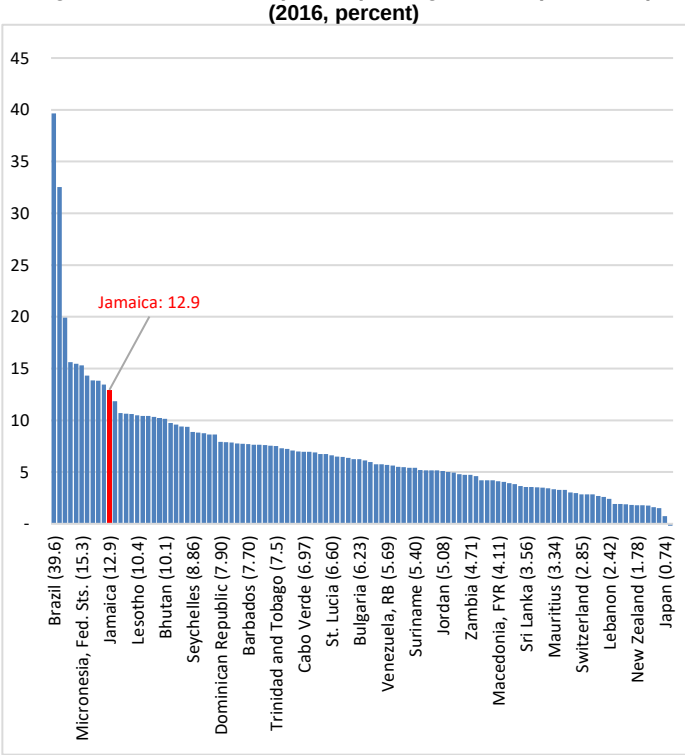


Figure d. Interest Rate Spreads (lending rates / deposit rates) (2016, percent)



Sources: Bank of Jamaica, IMF World Economic Outlook (April 2018), World Bank World Development Indicators, and author calculations.

Contributor: Jeetendra Khadan

Overview

Suriname is a small mineral-dependent economy that is vulnerable to external shocks. The economy is highly concentrated in the extractive industries—specifically, gold and crude oil—which play a key role in driving economic growth, foreign exchange earnings, and government revenues. Despite good economic performance for the decade ending in 2014, the recent decline in gold and crude oil prices and the cessation of alumina production have negatively affected the economy. The commodity crisis of 2015 showed that the country's past prosperity depended little on having an effective public sector to allocate resources efficiently or on a strong private sector, given the presence of large sums of foreign aid and mineral and crude oil rents. The recent decline in resource rents that led to adverse macroeconomic and social outcomes served to emphasize the need to strengthen public sector management and address structural weakness in the economy to promote sustainable growth and development. In this regard, this bulletin examines Suriname's recent economic and social trends, medium-term economic and social outlook, and risk factors, and discusses the country's main development constraints.

Recent Economic and Social Trends

Recent economic growth was affected by the 2015 commodity shock, with a low level of recovery projected for 2017. The fall in commodity prices and the cessation of alumina production continue to weigh heavily on Suriname's economic performance. Real GDP growth declined from an annual average of 4.4 percent during 2001–2014 to -3.9 percent in 2015–2016. In 2016, the wholesale and retail trade sector declined by 41.3 percent, followed by the construction sector (13.4 percent) and the mining and quarrying sector (9.8 percent). Notably, the mining and quarrying sector had been declining by an annual average of -8.2 percent since 2013. On the other hand, the transportation, storage and communication sector, agriculture sector, and manufacturing sector reported positive growth rates in 2016: 6.3 percent, 3.8 percent, and 1.8 percent, respectively. The International Monetary Fund (IMF) has forecast almost zero overall growth (0.001 of a percent) for 2017.

Fiscal performance and debt remain areas of concern. Suriname has been recording fiscal deficits since 2009. The size of fiscal deficits increased after 2014 due to a significant decline in mining-related revenues. Revenues from the mining sector fell from an average of 7.1 percent of GDP for 2012–2014 to 2.8 percent of GDP for 2015–2017. On the expenditure side, the authorities reduced expenditure by 5 percent of GDP in 2016 to bring it in line with historical levels. Alongside relatively larger fiscal deficits, economic decline, and an exchange rate depreciation, the country's debt-to-GDP ratio increased from 26.3 percent in 2014 to 73.5 percent of estimated 2017 GDP as of the end of May 2018, with external debt accounting for 70 percent of total debt.

Highlights

- *One of the most important challenges facing Suriname in the short term is achieving sustained economic stabilization.*
- *Structural reforms are needed to improve the business environment and enhance private sector performance.*
- *Social outcomes should continue to improve with investments in education and health.*
- *The country's relatively low crime rate, abundance of natural resources, and commitment to undertake reforms to support macroeconomic stability and improve the business climate are major strengths that can contribute to improving growth prospects in the long term.*

Inflationary pressures have subsided and there is greater stability in the exchange rate. Inflation, which accelerated to peak at 79.2 percent in October 2016, declined to 8.6 percent in March 2018. The nominal exchange rate has also been relatively stable at US$1:SRD7.5 since December 2016, after devaluation in 2016.

International reserves improved in 2017 after falling drastically in 2015. International reserves declined by an average of 30 percent annually over 2013–2015, reaching a low in 2015 of US$330 million, or 1.5 months of import cover. International reserves have since increased to US$533.4 million as of June 2018 (equivalent to roughly three months of import cover).

Suriname is ranked in the high human development category of the United Nations Development Programme's Human Development Index. The indicators show that life expectancy at birth stood at 71.3 years in 2015, about seven years more than what it was in 1990. Similarly, mean years of schooling increased from 7.7 years in 2005 to 8.3 years in 2015. The 2016–2017 Suriname Survey of Living Conditions estimated the country's overall poverty headcount rate at 26.2 percent, comparable to other countries in the region. However, poverty in the interior is much higher at 47.9 percent, with almost one in every two households classified as poor. Suriname's General Bureau of Statistics has reported that the unemployment rate almost doubled after the 2015

economic crisis, reaching 9.7 percent in 2016 compared to 5.5 percent in 2014.

Medium-term Economic and Social Outlook

Suriname's medium-term economic outlook remains challenging, but the IMF forecasts positive economic growth for 2018. The expected improvement in economic performance is primarily related to increased output from two gold mines and stabilization of gold prices. The state oil company has also signed production-sharing contracts for two blocks off the coast of Suriname in 2017, and drilling of several wells is expected to commence in the medium term. The IMF forecasts real GDP growth of 1.2 percent in 2018, with growth averaging about 2.6 percent over the period 2019–2023. Also, better prospects in the mining sector are expected to contribute to a narrowing of the current account deficit. However, fiscal imbalances and elevated debt levels are expected to remain challenges over the medium term. The IMF has forecast unemployment to decline over the medium term to an annual average of 5.4 percent over 2019–2023 and for inflation to decline to about 3.9 percent at the end of 2023.

Risk Factors

Risks to the country's medium-term outlook are mostly related to external factors. One of the main risks that persists relates to unexpected shocks to commodity prices in the presence of relatively weak economic institutions and limited fiscal and external buffers. Suriname needs to strengthen fiscal buffers over the medium term and continue to implement reforms to build resilience to global economic shocks. Additionally, recent developments related to the confiscation of shipments of euro dollars from Suriname by the authorities in the Netherlands could potentially affect Suriname in the medium term.

Development Constraints

The framework used to examine the development constraints facing Suriname is a benchmarking analysis that follows an approach similar to that set out in Hausmann, Rodrik, and Velasco (2005) and Borensztein et al. (2014). The main challenges in terms of macroeconomic stability, private sector development, and social outcomes are summarized below.[1]

One of the most important challenges facing Suriname in the short term is achieving sustained economic stabilization. Macroeconomic stability is affected by being highly dependent on only a few commodities, which contributes to an elevated level of sensitivity of government revenues and foreign exchange earnings to commodity prices. On the revenue side, tax compliance with respect to direct taxes is reported to be low, estimated at 40 percent of potential revenues (IDB 2017). Non-compliance is attributed to several factors, including (1) low technical capacity, which is reflected in a limited number of qualified staff, the need for specialized training in key areas such as tax collection, audits, processes, procedures and risk management, and difficulties in recruiting and retaining qualified talent; (2) organizational structure challenges, which results in inefficiencies; (3) outdated management procedures and systems; and (4) physical infrastructure (IDB 2016). On the expenditure side, government spending is rigidly focused on civil service wages and subsidies and transfers: the government's wage bill is estimated to be roughly one-third of government spending and reflects its large public sector workforce (IDB 2016), while subsidies and transfers account for another one-third of government spending. Moreover, the public sector has about 144 registered state-owned enterprises, not all of which are adequately monitored and performance-evaluated regularly (IDB 2016).

Structural reforms are needed to improve the business environment and the efficiency of public services to enhance private sector performance. Suriname was ranked relatively low in the World Bank's 2018 Doing Business Report: 165th out of 190 countries. The ranking reflects Suriname's performance on several factors that influence the ease of doing business. Compared to comparators – the rest of the small economies of the world (ROSE) (defined by a population size of less than 3 million), Latin America, and member countries of the Organisation for Economic Co-operation and Development (OECD) – Suriname underperforms in 7 of 10 areas examined by the Ease of Doing Business Index: dealing with construction permits, getting credit, protecting minority investors, registering a property, getting electricity, starting a business, and enforcing contracts. However, a historical look of Suriname's performance on the index shows improvements in areas such as starting a business, registering a property, protecting minority investors, trading across borders, and resolving insolvency (IDB 2017). In the 2018 Doing Business Report, Suriname reported a significant improvement in registering a property, as the government made transferring property more transparent. The improvement in trading across borders was attributed to implementation of an automated customs data management system (the Automated System for Customs

[1] For further details the interested reader is referred to IDB (2016).

Data), which led to a reduction in time for documentary and border compliance.

Businesspersons in Suriname have also identified several challenges that affect their performance, with the top three being an inadequately educated workforce, the cost of finance, and a perception of corruption (IDB 2017). Moreover, there are also institutional weaknesses related to intellectual property rights, the registration of patents and copyrights, and inadequate protection for trade secrets and design layout (U.S. Department of State 2015). The IDB (2016) also noted that current infrastructure and logistics present challenges for connectivity via air and shipping networks.

Health outcomes could be improved. Information from the World Bank's World Development Indicators shows that Suriname spends less than comparators (Latin America and ROSE) in the area of health. Public health expenditure is 2.9 percent of GDP compared to 3 percent for Latin America and 4.6 percent for ROSE. Associated with lower expenditure on health is relatively poorer health outcomes, as evidenced by several indicators. The country's life expectancy for males was 68.2 years in 2015 compared to an average of 74.6 years for Latin America and 67.5 for ROSE, while for females the difference is four years lower than Latin America and 1.5 years better than ROSE. A similar observation is revealed for other indicators of the country's health status. The infant mortality rate is 19 per 1,000 live births, higher than the average for Latin America (15 per 1,000 live births) but marginally lower than the 19.5 for ROSE.

Access to education has improved, but there are issues related to educational quality and high dropout rates. In 2015, 95.4 percent of children of primary school age were enrolled in primary or secondary school, compared to 78 percent in 1999 (IDB 2016). More work is needed to improve educational quality, particularly strengthening institutional capacity to effectively monitor and evaluate the performance of the school system. There is also a relatively high dropout rate at the primary and secondary education levels, especially for males. The World Bank's World Development Indicators show that the primary and secondary school dropout rate is 34.6 percent for males and 15.5 percent for females. Male dropout rates are higher than in Latin America (23.5 percent), ROSE (15.9 percent), and the OECD (3.9 percent). Also, female dropout rates are higher than in ROSE (13.2 percent) and the OECD (3.6 percent), but lower than in Latin America (22.4 percent). Nevertheless, despite the relatively higher dropout rates and other challenges facing Suriname's education system, data from the World Bank's World Development Indicators show that the country's adult literacy rate is high at 95.6 percent and better than the average for Latin America (93.1) and ROSE (90.6), but lower than that for the OECD (98.1).

Conclusion

Suriname faces several challenges that can affect its medium-term outlook, but the country is also progressing on reforms to tackle important development constraints. In terms of macroeconomic challenges, the authorities have committed to undertaking important reforms to strengthen the fiscal framework and the execution of fiscal policy. In this regard, the authorities have passed legislation to establish a Savings and Stability Fund, and have committed to continuing planned reforms to improve tax administration and tax policy over the medium term. In addition, the government should continue to undertake broad-based structural reforms to improve productivity growth, improve the business climate, and support economic activity in the non-mineral sector. Human capital is an important determinant of a country's development, and the evidence indicates that more effort is needed to improve both access to and the quality of health and education. There are some policy initiatives being implemented to improve health services and the internal efficiency of the education system that could potentially improve the quality of human capital over the long term. Amid these ongoing challenges, Suriname's low crime rate, abundance of natural resources, and commitment to undertake reforms to strengthen the macroeconomic framework and improve the business environment are some of its major strengths that could contribute to improving growth prospects in the long term.

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Borensztein E., S.J. Miller, G. Sánchez, and P. Valenzuela. 2014. Development Diagnostics for the Southern Cone. IDB Working Paper No. 85194. Inter-American Development Bank, Washington, DC.

Inter-American Development Bank (IDB). 2016. Country Development Challenges Report. IDB, Washington, DC.

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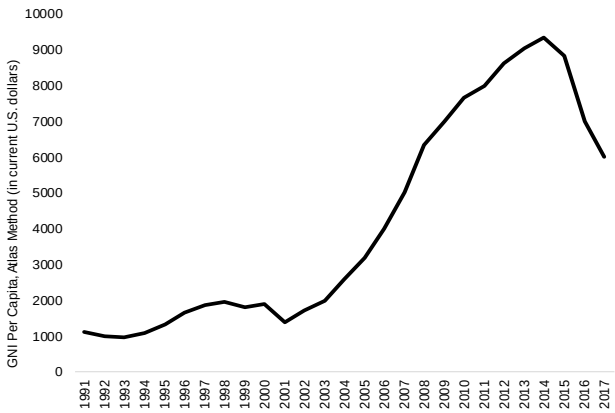
U.S. State Department. 2015. "2015 Investment Climate Statement – Suriname." Bureau of Economic and Business Affairs, U.S. State Department, Washington, DC.

Suriname is a middle income country that experienced a 36 percent decline in its GNI Per Capita since 2014.

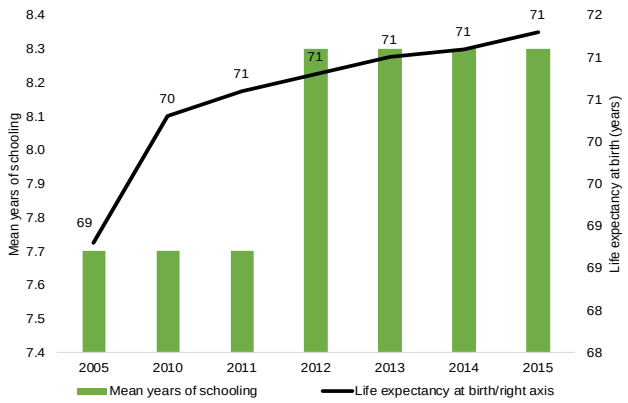
Figure a. GNI per capita, Atlas Method (current U.S. dollars)



Source: World Bank Development Indicators database.

…Suriname has made important improvements in key human development indicators.

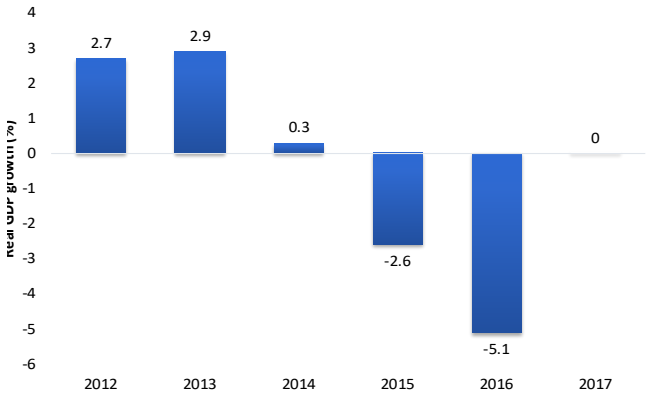
Figure b. Human Development Indicators



Source: United Nations Development Programme, Human Development Report (2016).

The 2015 commodity shock significantly affected economic growth…

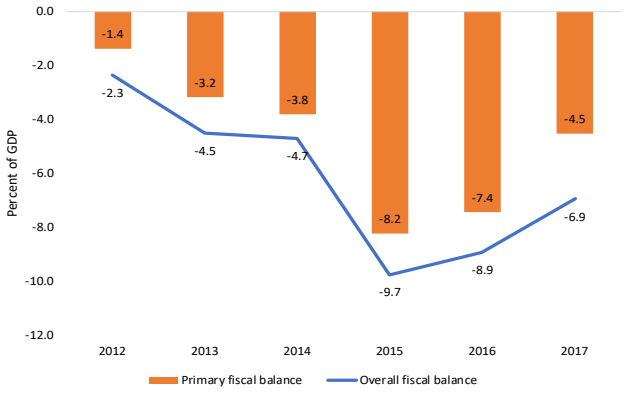
Figure c. Real GDP growth



Sources: Central Bank of Suriname; and the International Monetary Fund.

…and weakened the fiscal accounts.

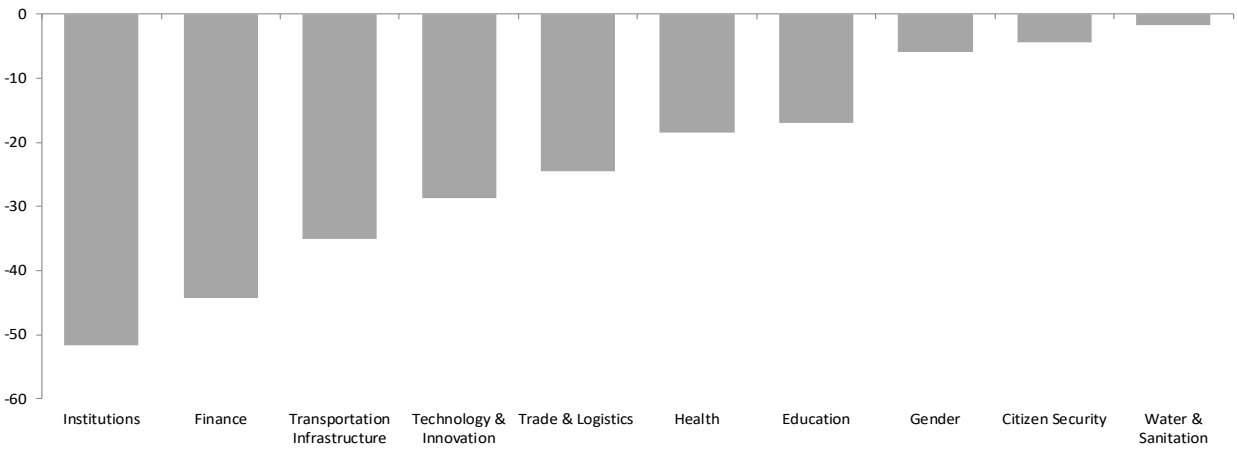
Figure d. Fiscal Balances (% of GDP)



Sources: Ministry of Finance; and the International Monetary Fund.

The most important development gaps based on a benchmarking exercise relate to the quality of institutions, financing (cost and access), transportation infrastructure, and technology and innovation.

Figure e. Development Gaps



Source: IDB (2016).

Note: A development gap is defined as the distance between the observed and the expected value of a development indicator for a country (Borenztein et al, 2014). The expected value of the development indicator is simply the linear (or quadratic) fit from a cross-country regression of such indicator on GDP per capita. As such, the development gap compares indicators taking into account differences in the income level of countries. The development gap definition was applied to 70 indicators grouped into the 10 sector identified in this chart.

Contributor: Lodewijk Smets

Overview

Trinidad and Tobago is a resource-based economy dependent on the performance of the energy sector. The population of Trinidad and Tobago is estimated at 1,350,000, and per capita income is US$30,520 (purchasing power parity - PPP), the highest among Latin American and Caribbean countries. Sustained investments in health and education have led to gains in social development outcomes. Recently, however, the country has had more difficulty making progress in these areas. While the economy is expected to grow at around 1.5 percent on average in the medium term, tackling structural development constraints – such as public sector governance and competitiveness – would contribute to increasing growth prospects.

Highlights

- *Trinidad and Tobago is a resource-based economy with a relatively high income level.*
- *The economy is expected to grow at 1.5 percent on average in the medium term.*
- *Tackling structural development challenges could further increase growth prospects.*
- *The country has shown a commitment to solve difficult development problems.*

Recent Economic and Social Trends

Trinidad and Tobago is slowly recovering from a deep economic recession. A sharp decline in energy prices and lower domestic production of oil and natural gas caused the economy to contract by 6.1 percent in 2016 and 2.6 percent in 2017. Recently, however, the country witnessed a turnaround in the energy sector, which is expected to lead to positive economic growth. The International Monetary Fund (IMF) projects the economy of Trinidad and Tobago to grow by 1 percent in 2018. Growth in the non-energy sector is expected to remain negative for the third consecutive year.

The government is engaging in a programme of fiscal consolidation. Facing significant energy revenue shortfalls, the government has adopted adjustment measures over the past two fiscal years. Key changes include tax reforms in the energy and non-energy sectors, a reduction of fuel subsidies, and the establishment of a procurement board and revenue authority. Aided by favourable conditions in the energy sector and reforms in corporate taxation, total revenue increased in the first quarter of FY2018 while expenditure fell, leading to a slight primary surplus.[1] Trinidad and Tobago's public-debt-to-GDP ratio decreased from 62.8 percent of GDP in September 2017 to 61.6 percent of GDP in December 2017.

Foreign reserves have continued to fall. Net official reserves had declined by 11 percent (year-on-year) as of the end of July 2018. The country's net official reserves stood at US$7.7 billion or 8.5 months of import cover. Sizable investments by energy companies, tax reforms, and favourable production and price conditions in the oil and gas sector may slow the decline in foreign reserves. The increased supply of hard currency may also ease the tightness in the foreign exchange market. Anecdotal evidence suggests that local firms are facing fewer difficulties in sourcing foreign exchange to service debts with foreign suppliers.

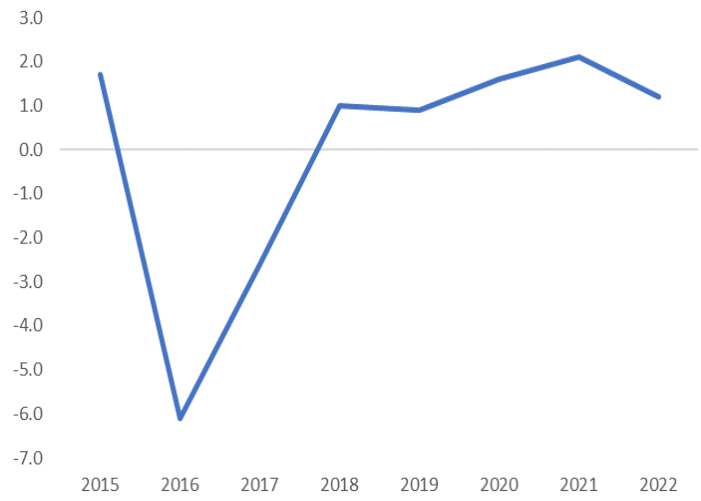
Sustained investments in health and education have led to gains in social development outcomes. In Trinidad and Tobago, the health and education sectors typically receive large allocations in the national budget. For instance, in FY2017 the education sector received 10 percent of the national budget, the second-highest allocation just behind national security. These investments led to increases from 1980 to 2013 in mean years of life expectancy (from 70 to 72.9 years) and schooling (from 11 to 14.8 years). Recently, however, Trinidad and Tobago has not been able to make much progress, and the country therefore dropped from 64th to 65th on the United Nations Development Programme's 2016 Human Development Index. According to the last official measurement — in 2005 — 16.7 percent of the total population was considered poor.

Medium-Term Outlook

According to the IMF, real growth will average 1.5 percent in the medium term. For 2019, the IMF estimates that the economy will grow at a rate of 0.9 of a percent, while in 2020 it is forecast to increase by 1.6 percent. For 2021 and 2022, the IMF projects the economy to grow at 2.1 and 1.2 percent, respectively (Figure 1). In 2019, growth is expected to come from the energy sector. For 2020–2022, the non-energy sector is anticipated to contribute to growth, possibly due to spill-overs from the energy sector and greater fiscal space.

[1] The fiscal year runs from October to September. The first quarter of FY2018 thus refers to the period from October 2017 to December 2017. Fiscal statistics are from the government.

Figure 1. Real GDP Growth (percent)



Source: International Monetary Fund

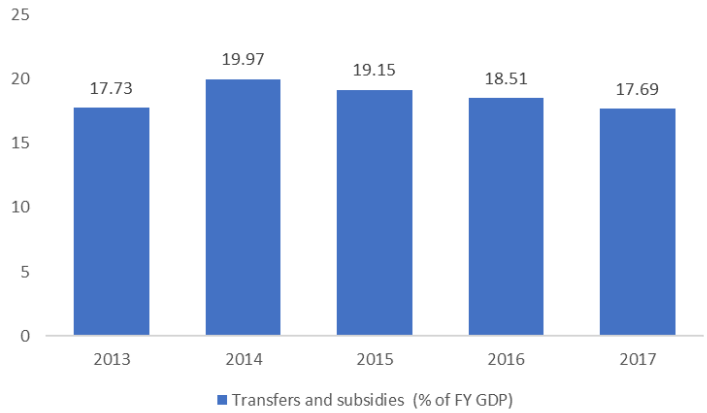
To fully restore macroeconomic stability, Trinidad and Tobago needs to continue with fiscal consolidation. The IMF estimates that the government needs to make fiscal adjustments of about 6.5 percent of GDP, balancing revenue increases with expenditure reductions. While the government is already taking steps towards this end, as noted above, further effort is needed. The IMF notes that addressing tax arrears, introducing value-added-tax reforms and new transfer pricing legislation, and optimizing transfers and subsidies and restructuring state-owned enterprises are important reform areas to pursue. Failing to restructure government finances may put public debt on an unsustainable path. In the short term, Trinidad and Tobago can rely on substantial financial buffers to finance fiscal deficits, but in the medium term consolidation is necessary to ensure growth and debt sustainability.

Several downside risks could affect Trinidad and Tobago's medium-term outlook. A reversal in energy sector conditions would curtail economic growth, reduce the inflow of foreign exchange, and negatively affect government revenues. Furthermore, continued monetary policy normalization in the United States may prompt the Central Bank of Trinidad and Tobago to raise its main policy rate, which could affect the cost of financing for both the public and private sectors. Finally, an accelerated depletion of foreign reserves holds the risk of triggering a balance of payments crisis.

Development Constraints

To raise growth prospects, Trinidad and Tobago has to address public sector governance challenges. Difficulties include civil service management, tax and revenue policies, and allocative inefficiencies in government expenditures. A development gap analysis indicates that Trinidad and Tobago scores below its potential in terms of public sector performance (see the Snapshot of the Economy). Inefficient spending is one of the biggest obstacles faced by the country. The key issues regarding fiscal expenditure are high transfers and subsidies – which constituted more than 17 percent of GDP in FY2016/2017 – and low capital investment (2.4 percent of GDP in FY2016/2017). Non-distortionary transfers to citizens of rents from natural resources are not necessarily an inefficient public policy. In Trinidad and Tobago, however, fuel and energy subsidies are highly distortionary, with significant environmental and fiscal effects. Furthermore, sound policies to efficiently regulate state-owned enterprises are lacking. This creates reporting and governance issues that may result in inefficiencies in public expenditures. Finally, the country lacks a sound framework to appraise and prioritize capital expenditure programmes. As such, it is difficult to link public investment projects to the country's development priorities and long-term vision.

Figure 2. Transfers and Subsidies (percent)



Source: Central Bank of Trinidad and Tobago.

There is scope to improve economic institutions in Trinidad and Tobago. Fiscal performance worldwide has been shown to improve with the existence of institutions that aim to correct incentives, contain overspending, and allow for medium-term fiscal planning. Trinidad and Tobago, however, has little experience with legal rules and institutions to improve fiscal performance. Therefore,

the country would benefit from a detailed fiscal medium-term framework that allows for planning and budget execution. Public procurement could also be strengthened. Trinidad and Tobago could benefit from enhanced transparency in public procurement processes by increasing the utilization of competitive tenders, recruiting highly qualified procurement staff, and publicizing information on procurement processes and awarded contracts. The recent appointment of a Procurement Board is an important step in strengthening public procurement processes. Finally, the Central Statistics Office (CSO) needs to be reformed to ensure timely availability of high-quality data. Currently, the CSO's legal framework is outdated, and the office also lacks the financial and human resources needed to perform its tasks. Fortunately, steps are being undertaken to transform the current office into an autonomous statistics institute.

There is a need to invest further in human capital development. A healthy and well-educated workforce will improve productivity and support sustainable growth.

In education, evidence from international and regional assessments shows that student performance in Trinidad and Tobago lags that of countries with comparable income. For instance, among the 70 countries and regions that participated in the 2015 Programme for International Student Assessment (PISA), Trinidad and Tobago ranked 52nd in reading and 53rd in mathematics. Even though the scores are similar to those of other participating Latin American and Caribbean countries, they are below averages for member countries of the Organisation for Economic Co-operation and Development. There is a need, therefore, to engage in policy reform that helps the education system produce a highly skilled and competent labour force.

In the health sector, the low quality of primary care services and the problem of non-communicable diseases (NCDs) remain major challenges. It is important to strengthen primary healthcare services to provide increased screening, early identification, and early treatment of NCDs through multidisciplinary teams, as well as to provide effective prenatal, postnatal, and child care consultations.

Trinidad and Tobago faces structural constraints to becoming a competitive and diversified economy. According to the World Economic Forum's latest Global Competitiveness Report, Trinidad and Tobago ranks 83rd out of 137 countries. To improve competitiveness, the country needs to tackle crime and violence. Murder rates have been continuously on the rise over the past four years. There were 494 murders in 2017, up from 403 in 2014. With 60 killings, January 2018 was the bloodiest month in the history of the country. Furthermore, Trinidad and Tobago needs to improve its institutional and macroeconomic framework, including by instituting measures to facilitate the ease of doing business. For instance, according to the World Bank's latest Doing Business Report, it takes 1,340 days to enforce contract conditions in Trinidad and Tobago. Labour market efficiency is also considered a constraint, especially in terms of the relationship between employers and employees, where Trinidad and Tobago is ranked 136th out of 137 countries in the Global Competitiveness Report. Furthermore, rigidities in public-private sector coordination to develop industries outside the energy sector prevent a deep diversification of the product space.

Conclusion

Trinidad and Tobago faces macroeconomic challenges and structural constraints, but has shown a commitment to solve difficult development problems. In the short term, Trinidad and Tobago needs to continue with fiscal consolidation to stabilize public debt. Medium-term constraints – such as public sector governance, competitiveness, and diversification – prevent the country from raising growth prospects. The authorities, however, have shown a willingness to engage in critical reforms. For instance, the latest budget statement includes a host of measures on both the expenditure and revenue side to reduce the budget deficit. Furthermore, the country has shown the ability to solve difficult commitment problems. In 2007, the authorities introduced the Heritage and Stabilization Fund, a mechanism to cope with energy revenue volatility and to provide for future generations. Finally, when facing difficulties, the government has been willing to cooperate with international partners to make use of their knowledge and financial resources.

Rising incomes…

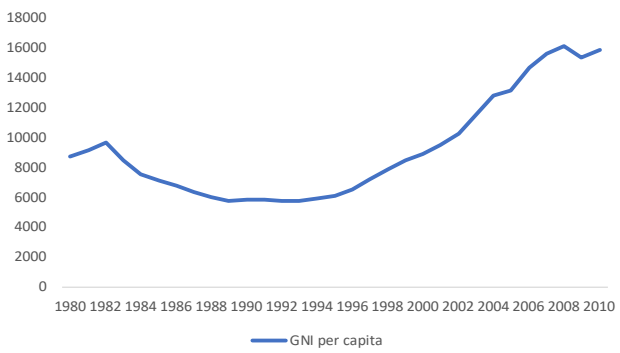


Figure a: GNI Per Capita (2010 constant U.S. dollars)

… have led to social development gains.

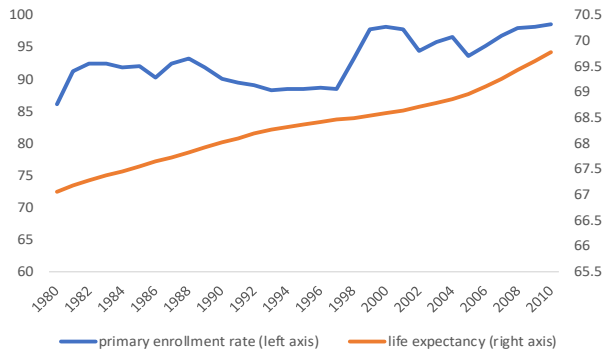


Figure b: Primary enrolment Rate and Life expectancy

Volatility in the energy sector…

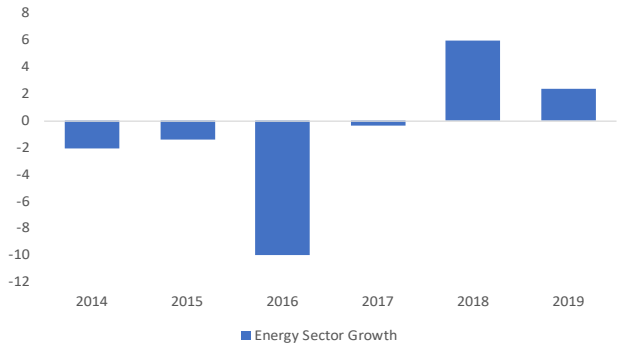


Figure c: Energy sector growth (percent)

… has a large impact on overall economic growth.

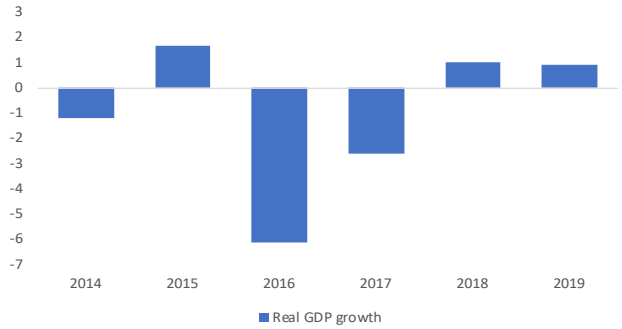


Figure d: Real GDP Growth (percent)

Trinidad and Tobago faces stuctural development challenges…

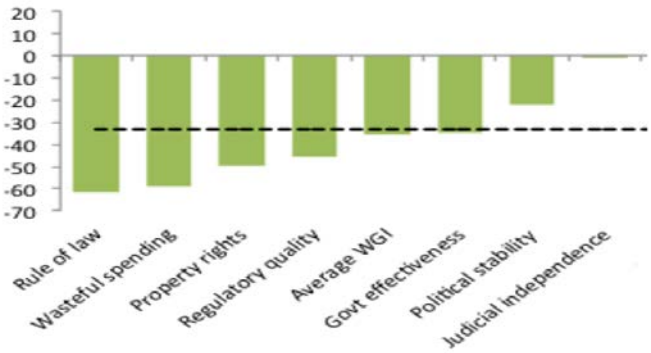


Figure e: Structural Development Challenges

… but has shown commitment to act when needed.

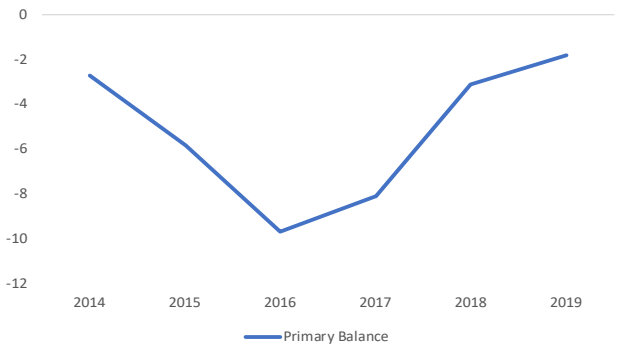


Figure f: Primary Balance (percent)

Sources: World Bank; International Monetary Fund; and Inter-American Development Bank.

Contributors: Kimberly Waithe, Juan Pedro Schmid, and Zubin Deyal

Overview[1]

The Organisation of Eastern Caribbean States (OECS) shares an institutional framework with a common monetary policy and coordinated fiscal policy.[2] The combined GDP of the region stood at around US$6.7 billion in 2017, while representing a relatively small population that ranges from approximately 57,000 in St. Kitts and Nevis to 176,000 in St. Lucia. The region faces key challenges, including being highly dependent on one highly volatile sector – tourism – along with limited fiscal space and frequent natural disasters. In contrast, these countries have achieved successes in social outcomes, particularly education and health.

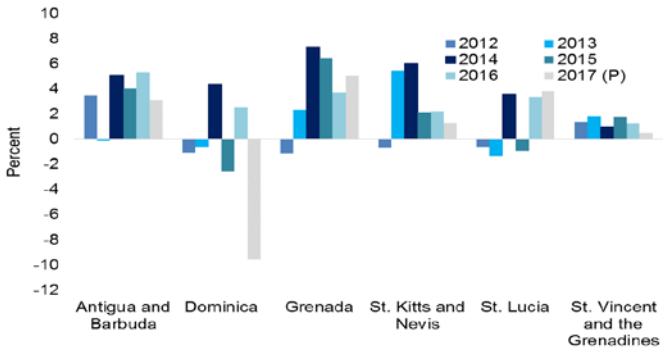
Recent Economic and Social Trends

The islands of the OECS have experienced mixed economic performances. The region saw robust growth during 2000–2007, averaging 3.7 percent annually. However, the immediate impact of the 2008 global financial crisis led to a decline in economic activity by 4.4 percent in 2009, followed by modest growth that averaged 1.3 percent annually over 2010–2017. This outturn was buttressed by a mixture of factors, including weak demand and a reduction in the competitiveness of the tourism industry, volatile international fuel and commodity prices, and natural disaster shocks. Data from the Eastern Caribbean Central Bank (ECCB) indicate that, on average, output for the region slowed from 3.1 percent in 2016 to 0.7 of a percent in 2017. On a country basis, three of the six countries recorded robust economic activity, while Dominica saw a contraction of 9.5 percent in 2017, following the adverse effects of that year's hurricane season (Figure 1). Growth in Grenada, Antigua and Barbuda, and St. Lucia reached an estimated 5.1 percent, 3.1 percent, and 3.8 percent, respectively, due to positive performances in the tourism and construction sectors. In contrast, moderate growth was registered in St. Vincent and the Grenadines (0.5 of a percent) and St. Kitts and Nevis (1.3 percent). The outturn in St. Vincent and the Grenadines was in part attributed to a notable decline in the hotels and restaurants sector (18 percent), while St. Kitts and Nevis saw a decrease in value-added contributions in the manufacturing (6.5 percent) and wholesale and retail trade sectors (6.1 percent).

Highlights

- *The OECS region has achieved high GDP per capita growth, despite frequent natural disasters that have affected economic activity.*
- *Firms are having difficulties accessing adequate levels of financing, along with limited access to qualified labor.*
- *The OECS has made important achievements in social outcomes through significant public investment.*

Figure 1. Economic Growth in the OECS Region



Source: Eastern Caribbean Central Bank (ECCB).

The OECS region is ranked relatively well across social indicators. The United Nations Development Programme's 2016 Human Development Report places the islands in the OECS region in the high human development category. Among the OECS countries, Antigua and Barbuda ranked highest, at 62nd out of 188 countries. This was followed by St. Kitts and the Nevis at 74th, while St. Vincent and the Grenadines recorded the lowest ranking at 99th. Public expenditure on health and education remains a priority in the national budgets of OECS countries despite constrained fiscal space, reaching around 3.4 percent and 4.7 of GDP in 2014, respectively, which is on par with the average in Latin American and Caribbean countries. While data on social indicators are limited in the region, estimates highlight that poverty and unemployment levels, particularly among women and youth, remain high.

[1] This bulletin focuses on developments in the independent member 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.

[2] The main findings of this analysis are drawn from the IDB publication *Together for Prosperity in the OECS: Growth, Development, and Adversity in Small Island Developing States.*

Medium-Term Economic and Social Outlook

Modest economic growth is expected for 2018, when real GDP in the OECS region is expected to increase marginally to 1.1 percent, compared with 0.7 of a percent a year earlier. The ECCB forecasts that the economy of Dominica will contract by 6.4 percent in 2018. However, reconstruction efforts are expected to bolster growth in the medium term. At the same time, although Barbuda also sustained substantial damage due to weather-related shocks, the twin-island nation of Antigua and Barbuda is expected to rebound to record growth of 3.9 percent at the end of 2018, primarily as a result of tourism and construction activities. For the other island nations in the region, economic growth is estimated to range from 1.2 percent in St. Vincent and the Grenadines to 3.2 percent in Grenada at the end of 2018. Consumer price inflation is expected to increase moderately in 2018, in line with the pick-up in international oil and food prices.

While fiscal performance is expected to vary in the region over the medium term, an overall fiscal surplus is expected for Grenada (2.5 percent of GDP), as the country continues to benefit from fiscal, structural and institutional reforms that were implemented during its International Monetary Fund (IMF) programme. St. Kitts and Nevis could witness a lower surplus, partly due to reduced Citizenship by Investment Programme inflows. In contrast, St. Vincent and the Grenadines could see a weaker fiscal outturn in light of fiscal measures announced in the 2018 budget, including higher spending for health and law enforcement services.

The region's indebtedness has been impacted by sustained primary deficits, higher interest rates, and weak GDP growth. Between 2010 and 2014, all OECS countries except for St. Kitts and Nevis had overall fiscal deficits, which drove debt accumulation. Moreover, natural disasters have contributed to increased borrowing during reconstruction periods. Data from the IMF's April 2018 *World Economic Outlook* indicate that only St. Kitts and Nevis and Grenada will see declining debt trends, with debt-to-GDP ratios projected at 60 percent and 64 percent in 2018, respectively. The trends in these two countries resulted in part from fiscal, structural, and institutional reforms under their respective IMF programmes. On the other hand, debt-to-GDP ratios in the other countries are projected to range from 74 percent in St. Lucia to 90 percent in Dominica over 2018–2019, well above the 60 percent target set by the ECCB. As such, the OECS region requires greater fiscal effort by adopting suitably designed fiscal rules, improving efficiency in revenue collection, and implementing fiscal responsibility legislation where needed to help in achieving the debt target. At the same time, revenues from Citizenship-by-Investment Programmes could be used to reduce public debt levels, where necessary. Reducing expenditure, particularly with respect to the public sector wage bill that accounts for a large portion of budgetary resources, would be key for fiscal consolidation.

Risk Factors

The region faces a number of downside risks that can affect its outlook over the medium term. First, the OECS region remains vulnerable to shocks in its main tourism source markets, particularly the United States, United Kingdom, and Canada. Second, frequent disasters, particularly hurricanes, have taken a toll on economic activity and forced reconstruction costs in countries with limited fiscal space. It is estimated that the OECS accrued US$1.6 billion in total damages due to weather-related shocks between 2004 and 2016. Third, increasing commodity prices along with the continued negative implications of Brexit for tourism and trade, pose a challenge to the region's medium-term outlook. Fourth, while some member countries continue to benefit from their Citizenship by Investment Programmes, a reduction or sudden stop in flows could have an adverse impact on planned construction projects, as well as on overall economic activity. Finally, the region is faced with high unemployment and poverty levels, and has low rankings on several indicators of the World Bank's Doing Business indicators.

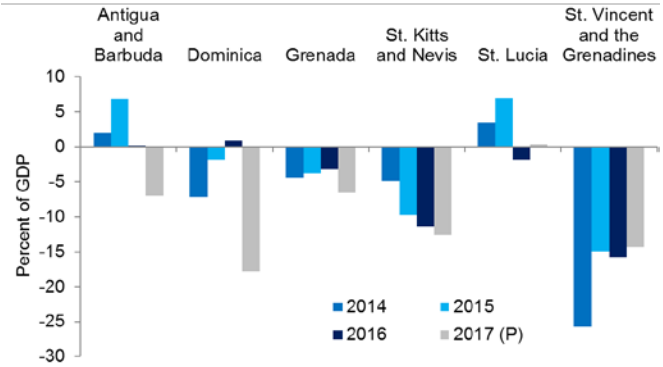
Development Constraints

The OECS countries' vulnerability to external shocks makes their growth highly volatile. The region is vulnerable to climate change and natural hazards, particularly in light of limited fiscal buffers to address frequent natural disasters. Moreover, the OECS is susceptible to fluctuations in external markets, primarily in tourism and oil. The tourism industry is the main engine of growth, fuelling employment and with spill-over effects into the other sectors. Data from the 2018 World Tourism Council Report suggest that tourism employs over half of the labour force in St. Lucia, 46 percent in Antigua and Barbuda, 34 percent in Dominica, and about a 25 percent in each of the other Eastern Caribbean islands.[3] However, with its heavy reliance on tourism, the OECS has become economically dependent on a few source markets (United States, United Kingdom, and Canada),

[3] This represents the total contribution of travel and tourism to employment, including jobs indirectly supported by the industry.

which makes it vulnerable to external growth shocks. At the same time, the region has a heavy reliance on imports, especially food and oil, which makes it susceptible to fluctuations in global commodity prices and has contributed to wider current account balances (Figure 2). Actions to build resilience, diversify economies, and mitigate the negative impact of climate change and natural disasters would be beneficial to growth.

Figure 2. Current Account Balances (percent of GDP)



Source: International Monetary Fund, World Economic Outlook Database, April 2018

Poverty and unemployment rates are elevated in the OECS region. Poverty levels remain high in the OECS, ranging from 18 percent in Antigua and Barbuda to 38 percent in Grenada.[4] Moreover, limited available data suggest that unemployment has been on the rise in the region, particularly after the global financial crisis, reaching 24 percent in St. Lucia and around 23 percent in St. Vincent and the Grenadines and Grenada in 2015.[5] At the same time, youth unemployment is considerably high, with estimates of around 40 percent in St. Vincent and the Grenadines and St. Lucia.[6] Improving the link between wages and productivity, including through civil service reform, could help address structural unemployment.

The OECS has had success in achieving specific health objectives, but challenges remain. Health remains a priority sector in the national budgets of the region. As a share of government expenditure, health expenditure ranged from around 6.5 percent in St. Kitts and Nevis to 14.9 percent in Antigua and Barbuda. Moreover, the OECS has low mortality and infant mortality rates that are better than the average for upper-middle-income countries. However, along with low mortality rates, the region has seen a reduction in fertility rates and an increase in life expectancy. High life expectancy and low fertility rates imply that the region has aging populations that will require more care and are costlier for the health sector.

Challenges remain in health with respect to nutrition and the control of non-communicable diseases (NCDs). The region has witnessed an increase in obesity, particularly among children, while water-borne infectious diseases still affect segments of the population. In 2015, Dominica had the highest level of obesity at around 38 percent of males and 65 percent of females. Similarly, obesity rates among females in St. Lucia stood at around 57 percent. At the same time, the incidence of Non-communicable diseases (NCDs) has been rising over time, and chronic NCDs (such as cerebrovascular diseases, heart disease, cancer, and diabetes) have become the leading causes of death (Table 1). The rise in NCDs places a financial strain on the public healthcare system and affects lower-income households more adversely, as there is already a heavy reliance on out-of-pocket payments. The public healthcare system will require investment over the medium term to manage the expected growth in demand for NCD care.

Table 1. Causes of Mortality, 2015 (per 100,000 population)

	Mortality Rates by Broad Cause Groups		Selected Cause-of-Death Rates			
	Communicable Diseases	Non-communicable diseases	Diabetes Mellitus	Isquemic Heart Diseases	Cerebrovascular Diseases	Breast Cancer
Antigua and Barbuda	85.0	517.1	48.9	52.8	49.1	31.4
Dominica	94.1	521.3	42.5	41.5	47.9	16.9
Grenada	131.8	752.4	97.5	79.5	78.0	38.3
St. Kitts and Nevis	44.6	496.3	55.8	50.3	73.3	34.2
St. Lucia	75.2	535.6	61.0	45.0	61.5	16.2
St. Vincent and the Grenadines	107.3	588.8	58.1	78.4	66.6	21.6
OECS average	89.7	568.6	60.6	57.9	62.7	26.4
Latin America and the Caribbean	78.9	453.2	45.3	66.0	43.1	14.1

Source: Pan American Health Organization, Core Indicators, *Health Situation in the Americas 2017.*

The quality of education remains a challenge in the region. Apart from the health sector, budget allocations for education in the region were protected, averaging 4.2

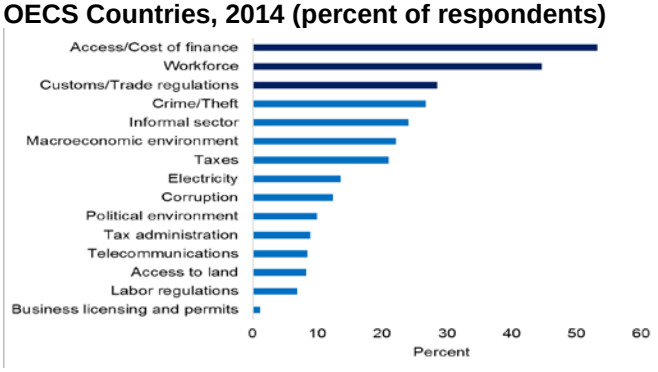
[4] Caribbean Development Bank, "The Changing Nature of Poverty and Inequality in the Caribbean: New Issues, New Solutions," May 2016.
[5] "IMF, Eastern Caribbean Currency Union, 2017 Discussion on Common Policies of Member Countries." Press Release and Staff Report, IMF Country Report No. 17/150, June 2017.

[6] Source: World Development Indicators, Unemployment, youth total (percent of total labor force ages 15-24) (modeled ILO estimate).

percent of GDP during 2005–2014. With free access to compulsory primary and secondary education, gross enrolment rates remain near 100 percent. However, literacy and numeracy remain significant challenges, as a significant proportion of secondary school students are graduating without the minimum qualifications to move to the tertiary level. OECS citizens who are 25 years of age and older have 8.4 years of formal education. This is below average when compared to international standards and lower than the 11 years of formal education in developed countries. At the same time, OECS students tend to have lower educational attainment, despite low student-teacher ratios, which are on par with developed countries. Moreover, as students move to higher levels of education, males tend to drop out at a faster rate and females record higher completion rates. Strengthening the quality of the education system is crucial to address low transition and high repetition rates.

Firms in the region have faced a number of constraints that have impacted their overall performance. Firms in the OECS are challenged by diseconomies of scale, low productivity, high emigration rates, and limited regional linkages. Supply-side constraints have kept firms in the region smaller, older, and locally owned. The average business in the OECS is 22 years old, which is above the average of the C6 countries (20 years) and the rest of the small economies of the world that are tourism-dependent (ROSE-T) (17.6 years).[7] Moreover, the average firm in the region tends not to export, while innovation among firms is limited. In Compete Caribbean's 2014 Productivity, Technology and Innovation in the Caribbean (PROTEqiN) Survey, firms reported that the main obstacles to their operations were access to and the cost of finance,[8] and limited access to qualified labour (Figure 3). Taken together, these constraints on the supply side have influenced firms' profiles.

Figure 3. Main Obstacles to Firm Operations in the OECS Countries, 2014 (percent of respondents)



Source: Compete Caribbean

Although the OECS has relatively strong governance indicators, there is room for improvement with respect to doing business. Apart from government effectiveness, the region outperforms similar small, open economies with respect to governance indicators (see Figure e in the Snapshot of the Economy). However, rigidities in the business climate persist in many OECS countries. The rankings of countries in the region on the World Bank's 2018 Doing Business Indicators ranged from 91st (St. Lucia) to 142nd (Grenada) out of 190 countries. Challenges accessing credit and weak insolvency frameworks remain major impediments to doing business, and the OECS countries are ranked below the ROSE-T and C6 countries in these areas (see Figure f in the Snapshot of the Economy). Strengthening institutions and implementing reforms to address the shortfalls in doing business should be a priority.

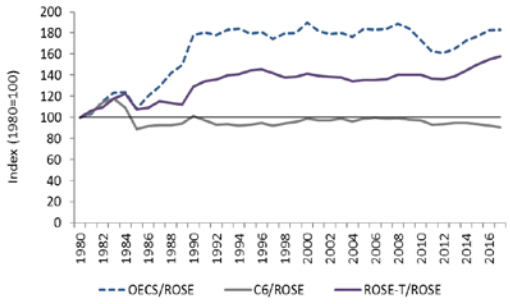
Conclusion

Medium-term challenges remain for the OECS countries. With modest economic growth expected over the medium term, considerable fiscal effort is required to address recurring fiscal deficits and high debt levels. Implementing policies and structural reforms to reduce vulnerabilities, improve resilience, and enhance growth prospects is key going forward. Maintaining the region's strong social achievements, particularly in health and education, should also be a priority. Social policies should seek to address the high prevalence of non-communicable diseases and improve the quality of education. Further, good governance in the region should also be complemented by business environment improvements.

[7] The C6 is comprised of The Bahamas, Barbados, Guyana, Jamaica, Suriname, and Trinidad and Tobago.
[8] In 2014, 37 percent of firms identified access to finance as the major impediment, which is an increase over the 25 percent reported in 2010.

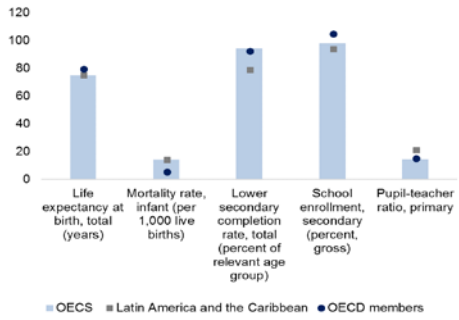
The OECS achieved high per capita growth…

Figure a. Per capita income, 1980-2017 (Index: 1980=100)



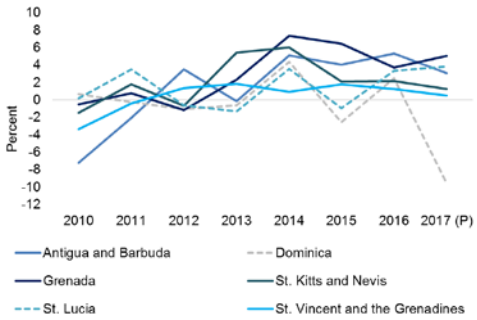
…as well as successes in social outcomes.

Figure b. Social Indicators



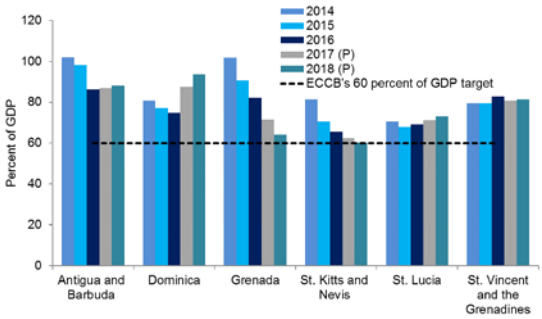
However, real GDP growth is weak among some countries...

Figure c. Real GDP growth (percent)



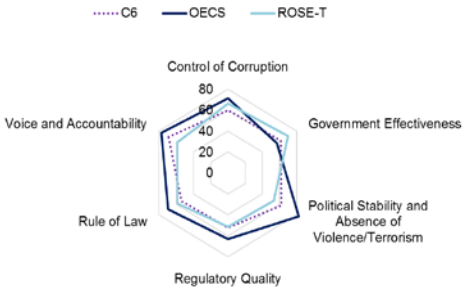
…and debt continues to remain elevated.

Figure d. Central Government Debt (percent of GDP)



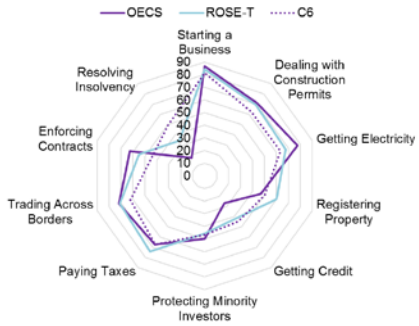
While the OECS ranks relatively well across governance indicators…

Figure e. Governance/Institutions Indicators, 2016



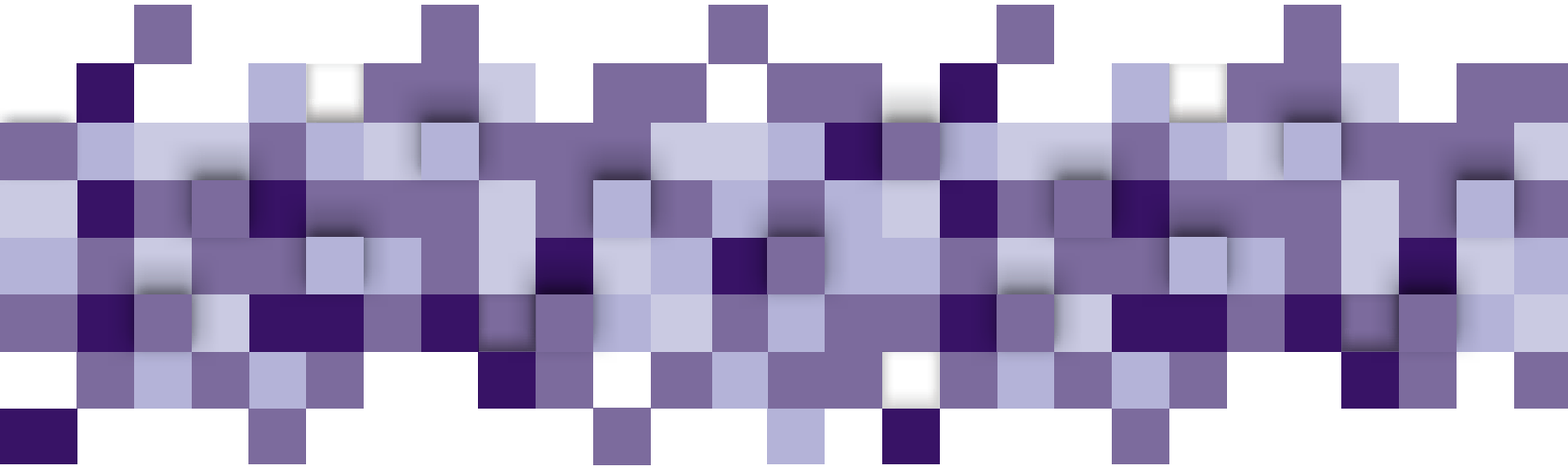
…there is room for improvement with respect to the business climate.

Figure f. Doing Business Indicators, 2018



Sources: Eastern Caribbean Central Bank; International Monetary Fund, April 2018 *World Economic Outlook*; and World Bank, World Governance Indicators, and Doing Business Indicators, 2018

Notes: (P): projected; C6: The Bahamas, Barbados, Guyana, Jamaica, Suriname, and Trinidad and Tobago; ECCB: Eastern Caribbean Central Bank; OECS: Organisation of Eastern Caribbean States; ROSE-T: rest of the small economies of the world that are tourism-dependent.



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