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**PRELIMINARY OVERVIEW OF CARIBBEAN ECONOMIES
2004-2005**

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Executive summary

The Preliminary Overview of Caribbean Economies analyses the macroeconomic performance of a selected subset of Caribbean countries for 2004 and examines the prospects for 2005.¹ The report comprises two sections. The first provides a regional overview of the economic performance and also focuses on relevant current issues. The issues addressed include the macroeconomic pattern of natural disasters and the current state of the Caribbean Community (CARICOM) Single Market and Economy (SME) integration process. The second provides a country-by-country account of the economic performance for 2004. The analysis focuses on the main trends, the fiscal and monetary regime, sectors of economic activity, prices, employment and the external sector.

In 2004, Caribbean countries were able to maintain the growth momentum of the previous year reaching a rate of growth of 3.5% on average (3% for 2003). Mining, tourism and the construction sectors were the drivers of economic growth. Mining benefited from favourable external conditions. Tourism witnessed the levelling out of the 11 September 2001 effects. Finally, the construction sector benefited both from public and private sector initiatives as a result of the recovery and rehabilitation activities that take place following natural disasters.

Natural disasters ravaged the Caribbean region affecting, within the CARICOM bloc, The Bahamas, Dominica, Grenada, Jamaica, Saint Lucia and St. Vincent and the Grenadines. Grenada was hit the hardest and sustained damage equivalent to more than twice its nominal Gross Domestic Product (GDP). Partly as a consequence of the impact of natural disasters, CARICOM countries have decided to extend the transition period for the implementation of the SME. As it stands the economic union is expected to be fully operational by 2008.

The fiscal policy stance was mixed. While some countries adhered to the principles of orthodox finance, others used government expenditure to propel short-term economic growth. The fiscal position of the countries affected by natural disasters deteriorated as these were faced with unforeseen expenditures.

The current account position did not witness significant changes and was influenced by conflicting trends. On the one hand, a higher import bill due to the increase in oil prices and declining terms of trade for agricultural products hastened the existing external gap. On the other hand, the improved terms of trade for mining exports and the widening of the surplus of the non-factor service account had the opposite effect on the external imbalance.

Monetary policy actions were conducive to growth and central banks allowed the process of economic recovery to take its course intervening only on counted occasions. The focus of policy was to facilitate, when possible, the decline in interest rates to stimulate the rate of economic expansion.

¹ The countries included are The Bahamas, Barbados, Belize, Guyana, Jamaica, the OECS member States, Suriname and Trinidad and Tobago.

In 2005, the orientation of economic policy is unlikely to change. The main challenges will be to ensure that the debt stock follows a sustainable path over time, to guarantee that reconstruction efforts in natural disaster affected countries work towards promoting long-term development and to tackle the increase in oil prices in such a way as to avoid unwanted rates of inflation or unwarranted rates of economic growth.

I. REGIONAL OVERVIEW

1. The economic performance in 2004

In 2004, Caribbean economies remained on the growth path of the previous year (3.0% and 3.5% for 2003 and 2004, on average) (see Table 1 below).² Most economies expect to maintain the current rates of expansion for 2005.

Belize, Trinidad and Tobago, and three Organisation of Eastern Caribbean States (OECS) member countries (St. Kitts and Nevis, Saint Lucia, and St. Vincent and the Grenadines) registered rates of growth within the boundary of 6% which were also the highest within the Caribbean region.

Antigua and Barbuda, Belize, Saint Lucia and St. Vincent and the Grenadines benefited from the expansion of internal demand as a result of the rise in capital expenditures. For its part, as in the past, Trinidad and Tobago's growth was determined by the robust performance of the energy sector.

The economic performance of Dominica, Grenada, and Jamaica was affected by the impact of Hurricane Ivan on their productive sectors. The Bahamas was also hit by two hurricanes, Jeanne and Frances, but was able to bounce back rapidly registering a rate of growth above that for 2003.

**Table 1
GDP growth
1980-2004**

	1981-1990	1991-2001	2002	2003	2004^a/
Antigua and Barbuda	6.1	3.4	2.1	5.5	4.0
The Bahamas	...	1.8	2.3	0.2	1.3
Barbados	1.1	0.9	-0.5	2.2	3.0
Belize	4.5	4.9	4.4	4.4	6.0
Dominica	4.4	2.4	-5.1	1.0	2.0
Grenada	3.5	3.5	-0.4	5.7	-1.4
Guyana	-2.9	4.7	1.1	-0.6	1.5
Jamaica	2.2	0.7	1.1	2.3	1.9
St. Kitts and Nevis	5.8	4.1	-0.3	0.6	5.7
Saint Lucia	6.8	1.4	0.4	3.7	5.1
St. Vincent and the Grenadines	6.5	3.0	1.7	3.6	5.8
Suriname	0.5	1.0	3.0	5.6	4.0
Trinidad and Tobago	-2.6	2.7	2.7	4.1	6.2
Average	3.0	2.7	1.0	2.7	3.5

Note: a/projected.
... denotes not available.
Source: On the basis of official information

² The analysis of the preliminary overview includes the following Caribbean countries, The Bahamas, Barbados, Belize, Guyana, Jamaica, the OECS Member States, Suriname and Trinidad and Tobago.

At the sectoral level, tourism, energy and mining and the construction sector were the drivers of economic growth.

Tourism (10% and 9.0% in 2003 and 2004, respectively)³ benefited from the return to normalcy of passenger arrivals following the impact of 11 September 2001 events. Other contributing factors included the expansion in the capacity of tourist accommodations in some Caribbean countries, the increasing number of yacht calls and the appreciation of the Euro against other currencies, including the United States dollar. When decomposed by country of origin and type of visitor the available evidence shows that the bulk of the number of visitors are cruise ship passengers from Great Britain.

The energy and mining sectors (5.1% and 8% in 2003 and 2004, respectively) were favorably affected by the upward trend in international prices, foreign direct investment and also in the case of the latter by the expansion of productive capacity.

The performance of both sectors had positive spill-overs on the evolution of the construction sector (4.2% and 10% in 2003 and 2004, respectively). The sector was also boosted by the reconstruction and recovery activities of natural disasters and, in some cases, by public investment programmes. Public expenditure contributed, as in the cases of Saint Lucia and St. Vincent and the Grenadines, to expand aggregate demand and promote growth.

Agriculture (-4.2% and -2.4% in 2003 and 2004, respectively) and manufacturing (0.5% and 2.3% in 2003 and 2004, respectively) exhibited the worst performance. Agriculture remained on the decline as a result of the deterioration of the terms of trade for traditional export products, the negative impacts of natural disasters and low productivity conditions. Manufacturing stagnated in most cases reflecting its long standing structural problems characterized by high costs, low productivity, and inadequate technological levels.

At the regional level fiscal policy was expansionary.⁴ On average, the fiscal stance rose from 33% to 45% of GDP. This contrasts with the explicit policy of fiscal restraint adopted by most countries in the previous year.⁵ Nonetheless, the experience at the country level was mixed.

³ The sectoral rates of growth refer to regional averages.

⁴ The fiscal stance is defined as government expenditure divided by the tax ratio (tax revenue over GDP). Formally,

$$(1) \text{ FS} = G / (T/GDP)$$

Where,

FS = fiscal stance

G = government revenue

T = total tax revenue

GDP = Gross Domestic Product

When the fiscal stance is neutral, that is when tax revenue covers government expenditure, $G=T$ and the fiscal stance is equal to GDP ($FS=GDP$). The fiscal stance is said to be expansionary when $G>T$ and $FS>GDP$. It is restrictive if $G<T$ and $FS<GDP$. The deviation between the fiscal stance and GDP as a percentage of GDP provides an indication of the extent to which fiscal policy deviates from a neutral stance. Source: W. Godley and FD. Cripps.(1983) *Macroeconomics* (New York: Oxford University Press).

⁵ OECS economies have three different fiscal years. Dominica's fiscal year starts in July and ends in June. The fiscal year in Anguilla, St Kitts and Nevis and Montserrat coincides with the calendar year. The rest of the economies have

Some countries maintained their commitment to reducing the fiscal deficit and managed to achieve their objective mostly on the basis of higher revenue growth and through the implementation of measures to widen the tax base and to a lesser extent through expenditure reduction. The countries in this group include Antigua and Barbuda, Barbados, Dominica, Guyana St. Kitts and Nevis, Trinidad and Tobago.

A second group of countries (Saint Lucia, St. Vincent and the Grenadines and Suriname) opted to use public expenditure as a leverage tool to manipulate aggregate demand or to respond to pressing social needs. Finally, a third group of countries (The Bahamas, Grenada and Jamaica) witnessed a deterioration in their fiscal position as a result of the rise in expenditure and decline in tax brought about by the effects of natural disasters. Within this group Jamaica managed, in spite of the increase of the fiscal imbalance from 3.8% to 4.2% of GDP, to remain within the fiscal target announced by the authorities at the beginning of the fiscal year.

The current account did not exhibit significant changes and remained roughly at the level of the previous year (11% of GDP for the regional average). The merchandise imbalance widened in most cases due to the increase in import growth as a result of the rise in oil prices and to a lesser extent due to the purchase of raw materials, intermediate and final consumption goods by countries affected by the hurricanes. At the same time, the behaviour of exports was affected by two opposing tendencies, the improvement of the terms of trade for bauxite, alumina, gold and oil and the deterioration of the terms of trade for sugar, bananas, and other traditional agricultural products.

The merchandise disequilibrium was financed in part by foreign exchange flows associated with non-factor services transactions, mainly travel, and foreign direct investment. In the case of countries affected by natural disasters, official and insurance (re-insurance) flows also contributed to narrow the gap. Barbados, Belize, and Guyana witnessed a decline in their stock in their international reserves. Jamaica, The Bahamas and Trinidad and Tobago registered the opposite result.

The monetary authorities did not allow the variations in international reserves to hamper the process of economic recovery. The monetary authorities used open market operations and quantitative instruments to offset declines in international reserves, as in the case of Belize. When the decline in international reserves occurred in a context of high liquidity (such as Barbados or Guyana) the monetary authorities did not intervene. Finally, lower interest rates followed the expansion of reserves to stimulate the demand for loans (Jamaica and Trinidad and Tobago).

a fiscal year that runs from April to March. The Eastern Caribbean Central Bank (ECCB) reports the fiscal accounts on a calendar year basis to make these accounts comparable.

2. The macroeconomic pattern of natural disasters

During the year natural disasters ravaged the Caribbean region underlining once more the vulnerability of Small Island Developing States (SIDS). The Bahamas, Grenada, Saint Lucia, St. Vincent and the Grenadines, Jamaica, the Cayman Islands, the Dominican Republic and Haiti were hit in different degrees by hurricanes. Total estimates amount to more than US\$2.2 billion.

Disaster damage is classified into direct and indirect. The former refers to the damage occurring at the time of the disaster and which is inflicted on immovable stocks and assets. Indirect damage refers to flows of goods and services and income. In this case, the damage results as a consequence of the interruption of production and distribution processes from the moment the disaster occurs. It can be defined as the sum of the value of income foregone (due to the interruption of production and distribution as a consequence of the natural disaster) and the increase in costs and expenditure to confront the damage of the disaster. In the case of the Caribbean the cost of the direct damage surpassed that of the indirect damage (see Table 2).

Table 2 Natural disasters in the Caribbean in 2004						
Country	Event	Date	Magnitude	Direct damage as % of GDP	Indirect damage as % of GDP	Total damage as % of GDP
The Bahamas	Hurricane	September	240 and 160 km/ph	4	3	7
Grenada	Hurricane	September	145 mph	213	26	239
Jamaica	Hurricane	September	180 km/ph	5	3	8
Dominica	Earthquake	November	6.0 Richter scale	13	4	17
Haiti	Tropical storm	November	...	5	3	8

Note:
 Direct damage refers to the value of damage to immovable assets and stocks at the time of the disaster.
 Indirect damage refers to the value of income flows lost as a result of the impact of the disaster on stocks and assets. The earthquake in Dominica measured 6.0 on a Richter Scale. In Grenada the winds provoked by the Hurricane reached 145 miles per hour. In the case of Jamaica, the strong sustained winds reached 180 kilometres per hour as the hurricane passed closest to the island. In the case of the Bahamas, Hurricane Frances reached a wind force of 240 km/ph and Hurricane Jeanne reached 160 km per hour. Mi/ph and km/ph = miles and kilometers per hour.
 ... denotes not available.
 Source: ECLAC and OECS (2004).

The damage assessment studies undertaken by ECLAC and the OECS have shown, once again, that hurricanes have a definite economic and more precisely macroeconomic pattern in terms of their impact and effects. The key factor that explains the pattern is the seasonality of the disaster, that is, the time of year at which the disaster occurs.

When the disaster occurs in the second half or latter part of the year, as has been the case in the Caribbean, the effects include in general:

- (a) A decline in GDP growth in the year during which the disaster occurs. The decline is commensurate to the magnitude of the event;
- (b) A quick but less sharp recovery in GDP growth in the post-disaster year;
- (c) The level of GDP growth, however, remains below that which it would have been without the disaster;
- (d) An increase in the budget deficit. This results from the combination of higher expenditure incurred by the government as a result of reconstruction and recovery efforts and lower tax revenue;
- (e) A widening of the current account disequilibrium. This results from the decline in export as a result of the damage of the disaster to productive sectors and the increase in imports due to the reconstruction and recovery needs and the replacement of lost production;
- (f) A jump in the rate of growth of the construction sector in the year in which the disaster occurs. The construction sector can level off or remain poised for continued growth depending on the magnitude of the disaster.

These effects are most clearly illustrated in the cases of Grenada and Jamaica (see Table 3). Both of these economies witnessed a decline in GDP growth. As expected and relative to the inflicted damage, the drop was much sharper in the case of Grenada than in Jamaica. Both economies are expected to exhibit a recovery in 2005. The fiscal and external gaps widened in the year of the disaster due mainly to greater than planned expenditure for rehabilitation purposes. Grenada also witnessed a significant decrease in tax revenues. In the case of Jamaica, the tax intake is not expected to be affected since the hurricane did not impact the activities or geographical zones that generate most of the tax collection. The construction sector acted both as a buffer stock for the decline in economic activity in the year of the disaster and as linchpin for growth in the post disaster year.

Table 3
Macroeconomic patterns of natural disasters

Country	Previous year, disaster year and after disaster year	GDP growth	Fiscal deficit as percentage of GDP	Current account deficit as percentage of GDP	Construction sector growth
Grenada	Previous year	5.7	4.9	33	29
	Disaster year a/	4.7	4.8	37	12
	Disaster year b/	-1.4	12	40	15
	After disaster year	-0.9	10
Jamaica	Previous year	2.3	5.9	12	1.2
	Disaster year a/	2.6	3.8	10	2.2
	Disaster year b/	1.9	4.2	11	3.4
	After disaster year	2.2

Note: a/ Denotes the estimates in the disaster year on the assumption that the disaster would not have taken place.
b/ Denotes the estimates in the disaster year taking into account the effects of the disaster.
Source: On the basis of official information.

In the cases of Saint Lucia and St. Vincent and the Grenadines, the disaster affected mostly the agricultural harvest. However, no figures have been released regarding the impact on GDP growth, government finances and the external sector.

The Bahamas represents, to some extent, an exception to the macroeconomic pattern described above as the economy registered an expansion in GDP growth in the year of the disaster. Nonetheless, the country recorded an increase in its budget and current account deficit as a result of the impact of the disaster.

Two important issues related to the macroeconomic impact of natural disasters and their aftermath are the estimation of the financing gap and the orientation and purpose of the reconstruction process. Both are intrinsically related. The financing gap refers to the flows that are needed to satisfy the net expenditure requirements of the government, which include reconstruction expenditures, in order to maintain a sustainable fiscal position. The financial flows are provided by multilateral organizations and the donor community. Guaranteeing the disbursement of those funds implies not only a commitment to macroeconomic stability on the part of the authorities, but also a clear institutional and financial plan for the reconstruction phase.

Table 4
Grenada
Central government financing needs after Hurricane Ivan, 2004-2007
Percentage of GDP

	2004	2005	2006	2007
Total revenue	24.8	24.7	26.4	27.1
Tax revenues	22.8	22.8	23.8	24.4
Total expenditure	39.3	47.0	44.5	40.8
<i>Of which</i>				
Personal Emoluments	12.6	12.6	12.6	12.6
Interest payments	6.1	6.9	6.5	6.3
Capital expenditure and net lending	12.1	19.0	17.0	13.5
Financing requirements	-14.5	-22.3	-18.2	-13.7
Identified financing	14.8	20.7	11.2	7.7
Domestic	-1.6	0.0	0.0	0.0
External loans	6.2	2.4	2.8	2.9
Committed donor support	10.3	18.2	8.4	4.8
Financing gap	-	1.7	7.0	6.0

Note: Financing requirements are equal to total revenue minus total expenditure. The financing gap is equal to the difference between the financing requirements and identified financing.

Source: IMF (2004). Grenada donors' conference. Presentation on the macroeconomic outlook. November 19, 2004.

The financing gaps for Grenada and Jamaica are shown in Tables 4 and 5. The difference is commensurate with the magnitude of the disaster. The greater the devastation of the disaster the higher are the expenditures, the lower are the expected tax revenues and the greater is the financing gap. In the case of Grenada, the financing gap is expected to reach 2% of GDP for 2005 and increase thereafter to a range comprising between 6% and 7% of GDP.

In the case of Jamaica, as it stands the financing requirements are equivalent to 4.2% of GDP taking into account the effects of the disaster. The difference between the financing needs with and without the disaster is the financing gap which in this case is equal to 0.4% of GDP.

While natural disasters have similar economic effects, each one also has its own unique features. These are determined by the type of event and magnitude, the dependent/independent status, the structure of the economy affected by the natural phenomenon and the perception of the event by the authorities, the public and the international community.

In the case of Grenada, the main characteristics of the disaster are the similarity of effects, the extent of the devastation, and the social dislocation it produced. Hurricane Ivan produced damages associated with only high winds. There were no damages related to flooding or heavy rains, such as landslides. As a result, to some the effects were replicable throughout the island. The event did not

spare any part of Grenada affecting roughly 90% of the population and the damages were equivalent to more than twice the value of nominal GDP (see Table 2 above).

For Grenada and the Caribbean, Hurricane Ivan represented the biggest natural disaster in the last 20 years. As a result, the event was perceived as a major catastrophe by the international community and captured its attention. Finally one of the key aspects underpinning the social dislocation is the mismatch between supply and demand for labour produced by the hurricane. The damage to the productive sectors, especially to tourism, provoked an increase in the number of unemployed. However, for reasons that range from gender issues to absence of a particular type of work skill, these could not be absorbed into those activities (mostly related to repairs and the construction sector) that experience a boom following a natural disaster.⁶

For Jamaica the disaster did not affect the main centres of economic activity. While the damage was estimated to be equivalent to 8% of GDP it did not have a major impact on its rate of growth (see Tables 2 and 3 above). The main characteristic of the disaster was the effect it would have on creditors' perception of the capacity of the authorities to fulfil its external obligations. Thus the main issue was to prevent rehabilitation and recovery expenditures from substantially altering the target fiscal deficit and in particular the announced primary surplus.

For Dominica, the distinguishing characteristics are the environmental effects and the endogenous-exogenous shock dynamics. In the past three years, Dominica has implemented a process of economic adjustment following the onslaught of a fiscal crisis that has not thus far managed to improve the country's growth perspectives. Growth is incipient and unevenly distributed among the different sectors of economic activity.

In some cases, the effects of the earthquake (the external shock) may compound those of the adjustment programme (the internal shock) amplifying the latter's intended consequences. In others, the effects of the external shock will partly offset or run counter to those of the endogenous shock.

3. The Common Market and Single Economy

Partly as a result of the impact of the disasters on the affected economies, CARICOM governments decided at their Tenth Special Meeting to postpone the formation of the Common Market and Single Economy (CSME) from January 2005 until November 2005.⁷

⁶ Females represent 65% of the labour force in tourism. Grenada has one of the highest dependency ratios in the OECS (95%).

⁷ Tenth Special Meeting of Heads of Government of the Caribbean Community, 8-9 November 2004, Port of Spain, Trinidad and Tobago).

Table 5 Jamaica Central government operations for fiscal year 2004/2005 Pre and post Hurricane Ivan scenarios				
Budget items	Pre-Ivan scenario		Post-Ivan scenario	
	J\$ Mill.	% of GDP	J\$ Mill.	% of GDP
Revenue & Grants	174,053	30.8	174,053	30.8
Tax Revenue	156,009	27.6	156,009	27.6
Non-Tax Revenue	9,805	1.7	9,805	1.7
Bauxite Levy	2,478	0.4	2,478	0.4
Capital Revenue	2,256	0.4	2,256	0.4
Grants	3,506	0.6	3,506	0.6
Expenditure	195,419	34.6	197,689	35
Recurrent Expenditure	186,911	33.1	187,006	33.1
Programmes	28,065	5	28,160	5
Wages & Salaries	62,926	11.1	62,926	11.1
Interest	95,920	17	95,920	17
Domestic	74,270	13.1	74,270	13.1
External	21,649	3.8	21,649	3.8
Capital Expenditure	8,509	1.5	10,684	1.9
Capital Programmes	8,192	1.5	10,368	1.8
Fiscal Balance (Surplus + / Deficit -)	-21,366	-3.8	-23,636	-4.2
Primary Balance (Surplus +/ Deficit -)	74,554	13.2	72,284	12.8

Source: On the basis of information provided by the ministry of finance Jamaica (2004).

While external shocks have contributed to the delay in the implementation of the CSME, they have at the same time highlighted the importance of regional cooperation in its different facets (political, financial, civil and military). Most importantly, they have underscored the need to define with precision the type of regional cooperation that can be feasible for CARICOM. Indeed, the most fundamental question is how to articulate a regional integration process that can benefit all its member States paying particular attention to the more disadvantaged countries.

For Latin America and the Caribbean regional integration has been an enduring and incomplete process. Countries have formed regional groupings that have at most reached a level of integration

commensurate with imperfect customs unions. CARICOM is not an exception. However, it is the only regional trading bloc that has explicitly formulated the objective of forming an economic union in its treaty of establishment. A key component for its success is to define a mechanism to deal with economic disparities and asymmetries at the regional level.

Currently there are two approaches to deal with the disparities. The first is to let market forces work their way through free trade and movement of capital and narrow the disparities. Within this setting, responding to the expectation of higher returns, capital flows should flow to the country which is relatively undercapitalized and which is also, in general, the less developed region. Greater levels of investment would translate into higher levels of productivity, income and development. This would eventually lead to a process of income and growth convergence.

This is the approach envisaged in the North American Free Trade Agreement (NAFTA) and the Free Trade Area of the Americas (FTAA); in the latter case, due to the countries agreeing in the negotiations to take into account their different levels of size and development. This involves mainly the provision of a flexible, transparent, simple and easily applicable framework that takes into consideration the heterogeneity, the differing needs, the characteristics that are specific to each member, and the differences in market access among the member countries. As part of the recognition of the differences in size and development, member countries agreed on a Hemispheric Cooperation Plan (HCP) as a supporting pillar of the trade negotiations. The HCP has six objectives. These can be summarized as providing a basis, permitting countries to confront and overcome the challenges associated with trade liberalization. The HCP consists of building ‘trade capacity’ through technical assistance aimed at enabling member governments to take part in the trading negotiations and to implement the clauses and provisions of the treaty.

The second approach recognizes that a regional agreement among unequal members is bound to aggravate their existing disparities. As a result, regional agreements must have a mechanism and, more precisely, a regional policy to level the playing field among different member countries or regions. This is the approach adopted by the European Union (EU).⁸

Europe’s regional policy is one of economic and social cohesion. The policy of social articulation is carried out through structural actions. These comprise structural and cohesion funds. The

⁸ The case for regional policies can be justified using different conceptual and theoretical approaches. The ones that apply to the Caribbean case are at the microeconomic level the ‘new economic geography’ and at the macroeconomic level asymmetrical responses to economic shocks. According to the new economic geography when trade barriers and transaction costs are high firms locate near the consumer rather than near other producers. In this case firms establish themselves in countries. In the opposite case, when trade barriers and transactions costs are low, firms take advantage of larger markets and tend to agglomerate in locations with larger markets. That is they locate near other producers and benefit from pooling effects and economies of scale. In short freer markets encourage the regionalization of production.

In the first case, if labour is not fully mobile, economic agents belonging to the regions which do not benefit from agglomeration effects are condemned to see their living standards decline. Equally, their economic and social potential will be underutilized. As a result regional policies are here justified in terms of equity and efficiency considerations.

former and latter represent 90% and 10% of the total funds allocated to structural actions. The largest programme is the European Regional Development Fund (ERDF) which absorbs 58% of structural funds.⁹ Structural actions represent one third of the EU budget and for 2005-2006 are estimated at 3% of the European Union's GDP for 1999.

The disparities in regional agreements such as the EU are measured by the respective GDPs per-capita relative to the mean. The countries that are below the mean are termed 'disadvantaged.' Those exhibiting a GDP per capita above the mean are the 'advantaged' regions. The advantaged/disadvantaged threshold has changed over time. In the case of the EU the threshold was set at 90% in 1991 and then at 75% in 1999 of the average GNP and GDP for Europe

At their last meeting, CARICOM countries agreed to put in place by December 2005 the core measures of the CSME.¹⁰ These include among others, the free movement of labour and the operationalization of the Development Fund for Disadvantaged Countries, Regions and Sectors.

Regarding the former, CARICOM Heads agreed to include a wide range of categories of workers among those that have the right of free movement among CARICOM economies. Thus far the CARICOM agreement considers five categories of workers - graduates, media workers, artistes, musicians and sportspersons.

Governments also agreed to define a finance mechanism for the Development Fund for Disadvantaged Countries, Regions and Sectors by July 2005. Finally, it was agreed that the implementation of the CSME should follow a sequencing process whereby the formation of the common market should precede that of the single economy. As things stand, the CARICOM single economy is expected to be fully operational by the year 2008.

At the same time that CARICOM is gradually perfecting its time schedule for the formation of the CSME, the smaller economies (namely the OECS) are, in turn, deepening their process of economic and political union. In this sense, at the last meeting the Heads of Authority of the OECS (11-12 November 2004) decided to proceed with the reformulation of the Treaty of Basseterre (1981) and devise an institutional structure to support their expected level of integration. Two of the key elements of the new Treaty include labor mobility and a supranational legislative framework.

4. The perspectives for 2005

For 2005 the rate of growth of Caribbean countries is projected to be within the vicinity of 4% on average. Tourism, mining and construction sectors will remain the main drivers of economic growth

⁹ The others include the European Social Fund, the European Agricultural Guidance and Guarantee Fund and the Financial Instrument for Fisheries Guidance.

¹⁰ See footnote 6 above.

underpinned by greater foreign direct investment flows and in the case of mining also higher international prices.

Agriculture will reflect the effect of natural disasters on the affected economies and the deterioration of the terms of trade for traditional products. Manufacture, as in the past, will most likely stagnate.

At the country level, Trinidad and Tobago and some selected OECS economies will register rates of growth ranging from 5% to 6%. The Bahamas, Barbados, and Belize are forecasting rates of growth between 2% and 4%. Jamaica and Guyana are expecting a 2% rate of economic expansion. Grenada and Dominica are bound to record contractions in their level of economic activity.

The fiscal outlook will not witness important changes and countries will record a variety of outcomes. The focus of the fiscal stance will be the management of expenditures and, in particular, capital expenditures. These will be determined by reconstruction and rehabilitation expenditures and by choosing to use capital expenditures as a leverage to bring about fiscal equilibrium or maintain aggregate demand. Revenues will vary in line with the pace of economic activity and, in some cases (OECS member States), there will be a widening of the tax base. Finally, in at least more than half of the Caribbean countries here considered the high levels of outstanding public debt and how to ensure their sustainability over time will remain two issues of major concern.

The balance of payments outcome will mainly reflect the growth in imports as a result of the increase in the energy bill. In spite of the good performance of some mining commodity exports and of that of non-factor services as a result of the ongoing recovery of tourism, with a few exceptions (i.e., Trinidad and Tobago), the current account will be negative. Countries will continue to rely on capital flows to balance their external accounts. The prospects are thus far favourable as countries expect continuing foreign direct investment flows for the tourism sector (OECS, the Bahamas and Barbados), the mining sector (Trinidad and Tobago, Suriname) while others (Guyana, Dominica, Grenada, Jamaica) are counting on foreign aid and insurance and re-insurance flows.

The fiscal and balance of payments result will determine the monetary policy stance. Authorities expect to be able to sustain the current recovery through lower interest rates. The main challenge will be how to maintain the flexibility of monetary policy in the face of rising oil prices.

II. COUNTRY REPORTS

Member States of the OECS¹¹

1. Main trends

The OECS member States noted a process of continued economic recovery which was partly halted by two natural disasters occurring in the second half of the year. The first one, Hurricane Ivan, mainly affected Grenada and, to a lesser extent, St. Vincent and the Grenadines and Saint Lucia in early September. The second one, an earthquake, shook Dominica in late November.

Hurricane Ivan inflicted damages to agricultural crops in the case of St. Vincent and the Grenadines and devastated the economy of Grenada.

In the latter case, these amount to more than twice the current value of GDP. For Grenada, the effects of the hurricane curtailed the level of employment and caused a contraction in GDP growth (-1.4%). Most of the damage was concentrated on infrastructure and, in particular, on housing, as 89% of the housing stock registered damage (the damage to housing alone is equivalent to 1.4 times the money value of GDP). In the agricultural sector where the damage was estimated to reach 10% of GDP, Hurricane Ivan wiped out traditional crops and inflicted severe damage to tourist accommodations and yachts (41% of GDP).

Growth in the OECS as an aggregate was sustained mainly by construction and tourism. Construction benefited from the rehabilitation and recovery efforts and the prevailing macroeconomic conditions. Notwithstanding Hurricane Ivan, the OECS countries together reported significant growth in the tourism sector.

Robust growth allowed most governments to maintain a prudent fiscal stance characterized by expenditure restraint and the implementation of tax measures to boost revenue collection. Countries badly affected by natural disasters suffered deterioration in their fiscal balances.

The OECS economies witnessed an increase in their external imbalance propelled by the decline in exports compounded by import growth due to the increase in international oil prices. The deficit was financed mainly by foreign direct investment flows oriented in part to the development of the tourism sector.

¹¹ The States members of OECS include Anguilla, Antigua and Barbuda, the British Virgin Islands, Dominica, Grenada, Montserrat, St Kitts and Nevis, Saint Lucia and St Vincent and the Grenadines. The analysis here presented covers all member States with the exception of the British Virgin Islands. These States form a currency union and fall under the monetary authority of the Eastern Caribbean Central Bank (ECCB). These economies have three different fiscal years. Dominica's fiscal year starts in July and ends in June. The fiscal year in Anguilla, St Kitts and Nevis and Montserrat coincides with the calendar year. The rest of the economies have a fiscal year spanning from April to March. The ECCB reports the fiscal accounts on a calendar-year basis to make them comparable.

[INSERT TABLE 6]

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[INSERT TABLE 11]

2. Economic policy

2.1 *Fiscal policy*

In 2004 OECS member States maintained at the aggregate level the fiscal stance of the previous year which managed to decrease the fiscal deficit by restraining the growth of public expenditure. At the country level the OECS saw a mixed variety of fiscal outcomes.

Antigua and Barbuda's fiscal performance (-8.1% and -6.3% of GDP in 2003 and 2004) improved due to strong economic growth as the government passed a series of expenditure increasing measures (grants, unemployment relief programmes, and pension schemes).¹²

Dominica managed to comply with an International Monetary Fund (IMF) Poverty Reduction and Growth Facility Programme target of 4% deficit in relation to GDP. This was achieved by the reduction in tax exemptions, expenditure cuts, the extension of the retirement age for public officials and the broadening of the tax base.

Grenada's fiscal situation deteriorated following the passage of Hurricane Ivan. The deficit reached 9% of GDP as a result of extraordinary expenditures and the steep decline in tax revenue collection. The government has taken measures to streamline and reorient expenditures.

In St. Kitts and Nevis the government reduced its deficit (7% and 6% in 2003 and 2004). The authorities managed to increase the current account surplus by curtailing the growth of current expenditure and improving tax revenue collection. To this end, the government introduced tax hikes, expanded the tax base and suppressed selected tax incentives.

Saint Lucia's fiscal deficit narrowed (7% and 6% of GDP in 2003 and 2004) due to the reduction in capital expenditures (10% and 8% of GDP in 2003 and 2004). Total revenues and current expenditures maintained their shares of GDP (24% of GDP for both for 2003 and 2004). The government remains committed to the use of capital expenditures as an instrument for the control of aggregate demand.

Finally, St. Vincent and the Grenadines' fiscal position deteriorated as a result of the expansion in capital expenditures notwithstanding the implementation of a series of measures (including a rise in the airport service charge, vehicle surtax, and charges applicable to travel documents) to raise the tax revenue collection.

2.2 *Monetary policy*

OECS economies form a currency union since 1983. Its monetary unit the Eastern Caribbean dollar is pegged to the United States dollar at EC\$2.70 per US\$. The union's monetary authority, the

¹² These results hold under the assumption that part of the said fiscal measures took their effect in 2004.

Eastern Caribbean Central Bank (ECCB), acts as a quasi-currency board and is required to back by statute up to 60% of its monetary liabilities. Since the formation of the union the Central Bank has maintained a neutral monetary stance and has hardly changed its reference rate of interest.

In 2004 most OECS countries expanded their liquidity in line with the growth of nominal GDP. Total monetary liabilities expanded on average for the OECS by 13% between September 2003 and September 2004 (5%, 6% for the same period). At the country level St. Kitts and Nevis registered the highest and Dominica the lowest liquidity growth (21% and 9%).¹³

The expansion of liquidity was driven by the growth of domestic credit as the growth of net foreign assets declined for the available period (7% and 30%; 50% and 15% for 2003 and 2004, respectively). The growth in credit responded to the public and private sectors' demand for finance (28% and 6% for 2003 and 2004, respectively).

The latter represented mainly personal loans (50% of the total) related to the acquisition of property (home construction and renovation) and other personal loans. Agriculture, manufacturing, tourism, transportation and construction activities represented 5%, 3%, 2% and 5% of the total, respectively. Construction and public utilities registered the most dynamic credit growth (62% and 50%).

3. Evolution of main variables

3.1. Economic activity

The aggregate performance of OECS economies reflected the robust expansion registered by Antigua and Barbuda, St. Kitts and Nevis, Saint Lucia and St. Vincent and the Grenadines and the negative effects of the natural disasters on Grenada and Dominica.

The performance of the agricultural sector reflected unfavorable international prices, adverse climatic conditions, the uncertainty that surrounds the future status of preferential trading arrangements, and the effects of the natural disasters on the output of bananas, nutmeg and other traditional crops. It also responded to efficiency considerations.

Manufacturing stagnated due to high costs, low levels of productivity and the external and internal limitations to the expansion of output of the agricultural sector. In the particular case of Dominica manufacturing output recovered (22% in the first quarter of 2004) responding to the gradually improving macroeconomic climate.

¹³ The rates of growth in this section are given from September of one year to September of the previous year.

Construction was boosted by the high levels of liquidity prevailing in most economies, the increased public capital expenditures and also by the positive effect of recovery and rehabilitation activities following the occurrence of natural disasters.

The tourism sector witnessed a definite recovery in 2004 in most economies. Available data indicate that tourist arrivals expanded by 16%, 4% and 11% in Antigua and Barbuda, Dominica, Saint Lucia and St. Vincent and the Grenadines. In both Dominica and in particular Grenada tourism contracted or stagnated. In Grenada the sector is projected to contract by 25% reflecting the damage to the hotel plant and the damages of approximately 90% of hotel rooms.

3.2. Prices, wages and employment

The rate of inflation increased marginally (0.6% and 1.14% in 2003 and 2004) due to the rise in the international price of oil, the tax measures passed in several of the member States and the weakness of the United States dollar. The level of employment moved in line with the expansion of the economy.

3.3. Evolution of the external sector

The OECS aggregate current account registered a deficit equivalent to 22% of GDP (21% of GDP for 2003) which was financed by foreign direct investment flows and to a lesser extent by capital transfers and portfolio investment (16%, 6% and 2% of GDP, respectively).

The performance of the current account responded mainly to the widening of the merchandise balance deficit (38% and 40% of GDP in 2003 and 2004). As the services income and current account results remained in terms of GDP at the level of the previous year (20%, -7% and 4% of GDP, respectively).

The merchandise trade balance responded to the growth in imports driven by the increase in the international price of oil, the effects of natural disasters and the production needs of an expanding regional bloc. External sales were affected by the decline in the terms of trade of the main traditional export products and the effects of natural disasters on countries' export capacity. However in some countries, such as Dominica, manufactured exports showed signs of recovery in 2004 after at least three years of continued declines.

The services balance benefited from tourist investments which were prominent in Saint Lucia and St. Kitts and Nevis. In Grenada and Dominica the tourist sector experienced supply constraints resulting from the damage sustained to hotel plants, marina bays, and other tourist infrastructure. Demand constraints were also present due the suspension of visitor arrivals, mainly stay-over, as a result of the overall effects of the disasters.

The surplus in the financial account responded to foreign direct investment flows oriented to the tourism sector, capital grants to the government and higher inflows associated with insurance as a result of the damage inflicted by natural disasters.

The Bahamas

1. Main trends

The Bahamas improved its economic performance (0.2% and 1.3% in 2003 and 2004) in spite of the damage (7% of GDP) inflicted by two hurricanes (Jeanne and Frances) in the month of September. Both phenomena affected Mayaguana, Long Island, San Salvador, Rum Cay, Cat Island, Eleuthera, New Providence, the Berry Islands, Abaco and Grand Bahama.¹⁴

Tourism was the most affected sector (Bah\$109 million and 3% of GDP) and registered a slowdown from its expected rate of growth. However, its enhanced resilience allowed it to recover rapidly and sustain a high rate of growth (11%) for the current year.

The housing and transport and telecommunications sectors also suffered significant damage (Bah\$99 and 104 million). The primary sector and in particular fisheries were less affected (Bah\$45 million). For its part the construction sector rebounded as a result of the increased activities of reconstruction and rehabilitation that follow the occurrence of a natural disaster and the greater level of capital inflows associated with the development of tourism.

The fiscal deficit narrowed in FY 2004 but this trend will revert in FY 2005 due to the increase in expenditures and the contraction in revenues resulting from the impact of natural disasters on productive activities.¹⁵

The central bank eased its monetary policy and increased domestic credit to stimulate aggregate demand and economic growth. This policy provided the required financing of the budget deficit. The rate of inflation rose due to the increase in the international price of oil.

The deficit in the current account was greater than expected and was more than offset by the positive result in the capital and the financial account.

¹⁴ Hurricane Jeanne affected Abaco and Grand Bahamas most severely. Hurricane Frances struck the same geographical areas as Hurricane Jeanne but hit Grand Bahamas most severely.

¹⁵ According to the convention followed throughout this report the fiscal year is denoted by the year in which the fiscal year ends. In the particular case of The Bahamas FY2004 denotes the fiscal year commencing on 1 July 2003, running to 30 June 2004. Prices are denoted in Bahamian dollars (i.e., Bah\$), unless quoted else wise. One Bahamian dollar is equivalent to one US\$. The Central Bank has maintained a fixed exchange rate with the US\$, with the Bahamian dollar being at par since 1970.

[INSERT TABLE 12]

2. Economic policy

2.1 *Fiscal policy*

The fiscal deficit narrowed (4% and 1% of GDP for the FYs 2003 and 2004) due to the combined effect of the increase in revenues coupled with the contraction in public expenditure. The deficit was financed by the increase in domestic credit (30%).

In FY 2004, government revenue (including grants) expanded by 10% while current and capital outlays contracted by 3% and 18%, respectively. The increase in government revenue responded mainly to the dynamism of tourism and to a lesser extent to import growth.

For FY 2005, the authorities expect the fiscal deficit to widen as a consequence of the impact of natural disasters. Expenditure (11%) will be guided by reconstruction and rehabilitation activities.

At the same time fiscal revenue will decline as a result of the reduction in the tax base. Whilst imports will increase substantially following the hurricanes, this will not be reflected in higher taxes from international trade, as the government has declared that a large number of items, largely related to reconstruction imports and the replacement of destroyed assets, will be able to be imported duty free given until 31 December 2004 – a date that is most likely to be extended. Tax revenue will also be lower due to lower tourist arrivals and dampened economic activity. It therefore seems unlikely that the 2.9% target deficit will be met, especially given recent experience with overshooting of previously announced targets.

The latest data available shows that government revenue and grants were \$73.4 million in July 2004, more than 42% lower than in June; with weak capital expenditure (down 88% over June) yet higher recurrent expenditure (19% higher than in June, standing at \$81 million), the July deficit reached \$12.5 million. These developments have affected total public sector which reached \$2,034.2 in September 2004, of which 14.3% was external debt. Over the first three quarters of the year, debt increased by 12.7%.

2.2 *Monetary and exchange rate policy*

Although the central bank largely maintained the restrictive monetary stance in the form of quantitative limits implemented after 11 September 2001 to avoid unsustainable imbalances in its balance of payments and to lessen the pressure on the stock of international reserves, this approach was eased in August 2004 with the central bank's lending restrictions slightly relaxed.

During the first eight months of the year The Bahamas witnessed an expansion in external net assets that translated into a rise in the level of deposits of commercial banks. These recorded a threefold increase between September 2003 and September 2004.

The increase in commercial bank liabilities was not matched by an equivalent rise in bank loans to the private sector (6%) notwithstanding the adoption of a more flexible monetary stance to stimulate economic activity. The demand for loans was led by sharp hikes in residential mortgages and consumer credit. In consonance M3 increased by 11.3% (September 2003 to September 2004).

As a result the level of excess reserves reached Bah\$179.9 (with external reserves representing 80% of the total), 16.3% higher than in September 2003, with excess liquid reserves up 21% over the last 12 months to \$202.53 million.

Whilst it may be too early to quantify the effect of the hurricanes on domestic credit trends, it should be pointed out that non-performing loans will increase as the severely affected islands account for roughly 17% of the banks' total loans.

3. Evolution of the main variables

3.1 Economic activity

Economic activity expanded in spite of the impact of the hurricanes on economic activity (0.2% and 1.3% in 2003 and 2004).

The performance of the construction sector responded to the dynamism of the activities related to the development of the industrial, residential and hotel sectors and to the economic impact of the natural disasters. As a result of the latter, substantial reconstruction will be necessary to restore previous living conditions. Housing estimated at more than \$69 million needs to be rebuilt. In addition, the outlook for construction was positive, with the recently increased investment of more than US\$1billion due to Phase III of the Kerzner project.

The transport sector will register a decline due to the damage inflicted by Hurricanes Jeanne and Frances.

The tourism sector exhibited a strong growth performance (11%) notwithstanding the effects of the hurricanes. This will result from the greater number of visitor arrivals and cruise ship calls. Total visitor arrivals for the year to date (January – September 2004) were 12% higher than the respective figure in 2003 given the strong performance in the months prior to the hurricanes as well as the fact that traditionally September (the month in which the hurricane hit the Bahamas) and October are relatively quiet months in terms of visitor arrivals.

3.2 Prices, wages and employment

Annual inflation reached 4% due to the increase in the international price of oil and the contraction in aggregate supply caused by the hurricanes.

3.3 *The evolution of the external sector*

The current account deficit witnessed a significant deficit that was amply financed by the surplus in the capital and financial account. As a result, the stock of international reserves increased.

The deficit in the current account (50% for the first quarter) in relation to the previous year was determined by the rise in imports of goods and services due to the activities of reconstruction and rehabilitation and the rise in the international price of oil. For their part, the performance of the exports of goods and services were affected by the temporary impact of the hurricane on tourism activities.

The positive outcome on the capital and financial account resulted from lower inflows to the banking sector and real estate, which were compensated with the reduction of external debt obligation payments.

Barbados

1. Main trends

The Barbados economy continued its expansion path, growing by 3% during 2004 compared to 2.2% in 2003.

Tourism continued to be the main driver of growth although the non-traded sectors grew significantly in 2004. Improvements were recorded for both tourist and visitor arrivals. The significant growth in the non-traded sectors was boosted by increases in commerce, transportation, storage and communications resulting largely from import growth and telecommunications liberalization.

The central government reduced its fiscal deficit as a result of increased indirect tax revenues and the contraction in capital expenditures.

The central bank adopted a neutral monetary policy stance notwithstanding the reduction in excess liquidity in the financial system. For its part the rate of inflation rose slightly, partly as a result of the increase in international oil prices.

The current account of the balance of payments recorded a deficit due to the growth in imports and the loss of export competitiveness. The foreign direct inflows destined in part to the tourism sector were insufficient to finance this disequilibrium causing a decline in the stock of international net reserves.

2. Economic policy

2.1. Fiscal policy

The central government reduced its deficit (3% and 2.5% of GDP in 2003 and 2004) due to the growth in revenues which managed to outstrip that of total expenditures.

The evolution of revenues responded to the rise in the indirect tax intake due to the higher import demand for most goods and in particular for motor cars. Direct tax revenue declined due to the reduction in the tax rate of corporations (38% and 36% in 2003 and 2004) and the tax base of individuals (23% and 20% in 2003 and 2004) as a result of the increase in the tax exemption income bracket threshold.

The behavior of expenditures reflected the contraction in capital expenditures. These offset the expansion of current outlays and more precisely that of subsidies, transfers and, to a lesser extent, wages and salaries. In turn transfers are explained by the change in the administration of the Queen Elizabeth Hospital.

The deficit was financed with domestic credit from the Central Bank. The government reduced its total debt (73% and 71% of GDP in 2003 and 2004 respectively). The total stock of external debt declined from 27% to 25% of GDP for the same period.

2.2 Monetary policy

The monetary authorities maintained a neutral stance. During the year the financial system witnessed a contraction in the stock of international net assets and a moderate growth in the level of deposits. Both the decline in foreign assets and the rise in deposits responded to the significant import growth.

This translated into an increase in the ratio of credits to deposits which redounded into a drop in the level of excess liquidity in the financial system. This in turn caused a contraction in commercial banks' demand for treasury bills leading to a rise in the rate of interest (0.64% and 2.14% in January and September 2004).

The variation in Treasury bill rates did not alter the term structure of interest rates. The demand for loans grew by 6% (January-September 2004) responding to the rise in economic activity. A share of the loans was channelled for the purchase of real estate and motor vehicles.

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TABLE**13]**

3. The evolution of economic activity

3.1 Economic activity

The Barbadian economy expanded its growth trajectory in relation to the previous year (2.2% and 3% in 2003 and 2004) driven by the dynamism of tourism and, to a lesser extent, by the non-tradable sector and, in particular, by transport, storage and communications.

Agricultural output fell as a result of the decline of sugar production for the fourth year in a row. The sector was also negatively affected by unfavorable climatic conditions.

Manufacturing stagnated (-1% and -0.1% in 2003 and 2004). The decline in food processing products more than offset the expansion of chemical products, beverages, and non-metallic minerals.

The performance of transport, storage and communication (1.3% and 3.2% in 2003 and 2004) responded to the dynamism of imports and to the process of market liberalization in the telecommunications sector.

The construction sector benefited from the ongoing remodeling of the airport and the activities related to the construction of the Hilton Hotel.

Tourism continued on its recovery path, which began in 2003 following the negative impact of the 11 September 2001 events. The number of visitors grew by 10% between January and September 2004 (7% for the same period for 2003). The number of cruise ship visitors increased by 32% in response to the greater number of calls.

International business and financial services exhibited a robust performance (2% in 2003 and 2004) in spite of the significant decline in the number of new registrations of offshore banks from 14 to 2 between 2003 and 2004.

3.2 Prices, wages and employment

The rate of inflation increased (1.6% and 1.9% in 2003 and 2004) as a result in the contraction of the supply of foodstuff and the rise in the international price of oil.

The number of persons employed increased by 4% from 129,400 in the last quarter of 2003 to 134,600 during the second quarter of 2004. The unemployment rate declined (by 2%) to 9.6% in 2004. Services, transportation and communications were the main sources of employment growth.

3.3 *The evolution of the external sector*

The balance of payments registered a deficit as the disequilibrium in the current account (US\$226 million) could not be offset by the surplus in the capital and financial account (US\$186 million). As a consequence the stock of international reserves of the central bank declined.

The deficit in the current account reflected the negative result in the commercial balance. In turn, this is accounted for by the growth in imports (11%) and in particular in capital and consumption goods purchases and by the rise in international oil prices. For their part export performance stagnated (2%) both as a result of the decline in sugar production and the deterioration of the terms of trade for traditional products.

The services balance widened its surplus (10%) which reflected an increase in the flow of tourist arrivals and more specifically of tourism from the United Kingdom.

The capital and financial account result is explained by the increase in foreign direct investment inflows destined to the development of the tourism sector, utilities and real estate.

Belize

1. Main trends

In 2004 the Belizean economy saw a strong growth performance (6%) led by healthy increases in tourism, agriculture and construction (30%, 12% and 8%, respectively).

Despite increased economic activity, tax receipts were below target while expenditures exceeded their planned levels. As a result, the fiscal deficit which reached 11% of GDP for FY 2003/2004 is unlikely to reach the 3% objective announced by the authorities.¹⁶

Inflation increased slightly (2.6% and 3.4% in 2003 and 2004) mainly due to rising fuel costs, water rates and other imports from the United States.

¹⁶ FY denotes fiscal year. The fiscal year runs from April to March. All figures, unless otherwise noted, are denoted in Belizean dollars, which are traded to the US\$ at a ratio of 2:1. The official rate of the Belizean dollar to the US dollar is held at Bze\$2:US\$1, however in effect, a multiple exchange rate system is operational in Belize, where higher rates have been observed in unofficial markets: despite the importance to the authorities of maintaining the official rate, several ‘cambios’ have been licensed to sell at rates up to Bze\$2.15:US\$1. They are however required to collect and submit information on currency transactions, as well as yield part of their earnings at the official rate to the central bank.

On the external front, Belize registered a negative result in its balance of payments as a result of external debt service payments. The deficit was largely financed by drawing on the stock of net international reserves.

For 2005 it is expected that the economy will record a rate of growth between 4% and 5%.

2. Economic policy

2.1 Fiscal policy

The fiscal deficit reached 11% of GDP for the FY 2004/2005 and is projected to decrease to 3% in FY 2005/2004. However, revenue has been below the budget estimations whilst total expenditure has been higher than foreseen. This could endanger the fiscal target of the government.

All revenue items underperformed except from taxes on goods and services, which were ahead of schedule.

The behaviour of total expenditure responded to the rise in current expenditures since capital expenditures contracted. Current expenditure saw a particularly large increase due to pension obligations as well as interest payments on public debt. Payments and transfers outweighed a 2.2% decline in expenditure on goods and services.

Contrarily, capital expenditure and net lending fell by 42.8% in an effort to control the expansionary course of fiscal policy. This outcome mainly reflected the contraction in capital transfers and net lending (-88%). In comparison the outlays financed with domestic and foreign sources also registered declines, albeit relatively moderate ones (-19% and -26%, respectively).

The deficit was financed with domestic sources (93% of the total). Despite loan disbursements of \$19.2 million, net financing from abroad was negative due to amortization and sinking fund payments amounting to \$32.4 million.

The central government's domestic debt increased 4.4% over to Bze\$270 million (for the period April to September 2004 relative to the previous year), with a 13.1% increase in its overdraft facility with the central bank. Interest payments totalled more than Bze\$11.3 million. However, public sector external debt decreased 4.2% to Bze\$1,443.3 million. Overall principal repayments totalled Bze\$44.3 million and interest payments totalled Bze\$76.7 million.

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TABLE**14]**

2.2 Monetary and exchange rate policy

In 2004 the money base contracted as a result of the decrease in external net assets (32.2%) which compensated the increase in net domestic credit (20%). However, the reduction of the reserve requirement for domestic banks by 5 percentage points to 19% allowed the narrow and expanded money supply (M1 and M2) to grow by 3% and 8.4% over the first three quarters of 2004, compared to 0.5% and 3.7% for same period in 2003. The increase of 11.6% in quasi money was also noted in the expansion of M2.

The increase in money supply allowed interest rates to decline. As a result, loans to the primary, secondary and tertiary sectors expanded by 10.1%, 19.5% and 23.5%, respectively. These sectors received a total of 12.6%, 27.9% and 43.7% of all loans and advances. Sugar production and utilities in particular saw large increases in loans and advances, or 48.9% and 61.7%, respectively, to personal loans in contrast contracted 9.4%.

3. Evolution of the main variables

3.1 Economic activity

GDP increased 6% over the year 2004. All sectors expanded across the board. The most dynamic sectors included agriculture, tourism and construction.

The performance of agriculture (12%) responded to favourable weather conditions, improvements in efficiency and input usage, and higher international prices for some of the main export products. Production of most crops and in particular of citrus rebounded.

Although the utilities sector contracted 5.6% due to price increases, construction saw an 8.1% increase, led largely by increased lending of commercial banks and the Development Finance Corporation (DFC). Manufacturing (including mining and quarrying) increased by 3.9%, responding to the primary sector's performance and spurred by large increases in juice production.

Tourism continued its upward trend. Total stopovers increased 5.4% over the first three quarters of 2004 relative to the first three quarters of 2003, cruise ship arrivals increased more than two thirds, bringing more than half a million (519,525) cruise arrivals to Belize.

3.2 Prices, wages and employment

Inflation increased (2.6% and 3.4% in 2003 and 2004) mainly led by the external pressure of rising fuel costs, higher water rates starting in April 2004 as well as increases in the cost of imports from the United States.

In terms of the components of the price index, the largest increase was registered in utilities, which includes water and fuel, and by transport and communication costs (6% for both). Food,

beverages and tobacco increased by 2.4% while household goods and maintenance did not record any variation.

3.3 The evolution of the external sector

The overall balance of payments result deteriorated substantially as the current account deficit more than compensated the surplus in the capital and financial accounts. The global deficit was estimated at US\$9 million for the first semester of 2004 and was largely financed by drawing upon the stock of net international reserves.

The outcome on the current account reflected the expansion of the commercial gap that more than offset the good performance of non-factor services (53% and US\$65 million). Higher receipts from tourists and increased revenues from the cruise industry were the driving force.

Exports contracted (-1% between September 2004 and 2003) largely due to unfavourable international price movements. For its part imports (15%) rose due to the hike in international oil prices and in spite of a 16.3% decline in external purchases corresponding to the free trade zone area. The decline of the latter was provoked by tightened Mexican customs procedures.

The surplus on the capital and financial accounts witnessed a significant deterioration contracting by -51% in the first semester. This outcome is mainly explained by a negative result (US\$- 1.6 million) in the capital account due to bridge financing a premium payment for the controlling interest in the Belize Telecommunications Company (BTL) and the contraction in the evolution of net financial inflows (-48%). In turn, these responded to the large increase in debt service payments which were able to offset the effect of the steep increase in foreign direct investment (US\$12 and US\$229 million in the first semesters of 2003 and 2004) in the telecommunications sector.

Guyana

1. Main trends

Economic activity improved in 2004, compared with 2003, buoyed by enhanced activity in the agriculture sector and the construction sectors. For its part mining lessened its decline in comparison with the previous year (-9% and -5% in 2003 and 2004). Real GDP growth expanded by 1.5% compared with a contraction of 0.6% in 2003. Meanwhile, real per capita GDP increased roughly by 2% following a 1.2 % contraction last year.

Government's fiscal position is set to strengthen in 2003, with the overall fiscal deficit falling to about 5% of product, relative to over 7% last year. Fiscal improvement is built on the platform of healthy growth in revenues in response to improved tax administration and collections.

Reflecting improved growth and some imported inflation from higher oil prices, inflation is expected to increase to 5.4 %, up from 5% in 2003.

Meanwhile, external disequilibrium worsened with the higher relative growth in imports than in exports. The deterioration in the balance of payments stemmed in part from significant imports of materials and equipment for the road rehabilitation project and for expansion of capacity in sugar and mining. The overall balance of payments is posed to register a deficit close to 10% of GDP.

For 2005 the authorities expect the rate of growth to be between 2% and 3%.

2. Economic policy

2.1 Fiscal policy

The government reduced its fiscal deficit mainly as a result of the increase in tax revenues (36% of GDP) and to a lesser extent to the control of the growth in current expenditures (33% of GDP) and in particular of wages and salaries (12% of GDP). This allowed the central government to register a surplus in its current account (4% of GDP) that was able to finance part of the Public Sector Investment Projects (PSIP).

External debt service increased slightly during the year (42% and 43% of government revenue in 2003 and 2004) and is estimated to reach 14.9% of goods and non-factor services.

2.2 Monetary and exchange rate policy

Monetary policy continues to aim at low inflation, stability in the exchange rate and improved intermediation of credit to the private sector. The authorities use open market operations and reserve requirements to absorb surplus liquidity in the banking system that could trigger higher inflation or undermine the exchange rate.

During 2004, commercial bank deposits rose (24% and 5% for sight and time deposits) over and above the demand for loans. The demand for loans stagnated and failed to be stimulated by the decline in interest rates. The nominal weighted interest rate declined from 15.9% to 14.1% between 2003 and 2004.

As a result the liquidity of the commercial banking system rose. The ratio of the excess of free to required reserves reached 64% at the beginning of the year. Excess funds were reinvested in external assets (21% and 39% in 2003 and 2004) allowing the banking system to realize capital gains notwithstanding the slight devaluation of the nominal exchange rate (G\$195 and G\$200 per one United States dollar in 2003 and 2004).

In consonance with this behaviour, the restricted and broad money supplies expanded by 9% and 19%, respectively (8% and 11% in 2003).

[INSERT TABLE 15]

2.3 Other policies

Complementing the core macroeconomic policies, government embarked on a number of programmes and reforms aimed at institutional strengthening and modernization. The main thrust of broad policy remains focused on restructuring of traditional primary goods sectors to ensure competitive production, more productive investment in human capital, jobs-creating growth and improved governance.

3. Evolution of the principal variables

3.1 Economic activity

The rate of GDP growth increased due to the dynamism of agriculture, construction, and the slowdown in the contraction of mining.

Agriculture rebounded strongly and is projected to grow by 6 %, following a decline of 1.2% last year. Sugar turned in a robust performance with production up by over 8% on that for 2003. Output of rice also recovered as a result of improved husbandry and restructuring of the sector.

The mining sector moderated its decline with respect to the previous year (-8.6% and -4.5%) in 2003 and 2004. Dynamic growth in the output of gold was offset by a contraction in value added in the bauxite subsector.

For its part, the construction sector responded to the increase in public capital spending and in particular in housing and infrastructure.

3.2 Prices, wages and employment

Average inflation is expected to increase slightly to 5.4%, compared with 5% last year. Even though fiscal and monetary stability has helped to reign in prices, this was countered in part by high fuel and food prices, the latter reflecting the lagged effects of higher transport costs occasioned by the rise in the cost of energy.

3.3 The evolution of the external sector

The global balance of payments registered a deficit (US\$-6 million) as the surplus recorded in the capital and financial account could not offset the current account gap (-11.5 % and -16% of GDP in 2003 and 2004). The deficit was financed by drawing on the stock of net international reserves from the central bank.

The imbalance in the current account widened as dynamic growth in exports was offset by even more robust rise in imports. The resurgence in exports of gold, rice and sugar (9%, 23% and 15%)

was more than compensated for by higher imports of construction materials, equipment and machinery for the expansion of capacity in sugar and mining.

The surplus in the capital account reflected incoming official funds corresponding to the assistance aid that Guyana receives for being part of the group of Highly Indebted Poor Countries (HIPC).

Jamaica

1. Main trends

The economic performance of Jamaica in 2004 was shaped by the impact of Hurricane Ivan which affected the southern and south western parts of the island in early September.

The total impact of the disaster amounts to US\$580 million (8% of GDP). As a result the economy witnessed a reduction in the rate of economic growth (2.3% and 1.9% in 2003 and 2004). Agriculture, electricity and water, transport, storage and communications were among the most affected sectors.

The productive sectors sustained damage and losses of J\$13,375 million, followed by the social sectors (J\$12,729 million), while infrastructure suffered a comparatively lower impact (J\$ 6,988).¹⁷

The effects of Hurricane Ivan did not, however, endanger macroeconomic stability. The government's deficit remained on target (4% of GDP for FY 2005) as the authorities continued their efforts at fiscal consolidation and interest rates maintained their downward trend.¹⁸ For its part, the rate of inflation increased slightly as a result of supply constraints.

The reduction in the current account deficit (12% and 11% of GDP in 2003 and 2004) reflected the good performance of the exports, especially in the first half of the year. The imbalance was financed by issues of bonds and disaster-related inflows. This resulted in an increase in the stock of net international reserves.

Jamaica is projected to register a growth rate of 2.2% GDP in 2005.

¹⁷ J\$ refers to Jamaican dollars.

¹⁸ FY stands for fiscal year. The fiscal year in Jamaica runs from March to April.

2. Economic policy

2.1 *Fiscal policy*

The fiscal deficit declined from 6% in FY2004 to 4% of GDP in FY2005 (without grants). This responded to the rise in tax revenues (27% and 28% of GDP in FYs 2004 and 2005) over and above the expansion in total expenditure as a result of the impact of the hurricane (34.6% and 35% of GDP in FY2004 and 2005).

Tax revenues (27% of GDP) reflected the growth of the economy in the first eight months of the year and the full effects of the tax measures that were passed in 2003. Most of the affected areas and activities do not contribute substantially to the tax revenue collection.

Current expenditures maintained their share in GDP (33% for both fiscal years) since the outlays corresponding to the two most important items of recurrent expenditure, wages and salaries and domestic interest rate payments (11% and 16% of GDP for FY2005) did not change. For their part, capital expenditures rose (1.5% and 2% of GDP for FYs 2004 and 2005) due to the reconstruction efforts.

The behaviour of wages responded to the implementation of a two-year policy of wage restraint (1 April 2004-31 March 2006). Interest payments on the domestic debt moderated as the central bank maintained its commitment to the reduction in the cost of borrowing. The increase in reconstruction expenditures are expected to be covered by grants and concessionary lending.

2.2 *Monetary and exchange rate policy*

The improved macroeconomic conditions in relation to the previous year allowed the Bank of Jamaica to reduce the spectrum of interest rates on its tenors (18% and 14% on the 90-day reverse repurchase instrument). This lessened the cost of the internal debt service of the government and also that of the Bank of Jamaica's open market operations.

For their part, the commercial banks followed suit and the real weighted average loan rate decreased from 7.1% to 6.2% in September 2003 and September 2004. Accordingly, the nominal exchange rate depreciated in line with the fall in interest rates (J\$59.71 and J\$61.89 per US\$1.00 in September 2003 and September 2004).

3. Evolution of the main economic variables

3.1 *Economic activity*

The rate of growth of GDP declined (2.3% and 1.9% in 2003 and 2004) due to the output losses as a consequence of the impact of the hurricane on the different economic sectors

Agriculture (4.5% and -5% in 2003 and 2004) was affected by heavy rainfall and floods.

The manufacturing sector (-0.8% and 4% in 2003 and 2004) responded to the increased demand for its products and improved productivity. The sector was mildly affected by the hurricane (4.7% and 4.2% for the pre- and post-Ivan scenarios) with losses concentrated in the food processing subsector.

The mining sector's performance (4.9% and 9.1% in 2003 and 2004) was determined by favourable external conditions, higher capacity utilization rates at bauxite and alumina plants and by losses due to the temporary stoppage of production caused by the event.

The electricity and water (4.7% and 2.2% in 2003 and 2004) sector was affected by the interruption of the power supply due to the effects of the hurricane.

Transport, storage and communications (3.6% and 2.6% in 2003 and 2004) recorded damage in production resulting from the temporary interruption of passenger and cargo traffic in the road network, the reduction in the volume of traffic and higher costs due to the use of alternative means of transportation and communications.

The activity of the construction sector (1.2% and 3.4% in 2003 and 2004) responded to ongoing government infrastructure projects and reconstruction efforts.

Tourism activities recovered fully from the effects of 11 September 2001. Notwithstanding, the economic performance of the sector reflected the temporary closure of some of the tourist establishments affected by Hurricane Ivan.

3.2 Prices, wages and employment

The rate of inflation accelerated (10% and 11% in 2003 and 2004) due to a decline in agricultural output, higher energy prices and transportation costs.

Temporary increases in unemployment occurred in some of the affected activities that are labour intensive. The banana subsector will sustain 8,000 temporary job losses.

The growth in wages was moderate due to the Memorandum of Understanding which will limit the increase in wages to less than 3% from April 2004 to March 2006.

[INSERT TABLE 16]

3.3 *The external sector*

The current account deficit (12% and 11% of GDP in 2003 and 2004 post-Ivan scenario) was amply compensated by the surplus in the capital and financial account.

The performance of merchandise exports (15%) responded to favourable price conditions, greater external demand and to the negative effects of the Hurricane on mining and agricultural output in the latter part of the year. At the same time, merchandise imports expanded (9%) due to the reconstruction efforts, the replacement of lost output and the increase in the international price of oil.

The services balance widened its surplus reflecting the dynamism of the tourism sector notwithstanding the temporary interruption in the flow of stay-over arrivals.

Current transfers rose (17%) as family members living abroad provided financial support to their relatives affected by the hurricane.

The capital and financial account's surplus is explained by the issue of bonds totalling more than US\$250 million. Also the financial and capital account registered additional flows related to recovery and reconstruction activities and insurance.

Suriname

1. Main trends

Suriname moderated its rate of economic expansion (6% and 4% in 2003 and 2004). The evolution of the economy was favourably affected by the dynamics of the primary sector and in particular by the growth of mining (bauxite and gold). The mining sector benefited from sustained capital inflows and from improved terms of trade for some of its main export products. Agriculture had a mixed performance. The construction sector was positively affected by ongoing projects to expand the productive capacity of mining.

The fiscal result deteriorated due to the growth of current expenditure and in particular of wages and salaries and, to a lesser extent, of capital outlays. For their part, monetary conditions remained fairly stable, with broad money supply expected to register moderate growth, consistent with maintaining stable movements in prices and the nominal exchange rate.

The current account deficit narrowed due to the decrease in import growth and the good performance of exports.

2. Economic policy

2.1 *Fiscal policy*

In 2004 the overall fiscal result of central government deteriorated (SD\$13 and -56 million in 2003 and 2004). This responded to the significant reduction in the current account surplus (SD48 and 16 million of in 2003 and 2004).¹⁹ The behaviour of the current account reflected rises in wages and salaries since interest payments, in particular those corresponding to the external debt, registered a decline (US\$11 and 9 million). The external debt stock diminished from US\$350 in 2003 to US\$347 million in 2004. The fiscal deficit was financed mainly with internal resources.

2.2 *Monetary and exchange rate policy*

Broadly, monetary policy aimed at maintaining the relative price stability and the viability of the Surinamese dollar (SD) that was introduced at the beginning of the year. The central bank continues to use the relatively static reserve requirements as the main instrument of monetary policy.

With the growth in confidence in the SD, and increasingly favourable macroeconomic conditions, reserve requirements domestic currency denominated deposits have been lowered from 35% to 30%. This had a positive effect on bank lending rates, which have fallen by 5% since the end of September to stimulate investment borrowing. However, the contraction in the growth of the demand for loans (-5%) has prompted commercial banks to acquire foreign-owned assets.

By contrast, reserve requirements on foreign currency deposits have increased by 5%, from 17.5% to 22.5% to contain their growth (50% in 2003 and 15% between January and September of 2004).

The narrow and expanded money supplies grew 12% and 14%.

3. Evolution of the main variables

3.1 *Economic activity*

The rate of growth of GDP (6% and 4% in 2003 and 2004) was determined by the dynamism of the primary sector.

The agricultural sector noted a process of recovery based on the resumption of banana exports. For its part, rice production contracted due to technical and financial difficulties.

¹⁹ The Suriname Dollar (SD) is the national currency. It was introduced in January 2004 at a rate of one Suriname dollar per 1,000 Guilders. It replaced the Guilder and currently, 2.7 SD exchanges for one United States Dollar.

[INSERT]

TABLE**17]**

The performance of the mining sector reflected increases in the output of bauxite, alumina and gold. The sector was positively affected by the rise in foreign investment inflows, favourable international prices and the expansion of productive capacity in the gold industry.

Manufacturing output is projected to increase 2.1% slightly above the figure for last year (1.5% and 2.1% in 2003 and 2004).

3.2 Prices, wages and employment

Inflation as measured by the consumer price index declined sharply from 26% in 2003 to 13%, in 2004 due to the stability of the nominal exchange rate which remained constant throughout the year (SD2.7 to US\$1.00).

In terms of the components of the consumer price index, the price level for the food and beverages sector remained relatively stable, while there was a moderate increase in the cost of transport and communications on account of higher fuel prices.

3.3 The evolution of the external sector

The current account deficit narrowed (18% and 13% of GDP in 2003 and 2004) due to the decline in import expansion as a consequence of lower economic growth and higher exports (5%).

Trinidad and Tobago

1. Main trends

In 2004 Trinidad and Tobago moderated its rate of economic expansion (13% and 6% in 2003 and 2004, respectively). The growth rates of most sectors returned to their historical trend after experiencing an unusual acceleration in 2003.²⁰ In particular, the energy sector normalized its operations in 2004 following an unprecedented surge in 2003 associated with the commissioning of the Train III liquefied natural gas facility.

Authorities adopted a prudent fiscal policy and were able to remain, thanks in part to the increase in international oil prices, in a surplus position for the FY2004.²¹

²⁰ In 2004 the authorities rebased the base year for the computation of GDP from 1985 to 2000. This has produced important variations in the GDP rates of growth. In 2003, the rate of growth of GDP with the base year 1985 was estimated 4.1%. Using the base year 2000, the rate of growth of GDP was estimated at 13%.

²¹ FY denotes fiscal year. The fiscal year starts on the 1 October and ends on 30 September.

The financial management of the debt benefited from the reduction of the required reserve ratio of the commercial banking system. This measure also eventually permitted the decline in the rates of interest in order to stimulate loan demand and economic growth.

Inflationary pressures increased in 2004 fed by the rise in food prices. At the same time the rate of unemployment continued on its downward trend.

On the external front, the global balance of the balance of payments recorded a surplus. The positive result in the current account balance reflected the effect of the upward movement in international oil prices on export performance which more than compensated the negative outcome of the capital and financial account.

For 2005, the economy will grow within a range of 5% to 6% led by the energy sector.

2. Economic policy

2.1 *Fiscal policy*

During FY2004, as in the previous corresponding period, the government maintained a surplus position (0.6% and 2% of GDP for each of these periods). This result responded mainly to the increase in corporate tax revenue (roughly 50% of total income).

This is explained in turn by the rise in oil prices and its derivatives. The intake derived from individual taxes that also contributed to generate this result reflected the incorporation of 108 firms and businesses into the Pay as You Earn (PAYE) system.

The income derived from earnings sourced in value added and specific taxes also increased due to the robust growth performance.

For their part, total expenditures responded to current payments (92% of the total). These reflected transfers and retroactive payments made to oil companies, government-owned firms, statutory boards, external debt obligations, and outlays to satisfy social needs.

Capital expenditures corresponded to the ongoing completion of the public sector investment programme.

Notwithstanding the positive fiscal result, the stock of debt of the central government rose (49% and 53% of GDP in FYs 2003 and 2004) due to the issue of bonds (TT\$1,160 million) which absorbed part of the increase in liquidity caused by the reduction in the reserve requirement ratio. The government also profited from the decline in interest rates to restructure the maturity of its debt. For its part, the stock of external debt decreased due to the fulfilment of part of the government obligations.

2.2. *Monetary policy*

During the year monetary policy was expansionary. The authorities maintained the Repo rate (the rate of interest charged to commercial banks for overnight borrowing) on their open market operations at the level of the previous year (5%). At the same time, they decreased in a first phase the requirement reserve ratio in four percentage points from 18% to 14%. In a second phase, after the month of September, the authorities engineered a further decline from 14% to 11%.

This monetary policy stance permitted the central government to finance its operations. It also gave the commercial banks the required flexibility to tune down the term structure of interest rates with the aim of stimulating the demand for loans. The preferential rate of interest that had remained at 9.5% in the first nine months of the year declined to 8.75% in the month of October. For its part, the demand for loans grew at rates above 16%.

In order to ensure the expansion of the monetary aggregates in line with the requirements of the real economy, the central bank intervened on several occasions through open market operations. The narrow and expanded money supplies grew 5% and 6%, respectively.

The capital market as a source of investment funds was enhanced with the introduction in July 2004 of a new auction system for government bonds. The single priced auction system replaced the previous competitive bidding process and is intended to facilitate the development of a secondary bond market. Trading on the equities market increased significantly (30.5%) during the first half of 2004 compared with the increase (4.2%) during the first half of 2003.

The foreign exchange market had limited flexibility during the first nine months of 2004 because of imbalances in demand and supply. This was due largely to the activity of regional sovereign and corporate entities on the local bond market. The central bank accommodated the demand through its sale of foreign currency. Its intervention helped to stabilize the local currency. The nominal exchange rate remained stable at TT\$6.29. Nevertheless, the trade weighted average selling rate of the local currency depreciated slightly relative to the major foreign currencies at the end of September 2004.

3. *The evolution of economic activity*

3.1 *Economic activity*

The economy moderated its rate of growth (13% and 6% in 2003 and 2004). This reflected the return to normalcy of the growth trajectories of most economic sectors, and in particular of the energy sector, after an exceptional performance in 2003.

The performance of the energy sector (31% and 11% in 2003 and 2004) responded to the levelling out in the production of natural gas and to the decline in the rate of growth of activities related to exploration, drilling and perforation. The subsector of petrochemicals and the processing of natural

gas maintained significant levels of economic growth (14% for both).

[INSERT]

TABLE

18]

Agriculture contracted (-20%) due to the sharp drop in sugar production (-43%). This behaviour is explained, in turn, by unfavourable climatic factors, technical difficulties, deficiencies in the quality of the sugar cane harvested and labour conflicts.

Manufacturing recovered (5.5% and 6.6% in 2003 and 2004) led by food, beverage and tobacco (11%) and assembly type industries (11%). The former responded to the greater level of activity of poultry processors, tobacco producers and non-alcoholic beverages. The latter reflected the dynamism of the materials of construction industry and of iron and steel.

3.2 Prices, wages and employment

The rate of inflation grew (3.8% and 4.5% in 2003 and 2004) due to the increase in the price of food (10% between august 2003 and august 2004). Headline inflation during the 12 months ending August 2004 increased by 3.7%. Food prices rose by 10.4% over the period and led the government to propose a number of measures to contain increases. The VAT on some basic foods was zero rated and the surcharge on imports of chicken and turkey parts was reduced from 86% to 40% in October and November 2004, respectively.

Unemployment continued to decline as the number of persons employed grew by 2.5% and the unemployment rate fell to 10.2% during the first quarter of 2004. Construction and services continue to be the main drivers of employment in the economy. Preliminary data indicate that the unemployment rate for the second quarter of 2004 could be as low as 7.8%.

3.3 The evolution of the external sector

The balance of payments registered a surplus as a result of the positive result in the current account (14% and 9% of GDP in 2003 and 2004) that more than compensated the negative outcome on the capital and financial account (10% and 4% of GDP for the same period).

The current account surplus is mainly explained by the rise in the value of exports caused by the increase in the international prices of oil and its derivatives (47% and 22% in 2003 and 2004). External sales of manufactured goods also contributed to global export performance, but to a lesser extent.

The outcome of the capital and financial account responded to financial sector acquisitions abroad as well as outflows to finance the placement of regional bond issues.