

Eastern Caribbean Currency Union

1. Main trends

Based on preliminary estimates by the Eastern Caribbean Central Bank (ECCB) in 2008, the growth of the economies of ECCU¹ was a mere 1.7% in 2008 compared with 5.2% in the previous year, falling short of the projected 3%. The two main drivers of economic growth, construction and tourism, were particularly affected by the global economic crisis. The manufacturing sector suffered a major setback, while agriculture and banks and insurance, recorded solid growth rates. Overall, there was a marginal decline in inflation (reaching 4.8% by the end of the year) catalysed by the stabilization of commodities prices towards the end of 2008. A fiscal deficit equivalent to 3.5% of GDP was recorded, and the balance-of-payments current account deficit remained at approximately 34.4% of GDP. The debt level continued to be unsustainable at 89.5% of GDP.

Compared with the results for 2007, economic growth declined in six of the eight countries, with Anguilla reporting a particularly sharp contraction from 21% in 2007 to -0.5% in 2008. Saint Vincent and the Grenadines also recorded negative growth (-0.5%). Positive growth was recorded in

Antigua and Barbuda (2.8%), Dominica (3.2%), Grenada (0.3%), Montserrat (6.2%), Saint Kitts and Nevis (2.5%) and Saint Lucia (2%). The economic growth forecast for 2009 is -1%, as the effects of the global economic crisis continue to filter through to these economies.

2. Economic policy

(a) Fiscal policy

As a result of the global financial crisis, governments have taken a number of policy decisions (removal of value added tax and the common external tariff on selected commodities, safety net programmes and unemployment

benefits) to cushion the impact of the crisis on the populace and have implemented a public service investment programme (capital investment projects) to stimulate economic activity. However, fiscal discipline is key to maintaining confidence, and the central government deficit actually shrank slightly from 3.9% of GDP in 2007 to 3.5% of GDP in 2008, and a modest primary surplus of 0.01% of GDP was posted, compared with a deficit of 0.4% of GDP in the previous year.

¹ ECCU member countries are Anguilla, Antigua and Barbuda, Dominica, Grenada, Montserrat, Saint Lucia, Saint Kitts and Nevis, Saint Vincent and the Grenadines.

Table 1
EASTERN CARIBBEAN CURRENCY UNION: MAIN ECONOMIC INDICATORS

| | 2000 | 2001 | 2002 | 2003 | 2004 | 2005 | 2006 | 2007 | 2008 ^a |
|---|--------|-------|-------|--------|--------|--------|--------|--------|-------------------|
| Annual growth rates^b | | | | | | | | | |
| Gross domestic product | 4.3 | -0.3 | 2.0 | -2.4 | 3.7 | 5.7 | 4.3 | 0.7 | -1.7 |
| Gross domestic product, by sector | | | | | | | | | |
| Agriculture, hunting, forestry and fishing | 5.5 | -2.0 | 19.0 | -3.8 | -7.3 | -15.2 | 5.5 | -14.6 | -5.8 |
| Mining and quarrying | 10.6 | 2.7 | 2.8 | 14.6 | 4.8 | -4.7 | -1.6 | -43.8 | -20.5 |
| Manufacturing | 9.8 | -20.6 | -5.7 | 22.2 | 24.2 | 40.1 | -31.0 | -12.0 | -1.8 |
| Electricity, gas and water | 26.9 | 6.3 | 5.7 | 6.6 | -29.5 | 13.0 | 18.1 | 2.5 | 6.0 |
| Construction | 30.6 | -22.2 | 18.0 | 6.6 | -1.2 | 9.5 | 28.5 | 5.1 | -10.0 |
| Wholesale and retail commerce, restaurants and hotels | -3.1 | 5.1 | -6.4 | 2.7 | 6.0 | 10.3 | 4.0 | -6.1 | -0.7 |
| Transport, storage and communications | 3.1 | -6.5 | 3.7 | 0.9 | 11.1 | 4.0 | 3.5 | -5.1 | -6.4 |
| Financial institutions, insurance, real estate and business services | 6.6 | 7.8 | 5.8 | -9.5 | 7.2 | 2.0 | 1.3 | 4.7 | 3.2 |
| Community, social and personal services | -2.0 | -1.9 | -2.2 | -3.0 | 2.7 | 4.9 | -2.3 | 4.4 | 0.8 |
| Millions of dollars | | | | | | | | | |
| Balance of payments | | | | | | | | | |
| Current account balance | -468 | -510 | -574 | -681 | -523 | -815 | -1 246 | -1 545 | -1 631 |
| Goods balance | -1 074 | -997 | -979 | -1 176 | -1 233 | -1 481 | -1 832 | -2 087 | -2 171 |
| Exports, f.o.b. | 352 | 309 | 299 | 259 | 342 | 370 | 359 | 378 | 454 |
| Imports, f.o.b. | 1 426 | 1 306 | 1 278 | 1 435 | 1 576 | 1 851 | 2 191 | 2 465 | 2 625 |
| Services trade balance | 661 | 574 | 526 | 604 | 763 | 710 | 638 | 628 | 594 |
| Income balance | -223 | -198 | -218 | -238 | -267 | -234 | -216 | -236 | -207 |
| Net current transfers | 168 | 110 | 98 | 129 | 215 | 188 | 164 | 149 | 153 |
| Capital and financial balance ^c | 489 | 577 | 633 | 722 | 634 | 811 | 1 349 | 1 591 | 1 613 |
| Net foreign direct investment | 328 | 372 | 340 | 553 | 449 | 632 | 1 106 | 1 229 | 723 |
| Other capital movements | 161 | 205 | 293 | 169 | 185 | 179 | 243 | 362 | 890 |
| Overall balance | 21 | 67 | 59 | 41 | 111 | -4 | 103 | 47 | -19 |
| Variation in reserve assets ^d | -21 | -67 | -61 | -41 | -110 | 16 | -92 | -47 | 19 |
| Other external-sector indicators | | | | | | | | | |
| Gross external public debt (millions of dollars) | 1 262 | 1 458 | 1 763 | 2 060 | 2 250 | 2 098 | 2 230 | 2 169 | 2 159 |
| Average annual rates | | | | | | | | | |
| Prices | | | | | | | | | |
| Variation in consumer prices (December-December) | ... | 2.4 | -0.1 | 1.7 | 2.7 | 4.1 | 1.5 | 5.5 | 4.8 |
| Nominal deposit rate ^e | 4.4 | 4.3 | 3.7 | 4.6 | 3.2 | 3.2 | 3.2 | 3.2 | 3.3 |
| Nominal lending rate ^e | 11.6 | 11.4 | 11.0 | 12.8 | 10.4 | 10.2 | 9.9 | 9.6 | 9.6 |
| Percentages of GDP | | | | | | | | | |
| Central government | | | | | | | | | |
| Total income ^f | 27.9 | 27.2 | 28.4 | 29.0 | 30.1 | 35.7 | 30.7 | 30.5 | 31.6 |
| Current income | 24.9 | 24.5 | 25.3 | 25.6 | 26.2 | 26.4 | 27.5 | 28.0 | 27.9 |
| Tax income | 21.3 | 21.1 | 21.8 | 22.3 | 23.1 | 23.8 | 24.8 | 25.3 | 25.0 |
| Capital income | 0.2 | 0.1 | 0.5 | 0.4 | 0.4 | 0.4 | 0.2 | 0.4 | 0.6 |
| Total expenditure | 32.3 | 34.3 | 36.9 | 34.0 | 33.7 | 33.5 | 35.3 | 34.4 | 35.1 |
| Current expenditure | 25.2 | 26.4 | 27.2 | 26.5 | 26.9 | 25.7 | 25.8 | 25.5 | 27.3 |
| Interest | 3.5 | 3.4 | 4.1 | 4.0 | 4.4 | 3.5 | 3.7 | 3.5 | 3.5 |
| Capital expenditure ^g | 7.0 | 7.9 | 9.7 | 7.5 | 6.8 | 7.8 | 9.5 | 8.9 | 7.8 |
| Primary balance | -0.9 | -3.8 | -4.4 | -0.9 | 0.8 | 5.7 | -0.9 | -0.4 | 0.0 |
| Overall balance | -4.4 | -7.1 | -8.5 | -5.0 | -3.6 | 2.2 | -4.6 | -3.9 | -3.5 |
| Public-sector debt | 46.5 | 53.1 | 63.7 | 67.6 | 59.9 | 57.2 | 55.1 | 48.8 | 45.6 |
| Percentages of GDP | | | | | | | | | |
| Money and credit^h | | | | | | | | | |
| Domestic credit | 75.4 | 79.1 | 79.3 | 75.9 | 75.8 | 79.2 | 82.6 | 90.8 | 94.7 |
| To the public sector | -1.3 | -0.9 | -1.1 | -2.7 | -2.2 | -0.3 | -1.6 | -0.5 | 0.6 |
| To the private sector | 76.7 | 80.0 | 80.4 | 78.5 | 78.0 | 79.6 | 84.2 | 91.3 | 94.1 |
| Liquidity (M3) | 76.7 | 80.6 | 83.8 | 86.9 | 91.6 | 92.3 | 92.5 | 92.4 | 94.5 |
| Currency outside banks and local-currency deposits (M2) | 66.9 | 70.3 | 72.3 | 75.4 | 78.7 | 78.1 | 76.4 | 76.4 | 79.5 |
| Foreign-currency deposits | 9.8 | 10.2 | 11.4 | 11.5 | 12.9 | 14.2 | 16.1 | 16.1 | 15.0 |

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official figures.

^a Preliminary figures.

^b Based on figures in Eastern Caribbean dollars at constant 1990 prices.

^c Includes errors and omissions.

^d A minus sign (-) denotes an increase in reserves.

^e Weighted averages.

^f Includes grants.

^g Includes net lending.

^h The monetary figures are end-of-year stocks.

Total central government revenue increased by 10.5%, from 30.5% to 31.6% of GDP between 2007 and 2008, thanks to improved tax administration and a broader tax base. Current income increased by only 6.3%, half the increase recorded in the previous year, on the back of increases in receipts from tax and non-tax sources (5.6% and 12.9%, respectively). Revenue from taxes on income and profit rose by 15.2%, mainly reflecting an increase in revenue from company taxes, especially in Saint Lucia. Revenue from property and international trade taxes, meanwhile, declined slightly.

Current expenditure grew by 14.3%, from the equivalent of 25.5% of GDP in the previous year to 27.3% of GDP in 2008, on account of increases in personal emoluments (12%), transfers and subsidies (23%) and goods and services (15.2%). The increase in personal emoluments was driven by salary and wage increases in Anguilla, Grenada, Saint Kitts and Nevis and Saint Vincent and the Grenadines. Higher outlays for transfers and subsidies were in part due to larger transfers to public entities in Anguilla, the expansion of safety net programmes in Antigua and Barbuda and an increase in retirement benefits in Grenada and Saint Vincent and the Grenadines. The rise in fuel prices and utilities costs was responsible for the increased outlays on goods and services. Capital expenditure declined by 7% as major works were completed on a number of projects.

The fiscal current account balance recorded a surplus of 0.6% of GDP, compared with 2.5% of GDP in 2007. Declining current account surpluses were recorded for Dominica, Grenada, Saint Lucia and Saint Vincent and the Grenadines. Saint Kitts and Nevis experienced a migration from a surplus of 1.2% of GDP to a deficit of 1.5% GDP and Anguilla from a surplus of 5.5% of GDP to a deficit of 0.3% of GDP. Montserrat's deficit shrank slightly from 46.1% to 42.8% of GDP, while the deficit of Antigua and Barbuda widened from 0.8% to 3.7% of GDP.

The public debt situation remains a major concern for the subregion. At the end of 2008, the debt level was at 89.5% of GDP, slightly lower than the level recorded in 2007 (92.6% of GDP), but still above the 60% target set by ECCB. Two countries still maintain debt levels exceeding 100% of GDP: Grenada (106.4%) and Saint Kitts and Nevis (170.3%). While the level of public-sector debt declined in Antigua and Barbuda and Dominica, the debt stock increased marginally in the rest of ECCU. The high level of debt presents a serious challenge to the member countries: the ratio between debt service and current fiscal revenue is as high as 25% for ECCU. In Saint Kitts and Nevis, the ratio is approximately 40%, making this level of debt particularly unsustainable.

(b) Monetary and exchange rate policy

Monetary policy continues to focus on the stability of the Eastern Caribbean dollar. Although ECCB does not employ inflation targeting, inflation worries have eased with the decline in commodity prices. In 2008, there was no change in the discount rate, which remained at 6.5%, while the interbank market rate fluctuated between 5% and 6%. The weighted average lending and deposit rates remained fairly stable at approximately 9.5% and 3.3%, respectively.

Monetary aggregates of ECCU grew at a slower pace than in 2007, reflecting the slowdown in economic activity. Broad money (M3) grew by 2.6% in 2008 compared with 10.4% in 2007, reflecting a 4.8% increase in liquidity (M2) and a contraction of 7.6% in foreign currency deposits. The main source of this increase was the expansion of domestic credit, which grew by 11.2%, driven again by the increase in credit to the public sector. Domestic lending to the private sector grew approximately 10%, compared with 19% in 2007. Growth in domestic lending to the public sector also slowed, from 42.9% in 2007 to 16.2% in 2008.

The exchange rate peg of US\$ 1 to EC\$ 2.70 continues to provide stability for the EC dollar. The real effective exchange rate remained unchanged in the second half of 2008, an indication of the stabilization of the United States dollar.

In order to avoid a run on the Bank of Antigua in the wake of the arrest of Sir Allen Stanford, the majority shareholder, in February 2009, ECCB exercised its emergency powers and seized control of the institution. Sir Allen Stanford was charged by the United States Securities and Exchange Commission over an alleged US\$ 8 billion dollar investment fraud. Subsequently, a consortium of indigenous banks² took control of the Bank upon the recommendation of ECCB.

Meanwhile, the subregion is still trying to get a handle on the CLICO³ debacle. In April 2009, a Liquidity Support Fund was established to provide financial support by providing liquidity to the Eastern Caribbean countries serviced by CLICO insurance and British American, two major subsidiaries of CL Financial Ltd. Trinidad and Tobago will inject US\$ 50 million, Barbados US\$ 5 million, Eastern Caribbean US\$ 10 million and international institutions US\$ 15 million into the Fund.

(c) Other policies

Progress was made on the establishment of the Economic Union of the Organization of Eastern

² Antigua Commercial Bank Ltd, National Bank of Dominica Ltd, National Commercial Bank (SVG) Ltd, St Kitts-Nevis-Anguilla National Bank.

³ Colonial Life Insurance Company Ltd.

Caribbean States (OECS).⁴ June 2010 was set as the date for the implementation of the Economic Union. This will see the creation of a single economic space which will facilitate the free movement of people, goods, services and capital and promote economic

diversification and growth, as well as greater export competitiveness, employment and human resources development. Meanwhile, efforts are ongoing to establish an economic and political union between OECS and Trinidad and Tobago by 2013.

3. The main variables

(a) Economic activity

In 2008, the growth of ECCU decelerated to 1.7% as a result of the slowdown in construction and in mining and quarrying, and the contraction of the tourism and manufacturing sectors. Between 2007 and 2008, valued added fell from 6% to 4% in the construction sector and from 22% to 5% in the mining and quarrying sector.

Agricultural activity increased by 4.3% as banana production, a major growth engine in the sector, expanded significantly. However, while banana production capacity was up by a notable 30% in Saint Lucia and by 21% in Dominica, plantations in Saint Vincent and the Grenadines were blighted by moko disease and leaf spot disease, which slashed production there by 40%. Cocoa production in Grenada, meanwhile, increased by 50%. Prospects for agriculture are, nevertheless, generally bleak: the future of the banana industry is still uncertain, and the subregion remains vulnerable to natural disasters. Banks and insurance drove growth in the financial services, insurance, real estate and business sectors (3.7%), which constitutes 19% of GDP and thus is a key sector in the ECCU.

Manufacturing industry contracted by 6.6% as a result of a decline in beverages and toothpaste production. The latter ceased altogether in Dominica in the last quarter of 2008, and there was a 33% drop in the production of beer and beverages in Saint Vincent and the Grenadines.

The tourism sector is a major source of foreign exchange and employment; in some countries, such as Anguilla, it represents as much as 25% of GDP. Despite the decline in tourism demand as a result of the global economic crisis, total visitor arrivals in ECCU increased by almost 2% on account of a marginal increase in Caribbean visitors and a large (22%) increase in visitors

from Canada. Tourist activity varied among ECCU countries according to the product differentiation, access and marketing strategies pursued. Tourist arrivals declined in Anguilla, Antigua and Barbuda, Montserrat and Saint Vincent and the Grenadines, but increased in Saint Kitts and Nevis, Dominica, Grenada and Saint Lucia. However, all countries posted a decline in tourist arrivals in the last quarter of 2008. Overall, there was a 4.6% increase in the number of cruise ship passengers, while the number of stay-over visitors, the highest-expenditure tourism group, and excursionists fell by 0.5% and 28%, respectively. In sum, tourism posted a 2.2% decline compared with growth of 0.5% in 2007.

Tourist arrivals are forecast to fall drastically in 2009. Some of the ECCU countries have already begun experiencing declines in hotel bookings. For instance, as of May 2009, bookings were down by at least 30% in Saint Lucia. Hotel investments have also slowed as credit remains tight. Given the dependence on tourism, a fall of 1% of GDP is expected in 2009.

(b) Prices, wages and employment

The December-December inflation rate for 2008 was 4.8%, down from 5.5% in 2007. With the exception of fuel and electricity, education and personal services, all other sub-indices showed high prices. Having risen by 13.5% in 2007, fuel and electricity prices contracted by 4% in 2008 on account of the fall in oil prices on the international market in the second half of that year. The highest price increases were recorded in food, (9%, fuelled by increased prices for cereals and dairy products), followed by transportation and communication (8%, reflecting the increase in fuel prices in early 2008). Saint Vincent and the Grenadines, Anguilla and Montserrat reported higher inflation, while the other countries reported a decline in the inflation rate.

Wages and salaries were raised in Saint Kitts and Nevis, Anguilla, Saint Vincent and the Grenadines and Grenada to offset the impact of nominal price increases.

⁴ The Organization of Eastern Caribbean States member States are Antigua and Barbuda, Dominica, Grenada, Montserrat, Saint Kitts and Nevis, Saint Lucia and Saint Vincent and the Grenadines. Anguilla and the British Virgin Islands are associate members.

Employment will be greatly impacted by the decline in construction and tourism activity. Tourism employs a substantial amount of the labour force in ECCU, and a downturn in this sector automatically translates into job cuts. In December 2008, Sandals Resorts in Saint Lucia laid off 210 workers, 80 persons were laid off at the Marriott Hotel in Saint Kitts and Nevis in April 2009, and 60 workers were laid off from the Jalousie plantation in Saint Lucia in January 2009. This trend is expected to continue. The negative impact of waning tourism on unemployment is expected to be compounded in Antigua and Barbuda by the seizure of the assets of Sir Allen Stanford, the largest private-sector employer.

(c) The external sector

The balance-of-payments current account deficit remained at a high 34.4% of GDP at the end of 2008, compared with 34.8% of GDP in 2007. In nominal terms, the current account deficit worsened by approximately

6%. The 20% increase in the value of goods exports (to US\$ 454 million) was not sufficient to offset the nearly 6.5% increase in goods imports (to US\$ 2.625 billion). The services account surplus deteriorated slightly to 12.5% of GDP from 14.1% of GDP in 2007 owing to the decline in tourism receipts as the number of stay-over visitors fell. There was a 29% drop in foreign direct investment, reflecting a significant decrease in equity investment in the tourism sector and real estate. On the capital account, the level of migrant transfers remained fairly unchanged at US\$ 51 million. The capital and financial account recorded a positive balance at approximately 32% of GDP. The overall balance-of-payment deficit was financed with a reduction in ECCB reserves. The Bank's net international reserves shrank by 0.8% to reach US\$ 755 million, covering 2.5 months of imports of goods and services.

The current account deficit is expected to decline marginally to 31.6% of GDP in 2009 on account of an increase in exports and a decline in imports as construction activity continues to slow.