A stylized map of the Caribbean region, showing the outlines of the islands and the surrounding landmasses in shades of gray against a light blue background. The map is centered on the Caribbean Sea.

Testing Times: Prospects and Challenges in the Caribbean

Alejandro Werner

Director, Western Hemisphere Department

October 17, 2014



Outline: Testing Times for...

- The World
- The LAC Region
- The Caribbean
 - Growth
 - Fiscal
 - External
 - Financial
 - Going Forward

Outline: Testing Times for...

- The World
- The LAC Region
- The Caribbean
 - Growth
 - Fiscal
 - External
 - Financial
 - Going Forward

The global recovery has remained slow-paced and uneven...

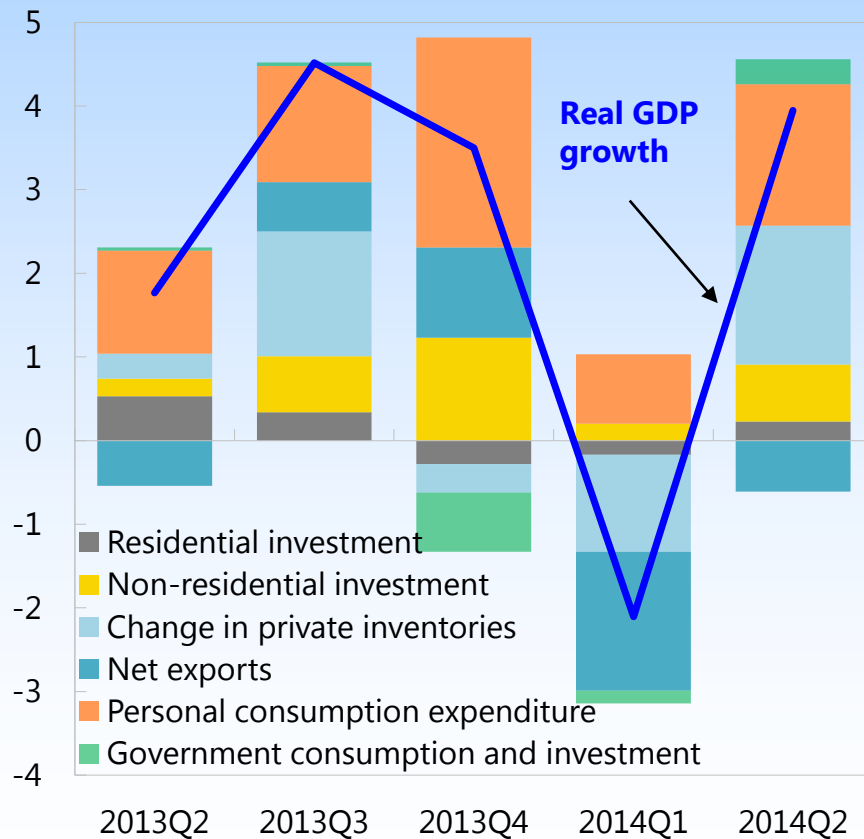
Selected Projections for Real GDP Growth (Percent)

	2012	2013	2014	2015
World	3.4	3.3	3.3	3.8
Advanced Economies	1.2	1.4	1.8	2.3
Euro Area	-0.6	-0.4	0.8	1.4
United States	2.3	2.2	2.2	3.1
Japan	1.5	1.5	0.9	0.8
Emerging Market and Developing Economies	5.1	4.7	4.4	5.0
Asia	6.7	6.6	6.5	6.6
Europe	1.4	2.8	2.7	2.9
Latin America and the Caribbean	2.9	2.7	1.3	2.2

Source: IMF, *World Economic Outlook*.

... as an increasingly solid recovery in the U.S. economy...

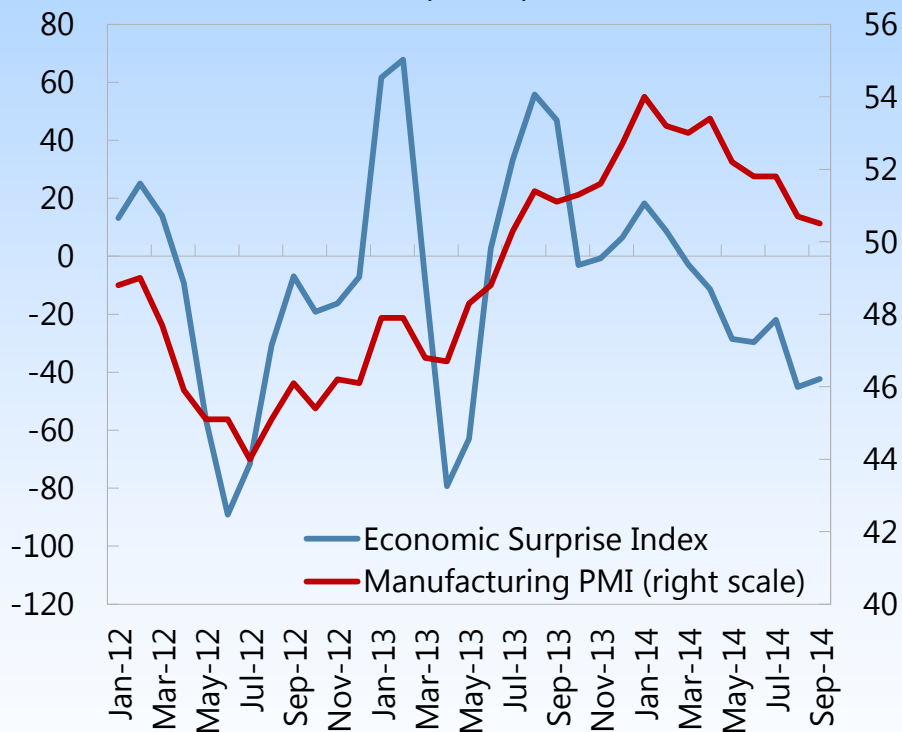
USA: Contributions to GDP Growth
(Percent change from previous quarter)



- 2014Q2 rebound after temporary setback in Q1
- Signs of firming recovery continue to accumulate
- U.S. economy projected to grow at 3+ percent in 2014H2
- Labor market slack declined, but remains sizeable

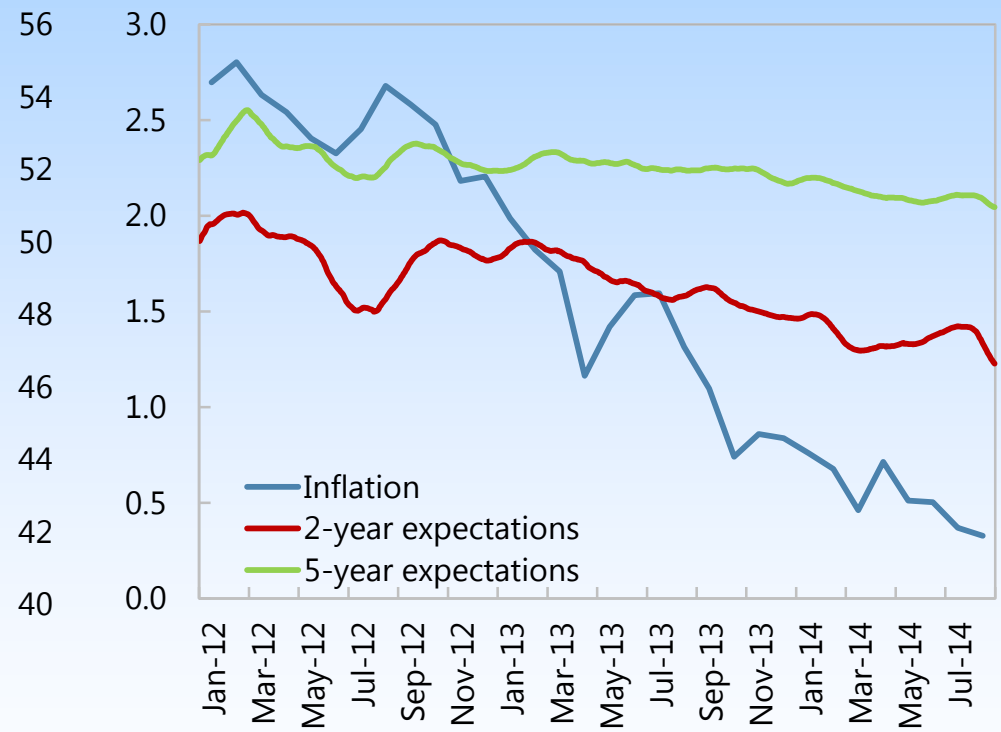
... contrasts with weak activity in many other parts of the world, notably the euro area.

Euro Area: Economic Surprise Index and PMI
(Index)



Source: Bloomberg.

Euro Area: Inflation and Inflation Expectations
(Percent)



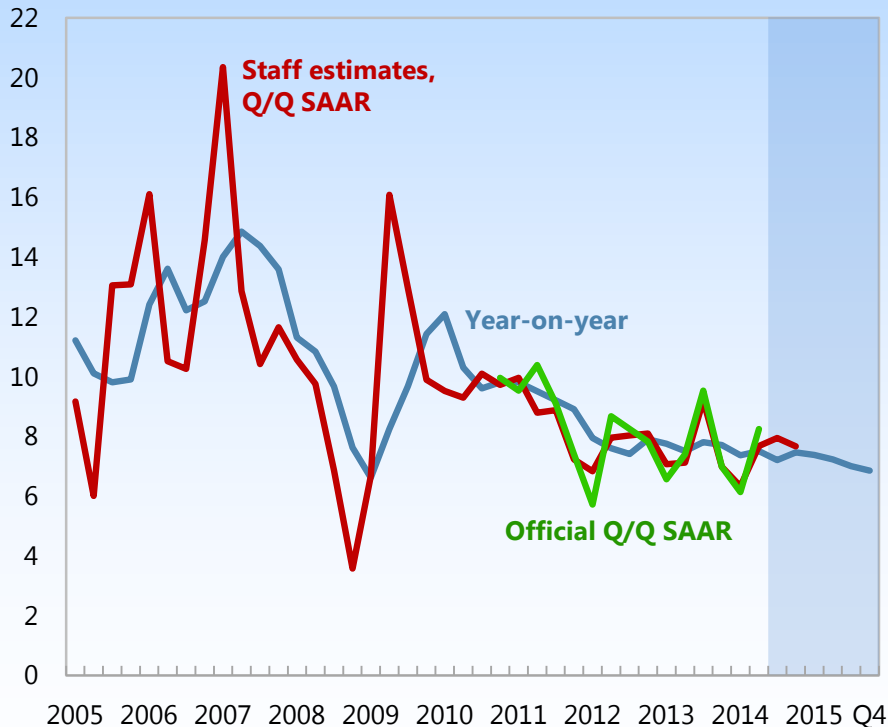
Sources: Haver Analytics; Bloomberg Analytics; and IMF staff calculations.

China is expected to grow above 7 percent, but the massive post-2008 credit boom casts a shadow.

Supportive policy measures should help to achieve the full-year GDP growth target...

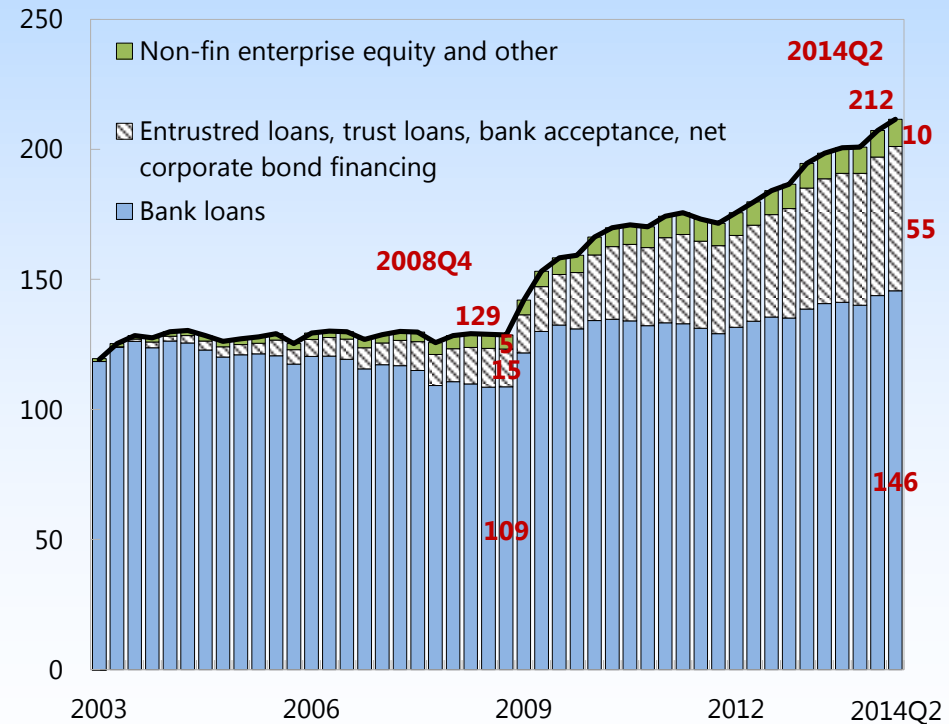
... but financial risks related to past credit growth and the property sector are significant.

Real GDP Growth
(Percent)



Sources: CEIC; and IMF staff calculations.

Stock of Total Social Financing¹
(Percent of GDP)



Sources: CEIC; and IMF staff calculations.

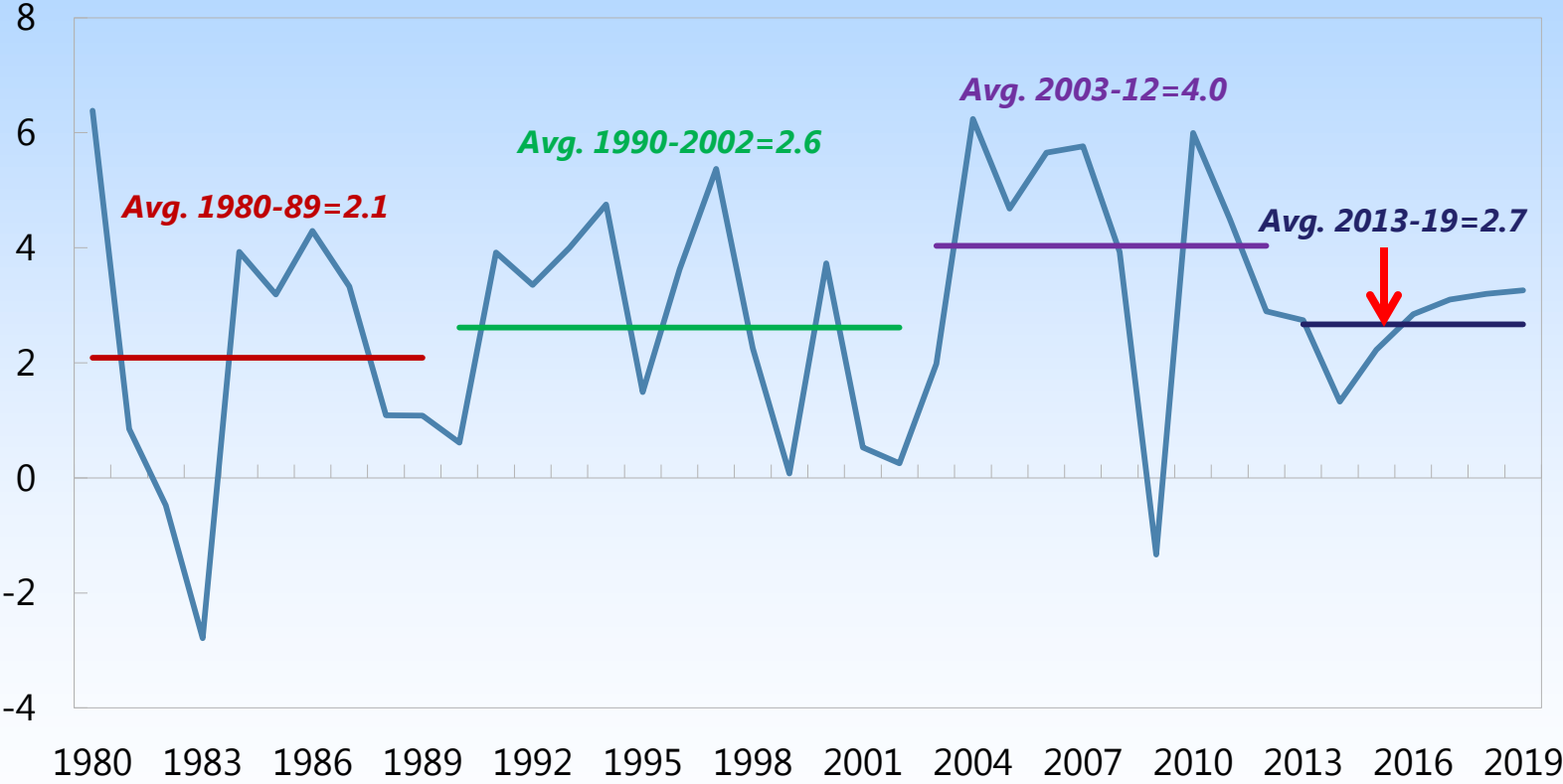
¹ In percent of 4Q rolling sum of quarterly GDP.

Outline: Testing Times for...

- The World
- The LAC Region
- The Caribbean
 - Growth
 - Fiscal
 - External
 - Financial
 - Going Forward

Against this backdrop, Latin America and the Caribbean is facing a lackluster outlook for growth...

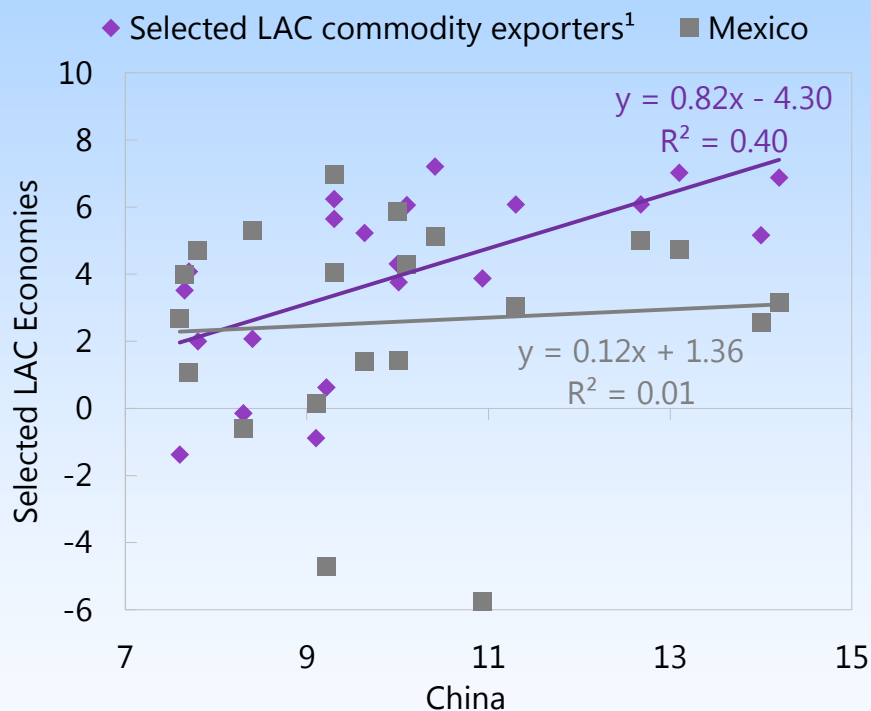
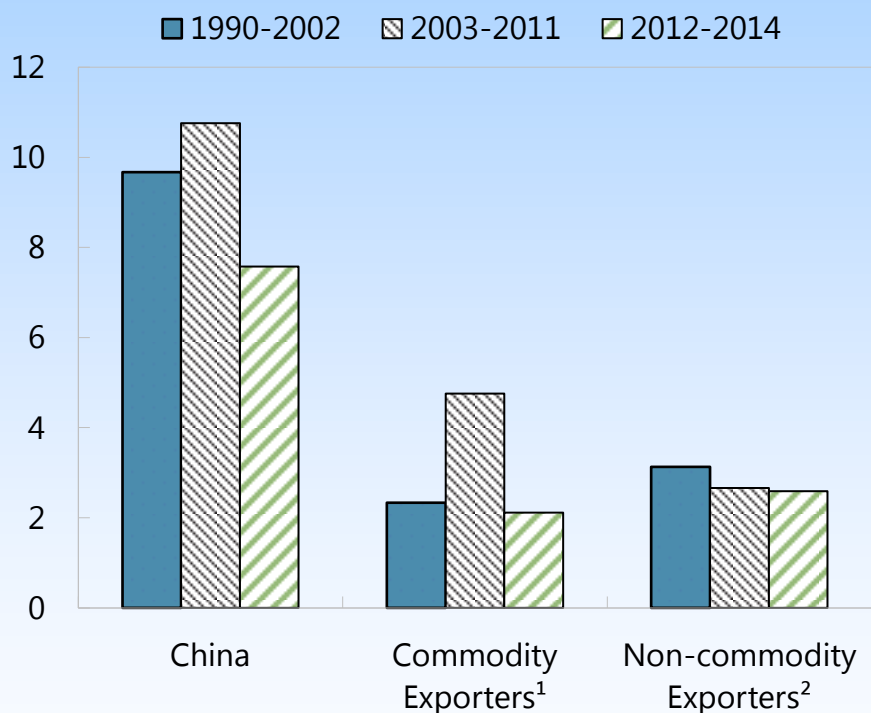
Latin America and the Caribbean: Real GDP Growth
(Percent)



Sources: IMF, *World Economic Outlook*; and IMF staff calculations.

... partly reflecting softness in global commodity markets, amid China's slowdown...

Latin America and China: Annual Real GDP Growth (Percent)



Sources: IMF, *World Economic Outlook*; and IMF staff calculations.

¹ PPP-weighted average of Argentina, Bolivia, Brazil, Chile, Colombia, Ecuador, Paraguay, Peru, Uruguay, and Venezuela.

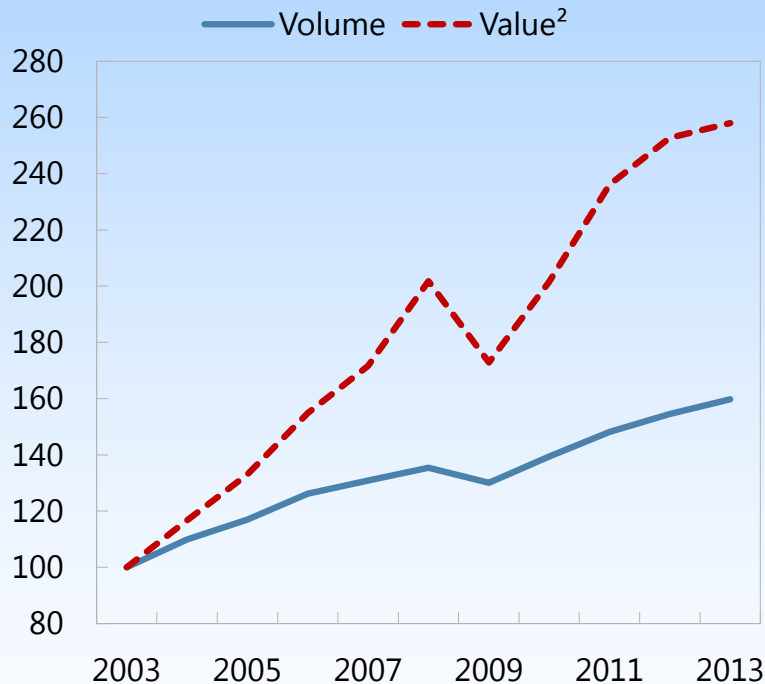
² PPP-weighted average of Costa Rica, El Salvador, Guatemala, Honduras, Mexico, and Nicaragua.

Sources: IMF, *World Economic Outlook*; and IMF staff calculations.

¹ Simple average of Argentina, Brazil, Chile, Colombia, Peru, and Uruguay. Real GDP growth rates are for the period 1993-2013.

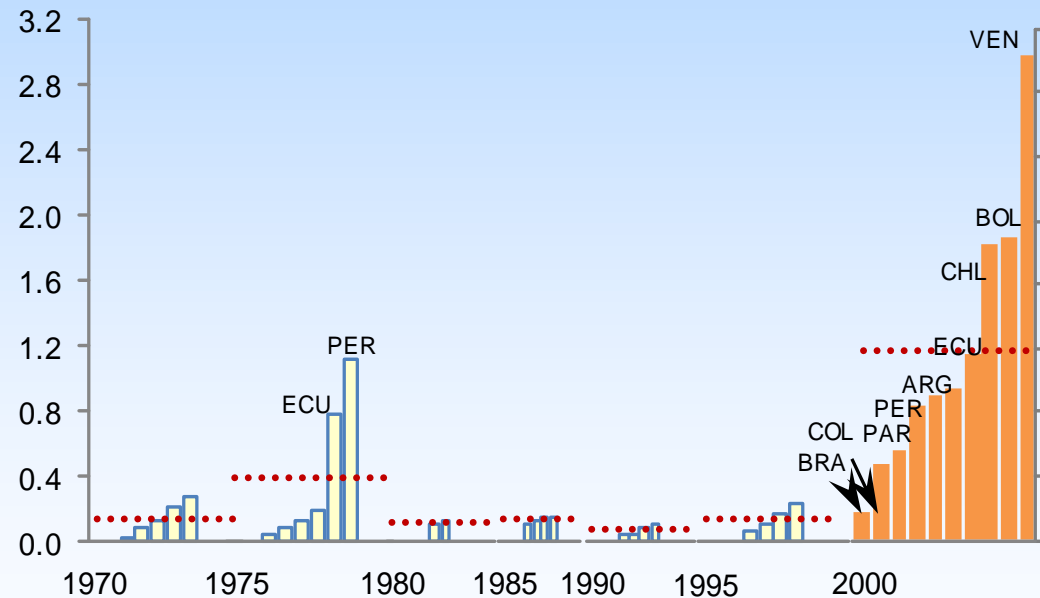
... following a terms-of-trade boom that had brought extraordinary income windfalls.

Latin America: Total Exports¹
(Index: 2003=100)



Latin America: Commodity Income Windfall, 1970–2012¹

(Cumulative windfall as share of annual GDP)



Sources: IMF, *World Economic Outlook*.

¹ Simple average of Latin American countries.

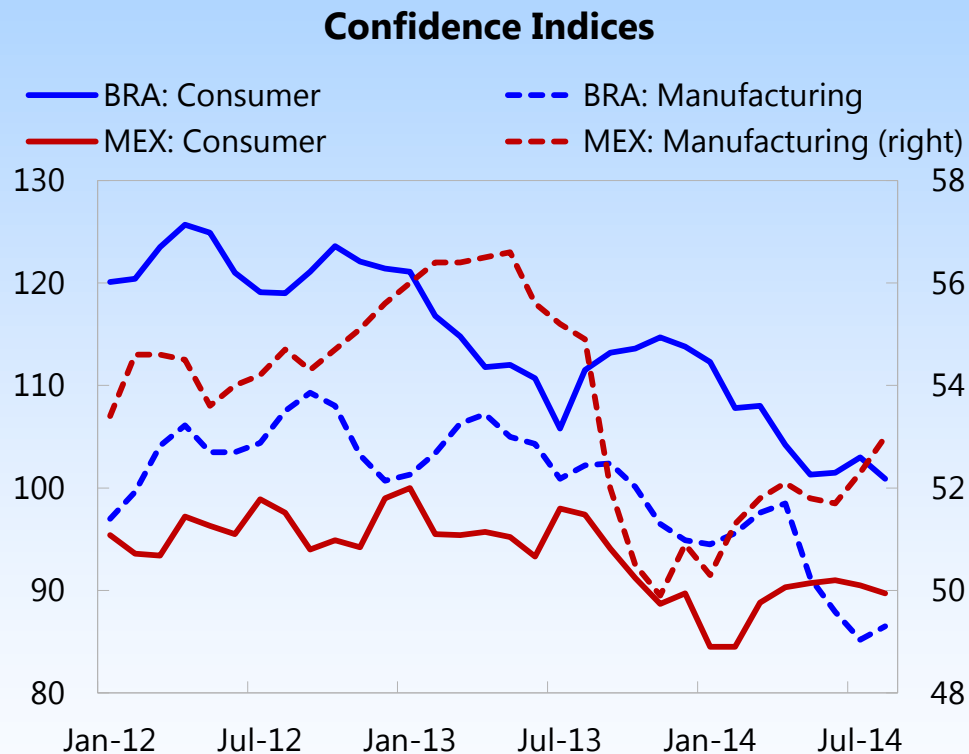
² Total exports in U.S. dollars deflated by the U.S. producer price index .

Sources: IMF, *International Financial Statistics*; and IMF staff estimates.

¹ Cumulative income windfall from start to peak of each identified episode.

Beyond weaker commodity prices, domestic policy uncertainties have also dampened confidence lately.

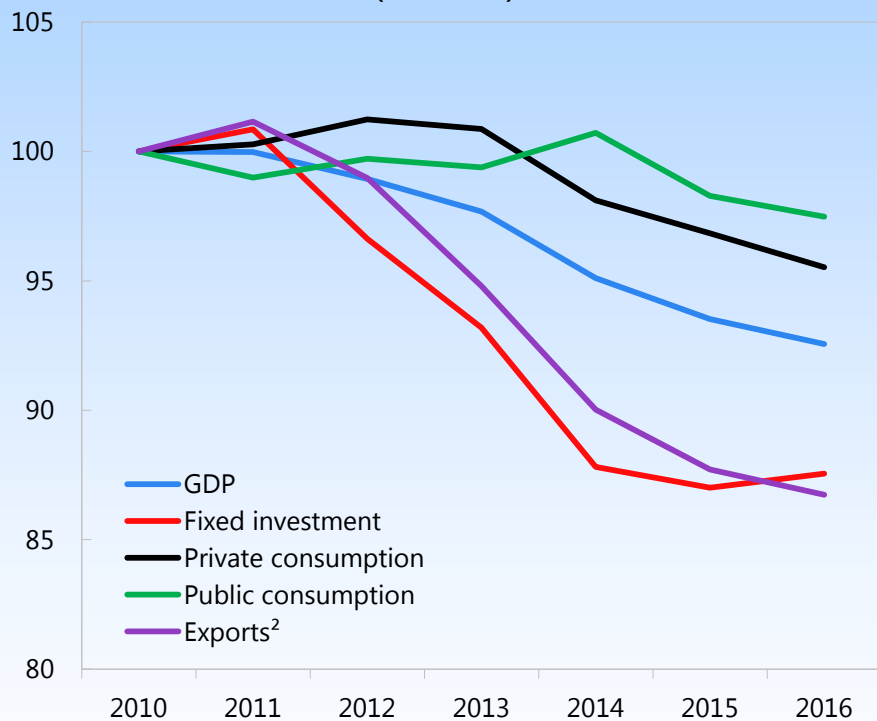
- In some countries, short-term uncertainty is a price worth paying for reforms with high long-run payoff (e.g., Mexico)
- In other cases, however, investor confidence has weakened amid perceptions of policy drift and lack of reform momentum



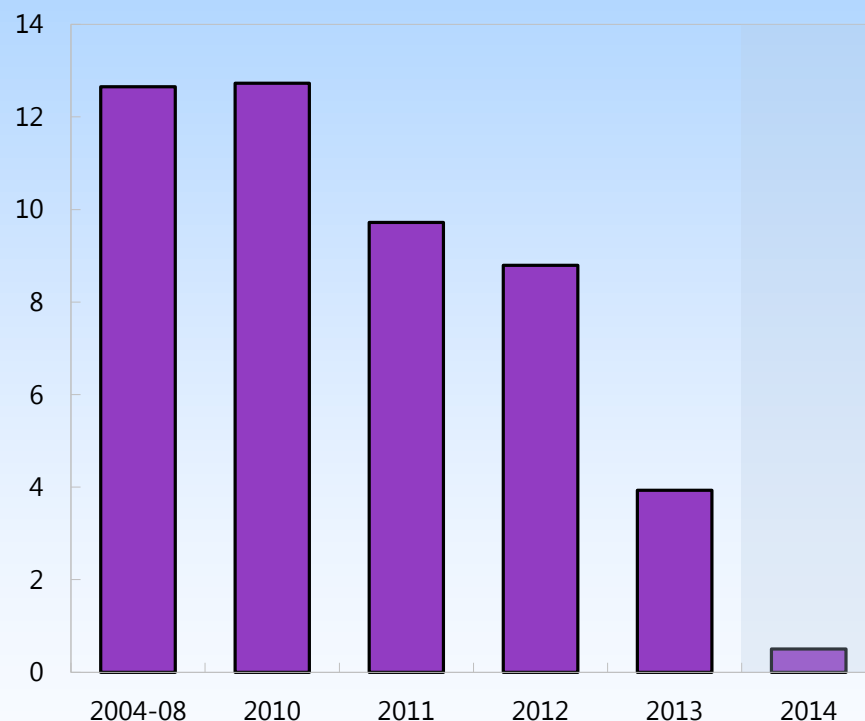
Source: Haver Analytics.

Growth expectations have been revised downward significantly, led by investment...

LAC: Current WEO Path for GDP and Components Relative to Sep. 2011 WEO Projections¹
(Percent)



LA6: Real Investment Growth¹
(Percent)



Sources: IMF, *World Economic Outlook*; and IMF staff calculations.

¹ Ratio of GDP levels between October 2014 and September 2011 WEO projections. A value of 100 indicates no difference between the two projections; values below 100 indicate downward revisions.

² Weighted by the value of exports of goods and services in U.S. dollars.

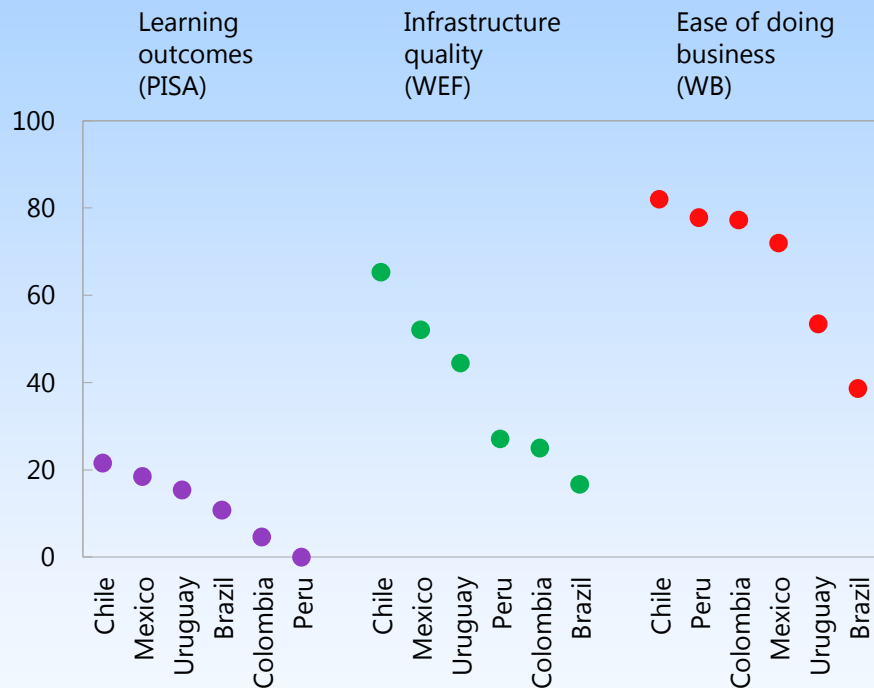
Excludes Dominica, Grenada, Guyana, Jamaica, St. Kitts and Nevis, St. Lucia, St. Vincent and the Grenadines, and Suriname due to data constraints.

Sources: IMF, *World Economic Outlook*; and IMF staff calculations.

¹ Simple average of Brazil, Chile, Colombia, Mexico, Peru, and Uruguay.

... underscoring the need for structural reforms to ease supply bottlenecks and boost productivity.

LA6: Structural Indicators¹ (Percentile ranks)



Sources: OECD, *PISA (2012)*; World Bank, *Ease of Doing Business database (2013)*; World Economic Forum, *Global Competitiveness Report (2014–15)*; and IMF staff calculations.

¹ The scale reflects the percentile distribution in all countries for each respective survey; higher scores reflect higher performance; PISA: Program for International Student Assessment; WB: World Bank; WEF: World Economic Forum.

Priorities differ by country, but generally include:

- Addressing infrastructure bottlenecks
- Enhancing educational outcomes
- Improving the business environment

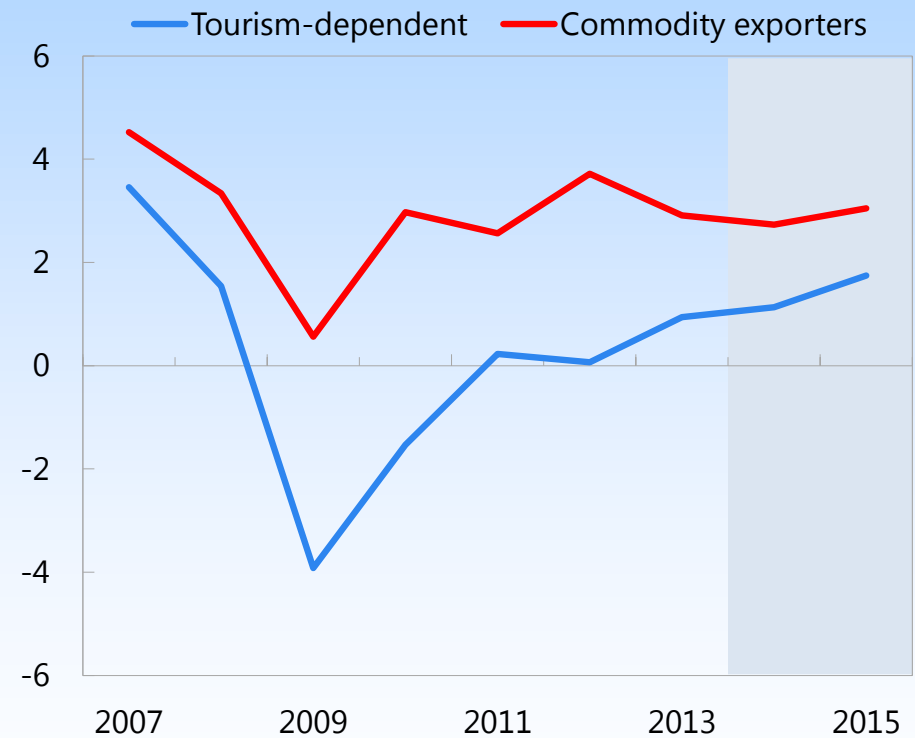
Outline: Testing Times for...

- The World
- The LAC Region
- **The Caribbean**
 - Growth
 - Fiscal
 - External
 - Financial
 - Going Forward

In the Caribbean, growth will remain tepid despite signs of tourism recovery...

Real GDP Growth¹
(Percent)

	2013	2014	2015
Caribbean	1.5	1.6	2.1
Commodity exporters	2.9	2.7	3.0
Belize	0.7	2.0	2.5
Guyana	5.2	3.3	3.8
Suriname	4.1	3.3	3.8
Trinidad and Tobago	1.6	2.3	2.1
Tourism dependent	0.9	1.1	1.7
Antigua and Barbuda	1.8	1.9	1.7
Bahamas, The	0.7	1.2	2.1
Barbados	-0.3	-0.6	0.5
Dominica	0.8	1.4	1.2
Grenada	1.5	1.1	1.2
Jamaica	0.2	1.1	1.8
St. Kitts and Nevis	3.8	3.5	3.2
St. Lucia	-2.3	-1.1	1.4
St. Vincent and the Grenadines	2.3	1.7	2.6
Eastern Caribbean Currency Union ²	1.0	1.3	1.8

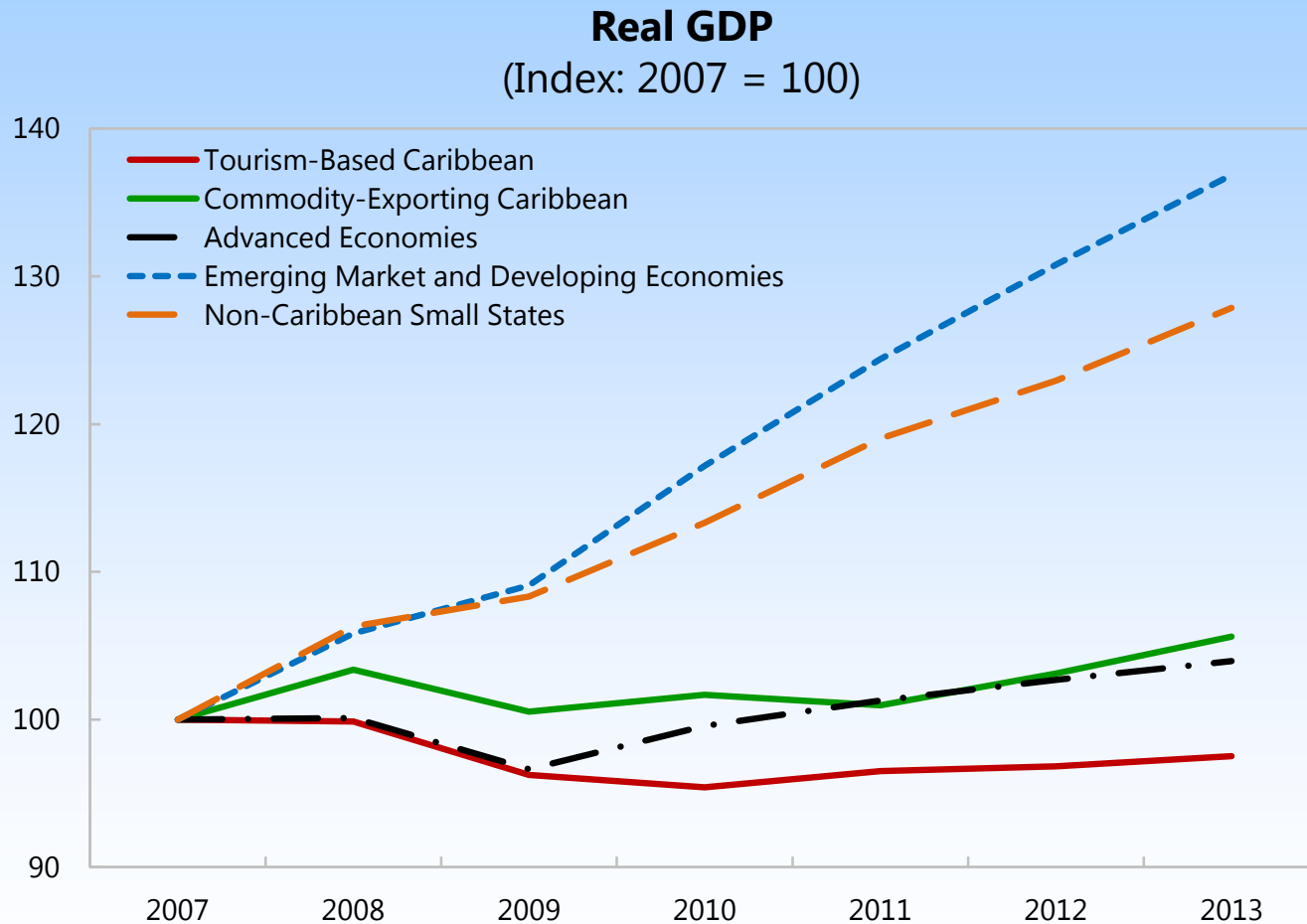


Sources: IMF, *World Economic Outlook*; and IMF staff calculations and projections.

¹ Aggregates are simple averages.

² Includes Antigua and Barbuda, Dominica, Grenada, St. Kitts and Nevis, St. Lucia, and St. Vincent and the Grenadines, as well as Anguilla and Montserrat, which are not IMF members.

... extending the period of sub-par growth since the global financial crisis...

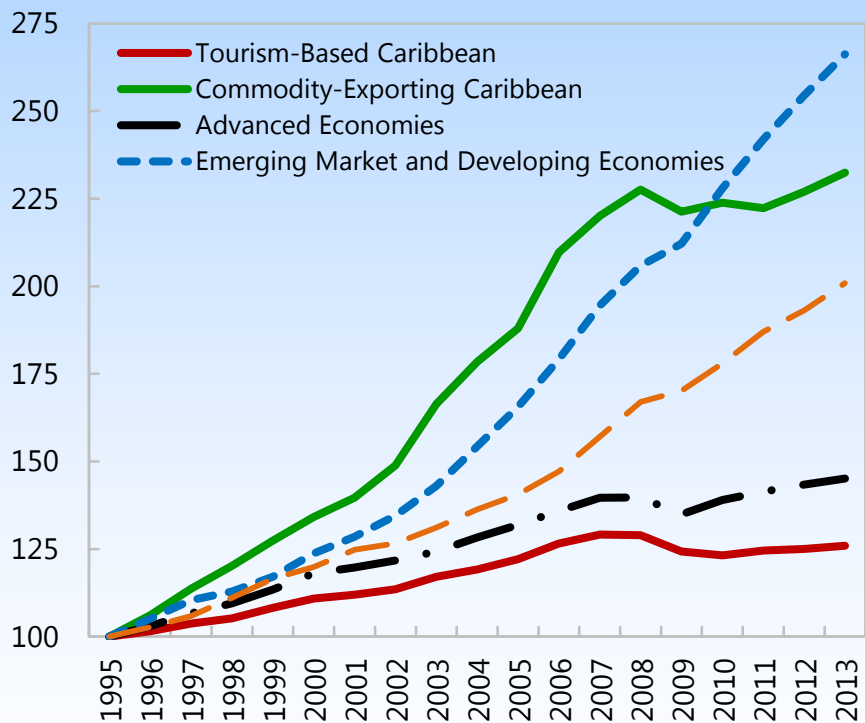


Source: IMF, *World Economic Outlook*.

... though economic weakness goes back even further in the tourism-based economies...

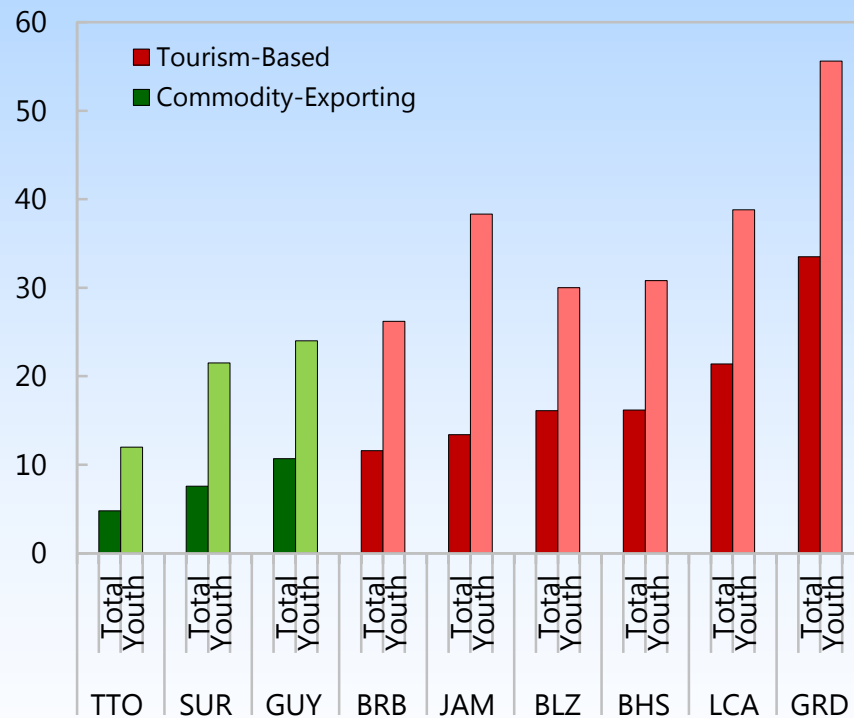
Real GDP

(Index: 1995 = 100)



Unemployment Rates

(Percent, latest available observation)

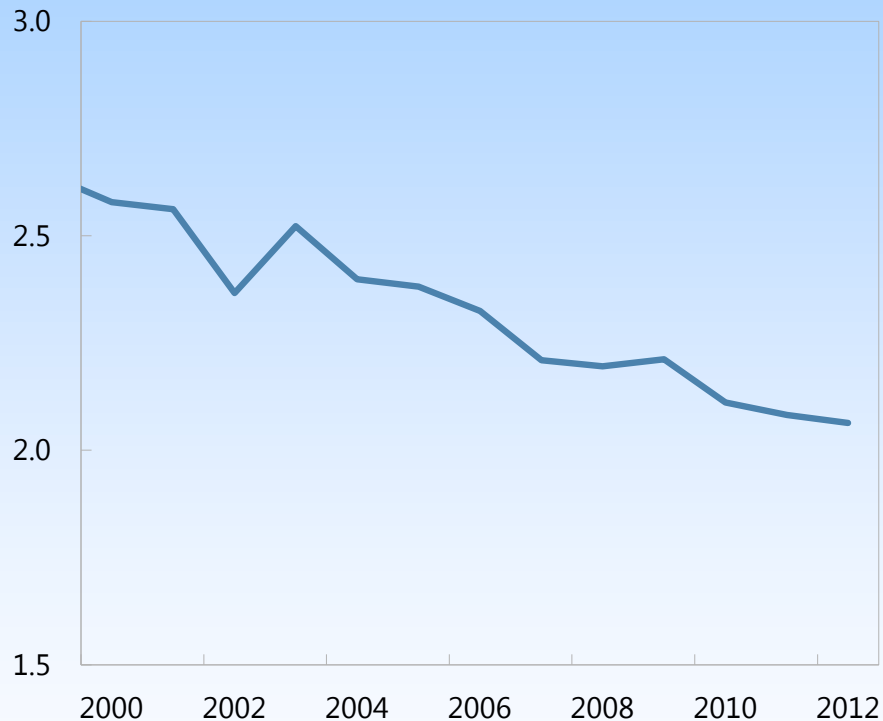


Source: IMF, *World Economic Outlook*.

Sources: National authorities; and IMF staff estimates.

... whose share of the global tourism market has declined by 20 percent since 2000...

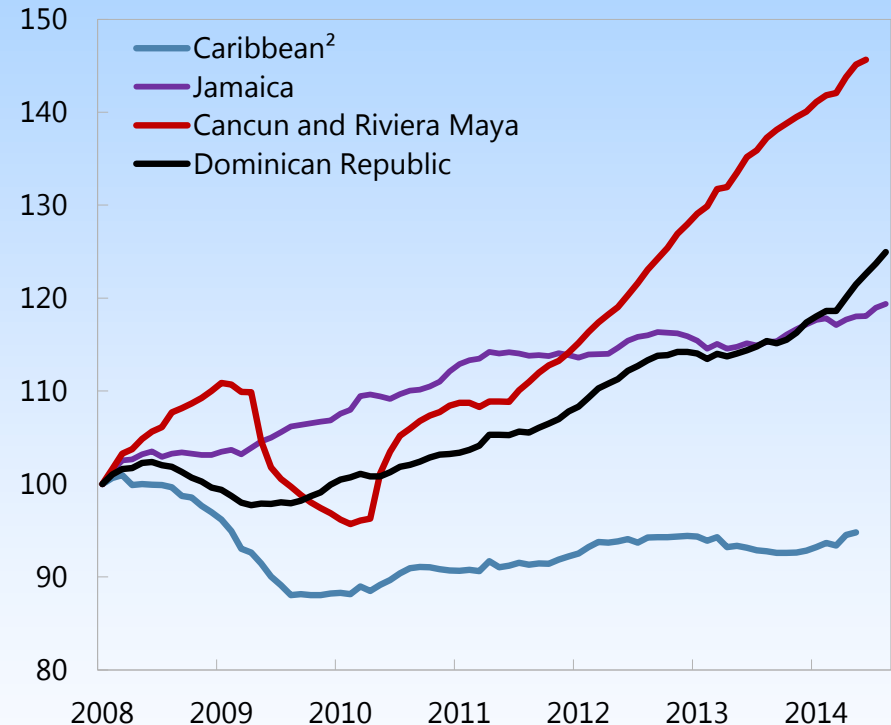
Tourist Arrivals to Caribbean
(Share of world tourist arrivals; percent)



Sources: World Tourism Organization, *Yearbook of Tourism Statistics*; and IMF staff calculations.

¹ Other tourism countries: economies with tourism receipts greater than 5 percent of GDP (avg. 2006-13).

Tourist Arrivals¹
(Index: January 2008 = 100)



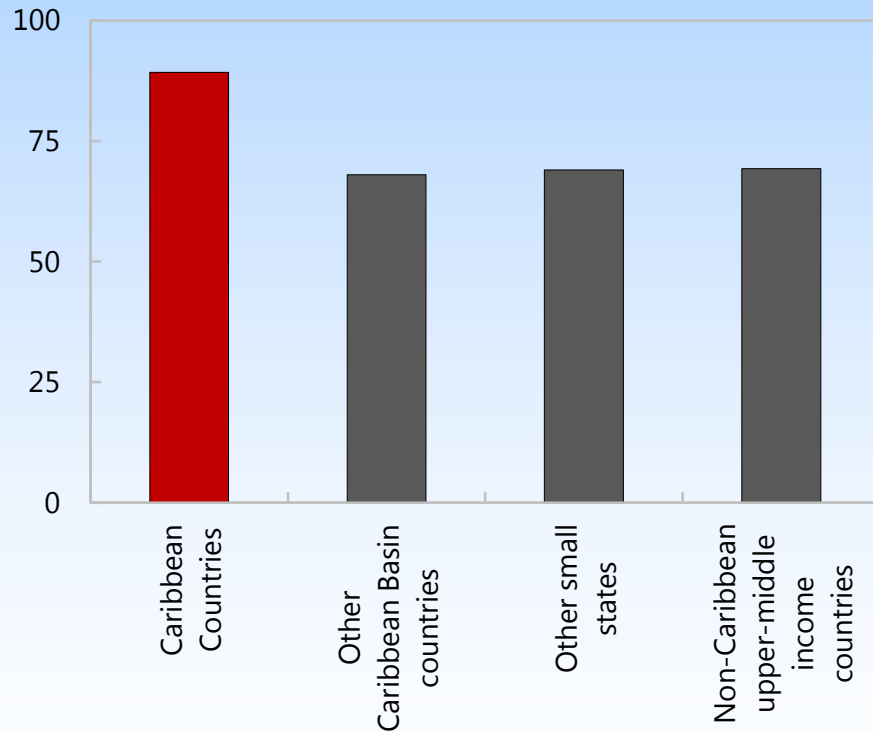
Sources: Caribbean Tourism Organization; Eastern Caribbean Central Bank; Secretaria de Turismo del Estado de Quintana Roo; and IMF staff calculations.

¹ 12-month moving averages.

² Includes Anguilla, Antigua and Barbuda, The Bahamas, Barbados, Belize, Dominica, Grenada, Montserrat, St. Kitts and Nevis, St. Lucia, and St. Vincent and the Grenadines.

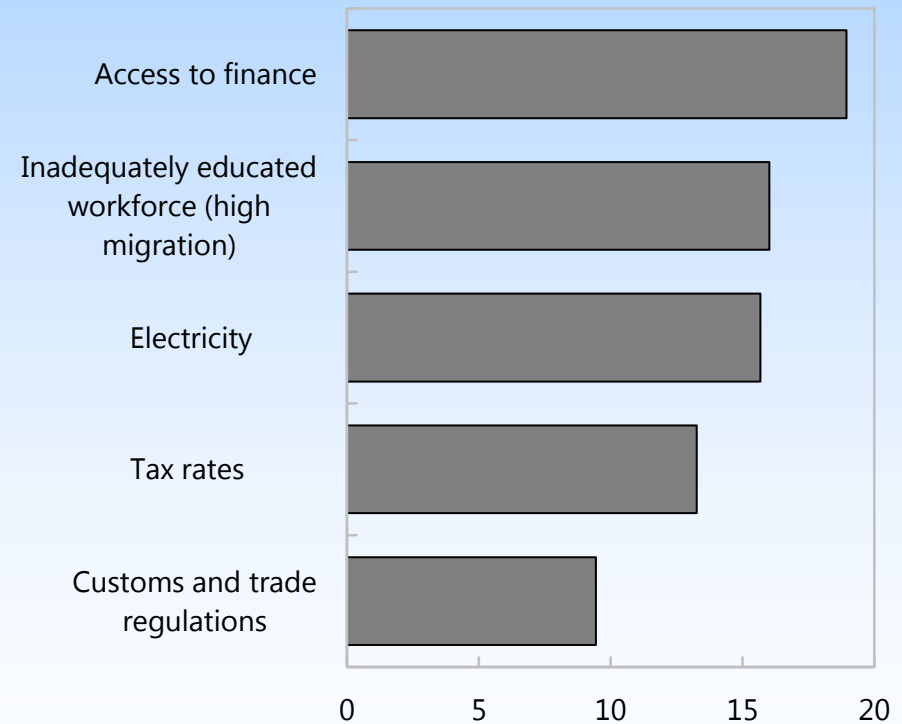
... amid weak cost competitiveness, which reflects a host of structural challenges...

Price-Level Indices
(World price level = 100)



Source: ICP, 2011.

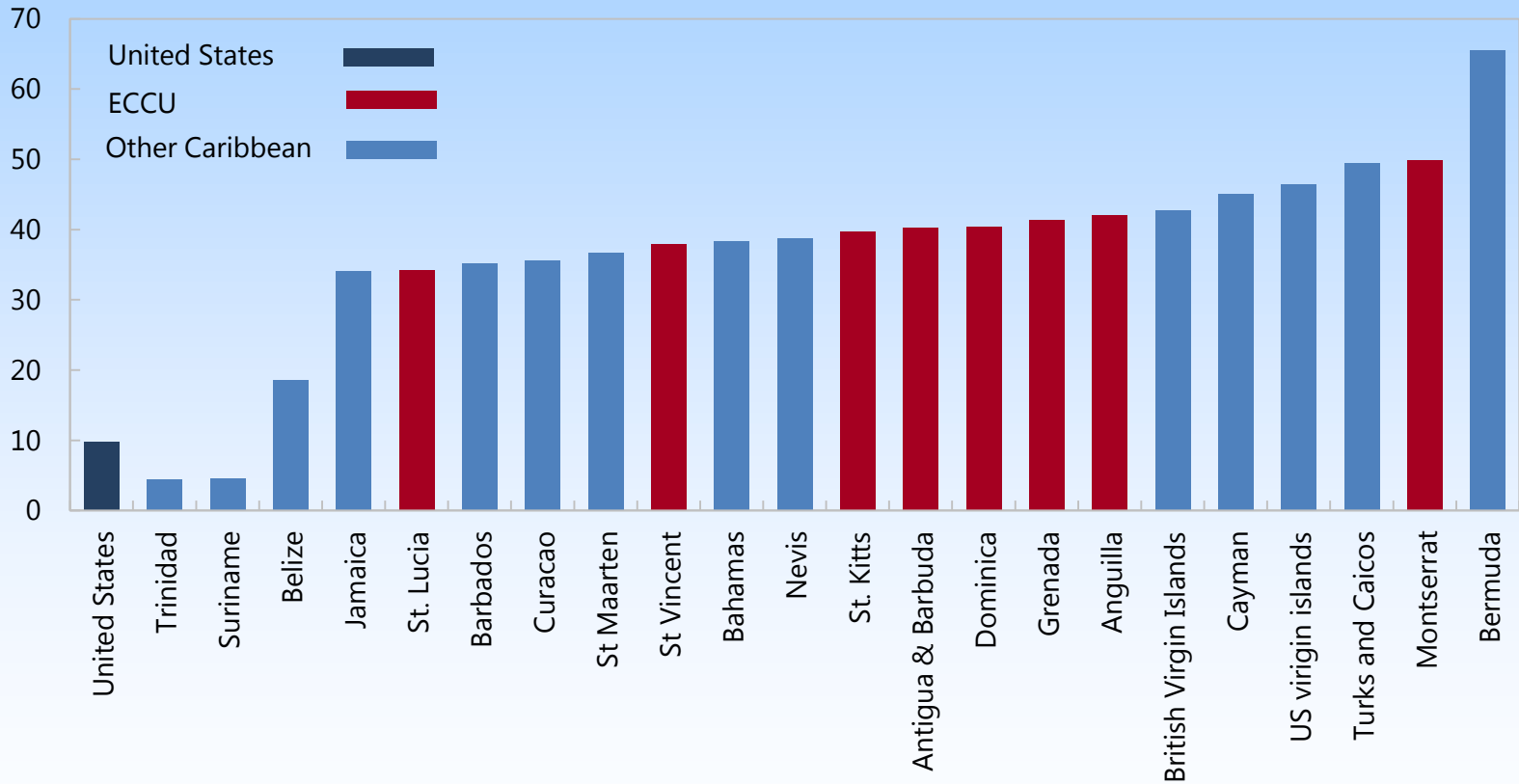
Top Obstacles for Firms
(Average share citing item as top obstacle to business)



Sources: World Bank, Enterprise Surveys.

... including very high local electricity costs.

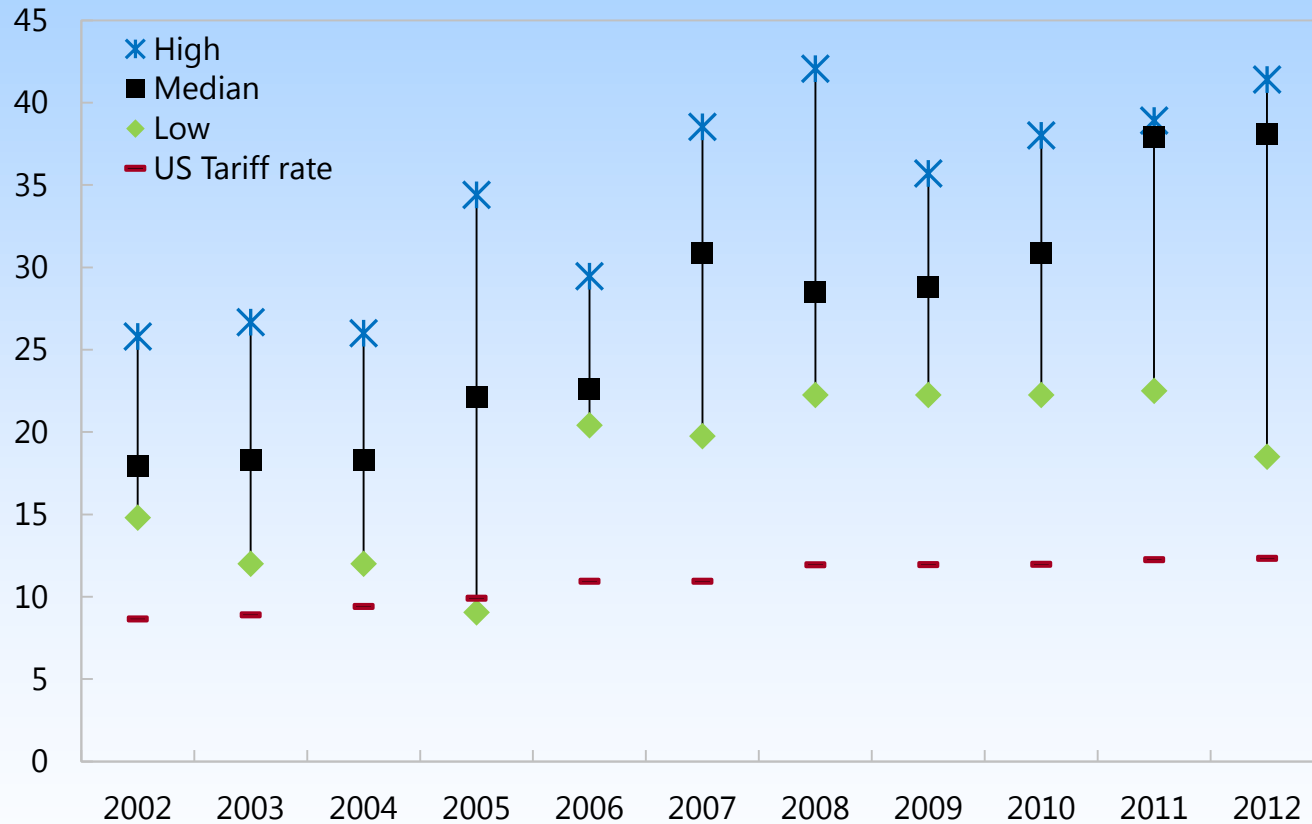
Domestic Electricity Tariffs, 2012
(US ¢/kWh)



Source: CARILEC.

Electricity tariffs have, on average, doubled in the last decade

Caribbean Residential Electricity Tariffs (2002–12)¹
(US ¢/kWh)

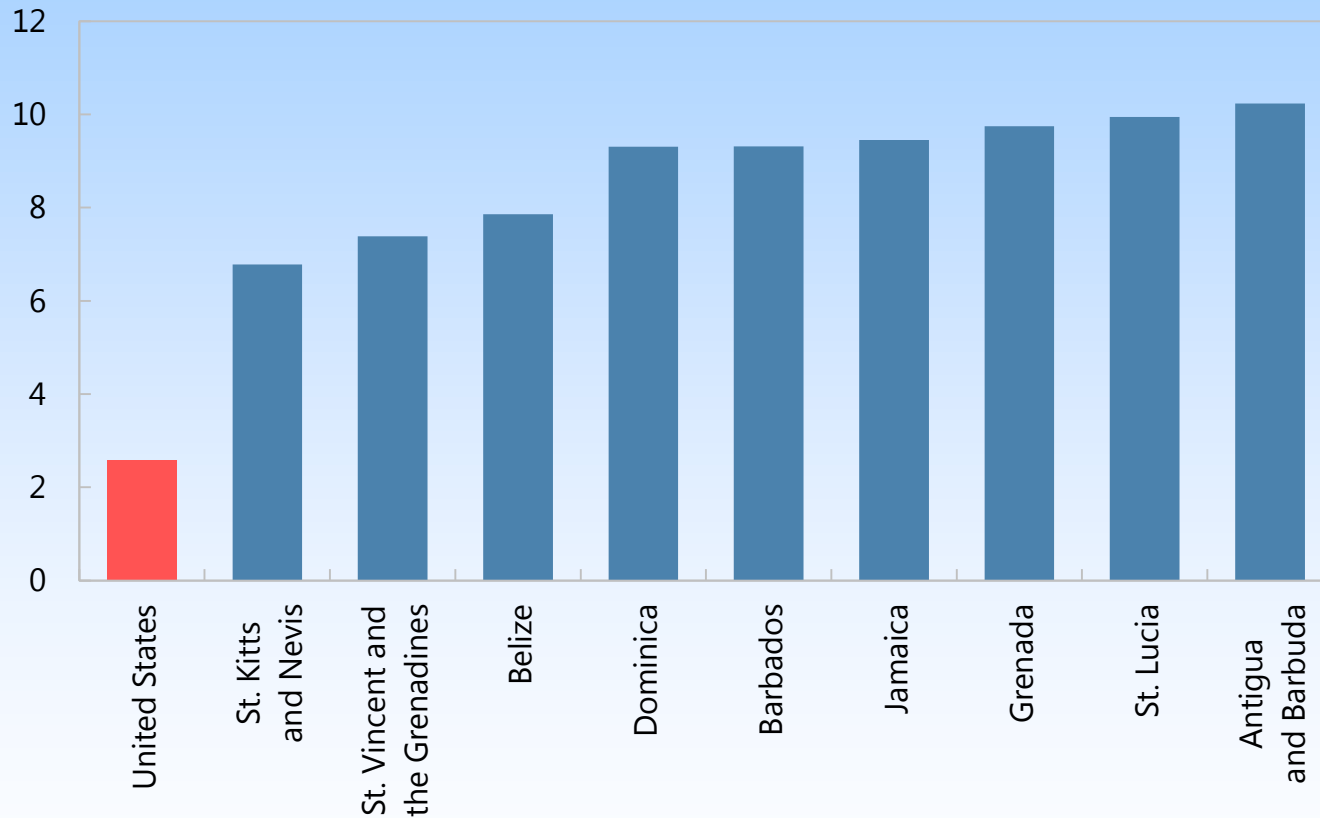


Sources: CARILEC Tariff Survey; and U.S. EIA.

¹ Includes data for the Bahamas, Barbados, Belize, Dominica, Grenada, Jamaica, St. Lucia and St. Vincent and the Grenadines; limited data available for Antigua and Barbuda and Nevis; excludes Trinidad and Tobago and Suriname.

... increasing the energy bill burden.

National Electricity Bill in Selected Caribbean Countries¹ (Percent of GDP)



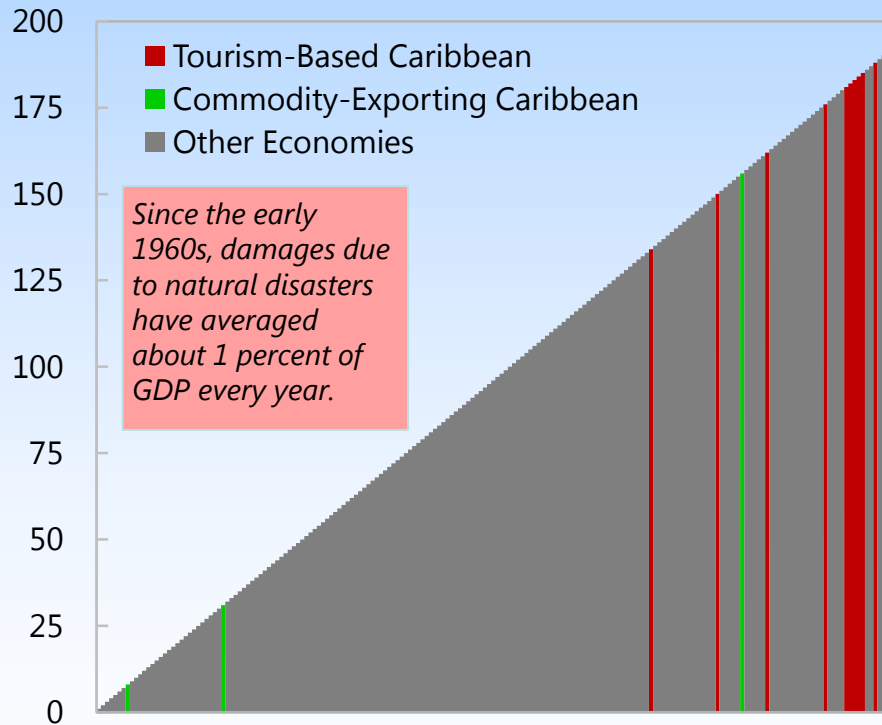
Sources: U.S. Energy Information Agency; IDB; CARILEC tariff survey; and IMF staff calculations.

¹ Based on total net consumption of electricity in 2011 and weighted average tariff rates for residential, commercial and industrial end-users.

Recurrent natural disasters have also set back economic activity.

Natural Disasters per Square Kilometer

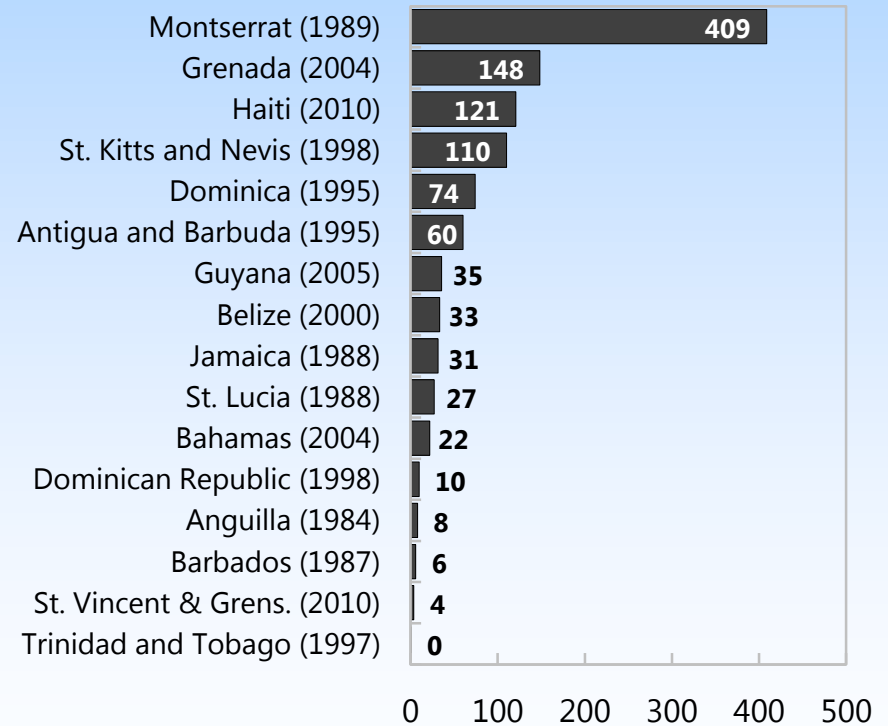
(Rank in world sample of 191 countries/territories)



Largest Disaster in Each Caribbean Country

1970-2012

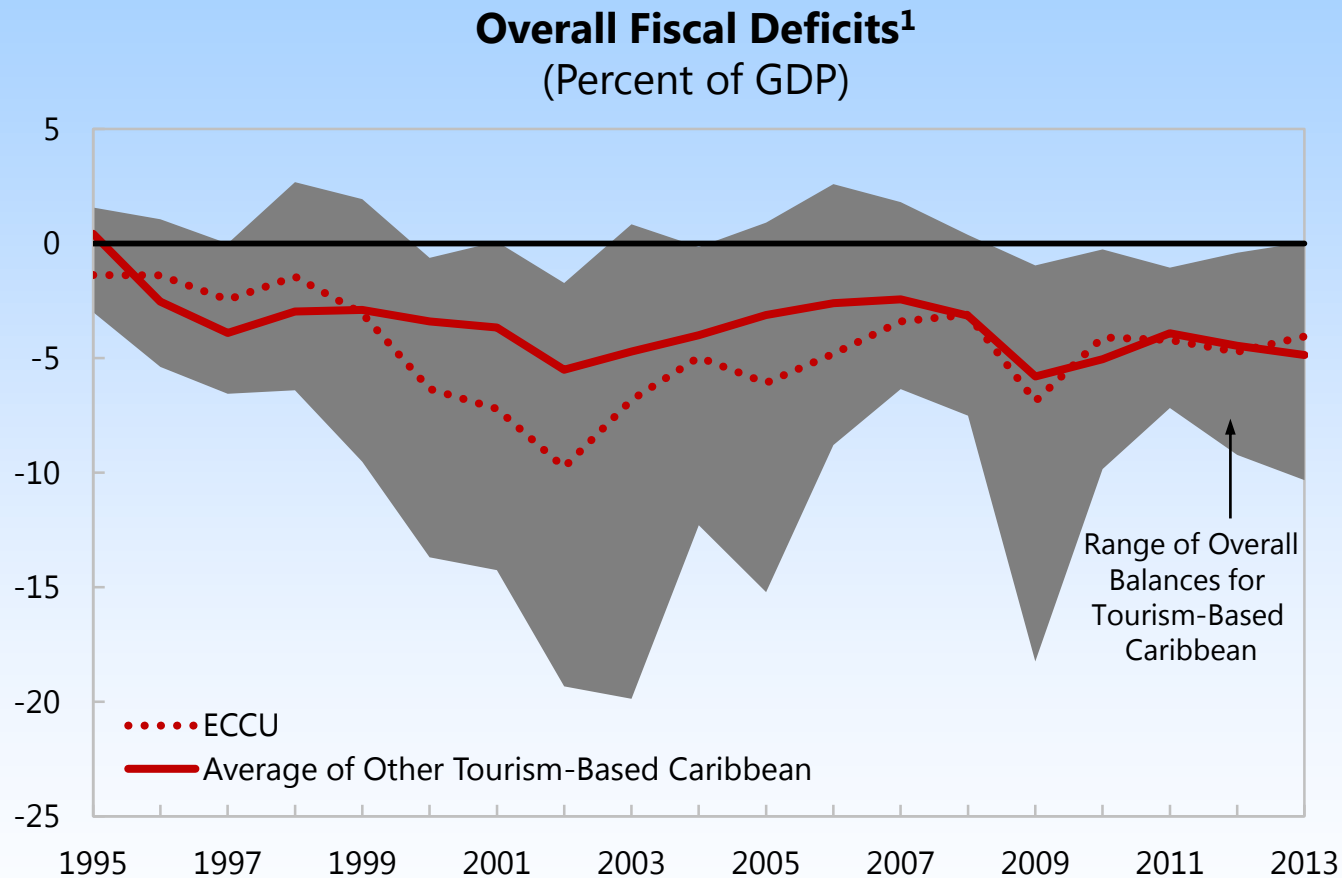
(Percent of GDP)



Sources: EM-DAT; World Development Indicators; and IMF staff estimates.

Sources: EM-DAT; WEO; and IMF staff calculations.

Low growth has contributed to elevated fiscal deficits...

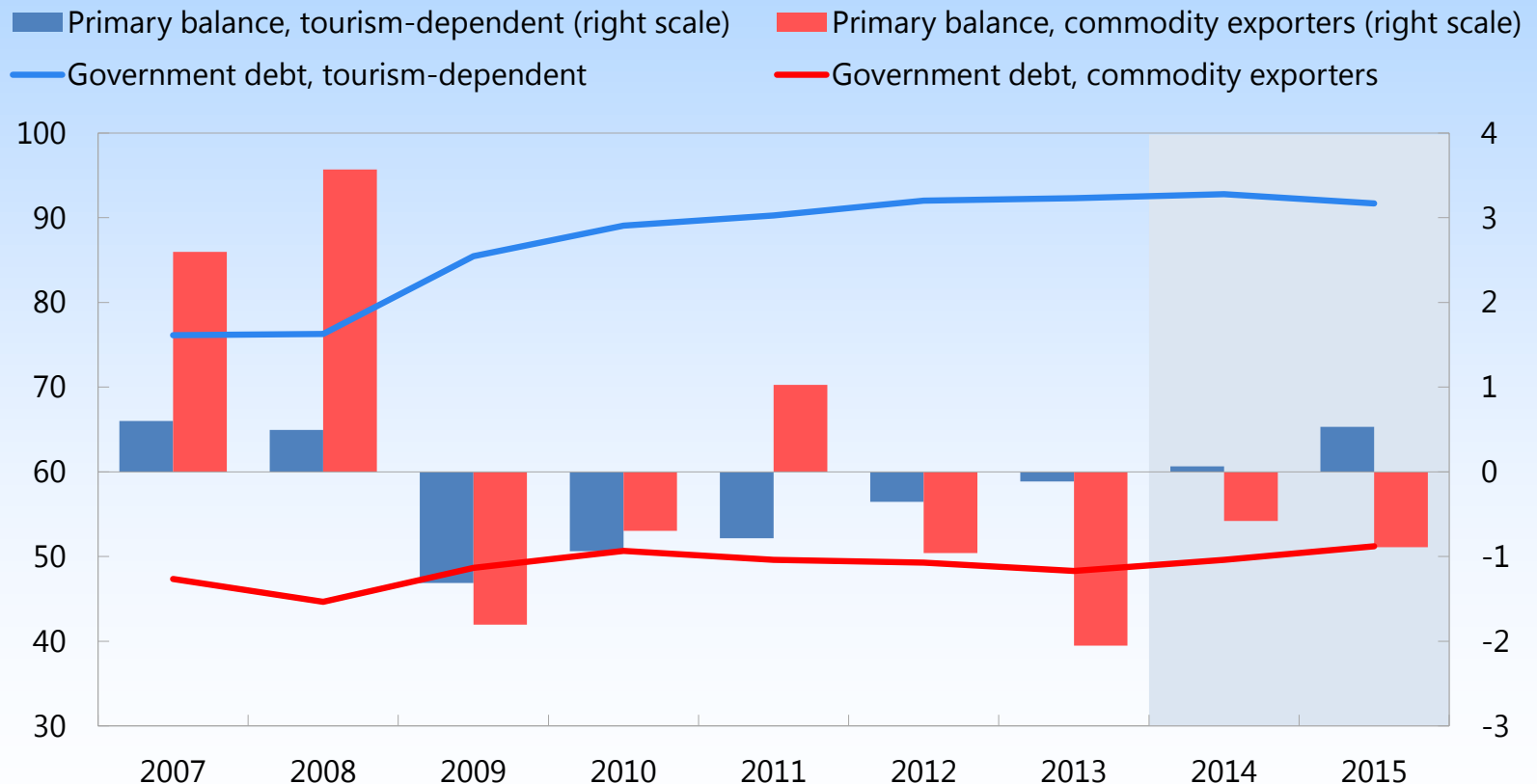


Sources: IMF, *World Economic Outlook*; and IMF staff estimates.

¹ Excludes direct Citizenship Program Revenues for Dominica over 2003-13 and St. Kitts and Nevis over 2005-13.

... which are expected to persist, despite improving primary balances in debt-constrained countries.

Fiscal Accounts¹ (Percent of fiscal year GDP)

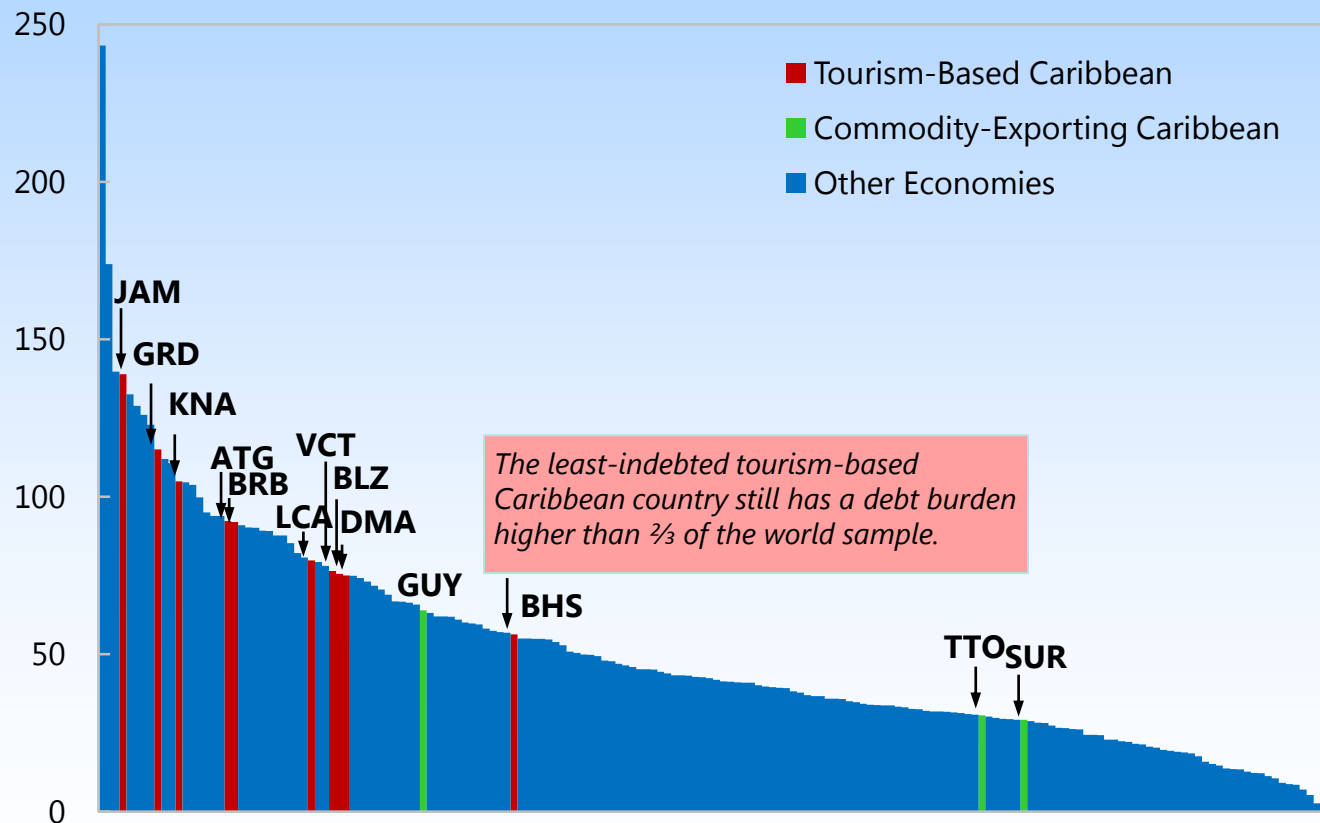


Sources: IMF, *World Economic Outlook*; and IMF staff estimates.

¹ Simple country averages.

The resulting high public debt burdens in turn are weighing on confidence and growth.

General Government Debt, 2013
(Percent of GDP, world sample of 177 countries)

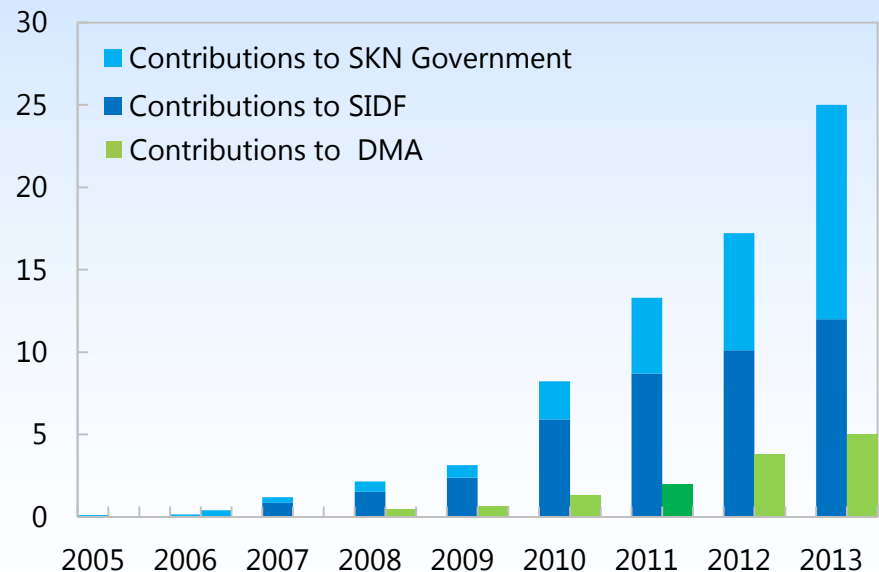


Source: IMF, *World Economic Outlook*.

In a few countries, citizenship-by-investment programs have provided relief...

- CBI inflows have surged in recent years
- Impact on **St. Kitts and Nevis** and **Dominica** is already large
- New programs just launched in **Antigua and Barbuda** and **Grenada** could also yield significant resources
- These inflows have already led to a robust recovery in St. Kitts and Nevis and *could* help support an economic recovery and improve macro balances in a few other economies

CBI Inflows in St. Kitts and Nevis and Dominica
(Percent of GDP)



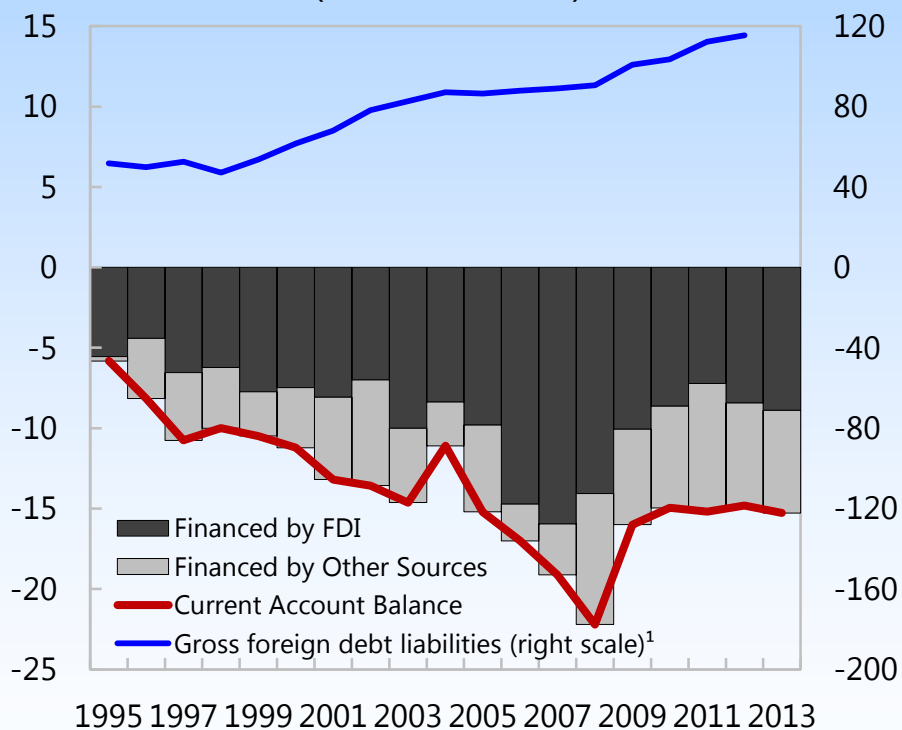
Sources: National authorities; and IMF staff calculations.

... but prudent management is key to containing the risks associated with these programs.

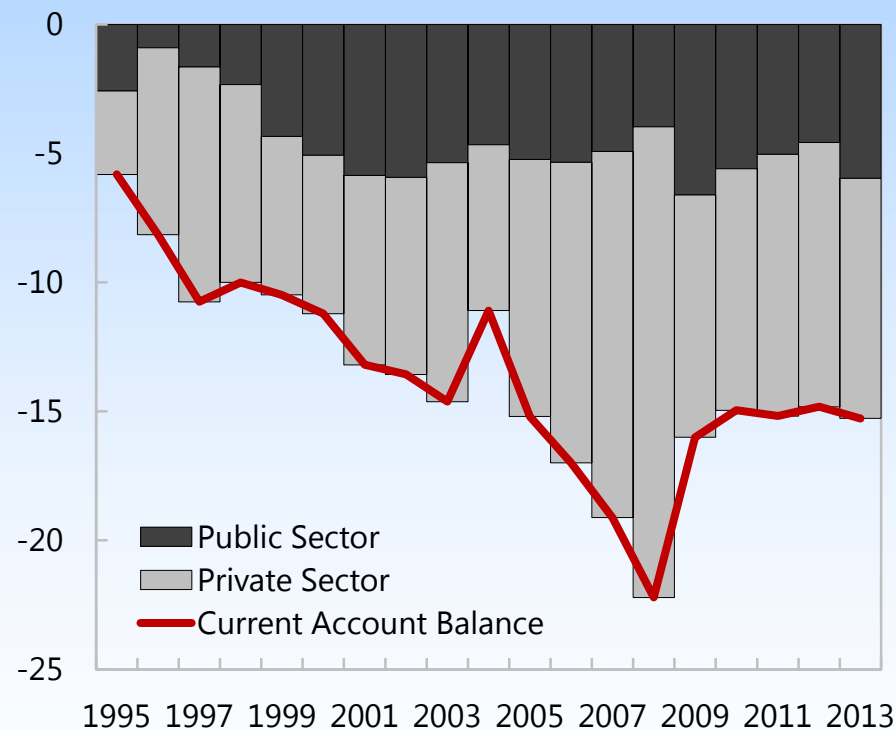
- **Large, volatile CBI inflows may increase macro vulnerability**
 - Economic overheating creates risks of Dutch Disease
 - Reduced fiscal discipline leading to increased dependence
 - Higher external vulnerability with risks of sudden stops
- **A prudent CBI framework is critical**
 - Pacing and regulating inflows into the private sector
 - Saving a significant share of public sector inflows to build fiscal buffers and reduce debt, while allowing for sustainable use of resources consistent with absorptive capacity
 - Enforcing a strict due diligence process and a prudent governance framework to reduce sustainability risks

Fiscal vulnerabilities are mirrored by very weak external positions, both public and private...

Tourism-Based Caribbean: Current Account Balance by Financing and External Debt
(Percent of GDP)



Tourism-Based Caribbean: Current Account Balance by Sector
(Percent of GDP)



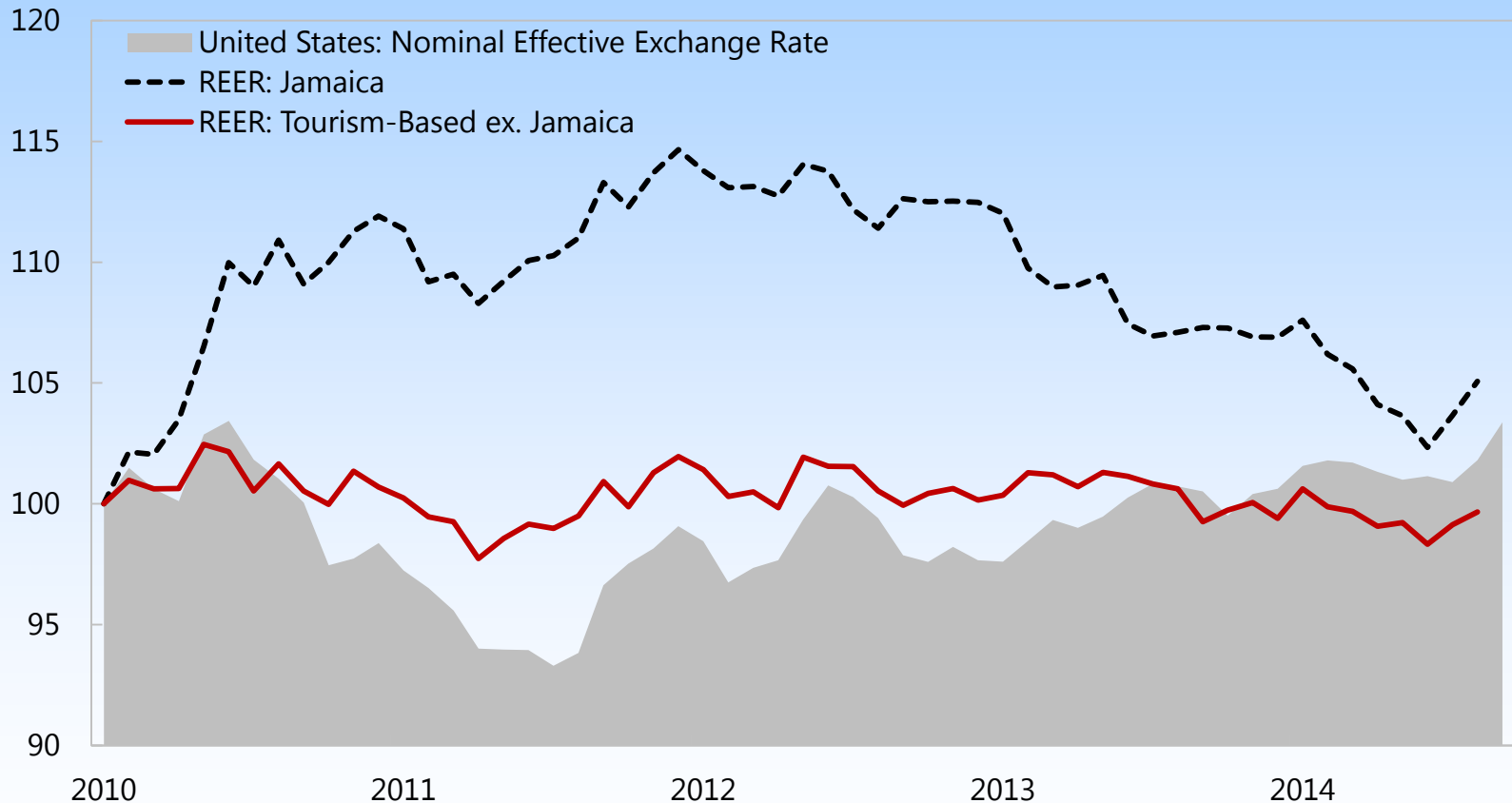
Sources: IMF, *World Economic Outlook*; and IMF staff estimates.

¹ Excluding the Bahamas and Barbados.

Sources: IMF, *World Economic Outlook*; and Fund staff estimates.

... and US\$ appreciation hurts competitiveness, despite some offset from low domestic inflation...

Exchange Rate Indices¹
(January 2010 = 100)

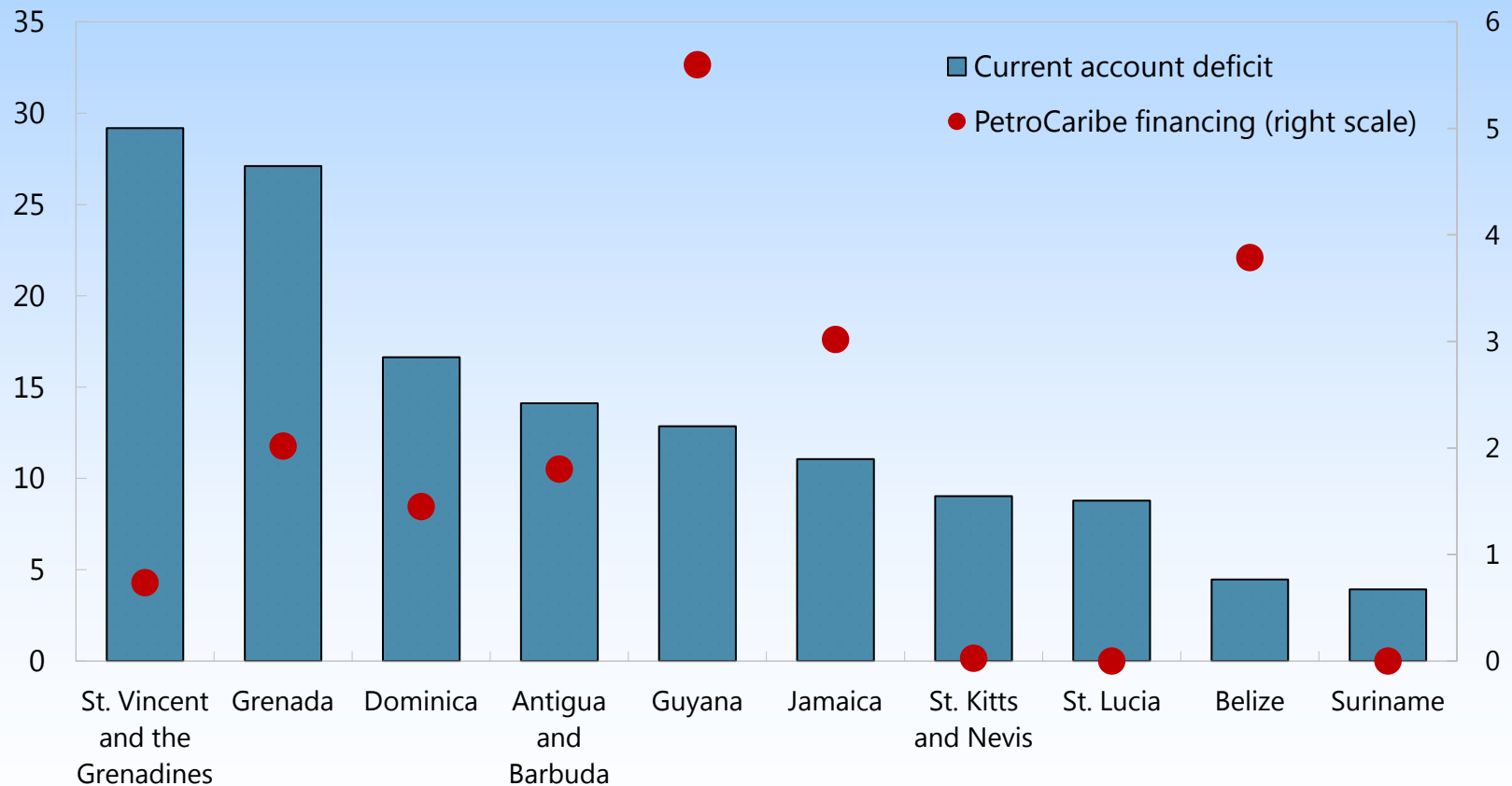


Sources: IMF staff calculations based on data from country authorities; IMF, *International Financial Statistics*; IMF, *World Economic Outlook*; Haver Analytics; and the Caribbean Tourism Organization.

¹ Real effective exchange rates calculated on the basis of CPI of four largest tourism-source countries as measured by tourist arrivals. Latest months' inflation data extrapolated from last observation of 12-month inflation. Regional averages calculated on the basis of countries' PPP GDP.

... while exposures to PetroCaribe create further near-term risks for some countries.

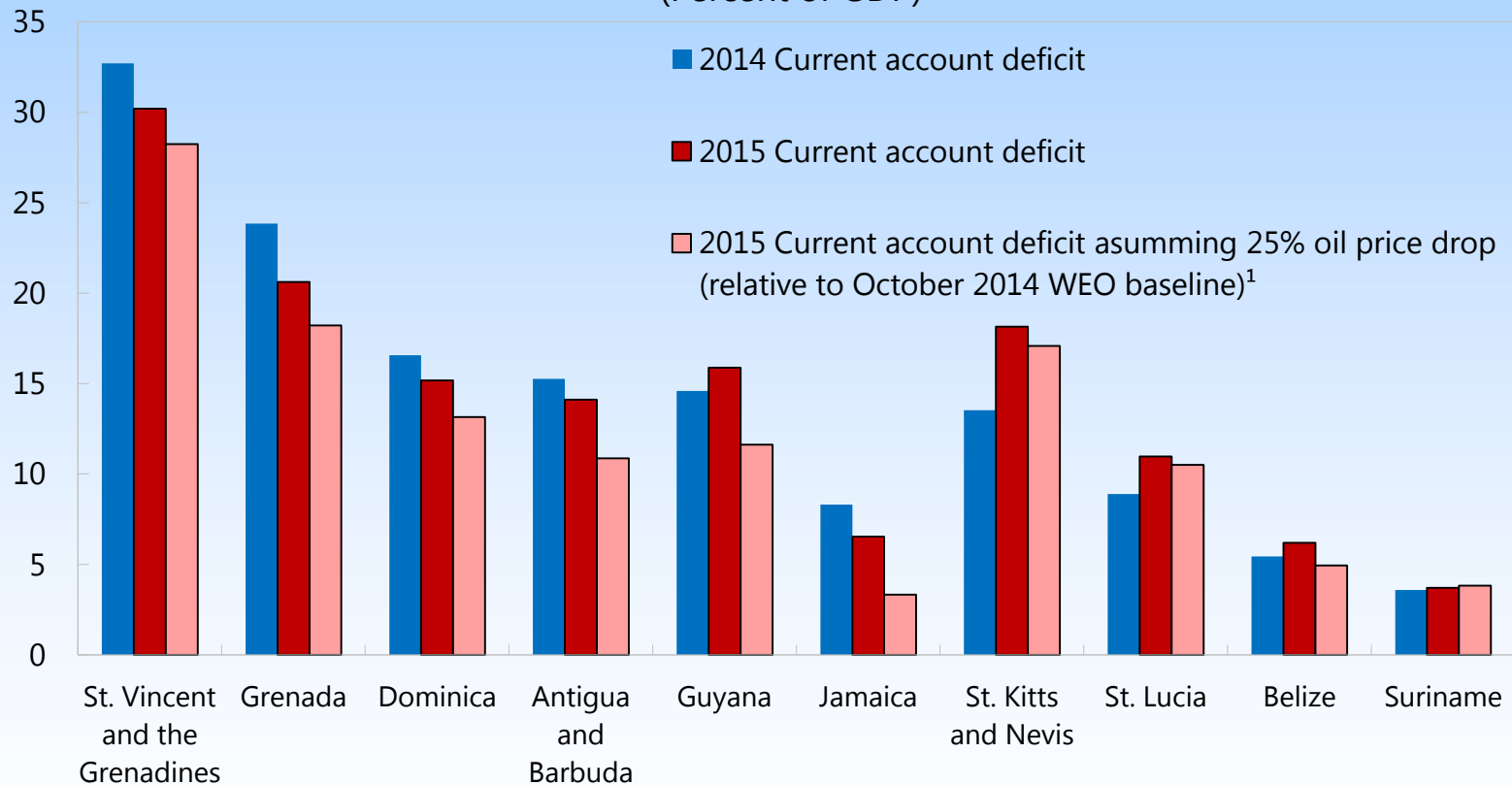
Current Account Deficit and PetroCaribe Financing, 2013
(Percent of GDP)



Sources: IMF, *World Economic Outlook*; and IMF staff estimates.

On the upside, lower fuel prices would help reduce current account deficits...

External Current Account Deficit with Lower Oil Prices
(Percent of GDP)



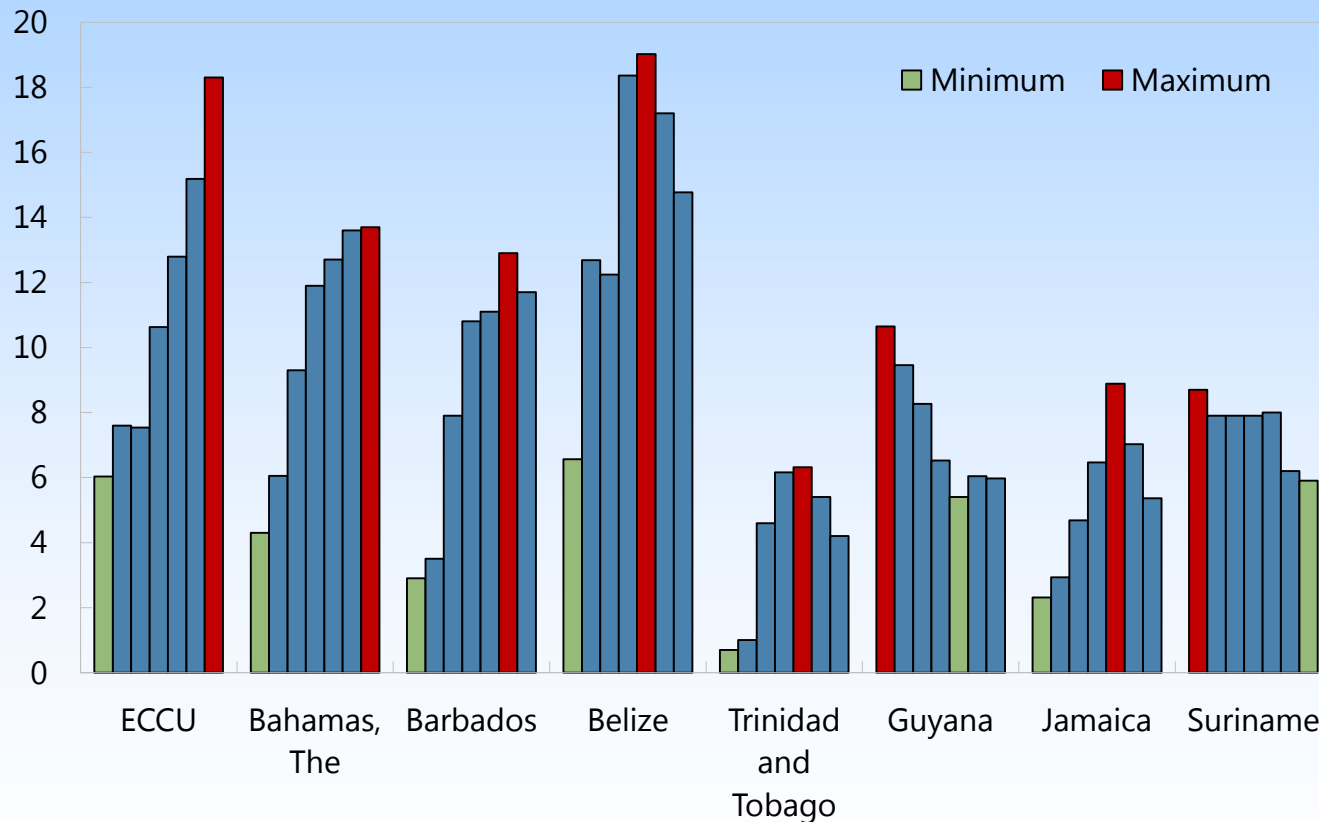
Sources: IMF, *World Economic Outlook*; and IMF staff estimates.

¹ October 2014 WEO baseline for 2015: US\$ 99/barrel. Scenario calculations assume no change in quantities in response to the price change.

Meanwhile, worsening bank asset quality adds to the challenges in several economies.

Nonperforming Loans, 2007–2013

(Percent of total loans)



Source: National authorities.

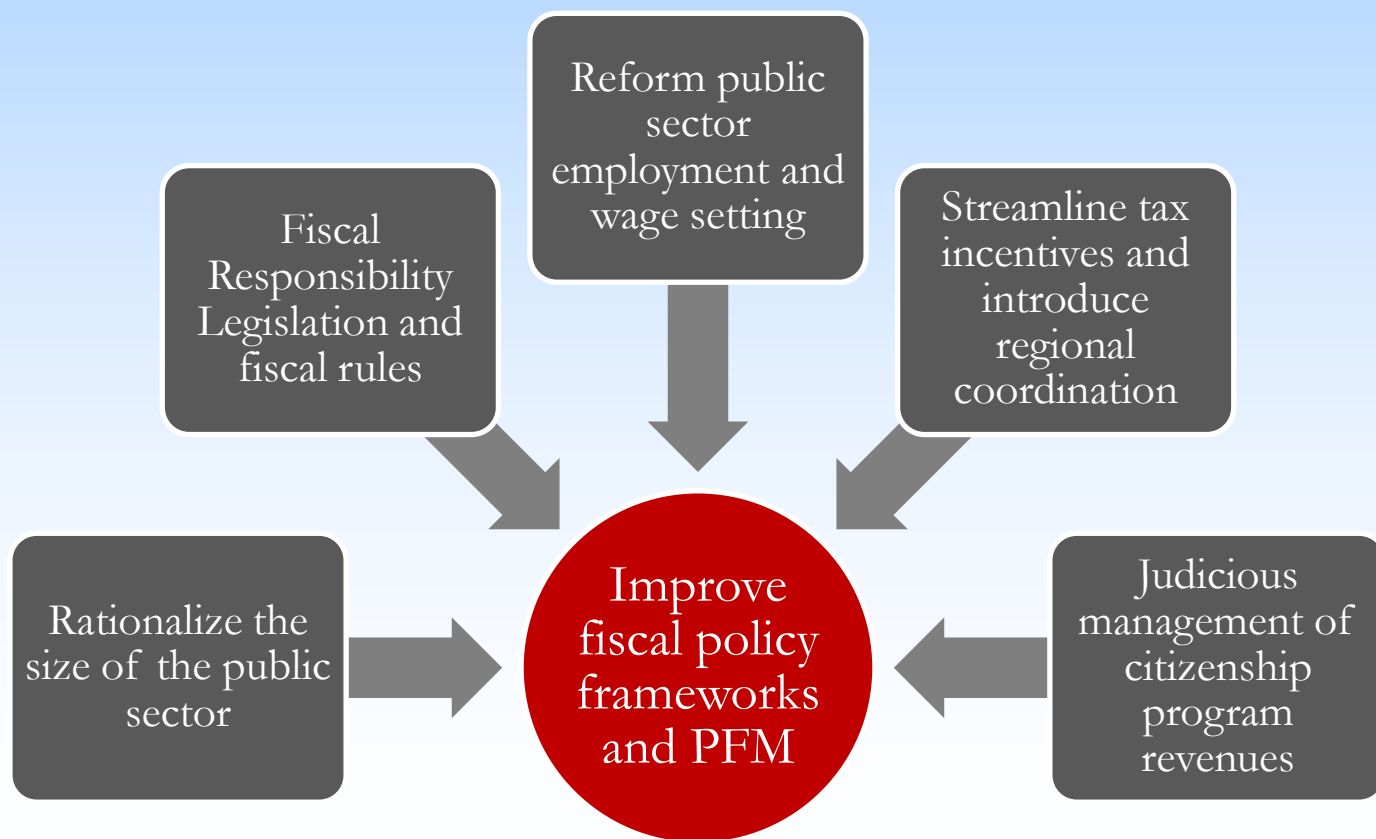
Outline: Testing Times for...

- The World
- The LAC Region
- The Caribbean
 - Growth
 - Fiscal
 - External
 - Financial

–Going Forward

To address these challenges, a multi-pronged strategy is needed, combining fiscal adjustment...

- Fiscal adjustment must be at the heart of any permanent solution, and underpinned by structural changes:



...with financial sector clean-up and steps to boost competitiveness.

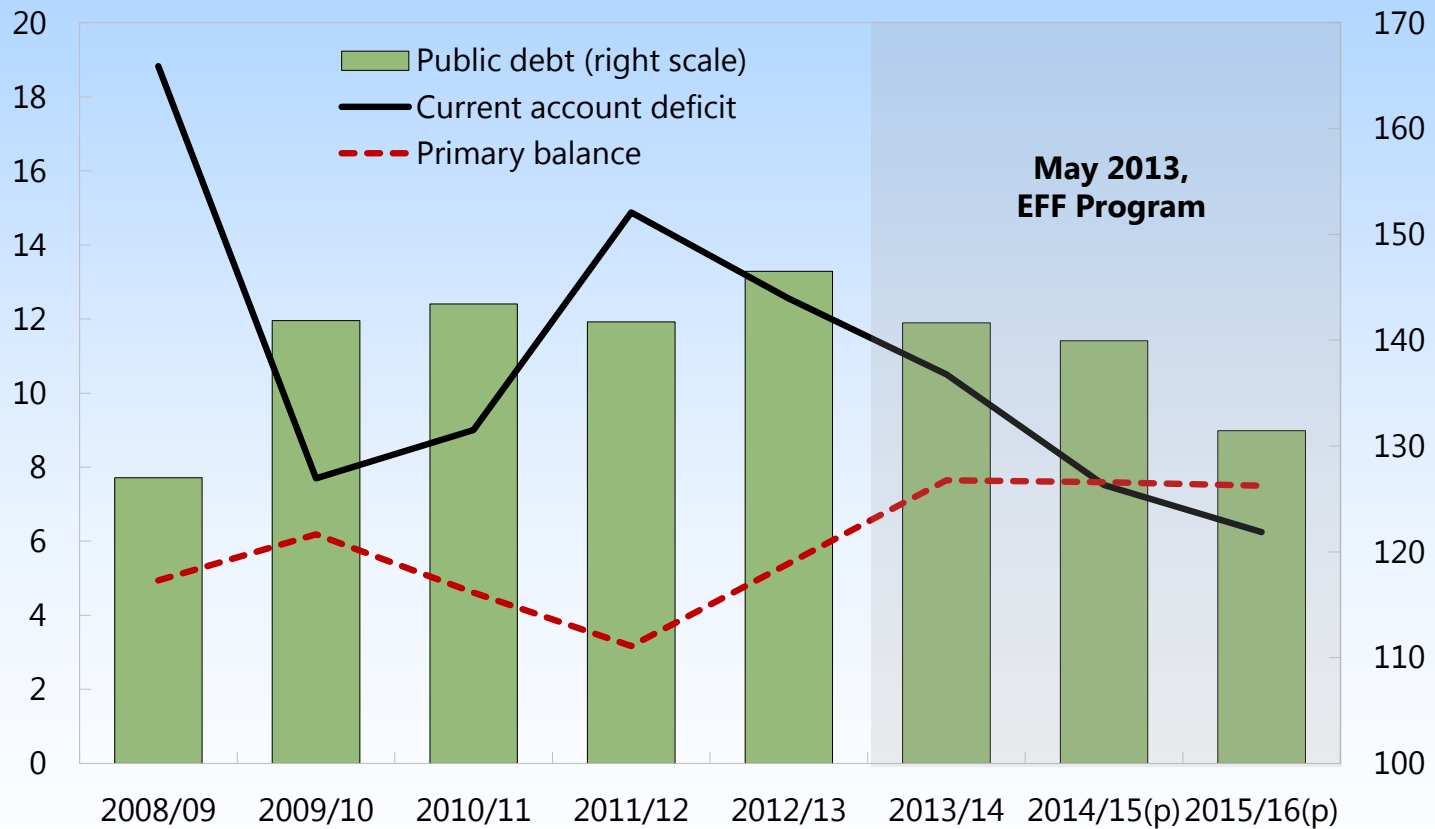
- Financial sector priorities in the ECCU:
 - Upgrade supervision and regulation to international norms
 - Asset quality reviews of banks
 - Strengthening banks' financial positions
- Improved competitiveness is key to restoring growth and external sustainability:
 - Intensify efforts to improve the business climate
 - Liberalize labor markets and improve training
 - Prioritize public investment to address infrastructure bottlenecks

A difficult road ahead, but some reasons for optimism....

- Policymakers' increasing willingness to take decisive action to make fundamental changes: e.g., Jamaica, Grenada, St. Kitts and Nevis
- Promising opportunities in health and education tourism, that offer high potential for growth and employment
- A lower oil bill?
- Potential “game-changing” opportunities to reduce energy costs, via increased use of natural gas and renewable energy

Jamaica's recent progress in strengthening fiscal and external positions is an encouraging example.

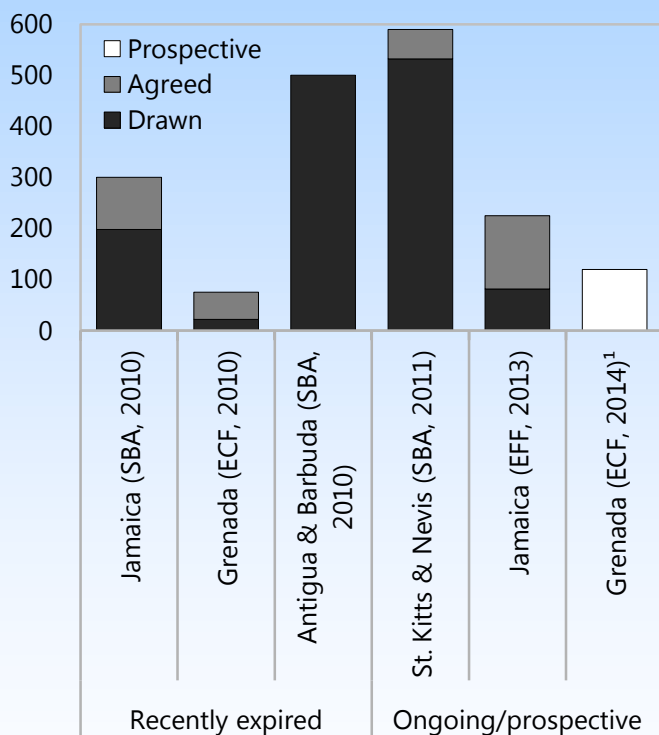
External Current Account and Primary Fiscal Balances
(Percent of GDP)



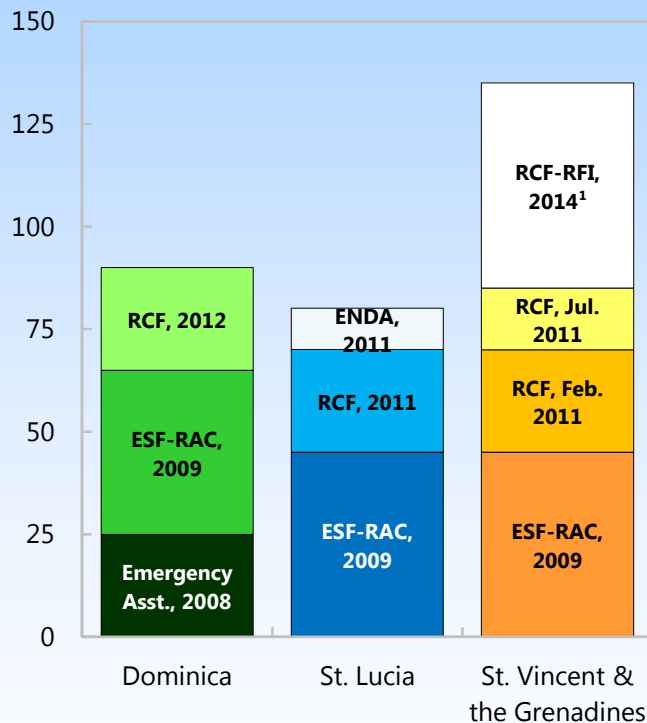
Sources: Bank of Jamaica; Ministry of Finance; and IMF staff calculations.

The IMF stands ready to help with a range of tools: programs, emergency credit, TA...

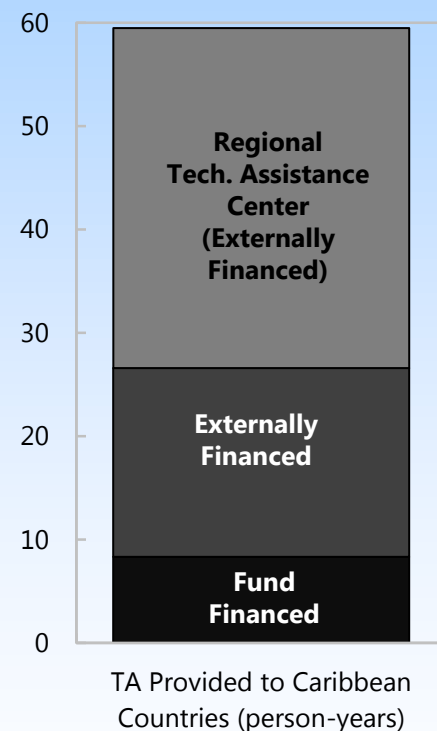
Recent Fund Programs (Percent of quota)



Emergency Assistance (Since 2008, percent of quota)



Technical Assistance



Source: IMF.

¹ Staff-level agreement on March 14, 2014.

Source: IMF.

¹ Prospective.

Source: IMF.

Thank You

