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St. Lucia: Request for Disbursement Under the Rapid-Access Component of the Exogenous Shocks Facility—Staff Report; Staff Supplement; Press Release; and Statement by the Executive Director for St. Lucia.

Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. In the context of the Request for Disbursement Under the Rapid-Access Component of the Exogenous Shocks Facility for St. Lucia, the following documents have been released and are included in this package:

- The staff report for the Request for Disbursement Under the Rapid-Access Component of the Exogenous Shocks Facility, prepared by a staff team of the IMF, following discussions that ended on June 11, 2009, with the officials of St. Lucia on economic developments and policies. Based on information available at the time of these discussions, the staff report was completed on July 10, 2009. The views expressed in the staff report are those of the staff team and do not necessarily reflect the views of the Executive Board of the IMF.
- A staff supplement on the joint IMF/World Bank Debt Sustainability Analysis.
- A Press Release summarizing the views of the Executive Board as expressed during its July 27, 2009 discussion of the staff report that completed the request.
- A statement by the Executive Director for St. Lucia.

The policy of publication of staff reports and other documents allows for the deletion of market-sensitive information.

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INTERNATIONAL MONETARY FUND

ST. LUCIA

Request for Disbursement Under the Rapid-Access Component of the Exogenous Shocks Facility

Prepared by the Western Hemisphere Department
(In consultation with other Departments)

Approved by Rodrigo Valdés and Aasim Husain

July 10, 2009

Executive Summary

Context. St. Lucia has been negatively affected by the global downturn. Following a lackluster performance of the tourism sector in the fourth quarter of 2008, there was a further sharp decline in visitor arrivals in the first quarter of 2009. Falling visitor and spending levels have led to job losses in the tourism sector, and are affecting plans for the construction of new (and expansion of existing) hotels and resorts. Given that government tax revenues, foreign exchange reserves, and employment levels are inextricably linked with the performance of the tourism sector, the damage to the economy from the crisis has been widespread. Consequently, the authorities have requested a disbursement under the Fund's Rapid-Access Component of the Exogenous Shocks Facility (RAC-ESF) to help mitigate the impact of the crisis on the economy.

Policy discussions focused on:

- **Preserving recent gains in fiscal consolidation while addressing the impact of the shock.** Allowing automatic fiscal stabilizers to work during the downturn and streamlining existing blanket subsidies (including on energy prices) to create the fiscal space for additional spending on social safety nets and infrastructure.

- **Achieving medium-term debt sustainability.** Continue implementing sound macroeconomic policies, including revenue and expenditure measures, aimed at entrenching fiscal consolidation and securing the debt-to-GDP ratio on a solid downward trajectory.

- **Strengthening financial-sector regulatory oversight.** Overhauling regulation and supervision of nonbank financial institutions in collaboration with regional counterparts to help prevent future problems such as those associated with the collapse of the CL Financial Group.

Access under the RAC-ESF. On the basis of the authorities' commitment to sound macroeconomic policies, staff supports the request for access of SDR 6.89 million, equivalent to 45 percent of quota.

Fund relations. St. Lucia has not had a financial arrangement with the Fund for decades. Access to Fund financing amid the current global downturn would signal endorsement of the authorities' policy agenda, catalyze financing from other international partners, and mitigate the loss of reserves.

Contents

I. BACKGROUND

1. **As a small, open, tourism-based economy, St. Lucia is highly vulnerable to exogenous shocks.** Tourism accounts for over three-quarters of exports, and the import content of both consumption and foreign direct investment (FDI) is very high (Figure 1). The economy has been buffeted by the global economic downturn, which has hobbled the tourism and construction sectors, with potential spillovers to the financial sector.

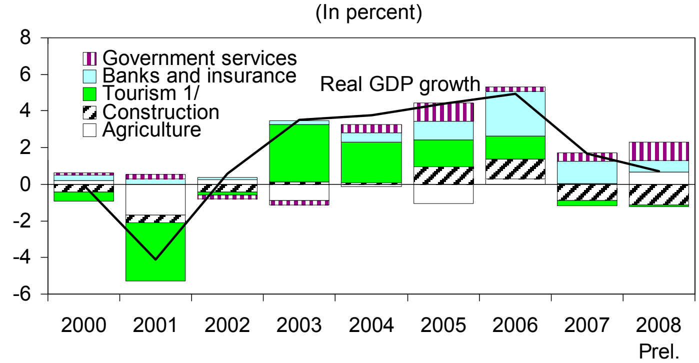
2. **The authorities have requested a purchase under the Rapid-Access Component of the Exogenous Shocks Facility (RAC-ESF).** Access under the RAC-ESF would support their efforts to mitigate the adverse impact of the global downturn on the economy. The mission that visited Castries during June 8–11 assessed the immediate balance of payments needs and reviewed the authorities' policy measures to address the sudden shock.[1]

3. **The thrust of the authorities' policies in recent years has been consistent with Fund advice.** The authorities have followed recommendations on bolstering revenues, particularly on the oil pricing mechanism, the value-added tax, and reforms to social security. However, they have been less responsive to staff recommendations to rein in capital spending, and progress with financial sector reforms has been slow.

II. RECENT ECONOMIC DEVELOPMENTS

4. **Real GDP growth slowed in 2007–08.** Spurred by preparations for the Cricket World Cup, St. Lucia's economy grew by about 5 percent in 2006. However, slowing construction and tourism activity, together with a hurricane-induced contraction in banana exports, reduced growth to an estimated 1.7 percent and 0.7 percent in 2007 and 2008, respectively. The unemployment rate increased by three percentage points to 16.8 percent during the same period. Despite being underpinned by the regional currency board arrangement, annual inflation reached 7.2 percent in 2008, reflecting high international prices of energy and food. With the decline in these prices, inflation has fallen to 3.2 percent by end-March 2009.

St. Lucia: Sectoral Contribution to GDP Growth
(In percent)



Sources: St. Lucia authorities; Eastern Caribbean Central Bank.
1/ Tourism includes wholesale and retail trade, hotels and restaurants, air transport and half of local transport.

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[1] The staff team comprised Mr. Cashin (Head), Ms. Wagner, and Messrs. Nassar and Perrelli (all WHD). Mr. McGoldrick (OED) joined for the final discussions. The mission met with the Prime Minister (and Minister of Finance) Stephenson King, the Permanent Secretary of the Ministry of Finance, and other senior government officials.

5. **Progress was made in reducing macroeconomic imbalances in 2008.** The government achieved a primary fiscal surplus of 0.2 percent of GDP, reflecting constraints on capital expenditure and higher tax collection due to an amnesty on tax arrears, and despite measures taken to mitigate the impact of soaring food and fuel prices. Public debt edged down marginally to about 67⅓ percent of GDP (Figures 2 and 3). Preliminary data for 2008 suggest a narrowing in the external current account deficit, due to an increase in exports of bananas and alcoholic beverages. The deficit was largely financed by FDI and a drawdown of commercial banks' foreign assets.

St. Lucia: Key Macroeconomic Indicators, 2004–08

	2004	2005	2006	2007	Prel. 2008
	(Annual percentage change)				
Real GDP at factor cost	3.8	4.4	4.9	1.7	0.7
Inflation (period average)	1.2	3.9	4.1	2.2	7.2
Inflation (end of period)	3.4	4.5	1.4	6.6	3.8
Real effective exchange rate (end of period, - = depreciation)	-4.8	-0.5	0.5	-3.6	1.1
Terms of trade (- = deterioration)	-5.8	-3.8	-13.2	-12.8	-14.0
	(In percent of GDP, unless otherwise indicated)				
Primary fiscal balance	-0.7	-3.0	-2.6	0.7	0.2
Overall fiscal balance	-3.8	-6.0	-5.9	-2.5	-3.3
Public sector debt	66.0	67.0	65.0	70.3	67.3
Current account balance	-10.9	-17.1	-30.2	-40.6	-34.5
Imputed net international reserves (in millions of U.S. dollars)	130.2	114.2	132.2	151.2	140.3

Sources: St. Lucia authorities; and Fund staff estimates.

6. **Credit to the private sector slowed considerably in 2008.** The weak economic environment contributed to a significant drop in demand for private sector credit. Moreover, with broad money growth decelerating, commercial banks relied on drawing down their foreign assets to expand credit to public enterprises (Figure 4). Interest rates, including yields on the Regional Government Securities Market (RGSM), remained stable.

7. **Prudential indicators have weakened.** Although the earnings performance of commercial banks improved, provisioning, asset quality, and capital adequacy ratios for local banks declined in 2008, reflecting the weak economic environment (Figure 5). Nonperforming loans (NPLs) of local banks increased and, while below the ECCU average, are higher than the ECCB's prudential target of 5 percent. The rise in the NPL ratio partly reflects the combination of the credit boom in preceding years and the current economic downturn.

Banking Sector: Selected Financial Soundness Indicators, End-December 2008 1/

(In percent)

	St. Lucia	ECCU Average
Capital adequacy ratio (domestic banks)	15.6	20.1
Nonperforming loans/total loans	6.6	7.7
Gross government exposure/total assets	20.6	17.8
Provisions for loan losses/total loans	2.5	1.8
Provisions for loan losses/nonperforming loans	37.5	23.4
(Pre-tax) return on average equity (domestic banks)	25.9	21.3
(Pre-tax) return on average assets	3.2	2.6

Source: ECCB.

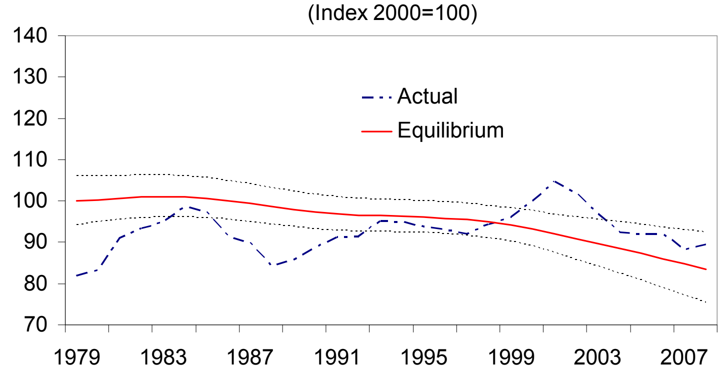
1/ Prudential indicators are based on commercial banks' own reporting, with infrequent onsite verification by the ECCB.

8. **While the banking system has so far weathered the global crisis, the nonbank financial sector has suffered problems.** In particular, while the collapse of the Trinidad and Tobago-based CL Financial Group has not adversely affected confidence in the overall financial system, it has highlighted weaknesses in the regulation of nonbanks. Credit unions and insurance companies compete with commercial banks for deposits and loans, but are not subject to similar supervisory standards. Throughout the region, insurance companies had been allowed to offer deposit-like products that yielded annual interest rates far in excess of those offered by commercial banks. The higher interest rates reflected the much riskier investment activities in which the head offices of the companies were engaged. The CL Financial Group's net liabilities in St. Lucia are estimated at US$68 million (about 6.8 percent of GDP). However, the fiscal implications of the financial collapse are likely to be much lower, as St. Lucia's share of total ECCU insurance company deposits is very small, and the local statutory fund for one of the two CL Financial insurance subsidiaries—the British American Insurance Company—is one of the few in the Caribbean with a surplus balance.

9. **St. Lucia's real effective exchange rate appears to be in line with fundamentals.** Staff analysis indicates that St. Lucia's actual real effective exchange rate (REER) was not far away from estimates of its equilibrium level in 2008, reflecting the depreciation through mid-2008 of the U.S. dollar against major currencies. Since 2000, the equilibrium REER has also fallen, due to the ongoing decline in both

St. Lucia: Actual and Equilibrium REER, 1979–2008 1/

(Index 2000=100)



Sources: IMF, Information Notice System; and Pineda, Cashin, and Sun, "Assessing Exchange Rate Competitiveness in the Eastern Caribbean Currency Union," IMF Working Paper WP/09/78.

1/ The dotted lines around the equilibrium exchange rate represents 90 percent confidence intervals of the prediction.

the terms of trade (of goods and services) and relative tourist arrivals, and the accumulation of net foreign liabilities (Figure 6).

III. Economic Impact of the Global Recession

10. **St. Lucia is set to experience a recession in 2009, and economic activity is likely to remain weak in 2010.** Real GDP is projected to contract by 2½ percent in 2009, slightly larger than that for the ECCU as a whole, reflecting the economy's greater dependence on tourism. A further but milder contraction is projected for 2010. Global economic conditions, according to the latest World Economic Outlook, are expected to begin to recover in 2010, just in time for St. Lucia's 2011 tourism season. Economic activity is thus expected to begin to recover only in 2011.

11. **In an initial response to the global crisis, the FY 2009–10 budget sought to bolster growth and protect the poor.** As a result, the budget (approved in April 2009) envisaged a deterioration in the primary fiscal balance of about 3 percentage points of GDP. This reflected a marginal decline in current revenues, while total revenue and grants were projected to increase by 2 percentage points of GDP, due to an increase in grants (about 2½ percentage points of GDP) from the European Union and Taiwan Province of China. Current expenditures were expected to increase, largely owing to a rise in social spending. Capital expenditures were also budgeted to increase by about 4 percentage points of GDP to reach 15 percent. The overall deficit (about 6½ percent of GDP) was not fully financed; identified financing only totaled 4½ percent of GDP—comprising concessional loans from the Caribbean Development Bank (2.1 percent of GDP) and loans from the Kuwaiti Fund (0.6 percent of GDP) and the World Bank (1.7 percent of GDP). The resulting government financing needs could be difficult to accommodate in the current financial environment.

12. **Although the external current account deficit is projected to narrow in 2009, the overall balance of payments position is expected to deteriorate.** The decline in FDI-related imports and the international prices of energy and food are expected to more than offset the decline in tourism receipts and remittances from abroad, contributing to a narrowing of the current account deficit in 2009. However, the projected deterioration in the financial account (comprised largely of a drop in FDI and a reversal of the drawdown of commercial bank net foreign assets) would more than offset the narrowing of the current account deficit,[2] resulting in an external financing gap on the order of EC$59 million (about US$22 million or 2.2 percent of GDP).

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[2] The financial account includes net errors and omissions.

St. Lucia: Estimated Net Impact of Tourism and FDI Shock
(In millions of EC dollars, unless otherwise indicated)

	2008	2009	Difference
Current Account	-919.3	-467.4	451.9
Of which			
(A) Exports	501.6	457.1	-44.5
(B) Imports	-1,559.9	-915.9	644.0
Of which			
(C) FDI-related (both fuel and nonfuel)	-198.0	-143.0	55.0
(D) Fuel and Food (price effect)	-59.8	-40.6	29.2
(E) Travel (net)	273.0	215.0	-58.0
(F) Private transfers	30.7	27.8	-2.9
Capital and Financial Account 1/	909.7	408.5	-501.2
Of which			
(G) Foreign direct investment	282.8	204.3	-78.6
Other multilaterals (CDB and the World Bank)		102.7	…
Requested ESF		28.8	…
Overall balance	-9.6	-58.9	…
Financing	9.6	58.9	…
Change in imputed reserves	8.8	58.9	…
(H) Gross impact (A+E+F+G)	…	…	-184.0
(I) Net impact (H+C+D)	…	…	-99.8
Memorandum items:			
Request for ESF (in percent of GDP)		1.1	…
Imputed reserves	378.8	319.8	…
Imputed reserves (in percent of M2)	16.3	14.1	…
Nominal GDP	2,664.3	2,675.7	

Sources: St. Lucia authorities; ECCB; and Fund staff estimates and projections.

1/ Includes net errors and omissions.

13. **Risks to the outlook are large and on the downside, given the uncertainty regarding the duration and severity of the global downturn.** Negative risks include a deterioration in the fiscal position, credit constraints and spillover effects from the collapse of the CL Financial Group, and slower recovery in the major tourism-source countries of the U.K. and the U.S., which may dampen tourism demand and FDI inflows. On the positive side, regional initiatives to defuse further rounds of the financial crisis may mitigate the downturn.

IV. Policy Discussions

14. **St. Lucia faces multiple constraints on policy responses to address the impact of the global crisis:**

- As a member of the Eastern Caribbean Currency Union (ECCU), monetary policy must be focused on preserving the quasi-currency board arrangement.

- In spite of progress toward reducing fiscal imbalances in recent years, public debt has increased from 65 percent of GDP in 2006 to 67⅓ percent of GDP in 2008, leaving little room for fiscal stimulus to boost growth in the downturn.

- Due to the very high import content of consumption and investment, fiscal stimulus is less likely to be effective in stimulating domestic output.

- About 75 percent of St. Lucia's current revenue is generated by indirect taxes, which generally tend to comove proportionately with the output gap.

- Transfer programs—in particular unemployment, welfare, and other social protection programs—are not well developed; even when they exist, their poor countercyclical design limits their impact on declining domestic output.

- Lack of capacity in the civil service poses institutional challenges for scaling up public expenditure quickly and efficiently.

- The labor market is relatively inflexible, and structural reforms to increase flexibility would take time to implement.

Against this background, policy discussions focused on maintaining macroeconomic stability and supporting economic activity with the tools available.

A. Fiscal Policy

15. **The fundamental challenge for FY 2009–10 is defining the role fiscal policy can play in mitigating the adverse effects of the weak economic environment, without derailing financial and macroeconomic stability.** The limited scope for increased discretionary spending and the deterioration in social conditions—with high and rising unemployment—would imply a refocusing of expenditure toward social protection. The mission sought the authorities' commitment to a credible strategy that would maintain government finances on a medium-term sustainable footing, while preserving and possibly expanding pro-poor spending.

16. **The authorities recognized the risks of increasing the primary fiscal deficit in 2009, as envisaged in the budget.** They shared staff's view that the current difficult economic environment necessitates adjustment to their budget, including less optimistic revenue projections, scaling back on capital spending, limiting public sector wage increases, and raising fuel prices.

17. **Consequently, the authorities agreed with an adjustment scenario in which automatic stabilizers are allowed to work—with revenue and current expenditure items adjusting automatically to the weak economic environment.** This scenario also envisages strengthening spending on a targeted social safety net. With total capital expenditure

curtailed to about 10 percent of GDP, in line with available concessional funding[3] and additional revenue measures (as described below), the primary fiscal surplus would reach 0.8 percent of GDP in FY 2009–10 while the overall deficit will reach 2.9 percent of GDP (3.6 percentage points lower than envisaged in the budget). Under this scenario, the public debt-to-GDP ratio would increase by about 2½ percentage points of GDP to about 70 percent this year, largely owing to the contraction in economic activity.

18. **Staff welcomed the authorities' commitment to introduce additional revenue measures this fiscal year, including, most importantly, a flexible oil pricing mechanism.** Retail prices of petroleum products in St. Lucia were the lowest in the ECCU for most of 2008, which led to a dramatic decline in the effective tax rate. The new pricing mechanism has the potential to boost fiscal revenue by ensuring that the revenue authorities garner the full amount of the legislated consumption tax as world petroleum prices change. The authorities intend to implement the new pricing mechanism by August 2009, with the consumption tax set at a level to yield about 1 percent of GDP. Among other revenue measures, the authorities have also increased taxes on alcoholic beverages, cigarettes, and vehicle licensing, and are implementing a market valuation-based property tax. These revenue measures should allow for broadly stable current revenues, despite the projected economic downturn.

19. **Staff urged expenditure rationalization and increased spending efficiency to create fiscal space for additional social spending.** The authorities intend to contain increases in public sector wages and headcount, within the context of broader civil service reforms aimed at increasing productivity and efficiency, and strengthen social spending. Moreover, the government introduced a voluntary 10 percent pay-cut for all members of Cabinet. The authorities also plan to cut back on unproductive spending, including on the operations of loss-making public enterprises. Fiscal space will also be created by enhancing the efficiency of spending programs, including by implementing a formal public sector investment program and rolling back the increases in broad-based consumption subsidies that were introduced in response to the surge in international fuel and food prices.

20. **The above measures would create the fiscal space for higher social spending, while reducing the overall fiscal deficit**. Thus, the authorities intend to spend an additional 1 percent of GDP to keep the most vulnerable St. Lucians covered under a variety of social safety nets. This includes an increase in pension allowances and funding for social protection projects, as well as better targeting of the conditional cash transfer program and streamlining of programs that are not cost-effective.

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[3] Includes funding from development partners such as the Caribbean Development Bank, the Kuwaiti Fund, and the World Bank.

21. **The mission welcomed the authorities' restatement of their commitment to introduce a VAT in April 2010.** In particular, the authorities' intend to establish a uniform rate (15 percent) VAT with a very limited number of zero-rated and exempt products and services, which could yield an additional 2½ percentage points of GDP in revenue. Staff noted that such a VAT regime would be among the best-designed in the region and would be simple to administer, thereby strengthening incentives to comply with the tax regime.

22. **The authorities recognized the need to address fiscal imbalances decisively to ensure medium-term debt sustainability.** However, because the contraction in GDP, together with the authorities' infrastructure investment plans, may raise the public debt-to-GDP ratio in the short-term, the mission urged the authorities to continue their efforts to strengthen their debt management capacity (Box).[4] With a longer-term perspective, the authorities' adjustment scenario, as illustrated in the Debt Sustainability Analysis and discussed above, should allow St. Lucia's public debt-to-GDP ratio to decline to about 52 percent by 2020, well below the benchmark debt target of 60 percent set by the ECCB for 2020. Accordingly, despite the exogenous shock of the economic and tourism downturn and additional borrowing from the Fund and other creditors, St. Lucia is expected to remain at moderate risk of debt distress.

B. Structural Policies

23. **Recent financial sector difficulties call for stronger and more proactive financial sector supervision and regulation.** The economic slowdown is likely to increase credit risk and, thus, nonperforming assets, thereby weakening financial institutions' balance sheets. To this end, the authorities are strengthening the regulatory and supervisory framework for nonbanks (including insurance companies) to help avoid spillovers to the domestic banking system and prevent the reemergence of schemes similar to that involving the CL Financial Group. In particular, they plan to pass a package of supportive legislation (including Insurance, Cooperatives, and Money Services Acts, among others) in August 2009 and put in place a Financial Regulatory Supervisory Authority (responsible for nonbanks) by October 2009. In addition, the authorities are engaged in regional efforts to reach a prompt and sustainable solution to the cross-border CL Financial issue.[5]

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[4] In 2008, St. Lucia benefited from MCM technical assistance to strengthen debt management.

[5] As part of that effort, in late June the St. Lucian Registrar of Insurance moved to appoint a judicial manager to manage the assets of the British American Insurance Company branch operating in St. Lucia, to protect policyholders from the risk that the company will be unable to meet its liabilities.

Box. St. Lucia—Key Elements of Debt Management Strategy

Per the request of the Government of St. Lucia, the Fund prepared a report to assist the authorities on improving public debt management in critical areas.[1] In the report, the staff provides guidelines on data reporting requirements, staffing and organizational arrangements, and the decision-making framework. A discussion of developments on the Regional Government Securities Market (RGSM) and secondary debt markets is also presented, along with a brief review of St. Lucia's public debt law.

Staff examined the core elements of St. Lucia's medium-term debt strategy in light of its portfolio structure and associated financial risks. Compared to other ECCU members, St. Lucia has the lowest debt-to-GDP ratio (around 67 percent in FY2008–09). The public debt is mostly owned by central government, and the exchange and interest rate risks are relatively small. However, the maturity profile is heavily influenced by bonds with short remaining maturity, and rollover difficulties pose significant risks to the financing of the debt.

To address this problem and enhance the effectiveness of public debt management, the staff identified five policy priorities to be pursued by the Government of St. Lucia:

- Establish a high-level Debt Management Advisory Committee, chaired by the Permanent Secretary of the Ministry of Finance, to ensure consistency between the annual financing program and a medium-term strategy committed to debt sustainability.

- Improve the capacity for conducting debt sustainability analysis, which would require appropriate staffing at the Ministry of Finance.

- Assign to the Debt and Investment Unit in the Ministry of Finance the task of formulating a coherent debt management strategy, and conducting regular cost-risk analyses of the debt portfolio.

- Take additional measures to mitigate rollover risks in the public debt portfolio, including the establishment of a general sinking fund that is more cost effective than the current bond-specific sinking funds. In addition, the staff recommends the implementation of a regular program of swapping bonds with short remaining maturity for longer-term bonds. Consideration should also be given to the inclusion of off-balance sheet projects in the debt strategy and sustainability analysis.

- Improve the functioning of the RGSM, which would entail switching from the fixed price auction mechanism to a more conventional competitive auction format for the sale of bonds. Moreover, the staff recommends the development of a medium-term program of market development reforms.

The St. Lucian authorities reacted positively to the staff's appraisal, and have committed to implement the staff's recommendations. The Government has already identified the members of the Debt Management Advisory Committee, and is working with other ECCU members on a harmonized public debt strategy under the umbrella of the Eastern Caribbean Central Bank. In addition, the Government decided to transfer the macroeconomic and fiscal policy unit of the Ministry of Economic Affairs back to the Ministry of Finance, to assist with the preparation of a debt sustainability analysis. Finally, the Ministry is also obtaining formal approval from Cabinet to establish a new operational structure for debt management.

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[1] St. Lucia—Public Debt Management: Institutional and Data Issues and the Key Elements of a Medium-Term Debt Management Strategy, mimeo, International Monetary Fund: Washington, D.C., 2008.

24. **The mission urged structural reforms to boost growth and enhance competitiveness.** Although St. Lucia generally scores well relative to its regional peers in measures of the attractiveness of the business environment, lowering the costs of starting a business and simplifying the process to register properties are likely to be rewarded by additional investment (Figure 7). On the labor market side, the mission encouraged matching incomes policy to productivity gains to help limit the contribution of wage pressures to inflation. In addition, structural reforms to boost productivity growth, enhance competitiveness, liberalize trade, and increase labor market flexibility could help mitigate wage and price pressures and facilitate economic recovery once the global financial crisis has begun to ease. In this regard, the authorities are developing a program, with assistance from USAID, to improve the competitiveness of the economy by addressing constraints identified in the World Bank Doing Business Report.

V. Access and Risks

25. **The authorities have requested Fund financing under the RAC-ESF in an amount equivalent to SDR 6.89 million (about US$10.65 million or 45 percent of quota).** This borrowing, which represents about 1.1 percent of GDP and covers about 29 percent of the net impact of the exogenous shock, would help meet the immediate foreign exchange needs stemming from the spillover effects of the global downturn and financial turmoil, thereby reducing the extent of the decline in external reserves. Fund financial support would also be key to catalyzing financing from the Caribbean Development Bank, the World Bank, and other donors to help close the financing gap.

26. **It is expected that St. Lucia will be able to discharge its obligations to the Fund in a timely manner.** As discussed above, downside risks to the macroeconomic outlook are significant, particularly given the country’s vulnerability to shocks (including natural disasters) and the still-high debt level. However, St. Lucia has an exemplary debt servicing record, has never had a fiscal crisis, and has a track record of prudent policies that has kept its debt-to-GDP ratio among the lowest in the region (with the average ratio in the ECCU at 100 percent). Moreover, the authorities are committed to reining in discretionary expenditures and following through on revenue reforms that will put the debt on a solid downward trajectory once a recovery is underway.

VI. Staff Appraisal

27. **St. Lucia faces significant policy challenges in 2009.** Its economy has been damaged by the global economic downturn that has led to a sudden fall in demand for tourism, its primary foreign currency earner and source of fiscal revenue. Although the recent easing of international prices of energy and food has helped reduce pressure on the fiscal position and balance of payments, the near-term revenue and reserves outlook is challenging and could further deteriorate should the global financial crisis deepen.

28. **The government's fiscal policies appropriately aim to maintain macroeconomic stability and minimize reserve losses.** The proposed tightening of the fiscal stance and contraction of domestic borrowing should help strengthen the fiscal position and balance of payments. In this context, access under the RAC-ESF and financial support from other international financial institutions and donor countries will be key to maintaining financial stability.

29. **The authorities are rightfully focused on ensuring medium-term debt sustainability.** In that regard, the government's plans to introduce a VAT in 2010 is welcome, which has the potential to broaden the tax base substantially. In particular, staff commend the authorities' plans to implement a uniform VAT rate with a very limited number of exemptions and zero-ratings, which would make St. Lucia a leader in the region with respect to VAT design and implementation. Building on these revenue initiatives and extending the reform effort to the fiscal expenditure side should place the fiscal accounts on a firm footing. Improving the efficiency of social spending will also be vital to this effort. Similarly, prioritization of capital expenditure, through implementing a formal public sector investment program mechanism, is an important component to raise spending efficiency over the medium term.

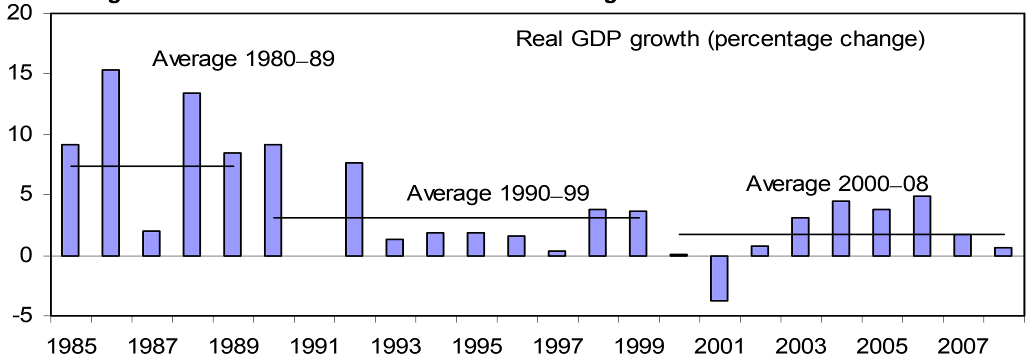
30. **The authorities' efforts to urgently address nonbank financial sector vulnerabilities should help prevent any spillover effects to the broader financial system.** The recent collapse of the CL Financial Group is a reminder that the financial sector is not immune to the crisis. Although the magnitude and consequences for St. Lucia are still not fully known, the authorities are collaborating closely with regional counterparts to find a solution that minimizes the macroeconomic and fiscal fallout. At the same time, they are putting in place a Financial Regulatory Supervisory Authority, together with supporting legislation, to strengthen the regulatory and supervisory framework for the nonbank financial sector.

31. **The importance of structural reforms for economic efficiency and competitiveness cannot be overemphasized.** In this context, pursuing labor market flexibility, aiming for productivity-matching incomes policy, and further strengthening the business environment should help position St. Lucia for a recovery once the global recession bottoms out.

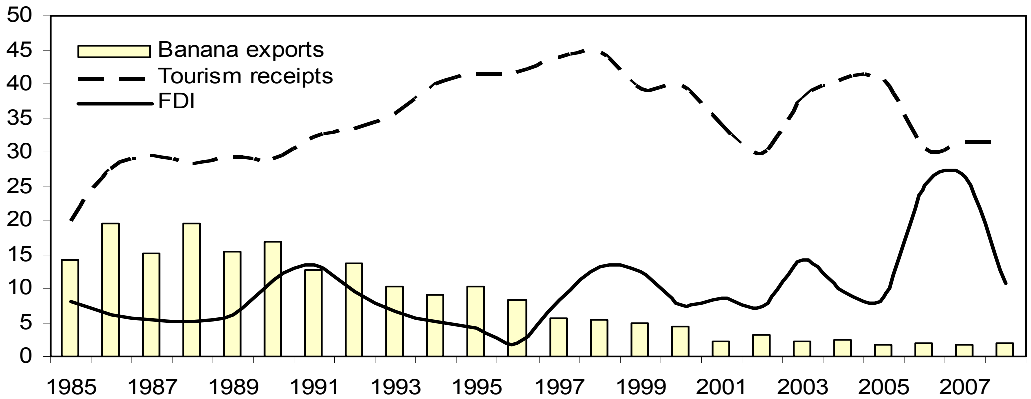
32. **Staff supports the authorities' request for a disbursement under the Fund's RAC-ESF.** Staff's support is based on the severe effects of the sudden shock on the economy, the associated large balance of payments needs, and the authorities' commitment to push ahead with a sound fiscal policy stance, aimed at placing debt on a firm downward path over the medium term, as outlined in the authorities' letter of intent. While downside risks remain, these risks are mitigated considerably by the authorities' resolve to maintain prudent fiscal policies and bolster private sector-led growth, and their commitment to continued close cooperation with the Fund.

Figure 1. St. Lucia: Macroeconomic Developments, 1985–2008
(In percent of GDP, unless otherwise indicated)

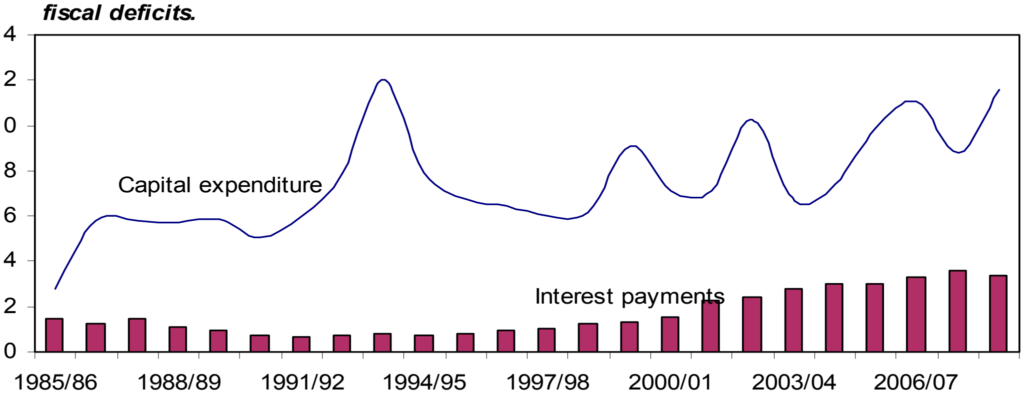
Exogenous shocks have contributed to volatile growth.



As banana exports have fallen, tourism has become the main growth sector, but tourism and FDI flows have declined sharply in recent years...



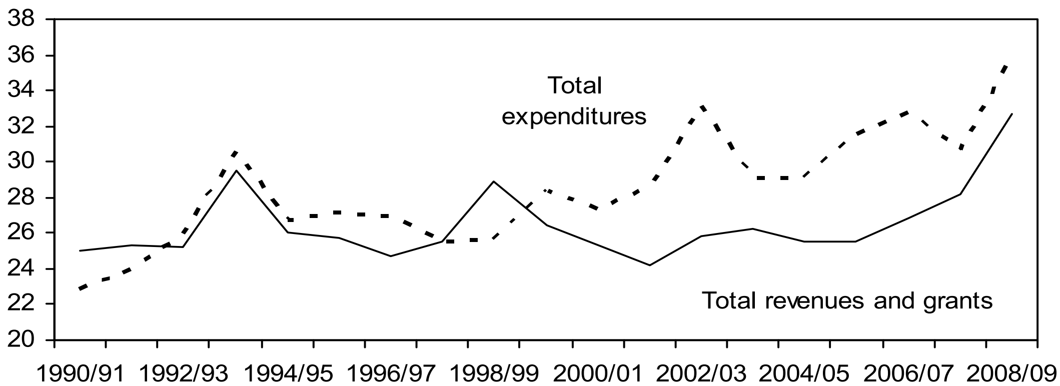
...while increasing interest payments and capital expenditure have contributed to fiscal deficits.



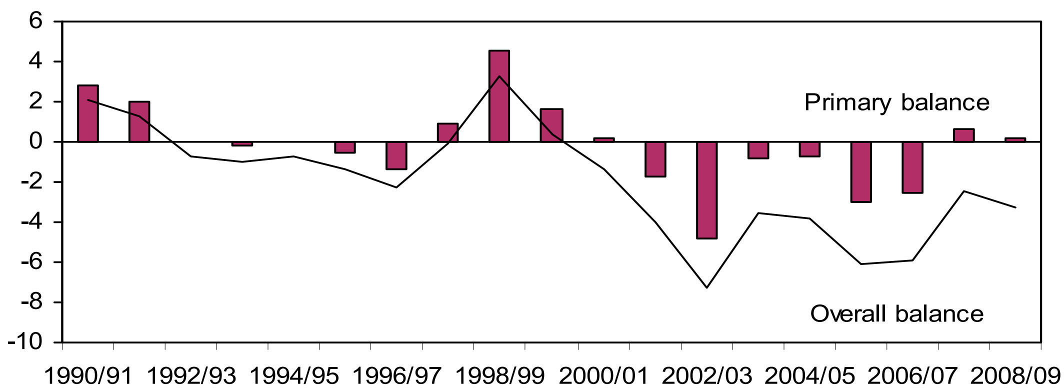
Sources: St. Lucia authorities; and Fund staff estimates.

Figure 2. St. Lucia: Fiscal Developments, 1990/91–2008/09
(In percent of GDP, unless otherwise indicated)

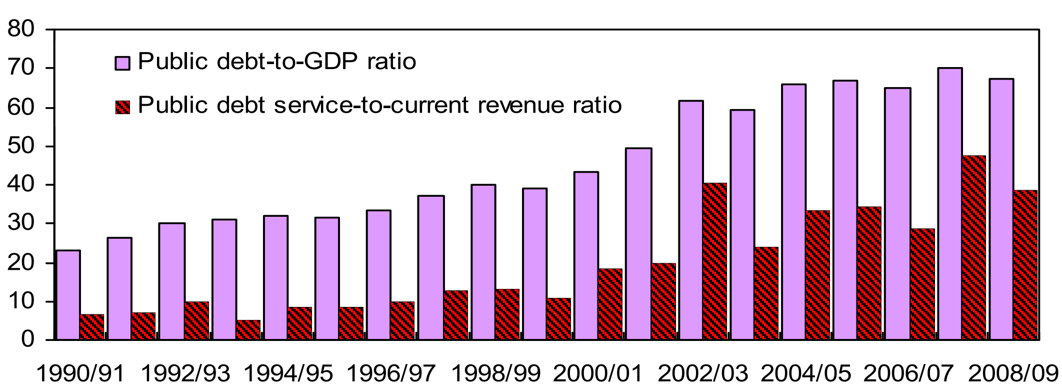
Revenues have risen since 2004/05...



...leading to some fiscal consolidation in the last two years...

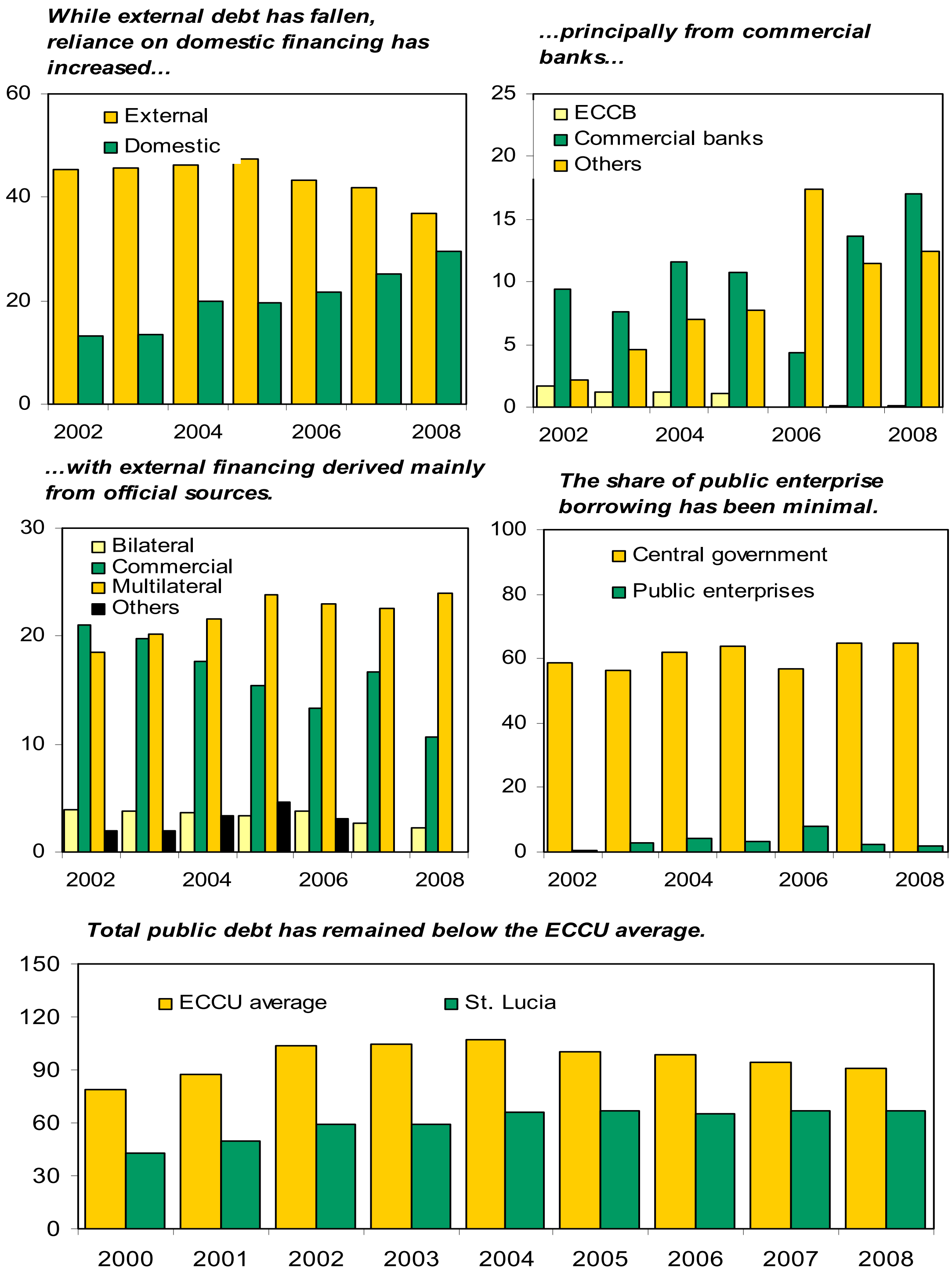


...contributing to a stabilizing debt-to-GDP ratio.



Sources: St. Lucia authorities; and Fund staff estimates.

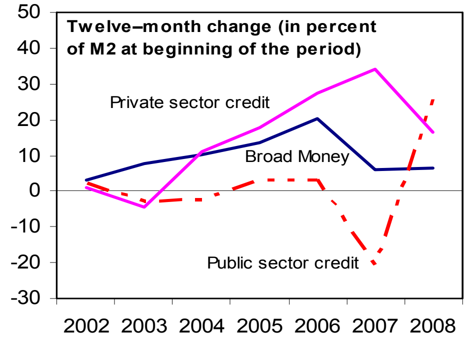
Figure 3. St. Lucia: Evolution of Public Debt, 2002-–08
(In percent of GDP)



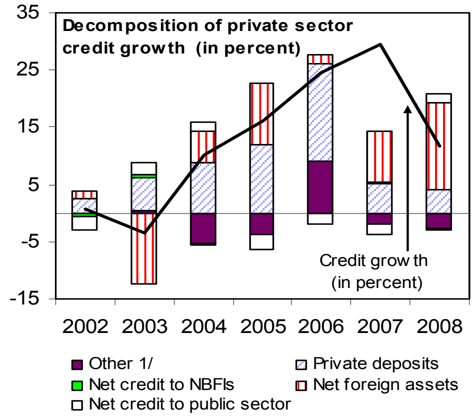
Sources: ECCB; St. Lucia authorities; and Fund staff estimates.

Figure 4. St. Lucia: Monetary Developments, 2002–08

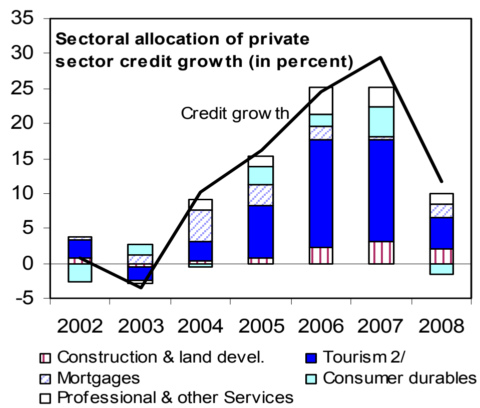
There has been a sharp expansion in public sector credit and a decline in growth of private sector credit…



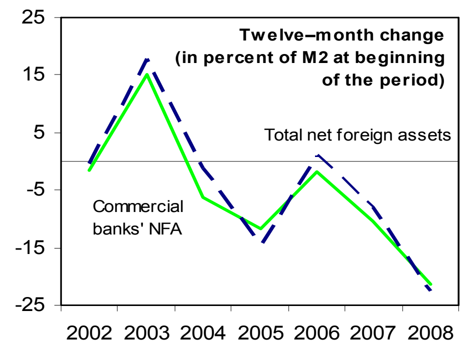
…with private credit financed primarily through a rundown of net foreign assets.



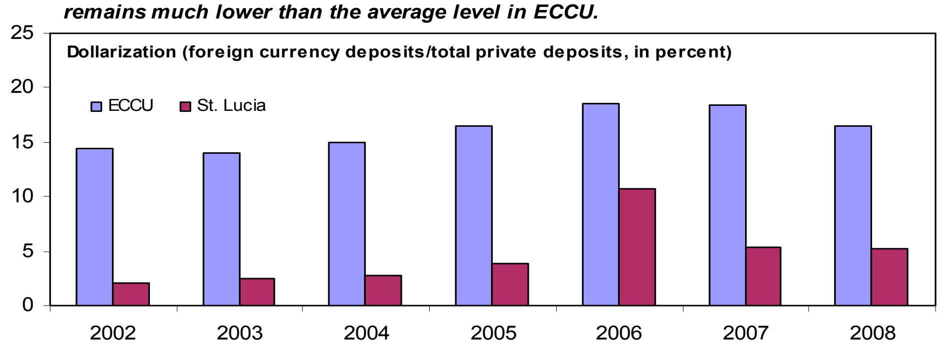
Private sector credit expansion started to cool in 2008, particularly credit to tourism.



Commercial banks' NFA have contracted since 2006.



Dollarization is increasing following the removal of capital controls in 2004, but remains much lower than the average level in ECCU.

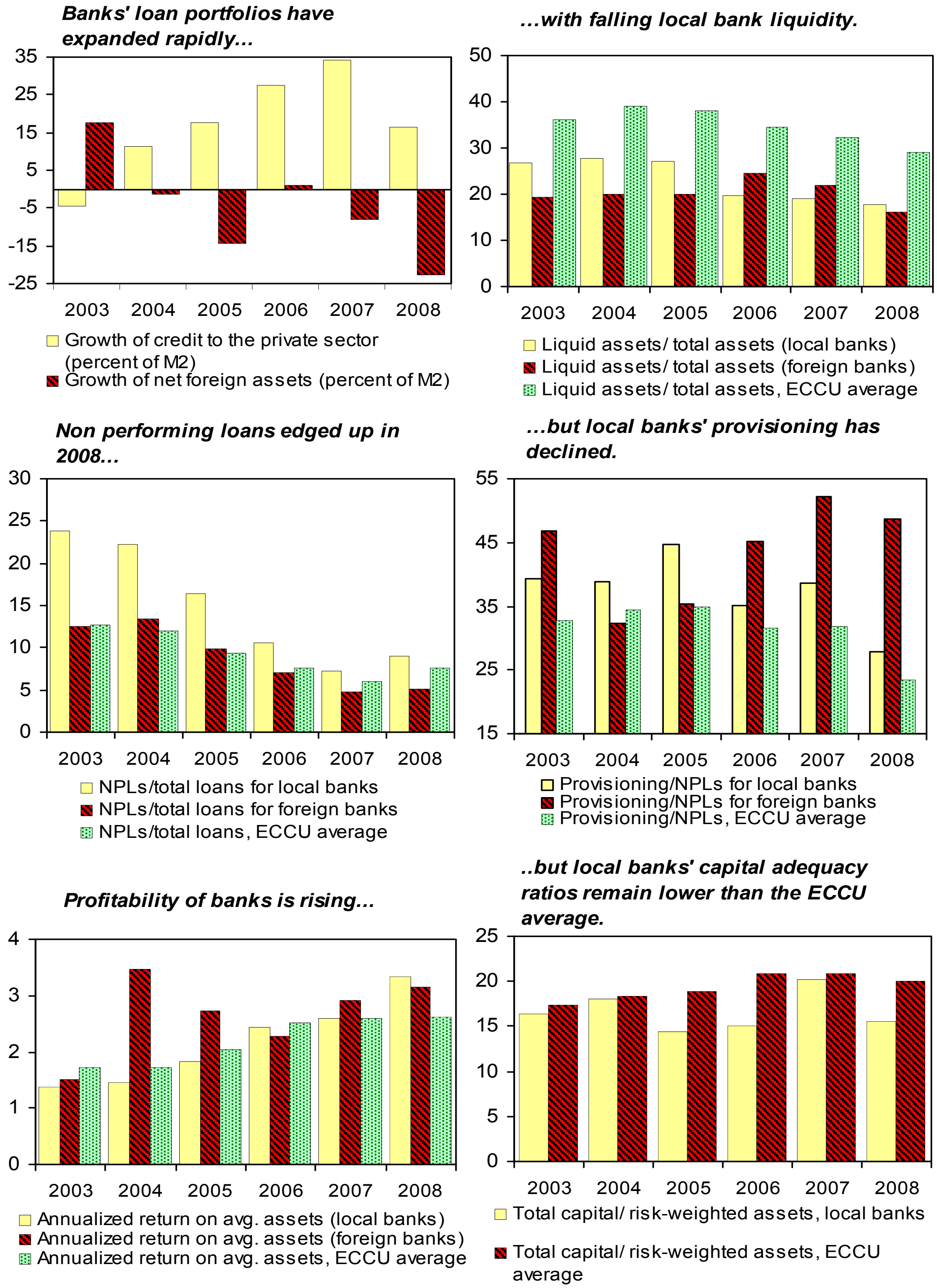


Sources: ECCB; and Fund staff calculations.

1/ Includes interbank float, reserves held with the ECCB, and other unclassified assets.

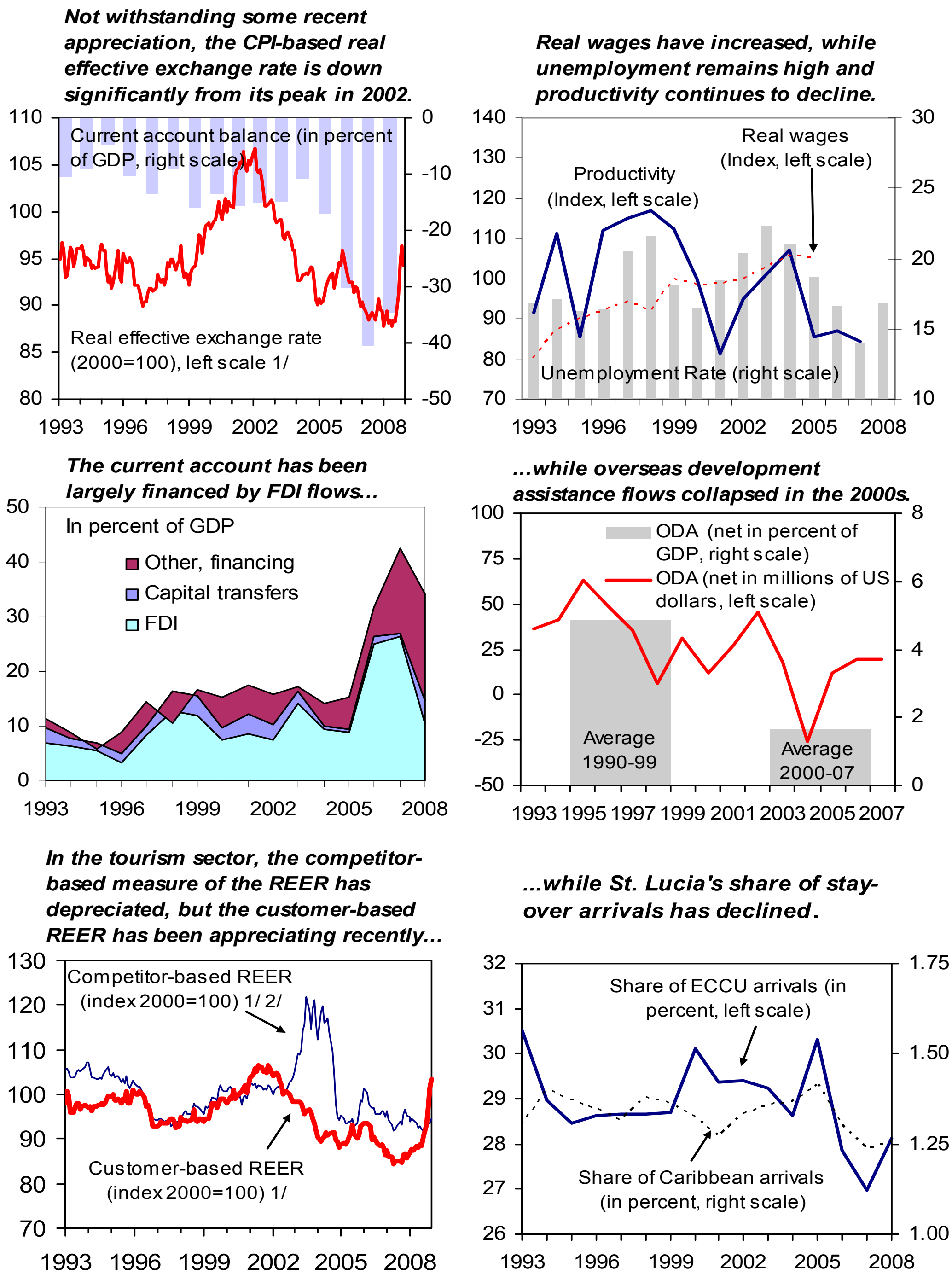
2/ Includes tourism, entertainment, and half of transport, distributive trade and professional services.

Figure 5. St. Lucia: Banking System Developments, 2003—08
(In percent; end of period unless noted otherwise)



Sources: ECCB; and Fund staff calculations.

Figure 6. St. Lucia: External Competitiveness, 1993–2008

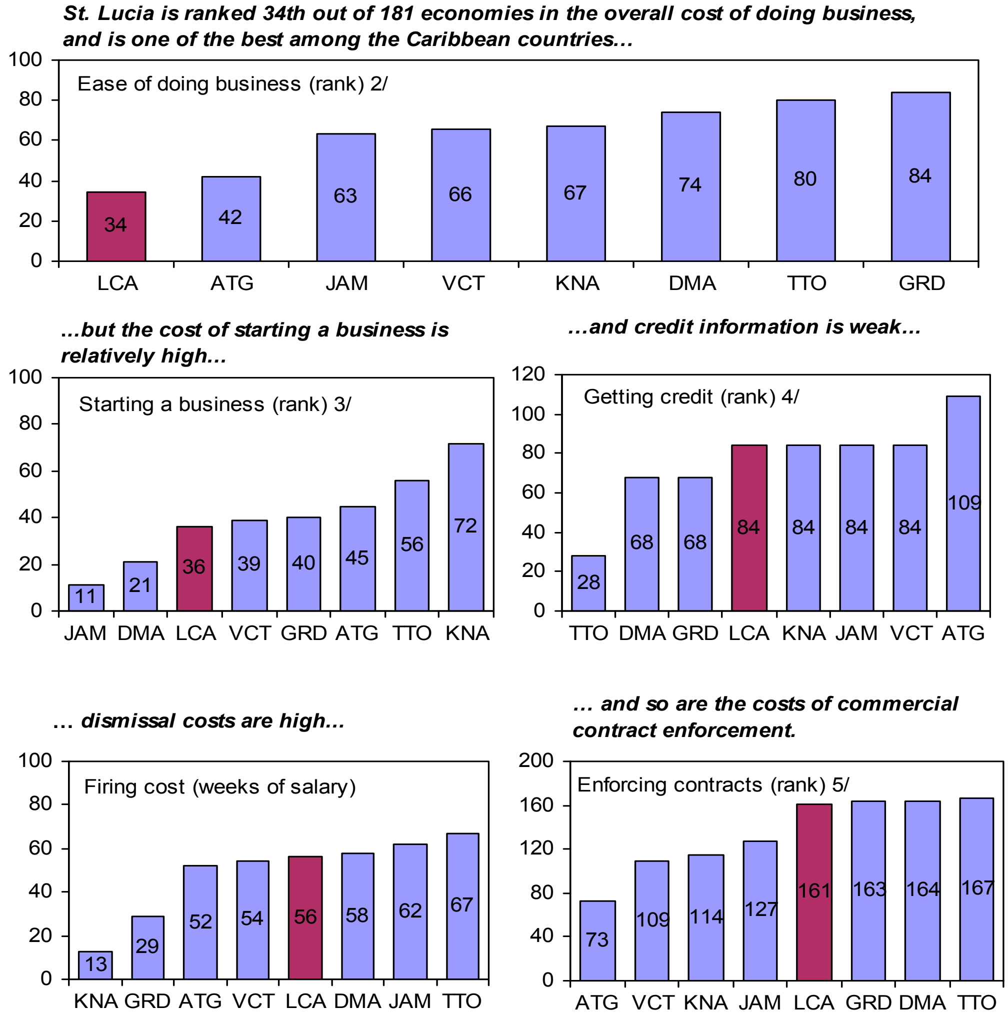


Sources: ECCB; Caribbean Tourism Organization; St. Lucia authorities; and Fund staff calculations.

1/ An increase (decrease) indicates an appreciation (depreciation).

2/ The sharp movements in the competitor-based real exchange rate in 2002–04 were largely driven by the Dominican Republic's peso.

Figure 7. St. Lucia: Doing Business Indicators, 2009 1/



Source: World Bank, *2009 Doing Business Indicators* (2008).

Note: ATG stands for Antigua and Barbuda, DMA stands for Dominica, GRD stands for Grenada, JAM stands for Jamaica, KNA stands for St. Kitts and Nevis, LCA stands for St. Lucia, TTO stands for Trinidad and Tobago, and VCT stands for St. Vincent and the Grenadines.

1/ Smaller numbers represent greater ease in doing business. The indicators are comparable across 181 countries.

2/ This is an overall indicator that captures the regulatory costs of doing business; it can be used to analyze specific regulations that enhance or constrain investment, productivity, and growth.

3/ This topic identifies the bureaucratic and legal hurdles an entrepreneur must overcome to incorporate and register a new firm. It examines the procedures, time, and cost involved in launching a commercial or industrial firm with up to 50 employees and start-up capital of 10 times the economy's per-capita gross national income.

4/ This topic explores two sets of issues—credit information registries and the effectiveness of collateral and bankruptcy laws in facilitating lending.

5/ This topic looks at the efficiency of contract enforcement by following the evolution of a sale of goods dispute and tracking the time, cost, and number of procedures involved from the moment the plaintiff files the lawsuit until actual payment.

Table 1. St. Lucia: Selected Social and Economic Indicators, 2005–10

I. Social and Demographic Indicators

Area (sq. km)	616	Life expectancy at birth (years, 2006)	74
		Infant mortality (per thousand live births, 2007)	23.5
Population		Human Development Index (HDI) ranking (2007)	72
Total (2007)	171,226	(rank out of 177 countries)	
Rate of growth (percent per year)	1.4		
Population density (per sq. km., 2007)	317.6	Gross Domestic Product (2007)	
Net migration rate (per thousand, 2002)	-9.8	(millions of US dollars)	960
Adult illiteracy rate (percent, 2004)	5.2	(millions of EC dollars)	2,592
		(US$ per capita)	5,606

II. Economic and Financial Indicators, 2005-10

	2005	2006	2007	Est. 2008	Budget 2009	Proj. 2009	Proj. 2010
	(Annual percentage change, unless otherwise specified)						
Output and prices							
Real GDP at factor cost	4.4	4.9	1.7	0.7	…	-2.5	-0.4
GDP at current market prices	9.8	6.1	2.9	2.8	…	0.4	2.4
GDP deflator at factor cost	3.1	2.3	0.5	2.1	…	3.0	2.8
Consumer prices (end of period)	4.5	1.4	6.6	3.8	…	3.1	2.2
Consumer prices (period average)	3.9	4.1	2.2	7.2	…	2.2	2.8
Banana export receipts	-23.0	15.9	-9.2	22.5	…	10.8	5.1
Unemployment rate (in percent)	18.7	16.6	13.9	16.8	…	…	…
External sector							
Exports, f.o.b.	-7.7	32.2	-13.7	83.5	…	-8.9	5.1
Imports, f.o.b.	20.1	24.6	4.0	6.7	…	-41.3	4.7
Travel receipts	9.3	-20.0	6.0	3.1	…	-18.8	4.4
Terms of trade (- = deterioration)	-3.8	-13.2	-12.8	-14.0	…	-1.2	-1.1
Real effective exchange rate (end of period, - = depreciation)	-0.5	0.5	-3.6	1.1		...	...
Money and credit 1/							
Net foreign assets	-14.5	1.0	-8.0	-22.7	…	-2.5	2.7
Net domestic assets	27.9	19.1	14.2	29.2	…	9.7	-0.6
Of which							
Credit to private sector	17.7	27.4	34.2	16.4	…	-8.1	2.3
	(In percent of GDP, unless otherwise specified)						
Central government 2/							
Total revenue and grants	25.6	26.9	28.2	32.7	34.7	33.9	32.7
Total expenditure and net lending	31.6	32.8	30.7	36.0	41.2	36.8	36.2
Current expenditure	21.3	21.7	21.7	24.7	26.2	26.7	26.1
Of which							
Wages and salaries	9.7	9.9	10.1	11.3	11.4	11.8	11.5
Interest	3.0	3.3	3.1	3.5	3.6	3.7	3.8
Capital expenditure	10.3	11.0	9.0	11.2	15.0	10.1	10.1
Overall balance (cash basis)	-6.0	-5.9	-2.5	-3.3	-6.5	-2.9	-3.5
Of which							
Current balance (savings)	4.0	4.9	6.2	5.1	3.5	2.2	4.1
Primary balance (after grants)	-3.0	-2.6	0.7	0.2	-2.9	0.8	0.3
Central government debt	63.7	62.4	68.0	65.5	…	67.8	69.4
Debt service in percent of current revenues 3/	34.3	28.5	47.7	38.8	…	34.8	31.1
External sector							
External current account	-17.1	-30.2	-40.6	-34.5	…	-17.5	-16.7
Of which							
Exports of goods and services	56.8	48.4	49.5	57.9	…	50.3	51.4
Imports of goods and services	67.1	73.9	84.5	86.5	…	61.6	61.9
Stayover arrivals (percentage change)	6.5	-4.9	-5.0	2.9	…	-10.0	1.5
Foreign direct investment (FDI)	1.6	25.1	26.4	10.6	…	7.6	15.0
Public sector external debt (end of period)	47.4	43.2	43.9	37.9	…	40.6	41.3
External public debt service 4/							
In percent of exports of goods and services	6.5	7.6	12.2	11.7	…	11.1	11.8
In percent of central government revenue before grants	15.4	15.0	22.7	24.5	…	20.7	21.4
Memorandum items:							
Gross public sector debt 5/ 6/	67.0	65.0	70.3	67.3	…	69.8	71.6
Nominal GDP at market prices (in millions of EC dollars)	2,374	2,520	2,592	2,664	2,676	2,676	2,741
Nominal GDP at factor cost (in millions of EC dollars)	1,924	2,066	2,111	2,171	2,175	2,175	2,227
Share of ECCU stayover visitors	30.3	28.1	27.0	28.1	…	...	...

Sources: St. Lucia authorities; ECCB; and Fund staff estimates and projections.

1/ Changes in relation to liabilities to private sector at beginning of period.
2/ Data are for fiscal years beginning April 1.
3/ Comprises domestic and external interest and amortization.
4/ Comprises external interest and amortization.
5/ Includes liabilities to the NIC.
6/ Total public (including nonguaranteed) debt in percent of GDP.

Table 2. St. Lucia: Operations of the Central Government, 2006–14 1/
(In millions of EC dollars)

	2006	2007	Est. 2008	Budget 2009	Proj. 2009	Projections 2010	2011	2012	2013	2014
Total revenue and grants	**682.6**	**735.6**	**871.3**	**933.4**	**913.5**	**905.4**	**928.5**	**1,017.1**	**1,084.9**	**1,151.9**
Current revenue	**675.3**	**729.2**	**794.5**	**797.5**	**777.6**	**836.8**	**906.0**	**993.2**	**1,059.6**	**1,125.0**
Tax revenue	**619.8**	**689.0**	**736.0**	**740.2**	**720.3**	**777.9**	**844.4**	**928.0**	**990.3**	**1,051.5**
Nontrade tax 2/	381.5	442.8	492.6	517.9	498.0	549.3	603.0	669.6	713.4	757.4
Trade tax	238.4	246.2	243.4	222.3	222.3	228.6	241.4	258.3	276.9	294.0
Nontax revenue	**55.5**	**40.2**	**58.5**	**57.3**	**57.3**	**58.9**	**61.6**	**65.3**	**69.3**	**73.5**
Capital revenue	**0.7**	**0.0**	**16.8**	**5.4**	**5.4**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**
Grants 3/	**6.6**	**6.4**	**60.0**	**130.5**	**130.5**	**68.5**	**22.5**	**23.9**	**25.3**	**26.9**
Total expenditure and net lending	**831.7**	**800.6**	**959.7**	**1,108.2**	**990.5**	**1,002.9**	**1,036.1**	**1,087.5**	**1,147.2**	**1,206.6**
Current expenditure	**551.4**	**566.4**	**659.7**	**704.3**	**717.8**	**723.3**	**740.9**	**774.7**	**811.9**	**850.6**
Wages and salaries	250.9	262.4	300.6	307.4	318.7	318.7	325.6	337.3	351.5	366.3
NIC contributions and retirement	46.3	49.2	51.9	55.6	56.2	57.8	60.4	64.0	67.9	72.1
Goods and services	101.5	107.6	127.0	164.3	148.2	110.7	115.8	122.7	130.2	138.2
Of which:										
Additional social spending	...	...			18.8	0.0	0.0	0.0	0.0	0.0
Transfers	68.5	65.0	87.7	81.0	96.4	130.1	127.3	134.9	143.2	152.0
Of which:										
Additional social spending	...	...	…	…	8.1	49.8	43.4	46.0	48.8	51.8
Interest payments	84.3	82.2	92.6	96.0	98.3	105.9	111.9	115.8	119.1	121.9
Domestic	27.7	34.2	43.2	43.1	44.6	47.8	51.4	53.5	53.9	54.1
External	56.6	48.0	49.4	52.9	53.7	58.2	60.4	62.3	65.2	67.8
Capital expenditure and net lending	**280.3**	**234.2**	**300.0**	**403.9**	**272.7**	**279.6**	**295.2**	**312.8**	**335.2**	**355.9**
Primary balance	**-64.8**	**17.2**	**4.2**	**-78.8**	**21.4**	**8.4**	**4.3**	**45.4**	**56.8**	**67.2**
(excluding grants)	**-71.4**	**10.8**	**-55.8**	**-209.3**	**-109.2**	**-60.1**	**-18.2**	**21.6**	**31.5**	**40.3**
Current balance	**123.9**	**162.8**	**134.8**	**93.2**	**59.8**	**113.6**	**165.1**	**218.5**	**247.7**	**274.4**
Overall balance (excluding grants)	**-155.7**	**-71.4**	**-148.4**	**-305.3**	**-207.5**	**-166.1**	**-130.1**	**-94.2**	**-87.6**	**-81.6**
Overall balance (including grants)	**-149.0**	**-65.0**	**-88.4**	**-174.8**	**-77.0**	**-97.5**	**-107.5**	**-70.4**	**-62.3**	**-54.7**
Financing	**145.4**	**89.3**	**130.8**	**219.9**	**77.0**	**97.5**	**107.5**	**70.4**	**62.3**	**54.7**
External (net)	53.0	-22.6	108.3	196.3	75.3	45.4	43.3	36.4	55.9	52.1
Loans	53.0	-22.6	108.3	196.3	75.3	45.4	43.3	36.4	55.9	52.1
Drawings	92.6	122.5	172.9	265.9	170.4	153.6	125.0	145.0	123.3	113.3
Of which:										
ESF	0.0	0.0	0.0	0.0	28.8	0.0	0.0	0.0	0.0	0.0
Amortization	39.6	145.1	64.6	69.6	95.2	108.2	81.7	108.6	67.4	61.2
Domestic financing	92.5	112.0	22.5	…	1.7	52.1	64.2	34.0	6.3	2.6
ECCB (net)	-14.2	0.0	0.0	…	0.0	0.0	0.0	0.0	0.0	0.0
Commercial banks (net)	67.0	71.1	12.7	…	6.9	-33.2	-4.4	50.7	36.3	43.8
Other domestic financing	39.7	40.9	9.8	…	-5.2	85.3	68.6	-16.7	-30.0	-41.2
Statistical discrepancy	3.6	-24.4	-42.3	…	0.0	0.0	0.0	0.0	0.0	0.0

Sources: St. Lucia authorities; and Fund staff estimates and projections.

1/ Data are for fiscal years beginning April 1.
2/ A VAT is introduced in 2010.
3/ For 2009, identified grants are from the European Union and Taiwan Province of China.

Table 3. St. Lucia: Operations of the Central Government, 2006–14 1/
(In percent of GDP)

			Est.	Budget	Proj.	Projections				
	2006	2007	2008	2009		2010	2011	2012	2013	2014
Total revenue and grants	26.9	28.2	32.7	34.7	33.9	32.7	32.1	33.2	33.3	33.3
Current revenue	26.6	27.9	29.8	29.6	28.9	30.2	31.3	32.4	32.6	32.6
Tax revenue	24.4	26.4	27.6	27.5	26.8	28.1	29.2	30.3	30.4	30.4
Nontrade tax 2/	15.0	17.0	18.5	19.2	18.5	19.8	20.8	21.8	21.9	21.9
Trade tax	9.4	9.4	9.1	8.3	8.3	8.3	8.3	8.4	8.5	8.5
Nontax revenue	2.2	1.5	2.2	2.1	2.1	2.1	2.1	2.1	2.1	2.1
Capital revenue	0.0	0.0	0.6	0.2	0.2	0.0	0.0	0.0	0.0	0.0
Grants 3/	0.3	0.2	2.2	4.8	4.8	2.5	0.8	0.8	0.8	0.8
Total expenditure and net lending	32.8	30.7	36.0	41.2	36.8	36.2	35.8	35.5	35.2	34.9
Current expenditure	21.7	21.7	24.7	26.2	26.7	26.1	25.6	25.3	24.9	24.6
Wages and salaries	9.9	10.1	11.3	11.4	11.8	11.5	11.2	11.0	10.8	10.6
NIC contributions and retirement	1.8	1.9	1.9	2.1	2.1	2.1	2.1	2.1	2.1	2.1
Goods and services	4.0	4.1	4.8	6.1	5.5	4.0	4.0	4.0	4.0	4.0
Of which:										
Additional social spending	...	…	…	0.0	0.7	0.0	0.0	0.0	0.0	0.0
Transfers	2.7	2.5	3.3	3.0	3.6	4.7	4.4	4.4	4.4	4.4
Of which:										
Additional social spending	...	…	…	…	0.3	1.8	1.5	1.5	1.5	1.5
Interest payments	3.3	3.1	3.5	3.6	3.7	3.8	3.9	3.8	3.7	3.5
Domestic	1.1	1.3	1.6	1.6	1.7	1.7	1.8	1.7	1.7	1.6
External	2.2	1.8	1.9	2.0	2.0	2.1	2.1	2.0	2.0	2.0
Capital expenditure and net lending	11.0	9.0	11.2	15.0	10.1	10.1	10.2	10.2	10.3	10.3
Primary balance	-2.6	0.7	0.2	-2.9	0.8	0.3	0.1	1.5	1.7	1.9
(excluding grants)	-2.8	0.4	-2.1	-7.8	-4.1	-2.2	-0.6	0.7	1.0	1.2
Current balance	4.9	6.2	5.1	3.5	2.2	4.1	5.7	7.1	7.6	7.9
Overall balance (excluding grants)	-6.1	-2.7	-5.6	-11.3	-7.7	-6.0	-4.5	-3.1	-2.7	-2.4
Overall balance (including grants)	-5.9	-2.5	-3.3	-6.5	-2.9	-3.5	-3.7	-2.3	-1.9	-1.6
Financing	5.7	3.4	4.9	8.2	2.9	3.5	3.7	2.3	1.9	1.6
External (net)	2.1	-0.9	4.1	7.3	2.8	1.6	1.5	1.2	1.7	1.5
Loans	2.1	-0.9	4.1	7.3	2.8	1.6	1.5	1.2	1.7	1.5
Drawings	3.6	4.7	6.5	9.9	6.3	5.5	4.3	4.7	3.8	3.3
Of which:										
ESF	0.0	0.0	0.0	0.0	1.1	0.0	0.0	0.0	0.0	0.0
Amortization	1.6	5.6	2.4	2.6	3.5	3.9	2.8	3.5	2.1	1.8
Domestic financing	3.6	4.3	0.8	…	0.1	1.9	2.2	1.1	0.2	0.1
ECCB (net)	-0.6	0.0	0.0	…	0.0	0.0	0.0	0.0	0.0	0.0
Commercial banks (net)	2.6	2.7	0.5	…	0.3	-1.2	-0.2	1.7	1.1	1.3
Other domestic financing	1.6	1.6	0.4	…	-0.2	3.1	2.4	-0.5	-0.9	-1.2
Statistical discrepancy	0.1	-0.9	-1.6	…	0.0	0.0	0.0	0.0	0.0	0.0
Memorandum items:										
GDP (at market prices, in EC$ millions)	2,538	2,610	2,667	2,692	2,692	2,769	2,894	3,066	3,255	3,456
Debt service (in percent of current revenue)	28.5	47.7	38.8	…	34.8	31.1	22.3	23.5	18.4	17.1
Central government debt (in percent of GDP)	62.4	68.0	65.5	…	67.8	69.4	70.1	68.5	66.4	64.1
External	35.0	37.0	41.0	…	39.2	40.9	34.9	35.4	34.7	33.9
Domestic	27.4	31.0	24.5	…	28.5	28.5	35.3	33.1	31.7	30.2

Sources: St. Lucia authorities; and Fund staff estimates and projections.

1/ Data are for fiscal years beginning April 1.
2/ A VAT is introduced in 2010.
3/ For 2009, identified grants are from the European Union and Taiwan Province of China.

Table 4. St. Lucia: Balance of Payments Summary, 2006–14

	2006	2007	Prel. 2008	Projections 2009	2010	2011	2012	2013	2014
	(In millions of Eastern Caribbean dollars)								
Current account	**-761.5**	**-1,052.8**	**-919.3**	**-467.4**	**-458.4**	**-638.5**	**-680.1**	**-706.3**	**-716.3**
Trade balance	-1,089.8	-1,189.3	-1,058.3	-458.8	-478.3	-845.4	-919.0	-977.4	-1,156.5
Exports f.o.b.	316.9	273.3	501.6	457.1	480.5	512.3	553.0	601.2	653.7
Of which									
Bananas	48.1	43.7	53.5	59.2	62.2	66.8	72.6	79.4	86.8
Manufactured exports	70.6	80.7	88.4	77.7	81.0	82.7	88.6	94.9	106.9
Imports f.o.b.	-1,406.6	-1,462.6	-1,559.9	-915.9	-958.8	-1,357.7	-1,472.1	-1,578.6	-1,810.2
Services (net)	446.4	283.3	296.6	155.0	190.7	384.4	425.3	468.0	647.9
Credits	902.4	1,010.0	1,041.9	888.6	927.5	1,136.3	1,206.5	1,283.7	1,499.8
Travel	768.4	814.5	839.7	681.5	711.2	906.9	963.6	1,025.8	1,226.1
Other nonfactor services	133.9	195.4	202.3	207.2	216.4	229.4	243.0	257.9	273.8
Debits	456.0	726.6	745.3	733.6	736.8	751.9	781.2	815.7	851.9
Travel	106.2	114.1	102.7	101.1	101.5	103.6	107.7	114.3	121.3
Other nonfactor services	349.8	612.5	642.6	632.5	635.3	648.3	673.5	701.4	730.6
Income payments (net)	-150.4	-183.5	-195.4	-197.8	-205.8	-214.0	-225.0	-237.8	-251.2
Current transfers	32.3	36.6	37.8	34.2	35.0	36.4	38.6	41.0	43.5
Net private transfers	33.6	29.1	30.7	27.8	28.5	29.6	31.4	33.3	35.3
Net official transfers	-1.2	7.5	7.1	6.4	6.6	6.8	7.2	7.7	8.2
Capital and financial account	**863.3**	**942.7**	**805.7**	**408.5**	**453.7**	**644.5**	**699.1**	**716.9**	**738.3**
Capital	30.7	21.1	109.7	130.5	68.5	22.5	23.9	25.3	26.9
Financial (net)	832.6	921.6	696.0	278.0	385.2	622.0	675.2	691.6	711.4
Official capital	53.0	-35.0	-69.4	75.3	45.4	43.3	36.4	55.9	52.1
Of which:									
ESF	…	…	…	28.8	…	…	…	…	…
Commercial banks	174.0	216.6	466.2	-1.6	-71.4	8.3	65.0	58.7	12.8
Private capital	605.6	669.6	237.1	204.3	411.1	570.3	573.8	577.0	646.6
Of which:									
Net direct investment	631.6	684.1	282.8	204.3	411.1	570.3	573.8	577.0	646.6
Errors and omissions	-64.5	160.1	103.9	0.0	0.0	0.0	0.0	0.0	0.0
Overall balance	37.3	50.0	-9.6	-58.9	-4.7	6.0	19.0	10.6	22.0
Financing	-37.3	-50.0	9.6	58.9	4.7	-6.0	-19.0	-10.6	-22.0
Change in imputed reserves (increase -)	-49.6	-51.3	8.8	58.9	4.7	-6.0	-19.0	-10.6	-22.0
Change in govt. foreign assets	12.3	1.3	0.9	0.0	0.0	0.0	0.0	0.0	0.0
	(In percent of GDP, unless otherwise indicated)								
Memorandum items:									
Current account	-30.2	-40.6	-34.5	-17.5	-16.7	-22.4	-22.5	-22.0	-21.0
Exports f.o.b.	12.6	10.5	18.8	17.1	17.5	18.0	18.3	18.8	19.2
Imports f.o.b.	-55.8	-56.4	-58.5	-34.2	-35.0	-47.6	-48.7	-49.3	-53.2
Net private transfers	1.3	1.1	1.2	1.0	1.0	1.0	1.0	1.0	1.0
Foreign direct investment	25.1	26.4	10.6	7.6	15.0	20.0	19.0	18.0	19.0
Indicators of diversification									
(In percent of exports of goods and nonfactor services)									
Banana exports	3.9	3.4	3.5	4.4	4.4	4.1	4.1	4.2	4.0
Tourism receipts	63.0	63.5	54.4	50.6	50.5	55.0	54.8	54.4	56.9
Tourism receipts	30.5	31.4	31.5	25.5	25.9	31.8	31.9	32.0	36.0
Total trade	68.4	67.0	77.4	51.3	52.5	65.6	67.1	68.0	72.4
Exports of goods and nonfactor services	48.4	49.5	57.9	50.3	51.4	57.8	58.3	58.8	63.3
Imports of goods and nonfactor services	73.9	84.5	86.5	61.6	61.9	74.0	74.6	74.7	78.2
Terms of trade for GNFS (percentage change)	-13.2	-12.8	-14.0	-1.2	-1.1	2.7	1.5	1.3	11.1
Excluding tourism (percentage change)	-6.5	-8.5	-5.8	0.2	-5.1	-1.6	-0.4	-0.1	-0.2
Public sector external debt (end of period)	43.2	43.9	37.9	40.6	41.3	41.2	40.1	39.5	38.7

Sources: St. Lucia authorities; ECCB; and Fund staff estimates and projections.

Table 5. St. Lucia: Monetary Survey, 2004–10

	2004	2005	2006	2007	Est. 2008	Projections 2009	2010
	(In millions of Eastern Caribbean dollars)						
Net foreign assets	**318.7**	**99.9**	**117.6**	**-47.7**	**-543.3**	**-600.7**	**-534.0**
ECCB (imputed reserves)	351.5	308.3	356.9	408.2	378.8	319.8	315.2
Commercial banks	-32.9	-208.5	-239.3	-455.9	-922.1	-920.5	-849.1
Net domestic assets	**1,190.5**	**1,611.9**	**1,938.6**	**2,230.9**	**2,867.5**	**3,093.0**	**3,078.5**
Public sector credit (net)	-324.7	-275.9	-222.8	-650.6	-93.6	-76.6	-148.3
Central government	-130.7	-90.7	-32.0	17.2	69.0	75.9	42.7
ECCB	-13.7	-10.0	-19.8	-43.2	5.9	5.9	5.9
Commercial banks	-117.0	-80.6	-12.2	60.4	63.1	70.0	36.8
Net credit to rest of public sector	-194.0	-185.2	-190.8	-667.9	-162.6	-152.5	-191.1
National Insurance Corporation	-240.9	-248.2	-264.2	-291.7	-340.3	-340.3	-369.2
Other	46.9	62.9	73.4	-376.2	177.7	187.8	178.1
Credit to private sector	1,650.6	1,917.3	2,386.8	3,090.8	3,449.9	3,262.0	3,319.3
Net credit to nonbank financial inst.	-35.4	-37.8	-40.4	-41.3	-29.2	-29.3	-30.0
Other items (net)	-100.0	8.3	-185.1	-168.0	-459.7	-63.2	-62.5
Broad money	**1,509.2**	**1,711.8**	**2,056.2**	**2,183.2**	**2,324.1**	**2,492.3**	**2,544.5**
Money	481.3	547.3	560.7	639.0	631.7	574.4	580.0
Currency in circulation	99.2	106.4	126.6	128.0	142.6	83.2	76.8
Demand deposits	382.2	440.9	434.1	510.9	489.1	491.2	503.2
Quasi-money	1,027.8	1,164.5	1,495.5	1,544.2	1,692.4	1,917.9	1,964.5
Time deposits	178.7	185.9	222.7	283.3	371.2	599.4	602.9
Savings deposits	810.4	916.3	1,064.9	1,150.8	1,206.6	1,211.7	1,241.2
Foreign currency deposits	38.7	62.2	207.9	110.2	114.7	106.8	120.4
	(Annual percentage change)						
Net foreign assets	-4.9	-68.7	17.8	-140.5	-1,040.0	-10.6	-11.1
Net domestic assets	15.0	35.4	20.3	15.1	28.5	7.9	-0.5
Credit to private sector	10.2	16.2	24.5	29.5	11.6	-5.4	1.8
Broad money	10.1	13.4	20.1	6.2	6.5	7.2	2.1
Money	40.3	13.7	2.4	14.0	-1.1	-9.1	1.0
Quasi-money 1/	0.1	13.3	28.4	3.3	9.6	13.3	2.4
	(Percent contribution compared to M2 at the beginning of the year)						
Net foreign assets	-1.2	-14.5	1.0	-8.0	-22.7	-2.5	2.7
Net domestic assets	11.3	27.9	19.1	14.2	29.2	9.7	-0.6
Public sector credit (net)	-2.5	3.2	3.1	-20.8	25.5	0.7	-2.9
Of which: central government	-1.9	2.7	3.4	2.4	2.4	0.3	-1.3
Credit to private sector	11.1	17.7	27.4	34.2	16.4	-8.1	2.3
Net credit to nonbank financial inst.	0.3	-0.1	-0.1	0.0	0.5	0.0	0.0
Other items (net)	2.4	7.2	-11.3	0.8	-13.4	17.1	0.0
Memorandum items:							
Income velocity 2/	1.5	1.5	1.3	1.2	1.2	1.1	1.1

Sources: St. Lucia authorities; ECCB; and Fund staff estimates and projections.

1/ Including resident foreign currency deposits.

2/ Nominal GDP at market prices divided by liabilities to the private sector.

Table 6. St. Lucia: Public Sector Debt, 2004–09 1/

	2004	2005	2006	2007	2008	Proj. 2009
	(In millions of EC dollars, end-period)					
Debt stock						
Public sector debt net of borrowing from the NIC	1,426.5	1,590.2	1,637.9	1,820.8	1,793.9	1,867.6
Domestic debt net of borrowing from the NIC	348.3	384.2	474.8	611.7	707.3	705.7
Domestic debt including borrowing from the NIC	428.4	464.4	549.4	683.2	783.8	782.2
By type of creditor						
ECCB	24.8	24.8	1.1	2.0	2.0	2.0
Commercial banks	252.0	256.0	109.2	365.5	384.7	391.5
Other (includes NIS and insurance companies)	151.6	183.5	439.1	315.7	397.1	388.7
By instrument						
Treasury bills	95.1	92.3	13.9	66.7	81.5	81.5
Loans	31.7	31.1	41.9	152.9	143.0	149.9
Bonds	217.3	217.3	123.2	386.4	483.1	482.8
Other (includes overdraft)	84.3	123.7	370.4	77.2	76.2	68.0
Public sector external debt	998.1	1,125.9	1,088.5	1,137.6	1,010.1	1,085.4
By type of creditor						
Official bilateral	77.3	81.4	96.8	96.4	76.8	79.7
Official multilateral	466.0	566.1	579.1	604.2	657.4	764.9
Commercial	382.6	367.4	335.3	441.2	277.5	240.7
	(In percent of GDP)					
Total debt	66.0	67.0	65.0	70.3	67.3	69.8
Domestic debt	19.8	19.6	21.8	26.4	29.4	29.2
External debt	46.1	47.4	43.2	43.9	37.9	40.6
	(In percent of government revenues)					
Total debt	252.9	260.7	242.3	249.7	221.1	238.5
Domestic debt	75.9	76.1	81.3	93.7	96.6	99.9
External debt	176.9	184.6	161.0	156.0	124.5	138.6
	(In millions of EC dollars, end-period)					
Debt service						
Total debt service	187.3	209.0	192.3	347.8	308.3	270.7
Amortization	120.3	132.4	110.8	250.8	211.4	172.4
Domestic	72.6	91.5	71.2	146.3	82.9	77.2
External	47.8	41.0	39.6	104.5	128.5	95.2
Interest	66.9	76.6	81.5	97.0	96.9	98.3
Domestic	22.2	26.5	28.3	44.9	45.0	44.6
External	44.8	50.1	53.3	52.1	51.9	53.7
	(In percent of GDP)					
Total debt service	8.7	8.8	7.6	13.4	11.6	10.1
Interest cost	3.1	3.2	3.2	3.7	3.6	3.7
Amortization	5.6	5.6	4.4	9.7	7.9	6.4
In percent of government revenue excluding grants	33.2	34.3	28.5	47.7	38.0	34.6
In percent export of goods and services	15.0	15.5	15.8	27.1	20.0	20.1
In percent of broad money 2/	12.4	12.2	9.4	15.9	13.3	10.9
Domestic debt service						
In percent of government revenue excluding grants	16.8	19.3	14.7	26.2	15.8	15.6
In percent export of goods and services	7.6	8.7	8.2	14.9	8.3	9.1
In percent of broad money 2/	6.3	6.9	4.8	8.8	5.5	4.9
External debt service						
In percent of government revenue excluding grants	19.8	15.4	15.0	22.7	24.5	20.7
In percent export of goods and services	8.2	6.5	7.6	12.2	11.7	11.1
In percent of broad money 2/	6.1	5.3	4.5	7.2	7.8	6.0
Memorandum items:						
Debt structure (in percent)						
Domestic	30.0	29.2	33.5	37.5	43.7	41.9
Treasury bills	6.7	5.8	0.9	3.7	4.5	4.4
Loans	2.2	2.0	2.6	8.4	8.0	8.0
Bonds	15.2	13.7	7.5	21.2	26.9	25.9
Other (includes overdraft)	5.9	7.8	22.6	4.2	4.2	3.6
External	70.0	70.8	66.5	62.5	56.3	58.1
Official bilateral	5.4	5.1	5.9	5.3	4.3	4.3
Official multilateral	32.7	35.6	35.4	33.2	36.6	41.0
Commercial	26.8	23.1	20.5	24.2	15.5	12.9

Sources: St. Lucia authorities; and Fund staff estimates and projections.

1/ Net of intra-public sector debt (mainly central government debt to the NIC). The consolidated public sector includes the government, the National Insurance Corporation (NIC), and nonfinancial public enterprises.

2/ Including foreign currency deposits.

Table 7. St. Lucia: Indicators of External and Financial Vulnerability, 2004–09
(Annual percentage changes, unless otherwise specified)

	2004	2005	2006	2007	Prel. 2008	Proj. 2009
External indicators						
Merchandise exports	-12.0	-7.7	32.2	-13.7	83.5	-8.9
Merchandise imports	-2.0	20.1	24.6	4.0	6.7	-41.3
Terms of trade deterioration (-)	-5.8	-3.8	-13.2	-12.8	-14.0	-1.2
Tourism earnings	15.5	9.3	-20.0	6.0	3.1	-18.8
Banana export earnings	23.6	-23.0	15.9	-9.2	22.5	10.8
Current account balance (in percent of GDP)	-10.9	-17.1	-30.2	-40.6	-34.5	-17.5
Capital and financial account balance (in percent of GDP) 1/	12.6	15.9	34.3	36.4	30.2	15.3
Of which						
Foreign direct investment (in percent of GDP)	9.6	8.9	25.1	26.4	10.6	7.6
Gross international reserves of the ECCB						
In millions of U.S. dollars	632.4	600.8	696.0	764.5	759.0	687.4
In percent of broad money	20.4	17.9	18.6	18.6	17.9	16.4
Gross imputed reserves						
In millions of U.S. dollars	130.2	114.2	132.2	151.2	140.3	118.5
In percent of short-term liablilities	516.8	943.5	1,092.1	1,249.2	…	…
External public debt (in percent of GDP)	46.1	47.4	43.2	43.9	37.9	40.6
External debt service (in percent of exports of goods and nonfactor services)	8.2	6.5	7.6	12.2	11.7	11.1
Of which						
Interest	3.9	2.2	4.6	3.7	3.2	4.0
Nominal exchange rate (EC dollars per U.S. dollar, end period)	2.7	2.7	2.7	2.7	2.7	2.7
Real effective exchange rate depreciation (-), end period	-4.8	-0.5	0.5	-3.6	1.1	...
Financial indicators						
Broad money	10.1	13.4	20.1	6.2	6.5	7.2
Credit to the private sector	10.2	16.2	24.5	29.5	11.6	-5.4
Prudential indicators (in percent)						
Capital adequacy ratio (local banks)	18.0	14.4	17.6	20.2	15.6	...
NPLs to total loans ratio	17.3	12.6	8.5	5.8	6.6	...
Of which						
Local banks	22.2	16.5	10.5	7.3	9.0	...
Foreign banks	13.4	9.9	7.1	4.8	5.0	...
Loan loss provision to NPLs ratio	36.1	40.4	40.1	45.5	37.5	...
Of which						
Local banks	39.0	44.8	35.2	38.6	27.8	...
Foreign banks	32.3	35.4	45.2	52.2	48.6	...
Gross government claims to total assets ratio	13.0	14.6	11.8	10.0	9.7	...
Foreign currency deposits to total deposits ratio	2.1	3.0	9.0	5.6	6.3	...
Net foreign currency exposure to capital (local banks)	65.2	122.3	53.6	73.9	49.3	...
Contingent liabilities to capital (local banks)	124.4	149.5	124.3	78.3	104.3	...
(Pre-tax) return on average assets	2.4	2.3	2.4	2.8	3.2	...
Yield to maturity sovereign bonds 2/	13.7	12.2	7.2	...	...	…

Sources: St. Lucia authorities; ECCB; and Fund staff estimates and projections.

1/ Includes errors and omissions.
2/ Composite Index.

Table 8. St. Lucia: Indicators of Capacity to Repay the Fund, 2008–19 1/

	Est.	Projections										
	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Fund obligations based on existing credit (in millions of SDRs)	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Principal	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Charges and interest	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Fund obligations based on existing and prospective credit (in millions of SDRs)	0.00	0.01	0.03	0.03	0.03	0.03	0.03	1.40	1.40	1.39	1.38	1.38
Principal	0.00	0.00	0.00	0.00	0.00	0.00	0.00	1.38	1.38	1.38	1.38	1.38
Charges and interest	0.00	0.01	0.03	0.03	0.03	0.03	0.03	0.03	0.02	0.01	0.01	0.00
Fund credit outstanding based on existing and prospective credit (in millions of SDRs)	0.00	6.89	6.89	6.89	6.89	6.89	6.89	5.51	4.13	2.75	1.38	0.00
Total obligations based on existing and prospective credit												
In millions of U.S. dollars 2/	0.00	0.02	0.05	0.05	0.05	0.05	0.05	2.17	2.16	2.15	2.14	2.13
In percent of exports of goods and services	0.00	0.00	0.01	0.01	0.01	0.01	0.01	0.26	0.25	0.23	0.22	0.21
In percent of external debt service 3/	0.00	0.04	0.09	0.10	0.08	0.11	0.11	3.75	3.47	3.21	2.96	2.74
In percent of GDP	0.00	0.00	0.01	0.01	0.00	0.00	0.00	0.16	0.15	0.14	0.13	0.12
In percent of quota	0.00	0.09	0.23	0.23	0.23	0.23	0.23	9.18	9.14	9.09	9.05	9.00
In percent of net international reserves	0.00	0.02	0.05	0.04	0.04	0.04	0.04	1.52	1.46	1.40	1.35	1.29
Outstanding Fund credit 3/												
In millions of U.S. dollars 2/	0.00	10.65	10.65	10.65	10.65	10.65	10.65	8.52	6.39	4.26	2.13	0.00
In percent of exports of goods and services	0.00	2.14	2.04	1.74	1.63	1.53	1.34	1.02	0.73	0.46	0.22	0.00
In percent of external debt service 3/	0.00	19.32	17.28	20.24	16.82	21.70	22.28	14.69	10.26	6.35	2.95	0.00
In number of months of imports of goods and services	0.00	0.21	0.20	0.16	0.15	0.14	0.13	0.10	0.07	0.04	0.02	0.00
In percent of GDP	0.00	1.07	1.05	1.01	0.95	0.90	0.85	0.64	0.45	0.28	0.13	0.00
In percent of quota	0.00	45.00	45.00	45.00	45.00	45.00	45.00	36.00	27.00	18.00	9.00	0.00
In percent of net international reserves	0.00	8.99	9.12	8.95	8.45	8.20	7.71	5.97	4.32	2.78	1.34	0.00
Net use of Fund credit (in millions of SDRs)	0.00	6.89	0.00	0.00	0.00	0.00	0.00	-1.38	-1.38	-1.38	-1.38	-1.38
Disbursements	0.00	6.89	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Repayments and Repurchases	0.00	0.00	0.00	0.00	0.00	0.00	0.00	1.38	1.38	1.38	1.38	1.38
Memorandum items:												
Nominal GDP (in millions of U.S. dollars)	986.8	991.0	1,015.1	1,056.2	1,118.5	1,187.2	1,260.4	1,338.4	1,421.7	1,510.6	1,605.6	1,706.9
Exports of goods and services (in millions of U.S. dollars)	571.7	498.4	521.5	610.6	651.7	698.1	797.6	837.2	879.7	926.5	976.3	1,029.5
External debt service (in millions of U.S. dollars) 3/	66.8	55.1	61.6	52.6	63.3	49.1	47.8	58.0	62.3	67.1	72.2	77.7
Imports of goods and services (in millions of U.S. dollars)	853.8	610.9	628.0	781.3	834.5	886.8	986.0	1,048.9	1,110.7	1,180.9	1,250.6	1,324.6
Net imputed international reserves (in millions of U.S. dollars)	140.3	118.5	116.7	118.9	126.0	129.9	138.1	142.8	147.8	153.2	158.9	165.1

Sources: Fund staff estimates and projections.

1/ Assumes RAC-ESF access in the amount of SDR 6.89 million (45 percent of quota).

2/ US$ 1 = 0.646451 SDR (as of July 2, 2009)

3/ Including prospective repurchases/repayments.

Attachment. Letter of Intent

Mr. Dominique Strauss-Kahn July 7, 2009
Managing Director
International Monetary Fund
700 19th Street, N.W.
Washington, D.C. 20431

Dear Mr. Strauss-Kahn:

The global economic and financial crisis is having serious consequences for St. Lucia's economy. Given our dependence on tourism, foreign direct investment (FDI), and remittances from abroad, all of which have suffered sharp declines in this difficult external environment, we are experiencing severe pressures on our fiscal and balance of payments positions. As a result, economic activity is expected to contract by as much as 2½ percent and unemployment to increase substantially in 2009.

As the global downturn worsens, St. Lucia's tourism industry, which accounts for over three-quarters of exports, is expected to contract significantly in 2009. Net foreign exchange receipts from tourism are projected to fall by 21 percent, contributing to a decline in our net international reserves. FDI inflows, which support the construction industry and had begun to decline sharply in the latter half of 2008, are projected to decrease by a further 28 percent in 2009. Consequently, the overall impact on our balance of payments position is estimated at US$37 million (about 4 percent of GDP) in 2009. Moreover, our fiscal position has come under stress this year, with revenues down amid mounting expenditure pressures.

The Government's response to the crisis has been bold and wide-ranging. Our fiscal program for FY 2009–10 aims at maintaining macroeconomic stability while protecting the most vulnerable in our society, with measures to increase our tax intake and control expenditures. Among the measures on the revenue side, we are introducing a flexible petroleum pricing mechanism in August 2009 and implementing a market valuation-based property tax; and have increased taxes on alcoholic beverages, cigarettes, and vehicle licensing. Together, our revenue measures are expected to achieve broadly stable current revenue receipts, despite the economic downturn. On the expenditure side, we aim to prioritize spending and control costs, including: (i) delaying the third tranche of the triennial salary increase for all civil servants; (ii) capping the size of the public sector at its current levels, within the context of broader civil service reform; and (iii) introducing a voluntary 10 percent pay-cut for all members of Cabinet. Regarding capital expenditure, we intend to only implement projects for which funding is available, including borrowing from our development partners (the Caribbean Development Bank, the Kuwaiti Fund, and the World Bank). This would imply lowering capital expenditure relative to our FY 2009–10 budget, to approximately ten percent of GDP.

With these measures in place, our fiscal program allows for higher social spending, while reducing the overall fiscal deficit. We intend to spend an additional 1 percent of GDP to keep the most vulnerable St. Lucians covered under a variety of social safety nets. This includes an increase in pension allowances and funding for social protection projects, as well as better targeting of the conditional cash transfer program. As we seek to strengthen the provision of these social services, we intend to streamline programs that are not cost effective. Taken together, our fiscal measures would allow us to achieve a primary surplus of about 0.8 percent of GDP in FY 2009–10.

With a longer-term perspective toward strong, sustainable growth, we are committed to keep debt on a solid downward trajectory and foster the private sector by improving the business climate and enhancing infrastructure. Our strategy is two-fold: (i) to target annual primary surpluses with a view to reducing the public debt-to-GDP ratio to below 60 percent by 2020, in line with the fiscal benchmarks established by the Monetary Council of the Eastern Caribbean Central Bank; and (ii) to improve the competitiveness of St. Lucia as a premier tourist destination, attract FDI, and continue the diversification of the economy. Among the key measures to be taken are: (i) introduce a value added tax (VAT) in 2010, with a uniform rate and very limited number of exempted goods and services, aimed at broadening the tax base; (ii) rationalize expenditures, with a focus on strengthening our public sector investment program; (iii) strengthen the regulation and supervision of the nonbank financial sector through passage of a package of supportive legislation in August 2009 and putting in place a Financial Regulatory Supervisory Authority by October 2009; (iv) develop a program, with assistance from USAID, to improve the competitiveness of the economy by addressing constraints identified in the World Bank Doing Business Report; and (v) implement our National Export Strategy.

We hope that the international financial community will support our efforts to restore economic growth and protect the vulnerable in our society. In this context, the Government of St. Lucia requests a purchase equivalent to SDR 6.89 million (about US$10.65 million or 45 percent of quota) under the Rapid-Access Component of the Fund's Exogenous Shocks Facility (ESF). We look forward to an early approval by the Fund of our request, and accelerated and increased financial and technical assistance from other donors, in particular the European Union, the Caribbean Development Bank, the World Bank, and governments.

The Government will continue to cooperate with the Fund in an effort to strengthen St. Lucia's balance of payments situation and maintain economic stability. We do not intend to impose new or intensify existing restrictions on the making of payments and transfers for current international transactions, introduce new or intensify trade restrictions for balance of payments purposes, or enter into bilateral payments agreements which are inconsistent with Article VIII of the Fund's Articles of Agreement.

Sincerely yours,

----------------------------------/s/--------------------------------

Hon. Stephenson King
Prime Minister and Minister for Finance

INTERNATIONAL MONETARY FUND

ST. LUCIA

External and Public Debt Sustainability Analysis

Prepared by the Staff of the International Monetary Fund

July 10, 2009

This debt sustainability analysis (DSA) assesses the sustainability of St. Lucia's public and external debt. The analysis suggests that, barring further shocks to the economy (including a prolonged weakness in the global economy and natural disasters), the baseline scenario, as discussed in this staff report, will achieve debt sustainability. St. Lucia's risk of external debt distress is moderate.

VII. INTRODUCTION

1. Notwithstanding a significant weakening of economic activity in recent years, the authorities continued to make progress in reducing macroeconomic imbalances. Real GDP growth declined steadily from an average of 3.7 percent during 2004–07 to 0.7 percent in 2008, due largely to slowing construction and tourism activities. However, fiscal imbalances narrowed during the same period, reflecting higher tax collection, and despite the impact of rising food and fuel prices. Primary surpluses of 0.7 and 0.2 percent of GDP were achieved in 2007 and 2008, respectively, the first since 2000. As a result, gross public sector debt declined from 70⅓ percent of GDP in 2007 to 67⅓ percent in 2008.

VIII. UNDERLYING DSA ASSUMPTIONS

2. The **baseline scenario** assumes the authorities will implement the near-term policies agreed with staff. In the medium term, growth is projected at around 4 percent, driven by a recovery in tourism and construction activities starting in 2011. While these main parameters imply a rate of growth lower than the staff projections and assumptions in the 2008 Article IV consultation DSA, they are consistent with the lower growth observed in recent years and the global economic outlook, according to the latest IMF *World Economic Outlook* (WEO). Inflation is projected to remain low, consistent with historical averages and the currency board arrangement. Interest rates are assumed to be around 5 percent a year—a combination of St. Lucia's current borrowing costs on the Regional Government Securities Market (RGSM) and, to a lesser extent, the rates applicable to concessional financing.

3. On the revenue side, new measures include the introduction of a flexible petroleum pricing mechanism, a market valuation-based property tax, a single-rate VAT (in 2010), and an increase in taxes on alcoholic beverages, cigarettes, and vehicle registration. On the expenditure side, social expenditure would increase in the short term (2009–10), while

capital expenditure falls in 2009 and increases gradually in the medium term. Annual disbursements of external capital grants peak at 4.8 percent of GDP in 2009, mainly due to grants from the European Union. In the medium term, grants are expected to remain stable at about 0.8 percent of GDP, consistent with historical averages. The current account deficit is assumed to widen, following a sharp decline in 2009–10, due to a recovery in construction- and tourism-related imports.

Box 1. Macroeconomic Assumptions (2009–29)

- Following a prolonged slowdown in the aftermath of the global recession, real GDP growth is projected to average about 4 percent over the longer term. Inflation is expected to remain in the low single digits, anchored by the currency board arrangement.
- The primary balance of the central government (including grants) is projected to average about 1.1 percent of GDP, reflecting revenue and expenditure measures committed to by the authorities. On the revenue side, new measures include the introduction of a flexible petroleum pricing mechanism, a market valuation-based property tax, and a single-rate VAT. On the expenditure side, emphasis is on rationalization and cost control of current expenditure, and prioritization of capital expenditure. After 2009 the nominal wage bill remains constant, while capital spending rises slowly to about 10½ percent of GDP.
- Annual grants are conservatively projected at 0.8 percent of GDP, consistent with the historical average.
- The current account deficit is projected to narrow in 2009, due to a decline in economic activity and FDI-related imports. However, as tourism and construction activities pick up over the medium term, the current account deficit is expected to stabilize at about 22 percent of GDP, largely financed by FDI.
- Following a sharp decline in 2008–09, FDI is assumed to rise to around 19 percent of GDP by 2014.

IX. Evaluation of Public Sector Debt Sustainability

4. At end-2008 public debt stood at 67⅓ percent of GDP, the lowest level in the ECCU. The economic downturn would raise the fiscal deficit and the debt-to-GDP ratio in 2009–11. In subsequent years, strengthened revenue administration and tightened expenditure controls would contribute to higher primary surpluses and a gradual decline in St. Lucia's public debt-to-GDP ratio over the medium term, with the public debt-to-GDP ratio falling below

60 percent—the Eastern Caribbean Central Bank's benchmark—by 2017. All other debt indicators (PV of debt-to-revenue ratio, debt service-to-revenue ratio) show similar patterns of steady improvement, particularly with debt service as a share of current revenue falling from 30 percent in 2009 to about 17 percent in 2029.

5. At end-2008 external and domestic debt represent 38 percent and 29 percent of GDP, respectively. Regarding the stock of external debt, the largest creditors are multilaterals (about 21 percent of GDP). The Caribbean Development Bank alone holds 14 percent of GDP, followed by the World Bank Group (7 percent of GDP). In the future, most of new external borrowing requirements are expected to be financed commercially through the ECCU's RGSM. Regarding the stock of domestic debt, the largest share is owed to commercial banks.

6. Sensitivity analysis shows that economic growth is a key driver of St. Lucia's debt dynamics. If growth is assumed to remain at one standard deviation below the baseline, the PV of debt-to-GDP ratio will reach 85 percent by 2029 (Table A2, Scenario A3). If both annual growth and the primary deficit were kept at historical levels, the PV of debt-to-GDP ratio would reach 108 percent by 2029 (Table A2, Scenario A1). The impact of a potential natural disaster on St. Lucia's debt dynamics is also important—if a hurricane was to hit in 2010, increasing the primary deficit by 3 percent of GDP for three years and reducing growth to zero, then the PV of debt-to-GDP ratio would reach 82 percent by 2012, declining to 51 percent by 2029 (Table A2, Scenario A4).[6]

X. Evaluation of External Debt Sustainability

7. St. Lucia's external debt sustainability analysis includes only public sector debt, as data on private sector external borrowing are not available. As a result, the external DSA follows a similar pattern as that of the public sector DSA.

8. Under the baseline scenario, the PV of external debt declines to about 29 percent of GDP by 2029, well below the prudential threshold of 50 percent.[7] [8] All other debt and debt service ratios also remain relatively stable and below relevant indicative thresholds.

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[6] The actual impact of this shock could be lower, given the participation of St. Lucia in the Caribbean Catastrophe Risk Insurance Facility, a regional insurance pool.

[7] The DSA uses policy-dependent external debt-burden indicators. Policy performance is measured by the Country Policy and Institutional Assessment Index (CPIA), compiled annually by the World Bank. The CPIA divides countries into three performance categories (strong, medium and poor) based on the overall quality of its macroeconomic policies, with strong performers having higher prudential thresholds than poor performers. St. Lucia is classified by the CPIA as a strong performer, implying prudential thresholds on PV of debt-to-GDP, debt-to-exports and debt-to-revenue of 50, 200 and 300 percent, respectively.

9. Sensitivity analysis shows that the level of external debt is most responsive to an extreme shock of nominal exchange rate depreciation. Under this scenario—with a one-time 30 percent nominal depreciation relative to the baseline in 2010—the PV of external debt-to-GDP ratio would breach the debt-to-GDP threshold of 50 percent (Table A4, Scenario B6). Similarly, the most extreme export shock scenario—of export growth at one standard deviation below the historical average in 2010–11—would push the debt service-to-exports ratio to slightly above the 25 percent threshold in one year (Table A4, Scenario B2).

XI. CONCLUSIONS

10. Staff analysis shows that, under the baseline scenario (with an average primary surplus of around 1 percent of GDP over the medium term), imbalances for the overall public sector would be on a decreasing and sustainable path, achieving a public debt-to-GDP ratio of 60 percent by 2017—three years earlier than the timetable for attaining the debt benchmark of the Eastern Caribbean Central Bank. St. Lucia would then continue to reduce its stock of public debt steadily, reaching 43 percent of GDP by 2029.

11. St. Lucia faces a moderate risk of external debt distress. While the baseline scenario indicates no breach of any threshold over the projection period (2009–29), the most extreme shock scenario suggests breaches of the PV of debt-to-GDP and debt service-to-exports thresholds. As private external debt data are not available, some caution should be used in interpreting these results, which cover public external debt only.

[8] St. Lucia is classified as a strong performer for its present policy and institutional framework, based on an average CPIA score of 3.96 for 2005–07.

Table A1.St. Lucia: Public Sector Debt Sustainability Framework, Baseline Scenario, 2006–29
(In percent of GDP, unless otherwise indicated)

	Actual			Average 1/	Standard Deviation 1/	Estimate	Projections								
	2006	2007	2008			2009	2010	2011	2012	2013	2014	2009–14 Average	2019	2029	2015–29 Average
Public sector debt 2/	65.0	70.3	67.3			69.8	71.6	72.3	70.5	68.3	65.8		54.6	43.2	
Of which: Foreign-currency denominated	43.2	43.9	37.9			40.6	41.3	41.2	40.1	39.5	38.7		33.9	28.6	
Change in public sector debt	-2.0	5.3	-2.9			2.5	1.8	0.8	-1.8	-2.3	-2.5		-2.2	-0.7	
Identified debt-creating flows	2.0	0.7	1.4			2.6	1.9	1.0	-1.7	-2.1	-2.4		-2.2	-0.7	
Primary deficit	2.6	-0.7	-0.2	1.4	1.7	-0.8	-0.3	-0.2	-1.5	-1.8	-2.0	-1.1	-1.8	-0.4	-1.1
Revenue and grants	27.1	28.4	32.7			34.1	33.0	32.6	33.7	33.8	33.8		33.9	33.8	
Of which: Grants	0.3	0.2	2.3			4.9	2.5	0.8	0.8	0.8	0.8		0.8	0.8	
Primary (noninterest) expenditure	29.7	27.7	32.5			33.3	32.7	32.4	32.2	32.1	31.9		32.1	33.4	
Automatic debt dynamics	-0.5	1.4	1.6			3.4	2.2	1.1	-0.2	-0.4	-0.4		-0.4	-0.3	
Contribution from interest rate/growth differential	-1.5	0.7	1.5			4.2	3.2	1.8	0.1	-0.3	-0.3		0.1	0.1	
Of which: Contribution from average real interest rate	1.7	1.8	2.0			2.5	3.0	3.1	2.6	2.4	2.3		2.3	1.8	
Of which: Contribution from real GDP growth	-3.2	-1.1	-0.5			1.7	0.3	-1.3	-2.6	-2.6	-2.6		-2.2	-1.7	
Contribution from real exchange rate depreciation	0.9	0.7	0.0			-0.8	-1.0	-0.6	-0.3	-0.1	-0.1		...	...	
Other identified debt-creating flows	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Privatization receipts (negative)	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Recognition of implicit or contingent liabilities	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Debt relief (HIPC and other)	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Other (specify, e.g. bank recapitalization)	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Residual, including asset changes	-4.0	4.5	-4.3			-0.1	-0.1	-0.2	-0.1	-0.1	-0.1		0.0	0.0	
Other Sustainability Indicators															
PV of public sector debt	65.0	70.3	67.3			68.4	70.4	71.3	69.7	67.5	65.1		54.6	43.2	
Of which: Foreign-currency denominated	43.2	43.9	37.9			39.2	40.1	40.1	39.2	38.7	38.1		33.9	28.6	
Of which: External	43.2	43.9	37.9			39.2	40.1	40.1	39.2	38.7	38.1		33.9	28.6	
PV of contingent liabilities (not included in public sector debt)	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Gross financing need 3/	10.3	12.2	11.3			9.3	9.2	6.9	6.2	4.3	3.7		4.2	5.5	
PV of public sector debt-to-revenue and grants ratio (in percent)	239.9	247.5	205.9			200.4	213.0	218.9	206.8	199.5	192.5		161.1	127.8	
PV of public sector debt-to-revenue ratio (in percent)	242.3	249.7	221.1			233.8	230.5	224.3	211.8	204.3	197.1		165.0	130.9	
Of which: External 4/	161.0	156.0	124.5			133.9	131.2	126.2	119.2	117.2	115.2		102.4	86.7	
Debt service-to-revenue and grants ratio (in percent) 5/	28.6	45.3	34.9			29.6	28.7	21.8	22.9	18.0	16.7		17.6	17.2	
Debt service-to-revenue ratio (in percent) 5/	28.9	45.7	37.5			34.6	31.1	22.3	23.5	18.4	17.1		18.0	17.6	
Primary deficit that stabilizes the debt-to-GDP ratio	4.6	-5.9	2.8			-3.3	-2.1	-0.9	0.3	0.5	0.5		0.4	0.3	
Key macroeconomic and fiscal assumptions															
Real GDP growth (in percent)	4.9	1.7	0.7	1.9	2.7	-2.5	-0.4	1.8	3.7	3.9	3.9	1.7	4.0	4.0	4.0
Average nominal interest rate on forex debt (in percent)	5.0	4.4	4.3	3.9	1.2	5.3	5.4	5.3	5.3	5.4	5.4	5.3	5.3	5.4	5.4
Average real interest rate on domestic debt (in percent)	4.8	5.0	4.2	4.5	1.7	2.6	3.2	3.9	3.8	3.6	3.6	3.5	3.6	3.8	3.7
Real exchange rate depreciation (in percent, + indicates depreciation)	2.1	1.5	0.1	0.2	1.1	-2.0	...	...	...	...	...	...	...	...	...
Inflation rate (GDP deflator, in percent)	1.1	1.1	2.1	2.2	1.2	3.0	2.8	2.2	2.2	2.2	2.2	2.4	2.2	2.3	2.2
Growth of real primary spending (deflated by GDP deflator, in percent)	7.3	-5.0	18.2	5.6	10.5	-0.1	-2.2	0.9	2.9	3.6	3.2	1.4	4.0	4.0	4.3
Grant element of new external borrowing (in percent)	…	…	…	…	...	39.4	1.3	0.0	0.0	0.8	0.9	7.1	0.0	0.0	0.0

Sources: St. Lucia authorities; and Fund staff estimates and projections.

1/ Historical averages and standard deviations are generally derived over the past 10 years, subject to data availability.
2/ Nonfinancial public sector gross debt, government guaranteed debt, and government nonguaranteed debt.
3/ Gross financing need is defined as the primary deficit plus debt service plus the stock of short-term debt at the end of the last period.
4/ Revenues excluding grants.
5/ Debt service is defined as the sum of interest and amortization of medium and long-term debt.

Table A2.St. Lucia: Sensitivity Analysis for Key Indicators of Public Debt 2009–29

	Projections							
	2009	2010	2011	2012	2013	2014	2019	2029
PV of Debt-to-GDP Ratio								
Adjustment scenario	68	70	71	70	68	65	55	43
A. Alternative scenarios								
A1. Real GDP growth and primary balance are at historical averages	68	70	72	74	76	78	89	108
A2. Primary balance is unchanged from 2009	68	70	70	69	68	67	61	48
A3. Permanently lower GDP growth 1/	68	71	73	72	71	70	68	85
A4. Natural disaster 2/	68	73	78	82	79	76	64	51
B. Bound tests								
B1. Real GDP growth is at historical average minus one standard deviations in 2010–11	68	71	75	74	73	71	65	60
B2. Primary balance is at historical average minus one standard deviations in 2010–11	68	73	77	75	73	71	60	47
B3. Combination of B1–B2 using one half standard deviation shocks	68	72	76	74	72	69	59	46
B4. One-time 30 percent real depreciation in 2010	68	88	89	88	85	83	72	60
B5. 10 percent of GDP increase in other debt-creating flows in 2010	68	80	80	79	76	74	63	50
PV of Debt-to-Revenue Ratio 3/								
Adjustment scenario	200	213	219	207	199	192	161	128
A. Alternative scenarios								
A1. Real GDP growth and primary balance are at historical averages	200	213	222	221	226	231	261	316
A2. Primary balance is unchanged from 2009	200	212	216	206	201	197	179	142
A3. Permanently lower GDP growth 1/	200	215	223	214	210	206	200	252
A4. Natural disaster 2/	200	222	240	244	234	225	189	152
B. Bound tests								
B1. Real GDP growth is at historical average minus one standard deviations in 2010–11	200	214	229	219	214	210	190	178
B2. Primary balance is at historical average minus one standard deviations in 2010–11	200	222	237	224	216	209	176	140
B3. Combination of B1–B2 using one half standard deviation shocks	200	218	233	220	212	205	173	137
B4. One-time 30 percent real depreciation in 2010	200	267	275	261	253	245	213	178
B5. 10 percent of GDP increase in other debt-creating flows in 2010	200	241	247	234	226	218	185	147
Debt Service-to-Revenue Ratio 3/								
Adjustment scenario	30	29	22	23	18	17	18	17
A. Alternative scenarios								
A1. Real GDP growth and primary balance are at historical averages	30	28	23	25	22	22	28	41
A2. Primary balance is unchanged from 2009	30	29	21	22	18	18	20	19
A3. Permanently lower GDP growth 1/	30	29	22	24	19	18	22	32
A4. Natural disaster 2/	30	29	22	23	19	19	21	20
B. Bound tests								
B1. Real GDP growth is at historical average minus one standard deviations in 2010–11	30	29	23	25	20	19	21	23
B2. Primary balance is at historical average minus one standard deviations in 2010–11	30	29	25	27	20	18	18	19
B3. Combination of B1–B2 using one half standard deviation shocks	30	28	24	26	20	18	18	19
B4. One-time 30 percent real depreciation in 2010	30	30	25	27	22	21	22	23
B5. 10 percent of GDP increase in other debt-creating flows in 2010	30	29	32	27	20	18	19	20

Sources: St. Lucia authorities; and Fund staff estimates and projections.

1/ Assumes that real GDP growth is at baseline minus one standard deviation divided by the square root of 20 (i.e., the length of the projection period).
2/ Assumes that a hurricane hits St. Lucia, increasing its primary deficit by three percent of GDP for 2010–12, and reducing growth to zero.
3/ Revenues are defined inclusive of grants.

Table A3. St. Lucia: External Debt Sustainability Framework, Baseline Scenario, 2006–29 1/
(In percent of GDP, unless otherwise indicated)

	Actual			Historical	Standard	Projections									
	2006	2007	2008	Average 2/	Deviation 2/	2009	2010	2011	2012	2013	2014	2009–14 Average	2019	2029	2015–29 Average
External debt (nominal) 1/	**43.2**	**43.9**	**37.9**			**40.6**	**41.3**	**41.2**	**40.1**	**39.5**	**38.7**		**33.9**	**28.6**	
Of which: Public and publicly guaranteed (PPG)	43.2	43.9	37.9			40.6	41.3	41.2	40.1	39.5	38.7		33.9	28.6	
Change in external debt	-4.2	0.7	-6.0			2.7	0.7	-0.1	-1.1	-0.6	-0.8		-1.0	-0.4	
Identified net debt-creating flows	2.4	13.0	22.7			10.8	1.9	1.7	2.1	2.6	0.6		0.0	2.0	
Non-interest current account deficit	**28.1**	**38.6**	**32.6**	**19.7**	**10.5**	**15.5**	**14.6**	**20.3**	**20.5**	**20.0**	**19.1**		**21.6**	**23.6**	**22.2**
Deficit in balance of goods and services	25.5	35.0	28.6			11.4	10.5	16.2	16.3	15.9	14.9		17.3	18.9	
Exports	48.4	49.5	57.9			50.3	51.4	57.8	58.3	58.8	63.3		60.3	57.9	
Imports	73.9	84.5	86.5			61.6	61.9	74.0	74.6	74.7	78.2		77.6	76.8	
Net current transfers (negative = inflow)	-1.3	-1.4	-1.4	-1.8	0.5	-1.3	-1.3	-1.3	-1.3	-1.3	-1.3		-1.1	-0.7	-0.9
Of which: Official	0.0	-0.3	-0.3			-0.2	-0.2	-0.2	-0.2	-0.2	-0.2		-0.2	-0.1	
Other current account flows (negative = net inflow)	3.9	5.1	5.4			5.4	5.4	5.4	5.4	5.4	5.4		5.4	5.4	
Net FDI (negative = inflow)	**-25.1**	**-26.4**	**-10.6**	**-13.0**	**7.0**	**-7.6**	**-15.0**	**-20.0**	**-19.0**	**-18.0**	**-19.0**		**-22.0**	**-22.0**	**-22.0**
Endogenous debt dynamics 3/	**-0.6**	**0.8**	**0.8**			**2.9**	**2.3**	**1.4**	**0.6**	**0.6**	**0.5**		**0.4**	**0.4**	
Contribution from nominal interest rate	2.1	2.0	1.9			2.0	2.1	2.1	2.1	2.0	2.0		1.7	1.5	
Contribution from real GDP growth	-2.2	-0.7	-0.3			0.9	0.1	-0.7	-1.4	-1.5	-1.5		-1.3	-1.1	
Contribution from price and exchange rate changes	-0.5	-0.5	-0.9			…	…	…	…	…	…		…	…	
Residual (3-4) 4/	**-6.6**	**-12.3**	**-28.7**			**-8.1**	**-1.2**	**-1.7**	**-3.2**	**-3.1**	**-1.4**		**-1.0**	**-2.4**	
Of which: Exceptional financing	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
PV of external debt 5/	...	...	36.4			39.2	40.1	40.1	39.2	38.7	38.1		33.9	28.6	
In percent of exports	...	...	62.9			77.9	78.0	69.4	67.3	65.9	60.2		56.2	49.4	
PV of PPG external debt	**...**	**...**	**36.4**			**39.2**	**40.1**	**40.1**	**39.2**	**38.7**	**38.1**		**33.9**	**28.6**	
In percent of exports	**...**	**...**	**62.9**			**77.9**	**78.0**	**69.4**	**67.3**	**65.9**	**60.2**		**56.2**	**49.4**	
In percent of government revenues	**...**	**...**	**111.4**			**114.8**	**121.2**	**123.2**	**116.4**	**114.5**	**112.5**		**100.0**	**84.7**	
Debt service-to-exports ratio (in percent)	**7.6**	**12.2**	**11.7**			**11.1**	**11.8**	**8.6**	**9.7**	**7.0**	**6.0**		**7.5**	**8.4**	
PPG debt service-to-exports ratio (in percent)	**7.6**	**12.2**	**11.7**			**11.1**	**11.8**	**8.6**	**9.7**	**7.0**	**6.0**		**7.5**	**8.4**	
PPG debt service-to-revenue ratio (in percent)	**13.6**	**21.3**	**20.7**			**16.3**	**18.4**	**15.3**	**16.8**	**12.2**	**11.2**		**13.4**	**14.4**	
Total gross financing need (in billions of U.S. dollars)	0.1	0.2	0.3			0.1	0.1	0.1	0.1	0.1	0.0		0.1	0.2	
Non-interest current account deficit that stabilizes debt ratio	32.3	37.9	38.5			12.8	13.9	20.4	21.5	20.6	19.8		22.6	24.0	
Key macroeconomic assumptions															
Real GDP growth (in percent)	4.9	1.7	0.7	1.9	2.7	-2.5	-0.4	1.8	3.7	3.9	3.9	1.7	4.0	4.0	4.0
GDP deflator in US dollar terms (change in percent)	1.1	1.1	2.1	2.2	1.2	3.0	2.8	2.2	2.2	2.2	2.2	2.4	2.2	2.3	2.2
Effective interest rate (percent) 6/	4.7	4.8	4.6	3.9	1.2	5.3	5.4	5.3	5.3	5.4	5.4	5.3	5.3	5.4	5.4
Growth of exports of G&S (US dollar terms, in percent)	-9.5	5.2	20.3	4.7	14.1	-12.8	4.6	17.1	6.7	7.1	14.3	6.2	5.4	7.5	5.7
Growth of imports of G&S (US dollar terms, in percent)	17.0	17.5	5.3	7.7	11.3	-28.4	2.8	24.4	6.8	6.3	11.2	3.8	5.9	7.1	6.2
Grant element of new public sector borrowing (in percent)	...	...	...	...	...	39.4	1.3	0.0	0.0	0.8	0.9	7.1	0.0	0.0	0.0
Government revenues (excluding grants, in percent of GDP)	27.1	28.4	32.7	…	…	34.1	33.0	32.6	33.7	33.8	33.8	33.5	33.9	33.8	33.8
Aid flows (in billions of US dollars) 7/	0.00	0.00	0.02			0.05	0.03	0.01	0.01	0.01	0.01		0.01	0.03	
Of which: Grants	0.00	0.00	0.02			0.05	0.03	0.01	0.01	0.01	0.01		0.01	0.03	
Of which: Concessional loans	0.00	0.00	0.00			0.00	0.00	0.00	0.00	0.00	0.00		0.00	0.00	
Grant-equivalent financing (in percent of GDP) 8/	…	…	…			7.4	2.6	0.8	0.8	0.8	0.8		0.8	0.8	0.8
Grant-equivalent financing (in percent of external financing) 8/	…	…	…			65.4	31.7	15.3	14.1	17.7	19.9		16.8	14.4	15.6
Memorandum items															
Nominal GDP (in billions of US dollars)	0.9	1.0	1.0			1.0	1.0	1.1	1.1	1.2	1.3		1.7	3.2	
Nominal dollar GDP growth	6.1	2.9	2.8			0.4	2.4	4.0	5.9	6.1	6.2		6.3	6.4	
PV of PPG external debt (in billions of US dollars)	…	…	0.4			0.4	0.4	0.4	0.4	0.5	0.5		0.6	0.9	
(PVt-PVt-1)/GDPt-1 (in percent)	…	…	0.0			2.9	1.8	1.7	1.4	1.9	1.7		1.3	1.4	

Source: Staff simulations.

1/ Includes public sector guaranteed and non-guaranteed external debt.
2/ Historical averages and standard deviations are generally derived over the past 10 years, subject to data availability.
3/ Derived as [i - g - r(1+g)]/(1+g+r+gr) times previous period debt ratio, with i = nominal interest rate; g = real GDP growth rate, and r = growth rate of GDP deflator in U.S. dollar terms.
4/ Includes exceptional financing (i.e., changes in arrears and debt relief); changes in gross foreign assets; and valuation adjustments. For projections also includes contribution from price and exchange rate changes.
5/ Assumes that NPV of private sector debt is equivalent to its face value.
6/ Current-year interest payments divided by previous period debt stock.
7/ Defined as grants, concessional loans, and debt relief.
8/ Grant-equivalent financing includes grants provided directly to the government and through new borrowing (difference between the face value and the NPV of new debt).

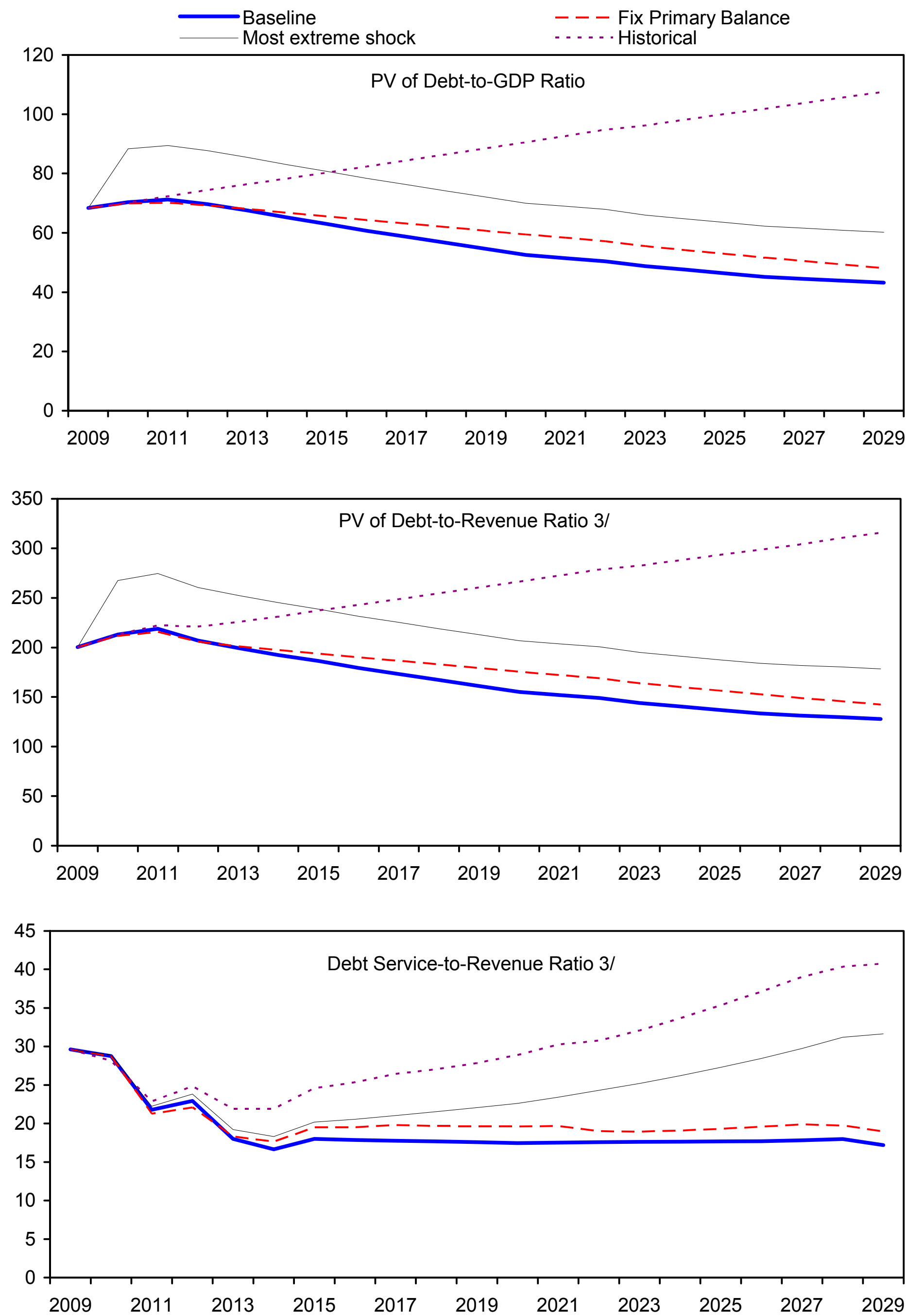
Table A4.St. Lucia: Sensitivity Analysis for Key Indicators of Public and Publicly Guaranteed External Debt, 2009–29
(In percent)

	Projections							
	2009	2010	2011	2012	2013	2014	**2019**	2029
PV of debt-to GDP ratio								
Adjustment scenario	39	40	40	39	39	38	**34**	29
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2009–29 1/	39	42	44	44	44	46	**52**	43
A2. New public sector loans on less favorable terms in 2009–29 2/	39	41	41	41	41	41	**40**	38
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2010–11	39	40	41	40	40	39	**35**	29
B2. Export value growth at historical average minus one standard deviation in 2010–11 3/	39	48	67	62	57	53	**40**	33
B3. US dollar GDP deflator at historical average minus one standard deviation in 2010–11	39	41	41	40	40	39	**35**	29
B4. Net non-debt creating flows at historical average minus one standard deviation in 2010–11 4/	39	49	61	57	53	50	**35**	29
B5. Combination of B1–B4 using one-half standard deviation shocks	39	44	57	54	51	48	**35**	29
B6. One-time 30 percent nominal depreciation relative to the baseline in 2010 5/	39	57	57	55	55	54	**48**	40
PV of debt-to-exports ratio								
Adjustment scenario	78	78	69	67	66	60	**56**	49
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2009–29 1/	78	82	76	76	75	72	**86**	75
A2. New public sector loans on less favorable terms in 2009–29 2/	78	79	72	70	70	65	**66**	65
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2010–11	78	78	69	67	66	60	**56**	49
B2. Export value growth at historical average minus one standard deviation in 2010–11 3/	78	108	177	163	150	128	**101**	88
B3. US dollar GDP deflator at historical average minus one standard deviation in 2010–11	78	78	69	67	66	60	**56**	49
B4. Net non-debt creating flows at historical average minus one standard deviation in 2010–11 4/	78	95	106	98	91	79	**58**	49
B5. Combination of B1–B4 using one-half standard deviation shocks	78	92	129	121	113	99	**76**	65
B6. One-time 30 percent nominal depreciation relative to the baseline in 2010 5/	78	78	69	67	66	60	**56**	49
PV of debt-to-revenue ratio								
Adjustment scenario	115	121	123	116	114	112	**100**	85
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2009–29 1/	115	128	135	131	130	135	**153**	129
A2. New public sector loans on less favorable terms in 2009–29 2/	115	123	127	122	121	121	**117**	112
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2010–11	115	122	127	120	118	116	**103**	87
B2. Export value growth at historical average minus one standard deviation in 2010–11 3/	115	144	205	184	170	156	**118**	99
B3. US dollar GDP deflator at historical average minus one standard deviation in 2010–11	115	123	127	120	118	116	**103**	87
B4. Net non-debt creating flows at historical average minus one standard deviation in 2010–11 4/	115	147	188	170	158	147	**103**	85
B5. Combination of B1–B4 using one-half standard deviation shocks	115	132	177	161	151	142	**104**	86
B6. One-time 30 percent nominal depreciation relative to the baseline in 2010 5/	115	171	174	164	162	159	**141**	120
Debt service-to-exports ratio								
Adjustment scenario	11	12	9	10	7	6	**8**	8
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2009–29 1/	11	12	9	11	9	8	**14**	15
A2. New public sector loans on less favorable terms in 2009–29 2/	11	12	8	10	7	6	**9**	5
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2010–11	11	12	9	10	7	6	**8**	8
B2. Export value growth at historical average minus one standard deviation in 2010–11 3/	11	14	17	28	23	20	**15**	17
B3. US dollar GDP deflator at historical average minus one standard deviation in 2010–11	11	12	9	10	7	6	**8**	8
B4. Net non-debt creating flows at historical average minus one standard deviation in 2010–11 4/	11	12	11	17	14	12	**8**	8
B5. Combination of B1–B4 using one-half standard deviation shocks	11	13	13	20	16	14	**11**	11
B6. One-time 30 percent nominal depreciation relative to the baseline in 2010 5/	11	12	9	10	7	6	**8**	8
Debt service-to-revenue ratio								
Adjustment scenario	16	18	15	17	12	11	**13**	14
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2009–29 1/	16	18	17	19	16	15	**25**	25
A2. New public sector loans on less favorable terms in 2009–29 2/	16	18	14	16	13	12	**17**	9
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2010–11	16	18	16	17	13	12	**14**	15
B2. Export value growth at historical average minus one standard deviation in 2010–11 3/	16	18	20	32	26	24	**17**	19
B3. US dollar GDP deflator at historical average minus one standard deviation in 2010–11	16	19	16	17	13	12	**14**	15
B4. Net non-debt creating flows at historical average minus one standard deviation in 2010–11 4/	16	18	20	29	23	22	**15**	14
B5. Combination of B1–B4 using one-half standard deviation shocks	16	18	18	26	21	20	**15**	15
B6. One-time 30 percent nominal depreciation relative to the baseline in 2010 5/	16	26	22	24	17	16	**19**	20

Source: Staff projections and simulations.

1/ Variables include real GDP growth, growth of GDP deflator (in U.S. dollar terms), non-interest current account in percent of GDP, and non-debt creating flows.
2/ Assumes that the interest rate on new borrowing is by 2 percentage points higher than in the baseline, while grace and maturity periods are the same as in the baseline.
3/ Exports values are assumed to remain permanently at the lower level, but the current account as a share of GDP is assumed to return to its baseline level after the shock (implicitly assuming an offsetting adjustment in import levels).
4/ Includes official and private transfers and FDI.
5/ Depreciation is defined as percentage decline in dollar/local currency rate, such that it never exceeds 100 percent.

Figure A1. St. Lucia: Indicators of Public Debt Under Alternative Scenarios, 2009–29 1/ 2/



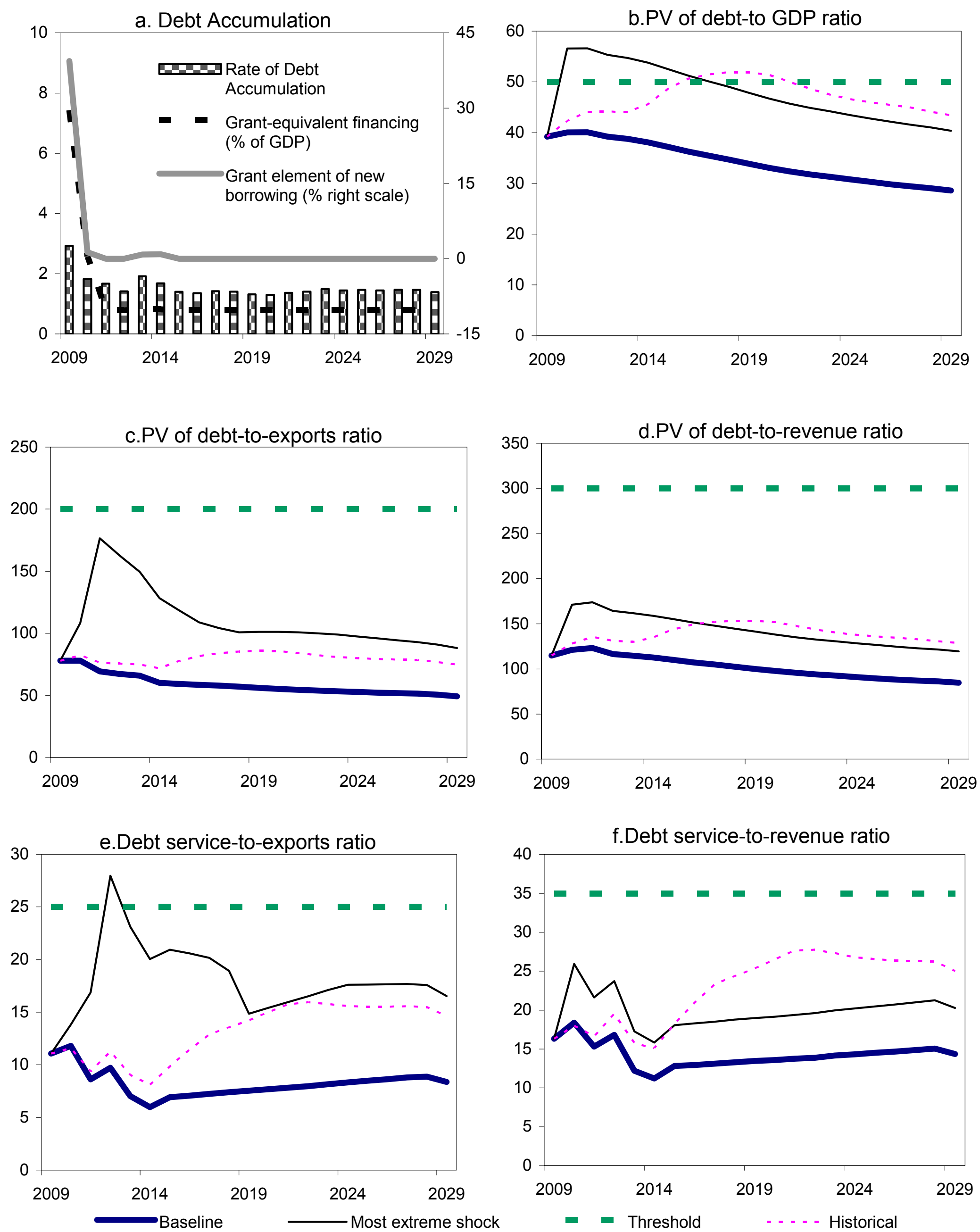
Sources: St. Lucia authorities; and Fund staff estimates and projections.

1/ The most extreme stress test is the test that yields the highest ratio in 2019.

2/ The first two figures correspond to a one-time 30 percent real depreciation in 2010, and the third figure corresponds to permanently lower GDP growth.

3/ Revenue including grants.

Figure A2. St. Lucia: Indicators of Public and Publicly Guaranteed External Debt under Alternatives Scenarios, 2009–29 1/



Source: Staff projections and simulations.

1/ The most extreme stress test is the test that yields the highest ratio in 2019. In figure b. it corresponds to a One-time depreciation shock; in c. to a Exports shock; in d. to a One-time depreciation shock; in e. to a Exports shock and in picture f. to a One-time depreciation shock.

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July 27, 2009

International Monetary Fund
Washington, D.C. 20431 USA

IMF Executive Board Approves US$10.7 Million Disbursement for St. Lucia Under the Exogenous Shocks Facility

The Executive Board of the International Monetary Fund today approved a disbursement of SDR 6.89 million (about US$10.7 million) to St. Lucia under the rapid-access component of the Exogenous Shocks Facility (ESF).

The global economic slowdown has strongly affected the tourism activity in the Caribbean region. The impact in St. Lucia has been considerable, since government tax revenue, foreign exchange reserves and employment are all closely linked to the tourism industry. The arrangement will help mitigate the impact of the global crisis on the country's economy.

Following the Executive Board discussion, Mr. Murilo Portugal, Deputy Managing Director and Acting Chair, issued the following statement:

"St. Lucia has been severely affected by the global economic and financial crisis. Sharp declines in tourism, foreign direct investment (FDI), and remittances from abroad have led to significant pressure on St. Lucia's fiscal and balance of payments positions. Real GDP growth is projected to contract by as much as 2½ percent and unemployment to increase substantially in 2009."

"The authorities' response to the crisis has been broad-based. The fiscal program for FY 2009–10 aims at maintaining macroeconomic stability while protecting social spending, with measures to enhance tax revenue and control expenditures. Among the measures on the revenue side are the introduction of a flexible petroleum pricing mechanism, the implementation of a market-valuation based property tax, and the introduction of a value-added tax in 2010. On the expenditure side, the authorities intend to prioritize spending, control costs, and only implement projects for which funding is available. Fund financing will help ease the balance of payments pressures, shore up external reserves, and catalyze support from the international donor community."

"The authorities are committed to placing public debt on a downward path, and to fostering the private sector by improving the business environment and infrastructure. They are committed to strengthening the regulation and supervision of the nonbank financial sector through a package of supportive legislation and the establishment of a Financial Regulatory Supervisory Authority."

"The authorities' implementation of prudent policies, together with support from the international donor community, will help position St. Lucia for a solid recovery once the global recession bottoms out."

Statement by Stephen O'Sullivan, Executive Director for St. Lucia

July 27, 2009

The request

The authorities of St Lucia would like to express their appreciation for the work which the staff has done in connection with this request for a purchase equivalent to 45 percent of quota under the Rapid-Access Component of the Fund's Exogenous Shocks Facility. The discussions which took place with the staff were constructive. Their outcome informed the Letter of Intent which the Prime Minister transmitted to the Fund on July 7, 2009. The authorities hope that the request will be approved as part of the response of the international financial community to the efforts which they are making to sustain growth and improve outcomes for the more vulnerable members of society in St Lucia during this exceptionally difficult period.

Context—the pre-crisis position

Prior to the onset of the global crisis, the St Lucian economy had been performing well. Output expanded at an average annual rate of around 4 per cent between 2003 and 2007, a period that saw both favourable and unfavorable forces at play. On the positive side, output growth was stimulated by the increase in tourism and construction activity in conjunction with the Cricket World Cup. Tourism capacity was substantially increased, supported by a surge in direct foreign investment and an uplift in public expenditure on infrastructure. On the negative side, a hurricane in August 2007 adversely affected agricultural output and damaged public infrastructure, and there was an earthquake in November of that year.

Progress was being made in reducing fiscal imbalances prior to the crisis. A primary budget surplus was recorded in 2007/08. Although rising recently on the back of public infrastructure investment, government debt remained below the regional average. Prospects for bringing the debt below the Eastern Caribbean Central Bank's (ECCB) targeted level of 60 per cent by 2020 were seen as quite good and St Lucia is still regarded as being only at a moderate risk of debt distress. Nonetheless, conscious of the fact that the reasonably strong growth performance pre-crisis was not delivering fully satisfactory government deficit and debt outcomes, St Lucia has adopted a stability-oriented fiscal policy stance.

St Lucia is in the process of transition from an agriculture-based economy to a modern services-based economy. It is currently very dependent on its tourism sector and on securing external finance for the development of that sector. Tourism accounts for over three-quarters of export earnings and is the primary driver of construction activity on the island. Visitor expenditure accounts for one-third of GDP. The capital required for the development of tourism capacity, which is the key to St Lucia's medium-term growth potential and therefore to addressing both debt sustainability concerns and improving social outcomes, is almost entirely externally sourced.

Progress on social outcomes was mixed. Unemployment, though falling, remained high. Poverty levels in rural areas were worsened by the secular decline of banana production as market access became more difficult.

Summary

St Lucia was performing quite well pre-crisis from the growth standpoint. However, principally for reasons related to the structure of the tax base, fiscal outcomes were not sufficiently strong to place the level of debt clearly on a downward path, a fact acknowledged by the authorities. Parts of the economy which once played a significant role were in secular decline. The economy remained extremely dependent on one key sector, a position that is not likely to change in the near-term. Furthermore, the development needs of that sector are largely externally financed. Accordingly, the scale and openness of the economy, its dependence on external sources of development finance and the ever-present risk of extreme weather events means that St Lucia was and still remains extremely vulnerable to unfavorable exogenous shocks.

The impact of the crisis

The crisis has seriously affected tourism earnings and capital inflows, the life-blood of the economy. The anticipated decline of over 20 per cent in net tourism earnings will impact net external reserves, a trend which will be reinforced by the expected reduction of close to one-third in foreign direct investment. As indicated in the Letter of Intent, the overall impact on the balance of payments will be around 4 per cent of GDP. The purchase which is requested would represent somewhat below 30 per cent of the emerging gap.

Principal policy issues

Fiscal policy is the key issue. It is almost one year since the Board concluded its most recent Article IV consultation with St Lucia. At that time, the view was that while medium-term growth prospects were favourable, risks were tilted to the downside. Directors highlighted the need for structural fiscal reforms and commended efforts to strengthen social safety nets. They emphasized the importance of fiscal consolidation and called for improvements in the regulation and supervision of nonbank financial institutions.

The current policy direction of the authorities is consistent with the views expressed by the Board at the conclusion of the 2008 consultations. The authorities are in the process of introducing a set of fiscal reforms which will address existing weaknesses and have durable long-term effects. The flexible oil pricing mechanism which is about to be introduced will strengthen the revenue base as will the planned introduction of VAT from April 2010, preparations for which are well on track. Together, these measures will constitute a major structural reform in the revenue base. The authorities remain appreciative of the support of CARTAC in designing the VAT reform.

The authorities are introducing other measures which will strengthen revenues both in the short-term and on a sustainable basis. These include the implementation of a market-based property tax and increased taxes on certain goods and services. In 2009, responding to the impact of the exogenous shock, the authorities intend to adjust the timing of revenue returns from the hotel industry in order to ease cash flow difficulties. This is a matter of the timing of receipts only and will have no sustained effect going forward as the deferred revenues will be recovered.

These revenue measures are being flanked by a mix of expenditure revisions embracing public sector pay, capital spending and social spending. Public sector pay will be curtailed by the deferral of some of the planned pay increases and the capping of public sector numbers. A voluntary pay reduction of 10 per cent for all members of Cabinet is being introduced. Capital expenditure will be restricted to 10 per cent of GDP this year, well below the level originally intended. These measures will create the headroom for additional spending, equivalent to 1 per cent of GDP, on social safety nets while still more than halving the scale of the originally envisaged budget deficit to below 3 per cent of GDP and the achievement of a primary surplus of 0.8 per cent of GDP. In setting the tighter target for 2009/10, the authorities had to strike a fine balance between a countercyclical budget and maintaining a sustainable fiscal stance. The revised target will send a signal to domestic and external stakeholders of the intention of the authorities to attain the fiscal benchmark set by the ECCB of reducing the debt/GDP ratio to below 60 per cent by 2020.

Financial sector issues

St Lucia has not been unduly affected by the failure of CL Financial Group. Nonetheless, recognizing potential vulnerabilities, the authorities are proceeding in cooperation with regional partners to strengthen the regulatory and supervisory structure for nonbank financial institutions. To that end, they plan to establish a unified Supervisory Authority in the coming months backed by enabling legislation that will lay down the parameters for the operation of the Authority. No new or intensified restrictions in making transfers for current international transactions are intended.

The ECCB is undertaking stress testing of commercial banks. It is worth noting that St Lucia's membership of the ECCU has provided tremendous benefits over the years in the form of low rates of inflation, foreign reserves stability and the regulatory framework. Indeed, the economic crisis has amplified the benefits of ECCU membership as seen in the coherent policy responses to the collapse of CL Financial Group.

Strengths of the St Lucian economy

The authorities would like to underline the fact that as well as having had a solid economic performance prior to the onset of the crisis and an established policy track record, St Lucia has a number of strengths which will enable it to benefit from the eventual recovery in the global economy. There are a number of projects in the pipeline which could be quickly resumed when conditions are right, providing a boost to construction activity and quick-starting a recovery. St Lucia is politically stable and is well served by its public administration. The quasi-currency board arrangement through the ECCU will continue to be a source of monetary stability. Although it is characterised by very large current account deficits, these are financed largely by non-debt creating FDI flows. The real exchange rate is not regarded as being out of line with fundamentals. St Lucia is well ranked in the World Bank's Doing Business Indicators and is a regional leader on that list. While the authorities are fully aware of the need to respect debt sustainability concerns, they would point out that on this criterion also, St Lucia ranks relatively well. St Lucia has a steady track record in seeking technical advice where necessary and, crucially, in implementing the results.

There are, of course, concerns. In addition to the debt sustainability issue already mentioned, the authorities are all too aware of the current trend in NPL ratios and in domestic provisioning and that a return to positive economic growth is still some distance away. In that respect, however, St Lucia is by no means alone.

Conclusion

The authorities reiterate their appreciation for the support that has been forthcoming from the Fund to date as they seek to deal with the impact of the global crisis on the economy. It is vital that St Lucia should be in a position to take full advantage of the eventual recovery in its external markets and that it should be able to cushion the impact on its reserves during this exceptionally difficult period. As noted in the staff report, St Lucia has an excellent debt servicing record and is implementing a revenue reforms agenda that will strengthen further its debt sustainability position. Accordingly, the authorities look forward to a positive assessment from the Executive Board of their request for a purchase under the Rapid Access Component of the Exogenous Shocks Facility in the amount of 45 per cent of quota.