

Barbados: 2002 Article IV Consultation—Staff Report; Staff Statement; Public Information Notice on the Executive Board Discussion; and Statement by the Executive Director for Barbados

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 Article IV consultation with Barbados, the following documents have been released and are included in this package:

- the staff report for the 2002 Article IV consultation, prepared by a staff team of the IMF, following discussions that ended on **October 16, 2002**, with the officials of Barbados on economic developments and policies. **Based on information available at the time of these discussions, the staff report was completed on December 20, 2002.** 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 statement of **February 6, 2003** updating information on recent developments.
- a Public Information Notice (PIN) summarizing the **views of the Executive Board as expressed during its February 7, 2003 discussion** of the staff report that concluded the Article IV consultation.
- a statement by the Executive Director for Barbados.

The document(s) listed below have been or will be separately released.

Statistical Appendix

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BARBADOS

Staff Report for the 2002 Article IV Consultation

Prepared by the Staff Representatives for the 2002 Consultation with Barbados

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December 20, 2002

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EXECUTIVE SUMMARY

- **Eight years of growth ended in 2001 as real GDP contracted by 2¾ percent**, owing mainly to the adverse impact on tourism of the global economic slowdown and the September 11 terrorist attack, as well as continuing declines in agriculture and manufacturing. Although tourist arrivals increased in the second half of 2002 relative to the same period in 2001, **real GDP is projected to decline by a further 1¾ percent in 2002.**
- To address the recession, **fiscal stimulus measures**, mainly increased capital spending, were implemented. These measures, as well as public wage increases and a deterioration in the finances of public enterprises, **widened fiscal deficits substantially in 2001 and 2002 and raised public debt relative to GDP.** A maximum average lending rate was introduced to address limited competition in the banking industry. **Protectionist measures** for the agriculture and manufacturing sectors were also adopted.
- Recognizing that stimulus policies have gone as far as possible, the authorities announced a **medium-term program of fiscal tightening and structural reforms** in October 2002. These policies include: reforms of the tax and social security systems, financial sector liberalization, and other steps to promote private investment. The authorities also intend to restrain public sector wage increases in the context of personal income tax reform.
- The authorities intend to resume Barbados' course toward trade liberalization, including in upcoming trade negotiations. **Tariff reductions, tax reform, and prudent public sector wage policy are critical for reducing the cost of doing business and enhancing external competitiveness.**
- **Financial sector reform and complementary capital market liberalization** will be pursued in the context of the Caribbean single market and economy, with the objectives of enhancing the efficiency of financial intermediation and capital inflows for investment.
- Barbados' economy faces **several risks.** A slower than expected recovery in the global economy could curtail tourism and diminish Barbados' growth prospects. A Middle East war could adversely affect tourism and raise petroleum prices. In view of the economy's vulnerabilities, the authorities are urged to implement additional measures in 2003 to secure their medium-term objectives—in particular, a public wage freeze, fuel price reform to ensure stable petroleum excise tax collections, and reductions in government spending on tourism projects that can be undertaken by the private sector.

I. INTRODUCTION

1. Discussions for the 2002 Article IV consultation and of the findings of the joint Bank-Fund FSAP mission in June–July 2002 were conducted in Bridgetown during October 2–16, 2002.¹ Barbados representatives included the prime minister (who is also the minister of finance), the governor of the central bank, and other senior government officials; the staff also met with representatives of labor, banks, and private business. Relations with the Fund, the Inter-American Development Bank (IDB), and the Caribbean Development Bank (CDB) are summarized in Attachments I, II, and III, respectively. Barbados has accepted the obligations of Article VIII, Sections 2, 3, and 4, and maintains an exchange system free of restrictions on payments and transfers for current international transactions.

II. BACKGROUND AND RECENT DEVELOPMENTS

2. **During 1993–2000, the implementation of sound fiscal policies, as well as structural reforms** that further shifted Barbados' productive base from agriculture into tourism and offshore services, helped promote strong growth of service exports in the context of its fixed exchange peg since 1975 of BD\$2 to US\$1. Real GDP growth averaged 3 percent annually and inflation 2 percent, as the unemployment rate declined from 24½ percent to 9¼ percent.

3. **Eight consecutive years of growth ended in 2001 as real GDP contracted by 2¾ percent**, owing mainly to the adverse impact on tourism of the global economic slowdown and the September 11 terrorist attack, as well as continuing declines in agriculture and manufacturing output (Table 1). The recession also reflected a deterioration in competitiveness associated with appreciation of the U.S. dollar and wage increases in Barbados that exceeded productivity gains and inflation since the late 1990s.

4. To lessen the impact of the September 11 attack, the authorities implemented a **national emergency program** in the fourth quarter of 2001, comprised mainly of fiscal stimulus measures that included: shifting spending to promote the tourism, manufacturing, and agricultural sectors; reintroducing import licenses for selected agricultural products to protect domestic production; and accelerating implementation of public investment projects. **Public sector wages increased by 2¾ percent in 2001 despite the sharp recession.**

5. The **12-month increase in consumer prices**, which averaged less than ¼ percent over 1998–99, rose to 2½ percent in 2001 and is projected to be the same in 2002, owing in part to an increase in tariff rates on agricultural and manufactured imports implemented in

¹The staff team comprised Mr. Pellechio (Head) and Mms. Randall, Eble, Xiao, and Aquino (staff assistant) (all WHD). Mr. Wajid (MAE), head of the FSAP mission, joined the mission to discuss the draft FSAP report. Ms. Lewis-Bynoe, Advisor to the Executive Director for Barbados, participated in the mission and Mr. Thomas (IDB) joined for the first week. Mr. Guzmán, Chief of WHD's Caribbean I Division, participated in final discussions.

November 2001. The **real effective exchange rate depreciated** by 9 percent in the 12 months to end-October 2002, largely reflecting depreciation of the U.S. dollar against the euro (Figure 1).

6. The **unemployment rate rose** to 10¼ percent by end-March 2002. **Real GDP is projected to decline by 1¼ percent in 2002**, although tourist arrivals increased in the second half of 2002 relative to the same period a year earlier.

7. Due to public sector wage increases in the face of the sharp recession, the fiscal stimulus and emergency measures implemented by government to reduce its depth, and deterioration in the finances of public enterprises, including significant losses in the public hotel enterprise, the **overall deficit of the nonfinancial public sector widened substantially** from ¾ percent of GDP in FY2000/01 to 3¾ percent of GDP in FY2001/02 and a projected 5 percent of GDP in FY2002/03 (fiscal year is April–March) (Table 2). The **central government deficit rose sharply** from 2 percent of GDP in FY2000/01 to 4¼ percent of GDP in FY2001/02 and a projected 5¼ percent in FY2002/03 (Table 3).

8. **Broad money grew** by 5½ percent in 2001, reflecting capital inflows and an increase in international reserves (Table 4). The **central bank continued to ease credit conditions**,² but **credit to the private sector stagnated**. Broad money is projected to rise 5½ percent in 2002, with private credit sluggish and the level of official international reserves remaining unchanged. **Nonperforming loans increased** to 5 percent of total loans in 2001, with about half fully provisioned. The **offshore sector contracted in 2001** owing mainly to Barbados' inclusion in the OECD's list of noncooperative tax havens, recovered somewhat in 2002 after its removal from the list early in the year, and slipped again as tax haven issues reemerged in bilateral tax treaty negotiations.

9. The **external current account deficit declined** from 5½ percent of GDP in 2000 to 3¾ percent of GDP in 2001, and is projected to narrow further to 3½ percent in 2002 (Table 5). This outcome stemmed from a contraction in imports in the wake of the decline in tourism and national income that was only partly offset by increased government spending. Net capital inflows more than covered the external current account deficit in 2001 as the **government issued US\$150 million in 20-year bonds in the international capital market** at an annual interest rate of 7¼ percent, 230 basis points above the 30-year U.S. treasury bond rate. As a result, the outstanding stock of public external debt rose from 21¼ percent of GDP at end-2000 to 27½ percent of GDP at end-2001 (Table 6). At end-2001 the **central bank's net international reserves** exceeded US\$700 million—equivalent to over 6 months of projected imports of goods and nonfactor services in 2002.

² The cash reserve requirement was reduced from 6 percent of deposit liabilities to 5 percent, the government securities requirement from 19 percent to 18 percent, the central bank's discount rate from 10 percent to 7½ percent, the minimum savings deposit rate from 4½ percent to 3 percent, and the maximum average lending rate from 10 percent to 8 percent.

III. POLICY DISCUSSIONS

10. The **authorities have been receptive to Fund policy advice** and have or will soon have implemented some key recommendations made by Executive Directors in concluding the previous Article IV consultation on November 26, 2001 (SUR/01/123)—in particular, elimination of import licenses reintroduced in the national emergency program; removal of the maximum average lending rate introduced as a short-term measure to address limited competition in the banking industry; and reform of the pension system to ensure its continued solvency. However, **in some areas, the authorities have not taken the course advised by the Fund**. As mentioned, public sector wages were raised significantly in the face of the recession, despite Directors' appeal to limit public wage growth and strong support for Barbados' policy of linking wage increases to productivity gains and targeted inflation. In addition, although Directors have recommended reduction of budget transfers to public enterprises by trimming operating costs and linking rate structures more closely to costs, these measures remain to be implemented.

11. The challenge facing Barbados is the **restoration of sustainable economic growth** through deficit reduction and continued financial sector liberalization, productive public investment, and tax and structural reforms, including trade liberalization and privatization of some public enterprises. The authorities addressed these issues in their **policy statement delivered to parliament shortly after the discussions**.³ They recognize that many of these measures are needed to strengthen Barbados' external competitiveness and would reverse the direction of certain policies taken since mid-2001, in particular interest rate regulation and protectionist trade measures.

A. Fiscal Policy

12. The authorities felt that they **have gone as far as possible with counter-cyclical policies** to address the recession since 2000, and are concerned about **high public debt**. They intend to implement policies to **put the nonfinancial public sector on a path toward overall balance** and strengthen public sector savings to help fund critical public investment over the medium term, with the objective of both achieving steady real growth and reducing public debt relative to GDP.

13. The authorities' economic program is projected to reduce the overall deficit of the nonfinancial public sector by 2 percent of GDP in FY2003/04 (Table 9 and Section IV). The authorities aim to **reduce discretionary spending**, believing that social progress depends more on growth than social spending in some areas, for example, government purchases of land to set up low-income housing. However, deficit reduction will be achieved mainly by **streamlining the public sector investment program to growth-oriented projects** that have

³ Government of Barbados, *Financial Statement: Economic and Financial Policies of Government*, October 22, 2002.

official long-term financing. An exception is the construction of a major hotel with substantial government financing. A government guaranteed domestic bond issue of BD\$150 million is planned to help finance infrastructural improvements that support tourism. The authorities are taking steps to expand the private sector's role in infrastructure projects.

14. In view of the need for a substantial upfront fiscal adjustment to achieve sustainability and of the risks in the external environment, **staff recommended several immediate measures**: freezing public wages and hiring, except as part of productivity enhancing reforms in critical areas, such as education; adjusting retail petroleum prices automatically to pass through fully changes in import cost; and halting nonessential public investment, particularly the construction of a major hotel, and privatizing existing government interests in hotels. The authorities were reluctant to adopt these measures immediately as they are politically sensitive and, in their policy statement, seek to address the underlying issues through alternative means.

15. The authorities acknowledged staff's concerns that **public wage increases** for 2001 and 2002 exceeded productivity gains and inflation, and put pressure on private wages, which may have helped erode Barbados' external competitiveness in a very difficult external environment. The authorities agreed on the need for restraint in the next round of wage negotiations, but were reluctant to accept the mission's recommendation for a wage freeze in the next two fiscal years. The authorities stated that they would restrain public sector wages as much as possible in the context of plans to reduce personal income taxation as part of direct tax reform (paragraph 29). They pointed out that unions already indicated their willingness to make concessions on wage increases if the government provided income tax relief. The authorities also intend to streamline public employment through attrition.

16. The authorities shared the mission's concern about unsustainable deficits in the operations of the water authority, transport board, government hotel and agricultural enterprises, and other public enterprises. They are calling for a **review of financial operations of public enterprises with a view to moving them toward cost recovery** and cutting back subsidies and transfers from the central government. They agreed with staff that action needs to be taken as soon as possible and plan to have proposals for new rate structures that cover operating costs submitted to the Fair Trading Commission.

17. Staff advised that retail petroleum prices be allowed to vary directly with import costs to protect revenue collections from **specific excise taxes on petroleum**. The authorities were not receptive given their concerns about distributional consequences and the risk of strong public reaction to higher fuel prices. They were also concerned about the impact of a sharp rise in petroleum prices on transportation and energy costs for business.

B. Monetary and Financial Sector Issues

18. The authorities discussed the **draft report of the joint Bank-Fund FSAP mission** in June–July 2002 and agreed with its conclusions on the financial system’s soundness and resilience to adverse developments (Box 1). They broadly accepted its recommendations on **strengthening regulation and supervision** and adopting a more flexible and market-oriented monetary policy framework and instruments. In line with their commitment to the Caribbean single market and economy, the authorities concurred with the mission that **capital account liberalization** must be pursued in an environment of sound macroeconomic policies and a strong framework for financial sector regulation and supervision. Staff advised that capital restrictions be reduced so that they dissuade only potentially volatile short-term flows, with a view to enhancing the efficiency of financial intermediation and capital inflows for investment.

19. The authorities viewed banks’ excess liquidity as a financial surplus that needed to be utilized to finance productive investment. **Deregulation of interest rates** was discussed with a view to improving the efficiency of financial intermediation. The minimum deposit rate exceeded the treasury bill rate throughout much of 2002, representing a cost to banks in a high-liquidity environment with controls on capital outflows. There was concern that the maximum average lending rate may impede commercial banks from using the interest rate as a mechanism for pricing risk, thereby limiting the availability of credit. The authorities decided to **eliminate the maximum average lending rate** from March 2003. While appreciating this decision, the mission recommended that the minimum deposit rate be reviewed periodically and set not higher than the three-month treasury bill rate as a first step toward eliminating it altogether.

20. The authorities plan to **phase out the tax on bank assets**, as it is unrelated to bank profitability and may discourage growth of assets. They also plan to **introduce a deposit insurance plan** in 2003 to provide full protection for small depositors and facilitate closure of failed institutions. This plan will be funded by flat rate premiums levied on all member institutions, with mandatory membership of all licensed deposit-taking institutions.

21. The authorities are seeking **strategic partners for the Barbados National Bank and Insurance Corporation of Barbados** to enhance their value for the next share offering. As such, the timing of offerings can not be ascertained, but the objective will be to reduce the government’s shareholding to less than a majority.

22. The authorities felt that their work to have Barbados removed from the OECD’s list of noncooperative tax havens helped begin to restore growth in the offshore sector. However, **the tax haven issue reemerged in negotiations for renewal of Barbados’ bilateral tax treaties**. Consequently, they will seek to narrow the difference between the onshore and offshore corporate tax rate through tax reform.

Box 1. Financial Sector Assessment Program (FSAP)—Main Conclusions

The FSAP mission's findings indicate that systemic risks in the financial sector are generally contained. Indicators of the health of the banking system and sensitivity analysis, point to a resilient and fundamentally sound system that can withstand a moderate recession. Off-shore banks are to a large extent insulated from the domestic banking system, although the importance of wealth management and treasury services in their operations exposes them to considerable market and transfer risks.

Observance of the international supervisory standards is high both in the onshore and offshore banking sector. Assessment of compliance with the Basel Core Principles for Effective Banking Supervision for the onshore banks and financial institutions indicates that of the 30 principles, 24 are "compliant" or "largely compliant," 4 are "materially noncompliant" and 2 are "not compliant." Settlement risk has been greatly reduced with the institution of the real-time gross settlement system (RTGS), which is in accordance with the Core Principles for Systemically Important Payment Systems.

Supervisory weaknesses exist in the nonbank financial sector. Credit unions have expanded rapidly and quality of their lending portfolio is weak and one fifth of outstanding loans are classified as delinquent. While the insurance sector is profitable and dynamic, serious weaknesses exist in its regulatory and supervisory framework. An assessment of the observance of the IAIS Insurance Core Principles indicates that out of 17 principles, 10 for the domestic sector and 12 for the offshore sector are "observed" or "largely observed," with important areas of nonobservance.

Capital markets remain underdeveloped and appear to present little systemic risk, given the low level of activity in the market. Limited activity and market size underscore the need to consider the development of the stock market in a regional context. In preparing for capital account liberalization, it would be important to ensure the adequacy of prudential regulations regarding foreign exchange exposures and market risks. In addition, the monetary policy framework and instruments will need to be more flexible and market oriented.

The authorities have worked hard to develop an effective framework for anti-money laundering and combating financing of terrorism (AML/CFT). The degree of AML/CFT effectiveness is commensurate with that of the broader supervision of financial institutions. Thus, effectiveness needs most attention in the insurance area and, to a lesser extent, in the securities market.

The FSAP mission recommended that:

- Regulations should be adopted to provide for market and country risks for both onshore and offshore banks. The Financial Institutions Act should be amended to strengthen the independence of CBB, impose aggregate limits on large exposure and connected lending, facilitate license revocation and distressed bank resolution, and require CBB's prior approval of the external auditor for licensees.
- A high priority should be assigned to completing the CBB assisted on site examinations of the five large credit unions and such examinations should be made regular.
- Effective supervision and regulation of the insurance sector should be instituted, including by increasing supervisory resources, independence and transparency, and by developing financial soundness standards and issuing related circulars.
- A framework for using market-based instruments of liquidity management and allowing greater market determination of interest rates should be developed.

C. External Issues

23. The authorities remain **committed to the fixed exchange rate regime** supported by prudent fiscal policies. The authorities felt that the **build-up in international reserves** through the government's large external commercial borrowing at end -2001 was necessary because of the risks to the current account, especially tourism receipts, posed by the global economic slowdown and September 11 attack. Staff agreed, adding that the very favorable terms of the government's borrowing supported this strategy. However, staff had argued that the proceeds should be used, at least in part, to reduce the cost and lengthen the maturity of existing public debt. Instead the authorities departed from their original plan to sterilize the proceeds of this bond issue and are using them largely to finance the budget, with the ratio of total public debt to GDP rising to over 60 percent in 2002.

24. Although Barbados can still access international capital markets on favorable terms, the authorities, in view of the high level of public external debt and in agreement with staff, have **no plans for large external commercial borrowing by the government**. Any such borrowing would aim solely at lowering costs and lengthening the maturity of public debt. They intend to finance the PSIP as much as possible through official long-term project finance. In light of prospective trade and financial liberalization, staff recommended that international reserves be maintained above four months of imports over the medium term and well in excess of short-term external debt on a residual maturity basis (Table 7).

25. While taking the position that the fixed exchange rate has served the country well, staff pointed out that the recession reflected not only adverse external factors but also a deterioration in external competitiveness due to appreciation of the U.S. dollar and large wage increases.⁴ The authorities were alert to the **risks to external competitiveness** posed by excessive wage increases and protectionist measures. They now see that tariff reduction would serve to reduce the cost of doing business and encourage real growth, and plan to resume progress toward trade liberalization in upcoming trade negotiations. As mentioned, they intend to restrain wage increases in the context of personal tax reform.

26. The import licenses on agricultural products reintroduced in November 2001 as part of the national emergency program were terminated in 2002. Special safeguard provisions for agriculture available from the WTO were applied in July 2002 to protect sensitive products.⁵ **Over the medium term the authorities intend to reverse recent tariff increases**, which have adversely affected import-dependent service sectors, especially tourism. Instead, assistance to some agricultural activities will be provided through direct transfers designed to restructure them to become more competitive. As stipulated in the October 2002 policy

⁴ The 12-month moving average of Barbados real effective exchange rate appreciated every month over the previous year from October 1999 through March 2002.

⁵ Barbados' index of trade restrictiveness remains unchanged at 6.

statement, some agricultural and manufactured products that received tariff protection at the WTO permissible rate of 60 percent had their rates reduced to the Caribbean common external tariff in January 2003. However, tariff rates on some poultry products were increased to protect domestic production. The authorities maintained that the timeframe for further tariff reduction will be determined in negotiations with the WTO on tariff reform and with the European Union as part of the African, Caribbean, and Pacific (ACP) group of countries to establish a new trade relationship. Staff urged an accelerated timeframe and stressed that selective protection compromises the authorities' objective of making agriculture and other industries more competitive and, more broadly, Barbados' external competitiveness.

D. Structural Issues

27. The authorities highlighted the agreement reached in May 2002 among labor, business, and government on the **fourth protocol on prices and incomes** as reflecting a common understanding of the need to link wage increases to productivity gains and inflation. Staff stressed that the public sector has a lead role in wage policy and that the recent wage increases appeared, given the sharp recession since 2000, to exceed what the protocol would suggest. As mentioned, there was agreement on the need for wage restraint in the future, although views differed on how to implement it. The authorities reiterated their support for employment rights and severance and unemployment benefits, and do not see them as impediments to labor market flexibility. Staff pointed out that mandated severance benefits limit the latitude of workers and businesses to negotiate termination of employment. Union representatives stressed the importance of fair treatment of dismissed workers.

28. As Barbados faces an aging of its population, the authorities plan to implement in January 2003 a **comprehensive reform of the public pension system** to achieve actuarial balance in the medium to long term (Box 2). Their reform will increase the contribution rate and restrain benefit growth by raising the retirement age and calculating benefits based on a person's average wage over a longer period. Staff had argued against increasing the contribution rate, but agreed that its cost may be largely shifted to labor given the tighter connection between an individual's contributions and benefits.

29. The authorities intend to implement a **comprehensive tax reform** over the next several years that reduces personal and corporate income tax rates, and gradually shifts the budget from reliance on high tariffs and direct taxes toward indirect taxes, mainly the value-added tax (VAT) (Box 3). They reiterated that the VAT had been introduced in large part in anticipation of trade liberalization and indicated a willingness to consider increasing the VAT standard rate and broaden the base to compensate for tariff reduction if it causes a loss in revenue. They viewed direct tax reform and tariff reduction as important for reducing the cost of doing business and encouraging real growth. They broadly agreed with the mission's view that **tax incentives** should be modified to promote only incremental investment, in line with FAD technical assistance recommendations.

Box 2. Summary of Pension Reform Proposals in Government's Policy Statement of October 22, 2002

The Prime Minister's financial statement outlined pension reform measures, designed to address the growing actuarial imbalance in the National Insurance Scheme (NIS). The measures, scheduled to go into effect January 1, 2003, were the outcome of extensive public debate that benefited substantially from the tripartite social partnership among labor, private businesses, and government. The main measures include:

- Increase contribution rate by 1 percent of insurable earnings each year for four years shared equally between employees and employers. The resulting rate of 17½ percent will remain in effect until 2030;
- Set the rate of accrual of pension entitlement to 2 percent per year of "final insurable earnings" for the first 20 years and then 1¼ percent per year with a maximum pension of 60 percent. Pension will be based on the best five years of insurable earnings;
- Increase standard retirement age from 65 to 67. This will start in 2006 by increasing the retirement age six months every four years until the new standard retirement age of 67 is reached in 2018;
- Permit retirement between the ages of 60 and 70 by providing an actuarially reduced pension to persons who opt for retirement prior to the standard retirement age, and an increased pension to those who retire later. A phased introduction will allow monitoring of the early retirement experience in order to protect the Fund's finances. Late retirement up to the limit of age 70 will be allowed immediately.

The adjustment of the insurable earnings limit on which the payment of pensions and other benefits is based, will shift from being determined by the minister of finance to a formula based on national average wage increases. Benefits will be increased by a formula that uses the lesser of the average wage increase and average price increase over a three year period. The increase granted will be subject to actuarial guidance on the maximum increase that may be granted to maintain a reserve ratio of five times pension expenditure.

Box 3. Summary of Tax Revenue Proposals in Government's Policy Statement of October 22, 2002

On October 22, 2002, the Prime Minister delivered his financial statement to parliament, outlining the government's policies for the short and medium term. Following parliament's passage of the legislation to reduce the onshore corporation tax rate from 40 percent to 37½ percent starting in 2002, the financial statement outlined measures designed to simplify the tax system, which include:

Corporate tax

- The onshore corporate tax rate would be reduced by 1½ percent starting in 2003 to 36 percent and then further reduced to 25 percent by 2006, with concessions and exemptions reduced commensurately.

Personal income tax

- Beginning January 1, 2003, the *basic rate* (now 25 percent on the first BD\$24,200 of taxable income) will be reduced to 22½ percent, and then further reduced to 20 percent in FY2004/05.
- In FY2005/06, the *marginal income tax rate* (now 40 percent of all taxable income above BD\$24,200) will be reduced to 37½ percent, and in FY2006/07 reduced from 37½ percent to 35 percent.
- An increase in the deduction allowable to homeowners for the cost of insurance on their properties from BD\$3,500 to BD\$6,000.
- An increase in the homeowner allowance from BD\$6,000 to BD\$10,000 in 2004.
- The introduction of a consolidated savings allowance—which consolidates personal savings allowances, so as to enable individuals to determine how best to apply this allowance among the various instruments available, including shares in credit unions, registered retirement plans.
- An increase in the threshold below which income tax is not payable (now BD\$15,000) beginning FY2004/05 to a presently undetermined amount.

30. The authorities intend to take actions over the medium term to **strengthen the finances of public enterprises** and reduce the cost of doing business. Specific actions include: (i) continuing to restructure or close loss-making operations of the public sugar company; (ii) curtailing subsidies to the public nonsugar agriculture company and limiting its role as sole importer of poultry products in the course of converting it to an institution that facilitates agricultural investment; (iii) restructuring the balance sheet of the government's tourist hotel project in order to privatize properties; and (iv) continuing to deregulate the telecommunications industry. Staff urged that these reforms be implemented expeditiously.

31. The authorities did not accept staff's advice to limit the government's role in the hotel sector to providing only environmental cleanup and essential infrastructure. Given the government's poor record of investment in hotels, staff strongly urged **privatization of hotels**. In addition, privatization of the airport and Bridgetown port were recommended so as to lower costs and improve services. Further, proceeds from privatization should be used to reduce public debt or build up the government's bank deposits.

E. Statistical Issues

32. The authorities noted that the Fund's definition of official international reserves does not include foreign assets of the National Insurance Fund (NIF) which, they believe, are a source of international reserves available to and under the control of the government. Staff stipulated that reserves data had to be assessed based on the Fund's reserves template. Staff assisted with the aggregation of government budget statistics and data on the finances of the NIF and public enterprise into a consolidated public sector account. In order to facilitate progress in improving the national statistical system using the GDDS framework, the mission urged the authorities to update the metadata and plans for improvement and to continue implementing their work program to upgrade their statistical system.

IV. MEDIUM-TERM OUTLOOK AND RISKS

33. The staff projected the authorities' economic program to be consistent with a **steady recovery of real GDP growth to 2½ percent over the medium term** with low inflation and expansion of private sector investment and employment (Table 9). This is a lower growth outlook from last year owing to a greater challenge posed by trade liberalization to agriculture and manufacturing, and uncertain prospects for the offshore sector.

34. Projected deficit reduction of 2 percent of GDP in FY2003/04 is achieved principally by **tightening capital spending**. Focusing the PSIP on growth-oriented projects with official long-term financing would reduce crowding out of private investment. Deficit reduction after FY2003/04 would be accomplished through **wage restraint and attrition in public employment, and reduction of government transfers** to public enterprises owing to improvement in their finances from structural reforms. Severance costs associated with attrition are more than covered by projected savings in transfers. Lowering direct tax rates

and import tariffs and relying more on indirect taxes on domestic consumption, along with telecommunication and other structural reforms, would lower the cost of doing business, improve incentives for private saving and investment, and enhance external competitiveness.

35. **Fiscal and external sustainability** depend critically on achievement of the full fiscal adjustment projected based on the authorities' planned medium-term economic policies (Tables 10 and 11). Fiscal sustainability is mainly attributed to expenditure reduction. About half of the 4½ percentage point improvement in the nonfinancial public sector's primary surplus over the medium term would come from reduced capital spending in FY2003/04, and the other half in subsequent years from reductions in the public wage bill and government transfers. The public wage bill declines by ½ percentage point of GDP during FY2004/05-2006/07. Greater reliance on official long-term project finance for public infrastructure investment reduces the public sector's recourse to domestic financing and supports increased private investment. As a result, the ratio of public debt to GDP declines gradually from 60½ percent in 2002 to 53¾ percent in 2006.

36. External sustainability is achieved in part from the projected fiscal adjustment, as well as a recovery in tourism receipts. **Official long-term finance and external private finance support a current account deficit of 4¼ percent of GDP over the medium term.** The ratio of public external debt rises from 29½ percent of GDP in 2002 to 32 percent of GDP in 2005 and subsequently declines.

37. The analysis of fiscal and external sustainability show a **high degree of vulnerability to various shocks**. The public debt to GDP ratio is sensitive to a higher real interest rate, lower real GDP growth, and a shortfall in the ratio of revenue to GDP. The stress tests carried out for these risks show public debt remaining above 60 percent of GDP throughout the medium term and rising above 90 percent in the latter case, although the ratio declines in the latter part of the medium term in all three cases. Public external debt is sensitive to lower real GDP growth and higher external current account deficit, with the debt ratio beginning to decline in 2006 in both cases.

38. In the discussion of risks to the medium-term outlook, staff prepared a **scenario based on a weaker fiscal adjustment after 2003** than projected based on the authorities' program. In this scenario, only the reduction in public capital spending in FY2003/04 would be realized (Table 12). Higher wage and transfer payments in subsequent years would crowd out officially financed public investment, increasing domestic financing and debt service. The overall deficit of the public sector would be 4½-5 percent of GDP over the medium term, about 3 percentage points higher than the medium-term outlook. Total public debt remains above 60 percent of GDP over the medium term. **The risks of unsustainable fiscal dynamics are amplified** as the higher debt levels under the above discussed shocks rise steadily relative to GDP throughout the medium term. The external current account deficit would be about one percentage point of GDP higher over the medium term, reflecting greater government spending, with the risk of recourse to further external commercial borrowing.

39. Barbados also faces several **exogenous risks** to its medium-term outlook. A slower than expected recovery in global economy could curtail tourism and diminish Barbados' growth prospects. A Middle East war could adversely affect tourism and cause petroleum prices to rise sharply, jeopardizing petroleum tax collections under Barbados' retail petroleum price system. Possible early parliamentary elections in 2003 may bring about a reluctance to adopting stronger measures as proposed by the staff—in particular, an immediate public wage freeze, fuel price reform to ensure stable petroleum excise tax collections, and a halt to public construction of a large hotel—in the event of adverse external developments.

V. STAFF APPRAISAL

40. The sharp recession that began in 2001 reflected adverse external shocks and a deterioration in external competitiveness owing to appreciation of the U.S. dollar and excessive wage increases. The authorities addressed the recession with fiscal stimulus measures, mainly increased capital spending. Protectionist measures for the agriculture and manufacturing sectors were also adopted. The government's external commercial borrowing in 2001 helped build up a substantial buffer of official international reserves as a precaution against risks to the external current account in the context of the fixed exchange rate regime.

41. The increase in tourist arrivals in the second half of 2002 over the depressed levels during the same period in 2001 provides evidence of an incipient recovery from the sharp recession that began in 2001. However, the authorities remain concerned about the adverse impact that a Middle East war could have on tourism and petroleum prices.

42. The authorities recognize that fiscal stimulus policies have been pursued as far as possible, given their concerns about recent accumulation of public debt. They are making an appropriate shift to medium-term policies geared to fiscal tightening and structural reforms to achieve sustainable growth. These policies would reduce the fiscal deficit substantially, reform the tax and pension systems, liberalize external trade and the financial sector, and support growth-oriented public investment projects in key sectors. Fiscal tightening includes restraining public sector wage increases in the context of personal income tax reform.

43. Staff supports these policies as broadly moving in the right direction. In view of the economy's vulnerabilities and the strong need for public sector wage restraint to preserve fiscal sustainability and enhance external competitiveness, the authorities are urged to implement stronger fiscal measures than those envisaged—in particular, an immediate public wage freeze, fuel price reform to ensure stable petroleum excise tax collections, and reductions in government spending on tourism projects that can be undertaken by the private sector. External commercial borrowing by the public sector should aim solely at reducing costs and lengthening the maturity of public debt.

44. After providing tariff protection to the agriculture and manufacturing sectors in line with Barbados' trade agreements, the authorities have reversed the reintroduction of agricultural import licenses and some recent tariff increases. However, selective protection continues. Given the benefit of tariff reduction to the critical export service sectors, the

authorities intend to pursue trade liberalization. Staff recommends aggressive pursuit, including removal of selective protection.

45. Tax and structural reforms are critical for reducing the cost of doing business and enhancing Barbados' external competitiveness. Moreover, public wage restraint is essential given the public sector's lead role in setting wages in the economy.

46. The authorities are to be commended for a successful participation in the FSAP. Elimination of the maximum average lending rate in March 2003 will be an important step toward financial sector liberalization. Staff supports further deregulation of interest rates along with complementary capital market liberalization in the context of the Caribbean single market and economy. Reducing capital restrictions so that they dissuade only potentially volatile short-term flows can enhance the efficiency of financial intermediation and capital inflows for investment.

47. Staff urges the authorities to pursue plans to privatize or increase private participation in public enterprises, especially in the hotel and financial sectors, expeditiously. Moreover, staff recommends that privatization proceeds be used to reduce public sector debt.

48. The provision and quality of data are adequate for conducting surveillance. Reporting on the finances of public enterprises has improved, although more progress is needed on the compilation of the consolidated public sector account. Availability of data on offshore banks could be improved to enhance surveillance of economic activity.

49. Staff recommends that Barbados remain on the standard 12-month Article IV consultation cycle.

Table 1. Barbados: Selected Economic and Financial Indicators

	1998	1999	2000	2001	Est. 2002
(Annual percentage changes)					
National income and prices					
Real GDP	4.2	2.9	3.0	-2.7	-1.8
GDP deflator	3.2	1.7	1.4	1.1	1.8
Consumer prices (12-month increase)	-1.3	1.6	2.4	2.8	2.0
Tourist arrivals	8.5	0.4	5.8	-6.9	-4.0
Unemployment rate (in percent of the labor force) 1/	12.3	10.4	9.2	9.9	10.5
External sector					
Exports	-11.1	6.6	4.5	-5.3	-8.6
Tourism receipts	7.3	-3.5	5.3	-1.2	-2.1
Imports	1.5	9.8	4.1	-7.6	-3.9
Real effective exchange rate (depreciation -) 2/	-1.1	4.1	6.0	-1.3	-9.0
Central government 3/					
Revenue	5.9	5.2	5.8	-0.1	-1.7
Expenditure	4.6	7.4	6.5	6.3	1.5
Money and credit 4/					
Net domestic assets	16.0	7.8	-4.3	-8.6	5.2
<i>Of which</i>					
Private sector credit	12.7	11.6	2.1	-0.3	-0.4
Public sector credit	-0.7	-0.3	-4.4	-8.5	5.1
Broad money (M2)	11.5	11.6	7.9	5.6	5.5
Velocity (GDP relative to M2)	1.8	1.7	1.6	1.5	1.4
(In percent of GDP at market prices; unless otherwise indicated)					
Public sector 3/					
Public sector overall balance (deficit -)	-0.2	-0.7	-0.7	-3.8	-5.1
Central government overall balance	0.1	-0.7	-0.7	-2.7	-4.3
National Insurance Scheme	1.1	1.2	1.5	1.6	1.7
Public enterprises	-1.4	-1.3	-1.6	-2.7	-2.5
Central government current balance (deficit -)	4.8	4.1	4.6	3.3	1.8
Savings and investment					
Gross domestic investment	18.6	19.8	17.2	17.4	17.4
Private investment	12.6	14.6	11.4	10.0	9.2
Public investment	5.9	5.3	5.8	7.4	8.2
Gross national saving	16.2	13.7	11.6	13.7	13.9
Private saving	9.4	9.2	6.7	9.7	10.7
Public saving	6.8	4.5	4.9	4.0	3.2
Foreign saving	2.4	6.0	5.6	3.7	3.4
Memorandum items:					
GDP at current market prices (millions of Barbados dollars)	4,746	4,965	5,183	5,098	5,098
Total public debt	45.5	44.2	45.7	58.7	60.6
<i>Of which</i>					
External 5/	15.6	17.2	21.2	27.5	29.4
Debt service on external public debt	5.0	6.3	4.3	5.3	6.2
(In percent of exports of goods and services)					
Overall balance of payments (deficit -)	-4.6	37.0	178.0	222.9	0.8
(In millions of U.S. dollars)					
Gross international reserves of the monetary authorities	2.3	2.5	4.0	6.0	5.8
(months of imports of goods and services)					

Sources: Barbadian authorities; and Fund staff estimates and projections.

1/ End of period.

2/ Information Notice System; for 2002, actual for end-October.

3/ Fiscal year beginning April 1st of stated year.

4/ In relation to money and quasi-money at the beginning of the period.

5/ Refers to central government and government guaranteed debt.

Table 2: Barbados: Public Sector Finances 1/

(In percent of GDP)

	1998/99	1999/00	2000/01	2001/02	Proj. 2002/03
Public sector current balance	4.9	4.3	5.1	3.5	3.0
Central government 2/	4.8	4.1	4.6	3.3	1.8
National Insurance	1.1	1.2	1.5	1.6	1.7
Public enterprises 2/	-1.1	-1.0	-1.0	-1.4	-0.5
Public sector capital expenditure	5.3	5.2	6.1	7.6	8.1
Central government 2/	4.7	4.8	5.3	6.0	6.1
<i>Of which</i>					
Capital formation	3.8	4.1	4.3	4.8	5.0
National Insurance	0.0	0.0	0.0	0.0	0.0
Public enterprises 2/	0.5	0.4	0.8	1.6	2.0
Public sector overall balance 3/	-0.2	-0.7	-0.7	-3.8	-5.1
Central government 2/	0.1	-0.7	-0.7	-2.7	-4.3
National Insurance	1.1	1.2	1.5	1.6	1.7
Public enterprises 2/ 3/	-1.4	-1.3	-1.6	-2.7	-2.5
Total public debt	45.5	44.2	45.7	58.7	60.6
Of which					
External 4/	15.6	17.2	21.2	27.5	29.4

Sources: Ministry of Finance; and Fund staff estimates.

1/ Fiscal years (April–March).

2/ Net of transfers from central government to public enterprises.

3/ Includes the following capital revenue of public enterprises (net of central government transfers) : 0.1 for 1998/99; 0.1 for 1999/00; 0.2 for 2000/01; and 0.3 for 2001/02.

4/ Refers to central government and government guaranteed debt.

Table 3. Barbados: Central Government Operations 1/

(In percent of GDP)

	1998/99	1999/00	2000/01	2001/02	Proj. 2002/03
Total revenue and grants	31.7	31.9	32.6	32.7	31.9
Current revenue	31.7	31.9	32.6	32.7	31.9
Tax revenue	30.4	30.0	30.9	31.0	30.5
Taxes on income and profits	9.5	10.2	11.3	11.0	10.8
Levies	0.6	0.6	0.5	0.5	0.6
Taxes on property	1.6	1.9	1.8	2.0	2.0
Taxes on goods and services	15.5	14.4	14.4	14.4	14.1
<i>Of which</i>					
Value-added tax	9.4	9.1	9.4	9.6	9.5
Import duties	2.8	2.7	2.6	2.8	2.8
Stamp duties	0.3	0.3	0.3	0.3	0.3
Nontax revenue 2/	1.4	1.9	1.7	1.7	1.4
Capital revenue and grants	0.0	0.0	0.0	0.0	0.0
Total expenditure and net lending	32.7	33.5	34.5	36.8	37.1
Current expenditure	27.6	28.3	28.8	30.2	30.4
Wages and salaries 3/	11.4	11.9	12.0	12.1	12.3
<i>Of which</i>					
National insurance contribution	0.7	0.7	0.7	0.7	0.7
Goods and services	3.2	3.2	3.6	3.9	4.1
Interest	4.5	5.0	4.2	4.9	5.1
Domestic	3.5	3.8	2.7	3.3	3.1
Foreign	1.0	1.2	1.5	1.6	2.0
Transfers	8.4	8.1	9.0	9.3	9.0
Capital expenditure and net lending	5.1	5.3	5.8	6.6	6.6
Acquisition of land and existing assets	0.3	0.2	0.2	0.2	0.1
Capital formation	3.8	4.1	4.3	4.8	5.0
Transfers	1.2	1.0	1.1	1.4	1.3
Net lending	-0.2	0.1	0.2	0.2	0.1
Overall surplus/deficit (-)	-0.9	-1.6	-1.9	-4.2	-5.2
Total financing	0.9	1.6	1.9	4.2	5.2
Foreign financing	-0.9	1.9	4.1	5.8	0.6
Disbursements	0.8	4.0	4.9	6.8	1.7
Amortization	-1.7	-2.1	-0.8	-1.0	-1.1
Domestic financing	1.8	-0.3	-2.2	-1.7	4.6
Banking system	0.4	-2.2	-2.1	-2.1	4.8
Central bank	0.9	-1.6	-5.1	-3.8	2.9
Commercial banks	-0.5	-0.6	3.0	1.8	1.9
Private nonbank sector	0.0	0.0	0.1	-0.3	0.2
National Insurance Scheme	1.2	1.6	-0.9	1.0	0.7
Other 4/	0.2	0.4	0.6	-0.3	-1.0
Memorandum items:					
Current surplus/deficit (-)	4.2	3.6	3.8	2.5	1.4
Primary surplus or deficit	3.6	3.3	2.3	0.7	-0.1

Sources: Ministry of Finance; and Fund staff estimates.

1/ Fiscal years (April-March). Ratios expressed relative to fiscal-year GDP.

2/ Excludes post office revenue.

3/ Includes national insurance contributions.

4/ Includes unexplained residual.

Table 4. Barbados: Summary Accounts of the Banking System

	1998	1999	2000	2001	Proj. 2002
(In millions of Barbados dollars)					
I. Central Bank					
Net international reserves	538.8	611.2	968.8	1,414.1	1,415.6
Net domestic assets	-52.7	-109.8	-405.9	-766.7	-732.6
Net credit to the public sector	-214.1	-197.2	-466.1	-777.8	-743.7
<i>Of which</i>					
Central government	-210.5	-193.0	-460.4	-770.9	-520.4
Unclassified items (net)	161.4	87.3	60.3	11.1	11.1
Medium- and long-term foreign liabilities	3.4	1.6	0.0	0.0	0.0
Monetary base	482.7	501.3	562.9	647.4	683.0
Liabilities to commercial banks	214.5	198.7	252.2	335.0	353.4
Currency in circulation	268.2	302.7	310.7	312.4	329.5
II. Banking System					
Net international reserves	417.7	517.3	892.5	1,342.0	1,343.5
Net domestic assets	2,374.3	2,583.2	2,456.5	2,181.4	2,358.0
Net credit to the public sector	333.3	325.8	193.6	-79.8	91.7
<i>Of which</i>					
Central government	585.7	573.9	471.6	228.9	607.6
Credit to the private sector	2,146.4	2,454.5	2,518.3	2,507.6	2,492.7
Unclassified items (net)	-105.3	-197.0	-255.4	-246.4	-226.4
Medium- and long-term foreign liabilities	128.8	128.8	143.5	137.1	129.1
Broad money	2,663.2	2,971.7	3,205.4	3,386.2	3,572.5
Narrow money	882.6	998.5	1,067.1	1,148.8	1,211.9
Quasi-money	1,780.7	1,973.2	2,138.3	2,237.5	2,360.5
(Annual percentage change)					
I. Central Bank					
Net international reserves	-1.7	13.4	58.5	46.0	0.1
Net domestic assets 1/	17.8	-11.8	-59.0	-64.1	5.3
Net credit to the public sector 1/	1.0	3.5	-53.6	-55.4	5.3
Monetary base	16.1	3.9	12.3	15.0	5.5
Liabilities to commercial banks	21.7	-7.4	27.0	32.8	5.5
Currency in circulation	11.9	12.9	2.6	0.5	5.5
II. Banking System					
Net international reserves	-10.4	23.8	72.5	50.4	0.1
Net domestic assets 2/	16.0	7.8	-4.3	-8.6	5.2
Net credit to the public sector 2/	-0.7	-0.3	-4.4	-8.5	5.1
Credit to the private sector	12.7	11.6	2.1	-0.3	-0.4
Broad money	11.5	11.6	7.9	5.6	5.5
Narrow money	17.1	13.1	6.9	7.7	5.5
Quasi-money	8.9	10.8	8.4	4.6	5.5

Sources: Central Bank of Barbados; and Fund staff estimates and projections.

1/ In relation to monetary base 12 months earlier.

2/ In relation to broad money 12 months earlier.

Table 5. Barbados: Balance of Payments

(In millions of U.S. dollars)

	1998	1999	2000	2001	Proj. 2002
Current account	-56.0	-148.8	-145.0	-93.8	-87.5
Merchandise trade balance	-644.1	-715.6	-743.9	-681.1	-667.2
Exports	257.0	273.9	286.3	271.2	247.9
<i>Of which</i>					
Domestic exports	189.6	196.1	189.6	176.3	163.4
Sugar and molasses	28.2	27.7	26.1	22.0	18.9
Other	161.4	168.4	163.5	154.3	144.6
Imports	901.0	989.4	1,030.2	952.2	915.1
Services (net)	591.4	571.1	602.9	586.8	587.1
Travel (credit)	711.9	686.8	723.0	714.0	699.1
Investment income (net)	-56.1	-71.4	-82.3	-93.4	-105.6
<i>Of which</i>					
Interest on public debt	-23.6	-29.0	-35.6	-44.6	-53.4
Current transfers (net)	52.8	67.1	78.4	93.9	98.2
Capital account	80.4	144.5	323.6	288.3	88.3
Long-term capital	72.0	111.3	287.0	277.1	70.2
Public sector	24.8	56.3	123.1	152.4	47.7
Central government	-13.8	43.0	104.4	164.8	48.8
Government guaranteed	39.6	14.2	19.7	-12.5	-1.1
Central Bank	-1.0	-0.9	-0.9	0.0	0.0
Private sector	47.2	55.0	163.9	124.7	22.5
Direct investment	16.7	54.1	155.7	128.0	26.5
Commercial banks	30.6	0.9	8.2	-3.2	-4.0
Short-term capital	8.4	33.2	36.6	11.2	18.1
Commercial banks	-19.7	13.6	8.8	2.1	0.0
Other private (including trade credits)	28.1	19.6	27.8	9.1	18.1
Errors and omissions	-29.1	41.4	-0.6	28.4	0.0
Overall balance (deficit -)	-4.6	37.0	178.0	222.9	0.8
Memorandum items:					
Current account (percent of GDP)	-2.4	-6.0	-5.6	-3.7	-3.4
Exports of goods and nonfactor services	1,280.6	1,266.2	1,376.5	1,356.5	1,329.8
Imports of goods and nonfactor services	1,333.2	1,414.9	1,517.6	1,450.7	1,409.9
Gross international reserves	275.4	312.4	484.4	707.0	707.8
Gross international reserves (in months of imports)	2.3	2.5	4.0	6.0	5.8
Total external debt (percent of GDP)	15.6	17.2	21.2	27.5	29.4

Sources: Central Bank of Barbados; Barbados Statistical Service; and Fund staff estimates and projections.

Table 6. Barbados: Summary of External Debt

	1998	1999	2000	2001	Proj. 2002
(In millions of U.S. dollars)					
Public and publicly guaranteed					
Total outstanding (end of year)	370.4	426.7	549.8	702.1	749.8
Central government	328.4	371.4	475.7	640.5	689.3
Government guaranteed	40.7	54.9	74.5	62.1	61.0
Central bank	1.4	0.5	-0.4	-0.4	-0.4
Debt service	64.6	79.6	59.4	71.5	81.8
Amortization	41.0	50.6	23.9	27.0	28.4
Interest payments	23.6	29.0	35.6	44.6	53.4
Private nonguaranteed debt					
Total outstanding (end of year) 1/	66.7	59.2	44.3	318.9	345.4
Debt service 2/	23.9	13.7	19.8	6.2	22.7
Amortization	19.9	7.5	14.9	6.0	15.2
Interest payments	4.0	6.3	5.0	3.6	7.6
(In percent of GDP)					
Total debt outstanding 1/	18.4	19.6	22.9	40.1	43.0
Public and publicly guaranteed debt 3/	15.6	17.2	21.2	27.5	29.4
(In percent of exports of goods and services)					
Debt service					
On total publicdebt outstanding 2/	6.9	7.4	5.8	5.7	7.9
On public and publicly guaranteed debt 3/	5.0	6.3	4.3	5.3	6.2

Sources: Ministry of Finance; Central Bank of Barbados; Barbados Statistical Service; and Fund staff estimates and projections.

1/ Includes only utilities and telecommunication until 2000. Stock adjustment in 2001. For 2001 includes all nonguaranteed external loans outstanding.

2/ Includes only utilities and telecommunication until 2002.

3/ Includes central government and government guaranteed debt.

Table 7. Barbados: Indicators of External Vulnerability

(In percent of GDP, unless otherwise indicated)

	1998	1999	2000	2001	Proj. 2002
Financial indicators					
Broad money (percent change, 12-month basis)	6.4	11.6	7.9	5.6	6.0
Private sector credit (percent change, 12-month basis)	15.9	14.8	1.6	0.3	-0.8
Three-month treasury bill rate 1/ 2/	5.7	6.1	3.9	2.0	2.8
Three-month treasury bill rate (real) 2/ 3/	3.9	3.2	1.4	-0.6	...
External indicators					
Exports of goods and services (percent change, 12-month basis in US\$)	2.6	-1.1	8.7	-1.5	-2.0
Imports of goods and services (percent change, 12-month basis in US\$)	2.8	6.1	7.3	-4.4	-2.8
Current account balance	-2.4	-6.0	-5.6	-3.7	-3.4
Capital and financial account balance	3.4	5.8	12.5	11.3	3.5
Gross official reserves (in US\$ millions)	275.4	312.4	484.4	707.0	707.8
Gross official reserves in months of imports of goods and services	2.3	2.5	4.0	6.0	5.8
Gross official reserves to short-term debt 4/ 5/	5.4	13.1	18.0	24.9	23.6
Gross official reserves to short-term debt plus current account deficit 4/ 5/	1.4	1.9	4.0	6.1	5.6
Broad money to reserves	4.8	4.8	3.3	2.4	2.5
Total public external debt	15.6	17.2	21.2	27.5	29.4
Total external debt to exports of goods and services (percent) 4/	28.9	33.7	39.9	51.8	56.4
External interest payments to exports of goods and services (percent) 4/	1.8	2.3	2.6	3.3	4.0
External amortization payments to exports of goods and services (percent) 4/	3.2	4.0	1.7	2.0	2.1
External interest payments to total fiscal revenue (percent) 4/	3.1	3.6	4.2	5.2	6.4
External amortization payments to total fiscal revenue (percent) 4/	5.4	6.4	2.8	3.2	3.4
Exchange rate (per US\$, end of period)	2.0	2.0	2.0	2.0	2.0
REER appreciation (12 month basis)	-1.1	4.1	6.0	-1.3	...
Real sector indicators					
Tourist sector 6/	15.5	14.8	15.5	15.0	14.7
Travel receipts to total exports (percent)	55.6	54.2	52.5	52.6	52.6
Tourist and general services sectors	72.7	72.2	72.8	73.5	73.4

Sources: Central Bank of Barbados; and Fund staff estimates and projections.

1/ Average rate of discount (end of period).

2/ Datum for 2002 is as of July 2002.

3/ Treasury bill rate adjusted for actual year-on-year inflation.

4/ Refers to public external debt.

5/ Maturity less than one year, defined on a residual maturity basis.

6/ Direct share (hotels and restaurants) of GDP.

Table 8. Barbados: Selected Indicators of Financial Sector Vulnerability 1/

(Percent, unless otherwise indicated)

	1998	1999	2000	2001	Mar. 2002
Solvency indicators					
Capital adequacy ratio 2/	16.6	14.9	15.9	18.2	18.3
Leverage (capital, percent of total liabilities) 2/ 3/	5.8	9.6	10.3	10.6	...
Off-balance sheet obligations, percent of liabilities	2.6	3.2	3.3	3.0	...
Liquidity indicators					
Loan to deposit ratio 4/	65.9	66.8	66.4	62.1	59.9
Demand deposits, percent of total deposits	30.7	29.2	30.5	29.5	32.8
Liquid assets, percent of total assets 5/	6.0	2.5	5.8	7.4	9.0
Excess liquidity 6/	34.0	13.8	30.7	42.8	52.8
Credit risk					
Total assets, annual growth rate	6.9	9.9	3.6	10.3	10.8
Loans and advances, annual growth rate	17.0	12.8	3.8	0.7	1.8
Mortgage loans, percent of loans and advances 7/	5.2	10.0	10.8	13.6	...
Nonperforming loans, percent of total loans	4.5	3.8	3.8	5.0	...
Loans classified as loss, percent of total loans and advances	1.3	1.4	1.8	2.0	...
Provisions for impaired assets, percent of assets	1.2	1.2	1.2	1.3	1.2
Foreign exchange risk					
Open position in foreign exchange, percent of capital 2/ 8/	-12.1	10.2	5.6	6.8	8.5
Deposits in foreign exchange, percent of deposits	13.0	14.0	9.7	11.0	11.3
Net foreign assets, percent of total assets	7.3	9.3	6.0	7.5	7.9
Profitability indicators					
Profit before tax, percent of total assets	2.6	2.4	2.5	2.2	...
Total noninterest expense, percent of total assets	4.5	4.1	4.0	3.7	...
Spread between lending rate and deposit rate 9/	6.9	6.3	7.0	8.0	...

Source: Central Bank of Barbados.

1/ Includes the seven licensed commercial banks.

2/ Does not include branches of foreign banks.

3/ Tier-1 capital.

4/ The loan-to-deposit ratio is calculated as loans and advances in percent of deposits. Note, the authorities use a different definition resulting in a higher loan-to-deposit ratio.

5/ Sum of excess cash reserve requirements and excess of the statutory requirement to invest in government securities in percent of total assets.

6/ Sum of excess cash reserve requirements and excess of the statutory requirement in percent of required reserves.

7/ Other loans, including personal loans, may be used to finance real estate activities. In 1999 a trust company transferred part of its loan portfolio to a commercial bank.

8/ Limits on open positions in foreign exchange only refer to so-called working balances.

9/ This spread does not fully reflect the intermediation margin.

Table 9. Barbados: Medium-Term Outlook

	1998	1999	Est. 2000	Proj.					
				2001	2002	2003	2004	2005	2006
(Annual percentage changes)									
National income and prices									
Real GDP	4.2	2.9	3.0	-2.7	-1.8	1.6	2.3	2.5	2.5
GDP deflator	3.2	1.7	1.4	1.1	1.8	2.0	2.0	2.0	2.0
Consumer prices (12-month increase)	-1.3	1.6	2.4	2.8	2.0	2.0	2.0	2.0	2.0
Exports	-11.1	6.6	4.5	-5.3	-8.6	0.4	0.8	1.7	1.7
Imports	1.5	9.8	4.1	-7.6	-3.9	3.3	6.7	6.5	5.4
Tourism receipts	7.3	-3.5	5.3	-1.2	-2.1	4.0	6.5	7.0	6.4
(In percent of GDP)									
Savings and investment									
Gross domestic investment	18.6	19.8	17.2	17.4	17.4	17.7	19.4	21.1	21.9
Private investment	12.6	14.6	11.4	10.0	9.2	10.5	12.0	13.5	14.5
Public investment	5.9	5.3	5.8	7.4	8.2	7.2	7.4	7.6	7.4
Gross national saving	16.2	13.7	11.6	13.7	13.9	14.0	15.3	16.8	17.5
Private saving	9.4	9.2	6.7	9.7	10.7	10.6	10.6	11.5	11.5
Public saving	6.8	4.5	4.9	4.0	3.2	3.4	4.6	5.3	6.0
Foreign saving	2.4	6.0	5.6	3.7	3.4	3.7	4.2	4.3	4.3
Total consumption	83.8	86.2	88.4	86.3	86.1	86.0	84.7	83.2	82.4
Private	63.1	65.5	67.4	60.6	69.3	69.4	68.4	67.2	66.5
Public	20.7	20.7	20.9	25.7	16.7	16.6	16.3	16.0	15.8
Public sector 1/									
Public sector overall balance (deficit -)	-0.2	-0.7	-0.7	-3.8	-5.1	-3.2	-2.6	-2.1	-1.2
Central government overall balance	0.1	-0.7	-0.7	-2.7	-4.3	-2.7	-2.3	-2.3	-2.0
National Insurance Scheme	1.1	1.2	1.5	1.6	1.7	1.6	2.1	2.0	2.1
Public enterprises	-1.4	-1.3	-1.6	-2.7	-2.5	-2.1	-2.4	-1.9	-1.3
Central government current balance (deficit -)	4.8	4.1	4.6	3.3	1.8	1.9	2.3	2.4	2.7
Total public debt	45.5	44.2	45.7	58.7	60.6	60.0	58.7	56.7	53.7
<i>Of which</i>									
External	15.6	17.2	21.2	27.5	29.4	30.6	31.7	32.0	31.5
(Annual percentage changes, unless otherwise indicated)									
Money and credit 2/									
Net domestic assets	16.0	7.8	-4.3	-8.6	5.2	3.2	3.7	4.0	4.0
<i>Of which</i>									
Private sector credit	12.7	11.6	2.1	-0.3	-0.4	2.6	3.1	3.2	3.2
Public sector credit	-0.7	-0.3	-4.4	-8.5	5.1	2.6	0.7	0.9	0.8
Money and quasi-money	11.5	11.6	7.9	5.6	5.5	3.7	4.4	4.6	4.6
Velocity (GDP relative to M2)	1.8	1.7	1.6	1.5	1.4	1.4	1.4	1.4	1.4
(In months of imports of goods and services)									
Gross official reserves	2.3	2.5	4.0	6.0	5.8	5.5	5.3	5.2	5.1
(In percent of exports of goods and services)									
Public external debt	28.9	33.7	39.9	51.8	56.4	58.8	60.6	60.8	59.7
Interest payments 3/	1.8	2.3	2.6	3.3	4.0	4.3	4.3	4.2	4.2
Amortization payments 3/	3.2	4.0	1.7	2.0	2.1	2.2	2.4	2.7	2.8

Sources: Barbadian authorities; and Fund staff estimates and projections.

1/ Fiscal year beginning April 1 of stated year.

2/ In relation to broad money at the beginning of the period.

3/ Refers to public sector debt.

Table 10. Barbados: Public Sector Debt Sustainability Framework, 1997–2006
(In percent of GDP, unless otherwise indicated)

	Actual					Projections				
	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006
I. Baseline Medium-Term Projections										
Public sector debt 1/ o/w foreign-currency denominated	47.5	45.5	44.2	45.7	58.7	60.6	60.0	58.7	56.7	53.7
	15.7	15.6	17.2	21.2	27.5	29.4	30.6	31.7	32.0	31.5
Change in public sector debt	-22.1	-1.9	-1.3	1.5	13.0	1.9	-0.6	-1.3	-2.0	-3.0
Identified debt-creating flows	-7.9	-3.1	-1.3	-1.1	4.7	4.1	1.2	0.1	-0.4	-1.3
Primary deficit	-4.3	-4.4	-4.3	-3.5	-1.0	0.0	-2.2	-3.0	-3.6	-4.5
Revenue and grants	46.2	46.0	49.7	50.9	51.2	51.2	51.4	51.9	51.7	51.8
Primary (noninterest) expenditure	41.9	41.6	45.4	47.4	50.1	51.2	49.2	48.9	48.1	47.2
Automatic debt dynamics 2/	-3.6	1.3	3.0	2.4	5.7	4.1	3.4	3.2	3.2	3.3
Contribution from interest rate/growth differential 3/	-3.6	1.3	3.0	2.4	5.7	4.0	3.4	3.2	3.2	3.3
Of which contribution from real interest rate	-0.2	3.1	4.3	3.6	4.4	4.0	4.3	4.6	4.6	4.7
Of which contribution from real GDP growth	-3.4	-1.9	-1.3	-1.2	1.3	0.0	-0.9	-1.4	-1.4	-1.4
Contribution from exchange rate depreciation 4/	0.0	0.0	0.0	0.0	0.0	0.2	0.0	0.0	0.0	0.0
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
Privatization receipts (negative)	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
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
Residual, including asset changes	-14.1	1.2	0.0	2.6	8.3	-2.2	-1.8	-1.5	-1.6	-1.7
Public sector debt in percent of revenues 1/	102.8	98.9	88.9	89.9	114.7	118.3	116.7	113.0	109.6	103.7
Gross financing 5/ In billions of U.S. dollars	22.2	14.5	14.8	12.6	15.6	20.1	18.6	18.1	17.9	17.0
	0.5	0.3	0.4	0.3	0.4	0.5	0.5	0.5	0.5	0.5
Key Macroeconomic and Fiscal Assumptions										
Real GDP growth (in percent)	5.6	4.2	3.0	2.9	-2.7	0.0	1.6	2.4	2.5	2.6
Average nominal interest rate on public debt (in percent) 6/	7.5	10.5	11.6	10.0	10.7	9.0	9.4	9.9	10.3	10.6
Average real interest rate (nominal rate minus change in GDP deflator, in percent)	0.1	7.2	10.0	8.6	9.5	6.9	7.4	8.0	8.2	8.7
Nominal appreciation (increase in US dollar value of local currency, in percent)	0.0	0.0	0.0	0.0	0.0	-0.6	0.0	0.0	0.0	0.0
Inflation rate (GDP deflator, in percent)	7.4	3.2	1.6	1.4	1.1	2.0	2.0	1.9	2.1	1.9
Growth of real primary spending (deflated by GDP deflator, in percent)	2.9	3.6	12.4	7.4	2.9	0.1	-2.3	1.7	0.9	0.7

Table 10. Barbados: Public Sector Debt Sustainability Framework, 1997–2006
(In percent of GDP, unless otherwise indicated)

	Actual					Projections				
	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006
II. Stress Tests										
1. Real GDP growth, real interest rate, and primary balance are at historical averages in 2003–2007						61.6	57.8	54.2	50.3	46.1
2. Real interest rate is at historical average plus two standard deviations in 2003 and 2004						60.6	63.2	65.1	63.6	61.1
3. Real GDP growth is at historical average minus two standard deviations in 2003 and 2004						60.6	64.5	68.5	66.5	63.5
4. Primary balance is at historical average minus two standard deviations in 2003 and 2004						60.6	61.2	62.1	60.4	57.7
5. Combination of 2–4 using one standard deviation shocks						60.6	62.9	65.7	61.2	55.5
6. One time 30 percent real depreciation in 2003 7/						60.6	75.4	75.0	73.9	72.0
7. 10 percent of GDP increase in other debt-creating flows in 2003						60.6	70.0	69.2	67.8	65.4
8. Impact on debt-to-GDP ratio if revenue-to-GDP ratio is at historical average minus two standard deviations in 2003–04						60.6	76.7	93.6	93.6	92.8
8a. Impact on debt-to-revenue ratio if revenue-to-GDP ratio is at historical average minus two standard deviations in 2003–04						120.7	227.9	278.0	184.6	182.8
Historical Statistics for Key Variables (past 10 years)										
						Historical Average				Standard Deviation
Primary deficit						-4.6				1.9
Real GDP growth (in percent)						1.7				3.4
Nominal interest rate (in percent) 6/						8.7				1.8
Real interest rate (in percent)						6.1				3.4
Inflation rate (GDP deflator, in percent)						2.5				2.7
Revenue to GDP ratio						44.5				5.4

Sources: Barbadian authorities and Fund staff estimates and projections.

1/ Indicate coverage of public sector, e.g., general government or nonfinancial public sector. Also whether net or gross debt is used.

2/ Derived as $[(r - p(1+g) - g + ae(1+r)] / (1+g+p+gp)$ times previous period debt ratio, with r = interest rate; p = growth rate of GDP deflator; g = real GDP growth rate; a = share of foreign-currency denominated debt; and e = nominal exchange rate depreciation (measured by increase in local currency value of U.S. dollar).

3/ The real interest rate contribution is derived from the denominator in footnote 2/ as $r - \pi(1+g)$ and the real growth contribution as $-g$.

4/ The exchange rate contribution is derived from the denominator in footnote 2/ as $\alpha e(1+r)$.

5/ Defined as public sector deficit, plus amortization of medium and long-term public sector debt, plus short-term debt at end of previous period.

6/ Derived as nominal interest expenditure divided by previous period debt stock.

7/ Real depreciation is defined as nominal depreciation (measured by percentage fall in dollar value of local currency) minus domestic inflation (based on GDP deflator).

Table 11. Barbados: External Sustainability Framework, 1997–2006

	Actual						Projections			
	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006
I. Baseline Medium-Term Projections										
External debt/Exports of goods and services	27.7	28.6	32.7	39.9	51.8	56.4	58.8	60.6	60.8	59.7
External debt/GDP	15.7	15.6	17.2	21.2	27.5	29.4	30.6	31.7	32.0	31.5
Change in external debt/GDP	-3.9	-0.1	1.6	4.0	6.3	1.9	1.2	1.1	0.3	-0.5
Net debt-creating external flows/GDP	-4.2	-2.9	2.0	5.2	6.2	3.6	2.8	3.0	3.0	3.0
Current account deficit, excluding interest payments/GDP	-4.4	-3.1	1.2	4.3	4.1	1.3	1.4	1.9	2.1	2.1
Deficit in balance of goods and services/GDP	2.2	2.5	5.8	5.4	3.7	3.1	3.4	4.0	4.2	4.3
Exports of goods and services/GDP	56.6	54.5	52.6	53.1	53.2	52.2	52.0	52.3	52.5	52.7
Imports of goods and services/GDP	58.8	57.0	58.3	58.6	56.9	55.3	55.4	56.2	56.8	57.0
Minus net non-debt creating capital inflows/GDP	0.2	0.4	0.3	0.1	0.2	0.2	0.1	0.1	0.1	0.1
Net foreign direct investment, equity/GDP	0.6	0.6	0.6	0.7	0.7	0.7	0.7	0.7	0.7	0.6
Net portfolio investment, equity/GDP	-0.8	-1.0	-1.0	-0.8	-0.9	-0.9	-0.8	-0.8	-0.8	-0.7
$(r-g-(\rho+g\rho))/(1+g+\rho+g\rho)$ debt/GDP	0.0	-0.1	0.5	0.8	1.9	2.1	1.2	1.0	0.8	0.8
Adjustment factor: $1+g+\rho+g\rho$	1.1	1.1	1.1	1.0	1.0	1.0	1.0	1.0	1.0	1.0
$(r-g-(\rho+g\rho))$ debt/GDP	0.0	-0.1	0.5	0.8	1.9	2.1	1.2	1.0	0.9	0.8
r (nominal interest rate) times debt/GDP	1.2	1.1	1.4	1.5	1.6	2.1	2.3	2.4	2.3	2.3
minus g (real GDP growth rate) times debt/GDP	-0.6	-0.7	-0.5	-0.5	0.6	0.5	-0.5	-0.7	-0.8	-0.8
minus $(\rho + g\rho)$ (ρ = US dollar value of GDP deflator, growth rate) times debt/GDP	-0.7	-0.6	-0.4	-0.1	-0.2	-0.5	-0.6	-0.6	-0.6	-0.7
Residual, incl. change in gross foreign assets/GDP	0.3	2.8	-0.4	-1.1	0.1	-1.7	-1.6	-1.9	-2.7	-3.5
Memorandum Items: Key macro and external assumptions										
Nominal GDP (local currency)	4,413	4,746	4,965	5,183	5,098	5,098	5,284	5,517	5,770	6,034
Nominal GDP (U.S. dollars)	2,206	2,373	2,482	2,591	2,549	2,549	2,642	2,758	2,885	3,017
Real GDP growth (in percent per year)	2.8	4.2	2.9	3.0	-2.7	-2.0	1.6	2.3	2.5	2.5
Exchange rate (local currency per U.S. dollar)	2.0	2.0	2.0	2.0	2.0	2.0	2.0	2.0	2.0	2.0
Nominal GDP deflator (in U.S. dollars, change in percent per year)	3.3	3.5	2.8	0.7	1.2	2.0	2.0	2.0	2.0	2.0
External interest rate (percent per year)	6.4	7.0	8.9	8.6	7.4	7.6	7.9	7.7	7.3	7.2
Growth of exports of goods and services (U.S. dollar terms, in percent per year)	2.8	3.6	0.8	5.5	-1.5	-2.0	3.4	4.9	5.1	4.9
Growth of imports of goods and services (U.S. dollar terms, in percent per year)	14.8	4.3	7.0	4.8	-4.4	-2.8	3.8	5.9	5.6	4.9

Table 11. Barbados: External Sustainability Framework, 1997–2006

	Actual						Projections			
	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006
II. Sensitivity Analysis for External Debt-to-GDP Ratio										
1. If interest rate, real GDP growth rate, US\$ GDP deflator growth, non-interest current account, and nondebt flows (in percent of GDP) in 2003–2007 are at average of past 10 years						29.4	26.3	22.7	18.2	12.7
2. If interest rate in 2003 and 2004 is average plus two standard deviations, others at baseline						29.4	31.7	33.9	34.2	33.8
3. If real GDP growth rate in 2003 and 2004 is average minus two standard deviations, others at baseline						29.4	33.1	37.2	37.6	37.3
4. If US\$ GDP deflator in 2003 is average minus two standard deviations, others at baseline						29.4	32.0	33.1	33.4	32.9
5. If non-interest current account (in percent of GDP) in 2003 and 2004 is average minus two standard deviations, others at baseline						29.4	36.5	43.1	43.7	43.5
6. Combination of 2–5 using one standard deviation shocks						29.4	33.9	37.7	38.2	37.8
7. One time 30 percent depreciation in year 2003 (-30% GDP deflator shock), others at baseline.						29.4	44.6	46.1	46.8	46.6
Memorandum Items										
Current account deficit, excluding interest payments (percent of GDP, average of past 10 years)						-2.8	-2.8	-2.8	-2.8	-2.8
Current account deficit, excluding interest payments (percent of GDP, standard deviation of past 10 years)						5.1	5.1	5.1	5.1	5.1
Net non-debt creating capital inflows (percent of GDP, average of past 10 years)						0.0	0.0	0.0	0.0	0.0
Interest rate (average of past 10 years)						8.0	8.0	8.0	8.0	8.0
Interest rate (standard deviation of past 10 years)						1.8	1.8	1.8	1.8	1.8
Real GDP growth rate (average of past 10 years)						1.3	1.3	1.3	1.3	1.3
Real GDP growth rate (standard deviation of past 10 years)						3.6	3.6	3.6	3.6	3.6
GDP deflator, U.S. dollar terms (average of past 10 years)						2.2	2.2	2.2	2.2	2.2
GDP deflator, U.S. dollar terms (standard deviation of past 10 years)						2.2	2.2	2.2	2.2	2.2

Sources: Barbadian authorities and Fund staff estimates and projections.

Table 12. Barbados: Public Sector Debt Sustainability Framework, 1997–2006—Weak Adjustment Scenario
(In percent of GDP, unless otherwise indicated)

	Actual						Projections			
	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006
I. Baseline Medium-Term Projections										
Public sector debt 1/ o/w foreign-currency denominated	47.5	45.5	44.2	45.7	58.7	60.6	60.0	60.8	60.9	60.4
	15.7	15.6	17.2	21.2	27.5	29.4	30.6	31.7	32.0	31.5
Change in public sector debt	-22.1	-1.9	-1.3	1.5	13.0	1.9	-0.6	0.8	0.2	-0.5
Identified debt-creating flows	-7.9	-3.1	-1.3	-1.1	4.7	4.1	1.2	2.2	1.8	1.2
Primary deficit	-4.3	-4.4	-4.3	-3.5	-1.0	0.0	-2.2	-1.0	-1.5	-2.2
Revenue and grants	46.2	46.0	49.7	50.9	51.2	51.2	51.4	51.9	51.7	51.8
Primary (noninterest) expenditure	41.9	41.6	45.4	47.4	50.1	51.2	49.2	50.9	50.2	49.5
Automatic debt dynamics 2/	-3.6	1.3	3.0	2.4	5.7	4.1	3.4	3.2	3.3	3.4
Contribution from interest rate/growth differential 3/	-3.6	1.3	3.0	2.4	5.7	4.0	3.4	3.2	3.3	3.4
Of which contribution from real interest rate	-0.2	3.1	4.3	3.6	4.4	4.0	4.3	4.6	4.7	4.9
Of which contribution from real GDP growth	-3.4	-1.9	-1.3	-1.2	1.3	0.0	-0.9	-1.4	-1.4	-1.5
Contribution from exchange rate depreciation 4/	0.0	0.0	0.0	0.0	0.0	0.2	0.0	0.0	0.0	0.0
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
Privatization receipts (negative)	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
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
Residual, including asset changes	-14.1	1.2	0.0	2.6	8.3	-2.2	-1.8	-1.5	-1.6	-1.7
Public sector debt in percent of revenues 1/	102.8	98.9	88.9	89.9	114.7	118.3	116.7	117.1	117.8	116.7
Gross financing 5/ in billions of U.S. dollars	22.2	14.5	14.8	12.6	15.6	20.1	18.6	20.1	20.2	19.7
	0.5	0.3	0.4	0.3	0.4	0.5	0.5	0.6	0.6	0.6
Key Macroeconomic and Fiscal Assumptions										
Real GDP growth (in percent)	5.6	4.2	3.0	2.9	-2.7	0.0	1.6	2.4	2.5	2.6
Average nominal interest rate on public debt (in percent) 6/	7.5	10.5	11.6	10.0	10.7	9.0	9.4	9.9	10.2	10.5
Average real interest rate (nominal rate minus change in GDP deflator, in percent)	0.1	7.2	10.0	8.6	9.5	6.9	7.4	8.0	8.2	8.5
Nominal appreciation (increase in U.S. dollar value of local currency, in percent)	0.0	0.0	0.0	0.0	0.0	-0.6	0.0	0.0	0.0	0.0
Inflation rate (GDP deflator, in percent)	7.4	3.2	1.6	1.4	1.1	2.0	2.0	1.9	2.1	1.9
Growth of real primary spending (deflated by GDP deflator, in percent)	2.9	3.6	12.4	7.4	2.9	0.1	-2.3	6.0	1.0	1.2

Table 12. Barbados: Public Sector Debt Sustainability Framework, 1997–2006—Weak Adjustment Scenario
(In percent of GDP, unless otherwise indicated)

	Actual					Projections				
	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006
II. Stress Tests										
1. Real GDP growth, real interest rate, and primary balance are at historical averages in 2003–2007						61.6	57.8	54.2	50.3	46.1
2. Real interest rate is at historical average plus two standard deviations in 2003 and 2004						60.6	63.2	67.2	67.7	67.6
3. Real GDP growth is at historical average minus two standard deviations in 2003 and 2004						60.6	64.5	70.8	71.3	71.1
4. Primary balance is at historical average minus two standard deviations in 2003 and 2004						60.6	61.2	62.1	62.4	62.0
5. Combination of 2–4 using one standard deviation shocks						60.6	62.9	65.7	63.2	59.9
6. One time 30 percent real depreciation in 2003 7/						60.6	75.4	77.0	78.1	78.6
7. 10 percent of GDP increase in other debt-creating flows in 2003						60.6	70.0	71.3	72.0	72.1
8. Impact on debt-to-GDP ratio if revenue-to-GDP ratio is at historical average minus two standard deviations in 2003–04						60.6	76.7	95.6	97.7	99.3
8a. Impact on debt-to-revenue ratio if revenue-to-GDP ratio is at historical average minus two standard deviations in 2003–04						120.7	227.9	284.1	192.8	195.6
Historical Statistics for Key Variables (past 10 years)										
						Historical Average				Standard Deviation
Primary deficit						-4.6				1.9
Real GDP growth (in percent)						1.7				3.4
Nominal interest rate (in percent) 6/						8.7				1.8
Real interest rate (in percent)						6.1				3.4
Inflation rate (GDP deflator, in percent)						2.5				2.7
Revenue to GDP ratio						44.5				5.4

Sources: Barbadian authorities; and Fund staff estimates and projections.

1/ Indicate coverage of public sector, e.g., general government or nonfinancial public sector. Also whether net or gross debt is used.

2/ Derived as $[(r - \pi(1+g) - g + \alpha e(1+r)] / (1+g+\pi+g\pi)$ times previous period debt ratio, with r = interest rate; π = growth rate of GDP deflator; g = real GDP growth rate; α = share of foreign-currency denominated debt; and e = nominal exchange rate depreciation (measured by increase in local currency value of U.S. dollar).

3/ The real interest rate contribution is derived from the denominator in footnote 2/ as $r - \pi(1+g)$ and the real growth contribution as $-g$.

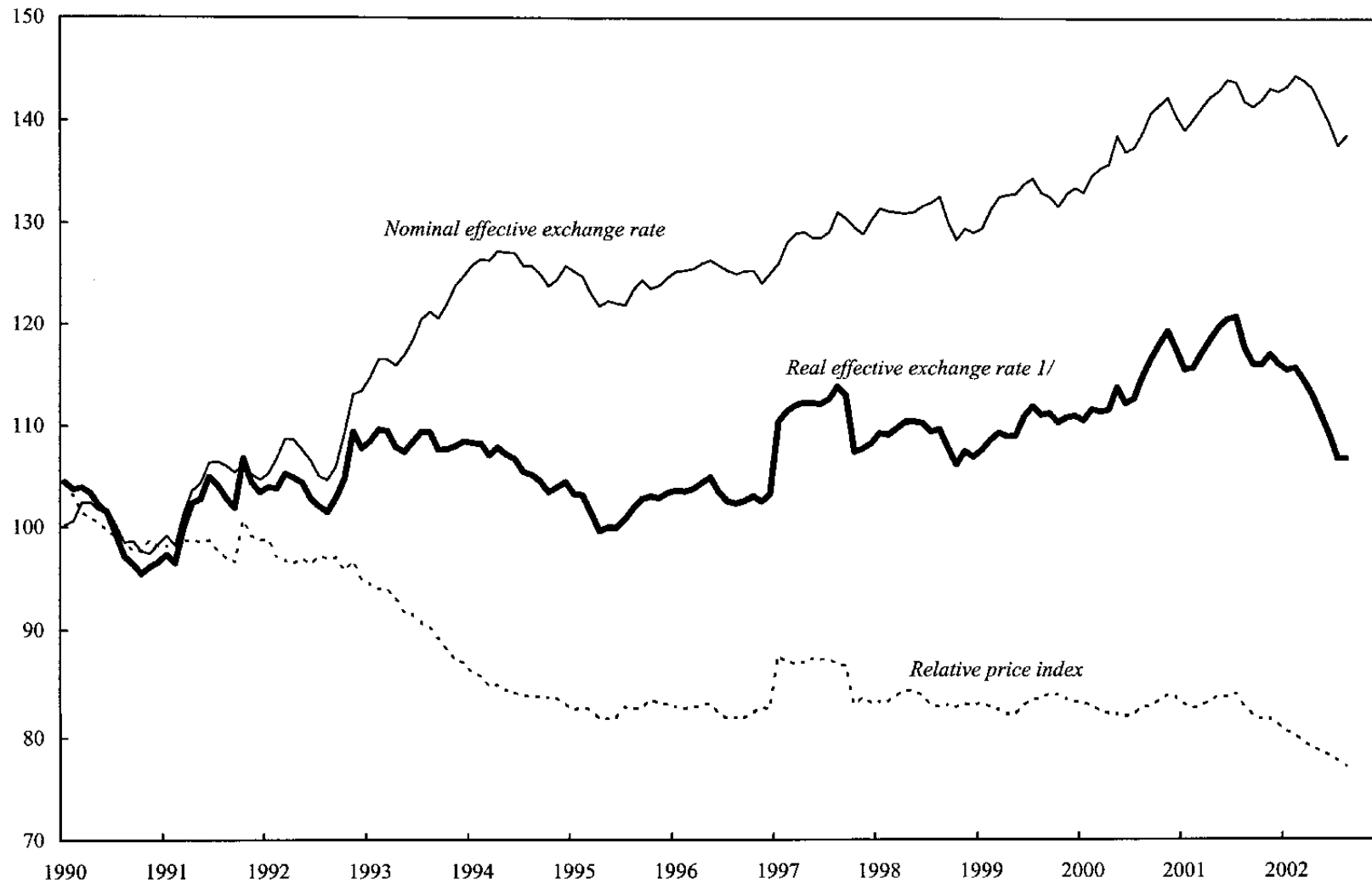
4/ The exchange rate contribution is derived from the denominator in footnote 2/ as $\alpha e(1+r)$.

5/ Defined as public sector deficit, plus amortization of medium and long-term public sector debt, plus short-term debt at end of previous period.

6/ Derived as nominal interest expenditure divided by previous period debt stock.

7/ Real depreciation is defined as nominal depreciation (measured by percentage fall in dollar value of local currency) minus domestic inflation (based on GDP deflator).

**Figure 1. Barbados: Exchange Rate Developments
(Index 1990=100)**



Sources: IMF Information Notice System; and staff estimates.

1/ The real effective exchange rate is estimated as a trade-weighted index of nominal exchange rates deflated by seasonally adjusted relative consumer prices. An increase means an appreciation.

BARBADOS—FUND RELATIONS
As of November 30, 2002

I. **Membership Status:** Joined 12/29/1970; Article VIII

II. General Resources Account:	SDR million	Percent of Quota
Quota	67.50	100.00
Fund holdings of currency	62.67	92.84
Reserve position in Fund	4.84	7.16

III. SDR Department:	SDR million	Percent of Allocation
Net cumulative allocation	8.04	100.00
Holdings	0.08	0.54

IV. **Outstanding Purchases and Loans:** None

V. **Financial Arrangements:**

Type	Approval date	Expiration date	Amount approved (SDR million)	Amount drawn (SDR million)
Stand-by	02/07/1992	05/31/1993	23.89	14.67
Stand-by	10/01/1982	05/31/1984	31.88	31.88

VI. **Projected Obligations to Fund** (SDR million; based on existing use of resources and present holdings of SDRs):

	Forthcoming			
	2002	2003	2004	2005
Principal				
Charges/Interest	--	0.16	0.16	0.16
Total	--	0.16	0.16	0.16

VII. **Exchange Rate Arrangements:**

The Barbados dollar has been pegged to the U.S. dollar since mid-1975 at BDS\$2.00 = US\$1.00. On July 31, 1995, the official buying and selling rates for the U.S. dollar were BDS\$1.9975 and BDS\$2.0350, respectively, per US\$1.

There are no restrictions on the making of payments and transfers for current international transactions subject to approval under Article VIII. There are exchange

controls on invisibles, but bona fide transactions are approved. All capital outflows and certain capital inflows require approval. The authorities accepted the obligations of Article VIII sections 2, 3, and 4 on November 3, 1993.

VIII. Last Article IV Consultation

The 2001 Article IV consultation discussion was concluded by the Executive Board on November 26, 2001 (EBM/01/119); the documents were Staff Report (SM/01/336); and Selected Issues and Statistical Appendix (SM/01/337). Barbados is on the standard 12-month consultation cycle.

IX. Technical Assistance:

Department	Dates	Purpose
CARTAC	March 18-29, 2002	Balance of Payments Technical Assistance Mission
FAD	May 28–June 8, 2001	Uniform taxation of domestic and offshore activities, and review of tax incentive regime.
STA	Jan. 25–Feb. 2, 1999	Development of metadata for the General Data Dissemination System.
FAD	Nov. 6–17, 1995 Feb. 28–Mar. 12, 1996	Introduction of a value-added tax.
MAE	Nov. 1995	Introduction of a deposit insurance scheme.
FAD	June 29–July 10, 1992 Oct. 26–Nov. 6, 1992	Reform of the indirect tax system.
FAD	Feb. 17–28, 1992	Reform of the direct tax system.
MAE	Jan. 28–Feb. 6, 1992	Restructuring of the Barbados of National Bank
STA	May 15–26, 1989	Review of balance of payments and banking statistics.
FAD	Feb. 28, 1989–Feb. 1, 1990	Resident Fiscal Advisor in the Ministry of Finance to provide assistance in budget formulation, structure, and execution.

X. Resident Representative:

The resident representatives post was closed in January 1995.

Barbados—Relations with the Inter-American Development Bank

I. ACTIVE LOANS TO BARBADOS AS OF AUGUST 2002

(In millions of U.S. dollars)

Purpose	Approval Date	Amount	Amount Disbursed	Amount Available
South Coast Sewerage	Nov. 1992	51.2	36.5	14.7
Global Pre-Investment	Dec. 1992	7.0	6.9	0.1
Bridgetown Roads	May. 1993	18.5	9.4	9.1
Solid Waste Management Program	Oct. 1998	13.0	0.1	12.9
Education Sector Enhancement Program	Dec. 1998	85.0	14.3	70.7
Administration of Justice	Aug. 2001	8.7	0.0	8.7
Coastal Infrastructure	Jan. 2002	17.0	0.0	17.0
Total		200.4	67.2	133.2

II. NET CASH FLOW OF IDB CONVERTIBLE RESOURCES

(In millions of U.S. dollars)

	1994	1995	1996	1997	1998	1999	2000	2001	2002
Loan approvals	3.6	35.0	0.0	0.0	98.0	0.0	0.0	8.7	17.0
Repayments	6.4	7.4	7.7	7.1	7.3	8.0	7.1	7.3	7.6
Disbursements	4.8	7.1	34.6	15.2	17.9	6.7	10.4	24.2	17.0
Net loan flow	-1.6	-0.3	26.9	8.1	10.6	-1.3	3.3	16.9	9.4
Interest and charges	6.3	6.7	6.7	8.0	8.3	9.8	7.4	8.7	8.9
Net cash flow	-8.1	-7.1	20.2	0.1	2.3	-12.4	-4.1	8.2	0.5
Debt service	12.7	14.1	14.4	15.1	15.6	17.8	14.5	16.0	16.5
Debt outstanding	100.6	102.0	122.4	125.0	140.2	139.6	138.5		

Source: Inter-American Development Bank.

Barbados—Relations with the Caribbean Development Bank

The Caribbean Development Bank (CDB) approved US\$197.3 million in loans to Barbados between 1970 and 2002. This represents 10.7 percent of total approvals to CDB's borrowing member countries.

Of the total funds approved US\$49.6 million or 25 percent were allocated to the productive sector which comprises agriculture, manufacturing tourism and mining. Within the productive sector, US\$32.1 million or 16.3 percent of the total was allocated to the manufacturing sector, while tourism accounted for 5.9 percent (US\$11.6).

Economic infrastructure accounted for US\$112.5 million or 57.0 percent of approved funds. Of these funds US\$52.1 million (26.4 percent) were allocated to the transportation, US\$54.9 million (27.8 percent) to the education, and US\$3.2 million (1.6 percent) to the health sectors.

In 2001, two loans were approved to the government of Barbados. The first was a US\$5.1 (Additional loan) for the Urban Rehabilitation project which was originally approved in the year 2000 at an initial amount of US\$25.23 million). The loan increase represented a revision in the scope in the project to allow for additional rehabilitation in Bridgetown. The second loan of US\$4 million was also an increase of an existing loan (the Secondary Education Project) which was originally approved in 1995 for US\$12.2 million. In July, 2002, CDB approved a US\$15 million loan to the Government of Barbados to be on lent via the Industrial Credit Fund at the Central Bank. The loan seeks to stimulate output in the export oriented sectors of the Barbados economy in light of the country's recent economic performance.

CDB Loans Approved to Barbados 1970–2002

Sector	US\$ million	Percent
Productive sector	49.6	25.1
Agriculture	5.8	2.9
Manufacturing	32.1	16.3
Tourism	11.6	5.9
Economic infrastructure	112.5	57.0
Power and energy	0.0	0.0
Water	0.8	0.4
Transportation	52.2	26.5
Housing	1.4	0.7
Education	54.9	27.8
Health	3.2	1.6
Multisector	35.2	17.8
Total	197.3	100.0

Source: Caribbean Development Bank.

Barbados—Outstanding Statistical Issues

Barbados participates in the General Data Dissemination System (GDDS). Information about Barbados macroeconomic statistics (metadata) and the authorities' plans for improving the statistical base are posted on the Internet on the Fund's Dissemination Standards Bulletin Board.

There is a significant debt recording initiative currently underway to centralize the debt data being compiled by the Central Bank of Barbados (CBB) and the Accountant General's Office using the Commonwealth Secretariat's Data Recording and Management System (CS-DRMS 2000+). The new system is expected to be fully implemented by the end of 2002, and is designed to provide instantaneous access to integrated debt statistics for all users. The CBB, the Accountant General's Office, and the Ministry of Finance will share joint responsibility for updating the system. In particular, the CBB's Exchange Control Department will continue to update the private sector debt (government-guaranteed and non-guaranteed), the CBB's Research Department would update the guaranteed debt of statutory bodies and have access to the new CS-DRMS system for analytical purposes; and the CBB's Banking and Currency Department would update exchange rate information on a daily basis. The Ministry of Finance would update information on government loans (including disbursements) on a monthly basis.

1. Real sector

Compilation of the national accounts by economic sector is hampered by lack of reliable and current data on nonsugar agriculture, private construction and nontourism service activities. The national accounts by expenditure suffer from weaknesses in the external trade and private investment data. Figures for gross domestic product at constant prices are based on 1974 price weights, but the authorities are in the process of updating the weights to 1994. Quarterly GDP estimates are no longer provided.

2. Nonfinancial public sector

Fairly comprehensive and up-to-date data (above the line) are available for the general government, but there is a lag in the reporting of transfers. As a result of net errors and omissions in the recording of financial transactions, a significant discrepancy exists between the overall balance and financing data. Data on public enterprises are not systematically and promptly reported to the Ministry of Finance. Also, financial sector data on public sector net domestic borrowing usually cannot fully be reconciled with above the line fiscal data, partly because of limited availability of the nonbank financial sector information. Data supplied by the public enterprises, such as on government transfers and capital spending, often differ from those provided by the Ministry of Finance.

Data are reported for publication in the *IFS* (with a significant lag), but no data are reported for publication in the *GFS Yearbook*.

3. **Financial sector**

Important weaknesses remain with respect to the overall quality, coverage, and timeliness of the monetary accounts. The concept of residency applied to the monetary statistics is not consistent with the fifth edition of the *Balance of Payments Manual*. The Central Bank of Barbados (CBB) classifies some loans to and deposits of nonresidents as credit to the private sector and part of broad money, respectively, instead of as net foreign assets of commercial banks. Moreover, non-national individuals are recognized as residents only after they have resided continuously in Barbados for at least three years. There is also a need to extend the coverage of data to include offshore bank accounts. Recently, the timeliness of data reported to STA for publication in IFS greatly improved. The lag in submitting monetary data decreased from about five months to about three weeks for the central bank accounts, and about six weeks for the monetary survey. Accounting conventions underlying monetary data compiled by the CBB are in need of improvement. The CBB data are reported on a cash basis and do not include accrued receivables and payables. Commercial banks' positions are recorded on an accrual basis; however, the accrued interest receivable and payable is classified under other assets and other liabilities, respectively, rather than under the appropriate category of domestic credit. Marketable securities are recorded at the acquisition cost and revalued to market value only on an annual basis (as of December 31). Short-term zero-coupon securities (treasury bills) are recorded at acquisition cost and are not revalued to market value until redemption at maturity. Positions with the IMF (SDR holdings, Reserve Tranche Position, and SDR Allocation) are valued at the IMF holdings rate rather than at the end-of-period market rate. These issues are being addressed in the context of the general framework of the GDDS.

4. **External sector**

Lags in the compilation of merchandise trade data limit the timeliness of estimating the external current account balance. Estimates of the components of the investment account need to be strengthened. A recent mission by the IMF Multisector Statistics Advisor at the Caribbean Regional Technical Assistance Centre in March 2002 noted that the coverage of foreign direct investment (FDI) is incomplete because information on offshore enterprise activities is not available from the existing surveys. Also, the surveys on FDI are deficient as the distinction between transactions and positions is unclear in the survey reporting form. Quarterly balance of payments estimates are no longer provided.

Barbados: Core Statistical Indicators
(As of November 30, 2002)

	Exchange Rates	International Reserves	Central Bank Balance Sheet	Reserve/ Base Money	Broad Money	Interest Rates	Retail Price Index	Exports/ Imports	Current Account Balance	Overall Government Balance	GDP/ GNP	External Debt/ Debt Service
Date of Latest Observation	Fixed	08/30/02	10/31/02	10/31/02	09/30/02	09/30/02	07/31/02	09/30/02	12/01	03/31/02	2001	06/30/02
Date Received		11/30/02	11/14/02	11/14/02	11/14/02	11/14/02	11/30/02	11/30/02	7/03/02	10/7/02	7/03/02	10/7/02
Frequency of Data 2/		M	M	M	M	M	M	M	Q	M	Y	M
Frequency of Reporting 2/		M	M	M	M	M	M	M	Q	M	Y	M
Source of Update 3/		A	A	A	A	A	A	A	A	A	A	A
Mode of Reporting		Monthly Publication	Monthly Publication	Monthly Publication	Monthly Publication	Monthly Publication	Monthly Publication	Annual Publication	Central Bank Internal Document	Monthly Publication	Annual Publication	Annual Publication
Confidentiality 4/		U	U	U	U	U	U	U	U	U	U	U
Frequency of Publication 2/		W	M	M	M	M	M	M	Q	M	A	M

- 1/ Preliminary estimate. Actual data provided with a lag of two to three months.
2/ W - weekly, M - monthly, Q - quarterly, Y - yearly.
3/ A - direct, reporting by central bank, ministry of finance, or other official agency.
4/ U - for unrestricted use.

Statement by the IMF Staff Representative on Barbados
February 7, 2003

Since the staff report was circulated to Executive Directors on December 23, 2002, the following information has become available; it does not change the thrust of the staff appraisal:

- Real GDP is now estimated to have decreased by 0.6 percent in 2002, reflecting a rebound in tourist arrivals in the last quarter.
- The overall deficit of the central government was 5.2 percent of annual GDP for the first three quarters of FY2002/03 (last three quarters of 2002), owing partly to higher than expected government spending for hurricane relief for households and tourism promotion. The deficit for the fiscal year could exceed 6 percent of GDP.
- The external current deficit is estimated to have widened to 4.9 percent of GDP in 2002 from 3.7 percent of GDP in 2001, owing in part to higher imports of capital goods. This exceeds the estimated deficit presented in the staff report.
- Net international reserves declined by US\$41.5 million to US\$665.5 million (the equivalent of 5.5 months of imports of goods and services); below the projection of 5.8 months presented in the staff report.



INTERNATIONAL MONETARY FUND

Public Information Notice

EXTERNAL
RELATIONS
DEPARTMENT

Public Information Notice (PIN) No. 03/16
FOR IMMEDIATE RELEASE
February 21, 2003

International Monetary Fund
700 19th Street, NW
Washington, D. C. 20431 USA

IMF Concludes 2002 Article IV Consultation with Barbados

On February 7, 2003 the Executive Board of the International Monetary Fund (IMF) concluded the Article IV consultation with Barbados.¹

Background

Fiscal policies implemented during 1993–2000, as well as structural reforms that further shifted Barbados' productive base from agriculture into tourism and offshore services, helped promote strong growth of service exports in the context of its fixed exchange peg since 1975 of BD\$2 to US\$1. Real GDP growth averaged 3 percent annually and inflation 2 percent, as the unemployment rate declined from 24½ percent to 9¼ percent.

Eight consecutive years of growth ended in 2001 as real GDP contracted by 2¾ percent, owing mainly to the adverse impact on tourism of the global economic slowdown and the September 11 terrorist attack, as well as continuing declines in agriculture and manufacturing output (Table 1). To lessen the impact of the September 11 attack, the authorities implemented a national emergency program in the fourth quarter of 2001, comprised mainly of fiscal stimulus measures that included: shifting spending to promote the tourism, manufacturing, and agricultural sectors; reintroducing import licenses for selected agricultural products to protect domestic production; and accelerating implementation of public investment projects.

The 12-month increase in consumer prices, which averaged less than ¼ percent over 1998–99, rose to 2½ percent in 2001, reflecting in part an increase in tariff rates on agricultural and manufactured imports implemented in November 2001. The real effective exchange rate depreciated by 9 percent in the 12 months to end-October 2002, largely reflecting depreciation of the U.S. dollar against the euro. The unemployment rate rose to 10¼ percent by end-March 2002.

¹ Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board. At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities.

Due to public sector wage increases in the face of the sharp recession, the fiscal stimulus and emergency measures implemented by government to reduce its depth, and deterioration in the finances of public enterprises, including significant losses in the public hotel enterprise, the overall deficit of the nonfinancial public sector widened substantially from $\frac{3}{4}$ percent of GDP in FY2000/01 to $3\frac{3}{4}$ percent of GDP in FY2001/02 (fiscal year is April–March). The central government deficit rose sharply from 2 percent of GDP in FY2000/01 to $4\frac{1}{4}$ percent of GDP in FY2001/02.

Broad money grew by $5\frac{1}{2}$ percent in 2001, reflecting capital inflows and an increase in international reserves. The central bank continued to ease credit conditions,² but credit to the private sector stagnated. Broad money is projected to rise $5\frac{1}{2}$ percent in 2002, with private credit sluggish and the level of official international reserves remaining unchanged. Nonperforming loans increased to 5 percent of total loans in 2001, with about half fully provisioned. The offshore sector contracted in 2001 owing mainly to Barbados' inclusion in the OECD's list of noncooperative tax havens, recovered somewhat in 2002 after its removal from the list early in the year, and slipped again as tax haven issues reemerged in bilateral tax treaty negotiations.

The external current account deficit declined from $5\frac{1}{2}$ percent of GDP in 2000 to $3\frac{3}{4}$ percent of GDP in 2001. This outcome stemmed from a contraction in imports in the wake of the decline in tourism and national income that was only partly offset by increased government spending. Net capital inflows more than covered the external current account deficit in 2001 as the government issued US\$150 million in 20-year bonds in the international capital market at an annual interest rate of $7\frac{1}{4}$ percent, 230 basis points above the 30-year U.S. treasury bond rate. As a result, the outstanding stock of public external debt rose from $21\frac{1}{4}$ percent of GDP at end-2000 to $27\frac{1}{2}$ percent of GDP at end-2001. At end-2001 the central bank's net international reserves exceeded US\$700 million—equivalent to over 6 months of projected imports of goods and nonfactor services in 2002.

Executive Board Assessment

Directors observed that Barbados' economic performance has weakened since 2001, reflecting adverse external events and continuing declines in agricultural and manufacturing output. Expansionary fiscal policies, including large public sector wage increases and deterioration in the finances of public enterprises have led to rising fiscal deficits and public debt. Directors stressed that restoration of sustained economic growth will depend on the implementation of strong fiscal measures and perseverance with structural reforms.

Directors therefore welcomed the progress made by the Barbadian authorities in implementing a medium-term program of fiscal tightening and structural reform since October 2002. They considered the authorities' fiscal consolidation efforts to be a critical step toward reducing the public debt ratio relative to GDP and preserving the fixed exchange rate, while providing the savings needed for critical public investment and a return to steady economic growth and lower

² The cash reserve requirement was reduced from 6 percent of deposit liabilities to 5 percent, the government securities requirement from 19 percent to 18 percent, the central bank's discount rate from 10 percent to $7\frac{1}{2}$ percent, the minimum savings deposit rate from $4\frac{1}{2}$ percent to 3 percent, and the maximum lending rate from 10 percent to 8 percent.

unemployment. They welcomed the authorities' plans to reduce discretionary spending, cut government employment through attrition, and undertake other measures to move the public sector budget toward overall balance. They also commended the authorities for the farsighted changes made to the public pension system to ensure actuarial balance.

Nevertheless, Directors cautioned that stronger fiscal measures than those envisaged may be needed to achieve the medium-term objectives. They emphasized, in particular, the need for wage restraint in the public sector—especially in view of the lead role the public sector plays in wage-setting in Barbados; fuel price reform to permit full passthrough of international oil price movements to domestic fuel prices; and reductions in government spending on tourism projects that can be undertaken by the private sector. Directors agreed that new commercial external borrowing should be aimed solely at lowering costs and lengthening maturity.

Directors supported the authorities' plans for comprehensive tax reform over the medium term to lower direct and import tax rates and increase the budget's reliance on the value-added tax and other domestic indirect taxes. They commended the authorities for eliminating tariff protection for some agricultural and manufactured products and import licenses for agricultural products. However, the increase in some tariff rates was considered a continuation of selective protection policies, that is not consistent with the objective of making industries more efficient.

Directors shared the authorities' concerns about the unsustainable operating deficits of some public enterprises. They encouraged privatization to engender efficiency gains and to generate revenue to reduce the public debt, suggesting that the authorities involve the private sector in the provision of services outside the government's core areas.

While acknowledging that the fixed exchange rate has served Barbados well, Directors noted that Barbados' external competitiveness has declined in recent years due to appreciation of the U.S. dollar, wage increases in excess of productivity increases, and foreign trade distortions. They therefore welcomed the agreement reached in May 2002 among labor, business, and government on prices and incomes as reflecting a common understanding of the need to link wage increases to productivity gains, inflation, and personal income tax cuts. However, it was stressed that the tradeoff between wage increases and tax cuts will need to be strictly enforced, since tax cuts in the absence of sufficient wage restraint will continue to impart fiscal stimulus.

Directors commended the authorities for successful participation in the Financial Sector Assessment Program (FSAP). They agreed that the adoption of a more flexible and market-oriented monetary policy framework would lead to more effective liquidity management. They considered the planned elimination of the maximum lending rate by March 2003 and the elimination of the tax on bank assets to be important steps toward financial sector liberalization, and urged further deregulation of interest rates along with complementary capital market liberalization in a regional context. It was also recommended that the Financial Institutions Act be amended to strengthen central bank independence.

Directors noted that the banking system is resilient and fundamentally sound. Nevertheless, they stressed that close surveillance over the banking system should remain a priority. They also emphasized the importance of strengthening the supervision of non-banks and improving the regulatory framework for offshore financial institutions. Directors commended the authorities for their efforts to develop an effective regime for combating money laundering and the financing of terrorism.

Directors encouraged the authorities to continue to use the General Dissemination Data System (GDDS) framework to improve statistical reporting, especially regarding the finances of public enterprises, the consolidated public sector account, the operations of offshore banks, and the external debt.

Public Information Notices (PINs) are issued, (i) at the request of a member country, following the conclusion of the Article IV consultation for countries seeking to make known the views of the IMF to the public. This action is intended to strengthen IMF surveillance over the economic policies of member countries by increasing the transparency of the IMF's assessment of these policies; and (ii) following policy discussions in the Executive Board at the decision of the Board.

Barbados: Selected Economic Indicators

	1998	1999	2000	2001	Proj. 2002
(Annual percentage changes)					
Output and prices					
Real GDP	4.2	2.9	3.0	-2.7	-1.8
Consumer prices (12-month increase)	-1.3	1.6	2.4	2.8	2.0
Tourist arrivals	8.5	0.4	5.8	-6.9	-4.0
Unemployment (percent of labor force)	12.3	10.4	9.2	9.9	10.5
Money and credit					
Net domestic assets 1/	16.0	7.8	-4.3	-8.6	5.2
Public sector credit (net) 1/	-0.7	-0.3	-4.4	-8.5	5.1
Private sector credit	12.7	11.6	2.1	-0.3	-0.4
Broad money	11.5	11.6	7.9	5.6	5.5
(In percent of GDP)					
Public sector operations 2/					
Public sector balance	-0.2	-0.7	-0.7	-3.8	-5.1
Central government	0.1	-0.7	-0.7	-2.7	-4.3
National Insurance Scheme	1.1	1.2	1.5	1.6	1.7
Public enterprises	-1.4	-1.3	-1.6	-2.7	-2.5
Savings and investment					
Gross domestic investment	18.6	19.8	17.2	17.4	17.4
Gross national saving	16.2	13.7	11.6	13.7	13.9
External sector					
External current account balance	-2.4	-6.0	-5.6	-3.7	-3.4
Public external debt 3/	15.6	17.2	21.2	27.5	29.4
Gross official reserves (in months of imports) 4/	2.3	2.5	4.0	6.0	5.8

Sources: Barbadian authorities; and IMF staff estimates and projections

1/ In relation to broad money at the beginning of the period.

2/ Fiscal years (April–March).

3/ Refers to central government and government guaranteed debt.

4/ Imports of goods and services in the following year.

Statement by Ian E. Bennett, Executive Director for Barbados
February 7, 2003

Overview

1. My Barbadian authorities wish to express their appreciation for the helpful advice provided by staff during the Article IV consultation. They are strongly committed to returning the economy to a sustainable growth path and they welcome staff's affirmation of the appropriateness of the direction of their policies towards this end.

2. The year 2001 was difficult for the small island economies of the Caribbean, including Barbados for which, after a long period of uninterrupted growth, real GDP contracted by 2.7 percent, largely as a result of the global economic slowdown and the events of September 11. The government responded decisively to this downturn by implementing a National Emergency Economic and Financial Programme (NEEP) in collaboration with the social partners. This included targeted support to the main productive sectors and implementation of other counter-cyclical expenditure measures, aimed at sustaining economic activity. More recently, with positive signs of reviving activity, the authorities are adjusting their economic policy stance with a view to fiscal consolidation and long-term debt sustainability.

Recent Economic Developments

3. During the first half of 2002, real GDP continued to decline against the background of sluggish external demand. Not surprisingly, unemployment rose further but inflation moderated. With the poor performance of the foreign exchange earning sectors, the external current account deficit widened somewhat. Nevertheless, foreign reserves remained high at over six months of import cover because of an early move at the beginning of the recession by government to raise a substantial loan on the international capital market in an effort to safeguard the country's reserve position. The economy has shown signs of recovery as evidenced by the increase in tourist arrivals between July and October, largely as a result of the marketing and promotion efforts. Real GDP for 2002, which had been expected to decline by 1.8 percent at the time of the Article IV consultation, is now likely to be about the same level as a year ago given the strengthening of the economy over the last six months.

Fiscal and Structural Policies

4. Traditionally, the authorities have maintained small and manageable fiscal deficits. The deficits in 1998, 1999, and 2000 have averaged less than one percent with significant primary surpluses. Over the recessionary period, however, the authorities engaged in counter-cyclical fiscal policy to help offset the severity of the recession facing the country. These measures supported domestic demand, and this contributed to a deterioration of the overall balance of the central government. In particular, capital expenditure was expanded with a focus on several major projects in education, road rehabilitation, and sewerage management. Commensurately, national debt rose but government's precautionary borrowing accounted for a large portion of this increase.

5. The authorities recognize the limit to which they can engage in fiscal expansion if they are to keep the level of public debt under control and maintain the fixed exchange rate regime that has served the economy so well for almost thirty years. Consequently, now that growth prospects are improving, they are resolved to consolidate the public finances. In this regard, emphasis is being placed on controlling expenditure growth by reducing discretionary spending and limiting public capital investment to growth-promoting projects which are externally funded. Halting the construction of the new Hilton Hotel project, as advised by staff, would be counter-productive as this project is an important source of foreign investment, and it is heavily foreign-funded. Additionally, once completed it will add significantly to the country's hotel room capacity at the higher end of the market and is, therefore, critical to the continued growth of the tourism sector.

6. Ongoing tax reforms aimed at reducing the direct tax burden, strengthening tax administration, and achieving greater convergence of the tax rates are to be accelerated to further stimulate economic activity. A crucial part of this reform is a phased program of reductions in corporate and personal taxes over the next four years, with a view to sharpening incentives and encouraging business activities. In consultation with the social partners, the authorities intend to link personal tax reliefs to moderation in wage growth so as to improve the competitiveness of the economy. A comprehensive reform of the public pension system is also ongoing with the aim of achieving actuarial balance in the medium to long term.

7. Moreover, longer-term fiscal viability will be underpinned by a restructuring of public enterprises also critical to the government's economic strategy. A fair trading commission has been established to determine appropriate charges for water and public transportation. Plans are being developed to require state enterprises to prepare programs for cost containment and improvements in the quality and delivery of services, and to accept new benchmarks for operational efficiency. The government is considering the sale of its interest in a commercial bank (Barbados National Bank) and an insurance company (Insurance Corporation of Barbados). As previous attempts to sell government shares in these entities were not successful, strategic partners are being sought so as to enhance their attractiveness to potential investors – this is a process which is already fairly advanced. Similarly, the government intends to dispose of its ownership of hotels (GEMs of Barbados) at the earliest possible opportunity.

Monetary Policy

8. The objectives of monetary policy are to safeguard the fixed exchange rate and facilitate an interest-rate regime which is conducive to economic growth, particularly in the foreign exchange earning sectors. The oligopolistic nature of the banking system remained a challenge to the authorities' efforts to lower the cost of borrowing, mostly to the productive sectors, and thereby stimulate economic activity. The introduction of an indicative or maximum lending rate was, therefore, intended to encourage the banking sector to lower interest rates and followed several other signals, including continual reductions in the minimum deposit rate set by the Central Bank, which were largely ignored by the banks. This is a temporary measure and will be removed on March 31, 2003.

9. The authorities are, however, conscious of the need to improve the efficiency of financial intermediation and are phasing out the tax on bank assets and introducing a deposit insurance plan. The minimum deposit rate will nevertheless remain in place, as its use is deemed necessary by the authorities to counteract the lack of competition in the banking system.

10. The authorities concur with staff on the desirability of capital account liberalization and they are moving towards that objective. Capital controls are to be partially liberalized in the context of the ongoing negotiations under the CARICOM Single Market and Economy (CSME). However, some restrictions will remain to prevent disruptions arising from short-term speculative flows.

Financial Sector Assessment Program (FSAP)

11. My authorities very much appreciate and welcome the recent FSAP report on Barbados which confirmed the soundness of the financial system. Indeed, the conclusion that the observance of international supervisory standards was high for both onshore and offshore sectors is an endorsement of the authorities' commitment to best practices in the provision of financial services. They continue to work to further enhance the functioning of the financial system through measures to improve prudential regulation and supervision, such as allowing on-site inspection of offshore banks, the creation by the Central Bank of an inspection unit for credit unions and deposit insurance schemes, and the establishment of a Financial Intelligence Unit to counter money laundering and the financing of terrorism.

Trade Policy

12. The authorities, while recognizing the importance of opening up their economies, took a deliberate step to slow the process during the recession, to avoid exacerbating the economic difficulties facing the country. Nevertheless, the authorities remain committed to trade reforms and propose to continue to liberalize trade and, with effect from January 2003, further reduce duties on selected items. However, they propose to retain special safeguards permitted by the WTO to protect the agro-processing and beverage industries from surges in low-priced imports from outside the region. In relation to agriculture, the revitalization and diversification of this sector is a priority of the authorities, whose focus is on providing income transfers and special incentives as opposed to higher tariffs.

The Road Ahead

13. It appears that the Barbadian economy will revert to a positive growth path but its prospects hinge largely on a resurgence in global tourism demand. The authorities are resolved to support this recovery through appropriate fiscal, monetary, and structural policies. However, given the economy's small size and openness, they realize that sustained growth in the future will depend critically on developments in the world economy. A less optimistic scenario is likely if a US-led war against Iraq materializes and undermines tourism activity in particular. However, the Barbadian economy appears to be emerging from recession.