

Growth and Indebtedness in the Eastern Caribbean: Recovering from the Global Crisis

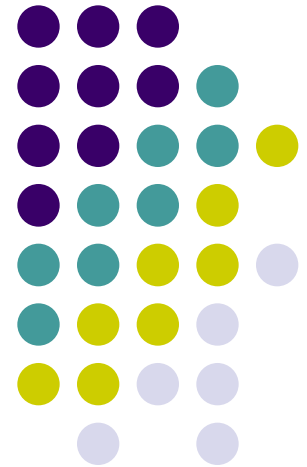
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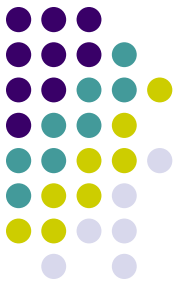
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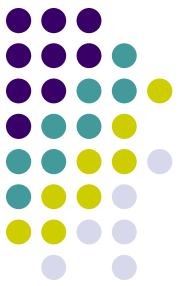
January 27th and 28th 2011.





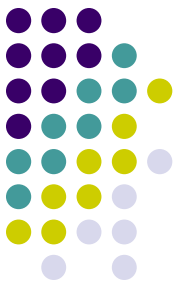
Introduction

- Paper covers Barbados plus the eight OECS states;
- All countries hard hit by world financial crisis and recession;
- Debt-to-GDP ratios above 100% for four countries, well above the ECCB's preferred 60% ratio in three others;
- Hence need to manage debt while recovering from recession;
- Outline:
 - Crisis, recession and debt;
 - Debt and growth;
 - Models of growth;
 - Conclusions



Crisis, Recession and Debt

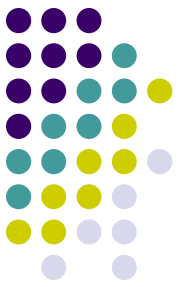
- Small countries, affected by world recession but not causing it;
- IMF reports that many countries got through the world crisis with no falls in GDP – but not so for the Eastern Caribbean;
- Why so vulnerable?
 - Small size, vulnerable to natural disasters, narrow production and export range, depend on volatile income and capital flows, trade conditions getting less favourable.
- Given all this, surprising done so well!



Crisis and Recession

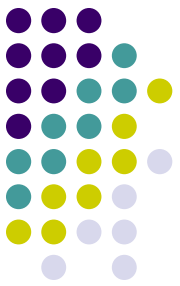
- Advanced country financial crisis – no immediate impact on Caribbean;
- Then recession hit tourism and demand for exports;
- Also cut FDI and remittances.
- Recovery going ahead, but slowly, in the advanced countries, much more dynamic in emerging markets;
- Gradual/delayed recovery likely in Caribbean

Debt



- Debt-to-GDP ratio above 90% slows down growth;
- No clear view on ‘optimal’ ratio, though ECCB favours 60% as a ‘normal’ upper limit;
- How to get debt ratio down?
- Economic growth;
 - Inflation – not advisable in Caribbean, depends on currency of debt;
 - Fiscal discipline, large primary surpluses;
 - Default – rather drastic, not generally recommended, but not always as bad as people expect it to be.

Managing indebtedness

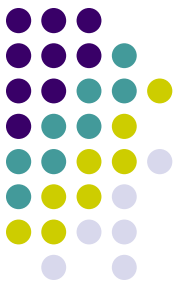


- IMF DSA approach – technically good, needs lots of data, not very quick and easy to apply.
- Our approach, a **simple debt tool** that needs little data and is very quick to apply. Details in paper, here we give numerical examples for three strategies for each country.
- **Strategy 1**. Existing policies as announced in most recent Budget Address, with the average rate on outstanding debt assumed to be 6% ($r = 0.06$) and the economic growth rate as currently projected.
- **Strategy 2**. Same as 1, except that the economy resumes faster economic growth at 5% per annum ($g = 0.05$).
- **Strategy 3**. Same as 2, but with debt restructured so that the average interest rate comes down to 4% ($r = 0.04$), and with the primary surplus of 10% of GDP ($p = 0.1$).

Table 5. Debt analysis of Barbados and OECS economies using new debt tool



Country/Item	Strategy	z_+	z	g	r	p
Barbados	1	1.03	1.05	0.02	0.06	0.06
	2	1.00	1.05	0.05	0.06	0.06
	3	0.94	1.05	0.05	0.04	0.1
OECS Countries						
Anguilla	1	0.84	0.64	0.02	0.06	-0.18
	2	0.82	0.64	0.05	0.06	-0.18
	3	0.54	0.64	0.05	0.04	0.1
Antigua and Barbuda	1	1.19	1.18	0.03	0.06	0.02
	2	1.17	1.18	0.05	0.06	0.02
	3	1.07	1.18	0.05	0.04	0.1
Dominica	1	0.86	0.85	0.02	0.06	0.02
	2	0.84	0.85	0.05	0.06	0.02
	3	0.75	0.85	0.05	0.04	0.1
Grenada	1	1.32	1.22	0.02	0.06	-0.05
	2	1.28	1.22	0.05	0.06	-0.05
	3	1.11	1.22	0.05	0.04	0.1
Montserrat	1	0.15	0.1*	0.02	0.06	-0.05
	2	0.15	0.1*	0.05	0.06	-0.05
	3	0.00	0.1*	0.05	0.04	0.1
St Kitts and Nevis	1	1.88	1.85	0.01	0.06	0.06
	2	1.81	1.85	0.05	0.06	0.06
	3	1.74	1.85	0.05	0.04	0.1
St Lucia	1	0.79	0.75	0.03	0.06	-0.02?
	2	0.78	0.75	0.05	0.06	-0.02?
	3	0.65	0.75	0.05	0.04	0.1
St Vincent and the Grenadines	1	0.79	0.75	0.01	0.06	0
	2	0.76	0.75	0.05	0.06	0
	3	0.65	0.75	0.05	0.04	0.1



Growth models

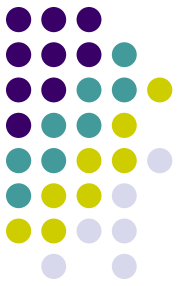
- Investment
 - Some implausibly high investment ratios reported in the region.
- Productivity growth
- Institutional improvements
 - Improving the business and investment climate
 - Need to get investors interested again.
- Sources of demand
 - Scope for export expansion?
 - What about a new form of import substitution?



Conclusions

- Debt situation serious in several countries, needs tough fiscal policy;
- Growth will help to reduce debt burden while also raising living standards;
- Need to re-think approaches to growth, incl. moving away from traditional products;
- No rent seeking, no ‘picking winners’, but need good environment for new businesses;
- Ideas in paper applicable more widely across the Caribbean.

Thank you!



- Time for questions and discussion