

## **Barbados: 2005 Article IV Consultation—Staff Report; and Public Information Notice on the Executive Board Discussion**

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 2005 Article IV consultation with Barbados, the following documents have been released and are included in this package:

- the staff report for the 2005 Article IV consultation, prepared by a staff team of the IMF, following discussions that ended on May 10, 2005, 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 July 19, 2005. 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 Public Information Notice (PIN) summarizing the views of the Executive Board as expressed during its August 5, 2005 discussion of the staff report that concluded the Article IV consultation.

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# INTERNATIONAL MONETARY FUND

## BARBADOS

### Staff Report for the 2005 Article IV Consultation

Prepared by the Staff Representatives for the 2005 Consultation with Barbados

Approved by Ratna Sahay and Matthew Fisher

July 19, 2005

- **Discussions:** A staff team comprising B. Clements (Head), G. Bindley-Taylor, C. Francis, and W.A. Samuel (all WHD), and L. Valderrama (ICM) held discussions in Bridgetown during April 26–May 10, 2005. The mission met with Senator Tyrone Barker, Parliamentary Secretary for Finance and Economic Affairs; Mr. Grantley Smith, Director General of the Ministry of Finance and Economic Affairs; Ms. Marion Williams, Governor of the Central Bank of Barbados; other senior officials; and representatives of the private sector. R. Sahay (WHD) and R. Campbell (OED) joined the mission for the final meetings.
- **Economic and social background:** Barbados compares favorably with other regional economies on economic and social indicators. The population is about 272,000, and per capita income (PPP) is about US\$15,700. Social indicators are among the best in the Caribbean region and compare favorably in a global context; in 2004, for example, Barbados was ranked 29<sup>th</sup> among 177 countries on the United Nations Development Program’s Human Development Index. Barbados is also one of only six countries in Latin America and the Caribbean with an investment grade rating for its sovereign debt.
- **Political situation:** The ruling political party enjoys a comfortable majority in the parliament and the next elections are due by September 2008. The Barbados Labor Party (BLP), led by Prime Minister Owen Arthur, won its third consecutive election in May 2003, securing 23 of the 30 seats in the House of Assembly. The main opposition party, the Democratic Labor Party (DLP), held office during 1986–94, and controls the remaining seven seats.
- **Last Article IV consultation:** At its conclusion on April 7, 2004, Directors supported the authorities’ plan for a gradual return to low fiscal deficits and continued implementation of structural reforms to enhance economic growth and competitiveness. They emphasized the need to align utility tariffs with operating costs and to reduce the level of transfers to loss-making public enterprises. Directors recommended the acceleration of efforts to adopt market based monetary policy tools, as well as the phasing out of the minimum deposit rate to improve the efficiency of financial intermediation.
- **Exchange system:** Barbados has accepted the obligations of Article VIII, Sections 2, 3, and 4, and maintains an exchange system free of restrictions on the making of payments and transfers for current international transactions. The Barbados dollar has been pegged to the U.S. dollar at BD\$2=US\$1 since 1975.

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## EXECUTIVE SUMMARY

### Recent developments

- **A strong economic recovery appears to have taken hold in 2004.** Real GDP grew by an estimated 4½ percent in 2004, led by the continued recovery of the tourism sector. The deficit of the nonfinancial public sector narrowed slightly to 6 percent of GDP, but public debt remains high at 86 percent of GDP. The balance of payments deficit widened in 2004, as a rapid expansion in private sector credit generated a surge in imports while private capital inflows declined. The banking system appears to be sound and financial sector indicators have improved with the rebound in economic activity.
- **A modest program of structural reforms was undertaken during the past year.** Tax rates have been reduced, the airport has been corporatized, and the telecommunications sector has been further liberalized.

### Policy discussions

- **The discussions focused on fiscal consolidation to reduce debt, enhancing the scope for utilizing indirect monetary policy instruments, reducing vulnerabilities, and structural policies to raise competitiveness and growth.** Real GDP is projected to grow by about 3 percent in 2005 and remain strong until 2007 because of the stimulus from the buildup to the World Cup cricket games. Maintaining high growth over the medium term, however, will require steps to correct macroeconomic imbalances and an acceleration of structural reforms.
- **Staff argued that the recent buildup of public debt and rapidly declining foreign exchange reserves called for a decisive fiscal adjustment.** Under the mission's active scenario, fiscal adjustment would begin this year, with the deficit declining to less than 1 percent of GDP by the end of the decade. The authorities concurred with the broad thrust of the mission's views, but were concerned that a sharp fiscal adjustment would be incompatible with their desire to continue to provide high-quality public services and maintain a high level of public investment spending to underpin economic growth.
- **The staff and authorities agreed that the fixed exchange rate regime remains appropriate for Barbados,** provided it was accompanied by appropriate macroeconomic and structural policies and wage increases in line with developments in labor productivity.
- **The authorities are moving ahead with structural reforms.** The mission endorsed the government's efforts in this area but urged a more ambitious agenda. It also suggested that the central bank phase out the minimum deposit rate and accelerate the adoption of indirect monetary policy instruments.

## I. BACKGROUND

1. **Barbados compares favorably with other Caribbean countries on economic and social indicators.** The economy is heavily dependent on tourism and financial services, but has been resilient in the face of external shocks. The population is about 272,000, and per capita income (on a PPP basis) is about US\$15,700. Poverty rates are the lowest in the Caribbean. Social indicators compare favorably in both a regional and global context; in 2004, for example, Barbados was ranked 29<sup>th</sup> among 177 countries on the United Nations Development Program’s Human Development Index. Barbados is also one of only six countries in Latin America and the Caribbean with an investment grade rating.

Barbados: Social Indicators of Selected Caribbean Countries

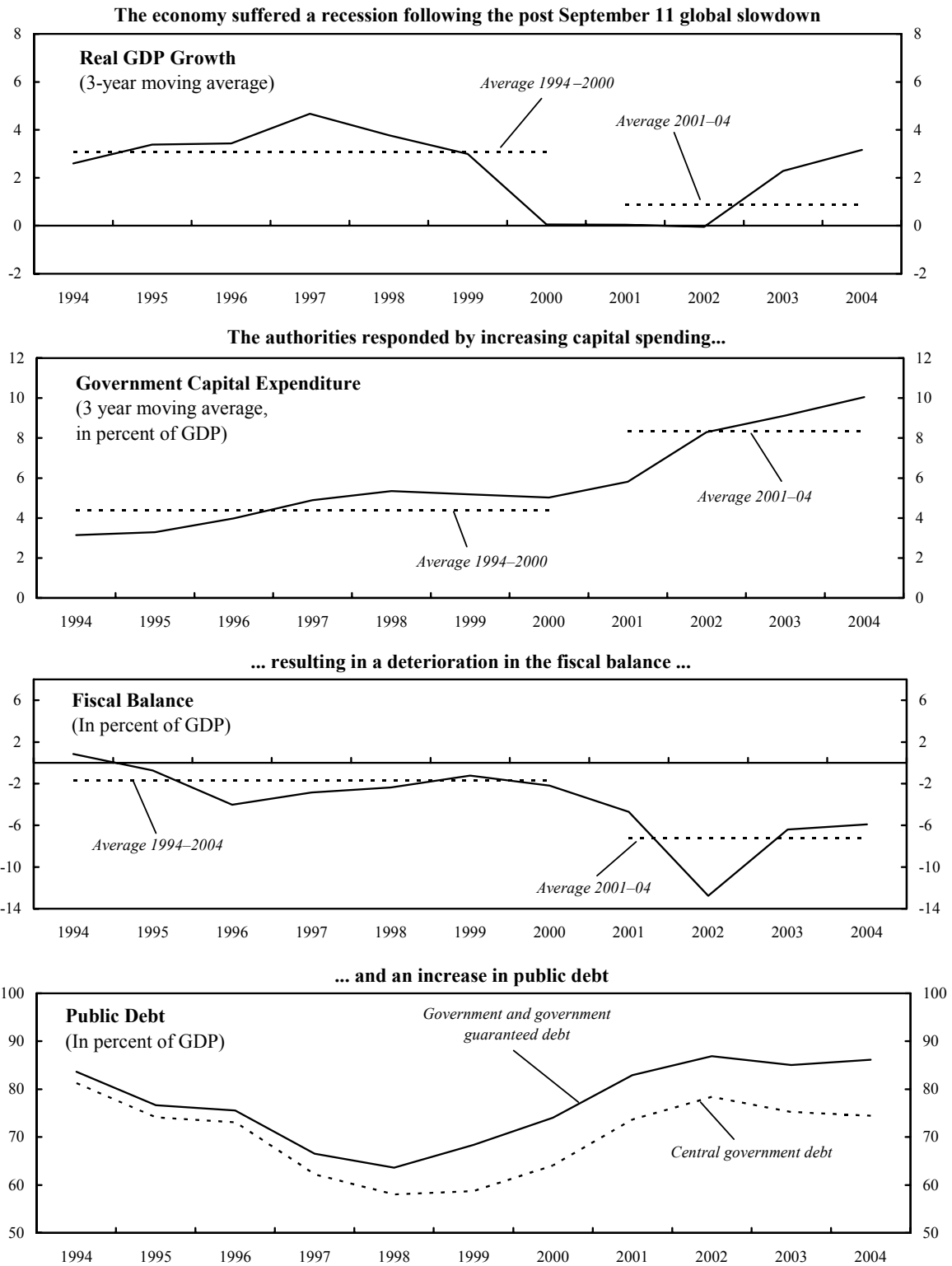
	GDP per Capita, U.S. dollars (PPP) 2003	Poverty Rate, Most Recent Available (In percent)	Human Development Index Ranking, Out of 177 2004	Illiteracy Rate (In percent) 2001
Barbados	<b>15,700</b>	<b>13</b>	<b>29</b>	<b>2</b>
ECCU (average)	5,600	29	39–95	8
Jamaica	3,900	19	79	13
Trinidad and Tobago	9,500	21	54	2

Sources: Country authorities and UNDP.

2. **Barbados was one of the better-performing economies in the Caribbean in the 1990s.** After an IMF-supported adjustment program in the early 1990s, Barbados grew at 3 percent, inflation was less than 2 percent, and public sector deficits were maintained at less than 3 percent of GDP over the 1993–2000 period. These small deficits and conservative monetary policy helped underpin the fixed exchange rate regime.

3. **The solid economic performance of the 1990s has given way to macroeconomic imbalances since 2001.** The economy—especially the tourism and financial services sectors—suffered a sharp recession in 2001–02 following the September 11<sup>th</sup> attacks and the global slowdown (Figure 1 and Table 1). In response to the deterioration in the external environment, the authorities implemented an expansionary public investment program to help revive economic activity. Combined with public sector wage increases, this contributed to a widening of the overall nonfinancial public sector fiscal deficit from about 2 percent of GDP in FY 2000/01 to about 13 percent of GDP in FY 2002/03. As a result, the public sector debt-to-GDP ratio rose from 74 percent in March 2001 to 87 percent in March 2003 (Tables 2 and Table 3). The high fiscal deficit and public debt prompted a downgrade in

Figure 1. Barbados: Selected Macroeconomic Indicators, 1994–2004



Source: Barbadian authorities.



Barbados' external credit rating in August 2004.<sup>1</sup> The external current account deficit remained at around 6 percent of GDP over 2001–03, but international reserves rose, owing to inflows linked to privatization and external borrowing by the central government.

4. **Growth has been hampered by low rates of private investment and the sluggish performance of manufactured and agricultural exports.** Even during the period of relatively good performance in the 1990s, private investment remained low; over 1995–2003, for example, it averaged 13 percent of GDP, compared with 22 percent for CARICOM as a whole.<sup>2</sup> The weak performance of goods exports, coupled with growing imports, has slowed growth and contributed to the weakening of the current account balance over time, with the surpluses of the mid-1990s replaced by deficits averaging over 6 percent of GDP since the end-1990s.

5. **High spreads between deposit and borrowing rates point to inefficient financial sector intermediation that may be curtailing investment.** Interest rate spreads, at over 7 percent, are higher than what could be expected of a country with Barbados' macroeconomic performance and economic characteristics.<sup>3</sup> This reflects certain features of the monetary policy regime, such as a minimum deposit rate and capital controls. This captive environment has, in some instances, generated excess liquidity in the banking system and short-term interest rates on government debt close to or below the minimum deposit rate. These low rates of return on nonloan assets relative to the cost of deposits have, in turn, put upward pressure on lending rates.

6. **The ruling political party enjoys a comfortable majority in the parliament and the next elections are due by September 2008.** The Barbados Labor Party (BLP), led by Prime Minister Owen Arthur, won its third consecutive election in May 2003, securing 23 of the 30 seats in the House of Assembly. The main opposition party, the Democratic Labor Party (DLP), held office during 1986–94, and controls the remaining seven seats.

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<sup>1</sup> In August 2004, Standard and Poors lowered the long-term foreign currency sovereign credit rating to BBB+ from A-, while the long-term domestic currency rating was reduced from A+ to A-.

<sup>2</sup> FDI has also been low in Barbados. See "Foreign Direct Investment in Barbados: Past Performance and Future Prospects," Chapter III in the accompanying *Barbados—Selected Issues*.

<sup>3</sup> See "Financial Intermediation and Monetary Policy," Chapter I in the accompanying *Barbados—Selected Issues* for further discussion.

## II. RECENT ECONOMIC DEVELOPMENTS AND NEAR-TERM PROSPECTS

7. **A strong economic recovery appears to have taken hold in 2004, which is expected to continue in 2005.** Real GDP growth in 2004 is estimated at 4.4 percent, led by a recovery in tourism, construction, and communications (Box 1 compares this recent performance with that in the rest of the region). In 2005, real GDP growth is projected to ease somewhat to 3.1 percent, as tourism activity expands at a more sustainable rate.<sup>4</sup> Growth will be supported by public and private sector investment ahead of the cricket World Cup in 2007, as well as favorable global demand. Inflation has remained low, although administrative steps to pass through higher international oil prices to domestic prices in 2005 are projected to raise inflation above 3 percent for the year.

8. **The fiscal position improved slightly in FY 2004/05 for the nonfinancial public sector as a whole, but is expected to deteriorate in FY 2005/06.**

The mission projects an increase in the deficit of about 1 percentage point of GDP to 7 percent of GDP, owing in part to increases in public investment projects related to the buildup to the World Cup cricket games. As a result, the ratio of primary public expenditures to GDP, which is already high by Caribbean standards, will rise further. At the same time, public debt (comprising central government and government-guaranteed debt for the public enterprises) is projected to rise from 86 percent of GDP in FY 2004/05 to 88 percent of GDP in FY 2005/06, far exceeding the average for Latin America and the Caribbean and for emerging market countries.

9. **Following the rebound in economic activity and a reduction in mortgage lending rates, growth in credit to the private sector—especially to households—accelerated in 2004.** Private sector credit grew by almost 17 percent during 2004, reflecting strong demand for mortgages (Table 4). Higher personal incomes of households also spurred private credit growth.

Barbados: Public Debt in Comparison with Latin American and Caribbean Averages, 2004 1/ (In percent of GDP)

	External	Total
Barbados	23.9	86.1
Latin America and Caribbean	45.8	71.7
Caribbean	52.0	90.9
Central America	52.9	69.9
<b>Memorandum item:</b>		
Emerging markets average 2/	38.4	74.4

Sources: Country authorities and Fund staff estimates.

1/ Figures refer to unweighted averages. Data for Barbados refer to end-year figures for FY 2004/05. Entire sample comprises 24 countries for Latin America and the Caribbean. For the Caribbean, ECCU countries are combined as one observation.

2/ Refers to 2003 data for 25 countries from the IMF Fiscal Affairs Department's emerging markets database. Argentina and Poland are excluded from the external debt data.

<sup>4</sup> For a discussion of the outlook for this sector, see “Tourism—Recent Developments and Prospects,” Chapter II in the accompanying *Barbados—Selected Issues*.

### Box 1. Barbados: Recent Performance in a Regional Perspective

- **Growth performance has been similar to other Caribbean countries.** At about 3 percent in 2003–04, it was slightly better than Jamaica and comparable to the rest of the Eastern Caribbean.
- **The primary budget deficit is the highest in the region.** Public expenditure is also significantly higher, owing to high levels of nonwage expenditure. Rising deficits have contributed to an increase in public debt of over 15 percentage points of GDP since the late 1990s. The debt burden, though rising in recent years, still remains below that of other countries in the region, except for Trinidad and Tobago.
- **As in many other Caribbean economies, external current account deficits are high.** Deficits are lower in Barbados than those in Jamaica and the ECCU territories. FDI, however, is lower in Barbados than in its regional counterparts.

Selected Caribbean Countries—Key Economic Indicators (Averages, 2003–04)<sup>1</sup>

	Barbados	Trinidad and Tobago	Jamaica	ECCU
GDP growth rate	3.2	9.7	2.2	3.3
Inflation	1.5	3.8	11.5	2.2
Unemployment rate	9.0	10.0	12.8	10–15
Central government primary expenditure/GDP	31.4	20.6	18.6	29.7
Public sector primary balance/GDP	-1.3	6.0	9.9	-0.7
Overall public sector balance/GDP	-6.1	2.3	-7.5	-5.2
Public debt/GDP	85.9	50.9	139.6	107.2
<i>Of which: external</i>	27.2	15.2	48.6	64.9
External current account balance/GDP	-8.7	10.0	-12.1	-19.3
Net FDI/GDP	3.8	13.1	5.4	10.8

Sources: Country authorities; World Economic Outlook database; and Fund staff estimates.

1/ All fiscal data, except for the ECCU, are presented on a fiscal year basis. For Barbados and Jamaica, data cover the fiscal year ending March 2005, and for Trinidad and Tobago, the fiscal year ending September 2004. Public sector data for Barbados and Trinidad and Tobago, unlike those for Jamaica, exclude the operations of their respective National Insurance Systems. All other data are presented on a calendar year basis. Data for the primary and overall public sector balances for ECCU countries refer to central government operations.

**10. After a largely accommodative monetary policy stance to support the economic recovery, monetary conditions were tightened in early 2005 to slow the growth of credit.**

Effective June 1, 2005, the minimum deposit rate was raised by 1 percentage point (to 3.75 percent), following a 0.5 percentage point increase on April 1. The authorities have indicated their intention to make further increases over the remainder of the year, as well as other steps to tighten monetary conditions. The central bank projects that private sector credit growth will drop to less than half the pace of 2004. Following the large contraction in base money in 2004 resulting from the decline in commercial banks excess reserves, base money is projected to decline further (Table 5).

	2001	2002	2003	2004
Capital adequacy ratio	18.2	18.8	25.0	17.9
Nonperforming loans/total loans	5.0	7.9	9.3	7.5
Loan loss provisions/total assets	1.2	0.9	1.2	0.9

Source: Central Bank of Barbados.

**11. The banking sector appears to be sound and financial sector indicators have improved with the pickup in economic activity.**

Commercial banks are well capitalized, with adequate levels of provisioning. As in other countries, nonperforming loans have fallen with the rebound in economic growth, albeit with a lag.

Barbados and Other Caribbean Economies: Nonperforming Loans As a Share of Total Loans

	2001	2002	2003	2004
Barbados (end-period)	5.0	7.9	9.3	7.5
ECCU (end-period)	13.1	13.7	13.9	12.0
Guyana (end-period)	38.2	37.2	23.3	18.8
Jamaica 1/	9.6	8.0	4.9	3.9
Trinidad and Tobago (end-period)	3.4	3.8	2.0	...

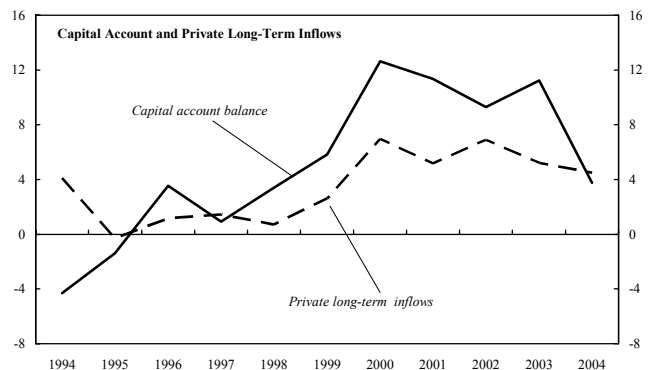
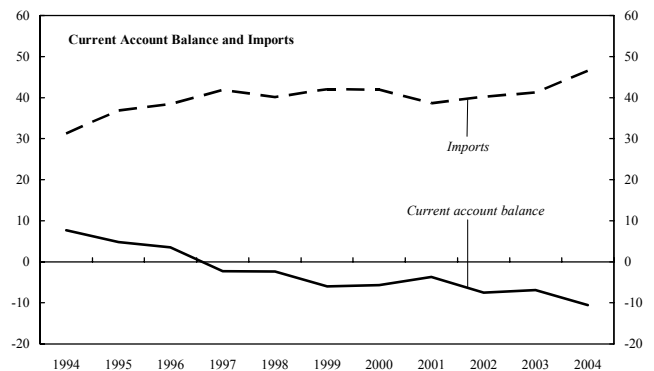
Source: Country authorities.

1/ Fiscal year ending March 31.

**12. The external current account deficit rose sharply in 2004, and is expected to remain high in 2005.**

The external current account deficit increased sharply from 7 percent of GDP in 2003 to 10½ percent of GDP in 2004 (Table 6), reflecting a broad-based import surge related to the rapid increase in private sector credit and the expansion in economic activity. Capital inflows also declined with the cessation of privatization receipts from abroad. As a result, the balance of payments moved from a surplus to a deficit of 5½ percent of GDP in 2004, with gross international reserves (GIR) falling to 3¾ months of imported goods and nonfactor services. Despite the projected slowdown in private sector credit growth and some increase in capital inflows, the external current account deficit will remain high at about 10 percent of GDP in 2005, reflecting the strong growth of imports linked to the preparation for the World Cup cricket games. As a consequence, external reserve coverage is expected to fall further to about three months.

Barbados: Selected External Sector Indicators, 1994 - 2004 (In percent of GDP)



Source: Barbadian authorities.

13. **Structural reforms have advanced in taxation, telecommunications, and the public enterprise sector.** Corporate and personal tax rates have been further lowered, in line with the multiyear reduction in these rates initiated in FY 2002/03. In telecommunications, the final phase of reform began in early 2005, and will involve the liberalization of external telecommunications and the issuance of new licenses for fixed telephone lines on a competitive basis. Legislation to corporatize the Airport Authority was also recently approved, paving the way for more efficient management.

### III. REPORT ON THE DISCUSSIONS

14. **Discussions again focused on the need for fiscal consolidation, enhancing the scope for indirect monetary policy instruments, and structural policies to raise competitiveness and growth.** While in recent Article IV consultation discussions the authorities have agreed with the staff's key recommendations—including for reversing the fiscal stimulus implemented after the 2001–02 recession—policy implementation has reflected a preference for a more gradual approach. More generally, the authorities take the position that their policy direction has been broadly in line with past Fund advice and that consultations have tended to result in a convergence of views.

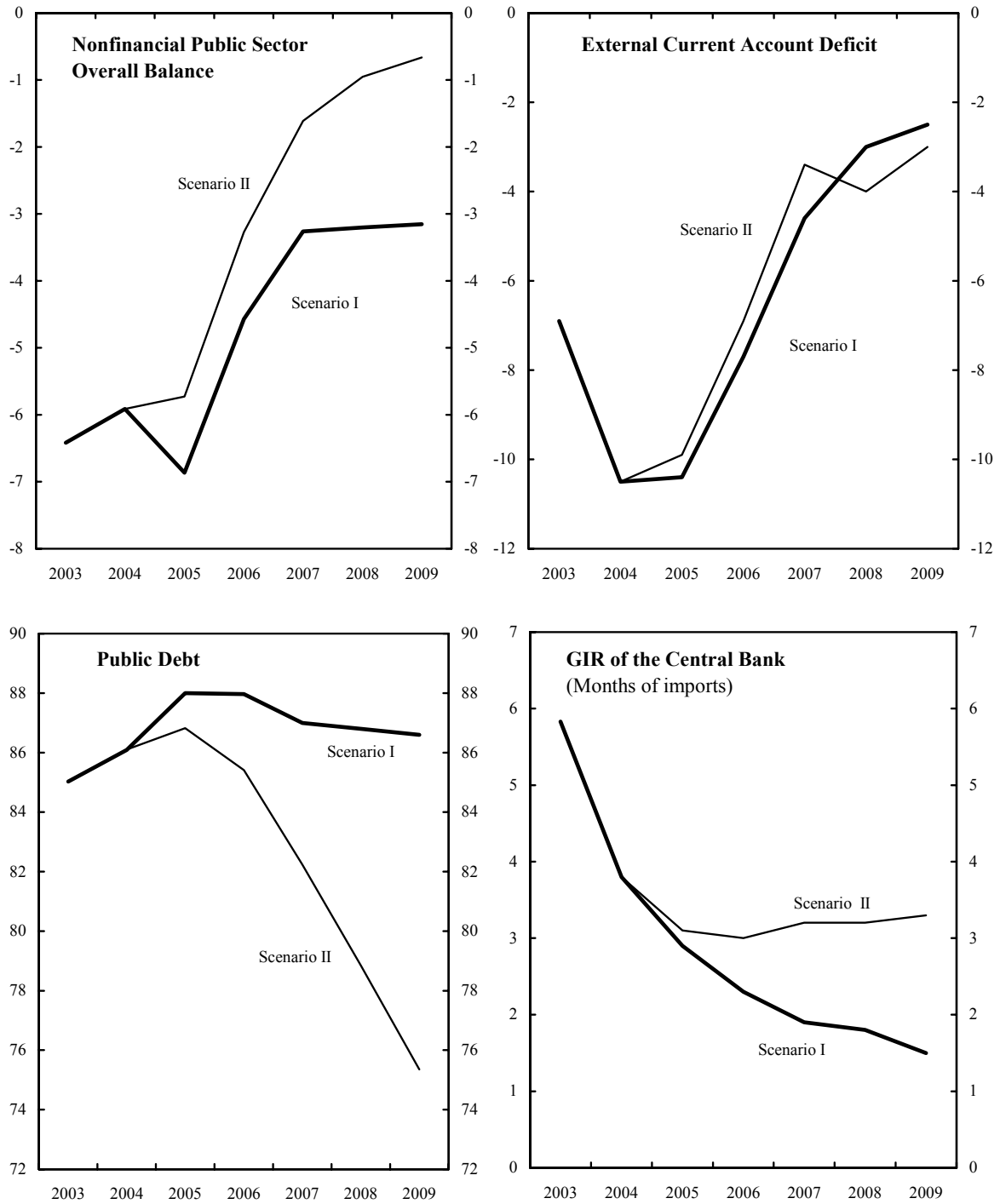
15. **Staff argued that the recent buildup of public debt and rapidly declining foreign exchange reserves called for a decisive fiscal adjustment.** In the absence of fiscal consolidation, the burden of addressing external imbalances would fall on the shoulders of monetary policy, crowding out private investment and dampening growth. Staff noted that there was now less scope for a gradual approach to reducing high fiscal deficits and public debt than in the past, given the recent deterioration of the external accounts. The authorities generally concurred with the broad thrust of the mission's views, but were concerned that a sharp fiscal adjustment would be incompatible with their desire to continue to provide high-quality public services and use public investment to boost Barbados' potential growth.

16. **The authorities and staff concurred that competitiveness would need to be enhanced to support the fixed exchange rate regime.** Staff argued that a tighter linking of wage awards with productivity developments, as well as structural reforms, were key to this effort. The authorities largely agreed, but viewed the growth fillip from structural reforms—especially trade liberalization—as likely to be modest in the near term, especially in light of the recent experience of some sectors in adapting to a more competitive environment.

#### A. Medium-Term Scenarios

17. **Activity in the near term will be boosted by the buildup to the 2007 cricket World Cup, but sustaining growth over the medium term may be more difficult.** The policy discussions with the authorities were guided by two medium-term scenarios that illustrated the importance of addressing macroeconomic imbalances and introducing reforms to enhance competitiveness (Figure 2 and Table 7). The baseline scenario (Scenario I)

Figure 2. Barbados: Medium-Term Scenarios, 2003–09  
(In percent of GDP)



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

incorporates the authorities' fiscal policy targets and presumes a relatively more modest set of structural reforms. As a result of the slow progress in reducing the debt and implementing structural reforms, growth is projected to revert closer to historical levels (2 percent) from 2008 onward. Despite some improvement in the current account, which is expected to occur as a result of monetary tightening and the associated decline in import growth, especially for consumer goods, international reserves will decline to less than two months of imports of goods and services by 2007.<sup>5</sup>

18. **The active scenario (Scenario II) envisages stronger policy adjustments.** These include accelerated structural reforms, a more ambitious fiscal adjustment to ensure debt sustainability and correct external imbalances, and a tighter monetary stance over 2005–07. As a result, sustained growth at 3–4 percent is achieved over the medium term, reflecting the supply-side effects of maintaining private investment at roughly the levels projected for the coming two years. The tightening of fiscal and monetary policy would also help curtail current account deficits and help maintain reserve cover at three months.

## B. Fiscal Policy

19. **The authorities indicated that their goal is to gradually return the deficit to around 3 percent of GDP, after allowing for an increase in FY 2005/06.** This would imply the nonfinancial public sector deficit falling from around 7 percent of GDP in FY 2005/06 to around 3¼ percent of GDP from FY 2007/08 onward, roughly the level that prevailed prior to the counter-cyclical stimulus in FY 2002/03. The authorities also reiterated their objective of reducing the debt of the central government to 60 percent of GDP, which they aim to achieve by FY 2010/11. Although the authorities have not established a target for the debt of the nonfinancial public sector as a whole, staff estimates suggest that it would remain at between 86–88 percent of GDP over the next five years.

20. **The authorities' fiscal strategy relies heavily on expenditure reduction.** Capital expenditures are projected to fall by over 2 percentage points of GDP with the completion of projects financed by privatization proceeds and greater use of public-private partnerships in the provision of economic infrastructure. Public enterprise balances are also projected to improve by over 1½ percent of GDP, owing to selective public tariff increases, and subsidies to cover enterprises' operating losses will be frozen in nominal terms, resulting in a decline in these outlays as a share of GDP. No additional revenue-raising measures are being contemplated, with the exception of a possible import surcharge on non-CARICOM imports that could yield ½ a percentage point of GDP in FY 2005/06.

21. **The revenue ratio, however, is expected to deteriorate significantly over the medium term.** The decline in import tariffs under the Free Trade Area of the Americas (FTAA), as well as the completion of the phased reduction in income tax rates, are projected to reduce revenues by 4–4½ percent of GDP. By FY 2009/10, revenues are projected to fall

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<sup>5</sup> Given capital controls, monetary policy is effective under the fixed exchange rate regime.

below 30 percent of GDP (3½ percentage points of GDP below their level at the beginning of the decade) and central government expenditures would decline to about 32 percent of GDP (some 2–3 percentage points below their level of FY 2000/01).

22. **Modest but important risks exist to achieving this baseline fiscal scenario.** The reduction in off-budgetary capital spending is not expected to be contentious, as this spending is limited to the funds generated by privatizations. Furthermore, the authorities' adjustment plans do not entail a reduction in government employment. However, some risks stem from the uncertainty regarding future increases in public tariffs, which will be necessary to improve public enterprise balances and reduce government subsidies. Furthermore, some of the fiscal incentives for selected sectors introduced in the Prime Minister's Economic and Financial Statement of December 2004 (for example, for dairy and beef production) could further erode the tax base.

23. **The mission called for a more ambitious plan of fiscal adjustment to put debt on a firmly declining path, reduce pressures on external reserves, and provide a fiscal cushion in the event of a negative shock.** Stronger fiscal adjustment was also needed to avoid excessive reliance on monetary tightening to shore up international reserves, which could choke off private investment and growth. A bolder fiscal consolidation would also strengthen the climate for private investment by signaling the authorities' resolve to reduce debt, which remains well above the average for Latin America and the Caribbean. The favorable world economic outlook would also support the growth of tourism and provide propitious timing for fiscal consolidation.

24. **Under the mission's active scenario, fiscal adjustment would begin this year.** Staff argued that otherwise, reserves could fall below three months of imports of goods and services, as suggested in the baseline scenario. In tandem with further projected losses, this could raise concerns about the consistency of the policy stance with the fixed exchange rate regime. Starting the adjustment now could also avoid the need for an even harsher and less gradual consolidation after the World Cup. Under the staff's scenario, the balance of the nonfinancial public sector would fall to 5¾ percent of GDP in FY 2005/06 and to slightly less than 1 percent of GDP by FY 2009/10 onward. The resulting deficit would result in a decline in public debt to around 75 percent of GDP by the end of the decade.<sup>6</sup> Beyond that point, it would be important to maintain the nonfinancial public sector deficit at this level in order to ensure that the debt ratio falls below 60 percent of GDP in another five years. The mission argued that in setting targets for public debt, the authorities should use this broader definition of public sector liabilities, especially in light of the significant amounts of public spending taking place outside the central government budget.

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<sup>6</sup> Net of government deposits in the banking system, government and government-guaranteed debt (excluding the National Insurance System (NIS)) would fall to 60 percent of GDP in FY 2012/13 and around 50 percent of GDP in FY 2015/16.



25. **The active scenario complements the authorities' planned reductions in expenditure with revenue measures.** Beyond what is included in the authorities' baseline scenario, no additional spending cuts are envisaged for central government expenditures, with the exception of off-budgetary outlays. In particular, since the scope for other measures in FY 2005/06 is limited, the team recommended that the privatization proceeds expected for the current year (about 1 percent of GDP) be used for debt reduction rather than extra budgetary capital expenditure. Thereafter, in order to achieve additional fiscal adjustment without causing an undesirable reduction in public services, the active scenario incorporates revenue measures of 1 percent of GDP. Drawing from FAD technical assistance recommendations, these could come from either the broadening of the VAT base, increases in the VAT rate, or increases in excises. Some additional adjustment would also come through increases in tariffs for water and public transportation, bringing the enterprises to a balanced position by the end of the decade.

26. **The mission suggested that the petroleum price mechanism be changed to preserve the financial position of the public enterprises.** During the past year, delays in adjusting administered prices for some consumers led to a deterioration of the balance of the state oil-importing company of  $\frac{1}{4}$  percent of GDP. Against this background, the team called for the introduction of a mechanism to allow for an automatic pass-through of the fluctuations in international prices to domestic prices. Harmonization of domestic and offshore tax regimes—which would improve the efficiency of the tax system as well as the environment for the growth of international business services and FDI—should also be considered, in line with recent FAD technical assistance.

27. **The authorities maintained that a more gradual and modest fiscal adjustment was appropriate.** In their view, a deficit of the nonfinancial public sector of about 3 percent of GDP was adequate and they expressed concern that a lower fiscal balance would be incompatible with the longstanding social pact between government, labor, and business that had served the country well. Furthermore, they stressed the need for infrastructure investment to generate faster growth over the medium term and the need to maintain a high level of public services. They also saw no evidence that past budget deficits had crowded out private sector investment, although they acknowledged their impact on the external current account deficit. They emphasized that government debt was held mainly by residents and in local currency, and vulnerabilities were mitigated by the low level of external debt. In light of the need to boost infrastructure ahead of the World Cup, as well as this more benign assessment of the near-term impact of higher fiscal deficits and debt on growth, they also saw less need to begin the fiscal adjustment in FY 2005/06.

### C. Budget Formulation and Fiscal Transparency

28. **The mission commended the authorities for their careful efforts to prepare for the adoption of a medium-term framework incorporating accrual and output-based budgeting, which is targeted for implementation in FY 2007/08.** Nonetheless, the team suggested that the understanding of the general public of the government's fiscal policy objectives and the implementation of fiscal policy could be further improved by broadening the coverage of fiscal data reported in budget documents. This could include supplemental

information on fiscal operations that are not explicitly recorded as government expenditure in the central government budget, but have a bearing on the public finances (such as tax concessions). The implications of public-private partnerships for government outlays could also be usefully incorporated into medium-term fiscal projections and disclosed in budgetary documents. The authorities took note of these suggestions, but observed that most of this information, while not in budget documents, was already in the public domain.<sup>7</sup>

#### **D. Monetary, Exchange Rate, and Financial Sector Policies**

29. **The staff and the authorities agreed that the fixed exchange rate regime continues to be appropriate for Barbados.** The peg to the U.S. dollar has served to increase the credibility of the exchange rate regime and provided an anchor for inflation and investor confidence. The authorities concurred with the mission on the need for supportive monetary, fiscal and structural policies to preserve the exchange rate regime.

30. **The mission suggested that additional monetary tightening was needed to maintain adequate reserves and support the fixed exchange rate regime.** In particular, slower credit growth in the coming years would be appropriate, especially in the face of the stimulus from the World Cup, and could avoid the need for a possibly more abrupt contraction in the future. The authorities envisaged a slowdown in commercial bank lending in 2005, although credit would still grow faster than nominal GDP over the next three years. The authorities cautioned that their external position was healthier than indicated by the level of central bank reserves alone, given the ability to require the repatriation of funds held by financial institutions under the “second-tier” reserves arrangement.<sup>8</sup>

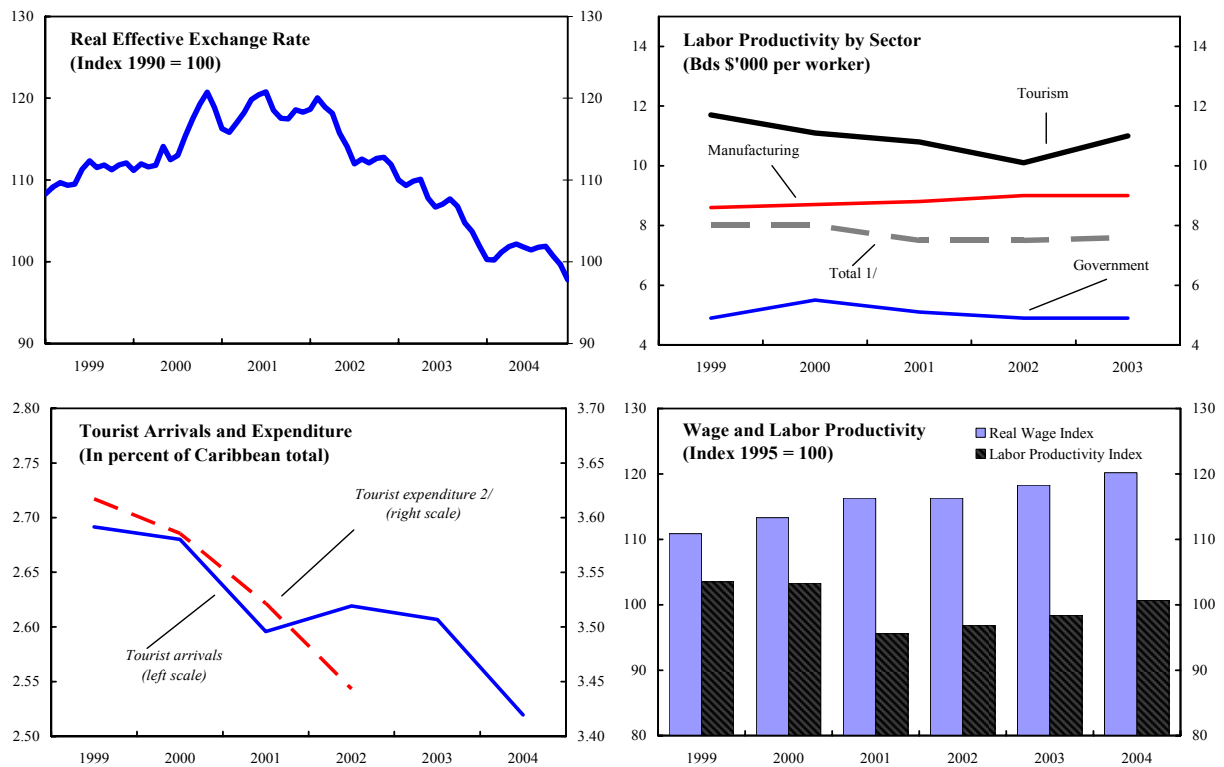
31. **The team also noted that sustaining the fixed exchange rate peg would require measures to strengthen competitiveness.** While the real effective exchange rate has declined since 1999, labor productivity has fallen by about 3 percent (Figure 3). Coupled with steady rises in real wages, falling productivity led to an increase in real unit labor costs of approximately 11 percent in 1999–2004. Moreover, competition from low-cost neighboring countries has intensified. This, coupled with rising unit labor costs, may have contributed to the deterioration in the trade balance and Barbados’ declining share of both

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<sup>7</sup> To assist the authorities in moving forward on their efforts to improve fiscal transparency, the mission recommended the authorities consider requesting a Report on the Observance of Standards and Codes (ROSC).

<sup>8</sup> The central bank’s policy of “second-tier reserves” is based on granting permission to private sector entities to make investments abroad, with the understanding that they be repatriated if required by the central bank. These reserves equaled about ½ month of imports of goods and services.

Figure 3. Barbados: Selected Competitiveness Indicators, 1999–2004



Sources: Barbadian authorities; IMF Information Notice System; Caribbean Tourism Organization; A. Downes (2005), *The Barbados Labour Market: A Diagnostic Study and Reform Proposals*; and staff estimates.

1/ Includes other sectors.

2/ Measured as average per day, multiplied by the number of tourists and average length of stay.

tourism arrivals and expenditures in the Caribbean. The authorities agreed with the staff on the need to better align wage increases with developments in labor productivity, and are aware of the need to strengthen competitiveness, particularly in agriculture and manufacturing. Toward this end, they have commissioned a series of studies by the IDB to assist them in formulating appropriate policy responses.<sup>9</sup>

32. **The mission encouraged the authorities to make greater use of indirect monetary policy instruments and to phase out the minimum deposit rate.** A phasing out of the minimum deposit rate, as well as greater reliance on indirect monetary policy instruments, could have a salutary effect on interest rate spreads and financial sector efficiency. In line with the recommendations of the 2002 FSAP, the government could consider issuing additional treasury bills through the central bank, with the proceeds placed in a blocked

<sup>9</sup> Papers on competitiveness, trade, tourism, agriculture and the labor market were presented at an IDB-sponsored workshop on April 1, 2005 in Washington, and in Barbados on May 4, 2005.

account. With greater reliance on these instruments for monetary policy operations, the minimum deposit rate could eventually be phased out.

33. **The authorities reiterated their commitment to develop indirect instruments, but preferred to maintain, at this time, the minimum deposit rate as their primary instrument.** In addition, they argued that the phasing out of the minimum deposit rate would increase (rather than decrease) spreads, owing to the oligopolistic structure of the banking system and the lack of competition for deposits. By contrast, analysis by the staff indicates a high degree of competition in the banking system.<sup>10</sup>

34. **The mission and authorities agreed that a further deepening of capital account liberalization should be contingent on macroeconomic conditions in Barbados.** Staff endorsed the authorities' strategy for capital account liberalization as envisaged under the Caribbean Single Market and Economy (CSME) initiative. The authorities reaffirmed their commitment to implementing the last steps in the liberalization process, which relate to investment abroad in real estate, the purchase of interest-bearing securities, and private borrowing. The easing of capital market restrictions could have several beneficial effects on the financial sector, principally by engendering competition for borrowing and lending, expanding the menu of saving instruments for the population, and allowing institutional savers such as the pension funds greater choice to diversify their portfolio of assets.

#### E. Addressing Vulnerabilities

35. **Fiscal sector vulnerabilities appear moderate, although high debt, and rising interest rates and oil prices, make the economy susceptible to shocks.** Gross financing requirements are high (25 percent of GDP), but are likely to be met mainly from domestic sources, and appear manageable over the medium term.<sup>11</sup> Nevertheless, a debt sustainability analysis, anchored on the baseline scenario, indicates that the debt ratio could rise markedly in the context of adverse shocks (Tables 8 and 9). Maintaining the primary deficit at its current level would also entail risks, with public debt rising to over 100 percent of GDP by the end of the decade. Furthermore, given the high correlation of economic activity with the industrial countries—owing to heavy dependence on tourism (Table 10)—the economy remains vulnerable to a downturn in world economic activity or deterioration in international security.

36. **The banking sector appears well poised to absorb shocks.** Current vulnerabilities are low in light of the high levels of capital and provisioning in the banking sector. Although recent ownership changes in the financial sector, including the privatization of the state-

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<sup>10</sup> See “Financial Intermediation and Monetary Policy,” Chapter I in the accompanying *Barbados—Selected Issues*.

<sup>11</sup> Commercial external debt represents less than 20 percent of the public debt. Vulnerabilities are attenuated by Barbados' investment grade rating for sovereign debt.

owned (and largest) bank potentially exposes Barbados' financial sector to shocks in other regional economies, vulnerabilities arising from this appear to be low.<sup>12</sup> The parent banks are well capitalized, and regional central banks have signed a memorandum of understanding for the consolidated supervision of interregional banks. The authorities are also progressing with outstanding issues raised in the FSAP, including those related to the preparation of guidelines for assessing market risks; revisions to the Financial Institutions Act; and strengthening the regulation and supervision of the insurance sector.

37. **Efforts have been made to mitigate weather-related vulnerabilities and their linkages to the financial sector.** Barbados lies outside the usual path for hurricanes in the Caribbean. Nevertheless, the recent destructive hurricanes in Grenada and the Cayman Islands—the former was last struck by a hurricane over 40 years ago—underscore how these disasters can have substantial ramifications for the financial sector in the region.<sup>13</sup> The authorities indicated that in the wake of last year's events, Barbados has been participating in efforts to reinvigorate the regional initiative for the pooling of catastrophic risk. National disaster preparedness plans were being reviewed on an annual basis, and all public assets were fully covered by insurance.

#### F. Growth-Enhancing Measures

38. **The mission encouraged an accelerated program of structural reforms aimed at improving the competitiveness and supply-side response of the economy.** The mission welcomed many of the measures taken by the authorities to improve the competitive environment in Barbados, including the reduction in corporate tax rates, telecommunications reform, and the corporatization of the airport. To further buttress these efforts, the mission suggested additional steps in the following areas:

- **Trade liberalization:** Although WTO compliant, Barbados' trade regime is moderately restrictive, reflecting an average tariff level of 16 percent and some residual export and import licensing requirements.<sup>14</sup> This imposes costs on a number of Barbados' more competitive activities, including tourism. Against this background, the mission strongly recommended against the imposition of a surcharge on non-CARICOM imports. The staff supported the authorities' strategy to liberalize trade in the context of the CMSE, including the proposed liberalization of trade of services, and the FTAA. At the same time, to complement these initiatives, the mission urged the authorities to eliminate remaining import and export licensing requirements.

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<sup>12</sup> During the last two years, two commercial banks were bought by Trinidadian and Bermudian entities.

<sup>13</sup> These hurricanes, for example, led to financial distress for a Jamaican-based insurance company.

<sup>14</sup> These apply to selected vegetables, processed food products, and manufacturing inputs.

- **Reform of the sugar sector:** The potential effects of the forthcoming changes in the European sugar regime—to be decided by the EU by end-2005—should be carefully assessed. The Government’s present strategy for the sector involves the diversification of the industry and promotion of new products, including ethanol. Given that Barbados is one of the world’s highest-cost producers of sugar, and in light of the reduction in prices envisaged under the EU sugar regime, it is questionable whether the industry—or activities using raw sugar as an input—can survive without high levels of public sector support. Moreover, the opportunity cost of land currently used for sugar production is high, given Barbados’ high population density. The team noted that the social costs of restructuring the industry could be ameliorated by the introduction of appropriate social safety nets for the affected workers.
- **Privatization and enterprise reform:** The mission supported the authorities’ strategy to privatize or place under private management all public enterprises that do not serve public policy objectives. In this context, it encouraged the authorities to move forward on their plan for divesting its shares in Gems hotels and the state-owned insurance company and to develop an explicit timetable for privatizing the remaining enterprises that fit the criterion described above.
- **Labor market flexibility:** The mission encouraged the authorities to explore options to further strengthen labor market flexibility, including those suggested in the recent IDB study on labor markets.<sup>15</sup> In particular, the authorities should examine whether there is scope to streamline unemployment and severance benefits in light of the dual eligibility of workers for both unemployment and severance payments. Options to improve worker training and the Labor Market Information System could also be explored.
- **Investment climate and fiscal incentives:** The mission noted that these incentives—which cover a wide range of activities and benefit both foreign and domestic producers—were costly, and that their effectiveness was highly uncertain. Rather than offering activity-specific tax incentives, staff suggested that surveys could be used to guide efforts to strengthen the investment climate, especially in light of the relatively low level of FDI outside of real estate. The mission also recommended a reassessment recent initiatives to ensure that market failures or public policy objectives justified the costs of government intervention. The authorities responded that recent initiatives were predicated on public policy concerns and that explicit financial support for these activities was captured in the budget. Regarding attracting remittances to Barbados from nationals living abroad, the authorities indicated that there were no impediments

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<sup>15</sup> See A. Downes, “The Barbados Labour Market: A Diagnostic Study and Reform Proposals,” paper prepared for an IDB-sponsored workshop on April 1, 2005 in Washington, and in Barbados on May 4, 2005.

to investment or remittances flows, and attributed the relatively low remittances to Barbados' high standard of living and the underreporting of these inflows.

### G. Statistical Issues

39. **The statistical information provided by Barbados is broadly adequate for surveillance purposes, although some important weaknesses remain.** While financial statistics are available on a timely basis, the coverage of data on the operation of public enterprises and on the capital account of the balance of payments need to be improved. The linkage between the offshore sector, the balance of payments, and the national income accounts also merits strengthening. An index of real estate prices would also greatly facilitate stress testing of different scenarios in financial markets.

### IV. STAFF APPRAISAL

40. **A strong recovery of the Barbadian economy appears to have taken hold during the last year, spearheaded by the tourism sector.** Growth prospects for the next three years are favorable, reflecting the strong global environment and the expected fillip to activity from the buildup to the 2007 World Cup.

41. **However, medium-term challenges remain.** In particular, macroeconomic imbalances—including high levels of public debt, high external current account deficits, and declining international reserves—will need to be addressed to preserve the fixed exchange rate regime and secure sustainable growth. In the absence of fiscal consolidation, public debt would rise steadily, and would exceed 100 percent of GDP by the end of the decade. The post-recession import surge has contributed to a widening of the external current account deficit, which is projected to remain at historically high levels over the next several years. The net international reserve position has weakened substantially during the last year, and is projected to fall below two months of imported goods and services by 2007 under the baseline scenario.

42. **Fiscal consolidation should be at the center of the strategy to address these imbalances.** While the authorities should be commended for the fiscal adjustment achieved over the last two years, the primary deficit nonetheless remains the highest in the region. Furthermore, the injection of fiscal stimulus in FY 2005/06, in the midst of a robust private-sector led recovery, will make the path to debt sustainability more difficult. Therefore, the fiscal deficit will need to be reduced decisively while the external economic environment remains favorable, so as to ensure that an adequate reserve cover is maintained, and that the government debt ratio is placed firmly on a declining path. This would help relieve the burden on monetary policy to shore up the reserve position and facilitate adequate credit growth to support private investment and economic activity.

43. **The government's effort to trim expenditures is commendable, but there is also a need to intensify the revenue effort.** These tax measures would partially offset the projected revenue loss from the decline in customs duties as a result of trade liberalization. The authorities' efforts to promote private sector participation in the provision of economic

infrastructure and services is welcome, but the expenditure commitments associated with these projects will need to be carefully monitored and controlled. The authorities are also encouraged to rationalize the tariffs of major public enterprises, in particular water and bus fares, with a view to reducing subsidies for these entities.

44. **The fixed exchange rate regime remains appropriate for Barbados.** The long-standing peg has become a strong anchor of price stability and investor confidence. To maintain the regime, it will be important to address recent macroeconomic imbalances that, if left unattended, will result in an erosion of external reserves to very low levels.

45. **Maintaining the fixed exchange rate regime will also require efforts to address rising unit labor costs that reduce competitiveness.** The decline in the real effective exchange rate—owing to the peg to the U.S. dollar—has shielded Barbados' external sector, to some extent, from the adverse effects of rising unit labor costs. To strengthen competitiveness, it will be important to better align wage increases with developments in labor productivity, and to accelerate productivity growth through structural reforms.

46. **The authorities are urged to make greater use of indirect monetary policy instruments.** The limited range of policy instruments has contributed to inefficient financial intermediation. It is recommended that the authorities phase out the administered minimum interest rate on savings deposits and consider accelerating the transition to market-based instruments of monetary control. Regarding broader financial sector reforms, the staff welcomes the actions taken to implement the remaining FSAP recommendations.

47. **There is scope to accelerate structural reforms in a wide range of areas.** The authorities have already made significant progress, including the corporatization of the airport authority and the move toward greater competition in the telecommunications sector, and the authorities' focus on reforms relating to the budget, tax policy, and privatization is welcome, as is their continued commitment to further trade and capital account liberalization in the context of the CSME and the envisaged FTAA. At the same time, there is scope to accelerate and deepen the structural reform effort, including by removing import and export licenses; reform of the sugar sector; privatizing the remaining public enterprises that do not meet public policy objectives; enhancing labor market flexibility; and rationalizing fiscal incentives.

48. **The statistical information provided by Barbados is broadly adequate for surveillance purposes, though some weaknesses remain.** In particular, the flow and coverage of data on the operations of the public enterprises and on the capital account of the balance of payments would need to be improved.

49. It is proposed that the next Article IV consultation with Barbados be conducted on the standard 12-month cycle.



Table 1. Barbados: Selected Economic and Financial Indicators

	2000	2001	2002	2003	Est. 2004	Proj. 2005
(Annual percentage changes, unless otherwise indicated)						
<b>Output and prices</b>						
Real GDP	2.3	-2.6	0.5	2.0	4.4	3.1
GDP deflator	0.0	2.8	-4.4	4.6	2.0	3.2
Consumer prices (12-month increase)	2.4	2.8	0.2	1.6	1.4	3.2
<b>Money and credit 1/</b>						
Net foreign assets	12.0	14.2	4.7	5.6	-8.8	-5.3
Net domestic assets	-4.2	-8.6	5.7	0.8	25.2	11.7
Net credit to public sector	-4.3	-8.1	12.2	3.6	4.1	7.4
<i>Of which</i> : central government	-3.4	-7.2	12.2	1.8	3.6	4.8
Credit to private sector	2.1	-0.3	2.4	0.6	11.0	4.3
Broad money (M2)	7.9	5.6	10.4	6.5	16.4	6.4
Velocity (ratio of GDP to M2)	1.60	1.51	1.32	1.35	1.21	1.21
<b>External sector</b>						
Exports of goods, f.o.b.	4.5	-5.3	-14.0	5.0	19.6	7.6
Tourism receipts	5.3	-1.2	-7.9	15.2	6.9	5.0
Imports of goods, f.o.b.	4.1	-7.6	0.1	11.6	18.3	5.2
Real effective exchange rate (depreciation -)	6.0	-1.3	-5.3	-8.9	-3.9	...
(In percent of GDP, unless otherwise indicated)						
<b>Public sector (fiscal year basis) 2/</b>						
Government revenue	33.3	33.6	33.9	34.2	33.0	32.5
Government expenditure	34.6	38.3	45.5	39.6	36.4	37.0
<i>Of which</i> : off-budget	-0.6	0.5	6.0	3.0	0.7	1.1
Government balance	-1.3	-4.7	-11.6	-5.4	-3.5	-4.5
<i>Of which</i> : budgetary balance	-1.9	-4.2	-5.6	-2.4	-2.7	-3.4
Public enterprise balance (after transfers)	-0.9	0.0	-1.2	-1.0	-2.4	-2.4
Nonfinancial public sector balance	-2.2	-4.7	-12.8	-6.4	-5.9	-6.9
Government and government-guaranteed debt	74.1	82.9	86.9	85.0	86.1	88.0
<i>Of which</i> : central government debt	64.1	73.6	78.4	75.3	74.5	74.7
<b>External sector</b>						
Current account balance	-5.7	-3.7	-7.5	-6.9	-10.5	-10.4
<i>Of which</i>						
Exports of goods, f.o.b.	11.2	10.7	9.4	9.1	10.4	10.5
Tourism receipts	28.3	28.0	26.6	28.1	28.8	28.4
Imports of goods, f.o.b.	40.3	37.3	38.5	39.5	44.7	44.2
Gross international reserves	18.9	27.8	27.6	27.9	21.2	16.1
(in millions of U.S. dollars)	484	707	683	752	595	473
(in months of imports of goods and services)	3.7	5.7	5.8	5.8	3.8	2.9
<b>Memorandum items:</b>						
Exchange rate (BD\$ per US\$)	2.00	2.00	2.00	2.00	2.00	2.00
Nominal GDP (millions of Barbados dollars)	5,118	5,108	4,952	5,390	5,625	5985

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

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

2/ Fiscal year begins on April 1.

Table 2. Barbados: Central Government Operations 1/

	2000/01	2001/02	2002/03	2003/04	Est. 2004/05	Proj. 2005/06
(In millions of Barbados dollars)						
Budgetary revenue	1,705	1,703	1,716	1,865	1,884	1,971
Tax revenue	1,615	1,613	1,637	1,793	1,827	1,899
Nontax revenue	90	90	79	71	57	65
Budgetary expenditure	1,803	1,917	1,997	1,997	2,039	2,178
Current expenditure	1,502	1,571	1,672	1,745	1,813	1,916
Wages and salaries and NIS contributions 2/	626	630	666	603	626	692
Interest	219	253	274	274	263	289
Transfers and subsidies	471	486	521	672	715	697
Capital expenditure and net lending	300	346	325	253	226	262
<i>Of which</i> : net lending	11	12	6	2	2	3
Budgetary balance	-98	-214	-281	-133	-156	-207
Float and extra-budgetary expenditure 3/	-33	23	305	162	42	65
Overall balance	-65	-237	-586	-295	-198	-272
Financing	65	237	586	295	198	272
Foreign financing (net)	163	322	-19	-16	-40	-59
Disbursements	203	364	58	55	35	18
Amortization	-40	-42	-78	-71	-75	-77
Domestic financing	-150	-85	606	121	238	271
Banking system	-113	-111	418	24	165	239
Rest of financial system	8	-26	83	57	72	0
National Insurance Scheme	-45	52	105	41	1	32
Privatization proceeds	52	0	0	189	0	60
(In percent of GDP)						
Budgetary revenue	33.3	33.6	33.9	34.2	33.0	32.5
Tax revenue	31.6	31.8	32.3	32.9	32.0	31.3
Nontax revenue	1.8	1.8	1.6	1.3	1.0	1.1
Budgetary expenditure	35.2	37.8	39.5	36.7	35.7	35.9
Current expenditure	29.4	31.0	33.0	32.0	31.7	31.6
Wages and salaries and NIS contributions 2/	12.2	12.4	13.2	11.1	11.0	11.4
Goods and services	3.6	4.0	4.2	3.6	3.7	3.9
Interest	4.3	5.0	5.4	5.0	4.6	4.8
Transfers and subsidies	9.2	9.6	10.3	12.3	12.5	11.5
Capital expenditure and net lending	5.9	6.8	6.4	4.6	4.0	4.3
Budgetary balance	-1.9	-4.2	-5.5	-2.4	-2.7	-3.4
Float and extra-budgetary expenditure 3/	-0.6	0.5	6.0	3.0	0.7	1.1
Overall balance	-1.3	-4.7	-11.6	-5.4	-3.5	-4.5
<i>Of which</i> : primary balance	3.0	0.3	-6.2	-0.4	1.1	0.3
Financing	1.3	4.7	11.6	5.4	3.5	4.5
<b>Memorandum items:</b>						
Overall balance of rest of nonfinancial public sector 4/	-0.9	0.0	-1.2	-1.0	-2.4	-2.4
Nonfinancial public sector overall balance	-2.2	-4.7	-12.8	-6.4	-5.9	-6.9
Government and government guaranteed debt	74.1	82.9	86.9	85.0	86.1	88.0
<i>Of which</i> : central government debt	64.1	73.6	78.4	75.3	74.5	74.7
Fiscal year GDP at market prices	5,115	5,069	5,062	5,449	5,715	6,066

Sources: Ministry of Finance; and Fund staff estimates.

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

2/ Reflects reclassification of the government hospital as a statutory corporation in 2003/04.

3/ Represents the difference between the budgetary deficit measured from above the line and the cash deficit measured on the basis of identified financing flows. Includes statistical discrepancy.

4/ After government transfers, based on financing data. Excludes the NIS.

Table 3. Barbados: Public Sector Financing Requirement and Debt

	2000/01	2001/02	2002/03	2003/04	Est. 2004/05	Proj. 2005/06
(In millions of Barbados dollars)						
<b>Gross financing requirement</b>						
Consolidated public sector deficit	112	239	646	350	337	417
Central government	65	237	586	295	198	272
Rest of the public sector 1/	47	2	60	55	139	145
Amortization payments on the public debt	903	926	1,014	1,138	1,077	1,098
Domestic	863	884	937	1,067	1,002	1,022
External	40	42	78	71	75	77
Gross financing requirement	1,014	1,166	1,661	1,488	1,414	1,515
Disbursements of domestic debt	1,030	975	1,337	1,232	1,396	1,437
Drawdown of deposits	-271	-173	265	12	-17	0
Disbursements of external debt	203	364	58	55	35	18
Privatization proceeds	52	0	0	189	0	60
<b>End-of-period public debt</b>						
Government and government-guaranteed debt	3,789	4,204	4,398	4,633	4,921	5,338
Central government	3,278	3,733	3,969	4,101	4,256	4,528
Rest of the public sector 1/	511	471	429	533	665	810
Domestic	2,625	2,719	2,984	3,211	3,390	3,873
External	1,165	1,485	1,414	1,423	1,531	1,465
(In percent of GDP)						
<b>Gross financing requirement</b>						
Consolidated public sector deficit	2.2	4.7	12.8	6.4	5.9	6.9
Central government	1.3	4.7	11.6	5.4	3.5	4.5
Rest of the public sector 1/	0.9	0.0	1.2	1.0	2.4	2.4
Amortization payments on the public debt	17.7	18.3	20.0	20.9	18.8	18.1
Domestic	16.9	17.4	18.5	19.6	17.5	16.8
External	0.8	0.8	1.5	1.3	1.3	1.3
Gross financing requirement	19.8	23.0	32.8	27.3	24.7	25.0
Disbursements of domestic debt	20.1	19.2	26.4	22.6	24.4	23.7
Drawdown of deposits	-5.3	-3.4	5.2	0.2	-0.3	0.0
Disbursements of external debt	4.0	7.2	1.1	1.0	0.6	0.3
Privatization proceeds	1.0	0.0	0.0	3.5	0.0	1.0
<b>End-of-period public debt</b>						
Government and government-guaranteed debt	74.1	82.9	86.9	85.0	86.1	88.0
Central government	64.1	73.6	78.4	75.3	74.5	74.7
Rest of the public sector 1/	10.0	9.3	8.5	9.8	11.6	13.3
Domestic	51.3	53.6	59.0	58.9	59.3	63.8
External	22.8	29.3	27.9	26.1	26.8	24.2

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

1/ Excludes the National Insurance Scheme.

Table 4. Barbados: Summary Monetary Survey

	2000	2001	2002	2003	Est. 2004	Proj. 2005
(In millions of Barbados dollars)						
Net foreign assets	749	1,205	1,365	1,576	1,224	979
Net domestic assets	2,456	2,181	2,373	2,404	3,408	3,950
Net credit to public sector	193	(67)	348	481	644	987
Central government	471	242	654	723	867	1,088
Rest of public sector	-36	-37	-22	154	183	334
National Insurance Scheme	-242	-272	-284	-396	-406	-434
Credit to private sector	2,518	2,508	2,589	2,612	3,049	3,247
Other items (net)	-255	-260	-564	-689	-285	-285
Liabilities to private sector (M2)	3,205	3,386	3,738	3,980	4,632	4,928
Currency in circulation	311	312	337	329	399	424
Demand deposits	756	836	1,104	1,202	1,498	1,594
Savings deposits	1,753	1,847	1,978	2,140	2,358	2,509
Time deposits	385	390	318	309	377	401
(Changes in percent of beginning-of-period, M2)						
Net foreign assets	12.0	14.2	4.7	5.6	-8.8	-5.3
Net domestic assets	-4.2	-8.6	5.7	0.8	25.2	11.7
Net credit to public sector	-4.3	-8.1	12.2	3.6	4.1	7.4
<i>Of which:</i> central government	-3.4	-7.2	12.2	1.8	3.6	4.8
Credit to private sector	2.1	-0.3	2.4	0.6	11.0	4.3
Other items (net)	-1.9	-0.1	-9.0	-3.3	10.2	0.0
Liabilities to private sector (M2)	7.9	5.6	10.4	6.5	16.4	6.4
<b>Memorandum items:</b>						
Second-tier reserves (in millions of Barbados dollars) 1/	n.a.	n.a.	24.7	183.4	168.6	168.6
Credit to private sector (12-month increase)	2.6	-0.4	3.3	0.9	16.7	6.5
M2 velocity	1.60	1.51	1.32	1.35	1.21	1.21

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

1/Under the second-tier program, private sector entities are allowed to make investments abroad, with a written agreement to repatriate funds, if requested by the central bank.

Table 5. Barbados: Summary Balance Sheet of the Central Bank

	2000	2001	2002	2003	2004	Proj. 2005
(In millions of Barbados dollars)						
<b>End-of-period stocks</b>						
Net international reserves	969	1,414	1,366	1,503	1190	945
Net domestic assets	-406	-767	-458	-421	-419	-199
Net credit to public sector	-466	-765	-477	-407	-428	-208
Central government	-461	-758	-474	-405	-428	-207
Rest of public sector	-6	-7	-3	-2	-1	-1
National Insurance Scheme	0	0	0	0	0	0
Credit to commercial banks	0	0	0	0	0	0
Credit to rest of financial institutions	9	9	9	9	9	9
Other items (net)	51	-11	10	-22	0	0
Monetary base	563	647	908	1,083	771	746
Currency in circulation	311	312	337	329	399	424
Liabilities to commercial banks	252	335	571	754	372	322
(Changes in percent of beginning-of-period monetary base)						
Net international reserves	71.0	79.1	-7.4	15.1	-28.9	-31.8
Net domestic assets	-58.7	-64.1	47.7	4.1	0.1	28.6
<i>Of which:</i> net credit to central government	-53.4	-52.8	43.8	7.6	-2.1	28.6
Monetary base	12.3	15.0	40.3	19.2	-28.8	-3.2
<b>Memorandum item:</b>						
Gross international reserves (in millions of U.S. dollars)	484.4	707.0	683.2	751.7	595.2	472.5
In months of imports of goods & services	3.7	5.7	5.8	5.8	3.8	2.9

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

Table 6. Barbados: Balance of Payments  
(In millions of U.S. dollars)

	2000	2001	2002	2003	Est. 2004	Proj. 2005
Current account	-145.0	-93.8	-185.5	-186.3	-295.4	-311.9
Merchandise trade balance	-743.9	-681.1	-719.8	-818.6	-964.9	-1,029.6
Exports	286.3	271.2	233.3	245.0	293.0	315.2
<i>Of which</i>						
Domestic exports	189.6	176.3	148.8	147.9	173.4	187.5
Sugar and molasses	26.1	22.0	18.8	20.5	22.4	25.4
Other	163.5	154.3	129.9	127.4	151.0	162.2
Imports	1,030.2	952.2	953.1	1,063.6	1,257.9	1,344.8
Services (net)	602.9	586.8	549.9	646.6	684.0	732.2
Travel (credit)	628.9	613.1	558.9	653.4	701.4	744.1
Investment income (net)	-82.3	-93.4	-101.8	-107.0	-110.5	-116.2
<i>Of which</i>						
Interest on public debt	-50.0	-44.6	-51.5	-51.5	-55.0	-56.1
Current transfers (net)	78.4	93.9	86.2	92.8	96.1	101.7
Capital account	323.6	290.1	230.2	302.4	106.1	189.2
Long-term capital	301.2	284.2	156.2	218.2	84.4	158.8
Public sector	123.1	152.4	-14.7	77.5	-42.0	-0.8
Central government	104.4	155.6	16.9	89.9	-2.0	8.3
Government guaranteed	19.7	-3.3	-31.6	-12.4	-40.1	-9.1
Central bank	-0.9	0.0	0.0	0.0	0.0	0.0
Private sector	178.1	131.8	170.8	140.7	126.4	159.6
Direct investment	170.6	133.9	97.1	158.6	131.1	117.5
other private	22.4	-0.3	77.9	-4.2	13.2	47.7
Short-term capital	22.5	5.4	74.0	84.2	21.8	30.4
Change in commercial banks assets	22.8	4.0	-112.5	0.0	0.0	0.0
Errors and omissions	-23.5	25.0	43.9	-47.6	32.9	0.0
Overall balance (deficit -)	178.0	224.7	-23.9	68.5	-156.4	-122.7
<b>Memorandum items:</b>						
Current account (percent of GDP)	-5.7	-3.7	-7.5	-6.9	-10.5	-10.4
Exports of goods and nonfactor services	1,279.8	1,261.6	1,190.1	1,313.4	1,408.3	1,485.3
Imports of goods and nonfactor services	1,560.7	1,484.0	1,410.9	1,547.4	1,859.3	1,966.1
Gross international reserves	484.4	707.0	683.2	751.7	595.2	472.5
Gross international reserves (in months of						
imports of goods and nonfactor services)	3.7	5.7	5.8	5.8	3.8	2.9
Second-tier reserves 1/	n.a.	n.a.	12.4	91.7	84.3	84.3
Second-tier reserves (in months of						
imports of goods and nonfactor services)	n.a.	n.a.	0.1	0.7	0.5	0.5
Public external debt	578.1	744.5	730.8	734.1	770.0	735.1
Public external debt (percent of GDP)	22.6	29.1	29.5	27.2	27.4	24.9

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

1/ Under the second-tier program, private sector entities are allowed to make investments abroad, with a written agreement to repatriate funds, if requested, by the Central Bank.

Table 7. Barbados: Illustrative Medium-Term Scenarios

	2003	Est. 2004	Projections				
			2005	2006	2007	2008	2009
<b>Scenario I (Baseline)</b> (Annual percentage changes)							
<b>Macroeconomic parameters</b>							
Real GDP	2.0	4.4	3.1	3.3	3.5	2.0	2.0
Average CPI	1.6	1.4	3.2	2.0	2.0	2.0	2.0
Nominal GDP	8.8	4.4	6.4	5.4	5.6	4.0	4.0
(In percent of GDP, unless otherwise indicated)							
<b>Budget and public debt 1/</b>							
Central government revenue	34.2	33.0	32.5	31.0	30.6	30.2	29.8
Central government expenditure 2/	39.6	36.4	37.0	33.7	33.2	32.7	32.3
Central government balance	-5.4	-3.5	-4.5	-2.7	-2.6	-2.5	-2.5
Nonfinancial public sector overall balance	-6.4	-5.9	-6.9	-4.6	-3.3	-3.2	-3.2
<i>Of which</i> : primary balance	-1.4	-1.3	-2.1	0.4	1.7	1.8	1.8
Government and government-guaranteed debt	85.0	86.1	88.0	88.0	87.0	86.8	86.6
<b>Banking system 3/</b>							
Net foreign assets	5.6	-8.8	-5.3	-3.9	-1.8	-0.9	-1.3
Net domestic assets	0.8	25.2	11.7	9.3	7.4	5.0	5.4
<i>Of which</i> : net credit to government	1.8	3.6	4.8	3.5	3.1	3.1	3.1
Broad money	6.5	16.4	6.4	5.4	5.6	4.0	4.0
<b>External sector</b>							
Current account balance	-6.9	-10.5	-10.4	-7.7	-4.6	-3.0	-2.5
Gross international reserves (in US\$ million)	752	595	473	377	330	304	265
(In months of imports of goods and services)	5.8	3.8	2.9	2.3	1.9	1.8	1.5
<b>Scenario II (Active)</b> (Annual percentage changes)							
<b>Macroeconomic parameters</b>							
Real GDP	2.0	4.4	3.1	3.5	4.0	3.5	3.5
Average CPI	1.6	1.4	3.2	2.0	2.0	2.0	2.0
Nominal GDP	8.8	4.4	6.4	5.6	6.1	5.6	5.6
(In percent of GDP, unless otherwise indicated)							
<b>Budget and public debt 1/</b>							
Budgetary revenue	34.2	33.0	32.5	32.0	31.6	31.2	30.8
Total expenditure 2/	39.6	36.4	35.9	33.6	32.7	31.9	31.4
Central government balance	-5.4	-3.5	-3.4	-1.6	-1.2	-0.8	-0.7
Nonfinancial public sector overall balance	-6.4	-5.9	-5.7	-3.3	-1.6	-1.0	-0.7
<i>Of which</i> : primary balance	-1.4	-1.3	-1.0	1.6	3.2	3.7	3.8
Government and government-guaranteed debt	85.0	86.1	86.8	85.4	82.2	78.8	75.3
<b>Banking system 3/</b>							
Net foreign assets	5.6	8.8	-4.2	-0.4	2.0	1.1	1.4
Net domestic assets	0.8	25.2	10.6	6.0	4.0	4.5	4.2
<i>Of which</i> : net credit to government	1.8	3.6	3.7	2.1	1.4	1.0	0.9
Broad money	6.5	16.4	6.4	5.6	6.1	5.6	5.6
<b>External sector</b>							
Current account balance	-6.9	-10.5	-9.9	-6.9	-3.4	-4.0	-3.0
Gross international reserves (in US\$ million)	752	595	499	488	541	570	611
(In months of imports of goods and services)	5.8	3.8	3.1	3.0	3.2	3.2	3.3

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

1/ Data refer to fiscal years beginning April 1.

2/ Includes extra-budgetary outlays.

3/ In percent of beginning-of-period broad money

Table 8. Barbados: Public Sector Debt Sustainability Framework, 2002/03–2010/11  
(In percent of GDP, unless otherwise indicated)

	2002/03					2003/04					2004/05					Projections					Debt-stabilizing Primary Balance 10/
	2002/03	2003/04	2003/04	2004/05	2004/05	2005/06	2006/07	2007/08	2008/09	2009/10	2010/11	2005/06	2006/07	2007/08	2008/09	2009/10	2010/11				
<b>Public sector debt 1/</b>	86.9	85.0	86.1	86.1	86.1	88.0	88.0	87.0	86.8	86.6	85.5	88.0	88.0	87.0	86.8	86.6	85.5	1.6			
<i>Of which:</i> foreign-currency denominated	27.9	26.1	26.8	26.8	26.8	24.2	22.6	20.8	19.5	18.0	16.7	24.2	22.6	20.8	19.5	18.0	16.7				
Change in public sector debt	4.0	-1.9	1.1	1.1	1.1	1.9	0.0	-1.1	-0.2	-0.2	-1.1	1.9	0.0	-1.1	-0.2	-0.2	-1.1				
Identified debt-creating flows (4+7+12)	12.9	-3.4	4.3	4.3	4.3	0.9	0.0	-1.1	-0.1	-0.2	-0.6	0.9	0.0	-1.1	-0.1	-0.2	-0.6				
Primary deficit	7.4	1.4	4.2	4.2	4.2	2.1	-0.4	-1.7	-1.8	-1.8	-2.2	2.1	-0.4	-1.7	-1.8	-1.8	-2.2				
Revenue and grants	33.9	34.2	33.0	33.0	33.0	32.5	31.0	30.6	30.2	29.8	29.8	32.5	31.0	30.6	30.2	29.8	29.8				
Primary (non-interest) expenditure	41.3	35.6	37.2	37.2	37.2	34.6	30.6	28.9	28.4	28.0	27.6	34.6	30.6	28.9	28.4	28.0	27.6				
Automatic debt dynamics 2/	5.5	-1.3	0.1	0.1	0.1	-0.2	0.4	0.6	1.6	1.6	1.6	-0.2	0.4	0.6	1.6	1.6	1.6				
Contribution from interest rate/growth differential 3/	5.5	-1.3	0.1	0.1	0.1	-0.2	0.4	0.6	1.6	1.6	1.6	-0.2	0.4	0.6	1.6	1.6	1.6				
<i>Of which:</i> contribution from real interest rate	6.3	0.8	3.5	3.5	3.5	2.3	3.2	3.3	3.3	3.3	3.2	2.3	3.2	3.3	3.3	3.3	3.2				
<i>Of which:</i> contribution from real GDP growth	-0.7	-2.1	-3.4	-3.4	-3.4	-2.6	-2.8	-2.6	-1.7	-1.7	-1.6	-2.6	-2.8	-2.6	-1.7	-1.7	-1.6				
Contribution from exchange rate depreciation 4/	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0				
Other identified debt-creating flows	0.0	-3.5	0.0	0.0	0.0	-1.0	0.0	0.0	0.0	0.0	0.0	-1.0	0.0	0.0	0.0	0.0	0.0				
Privateization receipts (negative)	0.0	-3.5	0.0	0.0	0.0	-1.0	0.0	0.0	0.0	0.0	0.0	-1.0	0.0	0.0	0.0	0.0	0.0				
Recognition of implicit or contingent liabilities	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0				
Other (specify, e.g., bank recapitalization)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0				
Residual, including asset changes (2-3)	-8.9	1.5	-3.2	-3.2	-3.2	1.0	0.0	0.0	0.0	0.0	-0.5	1.0	0.0	0.0	0.0	0.0	-0.5				
Public sector debt-to-revenue ratio 1/	256.3	248.5	261.2	261.2	261.2	270.8	283.9	284.1	287.3	290.6	286.9	270.8	283.9	284.1	287.3	290.6	286.9				
<b>Gross financing need 5/</b>	32.8	27.3	27.7	27.7	27.7	25.0	23.1	22.6	23.3	22.6	22.1	25.0	23.1	22.6	23.3	22.6	22.1				
In billions of U.S. dollars	830.3	743.9	790.5	790.5	790.5	757.4	737.4	760.8	815.9	823.8	837.1	757.4	737.4	760.8	815.9	823.8	837.1				
<b>Key macroeconomic and fiscal assumptions</b>																					
Real GDP growth (in percent)	0.8	2.6	4.2	2.1	2.1	3.2	3.4	3.1	2.0	2.0	2.0	3.2	3.4	3.1	2.0	2.0	2.0	2.6			
Average nominal interest rate on public debt (in percent) 6/	6.5	6.2	5.7	6.7	6.7	5.9	6.0	6.0	6.0	5.9	5.9	5.9	6.0	6.0	6.0	5.9	5.9	5.9			
Average real interest rate (nominal rate minus change in GDP deflator, in percent)	7.5	1.1	4.4	4.1	1.9	3.0	3.9	4.0	4.0	4.0	3.9	3.0	3.9	4.0	4.0	4.0	3.9	3.8			
Nominal appreciation (increase in U.S. dollar value of local currency, in percent)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0			
Inflation rate (GDP deflator, in percent)	-1.0	5.1	1.3	2.6	1.9	2.9	2.0	2.0	2.0	2.0	2.0	2.9	2.0	2.0	2.0	2.0	2.0	2.1			
Growth of real primary spending (deflated by GDP deflator, in percent)	24.8	-11.6	8.1	5.6	11.2	-4.0	-8.6	-2.8	0.5	0.5	0.5	-4.0	-8.6	-2.8	0.5	0.5	0.5	-2.3			
Primary deficit	7.4	1.4	4.2	-0.3	3.7	2.1	-0.4	-1.7	-1.8	-1.8	-2.2	2.1	-0.4	-1.7	-1.8	-1.8	-2.2	-1.0			
<b>A. Alternative scenarios</b>																					
A1. Key variables are at their historical averages in 2006/07–09/10 7/	88.0	89.2	90.5	91.8	93.1	88.0	89.2	90.5	91.8	93.1	93.9	88.0	89.2	90.5	91.8	93.1	93.9	1.6			
A2. No policy change (constant primary balance) in 2006/07–09/10	88.0	90.5	93.3	97.2	101.1	88.0	90.5	93.3	97.2	101.1	104.5	88.0	90.5	93.3	97.2	101.1	104.5	1.9			
A3. Country-specific shock in 2006/07, with reduction in GDP growth (relative to baseline) of one standard deviation 8/	89.8	89.9	88.8	88.6	88.4	89.8	89.9	88.8	88.6	88.4	87.3	89.8	89.9	88.8	88.6	88.4	87.3	1.6			
A4. Selected variables are consistent with market forecast in 2006/07–09/10	88.0	88.0	87.0	86.8	86.6	88.0	88.0	87.0	86.8	86.6	85.5	88.0	88.0	87.0	86.8	86.6	85.5	1.6			
<b>B. Bound tests</b>																					
B1. Real interest rate is at historical average plus two standard deviations in 2006/07 and 2007/08	88.0	91.5	94.0	93.9	92.9	88.0	91.5	94.0	93.9	92.9	92.9	88.0	91.5	94.0	93.9	92.9	92.9	1.7			
B2. Real GDP growth is at historical average minus two standard deviations in 2006/07 and 2007/08	88.0	94.4	101.3	104.4	107.5	88.0	94.4	101.3	104.4	107.5	109.7	88.0	94.4	101.3	104.4	107.5	109.7	2.0			
B3. Primary balance is at historical average minus two standard deviations in 2006/07 and 2007/08	88.0	95.6	103.6	103.7	103.8	88.0	95.6	103.6	103.7	103.8	103.1	88.0	95.6	103.6	103.7	103.8	103.1	1.9			
B4. Combination of B1-B3 using one standard deviation shocks	88.0	96.5	105.5	105.7	105.9	88.0	96.5	105.5	105.7	105.9	105.1	88.0	96.5	105.5	105.7	105.9	105.1	1.9			
B5. One time 30 percent real depreciation in 2006/07 9/	88.0	99.5	98.5	98.6	97.8	88.0	99.5	98.5	98.6	97.8	97.8	88.0	99.5	98.5	98.6	97.8	97.8	1.8			
B6. 10 percent of GDP increase in other debt-creating flows in 2006/07	88.0	98.0	97.0	97.1	96.2	88.0	98.0	97.0	97.1	96.2	96.2	88.0	98.0	97.0	97.1	96.2	96.2	1.8			

Source: 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  $(r - \pi(1+g) - g + \alpha(1+r)/(1+g+\pi+gr))$  times previous period debt ratio, with  $r$  = interest rate;  $g$  = growth rate of GDP deflator;  $\pi$  = growth rate of foreign-currency denominated debt; and  $\alpha$  = 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 numerator in footnote 2/ as  $\alpha(1+r)$ .

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/ The key variables include real GDP growth; real interest rate; and primary balance in percent of GDP.

8/ The implied change in other key variables under this scenario is discussed in the text.

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

10/ Assumes that key variables (real GDP growth, real interest rate, and other identified debt-creating flows) remain at the level of the last projection year.



Table 9. Barbados: External Sustainability Framework, 2002–10

	Projections										Debt-stabilizing non-interest current account 6/	
	2002	2003	2004	2005	2006	2007	2008	2009	2010			
<b>External debt</b>												
Change in external debt	29.5	27.2	27.4	24.9	22.8	21.0	19.6	18.6	17.2			
Identified external debt-creating flows	0.4	-2.3	0.1	-2.5	-2.1	-1.8	-1.4	-1.0	-1.4			
Current account deficit, excluding interest payments	-0.2	-6.1	12.1	3.8	2.3	0.0	-0.5	-0.4	-1.2			
Deficit in balance of goods and services	5.5	5.0	8.5	8.6	6.0	3.1	1.6	1.2	0.7			
Exports	8.2	8.1	16.1	16.3	13.3	10.1	8.3	7.9	7.4			
Imports	48.7	49.4	50.0	50.2	50.5	52.7	51.4	51.3	51.2			
Net nondebt creating capital inflows (negative)	56.9	57.4	66.1	66.5	63.7	62.9	59.7	59.2	58.7			
Net foreign direct investment (equity)	-6.8	-11.8	-4.5	-5.4	-3.9	-3.4	-2.7	-2.1	-2.5			
Net portfolio investment: equity	6.8	11.8	4.5	5.4	3.9	3.3	2.6	2.2	2.5			
Automatic debt dynamics 1/	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0			
Denominator: $1+g+r+g$	1.2	0.9	8.1	0.6	0.1	0.3	0.6	0.6	0.6			
Contribution from nominal interest rate	1.0	1.0	0.8	1.1	1.1	1.1	1.0	1.0	1.0			
Contribution from real GDP growth	1.9	1.9	1.8	1.9	1.7	1.5	1.4	1.3	1.3			
Contribution from price and exchange rate changes 2/	-0.1	-0.6	-1.5	-0.8	-0.8	-0.8	-0.4	-0.4	-0.4			
Residual, including change in gross foreign assets (2-3)	-0.6	-0.6	-0.5	-0.5	-0.4	-0.4	-0.4	-0.4	-0.4			
External debt-to-exports ratio (in percent)	0.5	3.7	-4.1	-6.3	-4.3	-1.8	-0.8	-0.7	-0.2			
Gross external financing need (in billions of U.S. dollars) 3/	60.5	55.2	54.7	49.5	45.1	39.8	38.2	36.2	33.5			
In percent of GDP	0.4	0.5	0.6	0.6	0.3	0.2	0.2	0.2	0.1			
	17.5	17.4	21.0	20.6	9.6	6.6	4.8	4.4	3.9			
<b>Key Macroeconomic Assumptions</b>												
Real GDP growth (in percent)	0.5	2.0	4.5	3.1	3.3	3.5	2.0	2.0	2.0			
Exchange rate appreciation (U.S. dollar value of local currency, change in percent)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0			
GDP deflator (change in domestic currency)	-2.3	2.9	2.0	3.2	2.0	2.0	2.0	2.0	2.0			
GDP deflator in U.S. dollars (change in percent)	-2.3	2.9	2.0	3.2	2.0	2.0	2.0	2.0	2.0			
Nominal external interest rate (in percent)	6.8	7.2	7.1	12.2	9.3	7.3	7.0	7.1	7.3			
Growth of exports (U.S. dollar terms, in percent)	-4.3	10.2	5.8	4.9	18.9	5.6	7.2	10.3	3.9			
Growth of imports (U.S. dollar terms, in percent)	-5.0	9.7	20.2	7.4	8.0	5.8	2.1	4.2	-1.2			
Current account balance, excluding interest payments	-5.4	-5.1	-8.7	-0.5	7.2	-8.5	-6.1	-3.2	-1.6			
Net nondebt creating capital inflows	6.8	11.8	4.5	3.7	3.7	3.4	2.7	2.2	2.5			
<b>A. Alternative Scenarios</b>												
A1. Key variables are at their historical averages in 2006–10 4/				24.9	19.2	15.5	12.6	9.6	6.8			
A2. Country-specific shock in 2005, with reduction in GDP growth (relative to baseline) of one standard deviation 5/				24.9	22.8	21.0	19.6	18.6	17.2			
A3. Unchanged current account deficit in 2005–10				24.9	23.1	28.1	32.5	39.0	45.7			
<b>B. Bound Tests</b>												
B1. Nominal interest rate is at historical average plus two standard deviations in 2006 and 2007				24.9	28.3	32.9	31.9	31.2	30.6			
B2. Real GDP growth is at historical average minus two standard deviations in 2006 and 2007				24.9	23.8	22.9	21.1	19.8	18.1			
B3. Change in US dollar GDP deflator is at historical average minus two standard deviations in 2006 and 2007				24.9	26.3	27.4	24.6	22.5	20.0			
B4. Non-interest current account is at historical average minus two standard deviations in 2006 and 2007				24.9	31.6	41.6	40.8	40.4	39.7			
B5. Combination of B1–B4 using one standard deviation shocks				24.9	30.7	41.0	39.6	38.7	37.3			
B6. One time 30 percent nominal depreciation in 2006				24.9	30.0	26.0	23.3	21.1	18.7			

Source: Fund staff estimates and projections.

1/ Derived as  $(1 - g - r + g) + \text{er}(1+r) / (1+g+r+g)$  times previous period debt stock, with  $r$  = nominal effective interest rate on external debt;  $r$  = change in domestic GDP deflator in U.S. dollar terms;  $g$  = real GDP growth rate;  $e$  = nominal appreciation (increase in dollar value of domestic currency), and  $a$  = share of domestic-currency denominated debt in total external debt.

2/ The contribution from price and exchange rate changes is defined as  $(1+r)(1+g) - \text{er}(1+r) / (1+g+r+g)$  times previous period debt stock.  $r$  increases with an appreciating domestic currency ( $e > 0$ ) and rising inflation (based on GDP deflator).

3/ Defined as current account deficit, plus amortization on medium- and long-term debt, plus short-term debt at end of previous period.

4/ The key variables include real GDP growth; nominal interest rate; dollar deflator growth; and both non-interest current account and nondebt inflows in percent of GDP.

5/ The implied change in other key variables under this scenario is discussed in the text.

6/ Long-run, constant balance that stabilizes the debt ratio assuming that key variables (real GDP growth, nominal interest rate, dollar deflator growth, and nondebt inflows in percent of GDP) remain at their levels of the last projection year.

Table 10. Barbados: Selected Vulnerability Indicators  
(In percent of GDP, unless otherwise indicated)

	2000	2001	2002	2003	Est. 2004	Proj. 2005
<b>Real sector indicators</b>						
Tourist sector, percent of GDP 1/	15.8	15.2	14.7	15.5	16.0	16.4
Travel receipts, percent of total exports	56.5	56.6	55.3	57.7	57.5	57.3
Tourist and general services sectors, percent of GDP	73.0	73.1	72.8	73.6	74.3	74.7
<b>Fiscal indicators 2/</b>						
Overall balance of the public sector	-2.1	-5.0	-12.5	-6.4	-5.9	-6.9
Primary public sector balance	2.2	-0.1	-7.1	-1.4	-1.3	-2.1
Gross public sector financing requirement	19.8	23.3	32.4	27.7	25.1	23.5
Public sector gross debt 3/	74.1	82.9	86.9	85.0	86.1	88.0
Public sector gross external debt 3/	22.8	29.3	27.9	26.1	26.8	24.2
External interest payments to total fiscal revenue (percent)	6.0	5.2	6.0	5.5	5.0	5.3
External amortization payments to total fiscal revenue (percent)	2.8	3.2	3.9	3.8	4.0	3.9
<b>Financial indicators</b>						
Broad money (percent change, 12-month basis)	7.9	5.6	10.4	6.5	16.4	6.4
Private sector credit (percent change, 12-month basis)	2.6	-0.4	3.3	0.9	16.7	6.5
Interest rate spread 4/	7.0	8.0	7.7	7.6	7.3	...
Three-month T-bill rate 5/	3.9	2.0	1.5	0.6	2.8	...
Excess liquidity ratio	7.7	8.9	17.9	21.8	18.4	...
Capital adequacy ratio (indigenous banks)	15.9	18.2	18.8	25.0	17.9	...
NPLs/total loans	3.8	5.0	7.9	9.3	7.5	...
Loan loss provisions/total assets	1.2	1.3	0.9	1.2	0.9	...
Loans to tourism/total loans	12.1	10.7	11.5	13.4	10.8	...
Loans to households/total loans	40.1	43.3	40.7	43.3	43.5	...
Mortgage loans/total loans	10.6	13.4	15.7	18.7	19.8	...
Gross government claims/total assets	21.5	21.6	22.3	22.2	21.7	...
FX deposits/total deposits	2.5	1.9	5.8	4.1	6.6	...
(Pre-tax) return/total assets	2.5	2.2	2.7	2.0	2.2	...
<b>External indicators</b>						
Exports of goods and services (percent change, 12-month basis in US\$)	4.4	-1.4	-5.7	10.4	7.2	5.5
Imports of goods and services (percent change, 12-month basis in US\$)	3.3	-4.9	-4.9	9.7	20.2	5.7
Current account balance	-5.7	-3.7	-7.5	-6.9	-10.5	-10.4
Capital and financial account balance	12.6	11.3	9.3	11.2	3.8	6.3
Gross official reserves (in US\$ millions)	484.4	707.0	683.2	751.7	595.2	472.5
Gross official reserves in months of imports of goods and services	3.7	5.7	5.8	5.8	3.9	2.9
Gross official reserves to short-term debt 6/ 7/	18.0	17.1	11.6	14.4	12.6	9.0
Broad money to reserves	3.3	2.4	2.9	2.6	3.9	5.2
Total public external debt service	2.9	2.8	3.7	4.1	3.8	3.5
Total external debt to exports of goods and services (percent)	45.2	59.0	61.4	55.9	54.7	49.5
External interest payments to exports of goods and services (percent)	3.9	3.5	4.3	3.9	3.9	3.8
External amortization payments to exports of goods and services (percent)	1.9	2.1	3.5	4.5	3.7	3.2
Exchange rate (per US\$, end of period)	2.0	2.0	2.0	2.0	2.0	2.0
REER 12-month basis (depreciation -)	6.0	-1.3	-5.3	-8.9	-3.9	...

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

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

2/ Fiscal data on a fiscal year basis, except for interest and amortization payments to fiscal revenue.

3/ Excludes the National Insurance Scheme.

4/ Spread between average lending and deposit rates, hence does not fully reflect intermediation margin.

5/ Average rate of discount.

6/ Refers to public external debt.

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

**Barbados—Fund Relations**  
As of May 31, 2005

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

II. <b>General Resources Account:</b>	<b>SDR million</b>	<b>Percent of Quota</b>
Quota	67.50	100.00
Fund holdings of currency	62.30	92.30
Reserve position in Fund	5.20	7.71

III. <b>SDR Department:</b>	<b>SDR million</b>	<b>Percent of Allocation</b>
Net cumulative allocation	8.04	100.00
Holdings	0.02	0.20

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):

	<b>Forthcoming</b>				
	<b>2005</b>	<b>2006</b>	<b>2007</b>	<b>2008</b>	<b>2009</b>
Principal	--	--	--	--	--
Charges/Interest	0.10	0.20	0.20	0.20	0.20
Total	0.10	0.20	0.20	0.20	0.20

V **Exchange Rate Arrangements:**

II.

The Barbados dollar has been pegged to the U.S. dollar since mid-1975 at BDS\$2.00 = US\$1.00. On May 15, 2005, the official buying and selling rates for the U.S. dollar were BDS\$1.98 and BDS\$2.04, 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 some 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 2004 Article IV consultation discussion was concluded by the Executive Board on May 5, 2004; the documents were Staff Report (Country Report No. 04/154) and Statistical Appendix (Country Report No. 04/153). Barbados is on the standard 12-month consultation cycle.

**IX. Technical Assistance (1994–2005):**

<b>Department</b>	<b>Dates</b>	<b>Purpose</b>
STA	Sep. 23, 2003–Sep. 22, 2005	Multisector statistics advisor
FAD	September 6–13, 2004	Tax policy
CARTAC	March 8–19, 2004	Regional BOP methodology course
CARTAC	January 26–30, 2004	Development of supply and use tables
FAD	July 3–18, 2003	Further reform of indirect taxes
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

In late 2002, an FSAP mission (joint Fund-Bank) assessed the Barbadian financial system.

**X. Resident Representative:**

The resident representative's post was closed in January 1995.

## Barbados—Relations with the Inter-American Development Bank

### I. Active Loans to Barbados as of June 17, 2005

(In millions of U.S. dollars)

Purpose	Approval Date	Amount	Amount Disbursed	Amount Available
Bridgetown roads	May. 1993	18.5	17.2	1.2
Solid waste management program	Oct. 1998	13.0	0.0	13.0
Education sector enhancement program	Dec. 1998	85.0	26.3	58.7
Administration of justice	Aug. 2001	8.8	0.5	8.3
Coastal infrastructure	Jan. 2002	17.0	0.1	16.9
<b>Total</b>		<b>142.3</b>	<b>44.1</b>	<b>98.2</b>

### II. Net Cash Flow of IDB Resources and Balance Outstanding

	1997	1998	1999	2000	2001	2002	2003	2004	2005 1/
Loan approvals	0.0	98.0	0.0	0.0	8.7	17.0	0.0	0.0	38.0
Repayments	7.3	7.5	8.1	7.3	7.3	8.1	11.0	13.8	12.1
Disbursements	15.1	17.9	5.8	10.4	24.2	15.8	16.0	7.9	7.5
Net loan flow	7.8	10.4	-2.3	3.1	16.9	7.7	5.0	-5.9	-4.6
Interest and charges	7.9	8.2	9.7	10.0	8.7	7.2	8.2	7.4	9.4
Net cash flow	-0.1	2.2	-12.0	-6.9	8.2	0.5	-3.2	-13.3	-14.0
Debt service	15.2	15.7	17.8	17.3	16.0	15.3	19.2	21.2	21.5
<b>Debt outstanding</b>	<b>133.5</b>	<b>143.9</b>	<b>141.6</b>	<b>127.0</b>	<b>143.9</b>	<b>151.6</b>	<b>156.6</b>	<b>150.7</b>	<b>146.1</b>

Source: Inter-American Development Bank.

1/ Provisional.

### Barbados—Relations with the Caribbean Development Bank

The Caribbean Development Bank (CDB) approved US\$224.4 million in loans, contingent loans, equity and grants to Barbados between 1970 and 2004. This represents 9.0 percent of total approvals to CDB's borrowing member countries.

Of the total funds approved US\$61.7 million or 27.5 percent were allocated to the productive sectors which comprise agriculture, manufacturing, tourism, and mining. Within the productive sectors, US\$45.5 million or 20.3 percent of the total was allocated to the manufacturing sector, while tourism accounted for US\$12.0 million, or 5.3 percent.

Economic infrastructure accounted for US\$112.9 million or 50.3 percent of approved funds. Of these funds, US\$52.4 million (23.4 percent) were allocated to the transportation, US\$55 million (24.5 percent) to the education, and US\$3.2 million (1.4 percent) to the health sectors.

Approximately US\$13.5 million in new loans (multi-sector) was approved in 2003 while no new loans were approved in 2004.

CDB Loans Approved to Barbados 1970–2004

Sector	US\$ million	Percent
<b>Productive sector</b>	<b>61.7</b>	<b>27.5</b>
Agriculture	4.2	1.9
Manufacturing	45.5	20.3
Tourism	12.0	5.3
<b>Economic infrastructure</b>	<b>112.9</b>	<b>50.3</b>
Power and energy	0.1	0.0
Water	0.8	0.4
Transportation	52.4	23.4
Housing	1.4	0.6
Education	55.0	24.5
Health	3.2	1.4
<b>Multisector</b>	<b>49.7</b>	<b>22.2</b>
<b>Total</b>	<b>224.4</b>	<b>100.0</b>

Source: Caribbean Development Bank.

## **Barbados—Statistical Issues**

1. The statistical information provided by Barbados is broadly adequate for surveillance purposes, although some important weaknesses remain. 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 Fund's Dissemination Standards Bulletin Board (DSBB) on the internet.

### **National accounts**

2. 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. To address some of these weaknesses, the authorities have scheduled a census of economic activity covering tourism, financial businesses, and transport and communications that should be initiated in June 2005. The Barbados Statistical Services (BSS) estimates the national accounts by expenditure based on selected surveys. Whereas the household survey yields a reliable estimate of aggregate consumption, the national accounts 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. The authorities are currently in the process of updating the weights to 2000 in order to facilitate comparison within the CARICOM area. National accounts are based on *SNA 68* as opposed to the updated *SNA 93*. Despite recent initiatives to update the consumer price index and the index of industrial production, potential misalignments in real estate prices are left unattended owing to the absence of a systematic index of property prices. The consumer price index uses an expenditure basket for 1998–99 for its July 2001=100 series introduced in January 2002. This is a welcome update on 1978 expenditure weights and given this infrequent basket change, comparisons of CPI data prior to 2002 with CPI data after 2002 should be undertaken with care. The index of industrial production is based on the sectoral weights prevailing in 1982. The authorities are currently working towards rebasing the series to 1994.

### **Nonfinancial public sector**

3. 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 the under-reporting of off-budget 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.

### **Financial sector**

4. 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 CBB classifies some loans to and deposits of non-residents 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 six weeks for the central bank accounts, and about ten 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 GDDS.

### **External sector**

5. Lags in the compilation of merchandise trade data limit the timeliness of estimating the external current account balance, in particular, information on the activities of offshore sector. Estimates of the components of the financial account also need to be strengthened. Quarterly balance of payments estimates are no longer provided.



**BARBADOS: TABLE OF COMMON INDICATORS REQUIRED FOR SURVEILLANCE**  
AS OF JUNE 15, 2005

	Date of latest observation	Date received	Frequency of Data <sup>6</sup>	Frequency of Reporting <sup>6</sup>	Frequency of publication <sup>6</sup>
Exchange Rates	Fixed				
International Reserve Assets and Reserve Liabilities of the Monetary Authorities <sup>1</sup>	3/31/05	4/29/05	M	M	W
Reserve/Base Money	3/31/05	4/29/05	M	M	M
Broad Money	2/28/05	4/29/05	M	M	M
Central Bank Balance Sheet	3/31/05	4/29/05	M	M	M
Consolidated Balance Sheet of the Banking System	3/31/05	5/25/05	M	M	M
Interest Rates <sup>2</sup>	2/28/05	4/29/05	M	M	M
Consumer Price Index	3/05	6/05	M	M	M
Revenue, Expenditure, Balance and Composition of Financing <sup>3</sup> – General Government <sup>4</sup>	12/31/04	2/8/05	Q	Q	Q
Revenue, Expenditure, Balance and Composition of Financing <sup>3</sup> – Central Government	12/31/04	2/8/05	Q	Q	Q
Stocks of Central Government and Central Government-Guaranteed Debt <sup>5</sup>	12/31/04	2/8/05	Q	Q	Q
External Current Account Balance	12/03	3/3/05	A	A	Q
Exports and Imports of Goods and Services	12/04	2/25/05	A	A	M
GDP/GNP	2004	3/3/05	A	A	Q
Gross External Debt	12/04	3/3/05	A	A	M

<sup>1</sup> Includes reserve assets pledged or otherwise encumbered as well as net derivative positions.

<sup>2</sup> Both market-based and officially-determined, including discount rates, money market rates, rates on treasury bills, notes and bonds.

<sup>3</sup> Foreign, domestic bank, and domestic nonbank financing.

<sup>4</sup> The general government consists of the central government (budgetary funds, extra budgetary funds, and social security funds) and state and local governments.

<sup>5</sup> Including currency and maturity composition.

<sup>6</sup> Daily (D), Weekly (W), Monthly (M), Quarterly (Q), Annually (A); Irregular (I); Not Available (NA).



INTERNATIONAL MONETARY FUND

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August 15, 2005

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Washington, D. C. 20431 USA

## **IMF Executive Board Concludes 2005 Article IV Consultation with Barbados**

On August 5, 2005, the Executive Board of the International Monetary Fund (IMF) concluded the Article IV consultation with Barbados.<sup>1</sup>

### **Background**

Barbados compares favorably with other Caribbean countries on economic and social indicators. The economy is heavily dependent on tourism and financial services. The population is about 272,000, and per capita income (on a PPP basis) is about US\$15,700. Poverty rates are the lowest in the Caribbean. Social indicators compare favorably in both a regional and global context; in 2004, for example, Barbados was ranked 29<sup>th</sup> among 177 countries on the United Nations Development Program's Human Development Index.

Barbados was one of the better-performing economies in the Caribbean in the 1990s. During 1993–2000, Barbados grew at 3 percent, inflation was less than 2 percent, and public sector deficits were maintained at less than 3 percent of GDP.

The economy—especially the tourism and financial services sectors—suffered a sharp recession in 2001–02 following the September 11<sup>th</sup> attacks and the global slowdown. In response to the deterioration in the external environment, the government implemented a public investment program to help revive economic activity. Combined with public sector wage increases, this contributed to a widening of the overall nonfinancial public sector fiscal deficit

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<sup>1</sup> 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.

from about 2 percent of GDP in FY 2000/01 to about 13 percent of GDP in FY 2002/03. As a result, the public sector debt-to-GDP ratio rose from 74 percent in March 2001 to 87 percent in March 2003. The external current account deficit remained at around 6 percent of GDP over 2001–03.

A strong economic recovery appears to have taken hold in 2004. Real GDP growth in 2004 is estimated at 4.4 percent, led by a recovery in tourism, construction, and communications. The public sector deficit fell to 6½ percent of GDP in FY 2003/04 and 6 percent of GDP in FY 2004/05 as capital expenditures declined from their high levels of the previous years. Following the rebound in economic activity and a reduction in mortgage lending rates, growth in credit to the private sector—especially to households—accelerated in 2004. Private sector credit grew by almost 17 percent during 2004, reflecting strong demand for mortgages. Higher personal incomes of households also spurred private credit growth. Base money declined, however, owing to the resulting from the decline in commercial banks excess reserves. The banking sector appears to be sound and financial sector indicators have improved with the pickup in economic activity.

The external current account deficit rose from 7 percent of GDP in 2003 to 10½ percent of GDP in 2004, reflecting a broad-based import surge related to the rapid increase in private sector credit and the expansion in economic activity. Capital inflows also declined with the cessation of privatization receipts from abroad. As a result, the balance of payments moved from a surplus to a deficit of 5½ percent of GDP in 2004, with gross international reserves (GIR) falling to 3¾ months of imported goods and nonfactor services.

Structural reforms have advanced in taxation, telecommunications, and the public enterprise sector. Corporate and personal tax rates have been further lowered, in line with the multiyear reduction in these rates initiated in FY 2002/03. In telecommunications, the final phase of reform began in early 2005, and will involve the liberalization of external telecommunications and the issuance of new licenses for fixed telephone lines on a competitive basis. Legislation to corporatize the Airport Authority was also recently approved

### **Executive Board Assessment**

Executive Directors observed that based on a recovery in tourism, construction, and communications, Barbados recorded stronger economic activity and low inflation in 2004. Directors noted that growth prospects for the next three years remain favorable, reflecting the positive global environment and the boost to growth from the buildup to the 2007 World Cup cricket games. At the same time, Directors underscored that a key challenge in maintaining and sustaining strong economic growth going forward will be to address macroeconomic imbalances, including a high level of public debt, large fiscal and external current account deficits, and declining international reserves.

Directors observed that the expansionary public investment program, implemented to revive the economy after the recession of 2001–02, contributed to raising Barbados' public debt to a level far exceeding the average for Latin America and the Caribbean. While welcoming the efforts to reduce the public sector deficit over the past two years, they noted with concern that the primary

deficit remains among the highest in the region and that public debt will rise steadily in the absence of fiscal consolidation. Against this background, they cautioned that the injection of fiscal stimulus in FY 2005/06, in the midst of a robust private-sector led recovery, could make the path to debt reduction more difficult. Directors therefore urged the authorities to seize the opportunity provided by the external economic environment to reduce the fiscal deficit decisively, thereby placing public debt on a firmly declining path and building a fiscal cushion in the event of negative shocks. Directors noted that faster fiscal consolidation will also help strengthen the external reserve position, without overburdening monetary policy, while allowing credit to be channeled to the private sector to support growth.

Directors welcomed the government's plan to reduce public expenditure over the medium term. Most Directors recommended that the authorities complement these efforts with revenue measures, as well as a rationalization of the tariffs of major public enterprises, with a view to reducing subsidies to these entities. Directors were encouraged by the authorities' preparation for the implementation of output-based budgeting within a medium-term framework, which is expected to improve budget formulation. While welcoming the authorities' efforts to promote private-sector participation in the provision of economic infrastructure and services, Directors cautioned that expenditure commitments associated with these activities should be carefully monitored and accounted for in budget documents. To assist their efforts to improve fiscal transparency, a few Directors recommended that the authorities consider requesting a fiscal Report on the Observance of Standards and Codes.

Directors supported preserving Barbados' fixed exchange rate regime, noting its positive role as an anchor for price stability and investor confidence. They emphasized, however, that going forward, the exchange rate peg will need to be supported by sound policies aimed at addressing the recent macroeconomic imbalances. Directors also stressed the need to strengthen competitiveness by tightening the link between wage increases and developments in labor productivity, as well as accelerating productivity growth through structural reform.

Directors welcomed the recent steps to slow the growth of credit, and recommended further tightening to help arrest the decline in foreign reserves. Directors encouraged the authorities to make greater use of indirect monetary policy instruments and enhance competition in the banking system. They noted that this would facilitate the gradual phasing out of the minimum deposit rate and improve the efficiency of financial intermediation. Directors noted that while the banking sector appears well poised to absorb shocks, risks related to the large share of public debt held by domestic financial institutions will need to be monitored carefully. Directors were encouraged by the progress made in addressing the outstanding issues from the Financial Sector Assessment Program report of 2002, and called for strengthened efforts to curb money laundering and the financing of terrorism.

Directors underlined the importance of structural reforms to encourage foreign direct investment, improve competitiveness, and enhance Barbados' long-term growth potential. They welcomed the significant progress that has already been made in some areas, including the reduction in corporate tax rates, telecommunications reform, and the corporatization of the airport. They welcomed the authorities' focus on reforms relating to tax policy and privatization, as well as their continued commitment to further trade and capital account liberalization within

the context of the Caribbean Single Market and Economy initiative and the envisaged Free Trade Area of the Americas. Key areas for further reforms include the removal of import and export licenses; reform of the sugar sector; restructuring or privatization of the public enterprises that do not meet public policy objectives; and enhanced labor market flexibility. Directors also urged the authorities to rationalize costly fiscal incentives to investment.

Directors observed that statistical information provided by Barbados is broadly adequate for surveillance purposes, but noted the need to strengthen the quality, coverage, and timeliness of data for the public enterprises and the capital account of the balance of payments

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### Barbados: Selected Economic Indicators

	2000	2001	2002	2003	2004
(Annual percentage changes)					
<b>Output and prices</b>					
Real GDP	2.3	-2.6	0.5	2.0	4.4
Consumer prices (12-month increase)	2.4	2.8	0.2	1.6	1.4
Tourist arrivals	5.8	-6.9	-1.8	6.7	3.8
Unemployment (percent of labor force)	9.4	9.9	10.3	11.0	9.6
<b>Money and credit 1/</b>					
Net domestic assets	-4.2	-8.6	5.7	0.8	25.2
Public sector credit (net)	-4.3	-8.1	12.2	3.6	4.1
Private sector credit	2.1	-0.3	2.4	0.6	11.0
Broad money	7.9	5.6	10.4	6.5	16.4
(In percent of GDP)					
<b>Public sector operations 2/</b>					
Nonfinancial public sector balance	-2.2	-4.7	-12.8	-6.4	-5.9
Central government	-1.3	-4.7	-11.6	-5.4	-3.5
Public enterprises	-0.9	-0.0	-1.2	-1.0	-2.4
Public debt 3/	74.1	82.9	86.9	85.0	86.1
<b>External sector</b>					
External current account balance	-5.7	-3.7	-7.5	-6.9	-10.5
Public external debt 3/	22.6	29.1	29.5	27.2	27.4
Gross international reserves (in millions of U.S. dollars)	484	707	683	752	595

Sources: Barbadian authorities; and IMF staff estimates.

1/ Changes in percent of beginning-of-period broad money.

2/ Fiscal years (April–March). Excludes operations of the National Insurance Scheme.

3/ Refers to central government and government guaranteed debt.