

**Statement by Thomas A. Bernes, Executive Director
for St. Vincent and the Grenadines
November 10, 1999**

1. On behalf of my Vincentian authorities, I would like to express my thanks to the mission chief, Mr. Rennhack, and his team for a helpful and informative consultation. My authorities appreciated the mission's constructive advice and the degree to which staff's assessment took into account the unique challenges faced by small-island economies. This "more nuanced" approach -- particularly with respect to civil-service reform and land holding -- was a welcome evolution in the ongoing dialogue between St. Vincent and the Grenadines and the IMF.
2. The authorities are in general agreement with the content of the staff report. I will therefore offer only a few comments and clarifications.
3. On the **macroeconomic** front, there is not much to add to staff's analysis. A word is probably warranted, however, with respect to what might appear at first glance to be a large current account deficit (about 15 percent in 1997-98). As staff note, exports suffered from adverse terms of trade developments and from pests on agricultural exports. The country's mango production was affected as were some root crops. Remedial action is well underway but there is likely to be a loss of access to the U.S. market for a period of up to three years. This is truly a regrettable development but it is worth noting that, as farmers begin to adopt more advanced agricultural practices like the use of greenhouse technologies (which are being actively promoted by the Government), the incidence of such infestations will be significantly reduced.
4. At the same time, Directors should be aware that the current account deficit is well financed, with concessional resources representing a significant component of the financing. This situation is likely to persist since a significant portion of STABEX grants from the EU have yet to be disbursed and, as staff note, official data likely understate receipts from tourism and the fishing sector. On the former, current data on tourism are based on an expenditure survey that is five years old. Given developments in the tourist industry since then, it is likely that per visit expenditure has increased substantially. The authorities acknowledge the need to undertake a new survey of spending patterns in the period ahead.
5. Staff have raised questions about the **budgeting process** -- in particular, the fact that actual expenditures have significantly undershot budgeted expenditure. To improve the situation, the authorities accept the need to strengthen the reporting requirements of public enterprises (although it should be noted that the largest public enterprises provide data in a timely manner). They note, as well, that actual capital expenditures are higher than recorded

on account of the disbursement of some donor funds directly to suppliers and contractors. Shortfalls in recorded expenditures are also partly due to uncertainties with the *pace* at which capital projects are implemented. While not condoning such deviations from budget, it should be noted that actual outcomes consistently *undershoot* targets, which is certainly preferable to the more-often witnessed situation of budget overruns! Directors may be interested to note that, with assistance from the Canadian International Development Agency (CIDA), projects have been launched to address weaknesses in financial management and budgeting.

6. In the context of an evolving global economy, no discussion of a small Caribbean island economy would be complete without attention being paid to the question of **economic diversification**. As many of its neighbors, St. Vincent and the Grenadines faces daunting challenges on a number of fronts. These include the erosion of agricultural preferences, periodic pest infestations of important agricultural crops, and civil-service capacity constraints. The situation is further complicated by the telecommunications monopoly position held by Cable and Wireless – a legacy of past administrations – that constrains St. Vincent’s ability to take full advantage of the opportunities provided by an increasingly globalized economy. It is in no small measure due to the determination of the authorities to maintain a stable and sound macroeconomic environment and to be proactive in policy making that St. Vincent and the Grenadines has been as successful as it has. Success in developing the tourism sector – where a single major project can have an enormous impact on GDP – is particularly noteworthy. However, as staff point out, and as the authorities fully appreciate, serious challenges remain.

7. Among the questions to be resolved is that of **airport expansion**. Currently, St. Vincent and the Grenadines lacks airport facilities capable of handling jet aircraft. This is problematic as it limits the extent to which St. Vincent can take advantage of charter carriers, bringing tourists to the region directly from major centres like Chicago, Toronto and New York. Other productive sectors, including fishing, manufacturing, informatics and the offshore financial sector are also affected by limitations on the existing facilities. However, as staff indicate, options are complex and many of them prohibitively expensive. That being said, the authorities record for fiscal prudence can be counted on to ensure that whatever decision is eventually taken, the fiscal consequences will be kept well within the Government’s ability to pay.

8. The authorities continue to regard development of the **offshore sector** as a key pillar of their diversification strategy. They remain fully cognizant of their responsibilities to assist the international effort to combat money laundering and, within their own internal resource constraints, have strengthened supervisory capacity. With respect to “harmful tax competition” concerns, the authorities are awaiting a clearer indication of the outcome of OECD efforts in this area. They remain concerned that – at a time when other avenues of economic diversification are being closed to them on account of telecommunications monopolies and trade disputes -- efforts in this direction may fall victim to excessive zeal on the part of some industrial countries to turn OFCs into “tax collectors” for industrial countries. As noted, they accept their responsibility as it pertains to illegal activities but

underline the fact that “tax avoidance” is not illegal (as is tax “evasion”). Nevertheless, they continue to cooperate with the OECD as it addresses issues of tax competition associated with the offshore sector.

9. Among the efforts made by the Government to develop and diversify the economy, staff list the extension of “public guarantees of private external debt”. As noted by staff, and as a result of a few serious and expensive past missteps with this vehicle (most notable being the Ottley Hall project), the authorities have *no intention* of extending such guarantees in the future. They would also hope that their experience will provide a cautionary note to other governments contemplating resort to such guarantees.

10. Staff have concerns with the degree of “discretion” in granting **tax or import duty exemptions** or in approving **foreign direct investment** projects. On the former, the authorities agree there is some scope to improve transparency, particularly by simplifying the range of incentives. With respect to foreign direct investment, the difficulty in establishing rigid rules on this front for a small island economy are well known given the potential for even a single FDI project to significantly affect land prices and alter the environmental landscape. That being said, all major decisions on FDI are taken by the full Cabinet.

11. Staff note that “price controls distort consumption and production patterns”. While this is clearly true in a “theoretical” sense, the question of the *degree* of distortion is key since the controls could be a second-best solution to an existing market imperfection. Indeed, small island economies are notable for the extent to which market imperfections exist. There is indeed scope to simplify the system of price controls, but the authorities see little evidence that any of the existing controls are binding enough to seriously distort consumption and production patterns.

12. With respect to the **financial sector**, the authorities share staff’s concern with the relatively high level of NPLs and are working with the ECCB and the banks in question to address the situation. A significant portion of the value of NPLs is accounted for by a single loan, for which the National Commercial Bank (NCB) believes that it can recoup a significant portion of the loss from the sale of the associated assets.

13. In terms of the issues staff raise with respect to the adequacy of the ECCB regulatory and supervisory framework, it should also be noted that officials of the ECCB requested an FSSA from MAE staff during last month’s Annual Meetings. They are still awaiting a positive response from the Fund and would welcome any encouragement Directors could provide to staff to ensure this is undertaken in the not-too-distant future.

14. Staff have provided an accurate description of the authorities plans for the NCB. The authorities have also undertaken measures to level the playing field with private banks, in particular, by permitting the NCB to charge a market rate on government overdrafts and by extending the one percent deposit levy currently paid by private-sector commercial banks to the NCB. The authorities also plan to establish a national development bank (on a modest scale). This is partly intended to permit the NCB to get out of the development loan business

and concentrate on strictly commercial lending. Development loans, by their very nature, are of longer maturity and their successful use requires the provision of specific business-related technical assistance to borrowers, neither of which the NCB has a comparative advantage in providing.

15. Finally, I am pleased to note that St. Vincent and the Grenadines is a participant in the pilot project on the release of Article IV staff reports.