



2013

**Eastern Caribbean Currency Union
Economic Review**



Presented by
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Realism and Hope: Moving Towards Our Development Goals

Before I commence tonight's presentation I would first like, on behalf of the Board of Directors, Management and Staff of the Bank, to express our heartfelt sympathies to the people of St Vincent and the Grenadines, Saint Lucia and the Commonwealth of Dominica, who were unfortunately affected by severe weather during the Christmas season. Our thoughts are particularly with the families who have lost loved ones or suffered injuries. The monetary cost of the damage, as a percentage of GDP, is tremendous and comes at a time when the countries can least afford it.

However, resilience and fortitude are long standing components of the fabric of our people and we are confident that we will individually and collectively rise again like the proverbial phoenix from the ashes of this latest catastrophe. The following quotation from Napoleon Hill should give us further encouragement: "Every adversity, every failure, and every heart break carries with it the seed of an equivalent or greater benefit".

It is by now evident that the year 2013 was another challenging year for the Currency Union. Our member countries are still grappling with low economic growth, persistent fiscal deficits, rising debt levels, high unemployment and poverty rates and some fragility in the financial sector. Once again the structural characteristics of our countries, namely, small size, extreme openness and high vulnerability to external shocks and natural disasters have become more evident.

Economic and financial developments in the ECCU continue to be shaped by the global economic environment which is still uncertain, with growth for 2013 likely to be lower than previously anticipated. In the USA, our main trading partner, a major contributor to the slowdown was the fiscal policy stance of the Federal Government and the political gridlock which had adverse effects on business and consumer confidence, despite the uptick in the housing market and the easing of credit conditions. In Europe, uncertainties persisted and unemployment rates remained elevated, while in the emerging economies there was a slowing down in economic activity.



Closer to home, we would like to bring to your attention the fact that 2013 marked the 30th anniversary of the establishment of the ECCB. One of our main achievements over this period was the maintenance of currency and financial sector stability, as mandated in the ECCB Agreement.

This presentation will focus on three main areas:

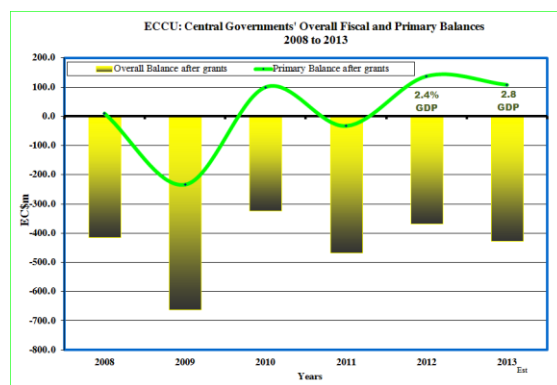
1. Economic developments in 2013;
2. The main challenges; and
3. The top priorities in the near to medium term.

Economic Developments in 2013

Preliminary data indicate that economic activity in the ECCU expanded at a modest pace of 0.7 per cent in 2013, building on the marginal growth of 0.2 per cent achieved in 2012, which reversed the negative growth trends experienced since 2009. The increase in economic activity was primarily driven by improved performances in agriculture, construction and tourism. The construction sector expanded by 2.9 per cent following a 4.3 per cent decline in 2012, as public sector construction gained momentum. In the tourism industry, value added is estimated to have increased by 0.4 per cent due to improvements in major source markets and more intense marketing efforts. However, this rate was lower than the 1.4 per cent growth recorded in 2012.

The consolidated fiscal position of the Central Government is provisionally estimated to have deteriorated in 2013 as the growth in expenditure outpaced revenue collections. An overall deficit of approximately \$427.3m (2.8 per cent of GDP) was recorded compared with one of \$367.3m (2.4 per cent GDP) in 2012. The deterioration in the overall deficit position reflected the increase in capital expenditure while current expenditure decreased.

In its October 2013 World Economic Outlook (WEO) the IMF forecasted that world output would expand by 3.6 per cent in 2014. The economies of the USA, the UK and Canada are forecast to grow by 2.6, 1.9 and 2.2 per cent respectively in 2014. Against the backdrop of the positive signs in the global economy but cognisant of the recent setback in some of our countries, real economic activity in the ECCU is projected to increase by 1.9 per cent in 2014. The expansion



in economic activity is expected to be supported by higher levels of output in the construction; hotels and restaurants; wholesale and retail; and transport, storage and communications sectors. This level of growth is however still below the target growth rate of 3.0 to 5.0 per cent, established by the Monetary Council as the rate needed to transform the economies, and is unsustainable given the prominence of the non-tradable sectors as the contributors to growth.

The Main Challenges

It may be safe to say that never before has the Currency Union witnessed such a prolonged period of economic stagnation.

In looking ahead there are three possible scenarios which confront the Currency Union and will weigh heavily on the decisions to be taken. They are:

1. The global economy remains in its relatively low growth, high unemployment mode, particularly in our main trading partners while the ECCU countries continue with their current policies;
2. Economic activity in the global economy does not return to its pre-crisis levels while the ECCU makes significant policy adjustments; and
3. The global economy goes through substantial restructuring and rebalancing and the ECCU undergoes significant socioeconomic transformation.

These scenarios imply major policy choices for the ECCU countries which have related outcomes. Four possible outcomes can be identified from the economic history and contemporary experience of nation states since the process of decolonisation following the Second World War. They are:

- Failed or failing states
- Barebones survival
- Moderate progress and
- Socioeconomic transformation

The obvious choice for us is of course, socioeconomic transformation, but this is a long term goal and requires resolute focus on a medium to long term strategy and the political commitment and social consensus to get there.

We must have a vision of what we want and a systematic, pragmatic and adaptable strategy for achieving our goals. That means that our goals must be clear and measurable with emphasis on

- An attainable and sustainable growth rate;

- A higher level of employment in quality jobs;
- Poverty reduction; and
- Maintenance and improvement of the Human Development Indices.

The Top Priorities in the Near to Medium Term

In the medium term, the top priorities for the region are:

- maintaining a stable currency by implementing policies and programmes aimed at high, sustained and balanced economic growth and development;
- continuing efforts at prudent debt management and fiscal reform; and
- enhancing the resilience of the financial system.

The new Economic Union Treaty gives us the framework within which we can successfully address our fundamental challenges. However, there is an increased urgency for implementation, given the obvious and glaring vulnerabilities we have recently experienced through the global crisis and the disastrous rain storms. Indeed, with respect to natural disasters, the uncomfortable reality is that they are now almost predictable. The only thing that is unpredictable is which country they will hit and when!

The Economic Union will help us to address one of our fundamental challenges, that of critical mass and scale. The new Treaty has created what can be referred to as an Eastern Caribbean State Nation which can be defined as "A grouping of separate sovereign states which pool their sovereignty and resources and coordinate their policies as an instrument for collective decision making and action to achieve the goals of socioeconomic development". This new arrangement allows us to contemplate a new economic model in the OECS based on the following premises:

- aggregation of resources
- coordination of policies
- increase in the quantity, quality, and competitiveness of production and output.

Three agents are vital to the success of this model, the state or government, the private sector and the financial sector.

The State

The state has a very important role to play in this new dispensation but it must be complemented by the activities and performance of the private sector and the financial sector. The concept of the developmental state would seem to be the nature of the role the government must play in our circumstances, and as such should:

- provide an efficient and effective system of justice, law and order;
- provide critical public services in health, education and social welfare;
- regulate the economy; and
- actively promote economic growth and development that is equitable and sustainable.

The fundamental problem facing governments in small, developing states such as ours is the absolute cost of government. With relatively small tax bases and the need to provide basic services, these states have serious fiscal challenges. The objective of such states must therefore be to operate low cost and highly efficient and effective administrations. In the case of the OECS member states we have several options as provided for in the Economic Union treaty. A significant possibility is to have a concentration of core functions at the national level and outsource several functions at the regional and local levels. For this, the treaty provides for:

- supranational arrangements,
- functional cooperation and
- the development of an effective and appropriate system of local government.

The treaty implies that there will be a dual system of government and governance which could lead to a more efficient, effective, lower cost and coordinated system of government.

The Private Sector

A dynamic and innovative private sector is absolutely vital to our development. The current situation is that the structure of the private sector does not lend itself to performing a major role in the development process. Based on census and survey data the private sector is currently two-thirds informal and one-third formal and concentrates its activities primarily in the wholesale, retail, real estate, construction, and services sectors. These sectors are referred to as the non-tradable activities as opposed to the export-oriented or tradeable ones. This ratio needs to be reversed so that a new private sector can emerge which can contribute significantly to economic growth and development.

For this process to be carried out a deliberate effort to develop the private sector should commence with the full involvement of the most enterprising elements of that sector. The process must concentrate on the development of firms, industries and markets.

One needs once again to stress the factor of critical mass. Each industry, generally speaking, has to reach a critical minimum size to be competitive and to provide the linkages which would contribute to its success. An interesting example was the development of the banana industry in the Windward Islands which focused on critical mass, research and development and transportation and marketing efficiencies. This gives us a very good idea of how to start a successful industry. We therefore have to do the following:

- Negotiate market access;
- Have a competitive product;
- Be able to differentiate the product or move to entirely new products as the market environment changes.

There must be a systematic programme for the development of a viable and innovative private sector in our countries. Without this most of our important business enterprises in the traditional sectors will be sold off to regional or foreign interests, others will cease operations as the founders pass from the scene; and the current age of internet buying will finish off the rest.

The private sector itself should be organised and represented at the sectorial level, for example agriculture; and at the national and the OECS levels. This organisational system and structure should facilitate the development of industry sectors through -

- a) better representation for interfacing with governments and other important institutions - nationally, regionally and internationally;
- b) research activities to facilitate effective advocacy, product improvement and marketing; and
- c) the provision of technical assistance to the sector as a whole.

At the governmental level, agencies such as Offices of Private Sector Relations (OPSRs), Investment Promotion Agencies (IPAs), Bureaux of Standards, Air and Seaport Authorities and Community Colleges are all critical to private sector development.

The private sector representative bodies must themselves also look to the region and the international community for willing partners. These partnerships are crucial for the transfer of technology, investment opportunities from joint ventures, and the absorption of business and management practices.

It is very encouraging to know that a group of private sector individuals representing various sectors has taken up the challenge and are in the process of establishing an OECS Business Council which will have as its objective the transformation of the private sector in our



Governor, ECCB (first from left) with the Interim Board of Directors of the OECS Business Council

jurisdiction. An interim executive under the chairmanship of Ms Lilian Piper of the Commonwealth of Dominica is hard at work on this initiative.

The Financial Sector

The financial sector is the third major domestic agency which has an important role to play in our economic development. This sector has been seriously impacted by the global crisis but this has given us the opportunity to review it in its entirety and we are now very advanced in a systematic process of restructuring.

We have carried out a major diagnostic study of the sector and the Monetary Council has approved a Resolution Strategy which is now being implemented with technical assistance from the World Bank and the IMF. This strategy has three components: stabilisation, consolidation, and development of the financial system in the ECCU.

With respect to stabilisation, a comprehensive review of the operational and balance sheet status of the banks is being undertaken and will be followed up by further reviews by the IMF and the World Bank. Revisions to the current Banking Act and relevant sections of the ECCB Agreement are also being undertaken.

The fragmented state of the financial sector which comprises 40 commercial banks, 61 credit unions, and 161 insurance entities, for a population of approximately 600,000, is not appropriate for the sustainability of the sector and poses significant risks. Therefore a systematic process of amalgamation and consolidation is necessary to reduce and mitigate the risks and increase the viability of the firms in this sector.

The continued development of the financial sector is vital to the growth process. The need for financial resources in sufficient quantities and with the appropriate terms and conditions is a challenge which we must address through the restructuring and development of the sector.

The ECCB has initiated this process with the establishment of such critical regional institutions as the Eastern Caribbean Securities Exchange and the Eastern Caribbean Home Mortgage Bank which have made major contributions to the system.

At the national and traditional levels, the amalgamation and consolidation of the commercial banks, development banks, insurance companies and credit unions will provide the critical mass for mobilisation and allocation of financial resources at lower cost.

Taken as a whole, the evolution of effective and efficient money and capital markets through these structural and institutional arrangements will significantly improve access to financing for a new and innovative cadre of entrepreneurs.

In conclusion, it has become clear that much more coordinated efforts at both the national and OECS levels need to be the hallmark of our policies in the coming year. We must enlarge our perspectives to realise that while there is a lot to be done within our borders, we will not succeed if we do not combine our efforts across our countries. This is one of the stark realities we must face for in this lies our hope for sustained and equitable development.

I end with this quotation from Thomas F Buxton: "With ordinary talent and extraordinary perseverance, all things are attainable".

