



ECLAC Subregional Headquarters for the Caribbean

Fiscal Consolidation with Medium term growth in the Caribbean

**Mr. Dillon Alleyne
Economic Affairs Officer, ECLAC**

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Outline

- Conceptual issues
- The Impact of the crisis
- The fiscal and balance of payments situation
 - Current account and fiscal balances
 - Trade in goods and services
 - The capital and financial account
- Growth prospects for 2010
- The way forward



Conceptual Issues

- Two perspectives on the expanding CA of the BOP and fiscal balance.
 - Static Mundell-Fleming (1962,1963) approach: budget deficits causes the current account deficit
 - Ricardian Equivalence (1974,1989): relationship between the budget deficit and current account is weak
- The hypothesis suggested is that causation runs from the current account to the fiscal deficit
 - Reorientation of trade rules under the WTO from the 1980's which removed trade preferences made many activities uncompetitive.
 - Lower FDI and other foreign exchange inflows, plus weak private sector response forced govt. to act
- In examining the cost of the crisis, the Caribbean was unprepared relative to economies in LA.



Table 1: Consolidated Impact of the Global Recession in 2009 on the Economies of the Caribbean

	Real GDP (percent)	Tax Revenue (percent GDP)	Foreign Exchange Receipts (percent GDP)	Summary Impact (percent GDP)
Antigua and Barbuda	-7.3	-4	-15.4	-26.7
Bahamas	-5.1	-1.2	-7.8	-14
Barbados	-4.6	-2.4	-2	-9.1
Belize	-3.4	0	-10.3	-13.7
Dominica	-0.3	0.2	-4	-4.1
Grenada	-7.9	-2.9	-8.9	-19.7
Guyana	2.1	0.8	-4.5	-1.6
Jamaica	-3.4	0.5	-5.9	-8.8
St. Kitts & Nevis	-6.2	-3.7	-6	-15.9
St. Lucia	-5.9	-0.1	-4	-10
St. Vincent & the Grenadines	-3.2	-1.3	-5.5	-10
Suriname	0.7	0	-8.7	-8
Trinidad & Tobago	-3.5	0	-23.4	-26.9
Caribbean^b	-3.7	-1.3	-8.2	-13.2

Trend generated using the Hodrick- Prescott filter



Impactcont'd

- **Observations**
 - **With respect to GDP, the losses were greater for service producers relative to primary commodity producers and manufacturers.**
 - **Most of the losses came through the foreign exchange route (FDI, remittances and export earnings)**
- **Responses**
 - **Fiscal stimuli within the context of limited fiscal space (Bahamas, Barbados and Jamaica)**
 - **External financing from the IMF and the IDB**
 - **Eight Point Stabilization and Growth Programme in the ECCU. The only sub-regional approach to the crisis in the Caribbean.**

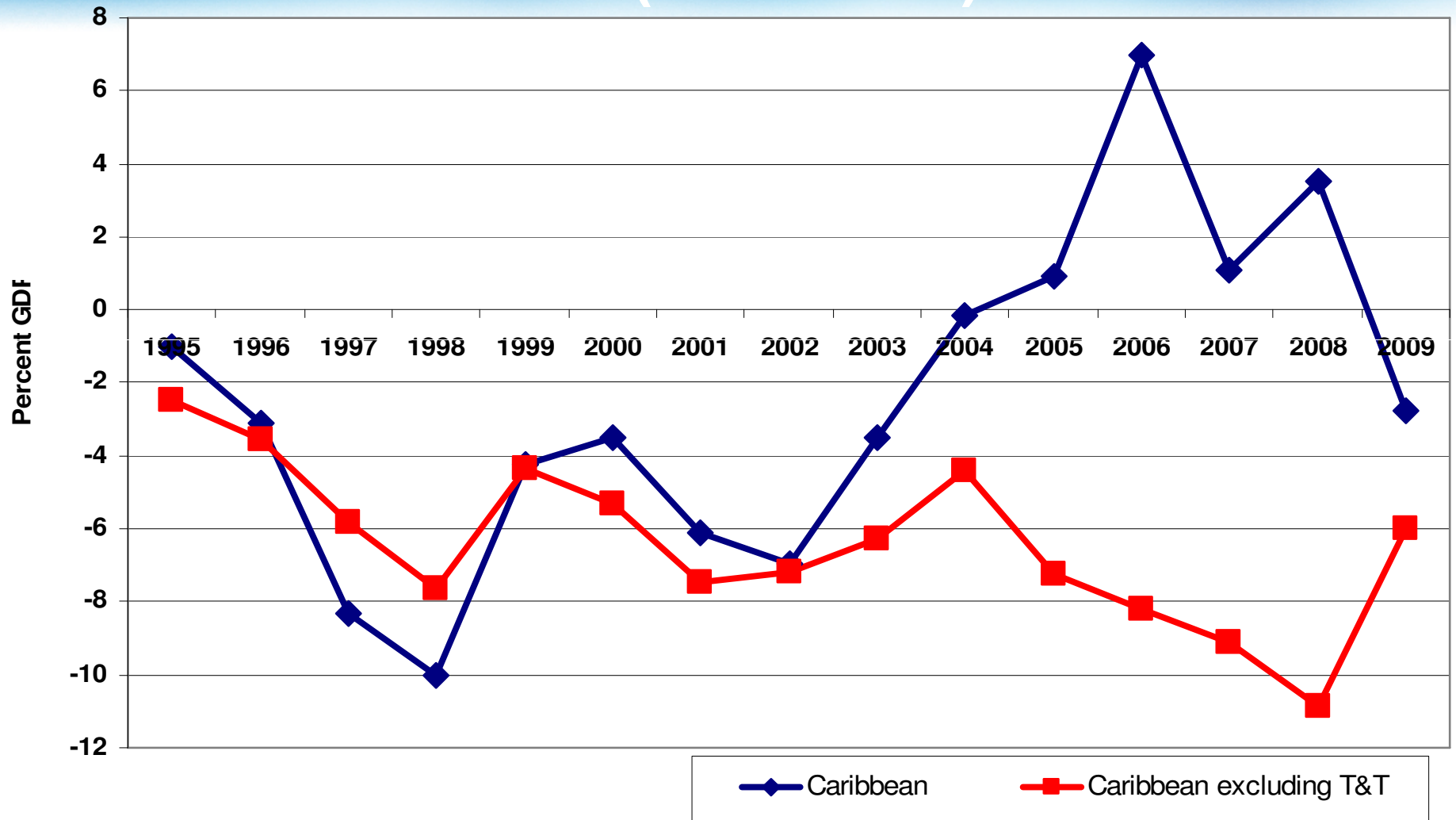


Current account and fiscal problems

- In light of limited fiscal space, high debt and growing CA balances –policy makers see the crisis as a short run problem of fiscal excess. The response has been attempts to improve revenue collection, lower expenditure mostly through the capital budget, and impose fiscal rules to address the problem.
- It is suggested that the origin of the problem lies in the deterioration of the CA balance of a number of countries with the exception of Trinidad and Tobago and Guyana until recently.

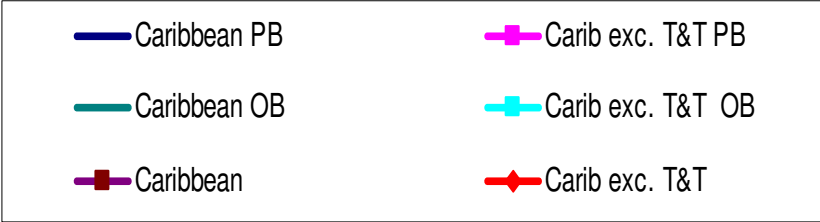
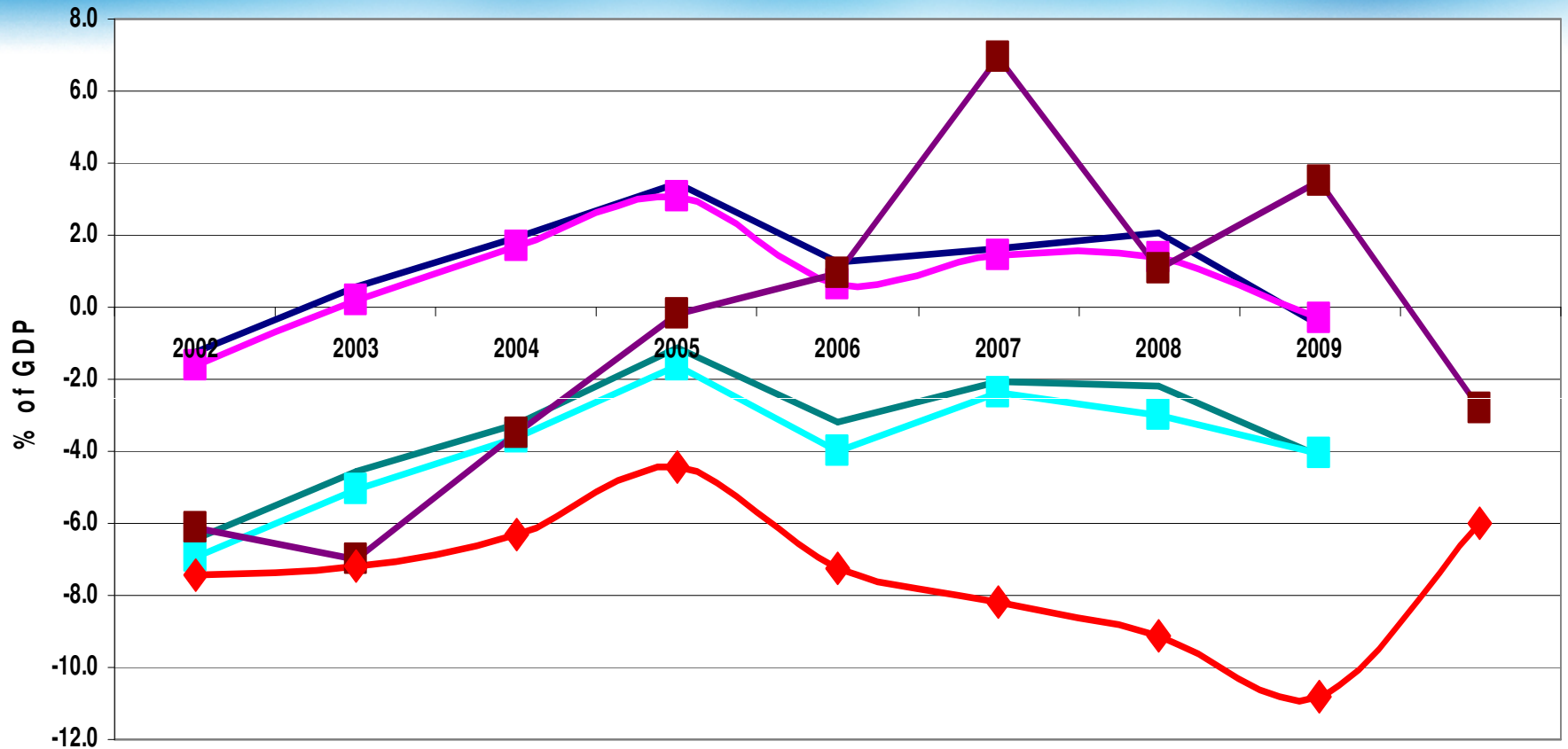


Current account balance, 1995-2009 (% of GDP)





Primary and Overall Balance as % of GDP ,and the Current Account Deficit for the Caribbean with and Without Trinidad and Tobago



Source: ECLAC based on official data



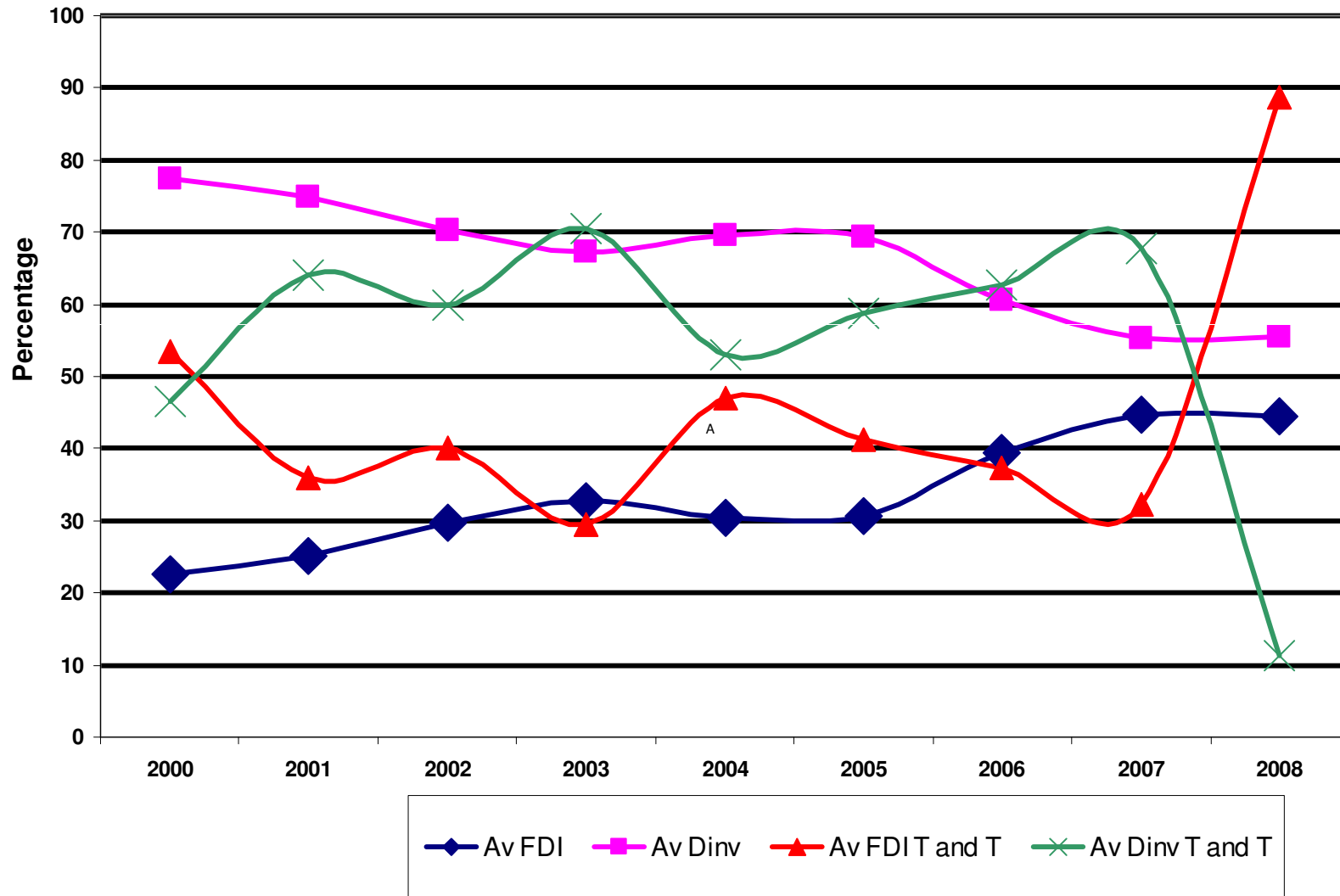
Causality and other evidence

The preliminary results from Granger causality tests showed that the CA deficit Granger-caused the OB deficit and not vice versa. This makes counter-cyclical fiscal policy difficult. Other evidence...

- Domestic Investment as a share of GFCF decline after 2005. S. Roache(2006) showed that PDI declined between 1988-2004.
- The fiscal stance was consistently in excess of the export performance ratio.
- Real public expenditure was either constant or trending up in the Caribbean.



Average Domestic Investment, and FDI as a share of GFCF for the Caribbean and Trinidad and Tobago 2000-2008

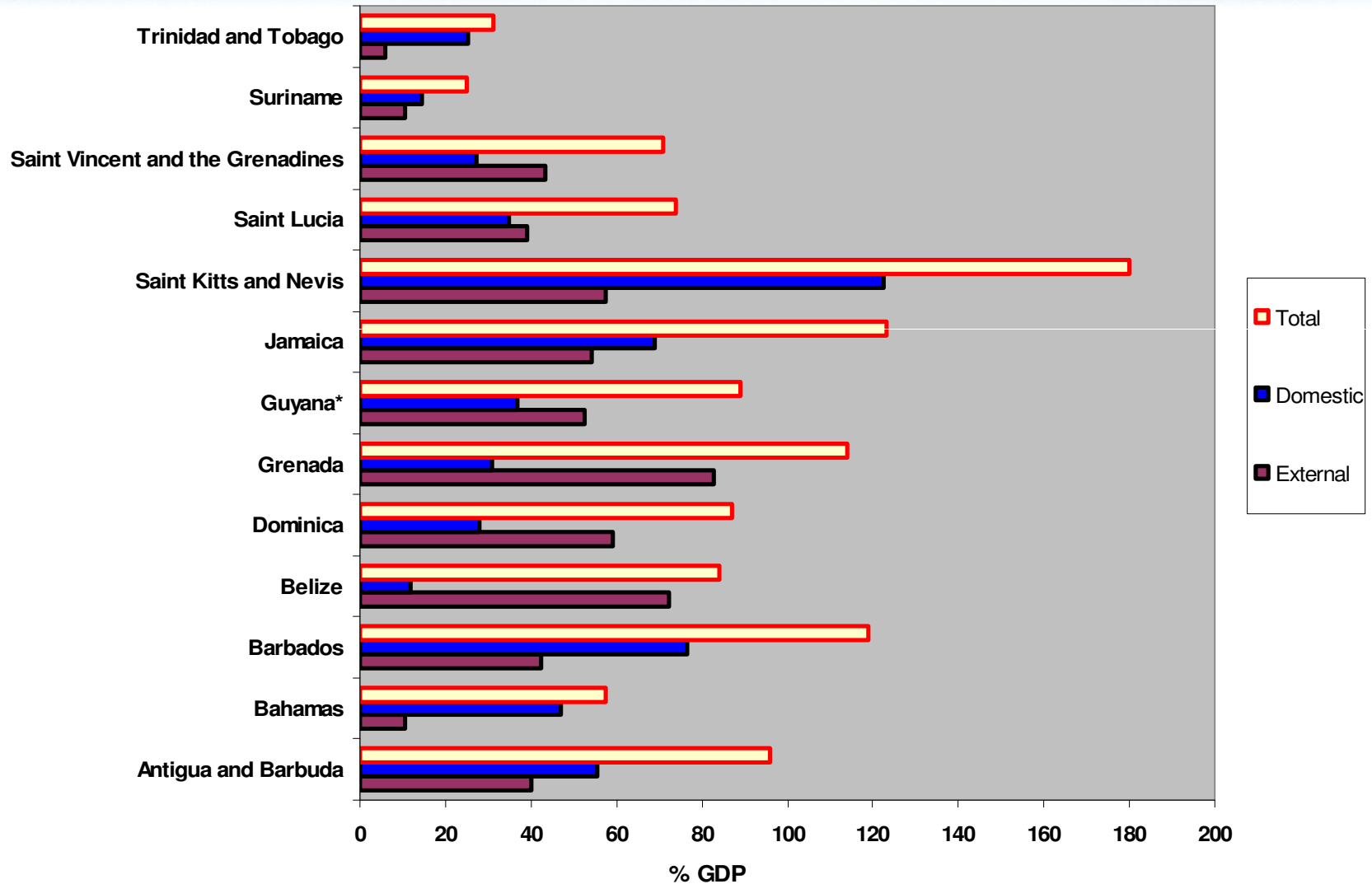


Source: ECLAC based on official data



Total public debt to GDP ratio and the % share of external and internal debt in 2009

Public Debt, % of GDP 2009.

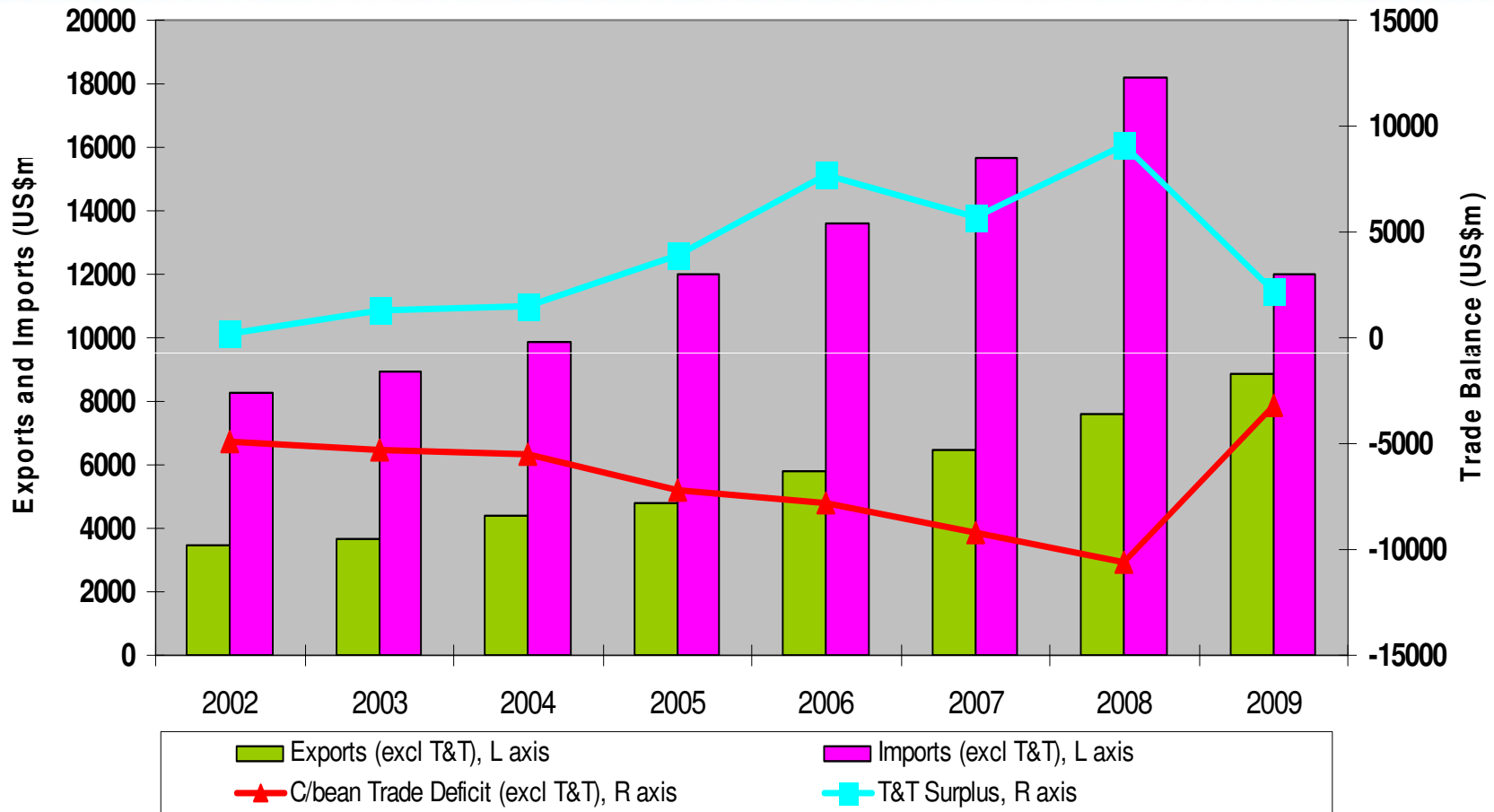


Source: ECLAC based on official data



Consequence of trade liberalization has been the weak response of the trade sector

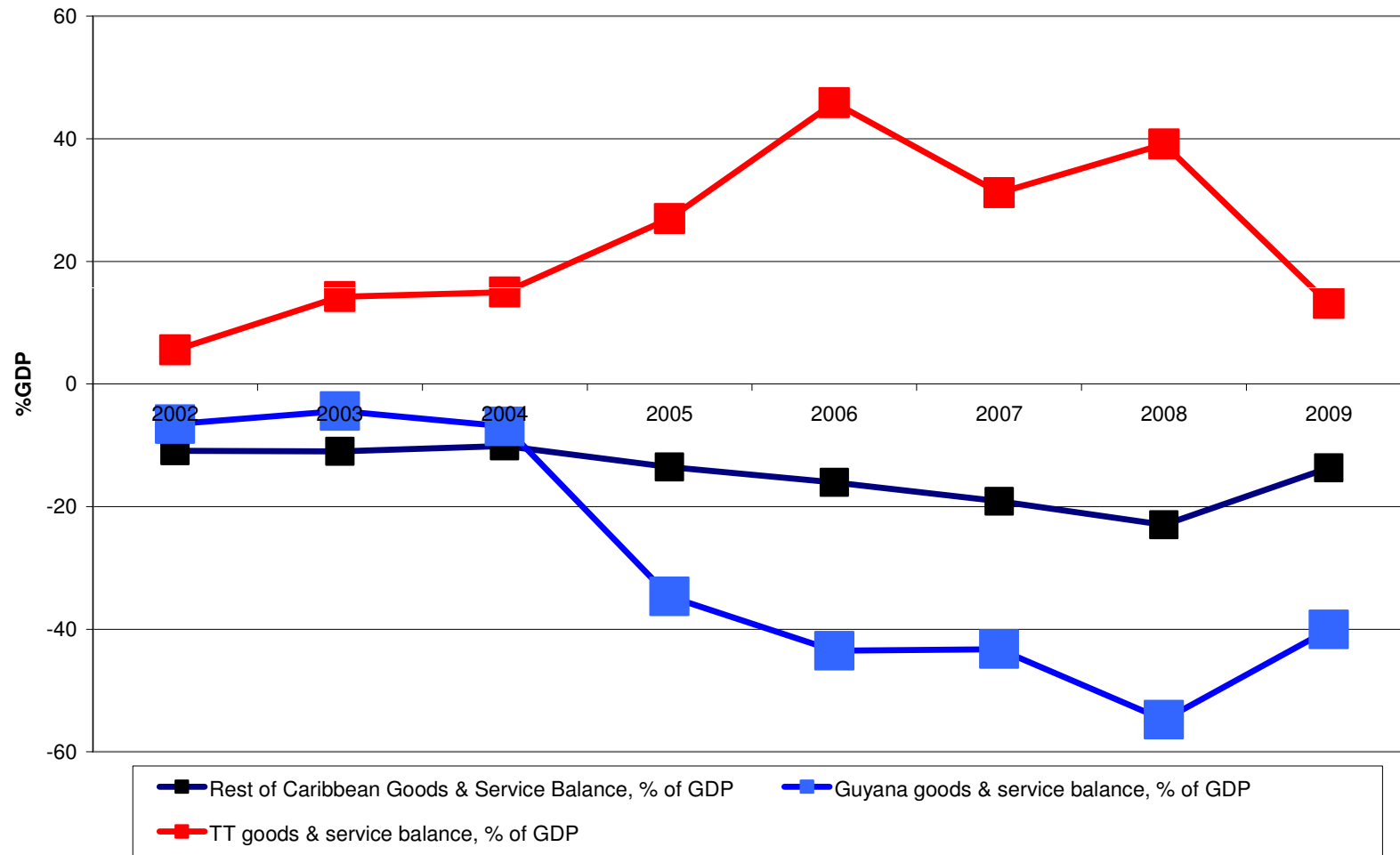
Merchandise Trade Deficit, 2002-2009
(with and without Trinidad and Tobago)





Goods and services balance for Trinidad and Tobago, Guyana and the rest of the Caribbean 2002-2009

Goods & Service balance, % of GDP



Source: ECLAC based on official data



Trade patterns and evolutions

- Regional goods exports have become increasingly dominated by Trinidad and Tobago as its share of exports rose from 37.4% in 1990 to 70.5% in 2008
- The OECS has lost GDP share in the region and export share of goods and services have declined over this period.
- There is an increasing concentration of exports on a few goods and services.
- The service sector has begun to lose global market share.

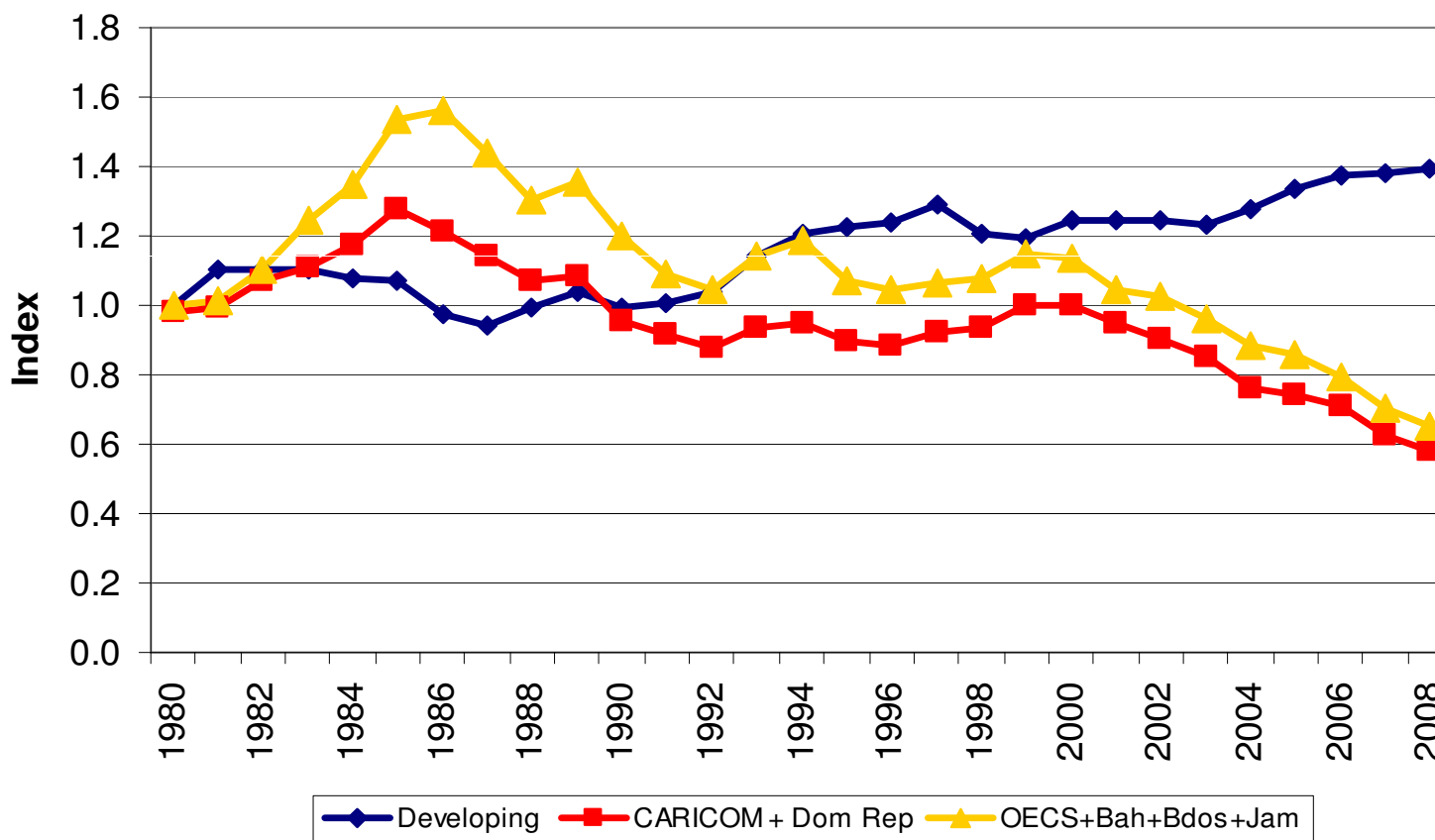


The search for new growth engines and the rejuvenation of a maturing service sector is an important part of the restructuring necessary for medium term growth

Index of Service Exports, 1980-2008

(as % of total global service exports)

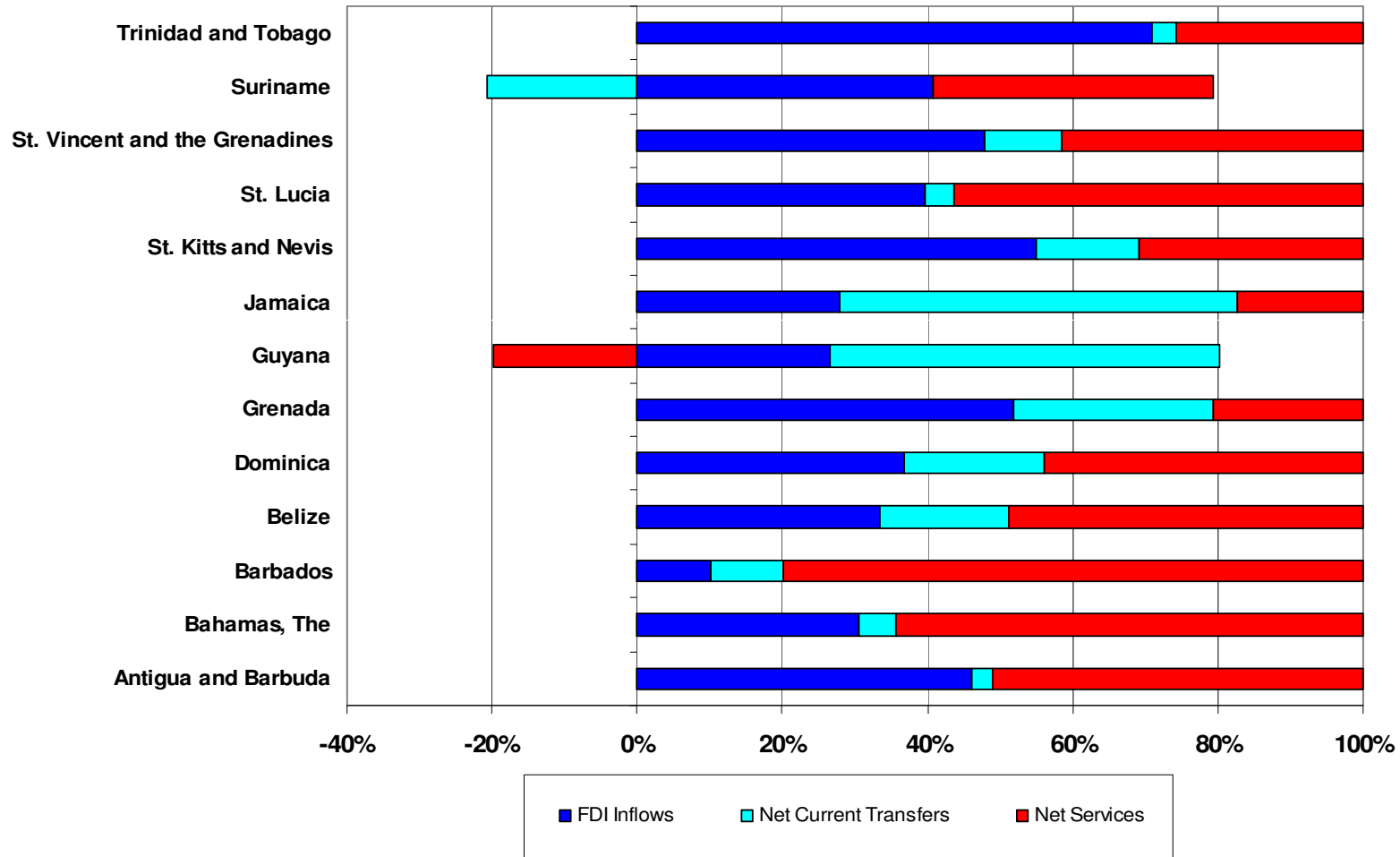
(Source: UNCTAD)





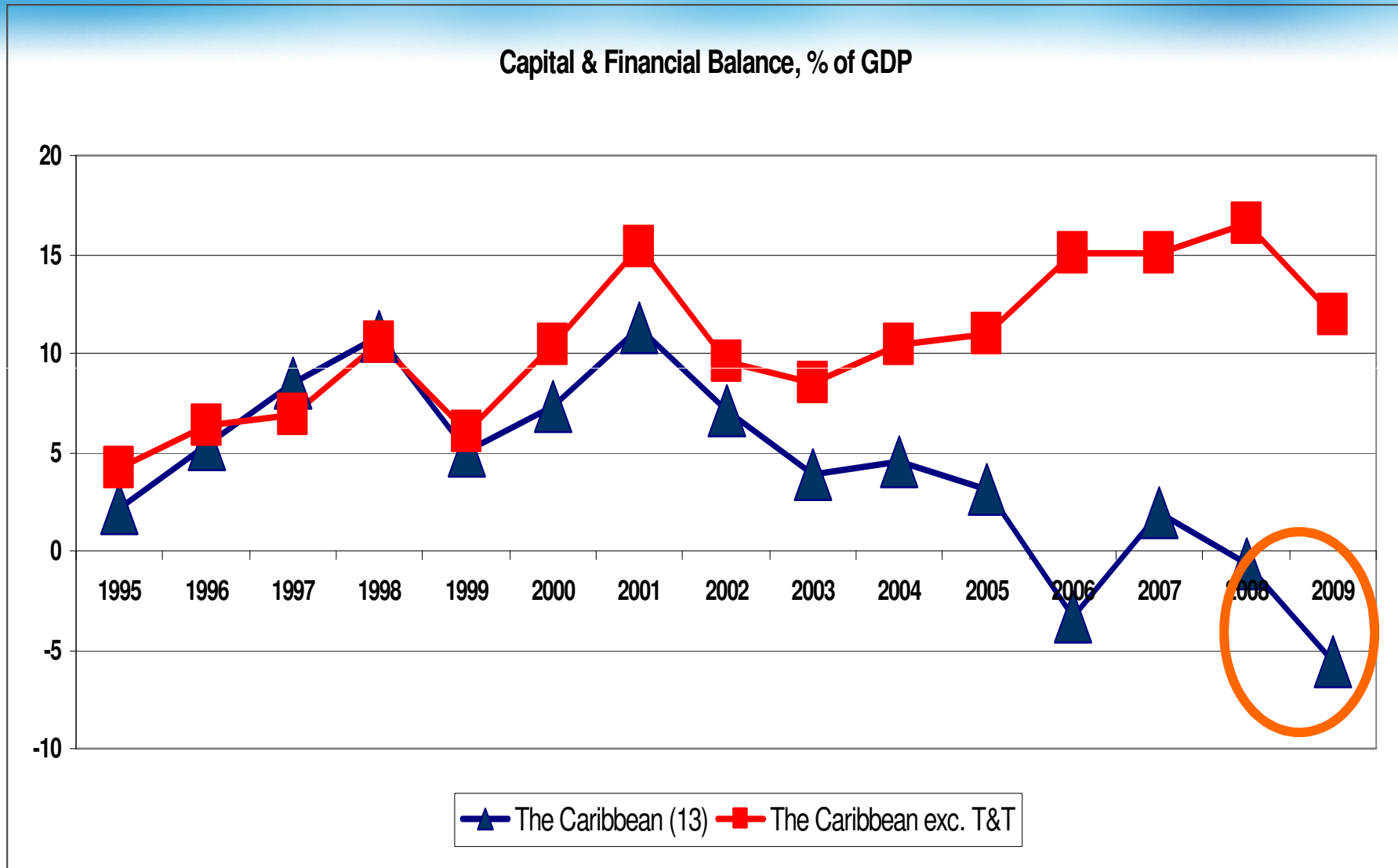
Financing the current account is crucial and the lack of foreign exchange is a binding constraint

Components of Foreign Exchange Inflows, 2002-2008





Capital and Financial Balance





Growth prospects for 2010

- Prospects for 2010 are so far better than 2009 but growth is constrained by continuing problems in the US economy and the EU.
- Growth in the MDCs is anticipated to be 1.6% with positive growth projected for Guyana (4.4%), Suriname (2.5%), Trinidad and Tobago (2.0%) and Belize (1.5%)
- The overall projection for the ECCU was a decline of 1.8% as a number of countries were expected to face continuing negative growth



The way forward

- A programme of fiscal consolidation should be pursued over the medium term but this must not disrupt investment in domestic capital which is designed to raise local capability.
- A pure export strategy is limited. Thus boosting internal and regional demand by the encouragement of sustainable projects through private and public sector partnerships is necessary.
- A programme of export diversification must be pursued in addition to market diversification, to reflect the emergence of new players in international trade.



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Thank You!