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FINANCIAL FLOWS TO CARIBBEAN COUNTRIES IN THE POST-CRISIS ERA

Introduction

The effects of the global economic crisis on the Caribbean have not been benign. Many Caribbean countries were pushed into economic recession by the crisis-induced contraction in demand for tourism services and offshore international financial services and widening fiscal deficits as revenue capacity deteriorated and pressures for fiscal stimulus and social protection increased. Faltering recovery of global economic growth starting in 2010, despite serious downside risks emanating from fiscal crises, financial sector fragility and public resistance to stabilization policy in some European countries, offer some hope for modest economic growth in the Caribbean. However, the capacity to finance capital investment programmes necessary to resuscitate and sustain economic growth is weaker in the immediate post-crisis period than it was previously.

Salient Features of the Post-Crisis Era

An important feature of the post-crisis era is the growth in financing needs of advanced economies. A substantial proportion of their gross debt is maturing thereby creating the need for refinancing. Moreover, fiscal deficits are projected to be large as renewed focus on economic growth moderates the implementation of fiscal consolidation policies. The IMF projects that in 2013 financing needs as a per cent of GDP will be 26.2% in the US, 13.9% in the UK, 17.8% in Canada and 19.5% in France. These large financing needs of governments in advanced countries will be a major call on global financial resources which could have the effect of crowding out small economies.

Government foreign indebtedness remains problematic in major economies. Gross government debt in 2012 is expected to be 106.8% in the US, 88.4% in the UK, 84.7% in Canada, 78.9% in Germany and 89% in France. The fiscal situation is also problematic given primary deficits exceeding 5% of GDP in the UK, the US and Japan. The situation with respect to fiscal balance and government debt sustainability is much worse in some other European countries.

There are enduring concerns about the possibility of debt delinquency and default as well as about political capacity to imple-

ment tough policies for economic stabilization and structural adjustment, especially in the weaker European economies. These concerns are reflected in the deterioration in the credit market ratings of several advanced economies such as the US, France, Ireland, Italy, Portugal and Spain which have either been downgraded or had negative outlooks issued by credit rating agencies.

Risk apprehension has increased among banks and other financial market investors who are taking action to reduce risk exposure. A common measure is deleveraging by reducing bank credit and overdraft facilities. Deleveraging is not confined to Europe. Spanish, US and UK banks have deleveraged substantially in Latin America.

Challenges for Caribbean Countries

Caribbean countries will have limited scope for refinancing commercial debt or accessing new commercial debt. Many of them were already experiencing difficulties in market access because of high transaction costs associated with relatively small credit demands. Increased risk apprehension, greater risk avoidance and larger funding requirements of the advanced economies compound the problems of access to commercial finance. It is noteworthy that while commercial loans to Latin America and the Caribbean as a whole remained robust in 2010-2011, Caribbean countries were not significant beneficiaries.

The prospects for bond finance are also less favourable. Large emergent economies, such as Brazil and Mexico, have been increasingly successful in the bond segment of international financial markets in 2010 and 2011. However, small countries such as Costa Rica, Guatemala, St Lucia and Trinidad and Tobago have engaged in only small, infrequent bond transactions, and most Caribbean countries have not entered the market at all in recent years. Furthermore, several Caribbean countries have been downgraded by either S&P or Moody's since 2008. These countries include The Bahamas, Barbados, Belize, Bermuda, Grenada, and Jamaica. In such cases, it would be surprising if the risk premiums for gaining access would not be large. It should be noted, however, that there are some small Caribbean countries with stable or improved ratings, e.g. Costa Rica, Curacao, Dominican Republic, Guatemala, Suriname and Trinidad and Tobago.

FINANCIAL FLOWS TO CARIBBEAN COUNTRIES IN THE POST-CRISIS ERA CONT'D

Corporate equity and debt do not seem to feature in international financial flows to Caribbean countries. The reasons would include the tightly held family-owned nature of most business enterprises, the underdevelopment of local capital markets and rating institutions which could provide information and other risk assessment services and opportunities for secondary trade, the generally weak framework for corporate accountability, and cost disadvantages of small financing requirements. Only the Caribbean offshore centres (Aruba, The Bahamas, Bermuda, and Cayman Islands) engage substantially in corporate issue of international securities and bonds.

Bilateral aid flows are quickly becoming a matter of history rather than a significant contemporary source of international finance for Caribbean countries. Aid flows from the US have diminished greatly since the 1990s and what little remains is concentrated on efforts to combat international narcotics trade and international terrorism. The UK, which has maintained a significant foreign aid presence, announced in 2011 a major strategic shift in its aid policy to concentrate primarily on countries and regions which are extremely poor or are crisis torn. As a consequence, the Caribbean is now a minor destination for UK financial aid.

Two principal options seem open to Caribbean countries, but not equally to all of them. One option is foreign direct investment. Because net FDI inflows to the Caribbean decreased in each year of the 2009-2011 period, operationalizing the FDI option would be tantamount to seeking to reverse the negative trend. Judging from the sector composition of FDI, countries with stronger manufacturing bases and prospects and countries with mineral resources are the ones more likely to be successful in achieving growth in net foreign direct investment. There are signs that the very small Caribbean exporters of tourism services will not be as successful unless there is sustained growth in the industry

The second option is loans from multilateral financial institutions and regional development banks. Since the start of the global crisis there has been a more liberal stance towards the capitalization of MFIs and regional or sub-regional development banks. Available financial resources have expanded tremendously. The challenge for small countries is to satisfy the portfolio risk criteria and the development effectiveness criteria of the lending institutions which are themselves being evaluated more stringently by the international credit rating agencies. This becomes essentially an assessment of debt sustainability, fiscal sustainability and project implementation capacity. In the immediate post crisis period, these criteria are not easily met by Caribbean countries, especially those who entered the crisis already in

considerable difficulty with fiscal management, debt overhangs and weak public administration. But it is a challenge they cannot escape.

Responses

Caribbean countries might seek to respond to the unfavourable short term and medium term outlook for capital inflows in several ways. First, they might try to more fully draw upon the excess liquidity in their banking systems for investment projects in the private sector and, depending on the extent of public sector indebtedness, also for investment projects in the public sector. Because foreign exchange resources are one of the macroeconomic constraints on the capacity to effectively activate idle financial capital, there will have to be a calibration of foreign exchange earnings and potential earnings with domestically financed investment expenditures. Second, as part of their response, they should also vigorously attempt to raise levels of resource efficiency. Productivity levels are currently low and have hardly responded to spasmodic and weakly implemented policies. Improvement of resource efficiency will increase the benefits of whatever financial resources are obtained. Third, another necessary component of the response will be efforts by small countries to win international reputation for sound financial management. This entails achievement of fiscal stability and debt sustainability. Progress in this direction should have the consequence of improved access to international financial markets and will make it easier for development banks to extend loans. Fourth, greater efforts could be made to attract financial capital from diaspora communities and to channel it to a greater extent into the production sectors of the economies. Success in attracting portfolio capital from the diaspora will be conditional upon improvements in the policy and regulatory framework governing cross border capital transactions and investor protection. These elements of a strategic response place the emphasis on domestic policy formulation and implementation capacity.

**By Professor Compton Bourne
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REGIONAL NEWS SUMMARY

CL FINANCIAL

- St Kitts and Nevis is being asked to permit the US\$6.6 million worth of assets held in CLICO International Life to be disposed of as part of a transaction that could see the insurance company's traditional business sold to one of two regional insurance entities (Carib360 31 Jul)
- Majority State-controlled Jamaican rum producer, Lascelles deMercado, declared after tax profits of \$417.5 million (J\$5.8 billion) for the nine-month period ending June 30, and the company is expected to pay out \$216.4 million (J\$3 billion) in dividends to its shareholders. Of the dividend payment, which is equal to about 52% of the company's net profit for the period, it is expected that T&T's coffers will benefit to the tune of \$188 million as some 87% of the ordinary stock units of Lascelles and 92% of the voting rights of the company are owned by subsidiaries of CL Financial, which in turn is controlled by the T&T Government (TG 2 Aug)
- Lawyers acting on behalf of State-owned Clico (Trinidad) failed to force Craig A Gomez, the Bahamian liquidator of Clico (Bahamas), to give information in relation to US\$126 million in transactions tied to the Bahamas subsidiary as well as possible assets held in Florida (Newsd 5 Aug)

CARIBBEAN

- Social programmes are taking up 20% of T&T's country's expenditure, Minister of Finance Larry Howai has said. (TE 22 Jul)
- The Barbados Government has been jolted into acceleration mode in an effort to "restructure and develop" the Barbados economy, following a recent humiliating downgrade by international credit rating agency Standard & Poor's (BN 24 Jul)
- In the face of continuing economic hardship, the government of Jamaica is pushing forward with its plans to increase the minimum wage by 11% (Carib360 26 Jul)
- Taking on debt may not be such a bad idea, even in these difficult economic times, says career banker and wealth management consultant Patrick Tannis. In fact, he says, managing debt could actually be a vehicle to financial prosperity (BN 26 Jul)
- The reduction of technical barriers to trade which currently exist between CARIFORUM countries and the EU is the focus of a BBD\$18.5 million EU-funded programme, coordinated by the CARICOM Regional Organisation for Standards and Quality (CNnow 26 Jul)
- The IMF completed the second review of St Kitts and Nevis' economic performance under a programme supported by a 36-month Stand-by Arrangement, allowing the immediate disbursement of an amount equivalent to SDR 3.161 million (about US\$4.83 million) (CNnow 26 Jul)
- Trinidad and Tobago needs more strategic corporate social responsibility (CSR) for sustainable social improvement to take place, the UNDP study on CSR in Trinidad and Tobago has suggested (TE 27 Jul)
- Mobile operator Digicel Group has signed a US\$17-million financing arrangement with mobile banking outfit Boom Financial to spearhead remittance products in the region (JG 27 Jul)
- Scotiabank and the CDB have closed a US\$103 million Interest Rate Cross Currency Swap transaction that has been termed "an unprecedented success" by both parties (Carib360 27 Jul)
- Brokerage house Jamaica Money Market Brokers has completed its acquisition of Capital and Credit Financial Group. With the deal, JMMB will be able to delve into the restricted unit trust market with CCFG's products: real estate, equity and fixed income trusts (JO 27 Jul)
- Suriname state oil company Staatsolie is considering selling stock through a partial privatisation similar to those carried out by state energy firms in Colombia and Brazil, a company official has said. Shares will also be sold in telecommunications firm Telesur and Surinam Airways, which are state owned, and the bank Hakrinbank, which is partly owned by the government (TG 27 Jul)
- The IMF says despite a deteriorating external environment, including the deepening Euro-zone crisis, Guyana's economy continues to be resilient. It said last year, the economy recorded another year of impressive growth of more than 5% driven in part by high commodity prices, foreign direct investment, and domestic credit expansion to the private sector (TG 29 Jul)
- Rosebel Gold Mines, Suriname's main gold producer, has reported a gross income of US\$608 million and a net profit of US\$196 million in 2011. Through taxes, royalties and dividends the Suriname government earned US\$156.5 million while RGM's local spending totalled about US\$143 million (CNnow 30 Jul)
- WITH Barbados' food import bill having been put at over \$170 million during the first four months of 2012, there are mounting fears that global food prices could again rise, similar to what took place four years ago (BAAdv 31 Jul)
- Guyana's revenue service has sent tax assessment forms en masse to entrepreneurs in the gold mining industry, especially those that have put up a lucrative business. Owners of the so-called 'gold pontoons' and 'scalians', the colossal vessels on the Corantijn, Suriname and Marowijne Rivers, are the first to be taxed (SN 2 Aug)
- Guyana freight firm Laparkan recently unveiled its new warehouse and corporate offices in Miami, Florida, to a high level audience that included Prime Minister, Samuel Hinds (Carib360 2 Aug)
- Improvements that make government payment programmes more efficient, safer and more transparent can cut related administrative costs by as much as 75% (CNnow 3 Aug)
- Australia-based company, Azimuth Resources Ltd has secured US\$6 million to continue its resource expansion and prospect drilling at its West Omai gold project in Guyana, even as the global demand for gold remains high (SN 3 Aug)

REGIONAL NEWS SUMMARY CONT'D

- Of all the industries, the one industry that has managed to withstand the recession is the cultural industry. This is according to Minister of Family, Culture, Sports and Youth, Stephen Lashley, who said that despite the financial circumstances, persons are still willing to spend money in the arts (BAdv 3 Aug)
- The Pan American Life Insurance Group has completed the acquisition of Algico in T&T along with other regional subsidiaries of Algico parent (TG 3 Aug)
- Barbados' exports to Trinidad and Tobago have surged significantly during the first four months of this year. This comes as recent difficulties relating to trade between the two countries have apparently been eased (BAdv 6 Aug)
- Remittances to Jamaica fell flat in May, reflecting a continued slowdown of money sent home from abroad (JO 6 Aug)
- Suriname's bauxite mining company Suralco is in the red and needs to change its policy drastically to be able to compete on the world market. Production costs have to be cut, but although this may look like a difficult task, it is not unachievable, says the new Managing Director Ruben Halfhuid (SN 6 Aug)
- T&T recorded a fiscal surplus of \$1.3 billion for the first eight months of the current 2012 fiscal year, according to the July Economic Bulletin, published by the Central Bank (TG 7 Aug)
- The data from T&T's CSO indicated that the unemployment rate fell from 5.2% for the third quarter, 2011 to 4.2% for the fourth quarter of last year (TE 8 Aug)
- Angostura Holdings Ltd announced an after-tax profit of \$90.9 million for the six-month period ended June 30 (TE 10 Aug)
- A delegation of private sector officials from CARIFORUM member states have concluded from a recent tour of several European countries that trade agreements with the EU are unlikely to bring significant economic gain to small operators in the short to medium term (SN 10 Aug)
- Trinidad and Tobago officials are harnessing the expertise of the Caribbean Information and Credit Rating Services Limited to develop a flexible medium-small enterprise credit risk rating methodology (Carib360 10 Aug)
- Standard & Poor's Rating Services has raised Jamaica's short-term sovereign credit ratings to 'B' from 'C'. The agency also affirmed Jamaica's long-term foreign and local currency issuer ratings at 'B-' (JG 13 Aug)
- The Central Bank of Barbados said Monday that the principal impact of the weak economic environment on the local financial sector continues to be anaemic loan growth across the sector. The CBB said there has been no overall growth in commercial bank lending to the non-financial private sector since September 2011 (GuyTim 14 Aug)
- Peppers and cocoa are in demand in the Florida market in the US, urea for fertilisers are in demand globally, and Trinidad and Tobago could provide these for American investors says Trinidadian-born Lt Governor Jennifer Carroll (Newsday 14 Aug)
- Moody's Investors Service has upgraded Suriname's junk-level bond rating, saying the government has demonstrated prudent fiscal management. The rating was increased to Ba3 from B1, three notches below investment grade. The outlook was changed to stable from positive (CNnow 15 Aug)
- More than 28,000 farmers in eight Caribbean countries are expected to benefit from a CAN\$20 million initiative over the next five years. The CIDA-funded project, dubbed the: 'Promotion of Regional Opportunities for Produce through Enterprises and Linkages', is aimed at providing an adequate and consistent supply of agricultural products to large purchasers, such as hotels and airlines within the region, by enhancing their capacity (JO 17 Aug)
- The quarrel between Curacao and St Maarten on the joint Central Bank is escalating (CNnow 21 Aug)
- A senior government official says Belize is seeking to engage creditors "as quickly as possible" and that the CARICOM country is definitely not in a position to meet its payments on its external date during a 30-day grace period (JG 22 Aug)
- The governments of Guyana and Suriname will continue to pursue funding from the IADB for a pre-feasibility study to build a bridge across the Corentyne River (GuyTim 22 Aug)
- The St Lucia government has launched a multi-million dollar stimulus package it is hoping would help turn around a sluggish economy. Prime Minister Dr Kenny Anthony said the construction stimulus programme would help address some of the worst financial conditions now being experienced in recent years and praised the private sector for contributing towards the reality of the fiscal package (BN 23 Aug)
- Standard & Poor's Ratings Services lowered its long- and short-term foreign currency sovereign credit ratings on Belize to 'SD' (selective default) from 'CC/C'. At the same time, the agency lowered its rating on Belize's bond due in 2029 to 'D' (CNnow 23 Aug)
- Jamaica and China have signed a new economic technical grant agreement valued at some J\$423 million (Caribseek 24 Aug)
- The debate surrounding cutting the cost of public-sector wages is about whether to do it primarily through wage concessions or job cuts. But Financial Analyst Dennis Chung says the Government's approach is wrong; that job cuts could hurt the economy at a time when it is in need of stimulus from consumer spending (JG 24 Aug)
- The Agriculture Development Bank and representatives of the Muslim community signed a Memorandum of Understanding for the establishment of a financing system according to Shari'ah (Islamic) law which would allow Muslim farmers to access loans (Newsday 24 Aug)
- For the second time in months several shipping lines have announced increases in their handling charges, and local manufacturers are concerned that these increases will add to their costs (TE 24 Aug)

REGIONAL NEWS SUMMARY CONT'D

- The First Meeting of the Joint Technical Committee of the CARICOM-Kingdom of Spain Joint Fund has launched the operation of the CARICOM-Spain Joint Fund as the new mechanism to manage the regional cooperation programme between CARICOM and Spain (CNnow 25 Aug)
- The restructuring of Belize's 2029 "superbond" may become a drawn-out battle, as creditors keep the country waiting for a formal response to proposals that could see them take a haircut of up to 80% on the net present value of their holdings (TG 26 Aug)
- T&T's inflation rate decelerated slightly for the second consecutive month in July, according to the Central Bank (TE 27 Aug)
- Guyana's mining sector continues to shine with a record breaking production of 251,000 ounces of gold from January to July of 2012, acting commissioner of the Guyana Geology and Mines Commission revealed (GuyTim 27 Aug)
- Lending to the private sector in Jamaica has stepped up, while interest rates continued to decline over the three months to June 30. The acceleration in growth in loans from commercial banks is being viewed as positive news for the economy by the Bank of Jamaica (JO 27 Aug)
- 2011 was the first year since the recession where the Caribbean's hotel industry posted positive growth in all three major top-line performance indicators (Carib360 28 Aug)

UPCOMING CONFERENCE

The Caribbean Centre for Money and Finance in conjunction with the Central Bank of Suriname will be hosting the 44th Annual Monetary Studies Conference on 7-9 November, 2012, in Paramaribo, Suriname. The theme of the conference is "Global Financial Shocks, Regional Macroeconomic Challenges and Their Impact on Regional Economic Integration", and will include sub-themes such as:

1. Banking, Finance and Regulation
2. Strategies and Policies to Strengthen Regional Economic Integration
3. Inflation and Economic Management
4. Fiscal Challenges and Debt Management in the Aftermath of the Global Financial Crisis
5. Improving Stock Market Performance in the Region
6. Understanding the Workings of Financial Markets in Small Open Economies
7. Public Sector Operations and Macroeconomic Stability
8. Sectorial Linkages and Economic Development
9. Financial Sector Stability

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