USAID
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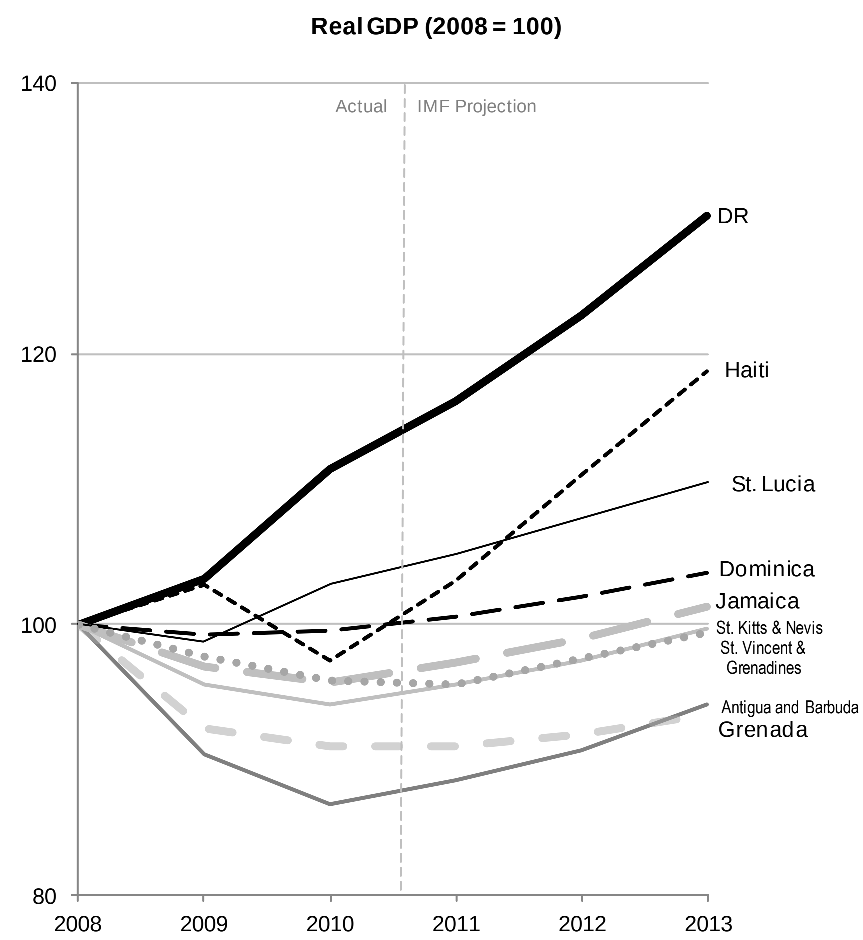
EADS Economic Trends Report

Caribbean

September 2011

Economic Overview



SOURCE: IMF, *World Economic Outlook*, September 2011.

Economic growth in the Caribbean region bounced back in 2010 after a contraction in 2009 as the world economy stuttered after the financial crisis. Country growth rates are strong (at 5 percent or higher) only in the Dominican Republic and Haiti. And in the case of Haiti, the currently strong real GDP growth rates reflect post-earthquake rebuilding and are in contrast to most of the previous decade when Haiti had the slowest growth rates in the Caribbean region.

One factor limiting the potential for rapid growth in the Caribbean is the continuing high levels of public debt, which are steering countries towards paths of fiscal consolidation. Many of the countries are using IMF standby arrangements to manage that process.

All of the economies remain vulnerable to natural disasters. Haiti is still struggling to recover from the earthquake two years ago. Hurricane Tomas caused enormous losses to the banana industry in St. Lucia (output down 88 percent) and St. Vincent & the Grenadines (down 27 percent), as well as the nutmeg sector in Grenada (down 45 percent). The tourism sector is also hard hit by recurrent hurricanes.

The six economies of the Eastern Caribbean Currency Union (ECCU) remained in contraction in 2010, with a 1.6 percent decline in real GDP on the heels of a 5.6 percent drop in 2009. Fiscal consolidation is proceeding quickly in the ECCU countries, with the overall fiscal deficit narrowing to 1.5 percent of GDP in 2010 from 4.7 percent in 2009. Policies in the ECCU are being guided by the "Eight Point Stabilization and Growth Programme" of the union's monetary council.

Countries covered in this report include Dominican Republic, Haiti, Jamaica, and the six countries of the Eastern Caribbean Currency Union (ECCU): Antigua & Barbuda, Dominica, Grenada, St. Kitts & Nevis, St. Lucia, and St. Vincent & the Grenadines. Due to data limits, not all countries are represented in every graph or analytical section.

Jamaica has also achieved a degree of fiscal consolidation in the past year. The deficit for fiscal year 2010/11 was just over 6 percent of GDP, down from a gap of just under 11 percent in the preceding fiscal year. Jamaica adopted a "fiscal responsibility framework" in 2010 and has implemented measures to improve its treasury management capacity.

Trade growth in the Caribbean region has not been as robust as in other parts of Latin America, where higher commodity prices and strong Chinese demand are boosting exports. In addition, foreign investment flows to Latin America have tended to be focused on South America rather than the Caribbean.

Since the regional free trade agreement with the United States, Central America, and the Dominican Republic in 2004, trade has grown for all the signatory countries. The accord has, however, increased the reliance of the Dominican Republic on the U.S. market, which is dampening growth in the short term as the U.S. economy tries to regain its footing.

World Bank Income Groups

Of the nine Caribbean countries in this report, only Haiti falls in the World Bank's Low Income group. All the other countries are Upper Middle Income.

In contrast to most of the rest of Latin America and other parts of the world, poverty rates declined in the Caribbean in the wake of the economic downturn in 2008. On that measure, the Caribbean outperformed the other sub-regions in Latin America.

Fiscal Policy

The Dominican Republican government missed its spending targets for the first half of 2011, so the fiscal deficit will be larger than expected and is projected to be 2.5 percent of GDP. In 2012, the deficit will be little changed even though recent tax-raising measures and electricity price hikes will boost revenue. With presidential elections set for May 2012, the government is likely to boost spending.

Jamaica is also facing elections in 2012 and this past summer agreed to a seven percent pay raise in the public sector. The country is under an IMF stand-by arrangement, with spending targets and financing from multilaterals. The Jamaican finance ministry has announced that it will impose additional cuts in capital expenditures to meet the spending targets.

Multilateral agencies are providing budget support to the Haitian government while technical assistance programs try to strengthen the government's ability to collect revenue. Currently, the government revenue is around ten percent of GDP and the intent is to raise that amount to 13 percent by 2013.

Monetary Policy

After a steady monetary policy during most of 2010, the central bank in the Dominican Republic has been raising the benchmark policy rate during the past twelve months. Assuming that the inflation rate responds by moderating, interest rates will probably once again be stable over the next year or so. Commercial lending has been growing briskly and the higher rates should slow that expansion.

For the six ECCU countries, monetary policy was unchanged during 2010. The two goals of financial system stability and exchange rate peg credibility were mostly achieved.

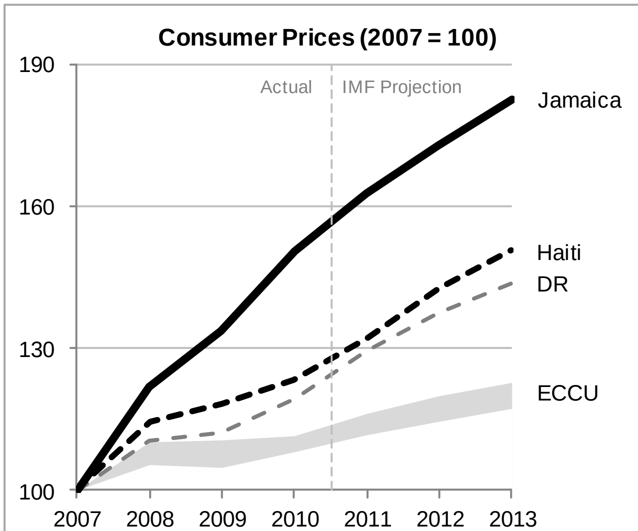
Haiti's monetary policy is dependent on IMF support. As foreign aid, remittances, and IMF support have surged into Haiti, the challenge has been to stabilize the exchange rate and expand credit to the private sector.

Jamaica's central bank eased its policy stance in 2010. The inflation rate had dropped notably from 2008 to 2009, an IMF stand-by arrangement had stabilized the exchange rate and spurred mild appreciation in 2010, and a new debt exchange institution (the Jamaica Debt Exchange) generally lowered interest rates in the economy.

Real GDP Growth Rates, 2010	South America 6.2%	Mexico 5.5%	Central America 3.7%	**Caribbean 3.4%**

Inflation

Over the past decade, and continuing into the next couple of years, the inflation performance of the six countries of the Eastern Caribbean Currency Union (ECCU) stand in sharp contrast to the other Caribbean countries. The ECCU record and projections show far more price stability than elsewhere. Haiti, Dominican Republic, and Jamaica have significantly higher inflation rates.



SOURCE: IMF, *World Economic Outlook*, September 2011.

In the Dominican Republic, inflationary pressures are from both energy and food prices. Although the annual inflation rate is now above the government's 5-6 percent, the July 2011 year-on-year 9.9 percent rate was boosted by a one-time hike in electricity charges. Jamaica's 11.8 percent inflation rate in 2010 was up by more than a percentage point from 2009. Progress had been made from the torrid 16.9 percent pace in 2008.

Higher fuel and food prices nearly doubled the ECCU rate of inflation in 2010, but it remained relatively low at 2.2 percent. Inflation convergence in the ECCU is not complete. The highest country inflation rate for 2010 was 4.2 percent in Grenada, where prices were pushed higher by the introduction of a VAT.

Inflation Trends

High inflation: During the past two decades, three Caribbean countries (Dominican Republic, Haiti, and Jamaica) have had three or more years with annual inflation exceeding 20 percent.

Low inflation: The six Caribbean members of the ECCU always kept annual inflation below 9 percent during the past two decades.

Consumer Price Inflation, 2011 (projected)	South America 8.8%	**Caribbean 7.7%**	Central America 5.4%	Mexico 3.6%

Banking and Financial Sector

Over the past decade, Jamaica has greatly expanded the level of its domestic credit relative to GDP, while Haiti and the Dominican Republic have shown a flat or declining trend.

Jamaican interest rates are trending downward over the past two years. Modest economic growth, fiscal consolidation, and the launch of the new Jamaican Debt Exchange are allowing the Jamaican central bank to encourage investment with lower interest rates.

The Eastern Caribbean Currency Union (ECCU) countries have kept their monetary policy stance largely unchanged the last two years, with little movement in interest rates. In 2010, several of the countries established financial services regulatory commissions and adopted new insurance regulations.

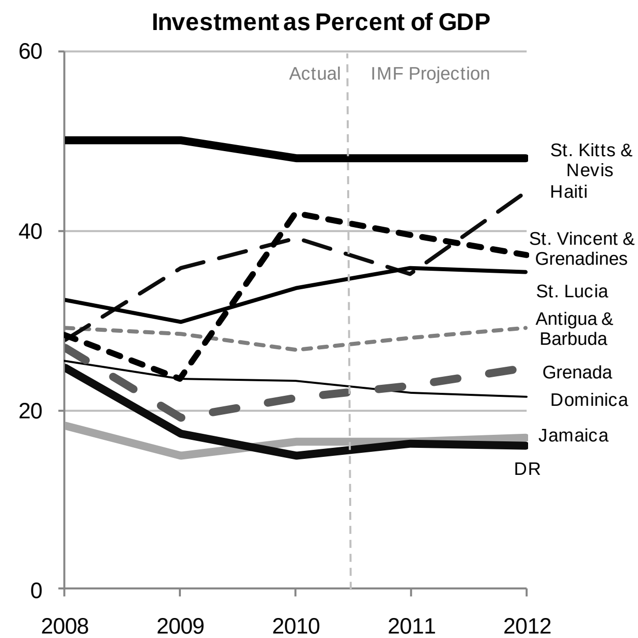
Investment

As was the case in other parts of Latin America, the Caribbean suffered a decline in its investment-to-GDP ratios in the wake of the world financial crisis. Only a small number of Caribbean countries have achieved a rebound.

Some fiscal tightening expected in the Dominican Republic over the next few years will dampen both consumption and investment. However, FDI and official lending should be able to pick up some of that slack.

Political uncertainties in Haiti are perceived as keeping some investors on the sidelines for now. However, a rebound in manufacturing orders has induced some spending on new equipment and plants.

In Jamaica, investor uncertainty is holding back spending as many sectors of the economy remain sluggish. The tourism sector in Jamaica is notably strong. In the ECCU countries, investment in 2010 was restrained by limited availability of foreign financing.

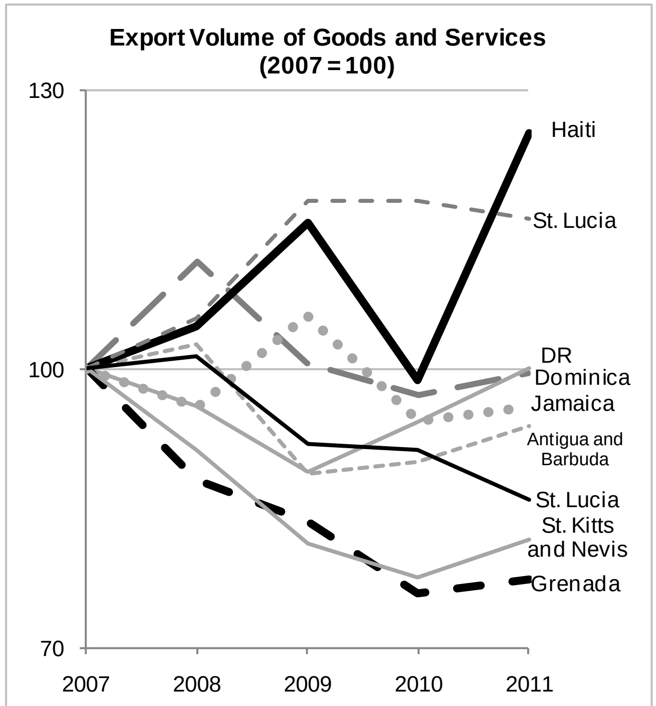


SOURCE: IMF, *World Economic Outlook*, September 2011.

The smaller island economies of the Eastern Caribbean Currency Union (ECCU) have been generally more successful over the past decade at raising their investment to GDP ratio. The Dominican Republic and Jamaica both have lower investment ratios now than a decade ago.

Investment as a Percent of GDP, 2010	Mexico 25.7%	South America 21.0%	Central America 19.8%	**Caribbean 17.7%**

Trade



SOURCE: IMF, *World Economic Outlook*, September 2011.
NOTE: 2011 values are projections.

Jamaica's exports have been stagnant since 2007 while their import spending continues to rise and cause a wider deficit. Part of the problem with exports has been tepid demand from Jamaica's main trading partners and adverse weather in 2010 that limited agricultural production. Part of the upward pressure on the import bill comes from higher commodity and fuel prices. If the price pressures ease in 2012, Jamaica is expected to post a narrower current account gap.

Haiti has been running increasingly large trade and current account deficits since the 2010 earthquake. Domestic production needs more time to fully recover and the demand for imports is strong. Some of the import demand is being financed by a significant rise in remittances.

The price of oil is a key determinant for the fluctuation in the trade balance for the Dominican Republic. With prices higher both this year and last, the current account deficit has widened sharply, approaching double digits as a percentage of GDP. The tourism sector has not been a reliable source of export growth, but mining production, especially nickel, should boost Dominican Republic exports over the next few years.

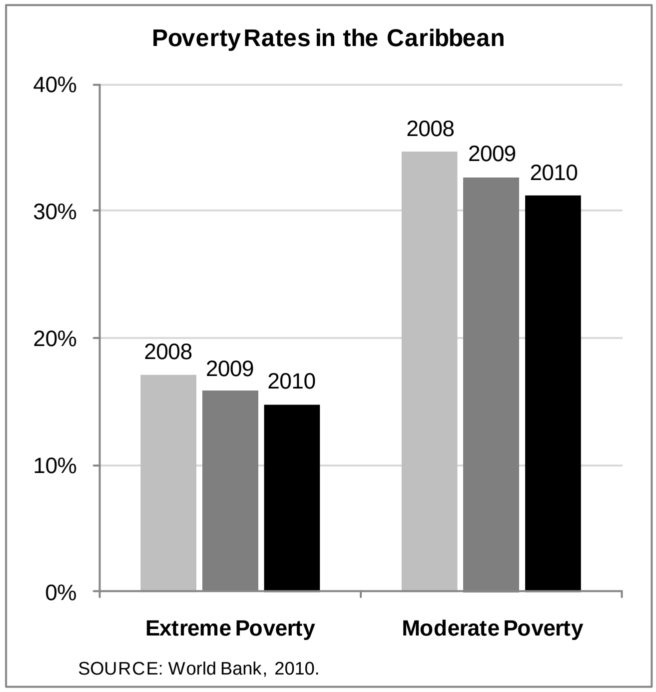
Among the smaller island economies of the Eastern Caribbean Currency Union (ECCU), sluggishness in the domestic economy did narrow the current account deficit in 2010. ECCU countries also experienced a sharp decline in foreign direct investment in 2010, as the tourism sector attracted smaller equity inflows.

For all the Caribbean countries, export performance is often heavily dependent on avoiding hurricanes and other natural disasters. Even the more relatively diversified economies in the region can be hit by an unforeseen disruption to production.

Percentage Change in Export Volume of Goods and Services, 2010	Mexico 14.2%	South America 8.5%	Central America 7.4%	**Caribbean 5.5%**

Poverty Reduction

The Caribbean region proved to be resilient despite slower economic growth throughout Latin America and in North America starting in 2008. The World Bank estimates that both measures of poverty—extreme and moderate—continued to decline in the region as a whole in 2009 and 2010. (World Bank, *Did Latin America Learn to Shield its Poor from Economic Shocks?*, October 2010)



Continued economic growth was able to reduce poverty rates even as unemployment rose in some Caribbean countries. In Jamaica, unemployment was 12.4 percent in 2010, up by a percentage point from 2009, according to ECLAC data. In Trinidad & Tobago, unemployment was also higher in 2010, but remained about half as high as in Jamaica. Unemployment in St. Lucia increased to just over 20 percent in 2010, while the rate in Grenada was nearly 30 percent.

Among the countries in the Eastern Caribbean Currency Union, inflation has been largely in check over the past two years. With inflation rates running between two and four percent annually, the pressures are in food and energy prices. Although inflation in those areas can hit the poor the hardest, the Caribbean countries are taming inflation and limiting the harm done to those in poverty.

Progress on Human Development

Nearly all of the Caribbean countries are rated as achieving "High Human Development" in the latest Human Development Index (UNDP). Only two (Dominican Republic and St. Vincent & Grenadines) are rated as "Medium Human Development." Haiti is rated as "Low Human Development."

Additional Information

For country-specific data and additional information about the countries covered in this report, please visit the EADS Country Portal at http://esdb.eads.usaidallnet.gov/query/do?_program=/eads/esdb/countryPortal.

Sources used in compiling this report include the semi-annual *World Economic Outlook* from the International Monetary Fund (http://www.imf.org/) and the *Global Economic Prospects* from the World Bank (http://www.worldbank.org/).