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Publisher's Note

The *Economic Review* is published three times a year in June, September and December, by the Central Bank of Barbados. It is prepared by the Bank's Research Department and contains articles of research undertaken at the Bank. In addition, we welcome contributions of a non-technical and empirical nature on economic and policy issues in the Caribbean. Book reviews and surveys are also welcome. All submitted papers are reviewed by the Editorial Committee* and external referees.

Articles and correspondence regarding the Review should be addressed to:

The Administrative Editor
Economic Review
Central Bank of Barbados
P.O.Box 1016
Bridgetown
Barbados
Tel: (246) 436-6870
Fax: (246) 427-1431
E-mail: cbb.lib@caribsurf.com
Website: www.centralbank.org.bb

***The Editorial Committee**

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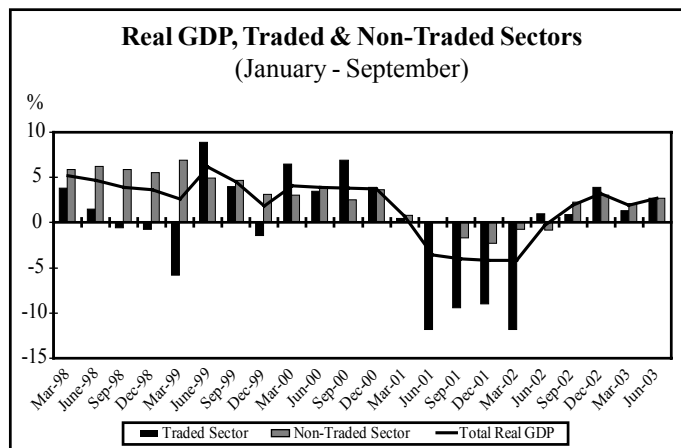
Review of Economy

During the first half of 2003, real economic activity in the Barbadian economy grew by an estimated 2.0%, in contrast to declines of 2.6% and 3.8% in the comparable period of 2001 and 2002, respectively. There was a significant boost in tourist arrivals, particularly during the second quarter, as the traded sectors rose by 2.5%. In addition, there was growth in most of the non-traded sectors (1.9%), particularly in the wholesale and retail industries and Government. Growth in economic activity led to an increase in the actual number of persons employed, but the unemployment rate expanded largely as a result of the entry of over six thousand new persons into the labour force. Domestic inflation was up marginally during the review period as movements in the major categories offset each other.

The current account of the balance of payments recorded a sizeable deficit for the first six months due to a significant rise in retained imports, which more than offset receipts from tourism. Consequently, the net international reserves (NIR) of the monetary authority increased by approximately \$13.1 million, about \$58.1 million less than the rise in the similar period of 2002, and the smallest expansion in the first six months since 1994.

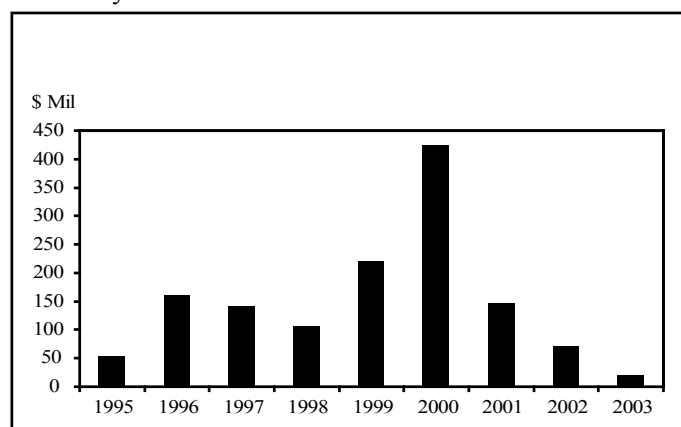
The balance on the capital and financial account was \$70.9 million, \$30.5 million more than that registered for the same period last year.

Domestic deposits denominated in local currency rose by \$71.6 million during the review period. This is considerably less than the figure for the same period in 2002 when domestic deposits grew by almost six times this amount as a result of the capital gains on the sale of Life of Barbados shares and Government's injection of funds into the local economy. In addition, credit to the private sector declined by \$8.5 million, leading to a 1% increase in the excess liquidity ratio to 18.7% at the end of the review period. The persistent high level of liquidity in the banking system



continued to contribute to the depression of the Treasury bill rate, which was 1.91% at the end of June 2003.

During the first half of the year, government operations yielded a deficit of an estimated \$41.4 million, \$47.4 million less than that for the same period last year. The reduction in the deficit reflects an improved revenue outturn together with significant reductions in capital expenditure since the beginning of the year. Financing was primarily sourced domestically.



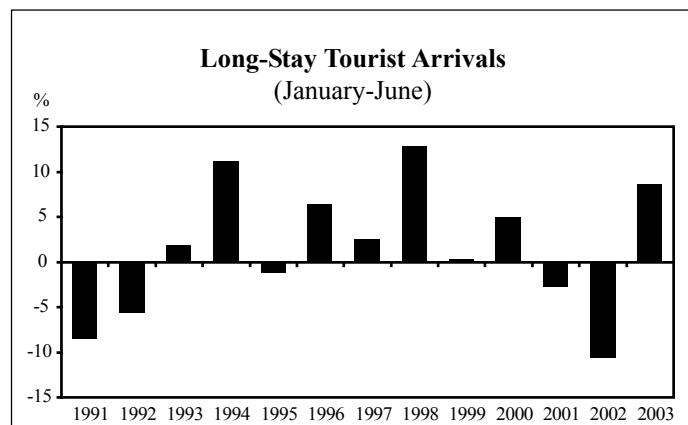
Production, Prices and Employment

Tourism

In the first six months of 2003, the tourism sector sustained the recovery that began in the latter half of 2002, as both long-stay and cruise passenger arrivals continued to

strengthen. As a result, real tourism value-added grew by approximately 8.6%, after plummeting by 9.7% between January and June a year ago.

The number of long-stay visitors rose by an estimated 10.3%, in marked contrast to a fall of 10.6% in the corresponding period of 2002 and a decline of 2.7% in 2001. Following the measured expansion in the first quarter, visitor numbers in the second quarter increased sharply, with



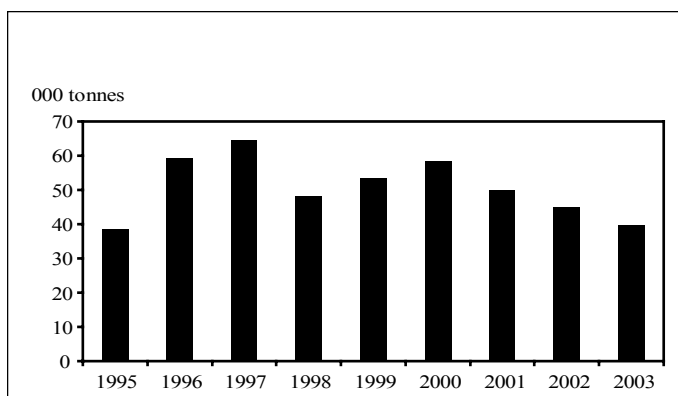
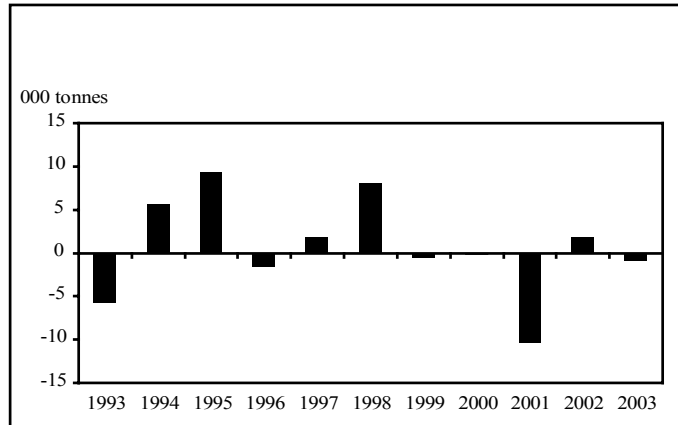
long-stay and cruise arrivals posting growth of 19.2% and 4.9%, respectively. The improvements registered for most of the island's main source markets has been largely attributed to the early re-launch of the "Best of Barbados" campaign, and other marketing initiatives in the region. Arrivals from the United States and the United Kingdom expanded by 7.3% and 10.6% respectively, while the Canadian market rose by 5.4%. CARICOM visitors were also higher, as both Trinidadian and other CARICOM arrivals climbed by 15.7% and 11.9%, respectively. There was also a significant upturn in the number of long-stay tourists from Germany (14.5%) and other Europe (14%).

Cruise-passenger arrivals grew by an estimated 2.7% during the first two quarters of 2003, which is in contrast to the 6.3% decline experienced in the comparable months of 2002, and considerably less than the robust growth of 15.7% and 28.3% in the first half of both 2001 and 2000 respec-

tively. This outturn signals an increasing demand for cruise travel, as activity in the industry gradually returns to pre-recession levels.

Manufacturing

Output in the manufacturing sector was estimated to have declined by 0.7% during the review period, in contrast to the 1.8% expansion registered over the corresponding two quarters of 2002. Notwithstanding increased produc-



tion in the food processing (2.4%), and beverages industries (3.3%) respectively, overall manufacturing output was hampered primarily by reductions in the production of non-metallic mineral products (4.2%), other manufacturing (1.4%), chemicals (8.9%) and electronics (16.5%). In particular, the decline in the output of electronic components was due mainly to the closure of a factory at the end of the review period last year.

Agriculture and Fishing

For the third consecutive year, sugar production fell in the January-to-June period. This outturn was on account of drought conditions and some operational problems at the factories at the beginning of the crop. The 2003 sugar crop produced approximately 39,600 tonnes of sugar - a decline of 5,219 tonnes or 11.6% from the level in 2002, and is the smallest yield since 1995. In contrast, non-sugar agricultural output rose moderately after falling by 2.7% in the equivalent period last year, primarily because of higher output of chicken (1.6%) and fish (10.2%).

International Business Services

For the first six months of the year, 145 new licenses were issued to companies in the international business and financial services sector, compared to 137 for the corresponding period last year. Of this, 126 went to international business companies, which follows 119 and 125 given for the same period in 2002 and 2001 respectively. Additionally, 14 offshore banks, 3 new exempt insurance companies and 1 new exempt insurance management company were authorised to operate.

Construction

During the first half of 2003, the key indicators of construction activity revealed a mixed performance of the industry. While imports of construction materials increased robustly by 8.8%, after falling 4.7% one year earlier, the average rate of employment in the industry rose by less than one percent or 100 persons, following a significant reduction in the first half of 2002. The main reason for the mixed performance seems to be a falloff in private residential building activity, which has been sluggish since 2001. After issuing 514 new mortgages over the first six months of 2001, finance houses (commercial banks, Barbados Mortgage and Finance Ltd. and trust companies) only issued 482 in 2002 and 475 in 2003.

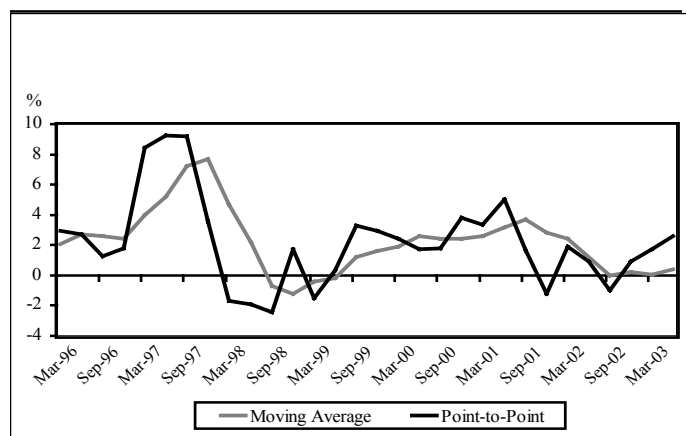
Other Non-Traded Sectors

The wholesale and retail trade, which benefited from the strong import demand, grew by about 2.7%, following a 2.0% decline in the similar period a year ago. Moderately higher output was also recorded in the business and other services and the electricity, gas and water sub-sectors with estimated output of 0.6% and 1.8% respectively. Conversely, mining and quarrying continued to deteriorate, contracting by an estimated 14.2%, due primarily to lower yields of crude oil, as well as stock adjustments in the quarrying industry in the first two quarters of the year. During this time, only one new well was brought into operation. This coupled with the natural decline in the productivity of previously drilled wells contributed to the decline in mining and quarrying.

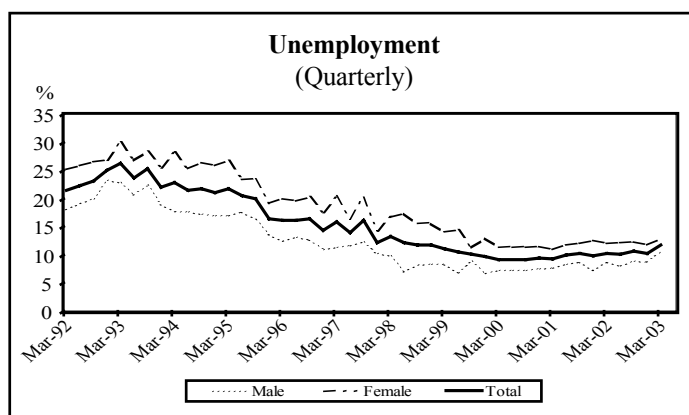
Electricity usage rose by 11.7% over the first six months of 2003, in contrast to a decline of 0.8% for the corresponding period in 2002. Commercial and industrial consumption expanded by approximately 12.5%, while residential usage grew by 9.7%.

Prices and Employment

At the end of May 2003, consumer prices went up marginally (0.4%) compared to a 1.7% rise for the corresponding period in 2002. Despite the overall absence of inflation,



several of the subcategories within the consumer price index registered higher prices. Among these were the medical and personal care, and the fuel and light indices, which increased by 5.2% and 6.4%, respectively. Housing and food prices also registered modest growth. These expansions were largely offset by a 6% fall in the cost of clothing and footwear and a 3.5% decline in the price of household operations and supplies. Transportation prices were lower by 0.8%, as falls in international airfares, and reductions in the prices of vehicle parts pushed down this category.



An expansion in the labour force of about 6,100 persons resulted in an overall rise in the unemployment rate, despite an increase in the total number of individuals employed. The rate of unemployment at the end of the second quarter of 2003 was 11.6%, some 1.5 percentage points above the figure for the same period a year prior. The male unemployment rate climbed to 10.2%, compared to 8.1% in the previous year, while the female rate rose to 13.1%, from 12.0% at end-June 2002. The most significant job losses occurred in government services, finance and business services, manufacturing and tourism services; however, there were noteworthy employment gains in general services, wholesale and retail, construction and transportation and communications, which caused the overall number of employed persons to increase by approximately 3,300.

Financial Sector

Deposits

Domestic deposits denominated in local currency grew over the first half of 2003 by 1.7% or \$71.6 million to reach \$4,398.9 million and was 9.1% less than the growth for the same period in 2002. Significantly higher deposit growth was registered for both public financial institutions (\$69.7 million) and statutory bodies (\$17.7 million), while the deposits of private financial institutions and central government declined by \$38.4 million and \$18.6 million during the review period.

Credit

Credit to the non-financial private sector fell by \$8.5 million (0.3%), which follows marginal increases of \$0.9 million in 2002 and \$4.4 million in 2001. This was primarily the result of major reductions in credit to private individuals (\$26.1 million) and the distributive sectors (\$14.9 million), which is in contrast to expansions of \$13.5 million and \$19.2 million, respectively for the first half of 2002. There was also a contraction of \$109.3 million in lending to private financial institutions, which reflects the repayment of a loan secured by Sagicor for the purchase of Life of Barbados. These major declines more than offset the rise of \$36.6 million in lending to statutory bodies. For the first two quarters, total loan from commercial banks fell by 3.8% to reach \$2,801.2 million.

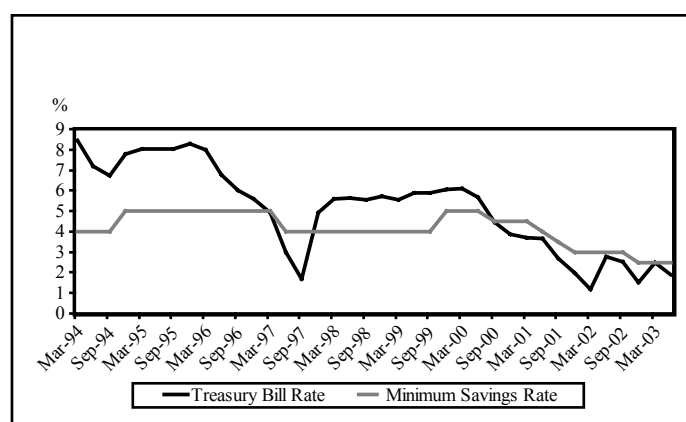
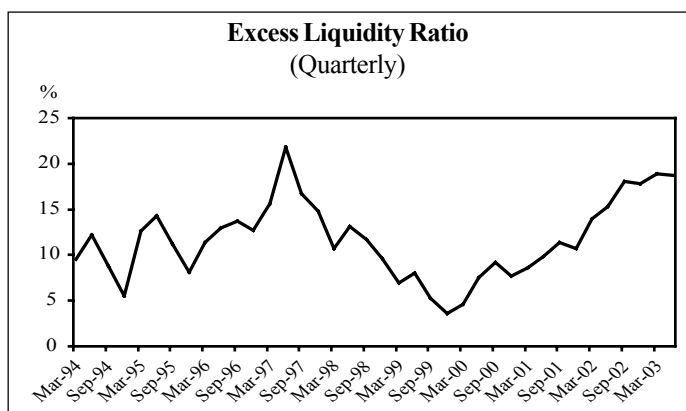
Liquidity and Interest Rates

During the first six months of 2003, the degree of excess liquidity in the financial system rose slightly due to weak credit demand and the growth in deposits. The excess liquidity ratio at the end of June 2003 was 18.7%, 0.9 percentage points higher than at December 2002. The marginal increase in the excess liquidity ratio resulted in the Trea-

Summary Accounts of the Banking System
(\$ Million)

	2001				2002				2003 ^P	
	Mar.	Jun.	Sep.	Dec.	Mar.	Jun.	Sep.	Dec.	Mar.	Jun.
Net International Reserve:	1,204.5	1,224.3	1,214.8	1,534.1	1,623.41	1,606.1	1,570.6	1,711.3	1,939.9	1,929.5
Monetary Authorities	1,096.4	1,115.5	1,106.6	1,414.1	1,482.3	1,485.3	1,441.3	1,366.4	1,357.9	1,379.5
Commercial Banks	108.1	108.8	108.2	120.0	141.3	120.8	129.3	344.9	582.0	550.1
Net Domestic Assets	2,167.0	2,234.3	2,266.3	2,002.5	2,004.9	2,133.6	2,157.2	2,186.4	1,944.8	1,973.6
Credit to Public Sector	25.5	120.9	124.8	(67.1)	(94.8)	(5.4)	158.3	366.9	349.5	335.3
Central Government (net)	337.3	405.7	477.2	241.6	235.0	390.7	553.2	659.3	644.2	684.0
Rest of Public Sector	(311.8)	(284.8)	(352.4)	(308.7)	(329.9)	(396.1)	(394.9)	(292.4)	(294.7)	(348.7)
Credit to Rest of Financial System	125.5	125.6	128.6	115.9	148.18	250.4	238.4	167.1	143.6	144.3
Liabilities to Other Financial Institutions	257.7	244.3	254.5	265.8	350.1	359.3	374.1	403.9	378.5	373.9
Credit to Private Sector	2,516.4	2,508.6	2,526.1	2,512.6	2,506.9	2,513.5	2,442.0	2,599.2	2,592.6	2,590.7
Liabilities to the Private Sector	3,371.6	3,458.6	3,481.1	3,536.8	3,628.3	3,739.7	3,727.8	3,897.7	3,884.8	3,903.1
Currency in Circulation	301.2	306.8	307.0	312.4	318.1	321.1	321.1	337.5	329.3	341.4
Demand Deposits	775.6	779.4	784.3	836.8	895.9	926.7	905.5	1096.6	1053.6	1,009.6
Time Deposits	390.7	418.2	425.0	413.1	399.1	417.2	384.0	345.9	347.7	341.1
Savings Deposits	1,904.1	1,954.2	1,964.9	1,974.5	2,015.4	2,074.6	2,117.2	2,117.7	2,154.1	2,211.0
MEMO:										
Domestic Deposits	3,794.7	3,866.1	3,978.1	3,971.8	4,183.2	4,417.7	4,360.6	4,524.7	4,430.0	4,505.1
Liquid Assets	1,055.5	1,080.4	1,075.4	1,392.4	1,459.9	1,471.4	1,436.5	1,365.5	1,256.6	1,382.4
Loans & Advances	2,721.3	2,722.5	2,757.1	2,732.5	2,771.5	2,876.2	2,792.8	2,910.3	2,811.0	2,801.2

Source: Central Bank of Barbados
P: Indicates Provisional



surety bill rate eventually decreasing to 1.91% at the end of the period from 2.51% at December 2002. The weighted average rate on total loans dipped 11 basis points to 10.24%, and the weighted average deposit rate fell by 4 basis points to 2.57%. The average lending rate for mortgages for the review period was 8.26%, compared to 8.74% last year.

Commercial Banks' Excess Cash
(BDS \$'000)
(End of Month)

Period	2001	2002	2003
January	114,664	152,370	322,771
February	139,937	220,974	367,840
March	77,458	208,026	325,459
April	128,134	294,952	428,860
May	134,072	382,413	443,985
June	124,185	368,351	368,147
Average	119,742	271,181	376,177

Government Securities

Acting as Government's fiscal agent, on May 2, 2003 the Central Bank of Barbados issued a 5.0% Treasury Note 2010, for a nominal value of \$30.0 million. This issue was heavily oversubscribed, as there continues to be a high demand for Government paper. During the first half of 2003, the Central Bank also offered two (2) Savings Bond issues with nominal values of \$5.0 million and \$15.0 million. Both issues were priced at a discount of \$80.74 to yield 4.779% over the five-year period.

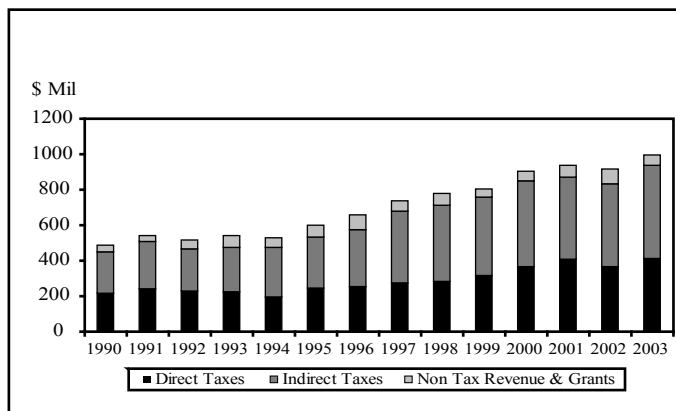
The nominal value of Debentures and Treasury Notes outstanding at June 30, 2003 was \$2.038 billion and it is anticipated that an additional \$100 million will be issued later in the year. The nominal value of Sinking Funds to service Government debt stood at BDS\$351.32 million as at end-June.

With low interest rates prevailing, the discount rate on 3-month Government Treasury Bills declined from 1.51% at the end of last year to 0.80% in early March. This was reversed near the end of the first quarter, when the 3-month discount rate rose to a high of 2.50% for the first six months of 2003. There were two auctions of 6-month Government Treasury Bills for the period, which resulted in an increase in the discount rate from 0.93% to 1.91% at the end of June.

Public Sector

Revenue

Total Government revenue increased by an estimated 8.0% (\$72.2 million), as both direct and indirect tax receipts expanded, more than offsetting a downturn in non-tax revenue. The intake of direct taxes rose by about 13.4% to \$414.1 million, in stark contrast to a decline of 10.7% during the similar period last year. Personal tax revenue grew by 8.7% to \$202.0 million, boosted partly by higher incomes and improved collection of arrears. Additionally, increased corporate profitability resulted in corporation taxes surging by approximately 31.6% to \$161.7 million, a turnaround from the 21.8% reduction in 2002. Receipts from property taxes fell by 8.8% (\$2.6 million) during the review period, after declining by 22.4% in the corresponding period a year ago.



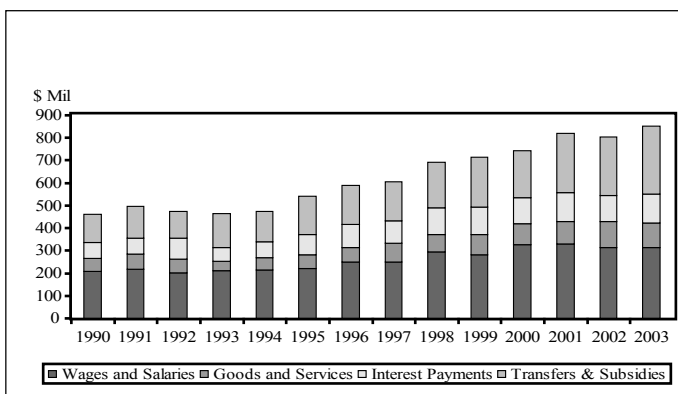
Indirect tax revenue was up by about 8.2% over the January-to-June period, fuelled primarily by an increased intake of VAT and excise taxes.

VAT receipts expanded by 7.6% to \$282.9 million due to strong second quarter economic activity. Excise taxes rose by 16.5% (\$9.8 million), which is in contrast to an equally significant decline of 28.2% (\$23.3 million) for the same period in 2002. while import duties decreased by 2.5% during

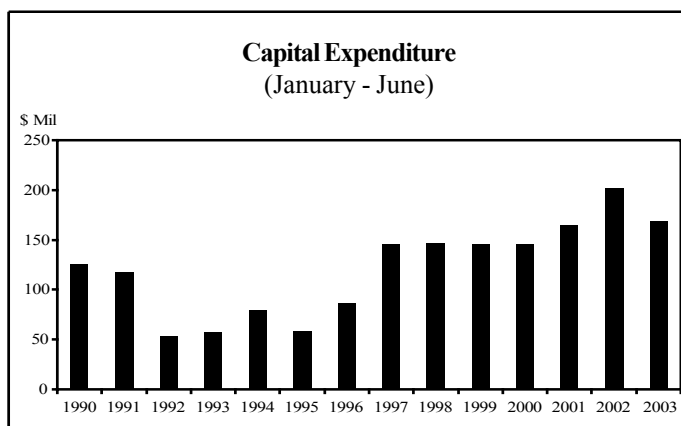
the corresponding period of 2003. Non-tax revenue shrank by an estimated \$15.0 million, following three straight years of relatively strong growth.

Expenditure

Driven primarily by greater outlays on interest payments and transfers and subsidies, current expenditure on government's operations expanded by approximately 6.7%



(\$53.9 million) in the first two quarters of 2003, a reversal of the small contraction recorded during the comparable months of the previous year. Interest expense was 12.5% above the level in 2002, primarily because of a considerable rise in the domestic debt component, which more than offset the decline in the foreign component. The increase in transfers and subsidies (15.8% or \$41 million) largely reflected an expenditure reclassification, as the



Government Operations
January - June
(\$ Million)

	1998	1999	2000	2001	2002	2003 ^P
Total Current Revenue	780.2	802.7	903.3	936.2	914.8	986.9
Tax Revenue	714.3	758.5	851.9	872.8	833.7	920.8
<i>Direct Taxes</i>	282.7	315.0	365.0	409.4	365.5	414.1
a) Personal	147.8	147.5	174.2	182.2	186.0	202.0
b) Corporate	85.7	118.9	136.1	157.1	122.9	161.7
c) Levies	8.0	8.8	6.1	10.9	8.7	4.7
e) Property	25.5	25.2	32.5	37.9	29.4	26.9
f) Other	15.7	14.6	16.1	21.3	18.5	18.8
<i>Indirect Taxes</i>	431.6	443.4	486.9	463.4	468.2	506.7
a) Consumption	0.3	0.0	0.5	0.0	0.0	0.0
b) Stamp	6.7	6.9	7.1	7.5	5.6	6.8
c) VAT	224.3	215.1	260.3	257.5	263.0	282.9
d) Excises	83.6	98.3	86.9	82.7	59.4	69.1
e) Import Duties	64.0	70.3	69.4	57.4	79.3	77.3
f) Hotel & Restaurant	0.4	0.4	0.4	0.3	1.0	0.4
g) Other	52.3	52.5	62.3	57.9	59.9	70.6
Non Tax Revenue & Grants	65.9	44.2	51.4	63.4	81.1	66.1
Current Expenditure	691.9	713.5	743.1	819.4	803.9	856.2
Wages & Salaries	293.5	283.4	327.8	329.1	314.3	318.4
Goods & Services	76.8	89.5	92.8	99.7	113.9	109.6
Interest Payments	118.3	121.0	115.0	128.5	116.0	128.5
External	24.7	5.2	36.0	53.1	56.4	80.1
Domestic	93.6	115.8	79.0	75.4	60.5	48.4
Transfers & Subsidies	203.3	219.6	207.5	262.0	258.9	299.7
Current A/C Balance	88.3	89.2	160.2	116.8	110.9	130.7
Capital Expenditure	147.2	146.3	146.2	164.2	201.7	168.7
Net Lending	0.4	0.4	2.9	10.9	2.0	3.4
Total Expenditure & Net Lending	839.5	860.2	892.2	994.4	1,003.6	1,028.3
Overall Balance	(59.3)	(57.4)	11.1	(58.2)	(88.8)	(41.4)

Source: Central Bank of Barbados and Accountant General

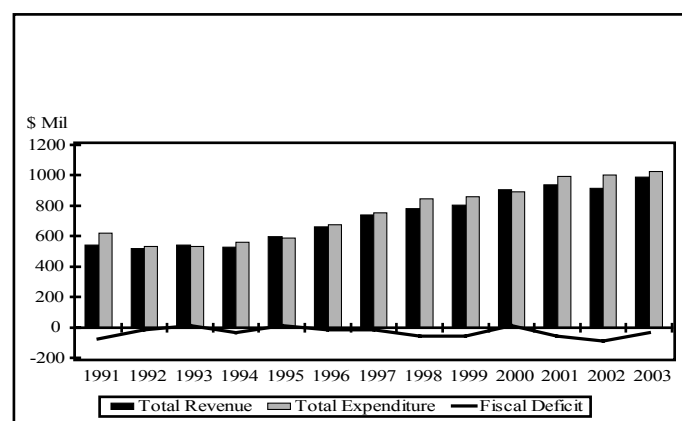
P: Provisional

administration of the Queen Elizabeth Hospital was placed in the hands of a statutory board in the second quarter. Consequently, there was a 3.8% reduction in goods and services, but wages and salaries increased by 1.3% on account of a rise in public sector employment during the period.

On-budget Capital expenditure was estimated to have decreased by 16.0% (\$33 million), following expansions of 22.8% and 12.4% in the comparable six months of 2002 and 2001, respectively. The fall-off in capital expenditure reflected the winding down or completion of some of Government's major capital works projects, such as the South Coast Sewerage Project and the Forensic Science Centre. However, off-budget capital expenditure is estimated to have been significant.

Financing

Government financed its fiscal deficit mainly through the use of domestic resources. In particular, the Central Bank and the National Insurance Scheme contributed approximately \$32.8 million and \$25.2 million, respectively, while commercial banks declined by \$12.1 million and private non-bank institutions supplied around \$8.4 million in funding. However, the government reduced its liabilities to other domestic entities by about \$17.4 million.



Source: Central Bank of Barbados

P: Provisional

Net foreign financing totalled \$4.5million, compared to \$2.4 million one year ago, as project fund inflows of \$40 million, outstripped amortisation payments of \$35.5 million.

Government Financing (\$ Million)

	January-June			
	2000	2001	2002	2003 ^P
Domestic Financing	(211.9)	-3.7	86.4	22.2
Central Bank	(352.5)	(46.2)	105.8	38.1
Commercial Banks	40.3	23.1	61.0	(9.3)
National Insurance Scheme	71.6	22.4	33.6	39.9
Private Non-Bank	42.1	33.1	(22.0)	46.5
Divestment	0.0	52.2	0.0	0.0
Other	(13.5)	36.1	(81.8)	(79.7)
Foreign Financing (net)	200.8	14.3	2.4	7.4
Capital Markets	200.0	0.0	0.0	0.0
Project Funds	22.1	36.3	21.0	37.2
Policy Loans	0.0	0.0	0.0	0.0
Amortisation	(21.3)	(22.1)	(18.7)	(29.8)
Divestment	0.0	0.0	0.0	0.0
Total Financing	(11.2)	58.2	88.8	(42.9)

Foreign Trade and Payments

Current Account Developments

During the first half of 2003, the current account of the balance of payments recorded a deficit of \$89.9 million, which is in contrast to the average first-half surplus of \$40.7 million in the preceding three years and is the largest deficit ever registered for the period. This was as a result of a surge in retained imports together with sluggish domestic exports, which more than offset the improvement in travel credits.

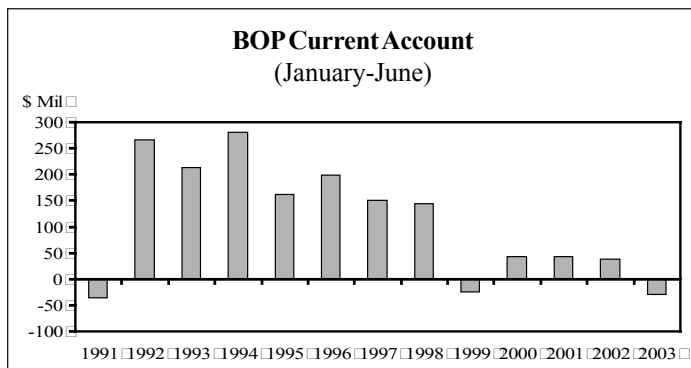
Domestic exports posted a slight increase of about 1%, in contrast to declines of 10.4% and 7.5% in 2002 and 2001. This outcome stemmed principally from an expansion in the exports of miscellaneous goods (11.7%), which outweighed losses in exports of electronic components (9.1%), food and beverages (8%) and chemicals (2.1%). Despite the overall decline in the exports of food and beverages, rum exports grew by 11.9% compared to 8.1% for the same period last year. Foreign income from sugar was also marginally lower

Balance of Payments
(January-March)
(\$ Million)

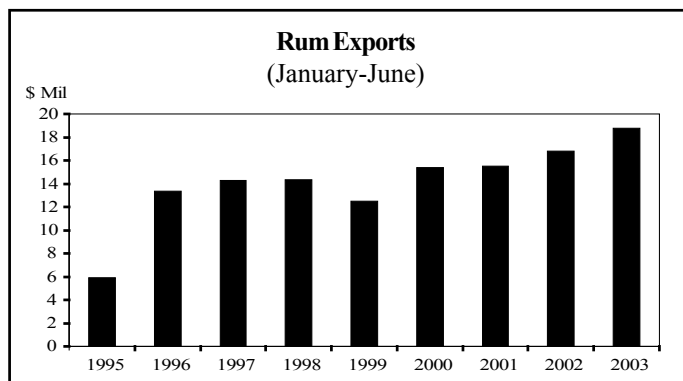
	1999	2000	2001	2002	2003 ^P
Current Account Balance	(23.7)	43.5	43.5	35.0	(89.9)
Merchandise Trade	(697.5)	(659.2)	(664.2)	(626.0)	(746.9)
Total Exports (BOP basis)	230.3	243.4	244.7	197.7	164.6
<i>Domestic Exports</i>	216.5	217.3	200.9	180.1	181.2
Sugar	52.4	52.2	44.0	37.7	37.5
Electrical. Comp	30.4	18.9	19.8	13.7	12.4
Chemicals	24.3	26.2	21.5	20.9	20.5
Food/Bev	40.2	43.3	44.5	44.8	41.2
All Other	69.2	76.7	71.1	63.0	69.7
Total Imports (BOP basis)	991.9	968.5	969.6	878.9	974.4
<i>Retained Imports</i>	1046.8	1012.2	997.3	926.5	1067.1
Consumer Goods	439.3	408.2	403.2	388.1	412.9
Capital Goods	260.8	238.4	217.8	198.5	240.4
Intermediate Goods	344.8	362.0	372.8	336.5	410.5
Miscellaneous Goods	1.9	3.6	3.5	3.4	3.3
Services (Net)	673.3	710.8	712.5	659.1	686.6
Travel Credits	798.5	835.8	847.9	771.5	802.9
Other	80.7	90.3	82.6	72.5	74.1
Investment Income (net)	(61.0)	(81.4)	(95.8)	(84.7)	(115.7)
Transfers (net)	61.5	73.3	91.0	86.7	86.2
Capital and Financial Account	192.3	451.6	90.7	40.4	70.9
Long term	168.9	388.4	117.0	36.4	70.9
Public Sector	148.7	231.5	(2.3)	(7.8)	(33.8)
Disbursement	170.5	256.6	27.1	21.1	40.0
Amortization	21.8	25.1	29.3	28.9	73.8
Private Sector	20.2	156.9	119.2	44.2	104.8
Disbursement	27.9	162.8	120.1	48.3	108.9
Total Outflows	7.7	5.9	0.9	4.1	4.1
Other	(9.0)	40.8	22.7	4.0	0.0
Short-term	32.4	22.4	(3.5)	0.0	0.0
Errors & Omissions	113.0	(39.4)	(10.1)	(3.4)	209.0
Balance for Official Financing	281.6	455.7	144.3	72.0	218.3
Official financing (net)	0.0	0.0	0.0	0.0	0.0
IMF	0.0	0.0	0.0	0.0	0.0
Other Financial Institutions	0.0	0.0	0.0	0.0	0.0
Reserve movements (CBB basis) □					
(-Increase/+Decrease) □	-281.6	-455.7	-144.3	-72.0	-218.3
Change in NIR (IMF basis) □					
(-Increase/+Decrease)	-221.0	-425.5	-146.5	-71.2	-13.1

Source: Central Bank of Barbados and Accountant General

P: Provisional



during the review period. Nevertheless, with the upswing in tourism activity, travel credits grew by 4.0%, following a 9% downturn in the corresponding period a year ago.



Boosted somewhat by the pick-up in economic activity, retained imports expanded by about 15.2% as businesses replenished their inventories. This is in contrast to the 7.1% drop in the equivalent period of 2002, when all categories of imports contracted because of the running down of business inventories. The turnaround was broad-based, with imports of capital goods and intermediate goods increasing by 22% and 21.9%, respectively, while consumer goods imports rose by 6.4%.

Capital and Financial Account Developments

The capital and financial account of the balance of payments recorded an estimated surplus of \$70.9 million during the first half of 2003, some \$30.5 million more than the sur-

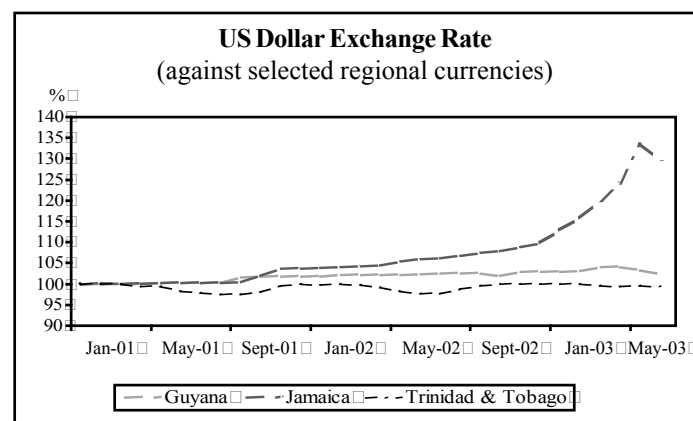
plus recorded last year, and \$19.8 million below the amount in 2001. Net long-term private sector capital inflows amounted to approximately \$104.8 million or \$60.2 million in excess of the previous year's figure. However, net long-term public capital outflows during the review period totalled \$33.8 million, \$26 million more when compared to the same period of 2002. This outcome reflects the repayment of a \$30.0 million loan by the Government of Barbados on behalf of Hotels and Resorts Ltd in the first quarter.

Regional Economic Developments

Overview

Against a background of tensions in the Middle East and uncertainty in the international arena, real economic activity in CARICOM was generally positive in most islands for the first quarter of 2003. During this time, there was a mixed tourism outturn as the industry's performance was largely influenced by external factors. Inflationary pressures remained subdued despite higher energy costs.

The foreign exchange market was also generally stable with the exception being Jamaica, which experienced a major crisis that resulted in the Jamaican dollar trading at a historical low in May 2003. Fiscal operations by the various gov-



NOTE: The exchange rate data are monthly averages that are indexed to January 2001. Exchange rates are in foreign currency units per dollar.

ernments were mixed with a sizeable surplus being registered in Trinidad and Tobago, while deficits of varying proportions were recorded for the other countries.

The Bahamas

Tourism output improved during the first three months of 2003, as an increase in room rates outweighed weak trends in visitor volume. Softening of US travel demand, as a result of fears related to the war in Iraq, lowered growth in visitor arrivals to 1.1% from 3.0%, to a first quarter count of 1.2 million. Air arrivals increased marginally (0.3%), in contrast to a 5.8% contraction in 2002. Conversely, cruise visitor growth slowed sharply to 1.4% from 7.5% in 2002, and was largely sustained by continued popularity of the Family Islands.

Estimates of the fiscal performance for fiscal year 2002/03 indicate a widening in the overall deficit, to \$45.7 million from \$2.5 million in the same period in FY2001/02. In contrast to almost unchanged revenue collections of \$218.8 million, total expenditure rose by 20.0% to \$264.6 million, under the impact of an appreciable hike in budgetary support to public sector entities. However, capital spending was cut by \$5.9 million (26.7%), partially offsetting the \$12.8 million (5.7%) upswing in recurrent outlays. Budgetary financing included significant short-term funding from the local banking sector.

Estimates indicate a marginal increase in the current account surplus to \$6.0 million in first quarter of 2003, from \$0.7 million in the corresponding period of 2002. Appreciating oil prices pushed up the merchandise trade deficit by 13.2% to \$296.6 million, but this was more than countered by a 9.2% improvement in the services surplus to \$296.8 million, and a one-third decrease in net factor income outflows to \$30.9 million. Net transfer receipts were also slightly higher at \$13.0 million. The capital and financial account registered an estimated deficit of \$68.8 million in contrast to

the 2002 surplus of \$89.7 million. Short-term flows through the banking system were reversed to a net outflow of \$76.9 million from a net inflow of \$40.9 million in 2002. In addition, net private equity inflows narrowed to \$9.5 million from \$34.0 million; net real estate sales, to \$3.9 million from \$9.9 million, and net private loan receipts, to \$10.7 million from \$18.6 million. The public sector's net external debt repayment increased to \$6.9 million from \$5.1 million.

Jamaica

Leading indicators of economic performance suggest an expansion in real GDP during the first quarter of 2003, which was much stronger than the growth of 0.7 percent recorded in the first quarter of 2002. Economic growth was estimated to have occurred in both the goods and services sectors. The estimated expansion in the goods producing sectors reflected improvements in mining and construction. Growth in services was driven by the performances of utilities and the tourism industry. The overall growth in the review quarter was consistent with the trends in credit demand. From the perspective of aggregate demand, the expansion in economic activity reflected estimated increases in both private and public sector consumption, which were partially offset by declines in public and private sector investment, as well as a reduction in net external demand.

Value-added in the Mining sector is estimated to have increased in the first quarter of 2003, relative to the corresponding quarter in 2002. This growth was primarily attributable to the production of alumina, which grew by 7.0 percent. This was, however, partially offset by a decline of 12.8 percent in the production of crude bauxite. Notwithstanding the contraction in crude bauxite, the level of production was approximately 10.0 percent higher than the average production level between 1995 and 2002. The growth recorded in alumina production partly reflects reduced output at one of the alumina processing plants in the first quarter of 2002.

The Currency Crisis in Jamaica

The instability that characterized the foreign exchange market in the latter part of the December 2002 quarter intensified in the first half of 2003 with the weighted average selling rate depreciating by 14.8 percent for the period. The movement in the exchange rate during the year was mainly influenced by a fall in market confidence triggered by a deterioration in the balance of payments and fiscal accounts, and the related downgrade of Jamaica's sovereign debt by Standard and Poor's (S&P). In addition, high levels of Jamaican dollar liquidity in the money market helped to push down the value of the Jamaican dollar. In order to address the macroeconomic imbalances in the economy and to ensure orderly adjustment in the exchange rate, the Bank of Jamaica (BOJ) tightened monetary policy at different points over the review period and augmented the supply of foreign exchange to the public.

Market pressure on the Jamaican dollar that had emerged in December deepened towards the end of February 2003 as Government opted to purchase foreign exchange from the BOJ to repay a maturing Eurobond, rather than issue new international debt. The withdrawal from the international market contributed to a sharp reduction in the price at which Government of Jamaica (GOJ) bonds were traded. This ultimately triggered a margin call on some domestic financial institutions by a large international brokerage house in March 2003, resulting in an increase demand for foreign exchange. The increased demand for US dollars in the first quarter was facilitated by significant Jamaica Dollar liquidity in the money market.

Since the beginning of the year, the Jamaican currency was caught in a vicious downward cycle, which the authorities said was caused by speculative trading and hoarding of the US dollar that created an artificial shortage in the market and at the same time stirred up enough panic to create artificially high demand for the currency. Moody's Financial Services placed a credit watch on Jamaica, and following this announcement, the Jamaican dollar continued its gradual

decline against the US dollar with the rate slipping to a historic low of J\$71 against the dollar during the week of May 12, compared to J\$50.18 at the end of 2002. This represents the sharpest depreciation on record. In response, the Prime Minister of Jamaica P.J. Patterson announced that the Central Bank would implemented a mix of policy measures designed to reduce local currency liquidity together with an appeal to the common sense of businesses and Jamaicans in general. On May 19, the Central Bank intervened on the foreign exchange market and attempted to meet the demand for foreign currency by selling an initially US\$100 million. In addition, on May 23, the Bank issued a 12% US-dollar indexed bond at a face value of J\$57 to the US\$1 dollar, making this the highest interest rate on offer by the Jamaican Government in two years. These actions were positively received by the market and subsequently led to a revaluation in the Jamaican dollar. At the end of June, the Jamaican dollar traded at J\$58.92 to the US dollar, representing a depreciation of about 14.8% from the beginning of the year, and partly confirms the view that the depreciation was partly manifested by a short-term lack of confidence, which caused a higher than normal demand for US dollars.

Even though the Jamaican Government anticipates improved economic growth, one of the economy's major components - tourism - has been dampened by the US-led war in Iraq and the impact of the Severe Acute Respiratory Syndrome (SARS). With such vulnerabilities to the tourism sector and the recent fiscal and currency challenges, at the end of May Moody's announced a downgrade of Jamaica's foreign currency and domestic debt.

Jamaican's foreign currency bonds and issuer rating were downgraded to B1 from Ba3, while its foreign currency deposits were lowered to B2. Moody's cited the high deficit and debt indicators as limits to any additional fiscal adjustment in Jamaica, thereby increasing the economy's vulnerability to shocks. On average, the outlook for these ratings remains stable due to the potential benefits of the sizeable adjustments made in the FY/2003 budget

Relative to the March 2002 quarter, there were estimated expansions of 24.3% and 7.0%, respectively, in visitor arrivals and expenditure during the review period. Cruise arrivals increased by 46.9% while stopovers expanded by 6.9%. The growth in cruise arrivals is due to larger vessels calling at the ports. Additionally, two new vessels called at the Jamaican ports in the March 2003 quarter.

The headline inflation rate for the first three months of the year was -0.4%. This outturn was below the inflation rate in the preceding quarter and that of the corresponding quarter of 2002. The deflation during the quarter reflected the recovery of domestic agricultural supplies, notwithstanding strong inflationary impulses from international commodities. Core inflation remained stable at 1.3% in relation to the December quarter.

Provisional data indicate that for the March quarter Central Government operations resulted in a deficit of \$1407.4 million or 0.4% of GDP, relative to a surplus of \$1500.0 million targeted under the IMF's Staff Monitored Programme (SMP). The deviation in fiscal performance largely reflected higher than anticipated expenditure, which just outweighed buoyant revenue flows. Divestment proceeds and domestic borrowing facilitated the financing of the deficit. The amortization of external debt exceeded the programme target, as a •200.0 million Eurobond that matured during the quarter was not reissued.

Organisation of Eastern Caribbean States (OECS)

During the first quarter of 2003, economic activity in the Eastern Caribbean currency union improved relative to the performance in the corresponding quarter of 2002. This improvement was partly on account of increases in value-added in the construction, manufacturing, and wholesale and retail trade sectors. There was a weak performance in the agricultural sector, reflecting a downturn in the banana industry and the tourism industry is estimated to have declined.

The merchandise trade deficit widened, attributable in part to lower export receipts and reflects the weak performance of the major export sectors. The current operations of the combined central governments resulted in a deficit that was below the level for the first quarter of 2002. Developments in the banking system were characterised by growth in broad money and net foreign assets. Liquidity of the commercial banking system increased during the quarter under review, while interest rates were virtually unchanged.

Construction activity expanded, but the pace slowed during the review period compared with the corresponding period in 2002 as some major projects in the private and public sectors came to an end or neared completion.

Performance in the agricultural sector was generally weak, partly reflecting the adverse effects of unfavourable weather. Banana production fell by 38.0% to 17,587 tonnes, well below the amount in the quarter ended March 2002 as all the banana producing territories recorded declines in production, mainly as a result of damage to the crop by tropical storm Lili in September 2002 and a drought experienced during the first quarter of 2003.

The tourism industry in the currency union was adversely affected by the US led war on Iraq. Total visitors to the region declined by 12.5% to 814,998, reflecting contractions in both stay-over visitors and cruise ship passengers. Arrivals fell in all countries with the exception of Dominica where visitors rose by 1.9%. The largest decline was reported for St Kitts and Nevis (31.4%). Despite a 24.5% decrease in visitors to St Vincent and the Grenadines, activity increased, as hotel occupancy levels and length of stay were well above the levels in the first quarter of 2002. This was mainly as a result of the presence of a Disney film production crew during the first quarter. Stay-over visitors fell by 3.7% to 230,263, reflecting decreases in all the member countries except Antigua and Barbuda and Dominica, which recorded increases of 2.2% and 9.9% respectively. With the exception

of the UK (up 0.2%), all of the major markets recorded declines in arrivals as follows, USA (2.6%), the Caribbean (8.6%) and Canada (5.7%).

The number of cruise ship passengers fell by 16.4% to 522,557, consistent with the decline in cruise ship calls mainly as a result of the cancellation of visits to some of the member countries by a major cruise line. The decline in cruise ship visitors contributed to a contraction in the value added for road and sea transport.

Available information on consumer prices movements in the member countries (excluding Antigua and Barbuda) in the first quarter indicates that inflation in the currency union remained low. This performance was partly influenced by the low rates of inflation in the major trading partners.

The fiscal operations of the central governments combined for the quarter under review revealed a narrowing of the current account deficit to \$13.0 million compared to \$22.2 million in the corresponding quarter of 2002. The improvement reflected faster growth in current revenue (4.4% to \$509.1 million largely reflecting higher collections of tax revenue) relative to the increase in current expenditure (2.4% to \$522.2 million, largely influenced by an increase in outlays on personal emoluments). Capital expenditure and net lending amounted to \$103.1 million, 18.5% below the total in the corresponding quarter of 2002. The lower current account deficit combined with the contraction in capital spending resulted in a smaller overall deficit of \$87.0 million. The deficit was financed largely from external sources.

Trinidad and Tobago

In the face of international uncertainties, the Trinidad and Tobago economy performed creditably as real output grew, inflationary pressures remained subdued and the central government posted a fiscal surplus for the first quarter

of 2003. While the demand for credit stagnated, the foreign exchange market continued to experience excess demand pressures arising from regional investments by the local private sector and increased activity by regional sovereign borrowers.

Despite the temporary slowdown of activity in the energy based industries, real output grew by 1.4% in the first quarter because of strong performances in Agriculture and the Transport, Storage and Communication (TSC) sectors. Although the output from sugar was lower than projected because of production shortfalls associated with severe dry weather, real value added in Agriculture grew by 13.7% compared with 21.7% for the same period in 2002. The labour unrest in Venezuela together with an unusually high number of cruise ship arrivals resulted in increased activity in TSC (7.3%).

A prolonged dry season led to higher food prices and some acceleration in the consumer price index, especially in the month of March. However, the overall rate of inflation for the first three months of 2003 was 3.1%, down from the 4.2% rise in prices in the last quarter of 2002. The unemployment rate rose for the second consecutive quarter to 11% from 10.4% and the end of 2002 as job losses in the manufacturing and services sectors outnumbered the job gains in the construction sector.

There was an improvement in the operations of the central government that led to a surplus of \$128.7 million for the first quarter thereby reducing the cumulative deficit for the first half of the fiscal year to \$71.3 million. The combined effect of an increase in revenues and contraction in expenditure produced this favourable outturn. The expansion of revenue was mainly attributed to developments in the oil sector. Even though petroleum production declined, higher oil prices, which averaged US\$34.33 per barrel in the first quarter, up from US\$27.30 in the previous quarter, brought about a 33% increase in oil receipts. Higher petroleum rev-

enues offset a decline of 10.5% in non-oil revenues. Despite an increase in the wage bill to settle outstanding salary arrears, government expenditure declined, as there was a reduction in transfers and subsidies as well as lower interest payments.

The high level of liquidity in the banking sector that prevailed in the last quarter of 2002 continued into the first quarter of 2003. However, net open market operations of \$390 million in March and interventions in the foreign exchange market of US\$86.6 million during February and March helped to reduce excess liquidity.

International Economic Developments

Overview

Global economic activity remained positive, though sluggish in the first half of 2003, with the growth in real output in the United States, the Euro area and Japan changing little from the previous quarter. Geopolitical uncertainties, higher oil prices, slow growth in the United States, persistent weakness in global high-tech sectors, and continued negative wealth effects from past declines in equity prices all weighed on growth. Economic expansion appeared to have remained weak in the second quarter despite the reduction in uncertainty associated with Iraq. Indicators suggest that manufacturing activity remained stagnant, with industrial production declining on average during the second quarter, relative to the first quarter in Japan, Germany, and France. Concerns over the spread of the SARS virus seemed to have hurt growth in the second quarter in several Asian developing economies and in Canada.

Central banks in several major industrial countries moved to ease monetary policy during the first half of this year. The European Central Bank (ECB) and the central banks of the United Kingdom, Sweden, Switzerland, Norway, and New Zealand all cut official interest rates. The pace of

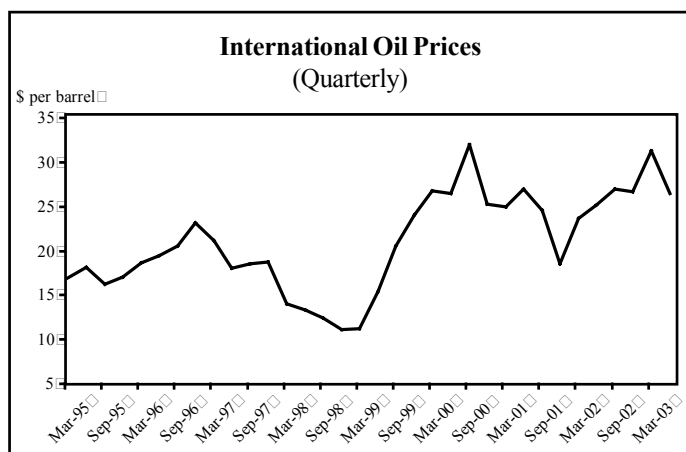
monetary easing in Europe picked up toward midyear, as inflationary pressures dissipated amid growing industrial slack, currency appreciation vis-à-vis the US dollar, and the decline in oil prices after the conflict in Iraq. In contrast, the Bank of Canada raised interest rates twice in the spring, in a continued effort to contain inflation. The Bank of Canada left rates unchanged in June, however, in response to a sharp appreciation of the Canadian dollar and a drop in Canadian inflation in April. The Bank of Japan (BOJ) maintained short-term interest rates at near-zero levels, further expanded its target for current account balances held by financial institutions at the BOJ, and took additional measures to stimulate the economy.

Industrial Economies

Economic activity in the United States remained sluggish in the first half of 2003. Businesses continued to be reluctant to undertake new projects given the unusual degree of uncertainty in the economic environment, and the softness in activity abroad crimped the demand for U.S. exports. However, consumer spending grew moderately, housing activity retained considerable vigour, and defence spending picked up. Real GDP rose at an annual rate of just 1.5 percent in the first quarter and appeared to have posted another modest gain in the second quarter. With output growth remaining tepid and labour productivity rising at a fairly robust pace, firms continued to trim payrolls in the first half of 2003, though job losses in the private sector were a little smaller than they had been in 2002.

For much of the first half of the year, movements in energy prices, which soared during the winter and retreated during the spring, shaped headline inflation news. Core inflation—which excludes the direct effects of food and energy prices—was held to a low level by slack in resource utilisation and continued sizeable advances in labour productivity. As a result of slow economic growth and the prospect that inflation would remain very subdued, the federal funds rate was maintained at the accommodative level of

1.25 percent for much of the first half of the year. Intermediate and longer-term yields declined, in some cases to their lowest levels on record. Equity prices, which through mid-March had fallen in response to weaker-than-expected economic news and rising geopolitical tensions, began a broad rally as it became clear that the war in Iraq would begin imminently. The apparent increase in investors' appetite for risk also helped push down risk spreads on corporate bonds and triggered inflows to equity and high-yield bond mutual funds. Since the beginning of the year, the value of the dollar has depreciated nearly 5 percent against the broad group of currencies of the U.S. major trading partners.

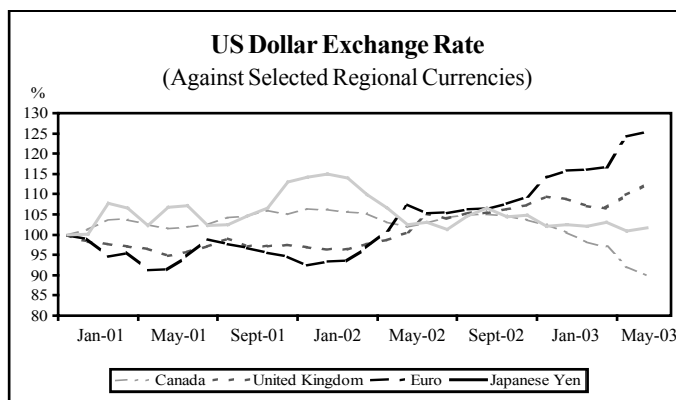


Canada's economy maintained a moderate pace of expansion in the first quarter, but recent indicators suggest that growth of real GDP slowed in the second quarter. First-quarter growth was supported by continued strength in domestic demand, as Canada's strong labour and housing markets propelled the economy. However, exports declined in the first quarter, largely because of a decline in exports of industrial supplies and forestry products to the United States. More recently, employment decreased slightly in April and May, and consequently the unemployment rate climbed. The outbreak of the SARS virus in Toronto hurt Canadian travel and tourism, and weak U.S. demand slowed the Canadian manufacturing sector. In June, employment rebounded, but

the gain was almost all in part-time work, and manufacturing employment continued to fall.

The euro-area economy stagnated in the first quarter of 2003. Consumer spending continued to expand at a modest rate and inventory investment grew, but business fixed investment fell sharply and exports declined. The German economy contracted in the first quarter and continued to under-perform relative to the euro-area average, in part owing to a fiscal tightening undertaken to bring the budget deficit into line with limits set out in the euro area's Stability and Growth Pact. The rise in the exchange value of the euro over the past year has begun to hurt euro-area manufacturers; exports have levelled off while imports have continued to rise. Recent indicators have shown little rebound in the pace of euro-area activity following the conclusion of the Iraq war, and business and consumer sentiment have remained sour. Core inflation has slowed from its 2002 peak, and inflation, which was temporarily boosted by oil prices, has fallen to the 2 percent upper limit of the ECB's definition of price stability.

Economic growth in the United Kingdom stagnated in the first quarter, but recent indicators—such as consumer confidence and industrial production—suggest that the pace has been somewhat stronger during the second quarter. Growth of consumption has slowed but continues to be held up by a strong labour market and by past gains in housing



NOTE: The exchange rate data are monthly averages that are indexed to January 2001. Exchange rates are in foreign currency units per dollar.

prices, although lately these price increases have slowed.

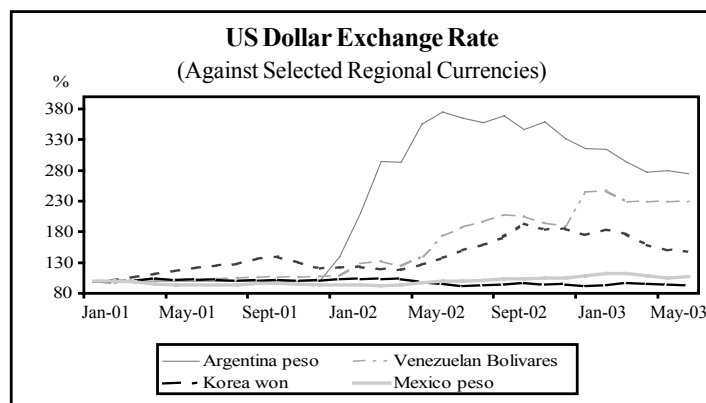
The Japanese economy barely grew in the first quarter after expanding almost 2.5 percent in 2002. Business investment continued to expand in the first quarter, and private consumption increased despite stagnating incomes. However, residential and public investment both fell sharply, and exports declined because of the weak global economy. The severity of consumer price deflation lessened somewhat, partly because of the spike in energy prices.

Emerging Market Economies

Economic growth in the Asian developing countries slowed in the first quarter, brought on by weakness in business investment and consumer spending. In South Korea, growth of real GDP turned negative in the first quarter after a rapid expansion in 2002. Tensions with North Korea contributed to a decline in consumer and business sentiment, but these indicators have stabilised in the second quarter. The Hong Kong economy also contracted, following strong growth in the second half of last year. The SARS outbreak held down both personal consumption and tourism in the first quarter, and even more negative effects are likely to be seen in the second-quarter data. Although the Chinese economy has also been adversely affected by SARS, it has been sustained by strong export growth and investment. Chinese inflation has moved back into positive territory on a twelve-month basis, largely owing to higher prices for energy and food.

The Mexican economy contracted in the first quarter, and exports and business confidence have declined in recent months. Consumer price inflation declined during the second quarter, helped in part by the net appreciation of the Mexican peso since early March. Measures of inflation expectations suggest that market participants expect the central bank to come close to achieving its inflation target this year.

Brazilian economic growth stagnated in the first quarter largely as a result of the tightening of macroeconomic policies in response to the financial crisis that erupted in mid-2002. The growth slowdown largely reflected a continued weakening in domestic demand, but exports also deteriorated. Monthly inflation has come down since early this year, and Brazil's central bank recently lowered its benchmark interest rate. The Lula administration's efforts to implement social security and tax reforms have bolstered investor confidence. Financial conditions in Brazil have improved markedly and as a result equity prices have risen more than 20 percent so far this year, while the *real* has gained more than 20 percent against the U.S. dollar. Credit spreads on Brazilian government debt have also narrowed by more than 600 basis points.



NOTE: The exchange rate data are monthly averages that are indexed to January 2001. Exchange rates are in foreign currency units per dollar.

The Argentine economy has started to turn around from the sharp contraction that occurred in the wake of the devaluation and default in late 2001, but the level of economic activity remains far below pre-crisis levels. The Argentine peso appreciated more than 20 percent against the dollar during the first half of the year.

International Outlook

Global economic activity is expected to strengthen later this year and in 2004, supported by further fiscal and mon-

etary stimuli and the broad-based improvement in financial conditions. Overall, GDP should grow around 2.5 % in 2003, and the pace of economic activity should accelerate to 3.5 % in 2004. Much of the optimism is directed toward the US where data point to a rebound in the second half of 2003, but there are also signs of improvement in Japan and the UK. However, the euro zone economy remains very weak and is entering the second half without much momentum.

Activity in the Euro area is expected to be very modest this year but should pick up to around 2.5 percent in 2004, with Germany and the Netherlands lagging France and Spain. An improvement in the second half of 2003 is anticipated as interest rate cuts, lower inflation and a rebound in the US take effect. However, growth for the year as a whole will be well below trend. Business investment may only recover in 2004, given the current significant surplus of spare capacity and pressures on profit margins.

Growth in the UK should accelerate in the second half

of 2003, given the very expansionary stance of fiscal and monetary policy and the likely improvement in the global economy. Overall, the UK economy looks well placed to take advantage of the global upswing, which is expected to commence in the remaining months of 2003. With growth strengthening in the second half, GDP should rise by 2% in 2003 as a whole. GDP growth may average 2.5% in 2004.

Emerging economies in Asia are expected to track the US business and consumer expenditure, as these countries benefit from renewed demand for high tech products. The region should average 5.5% growth in 2003 moving to 6% in 2004 as imports and business spending on high tech equipment improved gradually in the US. The continuing problems in equity markets and the related weak consumer confidence have also been a drag on growth, except in China. Relatively higher energy prices, business uncertainty caused by security risks, the fall-out from the SARS epidemic and concerns about global economic prospects would also temper growth prospects for this region.





Regional and International Capital Markets

Caribbean Stock Markets: 2003 Half-Year Summary.

Barbados Stock Exchange (BSE)

During the review period, the BSE index declined by 5.77% with volume 24,786,011, which saw 10 companies advancing, 8 declining and 6 remaining unchanged. The best performing company was Grace Kennedy & Co. Ltd, up 52.38%, whilst the worst performing company on the BSE was Cable & Wireless Barbados down 30.77%. Sagicor Financial Corporation was the largest contributor to activity in this market accounting for 91.08% to total volume. The market has declined for 3 months of this period, January (3.43%), April (6.48%) and May (0.56%). The best performing month was February, which was up 2.36%, coincident with the listing of Sagicor.

Despite the listing of Sagicor, the market is still very poorly traded at 28.55%. This is evident since 3 of the 6

unchanged companies have not traded a single share for the year. This market can be best described as comatose but actually has the best conditions for growth: very stable and positive economic conditions and good corporate earnings. This is a contradiction that investors are still trying to reconcile.

Jamaica Stock Exchange (JSE)

Volume on the JSE increased by 30.8% to 1,012,268,608 whilst the index was up 11.2% to 50,478.94, with 15 companies advancing, 22 declining and 2 remaining unchanged. Jamaica Money Markey Brokers Limited (JMMB) registered the best performance (+102.41%), while the worst performing company in this market was the Ciboney Group, which declined 52.94%. The overall market traded at an activity ratio of 95.16%, where the most actively traded companies were JMMB and Cable & Wireless (C&W), both of which traded at 100%. JMMB contributed 40.52% of the market volume while C&W contributed 15.57%. For the review period the JSE declined in two months only, 1.58% in January and 1.28 in June. The best month was May, which was up 6.61%.

Top Ten Best Performing Companies

BARBADOS		JAMAICA		TRINIDAD & TOBAGO	
Grace Kennedy & Co Ltd	52.38%	JMMB Limited	102.41%	JMMB Limited	56.25%
RBTT Financial Holdings	37.25%	Pegasus Hotel	57.50%	Furness Trinidad Limited	45.10%
Sagicor Financial Corporation	25.71%	Hardware & Lumber	39.84%	Caribbean Communications Network	27.27%
Neal & Massy Holdings Limited	20.00%	Montego Freeport	30.77%	Williams L.J Limited A	21.95%
West Indies Rum Distillery	19.05%	RBTT Financial Holdings Limited	30.03%	Neal & Massy Holdings Limited.	19.44%
West India Biscuit Co	13.64%	National Commercial Bank Jamaica	16.42%	RBTT Financial Holdings	17.91%
Insurance Corporation of Barbados	12.00%	Guardian Holdings Limited	14.71%	West Indian Tobacco Co. Ltd	14.54%
Trinidad Cement Limited	9.09%	First Caribbean Intl Bank Jamaica	14.67%	Readymix West Indies Limited	13.56%
Barbados Shipping & Trading	3.03%	Jamaica Producers Group	14.29%	Agostini's Limited	13.08%
Light & Power Holdings	1.14%	First Caribbean International Bank	12.88%	Scotia Bank T&T Ltd.	10.33%

Treasury Bill Operations Barbados
(January-March)

Issue Date	3-month bills (%) p. a	6-month bills (%) p. a	Results: Oversubscribed
2003-01-04	1.36	—□	63.61
2003-01-15	1.21	-----	134.02
2003-01-26	1.09	---	120.00
2003-02-26	0.91	0.93	147.80
2003-03-07	0.80	-----	175.00
2003-03-21	2.50	-----	83.39
2003-04-05	2.49	—□□	80.53
2003-04-16	2.39	—□	136.00
2003-04-30	2.30	—□	103.06
2003-05-22	2.16	2.19	92.16
2003-06-06	2.03	—□□	133.00
2003-06-20	1.91	—□□	108.80

Treasury Bill Operations Jamaica
(January-March)
(6-Month Issues)

Date of Issue□	Issue Size□ (Ja\$M)□	Interest Rate□	Under(-)/Over(+)□
2003-01-29□	500□	16.90%□	+389.49□
2003-03-26□	300□	26.68%□	+558.48□
2003-04-28□	300□	26.31%□	+482.22□
2003-05-29□	300□	26.68%□	+888.71□
2003-06-24□	300□	24.94%□	+716.46□

The advance-decline ratio, which is the number of companies declining relative to those advancing, indicates that what might appear to be a good performance is actually hiding some fundamental weaknesses in this market. The ratio is a good indicator of the overall market performance and currently indicates a weak market. Investor confidence will depend on a number of national issues including, interest rates, the national debt, the deficit, the currency and government's ability to manage and control these items. However, this market can best be described as volatile yet resilient.

Trinidad and Tobago Stock Exchange (TTSE)

The TTSE index increased 2.71% for the half year with volume 180,257,185 which saw 19 companies advancing, 9 declining and 2 remaining unchanged. The best performing company was JMMB limited, up 56.25%, whilst the worst performing company was L.J. Williams, down 34.87%. The market was very actively traded at 81.92%, with trading on the TTSE was totally dominated by JMMB, which contributed 77.57% of total market volume. If JMMB is taken out of the picture, volume on this market is actually down significantly from the same period last year. The market has declined for only 2 months of this period, January, down 0.35% and April down 1.51%. The best performing month was February up 3.45%, coincident with the listing of JMMB.

This market is best described as lethargic, with no major happenings or announcements to drive the market. In a relatively stable and quiet economic environment, investors will spend the remainder of this year focusing on those companies to release earnings.

Interest rates

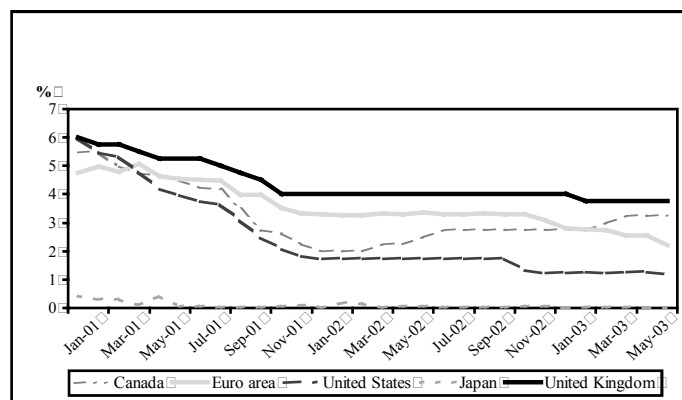
United States of America

During the first half of 2003, the federal funds rate was lowered by, twenty-five (25) basis points. The key interest rate, now at 1.0%, highlights the accommodative stance on monetary policy.

Financial markets had discounted the rate cut, which provided an indication that there was less worry about the prospect of inflation, compared to betting that future economic weakness needed to be addressed by lower interest rates. Long-term interest rates are likely to remain low. This should serve to maintain mortgage activity and reduce corporate borrowing costs.

Expansive monetary policy is expected to provide ongoing support to economic activity over the short to medium term.

Interest Rates
(In Selected Industrial Countries)



NOTE: The data are as of month-end and extend through June 2003. The interest rates shown are the call money rate for Japan, the overnight rate for Canada, the refinancing rate for the euro area, the repurchase rate for the United Kingdom and the fed funds rate for the United States.

Canada

In Canada, the monetary authority, raised interest rates twice since the beginning of the year, by 25bp each. For the past two years the Canadian economy performed better than any other in the G7, but over the last year the economy had begun to be affected by inflation pressures. Towards the end of the first half of 2003, with inflationary pressures waning, the Bank of Canada held its key interest rate - the overnight rate - at 3.25%.

Indicators point to a healthy domestic economy over the longer-term due to strong domestic consumer demand and an expected rebound in the U.S. economy during 2004.

United Kingdom

During the first half of the year, the Bank of England held the key repo rate constant, except for the 25bp reduction in February, which had reduced the rate to 3.75% - the lowest figure in almost fifty years. Despite above-target inflation that prevailed at the time, the Monetary Policy Committee opted to tackle growing evidence of economic weakness.

The BOE maintained that spending would moderate gradually because unemployment and interest rates remain low, and should consequently help to stimulate aggregate demand.

The Euro zone

In an effort to revive the continent's stagnant economy, the European Central Bank slashed its key refinancing rate to its lowest level since World War II. The rate had been 2.5% since a quarter-point cut in March - one that many pegged as too timid - but with the bolder half-point cut in June, the ECB drew closer to the policy stance of the more aggressive U.S. Federal Reserve.

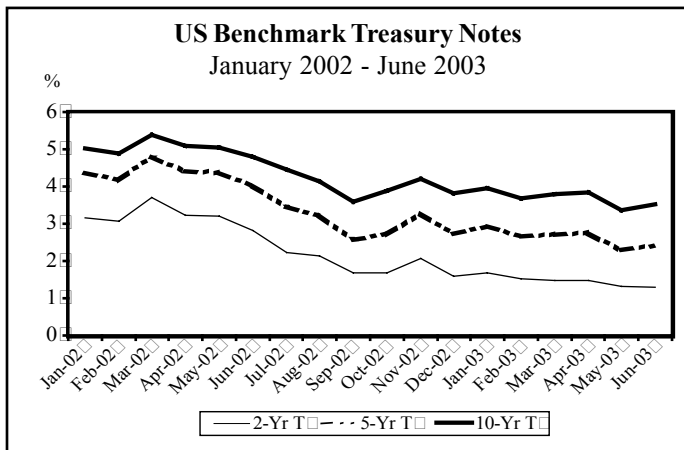
The narrowing of the interest rate gap between the U.S. and the 12-nation group was interpreted as lending support to the U.S. dollar and Euro-zone exports. With inflation at 1.90%, the ECB was able to implement measures aimed at boosting output, especially in Europe's largest economy - Germany.

Bond Market - US

During the first six months of 2003, the US bond market was characterised by a continued decline in yields, which generated substantial gains on Treasuries. The expansive monetary policy was deemed necessary in order to lend further support to the weak US economy and avert the possibility of deflation.

Overall for the six-month period, bond yields fell to their lowest levels in over four decades, with the five-year benchmark Treasury recording the sharpest decline of fifty-six (56) basis points.

During the first quarter of 2003 in particular, in response to the US-led war against Iraq, many investors sought the safety of Government debt, which placed upward pressure on bond prices.



During March, the rally in the bond market continued to generate gains. By mid-March, bond yields fell to their lowest level for the first quarter, with the two-year yield declining to 1.34%, while the rates for the five and ten year Treasuries stood at 2.48% and 3.57%, respectively.

Following the recovery in equities at the beginning of the second quarter, the demand for Treasuries began to diminish. However, this was soon succeeded by further gains in the bond market later in the second quarter.

By the end of June, the two-year Note was recorded at 1.30%, while the five and ten-year Notes traded at yields of 2.41% and 3.51%, respectively.

Emerging Markets

The major influence on emerging markets during the first quarter of 2003 was the US-led war on Iraq. However, as the war progressed and expectations grew that it would prove relatively short-lived, funds began flowing once more into certain key markets such as Brazil.

Notwithstanding, some highly US-dependent markets like Mexico remained relatively weak, as investors began shifting their focus to the outlook for the U.S. economy in the aftermath of the war. Demand for equities in the first quarter was especially soft, as concerns about the impact of the deadly Severe Acute Respiratory Syndrome (SARS) affected Asian stocks in particular. However, in the second quarter, with the war being over and SARS abating, most of these concerns had dissipated, leading to a healthy rebound in equity and currency markets. Bond markets remained fragile, as rising stock markets seemed to offer better returns, leading to a global bond sell-off.

Performance of Emerging Markets

	Index	Dec. 2002	Mar. 2003	Jun. 2003	% Change	
					Mar. -Jun.	Jan. -Jun.
Latin America						
Argentina	Merval Index	447.46	523.25	722.62	38.1	51.35
Brazil	Bovespa	11,268.47	11,273.63	13,007.64	15.38	15.43
Chile	IGPA Gen	1,000.00	1,009.13	1,228.93	21.78	22.8
Mexico	IPC	6,127.09	5,914.03	7,059.15	10.3	15.21
Venezuela	IBC	8,015.17	8,506.59	13,666.40	60	70.51
Average Performance		5,377.64	5,445.33	7,136.95	29.11	32.72
Asia						
China	Shanghai	1,357.65	1,510.58	1,436.02	(1.03)	0.4
Hong Kong	Hang Seng	9,321.29	8,634.45	9,577.12	10.02	2.74
Indonesia	Jakarta Comp.	429.95	398	505.5	27.01	18
Malaysia	KLSE Comp.	646.32	635.72	691.95	8.85	7
Philippines	Manilla Comp	1,018.41	1,039.67	1,222.80	17.01	20.07
Singapore	Strait Imes	1,341.03	1,267.82	1,447.89	14.2	7.07
South Korea	KoreaCmpEx	627.55	535.7	699.93	25	0.75
Taiwan	Weighted Price	4,452.45	364.55	451.82	2.08	20.55
Thailand	SET	356.48	4,321.22	4,372.15	12.75	0.43
Average Performance		2,171.79	2,078.63	2,326.13	11.97	7.11





Trade Developments and Macro Economic Implications*

Update on the Caribbean Single Market and Economy (CSME)

The importance of the CSME

One rationale for a single economic space for the Caribbean is that deeper integration is necessary in order to respond to the challenges and opportunities presented by globalisation and trade liberalisation if the Caribbean is to maintain its place in the global landscape. The main challenge is that of increased external competition for production, trade and investment, as reflected in the proliferation of international trade agreements and the impetus for elimination of traditional trade preferences. CARICOM banana farmers' loss of market share in Europe as a result of the WTO ruling against preferential treatment of Caribbean bananas is a prime example of this.

As negotiations unfold, the rules governing trading arrangements are requiring parties to create new institutions and implement and enforce trade-related measures, all of which may prove costly for individual small states, given their resource constraints. Examples of this include the cost of applying standards, sanitary and phyto-sanitary measures, anti-dumping measures and measures to protect intellectual property rights. This problem of resource scarcity is not confined to financial resources but extends to human resources as well – individual CARICOM member states have in the past encountered great difficulty in sourcing the expertise necessary to participate meaningfully in negotiations.

There are also time constraints, as CARICOM member states are currently engaged in negotiations for three

different trade arrangements: the FTAA, the WTO and the ACP-EU Cotonou Agreement. The deadlines for completion of these agreements are all between 2005 and 2007 and, in turn, this external agenda is largely determining the region's timetable for implementation of the CSME.

Implementation of the CSME prior to the completion of these international trade agreements is critical, as the region attempts to make a place for itself in an international trading system where economic and political power are critical. By providing a harmonised framework for policy formulation, as well as a larger market, with greater opportunities for employment, investment, production and trade, the CSME holds out the promise of endowing Caribbean countries with the economic and political strength necessary to meet these challenges.

At the same time, the CSME framework will enable member countries to take advantage of a number of opportunities. All of the factors previously mentioned – policy harmonisation, increased market size, rationalisation of costs, etc. – should help to lower costs and improve regional consumer welfare. The resulting increase in efficiency and competitiveness should also allow the region to better exploit its competitive advantage in the area of services. In addition, there are a number of benefits to be derived from intra-regional trade, which are being enhanced as the integration process advances. For example, an increasing percentage of CARICOM countries' trade is being sourced from other member countries, with tourism services leading the way in this regard. The example of tourist arrivals from other CARICOM countries which have helped some member countries maintain revenues in the face of declining arrivals from traditional extra-regional destinations is indicative of such benefits.

In short, the CSME aims to assist CARICOM countries in combating external threats, overcoming resource constraints and exploiting economic opportunities.

* The Trade Update was prepared by the Trade Unit in the Research Department of the Central Bank of Barbados

Implementation status of the CSME in Barbados

The CARICOM Secretariat has identified a number of steps that individual countries must take in order to fully implement the CSME: The following is an update on the status of implementation for Barbados

1. Treaty Revision - Signature, ratification and enactment into domestic legislation of the Treaty

The Revised Treaty of Chaguaramas has been signed and enacted into Barbadian law but has not yet been ratified. Under the principles of international law the depositing of an instrument of ratification is seen as an indication of readiness to implement a treaty fully. Therefore, the decision was taken by the Government of Barbados not to ratify the agreement until everything is in place for full implementation.

2. Removal of restrictions in respect of the right of establishment, the provision of services, the movement of capital and the movement of specific categories of Community nationals

This requirement essentially covers the provisions of Protocol II, which is considered the most important of the nine protocols, as it is felt that once it has been implemented, the others will more easily fall into place. The Prime Minister's Office, with the help of CARICOM Secretariat consultants and drawing on broad consultations with the relevant national institutions, identified a number of restrictions on the right of establishment and the provision of services that Barbados would need to remove in order to comply with this protocol. This Programme for Removal of Restrictions is ongoing, with the various ministries, departments and statutory corporations working closely together to develop an omnibus bill, which will contain all the amendments to the different laws and regulations necessary to the removal of these restrictions by the deadline of December

2003.

In addition, the Central Bank of Barbados has been ensuring the movement of capital through the ongoing liberalisation of exchange controls. The most recent move in this regard, which takes effect from September 15, 2003, provides for the transfer of funds from Barbados to CARICOM countries in respect of all current transactions, with the exception of certain specified transactions to which special limits apply.

With respect to the movement of Community nationals, the free movement of media workers, artistes, musicians, sports persons and university graduates was due to become a reality in Barbados, Jamaica and Trinidad at the end of August. However, the Immigration Department is still in the process of revising the Immigration Act. This process is scheduled to be completed by end December 2003, but in the interim the movement of these categories of persons is being facilitated through an administrative arrangement. Furthermore, the free movement of Community nationals and their families to provide services and/or to establish businesses, as provided for under Protocol II, is to be dealt with as part of the Programme for the Removal of Restrictions. In order to facilitate such movement, the Prime Minister's Office has held discussions with the Immigration Department about the recommendations of the Council for Human and Social Development (COHSOD) that member states should introduce machine-readable ID cards and a common E/D form by 2004.

3. Enforcement and Regulation - Enactment of legislation and establishment of institutions dealing with a range of issues such as subsidies and countervailing measures, intellectual property rights, competition rules, etc.

Barbados has signed, ratified and enacted into domestic law the agreement to establish the Caribbean Court of Justice (CCJ) and has signed on to the agreement creating the

CARICOM Regional Organisation for Standards and Quality (CROSQ), having already established the Barbados National Standards Institute (BNSI) many years ago. Furthermore, by setting up the Fair Trading Commission (FTC), Barbados has fulfilled the requirement to establish a national competition authority. Cabinet has also approved the establishment of a national accreditation agency by August/ September 2003 and the Attorney General's Chambers has prepared draft legislation in that regard. The establishment of such a body is necessary to facilitate the movement of Community nationals. Nevertheless, a number of changes remain to be made, such as the removal of Customs' environmental levy and the revision of legislation in respect of dumping, subsidies and countervailing measures. Barbados has thus far implemented two modules out of twenty required for the harmonisation of customs legislation.

4. National Administration - Establishment of administrative facilities and measures for the discharge of obligations under the treaty

Most of the necessary institutional and administrative changes have been made, including the identification of the Prime Minister's Office as the Ministry responsible for CARICOM affairs, complete with a CSME unit. Another such development has been the establishment of a national consultative framework involving both the private and public sectors.

5. Elaboration and implementation of a public information programme

Although Barbados' public education programme with respect to the CSME has already commenced with a series of consultations, as well as programmes put on by the Government Information Service, the Prime Minister's Office is proposing to develop a more far-reaching and comprehensive programme in the near future.

In summary, Barbados can feel confident that it has put in place many of the measures necessary from its end to meet its deadlines for full implementation. Nevertheless, important measures remain to be implemented, especially in the areas of removal of restrictions, further exchange control liberalisation, enactment of new legislation and public outreach. The latter is perhaps the most important aspect of this process, in the race to push through legislative and administrative changes. Only with public education as to the opportunities and challenges to be faced, as well as widespread public consultation on the various issues that emerge in the process, can we hope to build a single market and economy that is structurally sound and sustainable over the long term.

Financial Services and the CSME: Opportunities, Threats and Challenges

“Summary of an address to the National Consultation by Governor of the Central Bank of Barbados”

Financial Services and the CSME

The financial services sector has been the subject of intense focus in recent years, especially in the context of the Caribbean Single Market and Economy (CSME). The sector is of strategic importance to Barbados' predominantly service-oriented economy, as it offers many opportunities for economic development.

A necessary step in the process of evaluating the opportunities and challenges is to first examine the rights and obligations provided for in Chapter Three of the Revised Treaty of Chaguaramas – the legal text governing the establishment and functioning of the CSME. It calls for the liberalisation of financial services through the removal of restrictions relating to: 1. rights of establishment, 2. the provision of banking and other financial services, 3. the movement of capital and 4. the movement of labour. In addition,

provision is made in the treaty for the integration of financial markets through the harmonisation of legislative, supervisory and institutional structures in the region.

For Barbados, the obligation to remove restrictions on rights of establishment in the banking industry will not represent a significant change in the regulatory structure, as there are no non-prudential restrictions on access to the domestic banking market. In the case of offshore banking, the old Offshore Banking Act, which permitted different capital requirement ratios for resident and non-resident entities, was replaced by the International Financial Services Act, which eliminated discrimination. What remains is the requirement for a resident director. This ensures access by the regulator to the bank director and is seen as a prudential requirement and is not considered discriminatory. Therefore although, *de facto*, the domestic market was always open before, it is now more explicitly so.

With respect to the removal of restrictions on the provision of financial services, certain discriminatory laws that were identified in the insurance and securities sectors are being addressed. In addition, amendments are being made to the Immigration Act to allow for the entry of CARICOM nationals to the extent required to guarantee the right of free movement of labour in the sector.

Furthermore, Barbados has been gradually liberalising its exchange controls and is committed to fully liberalising them vis-à-vis CARICOM. Indeed, recent liberalisation measures will bring Barbados very close to complete current account liberalisation with respect to CARICOM. Also, the speed of movement of capital is being further facilitated as a result of the modernisation of the payments system through the introduction of the Real-time Gross Settlements (RTGS) system and the Automated Clearing House (ACH) and the issuing of e-banking guidelines.

In terms of integration of legislative, supervisory and institutional structures, harmonisation of regional legislative and supervisory frameworks is taking place through the efforts of the Working Group on Financial Services Sector Harmonisation, which deals with harmonisation in the non-bank financial sector, and through the Committee of Central Bank Governors, which deals with harmonisation in the banking sector. The integration of institutions is also moving forward: the regional private sector has already launched two projects geared towards establishing a regional stock exchange and a regional credit rating agency, respectively. In the context of the CSME, the Caribbean Regional Negotiating Machinery is another important institution. It was established to coordinate the region's negotiating strategy in all sectors, including financial services.

Opportunities

The liberalisation and integration of financial markets within the CSME offers tremendous opportunities for the development of the financial sector and for the economy as a whole.

For example, businesses, consumers and investors stand to benefit directly from the removal of restrictions on rights of establishment. Businesses, which have already gained a competitive advantage regionally, will find it easier to export services to other CARICOM states. More so, consolidation in the sector will become more feasible, thereby enabling regional financial institutions to attain the critical mass necessary to withstand increased external competition. In so doing, they should improve risk management and allocative efficiency, which would allow them to cut costs on existing service offerings. This should provide added incentive to expand into new, more specialised service areas; opportunities which would previously have been limited by diseconomies of scale. Consumers, in turn, should benefit from the resulting price reductions and increased choice;

furthermore, cross-border transactions should make it possible for them to enjoy these benefits even where there is no physical presence.

The removal of restrictions on the provision of financial services raises the prospects of indirect gains to businesses, consumers and investors, as well as regulators. The expected increase in the volume of cross-border transactions should lead to a greater emphasis on risk-based rather than rules-based supervision, which serves the interests of all stakeholders by ensuring financial sector stability and integrity.

In addition, with a regime of freer movement of capital in financial services we can expect the presence of excess liquidity within the financial systems of individual countries to be optimised. For example, with more opportunities for Barbadians to own shares in companies listed on regional stock exchanges, an outlet would be provided through which idle cash could be channelled into new investments.

Opportunities will arise in the area of employment, as the expected free movement of labour within CARICOM would allow Barbados' highly skilled financial services professionals to go where their skills are required, thus reducing the pressure on the domestic labour market.

The harmonisation of financial regulation and supervision in the region is expected to improve quality and cost efficiency through standardisation, as well as through sharing of resources and technical expertise. This should facilitate consistency across jurisdictions and discourage regulatory arbitrage. Greater collaboration at the regional level should also allow regional regulators to better respond to external challenges from international standards-setting bodies, such as the IMF, OECD, FATF and the FSF. In addition, by creating a predictable legislative environment for investors, such harmonisation should encourage intra-regional investment and FDI into the region.

Similarly, the creation of regional institutions such as the proposed stock exchange and credit rating agency would allow investors to evaluate risk under more transparent conditions, while providing opportunities for portfolio diversification and risk sharing. All of these factors should contribute significantly to the creation of an attractive investment climate and to overall economic growth in the region. In addition borrowers are likely to gain easier access to financing at more competitive rates, thus enhancing their international competitiveness. In the area of negotiations on financial services within the WTO and the FTAA, the pooling of negotiating expertise through the RNM will help to facilitate CARICOM's objective of negotiating in hemispheric and multilateral negotiations with a singular commitment and will help to achieve critical mass in terms of bargaining power.

Threats and Challenges

Despite the obvious opportunities, there are a number of factors that could constitute challenges to the financial sector.

In this regard, issues such as the removal of restrictions on rights of establishment could prove to be challenging. For example, the acceleration in the current trend of industry consolidation may reduce competition in financial services. This is essentially a challenge for small companies, which will need to be very strategic in their approach in an operating environment where critical mass is vital. It also represents a challenge for regulators, as the situation requires them to set guidelines on when market share is likely to lead to anti-competitive behaviour and to take a pre-considered response in the event of their infringement. These developments will call for greater cooperation and information sharing between regulators in different CARICOM jurisdictions and increased emphasis will have to be placed on consolidated supervision.

In removing the restrictions on the provision of financial services, the main challenge lies in overcoming the resource constraints that limit the pace of implementation. For example, the heavy workload placed on legal drafters, limits regulators' ability to make the necessary large-scale revisions to the legislation quickly and effectively.

The expanded universe of instruments available in the domestic market as a result of liberalisation will require improved risk management on the part of the entities involved and greater oversight by regulators. Furthermore, the opening up of possibilities for cross-border incorporation of off-shore financial institutions within CARICOM may require the harmonisation of tax systems across the region in the future.

With free movement of labour, especially in light of expectations of further consolidation in the sector, the movement of financial services providers could become more evident. This will have implications for the skill sets of professionals and will require that they ensure that their skills are comparable if not superior to those available elsewhere.

In order to create a harmonised supervisory framework certain modifications to regulations will be required, which may prove a challenge for regulators, who for the most part will have to be the initiators of such changes. However, the fact that national entities have already been taking steps to comply with international regulations makes this harmonising process slightly less of a challenge.

Of all the obligations imposed by the CSME, the liberalisation of capital movements poses the greatest challenges for Barbados. The first relates to the complete liberalisation of the current account, within CARICOM, given that some countries within the grouping have no exchange controls with respect to the rest of the world. A second challenge has to do with how fast we should proceed with capital account liberalisation, and what creative ways can be used to cushion the impact. Then there is also the chal-

lenge posed by existing interest rate differentials, with implications for potential interest rate arbitrage. Greater convergence of interest rates within CARICOM is desirable and would facilitate the process. Lastly, the free flow of capital given monetary policy objectives driven by each country's individual needs, raises the possibility that regional flows could impact central bank monetary policy in unintended ways.

Conclusion

The changing face of the financial sector will bring a number of challenges for all stakeholders. Businesses will need to do what it takes to be competitive and consumers and investors will need to be vigilant and less anti-competitive firm behaviour should become evident. At the same time, regulators will be required to develop new approaches in order to safeguard and balance all these interests. Any period of transition will involve some degree of dislocation, but if our responses are appropriate these challenges can be converted into opportunities.

Report on the WTO Ministerial Conference in Cancún

The Fifth Ministerial Conference of the World Trade Organisation (WTO) was held in Cancún, Mexico from September 10th to 14th, 2003. This conference marked the mid-point of the current negotiating round, which was launched at the previous Ministerial in Doha, Qatar.

The Lead-up to Cancún

The main objective in Cancún was to note and steer progress on the work programme decided at Doha, where the Doha Development Agenda (DDA) had set out a number of negotiating objectives and deadlines for the Round. The Agenda was considered to be development-friendly, with a number of provisions that aimed to address the concerns of developing countries, taking into consideration their spe-

cial conditions. The issues set for negotiation in the DDA were agriculture, services, industrial tariffs, implementation, trade and environment and some areas of intellectual property. In addition, Ministers were expected to discuss the possibility of launching negotiations on the “Singapore Issues”: investment, trade and environment, competition policy, trade facilitation and transparency in government procurement. The Dispute Settlement Understanding was also slated for reform, although this did not form part of the official agenda.

Since almost all the negotiating deadlines were missed in the run-up to Cancún, the substantive decisions on major issues were left to be taken at this conference. In addition to the above issues these included decisions on trade in agricultural and industrial goods, implementation and special and differential treatment (S&D), trade in services and other miscellaneous issues. Although the Cancún Ministerial had initially been seen as purely a stocktaking exercise, its outcome came to be seen as an indicator of the likely outcome of the entire round and prospects for world trade in general. With the world economy still in a fragile state of recovery, this uncertainty surrounding the outlook for trade began to assume even greater significance.

Negotiating Positions

Developed countries, emphasised liberalisation in the areas of industrial goods, the “Singapore issues”, and trade and environment. They were especially anxious to achieve a consensus for the launching of negotiations on the four “Singapore Issues”. The EC, the main proponents of these issues, stated up front their desire to launch negotiations among all members, to be completed by 2005. With respect to investment, they presented the case that the existing international regime of individual bilateral and regional investment agreements had led to confusion and therefore called for a WTO agreement that would create a simple, transparent, non-discriminatory environment for international investment. The arguments advanced for WTO agreements on

trade facilitation, government procurement and competition policy were similar, but they highlighted the need to fight against trade-restricting red tape, corruption in government procurement and powerful international cartels, respectively.

Also, developed countries had previously made proposals for sweeping cuts in tariffs on industrial goods and generally improved access to developing countries’ markets for their exports. They therefore went to Cancún with the intention of getting favourable decisions on these proposals.

Developing countries, focused more so on the issues of agriculture, implementation and S&D, as well as services. A particularly unified stance was adopted on agricultural issues, with developing countries insisting that the extent to which developed countries committed themselves to addressing imbalances in agricultural trade would make or break the talks. In line with this position, an alliance of twenty-one developing countries (the so-called G21) emerged to voice their concerns about developed countries’ agricultural subsidies. They argued that the \$300 billion spent annually on rich-country agricultural subsidies were so detrimental to poor farmers in developing countries that their removal should take priority in a so-called “Development Round”. Also, a new Strategic Products (SPs) and Special Safeguard Mechanism (SSM) Alliance (SPSSM), comprising 23 developing countries, advanced the need for special measures for small and resource-poor countries, such as longer time frames and less radical liberalisation to ensure food security and protect the livelihoods of rural communities.

African cotton-producing countries made a strong case for the removal of US subsidies on cotton, pointing out that as the most efficient cotton producers in the world they were not asking for special treatment, just the opportunity to engage in free and fair trade. Furthermore, they pointed out that while cotton farmers represented a considerable proportion of the working population in their countries, they were demographically insignificant in the US and overall US in-

terests would be better served by giving consumers access to cheaper African cotton. They therefore proposed that a decision on cotton be part of an “early harvest” in negotiations in Cancún.

Developing countries were also concerned by the failure to address their concerns about implementation and special and differential treatment. They felt that moves to expand the scope of negotiations in the Doha Round to include the “Singapore issues” were unreasonable at a time when they were still encountering difficulty in implementing the results of the previous Round. They therefore renewed their call for special and differential treatment in their implementation obligations, in line with the stated objective of the Agenda to promote the participation of developing countries in world trade.

In addition, although trade in services was the one area in which negotiations had progressed according to the Agenda prior to Cancún, many developing countries felt that developed countries had been too slow to liberalise in Mode 4, the movement of labour, which was the area of most interest for developing countries. Furthermore, they felt that enough attention had not been paid to the need for assessments to evaluate the economic impact of services liberalisation.

Results of the Talks

Discussions on the various issues focused on agriculture and implementation and special and differential treatment and the “Singapore issues”.

Developed and developing countries’ opposing positions were too entrenched for them to find any common ground. A short ministerial statement was issued outlining the reasons for the breakdown of talks and mandating more work to be done in key areas by Members on their return to Geneva.

Cancún Post-mortem

While G21 countries expressed disappointment with the setback, they were encouraged by the evidence of developing countries’ ability to band together in pursuit of common objectives. The G21 grouping nevertheless remained positive about the prospects for completing the round. However, the poorest countries, many of whom were represented in the SPSSM grouping, were not quite as optimistic in their outlook, they were disappointed by the failure of developed countries to make concessions on key issues such as cotton.

Completion of the Doha round by the target date of end-2005 appears dubious while the prospect for more orderly trade relations is less optimistic.

All this changes things significantly for CARICOM negotiators, as agreements at Cancún were expected to form the basis for negotiations in other arenas such as the ACP-EU agreement and the Free Trade Area of the Americas (FTAA). However, one positive outcome of the Cancún talks was developing countries’ realisation that it is possible for them to influence trade agreements at the multilateral level as long as they work together.



“Pension Reform in the English-Speaking Caribbean”
by Dr. Marion Williams, Governor, Central Bank of Barbados *

Mr. Chairman – Mr. Desmond Brunton, President Professor Compton Bourne, Mr. Euric Bobb, Mr. Pietro Masci of IDB, distinguished ladies and gentlemen. I am very pleased to have been invited to this symposium to share my views on pension schemes and their reform, a topic which has engaged the attention of policy makers consistently over the past 10 years or so.

I believe this issue needs to be discussed more in the region, since it is extremely critical to our continued economic and social development. I therefore, applaud the Caribbean Development Bank and the IDB for having the foresight to host this symposium.

In my address today I will touch on the case for pension reform and some of the issues which are, or will be, the concerns of reformers.

Notwithstanding the fact that the case for pension reform throughout the world has already been strongly made in many quarters, the arguments are worth repeating since pension reform is something which has to be sold, particularly where benefits are being modified or reduced or expectations changed. Given that funding costs of pension schemes are likely to continue to rise, understanding both current and future costs is necessary to allow enough time to plan for expected increases and to make the necessary modifications to existing plans. In our constantly changing environments, plan actuaries will need more than ever before, to continually review and modify assumptions to ensure that they are still good predictors of future expectations.

Since the early to mid 1990s actuaries and international institutions were speaking of “Averting the Old Age Crisis”. The implication for pension funds of aging populations which were expected to be healthier and to live longer was seen to be creating a crisis. Studies, which started first in the OECD countries, showed declining rates of labour force participation among able-bodied men of working age. There were also trends of early retirement and exit from pension schemes, decreasing fertility rates, and day-to-day demands

that had created lifestyles which led to smaller family sizes. These made formal pay-as-you-go (PAYG) pension schemes no longer well-positioned to provide sustainable streams of payments to citizens on reaching their retirement. It was around this time that international organisations, governments and individual analysts, who before this, had been making just incremental changes to pension schemes, began to dramatically reassess the adequacy of existing schemes, taking into account new trends in life cycles, changing demographics and working habit changes in the population. They became generally more proactive about finding remedial solutions.

In the case of developing countries, research shows that problems are more pronounced. There are likely to be faster changes in the demographic structure of populations of developing countries, resulting in a larger proportion of retirees at much lower levels of per capita income than in developed countries. This relatively faster rate of increase in the share of aging citizens implies that greater outlays of financial and other resources will have to be made to adequately satisfy their health and other welfare concerns. In Barbados, and in many CARICOM countries this was further influenced by declining fertility rates, and improved medical care which had raised longevity rates. If, as is the case in most CARICOM countries, the assumption here is that governments are expected to continue to be the primary providers of social security for its retired citizens, then this form of expenditure would likely crowd out other competing uses for scarce public funds unless remedial measures are taken.

A recent study shows that in Europe the population over 60 is forecasted to increase from 20% to 30% by 2030. Meanwhile the number of workers per pensioner is calculated to have fallen from 3.5 workers per pensioner in the 1950s to around 2.5 workers in the 1990s, and in the years ahead, is forecasted to decline further to around 2.0 workers per pensioner.

In the transition economies of Europe, this rate had already fallen to about 1.5 workers in the 1990s. While economic difficulties are the main cause in the transition economies, where tremendous fiscal problems are being encountered

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as they cope with the transition to a market economy, a large informal sector is one of the chief reasons for many of the pension problems in Latin American countries; while in Asia the ratio of the elderly to the working population is exceptionally high and is projected to triple in the next forty years. In Sub-Saharan African countries, where pensions systems are in their infancy, with coverage of less than 5 percent of the population and expenditure of only 1.5% of GDP, the situation appears not to be too critical with respect to funding of pension schemes though care of the aged remains a concern. In the Barbados case, prior to the reform recently instituted, it was projected that the current figure of 3.4 contributors to every pensioner would have fallen to 1.3 by 2060 in the absence of reform. Twenty Sixty may sound like a long way off, but since such reforms must be gradual if they are not to seriously affect pensioners due to changes in expected benefits, then planning has to have a long time horizon.

Much of the international dialogue on this matter tended to focus on 3 pillars or features. At the very basic level, an unfunded mandatory feature, a funded mandatory feature, and a voluntary private feature. The crux of the debate has concentrated on whether the features of reforms should be mandatory or voluntary, with defined benefit or defined contribution systems; or publicly or privately funded or fully funded options. The cross-country evidence reveals that a variety of systems were adopted.

In the early 1990s, most countries had mandatory public or quasi-public pensions systems. Some African and Asian countries had government-run provident accounts, while Chile was the only country with a privately-managed, funded, defined contribution system. It is noteworthy that at that time the Chilean model was regarded as a benchmark for change from PAYG defined-benefit systems to more advanced-funded systems with individual accounts. However, privately managed defined-contribution systems were criticised by some observers on the grounds that they did not adequately cover low-income workers, and that their adoption in other countries, particularly those with a large pension debt was problematic. It is argued that high overhead costs associated with such a pension system, could likely result in an erosion of positive returns on invested assets, and that there would need to be a tremendous savings effort to pay off debt in order to make an efficient switch. The

Chilean model of publicly-managed, funded defined-contribution subsequently lost favour.

While most countries have not taken this extreme course, in recent years there was however a distinct trend towards the tightening of the relationship between contributions and benefits. In this regard, the most fundamental changes were the implementation of notional defined contribution schemes mostly in developed countries. The main preoccupation was how to address the high costs of running individual financial accounts systems.

Research on these issues point to determined efforts to create financially sustainable mandatory public pension systems in Europe, Latin America and in the transition economies, and suggest that the combination of a PAYG system coupled with a scheme of funded individual accounts was the most popular approach. Though less research has been done on the Caribbean, the options are not much different. The Caribbean case is however complicated by the preoccupation with immediate fiscal difficulties, which in some cases, require concentrated attention.

Some European countries have raised the funding component in their mandated or quasi-mandated pension systems. In particular, the UK strengthened the option which allowed persons to contract out of the state earnings-related pension scheme to join private schemes. Others introduced individual financial accounts, in addition to a new PAYG notional account system. Following this reform, the quasi-mandatory public schemes were largely converted to defined contribution financial account schemes.

Several countries also raised the full-benefit pension age. Germany will gradually increase the full benefit age to 65, with the possibility that this age could be revised upwards. The reforms in Japan also propose a gradual increase the pension age for the earning-related part of its Employees Pension Insurance. Here in the Caribbean, Barbados has already announced an increase in the full-benefit pensionable age.

One of the issues in introducing schemes is how one treats existing workers. In some schemes new entrants were mandated to the financial account systems, but current

workers were given a choice of either remaining in the PAYG system or entering the financial account system.

Minimum guarantees have remained or have been created, in all of the countries that have implemented reforms involving notional defined contribution systems. Other countries have reformed their public mandatory schemes without including a funded compulsory element but have reduced avenues for early exit from schemes and have tightened benefit formulas in earnings-related PAYG systems.

In Latin America where most countries resorted to blends of a PAYG mandatory and a feature consisting of a privately funded component, research has shown that the reforms undertaken during the 1990s have helped to reduce pension debt and have created more fiscally sustainable systems. However, issues such as coverage and sizeable overhead costs remain controversial topics.

In Asia, similar approaches have been taken to that of many Latin America countries. Some have adopted blends by adding or strengthening their defined benefit schemes, while keeping defined contribution systems. Some countries are however likely to suffer the same benefit problems as in Europe where low retirement ages can motivate early exit from schemes, unless changes are made to their schemes.

Research studies show that the African and Middle Eastern countries are still largely rural with old age informal support systems, and their partially funded defined benefit PAYG systems apparently have sufficient reserves to cover average retirement benefits.

Within the English-speaking CARICOM, national insurance pension schemes are the most prevalent form of retirement income for workers, though in Trinidad and Tobago and Jamaica, a host of alternative savings vehicles also exist. However, just like our international counterparts, pension schemes in the Caricom region, are facing the same threats to sustainability.

Barbados has already embarked on pension reform. After an extensive consultative process involving inputs from a wide-cross section of Barbadians, reforms of the national insurance scheme were undertaken. These include:

1. An increase in the contribution rate of 1 percent of insurable earnings each year for four years to be shared equally among employers and employees until 2030;
2. An increase in the retirement age from 65 to 67 from 2006, with the retirement age rising by 6 months for every four years until 2018;
3. Flexibility in the retirement age between 60 and 70;
4. The permission for early retirement from 64, with the intention of gradually reducing that age each year.

Though Jamaica, Trinidad and Tobago, and the OECS are at earlier stages in the process of evaluation and reform, there is a growing consciousness of the need for pension reform in almost the entire Caribbean. With escalating costs, especially for defined benefit schemes, and increased scrutiny by employees due to market losses and diversification issues, it has become even more critical for pension scheme sponsors to focus on the design of their retirement programmes. After all, maximising the value of the state and/or corporate investment in these plans is one of the key obligations as a plan sponsor.

There are a few issues which, though relevant internationally, must be given particular consideration in the Caribbean context

At the macroeconomic level, plan sponsors will be concerned about the impact on employment of decisions to extend the working life of employees. There is the possibility of an adverse impact on new employment. This is an important consideration in high unemployment areas of the Caribbean.

For the most part most countries have opted to have public plans while adding a voluntary feature or encouraging individuals to supplement their plans with private annuities. However, in countries like Barbados and some other Caribbean countries where per capita incomes are relatively high, and such individual plans are affordable, this might be a development whose encouragement plan sponsors might see as a public relations responsibility. Tax benefits might be useful here as they could be seen as relieving government

of some responsibility. Some Caribbean countries, Barbados among them, have already taken this step, and it should be encouraged. The higher the per capita income the more this should be encouraged.

Furthermore, pension reforms should be structured well within acceptable financial, regulatory and legal best practices. The cases more recently of misuse of pension fund assets and the distress caused to aging pensioners are examples of the concerns here. The obvious challenge is to structure the reform programme within the already-established formal system, without too much dislocation, and without exerting too strong a burden on the informal systems that traditionally cared for the elderly, or without putting too much pressure on national budgets. In addition, older folks who do not have enough earning years to adjust to new rules without being disadvantaged, should be given consideration in the development of new structures. Delicate choices have to be made in weighing the health of the scheme against altering the expected benefits of persons at all income levels, whose best earning years are behind them. Adequate notice of impending changes are important. The question will be how much time is considered “adequate”.

For corporate employers the trend towards lengthening of retirement ages must require strategies to ensure that older employees are in tune with the new technologies and new thinking in their disciplines. It is important that employees who find difficulty in adjusting are not locked into remaining with the corporation when they really wish to go, but stay because it is not economically affordable to retire. This is a development which requires consideration in the interest of the increased productivity which we all desire.

Another factor which must also be addressed in the Caribbean, is the impact which HIV AIDS will have on assumptions about life expectancy of plan members. Actuarial assumptions will be influenced by the effectiveness of anti- AIDS programmes in the region, a measure which will be quite an informational challenge for actuaries.

Also, while much of the discussion has been about public pension plans, private pension plans also need to be restructured. This has already started in some cases, but

many of the considerations discussed in the context of public funds need to be applied to private pension funds as well. This gets us into issues of contractual obligations and raises the question as to whether new contracts should give flexibility to employers to change plan terms and whether, should such flexibility be possible, should it differ when plans are contributory as compared to when they are non-contributory.

Another important issue to be considered in the regional context is portability. If we are to move towards free movement of people in the CSME, not only must we have portability of pensions within Caribbean countries but between Caribbean countries as well.

There are other issues which you will probably be discussing which I shall only mention. One is – should pensions be indexed to wage increases or to inflation – or should they be indexed at all. Then there are the regulatory and supervisory issues – who regulates the pension funds and what is the scope of the regulation. Then there are governance issues – all of which have come to public notice in the last 18 months because of misuse and fraudulent use of pension funds principally in the U.S.

While I have not dealt with the use of Pension fund resources, since that is another very important topic altogether, let me say that as the single most significant source of public investible funds, pension funds should allow for the maximum use of resources for developmental purposes, consistent with the ensuring the security of the Fund resources. Diversification is important and hence some funds must be invested outside; however, when we invest outside, we are financing others. We must find ways to use these funds effectively on the regional front, without jeopardising their security. A careful review of asset allocation strategies, and a sound long-term investment strategy could provide the right balance of risk tolerance consistent with appropriate returns and investment time horizons which still give priority to regional investment. We need to find the right balance.

Judging by the programme you have before you over the next two days, it is clear that this Symposium will offer

insightful and meaningful dialogue not only on the types of reforms occurring internationally, but will also provide a forum for finding ways of adding impetus to the reform effort in the region. I look forward to your findings and recommendations. In this regard, the Caribbean Development Bank is playing an important role in the reform process by working closely with its borrowing members, offering technical assistance to national policy makers to

help identify the economic, social and demographic changes, with a view to implementing suitable policy responses. I congratulate the Bank for sourcing such an impressive array of speakers and most of all for choosing this important topic as the subject of your discourse.

I wish you well in your deliberations and I thank you for your attention.