

Review of the Economy for the First Six Months of 2004

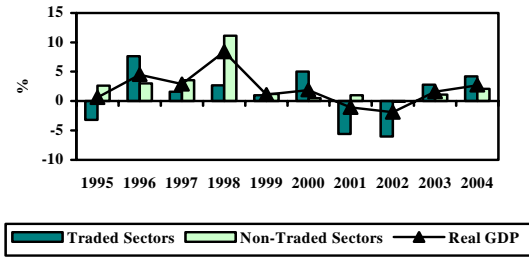
During the first six months of 2004, the Barbadian economy grew by approximately 2.7%, maintaining the momentum generated over the last 21 months. The improved first-half outturn primarily reflected expansions in the tourism, wholesale and retail and transport, storage and communications industries. Traded activity, led by tourism, rose by an estimated 4.3%, while non-traded output was about 2.0% higher.

Sectoral Performance

Driven by a robust first quarter performance, the tourism sector continued to be the main engine of growth expanding by an estimated 10.4% in the January to June period this year, the highest first-half growth

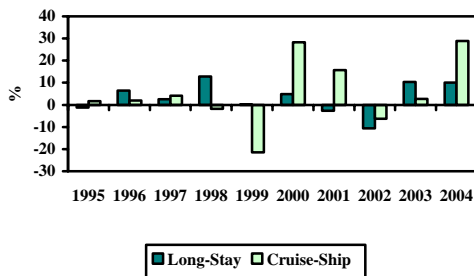
rate in a decade. Long-stay tourism performed well, due largely to increased airlift capacity, the continued recovery in most of Barbados' source markets and the staging of the third test match between England and the West Indies in Barbados. During the first five months of 2004, arrivals from the UK were up by 10.5%, while visitors from Canada and the US rose by 13.9% and 5.6%, respectively. Additionally, arrivals from Trinidad & Tobago and the rest of Caricom rose by 16.4% and 20.6%, respectively. However, tourist arrivals from other countries declined by approximately 10.9%.

**Real GDP Growth Rate
(January - June)**



Short stay visitors represented by cruise passenger arrivals continued its remarkable performance increasing by an estimated 28.8% between January and May. This compares with a 4.5% growth rate during the same period one year prior. The home porting of several liners in the first three months of the year was primarily responsible for the upswing in cruise activity.

**Tourism
(January - June)**



Sugar production decreased by 5.4% during the first six months owing to lower yields caused by adverse weather conditions during the critical

harvesting period. Non-sugar agricultural output is estimated to have fallen marginally, primarily because of a decline in fish landings and lower production of fresh milk.

Manufacturing activity deteriorated by approximately 2.2%. Though there were moderate increases in beverages and tobacco and chemicals, this was offset by declines in all other manufacturing industries.

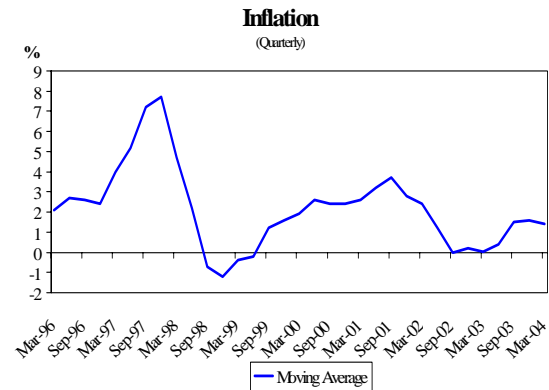
The wholesale and retail sector recorded robust growth of around 2.8%, owing to increased domestic demand and an improved tourism outturn. The liberalisation of the telecommunications market, contributed to higher activity in the transport, storage and communications industry which strengthened by 4.1%. Additionally, real output in the mining and quarrying industries rose marginally, reflecting a pick-up in quarrying activity.

However, output in the construction industry increased by only 0.7% as a

result of the completion of some major government projects in 2003. Work continued on the Airport and the Hilton Hotel as well as on private real estate ventures and tourism related projects.

Due to overall expansion in economic output, the unemployment rate fell to 10.1% compared with 11.7% in the first quarter of last year. The rate of unemployment among both males and females contracted by just under two percentage points to reach 8.8% and 11.6%, respectively.

The average rate of inflation was 1.4% at the end of March 2004, in contrast to one year ago when the average price level remained basically unchanged. Prices in the food, transportation and medical and personal care categories recorded the largest increases. However, declines were recorded in the costs of household operations and supplies, clothing and footwear and alcoholic beverages and tobacco.



At the end of June 2004, domestic deposits had risen by approximately 8.6%, compared to 1.7% a year ago reflecting the improved level of activity.

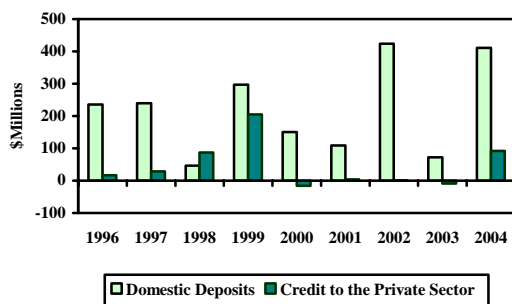
Commercial bank credit to the non-financial private sector expanded by an estimated 3.5% during the half-year, on account of an increase in corporate financing to facilitate the takeover of a domestic firm. Additionally, between January and May 2004, loans to the construction and distribution industries rose by 11.4% and 1.5%, respectively. However, there were contractions in credit to manufacturing and tourism-related establishments. Significant borrowings in other sectors included borrowings by the Barbados National Terminal Company Ltd. to assist with the construction of their new terminal

facilities leading to a 37.9% rise in credit to statutory bodies.

The build-up in domestic deposits, coupled with the reduction in the minimum securities requirement, increased the calculated excess liquidity ratio slightly to 21.9% at June 30, 2004. Consequently, the treasury bill rate fell from 0.64% at the end of last year to 0.35% at the end of the review period. Persistent high liquidity put pressure on the weighted average loan rate which declined by 41 basis points to 9.75% at May 31, 2004.

expanded by approximately 2.4%, due primarily to greater excise taxes (15.3%), import duties (13.1%) and VAT receipts (6.5%), reflecting the improved economic activity. Conversely, direct tax collections contracted by 3.9% due to a fall-off in corporate and personal tax receipts; corporate tax takings contracted by 3.8% following the reduction in the corporate tax rate to 36% while the 4.2% down-turn in personal taxes resulted from the increase in the tax allowance threshold, as well as the reduction in the marginal tax rate.

**Growth in Domestic Deposits and Private Sector Credit
(January-June)**



For the period January-June 2004, government recorded an estimated fiscal deficit of \$24.5 million, approximately \$14.6 million less than for the corresponding period in the previous year. Total revenues

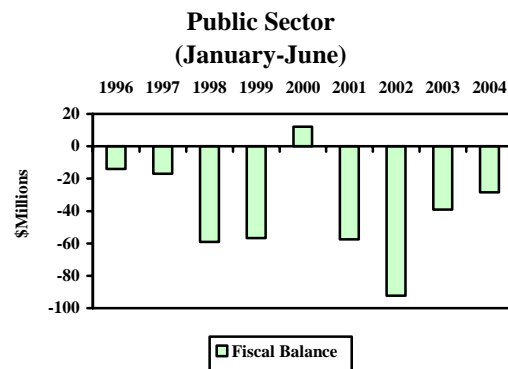
Total expenditure of central government grew by 1.3% over the review period, slightly lower than the growth rate recorded one year ago. This was primarily the result of a moderate rise in transfers and subsidies. Outlays on wages and salaries rose marginally, following an increase in public workers' wages and salaries, while outlays on goods and services fell by 1.2%. Interest payments contracted slightly as the reduction in domestic interest payments (\$1.5 million) offset the

expansion in foreign interest payments (\$1.2 million). Capital expenditure contracted by 8% as some major Government projects approached completion, after an expansion of 2.9% in the corresponding period one year prior.

The fiscal deficit was financed mainly from foreign sources by way of project funds. Government was a net depositor at the Central Bank of Barbados, while the National Insurance Board and commercial banks provided additional funds to cover some of Government's operations.

On the balance of payments, a significant pick-up in retained imports and the continued poor performance of the export sector resulted in a current account deficit of approximately \$52.2 million, substantially greater than last year's first-half deficit of \$7.3 million. Buoyed by higher food and beverages imports, the consumer goods category grew by 19.9% during the first six months of 2004. Moreover, capital goods imports

expanded by 30.7% on account of the importation of equipment for power generation and cellular phones to meet the increased demand after the launch of two new cellular companies in the first quarter.



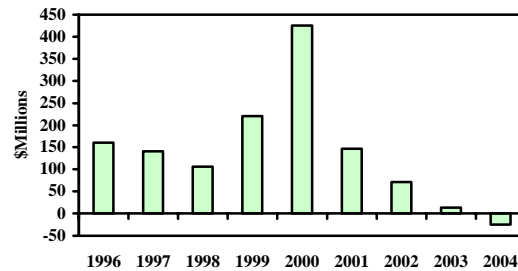
Domestic exports remained basically unchanged during the first half of 2004, after an expansion of 2.6% one year ago, despite greater exports of electronic components (18.3%). However, there were declines in the food and beverages (1.9%) and chemicals (1.8%) categories. Sugar exports contracted by 3.1%, but further receipts are anticipated next quarter.

Net capital inflows rose and the surplus on the capital and financial account at the end of June 2004 was

approximately \$146.4 million, compared to a surplus of \$52.9 million one year ago. Net long-term public capital inflows totalled \$21.5 million, in contrast to net outflows of \$36.6 million in the first half of last year when the government repaid a loan on behalf of Hotels & Resorts Ltd. Long-term private sector inflows were estimated at \$75.6 million and were mainly to the tourism, real estate and energy utility sectors.

For the first time since 1999, the Net International Reserves (NIR) declined in the January-June period, falling by an estimated \$25.1 million, in contrast to a \$12.8 million rise in the corresponding period a year ago. This extraordinary development was the result of a confluence of factors: Tourism earnings increased but were offset by stronger growth in retained imports, and there were additional outflows of \$46.3 million as the second tier reserves increased to \$130.5 million by the end of June 2004.

**Net International Reserves changes
(January-June)**



Outlook for the Remainder of 2004

The outlook for the rest of 2004 continues to be promising. The economy is expected to grow by between 2.0% and 2.5% in 2004, with the tourism sector providing the main impetus for growth. An increase in employment is anticipated. Average price inflation is forecasted to be about 2%, as the rise in petroleum prices will likely filter into other categories.

Wholesale and retail trade should benefit from rising disposable incomes on account of the reduction in the income tax rate. Construction value-added is anticipated to be slightly higher than one year ago; activity in the industry will continue to be propelled by the Airport expansion project, tourism related

ventures and road rehabilitation. Manufacturing, however, is likely to remain sluggish throughout the year.

Credit is expected to rise in response to the reduction in lending rates, particularly a declining mortgage rate. Nevertheless, liquidity in the banking system is expected to remain high.

Significant import growth during the year is expected to negate the anticipated expansion in receipts from services, resulting in a worsening of the current account deficit. Consequently, a contraction in the NIR is likely to occur.

With increased imports, growth in indirect tax receipts from VAT, excise taxes and import duties is expected. This, coupled with sluggish capital expenditure activity, should lead to a further narrowing of the fiscal deficit.

28 July 2004