

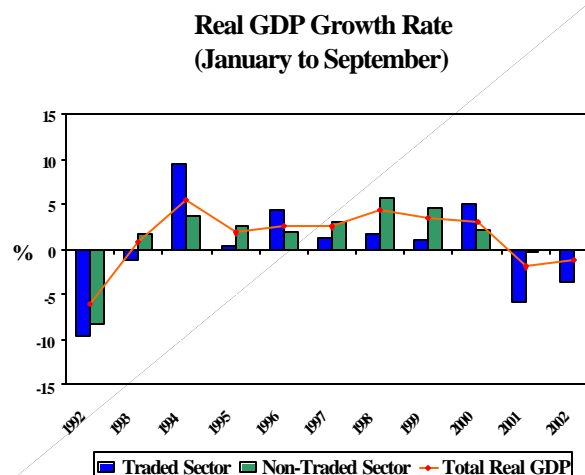
REVIEW OF THE ECONOMY FOR THE FIRST NINE MONTHS OF 2002

OVERVIEW

Following a decline in real Gross Domestic Product (GDP) in the first half of 2002, the Barbadian economy is estimated to have made notable gains in the third quarter, occasioned by an improvement in tourism, and, to a lesser extent, wholesale and retail activity. Nevertheless over the nine-month period ending September, real economic activity in Barbados is estimated to have contracted by 1.1%, compared to a 2% decline in the same period a year earlier. This outcome largely reflected the prevailing uncertainty in the international environment and weak domestic demand.

Commercial bank credit was also affected by sluggish demand, and contributed to the steady rise in excess liquidity during the review period. As a

consequence of the weak economic outturn, the unemployment rate at the end of the second quarter was slightly higher than at June 2001.



Government was, however, able to utilise some of the liquidity in the system to finance its growing deficit, which was largely the result of a counter-cyclical expenditure policy, designed to boost economic activity. The generally poor performance of the foreign exchange earning sectors, as well as significantly

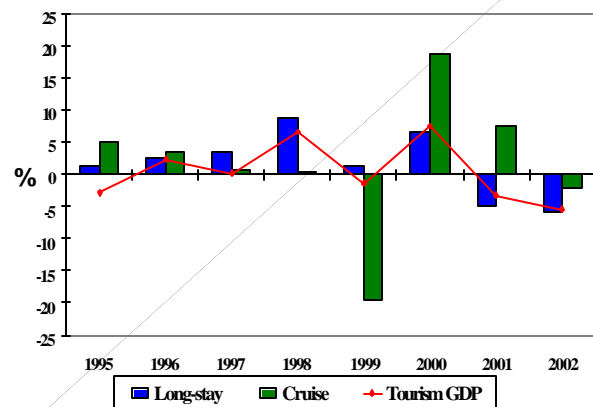
lower capital inflows when compared to last year, led to only a modest rise in the net international reserves (NIR). Inflation remained low during the first three quarters, principally as a result of falling import prices and depressed local demand.

SECTORAL PERFORMANCE

Notwithstanding the improvement in tourism value-added in the third quarter, tourism output for the first nine months contracted by an estimated 5.4%, compared to a 3.2% reduction for the corresponding period a year ago. With the exception of tourist arrivals from the US and Trinidad and Tobago, which recorded some growth, arrivals from most of Barbados' other traditional markets fell during the review period. With respect to the UK, Canada and Germany the number of visitors decreased by approximately 13.2%, 16.6% and 8.7%, respectively. Arrivals from the UK, the main-stay of the tourism industry, dipped on account of the withdrawal of a number of charters and increased competition. In contrast, the number of US visitors expanded by 11.7%, primarily because of an enhanced marketing effort by the Barbados Tourism Authority (BTA), and

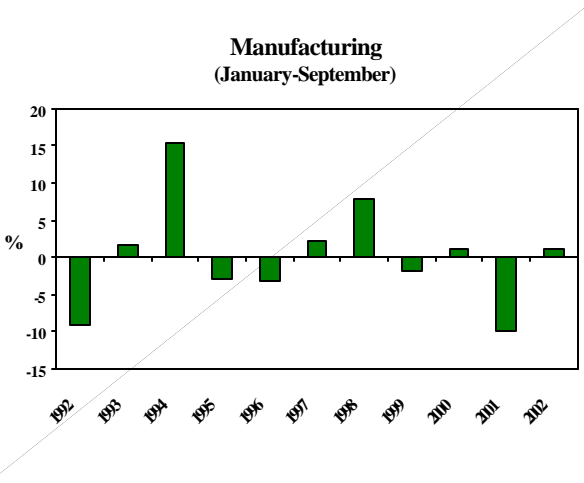
the introduction of US Airways, which increased capacity from non-traditional areas of the US. Arrivals from Trinidad and Tobago rose by 16.7%, mainly as a result of intensified promotion of the Crop-Over festival, and the hosting of more regional games in Barbados. Cruise-ship arrivals, despite an improvement in the third quarter, were 2.1% lower than in the corresponding period of 2001, as depressed demand for this type of travel led to a fall-off in the number of cruise-ship calls.

Tourism
(January to September)



The agricultural sector continued to perform poorly. In addition to the decline in sugar production, output of non-sugar agriculture decreased by an estimated 2.5% during the first three quarters of 2002, due to lower levels of milk and chicken production as well as fish landings.

The manufacturing sector, which was hard-hit by the effects of trade liberalisation, was able to benefit somewhat during the first nine months of this year from the continuation of the “Buy Local” campaign, and the 60% tariff imposed on selected imported goods. As a result, output in this sector expanded by approximately 1.2%, in contrast to a near 10% decline in the corresponding period a year earlier. Those sub-sectors recording the most significant gains were food processing and miscellaneous manufacturing, while downturns were registered for beverages, electronics and non-metallic mineral products.



Construction activity is estimated to have contracted by 5.6% during the review period, due to a fall in residential construction and the completion of large-scale commercial projects that had fuelled output in the sector during the past three years. This outturn follows

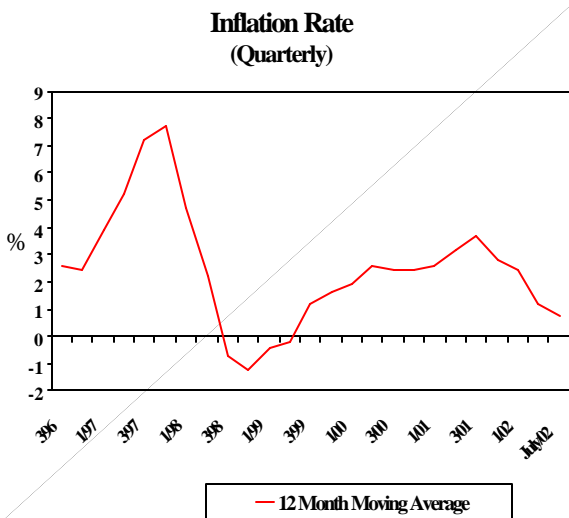
decreases of 2.9% and 0.4% in the corresponding periods of 2000 and 2001, respectively.

After shrinking by approximately 2.5% in the first half of 2002, the wholesale and retail sector is estimated to have picked-up in the third quarter, as the sector benefited from the spill-over effects of improved tourism activity during that period. Consequently, the decline in distribution slowed to 1.2% in the first nine months of 2002, from a reduction of 1.9% in the corresponding period a year ago. Transportation, storage and communications as well as electricity, and gas, are also estimated to have improved during the review period.

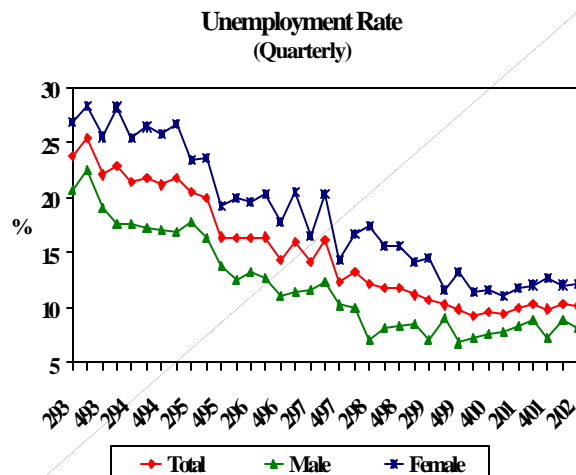
Despite an uncertain global environment, the international business sector was able to record an increase in the number of entities granted permission to operate during the first nine months of the year. Over the review period, the number of licensed international business companies grew by 197, compared to 187 in the same period last year. There were also six new licences issued to exempt insurance companies, up from two a year earlier, while permits to exempt

management insurance companies rose from one last year to three. The number of licences issued to new offshore banks remained unchanged at four. In contrast, 15 societies with restricted liabilities were granted permission to operate during the year, compared to 18 in the corresponding period of 2001.

The rate of inflation continued to be low, and at the end of July was estimated at 0.7%, down from 3.5% at the end of July 2001. Those categories that declined were fuel and light, household operations and supplies and clothing and footwear, while moderate price increases were recorded for food, alcoholic beverages, housing and medical and personal care.



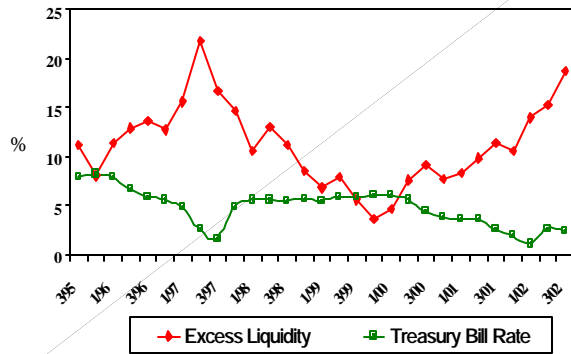
The unemployment rate at the end of June, 2002 was estimated at 10.1%, up marginally from the 10% recorded a year earlier. Employment in the general services and construction sectors decreased, offsetting gains in finance and business services, Government and wholesale and retail. The female unemployment rate rose to 12.1% from 11.8% a year earlier, while the male unemployment rate fell from 8.3% to 8.1% over the same period.



The high levels of liquidity evident in the first half of 2002 continued into the third quarter, as the excess liquidity ratio was 18.8% at the end of September, compared to 15.3% at the end of June, and 11.4% at the end of the third quarter a year ago. These conditions encouraged intense competition for treasury bills, which led to a decline in

the average discount rate from 2.71% at September 30, 2001 to approximately 2.51% at the end of the review period.

**Selected Financial Indicators
(Quarterly)**



The relatively weak domestic demand was reflected in a decline in commercial bank credit to the private sector. During the first three quarters of the year, private sector credit contracted by approximately \$51.6 million, in contrast to an increase of \$22 million in the same period in 2001. Reduced lending to private individuals and public financial institutions were the main contributors to the decrease, negating an expansion in credit to private financial institutions.

Domestic deposits grew by approximately \$343.8 million, following a rise of \$220.9 million in the corresponding nine-month period of 2001. The main reasons for this outcome were Government's draw-down

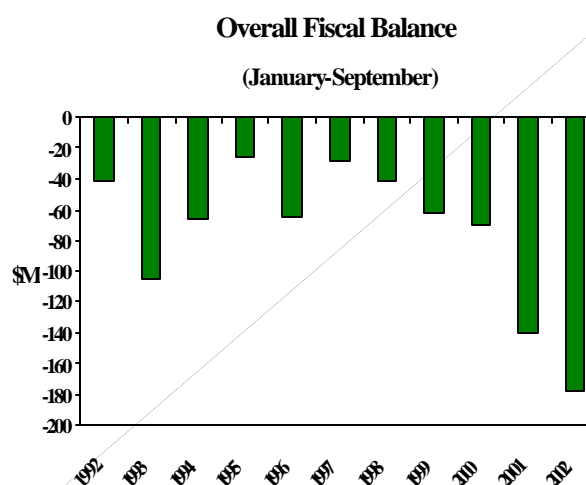
of its special deposits at the Central Bank and a rise in the ways and means account, the proceeds of which were subsequently re-deposited by the private sector in the banking system. The deposits by persons who sold their shares in Life of Barbados Ltd. to the Barbados Mutual Life Assurance Society also contributed to the growth in domestic deposits during the period. As a result, deposits of private individuals rose, along with those of financial institutions, and statutory bodies. Conversely, deposits of business firms contracted as a result of the lower economic activity.

Government's deficit widened to an estimated \$174.6 million over the first nine months of the year, up from the \$130.2 million recorded a year earlier. Total revenue decreased marginally by 0.2%, following an increase of nearly 2% in the same period of 2001, as a fall in direct taxes exceeded growth in indirect tax receipts. The 8% dip in direct taxes largely reflected declines in the collection of corporate and property taxes. Corporate taxes are estimated to have fallen by 18.9% due to reduced profitability of some businesses, while the 12.4% contraction in property taxes

followed a strong performance in 2001 when the early issuance of property tax bills facilitated the timely collection of revenues. The only category to record any significant improvement was personal taxes, which expanded by 3.2%, compared to a growth rate of 4.2% for the same period a year ago. Indirect taxes however, rose by an estimated 6% on the strength of increases in the collections of VAT and import duties, which grew by 5.1% and 29.2%, respectively. The expansion in VAT receipts reflected some measure of success in the collection of arrears, while the outcome for import duties can be attributed in part to the 60% tariff levied on selected goods. Conversely, excise taxes were 12.3% less after a fall-off of 11.9% in the corresponding nine months of 2001.

On the expenditure side, total spending is estimated to have risen by nearly 3% during the period January to September, compared to an expansion of 6.3% in the corresponding period a year ago. Outlays on recurrent items inched-up by 0.6% due to increases in goods and services (10.6%) and wages and salaries (0.5%), which reflected higher remuneration and rising public sector

employment. On the contrary, transfers and subsidies declined marginally and



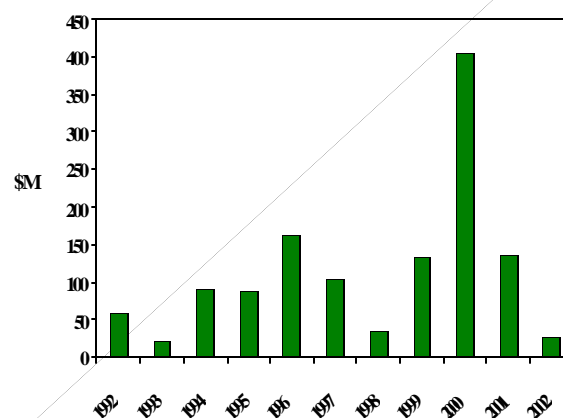
interest payments contracted by 4.8% because of lower domestic outlays. Capital expenditure, however, is estimated to have escalated by approximately 22.9% during the review period, which partly reflects Government's counter-cyclical expenditure policies, and compares with an increase of only 2.1% in the equivalent period one year earlier. The main factors responsible for the growth were the on-going work on EDUTECH, the South Coast Sewerage Project and upgrades at the air and sea ports.

Financing for public sector operations came primarily from Government's deposits at the Central Bank and borrowings from the institution. At the end of the review period, therefore,

funding from the Central Bank totalled \$220.7 million, in contrast to the previous three years when Government was a net depositor with the Central Bank. The National Insurance Scheme and commercial banks also increased their credit to Government, by \$72.2 million and \$147.2 million, respectively, while credit by other entities decreased by \$297.6 million. Net external financing more than doubled to \$25.3 million, as project funds amounting to \$77.4 million surpassed amortisation payments of \$52.2 million.

Official holdings of foreign reserves are estimated to have expanded by \$27.3 million in the first three quarters of 2002. This compares to a rise of \$137.9 million in the corresponding January to September period a year earlier, and represents the smallest nine-month increase in the NIR since 1993. Reduced earnings from tourism and domestic exports along with lower capital inflows were primarily responsible for this outturn, offsetting the effect of a reduction in imports.

Change in Net International Reserves
(January-September)



The rate of decline in domestic exports accelerated to 8.6%, from 7.4% in the same period a year ago, as earnings from all categories fell. The most substantial declines were recorded for sugar (14.4%), electronic components (28.3) and chemicals (5.3%). Net earnings from services also contracted, by 2.9%, as the improvement in tourism receipts in the third quarter was insufficient to offset the fall in the first six months of the year.

Retained imports, negatively affected by recession and general uncertainty in the business sector, slid by an estimated 4.4% after decreasing by 4.7% in the corresponding period in 2001, as imports of intermediate and consumer goods contracted. Imports of

intermediate goods were 8.3% below last year's level, as purchases of construction materials tapered-off, while a reduction in motorcar imports contributed to the 3.9% decline in consumer goods. Imports of capital goods, however, rose by 1.6%, following a decline of 10.6% in the nine-month period of 2001.

During the review period, Barbados recorded a capital account surplus of \$96 million, compared to one of \$170.9 million in 2001. While net long term private sector funds of \$75 million were received for tourism-related projects and public utilities, this amount was less than half that for the comparable period a year earlier. The public sector also received a net inflow of capital in the amount of \$17 million in contrast to net outflows of just over \$9 million which were recorded for the same period in 2001.

OUTLOOK FOR THE REST OF 2002 AND 2003

There are signs that Barbados is beginning to emerge from the recession experienced over the past several

quarters. However, the pace at which the Barbadian economy will emerge from this recession will be influenced, in large measure, by the extent of the uncertainty still characterising the international economy in the near-term. In addition to trade liberalisation and globalisation, which have severely affected the manufacturing and agricultural sectors, Barbados could also be adversely affected should there be a military invasion of Iraq. This could have a negative impact on energy prices and the propensity to travel. However, in the absence of any serious global setbacks, output is expected to rise in the fourth quarter and real output for the year is forecasted to decline by less than 1% in 2002, following the slump of 2.7% in 2001.

The recovery in tourism, which started in the third quarter of the year is anticipated to carry on into the final quarter of 2002, as the sector should continue to benefit from the enhanced promotional efforts. As a result, the decline in value-added in the tourism sector for the year as a whole is expected to be about half the 5.9% recorded in 2001. The growth of the manufacturing sector during the first

nine months of 2002 is also projected to extend to the rest of the year owing to the "Buy Local" campaign, the 60% import tariff and the recently implemented WTO safeguard mechanism. In the non-traded sectors, electricity gas and water, transportation storage and communications and business and other services are expected to record gains. Activity in the construction sector for the remainder of the year is likely to benefit from on-going work on the Hilton Hotel, EDUTECH, the South Coast Sewerage Project, the Bridgetown Road and Safety Improvement Project and the Urban Rehabilitation Programme to name a few. Consistent with the pick-up in tourism towards the end of the year, activity in the wholesale and retail sector is also projected to improve by year-end. In light of the anticipated increase in activity for the rest of the year, no further employment losses are expected. Inflation is also forecasted to remain relatively low, at around 2%.

The fiscal balance is projected to climb to around \$200 million or just over 4% of GDP for 2002. Capital expenditure is likely to rise by around 20%, as work progresses on infrastructural, housing

and educational programmes, while current spending is expected to rise by around 1% on account of higher wages and salaries. Total revenue should also increase, though at a slower rate than expenditures, reflecting higher collections of personal taxes, VAT and import duties. Financing for the deficit is forecasted to come from domestic sources, primarily through a further reduction in Government's deposits at the Central Bank.

The NIR is anticipated to decline by approximately \$45 million, following an underlying reserve increase of \$145.5 million in 2001. Lower export earnings, coupled with reduced public and private sector inflows are expected to be the main contributors to the reserve loss.

Liquidity is projected to tighten slightly towards the end of the year resulting from slower growth in deposits coupled with a modest expansion in credit, on account of greater spending by businesses and individuals.

The Barbadian economy is expected to return to its growth path in 2003, barring any global and other unforeseen impediments to real output. The

increase in real GDP in the up-coming year is anticipated to be in the region of 2%, on the strength of traded sector activity, particularly tourism, sugar and manufacturing. The expected moderate upturn in tourism is based on the assumption that the sector will continue to benefit from the enhanced promotional efforts of the BTA. The forecast for manufacturing however, is predicated on the sector profiting from the recent measures implemented to protect the industry. The outturn for the traded sectors should also have positive spin-off effects for non-traded activity, which would be expected to post some growth in 2003.

The projected rise in real GDP, however, could lead to an increase in imports, which may result in minor reserve losses, despite an anticipated upturn in tourism receipts. Capital inflows are also expected to be somewhat lower in the following year. The anticipated pick-up in economic activity in 2002 is also projected to lead to an increase in credit and possibly precipitate a decline in liquidity. Public revenues should also benefit from the likely increase in economic activity.

The challenges in the near term will be to bring the deficit under control and to allow normal repayments to reduce debt levels. Government is expected to rein in its counter-cyclical policies in 2003 and revert to modest deficits obtained prior to 2001 of less than 2.5% of GDP. This will require that private sector activity increases more rapidly if the economy is to reduce its dependence on government for effecting growth in the economy.

The process of gradual financial liberalisation is expected to continue as Barbados positions itself for the Single Market and Economy. It will be important in this context that we take steps to contain operational costs and to generally improve our competitiveness, both in relation to CARICOM and to the rest of the world. Wage control and productivity improvements will therefore be very important.

November 5, 2002