



BARBADOS

STAFF REPORT FOR THE 2017 ARTICLE IV CONSULTATION

January 11, 2018

KEY ISSUES

Context. The economy is slowing, following the recovery in 2016, reflecting an increased pace of fiscal consolidation and policy uncertainty, partly relating to the forthcoming elections. International reserves, which are already low, continue to decline. While there is significant progress in reducing the high fiscal deficit, the government will fall short in meeting the ambitious fiscal adjustment targets set in the May 2017 budget. The adjustment, if maintained, will lead to a decline in the debt-to-GDP ratio, but debt will remain unsustainable. Further delays in privatization will lead to a continued decline in reserves, while large financing requirements remain a serious challenge.

Focus of the consultation and key policy recommendations. Discussions focused on the need to continue fiscal consolidation, rebuild external reserves, support economic growth, and maintain financial stability. Balancing the budget within three years, and maintaining the balance thereafter, while challenging, would help address financing needs and decisively place the debt on a downward trajectory. The fiscal adjustment should focus on reducing expenditure, centered around cutting transfers by reforming state-owned enterprises (SOEs) and public pensions. The revenue effort should continue by broadening the tax base while increasing the overall progressivity of taxation. Strengthening the business climate and competitiveness would support economic growth. Eliminating reliance on the Central Bank financing of the government deficit would make monetary policy consistent with maintaining the peg.

Authorities' views. The authorities broadly agree with the staff assessment of the critical challenges and policy recommendations, although they indicated that the pace of adjustment may need to be more gradual. They recognize that the economy is slowing due to fiscal consolidation and external factors. They acknowledge that the fiscal deficit this year will be larger than expected and note some challenges with budget implementation. In particular, SOEs reforms have been slow, awaiting critical decisions on the modification of the social programs. They anticipate that the dialogue with the private sector in formulating the Barbados Sustainable Recovery Program will support a consensus on how to achieve these objectives. The authorities remain focused on stabilizing international reserves and are committed to maintaining the exchange rate peg.

Approved By
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The mission, consisting of J. Gold (Head), T. Dowling, G. Impavido, J. Okwuokei, B. van Selm (all WHD), D. Gurara (SPR), and A. Świstak (FAD) visited Barbados during November 7-21, 2017. N. Horsman and L. Zorn (all OED) joined for the concluding meeting. Y. Li and A. Veras provided excellent assistance. Outreach included meetings with the leader of the opposition, the private sector, labor organizations, and academics.

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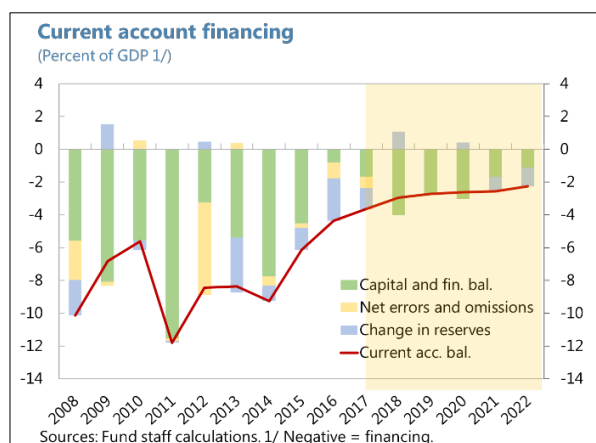
CONTEXT

1. Reflecting the impact of a prolonged recession following the global financial crisis, and inadequate fiscal policy, Barbados is contending with large fiscal deficits, high debt, and low reserves. The May 2017 budget sought to address the increasing funding challenges and falling reserves with an ambitious fiscal adjustment that aimed to eliminate new funding requirements including with receipts from additional privatization. The large adjustment was also intended to reverse the debt trajectory, but would slow growth and increase inflation. However, weaker than expected revenues and budget implementation slippages, suggest that the deficit is likely to remain significantly higher than planned with correspondingly large funding requirements. Debt also remains unsustainable, while low and falling international reserves raise vulnerabilities. Against this background, tourism continues to do well, some competitiveness indicators, although deteriorating, remain stronger than those of Barbados' peers, and the Human Development Index remains significantly higher than in the rest of the region.

RECENT DEVELOPMENTS

2. The economy is slowing in response to a large fiscal adjustment and weak confidence. Growth is estimated at 1.6 percent in 2016, and after a robust performance in 2017H1, it has sharply slowed in the third quarter. Long-stay arrivals increased by 6.2 percent in the first three quarters of 2017, after a strong performance in 2016.¹ Inflation increased to 6.6 percent in October 2017, following an increase to 3.8 percent at end-2016. Confidence is low reflecting repeated credit rating downgrades, falling reserves, protracted reforms of the public sector, and policy uncertainty, partly related to the forthcoming elections.

3. Notwithstanding a narrowing in the current account balance, reserves continue to fall. In 2016, the current account deficit (CAD) narrowed by 1.7 percentage points to 4.4 percent of GDP. However, net international reserves (NIR) fell to US\$340 million, or two months of imports, as official disbursements and private inflows deteriorated. In the first three quarters of 2017, the CAD remained broadly unchanged relative to the same period last year—despite a sharp fall in consumer and capital goods imports in the third quarter. This reflects a sharp increase in fuel imports of 23 percent because of a steep price increase. The financial account also deteriorated in the third quarter driven by net official outflows (debt service) and lower



¹ Cruise-ship arrivals plummeted by 21.3 in the third quarter relative to the same period last year (nonetheless, still increasing by 17.6 percent in the three quarters) but cruise spending represents less than 5 percent of total tourism spending.

private inflows. Consequently, NIR declined to US\$274.8 million, or 1.6 months of imports at end-September 2017.

4. Fiscal performance improved but the deficit remains large and the debt is high. In FY2016/17, the deficit declined to 5.5 percent from 8.9 percent of GDP in FY2015/16.² Tax revenues increased by 3.1 percentage points, in part, on account of special tax receipts (increase of 0.7 percentage points) as well as the new 2 percent National Social Responsibility Levy (NSRL), introduced in the August 2016 Budget.³ Reduced spending on wages, goods and services, and transfers offset a large increase in debt service.⁴ Transfers again exceeded planned levels but were lower than in FY2015/16 by 0.8 percentage points of GDP. Central Government debt (including the National Insurance Scheme (NIS)) increased to 137 percent of GDP, from 135 percent in FY2015/16, and up from 99 percent in FY2011/12.

2014/15-2016/17 Fiscal Outturn			
	2014/15	2015/16	2016/17 (e) ^{1/}
<i>In percent of GDP</i>			
Total Revenue	25.7	26.1	28.5
Tax	23.3	24.0	27.1
Non-tax	2.4	2.0	1.4
Total Expenditure	33.3	35.0	34.0
Current Exp (w/o Interest)	24.2	25.6	24.0
Interest	7.0	7.1	7.7
Capital Exp	2.1	2.3	2.3
Deficit	-7.5	-8.9	-5.5

^{1/} Revenue on gross basis (tax refunds in arrears not netted out)
Source: Barbados authorities and IMF staff calculations

5. The government embarked on an ambitious fiscal consolidation but it is likely to fall short of its objective. The May 2017 Budget sought to significantly reduce the deficit, in line with staff recommendations (Box 1), and eliminate new funding requirements with the assistance of privatizations. The budget was comprised of large tax increases, including an increase in the NSRL from 2 to 10 percent, expenditure cuts, interest bill reductions, and privatizations. However, several factors have led to a weaker performance, mainly (i) lower revenues from the NSRL, as a result of a narrowing of the base to exclude tourism, the International Business and Finance Sector (IBFS), pharmaceuticals and selected food items, and a sharper-than-expected fall in imports in the third quarter; (ii) higher SOEs transfers because of additional supplementary budget allocations; and (iii) postponement of the debt liability

May 2017 Budget Measures				
Main Measures	Fiscal Impact (estimate as of:)			
	Jun-17		Nov-17	
	FY17/18	FY18/19	FY17/18	FY18/19
	<i>(Percent of GDP)</i>			
• Increase in NSRL from 2 to 10 percent	2.1	2.6	1.4	1.7
• Increase in excise taxes on gasoline and diesel	0.5	0.6	0.5	0.6
• 2 percent commission on FX sales	0.4	0.5	0.4	0.5
• Tax amnesty for 6 months	0.3	0.0	0.1	0.0
• Planned cuts in current expenditure	0.8	0.8	0.3	0.3
• Interest bill reduction (voluntary exchange of debt instruments with NIS and CBB)	0.5	0.7	0.0	0.0
• Additional divestment of government assets	0.7	0.0	0.2	0.0
Total estimated change in deficit^{1/}	3.3	4.8	1.4	2.5

^{1/} Budget measures do not add up to the total estimated change in deficit due to other factors impacting projections of revenue and expenditures; also, divestment receipts are treated as financing item.
Source: Barbados authorities and IMF staff calculations

² Revisions reflect delayed tax refund payments, a correction for property tax from accrual to cash, and higher goods and services, have led to an increase in the FY2015/16 deficit from 7.0 to 8.9 percent of GDP. FY2016/17 estimates are gross of tax refund and may be revised down by about 1 percent of GDP following payment of tax arrears.

³ One-off increase reflecting bringing to account prior year sundry revenue (e.g., fines, penalties and various fees and charges) held previously in suspense accounts.

⁴ The interest bill increased due to assuming by the Government the debt of Barbados Agriculture Management Company (B\$190 million) and higher interest rates.

management operation. Staff project the primary surplus to increase to 3.7 percent of GDP from 2.2 percent in 2016/17, relative to the 2.3 percent projected in the 2016 Article IV staff report. The fiscal deficit is projected to decline to 4.1 percent of GDP relative to 5.5 percent the previous year.

Box 1. Implementation of 2016 Article IV Consultation Recommendations

Areas of progress:

- **Resuscitate fiscal adjustment to stabilize debt and reduce funding requirements.** Tax measures introduced in August 2016 and May 2017 budgets, together with continued efforts to contain current spending, have led to sizable fiscal consolidation, but more is needed to achieve fiscal and debt sustainability.
- **Revitalize revenue authority reform.** The Barbados Revenue Authority (BRA) is making progress to improve tax administration and tax compliance, including by implementing a new IT system, establishing a Large Taxpayer Unit and a Tax Management Unit tasked with a risk-based compliance management program, and by incorporating TADAT recommendations into BRA's strategic plan. The planned integration of Customs and the BRA has however stalled.
- **Ensure consistency of monetary policy with the exchange rate peg.** The CBB has significantly reduced its new government funding, but commercial banks have been required to pick up most of this funding through increased reserve requirements.
- **Improve data quality.** With a focused effort by the Barbados Statistical Service and IMF TA, significant progress has been made in improving national accounts.

Areas of limited or no progress:

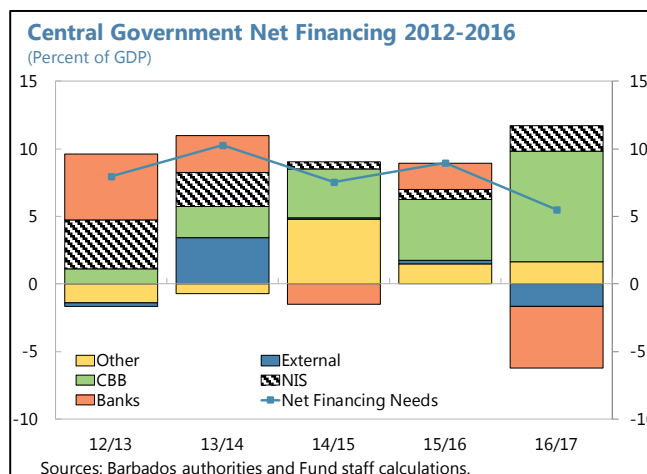
- **Take decisive steps to reform state-owned enterprises.** The pace of SOEs reforms has been slow; while transfers have been marginally reduced in FY2016/17, they could increase again in FY2017/18 as there has been limited structural reforms of SOEs. A new Financial Management and Audit Act, currently with the Cabinet, could strengthen the oversight of SOEs and facilitate their reform if implemented.
- **Improve public services and eliminate growth impediments.** There was no progress in this area. The Government is collaborating with the private sector to develop a reform plan in the context of the Barbados Sustainable Recovery Program.
- **Maintain NIS integrity.** The government continues to pay its social security contributions and rents to NIS through issuing new securities rather than cash, increasing NIS' already very high holdings of government debt.
- **Eliminate arrears.** Central government arrears stabilized in FY2016/17 at about 4 percent of GDP, but have significantly risen in the first half of FY2017/18 to 5.4 percent of GDP.

6. Reforms of SOEs have stalled, partially reflecting weaknesses in the oversight framework. The Management Accounting Unit (MAU) and the Parastatal Oversight Committee (POC) were established in 2015 following IMF recommendations but without committed policy support for reforms. The MAU is tasked with collecting financial statements, standard business plans, financial targets, and monitoring the performance of the SOEs. However, it does not have adequate resources or authority and it collects some data without a clear reporting or analytical framework.

The POC is an advisory group that lacks a clear reform mandate to monitor or follow up on implementation.

7. Financing challenges intensified with the decline in funding from official creditors and commercial banks.

In FY2016/17, gross financing needs were about 47 percent of GDP, largely met by the Barbados Central Bank (CBB) and the National Insurance Scheme (NIS) while banks reduced their exposure to sovereign debt by 4.8 percentage points of GDP. In the first half of FY2017/18, commercial bank holdings of government debt increased by about 2.2 percentage points of GDP following an increase in the minimum

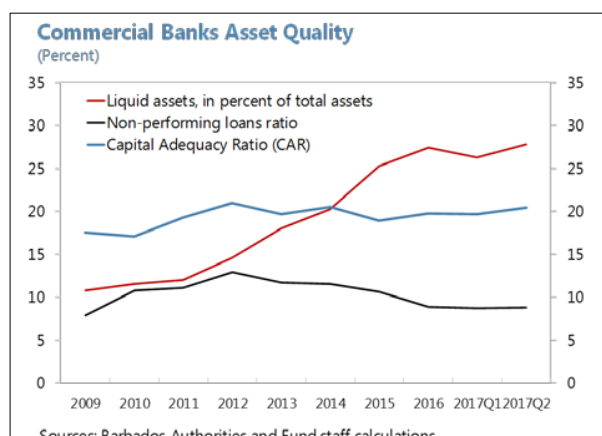


statutory holding requirements. In May 2017, the CBB raised banks’ statutory minimum requirement for government holdings from 10 to 15 percent of deposits, and as a result CBB net financing declined to 0.5 percent of GDP. The CBB again raised the banks statutory requirement on November 1st to 18 and 20 percent with effect on December 1st and January 1st 2018, respectively. The external financial account also deteriorated in the first three quarters of 2017 due to higher net official outflows and lower private inflows. On September 27th, 2017, Standard and Poor’s further downgraded Barbados’ long-term local currency debt to CCC because of concerns about low reserves, while maintaining short-term domestic and external ratings unchanged.⁵

8. Financial soundness indicators suggest a healthy banking system despite weak credit growth.

Private sector credit grew by 1.1 percent y/y at end-December 2016, accelerating to 1.5 percent in January to September, over the same period last year. Non-performing loans (NPLs) decreased to 8.8 percent in 2017Q2 from 9.6 percent a year earlier, while provisions covered 64 percent of NPLs. Capital adequacy (CAR) stands at 20.4 percent, sufficiently high to withstand a range of potential adverse shocks, except under extreme conditions. Profitability has increased but remains low at 1.1 percent of average assets. Liquidity remains elevated, and banks’ excess reserves at the CBB increased by 41.6 percent to B\$1.2 billion in 2016. The CBB on-lent the excess reserves to the government and created additional money, leading to a 67 percent increase in net domestic assets (NDA). The contribution of the IBFS to the economy has stabilized in recent years. More recently, new companies have started domiciling in Barbados because of changes in tax legislation abroad (IMF SM/18/8).

⁵ Standard and Poor’s also downgraded Barbados sovereign bonds on March 3, 2017 one notch to CCC+, and Moody’s followed on March 9th with a downgrade to Caa3 (with a stable outlook). It issued a further warning on November 28th, that Barbados credit profile has deteriorated but it maintained the credit rating. Barbados ratings were investment grade as recently as mid-2012.



Financial Soundness Indicators (Percent)					
	2014	2015	2016	2017Q1	2017Q2
Commercial Banks					
Capital Adequacy Ratio (CAR)	20.5	18.9	19.8	19.7	20.4
Loan to deposit ratio	70.3	65.5	62.3	63.0	62.3
Liquid assets, in percent of total assets	20.3	25.3	27.4	26.3	27.8
Non-performing loans ratio	11.5	10.6	8.9	8.7	8.8
Return on Assets (ROA)	0.7	0.9	1.0	1.1	1.1
Credit Unions					
Reserves to Total Liabilities	11.9	10.7	10.9	11.0	12.4
Loan to deposit ratio	92.8	90.8	89.3	87.6	86.5
Nonperforming loans ratio	9.4	9.0	7.6	7.1	7.8
Return on Assets (ROA)	0.9	0.9	1.1	1.1	1.3

Source: Central Bank of Barbados, Financial Services Commission.

9. The political discourse around economic issues intensified. Public debate in recent months revolved around the FY2017/18 budget. Labor actions have escalated with demands for wage increases following a nominal wage freeze since 2009 and recent tax hikes. At the same time, discussions with the private sector are ongoing to formulate a comprehensive approach to structural reforms, especially for SOEs, and to finalize the Barbados Sustainable Recovery Plan (BSRP); a new strategy to guide policy for the next few years.⁶ The Democratic Labor Party has been in power since 2008 and the next elections are due by June 2018.

OUTLOOK AND RISKS

10. The outlook for growth over the near term is weak and risks are high. Growth is expected to decelerate to 0.9 and 0.5 percent in 2017 and 2018, respectively, reflecting fiscal adjustment and policy uncertainty in view of the forthcoming elections.⁷ Average inflation is projected to accelerate to 4.5 and 5.1 percent in 2017 and 2018 respectively, mainly reflecting the increase in the NSRL. Over the medium-term, growth picks up to about 1 percent; below its historical average due to low international reserves and lingering uncertainty.

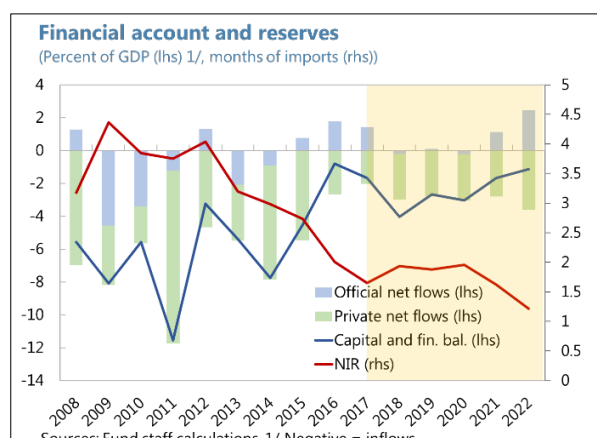
11. The higher primary balance would reduce the debt-to-GDP ratio, but it would remain high. The estimated cumulative fiscal adjustment of 2.2 percentage points by FY2018/19 would reduce the debt-to-GDP to 86 percent (120 per cent including NIS) by FY2022/23. Despite the rapid decline, debt remains high, while gross financing needs would increase to about 53 percent of GDP.

12. While the current account deficit (CAD) is expected to improve, international reserves continue to decline. For 2017, the CAD is projected to narrow to 3.7 percent of GDP, following the fiscal tightening. Reserves are projected to remain low at US\$275 million or 1.7 months of imports as a result of weak financial account. They could be lower if the expected privatization—an oil terminal and a large hotel—is delayed. In the medium term, the CAD is projected at 2.3 percent of GDP

⁶ The discussions initially took place in the context of the Social Partnership, a collaborative framework developed in the early 1990s to help implement an IMF-supported program, but the unions have withdrawn their participation.

⁷ Staff use a fiscal multiplier of 0.3.

because of weak growth and low FDI. With planned privatization, and absent further deteriorations of private and FDI flows, the international reserves are projected to stabilize at around 2 months of imports by 2020. In FY2021/22, NIR would fall reflecting larger than average external debt repayments (text chart and Table 4).



13. Domestic risks are high, primarily related to weak budget implementation and the government’s ability to sustain the higher primary surplus and stabilize external reserves (Annex I).

- Growth could be weaker than projected if fiscal multipliers are underestimated, and or if confidence continues to erode.
- Fiscal adjustment could be less than projected, due to weaker growth, weak implementation, or a reversal in policies in the run up to or after the elections.
- Financing challenges could intensify if the private sector seeks to reduce their government funding.
- Reserves may not stabilize if the two planned privatizations do not materialize, if there are fiscal slippages, and if private inflows are lower.
- New CBB funding could erode reserves and jeopardize the exchange rate peg.

14. External risks relate to potentially weaker growth in advanced economies and tighter global financial conditions. Weaker growth in key tourism source markets could slow arrivals and reduce private investment in refurbishing and expanding the tourism stock. Despite capital controls, amplification of sovereign credit concerns would put pressure on official reserves.

POLICY DISCUSSIONS

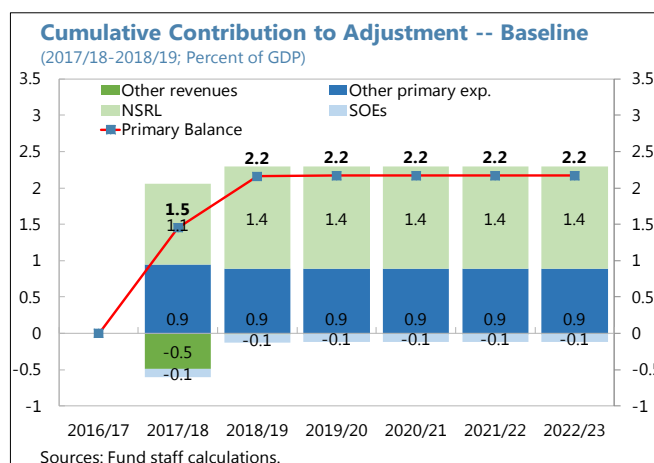
Policy discussions focused on measures to build on the recent fiscal adjustment efforts, to accelerate reforms of SOEs to allow for an enduring reduction in transfers, and achieve debt sustainability. Improving the external balance and especially rebuilding reserves must also be a priority. In addition, policy discussions included measures to support economic recovery, maintain financial stability, and address data shortcomings. The authorities remain committed to maintaining the exchange rate peg.

A. Fiscal and debt sustainability

15. Further fiscal consolidation is needed to address persistent large budget deficits and high debt. The May 2017 budget is making progress towards that objective, but more is needed to reduce financing requirements and imports, and rebuild reserves. In the absence of new measures,

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the fiscal and primary balances are projected to increase to -3.0 and 4.4 percent of GDP in FY2018/19, respectively. This reflects the full year impact of the tax measures enacted in May 2017. The cumulative fiscal adjustment relative to FY2016/17 amounts to 2.2 percentage points of GDP by FY2018/19 (text chart and text table). The debt-to-GDP ratio would fall to 86 percent of GDP (120 including NIS) by FY2022/23, while financing requirements would rise to nearly 53 percent of GDP. Given the already high debt, financing challenges, and weak international reserves, this policy stance would be insufficient to restore fiscal and debt sustainability. The DSA points to sizable risks, including from low growth, continued significant recourse to short-term debt, rising arrears, and contingent liabilities. The baseline debt path is also vulnerable to unfavorable shocks from real interest rates.

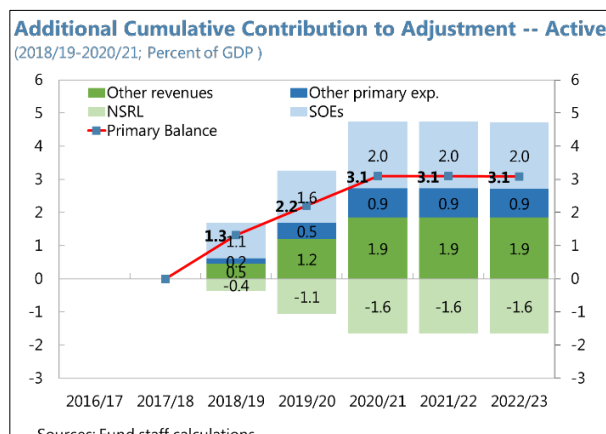


Medium-Term Macroeconomic Framework									
Baseline									
(in percent of GDP, unless otherwise indicated)									
	2014	2015	2016	Proj. 2017	Proj. 2018	Proj. 2019	Proj. 2020	Proj. 2021	Proj. 2022
Real GDP growth (percent)	0.1	1.0	1.6	0.9	0.5	0.8	1.0	1.0	1.0
Nominal GDP growth (percent)	0.0	0.5	1.5	5.4	5.6	3.7	3.7	3.7	3.7
Inflation (Average, percent)	1.8	-1.1	1.5	4.5	5.1	2.9	2.7	2.7	2.7
Current account balance	-9.3	-6.1	-4.4	-3.7	-3.0	-2.7	-2.6	-2.6	-2.3
Net international reserves	11.3	9.9	7.1	5.5	6.3	6.0	6.2	5.1	3.8
in US\$ Millions	526.0	463.0	340.5	275.3	331.7	329.4	352.3	299.3	230.7
in months of imports	3.0	2.7	2.0	1.7	1.9	1.9	2.0	1.6	1.2
	2014/15	2015/16	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22	2022/23
CG Total revenues 1/	25.7	26.1	28.5	29.1	29.8	29.9	29.9	29.9	29.9
CG Total expenditures 1/	33.3	35.0	34.0	33.1	32.8	33.0	33.3	33.3	32.9
CG fiscal balance 1/	-7.5	-8.9	-5.5	-4.1	-2.9	-3.2	-3.5	-3.4	-3.0
CG primary balance 1/	-0.5	-1.8	2.2	3.7	4.4	4.4	4.4	4.4	4.4
CG gross debt 1/	125.4	134.7	137.0	132.8	128.7	127.1	126.5	123.8	119.8
CG gross debt (excludes NIS) 1/	93.4	101.0	100.9	97.2	93.8	92.5	91.9	89.3	85.5
Gross financing needs 1/	42.7	47.4	47.0	50.9	49.6	49.5	50.1	51.8	52.7
Memorandum item									
Nominal GDP CY (BD\$ Million)	9,343	9,390	9,528	10,045	10,609	11,001	11,413	11,837	12,277
Nominal GDP FY (BD\$ Million)	9,355	9,424	9,657	10,186	10,707	11,104	11,519	11,947	12,391

Sources: Barbados authorities and Fund staff estimates and projections.
1/ Fiscal year is from April to March.

16. Substantial further fiscal effort is needed to reduce the debt-to-GDP ratio and funding requirements more rapidly. Given the urgency in addressing the high debt, funding and BOP risks, and the limited policy options, the fiscal adjustment must continue. The active scenario envisages an additional fiscal adjustment of about 3.1 percentage points of GDP (text chart and text table): i.e., an increase in the primary surplus from 4.4 percent of GDP expected under the baseline scenario in

FY2018/19 to 7.5 percent of GDP by FY2020/21. The proposed adjustment is very challenging, but given the limited policy options, it is necessary to address the difficult financing conditions. The envisaged adjustment is somewhat front-loaded to reverse the slippages relative to the May 2017 budget and address higher risk.



Medium-Term Macroeconomic Framework

Active
(in percent of GDP, unless otherwise indicated)

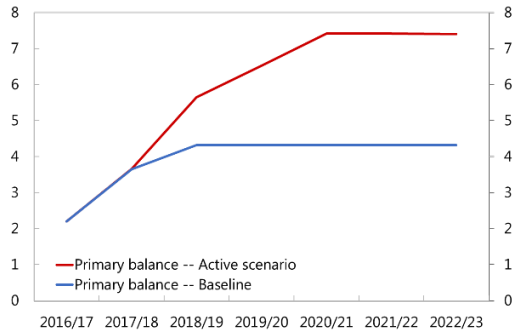
	2014	2015	2016	Proj. 2017	Proj. 2018	Proj. 2019	Proj. 2020	Proj. 2021	Proj. 2022
Real GDP growth (percent)	0.1	1.0	1.6	0.9	0.0	0.1	1.4	1.8	2.0
Nominal GDP growth (percent)	0.0	0.5	1.5	5.4	4.9	2.8	4.1	4.7	4.8
Inflation (Average, percent)	1.8	-1.1	1.5	4.5	4.9	2.7	2.7	2.8	2.8
Current account balance	-9.3	-6.1	-4.4	-3.7	-2.5	-2.2	-2.1	-2.2	-2.0
Net international reserves	11.3	9.9	7.1	5.5	7.3	8.3	10.0	10.5	10.9
in US\$ Millions	526.0	463.0	340.5	275.3	383.1	452.0	565.9	619.0	672.2
in months of imports	3.0	2.7	2.0	1.7	2.3	2.6	3.2	3.4	3.5
	2014/15	2015/16	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22	2022/23
CG Total revenues 1/	25.7	26.1	28.5	29.1	30.0	30.0	30.1	30.1	30.1
CG Total expenditures 1/	33.3	35.0	34.0	33.2	31.6	31.0	30.3	30.0	29.4
CG fiscal balance 1/	-7.5	-8.9	-5.5	-4.1	-1.7	-1.0	-0.2	0.1	0.7
CG primary balance 1/	-0.5	-1.8	2.2	3.7	5.7	6.6	7.5	7.5	7.5
CG gross debt 1/	125.4	134.7	137.0	133.0	128.5	125.5	121.0	114.0	105.5
CG gross debt (excludes NIS) 1/	93.4	101.0	100.9	97.4	93.8	91.5	88.4	82.8	75.9
Gross financing needs 1/	42.7	47.4	47.0	50.9	48.8	47.0	44.6	43.2	41.0
Memorandum item									
Nominal GDP CY (BD\$ Million)	9,343	9,390	9,528	10,045	10,538	10,828	11,277	11,802	12,371
Nominal GDP FY (BD\$ Million)	9,355	9,424	9,657	10,168	10,610	10,940	11,408	11,944	12,519

Sources: Barbados authorities and Fund staff estimates and projections.
1/ Fiscal year is from April to March.

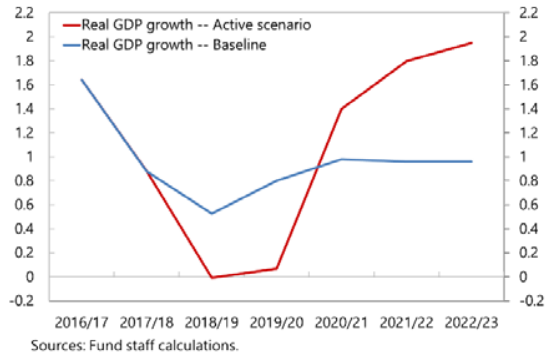
17. The reform strategy would be focused on reducing expenditures while maintaining the tax effort. Expenditure measures under the proposed adjustment would include: (i) lower transfers to SOEs, including a reversal of recent increases and further cuts based on structural reforms; and (ii) other current spending cuts, including a reduction in public sector pensions and containment of the wage bill and goods and services. The strategy would aim to marginally increase revenues and broaden the tax base to accommodate a partial reversal in the NSRL over time (text chart), conditional on progress in (i) and (ii).

Baseline Vs Active Scenario

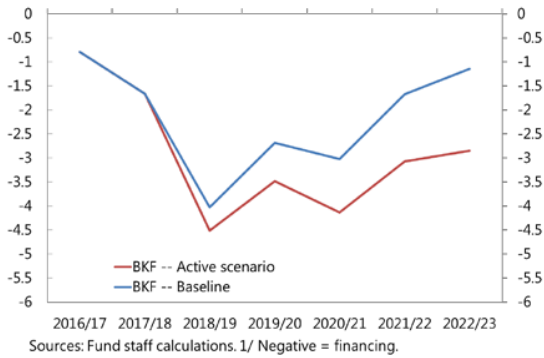
Primary Fiscal Balance
(Percent of GDP)



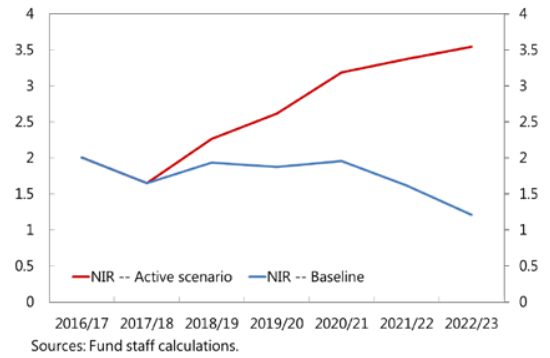
Real GDP Growth
(Percent)



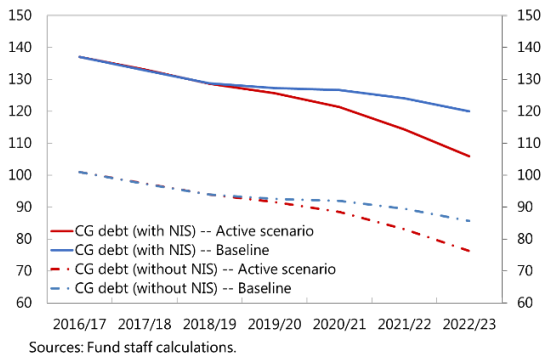
Capital and Financial Account Balance
(Percent of GDP 1/)



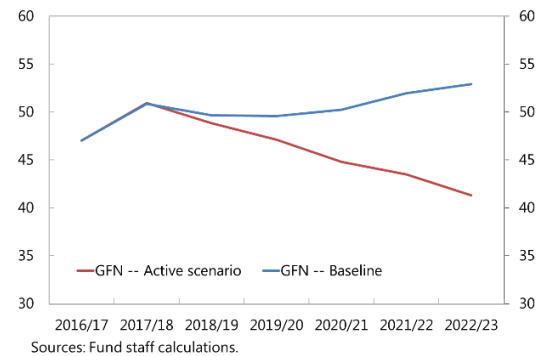
Net International Reserves
(Months of imports coverage)



Central Government Debt
(Percent of GDP)



Gross Financing Needs
(Percent of GDP)



18. The sizable fiscal adjustment would put the debt-to-GDP ratio on a more rapid downward trajectory but additional measures would be needed for a larger decline. The debt-to-GDP ratio declines to 76 percent (or 106 with NIS) by FY2022/23, while financing requirements would fall to 41 percent of GDP. Additional measures, such as further asset sales or liability management operations, could be considered for a faster reduction in the debt-to-GDP ratio to a sustainable level and address large financing requirements. The additional adjustment will initially adversely impact growth but will lead to higher growth relative to the baseline in the medium term because of greater investor confidence thereby boosting private investment (see para. 27).

19. Financing requirements remain high. Even in the active scenario, financing requirements while declining, remain high because of the large share of short-term debt (37 percent of total domestic debt). They would only significantly decline if the government's fiscal reform program increases private sector confidence leading it to increase its holdings of long-term debt. The planned liability management operation with the NIS and CBB (which together hold about 50 percent of total domestic debt), if undertaken, may significantly reduce interest costs and financing requirements. Discussion are in the early stages.

20. The focus on SOEs and public pension reforms would address a structural imbalance in the public sector. It would facilitate a rebalancing of the fiscal adjustment effort towards expenditure reduction. Transfers, especially to SOEs, are a critical weakness of Barbados' fiscal accounts. Public sector pensions, which accounted for 3.1 percent of GDP in FY2016/17, are also high relative to pension outlays in other countries in the region.

21. SOEs reforms will be complex but necessary. As noted earlier, the reform effort appears to have stalled because of the absence of clear guidance for substantive restructurings. Transfers to SOEs remain at about 7.4 percent of GDP in FY2016/17. There is an urgent need to reinvigorate reforms. The authorities plan to introduce a new Financial Management and Audit Act early in 2018. The bill aims to strengthen the governance and accountability framework for entities outside of Central Government, including SOEs (Box 2). It could facilitate an improvement in the performance of the SOEs, but only if a concerted effort is made to follow through with its implementation. Further measures aimed at cost recovery, cost reduction, and divestment will also be required, which may include a redesign of social benefits delivered through SOEs, as well as a reduction in the work force. Such reforms could have a larger adverse impact on growth than suggested by the fiscal multiplier, and will require reform of the social programs to better target protection for the most vulnerable.

22. Lower government expenditure would allow for a reform of revenues. Tax revenues are projected to reach nearly 30 percent of GDP, on the high-end for an emerging economy (See Annex IV). A widening of the tax base, by reducing exemptions, including to tourism, while making it more progressive, together with progress with fiscal consolidation would facilitate a partial reversal of the recent NSRL increases. Revenue enhancing improvements to tax policy and tax administration should also form an important part of the adjustment strategy.

Box 2. Transfers and State Owned Enterprises

Transfers have become a significant burden on the budget. They represent the single largest expenditure category—37.4 percent of current expenditures in 2016/17. Transfers to SOEs account for over 60 percent of the total transfers, followed by public sector retirement benefits, which represent another 25 percent. SOEs transfers support the provision of utilities (such as water, transportation, electricity or waste disposal), social programs, especially public health and education, and economic development (mainly to the tourism sector, small and medium enterprises, and investment promotion).

Transfers have been increasing. Total transfers grew from 9.5 percent of GDP in FY2006/07, to a peak of 13.5 percent in FY2013/14, and more recently were 11.8 percent in FY2016/17. Efforts to contain transfers to SOEs began in 2010, however, despite considerable technical assistance, there has been limited progress.

The reform effort focused on the fifteen entities that received the bulk of transfers. It centered on improvements to financial reporting, oversight, accountability, and management. Two recent IMF technical assistance missions have provided further inputs and proposals:

- The Public Financial Management mission proposed revisions to the Financial Management and Audit Act that would 1) establish clear definition for classification of public entities, including SOEs, and their related roles and responsibilities and 2) enhance monitoring and supervision of public entities by way of an internal audit, tighter and more precise reporting requirements, and sanctions for noncompliance.
- The SOEs reform mission recommended a new ownership policy for SOEs, that would allow the government to provide a clear statement of its policy and financial objectives, including which entities are eligible for government support and under what circumstance, and increase engagement between SOEs and the line ministries. In addition, it recommended a more robust engagement between government and SOEs over the budgeting process and a set of actions that would streamline costs and enhance revenues in selected entities.

Other reforms would be needed. In addition to legal, reporting and managerial and oversight reforms, the critical challenges will be to align the price of social services closer to their costs, eliminating inefficiencies, which will likely involve labor shedding, and reforming social programs. It is clear, that in the absence of a pragmatic strategy to address the high spending on social programs, it will be difficult to make significant headways in reducing transfers, as the share of transfers to support health and education alone amounts to more than 45 percent of the total in FY2016/17.

	2016/17
Current expenditures	31.6
Wages and salaries	8.1
Interest payments	7.7
Goods and services	4.0
Transfers	11.8
<i>o/w grants to public institutions</i>	7.4
<i>o/w retirement benefits</i>	3.1
<i>Sectors</i>	
Health	1.7
Education ¹	1.7
Tourism and investment promotion	1.3
Housing	0.4
Sanitation Service Authority	0.3

Sources: Authorities and Fund staff calculations.
¹ Includes University of West Indies and support of other educational programs.

Other Issues

23. Maintain the integrity of the NIS. The 15th Actuarial Review indicates that the NIS has a strong financial position. The report shows that reserves would be exhausted between 2045 and 2074. Key risks to the NIS are its large holding of government paper, which represents about 75 percent of its assets, and shortfalls in liquidity resulting from public sector arrears on contributions and rents. In recent years, the government has regularly issued new debt to repay

arrears, in place of cash. Further, contributions, which fell by 12.4 percent in 2014 owing to public sector retrenchment, have not recovered since some employers are reportedly classifying some staff as contract workers, avoiding contributions. Liquidity challenges are expected to intensify in the coming months. Staff urge the government to make its contributions in cash in a timely manner to ensure that the NIS has sufficient liquidity. Moreover, stricter enforcement may be needed to ensure that employers do not evade contributions.

24. Address arrears. Staff estimate that central government arrears amount to about 5.4 percent of GDP, of which arrears to the private sector are 1.7 percent of GDP. The latter include pending payments for goods and services and VAT and other tax refunds.⁸ The bulk of the arrears (3.7 percent of GDP) is due to the public sector—authorized transfers to SOEs and statutory bodies, and payments to NIS, mainly payroll contributions and rents.

	Mar-15	Mar-16	Mar-17	Sep-17
Private Sector	0.1	0.8	1.2	1.7
Tax refunds	0.1	0.8	1.0	1.3
Goods and Services	0.1	0.2	0.2	0.4
Public Sector	2.8	3.2	2.7	3.7
Transfers	1.2	1.6	2.1	2.3
NIS	1.4	1.4	0.6	1.3
Total	2.9	4.0	3.9	5.4

The government should undertake a netting out of intra-agency arrears, and agree with the private sector on a concrete repayment program, avoiding temporary arrangements. Going forward, staying current on obligations should be a priority, and it would be facilitated by a higher primary surplus, better liquidity management, and SOEs reforms.

Authorities' Views

25. The authorities generally agree with the staff views and proposed policies.

- ***They recognize that budget deficit will be larger than planned but they expect the performance to be stronger than staff estimates.*** They noted that the May 2017 budget set a very ambitious target intentionally and, hence, there is a high risk that it may not be fully realized. The revenue performance is somewhat weaker than expected because of lower imports as well as larger exemptions for the NSRL. However, some other taxes, particularly the corporate tax is doing much better, and may make up for some of the shortfall. The planned reduction in current expenditure was, in their view, on track. The increase in transfers to SOEs is based on last year's supplementary requests, of which only a small amount has been approved. The minister plans to carefully review the remaining requests, and would only approve those that are necessary to cover wages, pensions and debt service, and expects transfers to SOEs not to be higher than last year.
- ***The authorities recognize growing financing pressures and declining reserves.*** They remain committed to completing the planned privatization of the oil terminal, but the delay in finalizing the sale may be unavoidable, as it relates to legal challenges. In the meantime, they plan to strengthen implementation capacity to accelerate the drawdown of project financing in the

⁸ The outstanding tax refunds, especially those relating to VAT, may be higher as Barbados Revenue Authority's stock of refunds awaiting approval and authorization for payment is high and growing.

pipeline, about US\$280 million over the next few years. In the near term, the recently approved Inter-American Development Bank (IDB) project on the tourism sector should provide US\$30 million in external financing.

- ***The authorities agree that a higher primary balance is necessary to reduce public debt.*** However, the specific strategy and speed of adjustment would need to be carefully looked at. They indicated that a comprehensive strategy to reform SOEs has yet to be defined but emphasize that there has been some progress. Reform plans will be presented to Cabinet in December reflecting the strategy agreed to in the BSRP. SOEs reforms will also necessitate reforming social programs, which are mainly delivered by SOEs, and, hence, will need to proceed carefully as they could fundamentally change Barbados' society. Reforms will need to preserve the social fabric, since the leading industries depended on low crime and a skilled workforce. In the meantime, the authorities plan immediate steps to improve implementation. In particular:
 - the Management Accounting Unit (MAU) will be strengthened with new staff and with improved collaboration with the Ministry of Finance budget analysts responsible for the main SOEs; and
 - the new Financial Management and Audit Act will be implemented to provide the MAU with stronger oversight powers, including the ability to issue fines.
- ***Regarding increased NIS holding of government debt,*** the authorities noted that there are limited domestic investment options and external investments would reduce limited foreign reserves.

B. Economic Growth

26. While fiscal consolidation will initially lower growth, structural reform would help improve productivity and growth potential in the medium-term. Various global competitiveness reports point to common problems impeding growth including public sector inefficiencies and costly delays caused by bureaucratic hurdles. An IDB project has supported some reforms, including the electronic single window platform which was completed late last year, and should improve trade facilitation. Proposed structural reform of SOEs would improve the quality and efficiency of public services. Further reform is needed to increase speed and flexibility of business processes to significantly reducing clearance times at immigration, customs, and expedite issuance of construction permits in planning entities. There is also a need to reform legal processes and improve services at the Corporate Affairs and Intellectual Property Office (CAIPO). Labor laws should be modernized to increase labor market flexibility—including by easing labor market regulation, to improve incentives and to contribute to increasing productivity.

27. Rebuilding confidence is critical to improving growth prospects. The current uncertainty and concerns about fiscal and debt sustainability are impeding investment. The active scenario assumes an improvement in the government's credibility, improvement in credit ratings, and increases in external official and private funding, and thereby a growth dividend from reforms and

increased investment. Real growth is assumed to be about 1 percentage point higher than in the baseline after the first two years of the consolidation and structural reform.

28. The active scenario also faces high risks. It will require exceptionally high political commitment and entail challenging adjustments. Economic growth may be lower than projected due to a higher than estimated fiscal multiplier. SOE reforms are difficult to implement and there is also a risk that the projected primary surplus will not be sustained. Finally, the recovery in confidence and private inflows may not materialize if the government's reform effort is not perceived to be credible, or sufficient to restore fiscal and debt sustainability.

Authorities' Views

29. The authorities are in general agreement with staff views. They indicate that the economy is slowing down primarily to external factors and the ongoing fiscal consolidation. However, it is too early to assess the impact of the May budget since some of the measures were only implemented in August and September 2017. Going forward, the BSRP includes a strategy to reform business facilitation processes to promote growth. They thought that staff growth projections in the active scenario were too conservative. In their view, the fiscal multiplier is smaller, and growth would be higher, closer to 2.5 percent, as increased confidence in the economic strategy would lead to a rebound.

C. Financial and External Stability

30. Eliminating new CBB funding of the government is critical to preserving the exchange rate peg. Two years of large direct CBB financing of the government has contributed to the decline in international reserves, and have exposed its balance sheet to considerable credit risk. Recognizing these risks, the CBB has significantly raised the securities reserve requirement for banks, but thereby increasing commercial banks' exposure to sovereign debt. Such financial repression may adversely impact the business climate. Adhering to fiscal targets, and eliminating reliance on the CBB financing, is necessary to support the peg. Progress towards fiscal sustainability will allow the CBB to roll back these reserve requirements.

31. Close supervision of the banks and non-bank financial institutions should continue. Continued close supervision of banks and credit unions is needed to ensure progress in further reducing NPLs and raising provisioning to satisfactory levels. Credit unions loans, which account for three-quarters of credit unions assets, continue to register robust growth. However, credit unions face challenges, with low returns on assets, liquidity below prudential standards, low provisioning, and relatively elevated but declining NPLs. In line with FSAP recommendation, the government should extent the financial safety to credit unions and quickly resolve two small weak institutions. The insurance sector, with assets of 36 percent of GDP, has been stagnating, and profitability has been mixed. The Financial Service Commission, which supervises the insurance sector, needs to be better resourced, and regulations to permit consolidated, cross boarder supervisions and surveillance—particularly of regional systemically important institutions—need to be introduced. Moreover, exposure to sovereign risk remains a major concern. In line with 2014 FSAP recommendations, amendments to the Central Bank Law have been drafted to provide greater

central bank independence. It would be important for parliament to adopt this revised central bank legislation in 2018.

32. Uncertainty over the long-term prospects of the economically important IBFS sector calls for enhanced monitoring and repositioning to secure its viability. The sector, a vital source of foreign exchange, employment and tax revenue, has been slow to recover from the adverse impact of the global financial crisis and changes in Canadian tax legislation. Global banks' withdrawal of correspondent banking relationships (CBRs) has also had a negative—albeit relatively moderate—impact on the sector. Available data suggest that recent changes in the UK corporate taxation led to a modest recovery in number of newly-licensed entities in 2016. Information on the sector is limited, hampering an accurate assessment of the sector's activities to inform policy. The sector would benefit from enhanced monitoring, transparency, communication, and the authorities should move quickly to address deficiencies identified in the recent AML/CFT Mutual Evaluation Report, to improve Barbados position as an attractive and sustainable destination for international business.

33. Consistent implementation of an ambitious fiscal consolidation program is needed to strengthen the financial account and rebuild international reserves. Long-standing capital flow management measures (CFMs) provide some protection against a disorderly adjustment in the face of large deficits and rapid increase in public debt. The recent introduction of the FX fee (FEF) of 2 percent on all FX sales was determined by staff to be a CFM under the IMF's Institutional View on capital flows, by moderately increasing cost. Staff see the FEF as a crisis measure with limited impact on reserves. Only consistent fiscal consolidation will reduce the CAD and strengthen the financial account, and thereby reserves. Thus, the FEF should be eliminated as the reserve position strengthens.

34. The external competitiveness assessment suggests that the real effective exchange rate is slightly overvalued. Barbados' overall external position is moderately weaker than the level consistent with the medium-term fundamentals and desirable policies. The EBA-lite methodology yields mixed results and staff considers the current account model to be the most informative. The current account gap is estimated at -1.4 percent, translating into a 4.2 percent REER overvaluation. Substantial fiscal adjustment, together with continued fiscal discipline and structural reform would contribute to an improvement in external competitiveness and help stabilize international reserves. The Assessing Reserve Adequacy (ARA) methodology suggest that gross reserves should be about 2.8 to 4.2 months of import, whereas the 2017Q3 level of gross reserves cover was 1.7 months of import (1.6 months on a net reserves basis) (Annex III). In the active scenario, reserves increase to about 2.5 months of imports with a strengthening of private sector inflows. Reserves could strengthen even further if multilateral banks increase lending in response to improved macroeconomic conditions.

Authorities' Views

35. Authorities remain committed to reducing reliance on CBB for new financing of the government to preserve the peg. They noted that the increase in banks' statutory requirements are temporary measures while the government implements its fiscal consolidation strategy. They noted that these reserve requirements were increased to even higher levels in the 1990s when the economy

was undergoing a difficult fiscal adjustment, but were subsequently reduced following the economic recovery. They noted the risk associated with the declining reserves and are exploring various options to fortify reserves. They are following up with the implementation of FSAP recommendations, and have drafted legislative amendments to increase CBB independence and are awaiting the Chief Parliamentary Counsel's confirmation of the same.

D. Other Issues

36. While there has been progress with improving data, inadequacies continue to hamper understanding of macroeconomic developments. The data shortcomings increase the difficulties of establishing policy priorities and monitoring outcomes. Fund TA is supporting the revision of current and constant price-based GDP data, addressing the large inconsistencies between the two series, while the Barbados Statistical Service is close to publishing the new real GDP series (Box 3). Maintaining appropriate staffing and adequate resources, especially for benchmarking exercises, are critical to improving data quality. Follow up on agreements on timely data sharing among agencies is also essential to continuing to produce reliable data. Additional TA in this and other areas may also be needed.

STAFF APPRAISAL

37. After a prolonged period of decline and stagnation following the global financial crisis there was relatively robust GDP growth in 2016. This reflects the recovery in the tourism sector and pickup in domestic investment. However, notwithstanding a continued strong performance of tourism, the economy is slowing in response to the ongoing fiscal consolidation and political uncertainty, while headline inflation is picking up. Staff estimate real growth will slow to 0.9 percent in 2017 from 1.6 percent in 2016, with inflation rising to 5.5 percent by end-2017, from 3.6 percent at end-2016, reflecting increase in taxes this year. At the same time, notwithstanding a decline in the current account deficit by half since 2014, the reserve position continues to deteriorate reflecting weak official and private capital inflows.

38. There is progress with fiscal consolidation but the government's financing requirements and debt remain high. The fiscal deficit declined from 8.9 to 5.5 percent of GDP between FY2015/16 – 16/17, as a result of improved revenue performance, including the introduction of the NSRL and one-off factors, as well as efforts to contain current spending, including wages and salaries and transfers. Notwithstanding this, central government debt further increased to 101 percent of GDP (or 137 percent including NIS). Concerns about the high debt, as well as successive credit rating downgrades, have led to a decline in the private sector willingness to hold government securities and led to increased reliance of CBB funding.

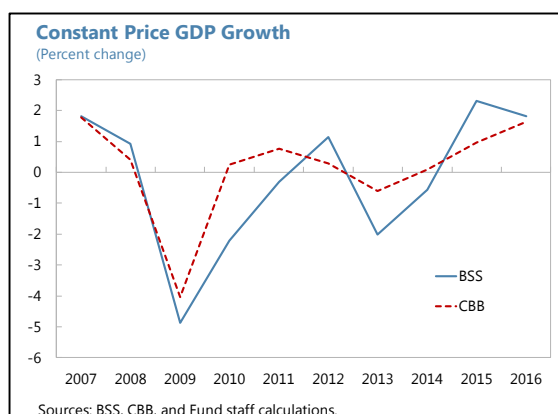
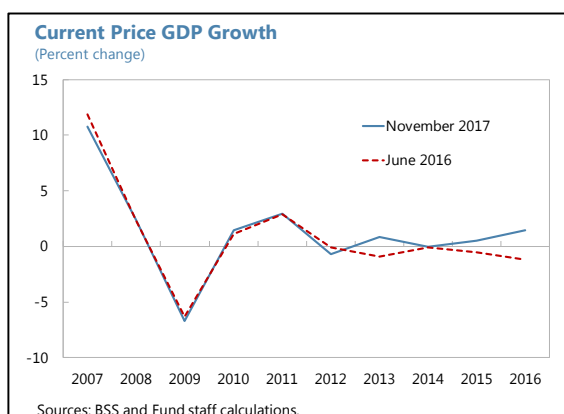
39. The government introduced an ambitious budget in May 2017 aiming to significantly reduce the deficit, eliminate need for new funding, and increase international reserves. The budget measures primarily relied on a large increase in the NSRL as well as other taxes and fees, and additional privatization, to eliminate the need for CBB funding. However, weaker than expected revenue performance as a result of narrowing of the NSRL base, lower imports, and lower than

planned progress in reducing transfers, suggest that the government will miss its target. Staff estimate the fiscal deficit in FY2017/18 to be 4.1 percent, excluding privatization proceeds, and a primary surplus of 3.7 percent of GDP. Further, in the absence of completing the planned privatizations, reserves will continue to decline and further endanger the peg.

Box 3. Strengthening National Accounts

There has been progress in strengthening Barbados’ national accounts. With technical assistance from IMF (mainly from Caribbean Regional Technical Assistance Centre (CARTAC)), and improved collaboration between the Barbados Statistical Service (BSS), the Central Bank of Barbados (CBB), the Ministry of Finance and Economic Affairs (MOFEA), and the Barbados Revenue Authority (BRA), there has been substantial progress in improving the national accounts, including the real GDP series.

The new national accounts figures update the BSS current price series and introduce two new products. These are: a constant price GDP series and a quarterly GDP series for both current and constant prices. The revisions include improved consistency with the 2008 System of National Accounts standards and adopt the International Standard Industrial Classification Revision 4 (ISIC Rev.4) presentation. The constant price GDP series was updated and compiled with a new base year, reflecting the 2010 bench-marking exercise.



Earlier national accounts data showed large differences from macroeconomic indicators and Central Bank estimates. A thorough review of the methodologies and source data along with diligent work by the BSS and CARTAC led to revisions that improved the quality of the statistics being produced. The revised GDP series is more consistent with macroeconomic indicators and CBB estimates. For 2016, constant price growth rates differ by only 0.2 percentage points.

Going forward, both the nominal and real GDP will be regularly produced by BSS, and will in the near term begin to include quarterly figures. The CBB will produce flash quarterly estimates and forecast for monetary policy purposes. It is important to note that GDP figures are subject to revision and improvements to methodology and access to data will be an ongoing process.

40. Additional effort is needed to balance the budget. Given the urgency in addressing the high debt, funding and BOP risks, and the limited policy options, the fiscal adjustment must continue. Staff advise reaching a primary surplus of 7.5 percent of GDP by FY2020/21, corresponding to an overall budget close to balance. The proposed adjustment would be tilted towards expenditure, primarily supported by SOE reforms, as well as reductions in other current expenditures. Revenue efforts could be improved by broadening the tax base, including by reducing exemptions,

thereby allowing, over time, a partial reversal in the increase of the NSRL. Additional measures, such as further asset sales or liability management operations, could be considered for a faster reduction in the debt-to-GDP ratio to a sustainable level.

41. Structural reforms underpinning the fiscal adjustment need to be accelerated. Reform of SOEs appears to have stalled, reflecting lack of clear direction and weaknesses in the oversight. There is an urgent need to reinvigorate SOE reforms by defining clear objectives, passing the Public Financial Management and Audit Act, and strengthening the MAU and the POC. Reconsideration of the size and form of SOE-supported social programs should yield cost reductions and direct recovery from beneficiaries will also be critical. Divestment as well as a reduction in the work force may also be needed.

42. Progress with fiscal consolidation would be critical to facilitate the elimination of arrears. Continued accumulation of arrears hinders both private and public sector, and tax arrears may result in lower tax compliance. The government should prioritize staying current to the private sector, and especially tax refunds. It also becoming critical that payments to the NIS be settled in cash rather than government securities so as not to undermine its liquidity position.

43. Efforts to support private sector developments need to be accelerated. Barbados is losing ground with regard to several business and competitiveness rankings. Reforms to improve public services, and reduce inefficiencies and delays, should be prioritized. There is also a need to reform legal processes and improve services at the CAIPO. Labor laws should be updated to increase labor market flexibility, improve incentives, and contribute to increasing productivity.

44. While the CBB has reduced its funding of the government, banks have been required to increase their support. The increase in statutory requirements for banks to hold government assets should be eased with progress with fiscal consolidation efforts and reductions in the financing requirements. The CBB should continue to refrain from providing new funding to the government. Direct CBB financing of the government represents a significant macro-financial risk and is incompatible with a fixed exchange rate.

45. The banking sector remains well capitalized and NPLs continue to decline. However, low profitability and financial repression pose a risk, and continued vigilance is important. Further efforts are needed to address FSAP update, in particular with regard to credit unions, and strengthen the AML/CFT regime.

46. Low international reserves pose a critical vulnerability. Indicators point to a modest overvaluation of the exchange rate, and reserves have continued to decline in the face of low official and private inflows. These declines reflect concerns about fiscal and debt sustainability. While the authorities refocus their fiscal consolidation efforts, to rebuild confidence, it's also critical that they take other steps to bolster reserves, including completing planned privatizations and improving capacity to drawdown project financing already in the pipeline.

47. Progress had been made in improving data quality but more is needed. The production of national account series has improved considerably. Appropriate staffing and adequate resources

BARBADOS

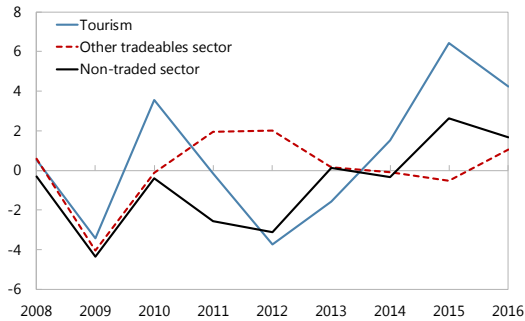
are critical to further improve data quality at the BSS. Following up on agreements on timely data sharing among agencies is also essential. The BSS should proceed to publish real and nominal annual and quarterly GDP series while the CBB should publish flash estimates in its press releases.

48. It is recommended that the next Article IV consultation with Barbados be held on the standard 12-month cycle.

Figure 1. Barbados: Real Sector Developments

For the first time since the crisis, Barbados has multi-year sustained growth, driven by tourism....

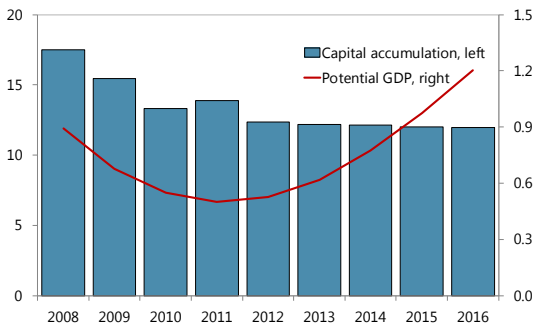
Real GDP Comparison
(Percent change)



Sources: Central Bank of Barbados and Fund staff calculations.

Potential growth fell alongside capital accumulation, but has recently steadily risen.

Capital Accumulation and Potential GDP
(Percent of GDP, left; Percent change, right)



Sources: Central Bank of Barbados, Invest Barbados and Fund staff calculations.

Non-tourism related industries remain relatively flat...

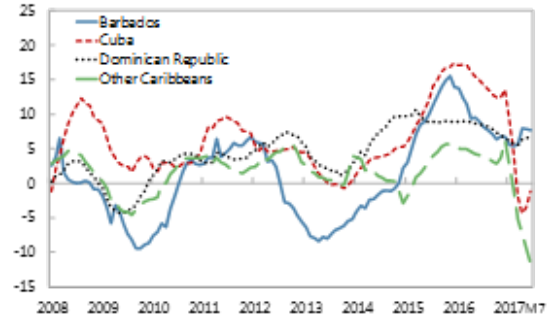
Construction and Business Sectors
(Percent of GDP)



Sources: Central Bank of Barbados, Invest Barbados and Fund staff calculations.

...as tourism arrivals are among the highest in the region.

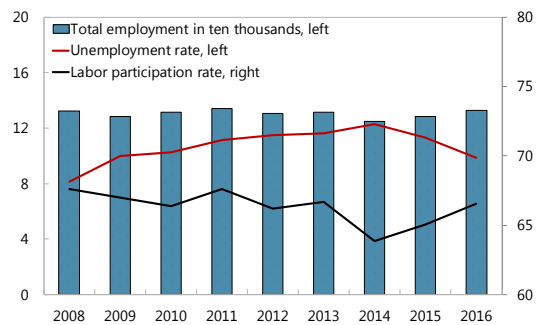
Tourist Arrivals
(%Y percent change, 12-month moving average)



Sources: Caribbean Tourism Organization and Fund staff calculations.

Unemployment fell and labor participation increased in the last 2 years.

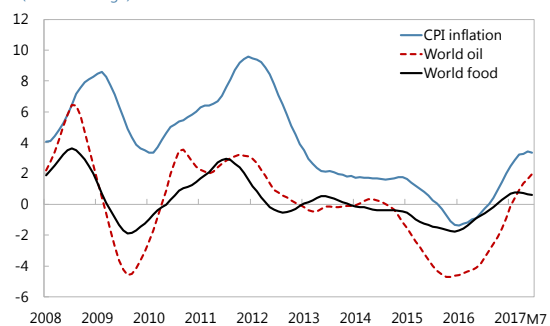
Labor Participation and Unemployment
(Ten thousands; Percent)



Sources: Central Bank of Barbados and Fund staff calculations.

...and inflation, having fallen, is beginning to pick up due to food prices and tax increases.

Consumer, Oil and Food Prices
(Percent change)

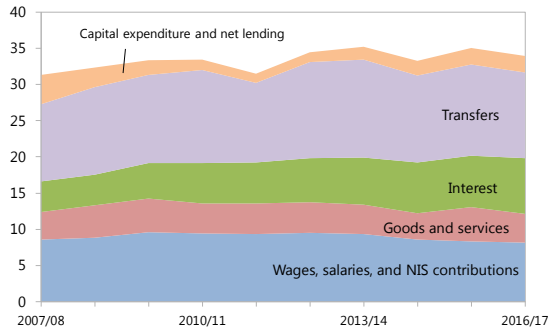


Sources: Central Bank of Barbados and Fund staff calculations.

Figure 2. Barbados: Fiscal Sector Developments

Spending on transfers and interest cost have significantly grown, but total spending has been reduced in recent years...

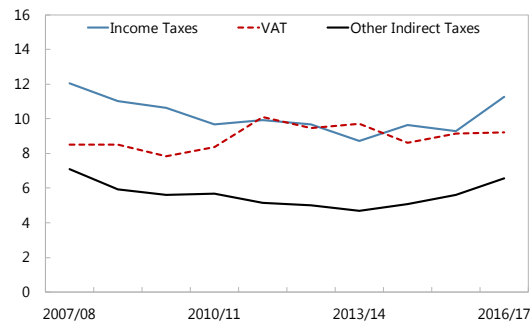
General Government Expenditures
(Percent of GDP)



Sources: Central Bank of Barbados and Fund staff calculations.

All revenue categories have improved but VAT has remained relatively flat after growing following the rate increase.

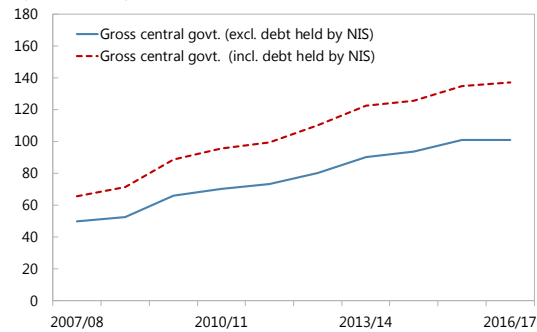
Tax Revenue Composition
(Percent of GDP)



Sources: Central Bank of Barbados and Fund staff calculations.

Central Government debt has risen sharply...

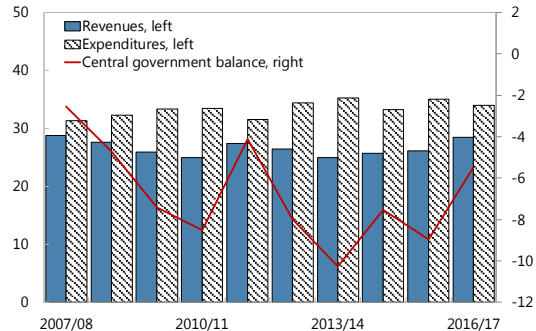
Central Government Debt
(Percent of GDP)



Sources: Central Bank of Barbados and Fund staff calculations.

...while revenues are recovering and the fiscal deficit is declining.

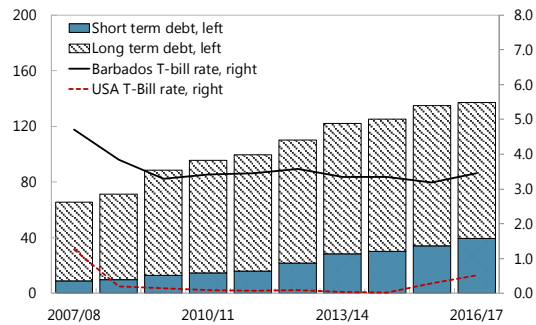
Central Government Balance
(Percent of GDP)



Sources: Central Bank of Barbados and Fund staff calculations.

Large financing requirements have been increasingly met with short-term debt instruments.

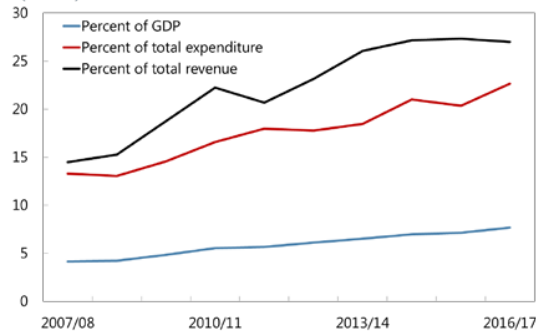
Government Financing
(Percent of GDP, left; Percent, right)



Sources: Central Bank of Barbados and Fund staff calculations.

... along with the debt service cost.

Debt Service Cost
(Percent)



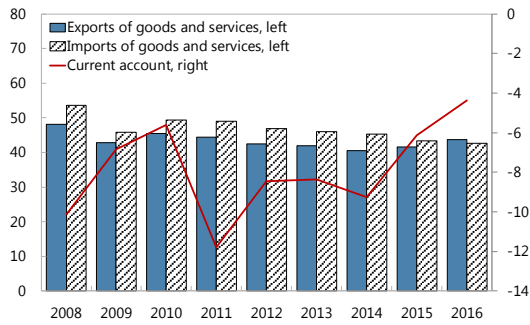
Sources: Central Bank of Barbados and Fund staff calculations.

Figure 3. Barbados: External Sector Developments

The current account deficit has narrowed, driven by lower imports and higher exports of goods and services.

Trade

(Percent of GDP)

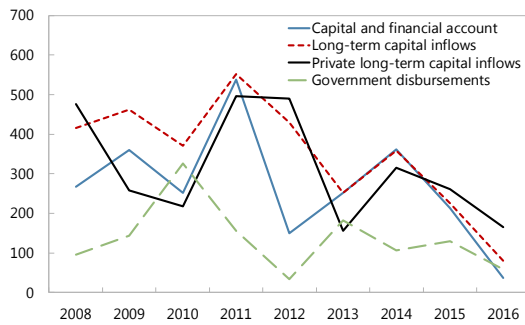


Sources: Central Bank of Barbados and Fund staff calculations.

Capital inflows are falling...

Capital and Financial Account

(Millions USD)

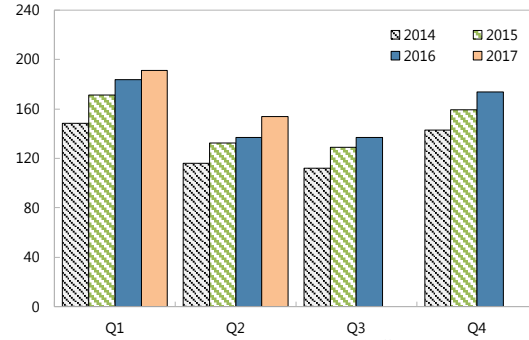


Sources: Central Bank of Barbados and Fund staff calculations.

Tourist arrivals continue to grow robustly.

Tourist Arrivals

(Thousands)

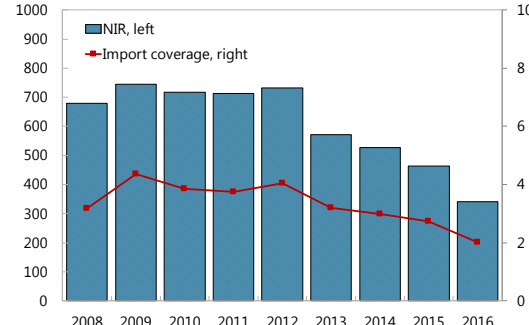


Sources: Caribbean Tourism Organization and Fund staff calculations.

...contributing to a further decline in reserves.

Net International Reserves

(Millions USD, left; Number of months, right)



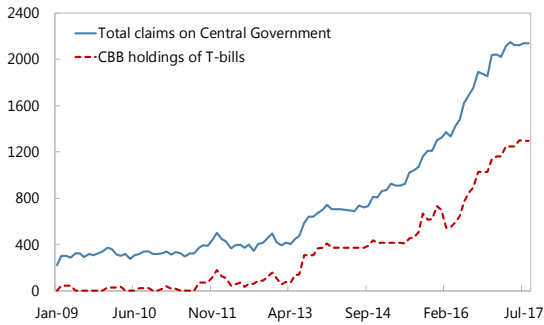
Sources: Central Bank of Barbados and Fund staff calculations.

Figure 4. Barbados: Monetary Sector Developments

CBB's claims on the Government have rapidly risen ...

Central Bank's Claims

(Millions BBD)

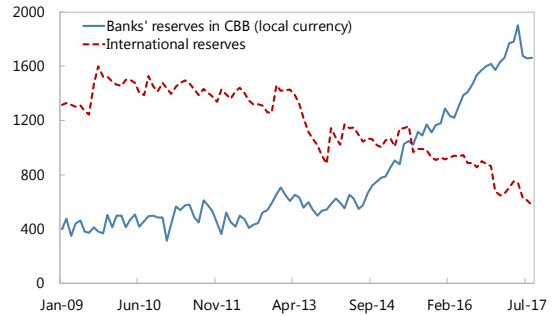


Sources: Central Bank of Barbados and Fund staff calculations.

...while commercial banks reserves at the CBB also have grown quickly.

Reserves

(Millions BBD)

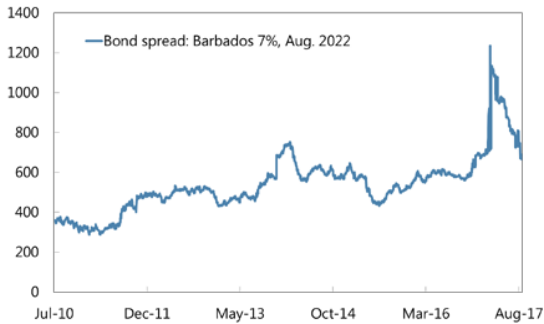


Sources: Central Bank of Barbados and Fund staff calculations.

The country risk premium peaked early 2017 but is falling...

Bond Spreads (Barbados over U.S. 10-year bonds)

(Basis points)

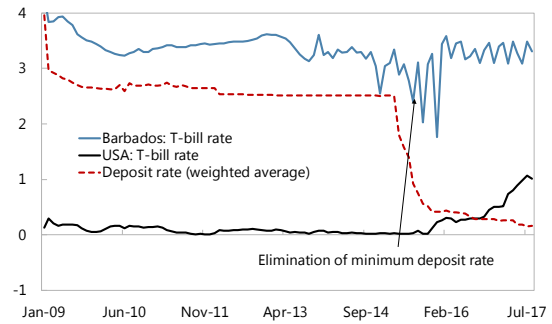


Sources: Central Bank of Barbados, Bloomberg and Fund staff calculations.

The domestic policy rate (3-month T-bill) averaged 3.3 percent in 2016, slightly higher than in 2015.

Interest Rates

(Percent)

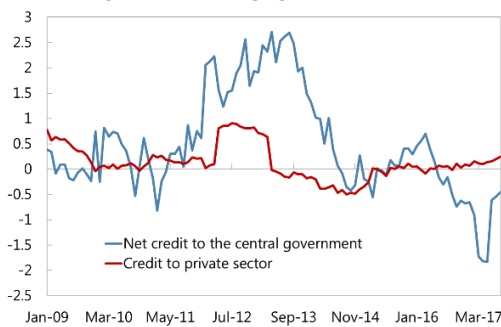


Sources: Central Bank of Barbados and Fund staff calculations.

Private sector credit growth remains weak...

Private Sector Credit

(Percent change of 12-month moving avg.)

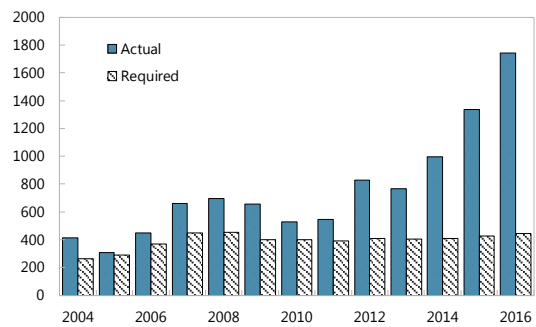


Sources: Central Bank of Barbados and Fund staff calculations.

... with excess liquidity parked at the Central Bank.

Commercial Banks: Reserves

(Millions BBD)

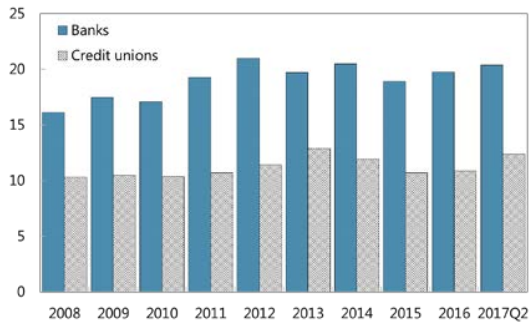


Sources: Central Bank of Barbados and Fund staff calculations.

Figure 5. Barbados: Financial Sector Developments

Capital adequacy ratios remains high and stable...

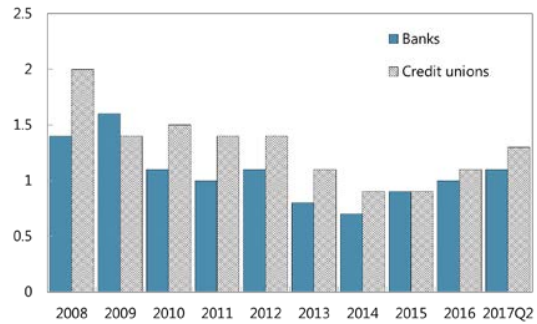
Capital Adequacy Ratio
(Percent of risk-weighted assets)



Sources: Central Bank of Barbados and Fund staff calculations.

... while profitability, albeit improved slightly, remains low.

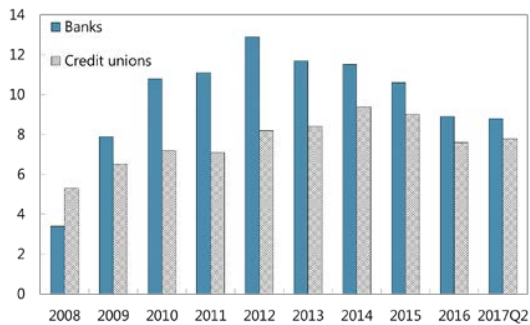
Return on Assets
(Percent of total assets)



Sources: Central Bank of Barbados and Fund staff calculations.

Banks' NPLs continues to slowly come down.

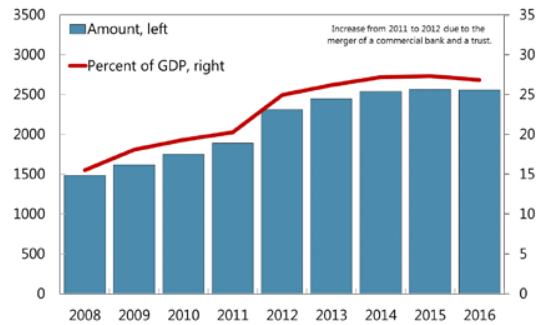
Nonperforming Loan Ratio
(Percent of total loans)



Sources: Central Bank of Barbados and Fund staff calculations.

Mortgage growth was flat in 2016...

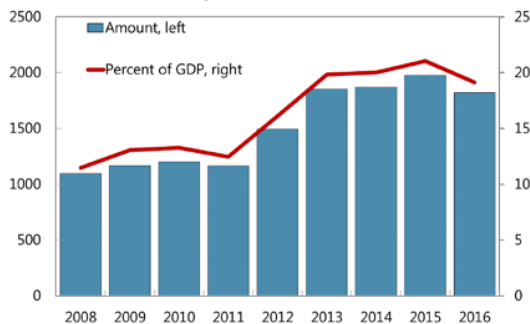
Commercial Banks' Mortgage Exposure
(Millions BBD, left; Percent, right)



Sources: Central Bank of Barbados and Fund staff calculations.

... while the banks' exposure to the Government fell in 2016.

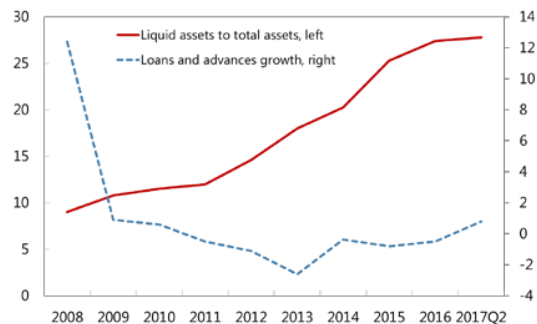
Commercial Banks' Sovereign Exposure
(Millions BBD, left; Percent, right)



Sources: Central Bank of Barbados and Fund staff calculations.

With weak loan growth, banks' liquid assets to total assets have increased.

Commercial Banks' Loans and Liquid Assets
(Percent)



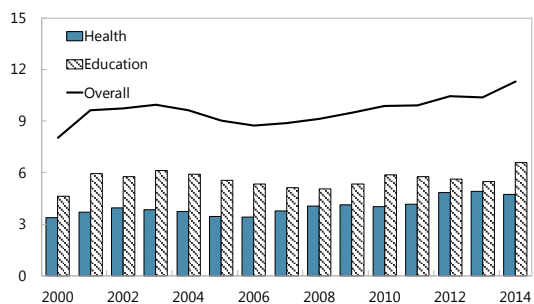
Sources: Central Bank of Barbados and Fund staff calculations.

Figure 6. Barbados: Social Development Indicators

Social spending is steadily rising...

Public Social Spending

(Percent of GDP)

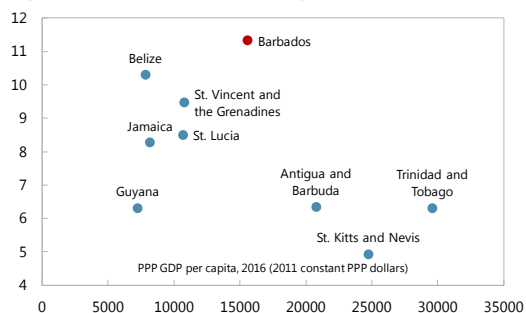


Sources: World Development Indicators as of Dec. 2017, and IMF staff calculations.

...and it is among the highest when compared to neighboring countries.

Social Spending: Selected Caribbean Countries

(PPP dollars, X-axis; Percent of GDP, Y-axis)

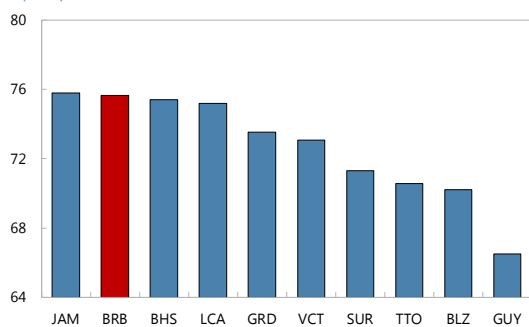


Sources: IMF World Economic Outlook, World Development Indicators, and Fund staff calculations.

High social spending has resulted in high life expectancy...

Life Expectancy, 2015

(Years)

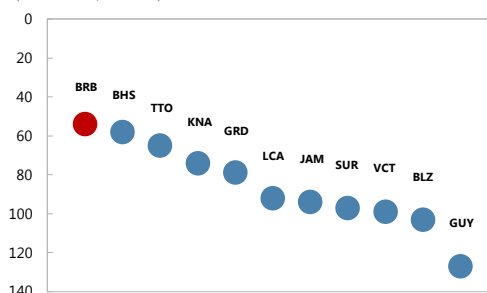


Sources: World Development Indicators and IMF staff calculations.

...and higher development outcomes relative to regional peers.

Human Development Index, 2015

(Rank of 188, 1 is best)



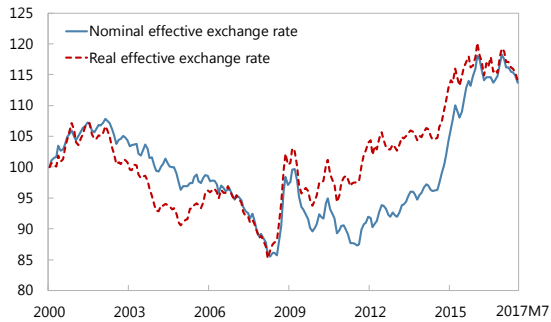
Sources: UNDP Human Development Index 2014 and IMF staff calculations.

Figure 7. Barbados: Competitiveness Indicators

Real effective exchange rate started depreciating in 2017.

Effective Exchange Rates

(Index: January 2000=100)

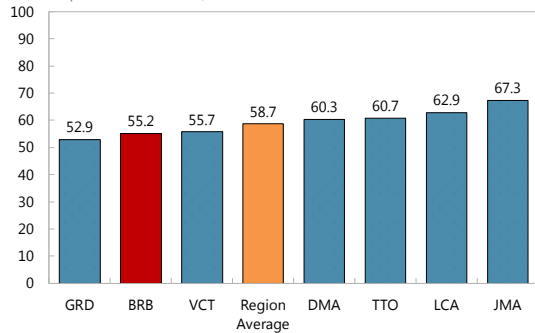


Sources: IMF Information Notice Service and Fund staff calculations.

Barbados scores below regional average on the "Doing Business Indicators".

Doing Business: Distance to Frontier, 2017

(100 represents the frontier)

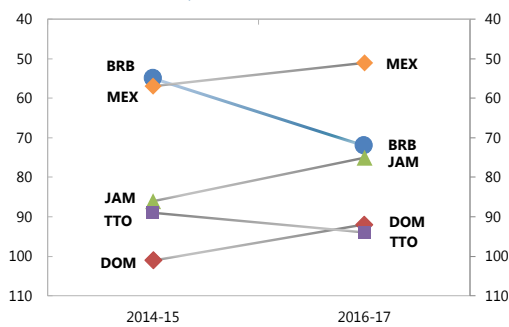


Sources: World Bank Doing Business Database and Fund staff calculations.

...as has its ranking in the Global Competitiveness Index.

Global Competitiveness Index Ranking

(Rank out of 148, 1 is the top)



Sources: World Economic Forum and Fund staff calculations.

Tourism market share and stayover arrivals are on the rise.

Tourism Market Share

(Share of 13 selected Caribbean countries)

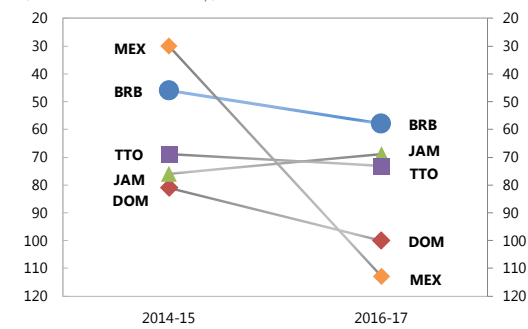


Sources: Caribbean Tourism Organization, IMF BOP Statistics, and Fund staff calculations.

While still strong relative to its peers, Barbados ranking in Tourism Competitiveness Index has deteriorated...

Tourism Competitiveness Index Ranking

(Rank out of 148, 1 is the top)

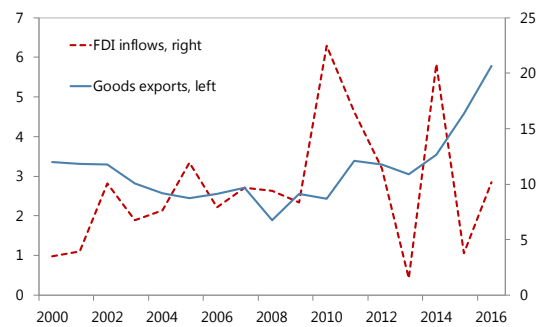


Sources: World Economic Forum and Fund staff calculations.

While export market share is increasing, capital flows remain volatile.

Exports and FDI Market Share

(Percent of 11 selected Caribbean countries)



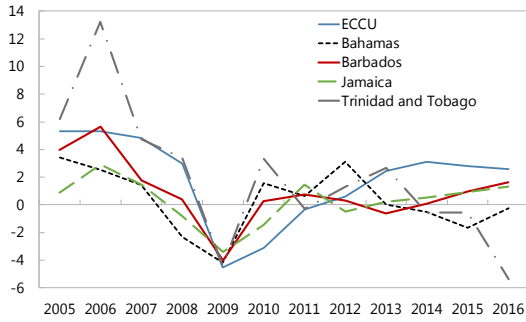
Sources: IMF World Economic Outlook, UNCTAD, and Fund staff calculations.

Figure 8. Barbados: Economic Performance in a Regional Context

Relative to its peers, Barbados' growth has picked up...

Real GDP Growth

(Percent change)

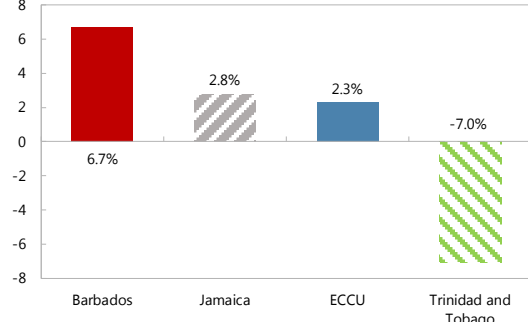


Sources: IMF World Economic Outlook and Fund staff calculations.

...reflecting robust growth in tourist arrivals.

Stayover Tourist Arrivals 2016

(y/y percent change)

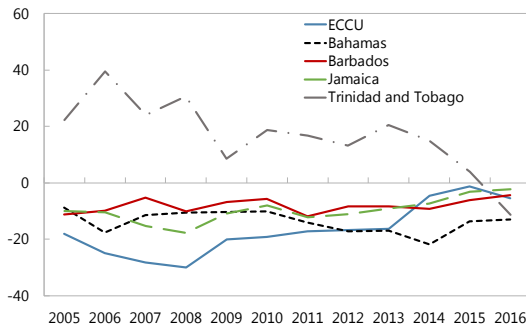


Sources: IMF World Economic Outlook and Fund staff calculations.

The current account is steadily closing...

Current Account Balance

(Percent of GDP)

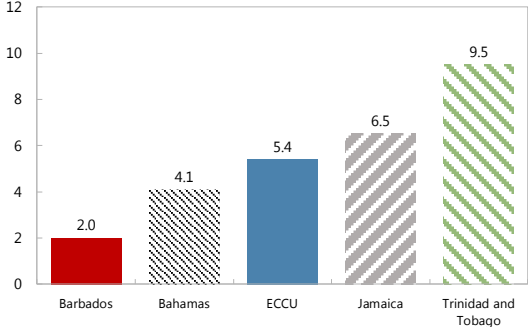


Sources: IMF World Economic Outlook and Fund staff calculations.

...however, reserves are much weaker than that of its peers.

Reserves in Months of Imports, 2016

(Months)

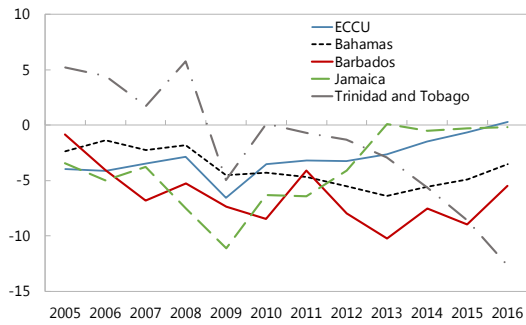


Sources: IMF World Economic Outlook and Fund staff calculations.

Barbados is lagging in its fiscal consolidation efforts...

Central Government Fiscal Balance

(Percent of GDP)

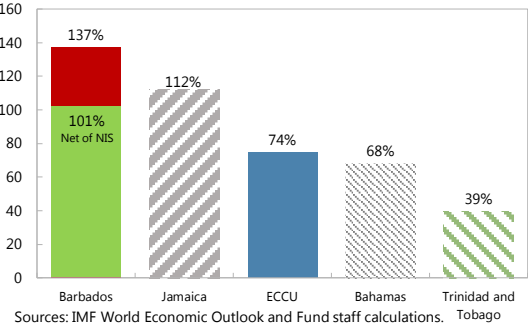


Sources: IMF World Economic Outlook and Fund staff calculations.

...while its debt is the highest in the region.

General Government Gross Debt-GDP Ratio, 2016

(Percent)



Sources: IMF World Economic Outlook and Fund staff calculations. Tobago Note: Jamaica's debt is the consolidated central government and public bodies' debt, excluding debt to the IMF held by the BoI, consistent with the Fiscal Responsibility Law.

Table 1. Barbados: Selected Economic and Social Demographic Indicators, 2014–18

I. Social and Demographic Indicators (most recent year)					
Population (2016 est., thousand)	280.4	Adult literacy rate	99.7		
Per capita GDP (2016 est., US\$ thousand)	17.0	Poverty rate (individual, 2010)	19.3		
Life expectancy at birth in years (2013)	75.3	Gini coefficient (2010)	47.0		
Rank in UNDP Development Index (2014)	57	Unemployment rate (2016 est.)	9.9		
Main products, services and exports: tourism, financial services, rum, sugar, and chemicals.					
II. Economic Indicators					
	2014	2015	Est. 2016	Projection	
				2017	2018
(Annual percentage change)					
Output, prices, and employment					
Real GDP	0.1	1.0	1.6	0.9	0.5
CPI inflation (average)	1.8	-1.1	1.5	4.5	5.1
CPI inflation (end of period)	2.4	-2.5	3.8	7.4	3.0
External sector					
Exports of goods and services	-3.6	3.2	6.5	-0.3	2.5
Imports of goods and services	-1.5	-3.9	0.2	-1.7	2.9
Real effective exchange rate (average)	2.1	8.0	0.9	...	...
Money and credit					
Net domestic assets	3.1	3.0	7.1	6.2	4.6
<i>Of which:</i> Private sector credit	-4.6	0.5	1.1	3.6	4.4
Broad money	2.1	3.7	3.6	4.3	5.6
(In percent of GDP, unless otherwise indicated)					
Public finances (fiscal year) 1/					
Central government					
Revenue and grants	25.7	26.1	28.5	29.1	29.8
Expenditure	33.3	35.0	34.0	33.1	32.8
Fiscal Balance	-7.5	-8.9	-5.5	-4.1	-2.9
Interest Expenditure	7.0	7.1	7.7	7.7	7.3
Primary Balance	-0.5	-1.8	2.2	3.7	4.4
Public Debt (fiscal year) 1/					
Central government gross debt (excludes NIS holdings)					
External	31.9	31.7	29.5	26.8	25.0
Domestic	61.5	69.3	71.4	70.4	68.9
Central government gross debt (includes NIS holdings)	125.4	134.7	137.0	132.8	128.7
Balance of payments					
Current account	-9.3	-6.1	-4.4	-3.7	-3.0
Capital and financial account	7.8	4.5	0.8	1.7	4.0
<i>Of which:</i>					
Official capital	0.9	-0.8	-1.8	-1.4	0.2
Private capital	6.9	5.5	2.7	2.0	2.8
<i>Of which:</i> Long-term flows	6.8	5.6	3.5	2.8	2.8
Overall balance	-1.0	-1.3	-2.6	-1.3	1.1
Memorandum items:					
Exchange rate (BDS\$/US\$)	2.0	2.0	2.0	...	...
Net international reserves (US\$ millions)	526.0	463.0	340.5	275.3	331.7
In months of imports	3.0	2.7	2.0	1.7	1.9
Nominal GDP (BDS\$ millions)	9,343	9,390	9,528	10,045	10,609

Sources: Barbados authorities; UNDP Human Development Report; Barbados Country Assessment of Living Conditions 2010 (December 2012); and Fund staff estimates and projections.

1/ Fiscal year is from April to March.

Table 2a. Barbados: Central Government Operations, 2014–23^{1/}

(In millions of Barbados dollars)

	Est.			Projection					
	2014/15	2015/16	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22	2022/23
Total revenue	2,407	2,458	2,749	2,962	3,196	3,315	3,439	3,567	3,700
Current revenue	2,350	2,440	2,740	2,959	3,185	3,304	3,428	3,555	3,687
Tax revenue	2,183	2,266	2,612	2,809	3,008	3,121	3,237	3,358	3,482
Income and profits	569	612	737	777	835	867	900	933	968
Taxes on property	164	133	135	141	148	153	159	165	171
VAT	806	861	890	950	1,002	1,039	1,078	1,118	1,160
Social levy	0	0	29	143	181	188	195	202	210
Excise	136	169	226	286	307	319	331	343	356
Import taxes	224	232	245	242	249	258	268	278	288
Other taxes	284	260	350	272	285	296	307	319	330
Nontax revenue	167	174	127	151	177	183	190	197	205
Capital revenue and grants	58	18	9	3	11	11	12	12	12
Total expenditure	3,112	3,302	3,279	3,376	3,510	3,670	3,839	3,976	4,076
Current expenditure	2,919	3,085	3,054	3,158	3,275	3,425	3,585	3,713	3,803
Wages, salaries and SSC	804	787	784	791	832	862	895	928	962
Goods and services	342	441	385	392	412	427	443	460	477
Interest	654	673	743	786	781	839	903	931	917
Transfers	1,120	1,184	1,142	1,189	1,250	1,297	1,345	1,395	1,447
o/w Subsidies	49	61	48	52	54	56	59	61	63
o/w Grants to public institutions	678	730	714	765	804	834	865	897	931
o/w Retirement benefits	286	314	299	310	325	337	350	363	376
Capital expenditure and net lending	194	216	225	218	236	244	253	263	273
CG Fiscal balance	-705	-843	-530	-414	-315	-354	-400	-409	-376
CG Primary balance	-51	-171	212	372	467	485	503	522	541
Financing	705	843	530	414	315	354	400	409	376
Foreign financing	10	26	-162	2	28	-25	44	-193	-339
Disbursement	128	303	57	148	153	155	144	209	214
Amortization	-119	-278	-219	-286	-225	-180	-100	-402	-553
Privatization	0	0	0	140	100	0	0	0	0
Domestic financing (net)	695	818	692	412	287	379	356	601	715
Central bank	341	423	792	97	0	0	0	0	0
Commercial banks	-142	182	-439	415	97	151	134	281	348
National Insurance Scheme	49	71	180	0	62	97	86	181	223
Private non-bank	63	109	95	-30	127	131	135	139	144
Others/unidentified financing	385	32	64	-70	0	0	0	0	0
Memorandum items:									
CG gross debt (excl. NIS)	8,739	9,522	9,744	9,901	10,048	10,266	10,584	10,672	10,592
CG gross debt (incl. NIS)	11,728	12,692	13,230	13,526	13,779	14,116	14,569	14,793	14,840
Nominal GDP, FY (BDS\$ millions)	9,355	9,424	9,657	10,186	10,707	11,104	11,519	11,947	12,391

Sources: Ministry of Finance; and Fund staff estimates.

^{1/} Fiscal year is from April to March.

Table 2b. Barbados: Central Government Operations, 2014–23^{1/}

(In percent of GDP, unless otherwise indicated)

	Est.			Projection					
	2014/15	2015/16	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22	2022/23
Total revenue	25.7	26.1	28.5	29.1	29.8	29.9	29.9	29.9	29.9
Current revenue	25.1	25.9	28.4	29.1	29.7	29.8	29.8	29.8	29.8
Tax revenue	23.3	24.0	27.1	27.6	28.1	28.1	28.1	28.1	28.1
Income and profits	6.1	6.5	7.6	7.6	7.8	7.8	7.8	7.8	7.8
Taxes on property	1.8	1.4	1.4	1.4	1.4	1.4	1.4	1.4	1.4
VAT	8.6	9.1	9.2	9.3	9.4	9.4	9.4	9.4	9.4
Social levy	0.0	0.0	0.3	1.4	1.7	1.7	1.7	1.7	1.7
Excise	1.5	1.8	2.4	2.8	2.9	2.9	2.9	2.9	2.9
Import taxes	2.4	2.5	2.5	2.4	2.3	2.3	2.3	2.3	2.3
Other taxes	3.0	2.7	3.6	2.6	2.6	2.6	2.6	2.6	2.6
Nontax revenue	1.8	1.8	1.3	1.5	1.7	1.7	1.7	1.7	1.7
Capital revenue and grants	0.6	0.2	0.1	0.0	0.1	0.1	0.1	0.1	0.1
Total expenditure	33.3	35.0	34.0	33.1	32.8	33.0	33.3	33.3	32.9
Current expenditure	31.2	32.7	31.6	31.0	30.6	30.8	31.1	31.1	30.7
Wages, salaries and NIS contributions	8.6	8.4	8.1	7.8	7.8	7.8	7.8	7.8	7.8
Goods and services	3.7	4.7	4.0	3.8	3.8	3.8	3.8	3.8	3.8
Interest	7.0	7.1	7.7	7.7	7.3	7.6	7.8	7.8	7.4
Transfers	12.0	12.6	11.8	11.7	11.7	11.7	11.7	11.7	11.7
o/w Subsidies	0.5	0.6	0.5	0.5	0.5	0.5	0.5	0.5	0.5
o/w Grants to public institutions	7.2	7.7	7.4	7.5	7.5	7.5	7.5	7.5	7.5
o/w Retirement benefits	3.1	3.3	3.1	3.0	3.0	3.0	3.0	3.0	3.0
Capital expenditure and net lending	2.1	2.3	2.3	2.1	2.2	2.2	2.2	2.2	2.2
CG Fiscal balance	-7.5	-8.9	-5.5	-4.1	-2.9	-3.2	-3.5	-3.4	-3.0
CG Primary balance	-0.5	-1.8	2.2	3.7	4.4	4.4	4.4	4.4	4.4
Financing	7.5	8.9	5.5	4.1	2.9	3.2	3.5	3.4	3.0
Foreign financing	0.1	0.3	-1.7	0.0	0.3	-0.2	0.4	-1.6	-2.7
Disbursement	1.4	3.2	0.6	1.5	1.4	1.4	1.3	1.7	1.7
Amortization	-1.3	-2.9	-2.3	-2.8	-2.1	-1.6	-0.9	-3.4	-4.5
Privatization	0.0	0.0	0.0	1.4	0.9	0.0	0.0	0.0	0.0
Domestic financing (net)	7.4	8.7	7.2	4.0	2.7	3.4	3.1	5.0	5.8
Central bank	3.6	4.5	8.2	1.0	0.0	0.0	0.0	0.0	0.0
Commercial banks	-1.5	1.9	-4.5	4.1	0.9	1.4	1.2	2.4	2.8
National Insurance Scheme	0.5	0.8	1.9	0.0	0.6	0.9	0.7	1.5	1.8
Private non-bank	0.7	1.2	1.0	-0.3	1.2	1.2	1.2	1.2	1.2
Others/unidentified financing	4.1	0.3	0.7	-0.7	0.0	0.0	0.0	0.0	0.0
Memorandum items:									
CG gross debt (excl. NIS)	93.4	101.0	100.9	97.2	93.8	92.5	91.9	89.3	85.5
CG gross debt (incl. NIS)	125.4	134.7	137.0	132.8	128.7	127.1	126.5	123.8	119.8
Nominal GDP, FY (BDS\$ millions)	9,355	9,424	9,657	10,186	10,707	11,104	11,519	11,947	12,391

Sources: Ministry of Finance; and Fund staff estimates.

^{1/} Fiscal year (April–March). Ratios expressed relative to fiscal year GDP.

Table 3. Barbados: Central Government Debt, 2014–23 ^{1/}

	Est.			Projection					
	2014/15	2015/16	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22	2022/23
(In millions of Barbados dollars)									
Central gov't gross debt (incl. NIS holdings)	11,728	12,692	13,230	13,526	13,779	14,116	14,569	14,793	14,840
External ^{2/}	2,984	2,987	2,852	2,734	2,672	2,655	2,708	2,524	2,194
Domestic	8,744	9,705	10,379	10,792	11,107	11,461	11,861	12,270	12,646
Central gov't gross debt (excl. NIS holdings)	8,739	9,522	9,744	9,901	10,048	10,266	10,584	10,672	10,592
External ^{2/}	2,984	2,987	2,852	2,734	2,672	2,655	2,708	2,524	2,194
Domestic	5,755	6,534	6,892	7,167	7,376	7,611	7,877	8,148	8,398
(In percent of GDP)									
Central gov't gross debt (incl. NIS holdings)	125.4	134.7	137.0	132.8	128.7	127.1	126.5	123.8	119.8
External ^{2/}	31.9	31.7	29.5	26.8	25.0	23.9	23.5	21.1	17.7
Domestic	93.5	103.0	107.5	106.0	103.7	103.2	103.0	102.7	102.1
Short term	30.1	34.0	39.3	40.5	40.9	42.0	43.2	44.4	45.3
Long term	95.3	100.7	97.7	92.3	87.8	85.1	83.2	79.4	74.5
Central gov't gross debt (excl. NIS holdings)	93.4	101.0	100.9	97.2	93.8	92.5	91.9	89.3	85.5
External ^{2/}	31.9	31.7	29.5	26.8	25.0	23.9	23.5	21.1	17.7
Domestic	61.5	69.3	71.4	70.4	68.9	68.5	68.4	68.2	67.8
Memorandum items:									
National Insurance Scheme	32.0	33.6	36.1	35.6	34.8	34.7	34.6	34.5	34.3
Treasury bills	2.1	1.4	2.1	2.0	2.0	2.0	2.0	2.0	2.0
Debentures	29.9	32.3	34.0	33.6	32.9	32.7	32.6	32.5	32.3

Sources: Ministry of Finance; Central Bank of Barbados; and Fund staff estimates and projections.

^{1/} Fiscal year (April–March). Ratios expressed relative to fiscal-year GDP.

^{2/} External debt is all medium- and long-term debt.

Table 4. Barbados: Balance of Payments, 2014–22

(In millions of US\$)

	2014	2015	Est. 2016	Projection					
				2017	2018	2019	2020	2021	2022
Current account	-433	-289	-208	-184	-157	-150	-150	-152	-139
Exports	1,894	1,954	2,081	2,076	2,127	2,181	2,238	2,302	2,370
Exports of goods	792	801	835	793	809	828	847	865	884
o/w Re-exports	205	240	265	225	228	230	233	236	238
Imports	2,115	2,032	2,035	2,000	2,059	2,105	2,158	2,218	2,285
Imports of goods	1,652	1,537	1,540	1,490	1,534	1,562	1,601	1,640	1,685
o/w Oil	439	302	251	309	313	330	347	364	381
Services (net)	639	659	752	773	794	809	834	859	886
Credit	1,102	1,154	1,247	1,283	1,318	1,352	1,391	1,437	1,485
o/w Travel (credit)	887	947	1,038	1,069	1,098	1,129	1,163	1,201	1,240
Debit	462	494	495	510	524	543	557	578	600
Investment income (net)	-197	-213	-221	-226	-216	-214	-218	-224	-212
Credit	263	256	258	263	286	297	308	320	331
Debit	460	469	479	489	502	511	526	544	543
o/w Interest on public debt	79	82	82	81	79	75	74	76	61
Current transfers (net)	-14	2	-33	-34	-11	-11	-11	-12	-12
Credit	70	90	58	56	95	99	103	107	110
Debit	84	88	91	90	106	110	114	118	123
Capital and financial account	362	213	38	84	214	148	173	99	70
Long-term	358	225	80	121	214	148	173	99	70
Public sector	42	-36	-85	-72	11	-6	13	-66	-150
Private sector	316	261	166	140	148	153	159	165	220
o/w FDI flows	316	261	166	140	148	153	159	165	220
Short-term	9	-4	-38	-38	0	0	0	0	0
Public sector	0	0	0	0	0	0	0	0	0
Private sector	9	-4	-38	-38	0	0	0	0	0
Unidentified financing	0	0	0	0	0	0	0	0	0
Errors and omissions	26	13	47	35	0	0	0	0	0
Overall balance (deficit -)	-45	-63	-123	-65	56	-2	23	-53	-69
Reserve movements (- increase)	45	63	123	65	-56	2	-23	53	69
Memorandum items:									
Current account (percent of GDP)	-9.3	-6.1	-4.4	-3.7	-3.0	-2.7	-2.6	-2.6	-2.3
Current account after FDI (percent of GDP)	-2.5	-0.6	-0.9	-0.9	-0.2	0.1	0.2	0.2	1.3
Exports of G&S (annual growth rate)	-3.6	3.2	6.5	-0.3	2.5	2.5	2.6	2.9	2.9
Imports of G&S (annual growth rate)	-1.5	-3.9	0.2	-1.7	2.9	2.3	2.5	2.8	3.0
Change in commercial banks assets	-12	75	7	0	0	0	0	0	0
Net international reserves (US\$ million)	526	463	340	275	332	329	352	299	231
In months of imports	3.0	2.7	2.0	1.7	1.9	1.9	2.0	1.6	1.2

Sources: Central Bank of Barbados; and Fund staff estimates and projections.

Table 5. Barbados: Monetary Survey, 2014–22

	2014	2015	Est. 2016	2017	2018	2019	Projection 2020	2021	2022
(In millions of Barbados dollars)									
Central Bank of Barbados									
Net foreign assets	1,052	926	681	551	663	659	705	599	461
Assets	1,106	957	718	588	701	696	742	636	499
Liabilities	-54	-31	-37	-37	-37	-37	-37	-37	-37
Net domestic assets	446	1,033	1,729	2,076	2,118	2,225	2,287	2,505	2,840
<i>Of which:</i> Claims on Central government	861	1,302	2,037	2,349	2,349	2,349	2,349	2,349	2,349
Monetary base	1,498	1,959	2,410	2,627	2,781	2,884	2,992	3,103	3,302
Commercial banks									
Net foreign assets	-323	-121	-107	-107	-107	-107	-107	-107	-107
Net domestic assets	7,803	7,875	8,128	8,439	8,898	9,222	9,563	9,915	10,170
Liabilities to the nonfinancial private sector	7,480	7,754	8,021	8,332	8,790	9,115	9,456	9,808	10,062
Monetary survey									
Net foreign assets	729	805	574	444	556	552	597	491	354
Net domestic assets	7,271	7,492	8,025	8,525	8,916	9,270	9,592	10,077	10,607
Net credit to the public sector	2,178	2,790	3,176	3,530	3,731	3,894	4,057	4,326	4,683
Central government	2,003	2,753	3,331	3,637	3,814	3,951	4,090	4,334	4,665
Rest of public sector	314	224	113	113	113	113	113	113	113
NIS	-138	-187	-267	-221	-196	-171	-146	-121	-96
Credit to the private sector	5,364	5,392	5,452	5,650	5,900	6,122	6,326	6,525	6,734
Credit to rest of financial system	-554	-744	-678	-678	-678	-678	-678	-678	-678
Other items (net) 1/	282	54	75	88	93	98	102	105	109
Broad money (M2, liabilities to the private sector)	8,000	8,297	8,599	8,968	9,472	9,822	10,190	10,568	10,961
Narrow money	2,705	3,169	3,645	3,802	4,016	4,164	4,320	4,480	4,647
Currency	519	543	578	637	682	707	734	761	899
Demand deposits	2,186	2,626	3,068	3,165	3,334	3,457	3,586	3,720	3,748
Quasi-money	5,295	5,128	4,953	5,166	5,457	5,658	5,870	6,088	6,314
Time deposits	944	786	667	696	735	762	790	820	850
Saving deposits	4,351	4,342	4,286	4,471	4,722	4,896	5,079	5,268	5,464
(Changes in percent of beginning-of-period liabilities to the private sector)									
Monetary survey									
Net foreign assets	-0.7	1.0	-2.8	-1.5	1.3	0.0	0.5	-1.0	-1.3
Net domestic assets	2.8	2.8	6.4	5.8	4.4	3.7	3.3	4.8	5.0
Net credit to public sector	3.4	7.7	4.6	4.1	2.2	1.7	1.7	2.6	3.4
<i>Of which:</i> central government	2.3	9.4	7.0	3.6	2.0	1.5	1.4	2.4	3.1
Credit to private sector	-3.3	0.4	0.7	2.3	2.8	2.3	2.1	2.0	2.0
Other items (net) 1/	3.3	-2.9	0.2	0.2	0.1	0.1	0.0	0.0	0.0
(In percent change)									
Monetary survey									
Net domestic assets	3.1	3.0	7.1	6.2	4.6	4.0	3.5	5.1	5.3
<i>Of which:</i>									
Private sector credit	-4.6	0.5	1.1	3.6	4.4	3.8	3.3	3.2	3.2
Public sector credit	13.8	28.1	13.8	11.1	5.7	4.4	4.2	6.6	8.2
Broad money	2.1	3.7	3.6	4.3	5.6	3.7	3.7	3.7	3.7

Sources: Central Bank of Barbados; and Fund staff estimates and projections.

1/ Line item "net unclassified assets" in CBB Monetary Survey. CBB indicates that this line is a residual item, the nature of which is not disclosed.

Table 6. Barbados: Medium-Term Macroeconomic Framework, 2014–22

(In percent of GDP, unless otherwise indicated)

	2014	2015	Est. 2016	2017	2018	Projection			
	2014	2015	2016	2017	2018	2019	2020	2021	2022
(Annual percentage change)									
National accounts and prices									
Real GDP	0.1	1.0	1.6	0.9	0.5	0.8	1.0	1.0	1.0
Nominal GDP	0.0	0.5	1.5	5.4	5.6	3.7	3.7	3.7	3.7
CPI inflation (average)	1.8	-1.1	1.5	4.5	5.1	2.9	2.7	2.7	2.7
CPI inflation (end of period)	2.4	-2.5	3.8	7.4	3.0	2.8	2.7	2.7	2.7
External sector									
Exports of goods and services, value	-3.6	3.2	6.5	-0.3	2.5	2.5	2.6	2.9	2.9
Imports of goods and services, value	-1.5	-3.9	0.2	-1.7	2.9	2.3	2.5	2.8	3.0
Real effective exchange rate (average)	109.7	118.5	119.6	...	...	...	...	...	...
Terms of trade	2.1	13.8	2.5	-3.0	0.5	-0.4	-0.2	-0.2	-0.4
Money and credit (end of period)									
Net domestic assets	3.1	3.0	7.1	6.2	4.6	4.0	3.5	5.1	5.3
<i>Of which:</i> Private sector credit	-4.6	0.5	1.1	3.6	4.4	3.8	3.3	3.2	3.2
Broad money	2.1	3.7	3.6	4.3	5.6	3.7	3.7	3.7	3.7
Velocity (GDP relative to broad money)	1.2	1.1	1.1	1.1	1.1	1.1	1.1	1.1	1.1
(In percent of GDP, unless otherwise indicated)									
Public finances (fiscal year) 1/									
Central government									
Revenue and grants	25.7	26.1	28.5	29.1	29.8	29.9	29.9	29.9	29.9
Expenditure	33.3	35.0	34.0	33.1	32.8	33.0	33.3	33.3	32.9
Fiscal balance	-7.5	-8.9	-5.5	-4.1	-2.9	-3.2	-3.5	-3.4	-3.0
Interest Expenditure	7.0	7.1	7.7	7.7	7.3	7.6	7.8	7.8	7.4
Primary balance	-0.5	-1.8	2.2	3.7	4.4	4.4	4.4	4.4	4.4
Debt (fiscal year) 1/									
Central government gross debt (excludes NIS holdings)	93.4	101.0	100.9	97.2	93.8	92.5	91.9	89.3	85.5
External	31.9	31.7	29.5	26.8	25.0	23.9	23.5	21.1	17.7
Domestic	61.5	69.3	71.4	70.4	68.9	68.5	68.4	68.2	67.8
Central government gross debt (includes NIS holdings)	125.4	134.7	137.0	132.8	128.7	127.1	126.5	123.8	119.8
Savings and investment									
Gross domestic investment	7.2	10.8	11.9	10.5	11.1	11.3	11.3	11.3	11.5
Public	-1.3	-0.7	1.5	0.8	1.7	1.4	1.2	0.9	1.2
Private	8.5	11.5	10.5	9.6	9.4	9.9	10.1	10.4	10.3
National savings	7.2	10.8	11.9	10.5	11.1	11.3	11.3	11.3	11.5
Public	-1.3	-0.7	1.5	0.8	1.7	1.4	1.2	0.9	1.2
Private	8.5	11.5	10.5	9.6	9.4	9.9	10.1	10.4	10.3
External savings	9.3	6.1	4.4	3.7	3.0	2.7	2.6	2.6	2.3
Balance of payments									
Current account	-9.3	-6.1	-4.4	-3.7	-3.0	-2.7	-2.6	-2.6	-2.3
Capital and financial account	7.8	4.5	0.8	1.7	4.0	2.7	3.0	1.7	1.1
Official capital (net)	0.9	-0.8	-1.8	-1.4	0.2	-0.1	0.2	-1.1	-2.4
Private capital (net)	6.9	5.5	2.7	2.0	2.8	2.8	2.8	2.8	3.6
<i>Of which:</i> Long-term flows	6.8	5.6	3.5	2.8	2.8	2.8	2.8	2.8	3.6
Net errors and omissions	0.6	0.3	1.0	0.7	0.0	0.0	0.0	0.0	0.0
Overall balance	-1.0	-1.3	-2.6	-1.3	1.1	0.0	0.4	-0.9	-1.1
Memorandum items:									
Exchange rate (BDS\$/US\$)	2.0	2.0	2.0	...	...	...	...	...	...
Net international reserves (US\$ millions)	526	463	340	275	332	329	352	299	231
In months of imports	3.0	2.7	2.0	1.7	1.9	1.9	2.0	1.6	1.2
Nominal GDP (BDS\$ millions)	9,343	9,390	9,528	10,045	10,609	11,001	11,413	11,837	12,277

Sources: Barbados authorities; and Fund staff estimates and projections.

1/ Fiscal year is from April to March.

Table 7. Barbados: Financial Sector Indicators, 2011–17

(Percent)

	2011	2012	2013	2014	2015	2016	2017Q1	2017Q2
Commercial Banks								
Solvency Indicators								
Capital Adequacy Ratio (CAR)	19.3	21.0	19.7	20.5	18.9	19.8	19.7	20.4
Liquidity Indicators 1/								
Loan to deposit ratio	70.9	73.6	70.0	70.3	65.5	62.3	63.0	62.3
Demand deposits to total deposits	32.1	29.3	32.3	33.9	39.6	44	43.3	44.3
Domestic demand deposits to total domestic deposits	27.6	26.8	29.3	30.9	35.7	40.3	36.7	39.8
Liquid assets, in percent of total assets	12.0	14.6	18.0	20.3	25.3	27.4	26.3	27.8
Credit Risk Indicators								
Total assets (growth rate)	-4.7	11.5 ^{2/}	2.8	-1.3	4.0	3.7	1.2	2.8
Domestic assets (growth rate)	-6.1	6.1 ^{2/}	6.5	-0.6	3.3	2.7	1.5	3.0
Loans and advances (growth rate)	-0.5	-1.1 ^{2/}	-2.6	-0.4	-0.8	-0.5	0.1	0.8
Non-performing loans ratio	11.1	12.9	11.7	11.5	10.6	8.9	8.7	8.8
Substandard loans/Total loans	8.7	9.9	8.6	9.0	8.0	7.2	7	7.1
Doubtful loans/Total loans	1.8	2.3	2.5	2.0	1.5	1.0	1.0	1.0
Loss Loans/Total loans	0.6	0.8	0.6	0.5	1.1	0.7	0.7	0.8
Provisions to non-performing loans	32.9	33.9	44.9	47.7	55.5	63.2	65.1	64.1
Foreign Exchange Risk Indicators								
Deposits in Foreign Exchange (in percent of total deposits)	6.6	4.9	4.4	4.8	6.7	7.0	7.0	7.2
Profitability Indicators								
Return on Assets (ROA)	1.0	1.1	0.8	0.7	0.9	1.0	1.1	1.1
Credit Unions								
Solvency Indicator								
Reserves to Total Liabilities	10.7	11.4	12.9	11.9	10.7	10.9	11.0	12.4
Liquidity Indicators								
Loan to deposit ratio	97.7	96.2	92.3	92.8	90.8	89.3	87.6	86.5
Credit risk Indicators								
Total assets, annual growth rate	5.1	4.3	4.2	6.2	7.2	8.3	7.9	8.1
Loans, annual growth rate	6.5	3.2	3.7	7.3	7.2	6.9	7.9	6.7
Nonperforming loans ratio	7.1	8.2	8.4	9.4	9.0	7.6	7.1	7.8
Arrears 3-6 months/Total Loans	2.0	1.9	1.7	2.2	2.0	1.3	0.8	1.6
Arrears 6 – 12 months/Total Loans	1.6	1.9	1.7	1.5	1.8	1.2	1.3	1.3
Arrears over 12 months/Total Loans	3.5	4.4	5.0	5.7	5.2	5.1	5.0	4.9
Provisions to Total loans	2.8	3.2	3.4	3.5	2.6	2.5	2.4	2.3
Profitability Indicator								
Return on Assets (ROA)	1.4	1.4	1.1	0.9	0.9	1.1	1.1	1.3

Source: Central Bank of Barbados, Financial Services Commission.

1/ Includes foreign components unless otherwise stated.

2/ Reflects removal of financial consolidation.

Annex I. Risk Assessment Matrix (RAM)^{1/}

Source of Risks	Likelihood	Impact	Policy Response
Global Risks			
Tighter and volatile global financial conditions. Could depress FDI inflows, especially funding for new hotels and residences, leading to reduced construction.	High	Medium	Continue with fiscal consolidation to significantly reduce debt-to-GDP ratio and rebuild credibility, thereby increasing investors' confidence.
Fed normalization leading to surge in the US dollar. Could further weaken cost competitiveness, although impact mitigated by large share of trade with the U.S. and dollar pegs of other Caribbean tourist destinations.	High	Medium	Structural measures to improve competitiveness and boost attractiveness to tourists. Strengthen social compact and contain wage increases to reduce competitiveness problems.
Structurally weak growth in key advanced and emerging economies. Tourism sector is sensitive to growth in advanced economies, notably Canada, the U.K. and the U.S.	High	High	Structural measures to improve competitiveness and support development of other sectors.
Reduced financial services by global/regional banks ("de-risking"). While commercial banks are foreign owned, and have not indicated plans to deleverage and/or pull out, several firms in the offshore financial center have already lost correspondent services.	Medium	Medium/ High	Strengthen AML/CFT framework, adhere to best practice and enhance monitoring of the sector. Explore alternative mechanisms; collectively approach potential correspondent banks with other Caribbean countries to increase business volume.
Country-specific risks			
Fiscal financing pressures. Fiscal financing pressures, high borrowing costs, and possible monetization of the deficit raise the risk of a liquidity crisis and/or imperil the currency peg.	High	High	Continue with fiscal consolidation to substantially reduce the debt-to-GDP ratio, to reduce financing requirements and strengthen creditworthiness assessments.
Fiscal slippages/higher fiscal multipliers. Would reinforce market concerns about fiscal sustainability and undermine private sector confidence necessary for investment.	High	High	Reform social programs and consolidate state owned enterprises sector to reduce transfers envelope; review other spending, including public sector wage bill and rationalize tax systems to reduce tax compliance cost and tax avoidance.
Post-Brexit. Adverse impact on tourism and investment from uncertainties and economic spillovers associated with U.K. negotiations with the E.U.	High	High	Structural measures to improve competitiveness and boost attractiveness to tourists. Adhere to fiscal consolidation strategy, and accelerate growth-promoting structural reforms to boost investor confidence.
Extreme weather conditions. Since Barbados is located outside the hurricane zone, it is less frequently impacted by hurricanes, but the impact, should it occur, can be large. Moreover, it could be subject to other natural disasters, such as flooding.	Medium	High	Invest in climate resilient infrastructure that could mitigate disaster risk.

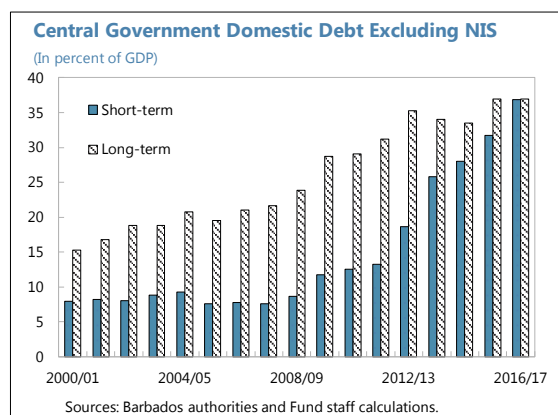
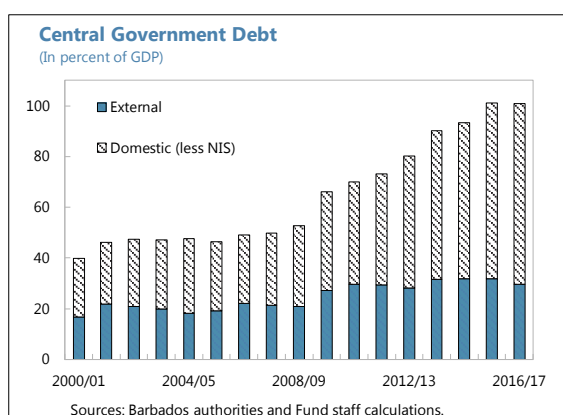
¹ The Risk Assessment Matrix (RAM) shows events that could materially alter the baseline path (the scenario most likely to materialize in the view of IMF staff). The relative likelihood of risks listed is the staff's subjective assessment of the risks surrounding the baseline ("low" indicates a probability below 10 percent, "medium" a probability between 10 and 30 percent, and "high" a probability between 30 and 50 percent). The RAM reflects staff views on the source of risks and overall level of concern as of the time of discussions with the authorities. Non-mutually exclusive risks may interact and materialize jointly.

Annex II. Debt Sustainability Analysis (DSA)

The May 2017/18 Budget measures are projected to place public debt on a downward trajectory. However, public debt remains high and sustainability risks elevated. Gross financing needs also remain a critical concern. The baseline debt path is highly vulnerable to unfavorable shocks from real interest rates. Moreover, there are sizable downside risks, including from low growth, continued significant recourse to short-term debt, rising arrears, and contingent liabilities.

A. Public Debt Sustainability Analysis

Structure of the Debt

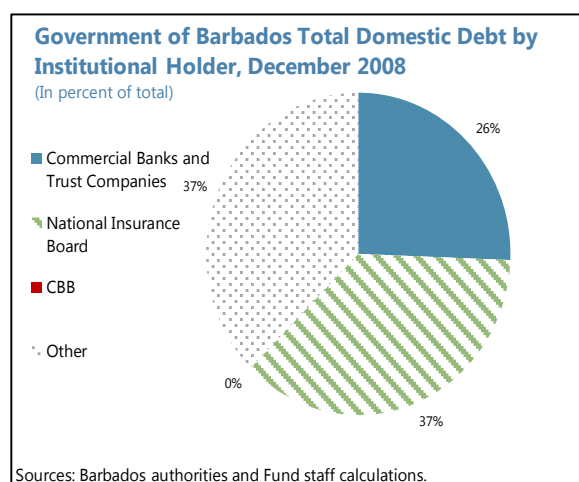
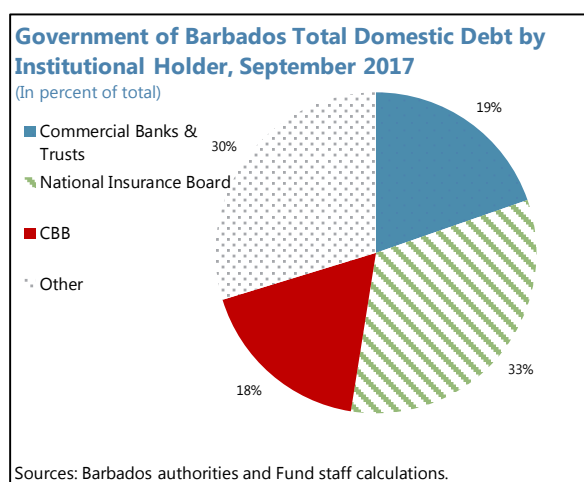


1. Barbados' central government debt, excluding NIS, more than doubled from 52.6 percent of GDP in FY2008/09 to 100.9 percent in FY2016/17. The definition of public debt used in this assessment is central government gross debt, excluding government securities held by the NIS and the stock of arrears.^{1,2} With the rapid increase in the debt, there has been an important change in its structure, with an increase in the share of short-term debt from 11.9 percent in FY2008/09 to 34.0 percent in FY2016/17. Domestic debt grew to around 70 percent of the total debt over the same period, from about 60 percent in FY2008/09. The share of commercial banks and trusts has declined to 19.1 percent in FY2016/17 from a high of 27.0 percent in FY2012/13. Central Bank of Barbados holdings of government debt reached 19.4 percent in FY2016/17 reflecting increased monetization of the debt. Government debt held by the NIS has grown from 18.5 percent of GDP in FY2008/09 to 36.1 percent of GDP at end-FY2016/17. External debt consists largely of

¹ Public debt obligations held by NIS are both assets and liabilities of the government, and are netted out under the definition prescribed in the IMF public debt statistics manual (see: Public Sector Debt Statistics: Guide for Compilers and Users, 2013). Including government securities held by the NIS, the debt stock increased from 65.4 percent of GDP in FY2008/9 to 137 percent in FY2016/17. Total public and publicly guaranteed debt was 150.0 percent of GDP at end FY2016/17 up from 73.2 percent in FY2008/09.

² Staff estimates central government arrears amounted to around 3.9 percent of GDP in FY2016/17; if accounted for in the DSA analysis the stock of debt would be accordingly higher. The expenditure data is based on approved expenditure, rather than paid, thus on an accrual basis.

bond placements and multilateral borrowing. Debt service has risen from 4.2 percent of GDP to 7.7 percent of GDP from FY2008/09 to FY2016/17.



Structure of the Debt									
	2008/09	2009/10	2010/11	2011/12	2012/13	2013/14	2014/15	2015/16	2016/17
	<i>Percent of fiscal year GDP</i>								
Central government debt, less NIS	52.6	66.1	70.0	73.2	80.3	90.2	93.4	101.0	101.0
	<i>Percent of central government debt excluding NIS</i>								
Domestic	60.4	58.9	57.7	59.9	65.1	65.0	65.9	68.6	70.7
<i>By institutional holder</i>									
Commercial banks and trusts	23.6	23.0	22.0	21.7	27.0	25.6	23.2	24.1	19.1
Central Bank of Barbados	1.8	1.8	1.2	2.8	2.1	5.3	7.8	11.9	19.4
Other, of which:	34.9	34.1	34.6	35.4	36.0	34.0	34.9	32.6	32.2
Insurance companies	7.4	7.4	8.4	9.8	11.8	10.4	9.6	8.6	8.2
Private sector	15.4	15.1	15.3	15.3	15.0	14.1	16.8	16.8	18.4
Other	12.2	11.7	10.9	10.3	9.2	9.4	8.5	7.1	5.5
<i>By type</i>									
Tbills	11.9	13.2	12.6	13.7	19.3	24.6	26.2	29.3	34.0
Debentures	34.3	32.4	32.6	34.4	35.2	29.8	30.1	30.6	29.5
Other (savings bonds, loans, and advances)	14.1	13.3	12.5	11.8	10.6	10.6	9.6	8.8	7.3
External	39.6	41.1	42.3	40.1	34.9	35.0	34.1	31.4	29.3
Multilateral	10.4	9.3	9.9	10.7	9.3	8.9	9.0	9.9	9.6
Bilateral	2.7	2.0	1.5	1.1	0.9	0.6	0.5	0.4	0.5
Commercial & PPP	6.4	5.3	4.7	4.2	3.7	7.7	7.9	7.2	5.7
Bond placements	20.1	21.7	23.1	21.0	18.4	15.5	14.5	12.0	11.6
Memorandum item									
Public sector debt less NIS, percent of FY GDP	63.3	80.5	86.1	89.5	94.6	105.3	107.8	115.1	114.0
NIS, percent of FY GDP	18.5	22.3	25.5	26.2	29.6	32.0	32.0	33.6	36.1

Sources: Barbados Statistical Services, Central Bank of Barbados, and Fund staff calculations.

Assumptions

2. The baseline scenario reflects the FY2017/18 budget proposals updated to take account of recent developments. The specific assumptions are as follows:

- **Growth and Inflation:** Growth is projected to dip in 2017 due to the fiscal consolidation and policy uncertainty, and recover slowly in the medium term, returning to around 1 percent in 2022. Inflation is projected to pick up to an annual average of 5.1 percent due to the pass-through from the higher taxes, then return to a long-run average of around 2.7 percent. The fiscal multiplier is calculated to be 0.3 reflecting the methodology in the FAD guidance note on fiscal multipliers.
- **Fiscal Balance:** The fiscal balance for FY2017/18, forecast to be -4.1 percent of GDP with a primary surplus of 3.7 percent. Over the medium term, the fiscal balance continues to improve to -3.0 percent of GDP on the assumptions of no policy change, which maintains current revenues and non-interest expenditure growth in line with nominal GDP, taking into account the full year impact of the 2017 budget, leading to an increase in the primary surplus to 4.4 percent of GDP.
- **Financing:** New financing requirements are primarily being met by new short-term debt instruments, with the share of short-term debt in total domestic debt rising; all long-term debt is rolled over reflecting the large role of NIS. External debt is based on available information on government plans to borrow from multilaterals and bilateral entities, based on the existing pipeline (following consultations with MDBs and donors). Assumptions on interest costs on new debt are:
 - Interest rate on external debt: US LIBOR (6M) plus spread (2pp) – 5.0 percent on average; all external debt is treated as one debt instrument, with 5 years' grace and 20 years' maturity,³ since the government is only borrowing from official bilateral and multilateral creditors
 - Interest rate on domestic short term: – 3-month U.S. T bill rate plus spread (2 pp) – 4.2 percent on average in medium term reflecting financial repression; all short-term debt is treated as one debt instrument
 - Interest rate on domestic long term: 10-year U.S. T-note rate plus spread (4pp) – 7.2 percent on average in medium term; all long-term debt is treated as one instrument with a 10 years' grace and a bullet repayment
 - Total privatization receipts are B\$240 million in FY2017/18 and 2018/19 from the sale of the Barbados National Oil Terminal Company and the Hilton Hotel, in foreign exchange.

Medium-Term Debt Sustainability Analysis

3. The public debt-to-GDP ratio is projected to fall from 97.2 percent in FY2017/18 to 85.7 percent in FY2022/23. Public debt dynamics are driven by the primary surplus noted above, of 3.7 percent in FY2017/18, expected to rise to 4.4 percent in the medium term. In the active scenario,

³ Reflecting that all new borrowing is from multilateral institutions at relatively low interest rates.

where the primary balance is increased to 7.5 percent over FY2017/18–FY2020/21, the debt declines to 76 percent of GDP by FY2022/23.

4. Risks are significant. The main risks are: (i) higher-than-expected increases in U.S. and domestic interest rates; and (ii) recognition of contingent liabilities and arrears, which are sizeable. The large gross financing needs are also an important risk, rising further from 51 percent of GDP in FY2017/18 to 53 percent by FY2022/23 because of the short-term nature of the debt and external debt payments in the outer years. The rollover risk is mitigated somewhat by the large share of the debt that is held by the Central Bank and the NIS, and the recent increases in reserve holding requirement on the commercial banks. However, the NIS capacity to absorb more government debt may be limited by its operational and investment surpluses which are projected to decline over time, and by prudential limits regarding asset concentration. Most importantly, the central bank has limited scope to finance the government given the fixed exchange rate regime, its ability to continue sterilizing the impact of monetization of the deficit indefinitely, and the level of reserves.

5. The heat map highlights significant risks to the debt profile, namely the rapid increase in short-term debt. That this debt is mostly held domestically helps to mitigate the risks from external shocks. Nevertheless, the high proportion of short-term domestic debt makes Barbados very vulnerable to an increase in domestic interest rates.

6. The stress test scenarios confirm the high vulnerability of debt and financing needs to shocks to real interest rates. Shocks to real interest rates push the debt-to-GDP ratio to about 101 percent by FY2021/22. Gross financing needs remain elevated at around 66 percent of GDP with the real interest rates shock. Shocks to real GDP growth, real exchange rates, and the primary balance can be absorbed, generating level changes but not significantly affecting the trajectory of the debt reduction.

7. Staff projections of GDP growth, the primary balance, and inflation have improved. Past projections have been generally overly optimistic, reflecting the unexpectedly prolonged nature of the economic crisis in Barbados, with an extended period dating back to 2008 of negative to stagnant growth and the inability of the authorities to implement their planned reform. More recently staff projections errors have been much narrower, and neutral, with growth and primary surplus slightly higher than projected. The “Boom-Bust” analysis does not apply to Barbados, because Barbados is experiencing weak growth.

B. External Debt

8. External public debt is relatively low and does not in itself pose solvency risks.

However, there are vulnerabilities in the medium term arising from the liquidity needs as a result of the repeated downgrading of Barbados' sovereign rating. This will make future access to external financing difficult and reduces the probability of rollover of existing debt and increases its costs substantially. Lack of data on external private debt prevents a full quantitative assessment of the economy's external position.

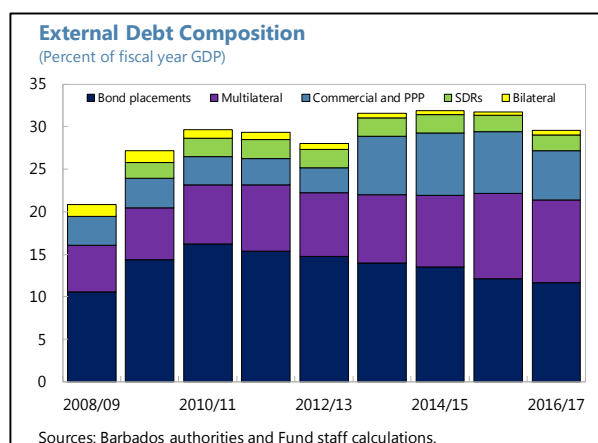


Figure 1. Barbados Public Sector Debt Sustainability Analysis (DSA) - Baseline Scenario

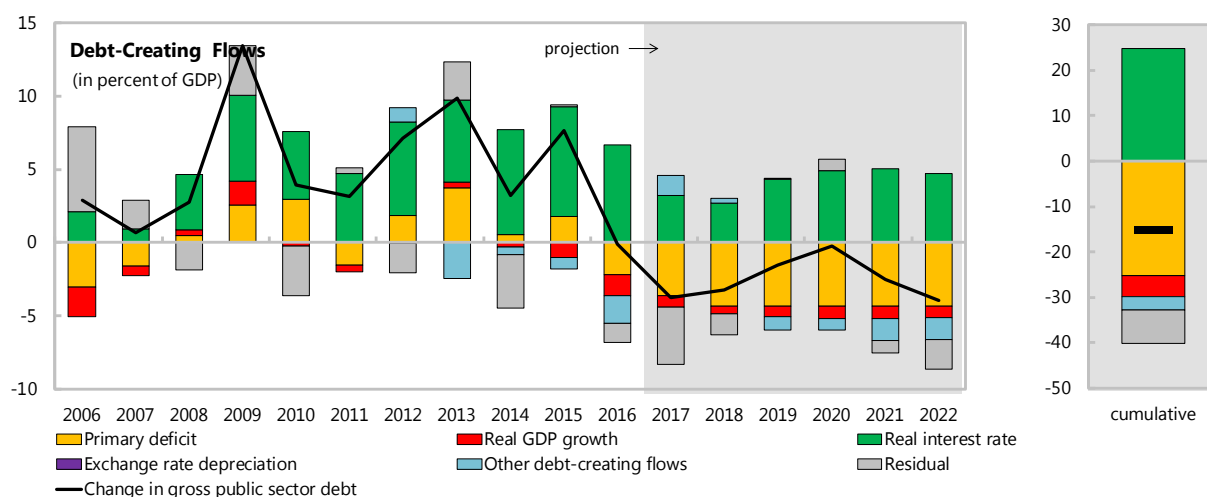
(in percent of GDP unless otherwise indicated)

Debt, Economic and Market Indicators

	Actual			Projections						As of October 01, 2017	
	2006-2014 ^{2/}	2015	2016	2017	2018	2019	2020	2021	2022		
Nominal gross public debt 1/	69.4	101.0	100.9	97.2	93.9	92.4	92.1	89.6	85.7	Sovereign Spreads (bp) 3/	628
Public gross financing needs	22.0	41.8	40.8	50.9	49.2	48.9	49.8	51.7	52.7	5Y CDS (bp)	n.a.
Real GDP growth (in percent)	0.4	1.1	1.5	0.8	0.6	0.8	1.0	1.0	1.0	Ratings	Foreign Local
Inflation (GDP deflator, in percent)	1.5	-0.4	1.0	4.6	4.5	2.8	2.7	2.7	2.7	Moody's	Caa3 Caa3
Nominal GDP growth (in percent)	1.9	0.7	2.5	5.5	5.1	3.7	3.7	3.7	3.7	S&Ps	CCC CCC
Effective interest rate (in percent) ^{4/}	8.5	7.7	7.8	8.1	7.4	7.6	8.3	8.4	8.2	Fitch	n.a. n.a.

Contribution to Changes in Public Debt

	Actual			Projections						cumulative	debt-stabilizing primary balance ^{9/}
	2006-2014	2015	2016	2017	2018	2019	2020	2021	2022		
Change in gross public sector debt	5.2	7.6	-0.1	-3.7	-3.3	-1.6	-0.3	-2.5	-3.9	-15.2	
Identified debt-creating flows	4.9	7.5	1.2	0.2	-1.9	-1.7	-1.0	-1.7	-1.9	-7.9	
Primary deficit	0.7	1.8	-2.2	-3.7	-4.3	-4.3	-4.3	-4.3	-4.3	-25.3	2.4
Primary (noninterest) revenue and grants	26.6	26.1	28.5	29.1	29.8	29.8	29.8	29.8	29.8	178.1	
Primary (noninterest) expenditure	27.2	27.9	26.3	25.4	25.5	25.5	25.5	25.5	25.5	152.9	
Automatic debt dynamics ^{5/}	4.4	6.4	5.2	2.5	2.1	3.6	4.0	4.2	3.9	20.3	
Interest rate/growth differential ^{6/}	4.4	6.4	5.2	2.5	2.1	3.6	4.0	4.2	3.9	20.3	
Of which: real interest rate	4.6	7.5	6.7	3.2	2.7	4.3	4.9	5.0	4.7	24.9	
Of which: real GDP growth	-0.1	-1.0	-1.4	-0.8	-0.6	-0.8	-0.9	-0.9	-0.8	-4.6	
Exchange rate depreciation ^{7/}	0.0	0.0	0.0	...	...	...	...	...	...	...
Other identified debt-creating flows	-0.2	-0.8	-1.9	1.4	0.3	-0.9	-0.8	-1.5	-1.5	-3.0	
Privatization receipts (negative)	0.1	0.0	0.0	1.4	0.9	0.0	0.0	0.0	0.0	2.3	
Contingent liabilities	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
National Insurance Scheme	-0.3	-0.8	-1.9	0.0	-0.6	-0.9	-0.8	-1.5	-1.5	-5.3	
Residual, including asset changes ^{8/}	0.4	0.1	-1.3	-3.9	-1.4	0.1	0.8	-0.8	-2.0	-7.3	



Source: IMF staff.

1/ Defined as central government debt excluding NIS holding of government debt.

2/ Based on available data.

3/ Long-term bond spread over U.S. bonds.

4/ Defined as interest payments divided by debt stock (excluding guarantees) at the end of previous year.

5/ Derived as $[(r - \pi(1+g) - g + ae(1+r))/(1+g+\pi+gnt)]$ times previous period debt ratio, with r = interest rate; π = growth rate of GDP deflator; g = real GDP growth rate; a = share of foreign-currency denominated debt; and e = nominal exchange rate depreciation (measured by increase in local currency value of U.S. dollar).

6/ The real interest rate contribution is derived from the numerator in footnote 5 as $r - \pi(1+g)$ and the real growth contribution as $-g$.

7/ The exchange rate contribution is derived from the numerator in footnote 5 as $ae(1+r)$.

8/ Includes asset changes and interest revenues (if any). For projections, includes exchange rate changes during the projection period.

9/ Assumes that key variables (real GDP growth, real interest rate, and other identified debt-creating flows) remain at the level of the last projection year.

Figure 2. Barbados Public DSA - Composition of Public Debt and Alternative Scenarios

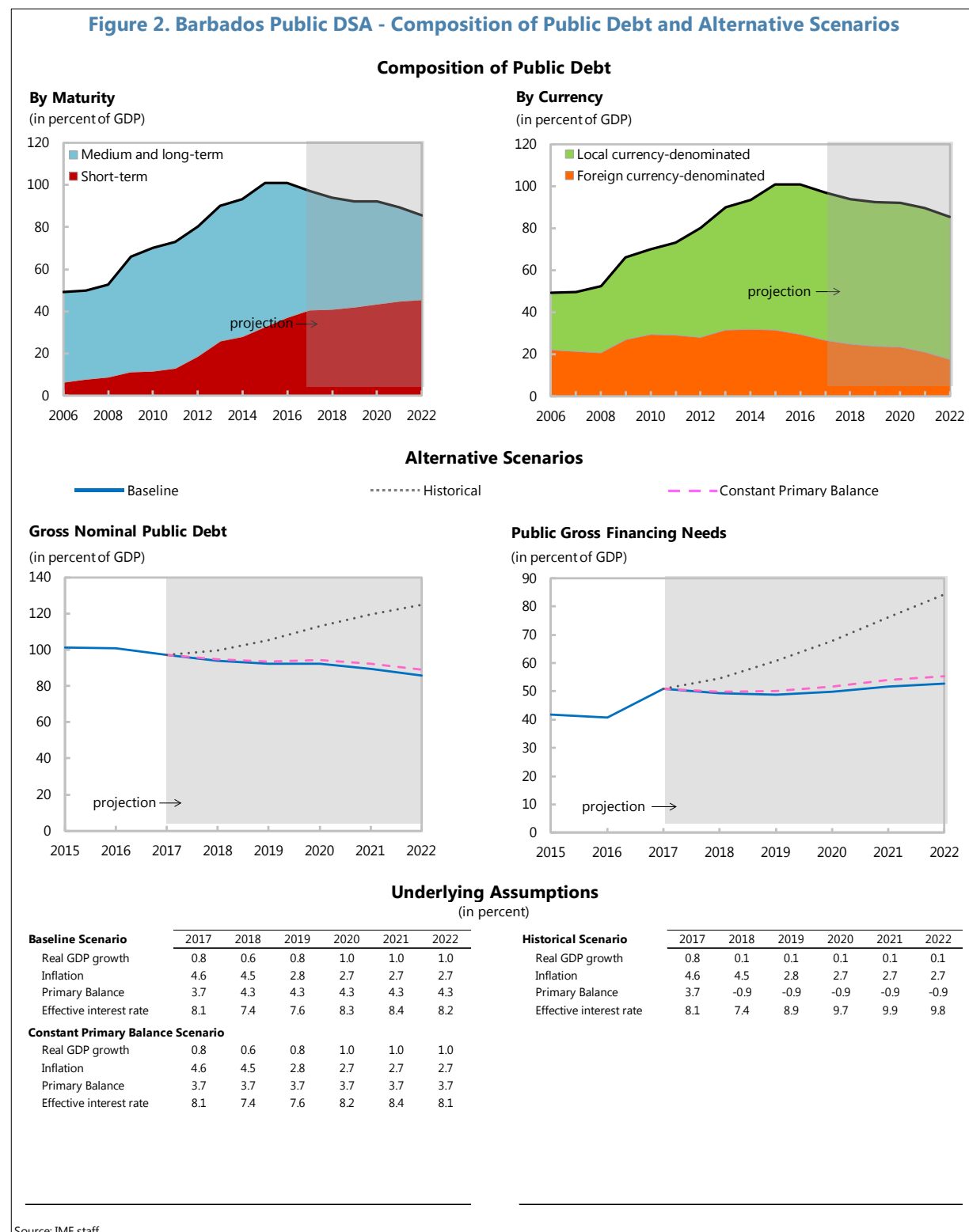
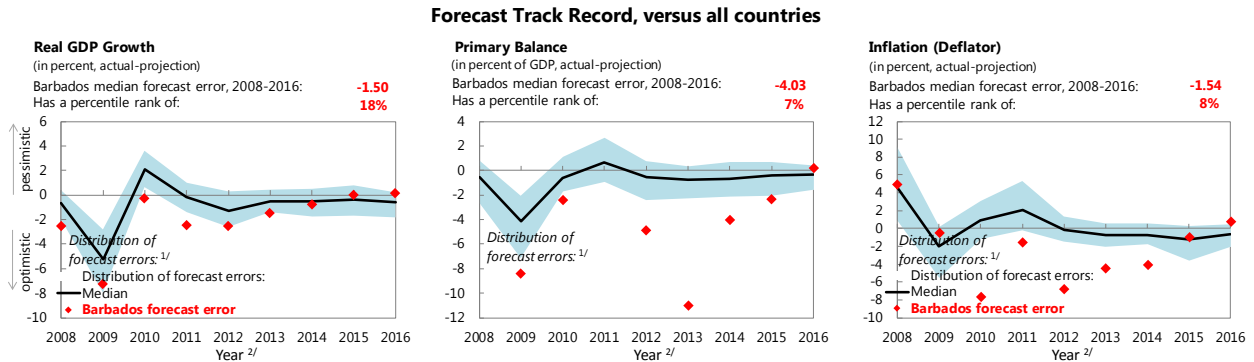
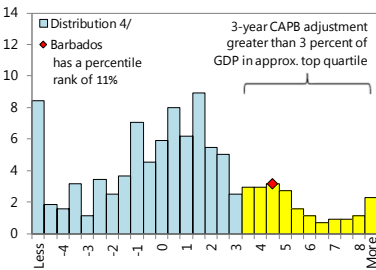


Figure 3. Barbados Public DSA – Realism of Baseline Assumptions

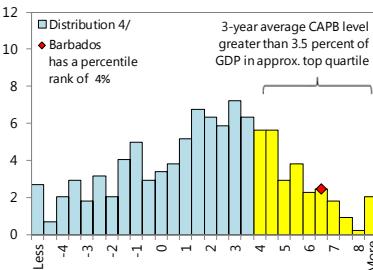


Assessing the Realism of Projected Fiscal Adjustment

3-Year Adjustment in Cyclically-Adjusted Primary Balance (CAPB)
(Percent of GDP)

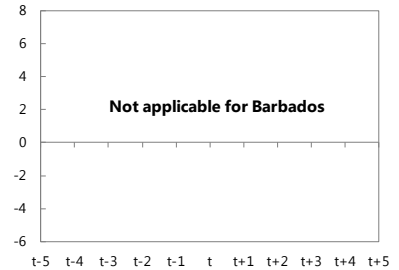


3-Year Average Level of Cyclically-Adjusted Primary Balance (CAPB)
(Percent of GDP)



Boom-Bust Analysis^{3/}

Real GDP growth
(in percent)
— Barbados



Source : IMF Staff.

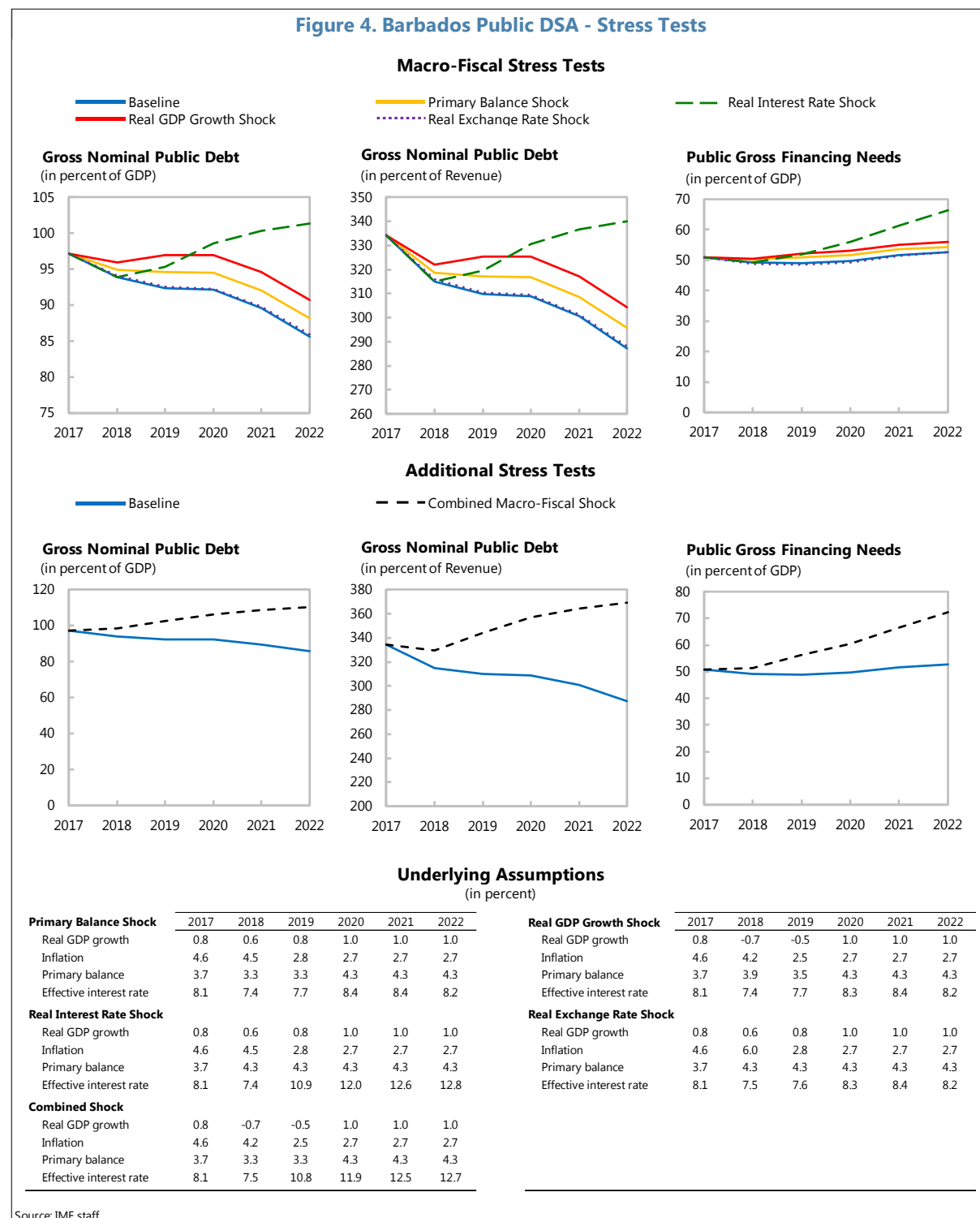
1/ Plotted distribution includes all countries, percentile rank refers to all countries.

2/ Projections made in the spring WEO vintage of the preceding year.

3/ Not applicable for Barbados, as it meets neither the positive output gap criterion nor the private credit growth criterion.

4/ Data cover annual observations from 1990 to 2011 for advanced and emerging economies with debt greater than 60 percent of GDP. Percent of sample on vertical axis.□

Figure 4. Barbados Public DSA - Stress Tests



Source: IMF staff.

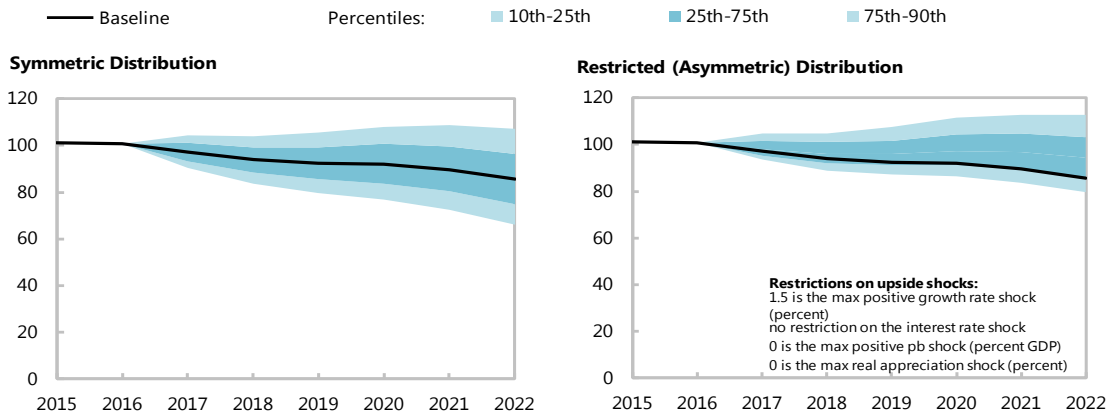
Figure 5. Barbados Public DSA Risk Assessment

Heat Map

Debt level ^{1/}	Real GDP Growth Shock	Primary Balance Shock	Real Interest Rate Shock	Exchange Rate Shock	Contingent Liability shock
Gross financing needs ^{2/}	Real GDP Growth Shock	Primary Balance Shock	Real Interest Rate Shock	Exchange Rate Shock	Contingent Liability Shock
Debt profile ^{3/}	Market Perception	External Financing Requirements	Change in the Share of Short-Term Debt	Public Debt Held by Non-Residents	Foreign Currency Debt

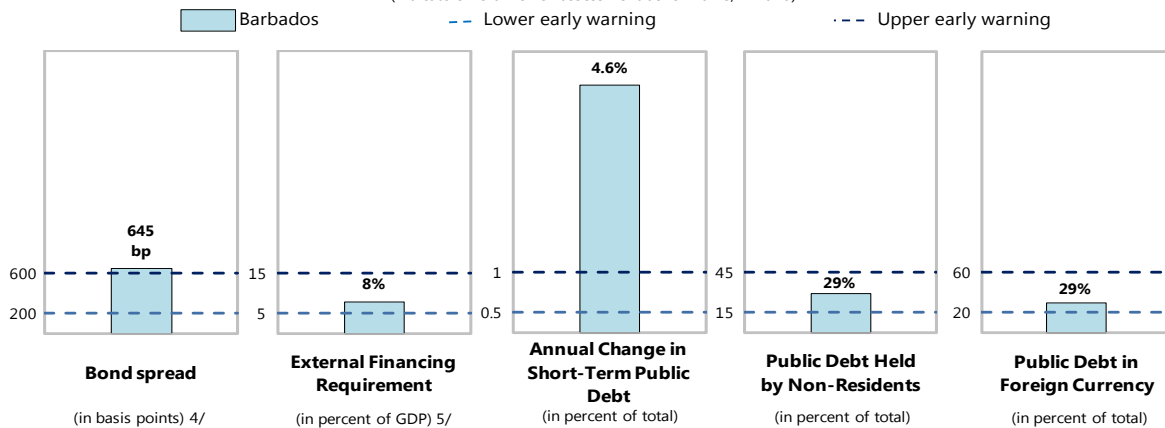
Evolution of Predictive Densities of Gross Nominal Public Debt

(in percent of GDP)



Debt Profile Vulnerabilities

(Indicators vis-à-vis risk assessment benchmarks, in 2016)



Source: IMF staff.

1/ The cell is highlighted in green if debt burden benchmark of 70% is not exceeded under the specific shock or baseline, yellow if exceeded under specific shock but not baseline, red if benchmark is exceeded under baseline, white if stress test is not relevant.

2/ The cell is highlighted in green if gross financing needs benchmark of 15% is not exceeded under the specific shock or baseline, yellow if exceeded under specific shock but not baseline, red if benchmark is exceeded under baseline, white if stress test is not relevant.

3/ The cell is highlighted in green if country value is less than the lower risk-assessment benchmark, red if country value exceeds the upper risk-assessment benchmark, yellow if country value is between the lower and upper risk-assessment benchmarks. If data are unavailable or indicator is not relevant, cell is white. Lower and upper risk-assessment benchmarks are:

200 and 600 basis points for bond spreads; 5 and 15 percent of GDP for external financing requirement; 0.5 and 1 percent for change in the share of short-term debt; 15 and 45 percent for the public debt held by non-residents; and 20 and 60 percent for the share of foreign-currency denominated debt.

4/ Long-term bond spread over U.S. bonds, an average over the last 3 months, 03-Jul-17 through 01-Oct-17.

5/ External financing requirement is defined as the sum of current account deficit, amortization of medium and long-term total external debt, and short-term total external debt at the end of previous period.

Table 1. Barbados: External Debt Sustainability Framework, 2012–2022
(In percent of GDP, unless otherwise indicated)

	Actual					Projections							Debt-stabilizing non-interest current account 6/
	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022		
Baseline: External debt	44.7	47.5	47.8	47.4	44.8	41.4	38.6	37.0	36.2	33.3	29.4		
Change in external debt	-3.3	2.8	0.3	-0.4	-2.6	-3.5	-2.8	-1.5	-0.9	-2.9	-3.9		
Identified external debt-creating flows (4+8+9)	-1.7	4.7	2.5	0.3	0.2	0.5	0.0	-0.4	-0.5	-0.6	-1.6		
Current account deficit, excluding interest payments	6.4	6.7	6.7	3.7	1.9	1.4	0.9	0.8	0.8	0.8	0.8		
Deficit in balance of goods and services	4.5	3.9	4.7	1.7	-1.0	-1.5	-1.3	-1.4	-1.4	-1.4	-1.4		
Exports	42.4	42.0	40.5	41.6	43.7	41.3	40.1	39.6	39.2	38.9	38.6		
Imports	46.9	46.0	45.3	43.3	42.7	39.8	38.8	38.3	37.8	37.5	37.2		
Net non-debt creating capital inflows (negative)	-10.6	-3.3	-6.8	-5.6	-3.5	-2.8	-2.8	-2.8	-2.8	-2.8	-3.6		
Automatic debt dynamics 1/	2.5	1.3	2.5	2.2	1.8	1.9	1.9	1.6	1.5	1.5	1.1		
Contribution from nominal interest rate	2.1	1.7	2.5	2.4	2.5	2.2	2.1	1.9	1.8	1.8	1.5		
Contribution from real GDP growth	-0.1	0.3	0.0	-0.5	-0.8	-0.4	-0.2	-0.3	-0.3	-0.3	-0.3		
Residual, incl. change in gross foreign assets (2-3) 3/	-1.6	-1.8	-2.2	-0.8	-2.8	...	...	...	...	...	...
External debt-to-exports ratio (in percent)	105.3	113.1	118.0	113.9	102.6	100.0	96.2	93.4	92.2	85.6	76.3		
Gross external financing need (in billions of US dollars) 4/	0.5	0.5	0.5	0.4	0.3	0.3	0.3	0.2	0.2	0.3	0.4		
In percent of GDP	10.0	10.0	10.6	8.7	6.8	6.3	5.2	4.5	3.7	5.3	6.5		
Scenario with key variables at their historical averages 5/													
Key Macroeconomic Assumptions Underlying Baseline						10-Year Historical Average	10-Year Standard Deviation						
Real GDP growth (in percent)	0.3	-0.6	0.1	1.0	1.6	0.1	1.6	0.9	0.5	0.8	1.0	1.0	
GDP deflator in US dollars (change in percent)	-1.0	1.5	-0.1	-0.4	-0.2	1.1	3.1	4.5	5.1	2.9	2.7	2.7	
Nominal external interest rate (in percent)	4.4	3.8	5.3	5.1	5.3	5.7	1.5	5.3	5.3	5.1	5.1	4.5	
Growth of exports (US dollar terms, in percent)	-5.2	0.0	-3.6	3.2	6.5	0.4	7.8	-0.3	2.5	2.6	2.9	2.9	
Growth of imports (US dollar terms, in percent)	-4.8	-1.2	-1.5	-3.9	0.2	-0.9	8.3	-1.7	2.9	2.3	2.5	3.0	
Current account balance, excluding interest payments	-6.4	-6.7	-6.7	-3.7	-1.9	-5.3	2.5	-1.4	-0.9	-0.8	-0.8	-0.8	
Net non-debt creating capital inflows	10.6	3.3	6.8	5.6	3.5	6.6	2.8	2.8	2.8	2.8	2.8	3.6	

Sources: Barbados Authorities and Fund staff projections.

1/ Derived as $[r - g - r(1+g) + ea(1+n)] / (1+g+e+g)$ times previous period debt stock, with r = nominal effective interest rate on external debt; r = change in domestic GDP deflator in US dollar terms; g = real GDP growth rate; e = nominal appreciation (increase in dollar value of domestic currency); and a = share of domestic-currency denominated debt in total external debt.

2/ The contribution from price and exchange rate changes is defined as $[-r(1+g) + ea(1+n)] / (1+g+e+g)$ times previous period debt stock. r increases with an appreciating domestic currency ($e > 0$) and rising inflation (based on GDP deflator).

3/ For projection, line includes the impact of price and exchange rate changes.

4/ Defined as current account deficit, plus amortization on medium- and long-term debt, plus short-term debt at end of previous period.

5/ The key variables include real GDP growth; nominal interest rate; dollar deflator growth; and both non-interest current account and non-debt inflows in percent of GDP.

6/ Long-run, constant balance that stabilizes the debt ratio assuming that key variables (real GDP growth, nominal interest rate, dollar deflator growth, and non-debt inflows in percent of GDP) remain at their levels of the last projection year.

Annex III. External Sector Assessment, Competitiveness, and Reserve Adequacy

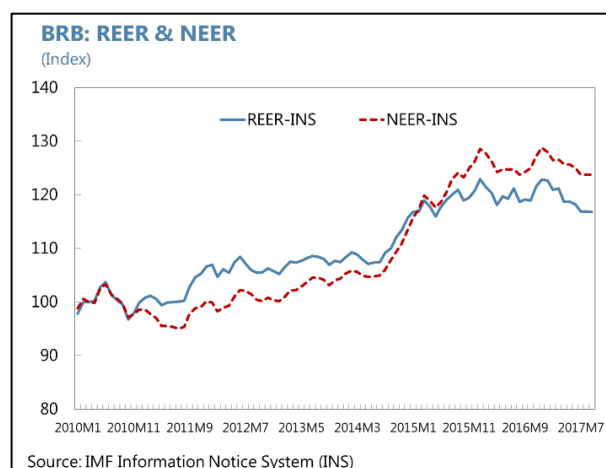
Overall Assessment: Barbados' overall external position is moderately weaker than the level consistent with the medium-term fundamentals and desirable policies. The current account gap is estimated at -1.4 percent, translating into a 4.3 percent REER overvaluation. The assessment is supported by the declining current account balance over the last two years. However, foreign reserves have fallen below the prudent level, covering only 1.6 months of imports by end-September 2017 because of depressed official and private inflows reflecting concerns about debt sustainability and central bank financing of the deficit.

A. Recent Developments in External Account

1. The Real Effective Exchange Rate (REER) has depreciated by about 5 percent in 2017Q3, reversing the 4 percent appreciation in 2016. The depreciation reflects the relative depreciation of the US dollar against major currencies.

Balance of Payments, 2014-16			
Percent of GDP			
	2014	2015	2016
Current account	-9.3	-6.1	-4.4
Trade balance of goods	-18.4	-15.7	-14.8
Exports of goods and services	40.5	41.6	43.7
Imports of goods and services	45.3	43.3	42.7
Services	13.7	14.0	15.8
Credits	23.6	24.6	26.2
Travel	19.0	20.2	21.8
Debits	9.9	10.5	10.4
Income	-4.2	-4.5	-4.6
Current transfers (private and public)	-0.3	0.0	-0.7
Capital and Financial Account	7.8	4.5	0.8
Public sector	0.9	-0.8	-1.8
Private sector	6.8	5.6	3.5
Of which, short term	0.2	-0.1	-0.8

Sources: Authorities and Fund staff calculations.



2. The current account deficit has fallen by more than half since 2014 reflecting the decline in fuel prices and an increase in export earnings. The current account deficit has narrowed to 4.4 percent of GDP in 2016, from 6.1 percent in 2015, and 9.3 percent in 2014. These improvements reflect better terms of trade, especially the fall in fuel prices, and growth in exports of goods and services, which increased by 3.2 and 6.5 percent in 2015 and 2016, respectively.

B. External Sustainability Assessment

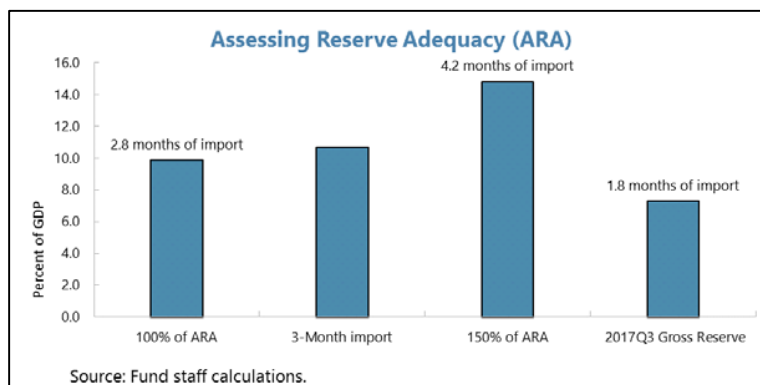
3. The EBA-lite current account model indicates that the external position is moderately weaker than fundamentals suggest. The EBA-lite methodology yields mixed results and staff considers the current account model to be the most informative. The current account gap of -1.4 percent of GDP reflects an actual current account deficit of -4.4 percent of GDP relative to an

estimated deficit norm of -2.9 percent. The policy gap of -2.4 percent largely reflects inadequate fiscal policy, a deterioration in the reserve position, and weak private credit growth.

Summary Table- Current Account Balance Approach			
CA-Actual	-4.4%	CA-Fitted	-5.3%
CA-Norm	-2.9%	Residual	1.0%
CA-Gap	-1.4%	Policy gap	-2.4%
Elasticity	-33.1%		
Real Exchange Rate Gap	4.3%	Cyclical Contributions	0.3%
		Cyclically adjusted CA	-4.7%
		Cyclically adjusted CA Norm	-3.3%

Source: Fund staff calculations

4. Reserves have fallen below what could be considered adequate because of weak capital inflows—both official and private. Official inflows were negative in 2015 and 2016, as debt service more than offset modest disbursements. Private inflows also remained low compared to historical norms. The Assessing Reserve Adequacy (ARA) methodology suggest that gross reserves should be in the range of 9.9 to 14.8 percent of GDP, corresponding to 2.8 to 4.2 months of import, whereas the 2017Q3 level of gross reserves is 5.9 percent of GDP, covering 1.8 months of import (1.6 months on a net reserves basis).¹ Staff



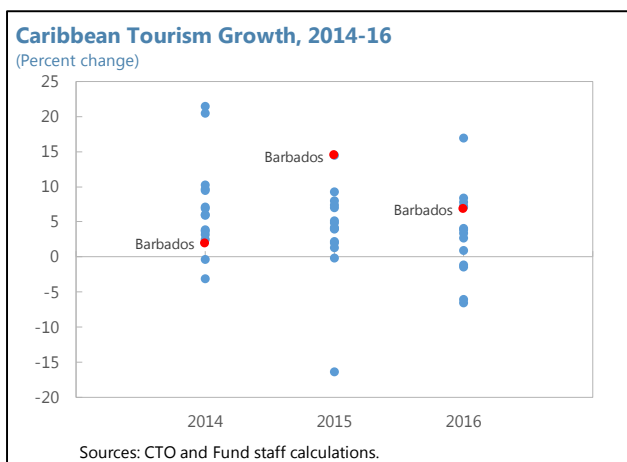
projections indicate that gross reserves—after stabilizing at about 2.1 months of imports (1.9 months in net reserves basis) over the next 3 years—would fall further because of large debt service bullet payments in FY2021/22.

C. Competitiveness

5. Despite the appreciation of the REER since 2010, other indicators do not indicate loss of competitiveness. Tourism, after several years of weak performance strongly rebounded in 2015, and continued to grow rapidly in 2016 and 2017. It has posted some of the strongest performances in the Caribbean. Long-stay arrivals increased by 14 percent in 2015 and 6.7 percent in 2016. Through September 2017, arrivals increased a further 6.2 percent relative to the same period last year while tourism spending in the first half of 2017 is estimated to have grown by 7.3 percent. While wage data is not available, other factors point to an internal devaluation that has taken place

¹ Gross reserves are total international reserves. Net international reserves exclude short-term reserve-related liabilities to nonresidents. In the case of Barbados, this is mainly commercial banks' credit facility.

that may not be reflected in the measure of the REER.² Public sector wages have not increased since 2009, while cumulative inflation during 2009 to 2017H1 was about 27 percent notwithstanding deflation in 2015. The decline in energy and other commodity prices point to lower domestic production costs, which are partly reflected in the negative and low inflation in 2015 and early 2016. Finally, anecdotal evidence suggest that hotels have been discounting, to maintain competitiveness vis a vis the rest of the region. Tourism spending estimates show a cumulative decline of 11 percent on spending on accommodations through end-2016 in three years, despite a cumulative increase in long-stay arrivals of 24.2 percent.³

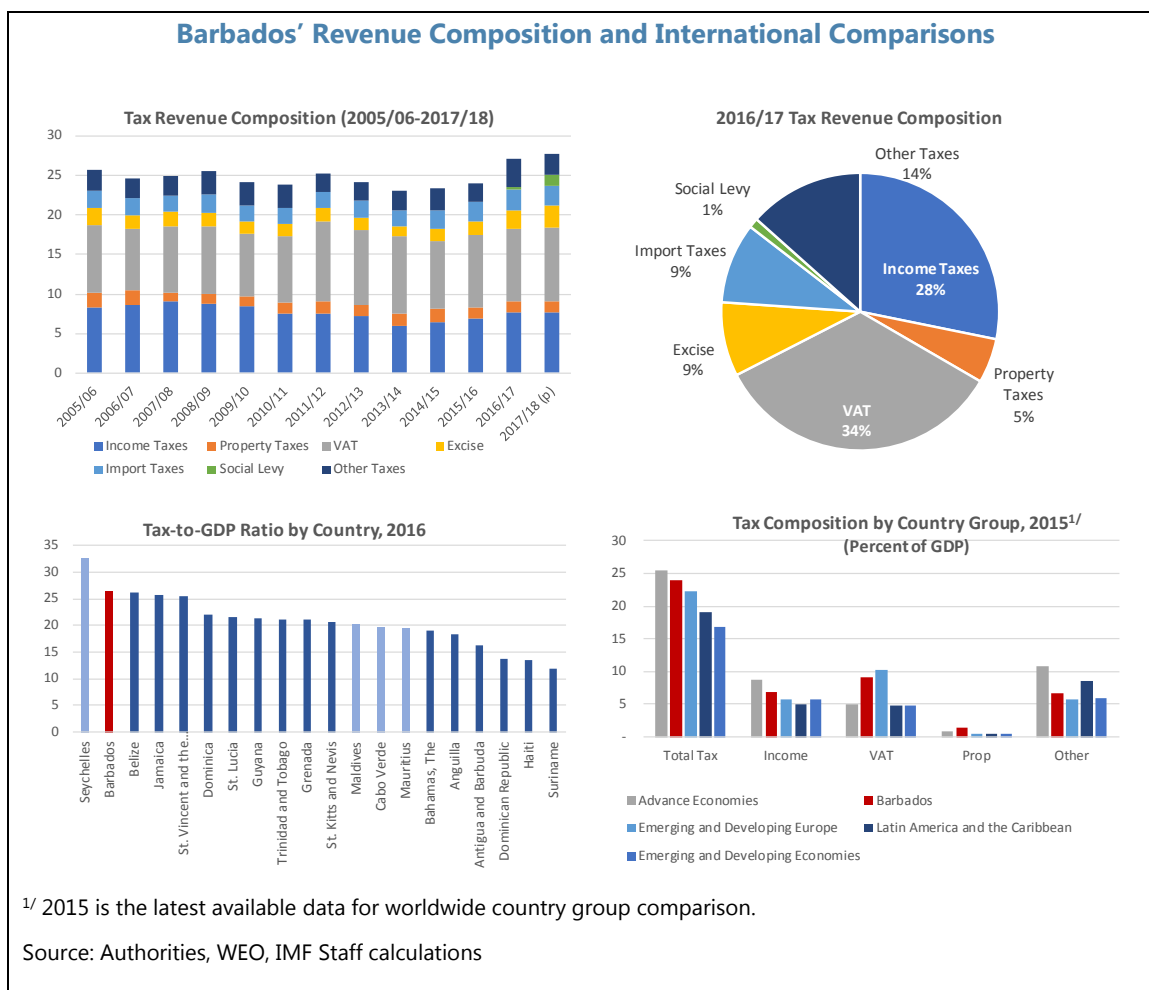


² The REER is estimated using 2004-2005 merchandise trade weights that excludes trade in services, and may therefore provide an incomplete indication of actual developments.

³ This data is inconclusive as it would also reflect the decline in average length of stay and increased use of internet based lower cost sharing platforms, such as Airbnb.

Annex IV. Barbados Revenue Mobilization

1. Barbados tax-to-GDP ratio is relatively high. It ranks as one of the highest in the Caribbean region and among similar, tourism-based economies, it is exceeded only by Seychelles. In 2015, Barbados' tax effort placed it in-between average ratios for Advanced Economies (25.5 percent of GDP) and Emerging and Developing Europe (22.3 percent of GDP).



2. The tax-to-GDP ratio has significantly increased in recent years. After deteriorating to 24 percent of GDP in the aftermath of the financial crisis it recovered in 2016/17 to early 2000s' levels, to 27.1 percent of GDP with a further improvement to 27.7 percent of GDP projected for FY2017/18.^{1,2} Since 2013/14, the tax-to-GDP ratio increased by 4 percentage points and is

¹ Income taxes registered the largest decline, partly reflecting a sharp deterioration of CIT receipts from the offshore sector.

² The tax-to-GDP ratio captures some non-tax receipts (e.g. proceeds from various registration and license fees, and sundry levies), which implies that the actual tax ratio is lower. In addition, revenue data for 2016/17-2017/18 is reported on gross basis, that is, including prospective tax refunds.

projected to rise by a further 0.6 percent in 2017/18. The major contributors to the tax revenue effort have traditionally been VAT and income taxes, accounting for 34 and 28 percent of total tax revenue in 2016/17, respectively.

3. The improved performance reflects numerous changes in Barbados' tax regime over the last several years. The authorities sought to increase revenue through: (i) base-broadening measures (abolishing the zero-VAT rate on certain items, imposing VAT to betting and gaming, subjecting airtime and sweetened drinks to excise taxes, and phasing out certain deductions under PIT);³ (ii) rate increases (bank asset tax, property taxes, petroleum excises); and (iii) the introduction of new taxes—the National Social Responsibility Levy (effectively an excise tax on imports and first sale of locally manufactured goods), and a Foreign Exchange Fee. However, the authorities have also increased tax concessions for the tourism sector to include imported consumption goods, including alcohol (2014), reduced the VAT rate (to 7.5 percent) on tourism services,⁴ decreased PIT rates, repealed the municipal solid waste tax (2015), and allowed the consolidation tax (a surtax on personal income) to expire (2016).⁵ They have also provided a tax amnesty in 2016 and 2017; which although it is intended to raise revenue, may contribute to lower compliance rates and hence lower tax collections in the long run.

4. The efficiency of the tax system appears to be suboptimal. Although the recent tax regime changes increased revenue productivity, they have reduced the overall efficiency and progressivity of the tax regime. In the last four years, the share of indirect taxes increased by 4 percentage points while that of direct taxes decreased by 2 percentage points. In particular, the increase in the NSRL's rate from 2 to 10 percent with a corresponding exemption for the tourism, manufacturing, and offshore sectors, increased the tax burden on households and small businesses relative to keeping the burden on productive sectors.

5. There is scope to improve the existing tax regime to make it more efficient and equitable. Given the high-level of taxation, the focus should be on increasing the efficiency of the VAT, income, and property taxes by reducing exemptions and seeking other ways to make it more progressive. This would allow for at least a partial reversal of the NSRL. In this regard the authorities should reconsider the recommendations of the 2014 IMF FAD tax policy report. Further, a thorough review of the existing tax structures is warranted.

6. Progress in reforming revenue administration will be central to boosting revenue. Strengthening revenue administration functions has the potential to not only safeguard but also improve collections. In response to the 2016 assessment of tax administration (TADAT) the authorities have embarked on a reform program with a view to improving Barbados Revenue Authority's (BRA) ability to perform effectively, including through: (i) improving its IT systems and

³ Most of the base-broadening measures followed the 2014 IMF FAD technical assistance' recommendations.

⁴ The concessions for tourism aimed to revive the tourism sector that only started recovering from the financial crisis in 2015.

⁵ The consolidation tax was introduced as a temporary measure to address the loss of other revenues as a result of the global financial crisis.

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data quality, to facilitate an increase in reliance on electronic payment facilities for taxpayers; and (ii) establishing a large taxpayer unit, which will be able use modern risk-based approaches in managing taxpayer and trader compliance. More is needed, in particular: (i) eliminating tax arrears and improving the management of this important function more broadly; and (ii) finalizing the merger of tax and customs to improve key customs functions. A review of tax policies, together with the strengthening of tax administration and improving tax compliance, per the authorities' Barbados Sustainable Recovery Plan, should be an important part of Barbados' strategy to improve fiscal balance and stimulate economic growth.