FOR AGENDA

SM/84/163

CONTAINS CONFIDENTIAL INFORMATION

July 9, 1984

To: Members of the Executive Board

From: The Acting Secretary

Subject: St. Vincent and the Grenadines - Staff Report for the 1984 Article IV Consultation

Attached for consideration by the Executive Directors is the staff report for the 1984 Article IV consultation with St. Vincent and the Grenadines, which will be brought to the agenda for discussion on a date to be announced.

If Executive Directors have technical or factual questions relating to this paper prior to the Board discussion, they should contact Mr. Amselle (ext. (5)7682) or Mr. Khor (ext. (5)7699).

Att: (1)

Other Distribution:
Department Heads

CONTAINS CONFIDENTIAL INFORMATION

INTERNATIONAL MONETARY FUND

St. Vincent and the Grenadines

Staff Report for the 1984 Article IV Consultation

Prepared by the Representatives for the 1984 Article IV Consultation with St. Vincent and the Grenadines

Approved by E. Wiesner and W.A. Beveridge

July 6, 1984

The 1984 Article IV consultation discussions with St. Vincent and the Grenadines were held in Kingstown in the period April 25-May 9, 1984. The representatives of St. Vincent and the Grenadines included the Prime Minister, who is also Minister of Finance; other members of the Cabinet; the Financial Secretary; senior officials in the ministries; and representatives of the major public enterprises. The mission also met with the Governor of the Eastern Caribbean Central Bank and with representatives of commercial banks and private businesses. The staff mission consisted of Messrs. Amselle (Head), Da Costa, Khor, Ms. Spinola (all WHD), Mr. Tareen (TRE), and Ms. Phillips (Secretary-TRE). The Fund mission collaborated with a World Bank mission which was visiting St. Vincent and the Grenadines concurrently. The mission was assisted by Mr. Gantt, the Fund's Regional Advisor. Mr. Leonard, the Alternate Executive Director for St. Vincent and the Grenadines, participated in the final round of policy discussions. St. Vincent and the Grenadines has accepted the obligations of Article VIII, Sections 2, 3, and 4 of the Articles of Agreement.

I. Recent Developments

In 1979-80 economic activity was adversely affected by a volcanic eruption and a hurricane which substantially reduced agricultural output. Real GDP rose by 9 percent in 1981, reflecting a strong recovery in banana production, but growth slowed to less than 3 percent in 1982 as agricultural production fell once again because of drought (Table 1). In 1983 real GDP rose by about 4 1/2 percent as agricultural output rebounded and tourism increased modestly. Prospects for 1984 are for continued growth in agriculture and rising activity in both manufacturing and construction, because of an expansion in industrial capacity and commencement of work on a large power project.

Table 1. St. Vincent and the Grenadines:
Selected Economic Indicators

	1980	1981	1982	Prel. 1983	Proj. 1984
(In millions of Eastern Caribbean dollars)					
GDP at current market prices	158.1	197.0	223.8	248.2	274.0
Gross domestic expenditure	224.2	244.2	282.9	304.3	334.5
GDP at 1977 market prices	114.3	124.6	128.0	133.5	139.5
(Percentage change)					
GDP at current market prices	12.8	24.6	13.6	10.9	10.4
Gross domestic expenditure	17.0	8.9	15.8	7.5	9.9
GDP at 1977 market prices	4.5	9.0	2.7	4.3	4.5
GDP deflator	8.0	14.3	10.6	6.3	5.6
Consumer prices (average)	17.2	12.7	7.3	5.4	4.0
Terms of trade	-3.3	2.4	2.1	4.5	0.8

Sources: Statistical Office, Ministry of Finance; Organization of East Caribbean States Secretariat; and Fund staff estimates.

In 1981, domestic demand rose at a much slower pace than nominal GDP, reflecting mainly a slowdown in private spending. As a result, the resource gap narrowed in relation to GDP, from 42 percent in 1980 to 24 percent in 1981. A modest upsurge in domestic spending in relation to output resulted in a slight widening of the resource gap in 1982, but the trend was reversed again in 1983 owing to a slowdown in private consumption outlays. The normalization of economic activity following the disruptions caused by the natural disasters in 1979-80 and a slower increase in import prices resulted in a substantial reduction in the rate of inflation; the average annual increase in consumer prices declined from more than 17 percent in 1980 to 5 1/2 percent in 1983.

Following a two-year freeze on civil servants' salaries, the Central Government agreed in July 1981 on a three-year contract which provided for a 30 percent increase in salaries of permanent workers in FY 1981/82 1/ and for annual increases of 10 percent for the next two fiscal years. The state enterprises and the private sector have traditionally followed the Central Government in granting wage increases; increases in 1982-83 were generally in the range of 7 percent to 12 percent, well ahead of the rate of increase in consumer prices. Because of the relatively low absolute level of wages, export-oriented manufacturing firms--most of which produce for the U.S. market--apparently have been able to absorb the increase in wage costs.

1/ Fiscal years begin on July 1.

After two years of deficits, public sector savings 1/ became positive in FY 1982/83, mainly because of a sharp improvement in central government receipts following the adoption of a number of revenue-generating measures. The balance on public sector current operations shifted from a deficit of 1 1/2 percent of GDP in FY 1981/82 to a surplus of 1 percent of GDP in FY 1982/83 (Table 2). In FY 1983/84 the current expenditures of the Central Government have risen faster than revenues, but the decline in central government savings has been more than offset by the growth in the savings of the National Provident Fund, and total public sector savings have risen to 1 1/2 percent of GDP. The overall public sector deficit after grants declined in relation to GDP from 6 percent in FY 1981/82 to 3 percent in FY 1983/84 as current revenues rose at an annual rate of 18 percent during the period, compared with a yearly growth in total expenditures of 8 1/2 percent.

Public sector investments, which to a large extent depend on the availability of project-related foreign financing, reached a peak in FY 1980/81 (22 1/2 percent of GDP), reflecting mainly outlays for reconstruction and for the purchase and installation of a sugar refining plant. The growth of capital spending moderated in the three following years and fell to less than 8 percent of GDP in FY 1983/84.

In the past three years the state-owned Sugar Industry Ltd. and the Arrowroot Industry Association have incurred increasing deficits. Although the domestic price of sugar is three times higher than international prices, it is still not high enough to cover the cost of producing sugar locally as the sugar factory has been afflicted by frequent breakdowns, uneven deliveries of sugar cane, and a large debt service burden. Since the startup of operations in 1981, current outlays have exceeded revenues from sales by a large margin and the enterprise has been relying increasingly on the state-owned National Commercial Bank (NCB) to finance its operating deficit. The Arrowroot Industry Association, which produces arrowroot starch mainly for use in the manufacture of a special paper for computer printers, has been adversely affected since 1981 by dwindling demand, as arrowroot has been increasingly displaced by cheaper substitutes. This has led to growing stocks which have been financed by increased borrowing from the NCB. In FY 1982/83, the combined deficit of these two enterprises was equivalent to more than 3 percent of GDP, and their indebtedness to the NCB represented more than one third of the total loan portfolio of that institution. The financial position of the Central Water Authority also has weakened in recent years as water user charges have not kept pace with costs.

During the period 1982-83, the commercial banks' net domestic credit expanded at a faster pace than their liabilities to the private sector, resulting in a substantial deterioration in their net foreign assets position. The growth in private sector deposits has been

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1/ The consolidated public sector comprises the Central Government, the Kingstown Board, the National Provident Fund, and eleven nonfinancial public enterprises.

Table 2. St. Vincent and the Grenadines:
Operations of the Consolidated Public Sector

	Fiscal Year Beginning July 1					
	1979	1980	1981	1982	Prel. 1983	Proj. 1984
	(In millions of Eastern Caribbean dollars)					
Current revenue	46.3	47.3	60.1	73.2	84.1	92.5
Current expenditure	41.4	48.1	63.5	70.9	80.3	88.6
Public sector saving	4.9	-0.8	-3.4	2.3	3.8	3.9
Central Government	3.4	-2.8	-4.4	2.3	1.3	0.2
Rest of general government	3.7	3.8	4.5	4.3	5.6	7.0
Public enterprises	-2.2	-1.8	-3.5	-4.3	-3.1	-3.3
Capital expenditure	15.4	40.1	22.4	27.6	20.4	45.4
Central Government	8.0	13.7	16.0	20.0	9.7	18.8
Rest of general government	0.2	0.4	0.2	0.2	0.3	0.3
Public enterprises	7.2	26.0	6.2	7.4	10.4	26.3
Overall deficit before grants (-)	-10.5	-40.9	-25.8	-25.3	-16.6	-41.5
Grants	6.3	14.8	13.9	14.8	8.2	14.6
Overall deficit after grants (-)	-4.2	-26.1	-11.9	-10.5	-8.4	-26.9
Central Government	1.3	-8.2	-7.6	-5.5	-1.0	-8.0
Rest of public sector	-5.5	-17.9	-4.3	-5.0	-7.4	-18.9
Financing	4.2	26.1	11.9	10.5	8.4	26.9
External (net)	5.7	24.3	4.1	6.2	4.8	18.5
Domestic banks (net)	1.1	-0.4	5.3	4.6	3.6	-0.4
Other domestic financing	-2.6	2.2	2.5	-0.3	--	8.8
	(As percent of fiscal year GDP)					
Current revenue	31.1	26.6	28.6	31.0	32.2	32.2
Current expenditure	27.8	27.1	30.2	30.0	30.8	30.9
Public sector saving	3.2	-0.5	-1.6	1.0	1.5	1.4
Capital expenditure	10.3	22.6	10.6	11.7	7.8	15.8
Overall deficit (-)						
Before grants	-7.0	-23.0	-12.3	-10.7	-6.4	-14.5
After grants	-2.8	-14.7	-5.7	-4.4	-3.2	-9.4

Sources: Ministry of Finance; and Fund staff estimates.

inhibited by the rigidity of the interest rate structure. Most loans are subject to a ceiling of 12 1/2 percent (14 1/2 percent for consumer loans of less than EC$14,500). In addition, commercial banks are subject to a 2 percent tax on deposits, which they are not permitted to write off against their income tax liability. While lending rates are near the legal ceiling, rates on savings and time deposits paid by most private commercial banks are generally below comparable rates offered by commercial banks in other Eastern Caribbean Central Bank (ECCB) member countries. Until recently, the NCB was exempt from the legal reserve requirement imposed by the Government and from the 2 percent tax on deposits, which allowed it to pay higher deposit rates than its competitors. However, the NCB, like other commercial banks, will be subject to the 6 percent reserve requirement recently established by the ECCB, although it has been granted until March 15, 1987 to discharge this obligation in full.

In 1982 the deficit in the current account of the balance of payments widened to 14 percent of GDP (from 8 1/2 percent of GDP the previous year) due mainly to a decline in net receipts from tourism and other services, and a reduction in exports of arrowroot and bananas (Table 3). A recovery in banana exports and tourism in 1983, coupled with an increased inflow of private transfers, contributed to a reduction in the current account deficit to less than 8 percent of GDP. In both years the current account deficits were almost fully offset by official and private capital inflows; therefore, the external overall balance was roughly in equilibrium.

St. Vincent and the Grenadines' foreign debt is mainly on concessionary terms and has increased modestly from US$16 million at the end of 1980 to US$20 million at the end of 1983; in relation to GDP, outstanding indebtedness has declined from 27 percent at the end of 1980 to less than 23 percent at the end of 1983. Debt service in 1983 represented 2 1/2 percent of earnings from exports of goods and services and about 5 percent of the public sector's current revenues.

II. Economic Policies

At the conclusion of the 1982 Article IV consultation with St. Vincent and the Grenadines, Executive Directors emphasized the need to strengthen public sector savings through restraint in current expenditure, in order to support planned increases in public investment. They also expressed concern over the liquidity position of the NCB, urged the authorities to raise the ceilings on interest rates, and encouraged them to review exchange rate policies with the other members of the ECCB. Action along the lines recommended by the Fund has been limited since the last consultation, and the discussions focused mainly on these issues.

Table 3. St. Vincent and the Grenadines: Summary Balance of Payments

	1979	1980	1981	1982	Est. 1983	Proj. 1984
	(In millions of U.S. dollars)					
Current account	-6.4	-13.2	-6.1	-11.4	-7.2	-7.2
Trade balance	-27.2	-36.0	-28.4	-29.3	-29.4	-32.6
Exports, f.o.b.	(19.1)	(21.1)	(29.8)	(34.3)	(42.0)	(43.9)
Imports, c.i.f.	(-46.3)	(-57.1)	(-58.2)	(-63.6)	(-71.4)	(-76.5)
Service balance	7.5	10.6	10.2	5.6	7.0	8.6
Travel receipts (net)	(9.0)	(12.5)	(12.6)	(9.6)	(10.0)	(11.8)
Other services	(-0.9)	(-1.0)	(-1.7)	(-2.2)	(-1.4)	(-1.6)
Interest on public debt	(-0.4)	(-0.7)	(-0.9)	(-0.9)	(-0.9)	(-1.0)
Investment income	(-0.3)	(-0.6)	(-0.3)	(-1.8)	(-1.8)	(-1.8)
ECCB profits	(0.1)	(0.4)	(0.5)	(0.9)	(1.1)	(1.2)
Private transfers (net)	13.3	12.2	12.1	12.3	15.2	16.8
Capital account	6.6	12.7	4.5	10.7	7.1	8.0
Official grants	2.8	3.9	5.3	5.3	4.2	4.2
Public borrowing (net)	2.2	4.4	2.7	2.3	2.6	2.4
Commercial banks (net)	-2.1	1.6	-2.0	6.4	-1.4	1.2
Private direct investment	0.6	1.1	0.5	0.6	3.0	2.0
Other (including errors and omissions)	3.1	1.7	-2.0	-3.9	-1.3	-1.8
SDR allocation	--	0.2	0.2	--	--	--
Overall balance	0.2	-0.3	-1.4	-0.7	-0.1	0.8
Financing	-0.2	0.3	1.4	0.7	0.1	-0.8
IMF	--	0.5	1.6	--	--	-0.5
ECCB	--	--	--	0.9	0.3	--
Change in foreign assets	-0.2	-0.2	-0.2	-0.2	-0.2	-0.3
	(In percent of GDP)					
Trade balance	-52.4	-61.4	-38.9	-35.3	-32.0	-32.1
Current account	-12.3	-22.2	-8.4	-13.8	-7.8	-7.1
Overall balance	0.4	-0.5	-1.9	-0.8	-0.1	0.8
Memorandum item						
GDP (in millions of U.S. dollars)	51.9	58.6	73.0	82.9	91.9	101.5

Sources: Statistical Unit, Ministry of Finance; Eastern Caribbean Central Bank; Tourist Board; and Fund staff estimates.

1. Development strategy

The Government's public investment program--which is still under discussion--envisages a substantial increase in capital outlays in FY 1984/85 and subsequent years. The most important item in the program is an integrated power project aimed at increasing hydroelectric capacity, rehabilitating existing facilities, and installing new transmission and distribution lines. The authorities also intend to expand construction of new factory shells and to continue their support for agricultural activities by direct lending and by improving feeder roads and port facilities. A substantial part of the investment program is financed from abroad. In particular, the US$34 million power project will be cofinanced by the International Development Association, the European Investment Bank, the Caribbean Development Bank, the Canadian International Development Agency, and the United States Agency for International Development. However, the multi-year investment program also includes outlays for schools and other social-oriented projects which require substantial domestic counterpart contributions. The locally financed portion of the investment program in FY 1984/85 is estimated at 17 percent of the total.

2. Fiscal policy

Over the past few years, the Government has made substantial progress in strengthening the public finances, both by increasing public sector savings and by reducing the overall deficit. However, the growing operating deficits that persist in some of the state enterprises have limited the scope for larger public sector savings and have placed considerable strain on the liquidity of the NCB.

At the time of the mission, the authorities were initiating preparation of the budget for FY 1984/85. At their request, the staff made a projection for the public sector operations in FY 1984/85, including an initial assumption advanced by the authorities that civil servants' wages would be raised by 10 percent and allowing for a substantial increase in investment spending. This projection indicated that, in the absence of corrective measures, an unfinanced gap of EC$9 million (equivalent to 3 percent of GDP) would emerge in FY 1984/85. The authorities expressed concern about the magnitude of the imbalance projected by the staff and indicated their readiness to adopt measures aimed at reducing the fiscal gap, stimulating the generation of saving in the economy, and strengthening the balance of payments.

The authorities noted that the level of taxation, which had risen from 25 percent of GDP in FY 1980/81 to 30 percent in FY 1983/84, was very high and left limited scope for further tax increases. In fact, they were considering some tax reductions with a view to reducing disincentives to producers and stimulating the flow of financial savings into the commercial banks. Among the measures under consideration were a reduction in the tax on interest-bearing bank deposits from 2 percent to 1 percent and a reduction in the 3 percent turnover tax enacted in

1982, which has met considerable resistance from the business community. The authorities also indicated that the banks would be permitted to write off the remaining 1 percent tax on deposits against their income tax liabilities. In order to compensate for the loss of central government revenues that would result from these measures, the Government would consider increasing duties on imports of consumer goods, which at present are subject to duties that are among the lowest in the region.

Because of the relatively high tax burden, the authorities recognized that a reduction in the emerging fiscal imbalance would have to hinge mainly on expenditure containment. Given the substantial reduction in the rate of inflation in recent years, and the difficult fiscal outlook for the coming year, the authorities said that they would consider limiting the wage increases to civil servants in FY 1984/85 to no more than 5 percent, instead of the 10 percent increase initially envisaged. They also indicated that they would seek to hold central goverment outlays for purchases of goods and services below the FY 1983/84 level. Moreover, they noted that the operations of the Vehicle Funding Scheme--a motor pool administered by the Central Government for the use of ministries and public sector entities--would be rationalized in order to reduce its operating deficit.

Although the authorities were concerned with the financial imbalance of some of the state enterprises, they felt that the scope for maneuver was limited in this area. In the case of the Sugar Industry, it was noted that a more than doubling of the already high domestic price of sugar would be needed to eliminate the deficit of the enterprise. The Government could not at this time implement such a large revision in price, but would favor a more moderate increase. In order to reduce its deficit from the sugar refining operation, the Sugar Industry intended to install a new distillery to process molasses for rum. A loan for US$1.5 million had already been approved by the Caribbean Development Bank for that purpose. It was expected that profits from the sale of rum, together with some upward adjustment in the price of sugar, would permit the enterprise to reduce substantially its deficit.

The authorities were distressed by the collapse of the foreign market for arrowroot, a product with a long tradition which provided employment to many farmers. They had come to the conclusion that it was futile for the Arrowroot Industry Association to continue supporting production of arrowroot and accumulating inventories in anticipation of a market recovery, and had decided to authorize the selling of stocks at a loss to reduce carrying costs. The Government expects gradually to replace arrowroot cultivation with vegetables and other cash crops.

The authorities were confident that the financing gap projected by the staff for FY 1984/85 could be closed by containing central government current expenditures and by reducing the deficits of the sugar and arrowroot enterprises. However, if necessary, the Government also would be ready to cut back capital expenditures with a high local financing content. They acknowledged that a more permanent restructuring of the public sector finances would be needed to ensure a sustainable balance in the medium term, but the approach of elections limited the feasibility of more sweeping measures at this time.

3. Monetary policy

St. Vincent and the Grenadines shares a common central bank with six other states, which limits the scope for independent monetary policy. As noted, lending rates are subject to an official ceiling, and commercial banks are subject to a 2 percent tax on interest-bearing deposits. The authorities agreed with the staff that these two measures contributed to the relatively low interest rates paid to depositors. In order to allow for more interest rate flexibility, the authorities expressed willingness to raise the ceiling on interest rates by 3 to 4 percentage points (from the present ceiling of 12 1/2 percent applicable to most loans), in addition to reducing the tax on bank deposits. However, the adoption of these measures might be delayed pending the results of a study being conducted by the ECCB on the structure of interest rates in its member countries.

The authorities were concerned about the liquidity position of the state-owned NCB, which is the main source of domestic financing for the state enterprises. Until recently, the NCB had been able to finance a substantial portion of the deficits of the state enterprises from the growth in deposits of the National Provident Fund, which at the end of 1983 accounted for 43 percent of its total deposits. Moreover, because the NCB was exempt from reserve requirements (before the creation of the ECCB) and from payment of the tax on interest-bearing deposits, the deposit rates offered by the NCB were higher than those offered by other commercial banks; this resulted in a relatively faster expansion of the private deposit liabilities of the NCB. Having lost both of these advantages in early 1984, the already strained financial position of the NCB is bound to come under additional pressure. The authorities expect the proposed reduction in the deficits of the state enterprises to contribute to an improvement in the liquidity of the NCB.

4. Prices, wages, and employment

Price controls are in effect for petroleum products, utilities, and various basic commodities such as sugar, dairy products, and cooking oil. A number of imported goods are subject to maximum mark-ups ranging from 7 1/2 percent to 20 percent at the wholesale level and 11 1/2 percent to 40 percent at the retail level. Both administered prices and mark-up margins for imported goods are revised periodically, and are not believed to have resulted in distortions.

In order to achieve greater flexibility in wage negotiations with civil servants in FY 1984/85, the Government has decided to depart from the previous practice of negotiating wage contracts to cover several years; instead, it has decided to seek agreement on the basis of a single fiscal year. Since wage agreements in the Central Government have traditionally set the standard for wage increases in the rest of the economy, the Government's willingness to exercise greater restraint in increasing real wages for civil servants should help maintain the competitiveness of the economy.

Labor relations in both the public and private sectors have been harmonious in the past, and the small number of disputes generally have not been wage related. Labor union membership has increased in recent years but unionization has not penetrated significantly the key productive sectors, such as the enclave export-oriented industries, the sugar industry, and the flour mill. Nevertheless, wage awards in the non-unionized industries have not differed significantly from those in the unionized sector.

Labor turnover is reportedly high in the enclave-type industries but productivity appears to be benefiting from the on-the-job training programs being conducted by some foreign firms. As noted earlier, wage rates in this type of industries have remained competitive, notwithstanding the increase in real wages in recent years, and the Development Corporation (DEVCO)--which manages the industrial estates--reportedly has more applications for factory shells from interested foreign industrialists than there is available space at present.

5. External policies

St. Vincent and the Grenadines' external balance has strengthened considerably since 1980 when reconstruction-related imports caused the current account deficit to reach 22 percent of GDP. Prospects for banana exports and tourism appear to be good and, notwithstanding the uncertain outlook for arrowroot exports, the current account deficit is expected to narrow to 7 percent of GDP in 1984 from 8 percent in 1983. Net inflows of capital are expected to exceed the current account deficit in 1984, thus permitting a small surplus in the overall balance.

The Government is actively pursuing a policy of agricucultural diversification which would move St. Vincent and the Grenadines away from dependence on exports of traditional products such as arrowroot and bananas, to new products such as asparagus, tomatoes, and other vegetables. In this regard, technical and financial assistance was being negotiated with Taiwan for both the production and marketing abroad of such crops. In addition, the fishery sector is to be developed with technical assistance from the Food and Agriculture Organization. Also, the Government is actively promoting the development of new enclave export-oriented industries. Because of the small size of the domestic market, there is a limited scope for import substitution. However, the authorities noted that one of the main objectives of the power project was to develop sufficiently the hydroelectric potential to cover local demand, thus reducing the dependency on fuel imports.

Payments for imports are subject to approval by the Ministry of Finance, but are not restricted. Payments for certain invisibles are subject to limits, but allocations can be increased with the authorization of the Ministry of Finance. Mandatory surrender of foreign exchange earnings from exports and invisibles is in effect but enforcement is lax. All outward capital transfers require exchange control approval but, owing to the relative freedom of capital movements within the East Caribbean currency area, such approval has not restricted outward movements of capital.

As a member of the ECCB, the exchange rate of St. Vincent and the Grenadines' currency, the Eastern Caribbean dollar, can only be changed by unanimous agreement of member states. The Eastern Caribbean dollar has been pegged to the U.S. dollar at EC$2.70 per U.S. dollar since July 1976. Though the index of the real effective exchange rate (weighted by St. Vincent and the Grenadines' trade in goods and services, including tourism) has increased by 16 percent since 1980, the authorities noted that the prospects for manufacturing and tourism are favorable and they did not see a need for a modification of the exchange rate. They argued that tourism and exports of manufactures and nontraditional exports are affected more by quality, marketing arrangements, and available productive capacity than by the exchange rate. They pointed out that to restore international competitiveness for arrowroot and bananas (bananas are exclusively exported under preferential agreements to the U.K. market) would require a very large depreciation of the Eastern Caribbean dollar and were concerned about the implications of such a devaluation on domestic prices and therefore on wages. However, the authorities have joined with other member states in requesting the ECCB to conduct a study of the implications of the real appreciation of the Eastern Caribbean dollar for St. Vincent and the Grenadines as well as the other member states.

III. Staff Appraisal

The economy of St. Vincent and the Grenadines showed considerable resilience in recovering from the natural disasters that affected the country in 1979-80. Real GDP rose by 4 1/2 percent in 1983 led by growth in agriculture and tourism. Prospects for 1984 are for a similar rate of growth, reflecting an expansion in manufacturing output and construction activity and continued growth in agriculture and tourism. Inflation slowed considerably in 1982-83 owing to a moderation of the growth in domestic spending and the slowdown in the rate of increase in import prices. Notwithstanding the substantial increases in real wages in recent years, industrial labor costs remain relatively low and manufacturing activity--particularly in the enclave-type industries--has continued to expand, encouraged by good labor relations and attractive tax incentives. The public sector investment program is geared to the development of supportive infrastructure such as roads, ports, electricity, and factory shells, which is expected to provide a basis for a continued expansion of private sector activity.

In the last two years, public sector savings have improved noticeably, mainly reflecting the effects of the revenue measures adopted by the Central Government in 1981 and the increasing surplus generated by the National Provident Fund. Central government savings declined somewhat in FY 1983/84 but have remained positive, while the operating deficits of some of the public enterprises, particularly the Sugar Industry and the Arrowroot Industry Association, continued to be sizable nothwithstanding efforts to reduce their costs of production. To provide sufficient domestic financing for the ambitious public investment program for FY 1984/85 and subsequent years, it is essential that the savings performance of the Central Government be improved and the deficits of the sugar and arrowroot enterprises be reduced significantly. The staff underscores the importance of restraining the growth in central government current expenditures as a means of enhancing public sector savings, and would urge the authorities to keep the increase in wages for civil servants to amounts consistent with a strengthening of the public finances.

The staff considers the recent decision of the Government to sell accumulated arrowroot stocks to be appropriate, since a reduction of the arrowroot enterprise's indebtedness to the National Commercial Bank would help reduce the interest burden faced by the enterprise and improve the liquidity of the bank. More importantly, the staff would note that the operations of the enterprise will need to be scaled down over the medium term in order to avoid a continuing drain on the country's resources. Also, the staff is of the view that the domestic price of sugar should be raised without delay in order to reduce the deficit of the sugar enterprise. The need to reduce the net indebtedness of the sugar and arrowroot enterprises to the NCB has become more urgent since the NCB became liable to the ECCB for meeting legal reserve requirements and because of the recent government decision to lift the NCB's exemption from payment of the 2 percent tax on deposits.

The staff notes the intention of the authorities to raise the ceiling on interest rates and to eliminate, or substantially reduce, the existing tax on bank deposits. Such measures would strengthen incentives for savings and promote a better allocation of credit. Thus, the staff would advise the authorities to act soon in these areas.

In view of the increase in the index of real effective exchange rate in the past three years, the staff welcomes the government initiative in requesting the ECCB to study the implication of the appreciation of the Eastern Caribbean dollar for St. Vincent and the Grenadines and for the other ECCB member countries. In any event, the staff would stress that a restrained wage policy for civil servants, through its effects on wage behavior throughout the economy, would help maintain the competitive position of St. Vincent and the Grenadines.

It is recommended that the next Article IV consultation with St. Vincent and the Grenadines be held before February 1986.

St. Vincent and the Grenadines - Fund Relations
(As of May 31, 1984)

I. Membership Status

(a) Date of membership: December 28, 1979

(b) Status: Article VIII

(A) Financial Relations

II. General Department (General Resources Account)

(a) Quota: SDR 4.0 million

	Millions of SDRs	Percent of Quota
(b) Total Fund holdings of St. Vincent and the Grenadines currency	5.15	128.75
(c) Fund credit:		
Total	1.50	37.49
Of which: Credit tranche	0.20	4.99
CFF	1.30	32.50
(d) Reserve tranche position:	0.35	8.75

III. Current Stand-by and Special Facilities

(a) Current stand-by or extended arrangement: None

(b) Previous stand-by arrangement: on November 21, 1980, the Executive Board approved a purchase of SDR 0.425 million by St. Vincent and the Grenadines under the first credit tranche as emergency assistance following a hurricane disaster.

(c) Compensatory financing facility: on March 20, 1981, the Executive Board approved a purchase of SDR 1.30 million by St. Vincent and the Grenadines under the CFF.

IV. SDR Department

(a) Net cumulative allocation: SDR 0.35 million

(b) Holdings: SDR 4,855 or 1.37 percent of allocation

(c) Current designation plan: none.

V. Administered Accounts: None

VI. Overdue Obligations to the Fund: None

(B) Nonfinancial Relations

VII. Exchange rate arrangement: Since July 1976, the East Caribbean dollar has been pegged to the U.S. dollar at the rate of EC$2.70 per U.S. dollar.

VIII. Last Article IV Consultation: The last Article IV consultations were held in Kingstown from November 23 to December 10, 1982 and were concluded by the Executive Board on March 18, 1983.

IX. Technical Assistance: None

X. Resident Representative/Advisor: Mr. Andrew Gantt, the Fund's Regional Advisor who is stationed in Antigua and Barbuda, has been accredited to St. Vincent and the Grenadines since January 1984. He succeeded Mr. Samuel Stephens who was similarly accredited to St. Vincent and the Grenadines from January 13, 1982 to February 14, 1984.

St. Vincent and the Grenadines - Basic Data

Area and population	
Area	150 sq. miles (388 sq. kilometers)
Population (mid-1983)	114 thousand
Annual rate of population increase (1975-83)	1.9 per cent
GDP per capita (1983)	SDR 770.2
Origin of GDP at constant factor cost (1983)	(Percent)
Agriculture and fishing	18.6
Manufacturing	12.3
Construction	11.8
Transportation and communication	20.2
Government	19.2
Other	17.9
Ratios to GDP (1983)	
Exports of goods and nonfactor services	70.2
Imports of goods and nonfactor services	93.6
Central government revenue 1/	33.5
Central government expenditures 1/	33.8
External public and government-guaranteed debt	22.3
Gross domestic savings	9.4
Investment	32.0
Money and quasi-money (end of year)	44.3

Annual changes in selected economic indicators	1980	1981	1982	Prel. 1983
		(Percent)		
Real GDP per capita	2.6	7.1	0.8	2.4
Real GDP	4.5	9.0	2.7	4.3
GDP at market prices	12.8	24.6	13.6	9.1
Domestic expenditure (at current prices)	17.0	8.9	15.8	7.6
Investment	(29.1)	(4.0)	(6.7)	(13.7)
Consumption	(12.9)	(10.9)	(19.2)	(5.6)
GDP deflator	8.0	14.3	10.6	4.6
Consumer prices (average of period)	17.2	12.7	7.3	5.4
Central government revenues 2/	4.0	34.9	17.0	3.7
Central government expenditures 2/	21.9	29.2	17.8	-5.9
Money and quasi-money	6.9	15.2	7.5	10.5
Money	(2.4)	(17.5)	(4.4)	(4.9)
Quasi-money	(9.1)	(14.1)	(8.9)	(13.1)
Net commercial bank domestic assets 3/	15.4	6.2	29.1	8.6
Net credit to Central Government	(-7.4)	(2.4)	(8.5)	(-0.1)
Net credit to other public sector	(4.9)	(3.6)	(6.1)	(-0.5)
Net credit to private sector	(21.5)	(6.7)	(13.5)	(18.8)
Merchandise exports (f.o.b., in U.S. dollars)	10.5	41.2	15.1	22.4
Merchandise imports (c.i.f., in U.S. dollars)	23.3	1.9	9.3	12.3
Travel receipts (gross, in U.S. dollars)	30.5	6.6	-3.4	5.8

Central government finances 2/	1980	1981	1982	Prel. 1983
	(millions of Eastern Caribbean dollars)			
Current revenues	44.1	57.9	70.5	78.4
Current expenditures	46.9	62.3	68.2	77.1
Current account balance	-2.8	-4.4	2.3	1.3
Capital expenditures	13.7	16.0	24.0	9.7
Overall balance before grants	-16.5	-20.4	-21.7	-8.4
Capital grants	8.3	12.8	12.2	7.4
Overall balance after grants	-8.2	-7.6	-9.5	-1.0
Foreign financing	8.5	2.0	4.0	-1.6
Domestic financing	-0.3	5.6	5.5	2.6
Balance of payments	(millions of U.S. dollars)			
Merchandise exports (f.o.b.)	21.1	29.8	34.3	42.0
Merchandise imports (c.i.f.)	-57.1	-58.2	-63.6	-71.4
Travel receipts (net)	12.5	12.6	9.6	10.0
Private transfers (net)	12.0	12.5	13.0	16.0
Other services	-1.7	-2.8	-4.7	-3.8
Current account balance	-13.2	-6.1	-11.4	-7.2
Official transfers and capital (net)	8.3	8.0	7.6	6.8
Private capital (net)	2.7	-1.5	7.0	1.6
Errors and omissions	1.7	-2.0	-3.9	-1.3
SDR allocation	0.2	0.2	--	--
Overall balance	-0.3	-1.4	-0.7	-0.1

1/ FY 1983/84.
2/ Fiscal year beginning July 1 of the year mentioned.
3/ In relation to liabilities to the private sector at the beginning of the period.