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**Statement by Mr. Sadun and Ms. Marchitto on Eastern Caribbean Currency
Union--2007 Discussion on Common Policies of Member Countries
(Preliminary)
Executive Board Meeting 08/11
February 4, 2008**

We thank the staff for an excellent set of papers and Mr. Fried and Ms. Morgan for the additional information provided in their detailed and eloquent Buff statement.

Growth Outlook

We concur with the staff's soft-landing scenario, and we particularly value the well-balanced analysis of the downside risks to the outlook. The fact that the authorities are cognizant of these risks, most of which are inherent to the very nature of these small and open island economies, bodes well for their commitment to pursuing the reforms needed to enhance the growth potential and the resilience of ECCU economies, by means of productive capacity diversification, greater competitiveness, and a more business-friendly environment.

We value the staff analysis of the sustainability of the large CAD, also in relation to the evolution of the REER, and we tend to agree with their assessment. We nonetheless consider that external imbalances exceeding 20 percent of GDP deserve continuous and close monitoring, especially in association with high public debt and in the context of a currency board arrangement.

Fiscal Policy

In light of the above-mentioned vulnerabilities, it is somewhat disappointing that strong GDP growth along with commendable reform of the tax system failed to deliver a marked improvement in the fiscal position of ECCU countries. Moreover, we note that fiscal deficits are largely structural (Figure 4), and while public debt has declined over the past few years, it remains high and very costly to service. This in turn, leaves little room for scaling up spending in other key areas (social programs, poverty-reducing expenditure, infrastructure investment). In this regard, the timely implementation of the ECCB's revised fiscal benchmarks -- by establishing a clear and simple link between medium-term benchmarks and

annual budget targets -- would be a crucial step forward. While fiscal discipline is a pillar to macroeconomic stability, whichever the exchange rate regime of the authorities' choosing, it becomes absolutely indispensable for countries participating in a currency union and abiding by a currency board.

On the revenue side, we are encouraged to hear that the authorities are aware of the distortionary impact of tax incentives as well as of their fiscal cost, and are willing to consider the staff's suggestions to aim for greater transparency and harmonization across the region. In this connection, we join the staff in stressing the importance of preserving the integrity of the newly-introduced VAT regimes.

The authorities' intention to improve debt management are undoubtedly well considered and commendable, but we are afraid that sound debt management can only be complementary to fiscal consolidation in any strategy aiming to significantly reduce public debt.

Monetary Policy and the Financial Sector

Against the backdrop of robust economic growth, and despite rising oil and food prices, the ECCB has been successful in maintaining low inflation. In fact, the monetary authorities deserve credit for prudently managing reserve coverage, thus contributing to both price and exchange rate stability.

The strengthening of banking supervision is also praiseworthy, although we note that enforcement remains weak according to the staff. In the context of rapidly expanding credit to the private sector, low provisioning for NPLs, high exposure of banks to the public sector and tightening liquidity worldwide, continued efforts -- along the lines recommended by the staff -- are necessary. Moreover, aligning prudential regulation of off-shore and on-shore financial institutions, improving supervision of cross-border financial movements, and strengthening and unifying the supervision of the non-bank financial sector, is crucially important to contribute to the soundness and transparency of the entire system.

With these remarks, we wish the authorities of the ECCU countries continued success in meeting the challenges ahead.