April 14, 2020
Approval: 4/21/20

INTERNATIONAL MONETARY FUND

Minutes of Executive Board Meeting 19/12-2

2:30 p.m., February 15, 2019

2. St. Vincent and the Grenadines—2018 Article IV Consultation

Documents: SM/19/23 and Correction 1 ; and Supplement 1; and Supplement 2; and Supplement 3

Staff: Ishi, WHD; Goodman, SPR

Length: 36 minutes

Executive Board Attendance

M. Furusawa, Acting Chair

Executive Directors	**Alternate Executive Directors**
	J. Garang (AE), Temporary
	S. Bah (AF), Temporary
	J. Di Tata (AG)
	G. Johnston (AP)
	P. Fachada (BR)
	Y. Zhao (CC), Temporary
	J. Rojas (CE), Temporary
L. Levonian (CO)	
	C. Just (EC)
	A. Castets (FF)
	U. Fritsch (GR), Temporary
S. Gokarn (IN)	
	I. Lopes (IT), Temporary
	N. Komura (JA), Temporary
	M. Saadaoui (MD), Temporary
	P. Al-Riffai (MI), Temporary
	V. Rashkovan (NE)
	S. Evjen (NO), Temporary
	Z. Smirnova (RU), Temporary
	R. Alkhareif (SA)
	R. Pandit (ST), Temporary
P. Inderbinen (SZ)	
	A. Clark (UK), Temporary
	M. Svenstrup (US), Temporary

G. Tsibouris, Acting Secretary
J. Morco, Summing Up Officer
E. Mannefred, Board Operations Officer
M. McKenzie, Verbatim Reporting Officer

Also Present
Strategy, Policy, and Review Department: M. Goodman. World Bank Group: D. Boskovski. Western Hemisphere Department: L. Bonato, L. Castellanos Garcia, K. Ishi, J. Moeller, M. Rosales Torres.

Senior Advisors to Executive Directors: N. Jost (NE), R. Morales (AG), E. Rojas Ulo (AG).
Advisors to Executive Directors: T. Manchev (NE), M. Sylvester (CO), A. Zaborovskiy (EC).

2. ST. VINCENT AND THE GRENADINES—2018 ARTICLE IV CONSULTATION

Ms. Levonian and Mr. Williams submitted the following statement:

Our St. Vincent and the Grenadines (SVG) authorities highly appreciate the Fund's continued support and thank staff for the productive engagement during the Article IV consultations. They welcome the report, value staff's advice, and appreciate the report's acknowledgement of noteworthy macroeconomic progress. That said, our authorities are of the view that the report could better highlight advances on structural reforms.

The government remains focused on transforming SVG into a more vibrant, competitive, and inclusive economy. In line with this objective, SVG will accelerate policies geared toward furthering fiscal consolidation, enhancing the business environment, and strengthening resilience to natural disasters and climate change. These efforts, to be accompanied by measures to bolster social protection, will be instrumental in diversifying the economic base and stimulating private-sector led job-rich growth.

Recent Economic Developments

Economic expansion continues to strengthen while inflation remains benign. Preliminary estimates point to an acceleration of growth in 2018 to 2.5 percent from an average annual growth rate of 0.8 percent over the previous three years. Growth was hampered in 2016 and 2017 by the closure of the island's largest hotel and adverse weather conditions - flooding and landslides. Underpinning the growth uptick was the strong performance of tourism and construction. The opening of the new Argyle International Airport in early 2017 - an important pillar of the economic transformation process - buoyed tourism flows. SVG also benefited from increased demand for construction materials by Dominica following Hurricane Maria in 2017. At the same time, higher commodity and fuel prices led to an uptick in average inflation to just over 2 percent, following years of deflation.

Fiscal performance supported debt reduction objectives. The primary balance remained in surplus and contributed to a reduction in public debt to an estimated 73 percent of GDP in 2018 from over 82 percent in 2016. Revenue collections were behind budget, however, restraint in current spending and under-execution of capital programs resulted in an estimated overall fiscal deficit of 2.0 percent of GDP, compared to the budgeted 6.7 percent.

Our authorities have advanced efforts to safeguard the stability of the financial sector. The sector remains broadly stable, but concerns linger about the loss of correspondent banking relationships (CBR), and de-risking more broadly. Notable progress in addressing AML/CFT deficiencies included amendments to several pieces of legislation and ongoing work on the National Risk Assessment (NRA). Of note, banks maintained high capital ratios while NPLs continued to decline and remained below the ECCU average.

Economic Outlook & Policies

Steady and sustained implementation of credible policies remain key to strengthening, diversifying, and inclusively growing the SVG economy. While our authorities consider the outlook to be favorable, they remain fully aware that SVG, like many small island states, is highly susceptible to external shocks and adverse weather conditions. Building on steps already taken to improve its ability to respond to natural disasters, enhance human capital, and upgrade the physical and legislative infrastructure, the government will continue to advance a multi-pronged approach geared toward tackling vulnerabilities and transforming the economy.

The growth outlook is positive but there are downside risks. Real economic output is estimated to grow at 2.5 percent for 2018 and slightly higher over the medium term. Our authorities are nevertheless mindful of inherent risks from, inter alia, natural disasters, higher commodity prices, and weaker than expected global growth. The new climate-resilient international airport has improved connectivity and is expected to further boost tourist arrivals and seafood exports, with positive spillovers to connected sectors. Significant private investment to boost hotel room stock, as well as large public infrastructure projects, including those related to climate change and upgrading of the road network, geothermal energy, and port facilities provide the impetus for stronger growth.

Fiscal Policy and Debt Management

Fiscal policy will be shrewdly managed within the context of achieving the ECCU debt/GDP target of 60 percent by 2030 while supporting economic transformation. Our authorities agree in principle with staff's suggestion that accelerating fiscal consolidation will help to build buffers and reduce debt faster. However, this must be carefully balanced against the need to stimulate higher levels of growth and reduce high unemployment and poverty. In this regard, the 2019 budget forecasts a significant scaling up of capital expenditure. While this may cause the public debt to rise in the near

term, the magnitude of increase would be moderated by faster growth and planned measures to boost revenue and contain current spending. The medium-term fiscal framework (MTFF) that informs the 2019 budget contains critical growth-friendly projects to be completed over the next two to three years. These include climate change-related projects that account for close to 40 percent of the capital budget, port modernization, and the geothermal plant, which on completion is expected to raise renewable energy usage to about 80 percent. Given the expected growth dividend alongside improved fiscal performance, our authorities are confident of remaining on course with the 2030 Debt/GDP target.

Efforts will be stepped up to drive ongoing and planned fiscal reforms. The government's MTFF that underpinned this year's budget will be tabled in Parliament shortly. Going forward, the MTFF will be the cornerstone of future budgets. Measures to mobilize revenue are underway with plans to table the Tax Administration and Procedures Act in Parliament during the first quarter of 2019. The proposed changes will considerably close tax loopholes currently being exploited by corporates. Additionally, regulations will be promulgated to enhance operations and oversight of SOEs. Pension reform also forms a critical part of our authorities' program to contain current spending and discussions surrounding the design of a scheme are advancing.

Financial Sector

Actions to bolster financial system stability will intensify. Recent legislative enhancements have yielded a more robust AML/CFT regime. Nevertheless, our authorities will continue to work assiduously to ensure that the framework remains compliant with international standards and commit to completing the NRA by September this year. Following good progress in the stress testing of credit unions, the FSA will extend the exercise to the insurance sector. Our authorities are seized with the urgency of strengthening vigilance over the financial sector. In this regard, an adequately-resourced FSA remains a priority, and the government will enact legislation to bolster the FSA's enforcement powers. The government also continues to collaborate with the ECCB as part of an ongoing regional initiative to establish a modern credit reporting system. Our authorities acknowledge that there are scale economies from consolidation and, in this context, they will pursue strategies for amalgamating small local banks, including within the wider ECCU region.

Structural Reforms

Our authorities will accelerate implementation of reforms to expand growth potential. SVG has implemented some key reforms to strengthen fiscal management and enhance financial sector supervision, but a lot more is required for the country to take advantage of existing and potential opportunities. The new international airport with direct flights to main source markets has expanded tourism prospects. To capitalize on these opportunities, our authorities will forge closer linkages between tourism and other sectors, particularly agriculture. The geothermal plant promises lower electricity costs, which will enhance competitiveness. However, the quality of the physical and human infrastructure needs to keep pace with these developments. Against this backdrop, the government is taking decisive steps to accelerate project implementation with donor support. They will also move with dispatch to review the current procedural and legislative framework for investment with a view to simplifying the requirements. To ensure that the workforce is in sync with labor market demands, the government will provide additional resources to expand skills training in the technical and vocational areas. These activities are all crucial to stimulate private sector investment and generate jobs in various sectors of the economy.

Social protection remains a priority for the government. Broad-based support is integral to the success of the reform agenda. To ensure that all Vincentians benefit from the economic transformation, our authorities endeavor to protect social spending, including intensifying targeted support toward gender development, childcare, and youth empowerment.

Strengthening Resilience to Natural Disasters and Climate Change

Our authorities consider natural disasters and climate change to be their most formidable near-and long-term threats. They appreciate staff's tailored stress tests incorporating natural disasters into the DSA. Strengthening resilience will provide important growth and fiscal dividends. The establishment of a Contingencies Fund in 2017, strictly for funding expenses related to natural disasters, was an important step in this regard. Moreover, the 2019 budget includes a sizeable allocation to climate-related projects, including allocations to the Natural Disaster Management and the Regional Disaster Vulnerability Reduction projects amounting to about 2 percent of GDP. This is further demonstration of the significance that the government attaches to resilience building.

Mr. Fachada and Ms. Mohammed submitted the following statement:

We thank staff for the report and Ms. Levonian and Mr. Williams for their statement. We commend the authorities for the recent economic performance of St. Vincent and the Grenadines and take note of the encouraging acceleration of GDP growth in 2018 to 2.5 percent, from an annual average of just 0.6 percent over the previous four years. Despite positive developments, St. Vincent and the Grenadines continues to face challenges in achieving sustainable growth, building fiscal buffers, bolstering resilience to natural disasters and ensuring financial stability.

Sound fiscal consolidation is necessary to achieve the debt target of 60 percent of GDP by 2030. We commend the authorities for curbing expenditure to limit the public deficit to 2 percent of GDP since 2015, despite significant pressures on capital spending. This notwithstanding, we are concerned about the larger-than-expected revenue loss in 2018 due to the reduction in the corporate and personal income tax rates. Further, we agree with staff that more ambitious fiscal consolidation would be required to achieve the debt target of 60 percent of GDP by 2030. Accordingly, we encourage the authorities to take additional revenue and expenditure measures, including strengthening of revenue administration, reduction of tax exemptions, restraining the wage bill and improving the sustainability of the public pension system.

The establishment of the Contingency Fund to bolster resilience to natural disasters and climate change is a step in the right direction. We take positive note that the Fund is being capitalized by the increase of the standard VAT rate and of the VAT rate for tourism-related activities, and by the introduction of a climate resilience hotel levy. We agree with staff that the Contingency Fund's governance and operational framework should be legislated to ensure accountability, transparency and effectiveness. With respect to staff's recommendation to allocate additional expenditure reserves for emergency operations, we have sympathy for the views of the authorities that additional expenditure measures would be burdensome, particularly with the existing fiscal challenges to meet the debt-to-GDP target.

The Financial Services Authorities (FSA) should advance the ongoing financial reform initiatives and fortify its regulatory and supervisory efforts to safeguard financial stability**.** We encourage the authorities to strengthen financial stability by approving and implementing the laws that are still pending. The stability risk that may arise from the rapid growth of loans by credit unions, which in part reflects a shift of borrowers away from banks, is a

cause for concern. Accordingly, we urge the authorities to ensure the enforcement of prudent standards and the maintenance of sound risk management in the segment. Moreover, we welcome the implementation of IFRS 9 and the development of a crisis management framework for the non-bank financial sector. We also welcome the initiation of the National Risk Assessment to strengthen the current AML/CFT framework.

Structural reforms to capitalize on growth opportunities are welcomed. We agree that the investment environment could be improved by streamlining the procedural and legislative requirements into one law under the oversight of a single agency. Also, there is merit in developing an infrastructure plan with the key stakeholders to prioritize projects consistent with the authorities' strategic development goals. This not only boosts donors' support and increase investors' interest, but it reduces wasteful use of resources. Finally, we welcome the construction of the geothermal electricity project, as it promises to reduce the dependence of imported fuel and enhances energy security.

Mr. Villar and Mr. Rojas Ramirez submitted the following statement:

We thank staff for its informative and comprehensive report and Ms. Levonian and Mr. Williams for their insightful buff statement.

St. Vincent and the Grenadines experienced a significant rebound in economic activity in 2018, when the country reached a GDP growth of 2 percent according to the staff report. As mentioned in the buff, more recent estimates suggest that this number could have been even larger, close to 2.5 percent, which in any case compares very favorably with a yearly average of 0.6 percent between 2010 and 2017. We welcome policy actions oriented at fostering growth and enhancing economic performance. The government has accomplished the upgrade of airport infrastructure with high impact on the tourism sector. Nevertheless, more efforts are necessary to make growth sustainable over the longer term. Authorities are committed to improving private sector expansion, promoting investment and strengthening human and physical capital. We welcome staff's recommendation on initiatives for fostering private sector participation, improving the investment environment and strengthening human and physical capital, while creating the required conditions to face natural disaster risks. We encourage authorities to take further actions to diversify the economy by improving productivity in the agriculture and fishery sectors and strengthening the institutional fiscal framework.

On the fiscal policy front, we welcome staff's recommendation on a risk-based approach for building buffers to cover natural disasters expected costs. Legislation to ensure the effectiveness and transparency of the Contingency Fund is important. Also, we agree on measures to broadening the tax base and reforming pension funds, prioritizing development projects and containing procurement cost. Authorities are committed to strengthening revenue administration, the fiscal framework, and fiscal institutions and processes for underpinning stability and inclusive growth. We commend reforms on revenue administration such as the implementation of the Tax Administration Procedures Act (TAPA) and the submission of the Medium-Term Fiscal Framework (MTFF) initiative along with the 2019 budget to parliament. We encourage authorities to continue working on the implementation of these reforms and on the establishment of a cash management system and a Cash Management Committee. We agree with staff that the Government's plan to strengthen the oversight of State-Owned Enterprises (SOEs) should be accompanied by putting in place a legal and institutional framework to assess potential risks pertaining to Public-Private Partnerships (PPPs).

The financial system risk indicators are according to the Eastern Caribbean Central Bank (ECCB) standards. Nevertheless, non-bank institutions present vulnerabilities. The NPLs have been declining but they are still above ECCB requirements. Against this backdrop, we welcome the authorities' commitment to strengthening oversight of the bank and non-bank financial sector, developing crisis management instruments, and establishing the National Risk Assessment framework. The approval of the Financial Services Authority (FSA) regulations is critical to help prudential enforcement requirements and to preserve system soundness. We concur with staff on making further efforts for improving the regulatory and supervisory framework. We see progress in improving legal deficiencies in the AML/Framework and commend authorities for completing the National Risk Assessment for ensuring the effectiveness of AML/CFT preventative measures.

Mr. Di Tata and Mr. Rojas Ulo submitted the following statement:

We thank staff for the comprehensive report and Ms. Levonian and Mr. Williams for their informative buff statement.

The main challenge faced by St. Vincent and the Grenadines' economy is to sustain the growth momentum over the long term. The economy had a weak performance after the global financial crisis but has

rebounded since mid-2017, following the opening of the Argyle International Airport. Real GDP growth could increase to 2½ percent in 2018, from an average of 0.8 percent over the previous three years. Notwithstanding this positive development, GDP per capita is still the lowest in the ECCU and the unemployment rate remains high at around 20 percent. Moreover, the country has a narrow production and export base and a high current account deficit, and it is highly exposed to natural disasters and external shocks. Assuming the continuation of sound policies, the staff projects that real GDP growth could be sustained at around 2.3 percent over the medium term owing to an increase in tourism-related activities, a gradual pick up in non-traditional crops and fisheries, and a boost in construction on new hotels and resorts. Against this backdrop, the Article IV consultation rightly focused on policies to achieve stronger and sustainable growth, build fiscal buffers, increase resilience to natural disasters, and ensure financial stability.

We welcome the authorities' recent efforts at fiscal consolidation, as well as their commitment to bring the debt-to-GDP ratio down to the ECCU regional goal of 60 percent by 2030. The authorities' efforts to mobilize revenue and contain expenditures led to a shift in the overall fiscal balance from a deficit of 3.4 percent of GDP in 2009-15 to an average surplus of ¼ percent of GDP in 2016-17, which is commendable. Looking ahead, based on the report's baseline scenario, the primary balance is expected to improve from 0.6 percent of GDP in 2018 to 1.1 percent over the medium term, which would permit achieving the 60 percent debt goal by 2030. Although further fiscal adjustment would be desirable to deal with downside risks, we agree with Ms. Levonian and Mr. Williams' buff statement that an acceleration of fiscal consolidation must be carefully balanced against the need to stimulate growth and reduce high unemployment and poverty. In this regard, we welcome the authorities' intention to close tax loopholes through the Tax Administration and Procedures Act, promulgate regulations to enhance the oversight of SOEs, and advance on the design of pension reform. In addition to these measures, we encourage the authorities to consider further measures to broaden the tax base, strengthen tax administration, and limit the growth of the wage bill (which is the highest among ECCU members). Could staff comment on the incidence of poverty and the existing social protection programs, as well as on the authorities' plans to intensify targeted support for gender development, childcare, and youth unemployment, as mentioned in the buff statement? We take positive note of the authorities' plans to submit the MTFF underpinning the 2019 budget to Parliament shortly.

The establishment of the Contingency Fund in 2017 was an important step towards protecting the public finances from natural disaster risks.

Looking forward, a specific legal framework dealing with the fund's governance and operations is necessary to ensure effectiveness. Moreover, we encourage the authorities to review the National Emergency and Disaster Act, conduct a national risk assessment for natural disasters, and provide adequate resources to the National Emergency Management Office. The inclusion of a sizeable allocation for climate related projects in the 2019 budget is noteworthy. Could staff elaborate on the support provided by donors in the past to deal with natural disasters?

The financial system remains broadly stable, but further efforts are needed to improve the regulatory and supervisory framework. Regarding commercial banks, the indicators for capital adequacy and liquidity are robust, but profitability remains volatile and nonperforming loans (NPLs) are still relatively high. At the same time, credit unions appear to be adequately capitalized but rapid credit growth in recent years raises concerns about their ability to monitor and manage credit risk. Could staff comment on the reasons behind the rapid growth in credit provided by these institutions in recent years? We welcome the steps taken to strengthen the FSA supervisory toolkit, including the introduction of stress testing for credit unions, but concur with staff that further efforts are needed to enhance non-bank supervision and improve stress-testing and financial stability assessments. It is also important to obtain prompt approval of pending legislation to help the FSA enforce prudential requirements and intervene problem institutions, and to develop a crisis management plan for the non-bank financial sector. Regarding AML/CFT, we welcome the actions taken last year to address many of the deficiencies identified in the 2010 FATF recommendations and encourage the authorities to ensure the effectiveness of AML/CFT preventive measures and to complete the National Risk Assessment initiated in 2017.

We fully agree that a renewed push on the structural front is needed to raise St. Vincent and the Grenadines' growth potential. This requires the implementation of structural reforms to foster the business environment, make infrastructure more resilient against natural disasters, and support increased productivity. In this regard, the development of the geothermal power plant is an important project that would help reduce dependence on imported fuels and enhance productivity over the medium term. We encourage the authorities to move ahead with their plans to streamline the approval process for foreign investment, including by consolidating procedural and legislative requirements in one standalone investment act. Efforts should also continue to strengthen human capital and improve productivity in the agriculture and fishery sectors to promote a more diversified and inclusive economy.

With these comments, we wish St. Vincent and the Grenadines and its people every success in their future endeavors.

Mr. Inderbinen, Mr. Kaya, Mr. Just, Mr. Imashov and Mr. Zaborovskiy submitted the following joint statement:

We thank staff for the insightful papers, and Ms. Levonian and Mr. Williams for their helpful buff statement. Like many small island economies, St. Vincent and the Grenadines is facing significant structural and climate-related challenges, and remains highly dependent on cyclical tourism revenues. We commend the authorities for making progress in addressing these challenges, broadly in line with recommendations of previous Article IV consultations. However, more remains to be done to reduce the risk of debt distress and to strengthen the external and fiscal positions. We broadly agree with the thrust of the staff report and would like to make the following points for emphasis.

Fiscal reforms to broaden the tax base, strengthen revenue administration, improve spending efficiency, and implement a medium-term fiscal framework remain critical to sustain the path of debt reduction. We encourage the authorities to undertake a more active fiscal adjustment in a growth-friendly manner, as well as to advance the pension reform without delay. Staff's analysis shows that the total effects from the possible tax and expenditure measures could reach 2.3 percent of GDP, which leaves the authorities with some room for maneuver in calibrating an economically and politically feasible fiscal package. We also note the rising costs of the weather-related disasters, which underline the importance of contingency fiscal planning. We welcome the establishment of the Contingency Fund and call on the authorities to steadfastly advance and strengthen the weather-related risk preparedness framework. We also agree with staff that additional efforts are needed to clear the existing budgetary arrears and resolve classification issues in this area. Could staff clarify how these arrears are reflected in the public debt data?

Financial stability risks should be vigorously addressed by enhanced supervision and regulation. In recent years, staff has consistently pointed to the financial risks stemming from the fast-growing lending by credit unions. We note that most credit unions appear adequately capitalized with a small amount of non-performing loans, and we acknowledge the authorities' recent initiatives to strengthen the supervisory toolkit. However, heightened vigilance is needed, considering the well-known risk management capacity constraints inherent to some types of credit unions. Extending the boundaries

of financial supervision beyond the banking sector and ensuring appropriate accounting standards would also create a level playing field in the financial services market. We welcome the progress in improving the AML/CFT regime. We encourage the authorities to complete the National Risk Assessment as planned and to use the period until the next AML/CFT assessment to further advance the appropriate legislation and ensure enforcement. In this regard, we would be interested whether staff is supporting the authorities to model the impact of climate-related risks on financial stability and to stress test the short-term impact of a climate event on the balance sheets of financial institutions.

Structural reforms are key to sustain the current growth momentum and diversify the economy. We note that the authorities broadly agree with staff's recommendations on structural reforms. Attracting foreign direct investment and the responsible implementation of public-private partnership projects could play an important role in boosting St. Vincent and the Grenadines' economic potential.

With these remarks, we wish the authorities every success in their policy endeavors.

Mr. Obiora and Mr. Garang submitted the following statement:

We broadly agree with the thrust of the staff's appraisal and policy recommendations, which reflect St. Vincent and Grenadines' return to non-inflationary growth, albeit with a slightly weakened external position. These economic outcomes emanate from inter alia, a boost in tourism-related services, reconstruction works, robust exchange rate peg coupled with lower travel receipts and higher net income payments. Notwithstanding the positive developments outlined above, we encourage the authorities to more proactively work towards better fiscal consolidation, strengthen the regulatory framework for non-bank financial institutions, and more forcefully address persisting structural challenges.

While we commend the authorities for concerted fiscal consolidation efforts, a lot more needs to be done in view of identified downside risks. We are encouraged by the establishment of the Contingencies Fund, the institution of the Cash Management Committee, and the strengthening of the overall institutional framework for fiscal policy. These have expectedly resulted in improvements in the fiscal position in recent times. But further efforts to enhance revenue mobilization through broadening the tax base and containing wage bill would be required should downside risks materialize. Given the role

that the Contingencies Fund could play in the event of natural disasters, we would welcome staff comments on the rules governing its use during normal times.

Notwithstanding the relative stability in the financial sector, we are concerned that risks in the non-bank financial sector (NBFS) may be overlooked. For example, NPLs in the NBFS remain quite high. We believe that greater attention should be paid to monitoring the developments in the subsector, including risks that might arise from the implementation of the IFRS9 and ultimate reduction in capital following any changes to provisioning requirements. We welcome efforts by the Financial Services Authority (FSA) to strengthen its supervisory toolkit and augment reporting requirements of credit unions. We urge the authorities to intensify efforts to strengthen regulatory framework, rationalize macroprudential standards, and boost reporting transparency by periodically publishing financial stability assessments and completing a host of pending pieces of legislations. In this regard, we would welcome staff comments on efforts presently underway to formulate a Crisis Management Strategy for NBFS.

It is critical that the authorities address several structural reforms with some sense of urgency. In order to set the economy on a path to reach its potential growth, we believe that greater attention has to be paid to addressing the skills mismatch in the labor market, improving the environment for private sector investments, building better resilience to natural disasters, and enhancing spending efficiency in public infrastructure projects. As highlighted in the buff Statement by Ms. Levonian and Mr. Williams, we are delighted with the potentials of the geothermal project to reduce electricity costs and improve competitiveness. We commend the authorities for implementing the AML/CFT related laws but urge them to ensure the effectiveness of preparedness measures, an issue that underscores the criticality of completing the National Risk Assessment by second quarter of 2019.

Mr. Sigurgeirsson and Ms. Karjanlahti submitted the following statement:

We thank staff for their report and Ms. Levonian and Mr. Williams for their buff statement. We are encouraged by the improved economic outlook for St. Vincent and Grenadines, while noting the importance of continuing to pursue structural reforms to strengthen potential growth and managing risks related to natural disasters. We are in broad agreement with staff’s assessment but would like to emphasize the following points related to structural reforms, fiscal policy, financial sector, and vulnerability towards natural disasters.

To sustain growth momentum, we strongly encourage the authorities to push the structural reform agenda. The opening of the new airport and growth in tourism flows give rise to new opportunities. Compared to peers, tourism flows to St. Vincent and Grenadines have been moderate. Improving the investment environment, by streamlining procedures and legislative requirements, increasing the transparency of the tax system and upgrading infrastructure will foster investment and further support growth in the sector. The airport and tourism growth also offer opportunities for agriculture and fisheries, where investment and technical support is needed to improve competitiveness. The completion of the geothermal project in 2020 should improve access and delivery and push down the price of electricity supporting productivity.

High debt levels and risks to natural disasters confirm the need to strengthen fiscal buffers. Tightening the fiscal stance would allow for maintaining the downward debt trajectory and reaching the ECCU target 60 percent of debt/GDP by 2030, even if some growth or natural disaster risks materialize. With growth being below potential, consolidation should focus on growth friendly areas, such as improving revenue administration and broadening the tax base by removing tax exemptions. On the expenditure side, we encourage the authorities to press ahead with the implementation of the medium-term fiscal framework, including a long-term infrastructure investment plan.

We agree with staff on the importance of strengthening the supervision of the financial sector including the effectiveness of the AML/CTF framework. Over the past years, borrowing from credit unions has grown significantly, shifting clients from banks to credit unions. This highlights the need to strengthen the FSA supervisory framework, especially related to non-banks. Could staff elaborate on the reasons behind the growth in borrowing from credit unions? We commend the authorities in their efforts towards addressing AML deficiencies identified in the FATF recommendations and would stress the importance of preventive measures. Here it will be important to complete the National Risk Assessment to identify sectors with high risk of money laundering and weaknesses in the legal framework.

We strongly encourage the authorities to focus on disaster preparedness. Risks related to natural disasters are high and seem to be intensifying with increased severity and frequency of events. As a small economy with limited fiscal space, St. Vincent and Grenadines will need to bolster its capacity to respond to natural disasters and climate change. We

commend the authorities for establishing the Contingencies Fund and encourage formalizing its governance arrangements. Having a transparently and well managed Contingency Fund together with sufficient coverage from the Caribbean Catastrophe Risk Insurance Facility will help to manage frequent shocks. These efforts should be supported by other means of disaster preparedness, such as investing in infrastructure that is more resilient to natural disasters.

Mr. Palei and Ms. Smirnova submitted the following statement:

We thank staff for their informative report and Ms. Levonian and Mr. Williams for their helpful BUFF statement. We welcome more dynamic GDP growth in St. Vincent and the Grenadines of about 2.5 percent compared to a level below 1 percent in the previous years. The challenge for the authorities is to secure a sustainable growth path over the long run, given the high risk of natural disasters and limited diversification of the economy. We broadly concur with the staff appraisal.

The growth momentum allows to build buffers and improve fiscal position of the economy. The authorities keep the fiscal deficit under control, and we hope that the public debt will remain on a downward path. From the cyclical perspective, we agree that it is an opportune time to rebuild fiscal buffers, we believe that capitalization of the Contingency Fund through tax increases is a prudent approach.

Among many recommendations in the report aimed at the longer term, we particularly support the proposal to advance the pension reform. The current composition of public expenditures, the state of the pension system, and the level of pension expenditures in other countries in the Eastern Caribbean Currency Union (ECCU) show that there is substantial room for improvement. A good medium-term fiscal framework, which aligns budget planning with planning and execution of public infrastructure projects, should be another policy priority. Since the country is exposed to major risks of natural disasters, building resilient infrastructure should help to keep the public debt on a downward path in the long run.

The financial sector exhibits some signs of vulnerabilities, which call for strengthening of the financial sector oversight. The rapid growth of credit union loans is worrying. In the report staff noted that “credit unions have lost nested correspondent accounts with domestic banks.” Could staff comment on whether the loss of nested correspondent accounts with domestic banks amplified the risks to financial stability arising from credit union activities?

We welcome the fact that banks have preserved their correspondent banking relationships and believe this is a necessary basis for tourism development. We also note that return on assets and return on equity in the banks have been quite volatile in the past several years. Could staff comment on the factors affecting this volatility? Could staff also comment on why return on equity for St. Vincent and the Grenadines differs substantially from that of the ECCU?

Finally, we commend the authorities for their approach to structural reforms explained in the BUFF statement. Actions geared towards creating opportunities for new business development and enhancing competitiveness, such as building a geothermal plant, should also bring long-term benefits and help to sustain growth.

Ms. Pollard and Ms. Svenstrup submitted the following statement:

We thank staff for their report and Ms. Levonian and Mr. Williams for their helpful buff Statement.

St. Vincent and the Grenadines (SVG) has seen a welcome recovery in growth in 2018, following the opening of the international airport and the subsequent boost to the tourism sector. Going forward, SVG faces the difficult task of maintaining this growth momentum over the medium term, while also pursuing a sustained fiscal consolidation to reach the ECCU 2030 debt target and enhancing resilience to natural disasters.

The ECCU public debt target of 60 percent of GDP is a reasonable anchor, and efforts to develop a medium-term fiscal framework and enhance fiscal institutions will be helpful in this regard. We urge staff and the authorities to thoroughly investigate fiscal multipliers associated with staff's recommended "more active fiscal adjustment" to ensure that this path does not undermine the authorities' efforts by further dampening growth. We welcome the establishment of the Contingency Fund and urge the authorities to take necessary measures to establish its legal framework.

Planned structural reforms will be critical to support growth. We note that SVG ranks as the most expensive destination worldwide in the "Week-at-the-Beach" index from the recent ECCU Article IV. Could staff discuss how much of this is attributed to the lack of an international airport prior to 2017? Further, could staff discuss how they see their proposed reforms to the investment and business environment, as well as the planned construction of a geothermal project, addressing supply-side constraints and thus cost?

Finally, we welcome the important progress made to safeguard financial stability and address legal deficiencies in the AML/CFT framework. We urge the authorities to continue their efforts in these areas, per staff's recommendations.

Mr. Rashkovan and Mr. Manchev submitted the following statement:

We thank staff for the focused report and Ms. Levonian and Mr. Williams for their informative buff statement. Growth re-bounded and government balances improved following the opening of the new international airport and progress with the geothermal energy projects. The near-term outlook is positive too, following the authorities' efforts and investment to promote agribusiness and mitigate natural disaster risks. Nevertheless, the small and prone-to-weather-shocks economy of St. Vincent and the Grenadines needs to further strengthen contingency planning, governance and its operational framework for disaster management and prevention. The authorities should expeditiously continue with structural reforms to foster private sector activity and economic diversification. Sustaining the growth momentum in the long term would require durable fiscal consolidation to put the debt-to-GDP ratio on a path consistent with the authorities' and the ECCU's target as well as strengthening oversight of the non-bank financial sector. Since we broadly share the thrust of the staff appraisal, the remarks below are provided for emphasis.

A credible long term fiscal consolidation strategy and strong implementation are warranted to reverse the budget position, reduce risk of debt distress, and bring the debt-to-GDP ratio back to the ECCU criterion by 2030. We agree with staff that the consolidation strategy should be well balanced and include both revenue and expenditure measures. Additional revenue mobilization should be focused on broadening the tax base and tax rationalization given the country's high average tax rate compared to its peers. On the expenditure side, staff rightly suggests that measures should aim at controlling the public wage bill and achieving a sustainable pension system, in order to have sufficient room for executing the capital spending. Could staff provide more information on the TA and capacity building plans to assist the authorities?

We urge the authorities to implement in full the prudent fiscal policy and debt management frameworks and operationalize them in line with staff's recommendations. The recent establishment of the Cash Management System and Committee are steps in the right direction. These measures should be supported by credible strategies to tackle budgetary arears and significantly

improve oversight over the SOEs. The single Tax Identification Number and risk-based approach in the revenue administration should also be fully implemented to increase tax compliance, and the tax registration database should become operational in real time. Development of a national infrastructure plan, operationalization of the planning process, transparency of project selection and prioritization should be closely linked with the medium-term fiscal framework. The establishment of the Contingency Fund was a major step towards a better handling of natural disaster risks, but its governance and operational framework need further strengthening, including through additional legislation. In this vein, we find it somewhat difficult to agree with staff (p. 7 of the report and draft press release) that natural disaster- and climate change-related risks are labeled as "domestic". Staff's further comments are welcome.

St. Vincent and the Grenadines' financial system is stable but increasing supervisory vigilance will be essential to tackle the remaining pocket of vulnerabilities. We welcome the recent initiatives of the national supervisor (FSA) to strengthen the supervisory toolkit and financial reporting in support of the initiatives at the regional level. The legislative base should be updated and upgraded and brought in line with the best international standards and practices to allow supervisors to take timely corrective actions and intervene in problem institutions. We welcome the authorities' commitment and efforts to properly address the remaining deficiencies in the AML/CTF framework. Staff rightly pointed out that the authorities' focus going forward should be on ensuring the effectiveness of the AML/CTF preventive measures.

Mr. Tan and Ms. Pandit submitted the following statement:

We thank staff for the comprehensive report and Ms. Levonian and Mr. Williams for their informative buff statement. After years of suppressed growth, the St Vincent and Grenadines economy has picked up on account of a recovery in tourism, aided by the newly opened modern international airport. Nevertheless, the risk of natural disaster and climate change and debt sustainability remain key policy challenges. We broadly agree with the thrust of staff's appraisal and would like to put the following comments for emphasis.

Effective fiscal consolidation is vital to reduce the risks of debt distress in the longer term including through legislative reforms. We welcome the authorities' commitment and continuous efforts to achieve the debt to GDP ratio at the regional target of 60 percent. We agree with staff

recommendations on broadening the tax base by reducing import tax exceptions and streamlining VAT exemptions, improving revenue administration via the implementation of Tax Information Number and avoiding the discretionary power of the tax offers. On the expenditure side, growth-enhancing spending on education and infrastructure should be preserved while developing a long-term national infrastructure plan will help with prioritizing and strengthening spending efficiency for key projects. Staff comments are welcome on the progress of authorities' commitment to bring the debt to GDP ratio down at the regional level.

Continuous financial reform is warranted to protect financial stability. We note that the role of non-bank financial institutions increased, while mainstream financial institutions hold high non-performing assets and experience volatile profitability. We welcome the introduction of stress tests and the IFRS 9 and look forward to the approval of relevant legislation and macroprudential regulations to make supervisory and prudential oversight more effective. On the AML/CFT front, we take positive note of the authorities' commitment to complete the National Risk Assessment by September 2019.

We welcome the creation of the Contingency Fund as part of efforts to strengthen resiliency to natural disasters. The establishment of the Contingency Fund is not only important to bolster resilience to natural disasters and climate change but also for sustainable economic growth. As the staff indicates that the annual cost of natural disaster is around 2 percent of the GDP, the authorities are encouraged to support the Contingency Fund with sound legal provision to enhance the governance framework over its operations. Such disaster preparedness efforts through strengthening of legal provisions are critical to protect infrastructure related to tourism which remains a key driver of employment and economic growth in this small island. Similarly, the proper matching of skills with labor demand would play a vital role in addressing the high unemployment rate. On the risk assessment, we invite staff to clarify the characterization of most severe and frequent natural disasters as a domestic risk.

With these comments, we wish the authorities every success in their future endeavors.

Mr. Johnston and Mr. Amor submitted the following statement:

We thank staff for their report and Ms. Levonian and Mr. Williams for the helpful buff statement. We welcome the renewed growth momentum

generated by the new airport, which has led to additional tourists and renewed interest from foreign investors. We are encouraged by the strong progress on reforms and the authorities' commitment to the ECCU debt target. We think staff offer good suggestions for revenue and expenditure initiatives, including base broadening in the tax system and pension reforms, that would help ensure the debt target is met and/or create headroom for investment in disaster resilience and other worthwhile projects. Could staff indicate the reason for cuts in corporate and personal income tax rates, as mentioned in the staff report, given the country is at high risk of debt distress?

The establishment of the Contingency Fund is a welcome step, and we agree it should be safeguarded with a legislative framework to guide effective governance and operational arrangements. We are less convinced by the need to save another 0.7 percent of GDP, on top of the 0.7 percent in the Contingency Fund, for spending after a natural disaster. The opportunity costs can be large in a resource-constrained small state like St. Vincent and the Grenadines. Any fiscal room the government has could also be spent on building resilience, reducing public debt, implementing development projects or delivering public services. It is not clear why natural disaster preparedness should have the first call on these resources. Besides, as the authorities point out, it may be better to re-allocate resources from non-priority areas to supplement the Continency Fund during an emergency, as and when they are needed. More generally, the recent Caribbean conference on building resilience to natural disasters highlighted the need for donor support to build ex-ante resilience, given debt levels are already high in many countries. Does the ECCU debt target of 60 percent of GDP by 2030 present any challenge to the authorities in securing financing for investment in resilience?

While growth will likely be supported by the new international airport and the ongoing geothermal energy project, further structural reforms are needed. Given the renewed investor appetite, we encourage the authorities to fast-track efforts to improve the investment climate. Streamlining investment procedures is a good start, and a standalone investment law and a one-stop-shop for foreign investors will be helpful in this regard. We also encourage the authorities to continue their efforts to promote human capital, raise productivity and match skills to business needs in key sectors. Improving access to affordable credit by small businesses and facilitating trade could foster greater linkages between tourism and other sectors, and enable fisheries and agriculture firms to utilize the enhanced airline connectivity to increase exports.

Mr. Ronicle and Mr. Clark submitted the following statement:

We thank staff for the informative papers and Ms. Levonian and Mr. Williams for their informative buff statement.

We welcome the positive economic progress and commend the authorities for the progress in addressing the emerging challenges and risks to the economic outlook. We agree with staff's main policy recommendations for the need to implement wider structural reforms to boost private sector activity, to consider additional fiscal adjustment to increase buffers and to adopt a medium-term fiscal framework and strengthen revenue administration.

We agree that whilst there is a more favourable outlook, we note the significant risk and high exposure to natural disasters – we concur with the authorities view that "natural disasters and climate change are the most formidable near- and long-term threats".

We therefore strongly support the establishment of the Contingencies Fund to help protect the public finances from natural disaster risk and encourage the authorities to legalise the operational and governance framework, especially the trigger, withdraws and replenishment procedures. Equally, we concur with staff that the authorities should explore additional buffers in anticipation of natural disasters, not only expanding the coverage of disaster insurance and setting aside resources for emergency operations, but also contingent credit instruments as part of a broader financial layering approach. This should be done in conjunction with an updated national risk assessment.

We noted with interest the natural disaster stress scenarios in the debt sustainability analysis. Since these indicate that under plausible scenarios debt reduction may be significantly more challenging than in the base case, we would encourage the authorities to explore options to achieve higher levels of fiscal adjustment, particularly on the revenue side.

Mr. de Villeroché, Mr. Castets and Ms. Albert submitted the following statement:

We thank staff for their insightful set of papers, as well as Ms Levonian and Mr. Williams for their informative buff statement. We welcome the more favorable outlook in St. Vincent and the Grenadines (SVG) following the opening of the new modern international airport. The economy is at a turning point, but despite positive developments, it remains exposed to more regular and more severe natural disasters. Consequently, additional efforts to build resilience against these shocks and to reduce the risk of debt distress appear necessary to create the conditions of a durable and sustainable

growth over the long term. We share the thrust of staff's appraisal and recommendations and we would like to add the following comments:

Outlook and Risks

Positive growth momentum is encouraging, but the economy remains exposed to both external and domestic risks. The new airport boosts tourist arrivals and tourism-related activities, production of local products, and construction activity. However, a United States economic slowdown deeper than anticipated or further tightening of global financial conditions both represent significant downside risks. Moreover, due to the dependence of SVG on imported fuels, an increase of oil price could weigh on GDP growth, whereas staff highlights that external position is already weaker than implied by medium-term and desirable policies (current account deficit of 17.2 percent of GDP in 2017, among the largest in the region). Against this background we commend the authorities for the implementation of a geothermal project (electricity production should start in 2020) aiming at reducing their dependence to fuel. Can staff provide an estimate of the expected impact of the geothermal project construction in terms of price electricity reduction and indicate in which extent it could help to reduce the fuel bill? Does SVG still receive fuel under the PetroCaribe agreement? Could staff provide additional details about the project of new port evoked p.18 of the report?

Building Resilience Against Natural Disasters

Considering the increasing number of severe and frequent natural disasters, designing an ex ante strategy is a priority. We commend the establishment of the Contingency Fund and encourage the authorities to strengthen the Building Code and Physical Planning Law as limited progress has been made in this area so far. As private-led growth and resilient investment should be further stimulated, reviewing the current procedural and legislative framework for investment might be warranted. Moreover, we support, as recommended by staff, the expansion of the coverage of disaster insurance to broaden and deepen risk transfer, especially in cases of flood. Could staff provide more details about the development of insurance tools that could be implemented in a complementary way? Would it be feasible to embed "hurricane-linked clauses" in St Vincent and the Grenadines debt contracts like in Grenada and Barbados? As many institutions are involved on those issues, we emphasize the need to ensure an efficient cooperation between all of them.

Fiscal Stance

Achieving the ECCU public debt target of 60 percent of GDP is challenging and we encourage the authorities to design a fiscal strategy as growth-friendly as possible. We welcome the recent fiscal positive developments, with the surplus of the overall fiscal balance over the past few years (¼ percent of GDP in 2016-2017, compared to a deficit of 3.4 percent of GDP in 2009-2015) and the debt to GDP ratio fell to below 75 percent of GDP at end-2017. While we agree with the view that the authorities should pursue their fiscal consolidation efforts to ensure long term sustainability of public finances, caution is needed to avoid a too burdensome situation as highlighted by the authorities. We note that current DSA has less favorable growth hypothesis than the previous one and that staff now considers a primary surplus of 1.1 percent of GDP as appropriate to reach the public debt target, a bigger one than recommended in the 2017 DSA (0.6 percent). We encourage the authorities to gradually take revenues and expenditures measures, although without jeopardizing growth and the most vulnerable. Priority should be given to streamlining tax concessions and other tax incentives, containing the growth of the wage bill to around 2.5 percent per year and designing an appropriate pension system to restore sustainability. The DSA analysis is very enlightening as it includes alternative scenarios including natural disasters. However, we wonder whether the baseline assumption should be considered as optimistic on natural disasters (it is based on the magnitude and frequency of the past 15 years) given that natural disasters will become more and more frequent and severe?

Financial Sector

We appreciate the progress made in addressing remaining legal deficiencies in the AML/CFT framework and encourage the authorities to ensure the effectiveness of these measures. Accelerating the approval of the several draft laws in the financial sector still pending, especially about the FSA regulations, will also contribute to improve the financial framework. Moreover, considering vulnerable spots in the non-bank financial sector, and fast growing of the lending by credit unions, we agree with staff that stress testing should be extended to analyze multi-factor shock scenarios for credit unions, cover insurance firms, and incorporate interlinkages among various institutions in collaboration with the ECCB. As highlighted in the last report on the ECCU, this collaboration is important for the establishment and implementation of plans addressing the weakness of non-bank institutions.

Mr. Sylla and Mr. Bah submitted the following statement:

We thank staff for their well-balanced set of papers and Ms. Levonian and Mr. Williams for their informative buff statement.

The authorities of St. Vincent and Grenadines should be commended for implementing sound policies following the global financial crisis and an ensuing period of very low growth. These have led the economy to renew with good macroeconomic performance. The recovery of growth since mid-2017 is supported by buoyant activity in the tourism sector in large part due to the opening of the new international airport. With this large investment, flows of tourists from neighbor and developed countries have increased and foreign investors have come in. As a consequence of this rebound, the fiscal balance has improved, the debt-to-GDP ratio has started to decline while the external position has weakened slightly. We also note that these positive developments are expected to continue over the medium term.

Despite these encouraging achievements and favorable prospects, the authorities of St. Vincent and Grenadines are facing daunting challenges to sustain high economic growth over the long term, which calls for building stronger resilience to shocks. Growth remains constrained by the country's limited land and resources as well as its exposure to severe natural disasters. Against this backdrop, the authorities should promote the development of the private sector and strengthen their preparedness to mitigate the effects of natural disasters by building solid infrastructures and further enhancing the fiscal and governance frameworks. These include the operationalization of the Contingency Fund and an update of the National Emergency and Disaster Act. These efforts to tackle the effects of a global "public bad" (climate change) should be supported better by the international community.

We encourage the authorities to pursue fiscal reforms and sound debt management to preserve fiscal and debt sustainability given the country's high risk of debt distress. We welcome the authorities' commitment to meet the ECCU debt-to-GDP ratio of 60 percent by 2030. The decline in the country's debt-to-GDP ratio in 2016 and 2017, thanks to improvements in the fiscal position, is encouraging. The authorities' pursuit of prudent fiscal policies while aiming at higher growth should be accelerated with the view to create the fiscal space needed to boost investment which has remained significantly low throughout the years. They should also complete their fiscal reform initiatives, including establishing a medium-term fiscal framework, enhancing tax administration and procedures, strengthening cash management and overhauling public pension systems. We would appreciate staff's elaboration on the technical assistance provided by the Fund to St. Vincent and Grenadines on public finance management.

While the financial sector is broadly sound, efforts are needed to ensure that the growing non-bank financial institutions meet adequate prudential requirements and that the regulatory and supervisory frameworks are robust. Progress has been made towards a stable financial system, with the decline in the NPL ratio, proper capitalization of most credit unions and their implementation of IFRS 9 standards. We encourage the authorities to ensure that non-bank financial institutions have adequate capacity to monitor and manage risks, the Financial Stability Authority (FSA) is appropriately equipped to supervise the sector, and stress testing covers a range of vulnerabilities and interlinkages relevant to preserving financial stability. Efforts are also needed to address the remaining legal deficiencies in the AML/CFT. We regret that the loss by credit unions of nested correspondent accounts with domestic banks is not addressed in the report. Noting the growing importance of these institutions in the sector, we would expect staff to elaborate on the risk that such development pose to financial intermediation, if any.

We urge the authorities to forcefully pursue far-reaching structural reforms to unleash the potential growth of St. Vincent and Grenadines. Structural reforms should be more focused on further improving the business environment to foster a vibrant private sector. Implementing measures to facilitate property registration and access to financing will be helpful in this regard. Moreover, we encourage further efforts to simplify investment legislative requirements and increase physical infrastructure-including roads, ports, irrigation and the water supply system-to attract more foreign investment and make the economy more resilient to natural disasters. In addition, there is a need to increase competitiveness notably through actions to enhance human capital and address the persistently high unemployment. To this end, improving labor market flexibility and promoting vocational education and training are of the essence. We see merits in the country participating in the project of Eastern Caribbean Regional Agriculture Competitiveness.

With these remarks, we wish the authorities of St. Vincent and Grenadines every success in their endeavors.

The Acting Chair (Mr. Furusawa) noted that economic recovery was underway in St. Vincent and the Grenadines. There was renewed interest from foreign investors in tourism projects following the opening of a modern international airport. The challenge was to sustain growth over the longer term in the face of the country’s weak competitiveness, infrastructure and human capital constraints, and high exposure to natural disasters. It would be critical to bring down public debt to increase fiscal buffers and provide room for

investments in disaster-resilient infrastructure, strengthen disaster preparedness, and implement structural reforms to enhance the investment environment

Ms. Fritsch made the following statement:

We have not issued a gray statement and would like to offer a few comments while broadly agreeing with the staff appraisal.

We welcome the ongoing economic recovery in St. Vincent and the Grenadines, and positively note that the authorities are making good progress on implementing the previous recommendations by the staff. Notwithstanding the brighter economic outlook, St. Vincent and the Grenadines faces significant challenges as a small island economy vulnerable to natural disasters and with limited scope for fiscal maneuver. To sustain the growth momentum, the authorities should put public debt on a downward trajectory, implement measures to enhance private sector-led investment and growth, and improve their resilience to natural disasters.

While we acknowledge the authorities' track record of prudent budget execution, public debt levels remain elevated, and further efforts by the authorities are needed to build fiscal buffers. In this regard, increasing revenue mobilization and advancing pension reform will be key steps to reduce the debt burden while creating room for growth-enhancing public investment and education spending.

We also welcome the staff's analysis on the impact of more active fiscal adjustments on debt dynamics, yet more analysis might be needed to assess potential outward effects on growth, as pointed out by Ms. Pollard and Ms. Svenstrup.

A sound fiscal strategy that is anchored in fiscal rules and better fiscal management could further help to meet the debt target of 60 percent of GDP by 2030. Frequent natural disasters and climate change pose significant risks to St. Vincent and the Grenadines. We welcome the authorities' efforts to sufficiently capitalize the contingency fund while seeing a need to establish a specific governance and operational framework. The staff's nuanced and detailed advice on this matter is much appreciated.

An annual expenditure reserve in the budget for emergency expenses could close the gap between the expected annual fiscal costs of natural disasters and the contingency fund.

Lastly, we welcome the authorities' progress on improving the Anti-Money Laundering and Combating the Financing of Terrorism (AML/CFT) framework. Ensuring the effectiveness of AML/CFT-related laws is an important next step to preserve financial stability and to safeguard correspondent banking relationships (CBRs).

With this, we wish the authorities all the best.

Mr. Rashkovan made the following statement:

We have issued a gray statement. However, I would like to raise one specific point in the context of risks related to natural disasters and climate change, a point also raised by Mr. Tan and Ms. Pandit. Before doing so, I would like to acknowledge that we highly value the engagement and the responsiveness of the Western Hemisphere Department (WHD) to the needs of the membership in the Caribbean region, including those members from our constituency. We thank the staff for their support in the recent years, including by helping to build resilience against climate-related risks.

The point I am making is possibly a broader one and does not concern this specific report on St. Vincent and the Grenadines. Similar to the risk assessment matrix in the Republic of Fiji staff report for the 2018 Article IV consultation and the 2018 Article IV report for Cambodia, the present staff report in paragraph 10 qualifies severe weather events as a "domestic" risk. We understand from the staff's written answer that this categorization is in line with the surveillance policy guidance note that states: "that the assessment of external risks should be guided by the global risk assessment matrix (G-RAM) and area departments' views on regional risks." Again, we thank the staff for this clarification.

While we can retrace staff's argumentation, we believe that, by characterizing climate-related risks as "domestic," the staff report could lead to the conclusion that their likelihood of occurrence could be influenced by the authorities, which is not the case. More generally, we believe it is important to distinguish between internal and external risks, as some can be actively reduced as a result of adequate policies, while others can be only protected against, for instance, by building resilience.

The authorities have little to no influence on external risks. We believe that this is an important qualitative difference, which also has implications for policy recommendations. We believe that in this context of the challenges that the region faces regarding extreme weather events, such a differentiation is

relevant. In this sense, we have doubts whether referring to severe and frequent natural disasters as a domestic risk in the press release would send the right signal. We kindly ask the staff to think about the exclusion of these words from the press release. I believe this subject is worth a further broader discussion. We look forward to future bilateral interactions with the staff on this matter and stand ready to positively contribute to the discussion.

Mr. Castets made the following statement:

We thank the staff for the insightful set of papers, notably on the DSA, which is very detailed, as well as Ms. Levonian and Mr. Williams for their informative buff statement.

We welcome the more favorable outlook in St. Vincent and the Grenadines, and we encourage the authorities to pursue their efforts to create the conditions for durable and sustainable growth over the long term, especially through an appropriate ex ante strategy, with resilient investment as the main pillar.

I would like to highlight a few points. First, as also alluded to by Ms. Fritsch, we support the establishment of a contingency fund, which we see as a useful buffer in case of natural disasters. We would like to emphasize the importance of going further with the appropriate development of financial tools, especially regarding insurance coverage. Therefore, we encourage the staff and the World Bank to keep working together on developing efficient instruments to transfer risk, such as hurricane clauses or sovereign insurance against natural disaster, which are two viable options. We have a question for the staff about the fact that the simulation of the three-layer strategy was developed in the last EQ report. It seems especially interesting as an approach in the case of St. Vincent and the Grenadines, and we ask the staff to explain how they would see this.

My second point regards fiscal policy. We recognize that the authorities have to deal with many constraints simultaneously. On the one hand, the convergence toward the debt target of 60 percent-to-GDP by 2030 appears appropriate, given the still high level of public debt in the country. But on the other hand, we would call for caution and to avoid jeopardizing growth among the most vulnerable in a context where the authorities need investment to deal with natural disasters. In this regard, we asked a question to the staff about the fact that the baseline scenario assumption is that natural disasters would occur at the same frequency as they did on average over the past 15 years. We wonder whether there would be a need to have a more

prospective approach to natural disasters since a significant amount of scientific work concludes that natural disasters will occur more frequently. I would appreciate the staff's elaboration on that point.

Finally, like Ms. Fritsch, we appreciate the progress made in addressing the remaining legal deficiencies in the AML/CFT framework. We encourage the authorities to focus now on the effectiveness of the implementation of the legal framework. We also associate ourselves with the question raised by Mr. Rashkovan about how natural disasters are described in the risk assessment matrix. We look forward to the staff's answer.

Mr. Johnston made the following statement:

That was a really good and interesting report. The staff's recommendations around natural disasters are of particular interest to us in our constituency because St. Vincent and the Grenadines looks a lot like the countries that we represent. I was just saying to my colleague next door, that if St. Vincent somehow managed to detach itself from the Caribbean and float around to the Pacific, it would feel very much at home.

The recommendation is that St. Vincent saves, on top of their 0.7 percent in their contingency fund, another 0.7 percent because the total of 1.4 percent is the amount that it spends, on average, on disasters each year. In one sense, this is an elegant and simple rule and makes sense. But I would like to know a few other things.

How did the staff weigh up the use of another 0.7 percent of GDP in another contingency fund versus spending it on other priorities that the country has, including building ex ante resilience to disasters in the first place or on other pressing social or infrastructure projects? I have a bit of sympathy for the authorities, because it is very difficult to keep stashing away more and more money when you have immediate needs in your country. People can legitimately ask why the government is putting away money for a future disaster when it has just closed the health clinic on an island, which some would consider to be a disaster in the present.

The approach of working out the average cost and putting that money aside, is that part of a common approach that is being developed across countries? Because that could equally apply to the sorts of countries we represent.

The staff representative from the Western Hemisphere Department (Mr. Ishi), in response to questions and comments from Executive Directors, made the following statement:[1]

I thank Directors for the many gray statements, comments, and questions. That helps us think carefully about St. Vincent and the Grenadines' situation.

We have responded to most of the technical questions, and we have also issued supplementary information on the 2019 budget. My intervention is focused on fiscal policy, together with natural disasters, specifically, how to take account of natural disasters in the fiscal policy framework.

The authorities have conducted fiscal policy over the past several years fairly prudently. But they always presented ambitious budgets. If one looks at the 2019 budget, they expect a significant widening of the deficit to over 7 percent of GDP. This is mainly due to a significant increase in capital spending. Capital expenditures will increase to around 9.5 percent of GDP in 2019. The question is whether these ambitious, frontloaded capital spending projects are consistent with their objective of meeting the 60 percent target by 2030. We did simple simulations. Basically, we tried to look at the overall capital spending plan through 2013 and tried to simulate more frontloaded capital spending and what it would mean for fiscal sustainability and the macro framework.

Our experiment is simple. Let us assume that over the next three years, the government spends around 9.5 percent of GDP in capital spending and after 2021, they roll over the capital spending. Our calculation suggests that the government can still meet the 60 percent target. By 2021, the debt would rise to 85 percent of GDP. Today it is 73 percent of GDP. To achieve 60 percent, real GDP growth is needed, around 2.8 percent of GDP. This is half a percentage point higher than our baseline scenario.

We view this frontloaded capital spending strategy as risky for three reasons. The first is implementation risk. This budget implies more than a 100 percent increase in capital spending in 2019, which looks ambitious, especially given the capacity constraints and complexity in the procurement.

[1] Prior to the Board meeting, SEC circulated the staff's additional responses by email. For information, these are included in an annex to these minutes.

Second, the growth impact is uncertain. Infrastructure spending, if done efficiently and productively, could boost growth and potential growth, but raising real GDP growth to 2.8 percent and sustaining it at a level over the medium term looks challenging, especially given the downside risks arising from natural disasters.

Finally, we agree that investment in residence structures would mitigate destruction and losses from natural disasters, but it does not mean that this eliminates all risk. The budget still needs to have a cushion for liquidity buffers in anticipation of natural disasters. That is why, given the downside risk, we still recommend that the authorities continue to implement the budget prudently, and the budget should include adequate buffers, and then consider a more active fiscal adjustment programming.

I will now respond to the specific questions raised in the gray statements.

First, some Directors raised concerns about whether our fiscal framework accommodates room for capital spending. We agree that our fiscal plans should balance the need for building fiscal buffers with the need for implementing development projects. Actually, in our medium-term fiscal framework, we accommodate more than EC$1.1 billion for capital projects over the next 10 years. This is about 50 percent of today's GDP, which is sufficient to implement ongoing and foreseeable donor-funded, climate-related projects. But this also highlights the importance of strengthening public investment management. That is why the staff recommended that the development of a national infrastructure plan and the prioritization of projects in collaboration with donors and stakeholders is important.

Second, some Directors also raised concerns about adverse fiscal multiplier effects. Let us clarify that in our suggested fiscal adjustment scenario, raising the primary surplus to 1.6 percent of GDP is moderate. For example, we are not recommending cutting the wage bill in value terms. We also believe the multipliers are likely small because St. Vincent and the Grenadines is a small and open economy, with imports accounting for nearly 40 percent of GDP, and many proposed fiscal measures, like containing the wage bill or pension reform, would not most likely affect households with liquidity constraints. Fiscal consolidation should boost investor confidence and private sector activities. But for information, our colleagues are now working on estimating fiscal multipliers, just focusing on small economies, including island economies.

Third, some Directors are less convinced about the need to save an additional 0.7 percent of GDP for expenditure reserves. The first thing I want to point out is that we are concerned that this contingency fund just started, and the stock of assets and the conditions of the fund are too small. We need to admit that, assuming that the expected natural disaster cost is true, they need extra buffers. At the same time, this contingency fund is the result of the government's hard work, because increasing the VAT and increasing the reserve, introducing a new hotel levy was politically very difficult. That is why we recommended that they need to provide some extra budget reserves. That budget reserve can be released at the end of the fiscal year if nothing happens and then can be used for debt reductions. In this way, we addressed the issue of opportunity cost.

On the question about more frequency in 10 years or 15 years, we basically made a judgment call and then our baseline—especially the GDP scenario it is not scientific. But given the country experience, and given the history of natural disaster costs over the last 15 years, our macroeconomic scenario is most likely plausible.

Finally, you raised a question about this. Our colleagues did a simulation in the Eastern Caribbean Currency Union (ECCU). That, I need to come back to you bilaterally because there is a technical element. And for that St. Vincent exercise, we need a simple approach, more accounting-based approach.

The staff representative from the Strategy, Policy, and Review Department (Ms. Goodman), in response to questions and comments from Executive Directors, made the following statement:

I will speak to the treatment of climate change-related risks in the risk assessment matrix (RAM). The staff has provided a written response on this issue. We did so because this has been raised recently in the Board discussion on Cambodia. We did receive informal inquiries in the context of the recent lapse-of-time consideration of Fiji's Article IV consultation.

I should start with the surveillance policy guidance note. From the surveillance policy guidance note, we hear that for each individual member, the assessment of external risks should be guided by the G-RAM and area departments' views on regional risks. Climate risks are not in the G-RAM and have not been identified as a regional external risk by the area department.

The reason that the climate risks are not in the G-RAM is because the G-RAM covers global risks that could materially alter the global baseline. Climate change is a long-term trend and should be included in that baseline. To the extent that climate change results in a higher-than-anticipated frequency of natural disasters, these disasters—while they have the potential to significantly impact individual members—are not expected to affect the global baseline, e.g. global growth, in the next one to three years, which is the time horizon for the G-RAM. As such, climate change risks are collectively classified as "domestic" in line with the guidance note because the guidance note also states that domestic risks should include major economic and financial risks, including the risks that policies are not fully implemented. Since these risks are not in the G-RAM and are heightened by the lack of policies for their timely mitigation, they have been classified as "domestic" in this case.

We recognize that there could be perspectives on this. From our side, it is helpful to have the discussion and the feedback. We take good note of these issues, and we will be considering how to address them.

Over a longer time horizon, I should also mention that the staff will be reviewing—in the context of the Comprehensive Surveillance Review—how domestic and external risks are defined in RAMs. But that is part of a more medium-term consideration.

Ms. Levonian made the following concluding statement:

Let me begin by thanking the staff for their efficient work in preparing the report and for their cooperative engagement with my authorities. I also thank Directors for their candid and insightful statements. I will convey their views to my authorities. Many of the comments reflect Directors' understanding of the mounting challenges that small island developing states like St. Vincent and the Grenadines face, especially their vulnerability to natural disasters and climate change. I am grateful for Directors support in this regard. In my buff statement, I stressed some of my authorities' key policy undertakings to make the St. Vincent and the Grenadines economy more vibrant and resilient, so I will emphasize a few points.

On fiscal policy, my authorities remain firmly committed to pursuing prudent fiscal policies to keep debt sustainable, but it is also important that the consolidation does not jeopardize growth. In this context, the fiscal strategy prioritizes growth-friendly and resilient capital projects. Relatedly, my

authorities will maintain a tight lid on recurrent spending while redoubling efforts to mobilize revenues.

On the latter, with the expiration of the tax amnesty last year, they will move aggressively to pursue tax evasion. The soon-to-be tabled Tax Administration and Procedures Act will further boost the government's ability to pursue tax evasion alongside other tax policies and administrative actions that they are taking.

Turning to inclusive growth and structural reforms, my authorities appreciate the acknowledgement by the staff and a further reiteration by Directors of the rebound in growth over the last two years. They also agree that uplifting and sustaining the trajectory will be a key challenge. With this in mind, the government is undertaking unprecedented investments to upgrade the country's infrastructure, strengthen resilience to shock, particularly from weather-related events, empower human capital, and modernize the public sector. These initiatives are vital for the country to tackle vulnerabilities, reduce unemployment—which remains too high at 20 percent—and keep debt on a trajectory toward the ECCU target of 60 percent of GDP by 2030.

Given the quality of the public investment projects underway, alongside plans to enhance the business environment, the government is solidly laying down the foundation for invigorating private sector investment. In this regard, my authorities remain confident of a higher future growth path than the 2.5 percent estimated for 2018. The new international airport is already yielding fruits, with a 5 percent rise in stopover arrivals in its first full year of operation. The addition of more flights will better enable St. Vincent and the Grenadines to exploit its vast tourism potential. The private sector is moving to seize these opportunities by opening new hotels and expanding and refurbishing their existing stock. The geothermal plant that is due to open in 2021 will ensure greater energy efficiency in an environmentally friendly manner, and it will provide more stable and reliable energy prices, reduce carbon emissions, and make the economy more competitive.

As the economy modernizes and becomes more vibrant, it is imperative that citizens are sufficiently equipped to take up the newly created jobs. My authorities recognize that more work is needed to better align education and skills with new labor market demands. To this end, both the World Bank and the Caribbean Development Bank are funding technical and vocational training.

On the financial sector, my authorities have made noteworthy progress in addressing AML/CFT deficiencies. However, they will remain vigilant to potential risk and work to strengthen the legislative, supervisory, and enforcement regimes.

I would just like to comment on the climate change and natural disaster aspect to this. I completely echo what my colleagues have said around the table. The Managing Director says that climate change is one of the key global risks going forward. The World Economic Outlook (WEO) this time around actually categorized climate change as an external risk. I understand that the best conversation around that might be around the review of the Comprehensive Surveillance Review. There is a real inconsistency there, and we are going to have to address that as we go forward.

In closing, let me, once again, on behalf of my authorities, thank the mission chief, Mr. Ishi, and his team for a splendid job and the constructive engagement.

The Acting Chair (Mr. Furusawa) noted that St. Vincent and the Grenadines is an Article VIII member, and no decision was proposed.

The following summing up was issued:

Executive Directors agreed with the thrust of the staff appraisal. They commended the authorities for successfully reinvigorating the St. Vincent and the Grenadines' economy. Nonetheless, they noted the continuing challenges in terms of making economic growth more sustainable, reducing public debt, and increasing resilience to natural disasters.

Directors stressed the importance of advancing structural reforms to raise longer-term growth. They urged the authorities to capitalize on the growth opportunities created by the new airport. They recommended vigorously implementing policies to foster private sector activity, by improving the investment climate and strengthening human and physical capital, including investing in climate-resilient infrastructure.

Directors emphasized the importance of bolstering fiscal buffers. They welcomed the authorities' commitment to meeting the 60 percent of GDP debt target by 2030 and underscored the need for fiscal consolidation that does not jeopardize economic growth. They recommended prioritizing capital projects taking into account capacity and budget constraints and seeking concessional financing. Directors also encouraged taking additional fiscal measures, including broadening the tax base and reforming the pension system.

Directors welcomed the establishment of the Contingency Fund as an important instrument to protect public finances from the impact of natural disasters and climate change. They underscored the need to legislate the Contingency Fund's governance and operational framework to ensure its effectiveness and transparency. Directors also suggested expanding the coverage of disaster insurance, especially against floods. More generally, they recommended continuing to strengthen disaster preparedness, including reviewing the National Emergency and Disaster Act, updating river basin flood risk maps, and enhancing public education and awareness.

Directors encouraged the authorities to strengthen the institutional fiscal framework. Priorities include adopting a medium-term fiscal framework, strengthening revenue administration by moving toward a risk-based approach and completing the various reform initiatives, issuing regulations to strengthen the oversight of state-owned enterprises, and establishing a legal and institutional framework to assess potential risks from public-private partnerships.

Directors highlighted the need to further strengthen financial sector oversight. They urged the authorities to enact pending legislation to strengthen the Financial Services Authority's enforcement power. Directors urged the authorities to move ahead with preparing a crisis management plan for the non-bank financial sector and setting up a Financial Crisis Management Committee, building on earlier technical assistance provided by CARTAC.

Directors commended progress in addressing remaining legal deficiencies in the AML/CFT framework. Going forward, they recommended focusing on ensuring the effectiveness of AML/CFT preventative measures and completing the National Risk Assessment.

It is expected that the next Article IV consultation with St. Vincent and the Grenadines will be held on the standard 12-month cycle.

APPROVAL: April 21, 2020

JIANHAI LIN
Secretary

Annex

The staff circulated the following written answers, in response to technical and factual questions from Executive Directors, prior to the Executive Board meeting:

Outlook and risks

1. ***We note that SVG ranks as the most expensive destination worldwide in the "Week-at-the-Beach" index from the recent ECCU Article IV. Could staff discuss how much of this is attributed to the lack of an international airport prior to 2017?***

- ***The latest available Beach Index (October 2018) suggests that St. Vincent and the Grenadines is a relatively expensive destination in the WHD region. This reflects, in part, expensive hotels. The index is calculated as the weighted average of the prices of hotel, taxi, meal, water bottle, beer, and coffee and does not directly reflect air fares.***
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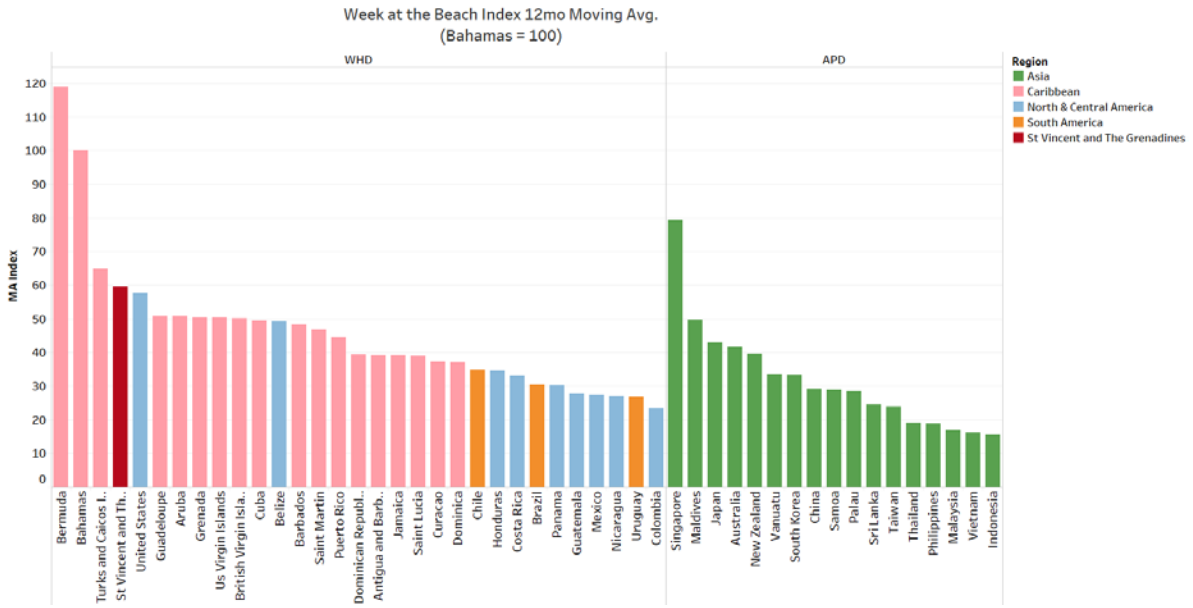


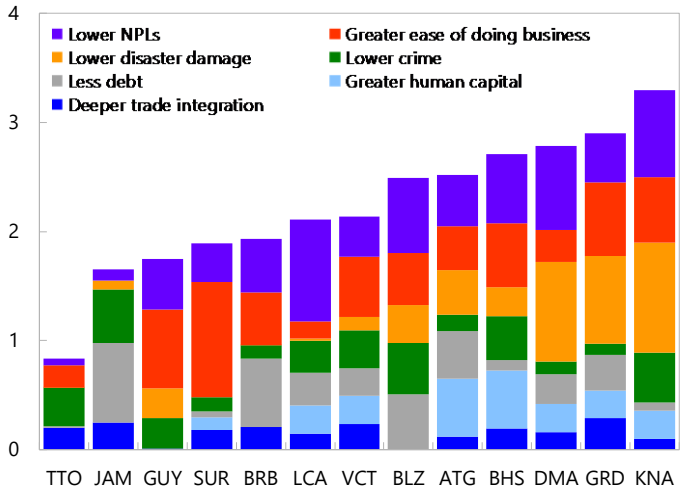
2. ***Further, could staff discuss how they see their proposed reforms to the investment and business environment, as well as the planned construction of a geothermal project, addressing supply-side constraints and thus cost?***

- The government's efforts to improve the investment and business environment included: (i) strengthening technical education to reduce the skills mismatch; (ii) strengthening the rule of law and contract rights; and (iii) reducing the time and cost of paying taxes through e-filing and payment. Most recently, the government has announced its plan to set up a Doing Business Unit at the Ministry of Finance to strengthen the monitoring of the main challenges in the business environment. It is

also planning to build a sub-sea high-speed fiber-optic broadband (extending to the Grenadines) to improve connection for all key government offices and enhancing e-government services.

- Last year, the Fund published "***Unleashing Growth and Strengthening Resilience in the Caribbean,***" which presented illustrative analyses on the growth impact of structural reforms (Chapter 2). For St. Vincent and the Grenadines (VCT), an improvement in the business environment (World Bank Ease of Doing Business Index distance to frontier was used as a proxy) would have the greatest impact on growth.

Figure 8. Reinvigorating Growth: Illustrative Medium-term Growth Gains
(Percentage points per year; deviation from baseline)



- On the impact of the geothermal project, see below (#3).

3. Can staff provide an estimate of the expected impact of the geothermal project construction in terms of price electricity reduction and indicate in which extent it could help to reduce the fuel bill?

- Once geothermal electricity production commences in 2021, fuel imports could be reduced by about 1-1.5 percent of GDP (from 4 percent of GDP in 2017). The impact would depend on how much diesel plants would still be used as peak demand plants.
- The expected impact on the electricity price would, in part, depend on the financing structure of the project, which has yet to be finalized. Over the long-term, the electricity price is expected to fall, but the expected reduction may be limited in the near term, due to debt service burden.

4. Does SVG still receive fuel under the PetroCaribe agreement?

- We had some difficulty in getting full information about the recent operations related to the PetroCaribe agreement.
- Available information, however, suggests that VINLEC (the public power generation and distribution company, the main buyer) no longer buys fuel from the PetroCaribe.

5. Could staff provide additional details about the project of new port evoked page 18 of the report?

- The new port is to replace the two cargo ports currently in operation and will handle container traffic, general cargo, and breakbulk, consolidating all international commercial goods traffic (except intra-regional movements).
- The project will also include a terminal for intraregional ferry services. A feasibility study has been undertaken, covering topographical and geotechnical aspects, financial and economic considerations, as well as the project's environmental and social impact, but the project plan has yet to be fully finalized.
- The total costs are estimated at US$145 million, partly funded by the Caribbean Development Bank, the UK Caribbean Infrastructure Fund, and the World Bank.

6. In this vein, we find it somewhat difficult to agree with staff (p. 7 of the report and draft press release) that natural disaster- and climate change-related risks are labeled as "domestic". Staff's further comments are welcome.

- Climate risks are not in the Global Risk Assessment Matrix (GRAM) and have not been identified as regional external risks by the area department. These risks are not in the GRAM because GRAM covers global risks that could materially alter global baseline. To the extent that climate change results in a higher-than-anticipated frequency of natural disasters, these disasters—while having potentially significant impact on individual economies—are not expected to affect global baseline (e.g., global growth) in the next 1-3 years, which is the time horizon for the GRAM.
- As such, the risks are correctly classified as "domestic" in line with the surveillance policy guidance note that states that the assessment of external risks should be guided by the GRAM and area departments' views on regional risks. The guidance note also states that domestic risks should include major economic and financial risks, including the risk that policies are not fully implemented. Since these risks are not in the GRAM and are heightened by the lack of policies for their timely mitigation, they have been classified as domestic."

Fiscal policy

7. Staff comments are welcome on the progress of authorities' commitment to bring the debt to GDP ratio down at the regional level.

- Staff will respond to this question during the Board meeting.

8. Does the ECCU debt target of 60 percent of GDP by 2030 present any challenge to the authorities in securing financing for investment in resilience?

- Staff will respond to this question during the Board meeting.

9. We also agree with staff that additional efforts are needed to clear the existing budgetary arrears and resolve classification issues in this area. Could staff clarify how these arrears are reflected in the public debt data

- The stock of arrears (1½ percent of GDP) are recorded in the public debt data.

10. Could staff indicate the reason for cuts in corporate and personal income tax rates, as mentioned in the staff report, given the country is at high risk of debt distress?

- In its 2018 Budget, the government decided to cut the corporate tax rate from 32.5 percent (one of the highest in the ECCU region) to 30 percent, on par with St. Lucia and Grenada, to preserve tax competitiveness. The government also reduced the personal income rate to 30 percent, in line with the corporate income tax cut.

11. Could staff provide more information on the TA and capacity building plans to assist the authorities?

- The Fund provided the following technical assistance missions in recent years.
- **Medium-term fiscal framework mission** to help strengthen macroeconomic and fiscal forecasting to support the budget process
- **Tax policy mission** to assess the tax system and provide recommendations aimed at broadening the tax base and streamline the use of tax incentives
- **Cash and liquidity management mission** to improve the management of government resources and reduce the cost of borrowing
- **Expenditure arrears mission** to assess the main sources of government payment arrears and provide advice on measures to reduce the stock of arrears and avoid the accumulation of new arrears.
- Ongoing TA activities (selected) are as following.
- **Customs administration** to help improve the core functions of the Customs and Excise Department
- **Revenue administration and governance** to strengthen revenue administration, management, management and governance
- **Budget preparation, execution, and control** to implement comprehensive, credible, and policy-based budget preparation and improve the effectiveness of budget execution and control

Natural disasters

12. Could staff elaborate on the support provided by donors in the past to deal with natural disasters?

- The example of donor-supported programs is as following (some ongoing).

Project title	Key donors	Year approved	Main objectives
Rehabilitation of Roads and Bridges	Caribbean Development Bank	2012	To upgrade 11.4 kilometer of roadway (from Kingstown to Layou) and associated drainage structures
The Japan-Caribbean Climate Change Partnership	UNDP and Japan.	2015	To bring together policy makers, experts, and representatives to encourage policy innovation for climate technology incubation and diffusion. Implement concrete mitigation and adaptation on the ground
Regional Disaster Vulnerability Reduction Project.	WB	2017	To measurably reduce vulnerability to natural hazards and climate change impacts
Conserving Biodiversity and Reducing Land Degradation	Global Environmental Facility	2017	To enhance biodiversity conservation and ecosystem services conservation
Sandy Bay Sea Defenses Resilience Project	German Development Bank	2018	To protect coastal resources from the negative impacts of climate change through local eco-system adaptation measures

13. Given the role that the Contingencies Fund could play in the event of natural disasters, we would welcome staff comments on the rules governing its use during normal times.

- Staff recommended that during normal times, revenues collected should be invested in a liquid and diversified portfolio which could be accessed quickly for emergency relief in the event of natural disasters.
- Staff also recommended that the size of the Contingency Fund should be capped at a certain level, given opportunity costs of funds. If the Fund reaches this level, revenues can be used to build resilient infrastructure or repay debt.

14. Could staff provide more details about the development of insurance tools that could be implemented in a complementary way? Would it be feasible to embed "hurricane-linked clauses" in St Vincent and the Grenadines debt contracts like in Grenada and Barbados?

- Among various risk transfer options, staff recommended expanding the insurance coverage against floods, provided by the regional Caribbean Catastrophe Risk Insurance Facility (CCRIF).
- "Hurricane-linked clauses" have been tested Grenada and Barbados, but in the context of their sovereign debt restructurings (and ex-post contexts). Experience in the primary market is limited, and benefits and costs of introducing such hurricane-linked clauses (ex-ante) should be carefully analyzed. This option would reduce financing needs but could be more expensive.

15. However, we wonder whether the baseline assumption should be considered as optimistic on natural disasters (it is based on the magnitude and frequency of the past 15 years) given that natural disasters will become more and more frequent and severe?

- The frequency and the damage of natural disasters is highly uncertain. This said, the average of total natural disaster damage has risen over time, estimated at 1.5 percent of GDP for the period 1980-2017, at 2 percent for the last 15 years, and 3.9 percent for the last 5 years.

Text Table 7: St. Vincent and the Grenadines: Major Weather-related Disasters since 1980

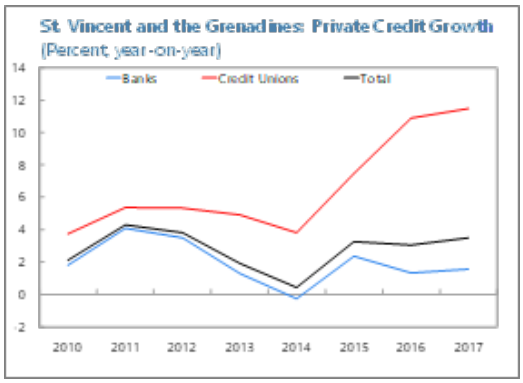
Year	Type	Total damage (% GDP)	Est. fiscal costs (% GDP)	People affected	
				Number	% population
1980	Hurricane Allen	19.8		20,500	20.9
1987	Floods	2.8		1,000	1.0
1987	Hurricane Emily	3.0		208	0.2
1999	Hurricane Lenny	0.5		100	0.1
2002	Hurricane Lili	2.4		NA	NA
2004	Hurricane Ivan	1.0		1,004	0.9
2005	Hurricane Emily	1.5		530	0.5
2010	Hurricane Tomas	3.7		6,100	5.6
2011	Floods	3.8		275	0.3
2013	Floods	15.0		17,422	15.8
2016	Floods	4.7		25,000	22.7
Annual average					
Full sample (1980-2017)		1.5	1.1		
Last 20 years (1998-2017)		1.6	1.2		
Last 15 years (2003-2017)		2.0	1.4		
Last 10 years (2008-2017)		2.7	2.0		
Last 5 years (2013-2017)		3.9	2.9		

Sources: Acevedo, S., 2016, "Gone with the Wind : Estimating Hurricane and Climate Change Costs in the Caribbean," IMF WP 16/199; EM-DAT database; and the St. Vincent authorities.

- This is why staff presented two alternative natural disaster scenarios (DSA Report, paragraph 18): (i) one-time natural disaster in 2019 (with the total damage, similar to the 2013 natural disaster experience) and (ii) recurrent more sever natural disasters. The latter assumes that natural disasters hit the country at the frequency and magnitude of the last 10 years (i.e., annual total damages and annual fiscal costs of 2.7 percent and 2 percent of GDP, respectively).
- To guard against such risks, staff recommended that the authorities should consider taking a more proactive fiscal policy and to this end, explore both revenue and expenditure measures.

Financial sector issues

16. Could staff comment on the reasons behind the rapid growth in credit provided by these institutions in recent years?



- Some foreign banks have scaled down their presence in St. Vincent and the Grenadines, and credit unions have increased their market share. In fact, for total banks and credit unions, credit growth has been relatively stable since 2015.

17. We would be interested whether staff is supporting the authorities to model the impact of climate-related risks on financial stability and to stress test the short-term impact of a climate event on the balance sheets of financial institutions.

- The business model of credit unions is focused mostly on residential mortgages and to a lesser extent, consumer loans.
- The current stress testing framework for credit unions does not explicitly take account of natural disaster risks, because mortgage loan books are covered by disaster insurance—borrowers are required to purchase insurance for their mortgages.
- For the insurance sector, the FSA is developing a stress testing framework with technical assistance of CARTAC. The model includes a hurricane scenario, which assumes a decline in real estate values, greater losses on mortgages, and a rise in property insurance claims.
- Staff have encouraged the FSA to further improve the stress testing framework. Next steps would include (i) analyzing multi-factor shock scenarios for credit unions, and (ii) analyzing interlinkages among various institutions (most importantly, credit unions, insurance firms, and banks). Going forward, stress testing models could be linked to macroeconomic scenarios, which take account of two-way linkages between the financial sector and the real economy.

18. In this regard, we would welcome staff comments on efforts presently underway to formulate a Crisis Management Strategy for NBFS.

- CARTAC provided technical assistance to develop a financial crisis management plan for the non-bank financial sector in early 2018. The final report was transmitted to the authorities in December 2018.
- We are encouraging the authorities to move ahead with formulating a crisis management plan and establishing a Financial Crisis Management Committee.

19. We also note that return on assets and return on equity in the banks have been quite volatile in the past several years. Could staff comment on the factors affecting

this volatility? Could staff also comment on why return on equity for St. Vincent and the Grenadines differs substantially from that of the ECCU?

- ROE has been volatile, which reflects a mix of one bank restructuring large corporate loans and another increasing loan provisions in different years.
- ROE for Vincentian banks is low due to one particular bank. Excluding this bank, the average ROE is much higher, equivalent to the ECCU average.

Correspondent banking relations

20. Could staff comment on whether the loss of nested correspondent accounts with domestic banks amplified the risks to financial stability arising from credit union activities?

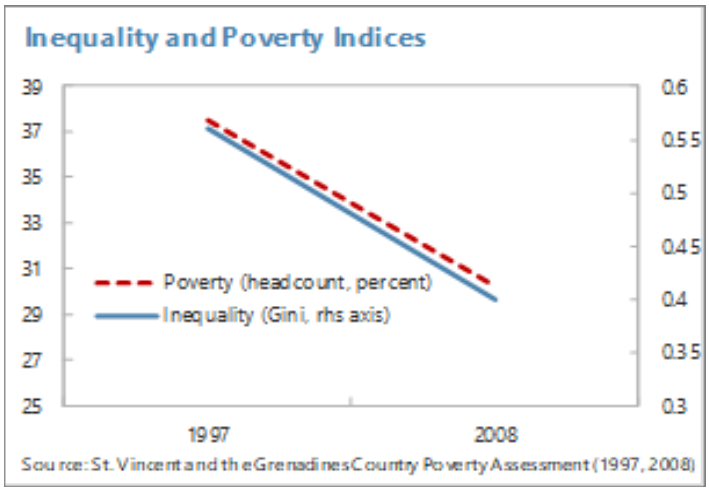
21. We regret that the loss by credit unions of nested correspondent accounts with domestic banks is not addressed in the report. Noting the growing importance of these institutions in the sector, we would expect staff to elaborate on the risk that such development pose to financial intermediation, if any

- Credit union representatives raised concern that they lost cross border payment-related businesses, as their customers moved to banks to transfer money across the border. However, credit unions have not faced the loss of their customers, maintaining strong memberships.
- The FSA also confirmed that financial stability risks pertaining to the loss of nested corresponded accounts had been muted.

Social issues

22. Could staff comment on the incidence of poverty and the existing social protection programs, as well as on the authorities' plans to intensify targeted support for gender development, childcare, and youth unemployment, as mentioned in the buff statement?

- The latest available poverty indicators are only for 2008.



- The main social protection programs are as following.

- The Social Welfare Program, which consists of different social assistance programs, including Public Assistance Program (to provide financial assistance to about 7,000 indigent people, as well as disabled, elderly, homeless children, foster homes), (ii) Community Capacity Building Program (to help community members enhance their skills and competences), and (iii) Community Enterprise Development Program (to help develop economic and social entrepreneurs).

- The National Insurance Scheme Program, which provides maternity, sickness, invalidity, age, elderly, funeral grants, as well as survivors and employment injury benefits.

- Supplementary Feeding School Program, which provides a nutritional supplement to children attending primary and pre-schools, aimed at preventing malnutrition, especially in children of disadvantaged, indigent, and poor households.

- The authorities' key plan to support gender development, childcare, and youth unemployment is as following.

- **Gender development.** The government has been promoting gender equality in the public sector. Currently, more than a half of government employees are women, and many senior positions (e.g., the FSA and the MOF) are held by women.

- **Childcare.** Prior to 2009, pre-schools and early childcare centers were private. The government has since opened 11 public pre-schools. As a member of the Organization of Eastern Caribbean States (OECS), the government is also implementing 2012-2021 OECS Education Sector Strategy. One of its objectives is to increase and expand access to quality early childhood development services.

- **Youth unemployment.** The government has launched several programs (e.g., Youth Empowerment Service Program, Coast Guard Summer Program, Police Youth Club Program, and Technical Vocational Education Training Program), aimed at developing skills through training and internships in the public and private sector. The Ministry of Education has also strengthened its training programs for secondary school teachers, in collaboration with the Caribbean Vocational and Qualification Community College. In 2019, the government is planning to launch new initiatives to support the youth, including the Sports Against Crime Program and the Youth Skills for Economic Growth Program, with support from UK DFID.