

**PRESENTATION**

**AT**

**THE INSTITUTE OF CHARTERED ACCOUNTANTS OF THE  
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**“THE GLOBAL ECONOMIC CRISIS: THE ROLE  
OF THE INTERNATIONAL FINANCIAL  
INSTITUTIONS IN THE CARIBBEAN”**

**SHERATON NASSAU BEACH RESORT  
NASSAU, BAHAMAS**

**JUNE 25<sup>th</sup>, 2010**

**The Rt. Hon. Owen S. Arthur**

You should allow me to begin by stating how very pleased I am to be able to share the same platform once again with Prime Minister Hubert Ingraham who until recently, like I do now, carried the title of Former Prime Minister. His presence fortifies my belief in the concept of the second coming.

The scope and severity of the economic and financial crisis which has engulfed the Caribbean over the past two years have and will inspire a very wide range of perspectives.

This presentation is intended to direct attention, deliberately so, to one matter which ought to be at the centre of public discourse, but which has lacked the focus it merits.

It has to do with the response of the international financial institutions to the plight that our region has faced as a result of the global economic crisis.

The promise of the Twenty-first Century is that we will live in a global community that is so truly interdependent in all of its aspects, and so held

together by a shared and common humanity, that it will take care of its own – without exception.

Nowhere has this concept been more splendidly articulated than at the London Summit of the G20 Leaders on April 2<sup>nd</sup>, 2009.

On that occasion, as they met to put together a programme to rescue the global economy, the leaders of the most powerful countries of the world warmed the hearts of men and women everywhere in a statement which said, *inter alia*:

*“We start from the belief that prosperity is indivisible; that growth to be sustained has to be shared; and that our global plan for recovery must have at its heart the needs and jobs of hard-working families, not just in developed countries, but in emerging markets and the poorest countries of the world too; and must reflect the interests, not just of today’s populations, but of future generations too.”*

They then went on to pledge their support for provision of an additional \$1.1 trillion to the IMF and the Multilateral Development Banks to enable them to carry out a programme to restore credit, growth and jobs to the world economy.

It bears repetition that this was an April 2<sup>nd</sup> and not an April 1<sup>st</sup> initiative.

Since then, we have witnessed the carrying out of a rescue and recovery programme for the world's **developed** economies, involving an unprecedented commitment of financial resources and the incurring of fiscal deficits on a scale that has hitherto been unimaginable.

We have seen also the bail out of some of the largest financial institutions in the world, whose irresponsibility and recklessness contributed, in a major way, to the extent of the economic and financial crisis which has confronted entire global society. The concept of "too big to fail" has become part of the vernacular.

Recently, we have been impressed by the alacrity with which resources have been found to salvage and to stabilize the Greek economy.

Where our region is concerned, Richard Bernal has recently offered the opinion that “the Caribbean has been more profoundly and adversely affected by the global financial crisis than the developed economies and most developing countries.”

An appreciation of the full dimensions of the crisis with which Caribbean economies have had to grapple bears out the validity of the assertion.

In such a context, it becomes relevant to enquire whether the region has received the full measure of the support promised by world leaders on April 2<sup>nd</sup>, 2010, or whether it has been short changed.

Have financial resources been mobilized and disbursed with the urgency and a scale commensurate with the extent of the economic and financial crisis which has prevailed in the region?

Has there been a major element of policy innovation in the instruments and measures deployed by the multilateral financial institutions to assist the region's economic recovery? And have the financial resources provided been **additional** to those which would have been available in any case under financial arrangements, operated by the multilateral institutions, which predate the crisis of the past two years?

Above all, what has been the motivation behind the response of the institutions? Has it been one merely intended to allow the region to stave off the worst and to remain in a holding pattern of continuing crisis? Or has it been one in which elements which can contribute to the recovery, stimulation and transformation of the regional economy can easily be discerned?

Before we address these issues, we need to appreciate fully the dimensions of the crisis which faced the Caribbean.

## DIMENSIONS OF THE ECONOMIC CRISIS

The Caribbean society has, throughout its history, lurched from one economic crisis to the next; and has in the process, developed special attributes of resilience as one of its major assets.

The recent experience has however been extraordinary, not only because of the scale and scope of the adverse effects which have represented the region's share of the global economic and financial crisis. It has been extraordinary because, while dealing with those effects, most of its economies have had to contend with three other sets of economic forces which have imposed on them the obligation to carry out major transformations to their economic structure at great costs, or to make major adjustments that have significantly narrowed the policy space within which they operate.

To begin with, the onset of the 2008 global crisis found some Caribbean economies still in the midst of dealing with the consequences of the loss of

trade preferences. By some calculations this resulted in a permanent loss of between 1% - 2% of GDP, the deterioration in their fiscal circumstances, a substantial reduction in their foreign exchange earning capabilities, and the lost of in excess of 60,000 jobs in the OECS.

Secondly, the start of the 2008 crisis found most Caribbean economies still groggy from the impact of the fuel and food prices crises that had taken a heavy toll on the households and enterprises across the region between 2006 and 2007.

The third set of forces has led to consequences that have been far more invidious.

By 2008, the Caribbean had in its midst some of the world's most heavily indebted economies. At least six of the countries had debt that exceeded 100% of their GDP, with that of St. Kitts and Nevis approaching 200%.

All of the OECS countries had entered a programme arranged by their Central Bank to reduce their debt/GDP ratio to 60% by 2020 - a task that



will entail such major expenditure reduction as to leave virtually no room for any fiscally-induced economic stimulation.

A similar programme to bring about fiscal and debt sustainability had also set in train in Jamaica and Belize where the debt/GDP also exceeds 100%. And the Government of Barbados committed itself in its Medium Term Fiscal Strategy to realise an overall surplus by 2015 in pursuit of policy to reduce its debt to more sustainable proportions.

The global crisis confronted these countries with a stark situation which amounts to a dilemma.

To carry out the programmes to bring about fiscal and debt sustainability they would have to pursue policies to reduce expenditure, which could in turn deflate the economy. On the other hand, to offset the worst effects of global recession, stimulation of the economy by fiscal and other tools was necessary. No easy answer can or has been found to such a dilemma.

## IMPACT OF GLOBAL ECONOMIC CRISIS

The global economic and financial recession in 2008 therefore only added a significant and additional new set of economic challenges to a pre-existing situation which would itself have put the economies concerned to the sternest test.

In a most insightful presentation, “Global Economic Crisis: CARICOM Impacts and Responses”, Professor Clive Thomas has asserted that the negative impacts of the global crisis have been transmitted to the Caribbean through ten major channels.

These include deterioration in the terms of trade, the volatility of exchange rates, difficulties in accessing trade credit and finance, the reduction in aid flows and the loss of opportunities for contract employment in North America.

He also cited financial contagion, as reflected in the collapse of the CLICO Financial Group and Stanford Financial Group, as one of the more damaging consequences of the global crisis.

However in terms of sheer financial volumes, the principal effects of the Global Economic crisis were transmitted through these major channels – the significant reduction in Direct Foreign Investment Flows, the decrease in remittances, and the substantial fall in foreign exchange earnings from the sale of goods and services that have occurred between 2008 and 2009.

Of these, the reversal of the recent trends in private capital flows is arguably the most significant.

Indeed, one of the major features of the pre-crisis performance of the Caribbean economy was the surge in private direct investment, principally to finance the development of new production capacity in the regional tourism sector.

Indeed, the Economic Commission for Latin America and the Caribbean has reported that the volume of private direct investment to the region virtually doubled between 2006 – 2008, rising from US\$5.9 billion to US\$10 billion over the period.

The flow was significantly reversed in 2009, when the volume of FDI to the region plunged by 42.1% to \$5.7 billion. Evidence of this major reversal is to be found in the large number of investment projects which have been temporarily halted or deferred in virtually every Caribbean country because of the global credit crunch.

There has also been a significant reversal in the flow of remittances to the region.

In this respect, it has been estimated by the World Bank that the value of remittances to the Caribbean amounted to US\$3 billion in 2008. The Caribbean Development Bank's Annual Report for 2009 however indicates

that “some regional economies reported significantly reduced inflows of remittances in 2009”.

The regional tourism sector which had averaged annual growth of 7% between 2000 – 2007, recorded a fall of 7% in 2008, and a decline in receipts in the order of 6% in 2009.

The offshore financial industry of the region was similarly adversely affected.

The global economic crisis also significantly impaired the performance of the major services and commodities export sectors of the Caribbean.

There was also evidence of a sharp contraction in the region’s bauxite/alumina industry and the production of steel in Trinidad and Tobago.

Taken together, the reversal of the flows of FDI, the reduction in the value of remittances and the significant decrease in the receipts from the exports

of goods and services led to the situation where the regional economy was effectively destabilized between 2008 and 2009 by an unprecedented decline in foreign exchange receipts, amounting to almost \$10 billion.

This amount relates only to the shortfall in foreign exchange receipts. It however does not capture the other financial obligations that have had to be assumed by Caribbean States of late, such as the extent of the financing required to fix the CLICO debacle, or that which is needed to support the programme of structural diversification which still has to be implemented to replace production capacity that has been lost through the erosion of trade preferences. Neither does it capture the extent of financial adjustment that the respective economies have to undertake to successfully carry out the programme to restore fiscal and debt sustainability over the short and medium term.

### **RESPONSES TO THE MULTILATERAL FINANCIAL INSTITUTIONS**

The sheer, overwhelming scale of these financial shortfalls and requirements present the essential context within which the responses of

the Multilateral Financial Institutions in the Caribbean have to be appraised.

At their April 2<sup>nd</sup>, 2009 Summit, the G20 Leaders agreed “to make available an **additional** \$850 billion of resources through the IMF and the multilateral development banks **to support growth in emerging market and developing countries by helping to finance counter-cyclical spending, bank recapitalization, infrastructure, trade finance, balance of payments support, debt rollover and social support.**

In respect of the IMF, \$500 billion was intended to be incorporated into a new and more flexible borrowing facility – the new Flexible Credit Line.

In addition, to increase global liquidity, the leaders agreed to support a general allocation of SDRS of \$250 billion, of which \$100 billion would go directly to emerging markets and developing countries.

In respect of the Multilateral Development Banks, the G20 Summit agreed to support a substantial increase in lending of \$100 billion to low income

countries. Beyond these commitments, the leaders also agreed to ensure \$250 billion of support for trade finance.

The issue that now arises is that as to what difference these commitments have made to the financial circumstances of Caribbean societies.

### INTERNATIONAL MONETARY FUND

In respect of the IMF, no Caribbean country has drawn upon the new Flexible Credit Line. This was intended to be the facility through which the bulk of **additional** IMF financing was to be channeled.

It was also especially intended to herald a fundamental change in the procedures for accessing IMF funds and meeting IMF programming tests.

This new Flexible Credit Line Facility was designed to allow countries to borrow without the limits that hitherto had to be applied based on their quota in the Fund. In addition, the typical programming tests and targets of the past were to be done away with and replaced by a new arrangement



under which countries seeking to access the facility would prequalify based on their pre-existing economic behaviour and fundamentals.

A facility with such features was judged to be more relevant to the time and circumstances, and excited the hope that its application would see the removal of much of the stigma of having to accept an IMF programme.

The new facility into which \$500 billion has been pledged to support recovery in the developing world while not being used by the Caribbean has however been used by countries in Latin America, Africa, Eastern Europe and Asia.

Over the years, and preceding the crisis of 2008, the IMF has developed a number of facilities which have been tailored to address specific circumstances of its members. These include the Poverty Reduction and Growth Facility (PRGF), the Exogenous Shock Facility and a facility to provide emergency assistance to support recovery from natural disasters and conflicts. Loans under these facilities involve little conditionality.

To help mitigate the adverse effects of the Global recession, St. Vincent and the Grenadines, The Commonwealth of Dominica and St. Lucia, requested financing under the Exogenous Shocks Facility.

Grenada requested support under the PRGF programme and St. Kitts and Nevis under the Emergency Assistance for Disaster.

Overall, IMF support dispersed under the EDF and the other pre-2008 crisis facilities to the OECS totalled about \$25 million in 2009. This was tantamount to almost 3% of the Union's foreign exchange reserves and the disbursements ranged between 0.5% and 1.5% of the economies concerned.

In the case of Belize, emergency assistance equivalent to 0.5% of its GDP was attained from the Fund in 2009.

For balance, it has to be acknowledged that the IMF made the allocation of SDRS in September 2009 as agreed at the G20 Summit.

This effectively led to a major addition to the countries' foreign exchange reserves. For instance, the BDS\$170 million Barbados received through this medium made a significant difference to the country's circumstances by halting the free fall in the country's foreign exchange reserves that was taking place in 2009.

This year, the Fund has agreed to two Stand-by Arrangements with Caribbean countries; one of almost \$1.3 billion with Jamaica, and the other of almost \$120 million in the case of Antigua and Barbuda.

In Jamaica's case, the funding was provided on the condition that the Government followed through on its fiscal reform programme. In this regard, the Government committed to creating a new Financial Sector Support Fund, and to use some of the IMF loan to provide emergency liquidity to financial institutions should they run into liquidity difficulties as a result of their participation in Jamaica's Debt Exchange Programme that was launched in January 2010.

It is also intended that a significant proportion of the Antigua and Barbuda's loan should be used to support the implementation of that country's fiscal consolidation and debt sustainability initiatives.

On balance, the response of the IMF to the crisis in the Caribbean has chiefly been felt in the allocation of SDR's which has helped to stem the slide in some countries' external reserves. Access to Fund resources under the SBA's should help Jamaica and Antigua cope with their debt sustainability programmes.

Beyond this, it however cannot fairly be said that IMF response has or will assist in any major material way in achieving the grand overarching objectives stated on April 2<sup>nd</sup>, 2009 of fostering counter-cyclical stimulation, spurring employment creation nor attending to the needs of structural diversification in Caribbean economies.

To the extent that the global community planned that its programme to stabilize and stimulate the economies of the developing countries, such as

the Caribbean, should take effect largely through the medium of IMF facilities, clearly the response of the global community has come up significantly short in the scope of its achievements in our region.

### **THE INTER-AMERICAN DEVELOPMENT BANK**

Consistent with the mandate of the G20 Leaders, the IADB has sought to expand its pre-existing loan portfolio in the Caribbean as part of its response to the global crisis.

As such, during 2009, the Bank approved eleven loans for the Caribbean with a total value of \$495 million, following on \$404 million in loans in 2008. This loan portfolio covered both policy based lending and investment loans for a wide range of activities.

That said, the **principal** response in the region of the IADB to the global crisis was not intended to be the expansion of its pre-existing loan portfolio but to be expressed in the form of a new Liquidity Programme for Growth Sustainability.

Established in 2008, with a pool of funds \$6 billion, the programme was intended to provide up to US\$500 million per country to provide liquidity to regulated financial institutions which were facing reduced access to foreign credit lines and interbank credit. The national Governments had to be borrowers or guarantors for all loans.

It was proposed that the facility should be temporary in nature with the authority to approve loans expiring at the end of December 2009.

Critically, the main requirement for approval was to be an assessment letter from the IMF.

Loans under this programme were to attract an interest with a significant spread over LIBOR, and were to be repaid in 2 years after a three year grace.

Loans of this nature are expensive, unwieldy and perhaps not inappropriate to Caribbean circumstances since the Caribbean banking

system was not severely affected the global financial crisis, and therefore had no need for a source of liquidity of this calibre.

The new facility therefore proved to be of virtually no importance to the Caribbean.

Jamaica had expressed an interest in taking up \$300 million under this programme.

However, on the date of expiry for loan approvals under this programme, no Caribbean country had chosen to participate in this facility.

### **THE WORLD BANK**

In similar vein, the World Bank has sought to expand its pre-existing and traditional portfolio of investment and technical assistance loans to eligible borrowing countries in the Caribbean as part of its response to the global crisis.

However, the Bank was mandated to employ financial innovations that took it beyond its traditional role in responding to the regional economic and financial needs.

The chief financial instrument that was proposed to be deployed as part of the Bank's new innovative role as it assumed a crisis-response posture was to be the Development Policy Loan.

This facility was designed to provide quick-disbursing finance to help a borrower meet development financing needs in areas such as the reduction in poverty, the improvement in service delivery, diversification of the economy, institutional reform, and the enhancement of the investment climate - precisely the kind of financing arrangements required the Caribbean at this time.

Funding from this facility was intended to take the form of general budget financing that would be subject to the borrowers own implementation



process - an arrangement that entirely fits the requirements of the Caribbean at this time.

However, access to the funds was made conditional on the borrower's "maintenance of an adequate macro-economic framework, as determined by the Bank with inputs from IMF assessments", as well as the successful implementation of the overall reform programme. Effectively a country had to have an IMF programme in place to be able to access this new facility.

For this reason, to date, no Caribbean country has made use of the resources of this facility to address any of the effects which have emanated from the global crisis.

### **THE CARIBBEAN DEVELOPMENT BANK**

Like the other multilateral institutions the CDB has also sought to respond to the crisis by expanding its pre-existing investment loans portfolio - in its case by the extent of \$260 million over the next 2 years.

To respond specifically to the crisis, the Bank proposes to use Policy-Based loans, amounting to \$100 million to provide budgetary support to Government.

The Bank also proposes to provide up to \$50 million over the next 2 years in intermediary lending to support micro, small and medium enterprises, and to expand access to student loans for tertiary education.

Through its Basic Needs Trust Fund, it will provide up to \$70 million in grant resources over the next 6 years to address social protection issues at the community level.

### CONCLUSION

In today's climate, every little bit will help.

However, given the magnitude of the financial requirements of the region, it can safely be concluded that the limited nature of the financial support

provided for the Caribbean by all the initiatives previously described puts the region in a position where it will affectively be asked to jump across a vast chasm by a series of small jumps.

For, on balance, the region has not benefitted in any major way from the pledge of substantial additional funding, through the Multilateral Institutions.

Indeed it has not been able to access any of the new lending facilities established to disburse the additional funding that the leaders of the G20 countries purported to put at the disposal of the developing countries to enable them to cope with the effects of the global crisis.

The countries of the region did not cause the global crisis but nonetheless suffered severely from its consequences.

The commitment given by the leaders to the global society, that such countries would have access to ample resources to enable them to implement counter-cyclical programmes to stimulate the economy, new

initiatives to structurally diversify their production systems, facilities to strengthen their social safety nets, and to meet the needs of the poor and the dispossessed in their midst, as well as new arrangements to address their debt problems need to be honoured.

The Caribbean, where the greatest need exists but where the least support has been received, must champion the call for the honouring of that commitment.

It would however lend credibility to the region's call for the honouring of the Global Leader's April 2<sup>nd</sup> pledge if we ourselves do much more to strengthen interdependence within our own region.

For if this global crisis has left any mark, it surely must be that no country can feel that it is free of the consequences of actions that take in other jurisdictions. In the case of the Caribbean one does not have formally to subscribe to the provisions of a Treaty to be subject to the vagaries and implications of being part of an integrated economic space.

Indeed, the debacle of CLICO has established that economic integration can be brought about as much by corporate actions, as by formal Treaty Arrangements.

The region therefore needs the co-operation of all to put in place the CSME Agreement relating to the operation of its financial services sector to prevent future disasters such as that which CLICO has foisted on our people.

In addition, even as we are negotiating new investment agreements in our new trade pacts with Europe and Canada, we need to put one in place to help us to regulate the flow of capital among our constituent members.

One of the consequences of the global financial crisis is that our countries face the common threat of a continuing challenge from the OECD to the functioning of our international financial sector. For some countries that threat will be amplified by challenges within the WTO over the incentives they have used to create and sustain offshore business. Several of our

nations have been given a waiver on the use of these incentives up to 2015. Beyond that lies an uncertain future.

Where there is common threat, we must devise and pursue a common response.

Should this global crisis engender such a common response to the common threats faced by the societies of the region, it will have served to usher in a better way of doing things in the Caribbean and will help to ensure that our best days are still ahead of us.

I thank you for the opportunity to deliver myself of these remarks in this place where the modern history of the Caribbean truly began.

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