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Grenada: 2001 Article IV Consultation—Staff Report; Public Information Notice on the Executive Board Discussion; and Statement by the Authorities of Grenada

Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. In the context of the 2001 Article IV consultation with Grenada, the following documents have been released and are included in this package:

- the staff report for the 2001 Article IV consultation, prepared by a staff team of the IMF, following discussions that ended on **March 30, 2001** with the officials of Grenada on economic developments and policies. **Based on information available at the time of these discussions, the staff report was completed on June 26, 2001.** The views expressed in the staff report are those of the staff team and do not necessarily reflect the views of the Executive Board of the IMF.

- the Public Information Notice (PIN), which summarizes the **views of the Executive Board as expressed during its July 11, 2001 discussion** of the staff report that concluded the Article IV consultation.

- a statement by the authorities of Grenada.

The document listed below have been or will be separately released.

Statistical Appendix

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GRENADA

Staff Report for the 2001 Article IV Consultation

Prepared by the Staff Representatives for the
2001 Consultation with Grenada

Approved by Claudio M. Loser and Jesús Seade

June 26, 2001

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EXECUTIVE SUMMARY

Grenada's economic performance improved in recent years owing to the authorities' strategy of promoting private investment through sound fiscal management and improvements in infrastructure. Real GDP growth averaged 7 percent a year during 1998–2000, while unemployment declined from 16 percent to 12 percent, and inflation remained in the low single digits. Indications are that real GDP growth will slow to about 5 percent in 2001, in line with a lower rate of execution of public sector and tourism projects, and a further softening in tourism demand, which began to be evidenced in 2000. A sharp increase in credit, coupled with rapid import growth associated with a pickup in projects, led to a doubling of the external current account deficit to almost 16 percent of GDP in 2000; the deficit was financed by direct investment, grants and concessionary loans.

Government saving rose from 1½ percent of GDP in 1998 to an estimated 6 percent in 2000 owing mainly to continued efforts to strengthen tax and customs administration. However, the central government budget registered deficits averaging 3½ percent of GDP during this period, financed mainly by concessionary loans and banking system borrowing. The government's fiscal plan for 2001 envisages a further strengthening of the budget position through a lowering of the overall deficit to 2 percent of GDP, and maintaining government saving at just under 6 percent of GDP. Information for the first quarter of the year indicates that revenue was weaker than envisaged, reflecting a decline in imports and tourist arrivals.

The discussions centered on measures to alleviate poverty and reduce unemployment by maintaining satisfactory rates of growth and increasing opportunities for job creation through greater economic diversification. The authorities' strategy to achieve these objectives will continue to focus on creating the conditions for attracting private investment in agriculture, tourism, and promising new areas such as agro-processing, internet-based marketing, and data processing. This strategy needs to be supported by the pursuit of sound fiscal policies over the medium term in order to maintain private sector confidence and investment. The authorities intend to continue the structural reform efforts aimed at improving efficiency in the public sector, and to bring the financial sector in line with international standards by expediting the implementation of additional measures to strengthen the monitoring and regulation of offshore financial services.

The authorities shared the staff's concerns that a sound fiscal situation would be difficult to achieve unless steps were taken to address some weaknesses in tax administration that appeared to be emerging in 2001, as well as the growing inflexibility in the structure of spending due largely to the rapid growth in interest and lease payments. They acknowledged the need for a full review of the tax exemption and concessions regime as a first step in arresting the continued erosion of the tax base, but stressed the importance of a regional approach to tax policy, including the introduction of a VAT. On the expenditure side, the authorities indicated their intention to make further efforts to reduce the wage bill by attrition, and to avoid new, commercially financed, lease-to-own projects.

I. Introduction

1. The consultation discussions were held in St. George's during March 20–30, 2001. The mission[1] met with the prime minister, the minister of finance, trade and planning, the permanent secretary in the ministry of finance, and other senior government officials. Discussions were also held with representatives of the private sector, the labor unions, and the political opposition. Mr. Whitehall, Advisor (OED), participated in the final round of discussions.

2. Grenada is on the 12-month consultation cycle, and the last Article IV consultation was concluded by the Executive Board on July 5, 2000. Relations with the Fund, the World Bank, and the CDB are summarized in Appendices II through IV.[2]

3. Grenada is a member of the Organization of Eastern Caribbean States (OECS) and the common central bank, the ECCB. The common currency, the Eastern Caribbean dollar, has been pegged to the U.S. dollar at the rate of EC$2.70=US$1 since July 1976.

4. At the last general election held in January 1999, the New National Party led by Prime Minister Mitchell won all 15 seats in parliament. The next election is due no later than October 2004.

II. Background

5. **Grenada comprises three small islands in the eastern Caribbean with a total land area of 345 square kilometers,** a population of 102,000, and a nominal GDP of about US$400 million. The economy is heavily dependent on tourism and exports of spices, but in recent years it has diversified into manufacturing and services, particularly telephone- and internet-based marketing, and offshore financial and educational services.[3] The cultivation and export of banana, the main economic activity until the early 1990s virtually ceased in 1997 as a result of low productivity and fruit quality, disease, and uncertainty regarding access to preferential markets in the European Community.[4] The industry has begun to recover slowly, and output in 2000 was equivalent to about one-third of the 1996 level.

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[1] The staff team comprised Mr. DaCosta (Head), Mr. Berezin, Ms. Francis, and Mr. Njoroge (all WHD). Mr. Boote (WHD) joined the mission for the final meeting. The team was assisted by Mr. Campbell and Ms. Marquez of the Eastern Caribbean Central Bank (ECCB), and Ms. Dawson of the Caribbean Development Bank (CDB).

[2] Grenada has accepted the obligations of Article VIII, sections 2(a), 3, and 4.

[3] These comprise facilities for establishing international business companies (IBCs) and offshore banks. The main offshore educational institution is the St. George's University and Medical School, which has a student body of about 2,000.

[4] The contribution of agriculture to GDP fell from 12 percent in 1991–92 to 7½ percent in 2000. Over the same period, the share of services rose from 56 percent to 68 percent.

6. **Economic performance improved in recent years** in response to the government's strategy of promoting private investment through sound fiscal management and improvements in infrastructure. During 1998–99, the behavior of most economic and financial indicators compared well with those for the ECCB region as a whole, and may be summarized as follows (Figure 1, and Appendix 1):

Real GDP growth averaged 7½ percent in 1998–1999, on the strength of a pickup in manufacturing, tourism and construction, as well as in telecommunications and financial services (Table 1);

The **unemployment** rate fell from 17 percent at the end of 1997 to 14 percent in 1999, and inflation remained below 2 percent reflecting mainly the fixed peg to the U.S. dollar;

Government saving rose from zero in 1997 to almost 5 percent of GDP in 1999, and the overall deficit (before grants) narrowed, owing to a strengthening of revenue administration, increased fees from offshore companies, and efforts to reduce the size of the wage bill and contain other current outlays (Table 2); and

The **external current account** narrowed from 25 percent of GDP in 1997 to 8 percent in 1999 reflecting a marked increase in exports of electronic components and higher nutmeg prices, as well as a slowdown in imports following the completion of two large office complexes and a sports stadium.[5] The deficits were financed by inflows of foreign direct investment, official grants and (largely concessionary) loans, and commercial borrowing by the private sector (in part, to finance the above-mentioned projects).

7. **Despite these achievements, social conditions have remained difficult.** Estimates from a poverty survey conducted with the assistance of the CDB in 1999 indicate that while progress has been made in education and health, one-third of the population lives in poverty. Most of the poor and unemployed comprise women, youths, and children who live in rural areas which have been affected by the decline in the banana industry.[6]

8. **In concluding the last Article IV consultation, Directors commended the authorities for pursuing policies that helped achieve a sustained economic recovery** and low inflation. However, they observed that unemployment remained high, and that indicators of poverty were among the least favorable in the Caribbean region. Directors welcomed the government's decision to place poverty alleviation at the forefront of its economic program, and supported the strategy of fostering economic growth through sound fiscal policies, increased private investment, and reforms to modernize the public sector and ensure a well regulated financial system. Directors welcomed the recent increase in central government saving, and stressed the need for continued fiscal efforts, including strengthening tax compliance, and limiting the growth of the wage bill.

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[5] The cost of these projects (which were constructed by the private sector and leased to the government) was equivalent to about 12 percent of GDP.

[6] Grenada was ranked 54th (of 174 countries) in the United Nations' Human Development Index for 2000, about the same ranking as in 1995.

9. **Grenada's statistical database remains weak** in terms of coverage and timeliness. These weaknesses—especially with respect to the national accounts, the balance of payments, and public and private debt—render effective monitoring of economic developments and policy analysis difficult. Grenada has begun to participate in the Fund's General Data Dissemination System (GDDS).

III. Developments in 2000–01

10. **The economy continued to perform well in 2000**. Real GDP grew by 6½ percent, unemployment declined further, and inflation remained in the low single digits. However, the growth of tourist arrivals slowed markedly because of the withdrawal of the direct air service between Grenada and the U.S. mainland, and the cancellation of weekly visits by the largest cruise ship.[7] Also, output in the agricultural sector fell slightly as the spice crop declined. Indications are that the rate of growth will fall to about 5 percent in 2001, reflecting mainly a slowdown the in implementation of public sector projects and continued weak tourism demand.

11. **The strong growth in economic activity was accompanied by a fairly robust expansion in banking system deposits and credit** (Table 3). Most of the credit flowed into construction and consumer goods purchases. Increased competition among financial institutions led to a moderate decline in bank lending rates, with the prime rate at some banks ranging from 8½–9½ percent at end-2000, compared with 10 percent at end-1998.

12. **A marked increase in imports associated with infrastructure and tourism projects, and the growth in private sector credit led to a doubling of the external current account deficit** to almost 16 percent of GDP in 2000 (Table 4).[8] Exports have performed well over the past two years, reflecting increases in nutmeg prices, shipments of electronic components to the U.S. market, and exports of fish products. Receipts from services experienced virtually no growth in 2000, due to the slowdown in tourist arrivals.

13. **Data on the external public debt are not comprehensive and reliable, but partial estimates indicate that it rose from 26 percent of GDP during 1997–99 to 28 percent at end-2000,** owing to the loan disbursements associated with the pickup of the public sector investment program. The debt service ratio has remained largely unchanged at 3–4 percent over the past three years. After registering little change during 1998–99, the external value of the E.C. dollar as measured for Grenada appreciated by about 6 percent in real effective terms during 2000, owing mainly to the appreciation of the U.S. dollar relative to other major currencies (Figure 2).[9]

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[7] The government is discussing with airline and cruise ship companies options for filling the gaps created by these developments.

[8] The deficits in 1999–2000 were financed by private investment flows, and grants and loans associated with the public investment program.

[9] The absence of reliable data on wages and producer/wholesale prices preclude alternative measures of the real effective exchange rate index. The staff plans to carry out an assessment of competitiveness of the exchange rate of ECCB member countries in the context of the next policy discussions with the regional institutions.

14. **The central government finances improved further.** The current account surplus rose to 6 percent of GDP in 2000, mainly reflecting continued efforts to strengthen tax and customs administration through the hiring of additional staff, increased audits of large taxpayers, and the payment of cash incentives to tax collection agents. Also, the wage bill was reduced, as about 200 temporary government employees were released. The overall deficit (before grants) rose slightly in 2000, as the savings performance was offset by increased spending on infrastructure projects.

15. **The government's fiscal plan for 2001 envisages a further strengthening of the budget** through a lowering of the overall deficit to 2 percent of GDP, and maintaining government saving at just under 6 percent of GDP. The key features of the budget are an increase in revenue by ½ of a percentage point of GDP owing largely to increased collections of licenses and fees, and a slowdown in the implementation of government projects. Information for the first quarter of the year indicates that revenue was weaker than envisaged (by the equivalent of about 3-4 percent of GDP at an annual rate), due to a decline in imports and tourist arrivals.

16. **The government's reform efforts have focused on reducing the scope and size of the public sector, and making the civil service more efficient.**[10] The privatization of the major state enterprises was completed in 1998, and selected government activities (such as road construction and maintenance) have been contracted out to the private sector. Currently, discussions are taking place with the labor unions on (i) the options for addressing the virtual insolvency of the sugar industry; (ii) modalities for making certain government departments more efficient by converting them into independent agencies run on commercial lines; and (iii) developing a performance-based pay system for the civil service (Box 1). Beginning in the second half of 2000, the Grenada International Financial Services Authority (GIFSA) initiated measures designed to correct weaknesses in the structure and supervision of offshore financial institutions that were revealed by the collapse of the largest offshore bank. The key measures include (i) audits of all offshore banks by an international firm; (ii) improved staffing to facilitate on-site inspections of offshore banks and closer monitoring; and (iii) recommendations for changes in legislation to address weaknesses in the legal framework.

[10] Total employment in the civil service was about 5,200 in 2000.

Box 1. Grenada: Public Sector Reform

Sustained efforts to reform the public sector began in 1985. The reform agenda included privatization, statutorization (under which selected government agencies would be converted into statutory bodies operated on a commercial basis), downsizing of the civil service, and the establishment of a merit-based pay system. A summary of the main initiatives in these areas is set out below.

Privatization

(i) Divestment

- During 1983–1992, about 20 nonfinancial public enterprises were privatized through direct sales. Some of the key entities privatized included (i) the National Fisheries Company, (ii) the Grenada Forestry Corporation, and (iii) the Grenada Telephone Company (70 percent of the shares were sold to Cable and Wireless Ltd.). Proceeds from the sale of these entities were estimated at US$37million, and were used to finance capital expenditure.

- Beginning in 1992, privatization increasingly took the form of the sale of shares in public utilities and banks, except in 1998 when the radio and television station was privatized. The government sold 90 percent of the equity of the National Commercial Bank in 1992; and 50 percent of GRENLEC and its remaining 30 percent share in the National Brewery in 1994. At end-2000, three public enterprises remained to be privatized—the sugar company, the gravel and concrete company, and the marketing board.

(ii) Statutorization

- Under this program, which began in 1996, the Post Office and the government printery were transferred out of the civil service; the conversion of the hospital and the community college is pending.

- Following resistance from within and outside the public service owing to concerns about job status, job security, and loss of public service benefits consequent on moving to a new agency, the government initiated an Executive Agency program under which selected government agencies/ services would be managed independently on a commercial basis, but would remain under the relevant line ministry. Some progress has been made recently in this area, with the move toward autonomy for the community college, and the contracting out of certain government services—construction and maintenance—to the private sector.

Civil service reforms

- These have centered on downsizing, mainly through attrition and a freeze on hiring, which led to a 20 percent reduction in the number of civil servants between 1992 and 1995;

- introduction of a more simplified and efficient salary scale (with the number of pay grades reduced sharply from 85 to 13), and a merit-based performance appraisal system designed to end the practice of automatic increments; and

- introduction of a peer-appraisal system (Emulation Program) and sensitivity training, designed to enhance human resource development through increased staff motivation.

Progress in the area of civil service reforms has been stymied by weaknesses in the structure of the new salary scales, which provide too much scope for large salary increases, and in the application of the performance appraisal system. In an effort to address these problems, greater emphasis is being placed on training supervisory personnel in the performance appraisal system. Another important development has been the introduction of internal and external feedback mechanisms, including the establishment of a Committee (comprised of senior managers in the public service, the unions, and the private sector) to review and assess the effectiveness of the public sector reform process.

IV. Policy Discussions

17. **The discussions centered on measures to alleviate poverty and reduce unemployment by maintaining satisfactory rates of growth and job creation.** The authorities indicated that their strategy to achieve these objectives would continue to focus on creating the conditions that would attract private investment in agriculture, tourism, and promising new areas such as agro-processing, internet-based marketing, and data processing.

18. **Government officials were confident that a rate of growth of real GDP of 4–5 percent over the medium term would be feasible** on the strength of (i) several ongoing and planned residential and tourist-related construction projects; (ii) proposals to expand output in the manufacturing sector—particularly electronics assembly and the processing of spice products; and (iii) favorable prospects for the further development of the telecommunications services sector, including through the establishment of additional call centers (Table 5). Growth in agriculture would continue to be moderate as the crop cycle for spices (the main export crop) does not permit a rapid expansion of production in response to the current high prices, while the ongoing banana rehabilitation project would result in a gradual recovery in output. However, new export opportunities were emerging for processed fish, fresh flowers, and fresh and processed fruit.

19. **The staff noted that such an outturn, supported by measures to raise government saving to facilitate increased investment in education and social services, would allow an increase in real GDP per head by an average of 3–4 percent a year.** The unemployment rate was likely to continue to decline gradually, owing to the projected slowdown in the rate of growth of output, and the still limited capacity for new jobs to be created in the formal sector at a rate significantly in excess of that of the labor force.[11] There was broad consensus that a number of risks threatened this scenario, including (i) the effects of the downturn in the U.S. on tourism demand; (ii) the likelihood of damage to infrastructure and property caused by the annual cycle of tropical storms through the region; and (iii) continued shortages of skilled labor, especially in construction and services.

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[11] High unemployment rates—ranging from 10–25 percent—co-existing with moderate rates of growth are common in the Caribbean region. The widespread inadequacy of data on the labor force and employment in the region has precluded in depth studies of this issue, including by the World Bank, and regional development banks. The Fund staff has begun work in these areas, which, together with the data expected shortly from the ongoing population census, is expected to address this important shortcoming in the economic analysis of the region. In the case of Grenada, work by the Fund staff shows that, on average, unemployment has fallen by a rate close to that predicted by models which incorporate the differential between actual and potential rates of real GDP growth.

A. Fiscal Policy

20. **The authorities view the adherence to sound fiscal policies over the medium term as essential for maintaining private sector confidence and investment.** They shared the staff's concerns that a sound fiscal position would be difficult to achieve unless steps were taken to address the slowdown in revenue that appeared to be emerging in 2001, as well as the rapid growth in interest and lease payments. Looking ahead, and taking into account likely flows of concessional loans and grants, the authorities and the staff agreed that limiting the budget deficit to about 2–3 percent of GDP, and maintaining a savings rate of about 5 percent of GDP would be consistent with the ECCB's guidelines on fiscal sustainability, allow sufficient room for a capital investment program that would address the government's social and infrastructure priorities, and avoid a worsening of the debt burden (see Table 5).

21. **The mission welcomed the efforts that had been made by the tax and customs agencies to improve revenue administration.** While part of the recent slowdown in revenue appeared to reflect the peaking of efforts to strengthen tax administration and collect tax arrears, the mission cautioned that it also stemmed from the persistent erosion of the tax base through concessions and exemptions.[12] The staff suggested that the government initiate a review of all exemptions, and discontinue those which are no longer justified on grounds of investment or job creation. In addition, it is important that steps be taken to reduce the *ad hoc* nature in which new concessions are granted, which gives rise to a wide variation of concessions across industries, as well as among firms in the same industry. Since concessions are an important feature of investment promotion throughout the ECCB area, the staff suggested that the government propose a region-wide re-appraisal and harmonization of the incentives regimes, aimed at reducing their scope and avoiding the erosion of the revenue base. It would be useful to incorporate into such a re-assessment, discussion of the feasibility of a value added tax in all member countries of the ECCB.[13] The staff recommended also that the exemption of civil servants' salaries from the income tax be eliminated, and that the objective of improving salaries be addressed through transparent salary adjustments. The authorities broadly agreed with the staff's assessment, and indicated that the Fund's support for technical assistance in a region-wide assessment of the incentives regime would be important.

22. **The staff noted that while government expenditure in recent years had been restrained, the structure of spending had become more inflexible** due mainly to the rapid increase in interest and lease payments associated with the recent infrastructure projects.[14] Consequently, the scope for discretionary spending had fallen sharply, and spending on goods and

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[12] See Appendix VIII.

[13] Technical assistance experts have indicated that an important prerequisite for the introduction of a VAT would be the reduction and harmonization of tax incentives.

[14] These payments are expected to rise from 1.8 percent of GDP in 1998 to 4.3 percent of GDP in 2001, or from 5 percent of total expenditure to 13 percent.

services had already been affected.[15] These developments could make it difficult to implement further spending cuts that may be required to offset a weakening of revenue, and create pressures to cut back infrastructure and social investment. The authorities said that they planned to reduce the inflexibility of expenditure through further efforts to reduce the wage bill by attrition, and by avoiding new, commercially financed, lease-to-own projects. They stressed the urgency of the long awaited, comprehensive review by the World Bank of the scope and composition of public expenditure, and hoped that the Bank could complete this task during 2001.[16]

23. With respect to the rest of the public sector, the staff observed that sustaining a sound financial position of the National Insurance Scheme (NIS) would require measures to eliminate arrears on contributions and interest owed by the government, public sector agencies, and the private sector.[17] An actuarial study of the scheme, completed earlier this year—but not yet released—is expected to have addressed the desirability of increasing the salary ceiling for NIS contributions, and of allowing the NIS to invest a proportion of its surplus in regional and international securities. The operations of the main public enterprises, the Port Authority and the Water Authority, also registered overall surpluses averaging 1 percent of GDP a year in 1999–2000. However, a full analysis of the finances of the public enterprises was precluded by the absence of regular reports to the ministry of finance. The staff recommended that this weakness be addressed promptly.

B. Monetary and Financial Issues

24. **Within the context of the common currency and fixed exchange rate arrangement, there is no scope for independent monetary policy in Grenada.** Temporary imbalances in banking system liquidity are offset by movements in credit, imports, and capital flows, while interest rates—except for the 4 percent interest rate floor on small savings deposits established by the ECCB—are determined by market factors. The discussions centered on the condition of the financial system, and steps being taken to strengthen its monitoring and regulation.

25. **Available indicators from the ECCB point to a broadly sound domestic banking system,** with capital/assets ratios averaging 30 percent, and nonperforming loans comprising about 9-10 percent of total loans (Table 7).[18] The mission expressed concern about the operations of one bank which, to date, has not been reporting its financial position to the ECCB, nor participating in the payments settlement system. It recommended that, based on an audit of the bank which has been undertaken, the government move promptly to (i) verify that the bank is sufficiently liquid to meet depositors' claims on a regular basis, and is adequately capitalized; and (ii) require that the bank begin to report its financial condition to the ECCB, and permit the ECCB

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[15] Nondiscretionary spending (i.e., the sum of wages, lease and interest payments, and transfers) as a ratio of current expenditure rose from 82 percent in 1996 to 87 percent in 2000.

[16] The Bank has not yet set a date for carrying out the expenditure review.

[17] The NIS registers annual surpluses of about 2½ percent of GDP. The outstanding stock of arrears stood at EC$34 million, or 3 percent of GDP, at end-2000.

[18] The domestic banking system comprises 6 banks, two of which are branches of foreign banks, and two others are subsidiaries of banks based in Trinidad and Tobago.

to carry out a thorough inspection of its operations. Failure to satisfy these requirements within a specified period should lead to the withdrawal of the bank's license, and the initiation of a process to recover depositors' funds.

26. **The mission welcomed the appointment in late-2000 of a new management board for the supervisory body for offshore financial services (GIFSA),** and the transfer of its offshore promotion activities to a separate body, leaving GIFSA free to concentrate on regulation. The new board has moved quickly to strengthen the staffing, which has permitted the start of on-site inspections of offshore banks (Box 2). Also, with the assistance of an international accounting firm, comprehensive audits—which will be completed in June-July 2001—are being undertaken of all offshore banks. Already, based on the results of the audits, 17 banks were closed in March 2001, and decisions on the future of the remaining banks will be made after the audits are completed. Supervisory officials agreed with the staff that, following the audits, the results of the self-assessment exercise initiated with the assistance of MAE and the ECCB, together with the proposed completion of a Financial Sector Assessment Program (FSAP) for ECCB member countries in 2002, could form the basis for establishing a strengthened regulatory framework, in which the central bank would play a greater role.

27. **GIFSA is working closely with the ECCB to ensure that the legislation and operating guidelines to financial institutions concerning money laundering are kept in line with current international practice.**[19] In addition, an Anti-Money Laundering Supervisory Authority has been established, and has started to investigate reports of suspicious financial transactions and possible money laundering.

C. External Sector Prospects and Policies

28. **The authorities noted that the widening of the external current account deficit in 2000–01 was not a cause for concern.** The deficits reflected imports associated mainly with a new phase of private investment in tourist facilities as well as public infrastructure projects, and were financed by capital transfers and inflows of private investment. The mission shared this assessment, but expressed concern about the quality and timeliness of the data on external transactions, particularly relating to trade and the capital account. With respect to the latter, concerns centered on the large size of unexplained private capital inflows and the lack of comprehensive and timely data on government and government guaranteed debt. The authorities agreed that additional resources should be devoted to addressing these weaknesses, noting that, given the staffing shortage in Grenada, heavy reliance would be placed on technical assistance from the ECCB and other regional or multilateral agencies.

[19] A Money Laundering Prevention Act was approved by parliament in 1999.

Box 2. Grenada's Offshore Sector

A. Structure and recent developments

The development of the offshore financial sector got underway in 1997 with the enactment of new legislation governing its operations. The sector subsequently grew rapidly in terms of businesses registered and fees paid to the government. At its peak in early-2000, about 300 people were employed in the sector, which comprised 44 banks, and 3,120 International Business Companies (IBCs); and for the year as a whole the sector contributed the equivalent of about 1 percent of GDP to government revenue. The event that dominated developments in 2000 and early-2001 was the collapse of the First International Bank of Grenada (FIBG), the largest offshore bank, following its inability to meet depositors' claims. In February 2001 the bank's license was revoked and a liquidator was appointed. Liquidation of the bank is still in progress.

B. Regulation and supervision

The collapse of FIBG highlighted the poor supervision of the sector, and led to a number of initiatives by the government, including the initiation of audits of all offshore banks. In addition, GIFSA has (i) strengthened its requirements and penalties relating to adequate capitalization and the timely filing of quarterly financial returns; (ii) begun closer collaboration with regulators in other jurisdictions; and (iii) started a review of the existing legislation with a view to identifying weaknesses. The legislative amendments under consideration would (i) restrict or ban the use of bearer shares, which have been the object of abuse; (ii) give the Minister of Finance authority to inspect IBCs; (iii) ensure that IBCs do not operate as banks; and (iv) enforce more vigorously the requirement that offshore banks do not accept deposits from residents. The main near term priorities are to complete the IMF-initiated self-assessment of supervisory practices as a first step toward a region-wide FSAP for ECCB member countries in 2002. The results of these exercises will form the basis of the development of a revamped offshore financial services sector over the medium term.

29. **The medium-term scenario developed by the staff** envisages a rate of real GDP growth of 4–5 percent a year, continued low inflation, and a central government deficit (after grants) of about 2½ percent of GDP a year. Under this scenario: (i) the growth of merchandise exports would slow from 13 percent a year in 2000 to 8 percent per year over the medium term owing to a projected decline in nutmeg prices, and a moderate pickup in manufactured goods exports; (ii) tourist receipts would rise by about 5½ percent a year; and (iii) the growth in merchandise imports would slow to 5–6 percent a year in 2002–05 as the need for improvements in the physical infrastructure becomes smaller. On this basis, the external current account deficit would decline gradually from 15½ percent of GDP in 2000 to 14 percent of GDP in 2005, financed by direct investment, grants, and concessional borrowing. The public external debt would stabilize at about 26 percent of GDP in 2001–2005, and the net imputed reserves would rise by 2 percent of GDP a year (Table 6). The main risks to this scenario would be the same as those noted in paragraph 14 above. With respect to the risks associated with the downturn in the U.S. economy, the staff projected that a decline in tourists arrivals (relative to the baseline scenario) of 10 percent a year would lead to a deterioration in the external current account deficit by about ½ of one percent of GDP.

30. **Grenada's trade policies are largely determined in the context of the country's membership in the OECS and CARICOM.** A recent review by the WTO on trade policies in the OECS region indicated that Grenada and other ECCB member countries are moving toward a more liberal trade regime, but are constrained by a shortage of human resources and institutional weaknesses. With the implementation of the final phase of import tariff reductions under CARICOM's common external tariff agreement, average tariffs have been reduced to 16 percent,[20] the same level as in other OECS member countries, while remaining quantitative restrictions (QRs)[21] are expected to be converted into tariffs by 2005. Together with the other countries of the Caribbean region, Grenada is participating in discussions aimed at creating a single market within CARICOM,[22] and a Free Trade Area of the Americas (FTAA).

V. Structural, Social, and Other Issues

31. **The government has made determined efforts to reduce the scope of the public sector to make it more efficient.** However, the staff observed that additional progress will depend on advances in the negotiations with the labor unions on privatization and civil service pay, and the availability of skilled, experienced staff to manage the reform process. Government officials noted that further progress in reducing the size of the public sector will not be possible without technical assistance and concessional financing for severance payments, and expressed concern with the apparent shrinkage in the availability of such resources. The staff suggested that the issue of financing of severance payments be discussed with the regional and multilateral development banks. Regarding staffing, the mission noted that, while the government had had some success in raising salaries of skilled and experienced staff in the civil service, bolder actions (such as the contracting of specialized staff for fixed terms) might be required to fill the remaining staff shortages.

32. **The authorities reiterated that unemployment and poverty alleviation remain at the forefront of their economic program.** The government had launched a major effort to tackle poverty by putting in place several measures, including increases in the old age pension by one-third, the provision of free transportation and medication for welfare recipients, and increased transfers to the poor for school books and housing repair. To address rural poverty directly, higher budget allocations had been made to provide financing for small-scale rural projects, such as village roads, clinics, and water supplies; to help establish small businesses in rural areas; and provide skills training—particularly for rural youth. In education, since 1996, the World Bank has been providing resources aimed at improving the quality of basic education, expanding the number of high school places, and improving school curricula.

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[20] The average tariff on consumer goods is 20 percent, while that on capital and intermediate goods is 5 percent.

[21] Remaining QRs on about ten items are permitted under the provisions of CARICOM.

[22] A major study on the Caribbean Single Market and Economy (SME) is scheduled to be completed by the CDB and the CARICOM Secretariat during 2002.

33. **The authorities fully supported the initiatives aimed at closer integration among ECCB member countries.** The priorities in this effort included (i) greater fiscal convergence along the lines recommended by the ECCB; (ii) the harmonization of tax systems and tax incentives, accompanied by a possible, uniform VAT for the region; (iii) a common regulatory framework for business and the financial sector; and (iv) the establishment of regional money and capital markets.[23] A considerable amount of work and technical assistance would be required to convert these initiatives into common policies, but officials were confident that steady progress was being made. Closer integration of ECCB member countries would facilitate the creation of a Single Market and Economy for all CARICOM countries, a goal to which Grenada was fully committed.

VI. Staff Appraisal

34. **Grenada's economic performance in recent years has been among the most positive of ECCB member countries**, owing largely to the government's strategy of focusing on promoting private investment through sound fiscal management and improvements in infrastructure. As a result, real incomes have risen, unemployment has declined, and there has been moderate progress in social conditions. This performance has been remarkable when viewed against the virtual collapse of the key banana industry in 1997 as well as other external shocks, and demonstrates the country's capacity to adapt to adverse shocks through sound policies. The main challenge is how to sustain investment, economic growth, and social progress in the face of an uncertain international environment and possible new shocks.

35. **The staff commends the government for its commitment to maintaining fiscal prudence, and pursuing reforms aimed at creating an environment that is conducive for foreign investment.** Fiscal policy in 2001 and beyond is likely to be difficult because of indications of emerging revenue weakness and increasing rigidities in expenditure. While the recent slowdown of revenue appears to reflect to a large extent a softening in demand for tourism and imports, in the staff's view it also stems from the wide-ranging concessions and exemptions that have eroded the tax base.

36. **It is important that the Government makes a start at addressing the incipient revenue weakness by initiating a review of exemptions** and removing those which are no longer justified on grounds of new investment or job creation. Also, the *ad hoc* nature of granting new concessions should be discontinued, since it creates distortions across and within industries, lacks transparency, and makes revenue administration unduly complex. In view of the prevalence of similar tax incentives throughout the ECCB area, the staff suggests that the government take the lead in proposing a region-wide re-appraisal and harmonization of these incentives, possibly as part of a region-wide initiative to reform the tax systems based on a common value added tax.

37. **Expenditure management has been generally prudent in Grenada,** with most of the recent growth in spending associated with improvements in the country's infrastructure. The staff welcomes the government's undertaking to refrain from commercial lease-to-own contracts to

[23] See SM/01/62: *Eastern Caribbean Currency Union-Recent Developments and Main Regional Policy Issues,* for a fuller description of these proposals.

finance infrastructure projects in future, which would help slow down the rapid growth of lease and interest payments. On wages, the staff encourages the government to press ahead with its discussions with labor union representatives on ways to reduce the size of the civil service.

38. **One of the weaker aspects of fiscal policy in Grenada has been debt management,** which has been affected by poor statistics and control. The staff welcomes the government's undertaking to press ahead with the comprehensive documentation of all debts contracted or guaranteed by the central government and state entities. Also, staff recommends that the contracting or guaranteeing of new debt by the government and state entities require the review and prior approval of the Ministry of Finance.

39. **Available indicators appear to point to a broadly sound domestic banking system;** however, the staff continues to have concerns about regulation of one of the banks which does not report to the ECCB, and is not a participant in the payments settlement system. It is important that, based on an audit which has been completed, the government ensure that the bank is sufficiently liquid and adequately capitalized.

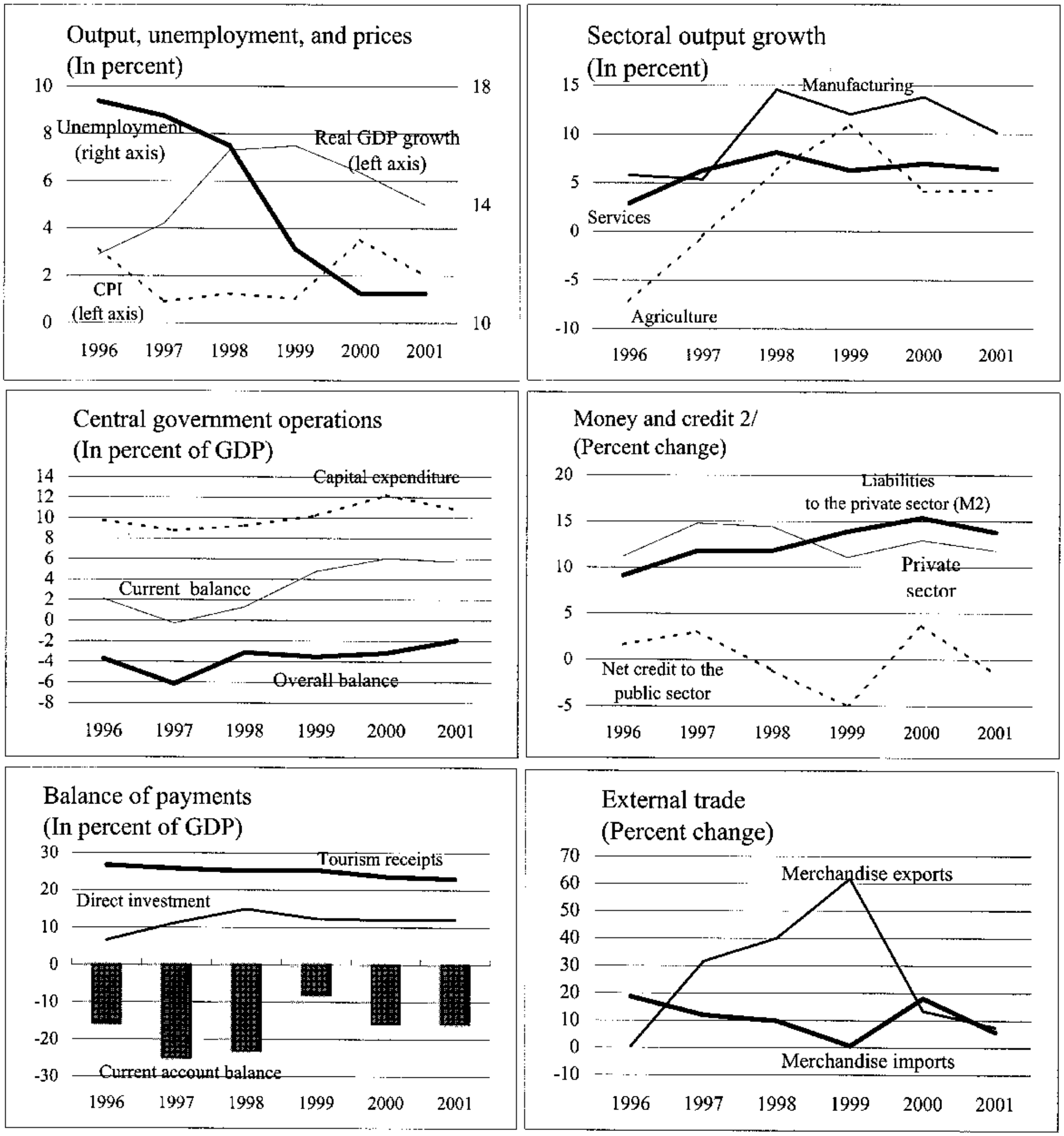
40. **The staff welcomes the efforts of the revamped supervisory agency for the offshore sector** (GIFSA) to correct weaknesses in the regulatory framework. It is important to complete the ongoing audits of all offshore banks, and on that basis, revoke the licenses of those institutions that contravene the existing framework. The staff suggests that these audits, together with the results of the self-assessment exercise initiated with the assistance of the Fund's Monetary and Exchange Affairs (MAE) Department, be used as a backdrop to setting up a more rigorous supervisory framework, with the ECCB playing a greater role.

41. **The financing of the external current account does not appear to be a cause for concern;** however, the staff regards as a matter of urgency, the task of unraveling the large unidentified private capital inflows, and the inconsistencies in the debt data. The staff welcomes the authorities' commitment to address—with the help of the ECCB—these important gaps in the analysis of the country's external position.

42. **While the statistical base has improved in recent years, weaknesses remain that adversely affect the quality of economic analysis,** particularly in the areas of the public sector debt, the capital account of the balance of payments, the finances of public enterprises and agencies, and labor statistics. The staff urges the authorities to seek external technical assistance to improve the reliability and timeliness of these data and ensure that the statistics office is adequately staffed, and welcomes Grenada's commitment to participate in the GDDS.

The staff recommends that the next Article IV consultation be conducted on the standard 12-month cycle.

Figure 1. Grenada: Selected Macroeconomic Indicators, 1996–2001 1/

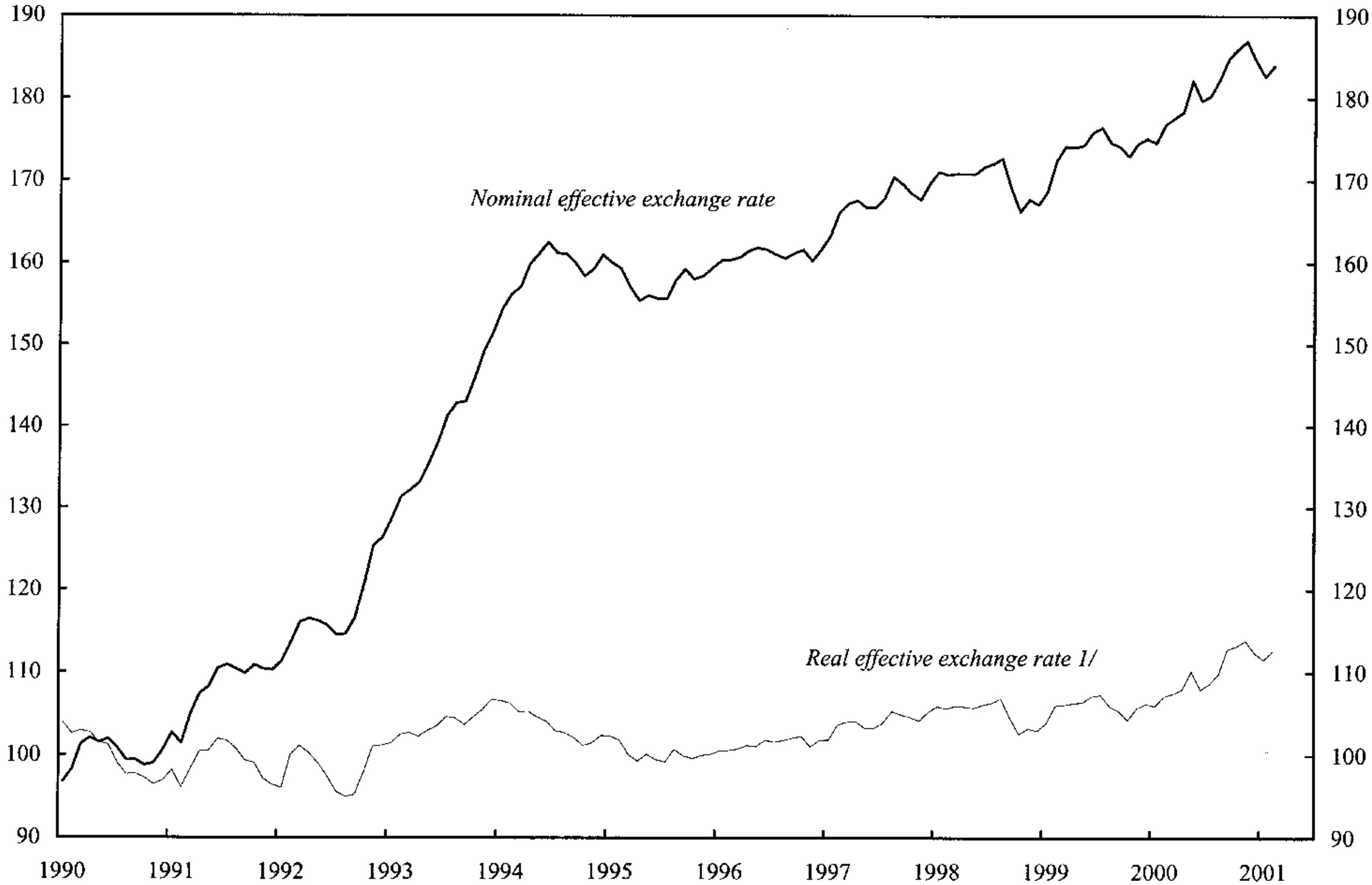


Sources: Ministry of Finance; Eastern Caribbean Central Bank; and Fund staff estimates.

1/ Estimated data for year 2001.

2/ As percent of private sector liabilities at the beginning of each year.

Figure 2. Grenada: Exchange Rate Developments
(1990=100)



Source: IMF Information Notice System.
1/ Trade-weighted index of nominal exchange rates deflated by seasonally adjusted relative consumer prices. An increase (decrease) indicates appreciation (depreciation).

Table 1. Grenada: Selected Economic and Financial Indicators

	1997	1998	1999	Prel. 2000	Proj. 2001
(Annual percentage change, unless otherwise specified)					
Output, prices, and labor					
Real GDP	4.2	7.3	7.5	6.4	5.0
Consumer prices (annual average)	1.3	1.4	0.5	2.2	2.0
Consumer prices (end of period)	0.9	1.3	1.0	3.5	2.0
Unemployment rate (estimated)	17.0	16.0	14.0	12.0	11.0
Banking system					
Net foreign assets of the banking system 1/	-6.8	0.3	6.1	-0.8	4.2
Money and quasi-money (M2)	11.8	11.8	13.9	15.4	13.8
Net domestic assets of the banking system 1/	18.6	11.4	7.8	16.2	9.6
Of which					
Credit to the public sector (net)	3.0	-1.2	-5.0	3.7	-1.6
Credit to the private sector	14.8	14.4	11.1	12.9	11.8
Average interest rate on deposits (percent per year)	5.4	5.5	5.5	5.5	5.5
Average prime rate (percent per year)	10.0	9.8	10.0	10.0	10.0
External sector					
Merchandise exports, f.o.b. (in U.S. dollars)	31.6	40.1	61.7	13.4	7.5
Merchandise imports, c.i.f. (in U.S. dollars)	11.9	18.1	0.9	18.1	5.7
Terms of trade	-0.8	30.2	11.9	4.3	0.4
Real effective exchange rate	3.4	-2.2	3.2	5.8	...
(In percent of GDP)					
Central government finances					
Total revenue and grants	26.9	30.0	28.1	29.8	30.6
Current revenue	24.1	25.2	26.2	26.8	27.5
Capital revenue	0.2	0.2	0.0	0.1	0.0
Grants	2.7	4.6	1.9	2.9	3.1
Total expenditure	33.1	33.1	31.6	33.0	32.6
Current expenditure	24.4	23.9	21.4	20.8	21.8
Of which					
Salaries and allowances	13.0	12.2	11.7	10.3	10.5
Capital expenditure	8.7	9.2	10.2	12.2	10.8
Current balance	**-0.3**	**1.3**	**4.8**	**6.0**	**5.7**
Overall balance (after grants)	**-6.2**	**-3.1**	**-3.5**	**-3.2**	**-1.9**
Foreign financing	0.5	2.1	2.8	1.8	2.0
Domestic financing	5.6	1.0	1.7	2.8	-0.1
Arrears	0.0	0.0	-1.0	-1.5	0.0
External sector					
Current account deficit (including current official grants)	-24.9	-23.0	-8.0	-15.6	-15.7
Current account deficit (excluding current official grants)	-24.9	-25.8	-10.2	-17.3	-17.3
External public debt 2/	25.7	25.9	26.3	28.0	28.4
(In millions of U.S. dollars)					
Official net imputed reserves (end of period)	42.7	46.8	50.9	57.7	65.1
Memorandum item:					
GDP at current market prices					
In EC$ millions	850	920	1,020	1,108	1,189
In US$ millions	315	341	378	411	440

Sources: Ministry of Finance; Eastern Caribbean Central Bank; and Fund staff estimates.

1/ As a percent of money and quasi-money at the beginning of the year.

2/ Government and government guaranteed debt, end of period.

Table 2. Grenada: Summary of Central Government Finances

	1997	1998	1999	Prel. 2000	Proj. 2001
(In millions of Eastern Caribbean dollars, end of period)					
Revenue and grants	**229.0**	**275.8**	**286.9**	**330.5**	**363.9**
Revenue	206.1	233.5	267.3	297.9	326.5
Current revenue	204.8	232.0	267.3	297.2	326.5
Tax revenue	187.3	204.7	232.0	265.2	284.8
Nontax revenue	17.5	27.3	35.3	32.1	41.7
Capital revenue	1.3	1.5	0.0	0.7	0.0
Grants	22.9	42.3	19.6	32.6	37.4
Total expenditure	**281.3**	**304.6**	**322.8**	**365.7**	**387.1**
Current expenditure	207.1	219.9	218.6	230.5	258.6
Salaries and allowances	110.6	112.3	119.3	114.4	125.0
Goods and services	30.7	34.4	27.1	26.5	31.3
Lease payments 1/	1.4	1.4	3.1	17.3	17.3
Interest	19.4	14.7	23.0	24.2	33.4
Domestic	13.2	9.8	15.0	11.7	24.0
Foreign	6.2	4.9	8.0	12.5	9.4
Transfers and subsidies	45.1	57.1	46.1	48.2	51.6
Capital expenditure	74.2	84.7	104.2	135.2	128.5
Current balance	**-2.3**	**12.1**	**48.7**	**66.7**	**67.9**
Overall balance (before grants)	**-75.2**	**-71.1**	**-55.5**	**-67.8**	**-60.6**
Overall balance (after grants)	**-52.3**	**-28.8**	**-35.9**	**-35.2**	**-23.1**
Financing	**52.3**	**28.8**	**35.9**	**35.2**	**23.1**
Foreign (net)	4.4	19.7	28.1	20.2	23.8
Domestic	47.9	9.1	17.7	31.2	-0.7
Arrears	0.0	0.0	-9.9	-16.2	0.0
(In percent of GDP)					
Revenue and grants	**26.9**	**30.0**	**28.1**	**29.8**	**30.6**
Revenue	24.1	25.4	26.2	26.9	27.5
Current revenue	24.1	25.2	26.2	26.8	27.5
Tax revenue	22.0	22.2	22.7	23.9	24.0
Nontax revenue	2.1	3.0	3.5	2.9	3.5
Capital revenue	0.2	0.2	0.0	0.1	0.0
Grants	2.7	4.6	1.9	2.9	3.1
Total expenditure	**33.1**	**33.1**	**31.6**	**33.0**	**32.6**
Current expenditure	24.4	23.9	21.4	20.8	21.8
Salaries and allowances	13.0	12.2	11.7	10.3	10.5
Goods and services	3.6	3.7	2.7	2.4	2.6
Lease payments	0.2	0.2	0.3	1.6	1.5
Interest	2.3	1.6	2.3	2.2	2.8
Domestic	1.6	1.1	1.5	1.1	2.0
Foreign	0.7	0.5	0.8	1.1	0.8
Transfers and subsidies	5.3	6.2	4.5	4.3	4.3
Capital expenditure	8.7	9.2	10.2	12.2	10.8
Current balance	**-0.3**	**1.3**	**4.8**	**6.0**	**5.7**
Overall balance (before grants)	**-8.8**	**-7.7**	**-5.4**	**-6.1**	**-5.1**
Overall balance (after grants)	**-6.2**	**-3.1**	**-3.5**	**-3.2**	**-1.9**
Financing	**6.2**	**3.1**	**3.5**	**3.2**	**1.9**
Foreign (net)	0.5	2.1	2.8	1.9	2.0
Domestic	5.6	1.0	1.7	2.8	-0.1
Arrears 2/	0.0	0.0	-1.0	-1.5	0.0

Sources: Ministry of Finance; and Fund staff projections.

1/ Payments related to the Financial Complex, Ministerial Complex, and the National Stadium, constructed under lease agreements.
2/ Mainly outstanding obligations to domestic suppliers.

Table 3. Grenada: Summary Accounts of the Banking System

	1997	1998	1999	Prel. 2000	Proj. 2001
	(In millions of Eastern Caribbean dollars, end of period)				
	I. Consolidated Banking System				
Net foreign assets	**85.9**	**88.2**	**133.8**	**126.5**	**168.4**
Net domestic assets	**585.7**	**662.3**	**720.8**	**859.3**	**953.5**
Net credit to the public sector	54.5	46.5	8.7	40.0	24.7
Central government	75.2	71.2	43.6	59.8	66.3
Nonfinancial public enterprises 1/	-20.7	-24.8	-34.9	-19.8	-41.6
Credit to private sector	588.0	684.7	767.9	878.4	994.8
Other	-56.8	-68.9	-55.8	-59.1	-65.9
Liabilities to private sector (M2)	**671.5**	**750.4**	**854.6**	**985.8**	**1,121.9**
Money	144.5	159.4	175.1	182.4	195.4
Quasi-money	527.0	591.0	679.4	803.5	926.6
	II. Eastern Caribbean Central Bank				
Imputed net international reserves	115.1	126.4	137.3	155.7	175.7
Net domestic assets	16.1	13.3	10.5	7.6	4.9
Base money	**131.2**	**139.6**	**148.0**	**163.4**	**180.6**
Currency held by the public	58.3	64.1	64.8	71.1	76.1
Commercial bank reserves	72.9	75.5	83.3	92.2	104.6
	III. Commercial Banks				
Net foreign assets	-29.3	-38.2	-3.5	-29.2	-7.3
Net claims on ECCB	73.5	73.4	83.8	92.2	104.6
Net domestic credit	**569.0**	**651.2**	**709.5**	**851.7**	**948.6**
Net credit to the public sector	38.4	33.2	-1.8	32.2	17.8
Credit to private sector	588.0	684.7	767.9	878.4	994.8
Other	-57.3	-66.7	-56.6	-59.0	-64.0
Liabilities to the private sector	613.2	686.4	789.8	914.7	1,045.9
	(12-month change in percent of M2 at the beginning of the period)				
Consolidated banking system					
Liabilities to private sector	11.8	11.8	13.9	15.4	13.8
Net foreign assets	-6.8	0.3	6.1	-0.8	4.2
Net domestic assets	18.6	11.4	7.8	16.2	9.6
Credit to private sector	14.8	14.4	11.1	12.9	11.8

Sources: Eastern Caribbean Central Bank; and Fund staff estimates.

1/ Includes the National Insurance Scheme.

Table 4. Grenada: Summary Balance of Payments Estimates

	1997	1998	1999	Prel. 2000	Proj. 2001
	(In millions of U.S. dollars)				
Current account balance	**-78.5**	**-78.4**	**-30.3**	**-64.2**	**-69.1**
Exports (f.o.b.)	32.8	45.9	74.3	84.3	90.6
Imports (f.o.b.)	-166.6	-183.0	-184.1	-217.4	-229.8
Services (net)	52.1	74.0	80.8	73.5	76.1
Receipts	108.6	127.0	161.5	165.3	174.5
Of which					
Travel 1/	81.1	85.8	95.8	96.9	101.1
Payments	-56.5	-74.0	-80.7	-91.8	-98.5
Income (net)	-16.7	-23.6	-29.3	-33.4	-35.9
Interest	-1.2	-4.0	-6.1	-8.5	-9.1
Other	-15.5	-19.7	-23.2	-25.0	-26.8
Transfers (net)	20.0	29.2	28.0	28.9	29.9
Private	20.1	19.8	19.6	22.1	22.9
Official	-0.2	9.4	8.4	6.8	7.0
Capital and financial account	**91.1**	**88.0**	**65.7**	**90.5**	**76.5**
Capital account (transfers)	34.2	28.7	27.2	30.2	28.6
Public sector (net) 2/	16.0	10.1	7.8	10.4	8.6
Private sector (net) 3/	18.2	18.5	19.4	19.8	20.0
Financial account	56.9	59.3	38.4	60.3	47.8
Direct investment (net)	35.3	50.9	46.4	49.3	52.9
Portfolio investment (net)	0.0	-0.1	0.4	0.0	0.0
Other investments (net)	21.6	8.5	-8.3	11.0	-5.1
Of which					
Public sector net borrowing 4/	4.8	3.9	11.4	11.5	9.3
Net errors and omissions	**0.0**	**-5.4**	**-31.4**	**-19.5**	**0.0**
Overall balance	**7.0**	**4.1**	**4.0**	**6.8**	**7.4**
Debt forgiveness 5/	**5.6**	**0.0**	**0.0**	**0.0**	**0.0**
Change in net imputed international reserves (increase -)	**-7.0**	**-4.1**	**-4.0**	**-6.8**	**-7.4**
Memorandum items:					
Net imputed international reserves (end of period)	42.7	46.8	50.9	57.7	65.1
	(In percent of GDP)				
Current account balance (including current official grants)	-24.9	-23.0	-8.0	-15.6	-15.7
Current account balance (excluding current official grants)	-24.9	-25.8	-10.2	-17.3	-17.3
Trade balance	-42.5	-40.2	-29.1	-32.4	-31.6
Exports of goods	10.4	13.5	19.7	20.5	20.6
Imports of goods	52.9	53.7	48.7	53.0	52.2
Public sector net borrowing 4/	1.5	1.1	3.0	2.8	2.1
Direct investment	11.2	14.9	12.3	12.0	12.0
Overall balance	2.2	1.2	1.1	1.7	1.7

Sources: Eastern Caribbean Central Bank (ECCB); Ministry of Finance; and Fund staff estimates.

1/ Adjusted to account for underreporting.
2/ Mainly capital grants.
3/ Migrants' transfers.
4/ Government and government guaranteed debt
5/ Refers to bilateral debt to the United Kingdom.

Table 5. Grenada: Summary Medium-Term Scenario 1/

	1999	Prel. 2000	Projections 2001	2002	2003	2004	2005
	(Annual percentage change)						
GDP and prices							
GDP at constant prices	7.5	6.4	5.0	5.0	5.0	5.0	5.0
Consumer prices (annual average)	0.5	2.2	2.0	2.0	2.0	2.0	2.0
	(In percent of GDP)						
Central government finances							
Revenue and grants	28.1	29.8	30.6	30.5	30.6	30.7	30.7
Revenue	26.2	26.9	27.5	27.5	27.6	27.7	27.7
Grants	1.9	2.9	3.1	3.0	3.0	3.0	3.0
Expenditure	31.6	33.0	32.6	33.1	33.2	33.4	33.3
Current expenditure	21.4	20.8	21.8	22.1	22.2	22.4	22.3
Wages and allowances	11.7	10.3	10.5	10.3	10.3	10.4	10.4
Goods and services	2.7	2.4	2.6	2.9	3.0	3.1	3.1
Interest	2.3	2.2	2.8	3.0	3.1	3.2	3.2
Lease payments	0.3	1.6	1.5	1.4	1.3	1.2	1.1
Other	4.5	4.3	4.3	4.5	4.5	4.5	4.5
Capital expenditure	10.2	12.2	10.8	11.0	11.0	11.0	11.0
Current balance	4.8	6.0	5.7	5.4	5.4	5.3	5.4
Overall balance	-3.5	-3.2	-1.9	-2.6	-2.6	-2.7	-2.6
External financing (net)	2.8	1.8	2.0	2.2	2.4	2.4	2.4
Domestic financing (net)	0.8	1.4	-0.1	0.4	0.2	0.3	0.2
	(In millions of U.S. dollars)						
External sector							
Current account balance	-30.3	-64.2	-69.1	-72.8	-75.8	-77.5	-80.2
(In percent of GDP)	-8.0	-15.6	-15.7	-15.4	-15.0	-14.3	-13.8
Official net imputed international reserves (end of period)	50.9	57.7	65.1	73.4	81.1	89.0	96.3

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

1/ Projections of domestic savings and investment are not incorporated in the table, as work is still ongoing on finalizing the estimates of the national accounts by expenditure.

Table 6. Grenada: Medium-Term Balance of Payments

	1999	Prel. 2000	Projections 2001	2002	2003	2004	2005
	(In millions of U.S. dollars)						
Current account balance	**-30.3**	**-64.2**	**-69.1**	**-72.8**	**-75.8**	**-77.5**	**-80.2**
Exports (f.o.b.)	74.3	84.3	90.6	97.8	105.6	113.9	122.9
Imports (f.o.b.)	-184.1	-217.4	-229.8	-242.5	-255.5	-268.2	-283.2
Services (net)	80.8	73.5	76.1	79.3	83.1	87.6	92.9
Receipts	161.5	165.3	174.5	184.8	196.1	208.6	222.5
Of which							
Travel	95.8	96.9	101.1	106.1	111.9	118.4	125.9
Payments	-80.7	-91.8	-98.5	-105.5	-112.9	-121.0	-129.6
Income (net)	-29.3	-33.4	-35.9	-38.4	-41.1	-44.1	-47.2
Interest	-6.1	-8.5	-9.1	-9.7	-10.4	-11.2	-11.9
Other	-23.2	-25.0	-26.8	-28.7	-30.7	-32.9	-35.2
Transfers (net)	28.0	28.9	29.9	31.0	32.1	33.2	34.4
Private	19.6	22.1	22.9	23.7	24.6	25.5	26.4
Official	8.4	6.8	7.0	7.3	7.5	7.8	8.1
Capital and financial account	**65.7**	**90.5**	**76.5**	**81.2**	**83.5**	**85.5**	**87.5**
Capital transfers	27.2	30.2	28.6	28.6	28.5	28.5	28.5
Public sector (net)	7.8	10.4	8.6	8.6	8.5	8.5	8.5
Private sector (net)	19.4	19.8	20.0	20.0	20.0	20.0	20.0
Financial account	38.4	60.3	47.8	52.6	54.9	56.9	59.0
Direct investment (net)	46.4	49.3	52.9	52.9	51.9	51.9	54.4
Portfolio investment (net)	0.4	0.0	0.0	0.0	0.0	0.0	0.0
Other investments (net)	-8.3	11.0	-5.1	-0.3	3.0	5.0	4.6
Net errors and omissions	**-31.4**	**-19.5**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**
Overall balance	**4.0**	**6.8**	**7.4**	**8.4**	**7.6**	**8.0**	**7.3**
Changes in reserve assets (increase -)	**-4.0**	**-6.8**	**-7.4**	**-8.4**	**-7.6**	**-8.0**	**-7.3**
Change in net imputed international reserves	-4.0	-6.8	-7.4	-8.4	-7.6	-8.0	-7.3
Memorandum item:							
Net imputed international reserves (end of period)	50.9	57.7	65.1	73.4	81.1	89.0	96.3
	(In percent of GDP)						
Current account balance (including current official grants)	**-8.0**	**-15.6**	**-15.7**	**-15.4**	**-15.0**	**-14.3**	**-13.8**
Current account balance (excluding current official grants)	-10.2	-17.3	-17.3	-17.0	-16.5	-15.8	-15.2
Trade balance	-29.1	-32.4	-31.6	-30.7	-29.7	-28.5	-27.7
Exports of goods	19.7	20.5	20.6	20.7	20.9	21.0	21.2
Imports of goods	-48.7	-53.0	-52.2	-51.4	-50.6	-49.6	-48.9
Overall balance	**1.1**	**1.7**	**1.7**	**1.8**	**1.5**	**1.5**	**1.3**

Sources: Eastern Caribbean Central Bank (ECCB); Ministry of Finance; and Fund staff estimates and projections.

Table 7. Grenada: Indicators of External and Financial Vulnerability
(In percent of GDP, unless otherwise indicated)

	1996	1997	1998	1999	Prel. 2000
External Indicators					
Exports (percent change, 12-month basis in US$)	-2.3	40.3	40.9	70.1	14.0
Imports (percent change, 12-month basis in US$)	29.3	3.0	18.1	0.9	-18.1
Terms of trade (percent change, 12 month basis)	-18.0	-0.8	30.2	11.9	4.3
Current account balance	-19.6	-24.9	-23.0	-8.0	-15.6
Capital and financial account balance	-19.5	28.9	25.8	17.4	22.1
Reserves to broad money (end of period)	16.0	17.2	16.8	16.1	15.8
External debt to exports of goods and services 1/	68.1	65.2	53.7	41.9	41.6
External interest payments to exports of goods and services 1/	1.5	1.3	1.2	0.7	1.4
External amortization payments to exports of goods and services 1/	3.7	4.0	3.0	2.6	2.1
REER appreciation, 12 month basis (percent change, Dec-Dec)	1.7	3.4	-2.2	3.2	5.8
Financial Indicators					
90-day Treasury bill, average discount rate (in percent) 2/	...	...	6.0	7.0	7.0
1-year Treasury bill, average discount rate (in percent) 2/	...	7.0	7.0	...	8.0
Share of non-performing loans in total loans of banks (in percent) 3/	14.2	11.0	16.4	10.0	9.0
Banks' total capital to risk-weighted assets (in percent)	30.9	28.9	25.5	31.5	30.4
Ratio of banks' before-tax profits to assets (in percent)	3.0	2.2	2.2	2.2	0.4

Sources: Eastern Caribbean Central Bank; and Fund staff estimates.

1/ Government and government guaranteed debt only.

2/ Treasury bills are sold only infrequently, at low volumes and at pre-announced discount rates.

3/ Nonperforming (i.e. unsatisfactory) loans are defined as those which have been in arrears for 90 days or more.

Grenada: Comparative Economic Performance

	Grenada	ECCB 1/
Population ('000; 2000)	102	580
GDP per capita (US$; 2000)	4,040	4,919
Real GDP growth at factor cost (percent; 1996–2000)	5.7	3.6
Unemployment rate (percent; 2000)	12.0	15.0
Inflation (percent; average rate; 1996–2000)	1.6	2.1
Prime lending rate (1999)	10.0	10.0
Central government revenue and grants (percent of GDP; 1996–2000)	28.7	27.7
Central government expenditure (percent of GDP; 1996–2000)	32.7	31.6
Central government wage bill (percent of GDP; 1996–2000)	11.9	12.5
Central government balance (percent of GDP; 1996–2000)	-3.9	-3.9
Central government saving (percent of GDP; 1996–2000)	2.8	0.8
Tourism growth, stay–overs (percent; 1995–99)	2.9	1.4
Export volume growth (percent, 1995–99)	21.8	-1.8
External current account balance (percent of GDP; 1995–99) 2/	-18.1	-14.9
Public sector external debt (percent of GDP, 1999) 3/	26.3	46.0

Sources: ECCB; and Fund staff estimates.

1/ Comprises the ECCB member countries, which are Antigua and Barbuda, Dominica, Grenada, St. Kitts and Nevis, St. Lucia, and St. Vincent and the Grenadines.
2/ Including migrants' remittances.
3/ Government and government-guaranteed debt, end of period.

Grenada—Fund Relations
(As of May 31, 2001)

I. Membership Status: Joined: 08/27/75; Article VIII.

II. General Resources Account:	**SDR Million**	**Percent of Quota**
Quota	11.70	100.0
Fund Holdings of Currency	11.70	100.0

III. SDR Department:	**SDR Million**	**Percent of Allocation**
Net cumulative allocation	0.93	100.0
Holdings	0.00	0.4

IV. Outstanding Purchases and Loans: None

V. Financial Arrangements

Type	Approval Date	Expiration Date	Amount Approved (SDR Million)	Amount Drawn (SDR Million)
EFF	08/24/83	01/23/84	13.50	1.13
Stand-by	05/11/81	05/10/82	3.43	2.90
Stand-by	11/06/79	12/31/80	0.65	0.65

VI. Projected Obligations to Fund: None

VII. Exchange Arrangement:

The currency of Grenada is the Eastern Caribbean dollar, which has been pegged to the U.S. dollar since July 1976 at the rate of EC$2.70 per U.S. dollar.

Grenada accepted the obligations of Article VIII, Sections 2(a), 3, and 4 in January 1994. There are no restrictions on the making of payments and transfers for current international transactions. There are exchange controls on payments for invisibles (i.e., indicative limit on travel allowances), but all bona fide transactions are approved.

VIII. Article IV Consultation:

The last Article IV consultation was concluded by the Executive Board on July 5, 2000. Grenada is on the standard 12-month consultation cycle.

XI. Technical Assistance:

An MAE mission visited Grenada in January 2001 to assist the authorities in preparing self-diagnostic exercises to assess the regulatory framework and operations of the offshore financial sector.

An FAD mission visited Grenada in October 1999 to review the tax system and advise on the feasibility of introducing a VAT.

As a follow up to FAD's report of February 2000, a mission from LEG visited Grenada in July 2000 to ascertain the specific needs of the authorities with respect to amendments to the tax laws required to improve compliance.

Grenada—Relations with the World Bank Group

(As of March 31, 2001)

I. Projects

Grenada is a participant in the World Bank supported and supervised OECS Solid Waste/Ship-generated Waste Management Projects, which were approved in FY 1995. The objective of these operations is to reduce public health risks and protect the environmental integrity of the Eastern Caribbean islands and their coastal and marine systems, by improving solid waste management facilities. The total regional financing for these projects is US$41 million. The Grenada component is US$5.4 million—US$2.2 from the European Investment Bank, US$1.7 from the Caribbean Development Bank, and US$1.4 from the World Bank (GEF).

In FY 1996, the World Bank approved a US$7.66 million loan for the Basic Education Reform Project. The Project is designed to improve the quality of basic education, expand access to secondary education, rehabilitate primary and secondary schools facilities, and help curriculum development for primary and secondary schools. The project will close at end-2001, and will be followed by another education project, the OECS Education Reform Project.

In FY 1998, the World Bank approved a US$6 million loan for an OECS Telecommunications Reform Project. Grenada's share of this project is US$1.2 million. The objective is to introduce pro-competition reforms in the telecommunications sector, and increase the supply of informatics-related skills in the five OECS borrowing countries.

The Bank's Board approved on October 17, 2000 the Grenada component (US$10 million) of the OECS Emergency Recovery and Disaster Management Program (ERDMP). It became effective on February 7, 2000. The first phase of this program included three OECS countries (Dominica, St. Kitts and Nevis, and St. Lucia). The second phase will include Grenada and St. Vincent and the Grenadines. The program aims to support the physical and institutional efforts of the participating countries for disaster recovery, and emergency preparedness and management.

II. Financial Relations

(In millions of U.S. dollars)

Operations	Principal	Disbursed	Undisbursed
Grenada Disaster Management	10.07	0.05	10.02
Telecommunications Reform	1.20	0.14	1.06
Basic Education Reform	7.66	5.50	2.16

Gross disbursements and debt service during fiscal year

	Actual							Projections	
	1994	1995	1996	1997	1998	1999	2000	2001	2002
Total disbursements	0.00	0.00	0.00	0.50	0.30	1.40	2.00	2.30	5.91
Repayments	0.00	0.00	0.10	0.10	0.10	0.10	0.10	0.10	0.10
Net disbursements	0.00	0.00	-0.10	0.40	0.20	1.30	1.90	2.20	5.81
Interest and fees	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.20	0.30

III. Economic and Sector Work

The last OECS Country Assistance Strategy (CAS) paper was prepared in 1995. The World Bank is currently working on a new CAS, which was presented to the Board on June 28, 2001. In addition, the World Bank is working on an institutional review of Eastern Caribbean States to identify areas where it is politically and technically feasible to develop cross-country agreements that reduce the unit costs of public services.

The Medium-Term Economic Strategy Paper for the period 2002–04 will be prepared by the Government of Grenada in cooperation with the World Bank and the Caribbean Development Bank, and will be presented at the June 2002 meeting of the Caribbean Group for Cooperation in Economic Development (CGCED).

Grenada: Relations with the Caribbean Development Bank (CDB)

(As of December 31, 2000)

I. Projects

The Caribbean Development Bank's operations in Grenada are designed to support the country's economic and social development through the financing of selected capital projects and technical assistance, and through policy advice on major developmental issues. Against this backdrop, the CDB's involvement with Grenada has covered areas such as: (i) infrastructure development to facilitate private investment, (ii) sectoral development to promote diversification, (iii) human resource development and institutional strengthening, (iv) emergency disaster rehabilitation, and (v) macroeconomic policy formulation.

Over the period 1970–99, the CDB provided US$98.9 million in loans and grants to Grenada, representing 5.1 percent of total disbursement to the Bank's 17 borrowing member countries. Of this, loans accounted for $88.4 million, 71.3 percent of which has been provided from "soft" resources. Technical assistance grants accounted for the remaining US$10.5 million. Economic infrastructure (including road development, expansion and improvements in the water supplies, and upgrading the port) absorbed 35 percent of CDB's financial support; the productive sectors, 29 percent; multi-sectoral projects (including the construction of industrial estates, emergency road and sea defense restoration, sanitary infrastructural improvements), 21 percent; and the social sectors, 15 percent.

CDB's technical assistance (through grants) has been targeted for institutional strengthening in various government agencies, training for small and micro enterprises, project preparation and pre-feasibility studies, and more recently, consultancy services to the small hotel sector. During 2000, grants were approved for a review of the hospital management systems and human resource capabilities, institutional strengthening of the Inland Revenue Department, and training in project preparation and appraisal. At end-December 2000, Grenada had a total outstanding loan balance of US$47.9 million.

Sectoral Distribution of Capital Projects, 1970-2000

Sectors	In Millions of U.S. Dollars	In Percent
Productive	**29.0**	**29.3**
Agriculture	16.8	17.0
Manufacturing	7.7	7.8
Tourism	4.1	4.1
Mining	0.4	0.4
Economic infrastructure	**34.1**	**34.5**
Power and energy	0.2	0.2
Water	2.5	2.5
Transportation	31.4	31.7
Social	**14.8**	**15.0**
Housing	5.1	5.2
Education	4.2	4.2
Health/sanitation	5.5	5.6
Multisector	**21.0**	**21.2**
Total	**98.9**	**100.0**

II. Financial Relations

(As of June 30, 2000)

(In millions of U.S. dollars)

	1994	1995	1996	1997	1998	1999	2000
Cumulative total credit approved	51.35	68.92	68.16	71.86	76.28	77.01	90.25
Cumulative disbursements 1/	49.31	52.28	53.07	56.08	61.18	67.10	71.66
Disbursements 2/	**5.23**	**2.97**	**0.79**	**3.01**	**5.1**	**5.92**	**4.56**
Ordinary capital resources	0.36	0.09	0.65	1.86	2.85	4.59	2.29
Special development fund	4.75	2.46	0.14	0.48	0.36	0.82	1.39
Other special fund resources	0.12	0.42	0.00	0.67	1.89	0.51	0.88
Amortization 2/	**1.66**	**1.48**	**2.30**	**2.07**	**2.1**	**2.68**	**1.98**
Ordinary capital resources	0.13	0.11	0.35	0.54	0.52	0.63	0.57
Special development fund	1.25	1.07	1.56	1.21	1.24	1.72	1.21
Other special fund resources	0.28	0.30	0.39	0.32	0.34	0.33	0.20
Outstanding debt (end of period)	39.07	41.09	39.28	39.89	42.17	45.09	47.91
Interest and commitment fees 2/	**1.15**	**1.18**	**1.90**	**1.29**	**1.36**	**1.63**	**1.57**
Ordinary capital resources	0.23	0.44	0.81	0.59	0.59	0.83	0.88
Special development fund	0.84	0.65	1.01	0.64	0.71	0.73	0.62
Other special fund resources	0.08	0.09	0.08	0.06	0.06	0.07	0.07

Source: Caribbean Development Bank.

1/ Including valuation adjustments.

2/ Ordinary capital resources are loans on non-concessional terms, and special development funds and other special fund resources are soft loans.

Grenada—Statistical Issues

Outstanding statistical issues

The coverage, consistency and timeliness of the statistical information reported to the Fund for surveillance remain weak, particularly in national accounts, the balance of payments, and debt. The Eastern Caribbean Central Bank (ECCB) publishes a quarterly economic and financial review, and an annual balance of payments for each member country of the Organization of Eastern Caribbean States (OECS).

Recently, Grenada completed requirements for participation in the Fund's General Data Dissemination System (GDDS) when it posted its metadata on the Dissemination Standards Bulletin Board. The metadata detail plans for statistical development in the main macroeconomic areas in the near and medium term.

Real sector

Except for consumer prices, no other real sector data are provided between missions. Data on the national accounts (in constant and current prices) are available annually, but there is a long lag with respect to the availability of data on aggregate domestic expenditure. The methodologies used to estimate capital formation and sectoral price deflators need to be improved and documented. The Central Statistical Office (CSO) intends to finalize and publish the results of a labor market survey, which was initiated in 1994. No comprehensive or regular labor statistics are available.

Government finance

The reporting of the central government data has improved significantly in recent years, but major weaknesses remain in the rest of the public sector. The authorities are now reporting quarterly central government operations in Fund economic classification format, with lags of one to two months. Regarding the rest of the public sector, there is no systematic reporting of information to the ministry of finance; annual statements for the major public enterprises are obtained from the ministry during Fund missions. Work is still ongoing by staff to compile consolidated public sector accounts. The 2000 GFS Yearbook contains data for 1991–95. The data cover the central government only (operations of the National Insurance Scheme are excluded), and no financing data are reported. After an interruption of about two years, Grenada has indicated that it will resume reporting government finance data to STA for publication.

Monetary accounts

Monthly data for publication in *IFS* are reported by the ECCB, normally with a two-month lag for monetary authorities and a three-month lag for commercial banks.. The data are reliable, and reported on a regular basis.

Balance of payments

Balance of payments estimates are compiled by the ECCB on an annual basis and incorporate the information collected by the CSO. The compilation of foreign trade statistics is hampered by software and hardware constraints, and there are discrepancies between the estimates prepared by the customs division and the CSO. Statistics on the direction of trade are relatively current. Imports by SITC section are available on a quarterly and annual basis. The methodology used to estimate tourist receipts (based on a 1986 survey) needs to be reviewed, and the the data on services and the capital account are not comprehensive. The latest data published in IFS and the Balance of Payments Yearbook are for 1996. However, the ECCB recently reported annual data for the period through 1999, which have yet to be published in the Fund publications pending clarification of a number of issues.

External debt

The information on external loans contracted and guaranteed by the government, as detailed in the annual budget estimates, is incomplete insofar as it excludes some loans, and may underestimate the amounts outstanding of some loans which are included. The coverage of external debt is weakened further by the fact that there is no central, comprehensive listing of debt contracted by state enterprises and other public sector entities, or of private sector debt guaranteed by the government.

Grenada: Core Statistical Indicators

As of June 12, 2001

	Exchange Rates 1/	International Reserves	Central Bank Balance Sheet	Reserve/ Base Money	Broad Money	Interest Rates	Consumer Price Index	Exports/ Imports	External Current Account Balance	Overall Government Balance	GDP/GNP	External Debt and Debt Service
Date of Latest Observation	n.a	Mar. 2001	Mar. 2001	Mar. 2001	Mar. 2001	Mar. 2001	Mar. 2001	1999	1999	Mar. 2001	Dec. 2000	Dec. 2000
Date Received	n.a	May 2001	May 2001	May 2001	May 2001	May 2001	May 2001	June 2000	June 2000	May 2001	Feb. 2001	March 2001
Frequency of Data	n.a	Monthly	Monthly	Monthly	Monthly	Quarterly	Monthly	Annual/ quarterly	Annual	Monthly	Annual	Annual
Frequency of Reporting	n.a	Monthly with one-to-two-month lag	Monthly with one-to-two-month lag	Monthly with two-to-three-month lag	Monthly with one-to-two-month lag	Monthly with one-to-two-month lag	Monthly with one-to-two month lag	Article IV Mission	Article IV Mission	Monthly with one-to-two-month lag	Article IV Mission	Article IV Mission
Source of Update	n.a	ECCB 2/	ECCB	ECCB	ECCB	ECCB	CSO 3/	CSO 3/	ECCB CSO	Ministry of Finance	CSO	Ministry of Finance
Mode of Reporting	n.a	Fax/e-mail	Fax/-email	Fax/e-mail	Fax/e-mail	Fax/e-mail	Fax	Article IV Mission	Article IV Mission	E-mail	Article IV Mission	Article IV Mission/ e-mail
Confidentiality	n.a	Unrestricted	Unrestricted	Unrestricted	Unrestricted	Unrestricted	Unrestricted	Unrestricted	Unrestricted	Restricted	Unrestricted	Unrestricted
Frequency of Publication	n.a	Annual and quarterly	Annual and quarterly	Annual and quarterly	Annual and quarterly	Annual and quarterly	Annual and monthly	Annual	Annual	Semi-annual	Annual	Annual and semi-annual

1/ Grenada is a member of the Eastern Caribbean Currency Union, in which the common currency of all member states (E.C. dollar) has been pegged to the U.S. dollar at US$1=EC$2.70 since July 1976.
2/ Eastern Caribbean Central Bank.
3/ Central Statistical Office.

Grenada: Social Indicators

	Grenada (most recent estimates)	Grenada (15-20 years ago)	Latin American and Caribbean (most recent estimates)
I. Social Indicators of Development			
Demographics			
Population (millions)	0.10	0.09	478.0
Density (population per square kilometer)	296.2	276.2	24.0
Population annual growth rate (percent)	0.6	0.9	1.7
Crude birth rate (per thousand population)	17.8	27.2	23.6
Crude death rate (per thousand population)	7.9	8.2	6.6
Fertility rate	3.6	4.0	2.8
Per capita income (U.S. dollars)	3,630	940	....
Labor force			
Economically active population (millions)	0.036	0.0	196.8
Agriculture (per cent of labor force)	13.8	30.0	25.5
Poverty (percent)			
Population below poverty line	32.1	...	...
Absolute poor	15.2	...	...
Health			
Infant mortality (per thousand)	16.2	14.9	...
Life expectancy at birth (years)	71.6	67.0	69.1
Population per physician	1,258	2,116	1,458
Immunized children under 12 (in percent)			
Measles	86.3	31.0	83.7
Diphtheria	78.2	76.0	80.0
Tetanus	82.6	76.0	80.0
Access to safe water			
Urban	100.0	74.6	89.5
Rural	96.0	...	57.0
Education			
Gross enrollment ratios (percent of school age group)			
Primary	129.5	132.2	109.7
Secondary	53.0	49.9	51.3
Pupil/teacher ratio			
Primary	24.6	27.0	...
Secondary	22.1	21.0	...

Grenada: Social Indicators

	Grenada (most recent estimates)	Grenada (15-20 years ago)	Latin American and Caribbean (most recent estimates)
Illiteracy rate (percentage of population over 15 years)	2.0	...	...
Newspaper circulation (per thousand of population)	21.0	27.0	86.3
Women			
Gross enrollment ratio (per cent of school age group)			
Primary	121.9	130.6	...
Secondary	63.5	55.9	...
Illiteracy rate (per cent of population over 15 years)	2.0	...	...
Life expectancy (years)	74.3	...	72.5
Labor force (percent of total)	51.4	46.8	33.4

Sources: Poverty Assessment Report; Grenada Labor Force Survey 1998, (Draft); A Survey of the Major Developments in the Economy of Grenada, Ministry of Finance, Grenada.

Grenada: Tax Exemption Regime

1. Grenada relies heavily on tax exemptions and concessions to attract private foreign direct investment, particularly in the areas of tourism and manufacturing. The tax regime embodies numerous exemptions and concessions. Under the tax exemption structure, which is governed mainly by the Caribbean Common Market (CARICOM) Agreement,[1] there is a list of "conditional duty exemptions" (CDEs) that countries are allowed to grant, most of which are defined in terms of the industry or user that would benefit from the exemption rather than by the specific good to be exempted. The main sectors that benefit from exemptions include agriculture and fishing, tourism, and cultural and sporting activities. The rules governing CDEs allow for flexibility in application across countries, particularly in the lesser-developed countries (LDCs) of CARICOM.[2]

2. In Grenada, as in other CARICOM countries, exemptions are also granted as part of "fiscal incentive" schemes. In this context, Grenada is guided by the CARICOM Harmonized Fiscal Incentives to Industry (HFII), as outlined below in Table 1.

Table 1. Fiscal Incentives under the CARICOM Harmonized Scheme

Type of Incentive	Duration
Profit tax holiday	10–15 years.[3]
Tariff exemptions	For the duration of tax holiday, inputs, machinery and spare parts may be imported duty free; all materials and equipments for new factories may be imported duty free.
Export allowance for extraregional exports after tax holiday expires extraregional exports	4-tier graduated scale (25–50 percent) of tax relief for up to 5 years, based on a similar tier of export profits as a proportion of total profits.
Dividend payments	For the duration of tax holiday, dividends paid to shareholders are tax exempt.
Loss carry-forward	Available for up to 5 years after expiration of tax holiday.
Depreciation allowance	After expiration of tax holiday, an annual deduction of up to 20 percent of capital expenditure incurred.

Source: Industrial Development Corporations, Price Waterhouse, "The Caribbean Common Market: Trade Policies and Regional Integration in the 1990s", World Bank, Report No. 8381-CRG (1990).

1. Under this Agreement, member states have adopted a common external tariff (CET) applied to imports from outside the region as well as to goods traded among member states, which do not qualify for Common Market treatment. The members of CARICOM are Antigua and Barbuda, The Bahamas, Barbados, Belize, Dominica, Grenada, Guyana, Haiti, Jamaica, Montserrat, St Kitts and Nevis, St Lucia, St Vincent and the Grenadines, Suriname, and Trinidad and Tobago.

2. These include Antigua and Barbuda, Dominica, Grenada, Montserrat, St Kitts and Nevis, St Lucia, and St Vincent and the Grenadines.

3. This applies to the lesser-developed countries (LDCs) of CARICOM. The corresponding period for the other members of CARICOM is 5–10 years.

3. As one of the LDCs of CARICOM, Grenada is allowed to offer more generous concessions under the "harmonized" policy, and to grant incentives not covered in the HFII, to promote small scale industries. Other incentives not covered under HFII, but of common application include the Hotel Aid Act, and concessional rental rates for factory space in industrial estates. Firms from the United Kingdom gain an additional tax credit from Grenada's double taxation treaty with the U.K.

INTERNATIONAL MONETARY FUND
Public Information Notice
EXTERNAL RELATIONS DEPARTMENT

Public Information Notice (PIN) No. 01/69
FOR IMMEDIATE RELEASE
July 20, 2001

International Monetary Fund
700 19th Street, NW
Washington, D. C. 20431 USA

IMF Concludes Article IV Consultation with Grenada

On July 11, 2001, the Executive Board concluded the Article IV consultation with Grenada.[1]

Background

Grenada's economic performance has improved markedly in recent years in response to the authorities' strategy that has focused on promoting private investment through sound fiscal management and improvements in infrastructure. Real GDP growth averaged 7½ percent in 1998–1999, and the economy continued to perform well in 2000, with output estimated to have risen by 6½ percent; unemployment declining further to 12 percent; and inflation remaining in the low single digits. Growth was fairly broad-based, with manufacturing, residential and hotel construction, and other services (particularly communications and financial services) registering strong advances. After two years of steady expansion, activity in the tourism sector slowed in 2000 because of the withdrawal of the only direct air service between Grenada and the U.S. mainland, and cancellation of weekly visits by the largest cruise ship. Indications are that real GDP growth will slow to about 5 percent in 2001, owing to the completion of the public sector and tourism projects, and continued weak tourism demand. Despite these achievements, social conditions have remained difficult, with poverty affecting an estimated 30 percent of the population.

The strong growth in economic activity was accompanied by a fairly robust expansion in banking system deposits, as well as in credit—mainly for construction and consumer goods. The increase in credit, coupled with the sharp growth in imports, associated with a pickup in infrastructure and tourism projects, led to a doubling of the external current

[1] Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board. At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities. This PIN summarizes the views of the Executive Board as expressed during the July 11, 2001 Executive Board discussion based on the staff report.

account deficit to almost 16 percent of GDP in 2000, which was financed by direct investment, and grants and loans associated with the public investment program. Exports performed well over the past two years owing to high nutmeg prices, increased shipments of electronic components to the U.S market, and strong growth in fish products. Receipts from services experienced virtually no growth in 2000, reflecting the slowdown in tourist arrivals.

During 1998–2000, the central government budget registered deficits averaging 3½ percent of GDP, financed by grants, mainly concessionary loans, and banking system borrowing. However, government savings rose from 1½ percent of GDP in 1998 to an estimated 6 percent in 2000 owing mainly to continued efforts to strengthen tax and customs administration through the hiring of additional staff, increased use of audits, greater focus on large taxpayers, and the payment of cash incentives to tax collection agents. Also, the wage bill was reduced, as about 200 temporary government employees were released.

Structural reform efforts during 1999–2000 continued to focus on reducing the scope and size of the public sector, and making the civil service more efficient. Currently, discussions are taking place with the labor unions on (i) options for restructuring the sugar industry; (ii) the modalities for making certain government departments more efficient by converting them into independent agencies run on commercial lines; and (iii) developing a performance-based pay system for the civil service. In the second half of 2000, the Grenada International Financial Services Authority (GIFSA) introduced measures designed to correct weaknesses in the regulation and supervision of offshore financial institutions that were revealed in the wake of the failure of the largest offshore bank, and the subsequent closure of several others. The key measures include (i) audits of all offshore banks by an international firm; (ii) improved staffing to facilitate on-site inspections and closer monitoring; and (iii) proposals for changes in legislation to address weaknesses in the legal framework. During the first half of 2001, a self assessment exercise for the offshore financial services sector was initiated, with the assistance of the Fund and the Eastern Caribbean Central Bank (ECCB).

Executive Board Assessment

Directors noted that Grenada's economic performance in recent years has been among the most favorable of the ECCB member countries—real GDP has risen sharply, unemployment has declined, and moderate progress has been made in improving social conditions. This performance, which followed the virtual collapse of the banana industry in 1997, demonstrated the country's capacity to adapt to adverse shocks through a strategy of promoting private investment by means of sound fiscal management and improvements in infrastructure. Directors observed that the main challenge now facing Grenada is to sustain investment, economic growth, and social progress in the face of a less favorable international environment.

Directors cautioned that maintaining a strong fiscal position in 2001 and beyond could be difficult, because of emerging revenue weaknesses and increasing rigidities in expenditure. They noted that while the recent slowdown of revenue appeared to be associated with a softening in the demand for tourism and imports, it also reflected the erosion of the tax base that had resulted from the authorities' wide-ranging concessions and exemptions to various industries. Directors therefore recommended that the government begin promptly to review all exemptions, and phase out those which are no longer consistent with government policy. In particular, they urged the authorities to discontinue the discretionary nature in which concessions are granted, as it creates distortions, lacks transparency, and makes revenue administration unduly complex. It was suggested that, in view of the prevalence of similar tax incentives throughout the ECCB area, the government might propose a region-wide reappraisal and harmonization of these incentives, possibly as part of a joint initiative to reform the tax systems based on the introduction of a common value-added tax.

Directors observed that expenditure management had been generally prudent in Grenada, but cautioned against the further growth of commercially-financed lease-to-own infrastructure projects and the civil service wage bill. In this connection, they welcomed the authorities' commitment to refrain from such projects in the future, and encouraged the government to press ahead with its discussions with labor union representatives on ways to rationalize the civil service.

Directors expressed concern with the weakness in debt management, which has been affected by poor statistics and inadequate control over borrowing. They encouraged the authorities to press ahead with their plans to document comprehensively all debts contracted or guaranteed by the central government and state entities.

Available indicators point to a broadly sound domestic system. To maintain the system in good financial health, Directors urged the authorities to ensure that banks, without exception, report on a regular basis to the ECCB, and satisfy all legal and prudential requirements. Directors commended the efforts of the supervisory agency for the offshore center to address weaknesses in the regulatory framework through the ongoing audits of all offshore banks. They suggested that these audits, together with the results of the self-assessment exercise initiated with the assistance of the Fund's Monetary and Exchange Affairs Department, could be used as bases for a more rigorous supervisory framework in which the ECCB would play a greater role. Directors welcomed the plan to follow up with a region-wide Financial Sector Assessment Program. The issuance of legislation and a set of anti-money laundering guidelines, as well as the enhanced enforcement capacity in this area also were seen as positive steps.

Directors welcomed Grenada's participation in the General Data Dissemination Standard, but expressed concern with the poor quality of the information in a number of areas. They stressed the importance of clarifying the large unidentified private capital inflows and the inconsistencies in the debt data with the help of the ECCB, and of addressing the weaknesses in the national accounts, the finances of public enterprises, and labor statistics.

Public Information Notices (PINs) are issued, (i) at the request of a member country, following the conclusion of the Article IV consultation for countries seeking to make known the views of the IMF to the public. This action is intended to strengthen IMF surveillance over the economic policies of member countries by increasing the transparency of the IMF's assessment of these policies; and (ii) following policy discussions in the Executive Board at the decision of the Board.

Grenada–Selected Economic Indicators
(Annual percentage changes, unless otherwise indicated)

	1996	1997	1998	1999	Est. 2000
Real sector					
Nominal GDP	6.6	6.9	8.2	10.9	8.6
Real GDP	2.9	4.2	7.3	7.5	6.4
Consumer price index 1/	3.1	0.9	1.2	1.0	3.5
Unemployment rate	17.5	17.0	16.0	14.0	12.0
Central government finances 2/					
Revenue and grants	28.9	26.9	30.0	28.1	29.8
Expenditure	32.7	33.1	33.1	31.6	33.0
Current	23.0	24.4	23.9	21.4	20.8
Capital	9.7	8.7	9.2	10.2	12.2
Current balance	2.1	-0.3	1.3	4.8	6.0
Overall balance	-3.7	-6.2	-3.1	-3.5	-3.2
Money and interest rate					
Net domestic assets of the banking system 3/	13.9	18.6	11.4	7.8	16.2
Public sector	1.6	3.8	-1.2	-5.0	3.7
Private sector	11.2	14.8	14.4	11.1	12.9
Liabilities to the private sector	9.1	11.8	11.8	13.9	15.4
Average prime rate (percent per year)	10.0	10.0	9.8	10.0	10.0
External sector					
Current account balance 2/	-19.6	-24.9	-23.0	-8.0	-15.6
Public external debt 2/	26.3	25.7	25.9	26.3	28.0
Public external debt service ratio (in percent of exports of goods and nonfactor services)	5.3	5.3	4.3	3.3	3.6
Real effective exchange rate (depreciation -)	1.8	3.4	-2.2	3.1	5.8

Sources: Grenada authorities; and IMF staff estimates.

1/ End of period.
2/ In percent of GDP.
3/ In percent of initial stock of liabilities to the private sector.

Statement by Thomas A. Bernes, Executive Director for Grenada
Executive Board Meeting
July 11, 2001

Overview

1. My Grenadian authorities are very appreciative of the opportunity for consultations with staff, are in broad agreement with their analysis and findings and found their advice to be timely and beneficial. Real growth has been among the strongest in the sub-region, particularly over the last four years, and the unemployment rate has declined by about 6 percentage points to 11 percent. Given Grenada's small size and population of just 100,000, and vulnerability to external shocks, my authorities are focused on the need for structural reform to develop a business-friendly environment. This will require that capacity be strengthened and it is heartening that the staff report suggests options for doing so, taking into consideration the unique circumstances of the island.

Background

2. Grenada is a significant producer of spices (33 percent of the world's production) and thus was not as vulnerable as other islands in the sub-region to the loss of preferential markets in Europe for bananas and sugar. Nevertheless, the authorities set about restructuring the banana industry when it became clear that preferential markets were eroding. Grenada is now the smallest producer of bananas in the sub-region. Its very small sugar cane crop is used for rum production. A successful attempt was made to diversify into services, including offshore financial services, and quick action has been taken to develop the regulatory and supervisory framework, but this will be an on-going process.

3. During 2000, the Grenadian economy continued to exhibit strong growth and exports of spices benefited from higher prices. But recently there has been a downturn in tourism which partly reflects the recent loss of some air links and the re-routing of a major cruise line. There has also been a more general slowdown in the sub-region due to the weaker international outlook as well as some slowing of the offshore financial services business.

4. Fiscal management remained tight in 2000 and there have been ongoing efforts to strengthen tax administration. Thus, there was growth in property tax and corporation tax, reflecting the growth of the economy. The surplus on the current account increased from 4.8 percent to 6 percent but the overall deficit remained just over 3 percent of GDP reflecting higher spending on infrastructure. During the first quarter of 2001 some categories of revenue slowed and the authorities responded by restraining recurrent expenditure and expenditure on a few capital items not related to capital projects.

Policy Issues

5. The main challenge of the authorities is to sustain and build on the achievements of the past. There are three pillars of the broad economic strategy: a) fiscal consolidation to create leverage for infrastructure development and poverty alleviation; b) structural reform to

strengthen the environment for private investment so that unemployment can be reduced, and c) capacity building, with technical assistance as necessary.

Fiscal Policy

6. Fiscal management improved during 2000 with a current account surplus of 6 percent of GDP and an overall fiscal deficit of 3 percent of GDP. There are, however, some downside risks to tax buoyancy in the medium term, particularly if the slowdown in growth and revenue becomes more entrenched. There are also indications that growth in the sub-region will slow in 2001. It will therefore be important to strengthen the revenue base. The authorities are keen to implement a value-added tax but this will require technical assistance and should be implemented as part of a regional approach.

7. The authorities are aware of the need to develop a more streamlined and transparent system of concessions (allowances) but this is a complex undertaking which will require technical assistance. The current framework extends to utilities, educational, religious and other establishments. The incentive framework is quite generous and rolling it back is also hinged on the need to harmonise incentives in the sub-region. An important starting point lies in reducing the allowance on vehicles but allowances for capital development will be retained.

8. The authorities are keen to reform the civil service subject to the necessary technical assistance. A strategy of outsourcing some services has already been put in place and this has facilitated a reduction in public sector employment. Some workers have formed cooperatives providing services not only to government but to the private sector as well. The wages bill has fallen significantly as a result but wage rates are compressed and this makes it difficult for the public sector to attract or retain trained professionals.

9. The emphasis on private sector development which creates employment and takes pressure off the Government has served Grenada well and will be continued. It is also planned to stimulate small business development, agricultural diversification, and agro-processing using inputs from local farmers. It is important to develop secondary products from the vital nutmeg sector and continued foreign inflows will be needed to finance investment projects, civil service reform, and upgrade capacity.

10. The authorities are keen to improve social conditions and alleviate poverty. However, the study by the CDB in 1998 estimated poverty to be approximately 32 percent. This figure appears overstated given the declining trend in unemployment over the past five years (from 26.7 percent in 1994 to 11 percent at the end of 2000). There is a need for a mechanism to regularly monitor the poverty situation in Grenada.

11. The rate of implementation of the PSIP significantly improved in 2000 with a rate of 72 percent up from 58 percent in the previous year. This accelerated rate of implementation had a very positive impact on economic activity. The economy grew by 6 percent.

Debt management

12. The external public debt at 28 percent is manageable and no new commercial debt has been contracted thus far for 2001. The authorities are committed to addressing the administrative, technical, and statistical aspects of debt management. The main problem is systemic and includes the difficulty of retaining trained personnel. Thus, a two-week ECCB course for technicians will be conducted in July to upgrade capacity in the use of the CSDRMS debt management software. In addition, a working group has been created in the Ministry of Finance and efforts are on-going to update the debt registry with inclusion of data from statutory corporations.

Tourism

13. In the medium term it is planned to implement strategies to improve nature, sports, and events tourism and educate school children and the general population to the sector's importance. The vital tourism product also requires attention to urban renewal, upgrading of infrastructure and the quality of attractions and strengthening of the link between tourism and the agricultural sector. But the loss of airlift and cruise capacity is a major setback. The new National Indicative Programme with the European Union will focus on tourism, specifically, training and infrastructural development.

Divestment & Commercialisation

14. The authorities remain committed to the divestment or commercialisation of public assets. In May 2001, an agreement was signed for the privatization of the Sugar Factory. It is considered prudent to commercialise rather than privatise entities such as the hospital, community college, and printery. There have been unexpected delays related to legal and administrative hurdles, the negotiations process, and difficulties in finding willing buyers for some public assets.

Financial Sector

15. The banking system is broadly sound under the supervision of the East Caribbean Central Bank (ECCB) and the authorities are aware of the need to strengthen weaknesses in monitoring and supervision of all commercial banks. Also assistance is being obtained from the Caribbean Development Bank (CDB) to restructure the development bank.

16. The authorities are upgrading capacity to monitor and supervise the offshore financial sector with the close cooperation of the ECCB and the Fund. A mission from the Fund's MAE department visited Grenada in January 2001 to assist the authorities in preparing a self-assessment and Price Waterhouse has recently been commissioned to perform audits of offshore entities.

17. The capacity of the Grenada International Financial Services Agency (GIFSA) has been strengthened with the increase in staff from 5 to 20. The due diligence process has been revamped and thus far this year licenses of 23 offshore banks and licenses of 2 offshore trust

companies have been revoked. There has also been significant progress in developing statistics on licensing of offshore entities. GIFSA participated in the financial self-assessment workshop at the ECCB in March and also attends on-going meetings of CFATF.

18. There is also an on-going effort to upgrade relevant legislation. In 2001 the Mutual Legal Assistance in Criminal Matters Treaty (Government of Grenada and Government of the United States of America), and the Extradition Treaty (Government of Grenada and Government of the USA) were enacted to document understandings previously negotiated. In addition, an amendment of the International Business Companies Act (being drafted) will impose constraints on the disposal of bearer shares. An amendment to the Offshore Banking Act last month will restrict GIFSA from promoting offshore business so that it can concentrate on its core supervisory responsibility.

19. On June 12, 2001, the authorities issued a comprehensive set of anti-money laundering guidelines at all financial institutions including commercial banks, offshore banks, insurance companies, credit unions, and money transfer agencies.

20. The authorities accept in principle the desirability of integrated supervision of onshore and offshore financial institutions. In this regard there will continue to be close collaboration between the revamped GIFSA and the ECCB. However, the modalities are still being worked out subject to consideration of capacity and the evolution of sub-regional arrangements.

Technical Assistance

21. The authorities have been engaged in upgrading weaknesses in the statistical base and recently, Grenada completed requirements for participation in the Fund's General Data Dissemination System (GDDS). There is also an ongoing programme of technical assistance from the Caribbean Development Bank (CDB) to facilitate institutional strengthening in various government agencies, training for small and micro enterprises, project preparation and pre-feasibility studies, and consultancy services for the small hotels sector. The authorities also want to train professionals to support the privatisation process (mainly in IT and Accounts). The new Caribbean Technical Assistance Center (CARTAC) will also be another avenue through which technical assistance can be provided.

The Road Ahead

22. Grenada has benefited from sound macroeconomic policies and its commitment to structural reform to facilitate a private sector-led growth path. It is important to sustain this momentum in order to provide resources to alleviate poverty and reduce unemployment. In this regard, Grenada continues to benefit from the fixed exchange rate as an ECCB member. Other sub-regional approaches, particularly in the areas of health, VAT, harmonisation of fiscal incentives, trade policy, and financial supervision will continue to be explored.