Barbados

Prepared by: Ravi Kurjah
ravi.kurjah@firstcitizenstt.com
Last Updated: October 2016

First Citizens
Research & Analytics

COUNTRY	
Real GDP growth (%) 2016	1.0% (S&P)
Next General Election	February 2018
Exchange Rate (BBD/ USD)	2.00

CREDIT RATING	
S&P Foreign Currency	B (Negative)
Fitch Foreign Currency	N/A
Moody's Foreign Currency Debt	Caa1 (Stable)

Major Trade Partners: U.S.(23.1%), T&T (12.4%), E.U. (7.8%), Guyana (5.2%)
Major Exports (%): Agricultural products (23.1%), Fuels (24.8%), Manufactures (52.0%)
GDP Composition: Services (82%), Industry (14%) and Agriculture (3.1%)

RECENT ECONOMIC DEVELOPMENTS

ECONOMIC OUTLOOK — **STABLE**

Barbados recorded economic growth of 1.3% over the first nine months of 2016, compared to 0.4% growth for the same period 2015. The economy expanded, significantly due to a 3% improvement in tourism, a 5% increase in construction and a 3% rise in business and other services. Concerns over Zika and Brexit have so far had a muted impact on the country's tourism sector. According to BMI, real GDP growth is forecasted to close at 1.0% and expected to accelerate modestly to 1.6% in 2017. Arrival numbers to Barbados have thus far shown few signs of slowdown. However, economic activity generated by Barbados' tourism sector is expected be tempered by government austerity initiatives, as officials seek to rein in expenditure.

INFLATION
MONETARY POLICY — **NEGATIVE**

Deflation of -1.2% for the first nine months of 2016 was recorded, significantly down from an average increase of 1% in 2015. Relatively low oil prices and the private sector's lack of confidence will keep inflation low. As a result of the significant drop in oil prices during 2015 and the stagnant economy, the island observed 1% deflation (first deflation since 1998), following average inflation of 1.9% during 2013-2014. Following the announcement of major hotel projects on the island and some pickup in growth, S&P expects inflation during the two to three years to be around 2%, which is still lower than the 10 year average of 4.5%.

TRADE BALANCE/ BOP — **STABLE**

Barbados' external accounts position will improve over the coming years as its tourism sector expands and weak domestic conditions limit import growth. Although a narrower current account deficit will reduce external debt accumulation, Barbados will continue to face weakening sovereign credentials. The current account deficit for nine months ended 2016 was lower by 3.6% of GDP, almost entirely because of tourism. Fuel imports were down by 1.9% of GDP, with a fall in both prices and the amount imported. The primary driver of Barbados' improving current account will be the expansion of its tourism sector. Tourism underpins the country's robust services trade surplus, equal to 21.2% of GDP in 2015, and is a major destination of foreign investment into Barbados economy.

FISCAL ACCOUNTS — **NEGATIVE**

The deficit for the 2016 April to September period is estimated to be BBD145 million on the current account. Accrued tax revenues are anticipated to increase by BBD13 million, with corporate taxes, property taxes, and excises increasing by BBD6 million, BBD14 million and BBD10 million respectively. Small reductions in grants to state-owned enterprises (BBD5 million) and in wages and salaries (BBD8 million) were more than offset by a BBD34 million increase in interest payments because of rising debt levels. Stricter control over expenditure at state-owned enterprises (SOE), some one-off revenues from the sale of the Barbados National Terminal Company, and the full impact of the fiscal measures announced in 2015 and 2016 should reduce the fiscal deficit (and change in government debt) toward 5% of GDP during 2016-2018. Ultimately, the management of SOE finances poses a risk to the success of the fiscal consolidation of the government. On Aug. 15, 2016, the government announced additional fiscal measures and a midterm financial and economic review. This process updates the pro forma budget proposal laid out in March, with updated economic assumptions, and incorporates further planned fiscal tightening. Moreover, the government introduced a social responsibility levy (2% on imports except those for tourism, construction, and agriculture) to fund health expenditure and increased the bank asset tax to 0.35% (from 0.2%). Finally, the government plans to reduce transfers to SOEs during the next four years below BBD1 billion, where they have stood for the last five fiscal years, through improving its control on its SOE's expenditures and refinancing arrears.

CREDIT RATINGS — **NEGATIVE**

On September 23, 2016 S&P downgraded Barbados' long term sovereign credit ratings to B- with a negative outlook from B due to high fiscal deficit. According to S&P, the rationale for the downgrade was persistently high fiscal deficits, reflecting both budget slippage and unbudgeted spending. The central bank continues to directly finance the government, which S&P considers at odds with its goal to defend Barbados' long-standing currency peg with the U.S. dollar.
On April 01, 2016, Moody's Investors Service ("Moody's") downgraded Barbados' government bond rating and issuer rating to Caa1 and changed the outlook to stable. Moody's decision to downgrade Barbados' issuer and bond ratings to Caa1 from B3 and revise the outlook to stable from negative was driven by slow progress towards achieving fiscal consolidation consistent with a sustainable debt trajectory and low level of foreign exchange reserves and weak funding conditions.

BUDGET 2017

Revenue raising measures:
- Implementation of a 2% import levy on all imports except goods for the manufacturing, agriculture and tourism sectors. It is estimated that the levy will raise annual revenues of BBD60.8m
- Increase Bank Asset Tax from 0.2% to 0.35% effective immediately, with the assessment period for the assets starting from 1 April, 2016.The average additional revenue is expected to be BBD14.3m.The estimated intake is BBD33.3 million using the 2015 asset base of the banking system.

Expenditure targets:
- Aim to reduce transfer by at least BBD50m annually for the next four years.
- Intention is to cut expenditure by BBD25m from all areas of discretionary expenditure and to target an additional BBD25 million in spending adjustments fowling the proposed mid-term Estimates review with all ministries.

Social development:
- Old age pensions increase by BBD40 per month. This is expected to cost the Treasury an additional BBD3.2million a year.
- The Retraining Fund which is managed by NIS will be invited to invest in a special Treasury Bill Issue to the tune of BBD5m to provide an immediate injection to the Student Revolving Loan Fund.
- A Working Committee led by the Ministry of the Civil Service will advise the cabinet on the procedure and legal requirements for appointing all temporary officers to permanent positions in the Public Service with more than three years' continuous service.

OUTLOOK

While the present administration is making an attempt to improve Barbados' fiscal status, consolidation and weak competitiveness will continue to hamper Barbados' economic recovery. There have been signs that the ability to borrow in the domestic market at low rates is diminishing and access to external markets has been affected by successive downgrades. The Central Bank's current projection for economic growth in 2016 has been lowered to 1.5%, mainly because most major investments projects are behind schedule. Although growth has resumed and short-term prospects are positive, imbalances persist between available resources and government programs. While developments have provided some room for maneuver, Barbados remains highly vulnerable and may not realize its potential without deep-seated reforms to align revenues and expenditures, and reduce debt. As a result of this and based on the trajectory of the fiscal accounts and pace of debt accumulation First Citizens Research & Analytics holds a **cautious** view on Barbados.