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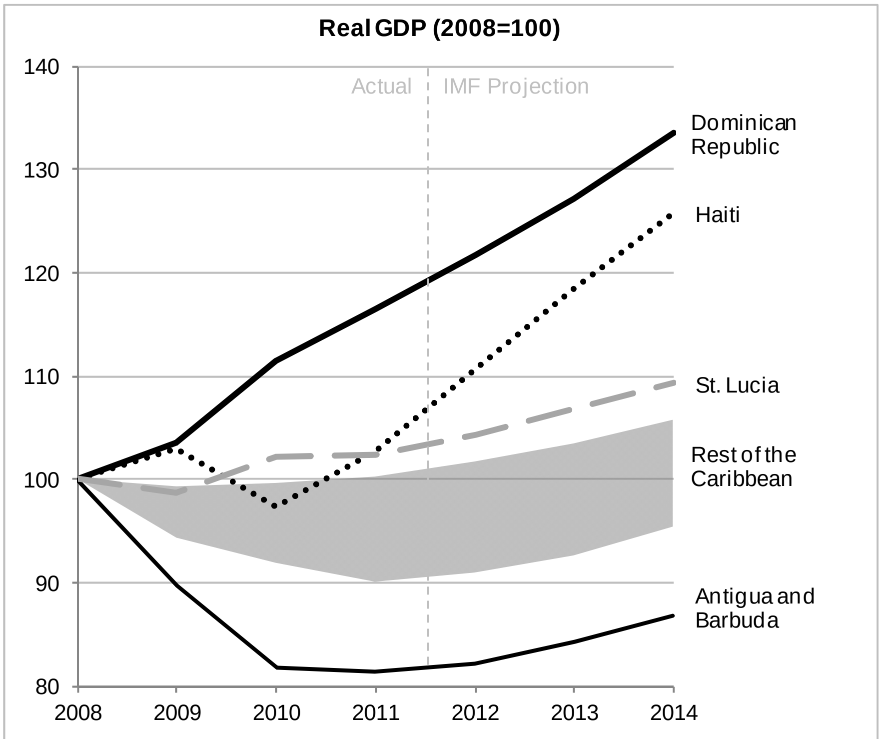
EADS Economic Trends Report
Caribbean

May 2012

Economic Overview

In the Caribbean economies, growth remained weak at an average 1.5 percent in 2011 with the output gap still negative. Growth was weighted down by high public debt levels, fiscal consolidation, high oil prices and weak performance in the tourism sector and a series of natural disasters. Torrential rains in April 2011 caused major flooding and landslides in St. Vincent and the Grenadines, which severely damaged the country's infrastructure. These followed hurricane Thomas, which had destroyed roads and bridges, and battered the agriculture sector, just half a year earlier. The combined negative effect of these two disasters is estimated at 3.6 percent of GDP.



SOURCE: IMF, *World Economic Outlook*, April 2012.

Antigua and Barbuda has struggled more than others to stabilize economic activity. Economic activity continued to contract in the first six months of 2011. Despite these difficulties, tourist arrivals have rebounded modestly since 2010, particularly towards the end of 2011. Overall though, output remains weak with activity in the construction sector remaining slow.

Slow growth in high-income countries has constrained growth in tourism revenues in the Caribbean. Tourism arrivals were up 4 percent in the first part of 2011, following growth of 3 percent in 2010. Performance in this region has been weaker than in South America where tourist arrivals increased 13 percent in the first eight months of 2011, following a 10 percent expansion in 2010. While South America benefited from a 44 percent increase in travel spending in Brazil, the United States, one of the Caribbean's main markets saw a much smaller 5 percent expansion on travel expenditure.

The Dominican Republic is the fastest growing economy in the region with a predicted growth rate of 4.5 percent in 2012, boosted by a favorable business environment and several new mining projects. The country's tourism sector seems to be finally picking up with foreign tourist arrivals increasing by 4.2 percent in 2011, which is good news both for the current account and economic activity, as the hospitality sector is the second largest after industrial manufacturing. While the current account is expected to post a negative balance in 2012, the elevated financial surplus should cover the gap, thanks primarily to significant FDI to the island's burgeoning mining sector. Goods exports are also expected to do well, particularly those from the island's free trade zones.

Countries covered in this report: Antigua and Barbuda, Bahamas, Dominica, Dominican Republic, Grenada, Haiti, Jamaica, St. Kitts and Nevis, St. Lucia, and St. Vincent and Grenadines. Due to data and space limits, not all countries are represented in every graph or analytical section.

The Bahamas will see some limited economic growth, 2.5 percent in 2012 up from 2.0 percent in 2011 and 0.9 percent in 2010, mainly driven by an uptick in gross capital formation from 2012 onwards and to a lesser extent by private consumption, as tourist arrival numbers pick up and the domestic economy begins to recover.

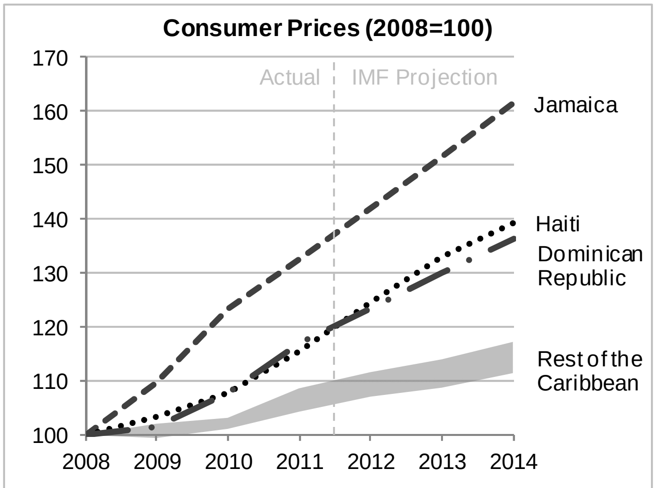
Following three years of negative growth in Jamaica, real GDP grew by 1.5 percent in 2011, primarily from increases in agriculture and bauxite/alumina production. However, economic growth in Jamaica remains sluggish at a predicted rate 1.0 percent in 2012. Unemployment remained high at 12.8 percent and the fiscal situation deteriorated with the public sector deficit predicted to increase to 7.3 percent of GDP and the ratio of debt to GDP at 140 percent of GDP.

On the positive side, commodity exporters will continue to benefit from robust demand from emerging Asia, although incomes will be affected by lower commodity prices. Growth in the Caribbean is expected to hover around 3 percent, supported by growth in the Dominican Republic. Growth in the Organization of Eastern Caribbean States will remain weak with high public debt burdens crowding out private investment and constraining growth. Slightly higher remittances should provide some relief to private consumption in countries such as Haiti and Jamaica, countries, which are heavily reliant on migrant remittances. However, continued high unemployment in the United States is expected to limit the recovery in the tourism sector.

Real GDP Growth, 2012 (IMF Projections)	South America 3.9%	Central America 3.8%	Mexico 3.6%	Caribbean 2.5%

Inflation

As compared with other regions, monetary authorities in the Caribbean do have some room to ease, having tightened monetary policy in the first half of the year. In addition, inflation expectations in most inflation-targeting economies are well anchored and monetary policy rates are close to neutral in most of these economies.



SOURCE: IMF, *World Economic Outlook*, April 2012.

Despite moderating somewhat, inflation in Jamaica remains high, growing at a rate of 7.0 percent in 2011 and 2012, down from 12.6 percent in 2010. This slow down reflects both moderate food and oil prices increases and real exchange rate appreciation. Interest rates continued to fall and the exchange rate remained stable. Even if global growth weakens monetary policy may have to remain relatively tight to bring inflation back down to acceptable levels.

Inflation in Haiti remains in the single digits, even though it grew by 7.4 percent in 2011. Rising food and energy prices pushed inflation to 10.4 percent at end-September before receding to 8.3 percent in December 2011. Non-food inflation has also begun to recede.

CPI Inflation, 2012 (IMF Projections)	South America 7.7%	Central America 5.4%	Caribbean 4.1%	Mexico 3.9%

Banking and Financial Sector

Countries such as Jamaica, which have estimated external financing needs of more than 15 percent of GDP in 2012, are more vulnerable to a deepening of the financial stress in the euro area. A reversal in capital flows, a drying up of credit, or a hike in interest rates may force these countries to sharply reduce their external financing gap by adjusting the current account, and/or closing the external financing gap through depletion of foreign exchange reserves and increased reliance on foreign aid. The World Bank recommends that these countries (Jamaica, Guyana, Panama and Nicaragua) pre-finance their financing needs to avoid sharp cuts in government and private sector spending.

Financial vulnerabilities remain high. Foreign bank ownership in the Caribbean is high and banks could be vulnerable- especially given the specialization of some banks in high-risk and relatively weakly regulated hedging and derivative activities. Financial sector indicators in the Eastern Caribbean Currency Union are deteriorating, having been hard hit by the 2008–2009 crisis and the slow economic recovery with some banks facing solvency issues that could require further intervention.

Countries with highly dollarized financial systems could also be exposed through currency risks. These risks are somewhat mitigated in countries that have large stocks of international reserves, which would allow central banks to inject liquidity into the banking system in the event of a credit crunch and to stabilize the currency in the event of excessive exchange rate volatility.

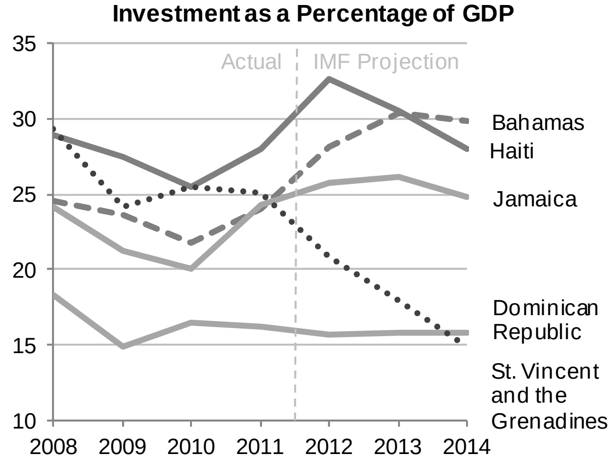
Jamaica's current account deficit is expected to widen in 2012 on the back of a growing goods trade deficit. While the current account deficit will continue to be financed by a surplus in the financial account, downside risks to the balance of payments remain in weak investment in 2012 and in the government's failure to meet its IMF fiscal consolidation targets.

Investment

Increased risk aversion internationally and the confidence effects associated with the euro area financial crisis will weigh on foreign direct investment (FDI) inflows, which account for a particularly large share of the national income of the Organization of Eastern Caribbean States.

In St. Vincent and the Grenadines, the construction of the Argyle International Airport and terminal building is expected to sustain growth somewhat over the next few years by expanding tourism, given some weakness in other sectors.

Investment as a Percentage of GDP



SOURCE: IMF, *World Economic Outlook*, April 2012.

In the Dominican Republic, the development of new mining projects has already seen FDI increase by 29.5 percent in 2011. With the country's strong business environment (ranked108 out of 183 on the Doing Business Index), further investment into the mining sector is expected.

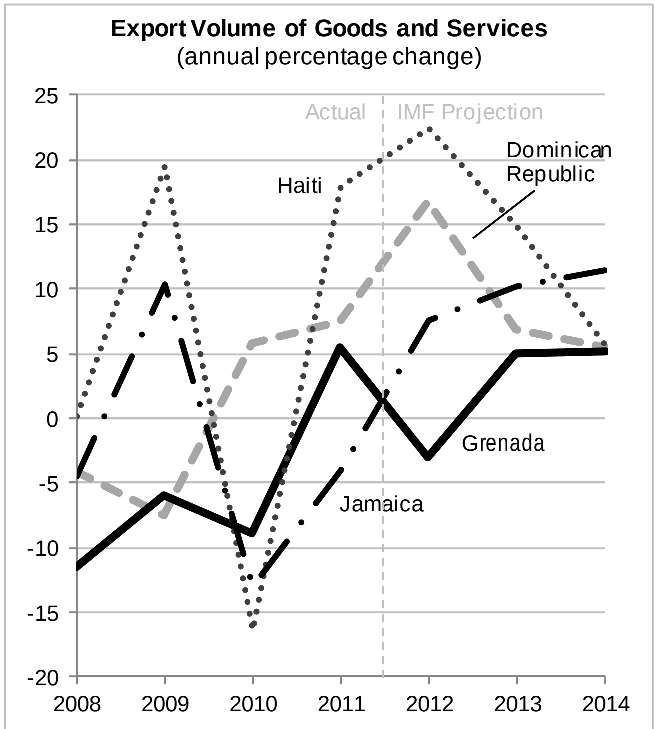
Total Investment, 2012 (as a percentage of GDP) (IMF Projections)	Caribbean 27.8%	Mexico 25.0%	Central America 22.7%	South America 22.6%

Trade

The goods trade deficit in Jamaica is expected to widen slightly in 2012 as a slowdown in sugar prices will drive down exports. In addition, the continued slowdown in the U.S. has limited demand for Jamaican alumina and bauxite, leading to a decrease in export volume of 4.0 percent in 2011. However, exports are expected to bounce back in 2012 with a growth rate of 7.5 percent in 2012.

In 2011, exports in Haiti grew 18 percent after a decrease of 16 percent in 2010, reflecting a significant increase in exports of textiles, helped by improved access to the U.S. market under the HOPE/HELP Initiatives. Exports are expected to grow another 22 percent in 2012.

Exports in the Dominican Republic, the largest economy in the region, grew by 7.5 percent in 2011 and are expected to grow a further 16.8 percent in 2012.



SOURCE: IMF, *World Economic Outlook*, April 2012.

Export Volume of Goods and Services, 2012 (annual percentage change) (IMF Projections)	Mexico 12.8%	Caribbean 5.8%	Central America 4.7%	South America 4.2%

The Recovery in Haiti

The January 2010 earthquake's destruction and economic losses were massive, estimated at 120 percent of GDP. A total of 300,000 houses, 13 out of 15 ministries, 4,200 schools and more than 60 percent of the country's hospitals were damaged or destroyed. Haiti's growth rate in 2010 is estimated at -5.4 percent. Growth has resumed, inflation remains at single digit levels, and the fiscal and external positions have strengthened and essential state functions have now been restored. However, the reconstruction has been slower than anticipated and the challenges ahead remain daunting. While camp occupancy has dropped by half, more than half a million people are still in temporary shelters.

The challenges ahead remain daunting. The unemployment rate is above 60 percent and most Haitians live below the poverty line. The health situation remains poor and in 2011, Haiti ranked 158 out of 187 countries on the

UNDP Human Development Index. Haiti is vulnerable to global downside risks through lower exports, external assistance and remittances. In addition, deterioration in the security situation and natural disasters could disrupt economic activity.

Political stability and an acceleration of the reconstruction efforts will be critical to strengthen the economic recovery in 2012. A rebound in agriculture and buoyant activity in construction and manufacturing are projected to contribute to boosting growth to 7.8 percent in 2012. Inflation should recede to 7.7 percent assuming that the shock from international food prices diminishes, domestic food production recovers and the supply chain improves.

Looking forward, Haiti's government should sustain high growth, alleviate poverty and strengthen the country's resilience to external shocks. This will depend on the success of its reform program in raising domestic revenue intake, improving the quality of public spending, public services and the business environment, as well as strengthening institutions.

Additional Information

For questions or more information, please contact the author, Marie-Ellen Ehounou, at mehounou@devtechsys.com.

For country-specific data and additional information about the countries covered in this report, please visit the EADS Country Portal at http://esdb.eads.usaidallnet.gov/query/do?_program=/eads/esdb/countryPortal.

Sources used in compiling this report include the semi-annual *World Economic Outlook* from the International Monetary Fund (http://www.imf.org/), the *Global Economic Prospects* and *Doing Business* Reports from the World Bank (http://www.worldbank.org/) and Business Monitor International Business Forecast Reports (http://www.businessmonitor.com/).