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Caribbean Faces Tough Macro Outlook

Global crisis has spanked the Caribbean and the bad news just keeps coming. Amid contracting liquidity, the region is pained by bruised tourism revenues and battered remittances.

by Taina Rosa



Global economic slowdown comes at a perilous time for the fragile Caribbean. Evaporating liquidity, declining tourism and flopping remittances come on the heels of storms and an increase in food prices.

This all puts the brakes on regional growth. BCP Securities expects Caribbean GDP expansion to slow to 0.4% in 2009 from 3.5% in 2008 and 7.0% in 2007. The biggest contractions in GDP, the shop estimates, will happen in Jamaica, set to shrink by 3.5% this year.

"Most Caribbean countries are highly exposed to the US economy as the US is their main trading and investment partner, and as a result, some regional economies are expected to contract substantially," says Neeraj Arora, LatAm strategy associate at JPMorgan.

The region's largest economy, the Dominican Republic, saw GDP increase 5.3% in 2008, but it is not expected to see any growth this year, according to JPMorgan. In 2010, the shop forecasts, the country's GDP should expand by 3.0%.

"The second half will probably be tough. A rebound will depend on how the global economy evolves," says Fitch senior director Theresa Paiz-Fredel. She adds that before the downturn, the Dominican government projected GDP would grow about 3.0% in 2009, from 5.3% in 2008.



Allegations of corruption, says Díaz

Trinidad & Tobago is seen as the Caribbean country best prepared to weather the downturn, despite ongoing troubles related to the CL Financial collapse. The major exporter of oil and natural gas should benefit from a rebound in commodities.

JPMorgan expects T&T's GDP to stay flat in 2009, before swelling by 2.5% in 2010. Between 2003 and 2007, T&T's GDP expanded by an average 9.2% and an estimated 3.5% in 2008, it adds.

JPMorgan paints a gloomier picture for Jamaica. The country's GDP contracted 0.6% in 2008 and the shop agrees with BCP that it will shrink by 3.5% this year. JPMorgan forecasts a 1.0% GDP bounce in 2010.

According to JPMorgan, exports have contracted 47% on average in Jamaica through the first quarter, ended March 31, largely owing to a slump in bauxite. In the Dominican Republic, exports have fallen 24.1% in the same period, it adds.

Hit Where it Hurts

Tourism, the heart of the Caribbean economy, has been suffering as cash-strapped travelers from North America and Europe opt to stay home or spend less on vacation. According to the World Travel & Tourism Council (WTTC), in 2008 tourism contributed \$39.9 billion to the Caribbean economy. This is expected to decline by 9.2% in 2009, says the WTTC. According to data from the Caribbean Tourism Association, tourist arrivals to the Dominican Republic dropped 4.8% in the period of January to April, compared to the same period of 2008. Other islands were also hit.

Despite a recovery in May, driven by tourists' concerns about drug-related crime and swine flu in Mexico, more tourism dollars have not flowed into the region. Arora explains that broadly speaking, arrivals are up, but spending is down. For instance, even after getting more arrivals in January to mid-July of 2009, Jamaica's tourism earnings fell \$70 million, or 6%, to \$1.1 billion, versus the same period of the previous year, he says.

For the Dominican Republic, adds Franco Uccelli, a VP for EM research at JPMorgan, tourism earnings fell about 8.0% from January to March to \$1.26 billion from \$1.37 billion in the same period in 2008. Tourism earnings make up about 9.1% of the Dominican Republic's GDP, he says.

Meanwhile, remittances, a major source of income for the region, are in decline. Arora says that remittances represent as much as 15% of some local economies.

"All of the countries in the region reported major declines in remittances. Not only is this creating problems on balance of payments, it is hurting the lower income levels very hard," says Walter Molano, head of research at BCP Securities.

For the first quarter of 2009, Dominican Republic remittances fell by 7.1% to \$722 million from \$777 million in the corresponding quarter of 2008, says Arora.

Paiz-Fredel says that remittances account for 7%-8% of the Dominican economy. "It's lower than in other countries in Central America and the Caribbean, but it is still significant enough to have an impact on the economy," she explains.

According to JPMorgan, remittances to Jamaica dropped 15.0% to \$415 million in the first quarter of 2009 from \$488 million, compared to the same period in 2008. Remittances make up 14.2% of Jamaica's \$14.3 billion GDP.

Caribbean Real GDP Growth				
DR doing best				
	2007	2008	2009	2010
Trinidad & Tobago	5.5%	3.5%	0.0%	2.5%
Dominican Republic	8.5%	5.3%	0.0%	3.0%
Barbados	3.3%	0.7%	-3.0%	1.0%
Jamaica	1.4%	-0.6%	-3.5%	1.0%

Source: JPMorgan

Salt in the Wound

In February, the central bank of Trinidad & Tobago announced that it would bail out financial services companies Clico Investment Bank (CIB), Clico Insurance Company, British American Insurance Company and Caribbean Money Market Brokers (CMMB), all of which are within the CL Financial Group, as they had been facing liquidity pressures. The government took control of CIB and transferred third party assets and liabilities of both CIB and CMMB to government-controlled First Citizens Bank.

"The problems at CL Financial apparently stemmed in part from the sharp drop in methanol and real estate prices, but also from risky practices that included excessive related-party transactions," says JPMorgan. As part of the bailout, the central bank had said it would sell, liquidate or collateralize its assets and use proceeds to meet funding requirements for both Clico and British American. It plans to provide full funding support to meet any remaining deficits.

According to the central bank, excluding CIB, Trinidad & Tobago's banking system is well capitalized, as the average capital adequacy ratio stands at 18%, and it is not facing undue liquidity challenges. The government took over CL Financial's local assets in June.

Meanwhile, the Stanford Bank scheme, said to amount to \$7 billion and to have spread practically all over LatAm and parts of the Caribbean, is also impacting the region, particularly Antigua & Barbuda. "The impact is significant, not only because you take out a major employer, but also because it subjects government officials to allegations of corruption," says Michael Díaz, managing partner of Miami-based Díaz, Reus & Targ, one of the law firms trying to help burned investors in the case. Stanford was Antigua & Barbuda's largest private sector employer before the company came under microscope of the SEC and was placed in receivership. While Allen Stanford, the head of the disgraced bank, has not been found guilty of running a Ponzi scheme, Díaz says there is a "substantial likelihood" that he will be.

Wendell Mottley, managing director with Credit Suisse, says the Stanford and CL Financial issues have aggravated the problem. "A number of pension plans throughout the Caribbean were hurt by the demise of CL Financial. These losses are in the hundreds of millions of dollars, excluding T&T, where the central bank has said it sees a deficit of \$5 billion Trinidadian dollars."

Just Sun, Sand and Sea

But that is not the only dire effect. Arora says that the cost of the bailout of CL Financial, estimated at about 3%-4% of T&T's GDP, which in 2008 was about \$25 billion, may constrain government expenditures that have supported growth in the past. "However, it seems that the CL Financial situation has been contained and the spillover effect to the rest of the banking system has been limited," he adds.

Mottley believes that ultimately, the government will sell off CL Financial assets to recoup money spent on the bailout. "However, it is taking a cautious approach, a wise approach. It doesn't want to be pressed into fire sales," he adds. The sale of a 55% stake in Republic Bank and a 56% in Methanol Holdings in Trinidad & Tobago are on hold until the global economy strengthens and stabilizes, says Carl Hiralal, inspector of financial institutions at Trinidad & Tobago's central bank. "There has been no decision to sell yet. These are good assets and this is not the best time to sell them," he tells LatinFinance.

Bankers in Trinidad said in April that Canada's CIBC, which holds a 91% stake in the country's First Caribbean Bank, is the most likely buyer of the 55% stake in Republic. It could cost \$1.3 billion to buy the chunk, according to a banker who asks not to be identified. However, a senior Republic executive says his institution is not interested in acquiring the shares.

One strategy the Caribbean could use to better handle future economic crises, believes Mottley, is to diversify away from tourism. "Without counting T&T's energy sector, the Caribbean has not been able to find a way economically to be of service to the rest of the world."

"This fundamental problem persisted before the crisis and the crisis has exaggerated that lack of direction, drive and leadership to find its way in the wider world," adds the banker. Most of the Caribbean, excluding T&T, is still just "sun, sand and sea," in Mottley's opinion. **LF**