Statement by Ms. Levonian, Executive Director,
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on Eastern Caribbean Currency Union
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Our Eastern Caribbean Currency Union (ECCU) authorities welcome the Staff Report for the 2021 Common Policies Discussion. The comprehensive report broadly reflects developments in the Currency Union within the context of the ongoing COVID-19 pandemic and embraces the actions and proposals that are being pursued to steer post-pandemic recovery, safeguard macroeconomic stability, support inclusive and sustainable growth, and build resilient economies. Our authorities appreciate their ongoing engagement with Fund staff and the candid dialogue that characterizes these discussions.

Framework for COVID-19 recovery

The pandemic has hit the economies of the ECCU hard with GDP for the Currency Union as a whole estimated to have contracted by 16 percent in 2020, with steeper declines in the more tourism-dependent economies. The economic losses are a direct impact of containment actions, including the closure of borders and strict lockdown measures, implemented to reduce the spread of the virus. Inflation has been contained at 0.2 percent year on year in December in line with the consumer price index in key trading partners.

The containment measures allowed for the first wave of the pandemic to be reasonably well-contained, with relatively low levels of infections and deaths. However, as borders were re-opened and global infections increased, the number of cases rose and eventually led to a re-implementation of containment measures.

As early as March 2020, several measures were implemented in ECCU member countries to mitigate the impact of the pandemic. These included increased health care spending, cash payments to vulnerable households, income support for displaced workers in the tourism and other sectors, tax and import duty deferrals, and accelerating the implementation of the public sector investment program, where possible, to boost employment. In addition, the Eastern Caribbean Central Bank (ECCB), in collaboration with the commercial banks, agreed to exercise regulatory forbearance and introduced measures in the banking sector, such as granting of moratoria on loan repayments. The actions taken by the commercial banks were largely replicated in the non-bank sector which is dominated by credit unions. In addition, the ECCB reduced the discount rate from 6.5 to 2 percent and the long-term credit interest rate from 6.5 to 3.5 percent to ease access to Central Bank credit for member governments and licensed financial institutions.

The ECCB proposes to implement a Program of Action for Recovery, Resilience and Transformation (PARRT) to help support the recovery process and pursue a path towards sustainable and resilient economic growth. The program was endorsed by the Monetary Council of the ECCB in October 2020 and is expected to be implemented over a three-year period. It consists of proposed policy actions to be undertaken at both the national and the regional levels and is built on the following four pillars:

1. Financial stability
2. Fiscal and debt sustainability
3. Resilient and inclusive growth
4. Payments modernization and digital transformation

Aspects of the program are already being implemented. For instance, in the context of pillar 4, on 31 March 2021, the ECCB launched 'DCash'- a digital currency that became the world's first retail central bank digital currency (CBDC) to be publicly issued within a formal currency union.

Financial and Monetary Sector Developments

Financial sector conditions are relatively sound with ample liquidity buffers and a stable deposits base. Nevertheless, several downside risks exist and safeguarding financial stability is crucial. Uncertainty about the duration of the pandemic is a major risk. Although accommodative financial sector policies have so far been appropriate, prolonged regulatory forbearance will mask weaknesses in the sector.

Maintaining a strong currency is a major policy objective. Despite the economic challenges and the uncertainties in the external sector, the exchange rate parity with the US dollar has remained fixed. Foreign reserves remain high and no change in the exchange rate is anticipated.

Our authorities agree with staff that comprehensive crisis management plans for implementation at the regional and national levels should be prepared. To that end, the main objectives of the financial stability pillar of the PARRT are structured to maintain stability in the entire financial system while stimulating economic growth. The authorities will ensure that the non-bank financial system operates within the applicable guidelines provided by the single regulatory units of individual governments. Likewise, licensed financial institutions will be required to operate within prudential benchmarks and relevant guidelines issued by the ECCB. In addition, actions will be taken to maintain the stability of the financial system through the support of recapitalization, effective resolution strategies, optimal liquidity management, and improved information exchange.

Sustained efforts are needed to address remaining financial sector weaknesses. The ECCB will work with Governments to build the databases that are needed to enrich the quality of banking sector assessments. These assessments will help with the identification of institutions which pose high systemic risk, especially those with very elevated NPL levels. The tourism shock is projected to almost triple banks' NPLs. Regional efforts to reduce NPLs will continue. One option is through purchases by the Eastern Caribbean Asset Management Corporation (ECAMC) which was established by the Monetary Council for that purpose. The alternative is through private sector asset management companies that are providing that service.

Corresponding Banking Relationships (CBRs)

The loss of correspondent banking relationships (CBRs) remains a concern for the region and poses a risk to financial stability. Although there have been no new terminations of CBRs, recent legislative changes in the U.S. could increase the cost of compliance, a key factor in the decision of correspondent banks on whether to provide services to Caribbean respondent banks. This action could re-elevate the risk of losing CBRs and magnify the concerns of potential impact on the banking sector and the economy more generally. With two foreign banks exiting the market in the last 18 months, domestic banks now serve close to two-thirds of the market. This highlights the magnitude of the challenge if ECCU domestic banks are not able to maintain adequate CBRs.

Our authorities will continue to pursue initiatives to prevent further loss of CBRs by adopting global regulatory standards, implementing reforms targeted at improving the AML/CFT framework, as well as to improve governance in undertaking all financial transactions. However, standards for AML/CFT continue to change and are adopted and implemented at significant cost. Enhancing capacity to address these issues remains a priority.

Our authorities look to the Fund and other multilateral institutions for the technical support to continue to enhance the AML/CFT framework and leveraging digital tools for transaction monitoring.

Fiscal Policy and Debt Management

The pandemic has worsened the fiscal situation of ECCU member states. Largely as a result of steep declines in GDP, the ECCB has recommended that member countries delay the achievement of the fiscal anchor of 60 percent debt to GDP ratio from 2030 to 2035. Public debt levels are high and increasing in several countries as new debts were incurred to finance the pandemic response. Accordingly, our authorities are committed to making well-focused and concerted efforts to improve fiscal performance and achieve debt reduction goals across the ECCU.

Our authorities agree that stronger fiscal consolidation efforts are needed to attain the debt targets by the revised date of 2035. The pace at which the target will be achieved will vary from country to country. ECCU member states are committed to prioritizing fiscal discipline, including through the adoption of fiscal rules. Well-articulated fiscal frameworks and comprehensive recovery plans are necessary along with the ECCB PARRT.

Measures to enhance revenue administration and collection are necessary. ECCU member states will need the assistance of development partners in raising the financing for closing the fiscal gap. This will be complemented by increasing domestic revenues. In that regard, technical support to achieve this objective is vital. For those states that rely heavily on resources from the Citizenship by Investment Programs, strengthening the governance in the operation of these programs will be undertaken to ensure greater sustainability.

Our authorities welcome the Fund's preparation of a comprehensive climate change strategy, including the plans to include climate change issues in surveillance and the preparation of a climate change dashboard. The ECCU countries are ranked among the most natural disaster-prone countries worldwide and are barely able to build buffers because of the frequency of climatic events and other natural hazards. The ongoing eruption of the La Soufriere volcano in St. Vincent and the Grenadines is evidence of the risks to which ECCU member states are exposed. **Building resilience is not optional and access to funding for resilience building is critical**. We continue to advocate for special consideration to be given to Small Development States (SDSs), including those of the ECCU, in light of their high level of vulnerability, and urge the Fund to work with other multilateral institutions in addressing this urgent and important matter.

Achieving Sustained and Inclusive Growth

The road to returning to pre-pandemic GDP levels could be long and protracted if the pandemic is not contained. As such, our authorities will pursue a path to achieving sustained and inclusive growth that is multifaceted. In the first instance, the focus will be on ensuring that the population is fully vaccinated in tandem with tourism source markets, which is needed to fully reopen the tourism industry as soon as possible. In this context, the Fund should continue its advocacy for vaccine equity among all countries. Additionally, our authorities continue to make investments in other sectors such as agriculture, physical infrastructure, renewable energy, and digitalization to lay the foundations for sustained and inclusive growth.

Our authorities remain committed to removing obstacles to doing business that impact on growth outcomes. Investments in education and continued support to the health sector will improve the quality of the labor force. New legislation to provide for the establishment of a credit bureau and simplifying foreclosure processes are all intended to encourage private sector investment.

The ECCU will pursue these developments in a coordinated manner and within the context of the OECS Economic Union framework**.**

Capacity Development

Central to the successful implementation of the ECCU recovery plans is the availability of technical support. Our authorities are grateful to the Fund's area and functional departments as well as the Caribbean Regional Technical Assistance Centre (CARTAC) for their tremendous efforts in facilitating capacity building in the ECCU and look forward to the continued strong support of the Fund in this regard.

Conclusion

Our authorities remain cognizant that much more needs to be done to achieve the long-term vision for the ECCU. Despite numerous challenges, our authorities are not daunted by the tasks that lie ahead and are keen to take the necessary steps to rebuild in the aftermath of the pandemic. Strengthening integration and greater collaboration among member states will make the development efforts more effective.

The support of the international community, including the Fund, as well as technical and financial assistance are critical to the success of the ECCU's plans to preserve macroeconomic stability, develop sound financial systems, and ensure sustainable, inclusive growth.