INTERNATIONAL MONETARY FUND

ST. KITTS AND NEVIS

STAFF REPORT FOR THE 2021 ARTICLE IV CONSULTATION—INFORMATIONAL ANNEX

July 29, 2021

Prepared By: The Western Hemisphere Department (in collaboration with other departments and institutions)

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FUND RELATIONS

(As of May 31, 2021)

Membership Status: Joined August 15, 1984; Article VIII.

General Resources Account:	**SDR Million**	**Percent of Quota**
Quota	12.50	100.00
Fund holdings of currency	11.52	92.15
Reserve position in the Fund	0.98	7.86

SDR Department:	**SDR Million**	**Percent of Allocation**
Net cumulative allocation	8.50	100.00
Holdings	4.64	54.63

Outstanding Purchases and Loans: None

Latest Financial Arrangements:

Type	Date of Arrangement	Expiration Date	Amount Approved (SDR Million)	Amount Drawn (SDR Million)
Stand-By	Jul 27, 2011	Jul 26, 2014	52.51	47.37

Overdue Obligations and Projected Payments to Fund[1/]:
(SDR Million; based on existing use of resources and present holdings of SDRs):

			Forthcoming		
	2018	2019	2020	2021	2021
Principal	0.00	0.00	0.00	0.00	0.00
Charges/Interest	0.00	0.00	0.00	0.00	0.00
Total	**0.00**	**0.00**	**0.00**	**0.00**	**0.00**

[1/] When a member has overdue financial obligations outstanding for more than three months, the amount of such arrears will be shown in this section.

Implementation of HIPC Initiative: Not Applicable

Implementation of MDRI Assistance: Not Applicable

Implementation of Catastrophe Containment and Relief (CCR): Not Applicable

Exchange Arrangement

St. Kitts and Nevis participates with seven other members in the Eastern Caribbean Currency Union (ECCU) and has no separate legal tender. Monetary policy and the exchange system is managed by a common central bank, the Eastern Caribbean Central Bank (ECCB), which operates like a quasi-currency board, maintaining foreign exchange backing of its currency and demand liabilities of close to 100 percent. The common currency, the Eastern Caribbean dollar, has been pegged to the U.S. dollar at the rate of EC$2.70 per U.S. dollar since July 1976. St. Kitts and Nevis accepted the obligations of Article VIII, Sections 2, 3, and 4 in December 1984, and maintains an exchange system free of restrictions on the making of payments and transfers for current international transactions and multiple currency practices.

Safeguards Assessment

Under the Fund's safeguards assessment policy, the Eastern Caribbean Central Bank (ECCB) is subject to a full safeguards assessment on a four year cycle. A 2021 update assessment has been substantially completed. The ECCB continues to maintain sound external audit and financial reporting practices, and the internal audit function has aligned its practices with international standards. The pilot project to introduce a digital currency is advancing and related new risks will need to be carefully managed. The ratification of draft amendments to the ECCB Agreement to include digital currencies should be prioritized by the participating governments that have not yet completed the process. In addition, the assessment recommended strengthening the operational autonomy of the ECCB, consistent with observations in the ECCU Staff Report for the 2019 Discussion on Common Policies of Member Countries. Necessary legal reforms to the ECCB Agreement Act center around governance arrangements for stronger delineation of the division of responsibilities on oversight and policy formulation among the decision-making bodies (Monetary Council, ECCB Board, and the Governor and Deputy Governor).

Last Article IV Consultation

The last Article IV consultation took place on September 14, 2018. The next Article IV consultation is expected to take place on the standard 12-month cycle. .

FSSA Participation, ROSCs, and OFC Assessment

St. Kitts and Nevis participated in the regional ECCU FSSA conducted in September 2014. The Financial System Stability Assessment is available at:
https://www.imf.org/en/Publications/CR/Issues/2016/12/31/Eastern-Caribbean-Currency-Union-Financial-System-Stability-Assessment-including-Report-on-17718

A review of St. Kitts and Nevis AML/CFT Assessment is currently ongoing by a team of assessors representing the Caribbean Financial Action Task Force (CFATF) with full completion by end 2021.

Technical Assistance: (2010–Present)

Since 2010, St. Kitts and Nevis has benefited from technical assistance (TA) in the areas of tax policy, tax administration, economic statistics, financial supervision, and macroeconomic management, both from IMF headquarters and the Caribbean Regional Technical Assistance Centre (CARTAC).

Real Sector

- CARTAC and the IMF's Statistics Department (STA) have provided TA to the National Statistics Office on rebasing the national accounts the consumer price index (CPI). CARTAC is assisting in developing quarterly GDP estimates, including compiling separate production-based measures of GDP for St. Kitts and Nevis and consumption GDP estimates. The milestone of developing the quarterly GDP methodology has been achieved; and good progress is being made in developing the compilation worksheets with around 80 percent completion. Experimental quarterly GDP estimates have been constructed but not been published yet. In addition, assistance is being provided to improve the CPI, and develop data collections and index methodologies for a producer price index and export-import price indices.

External Sector

- CARTAC assisted the St. Kitts and Nevis Department of Statistics and the ECCB in strengthening the compilation and dissemination of external sector statistics using the BPM6 methodology. In May 2021, the ECCB published comprehensive BOP and IIP tables for 2014-21. CARTAC TA helped develop and administer the business and visitor expenditure surveys, and trained data compilers and survey respondents. To address data gaps, CARTAC continues providing assistance in strengthening the business and visitor expenditure surveys; improving the coverage of source data used for the compilation of trade in goods; and further developing other data sources used to compile relevant components of the external sector statistics.

Fiscal Sector

- CARTAC has provided significant TA in tax administration, to both the Inland Revenue Department (IRD) and the Customs and Excise Department (CED). It has particularly helped IRD strengthening its auditing function, including through training of a group of risk compliance officers, as well as through the implementation of a new IT system. CARTAC's TA is now moving to strengthen the compliance risk program. The authorities highlight the importance of CARTAC assistance towards the implementation of the Automated System for Customs Data (ASYCUDA), which they indicate has significantly facilitated their operations and allow them to shift staff towards strengthening risk-based auditing.

- The Fiscal Affairs Department (FAD) has provided training in revenue administration and governance (with the goal to strengthen revenue administration, management, and governance arrangements); and tax administration core functions (which aimed at strengthening core tax administration functions).

- Under the Fiscal Management in the Caribbean Project (FMCP) the IMF is providing technical assistance in broad areas of Public Financial Management (PFM), including asset and liability management, as well as budget and execution control.

Monetary and Financial Sectors

- CARTAC, the IMF's Monetary and Capital Markets Department (MCM), and the IMF's Legal Department (LEG) advised the authorities on strengthening financial sector regulation and supervision, including risk-based supervision. With assistance from the Office of the Superintendent of Financial Institutions in Canada (OSFI), CARTAC provided technical assistance to the Eastern Caribbean Central Bank (ECCB) on drafting the OECS Insurance Act, and also, in conjunction with LEG, provided technical assistance to the ECCB in finalizing the drafting of the OECS Money Services Business Act. CARTAC also assisted in the development of the Single Regulatory Unit and provided training to the Financial Services Regulatory Commission (FSRC) on implementing Risk-Based Supervision, including for nonbank financial institutions in the Federation and the offshore banking sector in Nevis. Since 2014, CARTAC has been assisting the regulatory bodies in St. Kitts with the development of guidelines for supervisory interventions, the implementation of Basel II and risk-based supervisory frameworks. On the Financial Stability front, CARTAC also provided TA in the area of stress-testing and dynamic modelling of the banking system in conjunction with the ECCB and conducted several capacity building workshops on the development of financial soundness indicators, and on risk-weighted capital adequacy.

RELATIONS WITH OTHER INTERNATIONAL FINANCIAL INSTITUTIONS

- World Bank: http://projects.worldbank.org/search?lang=en&searchTerm=&countrycode_exact=KN
- Caribbean Development Bank: https://www.caribank.org/countries-and-members/borrowing-members/saint-kitts-and-nevis

STATISTICAL ISSUES

I. Assessment of Data Adequacy for Surveillance
General: Data provision has some shortcomings but is **broadly adequate** for surveillance.
National Accounts: Methodological deficiencies are present in the real sector statistics. GDP figures rely on the production approach, both in constant and current prices. Limited survey data hinder the assessments of value-added for each sector with some sectors suffering from significant weaknesses in estimation methodology. GDP figures are derived from the production approach in constant and current prices. In addition, annual current price expenditure-based GDP estimates are compiled and disseminated. One deficiency with the expenditure-based methodology is that Household Final Consumption Expenditures are derived residually. Weaknesses are observed in the methods to estimate gross capital formation. There are significant delays in completing data collection and processing of all the annual national accounts data. Staffing constraints in the compiling agency may compromise the development of new statistics, the quality improvement of the existing ones, and the intended improvements of timeliness. Quarterly GDP estimates are not published. Monthly data on tourism is disseminated by the ECCB with a lag.
Price Statistics: Monthly CPI data are posted on the ECCB website. The ECCB disseminates monthly data on tourism with a lag but estimates on tourism expenditure have been made. Except for data from the social security board and occasional labor force surveys, limited data are available on labor market developments.
Government Finance Statistics: Coverage of fiscal data is limited to the budgetary central government and the Nevis Island Administration, with limited below-the-line data. This omits revenues and expenditures of other general government units, notably the St. Christopher and Nevis Social Security Board. Fiscal data also have some methodological shortcomings with misclassification of some revenue and expenditure items. The authorities do not report any fiscal data to STA. However, some preliminary work has been undertaken by STA and the authorities to derive annual government finance statistics (GFS) in line with the GFSM 2014 on main aggregates and their components for revenue. expense, and financing of the budgetary central government.
Monetary and Financial Statistics: Monthly monetary statistics are compiled and reported to the Fund by the ECCB, based on standardized report forms (SRF) for the central bank (SRF 1SR) and for other depository corporations (SRF 2SR) since July 2006. The ECCB implemented the reporting system for commercial banks that is envisaged to address the recommendations made by the April 2007 data ROSC mission. The ECCB reports data on some key series and indicators of the Financial Access Survey, including the two indicators (commercial bank branches per 100,000 adults and ATMs per 100,000 adults) adopted by the United Nations to monitor Target 8.10 of the Sustainable Development Goals for its member countries, including St. Kitts and Nevis.

Financial Sector Surveillance: The ECCB compiles financial soundness indicators (FSIs) for its member countries, including St. Kitts and Nevis. However, due to confidentiality reason, dissemination of FSIs for the ECCB member countries has so far not been approved.
External sector statistics: Balance of payments and IIP data are jointly compiled and disseminated by the Department of Statistics of the country and the ECCB on an annual basis following the *BPM6* methodology. Further work is required to improve the coverage of the data, particularly, direct investment transactions due to low business survey response rates. Travel credit services are based on the results of the 2016 visitor expenditure survey (tourism expenditure) and business survey data reported by offshore universities (student expenditure). Plans for the implementation of a new visitor surveys have been postponed due to limited resources and the COVID-19 pandemic.
II. Data Standards and Quality
St. Kitts and Nevis participates in the Enhanced General Data Dissemination System (e-GDDS). Monetary Statistics Component of the Regional Data Module Report on Observance of Standards and Codes (ROSC) for the ECCB was published in 2007. Data ROSC was published in August 2007.

ST. Kitts and Nevis – Table 1. Common Indicators Required for Surveillance
(As of June 2021)

	Date of latest observation	Date received	Frequency of data[7]	Frequency of reporting[7]	Frequency of publication[7]
Exchange Rates	Fixed Rate	NA	NA	NA	NA
International Reserve Assets and Reserve Liabilities of the Monetary Authorities[1]	3/21	6/4/2021	M	M	M
Reserve/Base Money	3/21	6/4/2021	M	M	M
Broad Money	3/21	6/4/2021	M	M	M
Central Bank Balance Sheet	3/21	6/4/2021	M	M	M
Consolidated Balance Sheet of the Banking System	3/21	6/4/2021	M	M	M
Interest Rates[2]	3/21	6/4/2021	M	M	M
Consumer Price Index	3/21	6/4/2021	M	M	M
Revenue, Expenditure, Balance and Composition of Financing[3]—General Government[4]	4/21	6/1/2021	M	M	A
Revenue, Expenditure, Balance and Composition of Financing[3]—Central Government[4]	4/21	6/1/2021	M	M	A
Stocks of Central Government and Central Government-Guaranteed Debt[5]	4/21	6/1/2021	M	M	A
External Current Account Balance	2020	4/6/2021	A	A	A
Exports and Imports of Goods and Services	2020	4/6/2021	A	A	A
GDP/GNP	2020	6/1/2021	A	A	A
Gross External Debt	2020	4/06/2021	A	A	A
International Investment Position[6]	2020	4/6/2021	A	A	A

[1] Includes reserve assets pledged or otherwise encumbered as well as net derivative positions.
[2] Both market-based and officially determined, including discount rates, money market rates, rates on treasury bills, notes and bonds.
[3] Foreign, domestic bank, and domestic nonbank financing.
[4] Data available for central government only.
[5] Including currency and maturity composition.
[6] Includes external gross financial asset and liability positions vis-à-vis nonresidents.
[7] Daily (D), Weekly (W), Monthly (M), Quarterly (Q), Annually (A); Irregular (I); Not Available (NA).

disruptions on domestic activity. In response, the government introduced tax waivers, deferrals and incentives, and the Social Security Board provided unemployment benefits to affected insured workers. In parallel, the regional and national financial supervisors swiftly introduced temporary response measures, including loan moratoria, that supported liquidity and effectively mitigated the pandemic's financial system impact. Nonetheless, the pandemic resulted in an estimated annual decline in GDP of 12½ percent, and the general government's[1] first fiscal deficit (4.7 percent of GDP) since 2010, financed by drawing down on its sizeable deposit buffer

Containing the pandemic and supporting the economy remain the key near-term policy priorities. The government has made rapid progress toward its end-October vaccination target of 70 percent of the population (about a quarter of the target population is fully vaccinated and 65 percent have received the first dose). As the recently instated partial lockdown in response to budding community spread confirms, herd immunity has not yet been reached, and should remain the number one priority to save lives and livelihoods. Fiscal relief measures should be kept in place until the recovery firmly takes root. Maintaining robust levels of public investment would further support activity.

An expected rebound in tourism sets the stage for a strong recovery from 2022 onward, but risks to the outlook remain significant. We project a small further decline in GDP of 1 percent in 2021, followed by 10 percent growth in 2022. The pre-pandemic GDP level is expected to be reached in 2024. However, the recovery path could be derailed should the pandemic impose sustained disruptions on the anticipated pace of tourism inflows and domestic activity. Other risks include financial sector uncertainties, natural disasters, and lower-than-expected CBI receipts.

Once the recovery is firmly established, the government should resume its policy of saving part of the CBI revenues to build fiscal buffers. As a small, natural disaster-susceptible country dependent on tourism and historically volatile CBI revenues, St. Kitts and Nevis needs significant buffers. Higher buffers would also provide more fiscal space to mitigate contingent and long-term fiscal pressures, including possible further reacquisitions of lands swapped as part of the 2012-14 sovereign debt restructuring, and a possible future need to buttress the national pension system that under current projections will start to run deficits and begin depleting its reserves if corrective measures are not taken in due course.

Staff simulations suggest that maintaining an overall budget surplus of at least 2 percent of GDP would support a robust pace of buffer build-up. Assuming annual CBI revenues of 9 percent of GDP, the savings would allow reducing public debt to around 40 percent of GDP and rebuilding deposits to close to a quarter of GDP by the end of the decade, which would provide a significant buffer against both macro-economic and natural disaster shocks. The room for government investment would be modest, at around 3 percent of GDP annually, but could be expanded by policy measures such as reducing the government wage bill, reforming tax incentives and strenghtening public investment efficiency. Higher-than-assumed CBI revenues could also create more room for investment, albeit part of the

[1] The general government refers to the consolidated public finances of St Kitts and Nevis.

additional revenues should be saved (including as additonal buffer against contingent fiscal pressures). Lower CBI revenues would increase the necessity of policy adjustment and possibly additional borrowing, which would lead to a slower reduction of government debt.

Financial sector policies should increasingly focus on building readiness for the exit from temporary support measures. The financial system remains stable and benefits from sizeable buffers, but the pandemic's full asset quality impact will become apparent only upon the expiry of the loan moratoria. National authorities should therefore review and formalize operationalizable crisis management plans in close coordination with the ECCB. Long-standing high non-performing loans and elevated investment portfolio risks in the systemically significant bank should be more decisively addressed. In addition, a more robust divestment plan for the remaining lands from the sovereign debt swap should be pursued, based on updated valuations for the unsold lands, a revised cost-sharing agreement between the bank and the government on any shortfalls from original valuations, and a more active strategy to attract potential investors, including closer coordination with the CBI program. Further supervisory guidance, including on loan moratoria expiry and loan loss provisioning, can support timely balance sheet repair of the non-bank sector. Legislative reforms to streamline foreclosure processes would facilitate asset recovery efforts. Continued efforts to strengthen compliance with international AML/CFT standards and transparency and oversight of the CBI program can help mitigate risks to correspondent banking relationships.

There is room to strengthen productivity growth, economic competitiveness, and human capital. GDP per capita growth in the last two decades has been relatively weak and convergence with the U.S. has stopped. Growth has been held back by weak productivity growth as investment has been high, which may partly reflect the limits of a small-island economy. However, several reforms might help boost productivity growth and export competitiveness, including using the CBI program to attract investment beyond the tourism sector, upgrading skills through focused training programs, better aligning the education system with the needs of the labor market, and making it easier for small firms to access credit, including through reforms that facilitate use of non-fixed asset as loan collateral.

We would like to thank the authorities of St Kitts and Nevis for the very friendly and fruitful discussions.