REPORT TO CONGRESS ON
THE INTERNATIONAL MONETARY FUND'S
LOAN TO JAMAICA AND BARBADOS

A Report to Congress

consistent with

Section 1501 of the
Dodd-Frank Wall Street Reform and Consumer Protection Act, 2010

United States Department of the Treasury

July 2, 2019

Introduction

This report provides an assessment of the likelihood that the International Monetary Fund (IMF) loans to Jamaica (approved in 2016 but has not disbursed as the program is precautionary) and Barbados, made in 2018, will be repaid in full. This report is required by section 1501 of the *Dodd-Frank Wall Street Reform and Consumer Protection Act, 2010*.[1] Both countries had debt-to-GDP ratios greater than 100% at the time of the loan and are not eligible for assistance from the International Development Association.

JAMAICA

At the time of the initial program approval in May 2013, Jamaica's public debt was 145% of its GDP, a number which IMF staff estimates will fall to 99.6%[2] of GDP in FY 2018/19[3]. Its performance under successive IMF programs has been remarkably strong.

As directed by section 1501, and consistent with its longstanding practice with respect to all loans, the Office of the United States Executive Director (OUSED) at the IMF, in close coordination with the Treasury Department, conducted a careful and thorough evaluation of the proposed program for Jamaica when it was submitted to the IMF Executive Board. The OUSED and Treasury continue to monitor the progress under the program.

Overview

On November 11, 2016, the IMF Executive Board approved a three-year Stand-By Arrangement (SBA) in the amount of SDR 1.195 billion (about $1.6 billion at the time of approval) for Jamaica. The Jamaican authorities continue to view the SBA as precautionary; they have not drawn, and do not intend to draw, financing from the IMF unless external shocks—e.g., a sharp increase in oil prices, global market volatility, or natural disasters—generate an actual balance of payments need. This SBA replaced the country's Extended Fund Facility (EFF), approved in May 2013 for the amount of SDR 615.38 million (about $932 million at the time of approval).

The main pillars of the SBA include: (i) reorienting fiscal policy to better support growth and reduce poverty; (ii) reducing public debt to 60% of GDP by FY 2025/26 (the year ending March 2026) by maintaining a primary surplus of 7% of GDP for the duration of the program; (iii) building the foundation for monetary policy to move to inflation targeting; and (iv) augmenting financial sector resilience and inclusion.

Jamaica has by now established an exemplary multi-year track record of program ownership and implementation, under both of Jamaica's leading political parties. Looking back to Jamaica's previous EFF, the authorities successfully completed 13 program reviews, including maintaining

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[1] P.L. 111-203; codified at 22 U.S.C. 286tt(b), section 68(b) of the Bretton Woods Agreements Act: "Within 30 days after the Board of Executive Directors of the Fund approves a proposal [to make a loan to a country whose public debt exceeds gross domestic product and is not eligible for assistance from the International Development Association], and annually thereafter by June 30, for the duration of any program approved under such proposals, the Secretary of the Treasury shall report in writing . . . assessing the likelihood that loans made pursuant to such proposals will be repaid in full. . . ."

[2] FY2018/19 figures are still estimates due to the time lag in preparation of official statistics by Jamaican authorities.

[3] Jamaican fiscal year runs from April 1 to March 31.

a primary fiscal surplus of at least 7% of GDP over the lifetime of the EFF so as to markedly improve debt sustainability and be in a position to reduce debt-to-GDP down to 60% by FY 2025/26. Jamaica also made important progress under the EFF to restore macroeconomic stability: the exchange rate substantially adjusted toward its equilibrium level under a more flexible regime, inflation fell, and the central bank began to rebuild foreign exchange reserve buffers.

Under the current SBA, Jamaica has continued this positive trajectory. On March 28, 2019, Jamaica successfully concluded its fifth review on schedule. Treasury shares the IMF staff view that program implementation remains robust five years into economic reforms. Jamaica met all quantitative criteria for end-December 2018; the authorities have also passed amendments to the Bank of Jamaica's (BOJ) governance framework to improve governance and independence as part of the program's structural reforms. Importantly, program performance remained strong even following a change in government in early 2016, signaling a strong political consensus for reforms embodied in the IMF SBA. Fiscal consolidation has underpinned an increasingly stable macroeconomic picture. The latest IMF program review estimated that the public debt-to-GDP ratio fell to 99.6% in March 2019 from a peak of 145% in May 2013. Markets rewarded Jamaica for its strong policy track-record by upgrading the country's credit rating and lowering sovereign bond yields to historic lows. The IMF scheduled the sixth and final review for the fall of 2019.

Debt Status

Jamaica has reduced its public debt-to-GDP ratio by almost 45 percentage points since the start of its prior EFF in 2013, faster than the IMF originally anticipated, as the authorities supplemented aggressive fiscal consolidation with successful debt management operations. The IMF estimates debt-to-GDP to be 99.6% as of the end-March 2019, a reduction of 14% from the November program approval. As Jamaica proceeds with implementation of structural reforms, improvements in public revenue and stronger GDP growth should help further reduce the debt burden. Jamaica's Fiscal Responsibility Law, which places a floor on the overall fiscal balance, serves as a concrete policy measure to achieve the debt-to GDP ratio of 60%[4] by 2026.

Debt Management Strategy

The government's primary objective is to keep Jamaica's public debt on a downward trajectory to make space for essential public services and maintain access to debt markets. In order to meet this objective, the government remains committed to running primary surpluses that allow for a reduction in the level of outstanding debt-to-GDP. Jamaica adjusted the primary surplus downward from 7% to 6.5%, but this lowering of the primary surplus target will not materially impact Jamaica's ability to meet the 60% debt-to-GDP target by FY 2025/26. The government has also implemented a number of structural reforms, including enhancements to the central bank's governance framework to improve central bank governance and independence. The government has pledged to reduce the public sector wage bill by rethinking the compensation structure and composition of the workforce over a 4-year wage settlement period, via an agreement negotiated with public sector unions. Planned investments in farming infrastructure such as rural roads and irrigation should boost Jamaica's key agriculture sector while building

[4] This figure is calculated according to the debt methodology of Jamaica's Fiscal Responsibility Law, which differs from the IMF program's methodology primarily by excluding debt to the IMF held by the BOJ.

resilience against frequent tropical storms. The IMF projects that public debt-to-GDP will continue to decline after the program expires in late 2019.

Vulnerabilities

Growth and job creation dividends from the reforms have been slow to materialize, posing risks to Jamaica's strategy to further reduce debt and free up fiscal space for productive investments. Persistent below-potential real GDP growth rates, averaging only 0.9% since reforms began in 2013, could lead to decreased public support (although official commitment to the program has remained strong to date). Further, if the authorities are unable to effectively address high crime rates, expand private sector access to finance, and raise necessary infrastructure investment, these factors could impede private sector activity, keeping growth rates sluggish. Notwithstanding sluggish growth, success by the central bank in taming inflation, together with historically low unemployment, appear to have bolstered political support to continue on the reform path.

At the macro level, external shocks such as a sharp rise in risk premia due to volatility in international markets and an economic slowdown in key trading partners are downside risks to growth. Another vulnerability is volatility in international oil prices, as higher oil prices would tend to increase the current account deficit and create depreciation pressures on the currency. Finally, Jamaica remains highly exposed to the risk of significant weather-related natural disasters.

Public debt in foreign currency now accounts for about 61% of total public debt. However, the government's successful reopening of domestic debt markets in February 2016 and strong demand for domestic currency government securities in 2018 should help rebalance the composition of external versus domestic debt and ameliorate foreign currency risk over time. Domestic debt market development requires a series of well-sequenced reforms over the short and medium term that will reduce key inefficiencies in the market.

Overall Assessment

Jamaica remains heavily indebted and vulnerable. However, the EFF was highly successful in helping to address these issues, and the current precautionary SBA is providing a solid framework for the country to continue on a sustainable debt path and mitigate its vulnerabilities. The Jamaican authorities continue to demonstrate their extraordinary commitment to meeting IMF program objectives, and they are on track to maintain a strong level of performance and country ownership. Based on these factors and the IMF's preferred creditor status, the Treasury Department assesses that the IMF's loan to Jamaica is likely to be repaid in full.

BARBADOS

Barbados has struggled to break free from a vicious cycle of low or negative growth since the 2008-09 financial crisis. Public debt reached 126% of GDP (as of end-2018) after peaking in FY

2017/18[5] at around 160%. Barbados has embarked on a comprehensive Economic Recovery and Transformation (BERT) plan aimed at restoring fiscal and debt sustainability.

As directed by section 1501, and consistent with its longstanding practice with respect to all loans, the Office of the United States Executive Director (OUSED) at the IMF, in close coordination with the Treasury Department, conducted a careful and thorough evaluation of the proposed program for Barbados when it was submitted to the IMF Executive Board. The OUSED and Treasury continue to monitor the progress under the program.

Overview

On October 1, 2018, the IMF Executive Board approved a four-year Extended Fund Facility (EFF) in the amount of SDR 208 million (about $290 million at the time of approval) for Barbados. Barbados' international reserves rebounded sharply to $531 million as of end of March 2019 from $220 million at the beginning of the program. An additional $175 million in policy based loans from multilateral development banks and suspension of debt service on external commercial debt has aided the accumulation of foreign currency reserves.

The main pillars of the EFF include: (i) fiscal adjustment that adopts a primary surplus of 6% of GDP in the medium term; (ii) State Owned Enterprise (SOE) reforms to reduce transfers that have become a significant burden on the budget; (iii) external debt restructuring with foreign commercial creditors; (iv) maintaining the stability of the financial system following the impact of domestic debt restructuring; (v) growth-oriented reforms aimed at supporting both the traditional and non-traditional private sector.

Under the current EFF, the country authorities have shown strong ownership of the reform effort and program implementation. The rapid completion of a domestic debt restructuring has been helpful in reducing economic uncertainty and resulted in an immediate reduction in the debt-to-GDP ratio of about 30 percentage points in nominal terms. Barbados met all performance criteria for end-March, and has made progress on structural reforms, with six structural benchmarks implemented either on time or with minor delays. The government intends to increase its 3.5% primary surplus in FY 2018/19 to 6% in FY 2019/20.

This program involves significant risks due to the extensive nature of the structural reforms and adjustments needed with limited implementation capacity. However, Barbados has shown strong ownership of the reform effort by demonstrating important policy measures undertaken since the start of the program. With strong implementation of the program, we expect Barbados to repay the IMF in full. The IMF scheduled the second review for the fall of 2019.

Debt Status

At the time of program approval, Barbados' public debt reached an unsustainable 157% of GDP. Barbados completed a comprehensive domestic debt restructuring in October 2018 that significantly reduced its debt to commercial banks, insurers, central bank, and national insurance scheme. Public domestic debt has decreased by 36% of GDP from 129% in April 2018 to 93% of GDP in March of 2019. During the same time frame, external debt increased by 6% from

[5] Barbadian fiscal year runs from April 1 to March 31

28% to 34% of GDP due to a $100 million loan from the InterAmerican Development Bank and an additional $75 million loan from the Caribbean Development Bank used to increase foreign reserves. These loans and a moratorium on payments to external commercial creditors were crucial in replenishing foreign reserves.

The overarching objective and long-term anchor of the IMF program is to reduce public debt to a sustainable level of GDP by March 2024 (the IMF program suggests that an anchor of 60% debt/GDP by 2024 should guide macroeconomic policies, which is consistent with the debt/GDP target used by Jamaica, and the IMF's advice given to other small islands in the Caribbean). Implementation of structural reforms, improvements in public revenues, and the eventual recovery in GDP growth should help Barbados meet this target.

Debt Management Strategy

The external commercial debt moratorium is still ongoing. The moratorium on payments in May 2018 to stabilize foreign reserves has led to arrears to foreign commercial creditors. Negotiations are proceeding with the external commercial creditors to restructure outstanding debt to sustainable levels. Barbados has taken steps towards reaching agreement with external creditors by maintaining transparency through the negotiation process, although the parties have not yet concluded negotiations. Barbados has also agreed to repay small loans from external sovereign creditors (China and Canada).

The government's primary objective is to implement a reform program that supports higher private-sector led investment and growth and restores confidence in the economy. Growth oriented policies and fiscal discipline will allow the government to achieve a debt-to-GDP ratio of 80% by FY 2027/28 and 60% by FY 2033/34. In order to reach this objective, the government has undertaken a comprehensive restructuring of its domestic debt and committed to reach a 6% primary fiscal surplus over the medium term.

Implementation of SOE reforms will be critical to achieving a more sustainable fiscal position. Under the Financial Management and Audit law passed in January 2019, the government must approve all SOE borrowing and SOEs submit standardized quarterly reports on SOE performance. This reform will provide oversight of government debts and reduce transfers.

The Corporate Income Tax (CIT) reform to unify the treatment of domestic and international companies to comply with EU and OECD guidelines should foster a business-friendly environment in Barbados, further stimulating the economy and decreasing the debt-to-GDP ratio. The IMF projects a 5-7% decline per year in gross public sector debt from 2019-2024 debt reduction and GDP growth strategies.

Vulnerabilities

Key risks to the debt reduction strategy include limited implementation capacity of the government, untested ability to maintain fiscal discipline/high surpluses over a sustained period of time, and risks related to the external debt restructuring. Reforms to SOE reform will also include increases in tariffs and fees charged by SOEs (e.g. bus fares, water rates, and travel development fee) which may foster public discontent and lead to weakened political willpower to persevere with necessary reforms.

At the macro level, external shocks such as a sharp rise in risk premia due to volatility in international markets, and economic slowdown in trade partners are vulnerabilities to growth. A key vulnerability is a disorderly Brexit or a U.S. slowdown, both of which would reduce the number of tourists visiting from key source markets (U.K. tourists are 33% of tourist market share and U.S. tourists are 30%). The authorities have initiatives to diversify the economy into new areas over time such as renewable energy, high-tech, and software development to complement the traditional services sector, but these nascent industries will take time to develop. Finally, Barbados remains highly exposed to the risk of significant weather-related natural disasters.

Overall Assessment

Barbados remains heavily indebted and vulnerable. However, its comprehensive domestic debt restructuring was highly successful in reducing the overall debt burden and putting the country on a path towards sustainability. The EFF also provides a strong framework to help enable significant fiscal consolidation and an increase in foreign reserves. The Barbadian authorities continue to demonstrate their commitment to meeting IMF program objectives, including through strong public communications to maintain public support for the reform effort. Based on these factors and the IMF's preferred creditor status, the Treasury Department assesses that the IMF's loan to Barbados is likely to be repaid in full.