# Sir K Dwight Venner: Issues of concern to the Eastern Caribbean Central Bank and the Caribbean region as a whole

Feature address by Sir K Dwight Venner, Governor of the Eastern Caribbean Central Bank, at the opening of the new building of ABI Bank Ltd, Antigua, 5 March 2005.

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*Mr Chairman*

I would like to express my appreciation to the Directors, Management and Staff of ABI Bank Ltd for inviting me to be the Feature Speaker at the Opening of your new building.

A few years ago, I performed a similar function for the ACB and you would appreciate that the ABI Bank could do no less than invite me to bless their own undertaking, and I could do no less than accept. In addition, the charm and persuasiveness of my dear friend, McAllister Abbott put the matter beyond any doubt.

The ABI Bank Ltd has shown itself to be a very innovative institution. In addition, they respond to the regulatory concerns of the Central Bank fully realizing that in the business of finance, innovation must be balanced by prudence, and risks of any undertaking must be properly taken into consideration.

I consider this to be a very timely opportunity given the times we live in, to comment on some of the issues which are of concern to the ECCB and the region as a whole. It is also an opportunity to share with you some of my views on how we are approaching these challenges as the Central Monetary Authority of the OECS.

I would go as far as to say that this is a defining time for the region, as we seek to grapple with both external and domestic challenges of a very complex nature. There is also a great desire among our people for information and knowledge on the events that affect our lives at this time, and into the near and distant future.

The possession of information particularly when it is accurate and credible gives those who have it considerable advantage over those who do not. In the economic and financial spheres, information is so critical to the conduct of business that the provision of certain types, for example, accounts, are legally required and have to be publicly certified.

The use of information under certain circumstances, such as insider trading is legally prohibited and punishable by fines and imprisonment. Companies have to present statements of their performance to Annual General Meetings of their shareholders. Governments have to present their Estimates of Revenue and Expenditure to the Legislature, the elected representatives of the people or shareholders in the country, and the Budget is a public document. Individuals have to present their income and financial statements to the tax authorities so that they can be fairly assessed and make a contribution, so that in exchange the government can provide the services of law and order, sanitation, education, etc which add to the quality of life. All countries as members of the international community, and, in particular, the IMF have to transmit to that organization for official publication in a document entitled *"International Financial Statistics"* their National Accounts, Balance of Payments, Fiscal, Monetary and Price Statistics. These figures obviously are of critical importance to the country itself in two ways. Firstly, *how can good policies be made if there are no timely and accurate statistics, and how can the progress of the country be accurately assessed if there are no reliable statistics to make the judgment?*

Secondly, *if both foreign and domestic investors have no access to accurate data, how can they make serious decisions on potential investment opportunities?*

In both developing and emerging market economies, TV and radio stations, newspapers and business magazines keep the public well informed on commercial, financial and economic affairs. In this churning up of information, analysis and commentary, individuals and business firms are presented with increased choices for both saving and investment. In this environment, businesses rise and fall based on the performance of markets, and their ability to manage their resources. While speculation abounds this is mostly based on the review and analysis, no matter how cursory, of what is taken to be accurate and credible statistics produced and published at set periods by official or publicly acknowledged institutions.

Information is such a critical part of this era that not only do we speak of the Information Age but three distinguished Economists have received the Nobel Prize for their work in this subject area. It is against this background that we can outline the external and domestic environment in which we exist, define the domain or theatre of action in which we operate, point out the goals and objectives we have set for ourselves and/or have been set for us, and review the policy tools we have at our disposal to meet these objectives.

In the case of the external environment, we live in what has now been accepted as an increasingly globalised world. Barriers to trade and finance are being removed across the international community, and the spread of technology both in basic sciences and materials, as well as information and communication technologies have literally created a **global village.**

This trend has inevitably presented challenges to all countries in different ways. Free trade regimes have had an impact on our traditional agricultural export commodities, such as bananas and sugar whose preferences are being gradually removed. In the financial arena, the proliferation of standards and codes, and the efforts of the OECD have had a negative impact on our embryonic Offshore Finance Sector. They have also posed a challenge to our indigenous domestic banks by making it somewhat difficult with their correspondent relationships.

Fluctuating output of the world economy, and particularly in the countries we trade with, mainly the USA, Canada, the UK and Europe has a direct impact on our economic performance. The same is true in the case of the fluctuations in major currencies. We are linked to the US dollar so that fluctuations between that currency, the Euro, Sterling and the Canadian dollar have implications for us in the Currency Union.

A major factor which impacts on the performance of our economies is the price of oil which in recent times has been at unprecedentedly high levels. It is our major import, and the price passes through to almost every item of consumption or production.

Finally, the geopolitics of the international system, particularly the fight against terrorism has to be carefully examined, as it could potentially impact on our major foreign exchange earner, tourism.

Domestically we have to treat with the fundamental issue of small size, both in terms of land mass and population. The question we have to pose for ourselves is, *given the resources we have, what standard of living is possible and sustainable over long periods of time?*

The imbalance between expectations and resources in most countries shows up in the Balance of Payments on the external account and in the budget domestically. Not many, if any country, could like the US get away with running these twin deficits over any period of time, as they are almost self correcting as creditors both external and domestic will withdraw their support at some stage. In fact, in the US, Chairman of the Federal Reserve, Alan Greenspan has expressed his concern about the current situation. Antigua and Barbuda, as well as other countries in the Currency Union face this situation, and I can only urge that it be vigourously addressed.

The OECS countries have understood more than the rest of the regional community the need for regional integration. While the bigger countries like Jamaica and Trinidad and Tobago have felt that they had other options, the smaller islands have understood that it meant their very survival.

This is a defining moment in the sense that we are about to embark on a new venture, the Caribbean Single Market and Economy, CSME and for it to succeed the OECS as a bloc must step up to the plate, define its interests and assert its leadership. We must, therefore, define to our satisfaction and acceptance a unique and coherent space called the OECS, which at least in an economic sense is continuous and coterminous.

We have two concepts to engage our minds in this regard, first the OECS as an Economic Union, and the Eastern Caribbean Currency Union as a Single Financial Space. The only difference between the two is the absence of the BVI from the Currency Union as it uses the US dollar as its legal tender.

The OECS is a highly integrated area as the Treaty of Basseterre, 1981 establishing the Organisation indicates. In Article 3 (2), it sets out a number of arrangements which if all implemented would result in the formation of a new state. The founders accepted that as very small states there were three overriding advantages to the arrangement –

- To take advantage of the economies of scale and scope through sharing vital services;
- To mitigate risks by spreading them over several countries;

- Enhancing their capacity to negotiate with third countries or groups of countries.

The result is that the OECS is at a much higher level of integration than CARICOM with a common court, a common currency, central bank and stock exchange, a directorate of civil aviation, a joint pharmaceutical procurement system, joint diplomatic representation, and common projects in education and health, as well as joint regulation of telecommunications.

We now need to focus on these achievements and use them as a platform for taking advantage of the CSME and other arrangements like the FTAA. We also need to see how each individual island can contribute to the whole instead of assuming that we will be worst off, or that one will gain at someone else's expense. We need a different mindset in which addition and multiplication is seen as superior to subtraction and division.

Having established the concept of a domain we must then identify the objectives of this entity. This will require the convergence of both regional and national goals. At the regional level there is the OECS Economic Development Strategy, the OECS Development Charter, and the objectives set at a Special Meeting of Heads in November 2002. Those were:

- A sustainable growth rate of 6%;
- An unemployment rate of less than 6%;
- A poverty rate of less than 6%;
- Maintaining and achieving the Human Development Indices goals consistent with the Millennium Development Goals; and
- The transformation of our economies into internationally competitive entities.

At the national level, these objectives can be gleaned from manifestos, development plans, medium term economic strategy papers, public sector investment programs and budgets.

The policies which are available to achieve these objectives are -

- Monetary
- Fiscal
- Trade
- International Economic Relations
- Incomes
- Structural
- Social
- Environmental

Let me on this occasion confine myself to monetary and financial policies, given the occasion for which we are gathered.

The ECCB in assessing the situation both domestically and internationally has identified consistent with the objectives set by the OECS Heads two major objectives which are also consistent with the purposes of the Bank as set out in Article 4 of the ECCB. These are **Stability and Development.**

Under **Stability** the Bank has two goals, namely – Monetary Stability and Financial Stability.

Monetary Stability is tied to the performance of the exchange rate. We have chosen a fixed exchange rate regime, and have managed to successfully maintain this at 2.7 EC to the US dollar since July 1976. This has required us to maintain a very high level of foreign exchange reserves, presently 96% to the currency in circulation. This is above the legal limit of 60% and is approximately equivalent to four months imports where the benchmark is three months.

In order for this parity to be maintained, we focus our attention on the performance of the Balance of Payments, the fiscal and debt ratios of the countries, and the competitiveness of the currency as assessed by the Real Effective Exchange Rate. The Monetary Council has therefore set a number of benchmarks in the fiscal and debt areas which member governments have been requested to adhere to.

Financial Stability is related to the safety and soundness of the banking system and the effective regulation of non-bank financial intermediaries. This requires the appropriate legislative and legal framework and the capacity to effectively regulate the financial system.

Let me put these two stability conditions in a way that the ordinary layman would understand. If the currency is devalued, the ability to purchase goods from abroad will be decreased and the prices of all goods will go up due to inflation. Also, on the other hand, if wages and prices increase faster than productivity we will become less competitive. The Monetary Council has recommended to governments that they establish Tripartite Committees comprised of representatives from the government, private sector and the trade unions to monitor wages, prices, employment and productivity.

With respect to financial stability, whereas in the case of the devaluation you will lose the ability to purchase more goods and services, in this case, if a bank closes you will lose all of your money. A proper legal and regulatory environment is therefore vital to the maintenance of stability. Stability can therefore be spelt out under the following headings with the appropriate responsibilities assigned to different institutions:

- The Central Bank has the responsibility to maintain the external and domestic value of the currency;
- The Central Bank in conjunction with the Governments has the responsibility of ensuring the safety and soundness of the financial system;
- The Banks have the responsibility of ensuring the safety of their obligations to their depositors;
- The Government has the responsibility that they keep their obligations for salaries, services and debt repayments.

Without this stability, growth and development will be very difficult to achieve, much less maintained.

This brings me to two fundamental premises which I have taken great pains to bring to the attention of our governments and citizens, and will continue to do so on every available occasion.

Number one is that banks do not lend out their own money. They only lend what is deposited with them. It is therefore depositors money which is at risk. Secondly, governments can only provide services with money which they take in through taxes or its citizens. If the government provides a particular service it can follow several procedures. Firstly, it can decide on full cost recovery, that is, if it cost $100 to provide, they will charge $100. It can outsource the service so that an external firm provides it. The firm will charge the full cost plus, unless the government subsidises all or part of the service. It can provide the service free of cost to the consumer.

In the case of the subsidized and the free provision, the question would be, *who pays?* The simple answer is the Tax payer.

There is, of course, another route where these costs can be shared with other countries in the OECS, thus bringing down the unit costs.

These issues are important, not only in informing our citizens of our reality, that is, that there is no free meal and that someone has to pay or someone has to be held responsible, but also that they have developmental costs and implications.

With respect to costs, the expense of running so many services which have to be passed on to individual tax payers or business firms either directly or indirectly impacts negatively on our productivity and competitiveness. This high cost of government means less disposable incomes for individuals and higher running costs for businesses. The implications are that if we get our citizens into the mode of depending on the government for everything this will not get them into the creative spirit of creating wealth and jobs.

We must always remember that a nation is the aggregation of all its individual citizens and that if the nation is experiencing difficulty all of its citizens are also suffering in one way or the other. In rectifying the problem there has to be some level of equity in sharing the pain, but the basic fundamental problem still remains and has to be treated with. To give a basic example, suppose an individual earned $10,000 a month and was able to spend through credit $15,000 a month. At the end of the year he/she would be in debt to the total of $60,000. At this point the creditors would say we have stopped extending credit and you now have to start paying back. If the repayment period was one year, the individual would now have to live on $5,000 a month, which is quite a drop from $15,000. Of course, they might be given more time. The moral of this example is that this holds for individuals, firms and governments.

Speaking directly to the question of development, the ECCB sees its role to be in the area of money and capital market development once the stability conditions have been treated with. We have analysed the gaps in the system and are proceeding along the lines of establishing markets and institutions, putting in place the regulatory framework, and removing legal and administrative barriers to the creation of a single financial space. In the area of markets we have the following:

- A common market for the EC dollar and foreign currencies;
- An IBM to provide liquidity for banks;
- A RGSM to provide markets for government securities;
- A securities market for shares;
- A secondary market for primary mortgages.

With respect to institutions we have established:

- The Eastern Caribbean Securities Exchange Depository and Registry;
- The Eastern Caribbean Home Mortgage Bank.

We are now working on an Eastern Caribbean Enterprise Fund to be followed by an Eastern Caribbean Unit Trust.

A number of supporting institutions such as the Eastern Caribbean Institute of Bankers, the Eastern Caribbean Bankers Association, and the Eastern Caribbean Institute of Accountants have also been established.

We need to have close liaison with the OECS Bar Association and we hope that a vibrant OECS Business Council will be created to push the development of the private sector in the region.

We need the support of our governments and our people to create a highly sophisticated and internationally competitive financial sector, which can pave the way to the achievement of our goals and objectives.

We are confident that this is the correct path to proceed on and that with the political will of our governments, the innovativeness of our private sector, and the societal consensus of our people across the OECS, we will SUCCEED.

*However, in conclusion, we must remember that success comes before work only in the dictionary.*