

## Ewart S Williams: Coping with the international financial crisis

Address by Mr Ewart S Williams, Governor of the Central Bank of Trinidad and Tobago, at the Grenada Chamber of Industry & Commerce 20th Annual Banquet and Awards Ceremony, St George, Grenada, 22 November 2008.

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### Salutations:

The Honourable Tillman Thomas – Prime Minister  
The Honourable Nazim Burke & Mrs. Burke – Minister of Finance  
Mr. George Harford – Director  
Mrs. Yvonne Gellineau-Simon – President  
Mr. Richard Duncan – Managing Director

I am pleased to have this opportunity to address you at your Twentieth Annual Banquet and Awards Ceremony.

Let me congratulate the Grenada Chamber of Commerce firstly for your longevity (surviving since 1921 is an enormous achievement) and for your service to Grenada in general, and the private sector of Grenada, in particular. From time to time, policymakers in the Caribbean tend to take the private sector for granted, or rather fail to capitalize on the enormous advantages that could derive from close private-public sector collaboration. Large countries with large markets could depend on the forces of the market mechanism, although as recently seen in the US, in times of crisis, markets cease to work properly, whereupon close collaboration between public and private sector becomes not optional but the only prescription for survival.

Small countries, like Grenada, need to exploit the synergies inherent in a close private-public sector partnership and institutions like the Chamber of Commerce need to be at the centre of this partnership, for the good of the economic development and survival of the country.

I am sure that you would agree with me that the last few months have seen unprecedented events as regards geopolitics and the world economy. Even his ardent critics will concede that the election of **Barack Obama** as President of the United States was nothing short of momentous. Here is someone who four years ago was a little-known first term Senator, but who was able to **organize a crusade and kindle such passion** to become the first African-American President of the U.S... For many, that's pretty close to a miracle.

And for many, the events that are continuing to unfold in the global economy **are no less momentous** and even less explicable. The very respected Alan Greenspan, the former Chairman of the US Federal Reserve, described the recent meltdown in global financial markets as a **veritable tsunami**. US Treasury Secretary Henry Paulson, who is now trying to bring some order to the chaos, insist that the current crisis is without doubt a "once in a lifetime event".

What started, in the US, as a well-intentioned effort to facilitate homeownership among lower income wage-earners has now mushroomed into a global financial meltdown with far-reaching implications for the major economies as well as for **innocent bystanders** all over the world.

Clearly, this is a bit of over-simplification because, while the roots of the turmoil may have been in the sub-prime crisis, this was by no means the only factor. Excessive risk-taking by the world's largest financial institutions: overleveraging (meaning taking risks with borrowed money) greed, and a disdain for prudential regulation also played substantial parts in a very complex mosaic.

What is also incredible is the speed with which this turmoil has unfolded (**it could make Usain Bolt green with envy**).

Things appeared to be reasonably under control up to August. **September was a difficult month for credit markets** following the failure of Lehman Brothers and the collapse of Freddie Mac, Fannie Mae and AIG.

But **October was just unbelievable**, as several other major financial institutions failed or had to be bailed out by Governments: **credit markets** seized up, and interbank lending, which is the grease of the international financial system, almost completely stopped. When the dust cleared, the **world's major stock markets** had declined by an average of 40 percent: **the investment banking sector** in the US had virtually disappeared, or had been transformed and the world's largest banks and perhaps the largest insurance company were being supported by government funds.

The **economic slowdown in the US**, which had been mild up to July-August, deepened significantly after the credit market seizure in mid-September. In the third quarter, US GDP declined and with an even larger decline in the making for the current quarter, the US economy is now formally in recession, though, to the millions that have lost their jobs (unemployment is now at 6.7 per cent, the highest rate for more than two decades) , the recession came some time ago.

But the US has lots of company, **the UK** has been in recession for several months now, and within the last two weeks, **Germany** and **Japan** announced that they were also in recession.

Governments all over the world have been implementing **policy actions** to address the root cause of the financial stress and to support global economic recovery. The initiatives have included programmes to purchase distressed assets, use of public funds to recapitalize banks and provide comprehensive deposit guarantees and coordinated reductions in policy interest rates by major central banks.

**Market conditions are starting to respond** to these actions. Interbank lending is slowly reappearing and the major banks are beginning to lend again, though still at very high interest rates.

But the bad news continue and even seem to get worse, particularly in the US.

Over the last few days, you would have seen that all **three US automakers**, one of the flagship sectors in the US economy, are on the verge of bankruptcy and could go down if they do not receive US\$25 billion of support from the Government. In a worst case scenario, this could put as many as 3 million people out of jobs. And as if that was not bad enough yesterday the focus shifted to **CITIBANK**. Up to recently one of the crown jewels of the world banking system, Citibank's very survival is now in jeopardy, its stock price having fallen by about 50 per cent in one week.

## **And what about us in the Caribbean**

First a little story. Couple weeks ago we hosted a semi-annual meeting of the **regional central bank governors** and in comparing notes we came to the conclusion that while we were trying to explain to our separate publics that the Caribbean was not going to be seriously affected by the international crisis, for a number of technical reasons, **our publics knew better**. They were looking at television, seeing the US, Europe and countries around the world, virtually falling apart, financially and economically, and saying to themselves, that it can't be different with us in the Caribbean.

In hindsight, perhaps, we may have been trying to protect our people too much, because as things are unfolding we are all going to be affected – and in some cases, to a great extent.

Most countries in the region have not been seriously affected through the “financial channel”, **meaning simply that our banks have not collapsed**. This is so because our banks depend

more on domestic deposits than borrowing from abroad. That's not to say that a few high net-worth individuals, who were in the US stock market or perhaps some pension funds did not lose some money, though pension fund losses should not be serious, since in all Caribbean jurisdictions there are restrictions on foreign investments by pension funds. In reality, pension funds hold most of their assets in government securities.

**Jamaica** was perhaps the most seriously affected through the financial channel and this was because of their specific circumstances. It is no secret that Jamaica has a very high level of official external debt (about US\$6 billion or 50 per cent of GDP, while external reserves are about US\$2 billion). Given the global financial market jitters and the flight to quality by investors, the prices of Jamaican Government global bonds declined sharply. Unfortunately the Jamaican banking system holds a significant part of this debt and thus the decline in bond prices raised the prospect of some banking system instability. The Bank of Jamaica had to establish a US\$300 million facility to provide assistance to the commercial banks. This notwithstanding, credibility problems have remained and this is being reflected in capital flight, which has led to a sizeable depreciation of the Jamaican dollar.

In addition, Jamaica has also seen a decline in migrants' remittances, **which is a major source of foreign exchange earnings** (US\$1.8 billion a year). The Jamaican authorities have indicated that so far **tourism** has not been affected, but I suspect, that it is just a matter of time.

Unlike Jamaica, the Bahamas has already seen a sharp decline in tourism. In a national television address, Prime Minister Ingraham observed that since August, all the major hotels on the islands began to experience the lowest occupancy rates in many years, and that, advanced bookings for the next year painted an even bleaker picture. Many of you must have read that the **Atlantis Hotel**, the largest hotel in the region, had to send home 800 employees, because of the reduction in tourist arrivals. The Bahamas is also facing a "cessation of direct foreign investment in the tourism sector because of the poor outlook for the industry and because of financing difficulties".

As you know, tourism is the mainstay of the Bahamian economy; because of the decline in the sector, non-performing loans in the banking sector have increased by 40 per cent.

**In Barbados**, you have a similar situation of declining tourism activity, and the postponement of investments in the tourism sector. This has led to a sharp slowdown in economic activity so much so that the Government has embarked on a public sector-led recovery programme, in the context of a social compact, involving the private sector and the trade unions.

**In Trinidad and Tobago**, the impact of the global crisis is currently being reflected in the unfolding developments in the energy sector. The global slowdown has already led to a **dramatic fall in oil prices** by about two-thirds, from a high of US\$147 per barrel to around US\$52 per barrel; there have also been sizeable declines in the prices of other energy sector products – LNG, methanol, ammonia and urea. In addition to the decline in energy prices, several of the petro-chemical plants have had to cut output because of a slowdown in demand. As a result of these factors, government revenues are now projected to decline by about 15 per cent, compared with the budget.

In the light of the global economic slowdown and the decline in budget revenues, on Friday evening Prime Minister Patrick Manning announced cutbacks in government discretionary spending and in outlays on certain development projects. Prime Minister Manning pointed to the economic difficulties being faced by the CARICOM region, which is Trinidad and Tobago's second largest export market and undertook to maintain the resources of the CARICOM Petroleum Fund.

I must confess that I am not very up to date on the specifics of the **Grenada** case, but I would guess that you would face pretty much the same risks and vulnerabilities as the other OECS territories:

Grenada is a highly open economy and as such, very vulnerable to exogenous shocks, like the crisis that is currently confronting us all today. In addition to your vulnerability to natural disasters, you may well have to face:

- A **decline in visitor arrivals** as well as a postponement of foreign investment in the tourism sector, given that current uncertainties may cause investors to play safe, at least for the time being;
- Like the rest of the Caribbean, you are likely to face a **reduction in remittances** from abroad; and
- Any **other exports** you have could face difficulties in Caribbean markets

All these factors could lead to a slowdown in the pace of economic activity in Grenada. In addition, you have a pretty high **public debt burden**, and other things being equal, you could expect an increase in debt servicing costs (certainly on external debt), which would place additional pressures on your already strained public finances.

So you, like the rest of us in the region, could face challenges arising out of the global financial crisis, if you are not doing so already.

But for all the negative consequences, ladies and gentlemen, Grenada has tremendous positives and perhaps your real challenge is seizing the opportunities presented by these difficult times. And what are some of these opportunities:

- One immediate benefit you will have is **lower fuel prices** – one example of what is good for you is bad news for me;
- My understanding is that your **agricultural sector** is currently recovering from the ravages of recent hurricanes; but, this crisis should spur you to move beyond recovery, towards not only agricultural self-sufficiency, but towards making Grenada one of the regional food-baskets. You have a ready market in Trinidad and Tobago, where food shortages and in particular, insufficient supplies of fruits and vegetables are contributing to an over 30 per cent increase in food prices;
- The crisis presents an opportunity for you to strengthen your **skills bank** by luring back skilled Grenadians and West Indians, who could be the first to suffer from the labour market problems in the US, UK and other places. There are highly qualified Caribbean people out there who just want the nudge to come back home and the unemployment and uncertainty in the US and UK may be just enough to tip the balance, to provide that nudge.
- And some of these returning nationals may be able to bring not only skills but **capital**, as well, in the form of direct investment. Interest rates are much higher in the Caribbean than in the industrialized world, rates of return on capital are higher here than they are currently in the US and it's our job to go out and showcase our advantages to the Caribbean diaspora; to entice them to set up businesses back home. This is the right time and we should not lose the opportunity once again.

Ladies and gentlemen, in my many years of working with the IMF I have been exposed to many economies, both developed and developing, both large and small. I have seen economies waste resources and I have seen economies do miracles with little.

I can tell you that by developing country standards, the OECS economies are very well endowed. As a region we have abundant sun, sand and good weather (most of the time); our most attractive art, music and culture; proximity to the United States, fairly good educational resources, and fluency in the English language, which has become the language of trade and business.

I know also, the frustrations that Caribbean governments have faced in their quest for economic transformation. Oft-times globalization has not worked to our advantage.

I am acquainted with the **loss of preferences** in Europe for our agricultural commodities; our efforts at **light manufacturing**, which floundered in the face of technological advances, increases in labour costs and the advent of China as the world's manufacturer; and when the region tried to adapt through **offshore banking**, the Financial Action Task Force and new regulatory standards ensured the death of another promising avenue of potential diversification.

But many of our countries have continued to adapt and to remake themselves. And Grenada is one of those that has shown the ability to adapt. Your success in exporting tertiary educational services is a case in point. Grenada has a **world class medical school** that caters for students from the US and the Caribbean region. Some experts think that Grenada could capitalize on this platform and its current tourist industry, to expand into medical tourism and assisted living geared, for example, to the aging US population.

And while light manufacturing on a large scale may be out of the question, there is still room to exploit your comparative advantage in niche industries, like **organic spices – nutmeg and mace**.

You as business people know better than I ever can, that the current global environment will not provide you a free lunch. Rather, you will have to earn your keep through your ingenuity, by continually adapting and by continuously becoming more competitive and efficient in what you do.

Ladies and gentlemen, one lesson that the current crisis should teach us is that we need to enhance the region's competitiveness, in order to survive. This crisis should also provide additional impetus to the **regional integration movement**.

Former Barbadian Prime Minister Owen Arthur, who has been a leading proponent of the CSME recently reminded us that "**delays** in carrying out regional economic and financial integration, as contemplated under the CSME, will compromise severely the region's capacity to take advantage of new economic **partnership** agreements with our major trading partners, or to fit the regional economy into the evolving global economy".

While he recognized that the recently signed **EPA** was not a perfect agreement, he defined it as an important instrument of economic engagement and cooperation, which if used properly, would help the region build new competitive industries.

I noticed that the theme of your Banquet and Awards Ceremony this evening is "**Fostering Development through Partnership**". I am not sure which partnerships you had in mind. I nevertheless invite you to seek to build partnerships, throughout the region, to ensure the implementation of the CSME and the EPA, since it may be the best way of guaranteeing the development of Grenada and the region as a whole.

Thank you for inviting me and I wish your organization all the best.