COUNTRY ECONOMIC REVIEW 2017

BRITISH VIRGIN ISLANDS

Dollars ($) throughout refer to United States dollars (USD) unless otherwise stated

OVERVIEW

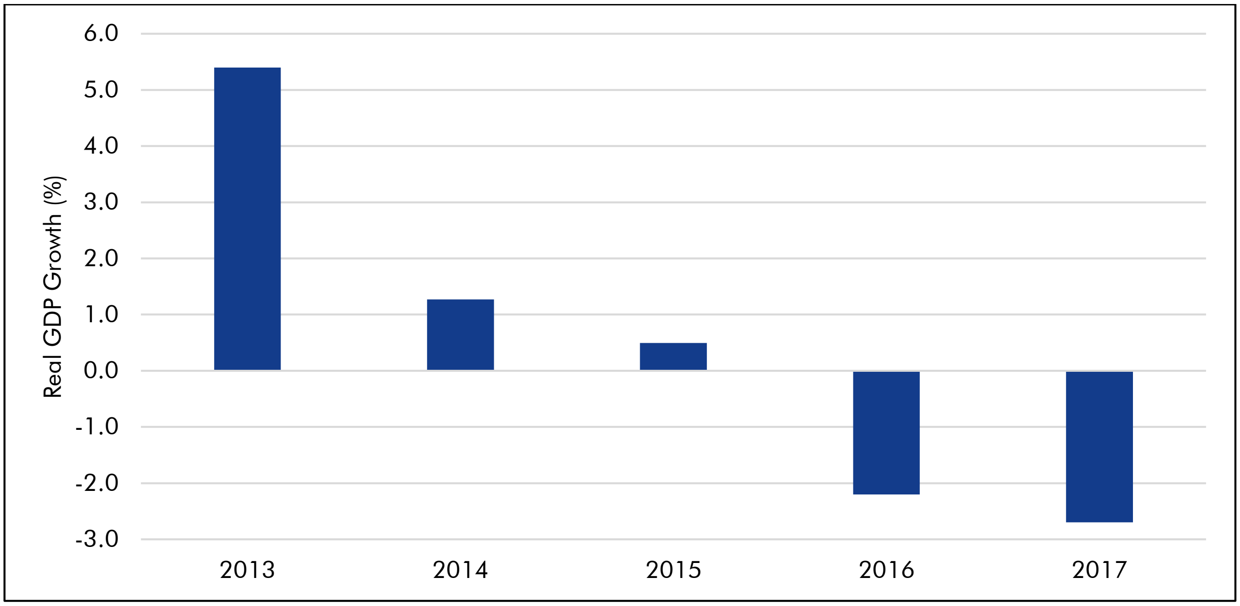
Economic growth in the British Virgin Islands (BVI) is estimated to have contracted in 2017, due in part to the impact of unprecedented weather-related events. Over the period August 7 to September 19, 2017, BVI was affected by severe flooding and two Category 5 hurricanes. The most destructive of the three events, Hurricane Irma, caused widespread and catastrophic damage to the Territory on September 6. This was followed by Hurricane Maria on September 19, 2017. Damage from the two hurricanes is estimated to have exceeded $3.6 billion, equivalent to approximately three and a half times the annual gross domestic product (GDP) of BVI. The decline in economic activity, particularly in the last quarter of the year, is expected to have weakened the fiscal and debt positions of the Government of British Virgin Islands (GOVI).

1. REAL SECTOR

1.01 BVI's economy is estimated to have contracted by 2.7% in 2017, following a decline of 2.2% in 2016. The decline in economic activity in 2017 is attributed mainly to the impact of the hurricanes on the tourism sector. Stayover arrivals in 2017 fell by 17.7%, while cruise arrivals and day trippers contracted by 42.9% in 2017. With a decline in arrivals, the sector was not able to realise the benefits which were expected to accrue from new major tourism projects and the reopening of some properties which had closed temporarily in 2016 for refurbishment and redevelopment.

1.02 Following the passage of Hurricanes Irma and Maria, severe damage was reported across all major hotels and resorts, as well as marinas and boats. The accommodation room stock was estimated at 2,700 rooms, which has been reduced to approximately 336 rooms as of March 1, 2018. Similarly, the charter and bareboat industry had a total of 3,800 berths at sea, and now reduced to 1,584 as of March 1, 2018.

FIGURE 1: REAL GDP GROWTH 2011-2017



Source: Ministry of Finance (MoF), Department of Statistics.

1.03 At the end of December 2017, inflation was estimated at 1.2%, representing a slight increase in the consumer price index. The increase in the index is attributed to increased prices, fees and charges on items or services such as education, miscellaneous goods and services, alcoholic beverages, and communication.

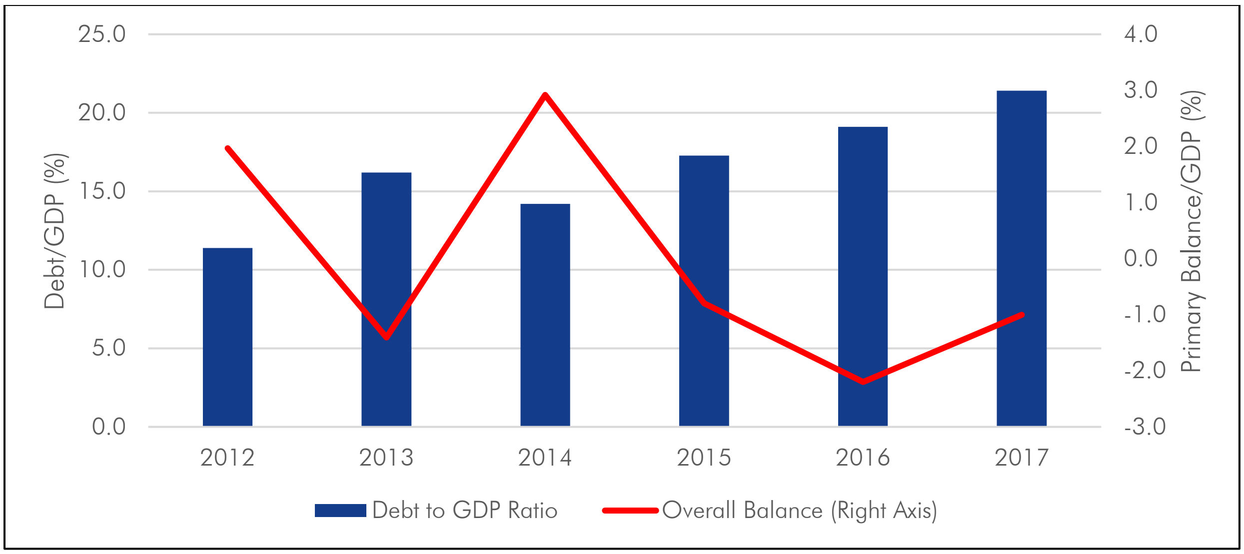
Social Sector

1.04 Unemployment in BVI was estimated at 2.9% at the end of 2017. Unemployment has been below 5% for almost a decade, while labour force participation rates have remained high, averaging 90% over the same period. At the end of 2017, the estimated population of BVI was 32,800, reflecting a decline of 9.1 % in 2017. Expatriates make up a significant proportion of the population and the workforce (approximately 67% in 2014).

2. CENTRAL GOVERNMENT OPERATIONS AND DEBT

2.01 An overall deficit (after contributions to the Reserve Fund) of 1.1% of GDP is estimated for 2017, the third year that a fiscal deficit has been recorded. Notwithstanding the overall deficit, contributions to the reserve fund were made in 2015 and 2016, with a fund balance of $57.1 million (mn) at the end of 2017. The performance of the fiscal accounts was influenced in part by the natural disasters of 2017. The overall fiscal position in 2017 was driven by a reduction in total revenue which was not offset by a commensurate reduction in expenditure. Total revenue fell by 4.6% to $292.9 mn in 2017. All sources of revenue declined except taxes on goods and services, which grew by 2.5%. Growth in taxes on goods and services is attributed to an increased intake from financial services following the fallout in 2016. Total expenditure of $305.7 mn was lower than the previous year's outturn of $317.6 mn, and remained relatively flat due to an 18% reduction in capital expenditure which was taken up by an increase in spending on goods and services and other recurrent spending.

FIGURE 2: DEBT/GDP AND PRIMARY BALANCE



Source: MoF.

2.02 In April 2012, GOVI committed to a pattern of governance consistent with global standards and international best practices by adopting the Protocols for Effective Financial Management. These include a number of actions and principles, including the active monitoring and management of fiscal and debt targets, as well as the maintenance of a reserve fund. As a result, debt levels have been relatively low with total public-sector debt at 19.5% of GDP in 2017, and averaging 17% over the last three years. Debt service represented 6.8% of recurrent revenue. GOVI breached one of its three debt management requirements[1], the ratio of liquid assets to recurrent revenue, which at 20.4% in 2017 was below the 25% minimum required.

3. EXTERNAL SECTOR

3.01 BVI does not compile Balance of Payments (BOP)[2] statistics. The main export sectors are financial services and tourism, and the main import source market is the United States of America.

[1] (a) Net Debt: 80% maximum of recurrent revenue; (b) Debt Service: 10% maximum of recurrent revenue; and (c) Liquid Assets: at least 25% of recurrent expenditure.

[2] BVI is expected to compile its first BOP with assistance from the Caribbean Regional Technical Assistance Centre in 2018/19.

Inflation in BVI, has been stable (under 2%) for the past five years. Given that BVI is dollarised, this low inflation environment may suggest that there are no BOP issues of concern.

4. FINANCIAL SECTOR

4.01 The latest statistics from the Financial Services Commission showed that total new business incorporations increased by 2.6 % in 2017 (32,592). However, the total number of BVI-registered companies at the end of 2017 was 389,459, 6.6% lower than the total at the end 2016 (416,784). The recent quarterly incorporation rates remain below the pre-2016 period, when usually more than 10,000 companies would form each quarter.

4.02 At the end of the third quarter of 2017, total assets of the commercial banking sector in BVI grew by 2.1% to $2,304.3 mn from $2,258 mn at the end of December 2016. This represents a slight increase in loans and advances (0.7%) from $1,398.7 mn at the end of 2016 to $1,409.0 mn at the end of September 2017. Total liabilities increased by 13.9% at the end of September 2017, reflecting an increase in deposits (3.1%) and long-term debt. At the end of September 2017, total liabilities and shareholders' equity grew by 2.1%.

5. OUTLOOK

5.01 The outlook for BVI remains prudently optimistic. Economic activity will be driven primarily by construction activity related to rehabilitation and reconstruction. Tourism is expected to recover slowly as more room stock becomes available by the beginning of the tourist season in November 2018. However, repairs to villas and cottages will support the tourism sector as the Territory continues to rebuild. The restoration of electricity by the end of March 2018, will also support, in part, the reopening of small businesses as the Territory returns to a state of normalcy. Growth is expected to average 3% over the next three years before returning to the long-term average growth of 1%. The pace of the recovery will depend on: (a) GOVI's ability to restore damaged infrastructure; (b) the pace at which the private sector is able to replace lost assets and resume regular business operations; and (c) the rate at which households are able to reconstruct damaged homes and replace personal assets.

5.02 Additional pressure is likely to be placed on the fiscal and debt positions as GOVI is expected to borrow heavily for the recovery and redevelopment of the Territory. Preliminary projections for 2018 anticipate lower revenues due in part to lower collections from the accommodation sector, taxes on international trade due to the import duty exemptions, and lower payroll taxes. Expenditure levels will be elevated in 2018 and in the short term, primarily due to higher capital expenditures for the recovery and redevelopment programme.

5.03 Downside risks are related to a fallout from the financial sector as the European Union proposes to make a decision on its blacklisting of BVI by the end of 2018. Capacity constraints are also expected to hamper the recovery process, as the demand for skilled labour around the Region heightens, due to elevated levels of post-hurricane rehabilitation and construction. Any additional weather-related shocks in 2018 will derail recovery efforts.

TABLE 1: SELECTED INDICATORS

	2013	2014	2015	2016	2017
Real GDP Growth (%)	5.4	1.3	0.5	-2.2	-2.7
Average Inflation (%)	1.5	1.9	0.8	1.1	1.7
Unemployment (%)	2.8	2.8	2.8	2.8	2.8
Primary Balance (% of GDP)	-0.9	3.4	-0.4	-1.8	-0.6
Public Sector Debt (% of GDP)	16.2	14.2	17.3	19.1	21.4

Source: GOVI.