CARIBBEAN DEVELOPMENT BANK

BRITISH VIRGIN ISLANDS

ECONOMIC BRIEF

United States Dollar (US$)

Overview

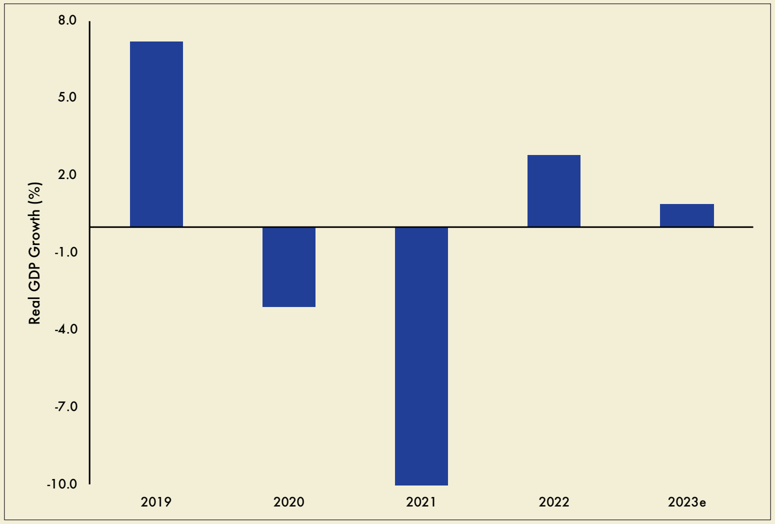
The British Virgin Islands (VI) economic recovery remained tepid in 2022, as strong headwinds from global economy unfolded. The full reopening of borders and strong demand for travel contributed to a resurgence in tourism, albeit below pre-pandemic levels; but the financial sector, the main driver of economic activity continues to be challenged. Fiscal balances deteriorated, but debt to gross domestic product (GDP) trended downwards to keep public finances compliant with key borrowing and fiscal ratios under VI's Protocols for Effective Financial Management (PEFM)[1]. Key banking sector indicators improved, as the sector remained well capitalised. The external current account deficit expanded, with increased imports buoyed by higher prices and volumes. The medium-term outlook is cautiously optimistic with heightened downside risks related to the global economy and geopolitical tensions.

KEY DEVELOPMENTS IN 2022[2]

Real GDP grew by an estimated 2.8% in 2022 as COVID-19 closures and restrictions were discontinued by July. This upturn follows an estimated contraction of 12.4% in 2021 as the pandemic continued to weigh heavily on the economy (see Chart 1). An increase in tourism and construction activity, and related sectors drove growth. Tourism continued to recover, with strong stayover and cruise arrivals in 2022. Stayover arrivals rose to 173,213 visitors, compared with 59,289 in 2021, but still below the levels recorded prior to the 2017 hurricanes. Cruise and day-trippers also trended upwards reaching 350,076, just 59.1% of the level recorded in 2019. The recommencement of annual events, such as the Virgin Gorda Easter Festival and the BVI Spring Regatta and Sailing Festival, contributed in part, to the increasing number of visitors during the year. The reopening of the Virgin Gorda Airport in November after a prolonged period of closure also contributed to the increase in overnight and day-trip visitors. In other sectors, public and private sector construction activity is estimated to have grown in 2022. Imports of construction materials – the proxy for construction activity – grew by 24.2% in the first 6 months of 2022 compared with the same period in 2021. Public sector investments were centred around several key infrastructure projects related to the hurricane reconstruction. Positive spill overs from construction and tourism sectors drove activity in other sectors such as transportation, wholesale and retail, and real estate and renting activities which was influenced by strong demand for rental of high-end properties.

The offshore financial services sector remained challenged[3] into 2022. Amid sanctions and the freezing of Russian assets, compliance with international standards, and heightened macroeconomic risks in key source markets, new company incorporations fell by 22.4%, a reversal of the growth recorded in 2021. The total number of active companies (367,672) at the end of 2022 was slightly lower (-0.3%) than the number recorded at December 2021.

Chart 1: Real Gross Domestic Product Growth



Sources: *Ministry of Finance (MOF), Caribbean Development Bank (CDB) projections.*

[1] The key ratios include borrowing ratios of net debt, debt servicing, and liquid assets.
[2] All comparisons are with respect to 2021, unless otherwise stated.
[3] The industry faces many challenges including: (a) sanctions and freezes on Russian assets; (b) the Organisation of Economic Cooperation and Development (OECD) global corporate minimum tax for multinational enterprises; (c) publicly accessible registers of beneficial ownership by 2023; (d) preparations for the Caribbean Financial Action Task Force mutual evaluation (first quarter, 2023); and (e) implementation of the recommendations of the Commission of Inquiry.

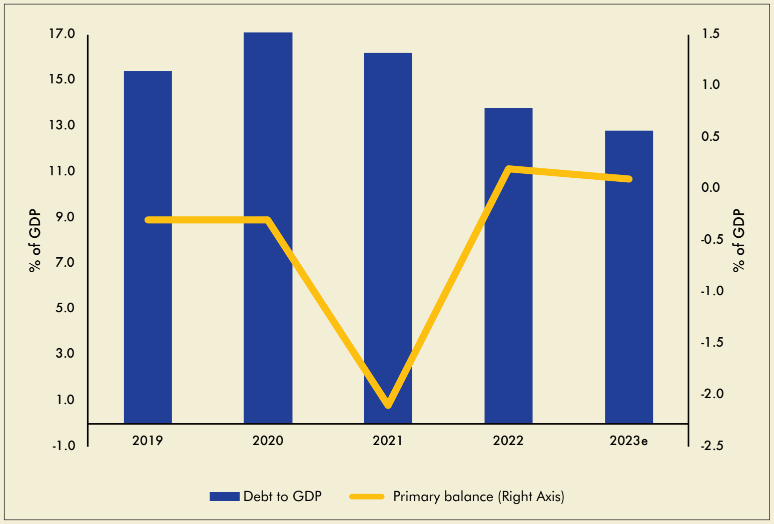
Consumer prices rose. Average inflation for 2022 is estimated at 6.4%, up from 2.8% in 2021 and 0.7% in 2020. The war in Ukraine and more acute global food and fuel supply and logistical challenges contributed to an increase in prices. While all consumer price index categories recorded increases, the largest increases were recorded in fuel and food. Other notable changes were in furniture and household equipment, education, utilities, and clothing and footwear.

The fiscal position of the government improved in 2022. Government operations resulted in a primary surplus of 0.2% of GDP, a turnaround from the 2.1% of GDP deficit recorded in 2021. Similarly, there was a reduction in the overall deficit, which improved to 0.1% of GDP from 2.5% in 2021. The enhancement in the fiscal balances was mainly influenced by a 7.2% increase in total revenue. The uptick in total revenue was largely attributed to higher intakes from income tax, and taxes on goods and services and other taxes, in line with the expansion in economic activity. However, the overall increase in revenue was tempered by a decline in collections from taxes on international trade, partly associated with the government's decision to reduce import duties as part of the broader economic stimulus.

Total expenditure declined marginally by 0.6% as spending on goods and services and other expenses decreased. Nonetheless, this reduction in total expenditure was offset by increases in outlays for subsidies, transfers, and employee compensation. Capital expenditure saw a significant surge of 49.1% compared with 2021, primarily due to increased investment in key infrastructure projects, including in the education sector.

Public debt[4] trended down in 2022. Debt fell to 13.8% of GDP, from 16.2% in 2021 (see Chart 2). This reflects a concerted effort by the Government to limit its accumulation of new debt. Central government debt service payments in 2022 rose to $19.9 mn, 1.4% of GDP.

Chart 2: Fiscal and Debt Performance



Source: *MOF, CDB.*

Domestic financial sector indicators remained strong in 2022 despite the upward trend in the non-performing loans (NPLs) ratio. Total assets of the banking sector stood at $2.8 billion (bn) at the end of 2022, up by 2.2%, compared with 2021. Deposits rose by 1.5% to $2.2 bn. At the end of the year, loans and advances grew by 26.9% to $1.6 bn. Net interest income for all commercial banks grew by 12.3% in 2022, when compared with 2021. The risk-asset ratio rose from 46.8% in to 49.0% at the end of 2022. The ratio of NPLs to total loans rose to 13.7% at the end of 2022, from 10.0% at the end of 2021.

[4] Public debt includes parastatals' risk-weighted debt and capitalised value of public-private partnerships.

2023 OUTLOOK

The outlook for VI is tepid and marked by heightened downside risks. Economic growth of 0.9% is projected for 2023. Tourism activity is expected to strengthen during the year, with the introduction of a direct flight from the United States of America market. However, the financial services sector, although resilient, will continue to face strong headwinds from the sanctions on Russia, the possibility of continued blacklisting from the OECD, and the upcoming December deadline for implementation of the beneficial ownership registry. To bolster revenue from the sector going forward, the Government has revised its financial services and maritime industry fees upwards and implemented an international tax authority filing fee. The commencement of key infrastructure projects, such as the West End Ferry Terminal, will bode well for construction activity. Positive knock-on effects are expected across ancillary sectors including wholesale and retail and transportation.

Over the medium term, the PEFM will be central to managing fiscal and debt balances and pursuing the objectives of sustainability. Fiscal deficits are expected to continue into 2024 as the economy experiences some rebalancing, lower revenue collection from the financial services sector, and headwinds from the global economy. Critical investments in infrastructure will be important to steer economic activity and prepare the country for longer-term sustained development. However, this is conditional upon the extent to which new borrowings will significantly impact compliance with the PEFM and the borrowing ratios.

Downside risks remain elevated in an evolving global economy. Vulnerabilities to other external shocks from the global economy and natural disasters remain present.

DATA

The table below summarises the key economic and social indicators underpinning this country brief. These data are taken from several sources and are the latest available at time of publication. The 2023 data estimates and subject to change.

Selected Indicators

	2019	2020	2021	2022	2023e
Real GDP growth (%)	7.2	-3.1	-12.4	2.8	0.9
Average Inflation (%)	1.4	0.7	2.8	6.4	4.2
Debt to GDP	15.4	17.1	16.2	13.8	12.8
Primary balance (Right Axis)	-0.3	-0.3	-2.1	0.2	0.1
Reserve fund balance (in % of GDP)	6.0	5.7	6.4	6.4	6.2

Source: *MOF, CDB.*

Note: e-estimate.