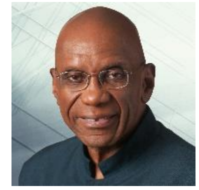

Economic Letter April 2018

Barbados' Problem of Deficit Financing

It has to be said at the outset that the problems arising from the financing of Barbados' Government deficit have nothing whatsoever to do with the printing of the currency. Barbados currency notes are printed by the firm of De La Rue in the UK, and stored in the vaults of the Central Bank until commercial banks request an additional supply to meet customer needs.

The real problem with Government finances arises whenever tax and other revenues are insufficient to cover monthly expenses, and Government is at its overdraft limit with the Central Bank.

The Central Bank is the Government's banker, and in that capacity the Bank provides Government with an overdraft to cover the ins and outs of its cash flow. The limit to this overdraft is set by law, at 10 percent of the estimated revenue for the fiscal year.

Over the past several years there have been many months when Government was already at its overdraft limit as civil servants' payday approached, and revenues accumulated at the Treasury were insufficient to cover the wages bill. In these circumstances the Central Bank buys Treasury Bills in order to provide the additional funds needed to ensure that all Government expenditures can be covered.

This does create a problem, because the Central Bank lends to Government for payments in Barbados dollars. However, when these dollars are spent, to buy groceries, to pay electricity bills, to pay for gasoline, and other necessities, they generate a demand for imports. Imports must be paid for in foreign exchange, so ultimately banks will return to Central Bank to obtain foreign exchange from the country's store of reserves, so they can meet the additional import demand.

It is this process which leads inevitably from Government overspending to the loss of foreign reserves. The only solution is a reduction in Government spending, sufficient to bring Government's current account into balance, in the first instance.

Expenditure cuts will need to be sustained for about three years, as suggested in my paper *The Barbados Economy: The Road to Prosperity* (*www.delisleworrell.com*). That is because of the need to generate savings on the Government's current account and rebuild an adequate store of foreign reserves. In that paper I show how this policy could lead to a healthy 3 percent growth rate by 2021, the achievement of reserves adequacy, and a gradual reduction of the ratio of Government debt to GDP.

The Barbados economy has great potential for growth and future prosperity. Our country is among the world's most desirable tropical resort destinations; Barbados is an attractive location for international business services; and a full commitment to renewable sources of power could pitchfork the economy into the first rank of economic development.

However, it all starts with fiscal rectitude and a public service that gets the job done. Ensuring Government savings on the current account, and renewing the public sector to provide efficient delivery of services, will remove the twin roadblocks in the way of economic prosperity and improved livelihoods for all Barbadians.