The Guyana Economy before Oil

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ABSTRACT

This report looks at the state of the Guyana economy at the end of 2018, the last year before the start of oil production. The picture that emerges is one of higher growth than in most other Caribbean countries. The authorities have taken a number of measures to improve the business climate, however, the country's potential remains stymied by skills shortages and a business environment that constrains investment. In addition, life expectancy, infant mortality, and overall human development indicators compare unfavorably with those of the rest of the Caribbean. With an operating budgetary surplus, low level of debt, and forthcoming oil revenues that will be sustained, there is sufficient fiscal space for higher public investment to improve social conditions. At the same time, structural weaknesses, such as the large size of the public sector and inefficient public enterprises and local governments that absorb a disproportionate amount of resources, have to be addressed. In the financial sector, banks are liquid and broadly profitable, but many face risks, such as low interest rates on assets, poor loan quality, weak provisioning, legal delays in settling delinquent loans, and relations with related parties. Other risks that require greater attention are those of cyber-crime and climate change.

1. Economic Growth

In 2018 the economy of Guyana is estimated to have grown by 4.1 percent, nearly twice the growth rate of the previous year (Table 1)**.** The overall growth rate benefited from contributions in almost all areas, with the exception of performance in the sugar industry. There was strong growth in the construction and services sectors, as well as increased output in a large number of crops, and livestock and forestry. On the other hand, the sugar industry suffered a contraction, a reflection of an ongoing major restructuring, which includes plant closures and a large reduction in its labor force.

a. *Agriculture, fishing and forestry*

There were strong performances for the main agricultural products in 2018, excluding the sugar industry. The sugar industry is estimated to have contracted by about 24 percent in 2018, reflecting the restructuring of the industry around a smaller number of processing plants. The new three-year plan of the Sugar Task Force aims to recapitalize the Albion, Blairmont, and Uitvlugt estates and to increase sugar production from 98,000 tonnes in 2018 to 145,000 tonnes in 2021. Among the other agricultural products, rice production benefited from the introduction of a higher yielding variety, improved cultivation practices, and higher domestic prices. Other crops, including fruits and vegetables, showed strong performances, reaching an increase of about 5 percent over the previous year (Table 2).

Table 1. Guyana: Selected Economic Indicators

					Estimate	Projection
	2014	2015	2016	2017	2018	2019
	(In percent)					
Real GDP	3.8	3.1	3.4	2.1	4.1	4.4
Consumer prices (average)	0.7	-0.9	0.8	1.9	1.3	2.1
Consumer prices (end of period)	1.2	-1.8	1.5	1.5	1.6	2.7
	(In percent of GDP)					
Private investment	8.3	8.3	8.0	8.2	…	…
Public investment	8	4.7	6.4	7.9	7.3	8.1
Current account balance	-9.6	-5.1	0.4	-6.8	-17.5	-22.7
Gross official reserves (mths of imports	3.5	3.7	3.3	2.6	2.1	1.8
GY dollar/US dollar (period average)	206.4	206.5	206.5	206.5	206.7	…
GDP (G$ Billion)	635.4	660.2	723.6	744.6	805.7	852.4

Sources: Ministry of Finance and IMF.

The livestock sector is estimated to have grown by about 23 percent in 2018. In particular, beef, pork, and mutton production benefited from improved farming practices. The output of chicken improved vastly, almost entirely meeting the demand in the domestic market. The fishing industry did not perform well in 2018, reflecting declines in the output of shrimp, tuna, and aquaculture. These declines overshadowed the strong performance in the output of finfish, which was a result of increased investment in the fleet of artisanal vessels. Overall, the production in the fishing sector is estimated to have declined by about 6 percent in 2018.

The output of the forestry sector showed only a marginal increase over the previous year. This performance is a reflection of difficulties in transportation caused by unfavorable weather conditions and insufficient road maintenance. This industry has grown for the first time in three years, reversing the downtrend after a tightening of logging rules in line with higher environmental protection standards.

Table 2. Guyana: Real GDP Growth Rates by Sectors
(In percent)

	2015	2016	2017	2018
Agriculture, Fishing, and Forestry	2.4	-10.2	0.4	1.5
Sugar	6.9	-20.8	-25.2	-23.8
Rice	8.3	-22.3	17.9	-0.5
Other crops	2.0	2.5	2.4	5.0
Livestock	5.8	-5.6	-2.8	23.1
Fishing	-2.6	20.4	1.0	-6.2
Forestry	-10.6	-27.3	9.1	1.8
Mining and Quarrying	9.0	45.4	-8.8	2.9
Bauxite	-13.4	1.9	-0.1	24.6
Gold	16.4	58.1	-8.3	-6.2
Other	-0.3	20.5	-17.6	45.9
Manufacturing	5.3	-9.2	4.2	1.0
Sugar	6.9	-19.9	-25.2	-23.8
Rice	7.6	-21.2	17.9	-0.5
Other manufacturing	3.5	0.6	3.1	5.2
Electricity and Water	5.2	4.4	2.8	2.0
Construction	-10.0	6.3	11.4	11.0
Wholesale and Retail Trade	-0.6	-1.8	8.7	8.1
Transportation and Storage	13.6	1.1	3.9	1.1
Information and Communication	5.5	1.2	2.3	1.9
Financial and Insurance Activities	7.5	2.5	-2.0	5.2
Public Administration	2.5	0.0	1.3	1.3
Education	3.8	1.5	2.0	2.4
Health and Social Services	3.7	1.1	2.5	2.4
Rental of Dwellings	2.5	1.3	5.0	7.5
Other Service Activities	1.7	5.7	3.5	14.0
Total	3.2	3.3	2.1	4.1

Source: Ministry of Finance.

b. Mining and Quarrying

The mining and quarrying industry showed a slight decline in output in 2018, in spite of a strong performance in the bauxite industry. While gold declarations of large-scale miners increased, those of small-scale miners, which account for almost two-thirds of all gold declarations, declined in 2018. Overall, gold declarations are estimated to have fallen by about 6 percent in 2018. On the other hand, bauxite production is estimated to have grown by 25 percent and other mining, including diamonds, sand and stone, increased by nearly 50 percent.

Table 3. Guyana: Balance of Payments
(in millions of US dollars)

					Projections
	2015	2016	2017	2018	2019
Current account	**-163**	**13**	**-246**	**-683**	**-936**
Merchandise trade	-340	-31	-206	-451	-685
Exports (f.o.b.)	1,151	1,434	1,438	1,379	1,490
Imports (c.i.f.)	-1,492	-1,465	-1,644	-1,825	-2,175
Services (net)	-282	-298	-361	-703	-753
Income (net)	460	341	320	471	502
Financial account	**206**	**8**	**233**	**670**	**936**
Net Official borrowing	-18	22	51	83	45
Foreign direct investment	122	32	212	495	1,022
Other	35	-47	-44	-39	-17
Errors and omissions	**-43**	**-21**	**14**	**-11**	**0**
Overall balance	**-67**	**-2**	**-13**	**-56**	**115**
Financing	**67**	**2**	**13**	**56**	**-115**
Memorandum item:					
Current account (in percent of GDP)	-5	0	-7	-18	-23

Source: IMF and Ministry of Finance.

c. Manufacturing and construction

The manufacturing sector is estimated to have shown a small expansion in 2018. This growth was driven by a 5 percent increase in manufacturing activities other than the processing of sugar and rice. These manufacturing activities include food and beverages, as well as pharmaceuticals and building materials. Construction activity picked up considerably, driving up the demand for locally mined sand and stone.

d. Services

The provision of services has continued to expand in 2018. This expansion largely reflects a greater number of visitor arrivals from the diaspora for festive events, as well as a rise in visitors associated with petroleum sector activities. An estimated growth of about 8 percent in rentals of dwellings was associated with petroleum sector activities. There was also an estimated 8 percent growth performance in the wholesale and retail sector, spurred by domestic spending confidence. Overall, services are estimated to have grown by about 4 percent in 2018.

2. External Sector Developments

The balance of payments deficit is estimated to have widened in 2018. The current account deficit widened to reach a level of US$683 million, more than twice the level of the previous year, reflecting both lower exports and higher imports (Table 3). Exports declined by about 3 percent to US$1,392 million, largely reflecting the lower outputs of gold and sugar. Imports increased by about 3 percent, mainly on account of higher prices for fuel and lubricants, as well as larger levels of capital goods. The financial account improved in 2018 as a result of foreign direct investment in the oil sector.

The Guyana dollar appreciated against major currencies in 2018. The exchange rate of the Guyana dollar stood at G$206.8 per U.S dollar at end 2018, compared to G$206.7 at end 2017, showing a slight depreciation. However, when compared with the Euro, the British pound, and the Canadian dollar, the Guyana dollar showed some appreciation.

3. Employment and Labor Force Participation

The shortage of skilled labor continued to be a major constraint to economic growth in 2018. The high rate of emigration of skilled labor, together with the low level of expenditure on education of 10 percent (compared to an average of 18 percent in the Caribbean), have contributed to significant gap in skilled labor. In addition, the female labor participation rate fell to 41.6 percent in 2018 from a level of 43.6 percent in the previous year (Table 4).

Table 4. Guyana: Population and Labor Indicators (2017)
(In percent)

Subject	Indicators	
Population and labor force	Share of adult population with advanced educatioı	5.4
	Labor force participation rate	56.0
	Labor force participation rate (men)	68.9
	Labor force participation rate (women)	43.6
	Labor force participation rate (youth)	50.2
Employment	Employment-to-population ratio	49.2
	Employment-to-population ratio (men)	62.1
	Employment-to-population ratio (women)	37.0
Unemployment	Unemployment rate	12.0
	Unemployment rate (men)	9.9
	Unemployment rate (women)	15.3
	Unemployment rate (youth)	21.6

Source: International Labor Organization.

4. Governance and Ease of Doing Business

Guyana ranks 134 among 190 countries in the World Bank's ease of doing business indicators. In recent years the Government has stepped up its efforts to strengthen governance and facilitate the ease of doing business. The Government has taken a number of measures to fight corruption, consistent with the United Nations Convention against corruption. These measures include the creation of the Financial Intelligence Unit (FIU) and the Specialized Organized Crime Unit (SOCU), as well as the passage by Parliament of the State Recovery Act (2017) and the Protective Whistle Blower Act (2018). In the area of asset declaration, the recently reestablished Integrity Commission has received declarations from over one-half of the 1,300 persons that were required to declare assets in 2018-19.

In preparation for oil production and export, the Government has strengthened the transparency and accountability in the extractive sector. The Government has published an Extractive Industries Transparency Initiative (EITI) with recommendations that include the establishment of an open database for EITI, reporting EITI data at project level, improving the accuracy and comprehensiveness of production and export data, public disclosure of mineral agreements, public disclosure of the register of licenses, the restructuring of the Guyana Geological and Mines Commission (GGMC) to improve efficiency, use of credible and audited financial statements for assessing payments and revenues to the Government, and the waiving of legal confidentiality restrictions.

The Government has also taken steps to reform its procurement system, in anticipation of the scaling-up of public spending in the near term. The authorities created the National Procurement and Tender Administration Board (NPTAB) to administer the procurement system, and the Public Procurement Commission (PPC) to regulate the system. The reforms include setting aside 20 percent of procurement to small businesses, registration of bidders, debarment procedures for unreliable contractors, and publication of bids and tenders.

5. Social Indicators

The provision of basic social services in Guyana is comparable to the rest of the Caribbean, with the exception of health services. Almost 98% of the population has access to clean water, compared to a median of 95 percent for the region. Similarly, about 83 percent of the population has access to adequate sanitation, just above the median of 82 percent for the Caribbean. On the other hand, the infant mortality rate (31.3 per 1,000) and life expectancy (66.8 years) compare unfavorably with figures of 12.1 per 1,000, and 74.5 years, for the region as a whole.

The quality of Guyana's human capital is lower than the median for the Caribbean. The World Bank has estimated that the human capital index (HCI) for Guyana is 0.49, which is just below the HCI of 0.50 for the Caribbean. The enrollment at primary and secondary school is high, but the quality of education as measured by the performance at the Caribbean Examination Council examination is lower than the average for the Caribbean. The level of human capital is also negatively affected by the high rate of emigration. A recent IDB report has estimated that Guyana has the world's seventh highest rate of emigration, compounded by the fact that most of the emigrants are well educated.

6. The Public Sector

a. Introduction

A comprehensive analysis of economic developments in Guyana requires an in-depth analysis of the role and activities of the public sector, given its control of financial and other resources, the relative weight of its expenditures within the economy, its central role in employment, and its ability to determine and implement overarching economic policies. This review provides information on the institutional coverage of the public sector and the evolution of employment in the sector. The review also contains an analysis of the financial operations of the central government, which is the institution that performs the core activities of the public sector. In this connection, the review examines the sources and uses of resources of the central government as well as the supplementary sources of financing government operations. A brief review of the public sector debt is also conducted.

b. The composition and size of the public sector

The nonfinancial public sector in Guyana comprises a total of ninety entities, including government ministries, local government agencies, statutory bodies, and the non-financial public enterprises (NFPEs). The NFPEs include the Guyana Sugar Corporation (GUYSUCO), Guyana Oil Company Limited (GUYOIL), Guyana National Shipping Company (GNSC), Guyana Power & Light (GPL), the Guyana Rice Development Board (GRDB), the Rice Milling Complex (MARDS), the Guyana Post Office Corporation (GPOC), the Guyana National Printers Limited (GNPL), and the National Insurance Scheme (NIS). The NFPEs, as a group, play an important economic role, particularly in production, employment, and exports.

According to the 2012 national census, the government remains the single largest employer in the economy, employing 22 percent of the labor force in 2012. Estimates of the cost of wages and salaries paid to government workers are shown in Box 1.

Box 1: Indicators of the Cost of the Public Service in Guyana			
	2014	2016	2018
Wages & Salaries as a percent of GDP	7.2	7.4	8.0
Wages & Salaries as a percent of Revenues	34.8	31.8	32.1
Wages & Salaries as a percent of Expenditures	25.1	24.9	25.7

Source: Ministry of Finance Budget Estimates

Recent data compiled by the Guyana Bureau of Statistics (BOS) show that the public sector employed a total of 37, 280 persons in 2018. Of this total, the majority, or 26,354 individuals were employed by the central government. These totals compare with employment levels in 2014 of 31,097 and 17,109 in the public sector and central government, respectively. The evolution of employment in the public sector reflects a rebound in employment levels in the central government following the decade of 1990's when adjustment policies were put in place to improve the overall financial performance of the public sector. In contrast to the recent trend which shows increased employment levels in the total public sector, since 2016 there was a reduction in employment levels in the rest of the public sector (the public sector excluding the central government), which is explained by the program of phased retrenchments and lower recruitment levels conducted by the Guyana Sugar Corporation (GuySuCo) in the context of a restructuring program.

c. Revenue receipts of the Central Government

The operations of the government are primarily funded with the receipts from a tax system that incorporates both direct and indirect taxes. Taxes levied on income, profits, and wealth of households that are attributed to individuals or corporations are generally considered to be direct taxes. Indirect taxes are generally those taxes levied on production, extraction, and the sale or transfer of goods and services. Also included in indirect taxes are taxes levied on the use of goods and on the performance of certain activities.

Table 5: Central Government Revenue by Type
(In percent of GDP)

Revenue Item	2014	2015	2016	2017	2018
Grand Total	22.9	24.5	24.5	26.2	26.9
Tax revenues and Duties	21.0	21.4	20.7	22.3	24.1
Income Taxes	8.1	8.3	8.4	9.1	9.7
Company	4.7	4.7	4.7	5.5	5.7
Personal	2.8	3.0	3.1	2.9	3.2
Self-Employed	0.6	0.5	0.6	0.7	0.8
Taxes on Property	0.4	0.5	0.4	0.5	0.6
Property Tax	0.4	0.5	0.4	0.5	0.6
Taxes on Production and Consumption	--	--	0.2	--	--
Consumption	--	--	0.2	--	--
Value-Added Taxes	5.9	5.4	5.0	5.7	6.0
Excise Taxes	4.4	5.0	4.3	4.5	5.0
Taxes on International trade	2.2	2.1	2.3	2.5	2.8
Other, incl. Non-Tax Revenue	1.9	3.1	3.8	3.9	2.8

Source: Ministry of Finance Budget Estimates.

Company taxes yielded more revenues than receipts from personal taxes on a consistent basis and deserve special attention. Income tax receipts from companies showed a marked improvement during the 2014-2018 period, which can be traced to a general improvement in tax administration. Measures were ramped up in 2018 when the Guyana Revenue Authority (GRA) was restructured to provide more efficient service to large tax-payers, enable electronic tax filing and strengthen regional tax offices. In addition, the implementation of a tax amnesty in 2018 was highly successful in collecting large amounts of tax arrears. A notable achievement of this tax amnesty was the collection of corporate taxes equivalent of about 0.9 percent of GDP.

While indirect taxes as group are a more important source of revenues than direct taxes, receipts from the individual indirect taxes were less buoyant than those from income taxes during the period 2014-2018. The main indirect taxes are the value added tax (VAT), excise taxes, and taxes on international trade. During the period under review, revenue receipts from the VAT were sustained at about 5-6 percent of GDP despite reforms in 2016 which reduced the tax rate from 16 to 14 percent while broadening the tax base to include electricity and water consumption. Other reforms made to the structure of indirect taxes included the replacement of the consumption tax, the purchase tax, the hotel-accommodation tax, the telephone tax, the service tax, and the entertainment tax by the VAT. Excise taxes grew marginally from about 4 percent of GDP in 2014 to 5 percent of GDP in 2018 as a result of increases in fuel excises which were raised as international oil prices declined.

d. Current expenditures of the Central Government

Between 2014–2018, government expenditures, comprising current and capital expenditures, accounted for a growing share of the economy, increasing from 29 percent of GDP to 35 percent of GDP. Capital expenditures declined marginally in relation to GDP but remained fairly stable between 2014 and 2018. Taking account of this development, the increase in the ratio of government expenditures to GDP was attributed exclusively to current account activities which grew from about 21 percent of GDP in 2014 to approximately 25 percent in 2018.

The allocation of budgetary resources across competing expenditure demands is a reflection of the government's framework of priorities. Within the envelope of current expenditures, the most significant component of financial resources is dedicated to paying wages and salaries, followed by the use or purchase of goods and services (Table 6). The combined weight of these two components exceeds the total weight of resources dedicated to all other government activities. Wages and salaries accounted. on average, for 33 percent of current expenditures during the 2014-2018 period, while the use of goods and services comprised, on average, 28 percent of these expenditures. The growth of these two components is also noteworthy. Wages and salaries grew from 7 percent of GDP in 2014 to 8 percent of GDP in 2018, reflecting increases in the wage and salary scales for civil servants starting in 2018 after many years of stagnant wages. Over the same period, spending on goods and services grew to slightly over 6 percent of GDP partly as a result of expanded services provided to communities, particularly in the interior of the country.

Budgetary transfers are the other significant component of current expenditures. These expenditures, which increased from 4 percent of GDP in 2014 to 6 percent of GDP in 2018, include the payment of subsidies to NFPEs, contributions to local and foreign organizations, and educational subventions. While the NFPEs play an important role in production, employment, and exports, their financial performance as a group has been characterized by large deficits. The central government, which owns and controls the NFPEs, continues to provide large budgetary transfers to these enterprises to support their operations on an ongoing basis. Central government transfers to the NFPEs, which were equivalent to 0.6 percent of GDP in 2014, grew to 1.5 percent of GDP in 2017 and fell slightly to 1.3 percent in 2018.

Table 6: Central Government Current Expenditure

	2014	2015	2016	2017	2018
			(In percent ofGDP)		
Economic Classification					
Wages & Salaries	7.2	7.4	7.4	8.0	8.0
Use of Goods & Services	6.3	6.5	6.4	6.6	6.5
Interest	0.7	0.8	0.8	0.8	0.7
Transfers	3.9	5.1	6.0	5.7	6.4
Social Benefits	1.7	1.6	1.9	2.0	2.2
Other	0.9	0.7	0.8	0.9	1.0
TOTAL	20.8	22.2	23.3	24.1	24.7

Source: Ministry of Finance: Budget Estimate 2017, 2018, 2019.

Significant transfers have been provided to GuySuCo, the public enterprise operating in the sugar industry to cover its financial losses. These transfers have placed a financial burden on the central government budget, diverting scarce resources from other activities. However. as a result of financial resources secured for GuySuCo by the National Industrial and Commercial Investments Limited (NICIL), a special purpose unit set up by the Government, transfers from the Government to GuySuCo declined in 2018. At the same time, the government initiated measures to restructure GuySuCo that targeted a reduction in inefficiencies and placing operations on a financially sound footing. As of end- 2018, progress has been achieved in restructuring GuySuCo in the following areas: the consolidation of some sugar refining operations; the closure of some sugar estates; severance payments to 5,500 displaced workers; and the consideration of offers for the privatization of 3 of 6 sugar estates. At the same time, reforms designed to improve cost efficiency and productivity were introduced across the NFPE sector. These measures have produced improvements in the financial performance of the power utility, GPL, and GuyOil.

e. Central Government capital expenditure

The capital expenditure budget determines the annual limits of public investment expenditures and the allocation of capital resources across economic sectors. The specific objectives of this budget are determined by the multi-year public sector investment program (PSIP) which has, as its major focus, making investments in areas where deficiencies have been identified as impediments to growth and economic diversification. At 8 percent of GDP in 2014, the implementation rate of capital expenditures was considered modest, accounting for 28 percent of total government expenditures. These expenditures declined sharply to around 5 percent of GDP in 2015 as a result of delays in the start-up of important components of the investment program due to a number of significant political developments, including presidential elections (Table 7). This trend was reversed in subsequent years following the implementation of a streamlined project procurement and approval process. As a result, capital expenditures rebounded to over 7 percent of GDP in 2018. Despite this, capital expenditures still account for only about 23 percent of total government expenditures.

Table 7: Capital Expenditure by Sector

	2014	2015	2016	2017	2018
	(In percent of GDP)				
Agriculture	0.8	0.5	0.4	0.4	0.4
Power Generation	0.7	0.1	0.1	0.5	0.4
Manufacturing	0.1	0.1	0.1	0.1	0.1
Construction	2.3	1.5	2.9	3.5	2.7
Transport & Communication	0.3	0.5	0.5	0.5	0.8
Housing	0.6	0.3	0.0	0.0	0.0
Environment and Pure Water	0.8	0.3	0.4	0.5	0.5
Education	0.5	0.3	0.5	0.4	0.5
Health	0.3	0.1	0.3	0.3	0.4
Culture/Youth	0.2	0.0	0.1	0.1	0.1
National Security & Defence	0.1	0.1	0.1	0.1	0.1
Public Safety	0.3	0.1	0.2	0.5	0.4
Administration	0.4	0.2	0.3	0.5	0.5
Financial Transfers	0.2	0.3	0.2	0.1	0.1
Social Welfare	0.5	0.1	0.4	0.3	0.2
TOTAL	8.0	4.7	6.4	7.9	7.3
Of which: foreign financing (G$ billions)	14.9	9.7	15.8	22.2	24.6

Source: Ministry of Finance: Budget Estimate 2017, 2018, 2019

An economic classification of expenditures does not exist, but the allocation of budgetary resources shows that construction activities, mainly of physical infrastructures, is the only economic sector to which financial resources were devoted in significant amounts (Table 7). As a result of this spending pattern, basic infrastructures are relatively well developed, with several transportation projects underway, including roads, bridges, and the upgrading of airports. During 2018, significant resources were also dedicated to improving sea defenses along the coastal areas. Specific deficiencies in the supporting capital infrastructure that remain a barrier to investment in the private sector have been identified. To address these shortcomings, the public investment program has undergone adjustments to target additional construction in areas such as roads, bridges, and sea defenses, plus improvements to the telecommunication networks. At the same time, spending on other economic sectors that provide key services, such as health, education and training (human capital formation) is lagging and compares unfavorably with several Caribbean countries.

f. The Public Sector Investment Program (PSIP)

The PSIP is a framework of developmental objectives identified by the government as priorities for public sector capital expenditures to be implemented in the context of annual government budgets. While the PSIP is the conceptual framework in which the objectives of capital investment are set out, taking into account well-defined and consistent criteria, implementation of these priorities is achieved through the annual capital expenditure budgets which allocate financial resources to various economic sectors and the underlying component projects.

The objectives of the current PSIP are discussed in the 2019 Budget speech and are based on the presentation of the investment program outlined in the official document, the Green State Development Strategy (GSDS). The GSDS is the conclusion of a collaborative effort between the Government and the United Nations Environmental Program (UN Environment) which undertook a consultative process in 2017 to create the GSDS to guide Guyana's economic and social development.

According to the *Green State Development Strategy: Vision 2040*, which will guide national development policies for the next 20 years, the objective of the PSIP is to provide a good quality of life for all citizens of Guyana, based on a sound education and social protection, low carbon development, and to promote new economic opportunities that are sustainable over generations. As identified in the most recent budget speech, for the immediate future, the Government has prioritized public sector investments that focus on the expansion of land, sea and air transport and telecommunications networks across the country. To meet other objectives of the PSIP, investments are to be undertaken that will improve housing, sea defenses, agriculture, water, sanitation and waste management. In addition to the construction of new infrastructure, resources are to be dedicated to maintenance and repairs, and to the modernization of public procurement procedures, which serve as a foundation for improved accountability and effectiveness.

The investment priorities set out in the PSIP for the medium term are particularly important, given the projection of significant petroleum revenues that are expected to accrue to the government in the near future. Within the framework of the GSDS, it is envisaged that the oil revenues will enable the ramping up of spending on infrastructure in order to improve and induce domestic and foreign investment, which is critical to private sector investment and growth. A significant feature of this investment program is that there will also be increased expenditure on education and healthcare to ensure enhancements of the quality of human capital.

g. The Central Government deficit and its financing

Given the operating surplus of the government during the period 2014-2018, the size of the overall deficit is entirely determined by implementation of the capital expenditure program. Starting at around 6 of GDP in 2014, the overall government deficit declined to about 2 percent of GDP in 2015, due to the delay in the start-up of the PSIP, before increasing to 4 percent of GDP between 2016-2018 (Table 8).

The overall deficit is financed by borrowing from both foreign and domestic sources. The foreign borrowing is the result of a peculiar characteristic of the capital expenditure budget in which a significant proportion of the public investment projects is financed by foreign creditors who extend loans to the government of Guyana on concessional terms. The main multilateral and bilateral creditors are the Inter-American Development Bank (IDB), the Caribbean Development Bank (CDB) and China. The International Development Association (IDA), part of the World Bank, and India are also significant foreign creditors. To the extent that these loans partially finance the capital expenditure program, they also reduce the government's reliance on domestic financing. However, despite the central role played by foreign creditors in financing an important portion of the public investment program and, by association, the budget deficit, the major share of the funding of the deficit comes from domestic sources. This financing is mainly from the banking system in the form of Treasury Bills, other government securities, and an overdraft at the central bank.

Table 8: Central Government Operations

	2014	2015	2016	2017	2018
			(In percent of GDP)		
Transactions					
Revenue and Grants	23.1	25.1	25.2	27.6	28.0
Current Expenditure	20.8	22.2	23.3	24.1	24.7
of which: Transfers	3.9	5.1	6.0	5.7	6.4
Interest	0.7	0.8	0.8	0.8	0.7
Operating Balance	2.3	2.9	2.0	3.5	3.3
Capital Expenditure	8.0	4.7	6.4	7.9	7.3
Overall Balance	-5.8	-1.8	-4.4	-4.4	-4.1
Financing	5.8	1.8	4.4	4.4	4.1
Net exernal financing	1.6	0.8	1.1	1.2	1.0
Net domestic financing	4.1	1.0	3.4	3.2	3.1
Total Public Sector Debt	51.9	50.1	50.7	51.4	52.9
External	39.5	35.7	33.2	34.4	33.9
Domestic	12.3	14.4	17.6	16.9	19.0

Source: Ministry of Finance: Budget Estimate 2017, 2018, 2019

h. The stock of public sector debt

Total public sector debt, comprising both external and domestic debt, exceeded 50 percent of GDP during the 2014-2018 period. This debt comprised the debt accrued by the central government and debt of the NFPEs that is guaranteed by the central government.

Box 2: Public Sector Debt
(In percent of GDP)

	2014	2015	2016	2017	2018 Prelim.
Total	51.9	50.1	50.7	51.4	52.9
External	39.5	35.7	33.2	34.4	33.9
Domestic	12.3	14.4	17.6	16.9	19.0

Source: IMF

The external debt is owed mainly to multilateral creditors such as the IDB, the International Development Association (IDA) of the World Bank, and the CDB. The external debt has a long maturity profile and low interest rates, reflecting the concessional terms on which the loans were extended.

Based on the trend that started in 2015, domestic debt obligations continued to rise, reaching a level of 19 percent of GDP at the end of 2018. While the larger share of this outstanding stock of domestic debt is comprised of bonded debt (G$80 billion at end December 2018) which is equivalent to 10 percent of GDP and consists of Treasury bills, debentures, bonds and the CARICOM loan,[1] the government has also maintained an overdraft on its deposit account with the Bank of Guyana since the final quarter of 2015. At end December 2018, this overdraft stood at G$55.2 billion (7 percent of GDP). While this overdraft could, in principle, be costly to the Government in terms of potential interest charges, in fact, the Bank of Guyana does not levy any charges on this overdraft facility, justifying this practice on the fact that, over time, the Government has maintained net deposit balances with the central bank. Nevertheless, this practice adversely affects the finances of the Bank of Guyana and understates the true cost of government borrowing. In addition, in the absence of any borrowing-costs associated with this form of borrowing, the Government has an incentive to make unlimited use of the overdraft facility to meet its borrowing needs. Rationalization of the Government's debt obligations would suggest that the government should settle its overdraft balances at the central bank and rely on the issuance of Treasury Bills for future government cash flow management.

With regard to the excessive reliance on short-term instruments, such as Treasury bills, as a source of fiscal financing, the government has indicated that it is committed to developing longer-term domestic debt instruments in the form of bonds that would provide a more stable and predictable source of government financing and would meet the demand for longer-term instruments from various financial institutions, The development of long-term domestic debt instruments would also facilitate establishing a clear distinction between financial instruments issued in support of fiscal policies and those issued in association the implementation of monetary policies.

7. The banking system

a. *Introduction*

The banking system comprises a central bank and six commercial banks. Local business groups and their affiliates hold majority shares in three domestic banks. Of the three foreign banks, two are branches of a Canadian and an Indian bank, while one is the local subsidiary of Republic Bank of Trinidad and Tobago. At the end of 2018 the commercial banks operated 46 offices and branches and their combined assets totalled G$503 billion, or about US$2.5 billion.[2] In that year the banks' return on assets ranged from 1.2-2.8 percent, while the return on equity varied between 7

[1] This is a loan that financed the construction of the building housing the CARICOM Secretariat.
[2] Throughout this section the source of indicators on the banking system is the Bank of Guyana 2018 Annual Report and its Quarterly Reports for 2019. All are available on the bank's website https://www.bankofguyana.org.gy/bog/

percent and 17 percent (Table 9). In their latest annual reports two banks (one local and one foreign-owned) indicated that the number of employees totalled 151, and 681, respectively.

b. Developments in the banking system

At about 50 percent of GDP since 2012-2014, the money supply has remained broadly in line with the trajectory of the economy. After a period of rapid expansion in 2013-2015 when domestic credit grew by an average of more than 20 percent a year, there was a slowdown in the following two years as some banks restrained credit growth to the private sector in response to high levels of nonperforming loans (NPLs). Except for a hiatus in 2017, credit to the government rose steadily during 2013-2018 (Table 10).

High liquidity and low domestic debt have contributed to a prolonged period of low interest rates. At the end of 2018 the rate on the benchmark 3-month treasury bill stood at 1.5 percent, almost unchanged from levels in 2012-2014. Similarly, the rate on savings deposits has remained unchanged at about 1 percent since 2014. The average lending rate stood at 10 percent at end-2018, 1 percentage point lower than in 2012-2014.

c. Bank of Guyana

In the five-year period ending 2018 the main financial developments in the central bank were a fall in foreign assets, a marked increase in deposits of banks and other institutions, and a build-up in the overdraft of the government. Foreign assets reached US$880 million in 2012. However, they fell to about US$700 million at the end of 2014 and $530 million at end-2018. Evidencing the liquidity in the banking system, bank deposits in the central bank in excess of the regulatory requirement amounted to $82 billion at the end of 2018. This excess was equivalent to 91 percent of required deposits, and it reflects several factors, including a dearth of suitable investment opportunities and a shortage of treasury bills or similar instruments for short term liquidity management.

Table 9: Summary Profile of Banks in Guyana-2018
(millions of Guyana dollars)

	Baroda	Citizens	Demerara	GBTI	Republic	Scotia
Total assets	**14,437**	**50,482**	**71,570**	**107,545**	**168,183**	**77,001**
Loans (net of provisions)	5,037	25,527	26,836	43,347	69,748	49,167
loans to real estate	1,410	11,032	7,734	12,424	25,438	25,070
loans to related parties	…	838	313	2,906	498	8,219
nonperforming/impaired loans	1,489	4,035	1,598	12,424	3,938	3,543
ratio nonperforming/total loans (percent)	30	16	6	29	6	7
provisions for nonperforming loans	344	1,519	926	3759	483	786
ratio provisions/nonperforming loans (percent)	23	38	58	30	12	22
Treasury bills and other securities	2,472	4,324	26,870	33,619	15,694	6,872
Cash and balances due from banks 1/	3,847	3,755	5,144	9,889	23,900	12,517
Balance with the central bank 1/	2,542	11,651	9,895	11,447	16,187	7,247
Other	539	5,225	2,825	9,243	42,654	1,198
Liabilities and capital	**14,438**	**50,482**	**71,570**	**107,545**	**168,183**	**77,001**
Deposits	11,404	40,903	58,200	89,286	144,655	58,703
Government/Public sector	…	4,189	…	13,989	32,355	776
Related parties	…	13,071	3,861	3,844	3,361	50
public/total deposits (percent)	…	10	…	16	22	1
Private and other deposits	…	36,714	…	75,297	112,300	57,927
Other liabilities	198	935	1,539	2,087	3,364	2,721
Equity/Capital	**2,836**	**8,644**	**11,831**	**16,172**	**20,164**	**15,577**
Capital ratios						
Capital to risk-weighted assets	…	31	36	25	26	38
Capital to total assets	20	17	17	15	12	20
Net profit after tax	**110**	**602**	**2,041**	**1,446**	**3,134**	**2,525**
Net interest earnings	368	2,245	3,166	3,842	7,404	5,165
on Loans, deposits, and investments	678	2,726	3,932	4,609	7,974	5,389
on deposits	-310	-481	-766	-767	-570	-224
Other income (net)	-258	-1,643	-1,125	-2,396	-4,270	-2,640
Other indicators						
Branches, including headquarters	2	6	7	13	13	5
Employees	…	151	…	…	681	…
Shareholders	…	95	…	1,800	1,371	…
Customers	…	52,708	…	…	…	…
Return on average equity (ROE)	…	7.1	17.3	9.2	16.5	…
Return on average assets (ROA)	…	1.2	2.8	1.4	2.0	…

Sources: Annual reports and financial statements of banks; Bank of Guyana.
1/ Some banks include balances in excess of required central bank deposits in balances due from banks.

Table 10: Guyana: Financial Sector Indicators
(billions of Guyana dollars)

	2012	2013	2014	2015	2016	2017	2018
			Bank of Guyana				
Total assets	**259.5**	**234.7**	**208.0**	**188.8**	**220.4**	**223.6**	**220.3**
Foreign assets	175.0	160.2	137.5	123.6	123.2	120.6	110.2
Total deposits	142.8	126.8	87.0	68.6	110.1	109.9	124.5
Banks	45.2	47.5	47.0	54.6	67.3	62.0	73.9
Government deposits	57.3	52.1	21.4	--	--	--	--
Other deposits	40.3	27.2	18.6	14.0	42.8	47.9	50.6
Government overdraft	--	--	--	2.3	21.3	26.5	55.2
Capital and reserves	15.4	10.0	13.4	12.2	11.3	8.3	2.8
			Commercial Banks				
Total assets	**378.1**	**413.6**	**421.8**	**442.9**	**467.3**	**471.1**	**503.4**
Annual percentage change	*15.2*	*9.4*	*2.0*	*5.0*	*5.5*	*0.8*	*6.9*
In percent of GDP	*64.9*	*67.4*	*66.4*	*67.1*	*64.6*	*63.3*	*62.5*
Loans to private sector 1/	155.4	178.8	196.7	208.2	213.2	218.5	229.2
% change	*21.4*	*15.1*	*10.0*	*5.8*	*2.4*	*2.5*	*4.9*
Business	80.1	91.2	101.7	101.7	102.0	103.5	108.4
Individuals	26.8	30.9	30.9	34.9	36.7	37.1	39.0
Mortgages	48.5	56.7	64.1	71.6	74.5	77.9	81.8
% change mortgages	*20.6*	*16.9*	*13.1*	*11.7*	*4.1*	*4.6*	*5.0*
Lending to public sector	73.0	82.0	63.4	65.7	68.1	66.5	72.3
Total resident deposits	306.7	330.1	329.8	343.8	361.3	351.8	378.8
Private sector deposits	233.5	242.9	247.4	250.6	259.5	267.1	284.5
% change	*12.0*	*4.0*	*1.9*	*1.3*	*3.6*	*2.9*	*6.5*
Deposits of nonbank fin institutions	18.1	26.0	22.7	25.0	28.4	34.0	35.5
Public sector deposits	55.1	61.2	59.7	68.2	73.4	50.7	58.8
Capital & reserves	45.1	52.4	60.0	67.0	74.0	79.8	83.6
			Banking System				
Foreign assets (net)	**214.3**	**197.0**	**195.2**	**178.6**	**179.9**	**177.0**	**168.1**
Net domestic credit	**99.0**	**123.8**	**154.9**	**184.6**	**198.9**	**219.3**	**253.7**
% change	*5.9*	*25.1*	*25.1*	*19.2*	*7.7*	*10.3*	*15.7*
Private sector	161.6	185.1	202.0	214.5	219.1	224.2	235.6
% change	*20.0*	*14.5*	*9.1*	*6.2*	*2.1*	*2.3*	*5.1*
Public sector	-44.9	-36.1	-25.8	-6.4	6.9	28.1	54.8
Government	-0.6	16.7	28.3	56.3	78.1	79.6	103.7
Rest of public sector	-44.3	-52.8	-54.1	-62.7	-71.1	-51.5	-48.8
Money and Quasi-Money	**301.8**	**313.4**	**329.6**	**334.5**	**351.0**	**367.2**	**394.9**
In percent of GDP	*51.8*	*51.0*	*51.9*	*50.7*	*48.5*	*49.3*	*49.0*
% change	*11.5*	*3.8*	*5.2*	*1.5*	*4.9*	*4.6*	*7.5*
GDP (billions of G$)	582.7	614.1	635.3	660.2	723.6	744.6	805.7

Sources: Bank of Guyana, IMF.

1/ Includes mortgage loans. Source: Bank of Guyana Statistical Bulletin Table 2.10(b).

The central government position in the central bank shifted from deposits of $21 billion at the end of 2014 to an overdraft of $55 billion at the end of 2018. In September 2019 the overdraft had risen to $69 billion. In its audited accounts and statistical reports, the bank classifies the overdraft as a negative deposit. If this lending were classified correctly as an asset, the bank's assets and liabilities would be adjusted by $55 billion or 6.8 percent of GDP at the end of 2018. The IMF has recommended that the overdraft be eliminated through an issue of treasury bills.

d. Commercial banks

Commercial banks experienced a period of strong credit growth in 2012-2014. Lending for real estate was particularly robust, rising by 21 percent in 2012 and 15 percent a year in 2013-2014. Since then, and particularly in 2016-2017, banks appeared to have entered a period of consolidation, as some took steps to reduce NPLs and strengthen credit management. The growth in real estate lending fell to 4-5 percent a year in 2016-2018, and the ratio of this category to total loans stood at 38 percent at the end of that period. Lending to business was almost stagnant in 2014-2017 before a modest upturn in 2018. Over the same period deposit growth also slowed, averaging 2½ percent a year, before picking up in 2018.

e. Risks [3]

The central bank view is that commercial banks are well-capitalized, liquid, and profitable.[4] **However, banks face a number of risks**. These relate to capital adequacy, NPLs, liquidity and low interest rates, and ownership structure. Banks also face climate-related and cyber risks.

Capital

In 2018 the ratio of banks' capital to total assets was 16.6 percent. The ratio of capital to risk-weighted assets (RWA) was 31 percent, well in excess of the minimum regulatory requirement of 8 percent. The IMF has recommended that this requirement be raised to 12 percent.

RWA is calculated by assigning varying risk weights to different types of assets. Loans to (or guaranteed by) domestic or regional governments are assigned a zero weighting. This means that before Barbados's default on its public sector debt in 2019, lending to that country through the purchase of government securities required no supporting capital. At least two banks suffered losses in 2018 related to

[3] This discussion covers banks only, while the discussion of risks in the central bank's annual report covers banks and two nonbank deposit-taking institutions.
[4] Bank of Guyana Annual Report 2018, p.43.

their exposure to Barbados government debt. In light of the fiscal risks faced by many regional governments, the central bank's zero risk rating of government securities should be reconsidered.[5] The zero-risk weighting for lending to local governments and state-owned entities in Guyana and other CARICOM countries should also be re-examined.

Loan quality

According to the central bank, NPLs are the most significant risk. At the end of 2018 the average ratio of NPLs to total loans was 12 percent.[6] At the individual bank level, ratios ranged from 6-7 percent in two foreign banks to 29-30 percent in two others. Reflecting these differences, provisions against NPLs ranged from 12 percent in the largest foreign bank to 38 percent and 58 percent in two domestic banks.[7] The average for all banks was 29 percent. Sectors contributing most to NPLs included agriculture, construction and engineering, and distribution.

NPLs to the largest borrowers are particularly concerning. The central bank reports that at the end of 2018 the top twenty borrowers accounted for 28 percent of total loans by all licensed deposit-taking financial institutions (LDFIs), however only 59 percent of these accounts were classified as favourable.[8] Proposals being considered by the central bank to address this issue include reducing the regulatory limit on loans to a single large borrower or group from 40 percent of capital to 25 percent.

The high level of NPLs is related to several factors. They include shifts in commodity prices, the loss of markets, and the structural decline in sugarcane production. NPLs are also related to inadequate credit information on borrowers and the heavy reliance by some banks on collateral in making loan decisions. However, liquidating collateral can often be difficult and costly because of a busy court calendar, delays sought by debtors, and changes in collateral values over time. Collateral also influences banks' provisioning. Current regulations allow them to avoid classifying as impaired loans that are past due for up to 180 days, if those loans are "well secured".

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[5] In 2018 the average ratio of public sector debt/GDP in tourism dependent Caribbean countries was 81 percent (IMF Outlook for Latin America and the Caribbean, October 2019). https://www.imf.org/en/Publications/REO/WH/Issues/2018/10/11/wreo1018

[6] At the end of 2014, the latest year for which data are available, the average ratio for the Caribbean region was 10.3 percent.

[7] See the annual reports of the banks available on their websites. The central bank indicators for these measures cover banks as well as two nonbank deposit-taking institutions.

[8] Bank of Guyana Annual Report, p.46. LDFIs include the banks, the New Building Society, and the Hand-in-Hand Trust Corporation.

Ownership structure and relations with related parties

The central bank defines conglomerate risk as "… *the potential that exposures to components of a group of related financial and non-financial enterprises will result in losses due to failures in other components of the group to honour their commitments to the institution*" (Bank of Guyana, 2009). Majority shares in all three domestic banks are owned by business groups or entities controlled by such groups.[9] In the case of one bank the chairman of the controlling group is also the chairman of the board of the bank, and five of nine directors are associated with the conglomerate. In another the chairman is a former chairman of the board of the controlling group. Because of this ownership feature, banks are exposed to related party risk and risks associated with insufficient independence of the board of the bank from that of the conglomerate (IMF, 2018).

At the end of their financial year 2018 lending by banks to their controlling groups was low, averaging about 6 percent of total loans. For the domestic banks that reported on this in their annual reports, deposits of related parties accounted for 6 percent of total deposits, but the range of exposure within this average varied between negligible to about one-third.

Public sector deposits

Public sector deposits account for about 16 percent of all bank deposits. In 2018, some banks held small or negligible exposures, while others held exposures ranging from 16 percent to 22 percent of total deposits. The main risk is that these deposits can be withdrawn rapidly in response to shocks, or to policy changes affecting public entities or the central government. This could affect temporarily the position of some banks.

Climate, cyber, and other risks

Banks in Guyana recognize the presence of climate risk as having the potential to damage their assets and that of customers. Effects could include slowdowns in economic activity, falling earnings, and increases in NPLs. However, this risk has not been discussed adequately in annual reports. To mitigate climate risk, banks have insurance against some losses, and installed offsite backup systems to protect data.

Cyber risk is also not yet included in the risk discussion in banks' annual reports. However, the growth in online banking and payments, as well as the oil-

[9] The groups are Banks DIH Ltd (Citizens Bank), Demerara Distillers (Demerara Bank), and Edward Beharry and Company (GBTI).

driven growth of the economy beginning in 2020, point to the need for risk management frameworks to incorporate this risk explicitly. To date, the main events in this area have been multiple reports of ATM fraud across the country.[10]

Two banks note in their 2018 annual reports that political uncertainty has affected economic activity and reduced lending opportunities.[11] Guyana was downgraded recently in the Fitch Short-be Term Political Risk Index, and the elections in March 2020 could be sharply contested and deepen uncertainty.[12]

Low interest rates present risk to the entire financial system. Current low yields on deposits and government securities are helping lower returns to banks, pension funds, and insurance companies, and could affect financial stability. In addition, low yields provide incentives to invest in other assets that carry greater risk.[13]

f. Conclusion

In 2015-2017 banks entered a period of consolidation following years of rapid growth in lending. However, there were signs of a slow recovery in credit and deposits in 2018. Banks appear well capitalized, but their average return on assets is low. In addition, the banks face several risks, including those of climate, cyber, and political uncertainty.

Addressing these risks requires prompt action from shareholders, management, and regulators. With the economy on the verge of rapid expansion following oil production which began in 2019, a strong, resilient banking system will be essential for preserving confidence, stability, and a balanced economy, by helping sustain growth in the non-oil sectors.

[10] For a description of one of the recent incidents, see https://www.stabroeknews.com/2019/news/guyana/05/15/republic-bank-says-some-customers-hit-by-fraud-on-visa-debit-card/
[11] See 2018 Annual Reports of GBTI and Citizens Bank.
[12] Economist Intelligence Unit, October 2019; https://country.eiu.com/guyana
[13] See Financial Times, 3 November, 2019 "Falling interest rates wreak havoc with US pension system." Available at: https://www.ft.com/content/60c5b80b-b227-405a-9290-0d5f78efa0f7