GOVERNOR’S PRESENTATION OF THE 2004/2005 ANNUAL REPORT

Introduction

Good evening ladies and gentlemen.

This presentation of the Bank's Annual Report is intended to improve public understanding of the role of the ECCB; to ensure transparency with respect to our operations and to raise the level of awareness of corporate governance throughout the currency union.

The Bank's major objectives are monetary and financial sector stability. These are intended to facilitate the economic development of the member countries.

In the pursuit of monetary policy, the ECCB targets a fixed exchange rate. The Bank aims to ensure that the value of the EC dollar remains stable, so that the currency can maintain its purchasing power enabling consumers and investors to conduct business with confidence.

Financial stability is a fundamental prerequisite not only for the preservation of the value of the currency but also for the facilitation of economic development.

It is for this reason that the ECCB has assigned a high priority to this issue, ranking it immediately after exchange rate stability. Regulation and supervision of the banking sector as well as the development of the money and capital markets are key components of financial stability. Ensuring that financial institutions remain sound and operate within prescribed guidelines, allows the public to deposit their money, knowing that their assets are safe, while the development of money and capital markets serves to increase the avenues for investment.

ECCB Headquarters, St Kitts, 30 June, 2005

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Governance Structure

The operations of the Bank are effected in the countries through a three-tier governance structure. At the apex of the system is the Monetary Council, comprising the Ministers of Finance who, as elected representatives, are accountable to the people in their respective member countries. It is the Council to which the management of the Bank must report on money and credit conditions; and it is the Council that appoints the Board of Directors, whose responsibility is policy and administration.

In an effort to improve transparency in the Bank's operations, the Monetary Council provides, monetary policy briefings to the cabinet and the legislature. Following each Council meeting, communiqués and reports are issued and press briefings conducted.

Given our multi-state arrangement, it is logistically difficult for the Central Bank to report to the legislature, as is the norm in a single state arrangement. Council members therefore function in two roles. As the monetary policy decision makers, they provide directives and guidelines to the Bank on monetary and credit conditions. They also function as Ministers of Finance in their respective territories with cabinet and legislative responsibilities. In this capacity they are required to ensure that laws providing for the safety and soundness of the financial system are passed in parliament and fully implemented.

This framework provides the link between monetary and fiscal policy and calls for close coordination at both the domestic and currency union levels. As members of the ECCB, the participating governments have agreed on financial targets and economic objectives that support the monetary policy objectives of the Currency Union.

It is in this context that the ECCB works closely with member governments in the alignment of relevant policies geared at maintaining the integrity of the exchange rate. These policies are intended to influence the balance of payments outcome which represents the net foreign reserves of the region. In addition, such policies target fiscal and debt sustainability issues of the member countries of the currency union.

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Challenges

Given that the Bank operates in a multi-state economic environment, issues impacting the economy of the member countries have implications for the execution of its mandate.

In the case of the external environment, the world economy, particularly the US, performed well, and had a positive impact on the performance of the domestic economies. Growth averaged 3.9 per cent in 2004 for the ECCU, as compared with 3.5 per cent in 2003. Tourism was the main driver of this growth with increased visitor arrivals and expenditure in both stay over and cruise categories. The relative movement in the major currencies, the dollar, euro, yen and sterling, with the dollar depreciating against the others contributed to the region becoming a more competitive tourism destination during this period.

For the period under review the region's economy was also influenced by:

- the significant increases in the price of oil and other commodities such as building materials, resulting from the rise of China as an economic power. That country's demand for such commodities is presenting significant challenges to regional economies.

- The continued implementation of the new trading arrangements, including the WTO, FTAA and EPA is reducing the viability of traditional exports.

In the domestic environment, the mismatch between the availability of resources and the expectations of the population, manifested itself in fiscal imbalances and increasing debt obligations. Activity geared towards the establishment of the CARICOM Single Market and Economy (CSME) gathered momentum. In response, discussions are ongoing at the highest governmental levels to revise the OECS Treaty to establish an economic union, with a view to accessing the CSME as a block.

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The Bank's Performance

During the fiscal year, the Bank achieved its main objectives of monetary and financial sector stability. The exchange rate peg of the EC dollar was maintained at EC$2.70 to the US dollar, while the financial system remained sound. The ECCB Agreement 1983 mandates that the foreign reserve backing of the currency must be at least 60 per cent of demand liabilities. This was achieved with the foreign exchange backing at 31 March 2005 being 96.4 per cent.

In executing its mandate the Bank paid close attention to:

i addressing any gaps in the financial system that would create undue exposure and risk to the system; and

ii Deepening the dialogue with the general public on issues impacting the region.

To this end several initiatives were undertaken:

- The Bank developed a risk assessment model for the banking system to form the basis for an early warning signal. The model is used to stress-test institutions and the financial system. The results of these tests help to establish risk profiles for the institutions and to inform their risk management policies.

- Efforts were made to promote enhanced corporate governance practices among banking sector institutions. The objective is to create a regulatory partnership between the ECCB and the regulated institutions. To this end the Bank has circulated for discussion with stakeholders prudential guidelines on corporate governance. The Bank has undertaken, at the request of the regional community, to coordinate the development of corporate governance principles in the area.

- The Bank also initiated enhancements to the payment system in the ECCU to make it more effective, efficient, reliable and secure.

- Coordination of the Structural Adjustment and Technical Assistance Programme (SATAP) for the member territories. This programmme was designed to achieve fiscal consolidation and to bring about convergence towards the fiscal benchmarks agreed upon by the Monetary Council.

- The Bank sought to engage the public in dialogue through the use of video-conferencing technology, in keeping with the Bank's policy of accountability and transparency.

The ECCB's financial objective for the year 2004/2005 focused on expenditure reduction, in an attempt to contain total expenditure in line with income from foreign reserve assets.

The year was particularly challenging, as there was a sharp reduction in income from the Bank's investment portfolio due to the unfavourable performance of the US Bond market in an increasing interest rate environment. The higher than anticipated reduction in income forced the introduction of several cost cutting measures.

Total income of $55.8m fell below the budgeted amount of $61m. The cost saving measures implemented during the year contributed to a lower total expenditure of $54.5m compared with a budgeted amount of $58.4m. This resulted in a realised net profit of $1.3m compared with a budgeted position of $2.8m.

Total assets of the Central Bank amounted to $1.8 billion compared with $1.7 billion at the end of the previous fiscal year, an increase of 6.5 per cent. The increase was mainly due to an expansion of foreign reserve assets.

The external environment and domestic circumstances of the past year have provided many challenges to our economies and to the Bank's operations. Concerted action to meet these challenges must continue in the year ahead if we are to ensure the stability of our currency and the safety and soundness of our financial system.