Steady as she goes

INTERVIEW WITH HÉCTOR VALDEZ ALBIZU
GOVERNOR, CENTRAL BANK OF THE DOMINICAN REPUBLIC

HÉCTOR VALDEZ ALBIZU
is the Dean of Central Bank Governors of the Americas. During his 18-year tenure (1994-2000 and 2004-present) of continued macroeconomic stability, the Dominican Republic registered the highest average rate of growth in the Americas, more than tripling the size of per capita GDP. He is a graduate of the Universidad Autónoma de Santo Domingo (UASD), the Institute of Social Studies of Chile's Universidad Católica and the IMF's Institute of Advanced Studies.

At a time when Latin American and Caribbean economies are struggling to adjust to the downturn in China and the continued impact of the financial crisis in the EU and the United States, in contrast, the mood in the Dominican Republic is one of quiet confidence in the future.

"The governor of the Central Bank of Mexico recently told me that we're laughing while our neighbours are crying," says Central Bank governor Héctor Valdez Albizu, adding: "The big risk to the region comes from the fall in commodities prices: Latin America now faces the conditions that will reduce growth."

Mr Valdez Albizu has worked at the Central Bank for most of his career, rising through the ranks after he joined in 1970 to become governor in 1994, a post he has occupied continuously since then, aside from a four-year break between 2000 and 2004. A veteran political insider, he is one of the main architects of the Dominican Republic's economic reforms of the last two decades, and offers unique insight into his country's success story and what sets it apart from its regional neighbours.

"Generally speaking, there are two kinds of economy in Latin America and the Caribbean: those focused on exporting raw materials and commodities, and those like ours, which while small, are open, flexible, and diversified," he explains.

After growing by an average of 4.3 per cent between 2004 and 2011, the economies of Latin America managed just 2.6 per cent in 2015. "Brazil has had to raise interest rates sharply to contain inflation and is unlikely to beat its 2013 growth of 2.3 per cent. Mexico, although less commodity-driven than South America, is unlikely to do much better. The data suggests that Chile is growing at its slowest rate for four years. Even Peru, along with Panama, the region's star economy of the past decade, is feeling the pinch," says Mr Valdez.

"Last year, Brazil went into recession, while we enjoyed 7 per cent growth; the previous year was 7.3 per cent. The growth in our economy has not been affected by the financial crisis in the US or China's slowdown," he continues, noting that in 2015, tourism, the economy's biggest sector, brought in US$6.5 billion in foreign earnings, while remittances from Dominicans working abroad amounted to US$4.5 billion. In total, the Dominican Republic's foreign exchange earnings from tourism, remittances, foreign investment, and exports of goods and services for last year exceeded US$23 billion, or 35 per cent of the total GDP, says Mr Valdez. The country's economy is worth around US$61 billion. Inflation remains at 2.3 per cent, below the 4 per cent target set by the government.

Mr Valdez says neither is he overly concerned about fall-out from the situation in Venezuela, even though its heavily oil-dependent economy has been sent into a tailspin by the collapse of crude prices, starving the country of cash to pay for domestic energy subsidies and imported goods. With little foreign currency reserves left, the economy is contracting, inflation has soared and the government has resorted to rationing food and other consumer staples.

Under former President the late Hugo Chávez, Venezuela launched the so-called Petrocaribe accord in 2005, seeking to become a low-cost energy provider and win political favour among small island economies heavily reliant on oil imports. Since then, it has drastically cut back that policy.

"Fortunately, the Dominican Republic has a more diverse source of oil imports and will not be hit as hard by the loss of cheap Venezuelan oil," says Mr Valdez. Furthermore, he says, much of the capital flight from Venezuela has landed in the DR's tourism sector.

Looking to the longer term, Governor Valdez believes a solution will be found to the current political stalemate in Venezuela.

Learning the lessons of history

The Dominican Republic learned the lessons of overdependence on commodities during the military rule of the early 1960s. When it emerged from civil war in 1965, successive governments introduced legislation to create an industrial base and to diversify the economy.

By the mid-1990s, having laid the foundations for a reasonably diversified economic base, successive governments began setting up special economic zones that provided the ideal conditions for capital investment by allowing companies within them to effectively operate outside the regular domestic economy.

What the DR also did was embrace globalisation. While many other countries have also done the same since, the Dominican Republic's experience has permeated more deeply, says Mr Valdez.

By the first years of the new millennium, the Dominican economy was stronger than it had ever been: it had enjoyed the fastest economic growth in Latin America since the 1970s, averaging 3.2 per cent annually until 2003. But that year it embarked on the ill-advised bailout of Banco Intercontinental (known as BanInter), the country's second-largest private bank, sparking a crisis that doubled government debt and destroyed the value of the currency.

"A drastic overhaul was needed to restore macroeconomic stability and confidence in the financial sector, as well as to tame spiralling interest and inflation rates," explains Mr Valdez.

In the years that followed, a series of hard-hitting financial reforms and the close coordination between monetary and fiscal policies ushered in a new period of economic growth and a revitalisation in all sectors.

Since then, the country has continued to attract FDI, which has increased by 245.5 per cent over the last decade. "The main factors that have influenced this increase are the country's macroeconomic stability, low inflation and relative stability of the exchange rate and a healthy financial, liquid, solvent and well capitalised system," says Mr Valdez.

"Creating the conditions investors need is not rocket science," he notes, highlighting the impact of continued legislation to improve the business climate, such as an FDI Act that provides the same facilities and guarantees to foreign investors as Dominicans, based on clear rules and regulations, with incentives for investors in different sectors.

"Diversification has contributed to the increase in investment flows," says Mr Valdez. "In 2000, four sectors: electricity, telecommunications, trade, and tourism, accounted for 82 per cent of FDI. Today, the spectrum of sectors has expanded to include real estate, construction, and finance. We're confident that we can now attract greater investment to develop mining and agriculture."

"In addition, ours is a country characterised by long-standing democracy that has provided political and social stability," he adds.

The country also benefits from its location along Caribbean and Central American shipping routes, while it is just three hours flying time from the eastern seaboard of the US. The country has first-world transport infrastructure, with eight international airports and a world-class telecommunications system.

Over the last four years, the DR has also pursued a policy of greater regional integration.

The country's participation in major trade agreements like DR-CAFTA, CARICOM, the Economic Partnership Agreement (EPA) with the EU and others boosts its appeal as an investment destination. In January, the Dominican Republic took over the rotating presidency of the Community of Latin American and Caribbean States (CELAC).

Banking sector reform

Since the crisis of 2003-2004, the financial sector has undergone considerable development through the implementation of robust policies that have addressed fundamental weaknesses and greatly improved performance.

New regulations, such as additional capital requirements, have been implemented, says Mr Valdez. Enhanced transparency in the eyes of the general public has been a key step, which has been supported via independent regulatory institutions and the introduction of relevant banking requirements, he explains.

"The principles of the Basel Accords were also adopted so as to enhance the standing of the Dominican Republic's financial sector within the international system: market risk is now highly regulated by ensuring equal treatment to all entities, regardless of capital origin," says Mr Valdez. The periodic review of contingency plans is also employed in order to address the shortage of funds of financial intermediaries.

Measures such as publishing of monthly and annual financial statements, as well as detailed information on the loan portfolios of various financial intermediaries, have improved transparency in the sector and contributed to its health: "We have moved to a model of risk-based supervision, based on high levels of liquidity and solvency, as well as greater international openness."

Elections unlikely to affect growth or investment

Mr Valdez is confident that the presidential elections in May, which current incumbent Danilo Medina is expected to win, will have little impact on the broader economy: "We project that this year, the DR will continue its sound economic performance, growing by its potential level of 5.5 per cent to 6 per cent, and that inflation will converge toward the lower limit of the target range of 4 per cent to 1 per cent at the end of the year, with a current account deficit of around 2 per cent of GDP." Mr Valdez says macroeconomic performance will be driven by the favourable international environment for the country, characterised by improved terms of trade (particularly lower oil prices and higher gold prices) and by the recovery in the United States, the country's main trading partner.

"Continued high levels of exports from industrial free zones, along with tourism, remittances, and foreign direct investment will all continue. Additionally, we expect private sector loans will grow by around 10 per cent, similar to the rate of expansion of nominal GDP, thus contributing to maintaining the growth of private production." F

Whilst its regional neighbours are buffeted by the chill winds of global commodity markets, the Dominican Republic continues to chart its own very different course