

Nancy Lee  
Deputy Assistant Secretary for the Western Hemisphere  
U.S. Department of Treasury  
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Chairman Meeks, Ranking Member Miller, members of the House Financial Services Subcommittee on International Monetary Policy and Trade, thank you for inviting me to testify at this important hearing on the current situation in Haiti. I know the leadership role you and others on this Committee have played on the Haiti issue, and it is a privilege for me to testify before you today.

I returned early this morning from Port-au-Prince, where I had the opportunity to meet with the senior economic team in Haiti, including Finance Minister Baudin, Central Bank Governor Castel, and President Préval's chief economic advisor, Gabriel Verret. I also had the opportunity to meet with the private sector, including heads of several banks and the president of Fonkoze, a remittance provider doing very important work in Haiti. I am pleased to have this opportunity to share my findings with you.

In the immediate aftermath of the January 12 earthquake, efforts were focused on providing urgent lifesaving and life-sustaining relief, as well as restoring essential public services, such as banking and money transfers. We saw an extraordinary level of coordination, both within the United States government and amongst the international community. Now – seven weeks later – we have moved from the emergency phase to the immediate recovery phase, and are about to move into the reconstruction and development phase. Yet the Haitian people will continue to face tremendous humanitarian and recovery needs, and meeting these needs will require a continued massive multilateral effort.

In my testimony, I will provide an overview of the current macroeconomic situation and challenges. I will then discuss Treasury efforts to help Haiti address these challenges through technical and financial assistance, including debt relief.

### **Current Status and Challenges**

Although the earthquake was a catastrophic setback, economic activity is beginning to recover, boosted by extraordinary international assistance and significant financial flows. Pre-earthquake projections pointed to 3.6 percent annual growth in 2010 and annual inflation of 8 percent. Post-earthquake, we can now expect a GDP contraction of at least 10 percent, and a significant increase in inflation, perhaps to 10-20 percent, as a result of severe shortages in particular goods. The economic impact of the earthquake is quite varied by sector and region, and it will take some time to fully understand the nature of these different effects. Today, I will provide you with our best current assessment of the financial sector, public finances, the balance of payments, and the debt burden.

### *Underdeveloped Financial Sector*

In the financial sector, the initial concern following the earthquake was re-establishing the payments systems and ensuring that there was enough physical cash in the system for banks and remittances providers to open. These cash needs were met through the joint effort of the Haitian government, the Haitian financial sector, multilateral institutions such as the IDB, and the U.S. government. The Haitian government was able to pay its employees for January through the hard work of the Ministry of Finance, the Central Bank, and local banks.

Going forward, a key challenge for the Haitian economy will be to create conditions that enable the financial sector to meet more effectively the needs of the economy. Credit growth has lagged for many years due to a combination of risk aversion, periodic shocks, and bouts of economic and political instability. Post-earthquake, this historical risk aversion has only intensified. At the same time, we know that Haitian companies are struggling. Their business activities and revenue streams have been interrupted at a time when they need more resources than ever to rebuild facilities and restore their productive capacity.

### *Fiscal Gaps*

On the fiscal side, the government faces a severe financing gap. The International Monetary Fund (IMF) estimates that domestic revenues may decline by as much as 40 percent due to the shock to economic activity and international trade. This is compounded by the devastating human and capital losses suffered by the revenue collection agency. Meanwhile, government expenditures are likely to increase to fund basic needs and reconstruction. The Haitian authorities have already taken significant steps to restore public financial management systems and procedures, with the support of technical assistance partners. Priority areas have included: basic treasury functions, basic audit service and expenditure monitoring, procurement functions for major purchases, IT services, and taxpayer records, and revenue administration.

### *Balance of Payments Pressures*

With regard to the balance of payments, the IMF has preliminarily identified a potential balance-of-payments gap of \$300 million for 2010, at least \$100 million of which is unfinanced. At the moment, the situation is stable with imports sharply down and remittances up. Haiti is heavily dependent on imports, but with the Port-au-Prince seaport and airport closed, until recently, to most commercial traffic, the volume of imports has declined. Moreover, remittances – which represent some 20 percent of GDP – have increased significantly. Given their economic importance, a smoothly functioning, competitive money transfer system is essential. Evidence of a short-term balance-of-payments improvement is seen in increased dollar deposits in the banks and recent purchases of dollars from the Central Bank to reduce the volatility of local currency movements.

### *Significant Debt Burden*

As you know, these looming fiscal and balance-of-payments pressures come on top of a still-significant Haitian debt burden. A considerable portion of Haiti's external debt was relieved

when the country reached the Heavily Indebted Poor Country (HIPC) Initiative completion point in June 2009; the United States forgave 100 percent of Haiti's bilateral debt at that time. Despite these significant strides, \$1.1 billion in external debt remains. Of this, the multilateral debt stock represents \$825 million, with \$447 million to the Inter-American Development Bank (IDB) alone.

### **Addressing These Challenges**

These challenges are vast and tackling them will require significant resources. Immediately following the earthquake in Haiti, Treasury began working closely with our government colleagues and international partners to support assistance efforts. We have seen an extraordinary level of coordination, both within the U.S. government and vis-à-vis the international community, and both in Washington and on the ground. The United States has demonstrated clear leadership in this endeavor. Treasury has played an important role in the inter-agency and international processes, and will play a role in reconstruction efforts.

Let me briefly describe some of our efforts to address the challenges I discussed and the measures we have taken to help the Haitian people.

#### *Financial Sector Development*

Development of the financial sector is vital for the economy. Treasury is focusing on helping Haiti not just re-start lending, but expanding access to finance to a broader range of households and businesses, especially microfinance enterprises. The rate of credit growth will be a principal factor determining the rate of private sector recovery, as well as job creation. To address these problems during this period of considerable uncertainty about Haiti's economic future, we are working with the multilateral development banks (MDBs) and IMF to develop tools for sharing risk with Haitian financial institutions. Further, many Haitian companies will be viable in the long term if they can weather the immediate drop in sales and surge in reconstruction costs. Accordingly, we are working through MDB private-sector windows to develop solutions to supply much-needed working capital.

To build confidence and reduce risk aversion, extending a sound regulatory framework to a broader range of financial services and institutions is key. We can help Haiti establish supervisory and regulatory frameworks for microfinance, insurance, and pension funds, as well as develop a deposit-insurance scheme.

These kinds of efforts yield disproportionate benefits for job creation. Relatively small investments of donor resources leverage much greater amounts of private finance.

#### *Balance of Payments*

With regard to balance of payments pressures, we strongly supported the January 27 augmentation of Haiti's IMF program by \$100 million, which will help close the projected gap. We commend the IMF for its rapid response. We also strongly support Managing Director

Strauss-Kahn's intention to develop a means of internally financing Haiti's remaining obligations to the IMF, including the \$100 million just approved.

### *Budget Finance*

The combined blow to the fiscal balance of the collapse in revenues and sharp increase in spending will generate substantial budget support needs. Here the MDBs have a central role to play. And we are working in close cooperation with them to provide technical assistance in rebuilding Haiti's revenue system.

### *Debt*

Although most of Haiti's bilateral debt – including debt to the United States – was cancelled in June 2009, Haiti still confronts large debts to multilateral institutions. It is imperative that we cancel this additional debt so that Haiti can proceed on a sustainable path to recovery. To this end, ahead of the G-7 ministerial in Canada earlier this month, Secretary Geithner announced that the United States is seeking commitments by donors to relieve Haiti's debt to the IDB, the International Fund for Agricultural Development (IFAD) and the International Development Association (IDA) in a manner that provides direct and immediate grant support to Haiti. In making this announcement, Secretary Geithner recognized the leadership in Congress, including among the members of this committee, in calling for debt relief for Haiti. At the G-7 meetings, the Secretary was able to work with his colleagues and secure agreement that Haiti's recovery should not be burdened by debt to multilateral institutions.

We must not only cancel Haiti's debt, we must do so in the right way. We believe it is crucial that support for Haiti debt relief not subtract other donor resources that otherwise could have been made available for urgent reconstruction and recovery priorities. In addition, the benefits of debt relief must be available to Haiti now, not slowly materialize over a long time horizon.

With these considerations in mind, Treasury has developed an innovative proposal for achieving the full cancellation of Haiti's multilateral debts that augments resources available for Haiti's recovery. First, we propose transforming the funds provided for debt relief into grant resources for Haiti. Second, we propose converting existing undisbursed loans into grants to guard against adding to debt. Separately, we are also pressing, in the context of on-going negotiations related to the IDB's general capital increase (GCI), for a commitment by the IDB to transfer a portion of its annual net income to finance projects in Haiti. The Treasury proposal is designed to generate resources in both the short and longer term. The proposal therefore attempts to accomplish three critical objectives:

- It creates a substantial pool of upfront grant resources;
- It mobilizes a long-term, continuous stream of grant resources; and
- It, through continued negotiations, works to ensure that the U.S. contribution leverages the maximum amount of multilateral resources.

To be sure, there will be a U.S. component to addressing the cost of providing debt relief for Haiti. And our hope is that we can build on strong, bi-partisan support for Haiti to translate debt

relief operations into new resources that the government of Haiti can apply towards the country's urgent reconstruction and development priorities. We look forward to working with you and your staff on this proposed approach in the days ahead.

### *Treasury Presence on the Ground*

In addition to debt relief efforts, Treasury promptly redirected significant human resources to give high priority to Haiti. We were able to respond rapidly to the tragedy with the deployment of on-the-ground support focused on enhancing human capital – that is, working with the government of Haiti to strengthen budgetary, tax, and financial management. We now have a temporary senior Treasury representative in Port au Prince. And we sent two seasoned technical assistance advisors to help the Central Bank and the Finance Ministry. Our ability to provide resident and intermittent technical advisors quickly is one of Treasury's specific strengths. We leverage skilled and timely assistance from a small resource base.

The first goal of our technical assistance advisors upon arriving in Haiti was to assess the impact of the earthquake on the government's ability to carry out its normal economic functions, including payment of government salaries, implementation of the budget, and ensuring financial system stability. Their next step was to discuss with Central Bank and Finance Ministry officials the assistance that they could provide in the medium term. Based on these discussions, our team has identified several priority areas, the most critical of which are improving the taxation structure, enhancing debt management and issuance capabilities, and enhancing the stability of the insurance and microfinance sectors. Work is already underway, for example, to support the recovery of data and systems housed at the government of Haiti's Directorate General of Taxation (DGI), the equivalent of our IRS. We hope to augment our technical assistance footprint to focus on these areas going forward in order to be able to sustain the effort to help Haiti build capacity to address these challenges.

Since his arrival, our senior Treasury representative has worked on a broad array of financial and fiscal challenges: facilitating the flow of remittances, restarting the payments system, helping to recover the government revenue system, and providing support in crafting Treasury's debt relief proposal. He is also supporting the U.S. Ambassador and advising the Haitian authorities in formulating their reconstruction and development strategy. He will continue to provide assistance in areas where Treasury has a core competency and assist in the deployment of future technical assistance.

### *Reconstruction Architecture*

Another principal duty of our senior representative is to represent the United States, with others, in the post-disaster needs assessment (PDNA), led by the World Bank, Inter-American Development Bank, United Nations, and European Commission. This need assessment, to be completed in mid-March will be fundamental to ensuring that we understand the economic needs for reconstruction and transition. It will provide the cost figures that will underpin donor burden sharing and pledging.

We must ensure that the needs assessment envisions a post-earthquake Haiti stronger, more resilient, and more prosperous than pre-earthquake Haiti and focuses on job creation and recovery of the productive sector to foster economic growth. Following the completion of the needs assessment, a high-level donor conference will be held in New York in late March. Treasury is working closely with our State colleagues on the contours of the needs assessment to ensure it is an effective instrument for defining the use of donor assistance for the most effective purposes.

Regarding the financing of reconstruction activities, Treasury anticipates that a multi-donor trust fund (MDTF) may be able to play a critical role in this effort and in filling the balance-of-payments and fiscal gaps I mentioned earlier. Together with our colleagues at the international financial institutions, we are contemplating a model that builds on the lessons learned from the 2004 tsunami in Aceh: a single facility with a steering committee of donors guided by a government-led national development authority that sets priorities and provides coordination. We are working with the international financial institutions to establish such a fund, which most likely would be administered by the World Bank with a strong project implementation role for the IDB.

## **Conclusion**

In summary, under the strong leadership of the President, the U.S. government has mobilized to help Haiti weather the immediate aftermath of the devastating earthquake. We must now effectively manage the transition from the emergency and immediate recovery phases to the reconstruction and development phase. In close collaboration and coordination with the Haitian government, its people, our international partners, and the rest of our government, Treasury is resolved to play an active role in helping Haiti build an economy and financial system that meets the needs and aspirations of the Haitian people.