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**DIRECTIONS FOR THE REFORM PROCESS
IN THE CARIBBEAN**



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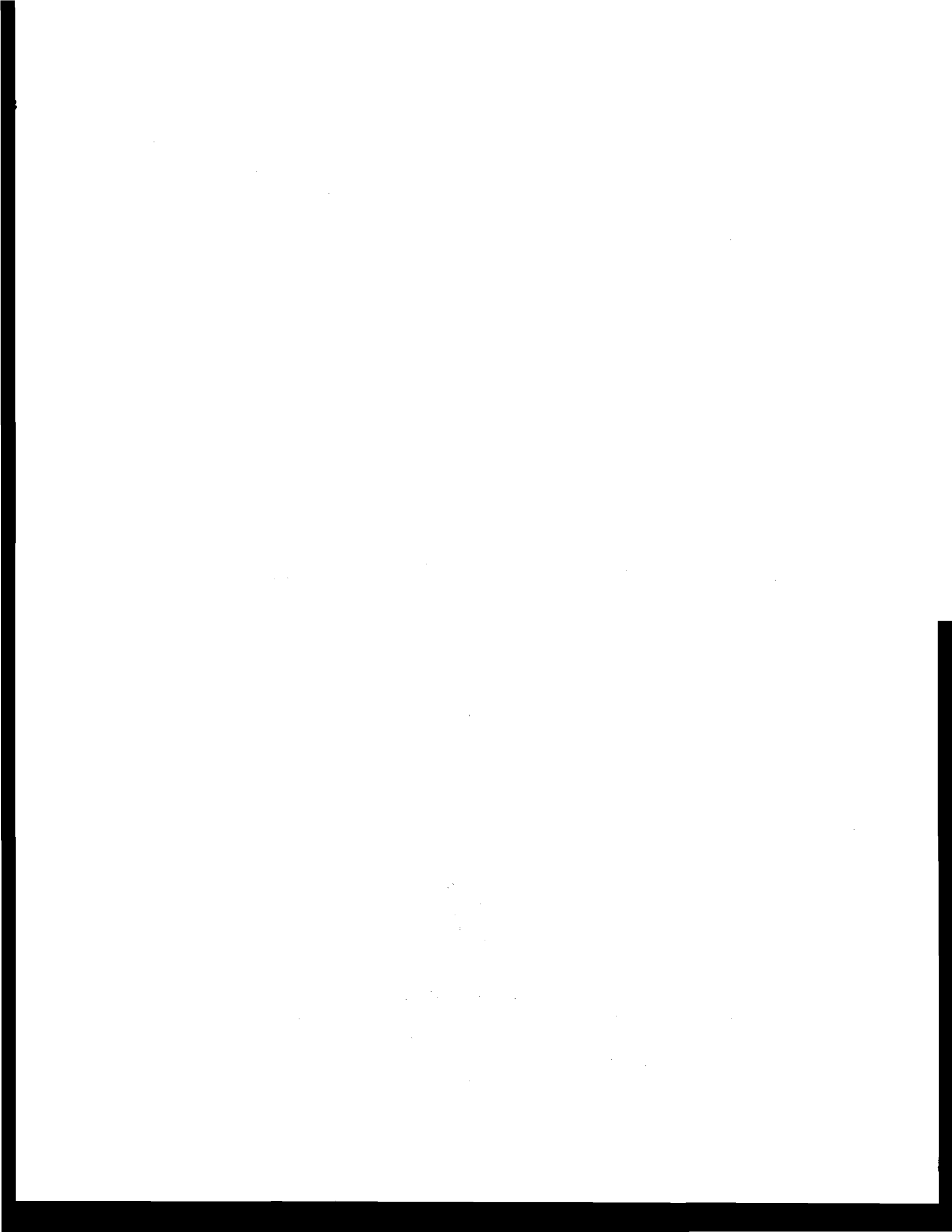


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INTRODUCTION

As we approach the end of the twentieth century, the pace and depth of change in the global economy is staggering. By challenging political boundaries and production frontiers, technology has affected not only economic systems, but political and social systems as well. The globalization phenomenon has created opportunities and challenges, but uncertainty has also increased. There is little consensus on issues of theory and policy and the reaction of some to persistent poverty and increased inequality is a growing sense of cynicism. The conflicting results and recommendations coming out of social enquiry do not help matters. In one school of thought, competition and market forces are seen as a panacea for almost all economic ills. Trade is targeted as the most effective way to increase development and associated with this view is the belief that global economic liberalization will lead to unlimited economic and social benefits that will be broadly shared. Others are not so sure, and raise questions about the ability of the world economy to sustain recent output and trade trends. The economic turmoil in East Asia towards the end of 1997 may have served to confirm some of these fears, but the assumption that the economic performances of a few countries in that part of the world could be easily replicated has not gone unchallenged.

In a global economy involving States with varying levels of economic strength, the impact of liberalization on equality, both among nations and at the national level also remains an open question. The trade-off between equality and economic growth has for long posed a dilemma for governments and the question now has to be approached with new perspectives reflecting the costs of particular kinds of interventions. How to link their economies to global forces responding increasingly to freer markets also raises challenging questions for developing States. In a borderless world, the authority of governments will be increasingly challenged, while the power of the transnational corporations is likely to be reinforced. The trend is already towards larger corporations and larger groupings as new strategies emerge. In some ways competition may be increasing, but the text-book model of perfect competition has little counterpart in practice. The lack of allegiance by transnational operators to any particular state assures neither equity in the sharing of benefits of growth nor unconditional access to technology. Neoclassical assumptions have to be approached with care.

A large number of developing countries, long dependent on the export of primary products and in many cases to preferential markets, have remained marginalised. Within a framework of reduced protection and shifting positions of comparative advantage, a common assumption is that these countries, regardless of size and other constraints, can make a rapid reorientation in resource allocation towards creation of an efficient manufacturing sector with minimal levels of external assistance and with under-developed infrastructures. High store is placed on a transparent trade and investment policy, a stable macroeconomic environment and the stimulating effects of a 'level playing field'. A longer time for adjustment to the new order is the major concession to the less developed players.

Caribbean countries are in various stages of completion with respect to what has been termed 'the first generation' of reforms. They have gone a long way in 'getting the prices right,' but the hard task of institutional reform, institution building and formulating clear long-term policies to facilitate movement to a more competitive plane remains. Though some growth has taken place, it

would be foolhardy to assume that these countries have been structurally transformed and are on the path to self-sustained growth. Poverty and unemployment remain at high levels, while public policy has been impotent in dealing with the problems of underemployment and low productivity. The unsatisfactory returns from expenditures in social sectors, such as health and education, point to the need for fundamental reforms. The rural sector has largely been ignored in the post-independence industrialization strategy which has increased rather than reduced economic vulnerability. The failure to appreciate the link between agricultural development and industrial development has been costly in both economic and social terms. The declining share of agriculture in GDP, while a natural part of the development process, might also be the result of the governments' own policies which failed to direct adequate resources to the sector. The problems and complexities involved, as well as the time required in moving from an agriculturally-based economy to an urban-industrial one were badly underestimated. Pricing, exchange rate and trade policies often militated against growth in the agricultural sector.

A highly skewed production base and low productivity levels reflect the failure of development policy both at the national and regional levels. Access to preferential markets and the occasional commodity boom served to remove some of the pressures to rationalize the production structure and increase competitiveness. In a world driven by revolutionary changes in micro-electronics, robotics, biotechnology, transport and telecommunications, the Caribbean can no longer ignore the imperative to use accumulated scientific knowledge to devise appropriate technology which could satisfy domestic, social and economic objectives. In this respect, educational institutions have not done very well, but this is part of the larger failure of public institutions and policies, which must be systematically analyzed.

Caribbean economies are precariously perched and remain under stress. The issues facing the public finances are far from settled. The restructuring of tax systems to take account of the trend towards lower tariffs and the need for new sources of revenues remains an ongoing challenge. On the expenditure side, governments can no longer afford to solve problems by simply spending more money, employing more people or creating new institutions. Spending has to be done with greater purpose. Pension and other social programmes in particular have to be rethought to ensure viability and sustainability.

A great deal is yet to be accomplished to attain a competitive position. Much of what are now being seen as 'second generation' reforms should have been addressed a long time ago. In a development setting the importance of non-economic factors is increasingly being recognized. A credible government is a *sine qua non* for economic development. Up-to-date laws and their effective enforcement help to define the social and economic environment. A high quality social and physical infrastructure are essential for higher levels of productivity. An efficient and transparent regulatory framework is necessary to define the rules of competition, investment and entrepreneurship. The development of a robust financial sector is critical to development and appropriate regulations and policies are needed to allow the emergence of structures which can increase financial savings and meet the investment needs of the economy. High unemployment rates, even when output is growing, call not only for a critical look at the functioning of labour

markets, but more fundamentally at development policy. Factors affecting access to credit, particularly by farmers and small and medium-sized businesses, have long been crying for attention.

Fundamental to these reforms is the need for new and innovative perspectives on development and governance. In the past, governments have assumed that with modern engineering techniques and technical advisers, development by central direction could easily be achieved. Policies have to become more inclusive. The failure to recognize the potential of 'social capital' and to involve communities in their own 'economic salvation' has proved to be a major error in 'development from the top' policies. As the social and economic damage from this approach is being assessed, development strategies remain vague and unformed with yet no clear focus beyond immediate survival. The relationship between the public and private sectors is yet to be defined. Incentives and the use of resources in relation to the desired production structure need to be more clearly specified in both a regional and international context. This is critical to overall public policy. While increasing production and employment must rank high on the agenda, governments' concerns in these areas cannot afford to ignore the impact on the environment. This is not a side issue in countries with limited resources. The export of goods and services will impact on the use of resources and the quality of the environment. In the same way that mineral resources can be exhausted, tourism, the main service export of the Caribbean can also reach the limits of its expansion. The challenge of greater trade and preserving the environment require an approach that is sensitive to concerns of health and sustainability, but is not at the same time overregulatory to the point of stifling growth and development. As the twenty-first century approaches, a major issue is not more State or less State, but a more effective State since there are situations where the market does not work and the State's comparative advantage compels it to play an active role.

At the international level, a great deal of activity is taking place to forge a more liberal framework for the movement of goods, services and capital, following the completion of the Uruguay Round. This environment will pose a strong challenge to Caribbean States in terms of existing trade patterns, exploring new trading links and devising tactical instruments and strategies to maintain control over development. With their fragile economies, Caribbean States are compelled to view with a great deal of circumspection the headlong rush to rapid liberalization in every sphere. Whatever contribution others may have to make, development must remain an internal responsibility subject to a high degree of national consensus. Economic development is part of the nation-building process, and if improperly conceived can lead to social stresses and the magnification of problems it was intended to solve. Economic results affect social cohesion. Accordingly, governments cannot ignore the effects of policies on the social fabric and on commitment to the national effort. There are areas of decision-making which the State cannot concede to anyone. The benefits countries get from foreign investment, for example, may depend on certain kinds of policy-guidelines with respect to joint-ventures, taxation, the use of local resources and technology transfer. The protection of resources from overexploitation and the sale of land to foreigners are areas which would require continuous State oversight. Given the importance of the media and communications sectors to cultural and national development, a policy informed by the need for local control could find broad acceptance in a transparent setting. In the search for economic security, farmers cannot be left to the manoeuvrings of powerful transnational corporations. The Research and Development necessary

for the creation of competitive and resilient production structures cannot be left to a weak private sector without research capabilities and a risk-taking culture. Governments have to be careful in moving from a situation of too much intervention to one that reflects an abdication inimical to national development. Governments must create the space for a higher degree of local thinking in policy formulation which should reflect specificities treated as insignificant in typical structural adjustment programmes. The approach to incentives, for instance, often assumes an entrepreneur with highly developed responses and operating in a well informed environment within an efficient institutional framework. The complexity of the reform and development challenge ought not to be simplified. A fair amount of damage has already been done by the assumption that problems that look the same all have common roots and can be attacked with the same facile solutions that ignore communal heritage and the fragmentations and ruptures that have resulted from attempts at modernization. Opportunities for properly conceptualizing development are arising, and Caribbean governments must grasp them.

The problems facing Caribbean countries have to be seen in a larger setting where new alliances are emerging to meet global challenges arising from the changing configuration of the world economy. The Caribbean has not only been slow in taking hard economic decisions, but has taken a great deal for granted in not questioning the durability and foundations of traditional commercial ties and trading patterns. In this mind-set it was easy to condone the laggard progress of regional economic integration and overlook its conceptual inadequacies. The potential for interaction with the emerging economic powers in the world economy seems to have evoked little more than passing interest. It is difficult to separate the performance of small open economies from the quality of their international relations and their perspectives on global economic and political changes. Micro and macro problems at the domestic level are difficult to separate from the larger internal and external management concerns that help to define the space for decision-making. In the context of narrowly conceived economic reforms, there is also need to elevate thinking to a higher plane that explicitly recognizes the link between economics and geo-political relations, and the nature of the factors influencing the new alignments.

The paper comprises an introduction and five parts. The first outlines the recent economic performance of the Caribbean countries and some of the salient issues and problems confronting policy-making. This is followed by a discussion on trading relationships and the prospects facing the Caribbean in the changing regional and world environment. The third outlines some of the challenges and issues facing State reform in the Caribbean. In the fourth section, an attempt is made to identify some of the elements and considerations which need to inform the ongoing process of structural reforms. The final section presents some concluding observations.

While it is necessary at times to make reference to the experience of the wider Caribbean, the discussion for the most part is confined to members of the Caribbean Community and Common Market (CARICOM) and particularly the Anglophone component. The members of CARICOM are Antigua and Barbuda, the Bahamas, Barbados, Belize, Dominica, Grenada, Guyana, Jamaica, Montserrat, Saint Kitts-Nevis, Saint Lucia, Saint Vincent and the Grenadines, and Trinidad and Tobago. Suriname (a former Dutch colony) was admitted in 1995 and Haiti in 1997.

1. THE CONTEXT FOR REFORM IN THE CARIBBEAN

Introduction

Rapid changes in the global economy and significant differences in the rates of growth and development among nations of the world community have challenged many of the early post-war ideas and conceptions of development. Interpretations of the paths chosen by the 'successful' countries, however, remain controversial. While certain influences, factors and conjunctural events have been identified, development does not seem to have a unique function that could easily be replicated everywhere, given different historical circumstances and environments. Within the emerging general principles and trends, development frameworks or models still need to draw on particular circumstances formed by history, culture, attitudes and experiences. Failure to recognize this accounts for the limited success of structural adjustment programmes in several countries.

Against the background of failed policies and growing poverty, there is increasing pressure on many countries to abandon unsuccessful paths and reformulate the development framework to achieve a more efficient use of resources. The experience of the fast growing economies of the world underscores the observation that factors of production are more complex and encompass a far wider range of elements than was thought to be the case many years ago and as reflected in economic theorizing of the 1950s and 1960s. Resources alone do not define the production frontiers. Technology is not static, but is constantly widening the space of operation and changing the way we look at size, location, market access and resource availability and use. Policies are seen to be critical to development and the new doctrines being enunciated draw heavily on neo-liberal principles requiring greater trade and investment openness, a more competitive environment, a liberalized financial system, flexible exchange rate systems and a more circumscribed role for the State. They also point to the critical need for heavy investment in human capital and changes in the relationship between the State and civil society.

The experience since the early 1980s has clearly shown that not all countries respond in the same ways to a given set of policies. Structural constraints and the institutional and cultural context have a critical bearing on the outcome. It is often difficult to separate short and medium-term adjustment policies from long term development objectives in situations where day-to-day management difficulties are integrally related to structural problems and rigidities in the economy. Stabilization is not a sufficient condition for sustained growth and development where the main challenge is to change the way economies are ordered and function and to achieve greater social well-being at the same time.

The need for Caribbean governments to rethink and reshape economic and social policies is being informed by several factors. The failure of particular strategies to effect the desired transformation and to deliver expected outcomes is basic to the review process. Policy results have fallen short both in terms of popular expectations and in effecting the structural changes needed to

strengthen the economic base. The success of some developing States with less endowments in other parts of the world have helped to put this failure into even sharper focus.

Another set of factors forcing Caribbean governments to adopt new paths to development or paradigms stems from changes in the global environment. The end of the cold-war and the spread of the market economy corresponds with the retreat of central planning and the 'development State' in its several roles as development promoter, entrepreneur, distributor and agency of change. The shift from the State to the private sector as the engine of growth was a pragmatic change forced not so much by the declining capacity of the State to provide welfare benefits, but by the imperative to make economies more efficient and competitive. The weakening of protectionist forces in the world economy and the trends towards a more open and competitive world trading system have undermined claims for preferential trading arrangements regardless of their historical origins or their current rationale. Investment and aid flows have also been affected by developments in the global economy. Private foreign investment is being attracted to the export oriented economies which have been able to sustain high growth rates over a long period of time. The need for higher rates of capital formation and modern technology and perceived shortages in national savings and entrepreneurship have heightened the competition for foreign investment. At the same time, the removal of exchange controls and the global integration of financial markets have increased the mobility of savings leading States to radically alter their approach to financial policy in order to encourage savings and discourage the flight of capital. Tax policies have had to change too, not only to encourage investment and effort, but to address issues of compliance, evasion and the elasticity of the tax system in a context where the State's social responsibilities continue to grow.

With their middle-income status and increasing per capita income in most cases, Caribbean countries have found it increasingly difficult to access concessional development finance. Even before the end of the cold war which had a major influence on the dispensation of aid, the declining trends with respect to the Caribbean was already evident. With some former donors now actively seeking aid, the competition for aid has intensified, and greater attention is being paid to the plight of the 'transition' and very poor countries.

Traditional exports and tourism have contributed immensely to the standard of living which Caribbean States currently enjoy. The international environment, however, has been changing. Uncertainties in market conditions and frequent fluctuations in prices and production in the face of a persistent increase in the value of imports point to the need for a more diversified and dynamic export sector with the resilience to deal with changes in the market place. Policies to achieve this aim, have so far met with only limited success. Members of the Organization of Eastern Caribbean States (OECS)¹ have traditionally run persistent trade deficits, but these have been offset by earnings from the service sectors and investment inflows. Remittances from nationals living abroad have also helped.

The increases in oil prices in the 1970s put a severe strain on the finances of the oil importing countries of the region. The debt crisis soon followed, with its threat to international monetary and financial instability providing a rationale for external technical and financial assistance to debtor

countries. Recession in a number of industrial countries, increases in real interest rates and the fall in commodity prices in the early 1980s intensified the economic pressures on Caribbean States. The impact of these external shocks on the macro-economic environment raised critical questions about the capacity of these States to maintain internal stability by manipulating standard policy instruments. The fact that the global dimensions of the crisis seemed to signal more fundamental developments in the functioning of the world economy than a temporary cyclical downturn, also raised questions about the relevance of inward-looking policies in a world where the leading performers had developed dynamic export sectors.

The simplistic structural adjustment packages quickly conceived by the international aid agencies in the early to mid-1980s to restore economic calm failed to instigate turnaround in a number of countries. In the Caribbean their limited impact not only raised questions about the problem of management in small, open, undiversified economies, but also about the real nature of Caribbean economic problems and the direction of reform. Stabilizing the internal and external balances had high social costs. Policy reforms designed to achieve results within a short to medium time-frame were soon acknowledged to require a much longer period for implementation. It was also realized that the success of many policies depends on institutional reform and the interaction of governments with the civil society. Reforms hold different implications for the various groups and interests in the society and not all of them are readily embraced.

In Caribbean economies, it is difficult to separate day-to-day management from fundamental problems in the economy. The nature and structure of production are closely tied to government revenue, foreign earnings and the exchange rate. Production is highly concentrated, so a downturn in tourism or a drop in the price or production of sugar, bauxite, bananas or oil has a ripple effect throughout the economy. Economic diversification has long been a major challenge in Caribbean economies, and it is now widely recognized that the failure of import substitution within a highly restrictive framework has to give way to development options consistent with a more competitive setting. How to make the leap from a culture of regulation and controls to a market-oriented production setting is a major policy challenge. Perhaps even more challenging is the need to devise strategies which not only seek to maximize output per person, but which can involve the entire national community and share the benefits of growth. Creating opportunities for different levels of skills have to go hand in hand with increasing production.

Recent economic performance

Whenever economic development and structural reforms are discussed in relation to Caribbean countries, the issues of size and its constraints are bound to arise. As can be seen in Table 1 both in terms of population and land area, Caribbean States are generally quite small. Only three CARICOM countries have a population of over one million. The total population of CARICOM is around 6.3 million with an average GNP of US\$2,714. This excludes Haiti² which has a population of 7.2 million. The total GNP of CARICOM, including Haiti, is US\$19 billion which is about 30 per cent of Chile's, 3 per cent of Brazil's and 6 per cent of Mexico's. Many questions in economic

Table 1
Selected Demographic and Economic Statistics

Countries	Area km ²	Pop. '000 (1995)	Pop. Growth Rate (%) (1985-95)	Pop. Per km ²	Total GNP ^a (1995) US\$mn	Per Capita GNP ^a (1995) US\$	Import Ratio ¹ (1995)	Export Ratio ² (1995)
CARICOM Countries								
Antigua & Barbuda	440	65	0.5	148	495 ^b	7,730 ^c	105	86
Bahamas	13,942	276	1.7	20	3,297	11,940	59	53
Barbados	432	266	0.5	616	1,745	6,560	57	63
Belize	22,960	216	2.6	9	568	2,630	60	50
Dominica	750	73	-0.1	97	218	2,990	67	48
Grenada	345	91	1.0	264	271	2,980	62	47
Guyana	214,970	835	0.6	4	493	590	112	98
Haiti	27,750	7,168	2.0	258	1,777	250	30	10
Jamaica	11,424	2,522	0.9	221	3,803	1,510	66 ^d	58 ^d
Montserrat	102	10	-1.3	98	..	..	..	..
St Kitts-Nevis	269	41	-0.4	152	212	5,170	75	49
St. Lucia	616	158	1.4	256	532	3,370	69	69
St. Vincent	388	111	0.8	286	253	2,280	57	46
Suriname	163,270	410	0.3	3	360	880	98 ^e	126 ^e
Trinidad & Tobago	5,128	<u>1,287</u> 13,529	0.9	251	<u>4,851</u> 18,875	3,770	41	53
Other Caribbean Countries								
Anguilla	91	10	3.6	110	61 ^b	6,100	..	..
Aruba	188	80	..	425	..	..	..	..
Dominican Republic	48,734	7,822	2.0	161	11,390	1,460	28	27
Netherlands Antilles	960	200	1.0	208	2,300	11,000	..	..

.. not available

a. current prices

b. GDP

c. Per capita GDP

d. 1994

e. 1993

1. Imports of goods and services as a % of GDP

2. Exports of goods and services as a % of GDP

Sources: World Bank, Atlas, 1997; ECLAC, Selected Statistical Indicators of Caribbean Countries, 1996.

theory are analyzed without reference to size, the assumption being that size does not matter. The exceptional performance of small countries like Hong Kong (6.3 million people), Mauritius (1.2 million) and Singapore (3.0 million) in recent years has raised doubts about whether size is a serious obstacle to development. Size, of course, does carry with it certain constraints in terms of resource availability and market potential. A small population goes hand in hand with a small Gross National Product and a narrow range of skills. A small home market is often a disincentive to large-scale industries which require long production runs to reach optimum size and enjoy increasing returns to scale. Diseconomies of scale are associated with high unit costs of infrastructure, investment and production. Besides structural disadvantages, small island economies like those in the Caribbean are exposed to the devastating effects of hurricanes, against which there is little or no defense. Agriculture is particularly vulnerable. A limited supply of good agricultural land can also influence what is produced and the cost of production. The scope for mechanization may be limited. Size and location are often seen as mixed blessings for Caribbean States, most of which are micro-island States. On the one hand major improvements of living standards do not require massive investment or huge export marketing opportunities. The "Caribbean's close economic and communications links with Europe and North America and the large expatriate communities there, could provide the necessary resources and market niches for goods and service exports."³ On the other hand, proximity to North America makes it easy for financial and human capital to migrate. Location between South and North America also attracts criminal activities, drugs and money laundering on a scale that puts the meager resources of these governments under severe strain.⁴

In the Caribbean structural change has been slow. The view has been expressed that preferences and other forms of foreign assistance reduced the pressures for change. The heavy concentration of production on a few mineral and agricultural products for export reflects the colonial legacy and the ineffectiveness of post-independence industrial strategies. The uncertainties associated with the markets for these products are now forcing the adoption of more outward-oriented trade policies, but these need support over a wide front within a realistic time-frame. Developments in technology affecting transport and communications and the reduction of protective trade barriers by most countries are altering the constraints of location and natural resource endowments. Policies are now recognized to have critical value. Notwithstanding the breakthroughs in technology and the effects of globalization, size can have an economic downside, since small economies will have great difficulty generating the volume of savings necessary to finance the desired scale of investment. Some very small countries do not even have the space for a modern airport. Because of the size of the airport and the volume of traffic, they are bypassed by major airlines. Even national governments which try to fill the gap have difficulty maintaining viable airlines which in most cases have to be subsidized to stay in operation.

Economic and financial management in small open economies raises additional problems. As can be seen in Table 1 more than half of total output in most cases is sold abroad. Because of the nature of the products exported and special marketing arrangements, devaluation of the national currency to stimulate exports is not likely to have a great effect on demand. The heavy dependence on imported goods, too, limits the scope for expansionary fiscal policy. Narrow money and capital markets distort the savings/investment process and the situation is often compounded by regulations

influencing competition among financial institutions and portfolio composition. In situations where a narrow range of financial securities exists, the pressure for savings to move abroad is strong. A high level of domestic savings does not necessarily lead to a high level of domestic investment. But there can also be another anomaly in that while domestic savings are flowing abroad, a country can become increasingly dependent on foreign savings to finance development.

While possessing a number of common features, economic performance and the standard of living vary widely from one Caribbean State to another. A common feature is the tendency for periods of boom to alternate with periods of recession. Gains made in one period can be quickly lost in economic downturns triggered by domestic factors or external shocks. A boom in commodity prices, capital inflows and the growth of resource-based sectors such as tourism are among the leading factors which lie behind the upswing phases in recent years. Foreign exchange is the fuel that drives these economies, and by expanding import capacity, foreign earnings make possible a higher level of spending, and can lead to a temporary increase in welfare. Because of the high propensity to import, a higher level of foreign earnings does not necessarily translate into a faster rate of domestic capital formation. In Caribbean societies with their democratic political arrangements, domestic policies tend to be highly responsive to populist pressures, and the enhanced capacity associated with phases of economic expansion can easily be dissipated in higher levels of consumption, or misdirected project selection and planning. The inability to sustain reasonable growth performances over long periods is not unrelated to modest savings rates and more productive use of resources. The ability to sustain growth over long periods on the basis of internal structural changes is a major challenge facing Caribbean States.

A recent study has indicated that economies in the Latin American/Caribbean (LAC) region are among the most volatile in the world. The volatility of real Gross Domestic Product (GDP) growth in the region "has been more than twice and the volatility of private consumption growth nearly three times, that experienced by the industrial economies."⁵ Except for Africa, the Middle East and North Africa, the LAC area is also more volatile than other developing regions. Some of the reasons cited for this situation include the following:

- High terms of trade volatility associated with the concentration of production and exports in a few primary commodities;
- Unpredictability of capital flows;
- Volatile monetary and fiscal policies stemming from external shocks and interaction with the relatively weak fiscal, financial and monetary institutions;
- Destabilizing exchange rate regimes;
- Shallow financial markets and their limited ability to absorb shocks.

The post-war development experience provides ample evidence of this volatility. The Caribbean economy in the 1950s revolved around a few basic sectors, viz., export oriented agriculture, mining, tourism and simple manufacturing. While available data for the 1950s indicate a growth in per capita income in most countries of the region, in some economic expansion was impressive. In Jamaica, for example, total real production increased by 77 per cent between 1953 and 1960 at an average rate of 11 per cent per year. In Trinidad and Tobago, real GDP growth averaged over 13 per cent over the same period. In both these countries, the mining sector was a significant contributor to this performance. The data also indicate reasonably high investment rates in the period. While in Jamaica, the Gross National Savings (GNS) ratio averaged around 16 per cent in the late 1950s, the investment ratio averaged around 23 per cent. In Trinidad and Tobago Gross Domestic Investment averaged over 25 per cent in the 1950s, while the Gross Savings Rate was around 21 per cent. In Guyana and Barbados, too, Gross Capital Formation was averaging between 20 and 25 per cent of total production, with domestic savings financing around 75-80 per cent of investment on average.

The 1960s constituted a milestone in the post-war history of the Anglophone Caribbean. The failure of the British West Indies Federation as an instrument by Britain for granting independence to a number of colonies in the Caribbean was quickly followed by a decision to allow the territories that so desired to attain political independence individually. With this new status, Caribbean governments began to assume a greater responsibility for social and economic development and to put in place a variety of controls, regulations and incentives to guide the process. The State saw its role as not only providing law and order and maintaining and improving the social infrastructure, but for one reason or another became increasingly involved in direct production. As was the case in a large number of developing countries, creation of an industrial sector was embraced as the main goal of development policy. Domestic production of consumer goods previously imported, via the policy of import substitution, was to be the basic strategy with tariffs and quantitative restrictions providing a protected environment. The theoretical underpinning to this strategy was that the expansion of the manufacturing sector through new investment and the reinvestment of profit, would absorb 'surplus' labour and generally raise the marginal productivity of labour in the economy. In the small economies of the Caribbean producing manufactures for foreign markets was seen to be an integral part of the strategy, but this did not become an explicit part of the policies adopted. Modernization became synonymous with industrialization, and the implicit assumption was that this modern sector could meet the needs of the entire population.

In defining the development framework in a period of high nationalism, political and economic objectives became closely intertwined, as the State attempted to straddle its several functions as promoter, investor, facilitator and distributor. Some policies lost their time horizons and some had no clear thrust. Tax policies, for example, gave confusing signals, while the policy toward foreign capital was ambiguous and uncertain. The foundations for much of the later difficulties were laid in the 1960s and 1970s.

The 1960s, however, promised much as the euphoria of independence and the promise of economic planning overwhelmed the concerns about size and limited resources. In this decade the

Anglophone Caribbean economies grew by about 4 to 5 per cent per year in real terms. Suriname and the Dominican Republic also experienced growth rates in the region of 5 per cent. A favourable international environment, stable or increasing commodity prices, aid inflows, high levels of government spending and available opportunities associated with import substitution activities were the main factors behind the growth in the 1960s, and provided the basis for a great deal of the optimism in the period. Low inflation rates and low energy cost (petroleum was averaging between 2 and 3 US dollars a barrel) contributed to the favourable environment. The growth of GDP generally exceeded the population growth rate, so the growth rate of per capita GDP was positive, in some cases exceeding 2.5 per cent per year.

The 1970s was a more difficult decade for the region, with some countries such as The Bahamas and Jamaica losing the momentum of the previous decade. While per capita real Gross National Product (GNP) grew by over 3 per cent per year in Barbados, Belize, Trinidad and Tobago, Suriname and the Dominican Republic, in Jamaica and The Bahamas it declined by an average rate of 2.8 and 2.9 per cent per year, respectively, between 1970 and 1980. In the OECS the performance was mixed, with per capita income declining in Antigua and Barbuda, Dominica, Grenada, and Saint Vincent and the Grenadines. The dramatic increases in the price of oil benefited Trinidad and Tobago as an oil exporter but had a disastrous effect on the balance of payments and economic performance of the oil-importing countries of the region.

The 1980s was in some senses a defining period for Caribbean States. Some of the difficulties that reared their heads in the 1970s continued unresolved in the following decade in which some countries experienced lower growth rates while others lost gains made earlier. The difference in economic performance among States pursuing different paths to development or at different levels of development raised a variety of questions with respect to the efficacy of particular economic policies and strategies. In the 1980s real GDP in the industrial countries grew by around 3 per cent per year on average as compared to 1 per cent for Sub-Saharan Africa, 8.4 per cent for East Asia and 1.6 per cent for Latin America and the Caribbean. Within the Caribbean some States far exceeded the average for the LAC region. The OECS and Belize, for example, which are regarded as weaker and more vulnerable grew by about 5 to 6 per cent per year. On the other hand, in 1993 real GDP in Barbados was at the same level as that of 1980. In Suriname and Haiti GDP hardly changed between 1980 and 1990, while in Guyana and Trinidad and Tobago it declined by 27 per cent and 32 per cent respectively in the period. Following the end of the oil boom, government real consumption expenditure in Trinidad and Tobago fell by 9 per cent between 1982 and 1990 but private real consumption expenditure dropped by some 47 per cent and gross capital formation by 67 per cent in the period. The shrinkage of the Trinidad and Tobago market not unexpectedly had an adverse impact on activities in other CARICOM countries.

In the industrial countries real GDP per capita increased by over 2.3 per cent per year in the 1980s, as compared to 6.2 per cent for East Asia and 0.4 per cent for Latin America and the Caribbean. In Guyana real per capita GDP in 1990 was 12 per cent below that of 1980 and 26 per cent below that of 1970. In Trinidad and Tobago real per capita GDP fell by 30 per cent between 1980 and 1990. In the OECS, however, real per capita GDP increased by about 4 to 5 per cent per

year in the 1980s. In the 1990s, real GDP in the LAC region has been growing by an average of about 3.3 per cent per year as compared to 1 per cent in the 1980s and 6 per cent in the 1970s. In terms of overall growth Chile and Guyana have been among the front-runners in recent years, with growth averaging over 6 per cent per year. As can be seen in Table 3 countries like Barbados and Trinidad and Tobago have recovered from the depressed performance of the 1980s, but generally the growth rate for the region is quite modest.

Table 2
World: Growth of Real GDP and Real GDP Per Capita, 1966-2006a
 (Annual Percentage Growth)

Countries	<u>Growth of Real GDP, Per Capita, 1966-2006</u>					<u>Growth of Real GDP, 1966-2006</u>				
	1966-73	1974-90	1991-95	1996e	Forecast 1997-2006	1966-73	1974-90	1991-95	1996e	Forecast 1997-2006
High Income	3.8	2.1	1.3	1.9	2.3	4.9	2.9	2.0	2.5	2.8
Low and Middle Income	3.8	1.4	0.5	2.7	3.8	6.7	3.3	2.3	4.5	5.4
Asia	2.8	4.3	6.8	6.4	5.7	5.5	6.2	8.2	7.9	7.1
Latin America and the Caribbean	4.2	0.4	1.4	1.7	2.7	6.9	2.6	3.2	3.4	4.2
Europe and Central Asia	5.5	2.2	-6.7	-0.8	4.0	6.6	3.1	-6.4	-0.3	4.5
Middle East and North Africa	5.8	-1.7	-0.1	1.4	1.1	8.7	1.4	2.6	4.1	3.6
Sub-Saharan Africa	2.0	-0.7	-1.1	0.8	1.2	4.7	2.2	1.5	3.8	4.1
World	2.9	1.2	0.5	1.4	2.0	5.2	3.0	2.0	2.9	3.4

a. based on 1987 prices and exchange rates

e. estimated

Sources: World Bank, Global Economic Prospects and the Developing Countries, 1997.

Table 3

Growth of Real GDP, 1981-1996
(Percentages)

Countries	Average 1981-91	1992	1993	1994	1995	1996 ^p
<u>CARICOM Countries</u>						
Antigua & Barbuda	6.9	1.1	3.7	5.0	-4.5	5.8
Bahamas	3.6	-2.0	1.7	0.9	0.3	3.0
Barbados	0.9	-5.7	0.8	4.0	2.5	4.7
Belize	4.9	9.5	4.3	1.5	3.8	1.5
Dominica	4.0	2.7	1.9	2.1	1.8	3.2
Grenada	5.0	1.1	-1.2	3.3	3.1	3.1
Guyana	-2.8	7.7	8.2	8.5	5.1	7.9
Haiti	-0.7	-13.2	-2.4	-8.3	4.3	2.8
Jamaica	2.5	1.5	1.4	1.1	0.5	-1.7
Montserrat	6.1 ^a	1.7	1.5	-0.8	-7.6	-17.7
St Kitts-Nevis	6.2	3.5	5.0	5.5	3.7	5.8
St. Lucia	7.0	7.1	2.3	2.1	4.1	1.9
St. Vincent	6.8	6.5	1.1	-1.2	8.3	1.0
Suriname	-0.3	5.8	-4.4	-4.2	5.2	3.4
Trinidad & Tobago	-1.7	-1.1	-2.6	5.2	3.1	2.8
<u>Other Caribbean Countries</u>						
Anguilla	8.9 ^b	7.1	7.5	7.0	-4.2	3.4
Aruba	...	4.0	5.0	5.9	5.7	3.9
Dominican Republic	2.7	8.0	3.0	4.3	4.8	7.3
Netherlands Antilles	...	5.2	-1.8	1.7	1.3	0.0

... not available

a. 1981-90

b. 1986-91

p. provisional

Sources: ECLAC; Caribbean Development Bank; World Bank.

As can be seen in Table 4 per capita income in the OECS now exceeds that of Guyana and Jamaica respectively, and in the case of Antigua and Barbuda and Saint Kitts-Nevis, it is now higher than that of Trinidad and Tobago. Interestingly, in the 1960s the larger Caribbean States such as Barbados, Guyana, Jamaica and Trinidad and Tobago were deemed to have greater potential than the smaller OECS States and were to be treated as the 'More Developed Countries' in the Caribbean Community in the context of policies and measures designed to discourage polarization. Guyana is now regarded as one of the poorest countries in the western hemisphere. The effects of the unsatisfactory economic performance of the region's MDCs in the 1980s were felt not only on the flight of skills and capital, but also on the pace of economic integration which slowed down considerably. Of course, there is a school of thought which argues that with a higher level of integration, the region would have been better equipped to withstand the external shocks of the 1970s and 1980s.

One of the interesting phenomenon in the Caribbean is the ability of a number of very small economies, some not yet independent, to use their limited natural assets, location and fiscal systems to generate relatively high per capita incomes and employment rates. Anguilla (population 11,000), the Cayman Islands (population 33,000), the Turks and Caicos Islands (population 15,000), the British Virgin Islands (population 19,000) and Aruba (population 84,000) generate per capita incomes in the region of between US\$5,000 and US\$20,000. Montserrat (still a British dependency) with a population of 10,000 people enjoyed a per capita GDP of over US\$5,000 before the recent series of volcanic eruptions. The Bahamas (pop. 276,000) also enjoys per capita GNP of over US\$10,000. Employment rates also tend to be high and some of these countries have shown remarkable resilience in recent years in recovering from depressed situations created by decisions taken outside their borders. In Aruba, following the closure of the Exxon's Largo refinery in 1985, un-employment soared to about 40 per cent. It is now estimated to be less than one per cent. These economies may never meet most of the standard criteria in terms of structural change used to define a state of development, but by encouraging the development of tourism and offshore financial activities they have been able to share in the international growth of these activities as the traditional sources of income have faded.

Table 4
Growth of Per Capita GNP, 1970-1995

Countries	Nominal Per Capita GNP (US\$)						Average Annual Growth Rate of Real Per Capita GNP(%)			
	1970	1980	1985	1990	1995	1995 PPP	1970-80	1980-90	1985-95	1970-95
CARICOM Countries										
Antigua & Barbuda	370	1,380	2,030	4,600	7,690 ^a	..	-1.7	4.7	2.7	4.9
Bahamas	2,300	3,450	7,150	11,510	11,940	14,710	-2.9	1.7	-1.0	1.7
Barbados	570	3,270	4,680	6,540	6,560	10,620	3.2	1.4	-0.2	1.9
Belize	590	980	1,130	1,970	2,630	5,400	4.8	2.5	4.4	3.9
Dominica	280	640	1,160	1,940	2,990	..	-3.1	3.0	4.0	2.5
Grenada	300	780	970	2,120	2,980	..	-0.6	5.1	6.6	..
Guyana	370	690	570	370	590	2,420	1.1	-3.2	0.8	-2.6
Haiti	110	280	350	370	250	910	1.8	-2.3	-5.2	-1.3
Jamaica	670	1,090	940	1,510	1,510	3,540	-2.8	-0.4	3.7	-0.8
Montserrat	..	2,107 ^b	3,083 ^b	5,730 ^b	5,840 ^c	..	..	..	..	..
St Kitts-Nevis	320	960	1,520	3,330	5,170	9,410	1.7	6.0	4.6	5.2
St. Lucia	340	890	1,210	1,904	3,370	..	3.0	4.2	3.9	..
St. Vincent	240	540	840	1,610	2,280	..	-1.0	5.7	3.9	3.7
Suriname	530	2,770	2,570	3,050	880	2,250	6.8	-5.0	0.7	4.3
Trinidad & Tobago	860	5,010	6,010	3,470	3,770	8,610	3.9	6.0	-1.6	-0.1
Other Caribbean Countries										
Dominican Republic	350	1,190	810	820	1,460	3,870	3.3	-0.4	2.1	..

- .. not available
a. estimated
b. per capita GDP, 1994
c. per capita GDP, 1994
ppp. purchasing power parity

Sources: World Bank, *Atlas*, Various Issues and *World Development Indicators*, Various Issues.

Saving and investment

Factor accumulation tends to rank very high in the literature as a determinant of output growth. In this connection, a great deal of attention tends to be centered on the level of saving and investment in an economy. There is some controversy over whether growth causes saving rates to rise, or a high level of saving is a pre-requisite for growth. What the evidence does show, however, is that fast growing economies are associated with a high level of saving and investment (see Table 5). Fourteen of the world's fastest growing economies over the past 10 years had a saving rate over 25 per cent, and none had a saving rate under 18 per cent. At the same time 8 of the world's slowest growing 20 economies over the same period had a saving rate below 10 per cent and 14 were below 15 per cent.⁶ Some recent studies seem to suggest that it is growth that drives savings rather than the other way around.⁷ Growth also tends to attract foreign investment which is often reluctant to enter environments which offer little prospects of recovering capital investment.

Table 5
Saving and Investment Rates in Selected Countries,
Average, 1993-95
 (% of GDP)

Countries Grouped by Saving Rates	(1)	(2)	(3)	(4)
	CAB	GDS	GDI	GNP Per Capita Real Growth Rate (%)
<u>Less than 10%</u>				
Bangladesh	-2.6	8.3	15.4	2.1
Bolivia	-7.8	6.8	15.2	1.7
El Salvador	-0.9	4.7	18.9	2.9
Ghana	-6.6	4.5	16.4	1.5
Senegal	-2.8	7.5	14.2	-1.2
<u>10-20%</u>				
Argentina	-2.7	19.5	18.8	1.9
Canada	-3.0	19.7	18.8	0.4
Denmark	2.1	21.0	14.9	1.5
Israel	-4.5	13.9	23.2	2.5
Mexico	-4.8	18.6	20.9	0.1
<u>21-30%</u>				
Brazil	-0.9	21.9	21.0	-0.7
Chile	-1.8	28.0	27.6	6.1
France	0.8	22.5	14.9	1.5
Germany	-0.9	22.5	21.8	..
India	-1.2	21.3	23.0	3.1
Mauritius	-3.4	23.4	29.5	5.7
<u>Over 30%</u>				
China	-0.4	41.5	41.2	8.0
Hong Kong	..	33.6	31.5	4.8
Japan	2.7	31.1	29.1	2.9
Malaysia	-4.7	36.7	38.1	5.7
South Korea	-0.8	35.6	36.1	7.6
Singapore	13.9	..	34.9	6.2
Thailand	-6.3	36.2	41.6	8.4

.. not available

CAB – Current Account of the Balance of Payments

GDS – Gross Domestic Savings (difference between GDP and total consumption)

GDI – Gross Domestic Investment (sum of all outlays on additions to capital assets, plus changes in inventories)

Source: World Bank, *World Development Indicators, 1997*; World Bank, *Atlas, 1997*.

The savings ratio, that is, GDS as a proportion of GDP, not only varies widely across the Caribbean region, but for individual countries can also fluctuate wildly from year to year. In the 1980s, most OECS countries had a savings rate of less than 15 per cent, but with the help of foreign resources, the investment rate averaged over 25 per cent, and this helps to explain the favourable growth experience in the period. In the larger territories the saving rates average less than 20 per cent, but in some cases, for example, Guyana and Jamaica, this has improved in the 1990s. The decline in the Trinidad and Tobago ratio from an average of around 40 per cent during most of the 1970s, to an average of 23 per cent between 1981 and 1991 corresponds with the significant drop in income in this period as a result of the fall in oil prices. The investment rate in the larger Caribbean countries ranged between 18 and 32 per cent of GDP during the 1980s and while the data for the 1990s indicate an improved performance for most countries, the ratio was in most cases less than 30 per cent.

While the concept of 'GDS' gives an indication of the savings capacity of a country, it may not reflect resources available for domestic investment. The related concept of 'GNS' takes account of factor income payments and net transfers abroad. In the case of Trinidad and Tobago, for example, the GDS ratio averaged 25 per cent per year between 1985 and 1995 as compared to 17 per cent for the GNS ratio. If account is taken of the consumption of fixed capital, the net national savings rate in this country has been averaging around 6 per cent of GDP since the mid-1980s. In the early 1990s the GNS ratio in Jamaica fluctuated between 11 and 24 per cent. In Guyana it was estimated to be around 13 per cent in 1994, while in Belize it has averaged 21 per cent in the first half of the 1990s.

Table 6
Savings and Investment Ratios in Selected CARICOM Countries, 1973-1995

Countries	<u>Savings Ratio</u> ¹				<u>Investment Ratio</u> ²			
	1973-80	1981-91	1992-94	1993-95	1973-80	1981-91	1992-94	1993-95
Bahamas	25.7 ^a	25.0 ^b	..	14.7 ^g	13.7 ^a	18.6 ^b	20.8	20.1 ^h
Barbados	12.1	17.2	17.3	15.8 ^c	22.8	18.9	12.3	13.1
Belize	..	18.7	20.6	18.6	27.2	24.4	29.1	25.2
Guyana	20.0	18.0	37.6	36.8	29.7	31.5	50.3	47.3
Jamaica	16.0	18.4	25.5	23.6	22.8	23.8	31.8	27.5
Trinidad & Tobago	39.3	23.1	24.6	27.4	27.0	21.7	12.8	15.7
<u>OECS</u>								
Antigua	..	21.5	20.9	23.9	..	33.8 ^e	21.8	32.4
Dominica	..	7.4 ^a	1.7	2.7	..	27.0 ^d	16.0	19.7
Grenada	..	8.1	15.3	17.0	..	38.0	30.5	31.4
Montserrat	..	-2.4	5.9	7.6 ^g	..	43.3 ^e	37.5	32.8 ^h
St. Kitts-Nevis	14.1 ^a	12.8	23.2	20.3	34.3 ^a	39.5	38.8	37.8
St. Lucia	7.1 ^f	11.2	10.2	19.1	34.3 ^f	24.5	15.9	24.7
St. Vincent	..	12.0	13.0	11.7	34.6 ^a	26.5	26.8	26.5

- (1) Gross Domestic Savings as a % of GDP at current market prices
(2) Gross Domestic Investment as a % of GDP at current market prices
.. not available
a. 1977-80
b. 1981-87
c. Gross National Saving
d. 1984-90
e. 1983-91
f. 1980
g. 1993-94
h. 1993 only

Source: World Bank, *World Tables, 1995*; CDB, *Annual Report, Various Issues*; Official Publications; CDB, *Social and Economic Indicators, Various Issues*.

While governments in the fast growing economies are saving between 5 and 10 per cent of GDP, government savings in the Caribbean tend to be small and often negative. Available evidence indicates that the poor performance of the larger CARICOM countries during the 1980s coincided with a decline in real investment.

With respect to aggregate private savings, data are not readily available for all countries but one can get some indication of their importance by deducting government savings from the overall figure which itself is a residual. In Trinidad and Tobago, for example, private savings, including depreciation, averaged 95 per cent of GNS in the early 1990s. Precise and up to date data on the contribution of personal and corporate savings are also not easily available. In Trinidad and Tobago the contribution of personal savings to total domestic savings amounted, on average, to more than three times the contribution of corporate savings in the 1950s. A study using more recent data appears to confirm that in this country the propensity to save out of personal income is higher than that associated with corporate profits.⁸ In Jamaica, however, figures available for the 1950s and 1960s indicated that corporate savings make a larger contribution to GNS than personal savings.⁹ In recent years public savings in most countries of the region have been increasing, and in certain cases average over 3 per cent of GDP (see Table 7).

Table 7
Central Government: Current Savings or Deficit (-) as a % of GDP

Year	Bahamas	Barbados	Belize	Guyana	Jamaica	Trinidad & Tobago
1980	2.8	2.7	4.7	-11.6	4.0	21.6
1981	2.6	1.0	2.0	-20.4	4.0	20.2
1982	0.8	0.9	1.3	-29.3	2.9	4.8
1983	0.3	2.4	0.1	-27.1	-8.6	1.8
1984	0.4	0.5	-0.2	-36.7	-1.4	1.8
1985	1.0	0.5	-2.0	-18.0	-0.7	1.9
1986	1.4	1.6	2.0	-5.0	5.1	-0.8
1987	1.5	1.2	3.8	-27.2	3.6	1.3
1988	-0.2	4.5	7.3	-10.3	2.3	-2.3
1989	-0.6	4.5	8.6	-4.9	4.1	-2.0
1990	0.2	0.2	9.3	-14.6	4.9	-0.1
1991	-1.1	2.7	7.3	-16.8	6.1	3.1
1992	0.1	2.3	5.7	-11.3	7.3	-1.2
1993	0.1	3.3	2.9	1.9	6.7	1.4
1994	1.9	2.3	2.6	5.4	6.0	1.4
1995	1.8	3.2	-0.6	6.5	7.4	2.0
1996 ^p	1.0	1.7	3.5	9.4	-0.2	3.2

p. provisional

Source: IDB, *Economic and Social Progress in Latin America, 1996 Report; Official Publications.*

Given the strong correlation which seems to exist between savings and investment, a major aim of public policy in the Caribbean is to increase both public and private savings. The factors which affect government savings, however, are not the same as those that affect private savings. With respect to the latter, some of the variables that have attracted attention are per capita income, financial intermediation, the rate of inflation, the level of taxation, and the availability of social security arrangements. The study of savings can also be usefully approached from the consumption side. Some studies have shown that an increase in government savings can have a negative impact on private savings as a result of taxation and expenditure (wages and salaries) policies.¹⁰ The ability of the government to save rests critically on the environment in which it operates. The efficiency of the bureaucracy and the tax system, its inclination to levy user charges where feasible, access to capital funds, and the approach to subsidies are among the complex of factors which may affect the level of public sector savings. One study has found that the creation of social and political institutions that reduce the degree of political instability will have a positive effect on public sector savings.¹¹

The contribution of foreign savings varies from year to year and from country to country. In recent years foreign resources have played a critical role in financing investment in countries like Saint Lucia and Dominica with low domestic savings rates (See Table 6). In the relatively more developed countries of the region, however, domestic savings have financed the bulk of domestic investment. Foreign savings seem to have contributed on average around 20-30 per cent to gross domestic capital formation. The trends in localization in the 1960s and 1970s created a very uncertain climate for private foreign investment, leading to a decline in private inflows and capital flight. This development was not unrelated to the increase in the public sector borrowing as governments increased their role in the economy to offset declines triggered by changes affecting the main sectors of the economy. Subsequently, the large share of foreign exchange earnings taken by foreign debt service underlined the limits of *ad hoc* borrowing.

In order to supplement domestic savings with foreign savings and to access technology, an increasing number of countries in the developing world are liberalizing their capital accounts and adopting investment-friendly policies. The competition for foreign investment has increased significantly in recent years. While net official development finance flows to developing countries have been on a declining trend during the 1990s, total private flows increased from US\$44.4 billion in 1990 to US\$244 billion in 1996, totaling US\$938 billion between 1990 and 1996. Private investment accounted for almost half of this total. Interestingly, the major recipient of private capital flows have been the high saving/high growth countries of East Asia and the Pacific which received over 40 per cent. Some 33 per cent flowed to Latin America and the Caribbean with Mexico, Brazil and Argentina accounting for just over 75 per cent.¹² It has been estimated that total net private flows to Latin America and Asia in 1996 alone exceeded total flows for the entire 1980s.¹³

As a result of market-oriented reforms and privatization, the opportunities for investment have grown significantly in recent years as an increasing number of countries become 'creditworthy'. Transnational corporations are increasingly servicing foreign markets through establishment of foreign affiliates rather than through exports. The growth of global sales has exceeded that of exports of goods and services by a factor of 1.2 to 1.3 since 1987.¹⁴

As far as the Caribbean is concerned, investment policies are becoming more open, but the subregion has received only about 2 per cent of net foreign direct investment flows since 1991. Though flows for most countries have increased in the 1990s, the pattern of flow is highly skewed towards a few recipients. (See Tables 8 and 9). Aside from the Cayman Islands, which is an offshore financial centre, Trinidad and Tobago has attracted the largest volume, US\$1.9 billion between 1991 and 1996 as compared to US\$57 million in the period 1985-1990. Most of this investment, however, has been flowing into the gas-based sector, with the result that this, the most industrialized of the CARICOM countries, continues to depend heavily on the petroleum and petrochemical industries.

Table 8
Inflows of Foreign Direct Investment by Country, 1985-1996 (US\$m)

Countries	1985 - 1990*	1991	1992	1993	1994	1995	1996**
Antigua & Barbuda	36	55	20	15	25	27	31
Aruba	22	185	-37	-18	-73	-6	30
Bahamas	2	55	73	118	137	171	210
Barbados	88	7	14	9	13	12	22
Belize	11	14	16	9	15	21	26
Cayman Islands	121	-9	27	447	447	470	510
Cuba	-	10	7	3	14	9	12
Dominica	11	15	21	13	22	25	19
Dominican Republic	87	145	180	91	132	271	160
Grenada	10	15	23	20	19	16	19
Guyana	1	13	147	70	107	74	81
Haiti	7	14	8	8	2	2	3
Jamaica	37	133	142	78	117	167	175
Netherlands Antilles	-22	33	40	11	22	10	11
St. Kitts-Nevis	23	21	13	14	15	20	17
St. Lucia	22	58	41	34	32	35	39
St. Vincent & Grenadines	7	9	19	31	51	31	45
Suriname	-67	10	-30	-47	-30	19	7
Trinidad & Tobago	57	169	178	379	516	299	320
TOTAL 19 countries	373	952	902	1,285	1,583	1,673	1,737

*Annual average. **Estimates. .. not available

Sources: *UN World Investment Report, 1997.*

Table 9
Foreign Direct Investment Stock,* 1980-1996 (US\$m)

Countries	1980	1990	1996**
Trinidad & Tobago	976	2,093	3,954
Cayman Islands	223	1,749	3,642
Dominican Republic	239	572	1,550
Jamaica	501	690	1,502
Bahamas	298	336	1,099
St. Lucia	94	315	554
Antigua & Barbuda	23	292	464
Netherlands Antilles	568	206	332
St. Kitts & Nevis	1	160	260
Barbados	102	169	256
St. Vincent & Grenadines	1	48	234
Aruba	..	131	212
Haiti	79	149	186
Grenada	1	70	183
Dominica	..	66	182
Belize	12	72	172
Cuba	..	3	57
TOTAL	3,118	7,121	14,839

*Estimated by adding flows. **Estimates. .. not available

Sources: *UN World Investment Report, 1997.*

Domestic capital formation

In the Caribbean, gross domestic investment (gross capital formation, or gross domestic capital formation) as a per cent of GDP tends to be higher than the savings ratio (See Table 6). This is particularly so in the OECS where the investment ratio of over 20 per cent in some cases is more than twice the savings ratio. Among the larger CARICOM countries, the investment performance seemed to have declined significantly from the 1970s at over 20 per cent in Barbados and Trinidad and Tobago and improved in Jamaica and Guyana where the investment ratio crossed 30 per cent in the early 1990s. Generally foreign savings in the form of grants, private investment and loans have made possible a higher level of investment than would have been warranted by the domestic savings effort.

Data on real investment are not available for all countries, but in the cases of Guyana and Jamaica, they give an indication of a significant decline since the 1970s. In Trinidad and Tobago, real investment increased by an annual rate of 12.7 per cent per year between 1973 and 1982, but since then it has declined to an annual rate of 9.5 per cent per year. In Jamaica real investment in the early 1990s, was below the level of the 1970s. Guyana, too, experienced a steady decline until the early 1990s.

Available data on the contribution of the public sector to capital formation in recent years amounts to less than 10 per cent of GDP in most cases (See Table 10). In certain countries, such as Saint Lucia and Belize, public sector investment has exceeded capital spending by the private sector. Most public sector investment was in infrastructure which is not only underdeveloped in some countries of the region, but has not been maintained in others.

Table 10
Contributions of the Public and
Private Sectors to Savings and Investment
(Average 1990-1994)

Countries	<u>Gross National Savings as a % of GDP</u>				<u>Gross Investment as a % of GDP</u>		
	Private	Public	Total	Foreign	Private	Public	Total
Antigua	18.7	-3.6	15.1	3.6	21.4	2.6	24.0
Barbados ¹	15.0	2.4	17.4	-4.0	11.4	2.1	13.5
Belize	14.5	8.8	23.3	5.5	11.4	16.1	27.5
Dominica	8.9	3.4	12.3	15.8	16.6	11.4	28.0
Grenada ¹	21.2	4.3	25.5	11.1	28.4	8.2	36.6
Guyana ¹	4.3	1.0	5.3	31.2	21.8	15.2	37.0
Jamaica	..	..	18.7	11.8	..	..	30.5
St. Kitts-Nevis ²	20.6	7.0	27.6	..	38.8	6.7	45.5
St. Lucia ¹	2.2	10.4	12.6	11.0	10.8	12.8	23.6
St. Vincent	..	..	..	..	17.6	11.6	29.2
Trinidad and Tobago	11.3	5.5	16.8	-2.1	10.5	4.3	14.8

.. not available

1. 1991-95

2. 1989-94

Source: IMF, *Country Reports*.

The deterioration of the utilities, transport, communications and social infrastructure in some Caribbean countries during the 1980s as a result of financial problems, would have discouraged private investment and no doubt contributed significantly to economic decline in this period. Poor macroeconomic management would also have contributed to the decline. Rebuilding and modernizing the social and economic infrastructure is a prerequisite for economic growth and development. Making greater use of existing capital stock also has to be on the agenda.

Given the common perceptions about the role of private investment in the development process, a great deal of attention is given both by academics and policy makers to identifying the critical determinants of an investment-friendly environment. Among those featuring in these exercises are natural resources, the size of the local market, the rate of growth of per capita income, the macroeconomic environment, tax incentives, exchange controls, interest rates, the quality of the workforce, the state of the physical infrastructure, etc. A recent econometrics study done on the Caribbean found that the share of investment in GDP was positively correlated with GDP growth and even more strongly with export growth¹⁵. The effect of government domestic borrowing on local investment, the 'crowding out' effect, was uncertain. The commonly accepted view that investment was negatively related to the lending rate was not supported. The interest rate variable came out with a positive sign. The study also showed the interest rate spread to be positively correlated with investment and growth. In the 'financial repression' debate it is often argued that a real interest rate policy will encourage savings, investment and growth. The deposit rate variable was found to be negatively correlated with these variables.

It is well known that the results of statistical analysis are often strongly influenced by the variables chosen, the quality of the data and even the time period studied. It is often difficult to quantify some of the most critical influences, such as the effects of external economies, the perception of government's economic management, the investment climate, the effects of bureaucracy on decision-making, and so on. Not surprisingly, investment policy reforms tend to rely on what seems to be obvious relationships and areas where specific action can be taken such as tax rates, investment laws and regulations, bilateral treaties, institutional factors and so on. These all carry different weights in different countries, and therefore a common investment function applicable to all countries will be hard to find.

Accumulation policies in a liberalizing environment

There are many factors which impact on growth. Among them are technological innovation, a boom in exports, capital inflows, discovery and exploitation of some major natural resource and so on. Most countries, however, have found it difficult to sustain high growth rates over a long period of time. The ability of a few countries in South East Asia to do this has been associated with a significant increase in savings and investment rates. Savings rates in these countries were lower than in Latin America in 1965, but by 1990 they exceeded Latin America's by almost 20 percentage points. At the same time while investment levels were about equal in Latin America and East Asia in 1965, by 1990 East Asia's investment rates were nearly double the average for Latin America.¹⁶

As can be seen in Table 5 the growth in per capita GNP of over 5 per cent per year is associated with savings and investment rates of over 30 per cent.

Current savings and investment rates in some Caribbean countries compare favourably with those in developed countries such as Canada, France, Germany and the United States. In the industrialized countries as a group the saving rate has been averaging around 22 per cent per year in the 1990s as compared to 21 per cent for domestic investment. An observation made with respect to the performance of fast growing developing countries, however, is worth noting. "We often fail to appreciate just how spectacular the rate of accumulation has been in the Third World compared to past historical standards. It took America more than six decades to do what the Third World has done in two or three: that is the investment ratios in the successful developing countries today are what they were in America in 1900 after 60 years or more of industrialization. In the absence of government intervention, the rate of accumulation in England during the first Industrial Revolution was about a third of that in contemporary LDCs and the saving rate was less than half."¹⁷

A relevant question here is why are some countries with reasonably high saving and investment rates not growing at the desired rate, or not narrowing the gap with the developed countries. Part of the answer may lie not only in the level of investment taking place, but where is the investment taking place and is it raising capital formation in strategic sectors of the economy. Is it raising productivity and is it developing the human capital resources needed for growth. Is the appropriate mix between public and private investment being achieved. While recognizing these issues, there is a view that even at current income levels, the Caribbean is capable of saving and investing a much higher proportion of national income. This, it is often argued, would reduce dependency on foreign savings and minimize the problems associated with foreign indebtedness.

What should be the target? One observer has suggested that if population growth can be controlled at 1 per cent per annum and GDP can grow at 6 per cent per annum, per capita income can double every 14 years. To achieve this level of growth performance the region requires "increased and more productive investments. Gross investment of at least 35 per cent of GDP at an incremental capital output ratio (ICOR) below 3 would help the Region to achieve its per capita income target."¹⁸ As indicated before, capital accumulation is a necessary, though not sufficient, condition for growth.

Development policy and the macroeconomic framework

In the Caribbean, both the countries that have undertaken structural adjustment programmes either on their own or in collaboration with the International Monetary Fund (IMF) and the World Bank, as well as those that performed reasonably well in the 1980s, face certain common development and management challenges. Periodic favourable growth performances often mask deep-seated structural problems that contribute to vulnerability and instability. Though there have been some changes in the structure of the economy inherited from the colonial period, in essential ways the functioning of the economy has not changed. The Caribbean economies produce largely for foreign markets and satisfy almost all their consumer and industrial needs from abroad. The

export base, however, is a weak one consisting largely of agricultural and mineral products exported in raw or semi-refined form. Two of the major resource-based exports, sugar and bananas, are produced at relatively high cost and require special marketing arrangements to survive. Foreign earnings are not only affected by changes in market conditions but by natural factors such as hurricanes, drought and disease. The emergence of tourism has strengthened the foreign exchange earnings capacity of the region, but this activity itself operates in an unpredictable environment.

If the refining and processing of natural resources are excluded from the manufacturing sector, the latter for the most part revolves around a few simple activities reflecting the failure of the import substitution strategy pursued since the 1950s and particularly since the 1960s. The approach was generally the same as in Latin America where in order to encourage the domestic production of consumer imports previously imported, a range of incentives was offered, including the use of tariffs and non-tariffs restrictions to exclude competing imports. The incentives paid little attention to the effect on resource allocation and bore little relation to specific objectives such as employment and exports. In order to safeguard their local share of the domestic markets, traditional suppliers responded by entering into licensing arrangements with local distributors for the assembly or packaging of goods previously imported in 'whole' form. In most cases local value added was small and some of the licensing arrangements explicitly prohibited exports. In the absence of a long-term sequencing strategy, the manufacturing sector in the Caribbean has proceeded little beyond the assembling and packaging of simple consumer products for the local and regional markets. The emergence of the highly capital intensive gas-based industries in Trinidad and Tobago's production landscape has to be seen as a distinct operation not related to the broader import substitution process associated with low value-added activities.

The 'new' production configuration reflected prevailing consumption patterns and income distribution. The small size of the domestic markets effectively removed the benefits of economies of scale and led to high per unit cost of production. The emergence of monopolies in various product lines encouraged poor quality goods and allowed earnings (economic rent) that were higher than could be earned from exports. In this sense the strategy had a strong built-in bias against exports. Imports of raw materials and capital goods have relied heavily on foreign exchange earned by the traditional resource based exports and tourism. Final consumer goods imports may have fallen, but imports of raw materials, intermediate imports and capital goods would have increased, resulting in little net foreign exchange saving. With the decline of agriculture the region has become increasingly dependent on imported food. Some import substitution activities, for example motor car assembly in Trinidad and Tobago, not only involved a considerable wastage of capital, but their inefficiency led to a severe exploitation of the local consumer.

As a strategy to broaden the production and export base of the economy and increase employment opportunities, the import substitution strategy pursued in the Caribbean has been a dismal failure. Unintentionally, perhaps, the incentives that were granted favoured capital intensive techniques of production and carried an anti-export bias. An environment of perpetual protection removed the incentives for greater efficiency. Initially, the infant industry argument was used to rationalize the protective structure, but with the persistence of high unemployment rates, protection

was often reinforced by other policies which militated against the development of the tradable goods sector. Policies to encourage manufacturing based on natural resources either at the country or regional level were never strongly embraced, though the benefits of such policies were widely recognized.

The failure of the manufacturing activities to emerge as a significant sector in Caribbean economies and the relative neglect of agriculture, have raised several issues relating to resource allocation and the development options open to the small Caribbean economies in a fast changing world. One reason for the emphasis placed on manufacturing relates not only to its potential for exports, but because of the opportunities offered for employment and increasing productivity. The inward-looking policy framework, however, effectively stymied the possibilities for expansion and the transformation of the economy.

The contribution of manufacturing to GDP is generally less than 10 per cent in Caribbean countries. Most of the activities are centred around simple manufactures including the processing of agricultural products. For example, in Trinidad and Tobago if we exclude petrochemical and oil refining from the sector, food, beverages and tobacco alone account for over 40 per cent of value-added of the total manufacturing contribution. With respect to employment, the sector in Barbados and Trinidad and Tobago accounts for about 10 per cent of the employed labour force.

The share of agriculture in GDP has been declining in almost all Caribbean countries (see Table 11). In Trinidad and Tobago it contributes 2 per cent as compared to 20 per cent in Belize. Agricultural exports have also been declining in most countries. In some countries, however, agriculture is still a significant employer of labour though agricultural employment as a proportion of the labour force has also been falling. In 1995, 68 per cent of the labour force in Haiti was agriculture, 11 per cent in Trinidad and Tobago, 24 per cent in Jamaica and 33 per cent in Belize.

The Caribbean economies are now highly oriented to services, which in most cases account for over 75 per cent of GDP. Tourism dominates the economy of Aruba, Antigua and Barbuda, Bahamas and Barbados and makes a significant contribution in Jamaica and the OECS. Following the example of the Bahamas and the Cayman Islands, some countries have attempted to encourage offshore financial activities with varying degrees of success. In all the Caribbean countries, tourist expenditure has been increasing (See Table 12), but the high import content and the limited linkages with other sectors of the economy have reduced the potential benefits of the activity to the region. The potential of the large numbers of visitors to the Caribbean as a market for a range of locally produced goods and services has not been fully exploited. While there are undoubted benefits accruing from tourism, the activity also has a downside in terms of its effect on the environment and on the price of land to nationals. In these areas public policy cannot remain unconcerned.

Table 11

Composition of GDP (at Current Factor Cost), 1970-1995

Countries	Agriculture ¹				Mining and Quarrying				Manufacturing				Utilities and other services			
	1970	1980	1990	1995	1970	1980	1990	1995	1970	1980	1990	1995	1970	1980	1990	1995
OECS																
Antigua & Barbuda	5	7	4	4 ^a	-	-	2	2 ^a	12	5	3	2 ^a	83	88	91	92 ^a
Dominica	32	31	25	19	-	1	1	1	6	5	7	7	62	74	63	73
Grenada	20	25	17	10	-	-	-	-	4	4	5	6	76	71	78	84
Montserrat	17	4	3	6	-	1	1	1	-	6	2	3	83	89	94	90
St. Kitts-Nevis	30	16	6	6	-	-	1	-	3	15	13	10	77	69	80	84
St. Lucia	16	12	15	10	-	1	1	1	3	9	8	7	81	78	76	82
St. Vincent	24	15	19	13	-	-	-	-	3	11	9	9	73	74	72	78
Other CARICOM																
Bahamas	..	..	3	3 ^b	..	..	-	-^b	..	..	3	3 ^b	..	..	94	94 ^b
Barbados	14	10	5	6	-	1	1	1	10	12	8	7	76	77	86	86
Belize	..	30	22	20	-	-	1	1	..	16	16	14	..	54	61	65
Guyana	19	28	43	41	20	16	10	16	12	12	9	11	49	44	42	32
Haiti	..	..	..	32 ^c	..	..	..	-^c	..	..	..	15 ^c	..	..	..	53 ^c
Jamaica	7	9	7	9	13	15	9	7	13	11	19	18	67	65	73	66
Suriname	..	..	11	23 ^d	-	-	3	2 ^d	-	-	13	14 ^d	..	..	73	61 ^d
Trinidad & Tobago ^e	6	2	2	2	22	42	24	27	9 ^f	6 ^f	7 ^f	8 ^f	63	50	67	63

.. not available

a. 1994

c. 1988

e. GDP at market prices

1. including forestry and fishing

- nil or negligible

b. 1992

d. 1993

f. excludes oil refining and petro chemical industries

Source: CDB; ECLAC; National Publications

Table 12
Tourist Expenditure, 1980-1996 (US\$m)

Countries	1980	1985	1990	1995	1996	<u>1995 Exp.</u> as a % of GDP
Antigua	42	133	250	200	237	40
Aruba	138	121	353	521	604	..
Bahamas	595	995	1,333	1,346	1,450	39
Barbados	251	309	494	1,231	1,302	66
British Virgin Islands	42	68	132	..	..	..
Cuba	48	116	268	1,100	1,350	..
Dominica	3	9	25	28	30	13
Dominican Republic	168	368	750	1,552	1,747	13
Grenada	15	32	34	72	74	27
Guadeloupe	111	95	231	..	..	..
Haiti	46	69	75	90	96	..
Jamaica	242	407	740	1,069	1,128	21
Martinique	75	93	240	..	..	..
Montserrat	4	8	11	..	..	..
Netherlands Antilles	260	225	449	591	579	..
Puerto Rico	615	723	1,377	1,827	1,898	..
St. Kitts-Nevis	13	31	63	58	61	25
St. Lucia	33	90	154	204	210	39
St. Vincent	14	23	46	47	48	18
Suriname	18	9	11	..	..	..
Trinidad and Tobago	151	197	95	..	..	..
U.S. Virgin Islands	304	507	707	..	..	..

.. not available

Source: *ECLAC*.

The macroeconomic environment

In the early 1960s, diversification of the economy, full employment and greater self-reliance were seen as major objectives of development policy. Against a background where Caribbean economies were driven by external factors and where key sectors of the economy were in foreign hands, the need to reorient the functioning of these economies and reduce economic dependence were seen as an essential part of the transformation process. With a weak private sector, the State itself took the lead role in nationalizing what it saw as the 'commanding heights' of the economy, and assumed the role of 'engine of growth.' In addition to its welfare responsibilities, the State's involvement in the economy varied from country to country. Guyana was an extreme case. By 1988, the Government had not only nationalized the major productive sectors, but controlled over 80 per cent of recorded import and export trade and 85 per cent of total investment.¹⁹

Between the late 1960s early 1970s there was growing concern over the failure to diversify the economy and achieve growth and employment targets. In Trinidad and Tobago, the unemployment rate showed a steady increase between 1970 and 1975. In 1973 foreign reserves reached its lowest point in many years, but the increase in oil prices in the 1970s significantly changed the picture. In Barbados and Jamaica the unemployment rate also exceeded 20 per cent by the mid-1970s, and while in Barbados the rate fell in the early 1980s, in Jamaica it continued to climb reaching over 27 per cent by the end of the decade. While Trinidad and Tobago as an oil producer benefited from the oil shocks of the 1970s, the oil importing countries of the region were severely affected. By 1976 the net foreign reserves position of both Guyana and Jamaica had already turned negative, and were to worsen further in the 1980s with the reduced earnings from the major traditional exports.

The 1980s was a particularly difficult period for the larger Caribbean States. Between 1976 and 1980 the Barbadian economy grew by an average rate of 5 per cent, but by 1992 total output was lower than the 1980 level. In Trinidad and Tobago, the decline of oil prices in the early part of the decade had an immediate impact on the reserves and revenue position of the government, but the full fiscal implications were delayed for a few years as the government drew on the public sector savings of previous years. The country's foreign reserves dropped from US\$3,348 million at the end of 1981 to US\$127 million at the end of 1988. In Guyana, total output declined by 25 per cent between 1980 and 1990 while export earnings dropped by almost 50 per cent between 1980 and 1990. Reflecting the inability of capital inflows to cover the current account deficits, foreign reserves moved from US\$58.3 million in 1978 to US\$4 million in 1988 and to US\$29 million in 1990. In Jamaica the economy grew at an average rate of around 2.2 per cent in the 1980s, but the 1990 output level was about the same as that of 1973. Despite a favourable balance on the services account, this could not offset the persistent trade deficits and the effects on foreign reserves which were equivalent to a little over one month's imports in 1990. The OECS grew at an average rate of over 5 per cent per year and were in a stronger position at the end of the decade. The deteriorating economic performance in the larger Caribbean States in the 1980s was reflected not only in output levels, but in employment and social conditions. In Trinidad and Tobago, for example, the unemployment rate increased from 9 per cent in 1980 to 20 per cent in 1990. The initial reaction by the State in the Caribbean to the

foreign exchange and revenue crisis in the 1980s was to increase borrowing, rather than institute fiscal and other adjustment measures.

Table 13
Unemployment Trends, 1980-96

Countries	1980	1985	1990	1991	1992	1993	1994	1995	1996
<u>Selected</u>									
<u>CARICOM Countries</u>									
Antigua & Barbuda	20.5	..	6.8	6.7	7.8	6.7	7.4	..	..
Bahamas	16.6	12.2	12.0	12.3	14.8	13.1	13.3	11.1	12.0
Barbados	11.4	18.7	15.0	17.3	23.0	24.3	21.9	19.7	16.4
Belize	..	15.1	14.8	13.8	11.9	9.8	11.1	12.5	13.7
Jamaica	27.3	25.0	16.0	15.7	15.4	16.3	15.4	16.2	16.0
Montserrat	5.4	5.3	1.0	6.0	9.0	10.0	8.3	..	..
Suriname	..	..	16.0	..	17.2	14.6	..	..	..
Trinidad & Tobago	8.7	15.3	20.0	19.0	19.7	19.8	18.4	17.2	16.3
<u>Other Caribbean Countries</u>									
Aruba	..	..	..	..	0.6	0.5	0.5	0.7	0.6
Dominican Republic	..	..	19.0	19.0	20.0	21.0	16.0	16.0	17.0
Netherlands Antilles	..	..	..	14.6	13.9	13.6	12.8	13.1	..

not available

Sources: *IDB; CDB; ECLAC.*

Generally, both the public domestic debt and public external debt grew in the 1970s and this trend continued into the 1980s. In Barbados, the outstanding external debt as a proportion of GDP increased from 9 per cent in 1970 to 19 per cent in 1981. In Guyana, it moved from 30 per cent in 1970 to 112 per cent in 1981 and in Jamaica from 16 per cent to 77 per cent over the same period. As can be seen in Table 14, borrowing by all countries increased during the 1980s in varying degrees. In most of the OECS countries and Belize, with the improving fiscal positions and capital inflows, particularly in the latter part of the 1980s, public debt did not increase as quickly as it did in the larger countries, where public revenues came under sustained pressure largely as a result of the performance of the external sector.

The increase in debt service payments in the 1980s accompanied by depressed earnings from exports resulted in a significant increase in the debt service ratio for some countries. A few had difficulty meeting debt service obligations. Guyana had already reached this position as far back as 1981. The scheduled debt service ratio for this country increased from 24.4 per cent in 1981 to 98.4 per cent in 1989. The actual ratio in the latter year was 11.5 per cent. In the case of Trinidad and Tobago, the ratio increased from less than 3 per cent in the early 1980s to over 20 per cent in the early 1990s, a trend reflecting the movement in oil prices.

In the 1990s, the outstanding external debt has increased in a few cases, but the debt of the largest debtors has fallen. The debt service ratio has also come down, as a result of the maturing of some loans, write-offs and rescheduling. It would be wrong to conclude from this, however, that the public debt is no longer an issue. In Guyana interest paid on the public debt in 1995 amounted to 40 per cent of current expenditure as compared to 43 per cent for Jamaica.

Table 14
Growth of the Outstanding External Debt, 1981-96

Countries	External Debt (US\$)			Debt as a % of GDP ¹			Debt Service Ratio ²		
	1981	1991	1996	1981	1991	1996	1981	1991	1996
OECS									
Antigua	57.7	260.0	223.6	46.0	61.6	48.3	8.2	2.2	1.5
Dominica	17.0	84.8	104.3	28.8	47.8	46.5 ^a	3.4	4.2	6.7 ^a
Grenada	17.1	85.9	89.3	17.6	40.9	36.6 ^a	3.7	4.3	4.9 ^a
Montserrat	2.0	3.4	10.0	9.9	5.7	..	2.4	2.0	1.8 ^a
St. Kitts-Nevis	10.8	36.8	54.3	20.9	21.5	23.2 ^a	3.0	2.7	1.2 ^a
St. Lucia	17.8	70.2	126.8	13.6	16.7	20.5 ^a	1.3	2.0	2.8 ^a
St. Vincent	15.6	58.7	87.4	21.2	26.2	31.8 ^a	1.6	3.5	5.2 ^a
Other CARICOM									
Bahamas	98.0	412.3	357.8	7.9	14.3	10.5	4.7	4.2	5.2
Barbados	176.1	466.6	362.9	19.0	27.5	24.0	2.6	19.6	14.2
Belize	54.5	150.6	216.9	34.8	41.4	42.0	1.4	6.7	9.5
Guyana	635.7	1,855.3	1,499.0	112.0	350.4	209.0	21.7	20.3	20.0
Haiti	423.0	906.0	800.0	26.1	35.8	28.0	9.2	10.2	..
Jamaica	2,293.1	3,874.4	3,231.9	76.9	119.6	59.2	28.6	25.7	19.9
Suriname	26.0	123.0	162.5	5.1	..	30.6	0.6	..	4.3
Trinidad & Tobago	1,050.0	2,195.4	1,875.7	15.3	67.0	36.5	2.4	20.0	13.7
Other Caribbean Countries									
Dominican Republic	2,255.0	4,492.0	4,200	31.0	59.1	31.9	34.7	14.0	16.1

.. not available

a. 1995

¹ At market prices

² Debt service payments as a % of export of goods and services

Sources: ECLAC; Caribbean Development Bank; IMF, Country Reports.

Export earnings not only help to define import capacity, but also influence public revenues and governments' ability to spend. The variability in recurrent revenue and the tendency for recurrent expenditure to increase at a faster rate than revenues result in public sector savings being very erratic. Rarely does public sector savings exceed 5 per cent of GDP. Increased debt service payments associated with the growth of the public debt have made it more difficult to save. In the OECS though the debt service ratios may appear relatively low, interest payments alone may be taking between 10 and 20 per cent of current revenues. Pressures on the central government finances have also come from the subsidization of poorly run government-owned or controlled public utilities and a range of State-owned enterprises, some of which were acquired as money-losing concerns. The failure of governments, to transform State-owned producing concerns into efficient enterprises not only had fiscal implications but seriously undermined the performance of the State in the capacity of 'engine of growth.'

Public sector investment programmes have depended heavily on borrowed funds and grants. The overall fiscal deficits as a per cent of GDP in the 1980s averaged 4.2 per cent in St. Lucia, 1.6 per cent in the Bahamas and 5.7 per cent in Belize, but was much higher in some of the other countries, for example, Grenada (24 per cent), Guyana (44 per cent) and Jamaica (14 per cent). The measures taken to improve the government's savings in Guyana, Jamaica and Trinidad and Tobago had a positive effect on the financing position in the 1990s as reflected in the overall deficit to GDP ratios. The division of financing between domestic and foreign sources varies widely from country to country. The OECS with their restricted access to the international capital markets have relied heavily on external concessional assistance to finance development programmes. With respect to borrowing from the Central Bank, control is exercised not only through the provisions of the Bank's Charter but the multinational ownership of the Bank makes it difficult for any member government to abuse its borrowing prerogatives. In the case of the larger countries, borrowing from the domestic banking system was more significant and in the case of Jamaica and Guyana particularly, this was accompanied by a significant increase in the inflation rate. By the early 1980s, outstanding accommodation to the governments of these two countries, had already accounted for over 80 per cent of the total assets of the respective Central Banks, and this position was maintained throughout the 1980s. In Trinidad and Tobago, the government also increased borrowing from the Central Bank in the later 1980s to finance its activities when budgetary savings declined. With the adoption of stabilization programmes, the deficit/GDP ratio has generally come down to less than 5 per cent in the 1990s (See Table 15).

Table 15
Central Government Overall Surplus or Deficit (-)
as a % of GDP

Year	Bahamas	Barbados	Belize	Guyana	Haiti	Jamaica	Suriname	Trinidad & Tobago	OECS
1980	-2.6	-5.2	-4.5	-31.8	5.4	-17.3	1.3	7.0	..
83	-14.1	-3.3	0.4	-46.0	-3.8	-15.9	-17.0	-12.0	..
84	-7.2	-5.2	7.1	-94.0	-7.4	-6.2	-16.0	-8.8	..
85	-4.5	-5.2	-0.8	-33.8	-3.5	-6.0	-20.0	-7.2	..
86	-0.5	-5.3	-4.5	-58.8	-2.1	0.3	-26.0	-5.9	..
87	-0.6	-5.3	0.4	-42.4	..	1.5	-24.8	-5.9	..
88	-3.0	-2.3	7.1	-31.6	..	-1.5	-21.3	-5.7	..
89	-4.1	-0.8	-0.8	-6.6	..	-0.2	-14.0	-4.2	..
90	-2.4	-6.7	0.7	-22.9	-1.3	3.0	-6.3	-1.2	..
91	-4.3	-2.1	-4.1	-20.5	-0.5	4.4	-17.4	-0.2	-1.7
92	-2.3	-1.1	-6.2	-10.5	-2.8	4.2	-11.2	-2.8	-2.0
93	-0.7	-0.1	-6.7	-7.6	-3.8	3.5	-8.3	-0.2	-2.1
94	-0.6	-1.8	-7.4	-3.8	-4.3	1.9	-2.3	0.0	-1.9
95	-0.7	1.1	-4.1	-5.8	-1.9	1.0	0.4	0.2	-2.7
96	-1.9	-3.1	-1.1	..	..	-8.3	..	1.6	-2.4

.. not available

Source: IDB, Economic and Social Progress in Latin America, Various Issues, ECCB.

The balance of payments problems and indirectly the fiscal challenge that confronted Caribbean countries in the 1980s was fundamentally a terms of trade problem that was largely the result of changes taking place in the global economy and the effects of these on traditional exports. With a rising import bill, the absence of a dynamic, competitive export sector undermined the region's ability to benefit from the expanding world economy. External borrowing was used to help counter the external deficits, but the basic problems were more structural and required a different approach. The use of the printing press to finance fiscal deficits in certain cases was quickly reflected in prices, pressure on the exchange rate and worsening of the balance of payments situation. Caribbean countries do not have a tradition of using the Central Bank to finance expenditure, and generally the inflation rates reflect price movements in their major trading partners. In the 1960s inflation rates averaged less than 5 per cent per annum in the Anglophone CARICOM States and this has continued to be the case for most countries (see Table 16). A figure of more than 10 per cent is rare. Guyana in the 1980s, Jamaica since the mid-1970s and Suriname in recent years have experienced inflation rates that are not typically Caribbean. All three countries are associated with fairly large depreciations of the nominal exchange rate.

Table 16
Inflation Rates in Selected Countries
(Percentages)

Countries	Average		1991	1992	1993	1994	1995	1996
	1970 - 1980	1980 - 1990						
Bahamas	8.1	6.8	7.1	5.7	2.7	1.4	2.1	1.4
Barbados	14.5	7.2	6.3	6.1	1.1	0.0	1.9	2.4
Belize	..	5.0	2.3	2.3	1.4	2.6	2.9	6.4
Dominica	..	7.2	5.6	5.5	1.6	0.0	1.3	1.7
Grenada	..	8.4	2.6	3.8	2.8	2.6	3.0	..
Guyana	10.6	19.7	2.3	2.6	..	..	..	..
Haiti	11.0	8.7	15.4	19.4	22.6	42.6	25.5	17.1
Jamaica	20.0	17.8	51.1	77.3	22.1	35.1	19.9	26.4
St. Kitts-Nevis	..	5.2	4.2	2.9	1.8	2.6	2.7	2.5
St. Lucia	15.3	6.2	5.7	5.1	0.8	5.8	2.7	..
St. Vincent & Grenadines	..	6.2	5.5	3.5	4.3	1.0	1.7	4.4
Suriname	10.2	15.1	26.0	43.7	143.5	368.5	235.6	..
Trinidad & Tobago	13.6	12.8	3.8	6.4	10.8	8.8	5.2	3.4
Brazil	38.8	513.4	440.9	1,008.7	2,148.4	2,668.5	84.4	18.2
Chile	178.0	24.0	21.8	15.4	12.7	11.4	8.2	7.4
Mexico	17.3	60.3	22.7	15.5	9.8	7.0	35.0	34.4
USA	8.4	6.1	4.2	3.0	3.0	2.6	2.8	2.9

.. not available

Sources: IMF, *International Financial Statistics*, Various Issues.

The exchange rate had not been actively used as an adjustment mechanism in the Caribbean until the 1980s, and this only in some countries. As can be seen in Table 17 the rates continue to remain fixed for long periods in certain States. There is a great deal of controversy surrounding the effectiveness of exchange rate changes in correcting external disequilibrium in countries without a manufacturing base and dependent on external sources for not only a wide range of consumer goods, but for food, intermediate materials and capital goods. Rather than increase exports and reduce imports, as the textbooks suggest, devaluations or depreciations, can lead to increases in domestic prices and demands for higher wages and salaries which, in turn, may require further adjustments in the exchange rate. In Guyana, despite significant depreciation between 1980 and 1995 there was a persistent trade, current account and overall deficit in the balance of payments, throughout the period. In Jamaica, too, where there was significant depreciation between 1980 and 1995 the trade balance was persistently negative, while the current account was positive in only three years. In Trinidad and Tobago, where the depreciation was not as rapid, the recovery in the price of oil from the low point of 1986 may have been a more significant influence in the recurring positive trade balances since 1987 than the depreciation of the currency. The persistence of the external

imbalances in the face of a decline in real wages reflects the structural nature of the problem which could not be resolved by simply changing import and export prices.

With greater fiscal discipline and a strong foreign reserves position, the OECS countries have been able to hold a fixed exchange rate. However, the use of the exchange rate to stimulate exports in the short term is acknowledged to be limited with the prices of major exports quoted in foreign currency and a small manufacturing sector. With the fall in output by 12 per cent between 1989 and 1993 and the precipitous decline in foreign reserves during the period, Barbados came under pressure to devalue its currency but opted to reduce domestic costs and increase productivity. The current surplus of the balance of payments has averaged 6.3 per cent of GDP since 1992.

The continuous depreciation of some of the region's currencies since the early 1980s as part of the effort to correct large external imbalances has raised the issue of confidence in societies not accustomed to seeing such large and frequent changes in the external value of their currencies. Some national currencies have lost a great deal of credibility as a store of value, a function which is being increasingly performed by the United States dollar. With the relatively high inflation rates in certain countries and the continuous fall in the external value of the currency, holding savings in foreign currency accounts even when the latter are associated with a lower rate of return, is seen as a way of safeguarding the value of savings. Interestingly, even in countries with a history of low inflation rates, like Trinidad and Tobago, there is a strong propensity for residents to hold their savings in United States dollars, and this raises questions about confidence in the currency. The removal of foreign exchange controls and the freedom to hold foreign currency accounts in local banks facilitates the process of flight from the local currency. Even where the foreign currency accounts are held in local banks, these accounts can be seen as a conduit out of the domestic savings stream, if the resources from these accounts are not used in the interest of the local economy. Paradoxically, the very arrangements which are being put in place to attract foreign capital can be exploited to take savings out of the domestic system.

Table 17
Nominal Exchange Rates, 1970-96
(Domestic Currency Per US Dollar)

End of Period	Bahamas	Barbados	Belize	EC	Guyana	Jamaica	Trinidad & Tobago	Haiti	Dominican Republic	Suriname
1970	1.00	2.01	1.67	2.00	2.00	0.84	2.00	4.99	1.00	1.88
1980	1.00	2.01	2.00	2.70	2.60	1.78	2.40	4.99	1.00	1.78
1985	1.00	2.01	2.00	2.70	4.20	5.48	3.60	4.99	2.94	1.78
1986	1.00	2.01	2.00	2.70	4.40	5.48	3.60	4.99	3.07	1.78
1987	1.00	2.01	2.00	2.70	10.00	5.50	3.60	4.99	4.96	1.78
1988	1.00	2.01	2.00	2.70	10.00	5.48	4.25	4.99	6.34	1.78
1989	1.00	2.01	2.00	2.70	33.00	6.48	4.25	4.99	6.34	1.78
1990	1.00	2.01	2.00	2.70	45.00	8.04	4.25	4.99	11.35	1.78
1991	1.00	2.01	2.00	2.70	122.00	21.49	4.25	8.24	12.66	1.78
1992	1.00	2.01	2.00	2.70	126.00	22.19	4.25	10.95	12.57	1.78
1993	1.00	2.01	2.00	2.70	130.00	32.47	5.81	12.80	12.77	1.78
1994	1.00	2.01	2.00	2.70	142.50	33.20	5.93	12.95	13.06	409.50
1995	1.00	2.01	2.00	2.70	140.50	39.62	6.00	16.16	13.46	407.00
1996	1.00	2.01	2.00	2.70	141.30	34.86	6.19	15.09	14.06	401.00
1997 ^a	1.00	2.01	2.00	2.70	142.30	34.98	6.25	16.50	14.33	401.00

a. End of March

Source: IMF, *International Financial Statistics*, Various Issues.

Table 18
Real Effective Exchange Rate Index, 1986-96
(Base = 1990)

Year	Antigua	Bahamas	Barbados	Belize	Grenada	Guyana	Jamaica	St. Lucia	Dominican Republic	Haiti	Suriname	Trinidad & Tobago
1986	104.9	105.3	92.3	116.1	119.1	276.2	94.8	112.8	117.7	72.2	76.4	113.9
1987	100.6	103.2	98.7	107.7	107.1	142.2	95.7	110.7	100.8	82.1	93.0	105.6
1988	100.1	101.7	101.3	106.4	104.0	179.2	95.5	103.6	84.2	87.6	68.6	99.1
1989	101.2	103.7	97.8	104.9	108.7	141.6	89.2	105.6	101.8	89.5	85.1	97.7
1990	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
1991	100.6e	103.1	98.2	101.3	99.3	85.4	111.1	101.9	102.2	129.7	84.7	100.4
1992	100.3e	105.9	95.4	99.2	98.4	93.8	127.8	104.5	103.0	131.3	90.6	102.5
1993	106.6e	108.4	94.5	101.6	103.6	102.3	111.8	108.4	107.0	124.7	115.8	92.5
1994	106.8e	104.1	93.1	97.0	103.0	102.0	95.0	108.8	106.4	124.7	101.3	85.4
1995	103.4e	100.5	91.7	94.7	98.4	103.2	94.6	109.3	105.2	125.0	69.8	83.7
1996	105.0e	101.0	..	96.6	100.5	111.5	..	..	105.6	..	..	85.2

.. not available

e. estimated

Source: IMF, International Financial Statistics, Various Issues.

Table 19

Current Account Surplus/Deficit (-) of the Balance of Payments
as a % of GDP

Year	Bahamas	Barbados	Belize	Guyana	Jamaica	St. Lucia	Trinidad & Tobago
1980	-5.8	-2.5	..	-22.2	-5.0	-34.0	5.7
1981	-9.4	-12.4	..	-32.3	-10.3	-36.0	6.0
1982	-7.8	-3.7	..	-29.5	-11.6	-26.9	-7.5
1983	-6.8	-4.1	..	-32.3	-9.4	-4.1	-12.1
1984	-6.3	1.4	-2.5	-22.1	-13.3	-10.2	-6.0
1985	-0.1	4.2	4.4	-21.1	-13.0	-6.7	-0.6
1986	1.1	0.5	5.2	-25.2	-0.8	-3.1	-8.6
1987	-2.4	-1.3	3.4	-35.0	-4.1	-6.0	-4.7
1988	-2.6	2.8	-0.8	-24.2	1.3	-6.7	-2.0
1989	-2.7	1.5	-5.3	-31.8	-6.9	-20.7	-0.9
1990	-1.1	-0.6	3.8	-37.8	-7.3	-11.3	9.0
1991	-5.8	-1.6	-6.0	-34.0	-6.4	-16.7	0.0
1992	1.3	8.8	-6.0	-33.6	0.9	-11.4	0.6
1993	2.4	4.1	-9.2	-25.1	-4.4	-10.0	-2.3
1994	-0.8	7.5	-7.2	-18.7	0.4	-10.4	4.5
1995	-4.0	4.7	-2.9	-19.0	..	-5.5	5.2
1996p	..	7.4	-1.8	..	..	..	0.8

.. not available

Source: IDB ; CDB; ECCB.

Towards a new policy framework

Notwithstanding the growth experienced by some Caribbean States in the 1980s, external shocks revealed serious weaknesses in the economic structure and shortcomings in economic policies. In Guyana, Jamaica, Trinidad and Tobago and Suriname the decline of foreign earnings, the emergence of balance of payments problems, the drop in foreign reserves, increasing government indebtedness and the pressures on the government revenue reflected the emergence of a serious crisis. The limited effect of the short term stabilization measures and the persistent difficulties facing economic management pointed to more serious structural problems relating the failure of development policies and the changes that had taken place in the international policy environment. Some countries such as Guyana, Jamaica and Trinidad and Tobago sought financial and technical assistance from the International Monetary Fund and the World Bank which by this time had already began to link stabilization measures with policy reforms designed not only to reduce internal and external deficits, but to increase efficiency in the economy.

Structural adjustment packages addressed development strategy, competition and protection policy, the role of government in the economy, incentives, market structures, tax reforms, subsidy policies, financial reforms and the exchange rate. In this new approach, private sector development was to be encouraged and market forces envisaged to play a greater role in resource allocation. A more active role was assigned to the exchange rate which was supposed to reflect more closely, the true value of the currency. To increase public sector savings, government expenditures were reduced on many fronts, including the social services, and subsidies to goods and services sharply curtailed. In some instances wages and salaries were cut and the public sector workforce reduced, thus increasing the number of unemployed. In keeping with the objectives of a more circumscribed role for government and strengthening public revenues, inefficient and money-losing government enterprises were to be sold to private interests. Increasing exports was to be a major goal in redressing the external imbalance and this was predicated on a more open and competitive economy. Many forms of quantitative restrictions on imports were removed in favour of lower tariffs, and the exchange control regime modified. In certain countries, for example Trinidad and Tobago, Guyana and Jamaica, the fixed exchange rate system was abandoned in favour of more flexible exchange arrangements. Growth was seen to hinge on a higher level of domestic and foreign savings. Greater openness required the removal of restrictions on foreign private investment and the adoption of regulations to encourage capital flows. In most countries the financial regulations have been updated to increase confidence in the sector and a more competitive and liberalized framework is increasingly being put in place.

Not all economies respond in the same way or in the same time-frame to a given set of incentives or stimuli. The stabilization/structural reform package has accordingly had mixed results in the Caribbean. The cuts in government expenditure which have included areas such as education and health have worsened social conditions. Reductions in government employment have also helped in creating a group of new poor to add to the existing chronic poor thus worsening the climate of social and political instability. Financial constraints bedeviling Caribbean governments have also impacted on maintenance and capital programmes, leading to a deterioration of the social and

economic infrastructure. The state of schools, hospitals, roads, government buildings and bridges reflects governments' reduced spending capacity. The deteriorating infrastructure has also negatively affected private investment since the state of the utilities and infrastructure has an influence on costs and competitiveness.

With stabilization, some degree of growth has returned in the 1990s to countries that underwent serious stress in the 1980s. In Guyana where output in 1992 was still 27 per cent below that of 1976, real GDP has been growing by over 7 per cent per year since 1992. In Jamaica, too, there has been some growth, but output is yet to reach the level of 1982. The Haitian economy continues to flounder, while the Dominican Republic's economy has grown in every year except one (1990) since 1986. These trends in production do not tell the full story. There is no automatic link between growth and employment in these economies. Growth does not necessarily lead to higher real wages or improve the distribution of income. In all these economies the level of unemployment and social conditions remain a major concern. Reduction of public expenditure may improve the fiscal position, but can militate against human resource development and create conditions which do not encourage investment. The adoption of programmes intended to mitigate poverty has recognized this fact. Unfortunately, the ad hoc way in which they have been put together has reduced their effectiveness. Many of these programmes have suffered from lack of adequate resources, proper targeting and administrative problems. It is widely acknowledged that the reform measures intended to bring about the kind of transformation that could increase income and significantly reduce un-employment and poverty involve a more complex process and a longer time period. Experience has shown that in implementing reform measures account must be taken of several factors including the institutional framework, the relationship between government and civil society and governance. Initially, social alleviation programmes might stand alone but increasingly they have to be integrated in general development programmes designed to create employment and raise the income of the poor.

The challenge facing the Caribbean in the late-1990s

Several social and economic indicators reflect the gains made by Caribbean States over recent decades. Life expectancy at birth has increased to over 70 years in almost all the countries and this is comparable to the level reached in the developed countries. The infant mortality rate has also been falling, and the adult literacy rate is over 90 per cent in most cases. Ten Caribbean countries are ranked by the United Nations Development Programme (UNDP) as countries with high human development, i.e., with an index of over 0.800. In terms of per capita income, if Guyana and Haiti are excluded, per capita GNP in current dollars ranged between US\$900 for Suriname to almost US\$12,000 for the Bahamas in 1995. Despite the difficulties in the 1980s, real per capita income has grown in a number of countries since 1970. This, however, is only one side of the picture.

In the first half of the 1990s most countries of the region have returned to a positive growth path. The fiscal situation has been tightened and the pressures on the external account have been eased following the implementation of stabilization and structural adjustment measures. Foreign reserves have increased and the unemployment rate has fallen in some cases. The question of sustainability and policy reversal, however, remains a valid concern in a situation where there are

high levels of poverty amidst growing per capita incomes and an unfolding policy environment that must adjust to a more open trading framework. An estimate of the number of poor depends on the choice of a poverty threshold. According to a recent World Bank Report the number of people in the Latin American/Caribbean region living on less than US\$1 a day (in 1985 purchasing power parity prices) increased from 91.2 million (22.0 per cent of the population) in 1987 to 109.6 million (23.5 per cent of the population) in 1993. In other regions with the exception of Sub-Saharan Africa, the proportion declined.

Table 20
Selected Demographic and Social Statistics

Countries	Head Count Index (percentage poor)	Life Expectancy at Birth (1995)	Infant Mortality Rate (per 1000 live births) (1995)	Adult Literacy Rate (1994) %	Human Development Index Value (1994)	
CARICOM Countries						
Antigua & Barbuda	12	75	75	18	96.0	0.892
Bahamas	5	73	73	15	98.1	0.894
Barbados	8	78	78	13	97.3	0.907
Belize	35*	74	74	20	70.0	0.806
Dominica	33	73	73	17	94.0	0.873
Grenada	20	72	72	..	98.9	0.843
Guyana	43*	66	66	60	97.9	0.649
Haiti	65	57	57	72	44.1	0.338
Jamaica	34*	74	74	13	84.4	0.736
Montserrat	..	..	..	..	..	..
St Kitts-Nevis	15	69	69	31	90.0	0.853
St. Lucia	25*	71	71	17	82.0	0.838
St. Vincent	17	72	72	19	82.0	0.836
Suriname	47	70	70	33	92.7	0.792
Trinidad & Tobago	21*	72	72	13	97.9	0.88
Other Caribbean Countries						
Anguilla	..	..	..	..	..	..
Aruba	..	..	..	..	..	..
Dominican Republic	21*	71	71	37	81.5	0.718
Netherlands Antilles	..	77	77	11	..	..

.. not available

a. only those estimates, with an asterisk were calculated using a similar methodology

Sources: UNDP, Human Development Report, 1997; World Bank, World Development Indicators, 1997; J.L. Baker, Poverty Reduction and Human Development in the Caribbean, The World Bank, 1997.

With respect to the Caribbean itself, poverty varies from country to country and a recent study has estimated that it averages roughly 38 per cent of the total regional population varying from highs of 65 per cent for Haiti and 43 per cent for Guyana to 5 per cent for the Bahamas and 8 per cent for Barbados. "Income distribution is shared, though slightly less so than the average for Latin America. The poor include the elderly, children, the disabled, small scale farmers, unskilled workers, indigenous populations, and in some countries female-headed households and the under-employed or unemployed, many of whom are school leavers who have few skills with which to enter the labour market."²⁰ While stabilization and structural adjustment reforms may have worsened poverty through fiscal and exchange rate adjustments, the fact is that by the early 1980s the signs of decline were already evident as those countries had failed to transform traditional production patterns into more resilient structures capable of responding to global changes and sustaining higher levels of income and employment. Among the factors which have been identified as contributing to poverty in the Caribbean are low economic growth, macroeconomic instability, deficiencies in the labour market resulting in limited job growth, low productivity and low wages in the informal sector, and a decline in the quality of social services.²¹ In the Caribbean the increase in poverty has impacted particularly heavily on women, a high percentage of whom are heads of households with estimates for individual countries ranging from 22 per cent to 49 per cent. Unemployment rates are higher among women than men. In view of the role women play in caring for children and the elderly, cutbacks in subsidies to services like health and education have increased the burden on women.²²

The growth of total production and per capita income with the existence of high unemployment rates and the inequities in the distribution of income reflect the orientation of development policy. The paucity of data on employment and underemployment and the distribution of income may also reflect the reduced priority given to these concerns in the process of planning and strategy formulation. The separation of production objectives from employment and poverty reduction targets assumed a strong redistributive role for the State which by spending on education and health could enhance the employability and earning power of the expanding labour force. In light of the increasing focus that is being placed on human development and its role in the growth process, issues relating to the level of spending and the efficiency of delivery systems are coming under critical review in the context of a more rational approach to State intervention in the economy.

In most countries of the region, public educational expenditures as a share of GNP may have fallen between 1980 and the early 1990s, but the level of spending was not insignificant compared to many countries. In the early 1990s, the proportion for the Bahamas was 4 per cent, for Barbados 7.5 per cent, Guyana 5 per cent, Jamaica 6 per cent and Trinidad and Tobago 4 per cent. The comparable figure for Chile was 3 per cent, for the Republic of Korea 5 per cent and for Singapore 3 per cent. With respect to health, total public expenditure (including social security systems) as a per cent of GDP in 1990 averaged 3.6 per cent in Latin America and the Caribbean as compared to 6 per cent in the industrial countries and 1.28 per cent in East Asia. For individual countries the proportion for the Dominican Republic averaged 2.0 per cent in 1990-1995, Haiti 1.3 per cent, Jamaica 3.0 per cent and Trinidad and Tobago 2.6 per cent. The comparable figure for Mauritius

was 2.2 per cent, for Malaysia 1.4 per cent, for Singapore 1.1 per cent and for Thailand 1.4 per cent. These figures do not reflect private spending in the Caribbean.²³

The problem in the Caribbean it appears, is not so much the share of income devoted to health and education which had a positive impact in some areas, but the efficiency of the health and education systems and the returns to the national communities. Poorly managed health and education systems have not only resulted in the deterioration of the infrastructure but also in the quality of the workforce. Unemployment has been growing while the demand for certain kinds of skills remains unmet. An increasing number of graduates remain unemployed or take jobs for which they are not trained. Failure to find employment locally can also encourage emigration and this contributes to a waste of resources. Increasing the capacity of the State to spend depends on an expanding economy and when this does not happen, the competition for limited resources becomes increasingly intense. Only a small proportion of the population may be able to access private health and educational services. In developing societies, educational opportunities not only offer the means for transforming people into more productive factors but also help in reducing income inequities. The failure or inability to incorporate up-to-date technological progress in the production process has also contributed to the decline of productivity and stagnation in some sectors of the economy.

In 1975 real output per worker in Latin America and the Caribbean was higher than that of the high performing Asian economies (HPAEs) and the rest of Asia and Africa.²⁴ By 1985 this was still the case, but by 1992 the HPAEs had moved ahead with a productivity advantage of 32 per cent. In 1960 Barbados and Trinidad and Tobago had a higher real per capita GDP than both Hong Kong and Singapore, but by 1980 the latter two had soared ahead. Policy choices were a significant factor in these outcomes. The correction of cost and price distortions is not sufficient to engender growth. While a stable macroeconomic environment is necessary for rationalizing the production structure, micro and sectoral policies have a critical role to play. The failure to restructure and reorganize the agricultural sector, for example, has been a major failure of Caribbean economic policy. Land tenure problems, size of farms, the level of technology, access to credit, pricing policy, incentives and marketing problems have plagued this sector for years. Falling productivity and income have tended to make agricultural activities less attractive than the public sector and manufacturing where remuneration is generally higher. The growth of tourism and its ability to pay higher wages and salaries also reduced the attractiveness of agriculture. Policies to increase intersectoral linkages have also been lacking.

Not only have countries that are basically agricultural in nature become increasingly dependent on imported food, but opportunities to use the natural resource base of the countries to develop higher value added activities have been reduced. The flight of people from the rural areas has worsened social conditions in the urban communities. The public sector, with bloated bureaucracies and a wages and salaries bill that has reached 50 per cent of current expenditure in some cases, is being forced to 'down-size' given the pressure to generate savings. With the exhaustion of assembling and packaging opportunities in the manufacturing sector, the scope for producing only for the local market is limited. Even the regional market for low value added import

substitution products is saturated. The pressure to produce goods that can compete extraregionally is increasing.

Unemployment rates in the region remain high notwithstanding the recent declines in some countries. Even where employment has increased there is a question about the quality of the employment. Some activities do not yield a living wage. The group of 'working poor' engaged in low productivity or marginal activities has grown. Poverty has also increased as a result of the fall of real wages and this raises other issues related to the functioning of the labour market. One question that immediately arises is, to what extent does a fall in real wages lead to higher levels of employment. In other words, what is the wage elasticity of labour demand. A related issue is the un-employment elasticity of the wage rate, which gives an indication of the extent to which workers and trade unions are prepared to exercise wage restraint in the event of unemployment. These are empirical issues which have not been sufficiently researched and attention tends to be focused on lack of flexibility and institutional rigidities in the labour market. The argument is made that "intensified competition in a global economy and of labour-saving technical progress requires flexibility in wages. Once created, unemployment is reinforced by ratchet effects; it becomes more and more difficult to find employment again when one has been out of employment for a while. The unemployed lose qualifications relative to the employed; in some cases they may lose their social competence altogether. Unemployment can easily become persistent, and to overcome rising unemployment in a self-reinforcing trap, it takes a comprehensive push of institutional change."²⁵

Labour unions are part of the institutional landscape in the Caribbean. Some are even affiliated to political parties. Unions, however, are not immune to market forces. A high level of unemployment tends to weaken their power and bargaining strength. In view of the prevailing levels of unemployment in the region, some governments have been moved to enact minimum wage laws to discourage exploitation. The level of wages, however, has a great deal to do with productivity and the fundamental approach to the wage issue is to create employment opportunities and to increase the productivity of labour.

2. CHALLENGES FROM THE NEW TRADING FRAMEWORK

Introduction

All the indications are that the world economy will become increasingly globalized and integrated and countries that fail to ensure greater efficiency are unlikely to benefit from this trend. The new trading order to be established as a result of the Uruguay Round is not fully in place, but the fundamental principle that underlies it is the belief that more open markets in goods and services will benefit both developed and developing countries. Protection as a development strategy has been greatly discredited and preferences enjoyed by some developing countries in the markets of developed countries are seen to be inconsistent with the new trading order. Not all countries are in a position to take immediate advantage of the opportunities created. Some developing countries have concerns about the pace of change, the degree of openness sought and the likely outcome in a situation where the playing field is made level, but the players are not all equal. There are fears about the proliferation of anti-dumping actions by some developed countries and the adoption of protectionist measures in the guise of environmental or quality concerns. Already, one observes wide disparities among developing countries in terms of the pace of integration with the world economy. For example, using the proportion of trade to GDP as a measure of integration, the ratio increased by 1.37 per cent between 1980-1983 and 1990-1997 for East Asia as compared to 0.45 for Latin America and the Caribbean. For at least six countries in the latter group it declined. "Changes in ratios of trade to GDP matter because competition in global markets exposes exporters to new technologies, designs, products, and management techniques and provides access to imports that were previously unavailable or that embody new technologies that can contribute to productivity gains."²⁶

The composition of exports tends to have a critical influence on the pace of growth of exports relative to production. Goods with a high income elasticity of demand (e.g. manufactures) tend to grow faster than goods such as primary products with low income elasticity and subject to volatile market conditions. Because of their size, policies and historical circumstances, Caribbean countries have come to depend heavily on international trade. The export of goods and services generally amounts to more than 40 per cent of GDP, while the import of goods and services ratio tends to be even higher. In certain cases the export ratio exceeds 80 per cent. Caribbean countries export mainly products for which demand is inelastic and for which they are largely price takers. From an almost total dependence on sugar cultivation for export since the eighteenth century, the post-war period has witnessed some diversification in economic activity, but the production structure is narrowly based, export-oriented and uncompetitive in several areas. In some cases, sugar production has stopped completely and has been replaced by bananas and tourism as the lead sectors. In most of the others sugar production has been declining, but is still relatively important in terms of employment and foreign exchange. Sugar and bananas are produced at relatively high cost and their survival has depended on special pricing and marketing managements, mainly in the United Kingdom market. Low value-added in the manufacturing sector has made it difficult for the Caribbean to take advantage of the market opportunities granted to the Caribbean in North America and Europe either within special arrangements or within the Generalized System of Preferences. The granting countries adopt rules of origin that ensure that the favoured countries are not used as

conduits by other countries to penetrate their markets. At the same time, the heavy dependence on foreign sources for raw materials has made it difficult for Caribbean countries to satisfy value-added criteria. These arrangements have not helped a great deal in developing a manufacturing sector and diversifying the export base.

The trading nexus between developed and developing countries has also undergone fundamental changes in recent years. Because of the displacement of natural resources by synthetic products and the more efficient use of raw materials resulting from technological developments, growth in the industrial nations no longer acts as an 'engine' that pulls along the poorer nations. At the same time, recent growth patterns have shown that growth in developing countries does not necessarily depend on the level of activity in the rich nations.

The trend towards greater trade liberalization is being accompanied by a rapid growth in international trade, averaging some 6 per cent per year in volume terms over the last 10 years as compared to less than 3 per cent for world production. Not all countries, however, have shared equally in this growth. While exports of goods from all developing countries grew on average by around 5 per cent per year between 1981 and 1994, the average for East Asia and the Pacific was 11.8 per cent as compared to 4.3 per cent for Latin America and the Caribbean and 2.3 per cent for Sub-Saharan Africa. The result of this uneven growth in trade is that some countries are losing ground in the world market place, while others are gaining. North America's share in world merchandise exports was around the same (16 per cent) in 1995 as it was in 1985, but Western Europe's share increased from 40 to 45 per cent and Asia's share from 21 per cent to 27 per cent. The share of Latin America and the Caribbean, however, fell from 5.6 per cent to 4.6 per cent over the period.

The fact that dynamic export performance seems to go hand in hand with impressive growth rates in output has been a driving force behind the formulation of recent trade and development policies. The changing composition of world exports also gives some indication of the structural changes in the world economy. Between 1985 and 1995, for example, the share of agricultural products in world exports declined from 13.7 per cent to 11.8 per cent, while the share of mining products fell from 21.9 per cent to 10.5 per cent. The share of manufactures, however, increased from 61.2 per cent to 74.4 per cent over the period. With respect to this group of products, there has been a shifting in the locus of production from North America and Western Europe to other countries, particularly those in East Asia. Countries like Mexico, Brazil, Singapore, Hong Kong, China and Thailand now account for a higher proportion of world exports of manufactures than they did in the early 1960s.

The changing world trading framework

Through regional trading arrangements and the adoption of structural adjustment programmes, a large number of countries were already committed to reducing trade barriers even before the conclusion of the Uruguay Round in 1993. An increasing number of bilateral agreements outside the General Agreement on Tariffs and Trade (GATT) framework had not only raised fears about the future of the multilateral framework, but had also inspired the proliferation of an increasing number of regional groups in the 1980s and 1990s, both among developed and developing countries.

When the World Trade Organization (WTO) was established on 1 January 1995, most members were parties to at least one regional agreement that had been notified to GATT.²⁷ Though the decisions flowing out of the Uruguay Round have strengthened the multilateral framework, it has not dampened the enthusiasm to accelerate the pace of regional integration, which countries see not only as a defensive measure, but as a necessary platform for developing an export base and for interacting with the larger world community. Between 1990 and 1995 intra-NAFTA merchandise exports as a percentage of total exports increased from 42.8 per cent to 46.2 per cent. Over the same period intra-Mercosur trade increased by over 300 per cent, accounting for 20.4 per cent of total exports in 1995 as compared to 8.9 per cent in 1990.

Since the mid-1980s, integration groupings particularly in developing countries have taken on new life, and most of them are now seen less as a protection strategy to encourage import substitution and more as a framework to encourage production and exports. While removing barriers to intraregional trade, tariffs against third countries have also come down. Average applied tariffs in Latin America are generally between 10 and 20 per cent. MERCOSUR, the Andean Group, CARICOM and the Central American Common Market (CACM) all have common external tariffs averaging between 9 and 13.5 per cent, although significant exceptions persist for individual countries.²⁸ Integration is increasingly being seen as encompassing much more than the removal of trade barriers.

The results of the Uruguay Round continue to see regional movements as not being inconsistent with the multilateral trading system. The Round achieved further cuts in tariffs, but even before it concluded, unilateral, bilateral and regional actions had already recognized the benefits of competition and larger markets. These developments may also have been a reflection of a growing loss of confidence in the multilateral framework represented by GATT in which an increasing share of trade was being conducted outside the Agreement. The results of the Uruguay Round reinforces the trend towards greater trade liberalization in a multilateral setting by adopting a more comprehensive approach to the question. Of particular interest to developing countries is the decision to reduce non-tariff barriers to trade which had proliferated in recent years. Among the most important quantitative restraints scheduled for removal are those in textiles and clothing applied under the Multi-fibre Arrangement. These restraints are to be phased out in four steps, starting 1 January 1995 and ending 1 January 2005. The results of the Round address not only border measures, but a whole range of factors which affect competition and also includes an agreement on services, the General Agreement on Services (GATS) and one on 'ideas', the Trade-Related Aspects Intellectual Property Rights (TRIPS). With respect to services, two initiatives were underway, the first relating to the trade in basic telecommunications services came into effect in February 1998 while the agreement relating to the liberalization of financial services was to come into effect on 1 March 1999, at the latest. The TRIPS Agreement is based on "a recognition that increasingly the value of goods and services entering international trade resides in the know-how and creativity incorporated into them. The TRIPS Agreement provides for minimum international standards of protection for such know-how and creativity in the areas of copyright and related rights, trademarks, geographical indications, industrial designs, patents, the lay-out design of integrated circuits and undisclosed information."²⁹ It also contains provisions aimed at the effective enforcement of such intellectual property rights and for the settlement of disputes. Developing countries have a transition period for bringing their legislation and practices in conformity.

The industrial countries account for about two thirds of world imports of agricultural goods. Non-tariff barriers in the form of bans, quantitative restrictions, variable import levies, minimum import prices and discretionary import licensing have been more important than tariffs in protecting agriculture in both developed and developing countries. Domestic and export subsidies are also to be reduced. In this way agricultural trade has been brought more in line with the rules and discipline of the GATT, although reforms are likely to be stretched over a period of 6 to 10 years. Non-tariff border measures, such as import quotas, are to be converted to tariffs that provide the same protection. These tariffs are then to be reduced by an average of 36 per cent for developed countries and 24 per cent for developing countries.

In order to achieve greater transparency in the international trading framework a new institution has been created. The WTO which was established on 1 January 1995 replaced the GATT which concerned itself largely with obstacles to trade in goods. The WTO not only has a potentially larger membership than GATT (128 at end of 1994 as compared to 132 for WTO at end of October 1997) but also a much broader scope including trade in goods, services and intellectual property. WTO membership to date accounts for more than 90 per cent of world trade. Countries that become members must accept all of the obligations of the GATT and its corollary agreements (with few exceptions) negotiated in the Tokyo and Uruguay Round. For many countries, particularly developing countries, this carries a stronger commitment, since they are obligated to substantially more trade obligations than previously required under the GATT regime. As far as dispute resolution is concerned, the WTO consolidates the various dispute provisions of the GATT accord into a unified and more effective dispute mechanism. "Countries can no longer block the establishment of arbitration panels, or ignore their findings as they could under GATT. And although they may appeal, the decision of the Appeals Body is final. Every stage of the process is subject to strict time limits, and countries that fail to comply faced authorized trade sanctions."³⁰

Challenges facing Caribbean trade

As indicated earlier, Caribbean countries are extremely dependent on foreign trade as a result of small domestic markets and a narrow production base. Foreign exchange earnings revolve around a few activities and with the decline of traditional exports various kinds of incentives have been used to diversify the export base, but these have produced limited results. The Bahamas depends almost exclusively on tourism and offshore financial activities. Tourism generates about 75 per cent of GDP, while banking and financial services contribute about 15 per cent. Antigua and Barbuda and Barbados have also become highly tourism-dependent following the decline of sugar cultivation. In the former country, tourism provides about 75 per cent of foreign exchange receipts and directly accounts for about 12 to 15 per cent of GDP. In Barbados, sugar and its by-products still account for about 20 per cent of domestic exports, but receipts from tourism tend to be more than four times those of domestic exports. Three products, sugar, bananas and citrus concentrates contribute about 70 per cent of Belize's domestic exports. In Guyana, sugar, bauxite, gold and rice account for over 80 per cent of domestic exports. In Jamaica, exports are also highly concentrated in sugar, bananas and bauxite, but tourism expenditure amounts to around 90 per cent of earnings from domestic exports. In Trinidad and Tobago, petrochemicals production based on the country's natural gas reserves has been increasing in recent years and this activity, together with exports of petroleum and petroleum products, accounts for about 75 per cent of earnings from domestic exports. In the other

OECS countries, sugar and bananas dominate the export trade but tourism has emerged as a major foreign exchange earner. In St. Kitts-Nevis, for example, tourism expenditure tends to be around twice that of earnings from exports. In addition to the products stated in Table 21, other domestic exports consist largely of agricultural products, and simple manufactures involving, in some cases, assembly or refining operations. Traditionally, the OECS countries have run a persistent trade deficit and this is normally covered by earnings from services, mainly tourism and capital flows.

Table 21
Main Domestic Exports (Most Recent Year)
(Percentages of Total)

Countries	Sugar & By-products	Bananas	Citrus & Concentrates	Petroleum & Petroleum Products	Bauxite & Alumina	Petro- Chemicals	Gold	Cocoa Nutmegs & Mace
Barbados	23							
Belize	35	15	20					
Dominica		39						
Grenada		10						36
Guyana	26				18		20	
Jamaica	12	4			50			
St. Kitts-Nevis	31							
St. Lucia		50						
St. Vincent & Grenadines		42						
Suriname								
Trinidad & Tobago	2			47		26		

Sources: IMF, Staff Country Reports.

As can be seen in Table 22, the trade partners of Caribbean countries are also highly concentrated. The United States is by far the most important, both as a source of imports and as a market. While for a few countries, such as Jamaica and Barbados, the share of exports to this country has increased in recent years, for others it has declined. Despite an institutional relationship with the European Union (EU) in the form of the Lomé Convention, trade has been declining. The Caribbean/Canadian Trade Agreement has not had any great impact on trade between the two partners. CARICOM as a market varies from around 5 per cent for Jamaica to over 40 per cent for Saint Vincent and the Grenadines. Intra-CARICOM exports has grown very slowly and is estimated to be less than 20 per cent of total exports.

Table 22
CARICOM's Direction of Trade, 1988 and 1995
(Percentages)

Country/Group	<u>Imports</u>		<u>Exports</u> ¹	
	1988	1995 ²	1988	1995 ²
CARICOM	9	10	13	18 ³
Other Caribbean	3	2	7	7
Canada	6	4	6	5
USA	40	46	42	35
Latin American Integration Association	8	9	3	6
Central American Common Market	1	1	..	1
European Community	19	14	24	20
of which UK	10	7	16	10
European Free Trade Association	1	1	1	3
Japan	5	5	1	1
Other	8	8	3	4
Total	<u>100</u>	<u>100</u>	<u>100.0</u>	<u>100.0</u>

.. less than 1 per cent

1. includes re-exports

2. excludes Antigua, Guyana, Grenada, Suriname.

3. when all countries are taken into account, this figure is likely to come down to around 13 per cent.

Source: *CARICOM Secretariat.*

As far as the relationship between the growth of output and the growth of exports of goods and services is concerned, the picture was mixed. For a number of countries, notably, Barbados, Haiti, St. Kitts-Nevis and Suriname, output grew faster than trade during the 1980s. In the 1990s, however, this trend seems to have been reversed in most cases.

The Caribbean countries are members of different blocs and trading arrangements that came into being under circumstances which have undergone immense change in an increasingly dynamic economic and political international environment. CARICOM, for example, was conceived in the

1960s in response to concerns about size and vulnerability in a protectionist world economy and against the background of integration initiatives in Western Europe and Latin America. The Lomé Convention emerged as an instrument to coordinate the aid effort of Western Europe to a group of former colonies in Africa, Caribbean and the Pacific. It was also an instrument that ensured reliable access to food, raw materials and markets for European countries. The opening up of the world economy, the impact of technology on raw material use and the desire to globalize trading relationships have significantly reduced the importance of the Lomé Agreement to Europe. The United States Caribbean Basin Initiative was a security/political initiative with an economic rationale. With the end of the Cold War, emphasis has shifted to the drug problem which threatens its social well-being. The spread of the market economy and moves towards global free trade has increased the scope for economic alliances which already transcend geographical and cultural boundaries. Several new forces and influences are operating in the world economy and even where special considerations may be required, new devices and instruments will have to come into play. The recent WTO ruling on bananas gives a clear signal of the philosophical orientation of the new order and the urgency for change.

In the following section we look at the prospects facing the Caribbean in its major trading arrangements.

The Lomé Convention

The Lomé Convention, which takes its name from the capital of Togo where the first four Conventions were signed, has its origins in the desire by the various European imperial powers and their former colonies to preserve highly valued trade and aid relationships following the granting of independence. A number of different types of agreements preceded the first Lomé Convention in 1975 which brought together under one umbrella, a group of African (both French and English-speaking), Caribbean and Pacific States in a cooperation framework with the European Community. Since 1975, there have been four Lomé Conventions, each building on the experience of the former. Though the Convention was normally signed for a period of five years, the Fourth was given a 10-year duration for the period 1990-2000, but the financial protocol was for five years. Provision was made for a mid-term review which took place in 1995 and the revised text was adopted in Mauritius in November 1995. This was the first time the Convention was signed outside of Lomé, the capital of Togo.

The Lomé Convention is essentially, a negotiated, contractual agreement between the European Union and a group of African, Caribbean and Pacific (ACP) countries, almost all of whom are former colonies of European countries. While the ACP suppliers benefited from access to a guaranteed market and relatively favourable prices for their major exports, the EU countries were simultaneously assured of a supply of critical raw materials and food. Since 1975, the membership of the Convention has been increasing. The first Lomé signed in 1975 involved 46 ACP States and nine European nations. The revised Fourth Convention adopted in Mauritius in November 1995, had as signatories 70 ACP States (47 African, 15 Caribbean and 8 Pacific) and 15 European countries. The Caribbean subgroup includes the CARICOM countries, Haiti, the Dominican Republic and Suriname. The total population of the ACP States numbers 570 million as compared to 370 million for the 15 EU States.

The Lomé Convention is a financial, trade and technical assistance package administered by a number of institutions within a defined set of rules and regulations. The financial assistance provided under the Convention is channeled through two sources: the European Development Fund (EDF) and the European Investment Bank (EIB). The latter not only administers the risk capital, but also provides loans from its own resources based on interest rates subsidized from the EDF. Starting in 1958 with the earlier association arrangements, there have been eight EDFs (including the most recent). The 1995 EDF is for 12,967 million ECU, while EIB resources amount to 1,658 million ECU, as compared to the 1990 EDF of 10,800 million ECU and EIB funds of 1,800 million ECU. Financial aid increased by 22 per cent between 1990 and 1995, while the ACP population increased by 24 per cent. If the financial package of 14,625 million ECU were to be divided by the total population, the average will be 26 ECU per person over five years, or about 5 ECU per person per year.

While the EU is the most important source of finance for some ACP countries, for others the trade package is considerably more significant. Basically the EU allows ACP countries access to its markets without insisting on reciprocal arrangements. The Convention states that "Products originating in the ACP States shall be imported into the Community free of customs duties and charges having equivalent effect" (Article 168 of Lomé IV). ACP exports to the EU, however, are not all treated in the same way. Some like sugar, rum and bananas are covered by special protocols. A select list of other agricultural products, for example, beef and veal, fishery products, processed fruit and vegetable products, fresh or chilled fruit and vegetables, cereals and rice are imported from ACP States on a conditional basis, so as not to frustrate the implementation of the Common Agricultural Policy. The bulk of the products, including manufactured and processed goods, fall under the provisions of the 'Trade Cooperation' Chapter which states the terms under which they can enter the EU market. Duty free entry into the EU market depends on the satisfaction of the value-added and processing criteria stipulated for various products or classes of products.

Trade development between the EU and the ACP was envisaged as a major plank in the cooperation framework. Not only has the share of ACP exports in world trade been declining, but the share of ACP exports to the EU has also been falling. This share fell from 6.7 per cent in 1976 to 2.8 per cent in 1994 (see Table 23). Latin America's share has remained fairly steady at around 5 per cent, but Asia's share increased from 4.2 per cent to 13.1 per cent over the period. ACP exports to the EU are dominated by a few primary commodities such as sugar, bananas, crude petroleum, uncut diamonds, cocoa beans and copper. Manufactured goods amount to less than 40 per cent of exports.

Table 23
Developing Countries' Share of EU Imports, 1976-1994 (%)

Country Group	1976	1980	1985	1990	1992	1994
ACP	6.7	7.2	6.7	4.7	3.7	2.8
Asia	4.2	5.9	6.5	11	13.6	13.1
Latin America	5.3	5.1	6.5	4.6	5.1	5.4
Mediterranean	6.1	6.1	8.1	6.5	6.2	6.1
All Developing Countries	44.8	42.4	34.7	31.2	29.2	34.2

Source: European Center for Development Policy Management, *Beyond Lomé IV: Exploring Options For Future ACP-EU Cooperation*, 1996, p. 2.

Although there has been some liberalization of the rules of origin over the years, this has not impacted significantly on the supply base. Looking at the picture from an European perspective, the EU buys more than it sells to the ACP which is not required to grant reciprocal trading arrangements. For various reasons, the EU has become less dependent on ACP's raw materials, and this is a factor that would influence its own position as it seeks to rationalize its trading relationship. Only a few countries (e.g. Mauritius) have been able to take advantage of the opportunities offered in the EU market. Two traditional products which are of major concern to the Caribbean are sugar and bananas, which are covered in special protocols. More needs to be said on those arrangements, which will be affected by the new trading rules.

Bananas

Bananas are a tropical fruit grown almost entirely in developing countries. Their production in the Caribbean on a relatively large scale corresponds with the decline of the sugar economy, particularly in the post-war period. Total banana exports from the Windward Islands comprising Dominica, Saint Lucia, Saint Vincent and the Grenadines and Grenada increased from 6.7 thousand tonnes in 1954 to 279.8 thousand tonnes in 1992. While bananas are also produced in Jamaica, Suriname and Belize, they are of greater importance to the economies of the Windward Islands. Over 35 per cent of the agricultural land in Dominica, Saint Vincent and the Grenadines and Saint Lucia are under banana cultivation. In Grenada it is about 4 per cent. Banana exports amount on average to over 50 per cent of domestic exports in the former three countries and for about 20 per cent in Grenada. Bananas are not only an important cash crop that can be cultivated throughout the year but they generate most of the jobs in these countries. Direct employment in the banana industry as a percentage of the active working population was estimated in the late 1980s as follows: Dominica 50 per cent; Saint Lucia 45.5 per cent; Saint Vincent and the Grenadines 54 per cent and Grenada 7 per cent. Government revenues are also critically dependent on the banana industry.³¹

Because the fruits are grown mainly by small farmers on land not ideally suited to production, cost tends to be high. Hurricanes periodically decimate the crops. The main market for Caribbean bananas is the United Kingdom, which in the late 1960s sourced as much as 95 per cent of its requirements from the Caribbean. Protection was provided by a specific duty on bananas from countries outside the Commonwealth Preference Area and by quota restrictions on bananas from Latin America. After Britain's entry into the EC in 1973, it continued to protect Caribbean bananas, importing Latin American bananas only to make up shortfalls from the Caribbean.

All EU countries have their favoured suppliers and they use national regulations, as was permitted by Article 115 of the Rome treaty, to control imports. For Spain, it is the Canary Islands; for France it is the Overseas Territories and former colonies in Africa; for Portugal it is Madeira; for the United Kingdom it is the Caribbean. Italy derives some 15 per cent of its supplies from Africa. The Latin American producers supply virtually 100 per cent of the Belgian, Danish and German markets; over 90 per cent of the Irish and Dutch markets, 85 per cent of the Italian market as well as 12 per cent of the United Kingdom market. Total imports into the EU market in 1994 was 5.0 million tonnes of which the United Kingdom accounted for 567.5 thousand tonnes or only 12 per cent. With the expansion of the EC three distinct banana regimes took form:³²

- (a) A preferential market in France, Britain, Spain, Italy, Portugal and Greece for either EU and/or ACP producers;
- (b) A duty free market in Germany;
- (c) A market subject to a 20 per cent tariff in Denmark, Ireland, Belgium, the Netherlands and Luxembourg.

With the move to form a Single European Market by removing all tariff and non-tariff barriers, the fear in the Caribbean was that bananas would be able to move freely within Europe, thus displacing the high cost producers, such as the ACP suppliers. Protocol 5 of Lomé IV, however, gives an undertaking to the ACP as follows:

“In respect of its banana exports to the Community markets, no ACP State shall be placed, as regards access to its traditional markets and its advantages on those markets in a less favourable situation than in the past or at present.”

Faced with this situation, the EU made some compromises in the new banana regime (NBR) which came into effect amidst a great deal of controversy on 1 July 1993. The NBR instituted a common market organization for bananas, replacing the various national banana import regimes existing in the member States. “The new Community -wide set of measures for bananas included duty-free access for traditional ACP suppliers and a tariff quota of 2 million tonnes for third country shipments and non-traditional ACP sources combined.”³³ Following the initiation of the dispute settlement proceedings by Colombia, Costa Rica, Guatemala, Nicaragua, and Venezuela, a GATT panel ruled in their favour on a number of issues and following negotiation, a tariff quota of 2.2 million tonnes of bananas was agreed for Colombia, Costa Rica, Nicaragua and Venezuela, which in turn agreed not to ask for adoption of the panel's ruling. The NBR not only met with opposition

from Latin American producers, but also from some EU members and was challenged in the European Court of Justice and reported both by the United States and some Latin American States to the WTO. The United States incidentally is not a producer of bananas, but was acting on behalf of its transnationals which dominate the production and marketing of bananas in Latin America. A recent ruling of an appellate panel has upheld the March 1997 WTO decision that the European banana regime is illegal and the arrangement will either have to be extended to all banana exporters or terminated.

The banana issue has affected Caribbean-Latin American relations. The former States are higher cost producers, but hold an insignificant part of the European market in one EU country. The Latin American producers dominate the world trade in bananas, accounting for some 75 per cent of world exports. The major players in the trade, however, are United States Transnational Corporations (TNCs), viz., United Brands (Chiquita), Standard Fruit (Dole) and Del Monte. With respect to the EU market which is second only to the United States, the three United States banana TNCs hold 66 per cent of the EU market divided 43 per cent to Chiquita, 13 per cent to Dole and 10 per cent to Del Monte.³⁴

The Sugar Protocol

Following Britain's entry into the EU the special arrangements governing the importation of cane sugar from Commonwealth sources had to be accommodated. Sugar imports in the EU are now governed by Article 213 and Protocol 8 of the Lomé IV Convention. The 'Sugar Protocol', it should be noted, is not an integral part of the Convention. It is part of the document, but has not been subject to the same five-year negotiating process as are the rest of the matters covered.

Protocol 8 states that the Community, but in practice mainly the United Kingdom, "undertakes for an indefinite period to purchase and import, at guaranteed prices, specific quantities of cane sugar, raw or white, which originate in the ACP States and which these States undertake to deliver to it." For each listed country there is a quota. Prices paid are fixed annually and are linked to those paid to EU sugar beet farmers, which are generally higher than world sugar prices.

Unlike the banana arrangements, the present regime for sugar is not incompatible with the completion of the EU's Single Market because the sugar protocol is already an EU-wide regime.

The future of the Lomé Convention

Speculation on the future of the Lomé Convention is taking place not only in the context of the single European Market and the new GATT rules, but perhaps more importantly against the background of changes in the world economy and the shifting geopolitical configuration. The EU's political and security interests have changed, and the newer members do not share the same historical ties as between the original members and their former colonies. The effectiveness of the Convention as a trade and development instrument is also being questioned, given the inability of the majority of ACP States to significantly diversify their exports and the fact that the ACP has among its membership all of the world's 50 least developed countries. Aid fatigue in the EU and the failure to develop even elementary administrative capacity in some countries have raised basic

questions about the Lomé arrangement. Reasons for the modest achievements range from the bureaucracy associated with the administration of the Convention to insufficient effort on the part of ACP States.

There is a widely-held view that the Lomé Convention will not survive in its present form after the year 2000. A Green Paper published by the European Commission for discussion has outlined a number of scenarios. The fact is that even though membership of successive Lomé Conventions has been increasing, the environment in which the Convention functions has been changing. At the global level the conclusion of the Uruguay Round has not only produced profound institutional changes in the world trading system but had removed many of the distortions which had crept into that system. Tariffs on manufactures in both developed and developing countries are scheduled to come down further over the next few years. Agriculture is back under the multilateral discipline and voluntary export restraints are expected to be abolished within four years. The Multi-fibre Arrangement will also be phased out. But even outside of the Uruguay discussions many developing countries, with IMF and World Bank prodding, were reviewing their trade policies and reducing protectionist trade barriers in order to encourage greater efficiency. In Europe itself the formation of a Single market is bound to have implications for the EU's external trade policy.

The proliferation of integration arrangements is another feature of the evolving world economy. The European Union has increasingly been negotiating bilateral agreements with single countries and groups of countries. The privileges which the ACP once enjoyed in the EU market have been eroding over time. As pointed out earlier, the ACP for various reasons has not been able to take advantage of the opportunities offered in the European markets. In fact the ACP States have often complained that the EU grants to some third countries have better preferential access than that available to ACP States on a number of products of particular interest to them. The reduced tariffs agreed to by the EC in the Uruguay Round will further reduce ACP preferences, given the requirements of the MFN provision. For the Caribbean, Europe is seen as a distant market, except of course for the traditional exports, such as sugar, bananas and rum. Transport costs can be a disincentive to the development of exports to this market.

Not only has EU-ACP economic relations not grown at an impressive pace, but intra-ACP relations have also failed to develop on any significant scale, notwithstanding the provision for cumulative value added in the convention in meeting rules of origin criteria and incentives for regional development.

In this new climate of liberalization, non-reciprocal arrangements are likely to become less and less a feature of international trade. In the event that ACP countries grant reciprocal access to other developed countries in any arrangement, similar concessions will have to be extended to EU countries. Caribbean countries cannot take high costs and inefficiency as an unchangeable condition. If reciprocity is accompanied by increasing efficiency, the cost of domestic production may not be as high as is sometimes made out to be.

The state of the Caribbean Community and Common Market (CARICOM)

Following the collapse of the West Indies Federation in 1962, most of the individual units subsequently achieved political independence from Britain, but the question of viability and vulnerability associated with small size was an ever present one. The decision to continue existing forms of functional cooperation and to pursue economic integration was founded in this reality. It was believed that Caribbean cooperation and integration was not being fired so much by the 'doctrines of integration economics' but by deeper socio-political and historical forces. "Caribbean regionalism is the outgrowth of more than 300 years of West Indian kinship – the vagaries of the socio-economic political history of a transplanted people from which is evolving a Caribbean identity."³⁵ After almost three decades, the pace of economic integration has remained slow and stuttering, as national sovereignty has yielded grudgingly to regional policy and objectives. The effort to construct a regional architecture to complement and reinforce national structures and policies is often subverted by failure to agree on or implement basic and critical instruments. Differences in the level of development and the competitive way regional States view each other provides part of the explanation as each State sees itself as having its own peculiar problems for which it must take responsibility. Within insular nationalistic settings certain habits and structures have taken root and resist change, notwithstanding the pressure for greater efficiency. A fundamental factor is that intraregional transactions form only a small part of total economic activity and focus is more on external interaction, which is seen to be more critical to national development. As a force in Caribbean economic transformation, CARICOM remains weak, undeveloped and unsure of its potential or objectives. It is always striving to catch up with events driving global changes. Ironically, an uninspiring record of achievements has undermined confidence in the movement, weakened commitment and reinforced the position of those who see the regional effort as irrelevant to national development.

CARICOM, which came into being in July of 1973 with the signing of the Chaguaramas Treaty in Trinidad and Tobago grew out of the less ambitious Caribbean Free Trade Agreement (CARIFTA) adopted in 1968. The Chaguaramas Treaty is not a purely economic one, and envisages cooperation in three main areas:

- (a) Economic integration, as represented by the Caribbean Common Market which replaces CARIFTA. This envisages market integration, coordinated or joint actions in production, joint actions in extraregional trade and other economic transactions and a Special Regime for the Less Developed Countries.
- (b) Cooperation in non-economic fields and in the establishment and operation of common services (e.g. health, education, examinations, shipping, air transport, meteorology, scientific research, etc.) and
- (c) The coordination of the foreign policies of the independent member States of the region.

CARICOM is more than a free trade area, but not quite a common market. While the Chaguaramas Treaty recognizes in its preamble the importance of the 'optimum utilization of

available human and natural resources of the Region', only small and tentative steps have been taken towards the free movement of labour and capital. Labour is a very sensitive issue, given the high levels of unemployment and the strong trade union movement. Only in 1996 was a decision taken to allow the free movement of University graduates and media personnel in the region, but the need for work permits can easily frustrate this objective. Different levels of development and different degrees of dependence on tariffs for revenues have made the adoption of a Common External Tariff (CET) a frustrating exercise. The CET is in its third phase, subject to exemptions and affected by different degrees of compliance.

The CET is not the only area where progress has been slow. Many issues identified in the 1960s and 1970s as critical to Caribbean cooperation and development received scant attention, particularly in the difficult period of the 1980s when the absence of effective regional mechanisms to assist member States was deeply felt. Structural and institutional problems continue to plague the agricultural sector where the need for rationalization has long been recognized. In the area of foreign policy, the member countries do try to coordinate their positions on some issues, but the unilateral approach is not uncommon when national interests take precedence over regional concerns. In the area of foreign representation, there has been little attempt to achieve more effective use of resources expended on this instrument, notwithstanding the financial stress under which governments are operating. There is a tendency for the rhetoric of integration to far exceed concrete actions and decisions.

Table 24
CARICOM-Common External Tariff Rates

CATEGORIES	1-1-1993 to 31-12-1994	1-1-1995 to 31-12-1996	1-1-1997 to 31-12-1997	1-1-1998
Agricultural Inputs	0	0	0	0
Non-competing primary inputs	5 (LDC's 0-5)	5 (LDC's 0-5)	5 (LDC's 0-5)	5 (LDC's 0-5)
Non-competing intermediate inputs	5 (LDC's 0-5)	5 (LDC's 0-5)	5 (LDC's 0-5)	5 (LDC's 0-5)
Non-competing capital inputs	5 (LDC's 0-5)	5 (LDC's 0-5)	5 (LDC's 0-5)	5 (LDC's 0-5)
Competing primary inputs	20	15	10	10
Competing capital goods	20	15	10	10
Selected imports	20	15	10	10
Competing intermediate inputs	25	20	15	15
Non-competing final goods	25	25-30	20-25	20
Agro-industry	30-35	25-30	20-25	20
Garments	30-35	25-30	20-25	20
General manufactures	30-35	25-30	20-25	20
Agriculture	40	40	40	40
LIST A	Suspended rates	Suspended rates	-	-
LIST B	Suspended rates LDC's	Suspended rates LDC's	-	-
LIST C	Minimum rates	Minimum rates	Minimum rates	Minimum rates
LIST D Parts I and III	Suspended rates LDC's	Suspended rates LDC's	-	-
Safety	0	0	-	-

The adoption of an industrial programming policy to encourage a more optimal use of scarce capital resources has proven difficult in a region where members are competing with each other for investment. The formulation of a foreign investment policy and a rational structure of incentives which were at one time seen as crucial to the goal of greater self reliance now commands less urgency. Though some steps have been taken recently to facilitate the regional movement of capital, there still exists a wide range of obstacles, some of which are not readily transparent. With respect to air and sea transport regional cooperation has been elusive.

In the 1960s, the decision to approach integration with a free trade area was not without controversy. One view originating largely in the academic community was that since intraregional trade was already largely unimpeded, the more sensible approach was to integrate the production sectors, developing a diversified regional manufacturing sector based on the Caribbean's natural resources. Such strong linking of the Caribbean economies was not seen to be politically feasible at the time, though its worth as a longer-term goal was recognized. The approach adopted was largely to facilitate the ongoing import substitution process at the national levels. Intraregional trade has grown very slowly, reflecting the competitive nature of Caribbean economies. In the 1960s intra-regional exports amounted to around 6 per cent of total domestic exports. In the 1970s this grew to around 8 to 9 per cent, and reached around 13 to 14 per cent in the early 1990s.

The emergence of balance of payments problems in the latter part of the 1970s and the failure to implement large parts of the Chaguaramas Treaty led to the first major review of the integration process by the end of the decade. The Report noted that despite "the great efforts that have been made in the post-independence era, economic, social and human progress in the region taken as a whole have not advanced at the rates which would be considered satisfactory by most people. Large pockets of chronic poverty in both urban and rural areas, endemic unemployment and deficiencies in basic amenities continue to characterize the lot of the region's population."³⁶ This was in 1981. The situation did not improve in the 1980s, particularly in the so-called 'More Developed Countries': Guyana, Jamaica, Barbados and Trinidad and Tobago. The distinction between 'more developed' and 'less developed' has become increasingly blurred since the early 1980s. Intraregional exports as a percentage of total exports are estimated to have declined from 10.3 per cent in 1973 to 8.3 per cent in 1980. Writing in 1992, the West Indian Commission commented as follows, "Overall, progress in developing a CARICOM economic space has been depressingly slow, coming to a complete halt for long periods and suffering reverses all too often."³⁷

With the challenges emanating from developments in the world economy, and with the increasing trends towards regionalism, Caribbean integration is now receiving a great deal more attention. The frustrating unanimity rule has been amended and most decisions can be taken with a three quarters majority. A decision has also been reached to establish a Single Market and Economy by 1999 and to encourage greater integration in the monetary and financial field. With an original population of 5 million people CARICOM had always faced the problem of reconciling the desire to deepen the movement with the need to widen the community. After more than two decades following the signing of the Chaguaramas Treaty it had done neither. Suriname with a population of 410,000 people and a per capita GNP of US\$900 was the first new member to join in 1995. Haiti with a population of 7.2 million people and a per capita GNP of US\$250 was

conditionally admitted in July 1997. With the admission of Haiti and Suriname the population of CARICOM is now 14 million. The application of the Dominican Republic has been put on hold.

In the context of what is taking place in the international arena and given the need for CARICOM to strengthen its diplomatic clout, the idea of continuing with the original core countries had become increasingly irrelevant. The view cherished by some that widening should await deepening was difficult to maintain in a context where deepening was proceeding very slowly and individual markets were being unilaterally opened under structural adjustment programmes. Very slowly Caribbean and Latin American countries were being integrated under the oversight of the World Bank, the IMF and the Inter-American Development Bank (IDB). With the formal admission of Suriname and Haiti, the shift away from the essential Anglophone nature of CARICOM is beginning to take place.

There appears to be no clear strategy with respect to expanding the integration arena, the sequence of steps or the ultimate goals. Decisions, however, are being made in a way that challenges old divisions and concepts and points to a much larger and complex configuration of space, language and culture. In 1994, for example, a major step was taken with the formation of the Association of Caribbean States (ACS) which includes several Latin American countries belonging to other subgroupings.³⁸ With a population of close to 215 million and a total GNP of US\$500 million, the ACS was conceived as an organization intended to foster discussion on matters of common interest and to promote integration including the liberalization of trade, investment, transportation and related areas.

In keeping with the need to develop new trading partners, CARICOM has signed a number of agreements with neighbouring States. These include a CARICOM-Mexico Joint Commission in 1974 aimed at providing training and technical assistance and to promote trade and other exchanges. This was followed by a CARICOM-Brazil cooperation Agreement in 1989 and a CARICOM-Cuba Joint Commission in 1993. The signing of the CARICOM-Venezuela Trade and Investment Agreement in 1992 created for CARICOM States a one-way duty free access to the Venezuelan market and provided a framework to encourage investment and joint ventures. In 1996 the Andean Development Corporation and CARICOM entered an agreement with the aim of advancing the integration process through the creation and promotion of joint ventures and investment opportunities. Partial scope agreements between Guyana and Venezuela and between Venezuela and Trinidad and Tobago are also in place. These agreements, however, have generated very little new trade or investment.

The United States Caribbean Basin Initiative (CBI) and the Canada/Caribbean Agreement (CARIBCAN)

The United States CBI and CARIBCAN are basically the same kind of agreements. They are one-way free trade arrangements that allow a select group of developing countries in the Western Hemisphere to export most of their products duty free to the American and Canadian markets, respectively. The CBI is wider in scope, including as it does certain Latin American countries in the Caribbean and Latin America, while CARIBCAN applies largely to CARICOM States and the still dependent British territories in the Caribbean. In both cases, there are value-added criteria to be met,

and certain sensitive products are exempted. In both cases, too, safety clauses operate to protect industries threatened by exports from the beneficiaries. Both arrangements came into being with the promise of financial aid and the adoption of measures to encourage foreign investment.

Though both CBI and CARIBCAN were intended to encourage trade and development, the fact that they discriminated in favour of some countries was seen as violating the most favoured provision of the GATT and a waiver of contractual obligations was sought and obtained under the provision of Article XXV. Though the Canadian Government has attached no time limit to CARIBCAN, the waiver obtained in 1986 was for a period of 12 years, running until 1998, but this could be extended. In CBI II reference to the termination of the Act in 1995 was removed, and no time-frame was included. This does not, however, mean that provisions of the Act (e.g. the value-added or eligibility criterion) cannot change.

The United States' CBI, or more precisely the Caribbean Basin Economic Recovery Act of 1983, was signed into law by President Reagan on 5 August 5 1983 and implementation began on 1 January 1984. The initiative followed the failure of the United States, Venezuela, Canada and Mexico to agree on the conditions for an aid package to the region. Initially, 27 countries were named as possible beneficiaries but countries could be added or subtracted depending on certain conditions. Puerto Rico and the United States Virgin Islands actively participate in the CBI notwithstanding their peculiar status as United States possessions. These two countries are given special treatment. To protect their rum exports, for example, excise taxes are returned to the respective treasuries of those islands.

The Initiative proposed that exports from approved beneficiary countries should enter the United States market duty free. Eligibility requires that products be grown, produced, or manufactured in the beneficiary countries. Products which are merely assembled or packaged do not qualify. Of course, there are exclusions such as textiles and apparel, leather goods, tuna, petroleum and petroleum products, watches and watch parts. Sugar was to receive duty free treatment, but only up to a certain limit. Quotas could be changed arbitrarily. Under the arrangements existing prior to the CBI, it was estimated that some 87 per cent of Caribbean Basin exports already entered the United States market duty free. The argument put forward for the CBI was that some of the duties that were still in place were in sectors of special interest to Basin countries. They also limited export expansion into many non-traditional products. It was also argued that the global reasons used for excluding certain products from the United States Generalized System of Preferences (GSP) were not relevant to the Caribbean Basin. The complex structures of the GSP itself militated against the ability of small inexperienced countries to take advantage of the opportunities offered.

For goods to qualify for duty-free entry at least 35 per cent of the appraised value of the article imported into the United States must consist of the cost or value of materials produced in one or more beneficiary countries and/or the direct cost of processing operations performed in one or more beneficiary countries. Puerto Rico and the United States Virgin Islands are defined as beneficiary countries for purposes of this requirement. The CBI was linked to promises to put in place incentives to encourage investment and to provide training and assistance for private sector development.

The first CBI has been succeeded by a second CBI (1990) in which one of the most notable modifications has been the removal of the termination date. The arrangement, however, can be terminated by Congress at any time, particularly if it concludes that the social, political and economic conditions which led to the CBI are no longer present. This is not a situation that can encourage long-term investment.

When assessing the CBI, it is difficult to separate the effects of this programme from others such as the GSP. What can be gleaned from Table 24 is that while for some countries, such as Dominican Republic and Jamaica, the value of exports to the United States increased between 1983 and 1995, for others, such as Barbados and Trinidad and Tobago it fell. Values, it should be noted, can be affected by fluctuation in prices. Repeatedly, Caribbean countries have been making the case that not only products of relevance to them are excluded from the arrangement, but their economic structure makes it difficult for them to satisfy the value-added criterion and there is need for a more flexible approach.

The same point has been made to Canada with respect to CARIBCAN which came into existence in 1986 as a trade aid and investment package designed to removed obstacles to almost all exports of the Commonwealth Caribbean entering the Canadian market. Excluded products initially included textiles and clothing, footwear, luggage and hand bags, leather garments, lubrication oils and methanol. CARIBCAN does not exempt Caribbean exporters from the taxes and regulations which govern the importation or sale of goods in the Canadian market. For a product to qualify, a minimum of 50 per cent of the ex-factory price must originate in any of the beneficiary countries or in Canada. Local value added can be "cumulated" among the countries of the region.

Table 25
U.S. Trade with Selected Caribbean Countries (US\$m)

Countries	1983			1995		
	Export	Imports	Trade Balance	Exports	Imports	Trade Balance
Antigua	N.A.	N.A.	N.A.	97	5	92
Bahamas	452	1,746	-1,294	661	171	490
Barbados	195	205	-10	201	52	149
Belize	36	29	7	100	56	44
Dominica	N.A.	N.A.	N.A.	25	7	18
Dominican Republic	632	855	-223	3,017	3,511	-494
Grenada	N.A.	N.A.	N.A.	27	6	21
Guyana	36	75	-39	141	129	12
Haiti	366	352	14	551	138	413
Jamaica	452	307	145	1,421	895	526
St. Kitts-Nevis	N.A.	N.A.	N.A.	58	24	34
St. Lucia	N.A.	N.A.	N.A.	81	36	45
St. Vincent	N.A.	N.A.	N.A.	42	8	34
Trinidad & Tobago	728	1,357	-629	689	1,054	-365

N.A. negligible or not available

Source: IMF, *Direction of Trade Statistics Yearbook*, Various Issues.

Besides the excluded products, Caribbean countries repeatedly complained about the high value-added criterion. Responding to these concerns, Canada subsequently reduced the exclusion list, leaving textiles and methanol. Caribbean rum was also given greater access to the Canadian market. Canada has responded to the general concerns by increasing financial aid and undertaking debt write-off.

As in the case of the CBI, it is difficult to assess the effect of CARIBCAN in Canadian-Caribbean trade relations, given the fact that Canada also has a GSP in place. Canada has had a long relationship with the Anglophone Caribbean, particularly in the areas of trade and investment. Between 1986 and 1995, exports from some Caribbean countries actually fell (see Table 25). In the case of Guyana and Jamaica, their export trade has traditionally been dominated by bauxite.

The access accorded Caribbean countries to the United States and Canadian markets through the CBI and CARIBCAN has been affected by the terms accorded to Mexico through NAFTA. To the extent that these exceed in scope and depth those granted to the Caribbean, the latter would find itself in a less favoured position. Of particular interest to the Caribbean would be those products, such as apparel, which are excluded from the CBI and CARIBCAN. Lower production costs in Mexico are also a factor to contend with. NAFTA membership would also have enhanced Mexico's attractiveness to foreign investment.

Table 26
Canada's Trade with Selected Caribbean Countries, 1986 and 1994 (US\$m)

Countries	1986			1995		
	Export	Imports	Trade Balance	Exports	Imports	Trade Balance
Antigua	N.A.	N.A.	N.A.	5	9	-4
Bahamas	21	21	0	15	13	-24
Barbados	31	15	16	22	14	8
Belize	3	1	2	3	9	-6
Dominica				1	8	-7
Grenada				3	1	2
Guyana	3	19	-16	6	138	-132
Jamaica	52	103	-51	62	151	-89
St. Kitts-Nevis	N.A.	N.A.	N.A.	5	2	3
St. Lucia	N.A.	N.A.	N.A.	7	1	6
St. Vincent	N.A.	N.A.	N.A.	2	N.A.	N.A.
Trinidad & Tobago	65	38	27	67	15	52

N.A. negligible or not available

Source: IMF, *Direction on Trade Statistics Yearbook*, Various Issues.

In the United States the acceptance of NAFTA was not without controversy. There is still a heated debate about the effects of the Agreement on domestic wage rates and employment. Not only has the United States Congress failed to give the President 'fast track' authority, but calls for NAFTA parity for Caribbean States have also gone unheeded. Though some countries led by Chile, have expressed interest in joining, NAFTA itself has not been seeking new members and attention by hemispheric countries is increasingly being focused on the Free Trade Area of the Americas (FTAA) scheduled to come on-stream by 2005.

The emerging hemispheric trade framework

Amidst the global efforts to liberalize multilateral trade, there has been a strong upsurge in regionalism in recent years. This has been in response to the difficulties that were associated with the GATT itself and a reflection of the increasing attention being given to the role of competition and markets in export development. While some new arrangements have come into being, old ones which floundered for years are seeking new ways and adopting new mechanisms to accelerate the process of integration. The European Union, which is the world's largest grouping next to NAFTA, has not only been deepening cooperation but has been expanding both in Europe and other regions through trade agreements with individual countries and groups of countries. In this hemisphere a number of initiatives have recently been taken, and these are worth noting since they are likely to have a significant influence on regional and, even perhaps, world trade policies in the years ahead.

The entry into force of the Canada-United States Free Trade Agreement in 1989 culminated over a century of attempts to liberalize the movement of goods and services between these two countries. The coming into being of NAFTA in 1994 was even more significant, not so much because of its size, but because it brought together the two most developed countries in the

hemisphere with a developing country. NAFTA is not a simple trade agreement requiring reciprocity. It is far broader in scope covering, among other things, conditions for fair competition, the removal of barriers to services, action to increase investment, provisions of protection and enforcement of intellectual property rights in each party's territory and an institutional structure for the implementation and application of the agreement. The inclusion of Mexico in the expanded arrangement troubled some countries, but also raised the expectations of other hemispheric developing States which saw in NAFTA the first step in the implementation of the "Enterprise for the America's Initiative" (EAI) announced by former President George Bush in 1990, and which had as its goals the establishment of a hemisphere-wide free trade zone. The change in administration in the United States in 1992 seemed to have put the process on hold and it was not until the Summit of America's meeting in Miami in December of 1994, that the vision of a hemisphere-wide grouping was raised again. Thirty-four leaders, including President Clinton, from the western hemisphere committed themselves to the creation of a FTAA by the year 2005. Following this meeting, a number of working groups have been set up to address particular issues. The attractiveness of the FTAA concept is that it involves a market of 750 million people and a GNP of over US\$9 trillion (average per capita US\$12,000), which makes it larger than the present European Union both in terms of population and GNP (see Table 27).

There are, of course, a number of integration movements among the developing countries of the hemisphere, dating back to the 1960s. While for many years little advance was made, more recently there is a new urgency and a new attitude in the context of the increasing abandonment of protectionism as a strategy of development, and the need for mechanisms to deal with the challenges emanating from the new world trading order. In 1980 the Montevideo Treaty establishing the Latin American Integration Association (LAIA) superseded the 1960 Montevideo Treaty establishing the Latin American Free Trade Association (LAFTA). In the LAIA framework, liberalization is carried out on a sectoral basis through two mechanisms: Regional Scope Agreements, covering all members of LAIA, which gives preferential treatment on a regional basis, and Partial Scope Agreements, conducted by subgroups of LAIA which offer preferential treatment to the signatories only. It is through a Partial Scope Agreement that the current economic integration initiatives are taking place. The LAIA in 1995 includes a wide range of agreements comprising MERCOSUR (Mercado Comun del Sur or Southern Common Market), the Andean Group, the Group of Three (Colombia, Venezuela and Mexico) and some bilateral and sector agreements. This process has allowed some groups to go ahead of others. In MERCOSUR trade has not only been growing faster than GDP, but from the beginning of 1995 MERCOSUR was able to put in place a Common External Tariff, thus making the group a customs union.

One of the features of the emerging trade architecture is the extent to which integration groups are being connected through bilateral arrangements. For example, just one month before the FTAA was announced in Miami, the NAFTA countries had announced their participation in the Bogor commitment for free trade in the Asia-Pacific region by 2020. Mexico also moved to comple-

Table 27
Selected Data on Latin American States and Economic Groupings, 1995

Countries/ Groups	Population (1995) millions	GNP (1995) US\$ mn	Per Capita GNP (1995) US\$	Exports as % of GDP (1994)
<u>CACM</u>	<u>29.9</u>	<u>37,421</u>	<u>1,252^a</u>	
Costa Rica	3.4	8,884	2,610	40
El Salvador	5.6	9,057	1,610	13
Guatemala	10.6	14,255	1,340	19
Honduras	5.9	3,566	600	41
Nicaragua	4.4	1,659	380	24
<u>Andean Group</u>	<u>101.2</u>	<u>212,566</u>	<u>2,100^a</u>	
Bolivia	7.4	5,905	800	17
Colombia	36.8	70,263	1,910	17
Ecuador	11.5	15,997	1,390	26
Peru	23.8	55,019	2,310	9
Venezuela	21.7	65,382	3,020	29
<u>MERCOSUR</u>	<u>201.9</u>	<u>882,834</u>	<u>4,373</u>	
Argentina	34.7	278,431	8,030	7
Brazil	159.2	579,787	3,640	7
Paraguay	4.8	8,158	1,690	27
Uruguay	3.2	16,458	5,170	18
<u>Other Latin America</u>				
Cuba	11.0	..	..	..
Chile	14.2	59,151	4,160	28
Dominican Republic	7.8	11,390	1,460	24
Mexico	91.8	304,596	3,320	13
Panama	2.6	7,235	2,750	37
NAFTA ¹	384.5	7,978,298	20,750 ^a	
European Union ²	372.0	7,979,000	21,448 ^a	
CARICOM ³	6.4	17,130	2,676 ^a	
ACS ⁴	215.2	502,000 ^b	2,460 ^a	

Note: The members of the Latin American Integration Association (LAIA) include Argentina, Bolivia, Brazil, Chile, Colombia, Ecuador, Mexico, Paraguay, Peru, Uruguay and Venezuela.

.. not available

a. average

b. excluding Cuba

1. Canada, United States and Mexico

2. 15 countries

3. Thirteen Commonwealth Caribbean countries plus Suriname. With Haiti the population will increase to 13.6 million and total GNP to US\$18,907 million giving an average per capita GNP of US\$1,390.

4. Association of Caribbean States. The ACS includes the CARICOM States and the following countries: Colombia, Costa Rica, Cuba, Dominican Republic, El Salvador, Guatemala, Honduras, Mexico, Nicaragua, Panama and Venezuela. Guadeloupe, Guyana and Martinique are Associate Members.

Source: World Bank, *Atlas, 1997*; World Bank, *World Development Indicators, 1997*.

ment its membership in NAFTA by negotiating trade and technical assistance agreements with Chile, CARICOM, Colombia, Venezuela, Bolivia and the Central American countries. It also joined the Asia-Pacific Economic Cooperation (APEC) and the Organization for Economic Cooperation and Development (OECD). Of course, it is also a member of the newly and loosely formed ACS and NAFTA. MERCOSUR and the Andean Group signed an agreement in April 1998 to create a South American Free Trade Area (SAFTA) beginning in the year 2000. Free trade agreements are also being contemplated with neighbouring countries. Frustrated with its attempts to get into NAFTA, Chile has negotiated trade agreements with MERCOSUR and the EU and is also entered into a bilateral agreement with Canada. It has already signed agreements with Bolivia, Colombia, Venezuela and Ecuador. It has also been admitted into the APEC Group. In most cases the share of intra-group exports in total exports is not high. In 1995, it amounted to 43 per cent in NAFTA, but in the case of MERCOSUR it was around 20 per cent, in the Andean Group 12 per cent, in the CACM 19 per cent and in CARICOM around 13 per cent. Intra-hemispheric trade amounted to just over 50 per cent.

Where does the Anglophone Caribbean fit into all this. As we saw earlier, the CARICOM countries have not been able to take advantage of the preferential markets to which they gained access. Preferences have largely served to protect traditional commodities. Caribbean countries still need to develop a manufacturing sector that goes beyond the simple assembly and packaging of foreign goods that cannot meet the required value-added criterion. Markets in themselves are not enough and greater attention needs to be paid to problems affecting production. In recent years, development and macroeconomic policies in some States have been addressing the question of quality and competitiveness, and this provides a good basis for further diversification of the production structure. The CARICOM market is small,³⁹ and this is certainly not enough to attract large-scale investment or to provide the economies necessary to bring down costs. The more developed countries of the region are increasingly looking for outside opportunities and, in this connection, more intense efforts are being made to attract foreign capital which is expected to bring entrepreneurs, marketing connections, technology, etc. Trinidad and Tobago expressed a desire to join NAFTA, but the question of relationship with groupings that require reciprocity is one that has to be studied more carefully, because some advantages with other groupings, such as the EU, could be lost.

With the Lomé IV Convention coming to an end in the year 2000, and with the new hemispheric configuration taking shape, reciprocity is an issue which must be addressed at some stage. If by accepting reciprocity Caribbean countries can gain more effective access to the markets of partner countries, the benefits from this in the medium term may far exceed those of existing arrangements which do not require reciprocity, but offer uncertain and highly qualified access. Some CARICOM countries are in a better position to deal with the issue of reciprocity than others and this may lead to some parting of the ways where trade relations with third parties are concerned. New bridgeheads may enhance the prospects for CARICOM which, incidentally, does not have the same significance for all its members.

Towards a new trade strategy

Notwithstanding the results of the Uruguay Round, many impediments to the free flow of goods, services and investment still exist in the global trading framework. Many areas of trade policy remain far from transparent. One reason for the continued interest in regional movements has to do with the desire of the participants to achieve liberalization beyond what has been agreed to within the global/multilateral framework. Because of their nearness to each other and common interest, members of regional groupings are able to pursue cooperation in areas that go beyond trade and investment. When there is a fair amount of homogeneity, cooperation can also be advanced at a faster pace with appropriate measures to accommodate the less advantaged.

Caribbean countries are caught in an economic maelstrom with both regional and international dimensions. The trends towards a more globalized and integrated world economy have unleashed forces which are affecting both the rich and poor nations and adjustments are being forced in both groups. National policy autonomy has been greatly reduced. Even before the end of the Uruguay Round the conditionalities associated with structural adjustment programmes had already challenged the model of national and regional import substitution in the Caribbean, where stagnation had already undermined the regional commitment and reinforced nationalistic tendencies. The slow movement towards development of a diversified competitive manufacturing sector and the threat posed to traditional exports are now forcing Caribbean countries to examine all the options and make hard decisions. Hemispheric changes have been profound, but technology has shrunk the world and now make possible alliances inconceivable two decades ago. The democratization of Latin America has been accompanied by a radical change in trade policy, and the reinvigoration of the integration movements reflects a deeper and more serious commitment to regional development.

In the evolving scenario, the Caribbean has to reposition itself. Differential and special treatment is becoming less important in the world economy, while concessional assistance is becoming increasingly difficult to access. The rapidly intensifying competitive environment may pose a challenge to current trade and development policies, but it also offers opportunities, particularly for small States with limited markets and resources. There is no doubt that preferences have influenced present lines of production and a major question to be faced is identifying the mix of domestic policies and external trading arrangements that could lead to a more optimal use of physical and human resources without producing economic and social dislocation. Caribbean countries are not only small, but are at differing stages of development and have different economic structures and tax systems. Some have large agricultural sectors, while others have a more diversified base and are better placed to make the transition to a more competitive setting.

There are various schools of thought about how the Caribbean should proceed in restructuring its present external trading relationships, most of which have had little effect in transforming national economic structures. The Caribbean is located in the western hemisphere midway between Latin America and North America, but still historically linked to Europe. The imperative to change the form of the Lomé Convention comes not only from the EU's desire to globalize its external relationships, but from the need to conform to WTO disciplines. Both with respect to the EU and the emerging integration trend in the hemisphere, the essential principle which has to inform the Caribbean's choice of external trading relationships must revolve around the need

for a transition period to rationalize existing production structures and for a geographic and policy framework which can encourage the creation of competitive and resilient economies. For the right 'trading atmosphere' there is no reason why some Caribbean countries should not be prepared to grant reciprocity. Joining group with group at a still delicate stage may be too much of a complex process at this point. The present trend is to allow individual members of the various groups to explore wider commercial contacts with other groups and States that are not incompatible with regional obligations and objectives. Such a process in time could create a network of relationships which leads to an increasingly larger trading space. The hemispheric concept could be realized from below moving upwards rather than through an imposed superstructure in which some countries would find difficulty fitting.

Both within the ACP group and among the developing countries of the hemisphere, the development of South-South cooperation has been disappointing. The use of strategies to encourage complementary development has been highly elusive. Countries often at a similar stage of development have resisted arrangements which would put them on a competitive plane. Vested interests have had a deep influence on national policy-making. The new global environment, whatever its weaknesses and uncertainties, by challenging the culture of protection across the board, could in time lead to greater South-South trade, once appropriate policies are in place. The market potential in developing countries is often greatly underestimated as a result of inability to market goods and services.

3. THE ROLE OF THE STATE AND THE IMPERATIVES OF STATE REFORM

Some general issues

Pressure to deregulate and liberalize their economies while retreating from involvement in the direct production of goods and services has not reduced the importance of governments to the developmental processes in poor countries. If anything, in the emerging competitive environment a greater responsibility is thrust on the State to provide direction, to ensure a competitive and up-to-date regulatory framework and to formulate and implement policies which reduce inequities in the society. In an age where information is power, the modern State has to be well-informed and sensitive to daily developments, both internally and externally. It has to explore opportunities for cooperation with other governments in fields which can benefit the local economy. It has to know how to mix its political concerns with its economic interests. Diplomatic skills have to be a basic asset of modern governments. The State has to interact with other governments in regional and international organizations, and maximizing benefits from membership in these organizations has to be a major objective. For small States, membership of such organizations can be an expensive matter. In negotiating agreements with other countries or groups preparatory work is essential, and the State has to be backed up by an organized and efficient bureaucracy. The private sector can help in formulating a position, but the State represents the interests of the entire society. A 'captured' State is an ineffective State. The vision of the State has to transcend partial interests and must reflect the well-being of the entire society. At all times the State must know what its options are and what are the costs and benefits associated with various alternatives. Research and monitoring of the economic and social environment have to be a structured and ongoing process in strategy formulation. For small countries, particularly, Statecraft and development diplomacy must go hand in hand.

External relations are an important complement to the function of the State at the domestic level. What the role should be, however, at the domestic level is not without controversy. While some favour minimal State interference, others point to the experience of certain fast growing States in East Asia, which involved a proactive State exercising varying levels of intervention to deal with issues of market failures and structural weakness. There are several different perspectives and interpretations of the role the State has played in these countries, but for good reason the State is widely recognized as a critically important player and an agent of change. The market needs the State for its orderly functioning.

The State has the power to change or make laws. The State is impartial (or should be) and has a legitimate right to be concerned about all groups or sectors in the society. The State as the conscience of the society has to pay attention to the social impact of economic policies. There are some things which only the State can do. Or put differently, there are some goods and services which only the State can provide. In the same way that a capable and efficient State can assist development and provide a higher level of welfare, an incompetent or poorly functioning State can be a hindrance to development. It is not enough for the State to have good intentions. The State cannot distribute what it does not have. The State occupies a unique position among actors in the social and economic fabric of each country and unless its role is informed by imagination, constant

review, cost effectiveness, a long-term vision and the exercise of functions that reflect its comparative advantage the overall outcome is bound to suffer.

In recent years, the threat to the legitimacy of the State has come from several quarters. The use of State authority by ruling cliques to brutalize opponents or to coercively maintain their stay in power served to weaken the moral basis of the State. Corruption of the State apparatus and the practice of patronage and clientelism have helped in creating parallel or informal economies in many countries, which by-passed formal rules and regulations. Declining foreign exchange earnings resulting from both internal and external developments and lower public revenues reduced the governmental capacity to deliver goods and services in a context where populist policies had significantly raised expectations that governments had unlimited resources and could not go bankrupt. Fiscal problems accompanied by stabilization programmes impacted on governments' ability to hold or attract personnel with high-level technical skills and this further weakened administrative and management capacity. The attempts by governments to govern societies with archaic or irrelevant laws and poorly functioning institutions in many cases took a heavy toll on social order, the administration of justice and the economic and investment environment. A major reaction to what was seen as a weakened and ineffective State (the delegitimization of the State) was the emergence of a variety of non-governmental organizations and other groups offering alternative solutions to persistent social and economic problems.

If the State has retreated in the face of attacks on its 'unwieldiness', its inefficiency, its amorphous presence and the increasing globalization driven by private sector interests, there is an emerging view that while the State must change, it must not wither away. In some areas there is need for more State. The State must retool itself and rethink its role to guide the process of change in a progressive and equitable manner. Equity and fairplay must continue to rank high in the concerns of the State. No system has yet delivered the completely just society. There is nothing wrong with a welfare function related to economic performance and delivered cost effectively. More than any other agent, the State is the conscience of the society and has to take both the short and long view and, therefore, must be concerned with the use of resources, the implications for future generations and the effects on the environment. Individuals concerned with daily survival and corporations preoccupied with profits tend to take the short view. Even in the present, theoretical life expectancy rates bear little relationship to actual mortality outcomes. The use of resources, the environment and the efforts to reduce or eliminate poverty are linked and raise critical issues for which the State must take paramount responsibility and provide practical guidelines in the context of internal and external pressures stemming from the internationalization of these issues.

Liberalization does not necessarily mean laissez-faire. There is no consensus on the role of the State, but the discussion has moved away from arguments of the 1980s about 'too much or too little State' to focusing on measures to achieve a more capable and efficient State to improve governance, mobilize resources and increase efficiency in an increasingly competitive environment.

A number of things that the State does can also be performed by the private sector. Given the revenue constraints and the rapid growth of public expenditure in both developed and developing countries, a great deal of attention has come to focus on the growth of the State, its performance in its various roles and the reform needed to make it a more effective actor and instrument. There is

a widespread discussion over what the State should do and what it should not do. Where the State's functions are concerned, generalization is always a difficult matter. In every country, the State has evolved in a particular political and social setting and reflects a range of historical factors and cultural values which may differ from place to place. In most developing countries the absence of a strong local private sector and the need to establish basic services encouraged the State to assume the role of 'engine of growth' (development promoter) and to put in place institutions and policies which could achieve this end. The State also assumed a welfare function using the tax system to finance a range of services, without discriminating among beneficiaries in terms of ability to pay. Expenditure often increased as a matter of course because these seem to be areas of high social value, but little attention was paid to the delivery system, efficiency, the quality of the service or the impact on the human resource base.

The first generation of reforms concerned itself with stabilization and, in some cases, resulted in increased unemployment and poverty without necessarily offering any promise of growth and development. Arbitrary cuts in expenditure to generate a budget surplus damaged both human and physical capital and further undermined the prospects for recovering from the initial crisis. Programmes to alleviate poverty which have come mainly as an afterthought, have generally been highly inadequate or misdirected. Increasingly, the approach is to deal with the question of poverty within the overall conceptualization of development that takes account of the specification of the particular case.

The Caribbean experience

In the Caribbean, the State has come to occupy a large and somewhat ambiguous role in the economic and social landscape. Following the achievement of political independence from Britain beginning in the early 1960s, the governments of the Caribbean countries saw the State as not only providing law and order, but as playing a catalytic role in the development process. The State was to provide not only the framework of incentives and regulations, but the social and economic infrastructure. This role assumed an increasingly larger dimension as the State began to acquire privately-owned enterprises in the production sectors for a variety of reasons including the need to save jobs or to take control of the 'commanding heights' of the economy. In the highly nationalistic atmosphere of the 1960s and 1970s, a large and visible foreign private presence in key sectors of the economy was seen to be inconsistent with the idea of political independence. New foreign investments were to be guided by investment codes which sought to define the spheres and terms of participation of foreign investors. Regulations governing the operations of the financial sector were also adopted to encourage greater local control and to retain a greater share of domestic savings for national development. These were backed up by stringent foreign exchange controls that were intended to support a fixed exchange rate system.

The State also assumed welfare functions, using the tax system as a redistributive mechanism. Some basic services, like health and education, were provided free while others were supplied at rates that could not cover the cost of production. Unlimited access to the offers of the Central Government removed the pressures to achieve efficiency.

With increasing population and growing demands for State services, the State bureaucracy increased significantly. To cope with the burgeoning administrative demands, the tendency was to employ more people rather than seek a solution through reorganization and increasing productivity. At the same time, wages and salaries were kept at levels below those prevailing in the private sector, thus making it difficult to attract skilled persons to the upper echelons of the public service. At the lower levels, wages and salaries in the public sector are generally higher than those in the private sector. In a number of cases, wages and salaries have grown to the point where they account for more than half of recurrent expenditures (see Table 28). In recent years the proportion has fallen in a few cases, for example in Trinidad and Tobago, as a result of structural adjustment programmes. Transfers and subsidies normally range between 10 and 35 per cent of recurrent expenditure. Part of the explanations for the figures at the higher end is to be found in the performance of State-owned companies. Many of the enterprises acquired by government were losing concerns, which did not even attract the interest of the private sector. Some profitable ones deteriorated as a result of a failure to improve management and accounting systems and to modernize their operation to increase efficiency and competitiveness. The result was that added demands were placed on the finances of the central governments. And this included the servicing of loans contracted by State-owned enterprises which the latter could not service.

Table 28

Selected Central Government Revenue and Expenditure Ratios, 1995

Countries	<u>As a percentage of GDP</u>			<u>As a percentage of Current Expenditure</u>		
	Tax Revenue	Current Exp.	Total Exp.	Wages & Salaries	Current Subsidies & Transfers	Interest Payments
Antigua	18	23	27	51	7	13
Bahamas	17	17	19	57	10	14
Barbados	28	30	31	38	29	19
Belize	19	20	26	55	11	10
Dominica	24	26	31	57	12	10
Grenada	25	23	27	53	22	9
Guyana	32	25	39	25	10	40
Jamaica	35	27	34	36	13	43
St. Kitts/ Nevis ¹	21	25	29	51	13	11
St. Lucia	22	23	33	54	16	4
St. Vincent	24	24	27	55	15	7
Trinidad & Tobago	25	26	28	37	32	20

1. 1994

Source: IMF, *Country Reports*.

The external shocks of the 1980s, and the impact on foreign exchange earnings on the governments' fiscal positions exposed not only weakness in the economy, but raised questions about the sustainability of welfare programmes and the level of State spending. Even before this, recurrent revenue was having difficulty keeping pace with the growth of recurrent expenditure. With the exception of Trinidad and Tobago in the oil boom years, budgetary savings were never significant, and for most countries the fiscal position deteriorated in the 1980s. Governments increased borrowing both locally and abroad to finance both capital programmes and consumption. Debt service payments as a proportion of government revenue and as a proportion of foreign exchange earnings increased to levels which forced expenditure reductions in other areas. In a number of cases the capital budget itself was reduced, resulting in a deterioration of the physical and social infrastructure. Real current expenditures in the social sectors (e.g. health, education, social security) also fell, resulting in worsening human conditions and a lower quality work force in a situation where questions were already being raised about the quality and effectiveness of the services provided. This had other consequences. An environment lacking in high quality social services not only makes it difficult to attract trained people, but also encourages residents with marketable skills to migrate, thus worsening the investment climate.

The economic crisis in which the Caribbean finds itself, increasing poverty in some cases and the changes in the global environment have forced Caribbean governments not only to review their development policies, but the role of the State as well. In a number of cases, the public service has been trimmed, but in certain instances the incentive schemes used to do so have lost the youngest and most talented, thus leaving a very weak base for development. At the same time, critical areas of the public service remains understaffed. In all the countries with a large State-enterprises sector, privatization programmes have been instituted thus reducing transfers and subsidies from the Central Government. Generally, health and education delivery systems are functioning under stress and are in need of urgent overhaul and modernization. The existence of unemployment with shortages of skills in a number of areas reflect the lack of planning and coordination in economic management. Inappropriate or poorly functioning health and education systems have major direct implications for the quality of the work force and ultimately for the country's ability to compete.

The State and development

The economies in the Caribbean have often been described as 'mixed economies' i.e. a mixture of State involvement and private enterprise. The State went beyond the provision of law and order, rules and regulations or essential services. The range of controls adopted to manage the economy and encourage development underwent little review and their distortionary effects are to be seen in the uncompetitive structures which make it difficult to compete in the domestic or foreign markets. Interaction with the global economy is taking place in a very limited way. The growth of trade and investment goes hand in hand with development. These countries are being challenged by the globalization process but they are not all benefiting from it. The growth of world trade and investment which has already reached record levels is likely to be further bolstered by the results of the Uruguay Round which not only relate to border restrictions but to a whole range of domestic policies which were once thought to be the exclusive preserve of national decision-makers.

In the emerging trading environment the practice of the 'control model' in the pursuit of development is becoming increasingly difficult to defend or sustain. No State could be unaffected by the economic and political forces shaping international policies. At the same time, the adoption of completely free markets without a role for the State is fraught with difficulties. The challenge for the State is to identify its 'comparative advantage' and to assume those functions which will enable it to perform effectively in a rapidly changing environment.

Increasingly, the view is that the private sector should be the 'engine of growth' and the State should act as facilitator creating an environment and a regulatory framework conducive to economic activity. Rhetoric is not the same as administrative efficiency. A credible State, it can be argued, is the foundation for social order and development. This means several things. First it means that the State must have a clear idea of its role, what is expected of it and its relationship to civil society. It must seek to operate not only efficiently but incorruptibly and with transparency. Its legislative function is crucial, and its aim should be not only to identify gaps and weakness in the law, but must seek to enact and update laws quickly. Laws must be enforced and administered efficiently, but because some laws are outdated their enforcement is often problematical.

Though the State must make it a habit of continuously reviewing its laws, there are some laws on the books of Caribbean States which have not been touched in decades. Laws and practice embody social and economic policy but very often they do not reflect current thinking and run counter to Stated intentions and objectives. When this is taken together with public institutions that are not functioning properly expected outcomes do not materialize.

In most countries of the region structural adjustment programmes have only been partially completed. The return of growth in some cases has led to some degree of complacency and the threat of regression is ever present. Trade and exchange control liberalization has gone a long way in some countries but the regulatory framework relating to operation of competition and monopoly is far from established in most States. Company laws have been slow to change and uncertainties in the business environment persist. Revenue and protection objectives in relation to national tariff structures and the CARICOM common external tariff are not yet settled. The system of fiscal incentives is in need of review as are the laws and regulations relating to foreign investment and the ownership of property. Rigidities in the labour market persist, while conciliatory procedures are slow and outdated and are in urgent need of overhaul. Fiscal reforms remain a major challenge as States grapple with the problems of rationalizing the public service, instituting incentives, reducing debt levels, funding pension schemes and privatizing State enterprises. Given the requirements of infrastructural development there is need for a framework which can encourage private sector involvement. Careful thought also needs to be given to the role the private sector can play in providing more efficient and modern health and education services.

There is a great deal that the State can do to improve the macroeconomic environment and encourage production, beyond the measures captured in stabilization and structural adjustment programmes. Some of these have deep historical and emotional roots and may require a longer period. But the State must be resolute and not allow inertia to set in.

In the light of past experience, it is important for governments to keep a balanced perspective on new ideas and thinking which carry pretensions of universal appeal, but often have serious shortcomings in specific applications. In the 1960s and 1970s there was a widespread assumption in developing countries that a highly centralized State using technical skills and modern planning techniques could transform agrarian societies into industrial economies and solve all the problems of poverty. While some growth was achieved, distortions increased and limited transformation occurred. The effects of this approach was not only felt in the structure of production but in the functioning of societies and in social values.

In the 1980s a high State presence came to be seen as part of the problem and a shrinking of the State, a greater role for private enterprises and the removal of controls to allow a greater freedom for market forces came to form the main planks of the medium term adjustment programmes. Markets and competition were proclaimed as the new mantra to remove all the constraints to development. Of late, however, a middle ground is emerging in which an effective and credible State is seen as a partner in the development process. In this paradigm the approach takes into account social relationships and practices which have proven their worth in sustaining communities, but which may not be found in textbooks and official reports. One of the concepts now in vogue is 'social capital' which refers to the economic value of shared norms and networks. It is not as easy to define as physical or human capital. The term itself may be new, but the social relationships and practices it covers have a long history in communities all over the world where people have confronted common problems by pooling their resources and know-how in cooperative actions. Social interactions can take place through simple everyday activities and by generating trust make greater cooperative interaction possible. Social capital is not a nebulous concept and addresses issues conventional economic theory has identified as impediments to development. Peter Evans⁴⁰ had summed up the benefits of social capital in four categories:

1. It lowers 'transaction costs – When you can count on the people you are working with (or trading with or borrowing from or lending to) you can focus on your main goals instead of worrying about enforcement and monitoring.
2. It increases information flows – When a community is closely connected, useful ideas will spread quickly so that everyone can take advantage of them;
3. It makes promising but risky ventures easier to try – When individuals feel they can count on their friends and neighbours they are more likely to try new strategies that will improve their lives, even if it means taking risks;
4. It makes possible coordinated pursuit of common goals – a foundation of trust and experience in relying on other members of the community makes it possible to tackle and sustain more complicated projects.

Since the concept of social capital links production and welfare at the same time, public policy has much to gain by fostering the development of social capital, some of which has already been destroyed in many communities. In the Caribbean, for instance, the disappearance of the extended family, the reduced status of key people like teachers and midwives and the waning of

informal financial mechanisms like 'sou-sou' and 'lend-hand' are seen as a loss of social capital which is reflected in the reduced abilities of people in many communities to cope⁴¹. At the same time there can be negative aspects to the expansion of social capital when members of a group or profession favors some sections of the community and discriminate against others. Exclusion has economic implications which can rupture a community.

Public policy can help in a number of areas. Governments can insist on access or entry rules being made more transparent. Rather than impose its ideas and products on local communities, both governments and local groups can become partners or co-producers in conceptualizing and undertaking projects with assets and resources from both partners complementing each other. Information on local problems and conditions can be critical to the success of an undertaking. No partner may have a monopoly on expertise and cooperation has a synergetic effect which enhances the chances of success. The State also has information on markets and technology which local communities may not have and can set up channels for the easy flow of such information to various groups.

The State and poverty

Development and poverty are closely linked. In a sense they are two sides of the same coin. It is impossible to discuss one without discussing the other. Poverty did not begin with the implementation of structural adjustment programmes in the 1980s, though in many cases retrenchment in the public sector, cuts in wages and salaries and reduced government spending in the sectors created a new group of poor to add to the chronic poor who did not benefit from ongoing development strategies. It is possible too, that without the adoption of structural adjustment programmes, the poor in some cases might have suffered even more.

While growth in aggregate output may help, growth by itself may not be sufficient to deal with the problems of poverty. It is known that growth can take place without an increase in employment or a reduction in inequality. It is widely acknowledged that since worsening social conditions can be destabilizing, the implementation of SAPs needs to be accompanied by measures to assist the poor, if reforms are to be sustained. How to do this has generated endless studies and a great deal of controversy that has often left governments more confused than ever. The tendency has been to put in place a variety of social programmes as adjuncts to SAPs, not so much to reduce or eradicate poverty, but to mitigate or ameliorate social conditions. Many of these programmes were poorly informed in terms of knowing who the poor are, the nature and causes of poverty, the location of the poor and the needs of the poor. In the absence of a proper framework of administration, safety net programmes have only limited effects.

Increasingly, the view is that poverty reduction and eradication must be an integral part of development programmes. Development must target both economic and social objectives so that growth, employment and equity are not seen as incompatible objectives achievable only in theoretical constructs. The premises on which the State acts must be re-examined, if civil society is to participate in decisions which affect its well being and also to ensure that State adopts an appropriate approach. The State must acquire a good knowledge of the poor and the causes of poverty in particular situations.

Whatever functions the State may be asked to assume or demit and whatever areas it may be asked to take under its purview, there is widespread agreement that it has a social responsibility for the way the society evolves and for holding the community together. It must be concerned not only with the growth of income but with the distribution of that income, with unemployment and with poverty in its various manifestations. Poverty is not good for anyone – not for the poor, not for the government, and not for society. It can lead to political instability which itself can affect investment, growth and development. It can lead to an increase in crime and it can also impact on the environment. In the 1970s and particularly in the 1980s, certain extreme positions emerged which argued for the retreat of the State and the promotion of competition and market forces as the instruments that would lead to greater participation in the world economy, which was seen as fundamental to the solution of domestic, social and economic problems. This was as unproductive as the other extreme view which held that high State control could bring about the desired transformation outcomes.

It is widely accepted that while economic growth itself does not necessarily lead to increases in welfare for the general population, it helps. The sharp decline in living standards in the 1980s and the difficulties created by structural adjustment programmes led to the view that poverty as a problem needs to receive special focus. The early approach was to simply try to alleviate the problem by making transfers and spending more on training and temporary relief and unemployment programmes. This was done in an ad hoc fashion without necessarily identifying who are the poor, what was causing the poverty, what were the needs of the poor, or where was poverty greatest. The approach was to mitigate rather than reduce or eliminate poverty. The effort was often vitiated by political patronage, corruption and clientelism. The unsatisfactory outcomes associated with poverty alleviation programmes had strong basis in some of the assumptions on which these programmes were formulated. "It is an excessively idealized notion to assume that the 'powerless' can easily be empowered and by means such as training (intensive or extensive), 'legalizing' their seizure of 'captured' land, making 'micro-entrepreneurs' of them, providing them with all the services (clean piped water, proper sanitation and solid and liquid waste disposal, access roads, secure shelter, and so on). First of all, the delivery ability and sustainability of the initial intervention has to be questionable, as well as expectations of decisive beneficial outcomes. ... Secondly, standardized re-education and training programmes hardly meet the necessary requirements of transmitting educational and technical progress to persons, especially the most disadvantaged at a level and a pace which they can absorb and over a sufficient period of time to ensure continuity of learnt new capabilities. Several of the poor are poor because they are less-motivated, more socially maladjusted slower learners than others also afflicted by poverty. It should not be expected that such persons could 'over-night' become entrepreneurs, own account workers, and responsible wage earners."⁴² The contention is that while there may be a case for immediate and direct relief, this should quickly be transformed into a programme of social development. The elimination of poverty is not a concern strictly for the poor but part of the larger programmes of social development.

With governments facing fiscal problems, it is difficult to increase social expenditures to meet the desired levels in critical areas. The challenge is to increase the quality of services through institutional reorganization, training, improved infrastructure, use of up-to-date materials and techniques. Greater spending does not always correlate with a larger volume of services or services

of a higher quality. With respect to the provision of water in Trinidad and Tobago, for example, almost half the water is wasted through leaks in the distribution system and consumers pay for this.

In the context of alleviating or eradicating poverty, there is considerable debate over not only how much governments allocate to various areas, but on the relative distribution as well. Though there are many causes of poverty, the contention is that certain areas such as education, are closely correlated with poverty and income distribution. In one study done on Latin America, education was found to be the variable with the strongest impact on income inequality and poverty. On average, one-fourth of total inequality was explained by the level of education.⁴³ Other studies have come to similar conclusions.

The question relating to the efficacy of the State involves not only what the State does, but how best to achieve its objectives. While trying to streamline the State bureaucracy and reduce costs, it has to be kept in mind that the efficiency of the State depends critically on having a range of skills, and, therefore, the need for an appropriate reward structure must not be underestimated. A simplified system of rules and regulations should help in minimizing corruption, but a structure that demands accountability provides a better safeguard against abuse of authority and the wastage of funds. At all times, the State should aim at maintaining the respect of the civil population if the population is to operate within the framework of law.

Increasingly, a decentralized State is being seen as a necessary mechanism in more effective governance. "For far too long, large-scale technocratic development projects in developing countries have been directed from above, administered by a distant un-coordinated and occasionally corrupt bureaucracy which is insensitive to local needs and concerns. Thus, projects have not involved the local people who have simply been treated as objects of the development process. Vast sums of money have been spent in the name of the poor, but very little has actually reached them. Even when it does reach them, it often perpetuates a cycle of dependency and an attitude of malfeasance and opportunism among the poor with an eye to milking the State cow for its uncertain bounties."⁴⁴ But decentralization may have problems of its own, since local elites may try to appropriate for themselves a large share of State spending. Still, decentralization offers opportunities for local participation in decision-making and for the State to draw on local resources using self-help and other techniques to assist poor communities.

Enhancing the position of the private sector

It is impossible to discuss the role of the State without focusing on the private sector. Surprisingly, the capacity of the private sector is often taken for granted. It is often assumed that once bureaucratic efficiency is increased, macro-economic stability restored and the regulatory fetters are removed, the private sector will be transformed into a dynamo capable of achieving what the State with all its powers could not do. Governments themselves will benefit since the "depoliticization of decision-making and the improved efficiency resulting from privatization will enable governments to reduce public outlays, cut taxes, reduce budget deficits, and shrink public sector borrowing."⁴⁵ There is a tendency to assume that simply transferring an enterprise from the public sector to the private sector would lead to increased efficiency, since the concern of private owners with profit and limited access to finance will force them to take the actions necessary to

reduce losses. The capacity of the private sector in many developing countries including those in the Caribbean is not well developed. Years of competition with the State for domestic savings, protection from competition, inability to access credit or up to date technology, limited experience with export marketing, high taxation, rigidities in the labour market, and inefficient government institutions have affected the growth and development of the local private sector.

In the context of the need to reform the State's finances, it was common to assume that the aim of State divestiture or privatization was mainly to rid the public sector of money-losing or badly managed enterprises which constituted a drain on the limited finance of the Central Government. The longer-term objective in rationalizing State-ownership, however, is to create a division of labour which enhances the production framework in a way which leads to a more efficient production of goods and services. Privatization does not reduce the management responsibility of the State. Some form of controls may become redundant as the new private owners may have obtained ownership with conditions that allow greater flexibility in pricing and operations. Since divestiture could lead to a concentration of ownership in private hands, or transform a State monopoly into a private monopoly, new regulations may be needed to ensure competition and prevent the exploitation of consumers. Besides the regulatory framework, the performance of the private sector rests critically on the existence of up-to-date and transparent laws, the availability of a skilled and healthy labour force, the State of the physical infrastructure, a functioning capital market, a tax system that is not burdensome, labour legislation and conciliatory procedures appropriate to domestic conditions and access to modern technology. In the Caribbean, not enough attention has been paid to the importance of Research and Development (R&D) and adapting existing technologies to local conditions. To be effective in developing countries, the market-friendly model requires a very strong working relationship between the State and the private sector, since the removal of some basic constraints to private initiative and the creation of a conducive environment for investment require the synergism of State-private sector cooperation. An essential requirement in forging a more creative relationship has to be a clear understanding of the roles of the respective partners within a transparent, legal and operational framework. The areas and levels of State intervention are not unique and can vary from one situation to another.

One of the major development challenges facing Caribbean States is undoubtedly the creation of a vibrant private sector able to respond to the opportunities being created through liberalization and deregulation. Producing for a larger, more competitive market or even for the local market without protective cover requires a different mind-set from one accustomed to producing in an environment with little or no competition. Producers have to be more innovative, more responsive to external market developments, more sensitive to technological improvements, pay more attention to R&D and acquire greater technical and marketing skills. Since these issues are linked to the expansion of the economy, the growth of exports and the creation of jobs, the State must have a direct interest and its own policies have to mesh with the requirements of the private sector. It is difficult, for instance, for the State to maintain an education system that does not take into account the direction of development policy and the skill requirements of the economy without contributing to an increase in unemployment.

For historical and other reasons, the State and the private sector in the Caribbean have not always had a very strong and productive relationship. Sometimes it has been positively suspicious

and antagonistic. Laws affecting private sector operation are often enacted without an adequate private sector input. Government Development Plans in the past have been articulated without a great deal of consultation with people engaged in private activity.

Based on size, national origin and integration into the formal economy, the private sector in the Caribbean can be divided into four groups:⁴⁶

1. Local, small-scale and informal entrepreneurs;
2. Local and mainly small and medium-scale enterprises;
3. Locally established and resident entrepreneurs with non-Caribbean origins or affiliation;
4. Non-resident, non-Caribbean, foreign business.

In terms of employment and diversity, the first group is by far the most significant. It includes not only the self-employed and street vendors, but an increasing number of cooperatives formed to advance the interests of their members. The second group, which is also indigenous, is more formal and organized, with activities spanning agriculture, processing, production and assembly of consumer goods and a range of service industries. It is difficult to separate the third group from the second, except that in the latter the scale of operations and networking may be larger and the managers or owners may be of foreign nationality or the descendants of second or third generation immigrants who may be still viewed as outsiders. The fourth group can be divided into two categories: the exclusively off-shore oriented operations related to the assembly of products for foreign markets and off-shore banking and other financial activities. The other relates to the large plants and tourism complexes drawing on local natural resources, using high level technology and marketing expertise, producing mainly for a foreign market. These operations involve a high degree of foreign ownership and management expertise.⁴⁷

The increasing withdrawal of the State from direct production requires it to play a more active role in helping the private sector to become more efficient producers by providing the kind of assistance needed. To do this, it has to increase its knowledge of the sector, its dynamics, its historical origins, its structure, its strength and weaknesses. It is now widely agreed that while poverty alleviation or amelioration programmes have their place, the cornerstone of poverty production has to be increased employment and output. The informal sector in most Caribbean countries has been growing even in the face of contraction in the formal sector and has provided an important cushion for both the chronic poor and the new poor. This says something about the dynamics and resilience of the sector. There is not a great deal of information on this sector. In Trinidad and Tobago, it has been estimated that the informal sector accounts for 23 per cent of employment as compared to 43 per cent for the formal private sector and 34 per cent for the public sector.⁴⁸ The sector which has grown as a result of economic pressures and the instinct to survive, has received increasing attention since it can provide insights into poverty and offer guidelines for government actions which have traditionally favoured the formal sector. There is a widely held view that with properly structured incentives, land reforms, access to improved technology, credit

availability and training, the sector could make a significant contribution to employment and income. There is also a view that too much formalization could stifle entrepreneurship.

The desire in the 1960s and 1970s to localize the economy as far as possible and to create an industrial base overrode serious consideration of the implications of size and the effects of some of the incentives adopted. The distortionary effects of the regulatory framework took a heavy toll on output and efficiency. Consumers paid a high price. Not only was the approach to protection based on the infant industry argument badly administered, but it was widely felt that some fiscal incentives were resulting in an unnecessary loss of revenue to governments, since the incentives did not appear to rank high among the factors influencing the investment decision. The efficacy of incentives needs to be reviewed regularly to determine whether they conform to market signals and the objectives of competitiveness and resource allocation.

With increasing liberalization, the policy of greater localization of ownership and decision-making of earlier decades has given way to more open policies toward trade and investment, but many of the existing practices and regulations relate back to the earlier period. The State may wish to have a regulatory framework that facilitates foreign investment, but may still wish to exercise control over the sale of land, work permits, the right to borrow locally, the disposal of waste, the pricing of natural resources, etc. The issue very often is not the right of the State to exercise some control over development but the transparency and quickness of the decision-making process. In restructuring the role of the State in the Caribbean, the problems being addressed have to be put in perspective and context. Failure to do this could result in increased chaos and confusion.

4. ELEMENTS IN THE STRATEGIC POLICY FRAMEWORK IN FURTHERING THE REFORM PROCESS

An overview of the reform and development process

In a dynamic setting where information is being generated and transmitted with increasing speed, knowledge on comparative situations and new ideas is continually changing the way problems are viewed and remedies proposed. Fresh insights, the postwar development experience, the perception of 'winners' and 'losers' in the development race and the outcomes of structural adjustment programmes since the mid-1980s, have thrown up a range of new perspectives which have challenged many commonly held notions of economic growth and altered the composition of typical development functions. The strong State-driven strategies of the pre-1980s have come under critical review but experience suggests that there are effective roles that the State can play. The lure of the market-driven paradigm is also being tempered by concerns of equity and the sustainability of reforms in situations where poverty is widespread or increasing. In most countries of the hemisphere, average GDP growth rates in the 1990s have exceeded those of the 1980s, though they are still generally below those of the 1970s. There is a large measure of agreement on the contention that economic growth can reduce poverty but it can also reinforce inequality. It can also reasonably be argued that poverty reduction can also lead to growth.

Despite increasing knowledge on how key economic variables respond to certain policy decisions, it would be wrong to conclude, however, that the uncertainty and the controversies surrounding the implementation of structural adjustment programmes (SAPs) have disappeared, and there now exists a consistent and unassailable body of ideas and policies which provide clear direction to development and the eradication of unemployment and poverty. Ideological positions, unfamiliarity with the development terrain, insufficient knowledge on specific issues and situations often mar diagnosis and can be reflected in proposed solutions and remedies. The most powerful in terms of financial leverage are not necessarily the most knowledgeable or best informed. The general principles of reform culled out of a variety of experiences must take into account local priorities, the stage of development, the social structure, the distribution of income and the functioning of markets and institutions if reforms are to be effective and if they are to make the desired impact. Many a programme of reform has suffered not only from improper pacing and sequencing but from an insufficient input of local thinking in analysis, conceptualization and even implementation.

With hindsight, and with a growing body of evidence following the adoption of emergency or quick-fix stabilization and structural adjustment programmes, there is an increasing degree of consensus in certain areas. The extreme position that all types of government interventions are harmful and that market forces and competition once let loose will remove all obstacles to development and usher in uninterrupted growth have now given way to propositions which call for a judicious mix of markets and governments. "Put simply, governments need to do less in those areas where markets work, or can be made to work reasonably well, and they need to do more in those areas where markets alone cannot be relied upon."⁴⁹ There still remains, however, a great deal of

ambiguity and controversy over what is termed 'the market-friendly model' and the 'strategic role' a State may be called upon to play beyond the provision of public goods and macroeconomic stability. The argument has gone beyond what the State should do, and what it should leave to the private sector. The limited impact of structural adjustment programmes, the failure of the centralized State, the increasing degradation of the environment, the breakdown of the rural economy, the disintegration of rural communities and the growth of the informal sector have put the spotlight on the State's relations with civil society.

With the drift of people from rural areas to urban centres and the increasing pressure on the social services, the State is being forced to take into account the traditions and practices of constituent communities as it seeks to refashion new modalities of government to counter the consequences of ineffective development policies, unacceptable levels of poverty, environmental damage and the challenge of globalization. What the State does not do is often as significant as what it does do. The State is a social construct and must have a clear idea of the strength and weaknesses of its constituent communities. National financial and development institutions often fail in a real sense because their operations do not take into account social realities and operate on structures fashioned by experiences of little relevance to local challenges.

Against the background of persistent budgetary and balance of payments problems there are many questions which have come to be asked of the structural adjustment programmes adopted in the 1980s, as a reaction to the emergence of internal and external disequilibrium in some Caribbean countries. The deflationary effect of stabilization policies had to be quickly supplemented by policies which could rekindle the growth process. The package of reforms widely used drew heavily on the experience of a small number of fast-growing economies in East Asia. The first generation of SAPs focused heavily on trade policy and fiscal reforms and assumed that within three to five years, a major restructuring of production would take place leading to increased income and employment.

SAPs have in some cases managed to reverse the slide and in a small number of others even helped in bringing about a moderate growth rate but generally they have failed in effecting the kind of transformation envisaged. Average GDP growth rates in the Latin American/Caribbean region in the period 1990-1996 ranged between -4.3 per cent for Haiti to 9.3 per cent for Guyana and 7 per cent for Chile. The average for the region was 3.3 per cent. If Guyana and Haiti, which incidentally rank as the poorest countries in the hemisphere, are excluded the average growth rate in CARICOM countries ranged between -0.1 per cent for the Bahamas, the wealthiest in terms of per capita income, to 3.8 per cent for Belize in the period. The OECS group averaged around 3 per cent. With this modest growth performance, poverty levels in Caribbean countries remain high and there has been little impact on the deteriorating social conditions that followed the adoption of SAPs in some cases. The adoption of safety net programmes to cushion the effects on the poor have suffered from a variety of deficiencies including unclear targeting, financial inadequacy and unsustainability and lack of an overall policy framework. It may not be an exaggeration to say that more resources have been expended studying the poor than helping the poor. With respect to SAPs, the time-frame for achieving results was generally too short, given the nature of the problems being addressed and the importance of institutional reforms in effecting change. The tendency to assume that a standard solution could be applied across the board without too much concern for the historical orientation

of the economy, the level of development, the distribution of income and wealth and institutional structure affected the outcome.

Nevertheless, the post-independence development experience in Caribbean countries has not been one of utter failure. Notwithstanding small size, limited resources and an unpredictable international environment they have been able to generate a moderate standard of living as reflected in per capita income, the level of employment and in health and education standards. Human and physical capital accumulation, though not at the level and of the quality it could have been, exceeds that in a large number of developing countries. This performance, however, has depended heavily on tourism and a narrow range of agricultural and mineral exports and access to preferential marketing arrangements. The effort to use import substitution as a way of diversifying and modernizing the economic base not only met with limited success but by increasing dependence on imports and concentrating on the local market, increased the vulnerability of the economies. Fluctuations in domestic production and external shocks have from time to time threatened internal economic stability and exposed the precarious nature of these economies. Recent trends in international trade policy and in the global economy, however, have narrowed the development options but also opened up new opportunities which call for radical changes in approach and development policy. At the international level the phenomenal growth in gross border flows of trade, services, investment, technology and cultural values is a reflection of the diminished importance of government restrictions and the challenge to regional and world cooperation. Old approaches will not work in this situation.

Globalization is a complex process and has an up side as well as a down side. While some communities may be blissfully unaware of the evolving trends or their impact, the Caribbean countries are open economies with economic performance and standards of living closely tied to trade and investment flows. More and more, Caribbean countries have to live by their wits and this calls for quick responses and more optimal use of human and physical resources as they seek to create resilient structures in a rapidly changing environment. The old boundaries of partnership have to be re-examined. In the face of collapsing security, economic and political alliances and traditional ties are coming under pressure as countries seek new alignments to enhance their position in the emerging new world order. Territoriality is taking on new meaning as States seek to refashion trading relationships in response to economic imperatives and competitive forces. Maps are being redrawn and governments have less power than they think. Global markets are being integrated largely through the transnational corporations which are constantly revising production and marketing strategies to meet global competition. With the liberalization of capital movements foreign markets are increasingly being serviced through the establishment of foreign affiliates rather than through exports of goods and services, the mode still largely used by developing countries. It has been estimated that the growth of global sales has exceeded that of exports of goods and services by a factor of 1.2 to 1.3 since 1987.⁵⁰

To survive in the contemporary world environment, the Caribbean has to reposition itself and develop new ways of thinking which would allow it to respond quickly and innovatively to external changes. The assumption in the 1980s that simply freeing up markets and prices in the context of a more stable, macroeconomic environment and transferring the 'engine function' to the private sector would restore economic strength was not well founded. Supply conditions have not

responded convincingly and the persistence of structural weakness has raised questions not only about the adequacy of the programmes themselves, but of the nature of poverty and underdevelopment. Structural adjustment programmes literally assumed away critical dimensions of the development problem by thinking that liberalization and deregulation by themselves could unleash the creative forces that could increase efficiency and production to the desired levels. Rigidities in capital and labour markets were seriously underestimated as was the power of the States to shake off vested interests and undertake regulatory and institutional reforms in a fairly short time. The capability of the State itself was an issue in terms of devising and implementing a coherent set of policies and fashioning an efficient and incorruptible bureaucracy.

The failure of industrialization as a transformation strategy must be seen as part of a larger failure involving the conception of and approach to development, economic management, the functioning of institutions, the use of resources and public sector efficiency. The early post-independence strategy was an urban-based one that largely ignored the possibilities for rural and agricultural development and the contribution of the latter to social improvement and broader-based development. Attention was often focused on urban poverty and the continued failure to address the problems of the rural sector only served to worsen the problem. Growth, it was assumed, would take care of income and employment, and the government apparatus would address the distribution issue. Development was seen largely as a technical and engineering function relying heavily on modern planning techniques and technology. Heavy store was placed on the accumulation of physical capital. There was no deliberate attempt to enhance or build upon the 'social capital' that existed, or to use as far as possible local raw materials and resources as the basis for a manufacturing sector. With stagnant or declining output in the 1980s, increased demand for public services was met by increased government spending and borrowing. In order to meet the need for increased revenues, the tax system became increasingly complicated and their incentive function lost a great deal of their effectiveness. Tax evasion and avoidance increased as the State took on an air of greater intrusiveness. With declining growth, governments became increasingly desperate and sometimes irrational.

Reform in many areas has been slow and painstaking. Most of the existing laws and regulations are a hangover from the colonial period and early post-independence years, and bear little relationship to present day challenges and realities. In most cases they are complex and lack transparency. Land tenure practices are a major problem affecting agricultural development and housing, even though the State is the largest owner of land in the Caribbean. The movement of capital and skilled people still suffer from the inability to reconcile the need to exercise some degree of national control in these areas with the advantages associated with greater access to investment and skills. Company laws suffer from major deficiencies, while the fundamentals for greater use of national stock-markets are yet to be put in place.

Apart from the incomplete and deficient legal and institutional framework, fundamental objectives are yet to be articulated in a coherent and comprehensive fashion to give credence to the policy and strategic framework. There is need for a clear vision of the role structure and orientation of the agricultural, industrial and service sectors in order to devise an appropriate policy within the liberalization process, or these countries could end with a diminished production capacity, dependent on outside sources for almost everything. What part of local requirement will be met from domestic

production and what part form imports will influence protection and incentive policies. The proportion of output exported will depend not only on foreign demand but on prices, design, quality, marketing, efficient delivery systems, service back-up, etc. Competition is a complex concept that involves much more than relative prices or quality. Technology and the mobility of factors make possible the production of a wide range of goods in countries with limited resources.

The private sector is not only in need of developing, but has to work more closely with the public sector. It is only in partnership can capital markets be developed and effective competitive and export strategies be formulated. A key area, which perhaps lies at the heart of Caribbean underdevelopment and retrogression is access to modern technology and its adaptation to local circumstances. National institutions have proven to be extremely weak in this area and their role, their capacity, output and relationship with the private sector need to be reviewed. The framework to encourage the protection of intellectual property and to safeguard the right of inventors and innovators has to be strengthened.

One recent study⁵¹ has found that 30-50 per cent rise in the demand for skilled workers can be attributed to the spread of computer technology. Other studies indicate that while computer-based technologies may reduce the demand for unskilled workers, overall employment can still be increased. The unemployment problem requires action on a broad front and how the region treats with technology and capital accumulation is a critical one. Increased efficiency may lead to some labour displacement in the short term, but the likely impact on competitiveness and growth can generate a level of activity that could increase employment opportunities. In the new global setting it is difficult to use defensive mechanisms to protect jobs in an inefficient or high cost environment. Increased efficiency and exports go hand in hand, but this need not lead to less employment where people are provided with opportunities to acquire the relevant skills and training that could increase their productivity. The separation of the education system from development strategy in the Caribbean provides the major explanation for the unemployment dilemma. A study of how this situation has persisted for long will provide an instructive insight into the causes of poverty and underdevelopment.

Organizational and institutional challenges in increasing policy effectiveness and delivery

The post-war development experience, and experiments with structural adjustment packages, have demonstrated in unmistakable terms that poverty and underdevelopment involve very complex factors and processes which do not easily lend themselves to simplistic solutions and approaches. Out of these experiences, however, have come useful lessons which should guide governments and aid agencies as they seek to put in place more effective policies and programmes which need to take account of specificities ignored or downplayed in earlier reform efforts. The tendency to approach heterogeneous situations with standard or near-standard prescriptions, often with little or no local inputs, has yielded limited results, and this has prompted the need for caution. A policy which works in one situation may not be effective in another because of assumptions made about underlying conditions and institutional development. A seemingly 'good' policy may get a bad name not only because of inadequate conceptualization, but because of poor implementation (including initiation in the wrong sequence) or because it is not supported by the necessary institutional and organizational reforms which are crucial to its success.

The time-frame for bringing about change has also tended to ignore the importance of particular political and social environments, and this has been a major factor in explaining the lack of significant success in bringing about lasting or fundamental changes beyond improvement in selected accounting variables. As a result of stabilization and structural reform programmes, internal and external balances have improved in some cases, but little impression has been made on basic structural factors or on prevailing levels of poverty. Though some growth has been achieved, vulnerability to external shocks remains critical and slippage and retrogression remain an ever-present possibility. Structural adjustment programmes in the Caribbean have increased frictional employment in a situation where there was already a large body of structural poverty. There is a tendency to see the poverty created by SAPs as 'transient' or 'temporary' and should be treated in a particular way. Many of the poverty alleviation or amelioration schemes appear to take this perspective, particularly since poverty now seems to cover an increasing section of the middle class. If the 'cosmography' of the poor is not properly defined and understood, there is growing fear that the transient poor could become an integral part of the chronic or structural poor.

The reliance on market reforms to instigate resource reallocation, factor mobility and increase efficiency has floundered in the face of an unwieldily and inefficient public sector (notwithstanding some piecemeal reforms), an inadequate rate of physical and human capital development, a regulatory framework giving confused signals, institutions with unclear missions and deficient capabilities. The political rhetoric has not been supported by action that is sufficiently quick, adequate or imaginative. In an open economy functioning in a competitive international environment, the existence of powerful disincentives to production compounds disadvantages related to resource endowment and structural factors with deep historical roots. In the first generation of reforms a great deal of naivete was displayed in the assumption that in all circumstances a quick supply response could be expected through the establishment of a free-market framework and macroeconomic stability assisted by a 'lean and mean' government. Very little attention was paid to the effects of budget cutbacks on the functioning of the State itself, the capabilities and structure of the private sector, implications of the limited pool of entrepreneurial talent, the problems of credit access in particular social settings, the operations of the banking sector, ownership patterns in the economy, the availability of land, the reform of factor markets, the power of vested interests, the legal framework governing competition, the enforcement of competition laws and the protection and enforcement of property rights and contracts. Not surprisingly governance has become a major issue in many developing countries in the context of straining administrative structures, technically weak civil services and the failure of centralized approaches to development to effect significant positive change. Even where laws exist, enforcement is often a problem because of lack of will or inadequate implementation capacity. In many areas reorganization and the creation of a framework that increases motivation and initiative may prove more effective in increasing administrative efficiency than greater public spending.

One of the heroic assumptions of the competitive market-driven model is that once responsibility is shifted to the private sector and the government knows its place and role, the pace of development would change and poverty would be reduced. The expected supply response has not materialized in many cases, and some countries in the Caribbean have become more dependent on traditional activities. Against this background, questions are being raised about the role of 'market signals' in situations of imperfect markets or where markets are not functioning properly. There are

some activities which are crucial to development, but it is not easy to relate inputs to outputs in these areas, and because they involve high risks or are associated with long-term returns, the interaction between the State and the private sector takes on special significance. It is now well established that simply increasing the levels of public spending do not necessarily lead to an improvement in the quality of public services or more productive facilities. Attention has to be paid to delivery systems which in the Caribbean involve administrative management and accountability cultures which require strong political will to change.

Issues in poverty and social services reform

Because of the attention which poverty issues receive, both nationally and internationally, it is often tempting to discuss poverty, as if it is a phenomenon distinct and apart from economic development. In situations where the concern is with the adequacy, or shortcomings of social mitigation or amelioration programmes, the question is often how to improve these to increase their efficacy in the short term in order to create an environment of stability. The more fundamental and long-term challenge, however, is to reduce poverty and this requires a combination of appropriate economic strategies and effective social policies. Trained, educated and healthy human beings are not only an objective of economic and social policy; they are a means to greater production and incomes and a higher standard of living.

While growth can help in reducing poverty, the relationship is not a simple and unambiguous one. Studies on growth-poverty reduction elasticity in the LAC region has ranged from -0.84 to 2 depending on the databases, time periods and poverty definitions.⁵² The effect growth has on income distribution may depend on a stage development. One hypothesis holds that inequality increases with income at the early stages of development and decreases at higher levels of income. There is also the view that the more unequal is the distribution of income, the greater the growth rate needed to make any dent on poverty. This view is seen as a possible explanation for the minimum impact of growth in the LAC region which evidence indicates to be 'notoriously inegalitarian'.⁵³ In the 1990s, it is estimated that only 4.5 per cent of regional income accrued to the lowest quintile of income earners, as compared to 52.9 per cent of regional income to the highest quintile of income earners. The concentration of assets (e.g. land) also helps to explain the impact of growth on poverty. With respect to structural reforms, the effect of these on distribution of income depends on several factors. Among them are the size and role of the traded goods sector and the relationship of the poor to that sector. The instrument of real devaluation of the exchange rate which features highly in structural reform programmes affect the producers of traded goods and the consumers of traded goods differently. "From the point of view of poverty, the most favourable situation for adjustment is in the countries where the poor are producers, but not consumers of traded goods. The least favourable situation is one in which the poor consume but do not produce traded goods".⁵⁴

One of the effects of stabilization and structural adjustment policies in the Caribbean has been a reduction of employment in both the public sector and the private formal sector. Real wages have also fallen and the poor are to be found both among the unemployed and the employed. For some countries of the region, the annual growth rate of employment has been growing at a faster rate than the annual growth rate of the labour force. Not only has the unemployment rate remained high, however, but the International Labour Organisation (ILO) has estimated that 94 of every 100 new jobs created in the LAC region between 1990-1995 were in the informal sector.⁵⁵ It has been noted

that these jobs are associated with low wages, job instability, lack of benefits and often poor and unhealthy conditions. There is some controversy, however, over how this problem should be approached. On the one hand, it is felt that greater accessibility to financial, technical and land resources could improve conditions in the informal sector, but the sector will have to be brought into the formal regulatory framework. There is an opposing view which takes a dim view of 'formalization' and argues that attempts to 'formalize' the sector would be counter-productive, since it is too much regulation that may be stifling entrepreneurial activity in the formal sector.

There are good reasons why governments of the region need to be concerned as much with existing poverty as with the long-term measures to reduce poverty and achieve self-sustaining growth. Poor nutrition, unhealthy living, inadequate education and training reduces the quality of labour and the ability of a country to extricate itself from the poverty trap. In the long term, the effect is felt on human development and on production capacity. Growth hinges critically on human development, physical capital accumulation and the productivity of these two factors. Human development is recognized as "one of the most, if not the most important determinant of long-term competitiveness and productivity growth Healthy and well-educated workers lose fewer work days to illness, are more productive at work, have greater inter-sectoral mobility, and have longer working lives."⁵⁶ A number of studies have shown that education is the variable with the strongest impact on income equality and poverty. One study shows that "on average, about one-fourth of total inequality can be explained as inequality between individuals grouped according to their level of schooling."⁵⁷

As indicated earlier, spending by Caribbean governments on the social services has by no means been negligible.⁵⁸ Public expenditure in education as a percentage of GNP for the LAC region in 1990 was 4.3 per cent (approximately US\$50 billion per year) as compared to 4.6 per cent for all countries. The ratio was higher than those of South and East Asia. Figures available for Barbados, Belize, Suriname and Jamaica in the 1990s indicate ratios of over 5 per cent as compared to less than 3 per cent for Chile and Peru. As a percent of GNP, public expenditure on health amounts to 3.55 per cent (not including 2.7 per cent for private expenditure), in the LAC region as compared to 3.22 per cent for all countries. Theoretically, a very high proportion of the population (in the case of Barbados, Trinidad and Tobago and the Bahamas, over 95 per cent) have access to health services. With the advent of stabilization and structural adjustment programmes in the 1980s, public spending in real terms has fallen in a number of cases, and this has impacted on the education system and quality of health care provided. One study has noted that despite the gain of recent decades, the LAC region's "average health and education levels today are lower than would be expected for its level of economic development, especially when compared with other regions of the world."⁵⁹ With respect to the education system, there are three specific areas where there is growing concern in the context of the need to increase competitiveness and reduce income inequality and poverty: low levels of academic achievement, the lagging of average educational attainment of the labour force behind that of other regions, and inequalities in educational opportunities which contribute to high income inequality and slow growth.⁶⁰ High drop-out rates (particularly among the poor) at both the primary and secondary levels, limited access to tertiary education, poorly motivated and trained teachers, unsatisfactory standards of physical facilities and sanitary conditions, unavailability of books, equipment and materials contribute to the present situation. Writing with respect to health and education systems in the region, the study has noted that the "failures in social

service delivery are principally the result of inefficiencies in the systems themselves” and that “greater progress is more likely to come from gains in efficiency than from increased spending.”⁶¹

The main reason for so much attention being paid to education is that it holds the key which can break the poverty circle. Educated and trained people are more mobile and can earn higher wages and salaries than those who lack learning and skills. Poverty, however, can be self-reinforcing, since poor children are often less prepared to enter school and physical conditions of schools in poor areas are often of a lower standard than those where the non-poor reside. Lower standards in public schools which the vast majority of the poor attend also contribute to lower performance.⁶²

With respect to health, spending by LAC countries on health as a percentage of GDP is higher than other developing areas of the world. Some of the impact of this spending can be seen in falling mortality rates and higher life expectancy. Mortality rates in the Caribbean are among the lowest in the LAC region. The health systems in the region, however, are also in serious crisis, and many of the deficiencies have come to the fore with the reduction in government spending. The unavailability of drugs, non-functioning equipment, the decline in physical facilities and inadequate professional care reflect the declining quality of health services and have become common in most countries, leading to an increasing number of people, who can afford it, to seek coverage in the private sector. The poor still depend on government social services.

The reorganization of the health sector involves a range of issues for which there are no unique answers since conditions vary widely from country to country. Among these are the role of the public and private sectors, the funding of health care, the balance between curative and preventive approaches and the administrative and organizational system for delivering the services. In the Caribbean, the administration of both the health and education systems have been highly centralized and, as often happens with all such systems, management and accountability issues have undermined their efficiency and their ability to meet the needs of the people who use them. Poor services accompanied by high costs point to the need for urgent restructuring of the social services delivery system that are critical to the development and functioning of people.

From both a social and development point of view, it is important to create a healthy and educated community. The importance of investment in human capital for economic growth has long been recognized. A healthy and educated community also creates conditions less conducive to crime and anti-social behaviour. Spending on health and education however has to be accompanied by effects to create opportunities for employment. The rate of growth of both human and physical capital and increasing productivity are critical to the expansion of production capacity.

Whatever concept one may have about the role of the State in post 1980s period, it certainly cannot exclude the formulation and implementation of an imaginative and effective regulatory framework. Because of the liberalization of the economy and the orientation towards a more market-oriented framework, many of the old regulatory institutions set up in a ‘control’ environment may have to be closed or restructured and new ones put in their place. Regulations themselves may have to be pruned, and more relevant and effective ones put in operation. The decision to have foreign investment play a larger role in the economy will also influence investment codes, purchasing of land, the incentives programme, access to local capital markets, competition policy and the tax

system. The need to closely monitor the effects of development on the environment will also place greater responsibilities on government agencies. With the down-sizing of governments, the private sector may also get more involved in the provision of infrastructural services and in this type of arrangement more innovative regulatory arrangements will be required. The need for faster and more efficient decision-making will not only require a more transparent framework, but reform and restructuring of the highly centralized public service whose role must be to provide a higher quality of social and economic services to the general community. Salaries, incentives, working environment and administrative structures have to be responsive to performance needs. The critical role of the civil service to overall development should not be underestimated. The civil service should be able to attract highly skilled people.

The challenge to the financial system

With the decline of the capital stock in some Caribbean countries, including the most wealthy, particular concerns are raised. Obsolescence and the effect of budgetary problems on maintenance have compounded the problem stemming from the fall in real annual investments in most countries.

The pace of physical capital accumulation is widely accepted in both developed and developing countries as a critical determinant of growth and development. In the Caribbean, more open policies towards private foreign investment has reduced neither the need nor the urgency to increase domestic savings and investment rates. If anything, the unpredictability of foreign capital flows and its concentration in certain sectors underscores the need for a policy framework that could lead to a higher level of savings and encourage the flow of resources to lagging sectors, not particularly attractive to foreign investors but of critical importance to development. Nurturing the saving/investment process is in itself part of the development challenge in terms of increasing self reliance and forging linkages between the real and financial sectors. The culture of controls is being questioned not only in the context of the negative effects on savings and the disposition of investible resources, but also in the context of the cost of funds, the establishment of more open systems and a lowering of exchange controls which have been a salient feature of economic management until quite recently.

Despite the shift to a more friendly attitude towards private foreign capital, Caribbean countries with one or two exceptions have not been successful in attracting significant amounts. Failure to achieve a persistent high-level growth rate, an opaque regulatory framework, even with respect to intra-Caribbean investment and infrastructural facilities below competitive standards provide some of the explanations. Some governments have signed bilateral treaties with certain industrial countries and entered international agreements as a signal of commitment to encourage private foreign capital, but the decision-making bureaucracy at the domestic level is still to be improved. Air transport to and from the Caribbean can often be a complex and painstaking undertaking. Even entering and leaving some countries can be a hassle.

In the Caribbean, because of fears of wrong sequencing and the nature of fiscal and balance-of-payments problems, reforms in the real sector have taken place at a faster pace than in the financial sector, where the implementation of certain structural, monetary and prudential regulations continue to raise questions about their effects on efficiency and the implications for raising the

saving and investment rates. The adoption of new laws in certain cases has gone some way in addressing some of the problems arising from recent bank failures and the growth of non-bank financial institutions. There has been some attempt to free-up deposit and loan rates and increase the independence of the central banks, but policy action is needed in certain areas, such as deficiencies in prudential regulations and supervision, the use of high reserve requirements to control banking activities, a more transparent relationship between banks and non-banks and a more explicit policy on competition among financial institutions. While the experience of other countries offers useful lessons in reforming the framework of laws and operational practices within which the financial system functions, Caribbean governments have to pay particular attention to their own circumstances in devising sequencing strategies and moving to new forms of controls. For instance, given the dubious links between interest rates and savings, Caribbean countries will need to be careful in adopting a real interest rate policy, particularly in the light of a history of relatively low inflation rates. At the same time, governments cannot be unmindful of interest rates spreads and their effects of investment in situations with limited competition.

Banks are the most significant financial intermediaries in Caribbean countries. Generally, however, their number in each country is small, creating an oligopolistic type of financial market which has raised questions about the prevailing degree of competition and efficiency. One study has found that operating costs as a ratio of total assets in the Caribbean averaged 11 per cent in Jamaica, 9 per cent in Trinidad and Tobago and 85 per cent in Barbados as compared to 3.34 per cent for insured banks in the United States.⁶³ Though there has been some attempt to attribute this situation to intense regulations, a recent study by the IMF on Trinidad and Tobago points to market structure. "Bank profits in Trinidad and Tobago have risen to record levels in the past two years. The spread between deposit and lending rates has widened to a degree not explained by reserve requirement changes. The prime lending rate is close to 17 per cent in an economy with both fiscal and balance of payments surpluses in recent years and low inflation. Cost-saving technological advances have not been shared with customers and the number of banks has been unchanged at six, after a consolidation from eight banks in 1993."⁶⁴ The study further concludes that the "large size of interest rate spread in Trinidad and Tobago suggests a capacity for monopolistic pricing."⁶⁵

A major concern facing Caribbean countries hinges not only on measures and policies to increase savings and channel financial resources to productive use, but how to attract and retain savings. A conducive macro-economic environment and governments' commitment to sound fiscal and monetary policies are critical. In a liberalizing environment there is need for new and imaginative regulations to deal with the greater mobility in the movement of savings across national frontiers. For example, the decision to allow residents to hold foreign currency accounts in local banks could become a conduit that drains savings from the local currency savings/investment stream, if regulations are not in place to encourage the banks to put foreign currency savings at the disposal of the national economy. Badly conceived measures can also be counter-productive. For example, the taxing of interest income from foreign currency accounts in local banks could drive these savings abroad and discourage new flows. This problem has to be handled imaginatively if the wrong signal is not to be give rise to fears that governments are not to be trusted. Non-interest bearing reserves in the central bank are not helpful in such situations.

Developments of active capital and stock markets both at the national and regional level should rank high on the list of measures required to satisfy the varied needs of savers and investors.

This is necessary for the efficient distribution of risk-bearing. The range of financial institutions and securities needs to be looked at carefully not only to meet specific investment needs in a situation where risks and returns vary, but to provide opportunities to savers. Venture capital funds are slowly taking their place in the financial landscape, but there exists a range of practices and regulations which stand in the way of more rapid development of capital and stock markets. In Caribbean countries because of the tradition of family enterprises, the number of public companies is small and this influences the stock exchange listing. Many companies cannot meet the requirements for inclusion. Some companies prefer to meet capital needs from borrowing rather than from selling new stocks. The informational infrastructure is lacking in most cases.

Table 29
Commercial Banks' Interest Rates in Selected CARICOM COUNTRIES, 1980-96

End of Period	<u>Barbados</u>		<u>Guyana</u>		<u>Jamaica</u>		<u>Trinidad & Tobago</u>	
	Deposits	Loans	Deposits	Loans	Deposits	Loans	Deposits	Loans
1980	5.6	11.0	11.5	13.88	8.75	15.86	6.06	11.70
1985	4.8	10.9	12.5	12.00	18.57	25.46	6.26	13.41
1986	3.5	10.2	12.00	15.00 ^a	17.35	26.92	6.08	13.25
1987	3.7	10.3	12.00	15.00 ^a	14.95	25.40	6.03	13.47
1988	4.5	11.1	12.00	15.00	14.30	24.94	5.83	12.05
1989	6.3	12.7	32.25	37.60	20.20	28.15	5.90	12.04
1990	6.1	12.1	28.10	32.44	24.50	31.59	5.53	11.73
1991	7.4	15.0	29.20	35.22	27.50	34.03	5.50	11.77
1992	5.0	12.6	18.17	29.76	23.00	46.04	6.34	12.76
1993	4.8	11.3	10.86	18.24	39.80	46.60	6.53	13.08
1994	5.0	11.9	12.81	20.80	27.85	45.79	6.50	13.81
1995	5.2	11.8	12.81	20.39	26.22	48.56	5.68	12.91
1996	5.0	11.9	10.50	18.46	20.79	42.19	6.39	14.24

a. prime rate

Source: *Official Publications.*

In the absence of exchange controls, and given the easy movements of funds which this makes possible, domestic policies have to be particularly sensitive to perceptions arising both from local developments and external factors. The exchange rate is susceptible not only to trade performance but to capital movements, and may move in directions not appropriate to the immediate requirements of the trading sector. The adoption of flexible exchange rate arrangements by some Caribbean countries, may remove some of the pressures on domestic policies to help restore external balance, but themselves can help create imbalance when rates assume levels consistent with capital account developments but inappropriate to the trading needs of the economy. In the Caribbean, foreign participation in local stock markets has not been significant, but direct investment flows can exert a large influence on exchange rate movements. Exchange rate regimes in the Caribbean remain far from settled as Central Banks continue to search for an institutional and operating framework that provide signals truly reflective of basic or 'fundamental' conditions. The experience both in the Caribbean and elsewhere that the exchange rate can come under pressure, even when 'fundamentals' are moving in the right direction should alert the authorities of the need for greater understanding of exchange rate changes and of the need to search for measures to deal with extreme volatility. The exchange rate is the most important price in an open economy and can easily overturn inflation and other objectives necessary for macroeconomic stability.

5. CONCLUDING OBSERVATIONS

A recent United Nations study⁶⁶ has indicated that while real GDP per capita⁶⁷ increased by 37 per cent in the developed economies between 1980 and 1996, it declined by one per cent in the LAC region and doubled in the case of Eastern and Southern Asia. In nominal terms, per capita GNP in the CARICOM region (excluding Haiti) averages around US\$2,700. While this does not compare favourably with that of the developed economies, which ranges between US\$20,000 and US\$40,000, or with that of some of the newly industrializing countries like Singapore (US\$27,000), or Hong Kong (US\$23,000), it is higher than that of a large number of developing countries. It is also not far behind that of certain second-generation Newly-Industrialized Countries (NICs) like Mauritius (US\$3,400), Malaysia (US\$4,000) and Thailand (US\$3,000). Besides the growth in per capita income a range of other social indices point to a steady improvement in the quality of life over time.

Notwithstanding their small size, limited resources and frequent vicissitudes, Caribbean countries have been able to attain a standard of living that places them among the top rungs of the developing countries. With the decline of traditional activities, dwindling aid flows and changes in the international environment, there has been some retrogression; and even to maintain the present standard of living, not to mention improving present social conditions, is becoming increasingly difficult. The failure to put in place a strong and diversified production base has left Caribbean economies in a vulnerable position, and forging the terms on which they interact with the global economy now has to be done in a more open and competitive setting that requires a different kind of mind set.

The fact that certain Caribbean States have been overtaken in the development race by some countries over which they enjoyed clear advantages in the 1960s, must raise questions about policies, attitudes, habits and approaches to governance and development. More intriguing is the observation that spending in such critical areas, like health and education, has by no means been insignificant. This would seem to signal that there are issues at stake other than finance. The post-war development experience and the results of the first generation of structural adjustment programmes point not only to the importance of policy, but to the quality of institutions, the legal and regulatory framework, the level of savings and investment, greater attention to research and development, and the calibre of governance and administration.

Structural reforms have started in both the real and financial sectors, but there are still problems with scope, the pace of change, sequencing, transparency and a clearly articulated long-term strategy of development. With the shortcomings associated with the import substitution policy, greater emphasis is being placed on export-oriented industrial development, but the policy framework for the transition is far from clear. There is some doubt in the literature about whether exports cause GDP to grow or the other way around, but the relationship between import-substitution and export development may well be one of emphasis. The scope for efficient import substitution should not be downplayed. With respect to the role of agriculture, a declining share of this sector in GDP was once viewed as a sign of development. In the Caribbean it could be seen as a reflection of failed agricultural and general development policy. There is every reason why agriculture should

be embraced as part of the general effort to increase import substitution, develop exports, create employment and reduce poverty. Agricultural development can serve as a basis for industrialization seeking to achieve a higher local content.

It has long been acknowledged that growth does not necessarily lead to development. One can also have growth taking place without any significant impact on poverty, unemployment or inequality. Broad-based growth, however, can help in creating employment opportunities. The issue of employment strategy cannot be separated from policies designed to improve the quality and range of the human capital stock. The existence of unemployment side by side with the demand for certain kinds of skills, to some extent, reflects the problem. Education and training cannot take place in a vacuum, but must be geared to technological requirements and development objectives. Curricula review and education delivery systems have to rank high on the reform agenda. A poorly functioning health system can also undermine the performance of the human capital base in an environment where fitness is critical to productivity and economic survival. In the present age, how a country equips itself technologically is also crucial to competitiveness and increasing per capita income. Technology affects all sectors of the economy, but some sectors have more access than others. Observations are often made about the effects of technology on employment, but technology can also save capital. In the medium and long term, technology properly used can increase employment and lead to a more secure employment base.

Stabilization and structural adjustment programmes have worsened the poverty situation in the Caribbean. In the short term, some poverty alleviation measures have been undertaken, but because of certain deficiencies their impact has been limited. Failure to act urgently in creating growth and employment opportunities could well see an enlargement of the chronic poor base, resulting in increased social instability. The fundamental challenge is to create perspectives which could increase the pool of entrepreneurs, make the business ethic more pervasive, encourage more purposeful use of savings and allow governance and administrative structures to emerge which can lead to greater participation in the development process. The centralized approach to development in the Caribbean has stifled initiative and increased dependency on the State. The bureaucracy created has been costly. Result-oriented institutions and a business culture have to become an integral part of civil administration.

Despite a shift in paradigm which emphasizes the private sector as the 'engine of growth,' the operational relationship between the public and private sectors in many areas remain far from clear. Markets are not perfect and a government still needs to intervene at critical points. Some goods and services can be provided both by the State and the private sector, but because of the social implications, the State may want to play the dominant role. There are some areas which demand a joint role, given the financial requirements and the critical function of the activity. One such is R&D and the transfer and adaptation of technology, which have not received adequate attention in the Caribbean development process.

It is generally accepted that a high level of savings and investment is a major factor in development. The importance of macroeconomic stability to increasing savings and investment of rates is widely acknowledged. Traditionally, the tax system has been used in the Caribbean to provide incentives to encourage private savings, but with the constraints on revenues, this has become more difficult. Increasingly, the trend is to use non-tax avenues, such as stock-market

development and pension arrangements, to encourage savings. In an effort to mobilize savings and to achieve more efficient financial intermediation, the tendency is to encourage greater competition in the financial sector. In most instances, adequate and transparent regulatory framework is still not in place. While the central banks have acknowledged the costliness of some traditional control instruments, new approaches have been slow in emerging. A major challenge is not only to mobilize savings, but to encourage their use in productive investment. An increased level of domestic savings may not only lead to a higher level of capital formation, but also to reduced dependence on foreign resources. A robust financial sector has a key role to play in development, but building the financial infrastructure needs careful attention. Sequencing is particularly important, and this needs to be informed more by practice than theory. Every situation has its own specificities.

The competition for foreign investment is leading to the creation of a more investment environment. The role of local investment, however, should not be underestimated, and a great deal more attention needs to be placed on the encouragement of small and medium-sized businesses. Investment policy also has to take a long view and recognize of the need to protect the environment and to make optimal use of national resources. A competitive framework is intended not only to meet consumer needs but must have a clear development thrust. The pace of change in the global policy framework is such that many developing countries are unable to gauge the impact on their own economies. The decision-making process has to become not only more efficient, but more broadly-based. Whatever the international regime, countries have a moral obligation to reconcile international obligations with genuine national interests.

END NOTES

1. In the continuing effort to advance political integration among themselves the small islands of the Eastern Caribbean established the Organization of Eastern Caribbean States (OECS) in 1981 to "strengthen links between themselves by uniting their efforts and resources and establishing and strengthening common institutions which could serve to increase their bargaining power as regards third countries." Members of the OECS are Antigua and Barbuda, British Virgin Islands, Dominica, Grenada, Montserrat, Saint Lucia and Saint Vincent and the Grenadines. Montserrat and the British Virgin Islands are still British dependencies. The Eastern Caribbean Common Market (ECCM) was established in 1968 to promote deeper economic integration among members of the group functions as a subgrouping within CARICOM.
2. At the CARICOM Heads of Government Meeting held in Jamaica in July 1997, Haiti was accepted as the fifteenth member of CARICOM on a conditional basis.
3. Webb (1997, p. 1).
4. See Webb (1997, p. 1).
5. IDB (1995, p. 194).
6. IMF (1995, pp. 69-71).
7. See John Page in Birdsell and Jaspersen (1997, p. 33).
8. See John Martin in Ramsaran (1995, p. 27).
9. See Bourne (1986).
10. See S. Edwards in Burki et al. (1995, p. 84).
11. See S. Edwards in Burki et al. (1995, p. 84).
12. World Bank (1997e, pp. 3-7).
13. BIS (1997, p. 101).
14. United Nations (1997, p. 3).
15. See Harris (1995).
16. World Bank (1993d, p. 4).
17. J.G. Williamson in Ranis and Schultz (1988, p. 29).

18. St. Rose (1996).
19. World Bank (1993; p. 3).
20. Baker (1997, p. xiii).
21. Baker (1997, p. xiv).
22. ILO (1997, p. 12).
23. IDB (1996, pp. 331-336) and World Bank (1997h, pp. 50-66).
24. IDB (1996, p. 248).
25. Siebert (1997).
26. World Bank (1996h, p. 21).
27. WTO (1996, p. 38).
28. WTO (1996, p. 36).
29. WTO (1996, p. 30).
30. World Bank (1997g, p. 134).
31. See Nurse and Sandiford (1995, p. 4).
32. See Sutton (1997).
33. WTO (1995, p. 16).
34. See Sutton (1997).
35. Demas (1981, p. 10).
36. Demas, (1981, p. 2).
37. The West Indian Commission (1992, p. 386).
38. The members of the ACS are: CARICOM countries (including Haiti and Suriname, but excluding Montserrat which is not independent) Colombia, Costa Rica, Cuba, Dominican Republic, El Salvador, Guatemala, Honduras, Mexico, Nicaragua, Panama and Venezuela, Guadeloupe, Guyana and Martinique are associate members.

39. Though the admission of Haiti more than doubles the present population of 6 million people, the per capita GNP of the expanded group is less than US\$1,500.
40. Evans (1997).
41. See Theodore (1997).
42. Duncan (1997).
43. Lustig (1995).
44. Bardhan (1997, p. 59).
45. Ramamurti and Vernon (1991, p. 75).
46. See World Bank (1994a, pp. 3-4).
47. World Bank (1994a, p. 4).
48. World Bank (1995a, p. 145).
49. World Bank (1991, p. 9).
50. United Nations (1997, p. xx).
51. BIS (1997, p. 25).
52. See Burki and Perry (1997, p. 88).
53. Burki and Perry (1997, p. 89).
54. Lustig (1995, p. 62).
55. Burki and Perry (1997, p. 91).
56. Burki and Perry (1997, p. 91).
57. Lustig (1995, p. 27).
58. IDB (1996, pp. 332-339).
59. IDB (1996, p. 242).
60. Burki and Perry (1997, p. 67).
61. IDB (1996, p. 242).

62. Burki and Perry (1997, pp. 98-99).
63. Williams (1996, p. 88).
64. IMF (1997, p. 50).
65. IMF (1997, p. 51).
66. United Nations (1997a, p. 233).
67. Exchange rate basis (1993 dollars).

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