

ISSN 1727-9917

S E R I E S

**STUDIES AND
PERSPECTIVES**

**ECLAC SUBREGIONAL
HEADQUARTERS
FOR THE CARIBBEAN**

A framework for Caribbean medium-term development

Michael Hendrickson



UNITED NATIONS

E C L A C

A framework for Caribbean medium-term development

Michael Hendrickson



UNITED NATIONS



This document has been prepared by Michael Hendrickson, Economic Affairs Officer in the Economic Development Unit of the Economic Commission for Latin America and the Caribbean (ECLAC) subregional headquarters for the Caribbean.

The views expressed in this document, which has been reproduced without formal editing, are those of the authors and do not necessarily reflect the views of the Organization.

United Nations publication

ISSN 1727-9917

LC/L.4291

LC/CAR/L.506

Copyright © United Nations, January 2017. All rights reserved.

Printed at United Nations, Santiago

S.16-01079

Member States and their governmental institutions may reproduce this work without prior authorization, but are requested to mention the source and inform ECLAC of such reproduction.

Contents

Abstract	5
Introduction	7
I. Macroeconomic stability: the foundation pillar	9
II. Building a competitive economy on the basis of economic restructuring and diversification	13
A. Green industries	16
B. Enabling economic restructuring and diversification: key drivers.....	17
1. Openness to trade and investment.....	17
2. A revitalized private sector in a reformed business environment	18
3. Innovation	18
4. Human capital upgrade	20
5. Mobilising and channeling finance to productive investment.....	22
6. Infrastructure.....	23
7. Upgrading the quality of institutions.....	24
III. Regional integration	25
IV. Social development	27
V. Putting the environment at the centre of development	29
IV. Conclusion	31
Bibliography	33
Studies and Perspectives Series: issues published	35

Figures

FIGURE 1	CARIBBEAN DEBT SERVICE, 2014.....	10
FIGURE 2	CURRENT ACCOUNT BALANCE	11
FIGURE 3	CARIBBEAN EASE OF DOING BUSINESS RANK RELATIVE TO ROSE, 2014-2015	19
FIGURE 4	HUMAN CAPITAL INDICES AND RANKS FOR SELECTED CARIBBEAN COUNTRIES, 2015.....	21

Abstract

This paper examines the key elements of a framework for Caribbean growth and development over the medium-term. The paper notes that while the Caribbean has made major adjustments in a challenging global environment, marked by slower demand, it needs to pursue a new sustainable development framework that integrates economic, social and environmental issues in a seamless way. Arguably, the foundation pillar of the new perspective is building a competitive economy based in part on diversifying into new productive activities. Given expected demand for low carbon products and services, investment in the green industries, including green energy, agriculture and tourism could provide the region with an important pillar of competitive advantage. To drive the diversification process, the region must address binding constraints in key areas. Important among these are improved macroeconomic stability and the liberalization of key sectors such as telecommunications and regional transportation to drive down costs and increase efficiency in production and trade.

Policymakers also need to design better policies and incentives to revitalise the private sector to make it the real engine of growth. This should include measures to improve the ease of doing business and enhanced incentives for investments in higher value added products and services that can compete in international markets. Nevertheless, a modern, competitive economy would only evolve if a number of binding constraints are addressed. An important requirement in this regard, is the need for a robust programme to upgrade the skills and competencies of the workforce and improved human resource planning to ensure that universities and vocational institutes turn out workers with the skills and expertise that are required in the workplace. In addition, the adoption of new technologies and greater investment in research and development (R&D) will facilitate the development of new products and services which can compete in new markets. Regional integration should be better leveraged through production integration such as the expansion of agriculture in Guyana and Belize with capital from other countries in the region and also through freer movement of labour. Also, greater attention should be focused on creating an efficient public bureaucracy to enhance service delivery in the region. This could be advanced by better use of information and communications technologies (ICT) and establishing standards for professionalism and effectiveness in the service.

Economic progress should be embedded in social reform to develop more transparent and equitable societies that are focussed on harnessing the full potential of each citizen. This requires tackling poverty and inequality through better employment and training programmes and well-targeted

social safety nets. It also demands improved systems of social inclusion and conflict resolution that provide opportunities for marginalised groups to participate in and benefit from development programmes. Further, the high crime rate in the region needs to be seriously addressed through strengthened national security, youth intervention programmes and criminal justice reform.

Finally, environmental conservation should be integrated into the development process. This should entail the efficient and sustainable use of natural resources, especially non-renewable resources, increased protection for natural species and biodiversity and reduction of the risk posed by natural hazards and climate change. The greater use of environmental audits and accompanying legislation to slow the depletion of exhaustible resources are important measures to reduce environmental risks. These policies together with disaster risk reduction will be critical strategies as countries pursue the Sustainable Development Goals.

Introduction

This paper outlines what are considered to be the key elements of a framework for Caribbean growth and development in the medium-term. The need to respond to challenges arising from both the international and domestic economic environment makes this a good time to sketch a pathway forward in advancing the region's development. On the international front, the global economy is undergoing an economic and geopolitical rebalancing with a diminution of the role of major traditional centres of international trade and finance. Moreover, in the aftermath of the global crisis, a number of factors have led to what has been termed a 'new growth normal'. This is marked by sluggish growth that is below the global potential.

A number of reasons have been put forward to explain this slowdown in growth. Important among them are the "secular stagnation hypothesis" that has been advanced by Krugman (2013) and Summers (2016). This posits that there has been a structural decline in global demand, owing to population ageing, rising inequality and changing technology (Reza and Sarker, 2015 and *The Economist*, 2015). This has led to saving outstripping investment, as persons save for longer retirement, for example in China. The other view is that the slowdown in growth is the result of cyclical factors such as debt deleveraging by businesses and consumers.

The Caribbean has been affected by the global slowdown. This has been reflected in sluggish demand for exports and increased volatility of foreign direct investment and remittance inflows. In general, the Caribbean economy is confronting major challenges, which if not tackled effectively, threaten to erode the developmental gains of the region. As a result the region could get stuck in a 'middle income trap', where it is unable to catch-up with more advanced economies. This document argues that a new development framework is required that responds to challenges in four broad areas as follows:

- Macroeconomic reform to reduce and eliminate chronic fiscal and current account imbalances.
- Economic restructuring and diversification as a platform for a competitive and flexible economy. This should promote improved openness to trade, incentives for a revitalised private sector with greater investment in tradable goods and services, human capital upgrading, innovation, appropriate finance and better institutions. These should be embedded in social and political reform to create equitable and participatory societies.

- Environmental reform to link production and consumption with sustainable use and management of natural resources.

These are broadly the critical areas to be addressed if the Caribbean is to successfully advance its sustainable development agenda. The model for tackling the deficits in these areas is of course not straightforward as there are synergies at the micro, meso and macro levels. Therefore, it is critical to consider these interactions in an effort to achieve sustainable development in the region.

While the Caribbean must pursue its own sustainable development agenda for reasons which will be outlined later, the region cannot do it alone. In fact, a number of international frameworks recognise the need for regional and international support. These include the 2030 Development Agenda and related Sustainable Development Goals (SDGs), the Samoa Pathway, which seeks to advance the sustainable development of Small Island developing states through their own efforts in conjunction with more effective international partnerships. The Sendai Framework for disaster risk reduction, the outcome document of the Financing for Development Conference in Addis Ababa, and the outcome of the Conference of the Parties on climate change in Paris (COP 21) round out these initiatives. The challenge is for the Caribbean to prepare the necessary programmes and specific high impact projects to attract available finance and capacity building to make the best of international cooperation. The rest of the document develops the four areas that have been identified and concludes the discussion.

I. Macroeconomic stability: the foundation pillar

By the nature of their insertion into the global economic system Caribbean economies are faced with inherent challenges. Crucial among them is that as Small Island developing States (SIDS), they have limited natural resources to facilitate development. Second, in light of their small domestic markets they are highly open to and dependent on trade, with trade openness indicators averaging in excess of 100.¹ However, such openness is not matched by flexible and competitive production and exchange systems that are necessary for the region to compete in a globalised world. As a result the Caribbean's ability to leverage trade as a vehicle for growth and development remains limited.

At the same time, despite their exposure to negative external shocks, Caribbean governments have a fair measure of control over macroeconomic policy-making. Therefore where policy levers are effectively applied they can provide a foundation for sustained and equitable growth. Macroeconomic policy-making in the Caribbean must promote economic stability² and encourage economic agents to channel factors of production into their most productive and competitive uses to boost exports and employment.

The most critical factor for achieving macro stability in the Caribbean today is fiscal consolidation and debt restructuring. The consolidation effort needs to be based on a combination of cuts in expenditure, especially the most inefficient components of current spending and revenue generating measures including tax reform such as the introduction of value added taxes (VATs) where they do not exist and increasing the rates for some taxes. Crucially, there is need for a harmonised system of incentives for foreign investors to reduce the likelihood of a 'race to the bottom' as countries engage in cut-throat competition to attract foreign direct investment.³

The majority of indebted countries in the Caribbean are highly indebted middle income countries (HIMICS). Their middle income status means that there is little willingness to provide a debt relief framework similar to the Heavily Indebted Poor Countries (HIPC) Initiative for them. Therefore,

¹ Openness is measured as the ratio of the value of imports plus exports to GDP.

² Key pillars of stability are stable prices based on monetary stability and stable exchange rates to provide confidence to agents in international transactions.

³ In some instances the incentives are so wide-ranging that there is doubt about the real net benefits that the country receives from the FDI.

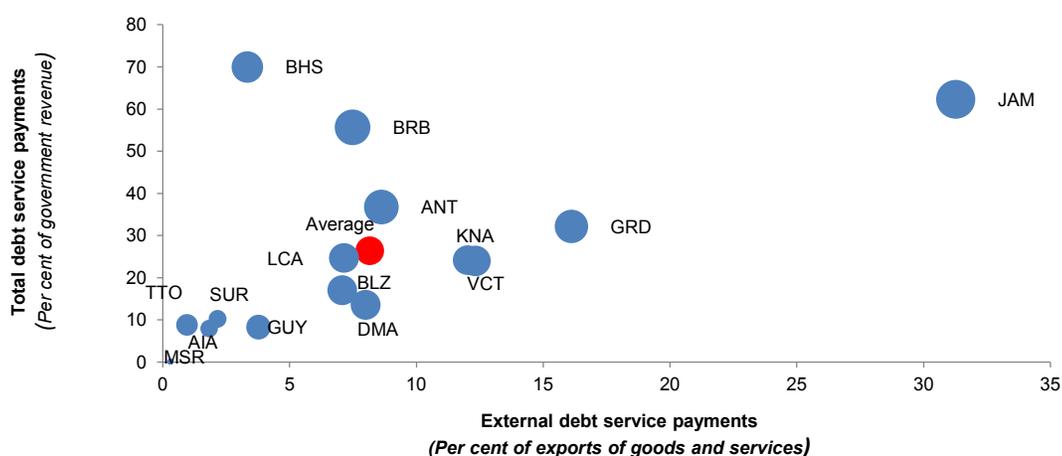
countries need to continue pursuing multilateral debt relief and restructuring through the Paris Club and bilateral restructuring and relief where feasible. UNECLAC's debt for climate change swap, which is aimed at securing relief to enable the Caribbean to develop green industries, improve energy efficiency and transition to a green economy is a timely initiative. Nevertheless, to ensure that debt restructuring and relief are effective they should not only provide adequate debt reduction, but must be complemented by improved fiscal management by governments and policies to boost long-term growth.

To be effective, however, the reforms⁴ must be based on careful analysis including public expenditure reviews to determine the effectiveness and efficiency of various components of spending and an audit of the tax system. These reforms are critical for bringing down debt levels and servicing costs to sustainable levels that would not impede growth. Indeed, the Caribbean is now one of the most indebted regions in the world and is certainly much more indebted than the rest of the small economies (ROSE). Since the global crisis of 2008-2009, Caribbean public debt has averaged over 77 per cent of GDP. This far exceeds the 56 per cent threshold above which Greenidge et al (2012) estimated that debt starts to hurt growth in the Caribbean.

The chart below shows that debt service payments, in relation to exports and government revenues are high. The chart shows that Jamaica in particular, has quite high debt service costs, but costs have increased significantly in the Bahamas and Barbados in recent years due to the decline in tourism services and foreign direct investment. Costs are also high in the OECS member States.

The implication is that the opportunity cost of debt service payments in terms of foregone public investment in development activities such as health, education and infrastructure is quite high.

Figure 1
Caribbean debt service, 2014

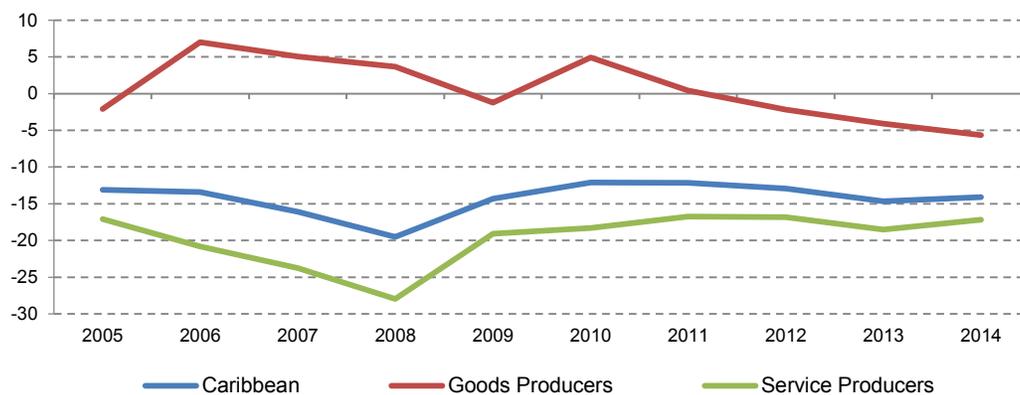


Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official figures.

The related imbalance on the external side is the chronic current account deficits on the balance of payments. This is related to the fact that growth in the region is balance of payments constrained. As a result, the countries need to grow their exports and foreign exchange earnings in order to import the capital and intermediate goods that are required in production process. Therefore, current account deficits make it necessary for the region to borrow overseas to finance its development (see figure 2 below). The deficit is the counterpart of inadequate domestic savings relative to investment. The sources of this deficit on the current account in the Caribbean are uncompetitive exports and inefficiency in the use of imports and high net payments to foreign investors in the region.

⁴ The region has made progress in other reforms including trade liberalisation, including the reduction in tariffs and quotas, the privatisation of inefficient public utilities, the strengthening of the financial sector through improved regulation, onsite monitoring and the use of risk-based stress-testing.

Figure 2
Current account balance
(Percentage of GDP)



Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official figures

As the figure shows, the current account imbalance is especially acute in the service producers, where tourism, financial and other services have not performed as well as commodities such as fuels, gold and alumina during the 2000s. The current account deficit would have to be ameliorated by developing more competitive export sectors, through investments in upgrading these sectors or developing new ones.

II. Building a competitive economy on the basis of economic restructuring and diversification

Caribbean economies have lost ground in traditional markets for their products and services. This has been reflected in a fall in the region's world market share for goods and services and widening current account deficits in the majority of member countries. For instance, the Caribbean's share of world exports declined from 0.5 per cent in 1980 to less than 0.2 per cent in 2012 (World Bank, 2014). Also, using a simple nominal price comparison, Laframboisie et al (2014) found that the price of a one week beach holiday in the Caribbean was higher than other beach regions in the world. Nevertheless, as small economies, regional firms are hard-pressed to compete based on economies of scale. Therefore, regional exporters need to upgrade their production and trading systems to compete based on productivity, innovation and the quality of their exports. To do so, a number of exporters will need to focus niche segments of global value chains, where small volumes of high quality products and services can be profitable.

Decades after independence, economic dualism remains the primary feature of the Caribbean economy. The economic landscape is marked on the one hand by traditional sectors and informal activity with relatively low levels of technology, low or semi-skilled labour and low productivity. These activities are found mainly in traditional agriculture, some segments of tourism and enclave manufacturing and services such as low grade business processing services. By and large, these activities are inefficient and are unable to compete on the international market. The other side of the dual consists of relatively high productivity firms using modern technology and skilled labour. These are usually domestic supply chains of multinational firms, including mining, large scale manufacturing such as steel production and large hotel chains. This gives rise to sectoral heterogeneity, which affects overall growth rates.

Nevertheless, even in those firms which are internationally competitive there is limited innovation and efforts to produce differentiated products to meet the special needs of customers. This is evidenced by the dearth of patents that result from R&D and innovation in these firms, the World Bank (2014) indicated that the Caribbean has made fewer patent applications per capita than other regions of the world in recent years. For example the Caribbean made 30 patent applications by residents between 2005 and 2012, whereas Non-Caribbean Small Islands made 1076 applications. Also, high tech exports

as a percentage of manufactured exports averaged 11 per cent for Non-Caribbean Small Islands, but only 5 per cent for the Caribbean.

Another indicator of relatively unsophisticated nature of Caribbean production is that even its most competitive firms are mainly imitators of product and process inventions from advanced economies. Meanwhile, there remains a large productivity gap between the most and the least competitive firms. Therefore the task of economic restructuring and transformation is therefore to push the productivity of the traditional sectors closer to the modern sectors and to imbue the modern sectors with a drive for innovation; invention and problem solving that meet the needs of high-end consumers, especially in export markets.

The competitiveness of Caribbean firms has been constrained by a range of supply side and institutional constraints. A critical factor in this regard has been low import productivity⁵ or efficiency with which foreign exchange is used to drive production. This is vital since growth in the Caribbean is constrained by chronic balance of payments deficits. Other key factors include inefficient markets for labour, financial services, energy and transport including information and communications technology (ICT). These combined with weak public sector institutions and poor policy choices in some instances have pegged back growth and adjustment in the region.

Therefore, a critical pillar for achieving medium-term growth entails rebuilding of export capacity in areas of comparative advantage and the search for new areas of potential competitive advantage. This entails a two-pronged approach - the first is economic restructuring, which is aimed at upgrading of traditional sectors, including agriculture, mining, light industry and tourism to make them competitive. This would entail enhancing the quality of production through innovation based on the use of improved technology, skilled labour, research and development and market intelligence. The second is economic diversification which entails developing new products and services and finding new markets to expand trade.

In practice, restructuring should focus on exploiting the available opportunities for innovative production in the traditional sectors to create high value added products and services that can capture market share both in the domestic and international markets. In the case of agriculture, the creation of a dynamic agro-processing sub-sector that adds value through processing of food crops, animal and fisheries products is an underexploited opportunity in the region. Agro-processing increases the price that food products can fetch by raising their quality, shelf-life and portability. It is estimated that consumer food products account for over 50 per cent of Caribbean's annual imports from the United States, comprising mainly poultry, red meats dairy products and processed fruits and vegetables. This list suggests that there is definite scope for substituting imports with higher domestic production. This can be facilitated by achieving greater economies of scale by expanding production in the larger countries such as Guyana and Suriname. Indeed, businesses in Trinidad and Tobago are now investing in food production in Guyana.

The regional mining sector also presents significant opportunities for increasing value added by tapping into downstream activities. The petrochemical sub-sector for instance presents opportunities for downstream activities such the production of plastics, melamine, pharmaceuticals and other products. Global demand for flat-rolled and extruded aluminium products is expected to increase by 5-6 per cent between 2016 and 2020, in response to growth in transportation (Djukanovic, 2016). Caribbean alumina producers need to explore how they can capture a share of this downstream market. Although economies of scale have limited the Caribbean's opportunities in large scale manufacturing, there is scope for niche manufacturing centred on high technology content, innovation and flexibility.

It is not anticipated that the market mechanism would provide the full range of incentives that are necessary for restructuring and diversification. The region will have to design a strategy that mixes market instruments and a smart industrial policy. Broad market-friendly or horizontal policies that entail broad support for a range of firms through ensuring macroeconomic stability, transparent property rights, the rule of law, ease of doing business and a strong public bureaucracy, among other factors, might be

⁵ This is defined as output per unit of imported intermediate inputs.

best suited for sectors and activities where there are no important market failures or missing markets. However, as Monga (undated) and Rodrik (2004) have argued, selected or targeted policies are often required to promote learning, technology adaptation and knowledge spillovers that are necessary for the upgrading of traditional sectors and the development of new sectors. In the Caribbean it is expected that the development of sectors such as ‘green energy’ and non-traditional agricultural exports and the creative industries might require selected industrial policies. Nevertheless, this would require the government to work closely with the private sector to undertake the market intelligence that is needed to decide where to direct investment resources. Also, support should only be for a period of time and there should be performance benchmarks, which are monitored and evaluated regularly and a willingness to change course if the policy is not working.

The second plank of building a competitive economy is economic diversification. The recent literature (Imbs and Wacziarg, 2003) and Rodrik (2007) suggests that economic growth and convergence of poorer countries is driven by economic diversification rather than specialisation based on comparative advantage. Indeed, specialisation comes later in the development process, after countries have achieved a threshold standard of living. This reinforces the point that at their present stage of development, Caribbean economies need to pursue an active diversification strategy to find new sectors and industries that can drive sustained growth and development. In fact, this is an essential part of the process of creative destruction where old sectors are replaced by new ones to maintain the engine of economic growth. Furthermore, diversification is crucial to reducing the risks of over-reliance on a few products and services, so that a collapse in demand or impact of a natural disaster on one sector does not jeopardise foreign exchange earnings and growth.

The Herfindahl-Hirschman index of export concentration⁶ is often used measure of export diversification. Longmore et al (2014) found that the index for Trinidad and Tobago fell from 0.8706 in 1980 to 0.2480 in 2010 implying on the face of it that important strides were made in diversification. Nevertheless closer examination of the export product structure indicated that most of the diversification has occurred within the energy sector. Therefore, the risks from declining global demand for energy products remain quite high. Also, Trinidad and Tobago remained less diversified than other small island economies and also islands which were net exporters of oil products. The situation has been similar in other Caribbean islands where countries have diversified within segments of the tourism industry or light manufacturing, but nonetheless remain quite vulnerable to the fortunes of a few sectors.

Economic diversification in the region should include a mix of horizontal and vertical diversification. Horizontal diversification refers to moving into and innovating in existing product lines and the creation of new products or service lines in the same sector, for example, new clothing lines from different materials in the clothing sector. Vertical diversification relates to producing other components or services within an industry- that is developing backward and forward linkages such the production of plastics and fertilisers in the petrochemical sector; and also the shift from a given sector or industry to another (Hvidt, 2013). There are opportunities for horizontal diversification into eco and heritage tourism in countries such as Belize and Guyana and also in agro-industry in the region. In addition, vertical diversification opportunities are available in sectors such as renewable energy, the creative industries and offshore education services. Nevertheless, countries need to remove hindrances in the incentive and institutional frameworks to stimulate private investment in these activities. Important among these are tax and regulatory disincentives, the ease of doing business and development of a more flexible labour market to allow persons to move between jobs and across countries in the region.

The challenge is to determine the right mix of policies and strategies to achieve an adequate level and quality of diversification. Obviously, the market should be used to allocate resources to areas of comparative advantage where market incentives would lead to the most efficient and socially optimal outcome. This is usually the case for the traditional sectors such as mining, export agriculture and large foreign-financed tourism.

⁶ The index ranges from 0 to 1, with indices that are closer to 0 suggesting higher levels of export diversification and an index close to 1 implying extreme export concentration as exports are dominated by just a few sectors.

However, it could be argued that the market incentives might not be enough to drive vertical diversification into new sunrise activities in the Caribbean. This is so because finding new sectors and activities entail search costs, learning by doing, experimenting with different options and costly market research and coordination (Stiglitz, 2016). In some cases this might lead to positive spillovers for firms and industries that do not contribute to the costs of these activities. As a result of these externalities, these critical developmental services tend to be underprovided by the regional private sector. Moreover, the Caribbean also faces missing or underdeveloped markets for financing business start-ups such as venture capital and angel investing and also for research and development and intellectual property development. This implies that although the private sector is expected to spearhead the diversification thrust, there will remain an important role for the state where there is markets failure or missing markets.

Caribbean states therefore have a role to play in designing smart, effective industrial policies to leapfrog the diversification process. The new industrial policy framework should reduce incentives for traditional low value added and also highly polluting activities and provide greater incentives for new high value added and green activities. Nevertheless, given weak government finances in the region and limited government capacity for monitoring and evaluating the performance of recipients of incentives, governments should focus on the most binding constraints to the growth of new activities.

There are four areas where there are binding constraints which industrial policy can alleviate thereby providing high social rates of returns. First, regional governments should design smart technology and innovation policies. This requires selected incentives including training and extension services, upgrading vocational institutions and partnerships with private firms to promote R&D, learning and the diffusion of technology in the wider society. Second, education and human capital development policies need to be more targeted to develop expertise and problem solving skills among workers. This is especially important for enabling the region to develop a competitive niche in the green industries, such as producing and servicing solar panels and greenhouse agriculture. Third, governments also need to incentivize the development of appropriate financing mechanisms for financing new activities. This could start with further liberalisation of the financial system to bolster competition in the banking sector to reduce lending rates, crowd funding. Also, major hurdles to starting businesses should be removed to encourage the development of venture capital and merchant banking institutions to provide funding for new start-ups, especially in the SME sector. Fourth, governments need to invest in upgrading transport and logistics systems and market research and intelligence to facilitate exports by SMEs.

A. Green industries

The green sector could provide an important pillar of the diversification thrust into new activities. The increasing priority being given to climate change mitigation and adaptation means that green industries are expected to become more important in global demand. Some countries are already transitioning to green growth as a new growth strategy. As UNEP has noted, green industries offer the potential to invest in environmentally significant sectors, while at the same time contributing to sustainable development and poverty reduction (UNEP, 2010a and UNEP, 2010b.)

Currently, energy imports have constituted as much as 30 percent of imports for countries of the region. However, fuel prices have fallen recently, and it is expected that a number of factors may interact to keep international petroleum prices very depressed for the medium term. The normalisation of relations with Iran, the introduction of new technologies in the exploitation of oil shale, and the economic slowdown in China, are significant developments that might keep energy prices lower than they have been in the last ten years.

In light of this, Caribbean governments/countries should be harnessing some of the savings on energy imports to explore opportunities in renewable energy. The reality is that the shift to renewable energy is a decided trend for the future. Therefore Caribbean countries should get on the bandwagon early to capture a decent share of the market. Renewable energy provides an ideal opportunity for galvanising the diversification effort in the region. Indeed, green energy should provide the foundation for activities, including the greening of traditional ‘grey’ sectors such as agriculture, light industry and tourism and also the introduction of new green products and services.

To their credit Caribbean governments have adopted Worldwatch targets for renewable power capacity. Nevertheless, the targets are ambitious and include 20 per cent renewable power capacity by 2017, 28 per cent by 2022 and 47 per cent by 2027. It also includes reductions in energy intensity and power sector CO₂ emissions by 33 per cent and 36 per cent by 2027. Although these targets might not be met by the established dates, concerted effort could lead to the region not undershooting some of the targets by much. This stems from the fact that there is significant renewable energy potential in the region including hydropower, solar, wind, biomass, geothermal and ocean thermal energy⁷ among others. Some of these sources are already being tapped in the region. The challenge now is to design an integrated strategy across the region to audit the potential of each source and to create an environment that encourages the domestic private sector and foreign firms to invest in the viable options in individual countries.

B. Enabling economic restructuring and diversification: key drivers

Having outlined the restructuring and diversification challenge, it is now useful to examine the key drivers of this process. The main structural factors that are necessary for advancing a successful restructuring and diversification effort in the Caribbean are: openness to trade and investment, a revitalised private sector, human capital development, mobilising adequate finance, the level of technology and innovation, the quality of institutions and the business environment.

1. Openness to trade and investment

Although Caribbean economies are relatively open to trade and investment, protectionist barriers remain in a number of areas. Sections of the regional economy including telecommunications, banking and transportation services could benefit from the disciplining effect of increased competition. This would not only drive down prices for consumers, but also force service providers to improve the quality of their services, thereby enabling these important sectors to better facilitate growth by boosting productivity in other sectors.

Another important area of reform that is required is the anchoring of trade policy in productive development policy. It is a given that the quality of products and services that are traded are directly linked to the quality of production systems. Moreover, trade in the modern context takes place for the most part in global value chains or production networks. Therefore, Caribbean countries need productive development policies and institutions to provide knowledge, targets, standards and extension services to help regional firms enter these value chains. Important areas of capability development that are needed include: information on the most appropriate technology for particular segments of production and service delivery, creating better links between education and training and production in firms and strengthening development finance institutions such as development banks to ensure their viability.

Openness to investment has enabled the Caribbean to attract substantial infows of foreign direct investment (FDI) in the last few decades. However, FDI remains concentrated in resource-intensive activities with relatively low value added, including mining, tourism and plantation agriculture. The region needs to attract more efficiency-seeking FDI, which could provide an avenue for exporting competitive niche products and a range of services. However, to facilitate this, governments would need to invest in upgrading the quality of the human capital base and strengthening the regulatory environment to provide a more attractive environment for this type of FDI.

⁷ The Development Bank of Latin America (CAF) has noted that there is significant potential for deep seawater air conditioning (SWAC) systems in the Caribbean. This could provide a renewable energy source for air conditioning systems, which account for some 40 per cent of energy consumption in hotels and resort properties in the region.

2. A revitalised private sector in a reformed business environment

It is well acknowledged that the private sector, as the engine of growth, has a pivotal role to play in economic transformation in the Caribbean. However, two sets of constraints have to be tackled to unleash the potential of the sector. The first is a set of internal constraints relating to the structure, motives and operations that limits the growth firms, especially in export markets. The second relates to a range of supply side obstacles that stem from weaknesses in the business environment and incentive framework.

With respect to the internal factors, most businesses in the Caribbean remain trading concerns, which use rather than generate foreign exchange. This is indicative of a risk adverse culture among many businesses, which prefer the ‘quiet life’ of trading, rather than the hard effort required to produce new goods and services, especially for export. It also reflects an incentive framework-duty concessions and other facilitation- that favours trading over production. The nature and structure of the private sector also point to three critical issues. The first, is that many businesses remain family owned and are not listed as public limited liability companies. This cuts them off from the advantages of incorporation, including the ability to raise capital through the issue of shares, the limitation of personal liability for the owners/operators and the division of ownership and control. The separation of ownership and control in particular provides beneficial opportunities to recruit talented technicians and expert managers who can bring clear, rational vision to the reform and repositioning of the company for exporting. Second, the small size of most businesses prevents them from reaping economies of scale that could drive down costs and provide critical mass in production. Third, a lack of a culture of innovation among most firms, reflected in limited investment in R&D and international standards such as International Organization for Standardization (ISO) certification (CDB, 2001). This is reinforced by a large productivity gap between branches of multinational corporations operating in the region and domestic SMEs.

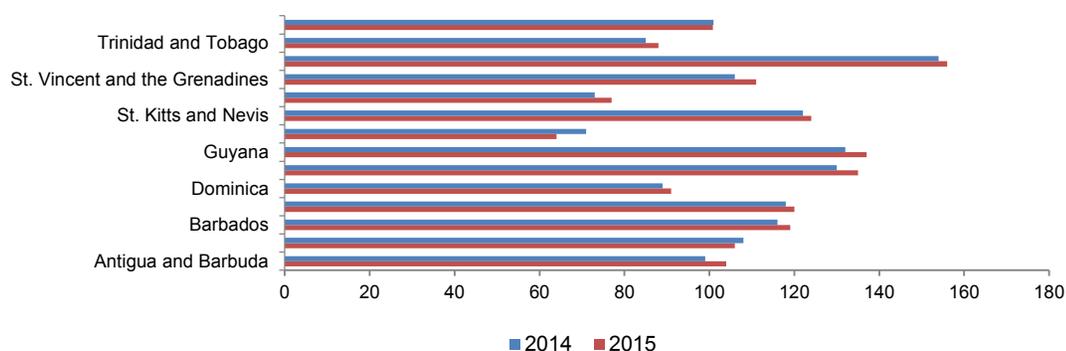
Appropriate policies and measures need to be implemented to overcome the constraints to the creation of dynamically competitive firms. The incentive framework needs to be revamped to prioritise production, especially for export over trading activities. This could be facilitated by preferential tax incentives, modern industrial estates and prioritising exporting firms in allocating scarce foreign exchange. Family owned SMEs should be encouraged to form private limited liability companies and some small firms in similar lines of production should be encouraged to merge to reap greater economies of scale. To facilitate this, agencies would need to disseminate better information on the benefits and risks of incorporation and incentives need to facilitate the strengthening of equity and venture capital markets to finance new start-ups and R&D.

3. Innovation

The promotion of a culture of innovation is probably the most important driver of firm competitiveness in today’s knowledge economy. As Reilly (2010) has noted the mandate for firms in the fast-paced environment of today is ‘innovate or die’. The Caribbean faces a number of constraints that limit innovation among its firms. First, an oligopolistic market structure with a few firms dominating activity in a number of sectors limits competition; which is a key driver of innovation and productivity growth (The Economist Intelligence Unit, 2015). Also, exporting firms tend to have higher levels of innovation than those that produce for the domestic market. This in part reflects less demanding standards and product quality requirements in some areas of the domestic market. To address these constraints, policy makers need to create further liberalise the market in key sectors to strengthen competition and to provide incentives for entrepreneurship training to promote the development of more businesses.

Furthermore, there is need for reform of the business and institutional environment to enhance the ease of doing business. Attention should also be given to improved funding and the development of networks and clusters that could drive innovation among firms. Governments need to support collaboration between universities and firms and to engage in PPPs to fund innovation centres within the constraint of budgetary resources.

Figure 3
Caribbean ease of doing business rank relative to ROSE,
2014-2015



Source: World Bank World Development indicators

Note: ROSE = Rest of Small Economies

As shown in the figure above, Caribbean countries still have a long way to go in improving their ease of doing business. In fact, the region continues to perform worst than the rest of the small economies (ROSE) that face similar size and resource endowment challenges. Therefore, governments need to identify the most serious obstacles to private sector development and eliminate them. Important among these challenges as indicated by the Economist (2005) are: the high cost energy and unreliability of electricity supplies with average retail prices of 33 US cents /KWh compared with 12 US cents/KWh for the United States. Also, limited access to and high cost of finance, especially bank loans, weak transport and logistics systems with over 73 per cent of firms surveyed in Belize, Barbados, Jamaica and Trinidad and Tobago indicating that transportation problems dampened their operations. Also, as Dohnert (undated) has noted, Caribbean firms are smaller, older and less likely to export than those in the ROSE.

Since the private sector is made up of diverse individuals and corporate structures, there will be need for differentiated approaches to garner their support and ensure their engagement in the development thrust through market-based solutions. This involves the establishment of the regulatory environment in which large-scale domestic and foreign capital are afforded transparent procedures for registering and running of enterprises, including access to fiscal incentives, application of taxes and duties, and the operation of labour laws.

Government support should help to crowd in non traditional private sector actors. There is need to unleash potential that resides beyond the traditional private sector in most countries. This requires capacity-building and the provision of business development services, and the strengthening of local micro, small and medium-sized enterprises. There is need for a focus on the financial inclusion of women, youth, socially marginalised groups and rural populations. Improvements in access to venture capital, loans, equity finance, guarantees and long-term capital for micro, small and medium-sized enterprises are critical if the private sector is to become the driver of growth and employment. Ruprah et al (2014) reports that according to the World Bank's Enterprise Surveys for the period 2007-2010, the sales growth of Caribbean firms has only been 26 per cent, employment growth 37 per cent and productivity (sales to employment) 19 per cent of the average for ROSE firms. In addition, three-quarters of Caribbean firms are small compared with two-thirds of ROSE firms. This presents a constraint to them benefitting from scale and productivity gains, which are often related to size.

The building of capacity of agri-businesses and small farmers and enhancing their access to finance, market information and technologies are elements in the strategy which Governments will need to address in financing of risk management instruments such as price, weather and disaster insurance for crops in the resuscitation of agriculture with the farming community, including PPPs.

The promotion of non-traditional enterprises in the services and goods sectors has to take account of the wide range of activities in which new entrepreneurs can engage in creating new niche market products and services. These include opportunities in the creative sector, ICT-based services, eco-tourism services and specialty goods and services based on indigenous content. The development of innovative financial instruments such as loan guarantees to boost SME lending by commercial banks and credit unions, and risk capital for financing SME projects is vital to the development process. Consideration also has to be given to the blended finance, which mixes private financing with public capital and support to fund projects. However, proper oversight is required to ensure that the government is not left with most of the cost if the project fails.

The international community has also committed to fostering enterprise finance and development in developing countries. The Addis Action Agenda recognizes that SMEs, especially those that are owned by women, tend to have difficulty obtaining financing. It proposes a relaxation of financial regulations in this case to allow the use of collateral substitutes, create appropriate exceptions to capital requirements and to allow microfinance institutions to generate savings by receiving deposits. It further commits to strengthen the capacity of financial institutions to undertake cost effective credit evaluation through establishing credit bureaux, where they are lacking (para 43).

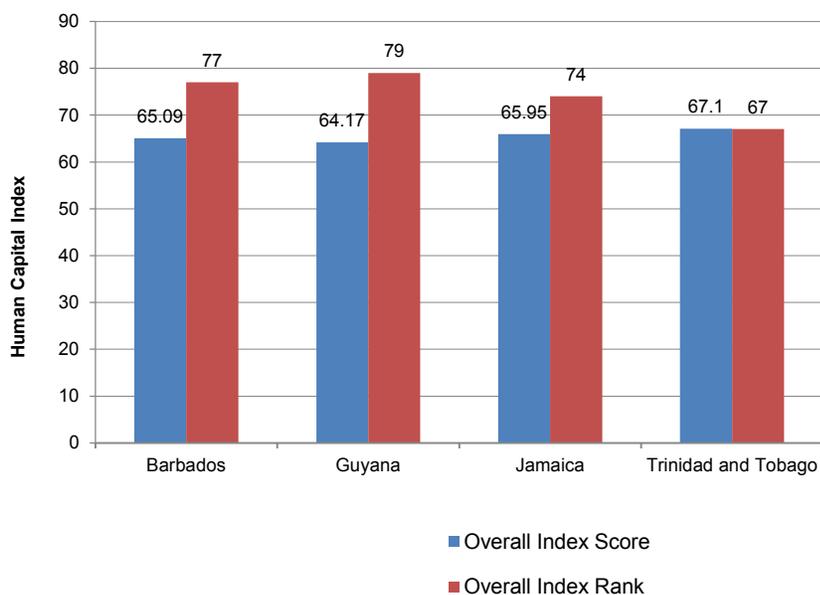
4. Human capital upgrade

Competitiveness⁸ and productivity growth depend vitally on the quality of education and training of the labour force. While the countries of the region have invested heavily in primary and secondary education and have all attained universal enrolment in the secondary level education, there is still a substantial section of the labour force who have no educational qualifications and are ill-equipped for participation in sectors where the application of technology and the use of high level knowledge are important in the production system. Indeed a high percentage of the work-force between the ages of 30 and 55 is in such a situation. Moreover, even where persons have attained university level training, they often lack the skills that should correspond to their level of training, especially in the public sector. This suggests that more attention needs to be paid to critical and creative thinking in learning and providing practical opportunities for students to apply what is being learned through apprenticeships in firms and public sector institutions.

The World Economic Forum human capital index examines the levels of education, skills and employment of people in different age groups against a benchmark to assess progress in human capital development. The indicators showed that Caribbean countries fell below the median rank for 124 countries, suggesting an unsatisfactory performance in building up human capital to compete in the region. Trinidad and Tobago was the highest ranked Caribbean country at 67 with a score of 67.1 followed by Jamaica at 74, Barbados at 77 and Guyana at 79 (see figure 4 below). The gap between the Caribbean and other more advanced small economies is illustrated by the much better indices for Singapore at 24, Malta 33 and Costa Rica 53.

⁸ Competitiveness refers to the ability and performance of a firm, sub-sector or country to sell and supply goods and services in a given market, in relation to the ability and performance of other firms, sub-sectors or countries in the same market.

Figure 4
Human capital indices and ranks for selected Caribbean countries,
2015



Source: World Economic Forum (WEF) Human Capital Report 2015, WEF.

To develop knowledge workers for the 21st century, the Caribbean needs to give priority to increasing the number of students undertaking science, technology, engineering and mathematics (STEM) programmes at universities and technical institutes. This can be achieved by promoting STEM skills in the community by providing high quality work placements, internships, and financial incentives for university recruits and engaging with schools to motivate students to take STEM subjects. This could go a long way in matching training with the need for innovation and technology driven production systems. Moreover, these broad skills would provide the flexibility that is required for workers to adapt to changes in sectors and activities in a knowledge-driven economy. There is also the need to reduce youth unemployment with entry-level and second chance programmes that improve their capacity to find meaningful employment. Priority should also be given to institutionalising of a system of continuous learning⁹ to encourage workers to upgrade their skills with support from Governments and the private sector.

Priority should also be given to indigenous technology and biodiversity. These could be promoted by better intellectual property protection to enable developers to appropriate the rents from their investments. It is also important to strengthen linkages with universities and technical institutes to develop practical networks to boost invention and innovation. In addition a regional system of innovation that creates a network of interactions among firms, research institutions, workers and policy makers to actively promote innovation could help to boost innovation in the region.

Human capital development can also be supported by encouraging members of the diaspora to return to the Caribbean to share their skills and technical capabilities. This can be complemented by online training and mentorship programmes to guide and encourage youths to set up their own businesses.

Governments need to focus on the ease of doing business to create an environment to help nationals living abroad, who have a business interest, to return home. Many of these persons may bring

⁹ As Alvin Tofler noted in his book *Future Shock* (1970), the illiterate of the 21st century will not be those who cannot read and write, but those who cannot learn, unlearn and relearn.

to the country specialised skills and experience to benefit the local economy. Improving administrative systems for reintegrating them in the society and helping them to quickly set up businesses can improve their contribution to the society. Free movement under the CARICOM Single Market and Economy (CSME) should be fully implemented to enhance the human capital base, especially of countries with deficits in certain skills and expertise.

Critical to human capital upgrading is the leveraging of information and communications technologies to facilitate those in school and those who can study from their homes. ICT should be used to deliver creative training programmes both for youths and adults in their communities to enable them to keep up to date with new developments in their fields.¹⁰ This opens up wide possibilities for delivering the content using graphics, animations and multimedia tools to stimulate and hold the attention of learners. In this regard, the region needs to develop a more active ICT policy to reduce the ‘digital divide’ both within and among countries in the region. Governments must also encourage local content provision to build local programming for local and international consumption through government media platforms. The international outreach programme of Radio Havana in Cuba is a good example of this.

5. Mobilising and channelling finance to productive investment

An IMF (2013) study¹¹ revealed that the financial sector in each of the individual Caribbean islands is heavily dominated by banks, which are mainly foreign owned. Partly due to prudential regulations and risk aversion, the banking system tends to be very conservative in its lending policies. This leads to limited, high cost and short-term credit for important productive sector activities. Moreover, the bulk of bank credit tends to be allocated to consumption, rather than productive activities. Indeed, a Compete Caribbean’s 2014 study of regional firms highlighted that 30 per cent of firms surveyed noted that access to finance was a moderate obstacle to doing business, while it was a major or severe obstacle for 26 per cent of firms.

Nevertheless, the allocation of credit to enterprises, especially for greenfield investment has its own risks. Indeed, banks complain that there is often a shortage of bankable projects that are likely to succeed with a reasonable level of certainty. This indicates the need for credit bureaus across the region to enable banks to assess credit risks by providing useful information on the risk profile of private investors.¹² However, banks themselves have access to a significant amount of information, which they can use. In addition, banks need to explore innovative forms of loan guarantee such as the use of mobile and intangible assets and the future earnings of the business as collateral.

There are some agencies such as the Junior stock market in Jamaica and the Barbados Youth Entrepreneurship Scheme that promote finance and business development. However, governments need to put in place institutional arrangements where they do not exist to facilitate the strengthening of stock markets and to incentivise the development of venture capital and angel investors which would be better equipped to provide the more risky term financing that is needed for business start-ups and expansion. This is vital to enable new entrepreneurs and firms secure adequate financing to invest in new products and services, especially for export.

There is also need for reform of the systems of allocating scarce foreign exchange in the region. Currently, priority in access to foreign exchange in most countries seems to go to firms importing goods and services from foreign markets. There is a clear need to give preference in foreign exchange allocation to firms that are or have the potential to become net exporters of goods and services. This change in allocation would then give priority to the earners of foreign exchange and thus enable them to continue earning this scarce resource. Governments should also facilitate business to business contacts, especially for SME that are exporters.

¹⁰ ICT companies could be encouraged to invest in such a programme as part of their corporate social responsibility.

¹¹ Sumiko Ogawa, Joonkyu Park, Diva Singh, and Nita Thacker (2013). Financial Interconnectedness and Financial Sector Reforms in the Caribbean. IMF Working Paper.

¹² Jamaica has set a credit bureau, but is voluntary.

To complement domestic finance, the Caribbean needs to mobilise suitable international finance. An appropriate finance mix would include a balance of equity and debt finance, particularly targeted at the development of growth oriented industries and services. Priority attention should be given to FDI, however, the Caribbean needs to provide more strategic incentives and to negotiate better to attract efficiency-seeking investments. Such investments in areas such as customised niche manufacturing, gourmet agricultural products, nutraceuticals and green industries is critical to enabling the Caribbean to move up the innovation ladder in its specialisation. Fine flavoured chocolate for instance has good prospects in Grenada and Trinidad and Tobago. Indeed, the internationally award winning organic dark chocolate is already being produced in Grenada in an environmentally sustainable manner. Other areas of comparative advantage that could be promoted include the creative industries, including music, the performing arts, fashion and indigenous digital animation.

Other forms of finance also need to be fully leveraged. The regional diaspora in the North Atlantic remains a largely untapped reservoir of finance. The diaspora is already an important source of remittances to the subregion, with flows averaging in excess of 10 per cent of GDP in Guyana, Jamaica and Haiti (Werner, 2016). A Caribbean diaspora bond could be explored as a mechanism for encouraging investment by the diaspora in the subregion. A reputable financial institution such as the CDB could issue the bond on behalf of member governments. It might be useful for Caribbean governments to test the market to gauge sentiments of the diaspora towards such an initiative.

Increased focus should also be placed on strengthening the soundness and integrity of the financial architecture. Derisking and the loss of correspondent banking by a number of Caribbean banks is a major concern. According to the IMF, as of May 2016, some 16 banks across five Caribbean countries have lost some or their entire correspondent banking relationships (CBRs.)

The loss of CBRs has a number of severe implications for finance, trade and growth in the Caribbean. Firstly, it is expected to affect international financial transactions, including settlements, credit, cash and wire transfers, which are crucial for the transfer of remittances to the region. The IMF estimates that more than 90 per cent of remittances are transferred through money transfer services, which would be badly affected by derisking (Erbenova et al, 2016). Moreover, a slowdown in the flow of remittances could severely affect consumption smoothing for households in a number of Caribbean countries, leading adverse effects on their general welfare.

Caribbean governments and the Caribbean Association of Bankers have come up with measures to mitigate the impact of the fall-out. Important among these are the potential establishment of a clearing institution in the United States, alternative methods of payment, the use of alternative correspondent banking relationships in the United Kingdom. Nevertheless, improved compliance with international risk-based prudential guidelines is critical to avoiding further damage.

6. Infrastructure

There is a range of physical and institutional infrastructure that has to be financed by the individual governments. However, the magnitude of the infrastructural needs require the governments of the region to coordinate their activity where the needs intersect and regional platforms are necessary, for example in ICT. Firstly, in light of global warming and the increased intensity of storms, hurricanes and other environmental threats, there is need for massive investments in sea defences. Much of the physical infrastructure has to be retrofitted to accommodate to more exacting standards, including public buildings and housing, but also the range of public utilities. The Addis Action Agenda outcome challenged the international community to step up funding from all sources for investment in low-carbon and climate resilient development. It noted that developed countries committed to the goal of mobilising \$100 billion a year by 2020 to address the needs of developing countries.

Secondly, there is also new infrastructure in the form of communications and transport system air and sea transport for the moving of people and cargo, which have to be upgraded and transport costs reduced. For instance, Sanchez and Wilsmeier (2009) has noted that maritime costs to CARICOM countries at an average of 13 per cent of FOB value of the product is almost twice the world average of 6.64 per cent FOB. At the institutional level, there is the facilitative infrastructure in the form of

regulatory systems – customs administration, trade facilitation, and support for export development that need to be addressed, along with the upgrading of public administration with the introduction of performance management systems. For instance, the larger ports in the Caribbean need to move speedily to become Panamax ready in order to be able to take ships that will carry three times the maximum cargo passing through the canal.

7. Upgrading the quality of institutions

Institutional quality is a critical determinant of the efficiency and competitiveness of an economy (Rodrik, 2003). Nevertheless, institutions like physical capital need to be continually upgraded and modernised to best serve their societies. This requires a continuous audit of the performance of existing institutions, a forecasting of where the society is headed and reform of institutions to match demands of the future.

In the Caribbean context, a number of the institutions that were inherited from the colonial past need to be modernised or reformed to serve the increasing demands of a 21st century society. The facilitation of private sector growth requires institutions that can collate and translate to domestic agents, insights gleaned from monitoring developments in major markets. **This could enable domestic firms to use this knowledge to develop new competitive products and services.** However, a number of institutional weaknesses continue to adversely affect growth in the region. A World Bank Survey found that there was a lower level of public trust, more unproductive rent-seeking and a higher cost of doing business in the Caribbean than ROSE countries (Ruprah et al, 2014).

Most countries of the Region need to invest in the reform of their public services to improve efficiency and imbue personnel with a commitment to accountability and transparency. This would require the adoption of output-based budgeting as against the traditional input-based budgeting. New Zealand has pioneered approaches to public sector reform that are illustrative of possibilities in institutional development in the Caribbean which can help to contain costs in the delivery of public services, at the same time as the quality and quantity are enhanced.¹³

¹³ <http://unpan1.un.org/intradoc/groups/public/documents/apcity/unpan046790.pdf>.

III. Regional integration

The CARICOM integration process has made little headway with production integration, as distinct from the integration of markets. Even in the area of market integration, intra-regional trade remains a small fraction of total trade of most countries. CARICOM needs to push to realise full potential of production integration through the creation of value chains, between CARICOM States and Latin American countries.¹⁴

A clear early winner in production integration might be in respect of agriculture. The Government of Trinidad and Tobago has recently actively encouraged investment in the agricultural sector of Guyana as a potential source for primary inputs into agro-processing in Guyana and in Trinidad.¹⁵ Primary produce from Suriname and Guyana can supply plants in other parts of the region, which have the processing capacity.

The region has faced an intractable challenge in fostering intra-regional transportation linkages that might contribute to trade and movement of people across the region. Transport costs among the island communities are much higher than costs between the region and metropolitan economies. This has constrained the flow of goods and people across the region. There is need for a revamped approach to regional air and sea transport, with better incentives for private sector investment and PPPs to absorb some of the upfront costs.

In addition, the telecommunications sector in the region needs to be fully liberalised to further reduce costs and improve quality. This could position the sector as a key facilitator of trade, investment and innovation both as a driver of efficiency in other sectors and as productive sector in its own right. However, robust efforts are needed to reduce the digital divide by increased training in community centres, libraries and other spaces and the active promotion of a high value added telecoms niche for animation, graphics and other services.

¹⁴ Barcena et.al. op.cit. Value chain creation and widening of integration are already evident with firms in Trinidad and Tobago investing in sourcing primary inputs for agro-processing from Central American countries.

¹⁵ <http://www.guyanatimesgy.com/2014/12/02/high-level-tt-team-for-four-day-visit/>

IV. Social development

Economic, social and political development is part of a triad in the 2030 sustainable development agenda; hence sustained equitable growth cannot be achieved without socio-political development in the region.

Major challenges to orderly social development and cohesion in the region are the high levels of poverty, inequality, crime, population ageing and weak systems for assisting persons with disabilities. Studies of living conditions and of poverty in the region point to continuing poverty levels in excess of 25 percent, even though the incidence of indigence seems to have fallen, and is now negligible in most countries. The social protection machinery has been successful in eliminating the worst form of poverty – food poverty. However, expenditure geared to poverty reduction might be wasteful because of poor targeting and insufficient emphasis on conditional cash transfer mechanism, which provide the opportunity for recipients to exit the poverty trap through improved education and health care.

Furthermore, the social development machinery has to be re-designed to assist communities to manage change stemming from trade adjustment and the reorganization of the economy. As some sectors decline in importance, workers and entire communities are affected. A major example of this was the substantial adjustment that was required to transition from agriculture to tourism in some OECS countries with the erosion of preferences for bananas and sugar. The transition for affected workers requires re-training for new jobs and temporary financial assistance in some cases to cushion the adjustment. Without these support services a number of persons might choose to engage in underground activity/informal activities or even a life of crime.

A high level of criminal activity is a major problem in the Caribbean. The region has some of the highest rates of homicides per 100,000 in the world, and this is associated in part with the impact of narco-trafficking, the proliferation of firearms and gang violence. The crime problem needs to be tackled by improved training and equipment for security officers, better outreach programmes to rescue at risk youths and reform of the criminal justice system to speed up trials and eliminate the backlog of cases. Strengthening regional coordination, information sharing and detection are also essential.

Social services are also under stress due to population ageing that presents a heavy burden for pension and social security systems. Better retraining programmes are needed to equip older workers with modern skills to enable them to continue to participate in the labour market as retirement ages are

raised. The region also needs to develop a targeted programme to tackle the high incidence of non-communicable diseases.

The Caribbean needs to develop an inclusive society that promotes inter-group harmony and leverages the full potential of all citizens. Therefore historically marginalized communities such as indigenous communities in Dominica, Belize, St. Vincent and the Grenadines, Guyana and Suriname need to be assisted in entering the economic mainstream of their countries, while respecting their wishes as to how far they want to engage.¹⁶

Another area that is in need of urgent reform is the treatment of persons with disabilities. Most countries in the region are at an early stage of development of institutions and policy to effectively integrate persons with disabilities in all areas of national life. As a result, persons with disabilities confront weak functional autonomy, which is defined as their ability to perform routine daily tasks that contribute to their well-being and integration in society. This stems in part from weak support systems including assistive technology. The region needs to move quickly to make public transportation; education systems and other facilities are user-friendly for the disabled. Initial steps could include the provision of ramps and wheel chairs to improve transportation, the use of specialist teachers and educating family caregivers so that they could provide better care for disabled persons living with them.

¹⁶ <http://www.ohchr.org/Documents/Issues/Minorities/UNDPmarginalisedMinorities.pdf>.

V. Putting the environment at the centre of development

The Caribbean has long recognised the importance of the natural environment as a key pillar in its development strategy. Indeed, the Barbados Programme of Action of 1994 was an early framework for addressing the vulnerabilities of SIDS. Nevertheless, with the impacts of natural disasters, climate change and the potential presented by sustainable use of environmental resources countries are now taking a more integrated approach to the environment in development. The Samoa Pathway and the 2030 Development Agenda and the SDGs highlight the synergistic relationship between the environment and development.

In the Caribbean putting the environment at the centre of development should balance three important issues:

- The efficient and sustainable use of natural resources, including the development of alternatives
- Better use and increased protection of natural species and biodiversity
- Building resilience by mitigating the risk from natural hazards, especially in the context of climate change

With respect to the first of these issues, the Caribbean needs to undertake a wide-ranging audit of its natural resources as a precursor to assessing current and potential future use relative to what is deemed sustainable use. This should entail an analysis of resource use relative to proven stocks or reserves to ensure long-term sustainable exploitation of resources such as fisheries, forests, water and minerals. An important concern as indicated earlier is the need to develop alternative forms of energy to fossil fuels, which are major contributors to climate change.

Better use, management and protection of biodiversity are critical for the region. This stems in part from a lack of knowledge of the future value of some of these species. For instance, one of the leading drugs used to fight cancer came from a Caribbean sponge and a Caribbean soft coral produces a compound with good anti-inflammatory properties. It is highly likely that Caribbean biodiversity holds great future potential for the pharmaceutical industry and should be protected based on the precautionary principle.

The third pillar, the impact of natural disasters is a clear and present threat to the region. The Caribbean is the most disaster-prone region in the world. According to ECLAC assessments, the region was impacted by in excess of 80 natural disasters between 1990 and 2016 with estimated costs of US\$145 billion (constant 2008 prices). Natural disasters in the region have often destroyed significant portions of the capital stock contributing to lower than trend growth rates over the medium-term. Moreover, the fall-out in the social sectors, estimated at around US\$55 billion, or 38 per cent of the total impact between 1990 and 2016 has led to severe welfare hardship for the affected population.

Importantly, disasters have been an important contributor to burgeoning debt, in countries such as the OECS and Jamaica, as governments have had to undertake borrowing to rebuild and improve capital assets such as ports, airports and electricity generating plants. The devastating earthquake in Haiti in early 2010 topped the scale for loss of life and economic and social costs, with an estimated 230,000 lives lost and costs estimated at US\$7.8 billion, exceeding the country's GDP. This level of damage and disruption calls for an integrated strategy to build back capital assets and production systems to build resilience and capacity to withstand disasters.

Global warming and climate change indicates that hydrometeorological disasters are likely to be more intense in the future. Therefore, the region needs to better programme disaster risk management and mitigation as an integral part of its development strategy to reduce the impact of these events that could set back the development process for many years. Regional collaboration in early warning mechanisms, implementation of building codes and provision of catastrophic risk insurance could go a long way in raising the state of readiness in the region.

VI. Conclusion

Having made significant economic and social progress after independence, the Caribbean is now challenged by a rapidly changing global environment. The traditional axis of trade and growth are changing and countries are positioning themselves for intense competition and slower global demand. This means that to secure and advance its development gains, business as usual is not an option for Caribbean. What is required is a radical change in the present growth model that is based on exporting commodities or traditional tourism and offshore financial services to one that is based on new products and services that make intensive use of innovation and skilled labour and meet the specific needs of customers. This is the only means of making the Caribbean exports competitive, thereby ensuring sustained growth in exports and foreign exchange earnings.

Nevertheless, economic transformation would not occur under a purely market-driven approach. The region needs to design its own blend of market-based and government-supported approaches to tackle a number of binding constraints that impede economic restructuring and diversification. Priority areas that need addressing include a major upgrade of the human capital base by improved and more targeted education and training to produce knowledge workers who are continuous learners. A strategic focus should be placed on entrepreneurship training to grow businesses, especially those that adapt modern technology to indigenous products and services to produce unique products and services. All of this should be embedded in a culture of innovation both in firms and government institutions to create new and improved products and processes. Policy makers should prioritise a major overhaul of the business environment to make it easy to start a business, trade and wind-up businesses by removing an array of bureaucratic hurdles to doing business.

However, economic revitalisation though necessary is not sufficient for building a robust and dynamic Caribbean society. Economic adjustment must be underpinned by socio-political reforms. Crucial among these are the creation of improved social protection systems to contain the fall-out from economic adjustment, policies to reduce inequality and poverty and smarter crime fighting strategies to reduce the impact of crime and deviance on Caribbean societies. Both economic and social reforms, however, need to be anchored in a framework that recognises the importance of the environment to development. Improved environmental management, including the protection of rare species and a focus on mitigating harmful effects of environmental damage caused by climate change, including potentially more intense natural hazards is central to sustainable development.

Bibliography

- Brautigam, Deborah and Woolcock, Michael (2001), “*Small states in a global economy: the role of institutions in managing vulnerability and opportunity in small developing countries*”, UN WIDER, Discussion paper No. 2001/37.
- Donhert, Sylvia (undated), “Clearing the hurdles: key issues affecting Caribbean private sector competitiveness”, *Compete Caribbean*.
- Djukanovic, Goran (2016). *Global FRP and extrusion aluminium outlook*, *Aluminium Insider*. <http://aluminiuminsider.com>.
- Erbenova, Michaela, Lin, Yan, Kryriakos-Saad et al. (2016), “*The withdrawal of correspondent banking relationships: a case for policy action*”, IMF Discussion note, SDN/16./06, June 2016.
- Hvidt, Martin (2013). “*Economic diversification in the GCC countries: past record and future trends*”, The London School of Economics and Political Science.
- Imbs, Jean and Wacziarg Romain (2003). “*Stages of diversification*”. Anderson School of Management, University of California, Los Angeles (UCLA).
- Krugman, Paul (2013). “*Secular stagnation, coalmines, bubbles and Larry Summers*”. New York Times, November 16, 2013.
- Longmore, Rohan, Jaupart Pascal et al. (2014). “*Towards economic diversification in Trinidad and Tobago*”, Policy Research Paper No. 6840. World Bank Portals/30/docs/DrivingGreenEconomy.pdf.
- Monga (undated). “Industrial policy: The New Consensus”. Senior Advisor to the Chief Economist and Senior Vice President, The World Bank.
- Reilly, Edwards T. (2010). “*Creating a culture of innovation*”, American Management Association.
- Ruprah, Inder, Melgarejo, Karl and Ricardo Sierra (2014). “Is there a Caribbean growth sclerosis”. Inter-American Development Bank.
- Stiglitz, Joseph, R. (2016). “Industrial policy, Learning and Development”. WIDER Working Paper 2016.
- Summers, Lawrence H. (2016). “The Age of secular stagnation: What it is and what to do about it”, *Foreign Affairs*, Vol 95, No. 2, March/April, 2016.
- Caribbean Development Bank (CDB) (2001). “Private Sector Development Strategy: From transitional adjustment to long-term competitiveness-organising Production for Sustained growth and competitiveness”.
- The Economist Intelligence Unit (2015). “Private Sector Development in the Caribbean: a Regional Overview”.
- ECLAC (Economic Commission for Latin America and the Caribbean) and (AFD) Agence Francaise de Developpment (2012). *Development Paths in the Caribbean*”. UNECLAC.

- UNEP (United Nations Environment Programme) (2010), A Brief for Policy makers on the Green Economy and Millenium Development Goals
http://www.unep.org/greeneconomy/Portals/30/docs/policymakers_brief_GEI&MDG.pdf.
- _____ (2010), “Driving a green economy through Public Finance for the United Nations Summit on the Millenium Development Goals”, September. <http://www.unep.org/greeneconomy>.
- Werner, Mark, D. (2016), *Caribbean Diaspora: How can they finance development in the region*, Inter-American Development Bank, Caribbean dev-trends.
- World Bank(2005), “A Time to Choose: Caribbean Development in the 21st century.
- _____ (2014), “The New Trade Environment and Trade Performance in the Caribbean”. World Bank.

**ECLAC****Studies and Perspectives Series – The Caribbean**

Issues published

A complete list as well as pdf files are available at

www.eclac.org/publicaciones

52. A framework for Caribbean medium term development, LC/L.4291, LC/CAR/L.506, 2016.
51. Preliminary overview of the economies of the Caribbean 2015-2016, LC/L.4290, LC/CAR/L.503, 2016.
50. Economic Survey of the Caribbean 2015 - Balancing economic recovery and high debt in the Caribbean, LC/L.4135, LC/CAR/L.487, 2016.
49. Dissemination of Caribbean census microdata to researchers - Including an experiment in the anonymization of microdata for Grenada and Trinidad and Tobago, LC/L.4134, LC/CAR/L.486, 2016.
48. An assessment of big data for official statistics in the Caribbean – Challenges and opportunities, LC/L.4133, LC/CAR/L.485, 2016.
47. Regional approaches to e-government initiatives in the Caribbean, LC/L.4132, LC/CAR/L.483, 2016.
46. Opportunities and risks associated with the advent of digital currency in the Caribbean, LC/L.4131, LC/CAR/L.482, 2016.
45. Ageing in the Caribbean and the human rights of older persons – Twin imperative for actions, LC/L.4130, LC/CAR/L.481, 2016.
44. Towards a demand model for maritime passenger transportation in the Caribbean – A regional study of passenger ferry services, LC/L.4122, LC/CAR/L.477, 2015.
43. The Caribbean and the post-2015 development agenda, LC/L.4098, LC/CAR/L.472, 2015.
42. Caribbean synthesis review and appraisal report on the implementation of the Beijing Declaration and Platform for Action, LC/L.4087, LC/CAR/L.470, 2015.
41. An assessment of performance of CARICOM extraregional trade agreements – An initial scoping exercise, LC/L.3944/Rev.1, LC/CAR/L.455/Rev.1, 2015.
40. Caribbean Development Report – Exploring strategies for sustainable growth and development in Caribbean small island States, LC/L.3918, LC/CAR/L.451, 2014.
39. Economic Survey of the Caribbean 2014 – Reduced downside risks and better prospects for recovery, LC/L.3917, LC/CAR/L.450, 2014.
38. An assessment of mechanism to improve energy efficiency in the transport sector in Grenada, Saint Lucia, and Saint Vincent and the Grenadines, LC/L.3915, LC/CAR/L.449, 2014.

STUDIES

AND

PE

SPEC

TIVES

52

STUDIES

AND

PE

SPEC

TIVES

STUDIES AND PERSPECTIVES



ECONOMIC COMMISSION FOR LATIN AMERICA AND THE CARIBBEAN
COMISIÓN ECONÓMICA PARA AMÉRICA LATINA Y EL CARIBE
www.eclac.org