CARIBBEAN
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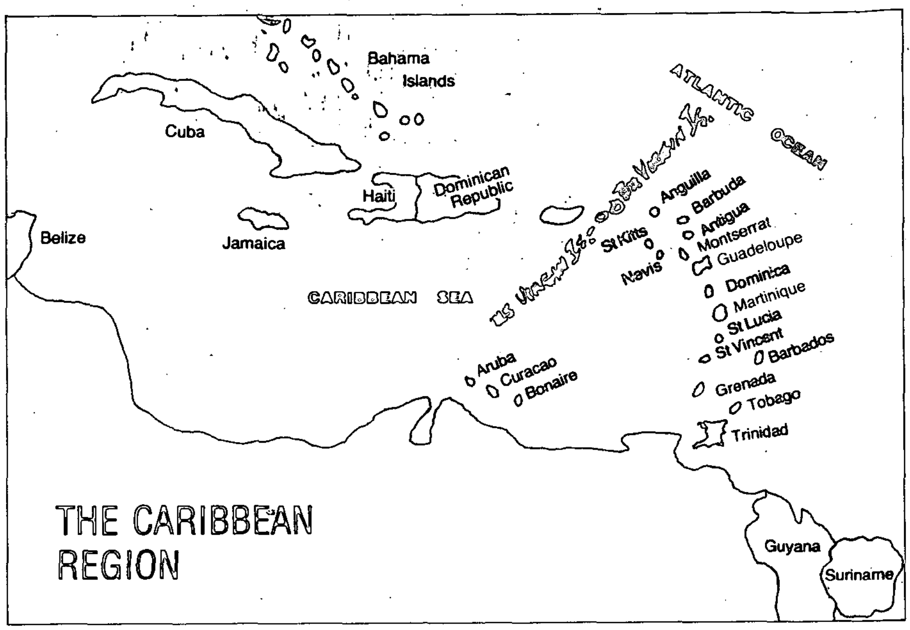

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CARIBBEAN DEVELOPMENT AND CO-OPERATION COMMITTEE

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EXTRAORDINARY CONFERENCE ON ECONOMIC DEVELOPMENT - SOME COMMENTS REGARDING THE CARIBBEAN

UNITED NATIONS
ECONOMIC COMMISSION FOR LATIN AMERICA AND THE CARIBBEAN
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PREFACE

The comments which follow attempt to provide a Caribbean orientation for those fundamental questions of development policy being re-evaluated by ECLAC prior to the Mexico meeting on economic development policy.

The meeting has its genesis in a call made by the President of Mexico for ECLAC, which has "... a historic legacy and great tradition of clear and independent thinking..." to re-evaluate its developmental policies and to provide " a current conceptual framework relevant to the problems of the region".

Given the heterogeneity of the region, any conceptual framework will also need to take into account the special developmental constraints faced by the smallest ECLAC members, and particularly the island countries of the CDCC.<1> This paper is an attempt to outline some of these, and to provide a brief sketch of some of those bases of policy which have been recently enunciated by various Caribbean governments and institutions, and which might be regarded as coalescing toward a Caribbean style of development.

By way of providing substance to some of the concepts, a number of developments highlighting attempts to adjust to the current economic difficulties are also adumbrated.

INTRODUCTION

The call for a re-evaluation of the developmental policy framework is justified by the economic shocks suffered by Latin American and Caribbean countries since the early nineteen seventies and the extreme difficulties which they are all experiencing in adjusting to those shocks.

Of concern also is the suspicion that the adjustment process, which is having to take place in an environment of stagnating world trade and rapidly changing patterns of production and of demand, is proceeding at a pace which is slower than that of many of its international competitors, so that its relative standing as a region is being eroded. Moreover there is concern that some of the policies which have been pursued in the past have rendered the economies less resilient in the face of global changes, than might have been anticipated.

For the Caribbean countries these concerns are particularly acute, since export performance determines the level of economic growth.

During the nineteen sixties, some Caribbean countries recorded relatively high levels of Foreign Direct Investment, one consequence of which was a relative abundance of foreign exchange. By the late sixties and early seventies a policy agenda had been developed, essentially to solve yesterdays problems. It placed a high priority on indigenous ownership and control, and a process of industrialization based on tariff walls producing for the local, and later for some countries, the CARIFTA and subsequently the CARICOM markets. It is noteworthy that the primary goal was neither the earning nor the conservation of foreign exchange, but rather the creation of jobs, and many industries evolved which were net users of foreign exchange, and incapable of competing in unprotected markets. The consequences of this policy were disguised as long as there was sufficient foreign exchange.

Moreover the process of localizing the economies had the effect of using investible resources and in some cases foreign exchange to acquire existing assets which were in the process of being made obsolescent by international developments, rather than creating new ones.

By that time the policies in place faced a dramatically different reality. The decade of the seventies witnessed a drastic reduction of foreign direct investment, rapid rates of inflation, and rapid increases in the prices of some essential imports for Caribbean countries, such as food and energy. By the mid seventies, there was a weakening of demand for many of the traditional exports, so that the abundance of foreign exchange which had been taken for granted, and upon which its development path had been predicated, was no longer assured.

Production for the domestic and regional markets was therfore constrained and regional trade began to decline partly because of protectionism, designed to conserve the declining foreign reserves.

In an effort to sustain economic activity in conditions which were percieved at the time to be short term and cyclical, public policy was oriented to deficit financing which had severe implications for the external debt in open Caribbean countries; and for the debt servicing capacity, once international interest rates recovered from the negative real rates which prevailed from the mid-seventies, until the end of the decade.

For the first half of the decade of the eighties, international trade has stagnated, while a series of structural changes have been initiated in industries of importance to Caribbean countries, such as the bauxite/alumina sector, and offshore oil refining, while the performance of agricultural exports, is being affected by shifts in consumption patterns and declining productivity. In conjunction with all these factors the costs of servicing the external debt has increased thus placing increasing demands on the already scarce foreign exchange.

This thumbnail sketch of the main economic developments over the past twenty five years, while well known, has been repeated as a preface to the discussion on development policies for the future, since it includes most of those factors which have prompted the agonising search for new policy orientations. That some new initiatives and responses are being developed is also a fact, and some of these efforts are described later in this paper.

Objectives of Development

The objective of development, taken in the context of a democratic society, is essentially an attempt to broaden the range of choice available to the members of that society.<2> It is an attempt to maximize the range of options available to the society for the present, as well as the future.

Implicit in this quest is the need for the society to achieve economic growth that is sufficiently stable and self sustaining so that the efforts of the past may be cumulative. In the short run it needs to develop the capacity to adjust rapidly to economic shocks originating locally, from situations such as natural disasters, or externally, from factors such as sudden fluctuations in commodity earnings. In the longer term it implies the capacity to respond to changes in technology, comparative advantage, or changing patterns of demand.

It also follows that development should be sufficiently broad based and diversified to maximize the use of all the available resources, particularly human resources. The objective will be reduced vulnerability resulting from a more diversified productive structure, but also increased participation in the productive process, leading to a greater level of democratization, equity, and welfare.

To achieve these objectives economic development policy meeds to be based on some measure of national concensus. The pace of development will be constrained by social attitudes to development as well as the capacities of its menbers to adjust. These constraints will prevail irrespective of whether the iniative is taken primarily by the state or left to individuals. In the former case the lack of consensus will result in failure to meet targets and plans and can lead to the use of increased exhortation coercion and polarization. The latter case has the merit of allowing individuals some choice in the pace that they set for themselves in social change, though it also implies that the costs and benefits attendant upon social change will be unevenly distributed, a fact which in the longer run might serve to increase the national consensus, through emulation, or to decrease it, due to increasing social differentiation and conflict.

Social concensus permits a consistency in policy which is necessary for long range decisions, and minimizes the uncertainties and wasted energy deriving from changing rules of the game. This implies consistency regarding fundamentals such as the place of the individual actor in the development process, the rate of investment and the treatment of investors, as well as more detailed aspects such as the rate of inflation, convertibility of currency, and so on.

From the foregoing it may be inferred that economic development differs from economic growth in a qualitative sense. In the long run growth is a necessary though not a sufficient condition for development. At the same time some optimal balance will need to be struck where tradeoffs<3> are needed, tradeoffs which will differ between different societies and even within the same society over time. But it may be, that policy makers in the region have assumed the existence of greater leeway in making tradeoffs, than can be justified with hindsight.

Caribbean governments have for the most part pursued many of the objectives of economic development directly, yet there is a pervasive feeling that the effort has not been adequately rewarded and that economic growth has also suffered, even when due allowance was made for the inauspicious international climate.

The lesson which may be learned from recent experience is that there are limits beyond which these goals may not be pursued directly, and in the absence of a respect for economic efficiency, without becoming counter-productive. Thus the objective of greater autonomy in national decision making, if pursued as an end in itself, might result in less autonomy, if political actions erode economic viability. The pursuit of greater security, if resulting in risk aversion, and a resistance to change, might result in greater vulnerability for declining or outmoded industries. The quest for greater employment if pursued through non productive activities will result in greater dislocation when they are no longer sustainable, and the goal of greater equity will be elusive if the disadvantaged groups are not equipped to contribute in a productive manner to the economy, over the longer term.

Role of the state in Economic Development

It has been postulated that as the process of development is not spontaneous the impetus to it needs to be provided by the state. Whatever the merits of the assertion, since it begs a number of questions, it would be difficult to envisage a stable developmental process without a series of supporting measures which are considered to be the legitimate domain of the state. In this regard there is little debate about the legitimate role of the state in providing a local and foreign environment which will permit its citizens to develop. A few comments will be made in a separate section regarding some the social and psychological preconditions for development so that the discussion which follows defers these aspects for later treatment.

Domestically, this implies as a minimum a secure social environment with clearly defined rules, a set of institutions through which the citizens may conduct their business, the provision of high standards of health, an education system that is supportive of the objectives of development, effective systems of communication, and the effective management of the monetary and fiscal system.

In the international arena, it is recognized that the state has the legitimate responsibility to conduct its external policy so as to preserve the integrity and security of the country, and to enhance the climate in which external commercial activities will be efficiently conducted.

While the foregoing list of functions might be regarded as unduly restricted by some, it is one which allows a great deal of leeway for the determination of policy. It moreover encompasses a series of tasks which are already beyond the resources of most developing countries. The valid concerns of the late eighties for Caribbean countries would seem to be, the need to devise ways to maximize state services given the contracting revenues available to it and bearing in mind the opportunity cost of those resources, to delimit the role of the state to the effective provision of those essentials, and to ensure that state policies are carefully selected so as to be consistent with goals.

For most of the newly emerging states of the Caribbean, it was taken as an axiom that the responsibility for redressing the legacies of the past lay with the recently elected democratic governments. These legacies were perceived to be deep-rooted in the political, social, cultural, and economic spheres.

In so far as economic development was concerned it was assumed that a government, having good intentions, and with the assistance of central planning, would rapidly eliminate poverty and unemployment, and achieve modernization. It was also assumed that any reluctance or inability on the part of the private sector to increase the pace of investment could be compensated for by government.

It is also noteworthy that political parties in most Caribbean countries were offshoots of, or had their genesis in, the labour unions, and that the struggle for independence against colonialism, was integrally related in the eyes of the new trades union/political elites with the battle for a higher money wage extracted from the private sector. A political and an economic struggle became indivisible.

The stage was therefore set, for a period of suspicion at best, and more probably for an environment of hostility to prevail, between the state and the private sector. The popular perception of the private sector was one of exploiter, the achievement of increased money wage being the indicator of development, with state economic action being expected to be welfare oriented.

For its part the private sector became marginalized, and concerned that its investments would no longer be secure and remunerative. The investment climate had been eroded, and despite some overtures by the state the perception of insecurity prevailing in the private sector has not been dissipated. The panoply of controls which were created in response to diminishing foreign reserves has increased the risk, and the costs, of doing business and made it increasingly difficult to reorient private sector attitudes. This in turn has meant that the private investors take a short view of development, to demand rapid rates of return and at the earliest opportunity move their assets to less risky locations.

The accession to independence required that the public sector expand, and would of itself, even in the best case, have placed increased strain on revenues. Yet in the light of the recent past one should not be surprised that expansion became an end in itself. There was also the assumption that improved infrastructure was necessarily productive investment, and that the acquision and management of the public utilities was essential to symbolize independence and to provide benefits to the public. Similiarly, the argument was used to justify the acquisition of directly productive activities in sugar and the minerals sector, and in some cases the services sectors, such as the banks and some hotels. It is therefore easy to imagine the impact that these policies had initially upon the budget, subsequently upon the balance of payments, and ultimately upon the external debt.

In the light of the material and human constraints now being faced by the public sector, an automatic expansion of the role of the state can no longer be assumed. In fact the converse is true, since most Caribbean governments are currently accruing deficits on the current account of their budgets, and in the scenario of stagnating economies are facing constraints on their capacity to increase revenues.

At the same time, while it is generally recognized that there are many areas where the state needs to ensure that services are provided to the public, it is no longer universally assumed that the state need itself do so. It has the option to sub contract these tasks to private operators, often at a saving while having a greater supervisory role in ensuring the quality of the product or service. It is also generally accepted that there is a greater likelihood that inefficiency in the public sector will go unpenalized, and at public expense, for longer than in the private sector.

A growing body of literature and of practice is being accumulated internationally and in the region, on issues such as, the economics of privatization; the checks and balances which may be used to overcome those abuses which may inhere in private sector monopolies; the distinction which can be made between the funding and the provision of a service; and the benefits which may accrue to strapped budgets from divestment. These new attitudes are encouraging a fresh and undoctrainaire look at the ways open to the state to achieve commonly accepted objectives without wasting its resources, the scarcest of which is managerial, in the actual task of implementation.

A reappraisal is also being made of the scope and type of planning which might be most effective in developing economies, especially those that are open, and therefore require speed and adaptability in their response to rapidly shifting global trends. Because of the complexity of issues and the levels of uncertainty inherent in global economic activity, the state needs to be more selective in its focus on key policy issues; to plan its strategies; to ensure that its incentive policies are consistent with goals; to secure a concensus between the various economic actors, both within the state apparatus, and in its dealings with the private sector; and to manage the public investment programmes, effectively.

Since the growth and even the survival of the economy is dependent upon trade, it is essential that the economy remains internationally competitive. The state has the responsibility to ensure that the necessary discipline is exercised by all the economic actors, including itself, so that competiveness is adjusted and sustained over time. This will in turn enhance the flexibility and adaptability of the economy to unforseen external events, and ultimately limit the extent to which external actors can intrude to influence state policy.

Role of International Trade in Economic Development.

The policy debate relating to the efficacy of the "open" or "closed" model of economic development, has continued in the Caribbean as it has elsewhere. Whatever the intrinsic merits of the case, due to the differences in size of the various countries, it is more difficult to sustain the argument for closure in the Caribbean than might be the case elsewhere.

Small size implies a limited domestic market, and a relatively narrow natural resource base. In the Caribbean, domestic markets are so small that in most cases they are unable to absorb the output of modern enterprises, given the prevailing technologies. Moreover, resource endowments are so narrow that at least in the initial stages there needs to be an emphasis on relatively few productive activities. The situation is complicated by the fact that as most of the islands share similiar assets and weaknesses there is a tendency for them to posess a comparative advantage in similar activities. On the supply side therefore the islands need to export a large part of their output, and they consequently export a similiar range of goods and services.

On the demand side, the corollary is that while Caribbean countries export a narrow range of products they need to import the bulk of what they consume. Since this openness is a historical fact, there is a tendency by those advocating closure, to assume that it is determined by the political and constitutional arrangements of the past, and not by geography, and that it is therefore amenable to correction by political actions.

While it is clear that effective development will diversify the range of outputs, it is also clear that a part or all of that output will also need to be exported, so that in sum, a large proportion of output will need to be competitive on the international markets. Import substitution is therfore either a very limited, or a very expensive option the inefficiencies of which cannot for long be disguised. The capacity of the state to recognize the constraints placed upon small islands, and to reorient its policies so as to permit the development of an efficient economy is therefore crucial.

Deriving from the practical realities which they face Caribbean states have assiduously sought to provide as effective an international framework as possible within which to conduct its international trade. A number of special trade arrangements have accordingly been agreed with the main trading partners in the United States, the European Economic Community, and Canada.

The Caribbean Basin Economic Recovery Act (CBERA) which governs the terms under which most<4> Caribbean countries trade with the United States came into effect in August 1983. It provides duty free access for goods produced by beneficiary countries for a twelve year period with the exception of some goods deemed to be specially sensitive such as, textile and apparel articles, leather goods not eligible under the GSP, canned tuna, petroleum and petroleum products, and watches and watch parts with materials from a non-MFN country.

While few in number, the exclusions were nevertheless important in consequence, and nullified much of the additional benefit which might have been derived over the GSP, since eighty-seven percent of Caribbean exports had entered the US market free of duty under the GSP. Moreover, the origin criteria were substantially the same as under the GSP, with additionality limited to the option of cumulating the inputs of other CBERA participants. The exclusions therefore placed limitations on participants in those areas in which they were likely to have the greatest potential for trade expansion. Concessions were therefore, found necessary in February 1986, to increase the quotas under Article 807 for garments assembled from cloth cut or woven in the US, when it became clear that the hoped for expansion in trade was not being realized.

Since the CBERA came into effect some products have shown an increased market penetration, such as furniture, electronics, seafood, winter fruits and vegetables, and garments. Some of the traditional exports have not fared as well, particularly sugar, since the existing quota arrangements had not been rescinded by the new trade provisions, and indeed quotas were in fact reduced. As a consequence, trade as a whole has not grown with the US under the CBI, although some non-traditional exports have.

Most notable of the non-traditional exports have been electronics and garments, both of which have developed quite rapidly in some Caribbean countries in the enclave type of manufacturing arrangement, sometimes in free trade zones. These activities, which had started to grow in the 1970s are not necessarily linked with the CBERA, and while making a useful contribution to employment, contribute only limited added value, and virtually no linkage within the economy itself.

It had been assumed by both parties to the agreement that increased market access would stimulate increased investment, which is the crucial need if the respective economies are to regain any momentum. A technical group to advise Caribbean governments estimated that private sector capital inflows of US$ 1720 million would be needed in the CARICOM group, while US$ 543 million and US$ 242 million would be needed for the Dominican Republic and Haiti, respectively. In order to induce such investment it was proposed that the existing double taxation agreements with the US would need to be modified to include the reinvestment of profits, tax sparing clauses, greater flexibility in depreciating capital and tax deferrals. No modifications to taxation agreements have however, been made under the CBERA, although bilateral investment treaties were briefly mooted. In February 1986 it was agreed that funds accumulating in the Puerto Rican Development Bank under Law 936<5> could be used for investment in the other Caribbean countries and it was hoped that this would speed up the development of twin plants whereby Puerto Rican firms would subcontract some of their inputs to other Caribbean countries.

While it is still too soon to arrive at any meaningful conclusions, it is clear that expectations relating to new investment flows are not being realized, and that economic reactivation and transformation will not be possible without a rapid growth in investment.

The Lome convention which came into force in April 1976, and to which the English speaking caribbean countries and Suriname are signatories, was originally envisaged as an arrangement to protect established marketing arrangements for traditional exports of participating countries, particularly to the UK on its accession to the EEC. It also extended duty free access for most originating products to the EEC. Other elements of interest included mechanisms for stabilizing export earnings, and for fostering industrial, financial and technical cooperation.

Since the first Lome convention was signed it has been revised twice, the Lome III convention being signed in December 1984, and valid for a period of five years. Perhaps the most significant departure from previous conventions is the provision of a section dealing with investments, capital movements, establishment, and services since the arrangements for access have been largely unexploited because of inadequate supply. The new provisions are therefore a recognition of these supply constraints and an attempt to encourage EEC investment into the region.

A new agreement CARIBCAN is also in the process of being implemented between CARICOM member states and Canada. Its provisions are likely to include duty free access for all originating products, so defined to qualify a product having a local value added of 60% of the ex factory price, with inputs from Canada to count as a part of the local value. Exeptions to the duty free provision relate to areas of potential production in the Caribbean, in textiles, clothing, footwear, luggage, handbags, leather garments, lubricating oils, and methanol. There is not likely to be a clause relating to investment promotion, despite a request, although provisions are likely to be made for trade promotion and training.

In summary the special trading arrangements are an attempt in the first instance, to protect traditional exports, secondly to secure market access for as wide a range of potential exports as possible, and latterly to formalize some arrangement which would foster investment and increased output, and also make provisions for marketing assistance. The efforts have been partly sucessful in that traditional exports which had long lost their comparative advantage and which were under pressure from substitutes were given a longer adjustment period in which to switch production to alternative products. The adjustment process has not been smooth, and has in some cases been hindered by arranged prices in excess of those prevailing in the free market since some producers were reluctant to switch from products which had once more become remunerative. Increased access to markets has highlighted the production constraints, and in those products having export potential brought home the reality of having to fight a continuous battle against various non tariff barriers, and the complexity of marketing and distribution faced by very small producers. Investment provisions usually intended in the framework of joint ventures are intended to try to circumvent these constraints.

Industrial Sector.

As a result of its tradition in exporting primary products, and its limited raw materials endowment the industrial sector has been traditionally small and in the last ten years has stagnated. Since the mid -eventies manufacturing has not contributed as much as 20% of GDP in any Caribbean country and in the smaller countries the contribution has averaged less than 10%.

Efforts to expand manufacturing between the nineteen sixties to the mid-seventies in the CARICOM countries, and between 1970-78 in Haiti and the Dominican Republic, were based on import substitution policies within the context of a free trade area in the former countries, or their domestic markets in the latter two. The range of products has been relatively narrow and produced in relatively small scale, concentrating on food processing, garments, footwear, furniture and consumer durables. They have depended on imported inputs and have not been competitive in price, surviving as a result of protection. Consequently, linkages between products have been few and the capacity to penetrate export markets limited.

Since the mid seventies some new products such as steel, extruded plastics, building materials, and chemicals have been added. Yet in the ensuing decade little additional progress has been made in the sector, as the domestic economies have contracted in the face of difficulties in the global economy, and as inputs to the industries such as packaging have increased in price or become unavailable due to foreign exchange shortages. Furthermore CARICOM trade contracted due to the need to conserve foreign exchange and the industries have been rendered increasingly uncompetitive due to declining investment and outmoded plant and equipment. Similiar patterns are evident in Haiti and the Dominican Republic as the domestic markets became saturated.

Concurrently, yet quite seperately from the domestic manufacturing sector, the offshore or export processing zones (EPZ) have developed in an attempt to produce for export markets, and circumvent some of the policy constraints which have sometimes rendered export production less attractive. The most notable export processing zones have developed in Haiti, the Dominican Republic, Barbados and Jamaica.

The export assembly industries account for 30% of total manufacturing in Haiti, growth accelerating from the mid seventies when import substitution industries began to stagnate. The principal product groups are clothing, metal products such as electronics and electrical equipment, and sporting goods. In the Dominican Republic the EPZ's concentrate mainly on textiles and garments(60%) footwear and leather products(12%) cigars and processed tobacco and electronic goods. The zones have recorded an annual growth rate in the value of exports of 20% between 1875-1980, and while the rate of growth since then has fluctuated the net value of exports exceeds the gross value of all other non traditional exports. They provide employment for over 50,000 persons mostly women.

In Barbados industries dealing in textiles and clothing averaged 39% growth between 1968-1978, although firms assembling electronic components grew almost as fast. By 1979 electronics had begun to grow faster than the garments sector and by 1980 it was larger in absolute terms. By 1983 electronics dominated export performance while the textiles and garments sector started to decline.

The Kingston Free Zone was inaugurated in 1976 mainly as a wharehousing and transhipment facility, and by 1980 export sales remained relatively modest. In the next four years export sales grew by about 240% per annum on average. Free zone activity is predominantly in the apparel industry (85%) the remainder in agro processing. The production of Methanol is also a fast growing sector and as such has come up against varying industry lobbies to prevent its inclusion as a CBERA export. The free zone has had a rapid increase in output at a time when output has declined nationally and has provided increased employment at a time when sector employment has stagnated.

For some of the smaller states, such as Antigua and Barbuda, Dominica, Grenada, and St. Vincent and the Grenadines, exports to the US comprise garments assembled from imported parts exclusively . Exports of garments to the US in 1985 for the region as a whole amounted to US$455 million and while data are not available for 1985 in 1984 the exports of assembled products mainly garments and electronics, and the main output of the free zones amounted to about 28% of total exports to the US.<5>

The contribution of the export processing zone to development, while not inconsiderable, is however limited since it is confined mainly to foreign exchange and employment generation. It nevertheless provides a window on the export market giving putative exporters some exposure to the training and quality control standards which will need to be maintained, ensures access to distribution facilities, provides its own mechanisms for preserving and sustaining the market share, and is sensitive to shifting market trends and advancing technologies. The EPZ can also provide the policy maker with a controlled experiment as to the measures needed to induce foreign investment, and a practical test of the relative productivity of a territory. It might also provide a basis on which to build a more mature export industry.

Criticisms of such industries center on the fact that they are volatile and shift rapidly whenever conditions in one locale deteriorate, or when costs become too high; and the fact that there is only limited integration into the domestic economy, so that inter sectoral linkeages are not established and the contribution to Gross Domestic Product is not maximized. But the fact that investment seems only to be induced into areas which are relatively untouched by government policy should cause some reflection about these policies if it is the intention to induce foreign investment for the longer term.

At the same time it is argued by some that domestic structural adjustment programmes may be so stringent that investment is stifled unless it is insulated by measures such as the export processing zones. They are seen therefore as an interim measure until the structural adjustment programme is more mature and a more consistent set of investment policies can be put into place.

Non-Traditional Agricultural Exports

Non traditional agricultural exports constitute a potential source of export growth for Caribbean countries, based primarily on favourable growing conditions, competitive labour rates and close proximity to a large market on the east coast of the US. The Dominican Republic and Jamaica have already made some progress in penetrating this market which falls into three basic categories. The longest established is the production of indigenous foods for the "ethnic market" which comprises mainly Hispanic and Caribbean populations. The second category which encompasses a large and lucrative though seasonal market comprises the cultivation of off season or winter vegetables. The third category is the year-round export of tropical products which have developed an international clientele such as pineapple and coconut and its various by-products, aloe, cocoa butter, cut flowers, house plants and various spices. The possibility of processing and packaging a range of these products either frozen or in cans needs also to included.

Prospects for Caribbean Regional Integration

Common historic and cultural bonds have traditionally existed between the English speaking Caribbean countries deriving from common constitutional practice, close proximity, and some limited institutional cooperation.<7> Such was the percieved strength of these bonds that a Federation was established in 1958 with the expectation that it would provide the most viable basis on which the several small islands could face the future. The federation was, however, not long lived and was dissolved in 1962.

While the political and constitutional implications of Federation were not acceptable to all members, the idea of ecomonic cooperation was more generally accepted so that the Caribbean Free Trade Association (CARIFTA) was formed in 1968. In the same year a *sub-regional integration institution*, the East Caribbean Common Market (ECCM) was also formed. In 1969 the Caribbean Development Bank was formed and commenced operations in 1970.

CARIFTA which had a special focus on free trade, but with the expectation that it was a precursor to deeper forms of integration, worked sufficiently well to encourage its members to move to the next phase in 1973 when the Caribbean Community and Common Market (CARICOM) was formed.

While the central focus of CARICOM remained trade and economic cooperation through the workings of the Common Market, and with the ultimate goal of economic integration remaining, two additional aspects were included, functional cooperation and the coordination of foreign policy.

During the life of CARIFTA intraregional trade among its members increased from 5% to 10% of total trade. CARICOM however came into being at a time when member countries began to face great instability in their external accounts due to rapidly increasing petroleum prices, and subsequently, declining prices for their export commodities. Despite the provisions made for a common external tariff, for the joint development of agriculture, the establishment of regional industrial programming, for the movement of capital and for a harmonised scheme of fiscal incentives, the integration movement faced severe impediments since many of the mechanisms agreed were only partially implemented, and intraregional trade declined, with intra CARICOM imports falling by 25% between 1981 and 1985.

Since CARICOM production was based on the assembly of articles which had traditionally been imported but now using imported inputs they were still significant users, and often net users of foreign exchange. Moreover, excess capacity had developed in the region as a result of unprogrammed industrial development so that as trade contracted with the general decline of the economies the contraction was exacerbated by the implementation ofquotas, and other non-tariff barriers in an attempt to preserve foreign exchange and protect domestic manufactures.

As a consequence of developments over the past decade the regional integration movement faces a number of challenges which it must meet if it is to continue to contribute to the economic development of the region. Briefly stated it must in the short run find the means to resuscitate intraregional trade, but in the longer run it must incorporate policies to stimulate the rapid growth of extraregional trade. It must reactivate those mechanisms agreed in principle, but which have not been implemented in practice, which would allow the stimulation of regional agricultural development, the resuscitation of the textiles industry, and the rationalization of the industrial sector.

In so far as the structure of the movement is concerned, it will need to satisfy the smaller states that measures are being taken to provide a more equitable balance between the costs and benefits of intraregional trade, it will need to devise a more effective decision making machinery, and ultimately, it will need to face the question of widening the membership from the current 5.5 million persons to include other caribbean countries.

CARICOM has started to move to meet the challenge; the integration mechamisms are not seen as an alternative to structural adjustment but as a complement to it, and the Nassau Accord on Structural Adjustment was agreed under the auspicies of the CARICOM heads of government, meeting in 1984. It is recognized that regional trade will need in future to develop with a greater openness to the external market, and the existing scheme for harmonizing fiscal incentives is being revised with a view to remove its anti-export bias, and some of the distortions created in in the regional economies. It has been agreed in principle that the Common External Tariff (CET) should form the principal means of protection, that low rates of duty should be made to apply to capital and intermediate goods, and that national quantitative restrictions should be phased out.

Applications by Suriname, Haiti, and the Dominican Republic for membership, or for observer status in CARICOM, are longstanding. Suriname was granted laision status in 1973, and has participated in a number of meetings of functional committes since then. Application for membership was received from Haiti in 1974, subsequently changed to observer status in 1982, the same year in which a similiar request was received from the Dominican Republic. While the subject of widening has been given serious study by the Secretariat, the internal difficulties experienced in the Common Market have hindered progress in this direction, and promted some governments to advocate solving the existing internal problems before widening the grouping.

Services

Caribbean countries are essentially services oriented. On average services contribute 65% of GDP in CDCC countries, with a higher proportion in the smaller countries and a lower proportion in the larger countries. In the last ten years there has been a tendency for the contribution of services to grow, and reflects the small domestic markets and relative scarcity of indigenous raw materials.

The most obvious service industry in the Caribbean remains Tourism, which is the single most important economic activity and the major source of hard currency for most Caribbean countries, with earnings amounting to nearly US$ 3 billion in 1985. It is also a major source of employment, although like many others the industry has not established strong linkages with other domestic activities such as food production and furnishing so that it does not maximize its contribution to domestic product.

A number of other services activities have grown however, such as offshore banking, which in the Netherlands Antilles provides foreign revenues almost three times greater than foreign earnings from Merchandise trade and provides 53% of the total revenues of the government of Curacao. In the Bahamas, while the impact is not as great, the sector nevertheless makes a valuable contribution to the economy.

Transportation services, such as ship registry and insurance, shiphandling, maintenance and repair, and transhipment facilities, are services from which the Netherlands Antilles also earns substantial returns. More recent developments include computer services, whereby Barbados and Jamaica sell key punch and other data processing services to the United States. Another recently established service industry with growth potential is that of health care, given the demographic profile of the US population, and the emphasis on physical fitness, and it can be seen as an adjunct to the leisure industry which is already well established in the region.

While subject to rapid change and volatility the Caribbean countries will continue to depend upon services as a useful source of employment and foreign earnings. Moreover, as the linkage between goods and services gets closer the Caribbean will need to develop a range of services clustering around its export industries if it is to penetrate external markets in the future.

External Debt and its impact on Development.

For a variety of reasons the international developments of the past decade have not impacted upon all Caribbean countries in the same ways, neither have all countries had at their disposal the same options nor the same policy responses to them. For instance, the OECS countries have at their disposal fewer means to cope with economic downturns, so that adjustment has been almost automatic and sudden, and ameliorated primarily by transfusions of Official Development Assistance (ODA).

In many of the member countries of the OECS, official development assistance (ODA) has been necessary in order to meet the recurrent costs of government as well as to initiate capital development. In the case of the former this was previously financed by UK grants in aid, but recently greater recourse is being made to the local banking system, and to a lesser extent to the Eastern Caribbean Central Bank (ECCB); and the International Monetary Fund (IMF).

Capital programmes have been financed by grants from the traditional Donor countries, mainly through the CGCED, and soft loans from the Caribbean Development Bank (CDB), the European Development Fund (EDF), Trinidad and Tobago and Venezuela.

It should be noted that while efforts need to be made to increase revenue, the base from which this must be extracted is small and fragile, and in any case the performance is not bad, the ratio of government revenue to Gross Development Product (GDP) being an average over 25 percent. The situation in fact provides a good example of the diseconomies of scale faced by small states, as there is a level beyond which the apparatus of government may not be easily compressed. Only through increased production activity can the dilemma be resolved.

At the same time the OECS have been spared the worst effects that a large external debt would have on current and future economic development.

All Caribbean countries have not been so spared, the larger and hitherto more "credit-worthy" of them now having to earmark 36% and 22% of exports of goods and services in the case of Jamaica and the Dominican Republic and for 47% of the hard currency earnings from goods and services of Cuba to service the debt.<8> It is a problem of somewhat lesser magnitude for Guyana and Haiti requiring 9% and 5.5% of export earnings, respectively. For the respective years the overall external debt represented 350%, 281%, and 215% of exports of goods and services for Jamaica, the Dominican Republic and Cuba respectively.

At a time when massive investment is required to transform these economies, and particularly investment which is foreign exchange intensive, such a high percentage of earnings being earmarked for debt service, represents a significant amount of investment denied, and renders the process of transformation more difficult.

Notes

<1> It is not the intention to argue that a seperate economic discipline applies to small states, but rather to suggest that for certain structural reasons they have fewer options in determining a developmental path than might otherwise be the case. The argument will be developed below.

<2> W. Arthur Lewis, The Theory of Economic Growth, Unwin University Books, p. 420.

<3> Tradeoffs are a recurring theme in economics, the most obvious savings/consumption, risk/return, growth/equity, and so on. They form the basis, either implicit or explicit, upon which policy is predicated.

<4> Currently all CDCC member countries are participants in the CBERA with the exception of Cuba, Guyana, and Suriname.

<5> Law 936 provides that profits accumulated by US companies operating in Puerto Rico will be exempt from tax if held locally and reinvested in that country, and an estimated US$8 billion have accumulated over time. While there have been attempts to repeal the law a successful lobby was mounted to retain it on condition that a portion of these funds, an estimated 10% held in the government development bank would be used in the Caribbean in "twin-plant arrangements".

<6> Data derived from US Department of Commerce, and excludes the exports of petroleum from Trinidad and reexports of petroleum from the Bahamas.

<7>For the puroses of this discussion the thirteen states, menbers of the CARICOM are being discussed except in that section relating to the widening of the integration movement.

<8> Figures for Jamaica and Cuba relate to 1984, and for Cuba the percentage relates to hard currency earnings of goods and services and the debt contracted in hard currency.