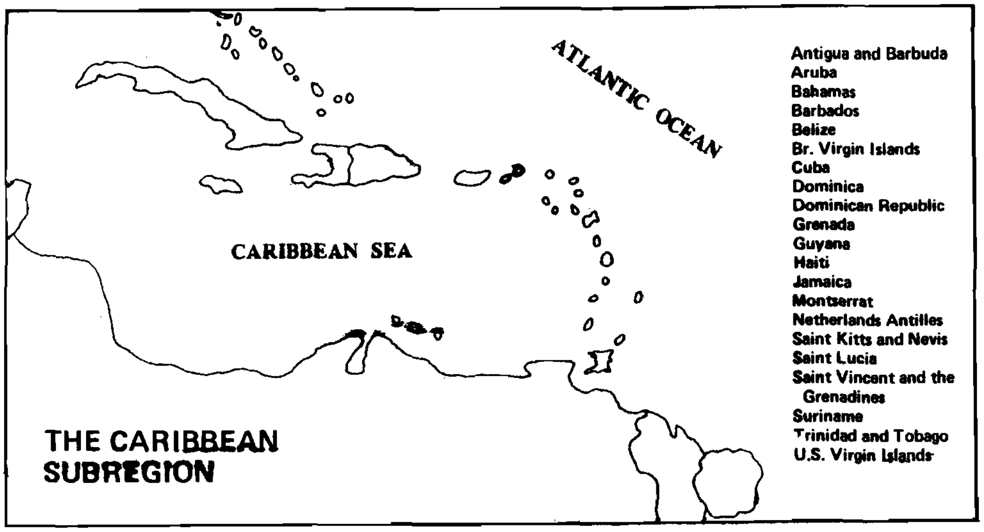
CARIBBEAN DEVELOPMENT AND CO-OPERATION COMMITTEE



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THE EVOLUTION OF SERVICES IN CARIBBEAN ECONOMIES 1980-1989: Some reflections on past performance and prospects for the future, with special emphasis on tourism services

UNITED NATIONS

ECONOMIC COMMISSION FOR LATIN AMERICA AND THE CARIBBEAN
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Methodologies and Definitions

Services are by their nature abstract and intangible. National accounting is by nature imprecise. This imprecision is compounded by any attempts to make cross-country comparisons, since definitions and methodologies can differ significantly from country to country, and nowhere is this more true than in the services sectors. This paper can do no more than try to shed some light on this murky area of Caribbean economies using the available data, inadequate as they are. Various measures are, therefore, used in an attempt to get a better picture of this complex reality.

The treatment of services has been characterized by ambivalence. This springs from the abstract nature of services, the difficulty in getting a clear definition and, therefore, a meaningful measure of the category. It also springs from the perception, shaped within an industrial culture, that a "good" is somehow a more meaningful output than, a service. As one discerns the shift from an industrial culture to an information culture, however, new insights are possible as to the nature and strategic importance of services. Accordingly, a new look is being taken at the services sector, since it is now being recognized that it has a major and strategic role to play in the development process.

While it is usually fairly easy to distinguish between a good, which is tangible and can be precisely described, and a service which is purchased, for example, to improve health or to complete a financial transaction, there are some vague boundaries as to what is good and what is service. Technological developments are making these distinctions even more imprecise. A more abstract definition is therefore needed. The following definition helps to present a new facet in an attempt to clarify the issue. "A service can be defined as an act which is the result of a productive activity and whose effect is to change the status or position of the beneficiary. The service output is not distinguishable from its production process and the result or effect of the service is inseparable from its beneficiary. It cannot form the subject of a new transaction"<1>.

National accounts are used to try to show the relationship of the services sectors to the economy as a whole and how this relationship has changed over the 10 year period 1980-1989. They are also used, where definitions are fairly consistent, to see how the various components of services have changed and how they relate to each other. Some meaningful conclusions can, therefore, be reached with respect to basic services (electricity and water, transport, storage and communications) and government services.

But national accounts present a severe limitation where a greater level of detail is needed to disaggregate the other services. For example, despite its importance to most Caribbean economies, it is impossible to obtain a clear idea of the contribution of tourism to their economies merely from an analysis of G.D.P. data. Not only is tourism not classified in its full impact, such as is done in agriculture or mining, but in some national accounts the category "hotels and restaurants" does not appear as a category at all. In some of the major tourist economies in the region up-to-date national accounts data are not available.

In an attempt to provide a clearer picture of developments, recourse has been necessary, therefore, to a number of other measures such as external earnings, which do not capture local tourism or subsequent leakages, or tourism arrivals figures. In the case of foreign earnings, balance-of-payments figures are often limited to formal flows through the official banking system. Accordingly, Caribbean Tourist Organization (CTO) estimates are deemed to be more indicative of the total foreign earnings from tourism than the balance-of-payments figures.

Finally, for all the reasons of data limitations outlined above, and others such as brevity, it has been necessary to select only those services having the major current or potential impact on economic development for discussion.

<1> Hill, T.P., " The economic significance of the distinction between goods and services" OECD, Reprinted from UNCTAD Trade and Development Report, 1988.

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INTRODUCTION

The purpose of this paper is to review the link between services and development. It will examine the services sectors in the Caribbean during the years 1980-1989 inclusive, to see how they have evolved and to anticipate the role they might play in the development process for the 1990s. The paper also seeks to see how services can be brought more completely within the ambit of development strategies.

Services activities are already of cardinal importance to most Caribbean countries, contributing between 50-80 per-cent of Gross Domestic Product (GDP). Unlike most developing countries which are net importers of services, countries in the region, for the most part depend upon services surpluses, mainly in tourism, to finance large deficits in merchandise trade.

Yet tourism is not the limit of services earnings since offshore financial services contribute significantly to the Bahamas, Cayman Islands and the Netherlands Antilles, which also benefits from ship-repair services. Remittances from nationals working abroad improve local living standards and the balance of payments of many islands, while the assembly of finished products in "offshore" enterprises[1] now provides a growing source of employment for many semi-skilled workers throughout the region. In fact, in most countries services earnings are larger than, or currently growing faster than, merchandise exports.

Some services are also significant contributors to government revenues directly and provide, through their operational expenses, substantial employment opportunities for indigenous professionals such as accountants and legal experts as well as other sectors, such as the retail trades and building and construction. In the Cayman Islands, the offshore insurance industry provided inflows to the economy of over US$15,000 per capita in 1989, while profit taxes paid by the offshore financial sector to the Island Government of Curacao was about US$1,500 per-capita in 1987.

Yet the full impact of the development of services cannot simply be measured in terms of GDP, foreign earnings or government revenues. The export of professional and other services can justify a constellation of high quality amenities which a small society might not otherwise be able to justify. This applies in areas such as health, education and culture services which can improve the

[1] Offshore assembly-type operations are often regarded as manufacturing for national accounting purposes, yet conceptually they could be regarded as services-the export of labour services.

quality of life in the present and materially affect development prospects for the future.

Globally the trade in services is significant not only for its rate of growth but because of its strategic nature in the creation of high technology products. Services constitute over 50 per cent of the value added in the aeronautical, data processing and telecommunications industries. They also have highly complex inter-relationships among themselves creating synergies and innovative new outputs of both goods and services.

For these reasons, as well as the imperceptible way in which it has grown across borders, efforts are now being made to place this trade within some regulatory framework, to reduce the barriers to its flow and to ensure that reliable mechanisms are in place to facilitate the international payments for some of the more intangible services, such as those covered by patents and copyright. These are some of the goals of the Uruguay Round of the General Agreement on Tariffs and Trade (GATT). Accordingly, governments have been forced to evaluate the services sectors anew to see how proposed changes might impact upon them. Even so, basic knowledge about the scope and contribution of the services sectors remains thin.

But services require study and attention irrespective of the immediacy given to the subject by the GATT, since the link between services and development is already strong and likely to strengthen in the future. In the face of declining export performance in agriculture and uncertainties about the protected markets for these commodities, reduced intensity of raw materials in global output and hence stagnant demand for raw materials, especially minerals, and the modest performance and prospects for manufacturing industry, greater attention needs to be paid to the benefits which might be derived from the services sectors. It, therefore, behooves Caribbean governments to treat the development of the sector as a major policy issue for the future.

In previous exercises conducted regionally, within the context of the GATT negotiations, primarily by Economic Commission for Latin America and the Caribbean (ECLAC), Caribbean Community (CARICOM) and the Latin American Economic System (SELA), five service groups have been identified as having potential for development and for international trade. They are tourism, financial services, professional services, telecommunications and culture services. Aside from looking at the evolution of all services as a component of domestic product, the first two services listed will form the core of this paper, to trace their evolution over the decade and to try to provide some indication of the contribution they have made to development in the respective countries. Comments will, nevertheless, also be made in the final section as to how the other services might increase their contribution to national development.

Table I

Average annual growth rates of GDP by sector 1965-1980 and 1980-1986 (%)

	G.D.P.		Agriculture		Industry		Manufacturing		Services	
	1965-80	1980-86	1965-80	1980-86	1965-80	1980-86	1965-80	1980-86	1965-80	1980-86
LOW INCOME COUNTRIES	4.8	7.5	2.7	4.9	7.5	10.6	7.6	11.2	5.1	6.6
MIDDLE INCOME COUNTRIES	6.6	2.3	3.4	2.3	7.0	2.1	8.2	2.5	7.6	2.6
INDUSTRIAL	3.6	2.5	0.9	2.5	3.2	2.5	3.7	...	3.0	2.6
DEVELOPING	6.1	3.8	3.1	3.6	7.2	4.6	8.0	5.9	7.1	3.4
Oil exporters	7.1	1.7	3.4	2.4	6.8	1.6	8.5	2.4	8.7	1.9
Manufactures exporters	6.6	6.2	3.0	5.0	8.9	7.8	9.1	8.6	7.4	5.3
Highly indebted countries	6.6	0.7	3.0	1.8	7.3	-0.2	7.3	0.4	7.2	1.0
Sub-Saharan Africa	5.6	0.0	1.6	1.2	9.4	-1.6	8.5	0.3	7.5	0.1

Source: World Bank

Services have grown faster than GDP for most categories of countries over the last 25 years. This rapid growth helps to explain the increased attention currently being given to the services sector. Although the rate of growth seems to have declined since 1980, services growth is still marginally greater than GDP growth and exceeds all other categories with the exception of manufacturing. For its part, manufacturing grew faster than services in most countries except in some middle-income countries, particularly the highly indebted ones and in sub-Saharan Africa. In the latter group, manufacturing was depressed with industry actually contracting in favor of agriculture which exceeded services in growth.

Table II

Distribution of GDP by sector in 1965 and 1986 (%)

	Agriculture		Industry		Manufacturing		Services	
	1965	1986	1965	1986	1965	1986	1965	1986
LOW INCOME COUNTRIES	42	32	28	35	21	24	30	32
MIDDLE INCOME COUNTRIES	20	15	30	36	20	22	50	48
INDUSTRIAL	5	3	40	35	30	23	55	61
DEVELOPING	29	19	29	36	..	..	42	36
Oil exporters	22	18	29	33	15	15	39	49
Manufactures exporters	34	18	31	35	..	..	36	44
Highly Indebted countries	18	15	32	36	23	23	49	47
Sub-Saharan Africa	39	36	19	25	10	10	42	36

Source: World Bank

By 1986 services also accounted for the largest proportion of GDP in most categories of countries except the low-income countries where it was still exceeded by industry. For developing countries as a whole, services and industry accounted for about equal parts of GDP and in sub-Saharan Africa it was equal to agriculture. In the industrialized countries, services exceeded the next largest sector of the economy, industry, by about 75 per cent. Over the 20-year period 1965-1985 the share of services increased for the industrialized countries, but for developing countries as a whole it declined. Within this category, however, declines in the share of GDP were recorded by the highly indebted countries and in sub-Saharan Africa, which declined significantly, but it increased significantly for the exporters of manufactures and the oil exporters. For the middle-income developing countries, manufacturing and industry grew while the services portion of GDP declined.

Table III

Merchandise trade and services balances (U.S. $b.)

	1980	1981	1982	1983	1984	1985	1986	1987	1988	1989
Industrial countries										
Trade balance	-67.4	-19.6	-14.8	-17.1	-44.6	-37.7	-0.9	-14.9	-5.9	-3.7
Services net	39.9	32.1	24.0	27.1	17.1	20.8	22.9	13.0	4.8	3.0
Developing countries										
Trade balance	96.4	38.1	8.2	16.7	48.7	44.2	5.7	49.5	40.1	42.9
Services net	-80.5	-102.0	-108.7	-97.2	-100.8	-90.1	-71.9	-74.5	-79.8	-84.1
By categories of exporters (developing countries)										
Primary product exporters										
Trade balance	-10.5	-23.5	-16.6	-0.4	12.9	19.5	17.3	15.6	16.2	17.9
Services net	-33.8	-40.9	-46.4	-44.6	-46.6	-43.9	-44.1	-46.2	-48.4	-50.0
Agricultural exporters										
Trade balance	-17.1	-16.9	-13.5	-4.3	10.0	12.2	9.6	8.4	8.7	10.4
Services net	-22.9	-28.0	-34.4	-32.9	-34.8	-33.2	-32.4	-33.7	-35.8	-37.1
Mineral exporters										
Trade balance	6.5	-6.6	-3.1	3.9	2.9	7.3	7.8	7.2	7.5	7.5
Services net	-10.9	-12.9	-12.0	-11.7	-11.7	-10.6	-11.7	-12.5	-12.7	-12.9
Exporters of manufactures										
Trade balance	-34.3	-29.0	-15.9	-11.9	-4.3	-15.2	-1.1	14.2	11.0	9.7
Services net	0.5	0.2	0.9	0.7	-2.0	-2.7	-0.6	0.6	0.7	-0.2
Service exporters										
Trade balance	-28.0	-30.7	-30.6	-28.8	-28.1	-26.4	-24.5	-26.0	-27.0	-28.6
Services net	9.8	8.5	8.1	7.7	7.0	6.2	6.1	7.5	7.5	8.3
Fuel exporters										
Trade balance	169.2	121.4	71.3	57.8	68.2	66.3	14.0	45.7	39.9	43.8
Services net	-57.1	-69.8	-71.2	-61.1	-59.3	-49.8	-33.4	-36.4	-39.5	-42.2

Source: I.M.F. World Economic Outlook 1989.

The industrialized countries have consistently incurred deficits in merchandise trade over the period 1980-1985. Accumulated surpluses on services have been able to compensate, although the gap between the merchandise and services balances has narrowed over the decade. For the developing countries as a whole the converse has been the case, with services deficits greater than (though fairly stable) trade surpluses. Within this broad generalization, however, various categories of developing countries manifest differing characteristics.

Deviations from the norm are the exporters of manufactures, which have shown only slight and intermittent deficits in services trade over the 10-year period, and the services exporters who are also beneficiaries from remittances from nationals abroad, who have achieved a positive balance on services, though insufficient, to compensate for the consistent deficits on merchandise trade.

The largest deficits on services have been incurred by the fuel exporters, as various services had to be imported to support the rapid economic growth made possible by substantial merchandise trade surpluses. But deficits were incurred by all the major primary products exporters, whether they were based on agriculture or minerals and reflect the fairly rudimentary stage of diversification achieved by them. This makes an interesting contrast to the exporters of manufactures, most of whom needed to develop fairly substantial services sectors of their own to become effective producers and exporters. Accordingly, they incurred only modest deficits on their services trade.

Table IV

Major **EXPORTERS** of services

Rank	All services	Value($b)	Share<1>
1	United States	45.4	12.1
2	France	39.2	10.4
3	United Kingdom	28.9	7.7
4	Germany, FRG	26.9	7.1
5	Japan	24.6	6.5
6	Italy	19.4	5.2
7	Netherlands	18.3	4.9
8	Spain	14.0	3.7
9	Belgium/Luxembourg	11.9	3.2
10	Singapore	9.7	2.6
	Top ten countries	238.3	63.4
	World total	375.2	100.0

Major **IMPORTERS** of services

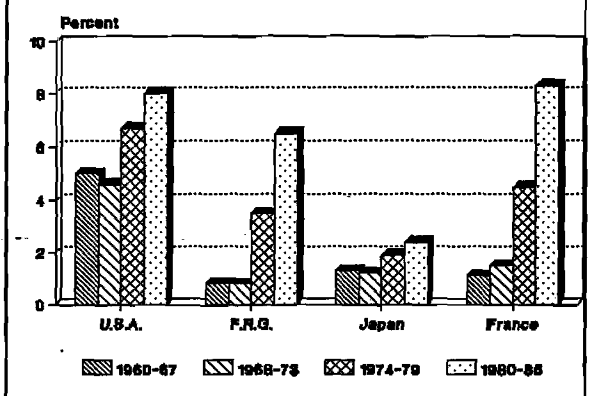
Rank	All services	Value($b)	Share<1>
1	United States	46.2	11.5
2	Japan	42.3	10.5
3	Germany, FRG	38.8	9.6
4	France	29.1	7.2
5	United Kingdom	25.6	6.3
6	Netherlands	14.7	3.6
7	Italy	14.5	3.6
8	Saudi Arabia	14.2	3.5
9	Canada	12.1	3.0
10	Norway	10.5	2.6
		248.0	61.4
		402.6	100.0

Source: IMF, UNCTAD

<1> Share of the market in per cent

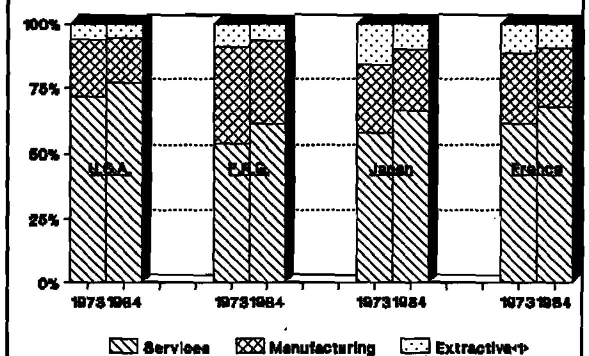
The global trade in services is dominated, for the most part, by the United States, Japan and the European Community, these countries accounting for nine of the top 10 exporters of services and seven of the top 10 importers. Among the top 10 traders in services, only Singapore appears for the developing countries as an exporter, while only Saudi Arabia appears as an importer.

Figure 1
Annual Unemployment Rates
Selected O.E.C.D. countries



Source: O.E.C.D.

Figure 2
Share of Employment by sector
Selected O.E.C.D. countries



Source: O.E.C.D.
*Includes Agriculture Mining Utilities

Noteworthy also are trends in employment in the services sectors globally. Up to 1973, the structure of employment in the most developed countries was fairly stable in terms of the proportion of labour allocated to the various sectors; productivity was fairly high and unemployment rates low. After 1973 unemployment rates increased fairly rapidly, productivity declined and a higher proportion of the labour force began to shift into services, including the informal services sector. Within the services sector, fastest growth was recorded in social services followed by producer services and personal services, respectively. The increasing capital intensity of the transportation and communications sub-sector, however, limited labour absorption in this category.

Initially the shift towards services employment created concern that it was a reflection of reduced productivity in the economy as a whole and was a symptom of "the de-industrialization process". Subsequently, a number of other factors were included in the analysis, such as changing product and market strategies, changing corporate structures and changing public policies. Together, these stimulated and were facilitated by changing technologies and particularly the information technologies, which in turn held the potential for huge increases in productivity by virtually revolutionizing many productive processes.

Changing product and market strategies were spurred by a number of factors such as the globalization of markets and de-regulation, which brought new entrants into the market from adjacent specializations. As markets became larger and more transparent, product differentiation for specific market segments became more viable and product lives were shortened as manufacturers became more sensitive to consumer shifts.

In partial response to these changes, a number of modifications were also taking place in corporate structures to emphasize market information, planning and product development, flexible production, advertising and innovative retailing methods. With the identification of and demand for specific types of expertise, greater specialization was possible with the concomitant development of specialized service firms. Similarly, services which had been provided within the firm were often sub-contracted, with further specialization of tasks both in the corporation and in the service firm.

Smaller firms also gained access to specialized services not previously available to them. At the same time, while sub-contracting many services, the firm nevertheless needed staff in-house that were capable of interfacing with the service firms. In conjunction with the need for staff to control sophisticated computer-controlled design and manufacturing processes, these factors have shifted the emphasis in staffing from blue collar manual workers to white collar and professional service workers.

Changing public policies have also impacted upon the evolution of global services. De-regulation, as mentioned before, has impacted upon fields, such as financial services and communications, to create new entrants to particular market segments as well as to create new combinations of services straddling former delineations. Changing perceptions about the role of the State, as well as similar trends evident in the private sector towards specialization, have stimulated policies towards divestment of public entities or sub-contracting of various tasks previously performed by the State. At the same time, concerns about equity and the provision of a safety net for those disadvantaged by the rapidly changing economic environment also encouraged the development of new social services.

The growth of services has impacted upon the structure of the labour market in a number of ways. It has permitted a sharp increase in participation rates among women and rendered a significant number of new tasks available to them. The shift from blue-collar to white-collar work and the demands of the new information technologies have placed a high premium on advanced professional and technical skills. Finally, and seemingly at variance to the above, new distribution modes for the retail and personal services sectors, such as franchising, have also increased the demand for low-wage, low-skilled, often part-time workers with little or no prospects for job mobility. And many such jobs are filled by women and youths.

In conclusion, the rapid transformation that has taken place in the 1980s in the production, distribution and exchange of goods has taken place hand-in-hand and been made possible by a virtual revolution in the area of services. New comparative advantages have been created by these changes and those best able to develop and use these services at the national or corporate level have gained a significant competitive edge over their rivals.

EVOLUTION OF SERVICES IN THE CARIBBEAN

Table V

CONTRIBUTION OF SERVICES TO G.D.P. <1>

	1980				1989			
	TOTAL<2>	BASIC	OTHER	GOVT	TOTAL<2>	BASIC	OTHER	GOVT
Antigua	82.5	21.4	61.1	12.2	78.8	24.2	54.6	9.4
Barbados<3>	59.6	7.2	52.3	12.1	74.9	10.3	64.6	13.4
Belize<3>	60.5	8.7	51.7	9.4	65.8	12.7	53.1	10.4
Dominica	57.7	8.2	49.6	22.9	58.6	11.9	46.7	19.4
Dominican Republic	52.0	5.9	46.1	8.3	54.3	9.6	44.7	9.6
Grenada	69.6	16.1	53.4	16.0	68.9	16.5	52.4	15.2
Guyana<4>	45.0	7.1	37.9	21.5	48.1	7.3	40.8	22.3
Haiti	38.4	2.7	35.7	9.2	41.8	3.4	38.4	11.6
Jamaica	71.4	6.7	64.7	19.2	69.3	10.0	59.3	15.4
St.Kitts/Nevis	61.0	9.7	51.3	19.5	71.1	18.1	53.1	18.9
St. Lucia<5>	72.2	13.6	58.6	18.0	74.2	13.7	60.5	22.1
St.Vincent	68.9	23.3	45.6	17.2	64.9	28.8	36.1	12.6
Suriname<5>	57.7	6.2	51.5	16.6	68.4	8.5	59.9	25.6
Trinidad/Tobago	54.3	10.0	44.3	7.8	63.6	10.6	50.0	12.7
Puerto Rico	56.9	8.9	48.0	13.1	57.0	8.1	48.9	11.1

Source: ECLAC, derived from national data.
<1>Contribution of services to real G.D.P. (in per cent)
<2>Refers to the contribution of all services; basic services refer to electricity, water transport storage and communications. Other services include government.
<3>Refers to 1980 and 1988
<4>Refers to 1982 and 1987
<5>Refers to 1980 and 1987

As a conservative estimate[2], services contribute in excess of 50 per cent of GDP for all Caribbean countries, with the exception

[2] For the purposes of this analysis the category "Construction and Installation" is not included in the definition of services.

of Haiti and Guyana[3]. For most of the smaller economies, the services sector accounted for over 70 per cent of GDP in 1989, while in the larger more diversified countries it was lower, with just over 40 per cent for Haiti and hovering around 50 per cent in the case of Guyana and the Dominican Republic, although Jamaica is fairly services-intensive with almost 70 per cent of GDP being so derived. Services contributed on average over 60 per cent for the region as a whole.

During the 1980s the wide variance between countries in their dependence upon services has narrowed slightly, from Antigua, on the one hand, at over 80 per cent (down to 79 per cent by 1989) to Haiti, on the other, at below 40 per cent in 1980 although increasing to almost 42 per cent by 1989. For the region as a whole, the dependence on services has increased slightly, by about 4 per cent.

Basic services, which comprise electricity, water, land, sea and air transport, storage and communications, represented a larger portion of GDP in 1989 than in 1980 in all countries, with the exception of Puerto Rico. In Saint Vincent and the Grenadines and Antigua and Barbuda, basic services had the largest proportion of GDP in 1980 and again in 1989, while Haiti recorded the smallest contribution in both years and reflected the fact that, for the smaller countries, infrastructure loomed larger in the economy than for the larger ones. For the region as a whole, the share of basic services increased over the 10-year period though at a slightly slower rate than for services as a whole. Nevertheless, such growth as has taken place in the share of services in GDP must be ascribed mainly to basic services.

A major issue of current public policy has related to the role of the State in the economy, intuition suggesting that whereas the 1970s was a decade of large government, financed by windfalls to some raw materials producers, the 1980s necessitated smaller government, much being made of the role of decentralization and divestment for countries in the throes of structural adjustment. It comes, therefore, as somewhat of a surprise that for the region as a whole, government services increased slightly from just under 15 per cent of GDP to just over 15 per cent of GDP.

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[3] Cuba is excluded from the GDP analysis because of incompatible national accounting methods which do not fully dis-aggregate services. The closest approximation, that of non-material product, only identifies transport, communications, commerce and other and together comprised 31 per cent of Global Social Product in 1989, down from 33 per cent in 1980.

Suriname recorded the largest share of government services followed by Guyana and Saint Lucia[4], all growing significantly since 1980. In the case of the former two countries, this occurred in a scenario of disequilibrium and declining GDP. The other country suffering major structural disequilibrium, Jamaica, however, recorded a significant decline in the government portion of its product, also in a scenario of stagnating or declining product. At 15.4 per cent, Jamaica is now only slightly over the regional mean. Other countries with large government sectors are Dominica, declining over the decade from almost 23 per cent to just over 19 per cent, and Saint Kitts/Nevis, which decreased marginally from just over to just under 19 per cent. Significantly below-average rates were shown by Antigua/Barbuda, the Dominican Republic and Haiti, although the latter has grown over the decade.

Of major policy interest, however, is not merely the contraction of public services, but rather the manner of the contraction and its impacts, observation leading to the conclusion that maintenance of plant and equipment suffered as did the interests of those individuals having lower bargaining power, such as health and education service workers.

The category "Other services[5]" grew slightly over the decade, by about one percentage point for the region as a whole. Within the overall aggregate there was, nevertheless, significant change at the country level, the fastest increase in GDP share being recorded by Barbados which, at the same time, had the highest proportion of other services to GDP, at almost 65 per cent. Suriname, Saint Lucia and Jamaica also recorded high proportions in this category.

A focus solely on macro-economic indicators, however, provides an incomplete picture of developments in the area of services. An attempt will, therefore, be made to look at some selected individual services activities in greater depth.

Tourism

Tourism is the fastest growing component of the world trade in services. By the middle of the decade it accounted for 28 per cent of such trade and this share has increased since. The World Tourism Organization (WTO) estimates that tourism arrivals grew from 160 million persons in 1970 to 285 million in 1980 and to 404 million in 1989. But the rate of growth was not even, for the first

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[4] Latest figures for Suriname, Guyana and Saint Lucia are for 1987.

[5] The category includes the activities of the distributive trades, real estate services, government services, household, private non-profit and other miscellaneous services.

three years of the decade tourism arrivals stagnated, though robust growth was recorded for the period 1984-1989. The WTO estimates that the developed countries provide 66 per cent of tourist arrivals and 72 per cent of receipts, but some developing countries such as Mexico, Thailand, Korea and Singapore were among the top 20 revenue earners in 1987.

Caribbean tourism accounts for a very small portion of the global industry, less than 3 per cent of the total volume and just over 3 per cent of the value. It has, however, grown faster than global tourism over the survey period, arrivals to the region increasing by 60 per cent over the decade in comparison with a global increase of 50 per cent[6].

For the region, however, tourism is a major economic activity at or near the top of export earners for most countries. Over the survey period tourist arrivals increased by about 63 per cent, while nominal expenditures increased by over 120 per cent. Cruise ship visitors arrived at an even faster pace than stopovers, at about 86 per cent. The number of hotel rooms grew by about 46 per cent, or 35,000 rooms, in the region as a whole and by the end of the survey period the number of people employed directly and indirectly by the industry was estimated to be over 400,000.

For 1989 estimated earnings for the region as a whole were in excess of $7000 million. Yet this could be an underestimate of its true contribution[7], since far from being a single activity, tourism is in reality a constellation of diverse inputs and services such as personal accommodation, entertainment including cultural and recreational services and local sightseeing - souvenirs, communications, advertising, airline charters, cruise-ship operations, credit cards and travel insurance.

The industry has integral linkages with construction, agriculture, light manufacturing and handicrafts. It creates a demand, and, therefore, supports local infrastructural and personal services which can significantly improve the quality of life of visitors and locals alike. It provides an outlet for local cultural elements which can impinge upon all of the above industries and services to improve the quality, uniqueness and, therefore, the value of the tourism product. Seen in this light, tourism makes a

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[6] Data for this section are drawn from various issues of C.T.O. Caribbean Tourism Statistical Reports. Some totals may differ due to the exclusion of Anguilla, Bermuda, the Turks and Caicos Islands and the Cayman Islands from some of the tables.

[7] At the same time this figure, which is based on CTO national estimates, is greater than would appear from balance of payments statistics. Greater discussion of these issues appears earlier in the text, in the methodological note.

greater contribution to the economy than is normally captured and holds unrealized potential for more intensive development.

Figure 3
Index of Export Earnings

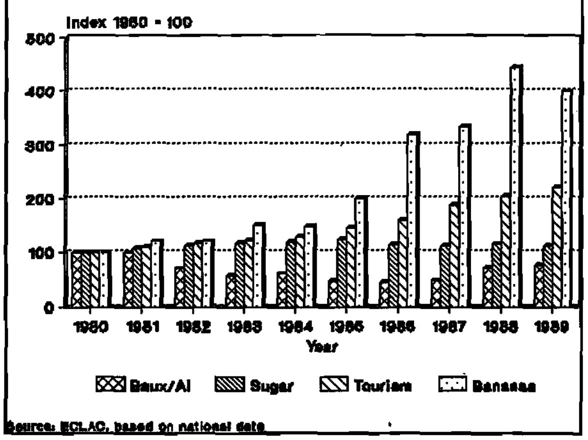
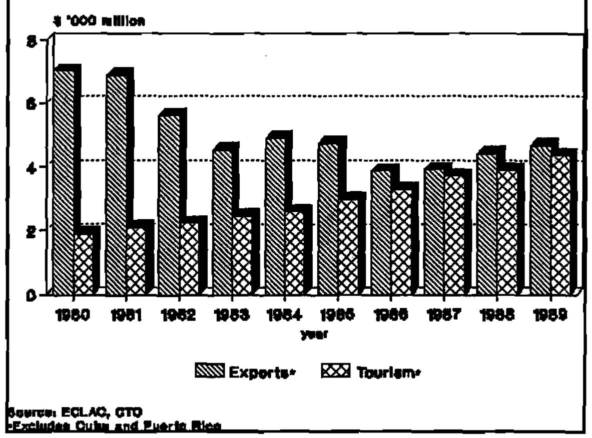


Figure 4
Merchandise and Tourist earnings



For the region as a whole, tourism has provided the engine of economic growth in the 1980s, growing faster than sugar, bauxite/alumina and petroleum, all of which actually contracted. While banana earnings have risen faster than tourism, they are relatively small in quantum, impact on a limited number of countries and are dependent upon uncertain preferential arrangements. On the other hand, regional tourism which operates successfully in a fiercely competitive global market has provided earnings in excess of total merchandise earnings for many countries in the region. If the respective merchandise and tourism earnings of the two largest economies, Cuba and Puerto Rico, are excluded, tourism earnings have grown in the face of a steady decline in merchandise earnings to the stage where they are now almost equal in magnitude[8].

Tourism expenditures, at current prices, grew almost twice as fast as arrivals, which averaged over 7 per cent per annum for the survey period. In fact arrivals declined in 1981 and grew relatively slowly up to 1984, in line with stagnating global tourism. Subsequently, however, arrivals picked up to sustain a rapid increase up to the end of 1989. As would be expected, fastest growth was recorded by the small new destinations, such as Antigua, Belize, Dominica and Saint Kitts and Nevis; or more established destinations recovering from past declines, such as Cuba, Grenada

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[8] The figure, which is based on data for a selection of 16 Caribbean countries, excluding Cuba and Puerto Rico, dramatizes the underlying shifts which are taking place. Reliable balance of payments data are not available for the remainder, but they are all essentially tourist economies and their inclusion would underline the argument

Table VI

TOURISM EXPENDITURE
(U.S $m)

	1980	1981	1982	1983	1984	1985	1986	1987	1988	1989
Antigua	42.0	49.0	58.9	77.1	109.7	132.5	156.2	186.7	213.5	231.8
Bahamas	595.0	639.1	654.5	770.2	801.5	995.0	1104.9	1145.8	1149.5	1230.0
Barbados	251.0	261.9	251.1	251.6	284.2	309.0	326.9	378.7	460.0	505.0
Cuba	47.5	52.4	61.2	74.3	95.5	116.4	150.0	185.0	223.0	230.0
Dominica	3.2	3.0	4.0	7.3	8.6	8.7	11.2	12.8	14.0	18.5
Dominican Rep.	167.9	223.2	272.7	282.3	315.0	368.2	420.0	545.0	616.0	750.0
Grenada	14.8	17.3	17.2	18.7	22.7	32.4	39.6	42.1	46.0	53.1
Haiti	46.3	55.5	55.5	61.0	66.0	69.2	63.1	69.0	75.0	75.0
Jamaica	241.7	284.3	337.8	399.2	406.6	406.8	516.0	595.0	525.0	593.0
St.Kitts/Nevis	13.4	16.1	17.3	18.6	24.2	31.0	38.0	47.4	53.8	60.0
St. Lucia	32.9	29.4	32.4	39.7	68.4	90.0	118.0	126.2	134.2	144.6
St. Vincent	13.7	15.0	16.0	16.7	19.0	23.0	29.3	35.2	38.6	42.9
Suriname	18.2	40.6	32.8	17.9	13.3	9.0	7.8	10.5	7.9	7.9
Trinidad/Tobago	151.1	151.9	178.6	205.7	197.8	197.3	83.2	91.6	80.0	80.8
Aruba	137.5	156.4	163.1	114.5	118.4	120.8	158.1	203.6	279.3	316.0
Br Virgin Is	42.3	53.8	65.6	81.5	54.6	67.8	88.8	110.8	120.8	124.6
Montserrat	4.3	5.4	5.8	6.0	6.7	7.7	7.5	9.8	11.2	10.6
Netherlands Ant	259.6	280.2	258.7	205.0	199.9	225.0	255.5	279.7	321.6	371.7
US Virgin Is	304.3	317.5	312.5	356.3	434.0	507.4	509.8	623.0	650.3	595.9
Guadeloupe	110.9	93.5	107.5	116.0	98.0	95.0	163.0	188.0	220.0	183.0
Martinique	74.6	75.2	81.6	82.6	87.0	92.8	107.8	210.0	230.0	272.3
Puerto Rico	615.0	649.7	699.2	690.7	681.2	722.7	743.0	896.2	1062.1	1135.4
TOTAL	3187.2	3470.4	3684.0	3892.9	4112.3	4627.7	5097.7	5992.1	6531.8	7032.1

Source: CTO. 1989 data are preliminary.

or Jamaica. Very strong performance was also recorded by the Dominican Republic, which has made significant adjustments away from traditional export earnings toward new non-traditional sectors, such as tourism.

But the more established destinations such as the Bahamas, Barbados and Puerto Rico, nevertheless, recorded solid gains to consolidate their positions. In fact, in 1989 the Bahamas and Puerto Rico each earned over US$1000 million from tourism and together accounted for one-third of regional earnings. Internal socio-political problems affected performance in Haiti, Suriname and Guadeloupe, the latter also suffering from hurricane damage, although only Suriname and Trinidad and Tobago actually suffered declines in growth over the decade.

Major destinations are Puerto Rico, the Bahamas and the Dominican Republic, all of which received in excess of 1 million stopover visitors in 1989. Yet judged by the intensity of the industry, it is some of the smaller destinations which stand out. In per capita terms, the British and United States Virgin Islands, the Cayman Islands and the Bahamas all receive in excess of six visitors per inhabitant in 1988.

Table VII

STOPOVER TOURIST ARRIVALS
(Thousands)

	1980	1981	1982	1983	1984	1985	1986	1987	1988	1989
Antigua	87	100	102	117	145	156	166	177	195	198
Bahamas	1181	1031	1101	1240	1279	1368	1375	1480	1475	1575
Barbados	370	353	304	328	368	359	370	422	452	461
Belize	64	64	67	64	88	93	94	99	164	220
Cuba	94	121	139	162	207	241	282	293	309	310
Dominica	14	16	19	20	22	22	24	27	32	35
Dominican. Rep	383	451	480	502	562	660	785	911	1116	1300
Grenada	29	25	23	33	40	52	57	57	62	69
Guyana	40	40	41	45	47	46	47	60	71	67
Haiti	136	139	135	145	141	150	112	122	122	122
Jamaica	395	406	468	566	603	572	664	739	649	715
St.Kits/Nevis	33	36	35	34	40	46	55	65	70	72
St. Lucia	80	69	70	78	86	95	112	112	125	133
St. Vincent	50	45	37	38	39	42	42	46	47	50
Suriname	48	54	52	39	36	32	29	27	21	21
Trinidad/Tobago	199	187	190	190	192	187	191	202	188	194
Aruba	189	221	220	195	210	207	181	232	278	344
British Virgin Is.	97	110	114	119	122	130	146	173	176	176
Montserrat	16	16	15	14	16	17	16	17	18	17
Netherlands Ant	402	404	427	410	476	518	567	632	685	751
US Virgin Is	380	344	340	345	370	412	470	555	543	492
Puerto Rico	1627	1573	1564	1530	1496	1545	1573	1872	2155	2257
Guadeloupe	157	133	255	260	227	216	246	293	329	255
Martinique	159	157	176	176	184	194	183	234	280	312
Total	**6230**	**6093**	**6374**	**6649**	**6995**	**7358**	**7786**	**8346**	**9562**	**10146**

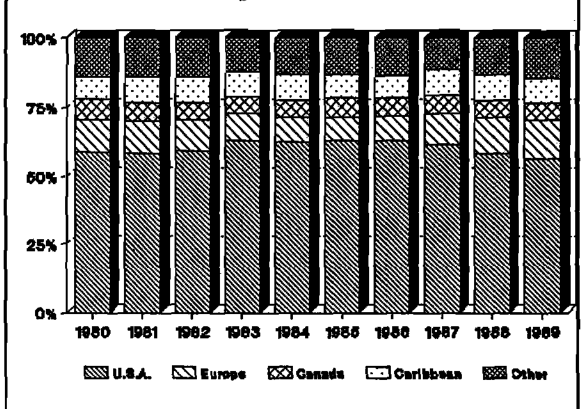
Source: CTO; 1989 data are preliminary.

As a highly competitive global industry, tourism is price sensitive and this is reflected in the growth of the industry both for the Caribbean as a whole and for the respective destinations within the region. It is also reflected in the origin of visitors as currency fluctuations affect the prices of Caribbean vacations relative to other competing areas.

The United States was the major source of visitors to the region, with almost 60 per cent of the total throughout the decade. But the dependence on the United States market varied quite considerably throughout the region, with the most dependent being the Bahamas, United States Virgin Islands, Cayman Islands and Puerto Rico at over 70 per cent, while Saint Lucia, Saint Vincent and the Grenadines, Cuba, Dominica, Grenada, Curacao, Martinique and Guadeloupe received less than 30 per cent of its tourists from that source.

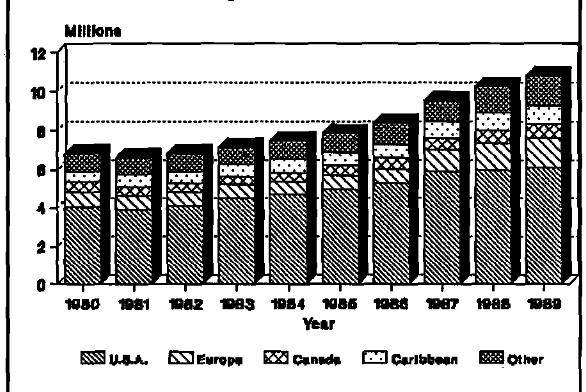
As Caribbean currencies are tied to the United States dollar, the prices of Caribbean vacations, which must be paid by other currency areas, will rise and fall in sympathy with the appreciation or decline of the United States dollar. Accordingly,

Figure 5
Tourist Arrivals
Origin of Caribbean Tourists



Source: CTO

Figure 6
Tourist Arrivals
Origin of Caribbean Tourists<1>



Source: CTO
<1>Totals include Bermuda and Cayman Is.

Western Europe which accounted for 12 per cent of the Caribbean market in 1980, fell to 8.6 per cent of the market as the dollar appreciated, but its market share climbed from that point to a peak of 14 per cent by the end of the decade, as the dollar declined. Arrivals from Europe grew by 128 per cent between 1984-1989 and was divided between France 28 per cent, the United Kingdom 25 per cent, West Germany 13 per cent, with the remaining countries accounting for 34 per cent. The eight major beneficiaries from the European market, which account for 70 per cent of the total, are ranked as follows: Martinique and Guadeloupe, mainly from France; Barbados mainly from the United Kingdom; Puerto Rico, St. Maarten, Cuba, Jamaica and the Bahamas. The European market is valued because it is barely exploited[9] so far. Europeans tend to stay for longer periods, spend more per visit, focus on summer vacations and are in many ways complementary to North American arrivals, not least because of the differing trade cycles becoming evident for both regions.

By the same token, the share of the market accounting for Caribbean people travelling within the region remained relatively stable at about 9 per cent. The major destinations for Caribbean tourists were Puerto Rico, the Dominican Republic, Curacao, Barbados and Trinidad and Tobago. In the latter the emphasis is on travel by friends and relatives mainly for Carnival celebrations.

The Canadian portion of the market which started the decade at 7.4 per cent declined steadily until 1984, making a recovery in 1985 and 1986, only to decline once more to 6.5 per cent by the end of the decade. The major destinations for Canadians were the Dominican Republic, Jamaica, Puerto Rico and Cuba.

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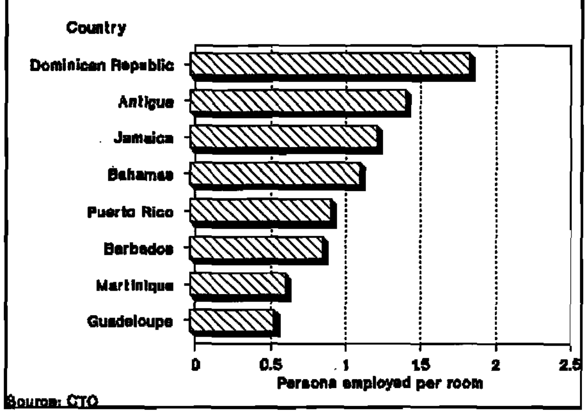
[9] Only 2 percent of travel outside Europe was to the Caribbean, compared with 25 percent for the United States.

But market share only gives some idea of the relative growth of the various sources of tourists. In fact in an expanding market, arrivals from all destinations increased in absolute terms and over the decade total arrivals grew by 63 per cent.

The employment effects of tourism are also significant although difficult to quantify with any accuracy. For some of the major tourist destinations the direct and indirect effects clearly surpass those of any other industry[10]. But even in countries with more diversified economies, the employment effects can be considerable.

Difficulties in arriving at an accurate figure arise from the seasonal nature of tourism, different levels of labour input between country and between establishments and differing estimates of the indirect effects of the industry. While the Caribbean Tourism Organization (CTO) is encouraging more precise data collection at the national level, some estimates have nevertheless been made which provide a guideline as to its effects.

Figure 7
Tourism Employment
Employee/Room Ratios



For direct employment effects, an employee to room relationship of 1.19 has been estimated by the CTO based on studies for 16 Caribbean destinations. At one end of the spectrum lies the Dominican Republic which is the most labour-intensive with 1.8 persons employed for each room, while Martinique and Guadeloupe employ 0.6 persons per room. If the ratio of 1.19 is employed for the Caribbean as a whole, the CTO estimates that over 140,000 persons are employed by the industry directly in accommodation establishments. Surveys and rule-of-thumb suggest a three-to-one ratio for total employment generated by the industry as a whole.

Tourism also makes a major contribution to government revenues in many countries. It arises from some or all of the following services: airport departure and hotel occupancy taxes; aircraft landing fees; sales taxes on air tickets and tourist purchases; import duties on goods and services used by tourists, corporation taxes and licence fees; income tax from tourism employees, entertainment fees; taxi drivers licence fees, and so on. As an

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[10] In the Bahamas this figure is estimated to be 49 percent, the US virgin Islands 35 percent, Antigua 24 percent, Saint Lucia 21 percent (Boxhill, Bryan "Employment Generated by Tourism in the Caribbean Region" CTRC 1982)

indication of the impact that this can have on government receipts, surveys estimated that in 1984 the Government of Jamaica received 31 per cent of each dollar of stopover tourist expenditure and 26 per cent of each cruise ship passenger dollar. In all, tourists provided the Central Government with 27 per cent of current revenue.

Financial services

Financial services contribute between 5-10 per cent of GDP for most countries and has shown modest growth over the survey period. This constellation of services is provided by banks, insurance and trust companies, mortgage and finance houses, savings and loan associations and, where appropriate, stock exchanges and unit trusts.

Briefly stated, the services provided include deposit taking and lending in local and foreign currencies to governments, corporations, and individuals. Also included are specialized areas such as trade financing, loan syndication and actual participation in business ventures. A range of advisory and brokerage services are also provided. For their part, insurance services transfer and share risk at the personal and corporate level over time and across borders and in the process they also provide an effective mechanism for the mobilization of private savings. As a consequence of this natural overlap of functions, there is an increasing tendency for the lines of demarkation between various financial services to be crossed.

The financial institutions hold a pivotal position in the national economy, since they interact with all the economic sectors and with virtually all institutions and individuals. Accordingly, they are a major target for government policy, both as it impinges on the financial sectors directly, and as it uses them to direct the macro-economy as a whole. As a key producer service, they have the capacity to influence the efficiency and competitiveness of the economy, for good or for ill, and this capability is in large measure determined by the regulatory policies under which they are required to operate.

Regulatory policies can, for example, affect the nature and the scope of the services provided to the public. For example, foreign exchange policies will condition the nature of financial services that can be provided beyond national boundaries. Regulations, rather than intrinsic reasons have established the demarkation of functions between, say, insurance companies and banks, but as services have become more diversified the areas of demarkation between various institutions have become blurred. The regulatory framework has, therefore, come under some strain, requiring adjustment if the sector is to provide the full range of innovative services to remain competitive. Regulations are also used to protect the interests of the various actors in financial transactions and provide some measure of protection against fraud, bankruptcy, default and so on.

At the same time, since the financial community facilitates a two-way flow of resources to and from the community, government finds it convenient to conduct a major part of its macro-economic management indirectly through the financial institutions, for example, the expansion or contraction of credit, the allocation of resources to key productive areas and the management of trade with the rest of the world.

Financial sector developments in the region

Any evaluation of the performance of the financial sector needs to be grounded in the macro-economic policies pertaining to a particular country during the survey period. An exercise of this magnitude is clearly beyond the scope of this paper, yet a few broad generalizations may be made to provide a sketch of developments in the financial sector over the survey period.

A number of common macro-economic policies provided the framework in which the financial institutions of the larger CARICOM countries operated. This policy framework evolved during the 1960's and 1970's, but was being increasingly questioned toward the end of the survey period, perhaps because the objectives upon which the policies had been predicated were not attained.

Fundamental to the policy was the localization of the banking sector, with the objective of increasing local savings and ensuring that they were retained and invested locally. Investment preferences were for long-term development ventures rather than the fostering of trade, particularly the import trade and the export-oriented plantations. Exchange controls were introduced to underpin the strategy, while it was assumed that low rates of interest would foster investment and selective credit controls and administered differential interest rates would be used to allocate resources in accordance with policy priorities. Midway between these two objectives, of mobilizing savings and that of allocating them to certain categories of investors, was a recognition of the need to transfer savings to instruments that would be amenable to long-run investment. In order to achieve this goal, there was a perceived need for structural changes and innovation in the banking sector itself. Fears that localization would cut local banks off from foreign capital markets and technical developments in the industry were expressed at the time, though it was felt that governments could perform the former role directly.

National savings ratios in the region are low and sometimes negative. For most countries, it is on average below 10 per cent during the survey period, a deterioration over the previous decade. Various regional studies suggest that savings increase with the level of national income though it is much higher among level of national income though it is much higher among corporations than among individuals and a major role is played by the public sector in the savings equation. In the latter case, one major issue is whether the public sector preempts the use of savings and crowds out the private sector. But the use made of the credit to the public sector is also crucial, since the development of infrastructure is recognized to be conducive to long-run aggregate savings, whereas the use of credit to finance public enterprise deficits or recurrent expenses is inimical to long-run aggregate savings.

Policies to bias the lending of commercial banks into predetermined areas, such as small-scale agricultural or industrial enterprises or low-income housing, were for the most part treated with circumspection by the banks themselves. The growth of government sponsored agricultural or industrial development banks or housing credit institutions in the More Developed Countries (MDC's) attested to the governments' belief that they would have to try to meet these needs themselves. The subsequent failure of many of these institutions to operate as viable commercial entities might be seen to further justify the reticence of the commercial banks to conform to government guidelines.

Empirical evidence shows an increase of capital outflows beginning in the 1970s and quickening in the 1980s[11]. Capital flight is believed to be related to expectations about future exchange rates (signalled early by the state of the balance of payments current accounts) and differential interest rates between the national and external markets. But the mere existence of foreign exchange controls increases uncertainty about the availability of currency in a timely fashion and limits the items for which it may be used, thus encouraging the holding of currency abroad.

Foreign capital inflows, primarily in the form of portfolio capital, have been used to meet the shortfall in domestic savings. A substantial portion of this has been to the public sector, government guarantees serving to erode much of the discipline that would normally be exercised by financial institutions in evaluating its use. Debt ceilings in some countries and developments in global financial markets suggest that external capital will be an increasingly more scarce source of funding for small Caribbean countries than it has been in the past. Direct foreign investment,

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[11] In Guyana, capital outflows increased from 32 per cent of external debt in the period 1976-1980 to 122 per cent of external debt in 1981-1984. For Trinidad and Tobago corresponding figures were estimated to be 63 and 98 per cent respectiveley. The trend was, however, reversed in Jamaica which seemed to have capital repatriation in 1984. Source: Bennett, Carl: External Debt, Capital Flight and Stabilization Policies" Regional Monetary Studies Conference 1987.

which was discouraged by some countries in the 1970s, but subsequently encouraged in the 1980s, has proven to be relatively insignificant in most CARICOM countries over the survey period, except in the Bahamas and Trinidad and Tobago. Increasingly, foreign investors are being swayed by domestic investment performance, so that foreign investment is likely to follow an upswing in domestic investment rather than to serve as a substitute for it.

The efficiency of investment in Caribbean countries is also low and determined by a number of factors such as labor productivity, maintenance of plant and equipment, but this is a clear-cut area in which better financial services could increase the efficiency of investment and the rate of economic growth. This could be done by the acquisition of the necessary financial skills by the financial sector to better evaluate, select and manage investment projects.

Aside from looking at the achievements of the financial sector, one could also examine how it has changed in structure, listing the amount of innovations it has adopted over the survey period. While there have been some, they have been few and late and often constrained by the regulatory framework governing banking operations.

In summary, it is difficult to arrive at clear conclusions about the performance of the banking sector in isolation, since it is virtually impossible to separate the efficiency of the financial sector from the macro-economic regulatory framework within which it must operate. Suffice it to say that most of the objectives set for the indigenous financial sector and for which policies were shaped, have remained unsatisfied. Even where it is fairly clear that innovations in the industry have been few, it might be argued that policies to limit new entrants into the sector have encouraged stagnation.

Exports of financial services

The export of financial services provides useful income for a number of Caribbean countries and others, such as Barbados, Jamaica Puerto Rico and some OECS countries, have enacted new regulations in the hope of encouraging its development. In the field of international banking, the Cayman Islands and the Bahamas are ranked sixth and eleventh, respectively, based on foreign liabilities in mid-1988 with global market shares of 4.8 per cent and 3.2 per cent, respectively. The existing major players have sought a competitive edge through tax-free status, existing banking expertise, a liberal regulatory framework, good communications infrastructure, confidentiality and strategic location between the United States, Latin America and Western Europe.

Table VIII

LEADING INTERNATIONAL BANKING CENTERS

RANK<1>	(1988) TOTAL FOREIGN LIABILITIES ($ billion)	MARKET SHARE %	(1982) RANK AT END 1982	MARKET SHARE AT END 1982 %
1 U.K.	910.3	18.5	1	20.5
2 JAPAN	659.4	13.4	8	4.2
3 U.S.A.	584.4	11.9	2	10.7
4 FRANCE	269.8	5.5	4	6.4
5 HONG KONG	247.5	5.0	14	2.3
6 CAYMAN IS<2>	233.3	4.8	6	5.1
7 SWITZERLAND	225.0	4.6	5	5.6
8 SINGAPORE	221.4	4.5	9	3.5
9 LUXEMBOURG	191.5	3.9	7	4.3
10 BELGIUM	176.6	3.6	10	3.3
11 BAHAMAS	158.9	3.2	3	6.3

SOURCE :IMF
<1> Ranked by foreign liabilities at mid-1988
<2> Figures relate to end 1987

with the United States, the United Kingdom and the Kingdom of the Netherlands. While initially a source of strength, the treaties which lapsed in the mid-1980s have caused a severe contraction in financial activities, so that new services will need to be developed if they are to survive in the future.

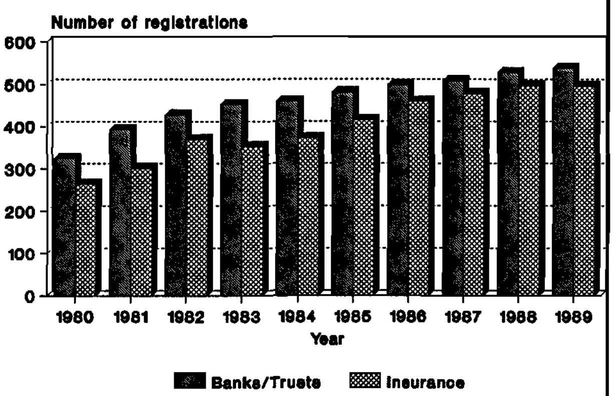
Finance and insurance is the second largest sector in the Cayman Islands economy, accounting for over 12 per cent of GDP and 9.4 per cent of employment in 1988. Tourism, the largest sector, accounts for 10.1 per cent of direct employment. Five hundred and thirty international banking operations, valued at US$250 billion, were registered by the end of 1988 in the Cayman Islands. They employed 1200 persons and provided an annual wage bill of US$11.8 million. This marks a 63 per cent increase in registrations over the decade. But this is not the full extent of financial services provided in the Cayman Islands which has a vibrant insurance industry and provides a locus for international company registration.

The financial sector came to full flower in the 1970s, registrations growing from 30 bank and trust operations at the beginning of the decade to 291 at the end of 1979. The offshore component, which grew from 25 in 1970 to 260 in 1979 conducted, inter-alia, Euro-currency borrowing and lending, bond and floating note issue, taking and placing of deposits, international fiduciary and corporate services and investment and asset management.

Figure 8

Offshore Financial Entities<1>

Cayman Islands



Source: Statistical Abstract, Cayman Is.
<1>Excluding company registrations

A number of factors common to other off-shore tax havens operated in favor of the Cayman Islands. These included confidence in the political, economic, social and administrative arrangements; confidentiality; flexible and accommodatory legislation and banking practices with an accepted supervisory framework; no income taxes; no foreign exchange restrictions, and so on. Initially the growing Euro-dollar market, and later the large flows of petro-dollars created the demand for the services provided in the Caribbean off-shore havens and subsequently capital flight from Latin America became an important factor in its consolidation in the 1980s. By the mid-1980s, a number of these external factors were no longer as pressing, while United States legislation and treaty arrangements with offshore countries were adjusted to erode the benefits of confidentiality and tax-free status put a damper on the growth of such services. Nevertheless, while limited information-sharing to cover criminal operations has been concluded, many of the original domestic advantages remain and have been strengthened as the security of United States banking institutions is called into question.

In the Bahamas, financial services are also estimated to be second in importance only to tourism. Table IX provides a breakdown of the contribution of domestic and offshore financial services to the economy. While there has been some expansion in the domestic portion of financial services, the same cannot be said of the offshore portion which has not managed to keep its global market share, which fell from 6.3 per cent at the end of 1983 to 3.2 per cent in mid-1988. The registration of new financial entities has stagnated since 1985 at just under 400. Total expenditures by offshore enterprises has fallen between 1986-1988, though a slight recovery was evident in 1989. Nevertheless, in 1989 391 banks and trust houses were registered with about US$160 billion in offshore deposits, employing about 850 persons with a wage bill in excess of US$26 million.

Efforts are now underway to stimulate the offshore financial sector with the enactment of the International Business Companies Act and the creation of the Banking and Financial Services Development Board. The prime task of the latter institution is the

Table IX

GROSS ECONOMIC CONTRIBUTION OF BANKS AND TRUST HOUSES IN THE BAHAMAS

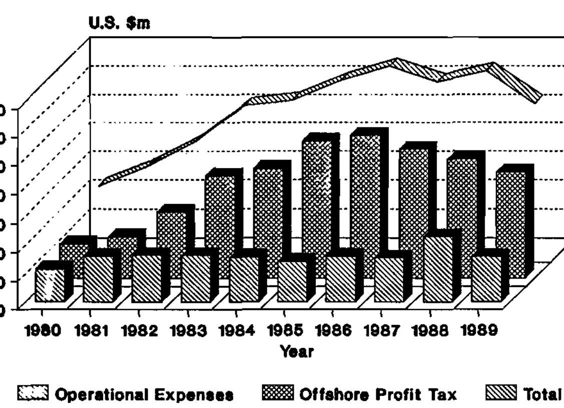
	DOMESTIC					OFFSHORE				
	1985	1986	1987	1988	1989	1985	1986	1987	1988	1989
Total employment	2325	2369	2365	2504	2622	721	859	869	885	846
Bahamians	2205	2246	2326	2407	2540	608	735	744	755	725
Non-Bahamians	120	123	39	97	82	113	124	125	130	121
Total operational Ccsts<1>	78.4	87.1	87.1	93.1	97	47.3	57.4	60.3	59.5	60.1
Salaries	47.6	48.1	50.2	56	58.5	18.2	22.5	24.6	25	26.1
Government fees	2.6	4.3	3.7	4.9	5.1	4.3	5	4.5	7.4	8.6
Staff training	0.6	0.4	0.7	0.9	0.8	0.1	0.2	0.2	0.5	0.2
Other costs	27.6	34.3	32.5	31.3	32.6	24.7	29.7	31	26.6	25.2
Capital expenditure<1>	2.3	5.3	11.4	12.5	11.6	8.3	9.9	2.2	1.7	4.8
TOTAL EXPENDITURE	80.7	92.4	98.5	105.6	108.6	55.6	67.3	62.5	61.2	64.9

Source: Central Bank of the Bahamas
<1> Costs and expenditures are in millions of U.S. dollars.

growth of financial services. A number of other bills are proposed, relating to the Offshore Assets Protection Trust and a Securities Industry Act to provide the legal framework for a Bahamian Stock Exchange and regulate Unit Trusts and Mutual Funds.

A picture of stagnation is also painted for the offshore financial services of the Netherlands Antilles, which had developed as a result of special tax regimes negotiated on behalf of the Antilles and the United States and the United Kingdom. In the mid-1960s, a number of financial entities were established to raise funds on the Euro-dollar market, since United States parent companies were exempt from Withholding Tax provisions, by virtue of a treaty signed with the United States in 1963. While a number of other financial services were performed, the Withholding Tax Treaty provided the core for the development of the offshore services sector, accounting for about 80 per cent of the taxes received from the sector by the Island Government of Curacao.

Figure 9
Offshore Financial Services
Netherlands Antilles

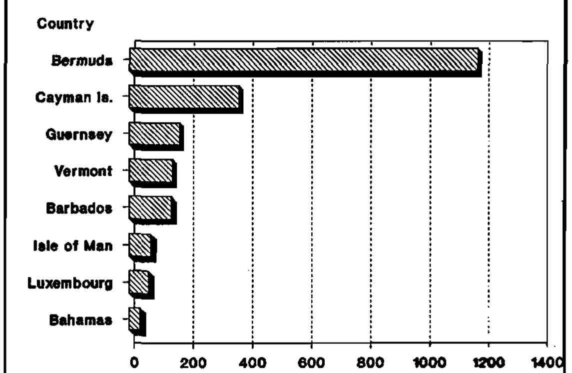


Source: Central Bank

While the sector is not labour-intensive, in 1984 at its peak it employed 250 persons directly, it provided 50 per cent of the total revenues of the Island Government in 1989 despite its decline since 1985. At US$183 million, however, it remains a considerable sum[12].

The stagnation of the offshore financial sector was preordained by the repeal of the Withholding Tax Treaty in 1984 and efforts to build a new range of financial services to compensate will take some time.

Figure 10
Leading Captive Insurance Centers
Number of Registrations



Source: Puerto Rico Business News

Offshore insurance and re-insurance services are also a major source of activities in some Caribbean islands, the leading centers being Bermuda and the Cayman islands, while Barbados and the Bahamas are also ranked in the first 10 in terms of the number of companies registered. The Bahamas, which had been a major center in the 1960s, lost some registrations to Bermuda and the Cayman Islands because of uncompetitive government taxes, but legislation was subsequently enacted in 1983 to realign conditions with its competitors.

Insurance companies have been induced to establish offshore operations, due to the increasing costs of insurance premiums and a reluctance to underwrite certain high risks, such as medical malpractice and environmental pollution suits in some of the major industrial countries. The second incentive for offshore operations relates to interest rate fluctuations; in times of low rates and squeezed profits the lower costs of doing business in offshore centers increases the profitability of the companies.

The benefits derived from offshore insurance and re-insurance operations are similar in origin to other financial services, being fees and other operating expenses, mainly employment. In Bermuda the sector employs 4000 persons and is valued at about $35 billion. In the Cayman Islands gross assets in 1988 were less, at 4.5 billion, but the net retained earnings from the economy were US$380 million or the equivalent of US$15,833 per capita.

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[12] For comparison, in Barbados the proceeds from income and profits taxes and import duties for fiscal year 1988/1989 amounted to US$ 173 million.

Telecommunications services

The assumption of perfect information has underpinned much economic theory and fundamental concepts, such as rational choice and transparency, are dependent upon it. Only relatively recently has this ideal been approached, made possible by innovations in telecommunications. As a consequence, one has seen a rapid increase in global activity, a trend which is dependent upon and at the same time has served to support the exponential growth in telecommunications traffic. New global policies, such as freely floating exchange rates have been made possible by it. As has been the case with other services, technological changes are reducing the lines of demarkation between the various telecommunications services, so that computer services, cable and satellite television, broadcast and telecommunications are being increasingly integrated.

The separation between domestic and international services is also becoming increasingly untenable since the need for national systems to access the systems of others gets greater by the day. The integration of local telecommunications systems into the global network is therefore essential if domestic business is not to be cut off from the information necessary for it to prosper. At the same time, the efficiency and the cost of using the telecommunications network is an important input to the productive process and can, as a result, confer a benefit or a disadvantage to domestic users.

A number of technical issues, the details of which are mostly beyond the scope of this document, have been facing regional policy makers. Briefly stated, they pertain to the following:

a) De-regulation, which has been a factor globally in telecommunications, has created competing firms and modes of transmission and spurred the pace of technological change. Nevertheless, it has increased the complexity in national decision-making with respect to the choice of external networks and means of transmission. It also raises the policy question of whether the benefits of competition can be transferred to the small user communities in the Caribbean. If that is found not to be possible, decisions need to be made to ensure the service does not stagnate with a monopoly, state-controlled or otherwise.

b) Proliferating satellite systems increase the complexity of choice. Elements of cost efficiency, speed, configuration and long-term survival are relevant considerations.

c) Issues relating to remaining in the North American Dial Plan (Area code 809). The costs and benefits have been widely studied yet with increasing usage and, therefore, congestion within the area pressures to change are likely to appear soon.

d) An appropriate amount of media diversity, including a proper mix of satellite cable and microwave systems, is deemed to be desirable. The mix will need to be established and revised from time to time as needs and technologies change.

e) The appropriate choice from the range of telecommunications services available.

In the latter case aside from the well-known services of telephone, telex, facsimile, telegraph, data transfer, private lines and packet switching, a number of relatively new and elaborate services are being introduced.

Some business services provided by INTELSAT include Intelsat Business Services (IBS) INTELNET, and CARIBNET. They provide a range of services including voice, low- and high-speed data transfer, electronic document distribution, electronic funds transfer, facsimile, data distribution and data collection for reservations systems, credit verification services and so on. CARIBNET also supports many of the above-mentioned options focusing primarily on services within the Caribbean and not carried by the public switched telephone networks. The speed with which these services can be integrated into business operations in the Caribbean and, especially the smaller indigenous business operations, will go a far way to determine how quickly they will become globally competitive. In turn this will depend upon how efficiently the services are marketed as well as the cost/benefit ratios perceived by potential users.

Distance teaching within the region, via INTELSAT, linking the various University of the West Indies (UWI) campuses from a hub in Saint Lucia, has developed during the survey period. The system, which includes video and audio links, has proven to be a useful teaching aid and a valuable communications model for the region on which future institutions might be built.

In the field of television, some of the larger islands have indigenous services, often to the exclusion of foreign stations. At the same time, some of the smaller islands lack any Caribbean programming yet have 12 or more non-regional channels available via cable or off-air transmission. A multi-origin multi-destination television service is now available through INTELSAT, to allow the exchange of television programmes on a daily basis. Participants currently include Aruba, Barbados, Curacao, Guyana, Jamaica and Trinidad and Tobago, but other countries are expected to participate eventually.

Culture services

The issues relating to the sale of cultural services are surprisingly similar to those relating to the development and sale of commodities, with added psycho-social and political dimensions which tend to make the debate somewhat more pointed. Indeed, it is these elements which differentiate the sale of culture services from that of other products and services and render policy decisions relating to cultural matters somewhat more complex.

For the purposes of this discussion, culture services relate to those elements of art and artifacts which spring from indigenous cultural forms. Included are the performing arts, printed, audio and visual outputs, painting, sculpture and handicrafts. For completeness, one should recognize those elements derived from history and geographic location which through adaptation have rendered products, including manufactured products, special and unique.

In essence local producers want freedom to gain the benefits to be derived from external markets, while having a relatively well-protected domestic market. Local consumers want variety and high quality, yet questions of identity, familiarity, ethnicity and so on create a fairly strong bias in the broad mass of the population to favour the local product.

At the levels of policy, there is a concern to develop local cultural services and a belief that infant industry policies are necessary for their development. Nevertheless, there is an awareness that considerable gains are to be derived from penetrating larger and more wealthy markets, with the caveat that these gains accrue also to the society as a whole rather than to the individuals alone. With the advent of new communications technologies, national elites fret that national/cultural integrity will disappear. The voices seeing cultural change as an adjunct to development are still somewhat muted, so that on balance policy tends to concentrate on the preservation of culture and the protection of domestic markets against foreign competition.

The outcomes seem, however, to be technologically influenced to a great extent, with developments such as cable/satellite television bringing a range of choice into the home that might ultimately defeat the attempt to regulate the consumption of cultural services. Emphasis should, therefore, be placed on providing the facilities such as training and infrastructure to develop local capabilities for local audiences and products, expand the local market by providing services to visitors to the region and, through the use of the new technologies, tap wider foreign markets.

Professional services

Exports of professional services relate to a number of issues, primarily the rights of professionals to practice their professions abroad, the rights of professionals to telecommunicate their services to clients abroad and to expand the market for their services to visitors. Underlying these issues is the question of the recognition of professional qualifications by the states in which potential clients reside.

Caribbean professionals in a variety of fields are now anxious for opportunities to expand their services abroad and many of them have managed to do so, primarily within the region. The professional services which have been identified in the region and which have a potential for trading include medical, dental, educational, architectural, accounting and engineering.

In the latter case, a distinction can be made between engineering design and construction. Engineering design falls more comfortably into the category of professional services, while construction has a mix of professional, semi-skilled and unskilled workers. Trade in construction services therefore holds potential for the employment of semi-skilled and unskilled workers which currently sell their services informally. While some of this informal trade in services does occur in the region, it tends not to be captured in discussions on services.

Barriers to the trade in professional services come from work permit regulations, designed to protect jobs for nationals, foreign exchange controls and the recognition of professional qualifications, the latter intended to preserve professional standards. For the most part, professional qualifications in the English-speaking Caribbean are mutually recognized and are accepted in the United States, Canada and the United Kingdom, the most promising developed country markets, where Caribbean migrant communities are expected to provide entry to the market.

At the same time that market access is being explored, however, concern is expressed that reciprocal liberalization will disadvantage local professionals in their domestic markets, so that the emphasis seems to be to seek liberalization within the region but limited non-reciprocal market liberalization with the developed countries.

CONCLUSIONS

Some tentative conclusions might be drawn from this review of the services sectors. While it may not be immediately obvious from a focus solely on the structure of G.D.P., Caribbean countries are coming increasingly to depend on services for their economic and social development[13]. A look at regional factor endowments and the contracting global demand for raw materials suggests that this trend will become even more evident by the end of the century.

The trend towards the export of services has taken place in a highly competitive global environment. That services earnings have grown more rapidly for most countries in the region than earnings from goods, in the absence of special protective measures or incentives, suggests a number of factors, including the rapid growth of the trade in services globally. More interestingly for the region, it suggests regional comparative advantage in some of these services, particularly in tourism.

If this is in fact the case, one needs to ensure that the policy environment and regulatory framework do not place impediments in the way of its growth. Secondly, in the face of increasing pressures to liberalize the trade in services, special efforts need to be made quickly, to ensure that the smaller weaker indigenous services, particularly those ancillary to the tourist sector, are not decimated by larger multinational organizations.

Policy environment and regulatory framework

Differential rates of growth of services within the region, lead one to search for the factors most likely to stimulate its rapid growth. The most striking characteristic of the services intensive countries is that they have no obvious agricultural or manufacturing potential. While this might appear to be circular reasoning, the absence of such potential might have served to increase macro-economic policy focus and reduce the incidence of policies designed to bias the movement of factors into traditional agricultural exports, minerals or regionally protected assembly type manufactures for regional consumption. Accordingly, resources flowed naturally into tourism or other foreign exchange earning services capable of sustaining higher standards of living.

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[13] These generalizations apply to a less extent in Belize, Cuba, Guyana, Puerto Rico and Trinidad and Tobago, which clearly have a more generously endowed natural resource base, than to the other islands in the region.

This contention is supported by a number of factors. On the one hand is the strong correlation between the intensity in services and per capita G.D.P. Secondly, structural adjustment policies which have as an objective the reversal of traditional distortions, have served to stimulate the development of services exports in countries, such as the Dominican Republic and most recently in Jamaica. The Dominican Republic, predominantly sugar and mineral exporting in the 1970s, has recorded the third fastest growth in tourism in the region in the 1980s, at an annual average of 14.5 percent. This rate of growth is exceeded only by some small island destinations, starting virtually from scratch. The other main growth area in the Dominican Republic might be regarded as a quasi-service, the offshore assembly operations for export.

The regulatory framework in place in various countries, therefore, seems to have had a significant impact upon the rate of growth in services. Where regulatory factors were too rigid, practitioners in the service sectors were inhibited from responding to new needs as they arose. This was true in the region and globally. In financial services, many developed country banks established branches in areas such as the Bahamas or Cayman Islands to escape the regulations which inhibited the growth of measures to service the Euro-bond market.

Similarly, they did not move to some other regional destinations for the same reasons, often because they were prohibited from doing so by regulations reserving the sector for nationals or by regulations prohibiting the free flow of capital. Where regulations prohibit, it takes some time for regulators to discern a trend and to devise new regulations to foster it, but early entry into a new market segment confers a major advantage. Other areas have moved belatedly into the field of tax free financial services, including New York, but this seems to have had relatively little adverse impact on the established areas and recently enacted legislation in other Caribbean markets to confer offshore status have similarly had no significant impact.

In some countries the protected environment for local financial institutions together with macro-economic policies have limited the scope of the financial sector to innovate and adopt facilities which could improve the productive sectors.

In the tourism sector, the regulatory framework has been relatively light. Private actors have been given a fairly free hand to run the industry so that a mix of local and foreign operators has developed, the latter helping to channel new technological developments and marketing contacts to the benefit of the local industry. Yet there are examples where domestic policies have severely damaged the industry, for instance, where import controls have denied it access to necessary inputs.

Some Caribbean destinations are also currently in danger of trying to extract too much from their tourism industries in taxation, with the effect that profitability is contracting, maintenance is declining and the attractiveness as a location for future investors, and for visitors, is declining. This helps to explain the growth and stagnation of various Caribbean destinations during the last 10 years, and will become more apparent in the future as the travel industry matures and becomes more competitive.

In entertainment, work permit policies to limit the freedom of movement of performers has at times limited the quality of live entertainment available to local audiences and also limited the opportunities of local performers to perform abroad. Even where work permits are forthcoming, foreign exchange regulations have severely increased the aggravation and the risk of such employment. Similar policies have limited the prospects of other professionals wishing to export their services.

Tariff policies in the telecommunications sector which has often used international transactions to subsidize local traffic, while possibly having some welfare benefits, might have the unintended consequence of limiting the adoption of innovations conducive to modernization and export-oriented development. Similarly, if national monopolies in the field of telecommunications continue to be the norm, a regulatory framework will need to be fashioned to guard against lethargy in adopting new technologies, prevent internal inefficiency in the enterprises and limit the monopoly rents which accrue to them.

The above is not intended to advance a simplistic argument for de-regulation, or for the absence of government involvement in services activities. It is rather for a regime of enabling, rather than inhibiting, regulation. For financial services to flourish, depositors need to be assured that their funds will be efficiently and securely handled. Banking practices need to be rigorous and well regulated. In all the services, good basic infrastructure is essential, whether it be good roads, airline facilities, potable water, secure electricity, good training facilities or good telecommunications. But as productive activities such services can sustain a level of infrastructure, from which locals can benefit, which might be beyond the capacity of the country in their absence.

Another dilemma faced by the policy maker derives from the infant industry argument. That is, to provide sufficient free space in the local market to allow the growth of indigenous services but not so much protection as to inhibit growth thereafter. This is particularly true of regulations which limit the efficiency of internationally traded services. Regulations which restrict the capacity of sectors to adjust or to take advantage of emerging opportunities will also inhibit their long term growth.

With respect to resource allocation the process of growth is speeded up when factors are used most efficiently. If the services sectors are the area of comparative advantage in the region, a policy framework which does not inhibit the flow of factors into them will accelerate the process of growth, though at the probable risk of greater specialization on fewer activities.

Adaptation to global changes

Many fast growth global activities are cauldrons of ferment and change. Therein lies one of the chief arguments against the encouragement of services in the region, indeed against all global tradables, that is, the belief that they are volatile and insecure sources of income. Volatility might derive from three sources. The first arises from socio-political factors and relate to services which require the product to be consumed at the locus of production, such as tourism or educational or health services. In such cases the local environment is a major enhancing quality of the product. Accordingly, if the environment changes to one of hostility, instability or environmental deterioration, the quality and, therefore, the price and/or the demand for the product declines. This is perceived by some to be a major potential source of vulnerability.

The second source relates to the fluctuation in earnings of a fairly homogeneous product, determined mainly by external economic factors. Nevertheless, external factors of an institutional nature are also of importance, such as developments in the Uruguay Round of the GATT, where the conditions under which products are customarily traded will be subject to change. In this instance, if the developments in the GATT are realized, markets in services which had been protected might be quickly opened up to global competition. Finally, volatility can also spring from evolution in the cycle of the product traded as continuous rounds of innovation are applied to modify and differentiate it.

Fluctuating earnings have bedeviled all of the region's traded commodities. An index of the major exports of commodities and services shows tourism to be in a stable upward trend. This has been due in part to the size of the global market and its expansion over the survey period. But the regional share of the global market seems also to have increased slightly.

At the same time the product itself is not static, it is evolving and differentiating and it is combining with a number of other services to change its configuration. This is, at one and the same time, a source of risk and of opportunity. But attempts to isolate the domestic industry from such trends will not only deny it the opportunities but also render it static and obsolescent.

If it is an internationally traded product it will become an undifferentiated homogeneous product in which the value added will be low and ultimately fall prey to the most cost effective in a mass market. If it is a producer service the quality of the input will fall behind to the detriment of other areas of the economy as a whole. This evolution is in accordance with the morphology of any other product cycle. The alternative is to become a well-informed and integral part of the evolving market and, where possible, to incorporate local cultural influences in a special way to create a unique diversified product. This has already been documented as happening for some tourism enterprises in the Caribbean[14].

Adaptation of this type is particularly well-suited to components of the tourism product, such as lodging and furnishings, cuisine and entertainment and it is in such areas that the industry can become the most diversified and profitable. It is an obvious factor in the entertainment industry where indigenous cultural inputs can help to distinguish performers.

In a number of other areas such as car and other recreational vehicle rentals, travel reservations, airline services and so on where the service is fairly standardized and familiar price and efficiency criteria are paramount and local firms will need to be abreast of new developments if they are not to succumb to the large multinationals in the field.

Fairly standardized services are also provided in the area of professional services, by medical, engineering, accounting and other such professionals. Normally, a strong presence in the market where the service is to be provided is necessary for effective performance. The quest for larger, more affluent markets is no less relevant for the trade in services than for the trade in goods. Lack of access to the larger markets constrains the development of the service and has no doubt provided an incentive for skilled persons to locate abroad. The alternative might be to induce a portion of that market to come for the service. An example of this might be medical/dental/recuperative services, linked to a regional vacation thus providing greater spinoffs to the local economy and sustaining a larger body of medical expertise than might be justified for a smaller market. Similar concepts might also apply for real estate or educational services. Caribbean communities abroad can be used to provide nodes from which a presence in the developed country market can grow. This applies to areas, such as medical and dental services and architectural/building and real estate services.

More generally, strong producers services help to increase international competitiveness, integrate more of the population into the productive process and bring new technologies into

[14] Poon, Auliana: "Flexible specialization and small size: The case for Caribbean tourism", May 1989.

productive activities. In so doing they help to attract investment, both foreign and local.

As has already been noted, the countries having the fastest growth in services have, in general, the most open economies and a regulatory regime that is facilitaitve rather then restrictive. Opening the market will create few shocks for such countries. For those countries which have a more comprehensive protective regime, it may be that many small uncompetitive operators have been able to survive. The challenge will be to manage the de-regulation process in such a manner as to enable such operators to compete more effectively for the future.

This applies to small hotels as well as to small tour operators, rental car firms and so on. Small hotels in the region tend to be at the lower end of the market[15] although they hold the best potential to create a culturally dense diversified product. But they currently lack managerial skills and standards and access to international reservations facilities, so that room occupancy rates are low. Accordingly, they are less profitable and often suffer from a lack of investment in maintenance and modernization.

In the area of producers services as with export services, changes are likely to be quite severe as markets are liberalized. If some of the smaller indigenous enterprises are to survive, ways will need to be found to quickly upgrade their performance through the infusion of capital, skills and new technologies. Where these inputs can be provided from local sources, mainly by the financial institutions, efforts will be needed to stimulate such action. However, if it is true that the financial institutions are themselves weak in these areas, then perhaps the most viable option open to the weaker indigenous services enterprises could be the establishment of joint venture operations with foreign partners.

Services industries, which are ultimately the sale of <u>human services</u>, place a greater premium on human qualities and skills than other types of activities. Their tradability will depend upon the quality and uniqueness of the service offered, while producer services are also dependent on the human capabilities they contain. This requires an emphasis on human skills and qualities, including the cultural component, which is the one most likely to create a differentiated product. For the longer-term development of services, greater emphasis will need to be placed on appropriate skills training, which will begin in schools, be augmented in tertiary institutions and completed at work. For while technologies are transmitted through machines, a fairly high level of skill is needed to understand, select and operate the technologies as they develop and confer competitive power on their users.

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[15] Although room rates are probably not significantly lower than the mass market hotels.