CHAPTER 7

The Caribbean in the World Economy

The prospects for Caribbean countries depend on the evolution of their terms of trade, on the way economic fluctuations in industrial economies affect their export markets, on the trends in international investment flows, on the availability of new free trade opportunities, on the proliferation of trade restrictions for particular products and on the terms of borrowing. For heavily indebted countries, the future also hangs on the extent of debt relief that they may obtain. These issues are explored in this chapter. In addition we ask how prospects might be enhanced by closer regional co-operation.

Debt and Debt Service

Countries may be distinguished according to the burden of debt they carry. For some – Guyana, for instance – debt service obligations are close to the equivalent of exports of goods and services, and the country has no hope of stabilising the external accounts unless significantly more debt relief is offered. Other countries such as the Dominican Republic and Jamaica will need to pay so much in debt service for the next decade that there may be little net foreign exchange for purchasing the inputs needed to raise output and incomes. A third group of countries – including Barbados and Trinidad and Tobago – has heavy debt service obligations, but could conceivably stabilise the external accounts and regenerate growth with the existing debt structure. In the fourth category are a large number of smaller Caribbean countries which have no debt service problem. Jamaica is unusual among highly indebted countries in having over half of its debt with international financial institutions, much of it with maturities of five to seven years, and no prospect of rescheduling.

The Mexican debt relief package is seen as the prototype for reschedulings and renegotiations with other countries. A major disappointment is that the arrangement offers little new financing, without which the prospects for growth are not good. A similar package would offer limited help to countries like Jamaica where the debt to international financial institutions is substantial. Real interest rates have been reduced in the Mexican arrangements, and the interest rate has been fixed. Heavily indebted countries need interest rate concessions that will bring the rate down to the rate of increase of export prices, as a first step; it remains to be seen whether this can be achieved.

Even with debt relief on the Mexican model net transfer will be made from heavily indebted countries to international lending institutions for several years. Proposals to agree on minimum terms for debt relief packages for Latin American and Caribbean debtors (SELA, 1989) and for new long term debt instruments to refinance existing debt of middle-income countries have elicited no positive response.

Foreign Investment and New Borrowing

International firms, and particularly the US based companies to whom the Caribbean looks to for most investment flows, seem less inclined to invest overseas than was the case in the 1960s. The 1970s saw the beginnings of a retreat from the Caribbean by US banks, manufacturers and hoteliers, many of whom had shown great enthusiasm for expansion in the area in the previous decade. Although there was something of a resurgence of interest in the tourism sector in the late 1980s, investment in all other areas remains very sluggish.

Economists and government administrations hope that foreign investment will return in due course, if confidence is built up through economic and political stability over several years. All share an apprehension that the period of waiting may be so long that the momentum of economic change is lost. Once confidence does return, foreign investment in the Caribbean should not be much affected by international business cycles, since the region's demands on capital markets are so small, relative to the international supply of finance. For just this reason, the new-found investor interest in Eastern Europe does not further reduce the chances of new investment in the Caribbean. In an effort to overcome the inertia of a long waiting period for new investment this study recommends careful export promotion strategies, designed to tap into targeted sources of potential investment.

The amount of new foreign debt that countries should seek may be derived from each country's economic strategy. It depends on the projected growth in exports of goods and services, the return on projects funded by foreign inflows, the proportion of that return that is received in foreign exchange, the maturity of the new loans, the interest rates, the proportion of equity in new capital inflows, expected rates of inflation, and existing debt service obligations. In many cases the target for new borrowing will be lower than will be needed to allow renewed growth, unless existing loans may be rescheduled with sufficiently long maturities and at real interest rates which are low enough to leave room for adequate new borrowing.

International Trade and Financial Agreements

International arrangements continue to play an important role in Caribbean trade and finance. They include negotiated agreements between states – the Lomé Agreement between the EC and a grouping of African, Caribbean and Pacific basin countries and the Caribcan agreement between the English-speaking Caribbean and Canada – unilateral provisions by an industrial country – the US Caribbean Basin Initiative, the Enterprise of the Americas Initiative and US sugar quotas – and intra-firm arrangements between local and overseas branches of multinational companies. The provision of the Lomé convention which has so far been most remunerative for the Caribbean is its sugar protocol, which makes provision for the supply of a predetermined amount of sugar at prices linked to the subsidised price paid to European sugar beet farmers. This has sustained commercial agriculture in some countries, and during the 1980s provided perhaps 5% of the foreign exchange earned by countries that benefited. The convention makes members eligible for long term developmental loans for infrastructure, social services and support services for private enterprise. An export stabilisation fund has not been used by Caribbean members, but they have received relief funding in the wake of natural disasters. The convention allows duty free entry to the EC for non-traditional exports, and there have been efforts, none really successful so far, to establish an export trade in vegetables, flowers and garments. The provisions of the fourth convention of Lomé will continue beyond the European single market in 1992. (The English and Dutch speaking Caribbean are members of Lomé; the Dominican Republic joined in 1991.)

The Caribbean Basin Initiative, launched in 1983, is effectively an enhancement of opportunities for free access to US markets which had been available to the Caribbean – and many other small countries – for many years, under specific sections of the US tariff code and GATT concessions for small developing countries (the Generalised System of Preferences, GSP). The immediate potential for enhancing trade through the CBI was limited by the exclusion of garments, the region's largest segment of non-traditional exports, and by the failure to include a sugar quota as part of the arrangement. The CBI helped to increase US investor awareness of the Caribbean, but that could be expected to yield only modest investment flows at a time when the US investor was increasingly looking inward. Since there were no provisions to increase the returns on the activities where the Caribbean already had productive capacity, the overall impact of the Initiative has not been very great. Nevertheless, the Initiative is important because it provides some assurance of a continuity of the free trade provisions, a factor which should affect the long term outlook of investors and assist the efforts which the Caribbean makes to promote new exports. The CBI has not swept away the non-tariff barriers which have proved a major obstacle to the introduction of new exports. (Guyana was the only Caribbean country not included in the list of CBI beneficiaries; it was added in 1989.)

The phasing out of the US sugar quota (a process which is not yet complete) has been a most serious reversal for the Caribbean, and has significantly reduced growth potential in the Dominican Republic in particular. The elimination of the quota is not necessarily a step in the direction of greater efficiency (though the quota price was so much above the "market" price that its demise was inevitable); most world sugar is not sold on free markets, and the "market" price bears no consistent relationship to supply, demand and stocks. The elimination of the quota, if accompanied by an abandonment of the domestic sugar price support (the outcome depends on the strength of political lobbies for sugar and its substitutes and is impossible to predict), may well cause such a contraction in supply as to send the "market" price soaring and create another round of instability, triggered by producers' attempts to cash in on the bonanza. Managing a quota system with flexible prices might have produced a more stable outcome.

In July of 1990 President Bush of the United States announced the Enterprise of the Americas Initiative (EAI), a wide-ranging collection of measures affecting US economic relationships with countries of the Western Hemisphere. The EAI envisages steps towards free trade between the US and other countries of the hemisphere, negotiated on varying timetables with countries or groups of countries. This will be a lengthy process with somewhat indeterminate outcomes depending on Congressional approval of negotiated agreements. A small amount of money is to be channelled to the Inter-American Development Bank to provide technical assistance for countries involved in a reform of their economic institutions. The package includes some relief on official debt owed to the US by hemispheric countries including repayment in domestic currencies and small debt for nature swaps.

The principal effect of the EAI is to intensify competition from Latin American countries for Caribbean exports to the US. Low cost suppliers of labour intensive products from Latin America, who may not now have access comparable to that enjoyed under the Caribbean Basin Initiative, pose a potential threat to some Caribbean exporters. The EAI offers no trade gains for the Caribbean, which already has free trade access under the CBI. Free trade agreements would not provide preferential prices for Caribbean sugar which is what Caribbean sugar producers require. Caribbean textiles, which are not eligible under CBI, would gain free access but they would have difficulty in meeting the competition from Latin America.

Private and public sector representatives from the US and Latin American and Caribbean countries are to form committees to deal with non-tariff barriers, which have been a critical difficulty for exporters under the CBI. It remains to be seen whether these committees can counter US pressure groups which find ingenious ways to exclude competitive exports.

Jamaica is the only Caribbean country likely to benefit significantly from debt relief under the EAI. That relief will not alleviate Jamaica's problems very much because of the predominance of debt owed to the international financial institutions.

The Caribbean is unlikely to get any additional funds for human resource development from the new IDB-administered Fund. The resources available to the Fund for the whole of the hemisphere are too little and the technical assistance which the Caribbean requires for its remaining institutional reforms is, in any case, negligible.

The Caribbean-Canadian agreement (Caribcan) has not been of much importance to date. The main items of interest to the Caribbean are by-products of sugar, which face standards regulations, licensing requirements and other non-tariff barriers designed to inhibit entry into the market.

The emergence of large trading blocs as a result of the further integration of Europe and the US-Canada free trade pact should not affect the prospects for the Caribbean in any significant way. No changes are envisioned for traditional exports; for non-traditionals the Caribbean will need to bend its full energies to securing firm niches in one or two markets where demand is already far in excess of the capacity they might aspire to. There is apprehension that the less developed members of the EC – Greece, Portugal and Spain – might compete for the non-traditional markets that the Caribbean aspires to supply, but these fears seem groundless when one recalls the difference in potential supply from the Caribbean and such countries. The Caribbean's best hope is highly differentiated segments of the market, where product characteristics maintain a loyal clientele. Fears have also been expressed about the end of quotas for sugar sales to the EC, but the greater threat to the sugar industry is a failure to rationalise production, increase productivity and reduce unit costs so as to remain competitive with new low cost suppliers and substitute products.

The Caribbean has a vital interest in the controversial issues of traded services and the agreements that will be built into the GATT to accommodate them. Tourism is the main traded service that Caribbean countries now provide. Although some private firms are interested in providing more non-tourism services to industrial countries from Caribbean locations, there is currently a large outflow on the non-tourism services accounts in all Caribbean countries except the Bahamas. (The other territories with net inflows are British dependencies, Bermuda and the Cayman Islands.) The outflows are for consultancy fees, management services and professional services. It is not yet clear what internationally agreed rules on travel might help the Caribbean to counter this by providing the services of skilled and semi-skilled workers to industrialised countries.

Export Markets

Tourism remains the most vigorous export sector in most Caribbean countries in 1991 even though the Gulf War and recession in the US depressed Caribbean tourism in the first half of the year. More than half of the region's visitors are from the US, with most of the remainder from Canada and Europe. Tourism is highly sensitive to economic cycles and it suffers from a tendency for over-expansion during times of rapid growth. There is evidence of this in the Dominican Republic and the Leeward Islands of the east Caribbean, where capacity has risen very sharply since the mid-1980s. The impact of the slowdown in tourist demand may be compounded by the curtailing of hotel construction and other private tourist development. The current rate of tourist expansion may be above the trend rate, and rather sharp fluctuations in activity may be expected. The

Caribbean may defend against a possible downturn to some extent by creating a product that is differentiated and by offering a range of services ancillary to tourism. Both strategies are yet in their infancy.

Contrary to uninformed opinion, sugarcane agriculture is an attractive export activity. The technology is well proven, and it makes use of quite sophisticated processes, which are subject to continuous evolution and improvement. The end-products are versatile: besides sugar in a variety of qualities and specifications, the product may be converted to beverages, industrial raw materials, or fuel, with building materials, animal feeds and other by-products created in the process. There is a growing world demand for sugar, though supply is also on the increase because of high prices on the protected markets of industrial countries. At more realistic prices demand might be even higher, and high cost supply would not command such a large share of the market. Sugar may be stored for long periods, and it is sold worldwide, in markets where futures contracts and hedging provide some insurance against price instability. There are many unrealised possibilities for aggressive new strategies for sugarcane agriculture, but few are being implemented in the Caribbean, where the industry is contracting everywhere because of neglect and unimaginative leadership. There are unexploited markets in North America and Europe for a variety of by-products, but there are non-tariff barriers to be overcome, including discriminatory regulations on alcoholic beverages and defensive strategies by existing firms in the target markets. Initiatives are needed to explore expanded markets for what are now minor products, such as molasses and ethanol. As markets change, and there is less protection for raw sugar, a more diversified mix of end-products is required.

Other agricultural exports are of minor importance and their supply has been erratic, plagued by uncertain delivery times and poor quality control. They include bananas, coffee, cocoa and rice, all of which have been exported for decades. Since about 1970 efforts have been made to develop significant exports of fruit, vegetables, fish, flowers and foliage. Initiatives are under way to resolve the quality and delivery problems for some products – for example, the high quality Jamaican coffees and bananas from Jamaica and the Lesser Antilles – but there is no prospect that non-sugar agriculture will be a substantial export (earning as much as 5% of foreign exchange, say) by the year 2000 in any Caribbean country.

The demand for bauxite and alumina contracted from the mid-1970s to the mid-1980s, first because the high price of oil raised the prices of aluminium, whose production is very energy-intensive. Subsequently, high performance lightweight plastics cut into the market for strong light industrial material. The demand may now have stabilised, and Jamaica, the Caribbean's leading producer, may succeed in holding production levels at the average for the 1980s, but it is doubtful that the other significant producers whose output has declined or who have gone out of production altogether – the DR, Haiti, Guyana and Suriname – will be able to regain much of their former market share.

Trinidad and Tobago is the Caribbean's only oil exporter (not including Venezuela, which is sometimes considered a Caribbean country, but is not included in this survey), and Barbados is the only other oil producer in the region. Both are experiencing declining production as existing wells mature and exploration lags or fails to yield attractive results. Trinidad and Tobago depends on the stabilising of oil prices in the vicinity of $18 per barrel in order to balance the external accounts with the austerity programme which has been put in place. The oil price is less crucial to the Barbados outcome. Other countries' external accounts could deteriorate badly if oil prices rose, particularly those which already have unmanageable debt burdens.

Manufactured exports from the Caribbean are mainly labour intensive products assembled from imported raw materials, with the exception of energy-based products which Trinidad and Tobago began to export in the 1980s. Manufactured exports have grown significantly in countries where income per head has fallen (Jamaica and the DR), and they have declined in Barbados, where output per head has risen. The prospects for expansion depend more on creative marketing than they do on the size of the market, which can absorb any volume the Caribbean can supply at competitive prices. The low-wage high-volume production is constantly under threat from countries with lower living standards and lower wage costs. Assembly plants in the Caribbean which do not attempt to produce a differentiated product or to address a particular segment of the market, find that they are less and less competitive as their own workers' standards of living rise relative to those of competing countries. The immediate prospects for expansion of labour intensive production in the free trade zones of Jamaica and the DR are favourable, because growth must be sustained for several years in order to restore recent losses in living standards. However, if the long term goals of a revived economy and steady growth are attained, the export manufacturers will need to transform their output or their technology in order to remain competitive.

The prospects for Trinidad and Tobago's steel, fertiliser and other energy-based exports appear to be brighter than was once feared. The use of recent technology seems to have given the firms something of an advantage in competitive pricing. However, the situation is far from clear, and competitors in the US maintain that selling prices for some products are being held below cost, and have succeeded on occasion in blocking shipments from Trinidad and Tobago. (That says nothing about the competitiveness of the Trinidadian product because US anti-dumping legislation is notoriously inequitable.)

With the advent of international data communications the Caribbean has entered the market to supply data entry and other information services to the US. The industry uses semi-skilled labour, requiring a level of education one step above the assembly firms, but in the long run they will face the same dilemma: if income per head revives and there is no worsening of income distribution, real wage increases will divert this activity to less successful countries. The scope for continuing growth is quite considerable in the meantime. Knowledge-intensive information services would provide a more secure long term basis for expansion, but they require technical, professional and business skills which Caribbean countries are yet to display in sufficient quantity.

The march of technology has opened new export possibilities by bringing information services into the category of tradables. It has also introduced a new threat to existing comparative advantage: the replacement of some labour-intensive processes by new technologies which use high quality labour more productively. The Caribbean will need to develop a capability to move in step with technological developments, in order to maintain its relative position.

To summarise the trade prospects, the Caribbean faces no significant tariff barriers for its exports, except for sugar and its by-products. Non-tariff barriers are a stumbling block for many lines of activity, including such diverse items as steel, fertilisers, ethanol, fruit and vegetables, and business services. Inadequate marketing is the major inhibitor; many potential avenues remain unexplored, and existing markets are not sufficiently insulated by means of product differentiation. There are also supply problems in many activities, caused by failures of quality control, inadequate planning and forecasting, lack of strategies to cope with contingencies, and failure to take account of technical change.

Migration and Remittances

In the 20th century significant migrations from the Caribbean – to Panama for the building of the canal, to Britain and to the US – have had the effects of relieving job pressure, providing remittances and enriching the pool of human resources with the skills and experience of returning migrants. The current economic crisis in the Caribbean has generated a smaller but nonetheless significant wave of emigration. Migrants' remittances are second to tourism as a source of foreign exchange in the Dominican Republic, and they may well be the principal source of foreign exchange in Guyana and Haiti, where there are no reliable data because funds are transferred via underground markets, and through transactions in kind. The numbers leaving the Caribbean have been too small to affect the job market; migrants have had to resort to sometimes desperate stratagems to get around strict quotas imposed on the unskilled by receiving countries. Migration has lowered efficiencies in some countries, because skilled workers are more successful in finding migration outlets. A trickle of returning migrants to the more economically successful countries has made a disproportionate contribution to entrepreneurship. The prospects are that emigration will continue to provide a small safety valve for weak economies, mainly through the remittances sent back, which relieve the excess demand for foreign exchange somewhat.

Regional Integration

The Caribbean Economic Community (Caricom) agreement provides a framework for the English-speaking Caribbean to co-ordinate efforts to accelerate export promotion and to use scarce skills most effectively. Joint negotiation has proved effective in concluding trade agreements such as the Lomé convention (and the sugar agreements which preceded it). The Caricom Secretariat has co-ordinated the regional approach to negotiations on traded services in the Uruguay Round, but little progress has been made with joint initiatives in debt restructuring and export marketing.

The Caricom treaty makes provision for joint production and marketing of products between firms in different member countries, but restrictions on capital flows within the region have inhibited such co-operation. There is growing recognition of the importance of freer intraregional movement of capital and skilled labour to take fullest advantage of the available resources. A number of regional institutions have been set up to facilitate this interaction – the Caribbean Development Bank, the Caricom Secretariat, the Caribbean Association of Industry and Commerce and the University of the West Indies – but free movement of factors is not yet a reality.

Caricom countries have focussed heavily on internal free trade, but with small regional markets this never offered much scope for growth, though it is a boon to small business. Currency unification has attracted attention, paradoxically as countries of the region moved further away from achieving unified exchange rates, but unification must follow the stabilisation of exchange rates. The policies which will serve to stabilise the exchange rate are precisely those needed for currency unification.

The Prospects

The prospects for heavily indebted countries are discouraging, under the circumstances of the current strategy for debt relief. The debt service burden remains too large to release resources – foreign exchange in particular – for the purpose of new investment and renewed growth, for at least a decade. In most other respects the prospects for the Caribbean depend on the region's ability to set initiatives in train, to a much greater extent than they do on the state of world markets. Investment remains sluggish, and there seems little likelihood that foreign investors will lead the way. A well designed investment strategy, focussed on targets for export improvement, seems the way forward; even those who are sceptical about incentives and investment policies have no alternative to offer. The current international marketing arrangements for traditional exports are satisfactory for the time being. Again, the onus is on the Caribbean to develop strategies to cope with changes in these arrangements, well in advance. There are opportunities for free trade in almost all non-traditional goods and services that the Caribbean has considered exporting; the region must mobilise more effectively to overcome the non-tariff barriers that stand in the way, or that materialise from unexpected quarters just when prospects for new markets appear most promising. By deepening the process of functional integration in the region all countries' abilities to improve on their returns to scarce human capital may be enhanced.