

NURTURING INSTITUTIONS FOR A RESILIENT CARIBBEAN

Editors:

Diether W. Beuermann and Moisés J. Schwartz



Institutions in the Caribbean have played a critical role in being able to enhance our democracy and to provide a platform for economic growth. They have protected the interests of those least capable of protecting themselves. It is vital that we work each day to ensure that our institutions continue to play this role without themselves becoming obsessively distracted with their own sustainability at the expense of achieving their core mission.

—Mia Mottley
Prime Minister of Barbados

This book is a wonderful starting point for anybody interested in understanding the economic problems of the Caribbean and how broad-based prosperity can be built in the region.

—Daron Acemoglu, Charles P. Kindleberger
Professor of Applied Economics, Massachusetts Institute of Technology;
coauthor, *Why Nations Fail: The Origins of Power, Prosperity, and Poverty*

The Caribbean has been a crucible for every institutional experiment of the modern world, from plantation slavery and globalization to building states and democracy from the ashes of extractive colonialism. It's a story of remarkable successes and frustrating failures and this fascinating book shows that there is so much we can learn from a rich set of natural experiments.

—James A. Robinson, The Reverend Dr. Richard L. Pearson
Professor of Global Conflict, University of Chicago;
coauthor, *Why Nations Fail: The Origins of Power, Prosperity, and Poverty*

This volume reflects the high level of scholarship that has made the IDB the respect institution it is. The Bank should be commended for investing in research dedicated to assessing the role of institutions in the growth and development of the small developing countries of the Caribbean. This is a very useful work which will be of great importance to the region as well as to other developing countries. Though focused on the Caribbean the book is a timely reminder to all developing countries that institutions matter for sustained growth and stability.

—Ewart Williams
Former Governor of the Central Bank of Trinidad and Tobago

Socio-economic and political institutions play a major role in development. This excellent volume brings together a group of prominent scholars and practitioners to analyze how these institutions have affected development in six Caribbean nations. The result is a theoretically informed, empirically rich exploration of the fascinating problems and prospects of these societies. This book will be of natural interest to those concerned about the Caribbean; it also makes fascinating reading for anyone interested in the political economy of development more generally.

—Jeffry Frieden
Professor of Government, Harvard University;
author, *Currency Politics: The Political Economy of Exchange Rate Policy*

This book answers two fundamental questions that emerge from influential scholarship. History and institutions matter for development, and particularly in the Caribbean. But which institutions? And reforms to accelerate development must take into account the historical and institutional context. But how? This book sheds new light on the complex interplay of colonial and post-colonial experience, political institutions and cultural norms, and the economic institutions that directly steer economic development. It offers new strategies that address the development challenges of the Caribbean and makes a fundamental contribution to our understanding of the role of institutions in development.

—Philip Keefer
Principal Economic Advisor, Institutions for Development,
Inter-American Development Bank

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Foreword

For the people of the Caribbean, the dream of the future looks different from the present: modern, digital economies where innovation thrives, and a climate-smart and resilient region where people are safe, productive, and happy. This is not necessarily a dream of a distant future: it is entirely possible by 2040. However, realizing this dream world of 2040 requires action. Progress in spurts, which has characterized the history of the Caribbean, can be attributed to myriad factors. Some factors are short-lived and have a limited impact on people. But arguably, no factor is more important than institutions. We know from evidence that institutions have a profound and enduring impact on the success of countries—think, for example, of slavery, colonization, and independence—given their role in determining long-term prospects for economic growth, development, and well-being.

Yet, while institutions matter greatly, a comprehensive review of the quality and impact of institutions in the Caribbean has long been neglected—until now. This volume, *Nurturing Institutions for a Resilient Caribbean*, provides new insights on institutions in the Caribbean for the 21st century. The book explores the historical development and status of political and economic institutions in the region. The Caribbean institutional setting is analyzed and compared with other regions and against international best practices. The emphasis is on institutions related to the rule of law (property rights, the judiciary, and the police), political and economic institutions (governance, central banks, and fiscal management), and institutions associated with the development of human capital (education and health).

The objective is to identify areas in need of improvement that could drive the 2040 vision of a sustainable and resilient Caribbean. There is a lot we can learn from the theory and empirical work on institutions in general. This volume has gleaned from that body of work the knowledge and

lessons that are relevant for the Caribbean to realize a better future. Both the classical knowledge and new findings in the institutional literature are presented here thanks to the work of global and regional specialists in the field, as well as our own team at the Inter-American Development Bank.

Improving lives in the Caribbean starts by nurturing stronger and better institutions. We cannot leave this process to chance. Therefore, we hope that the scope and richness of the analysis here will prompt our readers, policymakers, and Caribbean specialists to re-imagine institutions for the future and move to make them a reality.

Therese Turner-Jones

*General Manager, Caribbean Country Department
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Acknowledgements

The Inter-American Development Bank's Caribbean Country Department (CCB) is responsible for the development of the IDB's country strategies and programming, and for the portfolio management of its operations in The Bahamas, Barbados, Guyana, Jamaica, Suriname, and Trinidad and Tobago. Among its main activities, the department supports the regional and country-specific projects of CCB countries through productive dialogue with the region's stakeholders.

As part of this effort, the CCB undertook the exercise to explore the historical development and status of political and economic institutions in the Caribbean. The objective was to identify institutional areas in need of improvement that could facilitate a more sustainable development path in the region. Theoretical and empirical studies offer a vast amount of knowledge on institutions that can take CCB countries a step forward in their quest for a better future. This book aims at providing some of this collective and cumulative know-how.

Such an ambitious effort would not have been possible without the support of our colleagues at the CCB who work hard every day to improve lives in the Caribbean. Our most sincere gratitude goes to Therese Turner-Jones, General Manager of CCB, for her continuous and invaluable support for the project, as well as for her numerous comments and suggestions. Special thanks also go to CCB Country Office economists, who were able to collect a huge amount of information on their respective economies. The information gathered served as key raw material for the analysis presented in this book.

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The views expressed in this volume are those of the editors and authors of the corresponding chapters and do not necessarily reflect the views of the Inter-American Development Bank or its Board of Executive Directors.

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Jose Fajgenbaum is a Partner in the Centennial Group and Director of Centennial Group Latin America. Prior to joining the Centennial Group, he worked at the International Monetary Fund (IMF) for 30 years, where he advanced from Economist to Deputy Director of various departments. In addition to helping define and supervise these departments' work, he led missions to surveillance countries such as Brazil, Israel, Russia, and South Africa, as well as to countries supported by the IMF, such as Brazil in the early 1990s, the Dominican Republic, Kenya, Malawi, Peru, and Trinidad and Tobago. His expertise is on a wide range of development and macroeconomic issues. He holds a B.A. from the National University of Cuyo, a M.A. in Economics from the University of Chicago, and completed his Doctoral studies in Economics at the University of Chicago.

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Reports along with the *Journal of Public Sector Policy Analysis*. She has also published several research papers in international and local journals. Her research interest includes public finance and public policy, economic development, and energy economics. Ms. Waithe holds a master's degree in Financial and Business Economics and a bachelor's degree in Economics and Management (First Class Honors) from the University of the West Indies, Cave Hill Campus.

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SECTION I:

Current Economic and Social Situation in the Caribbean

Introduction: Institutions in the Caribbean

Diether W. Beuermann and Moisés J. Schwartz

“If the misery of our poor be caused not by the laws of nature, but by our institutions, great is our sin.”

Charles Darwin, 1845

History, fables, and legends are full of examples of monarchs and sovereigns pursuing the advice of sages and elders on how to safeguard their riches. While the wise people’s recommendations often entailed grandiose schemes such as war, conquest, and the subjugation of other communities, the long-term quest for prosperity has invariably relied on the fundamental rules that determine the functioning of societies. These rules and codes of conduct of human behavior that serve to organize societies were eventually recognized as “institutions,” and it is Adam Smith who has generally been credited with identifying the relevance of institutions for economic development and for bringing institutions to the fore of modern economics.

Long-run growth rates have differed across nations and, as a result, income gaps across them have widened over the centuries. For example, in 1820, high-income countries had average real gross domestic product (GDP) per capita equivalent to 2.9 times the average GDP per capita in low-income countries. By 2016, that difference had widened to 26.9 times (Bolt et al. 2018). While these discrepancies in growth and development around the world can be attributed to many different factors, institutional quality has been identified as a key component in determining patterns of prosperity (Acemoglu and Robinson 2012). This is because institutions shape the incentives of economic agents and frame the environment in which their interactions take place.

There is broad recognition that prospects for development are greater when economic agents have certainty about the rule of law, feel secure

about their property rights, have recourse to an effective judiciary and political representation, and when economic policy is anchored in a sound institutional framework. Less successful countries are those where these arrangements are absent or have not been properly developed. Furthermore, because overhauling institutions is often challenging and takes time, an ill-designed institutional framework may have long-lasting consequences on the development of a country and may become difficult to revert.

As previous studies have shown, the countries that constitute the IDB's Caribbean Country Department (CCB)—The Bahamas, Barbados, Guyana, Jamaica, Suriname, and Trinidad and Tobago—face challenges such as weak fiscal positions, crime and violence, a sluggish private sector, weak productive development policies, skill-biased emigration, and recurrent natural disasters. All these problems have significantly affected the countries' growth paths. However, the international evidence that will be examined in this volume has shown that political and economic institutions can play a significant role in (1) limiting the incidence of several of those factors that negatively affect economic growth and social development, and (2) building resilience to uncontrollable exogenous factors, such as natural disasters. Paradoxically, the nature and state of institutions in the Caribbean has not been systematically studied. This book intends to fill this gap.

The volume provides in-depth analyses of the design and quality of institutions within the six aforementioned Caribbean countries, with special emphasis on political, rule of law, human capital development, and economic institutions. The main objective is to document the status of institutions in these countries to promote dialogue and provide input to different stakeholders. This in turn will further our understanding of institutional changes that have the potential to deliver increased development and well-being to the countries and their citizens.

In Chapter 2, Diether W. Beuermann and Juan Pedro Schmid present the macroeconomic and social development outlook for the six Caribbean countries that are the subject of this study. The authors undertake a retrospective analysis covering some four decades, presenting the macroeconomic challenges that these countries have faced, with an emphasis on their relatively low and volatile growth rates, elevated debt levels, and weak fiscal positions. The chapter includes a description of key social sector indicators such as poverty, inequality, educational attainment, and health. The analysis shows that the Caribbean could do better and poses the question of whether stronger institutions could make the economies more resilient and promote long-term sustainable growth.

The second section of the book—Chapters 3, 4, and 5—reviews the evidence on whether and how institutions favor growth and development.

The authors take a theoretical and global empirical perspective without a specific focus on the Caribbean. The main objective of this section is to identify which institutions have been shown to be relatively more important for growth and development worldwide so that the subsequent sections of the book assess the state of such institutions in the Caribbean. In Chapter 3, Moisés J. Schwartz presents a systematic theoretical and evidence-based review of the literature on the topic of institutions in general, and on their role in promoting growth and development. The analysis starts with the initial writings of Adam Smith and takes us up to the present, covering some of the most influential contributions and lines of research on institutions. This review highlights the role of rule of law, human capital, and economic institutions as important determinants of worldwide prosperity. Chapters 4 and 5 complement the review in Chapter 3 by providing deeper analyses of these institutional features toward identifying specific key institutional aspects to assess within the Caribbean context in the subsequent sections.

In Chapter 4, Christian Dippel assesses in more detail institutions related to the rule of law and human capital formation and their role in promoting growth and development. Special emphasis is given to the institutionalization of property rights, health and education systems, and the administration of justice, the police, and other law enforcement institutions. The evidence presented highlights the importance of institutions that protect the property of citizens from expropriation by the government or powerful elites, provide for judicial independence and effectiveness, and support performance-based hiring and retention mechanisms for public education and health workers as significant drivers of growth and development.

In Chapter 5, Klaus Schmidt-Hebbel reviews the literature on the role of institutions that regulate and foster economic activity. Emphasis is on the importance of developing institutions that afford certainty in economic policymaking, such as trade and financial openness, tax rates, medium-term fiscal frameworks, fiscal rules and councils, sovereign wealth funds, exchange rate and monetary policy regimes, central bank independence, and financial sector policies. Based on this analysis, the author concludes that the proper implementation of economic institutions makes for better prospects for growth and development.

The third section of the book—Chapters 6, 7, and 8—documents key specific institutional settings within the six Caribbean countries that are the subject of this study. In Chapter 6, Christian Dippel and Jeetendra Khadan provide historical background on the colonization processes during which political institutions in the Caribbean countries were originally

established. The authors take a regional perspective but highlight individual country specifics when relevant. They uncover how heterogeneous country endowments and colonization experiences might have affected the differing institutional trajectories across Caribbean countries, and how those endowments and experiences could have affected contemporaneous institutional quality.

In Chapter 7, Diether W. Beuermann and Camilo Pecha report on citizens' views in terms of trust in and perceptions of the performance of different institutions that the previous section of the book showed to be relevant determinants of development. The authors focus on three key types of institutions: political, rule of law, and human capital development. They use different global datasets to benchmark the six Caribbean countries vis-à-vis comparable countries in terms of size (referred to as the rest of the small economies of the world), Latin American countries, and member countries of the Organisation for Economic Co-operation and Development.¹

In Chapter 8, Jose Fajgenbaum and Claudio Loser have a dual objective: first, to describe the fiscal situation in Caribbean countries and the main fiscal challenges they face; and second, to make the case for development of fiscal institutions in these countries. Specifically, given the observed weak fiscal performance in the six Caribbean countries that are the subject of this study, the authors outline the fiscal institutions that would be needed to promote fiscal sustainability in the medium term. They highlight the positive role that sound public financial management, medium-term fiscal frameworks, objective fiscal rules, and strengthened public debt management could play in fostering sustainable growth in the countries.

The six chapters that constitute the last section of the book provide in-depth analyses of the current institutional situation for each of the six Caribbean countries studied. Special emphasis is given to those institutions that were found in Chapters 3, 4, and 5 to be more relevant determinants of growth and development. The countries and the respective chapter authors are as follows: The Bahamas (Allan Wright), Barbados (Kimberly Waithe and Juan Pedro Schmid), Guyana (Elton Bollers, Kevin Bonnett, and Mark Wenner), Jamaica (Camila Mejia, Henry Mooney, and Juan Pedro Schmid), Suriname (Jeetendra Khadan), and Trinidad and

¹ Datasets include the World Bank's Doing Business Indicators and World Development Indicators; the World Economic Forum's Global Competitiveness Index; Transparency International's Corruption Perception Index; the Latin American Public Opinion Project; Eurobarometer; and the World Justice Project's Rule of Law Index.

Tobago (Jeetendra Khadan and Lodewijk Smets). The six chapters share the same core structure, with only minor variations. Each country chapter starts with an analysis of political institutions that describes the democratic system in place. Evidence is presented on the structure of political parties and periods in power, as well as the mechanisms in place for political representation, competition, transparency, and accountability. The relevance of political institutions lies in the fact that they lay the groundwork for the development of the other institutions that govern the behavior of economic agents. Any major shift in political institutions can alter other institutional settings and thus force an alteration in the development path.

The country chapters then proceed to rule of law institutions. The analysis assesses the strength of property rights, the protection of fundamental human rights, the independence and effectiveness of the justice system, and the efficacy of law enforcement institutions (mainly the police).

The next sections of the country chapters describe the major features of institutions in charge of fostering human capital development. Here the focus is on aspects of coverage and institutionalized mechanisms for quality control. The primary areas of analysis are education and health services. Institutions related to human capital development should be assessed in terms of their ability to satisfy the basic needs of the population. Access to quality health care and education is a precondition for realizing the full potential of a country's population and for triggering individual effort toward that end. As such, the institutional framework must also be capable of supporting that effort and fostering the accumulation of human capital.

Finally, the country chapters document the state of institutions that regulate and foster economic activity. The analysis includes institutions in charge of monetary policy design and implementation, institutions responsible for fiscal policy and public financial management, and institutions related to the ease of doing business. Economic institutions should provide a structure that rewards individual effort, gives certainty to economic activity, and facilitates its development. Competition and the deepening of markets are elements of this structure. Macroeconomic stability through credible fiscal and monetary authorities, as well as efficient policy instruments, should also be present. Based on the findings, the authors of each chapter provide relevant conclusions and policy recommendations for each country.

The book ends with Chapter 15 where Diether W. Beuermann and Moisés J. Schwartz provide overall concluding comments and some suggestions for policy reform. As discussed throughout this book, growth and development depend on the individual choices made by economic agents in their respective economies, and those choices are shaped by each country's institutional framework. Thus, it is up to each country to undertake the

required institutional reforms that provide the most suitable environment for economic agents to thrive. The accumulated knowledge on the importance of institutions for economic development is significant. Nonetheless, the ability of a country to alter its institutional setting and establish high-quality institutions ultimately depends on the country's specific situation and characteristics. It is our hope that the theoretical underpinnings and empirical evidence presented in this book will provide substantive material for countries in the Caribbean to embark on an agenda for institutional change that has the potential to improve living conditions in the region.

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Macroeconomic and Social Development Outlook in the Caribbean

Diether W. Beuermann and Juan Pedro Schmid

The Caribbean is a diverse region, home to a plethora of languages, customs, foods, traditions, religions, and other elements of heritage that can be traced to the diversity of its people, history, migration, and geography. This diversity is very much present in the six Caribbean countries that are the subject of this study: The Bahamas, Barbados, Guyana, Jamaica, Suriname, and Trinidad and Tobago.¹

In terms of economic structure, an evident distinction is that three of these countries—Guyana, Suriname, and Trinidad and Tobago—rely on commodities, with more than 50 percent of their exports concentrated in their main two commodities.² Therefore, these commodity-dependent economies tend to experience volatile swings in economic conditions depending on exogenously determined world commodity prices. By contrast, the other three countries—The Bahamas, Barbados, and Jamaica—rely on services, with an emphasis on tourism.³

Although income levels differ across the six Caribbean countries, common features during the last decade include relatively low economic growth and elevated levels of indebtedness. In highlighting the fiscal and debt challenges in the Caribbean, Yartey and Turner-Jones (2014) document that structural fiscal problems resulted in a sizable accumulation of debt in the late 1990s and early 2000s, exacerbated by the 2008 global financial crisis. Thus, Caribbean economies face high debt-to-GDP (gross domestic product) ratios, interest payments that take up a large share of revenues, and exposure to rollover risks that can feed fiscal crises.

¹ References in this chapter to the Caribbean refer to these six countries (CCB).

² For Guyana, these commodities are gold and rice; for Suriname, gold and aluminum oxide; and for Trinidad and Tobago, petroleum gases and oil.

³ Tourism accounts for about 50 percent of GDP in The Bahamas and Barbados and about 30 percent of GDP in Jamaica.

Other studies have explored several determinants behind this relatively weak economic performance. Chamon et al. (2017) provide an overview of conditions that have limited Caribbean growth such as the debt burden, crime, migration, natural disasters, and business environments. Ruprah, Melgarejo, and Sierra (2014) explore whether the relatively small size of Caribbean countries explains their underperformance. They find that size does not account for the documented underperformance and suggest that growth is held back by rent-seeking and state capture of private elites. Sutton and Ruprah (2017) focus on crime and violence, estimating an average welfare cost of crime in the Caribbean of about 3 percent of GDP.

Ruprah and Sierra (2016) and Khadan (2017) study the private sector and show that firms in the Caribbean underperform their peers in other regions across several dimensions, including investment, sales growth, innovative capacity, and productivity. Both studies conclude that the main constraint is a policy environment that fails to promote a dynamic and innovative private sector. They identify several areas with weak policies, including customs and trading, access to finance, crime, and the lack of a skilled workforce because of skill-biased emigration.

Regarding outward migration, Mishra (2006) finds that about 70 percent of the population with more than 12 years of education emigrates due to lack of opportunities in the Caribbean. This is a relevant issue for economic growth because, as noted by Ruprah and Sierra (2016), one of the most important barriers to doing business in Caribbean countries is the lack of an appropriately educated labor force. This becomes even more important for Caribbean commodity-dependent economies, where 40 to 60 percent of firms declare that the most significant constraint to doing business is the inadequately educated workforce.⁴ Similarly, Ruprah, Melgarejo, and Sierra (2014) report that 71 percent of the tertiary-educated labor force in Caribbean countries has migrated to member countries of the Organisation for Economic Co-operation and Development (OECD), and that remittances do not compensate for the public resources invested in education and the lost productivity due to emigration.

The economic and social consequences of natural disasters in the Caribbean have also received recent attention. Beuermann, Pecha and Schmid (2017) document that tropical storms and hurricanes that strike when a woman is pregnant have negative short-term effects on early childhood development and potential detrimental long-term effects on the

⁴ Source: 2014 PROductivity, TEchnology and INnovation (PROTEqin) Surveys, available at www.caribbeaneconomics.org.

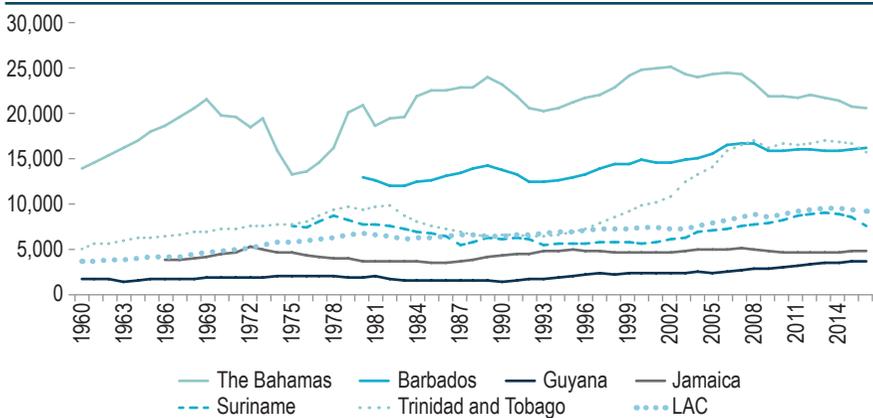
child's eventual adult productivity. Spencer, Polacheck, and Strobl (2016), focusing on high school academic performance, find significantly negative effects of hurricanes on science standardized examinations.⁵ Moreover, Pecha (2017) shows that hurricanes increase adult informal employment in Jamaica by 14.5 percent, thereby reducing productivity, limiting tax collection, and reducing contributions to the social security system.

It appears, therefore, that a combination of weak fiscal positions, crime and violence, a sluggish private sector, weak productive development policies, skill-biased emigration, recurrent natural disasters, and other structural impediments have resulted in a complex and challenging environment to promote sustainable growth and development in the Caribbean. As such, this chapter provides a brief outlook of key economic and social indicators in the region. The objective is to present the context in which the comprehensive institutional assessment provided in this volume will focus. This chapter starts with the macroeconomic outlook for the Caribbean, followed by the region's social outlook.

2.1. Macroeconomic Outlook

Real income levels in Caribbean countries have remained somewhat constant over time. As Figure 2.1 shows, GDP per capita levels in constant U.S.

Figure 2.1 GDP Per Capita (in constant 2010 U.S. dollars)



Source: World Bank, World Development Indicators.

Note: LAC: Latin America and the Caribbean.

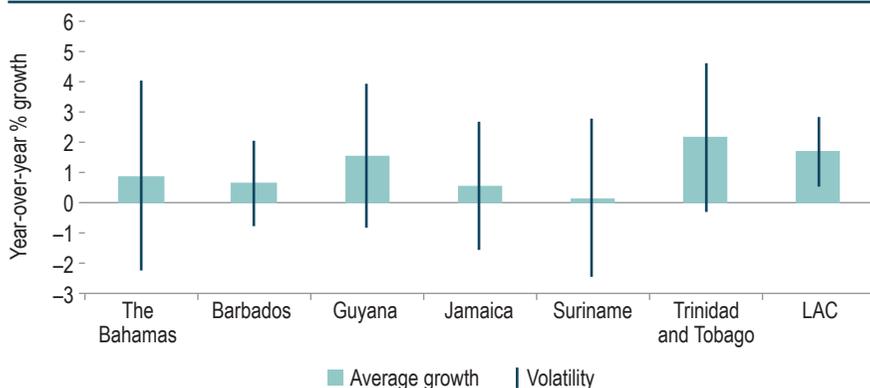
⁵ These are the Caribbean Secondary Education Certificate (CSEC) examinations administered in the last year of secondary school by the Caribbean Examinations Council (CXC). See the CXC website at www.cxc.org.

dollars in The Bahamas and Barbados are the highest in the region. However, they were already higher in the 1960s than the 2016 levels for Guyana, Jamaica, and Suriname. Trinidad and Tobago is an exception, as the country experienced an acceleration in per capita GDP on the back of oil price booms in the mid-1970s and the late 1990s (going from US\$6,400 in 1993 to a peak of US\$17,000 in 2013). Guyana remains the poorest in the group even though it has been catching up from low levels (from US\$1,470 in 1990 to US\$3,800 in 2017). Jamaica's income per capita has also been at the lower end and basically is the same today as it was in 1970 (US\$4,800 in 2016 compared to an average of US\$4,500 in the 1970s).

Compared to the Latin American and Caribbean (LAC) average for the last 56 years, Caribbean countries exhibit both relatively low growth and high volatility. Indeed, all Caribbean countries except for Trinidad and Tobago had lower growth than LAC. In addition, all Caribbean countries had higher growth volatility as measured by the standard deviation (Figure 2.2). Large swings in economic activity create uncertainty among economic agents, and thus are not conducive to sustained economic growth.

In terms of income convergence with richer countries, the region in general has not been catching up with OECD member countries either in terms of per capita U.S. dollars or, controlling for price differences between countries, at purchasing power parity (PPP) per capita U.S. dollars (Figures 2.3 and 2.4). The exception is Trinidad and Tobago, which saw improvements until 2008 but has fallen back since then (Figure 2.3). In addition, although still low in comparison with OECD levels, Guyana's PPP per capita GDP advanced from around 10 percent of the OECD level in

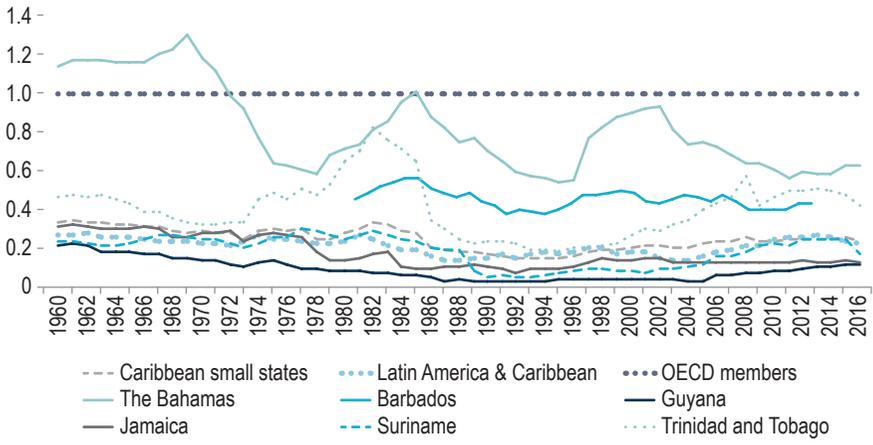
Figure 2.2 Average GDP Per Capita Growth and Volatility, 1960–2016



Source: World Bank, World Development Indicators.

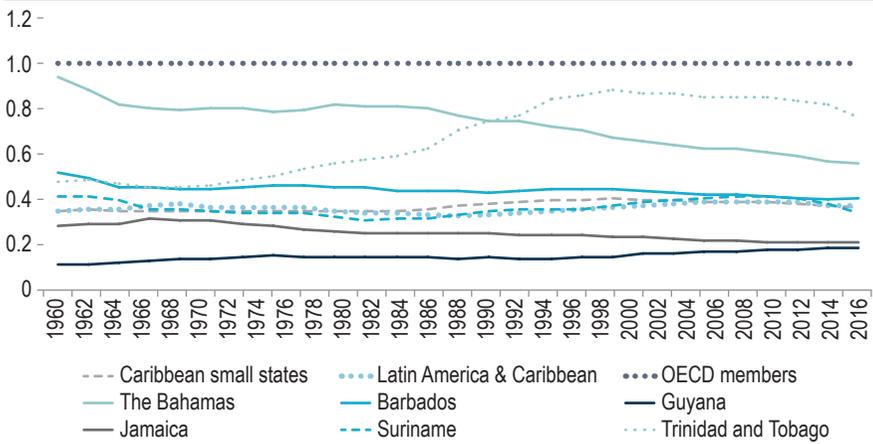
Notes: Average GDP per capita growth based on constant 2010 U.S. dollars. Volatility: standard deviation of yearly growth rates.

Figure 2.3 Per Capita GDP Relative to the OECD, 1960–2016



Source: World Bank, World Development Indicators.

Figure 2.4 Per Capita GDP (at purchasing power parity US\$) Relative to the OECD, 1960–2016

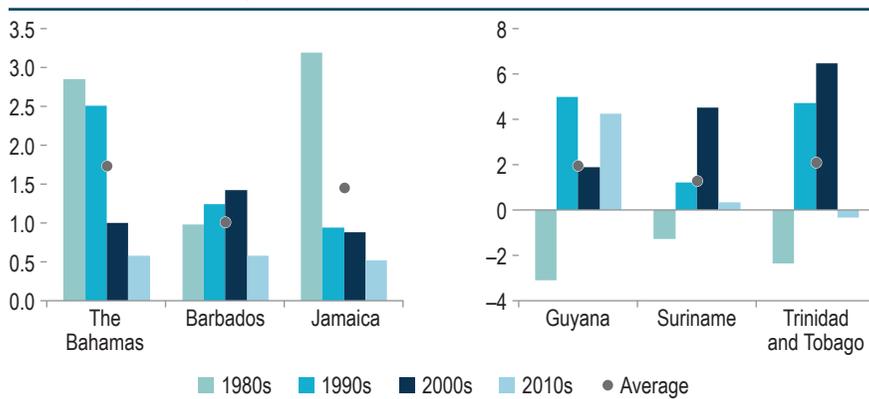


Source: World Bank, World Development Indicators.

1990 to 20 percent in 2016. The Bahamas, which had a per capita income level on par with the OECD in the 1990s, has seen its income per capita relative to the OECD average decline to around 60 percent. Performance in the other countries has been mostly flat, catching up in some years but reversing in others.

While the economic performance of Caribbean countries has varied widely since independence, several commonalities have emerged in

Figure 2.5 Real Economic Growth during Different Time Periods
(year-over-year in percent)



Source: Authors' calculations based on IMF (2017b).

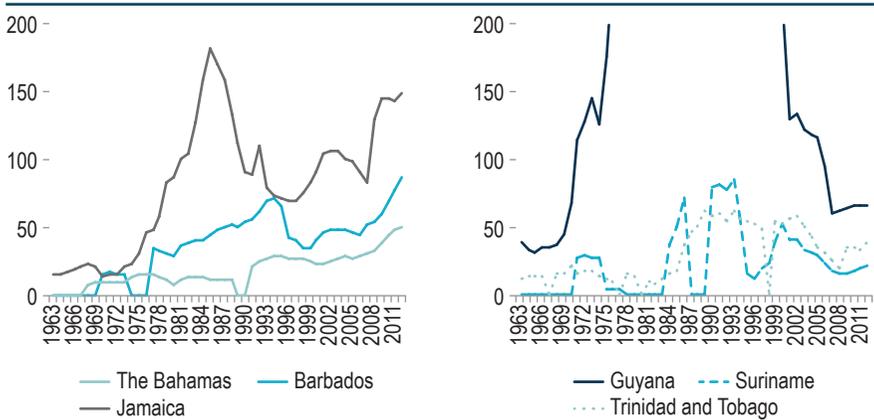
recent years for the non-commodity-dependent and commodity-dependent countries as groups.

The three non-commodity-dependent countries—The Bahamas, Barbados, and Jamaica—all have experienced weak and declining economic growth over the last few decades. Low economic growth in the 2000s declined further after 2010 (Figure 2.5), reflecting the challenge to adapt in the aftermath of the global financial crisis. The growth experience of the commodity producers—Guyana, Suriname, and Trinidad and Tobago—is marked by volatility over time and between countries (Figure 2.5). As with other commodity producers, following strong growth in the 2000s, Trinidad and Tobago and Suriname's growth has recently declined markedly. Guyana is an exception, as the combination of high gold prices and fiscal stimulus in anticipation of oil production kept growth rates high.

The volatile economic performance also had negative effects on public finances, especially in Jamaica and Guyana and, more recently in Barbados and The Bahamas. The Jamaican authorities reacted to the recession caused by the oil price shocks in the 1970s with fiscal expansion, which led to a ballooning debt-to-GDP ratio (Figure 2.6). Similarly, Guyana early in its history after independence experienced increases in debt that were only resolved in the early 2000s through massive debt reduction and forgiveness under the Heavily Indebted Poor Country (HIPC) Initiative and the Multilateral Debt Reduction Initiative (MDRI).

Debt-to-GDP ratios in the other two non-commodity-dependent countries, Barbados and The Bahamas, were more moderate for most of the time but showed an upward trend starting in 2008 (Figure 2.6).

Figure 2.6 Debt-to-GDP: Non-commodity versus Commodity Producers, 1963–2011



Source: International Monetary Fund Historical Debt Database. Available on the Fiscal Monitor Webpage of IMF.ORG, <http://www.imf.org/external/pubs/ft/wp/2010/data/wp10245.zip>.

Note: Maximum value for Guyana is 784% in 1991.

Finally, debt-to-GDP ratios in Suriname and Trinidad and Tobago have been characterized by volatility, reflecting boom and busts from a combination of commodity price swings and periods of domestic tensions (especially for Suriname).

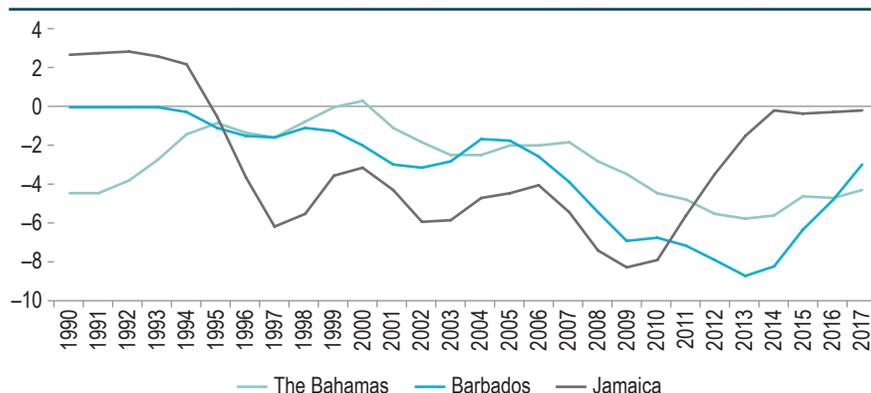
During the last decade, the weak growth performance of tourism countries was accompanied by a significant deterioration of fiscal outcomes and an upward trend in debt-to-GDP ratios (Figures 2.7 and 2.8, and Table 2.1).⁶ More recently, there have been efforts at fiscal restraint, especially in Jamaica, which almost managed to achieve a balanced budget, accompanied by a decline in its debt-to-GDP ratio.

Fiscal performance in the commodity producers follows the commodity cycle, with booms translating into strong fiscal performance, followed by busts when commodity prices decline (Figures 2.9 and 2.10, and Table 2.1). The effects on the debt-to-GDP ratio were especially pronounced in Suriname, where the recent fall in commodity prices triggered a fall in revenues, a contraction in GDP, and a devaluation of the currency.

The region's prolonged and sustained weak economic and fiscal performance poses significant challenges. Debt-to-GDP ratios have remained above the 60 percent threshold, which has been identified in the literature

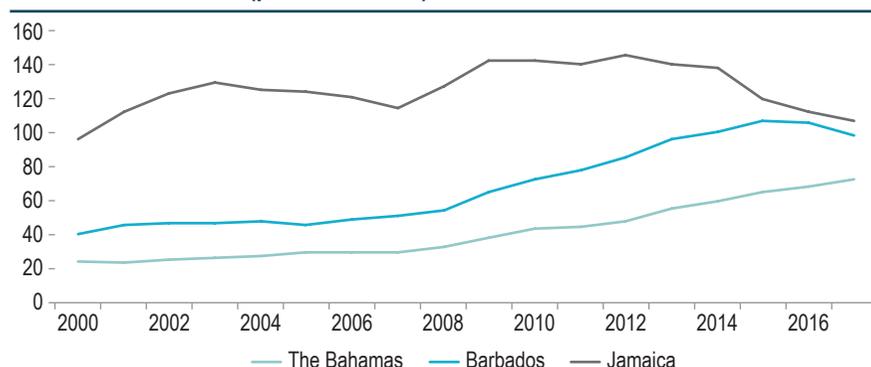
⁶ Jamaica came into the global financial crisis with high levels of debt and low growth, and its fiscal situation became critical around 2009. The authorities undertook a fiscal consolidation effort starting in 2010 that intensified in 2013. Because of these efforts, the country's debt-to-GDP ratio has been declining.

Figure 2.7 Central Government Fiscal Balance for Non-commodity-Dependent Countries, 1990–2017 (three-year averages; percent of GDP)



Source: Authors' calculations based on IMF (2017b).

Figure 2.8 Debt-to-GDP Ratio for Non-commodity-Dependent Countries, 2000–2016 (percent of GDP)



Source: Authors' calculations based on IMF (2017b).

as a level beyond which the amount of debt becomes detrimental to a country's growth prospects (Figure 2.11).⁷

Using the inverted U curve as a benchmark, Figure 2.11 paints a worrying picture for the Caribbean. Non-commodity-dependent countries and member countries of the Organisation of Eastern Caribbean States (OECS),

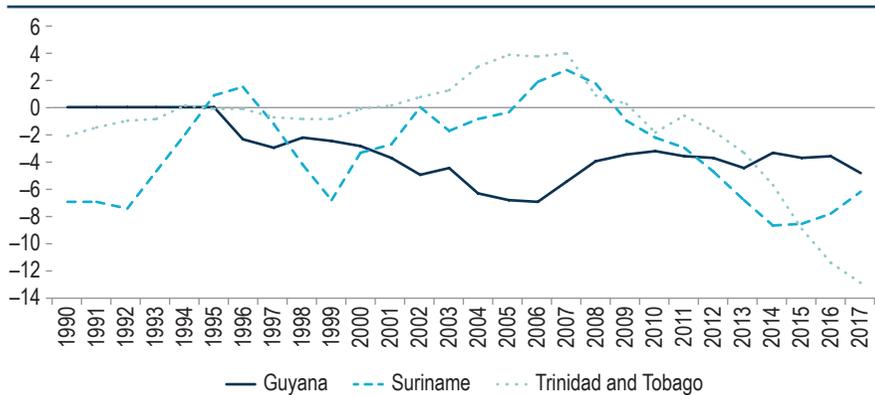
⁷ One possible debt benchmark is derived from the estimated relation between debt and economic growth. This is shown in Figure 2.11. The inverted U shape relation captures that for a debt-to-GDP ratio lower than 30 percent, any increase has a positive marginal and average effect on economic growth. However, above that level (the turning point on the inverted U curve), any further increase has a negative marginal effect, and above 60 percent the impact (marginal and average) becomes negative. See Greenidge et al. (2012).

Table 2.1 Fiscal Balances for Different Time Periods (percent of GDP)

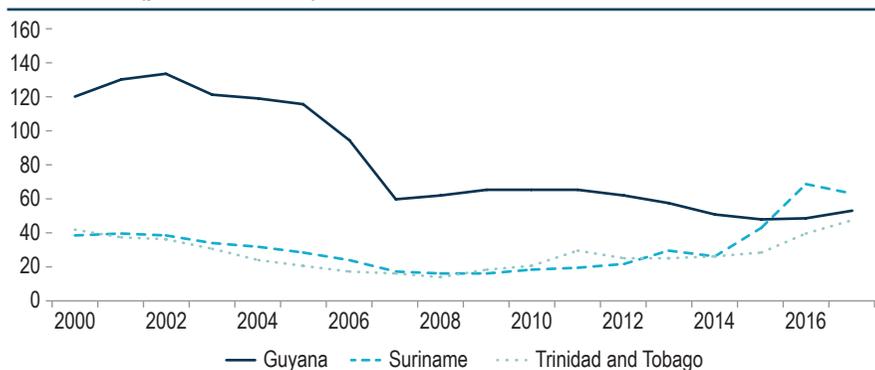
	1990s	2000s	2010s
The Bahamas	-1.81	-2.07	-4.98
Barbados	-1.12	-3.30	-7.42
Guyana	-2.14	-4.99	-3.57
Jamaica	-0.75	-5.45	-2.53
Suriname	-3.52	-0.42	-6.01
Trinidad and Tobago	-0.71	1.67	-4.53
LAC, excluding CCB	-1.83	-2.25	-2.84

Source: Authors' calculations based on IMF (2017b).

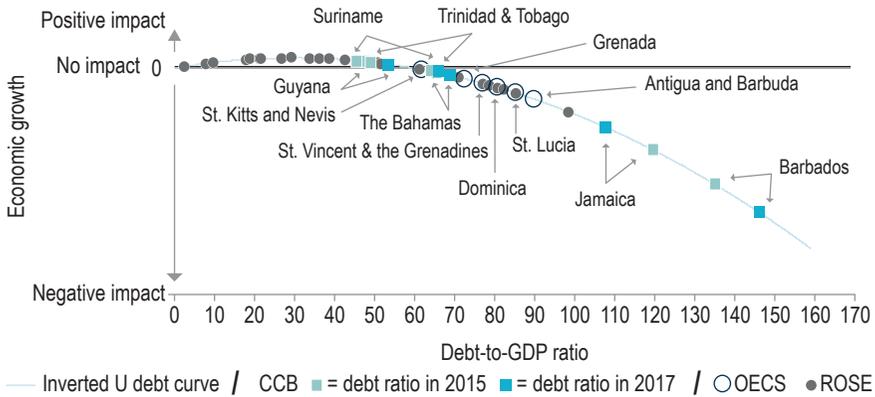
Note: CCB: The Bahamas, Barbados, Guyana, Jamaica, Suriname, and Trinidad and Tobago.

Figure 2.9 Central Government Fiscal Balance for Commodity-Dependent Countries, 1990–2017 (three-year averages, percent of GDP)


Source: Authors' calculations based on IMF (2017b).

Figure 2.10 Debt-to-GDP Ratio for Commodity-Dependent Countries, 2000–2016 (percent of GDP)


Source: Authors' calculations based on IMF (2017b).

Figure 2.11 Relationship Between Debt and Economic Growth

Source: Authors' calculations based on IMF (2017a).

Note: CCB: IDB Caribbean Country Department members; OECS: Organisation of Eastern Caribbean States; ROSE: rest of the small economies of the world.

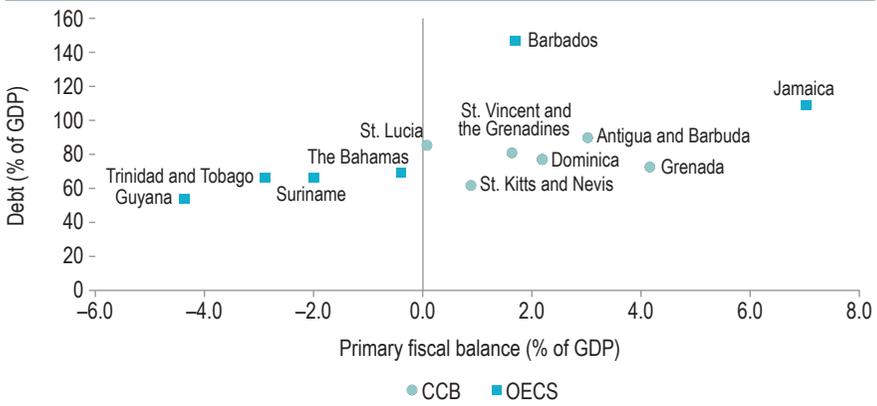
as well as Suriname and Trinidad and Tobago, are already in the negative region of the debt-growth relation, suggesting that the heavy debt burden is already diminishing their growth prospects. Guyana would cross the threshold soon, but the projected jump in GDP from the commencement of oil extraction in 2020 should halt the increase in its debt-to-GDP ratio. Jamaica is expected to reduce its debt ratio, but will remain in the negative region of the relation.

Related to the increase in the debt-to-GDP ratios are the weak levels of fiscal buffers. The higher the primary balance and the lower the current debt, the better the ability of a country to absorb shocks. In this respect, fiscal buffers in the Caribbean are insufficient. The two countries with positive primary balances, Jamaica and Barbados, have high levels of debt (Figure 2.12). In the other countries, the primary balances are negative, implying that they are already contributing to building up debt. Projections are that most countries will remain at current levels or increase their debt-to-GDP ratios. Thus, unless a substantial correction in the fiscal stance takes place, debt-to-GDP ratios could increase rapidly if the countries face a shock.

Other than Jamaica, which has made substantial progress under an International Monetary Fund (IMF) adjustment program, all the countries are in need of fiscal consolidation.⁸ Comparing the actual primary balance with the

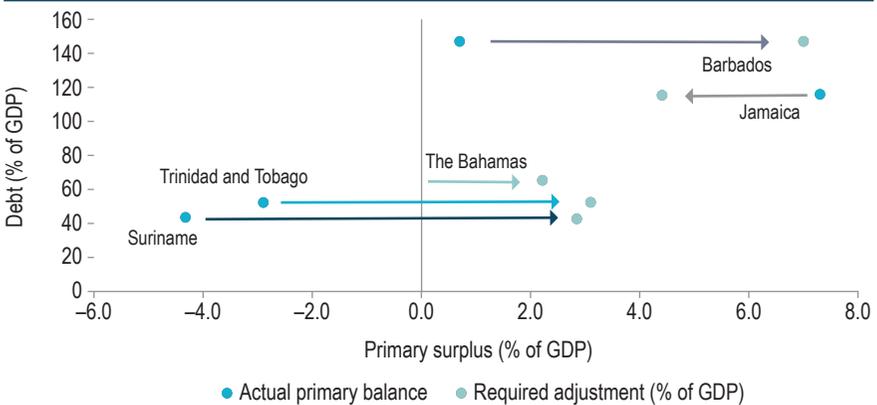
⁸ Given the relevance of this regional challenge, Chapter 8 provides a detailed assessment of the fiscal scenario in the Caribbean highlighting which institutions could help revert the current situation.

Figure 2.12 Fiscal Buffers, 2017



Source: Authors' calculations based on IMF (2017b).

Figure 2.13 Actual and Required Fiscal Balance, 2016



Source: Authors' calculations based on IMF (2017b).

required primary balance to stabilize the debt ratio at current levels gives an indication of the direction and size of the fiscal adjustments needed to avoid increasing the debt-to-GDP ratio.⁹ Figure 2.13 shows the estimated fiscal adjustment, drawn in terms of percentage points of GDP. Except for Jamaica, the required fiscal adjustment to stabilize the debt ratio at current levels averages 4 percentage points of GDP for Caribbean countries.¹⁰ Suriname's

⁹ Reducing the debt-to-GDP ratio from current levels requires an even more forceful fiscal adjustment.

¹⁰ This figure excludes Guyana, which falls under the Heavily Indebted Poor Country (HIPC) category. Therefore, a different criterion is used.

required adjustment is the largest (7 percentage points), followed by Barbados and Trinidad and Tobago (6 percentage points) and The Bahamas (2 percentage points). Jamaica's actual primary balance, a surplus of 7 percent of GDP, derives from the country's strict adherence to a fiscal rule that aims to reduce the debt-to-GDP ratio to 100 percent by 2020 and 60 percent by 2026.

Taken together, macroeconomic performance in the Caribbean shows a region that is facing headwinds. Non-commodity-dependent countries can best be summarized as "low growth and high debt," while "booms and busts" best describes the performance of commodity producers. While the volatile performance of the latter group is a challenge, it is in line with the experiences of other commodity producers. However, without a sustained and decisive fiscal adjustment, debt-to-GDP ratios could continue increasing, thus leaving the countries in an even more vulnerable position. Such a scenario would require stronger adjustments in the medium to long term.¹¹ The performance of the non-commodity-dependent countries is also weak by international comparison (Chamon et al. 2017). While these countries need to pursue fiscal adjustments, the underlying challenge is weak economic growth that has persisted for a prolonged period. Addressing this problem will require deeper structural adjustments beyond fiscal consolidation.

In summary, the macroeconomic performance of Caribbean countries has been weak for many years and is projected to remain as such. Jamaica, however, is a recent example of how fiscal discipline that relies on credible economic institutions could help improve this weak performance.

The macroeconomic figures presented, however, do not depict a comprehensive picture in the absence of an analysis of the social sector. Therefore, the next section provides an outlook of the main social indicators in the Caribbean.

2.2. Social Development Outlook

This section benchmarks key social indicators including poverty rates, educational attainment, and health status for Caribbean countries within a global perspective. In general, analyses of the social sector for the Caribbean are relatively scarce due to limited public access to household- and individual-level databases such as surveys of living conditions, labor force surveys, and population censuses. Against this backdrop, this

¹¹ Guyana's outlook is different given the expectation of oil production starting in 2020, when increases in GDP and oil-related revenues are expected. This could lead to a declining debt-to-GDP ratio in the years after 2020.

section exploits recently gathered databases measuring living standards across Caribbean countries.¹² For the rest of the world, the World Bank's World Development Indicators database is used. For benchmarking purposes, the analysis includes three country groups in addition to the Caribbean: Latin America, the rest of the small economies of the world (ROSE), and the OECD.¹³

As shown in Table 2.2, poverty rates in all Caribbean countries except for Guyana are lower than those of Latin America and ROSE. Although still significantly above OECD levels, The Bahamas' poverty rate of 11.39 percent is the lowest among Caribbean countries. Jamaica, Trinidad and Tobago, Barbados, and Suriname have poverty rates within a range of 21 to 26 percent. Finally, Guyana has a relatively high poverty rate of 41.2 percent. Inequality is measured by the consumption-based Gini coefficient, which ranges between 0 (full equality of consumption among all members of society) and 100 (extreme inequality, where just one household consumes all resources of society). Barbados is the Caribbean country with the least inequality, as shown by its Gini coefficient of 32.23, which is very similar to the OECD average (33.19). The rest of the Caribbean countries have Gini coefficients ranging between 36 and 43, suggesting medium to low levels of inequality comparable to levels of

¹² The data sources for Caribbean countries used for this section are the following: The Bahamas: 2013 Household Expenditure Survey; Barbados: 2016 Survey of Living Conditions; Guyana: 2017 Labor Force Survey; Jamaica: 2015 Survey of Living Conditions; Suriname: 2017 Survey of Living Conditions; and Trinidad and Tobago: 2014 Survey of Living Conditions. For the rest of the world, data were obtained from the World Bank's World Development Indicators database and IDB (2016).

¹³ The ROSE group corresponds to countries with populations of less than 3 million. However, to achieve greater similarity with the CCB countries, we also exclude some outliers in terms of income. Specifically, we exclude countries with GDP per capita levels above the CCB countries range. These excluded countries from the ROSE group are: Bahrain, Brunei Darussalam, Iceland, Luxembourg, and Malta. We also exclude OECD member countries from the ROSE such as Estonia, Latvia, and Slovenia. Therefore, countries considered in the ROSE group are: Bhutan, Botswana, Cyprus, Gabon, Lesotho, Macedonia, Mauritius, Mongolia, Montenegro, Seychelles, and Timor-Leste. Countries included in the Latin America group are Argentina, Bolivia, Brazil, Chile, Colombia, Costa Rica, Dominican Republic, Ecuador, El Salvador, Guatemala, Honduras, Mexico, Nicaragua, Panama, Paraguay, Peru, Uruguay, and Venezuela. The countries included in the OECD group are Australia, Austria, Belgium, Canada, Czech Republic, Denmark, Estonia, Finland, France, Germany, Greece, Hungary, Iceland, Ireland, Israel, Italy, Japan Republic of Korea, Latvia, Luxemburg, Netherlands, New Zealand, Norway, Poland, Portugal, Slovak Republic, Slovenia, Spain, Sweden, Switzerland, Turkey, United Kingdom, and United States. Notice that although Chile, Colombia and Mexico belong to the OECD, we do not consider them in the OECD group for the analyses as they are already included in Latin America.

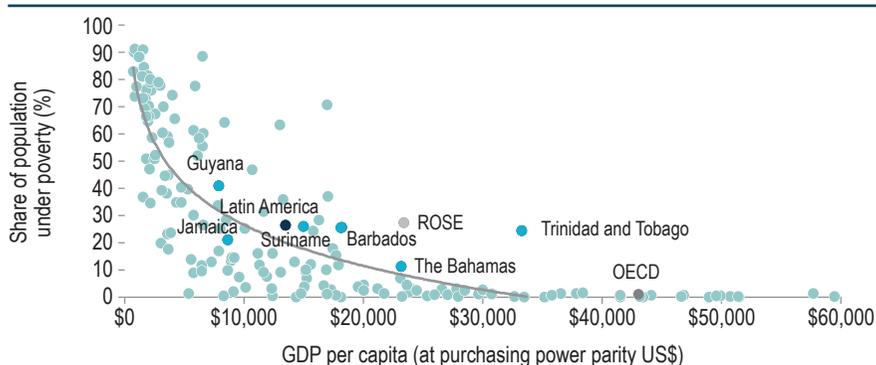
Table 2.2 Poverty and Inequality

Country Name	Poverty Rate (percent)	Gini Coefficient
OECD	1.12	33.19
The Bahamas	11.39	41.91
Jamaica	21.19	37.44
Trinidad and Tobago	24.50	42.22
Barbados	25.69	32.23
Suriname	26.10	43.79
Latin America	26.54	47.85
ROSE	27.45	40.48
Guyana	41.20	36.40

Sources: Authors' calculations based on the following: The Bahamas: 2013 Household Expenditure Survey; Barbados: 2016 Survey of Living Conditions; Guyana: 2017 Labor Force Survey; Jamaica: 2015 Survey of Living Conditions; Suriname: 2017 Survey of Living Conditions; and Trinidad and Tobago: 2014 Survey of Living Conditions. For the rest of the world, data were obtained from the World Bank's 2016 World Development Indicators database.

ROSE and lower than levels in Latin America, which has the largest Gini coefficient of 47.85 (Table 2.2).

Figure 2.14 depicts the empirical relation between country-specific poverty rates and GDP per capita worldwide, highlighting Caribbean economies. Not surprisingly, an immediate observation is that poverty rates decline as GDP per capita increases. Except for The Bahamas and Jamaica, however, poverty levels for Caribbean countries are significantly higher than what is observed for other countries with similar GDP per

Figure 2.14 Poverty versus GDP Per Capita

Source: Authors' calculations based on the following: The Bahamas: 2013 Household Expenditure Survey; Barbados: 2016 Survey of Living Conditions; Guyana: 2017 Labor Force Survey; Jamaica: 2015 Survey of Living Conditions; Suriname: 2017 Survey of Living Conditions; and Trinidad and Tobago: 2014 Survey of Living Conditions. For the rest of the world, data were obtained from the World Bank's 2016 World Development Indicators database.

capita (i.e., their poverty levels lie significantly above the dotted regression line). Trinidad and Tobago is the more serious case, with the highest GDP per capita within the Caribbean, but with a poverty rate (24.5 percent) located well above what is observed among countries with similar GDP per capita. For instance, Latin America has less than half of Trinidad and Tobago's GDP per capita but has a very similar poverty level (26.54 percent). Barbados, Suriname, and Guyana also have elevated levels of poverty relative to their GDP per capita. Poverty rates stand at 25.69 percent for Barbados, 26.10 percent for Suriname, and 41.2 percent for Guyana.

One relevant observation is that commodity-dependent Caribbean economies—Guyana, Suriname, and Trinidad and Tobago—on average have relatively higher poverty figures than Caribbean countries that are more dependent on services and tourism. Countries like The Bahamas, Barbados, and Jamaica on average have poverty rates more in line with other countries with similar levels of GDP per capita. The average distance between observed poverty and the poverty levels displayed by countries with similar GDP per capita is about 2.1 percentage points for The Bahamas, Barbados, and Jamaica as a group. However, this average difference is 13.78 percentage points for the commodity-dependent Caribbean economies of Guyana, Suriname, and Trinidad and Tobago. As discussed in other chapters of this book, such heterogeneity between Caribbean commodity-dependent and non-commodity-dependent economies could be associated with institutional characteristics that need to be considered to boost growth and reduce poverty.

2.2.1. Education

One of the most important drivers of economic development is an educated labor force that can foster higher productivity and the adoption of innovative technologies (Hanushek and Woessmann, 2012). Table 2.3 shows indicators of educational attainment levels across Caribbean countries. The average years of acquired formal education among working-age adults (25–65 years old) is relatively high for Barbados (12.36 years) and The Bahamas (11.96 years). These countries perform better than the OECD average (10.9 years). Jamaica has very similar levels compared to the OECD, with 10.84 years of education, which is above the ROSE average (10.12 years). While the commodity-dependent Caribbean economies (Trinidad and Tobago, Suriname, and Guyana) outperform Latin America (8.08 years), they range between 8.74 and 9.98 years of education and are below ROSE levels. Therefore, human capital development measured by years of

Table 2.3 Educational Attainment

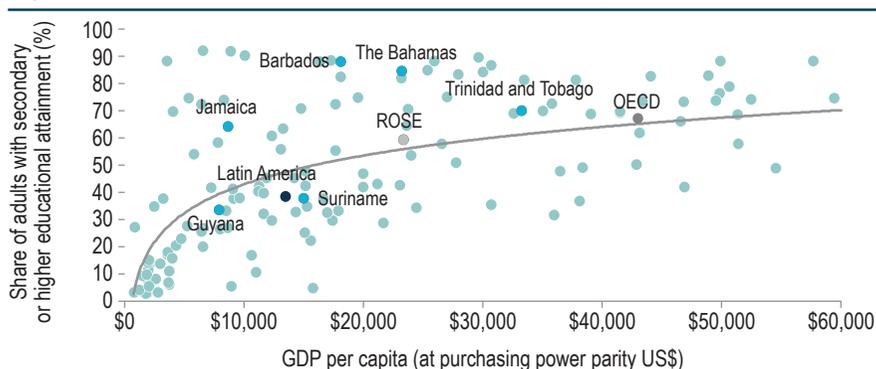
Country Name	Years of Education	Below Secondary (percent)	Complete Secondary (percent)	Tertiary (percent)
Barbados	12.36	12.50	51.10	36.40
The Bahamas	11.96	15.30	52.60	32.10
OECD	10.90	32.60	43.96	23.44
Jamaica	10.84	35.70	49.50	14.80
ROSE	10.12	40.45	40.42	19.13
Trinidad and Tobago	9.98	29.80	50.50	19.70
Suriname	8.87	61.90	26.40	11.70
Guyana	8.74	66.20	27.80	6.00
Latin America	8.08	61.61	25.58	12.80

Sources: Authors' calculations based on the following: The Bahamas: 2013 Household Expenditure Survey; Barbados: 2016 Survey of Living Conditions; Guyana: 2017 Labor Force Survey; Jamaica: 2015 Survey of Living Conditions; Suriname: 2017 Survey of Living Conditions; and Trinidad and Tobago: 2014 Survey of Living Conditions. For the rest of the world, data were obtained from the World Bank's 2016 World Development Indicators database.

Note: Educational attainment is measured among working-age adults (25–65 years old) who have completed their formal education.

formal education consistently suggests that Caribbean countries that do not rely heavily on commodities outperform those with a heavy reliance on commodities.

Figure 2.15 shows the relationship between the share of the adult population (25–65 years old) with complete secondary education or above and GDP per capita. Caribbean non-commodity-dependent countries

Figure 2.15 Educational Attainment versus GDP Per Capita

Sources: Authors' calculations based on the following: The Bahamas: 2013 Household Expenditure Survey; Barbados: 2016 Survey of Living Conditions; Guyana: 2017 Labor Force Survey; Jamaica: 2015 Survey of Living Conditions; Suriname: 2017 Survey of Living Conditions; and Trinidad and Tobago: 2014 Survey of Living Conditions. For the rest of the world, data were obtained from the World Bank's 2016 World Development Indicators database.

show significantly higher shares of individuals with secondary or above educational attainment than other countries with similar GDP per capita levels (i.e., above the dotted regression function). On average, the share of secondary or above educated individuals in Caribbean non-commodity-dependent economies outperforms by 29.21 percentage points the average of countries with similar GDP per capita levels. By contrast, except for Trinidad and Tobago, the Caribbean commodity-dependent economies have lower shares of secondary or above educated individuals with respect to their GDP per capita levels (i.e., below the dotted regression function). While Trinidad and Tobago outperforms this benchmark by 9.08 percentage points, Guyana and Suriname underperform this benchmark by an average of 8.41 percentage points.

2.2.2. Health

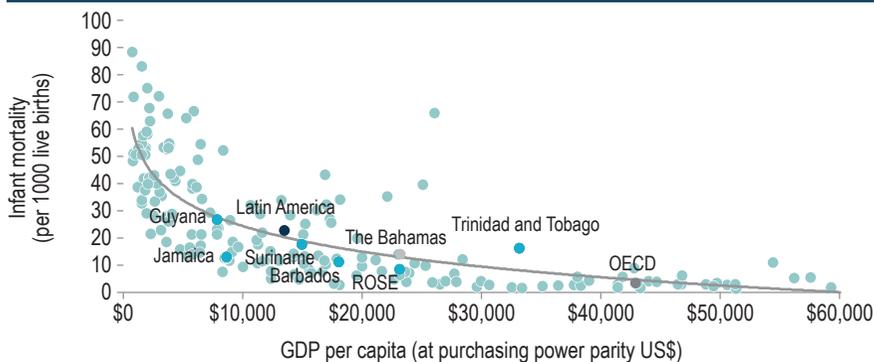
Health is another critical component of human capital (Bleakley 2007). Table 2.4 benchmarks some key indicators measuring health outcomes and the supply of health services. The table first looks at infant mortality, as it is an indicator widely used to measure overall health status (Jaba, Balan, and Robul 2015). The three Caribbean non-commodity-dependent countries (The Bahamas, Barbados, and Jamaica) outperform ROSE but are still below OECD levels. Trinidad and Tobago and Suriname outperform Latin America but lag ROSE, while Guyana underperforms all comparators.

Another relevant health outcome is life expectancy, which is also reported in Table 2.4. This alternative indicator evidences the same pattern, suggesting relatively better outcomes for Caribbean non-commodity-dependent economies.

Table 2.4 Health Outcomes and Health Supply

Country Name	Infant Mortality Rate (per 1,000 live births)	Life Expectancy at Birth (years)	Physicians per 1,000 population
OECD	5.93	80.12	2.86
The Bahamas	8.60	75.68	2.26
Barbados	11.40	75.91	1.81
Jamaica	13.20	75.97	0.47
ROSE	13.32	75.44	1.67
Trinidad and Tobago	16.50	70.67	1.82
Suriname	17.80	71.41	0.82
Latin America	23.04	70.93	1.25
Guyana	26.90	66.65	0.21

Source: Authors' calculations based on the World Bank's 2016 World Development Indicators database.

Figure 2.16 Infant Mortality versus GDP Per Capita

Source: Authors' calculations based on the World Bank's 2016 World Development Indicators database.

On the supply side, the number of physicians per 1,000 population is highest for The Bahamas (2.26 physicians) among Caribbean countries (Table 2.4). Barbados and Trinidad and Tobago follow with similar indicators (about 1.8 physicians, which is above the ROSE and Latin America averages of 1.67 and 1.25 physicians, respectively). By contrast, Jamaica and Guyana display low densities of physicians that are below all comparators. It is worth noting, however, that although Jamaica has a low density of physicians (only 0.47 physicians per 1,000 population), health outcomes in terms of infant mortality and life expectancy there are above ROSE and Latin American levels.

Figure 2.16 depicts the worldwide empirical relation between GDP per capita and infant mortality. The pattern suggests a negative relation, as higher income levels are associated with lower mortality rates. Within this pattern, most Caribbean countries display infant mortality levels according to their GDP per capita (i.e., very close to the dotted regression line). However, two Caribbean countries significantly diverge from that trend.

First, Jamaica (with 13.2 infant deaths per 1,000 live births) has significantly lower levels of infant mortality with respect to its GDP per capita (i.e., below the dotted regression line). Jamaica's infant mortality rate is comparable to those of Caribbean economies that have twice its GDP per capita, such as Barbados (11.4 infant deaths per 1,000 live births). This observation, coupled with the fact that health supply in terms of the density of physicians is also relatively low in Jamaica, suggests a relatively efficient health system.¹⁴

¹⁴ Related evidence provided by Beuermann and Pecha (2016) shows that the 2008 universalization of public health in Jamaica had noticeable positive impacts on adult health status and labor supply.

Second, Trinidad and Tobago is the Caribbean country with the highest GDP per capita but with an infant mortality rate significantly higher than that of comparable economies in terms of income (i.e., above the dotted regression line). With 16.5 infant deaths per 1,000 live births, Trinidad and Tobago is close to the level of Suriname (17.8), even though Suriname has less than half of Trinidad and Tobago's GDP per capita.

The analyses suggest that Caribbean commodity-dependent countries (Guyana, Suriname, and Trinidad and Tobago) show relatively higher vulnerability in terms of social indicators. However, while non-commodity-dependent Caribbean countries have relatively better social outcomes, it is also true that fiscal performance is relatively weak across all Caribbean economies. Coupled with greater frequency and magnitude of weather shocks such as tropical storms, hurricanes, and sea level rise, this implies worse income-generation opportunities for the people of the Caribbean (Hallagate et al. 2015).¹⁵ All of these external factors, plus a fragile macroeconomic context characterized by low rates of growth and high debt levels, could seriously hinder the development prospects for the region. As such, the remainder of this book explores relevant institutions that have been shown to spur growth and build resilience to external shocks, while also assessing the stage of development of such institutions across the Caribbean.

¹⁵ The tropical storm season in 2017 was one of the most devastating in history. In the United States alone, the estimated economic losses were US\$265 billion, according to the National Oceanic and Atmospheric Administration (NOAA). Available at <https://www.ncdc.noaa.gov/billions/events/US/2017> (accessed in January 2018). With respect to the Caribbean, countries such as Antigua and Barbuda suffered the destruction of almost 90 percent of their infrastructure as a result of Hurricane Irma in September 2017, as stated by Prime Minister Hon. Gaston Browne. See Steve Robson and Abigail O'Leary, "Island of Barbuda 'Left a Rubble' by Hurricane Irma as Prime Minister Says 90 per cent of Buildings Destroyed," *Mirror*, 7 September 2017. Available at: <http://www.mirror.co.uk/news/world-news/island-barbuda-left-a-rubble-11124904> (accessed in January 2018).

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SECTION II:

Institutions and their Role in Fostering Growth and Development

Institutions and Economic Performance: A Review of the Literature

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There is widespread understanding among the economics profession today that institutional quality plays an important role in shaping the patterns of prosperity around the world. It is well recognized that when economic agents have certainty about the rule of law, feel secure about their property rights, and have recourse to an effective judiciary and political representation, the prospects for development are greater. Moreover, countries that have set themselves on a course of strengthening the quality of their institutions to provide at least a minimum of certainty to economic agents have been able to alter their development path. Less successful countries are those where these arrangements are absent or have not been properly developed. Ill-designed institutions, or their nonexistence, have contributed to more vulnerable economies with reduced flexibility to adapt to and confront changing and unexpected circumstances.

As understanding of the role of institutions in economic performance gained ground in the economics profession, the study of institutions evolved into the relevance of institutions to a significant number of activities that ultimately also contribute to the well-being of nations. As such, the study of institutions moved into areas as varied as the role of institutions on reducing corruption, strengthening corporate governance, improving the regulatory framework, and reducing uncertainty in the implementation of economic policy. Advocates of this approach claim that clarity in the rules of the game and greater transparency and certainty in a whole range of policies and regulations have a long-lasting impact on a country's growth prospects.

A significant number of extensive and detailed articles present an exhaustive review of the literature, including Aron (2000), Acemoglu, Johnson, and Robinson (2005), Shirley (2005), Ugur (2010), Bluhm and Szirmai (2012), Evans and Ferguson (2013), Ogilvie and Carus (2014), Leite,

Silva, and Alfonso (2014), and Lee and Lloyd (2016). Thus, the aim of this chapter is neither to repeat these comprehensive reviews nor to cover every strand of this wide-ranging literature, but rather to trace the evolution of the institutional approach, identify some of the channels through which institutional quality could affect economic performance, and provide the most salient empirical findings of these studies. Only through a thorough understanding of the relevance of institutions for growth and development, and their historical origins within a country, can one be better placed to recommend changes to the prevailing institutional setting.

The next section defines the concept of “institutions” along the lines of North (1990), then proceeds to review some of the earliest work on the institutional approach. The writings of Adam Smith show his superb understanding of the relevance of institutions for economic development more than 250 years ago.¹ The chapter then analyzes institutions within the sphere of neoclassical economics and the emergence of “new institutional economics” (NIE). The importance of Douglass North’s work takes prominence in this review, as it continues to navigate some of the extensive literature that has been developed on the subject. Particular attention is given to the historical perspective of institutions, and to their role in determining growth and development. The final section wraps up some of the main findings and addresses some issues that remain unresolved.

3.1. What Are Institutions?

An obvious starting point in the discussion and definition of institutions is North (1990), whose influential work, along with Coase (1960) and Williamson (1985), shaped the emerging field of NIE. Their work gave rise to a robust analytical framework that had significant repercussions not only on the economics discipline, but also on the broad social sciences as well. For North:

“Institutions are the rules of the game in a society or, more formally, are the humanly devised constraints that shape human interaction. In consequence they structure incentives in human exchange, whether political, social, or economic.” (North 1990, 3)

By defining and limiting the set of choices of individuals, institutions reduce uncertainty in the relationships between economic agents as they

¹ Smith’s writings of 1755 already show a comprehensive grasp of institutions. Most of these ideas were later expanded in his influential 1776 work, *An Inquiry into the Nature and Causes of the Wealth of Nations*.

help them to form expectations of what others will do. Institutions minimize opportunistic behavior, facilitate the enforcement of contracts, and reduce transaction costs, thus providing a structure to everyday life. Consequently, all the written and unwritten rules, norms, conventions, codes of behavior, and constraints that constitute the framework within which human interactions take place can be defined as institutions.² Quoting North again, institutions

“...are perfectly analogous to the rules of the game in a competitive team sport. That is, they consist of formal written rules as well as typically unwritten codes of conduct that underlie and supplement formal rules, such as not deliberately injuring a key player on the opposing team. And as this analogy would imply, the rules and informal codes are sometimes violated and punishment is enacted. Therefore, an essential part of the functioning of institutions is the costliness of ascertaining violations and the severity of punishment.” (North 1990, 4)

Having thus defined institutions, let us now trace back some of the history of institutions in the economics literature.

3.2. Institutions in Economics: The Earliest Approach

Interest in the role of institutions on economic performance is not a recent phenomenon. Dating to ancient times, rules relating to the way societies should be organized (institutions) contributed to the prosperity of regions, lands, and empires. However, for modern economics, the recognition that institutions influence economic development dates back to Adam Smith. In the *Wealth of Nations* (1776), Smith brings to the fore the crucial role played by rules relating to how societies should be organized (i.e., institutions such as the rule of law and property rights) in determining the proper conditions to productively engage in economic activity. Smith’s profound understanding of the role of institutions for economic development is reflected in his writings:

“Commerce and manufactures can seldom flourish long in any state which does not enjoy a regular administration of justice, in which the people do not feel themselves secure in the possession

² The institutional economics literature often makes a distinction between formal and informal institutions. On the latter, see Platteau (2000).

of their property, in which the faith of contracts is not supported by law, and in which the authority of the state is not supposed to be regularly employed in enforcing the payment of debts from all those who are able to pay. Commerce and manufactures, in short, can seldom flourish in any state in which there is not a certain degree of confidence in the justice of government.” (v.3.7)

Or:

“In all countries where there is tolerable security, every man of common understanding will endeavor to employ whatever stock he can command in procuring either present enjoyment or future profit....In those unfortunate countries...where men are continually afraid of the violence of their superiors, they frequently bury and conceal a great part of their stock...” (II.1.30 and II.1.31)

Moreover, according to Smith, institutional factors can influence not only the cross-country differences in growth rates, but also regional disparities within a country:

“Order and good government, and along with them the liberty and security of individuals, were, in this manner, established in cities at a time when the occupiers of land in the country were exposed to every sort of violence. But men in this defenseless state naturally content themselves with their necessary subsistence, because to acquire more might only tempt the injustice of their oppressors. On the contrary, when they are secure of enjoying the fruits of their industry, they naturally exert it to better their condition, and to acquire not only the necessaries, but the conveniences and elegancies of life. That industry, therefore, which aims at something more than necessary subsistence, was established in cities long before it was commonly practiced by the occupiers of land in the country.” (III.3.12)³

While institutions have been part of the economic literature for a long time, however, it was only at the beginning of the 20th century with the

³ Peace, easy taxes, and a tolerable administration of justice are Smith’s fundamental pillars of prosperity. A modern reinterpretation of Smith’s arguments is presented in Besley and Persson (2011). These authors explain the existence of development clusters that combine effective state institutions, the absence of political violence, and high per capita incomes.

“old institutionalists” that a more systematic approach to analyze institutions began. Among others, Veblen (1898, 1904) and Commons (1924) emphasized the essential role institutions play in defining agents’ actions at the social and economic levels. According to Veblen’s school of thought, institutions embodied generally accepted ways of thinking and behaving that are developed in a spontaneous way. Institutions are patterns of behavior, internal norms, customs, and traditions that regulate behavior and mold the preferences and values of individuals. In contrast, the vision of Commons seems to be more legalistic, as this branch of thought placed more emphasis on issues of law and economics, covering topics such as the evolution of property rights and the legal context of transactions, among others. Commons’ view also sees institutions as rules that help governing agents’ behavior, but that emphasize their legal source and agents’ resolved design, as opposed to being developed spontaneously due to the agents’ regular interactions (Rutherford 2001). The advent of the Great Depression, the appearance of Keynesian economics, and new developments in theory and methods diminished interest in the “old institutionalists.” Moreover, from the 1930s onward, neoclassical theory underwent significant development, including theories of imperfect and monopolistic competition, market failures, and externalities, thus significantly diminishing the preponderance of the institutionalist school. It was not until the late 1960s and early 1970s, with the emergence of NIE, that institutions were brought back to center stage in economics.

3.3. Neoclassical Economics and the Advent of New Institutional Economics

The last 40 years have witnessed a renewed interest of economists in the role of institutions in society. In recognizing that institutions matter for economic performance because they reduce the uncertainty caused by arbitrary behavior and provide a necessary structure to human interactions, NIE emerged as a sub-discipline of economics. NIE studies institutions and how they interact with other organizational arrangements. Its goal is to explain what institutions are, how they arise, what purposes they serve, how they change, and how if at all they should or can be reformed (Klein 2000; Williamson 2000).

Neoclassical economics ignored the relevance of institutions for a long time as it attempted to explain economic growth (and thus the prosperity of nations) by reference to a technical production function that turned inputs into outputs, under the coordination of the price mechanism that maximizes profits. The standard neoclassical growth model relied on the accumulation

of capital, labor, and technological change. This is the case for the Solow-Swan model, the Ramsey-Cass-Koopmans model, and all their subsequent extensions and refinements. Neoclassical growth models worked well under the following key simplifying assumptions: (i) no transaction costs; (ii) perfect information; (iii) fully rational homogeneous agents; and (iv) institutions taken as given. However, the advent of NIE brought the validity of these assumptions into question. Specifically, the new institutionalists were troubled by the existence of positive transaction costs, and thus the lack of perfectly competitive markets. In addition, NIE claimed that institutions are endogenous and that economic agents have bounded rationality, are heterogeneous, and do not possess all the information available in the market.

The approach of the new institutionalists rested on the concepts of transaction costs, property rights, and contracts, and on recognition of the importance of institutions in determining these three concepts. The “rediscovery” of institutions by mainstream economics was perhaps most influenced by Coase’s contributions to the theory of the firm and externalities. The standard description of the economy as an automatic process that equilibrates supply with demand by means of the price mechanism was first challenged by Coase in “The Nature of the Firm” (1937) with the introduction of the concept of transaction costs. By eliminating the need for contracts and negotiations among the many owners of the factors of production, the firm was seen as a way to reduce transaction costs, thus providing a rationale for the firm’s existence and for its vertical boundaries. The relevance of defining and enforcing property rights—a key element in studies attempting to link institutions and economic growth—gained prominence with the publication of “The Problem of Social Cost” (Coase 1960), in which Coase proposed bargaining, provided transaction costs are zero, as a solution to the problem of externalities. His insights on the matter again placed institutions at the forefront of economic research.

In addition to Coase (1960), other authors such as Alchian (1961), Demsetz (1967), Alchian and Demsetz (1973), and Williamson (1975) also underscored the relevance of property rights and contracts and their enforcement. These authors focused on the way these institutions altered economic behavior. Specifically, they emphasized the importance of property rights in circumscribing economic agents’ behavior toward each other regarding the obligations of contractual arrangements. Well-established property rights and contracts play a fundamental role in sanctioning and preventing opportunism, cheating, or other types of misbehavior that would be feasible and suitable in their absence. The lack of entrenched property rights and contracts thus constrains the proper functioning of markets and economic activity.

3.4. Other Avenues of Research within New Institutional Economics and the Significance of the Work of Douglass North

The vast theoretical and empirical research that characterized the resurgence of institutions with the arrival of NIE has broadened to include an enormous amount of approaches and methods. It should be mentioned, however, that most of these studies have succeeded in incorporating the quality and existence of institutions as key elements in defining the behavior of economic agents and, consequently, economic performance (Leite, Silva, and Alfonso 2014). The inclusion of the quality of institutions in economic analysis has thus reinforced the view that to function effectively and optimally, markets require the existence of institutions capable of resolving collective action problems. The absence of such institutions may result in an economy settling on a suboptimal equilibrium for a long period of time. Such a suboptimal equilibrium would in turn result in a lingering and diminished capacity for the economy to stimulate and sustain growth in the longer term. For example, through the analysis of property rights and the theory of contracts, NIE has provided some answers to agents' behavior in circumstances of imperfect information and uncertainty. Some prominent exponents of this strand are Hart and Holmstrom (1987), and Stiglitz (1990). Game theorists, for their part, have managed to explain economic agents' behavior within a specific institutional structure. Shubik (1975), a pioneer in this line of research, uses the definition of "rules of the game" to delineate the role of institutions. Others have used mathematical approaches to study the emergence of institutions. For example, for Schotter (1981), institutions arise spontaneously from the interaction among agents. For others, institutions appear naturally through self-organizing processes (Young 1993; Aoki 1996). Another strain of thought is evolutionary theory (Nelson and Winter 1982), which defines institutions as rules, patterns of behavior, or customs that evolve through time. Other NIE economists have worked on more government-related issues that are associated with the public choice field. For example, Olson (1965, 1982), within the framework of collective action, analyses how agents may misbehave by becoming free riders or by forming coalitions that influence institutional design. In this branch of thought, the design of institutions is not only the result of the pure interactions between agents, but also the outcome of their strong determination to change rules and economic structures directly through their own particular power. Within this framework, the government plays an essential role in designing and offering solutions to collective action problems (see also Ostrom 1990).

An important impetus to the study of institutional quality and its relevance for economic growth and development was provided by the work of North. Even some of his earlier work provided institutional change a greater role in determining growth. In *The Rise of Western World: A New Economic History*, North and Thomas (1973) gave prominence to an “efficient economic organization” as a main determinant of economic growth. Furthermore, they asserted that an efficient economic organization requires “the establishment of institutional arrangements and property rights that create an incentive to channel individual economic effort into activities that bring the private rate of return close to the social rate of return” (North and Thomas 1973, 1). The authors claimed that, through their impact on innovation, economies of scale, improving efficiency in factor markets, and reducing market imperfections, new institutional arrangements such as written contracts enforced by courts were largely responsible for successful European economic development.⁴ However, it was North’s influential 1990 book, *Institutions, Institutional Change, and Economic Performance*, that focused more directly on the evolution of countries and the role institutions have played in their development journey. Specifically, North places the intervention of the state in the design of institutions as a major determinant of the success or failure of countries to develop, asserting that “...countries are poor because the institutional constraints define a set of payoffs to political/economic activity that do not encourage productive activity” (North 1990, 110). Furthermore, North also posits a rationalization for institutional change. Specifically, he argues that institutional change takes place when those who have the power to transform institutions perceive “that they could do better by altering the existing institutional framework at some margin” (North 1990, 8). In a subsequent article, North claims that societies’ inherited belief systems are difficult to change, and thus might obstruct the assimilation of rules, laws, and other codes of conduct that have been successful in stimulating development in other regions of the world. In North’s own words, “Societies that get ‘stuck’ embody belief systems and institutions that fail to confront and solve new problems of societal complexity” (North 1994, 364). In an effort to better understand the way beliefs are formed and how these determine individuals’ interactions in society, North (2005) resorts to cognitive science and “mental models.” In his unrelenting effort to elucidate the way institutions explain long-run economic performance, North, Wallis, and Weingast (2009), developed a theory of “open and limited access orders.” As discussed below, this theory emphasized intra-elite coalitions and the

⁴ See also Chapter 4 in the present volume.

role of institutions in shaping prospects for growth and development. This analysis gave way to a large body of applied research in political science, law, and economics (Shirley 2008, and Menard and Shirley 2012).

3.5. Upsurge in the Literature on Institutions and Economic Growth and Development

In the mid-1990s a vast amount of studies started to address the relationship between institutional quality and economic performance. This outburst in the literature gained momentum from the perceived institutional vacuum and poor economic performance that characterized the ex-socialist regimes during the late 1980s in their transition from centrally planned economies to a system that embodied economic liberalization and free markets. The economic hardship observed during the transition of these ex-Soviet economies highlighted the relevance of the design of institutions that support the creation of markets, define the rule of law, property rights, and a proper regulatory framework, and set the stage for the appropriate development of entrepreneurial activity. As Coase indicated in his 1991 Nobel Prize lecture:

“The value of including such institutional factors in the corpus of mainstream economics is made clear by recent events in Eastern Europe. These ex-communist countries are advised to move to a market economy, and their leaders wish to do so, but without the appropriate institutions no market economy of any significance is possible.” (Coase 1991, 3)

A significant number of empirical studies developed during the 1990s on the relationship between economic performance and institutional quality produced a statistically significant relationship between these two variables. Cross-country data and multiple regression analysis, with institutional quality indicators among the explanatory variables, were used by most of these studies. Some of the most important studies in this area are worth noting.

Knack and Keefer (1995) is one of the earliest papers to use an aggregate measure of institutions in regression analysis. They use two composite indices of institutional development capturing elements of both the quality of institutions (quality of bureaucracy and corruption in government) as well as of institutions setting the “rules of the game” (contract enforceability, risk of nationalization, and rule of law). Their analysis concludes that institutions protecting property rights are significant predictors of economic growth. A

subsequent study by Knack and Keefer (1997a) analyzes 29 countries using trust and civic cooperation norms as indicators of informal institutional quality. The study finds that both indicators are positively associated with per capita gross domestic product (GDP) growth rates and with investment-to-GDP ratios. Knack and Keefer (1997b) examine the role of institutions on a developing country's ability to catch up with developed economies. They find that weak institutional indicators on the rule of law, corruption, and the risk of contract repudiation, among others, have a significant relationship with a country's ability to catch up and converge to more advanced economies.⁵ Ades and di Tella (1996) report that corruption is negatively correlated with investment and is associated with less independent judicial systems. Using a worldwide survey of 3,600 firms, Brunetti, Kisunko, and Weder (1997a) focus on institutional factors that affect the credibility and predictability of the rules affecting business establishments. The authors construct an index of the "credibility of rules" that entails variables such as the predictability of laws and policies, the reliability of the judiciary, and the lack of corruption. Their findings confirm that the credibility of rules matters for investment decisions and economic growth. Brunetti, Kisunko, and Weder (1997b) find that for 20 transition economies, the predictability of the institutional framework—particularly the security of property rights and political stability—are relevant in explaining a significant share of the differences in foreign investment inflows and economic growth.

Other authors find similar results. Clague et al. (1997) report that institutional indicators such as expropriation risk, rule of law, repudiation of contracts, quality of bureaucracy, and bureaucratic delays have a statistically significant impact on investment and output. Hall and Jones (1999) find evidence on the positive association between institutions and productivity. Kaufmann, Kraay, and Zoido-Lopaton (1999) report a strong correlation between institutional quality and development outcomes (GDP per capita, infant mortality, and adult literacy). Rodrik (1999) analyzes the relation between institutional quality and the sustainability of economic growth. He argues that internal social conflicts and weak conflict-resolution institutions explain why high growth rates have not persisted in some countries and why growth collapsed in many countries after the mid-1970s. His findings suggest that institutional quality is not only positively correlated with economic growth but also with its sustainability.

While the empirical findings of many of the studies provided support to the argument that institutional quality is a significant determinant of

⁵ Chapter 7 presents a variety of indicators that reflect public trust and satisfaction with institutions.

cross-country variations in economic performance, some methodological concerns called for caution in interpreting these results. Specifically, the presence of endogeneity concerns in which institutional quality (explanatory variable) may be affected by economic performance (dependent variable), or both the explanatory and dependent variables may be determined by other unobservable factors, reduced the reliability of the results. Some studies have attempted to address these endogeneity concerns with empirical strategies based on instrumental variables.⁶ These attempts have aimed to identify a causal link from institutions to economic performance and not the other way around. As described below, one classical example and seminal work along this line is Acemoglu, Johnson, and Robinson (2001), in which institutional quality is instrumented with settler mortality rates.

3.6. The Historical Perspective of Institutions

The historical perspective of institutions suggests that their original design in a country is a major determinant of the country's development path. According to this view, the institutional structure in a country becomes entrenched and difficult to transform, and hence institutions are "time persistent." Since current institutions are linked to previous institutions and to the events from which they originated, institutions become "path dependent." This implies that institutions from the past will influence the country's performance in the future unless a drastic overhaul of institutions changes the course of events. New or modified institutions tend to emerge because of deliberate policy adjustments in their design, or as a consequence of a significant external shock such as colonization, war, revolution, or an economic crisis (North 1990).⁷ Empirical studies largely conclude that early institutions affect present and future institutions and development outcomes even centuries apart.⁸

The colonization experience across the globe has served as fertile ground for studying the long-run development impact of institutions.⁹

⁶ Instrumental variable approaches have also come under scrutiny (Deaton 2010). Recent studies have produced more sophisticated techniques to examine the relationship between institutions and growth (Acemoglu et al. 2014).

⁷ Banerjee and Duflo (2014) argue that for some scholars, institutions are mainly products of historical logic, while for others, accidents, leaders, and decisions have a significant impact in their development.

⁸ See Chapter 6 for a detailed analysis of possible historical path dependence of institutions within the Caribbean.

⁹ Michalopoulos and Papaioannou (2013) present evidence that pre-colonial institutions also matter for current development.

Engerman and Sokoloff (1997, 2000, 2002) argue that factor endowments or initial conditions in former colonies, such as climate, geography, and precolonial population density, had profound and enduring effects on the long-run paths of institutional and economic development. According to their view, differences in factor endowments between the colonies predisposed their development paths toward those associated with different degrees of inequality in wealth, human capital, and political power.¹⁰ Furthermore, early differences in the extent of these inequalities not only affected growth, but also promoted the development of institutions that preserved these inequalities. That is, a scenario of extreme inequality and institutions favoring elites over much of the population in terms of economic opportunities allowed the elites to maintain their privileged status over time, but at the cost of society not realizing the full economic potential of the disadvantaged groups.

Along similar lines, Acemoglu, Johnson, and Robinson (2001) emphasize the role of institutions protecting property rights for a broad range of the population. They use settler mortality rates as an approximation of early institutional quality based on the rationale that high settler mortality rates among European colonizers would occur in regions characterized by elevated health hazards, where settlers were less likely to establish themselves for a long period of time and were thus less inclined to build “good,” long-run institutions such as guaranteeing property rights. In these high-risk locations, colonies were established with the aim of exploiting the natural resources of that specific area, and the only institutions created were those necessary for the maintenance of power and the extraction of wealth. On the contrary, low settler mortality rates would manifest in low-health-risk areas, where colonizers were presumed to stay longer and build institutions that would properly serve them in the longer term. In other words, in locations where settlers benefited from good weather, soil, land conditions, and lack of disease, they established large communities and shaped institutions to assure and secure their rights and properties. Broad-based institutions for property rights protection were of particular

¹⁰ Bruhn and Gallego (2012) find similar results but at the country level in the Americas. They find that within-country differences in levels of economic development are correlated with the type of activity performed in each region during colonial times. The authors provide evidence that supports the hypothesis that regions that were suitable for the activities that displayed economies of scale and depended heavily on labor exploitation, such as mining and plantation agriculture, reached lower levels of economic development in comparison to those regions with low precolonial population density that engaged in activities that did not display economies of scale, such as the cultivation of subsistence crops, cattle raising, and manufacturing.

importance to take advantage of industrialization opportunities brought about by the Industrial Revolution, thus leading to income divergence in those places with the presence of such institutions encouraging significant investments and growth (Acemoglu, Johnson, and Robinson 2002).

According to this view, the colonization strategy of the Europeans around the world that started in the 15th century depended on factors such as the natural endowments and resources in the colony, the health hazards for the settlers, and the settlers' intentions as to whether or not to establish themselves as a community for the longer term. Distinct colonization strategies resulted in different institutional quality and thus in cross-country variations in income levels. This explains why the institutional setting of the "extractive states" such as colonies in Africa, Central America, the Caribbean, and South Asia, differs from those of the "settler colonies" such as the United States, Canada, Australia, and New Zealand, where Europeans settled in large numbers (Acemoglu, Johnson, and Robinson 2001; Acemoglu and Johnson 2005; Shirley, 2005).

The literature has thus provided a good rationale for the marked differences in the institutional setting of the "extractive states" and that of the "settler colonies." However, why is it the case that the extractive institutions set up by the colonialists persisted long after the colonial regime ended? Acemoglu, Johnson, and Robinson (2001) and Young (1994), among others, have suggested that the persistence of extractive institutions after independence is associated with the fact that the elites in these societies opted to maintain these institutions and to benefit themselves from their presence. That is, not only is it costly and difficult to alter a preexisting institutional setting, but those with the means and power to exploit the rents of the extractive society prevent institutions from evolving into "better" institutions that have the potential to benefit the whole country.

The previous studies have inspired subsequent research on the impact of specific colonial institutions, such as land tenure institutions in India (Banerjee and Iyer 2005), slave trade in Africa (Nunn 2008), and the *mita* forced labor system in Peru (Dell 2010), among others. These studies have strengthened the view of institutions as key drivers of long-term development.

In the same manner in which different initial factor endowments or alternative colonization strategies by the Europeans resulted in dissimilar institutional quality in their respective countries, Acemoglu, Johnson, and Robinson (2005) and Acemoglu and Robinson (2012) present several cases in which the isolation of a source of exogenous differences in institutions allows for a situation in which a number of otherwise-identical societies end up with different sets of institutions, and hence with a

significantly different development and growth path. They use “natural experiments” involving a pair of neighboring countries that share many geographic features but have different histories—for example, the Democratic People’s Republic of Korea (North Korea) versus the Republic of Korea (South Korea)—to make the case for differing institutions as a determinant for alternative paths for development and growth.

3.7. Institutions as a Fundamental Determinant of Growth and Other Strands of the Literature

The case for institutions as a dominant contributor to the development path of countries was further enhanced by studies such as Rodrick, Subramanian, and Trebbi (2004), who estimate the respective effects of institutional quality, geography, and openness to trade on income levels for a large sample of countries. This study concludes that once the institutional variable is added, geography and trade do not have any additional explanatory power in determining growth and development. In a similar vein, Acemoglu, Johnson, and Robinson (2005) contrast the significance of three possible causes of long-run economic growth: institutions, geography, and culture. The authors claim that institutions are the fundamental cause because

“...it is the way that humans themselves decide to organize their societies that determines whether or not they prosper. Some ways of organizing societies encourage people to innovate, to take risks, to save for the future, to find better ways of doing things, to learn and educate themselves, solve problems of collective action and provide public goods. Others do not.” (Acemoglu, Johnson, and Robinson 2005, 397)

In Acemoglu and Robinson (2012, 45), geography and culture are dismissed as “theories that don’t work” in explaining different patterns of economic growth.¹¹ This stands in contrast to a strand of the literature that has emphasized culture or cultural variables (values and beliefs) as an important determinant of growth.¹² While some authors have regarded cultural variables as different from institutions, and thus as distinct explanatory variables for economic growth, others have seen the relationship between culture and institutions as complementary and as a two-way causal effect. This interaction and mutual feedback between institutions

¹¹ See also Rodrik, Subramanian, and Trebbi (2004).

¹² See also Clark (2009) and Mokyr (2016).

and culture has sometimes hindered identifying the specific contribution of each of these two variables to growth and development (Alesina and Giuliano 2015). Among this literature, Tabellini (2010) provides evidence on how culture, measured as generalized trust, respect for others, and confidence in individual effort, is associated with regional economic development in European nations. Algan and Cahuc (2007) use inherited social attitudes by second-generation immigrants in the United States (born under an equal institutional environment) to study the impact of culture on development across their parents' home countries. However, Gorodnichenko and Roland (2011) use genetic distance as an exogenous source of variation of cultural traits and claim that an individualist culture leads to higher levels of innovation and growth. Likewise, several studies have shown how cultural traits can be determined by past institutions (Tabellini 2010; Nunn and Wantchekon 2011), thus not only strengthening the idea of a two-way causality, but also the role of historical institutions.

In an article on prospects for economic growth, Rodrik (2013) emphasizes two key dynamics behind growth and its sustainability. The first is the domestic development of fundamental capabilities in the form of human capital and institutions, and the second is structural transformation aimed at industrialization. Poor economies can experience structural transformations even when skills are low and institutions weak, and thus undergo prolonged periods of growth. For its part, growth based on the accumulation of human capital and the quality of institutions is a slow, difficult, and costly process, as it takes time for these fundamental capabilities to yield results. However, as argued by Rodrik, as an economy evolves, the two forces of growth tend to complement each other, and eventually, human skills and institutional development become the dominant stimulus in driving the growth process. Moreover, "...if strong fundamentals do not eventually come into play, growth driven by structural transformation runs out of steam and falters" (Rodrik 2013, 5). Convergence with rich economies thus eventually depends on the accumulation of human capital and the procurement of high-quality institutions within the country. In a more recent article, Vianna and Mollick (2017) provide new evidence that supports the role of institutions in promoting economic development in Latin America. The authors find that each 3.9 percent improvement in per capita GDP is associated with a 0.1 percentage point increase in an aggregate measure of institutions that encompasses several variables such as the control of corruption, government effectiveness, political stability and absence of violence, regulatory quality, rule of law, and voice and accountability.

The study of institutions and their effect on economic performance has further shaped other strands of the literature in economics and political

science. For example, La Porta, Lopez-de-Silanes, and Shleifer (2008) focus on legal institutions and their relationship to growth and development.¹³ They argue that some legal systems may favor economic development more than others. Persson and Tabellini (2003) revisited the role of political institutions in influencing economic policies by investigating the policy and economic consequences of different forms of government and electoral rules.

Acemoglu (2003), Acemoglu, Johnson, and Robinson (2005), and Acemoglu and Robinson (2005) have also focused on the role of political institutions and their effect on economic growth. These studies claim that political institutions are an important determinant of economic growth because they set the stage for the establishment and development of economic institutions that affect growth. Economic institutions are thus endogenous and determined by the collective choices of society that are defined by the political power of its diverse members. The studies emphasize the fundamental importance of conflict and balance of power between the different groups or social classes (elites and the rest of the citizens) in the determination of political institutions. According to this view, the form of government, such as a dictatorship, democracy, and even a coup is the result of the balance of power among the different members of society. Under a dictatorship, economic institutions do not likely provide protection of property rights or equal opportunity for all the population. However, once an autocratic regime becomes threatened by social unrest, demonstrations, or even revolution, those in power (the elite) tend to make concessions to the rest of the citizens. These concessions can take the form of a reduction in the political power of the elites. This process of democratization would then give rise to economic institutions that are more aligned with the new balance of political power and form of government in place. Political conflict can thus lead to the emergence of democracy, but the consolidation of democracy will depend on following a balanced path between pro-majoritarian concessions and assuring some power for the elites.

North, Wallis, and Weingast (2009) and Khan (2010) shift the focus away from property rights and the differing types of colonial institutions toward intra-elite coalitions and the adaptive capacity of institutions as fundamental determinants of growth and development. According to this view, throughout human history, elites aimed to reach compromises among themselves and to limit access to political and economic organizations by nonelites. This allowed elites to share power and distribute rents among themselves. Moreover, elites used exclusionary institutions to promote the

¹³ A deeper analysis of rule of law and human capital development institutions is provided in Chapter 4.

development of a stable equilibrium (natural state) that left nonelite citizens without access to the means of power and wealth. Under this hypothesis, the elites have used their privileged status to preserve those institutions that allowed them to prolong their grip on power and wealth as long as possible. Khan (2010) also emphasizes the distribution of rents among elites and other powerful groups as an instrument to bring about social stability. However, the author emphasizes the existence of a trade-off between growth-enhancing institutional reforms and declining social stability, as powerful groups resist reform attempts that alter the share of rents.

Regarding the implementation of policies aimed at promoting macroeconomic stability, and thus establishing the conditions for prolonged and sustained economic growth, the analysis of institutions has made enormous progress in emphasizing the relevance of transparency, clarity, and certainty in economic policymaking. Specifically, fiscal policy rules have been conceived as a means for achieving greater fiscal discipline, confronting excessive fiscal deficits, and implementing procyclical policies (Alesina and Perotti 1995; Debrun and Kumar 2007; Kopits 2001). On monetary policy implementation, central bank independence, along with an inflation mandate and greater transparency, has been established as a means of insulating monetary policy from short-term political pressures, and is thus associated with lower and more stable inflation (Blinder 1998; Debelle and Fischer 1994; Rogoff 1985; Walsh 2003). The argument for monetary and fiscal institutions or rules is based on the phenomenon of temporal inconsistency of policymakers (Kydland and Prescott 1977), which suggests that monetary and fiscal authorities can be tempted to use their policy instruments to achieve short-term objectives, such as stabilizing output over the business cycle, and risk the achievement of their long-run goals (price stability, fiscal discipline, and debt sustainability). Hence, the use of rules is designed to provide more clarity and certainty to economic agents and avoid the “inflation or deficit biases” that the corresponding monetary or fiscal authorities might be inclined to display (Wyplosz 2005).¹⁴

3.8. Where Do We Go from Here?

As discussed in this chapter, the last 50 years have witnessed a huge amount of progress in terms of our understanding of the role of institutions in promoting growth and development. Both theory and empirical evidence give strong support to the argument that the quality of institutions is an important determinant of growth, development, and the well-being of countries

¹⁴ See also Chapter 5 of the present volume.

in the longer term. The positive association between institutional quality and economic performance takes place through numerous and different channels and holds for assorted indicators of institutional quality. Given this evidence and the clear understanding of the relevance of institutions for economic performance, an obvious question one can pose is where do we go from here? Alternatively, what are the most relevant institutions for a country to set itself on a path of sustainable development and growth?

This is precisely the question that (Rodrik 2000) presents in his seminal article titled “Institutions for High-Quality Growth: What They Are and How to Acquire Them.” In this article, the author no longer questions whether institutions matter, but more specifically, “which institutions matter and how does one acquire them” (Rodrik 2000, 4). He defines a collection of non-market institutions that allow markets to perform adequately. His view is that these institutions carry out regulatory, stabilizing, and legitimizing functions that are complementary and supporting elements to a well-functioning market economy, and that their absence explains the divergence of growth paths among economies. Rodrik suggests a taxonomy with five types of market-supporting institutions: (i) property rights institutions; (ii) regulatory institutions; (iii) macroeconomic stabilization institutions; (iv) social insurance institutions; and (v) conflict management institutions.¹⁵ A clearly defined system of property rights and the rule of law provide the proper incentives to invest and innovate. A regulatory framework curbing fraud, anti-competitive behavior, moral hazard, and corruption is expected to prevent market failures. Fiscal and monetary institutions are considered important prerequisites for macroeconomic stabilization and sustainable growth. Institutions that provide social insurance are also understood as important preconditions to legitimize market economies and to “...maintain social cohesion in the face of large inequalities and volatile outcomes” (Rodrik 2000, 9). For their part, representative political institutions, democracy, and the judiciary are some of the institutions needed for conflict management. On the question of how to acquire or achieve having good institutions, the author defines democracy as a meta-institution for building such institutions and provides evidence to support the assertion that participatory political regimes are conducive to higher-quality growth. This is the case because democracies tend to produce better institutions that are more aligned to local circumstances.

The accumulated knowledge on the role of institutions, as evidenced by this literature review, leaves no doubt about the relevance of institutions

¹⁵ Some elements of Rodrik’s taxonomy are analyzed in detail in specific chapters of this book. Chapter 4 analyzes property rights and regulatory institutions. Institutions for macroeconomic stabilization are studied in Chapter 5.

for the sustained prosperity of nations. Furthermore, economic theory has also made considerable progress in pointing out which institutions are more critical to facilitate continued growth and development. However, the ability of countries to alter their institutional setting and establish high-quality institutions ultimately depends on a deep understanding of the historical origins and evolution of institutions in the country. Knowing what quality institutions should look like is thus not sufficient to develop and sustain these institutions, since any alteration of the prevailing institutional structure would in turn need to be built considering the dynamics of the previous setting. The historical foundations of institutions in a country have much to do with the current institutional setting, and a thorough knowledge of those foundations is paramount for any alteration of the system. In other words, to be successful, institutional reform must adapt and consider the specific features of the country itself. As a result, effective institutional reform might not necessarily look the same everywhere (Rodrik 2003).

The question then goes well beyond whether institutions matter for economic performance. Deeper and still unanswered questions need to address the best way for countries to acquire the correct institutions, and how to customize institutions to specific country contexts. While there are yet unresolved concerns about the optimal sequencing of institutional reform, the interaction between formal and informal institutions, and the robustness of institutional design, among other issues; the review in this chapter has identified key areas to keep in mind to attain a high quality institutional framework. Institutions related to the rule of law (e.g., well-defined property rights and the enforceability of laws) as well as institutions that guarantee appropriate development of human capital have been shown to be important determinants of growth and prosperity. Hence, Chapter 4 will provide a more detailed assessment of the evidence on these types of institutions. Likewise, economic institutions aimed at macroeconomic stabilization, have been shown to be relevant in supporting better economic performance. Thus, Chapter 5 will identify key economic institutions, provide possible transmission mechanisms between such institutions and development, and review the available evidence on the effectiveness of each type of economic institution toward supporting growth. By identifying critical institutions for development, Chapters 4 and 5 will therefore set the stage for the specific institutional assessments of the Caribbean countries reflected in the individual country chapters in the last section of this volume. Consequently, we hope that this volume will help different stakeholders in the Caribbean to understand and consider institutional amendments with the potential to deliver increased development and well-being to their countries and citizens.

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Rule of Law and Human Capital Institutions

Christian Dippel

There is an abundance of correlates of economic developments, among which researchers have tried to separate causation from correlation. Richer countries tend to have higher education levels, trade more with other countries, have stronger state capacity, and have more and better financial intermediation and institutions that are more conducive to growth. For each of these factors, there are convincing arguments that, rather than being a mere correlate of development, the factor is among development's fundamental root causes. As evidenced in Chapter 3, among these factors, good institutions have received significant attention in the literature. From the general review provided in Chapter 3, institutions associated to the rule of law and human capital development have been identified as important sets of institutions. This chapter focuses on these institutions by going deeper into the evidence linking them with growth and development. The main objective is, therefore, identifying which institutional arrangements related to the rule of law and human capital development have been shown to be relatively more important. Such identification will then guide the analyses of the institutional conditions within Caribbean countries documented in the chapters that integrate the third and fourth sections of this volume.

For the question of how to define institutions, one needs look no further than Douglass North's widely accepted definition: "Institutions are the rules of the game in a society or, more formally, are the humanly devised constraints that shape human interaction....They structure incentives in human exchange, whether political, social, or economic" (North, 1991, 3).¹

¹ See Chapter 3 in this volume for a deeper discussion of the definition of institutions and why such institutions may plausibly be the fundamental cause of differences in economic development.

The first “modern” instance of the argument as to why these rules of the game in turn affect a nation’s economic success dates to North and Thomas (1973), who argue that the origin of economic growth comes from “efficient institutions” that discipline the government to delineate, protect, and enforce property rights, and which incentivize individuals to undertake socially beneficial activities.² Such socially beneficial activities include engaging in fair market competition, innovation, and the accumulation of both physical and human capital. These are often seen as *proximate* determinants of economic development in the sense that they are caused by the institutions that are the more fundamental determinant of economic development.

Because this chapter’s focus is on the *empirical* evidence for the importance of institutions governing the rule of law and human capital development, it will begin with a brief chronology of this evidence. Initially, the empirical foundations of the study of institutions did not depart from case studies, such as North and Weingast’s (1989) interpretation of England’s development following the Glorious Revolution in 1688. In the 1990s, evidence of a more statistical type started to be brought to bear on the issue.

One of the first analyses to use such evidence was De Long and Shleifer (1993), who contrasted two types of reign in European countries from 1050 to 1800: autocratic rule by princes, and all others, prominently merchant-ruled city states such as the Dutch Republic. The data support the conclusion that autocratic rule was detrimental to consequent urban population growth when compared to merchant rule that was more broadly inclusive. The authors argued that the most distinctive difference between the two regimes was property rights, which were limited or nonexistent under autocratic rule.

The first macroeconomic study that took the importance of statistical evidence for institutions seriously was Hall and Jones (1999). They showed that the standard neoclassical drivers of growth (e.g., physical and human capital accumulation) left plenty of the variation in economic growth unexplained, and they suggested that this “Solow residual” in growth (Solow 1957) could largely be accounted for by institutions.³ Hall

² The importance of the “right” institutions for economic development has been recognized by scholars of various time periods, and famously by the founding father of modern economics, Adam Smith, in 1755: “Little else is required to carry a state to the highest degree of opulence from the lowest barbarism, but peace, easy taxes, and a tolerable administration of justice, all the rest being brought about by the natural course of things.” See Chapter 3 in this volume for an overview of the history of thought connected to the “new institutional economics” model and this older literature associated with the classic 18th, 19th and early 20th century economists.

³ They called this “social infrastructure.”

and Jones went further, arguing that even differences in physical and human capital accumulation themselves could in large part be explained by institutions. In other words, they argued that many of the standard neoclassical drivers of growth were proximate rather than fundamental causes of growth.

In the late 1990s and early 2000s, the literature evolved in two important ways. First, rather than taking conventional measures to the data and then speculating that the statistically unexplained residual was explained by institutions, researchers tried to measure institutions directly and include them as explanatory variables in regressions. Second, researchers started to take the “identification” of causal effects seriously. This was born of a realization that too many measures of broadly “good” things correlated in the data on socioeconomic development, and that by interpreting all these as causal one would invariably fall for the logical fallacy of “cum hoc ergo propter hoc,” meaning mistaking correlation for causation. In the quest for the statistical identification of causal determinants of economic development, researchers recognized the value of “natural experiments,” meaning accidents of history whereby, for example, Cuba was colonized by the Spanish and Barbados by the British.

In this focus on “natural experiments,” developing and emerging economies such as most of the Caribbean countries took center stage because this was where many of the “accidents of colonial history” had happened. An important consequence of this research push has been a rapid increase in the amount of good and reliable data that are being collected for developing and emerging economies, including on such subtle and hard-to-measure areas as good institutions. Some studies stand out for having pushed the empirical evidence for the importance of institutions in this period.

Engerman and Sokoloff (1997) focused on the comparison of “neo-European” settler colonies and extractive colonies and traced differences today back to historical inequalities rooted in extractive colonies’ suitability to plantation crop cultivation.⁴ The suitability for crops such as sugar, coffee, and tobacco encouraged the formation of a highly concentrated quasi-feudal elite who reaped the rents accruing from the plantation crops. This initial inequality then persisted through institutions advantaging elite members and continues to shape policies even today. The British colonies in North America experienced a different path of development. Being unsuitable for large monocultures, small family-owned farms reaped little economics of scale from their activity. The resulting relative economic

⁴ The term “neo-Europe” was coined in Crosby (1986).

equality in turn favored the development of institutions favorable to long-term growth.

Acemoglu, Johnson, and Robinson (2001) provided what was then the best empirical evidence that institutions matter. They focused on an institutional measure called “the protection against expropriation risk” and its effect on per capita income. Taking identification seriously, Acemoglu, Johnson, and Robinson (2001) sought an “exogenous source of variation” in this institutional measure and for this reason turned to a historical natural experiment. They established that European colonialists had varying incentives to set up different institutions upon their arrival in the Americas. High mortality among initial European settlers incentivized the creation of large-scale extractive plantations fueled by slave labor and the corresponding institutions, while low mortality rates allowed for the settlement of Europeans who then replicated European institutions to secure property rights for themselves in places such as Australia, the northern United States, and Canada. These institutions then persisted until the present day. Acemoglu, Johnson, and Robinson (2001) provided compelling evidence for this narrative.

La Porta et al. (1998) focused on the role of legal institutions on investor protection. Following Hayek’s (1960) argument by which economic liberties precede development, they inquired into the role of different traditions in legal systems. Especially, they asked how these affect the enforcement of investor property rights and hence the diversification of ownership. The main dichotomy is between common law originating from England and civil law based on Roman law. The legal system was among the legacies of colonialization in that former colonies modeled their legal institutions following one of these traditions. La Porta et al. (1998) found that while common law systems facilitated strong investor protection, superior contract enforcement, better property rights protection and developed capital markets; legal systems derived from civil law traditions did so to a lesser degree, if at all. Then, La Porta et al. (2008) further showed that these differences in legal institutions also determine differences in economic development across countries as measured by corruption incidence, labor market participation, employment and economic growth.

More recently, Anderson (2018) investigates how marital property law in Africa affects women bargaining power to negotiate safer sex practices with their spouses and how this has affected HIV infection rates. While traditional common law offers better investors protection, it also embeds weaker marital property laws for women. As such, in terms of women’s rights, traditional civil law outperforms common law. Civil law provides recognition of household work, joint property ownership within marriage,

and protects wives upon marital dissolution. However, traditional common law provides none of these features. Exploiting the fact that African common law countries have not amended these disadvantageous features for women (as opposed to western common law countries where these features have been amended in favor of women), the author shows that common law regimes in Africa are associated with reduced bargaining power of women within marriage, lower incidence of safer sex practices by their husbands (i.e., utilization of contraceptive methods that reduce the risk of HIV transmission), and increased female HIV infection rates originating from their husbands within monogamous marriages. Findings are consistent with the view that weaker property rights are negatively associated with development.

4.1. The “Policies Challenge” to the Institutions View

Chapter 5 in this volume surveys arguments about the importance of macroeconomic policies, especially those having to do with fiscal and monetary economics. There is no question that such policies are important. There is, however, a question as to whether they are important beyond the good institutions that underpin them. In other words, there is a question whether policies are a proximate or fundamental cause of growth.

Some caveats need to be applied when trying to answer this question. One is that the distinction between policies and institutions is often not a sharp one. If institutions are rules of the game, then one could argue that policies could also be considered institutions. A good way to draw the distinguishing line is probably to ask how easy a rule is to change. For example, laws can only be passed within the limits of what a country’s constitution allows. Within that framework, laws can be amended quite easily. In that sense a constitution can better be thought of as an institution, and a law should better be viewed as a policy.

A second caveat is that the question of whether better policies are designed and implemented as a result of better institutions is not of practical importance to the policymaker who is designing a policy in a given institutional framework. It is, however, of practical importance when policymakers can actually design institutions, and it is therefore a question of more than academic interest. For example, international agencies could presume that trade and macroeconomic policies conducive to growth can just be adopted (Collier and Dollar 2001). However, if such policies require the right institutions, then simply “adopting good policies” seems a less promising recommendation, since the required institutional features cannot be adopted as easily.

Some researchers have attempted to answer this question by carefully studying the data. Easterly and Levine (2003) empirically investigate the relative importance of policies and institutions. They show that policies do not have a direct effect on economic development once differences in institutions are considered, and hence conclude that institutions trump policies in determining development.⁵ Easterly (2005) casts further doubt on national politics mattering. Analyzing the economic models that scholars and multilateral development agencies have used to argue for the growth to be reaped by policies, he concludes that these presume the existence of an “incredibly complex set of institutions” whose development “is probably a long historical process.” Surveying the empirical literature on whether policies or institutions are deep determinants of economic development, he finds little evidence that they are and concludes that most differences in income levels across countries, while associated with policies, ultimately derive from deep, fundamental factors—most likely institutions which themselves resulted from the different historical experiences of countries.

While the evidence in Easterly and Levine (2003) and Easterly (2005) shows that institutions trump policies *on average*, this cannot imply that policies do not matter at all. Taking central bank independence as an example (covered in Chapter 5), a cursory recent comparison between Russia’s careful and measured central banking policies and Japan’s rather reckless ones would suggest central bank independence is neither fully necessary nor fully sufficient to ensure good monetary policy (although it certainly helps). Similarly, democratic elections are clearly not enough to ensure fiscally responsible government, although, again, they may help.

A particularly strong defense of the importance of policies over institutions happens to come from research that relies on the comparison of two Caribbean islands, Jamaica and Barbados. Henry and Miller (2009) argue that the primacy of institutions cannot possibly explain the different growth experience of Barbados and Jamaica, because both countries share an identical institutional legacy. Instead, they trace the two countries’ vastly different growth experiences to macroeconomic policy. While Jamaica’s ruling party in 1972 nationalized companies, increased tariffs, and raised government expenditure, resulting in high inflation rates, Barbados kept a low government deficit, remained more open, and managed to control inflation. According to Henry and Miller (2009), this supports a view by which policies, rather than institutions, determine success in

⁵ Easterly and Levine (2003) also study the role of endowments, which refers to direct effects of the geographic environment on production, such as the suitability of the soil or crops or minerals there.

economic development. However, as the discussion in Chapter 6 in this volume suggests, the arguments of Henry and Miller (2009) are based on a false premise because there was in fact a lot of historical institutional variation even just across the British Caribbean. Indeed, no serious historical account of Jamaica and Barbados can claim that they shared the same institutional legacy when they entered the post-independence period (Patterson 2014; Dippel, Greif, and Trefler 2015; Carvallo and Dippel 2016).

In summary, the relatively scarce evidence on this question seems to suggest that better institutions precede better policies. However, common sense demands this to be taken with a grain of salt. Institutions can clearly never be the only determinant of good policies. Even if the data suggest that they trump policies in a statistical sense, when it comes to explaining good outcomes, it needs to be acknowledged that these data are often highly imperfect. And indeed, there is some compelling evidence for the existence of other sources of variation in policies beyond institutions.⁶ However, while it is complicated to establish strict chronological links between institutions and policies, it is evident that good institutions and good policies are associated and complementary. As such, the review provided in this chapter will focus on the evidence regarding which rule of law and human capital institutions matter and on their ultimate effects on growth and development.⁷

4.2. The “Human Capital Challenge” to the Institutions View

Glaeser et al. (2004) make a more general argument against institutions as a fundamental cause of economic development. The authors believe in the primacy of human capital over institutions and argue that even in highly unequal or autocratic regimes, educated elites, or often single dictators, implement positive institutional reform by pursuing growth-enhancing policies. They find evidence for this in the experiences of Asian countries such as China and South Korea, which escaped dire poverty under the rule of autocratic leaders. Secure property rights and other institutional features, believed to be conducive to economic growth, are then the choices of enlightened autocrats rather than forced being upon them by political constraints. According to this argument, institutions are themselves

⁶ For example, one body of evidence finds that policymaking depends on the beliefs that policymakers hold, and not institutional constraints as such (Rodrik and Mukand 2016; Benabou and Tirole 2006). Relatedly, Passarelli and Tabellini (2017) show that political unrest fueled by emotions can shape public policy and institutions.

⁷ Another interesting question is which non-institutional aspects also matter for the adoption of policies. Unfortunately, such question goes beyond the scope of this volume.

often only a proximate cause of development and human capital is a more fundamental one. The argument of Glaeser et al. (2004) is also a central tenant of Lipset's (1959) "modernization theory," which argued precisely that education is the causal force driving institutional differences.

Before providing systematic evidence for these arguments, it should be noted that they express strong concerns regarding the main measures of institutions used in the literature. Neither expropriation risk nor government effectiveness, they argue, distinguishes between dictatorial choice and constrained adoption, and only the latter factually measures institutions. Constraints on the executive, another widely used measure in the literature, is extremely volatile in the data, as it reflects electoral outcomes rather than durable institutions.⁸ Cautiously concluding that some of the most widely used measures of institutional quality do not match well with the concept they are supposed to proxy for, Glaeser et al. (2004) then make their case that even when taking these measures seriously, modern panel data hint at the importance of human capital rather than institutions being the core determinant of economic development. To do so, they analyze the timing of changes in institutions, human capital, and growth across countries in the second half of the 20th century. The data show that initial human capital often precedes improvement in institutional quality, and hence seems more important in determining economic growth.

To date, the question of the direction of causality between human capital (and its primary input, education) and institutions is far from settled. On one hand, Glaeser et al. (2004) argue that some of the best evidence for the importance of institutions could also be construed as evidence for the importance of human capital. For example, they argue that the historical case outlined in Acemoglu, Johnson, and Robinson (2001), by which early colonizers set up institutions that persisted over time, is equally, if not more, supportive of a narrative by which colonizers brought their own human capital.⁹ On the other hand, Acemoglu et al. (2008) document that across countries, changes in the average years of schooling between 1970 and 1995 are unrelated to changes in measures of institutional quality in the same period once country-specific unobservable factors are statistically accounted for.

⁸ The various measures of institutional quality will be discussed in great detail in the next section of this chapter.

⁹ Some years after their initial contributions, La Porta, Lopez-de-Silanes, and Shleifer (2008, p.28) discussed their claims in light of the recent evidence available at the time. In doing so, they asserted that "the evidence on the relationship between institutions and aggregate growth more generally, which seemed substantial a few years ago, has been crumbling."

To a large extent, the debate boils down to what should be controlled for in studying the statistical relations between growth, education, and institutions. The fact is that in the post-World War II (and post-colonial) period there was a worldwide, simultaneous increase of both human capital levels and institutional quality. A researcher who believes that both were caused by a common underlying trend would include year fixed effects in a regression to wash out this common trend, and as a result the relationship between changes in human capital and institutions disappears. A researcher who does not believe in such an underlying trend would not include year fixed effects and would find a statistical relationship between changes in human capital and institutions.

Over the last decade or so, additional evidence has accumulated that the identity and history of people matters. However, this evidence has not undermined the importance of institutions but has rather complemented and expanded it by suggesting an increasingly nuanced notion of institutions that incorporates informal “cultural” factors such as trust and social norms.¹⁰ Nunn and Wantchekon (2011) are an excellent example. In earlier work, Nunn (2008) identified the negative effect of the slave trade in West Africa four centuries ago on contemporary development. In trying to understand the channels behind this finding, Nunn and Wantchekon (2011) provide compelling evidence that the slave trade’s long shadows negatively affected modern individual-level trust values. Trust in others, the fabric of societies and a requirement for the adoption of institutional frameworks conducive to growth, was destroyed and a culture of mistrust was established that persisted over time.¹¹

Research by Putterman and Weil (2010) perfectly summarizes this new “synthesis view” in which human-embedded cultural traits straddle and obscure the boundary between institutions and human capital. The authors attempt to control for the human capital embedded in each country’s population origins by constructing population flows between modern day countries since 1500. For instance, the United States has little to no history of organized statehood north of the Rio Grande, but the migrants to the United States who make up the vast share of its modern population in fact did move there from locations with a comparatively longer history of statehood. Putterman and Weil (2010) show that the

¹⁰ For a comprehensive treatment of the topic, see Mokyr (2016). Also see Chapter 7 of this volume for evidence regarding trust in several institutions across the Caribbean.

¹¹ Related evidence on the persistence of cultural traits is provided in Alesina, Giuliano, and Nunn (2013), Becker et al. (2016), Grosjean (2014), and Voigtländer and Voth (2012), among others.

historical origins of a country's people explain much of today's differences in development. They argue that two explanations are consistent with this fact. On one hand, people may have set up the growth-favoring institutions (executive constraints, expropriation risk, and government effectiveness) from their origin country in their new country of residence. These then persist and bring modern-day economic development.¹² This explanation of development is essentially one of institutional transplantation. On the other hand, people brought with them specific cultural traits such as trust, self-control, respect, and thrift that are conducive to growth and are passed to each new generation. This is essentially a story of cultural transmission. Taking advantage of a range of existing data on such variables, Putterman and Weil (2010) find evidence in support of both explanations.¹³

What does all this mean for policymakers looking for practical solutions to concrete problems? While a large body of research suggests that adopting good policies is more difficult without the right institutions, and that adopting the right institutions is in turn more difficult without the right culture, both of these insights are empirical regularities more than laws of historical determinism. Just as good policies can be implemented within a range of institutional settings, so too can good institutions be implemented within a range of historical circumstances and cultures, for example, at different levels of inequality or ethnic divisions.

The remainder of this chapter and the subsequent chapter will make no more reference to policies and culture, focusing instead on an in-depth discussion of specific formal institutions identified in Chapter 3 as important for growth and development. This chapter will cover institutions related to the rule of law, property rights, judicial independence, education, and public health, while Chapter 5 will cover economic institutions such as those in charge of fiscal and monetary policy, as well as financial and real sector regulation.

¹² Note the difference from Acemoglu, Johnson and Robinson (2001), who, as indicated earlier, argue that migrants to the new world chose which institutions to set up in the colonies depending on their feasibility due to geography. The claim by Putterman and Weil (2010), similar to that of Easterly and Levine (2003) leaves less room for decision and renders institutions, culture, or whatever it was that then caused further growth much less of a deliberate choice.

¹³ See Knack and Keefer (1995) and Tabellini (2010) for empirical evidence in this vein and Bisin and Verdier (2001) and Doepke and Zilibotti (2008) for theoretical frameworks. Spolaore and Wacziarg (2013) provide an overview of the literature on cultural transmission, while Alesina and Giuliano (2015) survey the literature linking culture and institutions.

4.3. Which Institutions Matter for the Legal, Education, and Public Health Systems?

The aim of this chapter is to summarize what we know about the legal, judicial, educational, and health institutions that perform best in improving citizens' lives. The discussion will benchmark different institutions by their effect on economic development.

4.3.1. *Institutions that Improve Private Contracting and Institutions that Limit the Predatory State*

Acemoglu and Johnson (2005) compare the importance of “property rights institutions” that protect citizens against expropriation by the state or powerful elites with that of “contracting institutions” that facilitate and secure private contracts between citizens. To do so, they use existing measures from the institutions literature, which are discussed briefly below.

The most common measure of property rights institutions was first introduced into the literature by Knack and Keefer (1995). They used an institutional indicator created by Political Risk Services, a private investment risk assessment company. Their main indicator measures protection against expropriation of private agents by the government. The measure assesses the risk of outright confiscation and forced nationalization for foreign investors. This measure forms an almost perfect empirical counterpart of North's (1990) definition of the “rules of the game” between citizenry and government, and has since been widely used, including by Acemoglu, Johnson, and Robinson (2001).¹⁴

The most common measure of contracting institutions was introduced into the literature and originally collected by Djankov et al. (2003), who joined forces with the largest international association of law firms to compare the exact procedure required for resolving disputes across more than a hundred countries. They do so for two exemplary cases, tenant eviction due to lack of payment, and collecting a bounced check. Based on this, they created a measure of *legal formalism*. Consistent with the earlier findings by La Porta et al. (1998) and a literature in comparative legal history, they identify differences between families of law. Civil law countries tend to regulate dispute resolution more heavily than common law countries do. This distinction matters: legal origins explain almost half of the variation across countries in legal formalism.

¹⁴ See the introduction of this chapter as well as Chapter 3.

Acemoglu and Johnson (2005) take these two measures and “horse race” them against one another in terms of their importance for economic development.¹⁵ In a cross-section of countries, both property rights institutions and contracting institutions are strongly correlated with a host of outcomes such as economic growth and investment rates. However, these correlations do not imply causation, meaning there is a danger of falling for the “cum hoc ergo propter hoc” fallacy. For example, the correlations are similarly supportive of an argument in which the direction of causality runs from the economic outcomes to institutions.

To remedy this concern, the authors rely on an instrumental variable identification strategy that uses only that part of the variation in property rights institutions and contracting institutions that is in turn caused by some exogenous or random shocks.¹⁶ A key contribution of Acemoglu and Johnson (2005) was that in their case the instrumental variable strategy allowed not only for the identification of a causal effect of one institution, but also for a clean “unpacking” of the two types of institutions. Using this strategy to obtain plausibly exogenous variation in (and therefore causal effects of) property rights institutions and contracting institutions, they find that property rights institutions matter strongly for economic growth and investment, whereas contracting institutions matter primarily for financial intermediation. They provide a compelling explanation for this: contracting institutions allow private agents (e.g., firms and households) to circumvent formal institutions (or a lack of them) with private contracts and with reputation built through repeated contracting. However, contracting institutions leave the interaction between private agents and the state unaffected, particularly the ability of private agents to protect their investments from the state’s “grabbing hand.” As such, both property rights and contracting institutions have positive effects on economic growth, but property rights institutions matter more than contracting institutions. In summary, this implies that protecting private agents from expropriation by the state is even more important than facilitating private contracting (which also matters). In fact, it is likely to be the single most important institutional conditional for economic development.

¹⁵ Acemoglu and Johnson (2005) also consider alternative measures of “contracting institutions,” such as the number of procedures required to resolve court cases revolving around commercial debt. As well, they consider alternative measures of property rights institutions such as constraints on the power of the executive, a measure coded by the Polity IV Project (Gurr, Marshall, and Jagers 2016).

¹⁶ The authors draw on earlier work by Acemoglu, Johnson, and Robinson (2001) and La Porta et al. (1998) for suitable instrumental variables for this case.

La Porta et al. (1998) and Djankov et al. (2003) are focused on legal formalism; their research focused on private agents' ability to use a country's legal code and norms to write contracts. Neither of them addresses the importance of the just and impartial enforcement of these contracts by the judiciary. This gap is filled by another slight permutation in the same core research team, La Porta et al. (2004), who find that two dimensions of the judicial system predict measures of freedom, which in turn matter for economic development. The first of these dimensions is judicial independence, meaning the separation of the creation and factual implementation of laws. It is measured by the length of the tenure and hence the strength of the independence of judges in a country's supreme court and administrative courts. Stronger judicial independence is statistically associated with higher levels of both economic and political freedom. These two outcomes are in turn proxied by a multitude of variables, including the aforementioned measure of the number of procedures and an index measuring the level of worker protection for economic freedom, as well as indices of political rights and human rights for political freedom. The other relevant dimension focused on by La Porta et al. (2004) is constitutional review, which is the ability of courts to limit the exertion of power by the legislative and executive branches, insofar as that power is controlled by a high court, in terms of whether that exertion of power complies with a country's constitution. They find that this measure is strongly associated with political freedom. A more balanced division of power in a country is critical to the level of its inhabitants' political freedom. The notion of judicial independence sits somewhere in between the distinct property rights institutions and contracting institutions that were articulated in Acemoglu and Johnson (2005). As such, there is no well-identified estimate of their separate quantitative importance. However, both of the La Porta et al. (2004) measures are only available for a relatively small set of 68 countries, omitting most developing and emerging countries.

4.3.2. Educational Institutions: Schooling

As discussed earlier within this chapter, human capital (as measured by education) is both a proximate and a fundamental determinant of economic development in the sense that education is partly something that just grows with economic development, but also partly a true requisite of development.

The first macroeconomic study to seriously estimate the effect of education on aggregate gross domestic product (GDP) growth was Mankiw, Romer, and Weil (1992). They showed that changes in education (human

capital) can account for a substantial part of the difference in growth rates and income levels across countries. However, human capital is also the outcome of (educational) institutions, and because the Mankiw, Romer, and Weil (1992) study preceded much of the newer institutional literature it did not include measures of institutions. Therefore, their estimated effect of education on growth needs to be viewed as a composite of the true (fundamental) effect of education on growth and its “proximate effect,” whereby education merely proxies for unobserved changes in institutional improvements.

Unfortunately, neither the broader literature on institutions nor the broader literature on the effects of education on cross-country economic development have all that much to say about educational institutions, for example, teacher hiring practices, monitoring of teacher quality and effort, the ability to fire underperforming teachers, and the scope for parental scrutiny and involvement. Instead, the literature on the effects of education on development is mostly focused on years of schooling, meaning the average years of schooling of a country’s workers. This has long been the go-to measure of education for most researchers, because of the obvious upside of being the most readily available cross-country measure.

One way in which the importance of educational institutions shows up indirectly is in measures of the disparity of the *quality* of education. One of the earliest studies on the quality of education was Hanushek and Kimko (2000), who focus on actual educational achievement as revealed in tests of cognitive skills. They find that these proxies for the quality of schooling are strongly related to economic growth and are easily more powerful predictors of economic growth than measures of quantity of schooling, meaning years of education. Not only does this suggest that policymakers should focus on the content and quality of schooling as opposed to the ill-advised focus on mere years of education, but also points to the importance of educational institutions. This is because educational institutions are likely to be at the heart of differences in the quality of education.

Hanushek and Woessman (2012) provide further evidence along these lines. The dominance of school quality over quantity in explaining economic growth rates withstands closer inspection and does not statistically depend on only the East Asian countries.¹⁷ As a case in point, in the 1960s Latin America had higher levels of years of schooling than any other developing region in the world, but these levels failed to materialize into economic development. This fact is explained because the

¹⁷ Education quality in this study is measured through the average country level performance on the Organisation for Economic Co-operation and Development (OECD)’s Programme for International Student Assessment (PISA).

quality of Latin America's education was also the lowest among the countries studied.

Closely related to the issue of educational quality is the issue of teacher quality. Chetty et al. (2011) used the random allocation of students to classes generated by a program called Project STAR to examine the long-run outcomes of different and experimentally varied class (and teacher) characteristics on students' later likelihood of college attendance and home ownership. They find that experienced teachers tend to have long-lasting effects on individuals. In further research they confirm the positive effect of experienced, high-value-added teachers on student test scores and a multitude of outcomes later in life, including earnings and retirement savings (Chetty, Cook, and Putterman 2014).¹⁸ More recently, in a large-scale experiment in Ecuador's kindergarten schools, Araujo et al. (2016) show that teacher quality is a key cause of learning in math, language, and executive function. However, while parents recognize teachers who are better, they do not compensate for lower teaching quality, for example, by investing more resources into their kids' education to compensate. This lack of compensating actions by parents reinforces the importance of institutions that ensure an appropriate quality of teachers.

The effect of educational quality is likely to increase even more in the future. Hanushek and Woessman (2012) find that the effect of cognitive skills on growth from 1980-2000 was almost double its effect from 1960-1980. This is in line with research emphasizing the increased demand for skilled workers due to complementarity with modern technology (Acemoglu 2002; Goldin and Katz 2008). Furthermore, the evidence on dynamic complementarities between educational investments across different stages of the life cycle, suggests that early investments (in early childhood) would likely raise the returns to educational investments later in life (Johnson and Jackson 2017). These findings make focusing on education mandatory for policymakers. The Economist (2017), for instance, identified educational outcomes and institutions as a potential bottleneck for Latin America in achieving convergence in development.

So, if the quality of education matters more than the quantity, and if the quality of education hinges primarily on the quality of teachers, how does one design institutions that create better teachers? Critical

¹⁸ Chetty et al. (2011) also study the effect of class sizes and confirm earlier research by Angrist and Lavy (1999) that smaller class sizes are better. On one hand, class sizes are less of an institutional feature in the sense that they are usually primarily driven by budgetary concerns, meaning spending per student. On the other hand, while class sizes are driven by budgetary constraints, they partially embody institutional features, meaning policies do exist that limit class size.

components appear to be monitoring of teachers' effort and quality, and performance-based hiring and retention decisions, meaning measures that most private sector human resource departments would view as basic best practice. Nonetheless, these basic best practices are regularly neglected in public services, where a relative lack of performance evaluation and performance-based pay or retention is the norm. While the negative effects of a lack of performance evaluation of a country's street sweepers may be limited, the negative effects of a lack of performance evaluation of a country's teachers may be severe, because of the huge externalities (spillovers) from education to economic development.

In developing countries, teacher monitoring can be so limited that the challenge is simply to get teachers to show up to work. Research by Duflo, Hanna, and Ryan (2012) suggests this can be remedied by very simple performance-pay schemes. They show that making teacher salaries contingent on (monitored) attendance had dramatic effects on teachers' attendance in India. Moreover, this simple policy was revenue neutral, meaning it did not raise the aggregate wage bill paid to the teachers.

In developed countries with better monitoring, the issue of attendance is less important, but the lack of performance evaluation on the job is a pervasive problem there as well. This is because of the traditionally strong unionization of teachers and because unions systematically assign greater importance to seniority than to performance. Recent events in Mexico highlight an underappreciated political economy side to the importance of teacher unions as educational institutions. The Mexican teachers' union, Sindicato Nacional de Trabajadores de la Educación (SNTE), is the largest labor union in Latin America. Until recently, SNTE was responsible for the hiring of teachers, essentially taking over a basic function of the government. Under this structure, Mexico's education system failed to deliver and was one of the worst globally on a per-dollar-spent basis. These issues were addressed with the signing of a law in 2013 that introduced teacher's performance evaluations and established objective criteria for the recruitment, selection and career progression of teachers.¹⁹ While there is an argument that teacher unions could increase teacher quality by increasing job security, the empirical evidence does not support this conclusion. Lovenheim (2009) assesses this by analyzing changes in student

¹⁹ Since then, the quality of education and teachers is said to be on the rise, although this is difficult to verify: the OECD's PISA study would be the right place to check for such an improvement but unfortunately it only covered Mexico in 2012 and 2016 (see <http://www.oecd.org/pisa/data/>).

outcomes as teachers unionize in a district. In a sample of three midwestern U.S. states (Iowa, Indiana, and Minnesota), he finds no effects of teacher's unionization on high school dropout rates. Cowen and Strunk (2014) summarize the state of this literature and conclude that it fails to refute the view of unions as rent-seekers, with little to no benefit for students.

4.3.3. Health

Health is a prime correlate of economic development: people in richer countries live longer and healthier lives. Understandably, public policymakers have argued that poor health is a primary roadblock for economic development (Gallup and Sachs 2001; Sachs 2002; Weil 2007). However, this focus on health policy as a fast track to development may be misguided. A critical distinction is that between health improvements that increase life expectancy and health improvements that improve productivity.

Health improvements that merely raise life expectancy may not raise incomes. Acemoglu and Johnson (2007) show that countries that benefited most from the international epidemiological transition—when cures for many infectious diseases (including malaria) were developed—indeed saw pronounced increases in life expectancy but that this did not increase economic development; GDP per worker or per capita in fact declined in countries where life expectancy rose. At some level this is surprising because longer life expectancy raises the returns to undertaking investments, including in human capital. One may therefore ask if there is a difference between changes in the ex-ante expected length of life, and the ex-post (unexpected) changes in the length of life that Acemoglu and Johnson (2007) identify. Bleakley (2017) carefully examines the economic magnitude of the “horizon” channel of longer ex-ante expected length of life and finds this effect to be miniscule. For a typical developed country, the gain attained through this channel is less than 1 percent of an individual's lifetime income.

By contrast, health improvements that raise productivity typically will also raise incomes. The most important productivity in this sense is that of children in the classroom, meaning the primary channel is again education. Healthier children are more likely to attend school and are better able to concentrate in class and acquire knowledge and skills. Many observers have noted the low school enrollment in many least-developed countries and gauged its effect on development.²⁰ However, the most convincing study

²⁰ See Hillman and Jenker (2005). Ensuring complete enrollment in primary education was the second of the United Nations' Millennium Development Goals. That goal was attained unevenly across targeted countries (De Herdt and Titeca 2016).

thus far on the importance of school attendance relies on historical evidence from the southern United States. Bleakley (2007) evaluates the effect of the eradication of hookworm there, an initiative by the Rockefeller Sanitary Commission between 1909 and 1915. Before the intervention, about 40 percent of school-aged children in the southern United States were infected. Bleakley estimates that children infected were 20 percent less likely to enroll in schooling. The intervention proved to be a success: hookworm eradication had sizable long-run beneficial effects on literacy and returns to schooling.

A secondary channel through which productivity raises incomes also works through education. Bleakley and Lange (2009) find evidence that some of the effect of health improvements on development comes through parental investments in children's education. Faced with better health institutions and environments, parents anticipate a higher return to investments in children's education and invest more. This points to complementarity between education-improving and health-improving institutions and parental investments in their children.

The evidence thus shows relatively clearly that (1) higher life expectancy itself has little or no effect on economic development, (2) improvements in health at younger ages do have significant effects on economic development, and (3) this effect works primarily through better educational attainment and cognitive development, as well as through rationally higher parental investments in children's education.

Unfortunately, there are no internationally comparable measures of health institutions at present. In their absence, the next section examines measures of health expenditure.

4.4. The Evidence

This section investigates quantitatively the evidence discussed in Section 4.3. In doing so, the section considers a single outcome variable: GDP per capita in 2014 from the Penn World Tables 9.0 (PWT). This outcome variable is related to five institutional areas discussed in the previous section:²¹

Data on property rights, political, and contracting institutions:

1. Protection against expropriation, from Political Risk Services
2. Constraints on the executive, from the Polity IV Project

²¹ Not all institutional measures are for the same year, as some have not been updated for a while or are only freely available for earlier years. The slow-moving nature of these measures means this is not a major concern, however.

3. Legal formalism, from Djankov et al. (2003).²²

Data on education and health outcomes:²³

4. As a rough proxy for educational institutions, the Human Capital Index from the PWT is used.²⁴
5. As a rough proxy for health institutions, the child mortality rate (deaths of children under age 5 per 10,000 population), from the World Bank's World Development Indicators is used.

On the diagonal of Table 4.1 the correlation coefficient of each measure with itself is represented, which by definition is 1. As well, the diagonal reports on the number of countries for which each measure is available. Below the diagonal are displayed the correlations between the five different measures as well as their shared number of observations. Correlations are stronger the closer the correlation coefficients are to 1 or -1. Table 4.1 therefore documents that these five different institutional measures are highly correlated with each other, which makes it very difficult to untangle their effects in a multivariate regression due to the problem of multicollinearity.

As well, institutions that are thought to be good for development (e.g., protection against expropriation, constraints on the executive, and institutions that bolster educational quality, proxied by the Human Capital Index) are positively correlated with each other and negatively correlated with factors that are thought to be bad for development (e.g., legal formalism, and child mortality as a proxy for the absence of institutions that bolster health and nutrition).

Table 4.2 relates these measures to economic development by running univariate regressions of the log of per capita GDP on each of the five institutional measures one at a time (across columns 1-5). Observed patterns are consistent with the evidence discussed in Section 4.3: protection against expropriation and constraints on the executive are significantly positively correlated with economic development, and human capital is also strongly

²² Legal formalism is measured by an index of procedural complexity and the number of required legal procedures for collecting a bounced check. We focus on the latter, as it turns out to be measured for the largest number of countries.

²³ In the absence of direct international institutional measures on education and health, we rely on outcomes which arguably reflect institutional development.

²⁴ The PWT Human Capital Index correlates very closely with Hanushek and Woessman's (2012) Cognitive Ability Index, but the PWT is available for a much bigger set of countries. Hanushek and Woessman's measure is based on the Programme for International Assessment study, which covers only relatively wealthy countries.

Table 4.1 Correlation Across Institutional Measures

	Protection Expropriation	Constraints on Executive	Legal Formalism	Human Capital	Child Mortality
Protection Expropriation (Source: Political Risk Services)	1 120				
Constraints on Executive (Source: Polity IV)	0.3889 112	1 158			
Legal Formalism (Source: Djankov et al. 2003)	-0.4851 101	-0.3003 121	1 128		
Human Capital Index (Source: Penn World Tables)	0.758 110	0.4835 132	-0.3754 115	1 143	
Child Mortality (Source: World Bank, World Development Indicators)	-0.6372 118	-0.3065 157	0.383 124	-0.8102 140	1 184

Source: Author's calculations.

Notes: Larger numbers on the diagonal are the number of countries for which each measure is available. The larger numbers below the diagonal are the shared number of observations.

positively correlated with it. Legal formalism and child mortality are significantly negatively correlated with economic development. The statistical significance of each regressor is reflected in the t-statistics in brackets. A t-statistic above 1.96 in absolute value indicates significance, and a relationship is tighter the bigger the t-statistic. Another important consideration is the R-squared, which measures what share of the variation in economic development is statistically explained by the regressor. Table 4.2 makes it obvious that the security of property rights, human capital, and health are considerably more powerful predictors of development than the other two measures (constraints on the executive and legal formalism).

Column 6 in Table 4.2 presents the results of a multivariate regression of economic development on all five institutional measures. Column 6 shows the difficulty of unpacking the effects of different regressors on a single outcome when these outcomes are strongly correlated. Some of the partial correlations no longer make sense. Constraints on the executive are now conditionally negatively correlated with GDP and legal formalism is positively correlated. This is a common issue that arises because multivariate regressions condition on all included controls.

Table 4.2 Univariate and Multivariate Regressions of GDP on Institutions

Outcome	(1)	(2)	(3)	(4)	(5)	(6)
	Log (GDP per capita)					
Protection Expropriation (Source: Political Risk Services)	0.504*** (11.214)					0.280*** (5.560)
Constraints on Executive (Source: Polity IV)		0.142*** (2.774)				-0.065* (-1.864)
Legal Formalism (Source: Djankov et al. 2003)			-0.029*** (-3.428)			0.018*** (3.501)
Human Capital Index (Source: Penn World Tables)				1.420*** (15.568)		0.559*** (3.578)
Child Mortality (Source: World Bank, World Development Indicators)					-0.027*** (-16.892)	-0.014*** (-5.572)
Observations	116	149	125	143	167	93
R-squared	0.524	0.050	0.087	0.632	0.634	0.847

Source: Author's calculations.

Notes: * Significant at 10%; ** significant at 5%; *** significant at 1%.

A simple but powerful approach to solving this problem is to parse the underlying true variation that is being captured by a number of correlated measures. This approach is called principal component analysis, which is a technique that statistically decomposes correlated variables into their “truly distinct” characteristics. The downside is abstraction: these characteristics are statistical constructs and can only be interpreted via their relation to the underlying variables (their “factor loadings”). The upside is clarity: the principal components are uncorrelated with each other by construction, so they cannot confound each other. In other words, whatever we think it is that a principal component captures, it cannot be explained by any of the other principal components. There are by definition as many principal components as variables (e.g., five), but they can be ranked by how much of the overall variation in the data they explain. Column 2 of Table 4.3 shows that the first principal component explains over 60 percent of the total variation in the five institutional measures, and the next two principal components explain a further 29 percent. In combination, the three principal components explain over 90 percent of the variation in the institutional data. Columns 3–7 show how each principal component correlates with each of the five institutional measures. A clean picture emerges if some principal components correlate strongly with some underlying variables and other principal components with other variables. This is not the case here: the first principal component correlates strongly

Table 4.3 Principal Components of Institutional Measures

	(1)	(2)	(3)	(4)	(5)	(6)	(7)
	Factor Loadings (Eigen Vectors)						
	Eigenvalue	Eigenvalue: Proportion	Protection Expropriation	Constraints on Executive	Legal Formalism	Human Capital Index	Child Mortality
Principal component 1	3.09	0.62	0.51	0.36	-0.35	0.52	-0.47
Principal component 2	0.76	0.15	0.05	-0.43	0.71	0.28	-0.48
Principal component 3	0.70	0.14	-0.05	0.81	0.58	-0.01	0.13

Source: Author's calculations.

with all five variables and in a way that it captures all the good institutional features. It is positively associated with all variables thought to be good for development and negatively with all the variables thought to be bad. The second principal component is quite different in nature: it correlates positively with legal formalism and negatively with constraints on the executive. The second principal component thus characterizes that which is more authoritarian but at the same time more legally codified.

Table 4.4 investigates how these principal components relate to economic development. Columns 1–3 again display univariate regressions. The first principal component strongly and positively predicts economic

Table 4.4 Univariate and Multivariate Regression of GDP on Principal Components of Institutional Measures

Outcome:	(1)	(2)	(3)	(4)	(5)
	Log (GDP per capita)				
Principal component 1	0.553*** (13.786)			0.553*** (19.392)	0.621*** (23.675)
Principal component 2		0.545*** (4.195)		0.545*** (9.493)	0.360*** (6.378)
Principal component 3			-0.058 (-0.390)	-0.058 (-0.964)	0.067 (1.238)
Oil rents as percent of GDP (World Bank, World Development Indicators)					0.035*** (6.247)
Observations	93	93	93	93	93
R-squared	0.676	0.162	0.002	0.840	0.889

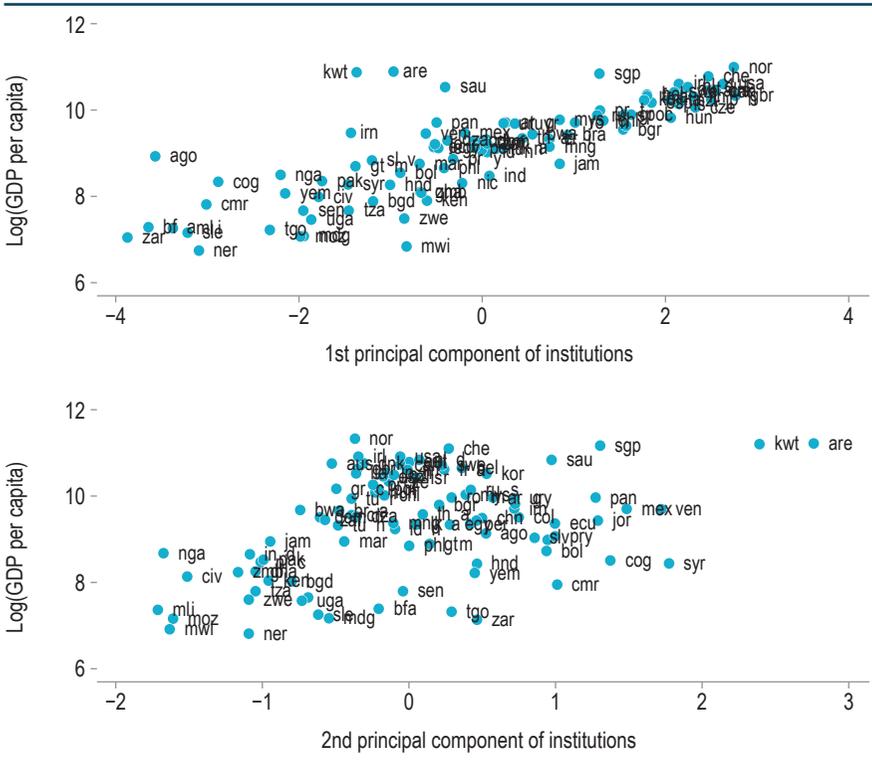
Source: Author's calculations.

Notes: * Significant at 10%; ** significant at 5%; *** significant at 1%.

development. This is unsurprising given its factor loadings reported in columns 3–7 of Table 4.3. More surprising is the second principal component. Despite correlating positively with legal formalism and negatively with constraints on the executive, it correlates strongly with economic development. Column 4 of Table 4.4 shows the great advantage of principal component analysis. Because principal components are by construction uncorrelated to each other, including them together in column 4 does not substantially alter the patterns one sees in the univariate regressions of columns 1–3. This is in stark contrast to the messy patterns in column 6 of Table 4.2.

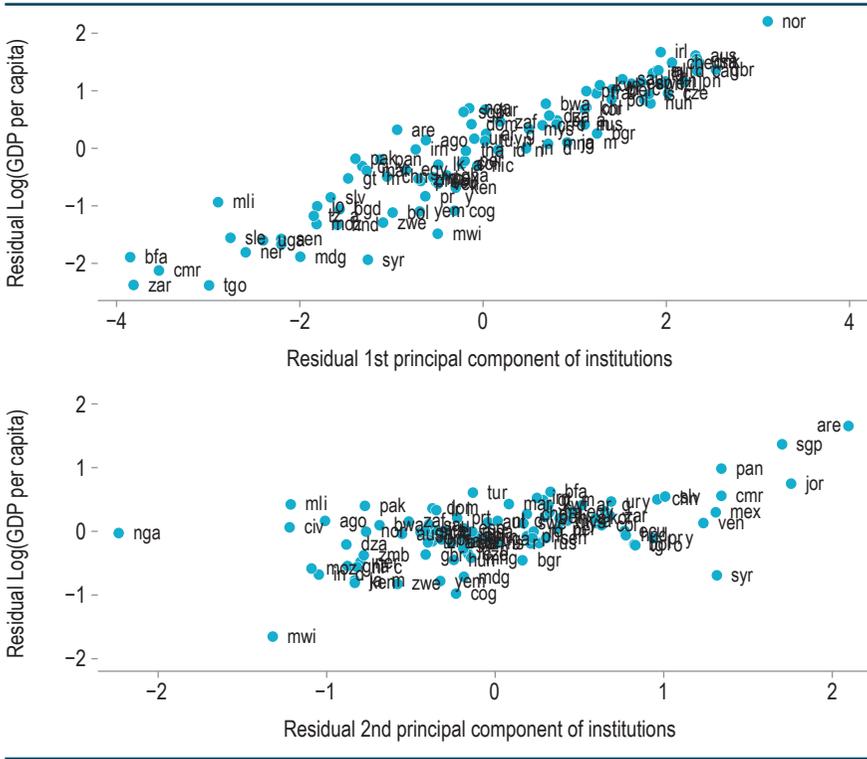
The top-two panels of Figure 4.1 visually display the relations between economic development and the principal components reported in columns 1–2 of Table 4.4. Some of the countries in the top-right of the scatterplot reflected in the second panel are Saudi Arabia (*sau*) and Kuwait (*kwt*). There is therefore an obvious concern that the principal component may positively correlate with development only because it proxies for the authoritarian but rich oil

Figure 4.1 Residual Regression Plots of GDP and Principal Components of Institutional Measures



(continued on next page)

Figure 4.1 Residual Regression Plots of GDP and Principal Components of Institutional Measures (continued)



Source: Author's calculations.

producers of the Middle East. However, this is not the case. In column 5 of Table 4.4 we control for a country's share of GDP that is generated by oil revenues. As can be seen, this weakens the relation between the second principal component and GDP (while strengthening the relation with the first principal component) but does not overturn it. This fact is visually represented by the bottom-two panels of Figure 4.1. Controlling for oil removes Saudi Arabia and Kuwait from the top right of the scatterplot in the bottom panel, but there remains a strong positive relationship. At the very top sits Singapore (*sgp*) and the Arab Emirates (*are*). These are countries that are relatively authoritarian but have strong legal codification. Importantly, these countries also have strong protections against expropriation.

4.5. Conclusions

This chapter has highlighted the importance of institutions for economic development. The chapter first presented a more extensive survey of the

state of knowledge on the importance of institutions that are specifically associated with better protection of citizens' property, more constraints on the executive, better contracting, better human capital acquisition, and better health provision.

The chapter then weighted this evidence quantitatively. It is worth reiterating that the evidence presented here is based on conditional correlations between different institutions and economic development, and that correlation does not necessarily imply causation. Nonetheless, for the purposes of a survey chapter like this one, where causation has already been established elsewhere in the literature, the relative strength of such partial correlations still tells us something useful about the relative importance of these institutions. The data suggest that all five institutions are indeed important for economic development. Three of the institutions investigated appear to be quite unequivocally good for economic development.

One of them, protection of citizens' property rights specifically against expropriation by the state, is a powerful predictor of levels of GDP in cross-country regressions. This specific notion of protection of property rights against the state is distinct from property rights that govern the relations between citizens or between corporations and citizens (e.g., copyright or trademark rights). It encompasses the idea associated most with De Soto (2000) that the inability of the "global poor" to formalize their informally recognized property rights (e.g., houses in shanty towns or favelas) is a big drag on economic development.

Another institution, education, as proxied by the Penn World Tables Human Capital Development Index, is a powerful predictor of levels of GDP in cross-country regressions. A recent report by Busso et al. (2017) sheds much light on the more fine-grained institutions that potentially underpin human capital development. The findings in Busso et al., combined with evidence presented in this chapter, suggest that teachers and parents are both critical in improving a country's education. One insight is that teaching needs to be an attractive career in order to attract good people. At the same time, a career in teaching needs to evolve based on merit, which is sadly often not the case in the public sector. Teacher effort and performance need to be evaluated, and good teachers should see their effort and performance acknowledged and rewarded in some way. Table 7.1 in Busso et al. (2017) provides a comprehensive list of interventions that have been shown to be effective in improving educational attainments. Countries with high educational achievements undertake many or most of these interventions. Invariably, the path to success is one that ensures that students, teachers, and parents all buy into the importance of education.

Institutions that ensure good health, as proxied in this chapter by low child mortality, are a third powerful predictor of levels of GDP in cross-country regressions. A key observation is that health improvements that prolong life are less associated with economic development than health improvements that improve productivity. Strikingly, the most important forms of health improvements are those that improve productivity in the classroom as opposed to, for example, in the workplace later in life. This means that, while health at old age is certainly desirable, it is health at young ages that is most critical for economic development. Berlinski and Schady (2015) shed much light on the more detailed web of institutions that need to be coordinated in order to achieve better health outcomes for economic development. Invariably, the devil of implementation is in the details, and the details can be very country-specific. However, the aforementioned guiding principle holds: better health as a necessary ingredient for better economic development is invariably a story of the better health of children of school-age or younger.

Finally, the relationship between the other two institutions investigated is less unequivocal but becomes clear once we parse out the part that is just a correlate of better property rights, better education, and better health (i.e., in Tables 4.3 and 4.4 and Figure 4.1). Both stronger constraints on the executive and less legal formalism have upsides for economic development, but also downsides. A possible, and even likely, explanation is that a stronger executive can—so long as property rights, human capital acquisition, and health provision are secure—facilitate policymaking and break political deadlock. Similarly, more legal formalism, while it can be economically inefficient, can also clarify the rules of the game and thus create more transparent and inclusive institutions.

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The Role of Economic Institutions in Supporting Growth and Development

Klaus Schmidt-Hebbel

Good institutions are central to sustaining high growth in a narrow sense and to achieving development in a broad sense, including the attainment of economic, social, and political objectives. However, identifying which institutions are relatively more important drivers of growth and development is fraught with analytical and empirical questions. First, what are institutions, and how are they different from other human manifestations that determine civilizations and cultures? Second, considering that growth and development influence each other, is it possible to distinguish between those institutions that cause growth and overall development from those that are a consequence? Third, among a broad set of institutional candidates, which are the key institutions that affect growth and development?

The general review of the theory and evidence regarding the role of institutions for growth and development provided in Chapter 3 has shown that, to a large extent, these broad questions are still not well addressed in the analytical and empirical literature in economics, political economy, political science, and history. However, some key sets of institutions have been shown to be important determinants of prosperity. This chapter, therefore, focuses on one of these narrower sets of institutions, namely economic institutions. As such, the chapter's objective is to survey the analytical literature and empirical evidence available to date on the direct and indirect effects of key economic institutions and reforms on growth and development. The chapter focuses on national institutions related to three key economic management areas: international integration, macroeconomic policies, and the financial sector.

The chapter first introduces 11 economic institutions within those areas and presents their evolution over time and across major world regions. Then we introduce several hypotheses about the mechanisms through which institutions could contribute to growth and development. The subsequent section develops the chapter's core analysis: an extensive review

of the empirical evidence on the direct and indirect contribution of these economic institutions to economic development, controlling for other factors. The most important conclusion is that the institutions covered make a statistically significant and positive contribution to gross domestic product (GDP) growth rates, per capita GDP levels, factor accumulation and productivity, and macroeconomic and financial stability.

On the related question of reverse causality—from growth and development to institutions—the chapter briefly summarizes theories of institutional change and the available empirical evidence on different determinants (including growth and development) of the adoption of key economic institutions. The chapter then discusses several issues related to implementation of institutional changes. The concluding section presents a summary of the chapter’s key findings.

5.1. Key Economic Institutions and Their Distribution Over Time and Across Regions

In his classic article, Douglass North’s definition of institutions brilliantly reflects the key aspects of institutions that will be documented here: they are informal or formal constraints that reduce uncertainty; they strengthen incentives to produce and exchange more efficiently; they evolve gradually over time; and they shape an economy toward growth, stagnation or decline (North 1991). However, to measure the contributions of institutions to growth, one must focus on a more specific set of institutions.

This chapter, therefore, focuses selectively on 11 formal economic institutions in three key areas of economic policy management: international integration, macroeconomic policies (fiscal policy, exchange rate regimes, and monetary policy frameworks), and financial sector policies. The institutions are: trade openness, financial openness, tax rates, medium-term fiscal frameworks, fiscal rules, fiscal councils, sovereign wealth funds, exchange rate regimes, central bank independence, monetary policy regimes, and financial sector policies. The institutions analyzed here define current best national practices in these three areas of economic policy management in both advanced and developing economies. Certainly, there are other economic institutions (related to product markets, labor markets, competition, innovation, and business conditions, among others) that are potentially very important in contributing to growth and development, but they are not assessed in this chapter.

The next subsections introduce the institutions in the referred three key areas and presents their distribution over time and across 98 countries classified into four major country groups: member countries of the

Organisation for Economic Co-operation and Development (OECD), Latin America (LA), the Caribbean member countries of the Inter-American Development Bank (CCB), and the rest of the small economies of the world (ROSE).¹ The analysis to be presented is descriptive in nature comprising cross-sectional comparisons across the outlined country groups. As such, the objective is to describe the evolution of the adoption of these institutions rather than suggesting any causal interpretation. The subsequent summary statistics for each institution comprise unweighted country averages or country counts for each country group.

5.1.1. *International Integration*

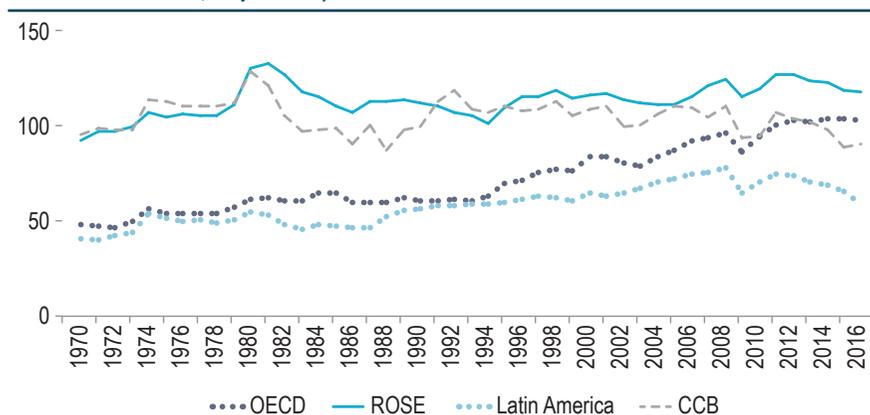
Economic openness is a key component of a comprehensive growth strategy. Two measures of a country's integration in the world economy are considered here: trade openness and financial openness. Trade openness is measured ex post, as the ratio of exports and imports to GDP (Figure 5.1). Trade integration shows a positive trend since 1970 in three of the four country groups. The exception is the Caribbean, where the share of trade to GDP was high in the 1970s but subsequently showed a weak declining trend. However, commodity prices affect the trade measure in all three country groups other than the OECD, including the Caribbean.

Financial openness is measured by the ex-ante Chinn-Ito Index of capital account restrictions on international capital account mobility (Figure 5.2).² Here all four regions show a significant trend toward capital

¹ The OECD includes 35 countries: Australia, Austria, Belgium, Canada, Chile, Czech Republic, Denmark, Estonia, Finland, France, Germany, Greece, Hungary, Iceland, Ireland, Israel, Italy, Japan, Latvia, Korea, Luxembourg, Mexico, the Netherlands, New Zealand, Norway, Poland, Portugal, Slovak Republic, Slovenia, Spain, Sweden, Switzerland, Turkey, the United Kingdom, and the United States. The Caribbean (CCB) includes six countries: The Bahamas, Barbados, Guyana, Jamaica, Suriname, and Trinidad and Tobago. Latin America includes 19 countries: Argentina, Belize, Bolivia, Brazil, Chile, Colombia, Costa Rica, Dominican Republic, Ecuador, El Salvador, Guatemala, Honduras, Mexico, Nicaragua, Panama, Paraguay, Peru, Uruguay, and Venezuela. The ROSE group includes 38 countries with populations of less than 3 million: Bahrain, Belize, Bhutan, Botswana, Brunei Darussalam, Cabo Verde, Comoros, Cyprus, Democratic Republic of Timor-Leste, Djibouti, Equatorial Guinea, Estonia, Fiji, FYR Macedonia, Gabon, Guinea-Bissau, Iceland, Kiribati, Latvia, Lesotho, Luxembourg, Maldives, Malta, Mauritius, Mongolia, Montenegro, Namibia, Qatar, Samoa, São Tomé and Príncipe, Seychelles, Slovenia, Solomon Islands, Swaziland, The Gambia, Tonga, Tuvalu, and Vanuatu.

² The Chinn-Ito Index (KAOPEN) measures a country's degree of capital account openness. KAOPEN is based on the binary dummy variables that codify the tabulation of restrictions on cross-border financial transactions reported in the International

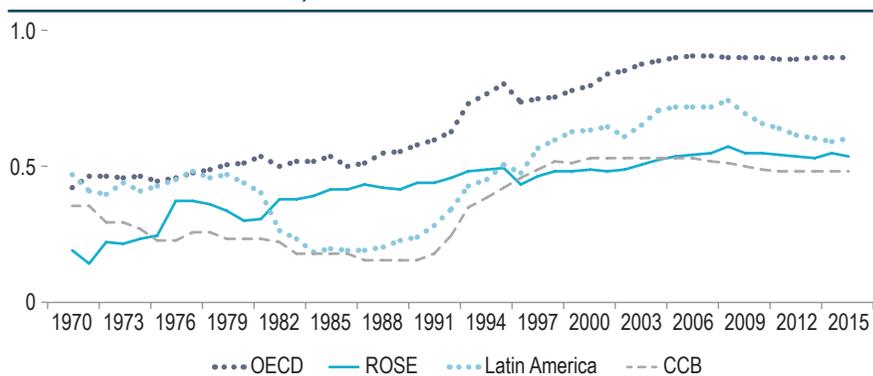
Figure 5.1 Trade Openness, 1970–2016 (sum of exports and imports as a share of GDP, in percent)



Source: World Bank.

Note: See footnote 1 for the countries included in each regional grouping.

Figure 5.2 Capital Account Openness, 1970–2015 (Chinn-Ito Index normalized between 0 and 1)



Source: Chinn and Ito (2017).

Note: See footnote 1 for the countries included in each regional grouping.

account liberalization. In Latin America and the Caribbean, capital account restrictions, which had been intensified in the 1980s, were reversed and further liberalized after the 1990s. However, at the end of the sample

Monetary Fund's *Annual Report on Exchange Arrangements and Exchange Restrictions* (AREAER). The authors use principal component analysis to extract the first principal component, which is the KAOPEN. The index is then normalized to range between zero (least open) and one (most open). More details are reported in Chinn and Ito (2006, 2017).

period (2015), international financial integration was still significantly less complete in ROSE, Latin America, and the Caribbean than in the OECD.

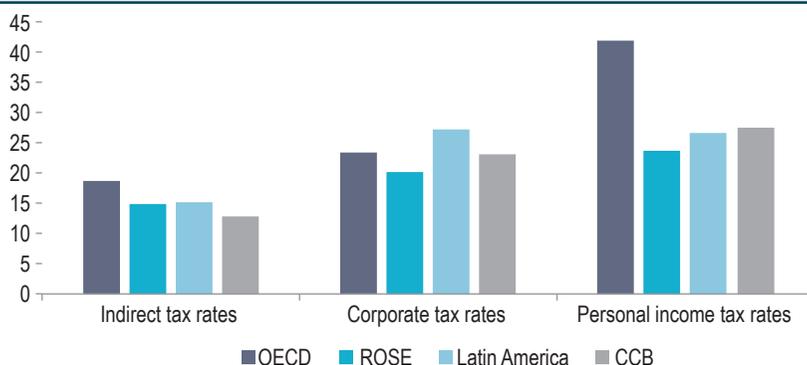
5.1.2. Fiscal Policy

A developed fiscal framework is based on several fiscal institutions that contribute to fiscal sustainability, solvency, transparency, intergenerational equity, and policy countercyclicality, and hence to growth and development. This section considers five key institutions of a fiscal framework: tax rates, medium-term fiscal frameworks, fiscal rules, fiscal councils, and sovereign wealth funds.

In the absence of comprehensive measures of tax systems that are internationally comparable, the analysis uses partial but readily available cross-country measures of taxes, namely legal tax rates on transactions (indirect taxes) and income (corporate and personal income taxes). There are complex trade-offs involved in the effects of taxes on growth and development. On one hand, the distortional negative growth effects of taxes rise more than proportionally with tax rates. On the other hand, higher taxes allow for financing higher levels of public goods that are necessary for growth (i.e., public infrastructure and education) and social integration and equity (public transfer programs).

Both indirect and direct tax rates are higher in the OECD than in other countries, reflecting the larger size of governments in high-income economies (Figure 5.3). Average indirect tax rates are close to 20 percent in the

Figure 5.3 Tax Rates on Transactions and Income, 2018 (percent)



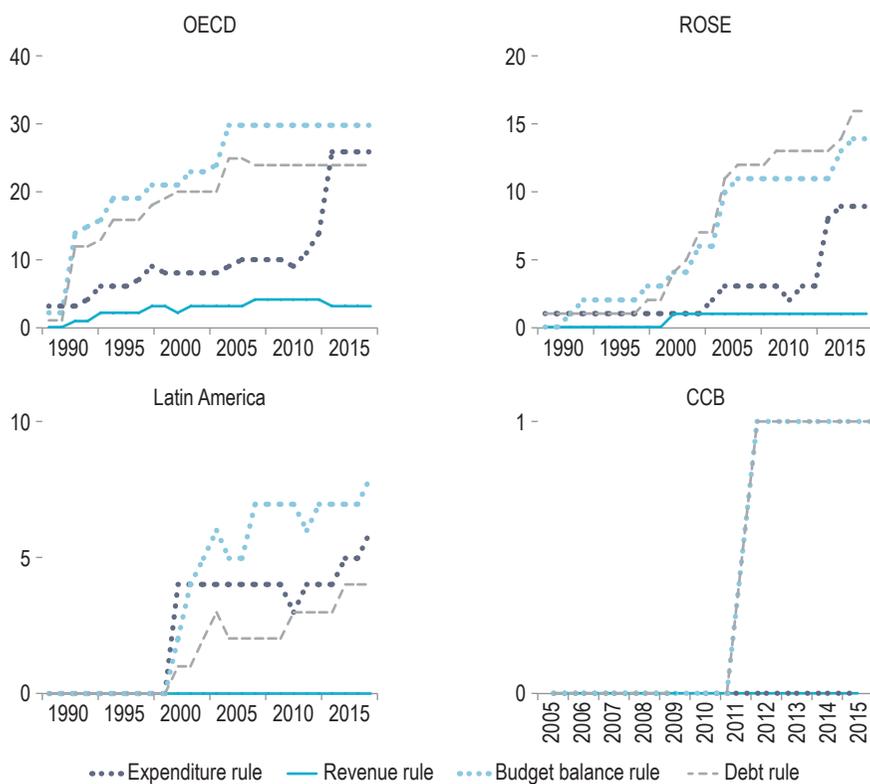
Source: Prepared by the author based on KPMG, Deloitte, and PWC data.

Notes: Indirect, corporate, and personal income tax rates are computed as simple averages of legal tax rates. Indirect taxes include the value-added tax, goods and services tax, and other taxes. The personal income tax is defined as the top marginal legal tax rate. See footnote 1 for the countries included in each regional grouping.

OECD and around 15 percent in Latin America, ROSE, and the Caribbean. Average legal corporate tax rates, close to 25 percent, are largely similar in the four country groups. However, the top marginal legal tax rate on personal income tax rates is much higher in the OECD (42 percent) than in the three other country groups (average just under 25 percent).

Since the mid-1990s, medium-term fiscal frameworks or multiyear budgeting processes have been increasingly adopted by a significant share of countries worldwide. For instance, Vlaicu et al. (2014) document that by 2008 around 70 percent of a sample of 181 countries worldwide had implemented medium-term fiscal frameworks. This is a sharp incursion rate considering that by 1995 only about 10 percent of countries had such institution in place. However, only one of the six Caribbean countries analyzed here has adopted fiscal responsibility legislation along these lines.

Figure 5.4 Number of Countries with Fiscal Rules, by Region and Type of Rules



Source: International Monetary Fund, Fiscal Rules Dataset 1985–2015.

Note: The vertical axis represents the number of countries with the corresponding fiscal rule in place. Jamaica is the only Caribbean country that adopted two fiscal rules in 2011.

Similarly, since 1990, fiscal rules have been adopted by an increasing number of advanced economies and emerging market and developing economies, including Latin America and ROSE (Figure 5.4). However, only one of the six Caribbean countries analyzed here has adopted fiscal rules. Among the types of rules, budget balance, debt, and expenditure rules are more frequently in place than revenue rules. Several countries have more than one rule in place.

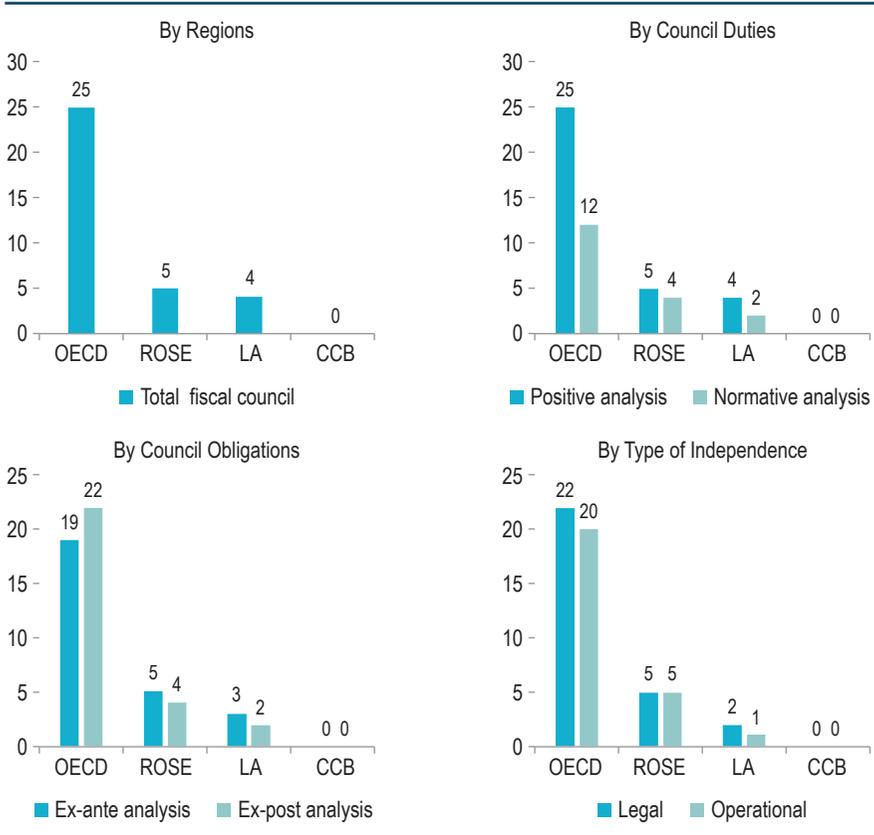
A fiscal council is a more recent institutional innovation, and such councils have been increasingly adopted since the 2008–2009 global financial crisis, mostly by OECD countries (Figure 5.5). Only five ROSE and four Latin American countries have fiscal councils in place, and no such councils have been adopted in Caribbean countries. Fiscal councils are government agencies with legal and/or operational independence that have a mandate determined by law to monitor budget preparation and execution (including compliance with fiscal rules), conduct positive and normative fiscal analysis, and provide policy recommendations. Most councils conduct positive analysis of fiscal policy (half of them add policy recommendations to their duties) and most conduct both ex-ante and ex-post analysis.

Sovereign wealth funds are important institutions in natural-resource-exporting countries that face volatile commodity prices and/or a finite endowment of resources. They are more frequently put in place by OECD and resource-rich emerging-market and developing economies (Figure 5.6). Trinidad and Tobago is the only Caribbean country with a sovereign wealth fund. A number of countries with such funds have more than one fund in place, either because they are linked to different policy objectives or they are implemented by individual states within a federated country. The Linaburg-Maduell Sovereign Wealth Fund Transparency Index shows large differences in the governance and financial transparency of sovereign wealth funds across different countries and world regions. Sovereign wealth funds are generally more transparent in advanced than in emerging-market and developing economies. It is worth noting that Trinidad and Tobago's fund (CCB in Figure 5.6) is ranked relatively high in transparency (above ROSE and Latin America).

5.1.3. *Exchange Rate Regimes*

The choice of an exchange rate regime is a key component of a country's macroeconomic framework. A floating exchange rate regime is a prerequisite for the conduct of independent monetary policy and offers protection against foreign shocks and currency crises, but at the cost of higher short-term exchange rate volatility. A hard peg or outright adoption of a foreign

Figure 5.5 Number of Countries with Fiscal Councils, by Region and Type of Councils, 2017



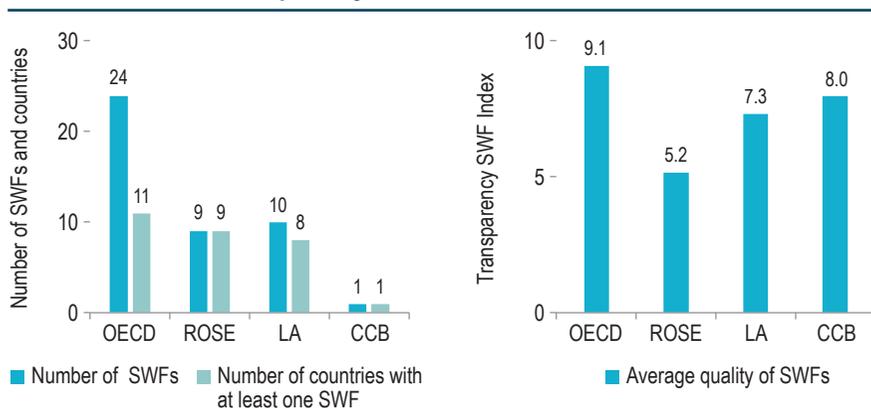
Source: International Monetary Fund, Fiscal Council Dataset, 2017.

Notes: The vertical axis represents the number of countries with the corresponding fiscal council. **Definitions:** Positive analysis: The council performs positive analyses (Yes: 1, No: 0); Normative analysis: The council performs normative analysis or provides recommendations (Yes: 1, No: 0); Ex-ante analysis (monitoring of fiscal rules): The council is mandated to monitor compliance with numerical fiscal rules (Yes: 1, No: 0); Ex-post analysis (Yes: 1, No: 0); Legal independence: The council's independence from political interference is guaranteed by law or treaty (Yes: 1, No: 0); Operational independence: Even if a council is not legally independent, it might operate (and be generally perceived) as an independent body because its analysis reflects its expertise. See footnote 1 for the countries included in each regional grouping.

currency is optimal for economies that are highly integrated with large economies, which is often the case in smaller countries. The world distribution of exchange rate regimes is biased toward soft pegs and floating regimes (Figure 5.7).³ Floating exchange rates dominate in OECD countries and in medium-sized and large economies, including several countries

³ Soft peg is a regime where the local currency maintains a stable value against an anchor foreign currency or composite of currencies (IMF 2016).

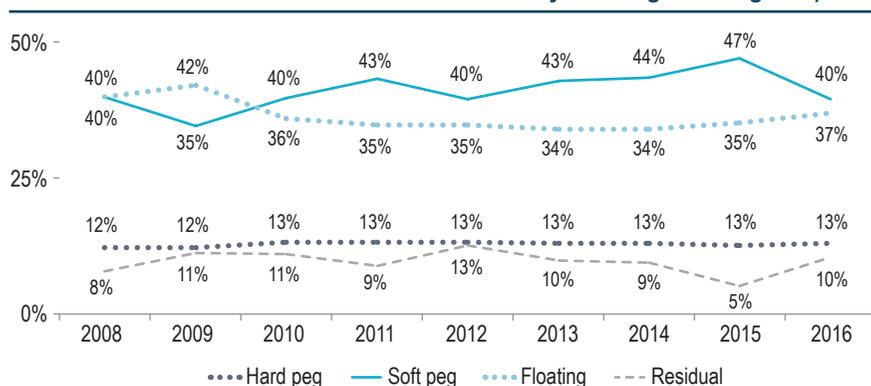
Figure 5.6 Number of Countries with Sovereign Wealth Funds, by Region and Level of Transparency, 2017



Source: Sovereign Wealth Fund Institute, February 2018.

Notes: Trinidad and Tobago is the only Caribbean country with a sovereign wealth fund (SWF). SWF transparency is measured by the Linaburg-Maduell SWF Transparency Index reported by the Sovereign Wealth Fund Institute. The index ranges from 1 (least transparent) to 10 (most transparent). See footnote 1 for the countries included in each regional grouping.

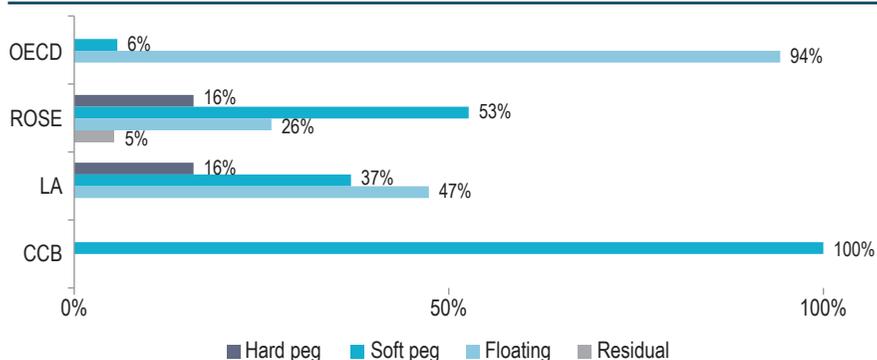
Figure 5.7 Exchange Rate Regimes in the World, 2008–2016 (percent distribution of IMF member countries by exchange rate regimes)



Source: International Monetary Fund (IMF), Annual Report on Exchange Arrangements and Exchange Restrictions database, 2016.

Note: The IMF classification of exchange rate arrangements is as follows: hard peg (no separate legal tender, currency board); soft peg (conventional peg, stabilized arrangement, crawling peg, crawl-like arrangement, pegged exchange rate within horizontal bands); floating (floating, free floating); and residual (other managed arrangements).

in Latin America (Figure 5.8). In contrast, soft and hard pegs are the norm in small economies. All six Caribbean countries analyzed here have a soft peg in place.

Figure 5.8 Distribution of Exchange Rate Regimes, by Region, 2016

Source: International Monetary Fund (IMF), Annual Report on Exchange Arrangements and Exchange Restrictions database, 2016.

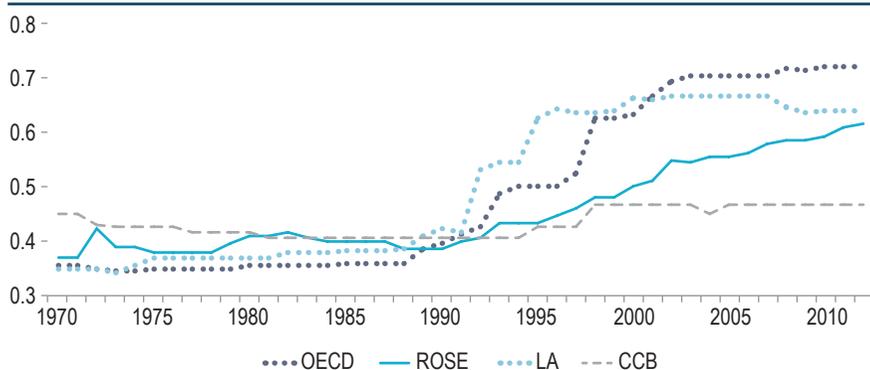
Notes: The IMF classification of exchange rate arrangements is as follows: hard peg (no separate legal tender, currency board); soft peg (conventional peg, stabilized arrangement, crawling peg, crawl-like arrangement, pegged exchange rate within horizontal bands); floating (floating, free floating); and residual (other managed arrangements). See footnote 1 for the countries included in each regional grouping.

5.1.4. Monetary Policy Frameworks

Two key institutions for effective monetary policy are central bank independence and the choice of monetary regime. Central bank independence is an important condition for conducting an independent monetary policy. The number of independent central banks has increased significantly since 1990 in most world regions (Figure 5.9). Garriga's (2016) measure of independence shows that OECD countries exhibit, on average, the highest levels of independence.⁴ Latin America and ROSE have somewhat lower levels of independence. Central bank independence is less important in small economies with a hard exchange rate peg. Hence it is not surprising that the six Caribbean countries exhibit lower levels of central bank independence.

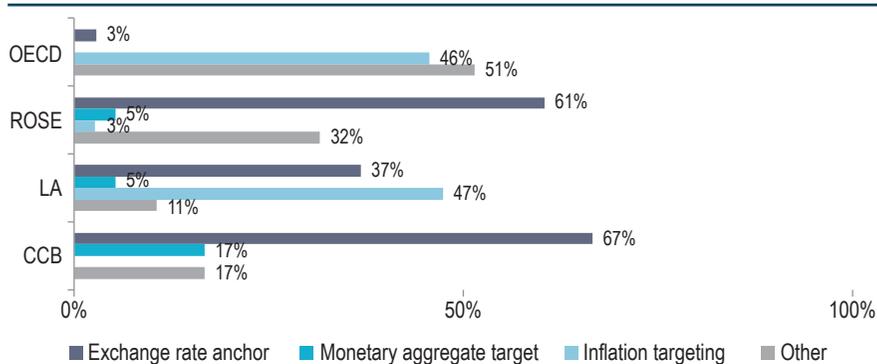
Since 1990, inflation targeting has been adopted as the monetary regime of choice in many medium-sized and large economies that aim to conduct independent monetary policy. About 50 percent of economies in the OECD and Latin America targeted inflation by 2016 (Figure 5.10). In contrast, in small economies the nominal anchor of choice is the exchange rate. Only 3 percent

⁴ Garriga (2016) identified four dimensions concerning the independence of central banks from political influence: who appoints the governor (weight = 0.2); whether there is direct government involvement in policy decisions (weight = 0.15); whether there are limits on the ability of the government to borrow from the central bank (weight = 0.50); and whether price stability is a core objective of monetary policy (weight = 0.15). The weighted average of these dimensions results in a Central Bank Independence Index ranging from 0 (lowest independence) to 1 (highest independence).

Figure 5.9 Regional Averages of Central Bank Independence, 1970–2012

Source: Garriga (2016).

Notes: Based on Garriga's (2016) Central Bank De Jure Independence Index, which ranges from 0 (least independent) to 1 (most independent). See footnote 1 for the countries included in each regional grouping.

Figure 5.10 Distribution of Exchange Rate Anchors, Monetary Aggregate Targets, Inflation-Targeting, and Other Monetary Regimes, by Region, 2016

Source: International Monetary Fund, Annual Report on Exchange Arrangements and Exchange Restrictions database, 2016.

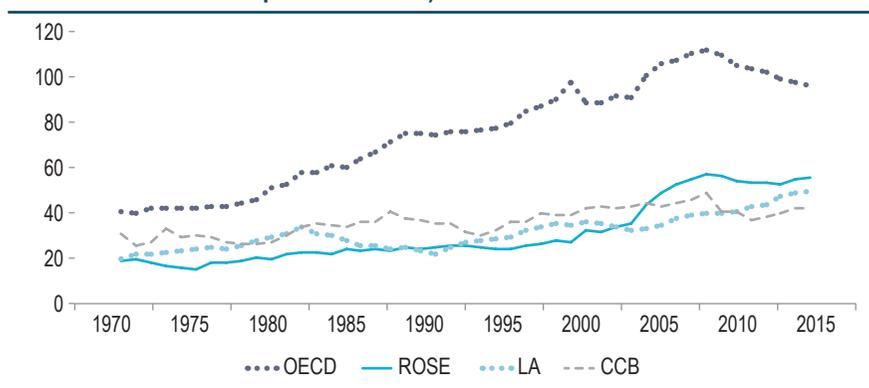
Note: See footnote 1 for the countries included in each regional grouping.

of countries among ROSE and no Caribbean country has inflation targeting in place; their dominant choice of nominal anchor is the exchange rate.

5.1.5. Financial Sector Policies

Liberalization of financial markets has been a key component of economic reforms in both advanced and emerging-market and developing economies since the 1970s. However, financial liberalization without adequate financial market regulation and supervision has led, time and again, to deep financial

Figure 5.11 Financial Development, 1970–2015 (domestic credit to the private sector as a percent of GDP)



Source: World Bank.

Note: See footnote 1 for the countries included in each regional grouping.

crises and recessions, ranging from the Latin American debt crisis of the early 1980s to the global financial crisis of 2008–2009. A huge empirical and analytical literature demonstrates that liberalization of financial intermediation and development of new financial instruments and markets is potentially beneficial for efficient allocation of capital and risk, as long as financial intermediation and risk-taking are well regulated and supervised.

In the absence of widely accepted ex-ante policy indicators of efficient financial sector regulation and supervision, this section uses a summary of ex-post measures of financial liberalization and depth: the domestic-credit-to-GDP ratio (Figure 5.11). This indicator reflects the result of financial liberalization but is also subject to credit booms and busts, often caused by failures in bank and capital market oversight. Since the 1970s, financial depth has shown an upward trend, often interrupted by episodes of credit deleveraging following financial crises, such as the Latin America crisis in the 1980s and the 2008–2009 global financial crisis. In the OECD, the average ratio of bank credit to the private sector was close to 100 percent of GDP in 2016, which is twice the ratio observed, on average, in Latin America, ROSE, and the Caribbean. This reflects that development and financial depth are associated.

5.2. Direct and Indirect Effects of Economic Institutions

5.2.1. *Effects of Institutions: Theory*

A large body of research points to the key role of well-designed political, social, and economic institutions in promoting growth and development.

Such institutions constrain the exercise of power at high and low political levels, the conduct of policymakers, and the behavior of individual agents (consumers, workers, firms) in any sector or market. Institutions restrict the exercise of discretionary power and support rule-based, efficient behavior.

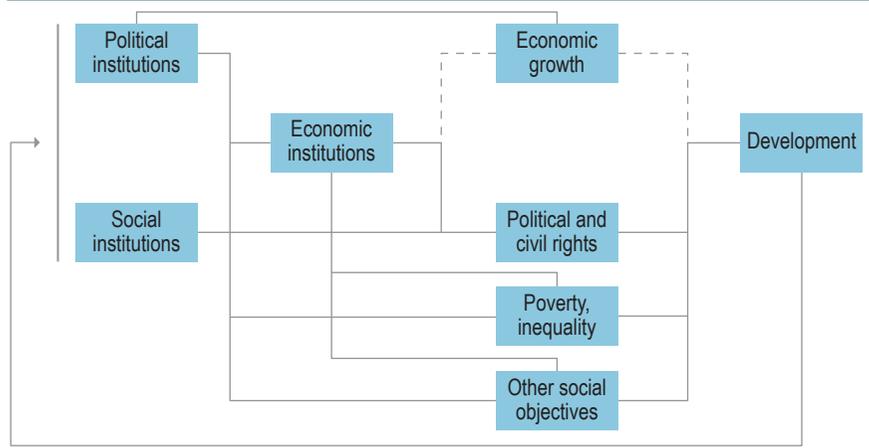
The transmission mechanisms from good institutions to growth and development are not easy to disentangle. Most of them are indirect, affecting intermediate variables before impacting ultimate objectives such as economic growth, per capita average income, or income distribution. For example, inflation targeting may contribute to better anchoring of inflation expectations, strengthening of monetary policy credibility, and macroeconomic stability, which may spur investment and ultimately growth. Trade opening is likely to lead to short-term closure of import-competing industries before exports respond to lower tariffs on inputs and a more depreciated exchange rate; hence productivity, investment, and GDP are likely to exhibit a U-shaped response to trade opening. A similar result is often observed in the case of financial deregulation and liberalization, especially when financial reforms are not carefully implemented, leading to a financial crisis, which prompts a second set of better financial reforms. Hence institutional reforms have very different effects on ultimate policy objectives—like growth—depending on the form they take and on the time horizon during which they are carried out.

A related complexity of reform effects stems from the interactions between institutional reforms in a particular front and other institutions in affecting growth and development. For the case of economic institutions, evidence suggests that their effects are conditional on politics and political institutions. For example, Keefer and Stasavage (2003) show that although, on average, central bank independence is related to reduced inflation; this relation is more palpable in more politically polarized societies. Acemoglu et al. (2011) report that central bank independence reforms tend to reduce inflation, but the stabilizing effect is asymmetric; that is, it is stronger (weaker) in countries with strong (weak) political institutions.

Tylecote (2016) discusses three important books on institutions and development—North, Wallis, and Weingast (2009), van Zanden (2009), and Acemoglu and Robinson (2012)—and concludes that the volumes are built on three key hypotheses: institutions matter for growth and development, politics and economics are interconnected, and sustainable economic growth requires strong participation and openness of institutions.

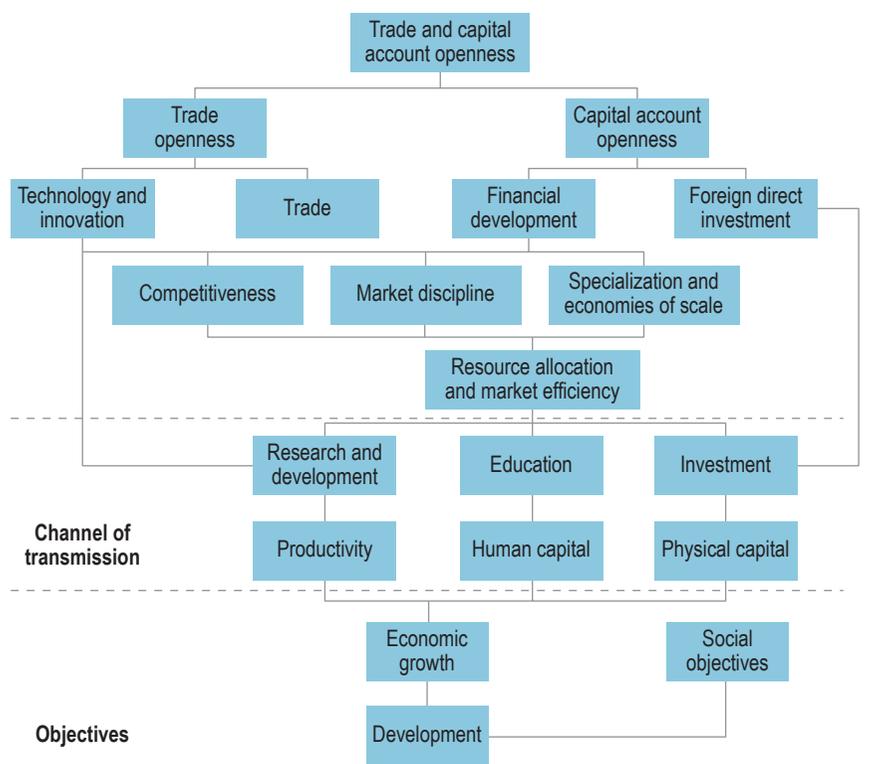
Figure 5.12, which is based on the theory and empirical evidence on institutions, growth and development, presents the links between political, social, and economic institutions on one hand, and growth and other indicators of overall development on the other. At this very general level, this

Figure 5.12 The Role of Institutions in Supporting Growth and Development



Source: Prepared by the author.

Figure 5.13 The Role of International Integration



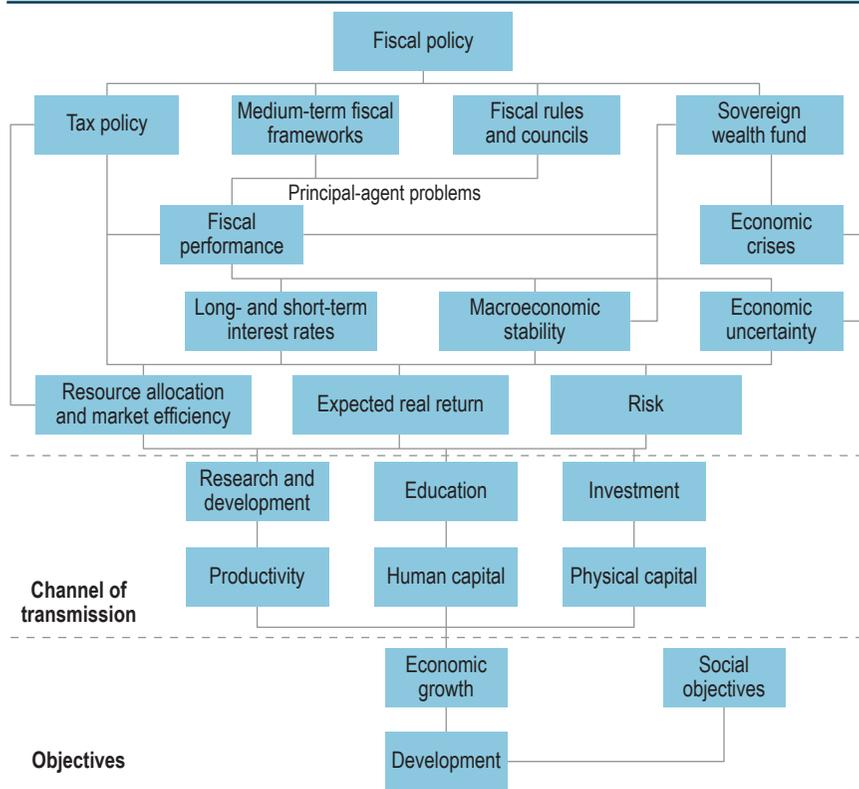
Source: Prepared by the author.

figure makes three points. First, it reflects the above-mentioned close connection between economics and politics. Second, economic institutions are in part a result of deeper political and social institutions. Finally, there are feedback effects from growth and development to institutional design and implementation: more advanced economies are more likely to develop and implement frontier institutions.

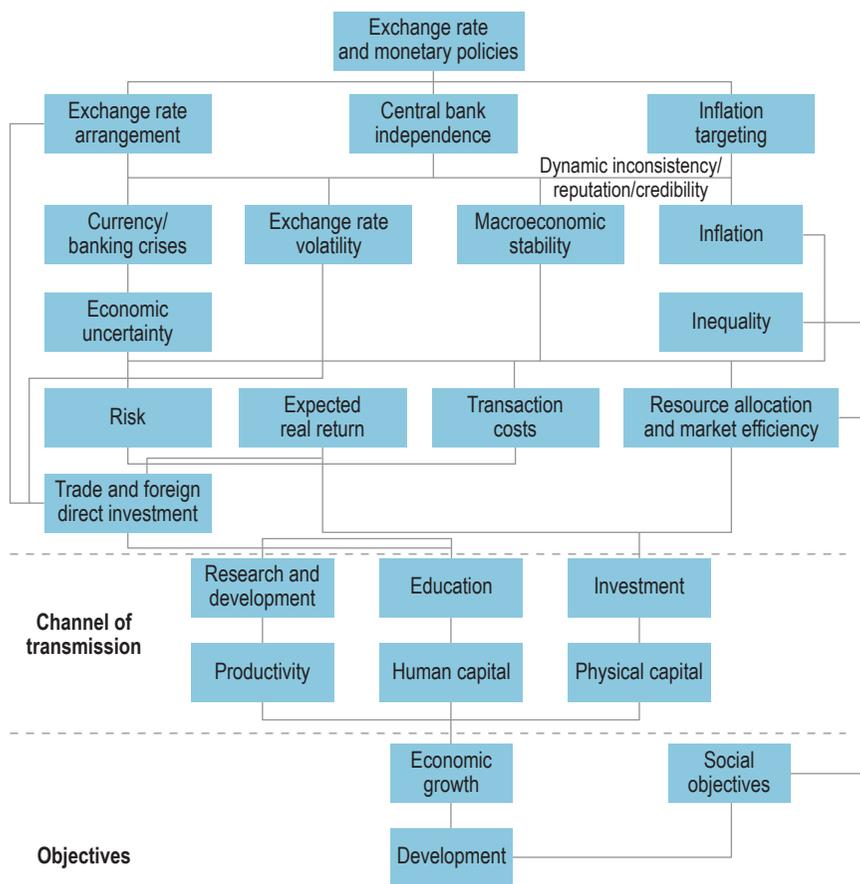
Figure 5.13 depicts the links from international integration to growth and development. Trade and financial openness boost trade and financial exchange, leading to financial and technological innovation, more market discipline and specialization, and better resource allocation and efficiency. This leads to more research and development, better education, and more investment, reflected in higher rates of human and capital accumulation and factor productivity growth.

Figure 5.14 depicts the links from five key fiscal institutions to growth and development. Medium-term fiscal frameworks, fiscal rules and fiscal

Figure 5.14 The Role of Fiscal Policy



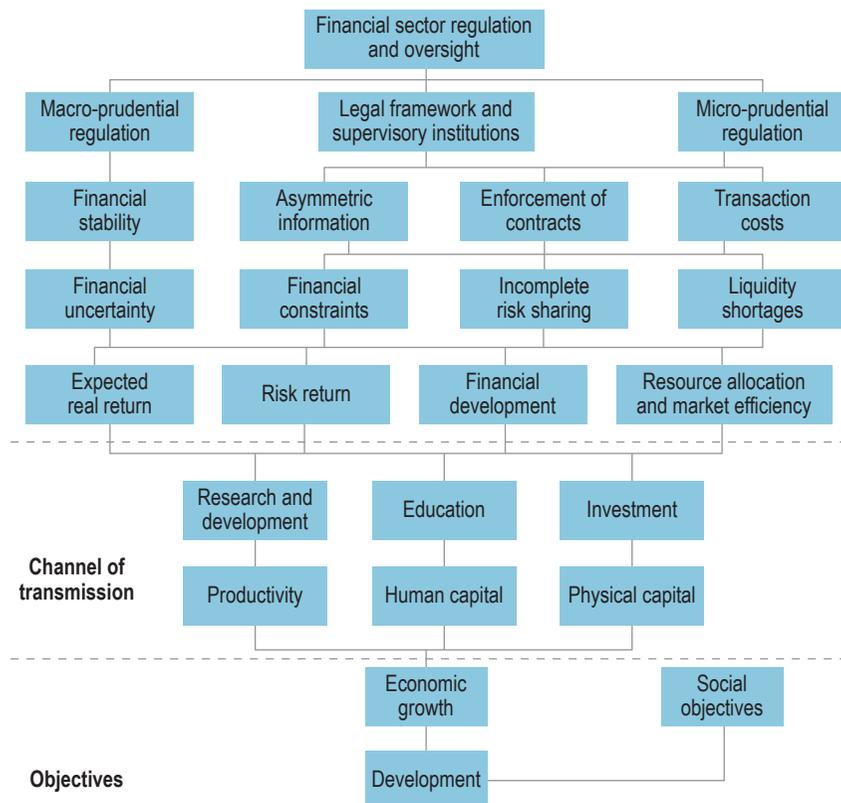
Source: Prepared by the author.

Figure 5.15 The Role of Exchange Rate and Monetary Policies

Source: Prepared by the author.

councils help reduce principal-agent problems and strengthen transparency and accountability in the conduct of fiscal policy, improving fiscal performance. Fiscal performance is also strengthened by an efficient tax system and well-managed sovereign wealth funds. Consequently, the incidence of economic crises and economic uncertainty is lessened, while macroeconomic stability is enhanced. Domestic short- and long-term interest rates are likely to decline, market efficiency and resource allocation improve, and the economy gets closer to its risk-return frontier. These benefits lead to greater accumulation of productive resources and further improvements in the productivity of those resources.

Exchange rate and monetary policies are strengthened by three key regimes and institutions in those countries that aim to conduct independent

Figure 5.16 The Role of Financial Sector Policies

Source: Prepared by the author.

monetary policy: a floating exchange rate regime, an independent central bank, and an inflation-targeting regime (Figure 5.15). This triad reduces the incidence of dynamic inconsistency in monetary policy and strengthens the credibility and reputation of central bank decisions. This may result in lower inflation and inflation volatility, lesser economic uncertainty, and strengthened macroeconomic stability, at the cost of higher short-term exchange rate volatility. The incidence of currency and banking crises is lessened. Transaction costs are lowered, resource allocation and market efficiency are boosted, and the distance from the risk-return frontier is reduced. Again, the previous effects lead to higher rates of factor accumulation and productivity growth.

Finally, Figure 5.16 presents the links from effective financial sector policies (combining financial liberalization with frontier regulation and supervision of financial markets) to growth and development. Regarding

financial oversight, the key institutional elements are an appropriate legal framework, frontier micro-prudential and macro-prudential regulation, and effective supervisory institutions. Having these institutional elements in place allows for reducing the incidence of several financial market imperfections, including weak contract enforcement, asymmetric information, financial constraints, incomplete risk sharing, liquidity shortages, and overall financial uncertainty. Improved financial certainty, lower and better diversified financial risk, and lower credit costs are likely to lead to improved resource allocation and market efficiency, macroeconomic stability, less frequent financial crises, and deeper and more developed financial markets. This implies better incentives for strengthened factor accumulation and productivity growth, enhancing growth and development.

5.2.2. Effects of Institutions: Empirical Evidence

Twelve methodological comments are in order on the scope of this review and the summary information presented in the tables that follow.

1. The review in this section comprises 125 empirical studies on the direct and indirect effects of 11 economic institutions on growth and development.
2. The set of studies comprises 115 multi-country (cross-section and panel-data) studies, six multi-state studies for a given country, and four country studies.
3. Most studies were published between 2000 and 2018; a few were published between 1990 and 1999.
4. The studies' multi-variate specifications are not derived from first principles but include potential causal variables as independent variables, which are broadly consistent with theory and previous empirical evidence.
5. Studies differ significantly in model specification, inclusion of right-hand-side regressors, estimation techniques, and samples. This review does not assess differences in the quality of models or the robustness of empirical findings of the studies surveyed here.
6. This is not a meta-analysis of previous research. However, it refers to the general conclusions reached by several meta-analyses and survey papers available on the effects of some of the institutions covered here. Those references are included in the subsequent text but not in the summary tables, which report results of individual studies.
7. Dependent variables include different measures of GDP levels and growth rates, close growth determinants (e.g., investment and

productivity), and other variables that are closely related to the corresponding institutions (e.g., fiscal performance measures in the case of fiscal rules).

8. Independent variables include measures and proxies of the institutions identified in the previous section and relevant controls.
9. Individual determinants included here are ordered by variable categories in the summary tables below.
10. Statistical significance of each relevant regressor is included by identifying the regressor's positive or negative sign (if significant at the 5 percent level), or both the zero and positive sign, or both the zero and negative sign if reported in different regressions of the same study. For example, Table 5.1 reports in its first line the empirical results on the effects of the dummy variable for open economies on per capita GDP growth. The first result is reported as + (1, 5), which means a statistically significant positive effect is reported by the studies listed as numbers 1 and 5 in the note to Table 5.1. The second result is reported as 0 or + (6), which means that the study listed as number 6 in the note to Table 5.1 reports two different results (in separate regressions), corresponding to statistically non-significant and statistically positive effects.
11. If at least one study reports a significant finding, other studies' statistically zero findings are also reported in the same line. For example, this is the case for the second line on per capita GDP growth in Table 5.1.
12. When one or several studies consistently report a non-significant result for the effect of an institutional variable, this result is not included as a line in the corresponding table. However, the studies that report non-significant results are identified at the end of the note to the corresponding table.

Tables 5.1–5.10 summarize the empirical findings on direct and indirect effects of the following economic institutions on growth and development.

International Integration

The direct effects of different measures of trade openness (trade liberalization and ex-post measures of trade-to-GDP ratios) on GDP growth rates and per capita GDP levels are generally positive and significant (Table 5.1). Eight studies report significant positive effects of different measures of openness on aggregate or per capita GDP growth. However, seven studies report non-significant results for some particular trade openness measures, although most of them present positive and significant results for other measures.

Table 5.1 Effects of Trade Openness

Dependent Variable	Independent Variable	Empirical Findings
Income and Growth		
Growth of GDP per capita	Dummy: 1 for open economies, 0 otherwise	+ (1, 5); 0 or + (6)
	Sum of exports and imports (percent of GDP)	+ (2, 7, 11); 0 (3); 0 or – or + (9)
	Dummy: 1 if the year is greater than the year of liberalization	0 or + (6)
GDP per capita	Sum of exports and imports (percent of GDP)	0 or + (2); 0 (10); + (12)
	Exports (percent of GDP)	0 (10); 0 or – or + (14)
	Composite Trade Share Index	+ (13)
Investment		
Foreign direct investment (percent of GDP)	Index of Trade Liberalization	0 or + (4); 0 or – or + (8)
	Barriers to trade: Tariff revenue (percent imports)	0 or – (4)
Gross fixed capital investment (percent of GDP)	Dummy: 1 if the year is greater than the year of liberalization	+ (6)
	Sum of exports and imports (percent of GDP)	+ (10)
	Exports (percent of GDP)	+ (10)

Sources: The sources for the results reported here are the corresponding tables and specific columns, rows, or regressions of the following studies: 1. Sachs et al. (1995, Table 11, columns 6–8); 2. Dollar and Kraay (2003, Table 1, columns 4–13; Table 4, columns 2–13); 3. Kraay (2004, Table 4, column 2; Table 5, column 2); 4. Demekas et al. (2007, Table 2, columns 2–3); 5. Kneller, Morgan, and Kanchanahatakij (2008, Table 2, column 2); 6. Wacziarg and Welch (2008, Table 3, columns 2–6; Table 5, columns 2–5); 7. Chang, Kaltani, and Loayza (2009, Table 1, column 2); 8. Kinoshita and Campos (2010, Table 1, columns 2–8; Table 2, columns 2–11; Table 3, columns 2–7; Table 4, columns 2–7); 9. Gries, Kraft, and Meierriecks (2011, Table 6, column 9); 10. Kim et al. (2011, Table 2, columns 2–5); 11. Gries and Redlin (2012, Table 4, columns 2 and 3); 12. Sakyi et al. (2012, Table 2, columns 2 and 3); 13. Sakyi, Villaverde, and Maza (2015, Table 4, column 2); 14. Huchet-Bourdon, Le Mouél, and Vijil (2018, Table 2, columns 2–8). The following studies report non-significant results for related variables: Kim, Lin, and Suen (2011, Table 2, columns 2–5); Kraay (2004, Table 4, column 3; Table 5, column 3).

Regarding indirect effects of trade openness on growth and development, there is weak evidence that trade liberalization and lower trade barriers increase foreign direct investment (FDI). There is strong evidence that trade liberalization and trade-to-GDP ratios raise gross fixed-capital investment.

The direct effects of different measures of capital account openness (aggregate and disaggregate measures of capital account liberalization, openness, and controls) on GDP growth are generally positive and significant (Table 5.2). However, one study reports positive results of capital controls on growth. Regarding indirect effects, capital account openness raises financial depth (measured by domestic credit to the private sector as percent of GDP).

Bumann, Hermes, and Lensink (2013) conducted a meta-analysis of previous research on the effects of external and domestic financial liberalization (capital account, banking, and equity market liberalization) on economic growth. The authors conclude that financial liberalization has, on average, a weak but positive effect on growth.

Table 5.2 Effects of Capital Account Openness

Dependent Variable	Independent Variable	Empirical Findings
Income and Growth		
Growth of GDP per capita	Quinn Capital Account Liberalization Index	+ (1); 0 or + (3, 6)
	Proportion of years in which countries had liberalized capital accounts (IMF dataset)	0 (1, 2, 3, 8); 0 or + (6)
	Index of Capital Controls	0 (4)
	Capital controls × (with financial crisis)	0 or + (5)
	Capital controls × (without financial crisis)	– (5)
	Index of Capital Openness	+ (9)
Growth of GDP	Dummy: 1 if controls on financial credits, equities, or collective investments in in t–1, else 0	0 or + (7)
Financial Development		
Domestic credit to private sector (percent of GDP)	Proportion of years in which countries had liberalized capital accounts (IMF dataset)	+ (8)

Sources: The sources are the corresponding tables and specific columns, rows, or regressions of the following studies: 1. Bekaert, Harvey, and Lundblad (2005, Table 4, columns 8 and 9); 2. Grilli and Milesi-Ferretti (1995, Table 4, columns 2–5); 3. Edinson et al. (2004, Table 5, columns 2–7); 4. Butkiewicz and Yanikkaya (2008, Table 1, columns 2–9); 5. Eichengreen and Leblang (2003, Table 4, columns 3 and 4; Table 6, columns 3 and 4); 6. Klein (2003, Table 1, columns 2–5); 7. Klein (2012, Table 4, columns 2–7); 8. Klein and Olivei (2008, Table 8, columns 2 and 4); 9. Quinn and Toyoda (2008, Table 8, columns 2–7).

Fiscal Policies

Tax cuts have generally positive effects on per capita GDP and GDP growth (Table 5.3). Corporate tax cuts and value-added tax reforms tend to have indirect positive effects on growth and development by raising investment, patents, research and development (R&D) spending, and business density, and by reducing corporate debt.

Medium-term fiscal frameworks or multiyear budgeting processes have been increasingly adopted worldwide constituting one of the most popular reforms to public budgetary processes (Filc and Scartascini 2010; World Bank 2012; and Vlaicu et al. 2014). Existing evaluations of their effectiveness, while relatively scarce, show unambiguous positive results. World Bank (2012) evidences that the adoption of medium-term fiscal frameworks improves fiscal balances, reduces overall expenditure volatility, and increases the share of public expenditures in human capital enhancement areas like health. Furthermore, the study also shows that complementing multiyear budgeting with performance targets by sector (denominated medium-term performance framework) improves the cost-effectiveness of public health expenditures. Vlaicu et al. (2014) using dynamic panel data models applied to a large sample of 181 countries worldwide from 1990 to 2008 that allow the authors to circumvent endogeneity concerns, show that

Table 5.3 Effects of Tax Reforms

Dependent Variable	Independent Variable	Empirical Findings
Income and Growth		
GDP per capita	1% tax liability cut	+ (5)
Growth GDP	1% legislative tax increase	– (7)
Investment		
Private sector gross investment per capita	1% tax liability cut	+ (5)
Foreign direct investment (percent of GDP)	Effective corporate tax	– (6)
Consumption		
Consumer expenditure per capita	1% tax liability cut	+ (5)
Innovation		
Number of patents by U.S. firms	Corporate taxes increase at the U.S. state level	0 or – (1)
	Dummy: 1 if there has been a significant tax increase, –1 if there has been a significant tax decrease and 0 otherwise	– (4)
Number of citations per U.S. patent	Dummy: 1 if there has been a significant tax increase, –1 if there has been a significant tax decrease, and 0 otherwise	– (4)
Pursue R&D (0 = No, 1 = Yes)	VAT reform (China), privately owned enterprises ^a	– (2)
	VAT reform (China), state-owned enterprises ^a	+ (2)
R&D spending (percent variation)	VAT reform (China), privately owned enterprises ^a	– (2)
	VAT reform (China), state-owned enterprises ^a	+ (2)
New product and process sales (percent variation)	VAT reform (China), privately owned enterprises ^a	+ (2)
	VAT reform (China), state-owned enterprises ^a	+ (2)
Firms		
Long-term book leverage by firms	Corporate taxes decrease at the U.S. state level	0 (3)
	Corporate taxes increase at the U.S. state level	+ (3)
Real long-term debt by firms	Corporate taxes increase at the U.S. state level	+ (3)
Business density (number of limited liability corporations) per 100 persons	Effective corporate tax	– (6)
Average number of limited liability corporations registered per year	Effective corporate tax	– (6)

Sources: The sources are the corresponding tables and specific columns, rows, or regressions of the following studies: 1. Mukherjee, Singh, and Zaldokas (2017, Table 2, panel A, columns 2–7); 2. Howell (2016, Table 8, columns 2–10); 3. Heider and Ljungqvist (2015, Table 3, columns 2–10); 4. Atanassov and Liu (2015, Table IIIA, columns 2–5; Table IIIB, columns 2–5); 5. Mertens and Ravn (2012, Figure 3); 6. Djankov et al. (2010, Table 5, Panel A, columns 2 and 5; Table 5, Panel B, columns 2 and 5); 7. Romer and Romer (2010, Figure 5, Panel C). The following studies report non-significant results for related variables: Mukherjee et al. (2017 Table 2, panel A, columns 2–7); Howell (2016, Table 8, columns 2–10); Heider and Ljungqvist (2015, Table 3, columns 2–10); Djankov et al. (2010, Table 5, panel A, columns 2 and 5); Tomljanovich (2004, Table 3, columns 2–4; Table 4, columns 2–4); Bloom, Griffith, and Van Reenen (2002, Table 1, columns 2–6).

Notes: R&D: research and development; VAT: value-added tax.

^a The VAT reform converted the VAT from the original production-based VAT to a consumption-based VAT, thereby removing the double taxation on investment goods (Howell 2016).

medium-term fiscal frameworks improve both total and primary budget balances. The authors also show that health expenditure volatility is reduced when fiscal frameworks establish both the aggregate resource envelope and the allocation of spending across sectors, programs and agencies. Finally, they show that health sector technical efficiency is positively affected only when medium-term performance frameworks are in place.

Regarding fiscal rules (aggregate or any rule, particular rules, Maastricht Treaty), most studies report significantly positive effects on per capita GDP growth (Table 5.4). Indirect effects of rules on GDP growth rates and GDP per capita levels are evidenced by positive significant coefficients of fiscal discipline on GDP.

There is also ample evidence that fiscal rules tend to improve fiscal performance, hence boosting growth indirectly. Several studies report positive and significant effects of different measures and types of fiscal rules on different measures of the budget balance. One study reports positive effects of fiscal rules on government deficits, but effects turn negative when the fiscal rule interacts with its legal enforcement. Government debt levels are not affected by fiscal rules.

Reported results on the effects of fiscal rules on fiscal policy cyclicality are mixed. In most cases, different fiscal rules do not affect the cyclical correlation between the government budget and GDP or between government expenditure and GDP. The exception is the expenditure rule, which reduces the cyclical correlation between government expenditure and GDP, hence turning fiscal policy more countercyclical.

Rules reduce government bond spreads. Fiscal rules raise the standard deviation of per capita GDP growth (not reported in Table 5.4) but reduce it when rules are interacted with a measure of discretionary fiscal policy (as reported in the table).

There is no evidence to date on direct effects of fiscal councils on GDP growth rates and levels. However, several studies report that fiscal councils significantly reduce GDP growth forecast errors (Table 5.5).

There is more evidence on the effects of fiscal councils on fiscal performance. Several studies report that different measures of fiscal councils significantly raise primary budget balances and significantly reduce their forecast errors. However, three studies report negative effects of councils on the level and variation of cyclically adjusted budget balances. A relevant result on the interaction between rules and councils is that existence of a fiscal council strengthens compliance with a numerical fiscal target rule.

There is also lack of evidence to date on the direct effects of sovereign wealth funds on GDP growth rates and levels. However, several studies show that sovereign wealth funds contribute to fiscal performance

and stabilization (Table 5.6). Funds are reported to reduce the level and growth rate of expenditure spending. Funds also reduce the volatility of government expenditure (both aggregate and capital spending) and the volatility of the cyclically adjusted fiscal balance.

There are several positive effects of funds on macroeconomic stability. Inflation levels decline and measures of volatility of broad money, inflation,

Table 5.4 Effects of Fiscal Rules

Dependent Variable	Independent Variable	Empirical Findings
Income and Growth		
Growth of GDP per capita	Overall Rule Index	0 or + (6)
	Expenditure Rule Index	0 or + (6)
	Budget Balance and Debt Rule Index	0 or + (6)
	Supranational fiscal rules in Eastern Caribbean Currency Union	0 or + (3)
	Supranational fiscal rules in Central African Economic and Monetary Community	0 or + (3)
	National fiscal rule	0 or + (3)
	Budget balance rules in low- and middle-income countries	0 or – (5)
	Maastricht Treaty (1997–2005)	+ (7)
Log GDP per capita	Index of Fiscal Discipline	+ (2)
Growth rate of GDP	Index of Fiscal Discipline	+ (2)
Fiscal Performance		
Fiscal policy volatility	Budget Balance Rule	– (1)
Government budget balance (percent of GDP)	Budget Balance Rule Index	+ (4)
	Budget Balance Rule	+ (16)
	Debt Rule	+ (16)
	Expenditure Rule	0 (16)
Government deficit (percent of GDP)	Budget Balance Rule	– (11); + (14)
	Legal enforcement × Budget Balance Rule	– (14)
	Expenditure Rule	0 (11); 0 or + (14)
	Debt Rule	– (14)
Real budget balance per capita	Fiscal Rule	+ (13)
Cyclically adjusted primary balance (percent of GDP)	Fiscal Rule Overall Index	0 or + (8)
	Fiscal Rule Coverage Index	0 or + (8)
	Output gap × Fiscal Rule dummy	+ (9)
Cyclical correlation between government expenditure and GDP	Budget Balance Rule	0 (16)
	Debt Rule	0 (16)
	Expenditure Rule	– (16)

(continued on next page)

Table 5.4 Effects of Fiscal Rules (continued)

Dependent Variable	Independent Variable	Empirical Findings
Cyclical correlation between government budget balance and GDP (continued)	Budget Balance Rule	0 (16)
	Debt Rule	0 (16)
	Expenditure Rule	0 (16)
Government debt (percent of GDP)	Budget Balance Rule	0 (16)
	Debt Rule	0 (16)
	Expenditure Rule	0 (16)
Other		
Government bond spread (10-year)	Balanced Budget Rule	0 or – (1)
	Fiscal Rule Index × Cyclical dummy	0 or – (10)
Government bond spread against the German Bund	Fiscal Rule Index	0 or – (12)
Standard deviation of the growth rate of real GDP per capita	Discretionary fiscal policy × Expenditure Rule	0 or – (15)
	Discretionary fiscal policy × Revenue Rule	0 or – (15)
	Discretionary fiscal policy × Budget Balance Rule	0 or – (15)
	Discretionary fiscal policy × Debt Rule	0 or – (15)
	Discretionary fiscal policy × Fiscal Rule	– (15)

Sources: The sources are the corresponding tables and specific columns, rows, or regressions of the following studies: 1. Badinger and Reuter (2017, Table 2, columns 3 and 5; Table 3, columns 3 and 5; Table 5, columns 2, 3, 4 and 6); 2. Maccim and Oprea (2017, Table 3, columns 2–7); 3. Menkulasi (2016, Tables 6.2–6.9); 4. Badinger and Reuter (2015, Table 5, columns 6–8); 5. Ray, Velasquez, and Islam (2015, Table A.2, columns 4–9; Table A.4, columns 4–9); 6. Afonso and Jalles (2013, Table 1, columns 2–13; Table 2, columns 2–13); 7. Castro (2011, Table 3, columns 2–8); 8. Debrun and Kumar (2007b, Table 2, columns 2–7); 9. Alberola et al. (2016, Table 4, columns 2 and 3); 10. IMF (2009, Appendix IIb, Table 1, columns 4–6); 11. Dahan and Strawczynski (2013, Table 2, columns 2 and 3); 12. Iara and Wolff (2014, Table 1, columns 2–13); 13. Krogstrup and Wälti (2008, Table 1, columns 2–7); 14. Neyapti (2013, Table 1, columns 2–7); 15. Sacchi and Saloti (2015, Table 4, columns 2–6; Table 5, columns 2–6); 16. Schmidt-Hebbel and Soto (2017, Table 4, columns 4–9; Table 5, columns 4–9; Table 6, columns 4–9; Table 7, columns 4–9). The following studies report non-significant results for related variables: Badinger and Reuter (2017, Table 2, columns 3 and 5; Table 3, columns 3 and 5; Table 5, columns 2, 3, 4, and 6); Maccim and Oprea (2017, Table 3, columns 2–7); Menkulasi (2016, Table 6.1); Ray, Velasquez, and Islam (2015, Table A.2, columns 4–9; Table A.3, columns 4–9; Table A.4, columns 4–9); Castro (2011, Table 3, columns 2–8); Alberola et al. (2016, Table 4, columns 2 and 3); IMF (2009, Appendix IIb, Table 1, columns 4–6).

and the effective real exchange rate are lowered by an oil fund. Adverse effects of commodity price volatility on physical capital are mitigated by a sovereign wealth fund.

Investments by sovereign wealth funds in corporations are a mixed blessing for those companies: the equity-price-to-book ratio rises, returns on equity decline, and Sharpe ratios decline.

Exchange Rate Regimes

De facto exchange rate regimes can have significant effects on growth. Consistent with the literature on optimal currency regimes, any regime—flexible,

Table 5.5 Effects of Fiscal Councils

Dependent Variable	Independent Variable	Empirical Findings
Forecast		
Absolute forecast error of GDP growth	Dummy: 1 if country has a fiscal council (FC)	– (3); 0 (6, 7)
	Dummy: 1 if country has a FC, legal independence	– (3); 0 (6)
	Dummy: 1 if country has a FC, safeguards on budget	– (3); 0 (6)
	Dummy: 1 if country has a FC, high media impact	– (3); 0 (6)
Forecast error of GDP growth	Dummy: 1 if country has a FC	0 or – (7)
	Fiscal Council × Fiscal Rule	+ (7)
Fiscal Performance		
Absolute forecast error of primary balance	Dummy: 1 if country has a FC	– (3, 6); 0 or – (7)
	Dummy: 1 if country has a FC, legal independence	– (3, 6)
	Dummy: 1 if country has a FC, safeguards on budget	– (3, 6)
	Dummy: 1 if country has a FC, high media impact	– (3, 6)
Primary balance	Fiscal Council Index × Fiscal Rule Index	+ (4)
Absolute value of the change in the cyclically adjusted bud balance	Intensity of media reports (t–1): number of times the official name of the FC appears in a country's national press	+ (2)
	Fiscal Council Index (t–1)	0 or + (5)
Cyclically adjusted primary balance	Fiscal Council Index	0 or – (1)
Primary balance	Dummy: 1 if country has a FC, legal independence	+ (6)
	Dummy: 1 if country has a FC, staff number	+ (6)
	Dummy: 1 if country has a FC, fiscal rule monitoring	+ (6)
	Dummy: 1 if country has a FC, costing of measures	+ (6)
	Dummy: 1 if country has a FC, forecast assessment	+ (6)
	Dummy: 1 if country has a FC, high media impact	+ (6)
Other		
Government compliance with numerical fiscal rule	Dummy: 1 if country has a FC in preceding period	0 or + (7)

Sources: The sources are the corresponding tables and specific columns, rows, or regressions of the following studies: 1. Debrun and Kumar (2007a, Table 3, columns 3 and 4; Table 4, columns 2–4); 2. Debrun, Gérard, and Harris (2012, Table 2, columns 2–6); 3. IMF (2013, Table 4, column 2; Table 6, column 2); 4. Maltritz and Wüste (2015, Table 2, column 2; Table 3, column 2); 5. Coletta, Graziano, and Infantino (2015, Table 5, columns 3–5; Table 6, columns 2 and 3); 6. Debrun and Kinda (2017, Table 5, columns 2–9; Table 6, columns 2–5; Table 7, columns 2–5); 7. Beetsma et al. (2018, Table 2, columns 2–8; Table 4, columns 2–8; Table 5, columns 2–8; Table 7, columns 2–10; Table 8, columns 2–6). The following studies report non-significant results for related variables: Maltritz and Wüste (2015, Table 2, column 2; Table 3, column 2); Debrun and Kinda (2017, Table 5, columns 2–9); Beetsma et al. (2018, Table 3, columns 2–8).

intermediate, or fixed—will affect growth, depending on the country's structural conditions. Unsurprisingly, the empirical evidence is mixed regarding the growth effects of exchange rate regimes in samples that are representative of all economies (Table 5.7). However, in separate samples comprising advanced

Table 5.6 Effects of Sovereign Wealth Funds

Dependent Variable	Independent Variable	Empirical Findings
Fiscal Performance		
Government expenditure	Stabilization fund dummy	0 or – (3)
	Stabilization fund dummy × GDP	0 or – (3)
Government expenditure growth	Sovereign wealth fund (SWF) dummy	0 or – (5)
	SWF dummy × GDP growth	– (4)
Volatility of government expenditure	SWF dummy	– (5)
Volatility of government capital expenditure	SWF dummy	– (5)
Volatility of cyclically adjusted fiscal balance	SWF dummy	– (5)
Stability		
Broad money volatility	Oil fund dummy	– (6)
Consumer Price Index inflation	Oil fund dummy	– (6)
Consumer Price Index inflation volatility	Oil fund dummy	– (6)
Real effective exchange rate volatility	Oil fund dummy	0 or – (6)
Capital stock per capita	SWF dummy × Commodity price volatility	0 or + (1)
Firm Performance		
Change in return on equity	SWF ownership in the company (t–1)	0 or – (2)
Price to book value of the company	SWF ownership in the company (t–1)	0 or + (2)
Sharpe ratio	SWF ownership in the company (t–1)	– (7)

Sources: The sources are the corresponding tables and specific columns, rows, or regressions of the following studies: 1. Mohaddes and Raissi (2017, Table 3, columns 8–10); 2. Urban (2017, Table 2, part 1, columns 3 and 5; Table 2, part 2, columns 2–5; Table 3, part 1, columns 2–5; Table 3, part 2, columns 2–5); 3. Asik (2017, Table 3, columns 2–13; Table 5, columns 2–9); 4. Coutinho et al. (2014, Table 6a, columns 2 and 6; Table 6b, columns 2 and 6); 5. Sugawara (2014, Table 1, columns 2–8; Table 2, columns 2–9); 6. Shabsigh and Ilahi (2007, Table 2, columns 2, 4, and 6; Table 3, columns 2, 4, and 6; Table 4, columns 2, 4, and 6); 7. Knill, Lee, and Mauck (2012, Table 5, column 2). The following studies report non-significant results for related variables: Mohaddes and Raissi (2017, Table 3, columns 2–7); Urban (2017, Table 2, part 1, columns 2 and 4; Table 2, part 2, columns 2 and 4); Bova, Medas, and Poghsyan (2016, Table 6, columns 3, 4, and 6); Koh (2017, Table 7, column 3).

(emerging and developing) economies, flexible (fixed) regimes are more likely to have positive effects. This is consistent with the fact that advanced (emerging and developing) economies tend to be larger (smaller), are more (less) likely to have a flexible (fixed or intermediate) exchange rate system in place and are more (less) likely to conduct an independent monetary policy.

Monetary Policy Frameworks

Central bank independence raises growth directly or indirectly by lowering central bank turnover and by boosting FDI (Table 5.8). Central bank independence also contributes to lower real interest rates on 10-year bonds.

Table 5.7 Effects of De Facto Exchange Rate Regimes

Dependent Variable	Independent Variable	Empirical Findings
Income and Growth		
Growth of GDP per capita	Flexible exchange rate regime: all economies	0 (5); – (7); 0 or – (3, 9); + (11); 0 or + (12)
	Flexible exchange rate regime: advanced economies	0 or + (14)
	Flexible exchange rate regime: emerging-market and developing economies	0 or – (14)
	Fixed exchange rate regime: all economies	0 (2, 11, 12); + (7); 0 or + (8); – (13)
	Fixed exchange rate regime: advanced economies	0 or – (4); 0 (13)
	Fixed exchange rate regime: emerging-market and developing economies	0 or + (4); – (13)
	Intermediate exchange rate regime: all economies	– (7, 13); 0 or + (11); 0 (12)
Growth of GDP	Fixed exchange rate regime: all economies	0 or + (1); 0 or – (6, 10)

Sources: The sources are the corresponding tables and specific columns, rows, or regressions of the following studies: 1. De Grauwe and Schnabl (2008, Table 4, column 6); 2. Petreski (2009, Table 3, columns 2–8); 3. Aghion et al. (2009, Table 1, columns 2–5); 4. Harms and Kretschmann (2009, Table 5, column 4); 5. Rose (2011, Table 2, columns 2–4); 6. Tsangarides (2012, Table 1a, columns 2–11; Table 2a, columns 2–11); 7. Bailliu, LaFrance, and Perrault (2003, Table H.1, columns 3, 4, and 7); 8. Harms and Kretschmann (2009, Table 1, columns 3–4); 9. Bleaney and Francisco (2007, Table 4, columns 3–6); 10. Coudert and Dubert (2005, Table 6, columns 2–3); 11. Garofalo (2005, Table 9, column 2); 12. Huang and Malhotra (2004, Table 1, column 2; Table 2, column 2); 13. Levy-Yeyati and Sturzenegger (2003, Table 5, columns 3–5); 14. Rogoff et al. (2003, Table 15, columns 2–10). The following study reports non-significant results for related variables: Coudert and Dubert (2005, Table 6, columns 2–3).

There is strong and systematic evidence, based on meta-analyses and surveys of previous research, that central bank independence contributes significantly and robustly to lower inflation (Berger, de Haan, and Eijffinger 2001; Klomp and de Haan 2010a). Further individual studies (included in Table 5.8) confirm the negative association between central bank independence and inflation, and the positive relation of central bank turnover (which is lowered by central bank independence) with inflation.

The evidence on inflation targeting and growth is mixed: most studies report evidence of positive growth effects of inflation targeting, but some studies report zero or negative effects (Table 5.9).

On inflation itself (and on inflation expectations) the results are also mixed but range from nil to negative effects of this monetary regime. As documented in the survey paper on inflation targeting by Schmidt-Hebbel and Carrasco (2016), the results depend on the country groups that are used as treatment and control groups in the corresponding studies. In advanced economies, inflation targeting is likely not to affect inflation,

Table 5.8 Effects of Central Bank Independence

Dependent Variable	Independent Variable	Empirical Findings
Income and Growth		
Growth of GDP per capita	Central bank governor turnover rate	0 or – (1); 0 (5)
Growth of GDP	Index of Central Bank Independence	0 or + (2)
Investment		
FDI	Index of Central Bank Independence	0 or + (3)
Other Variables		
10-year real bond rates	Index of Central Bank Independence	0 or – (3)
Central Bank Transparency Index	Index of Central Bank Independence	+ (4)
Index of Financial Instability Indicators	Index of Central Bank Independence	– (6)
Inflation		
Inflation	Central bank governor turnover rate	0 or + (7, 8, 9)
	Index of Central Bank Independence	– (8)

Sources: The sources are the corresponding tables and specific columns, rows, or regressions of the following studies: 1. Cukierman et al. (1993, Table 1, columns 2 and 6); 2. Garriga (2016, Table 2, columns 5 and 7); 3. Bodea and Hicks (2014, Table 2, columns 2–13); 4. Crowe and Meade (2008, Table 4, columns 2, 3, and 5); 5. de Haan and Kooi (2000, Table 6, column 2; Table 7, column 2); 6. Klomp and de Haan (2009, Table 2, columns 4, 6–9); 7. Klomp and de Haan (2010b, Table 1, columns 2–7); 8. Posso and Tawadros (2013, Table 1, columns 4 and 5; Table 2, columns 2–7); 9. Alpanda and Honig (2014, Table 6, columns 3, 5, and 7). The following studies report non-significant results for related variables: Grilli, Masciandaro, and Tabellini (1991, Table 16, column 2); Cukierman et al. (1993, Table 1, columns 3 and 5); Anastasiou (2009, Table A5, columns 2–7).

when compared to other advanced economies that do not employ inflation targeting. However, in emerging-market and developing economies, adoption of inflation targeting leads to significantly lower inflation, compared to other emerging-market and developing economies that do not employ inflation targeting.

Macroeconomic stability tends to be enhanced by inflation targeting. Most studies report negative effects of inflation targeting on the volatility of inflation, GDP growth, output gap, and short-term interest rates. As discussed by Schmidt-Hebbel and Carrasco (2016), this is likely a result of better anchoring of inflation expectations under inflation targeting.

Financial Sector Policies

Domestic financial liberalization can have negative effects on growth if it leads to rapid credit growth, excessive borrowing by households and firms, excessive risk-taking, and asset price bubbles, ending in financial crisis and deep recession. However, if financial liberalization is supported

Table 5.9 Effects of Inflation Targeting

Dependent Variable	Independent Variable	Empirical Findings
Income and Growth		
Growth of GDP per capita	Inflation targeting (D = 1)	0 or – (4)
Growth of GDP	Inflation targeting (D = 1)	0 (3); 0 or – (1); 0 or + (6, 8, 10)
	Soft inflation targeting (D = 1)	+ (5)
	Full inflation targeting (D = 1)	+ (5)
GDP per capita	Soft inflation targeting (D = 1)	0 or + (2)
	Full inflation targeting (D = 1)	0 or + (2)
Macroeconomic Variables		
Consumer Price Index inflation	Inflation targeting (D = 1)	0 (3, 6, 12, 19); 0 or – (1, 4, 7, 8, 10, 11, 13, 14, 15, 16, 20, 22); – (9, 17, 18)
Inflation expectations (one year ahead)	Inflation targeting (D = 1)	0 or – (10)
Stability		
Inflation volatility	Inflation targeting (D = 1)	0 (3, 6, 19); 0 or – (1, 10, 11, 13, 14, 21); – (9); 0 or + (8)
Growth of GDP volatility	Inflation targeting (D = 1)	0 (3, 6, 8, 9); 0 or – (1); – (10, 12)
Output gap volatility	Inflation targeting (D = 1)	– (9)
Volatility of short-term interest rate	Inflation targeting (D = 1)	0 or – (8, 10)

Sources: The sources are the corresponding tables and specific columns, rows, or regressions of the following studies: 1. Brito and Bystedt (2010, Table 2, columns 2–7; Table 3, columns 2–7); 2. Mollick, Cabral, and Carneiro (2011, Table 2, columns 6–11 ; Table 3, columns 6–11); 3. Naqvi and Rizvi (2009, Tables 2–5); 4. Ayres, Belasen, and Kutan (2014, Table 4, columns 2–6 ; Table 6, columns 2–6); 5. de Guimarães e Souza, de Mendoça, and de Andrade (2016, Table 1, columns 2–9; Table 2, columns 2–9); 6. Abo-Zaid and Tuzemen (2012, Table 13, columns 2–5; Table 14, columns 2–5); 7. Angeriz and Arestiz (2006, Table A1, Appendix, column 3); 8. Ball and Sheridan (2005, Table 6.3, panel B, columns 2–9; Table 6.4, panel B, columns 2–9; Table 6.6, panel B, columns 2–9; Table 6.7, panel B, columns 2–9; Table 6.9, panel B, columns 2–5); 9. Batini and Laxton (2007, Table 3, column 2); 10. Brito and Bystedt (2006, Table 2, panel B, columns 2–3; Table 3, panel B, columns 2–3; Table 6, panel B, columns 2–3; Table 7, panel B, columns 2–3; Table 8, panel B, columns 2–3; Table 9, panel B, columns 2–3); 11. de Mendoça and de Guimarães e Souza (2012, Table 3, columns 2–19; Table 4, columns 2–19); 12. Gonçalves and Carvalho (2008, Table 2, columns 2–4; Table 4, columns 2–4); 13. Lin and Ye (2009, Table 4, columns 2–8; Table 5, columns 2–8); 14. Mishkin and Schmidt-Hebbel (2007, Table 6, columns 2–7; Table 11, columns 2 and 3; Table 12, columns 2 and 3); 15. Valera (2017, Table 4.5, columns 2–9); 16. Calderón and Schmidt-Hebbel (2010, Table 3, columns 2–6); 17. Wu (2004, Table 2, columns 2 and 3); 18. Vega and Winkelried (2005, Table 3, columns 3–8); 19. Lin and Ye (2007, Table 3, columns 2–8; Table 4, columns 2–8); 20. Biondi and Toneto (2008, Table 3, columns 2–7); 21. Willard (2012, Table 1, columns 2–3 and 7–12); 22. Yamada (2013, Table 7, columns 3–9). The following studies report non-significant results for related variables: Abo-Zaid and Tuzemen (2012, Table 13, columns 6–7; Table 14, columns 6–7); Ball and Sheridan (2005, Table 6.8, panel B, columns 2–9).

by effective financial market regulation and supervision, it leads to gradual financial deepening, enhanced saving and investment, more innovation, better resource allocation and improved risk diversification, and higher growth. Against this backdrop however, it is interesting to note that many studies report positive effects of different ex-post measures of financial

Table 5.10 Effects of Financial Sector Policies

Dependent Variable	Independent Variable	Empirical Findings
Income and Growth		
Growth of GDP per capita	Banking sector development	+ (11)
	Stock market development	+ (11)
	Liquid liabilities (percent of GDP)	+ (10)
	Private credit (percent of GDP)	+ (10)
	Aggregate private credit	0 or + (1)
	Bank private credit to GDP	+ or – (5)
	Ratio of domestic credit to the private sector (percent of GDP)	+ or – (5)
	Assets in insurance companies, mutual funds, and pension funds	0 or + (5)
Log of GDP per capita	Aggregate private credit	+ (2)
	Liquid liabilities	+ (2)
	Private credit to GDP	+ (4)
	Insurance density (real insurance premiums per capita)	+ (3)
Innovation		
Number of patents	Stock market capitalization (percent of GDP)	+ (6)
	Domestic credit provided by the banking sector (percent of GDP)	– (6)
Introduction of new products and technologies	Share of firm investments that are externally financed	+ (7)
Growth Stability		
GDP per capita growth volatility	Private credit (percent of GDP)	– (8)
Standard deviation of GDP growth per capita	Ratio of total value traded (percent of bank credit)	+ or – (9)
	Ratio of domestic stock market capitalization (percent of bank credit)	+ or – (9)
	Ratio of capitalization of the private bond market (percent of bank credit)	+ or – (9)

Sources: The sources are the corresponding tables and specific columns, rows, or regressions of the following studies: 1. Aghion et al. (2009, Tables 1–2); 2. Law, Kutan, and Naseem (2017, Table 3, columns 2–3); 3. Liu, Lee, and Lee (2016, Table 3, column 2); 4. Ductor and Grechyna (2015, Table 4, columns 2–5); 5. Ruiz (2017, Tables 2 and 3); 6. Hsu, Tian, and Xu (2014, Tables 2 and 3); 7. Ayyagari, Demirgüç-Kunt, and Maksimovic (2011, Table 4, columns 2–3); 8. Islam (2016, Table 1, columns 2–7); 9. Bezooijen and Bikker (2017, Table 1, columns 2–7); 10. Compton and Giedeman (2011, Tables 1–2, columns 2–11); 11. Gazdar and Cherif (2015, Table 2, columns 2–3). The following studies report non-significant results for related variables: Gul, Podder, and Shahriar (2017, Table 5, columns 1–6); Law, Kutan, and Naseem (2017, Table 3, column 4).

depth and development on GDP levels and growth rates (Table 5.10). The measures range from banking and stock market proxies to credit-to-GDP ratios, nonbank financial assets, liquid liabilities, and insurance density.

Further indirect growth effects of financial development are likely to arise through improved innovation and growth stability. Stock market capitalization (but not bank credit) raises the number of patents and the share of external financing of firms accelerates introduction of new technologies and products. Finally, the volatility of GDP growth is reduced by the ratio of private credit to GDP and stock market capitalization, stock market trading, and bond market size.

5.3. What Determines Adoption of Institutions?

The previous survey shows that many key institutions contribute significantly to higher GDP levels and growth rates. Reverse causality from growth and development to institutions is also very likely. The reason is that more advanced and developed countries are more likely to design and establish innovative political, social, and economic institutions than emerging and developing economies. However, there are many potentially important factors that drive institutional change and adaptation, in addition to growth and development levels. This section refers briefly to the theory and evidence on the determinants of institutions.

5.3.1. *Establishment of Institutions: Theory*

A small but growing body of literature in economics and political economy has analyzed the conditions and determinants of institutional change, drawing from analytical models and cross-country experience. A brief selective review of this literature will help identify the variables that will be found in the subsequent empirical research on the adoption of institutions.

Good (bad) institutions in one policy dimension may breed good (bad) institutions in another realm. Hence it is not surprising that advanced economies exhibit high-quality institutions in most dimensions, while in poor countries the opposite is often observed. Also, past institutions that were adopted centuries ago are likely to affect current institutions in contemporaneous societies. Acemoglu, Johnson, and Robinson (2001) make this point, showing that European colonial institutions have strong effects on institutions and socioeconomic outcomes in the Americas even today.⁵

Rodrik (2000) refers to three forms of adopting good institutions in emerging-market and developing economies:

⁵ See Chapter 6 of this volume where the colonization experiences of Caribbean countries and their likely influence on contemporary institutional quality are analyzed.

1. Accepting institutional diversity
2. Acquiring institutions
 - Importing them from more advanced economies
 - Adapting them to local conditions
3. Using participatory politics as a meta-institution
 - Participatory political institutions are domestic meta-institutions that elicit and aggregate local knowledge and thereby help build better institutions.

Kingston and Caballero (2009) point toward three political economy theories of institutional change:

1. Collective choice: institutional change takes place as a result of rule-based negotiations among groups of individuals with conflicting interests.
2. Evolutionary process: change takes place because existing institutions fail and therefore require reform.
3. Equilibrium view: institutions reflect an equilibrium between different groups; hence any exogenous or endogenous shock to an existing equilibrium determines institutional change.

Lora and Olivera (2004) provide a comprehensive taxonomy of political economy theories that explain adoption or rejection of institutional reforms:

1. Distribution of costs and benefits: the distribution of costs and benefits among different groups ultimately determines the adoption of reforms.
2. Crises beget reforms: crises make adoption of reforms more likely.
3. Compensation schemes: compensating reform losers raises the likelihood of institutional change.
4. Contagion: other (preceding or simultaneous) reforms that are perceived as successful raise acceptance of additional reforms.
5. Optimal sequencing: a gradual, well-sequenced reform package is more likely to be adopted.
6. Other factors: change in government, international influence, and state capacity.

Drawing from Lora and Olivera (2004), Table 5.11 presents a comprehensive package of institutional reforms, where the potential losers of individual reforms are indirectly compensated by the effects of other reforms. For example, workers of state-owned enterprises that oppose

Table 5.11 Major Reform Opponents and Possible Indirect Compensation

	Major Opponents	Debilitating Factors	Possible Compensation
Trade Reform	Import-competing firms and their workers	Domestic demand recession	Devaluation; trade agreements
Domestic Financial Reform	Large firms; targeted credit users; large banks (especially state-owned banks)	Under high inflation: lower inflation tax	Reduce marginal income tax rates; improve access to external credit
Tax Reform	Medium to large-size firms, middle-class workers	Recession; lower wages; unemployment	Better access to credit and imported goods
Privatization	Workers of state-owned firms	Fiscal deficits; lower wages	Re-training programs and access to equity ownership
Labor Market Reform	Wage earners; unions	Lower wages; unemployment	Better access to social security; freedom to unionize

Source: Based on Lora and Olivera (2004).

privatization can be compensated in part by being provided with re-training and shares of privatized companies. Wage earners and labor unions that oppose labor market reforms can be compensated by being provided with better access to social security and more freedom to unionize.

5.3.2. *Establishment of Institutions: Empirical Evidence*

A recent review of OECD country reforms identifies initial economic, political, and reform conditions that are statistically significant (or not) in explaining the adoption of structural reforms of labor markets, product markets, framework conditions, and barriers to FDI (Da Silva, Givone, and Sondermann 2017) (Table 5.12). Reforms are more likely under adverse cyclical conditions (recession, high unemployment, low growth, low interest rates), an IMF assistance program, and/or a political majority in Parliament. Initial legal and regulatory conditions in the corresponding markets also raise the likelihood of adopting reforms.

In a recent survey paper, Schmidt-Hebbel and Martínez (2018) review the empirical literature on the determinants of establishing and maintaining economic institutions in advanced, emerging-economy, and developing countries. Their survey is based on findings reported by about 100 studies on the determinants of the economic institutions that were covered in Sections 5.1 and 5.2 of this chapter. The survey concludes that the main determinants of institutions can be grouped into seven categories.

First, development matters. Its proxy, GDP per capita, is a key co-determinant of the likelihood of adopting and maintaining most advanced economic institutions.

Table 5.12 Conditions that Determine Implementation of Structural Reforms in OECD Countries

	Labor Market Reforms	Product Market Reforms	Reforms on Framework Conditions	Reforms to FDI Barriers
Depth of Recession	+			+
Unemployment Rate	+			
Potential Growth	-	-	-	
Change in the General Government Annual Structural Balance	+		-	-
Short-Term Interest Rate	-		-	-
Financial Assistance Programmed by the IMF	+		+	+
Majority in All Houses of Government	+	+	+	
Single Market		+		
Employment Protection Legislation: Initial Conditions	+			
Energy, Transport, and Communication Regulation: Initial Conditions		+		
World Bank Doing Business Indicator; Initial Conditions			+	
FDI Legislation: Initial Conditions				+
Past Product Market Reforms	+			

Source: Da Silva et al. (2017, Table 5).

Notes: Blank cells indicate non-significant variables. FDI: foreign direct investment; IMF: International Monetary Fund.

Second, political regimes and political economy conditions matter. A higher level of democracy, less corruption, more government effectiveness, better quality of public institutions, political stability of the government, and government ideology significantly increase the likelihood of institutional change.

Third, few crises beget reforms. While crises (i.e., currency, banking, debt, and high inflation crises) may weaken reform opponents, it is not generally true that crises beget reforms. The evidence on the statistical significance of the timing of crises on reforms is weak and incomplete. Only trade and capital account liberalization are positively influenced by the incidence of some types of crises.

Fourth, financial development matters—weakly. Deep and diversified domestic financial markets co-determine economic institutions. The exception is the likelihood of having a floating exchange rate in place, which rises significantly with financial development.

Fifth, macroeconomic policy regimes and conditions matter—sometimes. A floating exchange rate contributes to the adoption of inflation

targeting. Monetary and fiscal policy conditions are statistically significant in explaining the adoption of exchange rate regimes, monetary regimes, and fiscal institutions (fiscal rules and sovereign wealth funds).

Sixth, macroeconomic conditions matter—sometimes. Often, but not always, inflation is positively associated with institutional change. The business cycle has a negative effect on institutional adoption, meaning it is more likely that institutions are put in place in recessions than in booms.

Finally, external conditions matter. Globalization (reflected by larger trade and capital account openness) and financial assistance provided by international financial institutions raise the likelihood of institutional reforms.

5.4. On Successful Design, Implementation, and Upgrading of Good Institutions

The previous section reviewed causal factors and conditions—including growth and development conditions—that explain the adoption of key economic institutions. This section complements the survey above by discussing different features and conditions that affect institutional design, implementation, and upgrading. It draws on the general literature on reforms, cited in previous sections, and on the authors' personal experiences.

International experience in the successful design, implementation, and upgrading of good economic institutions—that is, those that contribute to growth and development—suggest the concluding points outlined below.

5.4.1. *Current International Best Practices in Key Economic Institutions*

Current best practices are based on a combination of economic institutions that, according to current knowledge, implies the largest benefits for the conduct of policies, the behavior of households and firms, and overall growth and development. This mix combines high levels of international integration; a developed fiscal framework (including medium-term fiscal frameworks, fiscal rules, fiscal councils, and sovereign wealth funds); appropriate exchange rate and monetary regimes; and competitive, well-regulated, and well-supervised financial markets. Regarding the choice of exchange rate and monetary regimes, a floating exchange rate with inflation targeting is optimal for countries with an independent monetary policy. However, for smaller countries and/or those economies that are strongly integrated into large economies that

issue a reserve currency, a pegged exchange rate and an exchange rate anchor are optimal.

5.4.2. *Dynamic Evolution of Best Practices in Economic Institutions*

What is optimal today was not necessarily optimal some decades ago and is not likely to be optimal some decades into the future. For example, inflation targeting, medium-term fiscal frameworks, fiscal rules, and fiscal councils were largely unknown before 1995. What is understood by inflation targeting today is very different than what it meant at its start in 1990. The standards of bank regulation differ widely between Basel I and Basel III; macro-prudential regulation is a term developed only after the global financial crisis.

Best practices in economic institutions will continue evolving in the future, as technology, political demands, and policymaking change. This requires the continuing attention of policymakers, experts, and politicians to distil new international experience in order to adapt and change domestic institutions.

5.4.3. *Complexity*

Institutions vary enormously according to their complexity. On one extreme, best practices regarding international integration involve the free flow of goods, services, and capital across countries. Attaining this is relatively simple, as it implies eliminating domestic barriers to trade. On the other extreme is, for example, domestic financial liberalization carried out jointly with the establishment of domestic regulatory and supervisory standards in banking and capital markets to match international best practices. The latter is a very complex task that requires continuous upgrading as financial markets, instruments, and technology evolve.

5.4.4. *Legal Barriers to Institutional Change*

Different legal barriers must be overcome to adopt different institutions. Some institutions require constitutional changes, others need legal or regulatory amendments, and others are defined by technical authorities. Monetary institutions provide an example: central bank independence requires constitutional or legal amendments (depending on the country), while exchange rate and monetary regimes are determined by the minister of finance and/or the central bank board. Obviously, institutional change

must overcome more political hurdles if it involves legal or constitutional change approved by the legislature.

5.4.5. *Learning*

Institutional best practices evolve because of learning from domestic and international experience, policy contagion, and trial-and-error. Technology and more frequent contacts among policymakers and experts accelerate the international diffusion of best practices. As new institutional designs are tested every day in more than 190 independent countries, learning from international experience is made easy today.

Learning from policy failure is at least as important as learning from success. For example, financial liberalization without appropriate regulation and supervision—as occurred Latin America in the 1970s and 1980s, and in the United States in the 1990s and 2000s—led to deep financial crises and protracted recessions. These policy failures led to significant subsequent upgrading of financial regulation and supervision.

5.4.6. *One Size Does Not Fit All*

Institutions that are optimal for one type of country are not necessarily optimal for other countries. Two dimensions are critical for institutional choice: country development and country size. The degree of development determines the adoption of complex institutions, as shown by the empirical evidence discussed in the previous section. For example, financial markets are often underdeveloped in poor economies and therefore do not necessarily require complex regulation and supervision by large agencies staffed by financial market experts.

Country size represents a similar critical factor to consider for the effective adoption of complex institutions. In very small economies it is often not feasible to put in place complex, independent fiscal institutions like fiscal councils and sovereign wealth funds. Direct management of government resource rents by the Ministry of Finance, possibly constrained by a fiscal rule and accountable to Parliament, may constitute a more feasible fiscal framework in small economies.

5.4.7. *Timing, Sequencing, and Gradualism*

There is little systematic evidence on the optimal timing of institutional reform. The sooner reforms are undertaken, the earlier their benefits are reaped.

The sequencing of institutional changes—that is, which reforms should be done earlier and which subsequently—was intensely discussed both analytically and empirically during the 1980s and early 1990s, at a time of fundamental market reforms worldwide. However, no robust conclusions were reached about the optimal sequencing of reforms comprising different reform packages. Today, when discussing more refined policy reforms and institutions, the issue of optimal sequencing has all but disappeared from policy discussions.

On gradualism, there are institutions that are either not possible or not optimal to introduce gradually. This is evident in the case of adopting certain policy regimes (e.g., fiscal rules and inflation targeting) and institutional agencies (e.g., fiscal councils, sovereign wealth funds, and independent central banks).

However, the institutional complexity of the corresponding regimes and agencies can increase over time. For example, the tasks of an independent fiscal council could be widened over the years. Regarding inflation targeting, most countries adopted a “light” version of this regime during the 1990s that was gradually upgraded over subsequent years. Again, the complexity of institutions differs between rich and poor economies, and between large and small countries. Less complex institutions are often better in smaller countries than the complex institutions found in large advanced countries.

5.4.8. *International Technical Assistance*

International financial institutions and development agencies are uniquely positioned to provide technical assistance aimed at institutional improvements. They draw on extensive experience regarding international best practices in designing and implementing frontier institutions, as well as on the internal and external expertise of specialists. Many international institutions have made and are making a difference in helping countries—in particular, smaller economies and emerging-market and developing countries—bring their institutions closer to international best practices.

5.5. Conclusions

Good institutions are central to sustaining high growth in a narrow sense and to achieving development in a broad sense that attains economic, social, and political objectives. This chapter has surveyed the analytical literature and empirical evidence available to date on the direct and

indirect effects of key economic institutions and reforms on growth and development.

The chapter has focused on 11 formal economic institutions in three key areas of economic policy management: international integration, macroeconomic policies (fiscal policy, exchange rate, and monetary policies), and financial sector policies. The institutions analyzed here define current national best practices in the three areas of economic policy management, in both advanced economies and emerging or developing economies, for the following 11 institutions: trade openness, capital account openness, tax rates, medium-term fiscal frameworks, fiscal rules, fiscal councils, sovereign wealth funds, exchange rate regimes, central bank independence, monetary regimes, and financial sector policies.

The chapter presented the distribution of institutions over time and across 98 advanced and emerging-market or developing economies classified into four country groups: OECD member countries, Latin America, the Caribbean, and ROSE. The Caribbean here comprises the six countries that are members of the Inter-American Development Bank: The Bahamas, Barbados, Guyana, Jamaica, Suriname, and Trinidad and Tobago.

Several stylized facts emerge from the analysis in the chapter, as described below.

Rising trends in international integration have been observed in the four country groups since the 1970s. However, the degree of financial openness is still significantly higher in OECD countries than in other groups.

Direct and indirect tax rates are higher in advanced than in developing economies. Medium-term fiscal frameworks and fiscal rules have been adopted by many countries since the 1990s. However, they are more frequently found in larger and advanced economies; the only Caribbean country with such institutions is Jamaica. Since the 2008-2009 global financial crisis, fiscal councils have been instituted in many advanced countries but only in a few developing ones. Sovereign wealth funds are key fiscal institutions in natural-resource-exporting countries. Therefore, they are more often found in both advanced and developing resource-rich economies. Trinidad and Tobago is the only Caribbean country with a sovereign wealth fund.

A floating exchange rate is a pre-condition for conducting an independent monetary policy. By contrast, a hard peg or outright adoption of a foreign currency is optimal for smaller economies that are highly integrated with large economies. Unsurprisingly, flexible exchange rate regimes dominate in OECD countries and in many Latin American economies. However, soft and hard pegs dominate in small economies. All six Caribbean countries analyzed here have a soft peg in place.

Central bank independence—like a floating exchange rate regime—is an important institution in countries that pursue an independent monetary policy. Central bank independence has spread worldwide since the 1990s. The exception is the Caribbean country group, where independence remains low on average.

Since 1990, inflation targeting has been the monetary anchor of choice in many advanced and emerging-market or developing economies with an independent monetary policy. About half of OECD and Latin American countries targeted inflation by 2016. This stands in stark contrast to small economies (ROSE and the Caribbean), where inflation targeting is almost non-existent.

Liberalization of financial markets has been a key component of economic reforms in both advanced and emerging-market and developing economies since the 1970s. Liberalization of financial intermediation and development of new financial instruments and markets is potentially very beneficial for the efficient allocation of capital and risk, if financial intermediation and risk-taking are well regulated and supervised.

Since the 1970s, financial depth has shown an upward trend. In OECD countries, the average ratio of bank credit to the private sector was close to 100 percent of GDP in 2016, which is twice the ratio observed, on average, in Latin America, ROSE, and the Caribbean. This reflects the empirical association between overall development and financial development.

The chapter reviewed the theoretical links and the evidence on direct and indirect effects of the 11 economic institutions analyzed on growth and development. A brief review of the analytical literature revealed specific transmission mechanisms from institutions to growth and development that can be attained by improving policy regimes and by correcting market failures, leading to higher factor accumulation and productivity gains.

The chapter provided a survey of 125 empirical studies on the separate contribution of each institution, summarizing its statistically significant effects on GDP growth rates and levels, factor accumulation and productivity, macroeconomic policy performance and stability, and financial development. The survey found evidence that seven of 11 institutions—trade openness, financial openness, lower tax rates, fiscal rules, central bank independence, inflation targeting, and financial depth—contribute positively and statistically significantly to higher GDP growth rates and/or higher per capita GDP levels.⁶ Factor accumulation (mostly capital investment) and productivity growth are

⁶ This does not mean that the other four institutions do not contribute or contribute negatively to growth. It is simply that there is no evidence (yet). Similar comments apply to the subsequent reported findings.

positively affected by trade openness, lower tax rates, central bank independence, and different measures of financial development.

Several institutions were also found to contribute positively to different measures of macroeconomic and financial stability and development. Medium-term fiscal frameworks, fiscal rules, fiscal councils, and sovereign wealth funds significantly improve different measures of fiscal performance. Fiscal rules, fiscal councils, sovereign wealth funds, central bank independence, and inflation targeting contribute to different measures of macroeconomic performance and stability. Finally, financial openness increases financial depth.

Overall, there is compelling evidence suggesting that the 11 institutions covered in this chapter contribute significantly to growth and development, both directly and indirectly, by improving macroeconomic and financial performance.

It is likely that reverse causality from growth and development to institutional change and adoption is also important. To address this issue, the chapter briefly reviewed the analytical literature and referred to a survey of the empirical evidence on the determinants of adopting and having in place the 11 institutions covered here. There is a small economic and political economy literature on the factors that drive countries to adopt institutions, and there is a small complementary body of empirical findings on the drivers of economic institutions, based on international studies. A summary of the later points was provided, among them the fact that development matters, as richer countries are more likely to adopt and have in place advanced economic institutions. Political regimes and political economy conditions are also significant co-determinants of economic institutions. Few crises beget institutional reforms. Financial development is not a robust pre-condition or driver of institutions. Macroeconomic policy regimes also matter; for example, a floating exchange rate contributes to adoption of inflation targeting. Favorable macroeconomic conditions make the adoption of macroeconomic institutions more likely. Finally, globalization matters, as international integration and financial assistance provided by international financial institutions increase the likelihood of institutional reforms.

Beyond the adoption of institutions, the chapter reviewed specific conditions that affect institutional design, implementation, and upgrading over time. Current international best practices represent a combination of economic institutions that, according to current knowledge, implies the largest benefits for the conduct of policies, the behavior of households and firms, and growth and development performance. This mix combines high levels of international integration; a developed fiscal framework (including medium-term fiscal frameworks, fiscal rules, fiscal councils, and sovereign

wealth funds); appropriate exchange rate and monetary policy regimes; and competitive, well-regulated, and well-supervised financial markets.

Yet, best practices are dynamic: what is optimal today was not necessarily optimal three decades ago and will not be optimal some decades into the future. International diffusion of the changing international frontier in institutional best practices is accelerated by technology and frequent international contacts among policymakers and experts.

Economic institutions vary in complexity, ranging from simple measures (like trade and financial opening) to complex changes (like the adoption of legal and regulatory frameworks for financial markets, instruments, and corporations). Legal and regulatory barriers that must be overcome when reforming institutions are also very different across different reforms, ranging from constitutional reform (e.g., adopting central bank independence) to decisions by technical authorities (e.g., adopting inflation targeting).

Certainly, one size does not fit all. Two country features are critical factors for institutional choice: country development and country size. For example, low financial development in lower-income countries requires less sophisticated financial laws and regulations than richer economies, and complex fiscal institutions are also not on the reform priority list in poorer countries. Regarding country size, the choice of exchange rate and monetary policy regimes is significantly co-determined by country size and integration into larger economies.

Optimal timing, sequencing, and gradualism of different reforms were high on the policy and research agenda during the 1980s and 1990s. However, that is no longer the case because very few general recommendations, abstracting from particular country conditions, can be drawn regarding these dimensions of reform implementation.

International financial institutions and development agencies are still uniquely positioned to provide technical assistance—sometimes complemented by financial support—to help countries undertake institutional reforms. Drawing on international experience and their policy advice expertise, these international entities make a difference in supporting the adoption of frontier economic institutions, especially in smaller countries and emerging-market and developing economies.

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SECTION III:

The Institutional Setting in the Caribbean

Colonization and Institutions in the Caribbean

Christian Dippel and Jeetendra Khadan

Institutions and the historical conditions that influenced their formation are now widely considered important to understanding differences in economic development across countries (Acemoglu and Robinson 2012; Knack and Keefer 1995; Mauro 1995). As shown in Chapters 3 and 4 of this volume, several studies have linked the colonization experience of countries to their contemporaneous institutional quality, and through that, economic performance (e.g., Acemoglu, Johnson and Robinson 2001; Bruhn and Gallego 2012; Michalopoulos and Papaioannou 2013). There are alternative views on the channels through which the colonial experience may have influenced present-day development outcomes. Some economists have argued in favor of a “colonizer effect,” whereby British colonies benefitted from legal systems that were favorable for economic performance, compared to other colonial powers (La Porta et al. 1999). Others have emphasized that pre-existing conditions—among them the existence of coercive states, the suitability of soil for plantations, and mortality rates among early European settlers—had a strong influence on whether the colonists set up extractive states or, to the contrary, established “neo-European” settler states with good institutions that protected property rights, promoted the rule of law, enforced constraints on politicians, and provided equal opportunity to the majority of the population (Engerman and Sokoloff 1997, 2001; Acemoglu, Johnson, and Robinson 2001, 2002).¹

This chapter draws on this body of literature with a threefold objective. First, survey the literature to identify the different historical characteristics that have been found to influence the quality of contemporaneous institutions worldwide. Second, characterize the historical trajectories of Caribbean countries vis-à-vis those historical components that the literature has identified as determinants of institutional quality. Third, take stock

¹ The term “neo-European” was coined by Crosby (1986).

of the overall institutional quality in each Caribbean country to describe whether contemporaneous institutional gaps across these states map the differences in terms of historical trajectories that the literature has identified as important determinants of long-term institutional quality. Our approach, therefore, will investigate whether the institutional experiences in the Caribbean match with historical characteristics that the literature has identified as relevant. However, our exercise is descriptive in nature and does not claim any direct causal interpretation.

Descriptively examining a potential link between colonialism and present-day institutions, however, is particularly important for the Caribbean. European colonists had a profound influence on the region's politics, economy, and institutions. This history persists in the former colonies through their constitutions, language, education systems, transportation and trade linkages, and ethnic composition, as well as the economic models they follow. In terms of language, the official language of the former British colonies is English, while it is Dutch for Suriname. On attaining independence, the ex-British Caribbean colonies adopted the Westminster model of government, while Suriname followed the Dutch model. Similarly, the economic model and trade linkages that were in place during the colonial period were reinforced by Yaoundé agreements and Lomé conventions: monocrop economies exporting primary commodities to metropolitan markets. Moreover, through slavery and indentureship, colonialism altered the ethnic composition of populations, which later influenced the organization of political parties in many countries.

The next section reviews the literature examining the link between historical colonialism and present-day institutions with the objective of characterizing relevant aspects for the Caribbean. Then we provide a brief historical review of the colonization and post-independence experiences of The Bahamas, Barbados, Guyana, Jamaica, Suriname, and Trinidad and Tobago emphasizing the historical regularities that the evidence points out as relevant for the formation of institutions. The chapter then proceeds to take stock of contemporaneous measures of public policy and government capabilities to describe whether institutional gaps across Caribbean countries map with the colonial characteristics identified as relevant by the existing literature. Finally, we offer some concluding remarks.

6.1. Colonization and Post-independence Development: Key Lessons from the Literature for Caribbean Countries

Empirical studies have found a link between the process of colonization and the long-run development of former colonies as it relates to issues

such as economic growth, provision of public goods, democracy, and corruption. This has been surveyed, along with the literature on institutions more generally, in Chapter 3 of this book. Thus, the aim here is to narrow in on key aspects of colonial heritage that are applicable to the Caribbean's institutional formation and development. As we show in this section, three such aspects are relevant for Caribbean countries: different colonizers, the type of colonial institutions, and the varying historical approaches of those institutions in terms of securing labor inputs, which resulted in different degrees of ethnic fragmentation across the former colonies.

6.1.1. *The Colonizer Effect*

Several studies have found that British colonization led to better outcomes than colonization by the French or by the smaller colonial powers, with the most influential explanation to support this view focusing on attributes of the British legal system that presumably were favorable for economic growth (Hayek 1960; Lipset 1994; North 2005; La Porta et al. 1998). Drawing from many studies, Lee and Schultz (2012, 4) summarized the three main mechanisms through which the British legal system is thought to have positively impacted the development of British colonies: "(1) the common law systems provided greater rights to investors and property owners, (2) the British culture created a strong commitment to the enforcement of those rules, and (3) the independent judiciary and emphasis on separation of powers in common law systems provide a greater number of checks on political expropriation." Table 6.1 summarizes other key hypotheses and evidence from the literature in support of the idea that British colonization was better than colonization by other colonial powers.

6.1.2. *Do Colonial Institutions Matter?*

The positive attributes of British colonization did not go untested. Several empirical studies found evidence that did not support the "colonizer effect" hypothesis (Acemoglu, Johnson, and Robinson 2001; Acemoglu et al. 2009). From a theoretical perspective, the critique of the identity of the colonizer argument was that it did not account for the large unobserved variations attributed to pre-existing conditions in colonies, actual colonial institutions, and post-colonial policies. Rather, Acemoglu, Johnson, and Robinson, (2001, 2002) emphasize the importance of pre-existing conditions within each colony, which influenced the type of colonial institutions imposed by the colonizer. The authors argue that colonization strategies pursued by the Europeans had very different implications for economic

Table 6.1 Key Findings in Support of the Colonizer Effect

Study	Key Findings
Treisman (2000, 439–40)	Countries that were colonies of the British (or the United Kingdom) have significantly lower perceived corruption. This might reflect the fact that most former British colonies have common-law legal systems. Slightly stronger evidence suggests, however, that the British heritage effect is linked to a distinct “legal culture” governing the way the law is administered and enforced.
Hall and Jones (1999)	Output per worker is correlated with language, with English having a particularly strong positive effect, which Hall and Jones (1999) see as being primarily caused by the positive economic effect of European settlement (Lee and Schultz 2012, 5).
Klerman et al. (2008)	Education policies are the main reason why former British colonies have grown faster than former French colonies.
Weiner (1989); Huntington (1984)	British colonies are more likely to become democracies than are colonies of other nations, which is thought to be caused either by higher levels of political representation in former British colonies (Lipset 1994), the more gradual process of decolonization in the British empire (Smith 1978), or the greater level of indirect rule in British territories (Whittlesey 1962; Lee and Schultz 2012, 5).
Agbor, Fedderke, and Viegi (2010, 24)	The indirect influence of colonial education policies matter more for post-colonial growth than their direct influence. Agbor, Fedderke, and Viegi (2010) found that former British sub-Saharan Africa colonies grew marginally faster than former French colonies during 1960–2000, and that this is attributable to the favorable contribution of the indirect influence of the legacy of British colonization in education.

Source: Prepared by the authors.

development: institutions that enforced property rights and placed restrictions on politicians and powerful elites performed better than those that established extractive institutions.

Acemoglu, Johnson, and Robinson (2001) found evidence that different colonial policies and institutions yielded different development outcomes for colonies, and they identified different types of colonial policies: one extreme was the extractive state, and the other was the settler state. The extractive state did not provide much protection for private property rights and did not institute checks and balances against government expropriation, while in settler states or “neo-Europes,” colonizers tried to replicate European institutions, with a strong emphasis on private property and checks against government power. In fact, the main purpose of extractive states was to transfer wealth from the colony to the colonizer. It is the persistence of the colonial institutions and policies that some researchers have found to be important for partly explaining development outcomes in the post-independence era.

Particularly compelling evidence in favor of this view is presented in Bruhn and Gallego (2012). They focus specifically on the Americas and show that the historical colonial exploitation of labor led to economic underdevelopment in the long run. Their study is particularly compelling

because their data on both historical labor exploitation and on present-day economic development are at the subnational level, which expands their dataset from 17 countries to 345 regions and allows them to show that the same insight that holds across countries also holds within countries.

But why have colonial institutional legacies carried over into the post-independence era? It is costly to change institutions, especially if the cost had been sunk by colonial powers. Acemoglu, Johnson, and Robinson (2001) argued that if the new elites inherited extractive institutions at the time of independence, they are more likely to have a stronger preference to exploit the extractive system rather than incur the cost of introducing better institutions. In post-independent Sierra Leone, for example, governments continued to use the strategies of the British colonizers to solidify political control and extract resources from the rest of society (Reno 1995, as cited in Acemoglu, Johnson, and Robinson 2001). A comparable situation was also observed in Latin America (Coatsworth 1978; Lynch 1986). On the persistence of extractive institutions, Young (1994, 283) noted that “although we commonly described the independent polities as ‘new states,’ in reality they were successors to the colonial regime, inheriting its structures, its quotidian routines and practices, and its more hidden normative theories of governance.”

In this regard, it is worth quoting Acemoglu (2003, 29):

“European colonists did not set up institutions to benefit society as a whole. They chose good institutions when it was in their interests to do so, when they would be the ones living under the umbrella of these institutions, as in much of the New World. In contrast, they introduced or maintained existing extractive institutions when it was in their interest to extract resources from the non-European populations of the colonies, as in much of Africa, Central America, the Caribbean, and South Asia. Furthermore, these extractive institutions showed no sign of evolving into better institutions, either under European control or once these colonies gained independence. In almost all cases, we can link the persistence of extractive institutions to the fact that, even after independence, the elites in these societies had a lot to lose from institutional reform. Their political power and claim to economic rents rested on the existing extractive institutions, as best illustrated by the Caribbean plantation owners whose wealth directly depended on slavery and extractive institutions. Any reform of the system, however beneficial for the country as a whole, would be a direct threat to the owners.”

6.1.3. *Ethnic Diversity*

Ethnic fragmentation is one of the legacies of colonization that has become a decisive element in the post-independence Caribbean political processes. The European colonists of the Caribbean brought slaves from Africa to work on plantations. The slave trade was ended in 1808, 30 years before slavery itself ended in 1838. This created significant differences across the colonies in the relative supply of and demand for plantation workers on the eve of emancipation. These differences, in turn, ended up creating significant differences in ethnic composition today. In colonies with an insufficient supply of labor, plantations turned to importing indentured workers from Asia. As a result, significant ethnic factions developed in some places. Two major ethnic groups emerged in Guyana and Trinidad and Tobago, while Suriname is more diverse, with five such groups. Moreover, ethnic groups in the colonies remained largely segregated, although not by formal design. In the case of Trinidad and Tobago, for example, after slavery was abolished, Africans moved to and settled in the urban centers while persons from India who were recruited as indentured workers to replace the African slaves were settled in the proximity of the plantations, with restrictions on their movement (Mc Letchie 2013). Similar patterns of settlements emerged in Guyana (Bisram 2015).

While ethnic divisions already existed under colonialism, they were often accentuated with independence. In the period leading up to independence, there was some level of insecurity among the ethnic groups in each colony. In Trinidad and Tobago, for example, persons from India were concerned that when the British left they would be under the dominance of Africans, a community that “had [already] organized itself politically... gained access to English language education, staffed the police and civil service and influenced the government” (King 2003, 17). Hence, as the colonies transitioned into independent states with democratic systems, ethnic-based political rivalry took hold. Table 6.2 summarizes the key features of the main political parties in Caribbean countries.

The importance of ethnic divisions in the formation of policy was first documented systematically for Africa by Easterly and Levine (1997) and has since been confirmed in many studies. Some studies emphasize the inefficiencies arising in policy formation from ethnic divisions, for example because of diverging preferences for the provision of certain public goods (Alesina, Baqir, and Easterly 1999). A potentially more important aspect in the Caribbean context is the direct detrimental impact of ethnic fractionalization on the political process itself. For example, Banerjee and Pande (2007) show that ethnic voting leads to lower-quality politicians. Padro i Miquel (2007) shows that ethnic politics may allow leaders to extract more

Table 6.2 Characterization of Main Political Parties

Country	Political Party	Party Orientation	Ethnic Base	Age of Party (years)	Voting Rules
The Bahamas	PLP	Center	African	52.5	Plurality
	FNM	Right	African	43	
Barbados	DLP	Left	African	69	Plurality
	BLP	Right	African	77	
Guyana	PNC	Left	African	58	Proportional representation
	PPP	Left	Indian	45	
Jamaica	PNP	Left	African	75	Plurality
	JLP	Right	African	72	
Suriname	NPS	Unknown	Creole	69	Proportional representation
	VHP	Left	Indian	66	
	NDP	Left	Creole	28	
Trinidad and Tobago	PNM	Right	African	59	Plurality
	UNC	Center-left	Indian	26	

Source: Prepared by the authors based on the Constituency-Level Elections Archive database.

Notes: PLP: Progressive Liberal Party; FNM: Free National Movement; DLP: Democratic Labor Party; BLP: Barbados Labor Party; PNC: People's National Congress; PPP: People's Progressive Party; PNP: People's National Party; JLP: Jamaica Labor Party; NPS: National Party of Suriname; VHP: Progressive Reform Party (formerly known as the Verenigde Hindoestaanse Partij or United Hindustani Party); NDP: National Democratic Party; PNM: People's National Movement; UNC: United National Congress.

rents by exploiting their own supporters' fear that another leader representing the other group may be even worse. Moreover, a number of empirical studies have found a negative correlation between ethnolinguistic segregation and the quality of government, which largely occurs through the threat of secession, a lack of generalized trust in society, and ethnic voting (Alesina and Zhuravskaya 2011; La Porta et al. 1999; Alesina and Glaeser 2004).

To summarize, the literature connecting colonization and development finds that, in general, former colonies with particular pre-independence conditions are less likely to establish "good" institutions necessary to support long-run development. The conditions reducing this likelihood include the presence of colonial extractive institutions, ethnic fragmentation, and not being colonized by the British. As such, the next section provides brief historical summaries for each Caribbean country from colonialism to post-independence.

6.2. Colonization and Post-independence Experiences: A Caribbean Snapshot

6.2.1. European Colonization of the Caribbean

The West Indies was first inhabited by Spain in the 16th century. But as the Spanish influence started to decline by the 17th century, other European

Table 6.3 Timing of Colonialism in the Caribbean

Country	Onset of Colonialism	Conclusion of Colonialism
The Bahamas	1783	1973
Barbados	1627	1966
Guyana	1814	1966
Jamaica	1655	1962
Suriname	1651	1975
Trinidad and Tobago	1797	1962

Source: Lange, Mahoney, and vom Hau (2006).

Notes: Dates are after British colonization. Britain was the last and definitive colonial power in all of the countries above, except for Suriname.

countries took an interest in the region, including Britain, France, and the Netherlands (Table 6.3). The British established a colony in Barbados in 1627 and Barbados remained a British colony until independence in 1966. The Dutch established trading posts in Guyana in 1580, but Guyana changed hands several times between the Dutch, French, and British during the period from 1780–1813. Although the British had occupied Guyana since the Napoleonic wars, it was only in 1831 that Guyana was declared a British colony. Jamaica was occupied by Spain in 1509 and later captured by the British in 1655. The Dutch, British, and French attempted to settle in Suriname during the period from 1600 to around 1650, but all failed. The British were the first Europeans to establish a permanent settlement in Suriname in 1651. However, Suriname changed hands in 1667 when the British traded their part of Suriname to the Netherlands for New Amsterdam (later called New York City). Suriname was given full autonomy in 1954, but with the Netherlands retaining control over its defense and foreign affairs. Trinidad was colonized by the Spanish in 1532 while the Dutch settled on the island of Tobago in 1632. More Dutch and French settlers followed as the island changed hands several times during the period from 1650 to 1814, at which time Tobago came under British rule, and by 1889 Trinidad and Tobago had become a single British colony.

6.2.2. *The Caribbean Plantations and Labor Inputs*

Most Caribbean colonies, whether British or Dutch, produced mainly sugar and other primary goods. With natural resource endowments and climatic conditions conducive to extracting raw materials and produce primary commodities, the Europeans established plantation-type colonies in most Caribbean countries. As a notable outlier in this respect, The Bahamas, after a failed experiment in tobacco growing, developed an essentially

Table 6.4 Key Characteristics of Caribbean Colonies

	The Bahamas	Barbados	Guyana	Jamaica	Suriname	Trinidad and Tobago
Colonizer	British	British	British	British	Dutch	British
Type of Colony	Mercantile	Extractive	Extractive	Extractive	Extractive	Extractive
Main Crop(s)	Non-agricultural	Sugar	Sugar	Sugar	Sugar, cotton, indigo, and coffee	Sugar and cocoa
Labor Inputs (main sources)	Africa	Africa	Africa and India	Africa	Africa, China, Madeira, India, and Indonesia	Africa, India, and China

Source: Prepared by the authors based on Higman (1986).

mercantile economy as early as the 18th century (Lewis 2004, Chapter 12). The primary objective of these plantations was to exploit wealth and resources from the colony to empower the colonizer. Sugar was the main crop, although other crops such as coffee, indigo, cotton, and rice were also grown. Sugar became a very lucrative business for the Europeans and they amassed great wealth, allowing them to expand their global empire.

The labor inputs into Caribbean plantations came initially in the form of white indentured servants. However, these workers proved to be unreliable due to high mortality rates, and to their freedom to purchase or rent their own land and return to Britain or go to other colonies once their term of indentureship was over. With growing demand for luxury goods in Europe, labor in the colonies was critical, and this led to the transatlantic slave trade and the massive enslavement of Africans to meet the demand. As slavery ended throughout the British Empire in 1838, the Europeans turned to indentured workers from Asia, primarily East Indians, to work on plantations in some Caribbean countries (Table 6.4).

The next section examines the transition from colonialism to independence, followed by a brief review of the historical experience of each Caribbean country in some detail.

6.2.3. *The Transition from Colonialism to Independence*

Recently, the notion of administrative or state capacity has gained much traction with economists, the idea being that there are tangible and consequential differences in an administration's culture and the administrative know-how embedded in it. This is a potentially important driver in former colonies' post-independence performance. Patterson (2014), for example, makes the compelling argument that in some Caribbean colonies (notably Barbados and arguably The Bahamas), the British administration

transmitted its administrative knowledge and capacity to the non-British population, so when colonialism ended, the newly independent states did not have to start from a blank slate. Quantitative research into this question is in its infancy, but the argument carries much merit. The sections that follow review the historical experiences of individual Caribbean countries and how those experiences contributed to shape their institutional settings.

The Bahamas

The Bahamas is a clear outlier among the countries studied in this book in that its economy transitioned away from plantation agriculture very early on. As Lewis (2004, 325) notes, The Bahamas' "productive system, after a failed start in tobacco growing, was eminently mercantile." As is so often the case, the reasons were geographic: the islands' very low elevation made any agricultural crops particularly vulnerable to hurricanes because of the associated storm surges.² In addition, The Bahamas is highly fractured into many smaller islands, making inner-island transportation of agricultural output very difficult.

As a result, in the 18th century The Bahamas was already mostly associated with piracy, shipwrecking, and the production of sea salt. While slaves were still important, slavery had a different character than elsewhere in the Caribbean, and there was a much less stratified slave society (Craton 1997, 225).

In the 19th century The Bahamas took on an even more mercantile character. This was aided by its proximity to the United States. At two key moments, The Bahamas became a major smuggling port for the U.S. market. During the Civil War (1860–1865), southern cotton circumvented the Union Army's sea blockade by going through The Bahamas. Then again, during the Prohibition era of the 1920s, The Bahamas became a major smuggling port for U.S. bootleggers.

While The Bahamas' merchant elite—known as the "Bay Street Boys" of Nassau (Lewis 2004, 314)—made some attempts to institute coercive wage-labor contracts similar to those on other islands, wage labor and the legacy of slavery never had anywhere near the importance that they did elsewhere in the Caribbean. Craton (1997, 231) characterized the lives of freed slaves in The Bahamas as a sort of blissful "proto-peasantry" that

² Storm surges are hurricane-generated waves that hit the islands. At very low elevations, these surges can inundate agricultural land in ocean water, and the resulting salination can ruin harvests or render agricultural land unproductive for several growing cycles.

insulated freedmen from many of the coercive pressures of the plantations felt elsewhere. The Bahamas, therefore, is a distinctive Caribbean country in its relative lack of extractive colonial institutions, aspect that has been found to favor the emergence of “good” institutions in general by the literature reviewed in the previous section. In addition, it shares historical features that have been also suggested as positive determinants for institutional quality: British colonizers and low ethnic fragmentation. In combination, the lack of suitability for agriculture and the proximity to the United States gave rise to The Bahamas’ economic structure today, in which over 50 percent of gross domestic product (GDP) is generated in the tourism sector and 15–20 percent in financial services.

Barbados and Jamaica

The contrast between Barbados and Jamaica is particularly interesting for two reasons. First, the two islands are superficially very similar in their institutional and economic history. Both had been British colonies for a long time (compared to the relatively recent colonial acquisitions of Guyana and Trinidad) and had economic structures up to emancipation in 1838 based entirely on slave-produced sugar. Post-independence, the two countries had practically identical constitutions. Second, beyond their constitutional similarities, the two countries have diverged significantly in the post-independence period. While per capita incomes of Barbadians were about 60 percent higher than those of Jamaicans in 1950, they are about 300 percent higher today.³

It is natural to ask what explains this stark divergence. Henry and Miller (2009) provide a tentative answer: the divergence in economic outcomes can be traced to a divergence in macroeconomic policies. While Jamaica’s

³ The World Bank’s World Development Indicators (<https://data.worldbank.org/data-catalog/world-development-indicators>) report that Barbados’ per capita GDP reached US\$16,000 (inflation-adjusted) in 2007, up from US\$4,000 in 1980. Jamaica’s GDP per capita was US\$4,500 in 2007, up from US\$1,200 in 1980. Interestingly, the growth rate differential implied by these data is minuscule. Both countries essentially quadrupled their incomes over 25 years. The World Bank data, which do not go back further than 1980 for Barbados, thus suggest that the divergence between the two islands has been a relatively constant post-independence feature. Going further back in time, one needs to turn to Angus Maddison’s historical inflation-adjusted GDP per capita numbers. These report per capita income levels for Barbados of US\$2,123 in 1950, US\$6,537 in 1973, and US\$8,129 in 1990. For Jamaica, he reports US\$1,326 in 1950, US\$4,131 in 1973, and US\$3,609 in 1990 (Maddison 2001, 497). In combination, these data suggest that today’s almost 300 percent higher incomes in Barbados are mostly explained by the stark divergence in the 1970s.

ruling party in 1972 nationalized companies and increased tariffs and government expenditure, which resulted in high inflation rates, Barbados kept a low government deficit and managed to control inflation.

In their interpretation of the divergence, Henry and Miller (2009) take an “ahistorical” stance—that is, given how historically similar the two islands were, the authors conclude that the divergence cannot be explained by historical factors. Instead, they explain the economic divergence as resulting from differences in policy choices. Their explanation is political, centering on strong labor unions, and rising inequality that generated a demand for redistribution. All of these factors in Jamaica shaped both the policy outlook of and the electoral support for the People’s National Party (PNP), which defeated the incumbent Jamaican Labor Party (JLP) in the 1972 election. The PNP subsequently oversaw the bad policies that Henry and Miller (2009) blame for the divergence.

While these political effects were undoubtedly important, there is something odd about an explanation centered on politics that discounts altogether the historical roots of the formation of political coalitions and political fault lines.

Patterson (2014) articulated this criticism, arguing that there were indeed significant differences between the historical and institutional origins of Barbados and Jamaica. Patterson is particularly focused on state and administrative capacity. The nutshell argument (which does his nuanced analysis a grave injustice) is that in Barbados the British colonial elites were secure enough in their position in society to allow the emergence of a local administrative middle class. After independence the administrative state capacity embedded in this local middle class became the capacity of the Barbadian state and allowed its government to respond to the turmoil of the 1970s with the right policies. By contrast, pre-independence administrative capacity in Jamaica was more tightly constrained to a social layer of professional British administrators who worked for Her Majesty’s Colonial Service. As a result, the colonial administrative capacity left Jamaica with independence in 1962.

Patterson argues that this difference in the pre-independence administrative capacity in turn was driven by the sort of exogenous initial conditions surveyed in this chapter. One major condition was the availability of spare hinterlands in Jamaica. Jamaica’s hinterlands were typical of the Caribbean islands: most were volcanic and characterized by an interior that was fertile and suitable for small-holder agriculture, but unsuitable for large-scale sugar cultivation, which required flat land at low elevations. This geographic outside option allowed Jamaican freedmen to walk away from the plantation economy right after emancipation. As early as 1838,

this created a political equilibrium that pitted the freed slaves in opposition to the British plantation owners, and by extension, for the most part also against the British colonial administration. Barbados, by contrast, had no hinterlands. Its geographic exceptionalism is that it was the only British Caribbean sugar island that was made of non-volcanic limestone, meaning it was flat. As a result, while the average British Caribbean sugar island only had about 30 percent of its land under sugar cultivation on the eve of emancipation, in Barbados this figure was above 90 percent.

Dippel, Greif, and Trefler (2017) and Dippel and Carvalho (2017) exploit these differences for empirical analysis. Dippel, Greif, and Trefler conduct a panel analysis of 14 British Caribbean islands from emancipation in 1838 until 1914 and find that the geographic differences emphasized in Patterson (2014) explain the post-emancipation evolution of labor markets and coercive institutions very well. Specifically, they find that (1) the plantation economy went into decline in islands with substantial hinterlands, (2) the decline of the plantation economy was associated with substantial wage increases, (3) there were substantial decreases in the coercive application of the law, and (4) most of the wage increases can be statistically explained by drops in coercive policies. Dippel and Carvalho (2017) focus on the racial composition of Caribbean elites during the same period. They document that the local elite (members of the locally elected assemblies on the islands) became racially mixed after emancipation, and that “colored” elites were significantly more politically accountable to their voter base than white elites (because the latter usually got elected by tenants of their plantations through long-standing patronage relations). This created pressure on the existing political system, most famously associated with Jamaica’s 1865 Morant Bay Rebellion, and eventually led elites in all but one of the 10 islands under study to simply abolish their locally elected assemblies and invite the British Crown to replace them with a purely appointed legislature that would effectively make the local elites subject to more colonial authority but protect them from more local accountability.

In both studies, Barbados is an outlier. Nowhere else did the plantation system remain as entrenched and powerful in 1914 as it did there. And Barbados was the only island that never abolished its locally elected assembly. Because the right to vote was tied to land ownership and all Barbadian land was taken up by plantations, a significant black electorate never emerged in 19th century Barbados, and the old “rules of the game” remained intact.

There is a deep and bitter irony in these findings. Geographic conditions meant that freed slaves were worse off in Barbados than almost anywhere else in the 19th century British Caribbean. Their lack of options outside of

the plantation sector meant that they had the lowest wages and the least political representation. Yet, one hundred years later, Barbados' post-independence government navigated the perils of good macroeconomic policymaking better than arguably any other British colony in the Caribbean. If Patterson (2014) is right, then these facts are two sides of the same coin. The post-independence transition was smoother in Barbados precisely because its oppressive pre-independence conditions provided a form of political stability not seen on the other British Caribbean islands. Such stability would have provided incentives to landholders to share administrative capacity with plantation workers that would have latter fueled the formation of better institutions and policies during post-independence periods.

In summary, the qualitative evidence in Patterson (2014) and the quantitative evidence in Dippel, Greif, and Trefler (2017) and Dippel and Carvalho (2017) lead to a rejection of the simple “ahistorical” explanation in Henry and Miller (2009). While the later are probably correct that bad macro policies were the proximate cause of Jamaica's poorer economic performance relative to Barbados, they were likely wrong to discount the role of historical factors, because bad policies are likely to have themselves been caused by the islands' different 19th century institutional legacies.

Guyana

Guyana was one of the least developed countries in the Western Hemisphere after gaining independence from the British in 1966. Although Guyana's per capita income (GDP per capita, purchasing power parity, constant 2011 international dollars) has increased by more than 2.5 times since 1990, averaging US\$6,255 over 2007–2016. Such levels are less than half of the average for Latin America and the Caribbean over the same period. Guyana today can be characterized as a small, ethnically diverse, open, commodity-based, economy. Its population is only 747,000 persons: 39 percent of the population is of East Indian origin, 27 percent African, 24 percent multiracial, and 10 percent Indigenous (Amerindian).⁴

Politics and political parties in Guyana are a reflection of the country's ethnic diversity. Guyana's exports are concentrated in agriculture and extractive industries—specifically, gold and bauxite—and 71 percent of the export basket consists of gold, rice, timber, and sugar. These characteristics, both individually and in their interactions, underlie the manifestations of the country's development challenges.

⁴ Source: 2017 Guyana Labor Force Survey.

Guyana was first colonized by Dutch settlers in the 1600s. Sugar was the first crop produced, starting in 1658, but it was not until the late 1700s that its production took place on a large scale. There were an estimated 380 sugar estates along the coast of Guyana by 1800, and sugar remained one of its most valuable products for the next two centuries. The British took over the colony in 1814, just 20 years prior to the abolition of slavery, but it fell into turmoil after 1833 as the *Act for the Abolition of Slavery* in British Colonies was passed by Britain. Upon emancipation in 1838, the former African slaves abandoned the plantations and migrated to urban areas, after which mainly indentured East Indians were brought to work on the plantations until indentured labor was abolished in 1917.

Political independence was achieved in 1966, but this did not imply economic independence because most of the country's agricultural and mining enterprises were owned by foreign companies. The government saw this as an obstacle to economic development and began a process of nationalizing major companies operating in Guyana during the 1970s and early 1980s. By the late 1970s, almost 80 percent of Guyana's economy was controlled by the government and by the early 1980s the government had also taken control of most of the retailing and distribution systems. There was tight regulation on currency exchange and the government also controlled prices and placed restrictions on a wide range of consumer imports. The prices of both sugar and bauxite rose in the early 1970s, which favored the newly nationalized enterprises, but this was a short-lived boom. By the late 1970s to early 1980s commodity prices declined, triggering a drastic decline in economic output and significant macroeconomic challenges for the government.

These challenges worsened in the 1980s because of a lack of competent local expertise to manage the large agricultural and mining enterprises and a lack of private investment. At the time of independence, administrative capacity in Guyana was constrained by shortages of professional and skilled labor. The country was in a state of political and social instability characterized by ethnic violence, a breakdown in the rule of law, generally weak institutions and little consensus on economic policy. This period was associated with a high level of emigration of qualified individuals, a phenomenon which continued for decades after independence and impacted the performance of key institutions (DaCosta 2007). In 1988, Guyana's external debt was estimated to be six times its official GDP. A free market economy paradigm under an economic reform program with guidance from the International Monetary Fund was started in 1985, and by 1990 the 20-year experiment with a government-controlled economy was coming to an end. As Guyana transitions to a hydrocarbon-dependent economy

within the next decade, the quality and performance of key institutions are highly relevant for its long-run development.

Suriname

Suriname is perhaps the most unique among the set of Caribbean countries covered in this book. Although richly endowed with natural resources and ethnically diverse like Guyana and Trinidad and Tobago, it is a former Dutch colony with a somewhat colorful post-independence experience. Its official language is Dutch. Unlike in Guyana and Trinidad and Tobago, there is no single majority ethnic group. Suriname is also the youngest independent country in the Caribbean. The country was marred by political instability during the first two decades after attaining independence. Between 1975 and 1980, Suriname had a working parliamentary democracy. However, in February 1980 the elected government was overthrown by a military coup d'état. The military dictatorship dominated Suriname until 1991 and included alleged political assassinations in 1982, a ban on political parties in 1985, and a civil war that began in 1986. A new civilian constitution was approved by referendum in 1987 and a president subsequently elected. However, this first return to civilian government was short-lived, as military rule resumed when another military coup took place in 1990. The civil war ended, and a new government was elected in 1991 under the 1987 constitution, marking a return to civilian rule that has held since.

Politics and political parties are strongly influenced by Suriname's ethnic diversity, a legacy of its colonial past. The mobilization of political parties, which intensified during the period from 1942 to 1948 and occurred along ethnic lines, was motivated by the promise of full internal self-government in the early 1940s and around the attainment of universal suffrage (Dew 1996). Suriname's first political party, the Moslem Party, was formed in 1946. A number of political organizations subsequently emerged representing various ethnic and religious groups: the Catholics established the Progressive Surinamese Party (PSV), the creoles supported the National Party of Suriname (NPS), the Javanese mainly supported the Party for National Unity, and the Hindustanis predominantly supported the Progressive Reform Party (VHP). Many other small parties emerged in the post-independence period, with most of them forming coalitions and alliances to better their chances of getting into parliament.

A combination of factors—including mineral dependence, ethnic-based politics, and social and political instability in the early independence

era—may have diverted emphasis away from the development of quality institutions to support sustainable economic growth and development.⁵ Suriname’s average growth rate from its independence from the Netherlands in 1975 until 2015 was 1.6 percent. This was significantly lower, by almost half, than the average growth rate of 3 percent in other countries in Latin America and the Caribbean. Suriname also experienced two bouts of hyperinflation in the 1990s and plunged into a deep recession after the 2015 commodity price shock. In the literature, Suriname’s meager economic growth has been largely explained by a combination of external and domestic factors, including volatility in commodity prices, fluctuating Dutch aid flows, issues related to macroeconomic management, events that affected political stability, the “resource curse” (Dutch disease), and other binding constraints to growth (Elias 2014; Mungroo, Ooft, and Tjon Kie Sim-Balker 2014; Fritz-Krockow et al. 2009; van Dijk 2001). Although the country’s natural resource endowment (including bauxite, gold, oil, timber, and fertile land) did play a significant role in stimulating short growth spurts (Mungroo, Ooft, and Tjon Kie Sim-Balker 2014; van Dijk 2001), it has not led to sustainable growth and has not evolved into better social and development outcomes.

Trinidad and Tobago

On an income per capita basis, Trinidad and Tobago is one of the richest economies in the Western Hemisphere. Its per capita income (GDP per capita, purchasing power parity, constant 2011 international dollars) was estimated to average US\$31,131.46 over 2007–2016, which was more than two times larger than the average for Latin America and the Caribbean. The country’s wealth is largely attributed to its natural resource endowments: the petroleum sector (oil, gas, and petrochemicals) accounted for 42 percent of GDP in 2014. However, Trinidad and Tobago was not always a hydrocarbon-dependent economy. During the pre-independence period, agriculture (mainly sugar, coffee, cocoa, and cotton) were the country’s main economic activities.

Trinidad and Tobago’s pattern of development changed as its economy transitioned from one based on agriculture to one based on oil and gas. The first sugar plantation in Trinidad was established in 1787, and with that, agriculture expanded in the following decade with 159 sugar

⁵ Some studies have shown that political instability and civil wars can affect the development of quality institutions and disrupt the accumulation of human and physical capital (Compton, Giedeman, and Johnson 2006; Bellows and Miguel 2006).

plantations, 130 coffee estates, 60 cacao estates, and 103 cotton estates (Senauth 2010). In the 1800s, by which time the British had captured the island from the French planters, its sugar plantations were larger than in other Commonwealth Caribbean islands. The discovery of oil changed the country's pattern of economic development. The first oil well was drilled in 1857 and commercial production began in 1908. Exports of crude oil started in 1909 and were boosted during World War I as Trinidad and Tobago became a major source of oil for the British Royal Navy. Oil output increased from 125,000 barrels annually in 1910 to over 2 million barrels by 1920. Oil has remained an important part of economic development, with its boom-and-bust cycle manifesting itself in the country's economic performance, up until today. Some changes have occurred within the petroleum sector as Trinidad and Tobago developed capacity across the spectrum of the energy value chain with activities in the upstream, mid-stream, and downstream. Trinidad and Tobago also established one of the largest natural gas processing facilities in the Western Hemisphere during the mid-to-late 1990s, according to the country's Ministry of Energy of Finance.⁶ As a result, the country has transitioned into a largely gas-based economy. However, as with many resource-rich developing countries, Trinidad and Tobago exhibits symptoms of Dutch disease and, as argued by some economists, has fallen victim to the "resource curse" (Khadan 2016; Khadan and Ruprah 2016; Sinanan and Hosein 2010). The main challenge it faces going forward is addressing long-standing structural constraints and economic diversification (Khadan 2017).

With respect to social development, the country made significant progress in improving access to important social services in education, health, social security, and infrastructure. However, the performance indicators from these sectors are below expectations (Khadan 2016). Politics and political parties are very much influenced by the country's ethnic diversity. Unlike Suriname, there are only two major ethnic groups in Trinidad and Tobago, each represented by a political party: 35 percent of the population is of African origin, 34 percent East Indian, and 15 percent mixed (African and East Indians). Ethnic tensions for the most part appear more prevalent during periods of national and local elections. Unlike the experiences of Suriname and Guyana, Trinidad and Tobago has generally had peaceful transitions of governments in the post-independence era, with the exception being an attempted coup in 1990.

⁶ See <http://www.energy.gov.tt/historical-facts-petroleum/>.

6.3. Colonization, Political Institutions, and Policymaking in the Contemporary Caribbean

A large body of research thus suggests that the Caribbean's legacy of plantation agriculture and ethnic divisions could manifest itself in its present-day institutions and political processes. These in turn matter for economic development because institutions—particularly political institutions—shape economic policies, and policies matter for economic growth and development (Persson 2002). Institutions, especially political institutions, represent the central mechanism for decision-making in democratic systems, and play a major role in informing economic policies (Stein and Tommasi 2007; Persson 2002; Persson and Tabellini 2003, 2004; Rodrik 1996). Thus, it is important to ask: What are the important features for good policymaking and how does the Caribbean stack up against other countries?

In attempting to answer this question, this section follows Tommasi (2006), who identified several key features of public policy, including stability, adaptability, policy efficiency, public-regardedness of policies, and implementation and enforcement. This section briefly examines each aspect and evaluates how Caribbean countries stack up against selected benchmarks.

6.3.1. *Features of Public Policy*

Following Tommasi (2006), Berkman et al. (2008) constructed five indices to evaluate key features of public policy: stability, adaptability, efficiency, public-regardedness, and implementation and enforcement.⁷ Each index is constructed from several variables derived from various international datasets. This section briefly explains the subcomponents of each index.

- **Policy Stability Index:** This index measures the extent to which policies are stable over time. It is more desirable to have stable policies with incremental changes that build on the achievements of previous political administrations. Stable policy environments also tend to reflect strong consultations and engagement with stakeholders in society. The stability index in Berkman et al. (2008) is constructed using four variables: the Fraser Index of Economic Freedom; two variables from the World Economic Forum's Global

⁷ They also constructed a sixth index for policy coherence, but there are no data on this index for any of the countries considered here.

Competitiveness Report (one measures the extent to which legal or political changes influence the planning activities of firms, and the other measures whether contractual commitments and obligations are honored despite changes in political regimes); and a variable taken from the Institutional Profiles Database that measures the level of consistency and continuity of government action in economic matters

- **Policy Adaptability Index:** Policy adaptability considers whether countries can adapt policies in response to changing economic conditions and international learning about best practices. If policy adaptability is low, countries may not be able to respond to shocks adequately or may be trapped with undesirable policies for extended periods of time. The Policy Adaptability Index is constructed using four variables: the Bertelsmann Transformation Index; two variables from the Columbia University State Capacity Survey (one provides information based on expert ratings about effectiveness in responding to domestic economic problems, and the other measures the ability of the state to develop and implement national policy initiatives); and a variable taken from the Institutional Profiles Database, employers, and experts' evaluations on the decision-making capacity of the political authorities in economic matters.
- **Policy Efficiency Index:** Policy efficiency measures the ability of the state to allocate scarce resources to activities that yield the greatest returns. This index is constructed using expert evaluations of the composition of public spending and whether it is wasteful, whether the government makes optimal use of available resources (economic and human), and how effective the political system is in developing and executing policy. The three variables are taken from the Global Competitiveness Report, the Bertelsmann Transformation Index, and the Economic Intelligence Unit, respectively.
- **Public-Regardedness Index:** Public-regardedness measures the extent to which the policies pursued are in the public interest, or whether they tend to be directed toward special interest groups and members of the elite who have the resources and networks to influence policy decisions in their favor. Public-regardedness is constructed using expert evaluations and perceptions on issues related to corruption, public spending on social transfers, and whether government contracts are awarded fairly or generally favor well-connected firms and individuals. The first variable was taken from Transparency International Corruption's Perceptions Index, and the last two from the Global Competitiveness Report, respectively.

- **Implementation and Enforcement Index:** Policy implementation and enforcement accounts for how well countries can implement and enforce policies once they are approved, which can reflect how well the judiciary and other arms of the state work. The index is constructed using expert evaluations and ratings on six topics: (1) the degree to which the legally established minimum wage is enforced, (2) the prevalence of tax evasion, (3) the degree to which environmental regulations are enforced, (4) whether reform policies are effectively implemented by the government, (5) whether the state can develop and implement national policy initiatives, and (6) the effectiveness of tax collection. These variables are mainly sourced from the Global Competitiveness Report, the Bertelsmann Transformation Index, and the Columbia University State Capacity Survey.⁸

The five indexes discussed above were then used to construct an Overall Policy Index for the quality of public policies. The Overall Policy Index was constructed by applying equal weights to each of the key features of public policies and using a simple average over the five policy characteristics (Berkman et al. 2008).

Similar to Franco and Scartascini (2014), countries are classified here into three clusters (high, medium, or low) and ranked from high to low within each cluster. Values in the high cluster range from 4 to 2.5, values in the medium cluster range from less than 2.5 to 1.5, and values in the low cluster range less than 1.5 to zero. Table 6.5 shows these clusters, evidencing that Caribbean countries fall into different clusters. The Bahamas and Barbados fall into the high cluster, a group which represents better institutional quality. This group also includes most member countries of the Organisation for Economic Co-operation and Development (OECD). Remarkably, The Bahamas and Barbados place higher than the OECD average. The medium cluster includes Trinidad and Tobago, Jamaica, and Guyana. Only Suriname falls into the low cluster. From these observations, the worst outcome appears to be associated with being an ethnically diverse country, a non-British colony, a country colonized

⁸ The sixth index considered in Tommasi (2006) for the coordination and coherence of public policies measures the extent to which different agents operating in the same policy domain work together to formulate coherent public policies. It is constructed using two variables, one from Columbia University's State Capacity Survey, which rates the effectiveness of coordination between central and local government agencies, and another from the Institutional Profiles Database, which measures the level of coordination between government ministries and within a government administration.

Table 6.5 Cluster Analysis of Overall Policy Index

High	Medium	Low
Singapore	Fiji	Kenya
Finland	Seychelles	Argentina
Denmark	United Arab Emirates	Suriname
Luxembourg	Portugal	Pakistan
St. Lucia	Malaysia	Solomon Islands
The Bahamas	Bahrain	Maldives
Netherlands	South Africa	Tonga
New Zealand	Cabo Verde	Guinea-Bissau
Norway	Namibia	Bolivia
Switzerland	Costa Rica	Malawi
United Kingdom	Bhutan	Papua New Guinea
Sweden	Latvia	Comoros
Barbados	Caribbean	Nicaragua
Canada	ROSE	Bangladesh
Iceland	Brazil	Sierra Leone
Germany	Lesotho	Ecuador
Australia	Samoa	Swaziland
St. Vincent and the Grenadines	Greece	Guatemala
Brunei Darussalam	Ex-British	Venezuela
Ireland	Italy	Nigeria
United States	Kuwait	Equatorial Guinea
Chile	India	Paraguay
Qatar	Uganda	Sudan
OECD	Mexico	Yemen, Rep.
Cyprus	Trinidad and Tobago	Myanmar
Spain	Turkey	Afghanistan
Austria	Ghana	Zimbabwe
Japan	Gambia, The	Haiti
Slovenia	Macedonia, FYR	
France	United Republic of Tanzania	
Montenegro	Colombia	
Dominica	El Salvador	
Estonia	Sri Lanka	
Malta	Jamaica	
Uruguay	Grenada	
Korea, Rep.	Peru	
Botswana	Guyana	
Belgium	Latin America	

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Table 6.5 Cluster Analysis of Overall Policy Index (continued)

High	Medium	Low
Belize	Panama	
Mauritius	Zambia	
	Vanuatu	
	Dominican Republic	
	Kiribati	
	Djibouti	
	Gabon	
	São Tomé and Príncipe	

Source: Authors' estimates based on Berkman et al. (2008).

Notes: Data for three of the five subindices for The Bahamas and Suriname are not available. For Suriname, information is not available for stability, adaptability, and implementation and enforcement, and for The Bahamas information is not available for adaptability, efficiency, and implementation and enforcement. Trinidad and Tobago is also missing data for adaptability.

through extractive institutions, and a country with an economic structure that is presently commodity-dependent. The best outcomes are observed in The Bahamas, which was a British colony, was not extractive, is not ethnically diverse, and is not commodity-dependent.

We now turn to look at the disaggregated five components of the Overall Policy Index: stability, adaptability, efficiency, public-regardedness, and implementation and enforcement. Table 6.6 evidences that there are clear differences showing that some Caribbean countries perform better than others in the features of public policy. Caribbean countries appear to perform best when it comes to policy stability, where most countries are in the high cluster. For policy adaptability, information is only available for Jamaica and Guyana. The former is in the medium cluster while the latter is in the low cluster. In terms of policy efficiency, Barbados is in the high-efficiency cluster, followed by Suriname and Trinidad and Tobago in the medium cluster, and Guyana and Jamaica in the low cluster. Caribbean countries do particularly poorly on the public-regardedness dimension, where most appear in the low cluster, except for Barbados and The Bahamas. With respect to policy implementation and enforcement, all three countries for which data are available are in the medium cluster.

With respect to the benchmarks, the OECD average is in the high cluster for all dimensions of public policy except for efficiency. Notably, Barbados performs better than the OECD average. The average for ex-British colonies falls in the medium cluster for all dimensions, and the Latin American average is also in the medium cluster for three of the five dimensions and low for public-regardedness and efficiency.

6.3.2. State Capture

The findings in Table 6.6, particularly for the Public-Regardedness Index, indicate that in most Caribbean countries institutions that shape economic policy do not necessarily do so in the public interest and instead favor special interest groups or members of the elite. This entails unproductive rent-seeking by bureaucrats and government officials. Formally, state capture is defined as the efforts of firms or such groups as the military, ethnic groups, or kleptocratic politicians to shape the laws, policies, and regulations of the state to their own advantage by providing illicit private gains to public officials (Sebake 2017). Ruprah and Sierra (2016, 1) note that “small and politically stable societies like those in the Caribbean foster the development and institutionalization of growth-retarding special interest groups, which are then better able to influence policy to redistribute resources in their favor.” This line of reasoning is also consistent with Dookeran’s (2012) assertion that one of the key factors of policy failure in the Caribbean is the presence of “anti-growth coalitions” in the form of extractive elites.

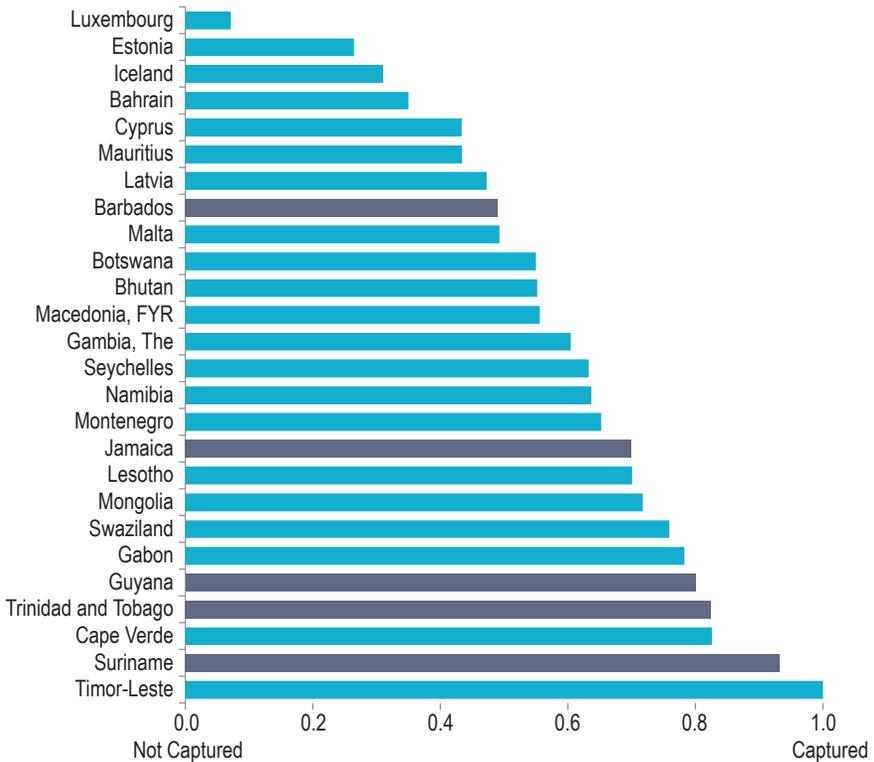
To further examine the extent of state capture, and as a robustness check on the public regardedness feature of public policy in Table 6.6, we construct a State Capture Index from expert opinion surveys. The index is constructed by taking the average from three pillars of the World Economic

Table 6.6 Key Features of Public Policy

	Stability	Adaptability	Efficiency	Public Regardedness	Implementation and Enforcement	Overall Policy Index
Ex-British Colonies	Medium	Medium	Medium	Medium	Medium	Medium
OECD	High	High	Medium	High	High	High
ROSE	High	Medium	Medium	Medium	Medium	Medium
Latin America	Medium	Medium	Low	Low	Medium	Low
The Bahamas	High	n.a.	n.a.	High	n.a.	High
Barbados	High	n.a.	High	High	n.a.	High
Guyana	High	Low	Low	Low	Medium	Medium
Jamaica	Medium	Medium	Low	Low	Medium	Medium
Suriname	n.a.	n.a.	Medium	Low	n.a.	Low
Trinidad and Tobago	High	n.a.	Medium	Low	Medium	Medium

Source: Authors’ estimates based on Berkman et al. (2008).

Note: n.a. = not available.

Figure 6.1 State Capture Index

Source: World Economic Forum, Global Competitiveness Index.

Forum's Global Competitiveness Index: Pillar 1 (Institutions), Pillar 6 (Goods Market Efficiency), and Pillar 7 (Labor Market Efficiency).⁹ From each country's average, we subtracted the minimum value (within small economies) and then this result was divided by the difference between the maximum and minimum values (Ruprah and Sierra 2016). The resulting index ranges from zero (no capture) to unity (full capture). The State Capture Index in Figure 6.1 shows that Suriname, Trinidad and Tobago, and Guyana are on the higher end of the index. As summarized in Table 6.4, these three countries' shared characteristics are that they are ethnically diverse, had extractive colonial institutions, and have a current economic structure that is commodity-dependent.

⁹ The Bahamas is not included in this exercise as it is not covered in the Global Competitiveness Index.

6.3.3. *State Capabilities in the Caribbean*

The previous section examined features of good policymaking. This section now turns to exploring some of the characteristics of key actors and institutions involved in the policymaking process (Stein and Tommasi 2007). Berkman et al. (2008) constructed an overall index of government capabilities derived from four subindices measuring (1) the policymaking capabilities of the congress, (2) the institutionalization of the party system, (3) judicial independence, and (4) bureaucratic quality. Each index is briefly described below.¹⁰

- **Congress Capabilities Index:** This index measures the extent to which congress has the capability to undertake discussion, negotiation, and enforcement of political agreements and the development of consistent policies over time.
- **Party system institutionalization:** Party system institutionalization accounts for the role that political parties have in the policymaking process. Greater institutionalization of political parties can encourage long-horizon commitments and facilitate intertemporal bargains both within the party and among parties.
- **Judicial independence:** This measure emphasizes the role of an independent judiciary in facilitating the intertemporal enforcement of prior political and policy decisions according to constitutions and laws that can improve the stability and quality of enforcement in the policymaking process.
- **Bureaucracy Index:** Civil service capabilities or bureaucracy emphasizes the importance of bureaucracies in the quality of implementation of public policies, as these capabilities promote less political opportunism and allow for investing resources into developing third parties that can limit the bureaucracy's discretion and enforce long-term commitments.

We use a similar approach as before to classify countries into three clusters (high, medium, or low) and rank them within each cluster. Again, Table 6.7 shows that Caribbean countries fall into different clusters. Barbados is the only Caribbean country in the high cluster, a group that represents better government capabilities. The medium cluster includes three Caribbean countries—The Bahamas, Jamaica, and Trinidad and

¹⁰ For more details on the construction of each index, see Franco and Scartascini (2014).

Table 6.7 Government Capabilities Index

High	Medium	Low
Luxembourg	St. Lucia	Guyana
Denmark	India	Dominican Republic
Norway	South Africa	Gambia, The
Barbados	Estonia	Guinea-Bissau
United Kingdom	Cyprus	Macedonia, FYR
Finland	Namibia	Bhutan
Iceland	Jamaica	Latin America
Singapore	Costa Rica	Suriname
Ireland	Chile	Swaziland
Canada	France	Peru
Malta	Ghana	Gabon
Australia	The Bahamas	Argentina
New Zealand	Spain	Vanuatu
Switzerland	Korea, Rep.	Panama
United States	Montenegro	El Salvador
Sweden	Portugal	Samoa
Austria	Uruguay	Bolivia
Mauritius	Malaysia	Grenada
Germany	Cabo Verde	Ecuador
Netherlands	Caribbean	Djibouti
Botswana	United Republic of Tanzania	Paraguay
OECD	Turkey	Equatorial Guinea
Brunei Darussalam	Sri Lanka	Nicaragua
Japan	Fiji	Solomon Islands
Belgium	Uganda	Guatemala
Slovenia	Latvia	Venezuela
	Bangladesh	Comoros
	Ex-British	Maldives
	Lesotho	Haiti
	Bahrain	
	ROSE	
	Greece	
	Belize	
	Malawi	
	Seychelles	
	Papua New Guinea	
	Brazil	
	Kuwait	

(continued on next page)

Table 6.7 Government Capabilities Index (continued)

High	Medium	Low
	Colombia	
	Trinidad and Tobago	
	United Arab Emirates	
	Mexico	

Source: Authors' estimates based on Berkman et al. (2008).

Tobago—including the average for ex-British colonies and small economies in the rest of the world. Guyana and Suriname appear in the low cluster with the Latin American average. Again, a similar pattern emerges: the worst outcome appears to be associated with being an ethnically diverse country, colonized through extractive institutions, and with a current economic structure that is commodity-dependent.¹¹

As shown in Table 6.8, there are clear differences suggesting that some Caribbean countries perform better than others in government capabilities. Guyana and Suriname are in the low cluster for three out of four pillars, while Trinidad and Tobago is in the low cluster for two. The Bahamas, Barbados, and Jamaica, where data are available, perform better, as they are in the medium and high clusters (a group that encompasses the average of OECD countries). Notably, Barbados performs better than the OECD average for congress capabilities. However, precisely the area where more than half of the Caribbean countries underperform is congress capabilities, followed by party institutionalization and bureaucracy. Guyana is the only Caribbean country in the low cluster for judicial independence.

Again, the patterns shown in Table 6.8 are suggestive that Caribbean countries showing politically polarized ethnic diversity, that were colonized with extractive purposes, and with a current commodity-dependent economy underperform in terms of contemporaneous government capabilities. These descriptive patterns are consistent with the features suggested by the literature examining the link between colonialism and contemporaneous institutional quality.

¹¹ As stated at the beginning of this chapter, no causal claims of the documented descriptive patterns are made. Several other proximate factors within each country, besides the historical characteristics highlighted in the literature, could have influenced present institutional outcomes. For example, the poor government capabilities observed in Guyana and Suriname could have been also influenced by, for example, the military coup in Suriname in the 1970s and the 1970s–1980s political regime in Guyana.

Table 6.8 Key Features of Government Capabilities

	Congress Capabilities Index	Party System Institutionalization	Judicial Independence	Bureaucracy Index	Overall Government Capabilities Index
Ex-British Colonies	Medium	Low	Medium	Medium	Medium
OECD	Medium	Medium	High	High	High
ROSE	Medium	Low	Medium	Medium	Medium
Latin America	Low	Medium	Medium	Low	Low
The Bahamas	n.a.	Medium	n.a.	High	Medium
Barbados	High	Medium	High	n.a.	High
Guyana	Low	Medium	Low	Low	Low
Jamaica	Medium	Medium	High	Medium	Medium
Suriname	Low	Low	Medium	Low	Low
Trinidad and Tobago	Low	Low	Medium	Medium	Medium

Source: Authors' estimates based on Berkman et al. (2008).

6.4. Conclusions

This chapter surveyed the literature evidencing the link between colonization and contemporary institutions with the aim of identifying relevant patterns for the Caribbean experience. It then reviewed the colonization experiences of each Caribbean country identifying which of the historical factors that the literature considers to be important for long-run institutional development were present. The chapter then explored whether what exists today in the Caribbean in terms of policymaking and government capabilities matches the historical dependence patterns identified by the literature.

Three main characteristics associated with the colonization experience of Caribbean countries were identified: different colonizers, the types of colonial institutions established, and the varying historical approaches to securing labor inputs. Of the six countries studied, five were ex-British colonies (The Bahamas, Barbados, Guyana, Jamaica, and Trinidad and Tobago) and one an ex-Dutch colony (Suriname). All ex-British colonies, except for The Bahamas, had been plantation-type colonies that produced mainly sugar and other primary goods. The varying historical approaches to securing labor inputs for the colonies in the Caribbean resulted in different degrees of ethnic fragmentation across the former colonies. Two major ethnic groups (East Indians and Africans) emerged in Guyana and Trinidad

and Tobago, while Suriname is more diverse, with five such groups (East Indian, Creole, Maroons, Javanese, and Chinese), as well as the original inhabitants of Suriname. African descendants form the clear majority in The Bahamas, Barbados, and Jamaica.

The chapter found that with respect to the features of “good” policymaking, the worst outcomes appear to be associated with ethnic diversity, being a non-ex-British colony, and having been colonized through extractive institutions. The best outcomes are observed for The Bahamas, which was an ex-British colony, was not extractive, and is not ethnically diverse. Similar evidence was observed for measures of government capabilities. Most Caribbean countries do particularly poorly in one of the features of policymaking—the public-regardedness dimension, which measures the extent to which policies pursued are in the public interest or whether they tend to be directed to special interest groups. This observation was reinforced, particularly for Guyana, Suriname, and Trinidad and Tobago, by the assessment in this chapter of the varying degrees of the State Capture Index across Caribbean countries. Thus, consistent with the literature, the chapter found that countries colonized through extractive institutions, that are ethnically diverse, and (in the case of Suriname) were not colonized by the British, appear to do relatively worse in present times in most features of “good” policymaking and government capabilities. Next, Chapter 7 explores whether contemporaneous trust levels in political, rule of law and human capital development institutions are also aligned with these patterns.

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Trust and Institutions in Caribbean Countries

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Having presented evidence in previous chapters that institutions matter for economic and social development worldwide, this chapter explores citizens' perceptions in terms of trust in institutions and their performance within Caribbean countries. The focus on trust follows from consistent evidence showing that trust among citizens and in the norms governing their interactions fosters economic development; that is, the legitimacy of institutions among members of a society is an important ingredient in the way in which institutions matter for development. For example, investment and saving decisions are incentivized when agents trust that the institutional setting or defined property rights provide assurance that neither governments nor other agents will expropriate those investments or savings. As such, greater trust in the strength and consistency of institutions governing the relationships among private agents and with the state incentivizes the accumulation of physical and human capital, the contribution to public goods, the development of markets, and the diffusion of technologies, which in turn increases total factor productivity and fosters growth. The relevance of trust for prosperity takes special interest given that, as evidenced in Chapter 4, contemporary trust levels appear to be persistent over time and having historical origins. As such, increasing trust in the present might not be straightforward and most probably would require a relatively long-term horizon.¹

Literature exploring the link between generalized trust, institutions, and development identifies trust as a key feature for prosperity that manifests in a society's culture or social capital. In the literature supporting this view, higher trust among citizens is associated with positive impacts

¹ See Nunn and Wantchekon (2011) for evidence on how the slave trade in West Africa four centuries ago had a long-term negative impact on present days individual-level trust.

on investment and growth (Knack and Keefer 1997).² In addition, higher levels of trust among members of society have also been associated with increased government efficiency. Indeed, La Porta et al. (1997) documented that increased trust among citizens improves judicial efficiency, bureaucratic quality, and tax compliance, while also reducing the incidence of corruption.³ Trust among citizens can also affect preferences for redistributive policies as the success of public education, for example, also depends on the amount of family inputs into the education process. Therefore, if citizens do not trust that public education beneficiaries will exert such household level complementary efforts, support for education spending might decline (Keefer 2018). In general, if people believe that redistributive benefits will accrue to ineligible citizens, support for such policies will be low. Public trust also facilitates the emergence of collective action by citizens in the form of civil society organizations that are needed to ensure the provision of public goods and limit the incursion of private interests into public policy (Keefer 2018). At the firm level, evidence suggests that trust within firms incentivizes decentralized management decisions, which in turn increases productivity (Bloom, Sadun, and Van Reenen 2012).⁴ Therefore, measures of trust captured through citizens' perceptions have been shown to be positively related with productivity, government efficiency, preferences for redistributive policies, collective action and growth. As such, while qualitative in nature, citizens' perceptions matter for investment decisions and economic activity.⁵

² Specifically, trust was measured using the 1990–1991 World Values Survey data, which cover 29 countries. The trust indicator is the percentage of persons who responded, “most people can be trusted” to the following question: “Generally speaking, would you say that most people can be trusted, or that you can’t be too careful in dealing with people?” The authors find that that an increase equivalent to one standard deviation in this trust measure among citizens within a country is associated with positive impacts on growth and investment of 1.15 percent and 2.04 percent, respectively.

³ They also measure trust using the 1990–1991 World Values Survey data (see footnote 1). The authors find that a one standard deviation increase in trust raises the judicial efficiency score by 0.7, the anticorruption score by 0.3, bureaucratic quality by 0.3, and tax compliance by 0.3 of a standard deviation.

⁴ The authors use data from 66 countries surveyed between 1981 and 2004 in the World Values Survey. The trust measure is also the percentage of persons who responded, “most people can be trusted” to the following question: “Generally speaking, would you say that most people can be trusted, or that you can’t be too careful in dealing with people?”

⁵ We also acknowledge that public perceptions, while having real economic and political effects, could deviate from reality. However, they tend to provide a valid reference or proxy statistic to characterize the cross-sectional differences across different regions or countries as we do in this chapter.

This chapter analyses the trust and perceptions of Caribbean citizens regarding three key types of institutions: political institutions, the rule of law, and institutions related to human capital development. It is worth noting that institutions in charge of regulating and fostering economic activity are not examined in this chapter. This is because such institutions undertake technical roles that are not easily captured in public perceptions. However, a formal analysis of such institutions is provided within a regional perspective in Chapter 8 and within individual countries from Chapter 9 onward.

This chapter relies on alternative global datasets capturing perceptions of citizens from several countries.⁶ Throughout the chapter, benchmark analyses are presented that place the perceptions of Caribbean citizens within an international perspective. In doing so, we recognize the heterogeneity of Caribbean countries in terms of their economic structure. Following Ruprah, Sierra, and Melgarejo (2014), we distinguish between Caribbean commodity-based economies (CCB-C) and non-commodity-based economies (CCB-NC). CCB-C includes Guyana, Suriname, and Trinidad and Tobago, where more than 50 percent of exports are explained by each country's two main commodities.⁷ CCB-NC includes The Bahamas, Barbados (where the total contribution of tourism to gross domestic product [GDP] is above 50 percent), and Jamaica (where the total contribution of tourism to GDP is about 30 percent). To gain a sense of the relative status of citizens' perceptions in Caribbean country institutions, alternative benchmarks are considered. First, recognizing that country size is relevant for economic and social development, comparable states denominated as the rest of the small economies (ROSE) of the world are considered.⁸ Second, given its geographical proximity, the Latin America region is also included.⁹

⁶ The datasets include the (i) WEF 2017–2018 Global Competitiveness Index; (ii) Latin-American Public Opinion Project (LAPOP) Surveys; (iii) Eurobarometer Surveys; (iv) Transparency International's 2016 Corruption Perception Index; and (v) 2016 World Justice Project database.

⁷ For Guyana these commodities are gold and rice. For Suriname they are gold and aluminum oxide, and for Trinidad and Tobago they are petroleum gases and oil.

⁸ The ROSE group corresponds to countries with populations of less than 3 million. However, to achieve greater similarity with CCB countries, we also exclude some outliers in terms of income. Specifically, we exclude countries with GDP per capita levels above the CCB countries range. These excluded countries from the ROSE group are: Bahrain, Brunei Darussalam, Iceland, Luxembourg, and Malta. We also exclude OECD member countries from the ROSE such as Estonia, Latvia, and Slovenia. Therefore, countries considered in the ROSE group are: Bhutan, Botswana, Cyprus, Gabon, Lesotho, Macedonia, Mauritius, Mongolia, Montenegro, Seychelles, and Timor-Leste.

⁹ Countries included in the Latin America group are Argentina, Bolivia, Brazil, Chile, Colombia, Costa Rica, Dominican Republic, Ecuador, El Salvador, Guatemala, Honduras, Mexico, Nicaragua, Panama, Paraguay, Peru, Uruguay, and Venezuela.

Third, the chapter considers the group of advanced economies that are members of the Organisation for Economic Co-operation and Development (OECD) as a best-practice benchmark.¹⁰

Throughout the chapter, we present citizens' perceptions captured in different public opinion surveys worldwide related to the trustworthiness of the different institutions considered. The analyses consider OECD countries as the highest benchmark and all measures have a value of 100 for this group of countries. Specifically, each item analyzed within this chapter normalizes the answers given to individual survey questions so that measures range from 0 to 100, where the OECD group has a value of 100. As such, each indicator has been calculated so that a higher value denotes favorable measures. Therefore, values for all country groups within each indicator are interpreted as their relative position with respect to the OECD group and how far they are from achieving OECD standards.¹¹ Appendix 1 provides the details on all sources of information and specific questions from the public opinion surveys that have been used for this chapter.

The next section assesses citizens' views with respect to the actors who operate within the political system.

7.1. Political Institutions

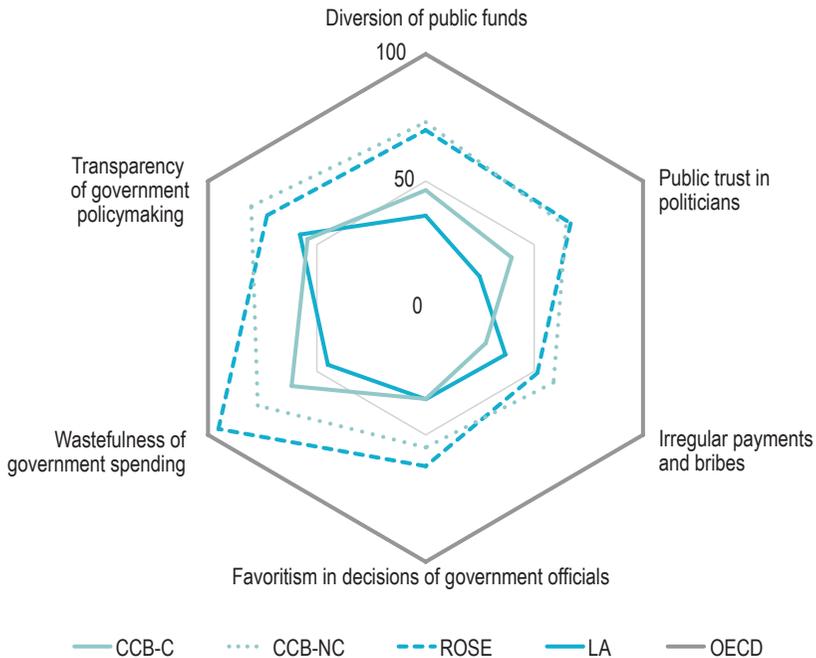
It has been suggested that the existence of inclusive and trustworthy political institutions characterized by an open pluralistic system with competition for political office, a widespread electorate, and openness to new political leaders conforms to the foundations for developing appropriate economic institutions, which in turn foster sustainable growth (Acemoglu and Robinson 2012). Therefore, this section first assesses how actors that operate in the realm of political institutions are perceived by citizens in the Caribbean in terms of trustworthiness, corruption, and openness.

¹⁰ The countries included in the OECD group are Australia, Austria, Belgium, Canada, Czech Republic, Denmark, Estonia, Finland, France, Germany, Greece, Hungary, Iceland, Ireland, Israel, Italy, Japan Republic of Korea, Latvia, Luxemburg, Netherlands, New Zealand, Norway, Poland, Portugal, Slovak Republic, Slovenia, Spain, Sweden, Switzerland, Turkey, United Kingdom, and United States. Notice that although Chile, Colombia and Mexico belong to the OECD, we do not consider them in the OECD group for the analyses as they are already included in Latin America.

¹¹ However, it is worth noting that while we present comparisons between CCB and other country groups, such comparisons are aimed to provide a descriptive analysis of relative trust levels but do not imply causality. Establishing causal inferences across country groups would need exogenous variation at the country level which does not exist within this context as institutional development, economic growth and trust are endogenously determined by multiple unobserved factors.

Figure 7.1 displays measures from the World Economic Forum's (WEF) 2017–2018 Global Competitiveness Index database regarding citizen perceptions of politicians and public servants. These measures include perceptions about diversion of public funds to private agents, the level of

Figure 7.1 Citizens' Perceptions of Trustworthiness of Politicians and Public Servants



Sources: World Economic Forum (WEF), 2017–2018 Global Competitiveness Index for index component 1 and calculations by the authors.

Notes: Diversion of public funds is based on the question: "In your country, how common is illegal diversion of public funds to companies, individuals, or groups?" [1 = very commonly occurs; 7 = never occurs] Public trust in politicians is based on the question: "In your country, how do you rate the ethical standards of politicians?" [1 = extremely low; 7 = extremely high] Irregular payments and bribes is based on the average score across the five components of the following WEF Executive Opinion Survey question: "In your country, how common is it for firms to make undocumented extra payments or bribes connected with (a) imports and exports; (b) public utilities; (c) annual tax payments; (d) awarding of public contracts and licenses; and (e) obtaining favorable judicial decisions?" In each case, the answer ranges from 1 [very common] to 7 [never occurs]. Favoritism in decisions of government officials is based on the question: "In your country, to what extent do government officials show favoritism to well-connected firms and individuals when deciding upon policies and contracts?" [1 = show favoritism to a great extent; 7 = do not show favoritism at all] Wastefulness of government spending is based on the question: "In your country, how efficient is the government in spending public revenue?" [1 = extremely inefficient; 7 = extremely efficient] Transparency of government policymaking is based on the question: "In your country, how easy is it for companies to obtain information about changes in government policies and regulations affecting their activities?" [1 = extremely difficult; 7 = extremely easy] A normalization was used to obtain a comparable index between 1 to 100 using the following formula: $I = (var - min) / (max - min)$, where *var* is the trust value in each question and the maximum and minimum are the highest and lowest value in the datasets, respectively. After that we compared each regional value with the highest value, which tends to be that of the OECD.

public trust in politicians, the incidence of irregular payments and bribes, favoritism among government officials toward well-connected private agents, the level of wastefulness of government spending, and the level of transparency of government policies with all actors in the economy.

An initial observation is the presence of clear heterogeneity across Caribbean country groups. In particular, CCB-NC countries are relatively better positioned on all the indicators when compared to CCB-C countries. This suggests that commodity dependence is negatively associated with the perception of citizens toward political actors. Indeed, Chapter 6 suggested that this heterogeneity could have emerged from a long-term process of institutional gestation influenced by the different types of colonial institutions established, and the varying historical approaches to securing labor inputs. CCB-NC countries are very close to the ROSE group in all dimensions except for wastefulness of government spending and favoritism in the decisions of government officials, where ROSE economies perform better. However, CCB-C countries significantly underperform the ROSE group and display levels closer to Latin American levels. Both, CCB-C and CCB-NC countries are significantly below OECD levels. However, CCB-NC countries have reached, on average, approximately 68 percent of OECD levels, whereas CCB-C countries are less than halfway toward reaching OECD levels.¹²

Public trust in politicians has recently been shown to be a key driver for tax payment compliance. Anderson (2017) shows that trust in government institutions increases the willingness to pay taxes for public goods and services. In addition, Carrillo, Castro, and Scartascini (2017) show that the provision of durable and visible public goods such as sidewalks or roads affect tax payment compliance persistently across time. Therefore, trust in political institutions and their direct actors has the potential to initiate a virtuous circle in which citizens increase tax payment compliance and, provided that the government invests these taxes in demanded public goods, tax-compliant behavior is reinforced over time. Of note, however, absence of trust would prevent the initiation and reinforcement of such a virtuous

¹² The observed pattern of relatively lower performance of commodity dependent economies when benchmarked against non-commodity dependent counterparts is not idiosyncratic to The Caribbean. Indeed, when the ROSE are divided between commodity (ROSE-C) and non-commodity dependent (ROSE-NC) countries, the same regularity is observed. Indeed, ROSE-NC countries have reached, on average, approximately 73 percent of OECD levels, whereas ROSE-C countries are approximately at 67 percent of OECD levels. ROSE-C include: Bhutan, Botswana, Gabon, Lesotho, Macedonia, Mongolia, and Timor-Leste. ROSE-NC include: Cyprus, Mauritius, Montenegro, and Seychelles.

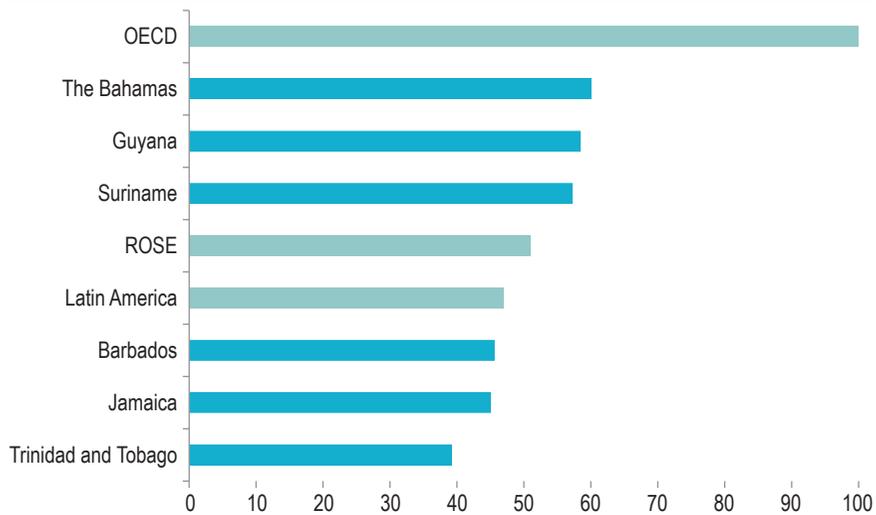
circle. CCB-C countries exhibit low levels of trust in politicians, at 40 percent of the levels of trust in OECD economies. While CCB-NC countries perform relatively better, they also fall below OECD trust levels, with levels that are 65 percent of this benchmark.

The absence of general trust in politicians, therefore, is likely to be preventing the emergence of reinforcing virtuous circles for productivity and growth.¹³ This relative absence of trust in politicians has several explanations. First is the perception regarding the appropriate use of public funds or taxpayers' money. It is expected that trust would be damaged if public resources are not appropriately used. Inappropriate use can entail inefficient use of resources (i.e., overpaying for public goods and services), utilization of public funds for other purposes (i.e., redirection of funds toward private use), or a combination of both. Figure 7.1 shows that both types of inappropriate use are perceived by citizens in the Caribbean. Perceptions of wastefulness of government spending and diversion of public funds are greater in CCB-C countries, standing at 61 percent and 46 percent, respectively, relative to the OECD benchmark. CCB-NC countries perform better, with respective levels of 77 percent and 73 percent relative to the OECD. The CCB-NC levels are closer to those of ROSE.

The second explanation for the relative absence of trust in politicians relates to the objectivity of government actions. Impartiality and transparency of policy decisions are expected to reinforce trust. To this end, Figure 7.1 reports citizens' perceptions of favoritism in the decisions of government officials and of the transparency of government policymaking. Citizens in CCB-C countries perceive a high degree of favoritism within government agents, with a level of 36 percent of the OECD benchmark. Again, CCB-NC countries perform relatively better but still fall below ROSE country levels, with levels that are 55 percent of the OECD. Similarly, the perceived transparency of policy decisions in CCB-C countries is lower than levels in ROSE, CCB-NC, and OECD countries. This indicator in CCB-C countries is 54 percent of the OECD benchmark, compared to a level of 73 percent observed among the ROSE group and 80 percent among CCB-NC countries.

The third explanation is that low levels of trust in political institutions are related to the emergence of illegal institutions such as irregular payments and bribes to obtain public services that are not formally subject to those charges. Indeed, Figure 7.1 shows that the incidence of such

¹³ Alternatively, such a reality could also motivate the emergence of a vicious circle: low tax collection, low revenues for public investments, and further low tax compliance.

Figure 7.2 Index of Trust in Parliament/Congress

Sources: Latin American Public Opinion Project (LAPOP) Surveys for the Caribbean (2006, 2008, 2009, 2010, 2012, 2014) and Latin America (2004, 2006, 2007, 2008, 2010, 2012, 2014); for the OECD, Eurobarometer (2012, 2013); and calculations by the authors.

Notes: The LAPOP Survey question on Parliament was: "To what extent do you trust the Parliament/National Congress?" [1 = not at all, 7 = a lot] The Eurobarometer poses the question differently: "And, for each of them, please tell me if you tend to trust it or tend not to trust it? The European Parliament" [1 = tend to trust, 2 = tend not to trust] A normalization was used to obtain a comparable index between 1 to 100 using the following formula: $I = (var - min) / (max - min)$, where *var* is the trust value in each question and the maximum and minimum values are in brackets. After that we compared each regional value with the highest value, which tends to be that of the OECD.

arrangements is high within CCB-C countries, at 28 percent of the OECD benchmark and below that of all other country groups. At 58 percent of the OECD benchmark, CCB-NC countries perform better than Latin America and like the ROSE.

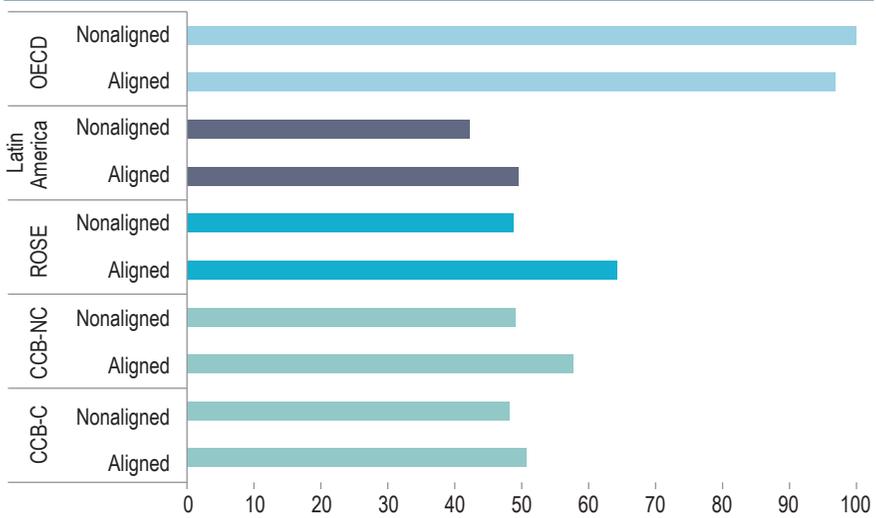
Given that most Caribbean countries have parliamentary democracies, levels of trust in the national parliament are highly relevant. To this end, we collected data from several public opinion surveys worldwide that record levels of trust in this institution.¹⁴ Figure 7.2 shows the results in terms of average levels of trust across countries. The results suggest that trust in the national parliament within all Caribbean countries is significantly below

¹⁴ For the Caribbean and Latin America, information was obtained from the Latin American Public Opinion Project (LAPOP), an academic project led by the Vanderbilt University. The project has been conducting opinion surveys in the Latin America region since 2004, and more recently has been surveying the Caribbean region, with support from the Inter-American Development Bank. For the OECD and part of the ROSE group, we rely on the opinion surveys by Eurobarometer in the euro area. This initiative has been led by the European Commission since 1973.

OECD levels. However, The Bahamas, Guyana, and Suriname display better levels of trust than comparable economies in the ROSE group. By contrast, Barbados, Jamaica, and Trinidad and Tobago display lower levels of trust than both the average ROSE and Latin American country. This evidence shows that trust of Caribbean citizens in what is arguably the most relevant political institution is relatively low, thus undermining the possibility of emerging virtuous circles flowing from trust to productivity and growth.

We also explore whether reported trust is sensitive to the political affiliation or alignment of citizens. This is important given that if individual trust is affected by whether the political party in power is the one to which the individual is affiliated or aligned, then comparisons across countries might be biased by the political alignment of interviewees. To this end, we exploit information on political affiliation collected in the surveys and different political cycles when different parties were in power. We then calculated levels of trust reported by citizens affiliated with the political party in power and trust reported by citizens not affiliated with the party in power. Figure 7.3

Figure 7.3 Index of Trust in Parliament/Congress (Alignment with Party in Power)



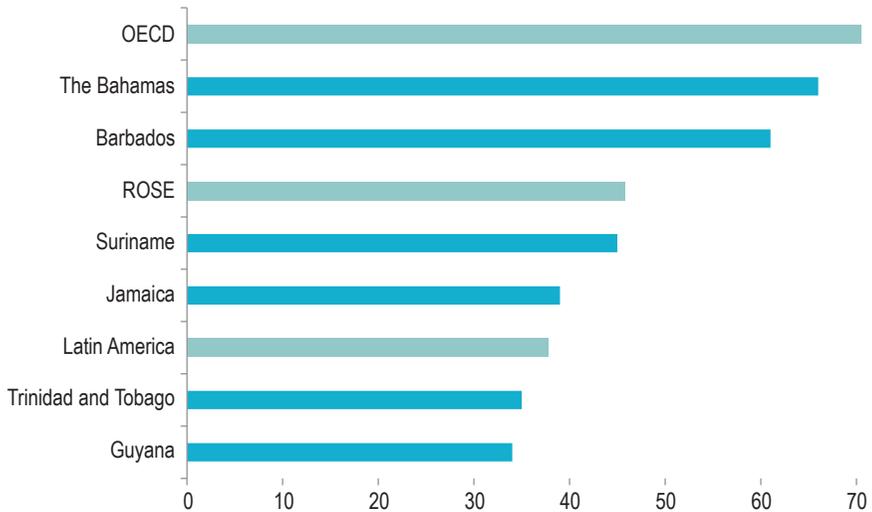
Sources: Latin American Public Opinion Project (LAPOP) Surveys for the Caribbean (2006, 2008, 2009, 2010, 2012, 2014) and Latin America (2004, 2006, 2007, 2008, 2010, 2012, 2014); for the OECD, Eurobarometer (2012, 2013); and calculations by the authors.

Notes: The LAPOP survey question on Parliament was: "To what extent do you trust the Parliament/National Congress [1 = not at all, 7 = a lot] The Eurobarometer poses the question in a different way: "And, for each of them, please tell me if you tend to trust it or tend not to trust it? The European Parliament" [1 = tend to trust, 2 = tend not to trust] To define the alignment with the party in power, we used the LAPOP question "Who did you vote for in the last general election?" and the Eurobarometer question "Which party would you be most likely to vote for at the European elections?" A normalization was used to obtain a comparable index between 1 to 100 using the following formula: $I = (var - min) / (max - min)$, where *var* is the trust value in each question and the maximum and minimum values are in brackets. After that we compared each regional value with the highest value, which tends to be that of the OECD.

summarizes the results. Trust levels within all country groups, except for the OECD, are somewhat higher when the individual is affiliated or aligned with the ruling party. This suggests that reported trust is positively affected when the individual identifies with the ruling party. However, when comparing trust levels across country groups separately between aligned and nonaligned citizens, we observe the same pattern in which not only the Caribbean, but also the ROSE and Latin America significantly underperform OECD levels. Therefore, the relatively low trust levels among Caribbean countries hold for a wide range of developing economies and are observed regardless of political party affiliation.

Corruption is another relevant factor that undermines trust in political institutions. Indeed, Alon and Hageman (2013) find that the incidence of corruption is negatively associated with firm-level tax compliance. Moreover, they also find that this negative relation is ameliorated in places with higher generalized trust. Therefore, corruption not only reduces public investment directly through the divergence of public funds, but also undermines general trust, leading to further reductions of public resources via lower tax compliance. As such, the perception of citizens with respect to the corruption of political institutions is a relevant factor that can have real consequences for public service delivery, productivity, and growth. Figure 7.4 shows the 2016 Corruption Perception Indexes from Transparency International by country groups and for each Caribbean country, complementing previous evidence from the WEF's *Global Competitiveness Report*. These indexes range from 0 to 100, where higher values denote a lower incidence of corruption. The figure shows that The Bahamas and Barbados have relatively low levels of corruption perception, with standards close to OECD levels and better than the levels of ROSE, Latin America, and the rest of the Caribbean countries. In a second group are Suriname and Jamaica, which perform below the ROSE group but better than Latin America. Finally, corruption perceptions in Trinidad and Tobago and Guyana appear to be relatively high, underperforming all country groups considered. This is somewhat consistent with previous patterns suggesting a relatively disadvantaged position for commodity-dependent economies.

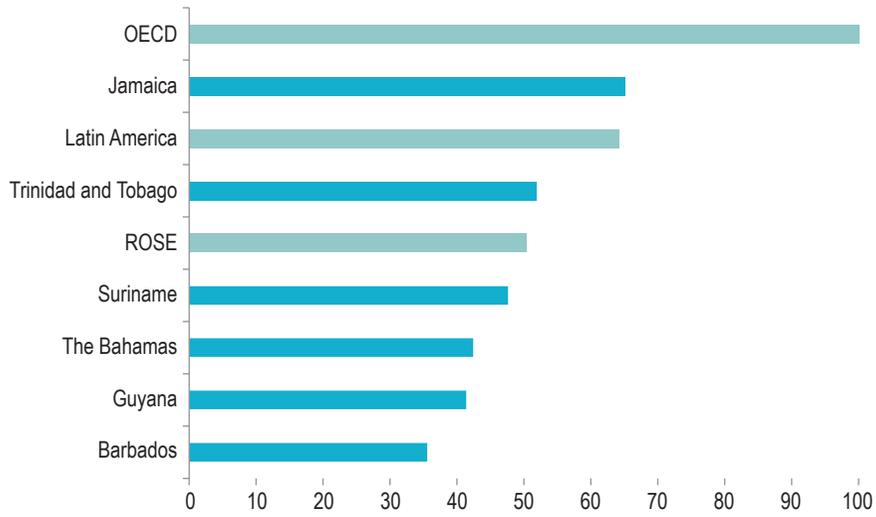
Openness of government in terms of being transparent with citizens about its decisions and the process through which such decisions are taken favors trust in politicians (Beuermann and Amelina 2014; Khemani et al. 2016). This includes, for example, policies of transparency in access to information like drafts of legislation bills to be discussed in Parliament or making legislative proceedings public through the mass media. As such we use data collected by the World Justice Project in 2016 regarding the level

Figure 7.4 Corruption Perception Index, 2016

Sources: Transparency International, Corruption Perception Index and calculations by the authors.

Notes: The following are the sources that Transparency International uses to build the index: African Development Bank Governance Ratings 2015, Bertelsmann Foundation Sustainable Governance Indicators 2016, Bertelsmann Foundation Transformation Index 2016, Economist Intelligence Unit Country Risk Ratings 2016, Freedom House Nations in Transit 2016, Global Insight Country Risk Ratings 2015, Institute for Management Development World Competitiveness Yearbook 2016, Political and Economic Risk Consultancy Asian Intelligence 2016, Political Risk Services International Country Risk Guide 2016, World Bank Country Policy and Institutional Assessment 2015, World Economic Forum Executive Opinion Survey 2016, World Justice Project Rule of Law Index 2016, and the Varieties of Democracy Project 2016. The Corruption Index is the average of the different indicators from the above-mentioned sources, with the highest value corresponding to the least presence of corruption.

of publicized laws and government data. This index puts together citizens' perceptions regarding ease of access to government-produced information on people's legal rights, the public availability of legislation in advance of its discussion in Congress, and the extent to which legislative proceedings are accessible through mass media. Figure 7.5 shows this index across countries, with the OECD as the higher benchmark normalized to 100. The figure suggests that all Caribbean countries significantly underperform the OECD. In addition, except for Jamaica (which performs at par with Latin America at levels around 65 percent of OECD levels), all other countries underperform Latin America. In this category, we also observe that ROSE exhibit modest levels of about 50 percent of OECD standards. The relatively low levels of openness and transparency, therefore, are consistent with lower trust in political actors and institutions, suggesting room for improvement. Transparent and timely access to data exploiting information and communication technologies could increase public trust.

Figure 7.5 Index of Publicized Laws and Government Data

Sources: World Justice Project, Rule of Law Index 2016 and calculations by the authors.

Notes: Publicized laws and government data is the average of nine variables from the World Justice Project's worldwide survey to generate the Rule of Law Index. A normalization was used to obtain a comparable index from 1 to 100 using the following formula: $I = (var - min) / (max - min)$, where *var* is the trust value in each question and the maximum and minimum values refer to the highest and lowest value in the data. After that we compared each regional value with the highest value, which tends to be that of the OECD.

Overall, this section documents that trust in political actors and institutions is low in CCB-C countries, whereas trust levels are higher for CCB-NC countries at levels similar to those of the ROSE group. Given the evidence suggesting that public trust in political institutions is associated with economic growth and productivity, these findings convey particular relevance and motivate objective analyses of the political institutions in each Caribbean country. Such assessments are presented in the individual country chapters within the last section of this volume.

7.2. Rule of Law

The concept of the rule of law refers to the principle that all people and institutions are subject to and accountable to law that is fairly applied and enforced. Within this concept one can differentiate alternative sets of institutions. First, we follow North's (1990) definition of "rules of the game" understood as the rules governing the interactions between individuals in the society, including the relationship between the citizenry and the government. One can then distinguish (i) institutions seeking to protect citizens against expropriation by the government and powerful elites,

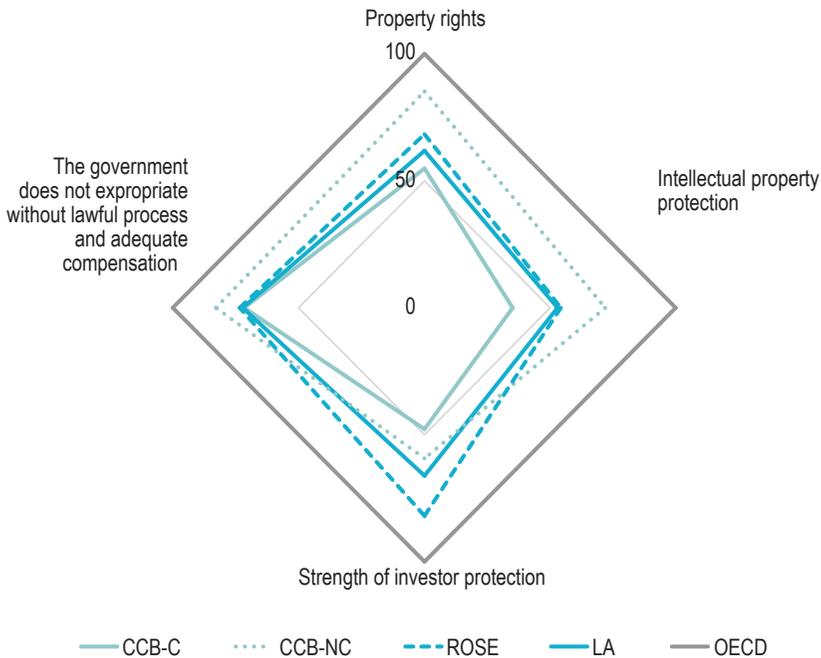
also known as “property rights institutions”; (ii) norms that regulate interactions among the private agents that make up the economy—that is, institutions that seek to facilitate and secure private contracts between citizens, which, following Acemoglu and Johnson (2005), are referred to here as “contracting institutions”; and (iii) institutions in charge of enforcing the previously outlined rules. The later include the police, as the front-line public law enforcer, and the judiciary system.

The next sections analyze the perceptions of citizens regarding the three aforementioned institutions.

7.2.1. Property Rights Institutions

Figure 7.6 shows perceptions captured by the World Economic Forum and the World Justice Project regarding the definition and protection of property rights. All indexes are standardized within a range from 0 to 100, with a

Figure 7.6 Protection of Property Rights



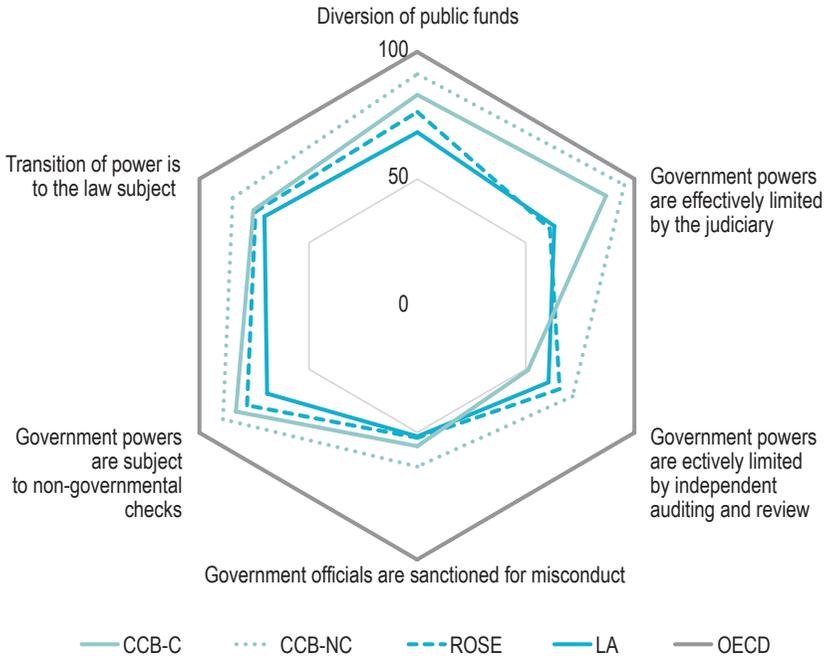
Sources: World Economic Forum, Global Competitiveness Index 2017–2018; World Justice Project, Rule of Law 2016; and calculations by the authors.

Notes: Data from the Global Competitiveness Index were used to calculate the variables for property rights, intellectual property protection, and strength of investor protection. Data from the World Justice Project were used to calculate the variable entitled “the government does not expropriate without lawful process and adequate compensation.”

value of 100 for the OECD as the highest benchmark. Consistent with previous patterns, the first observation is that CCB-C countries underperform all country groups in all dimensions and stand, on average, at 52 percent relative to OECD levels. By contrast, CCB-NC countries either outperform or equal ROSE levels.¹⁵ Furthermore, in terms of overall strength of property rights, intellectual property rights, and the lawfulness of expropriation processes, CCB-NC countries are close to OECD levels, with average levels of 80 percent with respect to this benchmark. However, in terms of the strength of investor protection set forth in the law, CCB-NC countries fall short, at 59 percent, with respect to OECD levels. This is relevant because incentives for long-term investments are affected by the strength of institutionalized protection for investors in the law embedded in the required disclosure of corporate information by management, the extent of director liability, and the ease of shareholder suits. As such, ensuring institutionalized and credible protection for capital investments in private firms should be an important agenda.

Besides the existence of laws protecting the rights of citizens, the presence of institutionalized constraints on government powers provides greater security that these laws will be honored. As such, components of this pillar from the World Justice Project are benchmarked in Figure 7.7. Interestingly, while CCB-NC countries are slightly better than CCB-C countries, both groups perform better than ROSE and are close to OECD levels in some specific dimensions. These include the lawfulness of the transition of political power and the perception that government powers are effectively limited by the legislature and the judiciary and subject to nongovernmental checks. These dimensions average 82 percent and 90 percent of OECD levels for CCB-C countries and CCB-NC countries, respectively. By contrast, both Caribbean groups fall relatively short with respect to OECD in terms of whether government powers are effectively limited by independent auditing and the likelihood that government officials are sanctioned for misconduct. CCB-NC countries, however, perform better than ROSE, averaging 68 percent with respect to OECD levels in these dimensions. Whereas CCB-C countries show levels equivalent to 53 percent of the OECD benchmark which are also below ROSE standards (equivalent to 59 percent of OECD).

¹⁵ Again, this pattern of relatively lower performance of commodity dependent economies when benchmarked against non-commodity dependent counterparts is not idiosyncratic to The Caribbean. ROSE-C also perform below ROSE-NC in terms of perceptions of protection of property rights. ROSE-NC countries have reached, on average, approximately 70 percent of OECD levels, whereas ROSE-C countries are approximately at 64 percent of OECD levels.

Figure 7.7 Constraints to Government Power

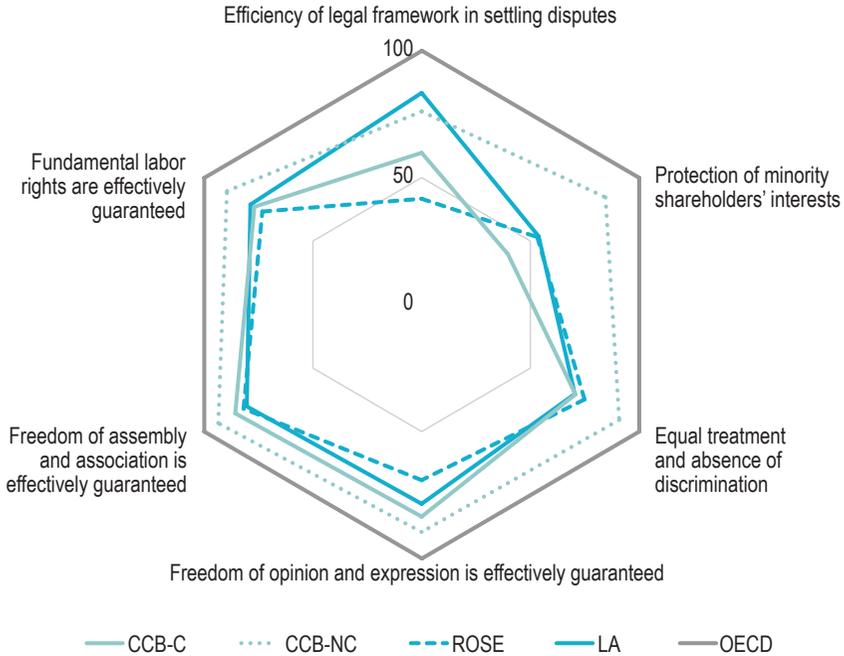
Sources: World Justice Project, Rule of Law Index 2016 and calculations by the authors.

Note: Each component of the figure is an average of a set of five to 16 variables from the World Justice Project Survey.

Overall, perceptions pinpoint appropriate functioning of nongovernmental checks of the legislature and judiciary in terms of limiting government powers. However, it seems that robust independent auditing and effective sanctioning of government officials for misconduct are relatively absent. This perception is in line with the relatively low levels of trust in politicians reported in the previous section.

7.2.2. Contracting Institutions

As mentioned previously, contracting institutions refer to the regulatory framework governing interactions between private agents in the economy. Figure 7.8 benchmarks components related to these institutions obtained from perceptions from surveys by the World Economic Forum and the World Justice Project. Consistent with previous patterns, CCB-NC countries outperform ROSE and CCB-C countries in all dimensions and are relatively close to OECD levels, with an average level of 87 percent with respect to this benchmark. However, it is worth noting that

Figure 7.8 Contracting Institutions

Sources: World Economic Forum, Global Competitiveness Index 2017–2018; World Justice Project, Rule of Law 2016; and calculations by the authors.

Notes: Data from the Global Competitiveness Index were used to calculate the variables on the efficiency of the legal framework in settling disputes and protection of minority shareholders' interests. Data from the World Justice Project were used to calculate the variables on equal treatment and absence of discrimination, freedom of opinion and expression is effectively guaranteed, freedom of assembly and association is effectively guaranteed, and fundamental labor rights are effectively guaranteed.

there are some dimensions where CCB-C countries are close to ROSE and Latin American levels and do not lag significantly behind CCB-NC countries. These dimensions refer to freedom of assembly, association, opinion, and expression, where CCB-C countries perform at an average level of 85 percent with respect to OECD levels. Similarly, regarding perceptions that fundamental labor rights are effectively guaranteed, CCB-C countries are relatively close to CCB-NC countries levels, at 77 percent of OECD levels.

In terms of the efficiency of the legal framework in settling disputes, CCB-C countries have levels equivalent to 60 percent of OECD levels, which are significantly below CCB-NC country levels, which are 76 percent of the OECD benchmark. Furthermore, unequal treatment and discrimination appear to be more prevalent in CCB-C countries, with levels equivalent to Latin American levels of 71 percent of OECD levels. This compares very unfavorably with respect to CCB-NC country levels that are 91 percent of

OECD levels. Protection of minority shareholders is at a low level among CCB-C countries, reaching only 40 percent of OECD levels and underperforming all country groups. As documented in Chapter 6, CCB-C countries show greater ethnic fragmentation than CCB-NC countries. This could be related to the observed higher perceptions of discrimination in CCB-C countries.

In summary, contracting institutions in Caribbean countries appear to perform relatively well in terms of protecting fundamental labor rights and the freedom of initiating an association or expressing opinions. However, in CCB-C countries, the legal framework in place for settling private disputes is perceived as having less than optimal efficiency. This is reflected in perceptions of low levels of protection of minority shareholders' interests.

7.2.3. Law Enforcement Institutions

Citizen perceptions regarding the legitimacy and competency of law enforcement institutions such as the police and the judiciary are important. Such perceptions have a direct relation with the willingness to report crimes and work with the authorities to enhance their effectiveness (Sutton and Ruprah 2017). In addition, if these institutions are perceived as lacking transparency, fairness, and accountability, then they could even generate unintended decreases in security perceptions and increases in crime, as well as discourage people from using legal procedures to resolve disputes. Therefore, trust in these institutions is highly relevant.

As shown by Jaitman and Torre (2016), in comparison with the average of 17 countries in the Latin America and Caribbean region, the Caribbean has devoted some of the lowest expenditure to the administration of justice and the highest expenditure to the police. Indeed, the average number of police personnel per 100,000 population in Caribbean countries is 563, while the world average is only 366.¹⁶ In terms of the administration of justice, the average number of professional judges per 100,000 population in Caribbean countries is 7.5, while the world average is 18.¹⁷ This shows the relatively larger resources allocated to the police compared to the judiciary.

¹⁶ Source: United Nations Office on Drugs and Crime, criminal justice data for 2014 or latest available year. Caribbean countries included are The Bahamas, Barbados, Jamaica, and Trinidad and Tobago.

¹⁷ Source: United Nations Office on Drugs and Crime, criminal justice data for 2014 or latest available year. Caribbean countries included are The Bahamas, Barbados, Jamaica, and Trinidad and Tobago.

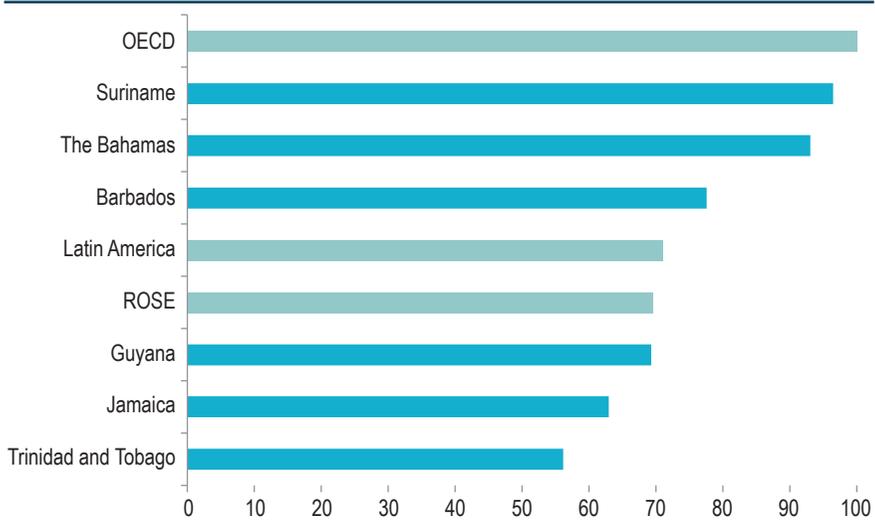
The Police

Although adequately sized police forces are necessary for public safety, it might not be sufficient. The relatively high investment in the police coupled with small populations has resulted in high police density in Caribbean countries, but the perceived effectiveness of the police is relatively low. For instance, in the 2014 Caribbean Crime and Victimization Survey, 65 percent of respondents in Caribbean capital cities reported that if someone were entering their home, it would take the police more than 30 minutes to arrive on a typical day around noon.¹⁸ This indicator suggests that although the physical coverage of the police is not an issue in Caribbean countries, more efficient utilization of police resources might be worth considering in order to improve police response capacity.

Overall trust in the police was measured by exploiting several public opinion surveys around the world and standardizing these measures with respect to the OECD benchmark. Figure 7.9 shows these results, which reveal relatively high trust levels in Suriname and The Bahamas compared with OECD levels. Barbados, while below the levels of the previous two countries, also has trust levels above ROSE and Latin America standards. Guyana shows equivalent trust with respect to both ROSE and Latin America. Whereas Jamaica, and Trinidad and Tobago show low trust levels that are below ROSE and Latin America standards. As such, trust levels in the police are heterogeneous across Caribbean countries. In an exploration of the determinants of trust in the police, Sutton and Ruprah (2017) show that the strongest significant predictor of trust was the perception of police competence in controlling crime. This points to the importance of strengthening training and building the capacity of the police in countries that do not enjoy favorable trust standards.

Another relevant statistic is the percentage of crimes reported to the police, as higher reporting would denote more confidence in this institution. Sutton and Ruprah (2017) examined rates of burglary, robbery, theft of private property, and assault and found that around 51 percent of these crimes are reported in Caribbean countries. This compares favorably to Latin America, where only 35 percent of such crimes are reported, but unfavorably with Western Europe, where 60 percent are reported. The higher level of crime reporting in Caribbean countries when compared to Latin American counterparts is consistent with reported corruption of the police, which can be viewed as discouraging the reporting of crimes.

¹⁸ These surveys were conducted as an extra module of the 2014 Latin American Public Opinion Project (LAPOP) Survey. Caribbean countries included are The Bahamas, Barbados, Jamaica, Suriname, and Trinidad and Tobago.

Figure 7.9 Index of Trust in the Police

Sources: Latin American Public Opinion Project (LAPOP) Surveys for the Caribbean (2006, 2008, 2009, 2010, 2012, 2014) and Latin America (2004, 2006, 2007, 2008, 2010, 2012, 2014); for the OECD, Eurobarometer (2012, 2013); and calculations by the authors.

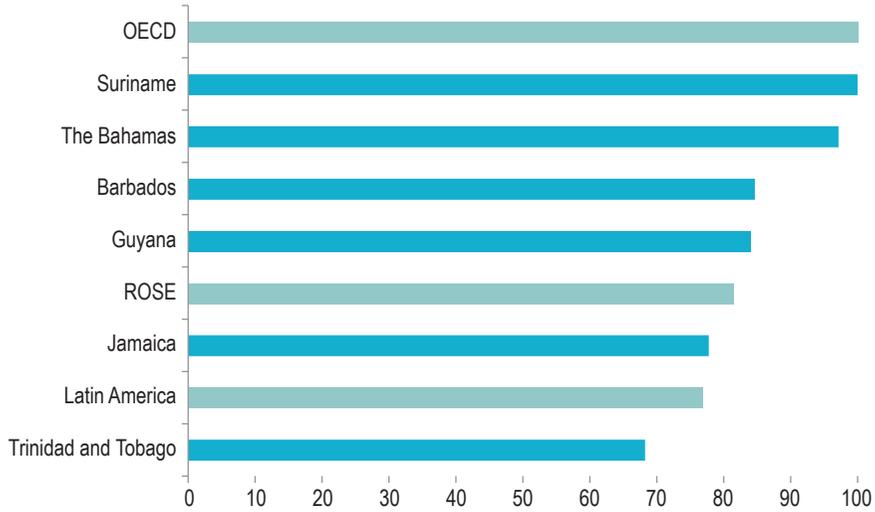
Notes: The LAPOP survey question on trust in the police was: “To what extent do you trust the police? [1 = not at all, 7 = a lot] The Eurobarometer poses the question in a different way: “And, for each of them, please tell me if you tend to trust it or tend not to trust it? The Police” [1 = tend to trust, 2 = tend not to trust] A normalization was used to obtain a comparable index between 1 to 100 using the following formula: $I = (var - min) / (max - min)$, where var is the trust value in each question and the maximum and minimum values are in brackets. After that we compared each regional value with the highest value, which tends to be that of the OECD.

Indeed, only 7 percent of respondents in Caribbean countries reported being asked to pay a bribe by a police officer, while 11 percent of respondents did so in Latin America.

In summary, the coverage of police services in the Caribbean does not appear to be an issue and indeed stands above global benchmarks. However, this has not always translated into effective capacity to respond quickly to citizens’ demands for public safety services. Indeed, levels of trust in the police are highly heterogeneous, with Suriname, The Bahamas, and Barbados performing above ROSE and Latin America; Guyana performing at par; and Jamaica, and Trinidad and Tobago falling short. This heterogeneity suggests that policies that support institutional strengthening through adequate training and the effective use of human resources are worth considering in settings where there is less trust in the police.

The Judiciary

The performance of judicial systems as well as the level of public trust in them affects levels of crime and violence (Sutton and Ruprah 2017).

Figure 7.10 Index of Trust in the Justice System

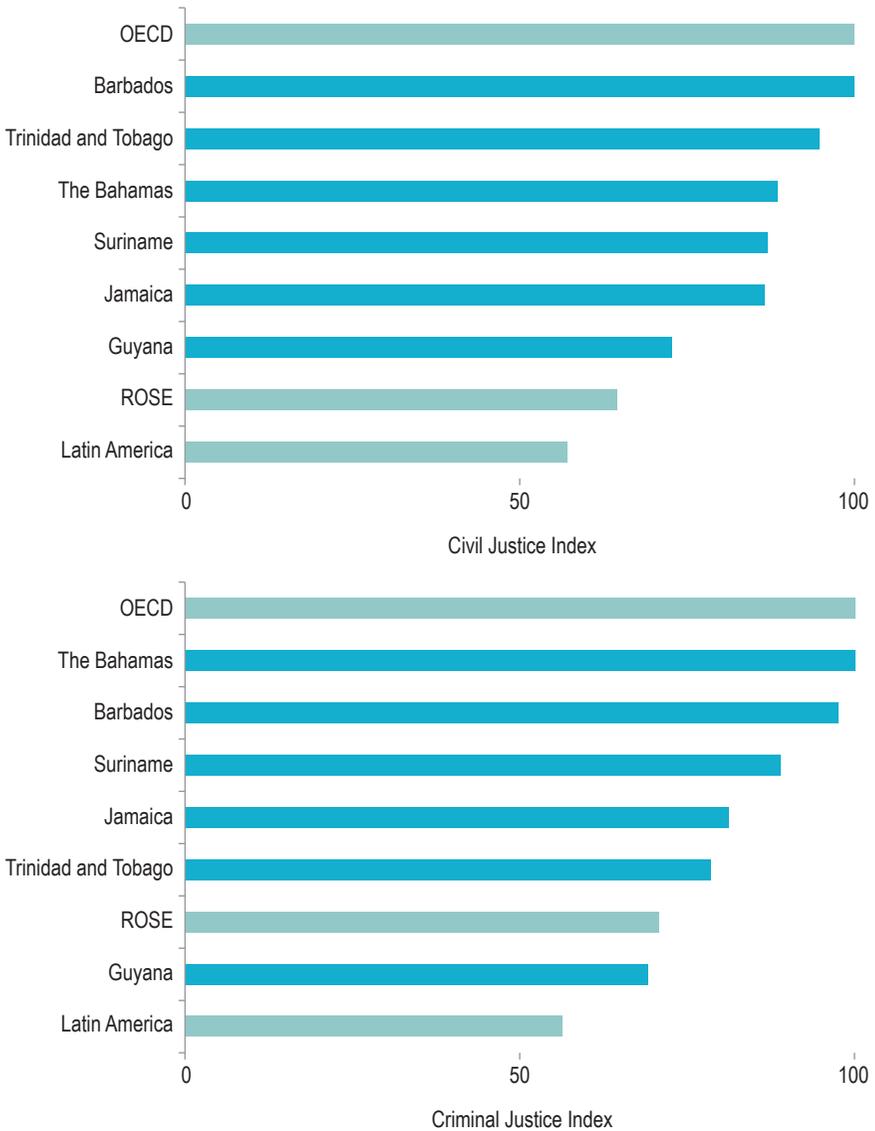
Sources: Latin American Public Opinion Project (LAPOP) Surveys for the Caribbean (2006, 2008, 2009, 2010, 2012, 2014) and Latin America (2004, 2006, 2007, 2008, 2010, 2012, 2014); for the OECD, Eurobarometer (2012, 2013); and calculations by the authors.

Notes: The LAPOP Survey question on Parliament was: "To what extent do you trust the justice system?" [1 = not at all, 7 = a lot] The Eurobarometer poses the question in a different way: "And, for each of them, please tell me if you tend to trust it or tend not to trust it? Courts" [1 = tend to trust, 2 = tend not to trust] A normalization was used to obtain a comparable index between 1 to 100 using the following formula: $I = (var - min) / (max - min)$, where *var* is the trust value in each question and the maximum and minimum values are in brackets. After that we compared each regional value with the highest value, which tends to be that of the OECD.

However, Caribbean countries invest the least amount of GDP in the administration of justice (Jaitman and Torre 2016). Therefore, it is worth asking about the relative effectiveness and trust in this institution.

As shown in Figure 7.10, overall public trust in justice systems across Caribbean countries is quite heterogeneous. The judiciary in Suriname and The Bahamas enjoys elevated levels of public trust comparable to OECD levels. Somewhat below are Barbados and Guyana, with trust levels in line with ROSE levels and at 84 percent of OECD levels. Finally, Jamaica and Trinidad and Tobago display the lowest levels of public trust. Jamaica is at the level of Latin America at 77 percent of OECD levels, while Trinidad and Tobago is below Latin America with trust levels that are 68 percent of the OECD benchmark. Not surprisingly, Trinidad and Tobago and Jamaica are the countries with the least number of judges per 100,000 population, with 7 and 3 judges, respectively. This is far below the world average of 18 judges per 100,000 population.

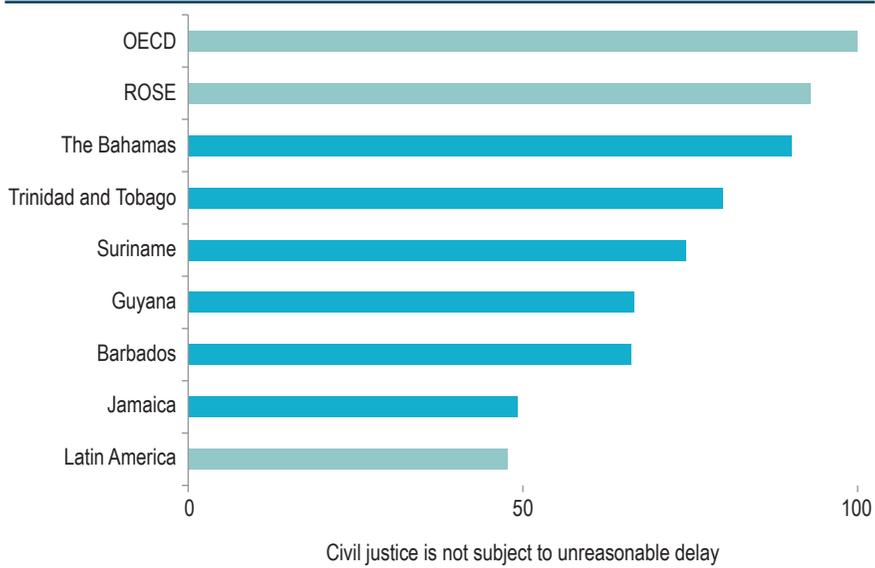
Objective performance measures of justice systems usually quantify the extent to which cases are processed fairly and without unreasonable

Figure 7.11 Perception of Corruption in the Justice System

Sources: World Justice Project, Rule of Law Index 2016 and calculations by the authors.

Note: Each component of the figure is an average of a set of six to 10 variables from the World Justice Project Survey.

delays. Unfortunately, as reported by Sutton and Ruprah (2017), basic objective indicators on the flow of cases through justice systems in Caribbean countries are not consistently available. Therefore, we rely on public perceptions collected by the World Justice Project. In terms of fairness of processes, we assess public perceptions regarding the presence of

Figure 7.12 Index of Timeliness in Civil Justice

Sources: World Justice Project, Rule of Law Index 2016 and calculations by the authors.

Note: Each component of the figure is an average of a set of five variables from the World Justice Project Survey as described in Appendix 1.

corruption in justice systems. Figure 7.11 displays public perceptions on the incidence of corruption within justice systems differentiated between civil and criminal justice. For civil justice, all Caribbean countries outperform ROSE and, except for Guyana, are relatively close to OECD levels. Similarly, in terms of criminal justice, the only country slightly underperforming ROSE is Guyana. However, even though Guyana is the poorer Caribbean performer, it performs relatively well when compared to Latin America. As such, we interpret this evidence as an indication that corruption within justice systems in the Caribbean is relatively low.

Timeliness in the administration of justice is another key determinant of performance. Figure 7.12 displays citizens' perceptions on whether civil justice is subject to unreasonable delays. In contrast with the presence of corruption, where almost all countries were better than ROSE, timeliness in the administration of civil justice is perceived to be below OECD and ROSE levels for all Caribbean countries. This situation is relatively more serious for Jamaica, as it is the only Caribbean country that not only underperforms ROSE but also is at par with Latin America, which is the poorest performer at levels that are 48 percent of OECD standards. These perceptions are consistent with the fact that Jamaica has only three judges per 100,000 population, the lowest number across the Caribbean, Latin

America, and the OECD, and a level comparable only with that of sub-Saharan Africa.

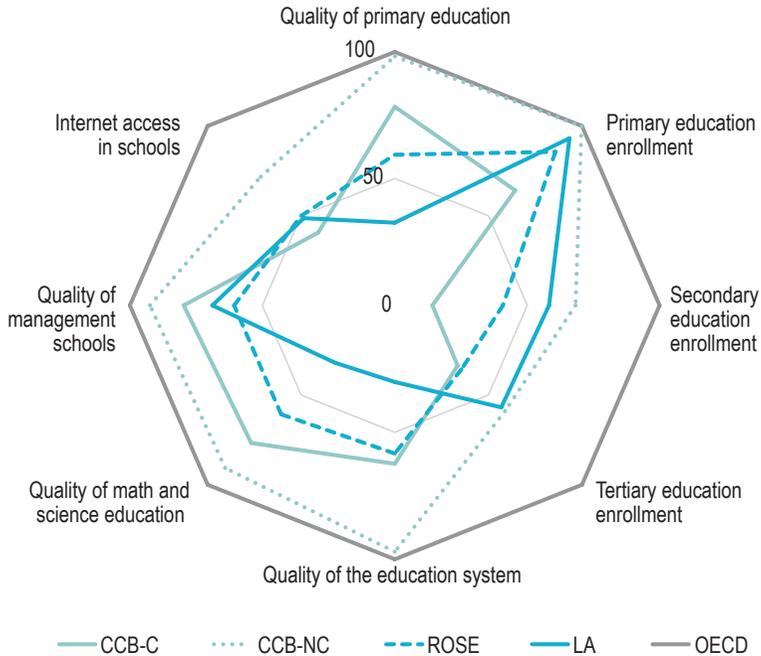
Overall, it seems that the heterogeneity of trust levels in judicial systems across Caribbean countries is primarily affected by the timeliness of the administration of justice. This is corroborated by the fact that investments in judicial systems across the Caribbean are relatively low. Therefore, increasing the coverage of efficient and competent administration of justice services is a policy that could be considered within Caribbean countries.

7.3. Institutions Related to Human Capital Development

The concept of human capital is quite broad, referring to the stock of cognitive skills, socio-emotional skills, habits, personality, physical and mental health, and any other characteristics feeding the ability to produce economic value and spur productivity. As such, there is no single measure of human capital. Rather, some key ingredients related to its production have been identified in the literature. Education and health are the two main attributes that feed most of the components embedded within the concept of human capital. Therefore, institutions responsible for the provision of education and health services constitute key drivers of human capital accumulation and, ultimately, productivity and growth. This section benchmarks some of the main education and health indicators across country groups to gain an initial understanding of where Caribbean countries stand. The individual country chapters in this volume will take a closer look at the country-level institutional settings of these services.

7.3.1. Education

Hanushek and Woessman (2012) have shown the effect of education on long-run economic growth. The authors disentangle the causal effects on country-level economic growth of the quantity of education (measured by years of schooling) and the quality of education (measured by performance on the Program for International Assessment examinations). Findings suggest that the quality of education matters for economic growth. However, the quantity of education is mostly orthogonal to growth once quality is accounted for. At the micro level, Beuermann and Jackson (2018) show that getting access to more selective secondary schools in Barbados with higher-ability peers, lower class sizes, and more diverse classmates; increases adult health status, quality of employment, and earnings. Therefore, both macro- and micro-level evidence

Figure 7.13 Perceptions of Educational Quality

Source: World Economic Forum (WEF), Global Competitiveness Index 2017–2018.

Notes: For quality of education, the question was: “In your country, how do you assess the quality of primary education?” [1 = extremely poor—among the worst in the world; 7 = excellent—among the best in the world] The primary, secondary, and tertiary education enrollment data reported by the WEF are obtained from UNESCO, Education at a Glance 2016, and national sources. The questions for the indicators for quality of the education system, math and science education, and management schools were: “In your country, how well does the education system meet the needs of a competitive economy?” [1 = not well at all; 7 = extremely well]; “In your country, how do you assess the quality of math and science education?” [1 = extremely poor—among the worst in the world; 7 = excellent—among the best in the world]; and “In your country, how do you assess the quality of business schools?” [1 = extremely poor—among the worst in the world; 7 = excellent—among the best in the world].

suggest that the quality of educational institutions matter for growth and productivity.

Figure 7.13 benchmarks several indicators collected by the World Economic Forum related to the quality and coverage of education. An initial observation is that CCB-NC countries outperform CCB-C countries in all dimensions and are, on average, at levels equivalent to 85 percent of OECD levels. This pattern is consistent with previous findings of relatively better perceptions of political and rule of law institutions among CCB-NC countries.¹⁹

¹⁹ Consistently, we also observe this pattern within the ROSE. ROSE-C also underperform ROSE-NC in terms of perceptions of educational quality. ROSE-NC countries have reached, on average, approximately 71 percent of OECD levels, whereas ROSE-C countries are approximately at 47 percent of OECD levels.

Nonetheless, CCB-C countries perform roughly similar to ROSE with an average performance across all measured characteristics that is 56 percent of OECD levels but above Latin America, which is the poorest performer with levels that are 52 percent of OECD levels. Therefore, the overall quality of educational institutions across the Caribbean is at the expected level considering the size of the economies. However, there is room for improvement, particularly in the CCB-C group.

Turning to individual dimensions, it is apparent that the public perception of the overall quality of the education system in CCB-NC countries is high and equivalent to OECD levels. This is also true for specific perceptions of quality of primary education, math and science education, and management schools. In CCB-C countries, quality perceptions are relatively lower but equivalent to ROSE levels at approximately 65 percent of the OECD benchmark. These levels are well above perceptions of the quality of education expressed within Latin America, which are at levels that are 51 percent of OECD levels.

However, both CCB-NC and CCB-C countries lag significantly behind OECD standards in terms of Internet access in schools and secondary education enrollment. Regarding Internet access, robust empirical evidence provided by Malamud and Pop-Eleches (2011), Fairlie and Robinson (2013), Beuermann et al. (2015), Cristia et al. (2017), and Malamud et al. (2018) shows that there are no effects of mere access to technology and Internet on cognitive, noncognitive, or socio-emotional skills. Therefore, while bridging the digital divide could be a necessary condition, it is far from sufficient to increase human capital. However, there are promising interventions that exploit technology to tailor teaching at the individual level, fostering development of students within a personalized experience. Muralidharan, Singh, and Gaminian (2017) show that this type of intervention caused large gains in student learning at all levels of pre-program ability. Therefore, attention within the Caribbean should be placed not only on accessing technology within schools, but also on exploiting it with specialized software tailoring the teaching experience at the appropriate level for each student.

Another area where the Caribbean falls relatively short pertains to the perceived shortfall of individuals with tertiary education. Indeed, CCB-NC country levels are 59 percent of OECD levels, while CCB-C countries are at 34 percent with respect to this benchmark. A comparison of labor demand and supply in Caribbean countries (with available data covering The Bahamas, Barbados, Jamaica and Trinidad and Tobago) by Ruprah and Sierra (2016) shows that these perceptions are connected to reality. Some 52 percent of positions in the private sector demand workers with secondary education or less, and 86 percent of the local workforce has this level

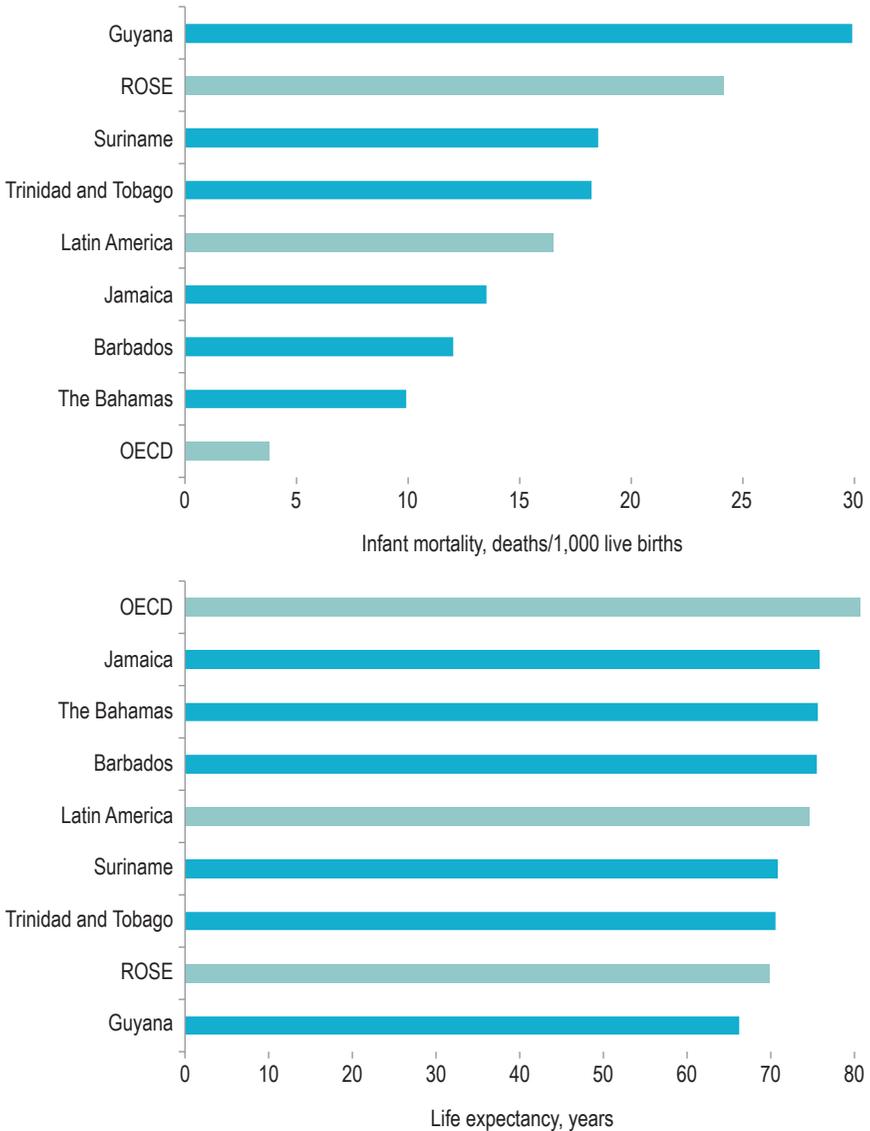
of education. By contrast, 48 percent of positions require post-secondary education and only 14 percent of the local labor force has this educational level. Clearly, there is an oversupply of lower-educated persons and excess demand for persons with post-secondary education. International migration of post-secondary-educated persons from the Caribbean explains most of this puzzle, as 65 percent of tertiary-educated persons from the Caribbean have migrated to OECD countries (Mishra 2006). This constitutes one of the highest emigration rates of skilled persons worldwide and is plausibly related to the higher wage premiums obtained by tertiary-educated Caribbean citizens abroad when compared to wage premiums enjoyed within the Caribbean (Alonso-Soto and Nopo 2017).

This scenario suggests a situation in which the overall quality of education in the Caribbean is relatively high, but the returns to such investments appear to dissipate due to skill-biased migration rates. This is consistent with relatively low levels of innovation and productivity within the Caribbean (Ruprah and Sierra 2016). This prevents higher educational wage premiums and reinforces a cycle of losing more educated citizens through migration, thereby undermining even more the potential for growth. Therefore, while the quality of education is relatively high in the Caribbean, the region is not benefiting from its educational investments. Increasing the potential for innovation and growth that translates into more attractive career paths for high-skilled individuals should therefore be a high priority among policies targeting institutional reform.

7.3.2. Health

Evidence has shown that health and education are complements to human capital development. Indeed, healthier persons will better absorb exposure to educational interventions, which in turn will transform into larger gains in human capital and future productivity (Acemoglu and Johnson 2007; Bleakley 2007). Therefore, good health status is not only relevant within an isolated view but is also important as a booster of long-term returns to educational and any other sort of human-capital-related interventions. As such, well-functioning institutions responsible for ensuring appropriate health of the population have the potential to impact long-term productivity and growth both directly through the good health of individuals and indirectly through the enhancement of potential effects of other interventions.

We benchmark health status within the Caribbean by focusing on two objective indicators: infant mortality and life expectancy. Figure 7.14 reveals that all Caribbean countries lag significantly behind OECD levels. Guyana has the highest rate of infant deaths at 30 per 1,000 live births.

Figure 7.14 Health Indicators

Source: World Economic Forum (WEF), Global Competitiveness Index 2017–2018.

Note: The data were obtained by the WEF from the World Bank's World Development Indicators.

This is significantly above the ROSE average rate of 24.16 deaths per 1,000 live births. Suriname and Trinidad and Tobago perform better but relatively close to ROSE with 18 deaths per 1,000 live births. Finally, Jamaica, Barbados, and The Bahamas perform significantly better with an average

of 11.8 deaths per 1,000 live births. This indicator shows again that CCB-C countries are relatively worse off, performing worse than Latin America. By contrast, CCB-NC countries perform significantly better than ROSE and Latin America, while still underperforming the OECD.

Similarly, life expectancy in CCB-C countries underperforms Latin America. CCB-C countries average 69 years of life expectancy which is close to ROSE (70 years) but below Latin America (75 years). By contrast, CCB-NC countries perform better, averaging 76 years, which is closer to the OECD level of 80 years. Both health indicators measuring distinct stages of life follow a recurrent finding: the relatively better position of CCB-NC countries and the relative underperformance of CCB-C countries.

7.4. Conclusions

This chapter has assessed the level of trust and other perceptions of Caribbean citizens, as well as some objective indicators, regarding the performance of three key sets of institutions: political, rule of law, and institutions related to human capital development. Overall, the chapter documents a pattern suggesting that commodity-dependent Caribbean countries perform below countries more dependent on tourism.²⁰ As documented in Chapter 6, this pattern is consistent with the literature that explores the link between historical colonization experiences and contemporaneous institutions.

Public trust in politicians in CCB-NC countries is at a level similar to the ROSE group at 65 percent of OECD levels. However, trust in politicians in CCB-C countries is lower, at 40 percent of OECD levels. Lower levels of trust are associated with higher perceptions of wastefulness of government expenditures and diversion of public funds, as well as with lower levels of transparency of government policymaking.

Perceptions regarding rule of law institutions in terms of property rights protection suggest an appropriate role of the legislature and the judiciary in terms of limiting government powers. However, consistent with the relatively low levels of trust in politicians, perceptions suggest relatively weak independent auditing processes and an absence of effective sanctioning of government officials for misconduct. When looking at contracting institutions, the Caribbean performs well in fundamental labor rights and freedom of association and expression. But CCB-C countries fall short in terms of mechanisms to protect minority shareholders' interests.

²⁰ This pattern, however, is not unique within Caribbean countries. Along the chapter, we have shown that such pattern holds within the ROSE as well.

Institutions that foster human capital development relate to education and health. Perceptions of educational quality in CCB-NC countries are at levels like the OECD. CCB-C countries show relatively lower perceived quality, in line with ROSE economies. However, all Caribbean countries share the shortcoming of relatively low availability of tertiary-educated persons. Indeed, the region has one of the highest emigration rates of persons with tertiary education. This prevents Caribbean economies from enjoying the returns of their public investments in education, thereby limiting their productive growth capacity. Similarly, health indicators such as infant mortality and life expectancy place CCB-NC countries at a relatively advantaged position compared to CCB-C countries.

Overall, the chapter has documented relatively low trust and perceptions of performance of the institutions analyzed. This problem is more profound in CCB-C countries, while less pervasive in CCB-NC countries. However, beyond this aggregate pattern, institutional improvement needs to have specific diagnoses and recommendations for each individual context. Therefore, the next chapter assesses the fiscal situation of Caribbean countries making the case for the development of appropriate fiscal institutions. Then, the individual country chapters assess the condition of each country in terms of political, rule of law, human capital development, and economic institutions with the aim to identify areas for improvement.

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The Fiscal Challenges in the Caribbean and the Role for Institutions

Jose Fajgenbaum and Claudio Loser

In the context of an aging global economy and, as a consequence, declining global rates of economic growth and increasing fiscal pressures, the six Caribbean countries that are the subject of this study—The Bahamas, Barbados, Guyana, Jamaica, Suriname, and Trinidad and Tobago—clearly need to engage in a major process of reform. Central to this effort is the need to strengthen their public sector performance, which has been relatively weak and has thus hampered economic growth and social development. This not only relates to the actual outcome regarding fiscal discipline and consequent debt sustainability, but also to the institutional framework within which fiscal policy is formulated, conducted, communicated, and assessed. Indeed, as evidenced in Chapter 5 of this volume, the institutional framework for fiscal policy is intimately related not only to fiscal outcomes but also to the overall efficiency in public expenditures and economic growth. Given the relevance of this institutional setting and the relatively weak fiscal performance across the Caribbean that was highlighted in Chapter 2, the aim of this chapter is twofold: (a) document the fiscal situation of each of the Caribbean countries analyzed in this volume; and (b) identify shortcomings in their fiscal institutional frameworks toward providing relevant policy recommendations on this front.

As indicated by Wright, Grenade, and Scott-Joseph (2017), public debts have grown largely due to fiscal mismanagement, sustained growth of public expenditure well in excess of revenue, and persistent deficits.¹ Based on the most recent World Economic Outlook data from the International Monetary Fund (IMF), expenditure for these Caribbean countries grew from a simple average of about 26 percent of gross domestic product (GDP) in 2000–2001 to an estimated 30.5 percent in 2016–2017. During the

¹ The increase in public expenditures also reflects, albeit in small part, the need to address the effects of natural disasters.

same period, average revenue was largely stable with a marginal increase from about 24 percent to nearly 25 percent, while the average overall fiscal deficit grew from less than 2 percent of GDP to 5.5 percent. The countries' average debt rose about 11 percentage points of GDP to 73.5 percent of GDP, which compares with 52 percent for the world's 164 emerging and developing economies for which information is available. Moreover, in 2016 the public debts of Jamaica and Barbados, in terms of GDP, were the 7th and 10th highest, respectively, among the emerging and developing economies. Procyclical policies to ameliorate the effects of the Great Recession of 2008, and declining terms of trade in more recent years generally in the absence of fiscal space, accelerated this deterioration. Wright, Grenade, and Scott-Joseph (2017, 1) suggest "that Caribbean countries cannot adequately surmount their fiscal and debt challenges in the absence of binding rules that are geared toward entrenching fiscal discipline, curbing fiscal procyclicality, and improving budget transparency and credibility."

The Caribbean Development Bank (CDB 2013) confirmed this view, noting that public debt is one of the most critical development challenges facing the Caribbean region. With debt burdens generally exceeding sustainable levels, the potential for distorted resource allocation is significant, compromising potential development gains and diminishing growth prospects. The CDB (2013) further noted that fiscal outcomes are strongly tied to the quality of policies and the strength of institutions, and that evidence shows that countries that adopt high-quality policies and institutions lower the probability of debt distress and thus reap growth dividends. By contrast, countries can get trapped in a high-debt-low-growth equilibrium because weak policies and institutions are unlikely to result in improvement.

As such, the next section of this chapter reviews the fiscal performance of the Caribbean countries, which is far from uniform. Some of the countries are commodity exporters, others are dependent on tourism, while in some cases, countries have developed significant services sectors, particularly finance and technology. Nevertheless, their fiscal behavior is closely linked to developments in international markets. The link is twofold—the impact of external events on the domestic economies and the uneven development and use of their own policies and institutions to ameliorate the effects of those events. The section illustrates that a protective institutional framework remains wanting, as the economies remain exposed to external events despite many years of experience. Notwithstanding their diversity, there have been common patterns. The countries experienced stable ratios of revenue to GDP, except for the two main fuel exporters, but all raised expenditure as a proportion of GDP, causing fiscal deficits and public debt to increase. Fiscal performance of the Caribbean countries

has been weaker than those of the emerging and developing economies in general and Latin America in particular. Although corrective measures have been taken in some cases, significant problems remain.

The chapter then illustrates how the weakness in fiscal policies, governance, institutional rules, and fiscal processes has led to poor public fiscal performance.² In addition to fiscal over-expansion (reflecting the absence of a political consensus regarding fiscal discipline), deficits and public debt have grown due to poor public sector governance (particularly checks and balances, accountability, and the rule of law), lack of sound budgetary institutions, and the absence of binding fiscal rules aimed at preserving fiscal discipline. These vulnerabilities were compounded by weaknesses in planning capacity, program budgeting and control over spending, and financial management processes, as well as inadequate availability or use of evidence upon which to base sound decision-making and evaluation. The absence of independent fiscal institutions may have been an additional factor.

Finally, the chapter concludes with a presentation of recommendations, based on best practices and international experience, adapted to the individual country circumstances. In this regard, the gaps between current practices and strong institutional frameworks and efficient budgetary processes are wide. Nevertheless, closing the gaps is necessary to ensure fiscal sustainability and promote growth and social development. While the individual action programs will have to be designed in line with the requirements and implementation capacity of each country, the needed urgency should not be underestimated. Strong support from regional development partners will be critical. The necessary reforms are not only imperative, but also do-able, if there is political will.

8.1. Caribbean Countries: Weak Fiscal Performance under Mixed Circumstances

The six Caribbean countries analyzed here constitute a diverse group, both in economic and fiscal terms. With total GDP estimated at US\$56 billion in 2017 (and almost US\$100 billion in terms of purchasing power parity), they account for 86 percent of Caribbean GDP. Counted as one, they would constitute the 14th largest economy in the Latin America and Caribbean region. Their (simple) average per capita income, at US\$12,000 in 2017, is well above the average of US\$9,100 for the whole region. Furthermore, per

² Particularly procyclical fiscal policies in boom times and expansionary countercyclical policies in recession periods accelerated the increase in public debt.

capita income for half of the countries in this group is among the highest in the whole region. As such, their performance can have a significant impact on the Latin America and Caribbean region in general, and the Caribbean region, in particular.

However, these countries are far from similar and synchronized in their behavior. Guyana, Suriname, and Trinidad and Tobago are commodity exporters. Jamaica is only partly so, and together with The Bahamas and Barbados is dependent on tourism. Moreover, The Bahamas and Barbados have developed significant services sectors both in finance and technology. As borrowers and financial centers, they are highly dependent on the behavior of capital markets. Thus, as small and open economies, they are inextricably linked to international events, namely terms-of-trade movements and GDP variability in advanced countries in the Americas and Europe.

Under these circumstances, their fiscal behavior is closely linked to developments in international markets. The link is twofold—the impact of external events on their economies and the development and use of their own policies and institutions to ameliorate the effects of those events. After half a century of independence, and even with a strong heritage and tradition in the public sector, the analysis of the behavior of these economies shows that they remain exposed to external events, and that a protective institutional framework remains wanting.

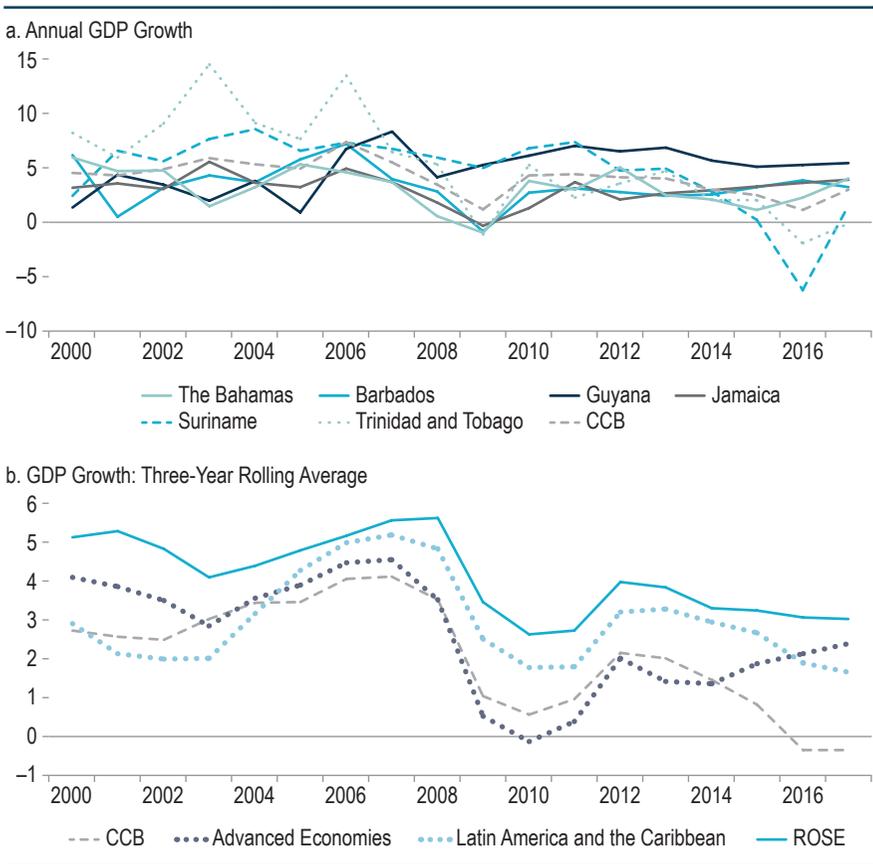
This section reviews the performance of Caribbean countries in this century, particularly the performance of public finances. Even if actions and events have not coincided, there are some general observations that can be made regarding the Caribbean group itself, and the Caribbean compared with other groups of countries.

8.1.1. *Economic Developments of Relevance to Fiscal Performance*

As background to the analysis of developments in public finance, and as noted in other chapters, economic performance in the region has shown a sustained decline since the beginning of the century and certainly since the 2008 global financial crisis. Average annual GDP growth, which had reached almost 3.2 percent in the period 2000–2011, declined precipitously to 0.2 percent in the following six years. This decline reflected the compounded effects of considerably lower terms of trade and weak growth in Europe and the United States—traditional tourist sources for the Caribbean countries. In addition, financial conditions have not favored emerging economies, even as interest rates declined worldwide. Further, concerns about money laundering and tax avoidance put pressures on financial business, particularly in The Bahamas and Barbados.

The declining trend in GDP growth rates was generalized, with the possible exception of Guyana, which benefited from a major public debt reduction under the Highly Indebted Poor Countries (HIPC) initiative. The decline was very strong in the cases of Suriname and Trinidad and Tobago, which were hit hard by the fall in their commodity export prices, after having benefited from high export prices in the previous decade. Figure 8.1 shows the growth performance of Caribbean countries, individually and as a group.³

Figure 8.1 GDP Growth of Caribbean Countries and Comparator Groups (percent change)



Sources: IMF (2017); World Bank, World Development Indicators; and authors' estimates.
Note: Caribbean (CCB): The Bahamas, Barbados, Guyana, Jamaica, Suriname, and Trinidad and Tobago; ROSE: rest of the small economies of the world.

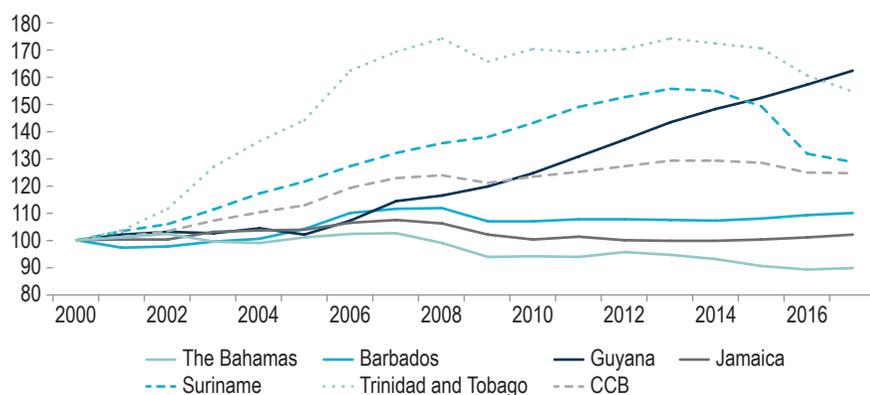
³ The growth value for the Caribbean group is calculated as a simple arithmetic average, as the use of a weighted average (based on GDP weights) would give considerable influence to developments in Jamaica and Trinidad and Tobago, and thus detract from a balanced analysis of all the countries under study.

Not only did the Caribbean show a declining growth trend, but it was also well behind the growth of the rest of the small economies of the world (ROSE) and Latin America and the Caribbean, even though the trend has been one of decline worldwide. The decline in growth of the Caribbean was particularly strong after the global financial crisis of 2008, even as Trinidad and Tobago—the country with the largest GDP in the group—maintained positive momentum until fuel prices collapsed in 2014. Furthermore, during the period 2010–2017 the growth rate of Caribbean countries as a group was -1 percent, compared with an average growth rate of 3.5 percent for ROSE. While the growth rate of the Caribbean had been closely associated with that of the advanced economies, the link broke in 2014, when the advanced economies started to recover, and growth of Caribbean countries declined and eventually became negative (Figure 8.1).

Because of the 2008–2009 crisis and its aftermath, per capita income has tended to decline in recent years. Again, the only clear exception was Guyana. Trinidad and Tobago and Suriname experienced marked declines in per capita income, while per capita income in Barbados and Jamaica stagnated and per capita income in The Bahamas declined moderately (Figure 8.2).

Movements in terms of trade and, more generally, the global financial crisis, singularly affected the performance of Caribbean countries. Furthermore, there was a generalized view that policymakers had to pursue expansionary expenditure policies to mitigate the effect of the crisis, which resulted in high deficits and rapid debt accumulation, beyond the direct

Figure 8.2 GDP Per Capita in Caribbean Countries (2000 = 100)



Sources: IMF (2017) and authors' estimates.

impact of terms of trade and declining economic growth.⁴ As described by Alexandra Peter in the book *Caribbean Renewal: Tackling Fiscal and Debt Challenges*, “the debt accumulation stems from counter-cyclical fiscal policy in bad times and procyclical fiscal policy during periods of economic boom” (Peter, 2014, page 25). Clearly this was not the case for all countries and at all times. In the case of Trinidad and Tobago, the considerable government deposits in the Heritage and Stabilization Fund reduced the effect of the procyclical tendency.

In fact, it is possible to associate a significant part of the high growth rates of Suriname and Trinidad and Tobago in the early 2000s with the increase in commodity export prices and associated revenue. This motor of the economy stopped operating when export prices stabilized, and even had a negative effect when they dropped, suggesting that policymakers may have underestimated the impact of price fluctuations in their formulation of fiscal policy in recent years. As a consequence, they engaged in expansionary policies with the expectation that their economies would recover quickly, which was not the case. The effects of this common underestimation were observed almost universally among commodity exporters worldwide.

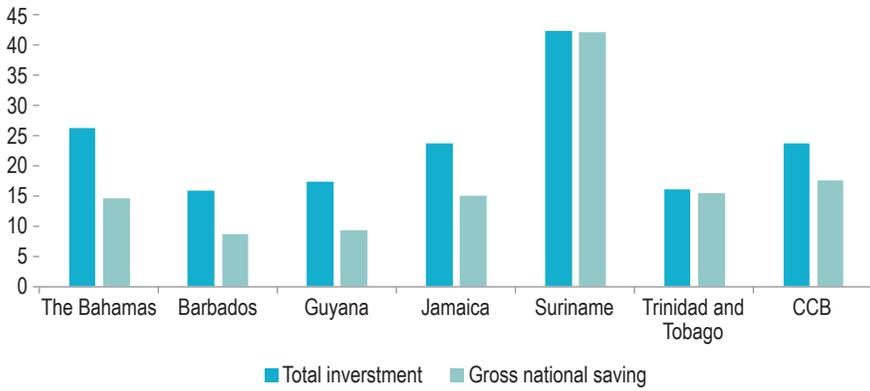
The disappointing performance in terms of growth is remarkable, as savings and investment levels, on average, were reasonable, although with sharp ups and downs as a proportion of GDP, particularly in the case of commodity exporters. This was not the case for Guyana, which, as mentioned, had benefitted from a major debt reduction and was not affected as strongly by the decline in terms of trade, and grew more forcefully. The average Caribbean ratios of investment and savings to GDP were significantly influenced by the high levels in Suriname, which had high savings during the commodity boom and high investment more recently on account of major efforts to develop the country’s oil potential (Figure 8.3).

The mirror image of these developments can be observed in the external current account balances, which were particularly volatile for Suriname and Trinidad and Tobago, although all countries showed considerable movements in the external accounts (Figure 8.4).

Real effective exchange rates of Caribbean countries generally appreciated after the 2008 global financial crisis. This was particularly the case for Trinidad and Tobago and Suriname. In the case of Barbados, the appreciation reflected increased government spending (financed by heavy

⁴ Policymakers had been aware of the additional (reduced) external income obtained (forgone) from commodity shocks, but they tended to underestimate the multiplier effects of these shocks on economic activity. This is discussed in detail in Loser and Vilkelyte (2017) as well in earlier publications of these authors.

Figure 8.3 Caribbean Savings and Investment
(percent of GDP, average from 2000 to 2017)

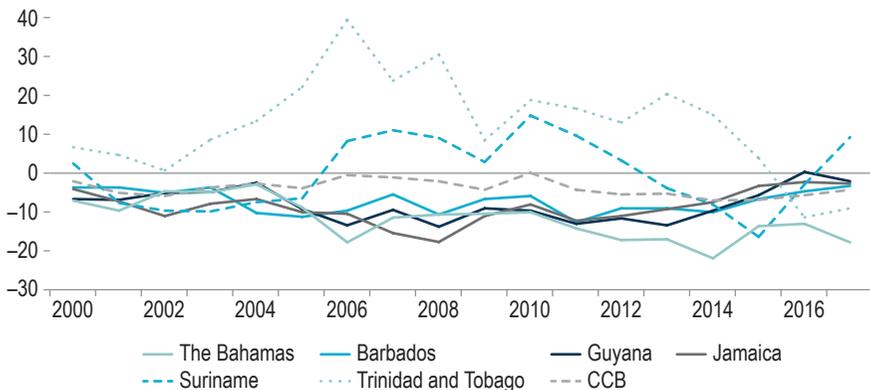


Sources: IMF (2017) and authors' estimates.

borrowing) to mitigate the effect of the recession. In the case of Suriname, the authorities were forced to sharply depreciate the currency in 2016 because the pace of borrowing could not be sustained.

Finally, inflation has not been a major problem in most of the region. For instance, average inflation ranged from 1.4 percent in The Bahamas to 5.7 percent in Jamaica during 2011–2017, well within the range of price increases among emerging and developing economies. By contrast, Suriname suffered major bouts of inflation, with average inflation of 16 percent during that period.

Figure 8.4 External Current Account in Caribbean Countries (percent of GDP)

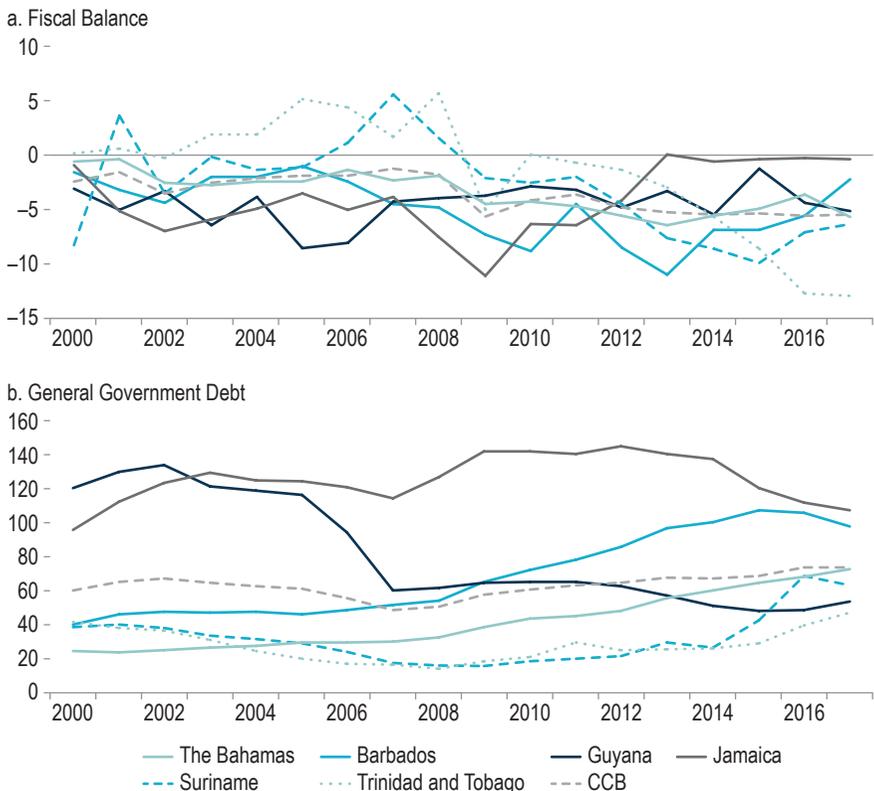


Sources: United Nations Conference on Trade and Development Statistical Database (COMTRADE) and IMF, *World Economic Outlook*.

8.1.2. Fiscal Performance of the Caribbean Countries as a Group

Fiscal performance among the six countries has been diverse, reflecting the different circumstances of their economies. Notwithstanding this diversity, there have been common patterns. The countries experienced generally stable ratios of revenues to GDP, except for the two main fuel exporters, Suriname and Trinidad and Tobago. In turn, all countries raised expenditures as a proportion of GDP, thereby increasing their primary and overall fiscal deficits, as well as government debt, with a poorer performance than comparator groups, as discussed above. The trends for the fiscal deficit and public sector debt among Caribbean countries are illustrated in Figure 8.5. However, the dynamics were somewhat different for Guyana and Jamaica. Both experienced a reduction in the debt burden on account of debt reduction/restructuring exercises. Even so, they

Figure 8.5 Fiscal Balance and General Government Debt (percent of GDP)



Sources: IMF, World Economic Outlook database and authors' estimates.

experienced considerable fiscal imbalances corrected only recently in the context of programs supported by international and regional institutions.

In summary, for the region, the average ratio of revenues to GDP remained largely stable, rising slightly from 24.8 percent during 2000–2010 to 25.4 percent during 2011–2017. By contrast, expenditures rose significantly from 27.3 percent to 30.7 percent. Thus, the overall fiscal deficit increased 2.8 percentage points, to reach 5.3 percent of GDP. The primary balance deteriorated 3.3 percentage points of GDP, only partially offset by reduced interest payments on public debt. As a consequence of these trends, and notwithstanding the noted debt reduction in Guyana, total public debt rose from an average of 59 percent of GDP during 2000–2010 to 69 percent during 2011–2017, well above the benchmark for the other regions, except for the weighted average for advanced economies.⁵

8.1.3. *Fiscal Performance of Individual Caribbean Countries during 2000–2017*⁶

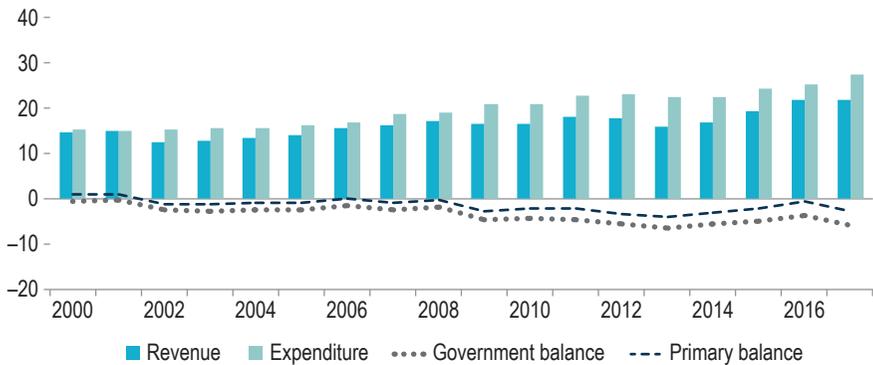
This section provides a brief discussion about the fiscal performance of each Caribbean country. The pattern of fiscal performance at the individual-country level helps bring out the different problems and opportunities across Caribbean countries. The section also provides scenarios based on a simple model (see Appendix 2) for each country that links the public sector deficit to GDP growth and terms of trade, adjusted for corrective programs as appropriate. Based on econometric results, two scenarios are built for each country, using a plausible growth path for the period through 2025, as derived from the Centennial Group world growth model (Kohli 2017). The scenarios assume either constant terms of trade or an average fall of 10 percent. An equivalent increase of that magnitude would result in symmetrical changes in the outcome. The calculations should be viewed as broad estimates, on the assumption that policies remain as they were during the observed years (1997–2007).

The Bahamas

Real GDP in The Bahamas has been declining since 2012. Natural disasters, some failed investment projects, and eroding competitiveness in the face

⁵ The weighted average for the Caribbean, in turn, rose by 8.5 percentage points of GDP, to reach 65 percent.

⁶ The analysis of fiscal performance is based to a significant extent on the most recent published IMF and IDB documentation. However, the views presented here do not and are not expected to represent the views of these institutions.

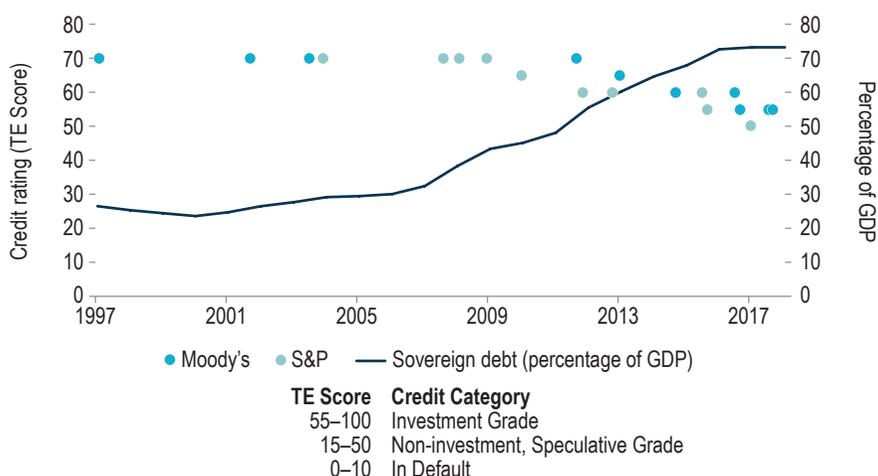
Figure 8.6 The Bahamas: Fiscal Performance (percent of GDP)

Source: IMF, World Economic Outlook database and published documents.

of slow growth in North America (where the bulk of tourist inflows come from) led to declines in real GDP. Even as The Bahamas has the smallest public sector as measured by the ratio of expenditure to GDP, the impact of these events on public finances was significant.

Sluggish economic activity combined with a major increase in government spending led to a considerable deterioration in public finances after 2008, although government deficits declined somewhat after FY 2012–2013. The overall deficit peaked from an average of about 2 percent of GDP during the 1990s and mid-2000s to 6.4 percent in FY 2012–2013, followed by a drop to about 3.5 percent in FY 2015–2016 and a significant increase in 2017 (Figure 8.6). The drop reflected the effective implementation of a 7.5 percent value-added tax and other tax reforms that widened the narrow tax base (yielding more than 4 percentage points of GDP), despite further large increases in expenditure. The overall deficit jumped subsequently owing to an additional increase in expenditure. The accumulation of deficits led to a major increase in gross government debt, from under 30 percent of GDP through 2007 to 73 percent in FY 2016–2017. Government guarantees of the debt of state-owned enterprises (or SOEs, such as The Bahamas Electricity Corporation, Water and Sewerage Corporation, Mortgage Corporation, and Educational Loan Authority) also grew rapidly. When this debt is included, total national public debt stands at close to 80 percent of GDP.

The deteriorating public finances and weakening growth potential resulted in a gradual downgrading of The Bahamas' credit risk. S&P has downgraded sovereign debt markedly since the global financial crisis, from high-quality investment grade to below investment grade in December 2016. Similarly, Moody's lowered its rating, but just to above investment grade (Figure 8.7).

Figure 8.7 The Bahamas: Credit Ratings and Debt-to-GDP Ratio

Sources: IMF, World Economic Outlook database and the Trading Economics website (<https://trading-economics.com/country-list/rating>).

Note: TE: Trading Economics.

The main areas of public sector weakness in The Bahamas are the wage bill and the mounting transfers to SOEs. The SOEs' debt also entails increasing contingent liabilities for the central government. A further burden is generated by the presence of an expanding National Health Insurance (NHI) program, which is not appropriately financed. This is also the case with the National Insurance Board (NIB), which provides pensions, unemployment insurance, and other growing benefits to insured employees. Receipts fall short of expenses, in the face of meager reserves and an aging labor force.

Revenue administration reforms since 2015 are expected to support fiscal consolidation. However, the revenue base is anchored in old-fashioned import duties and the value-added tax. Budgetary fiscal targets have been repeatedly missed. A medium-term fiscal framework would help enhance fiscal discipline and reduce fiscal policy uncertainty, and there are plans to introduce a fiscal rule as part of a fiscal framework.

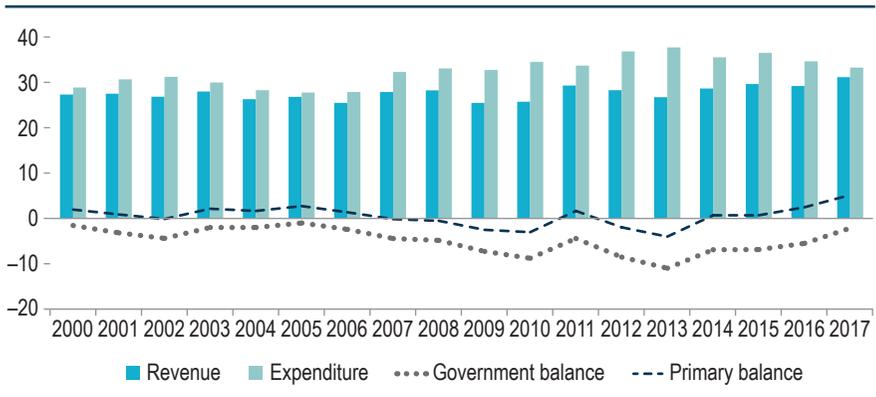
The scenario built for The Bahamas that links the public sector deficit to GDP growth and terms of trade suggests that with current-trend policies the overall fiscal deficit would narrow from the 5 percent estimated for 2017 to 3.5 percent in 2018, and then widen to 4 percent by 2030. This suggests the need for long-term fiscal action to keep debt from becoming unsustainable. A deterioration of 10 percent in terms of trade would widen the deficit by an additional 1.3 percentage points of GDP.

Barbados

The Barbadian economy has diversified into light industry and tourism, with about four-fifths of GDP and exports related to services. Offshore finance and information services are important foreign exchange earners. Barbados' tourism, financial services, and construction industries were hard hit by the 2008 global financial crisis. Subsequently, as the economy stagnated, the government implemented expansionary fiscal policies to stimulate it. This raised the overall public deficit to the equivalent of 11 percent of GDP in 2013. With the realization that this policy was unsustainable, the government embarked on significant adjustment, even as the economy remained sluggish. As a result, overall fiscal deficits declined to a still high average of almost 6.5 percent of GDP during FY 2014–2015 and FY 2016–2017. In recent years the Barbadian economy recovered on the basis of stronger tourism performance, while improvements in public finances have been slow to materialize (Figure 8.8). Economic growth was 1.6 percent in 2016 but decelerated to 0.9 percent in 2017. Further cuts in government spending lowered the fiscal deficit to 4.7 percent of GDP in FY 2016–2017. With increasing concern and reduced lending by creditor banks, the government made increasing use of credit from the Central Bank of Barbados to cover its financing needs.

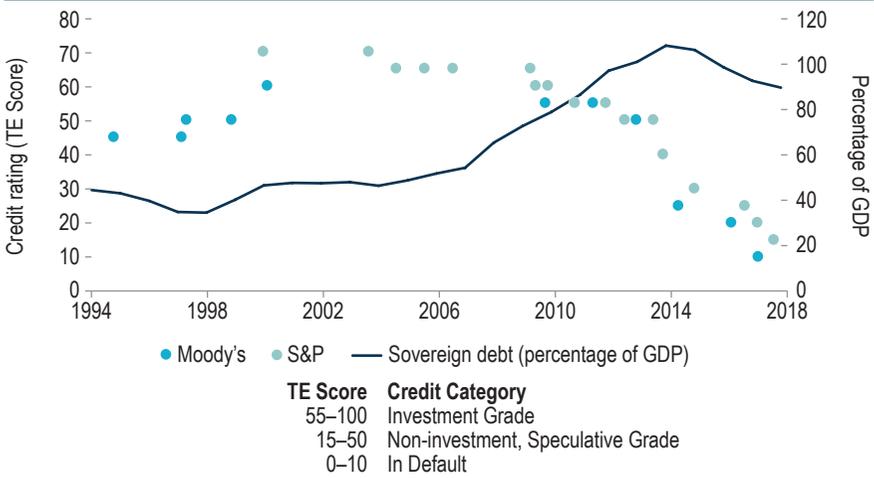
The FY 2017–2018 budget sought to accelerate the pace of adjustment. The budget was primarily focused on raising revenue while shoring up international reserves, including by increasing the National Social Responsibility levy, a tax on imports and domestic manufacturing, from 2 to 10 percent. The government also sought to cut current expenditure, complete ongoing privatization efforts, and undertake new divestments. In addition,

Figure 8.8 Barbados: Fiscal Performance (percent of GDP)



Source: IMF, World Economic Outlook database and published documents.

Figure 8.9 Barbados: Credit Ratings and Debt-to-GDP Ratio



Sources: IMF, World Economic Outlook database and the Trading Economics website (<https://trading-economics.com/country-list/rating>).
Note: TE: Trading Economics.

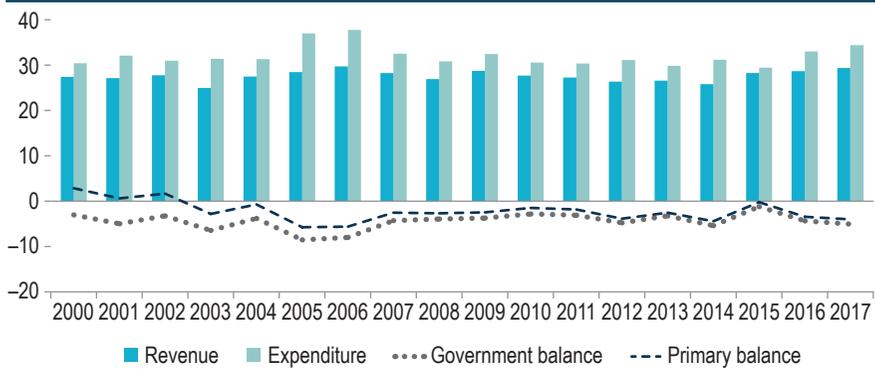
the government initiated a voluntary exchange of debt instruments with the National Insurance Scheme and the Caribbean Development Bank to reduce the interest bill. The continuous deficits gradually raised public debt from 40 percent of GDP in 2000 to 63 percent in 2009, and to 108 percent in 2016. Including the National Insurance Scheme, public debt reached 146 percent of GDP in 2016, up from 83 percent in 2009.

In this context, the high credit ratings that benefited Barbados’ public sector access to the capital markets were steadily lowered. The current ratings are among the lowest non-investment-grade levels, either defined as highly speculative or in default. These ratings reflect the serious concerns about the sustainability of public debt and the sluggish economy (Figure 8.9).

The scenario built for Barbados suggests that with recent-trend policies the fiscal deficit would widen from an estimated 5.5 percent of GDP in 2017 to 11 percent by 2030. A deterioration in the terms of trade would further widen the deficit by 1 percentage point of GDP. This reaffirms the view that Barbados’ public debt is moving to unsustainable levels. Recent actions and steps to promote economic growth could of course change the trend.

Guyana

The Guyanese economy is largely based on agriculture and extractive industries. The economy is heavily dependent on the export of six commodities—sugar, gold, bauxite, shrimp, timber, and rice—that represent

Figure 8.10 Guyana: Fiscal Performance (percent of GDP)

Source: IMF, World Economic Outlook database and published documents.

nearly 60 percent of the country's GDP and are highly susceptible to adverse weather conditions and fluctuations in commodity prices. Much of Guyana's growth in recent years has come from a surge in gold production, although trends in gold prices may affect future growth. Guyana is expected to become an oil producer by 2020, owing to a significant discovery of oil deposits offshore, conservatively estimated to hold between 800 million and 1,400 million barrels. At present, oil exploration and drilling are not included in Guyanese statistics.

An important historical event for Guyana occurred in 2015, when the country had the first change of party in government in 23 years and the second since independence in 1966.

Guyana has experienced sustained growth since 2006, while inflation has been low. The country became heavily indebted as a result of the inward-looking, state-led development model pursued in the 1970s and 1980s. Recent years have seen a major reduction in the government's stock of debt, from about 130 percent in the early 2000s to about 50 percent of GDP, under the HIPC initiative.⁷ Nevertheless, the government is still dealing with significant public debt, against the urgent need for expanded public investment.

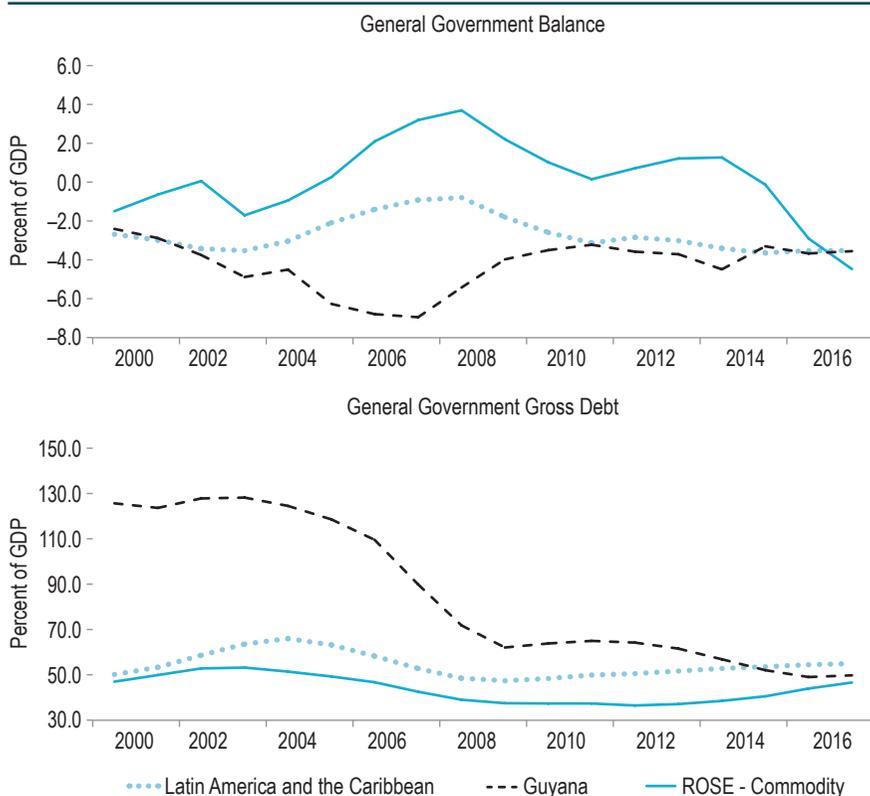
Aided by debt forgiveness, public finances improved in recent years, but deteriorated in 2016 as the public sector deficit widened from 0.2 percent of GDP in 2015 to 2.9 percent, despite curtailment of investment and increased revenue due to improvements in tax administration and higher mining royalties (Figure 8.10). This deterioration reflected a jump of 2 percentage points

⁷ In March 2007, the Inter-American Development Bank, Guyana's principal creditor, canceled nearly \$470 million of the country's debt, equivalent to 21 percent of GDP, in the context of the HIPC initiative.

of GDP in current expenditure, driven by transfers to constitutional agencies, subsidies to the state-owned Guyana Sugar Corporation, and a few one-off expenditures. Continued expansionary fiscal policies maintained sizable public deficits in 2016 and 2017, notwithstanding delayed capital spending. While the deficit is projected to subsequently narrow gradually, financing needs will remain high, which will result in a possible increase in the public-debt-to-GDP ratio from the current stabilized ratio of about 50 percent. Helped by new oil-related revenues, public finances are expected to improve and real GDP growth to increase over the medium term. As Guyana grows, it is likely to lose access to grants and concessional financing.

Figure 8.11 shows the developments in Guyana's fiscal accounts and public debt compared to Latin America and the Caribbean and the ROSE commodity-dependent countries. It also illustrates the considerable positive impact of the debt forgiveness obtained under the HIPC initiative.

Figure 8.11 Guyana: Comparison of General Government Balance and Debt with Other Country Groups (percent of GDP, three-year rolling average)



Sources: IMF (2017); World Bank, World Development Indicators; and authors' estimates.

The scenario built for Guyana suggests that, based on longer-trend policies, the fiscal deficit could initially drop and subsequently remain stable at about 3 percent of GDP over the period, which would induce an increase in debt to GDP. Deterioration in the terms of trade would widen this deficit by about 0.8 percent of GDP. However, if Guyana were to continue to pursue current fiscal policies, the deficit would be larger, and the debt accumulation much higher than this scenario suggests.

Jamaica

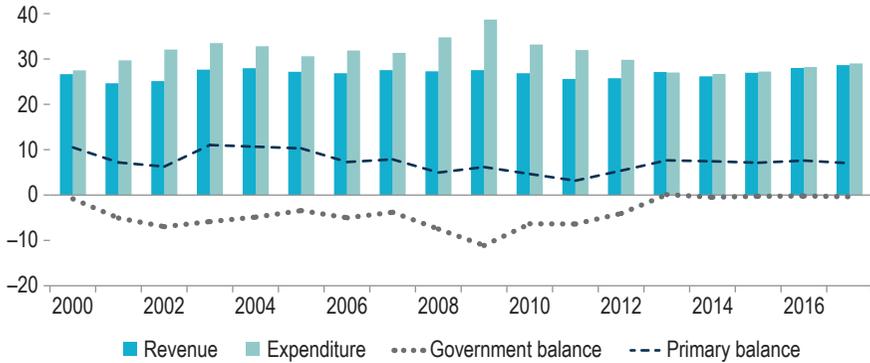
The Jamaican economy is heavily dependent on services, which account for more than 70 percent of GDP. The country derives most of its foreign exchange from tourism, remittances, and exports of bauxite/alumina. Earnings from remittances and tourism each account for about 15 percent of GDP, while bauxite/alumina exports have declined to less than 5 percent of GDP. Jamaica's economy has grown on average less than 1 percent a year for the last three decades and many impediments remain to growth, including a bloated public sector that crowds out spending on important projects.⁸ However, the country has made steady progress in reducing its debt-to-GDP ratio from a high of almost 150 percent in 2012 to about 115 percent in 2017, supported by successive IMF-supported programs. Jamaica's economic program continues to deliver strong results.

The Jamaican economy has improved recently, despite the impact of weather swings in 2017. Growth was positive for more than two years as of mid-2017. Together with strong arrears collection efforts and improved tax filing, this helped increase tax revenues, which were over 25 percent of GDP. Tax policy reforms also influenced the outcome. These included (1) transparent incentives that minimized the room for ministerial discretion, (2) the broadening of the value-added tax base to include government purchases, electricity, and some foodstuffs, and (3) implementation of the Employment Tax Credit.

A key reform of the Tax Administration of Jamaica (TAJ) has been strengthening the Large Taxpayers' Office (LTO), which yields half of revenues from the corporate income tax (CIT). *Amendments to the Revenue Administration Act* have allowed the TAJ to (1) compel for third-party information to cross-check taxpayers' information and activities, and (2) require mandatory e-filing for LTO clients for main tax types including the general consumption tax (GCT) and the CIT. A National Compliance

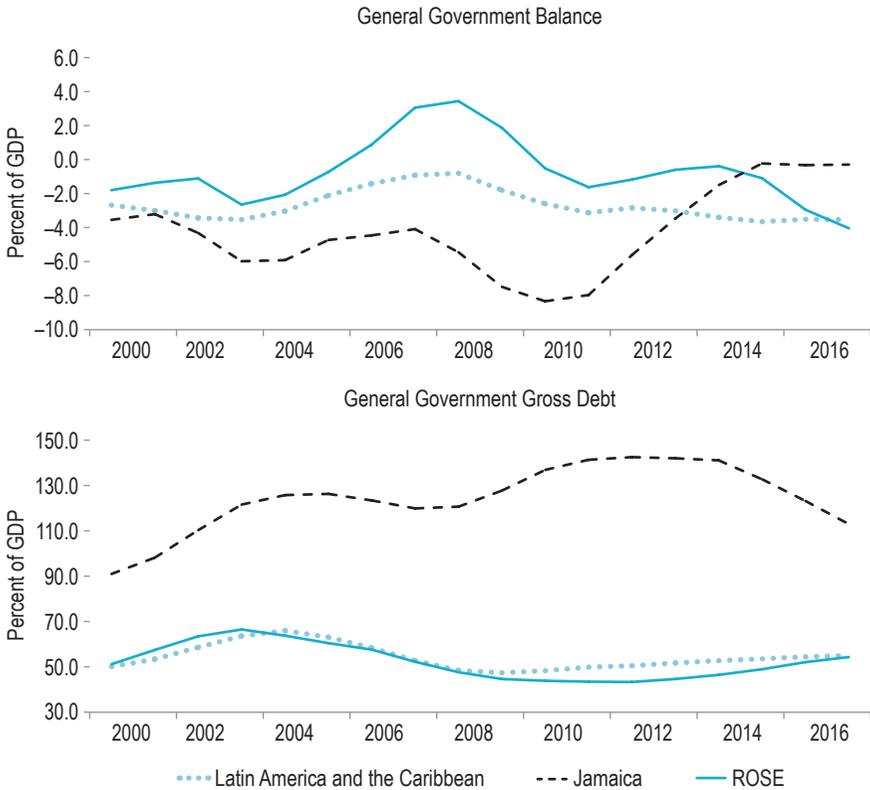
⁸ One concern for the country's future growth is the presence of powerful organized crime networks involved in international drug smuggling and money laundering.

Figure 8.12 Jamaica: Fiscal Performance (percent of GDP)



Source: IMF, World Economic Outlook database and published documents.

Figure 8.13 Jamaica: General Government Balance and Debt Compared to Other Country Groups (percent of GDP, three-year rolling average)



Sources: IMF (2017); World Bank, World Development Indicators; and authors' estimates.

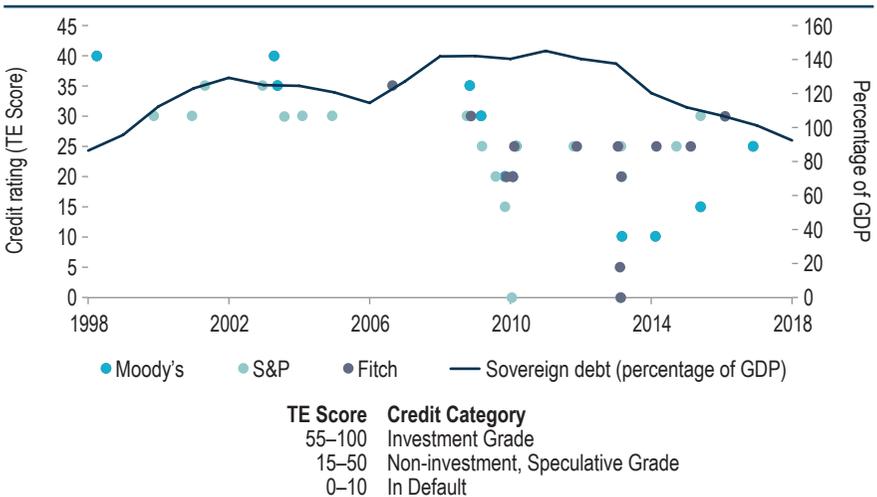
Plan has been published and performance indicators have been established to improve compliance measurement. The TAJ was empowered to collect outstanding arrears and seize and sell taxpayers’ property. Customs administration reforms have also focused on strengthening capacity for tracking of imports and exports.

With the implementation of its economic programs and the 2013 National Debt Exchange, which reduced debt service, Jamaica experienced a major improvement in its public finances. The central government primary surplus has been maintained at about 7 percent of GDP (Figure 8.12). The Petro Caribe debt buyback in 2015 also helped reduce public debt by 20 percentage points of GDP.

Figure 8.13 shows the developments in fiscal accounts and public debt compared to Latin America and the Caribbean and ROSE (the relevant group because of Jamaica’s dependence on commodity exports and tourism). It illustrates the earlier weaker performance compared to the region and ROSE. But with the process of debt restructuring and fiscal discipline, Jamaica’s fiscal performance is now stronger than comparators. The figure shows that despite the decline in public debt in relation to GDP, debt still remains high, suggesting the need for continued improvements in public finances.

The fiscal improvements described above have resulted in an upgrading in credit market ratings since Jamaica’s default ranking in 2014, although sovereign debt remains classified as speculative non-investment grade (Figure 8.14). The scenario built for Jamaica suggests that with

Figure 8.14 Jamaica: Credit Ratings and Debt-to-GDP Ratio



Sources: IMF, World Economic Outlook database and the Trading Economics website (<https://trading-economics.com/country-list/rating>).

Note: TE: Trading Economics.

recent policies supported by international and regional institutions, the fiscal position would show a small overall surplus. A deterioration in the terms of trade would have a very small adverse effect (widening the estimated fiscal deficit by only an additional 0.2 percent of GDP).

Suriname

Suriname's economy is dominated by the mining sector, with exports of oil and gold accounting for approximately 27 percent of government revenue. This makes public sector finances highly vulnerable to mineral price volatility. The worldwide drop in international commodity prices and the recent cessation of alumina mining in Suriname significantly reduced government revenue during the past few years.⁹ At the same time, private sector investment fell significantly. Economic growth declined annually from about 5 percent in 2012 to a negative 10.4 percent in 2016 and a further contraction in 2017.

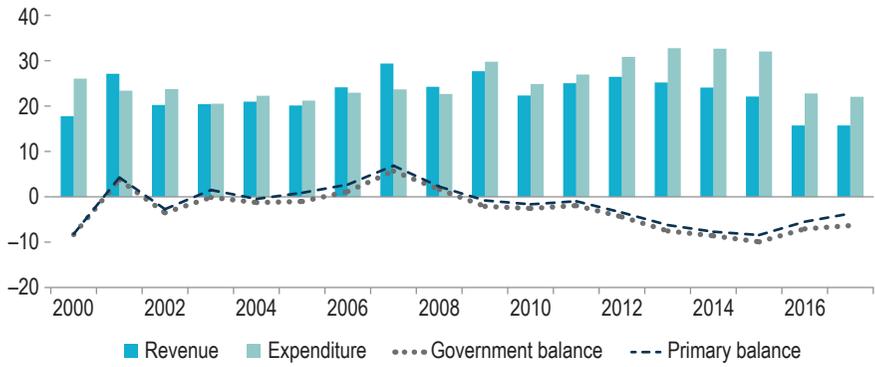
Government revenues began to slow in 2011-2012, but government expenditures continued to rise, and by 2012 the government faced the largest deficit since 2000, at more than 6 percent of GDP (Figure 8.15). The government increased spending without increasing revenues, in the context of an election cycle, and as a result the fiscal accounts deteriorated. As commodity prices declined, fiscal performance weakened further. With few financing options, the government resorted to central bank financing.

As this approach became unsustainable, Suriname began implementing adjustment measures in September 2015, including a 20 percent devaluation of the currency in November 2015 followed by a floating exchange rate system after March 2016. By the end of 2016 the value of the currency had declined by half against the U.S. dollar. This, together with hikes in electricity tariffs, caused prices to increase by 55.5 percent year-over-year in December 2016. The adjustment effort was supported by a 24-month Stand-By Arrangement with the IMF in mid-2016, as well as financing commitments from the Caribbean Development Bank, the Inter-American Development Bank, and the World Bank. The government reined in spending, cutting the fiscal deficit from the equivalent of more than 13 percent of GDP (annualized) during January-July 2015 to below 4 percent of GDP (annualized) during August-December 2015.

By mid-2016, however, a deepening recession led the government to stall or even reverse progress on several policy reforms, although preparations

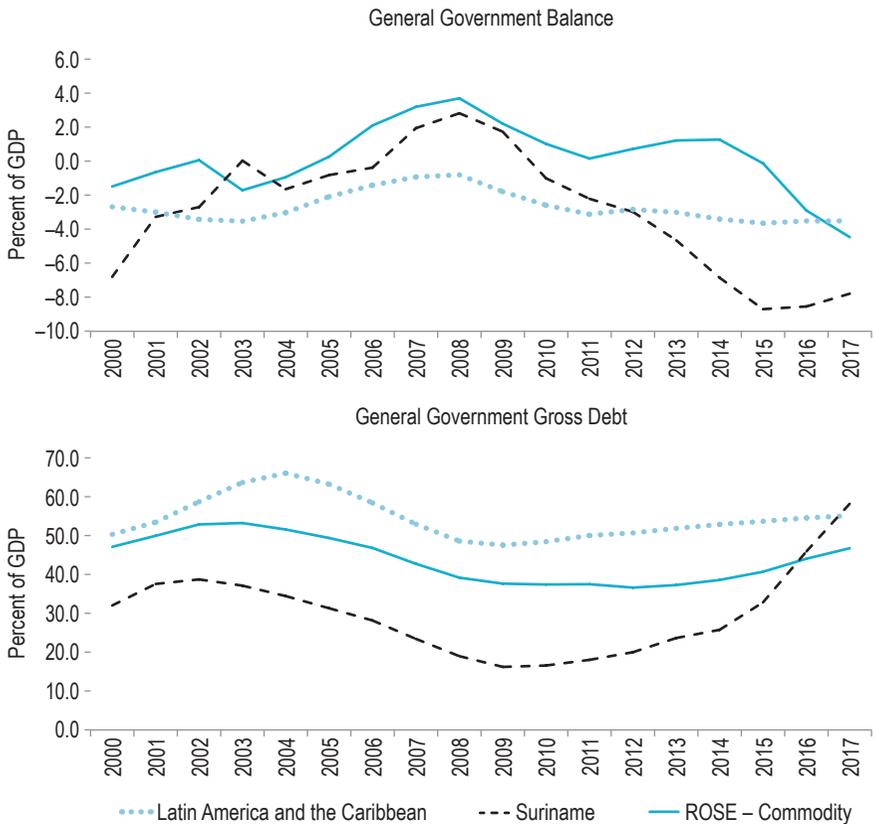
⁹ After 99 years of operations, a major U.S. aluminum company discontinued its activities in Suriname.

Figure 8.15 Suriname: Fiscal Performance (percent of GDP)



Source: IMF, World Economic Outlook database and published documents.

Figure 8.16 Suriname: General Government Balance and Debt Compared to Other Country Groups (percent of GDP, three-year rolling average)



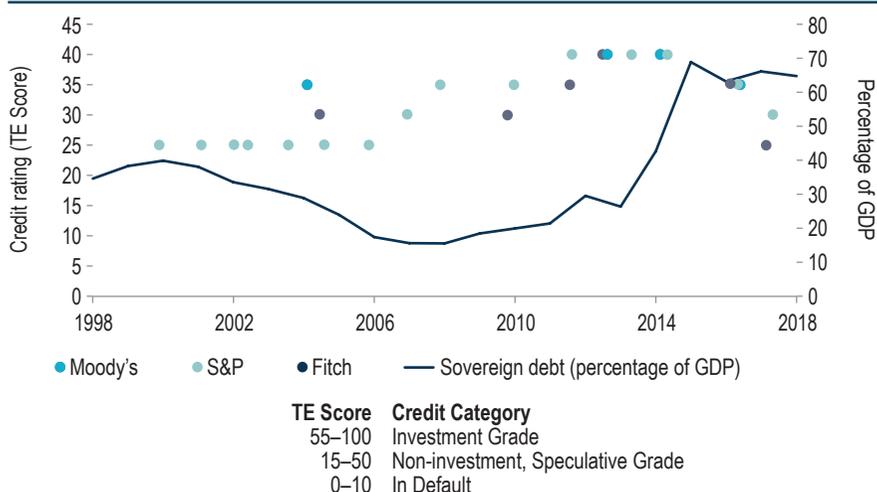
Sources: IMF (2017); World Bank, World Development Indicators; and authors' estimates.

continued for introduction of the value-added tax (VAT). Spending was raised, as fuel and other subsidies were increased, although the overall deficit narrowed to 6 percent of GDP in 2017. The debt-to-GDP ratio, which had been close to 15 percent of GDP in 2008–2009, rose to nearly 70 percent by 2016. The fiscal position needs to be strengthened by eliminating subsidies, introducing the VAT, controlling the wage bill (in part by reducing the high level of public sector employment, plagued by duplication and ghost workers), and creating space for priority social expenditure and investment. Institutional reforms to bolster fiscal discipline are also required.

Figure 8.16 shows the developments in the fiscal accounts and public debt compared to Latin America and the Caribbean and commodity-dependent ROSE. It shows the deteriorating fiscal performance compared to the region and ROSE, with debt levels exceeding those of comparators.

Suriname has been in the non-investment rating range for at least the last 20 years (Figure 8.17). Its rating improved during the commodity boom years, but fell in the recent past as the authorities weakened their commitment to an adjustment program and increased the country's public sector imbalances. The scenario built for Suriname suggests that with trend policies, and by moving away from the current serious imbalances, the fiscal position could show an initial improvement to a steady deficit of 3.5 percent of GDP, even with the expected acceleration in growth

Figure 8.17 Suriname: Credit Ratings and Debt-to-GDP Ratio



Sources: IMF, World Economic Outlook database and the Trading Economics website (<https://trading-economics.com/country-list/rating>).

Note: TE: Trading Economics.

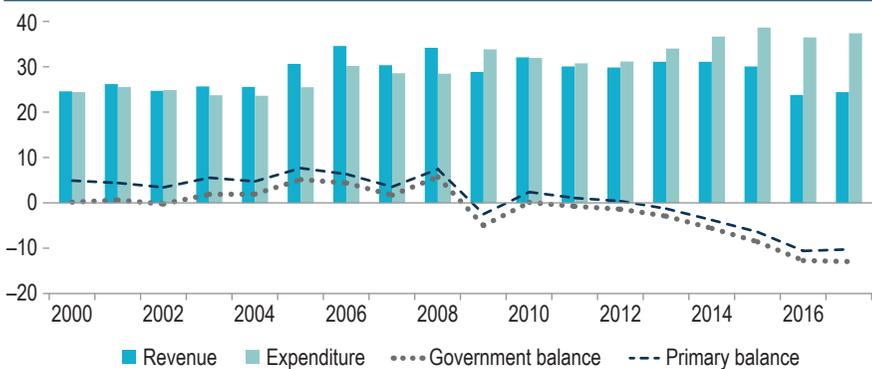
generated by the new mining and oil investments. However, recent events suggest that the outlook could be significantly weaker if exports do not materialize and/or if public expenditures are not reined in. A deterioration in the terms of trade would have a small additional adverse effect (0.6 percent of GDP) on the budget. For debt to decline from current elevated levels, continued tight fiscal policy and policy reforms to foster growth are needed.

Trinidad and Tobago

Trinidad and Tobago is the largest and one of the richer countries in the Caribbean thanks largely to petroleum and natural gas production and processing. The economy benefitted from the sustained rise in world fuel prices and new natural gas findings through 2013–2014, which had been temporarily interrupted during the onset of the global financial crisis. However, economic performance weakened following the crisis, subsequently aggravated by the sharp decline in the terms of trade experienced in late 2014.

Public finances deteriorated drastically after 2008, as government expenditure exceeded revenues by growing amounts (Figure 8.18). While fiscal policy remained cautious in the early 2000s, the considerable increases in energy export earnings and associated revenues led the government to expand expenditure significantly through 2008. The global financial crisis led to a major drop in revenue, but government spending proved difficult to contain and deficits increased. From FY 2007–2008 to FY 2014–2015 subsidies and transfers and public sector wages and salaries increased by nearly 50 percent (to 18.8 percent of GDP and 6.2 percent of

Figure 8.18 Trinidad and Tobago: Fiscal Performance (percent of GDP)



Source: IMF, World Economic Outlook database and published documents.

GDP, respectively), and government spending on goods and services rose from 3 percent of GDP to 5.2 percent. The large increases in subsidies and transfers reflected the growth of social programs and the proliferation of government agencies, which has led to overlapping mandates and coordination challenges. Almost all major categories of spending are subsidized, including housing, education, health care, water and sanitation, transportation, fuel, and energy. Transfers also help to fund the debt service and infrastructure projects of SOEs. The collapse of world oil prices, together with limited expenditure cuts, caused the overall government deficit to reach 12 percent of GDP in 2016 (on the basis of IMF data).¹⁰ However, the deficit was estimated to have narrowed modestly in 2017 to 11 percent, as the government took measures to correct the existing imbalance by reforming the energy tax regime, reducing fuel subsidies, and boosting non-energy revenues, while engaging in expenditure rationalization efforts.¹¹

The prudent fiscal policies and growing oil revenue through 2008 had helped reduce public sector debt from more than 50 percent of GDP in the 1990s to just 17 percent in 2006. But this trend was reversed following the 2008 global financial crisis as a result of growing deficits and weak economic growth. Public debt rose to 55 percent of GDP in 2017, a level still deemed sustainable. Within these totals the government is not the primary debtor but carries the risk of contingent liabilities for the equivalent of 16.3 percent of GDP, due to debt contracted by SOEs and statutory authorities.

Offsetting the noted levels of debt, the Heritage and Stabilization Fund (HSF) held foreign assets in excess of US\$5.75 billion (some 20 percent of GDP) as of end-2015. The HSF was created in 2007, with two key objectives: (1) to help to insulate fiscal policy from swings in world energy prices; and (2) to address intergenerational equity considerations by accumulating savings from the exploitation of the country's exhaustible energy resources for future generations. The HSF was only tapped in 2016, when the government withdrew US\$1 billion, and in 2017, when it withdrew a further US\$500 million. If the assets of the HSF were deducted from the public debt, net public debt would have been 35 percent of GDP in 2017.

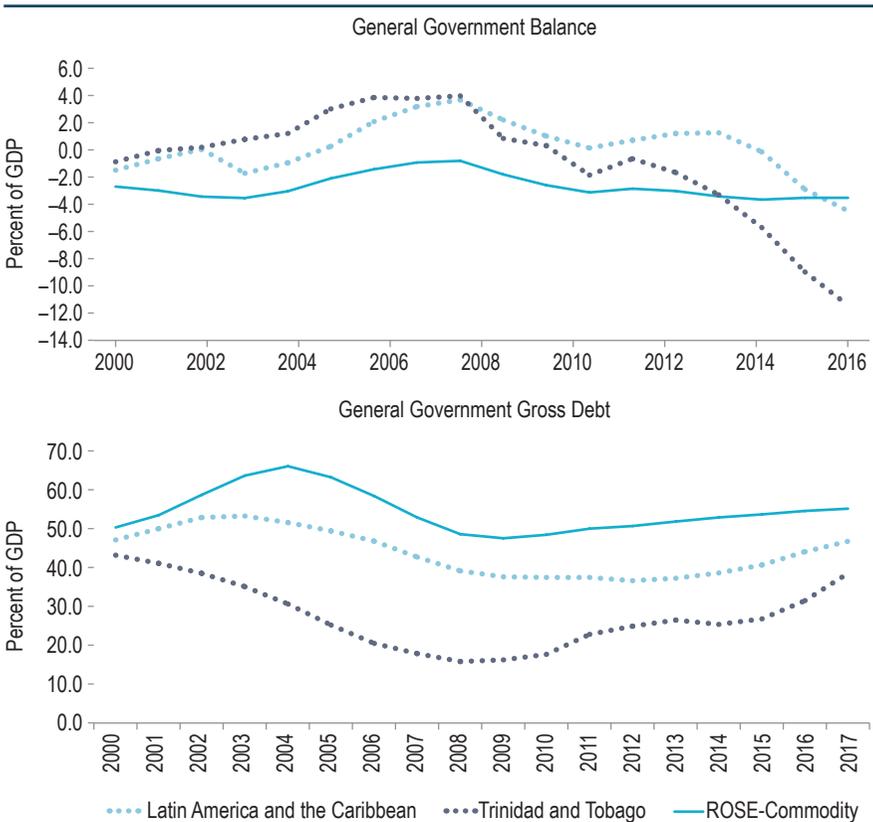
¹⁰ There are discrepancies between the IMF and central bank figures, mainly due to the use of different accounting standards, which leads the central bank to include asset sales and special dividends as revenues. As a consequence, central bank fiscal data are more favorable, showing a deficit of only 6 percent for FY 2016.

¹¹ Based on the most recent IMF Article IV Consultation Staff Report (November 2017).

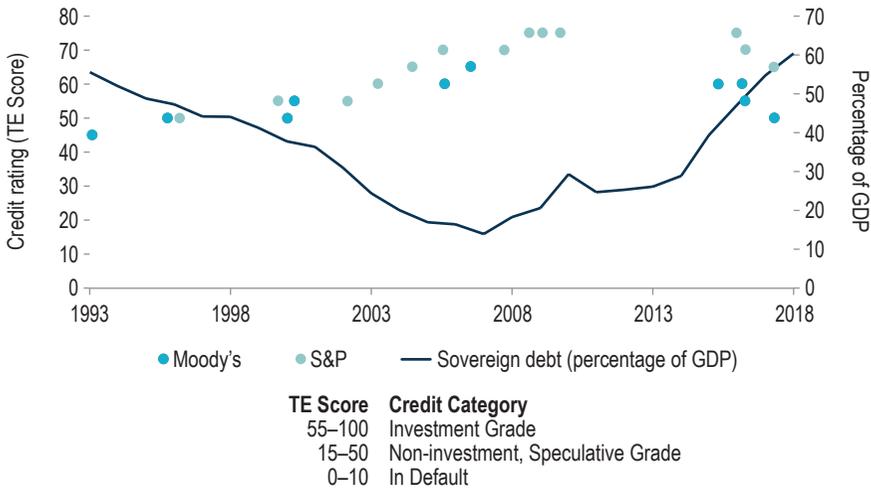
By making use of these resources, the government recognizes the considerable challenges created by the collapse in world energy prices. In this context, it has taken important steps to generate additional revenue and curtail spending. These steps included a widening of the VAT tax base, a reduction in fuel subsidies, and expenditure cuts. Recently, the government announced plans for structural reforms and the sale of assets.

Figure 8.19 shows the developments in the fiscal accounts and public debt compared to Latin America and the Caribbean and commodity-dependent ROSE countries. It shows that after years of solid fiscal results, fiscal performance worsened sharply compared to comparators, much in a similar pattern as Suriname. As a consequence, Trinidad and Tobago

Figure 8.19 Trinidad and Tobago: General Government Balance and Debt Compared to Other Country Groups (percent of GDP, three-year rolling average)



Sources: IMF (2017); World Bank, World Development Indicators; and authors' estimates.

Figure 8.20 Trinidad and Tobago: Credit Ratings and Debt-to-GDP Ratio

Sources: IMF, World Economic Outlook database and the Trading Economics website (<https://trading-economics.com/country-list/rating>).

Note: TE: Trading Economics.

moved from a very low ratio of government debt to GDP before the financial crisis of 2008–2009 to a ratio of almost 40 percent of GDP. In addition, state-owned enterprises accumulated considerable debt levels, as noted above.

Despite recent downgrades, Trinidad and Tobago's significant savings in its HSF have helped retain investment-grade ratings, although at relatively low levels (Figure 8.20). The scenario built for Trinidad and Tobago suggests that with policies that incorporate the trends of the last 15 years, the fiscal position would show a major improvement followed by growing deficits, which would increase by nearly 2 percent of GDP from 2017 to 2030. This would lead to potentially serious debt sustainability problems in the future, aggravated if the current policies persist. A weakening in the terms of trade would have the adverse effect of widening the projected deficits further by 1.2 percentage points of GDP, reflecting the importance of fuel in the country's fiscal performance.

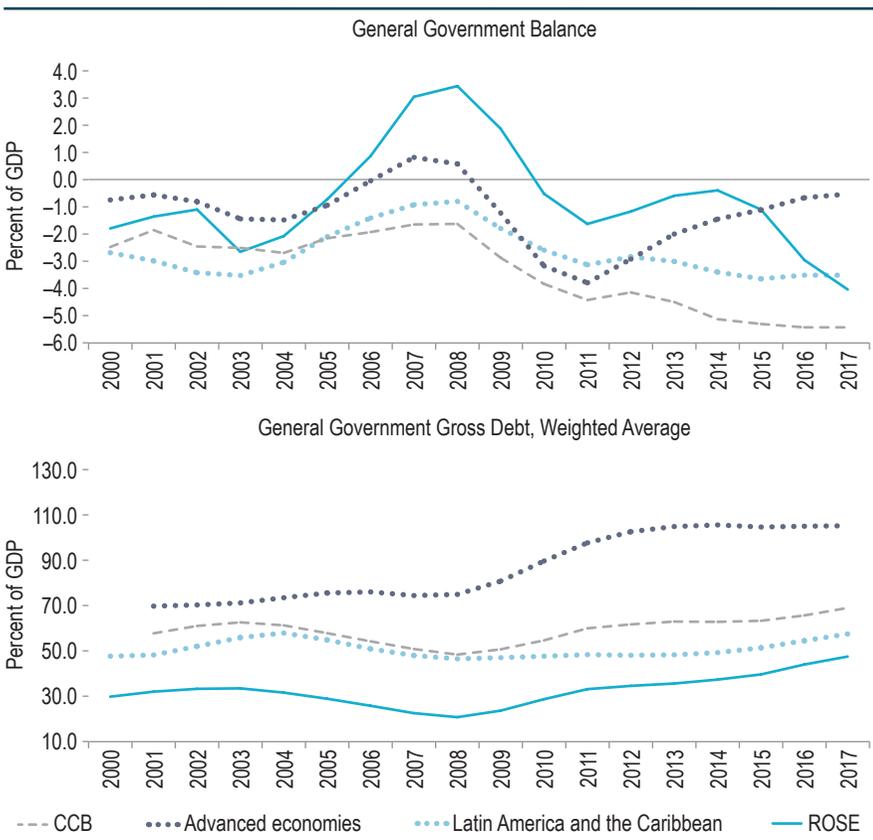
8.1.4. Fiscal Performance Compared to Advanced Economies, Latin America and the Caribbean, and the Rest of the Small Economies of the World

As described above, the performance of the six Caribbean countries has varied significantly, but there are common elements, particularly when

compared to other regions. The performance of Caribbean countries has been weaker than that of advanced economies, Latin America and the Caribbean, and ROSE. The figures below are estimated as simple averages for all the regions in order to provide equal weight to each country independent of size.

The primary and overall fiscal balances of Caribbean countries underperformed the other groups of countries, with the balances deteriorating by some 3 percentage points of GDP since 2008. Correspondingly, the ratio of public debt to GDP has grown rapidly and is showing levels well above those of Latin America and the Caribbean and ROSE (Figure 8.21). While debt had risen rapidly for advanced economies, this trend changed as these countries started to grow faster and fiscal performance started to improve, while those of Caribbean countries continued to weaken. All in

Figure 8.21 CCB General Government Balance and Debt Compared to Other Country Groups (percent of GDP, three-year rolling average)



Sources: IMF (2017); World Bank, World Development Indicators; and authors' estimates.

all, the comparison provides a worrisome image for the region, and clearly calls for prompt actions on policy.

8.2. The Role of Institutions in Enhancing Public Fiscal Performance

The previous section presented a sobering review of public finance developments in Caribbean countries. Perhaps the most salient statistic is the average level of public debt of these countries, which rose to the equivalent of 73.5 percent of GDP in 2016–2017,¹² compared with 52 percent for the 164 emerging and developing economies. Moreover, the public debt of Jamaica and Barbados were the seventh and 10th highest in terms of GDP among all of the world's emerging and developing economies in 2016.

As noted in the previous section, procyclical fiscal policies in boom times, especially among commodity exporters, and expansionary countercyclical policies in recession times—to ameliorate the effects of the global financial crisis of 2008 and declining terms of trade in more recent years, generally in the absence of fiscal space—accelerated the increase in public debt. However, as indicated by Wright, Grenade, and Scott-Joseph (2017), in addition to fiscal overexpansion, public debt has grown largely due to poor public financial management, especially budget transparency and credibility and poor public sector management, as well as the absence of binding rules geared toward entrenching fiscal discipline. Weak parliamentary oversight and the absence of independent fiscal institutions are additional factors. Moreover, and fundamentally, poor public sector governance and weak institutions explain most of these vulnerabilities.

More generally, poor fiscal performance is also attributable to weaknesses in the Caribbean countries' medium- and long-term national planning capacity, program budgeting, and financial management instruments. These weaknesses resulted in a limited focus on strategic objectives and control over public spending, and faulty or absent evaluation of spending effectiveness, incentives for achieving institutional objectives, and evaluation systems. Moreover, these weaknesses are heightened by inadequate availability or use of information on which to base sound policy decision-making and results-oriented management.

Ideally, fiscal policy should be consistent with debt sustainability, resilience in the face of shocks, and macroeconomic stabilization. But

¹² This average ratio would have been significantly higher in the absence of the major debt reduction that Guyana obtained under the HIPC initiative in the early 2000s, when the ratio of debt to GDP had reached 130 percent.

in reality, fiscal policy in Caribbean countries is influenced by distorted incentives. These incentives reflect, inter alia, “common-pool” problems:¹³ interest groups lobbying for spending on their preferred public goods and entitlements without consideration of the full budgetary costs and, concurrently, concerns about the electoral cycle leading policymakers to accommodate such spending increases. These incentives reflect, fundamentally, a weak political commitment to fiscal discipline and/or an insufficient understanding of the long-run constraints on fiscal policy. In this context, rules and processes aimed at making these constraints more explicit and binding would be circumvented, ignored, or simply abandoned over time. Put differently, procedural checks and balances in the budget, in the absence of “deeper” checks and balances in the political system, are not effective.

By contrast, many empirical studies show that countries with a strong commitment to fiscal discipline, supported by sound institutions and good financial management processes, show strong performance. For instance, Dabla-Norris et al. (2010) provide evidence that sound budget institutions promote fiscal discipline, as measured by higher primary balances and lower debt, and are relevant for shaping less procyclical responses to the fiscal cycle in low-income countries, including during the 2008 crisis. The analysis suggests that the most significant institutions are those related to planning and implementing the budget, and to the sustainability, comprehensiveness, and transparency of the budget process.

Therefore, the remainder of this section describes in some detail the institutional weaknesses of Caribbean countries in terms of public financial management, fiscal management, fiscal rules, and public debt management.

8.2.1. *Public Financial Management*

Public financial management is one of the five pillars of the Management for Development Results model.¹⁴ Public financial management relates to the way governments manage public revenue and expenditure, and the immediate and medium-to-long-term impact of these actions on the

¹³ Such as the overexploitation of natural resources in the absence of clearly defined property rights.

¹⁴ The model seeks to define the results that governments expect to achieve. It is based on the public policy management cycle, which includes five pillars: strategic planning, budgeting for results, public finance management, monitoring and evaluation, and program and project management.

economy or society. Public financial management deals with both process (how governments manage) and results (short- and long-term implications of financial flows relative to the government objectives). In this sense, functional public financial management systems should promote prudent fiscal decisions, credible budgets, reliable and efficient resource flows and transactions, and institutionalized accountability.

In general terms, the evidence shows that public financial management processes and systems of Caribbean countries are weak (see Appendix 3 for detailed analyses of each Caribbean country). The 2013 index for the public financial management pillar of the Management for Development Results model ranked Caribbean countries among the nine lowest countries in Latin America and the Caribbean, despite progress made after 2007 (Kaufmann, Sanginés, and García 2015). Public financial management processes and systems have not contributed to sound public resource management in the context of budget formulation, execution, and oversight, budget credibility, budget transparency, or good financial governance. Some of the existing processes or systems over-emphasize form and under-emphasize functionality. Moreover, systems in Caribbean countries demonstrate some capacity for allocating resources in accordance with priorities, but important weaknesses still undermine the effectiveness and integrity of spending quality and financial reporting.

Most resource-rich developing economies in particular face unique economic and fiscal challenges. They tend to have poor public management because commodity export booms tend to weaken state institutions and empower interest groups.¹⁵ Further, these countries often have procyclical fiscal policies, which typically lead to unstable economic performance, as revenue fluctuates in line with commodity price cycles.¹⁶ Thus, strong governance and institutions, as well as clear fiscal rules and stabilization-saving funds are central to manage revenues and expenditures over the commodity cycle in order to reduce fiscal cyclicity.

While in most Caribbean countries public financial management processes and systems have been weak, more recently Jamaica and Suriname—with the support of regional development institutions and the IMF—have introduced important improvements to their public financial management systems and processes. Other countries—The Bahamas, Guyana, and Trinidad and Tobago—have advanced in some specific areas.

¹⁵ Botswana and Chile are among the exceptions.

¹⁶ Typically, economic activity and external and fiscal balances deteriorate (improve) during commodity price downswings (upswings).

The sections below highlight key aspects of public financial management across different Caribbean countries.¹⁷

Budget Credibility

Following the global financial crisis of 2008–2009, budgets in Barbados and Suriname were no longer good predictors of actual revenue and expenditure. Similarly, the budget of The Bahamas' capacity to inform deviations in the mix of expenditures relative to what was planned has deteriorated. Reforms in Guyana helped reduce the gap between budgeted and actual spending, while reforms in Jamaica reduced revenue and expenditure gaps. However, credibility has been undermined in Barbados, Suriname, and Trinidad and Tobago by poor information on arrears and extra-budgetary operations. For example, spending through informal procedures led to unreported arrears in Trinidad and Tobago.

Comprehensiveness and Transparency

Most of the required information on the basis of best practices is presented in the budget documentation, and access to fiscal information is reasonable. However, information is lacking about extra-budgetary expenditures or funds in The Bahamas. In Suriname, main autonomous agencies and SOEs report their budget execution, liquidity position, and financial statements. In Barbados, capital expenditure is reported in totals only, hampering comparisons over time. By contrast, Jamaica and Suriname have made improvements in their budget formulation and implementation processes. This includes the timeliness of budget preparation, its comprehensiveness and reporting (including on extra-budgetary funds), and budget classification, which is now compatible with international standards.

Budget documentation in Guyana and Trinidad and Tobago is extensive, with complete economic and financial information. In Guyana, budget allocations and transfers from central to subnational governments follow a set of criteria and rules, but there is no consolidation of fiscal accounts by sector. In Barbados, statutory bodies do not meet the obligation to present budget estimates and audited accounts. In Suriname, procurement information is provided to the public. By contrast, procurement in The Bahamas, Guyana, Jamaica, and Trinidad and Tobago remains opaque,

¹⁷ Public financial management evaluation follows the Public Expenditure and Financial Accountability (PEFA) methodology. See Appendix 3 for a more detailed description of each country's public financial management.

largely as a result of non-competitive tendering, lack of qualified procurement staff, insufficient information on procurement processes, and no information on awarded contracts.

Policy-Based Budgeting

The fiscal deterioration of the last decade reflects weaknesses in the processes of policy, planning, and budget execution. Most countries did not have a detailed medium-term framework, which hampered planning decisions.¹⁸ Moreover, meaningful discussions are not possible on objectives and outputs in the absence of stated measured results. Guyana, and more recently Jamaica, Suriname, and Trinidad and Tobago, introduced a five-year rolling framework, including for debt sustainability analysis purposes, while Barbados includes projections for a second year, which serve as the basis for that year's budget. In Trinidad and Tobago, recurrent and investment expenditure are still two separate decision processes. Guyana is transitioning to a more formal and structured programmatic and results-based system.

Predictability and Control of Budget Execution

Tax legislation and procedures in Barbados and Trinidad and Tobago are comprehensive and clear. However, tax liability assessments and exemptions in Barbados and Suriname are still subject to discretionary powers of different government entities. The Bahamas lacks enforcement of its rules regarding tax liability assessments and exemptions. By contrast, in Jamaica, tax incentives and discretionary waivers were reduced and replaced with a rules-based, transparent framework. However, Jamaica is affected by inaccurate taxpayer data, low on-time filing and payment rates, delays in the

¹⁸ Indeed, as shown in Chapter 5, medium-term fiscal frameworks have been increasingly adopted worldwide (Filc and Scartascini 2010; World Bank 2012; and Vlaicu et al. 2014). World Bank (2012) shows that the adoption of medium-term fiscal frameworks improves fiscal balances, reduces overall expenditure volatility and increases the share of public expenditures in human capital enhancement areas like health. The study also shows that complementing multiyear budgeting with performance targets by sector (medium-term performance frameworks) improves the cost-effectiveness of public health expenditures. Vlaicu et al. (2014) illustrate that medium-term fiscal frameworks improve both total and primary budget balances. They also show that health expenditure volatility is reduced when fiscal frameworks establish both the aggregate resource envelope and the allocation of spending across sectors, programs and agencies. Finally, they argue that health sector technical efficiency is positively affected when medium-term performance frameworks are in place.

payment of refunds, and low-quality audits. In Guyana, the lack of effective tax revenue forecasting tools, enforcement capacity to apply penalties, and follow-up of delinquencies render the system voluntary.

Internal audit of expenditure remains relatively underdeveloped. In Suriname, internal audit is carried out following professional standards. Expenditure commitment control procedures exist and are partially effective, but there is usually no follow-up by ministries on internal audit recommendations. In The Bahamas, Barbados, and Guyana, effective internal controls are limited, possibly because internal auditors do not have the resources needed to carry out their job.

Accounting, Recording, and Reporting

In The Bahamas, annual financial statements do not meet international standards in terms of presentation or disclosure. Similarly, The Bahamas has experienced problems with reconciliations, and although Auditor Generals highlighted weaknesses and breaches of the rules, response efforts have been limited, reflecting lack of accountability and low regard for the auditors' opinion. While key budget reports are prepared, public access and financial information are rather limited as well in The Bahamas. By contrast, in Barbados, monthly budget execution reports are prepared regularly and sent to Parliament within about four months. These reports are then available to the public.

Guyana improved accounting, recording, and reporting with the adoption of the Integrated Financial Management and Accounting System, and further efforts are expected to attain real-time connectivity among all government agencies. Government financial statements are generally not consolidated.

External Scrutiny and Audit

The Office of the Auditor General in Trinidad and Tobago meets most of the independence standards set by the International Organization of Supreme Audit Institutions for audit institutions. The coverage of annual audits varies by country. They cover the whole central government in Barbados, three-quarters of total expenditure in Trinidad and Tobago, and 60 percent of expenditure in Suriname. Audit reports and audited financial statements are submitted to the Parliament according to the law in The Bahamas, Suriname, and Trinidad and Tobago, but with long delays in Barbados and Guyana. However, as noted above, most countries do not show systematic and timely follow-up on auditor general findings (The Bahamas, Jamaica,

Suriname, Trinidad and Tobago). The effectiveness of parliamentary budget oversight in Barbados, Guyana, Jamaica, Suriname, and Trinidad and Tobago is typically constrained by the limited time allocated to this function, as these reviews are based on almost finalized estimates and changes are no longer possible when the reviews are conducted.¹⁹

Caribbean countries have weak monitoring and evaluation functions, ranking in the bottom half among Latin American and Caribbean countries (Kaufmann, Sanginés, and García 2015). Monitoring and evaluation functions are essential to results-based management, as they provide information about the effects of government actions and the achievement of expected outcomes. In addition to qualified staffing, effective monitoring and evaluation systems require good and timely data.

8.2.2. Fiscal Management

Fiscal responsibility legislation, which would clearly specify fiscal performance targets for the medium term (typically overall budget deficits, but also primary balances) and debt ceilings, is associated with greater transparency and accountability. It also serves as an effective disincentive to public financial mismanagement and provides appropriate sanctions. The absence of fiscal responsibility legislation in the Caribbean, except for Jamaica since 2014, tends to lead to larger public deficits. Similarly, the absence of a multi-year fiscal framework prevents governments from having a view of the paths of revenue, expenditure and overall balances over the medium term, thus hampering debt outlook and management.

Most Caribbean countries, if not all, do not follow performance- or results-based budgeting practices. This constrains policymakers from having the tools to match inputs and outputs and to provide the incentive structure that results in effective departmental “ownership” of sectoral plans and budgets, and thus budget implementation that is consistent with strategic development objectives.

Some countries have not yet adopted a Single Treasury Account. Its absence results in less efficient use of government cash and may lead to unnecessary temporary borrowing and cost. Its absence also makes it difficult for the Auditor General and Parliament to carry out their oversight functions effectively.

Public ownership of corporations has often had significant negative consequences for fiscal performance because of mismanagement,

¹⁹ In some cases, parliamentary committees may not be able to contribute to the content and quality of the budget.

overstaffing, and mispricing. Public sector employment and salaries have often been politicized and entail unsustainable commitments. Similarly, cost overruns on infrastructural projects and procurement irregularities have undermined budget performance.

Fiscal management in the three Caribbean commodity exporters until recently had been procyclical and resulted in policies inconsistent with economic stability and sustained growth. Trinidad and Tobago created its Heritage and Stabilization Fund in the late 2000s, and accumulated considerable assets in the fund and reduced its outstanding debt, limiting the impact of increased government revenue associated with the oil and gas boom. However, it also engaged in major increases in current spending that have proved difficult to reduce during the downturn of the commodity price cycle and eventually led to an increase of public debt. Suriname has just created a Savings and Stabilization Fund. These funds also seek inter-generational equity in the context of the exploitation of exhaustible resources. Guyana's development partners have encouraged it to adopt a similar fund to save some gold export earnings as well as earnings from oil production envisaged for later in this decade.

8.2.3. Fiscal Rules

Fiscal performance in Caribbean countries, especially over the past two decades, suggests a lack or weakness of fiscal rules, or that they are poorly enforced and thus bypassed. This is generally reflected in deficient fiscal discipline and growing public debt, poor budget credibility, and procyclical fiscal policy. Put differently, fiscal rules address the deficit bias or the "common pool" problem discussed above, as they help contain expenditure pressures and minimize negative externalities.

Fiscal rules are medium-to-long-term constraints on fiscal policy through numerical targets/limits/floors that are set on one or more government budgetary aggregates (expenditure, revenue, budget balance, and public debt) and bound in legislation and fiscal arrangements.²⁰ The observance of such rules requires an institutional framework that produces a well-designed and strong budgeting process and a set of institutional checks and balances.²¹ While a solid commitment to fiscal discipline

²⁰ The seminal work on the principles to be observed when formulating fiscal rules is Kopits and Symansky (1998).

²¹ However, fiscal rules and medium-term planning constraints alone may be insufficient to instill fiscal discipline because in countries with weak institutional frameworks and budgeting processes, rules can be circumvented in many ways (Alesina and Perotti 1998).

backed by strong fiscal institutional frameworks and budgeting processes may not require numerical rules, the force of legal constraints and associated accountability raise the likelihood of stronger results, as noted below.

The Caribbean commodity-dependent countries (Guyana, Suriname, and Trinidad and Tobago) could benefit significantly by anchoring fiscal policy to a transparent rules-based framework. One such framework would set long-term ceilings on government expenditure based on a level of revenue associated with an expected long-term price of their main commodity exports. This would de-link the budget and the economy from the volatility of commodity revenue, stabilizing the overall fiscal balance throughout the commodity price cycle. It would therefore prevent procyclicality, and introduce a considerable degree of budget credibility, while promoting a stable environment for private sector activity and economic growth.

Several econometric studies find that fiscal rules are associated with stronger fiscal performance. These studies mostly cover European countries (Debrun et al. 2008; Deroose, Moulin, and Wiertz 2006; Debrun and Kumar 2007) and only a few cover emerging economies (Kopits 2004; Corbacho and Schwartz 2007). The main findings are that (1) tighter and more encompassing fiscal rules are correlated with stronger cyclically adjusted primary balances in European countries; (2) fiscal rules bolster fiscal consolidation efforts in small states; (3) budget balance and debt rules have contributed to better budgetary outcomes than expenditure and revenue rules; (4) rules covering wider levels of government have been associated with more fiscal discipline and credibility; and (5) rules supported by legislation and strict enforcement appear to have a beneficial impact on fiscal performance.

More recently Alberola et al. (2016) conducted a similar study on a sample of eight Latin American and Caribbean countries (representing 80 percent of the region's GDP, and including Jamaica). The study shows that most of these countries have strengthened their fiscal frameworks through the use of, among other things, fiscal rules. It shows that countries with fiscal rules with wider coverage (general government versus central government), and supporting procedures (e.g., an independent body that monitors implementation or suggests the appropriate set of assumptions) outperform others in terms of stronger countercyclical (i.e., stabilizing) fiscal stances. The study also finds that budget balance rules and structural rules are correlated with a more countercyclical fiscal stance. Specifically, the study's robust results show that countries with fiscal rules have behaved more countercyclically than countries without rules during the last two decades.

However, as the authors of these studies appropriately note, the positive correlation between fiscal rules and fiscal performance does not necessarily reflect causality because the adoption of fiscal rules may be

a consequence rather than a cause of a political commitment to better fiscal practices and discipline.²² As international experience has shown, fiscal rules cannot substitute for a strong commitment to fiscal discipline, as these rules can be circumvented, ignored, or simply abandoned over time.

The ideal fiscal rule is one that is transparent, flexible, and implementable. Indeed, fiscal rules must have escape clauses that provide sufficient flexibility to enable policymakers to respond appropriately to unforeseen and significant temporary shocks (e.g., natural disasters, external shocks, and financial crises). These clauses should be well specified to avoid ambiguity. Flexible rules would reduce the need for frequent modifications to the rules, which could damage confidence in the rule itself and in the policymakers' intentions to sustain fiscal policy (Corbacho et al. 2012).

Rules need to be supported by independent fiscal institutions (or councils), suggesting that fiscal rules alone do not ensure fiscal discipline. Caribbean countries have lacked independent fiscal institutions, the principal function of which is to analyse and assess the budget bill or any other legislative proposal in the fiscal area, including its consistency with fiscal rules (if any), prior to enactment (Kopits 2011).²³ Similarly, Caribbean commodity-dependent countries could benefit considerably from setting up independent advisory councils that would professionally estimate the above-mentioned long-term commodity export prices, thereby enhancing the credibility of budgetary revenue estimates.

8.2.4. Public Debt Management²⁴

Debt management in Caribbean economies is currently weak, and most countries do not have an explicit debt management strategy. While Caribbean countries have similar formal procedures regarding debt based on their colonial past, these are not adequate for current circumstances.

Most of the Caribbean countries have their public debt management functions dispersed across a number of institutions, as several ministries and agencies may be involved in and responsible for public debt management functions. Borrowing programs are often implemented by institutions such as the Ministry of Foreign Affairs, Ministry of Finance, planning departments,

²² Reverse causality could also bias the results, as fiscal rules could be adopted to “lock in” gains from consolidation.

²³ More specifically, an independent fiscal institution performs real-time costing and forecasting to ascertain the macro-fiscal consequences of the budget bill over a short-, medium-, and long-term horizon.

²⁴ This section is based on Nicholls (2014).

the treasury, and the central bank. Institutional responsibilities for borrowing are often assigned by source of funding (domestic or external) and by instrument type (direct loans or debt securities). The institutional framework is fragmented, resulting in limited coordination with macroeconomic policies. Borrowing plans are not fully articulated, and there is only limited practice of comprehensive debt recording and reporting to Parliament. The absence of modern public debt management legislation undermines the transparency and accountability of fiscal and debt management operations.

With no legal requirement to account for any discrepancy between outturn and stated objectives, and without provisions for transparency and accountability in debt management, government performance cannot be easily evaluated against quantifiable benchmarks. This increases the risks of excessive borrowing. In addition, the absence of clearly delineated institutional roles and responsibilities contributes to uncoordinated debt management operations.

Contingent liabilities represent a significant risk to fiscal and debt sustainability and are not adequately integrated into databases for external debt. Important liabilities originate outside of the central government and have been the main contributor to debt in the Caribbean over the last two decades. Many contingent liabilities have arisen from operations of public enterprises that do not deliver public goods. These operations undermine the integrity of the budget process, hampering credibility and transparency. Sound debt management requires close monitoring of explicit contingent liabilities, especially government guarantees and on-lending arrangements. Total explicit contingent liabilities in the Caribbean are conservatively estimated to average 19 percent of GDP, based on published data. Prudent debt management also requires monitoring of conditions that could trigger additional contingent liabilities, such as possible financial rescue associated with financial sector or public enterprise difficulties.

A major concern is the traditional use of cash accounting, where a liability is registered when cash is paid rather than when it is incurred. This type of accounting facilitates the accumulation and consequent non-recognition of payment arrears, leading to the under-reporting of true fiscal deficits and public debt increases.

Debt Management Practices in the Caribbean

Institutional framework. Apart from Jamaica and Suriname, which have a single debt management law, the legal framework for issuing and managing debt is fragmented. Debt is issued with a specific purpose, and under different laws. While these laws generally provide the minister of finance with the sole authority to borrow, they may or may not prescribe specific

borrowing limits. Furthermore, a fragmented organizational framework and low staff capacity (due to small staff size and office space, limited training, and high turnover) hinder the outcome.

Coordination. In most Caribbean countries, the coordination mechanisms between debt management and fiscal and monetary policies are either limited or very weak. Some countries, including Barbados and Jamaica, have recently created debt management committees to address issues in this area. At the domestic level the coordination mechanisms remain underdeveloped.

Debt management strategy. Debt management frameworks are inadequate, as only Jamaica and Barbados have explicit debt management strategies.²⁵ Even where these strategies exist, they are generally not comprehensive and not focused on a cost/risk analysis. In addition, even though Parliament is the ultimate authority on borrowing, some countries have no explicit requirements for reporting to Parliament or for the conduct of audits.

Borrowing activities. Government debt markets remain underdeveloped, particularly secondary markets, which are limited and inefficient, although secondary markets have been developed in Barbados and Jamaica, and auctions (including the participation of primary dealers) exist in Jamaica and Trinidad and Tobago. Further, most borrowing activities are generally not supported by evaluation of their impact on fiscal and debt sustainability. Debt sustainability analysis is infrequent in most Caribbean countries and therefore does not sufficiently influence policy. Moreover, there is limited involvement of government legal advisors.

Operational risk management and debt recording. Operational risk management procedures are generally not well developed, and if these procedures exist, they are often not followed. Concerning debt recording and reporting, except for Jamaica, countries do not regularly disseminate comprehensive debt statistics, due in part to staffing constraints and the relatively low priority given to debt management.

Against this backdrop, however, deliberate efforts are being made to improve the debt management frameworks in Barbados, Jamaica, Suriname, and Trinidad and Tobago, with support from the IDB, the World Bank, and other institutions.

²⁵ The legal framework in most countries does not contemplate the development of debt management strategies or the use of debt management objectives to guide borrowing.

8.3. Conclusions and Recommendations

Caribbean countries clearly need to strengthen their public sector performance, which has been poor, largely due to fiscal mismanagement. This is evidenced by growing public sector debt, which in some cases has become clearly unsustainable. Caribbean countries as a group have performed below their peers since the beginning of the century, and particularly since the 2008 global financial crisis, which sharply affected commodity export prices and led to weak growth in Europe and the United States, traditional tourist sources for Caribbean countries. The key indicator of the poor fiscal performance of Caribbean countries is the level of public debt, which reached the equivalent of 73.5 percent of GDP in 2016–2017 compared with 52 percent for the 164 emerging and developing economies worldwide. Poor fiscal performance led to a sustained decline in GDP growth, which has averaged 1.9 percent a year since 2000, compared with 4.3 percent for the emerging and developing economies and 2.9 percent for Latin America and the Caribbean.

The previous section showed that each of the Caribbean countries has different circumstances, strengths and weaknesses, and policy spaces. However, when the countries are taken as a group one can see that many of the debt drivers have their roots in deficient policy planning and formulation, weak institutional structures, and poor budget design and execution processes. In most Caribbean countries, this deficiency resulted in a weak base for fiscal management and macroeconomic stability, which has undermined fiscal discipline and hampered the strategic allocation of resources and efficient service delivery, thereby compromising the attainment of potential development gains. This has been aggravated by poor governance and the virtual absence of medium-term fiscal policy frameworks, which are guided by fiscal/public debt sustainability considerations and thus help avoid procyclical policies (World Bank 2012; Vlaicu et al. 2014). Further, the lack of or weak debt management systems, rules, and institutions have compounded that deficiency.

While country-specific recommendations will be provided within the individual country chapters of this book, overall it is essential that Caribbean countries make determined efforts to strengthen fiscal discipline, institutional structures of policy planning and formulation, processes, and rules shaping the conduct of fiscal policy, and budget design and execution. This should ensure prudent fiscal decisions, credible budgets, efficient resource use and reliable transactions, and transparency and institutional accountability. The objective should be to achieve fiscal sustainability, within fiscal and debt management rules and practices, consistent with a

sound medium-term fiscal framework. Underlying this objective is a desire for strong and sustained economic growth and social development. The establishment of home-grown independent fiscal institutions (which are non-partisan, technically competent, and accountable to the legislature) would help improve transparency and credibility, as well as increase the awareness and political costs of unsound policies. Continued and strong support from the regional development partners will be critical.

The individual reform programs will need to take account of the diversity of conditions, contexts, strengths and weaknesses, and policy spaces of each of the Caribbean countries. While most of the reforms discussed above reinforce each other, the design of the individual country programs must ensure that the sequencing of reforms reflects a country's requirements, implementation capacity, and legal processes.

In any event, most countries need to give priority to simultaneous reforms of public financial management practices together with the establishment of fiscal policy rules that set long-lasting limits on budgetary aggregates (preferably through legislation). This would mainly address the first four fiscal institutions needed to implement a credible fiscal strategy identified by the International Monetary Fund (Appendix 4). Some countries should focus on further strengthening their governance and public financial management systems. Finally, those countries with a heavy debt burden may need to prioritize the implementation of a sound debt management system (Appendix 5), supported by adjustment efforts to lower that burden. Two of the three commodity exporters have already established sovereign wealth funds, and the third country should do so without delay. To support the funds, these countries need to introduce fiscal rules that help avoid procyclical policies that typically create fiscal instability and harm economic growth.

To conclude, the urgency of the reforms needed by all Caribbean countries should not be underestimated. To remove the threat of unsustainable indebtedness, all of the weaknesses discussed in this chapter need to be addressed. This is especially challenging for small countries with already stretched capacity, but it is imperative and do-able if there is political will.

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SECTION IV:

The Institutional Reality Country by Country

The Bahamas

Allan Wright

9.1. Political Institutions

The political system of The Bahamas is based on a parliamentary Westminster democracy. The head of government is the prime minister. As a member of the Commonwealth, the archipelago follows the political and legal traditional framework of the United Kingdom. Queen Elizabeth II or her representative—the governor general—is the head of state. However, the Cabinet exercises executive power.

The Bahamas has a bicameral Parliament with a lower house (the House of Assembly) and an upper house (the Senate). Dating to 1729, the House of Assembly consists of 39 representatives, who are directly elected by popular vote for five-year terms. The party or coalition obtaining the majority in the House of Assembly selects a leader from among its elected members. The leader of this majority, therefore, would usually become the prime minister. There are 16 members of the Senate, nine of whom are appointed by the prime minister, four by the opposition leader, and three by the governor general on the advice of both the prime minister and the opposition leader. Members of Parliament can be re-elected with no limit on the number of periods.

There are at least nine members of the Cabinet, including the prime minister and the attorney general. The minister of finance must by law be a member of the House of Assembly. Other members of the Cabinet are also appointed by the prime minister either from the House of Assembly or the Senate, although only a maximum of three ministers can be drawn from the latter (The Constitution of the Commonwealth of The Bahamas).

9.1.1. *Political Parties and Background*

Two parties dominate the political landscape of The Bahamas: the Progressive Liberal Party (PLP), which is usually center left, and the Free National

Table 9.1 Profiles of the Main Political Parties in The Bahamas

Name of Party	Initials	Periods in Executive Power Since Independence	Ideology	Ethnic Voter Base	Prevailing Religion of Voter Base
Free National Movement	FNM	1992–2002 2007–2012 2017–present	Center-right	N/A	N/A
Progressive Liberal Party	PLP	1973–1992 2002–2007 2012–2017	Center-left	N/A	N/A

Source: Author’s elaboration based on www.caribbeanelections.com.

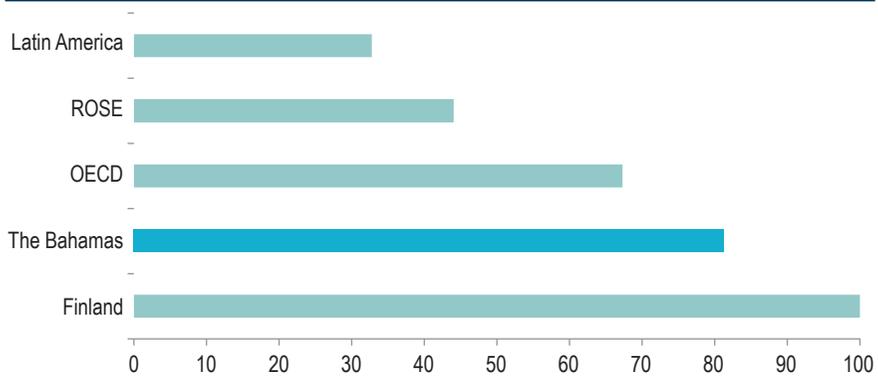
Note: N/A: not applicable.

Movement (FNM), which leans center right (Table 9.1). Since the 2012 elections, the Democratic National Alliance (DNA) has become more prominent as a third political option. Over the years since independence, The Bahamas Constitution Party (BCP), Bahamas Democratic Movement (BDM), Coalition for Democratic Reform (CDR), and the Bahamas Nationalist Party (BNP) have all sought national representation, though largely unsuccessfully.

The PLP was established as the first party of national representation in 1953 by a group of Bahamians of European and African ancestry. The party emerged from an alliance of Cyril Stevenson, William Cartwright, and Sir Henry M. Taylor with the pledge of anti-discrimination measures. The PLP was able to secure leadership and form the first black-led political government in the country from 1973 to the early 1990s.

The white elite had dominated the 1962 elections in The Bahamas through the United Bahamian Party (UBP). Considering that a white dominated party could be viewed as out of touch with the needs of a black majority citizenry, the party was dissolved and members of the former UBP along with support from other parties in opposition to the PLP joined together and formed the Free National Movement (FNM) in 1971. By attracting middle-class voters as well as a considerable number of working-class Bahamians, the party’s base was established (Bahamas: Independence and Beyond, 2003).

As shown in Chapter 6, the literature suggests that countries that had a lower reliance on extractive activities and coercive labor, have been more likely to develop open and inclusive political institutions. Given its colonial legacy of merchant elites, and freed slaves insulated from coercive labor arrangements after emancipation, The Bahamas fits within an historical trajectory that might have favored the emergence of a pluralistic and inclusive political system. Figure 9.1 shows the country’s favorable performance on the Public-Regardedness Index, which indicates the extent to which

Figure 9.1 The Bahamas: Public-Regardedness Index

Source: Author's calculations based on the database in Berkman et al. (2008).

Notes: Each measure was standardized to obtain an index ranging from 0 (worst performance) to 100 (best performance) using the following formula: $(var - min)/(max - min)$, where *var* is the individual country measure, and the maximum and minimum are the highest and lowest value in the datasets, respectively. Finland is the country with the highest Public-Regardedness Index score worldwide. OECD: Organisation for Economic Co-operation and Development; ROSE: rest of the small economies of the world.

policies pursued are perceived to be in the public interest or whether they tend to be directed to special interest groups.¹

The next section analyzes relevant rules and institutions in place to guarantee democratic participation and transparency in electoral processes.

9.1.2. *Political Representation, Competition, and Transparency in the Political System*

Countries are more likely to establish appropriate economic institutions that in turn spur development when the political system offers effective governance through a widespread electorate and openness (Acemoglu and Robinson 2012). As such, it is important to assess the extent to which political participation is widely accessible or whether rules and institutions restrict it to a minority elite. Answering this requires an inspection of the process by which political parties appoint their leaders and electoral candidates.

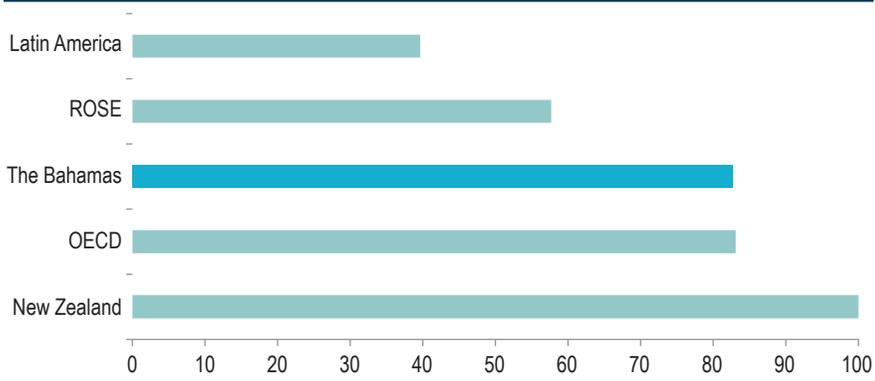
¹ As explained in Chapter 6 of this volume, the Public-Regardedness Index was proposed in Berkman et al. (2008). The authors computed this index using expert evaluations and perceptions on issues related to (1) corruption, (2) public spending on social transfers, and (3) whether government contracts are awarded fairly or generally favor well-connected firms and individuals. The index is the combination of these three measures. The first component was taken from Transparency International Corruption's Perceptions Index, and the last two components from the Global Competitiveness Report.

The procedures of internal democracy involve a system of party members or delegates in good standing with their party voting in internal elections for party leaders, members of special party committees, and candidates for upcoming elections. This process is usually carried out periodically at party conferences or conventions or before the holding of major elections. The constitutions of the major parties (PLP and FNM) in The Bahamas generally establish the law governing the party and the related branches. It is through this constitution that opportunities exist to change or reaffirm party leadership, elect officers, establish policies, and change bylaws and the overall party constitution.

The Bahamas has 39 divisions or constituencies. Each constituency elects one member to the House of Assembly. The country has had a marginal increase in its share of female representation in Parliament, from 12.7 percent in 2007 to 13.2 percent in 2016. Still, The Bahamas has the lowest level of female representation compared to other countries in the Caribbean region (UNDP 2015).

There seems to be a low degree of state capture in The Bahamas, as can be seen in the control of corruption dimension of the World Bank's World Governance Indicators. This dimension reflects, among other things, the extent to which the state is captured by elites and private interests. Figure 9.2 shows that The Bahamas performs on par with the average for the Organisation for Economic Co-operation and Development (OECD) and above the other reference country groups.

Figure 9.2 The Bahamas: Control of Corruption



Source: World Bank, 2017 World Governance Indicators database (www.govindicators.org).

Notes: Percentile ranking ranging from 0 (worst in controlling corruption) to 100 (best in controlling corruption). Control of corruption captures perceptions of the extent to which public power is exercised for private gain, including both petty and grand forms of corruption, as well as “capture” of the state by elites and private interests. New Zealand is the best country worldwide in terms of controlling corruption.

Open participation and transparency of electoral processes are central aspects of any democracy. The Parliamentary Registration Department (PRD) is the leading electoral management agency in The Bahamas. The PRD is headed by the parliamentary commissioner, who is appointed by the governor general on the advice of the prime minister after consultation with the leader of the opposition. The parliamentary commissioner appointment is constitutionally based. The commissioner can serve up to retirement (68 years old) but can be removed from office by the governor general for failure to adequately perform duties or for misbehavior. This can be done following the recommendations of a special tribunal appointed by the governor general to review the actions of the parliamentary commissioner. Assisting the parliamentary commissioner are deputy commissioners who are all appointed by the governor general on the advice of the Public Service Commission (PSC).²

For each succeeding period of five years (election cycle), the electoral code requires the complete re-registration of voters and the preparation of a new registry that must be made public.³ The registry is constantly reviewed to ensure that persons are not included twice or registered according to a qualification that they do not have. The registry has improved over time in terms of registering all potential voters. It was estimated in 2017 that around 75 percent of all potential voters in the Grand Bahama and Family Islands were registered (63 percent in 2012), while this percentage was 63 percent in New Providence.⁴

International and regional observers are invited to observe and scrutinize general elections. For the past general election, the Organization of American States and the Commonwealth Community served as international observers, while the Caribbean Community (CARICOM) and the United States were the regional observers. The 2017 general elections in The Bahamas took place peacefully throughout the archipelago with a turnout of 88 percent.

In summary, The Bahamas political system has achieved a well-functioning democracy with open political participation and a general absence

² The PSC regulations state that it “has powers to make appointments to Public Office, to remove and to exercise disciplinary control over public officers with the exception of those persons who come under the Police, and Judicial and Legal Service Commissions, consisting of a Chair and up to a maximum of four other members.” PSC members are appointed by the governor general based on recommendations from the prime minister in consultation with the leader of the opposition.

³ Voter cards and other counterfoils previously issued become null and void at the end of each five-year period with some 30 days’ notice.

⁴ Estimates are based on projected population growth.

of state capture by political or economic elites. In addition to political institutions a strong rule of law is another central institutional component. The next section assesses its standing.

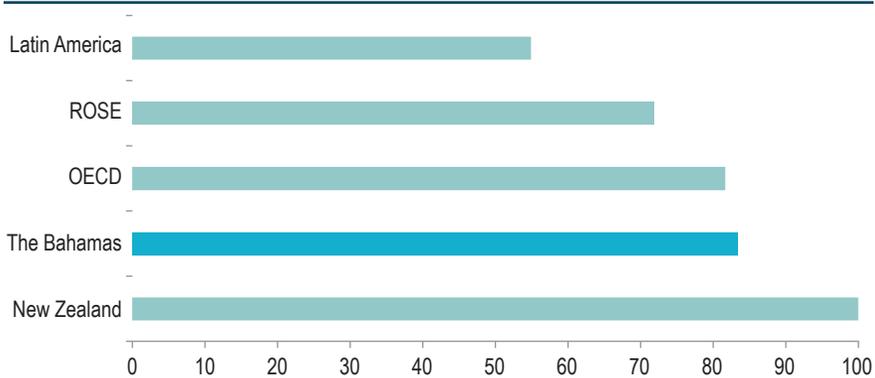
9.2. Rule of Law Institutions

As shown in Chapter 4, the literature to date clearly suggests that there are three key institutional rule of law components that have a significant causal relation with economic growth. The first relates to the strength of property rights enforcement protecting private agents from the risk of having their property expropriated. The second relates to the fundamental rights embedded in the constitution. The third refers to the possibility of obtaining fair and independent administration of justice with the strength to enforce the law without external pressures. This section assesses the situation of these institutions in The Bahamas.

9.2.1. Strength of Property Rights

The Political Risk Services' 2016 Index of Protection against Expropriation shows that property rights protection in The Bahamas is in good standing (Figure 9.3). Indeed, the country is on par with OECD standards regarding this summary index, showing that expropriation risks either by the government of powerful elites is almost non-existing in The Bahamas.

Figure 9.3 The Bahamas: Protection Against Expropriation Index



Sources: 2016 Political Risk Services database (www.prsgroup.com).

Notes: Each measure was standardized to obtain an index ranging from 0 (worst performance) to 100 (best performance) using the following formula: $(var - min)/(max - min)$, where *var* is the individual country measure, and the maximum and minimum are the highest and lowest value in the datasets, respectively. New Zealand is the country with the best protection against expropriation worldwide.

The next section assesses the protection of fundamental human rights in The Bahamas as a key dimension for social development and cohesion.

9.2.2. *Protection of Fundamental Human Rights*

The constitution of The Bahamas clearly establishes respect for fundamental rights and equal treatment of Bahamian citizens. According to the 2016 World Justice Project Rule of Law Index (Table 9.2), the protection of fundamental rights in the archipelago performs above the average for the ROSE and Latin America. However, the OECD exceeds The Bahamas in all index categories.

The Bahamas has the highest score for the right to life and security of the person, and all indicators are equal or above levels for Latin America and ROSE. The only exceptions are the guarantee of freedom of belief and religion and equal treatment and absence of discrimination, where The Bahamas scores below the ROSE average. Special attention should be placed on these issues as there is in fact scope for improvement in the protection of fundamental rights across all subfactors shown in Table 9.2.

Table 9.2 Protection of Fundamental Rights in The Bahamas

Fundamental Rights	The Bahamas	Latin America	ROSE	OECD
Overall Fundamental Rights	0.67	0.58	0.62	0.76
4.1 Equal treatment and absence of discrimination	0.60	0.51	0.62	0.70
4.2 The right to life and security of the person is effectively guaranteed	0.82	0.61	0.67	0.86
4.3 Due process of law and rights of the accused	0.62	0.46	0.56	0.73
4.4 Freedom of opinion and expression is effectively guaranteed	0.66	0.61	0.59	0.74
4.5 Freedom of belief and religion is effectively guaranteed	0.68	0.75	0.71	0.76
4.6 Freedom from arbitrary interference with privacy is effectively guaranteed	0.64	0.52	0.51	0.77
4.7 Freedom of assembly and association is effectively guaranteed	0.71	0.66	0.71	0.79
4.8 Fundamental labor rights are effectively guaranteed	0.60	0.56	0.60	0.71

Source: World Justice Project (WJP) (<https://worldjusticeproject.org/our-work/wjp-rule-law-index/wjp-rule-law-index-2016/factors-rule-law>).

Note: Scores for the WJP Rule of Law Index, as well as for its component factors and subfactors, range from 0 to 1, where scores closer to 1 indicate better performance.

The government of The Bahamas has proposed the establishment of the Office of Ombudsman to provide some relief to persons with legitimate grievances against institutions of government.⁵ Likewise, the Office of the Public Defender was established in January 2017 to protect the rights of citizens and provide legal representation to the public by investigating complaints against rights violations. Judiciary independence and effectiveness are central to fundamental rights protection. The institutional reality of these features in the administration of justice is assessed next.

9.2.3. Judicial Independence and Effectiveness

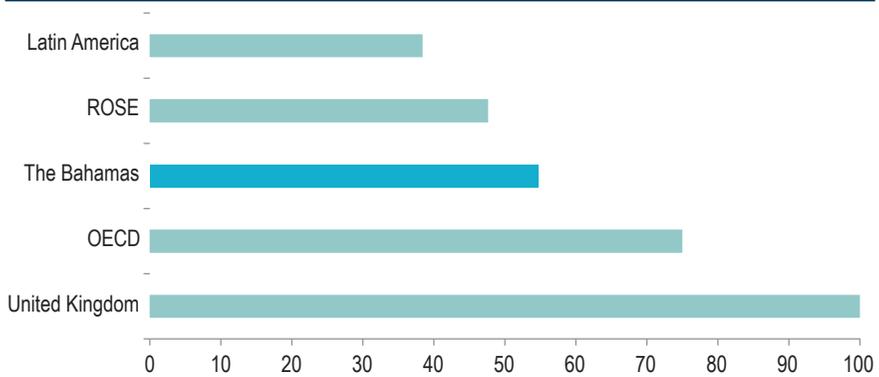
The laws of The Bahamas are based on English Common Law. The major institutions for justice are the Supreme and Magistrates Courts and the Court of Appeal. The final appeal or the highest court of appeal for all matters is the Judicial Committee of Her Majesty's Privy Council. The judiciary is formally independent of all government offices, and appointments are made by the governor general with advice from the Judicial and Legal Service Commission (JLSC).⁶ Still, the chief justice and the president of the Court of Appeal are appointed by the governor general with input from the prime minister and the leader of the opposition. With respect to tenure, judges on the Supreme Court can serve up to 65 years old but can be extended to 67. For appellate justices, tenure is up to 68 years old but can be extended to 70.

In turn, the chief prosecutor or Director of Public Prosecutions (DPP) is appointed by the governor general with the advice of the Judicial and Legal Service Commission. An independent office of the DPP was established recently by amending Article 78 of the constitution, which now gives the DPP powers relating to all criminal prosecutions.⁷ The government has

⁵ The legislation was foreshadowed in the Speech from The Throne, which outlined the government's policies and objectives at the official opening of the new session of Parliament in May 2017.

⁶ Following the British model, all justices are appointed by the governor general after advice from the JLSC. The JLSC is composed of five persons and is chaired by the chief justice. Other members are justices of the Court of Appeals, including the president of that court.

⁷ Speaking about legislative plans foreshadowed in the Speech from the Throne in May 2017, Press Secretary Anthony Newbold was quoted in the Nassau Guardian (September 2017) as saying "the House of Assembly will also focus on debate on a bill for an Act to Amend the Constitution of The Bahamas to provide for the Establishment of the Office of the Director of Public Prosecutions and for Matters Connected Thereto." According to Newbold, the bill would pass some powers previously held by the Attorney General on matters relating to criminal prosecutions, to the DPP.

Figure 9.4 The Bahamas: Judicial Effectiveness Index

Source: Author's calculations based on the 2017 Heritage Foundation Index of Freedom database (www.heritage.org).

Notes: Each measure was standardized to obtain an index ranging from 0 (worst performance) to 100 (best performance) using the following formula: $(var - min)/(max - min)$, where *var* is the individual country measure, and the maximum and minimum are the highest and lowest value in the datasets, respectively. The United Kingdom is the country with the highest Judicial Effectiveness Index ranking worldwide.

accordingly separated the DPP from the Office of the Attorney General. Consideration is being given in the appointment of justices that would see those appointments made by the governor general with the recommendation of the Judicial and Legal Services Commission instead of the prime minister and leader of the opposition.

In terms of judicial effectiveness, The Bahamas displays good to intermediate outcomes on the Judicial Effectiveness Index (Figure 9.4). Whereas the country outperforms comparable countries of equivalent size (ROSE), there exists ample room for improvement as the benchmark of most developed countries is significantly higher. As such, The Bahamas presents a relative lag that was not observed in the institutional dimensions previously assessed.

The timeliness of the administration of justice could be improved in The Bahamas. One objective measure, the density of judges, stands at 12 judges per 100,000 population in The Bahamas, which is moderately below the world average of 18 judges per 100,000 population.⁸

The next section assesses the institutional capacity to enforce the law, with a focus on the police as the main institution for law enforcement.

⁸ Source: United Nations Office on Drugs and Crime criminal justice data for 2014 (<https://data.unodc.org/>). There are roughly 15 Magistrates' Courts in New Providence, four in Grand Bahama, and one in Abaco, along with 12 justices of the Supreme Court and five justices on the Court of Appeal.

9.2.4. Law Enforcement

The Royal Bahamas Police Force (RBPF) has over 3,000 officers and an additional 300 public servants. The force has 846 officers per 100,000 population, one of the highest per capita ratios of police officers in the world.⁹ The current head of the RBPF is the commissioner of police, who reports to the minister of national security. The commissioner and the commissioner's major officers are appointed by the governor general on the advice of the Police Service Commission (PSC), with input from the head of the executive and the opposition leader. The PSC consists of a chair and at least two other members, none of them members of the legislature.¹⁰

Applicants for the RBPF must meet academic and medical standards and pass an assessment program. The interview process includes an in-depth evaluation at the National Training College, including physical fitness and agility, written, dictation, and aptitude tests. Psychological and medical assessments are also included as well as a detailed background check.

Government efforts to boost citizen security by strengthening and modernizing the law enforcement system have improved with the increase in RBPF police officers and equipment. General expenditures on the police represent approximately 1 percent of gross domestic product (GDP), a higher level of spending than the average for Latin America and the Caribbean (Jaitman 2017). In addition, The Bahamas is among the top three countries in the region in terms of overall public citizen security expenditures (between 1.15 and 1.94 percent of GDP).

The RBPF Strategic Policy and Planning Unit prepares indicators for gauging the performance of the force. Daily crime briefs, weekly CompStat meetings, and monthly productivity reports are used to measure performance, and crime reports are aimed at facilitating an understanding of efforts to reduce major crime.

Regarding police effectiveness and constraints, the geography of the archipelago must be considered. There is uneven population distribution over vast expanses of land and sea (over 700 islands and cays covering a 100,000 square mile area), creating difficulties for policing. Some sections of the southern-most islands have a limited police presence, posing border

⁹ Source: United Nations Office on Drugs and Crime criminal justice data for 2014 (<https://data.unodc.org/>).

¹⁰ Officers above the rank of inspectors are appointed or promoted by the governor general, with the advice of the PSC, while promotions, transfers, and appointments below the rank of inspector are vested in the hands of the commissioner of police, based on advice from the Police Promotion Board.

and security issues. This geography also poses challenges to gathering information, and the country's capacity to analyze data collected on crime and violence remains constrained.

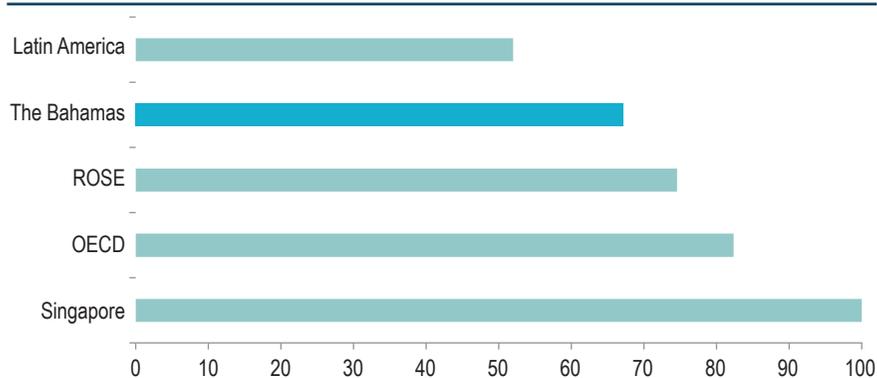
The RBPF resolved about 46 percent of serious crimes (murders) in 2015, a ratio that represented a decline of 5 percent with respect to 2013 levels. While this rate is relatively favorable compared to other Latin American and Caribbean countries, it falls short when compared to the levels of 64 percent in the United States (2013), 75 percent in Canada (2010), and 90 percent in the United Kingdom (2013).¹¹ Considering that The Bahamas has the third highest cost in Latin America and the Caribbean for investigating homicides, there exists ample room for improvement in terms of investigative effectiveness (Jaitman 2017).

Appearing before the United Nations Human Rights Council in January 2018, the Attorney General for The Bahamas outlined some deficiencies within the RBPF's complaints and corruption branch, primarily due to a lack of oversight. The attorney general also stated that while there was a decrease by some 11 percent in complaints against the RBPF in 2016 (167 complaints) from a year earlier in New Providence and the southern Bahamas, complaints increased by some 25 percent in other areas of the archipelago (Grand Bahama and the northern Bahamas). On these issues, the recently created Office of the Public Defender, which provides legal representation to members of the public, is expected to strengthen efforts to exercise stronger oversight of police-abuse-related issues.

Given the relatively high spending levels on the police force and the high ratio of police officers to the population, security and order within The Bahamas is relatively modest. For instance, The Bahamas has the third-highest social cost of crime in Latin America and the Caribbean (0.94 percent of GDP) and the third-highest level of private spending on citizen security (between 1 and 1.9 percent of GDP). These indicators are only higher for countries with a particularly high incidence of crime and violence like Honduras and El Salvador (Jaitman 2017). Figure 9.5 shows that on the Order and Security Index, The Bahamas is above the Latin American average but below ROSE and significantly below the OECD, suggesting ample room for improvement.

Overall, this section has shown that institutions supporting the protection of fundamental rights, the administration of justice, and law enforcement in The Bahamas have room for improvement as they perform below what would be expected given the country's development levels in

¹¹ See Sancheska Brown, "Crime Statistics: Murders, Rapes and Armed Robberies Up," *Tribune* 242, 11 February 2016. Available at <http://www.tribune242.com/news/2016/feb/11/crime-statistics-murders-rapes-and-armed-robberies/>.

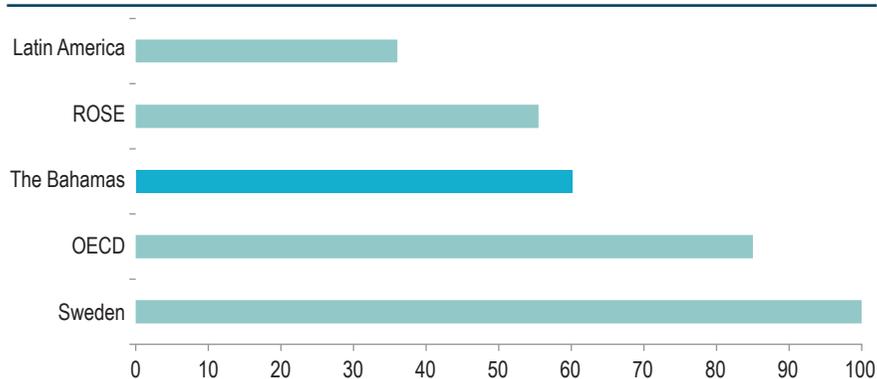
Figure 9.5 The Bahamas: Order and Security Index

Source: Author's calculations based on the 2016 World Justice Project database.

Notes: Each measure was standardized to obtain an index ranging from 0 (worst performance) to 100 (best performance) using the following formula: $(var - min)/(max - min)$, where *var* is the individual country measure, and the maximum and minimum are the highest and lowest value in the datasets, respectively. Singapore is the country with the highest ranking worldwide on the Order and Security Index.

other areas (e.g., in property rights protection). Several steps are already being taken to enhance judiciary independence and police accountability, which should be framed within comprehensive strategies to further improve the institutional framework for the rule of law.

Figure 9.6 summarizes this performance in The Bahamas based on the 2016 Rule of Law dimension calculated as part of the World Bank's World Governance Indicators. It shows that while The Bahamas outperforms

Figure 9.6 The Bahamas: Rule of Law

Source: World Bank, 2017 World Governance Indicators database (www.govindicators.org).

Notes: Percentile ranking ranging from 0 (worst in rule of law) to 100 (best in rule of law). Rule of law captures perceptions of the extent to which agents have confidence in and abide by the rules of society, and in particular the quality of contract enforcement, property rights, the police, and the courts, as well as the likelihood of crime and violence. Sweden is the best country worldwide in terms of the rule of law.

Latin America and ROSE, there is still room for improvement to reach best practice standards.

9.3. Institutions for Human Capital Development

As shown in Chapter 4, two main institutions supporting human capital development have been highlighted in the literature: institutions relating to education and health. This section documents the state of these institutions in The Bahamas.

9.3.1. Education

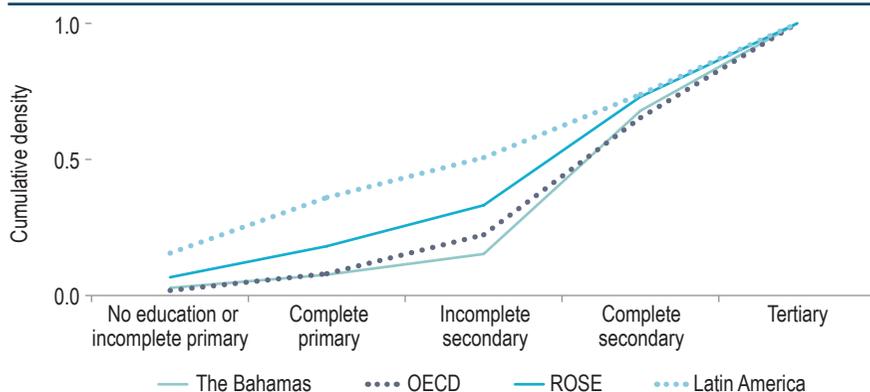
The related evidence presented in Chapter 4 suggests that the quality of education matters more than the quantity. Furthermore, the quality of education hinges primarily on the quality of teachers. Therefore, this section will focus not only on the ability of educational institutions to offer educational services coverage, but also on the condition of institutions directed toward ensuring appropriate teacher quality in The Bahamas.

The archipelagic profile and distribution of the population in the country makes the delivery of quality educational services a challenge for the government. Nevertheless, over the last decade, The Bahamas was able to make significant progress to guarantee free universal access for students from 5 to 16 years old up to the secondary school level and has made some progress in terms of quality in primary schools.

The public education system covers primary, secondary, and tertiary education, along with the recent inclusion of preschool. However, the system is concentrated on the primary and secondary levels, whereby pre-primary education provision remains low and is dominated by the private sector. In general, around 36 percent of students below the tertiary level rely on the private system.

Educational attainment in The Bahamas is depicted in Figure 9.7, which shows that the working-age population (25–65 years old) is mostly concentrated in the highest schooling levels, advantaging the other benchmark country groups. Indeed, 32 percent of the population of The Bahamas has a tertiary education, a level close to the OECD (34.6 percent) and above Latin America (26.1 percent) and ROSE (26.9 percent).

Considering effective institutions directed toward incentivizing better teaching quality, Chapter 4 suggested that the critical institutional components appear to be the monitoring of teacher effort and quality, and performance-based hiring and retention decisions.

Figure 9.7 The Bahamas: Educational Attainment

Source: Author's calculations based on The Bahamas 2014 Labor Force Survey and the World Bank's 2016 World Development Indicators database.

Note: Educational attainment is measured among working-age adults (25-65 years old) who have completed their formal education.

The Ministry of Education guides the development and implementation of policies for the delivery of public and private education in The Bahamas. Teaching posts can be filled by transfer or appointment from within or outside the service according to needs in the system. Teaching appointments are overseen by the Ministry of Education, which is responsible for administration, financial, and disciplinary purposes. Applicants to work in the public education sector are required to produce academic certifications, medical and police record certificates, and documented evidence of previous and related teaching experience. Public service applications are directed to and approved by the PSC.¹²

Evaluation of teacher performance follows a structured form of interaction between a subordinate and a supervisor that is usually conducted over a previously agreed-upon period. The performance of teachers is examined, and weaknesses and strengths are identified, as are opportunities for skill development and improvements, continuous employment, and incremental pay.¹³ However, the methodology used is to some extent connected to the old evaluation system, where feedback is not always focused on the development of system-wide effectiveness. Furthermore, there is no system of standardized student-based evaluation that could be

¹² Source: www.ministryofeducationbahamas.com/careers-at-moest.

¹³ Most evaluations within the education system are carried out by the Ministry of Education, the Anglican Central Educational Authority, the Catholic Education Board, the Baptist Educational Convention, the Methodist Schools, members of the International Association of Methodist Schools and The University of The Bahamas.

used to compute teacher value-added measures based on student performance. This is highly relevant, as objective evidence provided by Araujo et al. (2016) shows that teacher value-added measures based on student evaluations provide a better measure of teacher effectiveness than traditional teacher assessments based on direct evaluations or observation of teachers.

9.3.2. Health

Universal access to medical care is provided by the public health care system in The Bahamas. The *National Health Insurance (NHI) Act* passed in 2017 provided access to infant vaccination, primary care, and prescription coverage, though these provisions are basic. Later phases are planned to include expanded coverage for several noncommunicable diseases as well as maternal and neonatal services. Public health care provision remains dominant, as about 65 percent of Bahamians do not have private medical insurance.¹⁴

Health financing and primary care in the archipelago are provided by the government.¹⁵ The Ministry of Health performs most functions within an organizational model geared toward predominantly curative and disease-based treatment. Its functions cover public institutions, private for-profit institutions, and private non-profit institutions. Also, some public funding is provided directly to the private health care system.

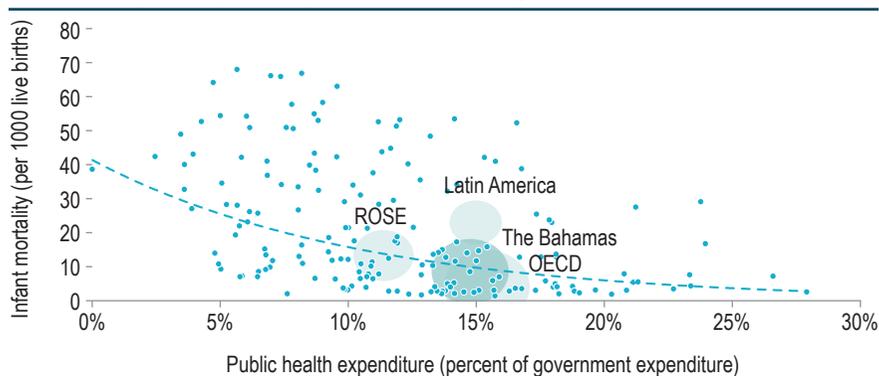
Public expenditure on the health sector, infant mortality rates, and the number of physicians per 1,000 population are depicted in Figure 9.8. The Bahamas has significantly higher coverage of physicians per capita than the averages for ROSE and Latin America, with a level closer to that of the OECD. Likewise, infant mortality in The Bahamas is lower than in ROSE and Latin America, performing on average in accordance with its level of public health expenditures. However, there is scope for improvement if one considers the OECD as the benchmark group, as the OECD has slightly higher and more effective spending in terms of health outcomes.

Besides the provision of health care funding, the Ministry of Health is also responsible for policy planning, regulation, monitoring, development, and implementation of public health programs and community health

¹⁴ Note, however, that over a third of the population in The Bahamas is covered by private health insurance (114,517 persons in 2014), one of the highest in the Caribbean.

¹⁵ The health sector comprises four clusters of service: The Ministry of Health, Department of Public Health, Department of Environmental Health Services, and Public Hospitals Authority.

Figure 9.8 The Bahamas: Public Health Expenditure, Physicians per 1,000 Population, and Infant Mortality



Source: Author's calculations using the World Bank's 2016 World Development Indicators database.

Note: The size of the bubbles is proportional to the number of physicians per 1,000 population for selected countries or country groups.

services. The *Health Professions Act* of 1998 provides the regulation and mechanisms for health care quality.

Recruitment in the health sector requires that prospective employees' academic and medical history be reviewed by an independent panel appointed by the Public Hospitals Authority (PHA).¹⁶ This process aims to determine employment suitability and enable the tracking of work performance throughout the employment period. The PSC or the PHA confirm persons selected for employment and pensions.

Upon initial appointment, salaries are based on qualifications and experience, with additional years of experience accounting for increments to the paid salary. All salaries are reviewed every three to five years with a view to an increase by the PHA and are tied to the cost of living index and other considerations, including performance. However, no systematized mechanisms to collect objective data on health practitioners' outcomes

¹⁶ Established in 1998, the PHA is responsible for the management of three government-owned facilities—the Princess Margaret Hospital, Sandilands Rehabilitation Centre and Rand Memorial Hospital—as well as all other health care services in Grand Bahama. The PHA is also responsible for the government's National Drug Agency, Materials Management Directorate, and National Emergency Medical Services. The PHA board is not involved in the operational management of the authority but rather solely policy-based. Board members can hold office for up to three years but can be reappointed thereafter. The chair and deputy are appointed by the minister of health, while the managing director is an ex officio member. Other members of the PHA board include representatives from the Ministry of Health, also appointed by the minister and representatives from trade unions and financial, industrial, and professional organizations.

in terms of patient results are in place. As such, the development of information and communication technologies to objectively calculate health practitioners' effectiveness and tie such statistics to performance-based pay is an institutional improvement that could be considered.

This section has shown that institutions supporting human capital development in The Bahamas are on a relatively good path. However, regional disparities within the country persist, as do gaps in public spending across schooling levels. Performance-based hiring decisions and economic incentives are institutional arrangements not currently in place within the public education and health systems. Therefore, such institutions could be considered toward achieving greater meritocracy and efficiency in the public service.

9.4. Economic Institutions

The Bahamas is one of the wealthiest nations in the Caribbean. It is a tourism-oriented economy with other developed services sectors, both in finance and technology. However, as both a borrower and financial center, the country is highly dependent on the behavior of international capital markets. Real GDP growth in The Bahamas has been sluggish since the 2008 global financial crisis and as a result of natural disasters, delayed large-scale private investment projects, and modest growth in North America (which is the main source of tourism in The Bahamas). The International Monetary Fund's April 2018 *World Economic Outlook* estimated medium-term growth levels of over 2 percent. Large-scale capital projects and a rebound in tourist value-added contributions are expected to be the leading contributors to the revival of growth.

This section assesses the state of key economic institutions that, as shown in Chapter 5, have been associated with increased confidence, investment, and growth.

9.4.1. Central Bank Independence and Transparency

The Central Bank of The Bahamas was established in June 1974 to conduct independent monetary and financial sector supervisory functions. It was established as a statutory body governed by the *Central Bank of The Bahamas Act* and administered by a Board of Directors. The board is chaired by the governor with a separate technical and budgetary framework. The governor of the bank is appointed for a five-year term, and like the board of directors, is appointed by the governor general.

Monetary policy in The Bahamas has focused on maintaining a fixed exchange rate in parity between the Bahamian and U.S. dollars. Reserve

requirements, selective credit controls, and some capital controls are key tools of monetary policy. In addition, policy relies on the management of financial sector liquidity by varying the central bank discount rate. Interest rate policy is informed by changes to bank liquidity and domestic credit conditions. The use of market operations in the conduct of monetary policy is limited to the issuance of treasury bills and bonds on behalf of the government.

The four strategic objectives of the Central Bank of The Bahamas are to (1) improve the operational framework for monetary policy; (2) strengthen regulatory and supervisory frameworks; (3) develop financial stability arrangements; and (4) enhance overall operational efficiency. Ultimately these approaches to monetary policy involve improvements to the predictive capability and sectoral linkages of the economic forecasting model. This also includes implementing the Online Reporting and Information Management System to improve the efficiency and accuracy of the data collected, compiled, and analyzed from the bank's licensees for supervisory and research purposes. Additionally, the Risk-Based Supervisory Framework is being enhanced to strengthen on-site examination capabilities. Work is being carried out to complete the introduction of the credit reporting system by establishing the credit bureau and fully integrating the credit unions into the supervisory net. Finally, improvements in efficiency are being implemented for current exchange control arrangements, while further opportunities for liberalization are also being undertaken.

With the 2008 global financial crisis and the reduction in consumption demand, policy-loosening initiatives were implemented by gradually lifting credit restrictions, lowering levels of reserve requirement ratios, and implementing capital and exchange controls. However, several monetary targets are non-negotiable elements of the *Central Bank Act*. For instance, the central bank's facilitation of Treasury borrowing should not exceed 20 percent of the central bank's demand liabilities. Also, external reserves held in support of the fixed exchange rate policy are to be maintained on a level equivalent to 50 percent of currency in circulation and the central bank's demand liabilities.

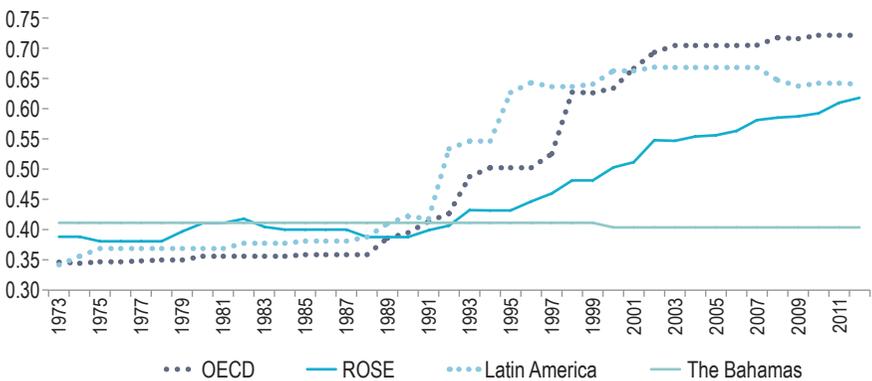
According to the 2017 Annual Report of the Central Bank of The Bahamas, the domestic debt market remains very active (over BD\$3.2 billion) and continues to be facilitated by central bank operations.¹⁷ In cooperation with the Ministry of Finance, the central bank invited the Commonwealth Secretariat to engage in a review of current domestic debt management. The recommendations resulted in the passage of the *Public Debt Management Act*, aimed at providing a framework for better public debt

¹⁷ The report is available at <http://www.centralbankbahamas.com/publications.php?cmd=view&id=16878>.

management and stronger oversight of public debt operations of state-owned enterprises. The report suggests that the establishment of a Centralized Securities Depository (CSD) will accelerate oversight and transparency. The central bank has made some progress toward the establishment of the CSD, but it is not expected to be deployed before the final quarter of 2018. Policymakers could consider undertaking further efforts to enhance transformation of the domestic debt management process by supporting independence, transparency, and oversight.

Objective international comparisons of central bank independence reported in Dincer and Eichengreen (2014) rank the Central Bank of The Bahamas relatively low at 73rd out of 89 countries worldwide.¹⁸ In a study covering an extended set of countries worldwide, Garriga (2016) ranked the Central Bank of The Bahamas 117th out of 179 countries.¹⁹ This recent relatively disadvantaged position in terms of independence, however, has not been the historical norm for the Central Bank of The Bahamas. Figure 9.9 shows rankings on Garriga's (2016) Central Bank Independence

Figure 9.9 The Bahamas: Central Bank Independence Index

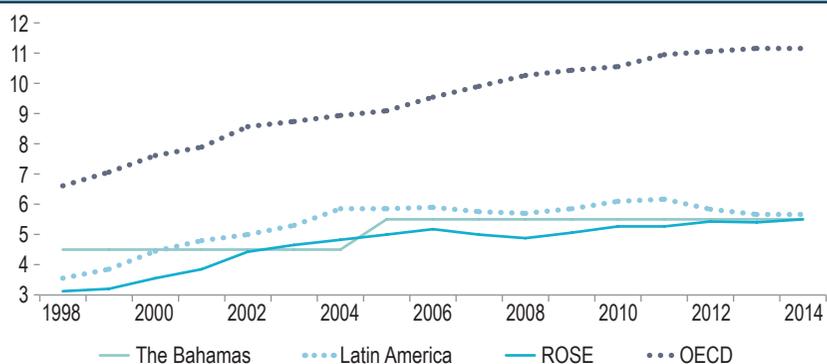


Source: Garriga (2016).

Note: The Central Bank Independence Index ranges from 0 (lowest independence) to 1 (highest independence).

¹⁸ This ranking is based on the Central Bank Independence Weighted Index (CBIW) for 2010 reported in Dincer and Eichengreen (2014). The CBIW is a weighted average of measures related to the following dimensions: chief executive officer appointment (weight = 0.1), policy formulation (0.15), objectives (0.15), limitations on lending to the government (0.50), and appointment of board members (0.1). For details on the specific components of these measures, see Table 18 in Dincer and Eichengreen (2014).

¹⁹ This ranking is for 2012. Garriga (2016) identified four dimensions concerning the independence of central banks from political influence: who appoints the governor

Figure 9.10 The Bahamas: Central Bank Transparency Index

Source: Dincer and Eichengreen (2014) updated database for Central Bank Transparency 1998–2014 (https://eml.berkeley.edu/~eichengr/Dincer-Eichengreen_figures&tables_2014_9-4-15.pdf).

Note: The Central Bank Transparency Index ranges from 0 (lowest transparency) to 15 (highest transparency).

Index from 1973 to 2012 for The Bahamas, Latin America, ROSE, and the OECD. The Central Bank of The Bahamas showed greater independence than all other country groups in 1973, but its level of independence has remained constant over time. By contrast, all other country groups have witnessed continuous improvements over time and, consequently, The Bahamas lagged all comparators by 2012.

Together with a central bank's budgetary and technical independence, the transparency of central bank functions is a key institutional feature. There is openness about the policy objectives of the Central Bank of Bahamas: monetary policy is centered on maintaining the peg (the parity between the Bahamian and U.S. dollars at 1:1) and steady credit availability for strengthening economic growth and development.²⁰ The *Central Bank Act* provides for the coordination of monetary and financial stability regulatory frameworks. This includes direct responsibility for the maintenance of the fixed parity rate of exchange and price stability through capital and exchange controls. By law and frequent practice, monetary policy mechanisms are publicly disclosed. Variations in the central bank's discount rate and capital control levels, as a signal to changes in monetary policy, are

(weight = 0.2); whether there is direct government involvement in policy decisions (0.15); whether there are limits on the ability of the government to borrow from the central bank (0.50); and whether price stability is a core objective of monetary policy (0.15). The weighted average of these dimensions results in a central bank independence index ranging from 0 (lowest independence) to 1 (highest independence).

²⁰ The *Central Bank Act* requires monetary policy based on fixed exchange rate parity between the Bahamian and U.S. dollars. This policy has prevailed since 1973.

generally announced. Nevertheless, the availability and frequency of public information on monetary policy and operational transparency appear to be below required levels. In addition, expanding the capacity of statistical departments within the central bank to provide better and more timely data would support a more transparent system. Indeed, as Figure 9.10 shows, the transparency of the Central Bank in The Bahamas is on par with Latin America and ROSE, but there is ample room for improvement to reach OECD levels.²¹

9.4.2. *Fiscal Institutions*

The Ministry of Finance by law has responsibility for fiscal policy in the archipelago. In May 2013, the government of The Bahamas, through the Ministry of Finance, embraced a Medium-Term Fiscal Consolidation Plan (MTFP) to anchor debt and expenditures at 50 and 23 percent of GDP, respectively, by FY 2016–2017. With the development of the MTFP, annual revenues were expected to grow by 4 percent from FY 2013–2014 onward. While tax revenues in fact exceeded that level with the implementation of the value-added tax (VAT) in 2015, expenditures grew faster and failed to contract by 2 percent due to increasing subsidies to state-owned enterprises and a higher public-sector wage bill.²² The impact of Atlantic hurricanes in 2016 and 2017 resulted in a further expansion of capital spending beyond 3 percent of GDP. In sum, central government debt is above the 50 percent of GDP target in the MTFP (Central Bank of The Bahamas, Economic Reports 2017/2018).²³

With current levels of national debt and deteriorating fiscal balances, the Bahamian authorities cannot easily correct the present situation in the

²¹ The Central Bank Transparency Index measures compliance with 15 best practices distributed across the following areas: political transparency (three practices), economic transparency (three practices), procedural transparency (three practices), policy transparency (three practices), and operational transparency (three practices). The index ranges from 0 (no compliance at all) to 15 (full compliance with the 15 best practices). For details on the specific practices and index construction, see Appendix 1 in Dincer and Eichengreen (2014).

²² Subsidies to state-owned enterprises now represent roughly 5 percent of GDP, which is considered an important factor crowding out investment in key sectors of the economy.

²³ For the first seven months of 2017/2018, expenditure contracted by some 7.6 percent and revenues grew by 2.2 percent of GDP, well within the full year target set by the government of reducing expenditure by 10 percent in 2017/2018. Central government debt has stabilized at 55 percent of GDP, and with contingent liabilities of 5.6 percent, general government debt is estimated at 61 percent of GDP. (Central Bank of The Bahamas FY 2017–2018).

absence of binding fiscal rules and a fiscal council geared toward entrenching fiscal discipline, curbing fiscal pro-cyclicality, and improving budget transparency and credibility. The establishment of such institutions is not only necessary to tackle present challenges, but also to support inter-generational equity.

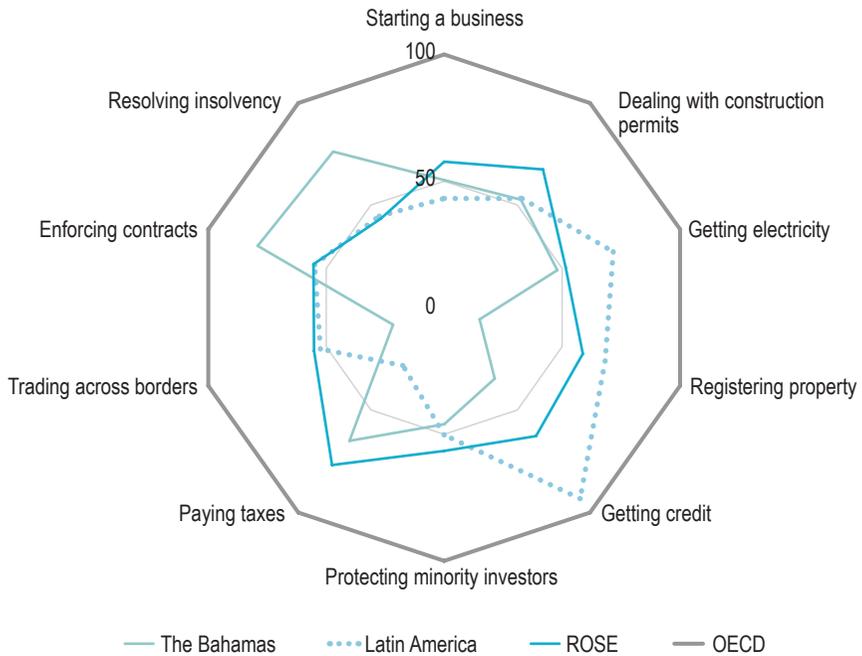
As such, a Fiscal Responsibility Legislation Draft Bill has been proposed for enactment on July 2018 that would establish a fiscal council within a year. The aim of the bill is to establish responsible fiscal management and allow the general public to have greater scrutiny of government budgetary performance. The proposed fiscal council would consist of five members appointed by the governor general on advice of the speaker of the house, and its members would be appointed for up to three years and eligible for reappointment. Members of the fiscal council could be removed by the governor general on the advice of the speaker if they are found to be guilty of misconduct or unable to perform their responsibilities. Included in the objectives of the fiscal responsibility legislation is the reduction of central government debt levels from 55 percent of GDP in FY 2016–2017 to no more than 50 percent of GDP.²⁴ The fiscal deficit is targeted to be reduced from its current level of 5.8 percent of GDP to 0.5 percent of GDP by FY 2020–2021. The transition target for the fiscal deficit is 1.8 percent of GDP in FY 2018–2019 and 1 percent in FY 2019–2020, gradually reducing the levels to achieve the medium-term target of 0.5 percent by FY 2020–2021. Finally, the Fiscal Responsibility Bill suggests that, upon achieving the 0.5 percent medium-term fiscal balance, recurrent expenditure should grow in line with the nominal growth rate of GDP.

9.4.3. *Ease of Doing Business*

As shown in Ruprah and Sierra (2016), private entrepreneurship is a key driver to boost investment, innovation, growth, and development. Therefore, institutions and regulations that permit and promote private sector development are extremely relevant. This section assesses the state of these issues in The Bahamas.

According to the World Bank's 2016 Doing Business indicators, The Bahamas has noticeable limitations in several areas when compared with ROSE, Latin America, and the OECD (Figure 9.11). These factors are the registration of property, trading across borders, protection of minority investors, and getting credit. In particular, property registration in The

²⁴ No specific medium-term target date has been provided yet.

Figure 9.11 The Bahamas: Ease of Doing Business

Source: World Bank, 2016 Doing Business database.

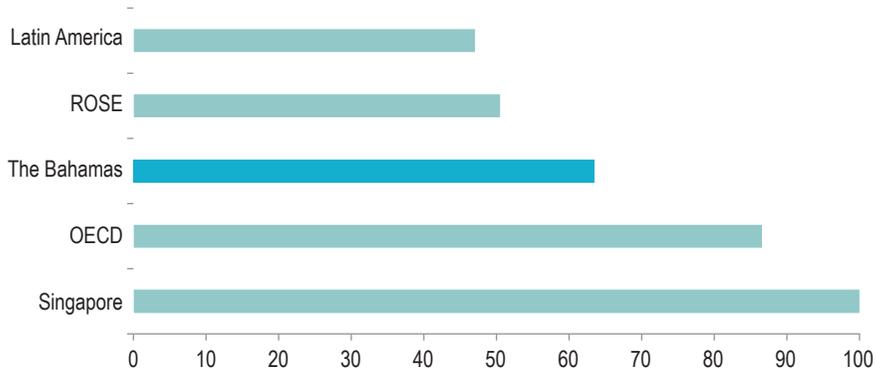
Notes: Each measure was standardized to obtain an index ranging from 0 (worst performance) to 100 (best performance) using the following formula: $(var - min)/(max - min)$, where *var* is the individual country ranking, and the maximum and minimum are the highest and lowest value in the datasets, respectively. The OECD was taken as the best practice benchmark with a value of 100 in each one of the dimensions measured.

Bahamas requires up to seven procedures and an average of 122 days, with costs estimated at almost 5 percent of the property value. Overall, such time costs and cumbersome processes negatively affect the ease of starting a business in The Bahamas.

Access to credit is another area where The Bahamas has a significantly weak performance. One main ingredient to improve access to credit would be to establish institutions that could reduce asymmetric information between potential borrowers and financial institutions. The establishment of formal credit registries to gather debt information from all sources at the individual level should rank high on the policymakers' agenda.²⁵

As shown in Figure 9.12, The Bahamas stands at a medium-level position in terms of regulatory quality. The Bahamas is better than Latin

²⁵ The government has initiated efforts to develop a credit bureau by the third quarter of 2018. Tender bids are expected to be completed by 29 June 2018.

Figure 9.12 The Bahamas: Regulatory Quality

Source: World Bank, 2017 World Governance Indicators Database (www.govindicators.org).

Notes: Percentile ranking score ranging from 0 (worst in regulatory quality) to 100 (best in regulatory quality). Regulatory quality captures perceptions of the ability of the government to formulate and implement sound policies and regulations that permit and promote private sector development. Singapore is the best country worldwide in terms of regulatory quality.

America and the ROSE with regard to the quality of regulations aimed at permitting and promoting private sector development. However, there is still ample room for improvement to reach OECD levels.

Despite no short-term threats to financial stability, as reported by the International Monetary Fund's Financial Sector Assessment Program (FSAP) conducted in 2012, the regulatory framework for the financial sector in The Bahamas has improved. On a different front, however, The Bahamas does not currently have a fair-trade commission to help promote the protection of consumer rights and limit anti-competitive behavior among the real sector and firms.

9.5. Conclusions and Policy Recommendations

The Bahamas is one of the wealthiest countries in the Caribbean and has an open and well-functioning parliamentary democracy. The country has a bipartisan political system characterized by a general absence of state capture by political or economic elites. This has allowed The Bahamas to set the stage for a more prosperous future. Nevertheless, The Bahamas could still improve the design and capacity of its institutions and thus solidify its prospects for growth and development.

Rule of law institutions in The Bahamas have room for improvement. Fully institutionalized independence of the judiciary is needed to isolate the administration of justice from improper influence, with the caveat that independence does not mean the right to non-accountability. The

separation of the Office of the Public Prosecutor from the Office of the Attorney General, as well as a reform to the process of appointing justices, are important ongoing steps in this direction. Additionally, there is room to increase judicial effectiveness, as the relatively low density of judges per the population is an indicator of a need for improvement.

The situation is different with regard to the police, as measured by the number of police officers per the population in The Bahamas. Even though that level is already high, the performance of the police is not on par with the highest standards. As a law enforcement institution, the police should have legitimacy built on effectively guaranteeing police presence across the entire territory of the country, and by increasing the professional quality of police officers rather than just increasing their number. The establishment of the Office of the Public Defender and efforts to create the Office of Ombudsman are good signals for the consolidation of rule of law institutions in The Bahamas.

Human capital accumulation constitutes a key foundation for economic growth and for the proper development of both rule of law and political institutions. In The Bahamas, institutions supporting human capital development are on a relatively good path. There are good schooling outcomes in terms of attainment and access, even though the archipelagic profile and distribution of the population make the delivery of quality educational services a challenge. Additionally, the methodology for teacher evaluation would benefit by considering the calculation of individual teacher value-added measures based on objective academic performance of students. The Bahamas has relatively good health outcomes, performing in accordance with its level of public health expenditures. However, the effectiveness of health practitioners could be measured more objectively by introducing performance-based incentives. In general, continued investments in education and health, enabled by sound economic performance, could enhance the development of The Bahamas.

Institutions regulating and fostering economic activity constitute another main engine of a country's institutional framework. Independence and transparency of central banks influence their credibility and effectiveness in controlling inflation, thereby providing a proper environment for economic growth and prosperity. It is therefore highly relevant to ensure technical independence as well as transparency mechanisms for the Central Bank of The Bahamas.

On the fiscal front, the main challenge is to effectively establish fiscal rules and supporting institutions, namely an independent fiscal council. These are key factors to tackle the current high government debt and fiscal imbalances, as well as to guarantee credibility and inter-generational

equity in the long run. The principal areas of public sector weaknesses in The Bahamas are the wage bill and the mounting transfers to indebted state-owned enterprises. The not-properly-financed National Health Insurance (NHI) program is an additional fiscal burden.

The Bahamas would benefit considerably from greater credibility of its budget. Actual expenditures should be more aligned with the budget. Furthermore, comprehensiveness and transparency could be enhanced by providing better information on extra-budgetary expenditures or funds. Enhancing transparency in public procurement processes is critical. Issuing competitive tenders, recruiting highly qualified procurement staff, and publicizing information on procurement processes and awarded contracts should be prevalent practices. All these aspects point to areas of institutional capacity and design that could be improved.

The economy of The Bahamas needs continued emphasis on diversification, mostly within the tourism segment. Oversight of fair trade practices, protection of minority investors, and improvements in the ease of registering property and getting credit are current issues that need to be addressed to promote entrepreneurship, investment, and growth.

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Barbados

Kimberly Waithe and Juan Pedro Schmid

10.1. Political Institutions

Parliamentary democracy in Barbados is closely modelled to that of the British Westminster system. The country has one of the oldest Westminster-style Parliaments in the Western Hemisphere dating to the 1600s. Independence from the United Kingdom was granted on November 30, 1966. Still, the country recognizes Her Majesty Queen Elizabeth II as the head of state, with the governor general being appointed by the monarch and serving as a vice-regal representative.

The Parliament of Barbados has a bicameral legislature. The House of Assembly (lower house) has 30 members who are directly elected by plurality vote in single-member constituencies to serve five-year terms. The party winning the most seats in the House of Assembly will then become the ruling party. The leader of that party becomes the prime minister and head of government. The party that attains the second highest number of seats in the House of Assembly is called the opposition.

The Senate (upper house) has 21 members, and they are appointed by the governor general, 12 on the advice of the prime minister, two on the advice of the leader of the opposition, and seven at the discretion of the governor general (Constitution of Barbados, Section 36). Members of both houses in the legislature can be reelected (lower house) or reappointed (upper house) during an unlimited number of periods.

Executive powers are exercised by the prime minister, who presides over the Cabinet and chooses its members from either the House of Assembly or Senate. Despite the bicameral Parliament, considerable power is concentrated in the executive. The controlling function of the Senate is moderate; most members of the upper house (senate) are nominated on advice of the prime minister, and the Senate can slow passage of laws but does not have any veto power to reject them.

10.1.1. *Political Parties and Background*

Since the introduction of universal suffrage in 1951, governmental power has switched between the Barbados Labour Party (BLP), founded in 1938, and the Democratic Labour Party (DLP), founded in 1955.

Both the DLP and BLP are considered “centrist social democratic parties” with origins in the British Labour movement. Both parties have strongly supported private enterprise and undertaken large public works, recognizing them as essential drivers of development (Meditz and Hanratty 1987). In foreign policy, both parties have endorsed and coordinated regional integration initiatives. Since the 1960s, party differentiation has been mainly in style and rhetoric as well as in leaders’ personalities, but because of the common origin there is no fundamental difference in ideology between the two parties. Neither the BLP nor the DLP are associated with a specific ethnicity or religion; it is worth noting that over 90 percent of the population in Barbados is of African descent.

A third relatively newer party that appeared in the political scene, the National Democratic Party (NDP), was formed in 1989 by former DLP members and won one seat in the 1994 elections. However, the NDP did not compete in any further elections. Table 10.1 summarizes the profiles of the main political parties in Barbados.

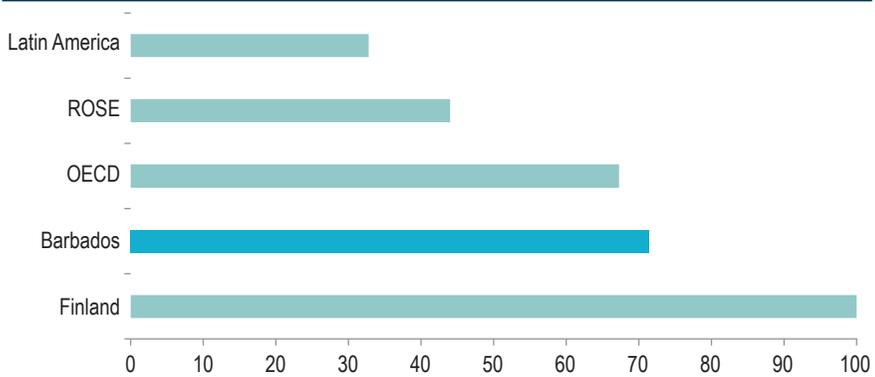
Barbados has a stable parliamentary democracy based on a bipartisan political system. Even though the DLP came as a more left-leaning alternative to the BLP, there are no fundamental social roots for political conflict between these two parties’ voter bases. Consequently, both parties have pursued similar goals, displaying agreement rather than polarization on central issues for economic development.

Table 10.1 Profiles of the Main Political Parties in Barbados

Name of Party	Initials	Periods in Executive Power since Independence	Ideology	Ethnic Voter Base	Prevailing Religion of Voter Base
Democratic Labour Party	DLP	1966–1976 1986–1994 2008–present	Social democracy, democratic socialism, republicanism	n.a.	n.a.
Barbados Labour Party	BLP	1976–1986 1994–2008	Social democracy, democratic socialism, republicanism	n.a.	n.a.
National Democratic Party	NDP	—	—	n.a.	n.a.

Source: Authors’ elaboration based on www.caribbeanelections.com.

Note: Other very minor parties, with one or two candidates representing them in the 2013 elections, are the People’s Democratic Party (PDC), Kingdom Government of Barbados (KGB), and Bajan Free Party (BFP). n.a. = not applicable.

Figure 10.1 Barbados: Public-Regardedness Index

Source: Authors' calculations based on the database in Berkman et al. (2008).

Notes: Each measure was standardized to obtain an index ranging between 0 (worst performance) and 100 (best performance) using the following formula: $(var - min)/(max - min)$, where *var* is the individual country measure, and the maximum and minimum are the highest and lowest value in the datasets, respectively. Finland is the country with the highest ranking on the Public-Regardedness Index worldwide. OECD: Organisation for Economic Co-operation and Development; ROSE: rest of the small economies of the world.

Barbados enjoyed a relatively smooth post-independence transition. As noted in Chapter 6, Barbados was exceptional in the political stability of its colonial elite, which stayed as a legacy for post-independence elites who were in turn influenced by the British Labour movement and sought responsible policies.

Figure 10.1 shows the performance of Barbados on the Public-Regardedness Index, which indicates the extent to which policies pursued are perceived to be in the public interest or whether they tend to be directed toward special interest groups.¹ Barbados outperforms the averages for Latin America, the rest of the small economies of the world (ROSE), and the Organisation for Economic Co-operation and Development (OECD), providing evidence of the favorable features of its political background explained above.

The next section analyses the relevant rules and institutions in place to guarantee wide political representation and transparency in electoral processes.

¹ As explained in Chapter 6 of this volume, the Public-Regardedness Index was proposed in Berkman et al. (2008). The authors computed this index using expert evaluations and perceptions on issues related to (1) corruption, (2) public spending on social transfers, and (3) whether government contracts are awarded fairly or generally favor well-connected firms and individuals. The index is the combination of these three measures. The first component was taken from Transparency International Corruption's Perceptions Index, and the last two components from the Global Competitiveness Report.

10.1.2. *Political Representation, Competition, and Transparency in the Political System*

Countries are more likely to establish appropriate economic institutions that in turn spur development when they have an open, pluralistic political system with competition for political office, a widespread electorate, and openness to new political leaders (Acemoglu and Robinson 2012). As such, it is important to assess the extent to which political participation is widely accessible or whether rules and institutions restrict participation to a minority elite. Answering this requires an inspection of the process by which political parties appoint their leaders and electoral candidates.

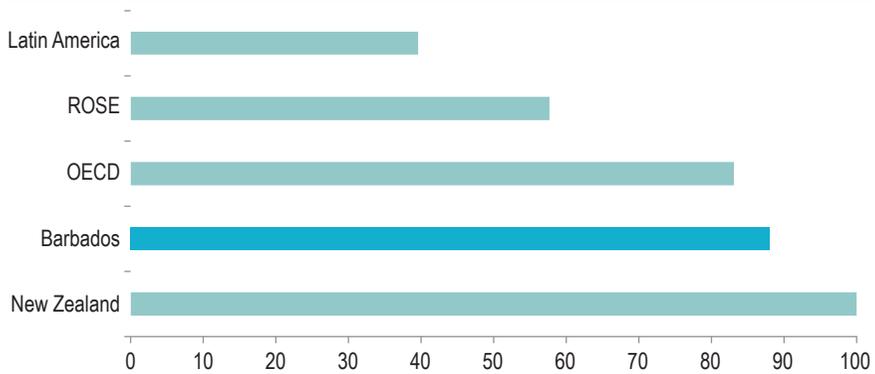
Historically, candidacy for the House of Burgesses (the former Barbados Parliament) was conditional on property ownership until the *Representation of the People (Amendment) Act* of 1950. This bill gave all persons aged 21 and above the right to vote and contest elections “without any income or property qualification.”² Currently, registered electors are 18 years of age and over.

Parties have their own guidelines and rules for electing candidates. In the DLP, the Executive Council selects a candidate within the party and the General Council ratifies that candidate in consultation with the Management Committee.³ In the BLP, persons submit their intent to serve a constituency to the party’s Management Council. Thereafter, a nomination election is held and the candidate who receives the most votes wins the nomination to represent the constituency. This nominee is then ratified by the management body of the party.

There are no gender/minority quotas for defining lists of candidates for the final composition of Parliament. Regarding party leaders, members of Parliament (MPs) within the parties are usually the ones electing their leader who should become the prime minister (or chief of government). Nonetheless, mechanisms of internal party democracy could still be improved in instances where party members are not included in the process to select party leaders. As shown by the control of corruption dimension of the World Bank’s World Governance Indicators in Figure 10.2, Barbados performs better than the OECD and other reference country groups. Furthermore, this indicator reflects, among other things, the extent to which the state is captured by elites and private interests, which for Barbados seems to be practically non-existent.

² Source: Barbados Parliament website. Available at: <http://www.barbadosparliament.com>.

³ See the DLP website at <http://dlpbarbados.org/site/candidate-selection-coming-soon/>.

Figure 10.2 Barbados: Control of Corruption

Source: World Bank, 2017 World Governance Indicators database (www.govindicators.org).

Notes: Percentile ranking score ranging from 0 (worst in controlling corruption) to 100 (best in controlling corruption). New Zealand is the best country worldwide in terms of controlling corruption. Control of corruption captures perceptions of the extent to which public power is exercised for private gain, including both petty and grand forms of corruption, as well as “capture” of the state by elites and private interests.

General elections in Barbados are held at least every five years, with the most recent one in 2018. Barbados is divided into 30 constituencies, and voters in each constituency elect one MP to send to the House of Assembly. It is the responsibility of the Electoral and Boundaries Commission (E&BC) to review the boundaries of the constituencies that make up the country.⁴

The E&BC is also responsible for handling voter registration, conducting elections in every constituency, and enforcing transparency during elections. The E&BC is a department under the Cabinet Office of government. The chairman, deputy chairman, and members of the commission are appointed by the governor general.⁵ To date, international observers have not been part of the electoral process in Barbados.

Even though there may not be fundamental sources of social conflict in Barbados, and figures above indicate there is a good degree of political representation, democracy could be significantly strengthened by guaranteeing full independence to the E&BC. In particular, a best practice should involve guaranteeing complete independence of the E&BC from the incumbent government and parties that the commission is meant to oversee.

⁴ The electorate in each constituency shall, so far as practicable, not exceed 115 percent, nor be less than 85 percent, of the average electorate per constituency.

⁵ The chairman is appointed by the governor general, on recommendation of the prime minister in consultation with the leader of the opposition. The deputy chairman is appointed by the governor general, acting on the recommendation of the opposition leader after consultation with the prime minister.

The voter registry in Barbados is continuously updated and, over the last decade, there has been an increase in voter registration. Voter turnout averaged around 62 percent between 2003 and 2013, and elections have been carried out peacefully.

The next section reviews the extent to which political institutions can place effective constraints on the executive.

10.1.3. *Constraints on the Executive and Accountability*

The checks and balances that the legislative power can use over the executive are limited by several factors in Barbados. Both houses (House of Assembly and Senate) debate all legislation. The House of Assembly can overrule the Senate's rejection of money bills and other bills except for bills amending the constitution.⁶ However, the prime minister presides over the Cabinet and advises the governor general to appoint 12 of the 21 members of Senate (some of whom may be members of the Cabinet). In addition, members of the majority government in the House of Assembly may also be sitting on the Cabinet.

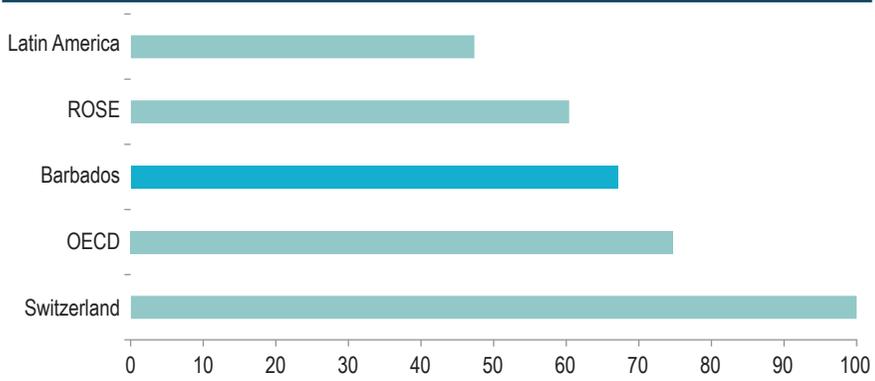
As it is set out in the constitution, Parliament is dissolved by the governor general acting on the advice of the prime minister. Moreover, the prime minister is the person controlling the appointment and advising the governor general for the removal of the ministers.⁷ At the same time, there is a process of impeachment in Barbados. The prime minister holds office subject to a vote of no confidence successfully held against him or her. Section 66(2) of the constitution notes that within three days of the passing of the resolution in the House of Assembly asking the appointment revocation, the prime minister can either resign or advise the governor general to dissolve Parliament. This process took place in 1994, when the prime minister instead decided to call general elections two years before they were constitutionally due, resulting in the opposition getting control over the government.

10.2. Rule of Law Institutions

As shown in Chapter 4, three key institutional rule of law components show a significant causal relation with economic growth. The first relates to the strength of property rights enforcement, protecting private agents from the risk of having their property expropriated by either government or powerful elites. The second relates to respect for the constitution and

⁶ See Sections 55 and 56 of the constitution on "restrictions on powers of Senate as to Money Bills and Bills other than Money Bills."

⁷ Section 66(3b) of the constitution.

Figure 10.3 Barbados: Strength of Property Rights Index

Source: World Bank, 2017/2018 Global Competitiveness Index database.

Notes: Each measure was standardized to obtain an index ranging between 0 (worst performance) and 100 (best performance) using the following formula: $(var - min)/(max - min)$, where *var* is the individual country measure, and the maximum and minimum are the highest and lowest value in the datasets, respectively. Switzerland is the country with the best performance on the index worldwide.

fundamental rights. The third refers to the possibility of obtaining fair and independent administration of justice with the capacity to enforce the law without external pressures. This section assesses the condition of these institutions in Barbados.

10.2.1. *Strength of Property Rights*

According to the Property Rights Index measured by the World Economic Forum's 2017/2018 Global Competitiveness Index, property rights protection in Barbados is better than the Latin American and ROSE averages, as depicted in Figure 10.3. Still, there is room for improvement if the benchmark of most developed countries is considered. In this regard, the World Bank's *Doing Business Report* points to challenges in key areas in Barbados that include protection of minority investors, enforcement of contracts, and property registration.

Beyond property rights, respect for and protection of fundamental human rights constitute underlying conditions for development and social cohesion. The next subsection assesses these issues.

10.2.2. *Protection of Fundamental Human Rights*

The Constitution of Barbados clearly establishes respect for fundamental rights and equal treatment of Barbadian citizens.

Table 10.2 Protection of Fundamental Rights in Barbados

Fundamental Rights	Barbados	Latin America	ROSE	OECD
Overall Fundamental Rights	0.79	0.58	0.62	0.76
4.1 Equal treatment and absence of discrimination	0.75	0.51	0.62	0.70
4.2 The right to life and security of the person is effectively guaranteed	0.91	0.61	0.67	0.86
4.3 Due process of law and rights of the accused	0.63	0.46	0.56	0.73
4.4 Freedom of opinion and expression is effectively guaranteed	0.72	0.61	0.59	0.74
4.5 Freedom of belief and religion is effectively guaranteed	0.88	0.75	0.71	0.76
4.6 Freedom from arbitrary interference with privacy is effectively guaranteed	0.87	0.52	0.51	0.77
4.7 Freedom of assembly and association is effectively guaranteed	0.82	0.66	0.71	0.79
4.8 Fundamental labor rights are effectively guaranteed	0.77	0.56	0.60	0.71

Source: World Justice Project (WJP) (<https://worldjusticeproject.org/our-work/wjp-rule-law-index/wjp-rule-law-index-2016/factors-rule-law>).

Note: Scores for the WJP Rule of Law Index, as well as for its component factors and subfactors, range from 0 to 1, where scores closer to 1 indicate better performance.

According to the 2016 World Justice Project Rule of Law Index, Barbados performs favorably in the protection of fundamental human rights. Across all subfactors shown in Table 10.2, the island ranked above the ROSE and Latin American averages. Moreover, when compared with the OECD average, Barbados' scores are on par. Particularly, the right to life and security of the person received a score of 0.91 out of 1. Similarly, adherence to fundamental rights such as freedom of belief and religion, freedom from arbitrary interference, and freedom of assembly and association all received scores above 0.80. The due process of law and rights of the accused was the lowest performer of all fundamental rights in Barbados with a score of 0.63, but still above Latin America and ROSE levels.

The independence and effectiveness of the judiciary are central to the sustainability of fundamental rights protection, since defense of the constitution is the judiciary's mandate in Barbados and, as such, the judiciary should be institutionally shielded from any government influence. As will be explained next, there is scope for improvement in this regard in Barbados.

10.2.3. *Judicial Independence and Effectiveness*

In Barbados, the institutions supporting the process of administration of justice are the Office of the Director of Public Prosecutions (DPP) and the judicial system.

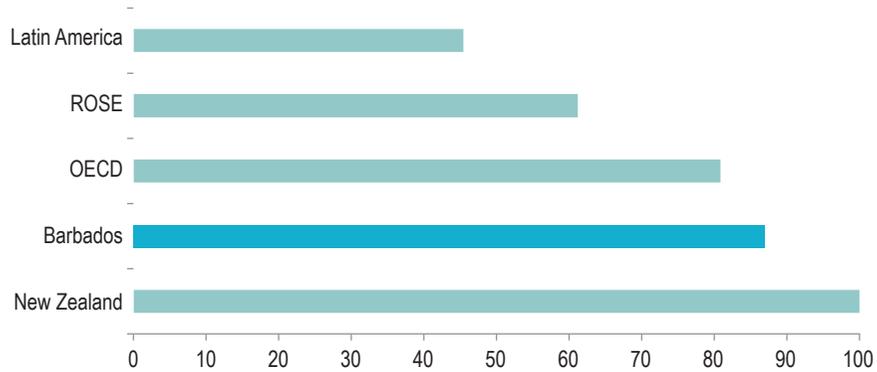
Subject to the constitution, the director of public prosecutions shall not be subject to the direction or control of any other person or authority, except for the attorney general, who holds a ministerial rank and may give directions to the director of public prosecutions in the case of certain offences.⁸ While the Department of Public Prosecutions is independent as set out in the constitution, it is dependent on government for financing (falling under the ambit of the Office of the Attorney General) and for appointments, indirectly. As such, appointment of legal professionals to office of the DPP is subject to an interview process by the Judicial and Legal Service Commission.⁹ In turn, members of the commission are appointed by the governor general, acting on the recommendation of the prime minister after consultation with the leader of the opposition. It must be noted that crown counsel in the DPP are selected based on an open and meritocratic process that may involve interviews, oral and/or written tests, and/or any other method of selection approved by the Judicial and Legal Service Commission.

A similar degree of independence exists in the judicial system. The Supreme Court comprises the Court of Appeal and the High Court, with both courts headed by the chief justice. The chief justice and other judges of the Supreme Court are appointed by the governor general, on the recommendation of the prime minister after consultation with the leader of the opposition. Magistrates Courts are appointed by the governor general with the advice of the Judicial and Legal Service Commission, whose members, as stated earlier, are themselves nominated on the advice of the chief of government after consultation with the opposition leader. Judges usually hold office until they reach a particular retirement age as set out in the Constitution. The judicial system's budget falls under the Office of the Attorney General and the Cabinet Office, whereby budget estimates are submitted to the Ministry of Finance and approved by Parliament.

Despite the limits to judicial independence mentioned above, Barbados performs relatively well on the Judicial Independence Index of Berkman et al. (2008) when compared with other reference country groups (Figure 10.4). This index is calculated considering the extent to

⁸ This includes offences relating to piracy; trading or otherwise dealing in slaves; foreign enlistment; publications calculated to interfere with the peaceful relations of Barbados with foreign states; high treason, treason, misprision of treason, or treachery; sedition or seditious meetings; official secrets; mutiny or incitement to mutiny; unlawful oaths; and any offence under an enactment relating to any right or obligation of Barbados under international law (Constitution of Barbados, Section 79A).

⁹ Section 89(1) of the constitution deals with the establishment and composition of the Judicial and Legal Service Commission.

Figure 10.4 Barbados: Judicial Independence Index

Source: Authors' calculations based on the database in Berkman et al. (2008).

Notes: Each measure was standardized to obtain an index ranging between 0 (worst performance) and 100 (best performance) using the following formula: $(var - min)/(max - min)$, where *var* is the individual country measure, and the maximum and minimum are the highest and lowest value in the datasets, respectively. New Zealand is the country with the highest Judicial Independence Index score worldwide.

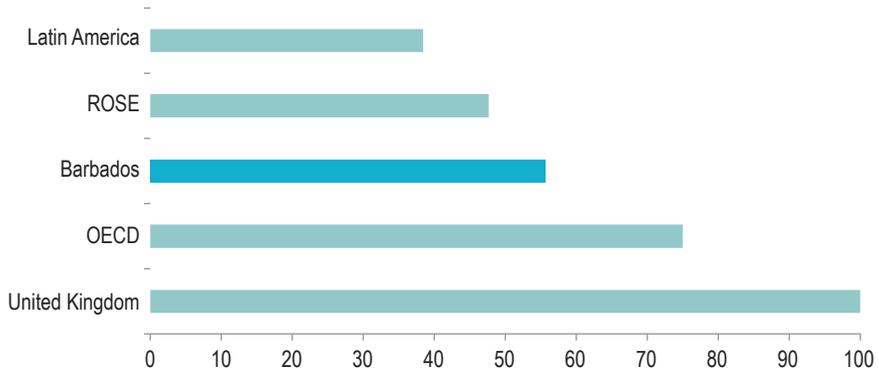
which the judiciary has not been subject to interference by the government and/or parties in dispute. The index is thus an outcome variable that, in the case of Barbados, most likely reflects the absence of rent-seeking behavior, political polarization, and conflict in the incentive structure of political actors. However, it does not necessarily denote fully institutionalized independence that can isolate the administration of justice from improper influence if such types of incentives arise.

The DPP and the judicial courts are sufficiently open and close for citizens to access them. On a different front, the system seems less effective in terms of civil justice enforcement and, generally, in delivering timely processes.

It was estimated in 2012, that there was a backlog of more than 3,000 cases, which led to several actions.¹⁰ Among others, in 2014, a code was established for public prosecutors to provide greater transparency in the legal process and promote better relationships with the press and the public. This code establishes clear guidelines to prosecute individuals in Barbados and to ensure structured decision-making, with an aim to assist with speedier prosecutions and greater transparency and objectivity in the criminal justice system.

There is a perceived need for more security around the Magistrates' Courts, particularly when dealing with high-profile cases. While judges

¹⁰ It was proposed the restarting of the Backlog Reduction Project, which at the outset is to address civil cases filed in the High Court between January 1, 1990 and September 30, 2009.

Figure 10.5 Barbados: Judicial Effectiveness Index

Source: Authors' calculations based on the 2017 Heritage Foundation Index of Freedom (www.heritage.org) database.

Notes: Each measure was standardized to obtain an index ranging between 0 (worst performance) and 100 (best performance) using the following formula: $(var - min)/(max - min)$, where *var* is the individual country measure, and the maximum and minimum are the highest and lowest value in the datasets, respectively. The United Kingdom is the country with the highest Judicial Effectiveness Index score worldwide.

have been afforded a security officer, this is not usually the case for magistrates. Figure 10.5 shows an intermediate level of judicial effectiveness in Barbados. While more effective than Latin American and ROSE peers, Barbados is significantly below the OECD average, which confirms that significant improvements could be made in this regard.

The next subsection assesses the institutional capacity to enforce the law. Hence, it focuses on the police as the main institution for law enforcement.

10.2.4. Law Enforcement

Founded in 1835, the Royal Barbados Police Force (RBPF) is the law enforcement arm in Barbados and currently falls under the ambit of the Office of the Attorney General, who holds a ministerial rank.

The Police Service Commission is responsible for the recruitment of police officers. There is a meritocratic process behind the appointment of the heads of the RBPF. The selection process may involve interviews, oral and/or written tests, and/or any other method of selection approved by the Police Service Commission. Officers are assessed based on relevant qualifications and professional training, experience, and general suitability, among other considerations. The commissioner of police is appointed by the governor general, acting on the recommendation of the Police Service Commission in consultation with the prime minister. In turn, members of the Police Service Commission are appointed by the governor general,

acting on the recommendation of the prime minister after consultation with the leader of the opposition.

The RBPF has an approximate staff of 1,400 officers, which represents 496 officers per 100,000 population (Bailey 2016). In 1995, Barbados established a Criminal Justice and Research and Planning Unit. The mission of this unit is to provide scientific identification of the range of factors related to crime and criminality, and to undertake evaluative research of current systems for managing criminal justice data.

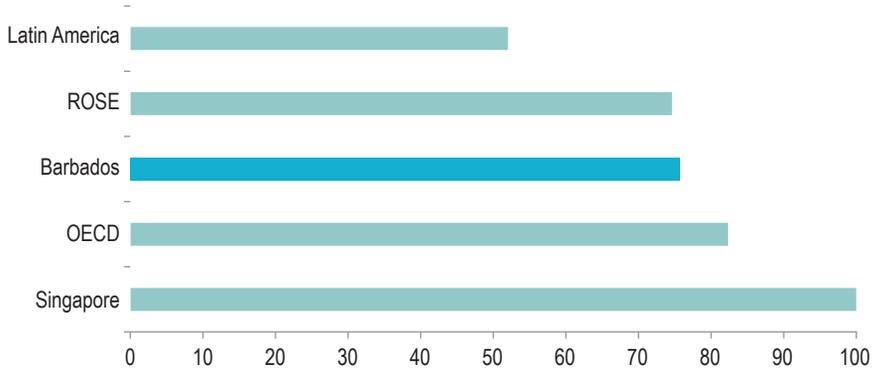
Evidence from the 2014 Caribbean Crime Victimization Survey reported in Sutton and Alvarez (2017) suggests that Barbadians are relatively satisfied with police performance. Approximately 76 percent of respondents in Bridgetown felt either very satisfied or satisfied with the performance of the police in their neighborhoods. Accordingly, survey data indicate that the RBPF has a relatively low incidence of corruption, all of which is reflected in relatively low levels of distrust in the institution.¹¹

The Police Complaints Authority is responsible for monitoring investigations by the RBPF of complaints in order to ensure that the investigation is conducted impartially. Alternatively, it is responsible for undertaking the direct investigation of complaints where it thinks necessary. The authority is comprised of members appointed by the governor general on the advice of the attorney general; one person appointed by the governor general at his or her absolute discretion; one person who is a former police officer and is appointed by the governor general on the advice of the Police Force Association; and the head of the Civil Service, *ex officio*. The authority lacks full independence and, in some cases, plays only a monitoring role on investigations conducted by the police against its own officers. Independence should be the fundamental feature of any investigative unit seeking to hold the police accountable. It must be also noted that complaints made directly to the police still outnumber those received by the authority, which is an issue that needs to be addressed. In 2016, the RBPF's Office of Professional Responsibility received 102 complaints versus 19 made to the authority.

Security and order within Barbados is on par with ROSE but underperforms the OECD, according to the World Justice Project (Figure 10.6). Even though the sub-dimension measuring effective control of crime received an outstanding score in Barbados of 0.91 (out of 1), above that of other country groups, the likelihood of resorting to violence to solve personal grievances seems to be relatively high in contrast to ROSE and the OECD, thus yielding this intermediate outcome in the overall Order and Security Index.

¹¹ See Chapter 7 of this volume.

Figure 10.6 Barbados: Order and Security Index



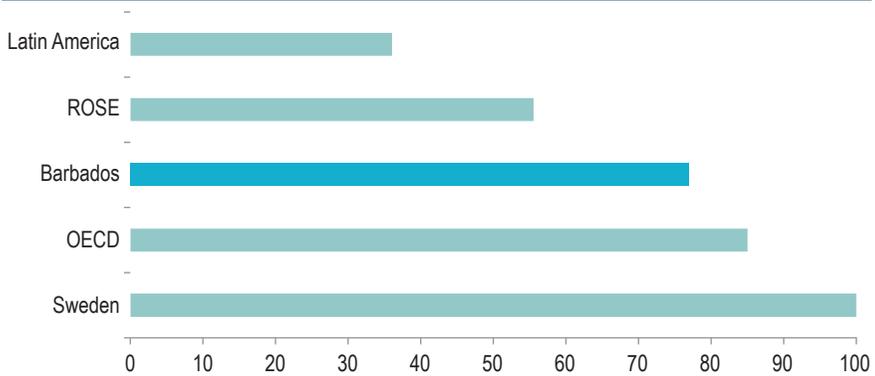
Source: Authors' calculations based on the 2016 World Justice Project database.

Notes: Each measure was standardized to obtain an index ranging between 0 (worst performance) and 100 (best performance) using the following formula: $(var - min)/(max - min)$, where *var* is the individual country measure, and the maximum and minimum are the highest and lowest value in the datasets, respectively. Singapore is the country with the highest Order and Security Index score worldwide.

Overall, this section has shown that institutions related to the rule of law in Barbados perform relatively well in comparison with the Latin American and ROSE averages, but there is still scope for improvement. More significant areas of improvement relate to effectiveness and independence in the administration of justice, and accountability mechanisms of law enforcement institutions.

Indeed, as shown in Figure 10.7, the 2017 Rule of Law dimension within the World Bank's World Governance Indicators summarizes this performance

Figure 10.7 Barbados: Rule of Law



Source: World Bank, 2017 World Governance Indicators Database (www.govindicators.org).

Notes: Percentile ranking score ranging from 0 (worst in rule of law) to 100 (best in rule of law). Sweden is the best country worldwide in terms of the rule of law. Rule of law captures perceptions of the extent to which agents have confidence in and abide by the rules of society, and in particular the quality of contract enforcement, property rights, the police, and the courts, as well as the likelihood of crime and violence.

in Barbados, which is above Latin America and ROSE but still below OECD levels. Working on the main weaknesses documented in this section, while deepening the relative strengths, should be an important avenue for promoting further development in Barbados based on sound rule of law institutions.

10.3. Institutions for Human Capital Development

As shown in Chapter 4, two main institutions supporting human capital development have been highlighted in the literature: institutions relating to education and health. Therefore, this section documents the condition of these institutions in Barbados.

10.3.1. Education

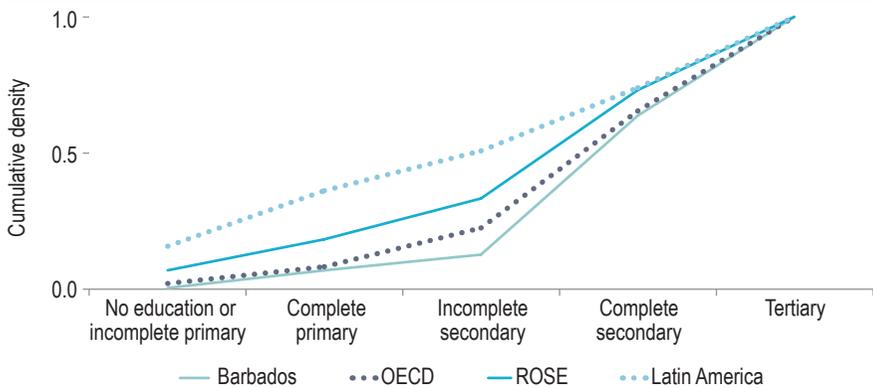
The related evidence presented in Chapter 4 suggests that the quality of education matters more than the quantity. Furthermore, the quality of education hinges primarily on the quality of teachers. Therefore, this section will focus not only on the ability of educational institutions to provide educational service coverage, but also on the state of institutions directed toward ensuring appropriate teacher quality in Barbados.

Barbados has universal coverage at the pre-primary, primary, and secondary education levels.¹² In addition, transport in public buses are free for primary and secondary school students. At the tertiary level, the government provides partial grant funding. Starting in the 2014–2015 academic year, students were required to pay around 20 percent of the annual cost of their programs at the University of West Indies (Cave Hill Campus). The educational system in Barbados also includes several private primary and secondary schools along with tertiary institutions, which in general provide an education similar to that of the public institutions.

Gross enrolment ratios in Barbados are high, according to the United Nations Development Programme's *2016 Human Development Report*: 84 percent in preschool, 94 percent in primary, and 109 percent at the secondary level (UNDP 2016). At the tertiary level, this ratio stood at 65 percent. As a result, 92.6 percent of the population in Barbados older than 25 years of age has at least a secondary education.

The good stand of coverage and educational attainment in Barbados is depicted in Figure 10.8, where the working-age population (25–65 years old) in Barbados is mostly concentrated in the highest schooling levels, advantaging the other benchmark country groups.

¹² Students are only responsible for minor fees and textbook expenses.

Figure 10.8 Barbados: Educational Attainment

Source: Authors' calculations based on the 2016 Barbados Survey of Living Conditions and the World Bank's 2016 World Development Indicators database.

Note: Educational attainment is measured among working-age adults (25–65 years old) who have completed their formal education.

In terms of effective institutions directed toward incentivizing better teaching quality, Chapter 4 has suggested that the critical institutional components appear to be the monitoring of teachers' effort and quality, and performance-based hiring and retention decisions.

The Ministry of Education, Science, Technology and Innovation (METI) in Barbados is generally responsible for quality monitoring and assurance of the public education system. It is a requirement of the *Education Act*, Cap. 41, that private schools also meet the standards set by the minister and that they be registered as having done so. The ministry has structured mechanisms for evaluating the quality of teachers: the evaluation period is continuous and systematic for a period of one year and should be conducted every three years for all appointed teachers. The teacher shall be observed on at least two occasions during the evaluation period before the final report is written.¹³ However, standardized and independent annual evaluations of students across all grades toward calculating teacher value-added measures do not exist. This is highly relevant because

¹³ The steps of evaluating public school teachers include a pre-conference, observation, and post-conference sessions (Ministry of Education, 2018). During the pre-conference session, the evaluation team meets with the teacher to discuss the proposed lesson plan and the areas of focus of the teacher. This action should take place no less than one day before the observation lesson (a classroom observation is not to take place unless a pre-conference has been held). During the observation, the evaluation team can use the appropriate checklist(s) to guide them. At the end of the observation, a time for a post-conference is determined. At the post-conference session, feedback is given to the teacher being evaluated. This session must take place within

objective evidence provided by Araujo et al. (2016) shows that teacher value-added measures based on student evaluations provide a better measure of teacher effectiveness than traditional teacher assessments based on direct evaluations or observation of teachers.

Teachers are recruited by way of the METI and the Board of Management of the schools. Tenure and career progress of teachers in Barbados are linked to transparent and meritocratic performance measures, as teachers are subject to continuous performance assessment. Teachers who consistently perform at a high quality with the prerequisite tenure and qualifications are more likely to be promoted.

To further ensure quality in the education system, the Curriculum and Assessment Section of the ministry is responsible for management of the national curriculum. This entails supervision of every aspect of teaching/learning in various subject areas at the primary and secondary schools. Officials in that unit “visit classrooms and assist teachers with the development of instructional and lesson plans, observe classroom practices, demonstrate relevant methodology, hold on site workshops and advise on curriculum materials.”¹⁴ Barbados allocates resources for the continual training of public teachers at both the primary and secondary levels within the budget of the METI.

10.3.2. Health

The Ministry of Health (MOH) is the executing agency for the delivery of health care in the public sector with an objective to provide comprehensive health care and ensure that environmental concerns are taken into account in all aspects of national development. The public health system is universally accessible in Barbados. Health care services are provided free at the point of delivery in the public sector and are mainly financed through government tax revenue that is allocated to the MOH.

Public health care provision is well distributed across parishes, but access to the public health system may be still limited due to relatively

14 days after the observation. At the end of the session, the senior member of the assessment team must complete an Interim Report (Form A). After agreement, the teacher being evaluated, and the team leader must sign Form A. Thereafter, arrangements can be made for follow-up observations until the evaluation cycle is completed. At the end of the evaluation cycle, the appraisal team will complete the Final Report (Form B), which will provide a summary record of the teacher's performance based on selected criteria and suggestions for future action. This form also includes a summary position that relates the teacher's performance with the selected criteria. After agreement, the teacher being evaluated, and the team leader must sign the Form B.

¹⁴ See the METI website at <http://mes.gov.bb/Departments/Curriculum-Assessment/>.

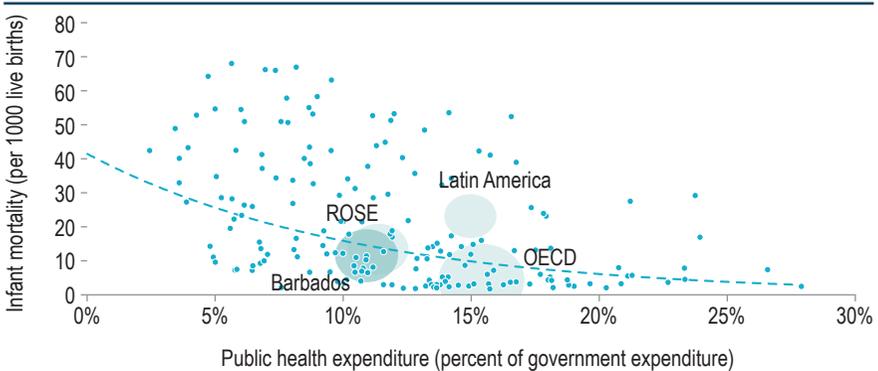
long waiting times, especially if compared with private clinics. The private sector is well developed. It has been estimated that 27 percent of the population is covered by health insurance plans, of which 13 percent were employer-based plans and 14 percent individual-based health plans (Ministry of Health 2015).¹⁵

Public health spending in Barbados has represented around 4 percent of gross domestic product (GDP) over the last five years, very similar to the average 3.9 percent of GDP in ROSE and almost half the amount in the OECD. This highlights the government's commitment to universal access to health care. At the same time, as a share of government spending, the health sector received over 10 percent.

Figure 10.9 shows public health expenditures together with infant mortality rates and physicians per 1,000 population. Barbados has better coverage of physicians per capita than the average for ROSE and Latin American countries. Likewise, infant mortality in Barbados stands at 12 per 1,000 live births, which is a positive outcome when compared with these country groups. Still, Barbados lags the OECD in health performance, although it can be established from Figure 10.9 that the country has similar health outcomes than other countries with equivalent levels of public spending on health.

The MOH is not only the executing agency for the delivery of public health care; it also has responsibility for planning, regulation, and

Figure 10.9 Barbados: Public Health Expenditures, Physicians per 1,000 Population, and Infant Mortality



Source: Authors' calculations based on the World Bank's 2016 World Development Indicators database.

Note: The size of the bubbles is proportional to the number of physicians per 1,000 population for selected countries or country groups.

¹⁵ Based on the 2012–2013 Health Accounts Study in Barbados, which was conducted using the System of Health Accounts (SHA) 2011 methodology.

evaluation across the public, private, and nongovernmental organization sectors. Among other tasks, it is responsible for the assessment, monitoring, and training of the human resource complement in the public sector and tracks the quality of work of public health staff.

Public medical professionals are generally recruited through the Public Service Commission, which is the central human resources agency of the government of Barbados. Vacancies are usually advertised through the relevant institutions, media, and agencies, and the interview process is conducted by senior health care officers and human resources personnel within the various institutions. After this process is completed, the recommended candidates are forwarded to the Permanent Secretary in the MOH; thereafter the recommendation is sent to the Public Service Commission of the Personnel Administration Division for final approval.

Regulation mechanisms in the health sector are well established in Barbados. Importantly, the Barbados Drug Service's programs seek to "encourage equity and allow patients who use either the private or public sector to receive the same quality pharmaceutical products" (PAHO 2008). On a different front, environmental health officers and the various environmental health services units of the MOH have responsibility for environmental sanitation and animal and vector control, among other tasks. Finally, several other units, mainly within the MOH, oversee disease prevention. For example, the Health Promotion Unit and the National Nutrition Centre build capacity for behavioral change among selected groups of the population, and other institutions work on the prevention of chronic diseases.

This section has shown that institutions supporting human capital development in Barbados are on a good path, fostering both coverage and quality in education and health. This constitutes an essential ground for the proper development of the different types of institutions considered in this volume, thus boosting the deepening of democracy, prosperity, and economic growth.

10.4. Economic Institutions

The Barbadian economy has diversified into tourism and financial services. The economy was hard hit by the global financial crisis and recovery has been weak. Expansionary fiscal policies were carried out to stimulate the economy, but this largely raised the overall public deficit and the level of debt. As of March 2018, debt-to-GDP is estimated at 150.5 percent (approximately 175% including arrears). Despite some efforts, the fiscal situation is fragile and economic activity has remained sluggish. Following a build-up in debt-to-GDP and increasing, but insufficient, fiscal measures, expectations are for the authorities to pursue a strong fiscal adjustment program,

possibly with the support of the International Monetary Fund. This section assesses the state of key economic institutions that, as shown in Chapter 5, are associated with increased confidence, investment, and growth.

10.4.1. *Central Bank Independence and Transparency*

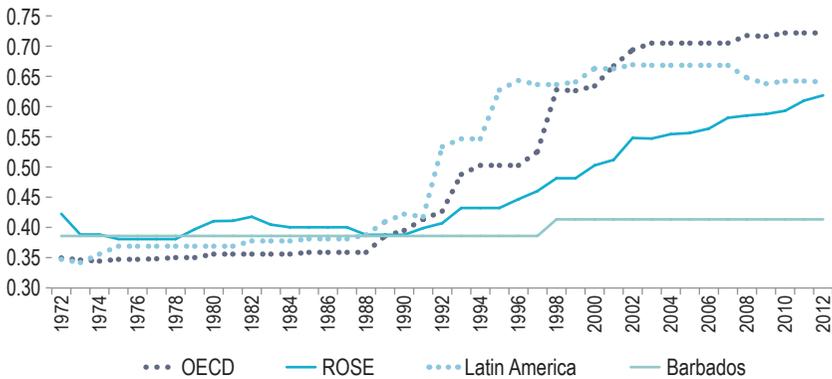
The Central Bank of Barbados (CBB), established in 1972, is governed by a board comprised of the governor and directors. Even though the CBB is a self-funded agency, which allows it to be operationally independent, it is not technically independent. The governor is appointed by the minister of finance for a period not exceeding five years and is eligible for re-appointment. Similarly, directors are appointed by the minister for three years and are also eligible for re-appointment. The minister of finance can issue written orders to the CBB if of the opinion that the “policies being pursued by the Bank are not adequate for, or conducive to, the achievement of the purposes of the Bank” (Central Bank Act, Section 49(1)). Likewise, when a licensee¹⁶ is aggrieved by the decision of the central bank, the licensee may, within seven days after it is notified of the central bank’s decision, appeal to the minister, whose decision is final (Financial Institutions Act, Cap 324A, Section 50(4)). In addition, the minister of finance has the authority to dismiss the governor of the CBB under conditions that are not clearly specified in the Central Bank Act.

Indeed, the CBB ranks relatively low (84th out of 89 countries worldwide) in the measures of central bank independence calculated by Dincer and Eichengreen (2014).¹⁷ Similarly, in a study covering an extended set of countries worldwide, Garriga (2016) ranked the CBB in the 112th position out of 179 countries.¹⁸ In addition, the International Monetary Fund’s 2014

¹⁶ “Licensee” means an entity licensed under the *Financial Institutions Act* (Cap. 324A).

¹⁷ This ranking is based on the Central Bank Independence Weighted Index (CBIW) for 2010 reported in Dincer and Eichengreen (2014). The CBIW is a weighted average of measures related to the following dimensions: CEO appointment (weight = 0.1), policy formulation (0.15), objectives (0.15), limitations on lending to the government (0.50), and appointment of board members (0.1). For details on the specific components of these measures, see Table 18 in Dincer and Eichengreen (2014).

¹⁸ This ranking is for year 2012. Garriga (2016) identified four dimensions concerning the independence of central banks from political influence: who appoints the governor (weight = 0.2); whether there is direct government involvement in policy decisions (weight = 0.15); whether there are limits on the ability of the government to borrow from the central bank (weight = 0.50); and whether price stability is a core objective of monetary policy (weight = 0.15). The weighted average of these dimensions results in a central bank independence index ranging from 0 (lowest independence) to 1 (highest independence).

Figure 10.10 Barbados: Central Bank Independence Index

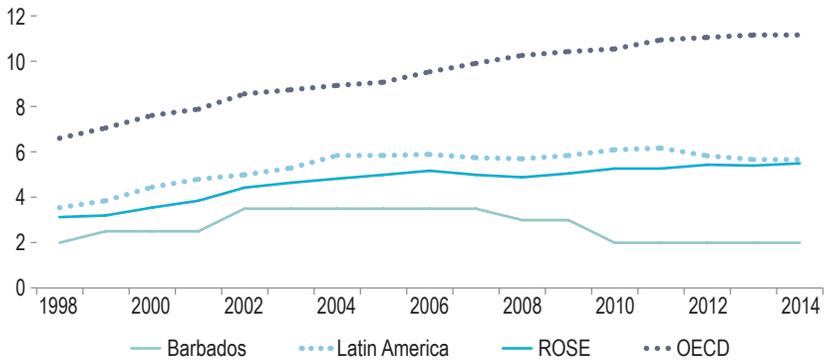
Source: Garriga (2016).

Note: The Central Bank Independence Index ranges from 0 (lowest independence) to 1 (highest independence).

Financial System Stability Assessment (FSAP) recommends strengthening CBB independence to assuage potential concerns (IMF 2014). This relative disadvantaged position, however, has not been an historical norm for the CBB. Figure 10.10 illustrates the evolution of the Garriga (2016) central bank independence index from 1972 to 2012 for Barbados, Latin America, ROSE and OECD member countries. The CBB showed similar independence levels than all other country groups in 1972, but such independence level has not improved over time. By contrast, all other country groups have witnessed continuous improvements over time and, consequently, for year 2012 Barbados lagged all comparators.

Together with budgetary and technical independence of central banks, transparency is a key institutional feature needed to complement the different dimensions of any central bank functions. Openness about policy objectives in the CBB is supported by a formal statement of monetary policy goals. On the CBB website, the Bank maintains a statistical database which is publicly available and includes relevant data for the conduct of monetary policy on a monthly, quarterly and annual basis.¹⁹ While the central bank provides a range for forecasted real GDP

¹⁹ The CBB further publishes annual reports, monthly economic letters and newsletters related to international business and financial services. The CBB, in collaboration with the Financial Services Commission—the regulatory body for non-bank financial institutions in Barbados—also produces the annual Financial Stability Report. The report gives a detailed assessment of risk exposures of banks, insurance companies, credit unions, and other depository financial institutions. In addition, the CBB produces quarterly economic reports that are in conjunction with a press conference held by the governor.

Figure 10.11 Barbados: Central Bank Transparency Index

Source: Dincer and Eichengreen (2014) updated database for central bank transparency, 1998–2014 (https://eml.berkeley.edu/~eichengr/Dincer-Eichengreen_figures&tables_2014_9-4-15.pdf).

Note: The Transparency Index ranges between 0 (lowest transparency) and 15 (highest transparency).

as part of their quarterly economic review, macroeconomic forecasts for several other variables and the macroeconomic model the CBB uses for policy analysis are not available to the public. Moreover, the CBB does not disclose how each decision on the level of its main operating instruments or targets was reached. As a result, the CBB has ranked consistently low over time as measured by the Central Bank Transparency Index (Figure 10.11).²⁰ This contrasts with other country groups such as ROSE, Latin America, and the OECD that have witnessed improving trends in transparency over time. Therefore, the gap in transparency between the CBB and all reference groups has widened significantly between 1998 and 2014.

10.4.2. Fiscal Institutions

The Ministry of Finance is responsible for fiscal management in Barbados. The Medium-Term Fiscal Strategy (2010–2014)²¹ and the Barbados Growth

²⁰ The Central Bank Transparency Index measures compliance with 15 best practices distributed across the following areas: political transparency (three practices), economic transparency (three practices), procedural transparency (three practices), policy transparency (three practices), and operational transparency (three practices). The index ranges from 0 (no compliance at all) to 15 (full compliance with the 15 best practices). For details on the specific practices and index construction, see Appendix 1 in Dincer and Eichengreen (2014).

²¹ Revenue measures introduced in the 2010 Medium-Term Fiscal Plan included an increase in the value-added tax (VAT) from 15 to 17.5 percent, an increase in the excise tax on gasoline, and an increase in bus fares, among other measures. These led to a 12 percent increase in overall revenue, with VAT receipts rising by 23 percent.

and Development Strategy (2013–2020) outlined several objectives.²² These include reducing the fiscal deficit and public debt and ensuring prudent management. However, the weak fiscal situation and debt build-up remain the main challenge for the country, which had a fiscal deficit of 4.2 percent of GDP at the end of FY 2017–2018 and an estimated debt-to-GDP ratio of around 150.5 percent of GDP at the end of March 2018 (inclusive of National Insurance Scheme holdings).

As shown in Chapter 5, fiscal performance worldwide has been shown to improve with the existence of institutions that aim at correcting incentives and containing overspending. If properly established, objective fiscal rules, independent fiscal councils, and sovereign wealth funds provide a medium-term anchor that enhances the credibility of policies and supports inter-generational equity. By contrast, the lack of such institutions makes fiscal mismanagement more likely. Barbados, however, currently has no fiscal rules, formal independent fiscal councils, or sovereign wealth funds in place.

While fiscal responsibility legislation would be beneficial, a comprehensive fiscal rule requires in depth data, technical forecasting capabilities, the ability to analyze sectoral linkages and business cycles, among others, which would take time to develop. In that situation, the fiscal effort could initially focus on fiscal consolidation and on the implementation of a simple debt target to better guide fiscal policy formulation.²³ Progress on this front, would allow for improved capacity and processes required to properly establish fiscal rules and the supporting institutions to guarantee the credibility and sustainability of fiscal policy in the medium and long terms.

10.4.3. *Ease of Doing Business*

As shown in Ruprah and Sierra (2016), private entrepreneurship and innovation are key drivers to boost investment, innovation, growth, and development. Therefore, institutions and regulations that permit and promote private sector development are extremely relevant. This section assesses the state of these issues in Barbados.

²² These objectives included (1) maintaining macroeconomic stability; (2) ensuring strong growth through increased efficiency, productivity, and competitiveness over the medium term; (3) reducing the fiscal deficit; (4) reducing the level of debt and improving the country's credit ratings, leading to reduced debt service costs; (5) maintaining stability in the foreign exchange market and through this action protecting the fixed exchange rate regime; and (6) ensuring that domestic and external confidence in the ability of the government to manage its resources in an efficient and balanced manner is maintained.

²³ IMF (2013), see also IMF (2018) for the most recent IMF recommendations.

According to the World Bank’s 2016 Doing Business Indicators, Barbados faces striking limitations in several areas compared with ROSE, Latin America, and the OECD. As shown in Figure 10.11, these areas are the protection of minority investors, the enforcement of contracts, and dealing with construction permits (which take an average of 442 days in Barbados). Although starting a business seems to be easier in Barbados relative to Latin America and ROSE, the consolidation of such new businesses is likely hampered by the other weaknesses. When compared with the country’s peers, the indicators for Barbados point to challenges in other key areas, including registering a property, getting credit, and trading across borders (Figure 10.12). These indicators suggest the need of policies that develop institutions that support the ease of doing business in the country.

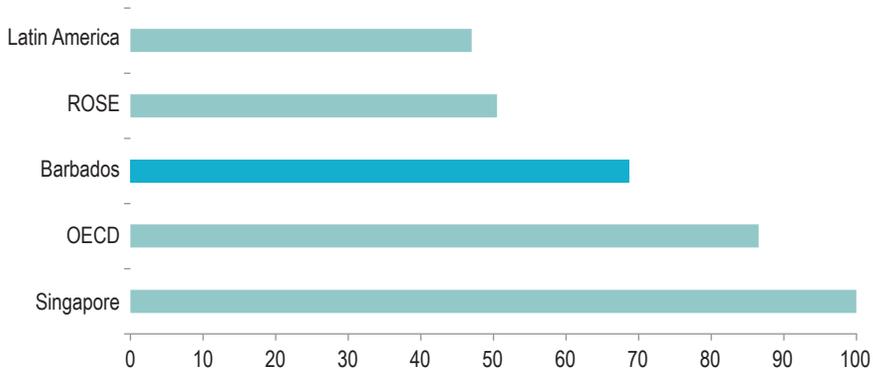
As shown in Figure 10.13, regulatory quality in Barbados is in a better stand than the doing business indicators for the country. Barbados is well above Latin America and ROSE in terms of the quality of regulations aimed at permitting and promoting private sector development, although it is not yet close to OECD levels.

Figure 10.12 Barbados: Ease of Doing Business



Source: World Bank, 2016 Doing Business database.

Notes: Each measure was standardized to obtain an index ranging between 0 (worst performance) and 100 (best performance) using the following formula: $(var - min)/(max - min)$, where *var* is the individual country ranking, and the maximum and minimum are the highest and lowest value in the datasets, respectively. The OECD was taken as the best practice benchmark with a value of 100 in each of the dimensions measured.

Figure 10.13 Barbados: Regulatory Quality

Source: World Bank, 2017 World Governance Indicators database (www.govindicators.org).

Notes: Percentile ranking score ranging from 0 (worst in regulatory quality) to 100 (best in regulatory quality). Singapore is the best country worldwide in terms of regulatory quality. Regulatory quality captures perceptions of the ability of the government to formulate and implement sound policies and regulations that permit and promote private sector development.

10.5. Conclusions and Policy Recommendations

Barbados has enjoyed a stable parliamentary democracy based on a bipartisan political system. The country has a colonial legacy of political stability, and ethnic homogeneity of the population, that have enabled the absence of strong or persistent social or political conflict. Nevertheless, the country could still stand to improve the design and capacity of its institutions, so that stability, wide political representation, and the virtual absence of state capture—current features of the Barbadian political system—become in fact institutionalized and can therefore constitute a formal structure to sustain and deepen democracy.

From the electoral process perspective, full independence for the Electoral and Boundaries Commission would be beneficial. In particular, independence from the incumbent government and parties that the commission is meant to oversee are critical features in need of institutionalization. In addition, inviting international observers as external guarantors of elections would increase the credibility and transparency of democratic processes.

The functioning of rule of law institutions in Barbados reflects the political, historical, and social fundamentals of the country. Hence, in the absence of rent-seeking behavior, political polarization, and conflict within the incentives structure of political actors, rule of law institutions perform well in comparison with Latin America and ROSE. Yet, there is scope for improvement in terms of the formal institutional design pertaining to judicial independence and law enforcement.

Barbados has performed well in the protection of fundamental human rights and the administration of justice on the principle of equality before the law. A fully institutionalized independence of the judiciary would further protect the administration of justice from the influence of other branches of government. Judicial effectiveness and property rights protection could also be strengthened in Barbados, considering the benchmark of most developed countries. Key working areas in the protection of property rights include protection of minority investors, enforcement of contracts, and property registration.

A similar recommendation holds for law enforcement institutions. Although the performance of the Royal Barbados Police Force is relatively satisfactory, the Police Complaints Authority, or any other authority designed for the purpose of holding the police accountable, should be independent from the police force. In addition, such institutions should not only oversee but also undertake investigations of complaints against the police, thereby effectively avoiding conflicts of interests.

Human capital accumulation in Barbados constitutes the best grounds for economic growth and the proper development of both rule of law and political institutions in the country. Human capital institutions, in turn influenced by the degree of the rule of law and political and economic development, are on a good path that has seen the pursuit of both coverage and quality in education and health. Continued investments in these priority sectors, with special focus on enabling mechanisms for objective and standard monitoring of performance to calculate individual value-added measures for teachers and health practitioners, could make the country progress even further along this path.

Institutions regulating and fostering economic activity should be another main engine in the country's institutional framework. The independence and transparency of central banks affect their credibility and effectiveness in controlling inflation, thereby providing a proper environment for economic growth and prosperity. It is therefore highly relevant to ensure technical independence as well as transparency mechanisms in the Central Bank of Barbados, both of which are in relatively weak standing at present. Given the country's high debt levels, financing the deficit has been challenging. New financing has largely been met domestically through the central bank, commercial banks, and the National Insurance Scheme. Particularly, elevated levels of CBB financing has been a cause of concern and exacerbated the pressure on international reserves.

On the fiscal front, the main challenge remains addressing its weak position. In the short term, a debt target with a supporting fiscal adjustment will be necessary to stabilize the Barbadian economy. However, in the

medium to long term, fiscal rules, if properly established, have the potential to increase the credibility and sustainability of fiscal policy. Particularly, Barbados would greatly benefit from higher credibility in the budget. The budget should be a better predictor of actual revenue and expenditure. Furthermore, credibility and transparency could be enhanced by providing better information on arrears and extra-budgetary operations and more detailed expenditures as opposed to aggregates. Barbados would also benefit from a more detailed medium-term fiscal framework that allows for planning and budget execution. Tax liability assessments and exemptions are still subject to discretionary powers of different government entities, effective internal controls are limited, and external scrutiny and audit could be further improved.

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Guyana

Elton Bollers, Kevin Bonnett, and Mark Wenner

11.1. Political Institutions

Guyana adopted a Presidential representative democratic system of government in 1980.¹ The legislature consists of a 65-person unicameral National Assembly, members of which are directly elected by popular vote within democratic processes held every five years. The executive branch consists of the President, cabinet, and government ministries. The President is the head of state, chief executive, and commander-in-chief of the armed forces. The President is elected by the National Assembly² for a five-year term and is eligible for re-election only once.^{3,4}

The President appoints the prime minister, who must be a member of the National Assembly, and members of the cabinet, who may be non-elected but normally are members of the National Assembly. Furthermore, the President has the right to appoint the board members to state-owned companies, chief judicial officers, and a host of commissions, except for the Judicial Service and Rights Commissions. The President can also veto legislation and must assent to bills passed by the National Assembly before

¹ From independence in 1966 until the 1980 constitutional reform, Guyana used the Westminster model of governance inherited from British colonizers.

² Article 91 of the Constitution of the Cooperative Republic of Guyana.

³ Article 90(2) of the Constitution of the Cooperative Republic of Guyana. This provision became effective in 2003 after a constitutional reform process.

⁴ However, there is a pending case in the Caribbean Court of Justice as to whether a Guyanese citizen can run for a third term. Oral arguments were heard on March 12, 2018. A final ruling has not been issued at time of this writing (March 21, 2018). The article 90(2) & (3) amendments to the constitution were enacted by Parliament in 2001 after a bipartisan Constitution reform process. The plaintiff in the current court case claims that Presidential term-limit was unconstitutional without the approval of the people through a referendum.

they become law. The President also has the right to prorogue (suspend) and dissolve the National Assembly at any time by proclamation.⁵

The Guyanese political system in practice is a hybrid Presidential-parliamentary system, unlike most independent Caribbean states (former British colonies) that have a classic Westminster parliamentary system and other Latin American states that have Presidential systems. In Westminster systems, the head of government is normally the prime minister, who is an elected member of Parliament, and the head of state is a ceremonial figure. By contrast, under the Presidential system, the executive leader is the President, who is elected by popular vote. In the Guyanese hybrid model, like Presidential systems but unlike the Westminster model, the President is both the head of government and the head of state. However, like the Westminster model but unlike Presidential systems, the President is not elected by popular vote but by the legislative branch. However, the Guyanese electorate votes for a list of candidates to the National Assembly with a known leader. As such, the leader of the party or coalition winning the majority of seats in the National Assembly would become the President.

11.1.1. *Political Parties and Background*

Since independence in 1966, two main traditional parties with a common socialist ideology but associated with different ethnic groups have dominated Guyanese politics: the People's National Congress (PNC) with an Afro-Guyanese ethnic base, and the People's Progressive Party (PPP) with an Indo-Guyanese ethnic base. There have been two extended periods where these two parties alternated control of government. For the first 26 years of independence the PNC held power, winning four consecutive elections in 1968, 1973, 1980, and 1985. Then, general elections in 1992 resulted in a victory for the PPP. The PPP held power for the next 23 years, winning consecutive elections in 1997, 2001, 2006, and 2011.

In 2006, the PNC undertook an internal restructuring process and renamed the party as the People's National Congress Reform (PNCR). The move was an attempt to recast the image of the PNC. Then in 2011, the PNCR formed an alliance with a set of nine smaller parties and civil society

⁵ Article 70(1) & (2) of the Constitution of the Cooperative Republic of Guyana. No session of the National Assembly shall begin later than six months from the end of the preceding session if it has been prorogued or suspended, and no session shall begin later than four months from the end of a preceding session if it has been dissolved.

organizations called A Partnership for National Unity (APNU).⁶ As such, the APNU is not a political party itself but a coalition of diverse groups. In practice, however, the APNU is dominated by the PNCR, the largest constituent organization in the umbrella grouping.

Finally, a relatively new party, the Alliance for Change (AFC), with a center-left ideology and a constituency composed largely of reform-minded persons of different racial/ethnic backgrounds, emerged in 2005. It was established by former members of both the PNC and PPP.⁷ The AFC contested elections in 2006 and 2011, winning seats in Parliament. During the Tenth Parliament (2011–2014), the AFC formed an informal coalition with APNU and together enjoyed a one-seat majority in the legislature. During this period, both the AFC and APNU voted together as a bloc, effectively thwarting much of the agenda of the Donald Ramator administration (PPP) and leading the standing government to suspend Parliament in an attempt to avoid a vote of no confidence in November 2014. After the dissolution of government and prior to the general elections of 2015, the AFC and APNU formed a formal coalition and fielded a joint ticket. It is worth noting, however, that post-election coalitions between political parties are not allowed by the constitution. Indeed, not even a formal or informal alliance can be formed with the aim to seize the presidency and the government.⁸ At present, the constitution allows the President to form a one-party (minority) government even if his/her party has less than 50 percent of the parliamentary seats.

The multiracial APNU-AFC coalition won the elections with a margin of 4,545 votes, representing the first time since independence that ethnic-based voting was modulated. Table 11.1 summarizes the profiles of the political parties in Guyana that have held power. Note that there are several other smaller parties that have contested elections. In the last general

⁶ The parties and civil society organizations that constitute the APNU are the (1) Guyana Action Party; (2) Guyana Association of Local Authorities; (3) Guyana National Congress; (4) Guyana's People's Partnership; (5) Guyana Youth Congress; (6) Justice for All Party; (7) National Democratic Front; (8) National Front Alliance; (9) Working People's Alliance; and (10) People's National Congress Reform.

⁷ The principal founders of the AFC party were Raphael Trotman of the People's National Congress, Khemraj Ramjattan of the People's Progressive Party, and Sheila Holder of the Working People's Alliance.

⁸ According to the Guyana Constitution, Title 4, The President, Article 177 (2): "A Presidential candidate shall be deemed to have been elected as President and shall be so declared by the Chairman of the Elections Commission (a) if he is the only Presidential candidate at the election or (b) where there are two or more Presidential candidates, if more votes are cast in favor of the list in which he is designated as Presidential candidate than in favor of any other list."

Table 11.1 Profiles of the Main Political Parties in Guyana

Name of Party	Initials	Periods in Executive Power since Independence	Ideology	Dominant Ethnic Group in Voter Base	Prevailing Religion of Voter Base
People's National Congress Reform (Name before 2006: People's National Congress)	PNCR (currently subsumed into a coalition with the AFC)	1966–1992, 2015–present (Government in coalition with the AFC)	Socialist	Afro-Guyanese	Christian
People's Progressive Party	PPP	1992–2015	Socialist	Indo-Guyanese	Hindu
Alliance for Change	AFC (currently subsumed into a coalition with the PNCR)	2015–present (government in coalition with the PNCR)	Center-Left	Multiracial	Christian

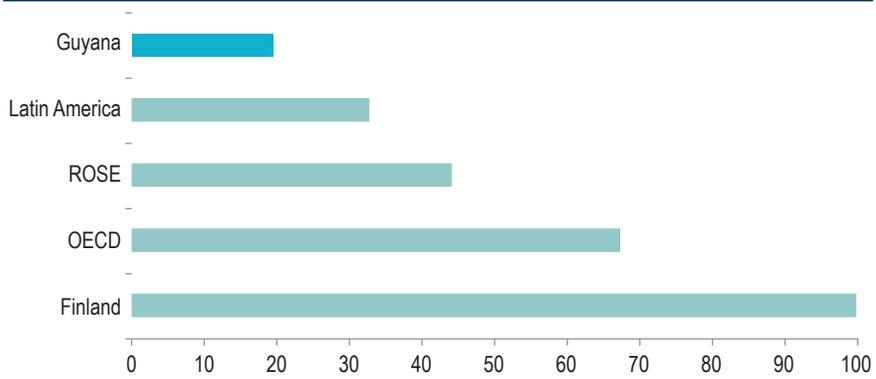
Source: Authors' elaboration based on www.caribbeanelections.com.

elections of 2015, the United Front, United Republican Party, Independent Party, and National Independent Party competed but failed to win seats in the National Assembly.

In summary, Guyana has a political model that concentrates considerable power in the chief executive. Dominant political parties are ethnically fragmented and have concentrated political power for extended periods of time. As shown in Chapter 6, ethnically fragmented political systems have been associated with an increased likelihood of rent-seeking behaviors by dominant elites who could influence policy decisions in their favor. Indeed, Figure 11.1 below shows that Guyana performs poorly on the Public-Regardedness Index, which indicates the extent to which policies pursued are perceived to be in the public interest or whether they tend to be directed toward special interest groups.⁹

The next section turns to analyzing the extent to which relevant rules and institutions in place have guaranteed democratic participation and transparency in electoral processes.

⁹ As explained in Chapter 6 of this volume, the Public-Regardedness Index was proposed in Berkman et al. (2008). The authors computed this index using expert evaluations and perceptions on issues related to (1) corruption, (2) public spending on social transfers, and (3) whether government contracts are awarded fairly or generally favor well-connected firms and individuals. The index is the combination of these three measures. The first component was taken from Transparency International Corruption's Perceptions Index, and the last two components from the Global Competitiveness Report.

Figure 11.1 Guyana: Public-Regardedness Index

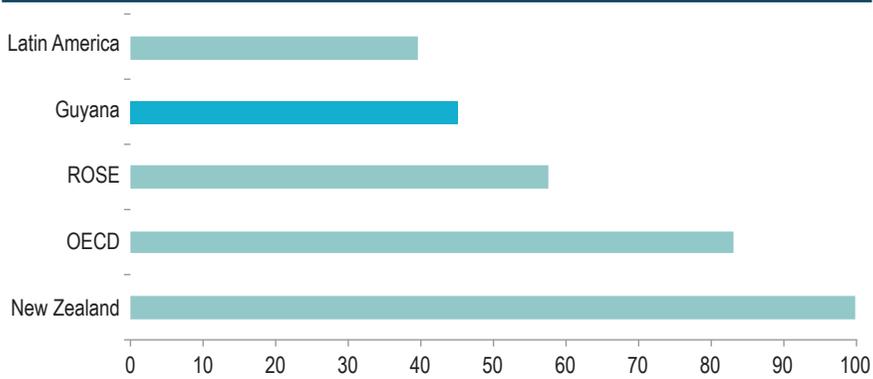
Source: Authors' calculations using the database in Berkman et al. (2008).

Notes: Each measure was standardized to obtain an index ranging between 0 (worst performance) and 100 (best performance) using the following formula: $(var - min)/(max - min)$, where *var* is the individual country measure, and the maximum and minimum are the highest and lowest value in the datasets, respectively. Finland is the country with the highest Public-Regardedness Index ranking worldwide. OECD: Organisation for Economic Co-operation and Development; ROSE: rest of the small economies of the world.

11.1.2. *Political Representation, Competition, and Transparency in the Political System*

Countries are more likely to establish appropriate economic institutions that in turn spur development when they have an open, pluralistic political system with competition for political office, a well-educated electorate, and openness to new political leaders (Acemoglu and Robinson 2012). As such, it is important to assess the extent to which political participation is widely accessible or whether rules and institutions restrict participation to a minority elite. Answering this requires an inspection of the process by which political parties appoint their leaders and electoral candidates.

The first point to note is that both the PNCR and PPP have central decision-making bodies denominated Executive Committees that allow leadership elites (and not the general membership) to select the titular head of the party. As mentioned earlier, the APNU is a coalition or alliance of several parties and its leadership team is comprised of representatives of all the parties in the coalition. However, de facto the PNCR representative is the “first among equals,” since that party has the largest number of registered voters in the coalition, and whoever is the titular head of the PNCR will be at the head of the APNU ballot list. The AFC has a slightly more liberal approach and members directly elect party leaders. However, the leadership elites of the three parties have been quite stable over time. There has been little turnover in the leadership or Executive Committees of

Figure 11.2 Guyana: Control of Corruption

Source: World Bank, 2017 World Governance Indicators database (www.govindicators.org).

Notes: Percentile ranking score ranging from 0 (worst in controlling corruption) to 100 (best in controlling corruption). Control of corruption captures perceptions of the extent to which public power is exercised for private gain, including both petty and grand forms of corruption, as well as “capture” of the state by elites and private interests. New Zealand is the best country worldwide in terms of controlling corruption.

each party. Over the last 15 years the same leaders of both major PPP and PNC parties have dominated the national scene.¹⁰ The election of the parties’ central decision-making bodies called *Executive Committees* resides with the leadership elites and not the general membership. The current constitution of the PPP and PNC places control of the party in the hands of its leaders, not its members. This suggests that openness to new political leaders is relatively low in Guyana.

Candidates for the National Assembly are nominated by the leadership elites of each party. Party discipline is strictly enforced among those elected to the National Assembly by popular vote, thus exerting a high degree of centralized power. Indeed, according to the World Bank’s World Governance Indicators, which measure the extent to which the state is captured by elites and private interests, Guyana has a relatively inferior performance, suggesting a high degree of state capture by minority elites (Figure 11.2).

Open participation in and transparency of electoral processes are central aspects for any democracy. The body charged with administering elections, certifying vote counts, and reporting results is the Elections Commission of Guyana. Established in 2000, the commission is independent of the central government, and the Chairman of the Commission is constitutionally appointed by the President from a list submitted by the Leader of the Opposition. The list must not be

¹⁰ In 52 years since independence, both the PPP and PNC have had only 4 party leaders.

unacceptable to the President.¹¹ For the election cycle of 2015, international observers, which included the Organization of American States, the Caribbean Community (CARICOM), British High Commission, Canadian High Commission, and the Carter Center, certified a transparent process. The national voter participation rate in the 2015 election was 78.9 percent, which is above the average rate for the English-speaking Caribbean countries (70 percent).

In summary, voter turnout and transparency of elections stand within appropriate standards. However, the low levels shown in the public-regardedness and control of corruption indicators, suggest the presence of state capture by minority elites.¹² This occurs within an ethnically fragmented political system that, as shown in Chapter 6, has been associated with relatively lower institutional quality. Within these circumstances and considering the relatively high concentration of power in the executive branch, including the power to suspend Parliament, it is relevant to assess (1) the mechanisms or de jure institutions under which the National Assembly could exert constraints and accountability over the executive; and (2) the extent to which such de jure mechanisms are exercised or translated into de facto institutions.

11.1.3. *Constraints on the Executive and Accountability*

In terms of political control, the National Assembly has the power to remove the President for violation of the constitution, gross misconduct, or incapacity (physical or mental). Nonetheless, this is unlikely to occur given that, as explained above, the President has the right to prorogue (suspend) and dissolve the National Assembly at any time by proclamation. In addition, elected members of the National Assembly must follow party instructions in voting. Indeed, in the 52-years history of independence, there has been no impeachment proceedings and there has only been one National Assembly (the 10th) when the ruling party did not hold a majority.

The National Assembly is legally entitled to exert control over its members. Procedures of the Parliamentary standing orders can sanction or remove a member of the assembly if his/her conduct bring the assembly into disregard or disrepute. The National Assembly can also censor

¹¹ Article 161(2) of the Constitution of the Co-operative Republic of Guyana.

¹² Indeed, Figure 6.1 of Chapter 6 in this volume, ranks Guyana as one of the countries with higher levels of state capture among the Caribbean and the Rest of Small Economies worldwide.

ministers who are not members of it by bringing them before a Privilege Committee. Furthermore, the National Assembly can sanction the minister, even though the sanction does not extend extra-parliamentary, meaning it is not subject to judicial review. If sanctioned, pressure may build on the President to remove him or her. However, either removing or sanctioning ministers require a majority vote in the National Assembly. Finally, the constitution contains a recall provision for any member of the assembly including Ministers to be recalled by their party.¹³

The National Assembly's main accountability procedure in terms of the executive branch is control of budgetary appropriations from the treasury, denominated through the Consolidated Fund. The executive must present an annual budget to the National Assembly and have it approved before April 1 of each calendar year. Any supplemental authorizations or emergency spending need to be approved by the National Assembly. The National Assembly has the right to question ministers on expenditures. In practice, however, these oversight and monitoring functions are not robustly exercised due to the low periodicity of statistical reporting and no institutional support to conduct independent, evidence-based analysis or thorough evaluation of programs and initiatives. Budgets are not analyzed by independent institutions and there is little opportunity to significantly change the presented budget given that the President's party normally holds the majority and the parties are well disciplined.

In summary, while *de jure* political constraints on the executive and accountability mechanisms exist, the *de facto* exercise of such powers by the National Assembly is largely limited and circumscribed.

11.2. Rule of Law Institutions

As shown in Chapter 4, the literature clearly suggests three key institutional rule of law components that show a significant causal relation with economic growth. The first relates to the strength of property rights protecting private agents from the risk of having their property expropriated by either government or powerful elites. The second relates to the fundamental rights embedded in the constitution. The third refers to the possibility of obtaining fair and independent administration of justice with the strength to enforce the law without external pressures. This section assesses the state of these institutions in Guyana.

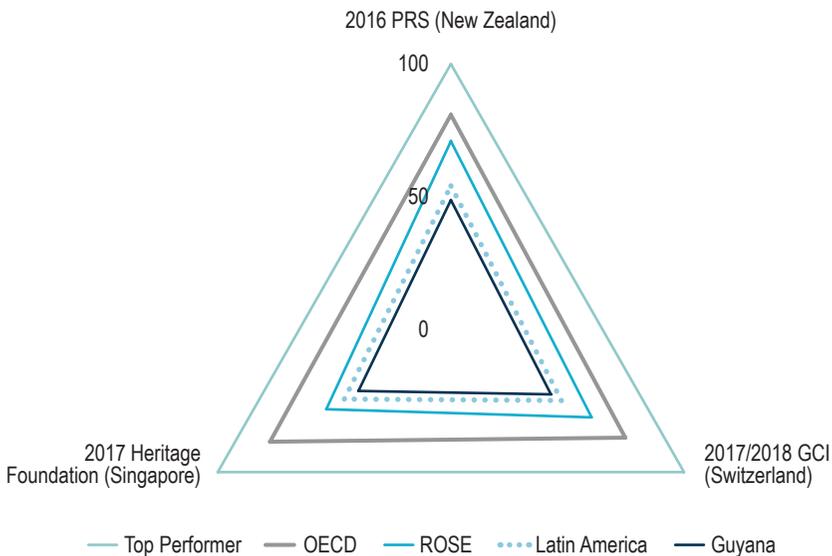
¹³ Article 156 (3) (C) of the Constitution of the Co-operative Republic of Guyana.

11.2.1. Strength of Property Rights

Several international assessments consistently report weaknesses in the institutional arrangements in place to protect property rights in Guyana. The 2016 Index of Protection against Expropriation calculated by Political Risk Services, which objectively assesses this institutional dimension across 140 countries worldwide, suggests low performance for Guyana (Figure 11.3). Similarly, the Property Rights Index that forms part of the World Economic Forum's 2017/2018 Global Competitiveness Index suggests that Guyana significantly underperforms comparable small economies in the rest of the world (ROSE). Furthermore, according to the Heritage Foundation's Index of Freedom for 2017, Guyana underperforms every international benchmark on the subcomponent for protection of property rights.¹⁴

Commonly reported problems include long waits for judicial enforcement of contracts, corruption, favoritism, and violation of intellectual

Figure 11.3 Guyana: Strength of Property Rights



Sources: Political Risk Services (PRS), 2016 database (www.prsgroup.com); World Economic Forum, 2017/2018 Global Competitiveness Index (GCI) database; and the 2017 Heritage Foundation Index of Freedom (www.heritage.org).

Notes: Each measure was standardized to obtain an index ranging between 0 (worst performance) and 100 (best performance) using the following formula: $(var - min)/(max - min)$, where *var* is the individual country measure, and the maximum and minimum are the highest and lowest value in the datasets, respectively. The countries listed in parentheses are the top performers on the respective indices.

¹⁴ See <http://www.heritage.org/index/country/guyana>.

property rights. According to the Heritage Foundation, Guyana is in the category of mostly unfree economies, ranking 106th out of 169 countries assessed. Therefore, given the evidence on the importance of property rights for economic and social development, special attention should be placed on improving such institutional arrangements in Guyana.

Besides property rights, a relevant dimension for social development and cohesion relates to the respect for and protection of fundamental human rights, which is assessed in the next section.

11.2.2. *Protection of Fundamental Human Rights*

Guyana has a long tradition of generally honoring freedom of speech, press, and religion, and the government has generally respected these fundamental rights since independence. However, according to the U.S. State Department's Human Rights Report for 2015, some important human rights issues exist. Problems relate to allegations of mistreatment of suspects and detainees by the police, mistreatment of inmates by prison officials, a high rate of pre-trial detention, discriminatory practices in the application of due process, and incidents of excessive use of force by the police resulting in the death of persons (U.S. State Department 2015). In addition, there are statutes that discriminate against women as well as lesbian, gay, bisexual, and transgender persons.¹⁵

Guyana's constitution makes provision for the establishment of several commissions with goals to strengthen social justice and the rule of law. These include the Human Rights Commission, Women and Gender Equality Commission, Indigenous Peoples' Commission, and Rights of the Child Commission. These commissions function reasonably well, but there is scope for improvement where educational and awareness programs are concerned, since a fair size of the population remains ignorant of their basic rights.

Guyana's constitution in turn provides for an Ethnic Relations Commission with important scope in eliminating all forms of discrimination based on ethnicity, as well as promoting harmony and a sense of security among all ethnic groups. This institution is relevant given the ethnic fragmentation that is embedded in the political system, as described above, hampering overall institutional quality.

According to the 2016 World Justice Project Rule of Law Index, Guyana ranks 70th out of 113 countries in the composite category measuring respect for and enforcement of fundamental rights, with a score of 0.54

¹⁵ Cap. 8:01 *Criminal Law (Offences) Act* Section 354; see also Sections 352, 353 and 355 of that act. See also U.S. State Department (2015).

Table 11.2 Protection of Fundamental Rights in Guyana

Fundamental Rights	Guyana	Latin America	ROSE	OECD
Overall Fundamental Rights	0.54	0.58	0.62	0.76
4.1 Equal treatment and absence of discrimination	0.39	0.51	0.62	0.70
4.2 The right to life and security of the person is effectively guaranteed	0.56	0.61	0.67	0.86
4.3 Due process of law and rights of the accused	0.34	0.46	0.56	0.73
4.4 Freedom of opinion and expression is effectively guaranteed	0.59	0.61	0.59	0.74
4.5 Freedom of belief and religion is effectively guaranteed	0.78	0.75	0.71	0.76
4.6 Freedom from arbitrary interference with privacy is effectively guaranteed	0.46	0.52	0.51	0.77
4.7 Freedom of assembly and association is effectively guaranteed	0.65	0.66	0.71	0.79
4.8 Fundamental labor rights are effectively guaranteed	0.54	0.56	0.60	0.71

Source: World Justice Project (WJP) (<https://worldjusticeproject.org/our-work/wjp-rule-law-index/wjp-rule-law-index-2016/factors-rule-law>).

Note: Scores for the WJP Rule of Law Index, as well as for its component factors and subfactors, range from 0 to 1, where scores closer to 1 indicate better performance.

out of a maximum of 1. As Table 11.2 shows, Guyana is ranked marginally below Latin America (0.58) and significantly below ROSE (0.62) and the OECD (0.76).

Table 11.2 also shows the individual subcomponents of this category, evidencing that Guyana ranks poorly on subcomponent 4.1 (equal treatment and absence of discrimination). This is consistent with a reality of political rivalry along ethnic lines, where the ruling elite has historically been able to discriminate against the opposing ethnic group. For example, the former governments led by the PPP (1992–2015) have been accused of nepotism, favoritism and allocating resources and opportunities indiscriminately to Indo-Guyanese, barring merit, and claiming, for example, that few Afro-Guyanese qualified for ambassadorial postings. Similarly, in the current coalition APNU-AFC government, the number of Afro-Guyanese appointed to high offices and boards of directors of state corporations seems to be proportionally higher than their share in the population. This reinforces the relevance of an institution like the Ethnic Relations Commission and the need to facilitate its appropriate functioning.

Guyana also shows an inferior performance on subcomponent 4.3 (due process of law and rights of the accused). This is consistent with the findings reported in the U.S. State Department Human Rights Report for 2015 in terms of high rates of pre-trial detentions and discriminatory practices in the application of due process. However, as it relates to subcomponent 4.5 (freedom of belief and religion is effectively guaranteed), Guyana exceeds

the averages for all comparators. Persons are generally free to practice their religion without any fear or intimidation.

11.2.3. *Judicial Independence and Effectiveness*

The judiciary branch is formally independent of the political authorities and subject only to the constitution and the law.¹⁶ However, the chancellor of the judiciary, who is the chief representative of judicial authority, is appointed by the President in consultation with the leader of the opposition. Similarly, the chief justice of the High Court is also appointed by the President with consultation. There is no standard tenure for either of these positions and they may serve until retirement (65 years old). The other judges are appointed by the Judicial Service Commission, an independent constitutional agency comprised of five senior jurists appointed by the National Assembly and confirmed by the President. The selection process for judges is meant to be open, transparent, and based on merit.¹⁷

Therefore, although the judiciary is formally independent, the appointments of key judicial authorities are decided by the political authorities. Moreover, Guyana has not had a substantive chancellor of the judiciary or chief justice of the High Court since 2005. The previous holders of these posts retired recently without being confirmed in the positions for more than a decade. Both the government and the opposition—past and current—have been at odds over the substantive appointments of nominees to these two highest judicial posts. This institutional reality harms judicial independence, as shown in Figure 11.4, which indicates that Guyana significantly underperforms in this dimension relative to other countries and groupings of countries.

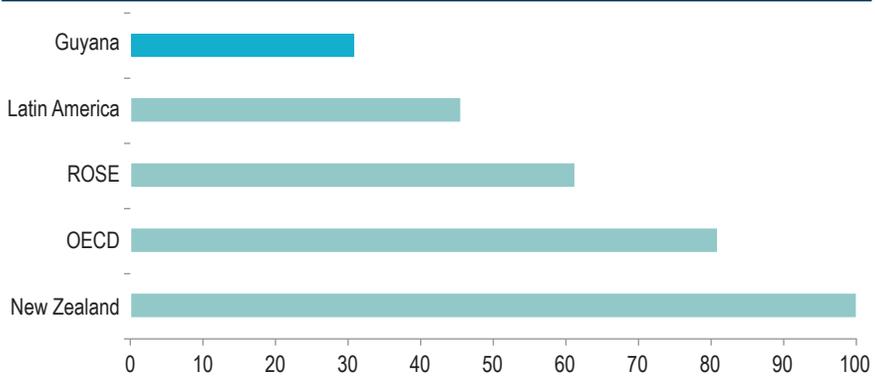
In terms of judicial effectiveness, several indicators are perceived to cause the high overcrowding rate of 118.5 percent in the prison system.¹⁸ These include over-reliance on custodial sentences with little or no use of fines, as well as the overuse of pre-trial detention. Indeed, about 36 percent of the inmates are pre-trial detainees (UNODC 2010, 25). As such, Figure 11.5 shows relatively low levels of judicial effectiveness, with Guyana underperforming ROSE.

Having analyzed the levels of judicial independence and effectiveness in Guyana, the next section turns to assessing the institutional capacity to

¹⁶ Article 122A (1) of Guyana's constitution states "all courts and all persons presiding over the courts shall exercise their functions independently of the control and direction of any other person or authority; and shall be free and independent from political, executive and any other form of direction and control."

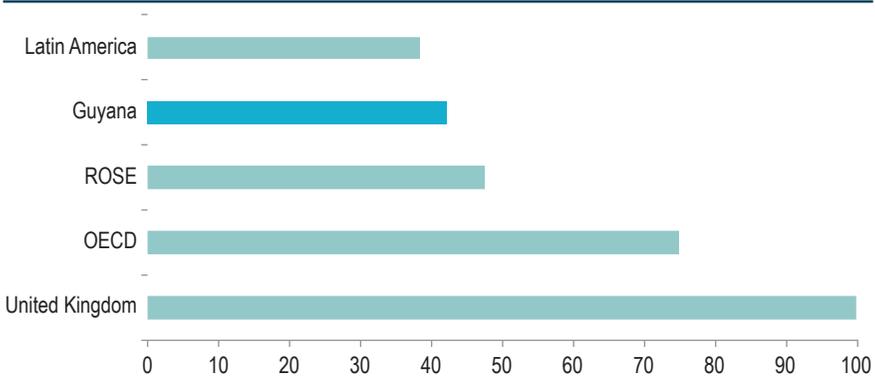
¹⁷ Article 129 (1) of Guyana's Constitution outlines the broad qualifications for judges.

¹⁸ See Institute for Criminal Policy Research, World Prison Brief, at <http://www.prison-studies.org>.

Figure 11.4 Guyana: Judicial Independence Index

Source: Authors' calculations based on the database in Berkman et al. (2008).

Notes: Each measure was standardized to obtain an index ranging between 0 (worst performance) and 100 (best performance) using the formula: $(var - min)/(max - min)$, where *var* is the individual country measure, and the maximum and minimum are the highest and lowest value in the datasets, respectively. New Zealand is the country with the highest Judicial Independence Index ranking worldwide.

Figure 11.5 Guyana: Judicial Effectiveness Index

Source: Authors' calculations based on the 2017 Heritage Foundation Index of Freedom database (www.heritage.org).

Notes: Each measure was standardized to obtain an index ranging between 0 (worst performance) and 100 (best performance) using the following formula: $(var - min)/(max - min)$, where *var* is the individual country measure, and the maximum and minimum are the highest and lowest value in the datasets, respectively. The United Kingdom is the country with the highest Judicial Effectiveness Index ranking worldwide.

enforce the law. As such, it will focus attention on the police as the main institution for law enforcement.

11.2.4. Law Enforcement

The Guyana Police Force is headed by the commissioner of police, who is appointed by the President in consultation with the opposition leader. Persons

are nominated for the office by the Police Service Commission and must meet certain criteria set out by the Guyana Police Force. The process of selection is a combination of merit and politics. All previous commissioners have served in the Police Force prior to promotion. The political filter, however, is that the President must feel comfortable with and hold the confidence of the commissioner. Interesting to note, the Guyana Police Force, along with the Guyana Defence Force, are two institutions where Afro-Guyanese tend to dominate.¹⁹

The standards to become a police officer are generally considered low.²⁰ The emphasis is more on physical fitness and less on academic prowess. The budget for the Police Force is normally developed on a mark-up basis. Therefore, the budget is not performance-driven and is thus an institutional design that does not incentivize high effort.

In terms of coverage, most of the 65 police stations nationwide are in coastal communities where population density is higher, while there are few police stations in the vast hinterland. Estimates of the ratio of police to population vary quite considerably from one source to another. However, the target for the Guyana Police Force is to have 3,570 officers, and it has been short of this target for over a decade (USAID 2016, 23). The Guyana Police Force tends to have a high turnover rate due mainly to more attractive remuneration packages from private security firms and the lure of migration. According to the Ministry of Public Security, the force is short-staffed by 1,070 officers, and loses about 300 to 400 persons each year.

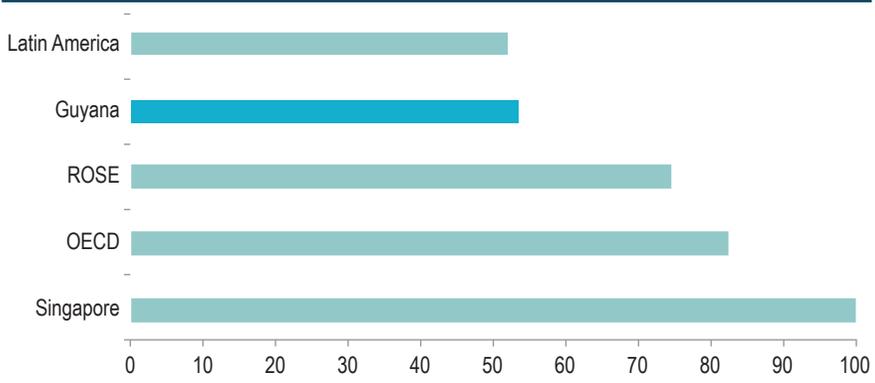
Evidence-driven policing is largely absent. The Guyana Police Force is supposed to collect, store, and analyze crime and victimization data. However, this information is selectively released to the public and few studies of criminality and victimization have been conducted.²¹ Police blotters (reports of crime) are not systematically mined to determine patterns and trends. No structured spatial statistical analysis and geo-referenced mapping of crime and violence exist. Policing tends to be reactive. When a crime spree occurs in an area, increased patrols are assigned, and when crime abates, the patrols diminish.

Accountability of the Guyana Police Force is supposed to be exercised by the Police Complaints Authority (PCA), which undertakes inquiries into complaints of misconduct by members of the force. However, the PCA is neither independent nor effective. The latest data available, from 2012, show that the PCA received 700 complaints, most for neglect and unnecessary

¹⁹ Of the 11 current and former police commissioners, nine have been Afro-Guyanese and two Indo-Guyanese.

²⁰ Source: Guyana Police Force Strategic Plan 2013-2017, Pg., 14-15, Personnel. Available at: http://www.guyanapoliceforce.gy/assets/pdf/strategic_plans/strategic_plans_GPF_2015.pdf.

²¹ For example, the last Drug Traffic and Use Survey was conducted in 2010.

Figure 11.6 Guyana: Order and Security Index

Source: Authors' calculations based on the 2016 World Justice Project database.

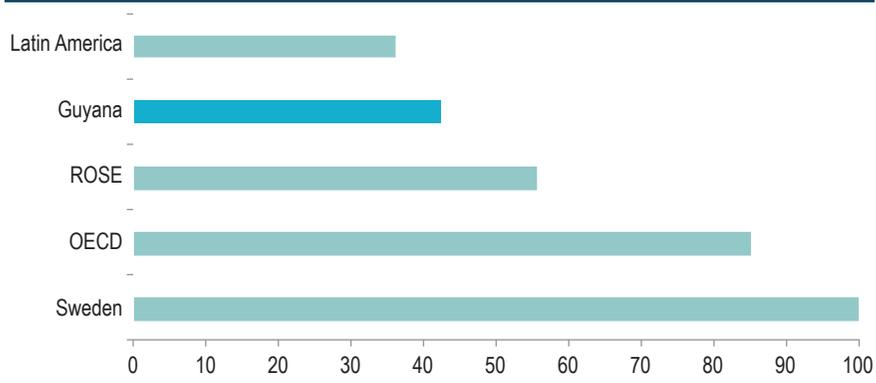
Notes: Each measure was standardized to obtain an index ranging between 0 (worst performance) and 100 (best performance) using the following formula: $(var - min)/(max - min)$, where *var* is the individual country measure, and the maximum and minimum are the highest and lowest value in the datasets, respectively. Singapore is the country with the highest Order and Security Index ranking worldwide.

use of force, and of those, disciplinary action was taken in 70 cases and criminal charges filed only in five cases (U.S. State Department, 2015). Until April 2015, the PCA lacked its own investigative unit and had to rely on the Guyana Police Force to conduct investigations into complaints against its own officers, creating a conflict of interest. Furthermore, while in April 2015 the PCA obtained its own team of investigators, the persons appointed were retired policemen and army members, maintaining a potential conflict of interest, as they would need to investigate former colleagues.

The outlined institutional weaknesses of the Guyana Police Force—low pay, understaffing, inadequate equipment, poor forensic support, high turnover of police officers, lack of capacity to analyze crime data, and poor accountability—have translated into poor outcomes. Indeed, Sutton and Ruprah (2017) report that the Guyana Police Force is the poorest performer in the Caribbean in terms of average response time, public satisfaction, and incidence of bribery. Furthermore, the force remains the least trusted institution in Guyana, according to the 2014 Latin American Public Opinion (LAPOP) Survey.²² Finally, Guyana underperforms on the Order and Security Index (Figure 11.6).

Institutional weaknesses of the police have, therefore, translated into low levels of security in Guyana. Overall, this section has evidenced that institutions related to the rule of law in Guyana suffer from weaknesses. Drawbacks

²² The LAPOP survey showed that 11.6 percent of respondents felt that the police would not come if they called, 22.5 percent said it would take more than three hours, and another 24.1 percent felt it would take from one to three hours.

Figure 11.7 Guyana: Rule of Law

Source: World Bank, 2017 World Governance Indicators database (www.govindicators.org).

Notes: Percentile ranking score ranging from 0 (worst in rule of law) to 100 (best in rule of law). Rule of law captures perceptions of the extent to which agents have confidence in and abide by the rules of society, and in particular the quality of contract enforcement, property rights, the police, and the courts, as well as the likelihood of crime and violence. Sweden is the best country worldwide in terms of the rule of law rankings.

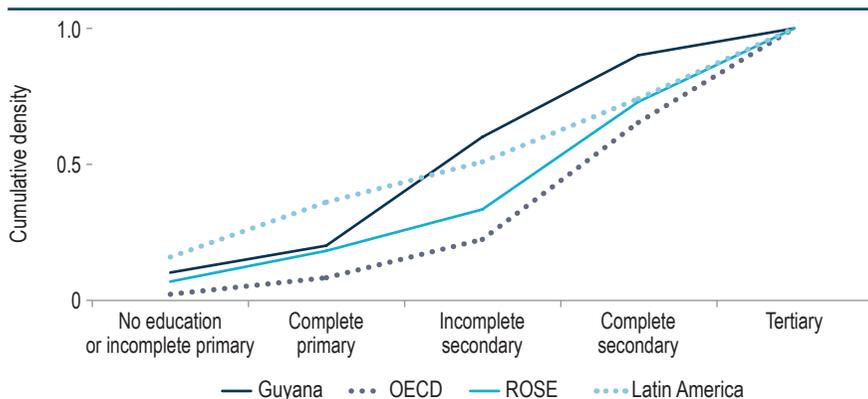
in the protection of property rights, lack of judicial independence, and police ineffectiveness combine to erode the confidence of economic agents in the rules of the society, thereby hindering the ability to spur investment and economic growth. As shown in Figure 11.7, the 2016 Rule of Law dimension from the World Bank's World Governance Indicators evidences the need for Guyana to increase performance vis-à-vis other groupings of countries. Improving this situation should rank high on the policymakers' agenda.

11.3. Institutions for Human Capital Development

As shown in Chapter 4, two main institutions supporting human capital development have been highlighted in the literature: those relating to education and health. Therefore, this section documents the condition of these institutions in Guyana.

11.3.1. Education

The related evidence presented in Chapter 4 suggests that the quality of education matters more than the quantity. Furthermore, the quality of education hinges primarily on the quality of teachers. Therefore, this section will focus not only on the ability of educational institutions to provide educational services in terms of coverage, but also on the state of institutions directed toward ensuring appropriate teacher quality in Guyana.

Figure 11.8 Guyana: Educational Attainment

Source: Authors' calculations based on the 2017 Guyana Labor Force Survey (third quarter) and the World Bank's 2016 World Development Indicators database.

Note: Educational attainment is measured among working-age adults (25–65 years old) who have completed their formal education.

Guyana has universal coverage at the pre-primary, primary, and secondary education levels. Indeed, enrolment rates across these educational levels stand around 90 percent (similar between girls and boys), a level comparable to Latin American and ROSE levels. This is not the case, however, for tertiary education, which is only offered in two of the 10 subnational regions. Tertiary enrolment among females is about 17 percent and among males it drops to 8 percent. These rates are significantly below levels in Latin America (females: 51 percent; males: 40 percent) and ROSE (females: 50 percent; males: 35 percent).²³ Tuition is charged at public universities and colleges (University of Guyana and Cyril Potter College of Education, Critchlow Labour College, and Guyana School of Agriculture), but the amount is heavily subsidized by the government and those institutions attract the largest enrolment.²⁴ In short, educational coverage up to secondary level is within international standards. However, access to tertiary education is low and unequal. Coupled with the high emigration rates of tertiary educated persons, this situation hinders potential labor productivity gains. Indeed, as Figure 11.8 shows, the

²³ See UNESCO (2015); and World Bank, World Development Indicators.

²⁴ There are several private institutions of higher education, including Texilia American University, Lincoln American University, Georgetown American University, Rajiv Gandhi University of Science and Technology, Greenheart Medical University, and others. However, their tuitions and fees are higher than the public institutions and enrolment is much lower than public institutions.

share of working-age adults (25–65 years old) with tertiary education is only 10 percent. This is well below Latin America and ROSE (where 26 percent have tertiary education) and the OECD (where about 35 percent have tertiary education).

In terms of effective institutions directed toward incentivizing better teaching quality, Chapter 4 suggested that the critical institutional components appear to be monitoring teachers' effort and quality, and performance-based hiring and retention decisions. Unfortunately, as shown below, neither of these institutional arrangements appear to be present in Guyana.

The Ministry of Education is responsible for assuring education quality. In terms of teacher monitoring, there is no structured mechanism for identifying and tracking quality teachers. Standardized and independent annual evaluations of students across all grades toward computing teacher value-added measures do not exist. This is highly relevant, as objective evidence provided by Araujo et al. (2016) shows that teacher value-added measures based on student evaluations provide a better measure of teacher effectiveness than traditional teacher assessments based on direct evaluations of teachers. Nonetheless, traditional external evaluations of teachers are also not carried out in Guyana. Furthermore, teacher attendance can be problematic at hinterland sites. In addition, at difficult and underperforming coastal schools, seniority rules are applied that permit an inequitable sorting of teachers. The most experienced teachers tend to transfer out from problematic schools using seniority rules, leaving the newest and most inexperienced teachers in settings that require the most experienced professionals (World Bank 2012).

Recruitment standards are low compared to high-performing school systems.²⁵ Teachers do not use teacher instructor manual/guides, and rote methods are commonly used. Given that teacher performance is not assessed objectively, it does not directly affect compensation. As such, monetary rewards are not tied to objective measures of teaching quality, resulting in low incentives to exert effort. Furthermore, additional pay is awarded to teachers because of additional training/certification and for "hardship school locations," but not for high performance. These policies are prone to reinforce a vicious cycle that ultimately results in suboptimal education levels.

²⁵ Teachers in Guyana must complete a two-year associate degree program at the Cyril Potters College (Technical Teaching School). In addition, they must satisfactorily complete a written test, a practicum, and a practice-based assessment. For those with a bachelor's degree, a teaching certificate program is required.

11.3.2. Health

Guyana has a universal health care system in which medical attention is free of charge for all citizens at public facilities. The public-sector health care infrastructure is multi-tier, with five levels of health facilities. While basic health care provision is widespread across Guyana, it is not the case for higher health care levels.²⁶ The system is structured so that its proper functioning depends on a process of referrals. Except for serious emergencies, patients are to be seen first at the lower levels, and those who cannot be treated at those levels are referred to higher levels in the system. However, in practice, many patients bypass the lower levels. The system is unable to provide certain sophisticated and specialized medical services. For these services, the Ministry of Health provides financial assistance to patients up to US\$5,000 to obtain treatment overseas. Priority is given to children whose condition can be rehabilitated, with a high probability of significant improvements to their quality of life. The ministry also provides financial assistance in the form of a 50 percent subsidy for specialized tests.²⁷

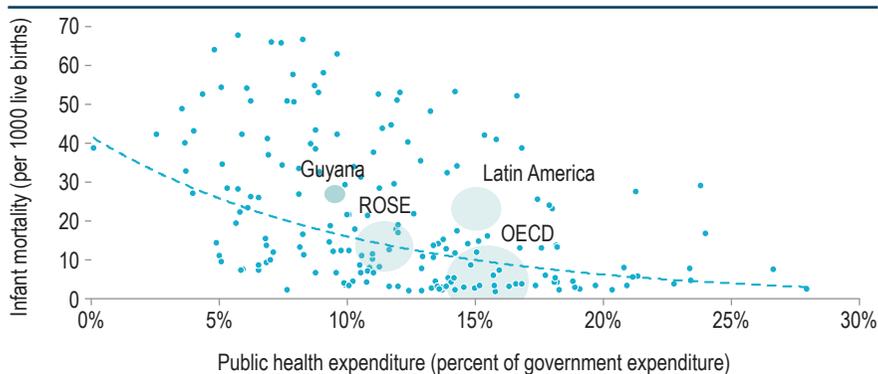
The public health facilities are complemented by nine private centers. Most private facilities are clustered in the capital, with the others in large provincial towns. They are perceived as health care providers of higher quality and, unlike public facilities, they are financed out of pocket or by private health insurance held by patients. In case a public hospital is unequipped to carry out a medical test, patients are referred to a private hospital, and 50 percent cost sharing is provided by the public sector. Physicians work in both the public and private sectors to augment their income, even though they prefer to work at private facilities due to less patient load, better equipment, and higher pay. However, the general availability of physicians is low. There are 0.21 physicians per 1,000 population in Guyana, far below Latin American (1.25), ROSE (1.67), and OECD (3.38) levels.²⁸ As a result, objective health indicators such as the infant mortality rate per 1,000 live births also underperform international standards. Guyana has high infant mortality of 26.9 deaths per 1,000 live births

²⁶ Health posts and centers (level 1 and 2) are located in smaller, rural, and peri-urban villages, whereas district hospitals (level 3) serve geographical areas with 10,000 or more residents. Regional hospitals (level 4) are in Region 2 (Northwest), Region 3, Region 6, and Region 10, four of the most populous administrative regions after Region 4, where the capital is located. Georgetown Public Hospital in the capital is the national referral hospital (level 5). There are also three specialty facilities for behavioral and mental health issues, geriatric care, and juvenile rehabilitation.

²⁷ These include, but are not limited to, CT Scans and MRIs.

²⁸ Source: 2016 World Bank, World Development Indicators database.

Figure 11.9 Guyana: Public Health Expenditures, Physicians per 1,000 Population, and Infant Mortality



Source: Authors' calculations based on the World Bank's 2016 World Development Indicators database.
Note: The size of the bubbles is proportional to the number of physicians per 1,000 population for selected countries or country groups.

compared to significantly lower mortality for ROSE (13.32) and the OECD (4.24). Such underperformance is poorer than countries with similar levels of Guyana's public health expenditures relative to overall government expenditures (Figure 11.9).

The observed weak health performance raises concerns about the institutional setting in place for quality control of health facilities and incentives to health practitioners. The Medical Council of Guyana is the regulatory body that monitors the functioning of all medical practitioners in Guyana. This institution is independent of the health service providers and oversees both public and private health care facilities and practitioners. However, objective periodic performance evaluations of health practitioners are not institutionalized. Therefore, personnel decisions such as promotions, raises, or non-pay benefits are not tied to objective performance shown in the provision of medical services. Introducing incentive schemes based on objective measures of performance might be considered to boost productivity and better results in the health sector.

11.4. Economic Institutions

The Guyanese economy is largely based on agriculture and extractive industries, and thus dependent on the export of commodities. Due to a surge in gold production, Guyana has experienced sustained growth since 2006, while inflation has been low. Moreover, because of relatively recent discoveries of oil reserves, Guyana will become an oil producer by 2020. This section assesses the state of key economic institutions that, as shown

in Chapter 5, have been associated with increased confidence, investment, and growth.

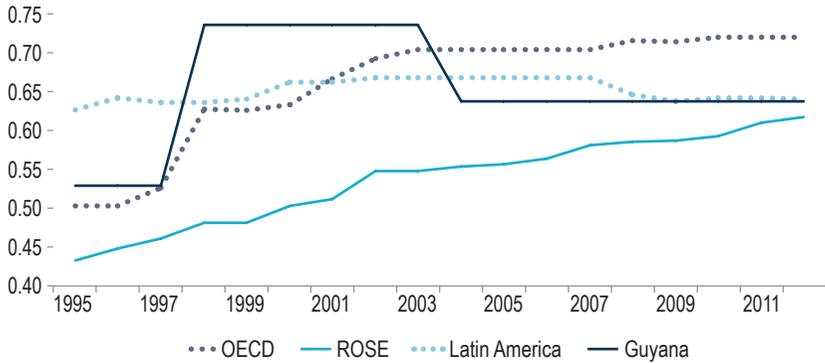
11.4.1. *Central Bank Independence and Transparency*

The Bank of Guyana (BoG), established in 1965, is responsible for setting and implementing monetary policy and maintaining currency convertibility. Its mission is to “maintain domestic price stability, through the prudent formulation and implementation of monetary policy” and to “foster conditions for a sound and efficient financial system.” The BoG supervises commercial banks, non-bank financial institutions, money transfer agencies, currency exchange companies, pension plans, insurance companies, brokers, and agents. To this end, technical and budgetary independence from the political authorities are key elements that positively affect the credibility and reliability of the BoG.

Formally, the BoG enjoys both budgetary and technical independence and, therefore, international rankings of independence provided by Dincer and Eichengreen (2014) rank it relatively well with respect to other Caribbean countries. Indeed, the BoG ranks 42nd out of 89 central banks worldwide in terms of independence, while all other Caribbean countries are ranked below the 73rd spot.²⁹ Similarly, Garriga (2016) in a study covering a wider set of countries ranks it in 51st out of 179 countries worldwide.³⁰ In addition, Garriga (2016) provides historical series of independence for the BoG from 1995 until 2012. Figure 11.10 shows these measures vis-à-vis the ROSE, Latin America and OECD member countries. While Guyana showed formal independence levels above all comparators between 1998 and 2003, then it declined to be at par with Latin America and behind OECD; while maintaining a better position with respect to the ROSE.

²⁹ This ranking is based on the Central Bank Independence Weighted Index (CBIW) for 2010 reported in Dincer and Eichengreen (2014). The CBIW is a weighted average of measures related to the following dimensions: CEO appointment (weight = 0.1), policy formulation (0.15), objectives (0.15), limitations on lending to the government (0.50), and appointment of board members (0.1). For details on the specific components of these measures, see Table 18 in Dincer and Eichengreen (2014).

³⁰ This ranking is for year 2012. Garriga (2016) identified four dimensions concerning the independence of central banks from political influence: who appoints the governor (weight = 0.2); whether there is direct government involvement in policy decisions (weight = 0.15); whether there are limits on the ability of the government to borrow from the central bank (weight = 0.50); and whether price stability is a core objective of monetary policy (weight = 0.15). The weighted average of these dimensions results in a central bank independence index ranging from 0 (lowest independence) to 1 (highest independence).

Figure 11.10 Guyana: Central Bank Independence Index

Source: Garriga (2016).

Note: The Central Bank Independence Index ranges from 0 (lowest independence) to 1 (highest independence).

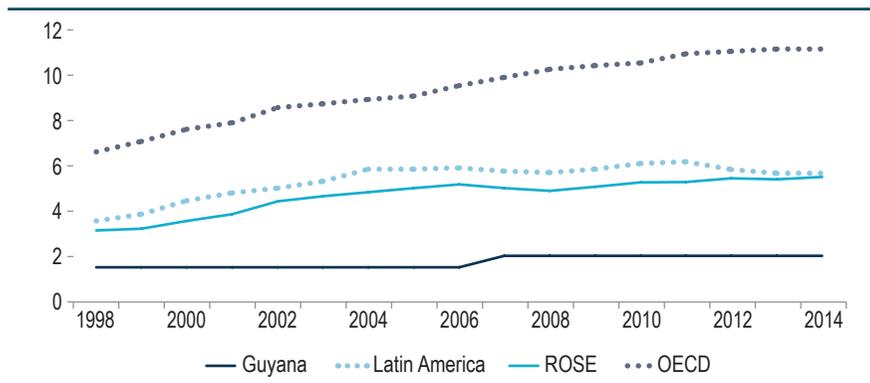
However, while budgetary independence is exercised, the BoG has limited technical independence in practice. The governor of the BoG is appointed by the President with renewable five-year terms. Therefore, even though the BoG should have nominal independence, the monetary and fiscal authorities tend, in practice, to act in unison.³¹ Loose fiscal policy exercised by the executive has been consistently supported by accommodative monetary policy of the BoG, thereby creating a procyclical policy stance. Oftentimes, statistics released by the BoG lack credibility and revisions to official statistics tend to be made only after International Monetary Fund missions.

The BoG also lacks transparency in several dimensions. In general, it does not have an active communications strategy, and does not produce any analytical work to support or validate the positions taken or to evaluate likely impacts of external developments. The main reasons for this lack of transparency are little statistical data gathering and analytical capacity, human resource constraints, and a political system that limits checks and balances. Indeed, as Figure 11.11 shows, transparency of the BoG has lagged significantly behind comparators during the entire period assessed by Dincer and Eichengreen (2014).³²

Independence and transparency of central banks influence their credibility and effectiveness in controlling inflation, thereby providing a proper

³¹ One recent example relates to currency shortages in late 2016 and early 2017. Within that episode, the governor of the BoG and the minister of finance coordinated and agreed to introduce capital controls.

³² The Central Bank Transparency Index measures compliance with 15 best practices distributed across the following areas: political transparency (practices), economic transparency (three practices), procedural transparency (three practices), policy

Figure 11.11 Guyana: Central Bank Transparency Index

Source: Dincer and Eichengreen (2014) updated database for Central Bank Transparency 1998–2014 (https://eml.berkeley.edu/~eichengr/Dincer-Eichengreen_figures&tables_2014_9-4-15.pdf).

Note: The Central Bank Transparency Index ranges between 0 (lowest transparency) and 15 (highest transparency).

environment for economic growth and prosperity. Therefore, it is highly relevant to ensure technical and political independence as well as transparent mechanisms in BoG operations.

11.4.2. Fiscal Institutions

The Ministry of Finance is the key institution responsible for the formulation and implementation of fiscal policy and public debt management.³³ The ministry's general fiscal policy objectives are the maintenance of output stability and debt sustainability. Although the stock of public debt has been reduced from about 130 percent of gross domestic product in the early 2000s to less than 50 percent, this has been mainly the result of Guyana's participation in a program of debt forgiveness.³⁴ Since debt

transparency (three practices), and operational transparency (three practices). The index ranges from 0 (no compliance at all) to 15 (full compliance with the 15 best practices). For details on the specific practices and index construction, see Appendix 1 in Dincer and Eichengreen (2014).

³³ To a lesser extent, the General Revenue Authority (GRA), a semi-autonomous entity established in 2000, is closely related to the Ministry of Finance because it is responsible for implementation and enforcement of Guyana's tax and custom laws. The GRA plays a pivotal role in the budget process in that it supplies revenue forecasts that are integral in the development of the annual budget.

³⁴ In March 2007, the Inter-American Development Bank, Guyana's principal creditor, canceled nearly US\$470 million of the country's debt, equivalent to 21 percent of gross domestic product, in the context of the Heavily Indebted Poor Countries (HIPC) initiative.

forgiveness, the government has run continued fiscal deficits over the last 12 years. As such, a continuation of current fiscal policies would trigger further debt accumulation, thereby reducing prospects for prosperity.³⁵ It is relevant, therefore, to consider the establishment of mechanisms that could help change this situation. As shown in Chapter 5, fiscal performance worldwide has improved with the existence of institutions that aim to correct incentives and contain overspending. If properly established, objective fiscal rules, independent fiscal councils that monitor compliance with fiscal rules, and sovereign wealth funds provide a medium-term anchor that enhances the credibility of policies and supports inter-generational equity. By contrast, the lack of such institutions makes fiscal mismanagement more likely.

Guyana, however, as most of the Caribbean countries, does not subscribe to fiscal rules and has no fiscal council in place. Moreover, fiscal planning and analytical capacity are limited due to poor financial and economic data production and dissemination. In addition, the analyses here show that the country would greatly benefit from greater openness, comprehensiveness, and transparency in the budget formulation process. Specifically, while budget allocations and transfers from central to subnational governments follow a set of criteria and rules, consolidation of fiscal accounts by sector is absent. Furthermore, Guyana would benefit from enhanced transparency in public procurement processes. This could be accomplished by increasing the utilization of competitive tenders, recruiting highly qualified procurement staff, and publicizing information on procurement processes and awarded contracts. The country would also benefit from a more detailed fiscal medium-term framework that allows for planning and budget execution. Effective internal controls are limited, and external scrutiny and audit could be further improved. At this time, a draft legislation is being considered to create a sovereign wealth fund. Such an institution is of the utmost importance given Guyana's prospects to benefit from oil proceeds in the future.

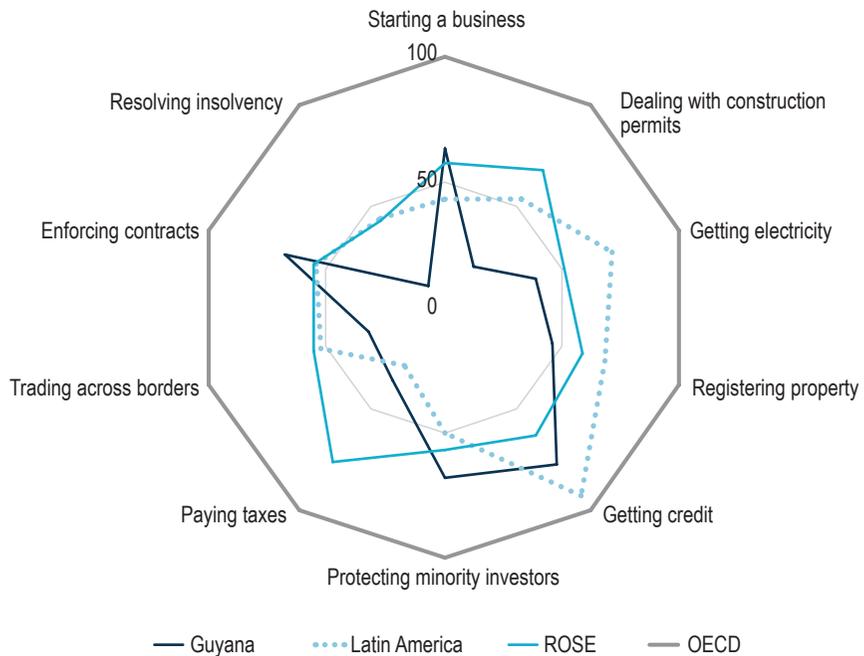
The establishment of these institutions will likely help raise transparency and credibility, as well as increase the awareness of the political and social costs of unsound fiscal policies in the country. The imminent development of the oil and gas sector make the establishment of adequate fiscal institutions, improved fiscal management, and enhanced public financial management a top priority.

³⁵ The one year (2015) when fiscal balances improved was due to one-off factors, namely a suspension of Parliament and a protracted electoral cycle that prevented a budget from being presented and authorized, which reduced government spending.

11.4.3. Ease of Doing Business

As shown in Ruprah and Sierra (2016), private entrepreneurship and innovation are key drivers to boost investment, growth, and development. Therefore, institutions and regulations that permit and promote private sector development are extremely relevant. As such, this section assesses the state of these issues in Guyana. According to the World Bank's 2016 Doing Business Indicators, Guyana has an unfavorable business environment compared to other country groups along several dimensions. As can be seen in Figure 11.12, Guyana underperforms all country groups in terms of getting construction permits, obtaining electricity, registering property, and resolving insolvency. However, in other dimensions such as starting businesses, enforcing contracts, protecting minority investors, and getting credit, Guyana slightly outperforms ROSE. Guyana improved its position in the dimension of credit access with passage in 2015 of a law that allows the nascent credit bureau to collect information from utilities and other

Figure 11.12 Guyana: Ease of Doing Business



Source: World Bank, 2016 Doing Business database.

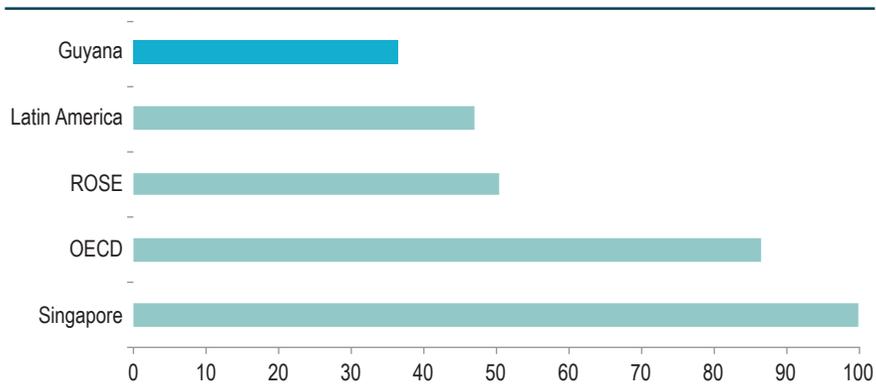
Notes: Each measure was standardized to obtain an index ranging between 0 (worst performance) and 100 (best performance) using the following formula: $(var - min)/(max - min)$, where *var* is the individual country ranking, and the maximum and minimum are the highest and lowest value in the datasets, respectively. The OECD was taken as the best practice benchmark with a value of 100 in each one of the dimensions measured.

companies beyond financial institutions. This type of institution could be highly beneficial in reducing information asymmetries between financial institutions and potential borrowers, and thereby increasing economic efficiency. However, the institution is not yet in full and effective operation.

Overall, Guyana is in a disadvantaged position regarding its overall ranking on the World Bank's 2016 Ease of Doing Business Index, lagging behind Latin America and ROSE. This low performance coincides with findings from the 2014 IDB Enterprise Surveys. Entrepreneurs report the excessive cost of electricity, perceptions of persistent corruption in the awarding of public contracts, and cumbersome tax payment processes as the top three issues limiting private sector development. Indeed, Guyana has some of the highest commercial and residential electric tariffs in the Caribbean region (US\$28-US\$31 per kwh). In addition, Transparency International's 2016 Corruption Perception Index suggests that Guyana significantly underperforms all Caribbean countries, Latin America, and ROSE. Lastly, current tax administration rules and procedures are cumbersome, as the average firm spends 256 hours in executing 35 annual tax payments compared to 195 hours and 25 annual payments by firms in ROSE.

Not surprisingly, as shown in Figure 11.13, Guyana lags significantly behind in terms of the quality of policies and regulations aimed at permitting and promoting private sector development. Indeed, Guyana lacks a comprehensive and consistent policy framework to promote economic diversification. For example, the horticultural sector has high growth

Figure 11.13 Guyana: Regulatory Quality



Source: World Bank, 2017 World Governance Indicators database (www.govindicators.org).

Notes: Percentile ranking score ranging from 0 (worst in regulatory quality) to 100 (best in regulatory quality). Regulatory quality captures perceptions of the ability of the government to formulate and implement sound policies and regulations that permit and promote private sector development. Singapore is the best country worldwide in terms of regulatory quality.

potential and the government has in fact expressed an interest in increasing exports of fruits and vegetables. However, there have been no investments in key institutions to develop these sectors, such as in developing quality assurance laboratories with the approval to certify products for export to North American and European markets.

11.5. Conclusions and Policy Recommendations

The Guyanese political scenario has been characterized by ethnic fragmentation and a relatively high concentration of economic power. The Guyana Electoral Commission that was established in 2000 has succeeded in building more transparency and trust in the electoral process and is thus central for political stability. But many challenges remain. The high concentration of power in the office of the presidency, continued ethnic polarization, and highly centralized political parties wherein political elites experience little turnover harm prospects for open and pluralistic political competition. The economic structure based on the production of unsophisticated export content has favored the emergence of an economic elite that hold de facto political power. This diminishes incentives to implement more inclusive and productivity-enhancing economic reforms.

Institutional capacity needs to be further strengthened in terms of checks and balances on state powers. The development of institutionalized mechanisms for oversight by civil society would be highly relevant. This should be complemented by increasing transparency and accountability of the legislature and the executive, and by improving openness about bills and approved laws, budget execution, policies and programs, and politicians' performance, among other matters.

On a different front, social cohesion and protection against any type of discrimination must be effectively guaranteed. Whereas freedom of belief and religion is in good standing in Guyana, significant improvements are still needed to eradicate discriminatory practices in other areas. Key features related to the administration of justice and law enforcement add to this scenario, thus placing Guyana's rule of law below other country groupings. Fragile rule of law institutions in Guyana undermine social cohesion and feed polarization, which spills into the political sphere, making governance and the forging of bipartisan collaboration difficult to achieve.

Deficiencies in the justice system are associated with high rates of defendants not being represented duly in their court cases, meaning that while due process is occurring de jure, in a material sense the de facto rights of defendants are diminished. Having more and better trained prosecutors would contribute to improving due process rights and reducing the

worrisome inefficiencies and backlogs of cases. The sizable percentage of pre-trial detainees results in overcrowded prisons and high rates of recidivism. The correctional system needs to play a role in the rehabilitation of inmates. Likewise, the legitimacy of the police should be strengthened with performance-based salary structures, adequate training, and the establishment of an independent investigative unit that can effectively hold the police accountable. This should have positive effects on trust in the police and crime reporting.

Rule of law institutions that guarantee equality before the law are best followed by human capital institutions that establish an even playing field for the population. Human capital institutions in Guyana need to generate conditions for economic growth. While access indicators are in general good (despite low tertiary education enrolment and attainment), quality indicators are poor compared to other countries. Increasing the quality of both the health and education sectors should be a central goal. The design and institutionalization of mechanisms to attract and retain trained staff, monitor objective performance, and tie incentives to quality in service delivery are highly relevant.

Institutions regulating and fostering economic activity are another main engine in the country's institutional framework. Macroeconomic stability needs to be pursued by ensuring technical independence of the Central Bank of Guyana and transparency in its operations. This should be a priority on the policymakers' agenda. On the fiscal front, the adoption of fiscal rules with the support of an independent fiscal council are key elements that are missing for proper fiscal policy design and execution. Being highly dependent on commodity exports, Guyana needs to delink the budget and the economy from the volatility of commodity revenue, stabilizing the overall fiscal balance throughout the commodity price cycle. Therefore, the country would significantly benefit from an independent advisory council that professionally estimates the long-term price of commodity exports, and from a sovereign wealth fund that smooths revenues and expenditures throughout the cycle.

While the establishment of these institutions would likely help improve transparency and credibility, credibility would need to be further enhanced by adoption of several aspects of public financial management, including enhancing the medium- and long-term national planning capacity; consolidating the fiscal accounts by sector; strengthening the transparency of public procurement processes by increasing the utilization of competitive tenders, recruiting highly qualified procurement staff, and making information public; and enhancing effective internal controls as well as external scrutiny and audit.

Finally, a comprehensive and consistent policy framework to promote private sector development and economic diversification is needed. Key ingredients should include the full and effective implementation of a broad-based credit bureau that could be extended to a mandatory credit registry in which all financial institutions, utilities, and service providers report the credit applications and debt status of individual and corporate clients. Simplification of tax payment procedures exploiting information and communications technologies, as well as the establishment of export quality certification laboratories for promising non-traditional industries, are policies that could be considered.

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Jamaica

Camila Mejia, Henry Mooney, and Juan Pedro Schmid

12.1. Political Institutions

The 1962 Jamaican constitution, which is comprised of 10 chapters that govern the rights and obligations of citizens, the government, the central bank, and the public service, came into force with the *Jamaica Independence Act* passed that same year by the Parliament of the United Kingdom.¹ The constitution established a parliamentary democracy based on the UK model, as well as a British-style civil service. As such, political and public institutions in Jamaica are similar to those found in many other Commonwealth and Caribbean countries.²

The British Monarch is the head of state but appoints on the advice of the prime minister a governor-general, who serves as the representative in Jamaica. The constitution gives the governor-general authority to name the date of a general election, to appoint ministers and assign them responsibilities, and to appoint parliamentary secretaries, the attorney general, senators, privy councilors, the chief justice, the president of the Court of Appeal, the director of Public Prosecutions, and members of the Services Commissions. In addition, the governor-general wields the prerogatives of judicial pardon, performs the ceremonial duties of head of state, and formally assents to bills before they can become law. In most cases the governor-general acts in accordance with the advice of the prime minister, in some cases after consultation with the leader of the opposition, and

¹ Constitution of Jamaica, 6 August 1962, available at: <http://www.refworld.org/docid/3ae6b4ed28.html>. The constitution may be amended by majorities of two-thirds in both houses of Parliament or, if the Senate does not concur, with the approval of a special majority of the electorate voting in a referendum. A summary of the constitution is available at <http://nlj.gov.jm/jamaica-constitution-brief/>.

² Countries in the Commonwealth Caribbean other than Guyana and Grenada have kept the main aspects of the Westminster model of government.

in other cases on the recommendation of such authorities as the Services Commissions and the Privy Council.³ In only a few minor matters does the governor-general act at his or her own discretion.

Even though executive power is vested in the Crown, it is in practice exercised by the Cabinet, which is led by the prime minister. The bicameral legislature consists of the 63-person elected House of Representatives and 21-person appointed Senate (13 members are appointed by the prime minister and eight by the leader of the opposition). The executive branch consists of the prime minister, Cabinet, and government ministries.

Elections in Jamaica are called by the governor-general on the advice of the prime minister. While elections can be called any time, Parliament dissolves five years after the first sitting of the new Parliament. Elections are then constitutionally due before the end of three months. Candidates are elected from 63 determined geographical areas, called constituencies, the delimitations of which are continuously reviewed by a Standing Committee. Each constituency elects one candidate by simple majority. As is the case in first-past-the-post electoral systems, the number of seats won by a party may not accurately reflect the total number of votes cast for it, and the disparity in seats won by the two parties is usually higher than the variance between the total votes.⁴ Each party presents one candidate, who is elected by internal competition. Jamaica has neither gender nor minority quotas.

Like most independent Caribbean states (former British colonies), Jamaica has a classic Westminster parliamentary system, in contrast to other Latin American states that have presidential systems. In the Westminster model, unlike presidential systems, the prime minister is not elected by popular vote but by the House of Representatives. Therefore, the prime minister would typically belong to the party that won the majority of seats in the House of Representatives. This, coupled with the fact that the prime minister also nominates 13 of the 21 members of the Senate, guarantees a parliamentary majority to the executive. As a result, the prime minister is subject to fewer checks and balances than would normally be found in a

³ When the constitution mandates that the governor-general is directed to exercise any function on the recommendation of any person or authority, that person shall exercise that function in accordance with the recommendation. While the governor-general can refer that recommendation back for reconsideration, he or she ultimately must follow the final recommendation. Similarly, even if the leader of the opposition has to be consulted, the prime minister's final advice is binding.

⁴ For instance, in 1949 the PNP only won 13 seats as opposed to the JLP's 17, even though the PNP won the majority of votes.

typical presidential system, where the president is not guaranteed to have the majority in the legislative.

The prime minister forms and presides over the Cabinet and advises the queen on the appointment of the governor-general. Furthermore, the prime minister advises the governor-general on the appointment of the six members of the Privy Council, on the dissolution of Parliament, and on appointments of the chief justice, the president of the Court of Appeals, and the three service commissions enshrined in the constitution. In the case of appointments of senior members of the judiciary and the service commissions, however, the prime minister's advice is given after consultation with the leader of the opposition.⁵

12.1.1. *Political Parties and Background*

The political landscape in Jamaica has been dominated by two political parties, the People's National Party (PNP) and the Jamaica Labour Party (JLP).⁶ The PNP was founded in 1938 and is the oldest political party in the Anglophone Caribbean. The JLP was founded in 1943 as the political wing of the Bustamante Industrial Trade Union. The PNP was traditionally more to the left of the ideological range than the JLP. As such, traditionally the PNP had strong worker/union representation while the JLP leaned more toward the business class. Political polarization increased in the 1970s when the PNP adapted "Democratic Socialism" as the new political philosophy for the country. As a reaction, the JLP declared itself a "Social Democratic Party." The period also coincided with a spike in violence in the run-up to the 1980 election. None of the major political parties in Jamaica represents specific ethnic or religious groups.

Since parliamentary elections were introduced in 1944, the two parties have alternated dominance of government. The exception was the period from 1989 to 2007, when the PNP was in power for 18 years, winning four consecutive elections in 1989, 1993, 1997, and 2002.⁷ In addition, the loss of the JLP in 2011 was the first time in Jamaica's history that an incumbent government was voted out after only one term. However, government changed again in 2016. Electoral violence became a central issue

⁵ While the leader of the opposition has to be consulted, the prime minister's advice is binding. See the Jamaica Constitution, Section 32, Subsection 4.

⁶ The only time independents won seats in a general election was in 1944.

⁷ For short summaries of all elections, see *The Gleaner's* diGJamaica.com blog at <http://digjamaica.com/blog/2016/02/05/the-history-of-general-elections-in-jamaica-part-1/>.

Table 12.1 Profiles of the Main Political Parties in Jamaica

Name of Party	Initials	Periods in Executive Power Before and Since Independence	Ideology	Ethnic Voter Base	Prevailing Religion of Voter Base
People's National Party	PNP	Before independence: 1955–1962. Following independence: 1972–1980, 1989–2007, 2011–2016.	Social democracy, democratic socialism, third way republicanism, center-left	None	Christian
Jamaica Labour Party	JLP	Before independence: 1944–1955. Following independence: 1962–1972, 1980–1989, 2007–2011, 2016–to date	Conservatism, center-right	None	Christian

Source: Authors' elaboration based on www.caribbeanelections.com.

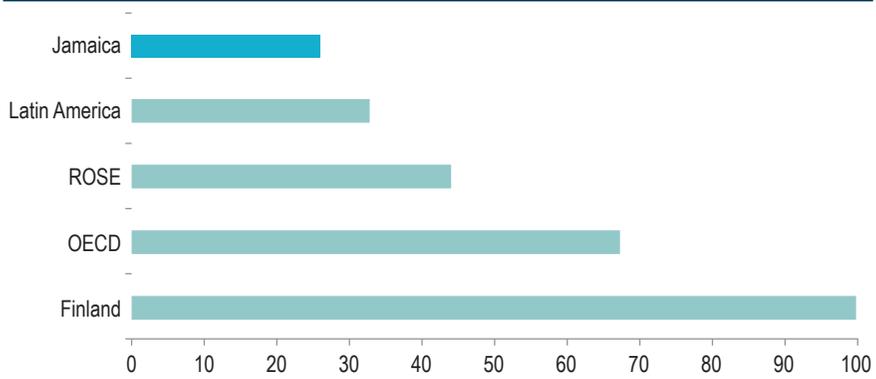
in the 1960s and, especially, 1970s, as involvement of organized gangs in the political process intensified (Clarke 2006).⁸ Table 12.1 summarizes the profiles of the political parties in Jamaica.

In summary, Jamaica has a political model that concentrates considerable power in the chief executive, and politics is dominated by two political parties that have alternated political power. Figure 12.1 shows the Public-Regardedness Index for Jamaica, which measures the extent to which policies pursued are perceived as being in the public interest or whether they tend to be directed toward special interest groups.⁹ The index illustrates that Jamaica has still ample room for improvement.

The next section turns to analyzing the extent to which relevant rules and institutions in place have guaranteed democratic participation and transparency in electoral processes.

⁸ Supporters of the of the two dominant parties began using extreme violence as a means of exerting influence and/or control over parts of the country. This and political polarization led to the creation of “garrison communities” or neighbourhoods controlled by supporters of one of the two main parties. While strong influence of political parties persists today, violence and crime have abated considerably, though localized outbreaks of violence still take place around elections. See also Clarke (2006) for a detailed recount of the nexus between crime, patronage, and elections in Jamaica.

⁹ As explained in Chapter 6 of this volume, the Public-Regardedness Index was proposed in Berkman et al. (2008). The authors computed this index using expert evaluations and perceptions on issues related to (1) corruption, (2) public spending on social transfers, and (3) whether government contracts are awarded fairly or generally favor well-connected firms and individuals. The index is the combination of these three measures. The first component was taken from Transparency International Corruption's Perceptions Index, and the last two components from the Global Competitiveness Report.

Figure 12.1 Jamaica: Public-Regardedness Index

Source: Authors' calculations based on the database in Berkman et al. (2008).

Notes: Each measure was standardized to obtain an index ranging between 0 (worst performance) and 100 (best performance) using the following formula: $(var - min)/(max - min)$, where *var* is the individual country measure, and the maximum and minimum are the highest and lowest value in the datasets, respectively. Finland is the country with the highest Public-Regardedness Index score worldwide. OECD: Organisation for Economic Co-operation and Development; ROSE: rest of the small economies of the world.

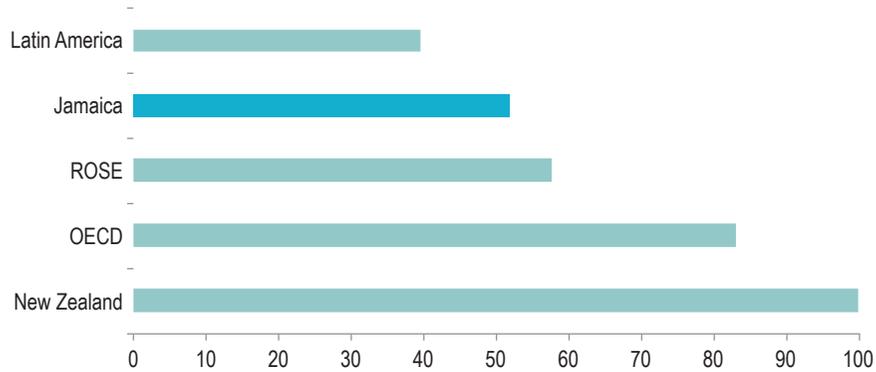
12.1.2. *Political Representation, Competition, and Transparency in the Political System*

Countries are more likely to establish appropriate economic institutions that in turn spur development when they have an open, pluralistic political system with competition for political office, a widespread electorate, and openness to new political leaders (Acemoglu and Robinson 2012).

Both parties in Jamaica have internal mechanisms to nominate their candidates. These nominations are overseen by the Central Executive for the JLP and the National Executive Council for the PNP.¹⁰ While these decision-making bodies concentrate substantial political power, the main decisions, including election of the party leaders and the president, are taken at the annual party conferences.

Candidates for the central government elections are nominated by the Constituency Conference for the PNP and the Constituency Committee for the JLP, but candidates can be vetoed and must be approved by party leadership. Neither appointed senators nor elected members of Parliament can be removed or replaced by the party leader or other members of Parliament except in specific circumstances such as ceasing to be a

¹⁰ Both parties have constitutions that govern them. See <https://issuu.com/milton-miles/docs/constitution> for the PNP and <http://www.jamaicalabourparty.com/content/constitution-jamaica-labour-party> for the JLP.

Figure 12.2 Jamaica: Control of Corruption

Source: World Bank, 2017 World Governance Indicators database (www.govindicators.org).

Notes: Percentile ranking ranging from 0 (worst in controlling corruption) to 100 (best in controlling corruption). New Zealand is the best country worldwide in terms of controlling corruption. The control of corruption dimension captures perceptions of the extent to which public power is exercised for private gain, including both petty and grand forms of corruption, as well as “capture” of the state by elites and private interests.

Commonwealth citizen, criminal behavior, or situations where they would have been ineligible to have been elected.¹¹ Thus, while party leadership plays an important and defining role in the selection of candidates, nominations are originated from a broader and participative platform.

The control of corruption dimension from the World Bank’s World Governance Indicators, which measures the extent to which the state is captured by elites and private interests, shows that Jamaica scores better than Latin America but below other country groups such as the rest of the small economies of the world (ROSE) and the OECD (Figure 12.2).

Public participation in and transparency of electoral processes are central aspects for any democracy. The Electoral Commission of Jamaica (ECJ) is responsible for conducting transparent elections.¹² The functions of the ECJ include the compilation and maintenance of the register of eligible electors, the production of the voter lists for elections, and the conduct of parliamentary and local government elections, by-elections, and referenda.

The ECJ was established in 2006 by way of the *Electoral Commission (Interim) Act*.¹³ It is comprised of nine members (four selected members, four nominated members, and the director of elections). The

¹¹ See the Jamaica Constitution, Section 40.

¹² This section draws on the ECJ website, available at <http://ecj.com.jm/about-the-ecj/about/>.

¹³ Available at <http://moj.gov.jm/laws/electoral-commission-interim-act>.

nominated members include two persons nominated by the prime minister and two nominated by the leader of the opposition, while the selected members are appointed by the governor-general after consultation with the prime minister and the leader of the opposition.¹⁴ The director of elections is elected on the recommendation of the eight members of the commission.¹⁵ One of the selected members is appointed chairman of the ECJ. The ECJ is a permanent, independent, and autonomous authority that reports directly to Parliament. Its day-to-day operations are carried out through the Electoral Office of Jamaica (EOJ), which is a public government agency established in 1943 to administer the holding of parliamentary and local government elections. The director of elections (who is also a member of the ECJ) manages the operations of the EOJ and reports to the ECJ. Voter registration is available on a continuous basis and must be done in person. In that process, personal data are collected, and residency verified. Afterwards, a voter ID is issued. All the information is available online and the main newspapers usually run stories with instructions around the time of potential elections. Voter registries are updated twice yearly (May and November) and only persons appearing on the voter lists may vote.¹⁶

The first international organization to observe parliamentary elections in Jamaica was the Carter Center in 1997.¹⁷ The Carter Center was also an observer in 2002. Caribbean Community (CARICOM) electoral observers were present in 2007 and 2016, and observers from the Organization of American States were present in 2007 and 2011 and 2016.¹⁸ Only rare incidences of politically motivated violence were reported in the 2016 election, confirming a trend that political violence, which had impaired elections since the 1960s, has been disappearing from Jamaica.

Voter turnout has been declining since the 1980s. The national voter participation rate in the 2016 election was 47.7 percent, the lowest turnout

¹⁴ The prime minister and the leader of the opposition can change their nominated members at any point, but selected members can only be revoked “by a resolution passed by the majority of all the members of the Commission having a right to vote or a resolution of each House of Parliament approved by not less than two-thirds of all the members of that House” (Paragraph 4 (5a) of the *First Schedule Electoral Commission (Interim) Act*).

¹⁵ See the *First Schedule Electoral Commission (Interim) Act* for details on the appointment of ECJ members.

¹⁶ See the ECJ website at <http://www.eoj.com.jm> or *The Gleaner's* diGJamaica.com blog at <http://digjamaica.com/electionja>.

¹⁷ A report by the Carter Center on the 1997 elections is available at <https://www.cartercenter.org/documents/electionreports/democracy/finalreportjamaica1997.pdf>.

¹⁸ Observer reports can be found on the Election Portal: www.caribbeanelections.com.

other than the 1983 election, which had been boycotted by the PNP.¹⁹ The turnout is also the lowest of all recent elections among the English-speaking Caribbean countries (average 70 percent). In summary, while transparency of elections in Jamaica stands within appropriate standards, voter turnout has been declining, indicating voter apathy.

Considering the relatively high concentration of power that the executive branch possesses, it is relevant to assess (1) the mechanisms under which Parliament can exert constraints and accountability over the executive or *de jure* institutions; and (2) the extent to which such *de jure* mechanisms are practically exercised or translated into *de facto* institutions.

12.1.3. *Constraints on the Executive and Accountability*

The prime minister is the most important member of the cabinet. The governor-general selects from the House of Representatives as prime minister the party leader who “is best able to command the confidence of a majority of the members.”²⁰ In addition, the governor-general appoints, in accordance with the advice of the prime minister, at least 11 other cabinet members from the two houses (two to four members from the Senate). The prime minister also directs cabinet business, and acts as the government’s chief spokesperson at home and abroad, usually also keeping control over foreign policy. In terms of political control, the prime minister may be removed by resigning, by otherwise ceasing to be a member of the House of Representatives, or by being given a vote of no confidence by a majority of house members.²¹ However, in this latter case, the governor-general gives the prime minister the option to dissolve Parliament.²² Similarly, other members of both houses can be removed if they resign, cease to be Commonwealth citizens, are absent from too many sittings, take obedience to foreign power, do business with the government of Jamaica, or circumstances arise that, if they were not a member of the House, would cause them to be disqualified for appointment or election.²³

¹⁹ For a short history of the 1983 election, see *The Gleaner’s* diGJamaica.com blog at <http://digjamaica.com/blog/2016/02/12/the-history-of-general-elections-in-jamaica-part-3/>.

²⁰ See the Jamaica Constitution, Section 70 Subsection 1.

²¹ See the Jamaica Constitution, Section 71 Subsection 1 and Section 71 Subsection 2.

²² See the Jamaica Constitution, Section 71 Subsection 3.

²³ For a full list, see the Jamaica Constitution, Section 41 Subsection 1.

In line with the Westminster system of government, the constitution secures the office of leader of the opposition, who is appointed by the governor-general as the member of the House of Representatives who “is best able to command the support of a majority of those members who do not support the government.”²⁴ As an institutionalized role, the leader of the opposition exercises consultative functions, especially on appointments to public offices, including that of the chief justice, the president of the Court of Appeal, and members of the Services Commission. The opposition leader nominates eight of the 21 senators.

The leader of the opposition heads the shadow cabinet and is expected to challenge the government and provide alternative policy choices for the public. The institutionalized role of the opposition leader and Jamaica’s democratic tradition give the opposition considerable freedom to criticize the government.

As in many other Commonwealth countries with a bicameral Parliament, the approval of both chambers is necessary for ordinary legislation to become law. In the Jamaican case, the Senate has only a veto to suspend and cannot prevent decisions made by the House of Representatives from going to the governor-general for assent.²⁵ In addition, the Senate can introduce legislative bills and review legislation submitted by the House. Concurrence of the Senate is needed for constitutional changes. Finally, the Cabinet must include two to four senators, while others may be appointed as parliamentary secretaries to assist Cabinet members. The existence of a Senate permits participation in public affairs by those who might not wish to run for election, but also encourages the patronage offerings of the major political parties.

Except for financial bills, any member of both houses may introduce new bills, even though bills aimed at implementing government policy are usually introduced by Cabinet members. While both chambers have several standing committees, these have relatively little investigative power and have not provided an avenue for containing the executive, which has fallen to the parliamentary opposition (Meditz and Hanratty 1987).

In summary, while *de jure* political constraints on the executive and accountability mechanisms exist, the *de facto* exercise of such attributions is limited because the system ensures that the executive will hold a majority in both chambers of the legislature.

²⁴ See the Jamaica constitution, Section 80 Subsection 2.

²⁵ The constitution allows the Senate to delay legislative bills for seven months and money bills for one month. Even in those cases, the Senate delay can be overridden if a majority in the House passes these bills three times in succession.

12.2. Rule of Law Institutions

Rule of law institutions play a crucial role in economic development. They guarantee accountability, predictability, and transparency in governance. The strength of these institutions increases business confidence, attracts investments, and guarantees the respect and enforcement of property rights and freedoms. In a country like Jamaica, with one of the highest violent crime rates in the world, rule of law institutions face multiple challenges. This section assesses these institutions and their challenges in Jamaica.

12.2.1. *Strength of Property Rights*

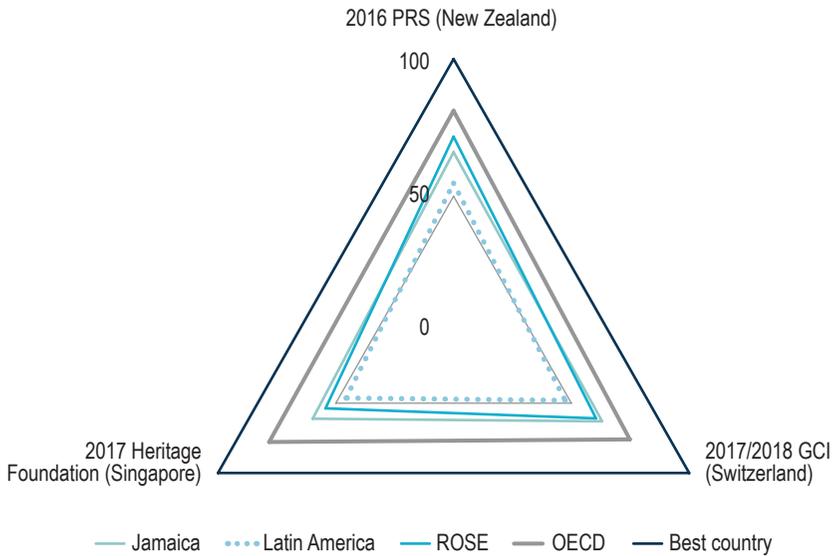
Jamaica performs relatively well in terms of property rights, although it has some weaknesses in the institutional arrangements in place to protect them. According to the Heritage Foundation's 2017 Index of Economic Freedom, approximately 55 percent of the land in Jamaica is registered, but a sizable percentage of those properties lack current titles and almost 20 percent of the population are squatters. These conditions lead to difficulties in developing land, proving ownership, and even taxing property. The main institutional challenges are related to strict land law requirements and long processing time incurred by the Jamaican title registration system (Koh and Knight 2014). These institutional challenges are recognized as the main hindrances for land registration and are key factors that undermine property rights and the rule of law.²⁶

Political Risk Services' 2016 Index of Protection against Expropriation, which objectively assesses the strength of property rights across 140 countries worldwide, and the Property Rights Index measured within the World Economic Forum's 2017/2018 Global Competitiveness Index, suggest that Jamaica over-performs compared to Latin American countries and has a similar performance to ROSE (Figure 12.3).

12.2.2. *Protection of Fundamental Human Rights*

Jamaica's constitution provides that every person, regardless of race, place of origin, political opinions, color, creed, or gender is entitled to certain fundamental rights and freedoms that include the right to life, personal liberty, freedom of movement, freedom from inhumane treatment,

²⁶ The Heritage Foundation's Index of Economic Freedom summary for Jamaica is available at: <http://www.heritage.org/index/country/jamaica>.

Figure 12.3 Jamaica: Strength of Property Rights

Sources: 2016 Political Risk Services (PRS) database (www.prsgroup.com); World Economic Forum, 2017/2018 Global Competitiveness Index (GCI) database; and the Heritage Foundation 2017 Index of Economic Freedom (www.heritage.org).

Note: Each measure was standardized to obtain an index ranging between 0 (worst performance) and 100 (best performance) using the following formula: $(var - min)/(max - min)$, where *var* is the individual country measure, and the maximum and minimum are the highest and lowest value in the datasets, respectively.

enjoyment of property, freedom of conscience, freedom of association, respect for private and family life, and freedom from discrimination.²⁷ The violation of any of these fundamental rights can be appealed to the Supreme Court (or on appeal to the Court of Appeal) for enforcement of rights and for redress.

The main human rights challenges in Jamaica are associated with access to justice and extra-judicial killings by security forces. According to the U.S. State Department's "2016 Country Report on Human Rights Practices," Jamaica's judicial system is over-burdened, under-resourced, and dysfunctional, which obstructs access to justice for victims of crime and their families and facilitates corruption and impunity.

International organizations such as Americas Watch, Amnesty International, and the United Nations have raised concerns in recent decades about police brutality and extra-judicial killings. Following the 2010 police operations in Tivoli Gardens and the subsequent state of emergency, the UN

²⁷ Chapter III of the Jamaica Constitution covers fundamental rights and freedoms.

Special Rapporteur and Amnesty International found evidence of excessive use of force by the police and raised concerns about the outcome of the June 2002 West Kingston Commission of Enquiry. Statistics of the Independent Commission of Investigations (INDECOM) show that there were 168 police fatal shootings in 2017, a 51.3 percent increase over 2016. The government charged a much larger number of police officers with abuses in 2016 than in the previous year, but the lack of willing witnesses and inefficiencies in the judiciary are main sources for delays in these judiciary processes.

Other human rights problems in Jamaica are related to prison conditions and abuses. Numerous government task force reports, several international organizations (including Amnesty International, Human Rights Watch, and the International Centre for Prison Studies), and the U.S. State Department's Bureau of Democracy, Human Rights and Labor have voiced concerns over overcrowding and deplorable physical conditions in the facilities (Harriott and Jones 2016). Violence and discrimination against women and against lesbian, gay, bisexual, transgender, and intersex populations represent major human rights challenges in Jamaica (U.S. State Department 2017).

According to the World Justice Project's 2016 Rule of Law dimension, Jamaica ranks 45th out of 113 countries in the composite category measuring respect for and enforcement of fundamental rights (with a score of 0.59 out of a maximum of 1). As Table 12.2 shows, Jamaica is ranked marginally above Latin America (0.58) but below ROSE (0.62) and the OECD (0.76).

Table 12.2 shows the individual subcomponents of this category, evidencing that Jamaica ranks poorly in subfactor 4.2 (right to life and security). The World Economic Forum's 2017/2018 Global Competitiveness Index ranks Jamaica 130th and 132nd out of 137 countries on the business costs of crime and violence and organized crime. This is consistent with the high violent crime rates that have affected Jamaica in recent decades and the concerns of abuse of power and extra-judicial killings by the security forces described above. Jamaica's violent crime rate of 223 per 100,000 inhabitants continues to be among the highest in the region.^{28,29} It is estimated that 50.3 percent of people in the country have lost a relative, friend, or other close acquaintance/associate due to violence.³⁰

²⁸ According to the Jamaica Constabulary Force Statistics and Information Management Unit for the period from May 2016 to April 2017.

²⁹ Of these "Category One Crimes," 23 percent are murders and the remaining 77 percent include shootings, rape, robbery, aggravated assaults, robberies, break-ins, and larceny.

³⁰ Source: 2014/2015 Caribbean Crime Victimization Survey in the Latin American Public Opinion Survey (Sutton and Ruprah 2017).

Table 12.2 Protection of Fundamental Rights in Jamaica

Fundamental Rights	Jamaica	Latin America	ROSE	OECD
Overall Fundamental Rights	0.59	0.58	0.62	0.76
4.1 Equal treatment and absence of discrimination	0.62	0.51	0.62	0.70
4.2 The right to life and security of the person is effectively guaranteed	0.45	0.61	0.67	0.86
4.3 Due process of law and rights of the accused	0.70	0.46	0.56	0.73
4.4 Freedom of opinion and expression is effectively guaranteed	0.79	0.61	0.59	0.74
4.5 Freedom of belief and religion is effectively guaranteed	0.60	0.75	0.71	0.76
4.6 Freedom from arbitrary interference with privacy is effectively guaranteed	0.75	0.52	0.51	0.77
4.7 Freedom of assembly and association is effectively guaranteed	0.58	0.66	0.71	0.79
4.8 Fundamental labor rights are effectively guaranteed	0.59	0.56	0.60	0.71

Source: World Justice Project (WJP) (<https://worldjusticeproject.org/our-work/wjp-rule-law-index/wjp-rule-law-index-2016/factors-rule-law>).

Note: Scores for the WJP Rule of Law Index, as well as for its component factors and subcomponents, range from 0 to 1, where scores closer to 1 indicate better performance.

Jamaica's high levels of crime and violence have also affected the country's growth prospects. The relation between high levels of crime and economic growth is well established in the literature: the incidence of crime, as well as the fear of crime and violence, affect investment decisions as well as institutions, divert private and public spending, and constitute a contributing factor that affects the decision of individuals to emigrate (Jaitman 2015).

Jamaica ranks above Latin America, ROSE, and the OECD in subcomponent 4.4 (freedom of expression). The law provides for freedom of speech and press, and these rights are generally respected by the government. According to the U.S. State Department (2017), Jamaica has an independent press, effective judicial protection, and a democratic political system that ensure freedom of speech and the press. The media in Jamaica are active and do not face major restrictions to express different views. There are no restrictions in terms of online content, access to the Internet, or academic freedom.

12.2.3. *Judicial Independence and Effectiveness*

The Jamaican judiciary and legal systems are based on English common law and practice. Jamaica has an independent judiciary branch that is guaranteed in the constitution. This includes prohibiting abolition of the Office of Judge of the Supreme Court or Court of Appeal while someone is

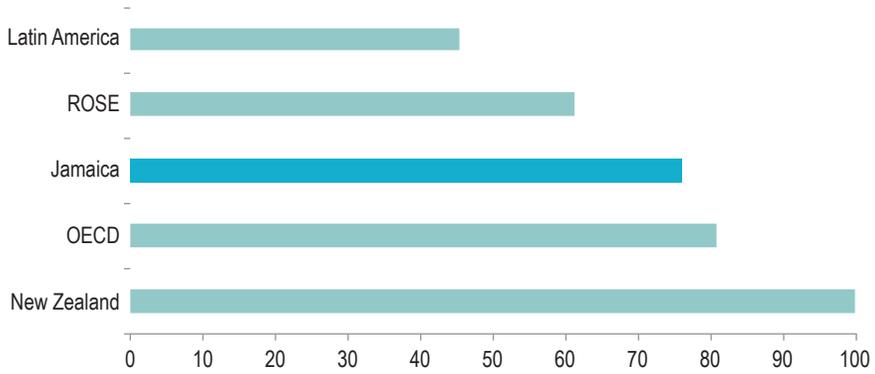
holding that office. It also outlines very clear criteria under which Supreme Court or Court of Appeal judges can be removed from office. Section 20 of the constitution further guarantees judicial independence.

The governor-general appoints the chief justice on the recommendation of the prime minister and following the prime minister's consultation with the leader of the opposition. The chief justice is the head of the judiciary, and by virtue of that office, he or she also is chairman of the Judicial Service Commission. Hence, the chief justice handles administrative matters such as appointments and transfers. The president of the Court of Appeal is also appointed by the governor-general on the advice of the prime minister, following the latter's consultation with the leader of the opposition. In addition to president's duties in the Court of Appeal over which he or she presides, the president is a member of the Judicial Service Commission. There is no standard tenure for either of these positions and they may serve until retirement (70 years old).

The Judicial Service Commission was constituted under Section 111 of the Jamaican constitution. The members of this commission are (1) the chief justice, who is the chairman; (2) the president of the Court of Appeal; (3) the chairman of the Public Service Commission; (4) one serving or retired judge of any Commonwealth jurisdiction chosen by the prime minister after consultation with the leader of the opposition; and (5) two other members chosen by the prime minister after consultation with the leader of the opposition from a list prepared by the General Legal Council of six persons, none of whom is engaged in active legal practice. This commission advises the governor-general on issues related to appointments, promotions, acting appointments, transfers, disciplinary control of judges including resident magistrates, judge of the Traffic Court, registrar of the Supreme Court, registrar of the Court of Appeal, puisne judges, judges of the Court of Appeal, and all other judges.

The other judges are appointed by the governor-general on the recommendation of the Judicial Service Commission. The selection process for judges is meant to be open, transparent, and based on meritocracy. An invitation for application is opened and there are several requirements that include years of experience as an attorney-at-law and a proven track record of integrity.

The attorney general is appointed directly by the prime minister, and is therefore a political appointee, serving as the principal legal adviser to the government. The solicitor general has overall administrative responsibility for running the attorney general's department. Although key appointments in the judicial system are decided by the political authorities, judicial independence in Jamaica is better than in Latin America and ROSE, as shown

Figure 12.4 Jamaica: Judicial Independence Index

Source: Authors' calculations based on the database in Berkman et al. (2008).

Notes: Each measure was standardized to obtain an index ranging between 0 (worst performance) and 100 (best performance) using the following formula: $(var - min)/(max - min)$, where *var* is the individual country measure, and the maximum and minimum are the highest and lowest value in the datasets, respectively. New Zealand is the country with the highest Judicial Independence Index score worldwide.

in Figure 12.4. One of the main reasons that may explain Jamaica's performance on this index is citizens' perception of the independence of the justice system.³¹

Three courts handle criminal matters at the trial level in Jamaica. First, the Resident Magistrates courts, established not by the constitution but by the *Judicature (Resident Magistrate's) Act*, are empowered to deal with less serious civil and criminal matters as well as with mutual assistance and extradition cases. In a review in 2006 of the Jamaica Justice System Reform, the Jamaica Bar Association raised concerns about the lack of constitutional protection of the Resident Magistrates courts (Buckley 2006). The second court that handles criminal matters is the Supreme Court which tries all felonies except those involving firearms, and the third is the Gun Court, which tries felonies that involve firearms. Currently, cases can be referred as the final court of appeal to the Judicial Committee of the Privy Council in the United Kingdom. Nevertheless, in the context of legal reform in Jamaica, there is a potential to replace the Privy Council with the Caribbean Court of Justice. Nevertheless, only three Caribbean states (Barbados, Belize, and Guyana) have made this replacement, and Jamaica has not yet indicated any timeline for doing so.

³¹ Jamaica scores relatively high compared to other Latin American countries on the World Economic Forum's Global Competitiveness Index on judicial independence, which is based on the question: "To what extent is the judiciary in your country independent from influences of members of government, citizens, or firms?"

Jamaica is among those countries that spend the least on justice administration, at around 0.06 percent of gross domestic product (GDP). Conversely, Jamaica has the highest percentage of crime-related police expenditures at almost 2.04 percent of GDP according to upper-bound estimates (Jaitman 2015). For instance, while the Ministry of National Security received JA\$56.4 billion for recurrent expenditures in FY 2017–2018, the Ministry of Justice and all its departments (including the courts, the director of public prosecutions, and others) received JA\$6.8 billion (0.374 percent of GDP).³²

In 2009, the Court Management Services (CMS) was established as an institution independent from the Ministry of Justice to fulfil the stipulations of the constitution in relation to the separation of the administrative functions of the judicial and executive arms of government. Previously, the Ministry of Justice was in charge of all the budgetary allocations for courts, as well as for administrative matters. With this change, the CMS is responsible for performing a range of court-related administrative services including finance and accounts, human resource management and administration, property management and maintenance, and internal audit. The indicators used by the CMS to allocate the budget to courts are unclear.

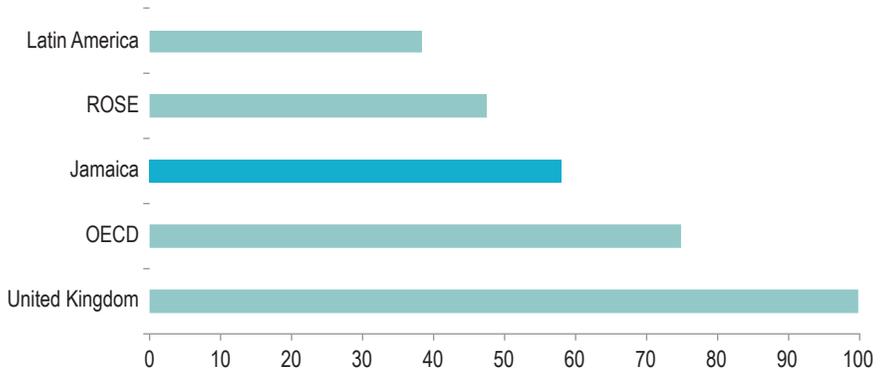
Although the judiciary branch is largely independent, it exists within an overburdened justice system operating with inadequate resources, both human and material.³³ Despite the fact that Jamaica performs better than ROSE and Latin American countries in terms of judicial effectiveness (Figure 12.5), the legal system is still inefficient and significantly below OECD standards. In addition, organizations such as the Heritage Foundation claim that long-standing ties between elected representatives and organized criminals allow some gangs to operate with impunity.³⁴

Trials in many cases are delayed for years and numerous cases have been dismissed because files cannot be located. The situation is

³² Ministry of Finance and the Public Service, “Estimates of Expenditure 2017/2018,” available at http://www.mof.gov.jm/downloads/budgets/eoe/Estimates_of_Expenditure_2017-2018.pdf.

³³ The Justice Reform Task Force in 2007 reiterated the inefficiencies in Jamaica’s justice system and identified several issues that contribute to the problem. Some of the main matters identified include low crime detection rates, which are a consequence of long case processing delays and low conviction rates for those arrested, disrespect of individuals before the court, poor infrastructure, underfunding, outdated and inefficient procedures, and unequal treatment, benefits, and protection.

³⁴ See the “Rule of Law” section of the Heritage Foundation’s 2018 Index of Economic Freedom at <https://www.heritage.org/index/country/jamaica>.

Figure 12.5 Jamaica: Judicial Effectiveness Index

Source: Authors' calculations based on the 2017 Heritage Foundation Index of Freedom (www.heritage.org) database.

Notes: Each measure was standardized to obtain an index ranging between 0 (worst performance) and 100 (best performance) using the following formula: $(var - min)/(max - min)$, where *var* is the individual country measure, and the maximum and minimum are the highest and lowest value in the datasets, respectively. The United Kingdom is the country with the highest Judicial Effectiveness Index score worldwide.

exacerbated by a court administration system that employs archaic practices that prevent justice from being dispensed efficiently (Sutton and Ruprah 2017). Several U.S. State Department reports on human rights practices, along with surveys and poll results, have reiterated the findings of the task force report related to denial of a fair public trial to poor defendants and a backlog of cases (U.S. State Department 2012, 2014). The number of professional judges in Jamaica per 100,000 inhabitants is comparable only to sub-Saharan Africa and below other countries in the Caribbean and Latin America (Table 12.3). An inefficient and ineffective justice system poses a considerable challenge to reducing crime and violence in Jamaica.

Citizens' perceptions of the justice system are also affected by the system's inefficiencies and lack of effectiveness. According to the 2014 Latin American Public Opinion Project (LAPOP) Survey, the level of trust in the justice system in Jamaica is among the lowest in the region (41 percent). Similar results are found in the Caribbean Crime Victimization Survey (CCVS), where 34 percent of respondents have no trust at all in the courts in Jamaica, the highest level in the Caribbean.³⁵ The level of distrust in the justice system and the high level of fear that citizens have for their own safety because of endemic violence have negatively contributed to a

³⁵ See the Caribbean Crime Victimization Survey module of the Latin American Public Opinion Project (CCVS/LAPOP), 2014/2015.

Table 12.3 Judicial Density

Country	Number of Professional Judges per 100,000 Population
Jamaica	3
The Bahamas	12
Trinidad and Tobago	7
Barbados	8
World Average	18
Regional Averages	
Latin America and the Caribbean	9
East Asia and Pacific (all income levels)	6
Europe and Central Asia (all income levels)	27
Middle East and North Africa (all income levels)	11
Sub-Saharan Africa (all income levels)	3

Source: Sutton and Ruprah (2017).

properly functioning justice system in which the public assumes its roles as witnesses or jurors.

Jamaica has created a Justice Reform Implementation Plan 2015–2020 that incorporates and adds to major justice sector initiatives being undertaken by the Ministry of Justice. These initiatives include management of the inventory of cases, reduction of case backlogs in the courts, strengthening of legislation and the legislative process, retooling and capacity development of major institutions within the justice system, introduction of other institutions such as the National Human Rights Institute, and development of a social component that will support improved access to justice at the community level and increased public trust and confidence in the justice system (Ministry of Justice 2016).

Another two critical reforms being undertaken are the establishment of a National Child Diversion Policy and improvements in access to justice. The Child Diversion policy will address the need for differentiated treatment for child offenders through a process of reconciliation, accountability, rehabilitation, reintegration, and empowerment. This approach is in keeping with the United Nations Convention on the Rights of the Child and in recognition of the core convention principle that the best interest of the child is of paramount importance.³⁶ In order to improve access to justice, the position of legal aid counsel was established in 2012. The counsel is mandated to organize and establish Legal Aid Clinics to administer

³⁶ See the Convention on the Rights of the Child, Section 40.

an efficient and coordinated legal aid system and to provide affordable legal representation for persons charged with an offence punishable by imprisonment.

Jamaica has several weaknesses in terms of property rights and the protection of fundamental human rights, as well as judicial effectiveness. Nevertheless, the government is implementing important measures to overcome some of these challenges. Law enforcement is a critical component to ensure that Jamaica will strengthen rule of law institutions. The next section assesses the main law enforcement institutions in Jamaica.

12.2.4. Law Enforcement

Ministry of National Security

The Ministry of National Security (MNS) is the main institution with responsibility for Jamaica's public safety, having overall responsibility for security and defense. In 2001, following the separation from the Ministry of National Security and Justice, the MNS was established as a stand-alone ministry with the mandate to (1) facilitate the maintenance of law and order; (2) protect Jamaica against internal and external threats; (3) ensure the safety of Jamaica's borders; and (4) punish and rehabilitate offenders.³⁷

The current organizational structure of the ministry, which is the result of several reforms that have produced a number of mergers and transfers, has seven major agencies: the Jamaica Constabulary Force (JCF), Jamaica Defence Force (JDF), Department of Correctional Services (DCS), Passport, Immigration and Citizenship Agency (PICA), Firearm Licensing Authority (JFLA), Institute for Forensic Science and Legal Medicine (IFSLM), and Private Security Regulation Authority (PSRA).³⁸ The MNS saw a 23.4 per cent increase in its budget allocation for FY 2018–2019, moving to JA\$78.5 billion from JA\$63.6 billion in FY 2017–2018.³⁹

³⁷ The MNS Vision and Mission Statement is available at <http://www.mns.gov.jm/content/vision-and-mission>.

³⁸ The ministry is currently undergoing a new strategic review that is looking its organizational structure.

³⁹ Chris Patterson, "Gov't Increases Allocation for Crime-Fighting," Jamaica Information Service, 8 March 2018. Available at <http://jis.gov.jm/govt-increases-allocation-for-crime-fighting/>.

The Jamaica Constabulary Force

The JCF has primary responsibility for law enforcement. The force is headed by the commissioner of police, who is appointed by the prime minister. Since its independence, Jamaica has had 17 commissioners of police, some who served in the Constabulary Force prior to appointment, along with others coming from the JDF. Due to the high levels of violent crime in Jamaica, this position is subjected to a lot of criticism and pressure from diverse stakeholders, which has translated in relatively shorter tenures.⁴⁰

Between 2015 and 2018, the organizational structure of the JCF has experienced changes as a result of several independent reports.⁴¹ The most significant changes were the merger of the Island Special Constabulary Force with the JCF with the objective to eliminate administrative duplication and free up more personnel for line duty. The Major Organized Crime and Anti-Corruption Agency was established through the union of the Organized Crime Division and the Flying Squad. Entities that operated independently—such as the Police Academy, Jamaica Constabulary Staff College, Caribbean Search Centre, Firearm and Tactical Training Unit, and the Driving School—were merged into the Jamaica Police College. A specific branch of the police, the Crime Prevention Community Safety and Security Branch, was established to deal with police-citizen relations, a problematic area for the JCF. This branch is in charge of community policing and is trying to build public confidence and better relations with communities.

Currently, the government of Jamaica is focusing on a legislative reform for the JCF.⁴² The legislation proposes to address some of the force's major concerns, including establishment of key civilian posts, citizen relations, and improving the accountability and monitoring of performance of police officers.

Training of police officers is conducted by the Jamaica Police College. Training generally combines academic as well as on-the-job training.

⁴⁰ For example, between 2010 and 2018 there were four leadership changes.

⁴¹ Canute S. Thompson, "The Making of a Seamless Merger," *The Gleaner*, 1 June 2014. Available at <http://jamaicagleaner.com/gleaner/20140601/lead/lead8.html>.

⁴² The new legislation proposes to rebrand the JCF into the Police Service of Jamaica, emphasizing services for citizens. The new draft legislation aims "to ensure that the people of Jamaica have a police service that is responsive to their needs by embracing a community policing philosophy, which recognizes the value of partnership and policing with the consent of the people." See also "Police Makeover Closer—Draft legislation Proposes Significant Changes to JCF," *The Gleaner*, 24 December 2017. Available at <http://jamaica-gleaner.com/article/lead-stories/20171224/police-makeover-closer-draft-legislation-proposes-significant-changes>.

All police applicants undergo a 20-week training program in the basic skills and competencies of policing. Nevertheless, training is insufficient, and curricula have not yet been updated to incorporate the use of technology for policing. For instance, police officers working in the Criminal Investigation Branch only receive six weeks of training to become crime investigators.

Jamaica has 178 police stations around the country with limited information and communications technology (ICT). Police stations are interconnected through a low capacity microwave network, only 12 percent have a high-speed Internet connection, and only 67 percent have at least one functional computer. There is no centralized crime report database. Crime reports are aggregated manually, entered into a spreadsheet, and transmitted by email to their divisional centers, which in turn transmit them to headquarters.⁴³ Where no working computer is available, the information is transmitted by two-way radio. Any attempt to digitize and centralize police reports and case management requires better technology and more and better equipment in all police stations.

Jamaica has a high police density of 423.8 police personnel per 100,000 population. This police density is significantly higher than the world average (Jaitman 2015). Nevertheless, compared to other countries in the Caribbean, Jamaica has the lowest police density and a proportionately smaller percentage of its population employed in public security (Table 12.4). Furthermore, Jamaica has the highest percentage of crime-related police expenditures (2.04 percent of GDP) in Latin America and the Caribbean (Jaitman 2015). However, relatively high police density in Jamaica (compared to world averages) has not translated into rapid police response or greater effectiveness in solving and investigating crime. Police clearance rates for the most violent crimes such as homicides are

Table 12.4 Police Density

Country/Region	Number of Police Personnel per 100,000 Population
Jamaica	423.8
The Bahamas	846.1
Trinidad and Tobago	477.1
Barbados	503.9
Latin America and the Caribbean	435.6
World Average	365.5

Source: Jaitman (2015).

⁴³ *Source:* JCF Information and Communication Technologies Department.

low (43 percent)⁴⁴ compared to countries like the United States (59 percent), Canada (67 percent), and other Caribbean countries (Bahamas 61 percent).⁴⁵ The limited use of technology in policing discussed above also explains the high police density and its limited effectiveness in preventing and controlling crime and violence.⁴⁶ Women are severely under-represented on the force in general and in its upper ranks (JCF 2015, 2016). Finally, with an attrition rate of around 500 police officers per annum, police attrition and turnover continue to be one of the main challenges for the police force.⁴⁷

There are currently three formal external oversight bodies that are in charge of police accountability in Jamaica: The Police Services Commission (PSC), Police Civilian Oversight Authority (PCOA), and Independent Commission of Investigations (INDECOM). The PCOA was established in 2006 as a mechanism, external to the JCF to ensure accountability, adherence to policy guidelines, and observance of proper policing standards by the force (Ministry of National Security 2008). The PCOA has a membership of seven. The chairman is appointed by the governor-general after consultation with the prime minister and the leader of the opposition. Currently, the government is trying to implement legislative measures to merge the PSC and the PCOA into one entity to be called the Police Service Authority.⁴⁸ The merger of these two entities would remove the ambiguity as to whom the police commissioner is accountable and create a single institution in charge of the appointment of the police commissioner, promotions,

⁴⁴ A case is considered cleared up when a suspect is arrested and charged with the crime and the casefile is sent to prosecution (source: JCF, Statistics and Information Management Unit).

⁴⁵ For all countries data is for 2016, except for Bahamas which is the average 2010-2015.

⁴⁶ For instance, police crime reports and registries are kept manually, and the information collected is not sufficient to identify crime patterns. All police stations keep between 20 and 42 different paper-based registries, from the Station Diary, which registers all events that are reported at the station, to registries for duty assignments, shift sign-ins, and weapons check-outs, among others. For instance, just at the police level (excluding the work of investigators), police officers need to fill out nine different paper-based registries in relation to incidents like shootings, murders, or sexual offences. The existing paper-based forms that police use to file crime reports are ill-suited for the identification of crime patterns. For example, in the case of domestic violence, early identification through documented history of abuse is critical in preventing the escalation of crime.

⁴⁷ "Montague Bemoans High Turnover Rate in Police Force," *The Gleaner*, 2 September 2017. Available at <http://jamaica-gleaner.com/article/lead-stories/20170902/montague-bemoans-high-turnover-rate-police-force>.

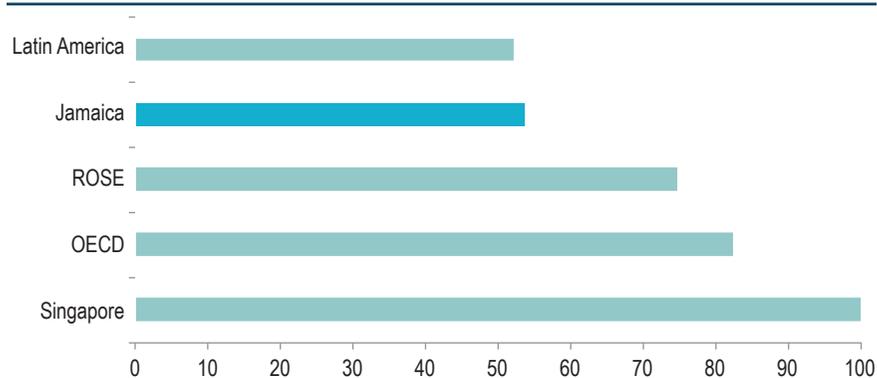
⁴⁸ This measure was first recommended by the Strategic Review of the JCF conducted in 2008.

staff discipline, and the accountability and performance of the JCF. INDECOM is an independent, non-police agency with the power to investigate allegations of misconduct by members of the public against members of the Jamaica Constabulary, Defence Forces, and correctional officers. A Strategic Review of the JCF found that none of these agencies were fully effective (Ministry of National Security 2008). The report states that while the functions of each of these agencies are legitimate, the execution of those functions by three different entities is inefficient, ineffective, and serves to diffuse accountability by creating confusion among the public and police. The review also points out the limitations of the entities in terms of resources and capacity constraints hindering their ability to have a significant impact on the weaknesses of the JCF. However, no practical action has been taken as a result of the Strategic Review.

Although citizens seem to be satisfied overall with the police in Jamaica, trust levels are low. More than 60 percent of the respondents to the 2014 CCVS interviewed in the Kingston metropolitan area declared being satisfied or very satisfied with police performance.⁴⁹ These numbers are confirmed by the 2014 LAPOP Survey, in which satisfaction with police performance in Jamaica was significantly higher than the average for Latin America and the Caribbean and for countries with lower crime rates like Uruguay or Ecuador. Similarly, according to the CCVS more than 60 percent of respondents seem to think that police are doing a fairly good job or a good job in controlling crime. However, given the high levels of under-reporting of crime in Jamaica, these numbers need to be taken with caution. Inversely, the legitimacy and trust of the police in Jamaica has been eroded by claims of abuse and excessive use of authority. Police harassment was perceived as a problem in Jamaica by almost half of the residents of neighborhoods with a gang presence (44.8 percent). Similarly, trust in the police seems to be an important challenge, with 37 percent of the respondents saying they do not trust the police.

The outlined institutional weaknesses of the JCF in terms of efficiency, trust, high attrition and turnover of police officers, excessive use of force, and poor accountability have translated into poor outcomes. JCF clear-up rates are low and murder rates in the country have increased exponentially in the last three years. According to the World Justice Project's 2016 Rule of Law Index, Jamaica ranks 90th out of 113 countries in order and security. As Figure 12.6 shows, Jamaica's Order and Security Index barely performs

⁴⁹ Caribbean Crime Victimization Survey module of the Latin American Public Opinion Project (CCVS/LAPOP), 2014/2015.

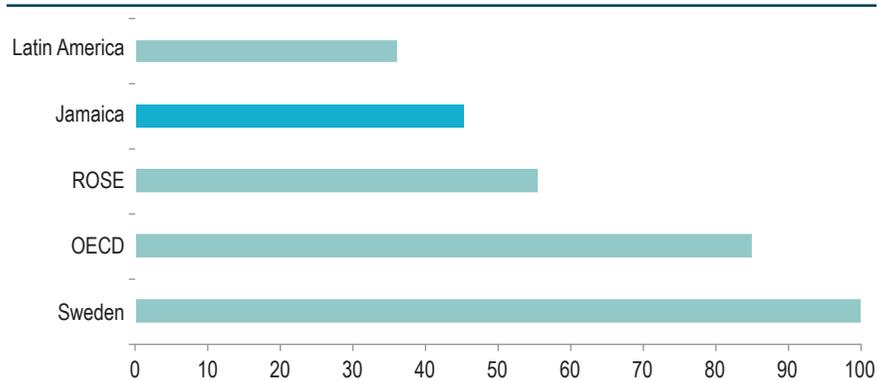
Figure 12.6 Jamaica: Order and Security Index

Source: Authors' calculations based on the World Justice Project 2016 database.

Notes: Each measure was standardized to obtain an index ranging between 0 (worst performance) and 100 (best performance) using the following formula: $(var - min)/(max - min)$, where *var* is the individual country measure, and the maximum and minimum are the highest and lowest value in the datasets, respectively. Singapore is the country with the highest Order and Security Index score worldwide.

above the average for Latin American countries and considerably below ROSE and the OECD.

This section has explored and outlined some of the main challenges of rule of law institutions in Jamaica. As shown in Figure 12.7, Jamaica underperforms in this dimension when compared to ROSE and the OECD. Strengthening rule of law institutions is and will be one of the main challenges of the country to reduce the incidence of crime and violence, thereby contributing to sustainable economic growth.

Figure 12.7 Jamaica: Rule of Law

Source: World Bank, 2017 World Governance Indicators database (www.govindicators.org).

Notes: Percentile ranking score ranging from 0 (worst in rule of law) to 100 (best in rule of law). Sweden is the best country worldwide in terms of the rule of law. Rule of law captures perceptions of the extent to which agents have confidence in and abide by the rules of society, and in particular the quality of contract enforcement, property rights, the police, and the courts, as well as the likelihood of crime and violence.

12.3. Institutions for Human Capital Development

As shown in Chapter 4, two main institutions supporting human capital development have been highlighted in the literature: education and health institutions. Therefore, this section documents the condition of these institutions in Jamaica.

12.3.1. Education

The related evidence presented in Chapter 4 suggests that the quality of education matters more than the quantity. Furthermore, the quality of education hinges primarily on the quality of teachers. Therefore, this section will focus not only on the ability of educational institutions to offer educational services coverage, but also on the state of institutions directed toward ensuring appropriate teacher quality.

Education in Jamaica is governed by the 1980 *Education Act*, which defines four education levels: early childhood, primary, secondary, and tertiary levels. Private providers exist at all levels but are dominant at the pre-primary level, where only about 20 percent of institutions are public. At the primary level, approximately 85 percent of institutions are publicly funded. Both public pre-primary and primary education are provided free of cost for households, as guaranteed in the Bill of Rights.⁵⁰ At the secondary level, most schools (94 percent) are public. There is no cost, but there is an expectation of parents making contributions based on their financial ability. At the tertiary level, the government provides a subsidy directly to public institutions, as well as to the regional University of the West Indies. Students pay in general approximately 20 percent of the costs at this level.

The Ministry of Education is responsible for the management and administration of public education in Jamaica. The organization is one of Jamaica's largest public entities and is comprised of 11 agencies, six regional offices, and a central office with approximately 40 units that fall under five divisions. Together they oversee more than 1,000 public educational institutions that serve over 100,000 students and over 20,000 teachers. The Ministry of Education is also responsible for two public universities and several community, multidisciplinary, and teachers' colleges.

The Ministry of Education is also responsible for educational quality assurance, which is operationalized through different entities. First, The Early Childhood Commission regulates the pre-primary level. It is an agency under the Ministry of Education but operates independent of the

⁵⁰ The *Charter of Fundamental Rights and Freedoms (Constitutional Amendment) Act*, 2011.

ministry and is governed by a board. It does take policy directive from the minister of education. Second, the National Education Inspectorate (NEI) aims to ensure educational quality at the primary and secondary levels. This is designed to be carried out through a three-year cycle of school inspections, which are then reported to Parliament after each round of inspection. The NEI is an agency of the Ministry of Education, is newly established, and is slated to be an executive agency governed by a board. The NEI provides policy advice and takes policy directives from the minister of education. Third, at the tertiary level the Jamaica Tertiary Education Commission is being established to regulate the tertiary sector and will be the gateway to entry. The University Council of Jamaica is the national accrediting body for tertiary education institutions and programs.

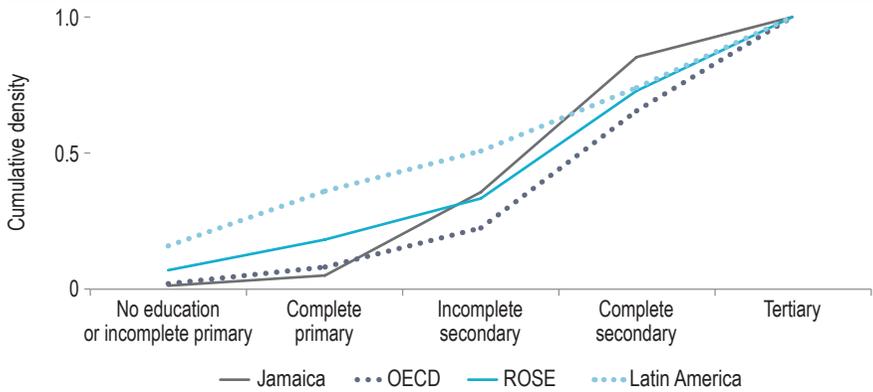
Due to the strong emphasis on expanding access to education over the years, Jamaica has made noteworthy progress, reaching net enrolment rates of 99 percent in pre-primary education, 92.5 percent in primary education from grades 1–6, and 80 percent for lower secondary education grades 7–9. However, coverage declines sharply at the upper secondary level, with only 62 percent of youngsters enrolled at this level.⁵¹ At this level, there are still schools on shift and classrooms are overcrowded.⁵² As such, the educational attainment profile is still unsatisfactory, with a relatively sizable share of the population with incomplete secondary education (Figure 12.8). Indeed, while the proportion of persons not entering secondary school, at 4.9 percent, is below that of comparators such as Latin America (36 percent), ROSE (18 percent), and the OECD (8 percent), the proportion of secondary school dropouts at 31 percent is significantly higher (Latin America, 14.7 percent; ROSE, 15 percent; and the OECD, 14.3 percent). This is also reflected in the fact that the share of persons with tertiary education, at 14.8 percent, is significantly below all comparators (Latin America, 26.1 percent; ROSE, 26.9 percent, and the OECD, 34.6 percent).

In addition, important differences in the quality of education persist and educational achievements are mixed.⁵³ Student performance,

⁵¹ Jamaica Survey of Living Conditions, 2012, and Ministry of Education statistics.

⁵² Seven percent of schools operated on shifts as of the 2016–2017 Education Statistics Report.

⁵³ Despite improvements, student performance in English and math is still low. In 2017, some 85 percent of all 4th grade students achieved mastery on the Grade Four Literacy Test and 67 percent on the Grade Four Numeracy Test. On the Grade Six Achievement Test (GSAT), the average score was 66 percent for English and 59 percent for math. Finally, the percentage of Grade 11 students passing the Caribbean Secondary Education Certificate (CSEC), administered by the regional Caribbean

Figure 12.8 Jamaica: Educational Attainment

Source: Authors' calculations based on the 2015 Jamaica Survey of Living Conditions and the World Bank's 2016 World Development Indicators database.

Note: Educational attainment is measured among working age adults (25–65 years old) who have completed their formal education.

although on an increasing trend, may not achieve the results envisioned at the onset of the Education Sector Transformation Programme.⁵⁴ More importantly, inequality in the school system is pervasive.⁵⁵ Since spaces at the secondary level are limited, the Grade Six Achievement Test (GSAT –to be phased out by 2018) and the upcoming Primary Exit Profile exam (PEP) are used for placement purposes, with the most prestigious schools receiving the majority of high-performing students as well as a disproportionate share of resources and highly trained teachers. While the schools receive the same allocations (and the teachers earn the same salaries), these “privileged schools” raise more funds from parents, who often are alumni of the same school, and from activities such as fundraising. Similarly, these schools attract the best teachers. As better-off parents have more resources to prepare their children for the entry exams to these schools, they attract students from more affluent backgrounds. As a result, the proportion of students at all levels (primary and secondary)

Examinations Council, increased for English from 28.5 percent in 2001 to 70.8 percent in 2017 and for math from 16.6 percent to 50.2 percent, a significant improvement but still just on par with the Caribbean average.

⁵⁴ The Education System Transformation Programme was established in 2005 to address shortcomings identified in the assessment of Jamaica's education sector as documented by the 2004 Task Force on Educational Reform.

⁵⁵ According to the September 2015 Chief Inspector Baseline Report, only 45 percent of primary and secondary schools were rated as overall effective. Similarly, students' attainment in English was rated below target in 78 percent of schools.

performing above average reached 71 percent in schools located in high socioeconomic locations compared to 31 percent of those in low socioeconomic locations. Likewise, while 74 percent of children ages 17–18 from the wealthiest group enrolled in upper secondary schools showed satisfactory performance, only 37 percent of those from the poorest group did so. Furthermore, only 4 percent of students from this latter group continued on to tertiary education.⁵⁶

Important gaps exist for Early Childhood Education in terms of regulation and coverage. The 2015 Jamaica Survey of Living Conditions indicated that there continues to be high levels of enrolment for children aged 3–5, with a gross enrolment rate of 99.9 per cent (100 percent for boys and 99.7 percent for girls). However, there are quality concerns, as the pre-primary level is dominated by a mostly unregulated private supply of early childhood institutions. Currently, only 32.4 percent of the teachers at this level satisfy the required minimum qualifications, and around 30 percent of these institutions are operating without a permit or are not in compliance with minimum acceptable standards of practice as established by the Early Childhood Commission.⁵⁷ Also, as of December 2017, most early childhood institutions had not been certified by the Early Childhood Commission.⁵⁸

In terms of effective institutions directed toward incentivizing better teaching quality. Chapter 4 has suggested that the critical institutional components appear to be the monitoring of teachers' effort and quality, and performance-based hiring and retention decisions.

Prior to 2004 no official system of teacher performance evaluation existed in Jamaica. Starting that year, the Ministry of Education implemented a standard teacher performance evaluation system in all public schools. Under that protocol, each teacher is evaluated through observations of teaching skills and an assessment of teacher professionalism. The evaluation team includes the school principal, the head of the department, and a third professional chosen by the teacher subject to the evaluation (Campbell 2014). While having an institutionalized and periodic evaluation system is positive, the instituted evaluation system does not conform to best evaluation practices. This is because the evaluation is

⁵⁶ Compiled by the PIOJ from data supplied by STATIN, 2012, and provided by the Ministry of Education in April 2014.

⁵⁷ The Early Childhood Regulations (2005) identify a qualified teacher as having, at a minimum, a diploma from a teacher training institution.

⁵⁸ See the report by the Early Childhood Commission for the 2017 Economic and Social Survey of Jamaica Social Development, Social Protection and Culture.

based on qualitative and subjective assessments by the evaluation team, rather than on quantitative and objective performance of the teacher's students. Indeed, evidence provided by Araujo et al. (2016) shows that teacher value-added measures based on student evaluations provide a better measure of teacher effectiveness than traditional teacher assessments based on direct evaluations or observation of teachers. The current Jamaican education system already implements nationwide standardized examinations to students across primary and secondary school.⁵⁹ However, databases containing those results at the student level are not systematized and linked at the individual level across time to track student performance. Organizing such a database and linking it to individual teachers in charge of each student across different grades could be exploited to compute individual teacher value-added measures based on objective student performance.

In terms of hiring and retention decisions, there are no monetary awards for high performance, but promotions depend on performance. In addition, before a new teacher's position becomes open-ended, there is a mandatory probation period that relies on performance evaluations. While the concept of performance-based hiring and promotion decisions is positive, the performance evaluation system in place as shown above could be improved to strengthen its objectivity and impartiality. Furthermore, while the Jamaica Teaching Council (JTC) has been established as a statutory body to register and license teachers, the empowering legislation has been delayed several times. The envisioned licenses would be for a period of five years and subject to renewal based on evidence of ongoing professional development (minimum 36 hours per year) in the relevant area of specialization. Once the legislation is implemented, schools would not be allowed to employ teachers who are not licensed. Professional development opportunities are envisioned to be provided through the JTC and teachers would be paid on a scale with increments earned upon performance reviews. As such, the establishment of the JTC along with the inclusion of objective performance evaluations of teachers based on student-level value-added measures constitute highly relevant institutional aspects that should rank high on the policymakers' agenda.

⁵⁹ These include examinations within primary school in the first, third, fourth and sixth (Grade Six Achievement Test - GSAT) grades. At the secondary level, these include the Caribbean Secondary Education Certificate (CSEC) and the Caribbean Advanced Proficiency Examination (CAPE), administered by the regional Caribbean Examinations Council.

12.3.2. Health

Jamaica's health system is organized as a public national health system, with a supplemental private health system.^{60,61} The Ministry of Health is the main provider of secondary care, with around 95 percent of all hospital beds. The country established a strong primary care platform in the 1980s with over 300 health centers that provided almost the entire population access to care within 10 walking miles. There are 27 hospitals with a total capacity of 5,000 beds, and 18 of those hospitals are acute care facilities, six are specialty hospitals, and three are chronic-care hospitals. In addition, the Ministry of Health has primary responsibility for policy formulation, regulation, and health intelligence. Responsibility for service provision has been decentralized to four Regional Health Authorities that oversee Jamaica's 14 parishes.

Health services are provided by a network of 348 primary care units and hospitals. Most providers are public (94 percent of hospital beds), although 75 percent of outpatient care is provided by the private sector. The private sector offers imaging, laboratory, pharmacy, ambulatory, and hospital services, although it provides only around 6 percent of total bed capacity. The population can also access private health facilities through out-of-pocket payments. Since 2008, most services offered by the public sector have been free of charge for users. Indeed, Beuermann and Pecha (2016) show that the 2008 reform significantly reduced the number of productive days lost due to illnesses and increased the labor supply among working-age adults. In the early 2000s, the country launched the National Health Fund, which today provides medicines for 15 chronic illnesses.

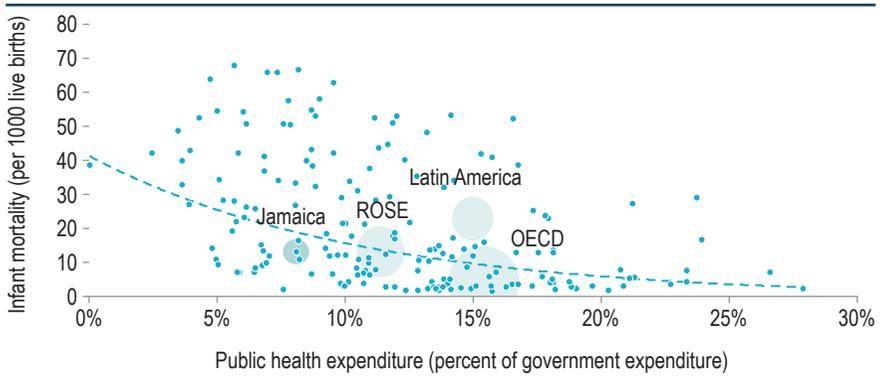
The public health system is financed mainly through general taxation. Since 2009, public health spending has averaged 3 percent of GDP, among the lowest levels in the Latin America and Caribbean region. The National Health Fund is financed by a combination of earmarked taxes on tobacco, a special consumption tax, and a 1 percent payroll tax.⁶²

⁶⁰ The abolition of user fees at public facilities in 2008 and the establishment of the National Health Fund in 2003 were aimed at reducing out-of-pocket financing, which still accounts for around 28 percent of expenditure. The National Health Fund provides a drug subsidy program that targets patients suffering from the 15 most common non-communicable diseases and also targets the elderly over 65.

⁶¹ In the 2012 Survey of Living Conditions, 18.8 percent of respondents indicated that they had health insurance, varying from 28.5 percent in the Kingston Metropolitan Area to 12.7 percent in rural areas, and from 4.7 percent among the poorest quintile of the population to 37.6 percent among the richest quintile.

⁶² The taxes on behalf of the National Health Fund are the Special Consumption Tax, collected by Tax Administration Jamaica; the Special Consumption Tax and Tobacco

Figure 12.9 Jamaica: Public Health Expenditures, Physicians per 1,000 Population, and Infant Mortality



Source: Authors' calculations based on the World Bank's 2016 World Development Indicators database.

Note: The size of the bubbles is proportional to the number of physicians per 1,000 population for selected countries or country groups.

In terms of health outcomes, life expectancy at birth (76 years old) is similar to ROSE (75.44 years old) but more than five years longer than the Latin American average, despite considerably less expenditures on public health than both groups. However, Jamaica lags behind more advanced OECD economies (81 years old). In addition, Figure 12.9 shows that although Jamaica has the lowest physician density and the lowest relative share of public health expenditures among comparators, it has infant mortality rates that are lower than Latin America and similar to ROSE.

Jamaica faces challenges with respect to institutional capacity in the health sector. The Ministry of Health has overall responsibility for the sector, including setting standards and hiring health workers. Health workers must be licensed to be able to work in Jamaica, with the licensing processes managed by specific councils. The Medical Council of Jamaica regulates the conditions of medical practice across the country.⁶³ The Nursing Council of Jamaica is a statutory body set up by the government of Jamaica

Tax, collected by Jamaica Customs; and National Insurance, collected by the National Insurance Fund. In FY 2016–2017, the National Insurance Fund payroll tax contributed 54 percent of tax revenue, while the Special Consumption Tax and the Special Consumption Tax and Tobacco Tax contributed 30 percent and 16 percent, respectively.

⁶³ This is done through the 1976 *Medical Act*, last amended 2004. Under amendments in 1996 and 2004, the council also has the duty to issue a practicing certificate annually to a registered medical practitioner if the council is satisfied that the practitioner has complied with prescribed requirements for continuing medical education and has paid the appropriate renewal fee.

to regulate and control the nursing and midwifery professions.⁶⁴ Councils also exist for pharmacists and dental health workers. The councils set and enforce standards and license health professionals, including relicensing that is linked to continuous training.

Pay in the public sector is only weakly related to performance. As public sector workers, health workers have had stagnant or even declining salaries in real terms during most years since the start of the country's fiscal consolidation in 2010.⁶⁵ In addition, migration abroad, especially to the United States, Canada, and the United Kingdom, has also responded to these countries' shortage of health workers and better pay.⁶⁶ As a result, health workers prefer private practice or working abroad, leading to a shortage of qualified health workers in Jamaica.⁶⁷ While migration by health workers is not being tracked, available pieces of information suggest that a substantial part of the trained workforce migrates. For instance, as of September 2017, the British National Health System employed 1,708 Jamaican nationals.⁶⁸ Similarly, a 2009 study estimated that around 21,500 English-speaking CARICOM nurses were working in the United States, Canada, or the United Kingdom, compared to 7,800 working in CARICOM countries (World Bank 2009).

12.4. Economic Institutions

With respect to structure and composition, Jamaica's economy is highly concentrated in a few productive sectors, with services (particularly tourism) responsible for the largest share at about 71 percent of total output, followed by industrial activities at 21 percent, and agriculture at about

⁶⁴ The *Nurses and Midwives Act* of 1964 and the Amendment of 2005 confer on the Nursing Council of Jamaica the power to control the education, training, and practice of nurses, midwives, and assistant nurses in Jamaica. The council also has the responsibility to register nurses and midwives and enroll assistant nurses. Licensing must be renewed every two years.

⁶⁵ The government of Jamaica imposed a wage freeze in 2010. While it was relaxed in 2015, nominal increases have remained subdued given the still high share of revenues dedicated to public sector salaries.

⁶⁶ Jason Beaubien, "Jamaica says U.S. and Others Are 'Poaching' Its Nurses," National Public Radio, 10 January 2017. Available at <https://www.npr.org/sections/goatsand-soda/2017/01/10/508991805/jamaica-says-u-s-and-others-are-poaching-its-nurses>.

⁶⁷ "The Role of Jamaican Nurses in Health Care Sectors," The World Mind, 13 October 2017. Available at <https://edspace.american.edu/theworldmind/2017/10/13/the-role-of-jamaican-nurses-in-health-care-sectors/>.

⁶⁸ "NHS Staff from Overseas: Statistics," UK House of Commons Library, 7 February 2018. Available at <http://researchbriefings.parliament.uk/ResearchBriefing/Summary/CBP-7783#fullreport>.

8 percent.⁶⁹ Industrial activities are concentrated in extractive industries such as bauxite, agricultural processing, and the production of rum, cement, and other consumer products. Despite its relatively small contribution to output, agriculture remains important given its proportionally large share of employment, including in rural areas and among populations at risk. The country's main crops include sugar cane, bananas, coffee, vegetables, meat, and shellfish.

Jamaica's real GDP has increased by an average of only 1 percent annually since the 1980s.⁷⁰ This modest performance has been driven by several endemic and one-off factors, including a history of poor and inconsistent policies leading to inflation and output volatility, government over-borrowing and resulting debt and financial crises, and frequent shocks driven by weather conditions (e.g., droughts), volatile external demand, and natural disasters. The country has also suffered from political and social unrest, rampant crime, and high levels of economic informality. Productivity growth has been stagnant over the past several decades, further limiting the scope for any meaningful increase in output. By the beginning of the 2000s, policy failures and the impact of successive shocks had left the country with one of the world's highest debt burdens, and very few alternatives to deep and meaningful reform of economic policies and institutions.

Since entering into a program supported by the International Monetary Fund under the IMF's Extended Fund Facility in May 2013, and subsequently a 36-month Stand-By Arrangement initiated in November 2016, Jamaica's economic policies, institutional capacity, and related outcomes have improved markedly. Guided by the quantitative and structural objectives of these IMF-supported programs, Jamaica's policymakers have succeeded in establishing and maintaining fiscal discipline—as characterized by large primary budget surpluses—driving down public debt levels, establishing binding fiscal rules, and modernizing central bank policies and objectives. While these and related strides are praiseworthy, further reforms of public and other economic institutions in Jamaica are required to set the stage for more rapid and sustainable growth in the years to come.

12.4.1. *Central Bank Independence and Transparency*

Jamaica's monetary authority is the Bank of Jamaica (BOJ). The BOJ began operations in May 1961 with the objectives of establishing an institution responsible for exchange rate management, monetary policy, and

⁶⁹ Estimates for 2017 from the World Bank's World Development Indicators database.

⁷⁰ Ibid.

regulation of the financial sector. This would replace the currency board that had been in place since 1939. The BOJ was conceived as a key pillar of the country's post-colonial transition and a central component of its new economic institutions and infrastructure (Bank of Jamaica 1991).

The BOJ's current role is similar to that of other monetary authorities, and includes the issuance of bank notes and coins, management of reserves, and acting as the financial agent for the government. Under the 1960 *Bank of Jamaica Act*, monetary policy is aimed at "...regulating the growth of money and credit in line with the resources expected to finance economic activity and generate employment, without undermining the conditions of price stability...[and] ensuring the stability of the financial system is organically related but operationally separate from the conduct of monetary policy."⁷¹

Regarding independence, the BOJ ranked 80th out of 89 central banks assessed worldwide by Dincer and Eichengreen (2014), using data available through 2010 (Table 12.5).⁷² Variables used to compile this index are intended to reflect the independence of the chief executive officer (the governor) and management of the central bank, including as it relates to policy formulation, the definition and construction of objectives or mandates, and the stringency of limits on the central bank's lending to the public sector. It is worth noting that while Jamaica's scores for 2010 were relatively low when compared to most of the Latin American and Caribbean central banks assessed, the United Kingdom's central bank was also a poor performer relative to others at all levels of development on this index (ranking 79th out of 89 countries assessed).

A more recent study (Garriga 2016) using an index of central bank independence similar in many respects to that discussed in the previous paragraph, and covering an extended set of countries, ranked the BOJ 120th out of 179 countries in 2012 (Figure 12.10).⁷³ It is worth highlighting

⁷¹ "Objective of Monetary Policy and Outlook," Bank of Jamaica. Available at http://boj.org.jm/monetary_policy/monetary_objective.php (accessed on 10 May 2018).

⁷² This ranking is based on the Central Bank Independence Weighted Index (CBIW) for 2010 reported in Dincer and Eichengreen (2014). The CBIW is a weighted average of measures related to the following dimensions: chief executive officer appointment (weight = 0.1), policy formulation (0.15), objectives (weight = 0.15), limitations on lending to the government (weight = 0.50), and board member appointment (0.1). For details on the specific components of these measures, see Table 18 in Dincer and Eichengreen (2014).

⁷³ This ranking is for 2012. Garriga (2016) identified four dimensions concerning the independence of central banks from political influence: who appoints the governor (weight = 0.2); whether there is direct government involvement in policy decisions (0.15); whether there are limits on the ability of the government to borrow from the central bank (0.50); and whether price stability is a core objective of monetary policy (0.15). The weighted average of these dimensions results in a central bank independence index ranging from 0 (lowest independence) to 1 (highest independence).

Table 12.5 Central Bank Independence Ranking

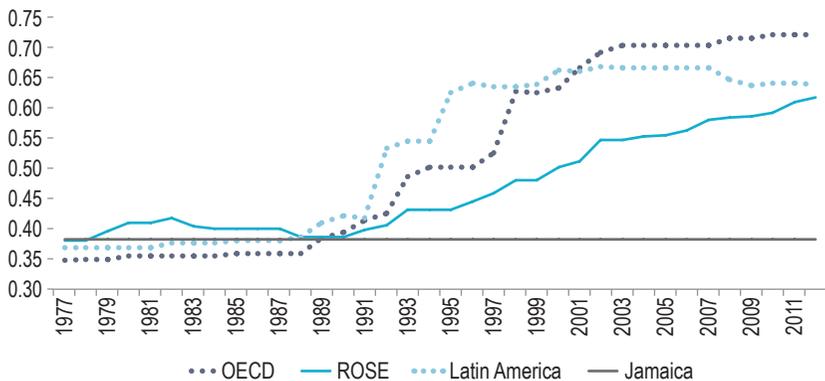
Rank Out of 89 Countries Worldwide	Country	Central Bank Independence Index
16	Chile	0.69
19	El Salvador	0.67
26	Mexico	0.63
32	Peru	0.56
32	Argentina	0.56
42	Guyana	0.50
69	Colombia	0.29
71	Cuba	0.27
73	The Bahamas	0.26
75	Belize	0.25
75	Trinidad and Tobago	0.25
79	United Kingdom	0.23
80	Jamaica	0.22
84	Barbados	0.17

Source: Dincer and Eichengreen (2014).

Notes: The figure represents the Central Bank Independence Weighted Index for 2010 reported in Dincer and Eichengreen (2014). This measure ranges from 0 (lowest independence) to 1 (highest independence). The United Kingdom is included for comparison purposes, while all other countries presented are from Latin America and the Caribbean.

that the BOJ’s performance on this measure of independence was similar to that displayed by other central banks in Latin America, ROSE, and the OECD when comparable data were first available in the late 1970s through to the late 1980s. However, these other groups have, on average, seen

Figure 12.10 Jamaica: Central Bank Independence Index



Source: Garriga (2016).

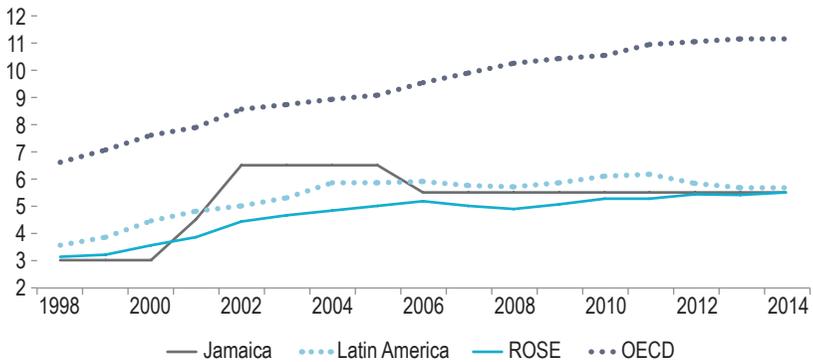
Note: The Central Bank Independence Index ranges from 0 (lowest independence) to 1 (highest independence).

significant improvements on this measure of independence since the early 1990s, while the BOJ's performance remained stagnant through to the latest data point in 2012. This rapid improvement among OECD and many other central banks is driven in part by the evolution of monetary and exchange rate policy regimes since the early 1990s, when advanced-economy central banks began formally adopting inflation-targeting frameworks. The first two countries to adopt such regimes were New Zealand in 1989 and Canada in 1991. By 2016, the IMF classified 38 central banks as having fully implemented inflation-targeting frameworks (IMF 2016).

Looking forward, it is expected that governance improvements of the BOJ will continue to take place, in line with the shift to inflation targeting. In particular, authorities have acknowledged that for the new regime to succeed, the potential for central government objectives to run counter to price stability (e.g., unwarranted central bank financing of the government, exchange rate objectives, etc.) must be diminished, including via updates to legislation. In this context, the government and the BOJ are in the process of updating the *Bank of Jamaica Act* to formalize price stability as the central mandate, and to improve the BOJ's governance and accountability structure, in line with international best practices for inflation targeting central banks. The envisioned reforms will also modernize arrangements for paying dividends to the government, appointing members of the BOJ board, and providing for central bank financing of the government (IMF 2018). It is likely that these and related legislative, operational, and organizational reforms would, once completed, result in improved performance and scores on measures of governance and independence in the near future.

Regarding transparency, since comparable data were first available in the late 1990s the BOJ has been assessed as performing in line with central banks in Latin America and the ROSE group of countries, but well below scores for OECD central banks on average (Figure 12.11). For example, the BOJ's score on the Dincer and Eichengreen (2014) Transparency Index was 5.5 in 2014 (within a range of 0 to 15), significantly below the average of 11.2 for OECD countries.⁷⁴

⁷⁴ The Central Bank Transparency Index measures compliance with 15 best practices distributed across the following areas: political transparency (three practices), economic transparency (three practices), procedural transparency (three practices), policy transparency (three practices), and operational transparency (three practices). The Transparency Index ranges from 0 (no compliance at all) to 15 (full compliance with the 15 best practices). For details on the specific practices and Index construction, see Appendix 1 in Dincer and Eichengreen (2014).

Figure 12.11 Jamaica: Central Bank Transparency Index

Source: Dincer and Eichengreen (2014) updated database for Central Bank Transparency 1998–2014 (https://eml.berkeley.edu/~eichengr/Dincer-Eichengreen_figures&tables_2014_9-4-15.pdf).

Note: The Transparency index ranges from 0 (lowest transparency) to 15 (highest transparency).

While the BOJ's focus has included exchange rate stability and employment, it has very recently shifted toward a more coherent emphasis on price stability, within the confines of an inflation-targeting framework. In this context, the Ministry of Finance and Public Service approved a continuous medium-term inflation target for the first time in September 2017—initially set at between 4 and 6 percent—as well as the BOJ's first pre-announced calendar of monetary policy decisions (for 12 months, to be updated semi-annually) in February 2018.⁷⁵ These innovations should support lower and less volatile inflation over time, but also ensure that liquid international reserve buffers are stronger and better insulated by less active intervention in foreign exchange markets. These reforms also reflect major strides toward more effective and efficient policymaking and execution by the BOJ.

Looking forward, a fully functioning inflation-targeting framework will support improvements in transparency and related ratings. Operational target ranges and their underpinning metrics will be made explicit and public on a regular basis, as will be discussions regarding interest rate and other policy actions and intentions in the context of achieving these quantitative targets. With these objectives in mind, the BOJ announced in early 2018 its intention to issue statements eight times per year at fixed dates (i.e., fixed action dates), outlining its policy decisions and key factors

⁷⁵ Bank of Jamaica, "Bank of Jamaica's Medium-Term Inflation Target," Press Release, 27 November 2017. Available at http://www.boj.org.jm/uploads/news/press_release_-_medium_term_inflation_target_bw_am_bw_final.pdf.

supporting such decisions.⁷⁶ More generally, this shift toward price stability as the overarching objective of monetary policy will help to improve the BOJ's operational independence, as it shifts from a mixed mandate that includes exchange rate, growth, and employment objectives to one focused primarily on inflation with clear quantitative targets.

In summary, the Bank of Jamaica deserves credit for rapid and successful progress to date on implementation of technical and other reforms required for the shift to inflation targeting—a major accomplishment for an economy at this stage of development. Looking forward, the BOJ should continue to develop technical and operational capacity to support its new policy regime and adhere to its price stability mandate above all other objectives. As has been observed in many other countries that have made similar transitions, flexible exchange rate regimes in the context of inflation-targeting policy frameworks both encourage and necessitate a great deal of clarity and transparency in order to operate effectively. In this context, the BOJ has initiated a program of legislative reform and targeted capacity-building aimed at improving governance and transparency, as well as upgrading data gathering and monitoring, forecasting, decision-making, and communications capacity.

12.4.2. *Fiscal Institutions*

In terms of institutional structure, public financial management and fiscal policy are primarily the responsibility of the Ministry of Finance and Public Service (MFPS), with support in terms of data collection, analysis, and execution from other agencies. Specifically, the MFPS has overall responsibility for developing the government's fiscal and economic policy framework, and for collecting and allocating public revenue. The MFPS's mission statement includes a focus on four key objectives: (1) a stable economy, (2) effectively regulated ministries, departments and agencies, and financial institutions; (3) effectively managed public funds; and, (4) public satisfaction.

As discussed above, years of imprudent and inconsistent financial policies in Jamaica resulted in unsustainable fiscal deficits, overborrowing by

⁷⁶ These and other measures aimed at improving transparency are being guided by the BOJ's implementation of a new forecasting and policy assessment system, which includes a commitment to fixing the dates in the decision-making calendar for the year ahead, and promptly disclosing each decision and its rationale to the public, with the explicit objective of helping to establish and influence the expectations and actions of capital markets and the general public.

public enterprises, successive financial sector crises and bailouts, and a heavy debt burden. After several failed reform efforts between the 1970s and early 2000s, Jamaica signed a four-year Extended Fund Facility (EFF) arrangement with the IMF in May 2013, with the aim of restoring macro-economic and debt sustainability and promoting structural reform. The EFF and its successor precautionary Stand-By Arrangement with the IMF helped to establish realistic objectives for restoring fiscal and external sustainability, aimed at reducing the debt-to-GDP ratio from over 140 percent in FY 2012–2013 to current estimates of below 100 percent by FY 2019–2020 (IMF 2018). The authorities have performed admirably under the program, with both fiscal performance and the recorded reduction in public debt levels exceeding initial expectations.

Two major drivers of this rapid progress toward fiscal discipline and debt reduction have been (1) wide-ranging fiscal reforms to broaden the tax base, and (2) the establishment of a fiscal responsibility framework and related fiscal rules. With respect to revenue reforms, the government was able to eliminate most exemptions and discretionary waivers to the general consumption tax, as well as shift from direct to indirect taxation for personal income taxes, resulting in a more efficient system (IMF 2017).

Regarding fiscal rules, as part of the structural reforms under the EFF program, the Jamaican government enacted legislation to enable the adoption of new fiscal rules in March 2014. Jamaica's fiscal responsibility framework, as articulated in the *Financial Accountability (Amendment) Act* of 2014 and the *Public Bodies Management and Accountability (Amendment) Act* of 2014, includes a balanced budget rule as well as debt rules focused on both debt accumulation and overall debt-level targets. These fiscal rules take into account all fiscal activities associated with the public sector, as well as fiscal implications of public-private partnerships.

The framework's objective is to limit the annual fiscal deficit of the public sector, with the longer-term goal of reducing public debt to 60 percent of GDP by FY 2025–2026. The rule includes an automatic correction mechanism triggered by substantial cumulative deviations from the annual balance target. It also includes an escape clause that can be invoked with parliamentary approval, allowing for suspension of rules for a specified period in the event of major adverse shocks, such as natural disasters, severe economic contractions, public emergencies, or financial crises. The accountant general is in charge of monitoring compliance with the fiscal rule.

Jamaica's strong performance with respect to fiscal prudence and debt reduction since the establishment of fiscal rules points to their

effectiveness.⁷⁷ Looking forward, there remains scope for further enhancing these mechanisms to help ensure long-term fiscal prudence and sustainability. In this context, the emerging consensus regarding optimal fiscal regimes and institutional frameworks suggests that fiscal responsibility frameworks and fiscal rules can be strengthened via the establishment of independent bodies tasked with developing economic and financial forecasts underpinning budgets, as well as with monitoring budgetary implementation (IMF 2013).

Until May 2018, Jamaica's fiscal framework did not include independent bodies either for setting budgetary assumptions or for monitoring implementation of the framework. The advantages of independent bodies include that they are broadly insulated from political influence that can compromise forecast accuracy and budgetary performance. By fostering transparency and promoting accuracy and accountability in fiscal forecasting and policymaking, studies suggest that having independent bodies can raise the reputational and electoral costs of undesirable policies and broken commitments (IMF 2013). Reforms of this type have proven helpful elsewhere for enshrining prudent fiscal objectives and policymaking. This is particularly true for countries that have reduced debt burdens to levels low enough that incentives for continued discipline must be predicated on the need to develop fiscal space and buffers to facilitate future countercyclical policy objectives (Mooney et al. 2017).⁷⁸

Against this backdrop, in May 2018 Jamaica's cabinet of ministers has approved the establishment of an independent fiscal council, as part of measures to strengthen Jamaica's Fiscal Responsibility Framework.⁷⁹ While the final structure and mandate of the council was not finalized at the time of this publication, initial considerations include tasking it, *inter alia*, with monitoring the government's compliance with fiscal rules, as well as keeping the public informed on economic matters according to a scheduled

⁷⁷ While the improved fiscal stance since has been a key driver of debt reduction over this period, it is worth noting that a number of other factors have also influenced debt dynamics, including lower real financing costs for new debt instruments, a return to positive real GDP growth, exchange rate movements affecting external debt, and other non-debt creating flows (e.g., privatization receipts, tax revenues, etc.). For a fuller discussion of these issues, see Mooney and de Soyres (2017).

⁷⁸ Jamaica does not have a sovereign wealth fund. In countries that have established them, such funds have helped provide countercyclical fiscal buffers and resources to ensure inter-generational equity once natural resource endowments are depleted. As Jamaica does not have significant resource endowments, there is not a strong case for the establishment of a sovereign wealth fund.

⁷⁹ See: <https://jis.gov.jm/cabinet-approves-establishment-of-independent-fiscal-council/>.

timetable. The government is committed to developing the fiscal council's full suite of responsibilities in consultation with key stakeholders, including the private and financial sectors, civil society, and members of other political parties.

12.4.3. Ease of Doing Business

Results of the World Bank's 2016 Doing Business Indicators highlight Jamaica's strengths and weaknesses with respect to the ease of establishing and operating a business. Like most emerging and developing economies in the region and across the world, Jamaica falls short of the OECD average for most of the 2016 Ease of Doing Business Indicators, with a notable exception related to the ease of starting a business and getting credit, where it fares better than the average for OECD economies (Figure 12.12).

Figure 12.12 Jamaica: Ease of Doing Business



Source: World Bank, 2016 Doing Business database.

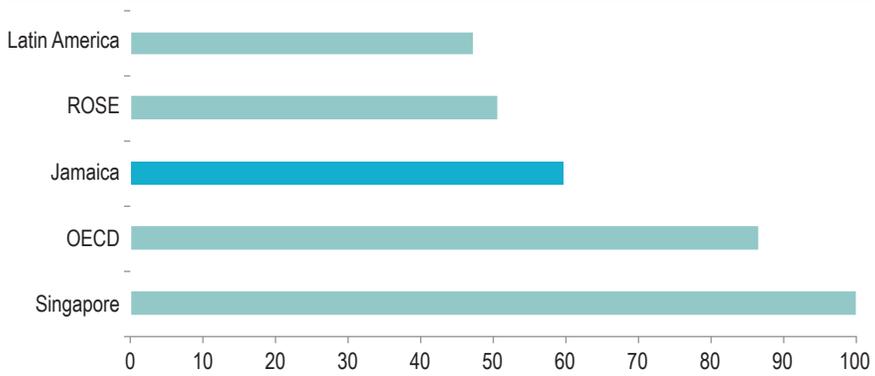
Notes: Each measure was standardized to obtain an index ranging from 0 (worst performance) to 100 (best performance) using the following formula: $(var - min)/(max - min)$, where *var* is the individual country ranking, and the maximum and minimum are the highest and lowest value in the datasets, respectively. The OECD was taken as the best practice benchmark with a value of 100 in each one of the dimensions measured.

On other indicators, particularly those related to access to electricity, registering property, trading across borders, and enforcing contracts, Jamaica falls well below scores registered by advanced economies. Jamaica does, however, display relative strength in areas such as insolvency resolution frameworks, construction permits, and investor protection, where related metrics assess Jamaica as displaying conditions far superior to the average for ROSE and Latin America.

Looking forward, there is considerable scope for improvement on these and related indicators for Jamaica. While some indicators of the business climate relate to variables that can be influenced in the near term via policy actions, others are more structural in nature, and will take time and considerable effort to remedy. Relatively low scores in areas such as taxation, access to electricity, and property registration are being addressed via reform efforts aimed at improving administrative and institutional processes and procedures, and via new investments in the power sector. For example, Phases I and II of the revenue-neutral tax reform program were recently completed with technical assistance and support from the IMF, with the objective of increasing transparency and efficiency by shifting from direct to indirect taxation.⁸⁰ Similarly, a new transfer pricing regime has been rolled out, and an administrative body has been established to administer new Special Economic Zones to encourage foreign investment in export-oriented sectors. Energy supplies should increase with the recent conversion of the Bogue power plant to liquid natural gas fuel (expected to commence operations in March 2019). Other reforms of land titling and property registration practices and procedures are also planned, which could help to address other concerns highlighted in the World Bank's Doing Business survey.

Other weaknesses in terms of the business climate—for example, trading across borders—are less tractable, and relate to broader challenges and/or infrastructure deficits that could take considerably more time and effort to address. Similarly, improvements in the tax environment facing private sector operators in Jamaica are at least in part related to the substantial primary fiscal surpluses that must be maintained to ensure continued debt reduction, as well as the large and rigid public wage bill. In this context, improving perceptions and conditions regarding taxes will require reforms of the public service to address its size and the complex structure of wage subsidies, as well as debt reduction sufficient to provide the government with additional fiscal flexibility for tax reduction.

⁸⁰ See the First and Second Reviews of the current IMF precautionary Stand-By Arrangement for details on these and related reforms. Available from: <http://www.imf.org/en/Countries/JAM>.

Figure 12.13 Jamaica: Regulatory Quality

Source: World Bank, 2017 World Governance Indicators database (www.govindicators.org).

Notes: Percentile ranking score ranging from 0 (worst in regulatory quality) to 100 (best in regulatory quality). Singapore is the best country worldwide in terms of regulatory quality. Regulatory quality captures perceptions of the ability of the government to formulate and implement sound policies and regulations that permit and promote private sector development.

Another key dimension of public institutions relates to regulation. As illustrated in Figure 12.13, Jamaica compares favorably to Latin America and ROSE on the 2017 Regulatory Quality dimension. This indicator reflects the quality of policies and regulations related to permitting and promoting private sector development. This relatively strong performance on related indicators is consistent with the country's performance on indicators of doing business highlighted above, with Jamaica scoring above the OECD average for ease of starting a business, and above Latin American and ROSE averages for dealing with construction permits and insolvency. Looking forward, the Jamaican government could support improvements in related scores by investing in areas that might improve the quality of export goods and make them both more attractive and competitive in foreign markets. One such initiative could be to invest in quality assurance certification processes, such as the laboratories required to certify products for export to North America and Europe.

12.5. Conclusions and Policy Recommendations

Jamaica has enjoyed a stable parliamentary democracy based on the British Westminster political system for over 50 years. While politically motivated violence has occurred, especially during the 1980s, the country has displayed relatively peaceful transitions of power and free and fair elections. Despite this strong democratic tradition, voter apathy is on the rise, as evidenced by low and declining voter turnout. Inherent in

the Westminster system is the concentration of considerable power in the prime minister. This makes it essential that other institutions—such as the judiciary and civil society—operate efficiently and ensure appropriate checks and balances.

Although Jamaica has several strengths in terms of rule of law institutions, it faces many important challenges that are key to unlocking growth. In terms of property rights, re-engineering land registration processes and investing in ICT to enhance the efficiency of those processes will be critical. Human rights require special attention from the government, focusing particularly on the investigation of extra-judicial killings that hinder efforts to improve police-citizen relations. Jamaica's relatively low expenditure on the justice system and high expenditure on law enforcement are leading to ineffectiveness and inefficiencies in the fight against crime. On one hand, despite its independence, the justice system is overburdened and operates in a context of scarce resources. On the other hand, the country has among the highest crime-related police expenditure of any country in Latin America and the Caribbean, as well as a high police density. Adequate allocation of resources that recognizes the critical roles of justice and law enforcement in reducing crime is needed. Investments in ICT for such areas as case and record management systems and training are essential to enhance the efficiency of both justice and law enforcement. The proposed legislative reform for the Jamaica Constabulary Force has the potential to address many of the outlined weaknesses of the force in terms of trust, high attrition, and turnover.

In the social sector, there are significant challenges regarding the quality of public education and health. Although Jamaica introduced an institutionalized performance evaluation system for teachers in 2004, further strengthening of that system is needed to secure its objectivity and impartiality. Teacher performance measures should rely more heavily on objective performance of their students measured through standardized evaluations. Furthermore, while efforts have been made to guarantee quality through licensing of teachers, the legislation has been pending for several years. Also, the very important early childhood education sector remains weakly regulated and is dominated by private sector providers of varying quality. In the health sector, Jamaica faces a serious shortage of health workers, many of whom move to the private sector or abroad for higher salaries and better working conditions. The continuing fiscal consolidation, coupled with free public health, poses a special challenge as Jamaica's expenditure for health continues to be among of the lowest in the region. A redirection of expenditures from less productive areas would be appropriate.

Since embarking on an IMF-supported program in 2013, Jamaica has made tremendous progress toward macroeconomic and fiscal stability, debt reduction, and reform of key economic institutions. This has been supported by impressive innovations to the fiscal framework, including tax reforms and the adoption of fiscal and debt rules and targets. The Bank of Jamaica has recently shifted from a mixed policy mandate to inflation targeting, with clear quantitative objectives. Supportive operational and legislative reforms are also under way to ensure that price stability is enshrined in legislation, and that the BOJ is further insulated from the potential influence of government. Looking forward, authorities should continue to develop fiscal and monetary institutions and capacity to help ensure that the debt reduction achieved under the IMF-backed programs can be sustained. In this context, the institutionalization of fiscal rules and the recently announced plan to create independent fiscal councils would be useful means of improving budget formulation, transparency, and accountability. Similarly, the completion of legislative reforms to modernize the BOJ would support responsible and effective monetary policy formulation and execution, as well as insulate the BOJ from any future fiscal policy-related interference. In all areas, further capacity-building and training of public servants in modern policymaking would be helpful. Most importantly, progress to date must be matched with efforts to transform the structure of the public sector, simplify and reduce the wage bill, and leverage technology to reduce costs and improve efficiency.

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Suriname

Jeetendra Khadan

13.1. Political Institutions

Suriname became an independent nation in 1975,¹ and between 1975 and 1980 the country had a working parliamentary democracy. However, in February 1980 the elected government was overthrown by a military coup d'état. This military dictatorship dominated Suriname until 1991, a period that saw alleged political assassinations in 1982, a ban on political parties in 1985, and a civil war in 1986. In 1987, a new civilian constitution was approved by referendum and a president subsequently elected. However, this was short-lived, as another military coup occurred in 1990. In 1991, a new government was elected under the 1987 constitution, marking a return to civilian rule.

The democratic system currently in place is a presidential system with parliamentary supervision. The legislative branch is the National Assembly, also known as The National Parliament (De Nationale Assemblée - DNA), which is a unicameral legislature and represents the highest organ of the state. The president is the head of state of the Republic of Suriname, head of government, chairman of the Council of State, chairman of the Security Council, and commander-in-chief of the armed forces.

The president and vice-president are not elected directly by the electorate as in most fully presidential systems. After national elections are conducted to elect members of the DNA, the Parliament convenes to elect a president and vice-president for a five-year term. If two-thirds of the members of the DNA fail to elect a president and vice president, then a United People's Assembly is convened where a simple majority vote is

¹ Suriname was colonized by the British in 1652 but ceded to the Netherlands in exchange for New Amsterdam (later called New York City) in 1667 and given full autonomy within the Kingdom of the Netherlands in 1954.

needed to elect the president and vice president. The United People's Assembly consists of all elected officials of the DNA, along with regional and municipal representatives.

13.1.1. *Political Parties and Background*

The organization of political parties in Suriname is heavily influenced by the country's ethnic diversity. The mobilization of political parties, which intensified during the period from 1942 to 1948 and occurred along ethnic lines, was motivated by the promise of full internal self-government in the early 1940s and around the attainment of universal suffrage (Dew 1996). Suriname's colonial past contributed to the country's ethnically diverse society that includes eight ethnic groups: Creoles, Hindustanis, Javanese, Maroons, Amerindians, Chinese, and Europeans.² Suriname's last party-less national election was held in 1946 with 22 candidates competing for 10 elective seats. From these candidates, *Unie Suriname*³ endorsed eight and the remaining were mostly Creole, Jewish, Dutch or Chinese, and one Hindustani. Seven of the eight *Unie Suriname* candidates won their seats. This meant that the *Unie Suriname* maintained influence over the state as the struggle for autonomy continued. Later, the *Staten* (state) accepted a proposal from *Unie Suriname* to send a mission to the Netherlands to seek autonomy and appointed three of its members to take the journey, excluding the Hindustanis and Javanese—a decision that triggered a series of events and eventually culminated in the establishment of Suriname's first political party in 1946, the Muslim Party.

A number of political organizations subsequently emerged representing various ethnic and religious groups. In 1946, the Catholics established the Progressive Surinamese Party (PSV), and the National Party of Suriname (NPS) found its support among the Creoles. In the next year, the Javanese-based Party for National Unity was formed, followed by the Hindustani-based Progressive Reform Party (VHP) in 1949. The VHP and the NPS have remained the two dominant political parties in Suriname. Many other small parties emerged in the post-independence period, most

² Population data available from 1964 show that Creoles (35.4 percent) and Hindustanis (34.7 percent) accounted for approximately 70 percent of the population, with the other ethnic groups accounting for the remainder: Javanese (14.9 percent), Maroons (8.5 percent), Amerindians (2.3 percent), Chinese (1.7 percent), European (1.4 percent), and other or unknowns (1.1 percent).

³ The *Unie Suriname* (Suriname Union) was an organization that embodied the Creoles' effort to counter autocratic methods by the then-governor and the apartheid policies at that time. The members included a number of Creoles, two Hindustanis, a Chinese, and a Javanese (Dew 1996).

of them forming coalitions and alliances to better their chances of getting into Parliament. Indeed, Suriname's electoral organization favors multi-party combinations to form the government. On average, four political parties, often representing different ethnic groups, have constituted the government following the past seven elections. Table 13.1 summarizes information about members of each coalition government, including their ideology, ethnic background, and periods in power.

Table 13.1 Profiles of the Main Political Parties in Suriname

Name of Party	Party Initials	Periods in Power	Ideology	Ethnicity Background
National Party Combination	NPK	1977		
National Party of Suriname	NPS		Undefined*	Creole
Renewed Progressive Party	HPP		Undefined	Undefined
Party for National Unity and Solidarity	KTPI		Undefined	Javanese
Suriname Progressive People's Party	PSV		Christian Democratic	Roman Catholic, Creoles and Mulattos
Front for Democracy and Development	FDO	1987–1991		
National Party of Suriname	NPS		Undefined	Creole
Progressive Reform Party	VHP		Left wing	Indian
Party for National Unity and Solidarity	KTPI		Undefined	Javanese
New Front for Democracy and Development	NF	1991–1996		
National Party of Suriname	NPS		Undefined	Creole
Progressive Reform Party	VHP		Left wing	Indian
Party for National Unity and Solidarity	KTPI		Undefined	Javanese
Surinamese Labour Party	SPA		Social democratic	Non-ethnic
New Front for Democracy and Development	NF	1996–2000		
National Party of Suriname	NPS		Undefined	Creole
Progressive Reform Party	VHP		Left wing	Indian
Party for National Unity and Solidarity	KTPI		Undefined	Javanese
Surinamese Labour Party	SPA		Social democratic	Non-ethnic
New Front for Democracy and Development	NF	2000–2005		
National Party of Suriname	NPS		Undefined	Creole
Progressive Reform Party	VHP		Left wing	Indian
Party for National Unity and Solidarity	KTPI		Undefined	Javanese
Surinamese Labour Party	SPA		Social democratic	Non-ethnic
New Front for Democracy and Development	NF	2005–2010		
National Party of Suriname	NPS		Undefined	Creole
Progressive Reform Party	VHP		Left wing	Indian

(continued on next page)

Table 13.1 Profiles of the Main Political Parties in Suriname (continued)

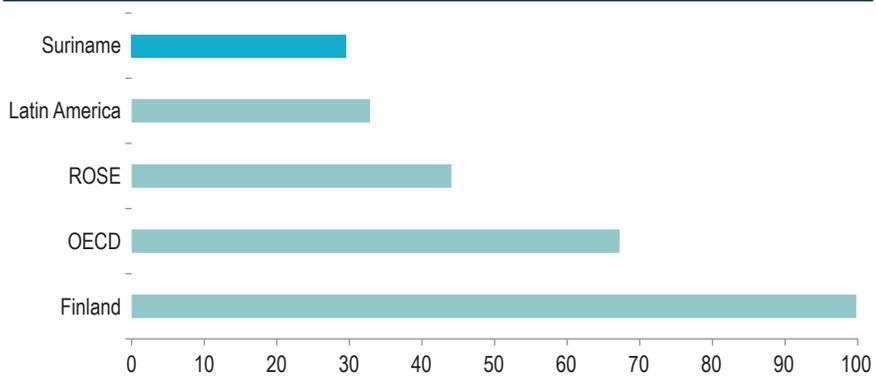
Name of Party	Party Initials	Periods in Power	Ideology	Ethnicity Background
Democratic Alternative '91	DA'91		Liberal	Non-ethnic
Surinamese Labour Party	SPA		Social democratic	Non-ethnic
Mega Combination	MC	2010–2015		
The National Democratic Party	NDP		Social democracy (Left-wing)	Creole
The Progressive Workers' and Farmers' Union	PALU		Socialism (Radical left)	Non-ethnic
New Suriname	NS		Undefined	Indian
Party for National Unity and Solidarity	KTPI		Undefined	Javanese
National Democratic Party; Party for Democracy and Development in Unity; Brotherhood and Unity in Politics**	NDP/ BEP/ DOE	2015–2020		
National Democratic Party	NDP		Social democracy (Left-wing)	Creole
Party for Democracy and Development in Unity	DOE		Reformism	Non-ethnic
Brotherhood and Unity in Politics	BEP		Unknown	Maroon

Sources: Bissessar (2017); Caribbean elections (2017); Stöver (2005); and Tjon Sie Fat (2009).

Notes: *Undefined is used to classify political parties without a distinctive ideology and or ethnic background. **The 2015 general election was historic for Suriname as it was the first time a single political party, the NDP, won the majority of seats in the National Parliament. However, the NDP went on to form a coalition government with the Brotherhood and Unity in Politics (BEP) and the DOE parties. The NDP obtained 26 seats, while the BEP and DOE obtained 2 and 1 seat(s), respectively.

The dominance of ethnic-based politics in Suriname raises important questions about the quality of governance and decisions related to the design and execution of public policy. The literature covered in other chapters of this book suggests that ethnic-based voting can lead to lower-quality politicians, facilitate the extraction of rents by political leaders, and promote policies that could disproportionately benefit special interest groups. Indeed, Figure 13.1 shows that Suriname performs lower on the Public-Regardedness Index compared to other countries, which is an indication that special interest groups in the society may have a strong influence on the direction of public policies.⁴

⁴ As explained in Chapter 6 of this volume, the Public-Regardedness Index was proposed in Berkman et al. (2008). The authors computed this index using expert evaluations and perceptions on issues related to (1) corruption, (2) public spending on social transfers, and (3) whether government contracts are awarded fairly or generally favor well-connected firms and individuals. The index is the combination of these three measures. The first component was taken from Transparency International Corruption's Perceptions Index, and the last two components from the Global Competitiveness Report.

Figure 13.1 Suriname: Public-Regardedness Index

Source: Author's calculations using the database in Berkman et al. (2008).

Notes: Each measure was standardized to obtain an index ranging between 0 (worst performance) and 100 (best performance) using the following formula: $(var - min)/(max - min)$, where *var* is the individual country measure, and the maximum and minimum are the highest and lowest value in the datasets, respectively. Finland is the country with the highest Public-Regardedness Index ranking worldwide. OECD: Organisation for Economic Co-operation and Development; ROSE: rest of the small economies of the world.

The next section turns to analyzing the extent to which relevant rules and institutions in place have guaranteed democratic participation and transparency in electoral processes.

13.1.2. *Political Representation, Competition, and Transparency in the Political System*

In a small and ethnically diverse country such as Suriname, where voting appears to occur largely along ethnic and religious lines, effective participation of different groups in the political process, the openness of the electorate to new political leaders, and transparency and confidence in the electoral process are important for an effective democracy. These issues are examined in this section.

Suriname has many political parties representing distinct groups in society: 25 political parties contested the 2015 national elections. However, there are few large parties, and many smaller parties that emerge prior to elections to form alliances with other political organizations to increase their chances of getting into government. Generally, if the smaller political parties are unsuccessful at the polls they tend to dissolve thereafter but may redefine themselves and return at the next national election.

The large political parties generally have constitutions that govern their operations. Internal party elections are held (usually every five years) to elect a chairperson and members of an executive team to conduct the

affairs of the political party. The party's chairperson is elected indirectly by the party membership. In principle, candidates contesting seats in the DNA are screened and selected by their party leadership. In selecting a candidate, it is reported that significant weight is attached to the individual's ethnicity and religion and social standing in the community, rather than ideological differences. Once elected into office, however, political parties have limited power to exert control over their members, especially in smaller parties. There has been a relatively low turnover of power over the past 27 years—three different presidents from two political parties—suggesting that openness to new leadership is relatively low.

Transparency of and participation in the election process are important aspects of any democracy. In terms of transparency of the election process, the Independent Electoral Council of Suriname has the responsibility for supervising the country's national elections and declaring the election results legally binding. It is comprised of at least seven members and three substitute members who are all appointed by the president. The council is not completely independent of the executive, as the president is authorized to dismiss any member of the council, including the secretary, or reappoint members after their term has expired. Elections in Suriname are often observed by international organizations such as the Organization of American States (OAS) and the Caribbean Community (CARICOM). The OAS has deployed Electoral Observation Missions for all national elections in Suriname since 1987. The missions have concentrated efforts on observing a broad range of issues, including structural elements like electoral organization and technology, definitions of boundaries, gender equality, political financing, and the electoral dispute resolution system. The level of public participation in the elections is relatively high: voter turnout was estimated to be 73 percent in the 2015 national election.

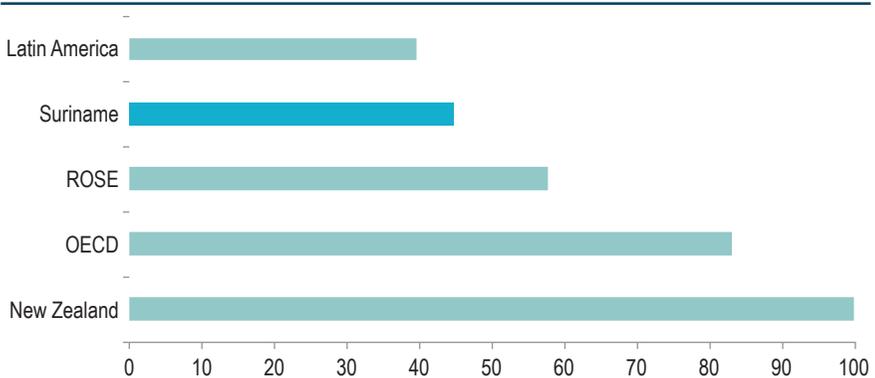
For the 2015 elections, the OAS mission concluded that there is an already strong election process in Suriname, but provided some recommendations related to apportionment of the average number of people represented in each electoral district, electoral organization, transmission and processing of results, campaign financing, participation of women, and legal remedies for settling disputes (OAS 2015). Civil society does not actively engage in election monitoring. It is important to note that in the last election there were no reports of political violence. In fact, even though political parties are permitted to campaign on election day at polling centers, the OAS (2015) noted that these activities were conducted in an environment of congeniality and celebration.

Although legislators who provide scrutiny over proposed laws and executive policies are elected freely, there is a strong perception that

public power is exercised for private gain, as reflected in Suriname's ranking on control of corruption in Figure 13.2. Indeed, Freedom House (2016) noted that more effective enforcement of anticorruption laws could help reduce the perception of corruption in Suriname. Some of the major lapses in checks and balances as noted by Freedom House relate to the lack of laws or inadequate enforcement of laws that should require government officials to disclose information on their finances, and the need for mechanisms that can provide the public with greater access to information on government decisions.

In summary, Suriname's political system shows both strengths and weaknesses. In terms of strengths, Suriname's political system encourages collaboration and alliances among various ethnically based parties, which contributes to a uniquely complex political balance. Within this system, consensus-building has become one of the salient features of the government's decision-making process. While that approach provides some clear advantages, it usually comes at a cost of a protracted pace of decision-making. Moreover, while the electoral process is considered to be strong and transition of power has been generally smooth over the last seven national elections, there are some notable areas for improvement. Internal party democracy could be improved. As it stands, the process seems to place a heavy emphasis on demographic attributes of potential candidates for the DNA rather than their technical prowess. While the political system promotes plurality within the multi-party system, the representation of some ethnic minorities remains low. There is also a need to strengthen institutions that can provide

Figure 13.2 Suriname: Control of Corruption



Source: World Bank, 2017 World Governance Indicators database (www.govindicators.org).

Notes: Percentile ranking score ranging from 0 (worst in controlling corruption) to 100 (best in controlling corruption). Control of corruption captures perceptions of the extent to which public power is exercised for private gain, including both petty and grand forms of corruption, as well as "capture" of the state by elites and private interests. New Zealand is the best country worldwide in terms of controlling corruption.

greater scrutiny of campaign financing, which could help to improve transparency and accountability, and lower the perception of corruption.

Within this context and considering the relatively high concentration of power possessed by the executive branch, it is relevant to assess (1) the mechanisms under which the National Assembly could exert constraints and accountability over the executive or de jure institutions; and (2) to what extent such de jure mechanisms are practically exercised into de facto institutions. These issues are examined in the next section.

13.1.3. *Constraints on the Executive and Accountability*

Notwithstanding some mechanisms that enable legislative oversight of the executive, the constitution gives the president considerable powers and lacks clarity on some critical constitutional issues. The executive is headed by the President of Suriname, who appoints the Council of Ministers and the Council of State after consultations with political parties that are represented in the National Assembly.

There are no clear and effective mechanisms for the electorate to recall members of Parliament or remove members of the cabinet who are not performing. The responsibility for appointing and removing ministers is at the discretion of the president. The constitution also lacks clarity on the removal of the president. While the constitution makes clear the procedures and requirements to be followed by the National Assembly when electing a president and vice president, it does not say anything about the procedures to remove these two officeholders. The lack of clarity on this critical issue led to a constitutional crisis in 1999, when the National Assembly sought to remove the president and vice president by a simple majority vote. There is also no impartial authority to adjudicate on constitutional issues as the country has not yet established a Constitutional Court, as required by the 1987 constitution.

Nevertheless, the legislature scrutinizes and debates the laws and policies of the executive. Legislative oversight of the executive takes two main forms. In the first instance, the president is required by the constitution to address the National Assembly on government policies each year. Secondly, the government must provide information to the National Assembly either in writing or orally when requested. More substantially, the legislature can pass, amend, and reject bills proposed by the executive. A simple majority of votes in the National Assembly is required to take decisions, while constitutional amendments and other special provisions as specified in the constitution require a two-thirds majority vote. A motion is considered defeated if it receives a tie vote by all members in attendance. In the

event that all members are not present, the motion is postponed to a subsequent sitting and if a tie vote arises again, then the motion is considered to be defeated. Bills passed by the DNA and approved by the president are to be enforced after proclamation.

In summary, while *de jure* political constraints on the executive and accountability mechanisms exist to some extent, the *de facto* exercise of those mechanisms by the National Assembly is limited. The next section reviews the state of institutions related to the rule of law.

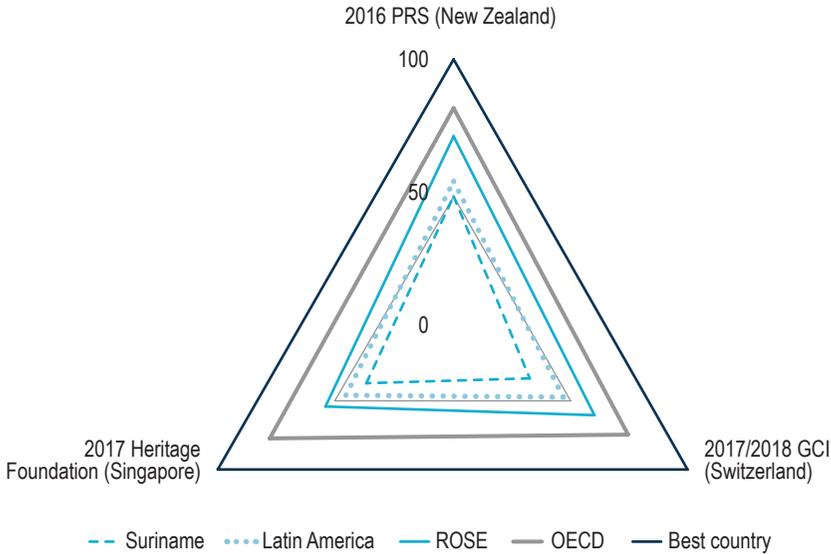
13.2. Rule of Law Institutions

As shown in Chapter 4, the literature suggests two key institutional rule of law components that show a significant causal relation with economic growth. The first relates to the strength of property rights to protect private agents from the risk of having their property expropriated by either government or powerful elites. The second relates to the possibility of obtaining fair and independent administration of justice with the strength to enforce the law without external pressures. This section assesses the condition of these institutions in Suriname.

13.2.1. *Strength of Property Rights*

The protection of property rights in Suriname could be improved. Suriname has an Intellectual Property Office (IPO) but it is not fully functioning. While Suriname is a member of the World Trade Organization and the World Intellectual Property Organization, it has not ratified the Trade-Related Aspects of Intellectual Property Rights Agreement. In a report on Suriname's investment climate, the U.S State Department (2015) noted that intellectual property rights protections are not enforced in the country. Moreover, while the legal framework acknowledges the protection of copyrights, trademarks and patents, the legislation and laws remain dated. In March 2015, amendments to the Music Copyright Law of 1913 were made, but enforcement is non-existent (U.S. State Department 2015). According to the Ministry of Trade, Industry and Tourism, the IPO only registers trademarks. The registration of patents and copyrights is done abroad due to inadequate legislation, and no protection exists for trade secrets and design layout (U.S. State Department 2015).

The relatively weak institutional arrangements described above are reflected in Suriname's performance in several international comparisons. As shown in Figure 13.3, Suriname was ranked low on the 2016 Index of Protection against Expropriation calculated by Political Risk Services,

Figure 13.3 Suriname: Strength of Property Rights

Sources: 2016 Political Risk Services (PRS) database (www.prsgroup.com); World Economic Forum, 2017/2018 Global Competitiveness Index database; and 2017 Heritage Foundation Index of Freedom (www.heritage.org).

Note: Each measure was standardized to obtain an index ranging between 0 (worst performance) and 100 (best performance) using the following formula: $(var - min)/(max - min)$, where *var* is the individual country measure, and the maximum and minimum are the highest and lowest value in the datasets, respectively.

which objectively assesses this institutional dimension across 140 countries worldwide. Similarly, the Property Rights Index measured by the World Economic Forum's 2017/2018 Global Competitiveness Index suggests that Suriname underperforms all comparators (Figure 13.3). Finally, the figure shows that, according to the Heritage Foundation Index of Freedom for 2017, Suriname underperforms every international benchmark on the subcomponent for protection of property rights.

Besides property rights, a relevant dimension for social development and cohesion relates to the respect for and protection of fundamental human rights, issues that are assessed in the next section.

13.2.2. Protection of Fundamental Human Rights

Suriname's constitution guarantees basic human rights and freedoms such as freedom of speech, a free press, and no discrimination on the basis of gender, ethnic background, language, religion, education, political opinion, economic position, or any other status. The authorities have generally honored these

fundamental rights and freedoms. However, the U.S. State Department’s *Human Rights Report* for 2016 identified some important human rights issues in Suriname. The most serious relates to the unresolved trial of a government official and a few co-defendants in relation to crimes committed in 1982. The report also identified other human rights problems such as “poor conditions in detention centers; self-censorship by media organizations and journalists; widespread government corruption; violence and abuse against women and children; trafficking in persons; continued lack of recognition of land rights for indigenous and tribal peoples; discrimination against lesbian, gay, bisexual, transgender, and intersex persons and other minorities; and child labor in the informal sector” (U.S. State Department 2016, 1).

The above-mentioned issues are reflected in Suriname’s low score on the World Justice Project’s Protection of Fundamental Human Rights Index. Indeed, Suriname underperforms on the overall score for fundamental rights with respect to all comparators (Table 13.2). The area where Suriname recorded the lowest score was in freedom from arbitrary interference where privacy is effectively guaranteed (0.26), compared to a score of 0.52 for Latin America, 0.51 for the rest of the small economies of the world (ROSE), and 0.77 for the OECD. In addition, Suriname underperformed relative to all comparators in the area of effective guarantees of the right to life and security of the person, freedom of belief and religion, and fundamental labor rights. Of note, Suriname scored higher than Latin America and ROSE in one area, freedom of opinion and expression.

Table 13.2 Protection of Fundamental Rights in Suriname

Fundamental Rights	Suriname	Latin America	ROSE	OECD
Overall Fundamental Rights	0.53	0.58	0.62	0.76
4.1 Equal treatment and absence of discrimination	0.52	0.51	0.62	0.70
4.2 The right to life and security of the person is effectively guaranteed	0.50	0.61	0.67	0.86
4.3 Due process of law and rights of the accused	0.49	0.46	0.56	0.73
4.4 Freedom of opinion and expression is effectively guaranteed	0.68	0.61	0.59	0.74
4.5 Freedom of belief and religion is effectively guaranteed	0.63	0.75	0.71	0.76
4.6 Freedom from arbitrary interference with privacy is effectively guaranteed	0.26	0.52	0.51	0.77
4.7 Freedom of assembly and association is effectively guaranteed	0.70	0.66	0.71	0.79
4.8 Fundamental labor rights are effectively guaranteed	0.50	0.56	0.60	0.71

Source: World Justice Project (WJP) (<https://worldjusticeproject.org/our-work/wjp-rule-law-index/wjp-rule-law-index-2016/factors-rule-law>).

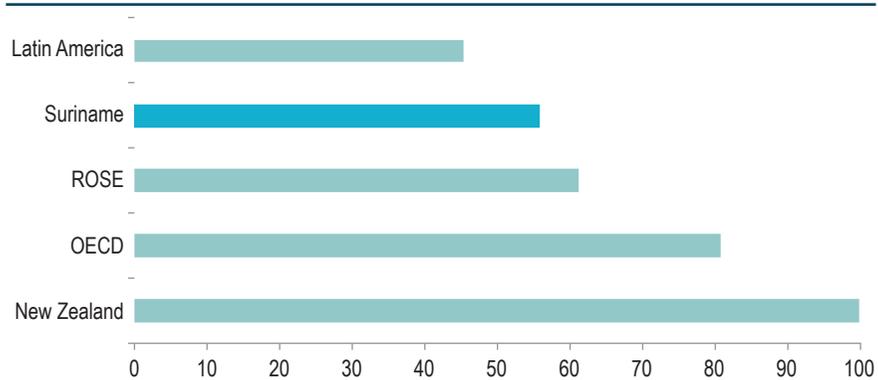
Note: Scores for the WJP Rule of Law Index, as well as for its component factors and subfactors, range from 0 to 1, where scores closer to 1 indicate better performance.

13.2.3. Judicial Independence and Effectiveness

The constitution provides for an independent judiciary. The judiciary, which is responsible for adjudication and prosecution, falls organizationally under the Ministry of Justice and Police, an executive agency. Members of the judiciary are appointed by the government based on the advice of Suriname's highest court. The president, vice president, and judges are appointed for life (up to 65 years of age). The constitution also provides the conditions under which members of the judiciary can be discharged. Candidates who are eligible to become a judge should possess a Master of Law and undergo the Trainee Judicial Officer Program (known by its Dutch abbreviation, RAIO), or possess a Master of Law, at least 15 years of legal experience, and undergo the Trainee Judge Program (known by its Dutch abbreviation, RIO).

Despite a constitutional guarantee for a politically independent judiciary and mechanisms to facilitate such an institutional setup, there is a relatively low perception that Suriname's judiciary is independent and not subject to government interference (Figure 13.4). Perhaps, as noted by Freedom House (2016) recent events related to the approval of an amnesty law that contravenes international law and effectively allows for a government official to evade trial for alleged gross human rights violations could be contributing to these perceptions. Moreover, the amnesty law, which was approved in Parliament in 2012 was subsequently challenged but requires a Constitutional Court for it to be reviewed. However, according to Freedom House (2016) the legislature has not yet established

Figure 13.4 Suriname: Judicial Independence Index



Source: Author's calculations using the database in Berkman et al. (2008).

Notes: Each measure was standardized to obtain an index ranging between 0 (worst performance) and 100 (best performance) using the following formula: $(var - min)/(max - min)$, where *var* is the individual country measure, and the maximum and minimum are the highest and lowest value in the datasets, respectively. New Zealand is the country with the highest Judicial Independence Index score worldwide.

the court and is therefore seen to be effectively blocking an important trial. Another event, which occurred in 1998, was when the government appointed a president of the Court of Justice and a prosecutor general without conducting due consultation with the judiciary. This challenged the independence of the judiciary, as the constitution clearly states that judges “shall be appointed by the government, after consultation with the Court of Justice.” The issue at that time stemmed from the lack of clarity on the definition and procedures for such “consultation.” Apart from these issues, there appears to be strong support and consensus in Suriname for promoting an independent judiciary and the separation of powers.

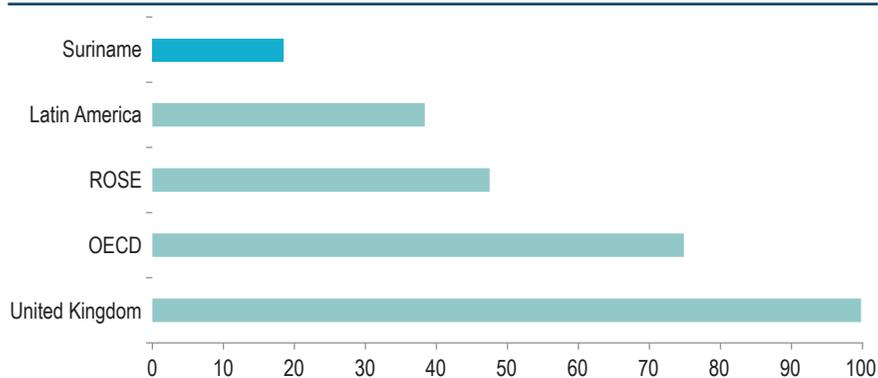
The judiciary lacks budgetary independence. Both the judiciary’s budget allocation and the administration of the budget are determined by the executive. In practice, the judiciary must make requests to the Ministry of Justice and Police (MOJP) for goods, services, and personnel, including allowances to travel to courthouses in the interior (IDB 2001). The MOJP then undertakes these transactions on behalf of the judiciary. Moreover, budget allocation to the judiciary is not linked to objective indicators such as the number of cases it must process. In fact, the budget is drawn up based on the cost experience of the previous year. Nevertheless, judges in Suriname are provided with protection/security from the Suriname Security and Assistance Service, which falls under the MOJP. There is no evidence of missing or delayed payments to judges in Suriname or widespread complaints of low salaries.

However, a shortage of judges, a lack of professional court managers and case management systems, and inadequate physical space have been highlighted as factors contributing to a backlog of cases and lengthy pre-trial detention (U.S. State Department 2016). These shortcomings can potentially affect the ability of the judiciary to deliver timely justice. As shown in Figure 13.5, Suriname significantly underperforms comparators on the Judicial Effectiveness Index, with an index value of 18 compared to the best performers’ score of 100. In fact, it is estimated that half of the prison population is made up of pre-trial detainees.⁵ The U.S. State Department (2016) noted that prisoners who appealed their cases sometimes serve their full sentences before the appeals process is completed.

13.2.4. Law Enforcement

The executive has considerable influence in selecting and supervising the chief of police, who is appointed by the President of Suriname and

⁵ See Institute for Criminal Policy Research (ICPR), “Suriname: World Prison Brief” (<http://www.prisonstudies.org/country/suriname>).

Figure 13.5 Suriname: Judicial Effectiveness Index

Source: Author's calculations using the 2017 Heritage Foundation Index of Freedom (www.heritage.org) database.

Notes: Each measure was standardized to obtain an index ranging between 0 (worst performance) and 100 (best performance) using the following formula: $(var - min)/(max - min)$, where *var* is the individual country measure, and the maximum and minimum are the highest and lowest value in the datasets, respectively. The United Kingdom is the country with the highest Judicial Effectiveness Index score worldwide.

supervised by the Minister of Justice and Police.⁶ There are three major law enforcement and security bodies in Suriname: (1) Korps Politie Suriname (KPS), (2) Military Police, and (3) Surinamese Bureau of National Security (OSAC 2014). The KPS is responsible for all policing efforts and includes two branches: the metropolitan police, which provide general police services, and the judicial police, which provide specialist police services (such as a Narcotics Department, Fraud Department, and Financial Investigation Unit for money laundering). The Military Police has responsibility for border control and immigration functions. The Surinamese Bureau of National Security is responsible for the Central Intelligence and Security Service, as well as the Presidential Personal Security Unit (OSAC 2014). The KPS budget is determined through the budgetary process as it falls under the MOJP. The budget allocation is determined based on discussion between the MOJP and the Ministry of Finance and is not necessarily linked to performance indicators.

Prospective police officers undergo rigorous screening and testing. Suriname's Police Training Academy is responsible for training new recruits. Prospective police officers are subject to a series of background checks and tests. Prospective candidates then undergo one year of basic police training, which includes exposure to both theory and practice.

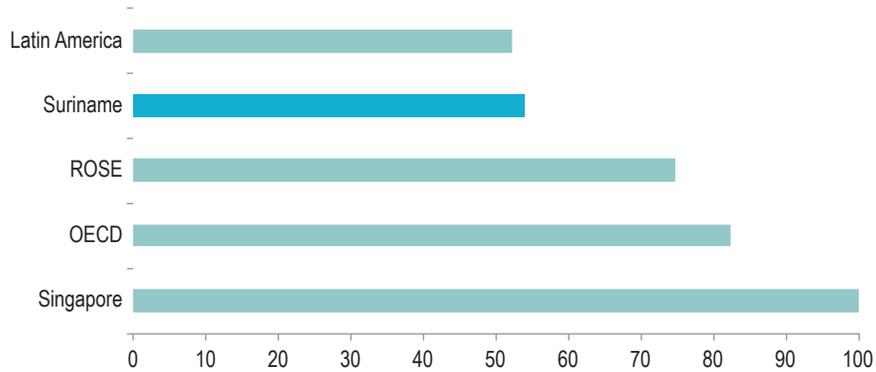
⁶ See the National Assembly document available at <http://www.dna.sr/wetgeving/surinaamse-wetten/geldende-teksten-tm-2005/politiehandvest/>.

Graduates from the Police Training Academy are then placed into various departments (such as traffic or narcotics) for a period of one year during which they are closely supervised, and their performance evaluated.

The Department of Criminal Information (DCIV) collects and analyses data on several types of crimes on a daily basis. Information on the main categories of crime is published regularly. The main categories are theft, qualified theft, burglary, robbery, armed robbery, domestic violence, and murder. Crimes concerning collision of two or more vehicles, accidents due to loss of control of vehicles, and other traffic-related crimes are published by the traffic police. The DCIV keeps a database for all the types of crimes and this information is used to inform policing activities such as the identification of crime hot spots and to design strategies and operations to detect and decrease criminal activities. Moreover, the information produced by the DCIV is used to help the KPS prepare budget requests and allocate resources among the different police districts.

There is a high level of trust in the national police. According to the 2014 Latin American Public Opinion (LAPOP) Survey, about 63 percent of the respondents indicated high levels of trust in the police, and 80 percent of respondents indicated that police harassment is not a problem in their neighborhood. These perceptions are supported by a relatively low number of complaints of police abuse against citizens. Indeed, Suriname has several institutions to keep a check on police behavior. These include the Personnel Investigation Department (OPZ) which is responsible for investigating complaints by citizens against members of the police force. Additionally, internal cases of misconduct by members of the police are investigated by the Internal Affairs Unit (ITZ), while the Military Police and the Judge Advocate investigate offences committed by the military (U.S. State Department 2016). A Central Inspection Section (CIO) investigates misuse of KPS assets. In the first nine months of 2016, there were 94 complaints from private citizens against members of the police force, which represents a decline from 140 complaints recorded for a similar period in 2014 (U.S. State Department 2014). With respect to internal cases handled by the ITZ, there were 238 investigated cases of misconduct for the same period in 2016, with disciplinary sanctions taken in 223 cases, including 15 terminations.

Crime levels in Suriname are among the lowest in Latin American and the Caribbean. One of the most serious forms of crime, intentional homicides, is 10.7 per 100,000 population compared to 22.3 in Latin America and the Caribbean. Nevertheless, while Suriname ranks better than Latin America on the World Justice Project's Order and Security Index, the country underperforms with respect to other country groups such as

Figure 13.6 Suriname: Order and Security Index

Source: Author's calculations using the 2016 World Justice Project database.

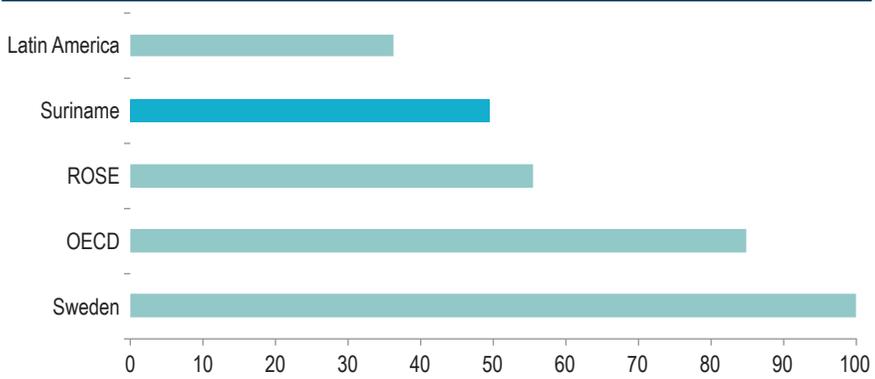
Notes: Each measure was standardized to obtain an index ranging between 0 (worst performance) and 100 (best performance) using the following formula: $(var - min)/(max - min)$, where *var* is the individual country measure, and the maximum and minimum are the highest and lowest value in the datasets, respectively. Singapore is the country with the highest Order and Security Index score worldwide.

ROSE and the OECD (Figure 13.6). The Order and Security Index takes into account crime, political violence, and vigilante justice. Perhaps this relatively lower ranking is attributable to recent increases in various types of crimes. Indeed, from 2008 to 2016, there has been a 141 percent increase in the number of reported cases of qualified theft, a 78 percent increase in homicides, and an 11 percent increase in theft, according to the MOJP.

Overall, this section has evidenced that there is room for improvement in institutions related to the rule of law in Suriname. The strength of property rights, contract enforcement, and judicial independence underperform other country groups. Such a situation can potentially erode the confidence of economic agents in the rules of society, thereby hindering the ability to spur investment and growth. Indeed, as shown in Figure 13.7, the 2016 Rule of Law dimension calculated within the World Bank's World Governance Indicators shows that while Suriname performs better than Latin America, there is more work to be done to reach the performance levels of ROSE and the OECD. In this regard, strengthening institutions related to the rule of law should rank high on the policymakers' agenda.

13.3. Institutions for Human Capital Development

Human capital is arguably one of the most important ingredients for countries to achieve sustainable economic growth. Many studies have shown that the educational attainment and health status of a country's workforce and by extension its population are important pillars for developing a strong human

Figure 13.7 Suriname: Rule of Law

Source: World Bank, 2017 World Governance Indicators Database (www.govindicators.org).

Notes: Percentile ranking score ranging from 0 (worst in rule of law) to 100 (best in rule of law). Rule of law captures perceptions of the extent to which agents have confidence in and abide by the rules of society, and in particular the quality of contract enforcement, property rights, the police, and the courts, as well as the likelihood of crime and violence. Sweden is the best country worldwide in terms of the rule of law.

capital stock that can improve productivity growth and development. The institutional mechanisms to support the development of Suriname's human capital as it relates to education and health are examined in this section.

13.3.1. Education

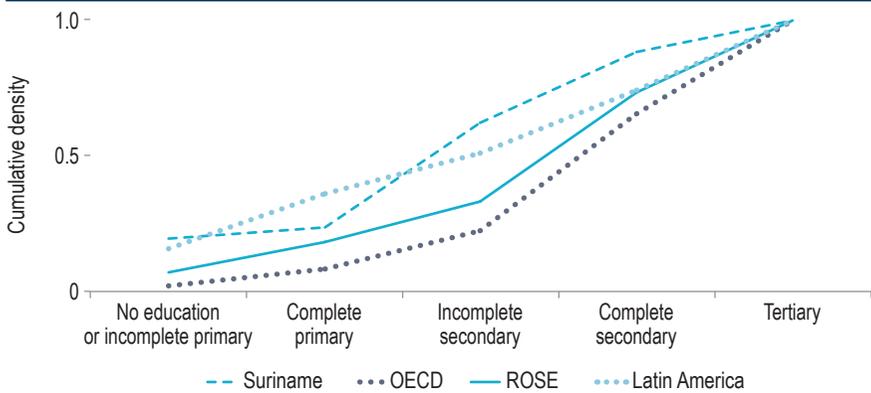
The literature and empirical evidence presented in earlier chapters of this book suggest that educational quality matters for development outcomes. In the school system, the quality of educational output is largely linked to the quality of teachers, among other factors. This section focuses on the ability of educational institutions in Suriname to adequately provide high-quality educational coverage and on the current state of institutions and mechanisms in place to ensure appropriate teacher quality.

The education system in Suriname has changed very little from the pre-independence Dutch system. The school system consists of four levels: pre-primary, primary, junior secondary, and senior secondary. Successful completion of the primary school test allows students to enter junior secondary education and defines their placement. Secondary education is divided into two phases: junior secondary education for three to four years, and senior secondary education for two to three years. Tertiary education is provided by Anton de Kom University of Suriname (ADEKUS) and a number of higher professional education institutes.

In terms of access, Suriname has made good progress and has come closer to achieving the Millennium Development Goal of universal primary education. Suriname performs better than Latin America, ROSE, and the OECD in net pre-primary enrolment rates but underperforms at higher levels of education. Net primary enrolment is high at roughly 91 percent for both males and females, but comparatively lower than the average for Latin America, ROSE, and the OECD. Gross enrolment rates for secondary school are lower for males (females: 89 percent; male: 68 percent) and lower for both genders when compared with other country groups: Latin America (females: 93.2 percent; male: 88.5 percent); ROSE (females: 91 percent; male: 89 percent); and the OECD (females: 114 percent; male: 112 percent). Gross tertiary enrolment data are not available for Suriname. However, information from the 2016/2017 Suriname Survey of Living Conditions shows that the country has the second lowest share of population with tertiary education (12 percent of individuals between 25 and 65 years old) across the Caribbean group. It is also estimated that through emigration, Suriname has lost from 48 to 78 percent of the stock of secondary- and tertiary-educated citizens, respectively (Mishra 2006).

There are some challenges with respect to school dropouts. At the primary and secondary education levels, dropout rates are higher for males in Suriname and higher for both genders when compared to most comparators. The primary and secondary school dropout rate for males is 34.6 percent compared to 15.5 percent for females in Suriname. Male dropout rates are higher than those for Latin America (23.5 percent), ROSE (15.9 percent), and the OECD (3.9 percent). Female dropout rates are higher than the average for ROSE (13.2 percent) and the OECD (3.6 percent), but lower than Latin America (22.4 percent). A combination of a lack of motivation and limited family resources are the main reasons given for the high dropout rates (PADF 2013). A survey of 119 youths revealed that work-related responsibilities (14 percent), no motivation (12 percent), and pregnancy (10 percent) were among the main reasons for dropping out of school (PADF 2013). Despite the relatively higher dropout rates, Suriname's adult literacy rate is high at 95.6 percent and better than the average for Latin America and ROSE, but lower than the OECD. However, as Figure 13.8 shows, only 38 percent of Suriname's population over the age of 25 has completed at least a secondary education, significantly lower than the averages for Latin America (49 percent), ROSE (67 percent), and the OECD (78 percent).

Two important institutional features that are required for incentivizing better teaching quality and educational outcomes, as highlighted in Chapter 4, are monitoring teachers' effort and quality, and performance-based

Figure 13.8 Suriname: Educational Attainment

Source: Author's calculations using the 2016/2017 Suriname Survey of Living Conditions and the World Bank's 2016 World Development Indicators database.

Note: Educational attainment is measured among working-age adults (25–65 years old) who have completed their formal education.

hiring and retention decisions. These two aspects of Suriname's education system are examined below.

Suriname's Ministry of Education, Science and Culture (MOE) is responsible for the education system. The ministry consists of two directorates: one responsible for education and the other for culture. The directorate of education is responsible for all matters relating to education and training, supervision of special education, promoting literacy, science and technology, libraries, and study facilities. Generally, limited staff and capacity at the MOE inhibits effective communication and monitoring of schools. Key units such as those responsible for curriculum, research and planning, and information and communications technologies are reported to be understaffed and lack training and equipment to perform their functions efficiently. Moreover, Jabbar (2014) noted that relatively weak communications systems within the MOE could be contributing to information asymmetries among staff about important initiatives. Capacity constraints also affect the MOE's ability to support schools and teachers and monitor schools effectively (Jabbar 2014).

The MOE has inspectors tasked with the responsibility of monitoring the quality of the education system and the physical infrastructure of schools. The main activities of the inspectors are to (1) determine whether schools have sufficient educational resources, (2) assess pedagogic and didactic skills of teachers, and (3) inspect school's physical infrastructure and facilities. However, the inspectors do not receive formal training, and are appointed based on their years of experience as a teacher and their reputation. Each inspector has the responsibility of at least five schools

at the primary level. At the secondary level, there are subject-oriented inspectors, meaning an inspector for each course or subset of courses. The frequency of visits to each school at both the primary and secondary levels is up to the discretion of its assigned inspector(s). Based on the findings, an inspector can request learning materials and improvements for facilities from the MOE. Information to assess the effectiveness of inspectors is not available. Therefore, in terms of teacher monitoring, there is no structured mechanism for identifying and tracking the quality of teachers. Inspectors do not possess standard evaluation protocols and, moreover, there are no standardized and independent annual evaluations of students across all grades toward computing teacher value-added measures. This is highly relevant, as objective evidence provided by Araujo et al. (2016) shows that teacher value-added measures based on student evaluations provide a better measure of teacher effectiveness than traditional teacher assessments based on direct evaluations or observation of teachers.

Teachers are recruited by the recruitment department in the MOE. The qualification required for teaching at the primary school level is a teaching diploma, which is obtained upon graduating from senior secondary school.⁷ At the junior secondary school level, teachers are required to have a bachelor's degree or an equivalent teaching diploma. There are no structured yearly calls for teachers at the primary and secondary levels. The recruitment department keeps a database of applicants and also advertises vacancies in local newspapers. Generally, recruitment at the primary level is determined by one's willingness to work in the interior and the needs of the interior. New teachers are required to sign a five-year contract to work in the interior, after which they are eligible to be transferred to another district or Paramaribo. Candidates are interviewed and prepared by the recruitment department prior to placement. At the secondary level, the recruitment process is similar but the requirement to work in the interior first does not apply. Career progress is dependent on further academic achievement, meaning a higher diploma. Remuneration for teachers, however, is based on their function or level and not performance. As such, monetary rewards are not tied to objective measures of teaching quality, resulting in low incentives to exert effort.

13.3.2. *Health*

The literature suggests that the health status of a country is an important determinant of economic success. Health itself is also considered to

⁷ There are three teacher training institutes in Suriname.

be a vital input to producing other forms of human capital and economic development. The institutions and systems that are in place to provide health care are of critical importance to a country's overall health status. Therefore, this section examines issues related to accessing quality health care in Suriname and the quality of relevant systems and institutions in the health sector.

Suriname's population has access to a mix of public and private health care services. The health care system is highly segmented, consisting of service providers that target different segments of the population. Primary health care is administered by Medical Missions (MZ) in the interior (the Amazon rainforest), Regional Health Services (RGD) in rural coastal areas, and either general practitioners or Regional Health Services in more densely populated urban areas. As of 2012, there were 274 primary health care facilities, including 63 Regional Health Services, 54 Medical Missions, 146 private polyclinics, and 11 company polyclinics. This represented a significant improvement in access to primary health care through Medical Missions and Regional Health Services for populations in the interior and coastal areas compared to the late 1970s (Goede 2014).

There are three main insurance schemes available to the Surinamese public: The State Health Foundation (SZF), programs of the Ministry of Social Affairs and Housing (MSA), and private insurance. Although the SZF is available to the public, the main beneficiaries are government employees and their dependents. It is estimated that the SZF provides health benefits to roughly 35 percent of the population and is financed through taxes on wages, subsidies, and voluntary premiums (PAHO 2002). The poor and near-poor segments of the population have access to state-subsidized health care through the MSA. The MSA covers roughly 42 percent of the population and mostly provides funds for secondary care, while the Ministry of Health and the Regional Health Services fund primary health care. Individuals without access to either MSA or SZF insurance can access private health care through private insurance, a company health clinic, or by paying out of pocket; this covers approximately 20 percent of the population (PAHO 2002). Health services are organized by the level of health care and geographical area. First-level care is provided by Regional Health Services and private practitioners in the coastal areas and by Medical Missions in the interior. Likewise, health education and preventive care are provided by the Bureau of Public Health and Regional Health Services in the coastal area, and by Medical Missions in the interior. Secondary care is provided by three general public and two general private hospitals.

Patients in the interior are usually flown to Diakonessen, a private hospital in Paramaribo, or to government hospitals: Academisch Ziekenhuis

(AZP) or the “sLands” Hospitaal (LH). Tertiary care that relates to kidney dialysis is provided by the private and public sectors, but for other services patients must travel abroad. Non-governmental organizations also provide a range of health services to targeted segments of the population (Goede 2014).

Suriname’s public health expenditure as a share of gross domestic product (GDP) is lower than all comparators considered: it is estimated at 2.9 percent of GDP, lower than the average for Latin America (4.3 percent), ROSE (4.6 percent), and the OECD (6.5 percent). A similar difference as relates to comparators is observed for total health expenditure, which stood at 5.7 percent in 2014. The comparatively low total expenditure in 2014 is close to the average for the last decade, but roughly 2 percentage points lower than the average of the previous decade (1995–2004). Despite the decrease in total health spending relative to GDP, total health expenditure per capita rose five-fold from US\$108 in 1995 to US\$589 in 2014. It is also interesting to note that private health expenditure as a percent of total health expenditure grew from 36 percent in 1995 to 48 percent in 2014, while the share of general government expenditure in total health expenditure declined from 64 to 52 percent over the same period. There was a significant increase in private insurance (percent of private health expenditure) from 1 percent in 1995 to 16 percent in 2014, while out-of-pocket expenditure in total health expenditure averaged 13 percent, a downward trend in the last decade from 15 percent in 2005 to 11 percent in 2014.

In terms of health practitioners, there is an acute shortage of health care professionals, and their distribution favors the capital. The relatively low expenditure on health is associated with a relatively low number of physicians per 1,000 population: for Suriname, it is 0.82 compared to 1.25 for Latin America, 1.67 for ROSE, and 3.38 for the OECD. The areas of specialty where the shortages exist include cardiac surgeons, neurosurgeons, neurologists, and dental surgeons, which are areas in high demand (IDB 2016). The shortage also has geographic and level-of-care dimensions. Indeed, most general physicians and nurses are located in Paramaribo and roughly 82 percent of registered nurses work in secondary care facilities (IDB 2016).

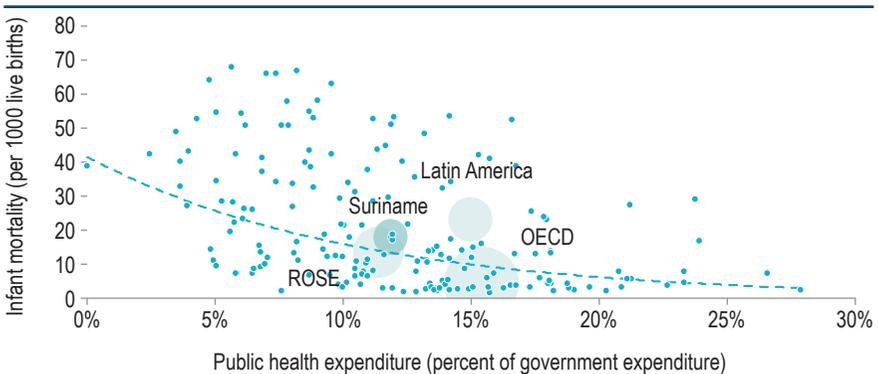
In terms of health outcomes, Suriname is below other comparator countries as evidenced by several indicators. The country’s life expectancy, an indicator that is correlated with individuals’ well-being, is lower than the average for other regions. Suriname’s life expectancy stood at 71.29 years in 2016, which is lower than the average for ROSE (75.44) and the OECD (80.94), but marginally higher than the average for Latin America (70.93). A similar pattern emerges for infant mortality. Infant mortality is 17.8 per 1,000 live births, which is higher than the average for ROSE (13.32) and the OECD

(3.39). This level of infant mortality is also higher than levels displayed by countries with similar levels of public health expenditures relative to overall government expenditures (Figure 13.9). A high rate of adolescent fertility is also a major concern. Suriname's adolescent fertility rate is 45.7 per 1,000 women ages 15–19, higher than the average for ROSE (40) and the OECD (12), but significantly lower than the average for Latin America (65).

Weaknesses in the institutions within the Ministry of Health that are responsible for planning and health contribute to an inefficient use of secondary and tertiary care resources. It is estimated that due to obsolete medical equipment and old infrastructure, primary health centers operate at 25 percent of their capacity. As a result, strain is added to an already-resource-starved secondary and tertiary sector: 60–70 percent of the population seeks assistance at hospitals for conditions that could be managed at the primary level (IDB 2016). Also, the current distribution of expenditure across levels of the health sector favors secondary care (about 50 percent), which is inconsistent with the health system's cornerstone principles of primary care and prevention.

A limited health information management system restricts assessment and tracking of the productivity and performance of health care providers. The health sector lacks mechanisms—such as an adequately resourced and robust health information management system—to generate real-time quality data on administrative, financial, and clinical procedures. Investment in such mechanisms would facilitate the modernization of administrative processes and the measurement of the productivity/quality of providers (IDB

Figure 13.9 Suriname: Public Health Expenditure, Physicians per 1,000 Population, and Infant Mortality



Source: Author's calculations based on the World Bank's 2016 World Development Indicators database.

Note: The size of the bubbles is proportional to the number of physicians per 1,000 population for selected countries or country groups.

2016). Such a system could also inform policy decisions in terms of the human resource constraint, thereby improving the quality of care and allocating resources more efficiently across distinct levels of care.

In summary, Suriname has made good strides in improving access to both health and education, but there is more work to be done to improve capacity, systems, and institutions to ensure higher quality of the human capital stock in terms of health and education outcomes.

13.4. Economic Institutions

Suriname's economy is small, heavily dependent on the mining sector, and highly open to international trade. Gold, oil, and alumina are the country's main export products, accounting for roughly 90 percent of foreign exchange earnings. The country's economic performance largely reflects the performance of the mineral sector. Suriname's average growth rate from 1975 to 2000 was 0.05 percent, significantly lower than the average growth rate of 2.96 percent for countries in Latin America and the Caribbean. The country turned the corner in the 2000s, recording a period of sustained growth that averaged 4.4 percent from 2001–2014, mainly due to favorable commodity prices. However, Suriname slipped into a deep recession in 2015 due to a sharp decline in international gold and oil prices and the cessation of alumina production. With relatively weak economic institutions and buffers, Suriname had a sharper recession and had to undertake much steeper adjustments than most commodity exporters. The country is currently undertaking macroeconomic reforms to strengthen economic institutions. This section examines the quality of economic institutions related to the implementation of monetary and fiscal policies, and the regulations and institutions for promoting private sector development.

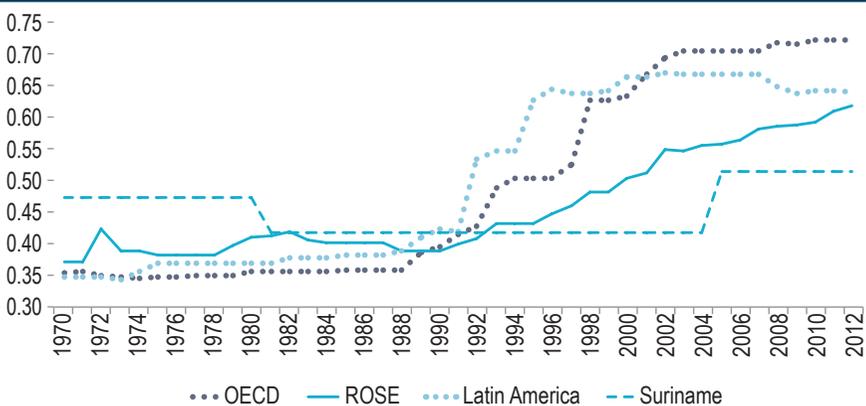
13.4.1. *Central Bank Independence and Transparency*

The Central Bank of Suriname (CBvS) is the country's monetary authority. The CBvS is a legal entity established in 1957 and operates in accordance with the *Central Bank Act* of 1956. The act lays out the bank's legal status, functions, and operational guidelines. The CBvS has as its core objectives preserving the purchasing power of the Surinamese dollar (SRD) and reserve accumulation. The CBvS also functions as supervisor/regulator of the financial sector, as banker to the commercial banks, and as cashier, banker, and financial advisor to the government. In this regard, the CBvS plays a crucial role in the financial development of Suriname. With these salient responsibilities, the bank's technical and budgetary independence

from political influence are of critical importance to ensuring the credibility of the bank itself and its policy directives.

Typically, the independence and transparency of central banks are evaluated within an objective and internationally comparable framework, as outlined in Dincer and Eichengreen (2014) and Garriga (2016). Dincer and Eichengreen (2014), however, did not include Suriname in their calculations of neither independence nor transparency. By contrast, Garriga (2016) expanded the coverage of countries and included historical series of central bank independence measures for Suriname. In terms of independence, Garriga (2016) identified four dimensions concerning the independence of central banks from political influence: who appoints the governor (weight = 0.2); whether there is direct government involvement in policy decisions (weight = 0.15); whether there are limits on the ability of the government to borrow from the central bank (weight = 0.50); and whether price stability is a core objective of monetary policy (weight = 0.15). The weighted average of these dimensions results in a central bank independence index ranging from 0 (lowest independence) to 1 (highest independence). Figure 13.10 below illustrates the evolution of the Garriga (2016) central bank independence index from 1970 to 2012 for Suriname, Latin America, ROSE and OECD member countries. While the CBVs showed relatively higher independence than all other country groups in 1970, it worsened in the 1980s and improved again in the early 2000s. By contrast, all other country groups have witnessed continuous improvements over time and, consequently, for year 2012 Suriname lagged

Figure 13.10 Suriname: Central Bank Independence Index



Source: Garriga (2016).

Note: The Central Bank Independence Index ranges from 0 (lowest independence) to 1 (highest independence).

all comparators. Indeed, in 2012 the CBvS ranked 87th out of 179 countries assessed in terms of independence.

The *Central Bank Act* of Suriname provides some insights into how institutional arrangements on issues relevant for independence work in Suriname. First, the governor of the CBvS is appointed by the President of Suriname for a five-year term that can be renewed immediately upon completion. The governor may be suspended or dismissed by the government on recommendation of the supervisory board of the CBvS. The *Central Bank Act*, however, stipulates that before such action is taken, the governor must be given an opportunity to be heard. Second, the *Central Bank Act* allows for the coordination of monetary and financial policy in cases where the minister of finance deems it necessary. However, if opinions on policy matters differ between the governor of the central bank and the minister of finance, the latter can instruct the former in writing to achieve the prescribed goal, in accordance with the *Central Bank Act* and after consultations with the supervisory board. The governor is then obliged to follow these instructions. If the governor objects to following the instructions from the minister of finance, the former can inform the government in writing within three days. The governor may be dismissed by the government if he or she refuses to or intentionally neglects to obey one or more instructions of the government. Therefore, autonomy of the governor is limited and with risk of high influence from the political power. Third, with respect to monetary financing, the CBvS is obliged in each case, as the minister shall deem necessary for temporary reinforcement of the Treasury, to grant the state advances in the current account secured by treasury bills, the issue or pledging of which is permitted under the law. At no point shall these advances total more than 10 percent of the estimated revenue of the government as budgeted for the current fiscal year. These advances shall be granted at the bank's current interest rate for these loans.⁸ Lastly, the main objectives of the CBvS include price and exchange rate stability (single-digit headline inflation and exchange rate targeting).

In terms of transparency to the public, economic agents, and policy-makers, the CBvS frequently publishes key monetary aggregates. In recent times, the CBvS has improved its provision of publicly available economic data relevant to monetary policy. Annual, quarterly, monthly, bi-weekly, weekly, and daily data are available for key variables such as money supply, inflation, exchange rates, interest rates, external accounts, and foreign

⁸ In May 2016, a memorandum of understanding was signed between the Ministry of Finance and the CBvS to cease monetary financing.

debt. The CBvS also puts out press releases on specific issues in relation to the bank and the economy in general. However, the CBvS does not publish monetary policy reports, economic bulletins, or annual reports, as is the case with other central banks in the Caribbean.⁹ Therefore, improving technical and political independence of the CBvS and transparency in its operations should rank high on the policymakers' agenda.

13.4.2. *Fiscal Institutions*

Suriname maintained relatively good fiscal performance with a relatively low debt-to-GDP ratio for the decade ending in 2014. However, the commodity shock of 2015 exposed the economy's vulnerability to the vagaries of commodity prices, and with a weak fiscal framework the authorities had to undertake frontloaded adjustments. Subsequently, Suriname commenced several reforms to strengthen the country's fiscal institutions to support macroeconomic stability.

Suriname's National Assembly passed legislation in February 2017 to establish a Savings and Stability Fund. The assembly also amended the country's debt law to effectively impose quantitative restrictions on fiscal deficits for a defined period, as the recession caused the country's public debt to exceed the previously established ceiling. Specifically, according to the Suriname Debt Management Office, the budget deficit is not to exceed 6.5 percent of nominal GDP in 2017 and at most 5 percent of nominal GDP for each year until 2021. The centerpiece of tax reform, which is expected to commence in 2018, is the introduction of a value-added tax and the removal of an inefficient sales tax. Suriname is also working on improving tax administration, as tax compliance with respect to direct taxes is estimated to be low, at 40 percent of potential revenue (IDB 2016).

In terms of transparency, the Ministry of Finance frequently publishes information on the country's fiscal accounts. Similarly, the Suriname Debt Management Office publishes detailed information on the country's debt profile. The budget is drafted in a multi-year Medium-Term Fiscal Framework (MTFF) that outlines expenditure and revenue for a given period and serves as a basis for determining the budget ceiling of government ministries per budget year. The objective of the MTFF is to ensure effective, efficient, and transparent implementation of programs and projects (Ministry of Finance 2017). It is also important to note that government priorities are established by law within the five-year multi-annual plan. The annual

⁹ The last seminal-annual report was published in 2014, which had a lag of roughly one year.

budget, in theory, is aligned with the multi-annual plan and is implemented through multi-year budgets. However, no information is available to determine whether there are institutional mechanisms to monitor and evaluate the success of programs. In addition, it is not clear whether the authorities undertake assessments related to fiscal sustainability and solvency, or to the fiscal effects of tax and spending changes for various economic sectors. There are no domestic agencies external to the government and the Parliament that provide comprehensive oversight and track compliance with fiscal objectives. While state enterprises receive a significant amount of transfers from the government, much more work needs to be done to understand their performance and identify and address perceived inefficiencies related to their workforce and operations.

Strengthening institutions and capacity within government departments related to public investment and procurement are also important for Suriname to maximize the growth and development benefits of capital spending. The IDB (2016) noted several weaknesses in public investment management as it relates to the design, execution, and evaluation of projects. Moreover, more work is required in the areas of establishing appropriate criteria to prioritize public investment projects and develop standardized methodologies for the preparation, monitoring, and evaluation of investment projects, including ex-post evaluation mechanisms. Similarly, in terms of public procurement, the IDB (2016) noted that several weaknesses need to be tackled, including establishing a Public Procurement Unit and implementing a procurement law that is consistent with international best practices.

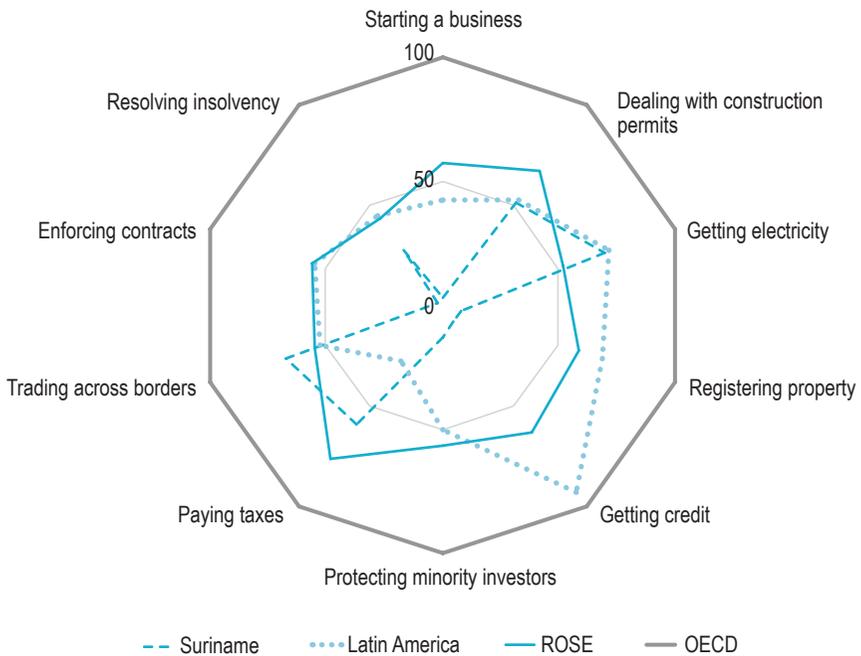
Since the 2015 commodity shock, Suriname has embarked on several initiatives to strengthen economic institutions. However, much work is still needed. Institutions that aim at limiting the possibility of fiscal mismanagement and increasing transparency and credibility of economic policies, have the potential to place Suriname on a more prosperous trajectory for growth and development.

13.4.3. *Ease of Doing Business*

A favorable business environment is important for promoting private investment, entrepreneurship, and sustainable growth (Ruprah and Sierra 2016). Private sector development, particularly in the non-mineral sector, is important for Suriname given its high dependence on a few commodities. This section examines the business environment, regulations, and institutions that are necessary to facilitate private sector development in Suriname.

The World Bank's *Doing Business Report* provides a set of indicators that allow for evaluating the favorability of the business environment in comparison to other countries. According to the report, Suriname has an unfavorable business environment compared to comparator groups along several dimensions and was ranked 165th out of 190 countries in the World Bank's 2018 *Doing Business Report*. Suriname underperforms all country groups in seven of the 10 areas of doing business: starting a business, dealing with construction permits, registering a property, getting credit, protecting minority investors, enforcing contracts and resolving insolvency. Suriname only scored better than Latin America in paying taxes, better than ROSE in getting electricity, and better than ROSE and Latin America in trading across borders (Figure 13.11). A historical look at Suriname's performance does show improvements in the areas of starting a business, registering a property, protecting minority investors, trading across borders, and resolving insolvency. In the 2018 *Doing Business*

Figure 13.11 Suriname: Ease of Doing Business



Source: World Bank, 2016 Doing Business database.

Notes: Each measure was standardized to obtain an index ranging between 0 (worst performance) and 100 (best performance) using the following formula: $(var - min)/(max - min)$, where *var* is the individual country ranking, and the maximum and minimum are the highest and lowest value in the datasets, respectively. The OECD was taken as the best practice benchmark with a value of 100 in each one of the dimensions measured.

Report, Suriname showed a significant improvement in registering a property, as the government made transferring property more transparent (World Bank 2018). The improvement in trading across borders was attributed to the implementation of an automated customs data management system, the Automated System for Customs Data (ASYCUDA), which led to a reduction in time for documentary and border compliance.

Overall, business performance in Suriname is likely to be constrained by many factors, as reflected in its overall Ease of Doing Business Index ranking that lags behind Latin America and ROSE. The constraints identified here are also consistent with the findings from the 2014 IDB Enterprise Surveys. Businesspersons from Suriname lamented several obstacles to business performance, with the top three being an inadequately educated workforce, financing constraints, and corruption. Indeed, the complaint of an inadequately educated workforce is reflected in the evidence presented earlier in this chapter on low enrolments rates, particularly at the tertiary level, the quality of the education system, emigration, and skill shortages and mismatches (IDB 2016). In addition, Suriname is one of the lowest-ranked countries in the Caribbean on Transparency International's Corruption Perception Index. This finding is consistent with evidence from the World Economic Forum (2015) that indicates that there is low public trust in politicians, a high perception of favoritism in decisions made by government officials, diversion of public funds, the occurrence of irregular payments and bribes, and wastefulness of government spending.

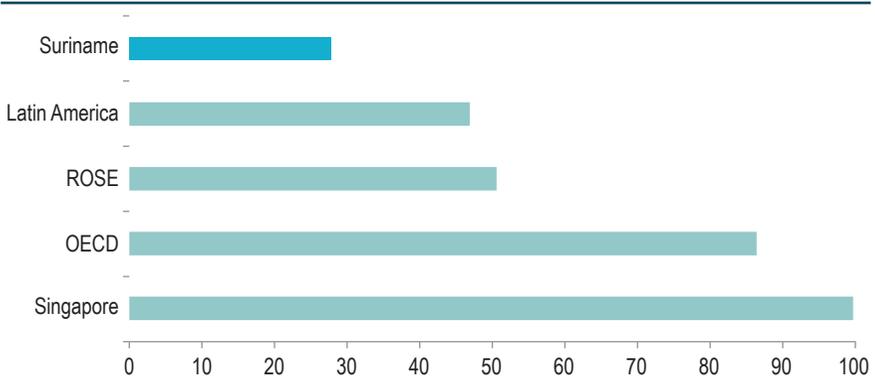
Lastly, with respect to financing constraints, Surinamese firms report that access to finance fixed assets and working capital is a major obstacle, and most of their resources originate from internal funds and retained earnings: 61 percent and 68 percent of firms report that they use retained earnings for more than half of required financing for working capital and fixed assets, respectively. Moreover, 29 percent of Surinamese firms identify the cost of financing and access to finance as a major to severe constraint to their operations. The constraints to accessing finance are related to a financial sector that is characterized by information asymmetry and an inadequate regulatory framework. Indeed, the World Bank's *2017 Doing Business Report* indicated that zero percent of adults in Suriname are covered either in a public credit registry or in a private credit bureau (World Bank 2017). This situation is broadly unfavorable compared to the world averages of 13.64 percent for credit registries and 30.81 percent for credit bureaus. Moreover, the country underperforms on the Strength of Legal Rights Index, which ranges from 0 to 12 (higher values imply better collateral and bankruptcy laws protecting the rights of borrowers and lenders). Suriname scores 2 on this index compared to 5.4 for Latin America and the

Caribbean. Weak land tenure rights also inhibit potential borrowing firms from having adequate proof of collateral to qualify for loans (IDB 2016).

In terms of medium-to-long-term planning, the country does have a Policy Development Plan, which is required by law. The most recent Policy Development Plan was published in January 2017 by the National Planning Office for the period 2017–2021. That plan, which replaces the Development Plan for the period 2010–2016, broadly outlines the country’s development policies and aims to address the recent economic crisis and promote social and economic development. The plan, which includes economic diversification, is based on four pillars: (1) strengthening development capacity, (2) economic growth and diversification, (3) social progress, and (4) utilization and protection of the environment. The Development Plan consists of two parts: the first is the substantive document and the second summarizes the strengths, weaknesses, opportunities, and threats analysis of the 49 development areas. Information regarding the estimated cost, time schedule for implementation, and development outcomes is included.

In terms of institutions to promote competitiveness, in 2012 Suriname established a Competitiveness Unit to coordinate and monitor issues related to national competitiveness and offer recommendations to improve the competitiveness of the national economy. Among its main tasks are to coordinate government actions to strengthen national competitiveness; coordinate business climate reform and a private sector development roadmap; establish consultations among ministries/institutes; engage with stakeholders; identify priority growth sectors; and formulate and monitor

Figure 13.12 Suriname: Regulatory Quality



Source: World Bank, 2017 World Governance Indicators database (www.govindicators.org).

Notes: Percentile ranking score ranging from 0 (worst in regulatory quality) to 100 (best in regulatory quality). Regulatory quality captures perceptions of the ability of the government to formulate and implement sound policies and regulations that permit and promote private sector development. Singapore is the best country worldwide in terms of regulatory quality.

competitiveness strategies. However, the country's draft competition bill is yet to be voted on by the National Assembly.

The U.S. State Department (2015) has highlighted that employment protection legislation in Suriname is very stringent, as labor laws require employers to obtain permission of the Ministry of Labor to fire an employee once that employee has completed his or her probationary period (two months as required by law). Moreover, taxes on the formal business sector are considered a burden, while a large informal sector remains untaxed. Indeed, as shown in Figure 13.12, Suriname lags significantly behind in terms of the quality of policies and regulations aimed at permitting and promoting private sector development.

13.5. Conclusions and Policy Recommendations

Since experiencing more than a decade of political instability and military rule after obtaining independence in 1975, Suriname has developed a strong electoral process that has facilitated relatively peaceful transitions of different political parties into government. Although politics is largely ethnic-based with limited turnover of political elites, Suriname has a system that encourages collaboration and alliances among various ethnic-based parties to form the government. That approach helps to promote consensus-building among the country's various ethnic and religious factions on important national issues. Moreover, Suriname also has an independent entity to oversee election processes, and international observers such as the OAS and CARICOM have generally provided favorable reviews of the country's election processes. Despite these strengths, there are some areas that could be further improved, including strengthening internal party democracy, promoting greater transparency with respect to political financing, and promoting women's participation in politics.

There is also room to strengthen institutional capacity and address ambiguities as they relate to the legislature's oversight of the executive. The constitution places considerable power in the Office of the President, but with what seems to be unclear mechanisms for the legislature to rein in such power. One of the main ambiguities relates to the lack of clarity of the legislature to remove the president and vice president from office before their tenure is constitutionally due. Related to this constraint is the absence of a Constitutional Court to deliver impartial judgements and interpretations on constitutional matters. Also, mechanisms are lacking for the electorate to recall members of Parliament and the executive during a five-year term. There is a need for the introduction and enforcement of legislation that can force government officials to declare finances, and for

greater transparency in campaign financing. Improvements in these areas, along with greater transparency of the decision-making process by the executive, could help reduce the high public perception of corruption.

In terms of the rule of law, despite some weaknesses related to law enforcement and effective functioning of the judiciary, Suriname has relatively lower crime rates than other countries in the Caribbean. While the judiciary is in principle independent of the other branches of government, its independence has come under scrutiny in the past due to ambiguities in the constitution and actions taken by the executive. While ambiguity on constitutional matters is not unique to Suriname, the lack of an impartial body to make interpretations and rulings accentuates adverse perceptions of the independence of the judiciary. The judiciary also lacks financial autonomy and suffers from several shortcomings related to inadequate resources, such as personnel and physical space to effectively undertake its mandate and provide timely justice.

There are some critical shortcomings that must be addressed to support the development of quality human capital in Suriname. In terms of education, the Ministry of Education lacks sufficient capacity to effectively monitor and evaluate the performance of the school system. These capacity constraints are reflected in inadequate resources and infrastructure (particularly in the interior), a shortage of quality teachers, disparity in the qualifications required for teachers in the interior versus urban areas, and low management capacity and limited communication channels within the education system. Moreover, information asymmetry between the demands of the labor market and the curriculum and insufficient employment-related services also contribute to lowering the probability of employment for graduates. Similarly, to improve the provision of quality health care Suriname needs to strengthen institutions related to health planning capabilities and invest in modern technology and medical equipment. As non-communicable diseases are the leading cause of deaths, a greater emphasis should be placed on strengthening and improving access to reliable primary health care along with a gender-balance focus on national health policies. Mechanisms such as information management systems are also needed to ensure that the productivity and performance of medical practitioners are assessed and tracked over time.

Finally, with respect to economic institutions, Suriname has embarked on several initiatives to strengthen the country's macroeconomic framework since the 2015 economic crisis. Some of the main measures currently being implemented include imposing limits on budget deficits, enacting legislation to establish a Savings and Stability Fund, and the implementation of a value-added tax along with other tax administration reforms.

While these reforms are important to help with fiscal management, other areas that require policy attention include providing greater transparency on the operation of state-owned enterprises, strengthening transparency on public procurement, and developing institutions and regulations related to public investment management. In terms of monetary policy, the *Central Bank Act* allows for executive influence over policy decisions of the central bank. Thus, increased independence of the CBvS, and further improvements in its transparency, through more frequent information on its operations and regular publications on monetary policy and economic developments in Suriname, would better guide the expectations and decisions of economic agents, particularly domestic and foreign investors.

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Trinidad and Tobago

Jeetendra Khadan and Lodewijk Smets

14.1. Political Institutions

Trinidad and Tobago functions as a parliamentary democracy based on the Westminster model of governance. In line with its British colonial legacy, Trinidad and Tobago's legislative branch consists of a bicameral Parliament. The House of Representatives is composed of 41 members of Parliament and the house speaker. Members of the House of Representatives are elected by popular vote for a five-year term with the possibility of reelection. The members of the House of Representatives are elected to represent 41 geographically defined constituencies. Each political party selects one candidate per constituency. The political leader of the winning party typically becomes the prime minister elect. The Senate or upper house holds 31 senators. Senators are appointed by the president: 16 on the advice of the prime minister, six on the advice of the opposition leader, and nine at the president's own discretion. There are no limits on the reappointments of senators.

Executive authority is vested in the president. The president is the head of state and commander-in-chief of the armed forces. The powers of the president are exercisable within constitutional limits that often require the advice of or consultation with another authority such as the Cabinet, the prime minister, or the leader of the opposition. The president is not elected directly, but through secret ballot by the electoral college, which consists of all members of Parliament, both the Senate and the House of Representatives. The candidate who has received the largest number of votes or who is unopposed is declared as the president for a term of five years. There are no term limits for the Office of the President.

The executive branch is made up of the Office of the President, the Office of the Prime Minister, and the Cabinet. The president appoints the ministers of government on the advice of the prime minister. The prime

minister selects the members of Cabinet mostly from the elected members of the House of Representatives, who are then appointed by the president. There are currently 27 government ministers who make up the Cabinet with responsibility for 22 government ministries.¹ A significant number of state agencies also fall under the executive, including state enterprises, statutory authorities and municipal corporations.

The constitution offers the House of Representatives a mechanism to keep the head of government under control in the form of a vote of no confidence. It stipulates that a majority in the House of Representatives can pass a resolution of no confidence in the prime minister. Several other measures aim to provide checks and balances in the political system. First, for amendments to the constitution, a special majority (either two-thirds or three-fifths) of voting members of both houses of Parliament is required. Second, the bicameral parliamentary system acts as a balancing mechanism, as bills generally must be passed by both houses (the Senate and House of Representatives) and receive the assent of the president before they become law. Third, both houses of Parliament scrutinize executive proposals and decision-making. Finally, Trinidad and Tobago has a strong civil society that has increasingly raised its voice through both traditional and social media.

14.1.1. *Political Parties and Background*

Trinidad and Tobago's struggle for parliamentary representation began in 1846 with a request to the Colonial Office for a representative assembly. The demand for political representation intensified during the 1930s through the trade union movement. In 1946, universal suffrage and a new legislative council were introduced. By the 1950s a structured party system began to take shape with a clear split along ethnic lines. The current political landscape is dominated by two political parties with a distinct ethnic base but with a common left-wing orientation. These parties are the People's National Movement (PNM) and the United National Congress (UNC). Table 14.1 summarizes the main characteristics and periods in power of both parties.

The PNM was founded in 1955 by Eric Williams. One year after the PNM was formed, the party contested general elections in 1956 and again in 1961, winning 13 of 24 seats and 20 of 30 seats in the Legislative Council, respectively. The PNM then led the country to independence on August 31,

¹ Some ministries have more than one minister. Those ministers are usually called "ministers in ministries," for example, the Minister in the Ministry of National Security.

Table 14.1 Profiles of the Main Political Parties in Trinidad and Tobago

Name of Party	Initials	Periods in Power	Ideology	Ethnic Background or Ethnic Voter Base	Prevailing Religion within Voter Base
People's National Movement	PNM	1956–1981 1991–1995 2002–2010 2015–present	Democratic socialism (center left)	African	Non-Hindu Indians, Muslims, and Christians
United National Congress	UNC	1995–2000 2001 2010–2015	Democratic socialism (center left)	Indian	Hindu

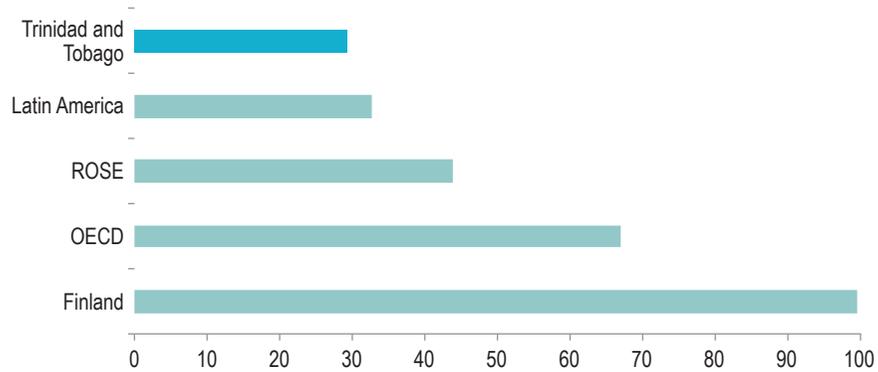
Source: Authors' elaboration based on www.caribbeanelections.com.

1962. After independence, the PNM held power for an unbroken period of 26 years, winning every election from 1966 to 1981. It regained power during the periods 1991–1995 and 2002–2010. The party's support base lies predominantly among African-Creole voters. It also attracts non-Hindu East Indians, primarily Muslims and Christians (Catón 2005).

The UNC was founded in 1989 by Basdeo Panday. The UNC entered government for the first time in 1995. It later went on to win an absolute majority in the 2000 election, but within one year in government a split in the party caused it to lose its parliamentary majority and control of government. The UNC entered government a third time in 2010, through a coalition agreement with other opposition forces called the People's Partnership Coalition.

The 2015 general election saw a return of the PNM to power under a new political leader, Keith Rowley. A total of 17 political parties registered, with four parties running as part of a UNC-led People's Partnership coalition arrangement. There were 1,099,279 registered voters in the 41 constituencies. On election day, 732,533 valid votes were recorded, representing a voter turnout of 66.8 percent. The PNM won 51.7 percent of total votes and secured 23 seats in the House of Representatives, followed by 17 seats for the UNC. The last remaining seat went to another member of the UNC-led People's Partnership (The Congress of the People).

In summary, Trinidad and Tobago has a political system that reflects the Westminster model of governance, with several checks and balances to keep the executive accountable. However, the main political parties largely draw on ethnic support, which holds the risk of identity voting and ethnic contention during election times. As shown in Chapter 6, previous literature has associated similar settings with increased incentives for rent-seeking behavior and interest group politics. Indeed, Figure 14.1 shows that Trinidad and Tobago performs insufficiently on the Public-Regardedness

Figure 14.1 Trinidad and Tobago: Public-Regardedness Index

Source: Authors' calculations using the database in Berkman et al. (2008).

Notes: Each measure was standardized to obtain an index ranging between 0 (worst performance) and 100 (best performance) using the following formula: $(var - min)/(max - min)$, where *var* is the individual country measure, and the maximum and minimum are the highest and lowest value in the datasets, respectively. Finland is the country with the highest Public-Regardedness Index score worldwide. OECD: Organisation for Economic Co-operation and Development; ROSE: rest of the small economies of the world.

Index, which indicates the extent to which policies pursued are perceived to be in the public interest or whether they tend to be directed toward special interest groups.²

The next section turns to analyzing the extent to which relevant rules and institutions in place have guaranteed democratic participation and transparency in electoral processes.

14.1.2 Political Representation, Competition, and Transparency in the Political System

Countries are more likely to establish appropriate economic institutions that in turn spur development when they have an open pluralistic political system with competition for political office, a widespread electorate, and openness to new political leaders (Acemoglu and Robinson 2012). As

² As explained in Chapter 6 of this volume, the Public-Regardedness Index was proposed in Berkman et al. (2008). The authors computed this index using expert evaluations and perceptions on issues related to (1) corruption, (2) public spending on social transfers, and (3) whether government contracts are awarded fairly or generally favor well-connected firms and individuals. The index is the combination of these three measures. The first component was taken from Transparency International Corruption's Perceptions Index, and the last two components from the Global Competitiveness Report.

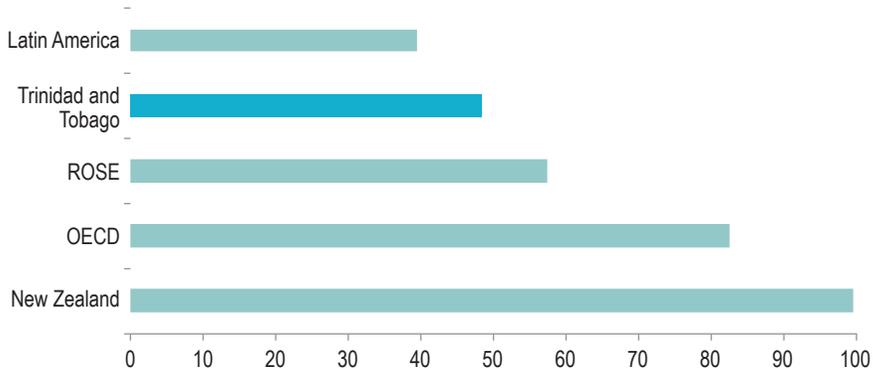
such, it is important to assess the extent to which political participation is widely accessible or whether rules and institutions restrict it to a minority elite. Answering this requires an inspection of the process by which political parties appoint their leaders and electoral candidates.

Political parties in Trinidad and Tobago have constitutions that govern their operations. Internal party elections are held—time periods vary by political party—to elect a political leader and members of an executive team to conduct the affairs of the political party. The political leader of the winning party typically becomes the prime minister elect. Each political party also sets up internal screening committees to interview and select potential candidates to contest seats in the general elections. Each political party selects one candidate per constituency. History has shown little variation in the political elite governing the country. For instance, from 1956 until 1981, Eric Williams (PNM) held the post of prime minister, while Patrick Manning (also PNM) headed the government for 15 years within the period 1991–2010.³ This suggests that the openness of the political system is somewhat limited, which may favor state capture by a minority elite. In the World Bank’s World Governance Indicators, which measure the extent to which the state is captured by elites and private interests within the control of corruption dimension, Trinidad and Tobago outperforms the average Latin American country but lags the rest of the small economies of the world (ROSE) and the Organisation for Economic Co-operation and Development (OECD), suggesting room for improvement in this dimension (Figure 14.2).

Public participation in and transparency of electoral processes are central aspects for any democracy. In Trinidad and Tobago, the body charged with administering elections, certifying vote counts, and reporting results is the Elections and Boundaries Commission (EBC). The EBC was established in 1971 and is comprised of a chairman and three members who are all appointed by the president in consultation with the prime minister and the leader of opposition. The EBC’s main responsibilities are to review the number of constituencies and their boundaries, the registry of voters, and supervision of the election process.

Elections in Trinidad and Tobago are often observed by international organizations such as the Commonwealth Observer Group and the Caribbean Community (CARICOM). Both organizations observed the election process in 2015 and concluded that the country has affirmed its strong track record of peaceful and credible elections. The Commonwealth

³ Between 1995 and 2001 Basdeo Panday of the United National Congress (UNC) was the prime minister in Trinidad and Tobago.

Figure 14.2 Trinidad and Tobago: Control of Corruption

Source: World Bank, 2017 World Governance Indicators database (www.govindicators.org).

Notes: Percentile ranking score ranging from 0 (worst in controlling corruption) to 100 (best in controlling corruption). Control of corruption captures perceptions of the extent to which public power is exercised for private gain, including both petty and grand forms of corruption, as well as “capture” of the state by elites and private interests. New Zealand is the best country worldwide in terms of controlling corruption.

Observer Group (2015) also emphasized the high degree of confidence that the EBC enjoys among various stakeholders in the country. Nevertheless, issues related to the legal framework and election administration, the election campaign and the media, and shortfalls related to special voting were identified as areas for improvement to further strengthen the country’s election process.

Within these circumstances, it is relevant to assess the mechanisms under which the legislative branch can exert constraints and accountability over the executive. The next section looks at these topics.

14.1.3. *Constraints on the Executive and Accountability*

The constitution provides the House of Representatives a mechanism to keep the head of government under control in the form of a vote of no confidence. It stipulates that a majority in the House of Representatives can pass a resolution of no confidence in the prime minister. If the prime minister does not resign or advise the president to dissolve Parliament within seven days of the passing of such a resolution, the president can revoke the appointment of the prime minister.

Several other measures aim to provide checks and balances in the political system. First, a special majority (either two-thirds or three-fifths) of voting members of both houses of Parliament is required for amendments to the constitution. Second, the bicameral parliamentary system acts as a balancing mechanism, as bills generally must be passed by both

houses—the Senate and House of Representatives—and receive the assent of the president before they become law. Third, both houses of Parliament scrutinize executive proposals and decision-making. For instance, before budget execution, the minister of finance needs to present the budget to Parliament. After the budget is debated and passed in both houses of Parliament, it is sent to the president for his assent. Only thereafter can execution commence.

Trinidad and Tobago has a strong civil society that has increasingly raised its voice through both traditional and social media. The country also has several watchdog organizations that monitor and debate decisions of Parliament and national authorities. The chambers of commerce and academia are also active in the public space, discussing the government’s policies and budget and the impact of international developments on the local economy through frequent conferences and seminars.

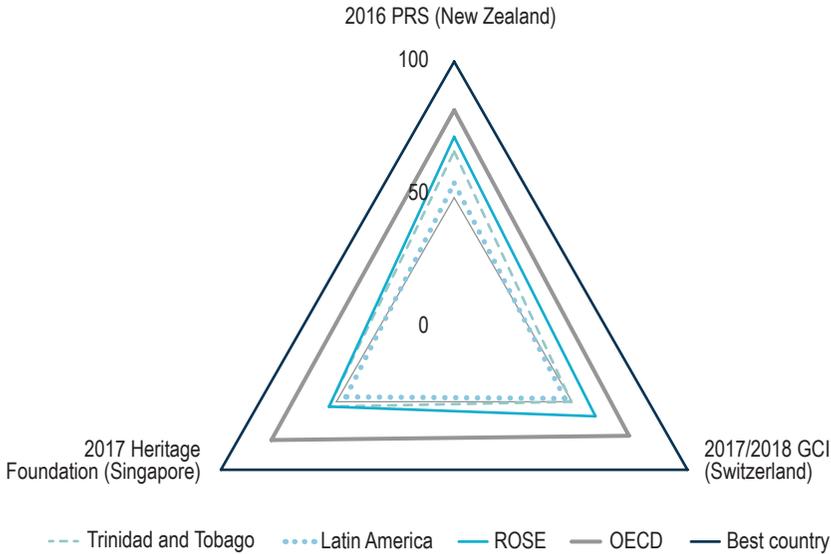
14.2. Rule of Law Institutions

As shown in Chapter 4, the literature to date clearly suggests that there are three key institutional rule of law components that show a significant causal relation with economic growth. The first relates to the strength of property rights protecting private agents from the risk of having their property expropriated by either government or powerful elites. The second relates to the fundamental rights embedded in the constitution. The third relates to the possibility of obtaining fair and independent administration of justice with the strength to enforce the law without external pressures. This section assesses the condition of these institutions in Trinidad and Tobago.

14.2.1. *Strength of Property Rights*

International assessments of property rights put Trinidad and Tobago on par with ROSE but also show there is room for improvement toward reaching OECD levels. Both the Heritage Foundation’s property rights indicator, the Index of Freedom, and the Political Risk Services Index of Protection against Expropriation show that Trinidad and Tobago has levels of property rights protection similar to those of ROSE (Figure 14.3). All three indicators reported in Figure 14.3 indicate there is room to improve the protection of property rights in the country.

Therefore, given the evidence on the importance of property rights for economic and social development, special attention should be placed on improving such institutional arrangements. Besides property rights, a

Figure 14.3 Trinidad and Tobago: Strength of Property Rights

Sources: Political Risk Services (PRS) 2016 database (www.prsgroup.com); World Economic Forum, 2017/2018 Global Competitiveness Index (GCI) database; and Heritage Foundation, 2017 Index of Freedom (www.heritage.org).

Note: Each measure was standardized to obtain an index ranging between 0 (worst performance) and 100 (best performance) using the following formula: $(var - min)/(max - min)$, where *var* is the individual country measure, and the maximum and minimum are the highest and lowest value in the datasets, respectively.

relevant dimension for social development and cohesion relates to respect for and protection of fundamental human rights. The next section assesses these issues.

14.2.2. Protection of Fundamental Human Rights

The constitution of Trinidad and Tobago guarantees equality before the law. The constitution states that “...in Trinidad and Tobago there have existed and shall continue to exist, without discrimination by reason of race, origin, color, religion or sex, fundamental human rights and freedoms...[which include] the right of the individual to equality before the law and the protection of the law.”

Table 14.2 shows how these constitutional rights play out in practice. It relies on data from the 2016 World Justice Project. Overall, Trinidad and Tobago scores on par with ROSE and slightly better than the Latin American average. Negative outliers in the protection of fundamental rights are due process of law, respect for the rights of the accused, and arbitrary

Table 14.2 Protection of Fundamental Rights in Trinidad and Tobago

Fundamental Rights	Trinidad and Tobago	Latin America	ROSE	OECD
Overall Fundamental Rights	0.61	0.58	0.62	0.76
4.1 Equal treatment and absence of discrimination	0.60	0.51	0.62	0.70
4.2 The right to life and security of the person is effectively guaranteed	0.61	0.61	0.67	0.86
4.3 Due process of law and rights of the accused	0.39	0.46	0.56	0.73
4.4 Freedom of opinion and expression is effectively guaranteed	0.68	0.61	0.59	0.74
4.5 Freedom of belief and religion is effectively guaranteed	0.73	0.75	0.71	0.76
4.6 Freedom from arbitrary interference with privacy is effectively guaranteed	0.48	0.52	0.51	0.77
4.7 Freedom of assembly and association is effectively guaranteed	0.74	0.66	0.71	0.79
4.8 Fundamental labor rights are effectively guaranteed	0.64	0.56	0.60	0.71

Source: World Justice Project (WJP) (<https://worldjusticeproject.org/our-work/wjp-rule-law-index/wjp-rule-law-index-2016/factors-rule-law>).

Note: Scores for the WJP Rule of Law Index, as well as for its component factors and subfactors, range from 0 to 1, where scores closer to 1 indicate better performance.

inference regarding privacy rights. However, Trinidad and Tobago scores high on freedom of assembly and association.

14.2.3. *Judicial Independence and Effectiveness*

The judiciary is headed by the chief justice, who is responsible for the general administration of justice. The judicial system is separated into a Supreme Court of Judicature (higher judiciary) and the Magistracy (lower judiciary). The Supreme Court of Judicature consists of the Court of Appeal and the High Court. The Magistracy is made up of the Courts of Summary Criminal Jurisdiction and Petty Civil Courts. The chief magistrate has responsibility for the Magistracy and reports to the chief justice. The Office of the Director of Public Prosecutions (DPP) is Trinidad and Tobago's prosecution entity.

The judiciary is established by the constitution to operate independently from the executive. The chief justice is appointed by the president in consultation with the prime minister and leader of the opposition. The holder of the position of chief justice is also the president of the Court of Appeal, an ex-officio judge of the High Court, and chairman of the Judicial and Legal Service Commission (JLSC). The JLSC has the responsibility of appointing justices of appeal, High Court judges, masters of the High

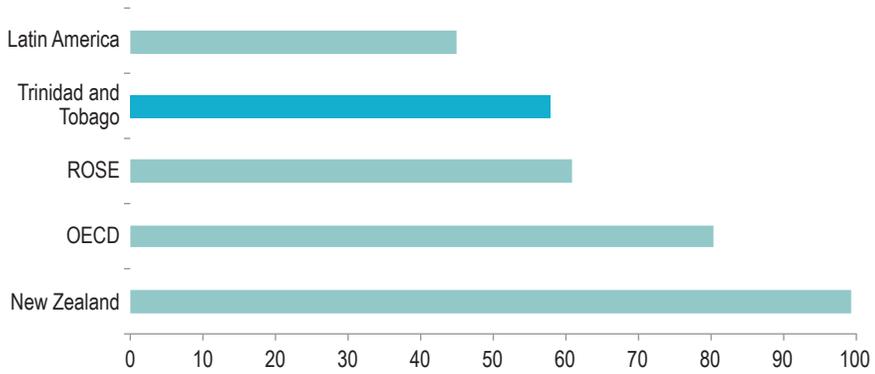
Court, magistrates, registrars of the Supreme Court, and the administrative secretary to the chief justice.

The Office of the DPP is established under Section 90 of the constitution and operates independently of the executive. The director of public prosecutions is appointed by the President of Trinidad and Tobago in consultation with the prime minister and leader of the opposition. The DPP is supported by legal staff that should number about 40 attorneys-at-law. Prosecutors are typically attorneys-at-law from the Office of the DPP. However, for criminal matters in the Magistrates Court, a police officer who has attained the rank of sergeant and above usually presents the facts of the case.

The judiciary lacks financial autonomy. Financial and administrative autonomy has been a key area of concern for judicial independence in Trinidad and Tobago (Mendes 2000). For instance, at the start of the 2014/2015 law term, the chief justice indicated that an insufficient budget allocation, low remuneration of judges, and delays in the release of funds from the government were among the main problems facing the judiciary. Similarly, in a meeting of the Joint Select Committee of Parliament in March 2017, the director of public prosecutions lamented the lack of physical space and abysmal under-staffing that has contributed to a backlog of cases. Furthermore, the level of protection afforded to state prosecutors could be significantly improved. The concern for the protection of prosecutors became a critical issue over the past few years due to the assassination of a state prosecutor in 2014. Increasing the financial autonomy of the judiciary and improving the protection of state prosecutors—two areas the government is currently working on—could further improve Trinidad and Tobago’s ranking on the Judicial Independence Index (Figure 14.4).

In terms of judicial effectiveness, Trinidad and Tobago performs better than Latin America, ROSE, and even the OECD in civil justice, but underperforms in criminal justice with respect to Latin America and the OECD (Table 14.3). Concerning civil justice, indicators show that Trinidad and Tobago’s judiciary is largely free from corruption and government influence. The data also show that Trinidad and Tobago performs better than Latin America and ROSE (but not the OECD) in the delivery of civil justice in a timely manner, civil justice being free of discrimination, and civil justice being effectively enforced.

As criminal justice is concerned, the evidence shows that Trinidad and Tobago has a weaker performance compared to Latin America and the OECD. The relatively lower scores reflect weaknesses in the criminal investigative system, the adjudication system, impartiality, due process of law and the rights of the accused, and effectiveness of the correctional system to reduce criminal behavior.

Figure 14.4 Trinidad and Tobago: Judicial Independence Index

Source: Authors' calculations based on the database in Berkman et al. (2008).

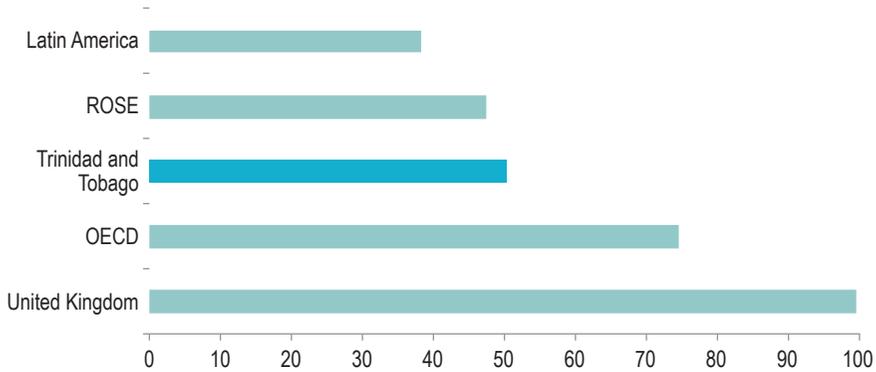
Notes: Each measure was standardized to obtain an index ranging between 0 (worst performance) and 100 (best performance) using the following formula: $(var - min)/(max - min)$, where *var* is the individual country measure, and the maximum and minimum are the highest and lowest value in the datasets, respectively. New Zealand is the country with the highest Judicial Independence Index score.

Table 14.3 Judicial Effectiveness

	Trinidad and Tobago	Latin America	ROSE	OECD
Civil Justice	0.61	0.57	0.47	0.60
7.1 People can access and afford civil justice	0.54	0.56	0.54	0.55
7.2 Civil justice is free of discrimination	0.61	0.57	0.51	0.63
7.3 Civil justice is free of corruption	0.78	0.74	0.47	0.62
7.4 Civil justice is free of improper government influence	0.72	0.64	0.44	0.57
7.5 Civil justice is not subject to unreasonable delay	0.48	0.43	0.28	0.56
7.6. Civil justice is effectively enforced	0.50	0.48	0.44	0.57
7.7 Alternative dispute resolution mechanisms are accessible, impartial, and effective	0.64	0.61	0.65	0.71
Criminal Justice	0.40	0.50	0.36	0.53
8.1 Criminal investigation system is effective	0.27	0.39	0.29	0.50
8.2 Criminal adjudication system is timely and effective	0.30	0.46	0.33	0.53
8.3 Correctional system is effective in reducing criminal behavior	0.31	0.41	0.22	0.51
8.4 Criminal system is impartial	0.41	0.44	0.38	0.51
8.5 Criminal system is free of corruption	0.63	0.69	0.45	0.62
8.6 Criminal system is free of improper government influence	0.51	0.66	0.37	0.50
8.7 Due process of law and the rights of the accused	0.39	0.49	0.46	0.56

Source: World Justice Project (WJP) (<https://worldjusticeproject.org/our-work/wjp-rule-law-index/wjp-rule-law-index-2016/factors-rule-law>).

Note: Scores for the WJP Rule of Law Index, as well as for its component factors and subfactors, range from 0 to 1, where scores closer to 1 indicate better performance.

Figure 14.5 Trinidad and Tobago: Judicial Effectiveness Index

Source: Authors' calculations using the 2017 Heritage Foundation Index of Freedom (www.heritage.org) database.

Notes: Each measure was standardized to obtain an index ranging between 0 (worst performance) and 100 (best performance) using the following formula: $(var - min)/(max - min)$, where *var* is the individual country measure, and the maximum and minimum are the highest and lowest value in the datasets, respectively. The United Kingdom is the country with the highest Judicial Effectiveness Index score worldwide.

The country therefore has a medium level of overall judicial effectiveness, as captured by the 2017 Heritage Foundation Index of Freedom, outperforming Latin America and ROSE but lagging the OECD (Figure 14.5). This is consistent with the relatively low density of judges, which stands at seven judges per 100,000 population, below the world average of 18 judges per 100,000 population.⁴

14.2.4. Law Enforcement

The Trinidad and Tobago Police Service (TTPS), the country's law enforcement body, falls within the ambit of the Ministry of National Security. The main mandates of the police service are to maintain law and order, protect life and property, prevent and detect crime, and enforce all laws and regulations that fall within its remit. The TTPS is comprised of nine divisions and 26 branches charged with various responsibilities. There are 6,500 police officers and 78 police stations in Trinidad and Tobago.

The commissioner of police is the head of the TTPS. The commissioner and deputy commissioners are appointed by the Police Service Commission (PSC) through a selection process determined by the Parliament. The

⁴ Source: United Nations Office on Drugs and Crime, criminal justice data for 2014 or latest available year. Caribbean countries included are The Bahamas, Barbados, Jamaica, and Trinidad and Tobago.

PSC is an independent body established by the constitution consisting of a chairman and four members who are appointed by the president in consultation with the prime minister and the leader of the opposition. In addition, the PSC is responsible for managing the monitoring, appointments, disciplinary, and appeals functions of the TTPS. The process to appoint a commissioner of police and a deputy commissioner is often described as rigorous, though convoluted and costly.

Trinidad and Tobago's Police Training Academy trains new recruits and conducts refresher courses for serving officers. Some courses are offered in collaboration with other agencies such as the Ministry of Education, Central Training Unit, and professional management consultants. The educational requirements to become a police officer require successful completion of secondary school. Applicants are also required to take an entrance examination and undertake several medical and physical tests. Successful applicants are then interviewed by a selection panel. Training involves an enhanced introduction program over a 24-week cycle. Successful trainees are then transferred to a police station to begin their career as a police officer. The new recruits undergo a probation period of two years during which they are closely supervised, and their performance evaluated. The opportunity to be promoted to the rank of corporal comes after three years of service. Promotion to higher ranks is attained through continuous assessment.

The Crime and Problem Analysis Branch (CAPA) is the TTPS data processing unit. It analyses information from crime reports and other sources to inform the crime deterrence, disruption, and detection efforts of the Police Service. A diagnostic analysis by the Crime and Problem Analysis Unit, however, found several areas for improvement: data collection, validation, and verification procedures and their application leave ample room for error (IDB 2016). Victimization surveys have not been carried out with any regularity in Trinidad and Tobago. In addition, complementary crime and violence data collected by other government ministries are not normally shared, published, or released, and systems to track, record, and analyze crime are lacking.

Oversight of the TTPS is performed by the Police Complaints Authority (PCA). The PCA is an independent body mandated to provide civilian oversight of law enforcement and to independently investigate complaints against police officers involved in criminal offences, police corruption, and serious police misconduct. The PCA accepts walk-in complaints, mailed complaints, and emailed complaints from the public. The *PCA Act* also allows the authority to initiate its own investigations.

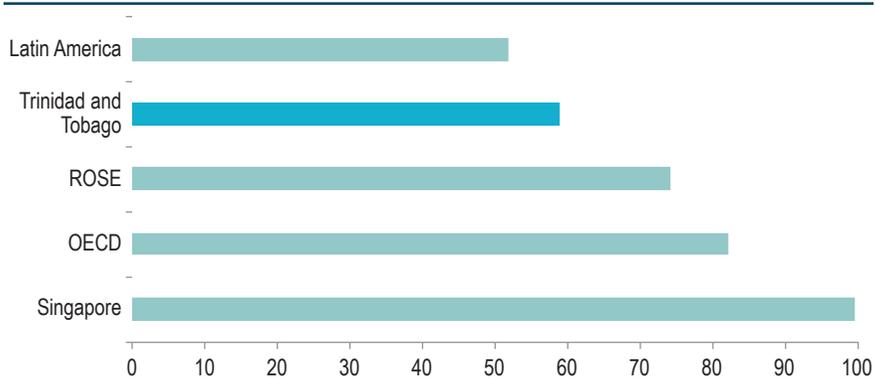
The number of complaints received by the PCA has increased over the past seven years. The PCA received 255 complaints in 2010 and 321

complaints in 2014. The highest number of complaints received in a single year was 491 in 2015. There are many allegations of criminal and disciplinary offences against or involving the police. For the period October 2014 to September 2015, the PCA received reports of 672 offences. It was estimated that 230 were allegations of criminal offences and 442 were allegations of disciplinary offences. The breakdown of these allegations shows that 60 percent were related to serious police misconduct, 37 percent to the commission of a criminal offence by a police officer, and 3 percent to police corruption.

The data suggest that police effectiveness needs to be improved. Despite increasing expenditure over the years, detection rates for major crimes remain low. Trinidad and Tobago has one of the highest homicide rates in the Americas (30.88 per 100,000 inhabitants). The number of homicides increased from 84 in 1990 to 463 in 2013. The detection rate, however, was 13 percent in 2013. Incidents of wounding and shootings increased from 391 to 542, while the detection rate declined from 61 to 24 percent during the period 1990 to 2013. Similar but less drastic declines in detection rates were reported for other crimes (Khadan 2016). The high incidence of crime and violence has been linked to drug-related activities, limitations in enforcing the law, lack of credibility of the police force, and a tendency to resort to violence to resolve personal grievances. Therefore, Trinidad and Tobago's ranking on the Order and Security Index remains well below the ROSE and OECD average (Figure 14.6).

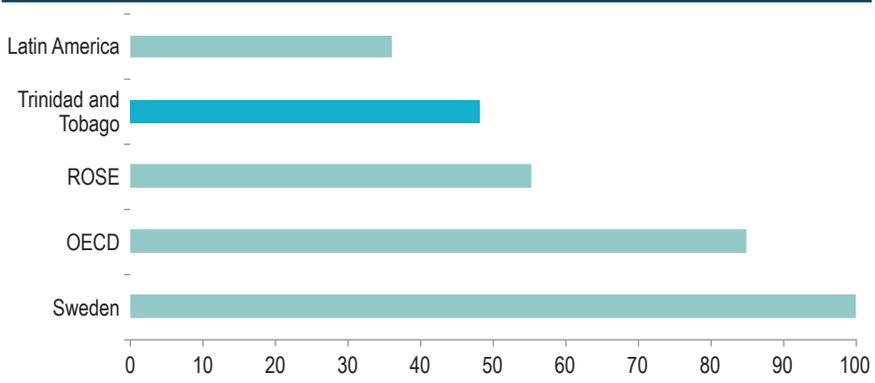
In summary, this section has evidenced that several institutions related to the rule of law in Trinidad and Tobago could be improved. There is scope to

Figure 14.6 Trinidad and Tobago: Order and Security Index



Source: Authors' calculations using the 2016 World Justice Project database.

Notes: Each measure was standardized to obtain an index ranging between 0 (worst performance) and 100 (best performance) using the following formula: $(var - min)/(max - min)$, where *var* is the individual country measure, and the maximum and minimum are the highest and lowest value in the datasets, respectively. Singapore is the country with the highest Order and Security Index score worldwide.

Figure 14.7 Trinidad and Tobago: Rule of Law

Source: World Bank, 2017 World Governance Indicators database (www.govindicators.org).

Notes: Percentile ranking score ranging from 0 (worst in rule of law) to 100 (best in rule of law). Rule of law captures perceptions of the extent to which agents have confidence in and abide by the rules of society, and in particular the quality of contract enforcement, property rights, the police, and the courts, as well as the likelihood of crime and violence. Sweden is the best country worldwide in terms of the rule of law.

enhance the protection of property and fundamental human rights, criminal justice, and security and order. The situation as it stands could partly erode the confidence of economic agents in the rules of the society, thereby hindering the ability to spur investment and growth. Indeed, as shown in Figure 14.7, the country's ranking on the 2016 Rule of Law dimension ranks below the average for ROSE, although it does perform better than the Latin American average.

14.3. Institutions for Human Capital Development

As shown in Chapter 4, two main institutions supporting human capital development have been highlighted in the literature: institutions related to education and health. Therefore, this section documents the situation of these institutions in Trinidad and Tobago.

14.3.1. Education

The related evidence presented in Chapter 4 suggests that the quality of education matters more than the quantity. Furthermore, the quality of education hinges primarily on the quality of teachers. Therefore, this section will focus not only on the ability of educational institutions to offer educational services coverage, but also on the extent to which institutions ensure appropriate teacher quality in Trinidad and Tobago.

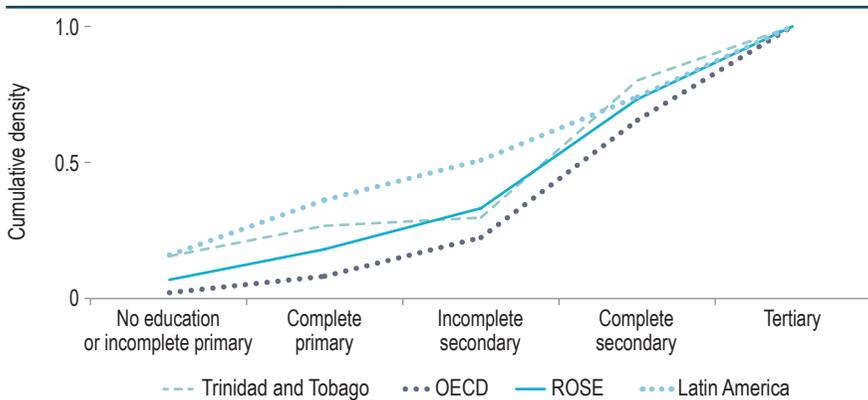
Trinidad and Tobago offers free public education from the pre-primary to the secondary level. Of the 895 primary and secondary schools, just over

half are managed by religious orders while being funded by the government. A further 37 percent are run and owned by the government and 21 percent are private. At the tertiary level, Trinidad and Tobago hosts three government-funded universities. The largest by enrolment, the University of the West Indies (UWI) St. Augustine Campus, offers post-graduate programs including PhD degrees. The Ministry of Education subsidizes full tuition for low-income households at the undergraduate level. However, the share of working-age adults (25–65 years old) with tertiary education is 19.7 percent, which is below the OECD, ROSE, and Latin American averages (Figure 14.8).

As mentioned above, it is the quality of education rather than the quantity that matters for development. Chapter 4 indicated that monitoring of teachers' effort and performance-based hiring are of crucial importance to improve the quality of the educational system. This section documents the extent to which institutional arrangements are present in Trinidad and Tobago to ensure appropriate teacher quality.

School supervision and quality monitoring of the education system largely fall under the Office of the Chief Education Officer within the Ministry of Education (MOE). The office consists of five units, including a unit charged with educational research and evaluation and a unit responsible for school supervision. Institutional efforts seeking to boost the quality of teaching has been undertaken in the past. These have included delinking of teachers' salaries from the general civil service, strengthening teacher training institutions, and introducing more rigorous entry requirements into the teaching profession. However, there is still ample room for improvement as

Figure 14.8 Trinidad and Tobago: Educational Attainment



Source: Authors' calculations based on the 2014 Trinidad and Tobago Survey of Living Conditions and the World Bank's 2016 World Development Indicators database.

Note: Educational attainment is measured among working age adults (25–65 years old) who have completed their formal education.

no explicit and structured mechanisms to evaluate teacher effectiveness are in place, except for a mechanism called clinical supervision. The objective of clinical supervision is to help teachers improve their teaching and delivery, but the mechanism is only employed in an ad hoc manner.

Although there are several standardized examinations that students take across primary and secondary school, such data are not organized as individual level longitudinal series, analyzed or used to evaluate both students and teacher performance over time. In terms of measures of teacher effectiveness, if appropriately organized, the existing data of students' evaluations across time could be used to compute teacher specific value-added measures. This is highly relevant, as objective evidence provided by Araujo et al. (2016) shows that teacher value-added measures based on student evaluations provide a better measure of teacher effectiveness than traditional teacher assessments based on direct evaluations or observation of teachers. Implementing this type of measures, however, usually faces resistance. This is a continued challenge for which, already existing, objective evidence showing the appropriateness of value-added based evaluations of teachers should guide agreements and policy decisions.

The recruitment of teachers for secondary schools is done through the Teaching Service Commission's Recruitment Committee. The Curriculum Division of the Ministry of Education, first, has the responsibility for determining an applicant's suitability for serving as a teacher in the teaching service. Candidates who have been assessed are then placed in a database according to their year of assessment. The Recruitment Committee of the Teaching Service Commission then calls candidates for interviews based on demands from the Ministry of Education in the relevant subject areas. Those candidates who are successful are placed on a priority list that is sent to the permanent secretary of the Ministry of Education. Placement of teachers in schools depends on the availability of vacancies and subject area. Teachers' career advancement is tied to academic advancement, meaning completion of a degree program or any other required training courses, and not to objective performance measures.

14.3.2. Health

Trinidad and Tobago's population has access to both public and private health care. Public health care is based on universal access and citizens can access free health care services at public facilities. Health insurance is not required, and medicines are free at public health facilities. The Ministry of Health—through five regional health facilities—manages a network of nine hospitals, nine district health facilities, and 96 health centers. Basic

or primary level care is provided at health centers and district health facilities, while secondary-level care is provided at public hospitals. Patients are referred to secondary care facilities by primary care providers when the need arises. Tertiary care is also offered, though limited, at specific hospitals.

Trinidad and Tobago also has a relatively small but vibrant private health sector. About 19.5 percent of the population has access to private health care.⁵ The private sector mainly consists of individual physicians, private pharmacies, and 10 medical institutions that can accommodate up to 39,000 patients. Private health care providers offer a variety of health services, both in-patient and out-patient treatment, and mostly operate on a fee-for-service basis, funded by out-of-pocket expenses or private health insurance. Private health care facilities are mainly located in urban areas and there is a strong perception that private medical facilities offer a better quality of service and treatment than public facilities. Although the government does not finance private medical institutions, the public sector has subcontracted some health services to private health care providers.

Trinidad and Tobago's total health expenditure is estimated at 5.93 percent of gross domestic product (GDP), lower than the average for Latin America (7.5 percent), ROSE (6.9 percent), and the OECD (8.7 percent). Similarly, public health expenditure (as a share of GDP) is 3.17 percent, below Latin America (4.3 percent), ROSE (4.6 percent), and the OECD (6.5 percent).⁶ There are 1.18 physicians per 1,000 population in Trinidad and Tobago, which is below the levels for Latin America (1.25), ROSE (1.67), and the OECD (3.38). With 16.5 deaths per 1,000 live births, infant mortality is higher than ROSE (13.32) and the OECD (4.24), but lower than Latin America (23.04). However, as shown in Figure 14.9, Trinidad and Tobago's infant mortality rate is equivalent to other countries investing a similar share of government expenditure in health.

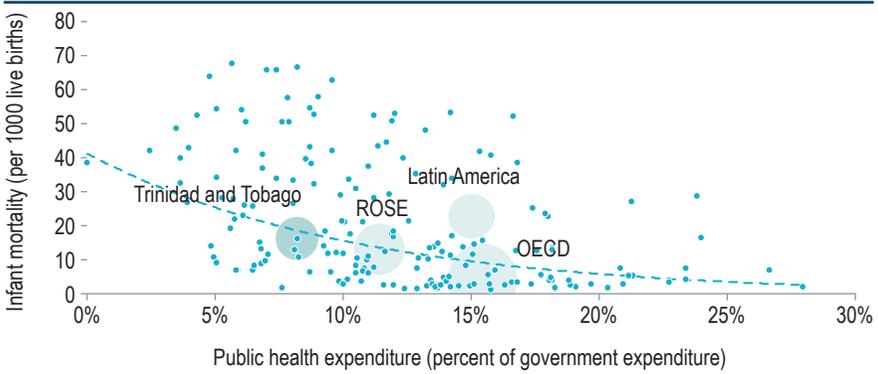
Trinidad and Tobago has undergone an epidemiological and demographic transition, fueled by an aging population structure, and characterized by a high prevalence of non-communicable diseases (NCDs), which now claim more lives than infectious diseases. Recent data indicates that six common NCDs: heart disease, hypertension, cerebrovascular disease (collectively referred to as cardiovascular disease - CVD), diabetes, cancer, and chronic respiratory illness, account for 60% of all deaths in Trinidad and Tobago.⁷ If taken all NCDs together, they account for 78% of all deaths in the

⁵ Source: 2014 Trinidad and Tobago Survey of Living Conditions.

⁶ Source: World Bank, 2016 World Development Indicators.

⁷ Source: Healthy Caribbean Coalition. (2014). Responses to NCDs in the Caribbean Community.

Figure 14.9 Trinidad and Tobago: Public Health Expenditure, Physicians per 1,000 Population, and Infant Mortality



Source: Authors' calculations using the World Bank's 2016 World Development Indicators database.

Note: The size of the bubbles is proportional to the number of physicians per 1,000 population for selected countries or country groups.

country.⁸ Furthermore, Trinidad and Tobago's CVD mortality rate is one of the highest in the Americas (289 deaths per 100,000 population compared to Chile at 125 per 100,000 population).⁹

The Chemistry Food and Drug Division (CFDD) is the principal authority responsible for implementing and enforcing health regulations in Trinidad and Tobago (WHO 2014). The CFDD is responsible for ensuring safe quality of an equitable standard for use by consumers of food, drugs, and medical services. These responsibilities are carried out by three different units of the CFDD: (1) the food and drugs inspectorate; (2) the pesticides inspectorate; and (3) the laboratory service.

Besides these institutional measures to maintain high-quality health services, individual-level incentives for health care providers in the public sector—for example, performance evaluation and merit-based promotion—are lacking in Trinidad and Tobago. The lack of such arrangements may prevent medical practitioners from being incentivized to exert high effort. Introducing a retention strategy which includes continued educational opportunities, financial and non-financial incentives based on objective measures of performance might thus be considered to boost quality in the health sector.

⁸ Source: World Health Organization. (2011). Trinidad and Tobago non-communicable diseases country profile.

⁹ Source: de Fatima Marinho de Souza et al. (2012). CVD mortality in the Americas. *Heart*, 98(16), 1207-12.

14.4. Economic Institutions

Trinidad and Tobago is a hydrocarbon-dependent economy whose fiscal and external performance is driven by the energy sector. During 2010–2015, the energy sector—producing oil, gas, and petrochemicals—generated 40 percent of nominal GDP. However, declining oil and gas prices in global markets and technical disruptions in domestic energy production led to an economic recession from which the country is slowly recovering. The downturn in the energy sector also led to twin deficits in the government and external accounts. Sound economic institutions are required to cope with such shocks. Therefore, this section assesses the state of key economic institutions that, as shown in Chapter 5, have been associated with increased confidence, investment, and growth.

14.4.1. *Central Bank Independence and Transparency*

The Central Bank of Trinidad and Tobago (CBTT) is the country's monetary authority. It is managed by a Board of Directors that includes a governor, at most two deputy governors, and at least six other directors. The Board of Directors is appointed by the President of Trinidad and Tobago. The governor is appointed for a term of five years, and deputy governors for a term fixed by the president. The *Central Bank Act* outlines a wide range of responsibilities for the central bank that range from maintaining monetary stability to conducting financial research. With respect to implementation of monetary policy, the CBTT has three primary objectives: the maintenance of a low and stable rate of inflation, an orderly foreign exchange market, and an adequate level of foreign exchange reserves.

The way central banks are governed influences the credibility of these institutions and their effectiveness in controlling inflation and providing a proper environment for economic growth and prosperity. The 2016–2020 strategic plan of the Central Bank of Trinidad and Tobago includes as an important pillar the strengthening of governance, transparency, and accountability. The bank has made noteworthy progress in this respect, especially in the area of operational efficiency.

However, data for 2010 provided in Dincer and Eichengreen (2014) and historical data covering the period 1970–2012 provided by Garriga (2016) show that improvements could be made to ensure central bank independence. For instance, the *Central Bank Act* permits the minister of finance to issue general directives to the CBTT to give effect to the government's monetary and fiscal policies. However, the *Central Bank Act* stipulates that the total amount of outstanding advances to the government is not to

exceed 15 percent of annual revenue, hence limiting the ability of government to borrow from the central bank.

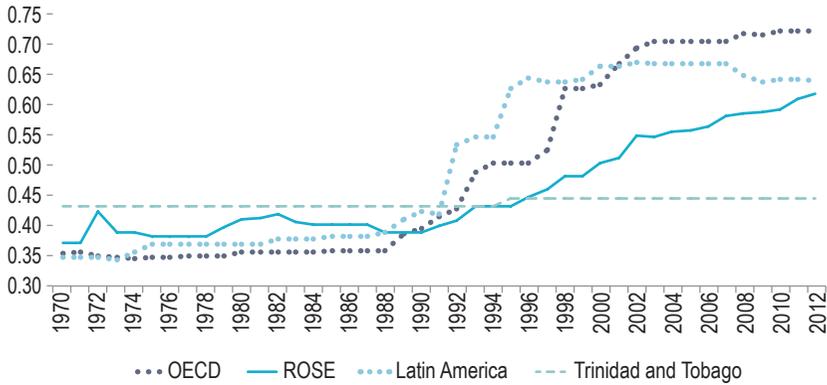
Objective international comparisons of central bank independence reported in Dincer and Eichengreen (2014) rank the CBTT relatively low at 77th out of 89 countries worldwide.¹⁰ In a study covering an extended set of countries worldwide, Garriga (2016) ranked the CBTT in the 106th position out of 179 countries.¹¹ This relative recent disadvantaged position in terms of independence, however, has not been an historical norm for the CBTT. Figure 14.10 illustrates the evolution of the Garriga (2016) central bank independence index from 1970 to 2012 for Trinidad and Tobago, Latin America, ROSE and OECD member countries. The CBTT showed higher independence than all other country groups in 1970, but its independence level has not improved much over time. By contrast, all other country groups have witnessed continuous improvements over time and, consequently, for year 2012 Trinidad and Tobago lagged all comparators.

In terms of legal requirements for accountability of the bank's operations, the *Central Bank Act* stipulates that the accounts of the bank shall be audited annually by auditors who are appointed by the board and approved by the minister of finance. In addition, the minister of finance may at any time require the auditor general to examine and report on the accounts of the central bank. Within three months after the financial year, the CBTT is required to provide to the minister of finance a report on the operation of the bank for the preceding financial year and the audited financial statements certified by the auditors. The annual audited statement is then presented in Parliament by the minister of finance and published in the Gazette. The bank is also required to prepare and communicate to the minister of finance on a weekly basis its assets and liabilities, which must also be published in the Gazette.

In terms of transparency to the public, the central bank publishes several reports with varying time frequencies. With respect to decisions about

¹⁰ This ranking is based on the Central Bank Independence Weighted Index (CBIW) for 2010 reported in Dincer and Eichengreen (2014). The CBIW is a weighted average of measures related to the following dimensions: CEO appointment (weight = 0.1), policy formulation (0.15), objectives (0.15), limitations on lending to the government (0.50), and appointment of board members (0.1). For details on the specific components of these measures, see Table 18 in Dincer and Eichengreen (2014).

¹¹ This ranking is for year 2012. Garriga (2016) identified four dimensions concerning the independence of central banks from political influence: who appoints the governor (weight = 0.2); whether there is direct government involvement in policy decisions (weight = 0.15); whether there are limits on the ability of the government to borrow from the central bank (weight = 0.50); and whether price stability is a core objective of monetary policy (weight = 0.15). The weighted average of these dimensions results in a central bank independence index ranging from 0 (lowest independence) to 1 (highest independence).

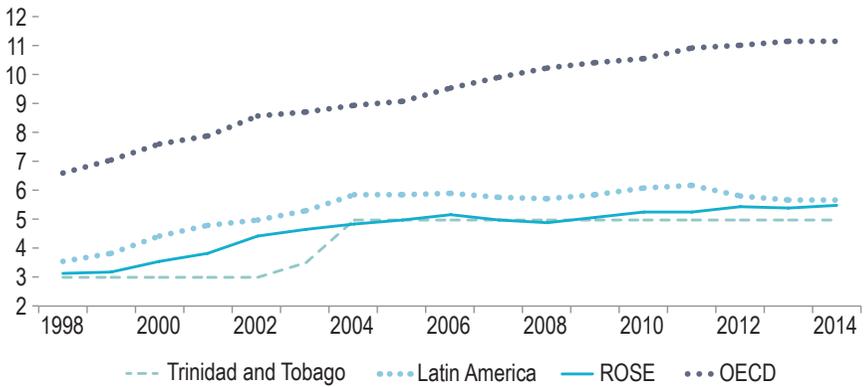
Figure 14.10 Trinidad and Tobago: Central Bank Independence Index

Source: Garriga (2016).

Note: The Central Bank Independence Index ranges from 0 (lowest independence) to 1 (highest independence).

monetary policy, the CBTT has an established Monetary Policy Committee (MPC) assisted by a Monetary Policy Secretariat (MPS). The MPC is chaired by the chief economist and comprised of members from various departments of the CBTT. The MPC has the mandate to develop and implement the monetary policy framework. In addition to setting the repo rate, the MPC supervises the preparation and publication of a bi-monthly Monetary Policy Announcement and a semi-annual Monetary Policy Report. The CBTT also publishes data on macroeconomic aggregates and several other reports, such as the Annual Economic Survey, Balance of Payments Report, Business Confidence Report, Consumer Confidence Report, Economic Bulletin, Financial Stability Report, Labor Confidence Report, Statistical Digest, and Summary of Economic Indicators Bulletin. However, following Dincer and Eichengreen (2014), measures of overall transparency that include political, economic, procedural, policy, and operational transparency suggest that, although the CBTT is ranked similarly with Latin America and ROSE, there is still ample room for improvement toward reaching OECD levels (Figure 14.11).¹²

¹² The Central Bank Transparency Index measures compliance with 15 best practices distributed across the following areas: political transparency (practices), economic transparency (three practices), procedural transparency (three practices), policy transparency (three practices), and operational transparency (three practices). The index ranges from 0 (no compliance at all) to 15 (full compliance with the 15 best practices). For details on the specific practices and index construction, see Appendix 1 in Dincer and Eichengreen (2014).

Figure 14.11 Trinidad and Tobago: Central Bank Transparency Index

Source: Dincer and Eichengreen (2014) updated database for Central Bank Transparency 1998–2014 (https://eml.berkeley.edu/~eichengr/Dincer-Eichengreen_figures&tables_2014_9-4-15.pdf).

Note: The Central Bank Transparency Index ranges between 0 (lowest transparency) and 15 (highest transparency).

14.4.2. Fiscal Institutions

Trinidad and Tobago's economy is highly dependent on the energy sector (oil, gas, and petrochemicals). For instance, during 2010–2015, the energy sector generated 40 percent of GDP and 50 percent of fiscal revenues. It is well understood that commodity-dependent countries are at a greater risk of facing significant fiscal adjustments due to price and supply shocks to the resource sector (for Trinidad and Tobago, see Khadan 2016). As such, it is important to establish strong fiscal frameworks with appropriate levels of stabilization savings, effective spending policies, and effective use of taxation to reduce revenue volatility (IMF 2015). If properly established, objective fiscal rules, independent fiscal councils monitoring compliance with fiscal rules, and sovereign wealth funds provide a medium-term anchor that enhances the credibility of policies and supports inter-generational equity (see Chapter 5). By contrast, the lack of such institutions makes fiscal mismanagement more likely.

Trinidad and Tobago only has an explicit fiscal target for its annual budget; a multi-year fiscal framework does not exist.¹³ At present, the Ministry

¹³ From time to time, however, the minister of finance may make broad statements on how the government would like to see the fiscal accounts develop over the medium term, although these generally lack detail on what the key policy measures are that will contribute to such an outcome. Moreover, medium-term forecasts of other macroeconomic aggregates (GDP, inflation) that are important to evaluate fiscal and macroeconomic performance are also absent from annual budget planning.

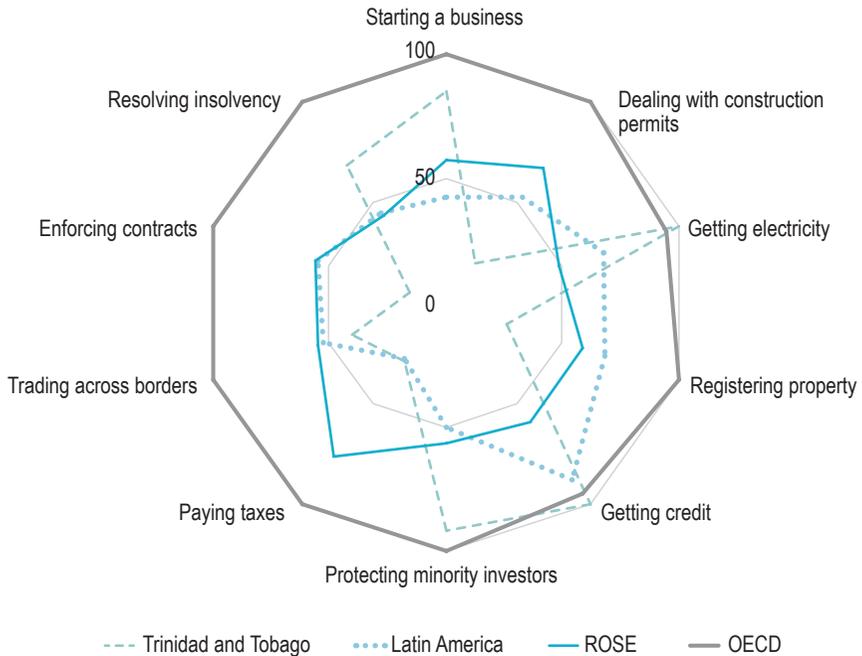
of Finance produces projections for revenues, expenditure, and the fiscal balance for one year. The authorities make public the assumptions of commodity prices used to estimate energy revenue forecasts, and the allocation of government expenditure across government ministries and by functional areas. Fiscal performance during the fiscal year is monitored and evaluated by the Ministry of Finance through the publication of a mid-year budget review that is debated in Parliament. While fiscal performance is publicly discussed, Trinidad and Tobago does not have an independent fiscal council.

Trinidad and Tobago can rely on a sovereign wealth fund to manage revenue volatility. It introduced its Heritage and Stabilization Fund (HSF) in 2007 with the objectives of smoothing public expenditures and saving resources for future generations. At present, it has mostly operated as a savings fund, with US\$3.5 billion—about 60 percent of the current stock—considered the “heritage” component, that is, the floor below which funds cannot be accessed for stabilization purposes. It was only in 2016 that the government of Trinidad and Tobago began to draw on the stabilization component of the fund to finance government spending. In terms of management and transparency, the HSF is managed by an independent board comprised of members from the Ministry of Finance, Central Bank, and the private sector. Operational management is delegated to the Central Bank and quarterly reports on the fund’s performance are published by the Central Bank.

14.4.3. *Ease of Doing Business*

As shown in Ruprah and Sierra (2016), private entrepreneurship and innovation are key drivers to boost investment, innovation, growth, and development. Therefore, institutions and regulations that permit and promote private sector development are extremely relevant. As such, this section assesses the state of these issues in Trinidad and Tobago.

According to the World Bank’s 2016 Doing Business Indicators, Trinidad and Tobago underperforms vis-à-vis other country groups in dimensions such as contract enforcement and property registration (Figure 14.12). The time and cost of enforcing contracts through a local first-instance court in Trinidad and Tobago is lengthy and high. On average, it takes 1,340 days to enforce contracts, the 13th longest time in the world and more than twice the time it takes in other Caribbean countries. With a large number of procedures and elevated costs, registering property in Trinidad and Tobago is also a challenge. This is reflected in the World Bank’s Ease of Registering Property Index, which ranks the country 150th out of 190 countries in 2017.

Figure 14.12 Trinidad and Tobago: Ease of Doing Business

Source: World Bank, 2016 Doing Business database.

Notes: Each measure was standardized to obtain an index ranging between 0 (worst performance) and 100 (best performance) using the following formula: $(var - min)/(max - min)$, where *var* is the individual country ranking, and the maximum and minimum are the highest and lowest value in the datasets, respectively. The OECD was taken as the best practice benchmark with a value of 100 in each one of the dimensions measured.

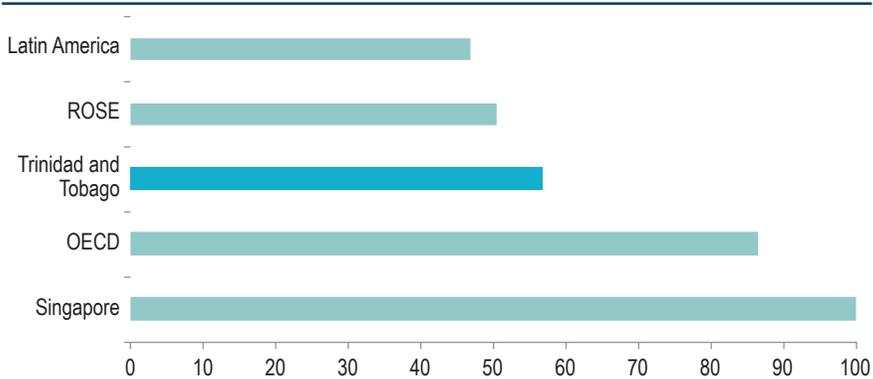
According to Figure 14.12, Trinidad and Tobago performs well along other dimensions, such as access to credit and protection of investors. The protection of shareholders is outlined in the *Companies Act* of Trinidad and Tobago. The act clearly stipulates that shareholders of a company (other than of an unlimited liability company) are not liable for any liability, act, or default of the company. This is reflected in the country's relatively good ranking in the World Bank's Ease of Doing Business Index for the protection of minority investors, at 62nd out of 190 countries.

The banking system in Trinidad and Tobago is generally well capitalized, profitable, and highly liquid. There is a high level of penetration of banking services. Commercial bank branches per 100,000 adults is estimated at 13, compared to 15 in Latin America and the Caribbean. However, electronic and Internet banking exist at all commercial banks, which facilitates greater access of banking services to citizens. Combined, these factors explain why economic agents in Trinidad and Tobago get good access to credit.

Current tax administration rules and procedures are cumbersome, as the average firm spends 210 hours and makes 39 payments annually compared to 183 hours and 24 payments annually by firms in ROSE. Sahadeo (2012) notes that tax administration in Trinidad and Tobago faces several challenges, including human capital management, customer service, and corruption. Regarding the latter, Trinidad and Tobago moved from 101st to 77th on Transparency International's 2017 Corruption Perception Index. However, an independent and autonomous anti-corruption agency would be a further step forward and help in reducing high levels of perceived corruption.

Finally, Trinidad and Tobago has produced several plans and strategies over time to diversify the country's exports and revenue sources. Some of the main plans in recent years include Vision 2020 and Vision 2030. These plans are generally very detailed and identify the challenges facing the economy, provide policy recommendations, and specify the relevant authorities and agencies responsible for undertaking policy action. In addition, most strategies are derived from rigorous research and consultations with key stakeholders in the economy. Despite these strategies and plans, however, the lack of an implementation and financing strategy, along with other structural features of the economy that disincentivize productive activity in the non-energy sector, has contributed to a slow pace of economic diversification. As such, the quality of policies and regulations to promote private sector development leave room for improvement. Trinidad and Tobago is above Latin America and ROSE in terms of regulatory quality, but still significantly below OECD levels (Figure 14.13).

Figure 14.13 Trinidad and Tobago: Regulatory Quality



Source: World Bank, 2017 World Governance Indicators Database (www.govindicators.org).

Notes: Percentile ranking score ranging from 0 (worst in regulatory quality) to 100 (best in regulatory quality). Regulatory quality captures perceptions of the ability of the government to formulate and implement sound policies and regulations that permit and promote private sector development. Singapore is the best country worldwide in terms of regulatory quality.

14.5. Conclusions and Policy Recommendations

Trinidad and Tobago has a political system that reflects the Westminster model of governance, with several checks and balances to keep the executive accountable. Except for an attempted coup in July 1990, Trinidad and Tobago enjoys peaceful transitions of power, governed by free and fair elections. Elections are administered by a representative Elections and Boundaries Commission and scrutinized by international observers such as the Commonwealth Observer Group and the Caribbean Community.

In Trinidad and Tobago, the main political parties largely draw on ethnic support, which holds the risk of identity voting and ethnic contention during election times. Furthermore, low historic levels of political turnover may provide incentives for rent-seeking behavior and interest group politics. Therefore, increasing transparency and accountability in the political system—for example, full information disclosure in budget execution, policies, and programs, objective monitoring of political performance, etc.—could enhance the country’s institutional capacity and lead to improved prosperity and development outcomes.

This chapter has evidenced that several institutions related to the rule of law could stand to be improved. There is scope to enhance the protection of property and fundamental human rights, criminal justice, and security and order. Improving the financial autonomy of the judicial system could increase the effectiveness of the criminal investigation and correctional system, leading to an eventual reduction in criminal behavior. Finding ways to increase the legitimacy of the police force could further contribute to improvements in the rule of law.

Health and education institutions are two important drivers of human capital outcomes. As the quality of education rather than the quantity is what matters for development, Trinidad and Tobago might consider developing rules and procedures for performance-based hiring and systems to monitor teachers’ effort. Besides some institutional arrangements to monitor the health system, individual-level incentives for health care providers—for example, performance evaluation and merit-based promotion—are lacking in Trinidad and Tobago. The lack of such arrangements may prevent medical practitioners from being incentivized to exert high effort. Introducing incentive schemes based on objective measures of performance such as individual-level value added might thus be considered to boost quality in both the education and health sectors.

Trinidad and Tobago has little experience with legal rules and institutions to improve fiscal performance. If properly established, fiscal rules and fiscal councils provide a medium-term anchor that enhances the

credibility of policies and supports inter-generational equity. Currently, no formal fiscal rules or councils exist in Trinidad and Tobago, which makes fiscal mismanagement more likely. The country would also benefit from a more detailed fiscal medium-term framework that allows for planning and budget execution. The Central Bank of Trinidad and Tobago is in the process of improving its transparency and accountability, especially in the area of operational efficiency. Ensuring central bank independence should also be on the policymakers' agenda.

Enhancing the business climate in Trinidad and Tobago could promote private sector development and sustainable economic growth. This chapter has pointed to problems with contract enforcement and property registration. Current tax administration rules and procedures are cumbersome, as the average firm spends 210 hours to comply with regulations. Furthermore, an independent and autonomous anti-corruption agency might help reduce elevated levels of perceived corruption. Finally, putting into practice plans and strategies to diversify the economy could provide a further boost to growth.

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A Policy Agenda for the Caribbean

Diether W. Beuermann and Moisés J. Schwartz

This book has provided an in-depth review of the evidence to date on the role of institutions for economic development worldwide, as well as a thorough analysis of the design and quality of relevant institutions within the six countries that constitute the Inter-American Development Bank's Caribbean Country Department: The Bahamas, Barbados, Guyana, Jamaica, Suriname, and Trinidad and Tobago. In doing this, the volume fills a gap in our understanding of the nature and state of institutions in the Caribbean. Following the literature, special emphasis has been placed on the institutions that frame the political system, the rule of law, human capital development, and economic management. The volume documented the status of institutions in Caribbean countries with the objective of promoting policy-relevant dialogue that could place these countries on a more prosperous development path. Weak fiscal frameworks in some of these countries, and their vulnerability to external shocks, prompted the exploration of relevant institutions that have been shown to increase certainty in economic policymaking and, thus, spur growth and build resilience to such shocks.

Inclusive and trustworthy political institutions—characterized by an open pluralistic system with competition for political office, a widespread electorate, and openness to new political leaders—constitute the foundation for developing the appropriate rule of law, human capital development, and economic institutions, which in turn fosters sustainable growth (Acemoglu and Robinson 2012). In terms of the rule of law, clearly defined property rights that protect citizens from expropriation of their property by the state or by powerful elites, and that ensure an independent judiciary, are unambiguous determinants of economic development. Institutions that promote the development of human capital by providing quality public education and health are powerful predictors of economic and social development. Objective, performance-based hiring and appropriate retention incentives

for teachers and health providers have been shown to attract qualified people into these careers, thereby increasing the productivity and effectiveness of public service delivery. For their part, economic institutions such as trade and financial openness, medium-term fiscal frameworks, fiscal rules and councils, sovereign wealth funds, and central bank independence and transparency increase certainty in economic policymaking and hence contribute to a more conducive environment for investment and growth.

As exemplified in this volume, the state and development of the numerous institutions analyzed in each country is different. For example, Caribbean commodity-dependent countries (CCB-C: Guyana, Suriname, and Trinidad and Tobago) show relatively greater vulnerability in terms of social indicators such as poverty, educational attainment, infant mortality, and life expectancy than do non-commodity-dependent Caribbean countries (CCB-NC: The Bahamas, Barbados, and Jamaica). Similarly, CCB-NC countries outperform CCB-C countries regarding trustworthiness in politicians, including perceived public trust, diversion of public funds, transparency of government policymaking, and favoritism in decisions of government officials. Nonetheless, while CCB-NC countries have relatively better social outcomes, fiscal performance is relatively weak across all Caribbean economies. This macroeconomic fragility, coupled with crime and violence, a stagnant private sector, high rates of outward migration, and adverse climate-related factors such as tropical storms, hurricanes, and sea level rise, has resulted in low rates of growth and high debt levels.

Regarding institutions that support the rule of law, the strength of property rights among CCB-NC countries stands at levels equivalent to member countries of the Organisation for Economic Co-operation and Development and well above the levels for CCB-C countries. This is relevant because investment and growth have been shown to be incentivized by strong rule of law institutions. In terms of the administration of justice, Caribbean countries in general have judiciary systems with a relatively low incidence of corruption. However, timeliness in the administration of justice is relatively protracted, significantly underperforming comparable small economies worldwide. For example, the average number of professional judges per 100,000 population in Caribbean countries is 7.5, while the world average is 18. Therefore, the region should consider implementing policies to increase the coverage of judicial services through appropriate staffing, improvements in efficiency, and greater use of technology.

Regarding institutions related to human capital development, Caribbean countries lack structured mechanisms for identifying and tracking quality teachers. There are no standardized and independent annual

evaluations of students across all primary and secondary grades that could be used to help design measures of the value added by teachers. Similarly, objective periodic performance evaluations of health practitioners are not institutionalized. Introducing incentive schemes based on objective measures of performance might therefore be considered to boost productivity and improve results in the education and health sectors.

The independence and transparency of central banks influence the credibility of these institutions and their effectiveness in controlling inflation and providing a proper environment for economic growth and prosperity. Caribbean countries, however, show relatively low levels of central bank independence and transparency. Ensuring technical and political independence of central banks, as well as introducing greater transparency in their operations, should rank high on the agendas of policymakers in the region.

Institutions that provide incentives for long-term sustainability and that contain overspending improve fiscal performance. If properly established, medium-term fiscal frameworks, fiscal rules, independent fiscal councils that monitor compliance with fiscal objectives, and sovereign wealth funds provide a sustainable anchor that enhances the credibility of policies and supports inter-generational equity. The lack of such institutions makes fiscal mismanagement more likely. The establishment of these institutions will likely help improve the transparency and credibility of fiscal policy, as well as increase awareness of the political and social costs of unsound policies. While some countries in the Caribbean have made significant progress in this regard, decisive action is still required to address fiscal imbalances and high debt levels, and to provide more certainty in economic policymaking.

The discussion of economic institutions would not be complete without considering the crucial role of regional integration. However, analyzing institutions related to integration in the Caribbean goes beyond the scope of this volume. Nonetheless, special attention should be given to Caribbean integration efforts, and more specifically to the Caribbean Community and Common Market (CARICOM), which aims to serve as a custom union and to provide policy and functional cooperation (Mesquita Moreira and Mendoza 2007). CARICOM was established in 1973 with the signing of the Treaty of Chaguaramas by Barbados, Guyana, Jamaica, and Trinidad and Tobago, and its membership expanded in subsequent years. Over the years CARICOM also expanded its efforts to deepen integration, including through the creation of the CARICOM Single Market and Economy in 1989.

Integration initiatives have traditionally relied on comparative advantage, economies of scale, increased productivity, and diversification to motivate economic agents, which should result in better growth prospects

through increased extra-regional exports. Mesquita Moreira and Mendoza (2007) review economic as well as political integration efforts in the Caribbean and argue that traditional trade-related gains from integration in the region might be limited because the countries are highly open, their common market is of limited size, and they have similar factor endowments. Nevertheless, besides the traditional economic rationale for integration, other reasons for integration, such as regional security and bargaining power in international negotiations, including for trade agreements, have motivated regional agreements for small countries (Mesquita Moreira 2018). There are also political reasons for integration, especially in terms of strengthening common interests, reducing rivalries, and fostering political consensus. A domestic political argument can also be made for north-south agreements.¹ This position draws on the so-called lock-in or domestic commitment argument, which reflects the idea that trade agreements reduce the influence of domestic lobbies and therefore, improve economic policies.² In addition, the potential gains from sharing physical and social infrastructure among Caribbean countries could also be substantial.³ However, the realization of such potential requires compromising on national preferences, which has proven to be elusive.⁴ Specifically, for the Caribbean, Mesquita Moreira (2018) suggests limiting the objective to achievable goals such as a customs union that could be instrumental in negotiations to increase market access in Latin America.

In sum, the reforms needed by all Caribbean countries should not be underestimated. To place the region on a more sustainable path that spurs growth and development, many of the institutional aspects discussed in this volume require attention. Some of these elements are more urgent than others, and some of the countries have already made significant progress in implementing them. Policymakers and the various stakeholders in each of the Caribbean countries face the task of identifying the best way to move forward and determining which of the many institutions need to be strengthened. This could be challenging for small countries with already stretched capacity, but institutional reform has the potential to build resilience and foster sustainable prosperity.

¹ Such as the North America Free Trade Agreement.

² Maggi and Rodriguez-Clare (2007) show that trade agreements can be motivated by the desire of governments to commit vis-à-vis domestic lobbies.

³ The University of the West Indies is an example of sharing human and physical infrastructure for education.

⁴ For instance, not all countries have subjected themselves to the Caribbean Court of Justice, which was established as the final court of appeal.

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APPENDIXES

Appendix 1

Methodological Report for Chapter 7

This appendix describes the data sources and methodologies used to build the figures shown in the chapter. A normalization was used for all the indicators studied. The idea was to obtain a comparable index ranging between 0 and 100 applying the following expression:

$$I_c = \frac{var_c - \min(var)}{\max(var) - \min(var)},$$

where I_c is the value of the graphed indicator between 0 and 100, var_c is the value of the variable used to build the indicator at the country or group of countries, $\min(var)$ corresponds to the minimum value of the variable in the entire database, and $\max(var)$ corresponds to the maximum value of the variable observed in the entire database. After this normalization, we compared each group of countries or an individual country against the highest value of I_c , which typically corresponded to the Organisation for Economic Co-operation and Development (OECD).

Figure 7.1 uses data from the 2017/2018 Global Competitiveness Index, a measure created by the World Economic Forum (WEF) for its annual competitiveness report.¹ This report seeks to shed light on how institutional characteristics of 137 countries are related to economic growth.² The six variables used for the figure were built using the answers to the following questions from the WEF's Executive Opinion Survey:

¹ The report is available at <http://reports.weforum.org/global-competitiveness-index-2017-2018/#topic=data>.

² The index covers the following groups of countries: Rest of the small economies of the world (ROSE): Bahrain, Belize, Bhutan, Botswana, Brunei Darussalam, Cape Verde, Comoros, Cyprus, Fiji, Gabon, Lesotho, Luxembourg, Macedonia, FYR, Maldives, Malta, Mauritius, Mongolia, Montenegro, Samoa, Seychelles, São Tomé and Príncipe,

1. *Diversion of public funds is based on the question:* In your country, how common is illegal diversion of public funds to companies, individuals, or groups? [1 = very commonly occurs; 7 = never occurs]
2. *Public trust in politicians:* In your country, how do you rate the ethical standards of politicians? [1 = extremely low; 7 = extremely high]
3. *Irregular payments and bribes:* Average score across the five components of the following Executive Opinion Survey questions: In your country, how common is it for firms to make undocumented extra payments or bribes connected with:
 - 3.1 imports and exports?
 - 3.2 public utilities?
 - 3.3 annual tax payments?
 - 3.4 awarding of public contracts and licenses?
 - 3.5 obtaining favorable judicial decisions?
 In each case, the answer ranges from 1 [very common] to 7 [never occurs].
4. *Favoritism in decisions of government officials:* In your country, to what extent do government officials show favoritism to well-connected firms and individuals when deciding upon policies and contracts? [1 = show favoritism to a great extent; 7 = do not show favoritism at all]
5. *Wastefulness of government spending:* In your country, how efficient is the government in spending public revenue? [1 = extremely inefficient; 7 = extremely efficient].
6. *Transparency of government policymaking:* In your country, how easy is it for companies to obtain information about changes in government policies and regulations affecting their activities? [1 = extremely difficult; 7 = extremely easy]

Figures 7.2 and 7.3 use data from public opinion surveys. The Latin America Public Opinion Project (LAPOP) Survey, administered by

Timor-Leste, Tonga, Vanuatu, Estonia, Iceland, Latvia, Slovenia. Latin America: Argentina, Belize, Bolivia, Brazil, Chile, Colombia, Costa Rica, Dominican Republic, Ecuador, El Salvador, Guatemala, Honduras, Mexico, Nicaragua, Panama, Paraguay, Peru, Uruguay, Venezuela. OECD: Australia, Austria, Belgium, Bulgaria, Chile, Republic of Korea, Luxembourg, Mexico, Canada, Czech Republic, Denmark, Estonia, Finland, France, Germany, Greece, Hungary, Iceland, Ireland, Israel, Italy, Japan, Latvia, Netherlands, New Zealand, Norway, Poland, Portugal, Slovak Republic, Slovenia, Spain, Sweden, Switzerland, Turkey, United Kingdom, United States. Caribbean tourism-based countries (CCB-NC): The Bahamas, Barbados, Jamaica. Caribbean commodity-based economies (CCB-C): Guyana, Suriname, Trinidad and Tobago.

Vanderbilt University, was used to obtain data for The Bahamas, Barbados, Guyana, Jamaica, Suriname, and Trinidad and Tobago (2006, 2008, 2009, 2010, 2012, 2014), as well as for Latin American countries, the United States, and Canada (2004, 2006, 2007, 2008, 2010, 2012, 2014).³ The Eurobarometer (2012, 2013), a project of the European Commission,⁴ was used for OECD countries. With respect to the variables used to build the indicator studied in the figures, the LAPOP Survey question on Parliament was: To what extent do you trust the Parliament/National Congress? [1 = not at all, 7 = a lot] The Eurobarometer poses the question in a different way: Please tell me if you tend to trust in or tend not to trust in? The European Parliament [1 = tend to trust, 2 = tend not to trust]

Figure 7.3 uses the following questions to define the alignment with the party in power: From LAPOP: Who did you vote for in the last general election? From Eurobarometer: Which party would you be most likely to vote for at the European elections? After the voted party or candidate's party was obtained from these questions, we compared whether the person or party voted for was the same as the one that won the elections. Therefore, if both were the same, the individual was considered as aligned with the ruling party, and not aligned otherwise.

Figure 7.4 uses data from the 2016 Corruption Perception Index published by Transparency International.⁵ The index is the arithmetic average of the following other measures of corruption across the globe:

1. African Development Bank Governance Ratings 2015
2. Bertelsmann Foundation Sustainable Governance Indicators 2016
3. Bertelsmann Foundation Transformation Index 2016
4. Economist Intelligence Unit Country Risk Ratings 2016
5. Freedom House Nations in Transit 2016
6. Global Insight Country Risk Ratings 2015

³ The LAPOP survey is available at <https://www.vanderbilt.edu/lapop/>. The countries included in LAPOP are as follows: CCB-C: Guyana, Suriname, Trinidad and Tobago. CCB-NC: The Bahamas, Barbados, Jamaica. Latin America: Argentina, Belize, Bolivia, Brazil, Chile, Colombia, Costa Rica, Dominican Republic, Ecuador, El Salvador, Guatemala, Honduras, Mexico, Nicaragua, Panama, Paraguay, Peru, Uruguay, Venezuela.

⁴ The Eurobarometer is available at: <http://ec.europa.eu/commfrontoffice/publicopinion/index.cfm/Chart/index>. Countries included in the Eurobarometer are France, Belgium, the Netherlands, Germany, Italy, Luxembourg, Denmark, Ireland, Great Britain, Northern Ireland, Greece, Spain, Portugal, Finland, Sweden, Austria, Cyprus, Czech Republic, Estonia, Hungary, Latvia, Lithuania, Malta, Poland, Slovak Republic, Slovenia, Bulgaria, Romania, Turkey, Croatia, Macedonia (FYROM).

⁵ The index is available at https://www.transparency.org/news/feature/corruption_perceptions_index_2016.

7. Institute for Management Development World Competitiveness Yearbook 2016
8. Political and Economic Risk Consultancy Asian Intelligence 2016
9. Political Risk Services International Country Risk Guide 2016
10. World Bank Country Policy and Institutional Assessment 2015
11. World Economic Forum Executive Opinion Survey 2016
12. World Justice Project Rule of Law Index 2016
13. Varieties of Democracy Project 2016.

The process of obtaining the corruption index starts with the selection of sources, which is done based on certain criteria, including quantification of corruption in the public sector, a valid methodology, implementation of the institution's credibility and the regularity of the data collection, and variation to identify differences across countries. These measures are standardized between 0 and 100, where zero is assigned to places where the corruption is highest and 100 to the lowest. After the standard measure is built for all the sources, an average of all available sources per country/region is made.⁶

Figure 7.5 uses data from the 2016 Rule of Law Index of the World Justice Project (WJP).⁷ The index is the result of data collection from five questionnaires administered to experts on the issue and citizens in general. In terms of indicators, publicized laws and government data are the average of the following variables:

1. In practice, the local government provides easy-to-understand information on people's legal rights (criminal suspects' rights; workers' basic rights; public health issues) [Strongly Agree (1), Agree (.667), Disagree (.333), Strongly Disagree (0)]
2. In practice, the basic laws of [COUNTRY] are available in all official languages [Strongly Agree (1), Agree (.667), Disagree (.333), Strongly Disagree (0)]
3. The basic laws are publicly available in all official languages [Strongly Agree (1), Agree (.667), Disagree (.333), Strongly Disagree (0)]
4. In practice, the government strives to make the laws accessible in languages spoken by significant segments of the population,

⁶ The index is accompanied by a standard error that accounts for the variation with respect to sources.

⁷ The index is available at <https://worldjusticeproject.org/our-work/wjp-rule-law-index/wjp-rule-law-index-2016>.

- even if they are not “official” languages [Strongly Agree (1), Agree (.667), Disagree (.333), Strongly Disagree (0)]
5. In practice, national regulations are published on a timely basis (i.e., within the timelines mandated by the applicable law or regulation). [Strongly Agree (1), Agree (.667), Disagree (.333), Strongly Disagree (0)]
 6. In practice, administrative regulations can be obtained at little cost, such as by mail or online [Strongly Agree (1), Agree (.667), Disagree (.333), Strongly Disagree (0)]
 7. In practice, judicial decisions of the highest court are published on a timely basis [Strongly Agree (1), Agree (.667), Disagree (.333), Strongly Disagree (0)]
 8. In practice, drafts of legislation (bills) to be discussed in the legislative body are made available to the public on a timely basis [Strongly Agree (1), Agree (.667), Disagree (.333), Strongly Disagree (0)]
 9. In practice, legislative proceedings (e.g., bills submitted or presented to the legislature for consideration or approval) are broadcast to the public by radio or TV [Strongly Agree (1), Agree (.667), Disagree (.333), Strongly Disagree (0)]

Figure 7.6 presents information from two sources, the WEF’s 2017/2018 Global Competitiveness Index and the WJP’s 2016 Rule of Law Index.⁸ The data used from the WEF correspond to the following indicators: property rights, intellectual property protection, and strength of investors’ protection. The indicator on property rights is obtained from the following question asked by the WEF’s Executive Opinion Survey: In your country, to what extent are property rights, including financial assets, protected? [1 = not at all; 7 = to a great extent] The intellectual property protection indicator is based on the Executive Opinion Survey question: In your country, to what extent is intellectual property protected? [1 = not at all; 7 = to a great extent] With respect to the strength of investors’ protection, the WEF bases its calculations on data from the Strength of Investor Protection

⁸ The countries framed by the World Justice Project are as follows: CCB-C: Guyana, Suriname, Trinidad and Tobago. CCB-NC: The Bahamas, Barbados, Jamaica. ROSE: Belize, Botswana, Macedonia, FYR, Mongolia, Slovenia. OECD: Australia, Austria, Belgium, Canada, Chile, Czech Republic, Denmark, Estonia, Finland, France, Greece, Hungary, Italy, Japan, Mexico, Netherlands, New Zealand, Norway, Poland, Portugal, Slovenia, Spain, Sweden, Turkey, United States, United Kingdom, Republic of Korea. Latin America: Argentina, Belize, Bolivia, Brazil, Chile, Colombia, Costa Rica, Ecuador, El Salvador, Guatemala, Honduras, Mexico, Nicaragua, Panama, Uruguay, Venezuela.

Index on a 0–10 (best) scale developed by the World Bank/International Finance Corporation for the 2016 *Doing Business* report.

Data from the WJP are related to the indicator “government does not expropriate without lawful process and adequate compensation,” which is based on the average from the following questions:

1. In practice, how likely is it that homeowners receive full compensation from the government at fair market value? [Very Likely (1), Likely (.667), Unlikely (.333), Very Unlikely (0)]
2. In practice, if homeowners sue the government in court seeking compensation for the demolition of their homes, how likely is it that they receive a fair compensation? [Very Likely (1), Likely (.667), Unlikely (.333), Very Unlikely (0)]
3. In practice, when the government expropriates communal land and resources of peasants or small farmers in [COUNTRY], the farmers receive adequate compensation. [Strongly Agree (1), Agree (.667), Disagree (.333), Strongly Disagree (0)]
4. Now, please assume that the monetary compensation offered by the government for the demolition of the houses is clearly unfair and inadequate. How likely are the following outcomes? Homeowners would do nothing and resign themselves to losing the money. [Very Likely (0), Likely (.333), Unlikely (.667), Very Unlikely (1)]
5. Finally, if the homeowners sue the government, how likely is it that they obtain fair compensation in court? [Very Likely (0), Likely (.333), Unlikely (.667), Very Unlikely (1)]
6. Now, instead of using local courts, suppose that the parties agree to submit the dispute to arbitration. Suppose the arbitral panel decides that the government agency must pay the disputed amount, but despite the arbitral award, the government agency continues to refuse to pay. In practice, how likely is the contractor to be able to enforce the arbitral award against the government agency through the local courts? If the award is from a national arbitration panel. [Very Likely (0), Likely (.333), Unlikely (.667), Very Unlikely (1)]
7. Now, instead of using local courts, suppose that the parties agree to submit the dispute to arbitration. Suppose the arbitral panel decides that the government agency must pay the disputed amount, but despite the arbitral award, the government agency continues to refuse to pay. In practice, how likely is the contractor to be able to enforce the arbitral award against the government agency through the local courts? If the award is from

- an international arbitration panel. [Very Likely (1), Likely (.667), Unlikely (.333), Very Unlikely (0)]
8. In practice, when the government expropriates private investors and companies in [COUNTRY], the investors receive adequate compensation. [Strongly Agree (1), Agree (.667), Disagree (.333), Strongly Disagree (0)]
 9. In practice, when the government expropriates property, it is for legitimate public purposes and in accordance with applicable laws and procedures (“due process”). [Strongly Agree (1), Agree (.667), Disagree (.333), Strongly Disagree (0)]
 10. In practice, when the government takes measures that have effects similar to expropriation (such as unjustified interference in the uses or benefits of investments), investors receive adequate compensation. [Strongly Agree (1), Agree (.667), Disagree (.333), Strongly Disagree (0)]
 11. In practice, foreign investors receive fair and equitable treatment from the government. [Strongly Agree (1), Agree (.667), Disagree (.333), Strongly Disagree (0)]
 12. In practice, legal restrictions on foreign investment are uniformly and consistently enforced. [Strongly Agree (1), Agree (.667), Disagree (.333), Strongly Disagree (0)]
 13. In practice, intellectual property rights (trademarks, copyrights, and patents) in [COUNTRY] are effectively enforced. [Strongly Agree (1), Agree (.667), Disagree (.333), Strongly Disagree (0)]

Data from the WJP’s 2016 Rule of Law Index are used for Figure 7.7. The indicators are the following: government powers are effectively limited by the legislature, government powers are effectively limited by the judiciary, government powers are effectively limited by independent auditing and review, government officials are sanctioned for misconduct, governments are subject to nongovernmental checks, and transition of power is subject to law. The indicators are built using the following questions:

1. In practice, the chief executive (President, Prime Minister, etc.) of [COUNTRY] rules without regard to legislative checks. [Strongly Agree (1), Agree (.667), Disagree (.333), Strongly Disagree (0)]
2. In practice, the government’s power is not concentrated in one person, but is distributed among different independent branches, for instance the President or Prime Minister, the Congress or legislative body, and judges. [Strongly Agree (1), Agree (.667), Disagree (.333), Strongly Disagree (0)]

3. In practice in [COUNTRY], opposition parties can freely express opinions against government policies without fear of retaliation. [Strongly Agree (1), Agree (667), Disagree (.333), Strongly Disagree (0)]
4. In practice, opposing factions within the dominant party can freely express opinions in public without fear of facing substantial negative consequences. [Strongly Agree (1), Agree (667), Disagree (.333), Strongly Disagree (0)]
5. Please assume that one day the president decides to adopt a policy that is clearly against the [COUNTRY] Constitution: How likely is the National Congress/Parliament to be able to stop the president's illegal actions? [Very Likely (1), Likely (.667), Unlikely (.333), Very Unlikely (0)]
6. In practice, the government's power is not concentrated in one person, but is distributed among different independent branches, for instance the President or Prime Minister, the Congress or legislative body, and judges.
7. The government always obeys the decisions of the high courts, even when it disagrees with these decisions Please choose the statement that is closest to your views on how the judiciary operates in your country:
 - a. When legal questions or possible violations are raised, the judiciary reviews executive actions and uses its powers to declare government actions illegal or unconstitutional.
 - b. The judiciary reviews executive actions, but is unwilling to take on politically sensitive issues and/or is limited in its effectiveness.
 - c. The judiciary does not effectively review executive policy.
 - d. Don't know/Not applicable.
8. In practice, the national courts in [COUNTRY] are free of political influence in their application of power. [Strongly Agree (1), Agree (.667), Disagree (.333), Strongly Disagree (0)]
9. The following question aims at identifying the main problems faced by the criminal courts in [COUNTRY]. On a scale from 1 to 10 (with 10 being a very serious problem, and 1 not being a serious problem), please tell us how significant are the following problems faced by the criminal courts in the city where you live: Lack of independence of the judiciary from the government's power [Serious Problem (0), Not a Serious Problem (1)]
10. Based on your experience, out of all the cases in which the government had an interest (as a litigant or third party), in what

percentage of them did the government exercise undue influence to affect the outcome of the case?

11. In practice, the local courts in [COUNTRY] are free of political influence in their application of power. [Strongly Agree (1), Agree (.667), Disagree (.333), Strongly Disagree (0)]
12. To what extent do you agree with the following statements: In practice, the electoral appeals court is free of political influence in its application of power. [Strongly Agree (1), Agree (.667), Disagree (.333), Strongly Disagree (0)]
13. Please assume that one day the president decides to adopt a policy that is clearly against the [COUNTRY] Constitution: How likely are the courts to be able to stop the president's illegal actions? [Very Likely (1), Likely (.667), Unlikely (.333), Very Unlikely (0)]
14. In your opinion, most judges decide cases according to: What the government tells them to do/What powerful private interests tell them to do/What the law says. [Single Answer: A. What the government tells them to do (0) B. What powerful private interests tell them to do (0) C. What the law says (1)]
15. Assume that a government officer makes a decision that is clearly illegal and unfair, and people complain about this decision before the judges. In practice, how likely is that the judges are able to stop the illegal decision? [Very Likely (1), Likely (.667), Unlikely (.333), Very Unlikely (0)]
16. Please choose the statement that is closest to your views on how the supreme audit institution or comptroller operates in practice in your country: (a) The supreme audit institution is effective in investigating financial irregularities in the government. (b) The supreme audit institution starts investigations into financial irregularities, but is limited in its effectiveness, particularly in regards to politically sensitive issues. (c) The supreme audit institution does not investigate financial irregularities effectively and fails to detect offenders. (d) Don't know/Not applicable.
17. In practice, the reports issued by the government auditor (supreme audit institution, comptroller, etc.) are taken seriously by the authorities, with negative findings drawing prompt corrective action. Please choose the statement that is closest to your views on how the National Human Rights Institution (ombudsman) operates in practice in your country: (a) The institution is effective in investigating human rights violations. (b) The institution starts investigations into human rights violations, but is limited in its effectiveness. The institution may be slow or unwilling to take on

- politically sensitive issues. (c) The institution does not effectively investigate human rights violations. (d) There is no such institution in my country. (e) Don't know/Not applicable.
18. In practice, the reports issued by the National Human Rights Institution/ombudsman are taken seriously by the authorities, with negative findings drawing prompt corrective action. [Strongly Agree (1), Agree (.667), Disagree (.333), Strongly Disagree (0)]
 19. Assume that a police officer inflicts severe physical harm on a criminal suspect to obtain a confession. Assume that the criminal suspect files a formal complaint with the competent authority (prosecutor, judge, ombudsman, etc.), and provides sufficient evidence to prove his/her case. Which one of the following outcomes is most likely? (a) The accusation is completely ignored by the authorities. (b) An investigation is opened, but it never reaches any conclusions. (c) The police officer is prosecuted and punished (through fines, or time in prison). (d) Don't know/Not applicable.
 20. Assume that, as a result of an audit, a LOCAL government officer is found to be unlawfully issuing a government license for personal benefit, for example, to a construction company owned by a family member. Which one of the following outcomes is most likely? (a) The accusation is completely ignored by the authorities. (b) An investigation is opened, but it never reaches any conclusions. (c) The LOCAL government officer is prosecuted and punished (through fines, or time in prison). (d) Don't know/Not applicable.
 21. Assume that the mayor of a small town in your country is taking government money for personal benefit. Please also assume that one of his employees witnesses this conduct, reports it to the relevant authority, and provides sufficient evidence to prove it. Assume that the press obtains the information and publishes the story. Which one of the following outcomes is most likely? (a) The accusation is completely ignored by the authorities. (b) An investigation is opened, but it never reaches any conclusions. (c) The mayor is prosecuted and punished (through fines, or time in prison). (d) Don't know/Not applicable.
 22. How likely is it that a powerful or politically connected person avoids or escapes legal consequences for a non-violent criminal breach of the law? [Very Likely (0) Likely (.333) Unlikely (.667) Very Unlikely (1)]
 23. Assume that a high-ranking government officer is taking government money for personal benefit. Please also assume that one of his or her employees witnesses this conduct, reports it to the

- relevant authority, and provides sufficient evidence to prove it. Please assume that the press obtains the information and publishes the story. Which one of the following outcomes is most likely? (a) The accusation is completely ignored by the authorities. (b) An investigation is opened, but it never reaches any conclusions. (c) The high-ranking government officer is prosecuted and punished (through fines, or time in prison).
24. In practice, members of the legislature abusing their power are sanctioned for misconduct. [Strongly Agree (1), Agree (.667), Disagree (.333), Strongly Disagree (0)]
 25. In practice, members of the legislature who commit crimes are prosecuted and punished. [Strongly Agree (1), Agree (.667), Disagree (.333), Strongly Disagree (0)]
 26. In practice, members of the judiciary abusing their power are sanctioned for misconduct. [Strongly Agree (1), Agree (.667), Disagree (.333), Strongly Disagree (0)]
 27. In practice, police officers abusing their power are sanctioned for misconduct. [Strongly Agree (1), Agree (.667), Disagree (.333), Strongly Disagree (0)]
 28. In practice, police officers who commit crimes are prosecuted and punished. [Strongly Agree (1), Agree (.667), Disagree (.333), Strongly Disagree (0)]
 29. Assume that a high-ranking police officer is found by a newspaper reporter to be taking money from a criminal organization. Assume that there is enough evidence to prosecute and convict. Which of the following outcomes is most likely? (a) The accusation is completely ignored by the authorities. (b) An investigation is opened, but it never reaches any conclusions. (c) The high-ranking police officer is prosecuted and punished (through fines, or time in prison). (d) Don't know/Not applicable.
 30. Assume that a police officer inflicts severe physical harm on a criminal suspect to obtain a confession. Assume that the criminal suspect files a formal complaint with the competent authority (prosecutor, judge, ombudsman, etc.), and provides sufficient evidence to prove his/her case. Which one of the following outcomes is most likely? (a) The accusation is completely ignored by the authorities. (b) An investigation is opened, but it never reaches any conclusions. (c) The police officer is prosecuted and punished (through fines, or time in prison). (d) Don't know/Not applicable.
 31. If a police chief is found taking money from a criminal organization, such as a drug cartel or an arms smuggler, how likely is this

- officer to be sent to jail? [Very Likely (1), Likely (.667), Unlikely (.333), Very Unlikely (0)]
32. In talking to people about their local government, we often find important differences in how well the government, police, and the courts perform their jobs. Please tell me how often you would say that in [COUNTRY], if members of the police violate the law, they are punished for these violations [Always (1), Often (.667), Rarely (.333), Never (0)]
 33. How likely is a citizen to be beaten by the police, without justification, for participating in a non-violent public demonstration in [COUNTRY]? [Very Likely (0), Likely (.333), Unlikely (.667), Very Unlikely (1)]
 34. In practice, people in [COUNTRY] can freely hold public non-violent demonstrations without fear of reprisal. [Strongly Agree (1), Agree (.667), Disagree (.333), Strongly Disagree (0)]
 35. In [COUNTRY], people can freely express opinions against the government. [Strongly Agree (1), Agree (.667), Disagree (.333), Strongly Disagree (0)]
 36. In practice, the media (TV, radio, newspapers) in [COUNTRY] can freely expose cases of corruption by high-ranking government officers without fear of retaliation [Strongly Agree (1), Agree (.667), Disagree (.333), Strongly Disagree (0)]
 37. In practice, the media (TV, radio, newspapers) in [COUNTRY] can freely express opinions against government policies without fear of retaliation. [Strongly Agree (1), Agree (.667), Disagree (.333), Strongly Disagree (0)]
 38. How likely is a journalist to be attacked by the police, without justification, for covering a non-violent public demonstration in [COUNTRY]? [Strongly Agree (1), Agree (.667), Disagree (.333), Strongly Disagree (0)]
 39. How likely is the newspaper reporter to be threatened, imprisoned, or punished (either through official or unofficial means), either by the police or by the organized criminal organization? [Very Likely (0), Likely (.333), Unlikely (.667), Very Unlikely (1)]
 40. In practice in [COUNTRY], the government does not prevent citizens from accessing content published online. [Strongly Agree (1), Agree (.667), Disagree (.333), Strongly Disagree (0)]
 41. What is the likelihood that a newspaper in your country declines to run a credible exposé of corruption because of threats of violence or legal action? [Very Likely (0), Likely (.333), Unlikely (.667), Very Unlikely (1)]

42. In [COUNTRY], the media (TV, radio, newspapers) can freely expose cases of corruption by high-ranking government officers without fear of retaliation. [Strongly Agree (1), Agree (667), Disagree (.333), Strongly Disagree (0)]
43. In [COUNTRY], the media (TV, radio, newspapers) can freely express opinions against government policies and actions without fear of retaliation. [Strongly Agree (1), Agree (667), Disagree (.333), Strongly Disagree (0)]
44. In practice, civil society organizations in [COUNTRY] can freely express opinions against government policies and actions without fear of retaliation. [Strongly Agree (1), Agree (667), Disagree (.333), Strongly Disagree (0)]
45. In [COUNTRY], civil society organizations can freely express opinions against government policies and actions without fear of retaliation. [Strongly Agree (1), Agree (667), Disagree (.333), Strongly Disagree (0)]
46. In practice in [COUNTRY], opposition parties can freely express opinions against government policies without fear of retaliation. [Strongly Agree (1), Agree (667), Disagree (.333), Strongly Disagree (0)]
47. In practice, opposing factions within the dominant party can freely express opinions in public without fear of facing substantial negative consequences. [Strongly Agree (1), Agree (667), Disagree (.333), Strongly Disagree (0)]
48. In [COUNTRY], political parties can freely express opinions against government policies and actions without fear of retaliation. [Strongly Agree (1), Agree (667), Disagree (.333), Strongly Disagree (0)]
49. The chief executive (President, Prime Minister, etc.) of [COUNTRY] was elected through a clean process. [Strongly Agree (1), Agree (667), Disagree (.333), Strongly Disagree (0)]
50. In practice, in [COUNTRY], local government officials are elected through a clean process. [Strongly Agree (1), Agree (667), Disagree (.333), Strongly Disagree (0)]
51. The chief executive (President, Prime Minister, etc.) of [COUNTRY] was elected in accordance with the rules and procedures set forth in the constitution. [Strongly Agree (1), Agree (667), Disagree (.333), Strongly Disagree (0)]
52. In [COUNTRY], detailed election results are readily available for public scrutiny. [Strongly Agree (1), Agree (667), Disagree (.333), Strongly Disagree (0)]

53. In practice, proper checks and balances exist to maintain public confidence in the electoral process. [Strongly Agree (1), Agree (667), Disagree (.333), Strongly Disagree (0)]
54. In practice, in [COUNTRY], people can vote freely without feeling harassed or pressured. [Strongly Agree (1), Agree (667), Disagree (.333), Strongly Disagree (0)]
55. In practice, the electoral appeals court is free of political influence in its application of power. [Strongly Agree (1), Agree (667), Disagree (.333), Strongly Disagree (0)]
56. In [COUNTRY], local government officials are elected through a clean process. [Strongly Agree (1), Agree (667), Disagree (.333), Strongly Disagree (0)]
57. In [COUNTRY], people can vote freely without feeling harassed or pressured. [Strongly Agree (1), Agree (667), Disagree (.333), Strongly Disagree (0)]
58. Coup d'état events. Average 5 years (1: Successful coups; 0.5: Attempted, plotted or alleged coup plot; 0: None) [Successful coups (0), Attempted, plotted or alleged coup plot (0.5), None (1)]

Figure 7.8 uses data from the 2017/2018 WEF and 2016 WJP. Data from the 2017/2018 Global Competitiveness Index were used to calculate indexes on the efficiency of the legal framework in settling disputes, and protection of minority shareholders' interests. These indexes were based on the following questions:

For efficiency of the legal framework in settling disputes: In your country, how efficient are the legal and judicial systems for companies in settling disputes? [1 = extremely inefficient; 7 = extremely efficient].

For protection of minority shareholders' interests: In your country, to what extent are the interests of minority shareholders protected by the legal system? [1 = not protected at all; 7 = fully protected]

Data from the 2016 WJP correspond to the following indexes: equal treatment and absence of discrimination, freedom of opinion and expression is effectively guaranteed, freedom of assembly and association is effectively guaranteed, and fundamental labor rights are effectively guaranteed.

For equal treatment and absence of discrimination, the questions relevant for the construction of the variables are:

1. In your opinion, how likely are the following criteria to put a person at a disadvantage before a civil or commercial trial court? The person is: A poor person. [Very Likely (0), Likely (.333), Unlikely (.667), Very Unlikely (1)]

2. Imagine that a well-qualified person applies for a junior position at a government agency. In your opinion, how likely is the applicant to be at a disadvantage during the hiring process because he/she is: A poor person. [Very Likely (0), Likely (.333), Unlikely (.667), Very Unlikely (1)]
3. Imagine that a sick person seeks treatment for a disease, such as measles, at a public clinic. In your opinion, how likely is the patient to receive treatment of a lower quality than other people because he/she is: A poor person. [Very Likely (0), Likely (.333), Unlikely (.667), Very Unlikely (1)]
4. Imagine that the local police detain a person suspected of committing a crime. In your opinion, how likely is the detained person to be at a disadvantage during the criminal process because he/she is: A poor person. [Very Likely (0), Likely (.333), Unlikely (.667), Very Unlikely (1)]
5. Imagine that the local police detain two persons equally suspected of committing a crime. In your opinion, which of the following characteristics would place one of them at a disadvantage? The suspect is: A poor person. [Very Likely (0), Likely (.333), Unlikely (.667), Very Unlikely (1)]
6. In your opinion, how likely are the following criteria to put a person at a disadvantage before a civil or commercial trial court? The person is: A female. [Very Likely (0), Likely (.333), Unlikely (.667), Very Unlikely (1)]
7. Imagine that a well-qualified person applies for a junior position at a government agency. In your opinion, how likely is the applicant to be at a disadvantage during the hiring process because he/she is: A female. [Very Likely (0), Likely (.333), Unlikely (.667), Very Unlikely (1)]
8. Imagine that a sick person seeks treatment for a disease, such as measles, at a public clinic. In your opinion, how likely is the patient to receive treatment of a lower quality than other people because he/she is: A female. [Very Likely (0), Likely (.333), Unlikely (.667), Very Unlikely (1)]
9. Imagine that the local police detain a person suspected of committing a crime. In your opinion, how likely is the detained person to be at a disadvantage during the criminal process because he/she is: A female. [Very Likely (0), Likely (.333), Unlikely (.667), Very Unlikely (1)]
10. Imagine that the local police detain two persons equally suspected of committing a crime. In your opinion, which of the following characteristics would place one of them at a disadvantage? The

- suspect is: A female. [Very Likely (0), Likely (.333), Unlikely (.667), Very Unlikely (1)]
11. In your opinion, how likely are the following criteria to put a person at a disadvantage before a civil or commercial trial court? The person is: A member of an ethnic minority [Very Likely (0), Likely (.333), Unlikely (.667), Very Unlikely (1)]
 12. Imagine that a well-qualified person applies for a junior position at a government agency. In your opinion, how likely is the applicant to be at a disadvantage during the hiring process because he/she is: A member of an ethnic minority. [Very Likely (0), Likely (.333), Unlikely (.667), Very Unlikely (1)]
 13. Imagine that a sick person seeks treatment for a disease, such as measles, at a public clinic. In your opinion, how likely is the patient to receive treatment of a lower quality than other people because he/she is: A member of an ethnic minority. [Very Likely (0), Likely (.333), Unlikely (.667), Very Unlikely (1)]
 14. Imagine that the local police detain a person suspected of committing a crime. In your opinion, how likely is the detained person to be at a disadvantage during the criminal process because he/she is: A member of an ethnic minority. [Very Likely (0), Likely (.333), Unlikely (.667), Very Unlikely (1)]
 15. Imagine that the local police detain two persons equally suspected of committing a crime. In your opinion, which of the following characteristics would place one of them at a disadvantage? The suspect is: A person from an ethnic group or tribe other than that of the police officer involved. [Very Likely (0), Likely (.333), Unlikely (.667), Very Unlikely (1)]
 16. In your opinion, how likely are the following criteria to put a person at a disadvantage before a civil or commercial trial court? The person is: A member of a religious minority. [Very Likely (0), Likely (.333), Unlikely (.667), Very Unlikely (1)]
 17. Imagine that a well-qualified person applies for a junior position at a government agency. In your opinion, how likely is the applicant to be at a disadvantage during the hiring process because he/she is: A member of a religious minority. [Very Likely (0), Likely (.333), Unlikely (.667), Very Unlikely (1)]
 18. Imagine that a sick person seeks treatment for a disease, such as measles, at a public clinic. In your opinion, how likely is the patient to receive treatment of a lower quality than other people because he/she is: A member of a religious minority. [Very Likely (0), Likely (.333), Unlikely (.667), Very Unlikely (1)]

19. Imagine that the local police detain a person suspected of committing a crime. In your opinion, how likely is the detained person to be at a disadvantage during the criminal process because he/she is: A member of a religious minority. [Very Likely (0), Likely (.333), Unlikely (.667), Very Unlikely (1)]
20. Imagine that the local police detain two persons equally suspected of committing a crime. In your opinion, which of the following characteristics would place one of them at a disadvantage? The suspect is: A person from a religion other than that of the police officer involved. [Very Likely (0), Likely (.333), Unlikely (.667), Very Unlikely (1)]
21. In your opinion, how likely are the following criteria to put a person at a disadvantage before a civil or commercial trial court? The person is: A foreigner (immigrant). [Very Likely (0), Likely (.333), Unlikely (.667), Very Unlikely (1)]
22. Imagine that a well-qualified person applies for a junior position at a government agency. In your opinion, how likely is the applicant to be at a disadvantage during the hiring process because he/she is: A foreigner (immigrant). [Very Likely (0), Likely (.333), Unlikely (.667), Very Unlikely (1)]
23. Imagine that a sick person seeks treatment for a disease, such as measles, at a public clinic. In your opinion, how likely is the patient to receive treatment of a lower quality than other people because he/she is: A foreigner (immigrant). [Very Likely (0), Likely (.333), Unlikely (.667), Very Unlikely (1)]
24. Imagine that the local police detain a person suspected of committing a crime. In your opinion, how likely is the detained person to be at a disadvantage during the criminal process because he/she is: A foreigner (immigrant). [Very Likely (0), Likely (.333), Unlikely (.667), Very Unlikely (1)]
25. Imagine that the local police detain two persons equally suspected of committing a crime. In your opinion, which of the following characteristics would place one of them at a disadvantage? The suspect is: A foreigner (immigrant). [Very Likely (0), Likely (.333), Unlikely (.667), Very Unlikely (1)]
26. In your opinion, how likely are the following criteria to put a person at a disadvantage before a civil or commercial trial court? The person is: A homosexual. [Very Likely (0), Likely (.333), Unlikely (.667), Very Unlikely (1)]
27. Imagine that a well-qualified person applies for a junior position at a government agency. In your opinion, how likely is the applicant

- to be at a disadvantage during the hiring process because he/she is: A gay, lesbian, or transgender. [Very Likely (0), Likely (.333), Unlikely (.667), Very Unlikely (1)]
28. Imagine that a sick person seeks treatment for a disease, such as measles, at a public clinic. In your opinion, how likely is the patient to receive treatment of a lower quality than other people because he/she is: A gay, lesbian, or transgender. [Very Likely (0), Likely (.333), Unlikely (.667), Very Unlikely (1)]
29. Imagine that the local police detain a person suspected of committing a crime. In your opinion, how likely is the detained person to be at a disadvantage during the criminal process because he/she is: A gay, lesbian, or transgender. [Very Likely (0), Likely (.333), Unlikely (.667), Very Unlikely (1)]
30. Imagine that the local police detain two persons equally suspected of committing a crime. In your opinion, which of the following characteristics would place one of them at a disadvantage? The suspect is: A homosexual. [Very Likely (0), Likely (.333), Unlikely (.667), Very Unlikely (1)]

For freedom of opinion and expression is effectively guaranteed:

1. How likely is a citizen to be beaten by the police, without justification, for participating in a non-violent public demonstration in [COUNTRY]? [Very Likely (0), Likely (.333), Unlikely (.667), Very Unlikely (1)]
2. In practice, people in [COUNTRY] can freely hold public non-violent demonstrations without fear of reprisal. [Very Likely (0), Likely (.333), Unlikely (.667), Very Unlikely (1)]
3. In [COUNTRY], people can freely express opinions against the government. [Very Likely (0), Likely (.333), Unlikely (.667), Very Unlikely (1)]
4. In practice, the media (TV, radio, newspapers) in [COUNTRY] can freely expose cases of corruption by high-ranking government officers without fear of retaliation. [Strongly Agree (1), Agree (.667), Disagree (.333), Strongly Disagree (0)]
5. In practice, the media (TV, radio, newspapers) in [COUNTRY] can freely express opinions against government policies without fear of retaliation. [Strongly Agree (1), Agree (.667), Disagree (.333), Strongly Disagree (0)]
6. How likely is a journalist to be attacked by the police, without justification, for covering a non-violent public demonstration in

- [COUNTRY]? [Strongly Agree (1), Agree (.667), Disagree (.333), Strongly Disagree (0)]
7. How likely is the newspaper reporter to be threatened, imprisoned, or punished (either through official or unofficial means), either by the police or by the organized criminal organization? [Very Likely (0), Likely (.333), Unlikely (.667), Very Unlikely (1)]
 8. In practice in [COUNTRY], the government does not prevent citizens from accessing content published online. [Strongly Agree (1), Agree (.667), Disagree (.333), Strongly Disagree (0)]
 9. What is the likelihood that a newspaper in your country declines to run a credible exposé of corruption because of threats of violence or legal action? [Very Likely (0), Likely (.333), Unlikely (.667), Very Unlikely (1)]
 10. In [COUNTRY], the media (TV, radio, newspapers) can freely expose cases of corruption by high-ranking government officers without fear of retaliation. [Strongly Agree (1), Agree (.667), Disagree (.333), Strongly Disagree (0)]
 11. In [COUNTRY], the media (TV, radio, newspapers) can freely express opinions against government policies and actions without fear of retaliation. [Strongly Agree (1), Agree (.667), Disagree (.333), Strongly Disagree (0)]
 12. In practice, civil society organizations in [COUNTRY] can freely express opinions against government policies and actions without fear of retaliation. [Strongly Agree (1), Agree (.667), Disagree (.333), Strongly Disagree (0)]
 13. In [COUNTRY], civil society organizations can freely express opinions against government policies and actions without fear of retaliation. [Strongly Agree (1), Agree(.667), Disagree (.333), Strongly Disagree (0)]
 14. In practice in [COUNTRY], opposition parties can freely express opinions against government policies without fear of retaliation. [Strongly Agree (1), Agree (.667), Disagree (.333), Strongly Disagree (0)]
 15. In practice, opposing factions within the dominant party can freely express opinions in public without fear of facing substantial negative consequences. [Strongly Agree (1), Agree (.667), Disagree (.333), Strongly Disagree (0)]
 16. In [COUNTRY], political parties can freely express opinions against government policies and actions without fear of retaliation. [Strongly Agree (1), Agree (.667), Disagree (.333), Strongly Disagree (0)]

For freedom of assembly and association is effectively guaranteed:

1. To what extent do you agree with the following statement: In practice, civil society organizations in [COUNTRY] can freely express opinions against government policies and actions without fear of retaliations. [Strongly Agree (1), Agree (.667), Disagree (.333), Strongly Disagree (0)]
2. To what extent do you agree with the following statement: In practice, people in [COUNTRY] can freely join together with others to draw attention to an issue or sign a petition. [Strongly Agree (1), Agree (.667), Disagree (.333), Strongly Disagree (0)]
3. To what extent do you agree with the following statement: In practice, people can freely join any political organization they want. [Strongly Agree (1), Agree (.667), Disagree (.333), Strongly Disagree (0)]
4. To what extent do you agree with the following statement: In practice, people in [COUNTRY] can freely hold public nonviolent demonstrations without fear of reprisal. [Strongly Agree (1), Agree (.667), Disagree (.333), Strongly Disagree (0)]
5. In [COUNTRY], people can freely attend community meetings. [Strongly Agree (1), Agree (.667), Disagree (.333), Strongly Disagree (0)]
6. In [COUNTRY], people can freely join together with others to draw attention to an issue or sign a petition. [Strongly Agree (1), Agree (.667), Disagree (.333), Strongly Disagree (0)]
7. To what extent do you agree with the following statement: In [COUNTRY], people can freely join any (unforbidden) political organization they want [Strongly Agree (1), Agree (.667), Disagree (.333), Strongly Disagree (0)]

For fundamental labor rights are effectively guaranteed:

1. Imagine that a well-qualified person applies for a junior position at a government agency. In your opinion, how likely is the applicant to be at a disadvantage during the hiring process because he/she is: A poor person. [Very Likely (0), Likely (.333), Unlikely (.667), Very Unlikely (1)]
2. Imagine that a well-qualified person applies for a junior position at a government agency. In your opinion, how likely is the applicant to be at a disadvantage during the hiring process because he/she is: A female. [Very Likely (0), Likely (.333), Unlikely (.667), Very Unlikely (1)]

3. Imagine that a well-qualified person applies for a junior position at a government agency. In your opinion, how likely is the applicant to be at a disadvantage during the hiring process because he/she is: A member of an ethnic minority. [Very Likely (0), Likely (.333), Unlikely (.667), Very Unlikely (1)]
4. Imagine that a well-qualified person applies for a junior position at a government agency. In your opinion, how likely is the applicant to be at a disadvantage during the hiring process because he/she is: A member of a religious minority. [Very Likely (0), Likely (.333), Unlikely (.667), Very Unlikely (1)]
5. Imagine that a well-qualified person applies for a junior position at a government agency. In your opinion, how likely is the applicant to be at a disadvantage during the hiring process because he/she is: A foreigner (immigrant). [Very Likely (0), Likely (.333), Unlikely (.667), Very Unlikely (1)]
6. Imagine that a well-qualified person applies for a junior position at a government agency. In your opinion, how likely is the applicant to be at a disadvantage during the hiring process because he/she is: A gay, lesbian, or transgender. [Very Likely (0), Likely (.333), Unlikely (.667), Very Unlikely (1)]
7. Thinking about the last 12 months, have you felt discriminated against in [COUNTRY] when looking for a job, or when you're at work? [Yes (0). No (1)]
8. In practice, workers in manufacturing can effectively organize into labor unions. [Strongly Agree (1), Agree (.667), Disagree (.333), Strongly Disagree (0)]
9. In practice, workers in manufacturing can effectively bargain for their rights with their employers. [Strongly Agree (1), Agree (.667), Disagree (.333), Strongly Disagree (0)]
10. In practice, workers in manufacturing can go on strike without fear of reprisals. [Strongly Agree (1), Agree (.667), Disagree (.333), Strongly Disagree (0)]
11. In practice, workers in agriculture can effectively organize into labor unions. [Strongly Agree (1), Agree (.667), Disagree (.333), Strongly Disagree (0)]
12. In practice, workers in agriculture can effectively bargain for their rights with their employers. [Strongly Agree (1), Agree (.667), Disagree (.333), Strongly Disagree (0)]
13. In practice, workers in [COUNTRY] can freely form labor unions and bargain for their rights with their employers. [Strongly Agree (1), Agree (.667), Disagree (.333), Strongly Disagree (0)]

14. In practice, the prohibition of child labor is effectively enforced. [Strongly Agree (1), Agree (.667), Disagree (.333), Strongly Disagree (0)]
15. In practice, the prohibition of forced or compulsory labor is effectively enforced. [Strongly Agree (1), Agree (.667), Disagree (.333), Strongly Disagree (0)]

Figures 7.9 and 7.10 use data from the Latin America Public Opinion Project (LAPOP) Survey, administered by Vanderbilt University, for The Bahamas, Barbados, Guyana, Jamaica, Suriname, and Trinidad and Tobago (2006, 2008, 2009, 2010, 2012, 2014), as well as for Latin American countries, the United States, and Canada (2004, 2006, 2007, 2008, 2010, 2012, 2014). We used the Eurobarometer (2012, 2013), a project of the European Commission, for the OECD. With respect to the variables used to build the indicator studied in the figures, the LAPOP survey questions on police and justice system were the following: To what extent do you trust the police? [1 = not at all, 7 = a lot] and, To what extent do you trust the justice system? [1 = not at all, 7 = a lot]. The Eurobarometer posed the question in a different way: Please tell me if you tend to trust in or tend not to trust in: The police [1 = tend to trust, 2 = tend not to trust], and the courts [1 = tend to trust, 2 = tend not to trust].

Figure 7.11 uses information from the 2016 WJP regarding the absence of corruption in civil and criminal justice systems. The questions that WJP uses to calculate these indicators are the following:

Civil justice system:

1. In a case like this, how likely are the following people to request a bribe (or other monetary inducement) from Mr. A, Mr. B, or both, to perform their duties or to expedite the process? Court personnel. [Very Likely (0), Likely (.333), Unlikely (.667), Very Unlikely (1)]
2. The following question aims to examine the reasons why poor people in your country do not use courts to settle their disputes. Please tell us how important are the following factors in influencing people's decisions on whether or not to go to court to resolve a dispute in the city where you live: Corruption of judges and judicial officers. [Very Likely (0), Likely (.333), Unlikely (.667), Very Unlikely (1)]
3. How frequently do people (or private companies) have to pay bribes, informal payments, or other inducements to: Expedite a court process. [Very Likely (0), Likely (.333), Unlikely (.667), Very Unlikely (1)]
4. In a case like this, how likely are the following people to request a bribe (or other monetary inducement) from Mr. A, Mr. B, or both, to

- perform their duties or to expedite the process? Judge or magistrate. [Very Likely (0), Likely (.333), Unlikely (.667), Very Unlikely (1)]
5. In a case like this, how likely are the following people to request a bribe (or other monetary inducement) from Mr. A, Mr. B, or both, to perform their duties or to expedite the process? Commercial arbitrator. [Very Likely (0), Likely (.333), Unlikely (.667), Very Unlikely (1)]
 6. Please tell us how serious the following problems are in civil and commercial courts in the city where you live (10 means a very serious problem): Corruption of judges and judicial officers (they don't move the cases unless the parties bribe them). [Very Likely (0), Likely (.333), Unlikely (.667), Very Unlikely (1)]
 7. In a case like this, how likely are the following people to request a bribe (or other monetary inducement) from either party to perform their duties or to expedite the process? Labor inspector [Very Likely (0), Likely (.333), Unlikely (.667), Very Unlikely (1)]
 8. Based on your experience during the past year with civil cases between private parties decided by trial courts, what percentage of cases reflect the following outcomes: The final decision was influenced by undue pressure from one of the parties or was influenced by corruption.
 9. Based on your experience during the past year with civil cases between private parties decided by trial courts, what percentage of cases reflect the following outcomes: The final decision reflected the judges' honest evaluation of the available evidence and applicable law
 10. In your opinion, most judges decide cases according to: What the government tells them to do? What powerful private interests tell them to do? What the law says?

Criminal justice system:

1. How much influence do criminal organizations, such as drug cartels or arms smugglers, have on the policies and actions of the following institutions of your country? The military. [Very Strong Influence (0), Significant Influence (.333), Minor Influence (.667), No Influence (1)]
2. How likely are police in your country to receive bribes from criminal organizations to turn a blind eye to their illegal activities (like selling drugs on the streets)? [Very Likely (0), Likely (.333), Unlikely (.667), Very Unlikely (1)]

3. How frequently do the police officers and court officers (prosecutors, court personnel, or judges) working on criminal cases request or receive bribes or other informal payments to: Actually prosecute a criminal. [Almost Always (0), In Most Cases (.333), In Some Cases (.667), Almost Never (1)]
4. How frequently do the police officers and court officers (prosecutors, court personnel, or judges) working on criminal cases request or receive bribes or other informal payments to: Destroy or tamper with evidence. [Almost Always (0), In Most Cases (.333), In Some Cases (.667), Almost Never (1)]
5. How much influence do criminal organizations, such as drug cartels or arms smugglers, have on the policies and actions of the following institutions of your country? The police. [Very Strong Influence (0), Significant Influence (.333), Minor Influence (.667), No Influence (1)]
6. How likely are local police officers to collect bribes from traders and small merchants so that they can carry on their activity? [Very Likely (0), Likely (.333), Unlikely (.667), Very Unlikely (1)]
7. How frequently do the police officers and court officers (prosecutors, court personnel, or judges) working on criminal cases request or receive bribes or other informal payments to: Actually investigate a crime. [Almost Always (0), In Most Cases (.333), In Some Cases (.667), Almost Never (1)]
8. How frequently do the police officers and court officers (prosecutors, court personnel, or judges) working on criminal cases request or receive bribes or other informal payments to: Drop charges or grant a bail. [Almost Always (0), In Most Cases (.333), In Some Cases (.667), Almost Never (1)]
9. How frequently do the police officers and court officers (prosecutors, court personnel, or judges) working on criminal cases request or receive bribes or other informal payments to: Expedite court processes. [Almost Always (0), In Most Cases (.333), In Some Cases (.667), Almost Never (1)]
10. The following question aims at identifying the main problems faced by the criminal investigation system in your country. On a scale from 1 to 10 (with 10 meaning a very serious problem, and 1 meaning not a serious problem), please tell us how significant the following problems are for the criminal investigative services (prosecutors, investigators, judicial police officers, etc.) in the city where you live: Corruption of investigators or judicial police [Serious Problem (0), Not a Serious Problem (1)]

11. Corruption exists in all countries and societies in some form or the other. How many of the following people in [COUNTRY] do you think are involved in corrupt practices, or haven't you heard enough about them to say? The police [None (1), Some (.667), Most (.333), All (0)]
12. Do people in your neighborhood have to pay a bribe or other inducements for the following procedures or actions: To receive the services of the police. [Yes (0), No (1)]
13. The following question aims at identifying the main problems faced by the criminal investigation system in your country. On a scale from 1 to 10 (with 10 meaning a very serious problem, and 1 meaning not a serious problem), please tell us how significant the following problems are for criminal investigative services (prosecutors, investigators, judicial police officers, etc.) in the city where you live: Corruption of prosecutors. [Serious Problem (0), Not a Serious Problem (1)]
14. During the past three years, have you or anyone living in your household been stopped or detained by the police?
15. Did you (or the person living in your household) have to pay a bribe to the police officer to avoid a problem (like passing a checkpoint or avoiding a fine or arrest)? [Yes (0), No (1)]
16. The following question aims at identifying the main problems faced by the criminal courts in your country. On a scale from 1 to 10 (with 10 being a very serious problem, and 1 being not a serious problem), please tell us how significant are the following problems faced by the criminal courts in the city where you live: Corruption of judges and judicial officers (they don't move the cases unless the parties bribe them). [Serious Problem (0), Not a Serious Problem (1)]
17. Corruption exists in all countries and societies in some form or the other. How many of the following people in [COUNTRY] do you think are involved in corrupt practices, or haven't you heard enough about them to say: Judges and Magistrates. [percent]
18. How much influence do criminal organizations, such as drug cartels or arms smugglers, have on the policies and actions of the following institutions of your country: Members of the courts. [Very Strong Influence (0), Significant Influence (.333), Minor Influence (.667), No Influence (1)]
19. Based on your experience with criminal cases decided by trial courts during the previous year, in approximately what percentage of cases showed that: The final decision was influenced by undue pressure or corruption.

20. In your opinion, most judges decide cases according to: What the government tells them to do? What powerful private interests tell them to do? What the law says?

Figure 7.12 uses the information from the 2016 WJP on the timeliness of civil justice, which is defined as the average of the following questions:

1. In practice, how long would it take to obtain a decision, or a judgment—starting from the moment the case is filed to the moment a decision or agreement is reached—if Mr. B uses the following mechanisms? Small claims court or magistrate. [Less than a month (1), Between one month and 1 year (.75), Between 1 and 3 years (.5), More than 3 years (.25), More than 5 years (0)]
2. In practice, how long would it take to obtain a decision, or a judgment—starting from the moment the case is filed to the moment a decision or agreement is reached—if Mr. B uses the following mechanisms? Regular civil or commercial court lawsuit. [Less than a month (1), Between one month and 1 year (.75), Between 1 and 3 years (.5), More than 3 years (.25), More than 5 years (0)]
3. How long would it take in practice to decide and enforce the case in local courts, starting from the time of initially filing the case to actual payment? [Less than a month (1), Between one month and 1 year (.75), Between 1 and 3 years (.5), More than 3 years (.25), More than 5 years (0)]
4. Please tell us how serious the following problems are in civil and commercial courts in the city where you live (10 means a very serious problem): Duration of cases (they take too much time). [Serious Problem (0), Not a Serious Problem (1)]
5. The following question aims to examine the reasons why poor people in your country do not use courts to settle their disputes. Please tell us how important are the following factors in influencing people's decisions on whether or not to go to court to resolve a dispute in the city where you live: Duration of cases (they take too much time). [Very Important (0), Somewhat important (.333), Not Very Important (.667), Not Important at all (1)]

The information for Figure 7.13 is obtained from the WEF's 2017/2018 Global Competitiveness Index based on the questions below.

In your country, how do you assess the quality of primary education? [1 = Extremely poor—among the worst in the world; 7 = Excellent—among the best in the world]

The primary, secondary, and tertiary education enrollment reported by the WEF is obtained from UNESCO, *Education at a Glance 2016*, and from national sources. The questions implemented for the indicators for the quality of the education system, math and science education, and management of schools were as follows: In your country, how well does the education system meet the needs of a competitive economy? [1 = Not well at all; 7 = Extremely well] In your country, how do you assess the quality of math and science education? [1 = Extremely poor—among the worst in the world; 7 = Excellent—among the best in the world] In your country, how do you assess the quality of business schools? [1 = Extremely poor—among the worst in the world; 7 = Excellent—among the best in the world]

Figure 7.14 uses information from the WEF's 2017/2018 Global Competitiveness Index and from the World Bank's World Development Indicators on infant mortality and life expectancy.

Appendix 2

Methodological Note on the Fiscal Scenarios Used in Chapter 8

Section 8.1.3 of Chapter 8 provided scenarios based on a model that links the public sector deficit to GDP growth and terms of trade, adjusted for the presence of an IMF program if relevant. Two scenarios are built for each country through 2025. The scenarios assume either constant terms of trade or an average fall of 10 percent. The calculations should be viewed as broad estimates, on the assumption that policies remain as they were during the observed years (1997–2016). The scenarios are based on two building blocks: (1) the estimated growth of GDP derived from the Centennial Group world growth model (Kohli 2017); and (2) data on revenue and expenditure for the individual countries based on the observed behavior from the early 1990s to 2016.¹

Econometric analysis is used to estimate the relationship between both public expenditure and revenue with GDP and terms of trade for each country, adjusted for the presence of an adjustment (IMF) program as a dummy variable, when relevant. The historical data for these variables for the different countries from the early 1990s to 2016 are used as a basis to develop two scenarios for the period through 2025: (1) a scenario based on no change in the terms of trade after 2016, and (2) a scenario based on an average decline of 10 percent in the terms of trade for the period of the projection. As indicated above, the scenarios are of a general and thus tentative nature.

The equations used are:

$$\text{Log } E_t = A + B \log \text{GDP}_t + C \log \text{TT}_t + P_t \quad (\text{A2.1})$$

$$\text{Log } R_t = A^* + B^* \log \text{GDP}_t + C^* \log \text{TT}_t + P_t \quad (\text{A2.2})$$

¹ Data from 1991 were used for The Bahamas, from 1994 for Barbados, from 1997 for Guyana, from 1996 for Jamaica, from 1990 for Suriname, and from 1988 for Trinidad and Tobago.

Equations (A2.1) and (A2.2) indicate that expenditure (E) and revenue (R) are functions of GDP and terms of trade (TT). P takes a value of 1 if a program with the IMF is present, and 0 otherwise.

Table A2.1 shows the key coefficients for the six countries. Results are mixed but the explanatory power of most variables (16 out of 24) is significant and evenly distributed. Based on these results, the figures in the text depict the trajectories of the fiscal deficits for the period through 2025, under the two scenarios mentioned earlier.

Table A2.1 Public Expenditure and Revenue Regression Results

Country	The Bahamas	Barbados	Guyana	Jamaica	Suriname	Trinidad & Tobago
Expenditure						
Intercept	3.6	0.7	2.6	0.2	1.3	2.0
GDP	0.2*	1.0	0.2	0.9	0.2	0.1*
Terms of trade	-1.0	-0.3*	-0.5	-0.02	0.1*	-0.03*
Dummy variable	n.a.	0.04	n.a.	-0.1	n.a.	n.a.
R ²	0.33	0.72	0.49	0.43	0.24	0.04
Revenue						
Intercept	2.9	1.9	2.2	-0.1	1.2	1.5
GDP	0.1*	0.3	0.2	1.0	0.2	-0.1*
Terms of trade	-0.6	-0.3	-0.3	0.04*	0.2	0.4
Dummy variable	n.a.	0.03	n.a.	0.0007	n.a.	n.a.
R ²	0.24	0.65	0.43	0.52	0.28	0.21

Sources: International Monetary Fund and the Centennial Group.

Notes: n.a.: not applicable.

* Low T and high P value.

Appendix 3

Public Financial Management Processes and Systems in the Caribbean Countries¹

The Bahamas

Until the onset of the global recession, The Bahamas budgeted fairly cautiously, with relatively small overall deficits, and the burden of debt not growing significantly. Only modest increases in the overall budget from one year to the next could be afforded, and the sectoral pattern of expenditure did not change much over time. The effect of the recession has been to reduce revenues considerably, particularly import duties. In these circumstances the government has sought to contain the growth of expenditure while avoiding redundancies among its workforce, while continuing with public infrastructure investments in order minimize increases in unemployment. The consequence has been a rapid escalation of the fiscal deficit and a sharp rise in debt as a proportion of GDP and in relation to the revenue needed for its future service.

This fiscal deterioration suggests the need for increased emphasis on improving the processes of policy, planning and budget execution, supported by fiscal discipline. Important weaknesses in the Bahamian Public Financial Management system undermine the integrity of financial reporting and spending quality. Moreover, capital budgeting is not fully integrated into the annual budget planning process and there is no legal framework for monitoring and facilitating the implementation of policy priorities. While the authorities have taken steps to modernize public financial management processes and systems, further efforts are needed to improve fiscal reporting and expenditure discipline. Completion of the National Development Plan should help strengthen the public financial management framework.

¹ Based on IMF Article IV consultations and other staff reports, IDB loan documents, public financial management, and published PEFA reviews.

The revenue base is small, and failures to maximize collections due to poor systems, slack administration, and a weak approach to enforcement mean that service levels cannot reach the standard they might otherwise achieve. Weaknesses in the salary and general expenditure payments systems mean there is no assurance that money is spent appropriately. Meanwhile instances of fraud and speculation go undetected and unpunished. Even when auditors report problems, they are ignored without explanation or justification, leading to the probability that the losses and poor value for money will continue.

The paragraphs that follow briefly summarize the assessment and key findings regarding the country's public financial management performance.

Credibility of the budget. Actual performance matched the overall budget fairly closely, but there have been variances in the mix of expenditure, which reached almost 10 percent of the original budget.

Comprehensiveness and transparency. The budget's presentation across departments and ministries does not provide a clear picture of sectoral spending, although most of the necessary information is provided in the budget documentation. By contrast, information about extra-budgetary expenditure is incomplete, while that on state-owned enterprises and local governments is inconsistent.

Predictability and control in budget execution. Weak tax administration and enforcement are reflected in significant tax arrears and poor levels of compliance. Expenditures are planned with some certainty as a result of the release of funds twice a year. Payroll and personnel systems are not integrated, and the division of duties between the Public Service Department and the Treasury hampers the former's ability to control the pay and grading of staff. Numerous audits have shown that there is no strong commitment to procurement through open tendering, despite clearly documented rules governing non-salary expenditure aimed at ensuring that integrity and value for money are achieved. It is not clear that internal auditors have adequate resources to achieve their objectives.

Accounting, recording, and reporting. Annual financial statements (completed around 12 months after the end of the year) do not meet international standards in terms of presentation or disclosure and fail to provide an understandable statement of the overall financial health of public finances and cash flow. There are problems with reconciliations and dormant cash-book balances that have no corresponding bank account balance. While

the auditor has repeatedly highlighted weaknesses and breaches of the rules, there has been no effort to establish robust controls, reflecting lack of accountability and low regard for the auditor's role and opinion.

External scrutiny and audit. While the auditor general prepares his audit report on the accounts some six months after receiving them, line ministries do not respond to the reports nor agree to implement the recommendations. Similarly, the National Assembly does not follow through on the auditor general's recommendations. There is no assessment of the significance of any errors and the need to correct them.

Barbados

The paragraphs that follow briefly summarize the assessment and key findings regarding the country's public financial management performance.

Budget credibility. Actual expenditure traditionally followed the budget, but a gap emerged after 2006. In the face of the Great Recession, revenue shortfalls and expenditure increases went well beyond budgetary guidelines. But these problems continued due to slow growth and defective policy implementation. More recently, the pace of expenditure has been curtailed and revenue increased, but doubts remain about the predictability of the budget.

In August 2016, IMF staff estimated that central government arrears had risen to almost 6 percent of GDP at end-FY 2015–2016, including arrears to the National Insurance Scheme (NIS). In addition, the arrears of state-owned enterprises are estimated to have risen to 5.5 percent of GDP, mostly involving arrears to the Revenue Authority and the NIS.

Comprehensiveness and transparency. The budget presents detailed program breakdowns, and detailed economic classifications. A functional presentation covers only current expenditure, with total capital expenditure reported in annual Financial Statements. This makes comparisons over time difficult. Revenue estimates are presented in detail to Parliament, but do not include the impact of changes in policy. Debt information is also presented in detail, but it excludes government guarantees; there is no general data about government financial assets. Available information on public accounts is difficult to use when assessing budgetary developments.

Statutory bodies do not observe the required presentation of budget estimates and audited accounts. Moreover, their detailed expenditure and revenue accounts, other than the transfers from the budget, are not

subject to supervision, and their financial reporting is delayed or incomplete. Thus the risks faced by the central government associated with their operations are difficult to assess.

Policy-based budgeting. Budget preparation follows well-established procedures. Most ministries are required to provide detailed projections of their budgets for two years, in the same format as the budget; the projections for the second year serve as the baseline for the preparation of the budget for that year. The Ministry of Finance puts together the budget, and following Cabinet approval, the document is submitted to Parliament. The Ministry of Finance may make changes to the budget without consultation with the affected units.

Predictability and control in budget execution. The tax system is well established, and individual taxpayer's liabilities are reasonably clear. In general, the effective tax is low, and in addition, the minister of finance has wide discretion to grant exemptions. In disputed cases concerning the value-added tax and income taxes, taxpayers can appeal to an independent advisory tribunal, which advises the minister of finance. The planned merger of the semi-autonomous Central Revenue Authority with the Customs Authority has been delayed. Financial controllers in each ministry conduct a certain amount of internal audits but with limited capabilities.

The Ministry of Finance releases quarterly expenditure funds on the basis of monthly cash requirements forecast by ministries. Procurement is largely governed by rules established in 1971. Records are inadequate to determine the value of contracts granted by tenders and those without effective competition.

Accounting, recording, and reporting. The Treasury's account at the Central Bank of Barbados is reconciled daily, and the differences are trivial. However, reconciling the Treasury's main accounts at commercial banks, and of special accounts where the Treasury holds balances on behalf of ministries, is more difficult. Monthly budget execution reports are prepared regularly and sent to Parliament within about four months; these reports are then made available to the public.

External scrutiny and audit. The auditor general audits the entire central government, while independent private auditors audit statutory bodies; these audits are then submitted to the Audit Office for transmission to Parliament. The auditor general also publishes reports on particular topics such as investment projects or the performance of statutory bodies. The

annual report on the government's financial statements is often delayed and incomplete because of understaffing. In addition, parliamentary scrutiny of budget proposals is relatively limited, in part because of the narrow room for modifications. The parliamentary commission has made limited progress in reviewing and making recommendations on the auditor general's reports.

Guyana

Guyana has made major strides toward improving and enhancing its systems. The government enacted new laws were to address systemic weaknesses and close loopholes; introduced a new computerized accounting system designed to interconnect the entire government; consolidated and fortified the budget process; and prepared and incorporated into the budgets a five-year rolling Public Sector Investment Programme consistent with Poverty Reduction Strategy Paper objectives and debt sustainability analysis. Guyana scored well in performance indicators that pertained to the existence of systems compliance with statutes, but scored relatively lower with regard to internal controls, internal audit, and oversight.

The quality of Guyana's institutions and governance framework is weak. Concerns include high perceptions of corruption and favoritism in decision-making; lack of public trust in politicians, the police, and the justice system; lack of transparency and accountability as it relates to public finances and the operations of state-owned enterprises; and the prevalence of data gaps, particularly for administrative-type data and micro-level data, which makes evidence-based decision-making difficult for both private and public sector entities. Further, institutional bureaucracy and/or outdated administrative systems hinder the private sector's ability to access public goods, and thus create incentives for graft and corruption.² Transparency International's Corruption Perception Index ranked Guyana 108th out of 176 countries in 2016 (Transparency International 2017). The World Economic Forum's 2015/2016 Global Competitiveness Index shows that the strength of auditing and reporting standards is still weak.

The following paragraphs briefly summarize the assessment and key findings regarding the country's public financial management performance, based on the Public Financial Management Performance Measurement Framework following the PEFA methodology.

² Guyana's Corruption Perception Index score is 30 out of 100 (Transparency International 2017). This score is lower than the average for commodity-dependent small economies in the rest of the world and is the lowest among Caribbean countries.

There are some fundamental weaknesses associated with implementation of the *public financial management legal and regulatory frameworks*, and with the sequence of the transition to a more formal and structured programmatic and results-based system. This is being carried out in a somewhat fragmented and unsynchronized manner, without consolidating some basic elements of public financial management reforms before implementing the subsequent stages. In particular, the implementation of common internal control and audit frameworks, and the unification of the current and capital budgets, were needed prior to moving toward a programmatic and results-based approach, which requires increased levels of delegation, flexibility, and management accountability.

Many areas of *budget formulation and implementation* have improved, including the timeliness of budget preparation, its comprehensiveness, reporting, and cash and debt management. However, outturns of expenditures and revenues continue to exceed planned amounts by 10 percent and 8 percent, respectively. Some of the excess expenditure was due to emergency spending, signaling the need for ceilings for line ministries and agencies at the outset of budget preparation. Extra-budgetary spending and arrears remain an issue.

Government current and capital expenditures follow different classification systems, and local and central governments have different expenditure classifications. While the budget is very comprehensive and includes all required information with the exception of financial statements, extra-budgetary expenditures and a number of statutory bodies receiving royalties are under-reported. Budget allocations and transfers from the central government to subnational governments follow a set of criteria and rules, but there is no consolidation of fiscal accounts by sector. Effective oversight of aggregate fiscal risk is impeded by significant delays in the submission of financial statements to the auditor general. While all key budget reports are prepared, public access and financial information are rather limited.

Predictability and control of *budget execution* is poor. Lack of effective tax revenue forecasting tools, enforcement capacity to apply penalties, and follow-up of delinquencies render the system voluntary. Audits are not planned on the basis of a risk assessment, undermining their overall effectiveness. Effective internal controls linked to a comprehensive framework of management responsibility in budget execution are non-existent. Lack of planning on non-donor-financed procurement, lack of integration with budget planning and financial management systems, prevalent use of non-competitive tendering on locally financed procurement, lack of qualified procurement staff, insufficient information on procurement processes,

and lack of internal control and internal audits produce a system with poor functional capacity. A simplified budgetary process for public procurement by individual agencies was recently introduced that brings flexibility but risks compromising project evaluation and internal controls.

Accounting, recording, and reporting improved with the adoption of the Integrated Financial Management and Accounting System (IFMAS), though some areas of concern remain. The next step is to attain real-time connectivity among all government agencies and to ensure that there are sufficient resources and staffing to make IFMAS operations sustainable.

Parliamentary involvement in budget preparation comes late, lacks time for real analysis, and may not be able to contribute to the content and quality of the budget. Parliamentary oversight of external audit and budget execution experiences significant delays. Although the Audit Office of Guyana made progress in modernizing its audit methods and standards, it lacks qualified audit staff.

Jamaica

The following paragraphs briefly summarize the assessment and key findings regarding the country's public financial management performance, reflecting in large part the findings of the IMF, as described in its Staff Report for the 2016 Article IV Consultation (IMF 2016), and subsequent IMF documents.

In recent years Jamaica has made significant progress in correcting its *public finances*, including through a strengthening of its institutional and legal framework for fiscal policy formulation and execution. Two successive IMF-supported programs that started in 2013 and extend to 2019 are helping this process, and have averted a severe fiscal and balance of payments crisis. The authorities have carried out important policy actions to increase the credibility of the reform program after repeated reform failures.

Tax incentives and discretionary waivers were significantly reduced and replaced with a rules-based and transparent framework. Tax administration was improved through capacity-building in the Large Taxpayers' Office (LTO), better compliance supported by the publication of a National Compliance Plan, and enhanced tracking of goods in customs within international best practices, according to individual country circumstances. In the area of public financial management, a comprehensive plan has been created to expand the Treasury Single Account.

A key reform of the Tax Administration of Jamaica (TAJ) has been the strengthening of the LTO, which yields half of total corporate income

tax (CIT) revenue. Significant improvements have been introduced in the context of the reform program, including (1) capacity improvement and amendments to the *Revenue Administration Act*, which have allowed the TAJ to require third-party information to cross-check taxpayers' information and activities, and to require mandatory e-filing for LTO clients for main tax types including the general consumption tax (GCT) and the CIT; (2) a National Compliance Plan, with performance indicators to improve compliance measurement; and (3) enabling the TAJ to collect outstanding arrears and seize and sell taxpayers' property.

Customs administration reforms have focused on capacity strengthening, with the hiring of new auditors for the Post-Clearance Audit Unit and implementation of the ASYCUDA World software, which has helped strengthen the tracking of imports and exports. The Jamaica Customs Agency and the TAJ are transitioning into full executive agency status and semi-autonomous revenue agency, respectively, which will lower costs and enhance efficiency.

With these reforms, *budget credibility* has generally improved in terms of aggregate budgeted expenditure and outcome, reflecting tight budgetary guidelines. However, significant modifications exist in expenditure composition. Revenue outcomes had tended to lag budget projections, although performance has improved more recently. Parliamentary oversight is impaired by the timing of the submissions of expenditure estimates and revenue, and because the submissions are debated independently from one another. Further, the relevant legislative committees have had serious capacity constraints to conduct the required analysis.

Information in budget documents is comprehensive, and budget classification is broadly compatible with international standards. The extensive budget documentation includes a complete series of economic and financial information, but could be simplified. The budget reflects government policy, and progress has been made through the introduction of medium-term fiscal forecasts. The process of integrating sector plans and recurrent and capital expenditure budgets appears to be solid.

External audit reports are generally submitted to the legislature in a timely manner, as required by law. The scope of these reports has significantly increased, and although this allows in principle for broader and deeper scrutiny, it requires a significant step up in terms of capacity of the auditing bodies. Reports from the auditor general, the accountant general, and the internal audit units have indicated recurrent events of non-compliance with rules on financial management and procurement. Follow-up has taken place, but there seems to be no systemic approach to address recurrent weaknesses in the public financial management system.

A recent IMF analysis shows that Jamaica's GCT collections could be higher by as much as 2 percentage points of GDP if compliance were improved by 5 percent. These shortfalls from potential, while sizable, have been declining in recent years due to the ongoing reform efforts, but further actions to strengthen compliance are needed. Similarly, reforms to address inaccurate taxpayer data, low on-time filing and payment rates, delays in the payment of refunds, and low quality of audits need to be implemented. In terms of *tax policy*, a continued broadening of the GCT base may reduce tax avoidance problems, as exemption loopholes are closed.

Improvements in public financial management are enhancing management of *domestic arrears*. The new organizational structure of the Accountant General Department aids in the department's transition to becoming a modern treasury and enhancing its capacity. The ongoing expansion of the Treasury Single Account at the Bank of Jamaica will soon make it the only operational account in the public sector, providing a unified view of the government's cash position. Reviewing legal provisions for all revenues to be paid into the Consolidated Fund and making improvements in accounting and fiscal reporting are important steps in this direction.

Suriname

In Suriname, fiscal discipline is a result of an annual exercise on debt sustainability analysis, good quality debt data, and solid legislation to contract debt. However, lack of unification of the budget processes likely affects fiscal discipline. In general, the strategic allocation of resources is supported by a comprehensive budget document and by a good budget preparation process. It is also supported by good quality intra-year budget execution reports and by fair parliamentary control (the draft budget law). Important improvements have been made in the public financial management processes in recent years, and further progress is expected once the new Integrated Financial Management Information System (IFMIS) is fully implemented.

Since 2011, the IDB has been working very closely with Suriname to implement reforms to develop the tools and framework critical to update the country's public expenditure and revenue systems. An IDB loan approved in 2017 seeks to strengthen the institutional capacity of the Ministry of Finance to collect tax revenue in an efficient manner and strengthen the planning, prioritization, preparation, execution, and monitoring of the annual budget, including implementation of public investment projects. The reforms are expected to provide the government with the resources to carry out priority public investments and to provide taxpayers better support to fulfil their tax obligations.

The following paragraphs briefly describe the assessment and key problems regarding the country's public financial management performance, in line with the Public Financial Management Performance Measurement Framework methodology.

The overall *credibility of the budget* of Suriname in the past was greatly weakened by large discrepancies between budgeted and actual expenditures and revenue, and by poor (or non-existent) data on expenditure arrears and extra-budgetary operations. Moreover, non-government entities were able to collect service charges, fees, and tariffs that are extra-budgetary operations, and that are spent with minimal supervision by the central government. More recently, the government, in its budgeting process, has made explicit the discrepancies between budgeted and actual expenditure in order to allow for transparency and policy analysis.

In the more recent past there has been considerable effort in terms of budget classification, and to enhance the overview of extra-budgetary funds and key autonomous agencies, although public disclosure of key fiscal information was delayed. The budget is now more comprehensive than in the past, the budgetary classification structure follows best practices, and data on central government operations are published on the Internet. Main autonomous agencies and state-owned enterprises are reporting their budget execution, but not at the subnational level.

Helped by recommendations from the IDB and international organizations and by the 2016 program supported by the IMF, *budget preparation* is of good quality, having been centralized by the Ministry of Finance with the support of the Council of Ministers on the basis of clear reporting instructions. However, the budget tends to be approved well into the fiscal year to which it applies. A medium-term fiscal framework for a five-year rolling period is prepared and updated semi-annually. Public debt sustainability analysis is conducted annually. However, recurrent and investment expenditures are not fully coordinated, even within the medium-term framework.

Tax legislation and procedures are comprehensive and clear, although questions arise about the consistency of implementation. Access to information on tax liabilities and procedures is easily available, with few exceptions. Compliance is low and non-compliance is generally unpunished. An appeal body was established in 2015.

The government now has available weekly data of revenue and expenditure, and the government has made progress in establishing a Treasury Single Account. A draft public procurement law has been prepared, with assistance from the IDB, aimed at making the system more effective and transparent. Systematic procurement information is provided to the public,

but procedures are not clear about non-competitive bidding. *Internal audit* is carried out well in line with professional standards. Expenditure commitment control procedures limit amounts to approved budget allocations, but only within the central government.

Bank accounts of the central government are reconciled, in line with the efforts to move to a Single Treasury Account. Reconciliation at the aggregate and detailed levels takes place monthly and annually with only limited discrepancies. Intra-year budget execution reports are prepared quarterly or more frequently and issued within four weeks after the end of the period. There are some concerns about the accuracy of information used in the reports, but the coverage is ample and does not fundamentally undermine the reports' usefulness. Even with good progress in consolidating accounts made so far, however, there are still separate statements for each ministry.

Final statements are submitted to the Supreme Audit Institution (SAI) for *external audit*, but with considerable delay (more than a year after the end of the fiscal year). The SAI usually presents its Annual Audit Report to the legislature according to the constitution. There is little evidence of response or follow-up on audit recommendations, but this may change with the adoption in 2016 of new audit legislation more in line with best practices.

The National Assembly reviews all budget proposals according to established procedures, but late in the budget year. Intra-year amendments to the budget are subject to precise rules and regulations and require the presentation of a supplementary budget, but this has not been implemented consistently. Fiscal discipline is a result of an annual exercise on debt sustainability analysis, good quality debt data, and solid legislation to contract debt. However, the lack of unification of budget processes likely affects fiscal discipline. In general, the strategic allocation of resources is supported by a comprehensive budget document and by a good budget preparation process. It is also supported by good quality in-year budget execution reports and by fair parliamentary control (the draft budget law). Important improvements have been made in the public financial management processes in recent years, and further progress is expected once the new IFMIS is fully implemented.

Trinidad and Tobago

When viewed from the perspective of the three main objectives of a sound public financial management system—namely, aggregate fiscal discipline, strategic allocation of resources, and the efficient delivery of services—Trinidad and Tobago performs well with respect to fiscal discipline.

The public financial management systems demonstrate some capacity for allocating resources in accordance with priorities (front end), but challenges remain regarding how effective the expenditure is (back end). The utilization of a multi-year fiscal framework (derived from the IMF Article IV consultation forecasts) facilitates a meaningful participation by ministries. Together with sound cash and debt management, the achievement of predictable budget releases, and effective payroll management, this points to efficient delivery of services. However, these positives are adversely impacted by the absence of cabinet-approved ceilings at the beginning of the budget formulation cycle, weaknesses in procurement management, and the lack of financial feedback at the end of the service delivery cycle.

There are two main factors that color the public financial management of the central government:

- The employment of manual non-salary expenditure control and accounting systems introduces some delay in reconciliation and reporting, although this does not seem to compromise quality or basic effectiveness other than discouraging reporting on expenditure arrears.
- The constrained role of Parliament in budgetary oversight, given the one-day-a-week attendance of parliamentarians and the number of parliamentarians who are members of government.

The following paragraphs briefly summarize the assessment and key findings regarding the country's public financial management performance, based on the Public Financial Management Performance Measurement Framework, following the PEFA methodology.

Credibility of the budget. Given that high volatility affects a large proportion of revenues (those from oil and gas), the Budget Division employs an intentionally conservative approach for its estimates. The evidence suggests that during the recent oil boom, excess revenue over the budget estimate was channelled principally to debt reduction and investment in the Heritage and Stabilization Fund. More recently, following the unexpected collapse of oil prices, revenue outturns fell short of budget estimates. Aggregate expenditure outturns match the budget estimates quite closely, suggesting a strong coupling between the budget formulation and preparation process, and in turn between the budget estimate and implementation. This also reflects a measure of fiscal discipline and effective cash and debt management as well as sound salary management. Managing and tracking of expenditure arrears are good, although the

budget releases are not fully aligned with the votes because largely effective commitment control procedures are occasionally bypassed. There is some indication that informal procedures are used to procure goods and services, leading to significant levels of unreported expenditure arrears, which are impossible to quantify. The budget release is predictable.

The public financial management systems effectively address fiscal risk vis-à-vis the Consolidated Fund due to unforeseen expenditure burdens arising out of subnational government loans or public enterprise bailouts. Nevertheless, significant extra-budgetary activities and poor monitoring of fiscal risk, debt, and contingent liabilities can undermine budget credibility. Similarly, the lack of a standard for budget estimates related to projects funded by development partners adversely impacts budget credibility.

Comprehensiveness and transparency. Fiscal forecasts are realistic and debt management is based on a debt management strategy with accurate and timely reporting and monitoring of the debt stock. The Central Bank of Trinidad and Tobago typically performs debt sustainability analysis on an annual basis. Budget documentation is complete, comprehensible, and comprehensive. It includes macroeconomic assumptions, the fiscal balance, financing, debt profile and status, financial assets, historical budget, and clear explanations on the impact of any major revenue and expenditure policy initiatives.

The standards for budget formulation and execution are based on economic and administrative budget classifications (Government Finance Statistics/Classification of the Functions of Government). Budget documentation includes a table that segregates expenditure according to functional classifications, although budget execution and financial reporting remain an economic and administrative classification. The chart of accounts is consistent with such classification.

All revenue generated by departments is transferred to the Consolidated Fund, which operates as a Treasury Single Account, and almost all expenditure is made through a centralized payments system. The Ministry of Finance oversees revenue and expenditure transactions through daily bank reconciliations, and monitors the plans and financial management of public entities. The consolidation of financial reports includes reconciliation between sources and uses of funds, ensuring no significant extra-budgetary funds outside development partner funds.

The vertical and horizontal allocation of resources to subnational governments follows a transparent system, which incorporates parliamentary oversight. The budget releases to subnational government entities are

timely and fully predictable. There is a fairly careful and comprehensive risk assessment of the operations of state-owned enterprises, but not all major public enterprises are complying fully with the Investment Division's financial reporting requirements. Timely and regular audited fiscal reporting of most state-owned enterprises allows for effective oversight by the Ministry of Finance.

There is a fairly high level of transparency in budget processes, especially inter-governmental fiscal relations, the oversight of public enterprises, and public borrowing. Budgetary, tax revenue, and audit information is made public in a timely fashion on the Internet, in the government bookshop, and in public and academic libraries. However, procurement remains opaque. Awarded contracts are not published.

Policy-based budgeting. Institutional arrangements ensure both strong policy and technical review of the budget. The budget process encompasses policy input from the Cabinet at the beginning and end of the process. The budget process starts within a pre-announced resource envelope derived from IMF Article IV forecasts. It covers both recurrent and capital outlays, coordinated by the Budget Division of the Ministry of Finance. There is a clear policy direction from the Cabinet to ministries and department agencies through the budget call circular. However, the lack of Cabinet-approved ceilings dilutes the effectiveness of the bottom-up process, making it difficult to systematically prioritize programs and projects. Budget ceilings are linked to the economic classifications of the fiscal framework.

There are links between sector development plans and the budget through annual public sector investment programs, but they are not fully costed. All such programs are approved by the Cabinet, although not included in the fiscal framework and not guided by ceilings. The absence of these ceilings results in bids from ministries and department agencies that are considerably higher than the final approved ceilings, reflecting the very late communication of final budgetary allocations to the ministries and department agencies. This leaves them no time to realign priorities with the final approved ceilings, undermining the well-intended bottom-up elements of the budget process and the achievement of technical and allocation efficiency. While the budget includes estimates of the projects funded by development partners, actual expenditure is not reported in the budget.

The budget is typically submitted to Parliament two to three weeks prior to the start of the fiscal year. The Parliament approves the appropriations within a month after the start of the fiscal year. The *Exchequer and Audit Act* allows for continued spending by the executive for just the first month of the new fiscal year.

Accounting, recording, and reporting. Bank account balances are determined daily; reconciliation and clearance of suspense accounts take place monthly (except for a few identified accounts). Accounting standards are consistently applied across all ministries and department agencies, and are included in the audited annual financial statements. The monthly expenditure returns are comprehensive, consistent with the budget classification and structure, and allow for direct comparison of budget implementation. The reports, which are issued within 30 days of the close of the month, include a reconciliation of revenues, net changes in debt, expenditures, and consolidated bank balances that ensure accuracy. The reports distinguish between commitments and actual expenditure.

Consolidated government accounts are prepared annually with revenue and expenditure information as well as a table of financial assets and liabilities. The annual appropriations accounts are completed within four months after the close of the fiscal year and audited within seven months of the close of the fiscal year.

External scrutiny and audit. Both the position and the office of the auditor-general meet most of the independence standards set by the International Organization of Supreme Audit Institutions for audit institutions. Although not all central government entities are audited every year, it is estimated that three-quarters of total expenditure is audited annually. These include financial, compliance, procurement, and systems audits. Audit reports, along with audited financial statements, are submitted to the Parliament within seven months from the end of the fiscal year.

The Comptroller of Accounts prepares an aggregated financial statement on ministry financial statements. There is little evidence of systematic and timely follow-up on external audit findings and it is often left to the field auditors to ensure that recommendations are followed through on as part of subsequent audits. Private audit firms audit public enterprises.

Parliamentary budget oversight includes expenditure achievements and the quality of expenditure management. While debates cover fiscal policies as well as revenue and expenditure estimates, the effectiveness of the parliamentary review is constrained by the limited time (less than one month) allocated to this function.

The Supplementary Budget Estimates presented by the minister of finance and voted on by Parliament are reviewed once a year, consistent with the government's emphasis on fiscal discipline. There are clear rules on in-year budget amendments.

A Public Accounts Committee conducts a review of expenditure anomalies identified in the external audit. The committee is able to review

less than 10 percent of audit reports, even though reviews involve in-depth hearings when they occur. While the committee relies on the auditor general to ensure implementation of the recommendations, no systematic or timely follow-up has taken place across all ministries and department agencies.

To eschew procyclical fiscal policies, the government established the Interim Revenue Stabilization Fund in 2000 and the Heritage and Stabilization Fund (HSF) in 2007. The design and governance structure of the HFS is in line with international best practices for sovereign wealth funds set forth in the Santiago Principles, especially regarding transparency and accountability. The deposits held by the HSF peaked at around 20 percent of GDP in 2015.

Appendix 4

Institutional Framework for Planning and Implementing a Credible Fiscal Strategy

According to the IMF staff, the institutional framework to support the planning and implementation of a credible fiscal strategy involves the following arrangements or institutions.¹ These arrangements or institutions are grouped reflecting the three key stages of the fiscal policymaking process.

Understanding the Fiscal Outlook and Challenges

A clear understanding of the current fiscal position and a realistic view of the medium-term outlook is a prerequisite for a credible fiscal strategy. In this context, the arrangements or institutions listed below are important:

- *Fiscal reporting.* Fiscal reporting arrangements that provide comprehensive, timely, credible, and transparent information are central to inform decision-makers and the public about the state and outlook of the economy.
- *Macroeconomic and fiscal forecasting.* A realistic and credible medium-term macroeconomic and fiscal forecast (updated on a frequent basis) is a starting point for the formulation of a credible fiscal strategy.
- *Disclosure and management of fiscal risks.* The government's fiscal strategy needs to take account of risks that threaten the fiscal position, including potential contingent liabilities, and disclose them in budget documents and alternative medium-term budget scenarios.
- *Independent fiscal agencies.* Independent fiscal institutions help improve the transparency and credibility of fiscal policies by analyzing and assessing the budget bill or any other legislative

¹ This section closely follows Gupta and Ylaoutinen (2014).

proposal in the fiscal area, including its consistency with fiscal rules (if any), prior to enactment.² These institutions also address the reputational costs of unsound policies.³

Formulating a Credible Fiscal Strategy

The formulation of a credible fiscal strategy can benefit from strong institutions. The strategy's credibility would be enhanced if it is based on broad fiscal objectives, takes a medium-term perspective, and connects the funds provided to public entities to their outcomes or outputs. The following areas are important:

- *Fiscal objectives and rules.* Broad fiscal objectives connect the medium-term fiscal strategy with numerical targets that will guide future decisions and against which performance can be measured.
- *Medium-term budget frameworks.* Medium-term budget frameworks are crucial to convert those targets into revenue and expenditure plans.
- *Performance-oriented budgeting.* Defined as the procedures that link spending on programs and the outcomes or outputs of these programs, performance-oriented budgeting provides information on how the budget contributes to the government's overall objectives and policies.
- *Intergovernmental fiscal arrangements.* These arrangements ensure the consistency of the fiscal stance within the different levels of government.

Implementing the Fiscal Strategy

In this regard, the following arrangements or institutions are central:

- *Budget unity.* A high degree of budget unity ensures that one decision-making process authorizes government expenditures,

² Commodity exporters could benefit from setting up an independent advisory council that would professionally estimate the long-term commodity export prices that would guide budget preparation, thereby enhancing the credibility of revenue estimates.

³ For these institutions to be effective, they must be home-grown and home-owned. They must also be non-partisan, technically competent, and accountable to the legislature, and they must have unlimited access to timely information to conduct meaningful surveillance of fiscal policymaking.

thereby making control over budget execution more effective. Central government expenditure should be covered by the central government budget and authorized annually. Also, major tax expenditures should be quantified and published.

- *Top-down budget preparation.* Under a top-down approach, limits on aggregate and sectoral spending are agreed upon at an early stage of budget preparation, thus increasing the likelihood that the annual budget will be consistent with the government's ex-ante fiscal objectives and fiscal plan. Revenue earmarking should be limited.
- *Constraints on parliamentary budget approval.* While Parliament's formal powers over the allocation of public resources vary greatly across countries, experience suggests that pre-budget or budget orientation debates can help create parliamentary ownership of the government's medium-term fiscal objectives. The legislature should first approve the main fiscal aggregates—the budget balance, total expenditure, and total revenue—before voting the allocation of resources to sectors, ministries, programs, etc.
- *Discipline in budget execution.* Effective budget implementation requires execution procedures that maintain overall fiscal discipline, while recognizing that unexpected events will occur during the course of the budget year. Overspending against budget totals should require a supplementary budget. Controls on carryover of expenditure or multi-annual commitments should be in place.

Appendix 5

Organization and Governance of the Debt Management Function

Among the institutional arrangements to be considered as benchmarks, the following stand out: (1) fiscal responsibility legislation with fiscal performance targets and requiring transparency and accountability in the government's fiscal operations; (2) sanctions for breaches of the legislation in place as an effective disincentive to public financial mismanagement; (3) procedural reforms to guard against fiscal slippage; (4) accrual accounting, as opposed to cash accounting, to help determine the correct level of financial commitment of the government; (5) Central Treasury Management (Single Treasury Account) that allows for more efficient use of the government's cash resources and reduces the need for temporary debt; and (6) constitutionally independent institutions (answerable to Parliament) that carry out their monitoring functions more effectively.

An agenda for debt management and sustainability must therefore address the institutional foundations for fiscal outcomes and debt accumulation. The internationally accepted principles of sound practice in debt management include the following key elements:¹

1. A process that separates high-level policymaking from execution ensures that debt management policy and strategic portfolio objectives are consistent with longer-term macroeconomic objectives. To this end, debt managers, fiscal and monetary authorities, and financial sector regulators should share an understanding of the objectives of debt management, fiscal, monetary, and financial sector policies given the interconnections and interdependence between their respective policy instruments.

¹ See in particular, IMF and World Bank (2014), Wheeler (2004), and Storkey (2006).

2. The development of a debt management strategy within an asset and liability framework that reflects the trade-off between cost and risk. This should include contingent liabilities (both explicit ones such as guarantees, and implicit ones that may emerge in times of stress) in formulating debt and risk management strategies.
3. A published mandate for debt managers, together with delegated authority to operate subject to specified objectives, limits, controls, etc.
4. A strong governance structure to manage and monitor the debt managers' operations. In this regard, an organizational structure is needed that is either an independent office or part of the Ministry of Finance. Sound practice entails distinguishing between separate front, middle, and back office functions.
5. A system of annual reports on the context and outcome of debt management, and regularly published information on the outstanding stock and composition of debt liabilities and financial assets, and, where they exist, contingent liabilities, including their currency denomination, maturity, and interest rate structure.
6. Annual auditing of debt management activities, information technology systems, and risk control procedures by external auditors, as well as regular internal audits.
7. Development of an efficient government securities market. Operations in the primary market should be transparent and predictable. To the extent possible, debt issuance should use market-based mechanisms such as competitive auctions and syndications. Also, the development of resilient secondary markets should be promoted.
8. Disaster management, in light of the serious fiscal and debt consequences from natural disasters such as earthquakes and storms. Caribbean governments prepare inadequately for the risk of these disasters, in light of experience. Multilateral insurance exists, but coverage is insufficient, and private insurance coverage needs to be explored. Any remaining contingent liabilities have not been explicitly accounted for or not provisioned enough in budgets, resulting in fiscal stress and higher public debt.

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