The Integration Movement in the Caribbean at Crossroads: Towards a New Approach of Integration

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ABSTRACT

The conclusion reached in this paper is that the integration process pursued by CARICOM has reached its limits -including the attempt to "widen" the process via the creation of the Association of Caribbean States (ACS). Thus, a new approach towards integration is required. It is not clear, however, which new paradigm will eventually emerge from the old integration scheme. One point is very clear: the competitive insertion of these economies into the global economy will be linked to the implementation of economic reforms. Three missing ingredients in the process of economic reforms are identified: Education, Enabling Government and Export Diversification. In the area of trade, the question is whether the current economic paradigm will accomplish the trade diversification that the old, import-substitution model could not. Moreover, the ability of the Caribbean economies in attracting foreign investment that brings with it expertise and technology is **the key factor** that will signal a change in the economic development paradigm.

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THE INTEGRATION MOVEMENT IN THE CARIBBEAN AT CROSSROADS: TOWARDS A NEW APPROACH OF INTEGRATION

Uziel Nogueira*

INTRODUCTION

The economies of the Caribbean Community (CARICOM) are undergoing a process of economic reform in which market-based policies, including trade liberalization, are key components of a new development strategy. As economic reforms gain momentum, the process of sub-regional integration comes into question. It is clear that CARICOM's original goal of economic integration has been surpassed by powerful new forces shaping global economic relations. These forces include the rapid process of globalization, and the formation of new, powerful trading blocs in the Western Hemisphere. However, it is not clear which role, if any, sub-regional integration schemes such as CARICOM or the Association of Caribbean States (ACS) can or will play in the competitive insertion of this area into the global economy.

In order to address the questions mentioned above, this paper is divided into four sections preceded by a brief background. The first section reviews the historical process of integration in the region. The second section examines new topics relevant to the process of integration such as the Free Trade Area of the Americas, the Association of Caribbean States, the Caribbean Basin Initiative and the North American Free Trade Agreement. The third section discusses trends and prospects of trade-related issues within CARICOM, while the final section presents some thoughts on the future of the process of integration.

BACKGROUND

The original thirteen member countries of CARICOM have a combined population of around 5.6 million people (approximately 1.2 percent of the total population of Latin America and the Caribbean) and a GDP of approximately US$12.5 billion in 1992 (1.6 percent of Latin America and the Caribbean's aggregate GDP). Per capita income, except for Guyana, is comparable and/or superior to the average for Latin America; the Bahamas and Barbados have the first and second highest per capita income in the region. Social indicators such as adult literacy, life expectancy at birth, infant mortality and daily calorie intake are, on average, superior to those existent in the rest of Latin America.

Resource-endowment has greatly determined the type of economic activities and the limited export base of the region (i.e., agricultural products, primarily sugar and bananas; mining activity, especially bauxite and alumina, in Jamaica, Suriname and Guyana, and petroleum and natural gas in Trinidad and Tobago). Tropical weather and beautiful beaches provide the basis for a vibrant tourism industry in nearly all the countries.

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As a result of economic reforms, traditional agricultural and mining activities are gradually being replaced by light manufacturing of goods such as textiles, clothing, footwear and service activities, particularly data processing, banking and tourism. The tourism sector has been flourishing in the last ten years as it replaces commodity-based exports as the main source of foreign currency earnings. Remittances from emigrants living in the United States, Canada and Europe, have also been an important source of foreign currency for many countries.

SECTION I. BRIEF REVIEW OF THE INTEGRATION MOVEMENT IN THE ENGLISH-SPEAKING CARIBBEAN [1]

In 1965, three Caribbean nations -Antigua, Barbados and Guyana- initiated the Caribbean trade integration process by signing the Treaty of Dicksenson Bay, which established the Caribbean Free Trade Association (CARIFTA). Three years later, with the Treaty of St. John's, CARIFTA was widened to include eight more members (Trinidad and Tobago, Dominica, Grenada, St. Kitts-Nevis-Anguilla, St. Lucia, St. Vincent, Jamaica and Montserrat). Previous integration movements included the establishment of the West Indies Federation (WIF) in 1958 under British tutelage and the creation of institutions such as the University of West Indies and the Regional Shipping Service. The federalist experiment failed, however, when Jamaica and Trinidad and Tobago withdrew and obtained their independence in 1962. In addition, the Eastern Caribbean Common Market (ECCM) was formed in 1968 (and still coexists with CARICOM) as a cooperation and integration effort of the seven less developed English-speaking islands. All of these integration efforts eventually evolved into a single, more comprehensive scheme with the signing of the Treaty of Chaguaramas on July 4th, 1973, creating the CARICOM.

Two Secretariats were created to support the integration movement: (1) the CARICOM Secretariat, servicing the Commonwealth Caribbean Heads of Government conferences and the Common Market Council, and (2) the Central Secretariat of the organization of Eastern Caribbean States (OECS) which services the Heads of Government Authority of these States as well as the ECCM. The CARICOM Secretariat is located in Georgetown, Guyana, while the OECS Secretariat has its main headquarters in Saint Lucia and an Economic Affairs Division in Antigua and Barbuda. Besides these two integration Secretariats, the overall integration effort is supported by two major regional institutions: the Caribbean Development Bank (CDB), located in Barbados and the University of West Indies (UWI), with campuses located in Barbados, Trinidad and Tobago and Jamaica. In addition to these institutions, there are around 200 small regional organizations operating in every conceivable area of activity in the Community.

From a historical perspective, the most intriguing question one might ask is **why 13 small economies, primarily small islands with limited resources and weak trade and communication linkages among themselves, sought to integrate their economies.** After all, the only successful model of economic integration occurring at that time such as, the European Common Market, involved large and highly industrialized economies. The Caribbean economies, on the other hand, epitomize the classical case of small, open economies, not considered the most suitable candidates to pursue economic integration. However, the answer to that question lies in the economic environment of the time, highly influenced by the idea of economic development sponsored by the Economic Commission for Latin America (ECLAC).

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[1] The analysis contained in this report deals only with the 13 traditional, English-speaking member countries of the Caribbean Community (CARICOM). They are: Barbados, Guyana, Jamaica and Trinidad and Tobago, the so-called More Developed Countries (MDCs), along with Antigua and Barbuda, Belize, Dominica, Grenada, Montserrat, St. Kitts and Nevis, St. Lucia and St. Vincent and the Grenadines, referred to as the Less Developed Countries (LDCs). The Bahamas became the 13th member state in July of 1983 but did not join the Common Market. Suriname became the 14th member, and first non-English speaking partner in February of 1995. In the last 17th annual meeting of CARICOM held in Barbados during the month of July, 1996, the British Virgin Islands and the Turks and Caicos had their status upgraded from associate to full membership, but only of the community, not the common market. The latter would require them to align their tariffs with that of CARICOM's CET, which would lead to a loss of revenue.

During the 1950s and 1960s, the ECLAC provided a foundation for new ideas of regional economists such as Raul Prebisch which argued for import substitution type of industrialization and regional economic integration as the formula which would provide larger markets for the region. Subsequently, Caribbean scholars, with Arthur Lewis at the forefront, were also proposing the industrialization and diversification route to development.

Thus, the idea of regional integration in the Caribbean -as well as in Latin America- has been closely linked to the idea of economic development. Regional integration has been seen primarily as a means of accelerating the industrialization of these primary-product economies and achieving the desired goals of economic development to which each country aspires. The nature of the integration-development link has changed over the years -such as the concept of open regionalism today- as the thinking on the process of economic development itself has changed, but the link has never been remote from the *raison d'être* of regional integration.

Thus, while assessing the Caribbean integration movement from the economic development perspective, a fundamental question arises: Has economic integration contributed to the economic development of CARICOM member countries? In this respect, methodological problems associated with a lack of reliable data do not allow a formal testing of the hypothesis. Thus, the second best approach is to look for other variables such as evolution of GNP and per capita income as proxies to measure performance of these economies.

Moreover, CARICOM performance is not impressive when compared to the rest of Latin America during the 1973-1993 period (See Table I). Within CARICOM, the four countries called Most Developed Countries (MDCs) -i.e., Barbados, Guyana, Jamaica and Trinidad and Tobago- were out-performed by the seven Less Developed Countries (LDCs): Antigua and Barbuda, Belize, Dominica, Grenada, Montserrat, St. Kitts and Nevis, St. Lucia and St. Vincent and the Grenadines.[2]

To a large extent, macroeconomic policy responses to the oil shocks of the 1970s and early 1980s and **not economic integration** explains the uneven growth rates observed between the two groups of countries (World Bank [1994]). In this respect, the seven smaller economies responded to the external shocks with a good public sector savings performance, a well structured and managed monetary system (through a single monetary union), a competitive exchange rate and, to a less extent, the capturing of niche export markets. The last point -related to the process of integration- is explained by the fact that within CARICOM, the seven smaller economies were given special trade treatment that allowed them to expand their intra-CARICOM exports despite the economic contraction experienced by the larger countries, particularly during the 1980s.

Also, in the case of the smaller economies, inflows of financing from the European Union also can explain gains in growth rates during that period. In this respect, the sustainability of growth in the OECS is now under question because of the possible loss of a guaranteed European market for

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[2] The MDC and LDC definitions are based on economic conditions prevailing at the time of CARICOM's creation; they are not entirely relevant in the present economic context. Guyana, for example, designated as a MDC, currently has one of the lowest per capita incomes in the Western Hemisphere.

banana exports, of great significance to many of these islands, and the curtailment of financial aid from the EU.[3]

In the case of the larger countries, domestic policy responses to the external shocks were quite the opposite from those taken by the smaller countries. Loose fiscal policies and increasingly over-valued currencies resulted in unsustainable fiscal and trade deficits financed primarily through external borrowing. As external financing began to dry up in the beginning of the 1980s, economic growth came to a halt. Even Trinidad and Tobago, the only oil exporter in the region, which enjoyed favorable movements in its balance of payments, failed to provide an appropriate incentive framework for its non-oil sectors. This shortcoming, in turn, ultimately reduced and offset the benefits of the oil price windfall.

TABLE I
CARICOM
GNP and GNP per Capita Growth, 1973-93
(constant prices - 1988 US dollars)

	GNP Growth (percent average annual growth)				GNP per Capita Growth (percent average growth)			
	1973-80	1980-85	1985-88	1988-93[a]	1973-80	1980-85	1985-88	1988-93[a]
CARICOM	2.9	-2.7	-1.6	n.a.	2.6	-1.4	1.6	n.a.
MDCs	2.8	-3.1	-2.3	0.9	2.8	-4.0	-1.5	-0.6
Barbados	3.6	-1.0	5.1	-0.5	3.3	-1.3	5.0	-0.8
Guyana	1.2	-6.9	-1.4	2.0	-0.9	-7.6	-1.8	1.5
Jamaica	-3.8	-1.0	2.3	3.3	-5.0	-2.5	0.9	2.3
Trinidad & Tobago	7.3	-4.0	-6.1	-0.4	5.6	-5.5	-7.5	-1.6
LDCs	4.3	3.6	7.0	5.4	2.3	2.4	5.1	3.5
Antigua	2.4	5.8	6.8	3.7	1.1	4.4	5.2	2.1
Dominicana	-0.4	4.6	7.3	6.7[c]	-1.0	3.2	5.9	5.3
Grenada	4.3	4.9	6.2	4.6	n.a.	2.9	4.2	2.6
St. Kitts	3.2	2.5	5.7	4.2[c]	3.2	2.3	5.2	2.3
St. Lucia	7.0	4.0	3.8	4.2	4.9	1.9	1.9	2.3
St. Vicent	2.4	6.2	5.4	5.0	0.3	4.7	3.9	3.5
Belize	6.9	0.4	10.8	7.8	4.8	-2.3	7.5	5.1
Latin America and the Caribbean[b]	5.7	1.5	2.7	1.8	3.0	-0.8	0.6	-0.1

[a] Growth rates for 1988-93 are measured in terms of GDP.
[b] Growth rates for Latin American and the Caribbean Total are measured in terms of GDP.
[c] 1988-1992
Sources: Data for 1973-88: The World Bank, *The Caribbean Common Market: Trade Policies and Regional Integration in the 1990s*, December 1990. Data for 1988-93: IDB official statistics. (IMF, IFS for LDC).

Moreover, if a comprehensive view of the integration movement in the English speaking Caribbean is taken, one might conclude that the integration process being pursued by CARICOM has reached its limit; intra-CARICOM trade has never exceeded 10-12 percent of total trade and intra-investment was non existent. The fundamental reason for this weakness is that, because of their similar productive structure in which few and similar tradeable goods are produced, the range of products available for intra-regional trade is limited (see Section III on trade patterns). As a result,

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[3] For a more detailed analysis of the policy options for the OECS see: World Bank (May 1994).

the smaller Caribbean economies cannot generate high levels of intra-regional trade and investment and, consequently, the dynamic spillovers associated with such activities as were achieved in larger and more dynamic trading blocs such as MERCOSUR and NAFTA. In addition, private corporate integration -which is the driving force of economic integration in the Western Hemisphere today- did not happen in the past, and still is not taking place today in the Caribbean. Also, deficient trade policies and inadequate transportation and trade facility arrangements play an important role in constraining regional trade as well as trade with the rest of the world.

The failure of the earlier integration movement in the Caribbean for the reasons discussed above -and elsewhere in Latin America- could also be interpreted as an indictment of the interventionist, inward-looking economic model adopted in the region until the early 1980s. Current mainstream thought in the area of trade (highly influenced by empirical evidence of the successful export-oriented economies of Asia/Pacific) argues that outward orientation (i.e., opening one's market to the rest of the world and promoting exports) leads to higher GDP growth (Krueger [1978]).[4] Today, in the new framework of open regionalism, the Latin American and Caribbean economies are attempting a more open, market-based and outward-looking economic model complemented by a modern integration process exemplified by MERCOSUR and NAFTA.

It should be recognized that despite CARICOM's shortcomings in the area of economic integration, the results achieved in other areas of regional cooperation have been highly positive in areas such health, education and culture, communications, natural disaster alleviation and improvement in air and shipping transportation linkages. Regional air transport has been deregulated, as the community adopted an air service agreement -signed by all CARICOM member countries with the exception of Jamaica and the Bahamas- which opens the skies to all CARICOM and international airlines. This is expected to increase tourist and business travel and to lower ticket prices. The new arrangement will also increase competition for existing airlines, some of which may not survive such as was the case of Carib Express which closed down in April of 1996.

In the area of education, the University of West Indies, considered a world-class institution, offers access to higher education to students of all CARICOM member countries. In July of 1995, a small but significant breakthrough was made when the governments decided that CARICOM nationals who are graduates of recognized universities will not need work permits in any member states. This is intended to allow free movement of skilled professionals. Journalists and athletes are next for such treatment.

Lastly, CARICOM has been a very effective political instrument for winning trade and financial concessions from the United States and Canada (e.g., CBI, CARIBCAN), and the European Union (Lome Convention). In addition, favorable non-reciprocal free trade agreements with Venezuela and Colombia have been negotiated in 1992 and 1993, respectively.

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[4] Almost all studies in the past 25 years have documented the superior growth performance of outward-oriented economies. Beginning with studies by Bela Balassa and followed by Anne Krueger's classic work on trade liberalization in developing countries, empirical studies have consistently found a high correlation between overall GDP growth and growth in export earnings.

SECTION II. THE PROCESS OF INTEGRATION DURING THE 1990's: THE ACS, NAFTA, CBI, AND THE FTAA

Realizing the shortcomings of CARICOM, a vivid debate on the insertion of the Caribbean economies into the global economy has emerged among policy makers in the last few years. There is a realization that two ominous trends are taking place. First, financial aid from the European Union and the United States has been sharply curtailed and preferential trade agreements with those countries are in danger of being phased out (e.g., Lome, CBI, CARIBCAN). Second, the Caribbean economies are not part of the new, powerful trading blocs emerging in the Western Hemisphere such as NAFTA or MERCOSUR. In the case of the emerging FTAA, the Caribbean countries see themselves in a weak negotiation position vis-a-vis the larger countries. As discussed next, collective initiatives have been undertaken by the region in relation to these challenges. The first collective initiative is an attempt to expand CARICOM via the ACS.

The Association of Caribbean States (ACS)

The first response from the Caribbean economies to the challenges of globalization and regionalization has been the creation, in 1995, of a new trade and economic organization called the Association of Caribbean States (ACS).[5] The idea behind it is to "widen" CARICOM (i.e., to include all countries located in the geographic area designated as the Caribbean Basin). The ACS would have a market of about 200 million people, with an estimated combined gross national product of US$500 billion, and a trade volume of about US$180 billion per year.

The ACS is expected to enhance mutual cooperation in economic and trade-related areas such as tourism, transportation, agricultural production, sustainable use of natural resources, and cooperation to overcome natural disasters. Its charter envisions a Special Committee on Trade, Development and External Economic Relations with a mandate to elaborate strategies for the convergence of trade policies both among participants in the Association as well as between the ACS, the hemisphere, and the rest of the world; the identification of intra-regional and extra-regional trade promotion initiatives; the strengthening of private sector participation in trade and regional developments; and the identification of tourism activities which can be promoted at the regional level.

Given the short period of time since the ACS came into existence, it is too early to assess its effectiveness as a future trading or economic bloc. However, as stated previously, it is doubtful that the basic economic constraints faced by CARICOM in the past can be overcome by the ACS in the future. This newly formed organization will face tremendous challenges, such as finding financial resource for the accomplishment of its ambitious trade-related activities and to take an effective role in fostering economic integration (especially difficult considering that trade and investment activities are minimal among its 25 member countries).

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[5] The 25 countries are: Barbados, Guyana, Jamaica, Trinidad and Tobago, Antigua and Barbuda, Belize, Dominica, Grenada, St. Kitts and Nevis, St. Lucia, St. Vincent and Grenadines, Bahamas, Cuba, the Dominican Republic, Haiti, Suriname, Costa Rica, Nicaragua, Guatemala, Honduras, El Salvador, Panama, Venezuela, Colombia and Mexico.

In a more pessimistic view, a recent paper states that "the ACS is waiting for an appropriate theory of international institutions to develop before it can foresee a clear mandate. A calypsonian could well depict the ACS, *as a medicine in search of a disease*" (Dookeran [1996], p.3). Nonetheless, it should be recognized that the ACS is part of a second generation, modern, outward-looking integration organization that could build an economic bridge between the English speaking countries in the Caribbean and their Spanish and French speaking neighbors.

The North American Free Trade Agreement (NAFTA)

The implementation of NAFTA has promoted a debate on how the Caribbean economies should position themselves in the emerging economic order dominated by trading blocs. The question probably is "does NAFTA matter to the Caribbean region?" The answer is that with over 45 percent of total exports destined to North America, maintaining preferential trade arrangements with this region is, clearly, the main trade-related topic in the Caribbean. Access to the U.S. market is of tantamount importance considering that, after Canada and Mexico, the Caribbean economies are the most integrated to the U.S. economy, and that the United States is by far the largest market for CARICOM (40 percent of their total exports). In addition, the U.S. is CARICOM's main source of direct foreign investment which amounted to US$6 billion by 1989 (U.S. Commerce Department).

Policy makers in the region argue that, over time, implementation of NAFTA could reduce the competitive advantage *vis-a-vis* Mexico that the Caribbean countries enjoyed through the Caribbean Basin Initiative (CBI). There is a fear that textiles and clothing exports to the U.S. market could be displaced by Mexican producers, and that this trade diversion would lead, eventually, to investment diversion.[6] Also, fear of protectionism in the U.S. market plays an important factor. For example, the Office of the U.S. Trade Representative has moved recently to restrain imports of underwear and nightwear, key products in the region's booming apparel sector, from eight countries including the Dominican Republic and Jamaica, to offset U.S. manufacturer's claim of damage.

Despite diplomatic initiatives in the last two years by Jamaica and Trinidad and Tobago arguing their "readiness" to join NAFTA, the political climate in the United States has not been conducive to an earlier expansion of NAFTA, as the negotiations with Chile have demonstrated. Thus, as NAFTA membership became a remote possibility, the second best solution for the Caribbean countries was to focus on winning eventual NAFTA parity via CBI (i.e., obtaining the same trade preferences as Mexico is granted under NAFTA).

[6] Since Mexico's accession to NAFTA, sales of Caricom textiles to the US market have been increasingly displaced by Mexican exports. These have risen to 10 percent of all US garment imports, while for instance, those of Jamaica have fallen to 2.2 percent. Jamaican garment exports to the USA dropped from $500 million a year to $377 million in the first nine months of 1996, with little chance of recovery in the final quarter. Garment factory closures led to the loss of 2,000 jobs in 1996. The Caribbean Textile and Apparel Institute, based in Jamaica, estimates that 120 Caribbean apparel firms have closed and 88,000 jobs have been lost in the last two years as a direct result of trade diversion to Mexico. Mexican competition is likely to intensify as new garment assembly plants open there at the rate of 40 per month (Oxford Analytica Latin America Daily Brief - February 3, 1997).

The Caribbean Basin Initiative (CBI)

The United States has created two preferential schemes offering duty-free treatment for certain goods: The Generalized System of Preferences (GSP), which was initiated in 1976 for 10 years and later extended until July of 1996; and the Caribbean Basin Initiative (CBI), which was approved in 1985 and made permanent as CBI II in August of 1990. CBI countries can choose to export a duty-free product under either program but most prefer to export through the CBI because it offers broader preferences, and more flexible rules. The benefits of CBI are limited to 24 eligible Central American and Caribbean countries. Except for a small number of goods formally excluded,[7] all products from CBI beneficiary countries can be eligible for duty-free entry. It is important to note that CBI is a one-way, non-reciprocal trade agreement (i.e., Caribbean and Central American countries have no obligation to reciprocate in their own markets).

From the Caribbean standpoint, the CBI's performance has not matched the high expectations created when it was launched. Utilization of the program has been highly concentrated in a few countries. Principal beneficiaries of the CBI program have been the Dominican Republic and Costa Rica, which together account for about 50 percent of all CBI duty-free imports. Other major users are Honduras, Guatemala, Haiti, and Jamaica, which account for about 30 percent of duty-free imports. The United States also has benefitted from the program; its exports to countries in the Caribbean Basin jumped from US$5.8 billion in 1983 to US$12.2 billion in 1993. This increase of 112 percent is three times the growth rate of U.S. global exports during this period. Further, the U.S. trade deficit with countries in the Caribbean Basin of US$2.6 billion in 1984 turned into a surplus of about US$2 billion ten years later.

In spite of heavy lobbying, initiatives for achieving NAFTA parity have not materialized, yet. In March of 1995, a bill by Congressman Phil Crane was introduced -The Caribbean Basin Trade Security Act H.R. 553- that would provide U.S. imports from CBI countries with NAFTA parity. The new legislation offered increased market access without requiring reciprocal commitments in the areas of intellectual property rights, environmental protection, investment and workers rights protection. The Executive has not acted on this bill because, among other things, it differs from its own initiative, the Interim Trade Agreement (ITP) put forward by the United States Trade Representative (USTR). Whereas the Crane bill covers all products, the ITP would only have provided parity to textiles and apparel products meeting NAFTA's rules of origin. Any initiative regarding NAFTA parity and other trade-related questions can be expected only after President Clinton's visit to Barbados in May of 1997. Nonetheless, there is no political climate in the USA for any non-reciprocal trade agreement such as the proposed NAFTA parity bill. Thus, if any trade agreement emerges, it will be linked to reciprocal concessions in trade or otherwise.

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[7] The products excluded are: footwear, petroleum products, categories of flat goods and gloves, leather apparel, canned tuna and a minor category of watches. Textiles and apparel are subject to special agreements such as the existing Tariff Preference Level (TPL) 807 applied to apparel products. Under 807, when merchandise manufactured from fabric made and cut in the U.S. is assembled in a CBI country and then re-exported to the U.S., duty is paid only on the value added of labor used in the assembly.

In this respect, efforts to reconcile growing conflicts between the United States and the 14 member countries of the CARICOM will dominate the economic and political regional agenda in 1997. The recent refusal of Jamaica and Trinidad and Tobago to accede to U.S. request for open access into their territorial waters for the pursuit of drug traffickers is one case in point. Another is CARICOM's closer ties with Cuba. Cuba is becoming slowly integrated into the Caribbean mainstream. It has been admitted to bodies such as the Caribbean Tourism Organization (CTO), and is striking trade, investment and other accords with various Caribbean countries, the most recent of which was with Trinidad and Tobago.

The Free Trade Area of the Americas (FTAA)

The Summit of the Americas, held on December 15, 1994 was an important event for the process of hemispheric integration, particularly for the small economies of the Caribbean Community. At the Miami conference, the governments of the Western Hemisphere (except Cuba) agreed to immediately begin the construction of a free trade area of the Americas in which barriers to trade and investment will be progressively eliminated beginning no later than 2005.

For CARICOM member countries, the establishment of a free trade area in the Americas is an important event since it can assist them in building stronger trade and investment linkages with the rest of the hemisphere, help consolidate and deepen domestic economic reforms, and more importantly, help attract much needed foreign investment. The challenges, however, are also daunting and include: (a) whether the 14 economies can sustain the programs of structural economic reform needed to capture the benefits derived from full participation in a hemispheric free trade area. At this point, economic reforms vary quite markedly among the 14 countries, with Jamaica, Trinidad and Tobago, and to a lesser extent Guyana and Barbados leading the process of reform (See Section III, for a review of the process of trade reforms); and (b) whether negotiations for a FTAA will strengthen or weaken CARICOM and the ACS.

That second point is important because the Miami Summit calls for the consolidation of existing sub-regional and bilateral arrangements as "building blocks" to broaden and deepen hemispheric integration. A weak CARICOM/ACS would be less effective at negotiating trade arrangements with larger, more powerful economies in the hemisphere. In this respect, the Caribbean countries' ability to win concessions from the larger economies will be tested in the negotiations to establish the FTAA. During the Denver Trade Ministerial meeting of last year, the Caribbean economies secured the creation of a working group for the purpose of examining ways to facilitate the integration of smaller economies into the hemispheric free trade area. However, it remains to be seen whether or not the smaller Caribbean countries will get special treatment or the technical and financial support to assist their insertion into the future free trade area.

SECTION III. ECONOMIC REFORMS AND TRADE LIBERALIZATION

Through various macroeconomic adjustment and sector adjustment loans (SAL) extended by multilateral institutions, the Caribbean economies started a series of economic reforms in the second half of the 1980s. Within the so-called "Washington Consensus" of market-oriented reforms, trade diversification and liberalization is considered a fundamental variable for achieving sustainable, long term economic growth.[8] This section briefly reviews the patterns of trade in the region, including composition and destination of intra and extra-regional trade, exchange rate regimes, the implementation of the Common External Tariff (CET) and progress of the trade reform program.

Background

Scarcity of data which, in turn, prevents the application of formal tests of international trade determination models is the main problem for analyzing trade patterns among CARICOM member countries and of CARICOM with the rest of the world.[9] Nonetheless, simple Ricardian and Hecksher-Ohlin trade models provide a strong theoretical basis for explaining trade patterns observed in the region. Technological differences, factor endowments, factor mobility and consumption patterns are very useful assumptions in explaining Caribbean trade patterns.

Even today, trade patterns reflect the Caribbean's colonial past in which the islands provided a few agricultural products, primarily sugar, a labor intensive activity, in exchange for manufactured goods from Europe. The only variation to this model occurred when petroleum was discovered in Trinidad and Tobago, bauxite in Jamaica and Guyana, and attempts at industrialization -via import-substitution -which took place during the 1970s. Exports of semi-finished products are recent and account for a small proportion of the overall exports of the region.

Given the similar consumption patterns of the Caribbean economies (reinforced by a similar colonial heritage, climate and language), differentiation and composition of trade are, to a large extent, determined by their production structure. Determinants of the direction of trade are geographical location, historical links and preferential market access agreements. Determinants of demand for and income from Caribbean exports are fluctuations in the prices of export commodities and growth of income in industrialized countries.

Overall, the composition of CARICOM's merchandise trade is as follows; on the export side, agricultural products and food make up the bulk of most CARICOM countries' exports.

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[8] The expression "Washington Consensus" was coined in the 1980s by John Williamson of the Institute for International Economics, located in Washington D.C. It refers to a body of policy recommendations aimed at establishing market-oriented economic reforms in Latin America. These recommendations, endorsed by the multilateral institutions, covered broad areas such as: public sector reform (privatization of state enterprises, fiscal discipline, public expenditure priorities, tax reform, reform of the judiciary); trade reform and liberalization; deregulation of labor and financial markets; unified exchange rates; and property rights.

[9] Analysis of investment flows in the CARICOM is even harder to do than those of trade. There is little consistent, detailed data on investment composition and direction. The balance of payments data published by the Central Banks distinguish between public and private capital flows, but the latter is not generally desegregated by sector, source or direction. The problem of private investment data is further compounded in those countries that no longer have exchange controls.

Manufactures constitute a significant proportion of total exports, only in Barbados and Jamaica. Fuel products dominate exports of the Bahamas and Trinidad and Tobago. On the import side, the main products are manufactured goods and food (the notable exception being the Bahamas whose imports are mainly crude oil required for its oil refineries). With the exception of Trinidad and Tobago, **all CARICOM countries incur overall merchandise trade deficits.**

In the case of the islands of St. Lucia, St. Vincent and the Grenadines and Grenada, agricultural dependence is even more concentrated on one crop, bananas. Banana exports averaged over 50 percent of exports for the first three islands and 18 percent for Grenada in 1990. As a share of export revenue, banana exports contribute, on average, to around 57 percent, while also amounting to 31 percent of GDP and 50 percent of employment. Moreover, the on-going dispute with the United States on the banana regime is cause for concern among those countries.

The cause for the dispute is that Chiquita Brands International, which markets bananas from Latin America, argues that its exports are suffering from the European Union's policy giving special market access to banana imports from African, Caribbean and Pacific (ACP) countries via the Lome agreement. The USTR is expected to take this case to dispute settlement panel of the World Trade Organization (WTO) if an acceptable solution is not reached during on-going negotiations. Should the WTO rule against the E.U.'s policy, it could be highly damaging to the smaller economies of the OECS.

The few manufacturing firms which operate in the OECS are of three types: (a) enclave industries serving U.S. markets; (b) agro-processing and related industries mainly serving the CARICOM market; and (c) industries serving primarily local markets. Enclave industries consist almost exclusively of firms producing garments and electronic equipment. Agro-processing and related industries which produce for the CARICOM market include soap products, flour, feed grain and cardboard boxes. Industries serving primarily local markets include beer, cigarettes, soft drinks, toilet paper, furniture and small appliances. Manufactured exports are heavily concentrated on a few products such as garments, sugar flour, cardboard boxes and beer which could be jeopardized by future trade liberalization.

Extra-regional markets play the dominant role in CARICOM's trade patterns. Europe and the United States are the destination for three quarters of Caribbean exports (see Table II). The United States is by far the largest market for Caribbean products (almost 40 percent of their total exports). The importance of the U.S. market is even greater because it imports the largest amount of manufactured goods, such as textiles, clothing and chemicals produced in the region, as well as assembly industry components (i.e., imported from the U.S., assembled in the region and re-exported to the U.S. market under reduced tariffs).

TABLE II
Destinations of Total Exports[1], 1994

Country	CARICOM	USA	Canada	UK	Other EU	Japan	Other	Total
MDCs								
Bahamas	n.a.	30.5	5.0	7.3	n.a.	2.0	55.2	100.0
Barbados	34.0	18.0	5.0	19.0	2.0	1.0	22.0	100.0
Guyana[2]	3.0	2.0	24.0	23.0	3.0	0.0	45.0	100.0
Jamaica	5.0	36.0	13.0	14.0	10.0	2.0	20.0	100.0
Suriname	n.a.	21.9	n.a.	6.0	52.0	6.0	14.1	100.0
Trinidad & Tobago	20.0	44.0	4.0	2.0	6.0	1.0	23.0	100.0
LDCs								
Belize	3.8	38.8	8.0	40.2	5.0	0.0	4.2	100.0
OECS								
Antigua[3]	67.0	n.a.	n.a.	n.a.	n.a.	n.a.	33.0	100.0
Dominicana[2]	31.0	4.0	0.0	52.0	4.0	0.0	9.0	100.0
Grenada[4]	31.0	13.0	2.0	20.0	19.0	n.a.	15.0	100.0
Montserrat	21.0	38.0	0.0	4.0	35.0	n.a.	2.0	100.0
Sr. Kitts-Nevis[3]	13.0	47.0	n.a.	21.0	n.a.	n.a.	19.0	100.0
St. Lucia	16.0	28.0	1.0	53.0	1.0	1.0	1.0	100.0
St. Vincent	55.0	10.0	1.0	30.0	2.0	0.0	2.0	100.0

[1] includes re-exports
[2] 1993
[3] 1990
[4] 1991
Sources: Ramesh F. Ramsaran: "Small Economies, Trade Preferences and Relations with Latin (South) America: Challenges Facing the Anglo-phone Caribbean in a Changing World Economy". Draft, September, 1996.

The Common External Tariff (CET)

CARICOM countries have, in principle, a common external tariff structure levied on imports from outside the region. The basic structure of the CET is set according to two principles: (a) imports that compete with regional production should have higher tariff rates than those that do not; and (b) imported final consumer goods should have higher rates than inputs and capital goods. Competing products are defined as those for which regional production can satisfy 75 percent or more of regional demand. There are, however, numerous exceptions to the CET's basic structure. By the end of 1995, the third phase of the CET started to be implemented with licenses and quotas on specific products being removed by most CARICOM member countries.

Jamaica and Trinidad and Tobago have eliminated virtually all -and Guyana most- of their extensive import and foreign exchange licensing requirements (see discussion on trade reform next). While many NTBs have been eliminated, a number of countries retain some protective barriers, especially against the importation of agricultural products. They include not only licensing requirements and quantitative restrictions but also public sector import monopolies. Attention also is focused on eliminating the plethora of stamp duties, import surcharges, and discriminatory rates of the consumption tax that are now levied on imports of many countries. These are in many cases a more serious source of anti-trade bias than are formal import tariffs.

Finally, it should be recognized that implementation of tariff reductions in the Caribbean presents a quandary for government officials. Because of their limited ability to generate fiscal revenues from traditional sources such as consumption or personal income, import duties are the main source of public revenue in most countries. Thus, the question of fiscal needs has always been balanced against the needs of tariff reduction and trade liberalization. At this point, there is no evidence that this problem has been resolved throughout the region. Also, it is recognized that the strategic importance of the CET is likely to diminish quite rapidly. Global tariff reduction, regionalism and bilateral trade concessions will further compromise the sustainability of the CET and reduce the group of countries to which it applies.

The Trade Reform Program

As mentioned before, over the last few years some members of the CARICOM have implemented trade policy reforms as part of their structural adjustment programs. Dr. Hilaire applies the methodology of identifying trade liberalization episodes, and derives important insights on comparisons of direction, sequencing, speed of reforms and the issue of policy reversals in the Caribbean (Hilaire [1995]). The analysis covers the 1971-1995 period and contain 5 phases defined as:[10]

- Phase I: Widespread quantitative restrictions (QRs), high tariffs, exchange controls on current and capital account and fixed exchange rates.

- Phase II: Reduced QRs, high tariffs, import surcharges, exchange controls on current and capital accounts and fixed exchange rates.

- Phase III: QRs mainly on agriculture, lower tariffs, lower import surcharges, exchange controls mainly on capital accounts, fixed exchange rates.

- Phase IV: QRs mainly on agriculture, lower tariffs, lower import surcharges, exchange controls mainly on capital accounts, flexible exchange rates.

- Phase V: Minimal QRs, low tariffs, no exchange controls, flexible exchange rates.

[10]For explanation of the methodology used to define trade liberalization, see: Papageorgious, Michaely and Choksi (1990).

TABLE III
Phases of Exchange Control Regimes

Country	1971-1975	1976-1980	1981-1985	1986-1990	1991-1995
Antigua & Barbuda	I	II	II	II	III
Dominica	I	II	II	II	III
Grenada	I	II	II	II	III
Montserrat	I	II	II	II	III
Sr. Kitts-Nevis	I	II	II	II	III
St. Lucia	I	II	II	II	III
St. Vicent & the Grenadines	I	II	II	II	III
Bahamas	I	II	II	II	III
Barbados	I	I	II	II	III
Belize	I	I	II	II	III
Guyana	I	I	II	III - IV	V
Jamaica	I	I	II	III - IV	V
Suriname					
Trinidad & Tobago	I	I	I	II	III - V

Definition of Phases of Exchange Controls - See Text.
Source: Alvin D.L. Hilaire.

The findings shown in Table III are the following:

1. During the 1970s, following the import substitution strategy, all CARICOM member countries relied heavily on quantitative import restrictions, particularly for those countries with relatively larger domestic manufacturing sectors.

2. Most countries entered Phase II during the early 1980s. Trinidad and Tobago's entrance was at the end of the 1980s. Reduction of QRs for Trinidad and Tobago, Jamaica and Guyana were formalized under conditionalities of IMF/World Bank adjustment programs.

3. Guyana and Jamaica moved progressively through all five stages; stages II, III and IV were concentrated in the late 80s and early 90s. Their transition between phases III, IV and V was marked by rapid currency depreciations as they experimented with different exchange rate systems (multiple, crawling peg, auctions).

4. Trinidad and Tobago skipped phase IV and moved into V, abandoning controls on both current and capital account transactions in switching from a fixed to a flexible exchange rate system.

5. The OECS countries, Barbados and the Bahamas have reached phase III, but do not appear to wish to reach phase IV and V.

6. In none of the Caribbean cases was there a policy reversal in the sense of reversion to an earlier stage of liberalization.

The Role of the Exchange Rate Regime in the Trade Regime

Until the 1980s, price stability in all CARICOM member countries was preserved by a fixed exchange rate regime pegged first to the British Pound and later to the U.S. dollar. In fact, the idea of **a Currency Board** used in the convertibility law of Argentina was first introduced in the Caribbean colonies by Great Britain. Such price stability was shattered by the oil price shocks of the 1970's and early 1980's which compelled the countries, particularly the larger ones, to undertake structural economic reforms.

The World Bank -which led and promoted the process of trade reforms in the Western Hemisphere- took the view that export diversification was a fundamental component of a new outward-oriented growth strategy. Moreover, such export diversification would only take place if a more competitive exchange rate system was adopted. Following the latter approach, Jamaica, Guyana and Trinidad and Tobago -as part of their programs of structural reforms- have adopted flexible exchange rate regimes. At this point, the economic authorities in those countries have given no indication of returning to a fixed system in the immediate future. The remaining eleven CARICOM member countries (i.e., the seven OECS countries plus Barbados, Bahamas, Belize and Suriname) have kept a fixed exchange rate system and give no indication of switching to a flexible one. One important consequence of the two exchange rate regimes is that such *status quo* makes it almost impossible to achieve a monetary union as originally envisioned by CARICOM.

The dilemma presented by the adoption of a flexible exchange rate regime in the Caribbean is presented by Havelock R. Brewster:

> "The extreme structural dichotomy of most Caribbean countries poses a virtually insoluble problem for exchange rate policies. On the one hand, the bulk of exports -traditional tropical agricultural and mineral products of high retained value added- faces a more or less fixed demand, with prices externally determined and quoted in foreign currency. On the other hand, the production of manufactured goods for exports is as yet minute, highly dependent on imports, an thus composed of a very small retained value added. As for Caribbean tourism, given its particular characteristics, import content, and lack of conclusive evidence of sensitive relative price demand elasticities, devaluation cannot be viewed as necessarily producing net beneficial results. (A comparison of the experience of Jamaica, Barbados, Antigua, and the Bahamas in the 1979-86 hardly supports the case for devaluation).
>
> On top of this, these small societies of such patchy economic structure it would prove extremely difficult to limit the transmission of devaluation to domestic prices, to the full extent, if not more. There is a clear danger therefore of having the worst of all worlds -very high social costs with little positive impact on export earning (Bourne et al. [1988]). It is recognized that devaluation entails transitional costs. However, the structural dichotomy referred to above is extreme in the Caribbean. For example, in Jamaica the most structurally developed of the community countries, exports of manufactured goods are about 5 percent of the total value of exports when expressed in net terms. This feature of the economy, together with the limited means available for mitigating social costs, suggests that the transitional period would be both very long and very painful, even if devaluation ultimately were beneficial."

Therefore, given theoretical and empirical arguments against the use of a flexible exchange rate regime, the litmus test for Jamaica, Trinidad and Tobago and Guyana is whether the new exchange rate regime can: (a) promote export diversification in the medium term, and (b) enhance competitiveness of manufacture exports to the rest of the world and thus "reveal' their comparative advantage. Unfortunately, at this point there is no analytical work done in order to test both hypothesis. The evidence in this area is the following so far:

First, the three countries have presented a fairly competitive exchange rate among themselves *and vis a vis* those of their trading partners in the ACS, i.e., Colombia, Venezuela and Mexico (See Table IV).

TABLE IV
Real Effective Exchange Rates
(1990=100)

	1980	1981	1982	1983	1984	1985	1986	1987	1988	1989	1990	1991	1992	1993	1994	1995p
Selected CARICOM																
Barbados	87	94	100	104	108	108	105	102	100	105	100	104	107	107	105	100
Guyana	192	208	236	276	282	291	276	142	179	142	100	86	95	105	104	103
Jamaica	147	155	160	165	105	92	102	103	104	111	100	86	78	87	87	94
Trinidad & Tobago	94	99	106	123	141	149	100	104	99	97	100	101	105	87	87	85
Group of Three																
Colombia	191	208	223	219	203	178	133	120	117	114	100	99	99	106	129	136
Mexico	130	147	100	95	113	114	79	74	91	98	100	109	119	127	122	83
Venezuela	214	236	255	273	188	197	180	117	142	105	100	107	112	114	107	134

p/ third quarter
Note: An increase indicates an appreciation of the local currency vis a vis that of its trading partners.
Source: INT/ITD based on data from the IMF.

Second, if Jamaica is taken as a case in point for devaluation and trade reforms, the results are quite disappointing. Jamaica has had substantial trade deficits in the last ten years which have accelerated in the last two. In 1995, for example, the trade deficit soared to US$1.3 billion (approximately 30 percent of GDP). Persistent trade deficits (not offset by investment inflows) have weakened the exchange rate and the Central Bank has not been able to bring it under control. The government hopes to stabilize the exchange rate through a new "industrial policy" aimed at attracting direct foreign investments of around US$1.3 billion in 1996-97. Since only US$118 million in foreign inflows were recorded in 1994, many consider the government figures highly unrealistic.

Third, contrasting with Jamaica, Trinidad and Tobago has had good trade performance which *per se* is not unexpected. In fact, because of petroleum and natural gas exports, Trinidad and Tobago is the only CARICOM country to post a trade surplus. Nonetheless, there is some indication that manufactured goods are experiencing good performance, particularly within CARICOM markets. The unilateral imposition of import quotas and duties on a number of Trinidad and Tobago goods (e.g., pasta and dairy products, hydrogenate oil, cigarettes and toilet paper by Barbados and electrical sockets by Jamaica) signals penetration into CARICOM's markets by Trinidad's manufactured exports.

At the heart of the trade dispute is the greater competitiveness of Trinidad and Tobago's manufacturers in the CARICOM region. The country's trade liberalization program has opened the economy to competition and domestic producers have responded by re-tooling and cost cut measures in order to become more efficient. As a result, Trinidad and Tobago is the first CARICOM member country to break into Latin American markets. Thus, reforms in the area of trade combined with a competitive exchange rate are helping the country to become more competitive in products other than oil and natural gas.

SECTION IV. THE OUTLOOK FOR THE PROCESS OF INTEGRATION

The conclusion reached in this paper is similar to the ones attained by other scholars and policy-makers (i.e., the integration process pursued by CARICOM has reached its limits, including the attempt to "widen" the process via the creation of the ACS). It is not clear, however, which new paradigm will eventually emerge from the old integration scheme. The only consensus is that a new approach towards integration is required.

"To be effective, any new integration paradigm for the Caribbean must go beyond matters of trade and respond to the international situation. This paradigm should link productive structures, promote interaction between the private sectors of different countries, and create technological advances that will reduce the cost of doing business, increase institutional flexibility, and promote social capital among the peoples of the region. The alternative is further economic marginalization and political peripheralization. But what the specific targets and methods will be, and how development will be secured by new integration paradigms, remain uncertain" (Dookeran [1996], p.3).

Thus, even though there is no clear definition of the future form that the integration movement will take in the area, one point is very clear: the competitive insertion of these economies into the global economy will be linked to the implementation of economic reforms. In this respect, a recent paper brings into focus some points for discussion. Using the economic development paradigm of the successful East Asian economies (e.g., Singapore, Hong Kong, Korea, Taiwan, Malaysia and Indonesia), Ms. Nancy Birdsall identifies three missing ingredients in the process of economic development in the Caribbean region: *Education, Enabling Government and Exports.* In the case of education, the argument is that even though this has been a successful area of accomplishment in the past, current public expenditures have decreased, and the quality of education has declined. In the case of enabling government, the argument is that "the challenge is the need to build a new consensus around the idea of government -not as the engine of growth, or as the caretaker of the population- but as the enabler and catalyst for the private sector to operate effectively in every respect. We may call this the deepening of the reform of the state (Birdsall [1996], p. 20)". From this diagnosis a series of measures are recommended such as privatization, deregulation and building a lean and strong government.

In the case of exports, the conclusions and policy recommendations coincide with previous studies undertaken in the region. Namely, it is critical for the Caribbean countries to rely less on commodity based exports and more on products/services that enhance their comparative advantage and increase value-added. In this respect, the successful Chilean experience of trade diversification has shown important lessons for the Caribbean and Latin American economies: first, the assumption that a small Latin American/Caribbean economy cannot compete in international markets is not valid any longer; second, a small economy can be big and dominate specific niche markets; and third, labor resources in the region can compete effectively with other areas in the world.

Moreover, in the case of the Caribbean economies, the question is whether the current economic paradigm will accomplish the trade diversification that the old, import-substitution model could not. In this respect, the basic argument is that the new economic policy orientation is expected to set the foundation for future, sustainable economic growth as it did in the case of Chile. Therefore, I would suggest -based on the Chilean experience of trade diversification- that the ability of the Caribbean economies in attracting foreign investment that brings with it expertise and technology is the **key factor** that will signal a change in the economic development paradigm.

Since, Trinidad and Tobago appears to be the "success story", its performance will be watched closely by other countries in the region waiting to implement or deepen their own economic reform programs. For example, a fourth consecutive year of real growth is in prospects for 1997 with GDP growing by 3.5 percent. The relative advance of manufacturing and services has reduced the economic dominance of energy, helping the economy to become more broadly-based.

Finally, one should bear in mind that, notwithstanding positive results occurring from the new approach towards economic development, vulnerability to external shocks and volatility -caused either by economic, financial factors or natural disasters- remain a fundamental issue which can adversely affect the performance of the Caribbean economies.

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