

US Foreign Policy Towards the Caribbean Community (CARICOM): Economic Aspects

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Testimony to the Subcommittee on the Western Hemisphere of the U.S. House of Representatives. Hearings on U. S. Policy Towards the Americas in 2010 and Beyond. March, 2010.

The United States of America and the member states of the Caribbean Community (CARICOM) share common traditions and goals of peace, democracy and prosperity. There has been a long-standing relationship of friendship between the governments and people of the United States and CARICOM in which the region is recognized by the United States as its Third Border. The United States in the post-World War II period has been the major economic partner of CARICOM, as is evident in the flows of trade, investment, tourism and migration.

U.S. foreign policy has an important impact on the economic progress of the CARICOM countries, and economic development is an essential foundation for peace and democracy in the region and an efficacious antidote to drug trafficking, transnational crime and social violence. The economic development of CARICOM is in the national interest of the United States.

POLICY RATIONALE: Acute Vulnerability of Small Middle-Income Developing Economies

The distinguishing characteristic of small middle-income developing economies (SMIDEs) is acute vulnerability to exogenous external events. The extent of vulnerability is more pronounced in small middle income developing economies (SMIDEs) because of the high degree of openness, narrow range of economic activities, concentration of exports, limitations of economies of scale and constrained competitiveness of small markets. The structural economic vulnerability is compounded by the proneness of the island states of this region to natural disasters including volcanic eruptions, hurricanes, tsunamis and earthquakes. The frequent incidence of natural disasters deprives the region of a significant portion of GDP on an annual basis.

To date this acute vulnerability has not been fully appreciated and is not adequately reflected in the financing facilities and the accompanying conditionalities of the multilateral financial institutions. The appropriateness of the policy requirements and the scheduled duration of adjustment are still open to refinement. Stabilization is not an end in itself; it is a necessary but not sufficient condition for the restoration and promotion of sustainable economic growth. Therefore stabilization must be linked with and facilitate adjustment and transformation. If these goals are to be accomplished in the context of a global economic recession, great care must be exercised in the application of macroeconomic policy platforms that rely predominantly on deflationary fiscal and monetary policy. Short-term policy must not undermine the building of long capacity for international competitiveness through investment in the expansion and

improvement of human resources and modern infrastructure. Economic adjustment must be adequately financed over a suitable term that is politically feasible and socially tolerable.

CONTEXT: The Impact of the Global Financial Crisis

The acute degree of vulnerability means that the SMIDEs of the Caribbean have been more profoundly and adversely affected by the global financial crisis than the developed economies and most developing countries. That these effects have not attained the international notoriety that accompanies dramatic economic collapse is a tribute to the creativity and political courage of policy making and economic management and to the enterprising people of the region. These economies cannot initiate an economic recovery from the deleterious effects of a global recession with deflationary macroeconomic policies, nor can they avoid the deleterious effects by resort to fiscal stimulus. Like those economies more able to provide them, SMIDEs warrant stimulus packages aimed at employment creation, maintenance of social safety nets and enhancement of international competitiveness. These economies require adequately funded remedial economic programs designed specifically to address their structural and institutional characteristics. Financing such economic programs requires a combination of external funding at concessionary terms over a development-oriented timeframe.

RESPONSE: A Growth-Promoting U.S. Foreign Policy

The SMIDEs have the best prospect of achieving sustained economic growth and, indeed, economic development if they pursue sound economic strategies; this prospect is complemented by a growing global economy. The governments of the developed countries and the large developing countries of the G-20 must refrain from policies—in particular, protectionism—that inhibit access to their markets. The United States, given its unique role in the world economy and as main economic partner of CARICOM, must continue to play a leadership role in shaping and nurturing an international economic environment which is sensitive to and supportive of the economic requirements of the SMIDEs. There is an umbilical link between the resumption of tangible growth rates in the SMIDEs of the Caribbean and the economic recovery of the G-20 engines of global growth via export demand, tourism, private capital flows and remittances. The United States can start by implementing economic policies and a foreign policy that actively promotes growth in CARICOM. Measures to this end should include adequate levels of the appropriate kind of development support, an enhanced trade regime which encourages CARICOM exports of both goods and services, measures to stimulate private direct investment; moreover, they should prompt an increased level of development financing from multilateral development institutions, facilitate the restructuring of debt to manageable proportions and provide for sustained aid for reconstruction of Haiti.

The elements of a growth-promoting U.S. foreign policy for the SMIDEs of CARICOM must include (a) sustaining and promoting opportunities, (b) alleviation and/or elimination of

constraints and impediments and (c) facilitating the attraction, mobilization, creation, allocation and utilization of resources.

The actions of the United States will not have an impact on all aspects of the multidimensional process that is development; they must be complementary to national development strategies within domestic social and political environments which are conducive to development and consistent with a deepening regional integration process aimed at creating an enlarged, seamless region-wide economic space.

1. OPPORTUNITIES

A. Expanding Trade

The United States is the largest trading partner of CARICOM, although its share of the region's trade has declined due to diversification. U.S.-CARICOM trade takes place within the framework of the Caribbean Basin Trade Promotion Act (CBTPA) which is in force until September 2010. The CBTPA allows imports from CARICOM to enter the United States free of duty.

CARICOM has written to various members of the House and Senate indicating that it is "most heartened" by the initiative of Senators Ron Wyden (D-Ore) and Bill Nelson (D-Fla) on February 2, 2010 of introducing S. 2978, the objective of which is to extend the duration of the CBTPA to September, 2013. The Governments of CARICOM believe that the continuation of preferential trade arrangements will be beneficial to their economies. They are not ready at this time to sign a free trade agreement (FTA) with the United States because their economies require more time to prepare for such a possibility. In the past the Office of the U.S. Trade Representative has indicated that such a FTA would be similar to CAFTA. The leadership of the region's governments and private sector believe that CARICOM economies cannot cope with an FTA with the United States. Further liberalization of market access for imports from the United States would have to be implemented in a manner similar to that of the recently concluded CARIFORUM-EU Economic Partnership Agreement. The Agreement is based on preferential treatment in the form of asymmetrically phased schedules of liberalization over periods in some cases as long as 25 years. Adjustment is facilitated and supported by development assistance funds and technical assistance, and takes account of the need to maintain the integrity of the regional economic integration process.

The United States has been urged by CARICOM to support special and differential treatment for small developing economies in the design of the Doha Development Agenda of the World Trade Organization (WTO). Special measures afforded them will be consistent with the S&D provisions of the WTO and would in no way disrupt international trade because these economies account for less than 1 percent of world trade. CARICOM continues its support for Aid for Trade as an indispensable means of improving the ability of developing countries to benefit from participation in an increasingly open international trading system.

The policies employed for the stimulation, acceleration and consolidation of the economic recovery of the U.S. economy and the world economy will also have a procreative and energizing impact on CARICOM. This will be manifested in the resurgence of tourist arrivals and expenditure, exports, remittances, loans, financing and direct foreign investment.

B. Promoting Private Enterprise Synergies

The U.S. business community, if provided with the right sort of encouragement from the U.S. Government, can help to reinforce a market-driven, private-enterprise-led growth process in CARICOM economies. Numerous CARICOM-owned firms and foreign corporations operating in CARICOM countries have demonstrated the capacity to be internationally competitive in a world economy in the throes of profound globalization. There are private sector synergies between the United States and CARICOM which are yet to be brought to fruition to the benefit of both economies as they struggle to restart a globally engaged dynamic for rapid and sustained economic growth.

The catenation of locally owned firms and U.S. corporations, particularly those of small and medium size, through strategic corporate alliances, can drive increased trade and investment. The United States should, in collaboration with the governments and private sectors of CARICOM countries, initiate a study to identify the institutional and policy measures that could be taken by both sides to increase foreign investment in both directions.

The International Finance Corporation (IFC) and the Inter-American Investment Corporation (IIC) can perform an invaluable service in funding the private sector of CARICOM in the current conjuncture of uncertainty in international capital markets. The International Finance Corporation, the private sector arm of the World Bank Group, has increased investment and advisory projects in the Caribbean. Since July 2008, IFC has invested more than \$133 million in 21 projects in the CARICOM region, including investments and advisory services.

The IIC has significantly increased its operations after a slow start in which both the IIC and the private sector of the CARICOM region were involved in a learning process. The portfolio has grown from \$2.7 million in 2007 to \$53.9 million at the end of 2009 and a further \$16 million is in the pipeline as of February 2010. The IIC must continue to expand its technical assistance to the private sector of the region in the form of energy audits, diagnostic studies and workshops, especially for local companies, which are very small by global standards.

2. RESOURCES

A. Increasing US Development Assistance

The U.S. development assistance to CARICOM countries, with the exception of Haiti, has declined from the mid-1980s. Many in the region have interpreted this as a sign that the United States does not regard CARICOM as a priority. The decline in U.S. aid has been accompanied by

the rise in importance to the region of economic aid from Venezuela and China. The United States should significantly increase its development assistance to CARICOM countries because this type of resource is still urgently needed to boost acutely vulnerable development processes in these SMIDEs.

There needs to be a better understanding: middle-level per capita income is an illusion masking acute economic vulnerability and a severe fragility in the nature and process of the region's economic growth. The SMIDEs have done relatively well compared to the majority of developing countries but this does not obviate the value of development assistance. Indeed, there is an ongoing role for an appropriate type and amount of development financing in modernization of infrastructure, enhancing education, stimulating an internationally competitive business environment, nurturing a market driven business culture and the strengthening of institutional capacity. These are secondary drivers are essential components for the transformation to sustainable and resilient economic growth and their efficacy cannot be enhanced and accelerated by development assistance. Current focus of development assistance is on poverty alleviation and basic development needs of lower-income, less-developed countries and this results in an insufficient recognition of the needs of CARICOM countries because of their middle level per capita income.

The United States should eschew efforts to graduate the SMIDEs of CARICOM from the concessionary facilities of multilateral development banks by the explicit recognition and application of the more relevant criteria of vulnerability to the allocation of development assistance.

B. Redimensioning Multilateral Development Lending

The World Bank's current portfolio in the CARICOM countries includes 45 projects for a total of \$733.7 million. These operations focus inter alia, on economic policy, urban development and education, catastrophe risk insurance, disaster risk management, HIV/AIDS prevention and control, biodiversity conservation, management of climate change impact, public sector modernization and telecommunications. The World Bank should substantially increase the amount of resources provided to CARICOM countries.

The Inter-American Development Bank (IADB) has proved vital development funding to CARICOM countries. The Caribbean constituency has had 53 loans amounting to \$1.2 billion. During 2009 the Caribbean constituency (the Bahamas, Barbados, Guyana, Jamaica and Trinidad and Tobago) received \$495 million in loans following on \$404 million in 2008. To date in 2010 a further \$235 million has been approved. These projects include policy-based lending and investment loans for infrastructure, education, water, agriculture, sanitation, energy and coastal protection. The IADB must be endowed with additional resources to enable it to continue its policy-based lending and counter-cyclical financing, and to expand its conduit of resources to the SMIDEs of the hemisphere, notably those of CARICOM. It is important that the smallest of the

CARICOM economies continue to access resources from the IADB through the Caribbean Development Bank (CDB).

The Board of Governors of the IADB have agreed to increase the capital of the Bank by \$70 billion, and the United States and other donor members must move expeditiously to complete the domestic political processes to give tangible effect to this commitment.

Multilateral development banks and bilateral aid agencies must remain fully cognizant of the fragility of SMIDEs while endeavoring to achieve meaningful poverty alleviation on an ever-increasing scale. There is a temptation to succumb to the blunt quantitative criteria of per capita income as a measure of development needs. Such a fixation raises the spectre of graduation of SMIDEs from the concessionary facilities. This is an ironic disqualification of those who by dint of careful management, public initiative and private enterprise have attained middle-income status despite their small size and paucity of resources. The CARICOM countries have made progress, but their quest for the higher levels of development could be frustrated by inadequate development funding.

C. Expanding the Caribbean Development Bank

The CDB has embarked on policy-based lending and hence will have to be the purveyor of this type of funds, whether from its own resources or as a lending institution. The CDB is due for a replenishment of its capital and although the United States is not a member it can contribute to the lending resources of this Bank.

The IADB provides resources to the CDB for disbursement to the member states of the Organization of Eastern Caribbean States (OECS), which are not members of the IADB. These countries are eligible for IADB funding through the CDB by a special amendment to the IADB Charter in 1977. Since then the IADB has approved 8 loans worth \$104.5 million and 13 technical assistance grants totaling \$6 million. The major beneficiaries were Dominica, Grenada, St. Lucia and St. Vincent. The IADB should continue the practice, which the Charter contemplates, of treating the CDB as if it were a sovereign borrower.

3. CONSTRAINTS/IMPEDIMENTS

A. Facilitating Debt Reorganization

The economies of the Caribbean are among the most heavily indebted among the emerging economies. Reorganization of external and domestic public-sector debt would be instrumental in providing the urgently needed fiscal space and alleviate pressure on interest rates and exchange rates. It would allow governments to have less resort to borrowing and to reorient fiscal policy to be a tool of development policy in contrast to being confined by the strictures of taxation and borrowing driven by sizeable fiscal deficits. The creation of a facility for debt reorganization in SMIDEs is urgently needed at this juncture, when access to international capital markets is still

prohibitively expensive and policy-based lending needs to be re-dimensioned. These economies have structural impediments similar to those of less developed countries but do not qualify for HIPIC treatment and are not large preferred borrowers of private sources of finance.

B. Enhancing Sustainability and Resilience

The countries of CARICOM, whether they are island states or part of Central and South America, are coastal societies. The vast majority of the population lives and works on the coast or within a few miles of the sea. Many of the vital economic activities—notably tourism, fishing and shipping—are sited on the beach and depend on the quality of coastal and sea resources. Climate change poses a clear and present danger to the region and requires immediate action. The identification and mobilization of resources to enable the governments of the region move quickly to formulate and implement suitable policies is a natural role for multilateral development banks. Any deterioration in the environment of the Caribbean will have a deleterious impact on the region and indeed, on the globe.

The Caribbean region has a history of being highly prone to and susceptible to natural disasters including annual incidents of powerful, hurricanes, earthquakes (most recently in Haiti), and volcanic eruptions as in Montserrat. Perennial hurricanes have caused damage to the CARICOM countries amounting to a considerable share of GDP. The global community has to devise a more systematic medium-term mechanism to sustain redevelopment after the relief efforts are completed. This is a challenge that the United States is well acquainted with, having experienced the destruction caused by Hurricane Katrina.

RECONSTRUCTION: Haiti

The World Bank and the Inter-American Development Bank must be commended for their response to the devastation in Haiti. The World Bank has indicated that it will provide an additional \$100 million for Haiti. The IADB has announced the cancellation of Haiti's debt to that institution, converted the undrawn portion of outstanding loans to grants and established a special department dedicated to the reconstruction of Haiti. Both institutions have signaled their commitment to the long-term redevelopment of Haiti.

The government and people of Haiti are neighbors and a member state of CARICOM, and, consequently, CARICOM intends to be a full participant in the process of reconstruction and development. It should be recalled that CARICOM has been requested and designed by President Preval to carry out certain representational functions on Haiti's behalf.

Haiti's recent experience graphically dramatizes the general point about vulnerability by demonstrating the devastation which natural disasters can cause in the economy and society of a small developing country.