

The Treaty of Chaguaramus envisaged progression towards a comprehensive economic community, beginning with tariff arrangements, the harmonization of fiscal incentives and institutional strengthening. The Caricom institutions and associated institutions for regional cooperation have proved durable but the deepening and strengthening of economic links envisaged by the framers of the Treaty have not materialised. Economic integration continues to be seen as a high priority for the Caribbean region particularly now that countries much larger have seen the need for economic unions. The relative economic success of the union of the Organisation of East Caribbean States (OECS) in contrast to the economic retrogression in Jamaica, Guyana and Trinidad and Tobago suggests that integration may improve economic prospects. However, there is growing frustration at Caricom's failure to mature as an economic unit. A reassessment of the Caricom experience is a first step to identifying and removing the roadblocks to further economic integration.

Trade

The Caricom market offers limited potential for intra-regional trade because of market size and economies of scale. With a population of five million and per capita incomes averaging about US\$2,000 the Caricom market is not large enough to support many firms of an internationally competitive size in any activity. Inevitably, most countries will try to specialise in the same limited range of items. The range of feasible production is so narrow that vigorous protective measures can enlarge the proportion

of local production very little as the experience of Trinidad and Tobago and Guyana shows.

The possibilities narrow further when one takes account of the geography of the market. Caricom may be regarded as a single market only for goods and services whose value is high relative to the cost of transporting them. The line of demarcation between products for which Caricom may be seen as a single market and others is not sharply drawn and national markets may be extended by product differentiation and marketing. However, the difficulties of regional market penetration increase sharply as the ratio of value to transaction costs decreases.

Transport costs within the region are a market inhibiting factor. Costs vary inversely with the volume of traffic. Because Caricom trade is a minor proportion of the total trade of member states intra-Caricom transactions costs are invariably higher than for trade with the rest of the world.

Much of Caricom trade is a result of income differentials between members. For example, Barbados' boom in manufacturing exports to Trinidad and Tobago in the late 1970s resulted from Barbados' lower per capita income and wage costs. Similar considerations are now motivating a resurgence of exports from Guyana to the rest of the region. As the integration movement succeeds in achieving convergence of

regional economic performance these differentials will be reduced, reversing somewhat the increases in intra-regional trade.

The disappointment with the performance of intra-regional trade is, to some extent, a result of unrealistic expectations for greater self-sufficiency. The political sentiment has been far more protectionist than the intellectual justification provided for the founders of Caricom. The intellectuals recognised that similarity of production structures limited trade potential.

Balance of payments crises of individual countries have had an adverse effect on intra-Caricom trade. A fall in member countries' real spending power caused a contraction of all imports, including imports from Caricom partners. These effects were especially powerful because of the contraction of Trinidad and Tobago, the region's largest economy, and of Jamaica, the second largest. The contraction for Guyana was particularly dramatic; that country shrunk from No. 3 in the economic rankings to last place.

The balance of payments effects were aggravated by misguided policies and misperceptions. Restrictions on imports from other Caricom countries, implemented in blatant defiance of the Caricom Treaty and without consultation with other members, were the most pernicious. Imports from Caricom were so minor in relation to total imports that countries did nothing to alleviate balance of payments problems

by banning them. Import restrictions were circumvented in any case, though usually to the benefit of Caricom producers.

There is a misperception that Caricom trade would have persisted but for restrictive practices. In truth, trade would have declined anyway because of the decline in regional purchasing power represented particularly by income contractions in Guyana, Jamaica and Trinidad and Tobago.

The Common External Tariff (CET)

The Caricom CET has been a symbol of regional frustration. In its original form it was one regime for so-called More Developed Countries (MDCs) of Caricom, a second for Less Developed Countries (LDCs) and special regimes for Belize and for Associated Territories which were not independent countries. Most LDCs have not completely implemented the regime intended for them. The scheme was revised in the early 1980s but the revision was not implemented. New deadlines for implementation were set at the Heads of Government Conference at Grand Anse, Grenada in 1989. However, by the time the deadlines arrived member countries were on second thoughts. A new compromise has been established for the CET and a schedule for reducing tariff rates under the CET was agreed early in 1993. The implementation deadline is set for June 1993.

The importance of the CET is vastly overrated. Trade will grow no more than in proportion to the rate of growth of incomes; if incomes converge trade will grow more slowly as the price advantage of low-cost regional sources diminish. Trade potential is limited to a range of processed foods, toiletries, clothing and furniture.

Trade Liberalization

Recent initiatives to liberalize trade by removing licences and non-tariff barriers will have a more significant impact on regional trade than changes in the CET. The process of trade liberalization has been underway since the mid-1980s, beginning in Jamaica. Many other countries have followed Jamaica's lead but extensive licensing systems affecting imports from Caricom remain in force in the OECS countries; most of them are permitted under the Caricom Treaty:

Tourism

Intra-regional tourism illustrates the fact that regional transactions are driven by income rather than tariffs. The patterns of Caribbean visitors to Barbados and Grenada, both of which draw a significant proportion of their tourists from within the region, closely parallel the problems of their exports of goods to the region. This suggests that both trade and tourism are affected by the same cause, that is, the ability to spend, particularly of Trinidad and Tobago.

The Agricultural Marketing Protocol (AMP)

The Chaguaramus Treaty, like most trading arrangements, made special provision for agricultural trade under an agricultural marketing protocol (AMP). The MDCs undertook to purchase certain basic foods such as edible oils from regional sources. The AMP seems to have worked reasonably well for the limited range of items identified at the outset despite the occasional complaint that market access was denied. However, the agreement was not successfully extended to a wider range of agricultural products and the administration of the AMP proved cumbersome.

The framers of the Treaty envisaged considerable intra-regional trade in foods, with land-rich Belize and Guyana supplying cereals, meat and fruit to the rest of Caricom. At the same time, they wished to realise the potential for extra-regional exports of non-traditional food crops. The Caribbean Food Corporation was set up to engage in trade, within the region and with the rest of the world. It has not had a substantial impact, perhaps because it has had to divide its attention between these two areas. It might have been more successful had it focussed exclusively on extra-regional exports.

Industrial Programming

In an effort to increase complementarities among regional economies provision was made for agreement on industrial programming. Countries would express a preference for some kinds of industry rather than others so that manufacturing sectors would

become diversified over time. Countries' specialisation and complementarity would also increase international competitiveness and extra-regional exports.

Attempts to engineer this process by allocating industries to countries met with no success. No country was willing to withdraw benefits that existing industry enjoyed, even in areas where other Caricom countries produced more competitively. Apart from a few natural resource-based industries, such as petro-chemicals in Trinidad and Tobago, few activities recommended themselves for location in one country rather than another.

The experience of successful exporters indicates there is little basis for predicting the location of industry (the cost of labour of comparable skill is often cited but that may well determine the choice of technology rather than the locus of production). Social, political and institutional factors may well be critical.

Efforts to determine the country bias in manufacturing production were misconceived. A more productive line of attack would have been to focus on technical assistance, finance and market development assistance for firms that were prepared to take export initiatives. Rather than force industrial production in pre-determined directions, policy should follow the lead of industrialists who have a good track record and the institutional strength to develop new markets.

Export Promotion

Contrary to popular notion the founders of Caricom never envisaged the union principally inward-looking. Import substitution was seen as important complementary to a more diversified range of extra-regional exports. Emphasis on regional harmonization of fiscal incentives was largely in recognition of the importance of foreign investment in stimulating regional production for exports. Studies which informed the foundation of Caricom, included projections for the regional combination of resources to produce items with a higher value added for extra-regional export.

However, at the time of the Treaty signing in 1973, the challenge of developing new export markets was seriously underestimated. Attention focussed exclusively on production and products. This situation was only rectified - partially - in the 1980s with the setting up of the Caricom Export Development Project (CEDP). It has its mandate to provide support systems for regional exporters of manufacturing and agricultural goods. CEDP has succeeded in raising the profile of exporters and provided technical assistance and other support services but it has not been allocated resources commensurate with the task it is called upon to perform. While its trade promotion activities have gained momentum in recent times its trade information systems remain underdeveloped, underfunded and underutilised.

Payments

The OECS countries share a currency but by the time of Caricom's establishment all other members had their own currencies. Transactions could be carried on between countries in these currencies, which all had fixed values, initially in terms of sterling and by the mid-1970s in terms of the US dollar. Central banks arranged to clear regional payments for commercial banks and established bilateral accounts among themselves. Outstanding balances on these accounts were settled monthly in US dollars.

In order to economize on the use of US dollars for settlement and to minimize the number of accounts, the central banks decided to replace the bilaterals with a multilateral clearing facility headquartered at the Central Bank of Trinidad and Tobago. The Caricom Multilateral Clearing Facility (CMCF) held a single account for each member bank through which all intra-regional clearings were made. Settlement of outstanding balances was done quarterly. Partial settlement of 50% of the outstandings was allowed, provided the debtor central bank was below the credit limit, set for each participating central bank.

The CMCF foundered in 1984 because the Bank of Guyana was allowed to pass oil payments to Trinidad and Tobago through the Facility at a time when it had no foreign exchange with which to make settlement. Furthermore, when the Bank of Guyana

reached its credit limit no action was taken. When Guyana had utilised the credit limits of all the other central banks the CMCF was suspended.

The demise of the CMCF was unfortunate because it was a clever device for effecting small but significant economies in the use of foreign exchange. The CMCF might have formed an institutional base for the planned federal system of Caricom central banks.

However, the popular conception that the collapse of the CMCF contributed to the decline in regional trade is without foundation. The multilateral system, which was reinstated, performs exactly the same functions as the CMCF in clearing trade payments. The problems of settlement result from exchange rate uncertainty, not from any deficiency in the payments system. Financial institutions refuse transactions in regional currencies when they are unsure of the value they will receive when drafts in regional currencies are presented to the issuing central banks. They would have had no reason to behave differently had the CMCF been in operation because in a regime of floating rates the CMCF would not know in advance the value that regional currency items would fetch on the day of presentation. The problem is an absence of forward markets in regional currencies, not the suspension of the CMCF.

Balance of Payments Support

The studies that informed the creation of Caricom envisaged a form of balance of payments support for members based on the pooling of foreign exchange reserves. The exports of the Community as a whole are more diversified and therefore fluctuate with less volatility than the exports of any member. Any member could cushion a temporary terms of trade loss through access to finance and foreign exchange shared with the Community as a whole.

Formal mechanisms for burden-sharing were expected to be developed later in the Community's life. However, events in the form of the first oil shock overtook Caricom. For one thing, terms of trade changes were of a magnitude never envisaged by the framers of the Treaty of Chaguaramus. The fact that the largest members suffered heavy adverse shocks meant that burden-sharing might have served to impoverish smaller members. There needed to be rules to prevent this.

At the event a short-lived boom in commodity prices cushioned the impact of the first oil shock temporarily; balance of payments problems emerged in Jamaica and Guyana only in the second half of the 1970s. Trinidad and Tobago, Caricom's only oil exporter, was in a position to offer balance of payments support to Jamaica at the head of a regional consortium to which other Caricom Central Banks made small contributions. Unfortunately, Jamaica's policy regime failed to restore that country's

balance of payments to equilibrium so the balance of payments support loan served only to ameliorate an import shortage for a short period. The amounts committed to the balance of payments support loan for Jamaica were not large enough to constitute a burden on the lenders who all maintained healthy foreign exchange reserve levels.

The CMCF, previously mentioned, operated as a limited balance of payments support financing facility. The outstanding balances which debtor banks were allowed to hold with the Facility in their own currencies constituted a temporary credit facility which had to be reduced quarterly but need never have been eliminated. The demise of CMCF emphasises the need for strict limits on members' access to balance of payments financing if large poorly managed economies are not to depress income throughout the Community.

Trinidad and Tobago inadvertently provided Guyana with in excess of US\$400 million in balance of payments support in the early 1980s by supplying oil on credit. By that time, oil prices had been halved from the 1979 peak and Trinidad and Tobago no longer had foreign exchange reserves sufficient to afford such largesse. A series of negotiations between the parties has so far failed to produce a mutually acceptable arrangement for settling these arrears.

Exchange Rates

The devaluations of the Guyana dollar, the Jamaica dollar and the Trinidad and Tobago dollar and their switch from fixed to floating exchange rate regimes over the last three years, constitute serious challenges to regional trade and finance. On the other hand, regionalism, in the form of a monetary union, offers the best opportunity to achieve the economic stabilization which is the objective of the new exchange rate strategies. Exchange rate instability has encouraged the prospect of advancing quickly towards monetary union as a means of stabilizing currency values and achieving policy convergence.

At the time of the Chaguaramus Treaty no mechanism was set up to deal cooperatively with changes in the status of currency pegs. As a result, countries which had not already switched from a sterling peg to the US dollar did so in a haphazard fashion and at a variety of rates. That was a nuisance but it did not hinder any regional transactions so long as the parities remained fixed.

Neither Caricom institutions nor national governments acknowledged that fixed exchange rates could be maintained only by the imposition of appropriate fiscal discipline. The Treaty makes provision for consultations on policy coordination but no effective mechanisms were set up. There remains a reluctance at the regional level to advise on fiscal policies. That is still regarded as treading on members' sovereignty.

Inappropriate fiscal policy led inevitably to the devaluation of the Guyana, Jamaica and Trinidad and Tobago dollars, from the late 1970s onwards. The devaluing countries gained a temporary price advantage to which some Caricom partners retaliated by imposing quotas and bans on the devaluing countries' exports. This defensive action did more harm than good, boosting uncompetitive domestic production without compensating for the loss of regional market share.

Balance of payments disequilibria, which should have been corrected by prompt fiscal action, instead provoked trade interventions, exchange controls and credit restrictions which disrupted Caricom transactions as well as commerce with the rest of the world without alleviating the balance of payments problem. The long period of reluctance to admit the fiscal constraint has left much uncertainty about the value of devalued currencies even when fiscal prospects seemed right for a stable value. This continues to be a factor inhibiting trade and capital movements. Potential investors must anticipate future relative values of Caricom currencies and many prefer to "sit on the fence" while the situation remains unclear. Investment may go forward in sectors which earn foreign exchange, but even in these cases, future trends in domestic costs, and therefore in net returns, remain uncertain.

Monetary Union

The Chaguaramus Treaty envisaged monetary union as a distant goal coming at the end of a long process which began with a customs union, developed through closer economic cooperation and coordination to bring about a measure of uniformity in monetary policy. Viewed from this perspective, monetary unions seems farther than ever from realisation because of the frustration over trade policy.

In recent times, it has come to be realised that monetary union is a mechanism that may be used to achieve objectives of trade policy and more importantly, to stabilize the balance of payments and currency values. The private sectors of countries with depreciating currencies have become disenchanted with unending loss of currency values. Informal rationing arrangements have been introduced by financial institutions in all three countries with floating rates to try to stabilize the exchange rate. The virtue of a predictable value of the currency is now generally recognised.

The example of the OECS states, which operate as a monetary union, suggests this as an effective device for securing a stable exchange rate. The monetary union, if it is set up with rules similar to the operating guidelines of the East Caribbean Central Bank (ECCB) lends credibility to governments' commitment to fiscal policies that keep the exchange rate stable. Once government has been forced to devalue the exchange rate, it finds difficulty in convincing the private sector there will be no further devaluation, no matter how tight the fiscal corset is drawn. There is nothing to

guarantee that social and political pressures which led to the first devaluation will reemerge. To make its commitment believable, government must deny itself access to the central bank as a source of deficit financing. It may do so by introducing legislation to secure central bank independence. Joining a monetary union is more convincing. It ensures that government may not unilaterally change its mind or revoke the independence of the central bank.

Caricom has made no real progress on policy coordination but the Heads of Government have now committed themselves to achieve a monetary union. Tentative steps have been taken with the establishment of a Caricom Council of Central Bank Governors.

Other Policy Coordination

The Caricom record on the coordination of economic policy is undistinguished. In respect to external economic relations the negotiation of the Lomé Agreement was the only achievement of significance. Acting as a group, the Caribbean gave decisive leadership in the negotiations between the African, Caribbean and Pacific nations and the European Economic Community. Their carefully argued position was a major factor in the conclusion of a trading and finance pact which is exempt from many ways.

Caricom failed to repeat this performance in negotiations over free trade arrangements with North America, in negotiations with the international financial institutions over domestic economic policies, in international debt negotiations and in any other area of external economic policy. Negotiations for a free trade arrangement with North America have been undertaken at a Caricom level but the agenda is dictated by the priorities of individual countries in their relationships with the United States.

In negotiation with international financial institutions each country has gone its own way. Ad hoc arrangements to share expertise and experience among countries have been arranged but there has been no attempt to bring a regional presence into bilateral negotiations with the international financial institutions. This has led, in the case of trade reform, to policies which are ill-conceived and inappropriate both from the national and regional points of view. Bowing to pressure principally from the World Bank, trade reform in Jamaica and Trinidad and Tobago has been accelerated at a pace which promises to lead to contraction in domestic manufacturing with no commensurate increase in extra-regional exports and only temporary gains in regional manufacturing trade. Moreover, the loss of Government revenues aggravates constriction on Government expenditure to balance the budget.

There are no mechanisms for a regional voice in national policy-making to ensure that policies do not lead to balance of payments divergences between members. It has taken too long for national decision-makers to accept that policy oversight is

necessary to ensure that economies achieve regional compatibility. Exchange rates among Caricom countries may not be determined by the balance of payments on Caricom transactions alone because these are only a minor item in the factors that determine the country's net demand for foreign exchange. In order to ensure the predictability of intra-Caricom currency values countries' balance of payments with the world as a whole must be stable. That requires regional oversight of fiscal policy, the major tool of balance of payments adjustment.

The harmonization of fiscal incentives for investment in Caricom has been a significant area of policy coordination. Fiscal incentives are not generally thought to be a determining factor in the investment decision. However, in an international environment where such incentives are universally available, countries need to offer them to get onto a level playing field. The Caricom system forms the basis for tax and other incentives to industry in all countries thereby avoiding "beggar thy neighbour" tactics within the Community. In keeping with the two-track philosophy embedded in the Treaty more generous provisions are allowed for the LDCs. In the changed economic circumstances of the 1990s that is not probably no longer logical but the differences are not significant enough to warrant reopening of the issue.

Capital Movements and Investment Financing

The performance of the Caribbean Development Bank, the regional development bank, is a success story of the regional integration movement. The Caribbean Development Bank has mobilised over \$1,000 million dollars in project finance from the region. Some part of these resources might have been available to individual countries but by most accounts CDB's presence has been a magnet for additional funding. Small territories of the East Caribbean are not members of some international financial institutions and might not have attracted funding on their own; CDB has been their conduit from these institutions. Also, many lending agencies such as the European Community designate funds for regional projects. Although that definition is somewhat loosely applied, the presence of overtly regional institutions raises the likelihood of attracting funds which are designated for regional projects.

The CDB has striven to accelerate disbursement of loans and their effective use by programmes of technical assistance and training. Over the years, it has made a considerable contribution to enhancing human resources for project implementation and business development. The Bank's major challenge is to augment its resources substantially so that it can play a much larger role in the development of Caribbean infrastructure for growth and private sector investment. It might also become more active in regional policy-making, particularly in the development of structural adjustment strategies tailored to Caribbean needs.

Caricom has had little effect as far as private capital flows are concerned. In regional capital flows are inhibited by exchange controls, uncertain currency value, countries which have no exchange controls, incompatible tax administration, restrictive laws on property transfers. A Caricom Enterprise Regime was established in an effort to circumvent these difficulties. Caricom enterprises are to be entitled the same privileges as domestic firms in every Caricom country. The Caricom Enterprise Regime has had negligible impact. Administrative processes for certification as a Caricom enterprise are long and cumbersome and the supposed benefits are automatic and are highly qualified. Although the Caribbean Association of Industries and Commerce (CAIC) pushed energetically for the adoption of the Caricom Enterprise Regime, few private entrepreneurs now evince an interest.

A major initiative in recent years was the establishment of facilities for cross trading on the securities exchanges of Barbados, Jamaica and Trinidad and Tobago, the active exchanges in Caricom. After an initial bout of activity, cross border trading virtually dried up because of exchange rate uncertainty. The potential for regional capital market transactions is considerable but it will be realised only if exchange rates have stabilised. Conversely, failure to stabilise exchange rates creates the risk of speculative market interventions which might aggravate nervousness about any exchange rate that seemed under threat.

Significant private capital transfers have been effected via joint ventures between companies in different Caricom countries. This investment totals only a small proportion of capital formation for any country but individual country projects may be quite large by Caricom standards. Since perhaps 80% of private capital fixed formation in some Caricom countries is financed from retained earnings or other own finance, this trend of joint finance is a promising one.

Regional institutions have not especially focussed on attracting foreign capital for investment in joint ventures. CAIC has taken some initiative in this respect but its efforts have been limited by inadequate funding.

Labour Mobility

The regional integration movement has failed to secure any liberalization in regulations against labour mobility within Caricom. By and large member countries treat Caricom nationals no differently from other non-nationals. Freedom of movement was envisaged as an aspect of the maturation of regionalism to be attained in the later stages of the union. Until recently, no attempt was made to bring the issue to the top of the regional agenda.

The integration concept has now shifted away from the notion of stages of unification starting from "easy" trade mechanisms and moving towards "difficult" factor market integration. This change in approach was reflected in the Grand Anse Declaration of 1989 which set limited freedom of movement of persons as an immediate goal. Alas, the change of concept did not ease the way to implementation and the first steps towards greater labour mobility are yet to be taken.

Institutional Strengthening

An important achievement of integration efforts has been the evolution of durable institutions in the many areas of what are known in the Chaguaramus Treaty as "functional cooperation". The University of the West Indies, now 44 years old, has developed a corpus of alumni whose contribution to the development of Caricom is wide and deep. The Caribbean Examinations Council has established standards of secondary achievement that are internationally comparable. Its innovations in some areas are being emulated in industrial countries. The Caribbean Association of Industry and Commerce has forced durable links among the largest firms in the regional private sector. The Caribbean Congress of Labour has done the same for workers' organisation.

The Caricom Secretariat and the numerous standing committees of Caricom have developed a rich network of knowledge and capability which, with better mobilization might strengthen the Caribbean's voice in international affairs.

There are, in addition, numerous affiliated institutions of Caricom, and more numerous regional professional, technical, sporting, cultural and voluntary associations. In the course of its regional consultations, the West Indian Commission took note of over 100 regional institutions which are listed in the appendix of its report Time for Action.

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June 4, 1993

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