CAPITAL MOVEMENTS - THE EXPERIENCE OF COMMONWEALTH CARIBBEAN COUNTRIES, 1970-84

by

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Introduction

Encouragement of capital flows from the industrial to the developing nations was widely accepted as an important element of international development strategy in the early post-war years. With the recovery of the European nations from the ravages of the War, and the emergence of many former colonies as independent nations, this position took a stronger hold, and in 1961 when the first United Nations Decade was launched, it was proposed that the developed nations should aim at transferring 1 per cent of their national income to developing nations as financial assistance.[1] This target (which incidentally covered both official and private capital flows) was subsequently adopted by the UNCTAD Conferences of 1964 and 1968[2], as well as by other forums. The Pearson Report,[3] for example, published in 1969 endorsed the 1 per cent target and suggested 1975 as the date for meeting it. It, however, went further and recommended that development assistance should be increased from 0.39 per cent of GNP in 1968 to 0.70 per cent in 1975, 'and in no case not later than 1980'. At the start of the Second United Nations Development Decade in 1970, it was urged that each economically advanced country should endeavour to provide annually by 1972, for the benefit of developing countries, resource transfers in the form of net disbursement of a minimum amount of one per cent of its gross national product at market prices, consideration being given to the special situation of countries which are net importers of capital.[4] Within this overall target a proportion of 0.7 per cent of GNP was set for official development assistance (ODA).

Available data indicate that by 1983/84 the ODA/GNP ratio for Development Assistance Countries (DAC) was 0.36 per cent as compared to 0.34 in 1970/71. For a few countries (including the United States and the United Kingdom) the proportion actually fell in the period. Of the seventeen (17) DAC countries, only five (5) had an ODA/GNP ratio of over 0.7 per cent in 1983/84. In the absence of inadequate official flows to developing countries, and given the difficulties they have encountered in borrowing from multilateral institutions, many of them have turned increasingly to the private markets to finance current account deficits and development programmes. It is estimated that international bank lending now represents more than 50 per cent of international capital flows and more than 50 per cent of total long-term external debt of developing countries. "Claims with a maturity of more than one year now represents about 50 per cent of total bank claims, thus contributing to the medium-term financing of current account deficits."[5] Increasing reliance on commercial bank loans has also been encouraged by inadequate flows of private direct investment. In fact, throughout the 1970s and early 1980s official development assistance grew more rapidly than private investment.

Commonwealth Caribbean countries have not been isolated from the trends outlined above. Several of these countries have ventured to borrow abroad from commerical banks, but in most cases such loans still form a small proportion of the total outstanding debt. The borrowing activities of a few of these countries have been hampered by low credit rating resulting from poor export performance, low or negative growth rates and inability to service past debt. Private capital inflows have dwindled in recent years, and in certain cases there has been a net outflow of funds as a result of dis-investment being larger than inflows. The paper examines the current account performance of the various countries and the main sources of finance since 1970. Some of the issues associated with the various sources of finance are raised against the background of changing financing trends. The paper is divided into three main parts. In the first, we clarify some balance of payments accounting concepts and outline the perspective which assigns to capital imports an important role in the development process. In the second, we examine the experience of individual countries with respect to capital movements. And in the third section, we discuss some issues connected with two major forms of capital flows, viz, foreign private direct investment and government borrowing. In the final part, we present some concluding observations.

The Functions of Capital Imports in a Development Context

In the 1950s and 1960s it was widely assumed that the major problem facing economic development was a shortage of capital. In the absence of inadequate levels of domestic savings and foreign exchange, external resources were needed to cover both a savings-investment gap and a trade gap. In this context, two gaps models[6] came to occupy a prominent place in the development literature. Assuming a simple relationship between capital and output a major purpose of these models was to project external capital requirements, based on certain rates of growth. In the light of the development experience of the last two or three decades and a greater understanding of the development process, such exercises have lost a great deal of their early popularity. This, however, has not diminished the call for a greater transfer of resources from the developed to the developing nations, which is now made with even greater intensity in the context where loan repayments in a number of cases are exceeding annual disbursements and private capital service payments are often greater than new inflows.

Foreign capital flows tend to take a variety of forms. Private direct investment, portfolio investment, government to government (including agencies) loans or grants, export credits, commercial bank loans and lending by multilateral agencies are among the best known. Some loans are made on strict market terms (hard loans), while others may possess varying degrees of grant elements as they relate to interest rates and grace and repayment periods (concessional funds). Some loans have non-financial conditions attached to them. Since each type of finance tends to be associated with different economic and political implications, some observers think a clear distinction should be made between the various kinds of foreign inflows.[7]

From a balance of payments accounting point of view, an attempt (based on theoretical reasoning) is often made to distinguish between autonomous transactions and accommodating transactions, i.e. distinguishing between transactions that are undertaken for their own sake and those which have their source in other transactions elsewhere in the account. In practice, this dichotomy is difficult to maintain given the problems in identifying the motivations of individual transactions, particularly where short-term capital flows are concerned.[8] At one extreme one can adopt an approach that draws the line below the current account balance i.e. treat all capital inflows as accommodating. Some presentations attempt to capture the spirit of the distinction by using a basic balance approach which focusses on the current and the long-term capital balance in an attempt to show long-term tendencies and a balance unaffected by fluctuating easily reversible or speculative flows. In this framework all long-term capital is regarded as autonomous, and all short-term as accommodating. While this approach is useful for some purposes, it does not strictly meet the theoretical rationale. Making a distinction between long-term capital and short-term capital is quite problematical, and often involves an arbitrary approach since conceptions of long and short can differ. In practice, capital with an original maturity of less than one year is generally regarded as short-term. Rather than distinguish between types of transactions, many countries prefer to make the distinction between types of transactors. In this approach, the only item below the line is the official settlements balance. Of course, not all official transactions are accommodating. Given the tendancy to associate welfare changes with the 'balances', many countries prefer to simply publish the details of the various transactions, leaving interested parties to make their own interpretations of events.[9]

A common feature of all forms of foreign capital flows is the association with foreign exchange availability. The importing country gains foreign exchange, while the exporting country loses it in the immediate transaction. Subsequently, the process is reversed when loans have to be serviced, or profits remitted back home, or in the event of disinvestment. For the capital importing country, foreign funds not only supplement domestic savings, but expand its foreign purchasing power. Foreign capital thus allows a higher level of imports of both consumer and capital goods without a net loss of foreign exchange reserves. It facilitates not only consumption, but investment. By enabling a country to import more than it exports, it discourages the imposition of exchange and trade restrictions, and thus prevents the distortions to which such measures give rise in the domestic economy. The adoption of restrictions by one country often invites retaliation by others with adverse effects on trade generally. In recognition of this, the provision of short-term credit to finance balance of payments deficits was a major reason for the establishment of the IMF which has as one of its main responsibilities the liberalization of international trade.

It is often argued that in the short-term developing countries need a continuous flow of capitl, since it takes time to develop the productive base of the economy and to increase productivity. For this reason, private capital of a long-term nature and loans with long maturities tend to be more greatly appreciated. The premise for attracting foreign capital is that the economy will move along a path that not only reduces the need for foreign exchange, but results in a higher national income and a greatly enhanced foreign exchange earning capacity that makes the servicing of foreign capital an easy task for the economy. In this connection, it is often suggested that there should be greater emphasis on attracting equity capital, rather than loan capital, since the servicing of the former depends on the making of a profit, while the latter has to be serviced regardless of how or where it is spent. Very often, however, public borrowing is undertaken in the absence of an inadequate private flows. Since equity investment is more directly associated with private enterprise, the two forms of capital are not completely substitutable, at least in the short term.

Events do not always turn out as theory suggests. Some countries which have long been the recipient of foreign capital have not been able to develop any substantial non-traditional export capacity, and have become increasingly dependent on foreign resources. Structural transformation has proved an elusive goal. One of the arguments for foreign capital is that the initial inflows would generate further investment, income, savings and employment. The extent to which this happens often depends critically on public policy. With respect to private capital, some of the incentives offered to attract foreign investors have not only often proved to be unnecessary, but counter-productive. Inward-looking strategies have in many cases worked against the development of an export potential. As far as borrowing by governments are concerned, a significant part of such loans has been used to finance consumption or spent on prestige projects, which have contributed little to productive capacity.

Donors and lenders themselves often determine where resources go and may finance projects that have a high profile, rather than those that can make the greatest contribution to national development. At the global level, political and strategic considerations rather than need,exert a strong influence on the pattern of resource allocation. Because of these distortions, capital may not flow to activities or areas where its marginal productivity is greatest. Some observers argue that the availability of foreign funds tend to discourage domestic savings efforts. Such funds do not supplement domestic resources, but replace them. Rather than finance investment, it is further contended a large part of foreign capital is used to increase consumption.[10] Econometric studies have shown that in some cases there is not only a negative relationship between domestic savings and foreign capital, but also between the latter and growth.[11]

In the following section we examine the current account performance of individual countries and the main sources of finance.

Bahamas

The Bahamas produces very little of what it needs, either for domestic purposes or for the tourism sector. Imports are critical to the functioning of the economy. While earnings from merchandise exports pay for only a small part (on average about 25-30%) of total import requirements, the foreign exchange from tourism and other services have been able to offset a large part of the trade deficits over the years. Between 1970 and 1974 the country had current account deficits in four years, but this was followed by five (5) consecutive surpluses (see Table 1). There has been a deficit in every year since 1980 totalling B$294.0 million between 1980 and 1984. While the net capital account balances in this period amounted to only B$191.0 million, the external reserves of the Central Bank increased steadily from B$78.7 million at the end of 1979 to B$181.5 at the end of 1985, continuing the trend from 1970.

Though the capital account balance fluctuates greatly from year to year, generally it has been positive, except for three years since 1970, viz, 1978, 1984 and 1985. These balances, however, are substantially less than those of the services sector in the current account. Between 1970 and 1985 they averaged about 12 per cent of the latter. An examination of the data for the last few years pertaining to the private long-term capital account tends to show a reversal of the trends of earlier years. The property purchase/sales

TABLE 1

Bahamas: Selected Balance of Payments Data, 1970-85

B$mn

Year	Current Account			Capital Account[1]									
	Trade Balance	Services Balance	Current Account Balance	Private Long Term (net)				Public Corporations (net)	Government (net)	Commercial Bank (net)	Other Financial Institutions (net)	Capital Account Balance	External Reserves of Central Bank[2]
				Property Purchases/ Sales	Loans/ Repayments	Other Investments	Total						
1970	-225.5	182.7	-58.3	n.a.	n.a.	n.a.	n.a.	5.2	-1.8	n.a.	n.a.	78.0	15.0
1971	-228.1	226.0	-14.1	n.a.	n.a.	n.a.	n.a.	6.0	-2.2	2.0	n.a.	98.0	19.1
1972	-124.5	223.4	86.7	n.a.	9.2	n.a.	76.0	3.8	-1.8	2.0	n.a.	78.0	32.0
1973	-212.4	151.9	-72.8	33.4	1.9	44.6	79.9	4.2	6.5	-3.9	n.a.	90.6	40.0
1974	-292.1	247.4	- 57.2	17.6	7.0	93.1	117.7	-2.0	2.4	7.1	12.0	118.1	41.6
1975	-222.8	291.6	58.6	8.7	2.4	39.8	50.9	-7.8	-5.1	-11.4	-2.1	38.0	45.5
1976	-248.6	331.1	70.9	7.1	5.3	5.0	17.4	-5.3	-5.0	-23.6	-5.8	7.1	45.9
1977	-234.4	356.2	108.5	20.0	3.4	11.4	34.8	-3.6	8.2	27.5	-7.8	39.4	67.2
1978	-290.9	400.4	94.7	- 2.3	-14.4	1.1	-15.6	-4.0	-6.2	-4.2	6.0	-25.8	58.8
1979	-427.0	446.8	15.8	8.1	-6.1	1.5	3.5	8.4	-7.7	-19.7	0.4	4.2	78.7
1980	-600.4	587.1	-15.2	- 0.4	3.5	4.5	7.6	10.2	-7.6	-4.3	-0.8	10.2	92.6
1981	-620.5	541.3	-82.3	15.5	52.9	18.6	87.0	27.0	31.3	17.8	-0.4	145.6	100.1
1982	-541.8	474.9	-63.1	- 3.4	22.3	6.2	25.1	2.1	46.4	5.4	1.3	73.6	113.6
1983	-597.0	555.4	-34.5	- 2.3	8.7	-3.7	2.7	-6.3	18.4	-17.8	-1.5	14.8	123.7
1984	-604.3	554.1	-48.4	- 5.3	0.0	-0.4	-4.9	-8.1	-1.6	-21.5	-2.3	-11.4	162.5
1985[P]	-595.4	538.3	-50.4	-10.4	8.7	-21.4	-23.1	-8.2	-10.5	25.9	-2.1	-41.8	181.5

1. Non-monetary sector
2. At end of year
P. Provisional
n.a. Not available

Source: Central Bank, <u>Quarterly Review</u>, Various Issues.

component experienced positive inflows in the period 1973-77. Between 1978 and 1985, net outflows in six (6) years were recorded. The private loans repayment category indicates a considerable drop in the balances since 1983, compared to 1981 and 1982. The 'other investments sector' (which includes direct investment) experienced positive balances between 1973 and 1982. Since then, net flows have been negative. If we were to exclude 1981 and 1982 which were heavily influenced by private loan repayments, the private long-term capital account is estimated to have experienced a net outflow of B$30.0 million between 1978 and 1985. Capital movements relating to the public corporations and the government accounts are strongly influenced by external borrowing activities and servicing of these loans. As we shall see later, the foreign debt of the public sector has increased significantly in recent years, as have amortisation and interest payments. For instance, in the period between 1979 and 1985, new drawings by both the Government and public corporations totalled B$274.6 million, while debt service charges amounted to B$298.9 of which B$125.4 million were interest charges. There was, therefore, a net transfer of resources abroad of some B$15.0 million in the period.[12]

Barbados

Between 1970 and 1984 Barbados experienced a current account deficit in every year, except 1984, when there was a surplus amounting to one per cent of GDP (see Table 2).

TABLE 2

Barbados: Selected Balance of Payments Data, 1970-84

B$mn

Year	Current Account: Trade Balance	Current Account: Services Balance: All Services	Services Balance of which: Net Direct Investment Income	Services Balance of which: Public External Debt Interest	Current Account Balance	Capital Account: Long Term Capital Flows: Private Sector[1]: Net Direct Investment	Private Sector[1]: Portfolio	Long Term Capital Flows: Public Sector[2]	Short Term Capital Flows: Public Sector	Short Term Capital Flows: Other[3]	Other Capital Flows: Commercial Banks	Other Capital Flows: Other[4]	Net Capital Movements	Basic Balance	Overall Balance	Reserve Movements (+ decrease) (- increase)	Net International Reserves[5]
1970	-163.7	79.9	- 8.2	- 1.8	- 83.7	16.9	7.0	0.6	-0.3	2.7	-	-	26.5	- 59.2	- 24.9	24.9	33.0
1971	-178.2	108.9	- 7.7	- 1.6	- 69.3	29.2	3.2	-0.06	2.3	1.6	-	-	36.3	- 36.9	13.8	- 13.8	37.0
1972	-198.2	122.0	-11.1	- 1.6	- 76.2	33.4	-0.4	5.0	-0.9	-2.6	-	-	34.2	- 38.3	- 1.0	1.0	50.3
1973	-234.9	138.8	-11.8	- 2.5	- 96.1	5.1	0.5	41.0	-7.6	1.9	2.0	-	43.0	- 49.5	- 25.6	25.6	40.1
1974	-280.8	182.4	-10.5	- 5.7	- 98.4	12.4	16.2	-7.1	1.0	-0.4	5.7	-	28.0	76.9	7.9	7.9	49.3
1975	-246.9	163.2	-16.2	- 3.3	- 83.8	44.7	6.6	-0.6	-0.2	6.9	-0.9	0.1	56.7	- 33.0	34.8	- 34.8	85.2
1976	-324.4	195.9	- 7.7	- 2.9	-128.4	12.4	26.4	5.5	0.3	4.3	2.1	-1.0	50.0	- 84.2	- 36.0	36.0	56.4
1977	-374.4	271.2	- 9.2	- 3.1	-103.2	9.3	18.5	11.1	-1.5	11.5	10.2	0.7	59.9	- 64.3	- 6.0	- 29.2	76.1
1978	-406.5	343.6	-10.3	- 5.6	- 62.9	18.8	-6.6	32.0	-1.4	32.0	8.4	-2.2	81.0	- 18.8	58.3	- 58.3	127.9
1979	-566.0	497.1	-11.1	- 9.9	- 68.9	10.2	-35.0	9.0	1.5	40.6	-8.4	-1.2	17.0	- 84.7	22.2	- 18.1	145.6
1980	-687.3	633.1	-10.6	- 9.7	- 54.3	1.8	-11.4	53.7	-1.4	51.6	4.3	1.5	100.2	- 10.1	40.1	- 25.1	169.0
1981	-825.0	574.9	-16.8	-15.0	-250.1	14.3	42.0	98.8	0.2	62.2	8.7	16.4	242.6	- 95.0	- 78.7	44.9	128.1
1982	-689.6	606.0	-12.5	-20.5	- 83.6	8.8	-14.1	35.2	3.2	26.9	11.1	24.5	95.6	- 53.7	18.5	- 65.9	188.0
1983	-701.9	601.3	- 8.5	-23.9	-100.6	4.6	-17.7	57.5	0.0	8.0	28.7	22.5	103.6	- 56.3	13.3	- 42.6	225.1
1984	-642.0	666.4	- 8.7	-24.9	- 24.4	-2.9	-44.5	11.7	-2.1	6.0	-0.2	1.2	-28.7	- 11.2	2.2	- 10.8	241.5

1. Non-monetary sector
2. Mainly loans and suppliers' credit
3. Includes private sector trade credits
4. Includes movements in foreign assets of the Central Bank not included in the foreign r[illegible]erves. Such assets include bonds of international lending agencies (which have an origin[illegible] maturity of one year) and issues of foreign governments
5. End of year position.

Source: Central Bank, Balance of Payments of Barbados, Various Issues; Annual Statistical Digest, Various Issues; IMF, Financial Statistics, Various Issues.

The trade balance was consistently negative in the period, but a major part of these deficits was offset by surpluses in the services account which has tended to be consistently positive, despite a significant increase in interest payments on the public debt in recent years. As a result of both private and public sector capital inflows, the capital account (non-monetary sector) was positive throughout the period, except for 1984. In the long-term capital category, direct investment inflows have tended to fall in recent years, while public sector borrowing has taken on more significant dimensions. Between 1970 and 1978 net direct investment inflows averaged B$20.2 million per year. Since 1979, however, the average has been around B$6.0 million per year. In 1984, there was net outflow as a result of the reduced level of investment and the sale of equity by foreign concerns. Between 1970 and 1984 total net direct investment inflows amounted to B$219.0 million, giving an average of B$14.6 million per year. In the same period net direct investment income (which is included in the current account) amounted to B$161.0 million with an annual average of B$10.7 million. In the fifteen year period between 1970 and 1984, the portfolio capital balance was negative in seven years. Total net flows for the period was minus B$16.3 million. With respect to the public sector long-term borrowing (loans and suppliers' credit)inflows between 1977 and 1984 totalled B$309.9 million as compared to B$51.4 million between 1970 and 1976. Between 1980 and 1983 these inflows averaged around 59 per cent of the current account deficit.

In the short-term category, private sector inflows have generally been positive. Between 1977 and 1982 net inflows totalled B$225.0 million as compared to B$13.7 million between 1970 and 1976. In 1983 and 1984 there was sharp fall in the contribution of this sector (which is dominated by trade credits) to the capital account.

The figures recorded under 'commercial banks' refer to transactions of non-residents with banks operating in Barbados as well as funds brought into Barbados by the banks for on-lending to both the public and private sectors. The figures indicate great fluctuations from year to year in the movement of these funds.

Despite a persistent deficit in the current account, the overall balance was in surplus in nine of the fifteen years between 1970 and 1984. With the exception of 1981 when there was a tremendous increase in the current account deficit and the country's foreign reserves declined by some B$45.0 million, reserves have increased in every year since 1977. Net international reserves at the end of 1984 was equal to just over two months merchandise imports.

Guyana

Guyana is one of the Commonwealth Caribbean countries most severely affected by a shortage of foreign exchange since the mid-1970s. The cumulative current account deficits between 1970 and 1984 amounted to G$3,245 million dollars (see Table 3). Since 1976 the payments problem has been critical. The country experienced a deficit of G$35 million in 1975, which was equivalent to 3 per cent of its GDP. The current account balance improved in 1978, but in the period 1979-84 fluctuated between G$208 million and G$468 million. As a per cent of GDP, the deficits since 1981 have averaged over 29 per cent. Both the trade and services sectors have contributed to the growth of the current account deficits. Since 1976 the trade account has shown a positive balance in only one year, viz, 1978. The deficit in the services account, which was less than G$100 million in 1979, has grown to over G$200 million per year in recent years. A major factor influencing this trend has been the increasing interest payments on the foreign debt.

Data on the capital account for recent years are not readily available in great detail. Capital inflows between 1970 and 1975 more than covered the current account deficits. Net international reserves increased from G$54.6 million at the end of the 1970 to G$197.3 at the end of 1975. Between 1976 and 1984 net capital inflows are estimated to have amounted to only 20 per cent of the cumulative current account deficits. As a result, the net international reserves position deteriorated from a positive G$197.3 million at the end of 1975 to

TABLE 3

Guyana: Selected Balance of Payments Data, 1970-84

G$mn

Year	Trade Balance	Current Account: Services Balance: All Services	Current Account: Services Balance: Investment Income	Current Account: Current Account Balance	Capital Account[1]: Private Sector: Direct Investment (net)	Capital Account[1]: Private Sector: Other Long Term Investment (net)	Capital Account[1]: Private Sector: Other Short Term (net)	Capital Account[1]: Official Capital Receipts (net)	Capital Account[1]: Balance on Capital Account	Overall Balance	Net International Reserves[2]
1970	- 3.4	- 44.0	- 42.5	- 46.7	17.9	- 0.5	- 3.6	21.7	35.5	2.1	54.6
1971	23.3	- 38.1	- 36.0	- 13.2	-3.6	14.6	- 4.8	32.1	38.3	-12.7	67.3
1972	1.9	- 25.5	- 22.0	- 22.6	5.2	5.1	1.0	24.4	35.7	-22.4	89.7
1973	- 84.4	- 39.0	- 27.0	-123.4	17.6	10.0	2.4	33.0	63.0	47.9	41.7
1974	33.0	- 45.0	- 38.0	- 17.0	18.0	2.4	14.7	57.5	92.6	- 63.6	105.4
1975	43.8	- 70.0	- 40.0	- 35.2	4.0	7.5	- 4.5	102.2	109.2	-92.3	197.3
1976	- 216.1	-119.2	- 59.0	-350.8	-3.9	-19.6	- 4.8	176.6	148.3	231.3	- 31.4
1977	- 143.1	- 98.0	- 65.7	-251.1	3.0	-15.0	- 5.0	84.7	169.7	74.4	- 100.2
1978	42.7	- 98.5	- 56.3	- 72.3	1.0	17.3	- 3.7	102.7	97.2	-24.9	- 109.2
1979	- 63.7	-145.4	- 73.2	-208.1	1.5	9.9	3.8	74.2	101.6	123.5	- 251.3
1980	- 92.4	-206.0	- 87.0	-300.4	1.2	0.3	6.5	71.6	85.6	214.8	- 471.4
1981	- 268.2	-208.2	-163.7	-475.8	-5.0	17.7	n.a.	348.0	300.6	-175.2	- 620.0
1982	- 116.0	-261.0	-130.3	-426.0	13.2	-11.6	n.a.	163.0	110.8	-280.8	- 946.2
1983	- 165.2	-221.0	- 88.0	-468.0	14.1	-56.0	n.a.	75.0	-182.0	-566.1	-1,263.6
1984[P]	- 58.2	-267.4	- 77.4	-434.0	n.a.	n.a.	n.a.	45.0	-216.1	-546.0	-1,952.7

P. Provisional
1. Non-monetary sector
2. End of year position
n.a. Not available

Sources: Central Bank, Annual Report, Various Issues and Statistical Bulletin, September 198[illegible].
IMF, Balance of Payments Statistics and International Financial Statistics, Various Issues.
ECLA, Economic Activity in Caribbean Countries, Various Issues.

minus G$31.4 million at the end of 1976 and minus G$1,952.7 million at the end of 1984. Since the early 1970s official capital receipts have dominated capital flows. For instance, between 1971 and 1984 inflows to the public sector amounted to about 80 per cent of net capital inflows. Because of its inability to raise funds abroad, as a result of its poor credit rating and continuing debt servicing obligations, net receipts by the official sector have fallen considerably in recent years. Public policies and the economic and political climate since the mid-1970s appeared to have adversely affected inflows of privvate foreign capital. The experience of both the private and public sectors has contributed to the deficits in the capital account in recent years.

Poor export performance and the decline in foreign capital inflows both to the public and private sectors have resulted in a severe cut in imports in recent years. There appears to be little scope left for further reducing imports without even greater adverse effects on the standard of living and the efforts being made to stimulate the economy.

Jamaica

Jamaica experienced a current account deficit in every year between 1970 and 1984. As a percentage of GDP, this deficit averaged about 9 per cent between 1970 and 1976. The proportion dropped during the following four years, averaging around 4 per cent. Since 1981, it has increased sharply, averaging over 12 per cent between 1981 and 1984. The current account position has been influenced by a consistent negative services account, and trade balances that were positive in only two years during the period (see table 4). The current account deficits would have been larger in the absence of the substantial inflows of unrequited transfers since 1979. These transfers amounted to 41 per cent of cumulative trade deficits in the 1979-84 period. A major factor affecting the trade position was, of course, the significant increase in oil prices during 1970s and early 1980s, and the problems facing the bauxite industry. The down-turn in tourism as a result of the political climate during the 1970s contributed to the unsatisfactory performance of the services sector. In recent years interest payments on the foreign debt has contributed significantly to the deficits in services and current accounts. Actual interest payments between 1978 and 1984 have ranged between 41 per cent and 92 per cent of the current account deficits.

With the exception of one year, the capital balance has generally been positive. These surpluses, however, were of a magnitude only on five occasions to offset the current account deficits. Until 1975, the country was able to

TABLE 4

Jamaica: Selected Blance of Payments Data, 1970-84

US$mn

Year	Current Account						Capital Account[2]					Overall Balance	Net Foreign Reserves[3]
	Trade Balance	Services Balance: All Services	Services Balance: of which: Direct Investment Income	Services Balance: of which: Interest on Public External Debt[1]	Unrequited Transfers	Current Account Balance	Direct Investment	Other Private Long-Term	Other Private Short-Term	Official Inflows	Capital Balance		
1970	-107.0	- 67.4	-103.9	- 13.9	21.5	- 152.6	161.4	- 3.7	- 2.8	- 1.4	160.9	21.5	115.2
1971	-132.7	- 4.0	- 48.9	- 15.0	21.0	- 115.6	119.4	9.3	2.8	4.9	136.3	44.3	158.6
1972	-151.3	- 2.1	- 52.3	- 17.2	27.9	- 125.6	26.5	13.5	11.5	23.4	74.9	-54.5	112.4
1973	-177.3	- 29.8	- 50.0	- 16.2	26.4	-180.7	22.2	75.8	2.3	36.6	136.9	-30.5	91.3
1974	-117.6	- 72.8	- 46.4	- 31.2	23.4	-167.0	23.3	112.1	17.7	90.1	243.2	59.5	156.2
1975	-159.5	-149.6	- 59.1	- 50.8	26.2	-282.7	- 1.9	80.1	7.0	123.6	208.9	- 81.0	68.0
1976	-135.2	-173.4	- 50.0	- 58.0	6.0	-302.6	- 0.6	11.0	-41.4	79.2	45.6	-262.0	-193.5
1977	83.9	-138.5	- 29.0	- 60.2	20.0	- 34.6	- 7.0	4.7	65.1	- 5.9	56.9	- 16.1	-214.8
1978	44.5	-156.9	- 92.1	- 75.5	25.7	- 86.7	- 28.8	-177.1	34.7	178.9	9.8	- 77.5	-292.2
1979	- 67.4	-134.7	- 81.6	-101.6	80.0	-142.6	- 26.4	- 53.9	- 1.4	71.1	- 10.4	-140.9	-430.4
1980	- 75.4	-181.7	-112.1	-153.0	90.8	-166.3	27.6	- 46.2	46.0	120.3	107.1	- 50.2	-432.9
1981	-322.7	-138.4	- 2.9	-186.6	124.3	-336.8	- 11.5	- 10.7	7.4	240.2	225.4	- 90.5	-600.4
1982	-441.5	- 96.8	28.0	-221.7	150.4	-387.9	- 15.8	- 12.4	47.8	446.0	465.6	86.1	-522.3
1983	-438.5	-143.5	- 0.6	-195.3	101.5	-480.5	- 18.7	- 26.1	-65.4	300.7	190.5	-289.1	-808.9
1984[P]	-291.7	-118.7	- 30.4	-186.0	120.6	-289.8	12.2	- 40.6	148.2	362.9	482.7	225.7	-584.6

P. Provisional
1. Figures from 1970 to 1973 include amortisation
2. Non-monetary sector
3. End of year position

Sources: Bank of Jamaica, Balance of Payments of Jamaica, Various Issues
Statistical Digest, Various Issues.

finance the overall deficits and maintain a positive net foreign reserves position. In 1976, as a result of the worsening of the current account position and a sharp drop in net capital inflows, the overall deficit moved from US$81 million in 1975 to US$262 million. As a result, the net foreign reserves changed from plus US$68 million at the end of 1975 to minus US$199.5 million at the end of 1976. The net reserves position has been negative since. At the end of 1983, it dipped to minus US$808.9 million, but improved the following year as a result of a reduced current account deficit and inflows of official and private short-term capital.

Between 1970 and 1975 net direct investment flows were positive, varying between US$22.2 million and US$161.0 million per year. In the eleven years following 1974, the figure was positive in only two years. Not only has new investments slowed down, but a certain amount of dis-investment (capital flight) has taken place. In the mining sector which attracted a great deal of investment in the 1950s and 1960s, inflows of foreign capital has virtually ceased. In the late 1960s and early 1970s, private capital inflows associated with expansion projects in the bauxite and tourist sectors accounted for approximately 30 per cent of domestic capital formation.[13] The negative balance of payments effects of direct investment movements tend to put in sharper focus the continued outflow of income associated with foreign capital, even though the absolute amount has fallen in recent years. Between 1970 and 1974 total direct investment inflows amounted to US$352.8 million while direct investment income outflow totalled US$301.5 million. Between 1975 and 1984 net direct investment outflows were of the order of minus US$70.9 million as compared to direct investment income of outflows of US$430 million.[14] Other private long-term capital flows which were positive until 1976 has been consistently negative since. Between 1978 and 1984 there was a total net outflow of US$367 million. Private short-term capital varies widely from year to year. Between 1970 and 1984 this account was negative in only four years. In recent times, capital movements associated with government borrowing have dominated the capital account. Between 1978 and 1984 official inflows totalled US$1,720 million, as compared to US$352 million in the previous seven years. A substantial part of these resources were for financing the balance of payments deficits. At the end of 1984, more than half (US$629 million) of the Bank of Jamaica external debt was owed to the IMF.

Trinidad and Tobago

Between 1970 and 1973 Trinidad and Tobago experienced a current account deficit in every year, with a cumulative total of TT$683 million for the period. (see Table 5). In

TABLE 5

Trinidad and Tobago: Selected Balance of Payments Data, 1970-84

TT$million

Year	Current Account					Capital Account[1]				Overall Balance	Net Foreign Reserves[2]
	Trade Balance	Services Account			Current Account Balance	Direct Invest-ment	Other Private Inflows	Net Official Inflows	Net Capital Movements		
		All Services	of which: Direct Investment Income	of which: Interest on Gov't External Loans							
1970	- 98.7	- 13.4	- 118.8	- 8.7	- 116.3	166.4	6.6	7.3	180.3	- 20.6	106.6
1971	-271.1	47.7	- 120.6	- 8.5	- 232.7	205.9	16.8	3.9	267.1	41.6	156.3
1972	-319.4	44.7	- 128.7	- 10.6	- 283.2	166.6	- 1.7	38.8	211.8	- 58.3	110.4
1973	-142.8	110.9	- 157.4	- 13.0	- 50.7	128.4	-66.3	56.5	120.4	- 28.1	67.1
1974	-823.2	-212.0	- 575.6	- 25.4	576.0	246.7	13.2	-125.1	67.9	602.1	768.3
1975	534.7	227.1	- 222.1	- 19.7	715.9	440.1	-30.9	- 48.3	334.7	956.3	1,640.1
1976	467.0	224.6	- 350.6	- 15.1	618.5	261.1	-20.9	-265.4	- 25.9	485.5	2,125.1
1977	473.0	15.3	- 604.6	- 10.0	414.5	336.2	8.1	342.8	685.1	1,059.7	3,204.1
1978	83.1	105.1	- 410.3	- 45.0	97.1	304.7	128.3	256.8	699.7	758.0	3,950.8
1979	359.5	-337.0	- 839.7	- 87.3	- 87.0	416.5	444.1	132.2	1,021.1	879.1	4,837.8
1980	1,292.4	-332.1	-1,149.6	- 83.5	994.8	328.8	49.6	155.4	478.2	1,472.4	6,336.7
1981	1,216.7	-247.7	-1,010.6	-134.7	751.3	487.9	260.6	-229.2	545.3	1,342.8	7,686.8
1982	-1,360.4	-227.2	- 813.4	-117.4	-1,785.5	637.4	262.9	166.1	1,131.7	- 646.7	7,160.1
1983	-729.8	-1,101.6	- 442.5^P	-157.8	-2,116.7	143.6	-90.8	138.8	119.6	-2,162.5	4,990.9
1984	461.9	-1,533.3	- 619.8^P	-184.5	-1,386.0	217.2	-390.7	255.4	81.9	-2,148.9	2,850.0
1985^P	1,322.4	-1,401.4	n.a.	-246.5	- 491.0	126.9	-161.4	239.7	205.2	- 630.7	3,023.2

P. Provisional
1. Non-monetary sector
2. End of year position

Sources: CSO, <u>Balance of Payments of Trinidad and Tobago</u>, Various Issues;
Ministry of Finance, <u>Review of the Economy</u>, Various Issues; Central Statistical Office.

the following eight years, there was a deficit in only one year, and that was in 1979. The net surplus for this period was TT$4,031 million. Since 1982, the current account has been consistently negative, the total deficits for the period 1982-84 amounting to TT$5,288.5 million. The favourable current account experience between 1974 and 1981 was due largely to the increase in international oil prices, and the effect of these on the trade account. Between 1970 and 1978, the services account was negative in only two years. Since 1979, however, a deficit has been experienced in every year, and this has contributed to the payments problem. Even though there were trade surpluses in 1984 and 1985, as a result of the measures instituted to curb imports, these were offset by the negative balances in the services account. The services deficits in the 1979-84 period totalled TT$3,779 million. As can be seen in Table 5 two of the major elements in this account are direct invesement income and interest on government loans. The falling income from government's diminishing external assets has tended to exacerbate the position.

In the period 1970-85, the capital account was in deficit in one year, and that was 1976. Two of the main factors contributing to this situation have been the positive direct investment inflows and government borrowing. Between 1970 and 1984, direct investment inflows totalled TT$4,488.0 million. In the same period direct investment income amounted to TT$7,564.3 million. As can be seen in Table 6 the petroleum industries have been the major recipient of direct invesement. They also, of course, account for the major share of direct investment income. Because of the depressed state of the oil industry in recent years, investment has fallen significantly since 1982.

Other private capital flows covers, inter alia, loan draw-downs and repayments by government-owned non-financial enterprises and changes in the foreign asset/liability position of firms other than direct investment enterprises. Between 1970 and 1977 there was a net outflow in this account in four years, the total net movements amounting to minus TT$75.1 million. In the following five years total inflows amounted to TT$1,145.5 million. This was followed by three consecutive deficits in the period 1983-85.

The figures under net official inflows indicate that Government was borrowing in the height of the oil boom, when foreign reserves were increasing. This was apparently being done, not so much out of need, but to help establish the country's credit worthiness in international capital markets.[15] A significant part of the funds borrowed in this period went into the highly capital intensive energy-based industries that were initiated as part of the diversification process.[16] The positive inflows since 1982 indicate that government borrowing activities have continued in the recession years,

TABLE 6

Trinidad and Tobago: Supplementary Balance of Payment Data, 1974-82

TT$mn

Year	Direct Investment Income				Selected Service Payments				Net Direct Investment Capital by Sectors	
	Petroleum Industries		Other Sectors		Management Fees	Professional & Technical Services	Commissions	Royalties Patents, etc.	Petroleum Industrial	Others
	Retained Profits[1]	Other	Retained Profits[1]	Other						
1974	528.1	29.0	12.3	6.2	7.2	24.0	2.3	2.7	206.0	40.3
1975	561.2	49.7	19.3	10.8	7.4	28.0	3.7	3.7	470.8	-30.7
1976	291.0	23.7	24.5	11.4	13.9	46.5	4.6	4.9	254.9	6.2
1977	480.4	71.7	39.8	12.7	13.9	72.5	9.2	9.7	250.5	85.7
1978	324.4	30.1	38.5	17.3	14.8	122.9	12.0	8.1	260.2	44.5
1979	684.5	85.4	48.1	21.7	11.5	173.9	15.6	11.7	353.6	63.0
1980	713.3	321.1	86.1	29.1	20.3	176.3	15.8	13.3	246.6	82.1
1981	555.9	362.3	76.5	15.9	11.9	207.6	17.8	13.7	722.5	7.9
1982	616.8	52.1	106.4	38.1	29.4	194.5	20.3	20.7	504.7	112.7

1. Estimated

Sources: CSO, Balance of Payments of Trinidad and Tobago, Various Issues.

but in the current economic situation, that is clearly more out of need.

With respect to the overall balance account, two (2) negative balances in 1972 and 1973 respectively were followed by eight years of positive balances totalling TT$7,556 million. The net foreign reserves of the country increased from TT$67.1 million at the end of 1973 to TT$7,686.8 million at the end of 1981. At the end of 1984, this had fallen to TT$2,850 million. It increased slightly at the end of 1985.

Organization of Eastern Caribbean States (OECS) and Belize

The propensity to import is much stronger in the OECS and Belize than in the MDCs. For instance, in the case of the latter, the import coefficient (the ratio of imports of goods and non-factor services to GDP) in 1984 was 47 per cent as compared to more than 75 per cent for the OECS and Belize. For the OECS group, the export ratio was only 35 per cent as compared to 45 per cent for the MDCs. This heavy import orientation is a major factor in the persistent current account deficits which these small economies experience. The deficits would be higher in the absence of the significant private transfers associated with nationals living and working abroad and grants from foreign governments. In the case of Montserrat, net transfers in 1984 are estimated to have amounted to over EC$19 million as compared to export of goods and non-factor services of EC$27 million. For St. Lucia, net private transfers averaged EC$13 million per year between 1980 and 1984. This was the equivalent of over 30 per cent of the earnings from domestic exports.

On the capital side, official transfers from friendly governments have played a major role in helping to sustain the high level of imports. (see Table 7). These transfers, however, have not been adequate in the context of the public sector investment programmes which the various governments have formulated in the post-independence period. Increasingly, they have turned to borrowing both from multilateral agencies and private markets, not only for project related purposes but for budgetary and balance of payments support. Servicing this debt has in some cases tended to put greater pressure on both the current and capital account. Detailed data on private capital flows are not readily available. Belize and OECS countries offer a wide range of incentives to foreign investors in pursuit of developmental objectives such as capital formation, employment generation, economic diversification, export generation etc. Because of the small domestic markets and the inadequate infrastructure, these incentives have not been very effective. A substantial part of private investment has flowed to the tourism sector, which has been one of the fast developing areas in these economies.

TABLE 7

Selected Balance of Payments Data[1] for Belize and the OECS

EC$mn

Countries	Current Account		Capital Account				
	Current Account Balance	of which Interest Payments (net)	Official Transfers	Official Borrowings (net)	Private Flows[2]	Capital Account Balance	Overall Balance
Antigua	- 69.4	- 7.9	5.5	9.8	55.3	70.6	1.2
Belize	- 38.9	- 6.5	n.a.	[illegible].2[4]	-2.4	30.8	- 8.1
Dominica	- 48.9	- 2.3	26.7	12.0	11.8	50.5	1.6
Grenada	- 64.5	- 2.9	43.4	20.6	-4.4	59.3	- 5.2
Montserrat[5]	- 17.9	- 0.2	3.5	0.1	n.a.	n.a.	n.a.
St.Kitts-Nevis	- 18.7	- 0.4	6.8	4.9	5.4	17.1	- 1.6
St. Lucia	-100.1	- 2.3	13.8	9.4	58.1	81.3	- 18.8
St. Vincent[3]	- 23.9	- 2.0	11.6	7.8	3.9	23.3	- [illegible].6

1. Figures are average for the five year period 1980-84
2. Including errors and omissions
3. 1979-83
4. Include transfers
5. Average 1983-84

Sources: ECLA, Economic Activity in Caribbean Countries, Various Issues; IMF, International Financial Statistics and Balance of Payments Statistics, Various Issues, Statistical Departments

Private Direct Foreign Investment (DFI)

Private foreign capital flows to developing countries take a number of forms. One of the most important of these forms is direct investment which implies control by the foreign investor, or at least an effective voice in management and decision-making. Such control need not require 100 per cent ownership of equity capital. Another form of inflow is portfolio equity investment which because of limited investment opportunities, national regulations and rates of return has tended to be less important for developing countries than direct investment. Portfolio capital is motivated more by financial returns than the desire for control of an enterprise. Domestic financial institutions also often borrow abroad to finance local activity, depending on local interest rates, the domestic liquidity situation and opportunities for lending. Foreign capital inflows also stem from borrowing by governments and their agencies in private capital markets which have come to play an important intermediary role between surplus and deficit countries in the international economy.

Net flows of direct investment from industrial to developing countries as a group, increased from an average of under US$2 billion a year during the early 1960s to an average of around US$10 billion a year during the 1974-82 period.[17]

Despite an increase in the annual direct investment capital, the rate of growth of such flows has been much lower than those associated with borrowing from official and private sources (see Tables 8 and 9). During the 1960s, direct investment accounted for well over half of all private capital flows from industrial to developing countries but by the late 1970s, it represented barely one-quarter.[18] The result of this trend is that by 1983, the outstanding external debt of non-oil developing countries was almost five (5) times the stock of direct foreign investment, as compared to about three (3) times in 1973. (see Table 8).

The international environment affecting direct investment flows has changed in several respects since the 1950s and early 1960s. In both developing and some developed countries concern over increasing control of key sectors of the economy by foreign enterprises had led in many instances to a more restrictive approach to foreign investment. Several countries either have drawn up codes to govern the behaviour of foreign investors or issued policy statements (some of them far from clear) indicating the conditions on which private foreign capital would be received and the areas where it will be welcomed or prohibited. Nationalizations during the 1960s and 1970s added an element of uncertainty to the investment climate in several host countries, leading to a certain amount of disinvestment. Even in countries where

TABLE 8

Non-oil Developing Countries: Composition of Financing Flows, 1973-1983

US$billions

		1973	1981	1983
1.	Current account deficit	10.9	108.5	52.6
2.	Reserve accumulation	9.7	3.7	10.0
	Financing (1 + 2)	20.6	112.2	62.6
3.	Net direct investment	4.2	13.1	9.3
4.	Official Transfers	5.5	13.1	12.0
5.	Net long term borrowing from official creditors	5.7	24.3	24.5
6.	Net external borrowing from private creditors	5.7	66.4	18.4
7.	Other sources[1]	-0.5	-4.7	-1.6

1. Includes errors and omissions

Source: IMF, Foreign Private Investment in Developing Countries, Washington, D.C. 1985

TABLE 9

Non-oil Developing Countries: External Liabilities, 1973 and 1983

	Stock of liabilities[1]		Average annual Growth Rate
	1973	1983	1973 1983
	US$billions		Per cent
Foreign direct investment[2]	47.0	140.9	11.6
Total external debt[3]	130.1	685.5	18.1
Short term debt	18.4	110.6	19.6
Long term debt	111.8	574.9	17.8
Official creditors	51.0	219.9	15.7
Private creditors[4]	60.8	355.0	19.3
Financial institutions[5]	17.3	204.1	28.0
(As a per cent of exports of goods and services)			
Foreign direct investment	41.5	31.7	
Total external debt	115.4	154.4	

1. End of year
2. Book value; net of disinvestments and nationalization
3. Excluding reserve related credits
4. Including debt not guarantees by government of debtor country
5. Guaranteed debts only

Source: IMF, Foreign Private Investment in Developing Countries, Washington, D.C., 1985 foreign investment was avowedly welcome, bureaucratic procedures and unclear regulations often served to discourage foreign investors. A certain amount of official ambivalence in the context of nationalistic environments often added to the uncertainty. In this situation foreign investors devised new ways for controlling or penetrating markets, increasing exports, and dealing with perceptions of political risks. To satisfy demands for local participation and to reduce risks, there has been some shift away from direct control by the parent company over management of an associated enterprise, to management participation, technical assistance agreements, production sharing, supply contracts, rent of technology etc.[19] There has also been an increasing shift from equity participation to the use of loans and suppliers' credit. Since these developments do not fall within the traditional definitions of 'private direct foreign investment' which has tended to be seen in terms of equity participation with an effective voice in management, the extent of foreign investment activity in a country can be seriously under-estimated.

In some capital exporting countries themselves, there is concern over the implications of capital outflow for domestic employment and the balance of payments. In the context of high unemployment levels and payments difficulties, some countries have tended to take a more restrictive approach to capital outflow, though such investment tends to generate foreign investment income which impacts favourable on the balance of payments in later years. The short-term view, however, often exerts a dominant influence on policies.

The role of foreign private capital in the development process remains a very controversial subject. In the early post-war years the direct investment component was not only associated with an inflow of capital, but with management, entrepreneurial and marketing expertise, technology as well as marketing connections. In at least one well-known model the re-investment of profits by the foreign controlled enterprise was seen as playing a critical role in the expansion of the local capital stock, the creation of employment and the growth of the modern sector.[20] In most cases there has been a great measure of disappointment over the contribution made by direct investment to economic transformation. In many cases the export base remains very narrow, and the technology transferred has been inappropriate, or of a vintage that has had no significant impact on productivity. Despite this, balance-of-payments problems, poor growth rates and prodding by multilateral agencies are leading some countries to intensify their efforts to attract private foreign capital. Inspired by the export and growth performances of such countries like South Korea, Hong Kong, Taiwan and Singapore, some states are not only modifying their development framework, but adopting more open door policies towards foreign capital.

Commonwealth Caribbean countries have long been in receipt of foreign investment. The areas of early interest were the agricultural plantations, mining, the utilities and the financial sector. In the post-war period, attention shifted to the manufacturing and tourism sectors, as governments (particularly after independence) began to institute active measures to promote these sectors out of concern with the narrow base of their economies and the need to create employment and develop new exports. Emphasis in the 1960s and 1970s was on import substitution, i.e. the domestic production (or assembly) of goods (largely of a consumer variety) previously imported. This did not reduce the level of imports, but tended to change its composition in favour of raw materials, intermediate and capital goods. Based on the infant industry argument, a number of devices, such as tariffs, quotas, exchange restrictions and licensing arrangements were used to protect the local market. These devices were bolstered by measures designed to encourage greater participation in the economy. In order to retain access to the local markets traditional suppliers found it necessary to enter into various kinds of arrangements with local business groups, or to establish local operations in the form of branches and subsidiaries. This process has in some instances resulted in a significant increase in service payments, not only in the form of direct investment income, but in commissions and fees relating to the use of foreign management, royalties, patent and professional and technical services. In the case of Trinidad and Tobago such service income (excluding direct investment income) increased from less than TT$10 million in 1970 to more than TT$250 million in 1982.

Favoured with an environment free of competition and with little pressure to export, costs have tended to remain high. With respect to exports, parent companies often find it necessary to prohibit their local operations from selling outside local markets to avoid competition with related establishments in other territories or in their home country. The strategy of market control by transnational firms has worked against exports development in Commonwealth Caribbean territories.

While, therefore, the manufacturing sector remains critically dependent on imports of intermediate inputs and capital goods for survival, the poor export performance of the sector has resulted in a situation where the net foreign exchange earnings capacity of the sector is negligible. Exports remain highly concentrated. The foreign exchange situation is exacerbated by the continuous need to service foreign capital, technology and know-how. The stream of such outflows often exceed the initial capital inflow, and this, of course, raises the question about the contribution of direct investment as far as foreign exchange is concerned.

The counter argument to this is that it is not correct to compare the series of subsequent service outflows (e.g. interest and dividents) with the initial equity inflow since the latter may not only have had a positive impact on output, employment and savings, but on exports both in the sectors directly concerned, as well as in other areas of activity through the linkage effect.[21] In the context of foreign exchange difficulties and poor growth performance being experienced in many cases, this issue remains a sensitive and controversial one.

Foreign private capital is associated with costs and benefits both for capital exporting and host countries. In the [illegible] of the latter, both political and economic considerations have influenced their approach as they try to maximize benefits and minimize costs. This has proved no easy task, as nationalistic policies and measures designed to increase the local contribution or to correct inequitable arrangements are often seen as an anti-foreign investment stance. For newly independent countries a completely open door policy to foreign capital in the context of efforts to encourage greater local participation in the economy has not been palatable, particularly against a background of historical foreign economic domination. Because of the size of local markets, high growth performance, macro-economic policies, political climate and development strategy, some countries have been more successful at attracting foreign capital than others. The experience of Brazil, however, which has received significant amount of foreign private capital since the early 1960s does raise some interesting questions. Mexico, too, despite a more nationalistic environment also attracted, during the 1960s and 1970s, a wide range of manufacturing concerns. A major question is, is 'peripheral capitalism' capable of leading to a stage of self-sustained growth? Put differently, is it capable of generating enough foreign exchange to satisfy its own cravings, since inflows of foreign capital seems to create a need for more foreign capital. Despite impressive growth rates in the 1960s and 1970s, the emergence of balance of payments problems in recent years have resulted in massive foreign borrowings by the government of these two (2) countries in order for these economies to function.

The Public External Debt

There is a tendency in Commonwealth Caribbean countries for current expenditure to grow faster than current revenue. A major factor in this situation has stemmed not only from increases in wages and salaries but from the growth in public sector employment, often at a rate far beyond what is required to maintain public services. In some cases, state subsidies have increased because governments have had to acquire unviable enterprises in order to save jobs, or take control of foreign enterprises which the owners no longer wished to operate and which, because of the size of the investment, the local private sector was not particularly interested. In a number of cases, government corporations (including the utilities) are unable to cover their operating expenditure for various reasons, and, therefore, these also require state subsidies. The financial position of governments is often made more difficult not only by a generally poor fiscal effort, but by depressed prices for major exports, declining production levels, natural disasters and recession in major trading partners. Of course, when current revenues fall, certain categories of current expenditure which loom large in government budgets are not easy to reverse, particularly when the state itself sees its role as having to maintain a high level of activity in order to offset some of the consequences stemming from a fall in the private sector investment.

Given the poor state of the infra-structure, particularly in the LDCs, and the commitment to a mixed economy framework, governments in Commonwealth Caribbean countries often find themselves investing more in infra-structural development than in directly productive activities. The gestation period of such investments tend to be long, and therefore are not quickly reflected in income and public revenues. Increasingly, the governments of the region have been borrowing (both locally and abroad) not only to finance budetary deficits, but investment programmes. In the case of the LDCs, grants from friendly governments have traditionally played an important role in budgetary support and public investment activities. In recent years, however, there has been a growing resort to foreign borrowing because of failure of grant receipts to match proposed development expenditure.

A glance at Table 10 shows that domestic investment as a proportion of GDP has varied widely among Commonwealth Caribbean countries in recent years. For example, in the 1982-84 period the average for Barbados was 20 per cent as compared to 15 per cent for St. Kitts-Nevis, 22 per cent for Jamaica and 37 per cent for St. Lucia. In most cases the gross domestic savings ratio is far below the investment ratio. Detailed data on domestic savings are not avialable, but public sector savings, as indicated earlier, tends to be small or negative. In most cases public capital investment has depended critically on borrowed funds. In order not to crowd out the local private sector, governments not infrequently turn to foreign markets for capital resources when these are avialable. In certain cases foreign financing as a proportion of GDP has tended to increase. For instance, the ratio for Jamaica averaged about 12 per cent between 1981 and 1984, as compared to 7 per cent between 1970 and 1980. For St. Lucia external finance averaged over 50 per cent between 1977 and 1982. This, however, was largely due to the construction of the Hess Oil Terminal. The figure has fallen considerable with the completion of the facility.

TABLE 10

Commonwealth Caribbean Countries: Selected Financial Statistics

	Domestic Investment as a % of GDP 1982-84	Gross Domestic Savings as a % of GDP 1982-84	Central Government Finances as a % of GDP (1984)					
			Current Revenue	Current Expenditure	Current Account Surplus (Deficit)	Capital Expenditure	Overall Deficit (Surplus	Domestic Financing
MDCs	n.a.	n.a.	28.0	29.2	(1.2)	8.8	9.9	6.6
Bahamas	n .a	n.a.	20.2	19.9	0.3	1.1	0.8	4.1
Barbados	19.9	20.4	24.8	24.3	0.5	5.8	5.3	1.0
Guyana	25.3	8.2	37.2	61.3	(24.1)	40.7	64.8	57.2
Jamaica	21.8	12.9	19.7	27.2	(7.5)	6.1	13.5	9.4
Trinidad & Tobago	n.a.	n.a.	33.2	31.8	1.4	10.2	8.8	6.4
OECS (Total Average)	29.6	n.a.	30.5	32.6	(2.1)	13.4	15.5	n.a
Antigua	2[illegible].4	12.6	27.2	31.6	(4.4)	12.5	16.9	14.1
Dominica	29.4	3.3	33.3	32.5	0.8	21.8	21.0	1.0
Grenada	41.6	n.a.	37.3	37.0	0.3	30.6	30.3	(0.3)
Montserrat	30.4	(16.3)	23.8	23.0	0.8	7.8	7.0	n.a.
St.Kitts-Nevis	14.7	(16.0)	31.5	34.8	(3.3)	5.5	8.8	n.a.
St. Lucia	36.9	10.3	28.8	33.1	(4.3)	8.4	12.7	6.1
St. Vincent	28.9	n.a.	31.9	31.8	0.1	7.0	6.9	n.a.
Belize	n.a.	n.a.	29.1	28.9	0.2	3.5	(1.7)	n.a.

n.a. Not available

Source: Caribbean Development Bank, Annual Report, 1985.

As can be seen in Table 11, the public external debt outstanding has increased in all cases, both in absolute terms and as a percentage of GDP. Some governments have increased their borrowing at a faster rate than others. For instance, while in the case of Barbados, the ratio of outstanding debt to GDP increased from 9 per cent to 16 per cent between 1970 and 1984, for Guyana the ratio moved from 30 per cent to over 150 per cent and for Jamaica from 16 per cent to 136 per cent. Judged in terms of the ratio of outstanding debt to GDP and service payments in relation to exports earnings Jamaica and Guyana have become two of the most heavily indebted countries in the developing world. While the external debt and and debt service payments have grown in volume terms, a contributing factor to this situation has undoubtedly been the stagnation or decline in GDP and export earnings. Even in the case of Trinidad and Tobago which experienced a significant growth in its net foreign reserves position during the 1970s as a result of the increase in international oil prices, there was an expansion in foreign borrowing. This debt,as indicated earlier was incurred, not so much out of need, as to establish the country's credit worthiness in foreign markets. Given the downturn in its economy in recent years, foreign borrowing is likely to increase, resulting in greater debt service payments. As far as the LDCs are concerned, in most cases there has been a significant expansion in foreign borrowing since independence. For instance, Antigua's

TABLE 11

Selected Data on External Debt, 1970 and 1984

Countries	External Debt Outstanding[1] US$mn (1)	External Debt Outstanding[1] US$mn (2)	Outstanding Debt as a % of GDP (3)	Outstanding Debt as a % of GDP (4)	External Debt Service Payments[2] US$mn (5)	External Debt Service Payments[2] US$mn (6)	Debt Service Payments as a % of Exports of Goods and Services (7)	Debt Service Payments as a % of Exports of Goods and Services (8)
	1970	1984	1970	1984	1970	1984	1970	1984
Barbados	15.1	182.6	9.0	15.9	0.9.	23.7	0.9	2.9
Guyana	80.0	683.0	30.0	153.0	6.0	31.0[4]	3.3	13.4[4]
Jamaica[3]	154.0	3237.1	15.8	136.0	14.0	394.0[4]	2.6	28.0[4]
Trinidad & Tobago	79.1	838.7	9.4	11.2	9.9	145.8	2.8	5.8
Bahamas	27.3	155.1	7.0	7.8	3.4	28.6	1.0	2.3
	1975	1984	1975	1984	1975	1984	1975	1984
Antigua	18.3	53.0[5]	27.9	40.4[6]	0.6	1.9[6]	1.2	2.2[6]
Belize	11.6	66.0[5]	12.1	39.3	2.1	6.5[6]	2.6	6.9[7]
Dominica	6.8	35.2	24.4	41.2	0.6	2.6	4.5	10.3
Grenada	5.5	48.2	13.7	55.5	0.6	5.5	2.7	32.0
Montserrat	0.4	2.7[5]	5.1	9.0	-	0.2[6]	-	2.1[6]
St.Kitts-Nevis	5.4[7]	15.8	18.7[7]	25.5	1.2[7]	1.1	6.2[7]	3.1
St. Lucia	3.4	31.2	8.5	20.6	0.1	1.8	0.4	0.7
St. Vincent	1.8	24.8	4.9	24.9	0.2	1.9	1.9	1.0

Note: Data for LDCs generally refer to external public and publicly guaranteed debt

1. End of period disbursed outstanding debt
2. Interest and amortisation
3. Refers to Central Government debt, debt guarenteed by government and Bank of Jamaica debt
4. Actual payments; on an accrued basis this figure would be much higher
5. End of 1983 position
6. 1983 position
7. 1976 position

Sources: CDB, Annual Report, 1985; Official Publications.

outstanding nominal debt increased by almost 200 per cent between 1975 and 1983, as compared to increase of over 400 per cent for Belize. and Dominica respectively.

The sources from which resources are borrowed often have a great bearing on the terms of repayment. The funds associated with multilateral institutions and government agencies tend to carry softer financial terms than commercial banks' loans. A substantial part of the LDCs debt is owed to the Caribbean Development Bank (CDB). In the case of St. Vincent, the CDB's share was 85 per cent as compared to 9 per cent bilateral at the end of 1983. For Dominica, the bilateral share was higher - 26 per cent, as compared to 56 per cent for the CDB. For Antigua the CDB share was far lower 19 per cent as compared to 80 per cent for other sources. A few of the LDCs have ventured to increase their commercial borrowing in recent years, in the absence of a greater volume of resources from traditional sources. The MDCs have tended to rely less on CDB funding. At the end of 1984, Jamaica's outstanding external debt stood at US$3,237.1 million. Of this US$265 million was government guaranteed debt, US$1,776.7 million central government and US$1,195.4 million Bank of Jamaica obligations. Of this latter figure, US$628.7 million (52.6%) was due to the IMF. A breakdown of the central government debt showed that 31 per cent was owed to international institutions, 39 per cent to other governments and 29 per cent to commercial bank and other commercial sources, while suppliers' credit represented about 1 per cent. Sixty four per cent of this debt had a maturity of less than fifteen years. In the case of Guyana, the commercial proportion of outstanding disbursed debt fell from an average of 45 per cent between 1972 and 1980 to 24 per cent in 1984. This situation may be a reflection of either a deliberate policy to rely less on commercial funds because of servicing difficulties, or an inability to raise such loans in the light of poor credit ratings of the non-commercial component, 48 per cent (5.4% in 1972) was owed to multilaterial institutions and 52 per cent was bilateral. Because of its relatively high per capita income, Trinidad and Tobago has been forced to do most of its borrowing on commercial terms. Of the total amount outstanding at the end of 1984, more than 75 per cent had a maturity of less than ten years.

Concomitant with the growth of the external debt, debt service payments have grown absolutely and as a percentage of earnings from the export of goods and services. Some countries have found it increasingly difficult to service this debt both from the point of view of public revenue and foreign exchange earnings. In a few cases defaults have occurred. Guyana's actual debt service ratio increased from less than 5 per cent in 1970 to 13 per cent in 1984. Inability to service its debt has resulted in an accumulation of arrears. On an accrual basis the average ratio in 1982-83 would have been in the region of 35 per cent. In recent years, Jamaica has also faced an arrears problem, in the light of its poor export performance and inability to mobilize enough resources to service past loans. The actual debt service ratio increased from about 3 per cent in 1970 to 28 per cent in 1984. On an accrual basis the latter figure would have been over 50 per cent. The comparative figure for 1985 was estimated to be 61 per cent.[22] The ratio of 6 per cent for Trinidad and Tobago looks small compared to that of Jamaica and Guyana respectively, but this could increase significantly in the light of the devaluation of the Trinidad and Tobago dollar in 1985, and the decline in oil prices. Some of the LDCs are also facing serious debt servicing problems, despite what appears to be low debt/GDP and low debt service ratios. Antigua, for example, because of its increasing reliance on commercial finance has experienced a significant growth in debt service obligations. In 1982 and 1983 less than half of accrued debt service obligations falling due were actually paid. Arrears increased from 9.1 per cent of current revenue in 1979 to 47.4 per cent in 1983.[23]

Because of debt servicing difficulties, both Jamaica and Guyana have had to seek re-scheduling arrangements with creditors. The continuing problems facing traditional exports, and the decline in private foreign capital flows, however, still make debt servicing a serious problem. As indicated earlier, Jamaica has relied heavily on IMF funding to help it with its payments difficulties. Belize and Dominica have also sought and received IMF financial assistance. Because of outstanding debts owed by Guyana to this institution, in May of 1985 the Executive Board of the Fund declared this country "ineligible to use the general resources of the Fund". Given the highly conditional nature of IMF credit, developing member countries tend to turn to the Fund as a last resort, and often because the Fund's approval of general economic policies is necessary to gain access to other sources of capital. Though commercial finance is associated with much harder terms that those associated with bilateral or multilateral sources the absence of conditions relating to domestic policies has tended to make it more attractive. In more recent years, however, the tighter liquidity situation and the inability of debtors to repay loans have made bank finance more difficult to obtain. Borrowing countries, themselves, have tried to reduce the share of commercial loans in total debt in order to mitigate the servicing problems. In order to escape from the debt trap developing countries have often called for a greater flow of concessional funds both from governments and multilateral agencies. The operation of the IMF itself has long been regarded as a subject for fundamental reform, given the widespread feeling that its adjustment programmes do not take account of the peculiar conditions prevailing in developing countries.

While the availability of foreign resources gives a government greater flexibility in the pursuit of developmental objectives, debt programmes have to be carefully managed if the gains made are not to be destroyed. Heavily indebted countries are often forced not only to give up development paths they may wish to pursue, but also sovereignty over short-term domestic policy formulation. The diversion of a large proportion of foreign exchange earnings towards debt servicing forces a nation to forego imports which are essential to the functioning and transformation of the economy. Its very capacity to service debt is thus damaged. In this connection, the willingness of creditors to enter into debt re-scheduling arrangements may have forestalled a stronger tendency to limit the amount of foreign exchange earnings that should go into debt servicing, as Peru decided to do a short time ago.

Concluding observations

The evidence indicates that foreign capital has played an important role in helping Commonwealth Caribbean countries to maintain a higher level of imports than would otherwise have been possible. The higher growth rates experienced by some of the economies in the 1950s and 1960s were associated with significant foreign inflows, particularly at the private sector level. In recent years capital movements stemming from government borrowing have dominated capital flows, particularly in the MDCs. Some countries, however, are finding it increasingly difficult to borrow in the light of poor economic performance, debt servicing difficulties, low credit rating and stricter policies by international banks. This situation combined with low or declining public sector savings, exclusion from the soft loans window of the World Bank and the influence of certain foreign govenments and multilateral agencies have led Commonwealth Caribbean governments to make a renewed commitment to attracting privage foreign capital. This development has no doubt also stemmed from a certain amount of dissatisfaction over local private sector performance and the conviction that access to certain kinds of technology needed can only be gained in this way. One suspects, too, that there is a feeling by the governments of these countries that they can bargain more effectively with foreign investors with respect to the division of benefits.

Whatever the merits in this policy, there are pitfalls in any strategy which place too high a reliance on foreign capital, particularly when the latter is viewed as a substitute for efforts at the domestic level. It is possible that with more imaginative policies and a higher level of fiscal responsibility a greater proportion of capital formation could be financed from local sources. It is possible too, that the crucial impediments to growth may not be a shortage of foreign capital, but poorly conceived macro-economic policies, the socio-political environment and weaknesses in investment strategy. For instance it can be argued, with a fair amount of evidence, that governments have allowed too high a proportion of foreign exchange resources to be spent on consumption.[24] The availability of foreign resources may have served to weaken the resclve to pursue policies aimed at getting a more satisfactory performance in the current account of the balance of payments. Specifically issues relating to the pursuit of realistic exchange rates and productivity have been ignored for far too long. With respect to public investment policy there is a feeling that the mix of directly productive/infrastructural investment may have been too much in favour of the latter.

It is evident that the absence of regional foreign investment policy and a strong commitment to regional industrial programming have resulted in a great deal of capital wastage. Duplication of facilities throughout the region is undoubtedly one factor explaining the under-utilization plants in the various territories, and the high costs of production. The needeto create jobs, and competition among the territories often lead governments to grant concessions to foreign enterprises, which have not served the long-term development interests of these countries. The setting up of local assembly plants generally has not led to foreign exchange savings or earnings, given the continued dependence on imports of intermediate inputs and capital goods, and the low propensity to export. There are indicaticn, too, that because of poor long-term planning and inadequate implementation capacity, the debt projects are not the ones always selected for finance.

As indicated in the paper, growth, by avoiding the compression of developmental imports, is facilitated by an inflow of foreign short- and long-term capital. Capital flows, however, are very volatile, responsive as they are not only to the domestic, political and economic situation, but to the whims of foreign governments who may be influenced by perceptions of what is or what is not an acceptable government in the host country. In the past, capital inflows both to public and private sectors, reduced the urgency with which disequilibrium in the current account should have been attended. Debt servicing problems and the increasing difficulties being encountered by some states with respect to foreign borrowing, plus the fact that private capital is not flowing at the desired rate have forced governments not only to reduce the level of imports, but to pay greater attention to increasing exports. The conditionality attached to funds from multilateral agencies and its effects on domestic policy objectives have also generated some concern with respect to strategies which envisage a critical dependence on these institutions. A question that remains in the context of the changing international environment is, to what extent should Commonwealth Caribbean countries encompass foreign capital as an element in development strategy. Specifically with respect to the current account, and this may relate both to development needs and the standard of living, the question can be posed in terms of, to what extent should they pursue disequilibrium policies, assuming as this does, a certain amount of capital inflows to cover the deficit. The fact that dependence on foreign capital seems to be inconsistent with to independent /a political stance, or the pursuit of certain kinds of economic and social policies, would suggest that this question has to be answered in a framework that encompasses a wide range of economic and political variables, if contradictions between political behaviour and the dictates of economic policy are to be avoided.

Footnotes

1. This followed the adoption of a similar resolution by the UN in 1960.

2. At the 1968 Conference the resolution specified 1 per cent of GNP at market prices and not national income. Since the former tends to be higher than the latter, the effect of the UNCTAD action was to raise the target.

3. See *Partners in Development: Report of the Commission on International Development* (Washington, D.C.: Praeger Publishers, 1969) pp 147-9.

4. 'International Development Strategy for the United Nations Development Decade', Resolution adopted by the 25th Session of the United Nation General Assembly, New York, 1970, A.Res/2626 (xxv)

5. See IMF, *The Fund, Commercial Banks and Member Countries*, Washington, D.C., April 1984. p 5.

6. One of the best known of these models was the Chenery-Strout model that came to prominenace in the mid-1960s. See H.B. Chenery and A.M. Strout "Foreign Assistance and Economic Development" in the American Economic Reviews, September, 1966.

7. See, for example. G.E. Papanek, "Aid, Foreign Private Investment and Growth in Less Developed Countries", Journal of Political Economy, Jan/Feb., 1973.

8. For a useful discussion on these problems see B.S. Cohen, Balance of Payments Policy. (Harmondsworth: Penguin Books Ltd., 1970: pp 39-45.

9. See Peter Wilson, International Economics - Theory, Evidence and Practice (Brighton: Wheatsheaf Books Ltd., 1986), p 161.

10. See, for example, Keith Griffin "Foreign Capital, Domestic Savings and Economic Development", Bulletin - Oxford University Institute of Economics and Statistics, May, 1970.

11. See, for example, N.L. Leff, "Marginal Savings Rates in the Development Process: The Brazilian Experience", Economic Journal, September, 1968.

    See also K. Griffin and J.L. Enos, Foreign Assistance: Objectives and Consequences, Economic Development and Cultural Change, April, 1970.

12. It should be pointed out that part of the public sector outstanding external debt consists of foreign currency loans extended by resident financial institutions.

13. Mrs. Fedrica Robinson, "Jamaica Balance of Payments Adjustment Process (1980-83)" in Bank of Jamaica, Balance of Payments of Jamaica, 1984.

14. Trends in direct investment income for recent years have been significantly affected by losses suffered by the mining sector. These losses reflect the level of which inflows by the companies to cover production cost are higher than the market value for the bauxite and alumina exported during the year. (See Bank of Jamaica, Balance of Payments of Jamaica, Various Issues.

15. See Central Bank, Annual Report 1978. p 23.

16. See the 1980 Budget Speech.

17. IMF, Foreign Private Investment in Developing Countries, Washington, D.C., 1983. p 3.

18. Ibid.

19. See OECD, International Investment and Multinational Enterprises - Recent International Direct Investment Trends, Paris, 1981, pp 32-33.

20. W. Arthur Lewis, "Economic Development with Unlimited Supplies of Labour", The Manchester School, May, 1954.

21. For an interesting discussion of this and related issues see Grant L. Reuber et al. Private Foreign Investment and Development, London, O.U.P. Press, 1983, pp 37-38.

22. See Owen Jefferson, "Jamaica's External Debt: Size, Growth, Composition and Economic Consequences", Paper presented at Symposium, Jamaica's Foreign debt: The Crisis and Possible Solutions, Mona, May 10, 1986.

23. World Bank, Antigua and Barbuda, Economic Report, Washington, D.C., 1985, p 13.

24. See Compton Bourne, "Government Foreign Borrowing and Economic Growth: The Case of Jamaica", Social and Economic Studies, December 1981.