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CURRENT CARIBBEAN BALANCE OF PAYMENTS PROBLEMS AND POLICIES: A REGIONAL APPROACH

The Balance of Payments is a clear reflection of the structure of the economy and the nature of the relationships with other countries. In the case of Commonwealth Caribbean Countries, the balance of payments by itself, illustrates the significance of the traditional sectors in the production structure, the import substitution bias and or the under-development of the industrial sector, the heavy reliance on foreign assistance and the significance of foreign ownership within the economy. At the same time, the balance of payments represents a constraint on domestic economic policies. This can be clearly demonstrated on the basis of the proposition that in an economy characterised by rigidity of the structure of production and in which the capital goods producing sector is of minor significance, the upper limit to the growth of output is set by the availability of foreign exchange. This proposition links the growth of output to the level and rate of capital formation which is largely determined by the economy's ability to import capital goods.

In the light of the relationship between the balance of payments, domestic economic policies, the economic relationships arising out of international economic co-operation and competition, and the structure of the economy, problems relating to the balance of payments could be a reflection of the failure of domestic economic policies to so adjust the level and structure of supply on the one hand, and the level and structure of demand on the other hand as to make the size and composition of imports a true reflection of demand which, given certain technological constraints, cannot be met from local sources.

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The problem might also be a reflection of the failure of domestic policies to so change the structure of the economy as to make it impossible or difficult for the relationship between the domestic economy and the rest
render ineffective
of the world to negage domestic economic policies which are formulated on the basis of the assumption that the local authorities have full control over policy formulation and policy implementation.

The fact is that if problems relating to the balance of payments in Caribbean economies can be identified as having their origin in the type of relationships which exist between the domestic economies and the metropolitan economies, then the policy prescriptions are obviously quite different from those which would be appropriate in a situation where the problems have their origin in those sectors and in the types of relationships within the local economy over which the authorities have full control.

This paper seeks to analyse briefly the nature and extent of the balance of payments problem now faced by Caribbean economies to identify and evaluate the current policies which have been formulated for dealing with them and to outline where possible, alternative policies and strategies. The paper is divided into three parts. In the first part, the problems are analysed. Part II deals with current policies, while Part III deals with alternative policies.

The structure of the paper and the extent of the analysis of each question investigated is substantially circumscribed by the availability of data. It is regretted that a number of issues have not been fully explored in quantitative terms in this paper and have come in for mere mention largely as a consequence of the fact that the appropriate data are not available.

We point out also that data availability has also compelled us to base our analysis and conclusions for the region as a whole on a limited range of data relating to the independent Commonwealth Caribbean Countries except Grenada. We are confident, however, that the problems and issues isolated in relation to the M.D.C.'s exist to an even greater extent in the case of the L.D.C.'s. We feel, therefore, that a great deal of damage has not been done by basing our analysis, findings and recommendations on data relation to four countries.

PART I

THE PROBLEM

There are two approaches to an analysis of balance of payments disequilibrium. The first approach is based very simply upon an analysis of movements in net foreign exchange reserves. In this approach, one simply establishes the trend in net foreign exchange reserves and then go on to indicate or analyse the main factors which operate upon the trend identified. In the second approach, the analysis is based upon the relationship between net national import capacity (1) and total imports. Since the import itensity of export production is taken into account in the definition of net national import capacity, the latter approach has a strong structural bias and is to be preferred to the former. In this paper, the problem is examined on th basis of both approaches.

NET FOREIGN EXCHANGE POSITION

As a general rule, a decline in net foreign exchange reserves the country's holdings of foreign exchange reserves is an indicator of t fact that the economy has bought abroad more that it has sold abroad an imbalance is financed from the country's holdings of foreign exchange.

(1) Net National Import capacity is defined as the value of merchand exports, of plus exports of services, plus net capital inflows, min imports/intermediate goods used in the export sectors.

It is generally agreed that a presistent decline in a country's foreign exchange reserves constitutes a danger signal. In this section of the paper, we examine trends in the net foreign exchange reserves of Jamaica, Trinidad and Tobago, Barbados and Guyana during the period 1970-1973.

TABLE I

Changes in Net Foreign Exchange Reserves

EC$mn.

	1970	1971	1972
Guyana	+3	-12	-20
Trinidad & Tobago	-1[illegible].8	-39.7	+46.3
Barbados	+0.6	- 9.2	+10.2
Jamaica	-40.0	-82.5	+98.9

(-) Increase
(+) Decrease

Jamaica

Jamaica's net foreign exchange reserves declined by EC$127.5m during the period 1971 to 1973. This trend compares very unfavourably with that relating to the 1970-1971 period. As will be seen from Table I net foreign exchange reserves increased significantly in 1970 and again in 1971. The decline in reserves in Jamaica is attributable to four main sectors:

(i) the rapid increase in merchandise imports;

(ii) the relatively slow growth in merchandise and services exports;

(iii) the decline in net capital inflows; and

(iv) some outflow of private capital.

Jamaica's balance of visible trade increased from EC$202.7m in 1970 to EC$275m in 1972 and EC$366.4m in 1973. This growth in the deficit is largely the result of a wide differential between the rate of growth of imports and the rate of growth of exports.

Jamaica's visible imports increased from EC$850.6m in 1970 to EC$1178.2m in 1973. This represents an increase in imports of EC$327.6m or an annual average increase of EC109.2m. The increase in imports during this period was substantially influenced by the imports of consumer goods especially food and motor vehicles and raw materials. Imports of petroleum and petroleum products also increased sharply. Price increases were important in the growth in the value of imports which took place during the period under review.

Merchandise exports on the other hand grew at a relatively slow rate. There was an average annual increase in the value of exports of $54.6m or 25.3% during the period under review. This increase in the value of exports is largely attributable to bauxite and alumina. An important point to note is that during the period 1968-1972, the volume of exports of most traditional items had shown significant decreases.

The trend relating to the services account was also unfavourable. During the period 1970-1973 the deficit on services account increased from $127.7m to $194.1m or at an annual average rate of 17.3%. The growth in the deficit on services account was largely influenced by the relatively slow annual growth of earnings from tourism and the dramatic increases in investment income payments. These payments increased from EC$216m in 1970 to EC$317.5m in 1973. The growth in payments relating to this item is quite clearly a reflection of the dominance of foreign capital within the economy and in particular the significance of foreign capital in the bauxite and alumina industry within the economy. The increase in the deficit on the services account is due also, although to a far less significant extent, to the increase in foreign travel by Jamaicans.

The extent to which capital inflows does play a significant part in the trends in net foreign exchange reserves in Jamaica can be clearly illustrated on the basis of the data for the period 1971 or 1970-1973. Net foreign capital inflows declined from a peak of EC$364m in 1971 to EC$255m in 1972. At the same time, net foreign exchange reserves declined from EC$217.5m in 1970 to EC$201.4m in 1972. In 1973, however, net capital inflows increased by $181.4m over 1972. At the same time, net foreign exchange reserves declined by $59.7m. With regard to capital outflows, it has not been possible to quantify this to any precise extent.

The trend which emerges, therefore, is one in which the rate of increase in the deficit on merchandise and services accounts accelerated. At the same time, capital inflows, the main determinant of the net foreign exchange reserves during the period, declined.

Trinidad and Tobago

The balance of trade deficit of Trinidad and Tobago rose from EC$77.5m in 1970 to EC$302.3m in 1972 a percentage increase of over 207%. This growth in the balance of trade deficit is attributable to approximately the same factors which influenced trends in Jamaica's balance of trade. The value of imports grew at a much more significant rate than the value of exports.

In the case of Trinidad, merchandise imports increased by $363m or at an annual average rate of 16.7% during the period 1970-1972. Visible exports, on the other hand, increased by $137.3m or at an annual average rate of 6.6% The deficit on services account, however, declined from $59.3m in 1970 to less than EC$1m in 1972. Available data do not permit an in depth analysis or an explanation of the movements in the balance on services account. Net capital movements declined during the period 1971-1972 and this was accompanied by a decline in net foreign exchange reserves during the period.

The pattern observed in respect of Trinidad and Tobago is not unlike that which is outlined above in respect of Jamaica:

(a) a rapidly rising balance of trade deficit due largely to substantial disequilibrium between the rate of growth of imports and the rate of growth of visible exports. The bulk of the increase in imports was largely a reflection of rapidly escalating import prices at source as well as increasing volume of imports, particularly, of raw materials and food stuffs. The relatively slow growth in merchandise exports on the other hand, is a reflection of the slow growth or in some cases, the decline in primary export production and the relatively slow growth in export industrial production;

(b) a continuous deficit on services account due largely to the rapid growth in payments in respect of investment income and the slow growth in exports of services.

In so far as net foreign exchange reserves increased, this increase was largely a reflection of the increase in capital inflows.

Barbados

In the case of Barbados, the balance of payments trend during the period under review was even more unsatisfactory. Over 70% of total visible export earnings come from sugar. Sugar production, on the other hand, has been declining at a relatively rapid rate since the last three or four years. This, coupled with a marked increase in the rate of growth of imports led to a significant widening of the trade gap especially during the period 1970-1972.

Merchandise exports declined from $61.8m in 1970 to approximately $60m in 1972. Visible imports on the other hand, increased from $235m in 1970 to $268m in 1972. The trade deficit increased from $155.9m in 1970 to $197.4m in 1972.

An important point to note in the case of Barbados is that during the period under review, the balance of payments position was substantially influenced by trends in the services account and in particular, by the growth in tourism. During the period 1970-1972, the balance on services account increased from EC$79.8m to EC$109.2m.

The pattern of movement and the role of capital inflows has been similar to that observed in the cases of Jamaica and Trinidad and Tobago.

Guyana

Guyana recorded a surplus on visible trade account during the period 1970 to 1972. There was, however, a deficit on services account throughout the period, with payments in the form of investment income as the largest single component of this account.

Of significance is the fact that the balance on current account declined from EC$35.5m in 1970 to EC$18.6m in 1972. Capital inflows, on the other hand, increased from EC32.6m in 1970 to EC$37.2m in 1972. At the same time, a declining trend in net foreign exchange reserves of the period 1968 to 1970 was reversed during the period 1971 and 1972.

The data reveal that there was a marked difference between the trend in the balance of payments position of Guyana and the rest of the Commonwealth Caribbean during the 1970-72 period. There was a net increase in foreign exchange reserves in the former while the latter had a persistent decline in reserves. It should be noted, however, that notwithstanding the favourable trend in Guyana's reserves, these reserves represented the equivalent of approximately two months imports of goods and services in 1972. This is about two months less than that which is considered to be a reasonably safe position by international standards. Jamaica was in the same position in 1972. It can be concluded, therefore, that the Guyana's balance of payments position was as precarious as that of the rest of the Commonwealth Caribbean, in spite of the fact that her foreign exchange reserves increased during the period.

As was indicated at the outset of this paper, an alternative approach to analysing trends in the balance of payments position of the region, is to examine trends in national import capacity in relation to the value of total imports.

Jamaica's net national import capacity at current prices increased from approximately EC$1429m in 1971 to EC$1800m in 1973. This represents an annual average increase of EC$185,5m or 15%.

in Jamaica is regarded as representative of the regional position and underscores the main underlying cause for the deficit on current account as well as the decline in net foreign exchange reserves observed above. The factors which account for the relatively slow growth of import capacity and the rapid growth of imports were examined in the treatment of trends in net foreign exchange reserves.

FURTHER AGGRAVATION OF THE BALANCE OF PAYMENTS POSITION IN 1973

The data used in analysing the balance of payments position of the four independent territories of the region were in the main related to the period 1970-1972. The point should be stressed, however, that since 1973 there was an aggravation of the balance of payments position of these territories due substantially to significant increases in the prices of a wide range of important raw materials and intermediate products as well as consumer goods. The increase in the price of crude oil had the greatest impact on the balance of payments position of the territories of the region. While it changed the balance of trade of Trinidad and Tobago from a deficit to a surplus position it placed the rest of the region in an even more precarious balance of trade and payments position.

In the case of Jamaica, the increase in the price of oil will, on the assumption that there is no growth in export earnings, add to her balance of trade deficit by some EC$159.1m in 1974. In the case of Barbados, the change in the deficit estimated on the same basis will be an increase in the balance of payments deficit of some $30m in 1974. The increase in Guyana's balance of trade deficit will be of the order of EC$46.5m. The rest of the Caribbean finds itself in very much the same position as Jamaica, Barbados and Guyana.

The balance of payments position of Commonwealth Caribbean countries was severely aggravated in 1973 and will be significantly affected in 1974 not only by the increase in the prices of petroleum and petroleum products, but by the significant increases in the prices of a wide range of food items and raw materials. These increases and their effects demonstrate the extent of the dependence of the region on the imports of essential foods and raw materials from third countries and the extent to which policy changes in the metropolitan countries have direct and far reaching effects on regional economies and in particular, the balance of payments position of these territories. It is because the imports affected in this way, fall in the category of competitive imports, that is, imports that can be economically produced within the region, that the conclusion is drawn below that an important strategy for dealing with the current balance of payments problem of the region must entail the type of policy changes which can lead to a re-structuring of the relationship between regional economies and third countries as well as a re-structuring of regional economies themselves.

The magnitude of the increases in the prices of imported food products and raw materials and the effect of these increases on the balance of trade and payments position of the region can be illustrated on the basis of data relating to the Jamaican economy:

(i) In mid-1972 the price of wheat was EC$153.8m (c.i.f.) per metric ton. By the end of 1972, it was increased to EC$473.4m per metric ton; and the current price is EC$495.4m per metric ton. This is an increase of over 200 per cent between 1970 and 1973.

(ii) The price of soya meal in 1972 was EC$220.7 per ton. By December 1973, the price increased to EC$977.3 per ton; and increase of over 400 per cent.

(iii) In the case of corn, the price stood at approximately EC$104.5 per ton in 1972. By the end of 1973 it had increased to EC$322per ton - an increase of over 300 per cent .

(iv) In February 1972, bulk rice from Guyana was EC$23 per 180 lb. bag (c.i.f.); at December 1973, it increased to EC$44.7 per ton, an increase of approximately 100 per cent. It should be noted,however, that the price of rice imported from U.S.A. sources increased at a much faster rate than that of rice imported from Guyana.

(v) In June 1971, milk solids was bought at EC$661.4 per long ton (c.i.f.). This increase to EC$1200.3 per long ton (c.i.f.) by the end of 1973 and at present, the price is approximately EC$1795 per long ton - an increase of approximately 175 per cent between June 1971 and January, 1974.

It is expected that while the prices of the items listed above will not increase as rapidly in 1974 as they did during 1973 and 1972, there will , however, be some increase in these prices and in any case, the increases which took place during the last two years are such they they will have a significantly adverse effect on the balance of payments position of regional economies in 1974.

It seem clear, therefore, that the weak balance of payments position of the regional economies which has been identified in respect of the period up to 1972 has been significantly worsened by changes in the prices of a wide range of essential imports including oil. Caribbean Commonwealth economies excluding Trinidad and Tobago are however truly in the midst of a severe balance of payments problem.

It can be concluded, therefore that the continuous deterioration in the balance of payments position of Commonwealth Caribbean territories is due largely to:

(a) sluggish growth in visible exports due largely to a decline in the production of agricultural exports and the slow growth of industrial production for export. The sluggish growth of export was also due to the relatively slow growth in the prices of most primary exports;

(b) rapid increases in imports especially of raw materials and consumer goods due both to an increase in the volume of imports and a rapid increase in the prices of imports;

(c) a steady, and in some cases, a rapid increase in the deficit on services account due to the relatively slow growth of earnings from tourism since 1970 and the significant growth in payments in respect of investment incomes - a trend which is substantially dictated by the fact that there is significant foreign capital participation in regional economies;

(d) the significant increases, firstly, in the price of crude oil in the latter part of 1973 as well as the massive increases in the prices of grain and other important raw materials and food-stuffs during 1973;

(e) a fall in capital inflows or an increase in capital outflows or both;

(f) over valuation of the currencies of the region. (this factor has so far not been analysed)

PART II

CURRENT POLICIES FOR DEALING WITH BALANCE OF PAYMENTS PROBLEM

It cannot be said at this stage that clear cut regional policies for dealing with the balance of payments problem analysed above have been completely formulated. There are, however, a number of proposals under discussion - proposals which could be drawn together into a meaningful regional package. Some of these proposals will be discussed in this section of the paper. There will be discussed, also the areas of agreement which have so far emerged at the regional level.

The discussion of current policies can quite appropriately commence with a brief review or summary of the policy measures within individual territories. As in the case of the analysis of the problem, the examination of current policies will be restricted to the four M.D.C.'s .

The basic components of the strategy which has been adopted by these territories are exchange control, quantitative import restrictions and in some cases higher import duties, credit control, other measures aimed at containing the demand for consumer goods, the revision of prices relating to sugar, bananas and bauxite and measures the objective of which is the expansion of domestic production.

Both Jamaica and Guyana have resorted to quantitative restriction on a wide range of consumer imports. Both territories have placed all imports under specific import licence. Both territories have prohibited the importation of a long list of consumer items. All imports are placed under specific licences on the basis that foreign exchange allocations to imports can be determined strictly on the basis of the relative importance of each category of imports. Thus severe restrictions have been imposed on luxury consumer goods. In the case of capital goods, the authority are placed in a position to link the import policy relating to these items very closely to the objective of ensuring that there is maximum utilization of the existing stock of capital. It should be observed, however, that the range of data required to facilitate the implementation of such a policy has not yet been compiled. (Data on capacity utilization, etc.).

A brief survey of policy measures at the national level show that:

> In Jamaica, the Bank Rate was increased. The Treasury bill rate, the commercial banks saving and deposit rates as well as prime advance rates were also increased. In addition, the central bank asked the commercial banks to implement a selective lending policy. Personal loans, loans to the distribution sector as well as instalment credit were restricted. In addition to these measures, the Bank of Jamaica placed a ceiling on rediscounting facilities to the commercial banks.

Several exchange control measures were resorted to by the Jamaican authorities:

(a) Foreign assets held abroad by residents of Jamaica had to be declared and a period specified for their repatriation.

(b) Limitations were placed on payments abroad in respect of gifts. A ceiling of J$150 per annum was established.

(c) Travel allowances for holiday purposes was substantially reduced. The reduction was from $500 to $350 per person and travel restricted to two trips per annum.

(d) The sale of foreign exchange in respect of football pools and other gambling purposes was prohibited.

(e) Exporters were requested to have the proceeds in respect of export sales paid to commercial banks locally.

In addition, the measures relating to interest rates, credit and exchange control, restrictions were imposed on a wide range of imports especially consumer imports. In the first place, a ceiling was placed on the total value of goods to be imported during 1974. In establishing this ceiling, care was taken to ensure that imports required for domestic production were fully accommodated.

The measures taken by Guyana in response to the balance of payments situation followed closely those outlined in respect of Jamaica. The measures were mainly in the areas of credit control, exchange control and the physical restriction of imports. It should be pointed out, however, that in terms of a total prohibition of consumer imports and restriction on the use of foreign exchange for foreign travel and payments in respect of gifts, the measures announced by the Guyana Government were more far-reaching than those announced by Jamaica.

It can be said that the response of the Barbados Government to the balance of payments problem has been less far-reaching than those instituted by Jamaica and Guyana. In fact the same could be said for the rest of the Caribbean. This is borne out by the fact that much has not so far been done in respect of the physical restriction on imports. The policy of import restriction so far, is based on the imposition of consumption duties on a fairly wide range of items. It is not clear, however, that the imposition of consumption duties by the Barbados Government has as its underlying objective, the restriction of imports. Judging from the type of items which have been taxed and the level of the duty, the conclusion could be drawn that revenue yield was the main objective.

The dramatic reversal in trend which has been taking place in the balance of payments position of Trinidad and Tobago consequent on the increase in oil prices her in a position to resort to a package of measures which have inflation and not the balance of payments as the main focus.

However, we raise the question as to whether improvements in the balance of payments which hinge entirely on increases in the prices of petroleum and petroleum products, make it unnecessary for Trinidad and Tobago to take the steps required to deal with the basic problem of the balance of payments. If the balance of payments position is merely a reflection of the structural imbalances within the economies of the region a point which has been argued in this paper, but not satisfactorily settled, . . an it can be concluded even without further examination that improvements in the balance of payments position of territories of the region consequent on increases in the prices of primary and secondary exports do not remove the pressing need for measures to be taken to effect structural changes within the economy.

An examination of what can be described as the negative measures so far taken by Commonwealth Caribbean countries reveals that so far, a regional balance of payments strategy has not yet emerged. In the field of monetary policy, such an approach could hardly have emerged given the institutional framework which currently exists for the formulation or determination of such an approach. The Caricom Agreement provides for consultation in the area of monetary policy and currently these consultations take place at the level of meetings of regional Ministers of Finance and Central Bank Governors. However, none of the L.D.C.'s now has a central bank and Barbados has only recently established such an institution. Besides, it would seem quite non-feasible at this point in time for a clearly identifiable regional approach to emerge in the field of monetary policy simply on the basis of consultations involving regional Ministers of Finance and Central Bank Governors. Questions relating to reserve management, payments etc would first have to be settled.

We maintain that steps should now be taken towards establishing the type of institutional framework which makes a regional approach in the area of monetary policy more meaningful. One such step relates to the question of the Currency Board Law which now obtains in the case of the Leeward and Windward Islands. There is agreement at all levels that the time has come for substantial revisions to be made in this Law. The revision should be such as to place the Leeward and Windward Islands in a position to utilize monetary policy as a tool of economic management.

In addition to changing the relationship which now exists between L.D.C.'s Governments and the Currency Board, areas can now be isolated for treatment on a regional basis in order to significantly increase the political feasibility of certain types of policies. One such area concerns the treatment of certain items within the services account of the balance of payments. In analysing the balance of payments problem now faced by the region, attention was directed to the fact that the growing deficit on services account is largely attributable to the significant growth in payments in respect of investment income. It does seem therefore the existing balance of payments situation require that some restrictions be imposed on outflows in respect of this item. It is recognised that the absence of control on such payments in all the foreign exchange policy measures so far taken by Caribbean governments is based on the consideration that in order to establish and preserve the right climate for foreign investment, there must be an absence of control on the investment income payments etc.

It is now proposed that control on payments in respect of investment income be regarded as an important element of regional monetary cooperation.

In spite of the problems in the way of the development of a regional strategy in the area of monetary policy, we regard the broad areas of agreement so far in regional consultations and the common positions taken during the last two years in international forums as indicative of significant progress in regional monetary co-operation. Moreover, the recent initiatives taken by Trinidad and Tobago in the provision of balance of payments support for CARICOM countries with central banks and the provision of assistance in the area of project finance for other CARICOM countries are other important manifestations of regional monetary co-operation. However, it remains true that a logical and effective regional monetary policy directed at the current balance of payments problem of the region is yet to be formulated. We contend that such a policy cannot be formulated within the present regional institutional framework. This dilemma presents a special challenge to the 1974 Regional Monetary Studies Conference.

Import restriction measures have not been formulated and implemented on a regional basis. So far, there has been no serious attempt to harmonize the list of third country products which are to be restricted by CARICOM countries. In the light of the Common External Tariff and Common Protective Policy, such a step would be a logical one. The harmonization of the import restriction programme in the region is justified by the current concern with import substitution on a regional basis. The restriction of a number of products in the import structure on a regional basis would render their production on a low unit cost basis far more feasible.

It will be seen, therefore, that in what can be described as the second major area of balance of payments policy, the restriction of imports, there has not been a regional approach. The failure to formulate such an approach is not attributable to the absence of an appropriate institutional framework. Since a regionally coordinated strategy could be highly beneficial to the region, we urge that steps be taken to adopt such a strategy.

The programme for the short and medium term development of industrial activities highlights an import substitution bias. The industrial activities selected for such development are:

(a) Textiles: The promotion of this industry is predicated on existing and projected regional demand and it has been agreed that an integrated regional plan is required for its development. Export prospects have so far not been examined, notwithstanding the experience of a number of developing countries in successful export development in this area of manufacturing.

(b) Leather and Leather Products:

The plan calls for joint action in the exploitation of import substitution opportunities in leather and footwear.

(c) Cement: The expansion of production of cement envisages the sale of a significant proportion of output to third countries. But this position was arrived at largely as a consequence of the fact that planned national capacity was already far in excess of regional requirements.

(d) Glass, Paper, Fertilizers and Processed foods: The development of all these industries is projected on the basis of import substitution.

We contend that the concentration so far on import substitution has tended to divert attention from the significant scope which must exist for export development in the areas identified. It may be that in the longer term regional industrial development programme full weight will be given to the question of export promotion.

With the establishment of a Working Party of officials on Industrial Development Planning and the Standing Committee of Ministers of Industry, we feel that much progress has been made in the development of an appropriate institutional matrix for treating with theburning question of regional industrial development.

Important decisions were also taken by CARICOM Ministers on the question of agricultural development in the region. Among these decisions is that related to the promotion of selected agricultural activities on a regional basis and the establishment of a regional institution for the promotion of agricultural development. The main concern has been with the promotion of these products, the import prices of which increased dramatically during 1973. Thus, as in the case of the short term industrial development programme the major concern has been with import substitution.

In the light of the foregoing, and against the background of the current balance of payments crisis, we propose that policies directed at the expansion of regional production should contain the following elements:

(a) a careful selection of manufacturing activities for promotion on a regional basis - regionally integrated industries. The selection should be based on dependable criteria;

(b) the establishment of appropriate machinery for the promotion of such industries;

(c) the formulation of a regional industrial strategy in which export development is an important component;

(d) the synchronization of national and regional industrial development programmes on a baiss which permits rapid development;

(e) the formulation of logical and effective programmes - production and marketing - for the sugar and banana industries of the region on a basis which will permit full exploitation of the opportunities which currently exist;

(f) regional collaboration in research in the area of food processing on a basis which permits import displacement and export development in respect of a wide range of food products;

(g) regional collaboration in efforts to secure the establishment of a meaningful price mechanism for primary exports.

In the examination of policies so far formulated for dealing with the current balance of payments crisis, we have sought to identify the regional content of each policy measure against the background of a brief sketch of the advantages which could flow from such an approach. Our findings are:

(i) in the area of monetary policy, there is some measure of co-operation at the regional level. But while scope remains for further co-operation, the existing institutional framework does not permit the development of a meaningful regional policy;

(ii) there has been no harmonization in regional terms of the import restriction policy - the most significant element of the package of policies;

(iii) production programmes have tended to overemphasize import substitution notwithstanding the recognition of the advantages from and scope for export development.

PART III

ALTERNATIVE STRATEGY

The question of a reasonable alternative strategy in response to the balance of payments problem is very relevant. In order to explore this question the main elements of the current national and regional strategies should be restated. They entail, essentially, attempts to control or to slow down the rate of increase of domestic demand for consumer goods, to increase the level ofdomestic saving, to reduce the rate of increase and level of demand for imports within the regional economy, to promote exports and to control the outflow of foreign exchange. It is sought to achieve these objectives mainly on the basis of credit control, foreign exchange control and physical control of imports.

The important missing component of the package is exchange rate policy. We argue that in any regional strategy concerned with the solution of a balance of payments problem, the whole question of exchange rate policy, and in particular, devaluation should be closely examined. There is, however, a great unwillingness touse devaluation as a strategy for dealing with the balance of payments problem within the region. This reluctance is based upon the following considerations:

(a) the effect of devaluation upon the cost ofliving;

(b) what has been identified as the inability of the majority of the export sectors and industries to respond to the stimulus provided by an adjustment of the exchange rate;

(c) the rise in the local currency price of imported inputs into the producing sectors especially manufacturing and the resultant reduction in the competitiveness of export products as well as import substitutes. The high import content of most regional industrial activities makes the concern with this question a particularly important one;

(d) the special marketing mechanism relating to such products as sugar, bananas, bauxite and alumina, which prevents these products from securing an enhancement of their competitive position consequent on devaluation;

(e) the decrease in the real value of natural resources which devaluation entails;

(f) the likely movement of the terms of trade against tourism.

We contend, however, that a policy of devaluation may effectively stimulate and promote export production and encourage import sibstitution in manufacturing and agricultural activities and services. In the West Indian situation this may be further encouraged by:

(a) The fact that many manufacturing industries operate below capacity and it is probably that there is a relatively high short run elasticity of supply of such products. Moreover, the higher local currency price of imported capital goods (machinery and equipment) may offer further advantages. In that it may tend to reduce the highly inappropriate capital itensity of production in the West Indies - a Region with a large pool of surplus labour.

(b) The low import content of both export and domestic agriculture (except for livestock which depends on imported animal feed.)

(c) The highly competitive nature of West Indian tourism which makes it very likely that the number of North American tourists to the West Indies is likely to increase as a result of a reduction in the price of a holiday.

(d) It is unlikely that the terms of trade will deteriorate partly because of the small amount of West Indian exports of a particular commodity in relation to total world exports and partly because many West Indian products are sold in administered markets abroad.

The argument for devaluation as a desirable part of the package of regional policies for dealing with current balance of payments is based on the notion that the currencies ofCARICOM countries are overwhelmed both in the sense that the rate of exchange is a contributory factor to the balance of payments problem and in the sense that given the cost/profit ratios in agriculture, manufacturing and tourism, the required structural changes and the required increase in employment are in some significant way impeded by the fact that the exchange rates of these countries are inappropriate.

We recognise however, that devaluation by itself could do more harm than good. The adoption of a devaluation strategy requires therefore such companion policies as Prices and Incomes, Monetary, Fiscal and policies for the stimulation of Domestic Production. Prices and Incomes Policy becomes an even relevant more relevant part of the package of policies in view of the fact that regional economies are faced, not only with a severe balance of payments problem but also a high rate of inflation and inequitability in the distribution of real income. Incomes policy is seen as having a favourable effect not on the control of inflation but also on the balance of payments, employment creation and the distribution of real income.

The main elements of the alternative regional strategy proposed by us are:

(a) Devaluation on a regional basis. The justification for a regional approach lies in a recognition of the fact that the workings of the Common Market could be disturbed if all member countries did not resort to exchange reate adjustment on a uniform basis. We suggest that there is no need for a once and for all devaluation. Exchange rates could be adjusted on an annual basis depending on the relative rates of inflation within domestic economies and in the economies of our main trading partners.

(b) A prices and incomes policy to be formulated and implemented by all member countries of the Common Market. Regional cooperation with the respect to this policy would serve to enhance the political feasibility of the policy as well as ensure the success of other regional balance of payments measures.

(c) Modification of the policy of physical restriction of all imports - a strategy which is currently pursued by Jamaica and Guyana. With devaluation, the restriction of imports would depend upon the upward adjustments in prices of these goods.

(d) The formulation of a comprehensive export development policy with export subsidies and market research as important elements.

(e) Continuation with efforts directed at the formulation and implementation of an effective regional import substitute programme, with regionally integrated industries as an important component.

(f) A regional approach to securing price revisions in respect of those exports which are marketed under special contracts: sugar, bananas, bauxite etc.

We contend that the package recommended above would place regional economies in a strange position to solve the current balance of payments problem and at the same time permit them to check the high rates of inflation which exists in these economies.

SUMMARY OF CONCLUSION AND RECOMMENDATIONS

Conclusions

(1) The underlying causes of Commonwealth Caribbean balance of payments problem have been identified as:

(a) Sluggish growth in visible exports due largely to a decline in the production of agricultural exports and the slow growth of industrial production for export. The sluggish growth of export was also due to the relatively slow growth in the prices of most primary exports.

(b) rapid increases in imports especially of raw materials and consumer goods due both to an increase in the volume of imports and a rapid increase in the price of imports.

(c) A steady, and in some cases, a rapid increase in the deficit on services account due to the relatively slow growth of earnings from tourism since 1970 and the significant growth in payments in respect of investment incomes - a trend which is substantially dictated by the fact that there is significant foreign capital participation in regional economies.

(d) The significant increases, firstly in the price of crude oil in the latter part of 1973 as well as the massive increases in the prices of grain and other important raw-materials and foodstuffs during 1973.

(e) A fall in capital inflows or an increase in capital outflows or both.

(f) Over-valuation of the currencies of the region.

(2) Improvements in the balance of payments position of Trinidad and Tobago consequent on increases in the prices of primary and secondary exports do not remove the pressing need for measures to be taken to effect structural changes within that economy.

(3) An examination of current regional policies related to the balance of payments problem reveals that:

(a) in the area of monetary policy, there is some measure of cooperation at the regional level. But while scope exists for further cooperation, the existing institutional framework does not permit the development of meaningful regional policies;

(b) there has been no harmonization in regional terms of the import restriction policy;

(c) production programmes have tended to overemphasize import substitution.

(4) A clear case exists for devaluation and such companion policies as prices and incomes policy to be considered as important elements of the strategy.

Recommendations

(1) Steps should now be taken towards establishing the type of institutional framework which makes a regional approach in the area of monetary policy more meaningful.

(2) Question of the Currency Board Law which now obtains in the case of the Leeward and Windward Islands should be carefully considered. There is agreement at all levels that the time has come for substantial revisions to be made in this Law. The revision should be such as to

place the Leeward and Windward Islands in a position to utilize monetary policy as a tool of economic management.

(3) Control on payments in respect of investment income be regarded as an important element of regional monetary cooperation.

(4) A regionally co-ordinated strategy could be highly beneficial to the region particularly with respect to the restriction of imports, and the current concern with import substitution on a regional basis.

(5) (a) A careful selection of manufacturing activities for promotion on a regional basis - regionally integrated industries - the selection based on dependable criteria.

(b) The establishment of appropriate machinery for the promotion of such industries.

(c) The formulation of a regional industrial strategy in which export development is an important component.

(d) The synchronization of national and regional industrial development programmes or a bias which permits rapid development.

(e) The formulation of logical and effective programmes - production and marketing - for the sugar and banana industries of the region on a basis which will permit full exploitation of the opportunities which currently exist.

(f) Regional collaboration in research in the area of food processing on a basis which permits import displacement and export development in respect of a wide range of food products.

(g) Exchange rate policy must be seen as an important part of any regional strategy concerned with the solution of the balance of payments problem.

(6) The main elements of the alternative strategy proposed by us are:

(a) Devaluation on a Regional basis. The justification for a regional approach lies in a recognition of the fact that the workings of the Common Market could be disturbed if all members did not resort to exchange rate adjustment on a uniform basis. We suggest that there is no need for a once and for all devaluation. Exchange rates could be adjusted on an annual basis depending on the relative rates of inflation within domestic economies and in the economies of our main trading partners.

(b) A prices and incomes policy should be formulated and implemented by all member countries of the Common Market. Regional co-operation with respect to this policy would serve to enhance the political feasibility of the policy as well as ensure the success of other regional balance of payments measures.

(c) The modification of the policy of physical restriction of all imports - a strategy which is currently pursued by Jamaica and Guyana. With devaluation, the restriction of imports would be dependent upon the upward adjustment in the prices of these goods.

(d) A regional approach to securing price revisions in respect of those exports which are marketed under special contracts - sugar, bananas, bauxite, etc.

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