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REGIONAL FLOW OF INVESTMENT:

THE NEED FOR AND ATTEMPTS AT RECHANNELLING

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INTRODUCTION

In this paper we have looked at Caribbean Capital flows specifically from the aspect of rechannelling of investment within the region.

The main arguments of the paper centre on the following premises:

(1) The differences in investment levels in the MDCs and the LDCs stem from built in factors associated with distribution of resources.

(2) The development of the whole area is dependent on the strengthening of the weak links.

(3) The removal of constraints in some existing institutional structures would aid in bringing about more rapid integration.

The paper analyses the structure of the economies of the region, looks at the CARIFTA/CARICOM organisation and the institutions associated with these and analyses their structure in terms of their likely effectiveness. Experiences have also been drawn from other areas which have attempted similar integration movements. Their problems and attempted solutions are discussed and the possibility of applying the lessons learned to the CARIFTA/CARICOM area is considered.

REGIONAL FLOW OF INVESTMENT:
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SECTION I - THE STRUCTURE OF THE ECONOMIES

Characteristics of the Economy

The Caricom territories have traditionally been underdeveloped dependent economies which demonstrate a persistent pattern of imbalances in growth and development both between the territories themselves and between the sectors of each economy. The common structural characteristics which make themselves manifest in all the territories are:-

1. a heavy dependence on exports and imports;
2. a pattern of production in which there is concentration in terminal activities, i.e. production of either primary products or an assembling of final products;
3. an unintegrated structure of production that leaves very little linkage if any at all between the sectors;
4. a high level of structural unemployment and underemployment;
5. a very underdeveloped domestic agricultural sector and a high cost agricultural export sector dependent on preferential shelter in metropolitan markets;
6. fairly rapid rates of growth in the modern sectors -- mining, tourism, and manufacturing; and
7. dependence on foreign decision-making by large corporations which bring in capital, technology and management and entrepreneurial skills into the economy.

On a regional basis, distinction has been made between more-developed countries and less-developed countries. The former group comprises of Barbados, Guyana, Jamaica and Trinidad and Tobago, while the latter includes Antigua, Dominica, Grenada, Montserrat, St. Kitts-Nevis-Anguilla, St. Lucia, St. Vincent and Belize. The distinction is based on the economic variables of:-

1. gross domestic product (both aggregate and per capita); and
2. population.

The more-developed countries account for approximately 87 per cent of the total regional population and 93 . per cent of the aggregate gross domestic product. In respect of per capita gross domestic product, the 1970 figures show that the more-developed countries average U.S.$600, while the less-developed countries average U.S.$300. The more-developed countries were also responsible for 95 per cent of the total regional production.

These facts seem to indicate that the more-developed countries are better off than the less-developed countries but relative social welfare can easily be clouded when only aggregates are considered. What is concealed is the fact that the rate of unemployment is almost the same in both groups, and the inequality of the distribution of income leaves some parts of the population of both groups at very low standards of living. We see, therefore that the problems of underdevelopment are common to both groups and the distinction is only one of degree.

The difference in the levels of development generally, reflect differences in investment flows, and the following structural factors have

been mainly responsible for the existing pattern:-

(a) Resources

The more-developed countries, with the exception of Barbados, are mineral-dependent economies, with bauxite in Guyana and Jamaica and natural gas, oil and asphalt in Trinidad and Tobago. In the individual territories, the mineral-based industries have been the dominant features of the economy without really becoming part of it. They provide a large part of government revenue in the form of taxes and royalties, earn foreign exchange, and are the major source of production. Nevertheless, because of the enclave nature of their operations, they have not fulfilled the role of "leading sectors" for which they are potentially suited.

The less-developed countries, on the other hand, rely on the traditional agricultural sector which does not have the income-earning capacity of the mineral sectors of the more-developed countries.

(b) Size

Another factor affecting the levels of investment is the difference in size of the domestic markets. The more-developed countries offer larger markets, thus reducing the diseconomies of scale associated with operations in the area.

(c) Infra-Structure and Development

Even if the problems of the small domestic markets in the less-developed countries can be overcome by the extension of national boundaries to include the whole Carifta/Caricom area, there remains the fundamental restrictions imposed by the underdeveloped state of the infrastructure of

the less-developed countries. While road systems are reported to be adequate for present demand and improved schemes are in operation, adequate port and airport facilities are lacking in these territories.

(d) Levels of Income and Savings

The lower levels of income in the less-developed countries serve as a further constraint on the size of the domestic market and the inadequate control of the financial sector aggravates the situation. Savings, mobilised in the less-developed countries, have been mainly through commercial banks and insurance companies, but in some of the less-developed countries these are in the main only branches.

The Pattern of Investment

In the absence of data on investment, the relative contribution to gross domestic product of the various sectors is taken as an indicator of relative investment.

Table 1 - SECTORAL CONTRIBUTION TO GROSS DOMESTIC PRODUCT AT CURRENT FACTOR COST FOR CARIFTA/CARICOM COUNTRIES (1967-1971 PERCENTAGES)

SECTORS	1967	1968	1969	1970[p]	1971[p]
1. Agriculture, Forestry & Fishing	12.4	11.6	10.9	10.1	10.4
2. Mining and Quarrying	17.1	16.1	16.5	16.0	14.6
3. Manufacturing	13.9	14.5	14.6	14.5	14.6
Sub-Total	43.3	42.2	42.1	40.6	39.6
4. Construction	7.6	8.7	8.8	9.0	9.1
5. Distribution & Transportation	19.4	19.8	19.5	20.7	20.6
6. Government	10.5	10.6	10.9	10.8	11.2
7. All Others	19.1	18.6	18.7	19.0	19.5
Sub-Total	56.6	57.7	57.9	58.9	59.7
TOTAL	100.0	100.0	100.0	100.0	100.0

SOURCE : Carifta Countries - Overview of Economic Activity 1972 - United Nations (ECLA).

While there was an apparent increase in investment in the construction industry, the available data suggest a decline in agriculture during the period 1967-1971. The downward trend in investment in agriculture is of particular significance since this is one of the sectors offering greatest employment opportunities in the region. In addition, its potential linkage with manufacturing increases the potential loss which will result from its neglect.

Although provision was made in the Carifta Agreement for the less-developed countries to be motivated to expand agriculture, apparently there were other militating factors, thus sufficient investment funds were not attracted to bring about the rate of growth expected. Domestic agriculture has thus stagnated in these territories, while imports have grown considerably.[1] One major reason for the lack of growth is probably the fact that taste in the region is heavily influenced by the demonstration effect of life in the metropolitan countries.

In the manufacturing sector, whatever dynamism exists has been concentrated in the more-developed countries which as a group provides over 95 per cent of the output. The present thrust in the sector is towards import-substitution and penetration of the whole regional market. However, the fact that the sector is heavily influenced by foreign capital and relies mainly on imported inputs results in the reduction of its contribution. The lack of sufficient export aggravates the situation as the full burden of the high import-content rests on the local economy. Thus, the value of investment in this sector of the economy is not maximised,

1. *The problem of lack of growth in agriculture and increasing imports is a circular one.*

either in terms of employment-generation or in export earnings. The problem becomes more acute when it is considered that the development of this sector was facilitated by generous incentives such as tax holidays, subsidies, protection and infrastructure provisions.

The shortcomings of foreign direct investment is even more marked in the mining sector, as from this sector the only benefits are wages and salaries to the extremely small proportion of the population employed, and revenue to the government in the form of taxes and royalties. At present efforts are being made to get more benefits from this most-important sector. The Guyana government, in 1971, acquired the bauxite company, DEMBA, and the Trinidad and Tobago government acquired the assets of British Petroleum Company in 1969, and also entered into partnership with various companies to explore and develop the oil resources on both land and sea. Since then further steps have been taken towards government participation in the petroleum industry in Trinidad and Tobago, the latest being the decision to acquire Shell (Trinidad) Limited, and the recent decision by the Jamaica government to obtain increased profits from bauxite.

Of the other sectors, dynamism in the construction industry represents basically much needed infrastructure development, particularly in the less-developed countries. This sector has the greatest social benefit in terms of employment and potential for economic development. The drive in construction in the less-developed countries resulted also from a conscious effort to develop tourism which normally has a potential linkage with the rest of the economy. However, tourist spending in the region has had a weak multiplier effect because of widespread foreign control of tourist

facilities and imports of food for tourist consumption; agriculture has therefore not benefitted from the growth of tourism.

It is clear that it is not only the volume of investment funds that is the constraint on the development of the region, but the pattern of investment also. The control and location of resources, the structure of production and the openness of the economies have combined to cause and maintain inequalities and imbalances both between territories and within each separate territory.

Table 2 - PROPORTION OF FOREIGN AND DOMESTIC FINANCING TO DOMESTIC INVESTMENT IN THE MORE DEVELOPED COUNTRIES: 1969-1972

	Percentages of Domestic Investment							
	Foreign Financing				Domestic Financing			
Country	1969	1970	1971	1972	1969	1970	1971	1972
Trinidad & Tobago	26.3	45.3	48.3	50.7	73.7	54.7	51.7	49.3
Guyana	16.6	35.0	10.4	18.9	83.4	65.0	89.6	81.1
Jamaica	39.8	46.7	47.1	56.1	60.2	53.5	52.9	43.9
Barbados	96.7	-	80.7	87.5	3.3	-	19.3	12.5

SOURCES : Central Banks' Annual Reports.
Eastern Caribbean Currency Board.

Financing of Domestic Investment - The Role of Foreign Investment

An analysis of investment financing in the more-developed countries, as shown in Table 2, suggests that there is a tendency among these countries to become more and more dependent on foreign capital inflows for their investment needs. Between the years 1969 and 1972, the proportion of foreign financing to total domestic investment has varied between 44.9 per cent (1969) and 53.3 per cent (1972). If Guyana, which has the lowest

proportional contribution from foreign sources (averaging 20.2 per cent for the period 1969-1972) is excluded, then the dimension of the problem would be readily recognised.

The combined averages of Trinidad and Tobago, Barbados and Jamaica ranged from 54.3 per cent (1969) to 64.7 per cent (1972). But the most noticeable case of foreign contributions to domestic investment is demonstrated in the case of Barbados where, during the period 1969-1972, the lowest proportion has been 80.7 per cent in 1971. During 1970, domestic financing in Barbados made no contribution to domestic investment; in fact, part of foreign capital inflows was used to finance consumption. This incident demonstrates the extent to which continued and increasing reliance on foreign funds can develop, to finance not only investment but also consumption needs.

There is considerable debate, particularly among developing countries, on the importance of foreign capital to finance the development needs of these economies. Essentially, the arguments supporting foreign capital inflows have been centred on the fact that these economies are generally short of investment funds and that domestic savings are insufficient to finance the volume of investment required for rapid development. The limited domestic financial resources, the argument emphasises, must be supplemented by foreign capital inflows to keep pace with the required rate of economic development. It has also been argued that foreign capital is accompanied by improved technology, foreign markets providing opportunities to earn foreign exchange, the training of locals and increased income to the economy in the form of wages, salaries and government revenue.

These arguments, however, have been based on the fallacious premise that there is a direct relationship between imported foreign investment and technology, and economic development. Unless the introduction of foreign technology is accompanied by safeguards for integrating it into the economy the benefits may never reach further than the operational stage.[1] In the absence of such integration, the net result of the incentives to foreign investment will be similar to the simple purchase of packaged components for assembling. In the long-run, the economy may be subject to net losses.

The bulk of private foreign investment in the region has been direct foreign investment. An examination of the situation in Jamaica reflects a situation characteristic of the economies of the region.

The average proportion of direct investment to total foreign private investment during the period 1967-1971 has been 87.3 per cent.

Table 3 - DIRECT INVESTMENT AS A PERCENTAGE OF TOTAL FOREIGN PRIVATE CAPITAL - JAMAICA (1967-1971)

1967	1968	1969	1970	1971
74.4	89.6	92.1	91.5	89.0

SOURCE - Central Bank of Jamaica. Annual Reports.

The agency through which such investment funds flow is usually the multinational corporation, a 20th century creation, arising from the complexities of international economic competition. The main feature of this institution is that as a private economic unit, internationally organised, its primary objective is to maximise profits internationally. A branch plant is

1. *For foreign technology to benefit the country in the long-run the nationals should be able to use the knowledge gained from that technology as the basis for development in other areas.*

established in a specific sector of the local economy, and given the sale of the operation may eventually assume dominance of that sector. By carving out a sector of the economy, the local branch through its direct integration with head office (and not with the rest of the economy) conducts its activities in a manner which is consistent with general company policy, and not necessarily with the local economic policy.

The Role of Domestic Savings

The foregoing analysis suggests that domestic savings should assume a more significant role in domestic investment in the region if long-term development is to be achieved. The bulk of domestic savings in the region is mobilised by commercial banks and insurance companies. It is useful, therefore, to examine the extent to which these institutions have allocated the financial resources at their disposal to sectors which are potentially income-generating or resource-activating.

Insurance companies by the very nature of their operations have at their disposal long-term funds which make possible long-term investment transactions. Because of the underdeveloped state of the capital market in the region, however, opportunities for share-trading are minimal and where no legislation exists such as in the less-developed countries there have been outflows. In the main, insurance companies have channelled their funds into mortgages, equities, government securities (particularly bonds and treasury bills) and policy loans.

An examination of the structure of loans and advances by the commercial banks in the region suggests that these institutions have made no attempt to adjust their lending patterns to meet the needs and priorities of the local economies.

The following tables show the average sectoral distribution of loans.

Table 5 - AVERAGE SECTORAL DISTRIBUTION OF LOANS AND ADVANCES BY COMMERCIAL BANKS IN THE MORE DEVELOPED COUNTRIES - PERCENTAGE OF TOTAL CREDIT: 1968-1972

	1968	1969	1970	1971	1972[e]
Manufacturing	18.2	18.4	19.3	18.0	18.8
Mining	1.3	2.1	1.8	2.8	1.7
Agriculture	7.9	5.5	5.3	5.3	5.7
Construction	6.9	7.7	8.7	9.4	9.3
Distribution	29.3	24.3	23.6	22.2	22.8
Tourism	2.8	5.5	4.5	4.4	3.8
Personal	20.3	21.8	18.9	21.2	22.9

e - estimate.

SOURCES : Central Banks' Annual Reports.
Eastern Caribbean Currency Board.

Table 6 - AVERAGE SECTORAL DISTRIBUTION OF LOANS AND ADVANCES BY COMMERCIAL BANKS IN THE LESS DEVELOPED COUNTRIES - PERCENTAGE OF TOTAL CREDIT: 1971-1972

	1971	1972
Manufacturing	7.0	7.6
Mining	-	-
Agriculture	7.5	6.4
Construction	10.0	10.0
Distribution	19.5	20.3
Tourism	11.0	11.6
Personal	23.5	23.6
Others	21.8	21.8

SOURCE : Commonwealth Caribbean Financial Statistics: Quarterly Digest, ISER publication, December 1972.

The above tables reveal that throughout the region personal loans and credit to the distribution sector together account for approximately 45 per cent of total credit granted by commercial banks. This characteristic of bank credit substantiates the view that commercial banks regard themselves as specialists in the provision of short-term credit, and is also consistent with the banks' traditional criteria for lending -- liquidity and safety.

A sizeable proportion of personal loans is used to finance the purchase of imported consumer durables, which has the net effect of creating further leakages from the economies and imposing an additional burden on the relatively scarce foreign exchange available to these countries.

Throughout the region, loans and advances for agricultural purposes have remained relatively insignificant, in fact, such loans absorbed a decreasing share of total credit. In the more-developed countries, for example, the aggregate share fell from 7.9 per cent in 1968, to 5.3 per cent in 1970 and 1971, with an estimated share of 5.7 per cent for 1972. A similar trend is illustrated in the case of the less-developed countries where the share of total loans received by the agricultural sector fell from 7.5 per cent in 1971, to 6.4 per cent in 1972.

The construction sector which like agriculture is a labour-intensive activity which provides scope for the utilisation if indigenous resources, has however, been receiving an increasing share of loans and advances in the more developed countries during the period 1968-1971. But with the exception of Jamaica and Barbados where construction accounted for 16.1 per cent and 14.3 per cent respectively in 1972, its share of total loans has been relatively low.

While within recent times specialised institutions have been established in the region to provide medium and long-term development finance in certain areas, there are still institutional gaps.

The analysis of the investment pattern indicates that the lack of control of the use of resources and the concentration on primary activity in the economies have resulted in less than optimum benefits

from the use of funds. In addition, there has apparently been a reinforcement of patterns of imbalances between the individual territories as well as between sectors in the economies.

The problem, therefore, calls for an approach to investment which would bring about:-

(i) an increase in total investment in the region;

(ii) greater mobilisation of savings in the region;

(iii) a greater dependence on domestic investment;

(iv) a more optimal distribution of investment within the region and between sectors; and

(v) increased benefits from foreign investment.

CARIFTA/CARICOM - An analysis of the effectiveness of this institution as an instrument for economic transformation

Regional integration movements are motivated by the expectation of a general improvement in economic conditions. The type of improvement and the rate at which it will be brought about will depend upon the type of economies which are to form the Regional Community, the goals set and the provisions made for achieving such goals.

The countries which formed the CARIFTA region had economies which could be described as competitive. Consequently the volume of trade between them was small.

Prior to the establishment of CARIFTA, trade patterns reflected the traditional types associated with developing countries. Trade with the metropolitan countries accounted for approximately 90 per cent of exports and these were - petroleum and petroleum products - 40 per cent, bauxite, including alumina - 16 per cent, sugar - 20 per cent, bananas - 4 per cent and a number of other items making up the balance of 20 per cent.

An examination of the pattern of production in the major industries shows that only a small proportion of the potential earning power actually accrued to the local economies. In the case of petroleum and petroleum products which are exported by Trinidad and Tobago, approximately 65 per cent of the value of exports came under the processing agreement arrangement. The returns from this portion being mainly processing fees.

In the case of bauxite and alumina, the limiting of processing to the alumina stage meant substantial losses in earning power. Up to 1967, seventy-six per cent of bauxite output was exported as dried ore. When it is considered that one ton of alumina has a value of four times a ton of crude ore, and one ton of aluminium in turn values seven times a ton of alumina, the problem is seen in its true perspective.

Sugar production for export is operated mainly under quotas and agreements. The United States Sugar Act sets quotas and certain conditions governing prices, and the Commonwealth Sugar Agreement sets prices as well as quotas for the region.

With the major exports so constrained, the countries of the region were actually handicapped to the extent of 72 per cent of their exports.

The justification for limiting production to the raw material stage is sometimes made on the comparative advantage argument. The argument is fallacious as a number of factors are ignored, including the "learning factor". Some of the factors which actually militated against the movement from raw material production to "end production" have been tariff barriers. In the case of aluminium production for example, exports to the United States would have to face tariffs of 4 per cent, while the European Community has a 7 per cent tariff.

Trade among the Carifta countries averaged 6 per cent of total trade in the period 1960 - 1967. The main items traded being rice and manufactures such as petroleum products, fertilizers, wood and cement. The items which later came under the Agricultural Marketing Protocol made up less than 4 per cent of total trade, while petroleum and rice together accounted for

58 per cent of trade. Copra, wood, medicines, cosmetics, fertilizers and cement together comprised 20 per cent. The rest of trade consisted of other light manufactures which had very small trading values; individual sections did not exceed $4,000.

Realising that as individual states all the limitations of their smallness would continue to weigh against them, the Caribbean governments agreed to establish Carifta. This was put into effect on May 1, 1968, with four participants. The seven others acceded to the agreement in August, and in 1971, the twelfth participant acceded.

The Agreement attempted to free all trade immediately by providing for the complete removal of all barriers to intra-regional trade, except in the case of a small number of commodities which can be placed into two main categories:-

(a) those which were placed on a Reserve List and which could produce serious dislocations of production if barriers are suddenly removed;

(b) those for which there should be elimination of the protection element in import duty.

In both cases, the reduction of duties would be effected over five-year to ten-year periods -- five years for the more developed countries and ten years for the less developed countries.

The Agreement prohibited the operation of quantitative restrictions among Carifta countries, whether they take the form of restrictions on imports or on exports. Exceptions were to be made only for the Agricultural Marketing Protocol, or because of balance of payments difficulties, or serious dislocations in domestic production and employment.

Individual territories were to maintain their own levels of duties against third countries. Generally, stand-still provisions were to operate with regard to incentives to industry in each territory.

The essence of the Agricultural Marketing Protocol is that member countries should take up available supplies of agricultural products before importing from outside sources. It was operated in such a way as to provide markets for the products of the less developed countries.

The less developed countries were permitted to accelerate the removal of tariffs among themselves, while maintaining those against the more developed countries. The Agreement also contained procedures to be adopted for the harmonisation of incentives, which should be so devised as to include special arrangements to stimulate the location of industries in the less developed countries.

The Agreement recognised the fact that prior to May 1968, regional governments made contractual agreements with third parties, extending protection to particular products in the particular markets. Such arrangements were to be registered with the Carifta Secretariat and excluded from the trade liberation measures in the first instance.

The emphasis of Carifta, therefore, was on trade liberalisation with certain provisions designed to protect the interest of the less developed countries.

An examination of the trade data shows that there has been some growth in intra-regional trade. Between 1967 and 1971, total intra-regional imports rose from E.C.$95 million to an estimated E.C.$193 million, representing an average annual increase of 19 per cent, compared with an average annual increase of 6 per cent between 1960 and 1967.

This trade liberalization, however, was more in favour of the MDC's than the LDC's. Between 1967 and 1970, the total CARIFTA trade increased by 67 per cent with the MDC's share of the total increasing from 67 per cent to 69 per cent - continuing to be more than twice the share of the LDC's. In addition the LDC's share of the increased trade remained heavily biased towards imports. Over the period their imports increased by 55 per cent while exports increased by only 19 per cent. Their ratio of imports to exports in 1970 was 6:1, compared with 4:1 in 1967. Even with the gradual phasing out of barriers, the LDC's having a longer period of phase out than the MDC's, the gap in regional trade shares within CARIFTA increased substantially.

Data on intra-regional payments show the same trend with receipts of the MDC's far outweighing payments.

It is this trend which has given rise to grumblings in some quarters on the issue of benefits and costs of regional integration. As stated earlier, increased trade earnings for the MDC's was the logical development of the mere freeing of trade.

This situation is not unique to CARIFTA, however; it has been recognised in other areas of economic integration for example, in the European Economic Community a similar problem existed. The president of the Commission in commenting on the situation, point out:

> "We cannot prevent the private benefits resulting from the Common Market from being distributed unequally. If we tried to prevent this, we should be making it impossible for the EEC to achieve its social and economic, as well as politicel goal."[1]

In the East African Community a similar problem almost brought about disaster and the complete collapse of the Community between 1965 and 1966. They averted the disaster and attempted to solve the basic problem by the Treaty for East African Co-operation in 1967[2]. In this treaty one of the most important provisions was the setting up of an Economic Consultative and Planning Council; something in the nature of a supra-planning Ministry.

1. *Sidney Dell, Trade Blocs and Common Markets - pp.176-177.* Constable and Company Limited, 1963.

2. *For details, see pp. 40-45*

The problem of distribution of benefits assumes even greater proportions when the reason for the integration is viewed in terms of trade benefits. The disparities which usually exist among developing countries make it inevitable that trade benefits will tend to be biased in favour of the more developed countries. In the CARIFTA/CARICOM area for example, the countries entered free trade with Jamaica's gross domestic product at over nine times that of Barbados, and over eight times that of the Eastern Caribbean taken as a group. Jamaica and Trinidad and Tobago together accounted for over 80 per cent of total area Gross Domestic Product (excluding Belize). If Guyana is included with these two, then together they accounted for 90 per cent of the total. In addition these three areas were responsible for the bulk of industrial activity in the area, together they accounted for close to 100 per cent of the gross product generated through mining in the area, and 95 per cent of that through manufacturing. Even in agriculture which is the main economic activity in the LDC', Guyana, Jamaica and Trinidad and Tobago accounted for 79 per cent of area agricultural products. It seems therefore, that short of bringing economic activity in the MDC's almost to a halt, there was no way of preventing them capturing the bulk of the new trade and direct gains from it, given their wider and more developed export bases.

The prospect for small countries outside some regional community, however, does not seem bright; world trade and development do not favour developing countries, least of all small developing countries. In addition, the smallness of the markets in developing economies renders them inadequate as individual economies to absorb levels of investment and technology to a sufficient extent to effect diversification and transformation. It seems, therefore, that in spite of the problems of regional integration, it is the only answer.

Regional integration looked at from the point of view of accelerated development presents a different picture. In fact the most important consideration of the Carifta region is the path of investment with the goal of accelerated development. As Dell[1] points out:

> "The main purpose of a common market for a group of underdeveloped countries is to promote the transformation of the economy through industrial development. Instead of seeking to establish protection for each country individually, the idea is to introduce infant industry protection on a regional basis, so as to take advantage of economies of scale and specialisation."

This observation certainly emphasises the need for a regional planning body.[2]

An analysis of the contribution of Carifta to the transformation of the total economy leads us to an evaluation of the extent to which trade created induced industrial integration and specialisation.

1. *Sidney Dell. Op cit.*
2. *See details on East African Community, page 45, and suggestions for Caricom, page*

A look at sectorial contributions to area gross domestic product, suggests that within the first three years of Carifta (1968 - 1971) some degree of sectoral shift occurred. Agriculture declined in importance from 12.4 per cent of gross domestic product to 10.0 per cent, while manufacturing increased from 13.9 per cent to 15.2 per cent. There were increases also in the contributions of construction, transport and distributive trades, and government. For the individual countries, the pattern was similar; declines in the importance of agriculture were registered in all countries, being as high as 13.6 percentage points in Barbados and 5.3 percentage points in the Eastern Caribbean group. Except in Guyana and Jamaica where the bulk of resources released were apparently absorbed in mining, rechannelling seemed to have been into manufacturing.

It is recognised that a three-year period and a simple analysis do not provide conclusive evidence to allow the establishment of a casual relationship between the movements observed and the liberalisation of trade. Nevertheless, it does suggest that there was some structural transformation within the region.

Apart from trade liberalisation, factors which would have influenced investment were those relating to the petroleum industry in Trinidad,[1] and climatic conditions as well as world demand factors relating to agriculture. In the case of the petroleum industry, intra-regional trade

1. *Trinidad and Tobago saw a marked decline in on-land drilling and crude production during this period. Proved on-land oil reserves were declining. By the end of 1972, however, this trend was reversed with increased offshore drilling and funds.*

has very little influence on mining activity since intra-regional trade in petroleum and petroleum products constitutes only a small proportion of total output. With agriculture, droughts, bilateral agreements with the metropolitan countries, and general world demand affect the more-important agricultural products to a large extent.

It has been shown that there was a substantial increase in manufacturing activity in the region as a whole. Again, any discussion on the distribution element of integration brings into focus the tendency for the more-developed countries to receive greater benefits. Up to 1971, the bulk of manufacturing activity and generated investment continued to be located in the more-developed countries, which together accounted for over 90 per cent of manufacturing output. In terms of the flow of induced investment into industrial activity, regional integration poses the problem of how to integrate industrial activity within the region and at the same time ensure the emergence of a modern industrial sector in the slower-growing areas.

In relation to market forces, the two aims are opposed to each other. With the liberalisation of trade, the inducement of industrial integration and specialisation is automatic. The search for greater profitability, however, tends to lead investors to the more-developed areas where facilities of infra-structure and market size are more favourable.

INSTITUTIONAL DEVELOPMENTS WITHIN CARIFTA/CARICOM
AIMED AT EFFECTING A RECHANNELLING OF INVESTMENT

Realising that the pace of the less developed countries' industrial development was severely limited by the existing inadequate infra-structure, i.e. roads, ports, factory shells, banks, agricultural stations, the Caribbean governments established the Caribbean Development Bank with the express purpose of providing credit facilities to aid in the development of the necessary infra-structure, particularly in the LDC's.

In the agreement establishing the Caribbean Development Bank, its main purpose was described as being "to contribute to the harmonious economic growth and development of the member countries in the Caribbean and to assist economic co-operation and integration among them, having special and urgent regard to the needs of the less-developed members of the region".

In formulating the lending policies of the Caribbean Development Bank, priority was given to investments in agriculture, livestocks, fisheries, manufacture, mining, tourism, transportation and the infra-structure related to the development of these sectors of the economy.

However, in the period 1970-1973, the Caribbean Development Bank failed to disburse the necessary funds (in sufficient quantity) to facilitate the kind of structural transformation in the economies of the less-developed countries that would attract small and medium-size industries. Out of a total loan commitment of US $44.2 million in the period 1971-1973, the bank disbursed only US $2.3 million which represented 5.0 per cent of total loan commitment. It was gratifying to note that all disbursements made as at December 31, 1973 were in respect of loans to the less-developed territories and represented some 40 per cent of the value of loan agreements. Of the total loan commitment to the LDC's, however, only 7.0 per cent has been disbursed.

Loan Commitment and Disbursement
[US $M.]

(1) Year	(2) No. of Loans	(3) Loan Commitment	(4) Disbursement	4 as % of 3
1971	21	$ 7.2	NIL	
1972	35	$16.8	$0.5m.	3.0
1973	54	$20.2	$1.8m.	8.9
Total:	110	$44.2	$2.3m.	5.2

SOURCE: Caribbean Development Bank: Annual Report for years, 1971, 1972 and 1973.

Total Loan Commitment of Bank
As at December 31, 1973

Ordinary Capital Resources (excluding Guarantee)	$22.4m.
Special Development Fund	$19.5m.
Agricultural Fund	$ 2.3m.

SOURCE; Caribbean Development Bank: Annual Report, 1973.

Throughout the period of 1971-1973, the Bank concentrated its loan commitment in such priority sectors as agriculture, marketing, livestock and processing in keeping with its function to give the less developed territories special consideration.

However, in the area of manufacturing the disbursement by the Bank was not very satisfactory. In its annual report of 1972, the Bank pointed out that its lending performance in this sector was severaly limited due to a lack of information on worth-while industrial projects which would warrant the kind of investment the Bank was prepared to undertake. As a result, the Bank failed to make any loan directly to a manufacturing firm in 1972. Neither did it take any initiative to promote such enterprises because it was waiting on the report of the Economic Intelligence Unit on industries suitable for establishment in the less developed territories. The Bank received this commissioned report only in September 1973.

To understand why the Caribbean Development Bank has not been more venturesome in its operations, one must refer to the Charter setting up this institution, specifically Articles 13 and 15.

Article 13 for example prohibits the Bank from investing in equity capital which is so badly needed by fledgling enterprises while Article 15 binds the Bank to invest in projects which are self-liquidating.

Unlike its counterparts as the World Bank and development banks in Latin America, Asia and Africa, the Caribbean Development Bank is bound by its Charter to lend to private enterprises without Government guarantees. This means that the institution is liable to suffer heavier losses from defaults and must carry larger reserves which in turn have to come from earning a higher profit ratio.

With such constraints, the Bank must adopt an extremely cautious approach in its lending policy, e.g. it will not participate unless a project when evaluated shows that it could yield economic benefits substantially in excess of costs when account is also taken of indirect benefits including cost savings and the employment of resources which would otherwise be underutilised. As a result, one finds that during 1972, the Bank did not extend a loan for a manufacturing project and was only able to analyse four (4) manufacturing projects for which loan applications were made during 1973.

In its 1972 and 1973 Annual Reports, the Bank was able to highlight several financial problems connected with development in manufacturing and processing sectors. They were:-

(i) the inability of applicants for direct loans in the manufacturing sector to provide adequate securities;

(ii) the lack of entrepreneurs and entrepreneurial skills in the less-developed countries;

(iii) most of the less-developed countries had no reserves and were not even balancing their recurrent budgets, which means that it would be extremely embarrassing to call on them to honour their guarantee if the need arises;

(iv) the lack of proper agencies and skilled administrative staff in the less-developed countries to administer loans efficiently; and

(v) public enterprises in the less-developed territories were very badlyrun and were in dire need of the financial and administrative expertise which every bank loan brings with it.

Consequently, the Caribbean Development Bank concentrated its lending to territorial development corporations for lending to small industries, and the building of workshops for leasing to small businesses. It has also given loans to build industrial estates for leasing at subsidised rents, e.g. St. Lucia in December 1972.

It should be noted that fledgling enterprises experience considerable difficulties in raising equity and security for loan capital at the same time. And, in the absence of a developed share market (Call Exchange or Stock Exchange) selling of shares of an untried business enterprise could be an insurmountable problem in the less-developed countries. The equity constraint on the Bank, therefore, has been one of the main reasons why it has been unable to get many projects off the ground once they were identified.[1]

The Caribbean Development Bank is a Bank of last resort [Article 15(d) and therefore must not lend money for purposes for which money could be obtained from other sources. Therefore, it does not lend money for working capital, since it believes that the commercial banks can perform this function adequately. Its speciality is long-term lending with favourable periods of amortisation.

The Bank must at all times act in accordance with "sound development banking principles" and therefore has a long list of requirements which the borrower must comply with before he is eligible for a loan, e.g. to borrow for a development project the borrower must establish beyond doubt that the proceeds will be used to raise the National Income, whether by increasing the use of fixed capital or by introducing new technology, and should the proposal fail to meet the least of these requirements it is not eligible. The authorities in the less-developed countries (development banks and the Industrial Development Corporation) now realise that an investment proposal will not be eligible unless, when direct and indirect benefits and costs are all included, it will yield at least 9.0 per cent, since capital is scarce in the less-developed countries.

[1] See page 23.

Consequently, we find that lending by the Caribbean Bank for agriculture has been confined to projects involving additional fixed capital or new technology and not to any agricultural projects which merely expands the area under cultivation without involving new methods that will raise productivity. And, since most farmers in the less-developed countries are not skilled in new technology, it is left to the technical staff of the Caribbean Development Bank to make detailed farm plans which is time-consuming and costly.

Has the Caribbean Development Bank Failed and is there a need for the Caribbean Investment Corporation?

Recognising the obvious limitations of the Caribbean Development Bank in facilitating the rapid economic transformation of the less-developed countries economies, the regional governments moved in April 1973 (between the 9th and 12th at the signing of the Chaguaramas Agreement) to further deepen and widen the integration process in the region by setting up the Caribbean Investment Corporation (on June 1, 1973). The Corporation is expected to take the initiative in industrial development in the less-developed countries. However, when one examines the operating principles of the Corporation, there appears to be some striking similarities to those of the Caribbean Development Bank which makes one wonder whether the Corporation would do the job better than the Caribbean Development Bank. For example, Article 11 (ii) of the Charter of the Corporation states "in the performance of its functions the Corporation shall invest in projects which are financially viable; due regards being paid to two other important criteria;

(a) the ability of the projects in which it invests to promote further industrial and economic development in the economy of the less-developed countries concerned; and

(b) the creation of employment opportunities in the less-developed countries concerned.

This implies that the Caribbean Investment Corporation[1] would have to duplicate a lot of the work already done by The Caribbean Development Bank and undertake time-consuming feasibility study to ascertain that any investment undertaken in the less-developed countries will meet these requirements.

The Caribbean Investment Corporation has an authorised share capital of E.C. $15.0 million but only E.C. $5 million worth of shares were to be issued in the first five years of the Corporation's operation.

The issued share capital of the Corporation is to be distributed between the public sector - 60 per cent and the private sector - 40 per cent. The authorised capital stock of the Corporation will be divided into 150,000 shares with a par value of E.C. $100 each and will be available for subscription by members in accordance with the provisions of Article 6 of the Agreement.

Conceptually, the proposed participation by the Corporation in the establishment of viable industries in the less-developed countries implies that there already exist capital markets in the area of the Common Market.

Actually, facilities for share trading exist only in Trinidad and Tobago and Jamaica, and with foreign banks going local in the former it seems that market for funds would be extremely tight there. This suggests that the Corporation hoped to raise most of its equity capital in the less developed countries which would require the setting up of a Call Exchange in that area of the Common Market for the marketing of shares. Such action would increase the time lag between actually identifying projects, raising of capital and effecting such industrial development. It seems however that this function could very well be performed by the Caribbean Development Bank if the regional heads of government decide to change Article 13 of its Charter. The Caribbean Investment Corporation might be very necessary when one analyses the present situation in the less-developed countries, but one wonders whether it could actually effect the industrial development it has been created for in a shorter time than the Caribbean Development Bank.

1 For more detail study of the Charter of the Caribbean Investment Corporation, refer to the Agreement establishing the Corporation (a Community Secretariat publication) on the Chaguaramas Agreement, April 9-12, 1973.

Other Alternatives - Special Fund

At the meeting of the Board of Governors of the Caribbean Development Bank in Grenada (May 1973), the Minister of Finance (Trinidad and Tobago) proposed that a "Special Fund within the Caribbean Development Bank" be set up which should be used to assist the less-developed states.. His proposal is that the Fund should be operated by the Caribbean Development Bank with minimum of restrictions which implies that the Caribbean Development Bank should ease considerably its long list of requirements. The Caribbean Development Bank, it is proposed, should take the initiative in making overtures to friendly countries who were interested in assisting Caribbean development. In the meantime, the Trinidad and Tobago Government reiterated on May 10, 1974, its willingness to make a substantial contribution to the Fund.

Although there is so very little information on the mechanics of this proposed Special Fund, the general concensus seems to be to use it for two purposes, namely:-

(i) to give development programme loans to the less developed states on a concessional basis; and

(ii) to permit the less-developed states to borrow from the Fund whatever counterpart funds are needed to meet criteria set down for the Caribbean Development Bank.

The Minister of Finance of the Trinidad and Tobago Government suggested at that meeting that on-going projects should be given priority, i.e. those projects not yet started as well as new projects, should qualify for support from the Special Fund.

Such actions, the Trinidad and Tobago Minister of Finance stated, should serve to remove the log jam on the execution of several projects, currently approved but which have not yet got off the ground because of the lack of the required "counterpart funds". In this way, the Minister, went on, the less

developed states would be able to make more obvious use of the Caribbean Development Bank's resources and finance their general development efforts. The ultimate aim of the scheme is to develop additional soft funds of a different nature in the Caribbean Development Bank for lending to the less developed states to assist them to partially maintain their import capacity for goods from more developed countries and accelerate their development.

The present initiatives to find a way to utilise the Caribbean Development Bank's resources could be commended if other steps were taken to change the Charter of the Bank to make it the main vehicle to rechannel investment in the region. Unfortunately, no such actions have been taken which leaves one with the impression that the Special Fund is short-term in nature and would be totally dependent for its supply of money on state governments presumably with comportable budget surpluses, e.g. Trinidad and Tobago and Venezuela which seem to have a special interest in the development of the less-developed states.

What continues to be left unanswered in these moves is the ability of the less-developed countries to finance such development when the Caribbean Development Bank has repeatedly cited cases of some less-developed countries being unable to even balance their recurrent budgets let alone build up required reserves to service these loans.

What is also left unanswered is whether the regional heads of government are willing to allow the less-developed countries to run substantial budget deficits to effect the industrial and infra-structural development in their economies, and whether to finance such deficits these governments are prepared to give substantial grants-in-aid to the less-developed countries.

SOME EXPERIENCES IN OTHER AREAS

We turn now to an evaluation of practical attempts at affecting the rechannelling of investment in three areas of regional integration among developing economies - Latin America, Central America and Africa.

Latin America Free Trade Area

The disparity in levels of economic development among the members of the Latin American Free Trade Area is marked to a point where three distinct sub-divisions can be observed in Argentina, Brazil and Mexico, relatively industrial giants; a middle group of Chile, Columbia and Venezuela; and Bolivia, Ecuador and Paraguay at the lowest level of development. There is no doubt that the source of the major problem faced by LAFTA, rests in this fact - involving the economic relations among these three sub-groups within the region. The two lesser groups claimed with some validity that their benefits from integration were minimal and in essence were becoming more and more just outlets for the "industrial surplus of the big three, subsidizing their production and further industrial development."

The Treaty of Montevideo which brought LAFTA into being in 1960 concerned itself mainly with a system of gradual removal of tariff barriers within the area. It was much less specific in relation to non-commercial co-operation, making a fleeting commitment to "pool their efforts to achieve the progressive complementority and integration of their economies on the basis of an effective reprocity of benefits."

In specific relation to the plight of the lesser developed areas the Treaty identified five basic policy proposals:-

1. Within the general preferential system, the LDC's were

allowed to receive special concessions from other members in order to "encourage the introduction or expansion of specific productive activities".

2. The removal of intra-regional trade restrictions was given a longer phase out period than for the more developed areas.

3. They were allowed to take steps to correct unfavourable balance of payments beyond the limitations of such policies set down for the general membership.

4. The LDC's were allowed, in areas of production that are of vital importance to their economic development, to maintain or apply non-discriminatory measures to protect their domestic production.

5. Commitment was made for regional arrangements to obtain assistance for the LDC's (financial and technical) from both internal and external sources, to stimulate their industrial development.

The Treaty made provisions for two regional institutions to cordinate the integration process - the Conference of Contracting Parties which constituted the supreme organ and the Standing Executive Committee to give ongoing supervision of the implementation of the Treaty provisions.

The Standing Executive Committee, however, concerned itself only with what from the outset was highlighted as the key factor in integration - trade commitments - the liberalization of intra-regional trade. The Committee was

never given the political authority to make the necessary decisions to implement the non-commercial commitments of the Treaty. The recognition of this failure led to the abortive attempt to set up institutions ataa higher level of authority - the Council of Ministers and the Conference of American Presidents whose call for a Common Market was put aside. The fundamental problem that any attempts to establish such institutions faced was the inability to chip off the strong nationalist outlook that saddled the integration process from its very outset. For example, development of intra-regional trade hinged upon Latin American suppliers being able to meet competitive prices from third countries - a position that contributed to the cease in growth of intra-regional trade after only seven years of LAFTA's existence, at the same time that trade with the rest of the world showed substantial increases. Further it was clear that the more developed areas placed priority on their domestic interests and objectives over regional co-operation. The fact is that given their already high levels of development, their trade with other LAFTA countries was too small a proportion of their total trade to encourage their desire to participate fully in arrangements where they will necessarily have to give unilateral concessions to the lesser developed areas. It is precisely the failure of these more developed areas to subject national interests in favour of co-ordinated regional development that led to disintegration of relationships to the point where the lesser developed areas formed an Andean common market within LAFTA (Columbia, Ecuador, Peru, Bolivia, Chile and Venezuela participating in the setting up deliberations), with the intention of moving much further and faster along the road to integration than LAFTA was prepared to go. An Andean Development Corporation was set up to carry out joint development projects.

The experiences of LAFTA demonstrates, that whereas regional trade liberalization with a special system of incentives to direct both foreign and local investment to the lesser developed countries is a necessary condition for proper and more equally shared regional development it is not a sufficient one. What is clearly lacking is a direct attempt to "promote investment and technical assistance, specifically designed to correct existing and future disparities." As discussed before, this necessitates the kind of regional institution that is politically capable of deciding upon and implementing the necessary measures.

In comparing Latin American integration with the European Common Market which grew out of attempts to overcome political nationalism, the Economist Intelligence Unit in its Quarterly Economic Review publication, stated that "The Latin American Common Market may be still born because the economic logic of such a welding cannot prevail against political nationalism."[1]

Central American Common Market

Even prior to the formal establishment of the Central American Common Market (General Treaty at Managua, 1960), regional co-operation was at a high level. From as early as 1951 the Central American Committee for Economic Co-operation was established to study and direct the movement towards regional integration. CACM stands unique among integration programmes in having such an extensive period of preparation. For close to a decade after its establishment the Committee concerned itself with the preparation and elaboration of - patterns of co-operation in compartmentalized areas

1. *The Economist Intelligence Unit, Q.E.R. Special No. 1 - The Crisis in Latin American Integration, London, 1968.*

cf issue. In addition to intra-regional free trade and a common external tariff the committee considered other areas of co-operation, e.g., integration of industrial development; agriculture, livestock and fisheries as a special area of concern; development of regional infrastructure; the social aspects, including the effect of regional free trade on government revenues.[1]

Out of the Committee's work evolved a series of treaties designed to integrate development in specific areas. The first of these a Multilateral Treaty on Free Trade provided for the immediate removal of all restrictions on intra-regional trade of about two hundred commodities and for further agreements to add new commodities and establish a common external tariff with the aim of achieving customs union status within ten years. The important aspect of this treaty however, was that the commodities cited were commodities not yet being produced within the region. In other words, unlike the Treaty of Montevideo (LAFTA) the aim from the outstart was to encourage the development of new rather than competition among existing industries, to the products of which was applied a more gradual liberalization process.

The second of these treaties signed was the Agreement on the Regime for Central American integration industries with the specific objectives to set up what was called integration industries[2] in order to "encourage and promote the establishment of new industries and the specialization and expansion of existing industries within the framework of Central American

1. *See Dell, A Latin American Common Market. p.52.*

2. *Integration industries are defined as those whose minimum scale for efficient operation requires the wider regional market.*

economic integration and -- on a reciprocal and equitable basis in order that each and every Central American State may progressively derive economic advantages".[1] The Treaty laid out the criteria and conditions under which such industries can be set up, but more importantly it provided for direct intervention in the locational distribution of these new industries to the point where the agreement states -- "In order to promote an equitable distribution of the Central American Industrial integration plants, the contracting countries states shall not award a second plant to any one country until all of the five Central American countries have each been assigned a plant --"[2]

By 1959 a third agreement had come into being, the Central American Agreement on the Equalization of Import Duties and charges that laid the basis for setting up a regional import tariff and the equalization of import duties and charges within five years.

It is in the background of development of these specific areas of co-operation that the General Treaty of 1960 finally established the Central American Common Market. The General Treaty ratified the existing areas of agreement and set up the necessary regional institutions to make regional integration a reality. An Economic Council, made up of Ministers of Economic Affairs was set up, to supervise the integration of the economies and co-ordinate the different economic policies; the application and administration of the Treaty proposals was put in the hands of a representative Executive Council and a Secretariat was established on appointment by the Economic Council. By far the most important regional institution set up by

1. *Agreement on the Regime for Central American Integration Industries - Article 1, Agreement appendixed to Dell, A Latin American Common Market p.270.*
2. *Agreement on the Regime for Central American Integration Industries - Transitional Article, Appendixed to Dell, A Latin American Common Market - p.275.*

the Treaty was the Central American Bank for Economic Integration designed to function "as an instrument for the financing and promotion of a regionally balanced integrated economic growth". Built into the Bank's charter is the recognition that industrial integration produced and at the same time depended upon "increases in exchanges of persons, goods, services, correspondence, communications, and energy", and that the main problem of industrial development, especially in the lesser developed areas, was the lack of proper infrastructural development which is a pre-requisite to the inducement of private investment. Although a great deal of its funds has gone into support of industrial projects its main objective is the financing of infrastructure development. Within nine years of the Bank's operation disbursements had totalled $150 million, fifty per cent of which had gone to the lesser developed areas of Honduras and Nicaragua.

The important basic features of the Central American Bank is that the wideness of its charter not only enabled it to promote infrastructure development, but also by its involvement in industrial activity to keep in close touch with and generate further activities of private enterprise. Further it is able to keep in tune with the operations of the monetary sectors of each of the member countries - its Board of Governors included at the Presidents of the Central Banks of the five countries. Its ability to generate a wide range of funds further induced the will of the members to integrate.

There is no doubt that the programme has generated strides in the economic performance of the area. By 1964 industrial production contributed 15 per cent of gross domestic product as compared with 9 per cent in 1950.[1]

1. *Phillipe C. Schmitter, Central American Integration: Spill-Over, Spill-Around or Encapsulation? in Journal of Common Market Studies, Sept. 1970. IX, No. 1. p.14.*

Greater strides were seen in the growth of intra-regional trade. By 1964 such trade had grown to $95 million constituting over 14 per cent of total trade as compared with $8.3 million in 1950 - 3 per cent of total. Between 1956 and 1964, the average annual rate of growth of intra-regional trade was over 25 per cent.[1]

Developments in the location of "integration industries" have been much slower for basically two reasons:

(1) the reluctance of both national and international lending agencies (specifically of the United States) to support the programme on the basis that the conscious interference with the market forces will produce less than optimum location of industry, that it would encourage monopoly and discourage small industries geared towards local markets.

(2) inability to find the proper trade off between political and economic consideration in making location decisions.

It is clear that that CACM is more of a success story than LAFTA. The gestation period prior to the General Treaty enabled the awareness of the fundamental problems faced by regional integration and therefore conscious attempts to build in at early stages the necessary mechanisms to deal with them. The Treaty therefore, was simply a cumulation of experiences in regional co-operation by which regional institutions to deal with the practical problems faced were set up, unlike the Treaty of Montevideo which constitutes a blue print without prior foundation being laid. This is exemplified in attempts at co-ordinating planning functions at a regional level recognizing that trade liberalization and a common external tariff

1. *Dell, A Latin American Common Market? p.58*

were necessary but not sufficient mechanisms to induce an increase in and rechanneling of investment within the region. These attempts led to the recognition that a pre-requisite to regional planning is the development of sophisticated planning mechanisms at the national level.

Moreover the small number of countries involved (five as compared with twelve for LAFTA and twelve for CARICOM) facilitated an easier development of the integration process. So too did the fact that the disparities in levels of economic development was from the start not as great as within LAFTA. In 1960, Gross National Product within CACM ranged from $1,029 million (US) in Guatemala to US$402 million in Nicaragua, as compared with from $20,080 million (US) in Brazil to $366 million (US) in Paraguay within the LAFTA area.

The progress of integration was drastically set back in 1969 by four days of warfare (the Football War) between El Salvador and Honduras. The war destroyed the fundamental basis of Central American integration-good relations among the member states. The effects of this breakdown was clearly seen in the severe restriction on intra-regional trade during the year. There is however, reason to believe that the solid foundation upon which Central American integration was established will enable the process to overcome this setback.

The basic problem with the Central American pattern was the fact that each issue area of agreement established with the relevant regional institutions remained separate entities. None of the institutions were subjected to any other nor were they all subjected to any overall regional body that could overseer the whole process in an integrated fashion. As such any problem that came up, external to the established issue areas could not be

dealt with. This is precisely what enabled the war to take place as El Salvador's attempts to involve the issue of labour mobility in the whole integration process was never dealt with.

East African Community

Somewhat similar to the Central American experience there was a substantial period of some degree of economic and other areas of co-operation among the East African Countries (Kenya, Uganda and Tanzania) prior to the formal establishing of a common market in 1967. "Economic Integration' in this area dates back to the colonial period and as such it is important to understand the nature and essence of integration under colonialism if any evaluation is to be made of problems facing regional integration in East Africa today.

By the very nature of colonial expansion of Europe, integration took two basic forms:

(1) the creating of the more highly developed sector of the devel- developing countries as an integral aprt of the metropolitan economy, geared towards supplying industrial development in the metropolitan with raw materials, and

(2) the creation of a homogeneous market to facilitate British investment and the British settlers who cont :lled economic activity in the region.

In other words, the motive for regional integration was not the development of economic co-operation of the three East African economies as such, but the facilitation of a much wider area and easier exploitation of natural resources. All the areas of co-operation developed during this period were

geared towards this fact.

Gurali points out that there were two basic purposes behind the creation of common services:

(1) "they were designed to facilitate the exploitation of raw materials in East Africa and to create easy access to the East African market for imported manufactured goods by providing easy transportation facilities.

(2) to serve as a basis for the expansion of foreign manufacturing industry in the region".[1]

That the whold arrangement had little to do with integration of the East African Economies is exemplified in the fact that the main economic activity of the region being raw material exploitation left no room for possible trade among the member countries.

The strategic geographical position of Nairobi in Kenya, made it the most appropriate point of take-off for Colonial expansion in the area. For example, Nairobi is a relatively lower cost centre for serving a larger part of Tanzania than any other single location within Tanzania. Further, it had the advantage of proximity to the flow of european colonial trade through the Suez Canal. As such Kenya housed a much greater percentage of non-African population, who because of their control of the main economic activities in the area, provided Nairobi with a much higher purchasing base and therefore the relatively greater capability of attracting investment geared towards the whole territory. The extent to which Nairobi was consciously developed as the industrial point of the region and to which the existing areas of co-operation were geared to easy colonial exploitation is exemplified in the fact that the East African Industrial Licensing Authority was designed to protect monopolistic British investments in Kenya from possible competition if other investors attempted to develop manufacturing industries in Uganda

1. *Kassim Gurali, Towards an Independent and equal East African Common Market,* [illegible]

or Tanzania. In fact Uganda and Tanzania served only as markets to absorb the products and give further incentive for industrial expansion in Kenya.

The concentration of industrial activity in Kenya served to further expand the non-African elite, making it an attractive market which induced further investment. This brings out the salient point of integration under colonial administration, in that what was really integrated was the elite, non-African markets in each territory, heavily biased towards that in Kenya. The bulk of each of these economies remained at the subsistence level, as far apart as they ever were.

It is this state of affairs the territories faced on coming out of direct colonial rule in the early sixties and which set the basis for the increasing imbalance of benefits from attempts at furthering regional integration. It was clear by 1966 that:-

1. although for the community as a whole, intra-regional trade had grown to be of substantial importance, Kenya alone had shown some increase in its relative importance.
2. Kenya had become the chief exporter of manufactures -- approximately 68 per cent of total manufactured exports in the area, indicating the extent to which the bulk of manufacturing industries attracted to the community was located in Kenya.
3. there was increasing imbalance in intra-regional trade in favour of Kenya; the continuing deficit in balance of payments of Tanzania and Uganda being attributable to their increasing import of Kenya's high-cost manufactures (trade diversion).

4. trade between Tanzania and Uganda remained relatively small, due to their low level of industrial development.

The benefits of import-substitution activities generated through increasing intra-regional trade accrued mainly to Kenya and the costs to Tanzania and Uganda.

The pre and post-independence nationalist fervour served to bring more forcibly to the fore the imbalances in the distribution of benefits from regional integration. The Raisman Commission set up to study and advise on the deteriorating situation proposed a Distributable Pool aimed at:-

1. providing an independent source of revenue for the non-self contained common services in evidence; and
2. to effect a direct redistribution of income so as to offset inequalities.

When implemented, the Pool did bring about some measure of redistribution of monetary gains but there were no proposals to deal with the fact that the market mechanism worked to Kenya's advantage, especially in terms of industrial development. Disagreements among the member countries continued to a point where the ultimate aim of federation seemed to be impossible and Tanzania threatened to withdraw. In an attempt to prevent the disintegration of the present level of regional integration the Kampala Agreement was signed in 1964, aimed specifically at eliminating the trade imbalances between the countries. The proposals of this Agreement, however, necessitated a high level of political co-operation to make the necessary decisions, especially in relation to the conscious allocation of industries. Without this political co-operation, relationships again broke down. Very

few of the proposals were implemented. A series of unilateral policies and counter policies were instituted to serve national interests which further irritated relationships and limited the possibilities of "taking advantage of any opportunities for regional specialisation."

A further attempt to promote meaningful regional integration came with the signing of the Treaty of East African Co-operation in 1967, making for the legal establishment of an East African Economic Community an integral part of which was the Common Market. The principal aim of the Treaty was "to measure the contribution to development of the Common Market and Common Services while ensuring the equitable distribution of their benefits and in particular industrial growth."[1]

In terms of promoting industrial development in the two lesser developed areas, i.e. in effect a rechannelling of investment, the Treaty proposed:-

1. a transfer tax by which a country in deficit in intra-regional trade in manufactures may impose a tax on a value of trade not exceeding its deficit from which the goods originate.[2] The tax can only be instituted if at the time of its imposition goods of a similar nature are being produced in the imposing country or is expected to be produced within three months. In essence, the tax constituted a sort of selective tariff aimed at encouraging new areas of production in Tanzania and Uganda, who

1. *Robson. p.154.*

2. *The rate of tax must not exceed 50 per cent of common external tariff - levied at the frontier on the market price including transport but excluding any tax already levied - temporary measure - to be ended after fifteen (15) years.*

given the nature of the tax and the existing pattern of trade are the only ones to impose such taxes, and at the same time to bring about an expansion in the deficit countries in the industries for which "the maximum permitted degree of protection is sufficient to offset Kenya's cost advantages from lower production costs."

2. the decentralisation of headquarters from Nairobi - the establishment of regional organisations and redistribution of actual and potential operations. Decentralisation was aimed at effecting a redistribution of income away from Kenya to Tanzania and Uganda, and induce infrastructural developments which in turn lays the foundation for investment inflows.
3. the East African Development Bank was established "to promote industrial development in the partner states through financial and technical assistance. It was designed to operate in three basic ways:-
   - (a) to give priority to industrial development in the relatively less-industralised partner states;
   - (b) to finance projects designed to make the economies of the partner states increasingly complementary in the industrial field; and
   - (c) to apportion the greater share of loan guarantees and investments to Tanzania and Uganda; they were to each get 38.75 per cent of the total.
4. an Economic Consultative and Planning Council was set up to facilitate the co-ordination of investment policies.

The Treaty has also instituted a wide range of regional institutions from the Authority (Head of States) to public corporations, to facilitate

the smooth running of all areas of regional co-operation. The extent to which these institutions, especially those at the higher level, has any degree of regional political jurisdiction is not quite clear and has not yet been tested. Although it is difficult to say at this point how effective the Treaty has been in bringing about a greater degree of industrial co-ordination and rechannelling of investment, it has been clearly successful in promoting smoother relations and increase in intra-regional trade.

CONCLUSIONS - Towards a strategy for achieving a rechannelling of investment.

From the analysis of the structure of the economies of the CARIFTA/CARICOM region, the examination of the institutional framework and operation of the institutions within the region, we find several factors militating against the rapid integration of the regional economies and the rechannelling of investment. These fall into three broad categories:

(1) The distribution and utilisation of resources.

(2) The level of infrastructural development of the LDC's.

(3) The structure and organisation of the existing institutions.

From the structure and organisation of other areas of economic co-operation, and the measures they have instituted, certain measures may be suggested whereby some re-channelling of funds could take place.

In the area of the distribution and utilisation of resources, we find that the basic factor hindering regional integration was the wide disparity in existing levels of development among member states. The historical reasons for this disparity were mainly the distribution of resources predominantly in favour of what are now called the MDC's, and the utilisation of those resources.

On the question of the utilisation of resources, it seems that the industries associated with the principal ones, petroleum and bauxite must be transformed from their present enclave position and become really part of the national economies; there should be more

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linkage of sectors in the national economy. This condition would then facilitate a more equitable distribution of benefits at the national level. *In fact this is a pre-requisite to real regional integration.* As Felipe Herrera, one-time President of the Inter-American Development Bank put it:

> "*Integration has a vertical dimension, in dept, which does not oppose, but rather of necessity precedes, the horizontal, geographic dimension of the movement of co-ordination and complementary functioning of multi-national endeavour .... if it grows out of the decision of the minority groups that care not whether they perpetuate the vast, empty distance separating them from the masses.*"[1]

A further area of militating factors is the level of infra-structural development of the LDC's. Much of the shortfall in investment in the LDC's had been due to their low level of infra-structural development. Private investors have been reluctant to move into these areas because of the lack of physical facilities. Due to the lack of administrative development in the LDC's the Caribbean Development Bank, which is commissioned to assist the physical infrastructural development through loans has been unable to fulfill this function. Certain pre-requisites to obtaining loans from the Bank could not be met because of lack of adequate administrative structures.

[1] *Felipe Herrera.* *The Inter-American Development Bank and Latin American Integration, in Latin American Economic Integration Experiences and Prospects, Ed. Miguel S. Wioncsek, p.27*

It is imperative, therefore, that these areas of weakness be removed.

The third area of militating factors is the institutional one; this we consider the most important one.

The mere removal of intra-regional trade restrictions and harmonization of fiscal incentives while necessary, are not sufficient conditions to effect a more equitable distribution of benefits, specifically in terms of industrial development. Other conditions are required, as mentioned earlier, for example the development of the infrastructure in the LDC's. There is also the need for determining priorities on a regional basis, and so implement the necessary policies to ensure increased regional investment and at the same time ensure a more equitable distribution of benefits from industrial development.

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