

MACROECONOMIC MANAGEMENT: IS IT WORKING?

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I. INTRODUCTION

The two oil price shocks of the 1970s had an important impact on global growth and income distribution: they required strong adjustment measures around the world to combat the resulting inflationary forces. The U.S. decided to contain the inflationary impact basically with monetary policy alone. The resulting spike in interest rates smothered the economic growth momentum in the early 1980s. Countries in nearby regions, especially in Central America and the Caribbean, that have such extensive financial and trade relationships with the U.S., suffered substantially from lower growth and export absorption by the U.S.

After a period of high external capital absorption due to the recycling of OPEC surpluses through the Western banking system, these countries were also hit hard by the spike in international interest rates that sharply increased the real burden of their external debt, as well as by the subsequent drying up of new capital inflows. The eventual result was a profound internal and external crisis, a decade of negligible growth, and sharply higher unemployment and poverty incidence.

This confluence of unfavorable factors, and their longevity, forced all governments in the region to thoroughly review the adequacy of their strategic policy mix in the light of the new circumstances. The eventual outcome of this process, that initially entailed aspects of trial and error, has been positive, albeit rather uneven as far as individual countries are concerned.

This paper will focus on the smaller economies of the Caribbean and Central America because of their comparability. All have relatively small economies and a high degree of openness. Virtually all also depend to some extent on export of commodities. These factors create a special vulnerability to external shocks, be they market disruptions, international interest rate rises, or sudden changes in the terms of trade. Effective macroeconomic

¹ The author is much indebted to Matias Silvani and Miriam Perez-Fuentes for their contributions to this paper.

management is therefore essential at all times to reduce economic volatility and thereby improving the potential for sustained economic growth. This paper aims at identifying those policy mixes that so far have proven to be effective in the economic environment of Central America and the Caribbean.

II. REGIONAL POLICY FRAMEWORKS IN HISTORICAL PERSPECTIVE

The events of the late 1970s and the first half of the 1980s once again demonstrated the need for consistently sound macroeconomic management, lest governments get overwhelmed by the consequences of major, unexpected external events that can threaten a country's standard of living for a long time to come. While we can easily agree on policy changes in the abstract, the practical question is: what mixture of macroeconomic measures is appropriate for what event, how can one be better prepared in the future, and how is one to distribute the eventual cost and pain?

The great Caribbean statesman and economist, Sir W. Arthur Lewis, while speaking at the second Annual Meeting of the Board of Governors of the Caribbean Development Bank in St. Lucia on April 21, 1972, somehow seems to have had a premonition of things to come: he explicitly referred to the failure of mining to provide adequate employment in Jamaica, Trinidad and Guyana, the poor shape of regional agriculture, and the slow pace of growth in manufacturing compared with other developing countries. He explicitly warned against the possible dire consequences of the high cost levels in the Caribbean region. These were already in his time forcing regional governments to offer tax exemptions and other privileges to newcomers, which reduced local benefits from these enterprises. He recognized that while governments realized this dilemma, the people did not: they were encouraged by populist leaders to "put all the blame on foreign devils".

Sir Arthur Lewis also recognized already then what later became infamous as the 'Dutch Disease', as he stated that "the expansion of the mines threatens to destroy all other economic activity, while itself providing an almost negligible amount of employment. In the process, costs in other industries are raised beyond what productivity can support, and the result is mass unemployment". He predicted at the time that there was no easy solution: in fact, it took the Netherlands a decade of deep policy adjustments and social pain to convert the disease into what has now become the 'Dutch Wellness'.

Sir Arthur Lewis' prescriptions for tackling the structural weaknesses of his beloved Caribbean countries were rather straightforward: they included using exchange rate corrections in cases of gross overvaluation, as well as foreign trade policy, to stimulate exports and restrain imports; reductions in

money incomes or incomes policy (which he believed was hard to implement in the regional context); and productivity increases. In short, he already had identified the core of the building blocks for what was to be called macroeconomic adjustment policy since the early 1980s.

Implicitly, he already then must have foreseen the future demise of the import substitution model that was still much en vogue throughout Latin America and the Caribbean, although it did result in strong economic growth driven by rapid industrialization in the 1960s and 1970s.

History now places the start of the external debt crisis in September 1982, when Mexico during the Annual Meeting of the Bretton Woods institutions in Toronto, declared its incapacity to honor its debt servicing obligations. However, smaller countries such as Costa Rica already experienced severe financial turbulence at an earlier date, while for others the date of reckoning was initially postponed by the concomitant commodity boom. The immediate effect was one of shock and paralysis: governments did not have immediate policy prescriptions for how to tackle the multiple problems facing them, skeptical electorates were not easily persuaded that the threat of a systemic failure required painful adjustment measures, and the international banking community which had followed its herd instinct and lent to developing countries on a massive scale in its eagerness to profitably recycle the OPEC surpluses, did the only logical thing at the time: they stopped lending to emerging economies. The result was severe fiscal and balance of payment imbalances, stagflation, lots of confusion, and an abrupt interruption of the development process throughout the region.

The period 1982-1987 has entered economic textbooks as the period of 'adjustment by default'. Initially, unorthodox adjustment policies were tried out by Argentina, Bolivia, Brazil, Mexico and Peru. These basically focused on creating substantial trade surpluses to free up resources to deal with the debt servicing obligations. Unfortunately, the successes were short-lived. By the mid-1980s, spiraling fiscal deficits and the ensuing hyper inflation underlined the failure of these attempts.

By 1987, the period of 'adjustment by design' began: often aided by the multilateral institutions, governments returned to more orthodox adjustment policies that included fiscal austerity, trade reform, policy reforms, and ending the import substitution model and instead adopting an export-led growth model. By the end of the decade, these policy combinations were termed the Washington Consensus by John Williamson, a name that he now admits was a misnomer: it was neither Washington inspired, nor a complete consensus. It was something that progressively emerged from experiments with orthodox economic policies in Latin America and the Caribbean, building on policy mixes that turned out to work.

The following 10 commandments formed the backbone of the Consensus:

- fiscal discipline: a primary surplus and overall deficits contained below 2% of GDP;
- tax reform: broadening of the tax base and reducing marginal tax rates to reduce fraud and tax evasion; progressively reducing the fiscal dependency on import duties;
- public expenditure priorities: towards areas with high economic returns to improve future growth and income generation, such as law and order, health and education, sanitation and infrastructure;
- financial liberalization: strengthening the financial system, improving regulatory frameworks and supervision, deepening capital markets, stimulating competition, making pension systems actuarially sound;
- exchange rates: unified exchange rate at sufficiently competitive level to stimulate non-traditional exports;
- trade liberalization: quantitative restrictions to be replaced by tariffs, which are to be reduced progressively to the 10 to 20% range;
- foreign direct investment: domestic and foreign investors essentially to be treated equally;
- privatization: concentrate State on core functions by leaving running enterprises and utilities to the private sector;
- deregulation: abolish regulations that impede the entry of new firms or that stifle competition: concentrate on environmental protection, labor safety and supervision of the financial sector;
- property rights: provide secure property rights and land titles to all, including small farmers.

The progressive implementation of combinations of these policy prescriptions, often with the help of the multilateral institutions, eventually did have positive results. By the end of the 1980s, fiscal deficits had been strongly reduced, both exports and imports grew rapidly again, capital inflows were picking up, and international reserve levels were building up in most countries. While some would like to portray this consensus list a final rejection of Keynesian economics and an embrace of Neo-Liberal policies with many supply side elements, trying to label these policy shifts may miss the point here. The shifts did not form part of a doctrinaire strategy that tried to change the fundamentals of our societies. Instead, in most cases they were conceived in the trial and error period of the 1980s, and progressively adopted

by governments of different signature, sometimes constituting a clear break with policy stances adopted during earlier times by the same regional leaders.

While the Consensus did advocate developing and using market forces rather than denouncing, repressing or distorting them, it did not include other articles of neo-liberal faith such as slashing government expenditures to balance budgets, identifying fiscal discipline with a balanced budget, calling for overall tax cuts to prep up the economy, and denouncing tax increases to redistribute income as plunder. It also did not prescribe either firmly fixed or free-floating exchange rates, nor did it call for the abolition of capital controls, or competitive currencies, or argue that the money supply should grow at a fixed rate.

Therefore, it makes more sense to approach the Consensus as a pragmatic and incremental response to the challenges of the times, instead of a deliberate, premeditated change of policy direction to promote new ideologies, or favor new constituencies. By removing the onus of doctrine we can now free ourselves to pragmatically look for additions and refinements that render us a policy mix suitable for the specific policy challenges of small and open emerging economies.

III. THE RETURN TO STABILITY AND SUSTAINABLE, BUT NOT ADEQUATE, GROWTH

The restoration of internal and external stability and sustainable growth had to wait until the early 1990s in most cases, especially in war-torn Central America, but also in the Caribbean, that still experienced a growth crisis in the period 1991-93, essentially because of stagnation in the tourism industry in the Bahamas and Barbados, and an economic reorientation in Trinidad and Tobago. So far in the 1990s, the English-speaking Caribbean region produced an average real growth rate of just 1.1% per year, or virtually zero in per capita terms. Including the Dominican Republic, Haiti, and Belize would bring real growth to around 2% per year, basically because of the strength of the Dominican recovery after a steep recession in 1990. The causes and consequences of this insufficient growth experience, as well as possible remedies, will be subject of further discussion in the continuation of this paper.

The big disappointment of the adherents of the Consensus was that, although it was instrumental in bringing back macroeconomic stability and restore the growth momentum, it could not deliver, on its own, the much broader policy goal of adequate per capita growth, reduction of unemployment, and eradication of poverty. Which were the essential elements still missing in the strategy? What about the recoil from the

financial crisis in Mexico at the end of 1994? Or, maybe, was there a change of paradigm in the first place?

Starting with the latter, there obviously was a paradigm shift in the sense that rather stealthily, but unmistakably, the globalization process has taken center stage, this time around truly worldwide. Therefore, it is often being blamed as the main culprit of today's economic and social problems, which I believe to be incorrect, for the following reason: contrary to popular belief, globalization is not at all a new phenomenon. A century ago the world in some respects was an even more open marketplace than it is today. For many countries the ratio between external trade in goods and services and GDP was higher then, capital flows were virtually uninhibited under the gold standard, and the movement across borders of persons in search of a new destiny was much less restricted and contested. However, what is different now is that technology and information are the driving forces, and transportation modalities are so much faster and affordable, so that competition becomes truly global now, while the time for reacting to changes and new challenges is so much shorter.

Without a doubt, this globalization process forms a formidable challenge to both Central America and the Caribbean because of existing deficiencies in infrastructure, human resources, transportation modes, market access, and limited global orientation of management in the private sector. The latter may also still be unduly protected behind its borders with import duties and non-tariff barriers, especially in the case of Panama, the Dominican Republic, Belize and Haiti. As these obstacles have to be broken down under the GATT-WTO negotiated timetables, such industries are facing an uncertain future at best, unless they can find strategic alliances that can help them become cost-efficient and export oriented.

The challenge of globalization is to stay ahead in the game, both in terms of price and non-price competitiveness. Technology (and the subsequent reduction in communication, information, transportation and production cost) makes globalization feasible, but only continued global trade liberalization can make it work. Different cultures and political systems may wish to approach these challenges in different ways, and some governments (like many citizens) may be tempted to go slow on change. However, we have to realize that after downsizing (some say rightsizing) the public sector, it is left with a reduced potential for shaping the course of events. That function has increasingly shifted toward corporations that operate daily on a global scale, and which set the standards for efficiency and productivity, technological renewal, and labor remuneration, whether we like it or not.

At this point, I would like to refer to another observation of Sir W. Arthur Lewis in his book on the *Industrialization of the West Indies* during

his tenure as Professor of Political Economy at the University of Manchester. After rejecting both *laissez-faire* economics and mystical views on industrialization and international specialization he stated:

"Or, again, the fallacy that countries cannot thrive importing raw materials, processing them, and exporting the finished product, a fallacy which is all the more surprising since this is how such countries as Britain, the Netherlands and Japan have prospered for many decades. It is this fallacy which causes West Indians to think of industrialization primarily in terms of processing local raw materials, when in many cases the processing of imported raw materials offers much greater prospects of success".

Obviously, he foresaw the future of export processing that now has become such a dynamic growth and labor absorbing factor in the Dominican Republic and Jamaica in our region, based on their most abundant production factor, namely labor. In both cases, the public sector after priming the pump with infrastructure, education and training, has now largely ceded the initiative to the private sector.

On the other hand, the role of the public sector has become much more important in other crucial areas, such as setting the rules of the game, regulating, supervising, and protecting where necessary, and fostering social progress. At the national level there is an important role for government to assure that the population at large is academically prepared, but also that the fruits and opportunities are equitably shared, so that a socially coherent society can be preserved, and its citizens receive adequate protection from predatory practices, corruption and environmental degradation.

The Mexican crisis was a wake up call for all those who believed that business cycles have now been overcome and external shocks can easily and timely be accommodated with timely domestic policy corrections only. Why did the Mexican crisis occur? Basically because the desire to increase the growth performance of the economy, and the foreshadows of NAFTA which boosted foreign investment, induced an increase in aggregate demand that created an import boom insufficiently compensated by increasing exports. The result was a deficit of around 8% of GDP on the external current account, three years in a row, despite the absence of fiscal deficits. Because of insufficient reduction in local inflation, real effective exchange rates kept appreciating, which made restoration of the external equilibrium increasingly difficult. Political events added to pressures on interest rates and induced capital flight. In addition, the successive increases in short-term interest rates by the Federal Reserve made Mexico relatively less attractive as an investment locus. Still, foreign investors were willing to climb aboard the private lending bandwagon, but increasingly so in short-term, dollar-indexed bonds. However, unnoticed by many observers, Mexico had gradually depleted its reserves and by late 1994 the situation became untenable so that

Mexico was forced to devalue the peso strongly despite earlier assurances to the contrary: the Tequila crisis was a fact. But now, three and a half years later, Mexico is back on track with 5% real growth in 1996 and 4 to 5% projected for 1997; basically thanks to persistently prudent macroeconomic policies, a remarkable expansion of exports and a relative compression of imports in the wake of a steep recession in 1995.

However, for Central America and the Caribbean countries which have seen their CBI preferences erode since the inception of NAFTA, this recovery in Mexico was bittersweet: exports to the U.S. of agricultural produce, and export processing products faced increased price competition from Mexico, whereas Mexico also sharply improved its value for money performance in the globally competitive tourism industry. In addition, there are indications that some planned investments in export processing and tourism were diverted away from Central America and the Caribbean towards Mexico. The final result: despite some improvement, the last two years have been unsatisfactory in terms of real growth in both Central America and the Caribbean, although the U.S. economy kept growing strongly. The cost factor that was such a central concern to Sir Arthur Lewis in 1972 is therefore back on the front burner for the entire Caribbean Rim region, requiring creative solutions.

One crucial factor, however, cannot rapidly be provided with either multilateral or bilateral support, namely local entrepreneurship. The educational and cultural value systems of our societies either produce enough of this scarce commodity, or one has to accept the fact that this crucial element for growth and renewal will have to be procured from abroad, at considerable cost. Past experience in the region with public sector entrepreneurship of corporations and utilities has not been sufficiently successful to justify further experiments beyond infra-structural support. The globalization process requires well-equipped and independent professionals to manage corporations and utilities to enable them to deliver the best product – be it goods or services such as electricity, telecommunications, transportation, water and sanitation, or port and airport facilities – around the clock at the lowest possible cost for all. In a global system where the winner tends to take it all, insufficiently competitive goods and services will eventually be pushed out of the market, or worse, if used as essential inputs for other goods and services, may cause irreparable damage to the survival chances of potentially viable activities.

IV. LESSONS FROM THE MEXICAN CRISIS

Some practical lessons from the so-called Tequila crisis for the international community of states and organizations were summarized

succinctly in an article by U.S. Deputy Secretary of the Treasury Lawrence Summers, published in *The Economist* of January 5, 1996:

1. International capital mobility makes sound policies essential.
2. Unsustainable policies eventually cannot be sustained.
3. Prudent emerging-market governments should treat capital inflows as transitory, but capital outflows as permanent.
4. Increasing sophistication in capital markets requires high rates of savings essential for healthy development.
5. Long-term investment promotion (both domestic and foreign) is essential.
6. Red alert is required if current account deficits surpass 5% of GDP, particularly if financed short-term.
7. Although persistent fiscal deficits increase the likelihood of external current account deficits as well (twin deficits), the latter can also become untenable without the former.
8. Transparency is essential to well-functioning international capital markets; timely and correct qualitative and quantitative information is needed to maintain confidence.
9. There is an established need for enhanced IMF emergency financing capacity (GAB).
10. There is no substitute for continuing economic integration if the reform momentum in developing countries is to be sustained.

Taken together, these prescriptions form a consistent set of prudent policies and external support facilities, that once put in place, should contribute to reducing the volatility in the regional economies. This reduced volatility will boost the confidence levels of investors and domestic savers alike, and thereby contribute to enhancing the potential for future sustainable growth and employment creation.

They also stress the fact that, because regional economies are increasingly open, both in terms of flows of goods and services, as well as capital flows, individual governments have reduced degrees of freedom to follow unorthodox policies with regard to macroeconomic management: there would be immediate negative repercussions from the capital markets.

In addition, the call for continued regional integration has become much firmer lately: MERCOSUR added Chile and Bolivia as associates while Peru is interested in entering. The Andean Pact added Panama after losing Peru, the Central American Common Market is integrating while bilateral free trade arrangements have been signed with Mexico, Colombia and Venezuela, and

CARICOM has been expanded with Suriname, while the Dominican Republic obtained observer status and Haiti is pressing for accession talks.

V. LESSONS FROM THE DEVELOPMENT THINKING AND PRACTICE CONFERENCE

Elements of good governance took center stage during the Development Thinking and Practice Conference, held at the IADB Headquarters between September 3-5, 1996. The general tenor of this conference was that the recuperation in Latin America and the Caribbean from the ravages of the 1980s is still far from complete. Although major headway has been made in restoring macroeconomic stability, growth has not been adequate given the demographic dynamism (less urgent in the Caribbean than in Central America), and deep-rooted unemployment and poverty problems. Despite some recent improvement, domestic saving and investment levels are still way out of line with those required to achieve a sustained 6% real growth rate that the participants agreed is necessary to address the fundamental ills of the region.

There is no magic wand to take care of all these problems in one grand design: both traditional macroeconomic stabilization measures and country-specific interventions at meso-and micro-levels were deemed necessary, as are institutional reforms and sharply higher investment in human capital and physical infrastructure (both major victims of the budget cuts in the 1980s). The conference concluded that the globalization trend reinforces the need for rapid productivity increases, export orientation (only those firms will eventually survive that can successfully survive on global markets), and rapid adaptation to technological change. This requires a better educated, disciplined, and more flexible labor force, and labor laws geared towards the future, not the glorious past.

The conference noted some valid social reasons for the recent backlash against reforms in Latin America. There are strong indications that the current income distribution in much of South and Central America and in parts of the Caribbean is out of line with the rest of the developing world, especially with fast-growing East Asia, as can be derived from Table 1. Excessively skewed income distribution is increasingly recognized as an obstacle to economic growth, productivity, saving and investment propensities, social progress, and eventually to the social and political cohesion of the regional societies. Possible remedies range from promoting higher growth, better education (called the great equalizer in the long-term) and labor training, financial sector strengthening, social security improvements, all easily acceptable to mainstream economists and politicians. However, the conference also stressed the need for more interventionist government policies, such as promoting

Table 1 - INTERREGIONAL COMPARISON OF INCOME DISTRIBUTION, SAVING, INVESTMENT AND GROWTH

	Income Distribution			GDP Growth		Gross Dom. Invest. as % of GDP		Gross Dom. Saving as % of GDP	
	(Observation Year)	Ratio Top 20% + Bottom 20% of Income	Income Share of Top 10%	Annual Average 1980-90	Annual Average 1990-95	1980/89	1993/95	1980/89	1993/95
C. A. & Caribbean									
Guatemala	(1989)	30.0	46.6	0.8	4.0	13.5	15.9	17.5	8.9
Panama	(1991)	30.1	42.5	0.3	6.3	18.2	24.5	21.7	23.1
Honduras	(1996)	17.1	42.1	2.7	3.5	18.0	26.3	13.0	15.4
Mexico	(1992)	13.5	39.2	1.0	1.1	21.9	20.6	25.1	18.6
Nicaragua	(1993)	13.1	39.8	-2.0	1.1	21.4	17.9	5.2	-10.9
Dominican Republic	(1989)	13.3	39.6	2.7	3.9	23.6	20.8	18.3	16.8
Costa Rica	(1996)	13.0	34.7	3.0	5.1	25.6	27.2	19.3	23.1
South America									
Brazil	(1995)	25.7	47.9	2.7	2.7	20.8	21.0	23.2	21.9
Chile	(1994)	17.4	46.1	4.1	7.3	18.2	27.6	19.6	28.0
Colombia	(1995)	19.8	46.9	3.7	4.6	19.8	19.9	20.6	16.2
Peru	(1994)	10.3	34.3	-0.2	5.3	24.6	19.0	25.0	14.6
Venezuela	(1995)	12.0	35.6	1.1	2.4	21.3	16.0	25.5	20.2
Bolivia	(1990)	8.6	31.7	0.0	3.8	11.2	15.2	10.4	6.8
US & W. Europe									
UK	(1988)	9.6	27.8	3.2	1.4	17.6	16.0*	17.4	15.0*
US	(1994)	9.4	28.5	3.0	2.6	19.4	16.0*	17.4	15.0*
Switzerland	(1982)	5.9	28.6	2.2	0.1	25.9	22.9	25.7	27.4
France	(1989)	5.6	24.9	2.4	1.0	20.9	17.6	20.6	19.8
Canada	(1994)	5.2	23.8	3.4	1.8	21.6	18.8	23.4	19.7
Germany	(1989)	4.1	22.6	2.2	1.5**	20.4	21.8	23.5	22.5
Sweden	(1992)	3.6	20.1	2.3	-0.1	18.8	13.9	20.2	17.9
Netherlands	(1991)	5.0	24.7	2.3	1.8	20.2	20.3	23.8	26.2
East Asia									
Malasya	(1989)	11.7	37.9	5.2	8.7	30.6	38.1	33.1	36.7
Singapore	(1982-83)	9.6	33.5	6.4	8.7	38.1	34.9	41.8	51.0*
Hongkong	(1980)	8.7	31.3	6.9	5.6	29.0	31.5	30.8	33.6
Thailand	(1992)	9.4	37.1	7.6	8.4	29.9	41.6	26.5	36.2
Philippines	(1994)	8.4	33.5	1.0	2.3	22.5	23.5	21.0	16.0
Korea	(1988)	5.7	27.6	9.4	7.2	30.2	36.1	33.6	35.6
Indonesia	(1995)	5.1	28.3	6.1	7.6	29.1	35.1	31.9	35.6
Japan	(1979)	4.3	22.4	4.0	1.0	29.6	29.1	31.6	31.1

Source: IBRD World Development Report 1995 and IBRD World Development Report 1997 and 1998

* 1995 only

**1992-95

collective bargaining in wage negotiations, and more equitable, progressive taxation, including taxes on wealth and inheritance. The latter because it is becoming more evident that initial conditions with regard to ownership of marketable assets (including land), are determining to a considerable extent whether individuals are likely to fall victim to poverty at some point in their life cycle.

The conference also agreed on the need to break the vicious circle of premature incorporation of youth in the labor market, a phenomenon especially prevalent in South and Central America, determined by the need for additional family income. This leads to very limited accumulation of human capital, resulting in underemployment or access to dead-end, low-paying jobs. Decentralization turns out to be much more effective not when the government disappears, but rather when it plays an active role in improving local government and empowering the civil society.

With regard to labor market strategies for employment creation the conference proposed:

- increasing flexibility and strengthening of social actors;
- redesigning and enlarging social protection;
- fostering international competitiveness, mainly through increasing productivity, as nominal labor costs are already comparatively low in the region.

Especially in the case of Central America and the Caribbean region, emigration to the U.S. has always acted as a safety valve with regard to excess supply of labor on the local labor markets. In return, expatriate workers send home family remittances that have become a staple for social improvement throughout the region, but especially in El Salvador (where they represent 12% of GDP, and the Dominican Republic, where they run at 6.5% of GDP). However, recent anti-immigration legislation in the U.S. is partly closing this safety valve and income generator, and is already exerting a negative impact on family remittances to El Salvador. Hence, there is both reason for concern and for enhancing self reliance, basically by adopting growth fostering policies to the full extent.

VI. THE NEW LATIN AMERICAN CONSENSUS

As far as improving the region's growth potential is concerned, John Williamson, the chronicler of the Washington Consensus, proposed during the conference replacement of the original list of Consensus commandments with

a more updated one. This was partly in response to the insufficient growth generated so far in the region, and partly in response to experience with the power vacuum that sometimes was left by a retreating public sector, which had created more opportunity for corruption by insiders who could outsmart weak supervisory institutions, thus diminishing the checks and balances that characterize civilized societies. Therefore Williamson now favors “a policy shift away from cutting back a state that had become bloated, to strengthening a number of key state institutions, whose efficient functioning is important for rapid and/or equitable growth” (Williamson, 1996).

This new Latin American Consensus should entail “strengthening of essential functions of the state; heightening of supervision to counter corruption, such as through independent central banks and new local variants of the Securities and Exchange Commissions; bolstering institutions, such as the legal, and judiciary branches, the police force and local government; and targeting social spending where it is most needed”. For the new LAC Consensus Williamson proposes the following updated set of policy prescriptions:

- increase savings, inter alia by maintaining fiscal discipline; inadequate savings can at best stifle economic growth, and at worst cause economic collapse;
- reorient public expenditure, inter alia toward well-directed social expenditure;
- reform the tax system, inter alia by introducing an eco-sensitive land tax;
- strengthen banking supervision;
- maintain a competitive exchange rate, abandoning both floating and use of the exchange rate as a nominal anchor;
- pursue intra-regional trade liberalization; the recently warming relations between the Central American Common Market, CARICOM, and Andean Pact countries are encouraging examples;
- build a competitive market economy, inter alia by privatizing and deregulating, including the labor market;
- make well-defined property rights available to all;
- build key institutions like independent central banks, strong budget offices, and independent and incorruptible judiciary, and an agency to promote productivity improvement;
- increase spending on education and redirect it to primary and secondary levels.

In virtually all regional countries the multilateral institutions are assisting governments to implement reforms in some of the above-mentioned areas (cf. Table 4), but the pace of reform is often less than expedient, nor is the coverage complete and consistent. Nevertheless, as illustrated by recent improvements in investment and savings fundamentals, more dynamism is gradually emerging, so that higher growth rates are feasible in the medium term. However, to make the transition towards the goal of 6% sustained growth, many reforms aimed at unleashing private sector initiative, and removing policy and infra-structural obstacles to growth, still remain to be implemented.

VII. RECENT COUNTRY EXPERIENCES IN THE CENTRAL AMERICAN AND CARIBBEAN REGIONS

To provide some tentative clues with regard to the degree of success of recent macroeconomic management in Central America and Caribbean countries, this section will review the regional performances with regard to real growth, the twin (fiscal and current account) deficits, export dynamism, savings and investment, real effective exchange rates, inflation, and unemployment trends. Subsequently, these crude indicators of policy success or failure will be extended further in two tables which present some commonly used criteria for sustainability of the development process. These tables can function as a report card to compare individual country performance with neighboring countries, and to identify areas for improvement. Like a normal report card, however, these tables do not pretend to capture all activities that may matter, nor do they establish relative weights. The latter vary from country to country, and from period to period. However, as the most recent time period is being compared with the average of an extended earlier periods, some indication of the relative degree of success can be derived from the direction of the indicators.

From Table 2 below, it is evident that the growth performance in the region has been rather uneven, and that it took until the mid 1990s before reasonable growth rates were restored, except in the case of Jamaica that continues to struggle, and currently has to address structural weaknesses in its financial system. The most remarkable performance during the last two years has come from the Dominican Republic, Guyana and Suriname, all of which recently engineered rather profound improvements in their macroeconomic policy stance. The table also shows that, despite the marked growth improvement in 1995-96, the regional growth average is still below the 6% – or because of the lower population growth of the region vis-à-vis Central America, 5% – needed to make a substantial dent in un(der)employment and poverty in the region.

Table 2 - REAL GDP GROWTH IN SELECTED CARIBBEAN COUNTRIES
(PERCENTAGES, AT 1990 CONSTANT PRICES)

Countries	1981-85	1986-89	1990-94	1995-96	1996
Bahamas	3.4	2.7	-0.5	2.3	4.2
Barbados	-0.3	5.4	-1.4	5.6	8.9
Belize	0.5	9.4	5.6	3.3	1.4
Dominican Republic	1.0	5.1	2.2	6.1	7.3
Guyana	-3.4	-4.2	6.9	6.2	7.3
Haiti	-1.0	-0.5	-6.8	3.6	2.7
Jamaica	0.1	4.8	2.0	-0.6	-1.7
Suriname	-0.2	1.1	-1.1	6.8	6.9
Trinidad & Tobago	-3.2	-3.2	0.9	2.8	3.1
Unweighted Average	-1.1	2.3	0.9	4.0	4.5
Idem, Central America	2.1	2.0	3.9	3.1	2.2

Source: IDB:ESDB

In Figure 1, the twin deficits (fiscal deficit and the external current account deficit) are depicted. This figure is intended to show the magnitude of the imbalances, their direction, and – most importantly – whether or not these imbalances tend to coincide, or reinforce each other. The graphs clearly show the marked improvement that the respective twin deficits, between which there exists an arm-length relationship, recently have undergone. This was especially the case in the Dominican Republic, Haiti and Suriname, and once again, improved macroeconomic management has been a major contributor.

Belize, a country that traditionally had very prudent fiscal policies, ran into serious fiscal problems from 1991 to 1995, but was able to turn the tides by 1996, basically by cutting current expenditures, that is reducing the public sector payroll. Remarkable fiscal discipline was displayed by the Dominican Republic throughout the last decade, albeit at the cost of lowly social expenditures and public sector wages. However, the real come-back case was Guyana, which from the mid-1970s onwards until as recently as 1992 was running double digit fiscal deficits, which it was able to contain to just 2.2% of GDP on average from 1994 through 1996.

Haiti, on the other hand, is still struggling with excessive fiscal deficits, which require urgent attention lest they become destabilizing. Similarly, Jamaica's relaxation of fiscal policy in 1996, which sharply contrasted with its

Figure 1 - THE CARIBBEAN REGION: TWIN DEFICITS

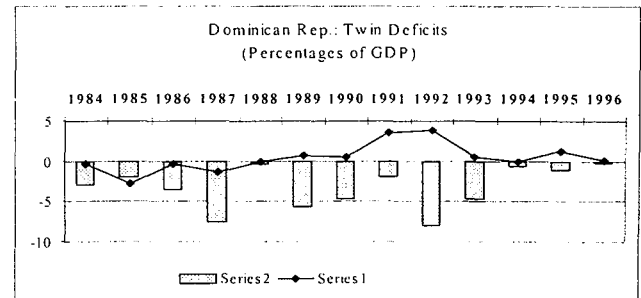
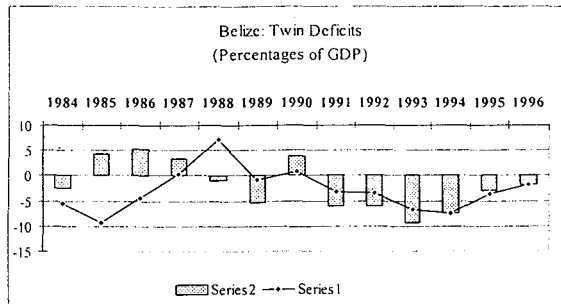
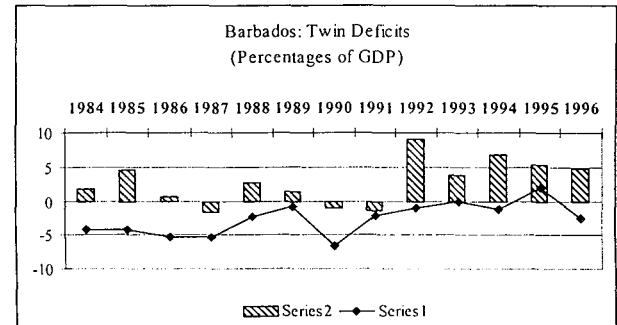
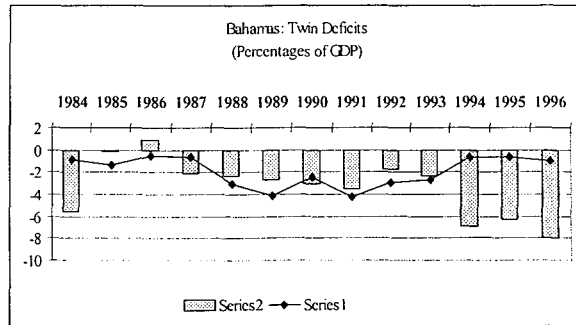
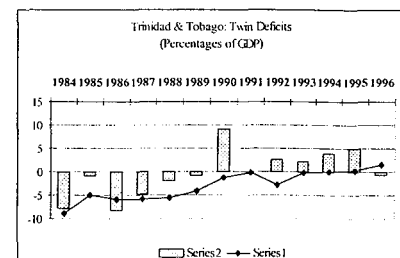
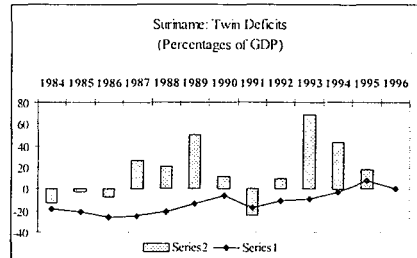
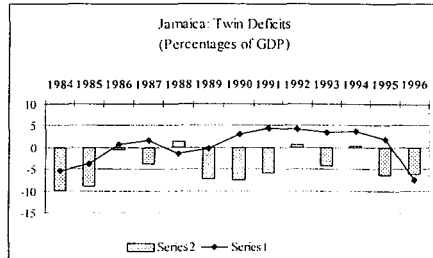
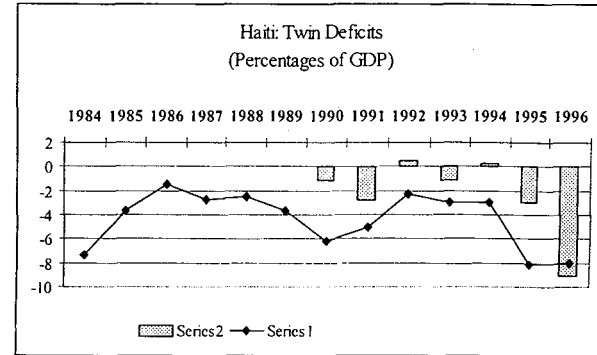
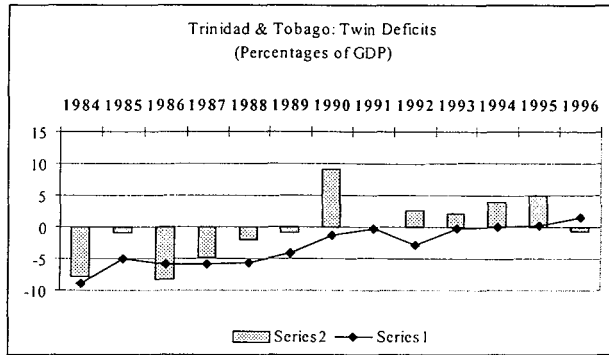


Figure 1 - THE CARIBBEAN REGION: TWIN DEFICITS (...continued)



tight monetary policy stance, resulted in a return to deficitary spending after six years of fiscal surpluses in an effort to reduce its external debt exposure. Most of the 1996 fiscal deficit, however, was related to a \$180 million rescue package for the financial sector. In the meantime, especially since 1994 Jamaica has experienced a rather steep increase in its domestic debt which, apart from causing high domestic interest rates, places a large burden on future budgets.

Export, export diversification, and saving and investment (as well as investment in human capital) are the forces behind improved growth performance as the East Asian Tigers and the industrialized world have convincingly demonstrated. So far, the regional export performance has been sub par when compared with Latin America as a whole, as demonstrated by Table 2. Also, the volatility in the region's export performance has been rather high, especially in Barbados, Guyana, Haiti, and Suriname. In addition, recent research has revealed that those countries that are successful in their export diversification efforts (and thus have reduced the countries' vulnerability to swings in their commodity-price-driven terms of trade), have realized higher and less volatile economic growth, and have been able to outperform others with regard to human development indicators (the causal relationship yet to be determined).

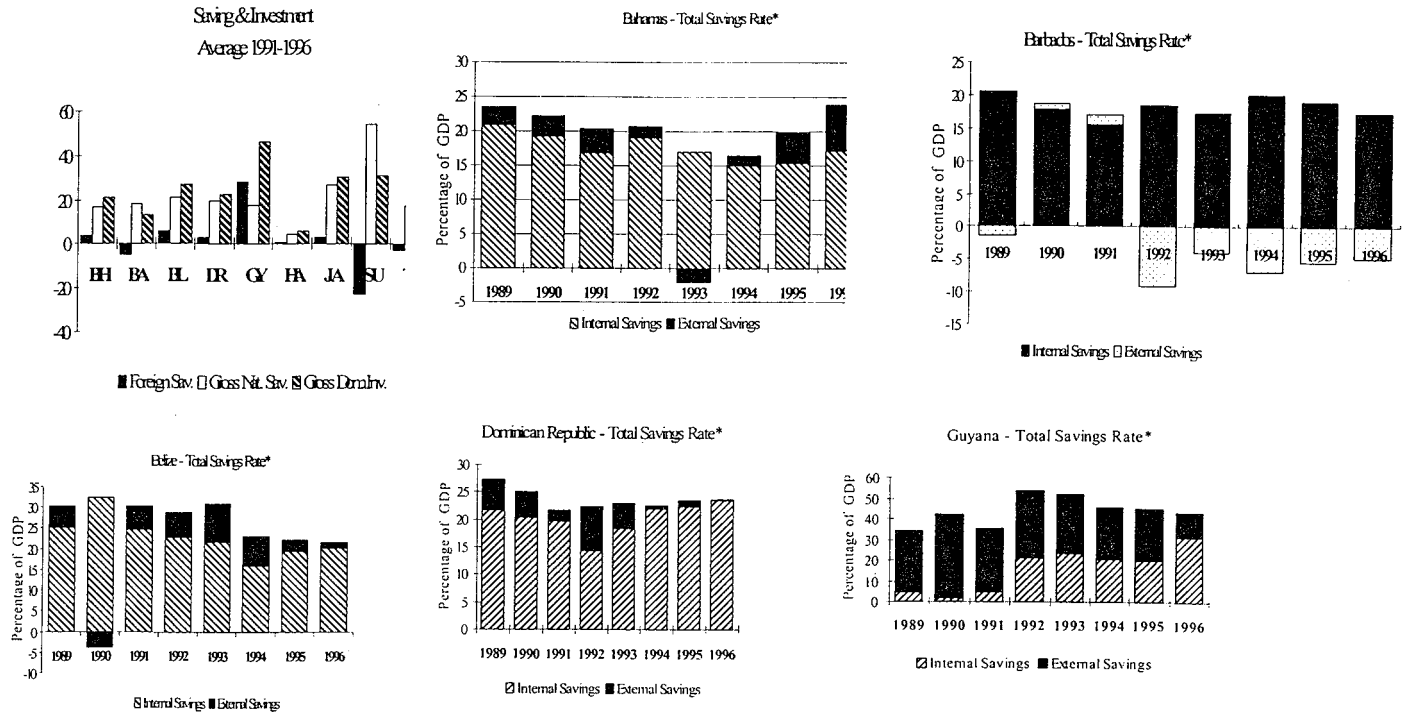
Table 3 - CARIBBEAN REGION: EXPORT GROWTH PERFORMANCE 1970-95 (GOODS & NON-FACTOR SERVICES: ANNUAL AVERAGE REAL GROWTH RATES)

Countries	1970-80	1980-90	1990-95
Bahamas	n.a	n.a	n.a.
Barbados	6.1	-0.8	0.4
Belize	n.a.	7.9	3.0
Dominican Republic	8.1	1.1	4.4
Guyana	-2.4	-4.0	13.6
Haiti	10.1	-2.8	9.5
Jamaica	-0.2	5.0	5.2
Suriname	2.7	-8.8	-14.3
Trinidad & Tobago	1.8	0.8	2.2
P.M.: Latin America	4.3	4.9	6.4

Source: IDB-ESDB

Figure 2 offers a tentative insight in the regional savings and investment trends, at least as far as national account data series are complete, which was not the case in the Bahamas, Belize, Haiti and Suriname. Striking features are first the high degree of disparity of saving and investment efforts: in Guyana, Jamaica and Suriname gross domestic investment to GDP ratios surpassed 30% between 1991 and 1996, most likely because of the relative importance of capital-intensive

Figure 2 - THE CARIBBEAN REGION: SAVING AND INVESTMENT

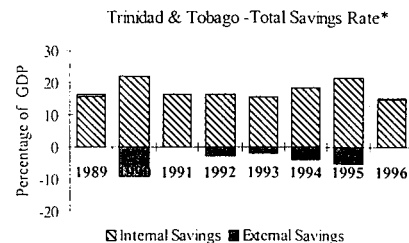
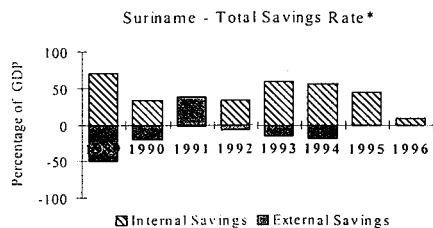
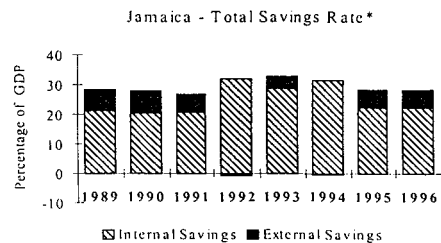
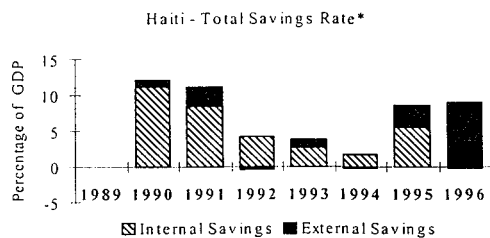


*External Savings = Balance on Current Account/ GDP

Internal Savings = Total Savings - External Savings

...Continued

Figure 2 - THE CARIBBEAN REGION: SAVING AND INVESTMENT (...continued)



*External Savings = Balance on Current Account/ GDP
 Internal Savings = Total Savings - External Savings

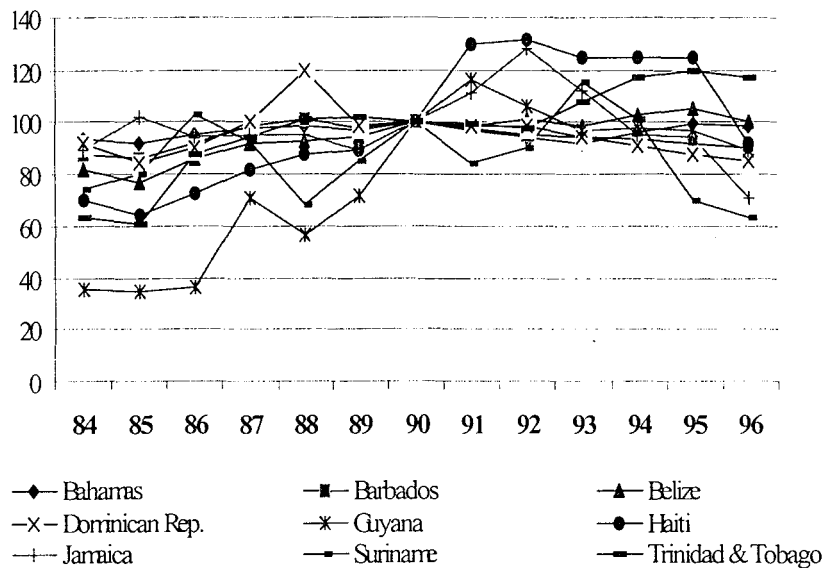
mining operations in these countries. Low investment averages were scored, on the other hand, in Barbados, Haiti, and Trinidad and Tobago, whereas the tourist destinations Belize, the Bahamas, and the Dominican Republic turned out to be intermediate investors during the observation period. Here it is interesting to see that despite relatively low investment ratios Barbados and Trinidad and Tobago have been able to return to intermediate real growth levels, suggesting an improvement in the efficiency of their investment effort (thus a reduction in their incremental capital-output ratios).

As far as internal savings efforts are concerned, very low scores are recorded in Haiti and Suriname, whereas also The Bahamas, Barbados and Trinidad and Tobago turned out to be nimble savers. Jamaica, Guyana and the Dominican Republic were in the higher savings brackets, the latter two with recently improving rates. Barbados and Trinidad and Tobago attracted negative foreign savings in recent years due to sizeable external current account surpluses. Guyana and Haiti, on the other hand, have consistently been heavy users of foreign savings.

The real exchange rates (REER: that is nominal exchange rates corrected for relative inflation differences between trading partners using trade volumes as weights) are important policy instruments for influencing countries' relative competitiveness. Using 1990 as the base year, Figure 3 shows that the Bahamas and Belize experienced very limited change in their REER's. But Barbados, the Dominican Republic, Guyana and Haiti (the latter after 5 years of depreciation), experienced a moderate appreciation vis-à-vis 1990. In the last few years, Jamaica and Suriname (the latter after a period of massive nominal devaluations), saw a strong real effective appreciation of their currencies, while only Trinidad and Tobago's currency remains depreciated compared with 1990. The result, regional exporters are complaining about loss of competitiveness, especially since the Mexican devaluations.

As exchange rates can substantially influence inflation rates, the appreciation tendency of regional currencies doubtlessly contributed to the strong decline in regional inflation rates since the early 1990s (see Figure 4). In the late 1980s and early 1990s especially Suriname, Guyana, the Dominican Republic and Jamaica experienced elevated inflation levels, whereas Suriname experienced hyper-inflation between 1992 and 1995, before banning inflation in 1996 with orthodox stabilization measures. During 1996 the average inflation levels of 7 of the 9 countries remained below 8 percent, while only Haiti and Jamaica had double digit inflation levels. In the aggregate, regional inflation levels in 1996 were the lowest in a decade.

Figure 3 - REAL EFFECTIVE EXCHANGE RATES, 1984-96 (Index 1990=100)



Year	Bahamas	Dominican Rep.	Jamaica	Barbados	Guyana	Suriname	Belize	Haiti	Trinidad & Tobago
84	10	30	10	10	30	10	10	10	10
85	10	40	10	10	20	10	10	10	10
86	10	10	10	10	10	10	10	10	10
87	10	30	10	10	30	10	10	-10	10
88	10	40	10	10	40	10	10	10	10
89	10	90	10	10	40	10	10	10	10
90	10	60	10	10	10	10	10	20	10
91	10	100	10	10	80	10	10	20	10
92	10	40	10	10	10	10	10	20	10
93	140	20	10	10	10	10	10	20	10
94	370	10	10	10	10	10	10	40	10
95	230	10	10	10	10	10	10	30	10
96	20	20	10	10	10	10	10	20	10

Table 4 gives an overview of the reforms so far undertaken by Caribbean countries. It shows that the highest incidence took place in economic stabilization efforts, trade liberalization, financial sector reforms, and some privatizations. The countries that had the highest score in terms of number of reforms were Jamaica, Guyana and the Dominican Republic, with Trinidad and Tobago, Belize and Barbados in the mid range, and Suriname, the Bahamas and Haiti as late reformers. However, labor reforms and pension reforms so far have been avoided in the region, but will have to be faced in the near future as the effects of globalization become more visible.

Table 4 - CARIBBEAN REGION: TIMING OF REFORMS BY COUNTRY, 1986-96

Type of Reform:	86-87	88	89	90	91	92	93	94	95	96
Stabilization	DR JA			DR		GY JA			SU	
Trade Liberalization	JA	GY	TT	DR		BA		BE HA SU		BH
Tax Reform							JA	BE		BA BE DR GY
Financial Sector	GY	GY		TT	DR	JA		BH	BA BE HA	GY
Privatization	JA				BE JA GY	BA		TT		
Labor Reform										
Pension Reform										

Source: IDB-IPES 1996

As far as privatization is concerned, between 1990 and 1995 Belize (2.5 percent of GDP), Guyana (1.7%), Trinidad and Tobago (1.6%), and Jamaica (1.5%) were the front-runners, followed at a long distance by Barbados (0.7% of GDP). For Latin America as a whole revenue from privatization amounted to 0.8% of GDP over the same period.

Table 5 shows the regional unemployment trends of the last 9 years, based on officially published data. Although the series are rather spotty in some cases, the level of unemployment is high compared with other regions in Latin America. Also, the trends are rather diverse: of three fixed exchange rate countries the Bahamas and Barbados had unemployment peaks in the early 1990s, with subsequent improvements, but Belize's unemployment has consistently, and rather sharply increased during that period. Jamaica's current crisis in the export processing industry has caused a substantial loss of employment in 1996, whereas the construction activity caused by strong

foreign investment in the hydrocarbon downstream sector has helped reduce Trinidad's jobless rates by 4 percentage points since 1993.

Table 5 - CARIBBEAN REGION: RECENT UNEMPLOYMENT TRENDS

Countries	88	89	90	91	92	93	94	95	96
Bahamas	11	12	12	12	15	13	13	11	12
Barbados	17	17	15	16	22	24	22	20	16
Belize				4		10	9	13	14
Dominican Republic	18	19	19	19	20	21	16	16	17
Guyana					12	11			
Haiti									
Jamaica	19	17	16	16	16	16	15	16	20
Suriname			16		17	16			
Trinidad & Tobago	21	22	20	19	20	20	19	17	16

Source: IDB-ESDB, CP and SEP 1997

In the final Tables 6 and 7, an application is given of 10 much-quoted sustainability benchmarks that by themselves do not guarantee adequate economic growth, but should contribute to improved growth performance by reducing macroeconomic volatility, and improving the country's capability to withstand unforeseen external shocks, such as rising interest rates and falling terms of trade. As mentioned earlier these benchmarks should be interpreted as indicative norms for desirable ranges, but their relative weights will vary from country to country and from period to period, depending on the country's most pressing constraints.

These selected benchmarks, which express a strong personal preference (if not bias), entail:

- fiscal deficit, ideally not to surpass 2% of GDP;
- fiscal revenue, ideally in the range between 20 and 30% of GDP;
- external current account deficits, ideally not to surpass 3% of GDP;
- international reserves, not to fall below 3 months of import coverage;
- consumption to GDP ratio, ideally not to surpass 75% of GDP to promote savings;
- investment ratio, ideally in the 25 to 35% of GDP range to foster the growth capacity;
- real effective exchange rate, not to appreciate more than 2% per year;

Table 6 – CENTRAL AMERICA: SUSTAINABILITY BENCHMARKS

COUNTRY	Fiscal (NFPS) Deficit 1/ (Max. 2% GDP)		Fiscal (NFPS) Revenue 1/ (20-30% GDP)		BOP Current Acct. Deficit (Max. 3% GDP)		Reserves/ Imports 2/ (Min. 12 weeks)		Consumption 3/ (Max. 75% GDP)		Investment 3/ (25-30% GDP)		REER 4/ Appreciation (Max. -2% p.a.)		External Debt Service (Max. 25% XGFS)		Inflation 5/ (Max. 10% p.a.)		Real GDP Growth/ Capita (Min. 0)	
	1990/ 94	1995/ 96	1990/ 94	1995/ 96	1990/ 94	1995/ 96	1990/ 94	1995/ 96	1990/ 94	1995/ 96	1990/ 94	1995/ 96	1990/ 94	1995/ 96	1990/ 94	1995/ 96	1990/ 94	1995/ 96	1990/ 94	1995/ 96
BELIZE	-4.0	-2.8	24.9	21.8	-4.6	-0.4	11.7	9.8	78.8*	80.4*	28.3	21.9*	1.1	1.4	7.9	13.5	2.1	4.6	1.7	-0.6*
COSTA RICA	-1.7	-3.3	27.6	27.4	-5.9	-1.6	20.8	16.0	77.1	77.4	27.9	23.2	2.8	-0.5	19.0	16.0	18.2	20.4	2.4	-1.4
EL SALVADOR	-2.0	-1.3	13.6	17.2	-1.8	-2.5	14.4	16.0	97.3	96.5	17.0	17.8	-4.5	-7.0	23.2	14.0	13.7	9.9	3.8	1.9
GUATEMALA	-0.8	-0.4	8.9	8.9	-4.5	-3.5	17.8	12.8	91.0	91.7	15.8	13.9	-3.9	-1.4	16.6	12.5	16.9	9.8	1.1	1.3
HONDURAS	-5.8	-3.2	28.1	29.9	-8.1	-4.5	6.1	9.5	78.0	73.2	27.7	31.5	4.7	-5.1	35.2	30.5	18.4	26.7	0.3	1.1
NICARAGUA	-4.7	-6.6	25.3	30.2	-25.1	-20.8	8.5	8.3	106.2	94.5	20.8	29.5	4.2	-0.4	71.0	26.5	158.1	11.3	-2.7	1.6
PANAMA	-0.7	0.3	30.8	28.4	-9.2	-2.6	13.8	16.5	72.7	72.5	22.2	26.8	3.5	0.3	7.6	9.0	1.1	1.1	4.8	0.4

Sources: IDB, IMF, WDT

OUTSIDE RANGE: GREY

WITHIN RANGE: WHITE

1/ Overall Deficit and Current Revenue. Belize and Guatemala: Central Government. Others: Non-Financial Public Sector.

2/ Imports of Goods (FOB). Ratio expressed in weeks.

3/ Refers to Total Consumption and Total Investment at current prices. Calculated as a percentage of GDP (local currency) at current prices.

4/ End of period. (Geometric) Average REER calculated from index (1990=100). A minus sign (-) indicates an appreciation of the local currency.

5/ Average annual inflation. Average inflation calculated as geometric mean over relevant period.

Table 7 – THE CARIBBEAN: SUSTAINABILITY BENCHMARKS

COUNTRY	Fiscal (NFPS) Deficit 1/ (Max. -2% GDP)		Fiscal (C.G.) Revenue 1/ (20-30% GDP)		BOP Current Acct. Deficit (Max. -3% GDP)		Reserves/ Imports 2/ (Min. 12 weeks)		Consumption 3/ (Max. 75% GDP)		Investment 3/ (25-40% GDP)		REER 4/ Appreciation (Max. -2% p.a.)		External Debt Service (Max. 25% XGFS)		Inflation 5/ (Max. 10% p.a.)		Real GDP Growth/ Capita (Min. 0)	
	1990/ 94	1995/ 96	1990/ 94	1995/ 96	1990/ 94	1995/ 96	1990/ 94	1995/ 96	1990/ 94	1995/ 96	1990/ 94	1995/ 96	1990/ 94	1995/ 96	1990/ 94	1995/ 96	1990/ 94	1995/ 96	1990/ 94	1995/ 96
BAHAMAS	-2.6	-0.8	17.0	18.5	-3.5	-7.2	7.9	6.7	89.1	87.5	20.8	23.5	-0.8	1.6	4.4	4.5	4.3	1.7	-2.1	-0.8
BARBADOS	-2.3	-1.4	29.9	30.4	3.5	5.1	13.4	16.5	83.1	84.0	14.5	13.4	-1.4	-1.5	14.4	9.0	3.3	2.1	-1.6	5.2
BELIZE	-4.3	-2.8	34.8	22.8	-4.9	-2.4	11.8	9.8	78.8	80.4	28.4	21.9	0.6	-1.3	8.2	13.5	2.3	4.6	2.7	0.6
DOMINICAN REPUBLIC	1.7	0.7	14.5	14.5	-4.0	-0.9	7.5	5.7	82.6	74.3	23.0	27.9	-1.9	-3.3	12.6	7.0	23.9	8.9	0.1	4.2
GUYANA	-14.1	-2.6	34.1	34.2	-31.5	-18.8	21.9	27.6	81.6	74.8	38.4	34.0	-0.5	-4.2	41.6	16.0	40.1	6.3	6.0	5.0
HAITI	-3.9	-5.5	5.8	8.6	-0.8	-6.0	2.8	8.4	106.0	118.3	6.5	3.8	4.5	-12.9	6.2	24.5	22.3	25.3	-9.0	1.5
JAMAICA	3.7	-3.1	29.7	33.8	-3.3	-6.2	9.9	14.3	74.7	79.9	30.0	32.3	-1.0	-12.7	27.8	21.0	40.1	20.7	1.0	-1.3
SURINAME	-9.5	2.6	23.5	34.6	4.8	0.3	n.a.	n.a.	65.2	74.3	25.5	28.2	0.3	-20.5	n.a.	8.0	100.8	117.5	-1.5	5.6
TRINIDAD & TOBAGO	-0.9	0.4	27.0	27.5	3.6	2.2	16.0	12.1	74.1	70.9	14.2	16.6	3.2	0.2	26.2	21.5	8.2	3.3	-0.2	1.6

Sources: IDB, IMF, WDT

OUTSIDE RANGE: GREY

WITHIN RANGE: WHITE

1/ Overall Deficit and Current Revenue (as a percentage of current GDP) of Central Government. Haiti: Refers to Non-Financial Public Sector.

2/ Imports of Goods (FOB). Ratio expressed in weeks.

3/ Refers to Total Consumption and Total Investment at current prices. Calculated as a percentage of GDP (local currency) at current prices.

4/ End of period. A minus sign (-) indicates an appreciation of the local currency.

5/ Average annual inflation. Average inflation calculated as geometric mean over relevant period.

- external debt service, not to exceed 25% of total exports;
- inflation, not to exceed 10% (above 8% seems to create distortions: IMF)
- last but not least, real growth should remain positive on a per capita basis.

To this list should be added ideally also domestic debt, as well as consistent improvement in income distribution and poverty incidence. Unfortunately, at this moment no region-wide consistent data series in these areas are available, so that they remain outside the scope of this paper.

The use of a matrix of sustainability criteria should be seen as an analytical tool that facilitates comparison of one country over different time periods, and/or comparison of different countries at the same, or different times. Neither of the criteria should be taken too absolutely, or too mechanistically. Some of the criteria may be too strictly formulated in some cases, whereas others may be very close to the margin. In some cases data may not be available, or very reliable in the first place. In addition, there may be very valid reasons for a country to have significant variations in certain variables or indicators during a certain time frame. Thus, there is no substitute for in-depth country knowledge. Nevertheless, the matrix may be a valuable analytical tool for the study of macroeconomic trends in the region and for inter-country comparisons.

The sustainability criteria matrix for the Central American region (Table 6) shows very tentatively an improvement over time for the region as a whole, when 1995-96 is compared with the average for 1990-94. It shows that Panama had the highest overall score, followed at some distance by Belize, Costa Rica, El Salvador and Guatemala. It also reveals that in 1995-96 just 3 out of 7 countries had satisfactory scores for the fiscal deficit whereas 5 countries reached positive economic growth on a per capita basis (but as indicated earlier, not of a sufficient magnitude), and for (ex post) external debt service ratios.

For the greater Caribbean region the sustainability matrix (Table 7) shows very substantial improvements towards fiscal balance (except in the cases of Haiti and Jamaica), and even 3 countries with a fiscal surplus over 1995-96. Furthermore, there was some improvement in the external current accounts, and modest improvements in investment ratios and international reserve adequacy. Moderate improvement took place in ex post external debt service ratios, and real per capita growth of the economy, while substantial moderation was recorded in inflation. However, as a counterpart to the inflation improvement 5 out of 9 regional countries experienced a more than marginal appreciation of the real effective exchange rate, and thus some real loss of external competitiveness. This was especially the case with Haiti, Jamaica and Suriname.

In the Caribbean Region the best overall score over the period 1995-96 was realized by Trinidad and Tobago (7 out of 10), Barbados, the Dominican Republic and Suriname (6), followed by Belize and Guyana (5). Masked by the average for 1995-96 is the fact that after a period of hyperinflation due to – among others – strong exchange rate corrections, Suriname's inflation rate fell from 235 percent in 1995 to virtually zero in 1996. The matrix also reveals that, not surprisingly, of all the regional countries Haiti still seems farthest away from sustainable economic trends, whereas Jamaica had difficulties reaching sustainable macroeconomic indicators in both periods reviewed.

VIII. CONCLUDING REMARKS

The foregoing suggests a fairly high degree of success of recent macroeconomic management in the region in terms of return to stability, despite the ripple effects of the Tequila crisis, and resumption of sustained growth. In some of our countries continued improvement in the growth performance is observable, but region-wide growth in the last two years still remains between 1.5 to 2.5 below the norm required to make serious inroads in ingrained un(der)employment and poverty.

It is ominous that this growth deficit persisted despite exceptionally high growth rates in the region's main market, the U.S., and exceptional growth rates in the Dominican Republic (on the strength of tourism and agriculture), and Guyana and Suriname (based on exploitation of tropical forests and non-renewable mineral exploitation). Hence the need to continue deepening structural policy and institutional reforms so as to better prepare the countries for the challenges posed by the upcoming trade liberalization measures agreed with GATT/WTO, and the ongoing process of globalization.

It is obvious that an early solution to the current financial crisis in Jamaica should foster economic recovery by removing current obstacles to domestic saving and investment. But it also would require a solution to the mushrooming internal debt, a problem not unlike the one facing Costa Rica. Haiti should be able to grow at a much faster pace once it is able to implement structural reforms that would trigger substantial bilateral and multilateral support for new investment in human resources and infrastructure. Suriname's remarkable growth rates in 1995-96 basically recovered the loss of 1993-94, and thus are likely to taper off somewhat in the medium term, as may Guyana's where the reform process enters a more mature phase.

The Bahamas, Barbados and Belize are the three countries in the region that (together with Panama) consistently have forgone using the exchange rate

as a vehicle to foster export growth and contain imports. Not surprisingly, in the case of the Bahamas and Belize this has recently led to low economic growth and tightening international reserves. The interesting case, however, is Barbados, because it has stuck to a tight fiscal policy, and a stringent incomes policy, combined with more dynamic marketing activities. So far, these policies have been rather successful, albeit aided by a fiscal policy relaxation in 1996. Especially the strong performance of the sectors producing tradable goods and services in Barbados was a noticeable feat that shows that alternatives to producing high volume, low value added productions can be successful in the region.

All in all, there is still considerable scope throughout the region for improving both the fiscal and the balance of payments situation, as well as for making the private sector, and the utilities, more agile and cost-effective. As the case of Barbados shows for the tradable goods and services sectors, and Jamaica, and the Dominican Republic as well as Barbados in the tourism industry, effective promotion can be a powerful marketing tool. Strengthening the domestic private sectors with joint ventures and strategic alliances or marketing arrangements, and bringing the utilities, as well as the transportation facilities, at their highest levels of technical and economic efficiency, is another one.

Unlike Central America, the Caribbean region has a fairly mature demographic profile, with population projections showing that around the year 2010 the dependency ratio (defined as the ratio between the dependent age brackets of 0-14 plus 60 and above, divided by the potential labor force age of 15 through 59), which had been consistently declining since 1970, will start rising again as more persons reach retirement age. This will have substantial long-range financial consequences, often beyond the current fiscal capabilities. Therefore, an urgent review of the actuarial soundness of regional pension and social security systems is highly recommendable. A movement towards more privatized and personalized pension systems like the one much earlier adopted by Chile, an example already followed by other Latin American countries, may become opportune.

Such a system might also be instrumental in developing local or regional capital markets, which could further be supported by continued reforms of the local banking systems, including adequate regulation and supervision, and strengthening competition. There is ample scope for improving the efficiency, effectiveness, and customer responsiveness of the local banking systems: improvements should enhance the local savings and investment propensities, and

reduce the cost of doing business, and therefore contribute to a higher growth dynamism and less dependency on foreign savings.

Both investment and exports – and especially a well-balanced export diversification and marketing program – are key instruments for fostering economic growth, as are investment in human capital, productivity enhancement, and productive infrastructure, all of which should therefore be prioritized over current consumption.

Finally, it is of paramount importance that all avenues be explored for creating a larger economic space for the Central American and Caribbean regions, whether it be accession to NAFTA, NAFTA-parity, CARICOM/CACM/Andean Pact cooperation, or alternative free trade arrangements such as the Free Trade Area of the America (FTAA) that is to be established by the year 2005. Such arrangements should help the region to establish economies of scale and get out of productions with little value added or with shrinking markets. Accepting the likelihood that the region will remain a medium-high cost environment should encourage the productive sectors to actively identify those productions and services, and market segments, that can generate higher value added. Making the transitions early in the game is going to be an essential prerequisite for improving the region's external competitiveness. Non-price competitiveness factors and marketing should therefore also receive the highest possible attention. The globalization process opens opportunities as well as challenges, and the best prepared stands to gain the most.

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