Achieving Sustainable Growth in the Caribbean: The Role of Competitiveness

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at the

Governors' Roundtable

of the

Forty-Sixth Annual Meeting of the

Board of Governors of the Caribbean Development Bank

held on

Thursday, May 19, 2016

Montego Bay

Jamaica

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Introduction

CDB's borrowing member countries (BMCs) have experienced low and volatile growth over the last decade, and as shown in Table 1, this growth has lagged other country groups, including other small states. Indeed, the average growth rate of BMCs during the period was less than half that of other small states, and just over a quarter of that of emerging market and developing countries. What is more significant is that the volatility of that growth was about twice that of other small states and emerging market and developing economies. In essence, average growth is lower, but the swings are more extreme.

Much of this performance results from the high export concentration among BMCs. In a sense, all BMCs rely exclusively on the exploitation of natural resources. In the case of Guyana, Suriname and Trinidad and Tobago, these natural resources are commodities, while for most of the other countries, the endowments relate to tourism assets. This has created a situation where these countries are highly susceptible to shocks that affect these respective industries, rendering growth rates that are very volatile, and on average, relatively low. This note seeks to explore the likely reasons for this performance, and more importantly, suggest some solutions. The main proposition is that institutional reforms that improve the business environment are key to increasing and sustaining investment and growth.

Table 1: Selected Country-Group GDP Growth, 2005-14

Country Group	Average GDP Growth Rate (%)	Volatility (standard deviation of growth rates)
World	3.7	1.7
Emerging Market and Developing Economies	6.1	1.8
Non-BMC Small States (WB definition)	3.4	1.7
BMCs	1.6	3.0

It is being proposed that the failure of BMCs to move beyond the exploitation of their natural endowments reflects a lack of competitiveness. Essentially, the delivery of goods and services produced in the Region to export markets can hardly be done at prices, quantity and reliability that compares with competitors. Even the exploitation of tourism assets cannot be profitably undertaken without special regimes that include tax holidays and other concessions.

There are approximately 54 economies in the world that are classified as small states by the World Bank or the United Nations, and all BMCs are included in this group. In 2014, the non-weighted average per capita GDP of CDB's 19 BMCs was roughly equivalent to that of other small states. Based on the average levels of population and GDP growth for the last decade and making adjustments for possible slowdown in GDP growth rates as countries transition through various stages of development, per capita GDP was projected to 2050. These projections suggest that by 2050, the average per capita GDP of BMCs could be half the average of other small states. Additionally, in 2014, eight BMCs were above the simple average per capita GDP of small states. The projections suggest that by 2050, while only 3 would be above the average under the scenarios. While this is indicative, it suggests strongly that the Region will largely trail other small states if efforts are not made to increase the current tepid rates of growth.

If the Region is to generate high and sustained growth that would allow it to maintain its standing in the global economy, it will require the development of competitiveness that can foster greater diversification. In small countries, diversification is limited. Nevertheless, many small countries have achieved relatively significant levels of diversification. These include Mauritius and Singapore - which are two and a half times and slightly smaller than the land area of Dominica, respectively - have done so, and consequently, have maintained relatively high and stable growth rates.

The Link Between Competitiveness and Low Growth in the Caribbean

According to the World Economic Forum, competitiveness refers to the institutions, policies and factors that drive productivity. At a very basic level, productivity determines the ability of a country to deliver a good or service to consumers at a level of price, quality and reliability that compares with other sources. By extension, productivity determines the rates of returns on investments in a country, and thus its ability to generate investment, income, exports, jobs and prosperity. Enhancing competiveness – raising productivity - has been established as the key determinant in driving growth and prosperity and reducing absolute poverty. Empirical evidence also points to a number of factors that drive productivity. Table 2 lists the "pillars" identified by the World Economic Forum and used in its Global Competitiveness Index to assess the competitiveness of countries.

Table 2: Competitiveness Determinants

Pillar	**Impact on Productivity**
Institutions	Defines legally binding or informal constraints and enforcement mechanisms, therefore affecting the way that people organize themselves and their economic transactions
Infrastructure and connectivity	Facilitates the exchange of products and ideas, and also allows the movement of people
The macroeconomic environment	Determines the level of uncertainty among potential investors, but also defines the leverage that governments have to guide the economy by way of their tax and expenditure policies
The health of the workforce	Influences the ability and availability of workers in the production process
The education of the workforce	Defines the efficiency of the workforce and the ability of a country to move up the value chain
Product and service market efficiency	Determining the way that resources are allocated, relative prices and the degree of innovation. This is affected by burdensome or distortionary taxes and discriminatory rules
Labour market efficiency	Allows for the effective matching of jobs and skillsets, while incentivizing employees and employers to act in a way that promotes productivity
Financial market efficiency	Influences productivity by allowing resources to find the best projects, facilitating the pooling of resources that can reduce risks and increase project size, better monitor investments, and reducing transactions costs
Market size	The size of the market allows for the exploitation of economies of scale
Business sophistication	The quality of networks (clusters, etc.) and the quality of individual firms, operations and strategies
Innovation	The development and implementation of technological breakthroughs

Source: "The Global Competiveness Report 20115-15" World Economic Forum.

There are a number of indices that are used to assess competitiveness or specific aspects of it. Perhaps the most comprehensive is the World Economic Forum's Global Competitiveness Index. The index uses various measures of the criteria above to compute an index of competitiveness which is used to compare performance across 140 countries. The latest version of this index includes only four BMCs – Guyana, Haiti, Jamaica and Trinidad and Tobago. Jamaica has the highest ranking at 86, followed by Trinidad and Tobago at 89. If the ranked BMCs are used to gauge other Regional countries that are not ranked, there are some general statements that can be made about the Region's competitiveness performance. The first is that the Region is well below the middle of the pack in relation to competitiveness. Secondly, higher education and training, business sophistication, the availability of financial services and technological readiness are dimensions where the Region performs well. Thirdly, infrastructure quality is middle of the pack. Fourthly, there is need for improvement other areas, especially macroeconomic stability.

The World Bank produces the Doing Business Index, which assesses the regulatory environment affecting small and medium-sized enterprises throughout their life cycle. The areas covered include time taken and cost to start a business, obtain planning and construction permission, get electricity, pay taxes, trade across borders, enforce contracts and close a business, as well as the extent of protection of minority shareholders and the ease of obtaining credit.

The index is used to rank 189 countries, including 14 independent BMCs (see Appendix 1). The average ranking of the BMCs is 115, with the highest ranked country being Jamaica at 64. Only Jamaica, St. Lucia (77), Trinidad and Tobago (88) and Dominica (91) are in the first half of the rankings. The advancement of institutional reforms that impact on competitiveness in BMCs has lagged that of other emerging market and developing economies. In fact, the average Doing Business rank of the Region slipped from 100 to 115 between 2014 and 2016 as reforms in other emerging market and developing economies continues to outpace those in the Caribbean. Only Jamaica being the only country with an improved rank

In relation to doing business, there are a number of areas where performance across most countries surveyed is way below global averages. These areas are registering property, getting credit and resolving insolvency, suggesting the need for significant reforms. Members of the Eastern Caribbean Currency Area performed reasonably well in relation to enforcing contracts; but in other countries, the performance is way below the global average.

There is significant evidence to suggest that there is a strong relationship between the Doing Business criteria and growth. Marek Hanusch (2012), in a study entitled "The Doing Business Indicators, Economic Growth and Regulatory Reforms" finds a strong causal relationship running from the Doing Business score to growth, especially those related to access to finance and enforcement of contracts. Similarly, Jamal Ibrahim Haidar (2012) tested the hypothesis that business regulation reforms covered by the Doing Business survey causes GDP growth increases, and was more specific in his findings. The study found robust support for the position that business regulatory reforms are good for economic growth estimating that on average, each business regulatory reform is associated with a 0.15% increase in growth rate of GDP. Moreover, small states such as Singapore, Mauritius, Costa Rica and Rwanda have managed to generate relatively high and sustained growth rates by, among other things, maintaining and improving the institutional and regulatory framework for businesses, as well as other dimensions of competitiveness. Indeed, compared with the average growth rate of BMCs of 1.7% in the last decade, Costa Rica, Mauritius, Rwanda and Singapore recorded average real GDP growth of 3.8%, 3.7%, 7% and 4.9%, respectively.

Improving Competitiveness in BMCs

Generating sustained inclusive growth for poverty reduction, requires that BMCs achieve some level of diversification by enhancing competitiveness. Diversification has its limits, given the size of the BMCs. There are clearly aspects of competitiveness where the performance of BMCs places them in a position to be competitive. However, these areas need to be complemented by improvements in other areas in order to fully develop and exploit competitive advantages in appropriate niches. It is reasonable to expect that some aspects of competitiveness will be more important for specific types of goods or services, but there are some critical drivers of competitiveness that are fundamental. The areas of competitiveness where BMCs need to improve include macroeconomic stability, as well as the regulatory and institutional framework for doing business. In those regard, there are some areas that require special attention

Macroeconomic Stability

Macroeconomic stability has the potential to discourage investors if they anticipate that corrective measures could change the return profile of investments. There is a need for some focus on the institutional improvements that are necessary to restore and maintain macroeconomic stability. Some of these reforms are incorporated in the Public Expenditure Framework Such improvements include budgetary system improvements, revenue system enhancement, debt management improvement and advocacy on debt issues.

Registering Property

Property registration can be a lengthy and involved process in the Region. Added to this, land dispute resolution, the quality, transparency and reliability of land administration needs to be improved. Steps would include the use of electronic platforms for land registry.

Access to Finance

Although general access to financial services is good in the Region, the access to finance of small and medium-sized businesses is affected by a number of deficiencies. These relate to the legislative and regulatory framework for using moveable assets as collateral; credit bureau establishment; and improvements in the venture capital eco-system.

Resolving Insolvency

There is a pressing need for the improvement of the legislative framework for resolving insolvency in the Region. Good insolvency legislation performs many roles. Insolvency legislation promotes entrepreneurship and risk-taking by allowing a “fresh start” in the case of failure and establishing clear guidelines for reorganization procedures. Some BMCs, including Grenada, Jamaica, St. Kitts and Nevis, St. Vincent and the Grenadines and Trinidad and Tobago, have modernized their insolvency legislation. However, there is a need for such legislative improvements to be rolled out across the Region, and to address bottlenecks that prevent the implementation of this reform.

Enforcement of Contracts

Investor confidence depends heavily on the ability of the court system to deliver speedy judgment on contract disputes. Indeed, empirical evidence suggests a strong link between improving this area and growth. Jamaica has taken a number of steps to improve its judicial system generally, and improve contract enforcement specifically. There are some lessons that can be derived from the steps that Jamaica has taken in this regard. Judicial reform needs to be at the center of this thrust.

Improving Competitiveness: The Case of Jamaica

Jamaica has been taking a number of steps to improve its competitiveness. These steps span both infrastructure upgrades as well as institutional and regulatory reforms. The institutional and regulatory reforms have also been broad, including public finance management reforms that have helped to engender macroeconomic stability. Together, these efforts have contributed to increased investment and an improved trade balance, and are expected to lead to higher and more stable growth.

There have been a number of reforms of Jamaica's public finance management systems that are intended to regain and entrench fiscal sustainability. These include a fiscal rule that is enshrined in law, and commits Government to a policy framework that is consistent with the achievement of a debt-to-GDP ratio of 60% by March 2016. There are also a number of reforms that are intended to improve tax collection, and enhance budgetary systems. The upshot of these has been the maintenance of a primary balance that is sufficient to reduce the very high debt to GDP ratio and a restoration of confidence.

The Government also has targeted the areas identified in the World Bank's Doing Business Index for improvement. Under these headings, the following reforms are underway:

- **Starting a business.** Emphasis been placed on implementing a single business registration form; implementing an electronic interface between BOJ and Tax Administration Jamaica (TAJ) and creating an electronic platform for registering businesses.

- **Taxes.** Electronic filing for all major taxes is mandatory, and recently introduced a special form to facilitate the quarterly submission of tax returns for self-employed persons;

- **Registering Property.** Reforms in this area have strengthened and expedited the Land Administration and Management Programme. Thousands of titles have been issued under this programme since 2011.

- **Access to finance.** Among several initiatives being undertaken in this area, Jamaica established a credit bureau. Moreover, led by the Development Bank of Jamaica (DBJ), the country is in the process of improving its venture capital ecosystem. The programme is a comprehensive one that seeks to address key weaknesses across all aspects of the venture capital ecosystem, including the sustainable flow of business-ready investments through support of entrepreneurs, incubators and accelerators and sponsorship of business model competitions and pitch events.

- **Trading across borders.** GOJ has implemented ASYCUDA World, as well as a Port Community System and went fully electronic on April 1, 2016, which should reduce goods processing times through the port. GOJ passed legislation recently relating to special economic zones that replace the traditional economic free zones, which were not compliant with the rules of the World Trade Organization.

- **Development Approvals.** GOJ is currently implementing the Application Management and Data Automation system (AMANDA), which will facilitate a faster, more efficient process of tracking of construction permits. Moreover, GOJ has prepared a programme of reforms to enable improvements to the Development Application Process, including provision for fast-tracking lower risks and smaller projects.

- **Resolving Insolvency.** GOJ has implemented the Insolvency Act, which seeks to amalgamate law relating to bankruptcy, insolvency, receiverships, provisional supervision and winding up. The law not only gives consideration to the rights of the creditor, but supports the rehabilitation of debtors and seek to preserve viable companies. More importantly, it helps to build a culture of encouraging entrepreneurship.

- **Electricity supply.** GOJ is taking action to reduce the time associated with the application and delivery of electricity permits by the Government Electricity Inspectorate and the time for installation by the power company.

- **Labour market reforms.** Jamaica passed legislation which will, *inter alia,* allow for the use of flexible working arrangements.

These actions have lifted the rank of Jamaica in the Doing Business Survey to 64 – the highest rank among BMCs - and along with other reforms, have set the stage for increased investment and sustained growth. Indeed, the impacts are already beginning to appear, as suggested by a number of indicators, including solid growth in gross capital formation (investment) in real terms during the last two years for which data is available (2013, 2014) in spite of lower capital expenditure by the public sector, sustained levels of foreign direct investment, and improvements in the external current account.

Conclusion

Low and volatile growth is no doubt linked to the high level of export concentration among BMCs. Moreover, exports largely reflect the exploitation of natural resources all BMCs. This reflects an inability to generate competitive advantages that would allow for greater diversification. Other small states have diversified their economies beyond the comparative advantages dictated by natural endowments, and have managed to generate relatively high sustained per capita GDP growth as a result.

If CDB's BMCs are to forestall losing their enviable position in the global development hierarchy, then efforts have to be made to improve competitiveness, especially those dimensions related to doing business. In this regard, Jamaica's experience provides important lessons, including the need for a systematic approach to improving the environment for doing business.

Economy		AB	BH	BD	BZ	DM	GD	GY	HT	JA	KN	SL	SV	SU	TT	RA	SG
Ease of Doing Business Rank		104	106	119	120	91	135	137	182	64	124	77	111	156	88	115	1
Starting a Business	Rank	107	118	100	159	63	76	92	188	9	90	67	77	183	72	100	10
	Procedures (number)	8	8	8	9	5	6	7	12	2	7	5	7	13	7		3
	Time (days)	21	28.5	18	43	12	15	18	97	3	18.5	11	10	84	11.5		2.5
	Cost (% of income per capita)	9.5	10.9	7.1	40.7	15	17.3	10.9	235.3	5	7.9	22.4	16.5	100.7	0.7		0.6
Dealing with Construction Permits	Rank	95	94	158	81	115	100	138	167	72	32	50	59	109	144		1
	Procedures (number)	16	16	9	15	10	13	7	12	17	10	14	14	10	16		10
	Time (days)	110	180	442	109	175	128	195	80	129.5	104	116	92	223	253		26
Getting Electricity	Rank	33	114	87	73	37	58	165	136	80	84	26	79	93	27	78	6
	Price of electricity (US cents per kWh)	44.5	39.4	22	22.3	36.5	29.8	29.3	35.7	28	30.4	36.8	30.1	7.2	7.2		11.3
Registering Property	Rank	118	183	134	128	165	139	125	179	122	170	104	160	176	151	147	17
	Procedures (number)	7	7	6	9	5	8	6	5	8	6	9	7	6	9		4
	Time (days)	39	122	118	60	42	32	75	312	18	82	17	38	106	77		4.5
Getting Credit	Rank	152	133	126	162	133	133	167	174	7	152	152	152	174	42	133	19
	Credit bureau coverage (% of adults)	0	0	0	0	0	0	2.4	0	22.4	0	0	0	0	69.6		58.6
Paying Taxes	Rank	161	24	99	69	98	132	117	143	146	147	83	97	75	114	108	5
	Payments (number per year)	57	19	28	29	37	42	35	47	37	39	35	36	30	39		6
	Time (hours per year)	207	58	237	147	117	140	256	184	358	203	110	108	199	210		83.5
	Total tax rate (% of profit)	41.9	33.7	34.7	31.1	37	45.3	32.3	40.3	35.2	49.7	34.7	38.6	27.9	32.2		18.4
	Profit tax (% of profit)	25.9	0	19.5	24.7	26.1	27.6	21.3	23.8	14.8	30.5	25.8	30.2	27.9	21.9		2
Trading Across Borders	Rank	114	97	127	117	61	138	139	76	146	70	72	68	77	114	101	41
	Time to export: Border compliance (hours)	85	36	41	96	19	101	72	30	82	3	11	28	84	60		12
	Cost to export: Border compliance (USD)	546	175	350	710	450	1,034	278	268	599	285	533	200	348	549		335
	Time to export: Documentary compliance (hours)	51	12	54	86	12	77	200	4	62	48	24	3	48	32		4
	Cost to export: Documentary compliance (USD)	121	260	109	125	50	40	178	48	314	150	63	80	40	250		37
	Time to import: Border compliance (hours)	85	51	104	48	39	37	84	91	106	37	27	48	48	78		35
	Cost to import: Border compliance (USD)	546	1,385	1,585	688	583	1,745	265	583	606	261	657	875	505	635		220
	Time to import: Documentary compliance (hours)	109	6	98	36	24	44	156	60	87	41	19	6	24	44		1
	Cost to import: Documentary compliance (USD)	132	140	246	75	50	50	163	150	331	150	98	90	40	250		37
Enforcing Contracts	Rank	19	60	164	133	83	89	87	123	107	42	67	31	186	167	97	1
	Time (days)	351	427	1340	892	681	688	581	530	655	578	635	394	1715	1340		150
Resolving Insolvency	Rank	125	61	34	81	129	189	156	189	35	189	109	189	128	67	120	27
	Recovery rate (cents on the dollar)	36	63.5	65.4	55	28.4	0	18.4	0	64.5	0	42.9	0	8.4	27.1		89.7
	Time (years)	3	3	1.8	2	4	np	3	np	1.1	np	2	np	5	2.5		0.8
	Strength of insolvency framework index (0-16)	5	6	11	5	6	0	5	0	11	0	5	0	9.5	11		8.5