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THE LIBERALIZATION OF THE FINANCIAL SECTOR

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On The Liberalization of the Financial Sector

I INTRODUCTION

Within recent years the issue of liberalization of trade and finance has taken a decidedly upward shift in terms of its importance in world economic affairs. The passage of the North American Free Trade Agreement, the signing of the General Agreement of Tariffs and Trade, as well as other free trade policies and programmes have enabled decision-makers to pay greater attention to their domestic economies in the context of a globalized, hegemonic system.

In the Caribbean, region decision-makers have been forced to play catch-up with the fall out of NAFTA, the downpour of GATT, the drenching of the European Community's policies, and they have started to position the regional economies or the edge of decision-making such that the region, too, may benefit from the largesse of the globalized market place in a free-market, liberalized scenario.

This paper will focus on the problems and prospects associated with liberalization of the financial sector in the Caribbean under three specific areas: (1) the management of the financial sector; (2) the management of the monetary sector and (3) the marshaling of resources to coordinate monetary and financial policy in a globalized and liberalized environment. Our concluding remarks will focus on the view that financial liberalization must be the way to go in an era of virtual reality, vis - a - vis the movement of funds across international borders.

II. THE MANAGEMENT OF THE FINANCIAL SECTOR

Problems

To appreciate the problems of liberalization we have to understand the current condition in the region. Even though the Common External Tariff (CET) has been made a reality in nearly all of the CARICOM countries, the region is still best described as one wherein its financial market is segmented, fractured and "repressed" in a McKinnon (1973) scheme. The banking system is still primitive, governments still dominate the financial system; funds are still obtainable at high -risk (junk - bonds) rate, and the equity market is narrow and woefully undercapitalized.

A closed market, one that does not permit a liberalized system, by its very nature, will be an inefficient functioning domestic finance market. The liberalized system is aimed at freeing up the trade and financial market. To date, however, only the trade side seems to be free. Cross-bordering trading, with Barbados, Jamaica, and Trinidad & Tobago, the CET and the other Tariff reduction have merely started to scratch the real problem of the economy. There is a problem here in that trade liberalization brings with it a focus on the systemic value of the real exchange rate. The effective real exchange rate in the region may hinder the attraction of funds to some sectors, depending on the profitability of the areas - and not on the goals and objective of the domestic economies.

The liberalized system means that governments should be able to borrow abroad to fund domestic projects. In fact, in the regional case where private capital flows are minuscule, it is to the advantage of the regional governments to seek funds in the liberalized financial environment. All things being equal, it would be useful to borrow the funds, make the appropriate rate of return, pay back the lenders and redirect the economic spectrum in the region.

The limiting factor here is the present viability of the countries in the region. The region, particularly the smaller groupingsof the region, has long been thought of as non-viable. It must be noted, though, that this view has waxed and waned over the years. The fact is, in a free-market, liberalized system, financial benefits freely identifiable are not easily obtainable. The justification to obtain funds may sometimes be in concordance with the lenders' perspective and in discordance with the desires of the borrows. In a liberalized system, there is a high degree of skewed perspective vis - a - vis the concordat between the lender and borrower.

Overall, when we view the Caribbean trading we see a region where liberalization is talked about, where nascent efforts are make to be update on the technicalities of the liberalization process, but we see a region that is still steeped in tradition. There is, at best, an unorganized financial market across the region. The segregated and disorganized market is both systemic. It is inter-countries and intra-countries. Some financial institutions have greater links with metropolitan, globalized financial institutions that with institutions next door. This extended link should minimize the down-side risk that the domestic economy has in accessing the international financial market. The reality is, however, the economies are not given any special privileges as a result of the link of local financial houses and international financial houses. The marginal cost of borrowing funds, therefore, is very high for governments.

Central Banks and other institutions in the region are put in very precarious positions. The money supply in the region has a direct link to the government's deficit position. Changes in the private sector trade balance also impact the supply of moneybut the government's component is the main variable. Finally, the equity markets which ought to move businesses from retained earnings and "mom - and power" financial sourcing, are not fully developed. Jamaica's equity market, the largest

the CARICOM region, has a number of problems that are closely linked to noise and manipulation in the market. Trinidad is a mere shadow of reality and Barbados stock exchange is ghost of reality.

Fundamentally, therefore, given these apparent attempts at equity markets, public sector debt in the region has to be forced on the banking system. In a liberalized system, the public sector and the private sector will be better able to mobilize resources to achieve economic growth.

Prospects:

The likely scenario of the management of the financial sector in the Caribbean entails a view of how we perceive the goals of the financial sector in a liberalized environment. Researchers at the Organization for Economic Co-operation and Development (OECD) and the World Bank contend that GATT's impact will add at least US$213 billion dollars a year to the world economy, starting at the turn of the century. The new trade rules, regulations and tariff cuts will, ceteris paribus, begin to impact on economies by the beginning of 1995 (next year) with the full force in effect by 1999 (five years from now.) (Crane, 1993).

What does this mean for the Caribbean? In this globalized environment it means that decision-makers in the region, broadly defined, have to, in a synergistic sense, begin to plan, further their plans, or maintain the integrity of their plans to ensure that the region accesses the finances that will devolve on the world economy as a result of liberalization.

Economic growth must be seen as the critical measure of economic performance. In this case, the role of finance assumes a considerable importance. Any

sustainable rate of growth, indeed any long-term viability of a country, depends on the rate at which it can secure finances and commit those funds to the growth perspectives of the country.

In a firm, the sources of funds are retained earnings, debt and new equity. In the Caribbean, narrowly conceived as CARICOM, equity creation is still in a nascent stage. It is imperative, therefore, that as decision-makers seek funds that they be even more vigilant about the rate of return and the risk profile on alternative products and projects. This rate of return and risk profile will determine the effectiveness, the critical importance, and the optimal strategy to put into effect to use the resources once they are obtained.

What are the prospects of obtaining new resources? What are the possibilities of accessing new and added funds? The prospects and possibilities, it appears, from a close reading of the globalized, liberalized system, depend on the effort of financial decision-makers. In a liberalized system, a free-market Adam Smith schema, if you will, financial decision-makers have to set their objectives and goals that will critically undergird the domestic objectives of the economy. In an interactive send, each economy is dependent on each other. However, a liberalized system is a win - win scenario with a positive-sum outcome.

Financial decision-makers, therefore, have to develop clear appreciation's of the workings of the international financial system and seek to recognize the shifting parameters relative to obtaining funds. Furthermore, they have to position the economies of the region along the continuum whereby the new paradigmatic shifts in funds mobilization are not all tied to social objectives, human rights or labor scenarios.

To be objective-oriented in the mobilization of finances from the

management point of view, means that the objective of the economies must be such that realistic, achievable, optimum investment strategies are to be delineated. For example, the region may want to set an objective of achieving a maximum return on its human investment while maintaining a high level of customer satisfaction, (a total quality management style), and while minimizing the impact of the brain-drain.

A series of goals in keeping with the objectives may be a 15 percent return on the human capital investment by the year 2,000, with a 15 percent reduction in customer complaints, and a 10 percent reduction in the brain-drain. Goals, fundamentally, are set with the view that if they are attained, they will contribute to the short and long term satisfaction of the economy - in a Herbert Simon ***satisficing schema.*** Paradoxically, therefore, the market for funds has to be managed, even though the new global reality revolves around the notion of liberalized trade and the liberalization of the financial process, attendant therewith.

The *liberalized financial system, which is a result of the parametric shifts* of the liberalized trade system, depicts a case where all countries are in competition. In this context where Adam Smith's *invisible hand is supposed to work, management of* the market is still a must. It is at this point that Caribbean financial decision-makers have to realize that they are no longer in a world of paradise, cocooned *in the reality of* yesteryear. What are the options? Two options are position.

Option one suggests that regional decision-makers muddle along in a typology where they hit and miss, with no plan. While they may not plan to fail, they may continue to fail to plan to make use of the information superhighway as it pertains to funds mobilization.

Option two suggests that they could aggressively set realistic objectives

and goals, within a framework of sustainable economic growth. Realistic objectives and goals will be tempered by historical reality. Sustainability will be functionally linked to the commitment, the depth of manpower and the creativity of the decision-makers in obtaining and managing funds for the betterment of the communities. In a nutshell, economic growth in a liberalized environment has to have a human face.

By management of finances we mean the training, skills, adroitness and inventiveness necessary to acquire and use funds to develop and sustain economic growth. Trade, in all of its perspectives, will have to be managed. Domestic trade, regional trade and world trade opportunities will have to be revised with a view of forging trade additionally and with the possibility of developing trade penetration.

In the liberalized system, trade additionally is the situation where a country is able to transform goods in multiple uses and trade them in ways from the normal and traditional forms. Trade penetration means the context where non-traditional markets are sought, or where market share is increased in traditional areas. It is to be borne in mind that this scenario always takes for granted that the liberalized system is a win-win case. Our paper is developing the plus on the Caribbean side. It is just as easy to develop the win side in the non-Caribbean context.

Management from the prospective side of liberalization of the financial process requires a great deal of negotiation for the available funds. Currently there are funds displacement from the Caribbean to those areas of the world which are coming in from the cold of communism.[1]

The Caribbean and other reduced - power areas have to seek to enhance and re-empower their economics by using the tools of the trade of negotiation. This

means that the financial decision-makers have to conduct the affairs of state to successful conclusions. As managers seek to guide the affairs of state to successful conclusion - here defined as sustained economic growth, history will either be the handmaiden or the handicap in the garnishing of funds. Our view is, however, that even though the region's power position has been reduced, the reduction is merely on a bilateral basis. Multilaterally, there is still ample power for financial decision-makers to orient their plans such that funds are obtained for the region.

What is the basis for this view? The basis for this view is dependent on the notion of the global reality. In a world of virtual reality, there cannot some free and some not free. When the balloon of reality is squeezed on one side, it bulges on another side. It cannot long last that some regions will always get and some regions will not get. What is distinctly possible is that some regions will continue to access the lion share of funds while some will, as a result of lowering political importance, get minuscule amounts. A classic example of this shifting power interests is the case of Eastern Europe "pro-free market" economies, and the "port -apartheid" South Africa. When a region is no longer newsworthy, funds diffuse to other regions. To stop this diffusion, regional decision-makers have to manage perceptions, manage their economies in a superior manner and manage the enabling international environment to maintain the spotlight of attention on the region. The rationale for this management strategy rests on the fact that the beneficial prospects deriving from a liberalized financial system are only as good as the efforts made to attain them.

II. THE MANAGEMENT OF THE MONETARY SECTOR

Problems

In considering the management of the monetary sector we will focus on the problems as they currently exist and the prospects of better or a different management under a liberalized system. Central to our discussion of the problems is our perception that the monetary sector in the region is, in many respects, too far removed from the real sector. Furthermore, the powers of monetary policy which are vested in the regional Central Banks are powers which, in spite of their gallant attempts of implicit policy coordination are powers which are set specific to individual countries.

In this regard monetary management in the Caribbean is a management that is, for the most part, reactive rather than pro-active. It is a policy that has substantial discretionary powers over the monetary sector but one that also conflicts at times with the dictates or the possibilities of the real sector. This bifurcation in policy thrust in the Caribbean stems, also, from the imperfect market structure.

Monetary policy which could focus on a bond/debt profile and keep in step governments' bonds at certain rates, has not always fulfilled that idea. Conventional theory would suggest that policy makers would assume that people would buy government bonds, given the inverse relationship between bond price and interest rate. If the rates are relative attractive, there will be a flight from bonds to money and from money to goods. This move invariably would lead to inflation. But, Central Banking policy with its open market operations, has the potential of mitigating the many episodes of inflation likely when there is a flight from money to goods.

In the Caribbean, however, even though the Central Banks have

substantial discretionary power over monetary policy, the practice has been that the monetary policy complimentary factor does not always work alongside the real sector management. When there is any flight, it is normally capital flight out of the country to havens where it is presumed, capital could be cordon-off from the vagaries of the market.

Fundamentally, monetary policy management in the Caribbean appears to have adopted some semblance of the policy that the USA Federal Reserve (Central Bank) started in the 1950's, namely "leaning against the wind." In essence, when the Board of Governors detect inflationary threats, they drive up interest rates, and economic growth is slowed down. This is the prevailing sentiment with USA today, under the Greenspan's era.

In the Caribbean, the regional monetary policy seems to be operational on two fundamental fronts: a direction policy relative to the domestic economy, and a reactive policy relative to the international economy. The substance of this is that there is a two-pronged approach to monetary policy management in the region. Sometimes there two prongs
could have counteracting effects.

The specific management problem here centers on the limitations of monetary policy in the region, circumscribed as it is to lag developments in the international monetary sector. In this lag relationship, policy-makers are forced to tip their policy thrust in the international sphere. This is the sphere which it is perceived as more secure, stronger, and less subject to vagaries that will be detrimental to the domestic economies. As has been demonstrated in the USA, sometimes leaning against the wind, may be leaning into the wind. In this regard the question is whether monetary policy, as articulated by Central Banks, follow the economy or leads the

economy. In the Caribbean the fiscal sector has been the prima donna for so long that, substantively, the economies lead the money policy and not the other way around.

To compound the problem in the Caribbean, there is no binding treaty, policy or arrangement that flows from the CARICOM into the monetary sector thereby leading to a common currency or a common Central Bank. The Maastrich Treaty of 1991 included plans for the transformation of the European Monetary System into a full-fledged monetary union. To many this was seen as an important step toward the economic integration of the European community. In many respects CARICOM has moved some ways towards economic integration. But, like the Maastrich Treaty demonstrated for Europe, events in the foreign - exchange markets can severely hamper the viability of a Pan - Caribbean currency and Pan - Caribbean monetary policy.

The current monetary policy attempts to highlight the compatibility among the countries. However, there is no real exchange stability among the countries. Exchange rate variability will continue in this market structure where a perfect market exists. Furthermore, as the exchange instabilities persist, there will always be the pressures for devaluations given the different economic production platform of the different countries.

Monetary policy in the Caribbean is best understood in the concept that was ably expounded by E.B.A. St. Cyr (1992): "On account of both historical and structural considerations, there is close affinity between money and foreign exchange in (the) Caribbean economy." (St. Cyr, 1992: 97). In this scenario it is clear that many of the problems of monetary policy management not only having a timing and sequence issue, but also have institutional rigidities which handicap the smooth functioning of the

policy. Thus, as St. Cyr (1992: 109) notes 'Given the size, structure and institutional configuration of Caribbean economies and the social orientation of (Caribbean) peoples, there appears to be an inherent tendency towards exchange rate depreciation, and persistent fiscal deficits appear to be a major contributor to this (problem)." Compounding the problem, St. Cyr (1992: 109-110) contends,

> Deficit financing constitutes an attempt by the state to commandeer more real resources than the public sector revenues warrant and ipso facto increases the quantity of money chasing after an unchanged flow of goods and services. This spills over into import demand with adverse consequences for the balance of payments and the exchange rate.

St. Cyr concludes that the regional governments should subject themselves to a higher moral authority as they seek to manage monetary policy as that policy impacts on the real sector, through price stability and the exchange rate.

Prospects

Sr. Cyr's arguments are solid in the context of managing the system without considering radical surgery. If radical surgery is to be instituted, then liberalization offers that choice. Under liberalization the prospects of monetary management have the possibility of assuming a greater role relative to economic growth in the region.

Liberalization of the system goes against the grain of some of the institutional, historical and other features that are endemic to the region. Furthermore,

liberalization is not necessarily the panacea, if it is merely patched onto the existing conventions. Karl Bennet (1993) has demonstrated that, in the context of Jamaica, liberalization which was earmarked to stabilize the foreign exchange regime, produced, instead, a system of hemorrhaging in the foreign exchange market. While some public and private sector initiatives provided a breathing room in exchange rate stability, Bennet (1993: 91-92) concluded that "the act of liberalization of the (foreign exchange) regime cannot in and of itself eliminate a chronic shortage of foreign exchange in the short run." Furthermore, "The Government in liberalizing the system must concurrently formulate a policy for managing the exchange rate. Such a policy, if it is to be effective, must be formulated in close collaboration with the institutions responsible for administering the market."

In this context of the prospects of management of the monetary sector in a liberalized environment, the issue is what criteria should decision-makers consider, among the alternative courses of action? Fundamentally, the choice of the appropriate decision criteria hinges on the salience of the importance of liberalization and the objective we have stated as the achievable goal. The principal objective, it must be reiterated, is to orient the economy to provide sufficient real economic growth to sustain economic development, maintain employment and hence the standard of living of the people of the region.

A liberalized monetary system puts the region in short-run and long-run scenarios such that access to the international and regional debt and equity markets would be widened. The widening of these markets would enable regional monetary decision-makers to be more intimately interlocked, on a real-time basis, with the international capital markets. While some of this already exists, the prospects of a liberalized monetary policy opens the regional economies to a larger matrix such that

local financial houses and other banking institutions can now internationalize and restructure their portfolio.

Today, international banking and, ***parri passu,*** international monetary policies are virtual reality. The on-line expediencies of moving funds from the back street to main street are now more real than was once envisioned. Commensurate with this virtual reality in monetary management is the necessity for monetary policy to be open, free, liberalized. Indeed, the centrality of liberalization is that crises in the international system could be anticipated, minimized and alleviated. This almost prescient action also opens up the economies, internationally, to an interlocking, dependent scenario. With this dependency comes a great down-side when policies go awry. By the same token, the liberalized system permits greater degrees whereby problems could be anticipated and controls imposed prior to a breakdown of the system.

One of the strong cases for the prospects of adopting a liberalized monetary policy in the Caribbean, is the nature of the economy. The Caribbean economy is an open economy. Historically, economic policies have been implemented as if the economy was a closed economy. Parenthetically while the open economy and its attendant features were recognized, the praxis of the policies were operationalized along a closed - economy type model.

A liberalized monetary policy in the Caribbean will not be immune from shocks of the international market. But, whereas the current old system is inherently susceptible to the vagaries of the international market, the new liberalized system, as proposed, will be a full part of the internationalized monetary system. The advantage of this liberalized system is clear because the system offers opportunities for decision-makers to access the international money market at open, competitive rates, and not at

the old type of money-market rates where premiums are charged for knowledge, and where information relative to the mobilization of funds is often limited to a few countries.

In the liberalized monetary system, sovereign countries have to surrender some autonomy of their national policies. This surrender of autonomy is merely a policy strategy and not a political surrender. When a liberalized system is in place, exchange rates are easily accommodated to the divergent exchange rate policies of the various countries. Such would be the prospects in the Caribbean, were a liberalized system to be fully in vogue.

Finally, and perhaps paradoxically, a liberalized monetary system has prospects that the central banking may best be operationalized as an independent management strategy. Cental Banks, if fully operational in a liberalized system, will have to have a certain degree of independence that is above what currently obtains in the region. There will be a need for the Central Banks to be independent of governmental dictates because the Banks will be fully part of the international monetary system. In the current system, while regional central banking could be seen as within the system, the international system need not be responsive to the regional system. In a true liberalized system, all systems are, by the very nature nature of the model, linked.

In a liberalized environment, central banking policy is cannot fully depend on governmental dictates. In such an environment political rules and regulations do not direct policies according to political expediency. Economic and financial reality assume greater importance. Increasingly, countries that have chosen the paths of liberalized environment, such as New Zealand, Chile and Israel, have discovered that in a liberalized environment, static rules and regulations vis-a-vis monetary policy cannot last long where the liberalized market is concerned.

IV THE MARSHALING OF RESOURCES TO COORDINATE MONETARY AND FINANCIAL POLICIES

Over the years, the merger of politics and economics in the Caribbean has led to statist policies which were reflective of personalities who made up the governments, and not really reflective of of the fundamental requirements of the economies. Admittedly, there is a fine line between the statist policies and the personalities in the state sector. Within recent years, as the political winds of change shifted from the command economies to a liberalized economies, the attendant monetary and financial policies moved step-by-step to accommodate the developments in the political and economic arena.

Jenkins and Sisk (1993) in their volume, ***Development By Consent (The Voluntary Supply of Public Goods and Services)***, imply that development of any country is possible if there is an expanding consensus of actions of the people. There is merit in this view. In recent years, the surging tides of international liberalism has fostered an external decision-making that is bound with the syndrome of hegemonic politics. Arising from this new hegemony is a policy oriented to liberalization in trade, finance, and all features which are bereft of minimal governmental interference, or no governmental intrusion.

In our perspective, the liberalization of the financial system in the Caribbean has to be part of the new hegemonic order, because the new dispensation of benefits derivable therefrom are best operationalized if region takes part fully.A corollary to this view is this: in the new system, we perceive of the marshaling of resources of the monetary and financial sector as the critical lynch-pin for development.

Financial liberalization is the popular buzz-word today. Our view is that liberalization has to be put in the context of the marshaling of the resources to enable a coordination of resources. The coordination is aimed, specifically, at minimizing waste,

eliminating the duplication of efforts, and in the final analysis , benefiting from efficiencies associated with scale economies. This thrust at marshaling of resources is our reflection of the developmental trajectories as far as today's capital market is concerned. Steve H. Hanke and Alan A. Waters (1991) demonstrate that capital markets were not always critical in the development trajectories of countries. Throughout much of the nineteenth century when the United States of America and much of the so-called developed countries were growing, Central Banks were the exception and appreciating currencies were the rule. Today, however, Central Banks are the rule and appreciating currencies are rare.

What this suggests is that debt and equity instruments which did not exist several years ago, and which were not necessary for development, are today pivotal in marshaling funds for the development process. These new funds have integral linkages of the monetary and financial portfolios. In a liberalized world, such as we are contending is necessary for the Caribbean, new debt and equity instruments will obviate themselves. These new instruments, however, bring with them risks and promises. Let us consider three of the risks.

Risks Of Coordinated Monetary And Financial Policy

The risks of forging a monetary and financial policy in a liberalized environment is a risk that has to be weighted by the Central Banks, the public sector and the private sector. In a liberalized system, these three "distinct" yet integral agents of change will be subjected to three types of risks. These will be ***contemporaneous risk, operational risk and market risk.***

By ***contemporaneous risk*** we mean that type of risk associated with the public sector or the private sector and the negative impact that is likely from a default of

a contemporary with whom debt/equity arrangements have been made.

Since a liberalized environment will open the market to possibilities of joint money and financial policy initiatives, it is conceivable that there could be contemporaneous risk. It is essential, therefore, that project evaluations be sound, that creditworthiness be fully ascertained, and that, even in a liberalized environment, resources be devoted to meshing the monetary and financial policies at a level that is compatible.[2]

Operational risk refers to risk linked to the monitoring, controlling and minimizing of risk associated with employees performance in the securing and or sequestering of funds. Sometimes agencies of governments or the private sector move slowly or haphazardly thereby losing benefits derivable from a project. The speed required to accomplish a task, or the speed of adjustment needed to achieve a given goal is not always appreciated in our part of the world when it comes to minimizing late fee payments or benefiting from early payments. For example, too often, in our part of the world, a business negotiates with government and invoices the government for some service, ***net thirty days. If a 40 percent is given, it means that if the bill is paid in thirty days, the benefit will accrue to government, and hence to the economy.*** Shipping and handling charges or transaction costs or some balloon-payments may not be part of this 40 percent. Nevertheless, the oft-practised style is for the government not to pay within the net the thirty day period. The public sector often times fails to pay because there is normally little or no coordination of the monetary and financial sectors to marshal resources to benefit from the discount.

Operational risk suggests that the operative characteristics of the region have to change in a liberalized environment. In a liberalized environment, time is truly money. Inefficiency is really a cost. A liberalized environment is geared to minimize

inefficiency, and oriented to maximize efficiency and effectiveness.

The last risk is market risk. ***Market risk*** is that type of risk associated with the three principal concerns of banks, namely liquidity, profitability and safety. In a liberalized environment, where monetary and financial policies are hypothesized to operate synchronously, market risk will develop if there is too much market exposure, too much uncertainty relative to liquidity available, and where sequencing and timing are problems.

Market exposure in this context pertains to how much a country will give up to another country or financial institution to obtain capital. Market exposure could also mean the level of primary or secondary mortgage an institution, business or country will endure to raise capital. In a liberalized system where conditionalities may not be as severe to obtain capital, there could be great risk exposure. This risk exposure is comparable to an individual expanding a line of credit with a bank or a credit card company, maintaining a running balance, but paying the monthly minimal balance. In due course, the risk exposure will impair the individual's creditworthiness if efforts are not made to reduce the exposure.

Liquidity risk in the market risk category refers to the type of risk associated with a country securing a loan on the international capital market, but where the draw-down facilities are blocked or altered because counterpart country funds are not available. This may be a case of timing from a cash-flow perspective. Cash-flow problems can severely handicap projects in any system. In a system where the monetary and financial policies are to be coordinated to efficiently marshal resources, cash-flow problems can de deleterious to development.

Finally, market risk associated with timing and sequencing may stem from a scenario where funds are secured from the international market under a a liberalized regime, but where the local fiscal office changes the flow of funds to the projects on a

basis that is different from what was negotiated. Another scenario could be the case where agencies of government are allotted funds in a budgetary scenario, but where the Office of Management and Budget allocates less that what was allotted or changes the disbursement cycle and the dispensations to the agencies. When timing and sequencing are changed to fit domestic policy dictates, funds which are negotiated internationally could be neutered as a result of the intricacies of political machinations. In this case market risk of timing and sequencing looms large.

Promises of Marshaling Resources of Monetary and Financial Systems

The promises of marshaling resources to coordinate monetary and financial policies in a liberalized environment are linked to today's technological space. There is a great deal of technological advance, today, which makes it easy for countries to access the international market. It is easier to access funds that it was before, it is more efficient, and it offers more scope. There is more risk too. Recently there have been many risks as result of misuse and abuse of the international money market via technological mismanagement. Some recent technological misuse and abuse are the massive failures of the USA Savings and Loans, the debacle of the Bank of Credit and Commerce International (BCCI), the mammoth melt-down of financial institutions associated with financial derivatives, (for instance the case of the USA subsidiary of of the German conglomerate ***Mettallgesellschaft AG,*** which lost $1.8 billion in oil futures and forward contracts, and ***Showa Shell, the Japanese affiliate of Royal Dutch/Shell***, which wiped out 82 percent of shareholders equity by taking a $6 billion position in yen/dollar futures, effectively betting five dollars for every dollar they hedged).

In many respects, the principal determinant of economic growth in today's liberalized environment is technological advance. The maintenance of a work

force with adequate skills, and the acquisition of technology to maintain those skills will lead to economic scale and scope in output. Technology, therefore, has become the fulcrum of development as countries shift from the old regulated system to a new liberalized system. In financial and monetary terms the speed with with a country can access funds and absorb those funds will have a negative or positive impact on the growth trajectory of the country.

Size, whichever way it is defined, has never been truly put in an empirical shape to state, unequivocally, that viability is constrained by size. In a liberalized system, size is not a constraint to survival; size is not a constraint to viability; size is not a constraint to credit-worthiness. In a liberalized system, a country's ability to negotiate, to sequester and to secure funds, by whatever means the market permits, are the critical factors in the marshaling of resources. The promises of a liberalized environment are of tremendous importance. Small countries such as those in the Caribbean would not necessarily have to be left out in the cold. This means, however, that countries cannot operate under quotas and protective clauses; they will now have to fend for themselves, as the market mechanisms dictate. There will be imperfections in the market. These imperfections must be minimized, in the limit, if all countries and all users of the capital market face the same risk profile.

In the system of which we speak, Central Banks will be international banks. They will have to usurp some of the roles of the public sector in the international funds market. Commercial banks will, also, have to usurp some of the roles of Central Banks, to the extent that the control of the money supply is a seen as a default role in a liberalized system. In some respects, Central Banks independence will make them competitive with commercial banks, in some respects. The mere control of the money supply will not be the only issue of centrality to Central Banks.

In the liberalized system that we are describing, there will be a need for

greater independence of the Central Banks primarily because Central Banks now reflect power surges in central bank policy dependent upon who are the personalities in charge, who are the governments in power, and sometimes what the nature of the economic system demands or requires. This is not to suggest that nothing good comes from the Central Banks and their policy. It merely suggests that in a liberalized system, political interference, real or perceived, would have to be minimized if the domestic economies are to benefit from the substance of liberalization. In the Caribbean, there is a tendency for institutions, and some decision-makers in the private and public sector, to adopt an imitative culture in terms of what they think is happening elsewhere. Too often the what is adopted is the dead-end of the policy, and the how to adopt the what is not clear. The net result of this partial equilibrium approach to policy suggests fact that too often regional decision-makers fail to position the economies on the cutting edge of change.

It should be deduced from what has been presented, thus far, that liberalization of the financial sector is not a nice, smooth, differentiable function. There are asymmetrical problems and corner solutions in the liberalization of the financial sector. These anomalies in the system, notwithstanding, are merely imbalances which would tend to be minimized over time. If the liberalized financial system works, as it is expected to work, then the system trend upwards and permit a leveling up process. By this we mean that the pace of development associated with a liberalized system, and specifically a liberalized financial process, is a pace that would, ceteris paribus, improve the body economic of those systems over time. In our instance, sustained economic growth is one of the hallmarks of the liberalized financial system.

The acceptable features of this system suggest that rules will have to set up to measure the performance of the system. Dysfunctional activities that will jeopardize the system will have to eliminated. Strict efforts will have to be put into effect

to marshal the forces of monetary and financial policy. The efforts will be needed such that the synergistic effect due to the workings of the two systems, will redound to the economies andultimately to the people.

There will be costs to move from the old system to the new system. Apart from the fact that the new system will come, whether we like it or not, it seems only reasonable that the taxpayers pay for the implementation of the new liberalized system. In the cases of GATT, CBI and the new CET, the cost to the region will be experienced in the reduction of taxes. This tax reduction, or elimination will have positive impacts on businesses and the government. There is, however, the possibility that there will be short-rub dislocations and distortions as the liberalized system is put into effect. These are costs that have to be kept in mind.

In the final analysis, the problems of the old system and, the problems of the new system of liberalization will offset each other, in the long run. The benefits of the new system will outweigh the benefits of the old system in the short and long run. We stress the need to have policy coordination of the monetary and financial sector to enable the countries in question to benefit from the economies of scale . The synergism that is also possible for the interaction of both types of policies is a synergism that is dynamic in nature and not static in scope.

CONCLUSION

In this paper on the liberalization of the financial system, our focus has been on an evaluation of the problems, risks, prospects and opportunities in the liberalization of the system in the Caribbean, as opposed to keeping an old system of rules and regulations in an imperfect system. Out conclusion is that, on balance, the financial of the system is best understood when it is appreciated that the new

liberalization as it relates to the new free market and hegemonic tariff-reducing systems is here to stay. If that view is tractable, then the decision-makers in the Caribbean have to get on the cutting edge of the process and ensure that they, too, participate in the process for the benefits that are derivable. There are risks associated with the system. However, the risks of the liberalized system outweigh the risks and problems of the old ***in situ*** situation.

Money and finance are central in this new liberalized system because the world economy is today fundamental a financial services economy. From Wall Street to the Jamaican Stock Exchange, from the Mexican Bolsa to the Paris Bourse, financial money management is of preeminence. The liberalized market offers the opportunities for small states to access that financial system. It is out view that in a liberalized system, the negatives of a small economy are not as deleterious as the negatives of a regulated, information-managed system.

There is an intense usage of economics in the financial system and that intensity has a direct bearing on the the economics of institutions, individuals and economies. Sometimes, as in the case of the disruption of the European Exchange Rate Mechanism in September, 1992, liquidity crises can negatively impact on countries, economies and regions. Money and finance in this liberalized system have been forged ahead by wide areas of technological developments. Mathematical theories, statistical theorems and computer systems are now part of the money and financial landscape. Regional decision-makers should seek o benefit from the liberalized system. In this system, time, knowledge and novelty are awarded benefits. The decision-makers have to position the economies on the cutting edge of change to ensure that the regional economies are not left out in the cold of indecision and lethargy, now that other countries are coming in from the cold of communism and central planning.

In liberalized system where money and finance are preeminent, the old system of looking at macroeconomics and monetary economics, or money and banking and interest rates, are necessary but not sufficient. Decision-makers now have to pay more attention to financial economics, financial markets, debt and equity markets, financial institutions, corporate finance and government's role in accessing international funds.[3] In the Caribbean there is a great deal of talk about the equity market but there are only three small attempts at equity markets, it is imperative that the decision-makers begin to have some working knowledge of well-known landmarks in the field of finance. This is not to suggest that all decision-makers know all of the differential equations associated with the Modigliani-Miller theorem on corporate finance or the Black-Scholes formula in options pricing, or all of the intricacies of random walk. They should, however, have a working knowledge of some of these ideas and be able to either utilize the essence of some of the ideas or avoid being slaughtered by someone who would set about to mesmerize or delude a country in the process. The problems with derivatives, even at the level of large financial institutions, are worthy of advice such that regional decision-makers take advice.

In the final analysis, the liberalization of the financial sector in the Caribbean could be as strong or as weak as decision-makers desire. From our discussion in this paper we are of the view that region should consider three institutional strategies in ensuring that the liberalization process benefits the region.

First, there should be a centralized supervisory agency, say in CARICOM or the Association of Caribbean States, whose purpose is to monitor the international markets to secure funds at competitive rates for the region. This idea is comparable to a situation where there is a clearing-house for grants and where there is an agency that

monitors requests for proposals to get the grants. In the region's case, it will be a agency which will be able to access the financial markets to seek capital at acceptable market rates. With the information superhighway, this is a reality. CD-ROMS, America On Line, Compuserve and Internet now provide this kind of information to those who need and can pay for it.

Second, there should be a greater harmonization of regional economic policies as those policies are linked to monetary and financial strategies and domestic development. This suggests that a clearer organization in economic strategies should evident in the region. Clearer monetary policies should be observable. Greater harmonization of a monetary policy from common precepts of a common currency and common central banking polices are necessary.

Finally, while not negating the second option, the individual countries should develop greater capacity to structure their domestic economies to penetrate and access the international liberalized markets, where it may be more expedient to penetrate and access on the individual basis than on the group basis.

A liberalized financial system assumes that all economies are equal in a market-sense. While this is not demonstrably false, in small countries there is synergy to be obtained from shared knowledge. The level of financial liberalization will vary from country to country. We have argued in this paper, however, that the heuristic evidence suggests that financial liberalization will have more sustaining economic benefits than a non-liberalized system. Some regional economies have attempted variants of liberalization. None has gone the full route of the liberalization of the monetary and financial system. The time is right for a such a move.

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