CARIBBEAN CENTRE FOR MONETARY STUDIES

PRESENTATIONS

XXXV ANNUAL CONFERENCE OF MONETARY STUDIES

THE FTAA AND THE FINANCIAL SERVICES IN THE CARIBBEAN: ISSUES AND PROSPECTS

By

Dr Lester Henry
Department of Economics
University of the West Indies, St Augustine, Trinidad

24-28 November 2003

Sir Cecil Jacobs Auditorium
Eastern Caribbean Central Bank
Basseterre
St Kitts

THEME:
Economic Reform:
Towards A Programme For The Resuscitation of Economic Growth And Development In The Caribbean

The FTAA and the Financial Services Sector in the Caribbean: Issues and Prospects

By

Lester Henry
Department of Economics,
University of the West Indies, St. Augustine

Presented at the XXXV Annual Conference of Monetary Studies
Basseterre, St. Kitts
November 24-28th, 2003

Abstract: This paper examines some of the critical issues facing the financial services sector in the Caribbean in the context of the Free Trade Area of the Americas (FTAA) that is due to become effective in less than 2 years. Generally, it is argued that the CARICOM region has been slow in addressing the potential impact of the FTAA on the financial services sector. Further, it is suggested that due to the weak regulatory environment in the region the adjustments required for FTAA readiness may be quite onerous in some countries. First, Section 1 introduces the issue and places the FTAA in a context of forum shopping. Second, a brief review of the pros and cons of financial liberalization in developing countries is presented. Third, a brief overview of the structure of the financial services sector in the region is presented. This is followed by a survey and assessment of some of the key liberalization issues in the FTAA process. In particular, the recently tabled US proposal on financial services liberalization is discussed. The regulatory and competitive environment for financial services in the region is examined. Finally, Section 5 summarizes with some policy implications.

1. Introduction

This paper examines the challenges facing the financial sector over the next several years due to developments in the FTAA. This issue is important because "financial services are at the nexus of savings and accumulation mechanism that drives economic growth"[Francois and Schuknecht, 1999]. In this regard, a vibrant and successful indigenous financial sector is critical for economic development. Even though there has been some measure of success among certain regional financial institutions, recent developments, however, may pose a threat to their profitability if not their survival. Further, will the policy changes resulting from the FTAA result in bigger banks from North America buying up much smaller regional banks? Increased competition and transparency requirements may prove to quite challenging to regional financial institutions.

The FTAA should be of concern to regional economists because of the far reaching nature of its proposals. It also represents one of the main forums in which the United States is attempting to spread its free-market liberalization dogma, while protecting its agricultural base. The US has been one of the practitioners of "forum shopping": What they cannot get in the wider World Trade Organization forum (WTO) forum it hopes to achieve in the FTAA. Even if this fails, they then fall back to Bilateral Trade Agreement (BTAs) with smaller nations. So as they move from one forum to the next they increase the chances of getting their agenda through.

There is very little available work on the issue of financial services in the FTAA from Caribbean perspective. This paper attempts to address this imbalance. Section 2 reviews some of the literature on the effects of financial liberalization in developing countries in terms of intermediation costs, competition, profits and economic growth. Section 3 provides a brief overview of the financial services industry in the Caribbean. Primary focus is on the banking, insurance, and offshore sectors since these are the most important for the region. Section 4 discusses some of the key areas of concern for the Caribbean in the context of the FTAA. Finally, Section 5 summarizes the main issues.

2. Liberalization of Financial Services in Developing Countries: Pros and Cons

Defining Financial Services

According to the WTO, the term financial services encompasses two main categories of services: (1) Banking and other financial services and (2) Insurance and insurance-related services. However, there is also a somewhat vibrant offshore banking sector within the region. Insurance and insurance-related services cover life and non-life insurance, reinsurance, insurance intermediation such as brokerage and agency services, and services auxiliary to insurance such as consultancy and actuarial services. While, banking services includes all the traditional services provided by banks such as acceptance of deposits, lending of all types, and payment and money transmission services. Other financial services include trading in foreign exchange, derivatives and all kinds of securities, securities underwriting, money broking, asset management, settlement and clearing services, provision and transfer of financial information, and advisory and other auxiliary financial services.

The Benefits of Financial Services Liberalization

The basic idea of financial services liberalization in the FTAA is not much different from that of the WTO. The FTAA, however, extends deeper into the internal economic affairs of its members since it really goes beyond a traditional Free Trade Agreement. Nevertheless, The standard view, according to the mainstream literature, is that liberalization of financial services can benefit developing countries in a number of ways, these include:

- Allowing the presence of foreign financial institutions which can result in:
    - Less distorted and volatile capital flows
    - Increased diversity to consumers and investors
    - Increased their local lending relative to domestically owned institutions in periods of crises
    - Lower financing costs and new investment and savings vehicles

- Efficient and productive allocation of foreign and domestic savings
- Encourage innovation in the latest technologies and products, and enhanced financial market development and stability
- Access to financial advisory services
- In the area of insurance, shared risk and facilitate trade
- Ambitious commitments for financial services help attract financial service providers, which in turn make countries more attractive destinations for investment in e-commerce networks and associated technologies
- New markets and increased demand for computer-related services since banks, insurance companies and securities firms rely very heavily upon specialized software and have high data processing needs
- Growth and access to new technologies
- Job creation

In recent times, there have been a number of empirical studies, mainly emanating from economists at the World Bank, attempting to verify these results. For example, Llaeven (2002,p.4) supports the view that "financial development reduces informational asymmetries in financial markets which leads to an improvement in the allocation of capital and ultimately to a higher level of growth". Clarke *et al*. (2001) cites a cross sectional study of 80 developing countries which finds that the presence of foreign banks increases competition and improves stability. They also use evidence from a survey of over 4,000 enterprises in 38 developing and transition economies to conclude that bank lending to firms of all sizes improves with the presence of foreign banks. Furthermore, Francois and Eschenbach (2002), uses cross-country regressions on data for 130 countries in the 1990s, and finds that there is a strong positive relationship between financial sector competition and financial sector openness, and between growth and financial sector competition.

Costs of Financial Services Liberalization

There are still concerns however, that financial liberalization can lead to financial instability, currency crises, and an erosion of domestic control over the financial sector (Grabel, 1995). For example, Fry (1997) argues in favor of financial liberalization but warns that certain prerequisites must be in place, such as: (1) "adequate and prudential supervision of commercial banks, (2) a reasonable degree of price stability, (3) fiscal discipline (4) profit maximizing, competitive behavior by the commercial banks, and (5) a tax system that does not impose discriminatory explicit or implicit taxes on financial intermediation". Without these, the above benefits may remain illusive. Further, if a country was financially repressed then liberalization can result in higher interest rates that may decrease investment and hence, hinder economic growth. Capital flight may also occur if there is instability.

3. Overview of the Financial Services Industry in CARICOM

The financial sector in the Caribbean has operated traditionally in an environment characterized by the following:

"(a) the high degree of concentration of firms in virtually all segments of the region's financial sectors;

(b) the relative smallness, fragmentation and inherent fragility of Caribbean economies and their financial markets;

(c) the pronounced presence of indigenous financial firms, and past policies which resulted in foreign firms being relatively less aggressive in the Caribbean; and

(d) the region's commitment to a single market economy."[1]

Commercial Banks

Firstly, regional commercial banks generally have high operating costs. There also tends to be a high degree of concentration, that is, in most countries, a few banks control large market shares. Further, very often they exhibit cartel like behavior and engage only in non-price competition. There is also the practice of having a large number of branches that act as a deterrent to new market entrants. In recent years, there has been a move toward consolidation across borders in the region with banks and insurance companies merging or smaller firms being bought out by larger rivals. A broad

[1] Caribbean Group for Cooperation in Economic Development (1998), "Wider Caribbean Financial Sectoral Review: Increasing Competitiveness and Financial Resource Management for Economic Growth." Report No. 17556-LAC, World Bank and the Caribbean Centre for Monetary Studies, May.

picture of the financial sector in the region is presented in Table 1. A detailed structure of the commercial banking sector is presented in [Henry, 2003].

Table 1
Main Financial Intermediaries within CARICOM

Regulatory	Financial Institutions	Non-Bank-Financial Institutions (NFIs)	Other Financial Institutions
1 Ministry of Finance 2 Central Bank	Commercial Banks-foreign & indigenous	1 Finance Companies & Merchant Banks 2 Trust & Mortgage Companies	1 Insurance Companies 2 Credit Unions & Cooperative Societies 3 Building Societies 4 Development Banks 5 Securities Exchange 6 Mutual Funds/Unit Trusts 7 Hire Purchase Firms

Apart from Trinidad and Tobago there is a high concentration of foreign ownership of commercial banks, suggesting that the sector is relatively open [Henry, 2003]. In Jamaica, for example, the financial crisis of the 1990s and subsequent government intervention has resulted in the situation where "as at September 2002, there were six commercial banks with a network of 121 branches operating throughout the country. All but one of the commercial banks is foreign owned. The lone Jamaican owned commercial bank accounted for a mere 2.0 percent of all commercial bank assets as at June 2002. This compares with a year earlier when three such entities accounted for 52.0 percent of all commercial bank assets"[2].

On the other side of this is Trinidad and Tobago where all the major retail banks are largely locally owned. In fact the two largest banks, RBTT and Republic which have 100 percent local ownership, accounted for 74 percent of interest income in 2001 (Figure 1). This illustrates the high concentration ratio that is common in the region.

Table 2 provides further details of the financial market structure in the Caribbean. In most cases, where data was available, the number of firms in 2002 was less than in the year 1997.

Further evidence of the noncompetitive behavior of Caribbean banks is observed by looking at the high loan rates that prevail along with low deposit rates. This has persisted over the years as is seen in Table 3. The banks have been able to maintain large interest rate spreads even during conditions of excess liquidity. In the mid-1990s the spread peaked at 22 percent in Jamaica and then began to narrow toward what seems to

[2] Bank of Jamaica, Economic Information & Publications Dept.

be the CARICOM norm of around 7 and 8 percent. In Guyana, Belize and Suriname, however, the spread remains in double digits indicating a tendency towards oligopolistic or non-competitive pricing behavior in these countries.

Table 2
Financial Structure in CARICOM By Number of Firms

COUNTRY	Commercial Banks		Offshore Banks		Finance Companies		Merchant Banks	
	1997	2002	1997	2002	1997	2002	1997	2002
BAHAMAS	10	8	309	173	na		na	
BARBADOS	7	6	30	56	4		-	
BELIZE	4	5	-	4	2		-	
GUYANA	7	7	-		1		-	
JAMAICA	11	6	-		4		25	
OECS	25	45	43		na		-	
SURINAME	6	5	-		6		-	
TRINIDAD & TOBAGO	6	6	-		10	5	6	5

COUNTRY	Trust Companies				Development Banks		Credit Union	
	1997	2002			1997	2002	1997	2002
BAHAMAS	99				1		10	
BARBADOS	4				1		47	
BELIZE	80				2	1	21	15
GUYANA	2				1		na	
JAMAICA	1				4	7	87	56
OECS	Na				7		74	
SURINAME	-				1		27	
TRINIDAD & TOBAGO	6	2			2	2	161	112

COUNTRY	Stock Exchange		Insurance Companies		Thrift Organizations		Unit Trust Companies	
	1997	2002	1997	2002	1997	2002	1997	2002
BAHAMAS	1		128		1		-	
BARBADOS	1	1	27		-		-	
BELIZE	-		20	17	1		-	1
GUYANA	-		11		1		-	
JAMAICA	1	1	11		15		4	4
OECS	-		185		na		na	
SURINAME	1		12		na		na	
TRINIDAD & TOBAGO	1	1	43	31	4		1	1

n.a. not available **Source: Updated from Borne et al (1998)**

Table 3
Commercial Bank Interest Rate Spreads

	Actual										
Countries	**1991**	**1992**	**1993**	**1994**	**1995**	**1996**	**1997**	**1998**	**1999**	**2000**	**2001**
Bahamas	8.2	9.2	9.7	9.7	8.5	7.4	7.8	7.3	7.5	7.9	7.3
Barbados	7.5	7.6	8.4	6.9	6.8	6.9	6.9	6.4	6.5	7.1	7.6
Belize	7.9	8.4	8.6	8.9	9.1	10.0	9.9	10.3	10.5	10.8	11.1
EC Currency Union	6.7	7.7	7.6	7.5	7.5	7.5	8.1	6.2	6.6	6.5	7.7
Guyana	4.0	11.6	7.8	6.8	7.8	8.1	9.9	10.3	8.5	9.0	10.0
Jamaica	4.1	22.3	7.0	14.6	22.6	15.6	18.1	14.2	10.4	8.4	8.4
Suriname	2.3	3.8	5.0	17.6	15.0	17.9	15.0	10.0	11.5	14.0	13.0
Trinidad & Tobago	6.1	5.0	5.3	6.7	7.1	7.8	5.3	8.3	9.5	8.7	7.5

Source: CCMS
(Caribbean Centre for Monetary Studies)

Insurances Services

The insurance industry in the region has many of the same characteristics of the banking industry. There is competition in the area of general insurance but with life insurance "there is little competition and high concentration of business by a few primary operators" [CGCED, pg. 29]. Premiums are generally high partly due to the low returns on assets. This, in turn, is caused by the lack of quality long-term assets in the region. Thus, by most accounts, the insurance sector in the region is considered noncompetitive and vulnerable. The case of Jamaica again is noteworthy, as there are currently four (4) life insurance companies (two of which are being merged).

In general, recent data on the insurance industry in many CARICOM countries is difficult to obtain. In many cases, insurance companies do not have to report to the Central Banks, but rather with the Central Statistical Office or the Supervisor of Insurance within the Ministry of Finance. These reports are deemed to be confidential and Cabinet approval is needed before they can be released. This is important in that within the WTO and the FTAA process such outmoded approaches cannot be sustained.

In the last few years, some countries have begun to allow citizens to hold US dollar denominated policies. This may increase the attractiveness of the regional market to more US and Canadian firms that can easily buy out all the local firms and again limit competition. Even before the formal law was passed allowing US dollar policies in Trinidad and Tobago, for example, many local firms were insuring a great deal of their business with foreign firms in foreign currency.

Offshore Financial Services

The offshore financial sector in the Caribbean has always been a source of contention. Nevertheless, the region has been able to do relatively well in this area. For example, the Bahamas, the Cayman Islands, British Virgin Islands, and the Netherlands

Antilles are well-established offshore banking centers. Also, Barbados has a large and growing offshore sector with over 6,600 licensed entities in 1999[3]. In fact, many of the OECS countries saw this sector as having great potential as an alternative to tourism since it involves low infrastructure cost while being able to generate high revenues. Thus, by the late 1990s virtually all had functioning offshore sectors.

Some Caribbean countries have a system for prudential regulation and supervision of financial institutions. Others offer secrecy and access to British legal redress, in case it is needed, to enhance their position in the market. The trend toward increased international movement of capital and the ongoing need for privacy will probably ensure that there is offshore business for the region for some time to come. This is so despite the negative fallout from the blacklisting by the OECD which has resulted in increased costs of operating offshore financial centers and Suss *et. al* (2002,p.18) argues that these countries should "evaluate carefully a decision to establish, or to expand any existing offshore center".

4. Issues in Financial Services Negotiations in the FTAA

The US Proposal on Financial Services

The proposal by the US on "Financial Services Text for the FTAA", released in February 2003, is quite extensive and poses some serious challenges for CARICOM. It is obvious that the US intends to seek a wide open market in the hemisphere where its firms will win out due to their advantages size and relative efficiency. One major challenge to CARICOM will be how to comply with some, if not all, of the articles in this text without compromising Protocol II.

More specifically, there are some issues in the text that have to be addressed:

1) There is little or no attention given to "small and developing states". This is important because the region thus far has insisted that "special and differential treatment" be an essential element of the agreement.
2) Issues such as the practical application of MFN need further discussion and clarification in an area where there exists so many bi-lateral and sub-regional groupings.
3) The text failed to include Article 4 on "Market Access for Financial Institutions" is a major drawback of the text. The position taken by the Bankers' Association of Trinidad and Tobago (BATT) that "no meaningful financial services discussions could be held without the core text on market access"[4] seems to quite appropriate on this issue.

[3] Suss et al (2002, p.24)

[4] Bankers' Association of Trinidad and Tobago (2003) "Comments on the U.S. FTAA Financial Services Chapter", p.2, mimeo.

4) The term "in like circumstances" is used to describe obligations to reciprocate on the part on FTAA members. This term is too hazy and is a throw back the to old U.S. protectionist argument that their market should be closed to any country that does not afford "comparable access" to its market. This argument has long been discredited.

5) Article 6 on "New Financial Services" should also be carefully examined since the region may develop a competitive advantage in a particular product at some stage and may wish to safeguard it for some time.

6) Article 9 on "Non-Conforming Measures" also needs careful consideration and wording since it may have implications for regional agreements and could also be crucial in terms of unhindered access to the U.S. market where interstate banking laws can be problematic.

7) The Transparency requirements of Article 11 may be somewhat onerous for small states to meet but it is perhaps the area where CARICOM financial institutions and regulators are at their weakest. Application and adherence to strict guidelines on transparency can only be of benefit to individuals and firms in the region.

8) Issues such as "Dispute Settlement" and "Investment Disputes in Financial Services" are more aimed at the larger Central and South American countries where there has been historical contention on these matters, especially in the area of investment.

At present the financial services sector in the region is still in an evolving stage. In 1998, the main issues confronting the financial sector in the region were cited as: "excessive public debt, geographic fragmentation and lack of competition in local markets, outdated regulation and weak supervision, scant supply of long-term finance or credit for small firms, low mobilization and inefficient use of contractual savings funds, and underdevelopment of capital markets"[5]. It is dominated by commercial banking and insurance in some countries and by offshore banking in others. The large and expanding banks of Trinidad and Tobago are the only ones that can possibility compete in the Central American and U.S. market or even hold their own against foreign competition in the region. Insurance firms in the region are generally regarded as being inefficient and vulnerable, hence the willingness to form alliances with banking entities.

Regulatory Environment in the Financial Services Sector in the Caribbean

As noted above, an outdated and weak regulatory environment prevails in the Caribbean. This should cause some concern for the region since liberalizing the financial sector in such a situation may lead to abuses not seen in the region thus far. In fact, most of the requests from the developed countries to CARICOM members make reference to improvements in transparency and regulatory clarity. It clearly conveys the impression that CARICOM countries have a very long way to go toward bringing their financial sectors on par with what exists in the advanced markets. The regulatory

[5] World Bank Group (1998) "Caribbean Financial Sector Review",p.1

framework within CARICOM is definitely inadequate in many areas, especially pertaining to Mode 1 (cross border supply) and Mode 2 (consumption abroad) in financial services. Therefore so-called suitcase traders in financial products can enter CARICOM markets, in person or over the Internet, and offer residents a variety of options completely without detection or hassle from authorities. A more open financial system without the necessary regulations will no doubt exacerbate this problem. Most CARICOM states do not have the laws of technological infrastructure to deal with this new development.

On the question of offshore banking, a number of OECS countries have pursued the development of this sector as a means of further "integrating with the global economy. However, in the current international environment, they have come under increasing scrutiny regarding international tax competition and supervision of offshore financial institutions, especially due to heightened concerns about illegal financial transactions. All the countries have taken steps to strengthen supervision of offshore banks, improve controls against money laundering and have made commitments to address harmful tax competition. Furthermore with assistance from the IMF, the OECS countries are participating in the self-assessment of their offshore sectors. The World Bank, in collaboration with the IMF and the ECCB, will support the preparation of a wider Financial Sector Assessment Program for the OECS" (World Bank- Country Brief OECS).

One CARICOM country with a large offshore sector, the Bahamas, has been keen to implement regulatory changes in recent years to protect its interest. In the wake of supra-national initiatives launched by the Financial Stability Forum (FSF) and the Financial Action Task Force (FATF), as well as the US Treasury led Qualified Jurisdiction (QJ) initiative, the Government of the Bahamas embarked on an ambitious overhaul of financial sector legislation. The result of this was that they enacted nine (9) new banking acts in 2000 in order to comply with the FATF Key enhancements that included:

- Enhanced powers of the Governor of the Central Bank to issue and revoke licenses to carry on banking and/or trust business from within the Commonwealth of The Bahamas.
- Operational independence of the Central Bank in supervision and regulation of banks and trust companies;
- Increased provision for information sharing with other regulators for supervisory purposes;
- Provisions upgrading banking supervision, including, but not limited to, on- site examination of banks and trust companies, as well as permitting examinations by appropriate overseas supervisory authorities;
- Upgrading and broadening of KYC[6] requirements and suspicious and unusual transactions reporting;
- Establishment of a Financial Intelligence Unit (FIU);

[6] Means "Knowing Your Customer"

- Introduction of licensing of financial and corporate service providers, such as lawyers, accountants and management companies;
- Removal of bearer shares from International Business Companies (IBCs) shareholding structures, and granting of permission for Bahamians to own IBCs.

The Central Bank of the Bahamas has all these acts and regulations relating to financial services laid out clearly on its website. It conveys the message of an open and transparent financial system from which other CARICOM members can learn. Even though the Bahamas example may not be feasible in other countries, it is clear from the U.S. proposal for services in the FTAA that a more open and transparent financial system cannot be avoided.

The Competitiveness of Financial Services Firms in the Caribbean

Can regional banks compete in a broader market?

In each Caribbean country, competition among commercial banks tends to be of a non-price nature. Within the context of the WTO, and more importantly, the FTAA, they may find it difficult to maintain some of their current practices. There are three underlying reasons why regional banks appear to be uncompetitive when compared to banks in larger, more developed areas. Firstly, regional banks face indivisible fixed costs, such as management, equipment and specialized personnel. Amortizing these fixed costs over a small volume of business makes for higher average operating costs. In addition, most indigenous banks within the region are very small (assets under $100 million) and additional financial benefits of scale include large pool of deposits to provide better liquidity and large portfolios of loans that can be diversified and less risky. Better liquidity and lower risk can increase banks safety within the region and is a factor of their small size. The last issue considers the competitiveness of regional banks and their economies of scale coupled with their ongoing consolidation efforts. While consolidation efforts among regional banks offer economies of scale, also arising out of this is increasing concentration, which can restrain competition[7].

The efficiency of Caribbean Banks

---

[7] Caribbean Group for Cooperation in Economic Development (1998)"Wider Caribbean Financial Sector Review: Increasing Competitiveness and Financial Resource Management of Economic Growth", Report No.17556-LAC.

Commercial banks in the region, as noted above, tend to be characterized by high operating costs and large lending spreads which are indicators of inefficiency. These usually arise when there is a general lack of competition and/or diseconomies of small scale. According to the World Bank and the Caribbean Centre for Monetary Studies, in 1992 the ratio of operating costs to total assets averaged 20% in Jamaica, 11% in Trinidad and Tobago, and 10 % in Barbados. The latter most likely had the largest presence of foreign banks of the three. Also in 1996, it was found that lending rate spreads were 18.8 % in Jamaica, 8.1% in Trinidad and Tobago, and 4.8% in Barbados. However the operating costs averaged 3.0-8.5% in Latin America and their lending spreads were 5.1-9.2%. While operating costs in the Asian NICs and the OECD averaged only 0.8-8.5% with lending spreads averaging 1.1-3.0%. Since that time there has been consolidation in the financial sector in the region as cross border ownership has increased rapidly in the past 5 years.

So it may be that regional banks may not be competitive generally when compared to banks in developed countries. There are reasons such as the small size of the market, vulnerability, and lack of economic diversity that partially explain the high operating costs of banks in the region. Nevertheless, their ability to compete will not be known until non-regional banks enter the retail market. In fact, one area were regional banks can be vulnerable is in competing for scarce human resources. The existing pool of managerial talent appears to be limited[8].

Would foreign banks come to the region?

There are no direct barriers to entry of foreign banks in most of the region even without the FTAA process. This is so despite the localization efforts of the 1970s by Guyana, Jamaica and Trinidad and Tobago in the 1980s. However, the presence of foreign banks is alive mainly in Barbados, Belize and the OECS [Henry, 2003]. Foreign banks have, in the past, withdrawn their presence in many Caribbean countries because of the following reasons:

(1) *Lack of profitability.*
(2) *Macroeconomic instability.* Bad fiscal and monetary policy makes countries within the regions unattractive to foreign financial institutions wishing to invest. Stability in key macroeconomic variables such as inflation, unemployment, gross domestic products, and savings. There was also the fear of political stability. Also there were concerns about the required infrastructure, legal and regulatory framework by potential investors.
(3) The existence of *financial repression,* which included interest rate ceiling and directed lending, high reserve requirements, and restrictions on foreign exchange.
(4) *Diseconomies at the operational scale.* Banking is subject to significant economies of scale; the smallness of regional banks (assets under $100 million) is a deterrent to foreign entrants.

[8] The AIC Group's entry into the Trinidad and Tobago market has already seen them creaming off the top Managers the RBTT's Group Merchant Bank.

Most of these problems have either been eliminated or severely reduced. The macroeconomic and political environment throughout the Caribbean is very stable and pro-business, with the possible exception of Guyana. Furthermore, commercial banking in many cases is extremely profitable. As noted above, Trinidad and Tobago's commercial banks have been making increasingly larger and larger profits over the past few years. This economic profit, higher than the average rate of return, can be a signal for new entrants into the market. It is useful to note that, with the FTAA, the competition may come from South and Central American banks rather than those from the North.

5. Summary and Recommendations

An important question for policy makers, which is of major significance to trade negotiations, is whether regional firms are more interested in market access to other FTAA countries or are they seeking to protect their market share from possible outside competition. The evidence thus far is mixed. The larger more aggressive banks in Trinidad and Tobago feel confident that they can withstand foreign competition, especially in retail banking. This is based on the fact that they have the confidence of their customers and understand the banking culture of the region, in addition to their established presence.

These banks further believe that they can compete in the broader Latin American market. The US market, however, with its relatively high capital requirements and stringent regulation may be off-limits to regional banks unless further consolidation takes place. The region should aggressively pursue market access for CARICOM banks in Latin American markets, given the above discussion; there is not much to lose. Furthermore, if the regional market is opened further to foreign banks in the process then the resulting competition will most likely be of great benefit to non-financial firms who currently are forced to pay very high interest rates and are denied many services that their counterparts in other regions take for granted.

The financial sector faces potential challenges from the outcome of the FTAA process, in particular, the insurance sector is considered to be very vulnerable. Meeting the transparency requirements called for by the US could be very costly and could result in major changes in the way in which regional firms do business. The general culture int the region is one of non-transparency. Regional governments will also have to re-design their legal and regulatory framework to comply with the new requirement. At the moment the general view seems to be that the region has a long way to go in this regard. The Caribbean has been slow in reforming its financial sector perhaps hoping to hide behind special and differential treatment for a number of years.

The completion of the FTAA could see new firms from outside the region coming in as all for barriers to entry are removed and the current level of profitability acting as a magnet. Also, the policy changes in the OECD countries aimed supposedly at stemming money laundering and illegal tax practices may severely undermine the offshore sector in the region. It is not all gloom and doom, however. The FTAA and technological challenges are also potential opportunities for regional firms it they can take advantage of the newer larger market at their disposal. There is absolutely no reason why efficiently run regional firms cannot also penetrate markets in North, South, and Central America.

References

Akyuz, Yilmaz (eds) (2002) **Reforming the Global Financial Architecture Issues and Proposals**, UNCTAD, Geneva.

Antoine, Rose Marie (2000) "The Offshore Financial Services Sector: Legal Policy Issues on the Path to Development", paper presented at the ISER Conference on "Alternative Development - The Role of the Services Sector", Sherbourne Center, Barbados, January.

Auffret, Philippe (2003) "Catastrophe Insurance Market in the Caribbean Region: Market Failures and Recommendations for Public Sector Interventions", Working paper # 2963, World Bank, Washington D.C..

Bankers' Association of Trinidad and Tobago (2003) "Comments on the U.S. FTAA Services Chapter", Mimeo.

Bello, Walden; Bullard, Nicola and Malhotra, Kamal (eds) (2000) **Global Finance New Thinking on Regulating Speculative Capital Markets**, The University Press, Dhaka.

Bissember, Enid E. "The Role of National Insurance Schemes in CARICOM in the Transformation of the Financial System" Economic Intelligence and Policy Unit, CARICOM Secretariat.

Bourne et al (1998) Competitiveness of Caribbean Financial Services and WTO Related Negotiating Strategies, Caribbean Community Secretariat/Regional Negotiating Machinery, Georgetown Guyana.

Canadian Foundation for the Americas (FOCAL), (19**) "The Smaller Economies of the Americas: Making A Case for Hemispheric Integration" Policy Paper FPP-00-9.

Caribbean Group for Cooperation in Economic Development (1998)"Wider Caribbean Financial Sector Review: Increasing Competitiveness and Financial Resource Management of Economic Growth", Report No.17556-LAC.

CARICOM (1997) "Protocol II: Establishment, Services, Capital" Caribbean Community Secretariat

Central Bank of Trinidad and Tobago (1999) "Table A1, Commercial Banks: Summary Data 1996-1999",
(http://www.centralbank.org.tt/rnd/statistics/data/finsumdata.pdf.)

Clarke, George R. G, Cull, Robert and Maria Soledad Martinez Peria (2001), "Does Foreign Bank Penetration Reduce Access to Credit in Developing Countries? Evidence from Asking Borrowers". (www.worldbank.org)

Clarke, Laurence and Danns, Donna (eds) (1997) **The Financial Evolution of the Caribbean Community** (1970-1996), Caribbean Centre for Monetary Studies.

Clemons, Eric K. and Hitt, Lorin M. (2000) "Hazards and Precautions Tales of International Finance" The Wharton School, University of Pennsylvania.

Danns, Donna (1996) "Financial Development in the Caribbean (1970-1995)", Caribbean Centre for Monetary Studies, Oct-Nov.

Devlin, Robert, Antoni Estevadeordal Antoni and Luis Jorge Garay,(1999) "The FTA: Some Longer Term Issues", **Intal ITD,** August, Occasional Paper 5.

Devlin, Robert and Luis Jorge Garay (1996), "From Miami to Cartagena: Nine Lessons and Nine Challenges of the FTAA", Working Paper Series 211, Washington D.C., IDB.

Devlin, Robert and Castro, Lucio (2002) "Regional Banks and Regionalism: A New Frontier for Development Financing" Institute for International Economics, February.

Dolar, Veronica and Meh, Cesaire (2002) "Financial Structure and Economic Growth: A Non-Technical Survey" Bank of Canada, Working paper 2002-24.

Dookeran, Winston (2000), Governor Central Bank of Trinidad and Tobago "Free Trade Area of the Americas: Challenges Ahead" Speech delivered at First Citizen Bank Breakfast Meeting, April.

ECLAC (2001) "Progress made by Caribbean Countries in the WTO built-in Agenda on Services and Intellectual Property Rights" UN ECLAC/CDCC. Subregional Headquarters: Port of Spain

Economic Perspectives (2002) "The Free Trade Area of the Americas: Expanding Hemispheric Trade", Vol 7, No 3, October.

Enterprise (2001) "A Publication of the Private Sector Organisation of Jamaica" Vol 17, No 1, March.

Feracho, Jackie and Samuel, Wendell (1997) "Regulation and Financial Services in the ECCB Area" **Social and Economic Studies**, Vol 46, No 2&3.

Francois, J. and Schuknecht, L. (1999) "Trade in Financial Services: Procompetitive Effects and Growth Performance", Discussion Paper No. 1999028/2, The Tinbergen Institute.

Francois, J. and Eschenbach, F. (2002) "Financial Sector Competition, Services Trade, and Growth", Tinbergen Institute Discussion Paper 089/2, Amsterdam: The Netherlands, September.

"Free Trade Area of the Americas: Overview of the FTAA Process (2001)" Website: http://ftaa-alca.org/ngroups/nginve_e.asp.

"Free Trade Area of the Americas: Trinidad and Tobago (2001)", Website:

http://ftaa-alca.org/busfac/cytindex/TnTmnpge.asp.

Fry, Maxwell. (1997) "In Favour of Financial Liberalization", **The Economic Journal**, 107(May), 754-770.

Grabel, Ilene. (1995)"Speculation-led economic development: a post-Keynesian Interpretation of financial liberalization programmes in the Third World", **Journal of Post-Keynesian Economics**, pp.127-147

Greenidge, Berkeley (2002) "The Development of the Services Sector in Caribbean Economies", PricewaterhouseCoopers, Barbados, September.

Haufbauer, Gary Clyde and Wada Erika (1999) "Hazards and Precautions: Tales of International Finance" Institute for International Economics, September.

Henry, Lester (2003) "Implications for CARICOM Countries of Negotiations on Financial Services in the FTAA and GATS: Assessment and Strategic Options", Caribbean Regional Negotiating Machinery, mimeo.

Johnson, Hazel J. (2000) **Global Positioning for Financial Services**, World Scientific publishing, New Jersey.

Joseph, Anne (1997) "Stratagic Alliances in the Financial Services Sector: Implications for Trinidad and Tobago" **Social and Economic Studies**, Vol 46, No 2&3.

Llaeven, Luc (2002) "Financial Liberalization and Financing Constraints: Evidence from Panel Data on Emerging Economies", (www.worldbank.org)

Litan, Robert E.; Masson, Paul and Pomerleano, Micheal (eds) (2001) "Open Doors: Foreign Participation in Financial Systems in Developing Countries" Worldbank and IMF.

Nader, Ralph (2002) "GATS" CommonDreams.org, September.

Nicholls, Shelton (2002) "Implications of FTAA Agreement for Financial Services", Presented at the UNECLAC Conference on the Development of the Services Sector in the Caribbean.

Mashayekhi, Mina (2000) "GATS 2000 Negotiations Options for Developing Countries" Trade-Related Agenda Development and Equity, Working papers 9.

Matthias, Rudolph C. (1999) "The Emerging International Financial System and its Implications for the Caribbean" **Caribbean Dialogue**, Vol 5, No 3&4.

Mattoo, Aaditya (1999) "Financial services and the WTO Liberalisation Commitments of the Developing and Transition Economies" World Bank, Washington D.C. September.

Mattoo, Aaditya; Rathindran, Randeep and Subramanian, Arvind (2001) "Measuring Services Trade Liberalisation and its Impact on Economic Growth: An Illustration" Worldbank, IMF and University of Maryland, August.

Morton, Colleen, (1997) "Progress Towards Free Trade in the Western Hemisphere Since 1994", **Monitoring the Summit of the Americas.** La Tolla: Institute of the Americas, Washington, D.C., September.

Oyowe, Augustin (1996) "Implications for Developing Countries of Liberalised Financial Services" **The Courier ACP-EU**, No. 45, March-April, pps 45-46.

Permanent Secretariat of the Latin American Economic System (SELA), (1997) "Gone With The Wind? Special Treatment for the Developing Countries", Strategic Issues, No. 29, February.

Permanent Secretariat of the Latin American Economic System (SELA), (1997) "Towards A Free Trade Area of the Americas, FTAA: The Moment of Truth", Strategic Issues No. 31, April.

Pollner, John D. (2001) "Catastrophe Risk Management using Alternative Risk Financing and Insurance Pooling Mechanisms", Working paper # 2560, World Bank, Washington D.C..

Primo Braga, Carlos (1996) "The Impact of the Internationalization of Services on Developing Countries", **Finance and Development**, World Bank, pp. 34-37.

Public Citizen (2002) "Unveiling NAFTA for the Americas" Washington D.C.

Public Citizen (2000), "The MAI Shell Game The Free Trade Area of the Americas (FTAA)". **Global Trade Watch,** http://www.citizen.org/pctrade/Shell_Game/Ftaa.htm

Rojas-Suarez, Lilliana (2002) "Toward a Sustainable FTAA: Does Latin America Meet the Necessary Financial Preconditions?" Institute for International Economics and Center for Global Development.

Seerattan, Dave (1996) "New Trends and Challenges for the Financial Services Sector in the Caribbean" Caribbean Centre for Monetary Studies, Oct-Nov.

Sorza, Piritta (1997) "The GATS Agreement on Financial Services- A Modest Start to Multilateral Liberalisation" IMF Working paper 55, May.

Stephenson, Sherry M. (1999) "Approaches to Services Liberalization by Developing Countries" OAS Trade Unit, February.

Suss, Esther C. "Oral H. Williams and Chandima, Mendis (2002) "Caribbean Offshore Financial Centers: Past, Present, and Possibilities for the Future", IMF Working Paper, WP/02/88, May.

Tease, Warren and Wilkenson, Jenny (1993) "The Provision of Financial Services – Trends, Prospects and Implications" Reserve Bank of Australia, Research Discussion paper 9315, December.

"Trinidad and Tobago The Business Centre of the Caribbean (2001)", Website: http://www.investtnt.com/

World Bank (1996) **Prospects for Services Exports from the English- Speaking Caribbean,** World Bank: Washington D.C., May.

WTO, Council for Trade in Service, (1998) "Jamaica's Schedule of Specific Commitments", GATS/SC/45/Supplement 2.

WTO News (1997) "Liberalizing Financial Services Helps Economies without Compromising their Right to Regulate" Press Release #76, September.

WTO News (2001) "Risks and Benefits for Developing Country Banking Systems from the Internationalisation of Financial Services Examined in the new book by the WTO and the World Bank" Press Release #208, February.

WTO Services (2001) "The Results of the Financial Services Negotiations under the General Agreement on Trade in Services (GATS)".

WTO Services (2002) "GATS Fact and Fiction"