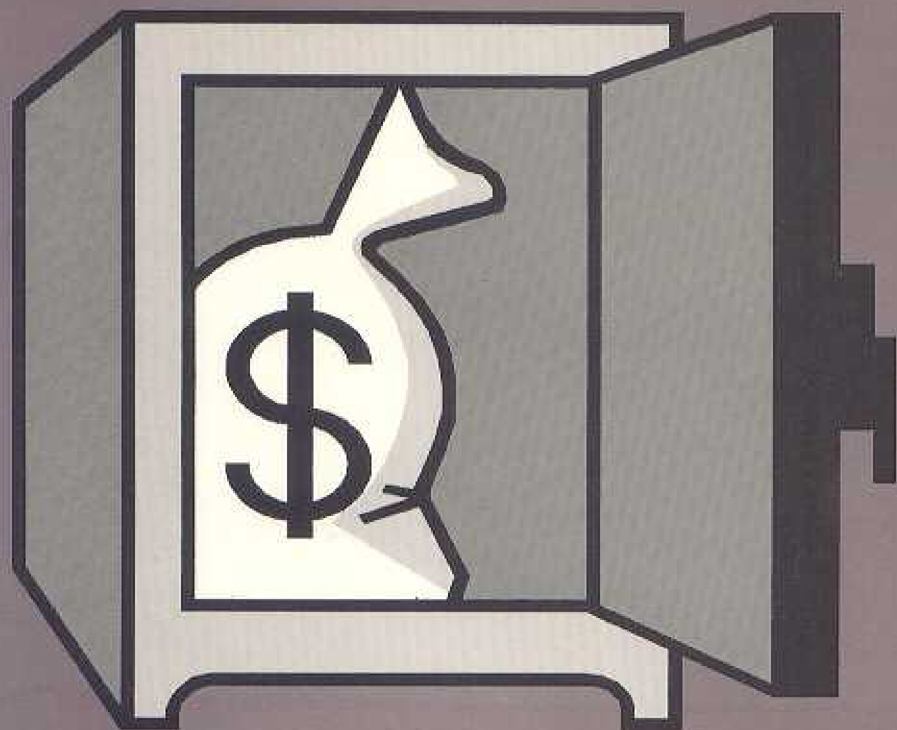
# Economic Liberalisation and Caribbean Development

*Lloyd Best, Norman Girvan and C.Y. Thomas*

*Edited by Ramesh Ramsaran*



The 'floating' of the Trinidad and Tobago dollar in April 1993 provided the occasion to convene a forum to address the implications of this move against the background of experiences in other parts of the Caribbean. The discussion brought together some of the region's leading scholars in a lively debate on this topic of immediate relevance to the Caribbean. This is the first in the **Occasional Paper Series** of the **Regional Programme of Monetary Studies (RPMS)**.

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**OCCASIONAL PAPER SERIES NO. 1**
Regional Programme of Monetary Studies

# ECONOMIC LIBERALISATION AND CARIBBEAN DEVELOPMENT:
## Proceedings of a Panel Discussion

Mr. Lloyd Best
Professor C.Y. Thomas
Professor Norman Girvan

Edited with an Epilogue by Dr. Ramesh Ramsaran

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**ST. AUGUSTINE**
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# OCCASIONAL PAPER SERIES OF THE REGIONAL PROGRAMME OF MONETARY STUDIES

It is now generally recognised that the Caribbean must do its own soul searching, and come up with its own management tools. It must not and should not relinquish this to others simply looking for technical solutions to fiscal and foreign exchange problems. Caribbean peoples must engage in continuous discussions in an effort to educate themselves. The Regional Programme of Monetary Studies (RPMS) has over the years made a valuable contribution by focusing attention on relevant monetary and fiscal issues of the day. The 'floating' of the Trinidad and Tobago dollar in April of 1993 provided the occasion to convene a forum to address the implications against the background of experiences in other parts of the Caribbean. The discussion brought together some of the leading scholars of the region. The panelists included Mr. Lloyd Best of Trinidad, Professor Norman Girvan of Jamaica and Professor Clive Thomas of Guyana. The session was chaired by Professor Compton Bourne, the Deputy Principal of the St. Augustine Campus, U.W.I.

The need for an Occasional Paper Series to disseminate more widely and more frequently the work of the RPMS has long been recognised. The time for this has arrived. The proceedings of the discussion which took place at the Institute of International Relations on April 29th, 1993 are now made available to the public in the form of the first issue of the RPMS Occasional Paper Series.

Ramesh Ramsaran,
Co-ordinator,
Regional Programme of Monetary Studies,
I.S.E.R., U.W.I., St. Augustine, Trinidad.
25th August, 1993.

# INTRODUCTION OF PANELISTS BY MODERATOR

**Professor Compton Bourne, Deputy Principal, UWI—St. Augustine**

Let me say how pleasantly surprised I am at the large turnout this evening. Since we've already had two sessions on this campus on the question of foreign exchange market liberalisation, the fact that you have come out here tonight in such large numbers is a measure of the importance of the topic and the importance you yourselves attach to it.

The subject of tonight's panel discussion is "Economic Liberalisation & Caribbean Development". I think it is good that the topic has been broadened this way beyond simply floating exchange rates, which I know is quite dear to the hearts of many now, because the exchange-rate regime and the changes therein are part of a general economic policy of liberalisation, both in the international and the domestic sectors. One is well advised therefore to see exchange-rate developments in that broader context and against a broader set of objectives. We are particularly fortunate tonight in our panelists. We have Mr. Lloyd Best who is well known here and requires no introduction, to speak on the topic of "An Appropriate Exchange Rate Regime for Trinidad & Tobago in the 1990s". He will be followed by Professor C.Y. Thomas from the University of Guyana, who is also no stranger to us, an expert in the field of economic development and money, and he will speak on "The Relevance of Financial & Trade Liberalisation to Caribbean Development". Thirdly, we have Professor Norman Girvan, no stranger either, also an expert in the field of development and he will address particularly "The Jamaican Experience of Liberalisation".

We therefore have a set of people who bring to bear considerable experience and expertise in the field of economic development, reflecting and researching in the area of policy. We span the spectrum of the Commonwealth Caribbean, so to speak. My job is a very simple one; just to keep these three distinguished gentlemen in line. The first rule here is that they each speak for no more than 25 minutes on the topic assigned to them, so that we will have ample time for discussion with participation from the floor. Let me therefore without ado call on Mr. Lloyd Best to get the ball rolling.

## An Exchange-Rate Regime for Trinidad & Tobago in the 1990s

**Mr. Lloyd Best**
**Director, Trinidad & Tobago Institute of the West Indies**

Mr. Chairman, ladies and gentlemen, almost everywhere they introduce me, they say that Lloyd Best needs no introduction. It reminds me of the time I went to New Delhi. My very good friend, Professor P.N. Dhar from Delhi University, who, like Pandit Nehru, is a Kashmiri Brahmin, sent to Kashmir to say "Lloyd Best is coming on a visit. Please make the arrangements." Back came the cable, "Mr. Good can come at any time". I remarked that they forgot the arithmetic but they got the algebra. They forgot my name but they got the concept very well.

Tonight it is going to be important for us to rise above the specifics of the arithmetic and get the algebra. I am to talk about a foreign-exchange regime for Trinidad & Tobago. I don't know if I know what that means. I must also tell you that I have to speak from my heart. These days every time I go to the computer for my text I can't get it to print. This is about the third time recently that it's happened to me. I did the stuff on my laptop but when I went this evening to the printer, I couldn't get it to work at all, so I'm afraid I have to rely on these rough notes, not that that is going to inhibit me in any way.

Perhaps we should start with what I call the "Tuesday morning blues". On that Tuesday morning of April 1993, the commercial banks were meant to begin this new regime of a floating exchange rate. I have asked myself what kinds of questions they needed to confront on that morning. I have one or two answers. First, they had to decide whether there was excess demand for foreign exchange and the extent of that excess demand. Secondly, they had to ask themselves at what rate they should intervene.

I think if we make sense of their predicament on that morning, we might get the essential insights as to what the underlying issues are in this business of exchange management and by extension, macro-economic and other management of these economies at this particularly crucial time in their history. Clearly, excess demand is the dominant theme. In some ways, the question they were asking on that Tuesday morning is what the additional excess demand was, or what the limits to excess demand were, because the source of the problem is the scarcity of foreign exchange.

The reason we have had ten years of persistent economic decline since 1983 is that our earnings of foreign exchange have dropped, perhaps by half. Since income and employment require foreign exchange as the crucial resource to keep them active, the drop in the foreign exchange that we earn has led to a drop in the level of activity in the economy. What has happened over the last 10 years is that the halving of the foreign-exchange earnings of the country from petroleum has forced the economy to adjust downward to just that level of activity, employment, output and income which can be sustained by the new and lower earnings of foreign exchange. There's no doubt that the excess demand for foreign exchange, which is the other side of the scarcity of foreign exchange is the crucial problem in all of these countries at several levels. I think we need to understand those levels.

Firstly, that by their history, the way in which these societies were founded, almost all the initial inhabitants wanted to realise their income and their wealth in terms of foreign commodities. In the pure case of plantation economies, if I put it that way, national income is actually zero, because all of domestic product flows out as factor income going abroad, since all of the people who earn income, the slaves earning none, are people who live outside. They don't want anything that is produced here on the spot; they want to realise their income and keep their wealth in foreign exchange. So it is a chronic historical problem in all these countries that people want to realise their income and their wealth in terms of the capacity to consume imports. In that sense, there is a fundamental problem of foreign exchange all the time which we simply have to notice.

Secondly, there is a fundamental problem of foreign exchange in the sense that at the current time, we don't have enough foreign exchange to sustain full employment. In that fundamental sense, it's scarce. The economy, as I've said before, after 10 years, has settled down and has reached an equilibrium at less than full employment. Here we have 20% unemployment. In a sense we can say that the reason for that is that there is not enough foreign exchange to bring the other resources into play.

Thirdly you might look at it in another way. You might say that there is what the economists call a "conjunctural problem" which is related to the other two but has to do with the gloominess of the expectations engendered by the second situation I have described, the long contraction, the settling down of the economy at less than full employment.

Therefore the excess demand for foreign exchange that we have now can be said to reflect three things. One is availabilities. The fact that you don't have foreign exchange is a problem that generates expectations and therefore both a rush to get foreign exchange and

projections of the future that may affect the rate at which people increase their demand for foreign exchange.

Then behind the factual situation of what foreign exchange is available, you also have the problem of policy credibility, because the lack of foreign exchange engenders management problems. The authorities intervene in one way or another to try to solve these problems. The way in which they intervene is more or less effective and people are speculating, of course, on whether these interventions will be effective or not. To the extent that they are not persuaded, you have a problem of policy credibility.

Thirdly, you have, in a wider circle still, the problem of the political and social setting. Quite independent of the measures that governments and the authorities may take to bring the system into some kind of equilibrium, or to promote growth if you like, quite apart from those measures, people are asking questions about the viability of the whole economy and society. We can only understand the Tuesday morning blues if we understand this environment I have just described. The historical problem of foreign exchange, the structural problem of foreign exchange, the conjunctural problem of foreign exchange, all conspired to make excess demand, which everybody already knew about; but at the particular juncture on that Tuesday morning, the new intervention forced the country to prick its ears up and ask, "What's happening now? Is there going to be additional excess demand?" We're talking now about the dynamic setting on that particular morning.

Naturally, the commercial banks knew that they would not have enough foreign exchange to meet the demands on that morning. Of course the Central Bank said that the commercial banks made the decision to reinstitute the exchange controls and chose their rate, but that was a manner of speaking. If they anticipated there was not enough foreign exchange to meet the demand on that morning, the next question was, "Would we be able to procure foreign exchange from the authorities to meet the deficit?" The answer was gloomy on both counts.

First, the central authorities did not have enough foreign exchange. As they have said, the foreign exchange that they have from tax receipts, from divestment proceeds, from draw-downs of loans from multilateral agencies and so on is just enough to meet their debt obligations, with very little left over. They therefore could not commit themselves to saying' "We will be the lender of last resort. If you go to the market on Tuesday morning and you have a free situation and you find you don't have enough exchange, we will have nothing to give you."

In that way, of course, it is the Central Bank that really decided upon the intervention rate. The Central Bank and tha Ministry of Finance made the decision first of all to keep the exchange controls

and to intervene at the rate at which they actually intervened. They had also to say to themselves that if we have excess demand on that scale and we put a price on it that would reflect the conditions of the market, that price would be very high.

Given the environment I've described, if they had set the rate so high, what would have been the effect of that? The effect would have been to tell people, "Boy, like these people feel the rate go run away from we!" and therefore the effect of the very high rate might very likely have been that people would seek *more* foreign exchange, not less. The higher the price, the more they would seek it, not less, because of the negative impact of a high price on expectations. They would say, "Boy, like we going through". Had they put a rate of 20 to 1 or 25 to 1 or 50 to 1, you see what I mean, any high rate, would have induced people to say, "I better go and get what foreign exchange I can this morning, oui." They would have got more excess demand rather than less, with a high rate, so they had to settle for a lowish rate, and the only way they could settle for a low rate is if they also retained the old regime of restrictions.

Thus, we can quite easily get away from the arithmetic and get to the algebra if we understand all that. The fundamental problem in the financial system and in the economy and in the country is that there is chronic excess demand for foreign exchange. That has been exacerbated in recent years by the persistent economic decline and the effect on income and employment as well as the effect on policy credibility of successive governments which have not been able to distinguish themselves one from the other, or to cope with the related problems of distributive justice or allocative efficiency.

The situation is aggravated even further by the dynamics of decline which have led to experimentation with restrictive macroeconomic policies leading to the intervention on April 13 with this liberalisation of the foreign-exchange regime. This measure however could not be effective, because any attempt to allow the market to work would have exacerbated the predicament by giving the impression that the situation was desperate. Therefore they settled on a transition period which will be marked first by a comparatively low rate of exchange which is not, however, an equilibrium rate since it does not eliminate the excess demand and second, by the retention of the regime of exchange controls.

I want to talk a little bit about what that really means for us in terms of economic management and the choices that we seem now to have or not to have. The orthodoxy of these times is that the solution to the problems of these countries lies in liberalisation of markets. I'm sure we'll hear later about the experience of Jamaica and Guyana. As you know, in the Jamaican case, they have experimented with almost every kind of foreign-exchange regime in recent years. Jamaica established a Central Bank in 1961. It was not

very different from all the other countries in the West Indies which operated the sterling exchange standard. At the beginning they pegged their dollar to sterling; they then pegged it to the US dollar in 1971 and since then have gone through frequent devaluations and a number of exchange regimes.

Between 1978 and '79 they had the so-called "crawling peg" with mini-devaluations. In 1983 they had the two-tiered system which then moved to a three-tiered system. At the end of 1983, they had an auction system with a flexible rate within a narrow band and then they had a flexible rate within a much wider band, in fact they removed the band altogether. Then in 1989, they fixed the peg. Then in September '90, they moved to a flexible exchange rate of the kind that we have now, what is called the interbank system, where they had licensed authorised dealers much as we have done with our commercial banks. The banks were free to sell and buy and so on. Then in September 1991, they deregulated altogether, removed all exchange controls and they allowed people to hold accounts at home and abroad. They freed all transactions, current and capital, and the only thing they kept under wraps was portfolio outflows by deposit-taking institutions. Of course you know the rest. It's been in the papers all over and you'll hear more about it.

Now I mention the Jamaican experience, which has been the most variegated of all and the one that we're looking at most closely, because the question that it raises is the role of the exchange rate in the management of the economy. We know from the theory of plantation economy that the external account is the most important account in countries like this. It is not the fiscal account; it is not the budget account. It is the capital-formation account, the external account. It's not the national income account or the domestic product account. In these countries, the most important single price is the price of foreign exchange, because these are externally-propelled systems which came into existence in order to export. Their whole life was consumed by exporting, and only late in their life did residentiary activity arise. Their purpose in life, their *raison d'être* was to export. Therefore the external account is crucial; it is decisive.

My view is that since this price is the critical price in all economic transactions, we cannot allow it to be uncritically dictated by the market. We have got to manage it under any conditions. The exchange rate, of course, is in the strictest sense, almost the terms of trade of the country. It is the price that regulates the relationship between exports and imports, and therefore everybody worries about its stability. It is now, as you can see, a source of great instability due to the turbulence of the international environment. In fact, for a lot of countries, it's a new experience. For us, we have

always had that. We have always had a turbulent international environment, and we've always suffered.

The stability promised by the liberalisers has failed to materialise. The argument is that if you have free markets and a free exchange rate, these systems will reach their equilibrium and settle down. Even the large industrial countries are in trouble, which is why the European countries have the European Monetary System which fixes a range. It is why the large countries keep reserves of gold and foreign exchange in their central banks to be able to intervene in the market to defend their rates within a suitable range. If rates just fluctuate or oscillate wildly, expectations would be impossible.

We are, as I have said, the extreme case of this phenomenon. Our situation is complicated by the fact that we have a narrow range of exports with very volatile prices. That complicates the issue enormously and it therefore makes exchange management a key area of macro-economic management. It makes devaluation or revaluation of the currency, changes in its price, an important instrument of management, especially since depreciations in the currency are the easiest and most neutral ways of affecting spending on the import side when income falls and you have to compress demand. I keep saying all the time here that when your export earnings have fallen, when your income has fallen permanently and you don't devalue to the correct rate, what happens is that those people who are privileged and can get foreign exchange at the wrong rate will get it, while most of the people will pay the price of that wrong rate by being forced to do without any foreign exchange at all.

If you devalue, it communicates to everybody that there's a crisis. The price of imports goes up to everybody and it's an across-the-board cut in real income for everybody in the country, especially if you undertook the devaluation at an early stage. Devaluation doesn't raise prices; what raises prices is the fall in income. If you don't have enough foreign exchange to purchase imports, prices are going to go up whether you devalue or not. The only question is who will get the burden of the fall in real income. When you devalue, the impact is the same on everybody. When you don't devalue, those people who are close to the Ministry of Finance and the Central Bank get foreign exchange while the rest do without and just submit to the pervasive increase in prices.

You can therefore see why for a long time countries such as this one maintained what I have called the Metropolitan Exchange Standard, when you keep your currency tied in some kind of mercantilist arrangement with some bigger country. In some ways, it's a kind of preemptive defence. When you set out on your own however and you become independent, and you have a central

bank that is managing your system, it gives you, of course, many more options to do the things that suit you; but it also makes life infinitely more difficult. The reason for that is the critical role of this price, the exchange rate, to all other prices and all other transactions.

So the economic liberalisers tell us that the way to proceed to make these economies function and bring them to stability and renewed growth is to remove import and export restrictions, remove subsidies and price controls, remove ceilings on interest rates, remove selective credit controls and free up all markets. The premise of this approach is that growth and development require free markets. What is not stated as an important premise as well is that in the regulation of markets, the firm is as important as the State. When they say "free markets", they are talking only about curbing the interventions of the State. What they don't talk about is altering the encompassing contexts that firms create for the markets as well. I mentioned somewhere recently that the Nobel Laureate in economics from Chicago, Professor Coase, reminded us how important the firm is as an instrument of regulating the market.

We discern it very clearly when we talk about money, when we talk about financial intermediaries, when we see how the intervention of banks and non-bank intermediaries affects transactions between surplus accounts and deficit accounts by lenders and borrowers. We see it less clearly in the way in which firms intervene in the transactions between buyers and sellers, consumers and producers. One of the reasons why the liberalisers are proposing liberalisation is that the firms that they themselves have operating in the international economy are the dominant ones and therefore they can be confident that the distribution of world output which is said to be higher as a result of free markets in the Ricardian economics will favour them, if you have free trade and free investment and free exchange regimes. Since, however, we in the Caribbean do not yet have firms that dominate the international scene, we have no choice but to use our governments instead. This price, the exchange rate is so important for us, and all the transactions in the external account are so important for us, we cannot leave it to the invisible hand. For me, that is a basic algebra.

Therefore my main conclusion here this evening is that the exchange-rate regime that we need and we'll talk about it later I'm sure, must be specifically addressed to the needs of Trinidad & Tobago and the CARICOM countries. I am not buying any orthodoxy, any of the fashions of economics, any of the neo-Ricardian mirages and fantasies that are everywhere about. People who don't have the courage or the competence to stand up and fight it and say, "I don't believe that!" are just kowtowing to all this wisdom

that is only received wisdom. Economists everywhere are just bowing to this new orthodoxy. I am not bowing to it; I can see no reason for it; I don't believe in it; I am not supporting it. I'm not a socialist, I'm not a communist, I'm not a populist, I'm not a capitalist, I'm not an academic, I'm not an intellectual, I'm not a professor. I'm none of these things. I am just Mr. Good, and I'm speaking in that capacity without dogma. What I'm saying is that I'm not wedded to any dogmatic position and certainly not to this fashionable new one.

I want us to look at the situation very clearly to understand our historical situation, understand our conjunctural situation, understand the structural environment in which we are and intervene on our own behalf intelligently, with a regime that's specifically addressed to our needs, understanding our own economy, our own region, as well as the wider world. I want an exchange regime that is independently conceived, one that is non-ideological, one that is process-centred, not one that merely hopes that somewhere down the road you're going to get exports and investment and that maybe people will bring back the money they have stashed away in foreign accounts.

What I want is a process-centred regime; I want a discriminating regime; I want a flexible, sensitive, sensible, hard-headed, and above all, managed regime. We have to be in charge of the world where we are. I am not living in any Third World, if you are. Wherever I am is the centre of the world. I am the First World as far as I am concerned and I am managing it from where I am. [Applause] I am not submitting to any fashions or any orthodoxy coming out of universities or multilateral agencies. I am advocating a regime of a specific kind and I want to give you the reasons why I am advocating it in very specific terms.

The algebra is alright, but the arithmetic is also important. It is quite clear that the whole concept of market that underlies all these orthodoxies that we're borrowing is scarcely one that is valid here. Our markets are not large; they're not deep. One transactor can intervene in Jamaica and make the difference. If one transactor can make the difference on the good side, no pun intended, one transactor can also make an intervention on the bad side. The markets are not sophisticated; the markets are not trusted by anybody, as a matter of fact.

If you look carefully at the statements made by the commercial banks the morning after, so to speak, you will see that they don't believe in markets at all. They are vehement in their opposition to speculation; but if you believe in markets, you must allow speculators to function as valid transactors, on the assumption that they will think that if the Trinidad & Tobago dollar is going down now, and you have confidence that the policies are going to work,

it will go back up some time later. You must expect the speculators who are buying US dollars now to buy TT dollars later if you really believe in the market. They don't believe in it. Nobody here does. The markets are not deep, they're not large, they're not sophisticated, they're not trusted, they're not competitive, that's the first thing.

The second thing is that the liberal view confuses financial flows with real flows. The proposals they are making are likely to get us into a domain of financial manipulation and speculation which might cloud the real choices needed to make the liberal orthodoxies relevant to effective macro-economic management. I think that even the liberals are beginning to concede that now. Their most articulate spokesmen are proposing that liberalisation needs to be phased; that there are certain conditions that need to be assembled; that the sequencing is important; that the fiscal preconditions must be put in place; that if you have a large debt overhang as we have in Trinidad & Tobago and your foreign-exchange resources are committed to meeting your debt obligations, you're going to have problems of constricted supply in a condition of chronic excess demand.

If you have monetary conditions where interest rates have to go up and prices are going up, you're likely to get a lot of difficulty. One of the difficulties the authorities faced on the morning of Tuesday, April 13, was that you did indeed have this overhang of excess demand likely to express itself in a surge if and when you moved the restrictions. What was likely to happen in terms of policy was that in order to curb that excess demand, you would have had to have very high interest rates.

So the liberalisation leads automatically to high interest rates as the best way of defending the system against chronic excess demand and additional and escalating excess demand. High interest rates make it profitable for people to keep their money at home and also make it expensive for them to get money from the bank with which to buy foreign exchange. High interest rates are therefore a *sine qua non* of the whole scenario.

If you have high interest rates, what happens? High interest rates compounded with depreciating currency lead to high prices, so you get a spiral of high prices/high interest rates. People's take-home pay loses value; real income falls; welfare falls in turn; and a problem of policy credibility quickly arises. People ask, "But what is this government doing?" when they go to the shop and they can only buy two-thirds of what they were buying yesterday.

The issue of policy credibility arises and by extension, all the issues I've raised of policy credibility and political stability and so on. The macro-economic interventions that you need to make are self-defeating: every time you raise interest rates in order to defend

yourself against excess demand, that sets off the spiral of prices, of speculations in regard to the effectiveness of policy and negative conclusions regarding policy credibility. People prefer even *more* than they did before to hold foreign exchange as their store of value in an historical situation which is already marked by excess demand, so that an additional excess demand simply runs away with you on its own terms.

That is what we faced; I think it is the scenario the authorities faced on that fateful morning of Tuesday, 13 April. They did a very sensible thing, I find they settled for a simple devaluation at TT$5.76-77, to US$1; they opted to retain the old exchange controls so as to keep back the surge and to prevent the floating rate from simply going through the ceiling. That has turned out to be a very wise and very effective piece of improvisation. My advice to the authorities is to do nothing more, save 'chinks' right there.

# The Relevance of Financial and Trade Liberalisation to Caribbean Development

**Professor Clive Y. Thomas, University of Guyana**

Mr. Chairman, because of the limited time at my disposal, what I propose to do tonight is to make a few general observations on the topic: adjustment, stabilisation and exchange-rate movements and then to spend the remaining minutes relating some of the experiences we have had in Guyana, so that you may benefit from the lessons we have had to learn, at very great social costs.

There are, as far as I'm concerned, four central benchmark ideas which should guide one through the morass of the issues raised in debates about stabilisation and structural adjustment. The first of these is that contrary to public opinion, adjustment and stabilisation issues are not a 1970s or even a 1980s invention. Countries have always had to adjust, including the Caribbean territories. In fact, when we were fighting for independence, the colonial monetary arrangements of the time, under the rubric of the Currency Board, were premised on two views. One was that a colony could not have a balance of payments problem, and the second was that a government would not be able to run an unsustainable budget deficit. Economists at the time argued that a colony under the Currency Board system would have neither external nor internal imbalances.

A lot of intellectual effort had to be directed at proving the fallacy of this reasoning. For the truth of the matter was that while on the surface the external accounts were "balanced", and internally the governments had no discretionary authority to create a deficit, real adjustment and stabilisation were nevertheless taking place. Our parents and grandparents had to pay the price in reduced incomes, starvation wages and depressed levels of living. Indeed, the lack of local discretionary authority to alleviate these defects of the Currency Board system was a very important motive force in the anti-colonial struggles of that period.

I think we therefore need at the very outset to understand why, if we have always had to adjust, this issue is being presented to us as a phenomenon of the 1970s, 1980s, as well as the 1990s and indeed threatens to be with us in the 21st century. The answer, I believe, lies in the fact that adjustment and stabilisation are now being presented with a very narrow focus designed to achieve certain strategic objectives. These are, first, to clear the external financial indebtedness of the South to the North, which we know as the "debt crisis". Second, there is the intention to ensure that the

maladjusted countries of the South as well as other economies there are fully integrated and/or reintegrated into the world system. Concurrent with achieving this, the aim is to remove any historical or moral challenges to the present operations of the international economy. If you recall, such challenges were very popular in the late 1960s and 1970s when many countries in the South and leading politicians including those in the Caribbean were speaking about a New International Economic Order and "disengagement" from a world economy which had "historically underdeveloped" countries of the South.

Third, what is being sought is a method of ensuring that the pattern of distribution of income which lasted up to the 1970s is changed. This was based on a social contract which operated for long periods (I would say at least for 30 years) which gave the workers a right, almost an automatic right, to share in technical progress and productivity gains of the so-called "Golden Age", that is, the 30- to 40-year period of tremendous expansion of the global economy which lasted up to the early 1970s. The aim also is to remove many of the welfare programmes of the state, and with it the earlier presumption that welfare compensation to citizens was due as of right. Linked to this are the twin goals of promoting the ascendancy of the private sector as an engine of growth and at the same time, the market as being universally efficient and "user friendly". These goals mark an almost complete reversal of earlier attitudes. Indeed, the presumption of "market failure" underwrote many of the initiatives of regional governments to intervene in the economic processes.

In sum therefore, the first benchmark idea is that countries have always had to adjust and what is new, are the different configurations which are deemed "appropriate" for governments to pursue in adjustment programmes. Those configurations which we do not have time to develop, boil down to the desire to impose a particular pattern of development on the world economy, in response to the threat posed earlier by the independence movements and the existence of a "socialist community". The latter of course is no longer with us.

The second benchmark idea is that the current pattern of adjustment is being presented to us as if there is no alternative. The intellectual basis on which this is premised is that first of all, a country has a problem of adjustment because the country as a whole is trying to live beyond its means. It is trying to purchase from abroad more than it is selling and therefore it has an external imbalance. Coupled with this and reinforcing each other in a dynamic way, is that governments too are living beyond their means, that is, trying to spend more than they're raising in revenue, thereby creating budget deficits and *ipso facto*, internal imbalance.

This logic is very persuasive because the bottom-line consideration is that this is literally true. This viewpoint has grown to the point where it has now become a dominant paradigm, the hegemonic set of ideas which rule economic science. I'm sure if I had asked most of you in this room about this view before this presentation, a majority would have supported it.

The postition is often taken that the manner in which adjustment takes place is nowhere as important as the fact that it ultimately has to take place. When posed this way, adjustment looks like something new, unique and peculiar to this particular historic period. It fails, however, to realise that once countries have to deal with each other, or that communities of people involved in exchange do not live in a single, homogeneous space, that there will always in fact be problems of adjustment. How this adjustment takes place is clearly vital, since economic policy cannot disengage from the choice or preferences in the distribution of adjustment among economic, social and political groups.

As an extension of the above, it is sometimes argued that there ought to be no *a priori* preference as to whether adjustment policies are pursued on the basis of an expansion of output, or the contraction of consumption in the short run, or some combination of both, as the only compelling logic is that adjustment has to take place.

The third benchmark idea which I use as a guide through the literature on adjustment is based on recognition of the fact that in practice the position outlined above has come under tremendous pressure. One has only to bear in mind the problems of environment and adjustment; women and adjustment; human rights and adjustment; trade-union rights and adjustment; indigenous peoples and adjustment and youth and adjustment. This catalogue can go on and on almost indefinitely. The point, however, of all of these examples is that the very set of dominant ideas which claims that there is no alternative to adjustment, ends up by having to recognise by dint of practice and experience, that tremendous social costs are associated with adjustment and these cannot be ignored. This has led to an "accommodation" with the call for "adjustment with a human face". Social adjustment and impact amelioration programmes are increasingly being appended to macro-economic adjustment and stabilisation programmes.

The fourth and last benchmark idea which I want to touch on is: what would be required to make another option valid? Because present practice stems from the dominant paradigm of ideas, there is almost a sense of resignation among many people as to whether it is worthwhile to challenge it. Many who feel this way are themselves practitioners of IMF/World Bank adjustment policies, who are not convinced, either intellectually, morally or otherwise, that there is virtue in what they are practising.

This shows the power of the paradigm: that people are servicing it, may in their heart of hearts not believe that it is based on any intellectual integrity, yet feel constrained nevertheless to support it. I have encountered this situation many times in my own country. I believe that very few of the major actors implementing adjustment programmes believe in what they are doing. Because of this situation, I think that the development of alternatives is not only a question of vision and devising programmes which meet the specific needs of particular countries. It also has to be supported by social forces which would give the alternative a real chance of challenging both the ruling ideas and ruling interests. Is there any prospect of this? The answer is that some international and regional agencies are challenging the present orthodoxy emanating from the IMF/World Bank. This is supported by important sections of the NGO, trade-union movement and other populist movements around the world and in the Caribbean. It is only here that mobilisation is taking place around alternative options.

In sum, therefore, the capacity to develop and implement alternative approaches to stabilisation and adjustment do not rest only in the intellectual power and clarity of thought behind these alternatives, but also in the social and political forces which can be mobilised around them.

As indicated at the outset, for the remainder of my presentation, I'd like to speak a little on what can be learned from Guyana's experience in its exchange-rate float. The first observation I would make is that the circumstances under which Guyana's exchange rate was floated is somewhat different from yours. Lloyd Best referred to your learning from the Jamaican experience, but the Jamaicans when they come to Guyana tell us that they are seeking to learn from our experience! We have therefore to be very careful. Guyana did not seek to follow the Jamaican experience. In truth, by the time our exchange rate was floated, the Jamaican auction system had effectively collapsed. It was no example to follow! The IMF had by then come around to the view that a free float was the best option and they indicated this to the authorities. Time does not permit it, but if one examines the course of IMF thinking, you would find that right up to 1990 (see their journal *Finance & Development* ) the view was being expressed that flexible exchange-rate systems could not work in developing countries! What has happened over the past two years is a remarkable turnaround.

When Guyana started its float, the economy was still experiencing a secular fall in real income; unprecedented deterioration of its physical and social infrastructure and double-digit inflation rates. It was estimated by the IDB that about 80% of the population was living below the poverty line. The black market and a parallel economy was estimated to range between about 33 and 99% of

GDP. Indeed, we had a situation in which the current absolute values of exports and imports in 1992 were less than what they were two decades ago! Of course we also had political problems, as you are all aware. The context therefore was quite different from that facing Trinidad & Tobago today.

A second observation is that the degree of liberalisation of the exchange rate was from the outset far greater than what you are attempting here at the moment. What appears to be the case in Trinidad & Tobago is that while "freeing" the exchange rate, you have transferred the exchange-control function from the Central Bank to the commercial banks. In Guyana, exchange control has been virtually abolished. Trading in foreign currencies was opened up to the streets. Indeed, the large size of the parallel economy and the black-market economy for foreign exchange had already made the street markets the effective controller of the exchange rate. Floating the Guyana dollar gave *de jure* recognition to a *de facto* situation.

At present, all transactions, except a few like the foreign debt, pass through our cambio system. Under this system, you can literally go and buy whatever foreign exchange you want, when you want it. In practice, however, many problems exist. The cambios have been known to advertise buying and selling of foreign currencies at rates which they do not honour. Generally, they are always willing to buy your foreign exchange, but are reluctant to sell, suggesting that capital flight is significant. At times queues develop and a rationing system is put in place by the cambios in an informal manner.

As I have written elsewhere, the cambios do not always give accurate information; they sometimes even practise misinformation and disinformation. There were two episodes which I don't want to burden you with, in which they actually attempted to corner the market and control the rate by declaring that they would only buy foreign currency at discounts of 40% and more below the selling rate! This took place twice, in August 1991 and August 1992. They were hoping they could force sellers, particularly visitors who were there for a short while, to off-load their currency at that discounted rate.

Guyana's experience also suggests that the movement towards a flexible rate was for the government a means of "minimising" the political costs of exchange-rate management. In the present system, when the exchange rate changes, it is pointed out that it is the people in the cambio who are changing it, not the government. [laughter] Devaluation and its consequences are thereby removed from the immediate, direct responsibility of the government. What is happening here in Trinidad & Tobago might very well be the

beginning of the off-loading of this responsibility from the government and the Central Bank to the commercial banks!

Another consideration behind our float was the belief that the pressure to carry foreign reserves is not as great as under the previous fixed exchange-rate system because external adjustment takes place more rapidly when the exchange rate also adjusts. The truth is of course that adjustment still has to take place and traditionally this has been achieved at the real expense of a decline in real income of the community. Thus the rise in the price of foreign exchange in Guyana has priced many former buyers out of the market, because of the decline in their real incomes which accompanied the decline in the external value. Yet the authorities are claiming, "Look, we have no foreign-exchange problem in Guyana. You can get as much as you want." In fact people are priced out of the market; the price system now does the rationing, rather than as was previously the case: administrative decisions. Do not believe therefore that the problems have disappeared. The real difficulties of generating foreign exchange continue.

Finally, it is important to realise that the benefit which you gain from an exchange-rate float is only temporary. In a sense it is a synthetic benefit, if systemic changes in resource organisation and the development of real competitiveness are not achieved. There is no quick-fix solution to achieve these. With those words, I bid you good luck in Trinidad & Tobago.

## Eight Lessons of Liberalisation in Jamaica

**Professor Norman Girvan, UWI—Mona**

Mr. Chairman, let me just begin by thanking Dr. Ramsaran and the Regional Programme of Monetary Studies for inviting me to share with you the lessons of the Jamaican experience and giving me yet another opportunity to visit the *second* greatest little country on earth.

On the day after the decision to float the Trinidad & Tobago dollar was announced, the BBC called to ask if I would answer some questions about the Trinidad & Tobago decision and the Jamaican experience. As we went along I realised that they wanted me to say that the same thing that happened in Jamaica would happen in Trinidad & Tobago. I could not say that. I insisted that the conditions of Trinidad & Tobago are different from those of Jamaica and it was not possible for me to make any statements about what might happen here without more information about the situation. What I want to do in the time available to me is to speak of the Jamaican experience. I thought it would be useful to organise my thoughts on this around "eight lessons of liberalisation in Jamaica."

The lessons relate to (1) the liberalisation decision; (2) monetary and fiscal policy; (3) structural factors at the macro-economic level; (4) the role of the specific mechanisms in the exchange market; (5) the role of expectations and speculative behaviour; (6) the role and limitations of socially responsible private-sector behaviour (or in other words, the Butch Stewart initiative and its limitations); (7) the private profitability of liberalisation and (8) the social costs of liberalisation.

### 1. The liberalisation decision

The liberalisation decision in my interpretation was not an autonomous decision taken by the Jamaican authorities to improve the allocation of resources in the classic or orthodox textbook sense. It was a defensive decision which was more or less forced on the authorities due to the mushrooming of the parallel exchange market to a size which had become much larger than that of the official market. It was also due to pressure from the private sector and the international financial institutions, principally the IDB and USAID. In fact when the PNP came into office in early 1989, the only thing it had said about the exchange regime in its manifesto was that it did not believe in the auction. It believed in a fixed rate

with regular adjustments to maintain competitiveness and it went through three or four phases of exchange-rate management. First of all it continued the auction system inherited from Mr. Seaga until that became unmanageable. Second, for a period of about one year, it went onto a fixed-rate system with adjustments. Third, it started liberalisation with the introduction of an inter-bank foreign-exchange system. Then finally in September of 1991, it engaged in full liberalisation.

It lurched, or appeared to lurch, from one decision to another and one regime to another. In my view, what was a necessity forced upon it by certain circumstances which I'll come to in a minute was represented by the government as a virtue, although in fact it was in line with their ideological thrust at the time. It also became a politically convenient standard to use to indicate the proof of its commitment to the market model to which it had recently become converted with almost born-again fervour. To quote Mr. Manley: "You just can't improve on Adam Smith."

**2. Monetary and fiscal policy**

The lesson here I read to be that an expansionary monetary policy throughout much of the period preceding liberalisation created excess liquidity in the economy and thereby set up the conditions for the mushrooming of the parallel foreign-exchange market and speculative buying of foreign exchange. The government wanted to fuel growth through credit expansion and this helped to precipitate the liberalisation decision. Once speculative buying of foreign exchange in Jamaica had become out of control, and this is the other lesson of monetary policy, monetary policy and fiscal policy became virtually the only tools available to influence the exchange rate, and this through draconian demand compression.

I'm saying that we had a period of expansionary monetary policy which created a parallel market, or contributed to a parallel market, which helped to precipitate the decision to liberalise. Liberalisation having taken place, and the rate continuing to be out of control, the only tools left to the authorities were monetary and fiscal policy through draconian demand compression. Hence, for example, within a few months after full liberalisation, the government was pushing interest rates up to 50 and 60% on certificates of deposit issued by them. Liquidity ratios in the commercial banking system were increased to 50%. In addition to this the government was committed to a budget surplus on central-government accounts of between one-half and one percent of the Gross Domestic Product, even with one-half of public expenditure going to service the public debt.

**3. The role of structural factors**

Here I will highlight three phenomena. First of all, the high propensity to import – between 60 and 70%. In fact the Bank of Jamaica estimates that out of every dollar of credit expansion, something like 70¢ of additional import demand is generated. Secondly, the burden of external debt pre-empting 30% of export earnings in statistical terms, but in reality something like 50% of the cash inflows to the Bank of Jamaica prior to liberalisation. Hence, as Lloyd Best was saying, foreign exchange inadequacy is endemic to the system. Thirdly, I would mention trade liberalisation, which pushed up the demand for imported consumer goods.

**4. The specific mechanisms of the liberalised regime**

This is something which I think has tended to be under-recognised in much of the discussion about liberalisation. There are several examples I can give of this. Prior to full liberalisation, the Bank of Jamaica required commercial banks to sell 25% of their intake of foreign exchange to the Central Bank to cover payments on foreign debt and on petroleum. This was pushed up to 50% because of inadequate inflows. Now initially, the Central Bank purchased these obligatory sales at the weighted average rate of all the banks together. What did this mean? It meant that the largest banks, which control about 60 or 70% of the inflows, effectively set the rate, because the smaller banks could not afford to go too far out of line since they would lose on their sales to the Bank of Jamaica which reflected the weighted average rate. Essentially, this operated as a mechanism to contain devaluations, to contain the rise in the price of the US dollar. Of course, at the same time, in doing so, it inhibited the ability of the banks to compete with the informal market.

Eventually as a result of reduced inflows, the Central Bank decided to allow each bank to sell to it at the average of its own buying rate. This change in the mechanism set off a bidding war among the commercial banks, each one bidding against the others and therefore accelerating the devaluation.

Let me give you another example. Up to April '92, the commercial banks were in effect able to pay different rates for different transactions within the same day. A small depositor could come with US$200 and sell at the published rate for the commercial bank for that day, but a large seller could call the bank manager and say, "Look, I have US$100,000. What will you give me?" He would get more because of the larger amount. Now what this did in effect was act as an incentive for informal traders to go around and buy up US dollars at the official rate and sell to the commercial banks at higher, negotiated rates. It accelerated the *de facto* devaluations which were taking place. In April '92, at about the same time as the Butch

Stewart initiative, the Central Bank required all commercial banks to publish a daily rate and carry out all transactions at that rate -- a specific change in mechanism which also helped to stabilise the rate.

There are other examples I could give. One that I think should be mentioned is that though Jamaica has allegedly fully liberalised, you still hear talk about a black market there. The simple reason for that is that trading in foreign exchange is in fact legally restricted to licensed traders. So if I sell US dollars for Jamaican dollars to my friends, I'm committing a crime. That's an illegal act if I'm not a trader licensed to change US dollars and therefore by definition part of the black market. The liberalisation just taken place is still therefore within certain legal parameters.

**5. The role of expectations and speculative behaviour**

I think this is perhaps the single most important lesson to be learned, both as regards driving up the price of the US dollar and eventually bringing it back down after the so-called Butch Stewart initiative. Expectations and speculative behaviour in the Jamaican experience appear to have been highly influenced by the macroeconomic environment as well as by monetary policy. The experience shows that speculation influenced by negative expectations about the value of the local currency, together with excess liquidity can be devastating, can in fact set off a vicious cycle of self-fulfilling expectations. We buy US dollars because we expect the price to rise, and by virtue of the speculative demand, the price *does* rise and this itself fuels further speculative buying and on and on and on in a vicious cycle. In fact, the full liberalisation of September 1991 was precipitated by such intense speculative buying and hoarding of foreign exchange, which dried up inflows into the inter-bank system. That full liberalisation was aimed to kill speculation and win back flight capital, but it had precisely the opposite effect.

When full liberalisation took place, the rate was officially J$12 to US$1 and the informal rate was 16 to 1. Within six months, the official rate had gone to 29 to 1 because of this vicious cycle of self-fulfilling speculations which triggered speculative buying. Here the role of the legal foreign-exchange accounts became crucial. Exporters no longer had to bring back or to sell their money to the Central Bank. Anybody could go and open, and many thousands of people did open, foreign-exchange accounts in the local banking system. There's no restriction on the amount which you need to open, unlike the way it is here. People used these accounts to park their US dollars that they acquired from speculative buying and to sell them and buy them back and so on. The liberalisation actually

facilitated the speculative buying and it had the very opposite effect of what it was designed to achieve. This was one of the main reasons why liberalisation initially had these devastating consequences on the exchange rate.

**6. The role and limitations of socially-responsible behaviour**

Butch Stewart's argument was very simple. "This is self-destructive behaviour. Social instability is going to destroy the tourist industry. I am going to take the step of selling my foreign exchange at below the going market rate to stabilise the dollar and ensure that I have a market next tourist season." It worked. Nine months after the Butch Stewart initiative and of course it snowballed with many other people jumping on the bandwagon, inflows to the commercial banks and the sales of foreign exchange to the commercial banks were nearly 50% higher than they were in the corresponding period of the year before. That I think is a measure of not only increased inflows from regular exports, but increased inflows from flight capital which had been building up. The price of the US dollar went back down from 29 to 22.10 where it has remained in fact ever since.

I come to the limitations. In the last two to three months in fact, an informal market has re-emerged. Shortages of foreign exchange from the banks have re-emerged. Inflows of sales of foreign exchange to the commercial banks in Jamaica have declined and inflows to foreign-exchange accounts have gone up, because people expect a devaluation, or people expect that the rate which all the banks now observe will not hold. It appears one of the reasons for this is the increased demand for foreign exchange especially resulting from the reduced tariffs on motor-cars. The tariffs on motor-cars were slashed by about a half. Banks are now lending customers money to purchase motor-cars.

There's a sudden increase in the demand for foreign exchange and this has put pressure on availability. This has fuelled a new bout of speculative demand on foreign exchange. The consensus in Jamaica now is that that rate which has held for over a year can no longer hold. It'll go to at least 24 or 25, maybe higher. So socially responsible private-sector behaviour, and this is one of the unique features of Jamaica, did in fact kill speculation, influenced the rate and did influence the situation. There are limitations, however; if the overall macro-economic environment is conducive towards excess demand for foreign exchange then it will become unstuck.

**7. The private profitability of liberalisation**

One should just mention here that there are two very lucrative avenues of banking profit which liberalisation allows: foreign ex-

change trading and foreign exchange trade financing. At the hotel where I'm staying, the spread between buying and selling rates seems to be 10%. That is, they give you 10% less when you change your US dollars than what they charge when they're converting their dollar rate into TT dollars. The banks in Jamaica are now amongst the most profitable of the firms as a result of foreign exchange trading and lending of foreign exchange from foreign exchange deposit accounts. They are allowed to lend out 50% of the money deposited in their foreign exchange accounts for trade financing. Banks are now busy buying up hotels in Jamaica, and effecting mergers and acquisitions and every day you're seeing the indicators of bank profits.

**8. The social costs of liberalisation**

There are just two points here. One: that because of the impact of the exchange rate on the price level, liberalisation which results in devaluation triggers inflation and big increases in the consumer price index. When we look for example at the relationship between the minimum wage in Jamaica and the cost of feeding a family of five in December 1989 before liberalisation, the minimum wage could purchase about 40% of the basic food needed to feed such a family. By December 1991, two years later, after liberalisation that relationship had halved. The minimum wage could now fund just 22% of the basic food basket for a family of five. That was December 1991 before many of the resulting price increases had occurred. The immediate effect, of course, is to push large numbers of people below the poverty line.

There is another factor which again I think tends to be underplayed. When devaluations take place, the cost of servicing the foreign debt in local dollars goes up in similar proportion and therefore that portion of the foreign debt which is borne by the central government increases in local dollars. In your situation it may be a little different because you also earn income in foreign exchange from the oil sector, but in Jamaica, this has been devastating. The cost of servicing the foreign debt as a proportion of public expenditure increased from 37% to 50% in two fiscal years. For the fiscal year just ended, 50% of total public expenditure was used to service the public debt, partly because of devaluations, and partly because of the high interest rates on treasury bills as a result of the restrictive monetary policy needed to dampen demands for foreign exchange. This has resulted in further cuts in the real expenditure on education and health and security which have become seriously run down in recent years in Jamaica. This social cost is one that has to be taken into account.

My conclusion based on our experience is that in an economy such as ours, government cannot abdicate responsibility over the management of the exchange rate. Indeed, even if it wishes to do so and it says it has done so through liberalisation, our case proves that with liberalisation setting off a frenzy of speculative buying and devaluation, the government, like it or not, had no option but to adopt tools aimed at influencing the exchange rate, that is the tools of monetary and fiscal policy, since its direct control had been relinquished. So whether it likes it or not, it will have to do so and again, the question is: by what means? The exchange rate, as the point has been made, is *the* single most important price in our economy. It is basic to the standard of living and it is also basic to all economic transactions and therefore governments have no alternative but to influence it in some way. Thank you.

## Discussion

**Professor Bourne**

I am tempted to make one comment supplementary to what Norman Girvan was saying about the Jamaican experience. It is on the question of the attempt by the monetary authorities to restrain any depreciation of the exchange rate by mopping up liquidity through the issues of certificates of deposit at very high interest rates. This was a dismal failure; it didn't work. It is also really the business of engaging in a sucker's game, because the banks always benefit in that situation. It results in the gross indebtedness of the Central Bank, virtually to the point of bankruptcy, as happened to the Bank of Jamaica, ending finally now in some desperate attempt to transfer those liabilities of the Central Bank to the Ministry of Finance, just to clean up the books of the Central Bank.

Just in case you believe that this is a Caribbean peculiarity, much the same thing happened in the Philippines when they liberalised their foreign exchange market and attempted at the same time to prevent the depreciation of the peso. There too, the Central Bank issued large quantities of Bank of Philippines bonds at increasingly high interest rates to try and mop up liquidity in the system to restrain demand for foreign exchange. There too, the Central Bank at the end of a five to eight-year period was pretty much bankrupt, thereby paralysing its ability to conduct monetary policy in the future. It necessitated in that case, certainly up to early last year, some discussion about shifting those liabilities to the Ministry of Finance, to clean up the books and make the Central Bank financially viable. So, the one thing one has to avoid here at all costs is Central Bank intervention through issue of high interest-rate bonds to mop up any liquidity in the system. That is a sucker's game, as I said. Now let me invite questions from the floor.

**Mr. George Hamel Legall, Former Permanent Secretary, Ministry of Energy, Trinidad and Tobago**

I want to congratulate the organisers of this discussion and of course the three panelists, these three great West Indian political economists. I want to address the topic by going back ten, fifteen years ago when we had plans for developing an aluminium smelter in Trinidad & Tobago, linking Guyanese and Jamaican bauxite with Trinidad's natural gas for cheap energy. Trinidad & Tobago as a few of us here probably know was third in energy resources in terms of ranking on a per capita basis a few years ago. It was on that

basis I believe that Dr. Williams way back in the mid-70s and the early 80s moved together with Jamaica and Guyana to establish an aluminium smelter. In those days, Dr. Williams spoke about our planning horizon being 40 years. In other words, 5-year plans were out; we had at that time natural gas resources to take care of our needs for the next 100 years. The situation has improved in terms of reserves since then.

It is in that context that I have come to see our problem of foreign exchange as due in large measure to the way we manage our resources. In point of fact I refer to a contract which was signed in November 1991 for a 20-year supply of gas to this country, by which AMOCO will provide it with some 350 million cubic feet a day. This is virtually handing over to AMOCO a monopoly of the supply of gas to Trinidad & Tobago for the next 20 years. Based on that contract, this country receives a cent and a half TT at the then rate of exchange for the next 20 years. A cent and a half per 1000 cubic feet. The contract starts at US$0.90¢ and escalates 5% to about US$2.20 twenty years from now. Twenty years from now, we will still receive a cent and a half TT, whatever the floating rate is. To give an idea of the magnitude of the contract we're talking about, I should indicate that it will bring revenues to AMOCO of something like US$5 billion, out of which this country will receive TT$36 million.

The point that I'm trying to make is that we're talking about Caribbean development and yet the countries of the region are placed in a situation where our own institutions are facilitating our exploitation by sponsoring and by being patronised by these foreigners. It's a long story and I can cite even more recent examples, but I want to pose my question now. If we so mismanage the development of our natural resources, how can we escape the clutches of the IMF, the IDB, the World Bank, the money-centred Paris Club banks with their conditionalities and the trade liberalisation agenda with the government of this country playing the role of facilitator of the foreign private sector? Thank you.

**Unidentified speaker**

Mr. Best, the government has stated quite emphatically that they are working towards full liberalisation. Are you satisfied that the mechanisms in place, the structures that exist at present can handle the impact of full liberalisation? If we work toward full liberalisation within 6 months, what do you expect the impact will be on the foreign exchange?

**Dr. Anthony Gonzales, Senior Lecturer in International Economic Relations, IIR**

I wanted to ask Lloyd whether he could tell us specifically what type of management he's looking at in terms of the exchange rate. You said that 5.75 is a relatively low rate and that it could only be supported with exchange controls. Now the parallel rate was something about 4.50. We as yet do not know what the real equilibrium rate is. I have always said there has been a fair amount of foreign currency in this country. The government said it commissioned a study which showed on the basis of the flow of foreign exchange that it was sufficient to support the rate at a certain level. I haven't had access to that study so I can't really say. I've always argued that we needed a stock of reserves to really make the float successful. On what basis are you suggesting that that rate is a low rate in terms of the experience of the country and the availability of foreign exchange?

**Unidentified speaker**

All the panelists seem to suggest that the government should attempt to manage the exchange rate. Let's assume that in the future they don't. Everybody also mentioned the concept of international competitiveness. My questions are: one, can we as a region or as individual countries be internationally competitive? Secondly, what mechanisms would you suggest or recommend for creating this international competitiveness?

**Mr. Best**

There are three questions. One, preconditions to a liberalisation; two, specific arrangements for managing; and three, equilibrium rate, was it low or high? I want to take the last question first because I think we need to make some estimates of the extent of excess demand on the assumption that if the excess demand is high and we do not have perverse effects, a higher rate will be required to bring the market into equilibrium. If the excess demand is low, the converse will be required. I have made some estimates here on what was likely to be the level of demand on the morning of Tuesday, 13 April and I'll give them to you. I looked at the level of time and savings deposits in the commercial banking system. I looked equally at the outflow of capital that preceded the decision, and as you know, as announced by the Central Bank, there had been an outflow of the order of US$200 million a year of capital flight.

There had of course been oscillations in this fleeing of capital and there were two critical periods. One, in the crossover from 1991 to 1992 and the other in the crossover from 1992 to 1993. It was not

a steady outflow. There were, as I said, oscillations, but we have the average over the period. The question is whether there is likely to be some acceleration in the outflow with the decision taken. I looked at the time and savings deposits and found that at the end of 1992, there were TT$6.6 billion in the commercial banking system only. Of course, a proper estimate would have to take account of time and saving deposits in all deposit-taking institutions. This is therefore something of a minimum figure. I first applied to it the import ratio, which is to say the amount spent on imports as a proportion of GDP at market prices, which is obviously a bad measure, because it's really more of a consumption measure. That gave me a figure which I rejected. Then I just applied some percentages, arbitrary percentages, 10, 15, 25, 30% to get an idea of what would happen if people decided to switch their preference from local assets to foreign assets at a certain level of preference.

I found that with a 15% shift of preference from holding time and savings deposits in Trinidad & Tobago in TT dollars, to holding them in US dollars, there would be an outflow of about $75 million a month. We could play the numbers across, and I have details on this. The point I am making is that by any reasonable estimate, it was clear that on the morning of Tuesday, 13 April 1993, there was bound to be a huge excess demand for foreign exchange. Therefore the question was posed: what rate of intervention was likely to deal with this? Especially given what I had said earlier, that the Central Bank had indicated at the press conference, when its representatives announced the decision, that they had no free or spare reserves with which to bail the commercial banking system out, if there proved to be a deficit on the morning of the opening of the new regime.

I thus asked myself what rates of exchange the banks might apply. Clearly there was a floor; $5 was about the parallel rate at the time and it couldn't be lower than that. $6, $7.50, $8... $7.50 was an interesting figure because $7.50 was a rate at which on certain assumptions the fiscal effect would be just equal to what was required to pay the public servants and so on. You could play with the numbers as you like on all kinds of assumptions. There is no doubt but that when you look at the level of excess demand, that 5.77 is a comparatively low rate and could be sustained only in the context of a retention of the old arrangements, which is what they have done. Now, saying that helps me to answer the second question, which deals with the preconditions to liberalisation.

Of course, I mentioned in my talk that both the fiscal and monetary conditions have to be congenial if the liberalisation is to work. If you do have constraints on your deployment of foreign exchange by debt, it weakens the capacity of the authorities to intervene in the market to defend rates. If you have loose monetary

Jamaica, even if you have tight arrangements, the problem is more problematic than it seems, because the right decisions to intervene could lead to the wrong results if you get a perverse effect, from which I abstracted at the beginning. If for example you use monetary instruments, above all your interest rate, to curb excess demand and people conclude because of the high interest rates that prices will get higher and you get the cycle that Norman talked about, then you'll get an accretion of excess demand. There's no equilibrium rate that can be even envisaged under that context.

I say that because the problem is not so much the preconditions although those exist. That is why I said that my regime would be process-centred and not product-centred. It is not the end product that you anticipate in terms of the reflows of foreign exchange through repatriation, through resurfacing and through new investment. That is not the important thing. It would be lovely if you could get it. It's a beautiful mirage at the end of the line, far away in the desert. What is important is how you are going to get there. Therefore the real question is: how do you organise the transition from when you start to these beautiful conditions you anticipate when you bring the system into equilibrium? What I am putting before you and what the evidence is clear about is that we can't get past the transition. We have to ask the question: when the time comes for us to remove the arrangements, will the public's asset preference for foreign assets over local assets be greater or less?

I don't know what the answer is, but in the surrounding context, I know the culture I'm dealing with. I know the society I'm dealing with. I gave you an idea of what it was; I gave you conjunctural factors; I gave you structural factors; I gave you historical factors which determine the preference people have for foreign assets over local assets. When I came back from Africa I went to Sangre Grande and a man told me something I've never forgotten. He said the problem with Trinidad is people live here as if they're on holiday. Williams called us a bunch of "transients" He was getting at the same point. He has a very strict reference to people's asset preferences. If Trinidadians have the choice of holding US dollars as against TT dollars, you better believe they'll hold US dollars anytime, especially when the policies of the government are having a negative effect on income and welfare and prices. People will think that the policies have no credibility; that's how they'll judge it. Maybe economists, maybe businessmen would judge the credibility of public policy in terms of what they say the impact will be on the aggregate. The man in the street will judge it in terms of what happens to income and prices. The policy will have no credibility if it's hitting him that way and in that context, I think the consequences are clear.

Your final question is about arrangements for managing. I don't know what these arrangements will be. I would grope, because there is no rate of exchange at which the system could be brought into equilibrium in my mind. If people are changing their asset preferences in relation to availabilities which is problematic in relation to policy credibility and in relation to the political situation in general, there is no equilibrium rate which can be envisaged under that situation. Therefore you have to play it by ear. I would keep the existing exchange controls and I would manage them quietly, without fanfare. I would ration foreign exchange to make sure the investment priorities of the country are serviced. I would consider myself lucky to have a country in which the foreign exchange accrues to the state and accrues to the state in a steady flow in which the vast proportion of foreign exchange earned by the country is owned by the state, whose biggest transactor is the government. That gives us a lot of room to play. I would take account of the fact that it's not a country that trusts the market. I said so before. I would take account of all of these things and I would run a fairly open regime. I would not be very tight as we've been doing in fact in the past. I would accept the parallel market; I would accept that there would be some capital flight but I wouldn't relax the hold on the system and I would say like Napoleon, "On s'engage, et puis on verra."

**Professor Bourne**

I'll invite Professor Girvan to join the debate at this point and then I'll ask Professor Thomas to comment, but before I ask Professor Girvan to speak, I wonder if I should yield to the temptation of saying to Lloyd that the people also do not trust political leaders.

**Professor Girvan**

I think it is probably fortunate that our technicians and politicians were not able to get their act together with respect to the smelter project. I say this because in the 1980s, the aluminium market has been very volatile. Prices have been going up, prices have been going down and independent smelters that are not owned by multinational corporations which guarantee the market for the output for the smelter have been faring very badly. In our situation it is quite possible that the smelter, had it been built, would have been caught in a vise with a heavy burden of interest charges on its debts but facing a highly volatile market, since independent smelters take the lowest price when the market goes down. I think you've had your problems here with these large capital-intensive and debt-ridden projects. I don't think I need to say any more.

I agree with Lloyd in answer to Peter Gonzales that there is no equilibrium rate. There *cannot* be any equilibrium rate, where there is a high speculative element. Each time a rate is established which might appear to clear the market, once the price of the scarce commodity is going up with each successive 'equilibrium', there will be grounds for expecting further increases, which adds to speculative demand. You're really trying to hit a moving target.

I think however the third point, the question which was posed about international competitiveness is really at the heart of the matter. Management or no management, there can be no stability in the exchange rate in our situation without a strong and sustained growth in exports. That is really the root issue that I think we need to deal with in the medium and long term, and in the short term too. The question was if we can become internationally competitive as countries or as a region, and secondly how we can achieve it. Let me give my brief answers. To the first question, yes. I think we can become internationally competitive. How? I would list four or five instruments.

First of all, by investing in human resource development at the national level and by training and upgrading of workers' skills and productivity at the firm level. This requires a commitment not just of the national leadership but of managers and owners of industrial enterprises and enterprises in general towards their labour force. Two, by an industrial policy which identifies certain key activities for investment, innovation, and product development through joint and cooperative action by the state and by the private sector. Three, by a strong and overriding political and social commitment to wage and price stability. Four, by a social contract which guarantees all social partners a reasonable and just share of the national pie. Finally, by a culture of discipline, thrift and hard work. Very easy.

**Professor Thomas**

If we keep going as we have been, I wonder if we'll get more than these three questions in! I just want to make a few very, very brief comments. First to the very last question. I think it starts from the premise that if a country is higher-cost than every other country in producing everything, there is no basis for trade. The principles of specialisation still allow it however, or make it possible for you to engage in trade fruitfully. As Girvan was suggesting, what we need to develop is our particular brand of specialisation. Everything we produce in the Caribbean could be produced more cheaply elsewhere and there is still a basis for trade, because trade is based on the principles of specialisation. If you have here the best typist and the best doctor in one person, you're not going to let the person

work as a typist; you'll let him work as a doctor. It's these principles of specialisation which operate and I think we need to know it.

The second point I want to make very briefly is that we're talking about liberalisation and the first question that was asked had to do with integration. I just want to make the observation that there is also a liberalisation view of integration which sees the integration of countries of our size and our characteristics as anachronistic. The new orthodoxies arising claim that there is no need to talk about integration of countries like ours. There is of course the larger movement of NAFTA which may be the final embracing device.

The final point which I want to make however, more important than either of the other two is that I believe that there are certain points that have come out of the Guyanese experience that you should take into account. First of all, I'm convinced from what has happened here that there will be increasing liberalisation of the rate. That is, other licensed dealers will emerge and you'll eventually get to a situation where there is almost off-the-street trading for everything. This market will eventually "clear" at some level where the dominant buyers and sellers are comfortable. Many of the buyers, maybe many of you in this room will have to leave the market because of falling real incomes and rising prices. You'll be rationed out by price. Capital flight will take place until two things happen: the pent-up stock of income and currency that people have here which they were not previously able to get out at a convenient cost is cleared out of the system and secondly, until businesspeople and those who have foreign exchange or engage in economic activities here settle the level where they have an asset balance between funds that they want to hold abroad and those at home and those at home generate more at home so that they can send it abroad. That's the scenario that will eventually happen.

All prices will eventually tend in some sense to reflect world prices, except two very critical prices. One will be your wage and the second will be the state assets that are being sold off in privatisation arrangements. In terms of the preference, I think at this point in time my own suggestion would be that the government should not let the rate float without any sense of guidance in terms of targets. It should have some view, some concept of where the rate is likely to settle down and that rate ought to be part of the government's stated intention and policy. What has happened in Guyana is that there is no informed position taken by the government. It surrenders itself to the market; it never talks anymore about what the exchange rate might be. That in any case was the political temptation that led them to this route and you might very well find the same thing happening here.

**Unidentified speaker**

I want to compliment the panelists for very lucid presentations. I want to focus on the position of the credit union movement. In the context of Trinidad & Tobago, one of the regulatory mechanisms is the Cooperative Societies Act of 1971, which restricts the interest rate in terms of lending to 12% per annum, and the dividend in terms of returns to the members to 8%. I would want to hear from Brother Girvan and Brother Thomas what impact the economic liberalisation has had on the cooperative sector in Guyana and Jamaica with specific reference to the credit union movement. What can one anticipate in the Trinidad & Tobago context, given the fact that the interest rate will be going up and credit unions will now have to compete on the so-called 'level playing field' with other financial players? Thank you.

**Unidentified speaker**

First of all, I'd like to thank the organisers for bringing three countries together on the same panel to discuss monetary issues in the Caribbean. What I want to say basically is that flexible foreign exchange rates, inflation, devaluation and interest-rate structures are monetarist issues as distinct from economic issues. It's a sort of specialist area. Given that decisions are being taken by monetarists, while comments, views and analyses are being made by economists as this panel is now doing and given that there are representatives from Jamaica, Guyana and Trinidad & Tobago, has anyone on the panel participated in attempting or completing a computerised, in-depth monetary analysis on the economic and monetary database existing in these countries, given the importance of high technology, global communications and the use of advanced monetary cybernetics in the information age of the 1990s?

**Mr. Mitchell**

At the last discussion on this topic I said that we should revert to the old system before the tragedy of Guyana, Jamaica and Venezuela. Revert to it in a much more serious way than Best is talking about and go back to the old system and fix it 10 to 1. Now, let me add one thing. There is a perception in Trinidad & Tobago that being an oil-exporting country, we would not suffer the same pain. The Venezuelan experience gives the lie to that. Venezuela has moved while I lived there from 2 point something to now 80 bolivars to the dollar, with all the accompanying hyperinflation and all the negative social effects. Growth, however, has been at 8 — 9% despite that. Despite that, of course, a lot of the people have gone below the poverty line.

Now I have had the advantage of not only living in Jamaica but I am now in Guyana, and I'm seeing the social impact of amelioration programmes. I've seen the civil servants, as the professor said, move below the poverty line. I've also seen a very strange thing: the Minister of Finance borrows or gets a grant from the World Bank in order to beef up salaries and bring people above the poverty line. Now, I am begging, I am begging the political directorate to stop the foolishness which is tantamount to tremendous speculative activity on a kind of roller-coaster. Stop it! Revert to the system. Not half-way as the professor said. Stop it and go back 10 to 1.

**Unidentified speaker**

Mr. Best, you set the tone for your address by describing these events and subsequent effects as being "Blue Tuesday", a plot and a conspiracy. However in closing, you did lend tacit support to these policies by indicating that the authorities should continue chinksing. What I would like to know is: do you see anything positive in all of this? Do you really believe, given the kind of recent experiences of the CARICOM countries with regard to setting even a simple thing like the CET, that we in Trinidad & Tobago could go on our own by taking charge of our destiny in this present scenario?

**Mr. Best**

I'll take the last question first. Of chinksing, and the reason I proposed that the monetary authorities, the Ministry of Finance and the Central Bank stay where they are now in the first instance is that they have not floated the currency in fact. They have half-floated it, I suppose. Somebody called it a "fixed float". What I mean is that they have retained the essential controls of the exchange regime and I think that makes a lot of sense. I also thought it made sense at the particular conjuncture to devalue the currency or to let it depreciate, because although we do not know the equilibrium rate, we know that the price is too low. My friend here has suggested 10 to 1, I don't know whether that's a good rate. I think we've been caught by the fact that we have intervened too late.

I proposed in 1982 that we devalue then, when we had foreign exchange in abundance, when we had energy in abundance, when people were not tired, when we had savings, when all kinds of things were present. Well we lost 10 years and now really there's almost nothing you can do with the rate that will help. People have become cynical, people have become tired, we have no foreign exchange, we have used up our savings potential, our foreign potential, and therefore we have a debt problem. We have rescheduled the debt, we have used up all the options and now it's extremely difficult to do anything at all. So I would stay there and

try to control excess demand and I would manage every morning in a way that attempts to restore confidence. I have said however that confidence does not depend purely on availabilities of foreign exchange. It depends equally on the policy environment and the way people regard it and the political and social environment and the way people regard that.

The great difficulty now is in the question somebody asked: will all wage earners now attempt to index their wages in relation to prices and interest rates? That's the vital question. The answer clearly can be no. Here again, the failure of both the technocratic and the political élites to state the problem clearly at the beginning as I have said over and over is now a problem. They ought to have told the country a long time ago from the start that the decline in petroleum earnings involved a decline in the level of activity which could not be avoided. There was no choice about it. Nor was that all. There was also no turnaround in sight. It's just nonsense, this talk about turnaround. What the system was going to do was to settle at a new equilibrium which could be sustained by the new level of foreign exchange. As Clive Thomas said, it was not the first time either that we had to adjust downwards over the long historical span. Once you understood that, that the adjustment could not be avoided, once the country understood that, the next thing was to get a scoreboard by which all the sectors in the country could judge their own situation in relation to what is happening in the nation. Thus, if the nation is 50% poorer, as it is now in 1993 than it was in 1983, how could anybody expect to be only 10% poorer?

We ought to have a policy of a safety net which shows that those at the bottom of the spectrum should take a lesser downward adjustment than those at the top. There needed to have been a discussion in the country a long time ago about the impact of the fall of export earnings on real income and its distribution and the problem of distributive justice had to be put properly on the table. So far as we could have addressed it scientifically on the basis of the data, we could say to teachers, "You have only dropped 40%; everybody else has dropped 50, so we can't pay you the arrears." That would make sense. Don't tell them, "We go give you your correct salary."

Everybody is fooling everybody, because we won't bring onto the centre of the table what the problem was and what the consequences were for everybody and pose the problem of equitable distribution of the burden. I would not be surprised if AMOCO workers who are earning in dollars, whose employers are earning in dollars, pose the problem of liberalisation of wages and say, "We want to liberalise our wages, we want free bargaining for wages and we want to be able to conduct our transactions in foreign exchange". If you are liberalising, it follows logically. They can do

that, but it would be subject to the limitation I have posed earlier, which is that we have to have some notion of what has happened to average income in the country and nobody should really get more or suffer more than the average.

The third thing is growth and Venezuela, which is not unrelated to what I have just been saying. Since the problem posed by the decline in foreign exchange was that the level of activity was likely to settle at a level which can be sustained by the new injections of foreign exchange, the logical management question that arose was, and I have posed it a thousand times without getting a response from the political directors of the country, was there anything we could do to raise domestic output without any spillover into the balance of payments? It's logical. If the level of activity that you can now sustain is governed by the availability of foreign exchange, then the logical question is: is there any higher level of activity which can be sustained without the intervention of foreign exchange? We therefore have to look inside the country and see what goods and services we can produce and supply for ourselves without having a balance of payments effect on the level of foreign exchange required, though it would obviously have an effect on the deployment of foreign exchange among competing claims.

I have proposed a thousand times that the answer to this is to raise the output of agriculture. I know that there are problems of agriculture with foreign exchange; I won't wish those away. I think however that on balance, the foreign exchange effect of an increase in agricultural output will be an impact on distribution and patterns and structures and not necessarily on levels, because agriculture has the potential for substituting for imports on a huge scale, as well as earning export earnings even in the short run. To the extent that the potential of agriculture for raising output without further complicating the balance of foreign exchange is positive, I think that the Venezuelan experience can be duplicated here to some extent. Trinidad & Tobago is not Jamaica; Trinidad is not Barbados in the sense that the amount of idle land and the pattern of its ownership, state ownership for the most part, admits a level of intervention in agriculture in Trinidad which is not possible in Jamaica.

Jamaica has gained a lot from the fact that it does have this big rural sector. When people in Kingston had problems, they could make alliances with their cousins in the countryside and get outputs that they could sell in the town. With this they can raise their price every day. The problem with wage earners is that you can't raise your wages every day, but if you have things to sell from the countryside, then you can, and that was important in Jamaica as a safety net. Trinidad does not have that safety net. Most of the people here are urban people; they have nobody in the country. Even the people in the country are more specialised; they're not like in

Jamaica, planting every little thing and so on. There is no question of being able to feed yourself on your own farm in Trinidad. Thus we have negatives from agriculture in that we don't have the large Jamaican thing.

On the other hand, land is owned by the state; Caroni is owned by the state. The whole country is open, because everybody's living on the continental shelf in Trinidad, on two roads, from Diego Martin to Sangre Grande, from Port of Spain to Point. The whole country is open. The potential for a rapid increase in output in the agricultural sector is much larger than people think. The result could be like Venezuela, though there are complications, because to make all of that possible, you need a framework of administration, of taxes, of all kinds of things and Trinidad & Tobago has failed to develop the municipal framework that is necessary for that. I know that's a limitation, but I don't think it's a limitation as severe as people say, if we take it that the important thing is not the product down the road, but the process. The important thing is to embark and to let the population perceive that their own intervention makes a difference. That is what will create the space.

The moment the population sees that its own intervention is making a difference to income and employment and to the whole outcome, you get time, which is what we need. You get confidence back; you get policy credibility back and that brings me back to my earlier analysis, of course, so the thing makes a picture. I am not pessimistic at all; I am extremely optimistic about what is possible. What is important is that the country learn something from this experience, that the country discerns the mistakes that we have made, discerns, coming third in the line, the mistakes that Guyana made, Jamaica made and so on and rise to the occasion by education and self-education, which is what we're doing here. I therefore want to close by thanking the organisers of this occasion for making it possible for us to educate ourselves.

**Professor Thomas**

In my final comment, I'd like to take the opportunity to thank the organisers for arranging this event. What I've chosen to comment on is the question that was asked in relation to the computerised models in the Central Banks, Ministries of Finance and so forth. I make the observation that we have in Guyana no indigenous or original computerised models in the Central Banking system, the commercial banking system, the Ministry of Finance or even in the State Planning Secretariat. Those which are used are largely derived from the IMF models, and we know what those are. I however do not believe that you can separate monetary analysis and the things that we've been talking about from other real dimensions of life in

the region. Money is not only a financial asset; even the neo-classicals, the orthodox economists would tell us that. It's also an oiling mechanism for real transactions. You can't really ever I think separate it from ongoing activity in the country.

I think this is dramatically evident if you look at some of the circumstances we have in Guyana. For example, the foreign debt is US$2 billion. On a per capita basis, it's probably the largest in the world for any country that has a significant debt. I call a debt significant if it's over US$1 billion. The servicing of this debt takes up 94% of tax revenue and somebody talked earlier about 50% in Jamaica and shouted in horror. Solving this problem is clearly impossible without a political input. There's no way that this can be resolved without a political input that involves the major countries we're indebted to. No doubt that's the reason your Junior Finance Minister Ken Valley made a recent trip to Guyana. In a sense therefore you cannot in any dimension of this problem isolate the monetary from the other important sectors.

There is also another observation. I don't know what the situation is like here in Trinidad & Tobago, but if you ask Guyanese who are the ten richest families, they'll reel off the names and if you ask them what they think they're worth, they'll say somewhere between US$50 and 100 million. They would also tell you that they've got 20 to 30-odd more with US$20 to 40 million. Now if you did a simple bit of arithmetic Lloyd talked about the algebra at the beginning this adds up to our external debt. Thus, in a real sense, we have considerable external debt problems, considerable internal pressure on the state, yet we live in a community where citizens that live among us may have assets abroad that may remove that burden. Now, you're not going to get them to give it up in the name of patriotism or anything like that, but it does show that the problem therefore does not reside only in the sphere of economics or even in a monetary analysis. It's clearly a political problem. You cannot effect redistribution or even a loan from them because we do not have the internal arrangements to do it.

An important question was tackled by Lloyd at the end when he asked what is the lowest cost foreign exchange type of activity that we could get into and he mentioned agriculture. I happen also to have a strong feeling and an increasing belief that the software of the economy is also very, very low-cost in terms of foreign exchange inputs. For example, what is called TVET technical and vocational education and training, which I think is probably the single largest potential impactor on economic performance in the region is something that has been badly neglected. This can use existing buildings. It needs a rationalisation, a reorganisation of syllabi, teaching modules and so on to avoid duplication, standards of certification and so on. You just look in all the newspapers of the

region and you see the increasing proliferation of these things duplicating each other, competing in the same market and delivering skills. This is an area where I think that a lot can be done without massive or very significant foreign exchange input.

I also think I must mention land reform, because I must come back to the point that in this region we've never really, since the Moyne Report talked about land settlement schemes, engaged in a fundamental redistribution of access to land. I still think that that is a completely intolerable situation as we approach the 21st century. Even in the very country that we are basing our models on, the United States, there is a very rapid revolution going on in the consolidation of land in the countryside. Now, I'm not saying that we need to replicate their models. The increasing efficiency of their agriculture, however, is based on very rapid reorganisation of the structure of ownership. We are deceiving ourselves if we believe that we can permit the existing entrenched interests in agriculture and in land to continue and at the same time achieve significant reforms in land and agricultural production.

My own belief is that this land and agriculture thing is seen as a dumping-ground for all our problems. Whenever we get into economic crisis, we say, oh, we must produce more agriculture and so on and that's where it remains. It has not moved past lip-service. The thing about it, however, is that a lot of this land in the region, for one reason or another, certainly in Guyana and to a lesser extent here in Trinidad & Tobago, is owned by the state. Therefore the problems of financing the land are not as acute. We go to countries abroad and ask them to write off debts. Have we envisaged a similar programme for our internally indebted small-business farming communities and so forth? We've never thought about it and I think that this is a matter that needs also to be addressed. We talk about local and community government, NGO empowerment and so forth, but what are we doing about it? Many of our countries are phasing out local government. People talk about NGOs, but there is no territory in the region that has a law that will allow you to define what an NGO is. Yet we continue to say that we have problems in the region. So I'd like to end on that note, to say that there are lots of things that can be done that are not demanding of foreign exchange, but they're demanding of political and social commitment to put the people of the region to the forefront. I urge you to bear this in mind, even when you discuss something as esoteric as the exchange rate, because there's really no disjuncture, no separation of the issues. Thank you.

**Professor Girvan**

Let me respond to three questions that were raised. Regarding the effect on credit unions, I don't have the detailed information, but you are correct in saying or implying that the big rise in interest rates did put pressure on the credit unions in Jamaica. They have been effectively marginalised in the credit system, because of their inability to attract deposits, being limited to fixed interest rates. If in fact you go into a higher interest-rate regime in Trinidad & Tobago, then the same kind of effect can safely be predicted.

Secondly, I don't think I'm the best person to ask if we have a computer model of the monetary economy in Jamaica. I would however hazard the opinion that if such a model were to be developed, the single most important issue to be tackled in it, or problem to be solved in it, is how to model expectations and speculative behaviour, because that's really the destabilising factor.

Thirdly, my friend Mitch asked about reverting to the old system. I have to confess that I have come around to that position. I am now a believer in the modified Currency Board system of the type that is operated by the East Caribbean Central Bank. I believe that in our vulnerable and fragile economies and with governments which are too often exposed to the temptation of expanding public spending in election years, in fact we have to be protected against this kind of behaviour. I'm saying so as someone who has in fact critiqued these arrangements in the past. We need strict limits on the ability of the monetary authorities to accommodate the central government and a fixed backing for the domestic currency issue 50%, which is the modified Currency Board arrangement. Further, these arrangements should be on a regional level. I believe that if we had a CARICOM Monetary Authority with these strict limitations, it would (a) facilitate intra-CARICOM trade to a tremendous degree and (b) contribute to exchange-rate and therefore price stability. It would therefore clear that particular issue out of the way for us to get on with the more basic questions of development strategy and how we bring about long-term growth and development. Thank you.

**Professor Bourne**

I think we've been fortunate in having three panelists who were able to address this question fairly comprehensively. Clearly there are lots of issues that many of us might have different positions on, but I think they all contributed to the process of identification of major issues for reflection and for further debate. I myself would have hoped that the discussion would have been a little more optimistic. I heard lots of horror stories and I would hope that this will not in any way disturb your sleep tonight. I want to thank the

organisers, the Regional Programme for Monetary Studies, the ISER and the Institute of International Relations for their foresight in bringing together Professors Girvan, Thomas and Best to address the matter. I look forward to subsequent sessions on other issues of fundamental importance to the Trinidad & Tobago economy and the region as a whole. Thank you very much and good night.

# Epilogue
# Fact and Fallacy in Economic Liberalisation

**Dr. Ramesh F. Ramsaran, Reader in International Economic Relations, Institute of International Relations**

In an effort to encourage growth and development, developing countries have used a variety of controls and incentives to achieve desired social and economic objectives. That the state could influence decision-making in any desired direction through legislative action was long taken for granted. Not surprisingly, a huge bureaucracy took root around this ethos which permeated both the real and financial sectors. Public expenditure grew in response to a variety of concerns and not surprisingly, this became a major influence on the structure and level of taxation, as these were frequently adjusted to meet the level of public spending.

Governments' intervention in the economy often not only extended to controls, but to ownership in key and non-key sectors of the economy. The state's intervention in the economy was dictated not only by a distrust in market forces, but by an adopted philosophy that it had to be the main actor in a context where it was often difficult to separate social and economic goals from political ones. Providing services at below cost of production, creating job opportunities, improving the distribution of income, subsidizing basic goods, rationalizing foreign exchange and controlling trade and services came to be regarded as major state functions. The implications of such policies for resource allocation were not felt until much later. The challenge originally came not from the IMF, the World Bank or the IDB. It came from the failure of income to keep pace with population growth. It came from the growth of unemployment, declining public revenues and capital inflows, falling foreign exchange earnings and more directly from persistently weak economic structures incapable of coping with the changing international environment. Import substitution as a transformation strategy in an irrational framework of controls had failed to deliver the goods in a large number of cases. The external aid agencies from whom assistance was subsequently sought formalised the verdict.

The latter themselves, however, had no clear idea of what should be put in place of what were perceived to be failed policies. There was no ready-made solution for economic ills by organizations who themselves had long resisted any change to their philosophy and operational policies. Their own orthodoxy, long

protected by the might of the dominant members and conservative advisors, had remained impermeable to new ideas. Many developing countries succumbed not because they thought that the intellectual solution to their basic problems was to be found in the neo-liberal ideas emanating out of Washington, but because they needed financial assistance or help in dealing with their debt burden and foreign exchange problems. In a global situation of collapsing Third World economies under pressure from both internal mismanagement and external developments, the Bretton Woods Institutions (BWIs) became increasingly powerful. In this situation it was easy to experiment. The 1970s and 1980s were decades in experimentation, the fruits of which are yet to be reaped.

The view emerged that there are certain principles that have universal application regardless of social or economic structure, culture, history, stage of development, size, etc. Too much state intervention was simply inconsistent with economic progress. The intellectual foundation of 'structural adjustment' rests on the belief that with less government and a liberalized economy, the consequences of 'misconceived' policies can easily be turned around, notwithstanding the international environment and the level of development. The basic tenet is, once controls are removed and market forces let loose, the path to a more vibrant and dynamic economy will emerge. Relative prices lead to efficient resource use. Initially, little attention was paid to the short-term social fallout of such an approach, or the relevance of unfettered market principles to particular situations. In time, against a background of criticisms, some issues came increasingly into the picture. These included the distribution of income, measures to deal with the poor and the unemployed, the need for growth as adjustment takes place, the unavailability of concessional finance, the impact of cross conditionalities of the major lending institutions, the time frame for adjustment, etc. While some of the contradictions and inconsistencies have been noted, no real solutions have been put forward. The fact is there are no economic policies that can guarantee anything.

What experience has taught us is that while problems may be easy to detect, solutions do not always easily suggest themselves. 'Quick-fix' approaches often give rise to further problems. The parameters within which decisions are being made are constantly changing and this has implications for the length of the adjustment period. Adjustment packages that might be internally consistent and meet all the criteria of rationality can quickly deteriorate into a set of ad hoc measures contradicting each other in objectives, if not in intent. It is a ludicrous train of thought which leads one to argue what has happened in some place will, or will not, happen in this other place. It is not only the basic economic structure that matters.

What also counts is the management capacity, the ability to take the hard decision, the timeliness and relevance of the measures, the availability of back-up finance and the commitment and willingness to see through a programme of reform. A programme must be credible to get support. The concept of sustainability derives not only from the availability of resources to carry through certain projects, but from the mode of execution which can affect the balance of social and economic forces in the society. In the absence of broad societal support, the restructured framework to support the new policy directions can quickly degenerate into a patchwork bureaucracy trying to restrain self-serving interests who have lost faith in the promised millennium. As important as the appropriateness of the reforms is the application of political finesse.

The question in the Caribbean is not whether economic reforms are needed, but what forms these reforms should take, the scope of the reforms, their sequencing and how fast they can be implemented. The import-substitution strategy left the Caribbean with an uncompetitive production structure, a stock of outmoded technology, high unemployment rates, a non-existent export base in manufactures and lack of an entrepreneurial class. The legacy also included a bloated public-sector work force put in place to administer the complex of controls and regulations that became necessary to support state functions, inefficient state enterprises and public utilities dependent for funding on the central government, an inadequate savings record, a heavy public debt in some cases and a spending policy out of line with revenue capacity. Drawing on past savings and later borrowing from the Central Bank and other sources were initially seen as tenable ways of propping up the standard of living and avoiding the taking of adjustment measures.

Borrowing soon produced a backlash in the form of increasing service payments which soon came to account for a significant proportion of government revenue and foreign exchange earnings. That the public debt would become such a major issue was not anticipated and little attention was paid to resource use, or the fact that the external environment could change so rapidly that comfortable situations could quickly turn into crises requiring major bailout. The populations themselves were lulled into believing that they were a world unto themselves and the governments would always provide. The link between the standard of living, people's desires and performance was not always easily understood. The position taken by the BWIs is that if people are made to feel the consequences of mismanagement and incompetence, they will more easily appreciate their position in the international marketplace. There is no free ride. The pressure from Washington is as much psychological as intellectual.

Admittedly, existing problems are not simply the result of mismanagement. Shortsightedness, inappropriate economic policies and the external environment have also contributed. Logically, adjustment needs to encompass a broad front, but the record to date shows a heavy concentration of effort at the national level, where the burden of adjustment is posing a serious threat to the sustainability of adjustment programmes which are either poorly conceived, badly executed or inadequately funded. Adjustment programmes do not deal with protectionist forces in external markets, access to modern technology or inappropriate pricing of major export commodities. Even if the quality and price are right, this may not be enough for a product to enter a foreign market.

Many of the goals are not in question. It is recognized, for example, that Caribbean countries need to become more competitive to export more, given their small domestic markets. Production and export bases need to be diversified. Fiscal systems have to be modernised, not only to be more efficient raisers of revenue, but also to provide incentives to encourage effort and production. Wasteful expenditures have to be curbed and resources channelled to the more productive sectors of the economy. Savings rates need to be raised if capital programmes are to be expanded without worsening the debt situation. Governments facing financial difficulties cannot continue to subsidise inefficient state enterprises through increasingly higher taxation approaching or long past the point of bearability. For the revenue capacity to increase, the cake must expand also. There are some social services which the state must provide but even these become threatened when revenues are not provided.

Traditionally, the export sector has not only brought the region foreign exchange, but has been a major contributor to government revenue in the Caribbean. Foreign exchange defines import capacity, in the same way that revenue defines Governments' ability to spend. Both impact on the standard of living and for countries critically dependent on imports for investment and consumption, foreign exchange is a major resource. There are several factors which have contributed to the decline of the traditional export sectors but most of these are to be found at the production level or in developments in the international economy. In this situation, encouraging foreign demand through devaluation of the national currency has limited relevance.

The problem is simply not one of price, particularly in a context where these countries are essentially price takers. The crisis brought on by a fall in foreign earnings has provided the opportunity for a general appraisal of economic policies and strategies. The exchange rate is brought into the battle, not because it may be of any help to the traditional export sector, but because it is the most important

price in the economy. It is viewed as one of the instruments that can be used to stimulate non-traditional exports. The assumption is that the major disincentive is a price one. The exchange rate, of course, can also be used to discourage imports of goods and services, without expanding the panoply of controls which distort resource allocation. For governments embarking on a programme designed to remove import controls, this is an attractive feature of exchange-rate manipulation.

A downward adjustment of the exchange rate can also increase the local currency equivalent of revenue received in foreign exchange. The advantages of a downward adjustment, however, are also associated with negative consequences related to the cost of living, debt-servicing, etc. The challenging question for a country mobilizing this instrument is not just what real rate would maximise the net benefits, but what the most appropriate regime for inducing this rate is. Experience has shown that neither the local technocrats nor the BWIs have already made answers in the absence of critical information. The latter's guess-working is often as bad as that of the locals, even though numbers are often churned out in the guise of an authority imbued with divinity. A general equilibrium model is assumed to exist where often there is none.

The fact of the matter is that for the exchange rate to contribute to adjustment, it has to go hand in hand with efforts in other policy areas. Very often the exchange rate is asked to do what it was not designed to do. Trying to force adjustment through perpetual downward movement in the rate ends up inflicting tremendous suffering on the population rather than leading to greater competitiveness. The Guyanese dollar moved from G$2.55=US$1.00 in 1980 to G$45.00=US$1.00 at the end of 1990. Over this period per capita GNP in nominal terms declined from almost US$600 to US$370. Since then the rate has slipped more radically, reaching G$125.00=US$1.00 in 1992. While there are some signs of growth in recent years, it is difficult to say how much of this is attributable to the exchange-rate policy. Guyana remains one of the poorest countries in the hemisphere.

In the case of the Jamaican dollar, the rate moved from J$1.78=US$1.00 in 1980 to J$7.18=US$1.00 in 1990. Over this period, real per capita GNP declined by an average rate of -0.4% per year. By 1992 the rate had slipped to almost J$25.00=US$1.00. The Trinidad & Tobago dollar went from TT$2.40=US$1.00 in 1984 to TT$4.25=US$1.00 in 1990. Per capita GNP in current dollars dropped by 45% in this period. In April 1993, the Government opted for a regime of limited controls and allowed the rate to 'float' to a level of around TT$5.75=US$1.00. On the other hand, Barbados has held its rate at around B$2.00=US$1.00 for more than two decades. Despite this, Barbadians have not been shielded from an

increasing cost of living situation, since internal taxes which have been used to raise revenue and discourage consumption have impacted on the price level.

To what extent the adjustments of the exchange rate in the Caribbean have achieved the initially envisaged objectives is difficult to say, since internal and external balances persist and sustained growth remains elusive. Adjustment measures have to be judged not only by their impact on the proximate objective (e.g., the balance of payments or the fiscal situation) but on overall social and economic conditions. Real wages and living standards have been falling as orthodox short-term measures are put in place to bring public revenue and expenditure in line and to adjust foreign expenditure to new levels of foreign exchange earnings. There is little that is new in the measures being used to encourage exports and attract foreign investment. The attitude taken by what could only be described as a highly unholistic approach to adjustment problems is rationalised on the argument that growth will take place somewhere down the road.

The position taken on the removal of exchange and trade controls is an interesting one. The removal of quantitative restrictions and the fall back on tariffs as a protective device are supposed to promote the competition that would eliminate inefficient production and encourage resources to move to more productive uses. If the objective is not simply to open these markets, but to increase domestic output and efficiency, then questions of the mode of intervention in an imperfect marketplace must be an integral part of the discussion. There are elements in the import-substitution strategy that can be salvaged and form part of the arsenal that developing countries must forge to deal with a more open world trading system. The idea that the world market is a perfectly competitive one is a myth which should not be accepted by distressed countries without question. There are industries that might be worth saving in an appropriate framework.

The related issue to the question of trade controls is the position taken on exchange controls. One argument is that it makes no sense to free up trade and retain exchange controls. The question is here: to what extent can developing countries whose currencies are not in demand for international transactions afford to operate free markets in foreign exchange? In a chronic situation where demand tends to outstrip supply, there will certainly be downward pressure on the rate which can fluctuate in a degree inimical to the economy. Foreigners generally do not demand 'insignificant' currencies and such demand as there is for the domestic medium rests on the confidence of the local population. The tendency in developing countries, however, is for the local population to transform their savings into a major currency which they feel offers a better

safeguard against devaluations and higher prices. For a while, a free or semi-free market with enough reserves (or supply) to meet demand may discourage capital flight. Once a persistent downward movement in the rate develops, however, and lack of confidence in economic management takes hold, the uncertainty that is generated provides the incentive for outward movement of capital. The fact is, poor countries would find it difficult to operate the same kind of monetary and financial policies as countries with a well-developed capital market and with currencies in demand for international transactions. Arrangements have to recognise local conditions and not simply reflect what others are doing.

The failure to appreciate what an exchange rate can or cannot do often leads to a preoccupation with this instrument that diverts attention from other vital policy areas which may have even greater implications for long-term development. The expectation in developing countries is that the exchange rate moves in only one direction and that is downward. The behaviour this generates can develop into self-fulfilling prophecy. The experience in certain countries shows that the devaluation spiral can quickly take the momentum of a runaway train moving in no clear direction and with no clear purpose. When this happens and local prices start taking unusual dimensions, a situation develops that provides serious disincentives to domestic savings and exports. The capital programme can become even more dependent on foreign savings. The use of the exchange rate as an adjustment measure is an attractive one since it eschews bureaucracy and touches everyone, but is clearly one that has to be handled with care. The distributional impact in a poor society is not one that can be ignored, particularly when the promised benefits of a flexible rate take long in coming.