The United States’ Win-Win Relationship with the Caribbean

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Almost every facet of the Caribbean economy is influenced by the U.S. economy. Much of this influence flows through capital, trade, communications, migration, and exchange rates between the two economies, with U.S. investment often dictating the direction of Caribbean trade. The nexus between the two is particularly pronounced in Trinidad and Tobago’s oil and gas operations in which U.S. imports of oil and gas from Trinidad and Tobago account for 80 percent of imports from the Caribbean Community and Common Market (CARICOM).

A similar relationship is evident in the tourism industry, which attracts a significant amount of U.S. investment. In 2004, U.S. tourists made up 52 percent of all tourists visiting the Circum-Caribbean, and an even larger percentage visited the Bahamas (87 percent) and Jamaica (70 percent). U.S. investment in the Caribbean also generates imports of U.S. goods and services and a return flow of profits to U.S. investors. This circular flow places the United States in a win-win relationship with the region.

The pegged relationship between Caribbean currencies and the U.S. dollar also has a direct impact on the direction of Caribbean trade. Depreciation of the U.S. dollar against world currencies improves the competitive advantage of Caribbean exports to non-dollar countries and shifts CARICOM imports from these countries to the United States. Between the first quarter of 1996 and the first quarter of 2007, CARICOM imports from the U.S. doubled from $1 billion to $2 billion.1

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Ransford W. Palmer

The Paradox of Preferential Treatment

The United States has used preferential trade arrangements to open its market to Caribbean trade. The aim of the Caribbean Basin Economic Recovery Act (CBERA) of 1983 was to replace aid with trade, bolstered by the argument during the Reagan Administration that trade would promote the growth and development of a vigorous private sector as a bulwark against the encroachment of socialism in the region.\(^2\) To accomplish this, the CBERA provided incentives for U.S. businesses to invest in the Caribbean and guaranteed a market for the region’s exports with duty-free entry into the United States. It channeled U.S. capital into apparel and assembly industries where it could exploit the abundance of cheap Caribbean labor. These industries sprouted in tax-free economic processing zones throughout the region and transformed Caribbean countries into export platforms with little or no connection to the indigenous economy.

Buttressing this process is a complement of local tax concessions to foreign investors, including tax holidays and the full repatriation of profits. This preferential treatment yields more benefits to the foreign investor than to the Caribbean. On top of that, a large share of the wage income generated by the employment of local workers is spent on the consumption of imports from the United States. The fact is that unilateral preferential treatment of Caribbean exports offered by the United States disguises the true beneficiary of that treatment: the United States. According to Hoekman and Özden, “The early debates and arguments that pointed to the potential downsides of special and differential treatment (SDT) proved quite prescient—benefits have been limited, skewed in their distribution, and arguably obtained at a high cost to the trading system, donor country consumers and many of the purported beneficiaries. Research has demonstrated that preferences can at best play a marginal role to assist developing countries—what determines and drives performance is not what others do, but what countries do for themselves.”\(^3\)

The Unequal Flow of U.S. Investment

U.S. investment in energy trumps all other types of investment in the Caribbean and influences the distribution of economic power in the region. The flow of U.S. investment into Trinidad and Tobago, CARICOM’s only oil exporter, has resulted in a trade surplus of one trillion U.S. dollars by the first quarter of 2007, placing Trinidad and Tobago in the pivotal position as a supplier of capital to the rest of the CARICOM. The opposite is true for Jamaica: the decline of U.S. direct investment in Jamaica since 2004 and the depreciation of the Jamaican dollar have worsened the country’s trade balance with the United States.\(^4\) At the core of this imbalance are differences in the
availability of profitable investment opportunities in both countries. For example, these differences are evident in relationship between employee compensation and net business income. While there is a high ratio of employee compensation to net income in predominantly labor-intensive tourism and manufacturing operations in Jamaica, there is a low ratio of employee compensation to net income in the capital-intensive oil and gas operations in Trinidad and Tobago.

The decline of U.S. investment has weakened Jamaica’s export growth. Textile and apparel exports declined steeply from $300 million in the mid-1990s to $7.5 million in 2005, forcing the closure of fabric and garment assembly plants. The United States International Trade Commission attributes this decline to difficulties in following CBERA rules of origin because of the need to “source increasing amounts of raw materials and inputs from outside the United States and the Caribbean basin region in order to be competitive.” But the key factor is the decline in profitability brought on by a combination of other things: the end of textile and apparel quotas in 2005; NAFTA (North American Free Trade Agreement)-related trade diversion to Mexico; growing competition from China; the extension of U.S. trade preference to lower-cost Central American countries through the Central American Free Trade Agreement (CAFTA) and high production costs resulting from rising crime.

**The Impact of Bilateral Agreements**

Bilateral and other trade agreements have undermined the impact of the CBERA. Beginning in 1993, NAFTA diverted trade away from CBERA countries, prompting the United States to amend the CBERA in 2000 with the Caribbean Basin Trade Partnership Act (CBTPA), which provides NAFTA parity to those countries designated eligible by the U.S. Trade Representative. The eligible countries include Costa Rica, the Dominican Republic, El Salvador, Honduras, Nicaragua, Panama, and five CARICOM countries: Belize, Guyana, Haiti, Jamaica, and Trinidad and Tobago. On 2 August 2005, President George W. Bush signed Public Law 109-053, known as the Central American Free Trade Agreement (DR-CAFTA), which includes the Dominican Republic. Currently, negotiations are underway with Colombia for a similar agreement.

While the garment assembly industry in Jamaica has declined due to higher labor costs, it has grown in Haiti, where the per capita income is the lowest in the Western Hemisphere. This growth has been stimulated by the Hemispheric Opportunity through Partnership Encouragement (HOPE) Act of 2006, which grants preferential access to the U.S. market beyond what is offered by CBERA. It has also induced a rise in direct investment, mostly from the United States, France, and Canada, from $6 million in 2002 to $160 million in 2006. Apparel products represent 90 percent of
Ransford W. Palmer

U.S. imports from Haiti. Just as NAFTA reduced Jamaica’s apparel trade with the United States under CBERA, CAFTA has had the same affect on Belize’s apparel trade (mostly tracksuits) with the United States. Direct investment from the United States into Belize has moved into other potentially more profitable sectors such as tourism, agriculture, telecommunications, and petroleum.

In extremely open economies such as those in the Caribbean, external developments can be the agents of diversification that CBERA tried to be. Yet the picture of U.S.-Caribbean economic relations that has emerged since CBERA is one in which the diversification of the Caribbean economy confronts two opposing forces. One is the undermining of the goal of CBERA by the proliferation of bilateral trade agreements; the other is that foreign direct investment flows tend to reinforce this retreat of diversification by switching to traditional sectors that are profitable. In a few instances, new international developments have been able to override this switch. Rising demand for ethanol in the United States triggered Brazilian investment in a dehydration plant in Jamaica to make ethanol from Brazilian hydrous raw material and a distillery to produce ethanol from Jamaican sugarcane. According to the United States International Trade Commission, fuel-grade ethanol was the leading U.S. import from Jamaica in 2006: 1.9 million barrels valued at $164.6 million, representing 10.9 percent of all U.S. ethanol imports.

Drug Trafficking and Money Laundering

Of the number of issues that challenge U.S.-Caribbean relations, drug trafficking and money laundering seem to receive the most media attention. In September 2006, President Bush designated the Bahamas, the Dominican Republic, Haiti, and Jamaica as major drug-producing or drug-transit countries. Jamaica was singled out as the largest marijuana exporter in the Caribbean and St. Vincent and the Grenadines as the largest marijuana producer. The lingering fear is that the declining fortunes of the major export crops of banana and sugar will drive more people into marijuana production and set up a criminal environment that could disrupt civil society. U.S. anti-drug strategy includes sustained efforts against money laundering that have increased in intensity since the terrorist attacks on 11 September 2001. According to the Congressional Research Service (CRS), “The State Department’s list of major money-laundering countries includes six Caribbean countries—Antigua and Barbuda, the Bahamas, Belize, the Dominican Republic, Haiti, and St. Kitts and Nevis—and one British Caribbean dependency, the Cayman Islands.”

The case of Antigua and Barbuda underscores the conflict between the aim of a
small country to diversify its economy with Internet gambling and the perception of the United States of that strategy as inimical to its national security. Antigua and Barbuda filed a complaint with the WTO challenging restrictions imposed by the United States on cross-border gambling. In 2005, the WTO backed Antigua and Barbuda’s claim that “the U.S. restrictions violate the United States’ market access commitments under the WTO’s General Agreement on Trade in Services.” Antigua now complains that despite the fact that it has enacted legislation to tighten the regulation of its financial sector, there has been no U.S. action to comply with the WTO ruling. According to the CRS, the State Department maintains that even with this new legislation “the country remains vulnerable to money laundering because the sector is loosely regulated and because of its Internet gaming industry.” As illustrated by the recent crash of the Antigua-based Stanford International Bank of Texas, the country may also be vulnerable to Ponzi schemes.

THE EMERGENCE OF RECIPROCITY

When globalization eliminates unilateral preferential arrangements, these small countries are forced to become competitive in order to survive. Within the WTO, for example, these countries have been reduced to waging guerrilla war on the periphery of consultation and decision-making processes between the European Union and the United States. This comes at a time when it is clearly evident that their economies and societies still require an enabling external environment, generated by appropriate international structures and policies, in order to survive. This message therefore has to be preached exhaustively by accomplished diplomats using appropriate coalitions and alliances, in all multilateral forays as well as in bilateral relations. Some see the elimination of preferential treatment as replacing social peace with social and political upheaval. The consequences are even more troubling because of the uncertainty of the place of the Caribbean in the governance structures of the institutions of globalization. The urgency of this concern is expressed by Jessica Byron: “The fear for their economic survival was behind the historic visit of fifteen heads of Caribbean governments to Washington DC to meet with the President of the United States in June 2007.”

But Anthony Gonsalves suggests that there is a tendency to see the threats rather than the opportunities in this process, a tendency that he believes “is linked to the fact that these economies depended on above-average protection [relative to other developing countries] in the markets of developed countries under the CBERA, Lomé and CARIBCAN.” The opportunities, Gonsalves argues, lie in removing the barriers to trade liberalization that slow the speed of integration with the global economy.
Between 2005 and 2006, U.S. aid to the Caribbean averaged $340 million a year and is projected to reach a total of $1.2 billion in the first decade of the 21st century. This is a significantly lower figure than in the 1980s, when it reached $3.2 billion. After its military intervention in Grenada in 1983, the United States poured large amounts of aid to restore a friendly government and support the free enterprise program of Edward Seaga in Jamaica. But after the collapse of the Soviet Union in 1991, U.S. aid fell sharply, and the Caribbean began to feel ignored. Caribbean socialist political leaders could no longer play the Soviet Union against the United States. By then the “trade, not aid” thrust of U.S. foreign policy toward the Caribbean had taken hold, favoring foreign investors and their local business partners. But because many Caribbean countries were burdened by debt, the trade relations did not produce any significant economic growth.

The Drain of Human Capital

Aside from being the major source of tourism and the host of a large population of Caribbean immigrants, the United States is also the destination of many Caribbean tourists, students, and businesspeople. These groups bring with them a flow of financial and human capital. It is estimated that Caribbean visitors to the United States from CARICOM and non-CARICOM countries spent an average of $1.5 billion a year between 1999 and 2005.

In 2006, among the 583,959 foreign students in the United States, 15,811 were from CARICOM countries, the seventh largest group, coming primarily from the Bahamas, Jamaica, and Trinidad and Tobago. If the average cost of education per student were $10,000 a year, allowing for scholarships and financial assistance, the total annual expenditure of Caribbean students would be $158 million. Although this is a small share of total student spending in the United States, it represents a large outlay of foreign exchange for small countries with persistent deficits in their balance of trade. Over the years, declining Caribbean exchange rates have reduced the number of students studying in the United States.

Foreign students serve as an important channel through which management skills and production technology can flow to their home countries upon their return. Many who go to the United States to pursue advanced science degrees often do not return to the Caribbean because of the lack of opportunities in their chosen fields. U.S. immigration policy encourages the retention of such skilled workers and U.S. corporations employ many. But even when they do not return home, foreign students
become part of an expatriate pool of skilled workers that can potentially be tapped by their countries of origin.

While studying in the United States facilitates the transfer of knowledge of technological processes, it usually takes foreign investment to transfer the process itself. But the transfer of technology does not transfer ownership; it merely gives the recipient country permission to use the process at a cost in the form of royalties and fees for patents and trademarks. Data for selected Caribbean countries show that an overwhelming number of patents are granted to foreign entities. This dominance underscores the dependence of Caribbean businesses on foreign technology. Although some argue that developing countries should invest more in research and development, it makes just as much sense to educate their labor force to use available technology. Indeed, the challenge for these countries is to use available technology to generate wealth and to craft policies to retain enough of that wealth for future growth and development.

What the Future Holds

As preferential arrangements give way to reciprocity, Caribbean economies tend to grow more dependent on foreign exchange generated by two types of travel: tourism and migration, both of which can be called travel economies. Tourism generates immediate foreign exchange, and migration, over time, creates a stream of remittances. The share of foreign exchange generated by these sources has been rising as earnings from traditional commodity exports fall. Since the United States is the source of most of the tourists, and the host of most of the immigrants, fluctuations in the U.S. economy are quickly transmitted to these travel economies. In a worldwide recession, like the one we are experiencing, there are no other sources of tourists and no other immigration escape valves to cushion the impact. This focuses the attention of the Caribbean on the quick success of the stimulus in the United States. Because most experts do not expect a quick recovery, the Caribbean’s economic contraction will likely continue for some time. The expectation in the Caribbean is that the Obama administration will help ease the pain directly through foreign assistance or indirectly through augmented resources for international institutions such as the World Bank and the International Monetary Fund.

Notes

According to the Economic Commission for Latin America and the Caribbean, “the Latin American and Caribbean region continues to receive a shrinking proportion of global FDI flows. The region took in 12 percent of global inflows in the 1980s, compared with 10 percent in the 1990s. Since 2000, it has received just over 8 percent worldwide FDI. This could indicate that the region is being gradually sidelined from FDI in the current pattern of globalization” (ECLAC, Foreign Investment in Latin America and the Caribbean, 2005: 23).

9. Ibid.
10. Ibid.
12. Lomé Convention is a preferential trade agreement between European countries and their former African, Caribbean, and Pacific colonies. CARIBCAN is a preferential trade arrangement between Canada and the Commonwealth Caribbean.