CARIBBEAN CENTRE FOR MONEY & FINANCE

SIR ARTHUR LEWIS MEMORIAL LECTURE

Dependent Economic Development in the English-speaking Caribbean, 1945 – 2000

14th October, 2008

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UWI St Augustine Sir Arthur Lewis Memorial Lecture

Sir Arthur Lewis

I am privileged to have known Sir Arthur, and I can attest to the fact that he was among the most exceptional of an extraordinarily gifted generation of Caribbean thinkers, and a towering giant in the field of economic practice. I began my career as an economist in the early 1970s when leading Caribbean economists had a love-hate relationship with Arthur Lewis. We were in awe of his magisterial "Economic development with unlimited supplies of labour" (Lewis, 1954), which is among the most quoted writings in economics of all time, but we believed that he had done the Caribbean a disservice by persuading our leaders to follow a Puerto Rican model of dependent development. It was not until a decade later that I really sat down to read Lewis' substantial contributions, including the extraordinary *Development Planning* (Lewis, 1966), a tour de force that is unlike any other book in development economics, before or since. It addresses development challenges in all their many facets, including issues of what we nowadays call "governance" and social stability, as well as things that economists are more comfortable with, such as savings and investment. It's been a long time since I read that book, but its impact was indelible, and I recall being astounded at the breadth and depth of insight Lewis brought to bear, on the practical issues of improving the material conditions of the developing world.

Just recently I read Norman Girvan's first lecture in the current series in Sir Arthur's memory, and I came across a comment on the importance of federal structures for good governance in the Caribbean. This is just the kind of example of Sir Arthur's keen insight that impressed me. Of course we have no counter-factual, but I firmly believe that if the member countries of the former British Caribbean Currency Board had achieved independence as a federation, we would all now consider ourselves first world nations, on par with Singapore or Iceland.

When I arrived at Princeton in the fall of 1980 for a one year fellowship that Sir Arthur had helped to arrange, I found that he was the toast of the university, along with Princeton's three other Nobel Prize winners. He was treated like royalty, and had the freedom of the place, but he was quite nonchalant about it all. That year he was outgoing president of the American Economic Association, the world's most influential, just one more reason to be in awe of him. It was quite daunting to have to offer a seminar under the penetrating scrutiny of the likes of Lewis, Willem Buiter (recently of the Bank of England), William Branson of text book fame, and Peter Kenen, Fritz Machlup's successor who ran the International Finance Institute from a basement in the economics building.

However, by 1980 I got the sense that Sir Arthur was becoming increasingly disenchanted with the direction economics was taking. I recall his comment about a Caribbean student in the Princeton graduate programme with whom he was particularly impressed. He thought it was a great pity she had elected to do economics rather than law, where he thought her potential contribution might have been so much greater. Sir Arthur wasn't quite serious when he said this;

rather, it was an expression of his frustration that economics was "pelting" down a dead end street.

Now, thirty years later, I feel much the same way myself. I suspect that future historians will indeed come to regard the last 30 years of economic thinking, led by the American university establishment, as a broad congested highway to nowhere. The current financial crisis in America is a crisis of economic thought, as much as it is a crisis of economic performance. Because the tools of contemporary economic practice gave no clear warning of the fragility of the foundations of the American financial system, they can offer no clue as to the depths of the crisis, and the reach of its economic consequences. Sooner or later we may have to go back to Keynes, Schumpeter, Lewis, Galbraith and Meier, and start all over again.

Human development in the Caribbean

The UNDP has developed a carefully crafted index of human development which, though subject to qualifications which the UNDP specifically acknowledges, is the best indicator available of the material well being of societies, when used circumspectly and in conjunction with all other relevant data that is available. By this measure, the English speaking Caribbean (ESC) had relatively high levels of human development in 2000. The top four countries (Barbados, St Kitts-Nevis, The Bahamas and Trinidad and Tobago) were all in the "high" human development group, and all others were in the "medium" group. The top five (those just mentioned, plus Antigua and Barbuda) were above Latin American countries. However, all ESC countries were below the mean value for the group of "high" human development index (HDI) countries as a whole, and they were overshadowed by some other small island states – Iceland, Singapore and Cyprus.

[Figure 1]

The HDI is made up from a) average national income per head, measured in terms of the amount of a standard "basket" of goods and services it will buy (purchasing power parity); b) measures of educational achievement; and c) indicators of the health of the population. This implies that when we take all together average incomes, the cost of necessities, average educational levels and the health and longevity of our populations, in at least four Caribbean countries the "average" person lives as well as does the "average" person in rich countries, more or less. And nowhere in the ESC is the quality of life desperately inadequate. There is much more to the story than that, of course, and there are many other indicators we need to examine in order to get the fullest picture of comparable living standards, but as a first approximation this corresponds to the everyday observation of anyone who has travelled extensively.

Incomes in the ESC are relatively low in US dollar equivalents, but indicators of the health of the populations are exceptionally good, and educational achievements are higher than for countries at similar income levels. The highest per capita income of any ESC country in 2000, measured in US dollars of equivalent purchasing power parity (PPP), was for the Bahamas, US$17,200. That was just over half the per capita average for OECD countries, also calculated in PPP equivalent dollars.

[Figure 2]

All ESC countries had life expectancies above comparable rates for Latin America, except for Grenada and Guyana. Three countries – Dominica, Barbados and Antigua and Barbuda – recorded life expectancy at birth of 74 years or more, a figure comparable to those of industrial countries. Other health indices, not included in the HDI because comparable data are not available for all countries, confirm the relatively good health status. Access to improved sanitation is universal in The Bahamas, Barbados and Trinidad and Tobago, and better than 75% in most of the rest of the ESC. Other indicators for the ESC are also strong: access to water, infant mortality, incidence of low birth weight babies, availability of skilled birth attendants, availability of hospital beds and protein intake. Guyana is the exception, with much lower access to sanitation and water, higher infant mortality, higher incidence of low birth weight babies, and lower availability of hospital beds.

With respect to education achievement, adult literacy rates are at levels similar to OECD countries for three countries (Barbados, Trinidad and Tobago and St Kitts-Nevis), and literacy rates are high elsewhere, except for Belize.

The contrast with levels of human development in the late 1940s and early 1950s is stark. In the late 1950s income per head in the ESC ranged from US$150 to US$250 per year, about 10 percent of per capita income in the US at that time. Trinidad and Tobago's income per head was a little higher, at about 20 percent of the US's. But health and education indicators were really dismal. In the late 1940s the life expectancy at birth in the ESC was about 50 years, no more, at a time when life expectancy for white people in America was almost 70 years. Infant mortality rates ranged from 100 to 180 per thousand, compared with 30 for the US. Illiteracy rates were 20 percent or higher, except for Barbados.

[Figures 3, 4 and 5]

Trends in income per capita in the ESC were common up to the late 1970s. Thereafter Jamaica and Guyana (and later Trinidad and Tobago) diverge from the others. The common trend was for steady growth of income per capita in the 1950s on into the mid-1960s. All the countries stagnated in the late 1960s and early 1970s, and growth resumed in the mid-1970s. From 1977/78 income per capita in Jamaica and Guyana declined while other countries continued to enjoy growth, led by Trinidad and Tobago, with the benefit of the first oil price boom. Income per head in Trinidad and Tobago fell sharply with the collapse of oil prices in 1982/83.

[Figure 6]

Barbados' income per head kept on growing, interrupted only by the balance of payments crisis of 1990-94. Income per head in the OECS countries grew steadily, as did income per head in Belize, which grew from a comparatively low base to overtake Jamaica in the early 1980s. Income per head in Trinidad and Tobago began to recover in 1994.

In the meanwhile, Jamaica endured a decade and a half of economic stagnation, from the late 1970s to the early 1990s, which left income per head at 1974 levels. Improvement did not come until the 1990s decade. Guyana went into a long period of decline from the late 1970s to the early 1990s, after which the recovery brought income per head a little above the levels achieved before the decline.

The transformation of the societies of ESC countries, from the poorest levels of HD to a situation where the "average" worker was adequately housed and fed, was literate and with a life expectancy at birth of about 70 years, was essentially complete by the end of the 1960s decade.

The most dramatic improvements in the 1950s and 1960s were in health indicators – life expectancy, infant mortality and morbidity. The life expectancy of males in Antigua and Barbuda, The Bahamas, Barbados and Jamaica increased from about 50 years to over 65 years between 1946 and 1970. Infant mortality rates, which ranged from 100 to 180 per thousand in 1945, were down to a range of 40 to 60 by 1970.

Incomes per head, and the purchasing power of those incomes, also rose more rapidly in the 1950s and 1960s than in the 1980s and 1990s.

There were also very important improvements in the quality and coverage of educational services in the 1950s and 1960s. By 1970 illiteracy rates were generally reduced to 10 percent or less, except in Jamaica and Belize, and primary enrollment everywhere was above 90 percent of the school age population. The proportion of students with secondary education increased dramatically in the 1960s decade. The 1980s and 1990s saw the growth of tertiary education, along with a broadening of the reach of secondary education.

Other indicators support the view that the lifting of ESC countries from very poor levels of HD to an adequate standard was largely accomplished during the 1950s and 1960s. Access to clean water was made almost universal in the Lesser Antilles, electricity services were greatly expanded, sanitation was much improved and the quality of housing was visibly better. There remained major deficits in all of these areas, but by the early 1970s the ESC indicators were considerably better than for our Latin American neighbours, as well as most developing countries. This was in marked contrast to the late 1940s, where these indicators for the ESC were among the worst anywhere in the world.

For the period from 1945 to 2000, the picture that emerges is of significant HD gains, even in countries where economic performance was disappointing. The better ESC performers have closed the gap between their levels of HD and those of the US and other countries with high HD, a fact which income per capita alone fails to detect. Even the worst economic performers in the ESC have achievements in health and education comparable to those of successful island economies such as Singapore and Mauritius, and these indicators for the ESC are generally somewhat better than for our Latin American neighbours. Most of this improvement came between 1946 and the mid-1970s. All ESC countries except Guyana registered improvements after that period, but they were relatively modest in comparison with what went before. Even with the long period of stagnation which Jamaica endured in the 1980s, that country's indicators point to improved material well being in 2000, compared with the mid-1970s.

In the present decade, five ESC countries are listed among those with high HD, in the UN's HDR – Antigua and Barbuda, The Bahamas, Barbados, St Kitts-Nevis and Trinidad and Tobago. This means that, based on average incomes, the purchasing power of those incomes, life expectancy at birth, infant mortality rates, adult literacy rates and school enrollment, and comparing across all countries worldwide, the "average' worker in these countries enjoys a quality of life which is comparable to the quality of life in the world's richest countries. In a meaningful sense we may say that these countries have already achieved developed country status.

It is ironic that Caribbean countries which are now setting targets, more or less distant, for achieving "developed country status" are already past that marker, if you take on board factors other than income per head. This is not to deny that there is much work to be done, to better the quality of life for everyone, especially those that fall below the poverty line. But the same is true of most developed countries, including the US. What the international comparison embodied in the HDI shows is that five ESC countries have more in common with rich countries than with the developing world, in terms of the quality of life of their citizens and the challenges they face in improving that quality of life.

This is true in spite of the acknowledged weaknesses of the HDI. There are varying opinions on almost every aspect of the calculation of the HDI: the weights assigned to its elements, the comparability of data across countries, the reliability of the data, and how well the indices represent the experiences of the beneficiaries of educational and health services. There are dimensions which everyone agrees should be added, but for which comparable data are not available over a sufficiently large number of countries. A prime example is the distribution of income. However, the results of HDI comparisons are consistent with everyday observation. This may be demonstrated by making a mental comparison between the US and the five ESC high HDI countries with respect to education, diet, dress, social life, housing, household amenities, health, life expectancy, travel choices, etc., for any comparable category of workers, such as teachers, nurses, restaurant chefs, bus drivers, farmers or construction workers. Now make the same comparison with a medium HDI country such as Guyana, or a low HDI country such as Haiti.

Endowments, technologies and behaviours

Endowments, technologies and behaviours are part of the reason for the good performance of countries which achieved high HDI status, but they do not explain why some countries failed to reach that level of HD. The ESC as a whole was quite well endowed with human, physical and knowledge resources in late 1940s, although much of that resource endowment was recognised only with the introduction of new technologies. Tourism potential, which has had the biggest material impact, only became a reality with the commercial development of jet transportation in the 1960s. With respect to minerals, oil & gas resources were much richer than was thought, but technological developments (especially the development of strong lightweight plastics) robbed bauxite and aluminium of much of their potential to benefit Guyana and Jamaica. With respect to agriculture, the focus on the physical resource rather than the region's accumulated knowledge of the technologies of cane growing and sugar production led to misguided strategies and squandered potential. The ESC proved rich in human resources, entrepreneurship that was expressed in pioneering, unconventional ways, and the populations proved to be remarkably thrifty. Surprisingly, though, indicators are that the rate of technical absorption was surprisingly modest.

In terms of physical resources, tourism and oil and gas were the most productive endowments of the ESC. What turned out to be the ESC's richest economic asset - tourism potential - was unrecognised in 1940s because it depended on the development of jet transport, which made mass market tourism to tropical regions possible and affordable. From the 1960s onward, tourism emerged as the leading export sector everywhere in the ESC except Guyana and T&T.

T&T's oil and gas potential turned out to be much richer than was known in late 1940s, thanks to the discovery of offshore reserves, including natural gas. The development of liquefaction techniques, including storage and transport of LNG, further enhanced this potential. The T&T government's initiative to jump start the manufacturing of energy based products was an important factor in increasing the returns to the local economy from the energy sector.

In contrast, bauxite/alumina, which was expected to yield rich dividends for Jamaica and Guyana, was much less beneficial than was expected. This was partly the result of technological developments - the rise of plastics as durable lightweight substitutes for aluminium; and partly due to policy choices by Jamaica and Guyana, and geopolitical changes.

Agriculture turned out to be much less productive than expected, even in Guyana and Belize, the countries with substantial land resources. Their governments failed to recognise that the major agricultural resource was knowledge embedded in what was a technologically sophisticated agro-industrial enterprise, with an equally sophisticated marketing and distribution network for a diversified output. As a result, they did not focus on turning that knowledge into a source of competitive advantage. Instead, governments and private interests pursued a backward-looking strategy, based on negotiation of protected markets.

The ESC was relatively well endowed with human resources, compared with other small open economies and their neighbours. They boasted relatively good educational levels, and a relatively high percentage of skills in the workforce, and these were further enhanced by investment in education, both by governments and by individual families, often at great personal sacrifice to the older generation. Caribbean households were also remarkably thrifty by comparison with countries in the Americas, with high real savings ratios as well as very high ratios of financial savings.

The ESC remains rich in entrepreneurship, expressed in novel ways, as it has always been. The main avenue available to the majority of the enterprising population has always been migration, to whatever destination appeared to have good prospects. The most enterprising families recognized that education was and is the most secure and dependable avenue to a better quality of life, and many of those who migrated did so with this goal in mind. Investment in real estate was also seen as a secure means of wealth enhancement by the more enterprising. The middle classes in the ESC have a tradition of sound household finance, reflected in widespread co-operative arrangements, formal and informal. Entrepreneurship is also reflected in the development and export of Caribbean brands of music and festival arts, and in marketing innovations, notably in tourism.

Small size

As with countries elsewhere, small size was not an obstacle to considerable improvement in HD in the ESC. Much of the policy debate about the implications of small size, focusing on the need for special trade and financial concessions, was misguided. Admittedly, there are some daunting diseconomies of small scale, especially in transportation, public utility services and infrastructure. Arguably, they make the case for larger government involvement than for larger countries in export promotion, market diversification, and provision of public utilities, all other things being equal. It is also true that the ESC is vulnerable to hurricanes and other weather related events, especially because of export specialization and lack of diversification, but regional compensatory mechanisms of private and informal markets (insurance and remittances especially) made for remarkable resilience to these events.

The main constraints of small size turned out to be limits on feasible economic and development policy strategies. Export diversification was not possible, except for ESC as a region. Financial isolation was not possible, and therefore independent monetary and exchange rate policies were not available. Import substitution was also not possible. In addition, the loss of skills was a more severe constraint than for larger countries.

These constraints still left ESC countries with a sufficient choice of policy instruments and strategies for sustained improvement in HD, particularly when those strategies were pursued as a region. Where countries failed to improve HD indicators or lagged other ESC, it was a result of the futile pursuit of economic strategies that were inaccessible because of their small size, e.g. import substitution, lower trade to GDP ratios, monetary policy independence, or private sector led export diversification.

Changes in the international environment

Integration of ESC economies into the global economy via trade, finance and movement of people is of long standing, and was characteristic of all ESC throughout the 1945 - 2000 period. However, there were major changes in technology and international thinking and policy, affecting the position of the ESC in the global economy. It was the changes in technology, particularly with respect to travel and communications, that had profound effects on the structure of ESC economies (the goods and services produced and sold, domestically and for export) and on their HD progress. The most far-reaching effects were the migration of a significant proportion of ESC populations to North America and the UK and the resulting emergence of a Caribbean diaspora in those countries; and the emergence of tourism as the dominant export activity. The changes in international economic policy and thinking had no measurable impact on the ESC - the amendment and elimination of special trading arrangements, lowering of tariffs and other trade barriers, changes in the international exchange regime, relaxation of restrictions on financial transfers, commodity price volatility, and swings in flows of international borrowing and lending.

The importance of large scale migration from ESC countries in the post-war period may be seen in the degree to which it relieved unemployment, and in the flow of remittances to all ESC countries. The imposition of restrictions by receiving countries in the 1960s arrested the flow of new emigrants, but the overseas community in North America and the UK was so large by the 1980s that remittances grew to become of overwhelming importance for poorly performing ESC countries, especially Guyana and Jamaica. The size of the diaspora and the depth of familial ties between the Caribbean and the diaspora facilitated a continuing migration flow, in spite of tougher admission rules. The diaspora grew to be a major market for specialised tourism services (music festivals, carnivals) and cultural exports, especially music.

Technical change is the aspect of globalisation which has had the greatest effect on the ESC's relationship with the rest of the world. It made possible the switch from agricultural export to tourism based economies. Telecommunications technology contributed directly to higher HD, and also opened the market for cultural products from the Caribbean. However, the ESC failed to capitalise on export possibilities in information services. ESC producers (including cultural producers outside niche markets) were not competitive with North America, and commercial technology altered tastes away from sustainable consumption.

The folding of Commonwealth trading agreements (affecting sugar and bananas) into the EU-ACP agreement, and the modifications in the agreement over time, were undoubtedly a factor in the evolution of the agricultural sector in ESC countries, but they were by no means the determining factor in the demise of export agriculture. Even with the support price under the CSA and Lomé arrangements, ESC sugar & banana producers lost money, and ESC output was seldom large enough to fulfill their quotas under the agreements. The economic returns to agriculture were not competitive with those from real estate. Except for Belize and Guyana, farm sizes were too small, and acreages too little for available technology, which has high fixed costs and large economies of scale.

The transformation of the GATT into the WTO, the introduction of the CBI and the establishment of NAFTA - none of these had any lasting effect. Textile exports to US, manufactured from US raw materials, surged temporarily, but wage costs (largely reflecting HD gains) put ESC (and other LAC countries) out of that market, once Asian countries entered in a big way. There was nothing in the international agreements to benefit the services in which the

ESC had an actual or potential comparative advantage – i.e. tourism, culture or information services.

The international debt and financial crises of the 1980s and 1990s had no effect on financial flows to ESC countries because the external funding for the ESC came mainly from sources that were segmented from the markets in London and New York. Foreign inflows were mainly project specific FDI in the public and private sectors, with significant market borrowing from time to time by Jamaica, T&T and Barbados. The sources of funds were often ESC residents, using their overseas accounts, and members of the Caribbean diaspora, rather than international fund managers, and transaction sizes were too often too small to be of interest to big fund managers. However, there was some rollover risk, on occasions when international financial markets contracted, as in the case of Barbados during Gulf War of the early 1990s.

Commodity price volatility had an impact mainly through oil prices. That impact was large only on isolated occasions, and it was not sustained. Terms of trade losses were also small, largely because export agriculture, which was the source of most of the impact, had declined so severely in the ESC.

ESC trade policies largely reflected changing international intellectual fashion, after the mid-1960's, when countries embarked on independent trade policies. From the mid-1960's to the late 1970's futile attempts were made to reduce the trade to GDP ratios by imposing high tariffs, other trade barriers and domestic content stipulations. These efforts were replaced by trade liberalisation measures from early 1980's onward. None of these measures had any noticeable effect on the trade to GDP ratio, so perhaps no harm was done.

Competitiveness

Natural resources and technology largely determined the choice of export, apparently, but competitiveness determined which products failed and which succeeded. Competitiveness was determined by the quality of the product, the intensity and penetration of marketing, the degree of innovation and market appeal and other non-price factors.

[Figure 7]

Price competitiveness was not an important strategy in the development of the ESC. In a comparison of wages of the ESC and neighbouring countries, we find that Trinidad and Tobago and the tourism-based economies generally did well in spite of uncompetitive wages. Comparing the two countries which retained an important agricultural base (Belize, which did comparatively well, and Guyana, which did not) we find that Guyana’s wage costs were much lower than Belize’s, in US$ equivalents. Further evidence may be found in Jamaica, where there was no correspondence between trends in wages and trends in economic performance. Before mid-1970s, when economic performance was generally better than ESC average, wages were comparable to those elsewhere in the ESC. Subsequently, Jamaica’s performance was persistently inadequate, during periods when wages were contained (e.g. in the 1980s) as well as when wage costs spiralled out of control (e.g. in the late 1990s).

Fiscal policy and human development

Fiscal policy that respected prudent financing limits had powerful effects in enhancing HD, via education, health & sanitation, public utilities, physical infrastructure, maintaining the rule of law, and providing social security. These expenditures made direct contributions to material wellbeing, and they contributed indirectly to increased productivity, through improvements in skills, communications and transport, etc. However, fiscal excesses in some countries undermined HD and led to regression, by eroding the purchasing power of wealth stored in assets denominated in domestic currency, and creating uncertainty about future values, leading to permanent and ongoing outflow of human resources and finance.

Although much has been made of the economic management, good and bad, of various administrations of ESC countries, particularly since independence, the only example of good government economic policy contributing to the development of any ESC country is the performance of the Eric Williams administration in T&T during the 1970s. In most other cases (Bahamas, Belize, Barbados, the OECS countries) countries have prospered with no contribution from government economic policies, while in the cases of Guyana, Jamaica and T&T after Eric Williams, government economic policies have been a brake on economic development. In contrast, government social development policies, reflected in spending on education, health, housing and social amenities (access to water, electricity, etc) have had a high payoff in human development gains, in all countries.

With respect to tax policy, to the extent that the burden was shifted away from taxes on consumption and imports, and towards an efficiently administered income tax, there would have been a contribution to improved equity and a corresponding improvement in human development. However, in many countries the burden shifted away from the income tax in the 1980s and 1990s, another way in which government policy inhibited development.

[Figure 8]

Both from the point of view of expenditure allocation and that of the tax structure, the period from the late 1940s to the early 1970s was the era when government polices made a substantial contribution to human development in the ESC. Government expenditure on education, social security and other social services increased significantly, as a percentage of GDP. Tax systems shifted significantly towards income taxes, which had an important and beneficial redistributive effect. This was the period of greatest gains in HD in the ESC, and government policies clearly played an important role in helping to lift HD indicators from low to medium-to-high ranges, by international standards.

[Figure 9]

By comparison, since the mid-1970s ESC government policies have made little apparent contribution to HD gains, and in some cases have put a brake on HD advances. Government expenditure on the social services stabilised or fell, relative to GDP. Tax system changes worsened the distribution of income, except in the case of Jamaica. Unsustainable fiscal policy, and the resulting balance of payments crises, foreign exchange shortages and economic stagnation, had an adverse effect on HD indicators in Guyana and Jamaica.

The one overtly "development strategy" of independent ESC governments which made a positive contribution to the growth of HD was the state-financed energy-based industrialisation policy of the T&T government in the 1970s. All other government development initiatives were innocuous at best, and at worst inhibited HD growth. That is true of import substitution policies, export promotion policies, policies to promote agriculture, tourism, industry and small business, nationalisation and state enterprises, financial and trade liberalisation policies, privatizations and other "structural" reforms. All ESC countries flirted with policies that were popular at one time or other over the course of the 1945 - 2000 period. In those countries that pursued them as part of a mixed economy strategy, development oriented policies did no good, but they caused no harm either. In Jamaica and Guyana, state control of major sectors, their development strategy of choice in the 1970s, inhibited HD by depressing economic output; and their later conversion to "Washington consensus" policies did nothing to rectify this situation.

The lesson for "development strategy" is similar to that gleaned from the experience of the Asian Tigers (Amsden, 1992; Perkins, 1994; Page, 1993, Stiglitz and Yusuf, 2001): focused government industrial promotion and finance, on a sufficiently large scale and sustained over several years, can play a major role in developing new areas of comparative advantage which can lift a country's potential growth and boost HD. The characteristics of the T&T experience of the 1970s included assistance that was massive and focused on a single sector, providing externalities. In addition, government absorbed several years of losses at start-up, thereby providing a platform on which private investment was able to build a profitable competitive energy-based industry.

Much has recently been made of the importance of policies for macroeconomic stability and structural reform, the so-called Washington consensus (Williamson,1999). ESC experience suggests that the only items of importance in the Washington consensus list are fiscal discipline and expenditure on social services. Expenditure on social services has a major positive impact on HD. Other fiscal policy is no more than a preventative: lack of fiscal discipline damages HD prospects, but fiscal discipline of itself does nothing to enhance HD. In the experience of the ESC, other elements of the consensus were either innocuous or harmful, as in the cases of tax reform (since the mid 1970s), interest rate liberalisation, competitive exchange rates and trade liberalisation, privatisation and deregulation.

Money, monetary policy and financial services

The improvement in the scope, range and availability of financial services made a major contribution to the improvement in the quality of life in the ESC, especially with the introduction of hire purchase (HP) and household mortgages in the 1950s and 1960s. In addition, banks did a good job of financing the working capital needs of companies, including the provision of trade credits. The financial sector played only a small part in the financing of investment, but that was because funding for profitable, internationally competitive investment was always in surplus, from the retained earnings of conglomerates and trading companies, and from foreign sources.

Monetary and financial policies in the ESC missed the mark, by and large. Central banks, established in the 1960s and 1970s, tried to control the money supply, with little success, and to no good purpose, because a dependable relationship between money and inflation (which was what the central banks aimed to control) proved to be undetectable. In the end the US$ turned out to be the only reliable standard of value, and the stability of the local currency (LC) in terms of US$'s the best guarantee that people would expect low rates of inflation.

Financial policies were concerned to switch funding from households to firms, and from consumption to investment. In the 1960s and 1970s the central banks issued directives on credit allocation, and governments set up state banks and development banks. When these proved wasteful and ineffective, governments and central banks fostered stock exchanges (SEs) and nonbank financial intermediaries (NFIs), which proved equally ineffective, and in addition exposed the financial system to the risk of a major crisis.

Central banks in the ESC proved their worth by improving the range of macroeconomic data and analysis generally available, helping to sharpen public awareness and public understanding of economic issues, and coordinating monetary and fiscal policy. Judged by these criteria the region's central banks did a tolerably good job, a fact which is obscured by conventional economic assessments, which use the effectiveness of monetary policy as their yardstick. In addition, in the wake of a spate of financial failures in the 1980s and 1990s, central banks took a more prominent role in financial regulation.

Investment

Investment creates the productive capacity to drive the economy forward. In policy discussions about ways to speed up investment, there continues to be a focus on acquiring more financing, as though more financing guarantees higher investment. In fact, for most of the post war period, financial resources were in excess of amounts needed for competitive investment projects in the ESC. What limited investment was a perceived scarcity of viable investment opportunities in the tradable sector.

Over the medium term, very open economies such as those of the Caribbean are limited by the pace of expansion in exports of goods and services such as tourism. Everything that is produced in the Caribbean has a large import content, so the proceeds of exports must be sufficient to supply imports needed for the production of the exports themselves, plus imported inputs for all other production and the general import needs of population. If exports do not grow rapidly enough, the supply of imports slows down, and so does the growth of the economy. Therefore it is the capacity to export, and the investment needed to expand that capacity, which sets the limit to the sustained growth of open economies.

There is no evidence anywhere in the ESC that potentially profitable investment in tourism, minerals, manufacturing exports or agricultural exports had to be delayed or abandoned simply because there was insufficient finance in the economy. When I mention this, people immediately cite examples of projects they know of personally that couldn’t attract funding. However, these projects were never ones in which they were personally prepared to invest money that they could not afford to lose.

There is ample evidence of the abundance of finance in the high reserve requirements central banks imposed on commercial banks throughout the region, typically 6 percent or more, when banks' cash fluctuations suggest that 2-3 percent would have been ample. What is more, banks almost always exceeded the requirements, by large amounts. Here was a pool of funds which, had they been invested, would have added several percentage points to investment ratios.

Moreover, banks financed very little capital formation that led to increases in productive capacity, other than commercial mortgages for hotel construction. What evidence we have suggests that the largest source of financing for investment was the financial surpluses of the investing companies themselves, and their associates, with bank finance being used mainly for working capital.

In any case, investment ratios in the ESC were very respectable by international standards. The gross capital formation ratios to GDP were in the region of 20 percent for most countries, and in some countries there were periods when investment to GDP ratios reached 30 percent or more. These ratios are comparable to those of south and east Asia. The problem appears to be that this investment was not as productive as expected, perhaps because a large proportion was invested in the nontradable sectors of the economy.

Summing up

- The material wellbeing of the populations of the ESC was transformed in the second half of the 20th century, from among the most desperately inadequate in the world, to an adequate, and in some cases, a superior quality of life, by comparison with countries worldwide.
- Even though ESC populations continued to improve their quality of life in the 1980s and 1990s, the major improvement in the indicators of HD came in the 1950s and 1960s.
- Government expenditures on health, education, social services, public utilities and infrastructure played a major role in the improvement of the quality of life. Their impact was reinforced by tax policies that helped to redistribute wealth and ensure a better sharing of gains in the period up to the mid-1970s.
- Equally important was the role of households in improving their own quality of life, taking advantage of whatever avenue was made available – migration, education, thriftiness, household mortgages, hire purchase and informal financing arrangements.
- While government social policies were crucial for HD, government economic policies were beneficial only in the case of Trinidad and Tobago, and there only in the 1970s, when government financed the development of a major new export sector. Other government economic policies were innocuous at best, immiserising at worst.
- Small size was not a limiting factor for HD, though it did limit the range of available policy options.

- Developments and changes in international trade and financial markets were not a determining factor in the HD of the ESC, but inappropriate reactions to global developments had severely adverse consequences.
- Development in the ESC can be described as dependent in that almost all the initiatives for investment in the export and tourism sectors came from foreign sources, with the exceptions of energy based industry in Trinidad, and two innovative hotel companies in Jamaica.

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Figure 1. HDI 2003

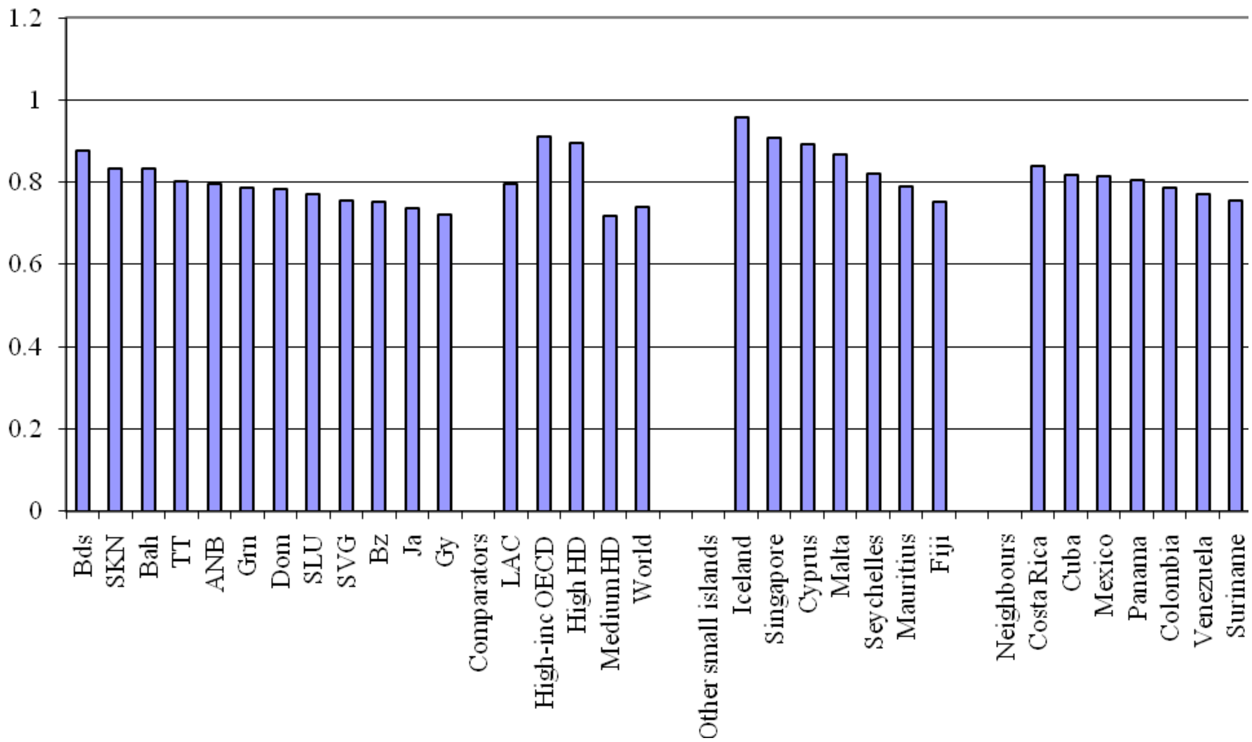

Figure 2.
Life expectancy, 2000

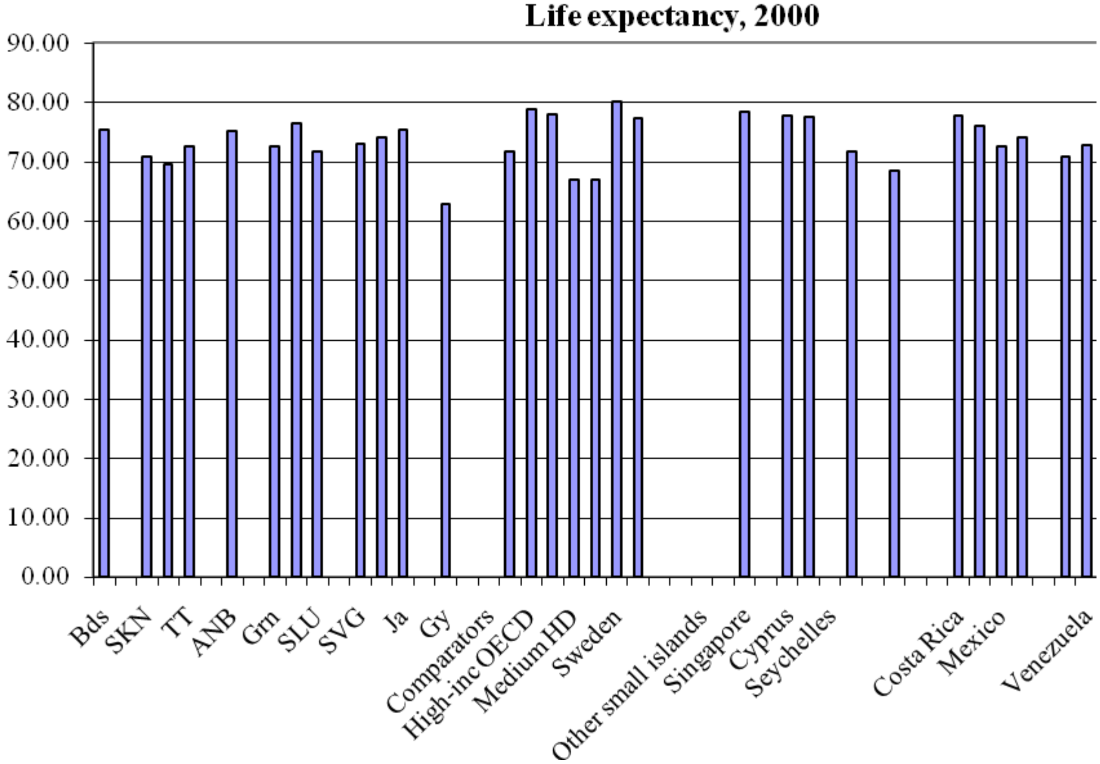

Figure 3. Life expectancy trends - males

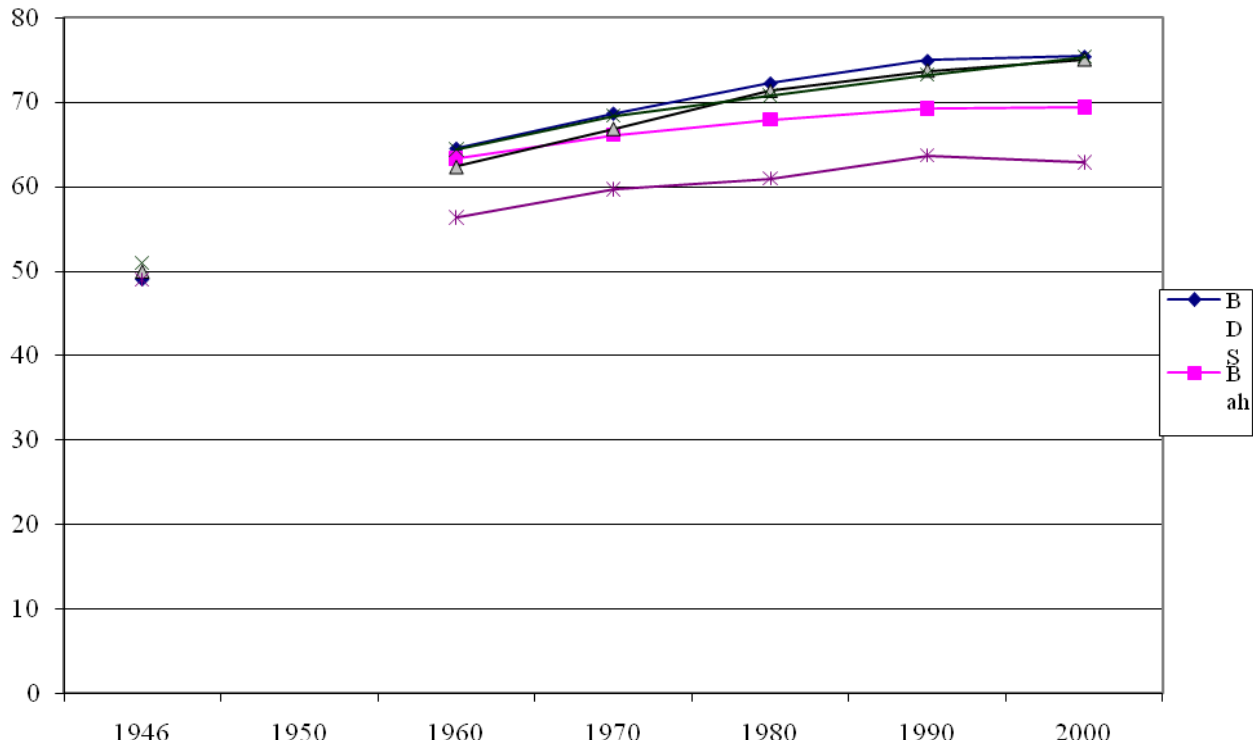

Figure 4. Adult Literacy Rate

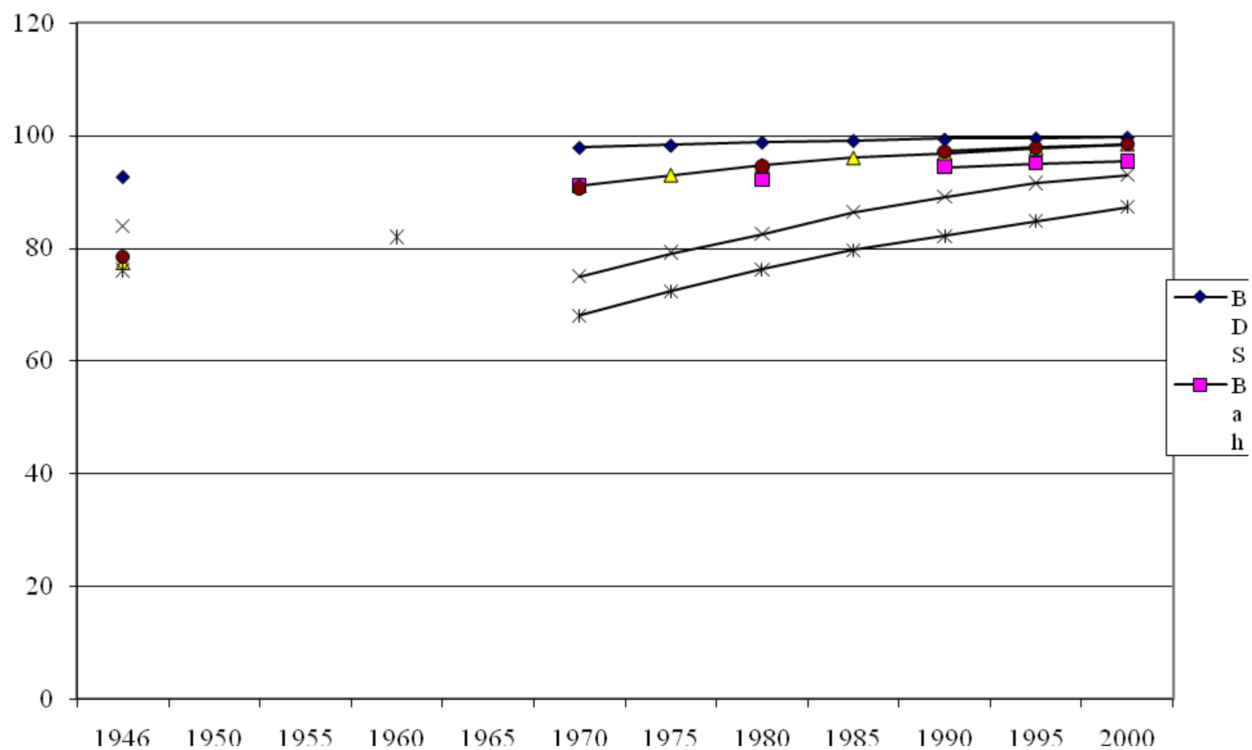

Figure 5. Infant Mortality

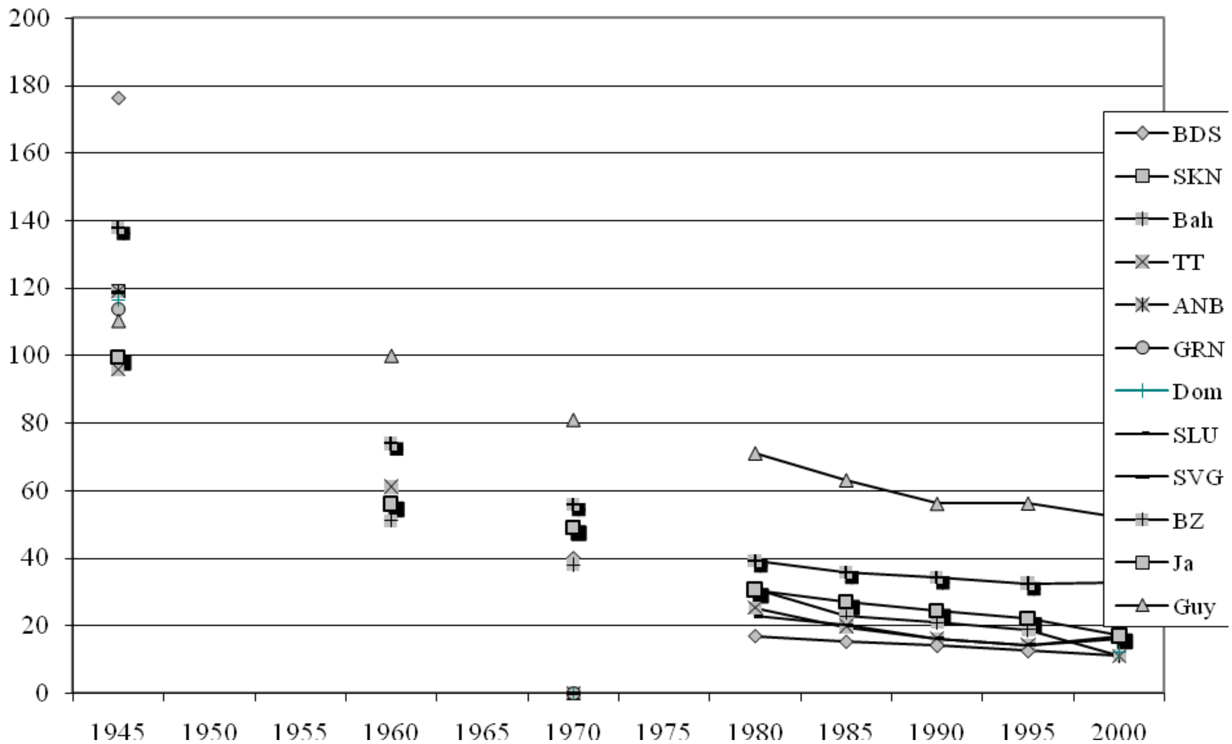

Figure 6. GDP per capita, 1995 US$

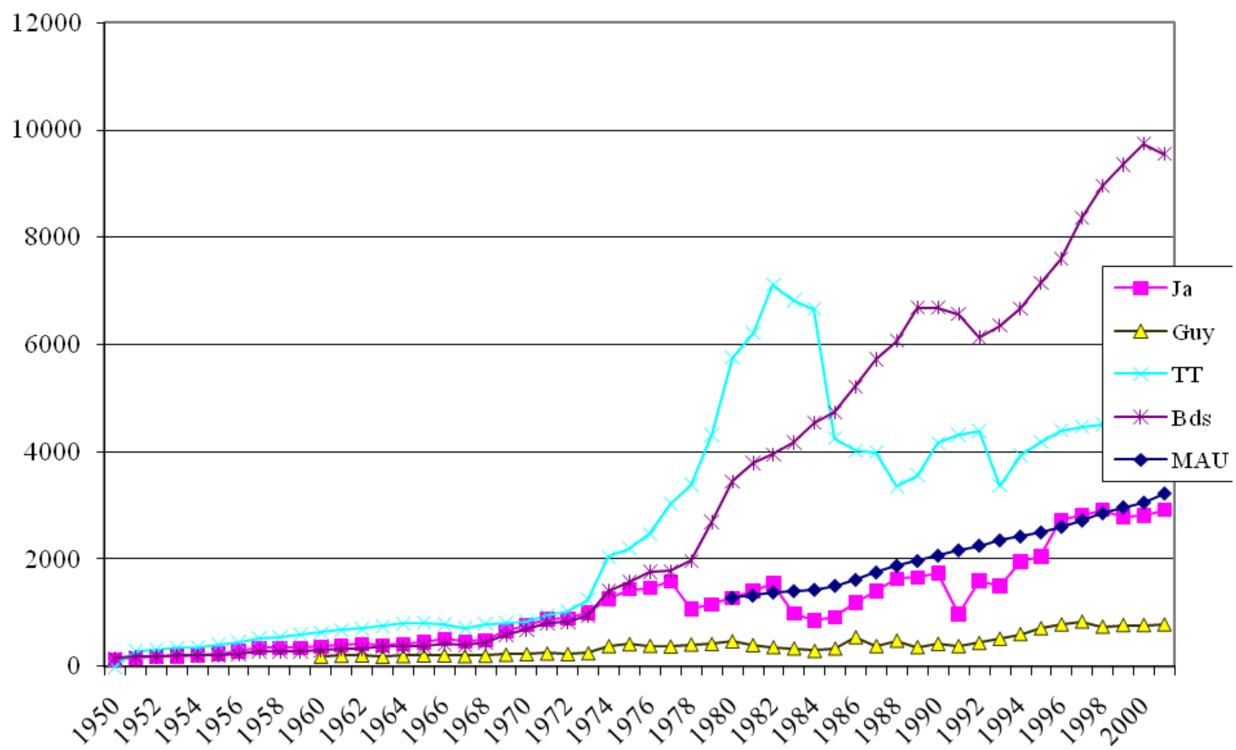

Figure 7. Wage comparisons, US$ equiv.

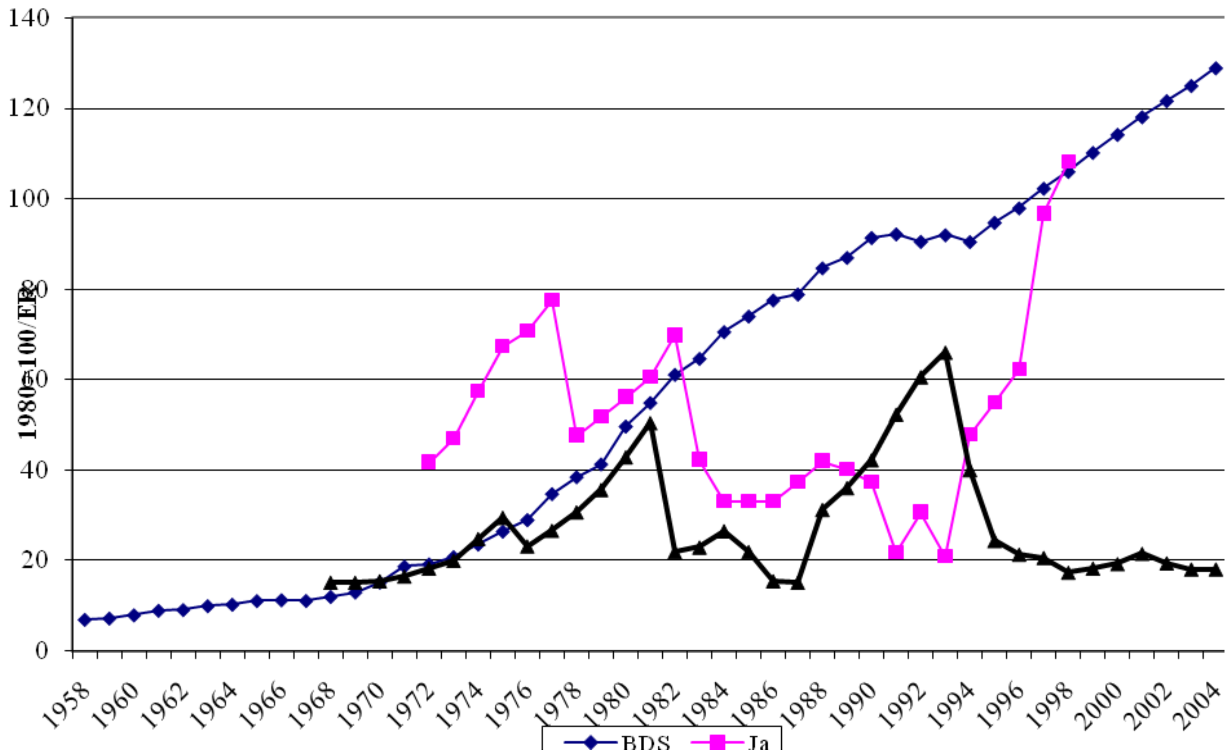

Figure 8. BDS - govt expenditure

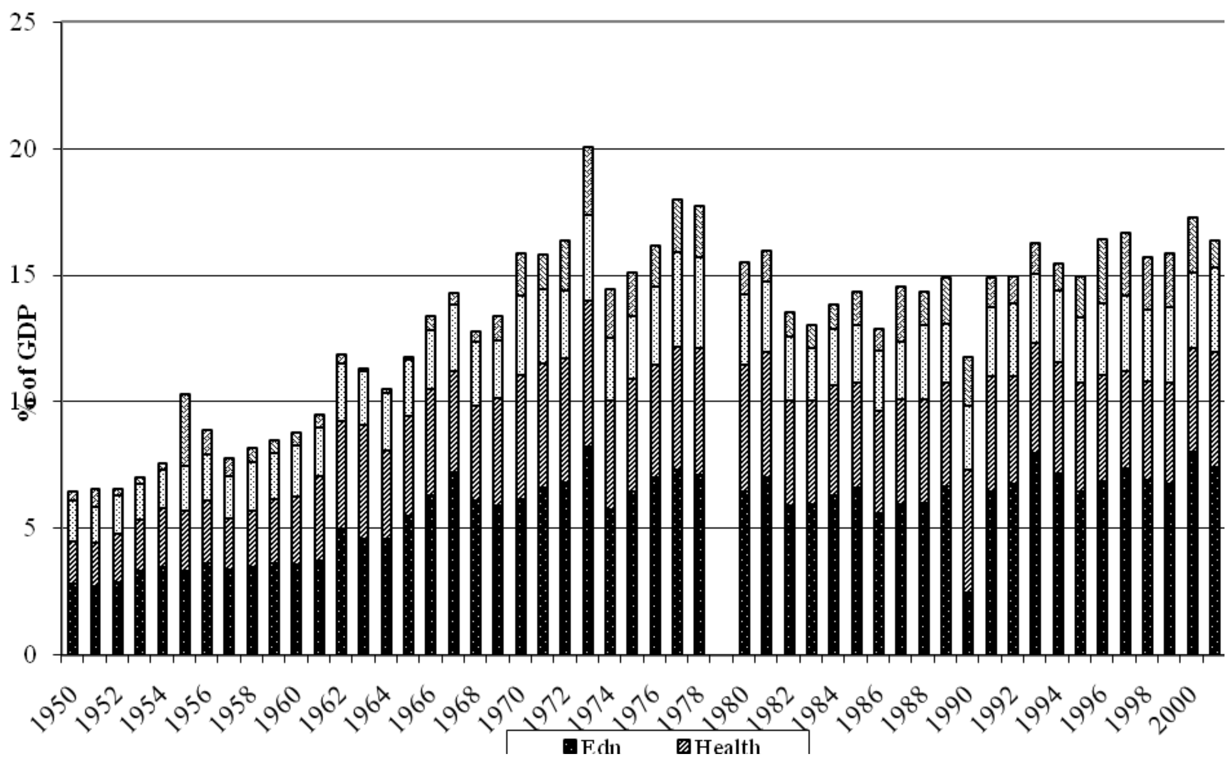

Figure 9. BDS - indirect taxes to total