

## HANDOUT 2-1

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### EXERCISE 2-4: CARIBBEAN OPEN TRADE SUPPORT (COTS)

#### SUMMARY

The purpose of this contract is to support program development, implementation and achievement of USAID/J-CAR's Regional Strategic Objective (RSO 9) "**Caribbean region positioned to succeed in an open trade environment.**" In order to achieve this strategic objective, two Intermediate Results (IRs) have been identified, specifically **IR1, Market opportunities leveraged through open trade** and **IR2, Natural assets and national investments protected.** Two lower-level IRs have been developed under IR1. They are **IR1.1, Key regional impediments to open trade mitigated** and **IR1.2, Improved market access for target countries.** The Contractor is expected to achieve these results through activities developed under this contract. Activities are expected to stimulate economic growth and to improve employment opportunities within the Organization of Eastern Caribbean States (OECS), and ultimately the Caribbean Community (CARICOM), through the strengthening of mechanisms leading to an open trade environment for the region. Results sought under this contract will contribute to new employment resulting from the removal of many administrative barriers to trade and investment as well as the creation of jobs across national boundaries. There will be an informed and improved OECS private sector as well as strengthened public-private sector partnerships that foster business growth and support increased and improved economic performance by enterprises in the sub-region. There will be improved disaster and physical planning frameworks which include policies focusing on reducing the risk of catastrophic loss from natural disasters and increasing resilience in the aftermath of natural disasters. These frameworks will provide a planning approach that better sustains the gains achieved in the strengthened economic base of the OECS and ultimately the wider Caribbean region.

The ultimate goal of the program is to facilitate the transition of the region to open trade and to position the countries to compete successfully and sustainably through galvanized private sectors that are charged to take on the challenges of the new trading agreements. To implement this goal, the focus of the program will primarily be the OECS and selected OECS member countries. The program will seek to develop and implement successful economic growth models of assistance at the country level; at the same time, the program will assist selected regional and sub-regional institutions to the extent that assistance at those levels supports or facilitates progress at the country level.

#### BACKGROUND

##### Introduction

The countries of the Caribbean, with their geographic dispersion, small size, and physical vulnerabilities, face new challenges of global economic competitiveness while traditional buffers such as preferential trade and direct foreign assistance decline. They are faced with emerging economic, social and political challenges as they adjust to an open trade environment being demanded of them under the various international trading agreements. The convergence of these various global processes including, the Free Trade Area of the Americas (FTAA), the World Trade Organization (WTO), the African, Caribbean and Pacific/European Union (ACP/EU)

trade regimes, as well as the region's push to create a single market and economy, have created a sense of crisis in the CARICOM countries. This situation provides the region now with an historical opportunity to restructure and galvanize the economies of each member state. Political and business leaders, while apprehensive about the transition, will be more receptive to economic policy change and reform over the next several years than at any time in the recent past.

Since the year 2000, countries in the Caribbean have been grappling with difficult fiscal and public debt situations, resulting from economic slowdown and from efforts to maintain domestic employment and incomes in the face of reduced external demand for traditional export products. Fiscal and debt bearing capacities remain two major constraints on the financing of development in most countries. Efforts are being made by some countries to develop new non trade-based, fiscal revenue structures which are broad based and capable of generating revenues on a sustainable basis. At the same time attention must be paid to improving public expenditure management. There is greater recognition of the onerous debt service implication of expensive, short-term credit from private sources and of the need to closely align the creation of public debt with fiscal capacity and strategies for sustainable economic growth.

Concomitant with small market size, the region's limited natural resource base, and the need to meet the commitments of the international trading arena, is a lack of an aggressive entrepreneurial spirit in the region's business sector, which significantly affects the capacity of businesses to increase intra-regional trade or successfully compete in international markets. The transformation of this sector so that it can meet these challenges is therefore critical and urgent in order to ensure that the region's competitiveness is enhanced. This transformation requires a rethinking of established economic paradigms and current policies and must be fast-forwarded if the region is not to be left behind in global trade.

The current effort to create a single economic space in the region -- through the CARICOM Single Market and Economy (CSME) -- as part of the process of increasing production efficiency and broadening the product range, is therefore critical to advancing the well-being of the region. This process needs to be accelerated with significant attention paid to removing the physical and institutional infrastructural constraints that inhibit accelerated social and economic development in the region. Fortunately, and somewhat belatedly, the region is attempting to implement this process by the year 2008.

The transformation needed to compete successfully in the evolving global trading environment comes against a background where the region is highly susceptible to natural disasters such as hurricanes, landslides, and earthquakes. Each time a natural disaster occurs, scarce resources must be redirected to rebuilding damaged assets to the detriment of sustainable development of the region's economic base. This issue is compounded by weak policies, institutions, processes and political will to address sustainable development in a holistic manner that includes specific measures to reduce vulnerability of communities at risk and the built environment and to mitigate environmental degradation caused by economic activities.

### **The Role of the Public and Private Sectors in the Caribbean Business Environment**

In the Caribbean, governments are involved in activities that go beyond what can be traditionally considered their core responsibilities – maintenance of public order, economic regulation, provision of infrastructure, improvement of services to meet

basic human needs, and the administration of safety nets for the poor. They have been involved in areas such as managing airlines, hotels, businesses which are the domain of the private sector. Modernization of the public sector is therefore necessary and has been influenced by the growth of the middle class, the diversification of the private sector, and pressure from non-governmental organizations (NGOs). The continued impetus for public sector modernization requires public education and bi-partisan support for reforms. One major aspect of public sector modernization in the Caribbean concerns the need for transfer of several activities, in part or in full, from the public sector to the private sector. The move towards heavier reliance on the private sector as the engine for change and development will involve building capacity in the private sector to take on these new tasks and employ a larger share of the labor force.

The transfer of appropriate activities from the public sector to the private sector and NGO's will release governmental financial and managerial resources for use in critical sectors such as the legal system, public health and safety, protection of the environment, and administration. Caribbean governments are a long way from satisfactorily fulfilling all of these functions. Given their limited resources, governments in the region cannot successfully perform all of them. Therefore, public-private dialogue is essential for determining priorities and agreeing on standards.

### **Legal and Administrative Infrastructure**

Another area requiring attention is the necessity to ensure that an enabling and supporting legal and administrative infrastructure is in place to facilitate trade and private sector growth and development. This is applicable at two levels. First, coming out of trade negotiations by the Regional Negotiating Machinery (RNM) and implementation of FTAA, WTO, and other trade agreements, as well as steps to move towards a common market and single economy, OECS countries and ultimately the wider Caribbean will need to develop or revise legislation, regulations, and administrative procedures to participate in and benefit from these new trading regimes and relationships. Second, recent investor and business road map studies performed under the 2000-2004 USAID Caribbean Regional Program, as well as studies by other local and international institutions, identify a number of legal and administrative infrastructure changes needed to create an environment conducive to new business investment and increased trade, even before considerations related to new trade agreements are factored in.

Some updating of laws and governing structures to address changes in the business environment have occurred in the region. However, revisions of laws pertaining to trade and other commercial matters, and the development of the capacity to implement the new laws, need continuous attention and support.

### **Competitiveness**

On the business front, the manufacturing sector continues to be adversely affected by competitiveness issues related to high unit production costs and relatively small volumes, with the overall situation being exacerbated by the prospect of increased competition resulting from ongoing trade liberalization. In recognition of the difficulties facing manufacturing and commodity production, the region should make a stronger thrust towards the development of services and higher value-added specialty products. This direction provides increased opportunities for product differentiation and utilization of the region's human resources and creativity. Even though tourism will continue to serve as one of the region's main business activities, the competitiveness of the region within the global market and the quality of the tourism

product will need to be improved. This improvement is especially important as the region prepares to host the World Cup Cricket in 2007, an event that will result in a tremendous influx of first-time visitors to the region, as well as creating awareness of its offerings among over a billion persons via television and other communications links.

While overall progress is taking place in the development of market-based economies in the region, the private sector needs to become more dynamic, proactive and competitive. The great need in this regard is to help the region unlock its entrepreneurial spirit and to encourage shifting from old paradigms to new ones, such as the need to continuously innovate so that the region's goods and services are competitive regionally as well as internationally. Advocacy organizations, self-regulating organizations, and other professional associations must be further developed so they can play a role in encouraging and strengthening public-private dialogue and policy debates that promote a supportive and enabling environment for investment and growth. Presently, business associations lack the ability to actively and positively influence the business environment in a significant way.

The low levels of business experience within the region's private sectors are exacerbated by the inability of most enterprises to independently produce coherent business plans, conduct market research, make financial forecasts, and other analyses required by potential lenders. However, access to current market information, industry trends, buyer and supplier networks, and accepted standards is vital to creating and managing competitive businesses. Managers and entrepreneurs in the CARICOM nations commonly do not have access to existing market information or the skills required to do research directly applicable to their business. This deficiency will become increasingly important as the region surges forward to embrace a single market and single economy among its 14 countries.