

TRADE AND PAYMENTS IN THE CARIBBEAN COMMON MARKET
THE CASE FOR A CARICOM RESERVE FUND

by

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The Case for a CARICOM Reserve Fund

The negotiations which led to the establishment of CARIFTA in 1968 and subsequently CARICOM in 1973, were based on a desire to create an environment which would encourage an expansion in intra regional trade. It was hoped that regional trade expansion would help to overcome the constraints to trade expansion experienced by the participating countries, brought about by the increasing difficulties they were facing, in gaining access to markets in the developed market economies of North America, Western Europe and Japan, particularly, for their manufactured products.

There had been substantial growth in intra-regional trade involving the major countries, Barbados, Guyana, Jamaica and Trinidad and Tobago, up to 1975. But in the post 1975 period further regional trade expansion has been curtailed as a result of license and quota restrictions imposed by Jamaica and Guyana, arising from the severe deterioration in their respective balance of payments positions. Therefore new initiatives in regional payments arrangements will be required to complement regional trade expansion. In this paper it will be argued that a new initiative in the form of a CARICOM Reserve Fund would be ideally suited to perform this function. Before proceeding with an outline of the operation of such a Fund, there will be a review of developments in CARICOM trade with a view to showing the importance of this trade to the four major countries. This will be followed by a critical examination of the current CARICOM payments arrangement.

In 1969, the first full year of CARIFTA, the total value of domestic

Table 1*

Total Domestic Exports/CARICOM Exports⁽¹⁾ 1969 - 1975

U.S. \$ Millions

Country	1969	1970	1971	1972	1973	1974	1975
<u>Barbados</u>							
Domestic Exports to CARICOM	4.5	5.6	6.9	8.7	10.6	14.7	16.2
Total Domestic Exports	28.7	31.0	28.3	30.9	40.0	61.4	88.9
CARICOM %	15.7	18.1	24.4	28.2	26.5	23.9	18.2
<u>Guyana</u>							
Domestic Exports to CARICOM	13.3	13.2	16.8	18.0	19.0	29.7	40.5
Total Domestic Exports	116.9	132.4	141.8	136.0	127.8	267.7	324.3
CARICOM %	11.4	10.0	11.8	13.2	14.9	11.1	12.5
<u>Jamaica</u>							
Domestic Exports to CARICOM	9.2	10.5	13.8	19.9	24.2	31.3	33.0
Total Domestic Exports	247.3	334.9	351.2	343.1	382.5	705.8	800.0
CARICOM %	3.7	3.1	3.9	5.8	6.3	4.4	4.1
<u>Trinidad and Tobago</u>							
Domestic Exports to CARICOM	36.2	41.6	53.0	55.7	69.5	136.5	141.5
Total Domestic Exports	467.9	470.7	532.5	514.7	654.7	1924.7	1618.5
CARICOM %	7.7	8.8	10.0	10.8	10.6	7.1	8.7
Total CARICOM Exports	63.2	70.9	90.5	102.3	123.3	212.2	231.2
Total Domestic Exports	860.8	969.0	1053.8	1024.7	1205.0	2959.6	2831.7
CARICOM %	7.3	7.3	8.6	10.0	10.2	7.1	8.2

1) Items in SITC Classes 0-8

*Sources. Estimated from annual external trade reports of each country converted to U.S. dollars at the central market rate reported in International Financial Statistics.

Table 2

Total Exports/Regional Exports of Manufactured Products⁽¹⁾ 1969 - 1975

U.S. \$ Millions

Country	1969	1970	1971	1972	1973	1974	1975
<u>Barbados</u>							
Exports to CARICOM	2.4	3.1	3.6	4.9	6.8	9.1	10.7
Total Exports	6.3	7.8	7.7	10.8	16.4	21.5	25.6
CARICOM %	38.1	39.7	46.8	45.4	41.5	42.3	41.8
<u>Guyana</u>							
Exports to CARICOM	1.4	2.0	2.8	4.5	5.9	6.2	7.7
Total Exports	3.8	4.1	4.6	5.7	7.2	7.6	8.5
CARICOM %	36.8	48.8	60.9	78.9	81.9	81.6	90.6
<u>Jamaica</u>							
Exports to CARICOM	7.1	8.1	9.8	13.0	15.4	21.0	22.2
Total Exports	21.5	21.7	28.1	26.6	27.7	35.9	37.8
CARICOM %	33.0	37.3	34.9	48.9	55.6	58.5	58.7
<u>Trinidad and Tobago</u>							
Exports to CARICOM	15.4	19.5	24.3	25.4	30.5	43.7	47.5
Total Exports	58.3	55.1	58.9	59.2	61.6	100.3	93.1
CARICOM %	26.4	35.4	41.3	42.9	49.5	43.6	51.0
Total CARICOM Exports	26.3	32.7	40.5	47.8	58.6	80.0	88.1
Total Exports	89.9	88.7	99.3	102.3	112.9	165.3	165.0
CARICOM %	29.3	36.9	40.8	46.7	51.9	48.4	53.4

1) Items falling within SITC classes 5-8

* Source: Same as for Table 1

central banks and monetary authorities. This has resulted in a change in the arrangement incorporating multilateral settlements and substantial increases in the lines of credit. The CARICOM Multilateral Clearing Facility which came into effect in June of 1977 with an overall credit limit of US \$ 40 million, currently has a credit limit of US \$ 80 million. The lines of credit for each participant are set out below.

Table 3*

CARICOM Multilateral Clearing Facility

U.S. \$ Million

Participant	Line of Credit
Barbados	11.0
Belize	10.0
E.C.C.A.	16.0
Guyana	19.0
Jamaica	18.0
Trinidad & Tobago	6.0
<u>Total</u>	80.0

*Source: Bank of Jamaica, Quarterly Bulletin. Vol. XVII, No. 3, September 1978, p. 12.

The Facility operates on the basis of semi annual settlements. Settlements are carried out on a multilateral basis with the Central Bank of Trinidad and Tobago acting as agent for the Facility. At the settlement periods, debtor countries are required to make a minimum payment, normally 50 percent, of their outstanding indebtedness with the Facility. Nominal interest rates of 5 percent are chargeable on debit balances during a settlement period to Guyana, Barbados, Jamaica and Trinidad and Tobago, and 3 percent to Belize and the E.C.C.A.

fact there were negative net private capital inflows in 1976 and preliminary estimates for 1978 indicate a similar situation.^{6/}

Table 4

Jamaica: Foreign Exchange Earnings from Major Export Activities
US \$ Mn. (At Exchange rate; \$1.00 = US \$1.10)

	1974	1975	1976	1977	1978
Bauxite/Alumina ⁽¹⁾	185.6	153.5	130.4	189.5	138.7
Sugar	81.1	153.7	61.5	59.5	58.2
Bananas	12.7	16.1	13.1	14.6	16.8
Tourism	133.3	128.5	105.7	72.0	98.3

D Production levy and royalties.

Source: Bank of Jamaica. Report and Statement of Accounts
Annual
Department of Statistics. Statistical Yearbook 1977

In view of these developments the government has been obliged to rely increasingly on external loans from both official and private agencies to satisfy minimal current spending. In 1977 and 1978 the greater portion of this borrowing was in the form of instruments with a period to maturity of less than five years. In 1976, the portion of direct government and government guaranteed external debt, with a term to maturity of less than five years, accounted for 24 percent of the government's external indebtedness. By 1978, these short term debts accounted for 46 percent of official external debt. The dependence on short term credits, and the higher costs associated with such credits, adds considerably to the burden of debt service charges in international payments and compounds the difficulty of dealing with the payments problem. In 1977, the estimated cost of servicing official debt, US \$191.9 million, absorbed 27 percent of foreign exchange receipts from all

Table 5

Foreign Exchange Reserves End of Period 1968-1977

US \$ Millions

Participants	1968	1969	1970	1971	1972	1973	1974	1975	1976	1977
Barbados: Total Reserves	15.5	12.5	14.6	15.2	22.8	26.6	33.3	32.5	21.0	29.7
Change in Reserves		-3.0	2.1	0.6	7.6	3.8	6.7	-0.8	-11.5	8.7
Guyana: Total Reserves	22.3	19.3	18.5	23.8	31.7	9.1	55.6	90.2	23.2	19.7
Change in Reserves		-3.0	-0.8	5.3	7.9	-22.6	46.5	34.6	-67.0	-3.5
Jamaica: Total Reserves	112.9	108.6	123.3	150.8	152.2	119.7	184.1	120.6	31.5	30.9
Change in Reserves		-4.3	14.7	27.5	1.4	-32.5	64.4	-63.5	-89.1	-0.6
Trinidad/ Tobago: Total Reserves	47.6	41.9	35.9	54.4	43.2	38.4	374.9	720.2	972.5	1433.4
Change in Reserves		-5.7	-6.0	18.5	-11.2	-4.8	336.5	345.3	252.3	460.9
ECCA: Total Reserves	22.9	12.0	12.3	17.7	7.6	28.5	24.5	50.2	64.4	--
Change in Reserves		-10.9	0.3	5.4	-10.1	20.9	-4.0	25.7	14.2	--
Total Exchange Reserves	221.2	194.3	204.6	261.9	257.5	222.3	672.4	1013.7	1112.6	--

A) From 1968-1972 estimated by subtracting Barbadian holdings from total ECCA external asset holdings.

Source: International Monetary Fund: International Financial Statistics
 Eastern Caribbean Currency Authority Economic and Financial Review

from the fund to reduce its overall balance of payments deficit, as measured by a decline in its gross foreign currency holdings, by one half, up to an amount such that its cumulative debt with the fund would be limited to a maximum of twice the value of its deposits in any year. Each participant would be required to use subsequent surpluses, calculated as an increase in its gross foreign currency holdings, to repay its debt to the fund, subject to the constraint that this would not absorb more than 50 percent of its surplus in the year subsequent to the deficit. Any participant being in a position of net indebtedness with the fund for four consecutive years would be subject to contractual amortization of the debt over a period not exceeding four years.

In table 6 is set out annual end of year estimates of foreign exchange reserves of the participants on the assumption that the fund had been in existence since 1969 with the automatic borrowing privileges described above. It is assumed here that all borrowing from the fund would be for payments to non CARICOM members. It is further assumed for purposes of this illustration that the usage of foreign exchange over the period would not have been affected by the existence of the Fund. Accordingly, it might be argued that our estimates of users changes might understate the actual changes which might have taken place had the fund been in existence. Based on these annual estimates of reserves we have derived estimates of the deposits with the Fund by the various participants. These are set out in Table 7. At the beginning of 1977 deposits with the Fund would have been US\$ 237.1 million. In the years 1969 through 1974 there would have been moderate fluctuations in exchange holdings. The large growth in exchange holdings in the subsequent period is entirely a result of the rapid growth in the foreign exchange reserves of Trinidad and Tobago.

Table 6

Adjusted⁽¹⁾ Foreign Exchange Reserves with CARICOM Reserve Fund 1968-1977

US \$ Millions

Participants	1968	1969	1970	1971	1972	1973	1974	1975	1976	1977
Barbados	15.5	14.0	14.3	14.7	22.1	26.6	33.3	32.9	27.0	28.3
Guyana	22.3	20.8	19.7	21.7	29.0	19.0	45.7	90.2	56.7	19.7
Jamaica	112.9	110.8	121.1	150.8	152.2	136.0	167.8	144.2	65.5	30.9
Trinidad/Tobago	47.6	44.8	40.4	47.0	45.1	41.7	369.2	720.2	972.2	1433.4
ECCA	22.9	17.5	14.9	16.3	8.6	21.9	24.5	50.2	64.4	--
Total	221.2	207.9	210.4	250.5	256.9	245.2	640.5	1037.7	1185.6	--

1) Adjustment based on automatic borrowing privileges designed to offset 50 percent of foreign exchange losses subject to the constraints outlined in the text.

Hypothetical Debt Positions With the CARICOM Reserve Fund

US \$ Millions

Participants	1969	1970	1971	1972	1973	1974	1975	1976	1977
Barbados									
Yearly borrowing ⁽¹⁾	1.5	--	--	--	--	--	0.4	6.0	--
Yearly repayments ⁽²⁾	--	0.3	0.5	0.7	--	--	--	--	1.5
Cumulative debt	1.5	1.2	0.7	--	--	--	0.4	6.4	4.7
Guyana									
Yearly borrowing ⁽¹⁾	1.5	1.2	--	--	9.9	--	--	33.5	--
Yearly repayments ⁽²⁾	--	--	2.1	0.6	--	9.9	--	--	--
Cumulative debt	1.5	2.7	0.6	--	9.9	--	--	33.5	--
Jamaica								(3)	
Yearly borrowing ⁽¹⁾	2.2	--	--	--	16.3	--	23.6	34.0	--
Yearly repayments ⁽²⁾	--	2.2	--	--	--	16.3	--	--	--
Cumulative debt	2.2	--	--	--	16.3	--	23.6	57.6	57.6
Trinidad/Tobago									
Yearly borrowing ⁽¹⁾	2.9	4.5	--	1.9	3.4	--	--	--	--
Yearly repayments ⁽²⁾	--	--	7.0	--	--	5.7	--	--	--
Cumulative debt	2.9	7.4	0.4	2.3	5.7	--	--	--	--
ECCA				(3)					
Yearly borrowing ⁽¹⁾	5.4	2.6	--	1.0	--	--	--	--	--
Yearly repayments ⁽²⁾	--	--	1.4	--	6.6	--	--	--	--
Cumulative debt	5.4	7.0	5.6	6.6	--	--	--	--	--
Total borrowing	13.5	8.6	--	2.9	29.6	--	23.6	73.5	--
Borrowing % of deposits	30.5	20.6	--	5.8	57.7	--	18.4	35.4	--

- 1) Yearly borrowing set at a limit of 50 percent of the annual reduction in gross foreign exchange holdings.
- 2) Yearly repayments restricted to a maximum of 50 percent of the annual increase in gross foreign exchange holdings.
- 3) Borrowing restricted below 50 percent of reserve reduction to restrict net indebtedness to twice the level of deposits held with the fund.

Table 9

Hypothetical Net Position With CARICOM Reserve Fund

US \$ Millions

Participants	1969	1970	1971	1972	1973	1974	1975	1976
Barbados	1.6	1.6	2.2	2.9	4.4	5.3	6.3	0.4
Guyana	3.0	1.5	3.0	4.3	-4.1	3.8	9.1	-15.5
Jamaica	20.4	22.2	24.7	30.2	14.1	27.2	10.0	-28.8
Trinidad/Tobago	6.6	1.6	7.7	7.1	3.3	8.3	73.8	144.0
ECCA	-1.6	-3.5	-2.6	-3.3	1.7	4.4	4.9	10.0

Net position represents the difference between the annual value of deposits and the cumulative debt of the participants.

short and long term interest of that country. It was pointed out in the first section of the paper that it was the country that had borne the major share of the reduction in regional trade, following the restrictions imposed by Jamaica and Guyana, in the past 1975 period. This was particularly true in the case of manufactured products where, between 1975 and 1977, its regional export sales declined by 28 percent. This decline in regional sales was not offset by increased sales to extra regional markets. Sales of manufactured products, excluding chemicals, that is, items falling within SITC classes 6 to 8, declined from TT \$85.3 million in 1975 to TT \$67.3 million in 1977.^{11/} Overall sales of manufactured products did not suffer as major a decline due to increased sales of chemical products. Nevertheless, export values for 1977 were still below those of 1975.

A revitalization of the CARICOM market is important to that country's export trade in the more labour intensive manufactured items, such as, clothing and appliances and in this way to overall employment in the country. To this extent relinquishing sovereignty over a part of its foreign exchange reserves to the fund can be viewed as a means of providing indirect support to output and employment in those export sectors mentioned above, in so far as it helps to ease the payments problems of its partners. A placement of 20 percent of its foreign exchange holdings in the fund would still have left the country, based on end of the year estimates for 1977, with US \$1,146.8 million for investments in the major financial centres.^{12/}

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