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International Agricultural Trade and Policy Center

Economic Asymmetries, Trade Liberalization And Integration: Issues And Policy Implications For CARICOM Countries

By

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MISSION AND SCOPE: The International Agricultural Trade and Policy Center (IATPC) was established in 1990 in the Food and Resource Economics Department (FRED) of the Institute of Food and Agricultural Sciences (IFAS) at the University of Florida. Its mission is to provide information, education, and research directed to immediate and long-term enhancement and sustainability of international trade and natural resource use. Its scope includes not only trade and related policy issues, but also agricultural, rural, resource, environmental, food, state, national and international policies, regulations, and issues that influence trade and development.

OBJECTIVES:

The Center's objectives are to:

- Serve as a university-wide focal point and resource base for research on international agricultural trade and trade policy issues
- Facilitate dissemination of agricultural trade related research results and publications
- Encourage interaction between researchers, business and industry groups, state and federal agencies, and policymakers in the examination and discussion of agricultural trade policy questions
- Provide support to initiatives that enable a better understanding of trade and policy issues that impact the competitiveness of Florida and southeastern agriculture specialty crops and livestock in the U.S. and international markets

ABSTRACT: Much has been written about the challenges facing CARICOM as a result of the liberalization, globalization and integration phenomena. This paper adds value to the conversation by addressing the nexus between and among economic asymmetries, trade liberalization and economic integration, as it relates to CARICOM as small developing economies. The paper seeks to highlight the salient issues of CARICOM economic adjustment challenges under trade liberalization and integration imperatives, particularly as they may be subjected to the *constraints* of economic asymmetries. In doing so, it steps away from the conventional approach of reciting a series of data usually associated with the issues and instead, engages in commentary and assessment regarding the changing economic landscape in the Region and elsewhere. The issues are indeed very complex and the arguments and conclusions flowing from this type of evaluation may not be in lock-step with the conventional wisdom. However, it is our contention that the regional trade and development policy solutions does not lie in *denial* of the existence of the problems; but rather, in tackling them head-on and incorporating them into existing and proposed systems of economic relations.

ECONOMIC ASYMMETRIES, TRADE LIBERALIZATION AND INTEGRATION: ISSUES AND POLICY IMPLICATIONS FOR CARICOM COUNTRIES[1]

Lurleen M. Walters, Garfield G. Lowe, and Carlton G. Davis[2]

Background

Multilateralism has emerged as the dominant feature in recent global trade policies in lieu of bilateral and preferential agreements between countries. The establishment of the World Trade Organization (WTO) in 1995 gave credence to this trend and many countries have benefited substantially since its inception. Inclusion in the international trading framework is particularly important for developing nations if they are to likewise benefit, since participation in liberalized trade has often been touted as a necessary (if not sufficient) condition for long run economic growth and development. The potential gains appear most lucrative in terms of increased export opportunities arising from trade policy reform concerning products of existing and prospective interest to developing nations. Quota elimination, tariffication on non-tariff barriers (NTBs), tariff reduction, agricultural trade reform, and increased bindings on developing country exports are some of the mechanisms that are expected to favor trade prospects for the vast majority of participants in the trading regime (Dornbusch, 1992).

The Uruguay Round of the GATT/WTO embodies the most comprehensive global trade policy agenda to date. Its salient aspects include, among other things: (1) reciprocal multilateral trade agreements based on prohibition of non-tariff barriers and the progressive reduction of tariffs; (2) market-driven imperatives and performance-based results; (3) increased cooperation at the regional and sub-regional levels oriented toward open regionalism; (4) linkages between trade and other economic and non-economic areas of liberalization such as finance and investment, skilled workers and management and; (5) contractual obligation between parties with respect to predictability and certainty

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of agreements (Davis et al., 2001). These rules are applicable to all member countries of the WTO.

It is increasingly apparent however, that specialized multilateral policies may be necessary for proper incorporation of developing nations into the WTO liberalized trade framework. It is now an accepted fact that total compliance with WTO rules requires a multidimensional infrastructure to facilitate the process. From our perspective however, it is difficult to think of any single dimension more contentious to the incorporation of developing nations into the WTO trade regime than the existence of economic asymmetries among WTO member countries. Within the multilateral trading system, economic asymmetries are generally viewed in an abstract sense as disparities in levels of development among countries. However, conceptually speaking, asymmetry is a much broader and flexible designation than that of the concept of "level of development." SELA (1997) argues that the former "...can be used to compare specific sectors or aspects within a country or between countries, as well as of the relations among them" (p.5). It should be apparent however, that there is a close relationship between basic asymmetries and levels of development. It is within the context of this associated relationship that economic asymmetries function as serious impediments to equitable trade relations among countries at different levels of development (Briguglio, 1995; Bardouille, 2000).

The fact that economic asymmetries exist and is pervasive globally is not a point of contention (UNDP, 1998). Although economic asymmetries are multi-faceted, it is none-the-less true that the most frequently mentioned dimensions of the phenomena relate to: (1) *production structure*; (2) *human resources training;* and (3) *infrastructure* (SELA, 1997). The generalized global response to these three dimensions has historically been via the principle and operational mechanisms of Special and Differential Treatment (SDT) within the spheres of trade, finance, and cooperation. However, under the umbrella of the WTO trade regime, the principle and operational modality of *reciprocity* has taken center stage and has been legally sanctioned and enshrined in legal agreements and obligations. On the other hand, while SDT has not been revoked or abandoned in multilateral trade relations, it has been relegated to a *discretionary status*. The net effect is that unlike reciprocity as a modality of trade, SDT lacks legal force and predictability (SELA, 1997).

The convergence of issues surrounding economic asymmetries, trade liberalization, and global/regional integration, takes on special significance for Caribbean Community and

Common Market (CARICOM) countries as small developing economies.[3] To be sure, *size* in all of its dimensions (economies of scale, economies of scope, geographical, etc.) is a key element of all three indicator dimensions of economic asymmetries pointed out earlier. In short, size is a dynamic force *shaping* the configuration of countries' production structure, infrastructure, and human resource quality (Bernal, 1994; Armstrong and Read, 1998; Davis et. al., 2001). Of the 193 small economies worldwide, CARICOM is a microcosm of this situation. By virtue of size alone, structural dimensions of the region have proven to be problematic in terms of planned transition into rules-based trade, owing to the existence of extra and intra-regional economic asymmetries. To compensate, member states have been the beneficiary of a number of preferential/nonreciprocal trading agreements with several industrialized nations (Lomé Convention; CBI; CARIBCAN). WTO statutes mandate that such arrangements are antithetical to liberalized trade and thus provide a platform for revocation. Should this occur, structural adjustment might be difficult. Two key questions that are being debated within (and outside) of this trading bloc are: (1) Can the region effectively compete without preferential status? and (2) What policies must the region undertake to minimize adjustment costs and maximize gains? These two questions rank high among the pertinent issues that must be addressed by regional policy agenda and WTO and Free Trade Area of the Americas (FTAA) protocols.

Much has been written about the challenges facing CARICOM as a result of the liberalization, globalization and integration phenomena. This paper adds value to the conversation by addressing the nexus between and among economic asymmetries, trade liberalization and economic integration, as it relates CARICOM as small developing economies. This paper seeks to highlight the salient issues of CARICOM economic adjustment challenges under trade liberalization and integration imperatives, particularly as they may be subjected to the constraints of economic asymmetries. In doing so, it steps away from the conventional approach of reciting a series of data usually associated

[3]CARICOM countries include: Antigua and Barbuda; Bahamas (a member of the Community, but not the Common Market); Barbados; Belize; Dominica; Grenada; Guyana; Montserrat; Jamaica, St. Kitts and Nevis; St. Lucia; St. Vincent and the Grenadines; Trinidad and Tobago, and Suriname. Haiti is formalizing arrangements to complete its full entry; it does not yet apply the trade policy. Associate Members are: British Virgin Islands; and Turks and Caicos Islands. Observer States are: Anguilla, Dominican Republic; Netherlands Antilles; Puerto Rico; and Venezuela. Within CARICOM, the smaller states are recognized as a subgroup, the Organization of Eastern Caribbean States (OECS). It includes: Antigua and Barbuda; Dominica; Grenada; Montserrat; St. Kitts and Nevis; St. Lucia; and St. Vincent and the Grenadines.

with the issues and instead, engages in commentary and assessment regarding the changing economic landscape in the Region and elsewhere. The issues are indeed very complex and the arguments and conclusions flowing from this type of evaluation my not be in lock step with the conventional wisdom. However, it is our contention that the regional trade and development policy solutions do not lie in denial of the existence of the problems. In this regard, we are in complete agreement with the SELA (1997) argument that solutions "...lies in tackling it head-on and incorporating it definitively into the system of economic relations that is set up" (p. 16).

TRENDS IN TRADE LIBERALIZATION AND INTEGRATION

Since the inception of the General Agreement on Tariffs and Trade (GATT) in 1947, significant progress has been made toward the creation of a global economy. Each successive Round of the GATT has deepened liberalization on a global scale, and sought greater integration of developed and developing nations. In recent years, developing countries have opted for outward-looking (exports-promotion) policies, as opposed to inward-looking (import-substitution) schemes as strategies for economic development and poverty alleviation (OECD, 1992; World Bank, 1996). According to the conventional wisdom, trade liberalization is perhaps best facilitated through economic integration, which involves the harmonization of global policies. As conceptualized by Balassa (1961), economic integration is both state – where discriminatory polices are eliminated between economies; and a process – where measures are implemented to remove such elements. Trade liberalization policies are technically defined in terms of the removal of tariff and non-tariff barriers to make trading systems between countries more open or neutral along a trade liberal/non-liberal continuum (Bhagwati, 1998; Davis et. al., 2001). In the case of both liberalization and economic integration, the establishment of economic linkages between entities is essential to the achievement of common goals.

Molle (1997) demonstrated the two major aspects that are involved in economic integration. The first aspect entails the integration of product and factor markets through Free Trade Areas (FTAs), customs unions, and common markets.[4] The second aspect

[4]Current literature uses liberalized trade and free trade synonymously. Strictly defined, free trade refers to trade without restrictions, whereas liberalized trade is a lessening of trade restrictions. In highlighting the differences between the two concepts, Ballayram and Davis (1997), show that public policy intervention is absent from free trade, unlike liberalized trade. Within FTA, trade within the group is duty free; but each member can set its own duty rates on imports from non-members. Within a custom

involves policy consolidation between nations to concretize the union. It is typical for the latter to include the formation of supranational entities through which monetary, fiscal, and social policies are harmonized.

Most countries in the world are members of some form of regional trade agreements (RTAs). At the end of the year 2000, there were over 200 RTAs recorded as providing notice to the GATT/WTO over time. According to WTO data (WTO, 2001b), there are currently 150 agreements in force, with the majority being concluded in the past 10 years. Of some significance however, is the fact that since 1995, over 100 agreements in goods and/or services have been notified to the WTO. Also, many countries hold multiple-agreement membership, and in many instances, there are differences in rules among agreements. WTO data (2001b) also shows that 60 percent of the notified RTAs in force in 2000 were among European countries. In contrast, roughly 15 percent of the total number of RTAs was among developing countries. It should be noted that within the context of the WTO regime, RTAs are not confined to countries belonging to the same geographical area. However, from a factual standpoint, RTAs are organized according to geographical location.

An increasing number of agreements are in existence in the Western Hemisphere. For example, South American nations participate in the Andean Group, the Southern Cone Common Market (MERCUSOR), and the Latin American Integration Association (LAIA), which encompasses both groups. Likewise, trade between Central American nations is governed by the Central American Common Market (CACM). Since the 1970s, Caribbean countries have participated in an RTA called CARICOM and more recently, the Organization of Eastern Caribbean States (OECS), which is a subgroup of the smaller Eastern Caribbean states country grouping within this trading agreement. Countries within these groupings were defined earlier. Prior to 1994, the United States and Canada traded via the Canada-US Trade Agreement (CUSTA); in 1994, it was subsumed by the North American Free Trade Agreement (NAFTA), which also includes Mexico. There exists considerable overlap in some cases, as in the Group of Three (G-3) arrangement between Mexico, Venezuela, and Colombia. This is indicative of countries' aims to maximize economic benefits under these arrangements. Table 1 shows selected economic indicators for some of the many Western Hemisphere trading arrangements (Caribbean Publishing Company, 2002).

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union, all members charge the same set of customs duty rates on imports from non-members.

Tremendous interest has also been demonstrated with respect to the proposed hemispheric RTA, the Free Trade Area of the Americas (FTAA) that will be fully implemented by 2005. Some 34 countries are expected to participate, and its specific goals will include: (1) trade liberalization; (2) elimination of investment restrictions; (3) freer movement of specialized workers; (4) harmonization of tax and monetary policies; and (5) the creation of a supra-regional institution for administrative purposes (Davis et al, 2001). According to the World Bank (2000), the reasons for regionalism are both political and economic in scope. Increased security, greater bargaining power accruing from increased size, and the advancement of government agenda through commitment mechanisms *inter alia* are common political reasons. Key economic considerations pertain to "scale and competition" effects, which evaluate increases in market size and scale efficiencies; and "trade location" effects, which assess trade creation and diversion, and resource redistribution.

The motivation for regionalism appears to differ between developed and developing countries. For example, the US has actively participated in various agreements with the following objectives in mind: (1) to address the relative decline in its economic and technological position; (2) dissatisfaction with GATT's ability to further US interests; and (3) the formation of the European Union (EU). One may characterize this behavior as 'trade seeking'. In contrast, economic survival appears to be the impetus for Latin America and Caribbean countries. Increased market access, foreign investment, and negotiating power are among the primary goals given in this regard (Bouzas and Ros, 1994). It should be recognized however, that the benefits of regionalism might not be readily apparent in some instances. Analyses of economic integration arrangements and their associated trade liberalization components tend to focus on net welfare effects via estimates of trade creation and diversion impacts.

In reference to the proposed FTAA, Singer (1995) alluded to the difficulty in ascertaining such impacts. In spite of this problem, there appears to be movement toward some consensus regarding the overall positive effects of such movements. For example, analysis by Burfisher (1998) shows RTAs have greater trade creation effects where: (1) larger unit production costs differences exist within the RTA; (2) smaller cost differences exist between members and nonmembers; (3) higher pre-RTA tariffs, and lower post-RTA tariffs exist between the RTA and nonmembers; (4) larger trade flows occur between natural trade partners; (5) the member country's supply and demand responsiveness is greater and; (6) the pre-RTA structure of members' economies is more competitive. It should also be noted that in this type of analysis, the following factors stand out: (1) differences in production costs; (2) relative supply and demand responses; and (3) initial tariff rates. According to the Burfisher (1998) finding, where these factors diverge considerably between countries, there is increased potential for considerable gains. Similar conclusions were arrived at by Robinson and DeRosa (1995), whose evaluation of several RTAs indicated a greater likelihood for trade creation as opposed to trade diversion. However, according to these studies, positive effects were guaranteed only if countries desisted from erecting formal trade barriers for non-member countries (Burfisher, 1998; Robinson and DeRosa, 1995).

Dornbusch (1992) and Haveman et al. (2001) discussed the various benefits accruing from trade liberalization and integration initiatives for developing nations within a globalized framework. According to their assessment, improvements in resource allocation, and increased access to markets and technologies are major benefits that could fuel economic growth and development to these countries. However, they also concluded that these impacts are usually not readily discernable from empirical estimating models, due to the myriad factors affecting growth. The lack of an internationally comparable indicator of economic *openness* is another constraint. Recently, this latter issue has been receiving increased attention in the economics literature, particularly with respect to the impacts of economic reforms in developing countries (Ballayram, 2001).

An Inter-American Development Bank (IDB, 1997) study raised the issue regarding the "appropriateness" of economic reform measures as they reflect indicators of openness and other aspects of country liberalization initiatives. This particular study (IDB, 1997) points out that economic data sets such as exchange rate differentials, inflation rates, tax structure and so on, deal with outcomes rather than the policies that give rise to them. In other words, it is argued that from a policy analysis perspective, these variables provide limited information regarding the impacts of structural policy mechanisms on the growth and development process in developing countries. We argue here that these structural policy variables assume high levels of economic relevance within the context of the impacts of economic asymmetries as they relate to liberalization and integration. In an attempt to address this issue, Lora (1997) developed structural policy indices for twenty Latin American and Caribbean countries in an attempt to measure the degree of market freedom (openness), as reflected in country economic policies. Methodologically, the indices are developed for areas covering: (1) trade; (2) taxation; (3) finance; (4) privatization; and (5) labor. In each of the five areas indices of market freedom (openness) are estimated. The structural policy index is a simple average of the indices in the five areas. The index can take on a value of zero to one, where 0 and 1 are the worst and best observations respectively, on market freedom in a particular country.

From the perspective of economic liberalization, the structural policy index is useful in providing some indicator of the degree to which countries are departing from past ways of operating their economies. Also from the perspective of Latin American and Caribbean countries, these indices suggest the relative degree of progress in market freedom (openness) achieved by Caribbean countries vis-à-vis other Latin American countries. Specifically, the computed indices shows that Jamaica, a CARICOM member country, registered the highest and continuous movement in market freedom among the twenty Latin American and Caribbean countries studied over the 1985-1995 period. The index for Jamaica was 0.426 in 1985; but increased to 0.684 in 1995. These values are higher than the average reported for the other countries in the sample (Lora, 1997). These estimates offer some additional evidence that the *existence* of liberalization, economic integration, and economic asymmetries are moving in lock step with each other and as such, would be better addressed together within a policy framework.

It is now quite clear that once countries are involved in RTAs that their economies, sectors, and firms must adjust quickly to increased competitive forces. Wherever such adjustments fails to occur, short run losses in government revenue, industries dislocation, rising unemployment, among other things, are the typical results. Although welfare economics theory generally assumes compensation of 'losers' by the 'winners', in reality, it is difficult to establish the required mechanisms for such adjustments to take place. As a result, the reality is that some members will benefit at the expense of others (Balassa, 1961). In a worst-case scenario, economic liberalization/ integration may widen the gap between trading partners, particularly if the aforementioned compensatory/adjustment mechanisms are lacking. Once again, we reaffirm our earlier proposition that economic asymmetries are *not neutral* with respect to the impact of liberalization and integration regimes. We further propose that from both theoretical and operational modality perspectives, compensatory/adjustment mechanisms are appropriate policy measure when such conditions exist.

CARICOM Overview

CARICOM[5] was created on July 4 1973 by the Treaty of Chaguaramas signed in Trinidad. Encompassing 14 countries, it has a total population of about 6.5 million and a combined GDP of approximately US$22 billion. Regional per capita GDP is roughly US$2,800. Tables 2, 3, and 4 provide a listing of selected economic indicators for CARICOM countries. The data contained in the tables demonstrates**,** among other things: (1) the disparity *between* these indicators and those of other Western Hemisphere

[5] See footnote 3 for country composition of CARICOM.

Countries[6] and (2) disparity *among* CARICOM countries themselves. It is our contention that these disparities taken together are tangible evidence of economic asymmetries with respect to: (1) production structure; (2) human resources; and (3) infrastructure. These asymmetries serve to mute or blunt the potential positive gains accruing from reciprocity-based liberalized trade and integration movements.

CARICOM governments have viewed regionalism as an important precondition for greater inclusion into the global economy, and have gradually eliminated intra/extra regional trade restrictions in accordance with liberalized trade schemes. Such reforms have led to substantial increases in trade as a percentage of GDP, despite greater import dependency (Tables 2).

There are three stated objectives of CARICOM as a regional integration mechanism. These are: (1) fostering of economic cooperation through the CARICOM Single Market and Economy (CSME); (2) coordination of foreign policy among independent Member States and; (3) provision of common services and cooperation in functional matters such as health, education and culture, communication and, industrial relations (CARICOM Secretariat, 2002a). These objectives have historically been pursued under the regional integration/development strategy known as open regionalism. Briefly described, this approach involves the synchronization of transitional arrangements via negotiations among a number of trading blocs (Davis et al., 2001; Gill, 1997). It should be noted that the CSME operational modality of the regional integration strategy is a work-in-progress. At the present time there are nine Protocols articulating the platform of the mechanism. CARICOM countries are at different stages of signing onto these nine Protocols (CARICOM Secretariat, 2002b). It should be pointed out that there are two (albeit complementary) components to the regional CSME strategy. One aspect is the *Single Market* (SM) dimension which is described as "*...an arrangement which allows CARICOM goods, services, people and capital to move throughout the Caribbean Community without tariffs and without restrictions to achieve a single large economic space, and to provide for a common Economic and Trade Policy*". Another dimension is the *Single Economy* (SE) which is described as "*...an arrangement which further harmonizes economic, monetary and fiscal policies and measures across all Member States of the Caribbean Community to underpin the sustainable development of the Region*" (CARICOM Secretariat, 2002b).

[6] Readers interested in comparative data for other Western Hemisphere countries can consult: Caribbean Publishing Co., 2002; CIA, 2001: UNCTAD, 2000; UNDP, 1998; World Bank, 2001.

Under the CSME initiative, concerted efforts are being made to specialize in key areas where comparative advantages exist, such as the tourism and information services sectors. Success in these areas is viewed as not necessarily a function of size, but more so of competitiveness. In 1998, these sectors contributed roughly 40 percent to GDP, up 15 percent from 1994 (Stotsky et al., 2000). In contrast, other export sub-sectors within agriculture and manufacturing have not been as successful. Reductions in the Common External Tariff (CET) have negatively affected revenue earnings. Moreover, the erosion of preferences, increased competition from NAFTA, and devastation of natural disasters have taken their toll on competitiveness and market share in external markets. It should be pointed out however, that reductions in the CET have benefited CARICOM in terms of consumer welfare and investment. It has led to an overall decrease in domestic prices of import items, and thereby encouraged greater availability of consumer goods. Lower tariffs have also resulted in intra-regional investment. Specifically, total regional and foreign direct investment grew 2.5 percent between 1994 and 1998. Given their strong correlation with production costs, such improvements have been particularly evident in the manufacturing sectors of Jamaica, Barbados, and Trinidad & Tobago (Stotsky et al., 2000).

Despite these successes however, Caribbean leaders have grown increasingly concerned with CARICOM's competitive position within the WTO and the FTAA regimes. They recognize the possibility for tremendous loss, particularly if preferences are completely eliminated. Fears of marginalization are legitimate, since the current level of economic asymmetries in all major dimensions within the CARICOM territory poses as effective constraints to realization of the touted large economic gains from unrestricted liberalization. As argued earlier, since liberalization and integration are joint products, it becomes incumbent upon policy makers to address issues of asymmetry, liberalization and integration together in trade negotiations.

EXPLORING THE ASYMMETRIES, LIBERALIZATION, AND INTEGRATION NEXUS: THE CARICOM PERSPECTIVE

Historical Approaches to Asymmetries

It was pointed out earlier that the traditional approach to dealing with issues of economic asymmetries has been via the principle and practice of Special and Differential Treatment (SDT). It was also pointed out that despite the tendency to discuss SDT primarily within the context of trade issues, the fact of the matter is that it has been extensively applied in areas of financing, investments, and development cooperation. SDT mechanisms have been in existence within Western Hemisphere trade and integration arrangements since the early 1960s. SELA (1997) provides documentation of ten instances where this mechanism has been formally enshrined in regional trading agreements in Latin America and the Caribbean, dating back to 1960. CARICOM is included among the ten trading arrangements, where special reference is made to the distinction made between the More Developed Countries (MDCs) and the Less Developed Countries (LDCs) of that Association.[7]

SELA (1997) also points out that SDT has been extensively applied at the *extra-regional* level toward Latin American and Caribbean countries. Examples cited are: (1) preferential treatment extended to Central American and Caribbean countries under the Caribbean Basin Initiative (CBI), by the United States and (2) by Canada to the Caribbean countries via the Caribbean-Canada Trade Agreement (CARIBCAN); (3) by the United States to all countries of the region (except Cuba) via the Generalized System of Trade Preferences (GSP); (4) by the EU to Caribbean members of the Africa-Caribbean-Pacific Group (ACP) via the LOMÉ Convention and the GSP, and; (5) by the EU to Latin American countries via the GSP. Examples of the extension of SDT to the area of finance are cited for: (1) the practice within the Inter-American Development Bank (IDB) of providing grants loans exclusively to Latin American and Caribbean countries, based on development level criteria and; (2) the World Bank at the international level; financing only developing countries and providing grants concessional loans *exclusively* to low income countries through its International Development Association (IDA) arm.

We pointed out earlier, that under the WTO trade regime, SDT has not been revoked or abandoned. Instead, it has been relegated to a *discretionary* status, while the principle of *reciprocity* has been given legal status. Within the context of the WTO therefore, SDT principle and modality are left to the discretion of the developed members of the approximate 143-member organization. Thus far, this discretionary status has been manifested almost exclusively in terms of an extended transitional adjustment period to the less developed members of the WTO, with respect to liberalization and reciprocity commitments (Ballayram and Davis, 1997; Davis, et al., 2001; Michalopolus, 2000). Davis, et al. (2001) points out that the five foundation liberalization and integrations

[7]The designated MDCs are: (1) Barbados; (2) Guyana; (3) Jamaica; (4) Trinidad and Tobago and; (5) Suriname. The LDCs are: (1) Antigua and Barbuda; (2) Belize; (3) Dominica; (4) Grenada; (5) St. Kitts and Nevis; (6) St. Lucia and; (7) St. Vincent and the Grenadines.

mechanisms of the proposed Western Hemisphere RTA (the FTAA), takes the process well beyond the traditional reciprocity concept among trading partners. If such a concept receives sanction by the WTO, then this would facilitate the up-front treatment of economic asymmetries in hemispheric trade arrangements. However at present, we see little predisposition in this direction on the part of the WTO. Furthermore, the United States as the dominant partner in the FTAA is firmly holding its ground on the reciprocity issue.

We think it is enlightening to the discussion of SDT and that of reciprocity, to differentiate between *conditions giving rise to SDT* and the *performance outcomes of SDT*. SELA (1997) rightfully points out that the former should relate conceptually and operationally to *the problem of categories and graduation*; while the latter should relate to *the effective use of SDT as developmental mechanism and not to reciprocity*. As such, SDT is enshrined in the factual existence of economic asymmetries among countries. It is thus a classification category, which sets certain countries apart from others. SDT for developing nations was established by the Articles of Part IV of the GATT in 1965. The concept of non-reciprocity was later introduced in 1979 under the Enabling Clause of the Tokyo Round which stipulates that 'developing economies must not be expected to provide reciprocity for concessions made in trade agreements, nor are they expected to make concessions that are inconsistent with their development, trade or financial needs' (OECD, 1992; Bardouille, 2000). Consequently, developing nations have been exempt from the fundamental principles/commitments of the WTO/GATT system, which include reciprocity, transparency, national treatment, most-favored nation (MFN) status, nondiscriminatory and predictability through binding of negotiated concessions. Consequently, a two-tiered system has evolved between contracting parties. The first tier is applicable to developed nations and requires full compliance with WTO stipulations. In contrast, the second tier exempts developing countries from WTO obligations, and allows special and differential treatment. We provided earlier examples of some of these arrangements within the Western Hemisphere.

The value of SDT in international trade has been challenged since its intended goals (infant industry protection and balance of payments stabilization) have not been fully realized (OECD, 1992; Michalopoulos, 2000). Rather, it appears that recipients have been disadvantaged in two main areas. For example, strong reliance on non-reciprocal arrangements has effectively barred countries from negotiations that involve their own exports. As such, tariff levels are disproportionately higher on developing country exports, while developed nations have managed to secure major concessions on their products. Furthermore, preferential treatment appears to have hindered economic development in some respects by encouraging rent seeking,[8] resource misallocation, and stagnant productivity.

Such evidence lends support to WTO mandates that explicitly forbid preferential treatment in international trade, except as provided under its exemption and special waiver clause. However, SELA (1997) challenges the conventional wisdom regarding the inherent non-performance bias of SDT mechanisms. Specifically, it argues that the lack of results obtained through SDTs have been due to the development difficulties of the countries of the region (Latin America and the Caribbean) and the weaknesses of the integration schemes rather than to the characteristics of the mechanisms adopted. The SELA document provides an interesting and informative discussion on the development difficulties experienced by the region and some of the weaknesses of the integration schemes.

CARICOM Perspective

Within the context of CARICOM as small developing countries, a critical question has to do with the potential short and long-run impacts of the elimination of SDT on the region's already struggling economy. Empirical studies indicate that short-run economic instability is possible from such action (McIntyre and Gonzales, 2000). Yamazaki (1996) estimated aggregate losses of US $632 million (1992 dollars) due to preference erosion between developing countries and the US, the EU and Japan. Central America and the Caribbean were projected to lose US$58 million – approximately 19 percent of their total pre-WTO benefits from the US and EU markets. Although these impacts may seem minor in comparison to other countries, Davis et al. (2001) points out that the economic significance cannot be disregarded. The high dependency on preferential agreements could very well trigger tremendous losses in all sectors. Market loss, reduced economic benefits, and increased price variability would seriously undermine progress for the most vulnerable economies.

CARICOM member states possess certain structural/institutional characteristics giving rise to asymmetries that could limit trade competitiveness and heighten their vulnerability to disruption by external factors. Specific examples of these asymmetries include, small

[8] Rent seeking refers to the waste of resources to society at large to capture (or create) the private benefits and/or to avoid (or to prevent) the private costs resulting from actual (or potential) government policy or institutional settings (See, deGorter et al., 2001; Just, et al., 1982).

size, disaster proneness, insularity, environmental fragility, and a high dependency on foreign assistance. Without the assistance of SDT, these will undoubtedly have important implications for the region. In the case of CARICOM, size is problematic for the following reasons:

ECONOMIC OPENNESS: Here, high ratios of trade to GDP, and strong correlation between domestic and import prices are key indicators. These arise from the inherent inability of the domestic market to support certain types of production, whether due to limited natural/technological resource endowment, and/or low inter-industry linkages. Foreign exchange earnings and trade taxes generally constitute significant proportions of government revenue. For example, in St. Lucia and Belize, trade taxes comprise more than 50 percent of total government revenue (Bernal, 2000).

EXPORT CONCENTRATION IN FEW MARKETS: Since export diversification is generally infeasible for small economies, they are highly dependent on a narrow range of goods and services within very few markets. Within the OECS Sub-Region of CARICOM, the Windward Island banana sector is a prime example of this phenomenon. In this context, the UK imports roughly 80-90 percent of the exports. Such strong linkage increases CARICOM's vulnerability to unfavorable economic conditions and policies in overseas markets. The banana dispute has become one of the most contentious trade issues confronting the WTO.

LIMITATIONS OF IMPORT SUBSTITUTION SCHEMES: These strategies are generally ineffective for small economies, and may hinder sustainable economic development by encouraging higher domestic prices, inferior quality products, and parallel markets in foreign products (Briguglio, 1995).

LIMITED CAPABILITIES IN EXPLOITING SCALE ECONOMIES: Indivisibilities and limited specialization arising from small size do not bode well for competitiveness in an international setting. The unfortunate results are usually higher average costs associated with production, infrastructural development, and transportation. These may serve as disincentives for investment such that costly concessions are necessary (Briguglio, 1995; Bernal, 2000).

LIMITED SCOPE FOR DOMESTIC COMPETITION: Monopolies and oligopolies naturally evolve since small economies may have extra difficulty in supporting perfectly competitive industries.

ADMINISTRATIVE PROBLEMS: Mediocrity and incompetence are common obstacles to efficiency and performance within the civil service. In some instances, human resource levels are inadequate and specialized skills must be procured from other countries. Alleviation of this problem must precede all attempts to correct the aforementioned deficiencies.

In a study of the proposed FTAA (Harker et al., 1996) discussed the implications for the Caribbean region with respect to size constraints. They found an overall unpreparedness for regional accession to the FTAA, and argued that CARICOM's interests may be better served in the short run by the adoption of policies aimed at correcting major shortcomings. To reduce transitional costs and enhance participation in such agreements, the region must first secure temporary arrangements regarding internal policies in prior negotiations, and engage in joint negotiating strategies. Local policymakers must procure the necessary specialized skills to effectively exploit existing ambiguities in WTO and FTAA policies. If this is not done, developed nations and organizations may be indirectly empowered to issue edicts that disregard regional interests. Finally, measures must also be undertaken to increase the production of exportable goods to mitigate risks associated with limited production ranges (Harker et al., 1996). In spite of these shortcomings however, another study (Armstrong and Read, 1998) noted several advantages of small size. Some of these advantages include factors such as high degree of social homogeneity, cohesion, and cultural identity. Although theoretically these could create a positive environment for economic development, in reality they may not do so. Instead, they may encourage micro-nationalist biases in political policies, which could seriously undermine regionalism and economic progress. This particular disadvantage has been highlighted by Dookeran (1995), who argues that political division within CARICOM - not economic weakness - is the main contributor to regional vulnerability. This implies that leaders must strive for greater solidarity if long-run success is to be achieved. The current CSME underway in the region is a positive step in removing this critical bottleneck.

POLICY IMPLICATIONS AND CONCLUSIONS

Intra-Group Strategy Implications

The basic tenets of conventional (Ricardian and Heckscher-Olin-Samuelson) trade theory assume that transactions are executed in a perfectly competitive environment, and that trade arises from differences in comparative advantage owing to resource or technological endowment. Much of the support in the economics literature for trade liberalization is based on this model. Also, within the context of this theoretical framework, small countries are supposed to benefit *disproportionately* from the opening up of trade with larger countries. This disproportionate accrual of benefits to small states is based on the argument that large countries' domestic price structure will dominate in the determination of world prices and as such, the structure of incentive that prevails will remain unaltered. In contrast, small countries will experience significantly altered prices, which will lead to increased gains resulting from reallocation of production and consumption derived from trade expansion. A critical assumption underlying this argument is that small countries will derive substantially large levels of benefits resulting from scale economies associated with expanded trade (Balassa, 1961; McIntyre and Gonzales, 2000). McIntyre and Gonzales (2000) points out that this theoretical framework abstracts from *adjustment costs* and that such costs on both *private* and *social* accounting bases are disproportionately large for small developing countries. In the case of CARICOM, they conclude among other things, that adjustment costs can significantly erode the potential benefits of trade liberalization in the short to medium term. They further argue that, "*...this provides a strong rationale for the implementation of transitional policies to mitigate the cost of adjustment*". The study provides a comprehensive discussion of the various dimensions of the adjustment costs (McIntyre and Gonzales, 2000).

In terms of the focal points of this paper, a critical connection is that economic asymmetries foster high adjustment costs within trade liberalization and integration movements. We have been advancing the proposition that these asymmetries and their associated adjustment costs are ignored, when in reality they may negatively impact participation in the global economy. The WTO recognizes the need for special treatment for developing economies by advocating: (1) longer time periods for the implementation of agreements and commitments; (2) stipulations requiring all members to recognize and safeguard the interests of developing countries and; (3) financial and technical support to build the infrastructure necessary to implement WTO statutes, and technical standards, and resolve disputes (WTO, 2001a). The underlying objective is to encourage trade activities commensurate with developmental goals. The WTO regime makes no further distinction between developing countries as a general group, and small developing economies as a sub-set of the general group.

The WTO and FTAA herald the new competitive atmosphere in which CARICOM must function. Full participation will first require a complementary economic and social environment at the regional level. Policies must be formed or strengthened to improve competitiveness, reduce socioeconomic adjustment costs, and promote trade reform. Since these are inextricably linked, policymakers must be cognizant of the possible interactions.

Competitiveness is a function of capital productivity and production flexibility. Exploitation of new opportunities will require improvements in these two areas. The issue of freer labor movement within CARICOM must be adequately addressed if appropriate supply responses are to be made. Worker education and training are also crucial. Increased competition necessitates strengthening of corporate linkages through policies that support capital mobility and regional financial integration. Greater involvement in research and development is imperative to develop new products and processes for external markets. Some of these issues are currently being addressed via the protocol of the CSME. However, speedy ratification among member states is essential for progress.

The transition to a more competitive environment will entail major social and economic costs. These must be adequately addressed within the appropriate transition policies in order to minimize loss. To compensate for expected losses in tariff revenue, Stotsky et al., (2000) recommend member states undertake tax reform policies aimed at broadening and strengthening domestic taxation. They also recommend harmonization of tax policies across the region. Losses to industrial sectors could be minimized through policies that emphasize trade reform and improve competitiveness. Moreover, unemployment issues can be addressed through free movement of labor and capital within the region.

Trade reform is of paramount importance. Barclay et al. (2001) give explicit direction in this regard by stating: "*...the Region [CARICOM] should consciously seek to wean itself away from the taste for preferences, and should explore initiatives in trade negotiations and trade diplomacy with a focus towards taking a definitive shift to improve its commercial presence, and to keep itself abreast of knowledge on marketing, distribution and technology*". CARICOM must focus on trade promotion, foreign market creation and market penetration[10]. In an analysis of policy imperatives, Bernal (1994) pointed to the need for reorientation of exports toward the services sector. The significant growth in this area between 1994 and 1998 gives credence to Bernal's position.

The aforementioned strategies will embody deeper CARICOM integration. In recognition of this, regional leaders recently ratified the CARICOM charter via the nine protocols of the CSME to improve coordination of macro economic policies (CARICOM Secretariat, 2002b). Clearly, it is a start, but must be followed through with actual implementation of policy goals and objectives.

Inter-Group Strategy Implications

[10]Market access is not synonymous with market entry. The latter is achieved through active and deliberate efforts to penetrate the market.

The preceding discussion reveals an urgency for explicit recognition and treatment of economic asymmetries due to size constraints, given the fact that SDT and non-reciprocity treatments are likely to receive limited applicability in future agreements given the direction of trade negotiations. In addition to policy adjustment strategies at the national and intra-CARICOM levels, changes must also be made at the international or inter-group levels.[11] According to Bernal (2000), the specialized circumstances of small economies will require multifaceted transition provisions and short term preferential treatment along the following lines:

> **LOWER LEVELS OF OBLIGATIONS**: Smaller economies should only be required to undertake/implement concessions and commitments that are commensurate with their current development, adjustment capacity, and economic needs. Negotiations must be done on an 'issue-by-issue' basis, and must incorporate policies that foster international competitiveness while reducing the costs of adjustment. Exemptions in investment and domestic support may be required.
>
> **ASYMMETRICALLY PHASED IMPLEMENTATION TIMETABLES:** Existing developmental disparities between CARICOM and other countries necessitate different adjustment periods. Concessions similar to those afforded other countries in the past could be considered, for example - Mexico under NAFTA.
>
> **BEST ENDEAVOR COMMITMENTS:** Developed economies must adopt measures that provide temporary easement. For example, special consideration could be given prior to the imposition of duties, and other forms of taxation that affect small economies.
>
> **FLEXIBILITY IN APPLICATION OF DISCIPLINES:** Trade rules should be relaxed in the short run to allow temporary usage of trade restrictions, so as to lessen problems associated with balance of payments and infant industry development.
>
> **ENABLING ACCESS TO MEDIATION:** Small states have limited institutional/economic capabilities to utilize the Dispute Settlement mechanisms of the WTO. Larger economies could provide expertise in this area.

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[11] Some inter-group adjustments are being made that could have significant implications for CARICOM countries. For example, the EU-ACP Cotonou Agreement signed in June 2000, replaces the twenty-five years of cooperation under four successive Lomé Conventions with a new structure of trade and development assistance between the two groups. CARICOM countries are quite apprehensive about the economic impacts of this regime on their economies.

TECHNICAL ASSISTANCE AND TRAINING: Schemes must complement the adjustment process, and promote capacity building. Assistance with WTO and FTAA negotiations/obligations could facilitate timely implementation.

CONCLUDING COMMENTS

The fact that the WTO and FTAA trade regimes link economies with great developmental disparities cannot be disputed. The adjustment costs that are subsequently incurred from such linkage are likely to be great. This has already been recognized and articulated to some degree by the granting of greater transitional time frame for commitment compliance and the granting of special waiver for SDT by the WTO. Similar concessions should be crafted within the FTAA, and it would be reasonable for CARICOM to actively negotiate such concession up front. Apart from effectively facilitating the region's participation in the hemispheric integration RTA, it would permit proper economic and institutional adjustment. It would also significantly reduce the inevitable 'shocks' – since CARICOM would be making the transition from a relatively highly protected to a competitive environment. However, from both theoretical and practical points of view, such considerations probably would be best if they do not last into perpetuity, but must have definite time/target constraints. This suggestion is based on some theoretical *cum* observational assessment that great economic inefficiencies are likely to arise when protective umbrellas are given into perpetuity.

Acquiring temporary SDT status within multilateral trade arrangements is merely one challenge facing CARICOM. Another major challenge comes from within. From all indications, significant progress must be made in terms of deepening regional integration such that benefits can be gained from liberalized trade. In addition to increasing productivity, developing service and value-added industries, and enabling freer movement of capital and labor, CARICOM must maintain its integrity. The CSME is a step in the direction; but speed is of the essence and the process is taking too long. Should the proposed FTAA widen economic asymmetries between the region and other countries such that they cannot be adequately addressed, the subsequent socioeconomic instability, and political division could threaten the very existence of the group.

We are aware that the conventional counter-argument given to SDT is that they intrinsically distort competition in trade relations. This assertion however, is not universally embraced by economists and trade analysts. In fact, many trade analysts asserts that the anti-SDT argument is only valid in cases where preferences are targeted to specific activities. In cases where SDT general mechanisms are based on economic asymmetries between countries, the argument may not be valid. We subscribe to the latter position. Thus, within this context we support the SELA (1997) conclusion that, "*The incorporation of special treatment according to level of development within a general legal framework would in fact prevent modalities being applied that do distort competition*".

Finally, the importance of information in a competitive environment cannot be over emphasized. There is an urgent need for data capture and dissemination. Poor quality and/or lack of data are major limitations of regional studies, and affect the formulation of sensible policies. If CARICOM is ever to recognize its full potential, this problem must be resolved. Within this context, high priority must be accorded to trade data collection, processing, evaluation, and dissemination within CARICOM. Also, the CARICOM Secretariat, Caribbean Development Bank (CDB), and the Caribbean Regional Negotiating Machinery (CRNM) must assume central roles in this endeavor.

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Table 1. Selected Economic Indicators of Western Hemisphere Trading Arrangements, 2001.

Trade Bloc	Population	GDP[a]	GDP per Capita	Group of Countries
	Million	US Dollars		Number
NAFTA	338	7,557 billion	19,486	3
MERCUSOR	207	725 billion	3,507	4
G-3	153	403 billion	2,743	3
Andean Community	101	204 billion	2,017	5
CACM	31	32 billion	1,237	5
CARICOM[b]	6.5	22 billion	2,855	14
OECS	0.54	1.24 billion	2,134	7

[a] GDP data in nominal terms.
[b] Excluding data for Haiti. See footnote 3 of text for clarification.
Source: Caribbean Publishing Company (2002).

Table 2. Selected Indicators of CARICOM Production Structure, 1999[a].

County	GDP	GDP per Capita	GDP Growth Rate	Exports/ GDP Ratio	Imports/ GDP Ratio	Ag. Production/ GDP Ratio	Manufacturing/ GDP Ratio	Service/ GDP Ratio	Trade Balance	Inflation Rate
	US$Million	US$	Percent	Percent	Percent	Percent	Percent	Percent	US$Million	Percent
Antigua & Barbuda	653.70	9338.62	0.10	7.00	63.00	3.90	2.25	77.30	-371	5.20
Barbados	2490.00	9222.22	1.24	9.00	41.00	4.30	5.09	72.40	-775	3.43
Belize	732.50	2930.00	4.74	23.00	50.00	15.30	13.15	56.30	185	3.50
Dominica	264.59	3779.89	0.89	20.00	53.00	20.02	8.77	59.00	-80	2.30
Grenada	360.00	3600.00	5.32	8.00	51.00	8.37	7.14	69.30	-154	1.87
Guyana	679.44	790.04	3.00	77.00	81.00	35.57	9.80	36.40	-46	8.47
Jamaica	6680.64	2569.48	-0.53	17.00	39.00	8.00	15.00	62.20	-1570	8.23
St. Kitts & Nevis	300.65	7516.15	2.85	10.00	52.00	4.80	9.10	70.70	-126	1.82
St. Lucia	666.60	4444.00	3.55	11.00	51.00	8.36	5.75	72.80	-265	3.00
St. Vincent & The Grenadines	328.60	2987.2	2.54	15.00	61.00	10.86	6.86	63.80	-148	1.00

Grenadines		7								
Suriname	818.00	1995.1 2	-1.00	58.00	54.00	10.40	9.20	68.20	-45	180.12
Trinidad & Tobago	6869.48	5284.2 1	6.76	38.00	38.00	1.52	8.20	57.00	-377	5.15
Total	20844.20	2800.0 0								

[a] All values in nominal terms, except as noted.
Source: Caribbean Publishing Co. (2002); CGCED (1999); UNCTAD (2000); World Bank (2001).

Table 3. Selected Indicators of CARICOM Human Resources Levels, 1999.

Country	Population	Unemployment Rate	Poverty Rate in Population	Households with Piped Water[a]	Households with Flush Toilets[a]	Households with Electricity[a]
	Million	Percent	Percent	Percent	Percent	Percent
Antigua & Barbuda	0.07	7.00		61.80	52.90	89.10
Barbados	0.27	16.00		95.80	66.30	92.60
Belize	0.25	12.80	33.00	49.20	34.80	67.20
Dominica	0.07	20.00		50.20	36.80	79.20
Grenada	0.10	15.00	32.10	63.30	36.10	68.70
Guyana	0.86	12.00		60.80	29.50	71.60
Jamaica	2.60	16.00	34.20[b]	65.00	40.20	80.00
St. Kitts & Nevis	0.04	4.50		72.00	55.70	81.90
St. Lucia	0.15	15.00	25.10	62.60	35.70	72.90
St. Vincent & The Grenadines	0.11	22.00	37.50	53.80	33.20	66.80
Suriname	0.41	20.00				
Trinidad & Tobago	1.30	12.80	21.00	71.40	57.70	89.30

Total	6.23

[a] Data are for 1990, except stated otherwise.
[b] 1992 data.
Source: Caribbean Publishing (2002); CDB (2000); Kairi Consultants, Ltd. (1999, a, b).

Table 4. Selected Indicators of CARICOM Infrastructure Levels, 1999.

Country	Area	Total Highway Surface Area	Paved Highway Surface Area	Commercial Airports	Commercial Seaports	Radio Stations	Television Stations	Telephones Main Lines
	1,000 Sq Km	Miles	Miles	Number	Number	Number	Number	Number
Antigua & Barbuda	0.40	616.0	236.0	1	2	3	1	32,000
Barbados	0.30	1019.3	916.0	1	1	5	1	108,000
Belize	23.00	2365.0	212.0	2	3	13	2	31,000
Dominica	0.70	465.8	310.5	2	2	13	0	19,000
Grenada	0.30	700.0	360.0	2	5	3	4	26,804
Guyana	215.00	4754.0	341.0	1	1	6	3	70,000
Jamaica	11.00	11304.0	7826.0	2	12	23	7	353,000
St. Kitts & Nevis	0.30	186.0	78.5	2	2	4	1	17,000
St. Lucia	0.60	626.0	510.0	2	2	5	3	36,000
St. Vincent & The Grenadines	0.40	645.6	281.0	3	1	1	4	20,500
Suriname	163.00	2813.0	756.3	1	1	18	3	64,000

Trinidad & Tobago	5.00	4969.0	2485.0	2	5	14	4	243,000
Total	420.00	30463.7	14312.3	21	37	108	33	1,020,304

Source: Caribbean Publishing Co. (2002); CIA (2001).