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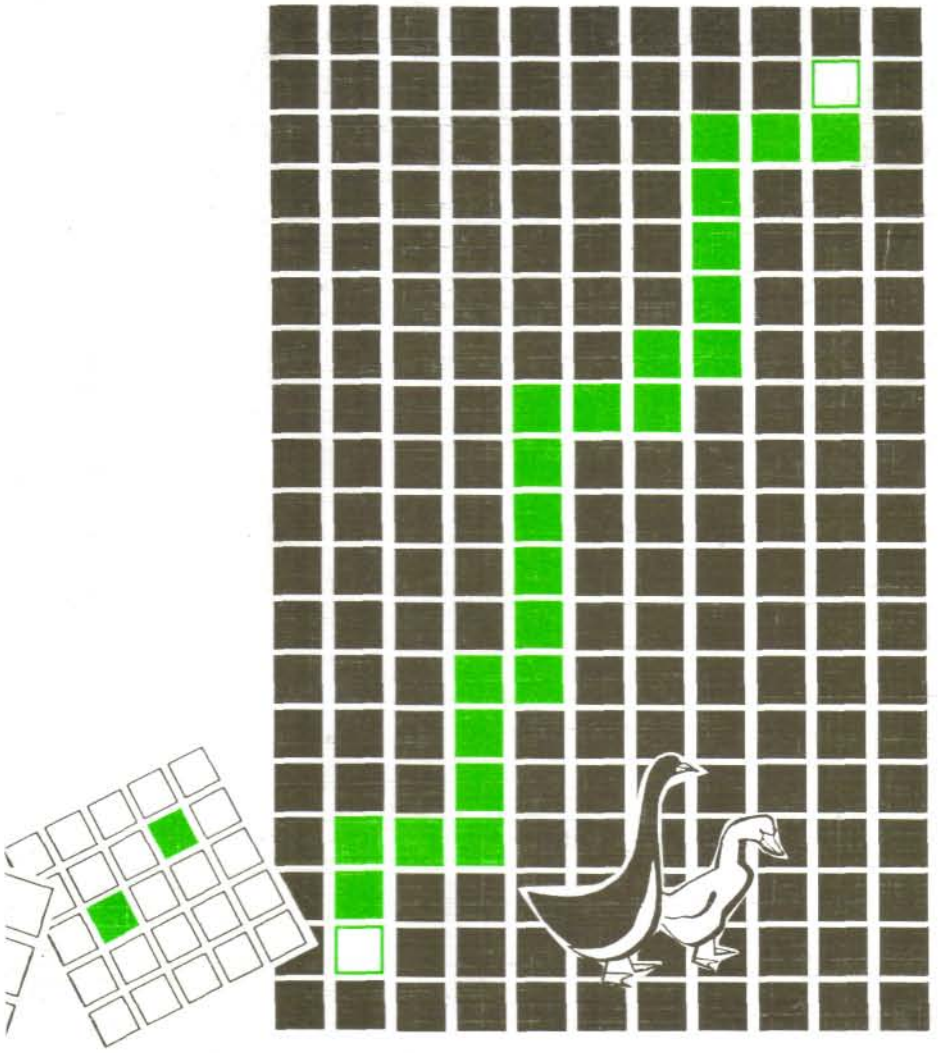

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Economic Asymmetries, Trade Liberalization and Regional Integration: Issues and Policy Implications for Caricom Countries

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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 assesses 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.

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INTRODUCTION

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 gives 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.

It is increasingly apparent that specialized 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 member countries. In an abstract sense, these are viewed as significant economic differences among countries, owing to disparities in levels of development (SELA, 1997). The most frequently mentioned dimensions relate to production structure, human resources training and infrastructure, from which comparisons are made using such indicators as Gross Domestic Product (GDP), GDP per capita, growth rates, and population. It is within this context that economic asymmetries function as serious impediments to equitable trade relations between countries (Briguglio, 1995; Bardouille, 2000).

Special and Differential Treatment (SDT) in the areas of trade, finance, and cooperation has been the generalized global response to problems associated with economic asymmetries. However, under the umbrella of the WTO trade regime, the principle and operational modality of reciprocity has taken center stage and has been 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.[2] Size in all of its

[2] *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. As at the time of writing, Haiti was formalizing arrangements to complete its full entry; it does not yet apply the trade policy. Haiti was granted full accession at the Heads of CARICOM meeting in Guyana on July 3-5, 2002. 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*

dimensions (economies of scale, economies of scope, geographical, etc.) is a key element of the aforementioned indicator dimensions, in that it affects the configuration of countries' production structure, infrastructure, and human resource quality (Bernal, 1994; Armstrong and Read, 1998; Davis et. al., 2001). The structural dimensions of the region have been 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). However. 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; hence the readiness of CARICOM must be assessed accordingly. Can the region effectively compete without preferential status? How must the regional policy agenda change in order to minimize adjustment costs and maximize gains? Certainly these are among the pertinent issues that must be addressed by trade liberalization protocols and regional integration schemes.

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 assesses 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 solution does 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 A ... lie in tackling it head-on and incorporating it definitively into the system of economic relations that is set up@ (p.16).

TRADE LIBERALIZATION AND ECONOMIC INTEGRATION: RELEVANT ISSUES

As conceptualized by Balassa (1961), economic integration is both state B where discriminatory polices are eliminated between economies, and a process B where measures are implemented to remove such elements. Product and factor market linkage via free trade areas, customs unions, and common markets[3], and policy consolidation between

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.

[3]Current literature uses liberalized trade and free trade synonymously. Strictly defined, free trade refers to trade without restrictions, whereas liberalized trade is a

nations are important dimensions of the process (Molle, 1997). The latter may include the formation of supranational entities to facilitate the harmonization of monetary, fiscal, and social policies. Trade liberalization refers to 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 both cases, the formation of economic linkages between member countries is crucial for the achievement of common goals.

The global economic landscape has undergone marked change in recent years. For example, trade flows are now determined not only according to classical comparative advantages, but also by scale and scope economies (IDB, 2000). Hence, more countries are pursuing globalization and trade liberalization through various multilateral arrangements and integration schemes, an approach commonly known as open regionalism (Gill, 1997; Davis et al., 2001). This mode of operation is particularly advantageous for developing countries, as they are better able to explore liberalization initiatives without compromising their developmental goals.

Subsequently, regional trade agreements (RTAs) have become quite popular in recent years; as of the year 2000, there were over two hundred in existence. According to the World Bank (2000), the reasons for regionalism are both political and economic in scope. Increased security, greater bargaining power due to 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 that evaluate increases in market size and scale efficiencies, and "trade location" effects that assess trade creation and diversion, and resource redistribution (World Bank, 2000). The overall motivation also appears to differ between developing and developed countries. For example, whereas developing nations tend to participate primarily for economic gain, for developing nations, it becomes an issue of economic survival (Bouzas and Ros, 1994).

Burfischer (1998) notes that 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,

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

(3) initial tariff rates. According to Burfischer, where these factors diverge considerably between countries, there is increased potential for considerable gains. This conclusion is consistent with the findings of Robinson and DeRosa (1995), whose evaluation of several RTAs indicated a greater likelihood for trade creation as opposed to trade diversion. However, as the authors carefully point out, positive effects were guaranteed only if countries desisted from erecting formal trade barriers for non-member countries (Burfisher, 1998; Robinson and DeRosa, 1995).

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 argues 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.[4] 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 issues relating to liberalization, economic

[4]*In trade, the indices are average tariffs and tariff spreads. In taxation, the indices include among other things, tax rates on companies and individuals. In the areas of finance, privatization and labor, the indices would include such items as freedom of interest rates on deposits, loans, reserve bank deposits, etc. (IDB, 1997; Ballayram, 2001).*

integration, and economic asymmetries are moving in lockstep with each other and as such, would be better addressed together within a policy framework.

It is now quite clear that effective participation in RTAs requires considerable flexibility, since individual economies must be able to rapidly adjust to changing business conditions and increased competition. Wherever such adjustments fail to occur, temporary socio-economic dislocation is likely until the appropriate response can be made. Although welfare economics theory generally assumes compensation of "losers" by the "winners", it is quite difficult to establish the necessary mechanisms to facilitate this; therefore some members are likely to benefit at the expense of others (Balassa, 1961). In a worst-case scenario, economic liberalization/ integration may actually widen the gap between trading partners, particularly if these mechanisms are lacking.

The proposed Free Trade Area of the Americas (FTAA) is expected to significantly advance liberalization and integration imperatives in the Western Hemisphere. Slated for 2005, it will comprise the largest trade bloc in the world, encompassing 34 countries with a total population of 750 million, and a combined gross domestic product (GDP) of nearly 9 trillion (World Bank, 2002). Its specific goals will include trade liberalization, elimination of investment restrictions, freer movement of specialized workers, tax and monetary policy harmonization, and the creation of a supra-regional institution with administrative oversight. These stated objectives have important implications for its members, since the implicit commitments clearly transcend traditional reciprocity between trading partners (Davis et al, 2001). Participants may derive substantial benefits from the agreement, but serious consideration must be given to the significant disparities in size and development among the 34 member states. These asymmetries cannot be neutral within the context of trade liberalization and integration – they will determine adjustment capabilities, competitiveness, and impact the respective economic performances of individual participants (SELA, 1997; Bryan and Bryan, 1999; Davis et al., 2001). It is clear that they must be explicitly recognized and treated by the emerging policy agenda, such that the overall effectiveness and integrity of the FTAA is maintained. It is also important that the FTAA not function as a vector for greater inequality between its members, but rather serve as an impetus for sustainable economic development for its most vulnerable members.

REGIONAL INTEGRATION

Overview

Economic integration in the Caribbean has always been driven by the need to overcome the challenges of development due to small size (Bryan and Bryan, 1999). CARICOM[5] was created by the Treaty of Chaguaramas signed in Trinidad on July 4, 1973, and founded primarily with the overall goal of promoting economic and social development for its member states. It currently comprises 14 countries, has a total population of about 6.5 million and a combined GDP of approximately

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

US$22 billion (Caribbean Publishing Co., 2002). Specific objectives include:

- To facilitate economic cooperation through the CARICOM Single Market and Economy (CSME), requiring free movement of goods, services, labor and capital between member states;
- To coordinate foreign policy among independent member states. This strengthens the region's external position by presenting a unified voice on matters of interest;
- To provide common services and cooperation in functional matters such as health, education and culture, communication and industrial relations (CARICOM Secretariat, 2002a).

Although CARICOM has performed reasonably well in the latter objectives, the common market is yet to be fully implemented. This can be directly attributed to legislative shortcomings in the original Treaty, which focussed primarily on creating a free trade area for goods and the Common External Tariff (CET), at the expense of the common market (Bryan and Bryan, 1999; Jessen-Rodriguez, 1999). The Treaty is currently being amended via nine protocols that outline specific rules/schedules for factor mobility and trade services liberalization, in order to facilitate a functional CSME and harmonize economic, fiscal and monetary policies across member states by 2004 (CARICOM Secretariat, 2002b).

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.

CARICOM faces myriad challenges as it seeks inclusion in an international economic framework that demonstrates minimal concern or tolerance for the special needs of small developing economies. Whereas small size, resource endowment, and other developmental disparities were sufficient reasons for special treatment in the past, the discretionary status of SDT lessens the likelihood that they would even matter in future arrangements. Although the WTO does recognize and advocate special treatment for developing economies in general, it makes no distinction for small developing economies as a sub-set.

Concomitant to such developments, the future of SDT for the Caribbean is contingent upon the political landscape of the European Union (EU). As the Union expands to include nations that lack historical ties to the region, its development cooperation policies are being rapidly redefined. Financial aid and preferential treatment are now conferred according to urgent development needs – not merely on geopolitical grounds or colonial legacies (Bryan, 1997). Indeed, when compared to destitute nations in Sub-Saharan Africa and Eastern Europe, it appears that CARICOM's relatively stable economic performance and social development has led to the perception that SDT is unwarranted.

Consequently, 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. The definite shift toward reciprocity in trade relations is indicative of an emerging economic system where market forces are shaped by efficiency, competition, and private enterprise – it is unlikely that preferences will matter significantly in this scheme. Therefore, 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.

Intra-CARICOM Symmetries and Asymmetries:

The structural characteristics of CARICOM member states are quite unlike those of other groups in the Americas, and provide compelling evidence of the need for special consideration. Even within the region itself, major differences in size and levels of development are obvious, as shown in Tables 1, 2 and 3. CARICOM economies are extremely vulnerable to external economic shocks, and exhibit high degrees of openness. Service activities dominate local and regional GDP, and typically contribute 50% or more in this regard (Davis et al., 2001). Agriculture and manufacturing are also important activities, although their relative contributions have declined in recent years. The overall importance of agriculture is not to be underestimated however, since primary commodity exports do comprise a large portion of total regional merchandise exports. As a major foreign exchange earner and employer, it wields considerable influence on the socio-economic health of the region (Davis et al., 2001).

CARICOM countries exhibit the following characteristics:

- *Small Open Economies:* A ranking of FTAA participants by Davis et al. (2001) emphasizes the vulnerability of CARICOM vis-à-vis other hemispheric groups: it comprises less than one percent of the total market, whether in terms of GDP (0.2%), landmass (0.67%), or population (0.82%). Product diversification is difficult given the limited resource base, and the small market prevents the exploitation of economies of scale and scope. Trade is an important activity, as reflected in the high trade/GDP ratios for individual countries and the region. For example, based on 1997 data, Jessen and Rodriguez (1999) estimated a ratio of 116% for CARICOM, which far exceeds that (74.7%) of the Central American Common Market (CACM). Member states are also heavily reliant on foreign exchange earnings from services and merchandise exports, and trade taxes are a major source of government revenue. The latter can amount to 50% or more in some states (Bernal, 2000).
- *Export Concentration in Few Markets:* Export diversification has been minimal due to the limited resource base and production options. Preferential schemes have also exerted tremendous influence in this regard; indeed, member states have been 'locked' into the production of certain products as a consequence of colonial

history. Merchandise exports are dominated by primary commodities, which have commanded sluggish prices on international markets in recent years. This is indeed interesting, since one can conclude that the regional economy would have been adversely affected without SDT. The perils of a narrow export base are further exemplified by the Windward Islands banana sector: having depended on the EU market for 80-90 percent of its exports, an unfavorable WTO ruling resulted in major problems in those economies.

- *Reliance on Special and Differential Treatment (SDT) and Capital Concessions:* For historical reasons, CARICOM nations have enjoyed privileged access to North American and European markets[6] and concessionary financial arrangements. That these have benefited the region is not a source of contention, but as discussed previously, the tremendous influence on the size/pattern of regional exports has done little to support export diversification.
- *Imperfect Competition Diseconomies:* Exploitation of scale economies is difficult given the small market size and firms. Moreover, the high costs associated with transport, utilities and financial services hinder regional and foreign investment. Markets are dominated by monopolies, and pricing inefficiencies are common – the transportation and telecommunications sectors are typical examples. Given CARICOM's high trade dependency, it would be wise to correct these particular shortcomings as soon as possible, so as to improve regional competitiveness.
- *Low Administrative Capacity:* This is manifested in an overall inability to implement policies in a timely fashion, primarily as a result of skill inadequacies. Hopefully, this problem would be effectively addressed by the CSME. - Comparative Economic Performance.

The prospect of reciprocity and its ramifications for CARICOM appear particularly ominous when comparisons are made with other integration schemes in the Western Hemisphere, namely the Andean Community, CACM, MERCOSUR, and NAFTA[7].

Much like CARICOM, these groups have vigorously embraced trade liberalization imperatives via open regionalism, despite having many economic setbacks over the years. The indicators (IDB, 2000) listed in Table 4 provide tangible evidence of inter-group disparities. Size and population notwithstanding, CARICOM consistently ranks lowest in the major indicators (real GDP, growth rates).

A similar trend is noted for extra-regional merchandise trade growth over the same period. The CACM and MERCOSUR were the best performers at 12% and 9.2%, respectively, followed by NAFTA (7%), the Andean Community (6.3%), and CARICOM (6.2%).It is worthwhile to point out that CARICOM's performance was only slightly below that of the Western Hemisphere (6.9%), and the World (6.6%). No doubt, differences in

[6] The US, EU and Canadian markets absorb 36%, 21% and 6% respectively, of CARICOM's total sales abroad. Duty free access is granted in all markets in varying degrees (Source: Jessen & Rodriguez, 1999).

[7] See Appendix for country listings.

market structure and trade preferences are among the key determinants of these trends.

CARICOM performs better in terms of real GDP per capita, but given that this is merely a function of size, inferences of relative prosperity are misleading. As Bryan and Bryan (1999), and Jessen and Rodriguez (1999) rightfully point out, this indicator neither captures true economic strength, nor the sustainability of income levels over time, but rather obscures major disparities in socio-economic development between countries.

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

Historical Approaches to Asymmetries

As discussed previously, the traditional approach to dealing with issues of economic asymmetries has been via the principle and practice of Special and Differential Treatment (SDT). Despite the tendency to confine it to 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 used in hemisphere trade and integration arrangements since the early 1960s. CARICOM is included among 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.[8]

According to SELA (1997), 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; (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.

As we alluded to earlier, SDT has not been revoked or abandoned by the WTO. 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

[8] *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.*

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). As noted by Davis et al. (2001), the fundamental mechanisms of the proposed FTAA go beyond traditional reciprocity concept among trading partners. If the concept receives sanction by the WTO, it 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 differentiate between conditions giving rise to SDT and the performance outcomes of SDT. As SELA (1997) rightfully argues, 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, and is thus a classification category that sets them apart. Preferential treatment 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). Developing nations have therefore been exempt from the fundamental principles of the WTO/GATT system[9]. Naturally, a two-tiered system has evolved over time between contracting parties: the first tier requires full compliance with WTO stipulations and applies to developed nations only, whereas the second tier allows SDT for developing countries. Examples of these arrangements in the Western Hemisphere were provided earlier.

SDT is often challenged on the basis that it has not produced the intended outcomes. According to the OECD (1992) and Michalopoulos (2000) it appears that recipients have been disadvantaged in several areas. First, the 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, vis-à-vis those of developed nations. Second, it appears that preferential treatment has encouraged rent seeking,[10] resource misallocation, and stagnant productivity in some respects. These cases have lent support to WTO mandates that explicitly forbid preferential treatment in international trade, except as provided under its exemption and special waiver clause.

[9]These principles are reciprocity, transparency, national treatment, most-favored nation (MFN) status, nondiscriminatory and predictability through binding of negotiated concessions.

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

However, SELA (1997) challenges this notion by arguing that in the case of Latin America and the Caribbean, the lack of results obtained through SDT have been due to the development difficulties of recipient countries and the weaknesses of the integration schemes, rather than to the characteristics of the mechanisms adopted. A deeper understanding of these problems is therefore in order before the international community can dismiss SDT as an ineffectual policy.

POLICY IMPLICATIONS

Intra-Group Strategy Implications

Much of the support in the economic literature for trade liberalization is based on conventional trade theory[11], which assumes (1) a perfectly competitive business environment, and (2) comparative advantages due to resource/technological endowment. Within this theoretical construct, smaller countries are supposed to benefit disproportionately from liberalized trade with larger countries. The premise of this argument is that the larger countries domestic price structure will dominate in the determination of world prices, thus the structure of incentive that prevails will remain unaltered. Conversely, the altered price structure experienced by smaller countries will efficiently reallocate production/consumption patterns, such that trade gains increase.

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). However, McIntyre and Gonzales (2000) point 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, "*A. ...this provides a strong rationale for the implementation of transitional policies to mitigate the cost of adjustment.* "

As the evidence clearly indicates, economic asymmetries are indicative of underlying inequalities in resource endowment and institutional capabilities among countries. Their effects are two-fold: (1) they blunt potential positive gains from reciprocity-based liberalized trade, and (2) they inevitably increase the severity and costs of the adjustment process arising from trade reform initiatives. As Bernal[12] succinctly states, small size does not necessarily imply an inherent economic disadvantage for CARICOM, but it does constrain the range of policy options and resource availability – particularly when coupled with lower levels of development. The WTO/FTAA machinery must therefore demonstrate greater understanding of this problem, whether through the provision of specialized policies or by legally sanctioning temporary SDT. Immediate, universal application of reciprocity will not engender fair and equal trade relations, but only exacerbate existing asymmetries.

If successful strategies are to be mounted against these challenges, regional leaders

[11] *Ricardian and Heckscher-Olin-Samuelson theories*

[12] *See Bryan and Bryan, 1999.*

must commit fully to regional integration. Although the sovereignty of individual member states is important, it must not be used as a platform for micro-nationalism; otherwise the integrity of CARICOM as an integration mechanism will be seriously undermined. Dookeran (1995), who argues that political division within CARICOM -not economic weakness - is the main contributor to regional vulnerability, raises this point.

The regional implications of reciprocal trade within the FTAA and WTO are widely debated in many studies (Harker et al., 1996; Yamazaki, 1996; Bryan, 1997; Jessen and Rodriguez, 1999; McIntyre and Gonzales, 2000; Davis et al., 2001; Girvan, 2002). Empirical analyses by McIntyre and Gonzales (2000) and Yamazaki (1996) allude to the possibility of economic instability in the region over the short-run, following the removal of SDT. In his study, Yamazaki found that the aggregate losses for developing countries could total US$632 million (1992 dollars) due to preference erosion in the US, EU and Japanese markets. Central America and the Caribbean were projected to lose US$58 million B approximately 19% of their total pre-WTO benefits from the US and EU markets. Despite the temptation to disregard these impacts as minor, the overall economic significance cannot be disregarded given the high dependency of the Caribbean economies on preferential agreements.

Meaningful participation in the WTO/FTAA regimes will first require a complementary economic and social environment within CARICOM. In recognition of the region's overall unpreparedness, leaders must negotiate and secure transitional arrangements and technical assistance to mitigate the costs of adjustment, while undertaking the necessary steps to improve global competitiveness.

Trade reform is of paramount importance, and should target trade promotion, foreign market creation and market penetration. Barclay et al. (2001) give explicit direction in this regard by stating: "*A. ...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.*"

This implies that new production possibilities and niche markets must be vigorously explored. For example, an inter-island production / marketing approach could be considered where each member performs a specific role in the production process. Not only could this prevent direct competition between member states, but it may also improve product quality, if properly executed. In an analysis of policy imperatives, Bernal (1994) points to the need for reorientation of exports toward the services sector. Sustainable success of any trade reform however, rests on the overall competitiveness of the region.

Concerted efforts should be made to harmonize macroeconomic policies between member states, such that resource allocation could be made more efficient. Member states should further modernize and liberalize their investment regimes, so as to (1) improve export performance, particularly in the service

sectors, and (2) foster a competitive environment for regional and foreign direct investment (FDI). The business environment must operate within international standards – thus the convergence of regional regulatory frameworks to meet these standards would be worthwhile. Reforms will also be necessary in the telecommunications and transport sectors to improve overall market efficiency.

Effective policy coordination and execution is inextricably linked to the strength and efficiency of CARICOM's institutions. Hence, their core objectives should seek to (a) maximize the allocation of scarce human resources, (b) strengthen capacity for policy formulation, and (c) promote efficient functioning of markets. Education/human resource training and research and development (R&D) activities must be improved, particularly in the areas of technology and finance, in order to satisfy labor market demands as they evolve. Likewise, data collection and management must be improved to complement research activities across the region. Jessen and Rodriguez (1999) suggested that this be an area of regional cooperation, i.e. the development of efficient regional information stems and data management. The CARICOM Secretariat, Caribbean Development Bank (CDB) and the Caribbean Regional Negotiating Machinery (CRNM) should assume central roles in this endeavor.

CARICOM should continue to build strategic alliances with other integration groups, in order to enhance its bargaining position within the WTO and FTAA, and strengthen its negotiating capabilities. The CARICOM-CACM alliance is a recent example of this. However possible, stronger efforts must be made to deepen and widen the integration process, since it would tremendously increase the resource base and market opportunities, and fortify the political clout of the region.

Inter-Group Strategy Implications

As the breadth and scope of this issue will surely tax the resources of CARICOM, certain changes must also be made at the international or inter-group levels[13] to assist in the successful transition to reciprocal trade. According to Bernal (2000), the specialized circumstances of small economies will require multifaceted provisions and short-term preferential treatment along the following lines:

- *Lower Levels of Obligations*: CARICOM should only be required to undertake/implement concessions and commitments that are commensurate with its 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. Temporary exemptions in investment and domestic support may be required.
- *Asymmetrically Phased Implementation Timetables:* Existing developmental

[13] *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.*

disparities between CARICOM and other countries necessitate different adjustment periods and application of the rules and disciplines.

- *Best Endeavor Commitments:* It would be helpful if the international community were to adopt specific measures aimed at providing temporary easement. For example, special consideration could be given prior to the imposition of duties, and other forms of taxation policies 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:* In its current state, CARICOM has limited institutional expertise and economic capabilities to utilize the Dispute Settlement mechanisms of the WTO, as shown in the recent EU banana dispute. Technical assistance is urgently needed in this area.
- *Technical Assistance and Training:* Schemes proposed by the international community must complement the adjustment process, and promote capacity building. Moreover, assistance with WTO and FTAA negotiations could facilitate timely implementation of the various rules.

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" B 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.

We are aware that the conventional counter-argument given to SDT is that they intrinsically distort competition in trade relations. Economists and trade analysts however, do not universally embrace this assertion. 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. Thus, within this context we support the SELA (1997) conclusion that,

"*A. 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*". Stated differently according to Girvan (2002, p9), "*...in the absence of special remedial measures the equal treatment of unequals is almost certain to accentuate inequality.*"

The CARICOM leadership can ill afford to ignore the realities and the implications of globalization and trade liberalization. Without SDT, social and economic costs are inevitable; however, the dynamics of the international economy are such that an effective regional response must be mounted to mitigate these costs, and to improve global competitiveness. Clearly, economic isolation is not an option -- given the openness of the regional economy, the adverse effects would far outweigh any immediate and short-term costs associated with adjustment.

Finally, from all indications, CARICOM should proceed with deepening regional integration to capitalize on the gains of liberalized trade. The CSME is a step in this direction, but time 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 could threaten the very existence of the group. Also, CARICOM's limited resource base, in combination with the narrow transitional period granted by the WTO, dictates that the best policies must be rapidly identified, combined and sequenced such that the best performance outcomes are achieved.

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Table 1. Selected Indicators of CARICOM Production Structure, 1999[a]

County	GDP	GDP per Capita	GDP Growth Rate	Exports /GDP Ratio	Imports /GDP Ratio	Ag. Prod./ GDP Ratio	Manufac-turing/ GDP Ratio	Service /GDP Ratio	Trade Balance	Inflation Rate
	(US$ Million)	*(US$)*			*(Percen)t*				*(US$ Million)*	*(Percen) t*
Antigua & Barbuda		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 Grena-dines	328.60	2987.27	2.54	15.00	61.00	10.86	6.86	63.80	-148	1.00
Suriname	818.00	1995.12	-1.00	58.00	54.00	10.40	9.20	68.20	-45	180.12
Trinidad & Tobago	6869.48	5284.21	6.76	38.00	38.00	1.52	8.20	57.00	-377	5.15
TOTAL	20844.2	2800.00								

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

Table 2. Selected Social Indicators of CARICOM

Country	Population	Unemployment Rate	Poverty Rate in Population	Households with Piped Water[a]	Households with Flush Toilets[a]	Households with Electricity[a]
	(Million)			*(Percent)*		
Antigua & Barbuda	0.07	7.00	---	61.80	52.90	89.10
Barbados	0.27	16.00	13.90[b]	95.80	66.30	92.60
Belize	0.25	12.80	33.00[c]	49.20	34.80	67.20
Dominica	0.07	20.00	---	50.20	36.80	79.20
Grenada	0.10	15.00	32.10[d]	63.30	36.10	68.70
Guyana	0.86	12.00	43.20[c]	60.80	29.50	71.60
Jamaica	2.60	16.00	26.10[c]	65.00	40.20	80.00
St. Kitts & Nevis	0.04	4.50	31.25[a]	72.00	55.70	81.90
St. Lucia	0.15	15.00	25.10[c]	62.60	35.70	72.90
St. Vincent & The Grenadines	0.11	22.00	37.50[c]	53.80	33.20	66.80
Suriname	0.41	20.00	---	---	---	---
Trinidad & Tobago	1.30	12.80	21.20	71.40	57.70	89.30
TOTAL	6.23	---	--	---	---	---

[a] Data are for 1990.
[b] 1997 data; [c] 1996 data; [d] 1998 data; [e] 2000 data; (---) data not available.
Source: Caribbean Publishing (2002); CDB (2000); Kairi Consultants, Ltd. (1999, a, b); CDB (2002).

Table 3. Selected Indicators of CARICOM Infrastructure Levels, 1999.

Country	Area	Total Highway Surface Area	Paved Highway Surface Area	Commercial Airports	Commercial Seaports	Radio Stations	TV Stations	Tel Main Lines
	('000 sq. km)	(Miles)			(Number)			('000)
Antigua & Barbuda	0.40	616.0	236.0	1	2	3	1	32
Barbados	0.30	1019.3	916.0	1	1	5	1	108
Belize	23.00	2365.0	212.0	2	3	13	2	31
Dominica	0.70	465.8	310.5	2	2	13	0	19
Grenada	0.30	700.0	360.0	2	5	3	4	26.8
Guyana	215.00	4754.0	341.0	1	1	6	3	70
Jamaica	11.00	11304.0	7826.0	2	12	23	7	353
St. Kitts & Nevis	0.30	186.0	78.5	2	2	4	1	17
St. Lucia	0.60	626.0	510.0	2	2	5	3	36
St. Vincent & The Grenadines	0.40	645.6	281.0	3	1	1	4	20.5
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	1,020.3

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

Table 4. Selected Economic Indicators of Western Hemisphere Trading Arrangements, 2001.

Trade Bloc	Population	GDP[a]	GDP per Capita	Trade[b] Growth in US($)	Real GDP[c] Growth Rates	Group of Countries
	(Million)	*(US$ billion)*	*(US$)*	*(%)*		*(Numbe)r*
NAFTA	338	7,557	19,486	7.00	3.00	3
MERCUSOR	207	725	3,507	9.20	2.38	4
G3	153	403	2,743	-	-	3
Andean Community	101	204	2,017	6.30	2.99	5
CACM	31	32	1,237	12.00	4.33	5
CARICOM[d]	6.5	22	2,855	6.20	1.86	14
OECS	0.54	1.24	2,134	-	-	7

[a] GDP data in nominal terms.
[b] Merchandise extra-regional trade, average annual growth rates 1990-1999 ; (---) data not available (IDB, 2000).
[c] Average for 1990-99 period ; (---) data not available (IDB, 2000).
[d] Excluding data for Haiti. See footnote 3 of text for clarification.
Source: Caribbean Publishing Company (2002).

Table 5. Membership in Western Hemisphere Integration Groups

ACS	25 members include all Caricom (except Montserrat), CACM, and G-3 members, Cuba, the Dominican Republic, and Panama
ALADI	Includes Andean Community and Mercosur members, Chile, Cuba and Mexico
Andean Community	Bolivia, Columbia, Ecuador, Peru, Venezuela
CA-4	Guatemala, El Salvador, Nicaragua, Honduras
CACM	Costa Rica, El Salvador, Guatemala, Nicaragua, Honduras
CARICOM	Antigua and Barbuda, The Bahamas, Barbados, Belize, Dominica, Grenada, Guyana, Haiti, Jamaica, Montserrat, St. Kitts and Nevis, St. Lucia, Suriname, St. Vincent and the Grenadines, Trinidad and Tobago
G-3	Columbia, Mexico, Venezuela
MERCOSUR	Argentina, Brazil, Paraguay, Uruguay
NAFTA	Canada, Mexico, United States