THE GLOBAL FINANCIAL AND ECONOMIC CRISIS

Elements of a Strategic Response by the Caribbean

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Introduction

The current global financial crisis, which has blossomed into a full-fledged economic crisis, has had a far-reaching impact not only on the developed countries but also on the developing countries, including those in the Caribbean which will be the main focus of this paper.

There is general consensus that the crisis, which originated in the US, was caused by a combination of several factors, the most notable being the sub-prime mortgage debacle, the development of complicated financial instruments which multiplied risk and which therefore had unforeseen systemic implications, and excessive reliance on market forces with a correspondingly lax regulatory framework. In addition, some have argued that the crisis was underpinned by a deep-seated structural imbalance between savings and investment in the global economy which was reflected in growing inequalities between the developed and developing countries in the context of an unrelenting process of globalisation. These developments in turn led to a precipitate decline in the stock market, the freezing of credit, a steep decline in production in a number of key sectors, with a consequential adverse impact on employment, severe trade contraction and significant reduction in GDP growth. Indeed, the IMF and the World Bank have both projected only modest growth in the global economy into 2010.

In analysing the crisis it is important to focus not only on its origin and impact, as described above, but more importantly, on the elements of a strategic response to deal with the crisis in a proactive manner, given the particular circumstances of the Caribbean.

Specific Implications of the Financial Crisis for the Caribbean

In the case of the Caribbean, the crisis has had an adverse impact on a number of sectors, including tourism, as evidenced by lay offs in the hotel industry in the Bahamas and elsewhere, due to a fall off in tourist arrivals, falling demand for bauxite/alumina which has also resulted in job losses at Alumina Partners (ALPART) in Jamaica and at Rusal Bauxite Company in Guyana. Even in those cases where tourist arrivals have suffered a relatively modest decline, this has been achieved on the basis of a significant discount in hotel room rates which will therefore have a negative impact on the foreign exchange earnings of the sector. In addition, the region is likely to be impacted negatively by a decline in remittances as a result of financial uncertainty and job losses among the Caribbean immigrant communities in North America and the UK which have been the main sources of such remittances. The situation has been further complicated by the SEC investigation into the Stanford operations which forced the take over by a consortium of Eastern Caribbean banks of the Stanford holdings in the Bank of Antigua. The recent CLICO ‘crisis’, which forced the Central Bank of Trinidad and Tobago to provide financial support to bolster the liquidity position of the company has reverberated throughout the Caribbean since CLICO has
operations in many countries in the region. It is likely that as a result of the crisis, the region will also experience a reduction in foreign investment and, possibly, foreign aid, which will slow the expansion of the productive sectors and also affect infrastructural development. In sum, the decline in the productive sectors, the contraction in trade, the fall-off in remittances, declining investment and aid, and continuing financial instability and uncertainty are likely to generate increased unemployment and even increase the incidence of poverty in the Caribbean unless urgent and creative measures are adopted to deal with the situation.

**Elements of a Strategic Response**

In seeking to respond to the crisis, it is important to distinguish between the short-to-medium term and the longer term aspects of a strategic response. There is, of course, considerable uncertainty and differences of opinion regarding the likely duration of the crisis. Some believe it will involve a steep decline followed by a sharp upward swing, once the various stimulus packages put in place by the US and other countries take effect. Others feel that it is a steep decline followed by a long trough before the global economy begins to recover. Yet others, adopting a more pessimistic view, see the crisis as a steep decline followed by a long period of recession before global economic prosperity returns. Given the diversity in the assessment of the duration of the crisis, the region will need to identify a number of short to medium-term as well as a long-term measures, with a built in flexibility to move on both fronts simultaneously, instead of becoming fixated on short-term approaches, notwithstanding the need to respond in some cases with an appropriate sense of urgency to address pressing problems.

Similarly, the policy response will need to distinguish between action to be taken at the national level and that at the regional level. While action at the national level is unavoidable and necessary, it is felt that in the context of current efforts aimed at increased regional economic integration within the framework of the Caribbean Single Market and Economy (CSME), special emphasis should be placed on regional initiatives since increased coordination of effort is required at this level in order to avoid duplication of effort or even the pursuit of contradictory initiatives. Indeed, the individual members of the Caribbean Community will need to resist the temptation to pursue protectionist policies and avoid arbitrary national action which is inconsistent with the provisions of the Revised Treaty of Chaguaramas. In recognition of this need the Caricom Council for Finance and Planning (COFAP) has appointed a Task Force to examine the implications of the financial crisis and to make appropriate recommendations that will enable the region to respond effectively to the crisis. It is important to note that the membership of the Task Force includes representatives from government, the private sector and the labour movement and therefore fully embraces ILO’s constituencies.
• **Action at the National Level**

A primary requirement at the national level is the adoption by government, in consultation with its social partners, of a policy aimed at ensuring financial stability, stimulating productive sector activities with special emphasis on employment generation and to guarantee social welfare objectives. Already governments in the region have begun to adopt measures designed to respond to the challenge presented by the crisis. In Jamaica, the government has resorted to external borrowing through the IDB and the CDB to fund high priority projects aimed, among other things, at the strengthening of financial management, controlling debt and streamlining revenue systems and has also pursued a high interest rate policy to stabilise the exchange rate and prevent a depletion of its foreign reserves. Some have pointed out that high interest rates serve as a disincentive to investment in the productive sector. This is a potential contradiction that will need to be resolved on the basis of a creative policy compromise. In addition the government has committed itself to maintain budgetary allocations to health and education and to provide continued support to social programmes such as PATH in order to cater to the needs of the poorer segments of the society. In recognition of the importance of tourism, Barbados has provided emergency support to the hotel industry. The Bahamas has also provided support to the industry and has increased investment in construction in an effort to generate employment. For its part, Belize has launched a stimulus package in order to expand output and generate employment. The member states of the Organisation of Eastern Caribbean States (OECS) have adopted measures to shore up the tourist industry and stem unemployment. They have also sought to ensure the viability of the financial services sector which is now a major prop of the economies of that sub-region. In the face of the re-emergence of the OECD attack upon so-called ‘tax havens’ it will be important for the OECS countries to mount a joint effort with the other members of CARICOM in defence of their interests in this important area. In addition, the OECS governments have agreed to revisit their earlier poverty assessments in order to identify the specific vulnerable groups impacted by the crisis and, on this basis, to fashion a suitable ‘social safety net’ programme. However, as was stated earlier, action at the national level will need to be supplemented by initiatives at the regional level if the Caribbean is to develop an effective strategy to respond to the crisis.

• **Action at the Regional Level**

Apart from the benefits to be derived from increased cooperation among the member states of the Caribbean Community, the crisis provides a useful opportunity to pursue a number of creative initiatives at the regional level. Given the need for increased prudential oversight of the financial sector, the region will need to establish a suitable Regional Regulatory Mechanism in order to adopt a common approach in the effort to ensure more effective regulation of the economy. The Caricom Heads of Government have
recently agreed to establish a system of coordination among national regulatory agencies. But this must be seen as a first step rather than a final goal in regional cooperation. In addition, the region should revisit the establishment of a Regional Stabilisation Fund, or a Regional Mitigation Fund, as some have termed it, as a mechanism for providing financial support to countries in need of such support, especially in a time of crisis, such as is the current reality. It should be noted that in Asia, the Chiang Mai Initiative (CMI) which was established in the wake of the East Asian financial crisis is designed to serve a similar purpose.

More important still, the Caricom countries should seek to intensify the process of economic integration by embarking on a systematic strategy of production integration based on the joint utilisation of the resources of the region – which are not insignificant. This will require a new approach to regional investment which is premised on increased cross-border inter-sectoral and intra-sectoral integration as a means of optimising the development possibilities of the region. In other words, the lesson to be drawn from the crisis is the need to intensify regional cooperation and economic integration and not to delay the process further, as some countries might be inclined to do. Of course, the promotion of closer economic integration will require the adoption of creative and pragmatic governance arrangements at the regional level in order to manage more effectively the integration process.

While seeking to accelerate the pace of regional integration, the Caribbean should also intensify its efforts to explore options for the diversification of its external trade and investment possibilities. While maintaining traditional economic links with North America and Europe, based on historical imperatives, the region will need to strengthen economic and trading links with countries such as China, India and Brazil in view of their increasing importance in the global economic system, bearing in mind the fact that by the middle of this century, China is projected to surpass the US as the largest economy in the world, measured in terms of GDP, while India will be the third largest after the US, with Brazil also emerging as a global economic power. In fact, a new ‘geography’ of trade and investment is emerging in the global economy, based on the spectacular growth achieved in some developing regions, notably Asia, which has accumulated significant reserves.

Equally important, the Caribbean will need to add its voice to the demand for the restructuring of the international financial architecture in order to provide more effective oversight over the global economy and thus ensure greater financial stability. It has also become quite clear that the global economy in the age of globalisation cannot be managed by a small group of developed countries meeting in the G8, as has been the practice until now. Indeed, there is growing recognition of this fact, as is evidenced by new initiatives to involve a wider range of countries in the form of the G20 which met at ministerial level in London recently, as a prelude to a Summit Level meeting of the Group to be held in London in April, 2009. Both Prime Minister Gordon Brown of the UK and Mexican President Felipe Calderon have in fact called for a revamping of the international financial system with an emphasis on its further democratisation in order to give a more effective voice to the developing countries, including those in the Caribbean, in the decision-making process.
Finally, given the effective discrediting of an unfettered neo-liberalism based on market fundamentalism, the region will need to revisit the theoretical foundations of current economic policy in order to arrive at an alternative or, perhaps more appropriately, a modified economic paradigm that is premised on the need for a more effective regulatory framework in order to provide continuing oversight over the operation of the market. Already a number of analysts have begun to call for a more ‘managed capitalism’ while others have advanced to concept of an ‘egalitarian capitalism’ that is more responsive to social needs. Concepts such as structural Keynesianism, which seems to be currently practised in the US in response to the crisis, have gained increased currency in the emerging literature on economics as a counter to the dogmatism associated with market fundamentalism.

**A Socially-Responsive Macroeconomic Policy Framework**

While the measures identified above are relevant and necessary to promote financial and economic stability, they are not sufficient in themselves to deal with the full effects of the crisis which has a large social dimension. In order to ensure social justice and societal stability, in a climate of crisis, it will be necessary to formulate a creative macroeconomic policy as a basis for promoting financial viability, optimising output and pursuing targetted interventions in an effort to alleviate the situation of the poor and other vulnerable groups in the society.

There is, of course, a large literature dealing with social justice and equity in the realm of public policy. John Rawls, for example, in his famous books entitled ‘A Theory of Justice’ and ‘Political Liberalism’, equates justice with fairness in assessing public policy outcomes. On the other hand, conservative theorists, such as Robert Nozick, argue against this philosophical position and emphasise instead the primacy of individual rights based on an ‘entitlement theory’ as the true test of the effectiveness of public policy.

This ideological divide is reflected in the fact that protagonists on the ‘left’ generally advocate a public policy aimed at improving the situation of the poor through a more equitable distribution of the resources of the society and therefore support increased transfer payments in the form of social security and other similar benefits. In contrast to this position, protagonists on the ‘right’ tend to apply a conservative logic to public policy which emphasises the need to impose limits on government expenditure relating to social welfare benefits. In addition, they advocate a reduction in personal and corporate income tax as well as inheritance taxes which they argue would be beneficial to the society since it would put increased resources in the hands of the wealthy which would then be invested in the productive sectors and thereby generate employment and increased income. However, as is evident in the debates taking place in the US and in many other parts of the developed world, the current crisis has raised serious questions regarding the validity of the latter thesis.
In the past, there has been, to some extent, a disconnect between the perceived imperatives of economic policy per se and the satisfaction of social needs, as was evident in the initial economic liberalisation and structural adjustment programmes sponsored by the IMF and the World Bank during the 1980s. Under these programmes, the need to rein in public sector deficits, which was seen as important objectives of economic policy, often led to major cut-backs in social sector expenditures, notably in education and health with resulting hardship on the lower socio-economic groups in the society. However, in recent years other UN organisations such as ILO, UNDP and UNICEF have advocated more human-centred development strategies which put the satisfaction of human needs at the forefront of public policy and have therefore made an enlightened contribution to the debate on development. It is not surprising that the Millennium Development Goals (MDGs) adopted by the UN General Assembly are based largely on social sector development objectives.

A socially responsive macroeconomic policy should therefore seek to reconcile the logic of economics with the primacy of human needs. As such, it should combine a progressive monetary and fiscal approach with interventions designed to alleviate poverty and address the needs of the most vulnerable social groups, such as women, children and the disabled. A prime requirement would be the reform of the tax system in order to provide tax relief for the poorer segments of the society. In addition, it should provide a stimulus for investment in critical productive sectors, with special reference to the needs of small enterprises, in an effort to generate employment and prevent wage depletion. Investment in infrastructure should also be emphasised not only in terms of its economic benefits but also its employment generation potential. In order to complement these measures, emphasis should also be placed on the funding of suitable public assistance programmes, such as food stamp distribution, in order to enable recipients to purchase a basic nutritious food basket. Finally, Caricom governments should seriously consider the possibility of providing unemployment benefits, more particularly so during periods of economic crisis, as is currently the case.

In recent years a number of innovative approaches have been identified in the context of a pro-poor and human-centred development strategy designed to ensure the empowerment of people and communities. In this context, increased emphasis has been placed on working with communities with a view to enabling them to pursue a sustainable livelihood that takes account of the requirements for economic survival as well as environmental preservation. At this time of crisis, special emphasis should be placed on the promotion of creative grassroots initiatives geared to employment generation.

It will, of course, not always be easy to arrive at an optimal level of economic and social adjustment in the context of the impact of the crisis. A decision to maintain the current level of budgetary allocation to education and health, for example, would probably require cuts in other sectors which would in turn have a negative impact on those sectors. A decision will therefore need to be made regarding the relative priority to be assigned to the activities carried out in various sectors which could be determined based on criteria such as their contribution to GDP, foreign exchange earnings, employment generation potential and also their contribution to the satisfaction of critical social needs. Moreover, it will not always be possible to
sustain, in the short-term, activities in some sectors at their pre-crisis level, for example, in the case of bauxite since, given the current decline in global demand for this product, there may be no other option but to scale back operations in the industry and explore other possibilities for stimulating output and employment.

As ILO has consistently argued, the approach to public policy must be based on the construction of a social dialogue designed to bring all of the social partners (government, private sector and labour) to the table with a view to arriving at a consensus regarding the elements which should inform the formulation of economic and social policies and also to ensure that the implementation of such policies is supported by the society as a whole. In this context, ILO has done an immense service to the region by providing a comprehensive framework as well as a number of practical measures for dealing with the social and employment-related aspects of the crisis within the framework of its Decent Work Agenda which should serve as an invaluable blueprint for action by governments. Such a framework, together with the other measures identified above, represents an essential precondition for the pursuit of a socially responsive macroeconomic policy in the face of the current crisis.

**Conclusion**

The Caribbean stands at an important cross road in its historical evolution since it faces a number of challenges in tackling the current crisis, which, depending on its response, could influence its future development prospects in a number of profound ways. The region will therefore need to respond to the crisis with creativity and with a sense that, although it presents major challenges, it also provides an opportunity to advance its interests based on the adoption of a common regional approach to its problems. Indeed, a common regional response is an indispensable requirement for dealing effectively with the crisis.
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