Trade liberalization: The Jamaican Experience

Prepared for UNCTAD

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Table of Contents

Section 1.1: Introduction and overview of the country

The Population

The census of 2001 reported that Jamaica had a population of approximately 2.60 million growing at an average annual inter-censal rate of 0.9%. By 2003, the population was estimated to be 2.64 million. According to the Economic and Social Survey of Jamaica (ESSJ) for 2003, "Jamaica is currently at an advanced stage of the demographic transition which is evident in an overall decreasing trend in fertility and mortality rates. These changes in the population have resulted in the ageing of the population structure, evidenced by a declining 0 -14 age group and an increasing working age group (15 – 64), as well as an increasing dependent elderly group (65+)."[1]

Jamaicans have been migrating since the building of the Panama Canal in the late 19th century, and there are now well-established Jamaican communities in many cities of the USA, Canada, the UK, and Central America. Since the 1970s, the annual migration rate is a little over 20,000 persons, a high percentage of whom are skilled.

The economy

Up to World War II in the middle of the last century, the Jamaican society was based on an agricultural economy oriented to the production of food for the domestic market and sugar and bananas for export of to the United Kingdom (UK). In the first post-World War II decade, the economic development strategy was the promotion of industrialization by appropriate state incentives offered to investors, particularly foreign investors. Jamaica gained political independence in 1962 when the process of diversification of the economy was well underway with rapidly growing mineral (bauxite and alumina), manufacturing, construction and tourism sectors. The first decade of independence was a second decade of rapid economic growth, but at a slower rate than in the 1950s, and with mounting pressures for social reform from sections of the population that had unrealized expectations of economic opportunities after colonialism.

The decade of the 1970s has come to be seen as a watershed in the history of the Jamaican economy because of the attempts by the government to chart an alternative path

[1] ESSJ, 2003, P.20.2

to economic development[2] so as to address the social inequalities that was the colonial legacy. A central element of the development strategy of the decade was an increasing role for the state, as the senior partner with the local private sector. In the end the record of economic performance was poor – declining real GDP and real GDP per capita, persistent inflation, an enduring foreign exchange crisis, capital flight and other forms of disinvestment. These were years of intense ideological struggle that not only weakened the economy but also spawned political tension and violence on a scale that hitherto had been unknown. In the minds of the Jamaican voters in 1980, the negative economic performance offset the gains in social policy, and a new government committed to a free market, export-led approach to economic development was elected.

This study examines the record of trade liberalization and the impact that it had had on the Jamaican economy and certain aspects of the development experience. As such it treats with the policies implemented from the 1980s to the present.

Table A1 in the annex shows that from 1981 to 2001 the real GDP grew at an annual average rate of 1.5%, and the real GDP per capita grew at an annual average rate of 0.5%. The first (1981-1986) and the last (1996-2001) were the periods of slowest growth, and declines in the per capita GDP. This record of poor economic performance begs explanation since the reason for undertaking the austerity measures associated with stabilization and structural adjustment and various programmes of sacrifice for the majority of the population was precisely to create the conditions for economic growth.

Except for a couple of years in the late 1960s and the period 1985 to 1990, the trend toward a service economy that began in the early 1960s has continued to the present day, and accelerated after 1990. It was led by the growth of the wholesale and retail trades, tourism, transport, communication and the financial services.

A broad sectoral profile of the GDP is shown in Table A1 and Chart 1 for each of the years 1980-2000. Whereas there is a rising trajectory for the service sectors, there is a declining trajectory for agriculture and the industrial sectors. Table 1 and associated Charts 2 and 3 present more detailed information on the sectoral profile of the GDP. Chart 2 compares three goods sectors with distribution. It is clear that manufacture was

[2] It was to be informed by the ideology of democratic socialism, a variant of Western European social democracy, such as practiced in some Scandinavian countries in the 1970s.

in decline, falling from 21.4% to 15.8% of GDP between 1986 and 2002. At the same time, the distribution sector was on the rise at the end of the period after a decline in the early 1980s. Chart 3 compares the three leading service sectors with the sector, "producer of government services". In this figure, the government's contribution to GDP is in decline while the shares of the GDP contributed by these three services shown are rising.

Education

(To be done)

Employment and Productivity

Despite the weak growth record, the national unemployment rate was almost halved, declining from 27% to 15%, over the two decades, 1980-2000. Typically, the unemployment rate for youth is twice the national rate, and the unemployment rate for women is more than twice the rate for men. **Table 2** shows the real GDP per employed person and the unemployment rate for ever three years between 1980 and 2001.

Table 2: **Macro-Economic Indicators, 1980-2001**

Years	Real GDP Per Employed Person (J$)	Unemployment Rate, %
1980	20,516.7	27.4
1983	21,333.4	26.4
1986	18,663.0	23.6
1989	20,440.4	18.0
1992	21,438.3	15.7
1995	20,949.8	16.2
1998	20,510.2	15.5
2001	21,226.5	15.0

Source: Statistical Institute of Jamaica; World Development Indicators, 2003; ESSJ (Various Years).

Productivity, as measured by the GDP per employed person, made marginal gains over the period.

External Trade

Historically Jamaica has been dependent on a narrow range of primary product exports sold in the UK, the USA, and a few other markets of developed countries, and a wide range of imports of manufactured goods, raw materials for processing, and capital goods from mostly the same narrow range of trading partners. As indicated above, bauxite and alumina replaced sugar and bananas as the leading exports after World War II, and since the 1980s, tourism has become the leading earner of gross foreign exchange.

Chart 4 shows that for the two decade period under review there was a marginal decline in the openness of the economy as measured by the ratio of the sum of exports and imports of goods to GDP. However, there was a marginal increase if the ratio of the sum of exports and imports of goods and services to GDP is used. The second measure is more appropriate since the economy has been reoriented to the production of services.

Except for 1987-1991, and 1993-1995, the ratio of exports of services to exports of goods has risen steadily and sharply reflecting the growth of tourism. **Chart 5** traces the data in **Table III (Economic Performance)** showing the increasing dominance of exports of services over exports of goods.

A plot of manufactures as share of exports of goods, **Chart 6**, shows two distinct cycles of expansion and decline. The share of manufactures expanded from 1984 to 1987, declined through 1990, increased again to 1993 and declined thereafter. Nevertheless, the overall trend was an increasing share for manufactures. The cyclical pattern reflected the rise and decline of the apparel export sub-sector.

Balance of Payments (**To be completed)***

The principal features of the Jamaican balance of payments are:

- The growth of the deficit in the current account ---
  - Faster growth of imports than exports
  - Growth of tourism expenditure
  - The net outflows of investment income
  - The inflows of remittances
- The inflows of private investment
- The inflows of government loans

Section 2.1: Trade liberalization

i. *Process of trade liberalization*

a. The international context

The international context of the liberalization of the Jamaican economy derived from three main processes of change that would eventually help to constitute the process now commonly referred to as globalization:

- The aggressive promotion of economic liberalization within the USA and the UK, and within their international spheres of influence. It began in the USA with the Nixon administration's disconnection of the US dollar from gold in 1973, and was followed up by the pro-business policies of the Reagan administration in the USA and the Thatcher administration in the UK. From Jamaica's perspective, a particularly important response to the de facto devaluation of the USA dollar was the establishment of OPEC and the subsequent rise in oil prices. This would generate a long-lasting shock to the economy because of its almost total dependence on imported petroleum energy products. It would also point to the imperative of a non-petroleum alternative energy utilizing such sources as solar, wind and ethanol from sugar cane.
- The determined efforts by the international financial institutions, led by the International Monetary Fund (IMF) and the World Bank, to promote neo-liberal economic policies. These policies, later to be dubbed the Washington Consensus, ran counter to the nationalist orientation of development strategies that had been adopted by Jamaica and other Third world countries upon attainment of their political independence. The nationalist strategies took the nation-state as the basic frame of reference, sovereignty as the ultimate right of the state, and improvement in the social conditions of the masses of the population as the prime driving force for public policy.
- The decline and eventual collapse of the USSR that transformed the world from a bipolar to a uni-polar world. The existence of the USSR and its socialist strategies meant that there were alternatives to capitalism, and Jamaica like many other Third World countries sought alternative strategies that were consistent with

its historical experiences. One symptom of the decline of the USSR had been the failure of agriculture that forced the USSR to purchase grain from the USA. The subsequent inflation of food prices in 1973, like the rise in oil prices, shocked the Jamaican economy and helped to precipitate the crisis in the balance of payments of the early 1970s. With the collapse of the USSR, the potential development policy space seemed to narrow to what was acceptable to the international financial institutions and the developed countries that determined their policies.

b. The National Context

In the first two decades after World War II, the Jamaican economy was transformed from its traditional dependence on sugar and bananas for export, and domestic agriculture. The export sector was diversified by the development of bauxite mining and alumina production for export, and tourism. The domestic economy developed around import substituting manufacturing, the distribution of imported commodities, construction, and public sector funded utilities and social services[3]. The investment in developing the mining sector provided the foreign exchange for the import dependent manufacturing sector and household consumption[4]. The manufacturing sector had grown up with the incentives and behind the protective barriers that W. Arthur Lewis had recommended, but instead of producing for export as he had advised, it had been diverted to the lucrative fast-growing domestic, and later, to regional markets for consumption goods. As the investment cycle in the mining sector tapered off at the end of the 1960s, the supply of foreign exchange declined, and the demand pressures on the foreign exchange market intensified.

In response to unfulfilled expectations of the popular classes after the first decade of Independence, the government that was elected in 1972 sought to implement reforms and extend social services to the poor and other weak sections of the population. Inevitably, these generated additional pressures on the import bill. With the rise in food and oil prices at the beginning of the decade of the 1970s, a full blown foreign exchange crisis developed and attempts to deal with this characterized the efforts of the government for the rest of the decade. These attempts revolved around:

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[3] See Appendix Table 1
[4] See N. Girvan, 1971

1. Securing more foreign exchange from the leading export industry, bauxite and alumina. After failing to conclude amicable agreements with the multinational mining companies, the government imposed a production levy on the companies that yielded approximately the same amount of increased revenues as the increased cost of imported petroleum. However, the negative reaction of the international investor community to the imposition of the levy with the support of the USA government triggered disinvestment by foreigners, capital flight by local investors, and tight loan conditions by the international financial institutions.
2. International loans, in a climate of cheap finance based on recycled petro-dollars. With the expectation that the temporary slow-down of the economy arising from the negative reaction of the mining companies to the bauxite levy and the international recession of the mid-1970s, the government sought to ease the adjustment with cheap loans being aggressively marketed in the region by the international banks.
3. Restricting imports of luxuries and other "non-basic" goods by way of prohibitive tariffs, quotas, import licensing, and foreign exchange licensing and other controls. "As a result [of falling foreign investment and the oil crisis of 1973], several items were added to the Restricted Import List, partly with the view of saving foreign exchange and partly with the view of encouraging increased import substitution production. By 1975, all items, including CARICOM goods, with the exception of some 19 groups were placed under import licensing. Import quotas were established for virtually all sector categories from the md-1970s"[5]. In short, the government attempted to manage its international trade relations in line with the reduced access to foreign exchange supplies.

By 1977, the government concluded that its efforts to manage the foreign exchange crisis over the previous four (4) years had failed, and that it needed to seek an arrangement with the IMF to facilitate more international loans. Over the next three (3) years, the government concluded two agreements with the IMF, both of which had conditionalities

[5] ECLAC, 1999, P.15

that it was unable to meet, and the loans were suspended[6]. The political crisis that attended the failure of the IMF tests precipitated early elections that brought to power a government that was more favourable to the market-led economic development policies promoted by the IMF, and whose foreign policy aligned it closely to the USA and the UK.

c. International Financial and Trade Agreements

The process of trade liberalization began with the stabilization programmes of the IMF in the late 1970s, and accelerated in the 1980s with the structural adjustment programmes of the World Bank. Between 1977 and 1990, Jamaica signed eight (8) agreements with the IMF and six (6) with the World Bank. In the 1980s too, the United States Agency for International Development's (USAID) loan programmes played a supporting role to the IMF and the World Bank by way of the cross-conditionalities of the financial programmes that were enshrined in what was called the Tri-Partite approach (1987) to Jamaica's adjustment process. In the 1990s, the trade liberalization process was continued with the reform of the Common External Tariff of the Caricom, the pressure to comply with the World Trade Organization's (WTO) international trade regime, the restructuring of trade relations with Europe that is embodied in the Cotonou Agreement, the successor to Lome IV, and the commitments taken in the context of the process to establish the Free Trade Area of the Americas (FTAA). In Jamaica's case, the process of trade liberalization was complemented by far-reaching financial liberalization undertaken in 1991 in the context of a loan programme with the Inter-American Development Bank (IDB).

Trade liberalization was a direct reversal of a strategy of managing Jamaica's international trade relations that were undertaken within a strategic commitment to reducing the trade dependence of the economy and in response to the foreign exchange crisis that mushroomed in the mid-1970s. The economic development strategy of the 1970s had the following as central themes:

1. trade diversification through restructured export and import baskets and a broader range of markets

[6] See Girvan, Bernal, Hughes , 1980

2. import licensing to support import substituting industrialization, and to manage scarce foreign currency resources
3. support for international efforts to index the prices of primary product exports from developing countries to the prices of manufactured imports from the developed countries so as to halt and perhaps reverse the decline in the terms of trade of developing countries.

In return for balance of payments support, a series of IMF stabilization loans required the government to reverse the thrust of its development strategy. One of the key conditions was the reversal of the trend towards more managed trade. In the beginning (late 1970s), the resistance of the government to the change in the policy directions, and its reluctance to implement the agreed loan conditionalities meant that liberalization was essentially the cessation of putting further restriction on trade. With the change of government in the early 1980s to one committed to market led development strategies, and with the support of the IMF and IBRD loan programmes, the pace of liberalisation began slowly and then accelerated as the 1980s turned into the 1990s.

Because of the context in which trade liberalization proceeded, it is difficult to separate out its impact from the impact of fiscal reform, financial liberalization, exchange rate policy and divestment of public enterprises. Indeed, it may well be that the demand management policies that constituted the stabilization programmes of the IMF with the support of the World Bank, raised the price of imports through the devaluation of the Jamaican dollar while reducing the purchasing power of Jamaicans. In this way, there was no surge of imports following the lowering of trade barriers. What is more, the decline in the prices of traditional exports, particularly bauxite and alumina, and the gathering difficulties for sugar and banana in a liberalized international trade regime that withdrew Caribbean and other ACP preferential access to European markets led to a decline in the ratio of trade to GDP, the most common indicator of the openness of an economy.

ii. Measures of liberalization taken

1. 1982-4: Prior to 1982, the trend toward more managed trade was stopped by the conditions of the two IMF loans of the late 1970s. The first positive effort to

liberalize trade came in 1982 as a condition for World Bank financing[7]. The government removed a large number of items (180) from the Restricted Imports List, and eventually abolished import licensing and quota requirements on all but a small number of items. Except for Caricom imports, a new system of tariffs was imposed. The process of liberalization was projected to begin with the substitution of the equivalent tariffs for quantitative restrictions. King and Handa[8] argued that this stage of the process frustrated the intent of trade liberalization

2. 1987-1991: Prior to 1987, import substitution was supported by " high tariff rates, stamp duties imposed on top of the tariffs, a wide array of non-tariff restrictions, complex customs procedures, and a large number of exceptions to the general rules"[9]. The tariff reform programme of 1987-99 sought to:
    - "Reduce--- the bureaucratic obstacles by simplifying the duty system and its administration", increase transparency, reduce the scope for discretionary actions"
    - "Reduce the overall level of tariffs and rationalize the structure of protection by reducing the widely dispersed rates"[10]
3. In 1991, the import monopoly of the Jamaica Commodity Trading Company[11] (JCTC) was abolished. JCTC had been established in 1981 with a monopoly on a wide range of basic foods, including food, cars, pharmaceuticals, and energy. Profits from these items were used to subsidize agricultural imports. The World Bank had identified a number of inefficiencies associated wit the operation of this monopoly, not the least of which was that the majority of the subsidies intended for the poor were benefiting the non-poor.
4. Also in 1991, the government began to aggressively implement the Common External Tariff (CET) of Caricom[12] by which the average level of import duties

[7] The World Bank made three (3) Structural Adjustment Loans to Jamaica between 1982 and 1985 for a total of US$190 million. In 1985, lending was discontinued because the Bank was dissatisfied with the pace of policy changes.
[8] King and Handa, 2000
[9] WB, 1994, P. 37
[10] Ibid, P.37
[11] The JCTC was actually the successor to Jamaica Nutrition Holdings that had been established in 1975 to engage in bulk imports of basic foods and became a vehicle for bilateral food aid. It was therefore an important element of the government's response to the rising import bill of the 1970s
[12] Caricom is a grouping of 14(?) primarily English speaking Caribbean countries that --

> was reduced. In Phase I of the reform of the CET reduced the tariffs from a range of 1-45% between 1990 and 1993 to 5-30%. The revision of the CET was an element in the Caricom strategy of reducing production costs, stimulating more efficiency, protecting sensitive industries and encouraging new types of production activities[13]. Phase II was implemented in the beginning of 1995, and Phase IV in 1999.

King and Handa summarize the trade liberalization measures in the 1990s as follows: "In 1990, the average tariff rate was 25 percent (see **Table 5 below**). The first tariff reduction exercise occurred in 1991 and reduced the average tariff to 22.1 percent. More importantly, the exercise started a process of simplifying the tariff code to reduce the tariff dispersion. The estimated standard deviation of tariffs fell from 20.7 to 16.8 percent at this time. The second round of liberalization in 1993 saw average tariffs reduces to 15.9 [percent], and with further simplification of the tariff code the standard deviation fell to 13.4[percent]. In 1995, another implementation dropped average tariffs to 14.0 [percent]. Finally, by the last round, which was effected in 1999, the average was brought to 11.9 [[percent]. Even with this, a fair amount of trade interference still persists since the dispersion of tariffs remains high, with some tariffs, particularly those on raw materials for manufacturing, at zero, while on some final goods that compete with domestic industries, the tariff is near to (and in a few cases above) 100 percent."[14]

A major study led by Bloom concluded [in 2004] that "There are still some trade restrictions in place, in the form of customs and stamp duties for domestic consumption on products that are not produced domestically, such as automobiles, and high tariff rates on vulnerable domestic industries, such as agriculture; but the tendencies towards reduction of trade barriers are obvious".[15]

[13] See ECLAC, 1999, P. 32
[14] King and Handa 2000, P.3
[15] Bloom et al, 2004, P.9

Table 4-: Average Tariff by Economic Sector, %

Sector	1985	1987	1989	1991	1997	2002
Whole economy			49.9	20.3	10.9	8.9
Agriculture			53.0	24.4	20-40	
Mining			43.5	9.6		
Manufacturing			49.8	20.2	10.3-30	
Consumer Goods	10-60	40-103	58.0	29.5		5-20
Intermediate Goods	5-54	16-68	50.5	13.4		
Capital Goods	10-60	30-89	24.9	12.1		0-5

Source: World Bank, 1994, Table 1, P.38; 2004, P.144

King and Handa estimated the average import tariff and the dispersion in the 1990s. Their estimates, and the estimates of the average import tariff by the World Bank, are shown in the **Table 5**:

Table 5: Average Import Tariff, 1989- 2002

Year	Average[a] Import Tariff, %	Standard Deviation of Tariffs	Average[b] Import Tariff, %
1989	25.0	20.7	n.a.
1990	25.0	20.7	n.a.
1991	22.1	16.8	20.3
1992	22.1	16.8	n.a.
1993	15.9	13.4	n.a.
1994	15.9	13.4	n.a.
1995	14.0	13.4	14.0
1996	14.0	13.4	20.8
1997	14.0	13.4	10.9
1998	11.8	14.7	9.7
1999	n.a.	n.a.	8.9
2000	n.a.	n.a.	10.6
2001	n.a.	n.a.	
2002	n.a.	n.a.	8.9

Source: [a] King and Handa, 2000, Table 2, P.30

[b] WB, 2004, Fig. 7.1, P.144

The decline of the average import tariff over the decades of the 1980s and 1990s is shown in **Tables 4** and **5**, and is the principal indicator of the liberalization of the import regime in Jamaica. However, there have been other measures taken that facilitate trade.

The government is implementing a trade facilitation project that seeks to upgrade the quality of the customs and to reorient it as a service to facilitate rather than hinder international trade. This began in 1993 with the World Bank's Private Sector Adjustment Loan that had as conditions the reduction of tariff protection under the CET and the reform of the Customs so as to improve the quality and speed of clearance. It also sought to improve government revenues. This is currently a part of a programme to make Jamaica more WTO compliant.

In 2002, the government started using actual import prices as the basis for customs valuation instead of the traditional reference price, a move that led to a decline in import values in addition to making valuation more transparent.[16]

iii. *Major constraints inhibiting country exports*

Jamaica's export basket became increasingly diversified in the latter half of the 20th century. Up to World War II, Jamaica's exports were substantially sugar and bananas, both marketed under preferential agreements with the United Kingdom. In the 1950s Bauxite and Alumina exports assumed the role as the principal export and has held that position since then. However, in the 1980s, the rapid growth of tourism established the sector as the leading earner of foreign exchange (in gross terms[17]).

Liberalization of international trade regimes in the era of the WTO has dismantled Jamaica's (and other Caribbean and ACP producers') preferential access to the European markets, especially for sugar and bananas[18]. The impact of these changes is not as important to Jamaica's export earnings as movements in the price of aluminium which determine the earnings from bauxite and alumina exports. There are other factors as well, particularly the reaction of the multinational mining companies to the levy regime imposed by the government on production and the temporary loss of smelting capacity for Jamaican bauxite with the damage to Kaiser's Gramercy plant in Louisiana in 1999. While measures to liberalize international trade would have had little impact on the mineral exports since the sector had never been protected, it is arguable that Jamaica became a more attractive investment prospect for the mining companies as a result of the liberalization of the economy and in particular the financial liberalization that removed exchange controls and controls on the movement of capital.

Like the Bauxite and Alumina sector, it was less trade liberalization, and more the overall thrust to a market-driven economy that boosted investor confidence in the tourism sector.

There was some short-lived success in non-traditional manufacturing exports, primarily apparel, produced in the Free Zones. For the most part these were operations that assembled imported parts using cheap, mainly female non-unionized, labour. There were no linkages with other local industries except for the supply of utilities. Eventually,

[16] WB, 2004, P.144
[17] There is mixed evidence that the sector is a net earner of foreign exchange. See OAS, 1994
[18] See Myers, 2004

Jamaica became relatively uncompetitive vis a vis other Central American and even South American producers because of relatively high labour costs, relatively low labour productivity, and high utility and security costs. The enterprises in the Fee Zone technically operated outside of the customs of Jamaica, and as such were unaffected by the trade liberalization measures.

iv. Major reversals of the trade liberalization process

The trend of declining protection was interrupted by the imposition of “additional stamp duties” on “agricultural products, beverages, tobacco, and aluminium products”.[19] Beyond the inefficiencies in implementing change, and attempts to slow down the process especially with regard to agricultural products, there have been no deliberate attempts to reverse the liberalization process.

v. Financial liberalization – chronology and relationship to trade liberalization

a. In 1990, the government began the liberalization of the financial markets by licensing commercial banks to trade in foreign exchange and to hold foreign currency denominated deposits. The following year, 1991, exchange controls were eliminated, and the ensuing rapid devaluation of the Jamaican dollar stimulated the highest recorded annual inflation rate, 80.2%. In return for promised balance of payments support from the IDB, the government also ended the policy of subsidizing interest rates to certain sectors of the economy, particularly, agriculture, as well as other controls on the capital market.

b. There have been many studies of the financial liberalization seeking to understand the causes of the crisis of the mid-1990s that has left the government with a huge debt. Certainly, the financial liberalization made Jamaica more attractive to foreign investors in search of interest differentials on short term investments. It stimulated as well the rapid growth of the financial sector in a speculative boom that inevitably imploded. This was one of the reasons for the rapid growth of the service sector in the 1990s.

[19] WB, 2004, P.144. The Bank provided examples of how increased rates of additional stamp duties (raised from 32% to 80%) on agricultural products, such as beef, with a tariff at the bound rate of 100%, more than tripled the duty from about 85% to 260% so as to provide substantial protection for domestic producers. However, it should be noted that the level of protection could have been lower if imports, particularly from the USA had not been subsidized.

vi. Implementation

By way of summary, trade liberalization was one of several policy changes that were implemented over two (2) decades, 1980 – 2000, in the context of IMF Stabilization and World Bank and IDB structural adjustment programmes with support from USAID balance of payments support funding to the government of Jamaica. Even with the change in policy orientation of the new government in 1980, there was initial resistance to rapid liberalization of the economy, and measures were implemented slowly and often not in the spirit of the commitments given in the various international agreements. Like other aspects of liberalization, trade liberalization was a condition for receiving international funding.

It is arguable that other elements of the policy reform, particularly the stabilization programmes of tight demand management and tight monetary policy, tended to counter the expected impact of trade liberalization on the balance of payments and on economic growth.

Section 2.2: Economic impact of trade liberalization

i. Impact of trade liberalization on economic growth

The period of fastest growth in the last two decades was 1986-90 when the growth rate of the GDP rose to a robust 5.0% per annum. This latter period was preceded by the first major trade liberalization programme (1982-1986), and despite the severe damage[20] wreaked by Hurricane Gilbert in 1988, this was the five-year period of very high growth by Jamaica's recent standards. Recall that Jamaica entered into three (3) IMF Stand-By agreements and two (2) World Bank sector adjustment loans during the period, 1986-90. Two of the principal factors accounting for the high growth rates were the growth of tourism and the sharp decline in oil prices.

Throughout the 1990s the economy grew much slower. The decade began with the liberalization of the financial markets and in particular the foreign exchange market. Following a four year speculative boom the rapidly growing financial sector went into a major crisis. The government opted to bail it out and succeeded in doing so in record time, but at major costs that reversed the gains that had been made in the state of government finances in the previous years. "The crisis, one of the largest in the world (in terms of GDP) was resolved relatively quickly and has led to significant improvement in regulation and supervision of the financial system but also to a huge increase in an already large public sector debt."[21]. In the balance, the marginal movements of the GDP in the last 5 years of the 1990s meant that the economy was virtually stagnant, but there was an indication that the declining growth trend was being reversed.

GDP per capita, per employee - to be done

In theory, trade liberalization meant easier access to imports that were crucial to expanding output, and in particular exports. On the other hand, in order to protect the balance of payments from a surge of imports the government maintained tight monetary

[20] ECLAC, 2004, P.51, estimated the damage to be US$595 million.
[21] WB 2004, P.24

policy and strict demand management. Devaluations of the Jamaican dollar also restrained the tendency to import.

In 1993, the PIOJ expressed concern in its annual report on the economy, the Economic and Social Survey, about “trying to achieve multiple policy objectives simultaneously in a consistent manner”:

“While the reduction in tariff levels may have made the country more externally competitive in one respect, there are indications that the domestic policy environment worked against the attainment of this goal. This was evidenced by the fact that the rate of increase of domestic inflation (30.1 per cent) far exceeded the annual average rate of depreciation of the exchange rate of the Jamaican dollar vis-a vis its US counterpart (11.8 per cent). This is a significant disincentive to the production of exportables, especially in light of accompanying high interest rates. On the other hand, the increase in the domestic crop production during the review year could be an indication that the higher exchange rate which prevailed during the year enhanced the production and consumption of import substitutes”[22]. This observation would continue to be relevant throughout the 1990s.

The World Bank has put forward several reasons for the weak growth performance as indicated by estimates that were based on official statistics:

1. The rate of growth of GDP underestimates the actual growth because of the significant size of the informal economy. In 2002, the IDB estimated the informal economy, excluding illegal activities such as the trade in illegal drugs, to be upwards of 40% of GDP in 2001.
2. The stagnation in the last decade of the 1990s was in part a consequence of the financial crisis of the mid -1990s “and the consequent monetary tightening that left a massive, costly debt overhang.”[23] The crisis itself resulted from the financial liberalization without the appropriate regulatory mechanisms being put in place. In hindsight, the liberalization of the capital account appears to have been precipitate without proper preparation.

[22] Economic and Social Survey, 1993, P. 3.7
[23] WB, 2004, P.57

3. Negative international economic conditions. This was especially important for the bauxite/alumina and tourism sectors on which the performance of the Jamaican economy depends critically.
4. Appreciation of the real exchange rate as a result of capital inflows attracted by the high interest rates of the tight monetary policy. It is argued by some[24] that this re-valuation of the Jamaican dollar served as a disincentive to the development of non-traditional exports because the production of non-tradables continued to be more attractive.
5. The rise in real wages after 1996 was yet another disincentive to export activities. There is ample evidence that many garment producers operating in the Free Zone in the late 1990s and the early 1990s re-located to other countries in Latin America and the Caribbean because of rising costs in Jamaica. The three most commonly cited costs were the costs of security, utilities and labour. In the latter case, it was of course the cost of labour in relationship to the productivity of labour. There is evidence that the productivity of labour also declined in the last decade of the 1990s.
6. High crime rates required high security expenditures by firms, and thus higher production costs.
7. "Foreign Direct Investment (FDI) moved from US$129.7 million in 1994, to US$722 million in 2001, making Jamaica the second largest earner in the Caribbean, and number five in the wider Latin American region. Additionally, in terms of FDI inflows, Jamaica has been ranked an "overachiever" since 1988 and was ranked 26th among the 140-country grouping of the United Nations"[25]. Despite this high rate of investment, the economy did not have the anticipated growth impact because so much of the capital created – physical infrastructure – was underutilized. Enterprises were restricted to single rather than multiple shifts because of the risks of crime. The Bank could also have noted that much of the FDI funded a change in titles of existing enterprises (e.g. change in ownership of the electricity monopoly) rather than created new productive capacity.

[24] King and Handa, 2000, P.7
[25] Ministry of Foreign Affairs and Foreign Trade, News Release, February 17, 2003

8. The Bank also noted the views of some Jamaican entrepreneurs that the high rates of interest on government paper made investment in production, with all its risks and costs, far less attractive to investors.

In summary, these factors individually and collectively counteracted whatever growth impetus that trade liberalization was expected to have.

ii. Industrial development

In the 1990s, in the wake of the trade and financial liberalization processes, the sectoral composition of the GDP shifted sharply in favour of the services, and against the goods producing sectors and the "producers of government services". Between 1991 and 2000, the shares of the various sectors in the GDP increased as follows:

Table 6: Changes in the Sectoral Profile of the GDP

Sector	Growth of Share of GDP, 1991-2000, %
Transport, Storage and Communications	85
Finance	42
Electricity and Water	38
Miscellaneous services	27
Real Estate and Business Services	14
Distribution	13
Mining	6
Agriculture	3
Government	-3
Manufacturing	-14
Construction	-17

Transport, storage and communication grew the fastest because of the importation of motor vehicles and telecommunications equipment. Prior to trade liberalization, motor vehicle imports had been highly restricted. The boom in telecommunications services was driven by the international growth that in turn was spurred by the information technology and telecommunications revolution. But in part, it was also facilitated by the deliberate liberalization of the telecommunications sector that eventually eliminated the monopoly that had been guaranteed to Cable and Wireless, the UK multinational, when the state owned Jamaica Telephone Company had been divested in 1988[26].

Next was the Financial sector that increased its share of the GDP rapidly up to 1994, declined through 1998, and resumed its rapid increase since then. Electricity and Water also grew fast, but its share of the GDP is small, around 5.5% in 2000.

More important are the very high increase of the share of the "miscellaneous services" (27%), primarily tourism, and the modest to high increase (14%) of the share of the distribution sector, primarily the wholesale and retail trades. All of these sectors are import intensive, and must have benefited from the trade liberalization measures.

Only mining and agriculture showed marginal increases over the decade. Notably manufacturing and construction, the two sectors that drove the industrial development of the domestic economy in the high growth years of the 1950s and 1960s both contracted sharply over the course of the 1990s. Note too that the contribution of the government to the GDP also declined marginally.

iii. Demise of traditional manufacturing and the rise of Free Zone manufacturing

The decline of manufacturing had begun in the 1980s. Even the apparel sub-sector, the most successful in thepost-1980 period had suffered. In an unpublished survey of the apparel sub-sector of the manufacturing sector undertaken for JAMPRO[27], the report noted a decline in the number of firms and the total employment in the sector between 1980 and 1989. The report estimated that in the 10 year period, the number of firms had declined from 650 to 115 and the total employment had declined by 68%.

In 1992, the PIOJ summarized the problems facing the manufacturing sector in its discussion of the sector's performance in the annual ESSJ. It singled out the complaints by the sector's leaders against high interest rats (that were associated with stabilization of the economy) and the unfair competition that had been triggered by trade liberalization. With regard to the latter, the government had set up an Anti-Dumping Board and Import monitoring programme to ensure that sub-standard products were not imported to the detriment of the local producers. In addition, the government provided technical

[26] See Davies 2003

[27] JAMPRO is the specialized government agency for promoting investment. In 1989, it had invited a well-established firm, Market Research Services to conduct a survey of the apparel sub-sector.

assistance for the modernization of the sector to enable its competitiveness. Finally, the ESSJ noted the mixed reaction of the sector to the reform of the CET that effectively lowered tariffs. While the manufacturers opposed the reduction of tariffs on the grounds that it exposed them to competition from extra-regional producers, they welcomed the reduction of duties on raw materials and capital goods[28].

Chart 7 shows that manufacturing exports rose almost without exception to 1999, and then collapsed precipitously over the next five (5) years. The rise in exports together with the decline of the sector's share of GDP throughout the 1980s and 1990s shows the shift from non-tradable production to tradables. Alternatively, the decline in the contribution of manufacturing to GDP was net of the growth of non-traditional manufacturing, primarily apparel for exports. Again, there were so many external and internal influences on the sector's performance that it is very difficult to separate out the impact of trade liberalization on the sector's performance.

iv. ***Government revenue***

ECLAC's study (in 1999) of the impact of trade liberalization on government finances in Jamaica concluded that "International trade taxes are very important to the government's revenue. In addition, the study has shown that liberalization of the economy did not have a negative impact on government revenue because as the tariff rates fell, imports increased and more duty was collected. Furthermore, the General Consumption Tax[29] (GCT) introduced in 1991 (and charged on imports after duty) more than compensated for any losses in revenue"[30]

The GCT was introduced in the same year, 1991, that the government began to implement the Common External Tariff (CET) of Caricom[31] by which the average level of import duties was reduced. In Phase I of the reform of the CET, tariffs were reduced from a range of 1- 45% between 1990 and 1993 to 5 -30%. The revision of the CET was an element in the Caricom strategy of reducing production costs, stimulating more

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[28] ESSJm 1992, P.10.1-10.3

[29] The GCT is a sales tax. When it was introduced, it was 10% on a limited range of goods and services. Since then it has been increased in two stages to 15% and the range of goods and services exempted from the tax has been reduced.

[30] ECLAC, 199, P.9

[31] Caricom is a grouping of 15 primarily English speaking Caribbean member countries and 5 associated members. The group is in the final stages of implementing a single market with the commitment to move to a single economy.

efficiency, protecting sensitive industries and encouraging new types of production activities[32]. The GCT was a central element in the tax reform that sought to simplify the system by replacing a number of indirect taxes while shifting the burden of taxation from production to consumption. In the year that it was introduced, together with the Special Consumption Tax (SCT) levied on "petroleum products, cigarettes, spirits/beer, wine and alcoholic beverages etc", the GCT compensated the government successfully for the loss of import revenues by bringing in more tax revenue than had been anticipated.

While the import duties were replacing quotas, and then themselves being reduced, international trade taxes came to include GCT (levied on imports) and SCT. The net effect was a continuous absolute growth in international trade taxes. **Table 7** shows that in 1991, these taxes accounted for 18% of total government revenue, increased to 37% in 1995, and then declined to 26% in 1997.

The decision to intervene in the financial sector crisis of the mid-1990s has left the government of Jamaica in difficult financial circumstances. The national debt is currently upwards of 145% of GDP, 65% of revenue is used to service the debt, and indeed the government of Jamaica has maintained an impressive record for several years now of no default and high primary surpluses – 15% of GDP – in order to assure bond holders of the government's willingness to honour its obligations. In this situation, the medium term strategy hinges crucially on economic growth to generate the revenue to service the debt and to improve the financial indicators measured with respect to the GDP. The recent damage wrought by Hurricane Ivan an the shocks from the oil price hike in 2004 have again set back the government's programme of recovery, but so far it appears that it will weather these recent shocks

v. *Openness*

Chart 8 shows that for the two decade period under review there was a marginal decline in the openness of the economy as measured by the ratio of the sum of exports and imports of goods and services to GDP. Imports of goods and services as a proportion to GDP rose marginally but not sufficient to offset the decline in the ratio of exports of goods and services to GDP

[32] See ECLAC, 1999, P. 32

Sugar and banana exports have been in secular decline in the context of the withdrawal of preferential access to traditional markets in Europe. This is one of the far-reaching impacts of global liberalization on the Jamaican economy.

vi. *Growth of imports*

The reduction of stamp duties on agricultural goods, as conditions for the World Bank Agricultural Sector Adjustment Loans I and II, led to a significant rise in imports of fruits and vegetables as early as 1993. Similarly, there was a rise in imports of meat products, particularly poultry parts. Imports of dairy products grew as a result of the deregulation of the dairy trade with the elimination of the JCTC import monopoly in 1991.

The ratio of imports of goods and services to exports of goods and services increased slightly---

"Manufactured goods imports fell in the 1970s owing to the imposition of quantitative restrictions (QRs), but these recovered in the 1980s after most QRs were eliminated by 1985, and had gone up to over 67 percent of merchandise imports in 2001, from 40 percent in 1980."[33]

vii. *Pressure on the exchange rate*

Trade liberalization naturally increased the demand pressures on the foreign exchange market that spilled over into the vibrant black/parallel/street market in foreign exchange until the system of controls was abolished in 1991. **Table 8** shows the nominal and real exchange rates, and the annual inflation rates.

[33] WB, 2004, P.143

Table 8: Inflation, Nominal and Real Exchange Rates with the US$

	Annual Inflattion rate, %	Nominal exchange Rate, J$ = US1.00	REER 1990=100
1985	23.0	5.56	96.91
1986	10.4	5.48	104.13
1987	8.4	5.49	102.77
1988	8.8	5.49	104.98
1989	17.2	5.75	112.35
1990	29.8	7.99	100.00
1991	80.2	20.95	90.15
1992	40.2	22.15	78.07
1993	30.1	32.25	88.19
1994	26.8	33.04	86.61
1995	25.6	39.44	92.37
1996	15.8	34.70	109.87
1997	9.2	36.09	126.93
1998	7.9	36.95	134.22
1999	6.8	41.16	132.96
2000	6.1	45.30	130.59
2001	8.8	47.17	131.76

Sources: STATIN, BoJ, World Bank, 2004

As the stabilization policies brought the inflation rate down to single digits, the real exchange rate appreciated despite the depreciation of the nominal rate. The World Bank attributes the "uninspiring export performance"[34] to the appreciation of the rate. Whatever the validity of this claim, it is only one of several factors that inhibit the growth of production. Chief among these are the high rates of interest on government securities that are far more attractive than investment in productive activities.

viii. *Informal economic activity*

In the context of import restrictions in the 1970s, the informal sidewalk trade in illegally imported consumption goods mushroomed. Demand by these traders for foreign exchange under the pre-liberalization system of licenses, led the government to license some traders as Informal Commercial Importers (ICI). As the restrictions on imports

[34] World Bank, 2004, P.145

were eased in the 1980s, many of the ICIs who supplied the sidewalk vendors/higglers lost their competitive advantage to the established importers of the formal business sector who could finance larger shipments of imports at lower unit costs. Many vendors began to source their supplies from local wholesalers, especially from the most recent influx of Chinese immigrants who were importing goods from Asia.

On the other hand, access to cheaper used vehicles imported from Japan created the basis for other informal economic activities, such as illegal taxi operations and other transport related activities

Section 2.3: Development impact of trade liberalization

i. Adjustment costs of trade liberalization, unemployment, duration of unemployment

Table 9: Labour Market indicators

The unemployment rate declined from 27.6% in 1982 to 18.0% in 1989 due to a slowing of the rate of growth of the labour force and the rapid increase in female employment in the second half of the decade in the expanding apparel export sector in the Free Zones. Despite this, females were more than twice as likely to be unemployed as males as the female unemployment rate rose to as high as 2.39 times the male unemployment rate in 1989[35].

The sectoral profile of the employed underwent radical shifts over the course of the 1980s. As a share of the total employed labour force, public sector employment fell from 19.1% in 1980 to 11.1% in 1989, which was consistent with the programmed reduction of the role of the state in the economy. The share of agriculture also declined from 35.9% in 1977 to 28.4% in 1989.

Manufacturing's share of total employment increased in the 1980s until it reached a high of 15.4% in 1989, marginally less than the 15.6% share of commerce. "Other services" accounted for 19.9% in 1989, up from 13.8% in 1977. Altogether, the service sectors dominated employment with 48.9%, almost a half of total employment.

These major changes in the level, rate, and sectoral composition of employment undoubtedly resulted from the policy changes that sought to transform the economy into a liberal market-driven economy, but we cannot separate out the impact of the trade liberalization component from the rest of the other policy changes. We surmise that the shift in manufacturing output from consumption goods for the domestic market to apparel for export was in part the result of the competition from imported consumer goods made possible by the trade liberalization. The rapid growth in employment in the distributive trades in the 1980s supports this conjecture.

In the 1990s, the unemployment rate remained fairly constant at between 15% and 17%. Employment grew from 908,000 in 1991 to 960,000 in 1996, and, following the financial

[35] Witter and Anderson, 1991, P. 69

crisis, it declined to 939,000 in 2001 for a net gain of only 30,000 jobs in the decade. One explanation for the weak employment effect of the investment flows is the capital-intensive nature of the new economic activities in the face of rising wage rates in the second half of the 1990s. Yet another is the underutilization of the capacity built by the high rate of investment because of crime.

A part of the reason for the fairly constant unemployment rate despite the small number of jobs created was the high rate of migration, averaging more than 20,000 per year, which in effect siphoned off the natural increase in the labour force. Yet another reason were the overseas employment opportunities as agricultural labour and hotel workers. In recent times, recruiters from the USA and the UK have come to Jamaica every year to hire nurses and teachers. What is more, a high proportion of the migrants were skilled. The World Bank cites Carrington and Detragiache, 1998 to conclude that "----in 1990, between 25 and 30 percent of Jamaica's secondary graduates and over two-thirds of its tertiary graduates were in the United States".[36]

At the end of the decade of the 1990s, the following changes in the structure of employment were notable:

- Agricultural and manufacturing employment had declined by 20% and 40% respectively
- Employment in the Services had grown by 12%
- Whereas the male employment rate was fairly constant around 90%, the female employment rate increased by a little over 7% to reach 82% by 2002. The unemployment gap between males and females was therefore closing.

Witter and Anderson showed that the structural adjustment polices had reduced the real value of wages throughout the 1980s. King and Handa argued that the adjustment at the beginning of the 1990s sharply reduced the real value of wages, and that it was not until 1996 before wages caught up with where they were in 1989. By 1998, they were "29.3 percent higher – during a time when the economy stagnated"[37] They go on to argue that "While average wages in the tradable sector was 85% of those in the non-tradable

[36] World Bank, 2004, P.66
[37] King and Handa, 2000, P.13

activities in1989, by 1998 they were only 69%. Further the relative fall in wages in tradables occurred across skill levels."[38]

ii. Existence and efficacy of policies or institutions that helped to mitigate the extent of the adjustment costs

(To be done)

- Social Safety net programmes
- Informal economy
- Remittances
- Migration
-

iii. Impact of trade liberalization on poverty levels and other development indicators

As with the unemployment rate, the poverty rate in Jamaica declined throughout the decade of the 1990s after the trade and financial liberalization processes had been completed. Poverty rates (headcount) have been estimated annually based on data from the Survey of Living Conditions. Table 10 shows the incidence of poverty as measured by the headcount index. Notice the sharp drop in 1997 and 1998, years when the inflation rate went into single digits, and the inflow of remittances was rising. Both of these had appositive impact on per capita real consumption, and are the most likely explanations for the decline in poverty rates in a period when the growth rate of the economy was marginal.

Table 10: Incidence of Poverty, %

	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001
Poverty, %	28.4					27.5	26.1	19.9	15.9	16.9	18.7	16.8

Source: PIOJ, Survey of Living Conditions, Annual

Here again there has been speculation that the informal economy is providing incomes that are not being captured in official estimates of the GDP. Three other indicators that are commonly cited to show the relatively high standards of mass consumption are the

[38] Ibid, P.13

growth of automobile ownership, cell phones and computers. Table A10 shows data for these three indicators.

Section 3: Policy lessons and implications

Section 3.1: Conclusions and Policy lessons

i. Key lessons to be learned from case study on trade liberalization

- Stabilization should precede liberalization
- Establish regulatory framework before/simultaneously with liberalization – e.g. anti-dumping, standards
- Improved education of producers, workers and consumers likely to be impacted by liberalization –
- More time for sectors of particular sensitivity with respect to food security, employment, agro-industrial potential to adjust to import competition
- Assistance to producers to adjust to the competition by way of improved productivity and/or change of activity

Section 3.2: Major issues country in current Doha Development Round

ii. Implications of the current Doha negotiations and the trade reform process

(To be done)

In an "Update" provided by the Foreign Trade Department, Ministry of Foreign Affairs and Foreign Trade, December 16, 2004, the concerns were set out as follows:

- Special and Differential Treatment. There has been little progress in implementing the Doha mandate on special and differential treatment for "small vulnerable developing countries'
- NAMA
    i. Jamaica is concerned about the non-linear formula being proposed to cut tariffs in the "July Framework Package (WT/L/579) adopted by the WTO General Council on August 1, 2004. This --- can cut higher tariffs more deeply, and could force reductions in our applied tariffs on a number of products that are sensitive or yield significant duties."
    ii. The challenges facing Jamaica in NAMA are greater than the agricultural access because there are no exemptions like the Special Products category for agriculture. Jamaica will have to be

careful to ensure that the scope and timing of the reductions “do no harm to our vital interests with respect to trade and economic policies”

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