RNM/OECS COUNTRY STUDIES TO INFORM TRADE NEGOTIATIONS: ANTIGUA AND BARBUDA

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ANTIGUA AND BARBUDA

INTRODUCTION

The economy of Antigua and Barbuda traditionally depended on the production of sugar and cotton. However, over the years the authorities pursued a strategy of development based on the tourism sector. This industry that utilises Antigua's many white-sand beaches, account for about 75% of foreign exchange earnings, contributes directly and indirectly about 60% of GDP and employs about 25% of the active labour force (1998 MTESP).

The structure of the Antiguan economy has remained roughly stable over the period 1986 to 1998. The Wholesale and Retail sector is the largest, accounting for roughly 20% of GDP. The next largest tourism represented by Hotels and Restaurants accounts for 15% of GDP. Communications represents about 15% of GDP and Government services 10%. The economy is dominated by the production of services. Together the services sectors account for approximately 81% of GDP.

RECENT MACROECONOMIC PERFORMANCE

The recent economic performance of the economy of Antigua and Barbuda can be divided into three distinct periods. From 1986-1989, the economy grew at a rate of about 6% annually continuing the relatively high growth rates experienced during the early eighties. The period 1990-94 was marked by modest growth with tourism growing at a reduced rate. The final period 1995 to 1999 was marked by alternating decline and partial recovery from the effects of five hurricanes in the space of five years.

The economy grew at a rate of 7.7% per annum over the period 1986-1989 fuelled largely by expansion in the tourism and related construction sectors. Stay over arrivals averaged 12% per annum and the construction sector grew at an average of 20% annually over that period. Substantial growth also occurred in the communications (18.8%) and financial services sector (18.1%). The manufacturing sector experienced relative stagnation growing by a mere (3.1%) annually.

The period 1990 to 1994 was marked by much slower growth as the worldwide recession led to a marked slowing of the rate of increase in tourist arrivals. The rate of growth of GDP slowed from 6.8% in 1989 to 2.3% in 1990. Although the growth rates recovered in 1993 and 1994 the average rate of growth for this sub-period was 3.9% - approximately one half the rate for the earlier period. The rate of growth of all the sectors slowed considerably with the rate of growth of tourist arrivals slowing to about 6%. The communications sector, however, showed some resilience growing at a rate of 10.1%. The manufacturing sector recorded a decline of -3.4% over the period consequent on the softening of the market for electronic exports in the USA and the uncompetitiveness of the products and payments difficulties in the CARICOM Market.
Antigua and Barbuda recorded a -4.95% growth rate in 1995 consequent on the passage of hurricanes Louis and Marilyn. Much of the hotel plant, private housing, businesses and infrastructure were severely damaged. Recovery was fairly rapid in 1996 and 1997 with growth rates of 6.1% and 5.6% respectively but another hurricane in 1998 and two more in 1999 have highlighted the vulnerability of small states dependent on tourism as their livelihood. The successive hurricanes have placed the country in a state of continuous adjustment to natural disasters. Neither the level of total tourist arrivals or the earning from tourism as a percentage of GDP has re-attained the levels reached in 1994. In fact the hotels have had to discount their rates heavily in order to keep the level of occupancy up and since then, they have not been able to apply the rates charged prior to the hurricane in 1995.

**RECENT FISCAL PERFORMANCE**

Fiscal performance in Antigua has reflected the administration’s strong interventionist policies over the past fifteen years towards its goal to expand productive investment and provide employment for its citizens. Government expenditures have been directed towards stimulating investment by providing direct support in services to private sector development as well as direct investment in productive enterprises. At the same time government provided generous tax incentives to support private sector initiatives in all sectors of the economy.

Central government fiscal performance was relatively strong during the period 1984 to 1988 with current surpluses averaging 2.8% of GDP and overall surpluses averaging 1.6% of GDP. However, this performance deteriorated as government increased capital outlays and its reliance on commercial borrowing from both domestic and external sources. By the end of 1998, the fiscal deficit stood at 4.8% of GDP.

Revenue buoyancy declined steadily after 1986, although this decline was less evident in the case of taxes on international trade than on direct taxes. Revenue buoyancy for direct taxes averaged 0.8 during the period 1987 to 1998 compared to taxes on international trade at 0.9. Recurrent revenue as a per cent of GDP fell from 25.1 in 1984 to 24.8 by 1998.

On the other hand recurrent expenditure rose from 24.3% to 24.5% of GDP during the same period. Although the overall growth of recurrent expenditure as a per cent of GDP was marginal, significant increases occurred in wages and salaries which increased proportionately from 45.7% to 56.7% of total recurrent expenditure. Similarly, expenditure on transfers as a per cent of total recurrent expenditure increased from 8.4 in 1984 to 10.6 in 1998 as government sought to absorb the losses incurred by public utilities, while outlays on goods and services as a per cent of total recurrent expenditure fell from 33.1 in 1984 to 21.7 in 1998. Interest payments as a per cent of total recurrent expenditure was fairly stable at 12.9 in 1984 and 11.2 in 1998; but this does not take account of payment arrears.

An analysis of the sectoral allocation of recurrent expenditure reveals that expenditure on general administration showed the highest growth in absolute terms (average annual growth rate was 23.4%) during the period 1990 to 1995. This growth reflects the high level of employment in the general services as government sought to absorb some of the surplus labour in the economy.
Health and education realised average annual growth rates of 7.6 and 10.6% respectively during the same period. Economic services increased at an average annual rate of 6.8%.

At the end of 1998 the external public debt stood at $619.22 million, having declined from a high point of $700.54 in 1991. The stock of debt was heaviest in the utilities sector and in the tourism sector which accounted for $177.6 million and $262.4 million respectively at the end of 1998. GDP growth in both sectors was significant, but uneven. The government sought and obtained debt forgiveness and restructuring for a large part of its debts during 1997/1998 which considerably reduced the stock of debt, debt service arrears (which fell to about 5.0% of GDP in 1998) and debt service costs.

However, the persistence of fiscal deficits has necessitated increased borrowing, both domestic and external. One disturbing aspect of the debt profile is the high proportion of commercial debt. By 1999, commercial debt (including export credit) accounted for 88.8% of total external debt compared to 9.0% bilateral debt. While most of the commercial debt is denominated in US dollars and deutsche marks, significant changes were observed in the level of debt denominated in Kuwaiti and Chinese currencies, pointing to greater exposure to currency risks in the management of Antigua’s external debt.

STRUCTURE OF REVENUES

Antigua’s dependence on taxes from international trade increased from 51.0% in 1994 to 57.6% in 1998. In that year taxes from income and profits amounted to only 8.0% of total revenue, taxes on property 1.2%, taxes on domestic goods and services 18.8% and non-tax revenue 14.5%.

Direct taxes generally consist of the following:

- personal income tax on incomes earned by non-residents with rates ranging from 2.5 to 55%, the highest rate applying to incomes above $30,000;

- education levy on wages and salaries above $6,500 with rates of 2.5 and 5%, the higher rate applying to income over $60,000;

- corporation tax of 40% of net income;

- business tax at 25% of net income of non-incorporated businesses;

- withholding tax of 20% on dividends, royalties, interest income, rents and management fees;

- property tax based on the annual rental value of properties ranging from 3.5% to 14% in the case of properties owned by citizens and 5% to 20% on properties owned by non-citizens. Other taxes on property include a non-citizens undeveloped land tax ranging from 5 to 20%, a non-citizens property transfer tax at 5% and a general property transfer tax at 10%.
Taxes on domestic goods and services include:

- a consumption tax on locally produced goods generally at 15% rising higher to 20 and 50% in the case of domestic appliances and alcoholic beverages respectively;

- a hotel accommodation tax ranging from US$2.00 to US$6.00 per guest night, a hotel guest tax at 6.5% on room rate, a hotel guest levy at 2% on room rate and a restaurant tax of 7% of sales. There is also a time-sharing occupancy tax of 5% and a time-sharing service tax of 5% of sale of time-sharing intervals;

- telecommunications tax at 20% of the cost of overseas calls;

- entertainment tax at 15% of ticket price;

- insurance premium tax at 3% of the premium value;

- gaming taxes including casino at $100,000 to $300,000 per annum and football and betting tax at 15% on overseas pools;

- a number of licenses for general business (with differentiated rates for citizens and non-citizens), banking and insurance, radio and television, telecommunications, tobacco and liquor, hotels, taverns and clubs and motor vehicles.

Taxes on international trade and transactions consisting of:

- import duties on the c.i.f. values of imported goods at rates generally varying from 5 to 35% but with higher rates on edible vegetables, fruits and spices, animal and vegetable fats, beverages and arms and ammunition;

- customs service charge at 5% of the c.i.f. value of all imports;

- consumption tax at rates varying from 10 to 50% with the highest rate applying to motor vehicles;

- export tax at specific rates per pound ranging from 4 cents on cotton exports and 10 cents and 50 cents on fish and lobster respectively;

- foreign currency tax at 1% of foreign currency purchases;

- travel tax at 10% of the ticket price;

- cruise ship passenger tax at $8.10 per passenger;

- embarkation tax at $25.00 for nationals and $51.00 for non-CARICOM nationals;

- stamp duty ranging from $1.00 to $30.00 on import documents.
There are significant variations in the application of taxes to domestic and non-resident incomes, goods and services. For instance, personal income tax at rates ranging from 2.5% to 55.0% is applied to incomes earned by non-residents, whereas incomes earned by residents are generally exempt. Similarly, as indicated above, property tax rates as applied to residents are lower than the rates applied to non-residents. Similar variation occurs in the application of embarkation tax on nationals and non-CARICOM persons. Such variations appear to be discriminatory and should be leveled within a general programme of tax reform and in conformity with MFN principles enshrined in the WTO.

More significantly, the high rate of customs service charge at 5.0% exceeds the permissible limit of cost recovery under the GATT protocol. The stamp duty on import documents also falls within this limitation. Steps should be taken to reduce the current rates within the permissible limit for cost recovery. In addition, foreign currency levy at 1.0%, although much reduced from previous levels, constitutes an additional imposition on imports and should be phased out or worked into adjusted tariffs and consumption taxes.

The incidence of taxes on tourism and tourism related services appear to be extensive. Altogether, hotel guests appear to be subject to at least three different taxes on accommodation and meals: accommodation tax (paid by the proprietor), a hotel guest tax and a hotel guest levy. Time-sharing owners and managing agents are liable for a time sharing occupancy tax and a time sharing service tax respectively. In addition, there is a general tax on restaurant sales. The accommodation tax is directly targeted at specific establishments with rates graduated to different categories or groups, while the guest tax and guest levy are impositions on guest expenditure for accommodation and meals. The multi-layered structure of the taxes appears to be susceptible to cascading, is unduly complex and should be simplified into a single sales tax or built into a general VAT that will be inclusive also of restaurant sales.

**Recent Tax Changes**

The most significant change during the review period was the introduction of an education levy to replace the tax on wages and salaries which had been abolished previously. The rates were set at 2.5% on wages and salaries above $6,500 and 5% on wages and salaries over $60,000. A 7% tax on restaurant tax was also introduced. At the same time the hotel guest tax was increased from 5 to 6.5%. The customs service charge was increased from 2.5 to 5% and the customs surcharge was abolished.

Recently, the departure tax applied to non-CARICOM citizens was increased from $25.00 to $51.00.
MEDIUM TERM ECONOMIC PROSPECTS

The medium-term economic prospects for Antigua & Barbuda depend heavily on developments in the tourism sector. Although robust growth and low inflation are projected for the major countries from which Antigua receives its tourists, viz. USA, UK and Canada and Euro 11, there are some significant concerns about the competitiveness of tourism product. In spite of unprecedented and uninterrupted growth in the US economy, Antigua has lost market share from that destination. This is also the largest segment of the market for Antigua & Barbuda and softness in that market is worrying. Antigua and Barbuda is a maturing destination and much of the tourism plant is slightly older than the emerging OECS destinations. The country would need to undertake significant investment in an effort to modernise the plant and add some freshness to the destination as done by Barbados and the Bahamas in recent years. This is in addition to enhanced marketing effort to maintain its position in the market

In addition, the government will need to undertake significant investment in infrastructure which has lagged in recent years, both in terms of maintenance and new developments. In particular roads, electricity and water would need to be improved. These efforts would be constrained by the continuing weaknesses in the public finances of the country which were exacerbated by the effects of adjustment after the hurricanes and the forgone revenue just prior to the 1999 elections.

FISCAL PROSPECTS

On the basis of current revenue and expenditure flows, the fiscal account will continue to be in imbalance unless remedial actions are taken to increase revenues and contain expenditure. Although the economy has achieved a satisfactory level of buoyancy, revenue response has been less than optimal mainly due to failure to collect taxes due and the generous concessions granted by government. Additionally, the allocation of a large part of revenue resources to administration puts a strain on government finances that have to be supported by increasing use of domestic commercial borrowing. Moreover, with the reduction of concessional flows, public sector investment demands increasing use of non-concessional financing which could set back the recent debt relief obtained from the restructuring of Antigua’s external debts.

The authorities are aware of this problem and have identified a number of initiatives that will help to stabilise the fiscal account. These include:

Revenue

• institution strengthening of the Inland Revenue – technical assistance is sought to improve the auditing capability and streamline processes within the department;

• institution strengthening of Customs to introduce the ASYCUDA system by 2000 and to intensify training of customs officials;

• review/redesign the property tax to substantially increase revenue yield;

• introduce a turnover levy on goods and services (mainly professional services).
Expenditure

- a UNDP programme for public sector reform with special emphasis on fiscal management that will introduce programme budgeting, upgrade the legal/management framework and design a funded scheme for pensions;

- reducing utility costs by rationalising their operations including privatisation of the generation activities of the water company, privatising new activities in electricity generation and upgrading telephone technology to reduce cost of operations.

To restore fiscal balance and eliminate debt payment arrears in the medium term, a number of policy issues will have to be addressed. A stronger tax effort will be required to mobilise increased revenue resources while maintaining control on recurrent spending so as to increase current account savings.

Antigua, like the other OECS countries, depends heavily on external flows of direct investment and has to balance the need to maintain tax/GDP ratios that support its competitive position for attracting foreign investment against the demand for providing basic services and social and economic infrastructure. Nevertheless, Antigua has the lowest revenue/GDP ratio among the other OECS countries at 24.8%, a ratio which is attractive by international tax comparisons.

However, given the low revenue buoyancy ratio at 0.8%, it appears that there is considerable room for maximising its revenue potential. Antigua has already taken an important step in establishing a tax compliance unit to audit the operations of the inland revenue and customs departments and has initiated requests for assistance to strengthen their organisation and skills and computerise their processes.

More fundamental changes will be required to induce voluntary compliance and improve tax efficiency. Although Antigua’s tax system appears to be less complicated than those of most other OECS countries, there is evidence of tax discrimination especially with regard to the income tax and property tax which suggests a bias against external transactions and non-resident labour, a condition which should be examined against the non-discriminatory principles of liberalisation of trade and international transactions. Furthermore the high incidence of exemptions and ad hoc concessions distorts the relative burden sharing among sectors and within sectors of the economy, provides opportunities to divert taxable income from the incidence of taxation, narrows the tax coverage and undermines the authority of tax administrators, especially in situations where recipients of tax incentives and concessions are not held accountable for benefits received. It is estimated that waiver of taxes on international trade in 1998 was equivalent to 8.0% of GDP or 36.6% of potential revenue yield in this revenue category. While much of this is related to reconstruction work after hurricane damage, the magnitude of the revenue loss in previous years (4.5% of GDP average during 1992 to 1994) requires a reevaluation of government’s tax incentive and exemptions policy.

The present tax system has evolved out of a bias towards import substitute goods producing sectors and the hotel sector. The increasing significance of diversification within a broader services sector has shifted the relative importance of the major sectors of the economy and
brought into question the appropriateness of present policies for providing fiscal support as a stimulant to balanced growth and expansion. An overall review of the tax system as it applies to the various sectors of the economy should be undertaken so as to improve tax efficiency and equity in burden sharing. At the same time, given the capacity of tax administrators to manage the number of tax handles presently employed, consideration should be given to reducing the number of taxes and charges, especially low yielding taxes and charges, to improve cost effectiveness and simplify the tax system. Fewer and broad based taxes with potential for maximum coverage of all sectors could prove far more efficient and cost effective than the present tax regime.

The rationalisation of user charges and the pricing of services both within central government and the rest of the public sector also offer scope for revenue enhancement. Within the central administration, the move towards programme and performance budgeting and computerised accounting should provide costing data and adequate management information to reformulate government’s policy for the pricing of goods and services provided to the public and between agencies. Public utility tariffs should also be reviewed to eliminate the need for transfers from government revenues.

While the ratio of recurrent expenditure to GDP is low as compared to other OECS countries, there appears to be scope to rationalise the allocation of revenue resources to the recurrent budget. Wages and salaries take up 56.7% of recurrent expenditure. At the same time the overall cost of administration accounted for nearly 40.0% of the recurrent expenditure budget as compared to 11.6% for education and 13.6% for health (1995 data). Government’s recruitment policy has been geared towards taking up the slack in employment creation as a means of maintaining social stability. However this strategy may be unsustainable in the face of growing government deficits and debt payment arrears which will have the effect of constraining adequate levels of public sector investments in necessary social and economic infrastructure. Public sector reform initiatives should focus on rationalising employment within the public service and improving the compensation and incentive package so as to attract and retain appropriate skills at management and mid-management levels. There are two elements of government’s pay policy that need to be addressed. The first concerns wage setting, in particular, relativities between government pay scales and those of suitable comparators in the private sector and the rest of the public sector. The second concerns the determination of annual wage adjustments in the process of regular wage negotiations. Both are important and should be done within a framework of acceptable and transparent indicators that will serve to guide the process of negotiations between government and representative unions.

Budget reform should also provide an opportunity to examine and prioritise government’s programmes and to identify activities which can be commercialised or divested. Agency services traded between departments should be made competitive or divested so as to save costs. In particular, the operations of loss making public enterprises should be reviewed so as to reduce costs, adjust tariffs and make them viable.

Tax reform coupled with more effective control of expenditure should help to stabilise the fiscal account in the short term, improve tax buoyancy and efficiency and set the economy on a path of sustained growth in public sector savings and investment. Such reform should be a pre-requisite
for moving towards the more demanding task of liberalising trade which should be done within a more favourable macro-economic framework in order to minimise its impact on sector competitiveness, prices and the fiscal account.

In addition to the need for fiscal reform, in the light of persistent budget deficits, the increasing use of commercial debt and rising exposure to currency risk, there is urgent need for an effective approach to external debt management. Such an approach must take into account a commitment to developing economic strategy programmes that recognise the need for debt contraction, the prioritisation of investment projects and the formulation of viable financing plans. This requires increased coordination among the key economic management units, particularly finance, planning and debt management, which are responsible for project evaluation and ranking, and financing negotiations. Additionally, increased attention should be paid to currency risk analysis and management when contracting non-US loans, especially with regard to currencies susceptible to volatile changes.

STATUS OF COMMON EXTERNAL TARIFFS

Antigua is still at Phase II of the programme to adjust to the common external tariff. Phase II was accomplished without significant loss of revenue or the need to take compensatory revenue measures. Antigua intends to move to the final phase during 2000. The revenue implications of this move are being studied and a report on the implementation of the final phase will soon be presented.

POLICY OBJECTIVES

The Government is committed to implementing policies that would enhance the role of the private sector as the engine of growth. The most recent Medium Term Economic Strategy Paper proposes the following goals and objectives:

(i) an economic growth of at least 6% per annum based on incentives to encourage private sector investment;

(ii) Central Government will improve its current deficit to a surplus to 2% of GDP

(iii) public sector investment will average 7% of GDP for the period 2000-2002

(iv) external arrears on public sector debts will be progressively eliminated by debt rescheduling; and

(v) additional revenue raising measures will be introduced, if necessary so that the fiscal stance could be maintained.
The policies to be pursued will be designed to:

(i) increase economic efficiency through improved resource allocation, the divestment of selected state-owned enterprises;

(ii) improve the external competitiveness of the economy through trade reform;

(iii) enhance the country's human resources as a key component of national development;

(iv) improve the efficiency of the social safety nets;

(v) safeguard the environment.

In the area of fiscal policy the major objectives are:

(i) improving the efficiency and effectiveness of tax collection, strengthening tax administration and eliminating discretionary tax exemptions;

(ii) reforming the property tax system by changing the base from rentable value to improved value;

(iii) conducting an O&M study to assist in the formulation of a public policy sector reform strategy aimed at rationalising skills and staff in the public service;

(iv) The provision of electricity and water by private sector operators using build, own, operate and transfer (BOOT) method of financing;

(v) Utilising the proceeds from privatisation of state-owned enterprises and from the sale of land to reduce public debt and to finance the PSIP.

SECTORAL STRATEGIES

The authorities in Antigua & Barbuda are focussing on four major areas for the development of the economy over the medium-term. These are tourism, offshore financial services, manufacturing and agriculture. The specific strategies for these sectors will be discussed under the appropriate sub heading. However there are some cross cutting issues that affect all four sectors that can be discussed at this point. These are related to economic infrastructure, social infrastructure and the environment. These are potential constraints to the development of the productive sectors and would need to be addressed if the country is to take advantage of the opportunities afforded by trade liberalisation.

ECONOMIC INFRASTRUCTURE

The road network of Antigua and Barbuda has deteriorated over several years. This process was further exacerbated by the passage of several hurricanes since 1995. The existing road network
will require extensive rehabilitation and upgrading to effectively service the productive sectors. This can be achieved by strengthening the capacity of the Ministry of Communications and works to undertake proper maintenance and/or the awarding of contracts to the private sector to improve the rate of progress. The latter will enhance the ability of the fledgling construction services sector to begin to become competitive.

The electricity company has had difficulty meeting peak load demand on a continuous basis. This has led to frequent load shedding and power outages. The government has experimented with a BOOT project for the generation of part of the electricity needs. This seems to be working satisfactorily and may be a viable option in the future once the financing can be negotiated on reasonable terms. In addition, it would be necessary to step up the maintenance of the distribution system to avoid leakage and low voltage, and regular maintenance of the generating plants owned by the APUA.

Antigua & Barbuda suffers from frequent water shortages especially in the dry season, which coincides with the tourist season. Much of the problem is a result of a poor distribution system which leads to significant amounts of leakage. This would require the replacement and upgrading of most of the distribution system. In addition it may be necessary to build another desalination plant. The capital cost of the rehabilitation of the water distribution system may be quite onerous in the context of weak public sector operations and the government may need to enter into partnership with the private sector to improve the service.

**SOCIAL INFRASTRUCTURE**

The development of human resources has been identified as a critical prerequisite for the improvement of the competitiveness of the economies. In addition, it is also a social service to the society and one of the more effective avenues for the redistribution of wealth. The output of the education system - both in terms of quantity and quality - is inadequate to build sustainable competitiveness. Hence much effort and finance would need to be expended to upgrade the quality of the education system. Antigua spends approximately 13% on education but most of it is on personnel emolument as much overstaffing occurs. Some of the resources would have to be shifted to provide material, which are necessary for a modern education system.

The provision of adequate level of primary health care at a reasonable cost is one of the major challenges of the authorities. It would require significant enhancement of the healthcare delivery system. This would involve improvement in both the management of the system and the physical infrastructure. The latter is being addressed by the construction of a new hospital through the BOOT method of financing. The finance and management of the healthcare system is being addressed via the reform of the medical benefits scheme and the creation of a statutory board to manage the hospital system. A comprehensive review of the health sector has also been undertaken.

**THE ENVIRONMENT**

Like most small island economies, Antigua and Barbuda must always be aware of the fragility of its ecosystem. This is particularly so since its major industry, tourism, is heavily dependent on
the preservation of the environment but at the same time can be heavily destructive of the environment. Thus greater attention has to be paid to environmental issues including protection of the fragile ecosystem, bio-diversity, environmental impact assessment and general environmental issues. It is possible to turn the emphasis on environmental issues into profitable opportunities for these economies.

The implementation of the World Bank Solid Waste project and the environmental levy for its finance, the passage of umbrella environmental legislation and coastal management in conjunction with the OECS Natural Resource Management Unit are positive steps being taken by the authorities to try to preserve the environment.

THE MANUFACTURING SECTOR

The Manufacturing sector in Antigua and Barbuda is in the early stages of development having only taken root in the early seventies. The fortunes of the sector were closely tied up with intra-CARICOM trade. Like intra-CARICOM trade. It went through a period of rapid growth during the seventies, peaked in 1983 and since then the sector has been relatively stagnant contributing on average of 3-4% of GDP. The sector consists mainly of light manufacturing and food processing. The major products include food and beverages, paints, furniture, household products mainly for domestic consumption and export to the regional market.

The manufacturing sector in Antigua can be broadly divided into two sub-sectors, the traditional import substitution and the agro-processing. They vary in their potential to be internationally competitive and their contribution to real output of the local economy. The import substitution sector which, produces assembly type products does not have much potential to be internationally competitive and its net contribution to the local economy is also small. The agro-processing sector has strong linkages with the agricultural sector and has the potential to be competitive in selected niche markets.

The agro-processing sector is characterised by home based family production and small processing employing 5 to 20 employees. The technology is characterised by varying degrees of sophistication, but in general there is little modernisation of equipment and facilities. The local raw material content ranges from 80% to 100%. Surplus agricultural output is the main component of local raw materials.

The import substitution manufacturing sector consists of paint and varnishes and household durables. It is characterised by a high import content in the production processes. Not only are capital goods imported but in some cases up to 100% of raw materials are imported from extra-regional sources. Production is geared mainly to the local and regional markets and very little is exported extra-regionally. World Bank (1990A) asserts that the sector is highly uncompetitive internationally and can only survive with excessively high amounts of effective protection. Moreover, they argue that this is compounded by industrial incentives which have a high anti-export bias. The granting of blanket duty-free import of inputs, untied to export performance only encourages inefficient production for the local market.
Most of the plants are built for the minimum efficiency scale of production and still operate with excess capacity as high as 60% to 70%. Regional trade and payments problems have pushed capacity utilisation to even much lower levels.

**Recent Performance of the Manufacturing Sector**

The manufacturing sector in Antigua and Barbuda exhibited considerable growth during the late 1970's and early 1980's. However, since then, production has declined in the face of higher wages due to the success of the tourism sector. All of the firms which produced garments under the 806/807 scheme have closed and some firms in the other sectors have also discontinued production. The contribution to GDP peaked at 6.29% in 1984 and has fluctuated just below 6% since then. In recent years there has been some growth in production which is related to increased local demand in the manufacture of furniture and construction materials.

**Constraints to the Development of Manufacturing**

The manufacturing sector in Antigua & Barbuda operates under several constraints. These include:

**Finance.** Although large firms have access to foreign finance or can attract local financing quite easily, indigenous firms face great difficulties in accessing finance. The commercial banks have a penchant for short term less risky lending and hence lend more for mercantile activities, rather than for manufacturing and agriculture. The percentage of loans to the personal and distributive sectors account for more than 60% of loans outstanding while the manufacturing sector receives less than 10%. Moreover indigenous firms do not have the requisite expertise in the conceptualisation of projects and presenting them to commercial banks as projects for financing. Neither do the commercial banks have the expertise to assist in this type of activity.

In addition, the high cost of finance in the face of high price elasticities of consumer demand, regional trade and payments problems, excess production capacity, primitive technology, deficient technical skills, unreliable transport and quality of raw materials all constrain the development of the sector.

**Technology and Technical Skills** are two other sources of concern. The rapid pace of technological development worldwide hastens the obsolescence of capital and erodes the competitiveness of less technologically dynamic countries. The high cost of upgrading capital and the inadequacy of technical capability to speed up the transfer and diffusion of technology retards the export competitiveness of the firms. Hence their inability to penetrate extra-regional markets and even its ability to hold on to domestic markets. The paucity of technical training results in wastage of raw materials, inadequate maintenance leading to loss of production during down times, and the need for foreign technical assistance to diagnose and solve some very simple problems.

**High Labour Costs.** Antigua and Barbuda is by no means a low wage area. Thus the type of manufacturing sector which emerges must take this as a given. The higher remuneration in the tourism sector has tended to attract workers away from manufacturing. Although the differential
between wages in the two sectors is not very large, in tourism, tips and other gratuities increase the earnings of workers in tourism.

**Inadequate Transportation Links.** The paucity and reliability of transportation links is another constraining factor. Sea transport is not only scarce but sometimes unreliable. In addition, the cost of sea transport is not significantly lower than air transport which is usually more reliable. Due to the relatively high value to volume of the products it produces, the enclave sector depends heavily on air transport to get raw materials in and the final product out. Even with superior air access, Antigua and Barbuda still suffers from a shortage dedicated cargo space resulting in delays and additional cost due to roundabout routing of final products.

**The Size of Firms and Local Market.** As mentioned earlier, most of the manufacturing firms in the country employ less than 20 employees. This limits the ability of the firms to reap economies of scale and spread overheads. Moreover the majority of indigenous firms are contented to produce for protected local markets which are extremely small. The markets are protected by the CARICOM CET and in some cases by Article 56 of the CARICOM treaty\(^1\).

**The Regulatory Framework for Businesses.** The regulatory and legal framework in which business operate may have impeded the development of the manufacturing sector. The process by which projects are approved is too long and circuitous. In addition, there is the perception that the process favours foreign investment over local investment. Some regulations and legal requirement tend to impede the flexibility of the firms.

**The Effects of Protection.** The protection accorded by the CET along with an incentive regime which treats production for the local market and production for export in the same way create an anti-export bias. There is no incentive to produce for the more competitive, more risky export market, while production for the protected local market is quite profitable. The reduction in the CET would tend to redress this bias to some extent but specific incentives have to be put in place to encourage production for export. However the regime of quantitative restrictions is being phased out via a process of tariffication which would initially increase the import duty. The incentives regime reflects the earlier inward looking policy of industrialisation and need to be given a thorough overhaul to reflect an external orientation.

**Fiscal Charges.** The size of the country and the inadequacy of transportation links already impose severe disadvantages on the countries in terms of their ability to compete internationally. Thus it is essential that no inordinate charges are imposed to prevent the firms from sourcing their inputs at international prices. Additional charges like high port charges impose further restrictions the ability of the firms to compete internationally. The consumption tax on inputs which is not rebated on export goods creates a disadvantage for Antiguan firms vis-à-vis their CARICOM counterparts whose exports are zero-rated under the VAT.

**Non-Tariff Barriers in Export Markets.** The existence of non-tariff barriers in the export markets especially the USA has tended to impede the growth of manufacturing exports.

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\(^1\) Article 56 allows the less developed CARICOM countries to impose quantitative restrictions and suspend origin treatment for goods of the more developed countries in an effort to develop the manufacturing sector in the less developed countries.
Antiguan exports face a myriad of regulations which only experience in the markets can help to get around. Many firms are seeking ISO and HASIP certification to facilitate entry into international markets. Although the greater transparency under the new WTO rules may have reduced the uncertainty of entry, many indigenous firms may be unable to finance the cost of the barrage of legal challenges which they may face in these markets.

**Knowledge of Export Markets.** The paucity of knowledge about export markets is another significant obstacle to export development. Basic information regarding the structure of markets, changes in taste, import regulations in the foreign country, appropriate technology, new processes, new products and potential competitors has to be assembled. Market intelligence is a costly exercise for the individual producer and there are also externalities associated with this activity. This suggests the need for co-ordinated action at the OECS level. The activities of Export Development and Agricultural Diversification Unit (EDADU) are aimed at reducing some of these difficulties, but the organisation remains largely under-funded and suffers from a lack of clear commitment and strategic focus. In addition tapping into international producer and market information networks would reduce significantly the cost of gathering market intelligence.

**Inadequate Infrastructure.** The inadequacy of economic and social infrastructure of the countries is a significant constraint on the development not only of manufacturing but all of the productive sectors. The inadequacy of the infrastructure translates into higher cost of utilities and in the case of electricity into downtime losses due to frequent interruption of power supply. It will be necessary to upgrade to a varying extent, the roads, electricity, water and waste disposal.

**TOURISM**

**RECENT ECONOMIC DEVELOPMENTS**

The economy of Antigua and Barbuda is dominated by developments in the tourism industry. The importance of the industry to the development of the country is underscored by the extent of government ownership of hotels and significant shareholding in a regional airline. During the early development of the industry the government felt constrained to investment in hotel development to serve as a catalyst to the industry. In recent years they have tried to divest some of their interest in hotels.

The Antiguan economy has been fully transformed into a service driven economy with an increasing penetration of services over the period 1986-98. Over the period 1986-89 the service penetration index was 13, declined to 11 during 1990-94 and increased to 25 over the period 1995-98.² Gross receipts from tourism averaged 70% of all foreign exchange inflows into the services account over the period 1986-96 (Table 1).

Over the period 1986-89 gross tourism receipts grew rapidly averaging 16.8% due to an average growth in stay-over visitor arrivals and cruise ship passengers of 5.6% to 165,128 and 23.7% to

² The services penetration index is derived as the ratio of service exports to merchandise goods exports.
185,235 respectively. By the early 1990s, gross tourism receipts fell, averaging 7.9% over the period (1990-94) reflecting the impact of a world wide recession on demand from major destinations and the effects of the passage of hurricane Hugo. During this period stay-over visitors grew on average by 6.2% to 203,196 while cruise ship passengers grew by 1.5% to 251,248. The sector suffered an additional supply shock during the 1995-98 period with the passage of hurricane Luis in 1995, consequently average tourism receipts declined to 2.9%. Average stay-over growth was –2.9% (an average of 201,760 passengers) due to the substantial damage to social and economic infrastructure while cruise ship passenger growth was 5.9% to 269,570 reflecting the minimal need for supporting infrastructure.

Stay-over visitors from the USA continued to have the largest market share of all visitor arrivals but this share has declined from 49.6% during 1986-89 to 31.8% over the period 1995-98. The United Kingdom (UK) has increased its market share over time from 12.8% in 1986-89 to 26.6% during 1995-98. The U.K. currently ranks second to the USA as the major source of stay-over visitors. The Caribbean region has lost its second place in market share to the U.K. and accounted for 19.0% of all visitors by 1998.

Antigua and Barbuda accounted for 34.0% of all stay-over arrivals into the Eastern Caribbean Currency Union (ECCU) in the 1980’s but this share was eroded in the 1990’s to approximately 28.0%. Its share of Caribbean stay-over visitor arrivals has also declined from 2.0% in the 1980’s to an average of 1.3% in the 1990’s. Cruise ship passenger shares in the ECCU followed a similar trend to those of stay-overs. These have declined from an average of 35.5% in the 1980’s to 25.5% in the 1990’s. These trends reflect a maturing of the tourism product and increased competition from other destinations.

**CONTRIBUTION TO GDP**

The role in the tourism industry in the economy as measured by the value added in the hotels and restaurants sector has averaged 15% of real GDP over the period 1986-96. This relative contribution to GDP has been fairly stable in the latter 1980’s, early 1990’s and during the post hurricane Luis period (1995-98). However real growth has been uneven averaging 0.21% during 1986-89, increasing to 8.2% during 1990-94 and declining to -3.3% during 1995-98. The reasons for the lower real GDP growth over the 1986-89 period despite an average stay-over growth of 5.6% were due to declines in visitors who stay for longer than a week. This category of visitors has a higher weight in the calculation of value added.

**ROLE OF FOREIGN DIRECT INVESTMENT**

Foreign direct investment flows into the economy have been linked primarily to the tourism industry and to the telecommunications sector to a lesser extent. These inflows averaged 11% during 1986-89 contributing to the expansion in the tourism plant. As the tourism product matured during the 1990’s these flows averaged 8.4% over the period 1990-94 and slowed to an average of 5.0% after 1995. FDI inflows are cyclical reflecting variability in the project completion cycle.

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3 This measure ignores linkages to transportation, communications, wholesale and retail, agriculture, government and banking services and utilities.
Antigua accounted for 31.4%, 18.9% and 12.0% of total foreign direct investment inflows into the ECCB area over the three sub-periods. These inflows were important in financing the savings investment gap over the period of analysis. As a per cent of GDP, foreign direct investment averaged 8.9% during 1986-89, 8.8% during 1990-94 and 11.0% during 1995-98. The composition of FDI also changed over the review period with equity inflows for hotel construction accounting for over 80% in the 1980’s but declining to approximately 30% of all inflows during the latter 1990’s. In addition to reflecting cyclical nature of flows these trends also suggest some maturity in the tourism product. FDI inflows are also closely linked to construction, transportation, architectural, telecommunications, management, real estate and financial services.

Re-invested earnings of hotels and of the major telecommunications provider increased from 10.5% of total inflows into the territory during 1986-89 to 21.1% during 1995-98. This increase reflected in part the need for rehabilitation of the hotel plant with the passage of hurricanes Luis and Marilyn as well as the general aging of the hotel infrastructure. Land sales associated with FDI flows averaged 7.2% of total inflows over 1986-89 to 17.0% during 1990-94 and increased to 19.0% over the 1995-98 period. The latter increased reflected the acquisition of lands associated with the Guiana Island project.

Trends in room capacity indicate initial growth in the number of rooms and beds in the 1980s during the establishment of the industry (Table 2). However this growth in capacity has slowed in the 1990’s due in part to the impact of hurricanes and the lack of substantial new investment in hotel plant.

**CONSTRAINTS TO TOURISM**

The major constraint to tourism development in Antigua and Barbuda is the low levels of marketing and promotion of the territory. The current subvention for this activity is approximately EC$500,000 and pales in comparison to financial resources provided to the Barbados Tourism Authority. The Antigua Hotel and Tourism Association conducts a large proportion of the marketing of the destination to travel and trade magazines. In addition, there needs to be a prompt response to negative news on the readiness of the destination in the aftermath of hurricanes. The recent establishment of the Tourism Development Corporation (TDC) to market all aspects of the product is laudable but ineffective if the perpetual fiscal imbalance prevents the allocation of a consistent and desired level of resources to the TDC. The existing 1% of revenue earmarked from the Hotel Guest Levy does not always accrue to the Department, which seriously impairs the execution of work programmes.

The degree of tax effort by the government of Antigua and Barbuda is also constrained by the multi-tiered nature of tourism taxes, which need to be simplified. The accommodation tax is based on four categories of property and on the number of guests and their length of stay. Both the hotel guest tax and the hotel guest levy are levied on room, food and drink at a rate of 6.5% and 2.5% respectively. This factor in addition to approximately 50.0% of the product being all-inclusive will limit the degree of resources collected from the sector, which could be used for promotional purposes. A related issue is the differential taxation of the cruise ship industry and its relative contribution to economic growth. The cruise ship industry currently derives
approximately 65.0% of its profits from the Caribbean as most activities are provided on ship with the exception of sightseeing. Some cruise lines purchase tours from local operators at discount and resell to passengers at a markup. It is noteworthy that the cruise liners are becoming larger with a capacity to provide most services onboard. In some cases existing berthing facilities are inadequate in accommodating the mega liners and warrant additional expansion. The cost benefit analysis of additional capital expenditure is warranted. A regional approach to the coordination of tourism policy is required in negotiations with Florida Cruise Ship Association.

Antigua and Barbuda can best be described as a mature destination with a considerably older hotel plant in comparison to the newer destinations. The degree of reinvestment in plant for upgrading and renewal has lagged considerably. The product has also evolved towards being predominantly all-inclusive and this has implications for the degree of value added in the sector and inter sectoral linkages. Labour laws also add a measure of inflexibility in improving productivity at the micro level. The cost of replacing unproductive workers are prohibitive and can impact the competitiveness of the industry.

Although the United States America (USA) continues to be the most important market for the destination, there has been a lack of airline seats from a number of major cities. The demise of Pan Am, Continental and Eastern airlines has constrained the opportunities for diversification of the product and the development of potential markets. Potential markets that have not been fully exploited include Canada, Europe, South America and some major cities in the USA. Dependence on one major carrier in bringing visitors to the region predisposes the economies to a number of risks. These include strikes, hegemony, and the vagaries of corporate strategies.

CONSTRUCTION

RECENT ECONOMIC DEVELOPMENTS

The construction sector accounted for an average of 11.3% of real GDP during the period 1986-89. During this period the major projects were related to hotel construction (Deep Bay Hotel), public sector investment, and private home construction. Major road works, the resurfacing of the airport and the construction of electricity and desalination plants were the significant public sector projects. The construction sector business cycle closely mirrors FDI flows into the tourism industry. In the 1980’s FDI inflows into the territory were used primarily for hotel construction. Consequently, real GDP growth during this period averaged 33.6%.

Although the construction sector continued to contribute on average of 10.9% of real GDP during 1990-94, real average growth was -1.4% reflecting the completion of major projects that commenced in the latter 1980’s. Nevertheless, tourism related construction activity continued in the Hodges Bay and Jolly Harbour but a slow rate of implementation. Lower levels of public sector investment and fall in residential construction also contributed to the reduced growth. The fall in residential construction reflected a fall in business and consumer confidence.
During 1995-98 the sector contributed 12.0% to real GDP while real growth averaged 9.0%. The sector received a boost in rehabilitation and repair work in the aftermath of hurricanes Luis, Marilyn and Georges. Residential and commercial construction was particularly high during this period. A number of housing projects were implemented during this period and were facilitated by commercial bank lending.

TRANSPORTATION

RECENT ECONOMIC DEVELOPMENTS

The transportation sector like construction is also closely linked to developments in tourism. Air transportation and road transportation account for approximately 90.0% of all value added in this sector. This sector contributed on average 12.0% of real GDP during 1986-89 while real growth averaged 10.7% during the review period. Its share to real GDP rose to 12.4% of real GDP during 1990-94 but at a lower level of real growth of 3.3%. This lower growth reflected recession in most major tourism markets in the early 1990’s and lower public sector investment in roads. Although the sector maintained its relative contribution to GDP during 1995-98 at 11.8%, real growth declined to 1.6%. The lower growth rate reflected a decline in stay-over passengers arising from the passage of major hurricanes as well as lower levels of public sector investment.

CONSTRAINTS

Value added in the transportation sector hinges on the development of a multi-year public sector investment programme to place the territory on a sustainable development path. In view of the existing fiscal imbalances, the capital programme in particular road works and improvements to the airport, are the first to be cut in bringing closure to the savings-investment gap. Given the close links to tourism it is critical that the supporting infrastructure does not deteriorate to a level that does not complement private sector investment.

COMMUNICATIONS

The liberalisation of basic telecommunications under the General Agreement on Trade in Services (GATS) signed in 1997 has unleashed a wave of competitive pressures which has resulted in a spate of international mergers, as formerly protected national telecommunications companies scramble to position themselves to be players in the global market. No doubt this development has forced the monopoly provider of telecommunications services in the Organisation of Eastern Caribbean States (OECS) countries to soften its stance and agree to renegotiate its contract with five of the independent OECS countries. Many of these contracts date well into the new millennium.

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4 Five of the independent OECS countries are involved in a World Bank financed project to reform the telecommunications industry. The five countries are Dominica, Grenada, St Kitts-Nevis, St Lucia and St Vincent and the Grenadines.
At the same time, technological advances in the telecommunications industry is threatening to create a glut of bandwidth internationally that would force the price of telecommunications services to near zero levels. These advances are taking place at all three critical points in telecommunications networks, i.e., international/long distance carrying capacity, switching gear and the local loop. Cost reduction in the local loop is critical for 75.0% to 80.0% of the cost of a call consists of the cost of the link in the last couple of miles. About two thirds of the assets of telephone companies is invested in this segment hence making them a candidate for natural monopolies.

**Recent Performance**

The communications sector has grown consistently over the 1980’s and 1990’s and has increased its relative contribution to real GDP. During the period 1986-89 the sector accounted for 5.4% of real GDP and grew in real terms by 15.0%. Its relative share to real GDP increased to 7.0% during 1990-94 and grew by 9.0%. By 1995-98 its relative share to real GDP increased further to 9.3% and grew by 8.5%. The number of telephone lines per 100 inhabitants averaged 40.8 in 1997 far above the middle income country average of 14.4% but below the upper income country average of 54.7 during the same period.

Over the period 1977 to 1998, the percentage contribution of the communications sector in the OECS (of which telecommunications is the largest sub-sector) ranged from 2.8% at the beginning of the period to 9.6% at the end of the period. Over the years, the sector’s contribution to GDP has been growing at a steady rate, largely reflecting the impact of an improved telecommunications sector. The liberalisation of the sector is expected to lead to a reduction in the cost of telecommunications services, thereby fostering an improvement in the linkages between other vital sectors in the economy.

Antigua and Barbuda like the other OECS countries which has a comparative advantage in the provision of services. The information infrastructure is the pillar on which many of these services are delivered. Therefore, the fall in the cost of international and regional communications which liberalisation of the telecommunications sector is expected to achieve, will in fact increase the potential for trade in services and consequently improve the region’s value of services produced. As was mentioned earlier, expansion in areas such as the informatics industry would have a positive impact on the region’s Gross Domestic Product.
FINANCIAL SERVICES

OFFSHORE FINANCIAL SERVICES

The term Offshore Financial Services refers to a variety of activities which take place between corporations registered in a country with residents in the rest of the world with little interaction with domestic residents. It is rather limiting as offshore financial services does not accurately describe the range of activities undertaken in these centres and may also limit the scope of opportunities considered when one is trying to visualise the future development of the industry. A more accurate descriptor would be International Business Facilitation Centres. Not only does this nomenclature cover the wide range of services provided by the offshore sector, it also makes for a much neater classification of the activities and would ultimately assists in resolving some of the ticklish regulatory issues, since different types of activities do not necessarily need the same level of regulation.

The offshore sector was developed to provide services which are normally provided in the domestic economy at lower cost or under a less demanding regulatory environment. Thus, all of the activities which take place in the offshore sector have counterparts in the domestic economy and it is quite natural that any such classification would be equally applicable to the offshore sector. The International Monetary Fund along with the other international institutions has recently revised its classification of financial institutions and this framework can be useful in the development of a taxonomy of International Business Facilitation Services (IBFS).

The IMF Classification divides corporations/enterprises into five mutually exclusive sectors, Households, General Government, Financial Corporations, Non-financial corporations and Non-profit institutions. IBFS are concerned with Financial Corporations and Non-financial Corporations and the bulk of the activity is concerned with the former.

The offshore Services Sector in the OECS territories is currently at varying stages of development ranging from Antigua and Barbuda which is the most established, dating back to 1982 and St. Lucia where the legislation was passed in 1999. The oldest offshore centre is St. Vincent and the Grenadines which had offshore banking and ship registry legislation enacted in 1976. However the activities, promoted by the St. Vincent Trust Authority Limited based in Liechtenstein have not really taken off. The legislation was modernised in 1996 to give the sector a new lease on life. The most dynamic centres are Nevis and Anguilla which have recently passed modern legislation creating fiscal consumer products which are on the leading edge of the industry.

The legislation of most of the OECS countries is patterned on that of the British Virgin Islands which is reputed to be one of the most successful emerging offshore financial services centres. The sector is usually exempt from all forms of corporation taxes in the jurisdiction of incorporation. These include income taxes, corporate taxes, capital gains taxes, inheritance taxes, withholding tax, other indirect taxes levied on international business activity. Offshore activities are also exempt from indirect taxes such as stamp duties and customs duties. Government revenue from these activities is generated by modest licence fees. A variety of products are offered but countries seem to be operating in specific niches.
Several opportunities exist for the countries in the ECCB jurisdiction to develop offshore financial centres. The opportunities can be discussed under seven broad categories:

**Tax Advantages** - Individuals of high net worth and multinational corporations are attracted to offshore jurisdictions because of the many tax advantages they offer. These jurisdictions offer legitimate deferral, reduction or avoidance of taxes on certain profits earned abroad. Most of the OECS countries have chosen to be no tax jurisdictions. This factor makes them attractive to external investors as possible tax havens. However, this non-tax situation may make these offshore jurisdictions reluctant to enter into bilateral double taxation agreements with other nations because the initial benefits are not always apparent. These bilateral agreements do however have certain distinct advantages for the developing financial services provider jurisdictions. Some of the benefits may be that the home country provides the developing host offshore jurisdiction with avenues for resolving disputes, procedures for exchanging information regarding drug abuse and other illegal activities, favourable tax treatments for residents or companies organised under signatory laws.

**Product Development** - Offshore financial product and laws can be viewed as fiscal consumer goods. The range of legal products offered can be as broad as the jurisdiction so desires and spans the fields of banking, brokerage and other "traditional" financial services, immigration and nationality, manufacturing and general law services. Emerging jurisdictions are advised that the more readable, and understandable the laws, the more saleable is the jurisdiction. Putting the appropriate legislation in place is a therefore a necessary, albeit not sufficient, condition for the development of the offshore sector. Jurisdictions have to be vigilant to ensure that their legal products always remain on the leading edge of the industry.

**Niche Positioning** - Since it may not be possible or advisable for an emerging centre to simultaneously develop the full range of financial services to the same degree, countries should seek to develop niches and therefore position themselves and gain an international advantage. In the development of a niche profile countries should seek to render quick, efficient and professional service, and be innovative in meeting the needs of a niche clientele in a changing and dynamic environment. It is advisable for emerging centres to develop niches and to seek to gain an international advantage in a particular segment of the market. This strategy may, however, prove difficult to pursue given that other more established and resourceful jurisdictions are competing to diversify into new and different products.

**Marketing and Promotion** - A continuous marketing and public relations programme is necessary to support the legislation in place.

**Private-public Sector Co-operation** - Other successful Caribbean jurisdictions have identified the need to have co-operation between the private sector professionals and government officials.

**Communications Technology** - Private banking and other financial services increasingly utilise high technology communications systems and electronic payments systems, which offer opportunities for emerging centres to compete globally. Moreover an offshore jurisdiction cannot compete effectively if it does not offer twenty-four hour online searches and registration.
Supervisory and Regulatory System - Those jurisdictions with effective systems for supervision are increasingly the choice of reputable institutions and individuals. The threats of money laundering and other illegal activities require that countries put in place a competent and efficient regulatory system.

Among the major challenges facing the offshore industry in the OECS are the following:

Limited Professional Expertise - To attract desirable investors OECS countries must have in place an infrastructure accompanied by highly trained professional accountants, bankers, taxation specialists and legal experts.

Telecommunications and Air Transportation - The cost of telecommunication service in the region is generally regarded as high and in some cases prohibitive. The irregularity or unavailability of international flights also inhibits efficient travel services.

Regulation and Supervision - Unregulated or inadequately regulated financial services centres pose a threat to global financial stability. Hence the need for new regulatory standards for their operation. The new regulatory standards will constrain growth of new centres due to increased financial and human resources requirements. At the same time the need for a good reputation should ensure that laxity in regulation frameworks is not encouraged.

Financial Liberalisation in Developed Markets - In the 1980's many of the regulations which encouraged institutions to move offshore were dismantled as developed countries have liberalised and deregulated their economies. New threats are always emerging from the anti-tax haven posture of the U.S Government and new laws are being continuously passed which serve to restrict the development of offshore centres. The recent threat by the OECD countries on harmful tax competition follows in this same vein. Such challenges are likely to increase in the future. It is therefore incumbent on newly-emerging offshore centre like the OECS countries to maintain the highest standard of regulation and propriety.

In spite of these constraints the offshore sector provides significant opportunities for economic diversification. The global offshore sector is growing at a rapid pace propelled by the growth in the World's economic wealth. Countries embarking on this path however need to remain cognisant of the many responsibilities they face to uphold the integrity of the financial system.

Offshore Financial Services in Antigua and Barbuda

The International Business Corporation Act of 1982 governs the offshore financial services sector. The Act permits the incorporation of four types of institutions such as general international business corporations (IBC), offshore banks, offshore insurance corporations and offshore trusts. The Act also facilitates the establishment of offshore Internet gaming companies. By end 1997 there were 10,900 registered IBCs, 53 offshore banks of which 48 were in good standing. Nine of the offshore banks had a physical presence and in some instances were affiliated with a domestic commercial bank. This sub-sector of the banking system has the potential for generating increased revenues for government. Central government revenues derived from the offshore financial sector was $6.7m and $5.2m in 1997 and 1998 respectively.
In 1997 revenues from the offshore financial sector represented 14.4% of non-tax revenue or 2.0% of current revenue. In 1998 there was a flight to quality and these proportions declined to 10.5% and 1.5% respectively as revenue declined to $3.5m and $2.9m. The Authorities in Antigua and Barbuda have taken several steps to reform the operations of the offshore sector to accord with international best practice. The legislation has been amended to strengthen the anti-money laundering provisions and the regulation of the sector has been brought under the Offshore Financial Services Authority – a statutory corporation that now receives the revenue that formerly went into the consolidated fund. The sector has some potential to contribute to the diversification of the economy if the threats discussed earlier can be addressed.

<table>
<thead>
<tr>
<th>Antigua and Barbuda</th>
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<tbody>
<tr>
<td>Government Revenue from Offshore Financial Services</td>
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<tr>
<td>EC$ ‘000</td>
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<td>Economic Citizenship</td>
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Source: Offshore Financial Services Authority
## Antigua & Barbuda
### Structure of the Financial System

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</table>

*Most recent data (December 1994 - December 1999)
**36 companies were registered, at reporting date only 20 companies were active.
ºData reported for two institutions of which one is not a deposit taker.
±Data reported for one institution only.

## Offshore Companies

<table>
<thead>
<tr>
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<th>Number</th>
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</thead>
<tbody>
<tr>
<td>Banks</td>
<td>27</td>
</tr>
<tr>
<td>Insurance</td>
<td>6</td>
</tr>
<tr>
<td>Trusts</td>
<td>-</td>
</tr>
<tr>
<td>IBC's</td>
<td>2595</td>
</tr>
<tr>
<td>Exempt Companies</td>
<td>-</td>
</tr>
<tr>
<td>Internet Gaming</td>
<td>-</td>
</tr>
<tr>
<td>Economic Citizens</td>
<td>-</td>
</tr>
<tr>
<td>Registered Agents</td>
<td>-</td>
</tr>
<tr>
<td>Limited Liability Companies</td>
<td>-</td>
</tr>
</tbody>
</table>
BANKING SECTOR

The banking sector has played a critical role in the development of the economy. Assets of the banking system have grown from $657.9m during 1986-89 to $1,564.5m in 1995-98. Its contribution to real GDP has increased from 4.7% during 1986-89, to 6.0% during 1990-94 and to 8.2% during 1995-98. The corresponding real growth rates for the respective periods were 13.9%, 5.7% and 16.7%. The expansion in the banking system is also linked to the FDI inflows into the economy as well as the increasing role of offshore financial services.

Domestic credit grew on average by 20.3% to $459.1m during 1986-89 reflecting growth in credit to the private sector (21.1%), and Central Government (13.6%). The other public sector was a net depositor to the banking system. Monetary liabilities (M2) on average grew at a faster rate than domestic credit (21.4%) to $435.93. Within M2, narrow money (M1) grew on average by 24.8% to $104.5m while quasi money grew by 34.1% to $331.4m. Savings, time and foreign currency deposits grew by 29.1%, 14.3% and 9.8% respectively. Liquidity conditions within the banking system as measured by the loans to deposit ratio were on average 62.1% during this period. This increased liquidity was reflected in the accumulation of net foreign assets of the banking system which grew on average by 48.3% to $12.6m.

Growth in domestic credit slowed to 4.2% during 1990-94 reflecting a general tightening in liquidity conditions. The economy also experienced slower growth due to the combination of the impact of hurricane Hugo in 1989 and a global recession in the early 1990’s. Net credit to Central Government slowed to 4.3%, while that to other public sector and to the private sector grew by 30.9% and 5.8% respectively. The other public sector, which includes social security schemes, continued to be a net depositor to the banking system. Total monetary liabilities also grew at a slower pace of 8.4% to $693.6m. Both categories of narrow money M1 and Quasi money grew on average by 8.4% and 12.5% respectively. The accumulation of net foreign assets during this period reflected reinsurance inflows associated with claims after the passage of hurricane Hugo.

By 1995-98 domestic credit expanded on average by 15.3% to $1,029.9m. The private sector and Central Government absorbed this expansion in credit. These sectors experienced growth in credit of 15.3% and 15.9% respectively. The increased credit to Central Government reflected the structural savings-investment imbalance arising from inefficiencies in tax efficiency and administration and unrestrained expenditures. The growth in credit to the private sector pertained to reconstruction and rehabilitation of housing infrastructure in the aftermath of the passage of hurricanes Luis and Marylyn. The average growth in net foreign assets of 10.9% reflected inflows of reinsurance claims after the passage of hurricanes Luis and Marylyn.

OPPORTUNITIES AND CONSTRAINTS

The banking system has the potential to provide new financial products within an increasingly liberalised environment. The development of money and capital markets in the currency union also provides the opportunity for banks, accounting and law firms to act as broker intermediaries. The challenges to the regulator pertain to the issue of principal agent as the government has the authority to issue a banking license while the proposed Securities Exchange Commission (SEC)
will regulate the intermediary function. In order to encourage participation in and the orderly development of the capital market in the interim, the regulator may have to waive the establishment of a subsidiary to conduct the intermediary function. Alternatively, the minimum capital requirements could be established in line with existing benchmarks for the purposes of eligibility to trade with an additional net capital requirement for the purposes of trading. In this way the credit and other risks are based on the volume of trading activity.

The banking system is currently characterised by wide spreads that either reflect the cost of providing services and the pricing of risk and/or the pursuit of rent seeking behaviour. Interest rate spreads in Antigua and Barbuda ranged from between 6.8 to 8.3% over the period 1991-96 compared with a range of 6.6 to 8.2% in the ECCB area. A recent study by Randall (1998) suggested short run scale diseconomies in commercial banking in the ECCB area as a whole. The study also found that 53.0% of the spread was attributable to operating costs, 6.0% for reserve requirements and 41.0% for the implied return on equity.

Growth in the offshore financial sector will be constrained to the extent that developed countries particularly members of the OECD stifle the degree of international tax arbitrage. The issue of harmful taxation as articulated by the OECD will bring pressure to bear on the flight of capital to Offshore Financial Centres (OFCs). Increased regulation and supervision of OFCs will erode some of the comparative advantages that ensue from competitive legislation and the degree of disclosure. The conflict arising from the Ministry of Finance both promoting and regulating the offshore sector culminated in adverse publicity surrounding allegations of impropriety by several offshore banks. Weak supervision arises from inadequate human resources to police the sector.

**STATUS OF COMMON EXTERNAL TARIFFS**

As part of the regional integration movement and towards the structural adjustment of the economies of the CARICOM countries, a common external tariff was adopted for implementation in 1991. The tariff was later reviewed in the light of developments in the international economic environment with greater emphasis on trade liberalisation and competitiveness as well as the formulation and expansion of regional economic groupings. A number of factors were taken into account in formulating policies for the new tariff structures:

- differences in the levels of development of member states;
- differences in their industrial structures;
- their respective exchange rate regimes;
- the nature of their fiscal regimes;
- their respective administrative capabilities.
Factors that determined the principles guiding the design of the new tariff included:

i. international competitiveness;
ii. efficient production for the regional market;
iii. the preservation of government revenue;
iv. controlling inflation so as not to increase the price of basic foods and social services;
v. duty exemptions regime should be reduced/removed so as to foster uniform treatment of production inputs across the common market;
vi. uniform rates for the same items notwithstanding their economic use;
vii. the special needs of the LDCs;
viii. the need for simplification of the tariff structure with fewer bands and less room for discretionary application.

The phasing of the implementation of the new common external tariff for the OECS was as follows:

<table>
<thead>
<tr>
<th>Period</th>
<th>Rate Range</th>
</tr>
</thead>
<tbody>
<tr>
<td>January – June, 1993</td>
<td>0 – 5% to 30/35%</td>
</tr>
<tr>
<td>January – June, 1995</td>
<td>0 – 5% to 25/30%</td>
</tr>
<tr>
<td>January – June, 1997</td>
<td>0 – 5% to 20/25%</td>
</tr>
<tr>
<td>January – June, 1998</td>
<td>0 – 5% to 20%</td>
</tr>
</tbody>
</table>

Antigua is still at Phase II of the programme. Phase II was accomplished without significant loss of revenue or the need to take compensatory revenue measures. Antigua intends to move to the final phase during 2000. The revenue implications of this move are being studied and a report on the implementation of the final phase will soon be presented.

**TRADE LIBERALISATION NEGOTIATIONS (FTAA & WTO)**

Antigua is to conduct negotiations on trade liberalisation through the Regional Negotiating Machinery established by CARICOM to represent the interests of the region at the WTO and the FTAA. Tariff adjustments towards the implementation of the CET has not had any significant impact on the revenue up to Phase II of the implementation schedule. It is expected that any loss arising from the full implementation up to Phase IV will be compensated for by improved collection of existing taxes and by increased revenue deriving from a restructuring of the property tax.

Trade liberalisation on a global scale, however, is of much greater significance as far as Antigua’s fiscal situation is concerned. There are a number of factors which should be taken into account:

- the importance of import duties to Antigua’s revenue (15.7% of total revenue in 1998);
- the inefficiency of the current fiscal regime to respond adequately to changes in external conditions;
- the market structure of import trade and the absence of effective price competition.
• Possible contraction in the economy arising from negative sector response to external competition which would have an impact on revenue generating capacity.

As mentioned above the revenue potential of the economy is hindered by inefficiencies in the fiscal regime. The tax burden is disproportionately distributed among sectors and within sectors. Incentives, exemptions and ad hoc concessions as well as undervaluation of imports cause considerable leakages of revenue resulting in low tax buoyancy and elasticity. Tax and tariff adjustments are not always passed on to consumers thus restraining elasticity responses to price changes. Although direct tax increases may occur from windfall profits, reduced demand for taxable goods are likely to result in a net loss of revenue. Additionally, tariff reductions will reduce the competitive advantage of domestic production, with possible contraction of the economy and with consequential decline in revenue yields. Complementary adjustments in exchange rates to readjust prices, in a situation where both import substitute goods and hotel services have a high import content, may have only marginal effect that will continue to favour imports.

On the fiscal side two complementary approaches are required to make the process of trade liberalisation successful:

1. A comprehensive fiscal reform including tax and budget reform to strengthen the fiscal structure to better withstand the impact of tariff changes.

2. A phased approach towards the elimination of tariffs so as to minimise disruptions to revenue flow.

SIMULATIONS OF A REDUCTION IN TRADE TAXES

This section proposes to analyse the impact on the fiscal accounts, the sequential reduction in tariff rates based on trade liberalisation. The basis of the exercise is premised on a given set savings investment balance of the economies in question. By how much would indirect taxes have to increase in order to maintain this balance. The adjustment is therefore entirely fiscal and consistent with the economic foundations of the Eastern Caribbean Central Bank Currency Union. Given the limits placed on the degree of Central Government borrowing from the monetary authorities, there is a binding constraint on governments’ ability to monetise their deficits. This adjustment is further reinforced by the choice of nominal anchor whereby the exchange rate is pegged at a fixed rate to the United States dollar. Given our degree of openness the economies of the Currency Union have been heavily dependent on taxes on international trade and transactions as a major source of revenue. This degree of dependence increases the vulnerability of the economies to shocks arising from increased trade liberalisation. The likely establishment of Regional Economic Partnership Arrangements (REPAs) under the new Lomé 5 protocol and accession to the Free Trade Area of the Americas (FTAA) will alter tariff rates among the membership in these regional trading blocks.

Member countries of the Currency Union therefore must take a proactive and anticipatory stance in mitigating the costs of adjustment arising during the transitional period.
The One Country, Two Sector, Three Good (123) Model

This model refers to one country with two producing sectors and three goods. The sectors are the traded and non traded goods sectors while the goods produced are the export good, a domestic good and an import good. The three agents involved in the model are a producer, a household and the rest of the world. There are a total of twenty equations and two accounting identities. Five equations describe the underlying relationships that generate real flows. Six explain price relationships. Four describe nominal flows while the remainder describe equilibrium or market clearing conditions. These market clearing conditions state that supply must equal demand and that the balance of trade constraint must be satisfied. The model does not assume that all tradables are perfect substitutes with domestic goods. The model is static and does not yield a dynamic solution but a one period result based on the type of shock that is selected.

Simulations

The simulations were based on a 25.0%, 50.0% and 100.0% reduction of import tariff rates in the face of increasing trade liberalisation. The method of adjustment assumed was internal based on a change in the tax regime. It was assumed that given the reliance on trade taxes for most revenue that indirect tax rates would have to change in order to maintain the existing savings investment balance. The indirect taxes could take the form of a sales tax or some other form of indirect tax on consumption. The baseline year chosen was 1998.

Antigua and Barbuda

Antigua and Barbuda has depended heavily on trade taxes for 53.0% of its revenues during the 1980’s. The degree of dependence increased to 55.7% during the 1990’s. This category of taxes accounted for 11.7% of GDP in both the 1980s and the 1990’s. The elasticity associated with current revenue was elastic during the 1980s at 1.15 while that for trade taxes was 1.07. During the 1990’s the revenue elasticity was approximately unity at 0.99. The trade tax elasticity however increased over the previous period to 1.09. This reflected greater efforts at collection on the part of the authorities during the latter part of the 1990’s with the establishment of a Tax Compliance Unit.

Antigua and Barbuda Revenue and Trade Tax Elasticities

<table>
<thead>
<tr>
<th></th>
<th>1980-98</th>
<th>1980’s</th>
<th>1990’s</th>
</tr>
</thead>
<tbody>
<tr>
<td>Revenue</td>
<td>1.04</td>
<td>1.15</td>
<td>1.00</td>
</tr>
<tr>
<td>Trade Tax</td>
<td>1.03</td>
<td>1.07</td>
<td>1.1</td>
</tr>
</tbody>
</table>
The simulation conducted explored the fiscal revenue implications of a 25%, 50.0% and a 100.0% reduction in the import tariff rate arising from trade liberalisation. The question that arises is by how much will domestic indirect taxes need to be raised in order to keep the current account from deteriorating while keeping the same level of productive investment in the economy. The average tariff rate was 17.3% based on the ratio of taxes on international trade and transactions to imports of goods. For a 25% reduction in the tariff rate indirect domestic taxes would have to be raised to 2.0% of GDP. At a 50.0% reduction these taxes would have to be raised to 6.0% of GDP and at full liberalisation 11.7% of GDP. These indirect taxes would take the form of a sales tax or value added tax.

### Antigua and Barbuda Simulations

<table>
<thead>
<tr>
<th>Tariff Rate</th>
<th>Indirect Tax Rate Per Cent GDP</th>
</tr>
</thead>
<tbody>
<tr>
<td>25% reduction in Import Tariff</td>
<td>2.0</td>
</tr>
<tr>
<td>50% reduction in Import Tariff</td>
<td>6.0</td>
</tr>
<tr>
<td>100% reduction in Import Tariff</td>
<td>11.7</td>
</tr>
</tbody>
</table>

### Table 1: Antigua and Barbuda Base Line Indicators

<table>
<thead>
<tr>
<th>1998 Baseline</th>
<th>EC$M</th>
<th>Per cent GDP</th>
</tr>
</thead>
<tbody>
<tr>
<td>GDP Market Prices</td>
<td>1680.00</td>
<td></td>
</tr>
<tr>
<td>Consumption</td>
<td>1315.81</td>
<td>78.32</td>
</tr>
<tr>
<td>Private</td>
<td>961.83</td>
<td>57.25</td>
</tr>
<tr>
<td>Public</td>
<td>353.98</td>
<td>21.07</td>
</tr>
<tr>
<td>Domestic Savings</td>
<td>364.19</td>
<td>21.68</td>
</tr>
<tr>
<td>Investment</td>
<td>720.64</td>
<td>42.90</td>
</tr>
<tr>
<td>Imports of Goods</td>
<td>1139.4</td>
<td>67.82</td>
</tr>
<tr>
<td>Exports of Goods</td>
<td>110.62</td>
<td>6.58</td>
</tr>
<tr>
<td>Foreign Saving</td>
<td>262.6</td>
<td>15.63</td>
</tr>
<tr>
<td>Av. Tariff Rate /1</td>
<td>0.173</td>
<td></td>
</tr>
<tr>
<td>Current Revenue</td>
<td>342.3</td>
<td>20.38</td>
</tr>
<tr>
<td>Trade Taxes</td>
<td>197.1</td>
<td>11.73</td>
</tr>
<tr>
<td>Current Expenditure</td>
<td>363.98</td>
<td>21.67</td>
</tr>
<tr>
<td>Current Account Balance /2</td>
<td>-6.01</td>
<td>-0.36</td>
</tr>
<tr>
<td>Overall Balance</td>
<td>-52.81</td>
<td>-3.14</td>
</tr>
</tbody>
</table>

1/Defined as the ratio of Trade Taxes to Imports of Goods
2/ Denotes Current Account After Grants
LIBERALISATION OF TRADE IN SERVICES

Antigua and Barbuda's international obligations for the liberalisation of trade in services are related to its commitments under the GATS and Protocol II amending the CARICOM treaty. The commitments under Protocol II represent advancement on the GATS hence this section begins with a discussion of the GATS.

COMMITMENTS UNDER GATS AND TRADING ARRANGEMENTS

The general objective of the GATS is to develop a set of rules that would foster increased transparency, consistency, certainty and non-discriminatory norms and regulations in the governance of trade in services. The services not covered by the agreement pertain to transportation and airline services. With regards to modes of supply four specific mechanisms apply as follows:
1. Cross border supply;
2. Consumption abroad;
3. Commercial presence; and

The Most Favoured Nation (MFN) principle under the GATS dictates that trading partners whether with the Free Trade Area of the Americas (FTAA) or the Regional Economic Partnership Agreements (REPA) of the EU. Albeit temporary exemptions may be allowed for transitional purposes. The principle of National Treatment dictates that once a foreign entity supplies a service to WTO member country then there should be no discrimination between this entity and a local one.

Antigua and Barbuda has made commitments under GATS for the following services:
1. Business services, specifically professional services, computed and related services, and research and developmental services;
2. Financial services, specifically insurance and insurance related services;
3. Tourism and tourism related services;
4. Recreational, cultural and sporting services; and
5. Transport services.

In the above five areas limitations to market access pertaining to horizontal commitments are specific to commercial presence and presence of natural persons. In the case of commercial presence, joint ventures are encouraged with prior approval from the authorities. However 100% foreign ownership is permitted. With respect to movement of natural persons every person who is not a national of Antigua and Barbuda is required to obtain a valid work permit if employment is sought in the territory. For all practical purposes Antigua and Barbuda has one of the most liberalised labour markets in the Eastern Caribbean and up to 30% of the labour force is comprised of non-nationals. For those services that are included in Antigua and Barbuda’s offers, the obligations of MFN and transparency would apply.
Professional Services

Legal, accounting, computer, research and development taxation, engineering and medical services have no restrictions with respect to cross-border supply and consumption abroad. With regards national treatment there are no restrictions related to cross-border supply and consumption abroad. Restrictions pertaining to commercial presence are treated under the respective Acts that govern the particular service, e.g. Business or Architect Act.

Financial Services

Commitments under financial services are specific to insurance and insurance related services. There are no limitations to market access or national treatment other than those articulated in the Insurance Act.

Tourism and Tourism Related Services

As in the case of professional and financial services there are no limitations to market access and national treatment other than those enshrined within the Hotel Proprietors Act. These services are heavily dependent on FDI flows and so are already at fairly high degree of liberalisation. The incentive regime provided under the Fiscal Incentives and Hotels Aid Acts are designed to facilitate these inflows without undue restriction.

Recreational and Sporting Services/Transport Services

There are not restriction on market access or national treatment other than those guiding provisions under the Business Act and the Merchant and Shipping Act.

Direction of Trade

Antigua and Barbuda is a net exporter of tourism and financial services to both the EU and the USA. These two sectors offer the greatest opportunity for growth over the medium term. Business and travel services are the major imports into the EU from CARICOM countries. The UK, France and Germany are the largest importers of these services from CARICOM. In the establishment of REPAs with the EU a number of limitations may arise with respect to market access particularly with regards to the movement of natural persons and commercial presence. In education for example Antigua and Barbuda has not made any offers. However as telecoms reform progresses and the bandwidth is widened there will be opportunities for distance learning. While a number of US based universities provide such services in the currency union, challenges may arise in providing these services to the U.K. for example where there is no harmonised nor centralised accreditation process.

LIBERALISATION OF TRADE IN SERVICES IN CARICOM

If the CARICOM regime of free trade in services is to have meaning, it must provide for a greater level of liberalisation than is implied the current bindings of the countries under the GATS. Protocol II amending the Treaty of Chaguaramas provides the framework for the regime
of free trade in services. However, in its current form Protocol II provides a statement of intentions and the elements of the regime will only be clearly defined when the implementation schedule is adopted.

Protocol II provides for Rights of Establishment, Provision of Services and the Movement of Capital. Article 35 provides for a standstill on restrictions to the rights of establishment and for member states to notify the Council for Trade and Economic Development (COTED) of the existing restrictions. It also provides for establishment of criteria to safeguard these rights. The Article also addresses the abolition of restrictions on the right of establishment on a phased basis. It also establishes a consultative mechanism for the establishment of a programme for the abolition of restrictions on right of establishment in progressive stages. COTED would identify the activities to which rights of establishment shall not apply; establish the conditions under which it would be achieved and the stages and time frames for the removal of restrictions. Article 35 also provides for access to land and buildings, free movement of skills, the treatment of monopolies and the mutual acceptance of certificates and other evidence of qualifications.

Article 36 provides for a standstill and the progressive removal of restrictions on the provision of services within the community. It also mandates COTED in consultation with the competent organs of the community to establish a programme for the progressive removal of restrictions on trade in services. The Article does not explicitly mention the various modes of provision of services, together with the Article 35 and Article 37 which deals with the movement of capital all four modes would be covered. However, the right to exclude certain financial services from the provisions of this Article is given to the Council for Finance and Planning (COFAP). As with the WTO certain government services are excluded from Protocol II. These include the operations of Central Banks or monetary authorities, national security and the maintenance of public order, social security and public retirement plans.

Protocol II provides a framework for free trade in services, by providing for a standstill on current restrictions and a progressive liberalisation of the existing restrictions. The nature of the regimes which emerges depends on the strength of the programmes established for the progressive removal of restrictions. If the current WTO commitments are anything to go by, member states would have to improve significantly their offers if the trade in services regime is to be meaningful.

The completion of a regime in services would unleash competitive effects similar to goods with a consequent reduction in the price of these services. Because the use of services especially financial services permeates all types of production (including services themselves), there is a further knock-on boost for all types of businesses using these services. Competition in the provision of financial services can lead to the reduction in cost of credit if firms can raise their loans in other CARICOM territories. Similarly, the prices of insurance services can be reduced by increased competition.
CONCLUSIONS

The performance of the Antigua and Barbuda economy was similar to most of the other OECS economies, experiencing high growth in the 1980s but falling off during the 1990s. The last five years have largely reflected adjustment to the effects of five hurricanes which would have interrupted the development of the economy.

Antigua and Barbuda faces the same challenges of globalisation as the other OECS countries except for the fact that agriculture plays an insignificant role the economy. The fiscal difficulties faced by the country reduces its degrees of freedom to make the adjustment required.

The economy remains heavily dependent on tourism which in recent years have show signs of going through the maturity phase of the product cycle. The industry faces several problems relating to its structure. These include airlift capacity, the paucity of new investment in the industry, quality of service and inadequately maintained infrastructure. Tourism remains a viable industry however attention would have to be paid to product development and rejuvenation, marketing and accessing private financing for the needed investment in the industry. The model of government investment in the industry used in its early development would be hard to replicate in the new environment given the high debt burden of the government.

The manufacturing sector in Antigua has all but disappeared due to among other things the high cost of labour, lack of finance and general uncompetitiveness of this activity. Agriculture has not been a significant activity and the competitiveness studies do not identify any export competitive agricultural activities in that country.

The offshore financial sector has some potential for diversification of the economy, but the concerns of the OECD with respect to the regulatory framework will need to be addressed. The authorities have tried to address these concerns by passing legislation to strengthen the anti-money-laundering provisions and reform the regulatory framework.

The structure of Antigua’s recurrent revenues shows a heavy dependence on taxes derived from international trade; and a transition towards trade liberalisation will require major adjustments to the tax system towards domestic income and transactions. There is little evidence of non-compliance with WTO standards except for variations in the application of a few taxes and charges to nationals and non-residents as in the case of personal income tax, property tax and embarkation tax which appear to be inconsistent with WTO MFN principles. The rate of customs service charge coupled with stamp duties on customs entry documents appears to be in violation of the limits allowed for cost recovery and will require a downward adjustment.

On the basis of current revenue and expenditure flows, the fiscal account will continue to be in imbalance unless remedial action is taken to increase revenue and reduce expenditure. At the same time, the structure of taxes and the prevailing policies to grant incentives and concessions have led to low revenue buoyancy and serious defects in allocative efficiency. Tax incidence on tourism and tourism related services appear to be extensive, multi-layered and unduly complex, with possible cascading effects on tourism expenditure, and should be simplified into a single
sales tax or a more general VAT. Tax administration weaknesses have also contributed to the low tax buoyancy ratio.

Further liberalisation of international trade taxes will require a major overhaul of Antigua’s tax system, not only to recoup revenues foregone; but more importantly to assist Antigua’s economy to be more responsive to and competitive with the rapidly evolving external environment.

In addition, more attention should be given to efficiency in resource allocation and use, both on the consumption side and on investment. Budget reform should assist in rationalising and containing government recurrent and capital expenditures. The persistence of fiscal deficits in the past has necessitated increased borrowing, both domestic and external, with rising debt levels, increased budget commitments to debt servicing and rising exposure to currency risk requiring major improvements in debt management.

The scale and scope of fiscal reform needed in revenue, expenditure and debt management suggest an extensive programme of work which will require considerable international support and a long period of transition. Such a programme of reform must be a pre-requisite for moving towards the more demanding task of trade liberalisation which must be done within a more favourable macroeconomic framework than exists presently, in order to minimise its impact on sector competitiveness, prices and the fiscal account.

The study suggests that the market for services in Antigua and Barbuda is already characterised by significant liberalisation further liberalisation would benefit the country more than it would lose. Thus a negotiating strategy would move to further liberalise the services sector in exchange for concessions in agriculture. The study could not identify a case for Antigua as part of the OECS grouping to pursue a negotiating strategy that was different from the rest of CARICOM except in so far as the sequencing of adjustment measures and the transition period for liberalisation are concerned. Action to be taken and the transition period required are indicated in the Section on The Way Forward in the Overview.
<table>
<thead>
<tr>
<th></th>
<th>Mean 1986-89</th>
<th>Mean 1990-94</th>
<th>Mean 1995-98</th>
</tr>
</thead>
<tbody>
<tr>
<td>Stay-overs</td>
<td>165,428</td>
<td>203,19</td>
<td>201,760</td>
</tr>
<tr>
<td>Stay-over Growth</td>
<td>5.57</td>
<td>6.15</td>
<td>-2.75</td>
</tr>
<tr>
<td>Cruise ship Passengers</td>
<td>185,235</td>
<td>251,24</td>
<td>269,570</td>
</tr>
<tr>
<td>Cruise ship Passenger Growth</td>
<td>23.70</td>
<td>1.45</td>
<td>5.94</td>
</tr>
<tr>
<td>Total Visitor Growth</td>
<td>14.36</td>
<td>5.16</td>
<td>1.63</td>
</tr>
<tr>
<td>Visitor Expenditure Growth</td>
<td>16.76</td>
<td>7.85</td>
<td>-2.92</td>
</tr>
<tr>
<td>Service Penetration Index/1</td>
<td>12.93</td>
<td>11.02</td>
<td>22.54</td>
</tr>
<tr>
<td>USA Market Share</td>
<td>49.6</td>
<td>37.8</td>
<td>31.8</td>
</tr>
<tr>
<td>UK Market Share</td>
<td>12.8</td>
<td>19.8</td>
<td>26.6</td>
</tr>
<tr>
<td>Caribbean Market Share</td>
<td>16.5</td>
<td>19.3</td>
<td>19.0</td>
</tr>
<tr>
<td>Canadian Market Share</td>
<td>8.2</td>
<td>7.4</td>
<td>7.6</td>
</tr>
</tbody>
</table>

/1 Defined as the ratio of service exports to merchandise goods exports
### Table 3: Antigua and Barbuda Hotel Capacity

<table>
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<tr>
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<tbody>
<tr>
<td><strong>Hotels 1/</strong></td>
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1/ Reflects the temporary closure of hotels following hurricanes Luis and Marilyn during the last quarter of 1995
### Table 4: Antigua and Barbuda Foreign Direct Investment (FDI) Profile

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### Table 5: Antigua and Barbuda: Contribution to Real GDP and Real Growth of Services

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