

***RNM/OECS STUDIES TO
INFORM TRADE NEGOTIATIONS:
ST. LUCIA***

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ST. LUCIA

INTRODUCTION

The Economy of St. Lucia can be described as highly open and consequently heavily dependent on foreign trade. Exports of goods and services averaged about 65% of GDP, while imports of goods and services exceeded 70% of GDP. The economy was heavily dependent on agriculture during the 1970s and 1980s with agriculture contributing 16% of GDP in 1977, has shown some degree of diversification in recent years. Agriculture's contribution was reduced to 9% in 1998. On the other hand growth in the services sectors was fairly rapid especially in the area of tourism, construction and communication services. The growth of the tourism sector has contributed to the structural transformation of the economy to a more service oriented one.

St. Lucia faces a difficult period of transition to a more liberalised international environment. The emerging international order is less accommodating, even hostile to small developing countries and hence it calls for more focussed policy-making and strategic planning. The authorities are largely aware of the gravity of the circumstances they face and have sought to address the situation in a variety of ways. Recent Medium Term Economic Strategy Papers which set out the near-term strategy for dealing with the challenges of globalisation represent the national responses to these difficult circumstances.

RECENT MACROECONOMIC PERFORMANCE

During the period 1986-1998 the economy of St. Lucia grew at an average of 4.9% annually. However, this statistic masks the variety of performances achieved over that period. The economic performance over the period can be divided into three distinct periods. The period 1986-1989 was a period of high growth during which the economy experienced real growth averaging 8.3% annually. Growth was driven largely by simultaneous expansion in both the banana and tourism industries. High prices on the European market and favourable movements in the nominal exchange rate of the pound sterling vis-à-vis the EC dollar resulted in expansion of production of bananas and significant increases in foreign exchange earnings. During this period the contribution of agriculture to GDP was at its highest in recent times averaging about 14% of GDP. This was fuelled largely by expansion in banana production.

Meanwhile tourism also expanded at a rate of 19.46% in 1986 and 10% in 1987. Growth in the sector fell to just over 4% in 1988 and 1989 as the international recession began to take root. Communications services expanded at a fast clip averaging 22% over the period 1986-1989. Similarly the construction sector expanded rapidly at a rate of 26% annually fuelled by expansion of the tourism plant to cater for the increased demand in the tourism sector.

During this period, the deficit on the current account of the balance of payments widened from 2.2% of GDP in 1986 to 19.3% in 1989. Exports grew at an annual rate of 17% while imports grew at 24.6%. Never the less, the overall balance of payments recorded an overall surplus during this entire period. Capital transfers amounting to 4% of GDP and Foreign Direct

Investment (FDI) averaging 5.8% of GDP were able to offset the widening current account balance.

The period 1990-94 was a period of much lower growth as the economy could only muster an annual growth rate of 2.1% annually over this period. Growth in the agricultural sector turned negative due to the uncertainty of the banana industry consequent on the completion of European Single market. In addition the pound sterling exited the European Exchange Rate Mechanism (ERM) precipitating a fall in the local price paid to the farmers of bananas and, consequently, export earnings. Similarly, manufacturing and the construction sectors recorded negative growth as the recession in the USA softened the market for garments and electronic products. During this time a number of manufacturing concerns closed their doors as the added threat of the entry of Mexico into NAFTA made its presence felt. Construction declined on the heels of a slow down in the expansion of tourist arrivals. The intensification of competition and the decline of official assistance resulted in some dampening of the growth rate. Although the expansion in the rate of growth of tourism fell it was still positive and strong enough in conjunction with expansion in the growth rate of communication services to prevent a decline in the economy except in 1991 when a growth rate of -0.86% was recorded.

This period saw a slight improvement in the current account of the balance of payments as it narrowed from 15.4% of GDP to 11.6%. The negative growth rate in banana production coupled with the fall in the domestic currency price of bananas consequent on the exit of the pound sterling from the ERM resulted in an EC\$84m reduction in earnings from merchandise exports. Merchandise export earnings declined from EC\$353.6m in 1990 to EC\$269.7 in 1994. However this poor performance in merchandise exports was more than offset by improvement in the export of services especially tourism services which almost doubled during the period. The average tourism expenditure for the period 1990-94 was EC\$440m compared with EC\$225m for the period 1986-1989. FDI flows amounting to 9.6% of GDP and other flows on the capital and financial account were insufficient to fully offset the current account deficit and hence overall surpluses approximating 1.5% of GDP were recorded for the years 1992-1994.

The period 1994-1998 represented a slight deterioration from the marked slow down experienced during the first part of 1990s. The growth rate averaged about 1.7%. Again the poor performance of the agricultural sector was the most important contributor to the slow growth rate. The agricultural sector declined 19.4% in 1994 and by a further 17.9% in 1997 after modest recovery in 1995 and 1996. These declines resulted from -20.5% and -23% declines in the value added in bananas, in 1994 and 1997 respectively. Moreover the 1997 performance was exacerbated by a 32% reduction in the value added from other crops. Fisheries and livestock were the only two agricultural activities that exhibited robust growth during this period.

The manufacturing sector continued to be beset by lack of competitiveness in the regional market and experienced declines in every year during this period except 1995. Meanwhile the tourism sector recorded relatively strong growth averaging 5.8%. The communications sector turned in a mixed performance, alternating between relatively strong growth and slight declines.

The current account Balance of Payments deteriorated during the period as a result of the poor performance of merchandise exports - principally related to the developments in the banana

industry and the continued increases in the import of goods and services. By 1998 the current account had widened to 16% of GDP. However, these current account deficits were largely offset by inflows on the capital and financial account as St. Lucia still attracts significant amounts of foreign direct investment (8.2% of GDP). In addition, STABEX transfers from the European Union and official borrowing of the Central Government augmented capital account inflows.

RECENT FISCAL PERFORMANCE

Fiscal performance in St. Lucia improved remarkably between 1984 and 1998. The current account balance, which was in deficit equivalent to 1.7% of GDP in 1984 improved steadily to a surplus of \$99.0 million dollars or 8.7% of GDP at the end of 1993. However, it declined to \$49.9 million dollars or 3.8% of GDP by 1997 before recovering to \$82.7 million dollars or 5.8% of GDP in 1998. The overall deficit which stood at 5.0% of GDP in 1984 also improved to 2.7% of GDP in 1998 despite increasingly large outlays on capital spending and a relative decline in grant funding. Improvements in the fiscal account began in 1986 in which year 43.0% of the investment programme was financed from local revenue, increasing to 53.9% by 1993 before declining to 48.0% in 1998.

Recurrent revenue which averaged 28.6% of GDP over the review period grew at an average rate of 9.2% with an average buoyancy rate of close to 1.2. The buoyancy rate for tax revenue was consistent with this average. Taxes on international trade, however, exceeded the average at 1.3; but lapsed towards the end of the period to less than 1.0 as a result of a fall in petrol revenue and generous duty-free concessions.

Taxes on international trade as a per cent of total revenue also grew in importance from 51.8% in 1984 to 56.7% in 1998. Domestic taxes reduced its share of total revenues from 38.8% in 1984 to 35.5% in 1998. Non-tax revenue also declined in importance from 9.4% of total revenue to only 6.8% by 1998. As a per cent of GDP, domestic taxes increased from 9.9 in 1984 to 10.4 by 1998, taxes on international trade from 13.2 in 1984 to 16.1 by 1998 and non-tax revenue declined from 2.4 in 1984 to 1.9 in 1998.

Recurrent expenditure averaged 23.6% of GDP during 1984 to 1998 with high ratios prevailing in 1984 and 1985 at 27.1% and 28.4% respectively and substantial reductions during 1986 to 1992 averaging just over 21.5%; but rising steadily to 25.0% by 1997. Annual growth rates of recurrent expenditure averaged 6.9 during the period compared to 9.2% for recurrent revenues.

Growth in wages and salaries averaged 7.8% with intermittent substantial wage awards up to 1995. Recent wage awards have been moderate and growth in wages and salaries have levelled off to an average 1.8% over the three years 1996 to 1998. Goods and services averaged 7.0% annual growth but have been subjected to strict economies since 1998 with the introduction of programme and performance budgeting. Interest payments, on the other hand which also averaged 7.0% annual growth has shown a tendency to rise sharply since 1995 as more extensive use was made of short term non-concessional financing. Growth in expenditure on transfers

which averaged 8.2% has been declining since 1997 as a result of a reduction in transfers to the private sector.

The share of wages and salaries in total recurrent expenditure increased from 51.9% in 1984 to 55.7% by 1998. The share of interest payments increased marginally from 5.6% to 5.9% while the share of transfers declined from 22.7% to 20.3% over the same period. Goods and services, on the other hand, fell from 24.6% to 17.7%. This classification of expenditure is the only true variable cost showing much greater flexibility to budget adjustments than do the other classifications.

Sectoral allocation of recurrent expenditure has shifted towards higher outlays on education, health and general administration. The share of expenditure on education moved from 24.3% in 1990 to 25.3% in 1998 and on health from 11.0 to 12.3%, indicating greater emphasis on human resource development. Except for general administration which increased its share marginally from 31.5 to 33.2%, most other services declined in relative importance. Economic services, in particular, declined from 18.1 to 13.0%, while other social services together fell from 10.7 to 9.4%.

St. Lucia's strong fiscal performance and significant flows of foreign grants have supported substantial outlays on its public sector investment programme. However, between 1988 and 1998, its public external debt rose from 15.1% of GDP to 26.2% of GDP. The largest share of external borrowing went to public utilities which accounted for 32.7% of debt outstanding in 1998. This sector has responded with fairly strong growth during the entire period. Internal communication (roads and bridges) also accounted for a major share of the debt at 18.6% followed by industrial development at 17.9%. Growth response to borrowings for industrial development, however, was less than adequate.

Domestic borrowing increased by more than 32.0% in 1998 due mainly to the absorption of the St. Lucia Banana Growers Association (SLBGA) debt. This as well as other non-concessional borrowing has put strong pressure on debt servicing costs which increased by 43.2% in 1998. As a result of increased use of non-concessional borrowing the debt service ratio increased from 3.1 in 1995 to 4.1 in 1998.

STRUCTURE OF REVENUES

St. Lucia continues to be heavily dependent on taxes on international trade which consisted of 56.7% of total recurrent revenue during 1997. Domestic taxes accounted for 36.5% while non-tax revenue contributed 6.8%. Taxes on income and profits as a per cent of total recurrent revenue stood at 21.9% while taxes on domestic goods and services accounted for 14.3%. Taxes on property were minimal at 0.3% as transitional arrangements are in process for reform and consolidation of this tax.

The basic structure of taxes is similar to those obtained in other OECS countries and are classified broadly as taxes and charges on domestic goods and services and taxes on international trade. These consist of the following:

Taxes and Charges on Domestic Goods and Services -

- personal income tax with graduated rates from 10.0 to 30.0%, the latter rate applying to income over \$30,000 after a threshold of \$10,000 plus a number of qualifying allowances;
- a corporate tax at 33.33% of net income;
- withholding tax at 25.0% levied on payments of royalties, rents, management fees, premiums, commissions, annuities and other payments to non-residents;
- property tax at 7.0% of annual rental value;
- land tax on lands over 10 acres at graduated rates rising from 25 cents per acre on lot sizes between 10 to 50 acres to \$1.00 per acre on lot sizes exceeding 500 acres;
- property transfer tax on the sale value of properties at rates rising from 2.5% of properties over \$50,000 to 5.0% on properties valued at over \$75,000 with a special rate of 10.0% for foreigners;
- consumption tax at rates ranging from 4.0% to 30.0% on locally produced goods;
- excise tax at \$2.35 per litre of locally produced alcohol;
- hotel accommodation tax at 8.0% of hotel bills; in the case of all-inclusive hotels, a head tax of \$27.00;
- insurance premium tax at rates ranging from 1.5 to 3.0% of premium;
- entertainment tax at 15.0% of gate receipts;
- telecommunications tax at 10.0% of net income of telephone company;
- various licenses on trade professions and vehicles.

Taxes on International Trade and Transactions -

- import duties at rates ranging generally from 5.0 to 35.0% with higher rates at 40.0% on agricultural imports and agro-processed goods as well as selected luxury items such as jewellery, motor vehicles, record discs and electronic music players;
- consumption tax at rates ranging from 4.0 to 30.0%;
- an export tax on bananas at 5.0% of gross export sales;
- a customs service charge at 4.0% of c.i.f value;

- airport departure tax levied on departing passengers at \$35.00 per passenger for nationals and \$40.00 per passenger for non-nationals;
- travel tax at 7.5% of tickets issued by carriers in St. Lucia.

St. Lucia's tax structure, as in other OECS states, reflects a strong emphasis on income and goods. There are few expenditure taxes on services, notably insurance premium tax, entertainment tax, telecommunications tax and professional licenses.

Basically, the tax structure is consistent with WTO rules except for an aliens land holding license fee and an embarkation tax that appear to discriminate against non-nationals. The removal of the aliens landholding license fee and downward equalisation of the embarkation tax could be done without significant loss of revenue. However, in the case of the aliens landholding license, social considerations demand a cautious approach to deregulation. Concerns about the demand/price effect of complete and immediate deregulation and the possible alienation of lower income nationals from lands needed for basic shelter and small farming in a society where poverty levels are high suggest a gradual approach and the devising of physical structure plans and policies that ensure the basic needs of nationals are provided for.

The customs service charge was recently increased from 3.0% of CIF to 4.0% of CIF. This is a considerable revenue earner with annual yield estimated at over \$34.0 million. Since the tax is an additional imposition directly on imports, it may be considered a potential violation of WTO rules; but only in so far as it exceeds the permissible limit for cost recovery. Immediate adjustment of the tax would result in considerable revenue loss of revenue. The alternative to commensurately and immediately adjust the consumption tax as a compensatory measure would put additional pressure on domestic production. Such an adjustment would be more viable over a period of transition and within the framework of a general tax reform programme that shifts taxes from imports downstream to a broadened expenditure base.

RECENT TAX CHANGES

Since the restructuring of its income tax in 1986 and the implementation of the CET in 1993, St. Lucia has not made any major change in its tax system except:

- a) the abolition of the foreign exchange tax;
- b) increasing the customs service charge from 3.0 to 4.0%;
- c) an upward revision of trade, liquor and drivers' licenses.

Government introduced a 5.0% levy on telephone bills and a 20.0% surcharge on fuel for electricity generation.

The government announced a number of additional tax changes in its 1998/99 budget including:

- the abolition of vehicle licenses and the restructuring of the consumption tax on petroleum products;

- increases in learners and visitors' drivers permits and vehicle registration with a new charge for the transfer of vehicle ownership and a special license for tandem axle vehicles;
- a head tax on all-inclusive hotel guests at \$27.00 per head;
- redesign and strengthening the administration of property tax;
- exemption of imports of medical equipment from import duty and consumption tax;
- derogation of liquor license fees to village councils;
- increase of 10.0% on consumption tax on cigarettes and 5.0% on cigars;
- a change in the method for determining capital allowances;
- an interest allowance for persons servicing student loans;
- allowances for premiums paid towards retirement plans;
- the abolition of charges for tax exit certificates.

MEDIUM TERM PROSPECTS

The improvement in economic policy and business environment achieved in recent years has laid a strong basis for robust expansion of the economy. The St Lucian economy is projected to grow at 3.6%, 3.1% and 3.0% in 2000, 2001 and 2002 respectively, compared with 1.7% experienced during the period 1994-1998. This forecast is based on anticipated developments in the tourism industry and the agricultural and construction sectors. Growth in the tourism industry is anticipated as both stay-over arrivals and cruise ship passengers are expected to increase throughout the period. Agricultural production is expected to increase in 2000 and thereafter remain relatively flat. An expansion in construction activity is anticipated from both the public and private sectors. The fiscal position of the central government as represented by the current account balance is likely to remain favourable throughout the period being forecasted. The external current account deficit is expected to worsen throughout the three-year period. The rate of inflation is projected to remain low, but will be influenced by price movements in the major trading partners. Liquidity in the banking system is expected to tighten.

During the years 2000 to 2002 growth in the hotel and restaurant sector is projected as a result of an expected increase of 48% in stay-over arrivals in 2000, and 5.0% and 2.0% in 2001 and 2002 respectively. There is likely to be an increase in room capacity in light of the expansion of some existing hotel facilities and the expected completion of a 100-room hotel in 2001.

Banana production was expected to increase to 70,000 tonnes in 2000 reflecting the replanting exercise at the end of 1999. Thereafter production is likely to remain flat based on the continued uncertainty within the industry particularly on the domestic side. The output of the agricultural

sector is expected to move in line with banana production, which is likely to account for about 50.0% of total agricultural production.

The available information indicates that there is unlikely to be any significant improvement in the manufacturing sector. The level of activity in the sector is expected to remain relatively stable during the medium term as the problems that beset the sector are unlikely to be alleviated in the short-run. The output from wearing apparel industry is expected to remain fairly stable. The production of paper products will be influenced in part by developments in the banana industry.

The major stimulus to growth during the forecast period is likely to be the construction sector. This forecast is based on the number of ongoing and proposed government projects, including the national stadium, national cricket grounds, road improvement management project school construction under the basic education reform project, the correctional facility (\$44.7m), a multi-story car park (\$21.6m) and government offices (\$14.1m). Construction activity in the private sector is expected to remain strong based on planned hotel development projects.

The annual rate of inflation was expected to be 5.0% in 2000 and 3.0% in 2001 and 2002, broadly in-line with inflation expectation in St Lucia's major trading partners.

The current account deficit on the balance of payments is expected to deteriorate throughout the forecast period to an estimated \$400.9m in 2002, due mainly to a projected worsening on the merchandise account which is forecasted to widen from a deficit of \$671.3m in 1999 to a one of \$1,006.4m in 2002. Imports are projected to increase due to the anticipated growth in construction activity, and buoyancy in tourism, while exports are likely to remain flat, based on expected outturn in the banana industry and the manufacturing sector.

Gross visitor expenditure is projected to increase by 10.4%, 8.4% and 5.1% in 2000, 2001 and 2002 respectively, based on the expected growth in stay-over visitors and cruise ship passengers.

Net inflows in the capital and financial account is expected to increase throughout the period being forecasted. In 2000 the surplus is projected at \$344.2m, based on increases in capital grants of \$21.3m. In 2001 the surplus is projected to increase to \$399.2m, largely as a result of growth in central government borrowing and government guaranteed loans totaling \$31.5m. A further increase in the surplus is expected in 2002 as a result of an 18.7% increase in foreign direct investment inflows. At the same time inflation is expected to increase slightly in 2000 but settle around 3%, in line with St. Lucia's trading partners, for the remainder of the period.

FISCAL PROSPECTS

The fiscal outlook is for continued growth in central government savings if the proposed revenue enhancement measures are fully implemented, firm control is maintained on recurrent expenditure, in particular wages and salaries, investment spending is carefully prioritised and less reliance is placed on non-concessional short term borrowing. A number of initiatives have already been taken to strengthen tax administration and improve expenditure management:

- a standard integrated government tax administration system (SIGTAS) has been introduced to improve tax assessment, collection and accounting which has already achieved a 95.0% collection rate for corporate taxes;
- improvements in customs administration through the CRM and ASYCUDA designed to strengthen management and provide data for policy formulation and analysis;
- budget reform to rationalise the allocation of resources and control spending – significant savings have already been achieved through more analytical review of outlays on goods and services;
- enhancing the procurement, payments, accounting and reporting systems (SIGFIS) to support effective financial management.

Other policy issues to be considered include the updating of user charges and public utility rates, the commercialisation/privatisation of selected activities and continued divestment of government assets. Rationalisation of tax incentives will also be of primary importance for St. Lucia's fiscal prospects. The extent of revenue forgone as a result of duty-free concessions has been estimated at close to 30.0%.

Although revenue buoyancy has been high in St. Lucia there are deficiencies in the tax system which need to be corrected to improve efficiency and equity in burden sharing and to make the fiscal system more responsive to changes in the domestic and external environment.

The unequal distribution of the tax burden among sectors encourages non-compliance as well as shifting resources to preferred sectors where rents in the form of tax incentives are more readily available. Non-compliance is often countermanded by arbitrary assessments resulting in large accumulation of arrears. Tax officials are often constrained in enforcing tax laws because of their complexity and a lack of legal support to pursue defaulters in court. The incentive regime also creates distortions in burden sharing and provides opportunities to evade tax liabilities in respect of taxable income.

Customs revenue suffers similarly from undervaluation of imports and smuggling. E-commerce and electronic transactions have introduced new dimensions to customs administration in a situation where most customs officials have received only basic training in customs procedure. The situation becomes even more difficult with the diversion of officers to undertake drug prevention and surveillance work. The dilution of customs revenue from all these factors necessitate high rates of customs duties and taxes to maintain the revenue yield.

Additionally, generous concessions and exemptions result in substantial revenue leakages estimated at close to 30.0% of potential customs revenues. A similar situation exists with respect to the granting of tax exemptions under the fiscal incentives scheme. In addition to the direct revenue loss arising from these exemptions and concessions, lack of transparency in incentives policy and the absence of any system of accountability on the part of beneficiaries under the fiscal incentives scheme undermine the authority of tax officials and their ability to enforce observance of the tax laws. There is urgent need to review the incentives framework as applied

under the fiscal incentives scheme and discretionary grants by government to determine their appropriateness in the current situation in which all sectors become important in the drive towards overall expansion and diversification of the economy especially in non-traditional sectors such as the services sector.

Recent initiatives have been taken to strengthen the inland revenue and customs. The SIGTAS programme has assisted in streamlining operations, computerising assessment and collection processes and improving the technical skills of tax officials with encouraging results. It is estimated that the compliance rate for companies has now reached 95.0%, a traditionally difficult area. The programme has also helped in accelerating the tracking and collection of arrears.

ASYCUDA and a programme for institution strengthening supported by DFID has helped to improve operations at the customs; but much work requires to be done on ASYCUDA to realise its full potential.

Although the two principal revenue departments have undergone major reorganisation and strengthening, their capacity is still stretched by the number of taxes to be administered. A lot could be gained in tax efficiency if the entire tax system should be streamlined to focus more on fewer and broad based taxes with wide coverage that can be administered with greater cost effectiveness.

The high level of transfers in the government budget at 20.3% of recurrent expenditure draws attention to the performance of public enterprises and the need to make them commercially viable. Utility tariffs should be reviewed and brought to economic levels so as to generate savings and eliminate transfers from the central government. St. Lucia has established a good record on its divestment of public assets. Consideration should be given to extending the divestment programme especially to loss-making enterprises.

The ratio of recurrent expenditure to GDP at 22.6% compares very favourably with similar ratios for the rest of the OECS region. Placed against a revenue to GDP ratio of 28.4%, this level of expenditure if prudently controlled holds good prospects for growth in current account savings from the present level of 5.8% of GDP. However, an examination of both the economic classification and sectoral allocation of recurrent expenditure brings into question the efficiency with which resources are utilised.

The share of wages and salaries in total recurrent expenditure was at 55.7%, while the cost of general administrative services took up 33.1%. Notwithstanding the persistent problem of diseconomies of scale in the delivery of public services due to the small and scattered population, employment in the central government service at over 7,700 is considered high, even on a per capita basis. The fact that St. Lucia has gone ahead of the other OECS states in maintaining competitive wage rates for higher level public servants makes it imperative that the numbers employed should be rationalised. Public sector reform and budget reform should focus on redefining governments principal objectives and priorities and determining the optimal resources required to implement them. Reduction in numbers may be achieved within a programme of retraining for alternative employment and attrition by natural wastage.

The budget reform programme has been designed to strengthen the process of reviewing expenditure, enhance accountability for procurement and spending and to generate management information for policy review and reformulation. Although the system has introduced new methods of translating government's plans and programmes into effective annual budgets and brought transparency in the programming of expenditure, the system operates within the framework of rigid organisational structures which reduces the dynamics of change that is inherent in the concept. There is a danger that over time annual budgets will merely be incremental adjustments to pre-established programmes. This could change if the element of strategic planning that is part of the process takes precedence over institutional interests.

The effectiveness of programme and performance budgeting has the potential to provide the level of analysis that will help to determine the unit cost of service delivery and the level of charges required for cost recovery. This will also aid decisions leading to commercialisation of services or divestment of activities with commercial potential.

The high level of public sector investment at 12.7% in 1998 has been assisted by substantial grants estimated at 6.0% of GDP. To sustain this level of investment in the medium term will require stronger efforts to increase recurrent revenue and control recurrent spending as the level of grant funding diminishes. More careful selection and prioritisation of projects will also assist this effort.

The relatively high savings rate and significant grant flows have helped to keep the public debt within moderate bounds. St. Lucia's public debt in 1998 was the lowest among OECS countries at 26.2% of GDP. Interest payments took up only 5.9% of recurrent expenditure.

Overall the prospect for strong fiscal performance appears to be favourable; but with declining concessional flows there will be need to improve the efficiency of taxes and tax administration, and enhance the process of selection and programming of investment projects.

MEDIUM TERM POLICY OBJECTIVES

The medium term macroeconomic policy objectives are related to the implementation of measures to enhance the competitiveness of the economy to face the competitive pressures in the new international environment. The most important of these are:

- (i) Increasing the level of national saving in the economy: Over the period 1986-98 gross capital formation averaged about 25% of GDP while gross national saving averaged about 15%. The saving investment gap was therefore financed by foreign inflows largely in the form of foreign direct investment especially in the tourism sector. However, government investment in physical infrastructure was financed largely by official borrowing internationally. In recognition of the need to reduce the saving-investment gap, the government is committed to increasing the level of public sector saving to 7% of GDP and the central government saving to 5% of GDP, in line with the framework for mutual obligations conditioning the disbursement of STABEX resources. Among the measures being implemented to try to achieve the level of public sector saving are:

- (a) rationalisation of tax incentives;
 - (b) implementation of comprehensive reform, including income tax, property, tax, indirect taxes and the reduction of the Common External Tariff;
 - (c) Improvement in tax administration;
 - (d) Extension of the granting of Capital Allowances;
 - (e) Increasing the efficiency of public enterprises in particular the Water and Sewage Authority.
- (ii) Private sector saving would be enhanced by the development of money and capital markets being developed on a regional basis by the Eastern Caribbean Central Bank, and the creation of specialised saving vehicles to encourage contractual savings
- (iii) Rationalisation of the incentive regime: The incentive framework in St. Lucia is centred around four pieces of legislation; viz., The Tourism Incentives Act, Hotel Aids Ordinance, The Fiscal Incentives Act and the Consumption Tax Ordinance. The first two relate to hotels and guest-houses under which tax deductions are allowed for capital expenditure involved in the construction or expansion and general repair of these facilities. The manufacturing sector receives incentives under the Fiscal Incentives Act and the Consumption Tax Ordinance. They are entitled to tax holidays lasting from 5 to 15 years and eligible enterprises are permitted to import equipment, spare parts and raw materials free of duty from outside of the CARICOM region. Further rationalisation of the incentive regime and the reduction in discretion in the granting of incentives are critical steps in improving the investment environment. These would support the restructuring of the National Development Corporation which has been undertaken.

SECTORAL STRATEGIES

The authorities in St. Lucia are focussing on five major areas for the development of the economy over the medium-term. These are tourism, agriculture, offshore financial services, manufacturing and other services including informatics. The specific strategies for these sectors will be discussed under the appropriate sub-headings. 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 infrastructure of St. Lucia has undergone significant improvement in recent years. There is a programme for the continuous improvement of the 5 official Seaports in the country. Port Castries will be progressively developed into a cruise ship Terminal while the cargo activities

would be moved to an enhanced container port at Cul de Sac. View Fort is targeted to become the major transshipment port in the Eastern Caribbean with the development of a Free Zone in that area. The other leisure ports would also be upgraded. Similarly the airport facilities have been upgraded with the expansion of the Hewanorra International airport and the continued enhancement of the facilities at the George F. L. Charles Airport.

Electricity generation capacity has also been improved with the installation of two new 9.3 MW generators and the commissioning of another 30 MW of plant. This will increase the generating capacity to 63.5 MW compared to the estimated peak-load demand of 35 MW, and provide for the projected demand that would come from the increase in the hotel room capacity and household and industrial demand that is expected in the next few years.

The road network in St. Lucia is good as significant improvements have taken place during the last ten years. Under the CDB financed Road Improvement and Management project, the Ministry of Communications, Works and Transport established a road inventory and database system. The system has the capacity to generate comprehensive road maintenance plans. In addition new roads have been constructed and planned. The major project completed is the Castries Cul de Sac Highway. However less spectacular but no less important progress has been achieved in the construction of feeder roads to service the agricultural sector and enhance the geographical concentration of production infrastructure in the sector. A 21 million dollar multistory car park is being constructed and this along with the migration of some facilities out of Castries and the construction of the inner relief road would enhance the functionality of the City.

Rapid expansion of the tourism sector creates increasing demand for potable water. The North of the island would be comfortably serviced by the recently constructed John Compton Dam until the year 2025. Plans are also in train to complement this capacity by the improvement in the transition mains and distribution network. The South of the island has also been targeted for significant development initiatives. However, the isolated nature of the rural water systems will render the supply inadequate to service the increase demand for water. Plans are already being laid to implement the appropriate infrastructure to satisfy these needs. The Water and Sewage Authority is being restructured and the tariff is being structured to ensure the financial viability of the Authority.

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. The Government of St. Lucia spends about 25.3% of current expenditure on education. However most of it is on personnel emoluments and not much is left over for supplies and materials.

The Basic Education project which was officially launched in 1996 is aimed at improving the quality education through teacher training, curriculum development, construction of new schools and the refurbishing of the existing stock. The Ministry of Education was used as the pilot for the programme budgeting exercise and the establishment of an education planning division staffed with a qualified education planner has greatly enhanced the management of the education sector.

Access to and improvement in the quality of education would be enhanced by the following initiatives identified in the 1998 MTESP.

- (i) The establishment of minimum standards via an emphasis on quality assurance;
- (ii) Improvement in the efficiency and effectiveness of education management at all levels of the sector, by strengthening the planning, statistics and database capacity of the Ministry of Education and the empowerment of principals and teachers in the areas of policy and decision-making;
- (iii) Improvement in technical and vocational education training programmes;
- (iv) Expansion of access to secondary education by the construction of new secondary schools to address the perennial shortage of secondary school places;
- (v) The enhancement of the quality of learning through the upgrading of basic teacher training and the expansion of in-service training for all teachers;
- (vi) Exploration of financing options such as cost recovery in the sector, particularly in the area of tertiary education.

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. At present expenditure on health accounts for 12.3% of the recurrent budget. The 1998 MTESP observes that the reform of the sector is a prerequisite for effective healthcare system. The reform process will embrace areas such as reorganising and restructuring of all health institutions, designing appropriate health management systems and health delivery systems, and developing a national health information system to allow for proper monitoring and evaluation.

In order to make health care more accessible the authorities have been looking at cost recovery mechanisms and greater private sector participation in the provision of health services. A National Health Insurance scheme is being proposed. To this end a National Health Insurance Board has been established with the following tasks:

- (i) formulation of a plan of action for the implementation of the National Health Insurance;

- (ii) preparation of a Patients Charter/Bill of Rights that articulates the benefits and expectations of the scheme;
- (iii) introduction of a programme for upgrading the management systems of health institutions involved in the scheme.

THE ENVIRONMENT

Like most small island economies, St. Lucia must always be aware of the fragility of its ecosystem. This is particularly so since one of 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 environment issues faced by the country are related to the use of its natural resources for agriculture and tourism. Some of the specific issues highlighted in the National Environmental Action Plan (NEAP) are watershed management, coastal zone management, marine resource management, solid waste management, liquid waste management, water resources and forestry resources.

There are several initiatives at varying stages of implementation to address these critical environmental issues. The Watershed Management project was implemented as a result of the flood damage from tropical storm Debbie. Its objectives are to rehabilitate the hydraulic systems of the country, develop of a watershed management plan to enhance sustainable watershed development and to strengthen Government's capacity in environmental management and flood preparedness. The implementation of the World Bank Solid Waste project and the environmental levy for its finance is another initiative to protect the natural environment. A comprehensive plan for coastal zone management has also been developed in conjunction with the OECS Natural Resource Management Unit and the introduction of measures aimed at protecting forestry resources are other positive steps being taken by the authorities to try to preserve the environment. In addition, user fees and incentive mechanisms for agriculture, tourism and industrial uses of forest resources to reflect environmental costs would promote sustainable practices and discourage the unsustainable ones.

However all of this investment in economic and social infrastructure will go to waste if the private sector does not step up into its role as the engine of growth. The economic and social infrastructure will provide growth while they are being constructed but the end result is that private sector investment is undertaken to complement the economic infrastructure. Several studies, e.g. a recent UNDP study suggest that a deliberate policy of private sector development would need to take place to prepare them for the role.

Enhanced public sector management and consensus building will also be critical. The institutional framework for the state to become a facilitator of development would need to be effected by civil service reform to engender a change in the mindset of the civil service. The

forging of consensus on the main elements of a strategy for development, among the social partners (Government, private sector, labour and non-governmental organisations) would provide a firm basis for going forward.

AGRICULTURE SECTOR

Contribution of Agriculture

The Agricultural sector remains an important component of St. Lucia's economy. In 1999 although banana production was down 52% from its peak 1990 level, Agriculture accounted for over 7% of real GDP (Table 1.1). In fact, during the 1985-1998 period, the sector contributed an annual average of nearly 13% of GDP. Agriculture plays an even greater role in the country's trade balances and hence its foreign exchange earnings. Agricultural exports in 1999 amounted to EC\$98 million, or 62% of all exports. Notwithstanding income multiplier effects, the employment contributions of agriculture are far reaching. The banana industry alone is said to employ (directly and indirectly) roughly 30,000 workers, which represented over 40% of the islands 1999 labour force.

Table 1.1.
The Agriculture Sector, Selected Indicators, 1999

Indicators	Values
GDP (factor cost EC\$M)	1,497
Total Export (EC\$M)	159
Agricultural Output (EC\$M)	110
Agricultural Export (EC\$M)	98
% Agriculture of GDP	7.4%
%Agricultural Export of Total	61.8%

Source: St. Lucia Government Statistics Dept.

Structure of Agriculture

Agriculture in St. Lucia is characterised by small and middle size holdings. In 1996 farms of under 5 acres accounted for 26% of agricultural lands, those 5 to 10 acres occupied 21%, while 10 to 25 acre holdings occupied another 18% (Table 1.2).

Table 1.2. Total Area by Size of Holdings, by Census Year.

Group Size Acres	1973/74		1986		1996	
	Total Area	%	Total Area	%	Total Area	%
up to 5	10,204	14	12,350	21	13,521	26
5 to 9.9	7,068	10	7,802	13	10,899	21
10 to 24.9	6,396	9	7,763	13	9,375	18
25 and over	48,333	67	30,101	52	17,528	34
Total	72,001	100	58,017	100	51,323	100

Source: 1996 Census of Agriculture Report

Another feature of St. Lucian agriculture is that while the number of farm holdings is on the rise, total agricultural acreage is declining. The 1996 agricultural census reported 13,336 farm holdings, representing an increase of 15.7% from the previous census (1986). In contrast, total land on agricultural holdings decreased by 11.5%, from 58,017 to 51,323 acres (Table 1.2). Notwithstanding the overall increase in holdings, there was a 12.8% decline in holdings of 25 acres or more, thus all of the observed increases in land holdings were holdings of fewer than 25 acres (Table 1.3). This has meant a more even distribution of agricultural land ownership, as reflected in the fact that the acreage share of holdings of fewer than 25 acres increased from 47% in 1986 to 65% in 1996 (Table 1.2).

Table 1.3
Number of Holdings by Acreage Size, by Census Year.

Group Size Acres	1973/74		1986		1996	
	Holdings	%	Holdings	%	Holdings	%
Landless	502	4.6	830	7.2	1630	12.2
up to 5	8558	78.2	8770	76.1	9166	68.6
5 to 9.9	1082	9.9	1191	10.3	1713	12.8
10 to 24.9	475	4.3	560	4.9	700	5.2
25 and over	321	2.9	180	1.6	157	1.2
Total	10938	100.0	11531	100.0	13366	100.0

Source: 1996 Census of Agriculture Report

Lands devoted to crops represented 80% of agricultural lands, and as to be expected, bananas followed by coconuts accounted for the leading share of croplands. In 1996 bananas occupied the equivalent of 44% of all croplands, and coconuts 29%. Mangoes with the equivalent of 6.8% of croplands had the third largest share (Table 1.4).

Table 1.4
Crop Acreage

Crop	'1986		'1996	
	Acreage	%	Acreage	%
Banana	15,786	40.3	15,163	44.0
Coconut	15,111	38.6	10,013	29.1
Mangoes	1,671	4.3	2,355	6.8
Citrus	1,178	3.0	1,379	4.0
Breadfruit	667	1.7	1,350	3.9
Plantain	470	1.2	863	2.5
Avocado	433	1.1	492	1.4
Cocoa	548	1.4	323	0.9
Total	39,169	100.0	34,428	100.0

Source: St. Lucia Government Statistics Dept.

Population growth, improvements in standard of living and growth in the hospitality sector have expanded the domestic market for locally grown food. Producers of non-traditional crops now have a number of outlets for their products, including the marketing board, village and city markets, hotels and supermarket chains. However, in spite of the rise in domestic consumption of locally grown foods, the country's food import bill rose from \$97 million in 1987 to \$200 million in 1998, and the food trade balance changed from an \$82 million surplus in 1987 to a deficit of \$109 million in 1998.

Over the past five years the banana industry has met with considerable change. Prior to 1994, the St. Lucia Banana Growers Association (SLBGA), a statutory institution established under the St. Lucia Banana Growers Association Act of 1967, was responsible for purchasing all export quality bananas from farmers, and boxing, delivering and selling the bananas to Geest. In addition, the SLBGA controlled diseases affecting bananas and organised and administered the banana extension service. Each of the Windward Islands had a similar banana growers association (BGA).

The Windward Islands Banana Growers Association (WINBAN) was the umbrella organisation of these BGAs. WINBAN negotiated and monitored marketing and shipping contracts for bananas, represented the growers on the UK Banana Trade Advisory Committee in London, initiated research and supplied farmers with technical assistance and needed banana inputs. Then in 1994 the governments of the Windward Islands replaced WINBAN with the Windward Islands Banana Development and Exporting Company (WIBDECO). Two years later, WIBDECO and Fyffes Plc., each purchased a 50% stake in the buyout of Geest Bananas. WIBDECO's functions were to (1) negotiate marketing and freight arrangements for windward islands fruit, (2) manage the industry's investments, (3) reinforce the Windward Islands and Caribbean banana lobby in Europe, (4) arrange payments from export sales and other trading activities to the BGA, (5) manage receiving and loading operations in the windward islands, (6) co-ordinate the Geest shipping agency and branch operations in these islands, and (7) provide technical services to the industry to enhance productivity and fruit quality.

Contribution and Performance

Over the 1988-1993 period banana production averaged 126 thousand tons per year and earned annual export revenues of \$165 million. In contrast, during the 1994-1999 period, annual productions fell to 85 thousand tons, and export earnings to \$106 million. Production reached a low of 65 thousand tons in 1999, representing less than half of 1990's output, and earning only \$87 million in export revenues. It is estimated that between 1992 and 1997, 49% of farmers left the industry, and many others reduced their level of on-farm investment.

Table 1.5
Crop Production and Exports, 1985-1999, St. Lucia

Year	Production				Exports		
	Bananas (tons)	Copra (tons)	Cocoa (tons)	Crops EC\$M	Bananas EC\$M	Cocoa EC\$M	Non- Trad. Crops EC\$M
1985	83,532	4,393	50		89.53	0.37	
1986	112,540	3,836	47		150.55	0.35	
1987	93,028	4,382	46		113.74	0.34	
1988	135,277	3,516	44		177.43	0.33	
1989	126,634	3,992	29		158.00	0.20	
1990	135,367	4,618	47		186.90	0.33	
1991	100,877	3,655	44	13.9	146.40	0.32	
1992	135,291	3,046	62	15.6	184.80	0.38	
1993	122,927	3,764	53	16.0	137.90	0.40	
1994	90,909	2,867	51	19.8	115.70	0.33	
1995	105,658	2,221	28	18.5	128.10	0.30	3.39
1996	105,547	2,053	29	19.1	125.80	0.19	4.25
1997	71,395	2,859	30	18.1	85.94	0.19	N/A
1998	73,219	1,508	23	22.3	91.50	0.10	3.95
1999	65,196	2,900	21	19.6	87.00	0.15	5.55

Source: Government Statistics Department, Economics and Social Review

Other traditional crops have also experienced similar declining fortunes in recent years. Cocoa production fell from a 1985-1994 average of 47 tonnes, and annual export earnings of \$335 thousand to 26 tonnes and export earnings under \$184 thousand between 1995-1999. Tropical Storm Debbie in 1994, which destroyed an estimated 141 acres of cultivated cocoa, was largely responsible for the decline which occurred in the post-1995 period. The existence of a guaranteed export market for polished cocoa beans offers some incentive for farmers to increase production and exports. The industry has been determined to have the potential to earn at least \$2 million in export revenues. However, in 1999, output was far below its potential, explaining the relatively low level of export earnings, averaging \$150 thousand. Copra production has also been on the decline. Between the 1985-1994 and the 1995-1999 periods annual output fell by 63%, from 3,911 to 2,401 tonnes. The increasing popularity of the domestic trade in jelly coconuts suggests that reversing this downward trend may prove a difficult task.

The non-traditional crop, livestock and fishing sub-sectors reported encouraging, albeit variable performance over the review period. Since the mid-1990s, the value of non-traditional crop output has held at about \$19 million and exports have averaged at about \$4.3 million. However, in 1999 exports jumped by 41%, from \$3.95 million in 1998 to \$5.55 million. This recent growth in exports was partly due to a 33% rise in exports of green bananas to regional markets and significant increases in the prices of hot peppers and breadfruit.

Growth has also occurred in the domestic food market due to population growth, improvements in the standard of living and growth in the hospitality sector. The expansion in domestic demand for locally grown food and the increase in the number of market outlets for local producers of non-traditional crops, including the marketing board, village and city markets, hotels and supermarket chains, has increased opportunities for local producers.

Agriculture continues to be of major importance in the economic development of St. Lucia, in terms of contribution to national output, foreign exchange earnings, balance of payments and employment. Notwithstanding income multiplier effects, the employment contributions of agriculture are far reaching, and are particularly important given the predominance of small and middle size farm units. In 1996 farms of under 5 acres accounted for 26% of agricultural lands, those 5 to 10 acres occupied 21%, while 10 to 25 acre holdings occupied another 18% (Table 18). The banana industry alone, is said to employ (directly and indirectly) roughly 30,000 workers, which represented over 40% of the 1999 labour force.

Agriculture in St. Lucia has been declining, both in terms of relative percentage share in GDP and real growth. Between 1995-1999 agriculture contributed on average, 8.4% of GDP growth, down from an average of just over 13% between 1985-1994. The decline in total agricultural acreage may also be another explanatory factor accounting for the declining share of agriculture in GDP. This decline in total acreage was led by a 12.8% decline in holdings of 25 acres or more. In contrast, the share of farm holdings within the under-25 acre category increased from 47% in 1986 to 65% in 1996, suggesting a more even distribution of agricultural land ownership. In 1996, area under crop production represented 80% of total arable agricultural lands, dominated by bananas (44%), coconuts (29%) and mangoes (6.8%). This structure of production holds far-reaching implications for the performance of both the export and food production agricultural sector.

In 1997, the sector entered its fifth consecutive year of decline, a trend largely reflective of the continued contraction in the banana sub-sector (Table 19). Banana production peaked in 1990 at 135.4 thousand tonnes. The wide spread use of field packing, the construction of feeder roads, the appreciation of the British pound against the US dollar, and a rehabilitation program that sought to raise yields through increased application of fertilisers and pesticides, are some of the factors that helped spur the expansion of the banana industry during the late eighties and early nineties. However, since the mid-nineties the banana industry has experienced a reversal in fortunes that was brought about by the sharp depreciation of the British pound in 1993 and the instability and uncertainty that continue to surround the EU banana regime.

Table 19
St. Lucia, Share and Growth Indicators Agriculture

Real Prices (1990)	1990-94 Avg.	1995	1996	1997	1998	1999
Agricultural GDP Share Per Cent	13.0	11.16	11.10	9.06	9.14	7.4
Agricultural GDP Growth Per Cent	-3.34	4.94	0.79	-17.92	3.86	
- Bananas	-4.54	16.55	-4.61	-32.04	2.30	
- Other Crops	4.62	-20.17	6.91	4.01	1.24	
- Livestock	-7.29	-6.55	31.17	12.02	16.21	
- Fishing	15.46	15.68	21.43	14.89	11.60	
- Forestry	-7.71	-9.85	-10.92	-7.55	-9.69	
Total GDP Growth Rate	3.53	1.03	0.82	0.92		

Source: St. Lucia Government Statistics Dept.

The decline in banana production adversely affected banana exports (Table 20). Agricultural exports in 1999 amounted to EC\$98 million, or 62% of total merchandise exports, and has traditionally been dominated by bananas, earnings of which dropped from \$187 million in 1990 to \$87 million in 1999.

Table 20
Crop Production and Exports, 1985-1999, St. Lucia

Year	Production				Exports		
	Bananas (tons)	Copra (tons)	Cocoa (tons)	Non- Trad. Crops EC\$M	Bananas EC\$M	Cocoa EC\$M	Non- Trad. Crops EC\$M
1985- 89Avg.	91,835	3,353	36	-	114.88	0.27	-
1990	135,367	4,618	47	-	186.90	0.33	-
1991	100,877	3,655	44	13.9	146.40	0.32	-
1992	135,291	3,046	62	15.6	184.80	0.38	-
1993	122,927	3,764	53	16.0	137.90	0.40	-
1994	90,909	2,867	51	19.8	115.70	0.33	-
1995	105,658	2,221	28	18.5	128.10	0.30	3.39
1996	105,547	2,053	29	19.1	125.80	0.19	4.25
1997	71,395	2,859	30	18.1	85.94	0.19	n/a
1998	73,219	1,508	23	22.3	91.50	0.10	3.95
1999	65,196	2,900	21	19.6	87.00	0.15	5.55

Source: Government Statistics Department, Economics and Social Review

Agriculture in St. Lucia faces a number of constraints which limit the nature and pace of production. These constraints have been relatively less manifested in the traditional crop sub-sector due to the relatively more organised support structure. Within recent times, this support structure has undergone significance change. This change was precipitated by the establishment of the Windward Islands Banana Development and Exporting Company (WIBDECO) to replace the Windward Islands Banana Growers Association (WINBAN) in 1994. WIBDECO's function ranged from undertaking market negotiations and marketing of Member country banana exports, to the provision of technical services to the industry to enhance productivity and fruit quality. The Company represented an important medium through which the Windward and Caribbean island banana lobby could be strengthened in Europe. In 1996, WIBDECO and Fyffes Plc., each purchased a 50% stake in the buyout of Geest Bananas, which increased the Windward Islands control and share in the returns in the banana marketing business.

At the national level, the dissolution of the SLBGA in September 1998, through the St. Lucia Banana Growers Association (Dissolution) Act, resulted in a transfer of the assets, liabilities, privileges and obligations of the SLBGA to the St. Lucia Banana Corporation (SLBC). The SLBC was a new privately owned company formed by registered banana growers. Since then, two other private companies have been established and are also engaged in the buying of farmers' fruit for sale to WIBDECO the sole exporter. These are the Tropical Quality Fruit Company (TQFC) and the Agricultural Commodity Trading Company (ACTCO). The SLBC, with an 85% share, dominates domestic buying, followed by the TQFC, with a 15% market share. Given its recent entry in the market, it is too soon to determine the share of the ACTCO. Indications are that further change in the organisation of the national industry may be imminent. Recently, the SLBC has expressed intentions to bypass WIBDECO and sell directly to Geest. WIBDECO has also indicated its intention to undertake direct purchasing from growers.

The restructuring which occurred in the administration of the banana industry over 1995-1999 period should further strengthen the position and attractiveness of bananas relative to non-traditional crops. The existence of such an organisational structure has been one of the major reasons cited why farmers who remain in agriculture have generally remained in banana production as opposed to cultivation of other crops despite the difficulties faced by industry. Some of the other major constraints that the non-traditional agricultural sector faces have been identified as limited land space, low level of technology, an unfavourable land tenure system, poor infrastructure, inadequate finance, poor marketing, unreliable and inconsistent domestic and export markets, and lack of reliable and cost effective shipping to export markets. The success of the banana industry in the 1980s and early 1990s further exacerbated these constraints in that land (sometimes unsuitable), capital and labour were diverted from food to banana production. Also, the growth of the tourism and other service sector industries has pushed up the cost of labour and thus has made the agricultural sector a less attractive source of employment. These reasons thus explain the declining share and growth of agricultural GDP in the 1990s.

Policies and Prospects

In response to declining banana production and the uncertainties surrounding the banana industry, the government is taking steps to improve the competitiveness of the industry, diversify the agricultural sector, and implement a rural program that would arrest the social and economic

dislocation that may result from attempts at transforming the banana industry. The Government's efforts at improving the competitiveness of the industry centre around the Banana Production Recovery Plan endorsed in August 1998 by the governments of the Windward Islands and representatives of the banana industry. Through improved drainage, new irrigation systems and on-farm finance, the plan envisions that by the year 2000 and beyond banana production will be maintained at 110,000 tons per year.

In 1996 the Certified Grower Program was adopted to develop a pool of farmers who consistently produce fruit of the quality and under the conditions required by British supermarkets. Under the Banana Production Recovery Plan certified farmers will receive resources that will allow them to recapitalise their farms, expand their acreage, improve farm drainage and implement new irrigation systems. About 40% of production now comes from certified farmers, and as a result fruit quality has improved considerably. Besides encouraging certified farmers, the government anticipates that about 2200 inefficient farmers, those who are fringe producers or are operating on marginal lands, will move out of bananas. By the end of this restructuring, it is expected that fruit quality and yield would be such as to enable St. Lucian bananas to compete, if not on the basis of price, on the basis of quality and other non-price factors (environmental and labour friendly production, for example).

With a diversified agricultural sector the government hopes to stabilise the economy, increase the net foreign exchange derived from the agricultural sector (by reducing the food import bill and by exporting a wider range of food commodities), and stimulate growth in the whole economy through the linkages that exist between agriculture on one hand and tourism and manufacturing on the other. More specifically, by the year 2005, the government plans to reduce the trade deficit balance on food by 10%, reduce the food import bill by 15%, raise the volume of non agricultural exports by 20%, and increase by 20% the tourist sector's consumption of locally produced food.

The government has taken several initiatives to aid in the accomplishment of these goals. It is revitalising the St. Lucia Agricultural Association to provide assistance to the declining cocoa sub-sector. Assistance is being given to the Coconut Growers Association to hasten its recovery. The government is planning on privatising the retail functions of the marketing board, and establishing a marketing agency within the Ministry of Agriculture that would be responsible for advancing exports of agricultural commodities. The ministry is currently implementing the Rural Economic Diversification Incentives Project as a vehicle for providing credit to agricultural enterprises. With recent improvements in the island's fishery infrastructure and the upgrading of associated institutions the government is expecting the island to become self-sufficient in fish products. Also, besides encouraging the production of non-traditional crops such as cabbage, lettuce, tomato, sweet pepper, cucumber, dasheen, sweet potato, yam, plantain, and cut flowers, the government has embarked on a media campaign, encouraging residents to buy local.

The European Community has promised the government 8.5 million Euros to assist the country in a five-year plan to further commercialise the banana industry, to diversify the agricultural and rural economy, and to implement a rural recovery program. Over half of the money is earmarked for on-farm irrigation and drainage, and \$4.69 million will be used in the first year to establish

an agricultural diversification program that will seek to enhance the marketing of agricultural commodities, facilitate technology transfer, and strengthen farmer organisations. In anticipation of the exit of some 2,200 banana farmers, another \$40.3 million of the funds will be used over the duration of the program to buffer the economic and social dislocation that may result.

Among the initiatives contemplated to stimulate and achieve non-banana agricultural development include:

- the revitalisation of the St. Lucia Agricultural Association to provide assistance to the declining cocoa sub-sector;
- provision of assistance to the Coconut Growers Association to hasten its recovery;
- plans to privatise the retail functions of the marketing board; and
- establishment of a marketing agency within the Ministry of Agriculture responsible for promoting exports of agricultural commodities.

The Ministry of Agriculture is currently implementing the Rural Economic Diversification Incentives Project as a vehicle for providing credit to agricultural enterprises. With recent improvements in the fishery infrastructure and the upgrading of associated institutions, the government is expecting to increase the self-sufficiency levels in fish products. In addition to encouraging the production of non-traditional crops such as cabbage, lettuce, tomato, sweet pepper, cucumber, dasheen, sweet potato, yam, plantain, and cut flowers, the government has embarked on a media campaign, encouraging residents to increase purchases of locally produced foods.

Non-traditional Sector

As part of its plans to expand the economic base of the country, the government has identified tourism and services as the leading growth sectors of the economy. In this regard, the goal is to increase the country's share of the Caribbean tourism market to 5% from its current level of 1.3%. To facilitate the attainment of this objective, \$16.7 million of the 2000 budget was allocated to the marketing of tourism, and gaming would be permitted at some of the island's hotels. To further encourage tourism-related activities, car rentals will be included on the list of items for tax exemption, and new cars used for taxi services may also be afforded duties and consumption taxes exemption.

The economic diversification programme also includes the establishment of an international financial service sector to facilitate the recently opened goods distribution free zone. Within this zone, businesses will enjoy exemption from custom duties, taxes and related charges on goods entering the free zone, exemption from dividend taxes for twenty years and from income taxes the first five years. Plans to establish a second informatics park to provide employment in informatics, including telemarketing, are also in the pipeline.

To comply with the final phase of the Common External Tariff (CET), 1,453 of 6,337 tariff items will require tariff rate increases, while 1,140 will require reductions. Import duties and consumption taxes are important sources of government revenues, and reductions in the CET may result in a decline in tariff revenues by \$4.70 million or 7% of 1998's total (\$67.2m), and a decline in consumption tax by \$0.43 million, a loss of 4% of 1998 total (\$120.1m). Accordingly, the government is planning to impose increases in consumption taxes on targeted import items, to not only offset loss of revenue arising from tariff rate reductions, but also, to generate a net import tax revenue gain of \$10 million.

The government has recognised that although its system of import licensing provides protection for domestic production, it is inherently inefficient and is at odds with the WTO and CET. Consequently, plans are on the way to phase out the import licenses and replace them with tariffs that are consistent with the CET. The recent passage of the Environmental Protection Levy Act imposes a fee on imported goods (excluding clothing, footwear, foodstuffs and pharmaceuticals) to be used to help cover the cost of protecting the environment.

With a diversified agricultural sector and economy, the government hopes to stabilise the economy, increase the net foreign exchange derived from the agricultural sector (by reducing the food import bill and by exporting a wider range of food commodities), and stimulate growth in the whole economy through the linkages that exist between agriculture on one hand, and tourism and manufacturing on the other. More specifically, by the year 2005, the government plans to reduce the trade deficit balance on food by 10%, reduce the food import bill by 15%, raise the volume of non agricultural exports by 20%, and increase by 20% the tourist sector's consumption of locally produced food.

FISCAL POLICY

The government has identified tourism and services as the leading growth sectors of the economy, and as such its goal is to increase the country's share of all Caribbean tourism to 5% from its current level of 1.3%. To help achieve this goal, \$16.7 million of year 2000's budget was allocated to the marketing of tourism. The government's plan to allow gaming at some of the island's hotels is another indication of its tourism focus. Also, as further encouragement, car rental will join gratuities and tips on the list of items on which taxes have been abolished, and new cars to be used for taxi services will soon be exempted from import duties and consumption taxes.

As part of its plans to expand the economic base of the country, the government has established an international financial service sector, and has opened a new goods distribution free zone where businesses will enjoy exemption from custom duties, exemption from taxes and related charges on goods entering the free zone, exemption from dividend taxes for twenty years, and exemption from income taxes the first five years. The government also has plans to establish a second informatics park that will provide employment in informatics, including telemarketing.

MANUFACTURING SECTOR

The manufacturing sector in St. Lucia accounts for approximately 6% of GDP declining from 8% in 1986. It has fluctuated between that range over the period 1986-1998. The sector consists of some comparatively large foreign-owned apparel and electronic component producing firms and smaller locally owned operations producing import substitution goods and agro-processing firms. The range of products from the manufacturing sector include, processed foods, soft drinks, beer, malt, stout, rum, garments, paper products and detergents. 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 1990 and since then the sector has been relatively stagnant contributing on average of 6-7% of GDP.

Contribution to the Economy

In light of the banana situation great emphasis is being placed on tourism, but heavy reliance on tourism could be just as problematic as the current dependence on bananas. A growing and vigorous manufacturing sector could provide a needed counterweight and therefore play a critical role in the country's drive towards diversification. In 1999 the manufacturing sector accounted for \$85 million (value added) or 5.7% of GDP and exports of manufacturing products generated \$47 million or 6% of all exports. Employment in the sector totalled 4,325 workers, representing over 7% of all employed workers. However, the importance of the manufacturing sector in the future will depend on the willingness to invest and the international competitiveness of the industry.

Table 1.6. The Manufacture Sector, Selected Indicators, 1999

Indicators	Values
GDP (factor cost EC\$M)	1,497
Total Export (EC\$M)	159
Total Employment	59,850
Manufacture Output, Value Added, (EC\$M)	85
Manufacture Export (EC\$M)	47
Manufacture Employment	4,325
% Manufacture of GDP	5.7
% Manufacture Export of Total	29.4
% Manufacture of Employment	7.2

Source: St. Lucia Government Statistics Dept.

Industry Structure

Based on their potential to be internationally competitive and to contribute to the economy the manufacturing industry in St. Lucia can be divided into enclave, traditional import substitution, and agro-processing firms. The enclave sector produces mostly apparel, textile, and electronic components for export, mainly to the US. The enclave firms could themselves be a source of economic instability since they tend to be footloose and cater for volatile export markets where

technological changes, recessions and lower wages elsewhere can quickly erode their competitiveness.

The production of the import substitution sub-sector is geared mainly to the local and regional markets, and includes beverages, paper and paperboard products, chemicals, and plastic and rubber products. This sector is considered to be highly uncompetitive and depends on high levels of effective protection for its survival. The protections in turn are anti-export bias and encourage inefficient production.

The agro-processing sector makes use of mostly locally produced agricultural products for its raw material. Fruit jams, sauces, condiments, confectioneries, banana chips, milk and meat products, spring water, pasta products, copra and its derivatives are some of the products that are being processed. The sector is said to be suffering from excess capacity, outdated technology, and low level of technical skills. However, because of the sector's backward linkages with agriculture and forward linkages with tourism it is in a good position to spur sustained industrial development. Moreover, the potential may exist for the sector to become internationally competitive in certain niche markets.

The manufacturing sector in St. Lucia comprises mostly of small firms. Of the 173 enterprises in operation, 94 employ less than 10 workers. Many of the smaller firms are found in the furniture and agro-processing sectors. For example, in the furniture sub-sector there are 40 firms employing an average of 6 workers, while in agro-processing there are 19 firms employing an average of 18 workers. In contrast, there are only 7 firms employing more than 100 workers, and most of them are concentrated in the electronics and garment sub-sectors. During the 1994-1999 period agro-processing represented 37% of manufacturing, paper and paperboard 27%, electronics 13%, garment and textile 9%, chemicals, plastic and rubber 8% and lumber and lumber products 1.0%. In recent years there has been notable declines in the garment, and paper and paperboard sub-sectors (Table 1.7).

Table 1.7
Share of Manufacturing Production, 1985-1990, 1994-1999, St. Lucia.

Sectors	1985	1986	1987	1988	1989	1990	1994	1995	1996	1997	1998	1999
<i>Manufacturing Production EC\$000</i>												
Agro-processing	37791	41846	47714	49030	56413	53652	39662	47882	47119	55917	50944	63596
Apparel and Textile	13033	14191	18396	20571	20663	17906	11940	11850	16086	11162	11118	11625
Paper and Paperboard	41241	37260	38948	53518	47324	47736	37101	50173	45039	29618	30818	26031
Electronics	5728	8393	8262	9167	10740	12081	13990	14725	16578	16291	21553	23905
Chemicals, Plastics, and Rubber	1308	2583	2466	2498	2844	2433	8377	7055	12407	16034	12668	12115
Lumber and Lumber Products	63	57	33	20	18	19	0	0	1954	2382	2548	2778
Misc. Manufacture	1987	1733	1994	1905	1877	1925	7551	6486	2495	3635	9636	9181
<i>Percent of Total Manufacturing</i>												
Agro-processing	37.4	39.5	40.5	35.9	40.3	39.5	33.4	34.7	33.3	41.4	36.6	42.6
Apparel and Textile	12.9	13.4	15.6	15.0	14.8	13.2	10.1	8.6	11.4	8.3	8.0	7.8
Paper and Paperboard	40.8	35.1	33.1	39.1	33.8	35.2	31.3	36.3	31.8	21.9	22.1	17.4
Electronics	5.7	7.9	7.0	6.7	7.7	8.9	11.8	10.7	11.7	12.1	15.5	16.0
Chemicals, Plastics, and Rubber	1.3	2.4	2.1	1.8	2.0	1.8	7.1	5.1	8.8	11.9	9.1	8.1
Lumber and Lumber Products	0.1	0.1	0.0	0.0	0.0	0.0	0.0	0.0	1.4	1.8	1.8	1.9
Misc. Manufacture	2.0	1.6	1.7	1.4	1.3	1.4	6.4	4.7	1.8	2.7	6.9	6.2

Source: Economic and Social Review

Contribution and Performance

Based on the experience resulting from the over-dependence of agriculture on the banana industry, the economic diversification programme recognises the need to place equal emphasis on other sectors of the economy. While tourism has received much attention, in recent years similar emphasis was to be placed to develop a growing and vigorous manufacturing sector. The manufacturing industry in St. Lucia can be divided into enclave, traditional import substitution, and agro-processing firms. The enclave sector produces mostly apparel, textile, and electronic components for export, mainly to the US. The enclave sub-sector is considered internationally competitive, but its contribution to the economy is limited since (because most of their inputs are imported) the value it adds to real output is low. This feature of the enclave sub-sector increases its vulnerability to external instability and their longevity is closely tied to their ability to keep pace with rapid technological change in export markets and maintain their low-cost labour-based competitive advantage.

These features of the manufacturing sector largely explain its relatively low contribution to gross value added (Table 21). Since the 90's the performance of the manufacturing sector has been lackluster. Between 1990-1995, annual real growth averaged 1.5%. During this period, the sector reported negative growth between 1991 and 1994, recovering somewhat to achieve a 5% increase in activity in 1995 from 1994. This recovery was short-lived as the sector registered a negative growth between 1996 and 1999. As a consequence, manufacturing as a share of GDP declined from a high of 8% in 1990 to 5.7% in 1999.

Table 21: St. Lucia, Share and Growth Indicators, Manufacturing Sector

Real Prices (1990)	1990-94 Avg.	1995	1996	1997	1998	1999
Manufacturing GDP Share Per Cent	7.49	7.02	6.45	6.39	6.08	5.7
Manufacturing GDP Growth Per Cent	-2.23	5.93	-6.78	-0.33	-2.11	
Total GDP Growth Rate	9.13	1.03	0.82	0.92	2.87	

Source: St. Lucia Government Statistics Dept.

PRODUCTION AND EXPORT PERFORMANCE

Since the 90's the performance of the manufacturing sector has been lackluster. During the 1985-1990 period the sector grew by an annual average of 12%. The following five years, 1991-1995, growth slowed to 3%, and in the latter half of the 90's the sector registered a negative growth rate of 1.0%. As a consequence manufacture's share of GDP declined from a high of 8.2% in 1985 to 5.7% in 1999 (Table 1.8).

Table 1.8
Manufacturing Output, 1985-1999, St. Lucia

Year	GDP EC\$M	Manufacturing EC\$M	% Manuf. Of GDP	Manufacture Growth %
1985	527.3	43.4	8.2	
1986	631.8	50.0	7.9	15.2
1987	677.4	55.5	8.2	11.0
1988	763.6	62.2	8.1	12.0
1989	866.7	69.5	8.0	11.8
1990	951.1	77.6	8.2	11.7
1991	1,019.6	82.2	8.1	5.9
1992	1,129.7	82.0	7.3	-0.3
1993	1,137.3	82.3	7.2	0.4
1994	1,191.1	76.7	6.4	-6.8
1995	1,280.4	88.8	6.9	15.8
1996	1,298.8	87.7	6.8	-1.3
1997	1,337.9	84.9	6.3	-3.1
1998	1,425.7	82.4	5.8	-3.0
1999	1,496.6	84.9	5.7	3.0

Source: St. Lucia Government Statistics Dept.

Contraction in the Garment and paper and paper sub-sectors has been mostly responsible for the recent decline in the manufacturing sector. Garment and textile production declined from over \$20 million in 1989 to under \$12 million in 1999. Similarly, between 1988 and 1999, output of paper and paperboard products fell from \$53.5 to \$26 million. In sharp contrast, the agro-processing and electronic sub-sectors showed steady growth. For example, between 1995 and 1999 the agro-processing sub-sector grew in value terms by an annual average of 10.8%, while the electronics sub-sector grew by 11.8%.

The decline in the paper and paperboard sub-sector is a result of recent contractions in the banana industry, the sector's largest customer of cardboard boxes. On the other hand, the garment industry's performance can be explained by (1) the erosion of CBI preferences as a result of the North American Free Trade Agreement and the resultant transfer of foreign-owned garment assembly firms to Mexico; and (2) the shifting of production to lower wage and lower unit labor cost CARICOM, Latin American and Asian countries. As a result of sharp declines in exports of garments, as a whole, exports of manufactured products have fared even worse than production. Between 1995 and 1999 exports of manufactured products contracted by an annual average of 16%, and the sectors share of total exports fell from 35 to 29% (Table 1.9).

The small share of manufacturing in GDP is also a factor of the predominance of small sized firms. In 1999, the sector accounted for 7% of the employed labour force, representing 4,325 workers. Of the 173 enterprises in operation, 94 employ less than 10 workers. Many of the smaller firms are found in the furniture and agro-processing sectors. For example, in the

furniture sub-sector, there are 40 firms employing an average of 6 workers, while in agro-processing there are 19 firms employing an average of 18 workers. In contrast, there are only 7 firms employing more than 100 workers, and most of them are concentrated in the electronics and garment sub-sectors. During the 1994-1999 period, agro-processing had the largest share (37%) of the manufacturing sector, followed by paper and paperboard (27%). With the exception of the electronics, the other industries averaged less than 10% of the manufacturing sector (Table 22).

The decline in the garment, and paper and paperboard sub-sectors within recent times have been the most evident, and was largely responsible for the decline in the manufacturing sector. In sharp contrast, the agro-processing and electronic sub-sectors showed steady growth. For example, between 1995 and 1999 the agro-processing sub-sector grew in value terms by an annual average of 10.8%, while the electronics sub-sector grew by 11.8%.

The decline in the paper and paperboard industries resulted from the recent contractions in the banana industry, the industry's largest consumer. On the other hand, the garment industry's performance can be explained by (1) the erosion of CBI preferences as a result of the North American Free Trade Agreement and the resultant transfer of foreign-owned garment assembly firms to Mexico; and (2) the shifting of production to lower wage and lower unit labour cost CARICOM, Latin American and Asian countries. As a result of sharp declines in garment exports, exports of manufactured products have fared even worse than production. Between 1995-1999 exports of manufactured products contracted by an annual average of 16%, and the sectors share of total exports fell from 35% to 29% (Table 19).

Table 1.9. Manufacturing Exports, 1995-1999, St. Lucia

Year	Total Exports EC\$M	Manufacture Exports EC\$M	% Manuf. Exports of Total	Manufacture Export Growth %
1995	294.2	103.5	35.2	
1996	214.7	55.8	26.0	-46.1
1997	165.4	52.4	31.7	-6.0
1998	167.9	48.9	29.1	-6.6
1999	159.1	46.7	29.4	-4.5

Source: St. Lucia Government Statistics Dept.

Constraints to the Development of Manufacturing

The manufacturing sector in St. Lucia 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. St. Lucia is by no means a low wage area. The boom in prices of traditional agricultural exports during the 1980s pushed up the price of agricultural and had a demonstration effect on the other sectors. Thus the type of manufacturing sector which emerges must take this as a given. Moreover higher remuneration in the tourism sector has tended 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 unreliably. 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, St. Lucia 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 treaty¹.

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

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.

that the process favours foreign investment over local investment. Some regulations and legal requirements 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 St. Lucian 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. St. Lucian exports face a myriad of regulations which only experience in the markets can help to get around. Many firms are seeking ISO and other international 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.

A recent study conducted by UNCTAD identifies a similar list of constraints affecting the competitiveness of the manufacturing sector. These include (1) Human Resources: poor work ethic and shortage of skill workers. (2) Government Institutions: arbitrary allocation and slow granting of fiscal incentives; considerable delays in customs clearance and issuing work permits; weak technical assistance for small firms, export promotion, and quality control. (3) Finance:

lack of working capital financing which hampers bulk imports and purchases of good quality inputs; and lack of medium-term capital, hindering technological improvements. (4) Infrastructure: high cost of utilities (electricity, water, and telecommunications); high port and shipping charges; poor maintenance of factory shells and roads in industrial estates. (5) Productivity--diseconomies of scale for domestic firms producing exclusively for domestic market; obsolete machines; lack of proper production records, inventory of raw materials, tracking of work in progress and machine maintenance records; operators' performance hampered by cramped space, poor layout of work areas. (6) Quality Control: lack of standards specifications, and purchasing of low quality inputs.

Among its recommendations, the study advises that the country needs a new industrial policy that focuses on exploiting possibilities for efficient import substitution; that promote industrial deepening through technological upgrading and increasing linkages with other sectors, namely, agriculture and tourism; that engages in industrial targeting, by identifying and encouraging the most promising sub-sectors, in terms of their market prospects and potential contribution to the economy's value added, employment, and exports. In this regard, the study suggests three sub-sectors for industrial targeting. The first is informatics, especially the high-end side of it. Second, agro-processing, partly because of its strong backward linkage to agriculture and its forward linkage to tourism. Third, electronics, because of its high employment effect, moreover, it is already an internationally competitive sector.

Strategy for Revitalisation of Manufacturing

The 1998 MTESP identifies three broad areas in which action will be taken to revitalise the manufacturing sector.

- (i) *Establishment of linkages between manufacturing and other sector.* The provision of incentives for the forging of linkages between tourism operators and agro-processors via the establishment of demand/supply contracts.
- (ii) *Enhancement of the capacity of the Small Enterprise Development Unit (SEDU).* To encourage the trend toward the development of locally owned enterprises the SEDU was strengthened to provide assistance in the areas of marketing and sourcing of specialised technical assistance. But this just part of the institutional strengthening which is being financed by STABEX resources. Other agencies include, the Chamber of Commerce, the Small Business Association and the National Development Corporation.
- (iii) *Provision short-term Protection.* Recognising that many firms would not be able to immediately withstand the competitive pressures of a changing international environment, the Government has promised to use legitimate mechanisms under the existing treaty arrangements to provide breathing space for firms in the embattled manufacturing sector.

Fiscal Policy

For its part, in recent years, the government has put in place a number of initiatives to promote manufacturing activity on the island, and has several other proposals under consideration. An informatics park has been established in the north on which there are now four firms, employing a total of 335 workers. Plans are under way to establish another Informatics Park, this time in the south of the island. Import duties and consumption taxes have been removed on machinery, equipment, and raw materials imported by new business start-ups. Such duties and taxes have also been removed from business surveillance and security equipment, and from all building materials and equipment purchased to repair, rehabilitate and renovate places of business.

To better serve businesses and the manufacturing sector, plans are underway that would strengthen and expand the role of the Small Business Enterprise Development Unit, the St. Lucia Small Business Association, the Chamber of Commerce, the National Research and Development Foundation, and the National Development Corporation. In addition, the government has plans to establish an International Business Information Centre within the Ministry of Commerce, International Financial Services and Consumer Affairs. It is hoped that the newly established goods distribution free zone will help spur industrial development, especially in the south of the island. Assistance is now being given to the Coconut Growers Association in an attempt to hasten the recovery of the copra and derivatives manufacturing sub-sector. The government has embarked on a *Buy Local* campaign that encourages locals to patronise the products of local farmers and manufacturers.

The government has taken steps to improve the efficiency of several key institutions that have a direct impact on the functioning of the manufacturing sector. The customs department is now being overhauled. Water supply provision has been privatised. The telecommunication industry is being reformed and the process has already resulted in significant Internet and telephone rate reductions. A commission of inquiry has been set in motion to find ways of improving the quality and reducing the cost of electricity services.

Among CARICOM countries, St. Lucia is said to have the largest number of product categories under import licenses. These licenses were instituted to provide protection for domestic production. However, these licenses are inherently inefficient, they undermine the drive towards international competitiveness, and they are at odds with WTO and CET rulings. In recognition, the government is planning to phase out the import licenses and replace them with tariffs that are consistent with the CET.

Policies and Prospects

The ability of the manufacturing sector to expand and increase its contribution to GDP depends, in part, on the willingness to invest and the ability to increase the international competitiveness of its products. In recent years, the government has put in place a number of initiatives to promote manufacturing activity and has several other proposals under consideration. An Informatics Park has been established in the north on which there are now four firms, employing a total of 335 workers. The establishment of another Informatics Park in the southern part of the island is also on the development agenda.

Incentives to manufacturing are in the form of the removal of import duties and consumption taxes on machinery, equipment and raw materials imported by new business start-ups. Such duties and taxes have also been removed from business surveillance and security equipment, and from all building materials and equipment purchased to repair, rehabilitate and renovate places of business.

In terms of institutional capacity, the government has also taken steps to improve the efficiency of several key institutions that has a direct impact on the functioning of the manufacturing sector. The customs department is now being overhauled. Water supply provision has been privatised. The telecommunication industry is being reformed and the process has already resulted in significant Internet and telephone rate reductions. A Commission of Inquiry has been set in motion to find ways of improving the quality and reducing the cost of electricity services.

Measures are being taken to strengthen and expand the role of the Small Business Enterprise Development Unit, the St. Lucia Small Business Association, the Chamber of Commerce, the National Research and Development Foundation, and the National Development Corporation to improve services to the commercial and manufacturing sectors. The Coconut Growers Association has been provided with assistance in an attempt to hasten the recovery of the copra and derivatives manufacturing sub-sector. The government has embarked on a *Buy Local* campaign that encourages locals to patronise the products of local farmers and manufacturers. In addition, the government plans to establish an International Business Information Center within the Ministry of Commerce, International Financial Services and Consumer Affairs. It is hoped that the newly established goods distribution free zone will help spur industrial development, especially in the south of the island.

TOURISM

Stay-over visitors arrivals grew consistently over all periods of analysis. During the 1986-89 period stay-over visitors grew by 8.4% to 120,756. Cruise-ship passenger arrivals also grew strongly during this period by 19.2% during this period to 82,745. As a result of this robust growth in visitor arrivals, visitor expenditure rose by 10.2% to \$224.9m.

During the 1990-94 period, stay-over visitors recorded positive growth of 10.9% to 177,231 while cruise ship passengers arrivals decelerated to 12.44% or 152,004. The slowdown in cruise ship passenger arrivals reflected an impasse in negotiations with the Florida Cruise ship Association over passenger head tax rates. The stronger growth in stay-over visitor arrivals compensated for the lower growth in cruise ship passenger arrivals and contributed to a 16.9% rise in visitor expenditures to \$440.4m.

A sustained marketing and promotional effort during the 1995-98 period including the annual staging of a Jazz Festival contributed to the 15.4% increase in stay-over visitors to 285,529. Cruise ship passenger arrivals to the destination also rose on average by 24.3% 264,600. Visitor expenditure grew on average by 7.6% to \$673m.

The increased role of tourism, which accounted for the majority of service exports revenues resulted in a rising service penetration index. This index increased from 1.1 during 1986-89 to 3.9 by 1995-98.

The USA maintained its leadership share of stay-over visitors to the destination across all periods. This share however declined over time as other destinations increased in importance. During 1986-89 Stay-over visitors from the USA accounted for 31.3% of all stay-overs, followed by the Caribbean and UK (22.0%), and Canada (11.5%). During 1990-94 the USA's market share declined to 29.0% but still maintained leadership. This was followed by visitors from the Caribbean 23.9% and the UK at 23.4%. The Canadian market accounted for 7.9% during this sub period. By 1995-98 the USA, Caribbean, UK and Canadian market shares were 29.3%, 20.7%, 20.1% and 4.8% respectively.

Contribution to GDP

The tourism industry as represented by the hotels and restaurant sector increased its relative contribution to GDP from 9.8% to 10.3% to 12.3% respectively over the three periods of analysis. Real GDP growth reflected the maturing of the tourism product with highest growth being experienced during 1986-89 (9.6%). This growth declined over the subsequent two sub periods of analysis to 7.2% and 5.4% respectively. This outturn reflected in part the international recession of the early 1990s and the evolution of the product towards being more all-inclusive which has a lower level of value added.

St. Lucia considerable of competitive advantage in Tourism, by virtue of its natural, historical and cultural resources; its relatively pristine environment; and its proximity to the major North American market. However, the sector is plagued by some major weaknesses Included among these weaknesses are the following:

- (i) Vulnerability to economic shocks in the source markets, as well as its susceptibility to natural disasters.
- (ii) An over-reliance on foreign airlines to bring visitors to the region; the attendant unpredictability of the services provided by these airlines; and the unreasonable restrictions placed by these airlines, on seat availability;
- (iii) The high import content of tourism expenditure leading to leakage of precious foreign exchange earnings;
- (iv) Insufficiency of rooms;
- (v) Inadequate/inappropriate policy, planning and institutional mechanisms to enable the adoption of integrated approaches to tourism development, that balance economic growth with human and social development, and preserve the natural environment, cultures, and heritage of local communities;

- (vi) The absence of effective measures to strengthen backward and forward linkages between Tourism and other productive sectors of the economy;
- (vii) A lack of diversity in the entertainment content of the tourism product;
- (viii) Limited opportunities for meaningful participation by the local populace in the industry;
- (ix) Slow rate of technology transfer to sector.

The tourist industry in St. Lucia is interestingly poised to really take off with the aid of effective planning and the adoption of new technology. Technology can be used to enhance the natural attributes of the country. The advantages of adoption of new technology can come from improvement of the product offered, marketing and improving the value-added by the sector. Modern technology can allow hotels to recreate the office environment of business executive right in his room via the use of the Internet and telecommunications. Thus opportunities for extended working vacations and even long distance telecommuting are possibilities that can be investigated. Few hotel rooms offer Internet services on demand or even data ports on the standard telephone system. These ancillary services add value to the tourism product but technology can also be used to capture and market aspects of the culture of the country and made available to the itinerant population which serves to extend the local market several times the permanent population.

The marketing of the sector via the Internet has only scratched the surface of the potential of this media. A recent presentation by the Internet firm Travelocity was met with much scepticism by the regional tourism officials at a CTO conference in 2000. The Internet affords smaller hotels the opportunity to have global reach that will be too expensive to obtain via other media. V-SAT technology allows for easier making of hotel reservations which can be used for international hotel chains similar to the call-centre activity. The liberalisation of the telecommunications sector and the consequent reduction in the price of telecommunications services is a prerequisite for exploiting these advantages.

Role of Foreign Direct Investment

Foreign Direct Investment (FDI) has been critical to the development of the tourism industry. These inflows rose as a per cent of GDP from 5.9% during 1986-89, to 9.6% during 1990-94 and declining slightly to 8.2%. Equity inflows were highest during the infancy of the tourism industry at 68.6% of total inflows. These declined to 4.5% during 1990-94 but rose to 18.2% by 1995-98. The variability in these flows reflects the cyclical nature of the FDI related projects.

Land sales in FDI are highly correlated with hotel construction although they also reflect investment by nationals abroad and non-nationals in residential construction. These sales rose from 10.2% to 14.7% during 1986-89 and 1990-94 respectively. However there was a decline by 1995-98 to 7.9%.

CONSTRUCTION

Recent Economic Developments

The construction sector has also increased its role in the economy over time. As a percentage of real GDP this sector contributed 6.9% and grew at 18.9% during 1986-89. Major projects during this period included the development of the Castries harbour, the Pointe Seraphine tourist complex and the West Coast Road and related feeder road projects. There was also strong activity in residential and commercial property development.

Although the construction sector's relative contribution rose to 7.9% during 1990-94, real growth fell to 4.0%. This reflected completion of a number of large public and private sector investment projects. In the private sector, two large hotels (Royal St. Lucian and Jalousie) and a shopping mall were completed while in the public sector construction work at the air and seaports were completed.

Despite an increase in relative contribution to 8.4% of real GDP the construction sector demonstrated very weak growth at 0.6% during 1995-98. This decline in growth reflected the project cycle as a number of large projects were completed during the previous period. These included the improvements to the Hewnaorra and Vigie airports, the construction of the John Compton Dam, the West Coast Road and a liquid waste disposal facility.

TRANSPORTATION

Activity in the transportation sector is highly correlated to developments in the tourism industry and the project cycle in both the private and public sectors. The transportation sector grew by 9.6% during 1986-89 and accounted for 11.2% of real GDP. This was also a period of robust growth in both stay-over and cruise ship passenger arrivals.

The relative contribution of the sector however declined to 10.3% during 1990-94 but rose to 10.8% by 1995-98. Growth in the sector in these two periods was 1.9 and 2.2% respectively. The slower growth in the early 1990's reflected the impact of a recession on visitor arrivals as well as a lower number of cruise ship passenger calls.

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 countries². Many of these contracts date well into the new millennium.

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.

The telecommunications reform occasioned by the re-negotiation of the licenses and continued advances in technology will usher in major changes in the industry for which the country needs to be prepared.

Recent Performance

The communications sector increased in relative contribution from 4.0% during 1986-89 to 6.9% during 1990-94 to 8.6% by 1995-98. The late 1980's recorded the strongest growth at 21.3%. Re-invested earnings in FDI flows during the period accounted for 8.6% of all inflows.

The sector maintained double-digit growth (17.2%) during 1990-94 as re-invested earnings increased its share in FDI inflows at 32.3%. Although re-invested earnings rose in their contribution to FDI flows (47.6%) during 1995-98, real growth slowed to 2.2%.

Telecommunications is already the fastest growing area in St. Lucia and its increased contribution to GDP has largely offset the decline in the contribution of agriculture in recent years. For the OECS as a whole, over the period 1977 to 1998, the contribution of agriculture to GDP declined from 19.8% to 8.5% while the contribution of communications have grown from 2.1% to 9.7%. Hence any prices stimulus that increases demand and hence the equilibrium quantity of telecom services would be adding to an already dynamic leading sector. In examining the effect which the reform process would have on the GDP for the OECS, it is important to recognise the role which telecommunications play in economic development. In doing so, it is imperative that one examines the sector's contribution to GDP over a given period of time.

St. Lucia like the other OECS countries which have 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 regions value of services produced. As was mentioned

² 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.

earlier, expansion in areas such as the informatics industry would have a positive impact on the regions 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 and with little interaction with domestic residents. It is rather limiting for 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 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 (see appendix I). 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 as shown in Appendix I.

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 deferment, 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 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 St. Lucia

St. Lucia is a relative newcomer to the offshore financial services industry. Although the legislation has been under consideration for some time, it was only passed in 1999. The legislation provides for the establishment of Trusts, IBCs, Insurance, Registered Companies, Banking and Mutual Funds.

Hence when the offshore centre is fully operational, the services would be provided through a network of Licensed Registered Agents who will be responsible for due diligence with respect to their clients. The registration services would be provided by the through an online Registry offering 24-hour service. The Website will be hosted in St. Lucia and would feature advanced encryption.

There will be a strong regulatory framework which accompanied by the Ant-money Laundering Act should measure up to international standards.

Domestic Financial Services

Due to the unavailability of information on other financial services this section would concentrate on the banking sector. The role of banks in the financial sector rose in prominence over the periods of analysis. Banks contribution to real GDP was 6.8%, 7.7% and 9.4% respectively across the three periods of analysis. Real growth in the sector reflected developments in the macro economy with the strongest growth being realised during 1986-89 (16.5%). Total banking sector assets rose by 17.0% to \$645.4m. Loans accounted for over 65% of total assets.

By 1990-94 growth in the banking sector however slowed to 4.7% due to the impact of a global recession and a deterioration in the terms of trade for primary exports. Despite a lower overall growth, banking sector assets grew by 10.2% while loans share in total assets increased to 74.3%.

By 1995-98 real growth increased to 6.9% with a surge in residential and commercial construction. Total assets of the banking sector grew by 7.9% while loans further increased its share to 81.2%.

Growth in domestic credit rose by 15.2% during 1986-89 and was allocated mainly to the private sector. Net credit to the Central Government declined during this period. The Central Government generated sizeable current account surpluses that were utilised in financing public sector investment. By 1990-94 growth in domestic credit although in double digits (11.5%) grew at a slower rate than in the previous period. Growth in private sector credit rose by 10.7% while that to Central Government declined due to the continued strong fiscal performance. The Central Government was a net depositor to the banking system. There was a further deceleration in the growth in domestic credit during 1995-98 to 8.5%. Most domestic credit was allocated to the private sector as the Central Government, non-bank financial institutions and other public sector were net depositors to the banking system.

Total Monetary liabilities (M2) grew by 19.4% during 1986-89 and stabilised between 7.0-8.0% during 1990-94 and 1995-98. Savings deposits accounted for the majority of deposits in the banking system. The faster growth in credit relative to monetary liabilities resulted in an increased tightening in liquidity conditions over time from 79.1%, to 86.5% to 96.7% respectively over the three periods of analysis.

TRADE LIBERALIZATION

St. Lucia is simultaneously taking part in a number processes of trade liberalisation. The first results from the deepening of the CARICOM Integration movement which has resulted in a phased reduction of the CET. At the same time the country is participating in a number of international negotiations which would lead to freer trade. These include the FTAA, the post Lomé IV, the millennium round of the WTO and a number of CARICOM sponsored trade liberalisation negotiations.

STATUS OF THE CET

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.

These factors determined the principles guiding the design of the new tariffs:

- i. international competitiveness;
- ii. efficient production for the regional market;
- iii. the preservation of government revenues;
- 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. there should be uniform rates for the same items notwithstanding their economic use;
- vii. the special needs of LDCs should be taken into account;
- viii. the tariff structure should be simplified with fewer rate bands with less room for discretionary application.

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

January – June, 1993	0 – 5% to 30/35%
January – June, 1995	0 – 5% to 25/30%
January – June, 1997	0 – 5% to 20/25%
January – June, 1998	0 – 5% to 20%

St. Lucia has implemented Phase II of the CET and intends to move directly to Phase IV. Proposals for putting Phase IV into effect are presently being reviewed. A committee has also been set up to review proposals for compensatory measures to recover revenue lost.

No action has been taken regarding Article 56 items. The issue of tariffication has also not been addressed and should be considered following the outcome of a study to be undertaken.

St. Lucia has implemented the ASYCUDA system. However, a number of difficulties have been experienced with its functionality:

- current capacity precludes processing during normal working hours;
- commodity lists are not available in a format usable by the system and have to be compiled online separately;
- considerable processing time is required since two data bases covering half year's data have to be maintained because of inadequate storage capacity;

To overcome these problems source documents were re-entered in the statistical system as trade data from which simulations were made of the effect of tariff adjustments. Problems were also encountered in converting from HS93 format to HS96 format because of imperfect correlations between the two.

The proposals for putting Phase IV into effect took account of the following guidelines:

- revenue loss from the reduction of import duty would be compensated for by an increase in consumption taxes;
- the opportunity should be taken to simplify the consumption tax by reducing the number of bands from nineteen to eight and the range of rates from 0% - 95% to 0% - 35%;
- the effect on food items, clothing, medicines, basic education material and petroleum fuels should be revenue neutral;
- the inflationary impact should be low;
- there should be a reasonable degree of protection for domestic production.

The proposals contained two recommendations that would yield an estimated \$10.0 million, \$4.9 million over the actual revenue loss, as follows:

1. A general 5.0% increase in the consumption tax, including computers which were formerly zero rated, and higher increases for items in which the import duty loss exceeded the value of the general increase.
2. Broadening the excise duties to include motor vehicles, alcohol and explosives.

Import duties and consumption taxes are important sources of government revenues. In 1998 the government collected \$67.2 million in import duties and \$120.1 million in consumption taxes, together, representing 47.6% of tax revenues. To comply with the final phase of the Common External Tariff (CET), 1453 of 6337 tariff items will require tariff rate increases, while 1140 will require reductions. Government economic planners estimate that the CET will cause tariff revenues to fall by \$4.70 million or 7% of 1998's total, and consumption tax to decrease by \$0.43 million, a loss of 4% of 1998 consumption tax revenues. Accordingly, the government is planning to impose increases in consumption taxes on targeted import items not only to offset loss of revenue arising from tariff rate reductions but also to generate a net import tax-revenue gain of \$10 million.

The government has recognised that although its system of import licensing provides protection for domestic production, it is inherently inefficient and is at odds with the WTO and CET. Consequently, plans are on the way to phase out the import licenses and replace them with tariffs that are consistent with the CET. Additionally, the government recently passed the Environmental Protection Levy Act whereby a fee to be used to help cover the cost of protecting the environment will be imposed on imported goods (excluding clothing, footwear, foodstuffs and pharmaceuticals).

REVENUE EFFECTS OF THE CET

The following simulations were undertaken to determine the impact of varying the rates of the CET on the agricultural sector consequent on the tariffication of the quantitative restrictions (QR).

The Common External Tariff (CET) represents an attempt by CARICOM countries to promote industrialisation in the region and to harmonise their trade policies as a first step in meeting the challenges of global competition and trade liberalisation. The CET proposes that all CARICOM members should apply common tariffs on imports from non-CARICOM countries. Starting in 1993, the CET was to be implemented in four phases.

By the end of the last phase, which was adopted for implementation by 1998, all CARICOM countries should have had the following CET rates (on non-CARICOM imports) in place: (1) a 0-5% import tariff on non-competing, primary, intermediate, and capital inputs; (2) a 10% tariff on competing primary inputs and capital goods; (3) a 15% tariff on competing intermediate inputs; (4) a 20% tariff on non-competing final goods; and (5) a 20% tariff on garments, general manufactures and agro-industry commodities. For most CARICOM countries to meet the requirements of the CET, they would need to decrease import tariffs on some items and increase it on others. Declines in imports arising from tariff rate increases may suggest the extent to which CARICOM production is being substituted for non-CARICOM imports. On the other hand, tariff rate decreases imply loss of tariff revenues that member countries may need to make up for by increasing non-CET import taxes.

This section analyses the effect of changes in CET rates on OECS tariff revenues, and non-CARICOM agricultural imports. OECS imports were grouped in accordance with seven CET rate brackets: 0%, 0-5%, 5-10%, 10-20%, 20-30%, 30-45%, and >45%. The Analysis will help

OECS policy planners to anticipate, in the presence of CET rate changes, the extent to which CARICOM production would substitute for non-CARICOM imports, and the amount by which non-CET import taxes would have to rise to keep net import tax revenues unchanged. To conduct the analysis, the study employed a simulation exercise in which the CET rate on non-CARICOM agricultural imports was increased by 5, 10 and 15%. Next, CET rates were adjusted to ensure that commodities in each rate group faced a CET rate of 100%.

For the purposes of this exercise, the CET rate increases and adjustments were applied only to commodities that fell within the CET rate brackets of >20% (20-30%, 30-45%, > 45%). The study assumes that non-CARICOM imports entering the OECS face symmetric unitary import demand elasticities. The elasticities are symmetric in that a given percentage increase or decrease in CET rates (or in import prices) would produce the same magnitude of change.

In 1997, OECS (excluding Antigua) imports of agricultural commodities from non-CARICOM countries amounted to \$232.62 million. About 54% of these imports faced no import tariffs, 21.4% faced import tariffs of 5% or less, 4.9% faced rates ranging between 5 and 10%, 4.2% faced rates between 10 and 20%, and another 15% faced tariff rates in excess of 20%. Over \$15 million in CET revenues were collected, representing 41% of all import taxes. Commodities falling in the >20% rate groups accounted for a disproportionate 80% of the CET revenues.

The simulation results suggest that the CET rate increases on commodities in the >20% rate groups would cause imports to fall, CET tariff revenues to rise, and the resulting decline in imports would cause non-CET import tax revenues to decline. However, increases in CET revenues would more than offset non-CET revenue losses. For example, a 10% increase in the CET rate would cause OECS imports to fall by 1.2%, CET revenues to rise by 15.3%, or \$2.40 million, and net import tax revenues to rise by 6%, or \$2.25 million.

In 1997 St. Lucia imported \$83 million worth of agricultural commodities from non-CARICOM countries, representing a slight increase of 1.6% from the previous year. The share of imports falling in the various tariff rate groups remained relatively constant. For example, the share of imports associated with tariff rates of 5% or less increased by only 1.0% to 68.8%, while the share accounted for by the >20% rate groups decreased slightly from 23.5 to 23.3%. Consequently, there was very little change in CET and total import tax revenues. CET revenues totaled \$7 million, or 54% of all import taxes. The >20% rate groups accounted for 89% of all CET revenues.

Among the >20% rate groups, in 1997 the 20-30% rate group had an average tariff rate of 27.6%, the 30-35% group an average rate of 35.8% and the >45% group had an average rate of 48.5%. These average rates were quite similar to those obtained in 1996.

A 5% increase in CET rates among the >20% commodity rate groups would cause imports to fall by 0.9%, CET revenues to rise by 9.9%, and net import tax revenues to increase by 5.3%, from \$13.1 million to \$13.8 million. Similarly, a 10% CET rate increase would induce a 1.8% decline in imports, an 18.8% rise in CET revenues and net import taxes would increase by \$1.3 million, a rise of 10%. Regarding the 15% CET rate increase, imports would fall by 2.7%, CET and net import tax revenues would rise by 27 and 14%, respectively.

As a result of these tariff simulation exercises, the average tariff rate associated with the 20-30% rate bracket ranged from 31.3% in the presence of the 5% rate increase to 37.6% when it was the 15% increase. Similarly, for the 30-45% rate group the average tariff rate ranged from 39.3% to 45.2%, and the average rate for the >45% rate group ranged from 51.7% to 57.2%. Imposing a CET rate of 100%, would lead to a 12% decline in imports, but CET and net import tax revenues would rise, respectively, by 44 and 18%. According to Figures 3.a and 3.b, the 20-30% rate group followed by the 30-45% group accounted for the greater share of imports and tariff revenues, and, among the simulation scenarios, the 100% tariff imposition produced the greatest effect on both imports and tariff revenues.

TRADE LIBERALISATION NEGOTIATIONS (FTAA & WTO)

St. Lucia is to conduct negotiations on trade liberalisation through the Regional Negotiation Machinery established by CARICOM to represent the interest of the region at WTO and FTAA.

The impact of trade liberalisation on a global scale is likely to have much greater significance as far as St. Lucia's fiscal situation is concerned than the changes that have taken place on its tariffs so far. Despite a high revenue buoyancy ratio and its relatively strong fiscal performance, its fiscal regime is still deficient in many respects. The tax system needs a major overhaul to remove inefficiencies both in terms of its allocative efficiency and its cost effectiveness. Although the recurrent expenditure/GDP ratio is moderate, there is need to examine the efficiency of its resource use. Furthermore, its savings ratio has been supported by large grants which may be unsustainable in the medium term. In this situation there are a number of factors to be considered in moving towards complete trade liberalisation. Among these are:

- the importance of import duties as a share of total recurrent revenue;
- the deficiencies in the current fiscal regime;
- the market structure of the import trade and its response to changes in border prices;
- possible contraction in the economy arising from negative sector response to external competition which could have an impact on revenue generating capacity.

St. Lucia depends on international trade for a considerable part of its recurrent revenue. Overall taxes on international trade account for 56.7% of its total recurrent revenue of which import duties account for 14.2%. A one-off removal of import duties would destabilise its fiscal situation, especially in view of the deficiencies that presently exist in its fiscal system.

In general, reductions in tariff do not necessarily result in loss of revenue. Price elasticity of demand, in theory, stimulates growth in import volumes with usually low inflationary effects. However, if the market structure does not favour price competition, then the reverse will be experienced. Business in St. Lucia is generally competitive and there is no evidence of cartelism as in the case of most of the other OECS countries. But given the magnitude of the adjustment required there will be opportunities for windfall profits which could frustrate opportunities for expansion in trade.

Moreover, while price elasticity of demand could stimulate short-term increases in the volume of imported goods and keep revenue buoyant, they could also reduce demand for import substitute

goods and cause the domestic economy to contract in the long term. The use of exchange rate adjustments as a mechanism for price realignment may have minimal impact given the high import content of domestic production, especially import substitute goods.

The net effect could be a fall in demand and contraction in both the economy and government revenues.

The magnitude of the adjustment as indicated above requires firstly that the fiscal regime be strengthened to remove inefficiencies in the current tax system and improve resource allocation and use in the government budget. Secondly, the elimination of tariffs should be done on a phased basis that would have minimal disruption to the flow of revenues into the government budget.

In order to address the latter simulations of the effect of the reduction in tariffs were conducted using the World Bank 123 model.

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 describes 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.

Transmission Mechanism of A Reduction In Tariffs

One of the key assumptions underlying the model is imperfect substitution between tradables and non-tradables. This assumption enables deviations from the law of one price which is standard in classical trade theory. By relaxing the assumption of perfect substitution between traded and non traded goods the model reflects the body of empirical evidence that indicates that changes in the price of imports and exports are only partially transmitted to the prices of domestic goods. Product differentiation of both imports and exports given the level of aggregation permits an extension of the Salter Swan model and gives rise to normally shaped offer curves. All domestic goods that are not exported are effectively treated as non-tradables (semi-tradables). Another key assumption in the model is the small country assumption whereby the country is a price taker in both import and export markets.

In this model, consumers consume a composite good (Q) that is comprised of imports (M) and domestic good (D). Relatedly all income is spent on the composite good to satisfy the equilibrium condition that the value of goods demanded must equal aggregate expenditure. The desired ratio of imports to the domestic goods is a function of relative prices for a given degree of substitution. This allows for the relative demand functions to be linearly homogeneous of degree zero thus mitigating issues of “money illusion”.

When the import tariff rate is cut this changes the relative price of imports to the domestic good. Imports become cheaper and there is a real appreciation of the exchange rate. There are two effects that arise: the income effect and the substitution effect as imports become relatively more attractive. For a given propensity to import, consumers maximise utility by consuming more of the import good as real income is now higher. For most developing countries such as those of the currency union the income effect is likely to dominate given low elasticities of substitution. Both exports and the domestic good will be more expensive relative to imports.

In the simulation the constraint that the overall savings investment balance should remain the same is imposed. The simulation basically asks the question by how much would sales tax/value added tax or excise tax revenues have to be raised in order to ensure revenue neutrality. The current revenue has three components related to (a) tradable sector; (b) non-tradable sector and (c) overall income. Revenue is therefore a function of the product of the import tariff rate times the real exchange rate times the value of imports plus the product of the sales/excise/value added tax rate times value of demand for the composite good plus the product of the direct tax rate times total income. Hence when the import tariff rate is cut it, the income effect results in more imports hence the quantity effect dominates the price effect for a given propensity to import in the revenue function. The second effect is traced through the sales/excise or value added tax rate as it is applied to demand for the composite good which is comprised of both imports and domestic goods. The sales or excise tax provides a compensatory mechanism that ensures that the savings investment balance is maintained for a given cut in the import tariff rate. Walras’

Law ensures that the sum of the price-weighted excess demands summed over all markets must be zero.

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.

During the 1980's trade taxes accounted for 51.8% of current revenue. The degree of dependence on these taxes increased during the 1990's to 54.0% of current revenues. The yield from these taxes as a per cent of GDP rose from 12.3% to 13.1%. Arising from a higher growth in nominal GDP, the revenue and trade elasticities in the 1980's were 1.16 and 1.26 respectively. Slower GDP growth arising from a weaker export sector in both goods and services in the 1990's resulted in a revenue and trade elasticities of 0.92 and 0.88 respectively.

St. Lucia Revenue and Trade Tax Elasticities

	1980-98	1980's	1990's
Revenue	1.07	1.16	0.92
Trade Tax	1.13	1.26	0.88

For a 25% reduction in tariff rates indirect taxes would have to be increased to 3.0% of GDP and for a 50.0% reduction these taxes would have to rise to 6.0% of GDP. For the full liberalisation scenario these taxes would have to rise to 13.4% of GDP

St. Lucia Simulations

Tariff Rate	Indirect Tax Rate Per Cent GDP
25% reduction in Import Tariff	3.0
50% reduction in Import Tariff	6.0
100% reduction in Import Tariff	13.4

Table 1.10: St. Lucia Baseline Indicators

	EC\$M	1998 Baseline Per cent of GDP
GDP Market Prices	1698.2	
Consumption	1414.7	83.3
Private	1101.7	64.9
Public	313.0	18.4
Domestic Saving	283.5	16.7
Investment	418.48	24.6
Imports of Goods	878.0	51.7
Exports of Goods	169.22	10.0
Foreign Saving	181.1	10.7
Av. Tariff Rate /1	0.260	-
Current Revenue	424.4	25.0
Trade Taxes	228.4	13.4
Current Expenditure	333.2	19.6
Current Account Balance /2	90.18	5.3
Overall Balance	-90.32	-5.3

1 /Defined as the ratio of Trade Taxes to Imports of Goods

2 / Denotes Current Account After Grants

Fig. 3.a: St. Lucia, Simulation Results on Imports, 1997

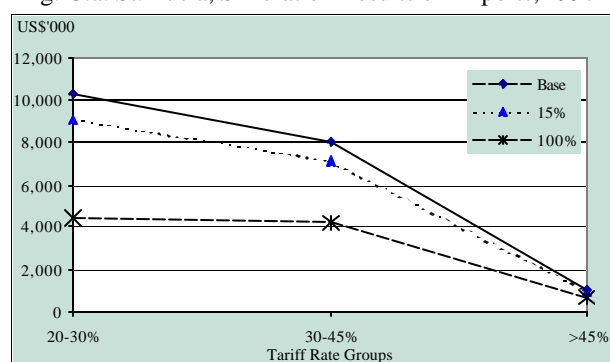
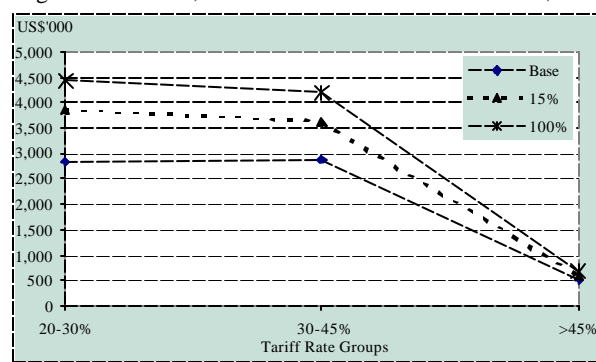


Fig. 3.b: St. Lucia, Simulation Results-Tariff Revenues, 1997



CONCLUSION

The performance of the St. Lucian economy during the 1990's has reflected the challenging times in which the country operates. Growth averaged only 1.7% annually towards the end of the decade of the 1990s compared to 5% during the last few years of the 1980s.

In the coming years the country faces the challenge of adjusting to the changed circumstances in the international environment, but it faces these challenges better equipped than most of the other OECS countries. A starts out with a strong fiscal position, a more diversified economy and a stronger human resource base.

In the area of agriculture the competitiveness studies suggest that the country is most export competitive in the production of bananas, mangoes, pineapple, plantains, coconuts, avocado, yams sweet potato and ginger. Among the beverages and processed foods, St. Lucia was shown to have a competitive advantage in coconut oil, beer, but competitive disadvantage in alcoholic beverages.

The manufacturing sector that has developed with the aid of high levels of protection. The agro-processing sector has strong linkages with the agricultural sector and has the potential to be competitive in selected niche markets but the survival of some firms in the sector may be doubtful without the protective arrangements. In this regard the authorities may need to allow the least efficient firms to exit the sector in an orderly manner while providing support to those firms that have the potential to be export competitive. A package of assistance would need to be provided to these firms and may include, finance and technical assistance in product development, factory layout, marketing etc. Given the tight budgetary constraints facing the country and the expected loss of revenue from trade liberalisation it may be necessary to access the required resources from external sources.

The tourism industry has been the main source of growth in the economy. Occupancy rates which have been variable have averaged approximately 67%. Although the USA, UK and Caribbean markets have accounted for, on average, over 70% of all stay-over visitors, there is a need to increase arrivals from the Canadian market. European visitors stay an average of two weeks in contrast to 3-7 days by visitors from the USA. Increased marketing and promotion and airlift capacity from Europe would enhance the foreign exchange earnings of the destination. There is also a need for increased integration of this industry with the agricultural sector in order to increase the local content in value added in the industry. As the tourism product become increasingly all inclusive (60% of all rooms) this will have implications for foreign exchange retention, value added and the degree of government revenue derived from the industry for the purposes of marketing and promotion.

The recent granting of a subsidy to American Airlines to ensure airlift capacity to the destination speaks to a need for focussed marketing and promotion. The staging of the St. Lucia Jazz Festival has increased stay-over visitor arrivals from the three leading markets but this may not be sufficient in attracting more long stay visitors. Targeting a room capacity of 5000 by the year 2000 highlights the need to integrate FDI inflows into increasing hotel plant with a medium term strategic plan to enhance air lift capacity to the destination.

Differentiation of the tourism product is possible given the increasing number of small hotels. These can be marketed in a manner that distinguishes them from the several of the larger hotels that are owned or operated by international chains. The role of the cruise ship industry has to evaluate in the context of the substantial costs of infrastructure and low average daily expenditure of this type of passenger. The Tourist Board will have to evaluate using market intelligence the number of stay-over visitors that were once cruise ship passengers. The move towards mega cruise liners may warrant additional investment in infrastructure.

St. Lucia's tax structure is generally compliant with WTO rules except for differentiation in rates of embarkation tax applied to nationals and non-nationals and the aliens landholding license fee required of non-nationals entering into land transactions which appear to discriminate against non-nationals. The main concern is not the revenue loss involved in a downward leveling of the embarkation tax or the deregulation of land transactions, which can be absorbed with slight budget modifications. With regard to the aliens landholding license fee, however, there are social considerations involved principally the possible alienation of deserving nationals from lands critically needed for basic shelter and small farming. A phased approach to deregulation should be considered. A customs revenue charge at 4.0% appears to be in violation of the limit set for cost recovery. Downward adjustment to the permissible limit of 1.0% would result in considerable revenue loss and compensatory measures that could disrupt domestic production unless it can be done within the framework of an overall tax reform aimed at shifting taxes from imports downstream to a wider base of expenditure.

St. Lucia's fiscal performance has been fairly stable with current savings equivalent to nearly 6.0% of GDP in 1998. Although revenue buoyancy has been high, there are deficiencies in the tax system which need to be corrected, principally inequalities in the distribution of the tax burden and weak enforcement capacity. The incentive regime creates distortions in burden-sharing and resource allocations and also provides opportunities for tax evasion or avoidance. There is urgent need to review the structure of taxes, the incentive framework and discretionary concessions policy as well as to strengthen tax administration.

On the expenditure side, improvements are needed to rationalise budget allocations, especially with regard to the outlay on wages and salaries. The level of investment spending in a situation of declining fiscal savings has called for greater attention to project selection and resource mobilisation. The steep rise of St. Lucia's public debt and the large share of domestic financing signals the need for prudence in the structure and cost of investment financing.

St. Lucia has implemented Phase II of the CARICOM CET and intends to move directly to Phase IV. This further step towards trade liberalisation and any future movements towards the elimination of tariffs are likely to result in high revenue costs unless adjustments are made within a comprehensive tax reform aimed at shifting border taxes downstream to expenditure and broadening the tax base to capture more of the services sector. There may be need for considerable international support and a period of transition that takes account of St. Lucia's institutional strengths and possible economic disruptions.

The study suggests that the market for services in St. Lucia 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 the St. Lucia 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 1.11: St. Lucia Tourism Statistics

	Mean 1986-90	Mean 1990-94	Mean 1995-98
Stay-overs	120,756	177,231	285,529
Cruise ship Passengers	81,475	152,004	264,600
Stay over growth	8.41	10.93	15.37
Cruise ship Passenger growth	19.21	12.44	24.31
Total Visitor Growth	12.08	11.30	19.28
Visitor Expenditure EC\$m	224.90	440.36	673.00
Visitor Expenditure Growth	10.21	16.89	7.64
Service Penetration Index /1	1.12	1.73	3.89
USA Market Share	31.29	28.99	29.32
UK Market Share	21.96	23.36	20.11
Caribbean Market Share	22.04	23.89	20.65
Canadian Market Share	11.51	7.87	4.81

1/ Defined as the ratio of service exports to merchandise exports

Table 1.12: St. Lucia Real Sectoral Growth and Real Relative Contribution

	Mean 1986-89	Mean 1990-94	Mean 1995-98
Tourism			
Contribution	9.81	10.26	12.25
Growth	9.57	7.17	5.44
Construction			
Contribution	6.87	7.87	8.35
Growth	18.88	4.01	0.57
Communications			
Contribution	3.99	6.87	8.56
Growth	21.25	17.20	2.15
Transportation			
Contribution	11.19	10.30	10.83
Growth	9.59	1.87	2.22
Banks			
Contribution	6.80	7.73	9.43
Growth	16.49	4.72	6.94

Table 1.13: St. Lucia Foreign Direct Investment (FDI) Profile

	Mean 1986-89	Mean 1990-94	Mean 1995-98
FDI as Per Cent of GDP	5.85	9.6	8.2
FDI as Per Cent of ECCB Inflows	16.74	24.65	20.81
Equity Share of FDI	68.62	4.45	18.21
Land Sales Share of FDI	10.24	14.67	7.9
Reinvested Earnings Share of FDI	8.61	32.33	47.59
Other Investment Share of FDI	12.53	48.45	6.98

Table 1.14: St. Lucia Monetary Survey (EC\$M)

	1986	1987	1988	1989	1990	1991	1992	1993	1994	1995	1996	1997	1998
Net Foreign Assets	107.73	142.40	179.07	145.10	152.24	196.43	176.57	115.06	71.93	92.14	11.78	(7.04)	92.61
Central Bank (net)	67.81	83.12	88.15	103.16	115.67	150.28	144.89	157.25	147.83	163.14	146.07	159.38	185.05
Commercial Banks (net)	39.91	59.28	90.93	41.94	36.57	46.15	31.69	(42.19)	(75.90)	(71.00)	(134.29)	(166.41)	(92.44)
External (net)	40.46	58.64	77.34	44.61	38.58	38.22	35.14	(17.37)	(52.01)	(54.65)	(105.37)	(88.63)	(78.82)
Other ECCB Territories (net)	(0.55)	0.64	13.58	(2.67)	(2.02)	7.93	(3.46)	(24.82)	(23.89)	(16.35)	(28.92)	(77.78)	(13.62)
Net Domestic Assets	197.00	221.75	261.47	366.68	433.09	435.23	463.92	592.25	676.85	724.69	820.72	895.60	903.84
Domestic Credit	243.09	271.98	320.60	419.40	464.95	481.15	516.56	659.26	714.27	773.07	864.34	953.13	989.94
Central Government (net)	71.77	72.50	45.50	44.02	34.01	15.03	(10.44)	(12.66)	(16.16)	(20.19)	(15.21)	(23.37)	(38.89)
Other Public Sector (net)	(48.39)	(61.40)	(104.48)	(116.13)	(127.90)	(137.81)	(109.04)	(99.56)	(100.08)	(112.77)	(125.91)	(134.73)	(171.30)
Non-Bank Financial Institutions (net)	(55.44)	(49.32)	(21.94)	(27.91)	(19.65)	(19.85)	(44.11)	(35.00)	(29.97)	(40.13)	(61.48)	(45.31)	(49.95)
Subsidiaries (net)	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.08	(0.27)	(4.32)	(15.29)	(8.12)
Private Sector	275.15	310.21	401.52	519.42	578.48	623.78	680.14	806.47	860.41	946.42	1,071.26	1,171.82	1,258.19
Other Items (net)	(46.10)	(50.24)	(59.13)	(52.72)	(31.86)	(45.92)	(52.64)	(67.00)	(37.42)	(48.37)	(43.62)	(57.53)	(86.11)
Money Supply (M2)	304.72	364.15	440.54	511.79	585.33	631.66	640.49	707.31	748.78	816.84	832.50	888.56	996.44
Currency	39.05	52.06	56.28	67.28	64.23	62.88	64.26	67.15	65.24	73.56	70.30	69.61	77.52
Demand Deposits	46.34	55.33	70.67	78.90	90.99	86.31	134.77	147.20	146.62	164.61	155.37	169.65	170.38
Savings Deposits	123.98	152.73	192.79	230.61	257.58	287.08	287.71	326.33	359.11	400.82	417.22	427.43	467.90
Time Deposits	95.02	103.79	119.26	133.97	171.45	193.88	152.62	164.41	174.41	173.59	186.10	217.63	273.57
Foreign Currency Deposits	0.34	0.26	1.54	1.03	1.07	1.51	1.14	2.22	3.40	4.25	3.51	4.25	7.07

Table 1.15
St. Lucia Savings Investment Profile

	1986	1987	1988	1989	1990	1991	1992	1993	1994	1995	1996
Source of Funds	150.0	161.6	221.3	291.3	276.6	288.2	306.4	323.4	327.7	330.2	341.8
Gross National Savings	135.7	127.2	177.2	123.6	130.2	101.2	164.9	197.0	215.3	259.3	191.8
Gross Domestic Savings	118.4	103.5	185.9	133.1	180.4	144.3	218.2	263.1	257.2	312.7	247.4
Public Sector	64.8	84.0	36.4	42.3	22.5	122.0	143.0	154.0	148.0	124.0	128.0
Private Sector	53.6	19.5	149.5	90.8	158.0	22.3	75.2	109.1	109.2	188.7	119.4
Transfers from Abroad	30.3	37.3	20.5	19.1	20.5	36.9	24.4	25.0	48.2	51.8	35.6
Net Factor Income	-13.0	-13.6	-29.2	-28.6	-70.7	-80.0	-77.7	-91.1	-90.1	-105.2	-91.2
Foreign Savings	14.3	34.4	44.1	167.7	146.4	187.0	141.5	126.4	112.4	70.9	150.0
Use of Funds											
Domestic Investment	150.0	161.6	221.3	291.3	276.6	288.2	306.4	323.4	327.7	330.2	341.8
Public Sector	87.6	92.8	146.6	158.7	183.0	155.0	174.0	187.0	194.0	136.0	156.0
Private Sector	62.4	68.8	74.7	132.6	93.7	133.2	132.4	136.4	133.7	194.2	185.8
(In percent GDP Market Prices)											
Source of Funds	20.6	20.2	24.3	28.3	24.6	23.8	22.8	24.1	23.4	22.1	22.2
Gross National Savings	18.6	15.9	19.5	12.0	11.6	8.4	12.3	14.7	15.4	17.3	12.4
Gross Domestic Savings	16.2	12.9	20.4	12.9	16.1	11.9	16.2	19.6	18.4	20.9	16.0
Public Sector	8.9	10.5	4.0	4.1	2.0	10.1	10.6	11.5	10.6	8.3	8.3
Private Sector	7.3	2.4	16.4	8.8	14.1	1.8	5.6	8.1	7.8	12.6	7.7
Foreign Savings	2.0	4.3	4.8	16.3	13.0	15.5	10.5	9.4	8.0	4.7	9.7
Use of Funds											
Domestic Investment	20.6	20.2	24.3	28.3	24.6	23.8	22.8	24.1	23.4	22.1	22.2
Public Sector	12.0	11.6	16.1	15.4	16.3	12.8	13.0	13.9	13.9	9.1	10.1
Private Sector	8.6	8.6	8.2	12.9	8.3	11.0	9.9	10.1	9.5	13.0	12.0