

UNLEASHING CARIBBEAN GROWTH: DISCIPLINE DRIVES TURNAROUND*

Thank you, Alejandro for that kind introduction and for inviting me to speak in my home town. It is an honor to be here, and since you were the teaching assistant for the course on international macroeconomics I took in graduate school, I assume you will take the blame for any errors in what I say this afternoon [**Click to Slide #1**].

In all seriousness, I would like to take the liberty of dedicating my remarks to Sir K. Dwight Venner, the late Governor of the Eastern Caribbean Central Bank (ECCB), who passed away last December. Dwight, who spent a significant fraction of his working life at International Monetary Fund (IMF) gatherings like this one, was a friend and mentor who was kind enough to give me my first job as a professional economist at the ECCB during the summer of 1994. Things came full circle when, twenty years later, in November of 2014, Dwight invited me back to the ECCB to give a lecture in honor of Sir W. Arthur Lewis, the great Caribbean economist and Nobel Laureate.

Arthur Lewis died in 1991, thirty-seven years after the publication of his celebrated article “Economic Development with Unlimited Supplies of Labour” (Lewis, 1954) and three years before the dramatic turnaround in so-called Third World economies that Lewis’s earlier work anticipated. We now refer to these nations as emerging and developing economies, in large part because of their economic turnaround [**Click to Slide #2: Figure 1**]. That turnaround is depicted in Figure 1, which I constructed using data from the IMF’s World Economic Outlook (WEO) database. The figure plots the average growth rate of real GDP in advanced as well as emerging and developing economies from 1980 through 2015. The figure makes three essential

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points.

First, the growth rate of real GDP in the emerging world has been dramatically higher in the last two decades than it was in the previous period. From 1980 to 1994, real GDP in emerging and developing economies grew at an average rate of 3.5 percent per year versus 5.5 percent from 1995 to 2015. The significance of this two-percentage-point increase in growth is profound. For a country whose population grows at 1 percent per year, annual GDP growth of 3.5 percent means that its per capita income doubles once every 29 years; with 5.5 percent growth, per capita income doubles in just 15.

Second, contrary to the increasingly fact-free rhetoric coming from leaders and media in a number of G7 countries, there is no evidence to support nationalist notions that faster growth in the emerging world comes at the expense of average living standards in advanced nations. Excluding the years 2007–2012, which was a period of slower growth in developed countries because of the Global Financial Crisis and the attendant recession—a negative shock that had little to do with developing countries per se—there has been no substantive change in advanced-country growth following the acceleration of growth in the developing world. Developed countries grew by 2.9 percent per year from 1980 to 1992—almost identical to the 2.8 percent rate at which they expanded from 1993 to 2007.

The third essential point about Figure 1 is that the relatively unchanged growth performance in advanced economies over the two periods of observation suggests that the accelerated rise of living standards in developing countries was not caused by an aggregate shock to the global economy, but points instead to country-specific policy changes that were adopted by developing countries during the 1990s as an unprecedented number of them rejected ideological approaches to economic policymaking and instead embraced discipline.

The rest of my remarks this afternoon will focus on three aspects of the word *discipline*: (a) exactly what I mean by it; (b) how emerging and developing countries in general have used discipline to turn themselves around; and (b) most critically what specific lessons Caribbean countries can learn and adapt from these past experiences to develop disciplined policies that will help them deal with the challenges of fiscal adjustment, high debt, and low productivity that stand in the way of sustained and inclusive growth.

TURNAROUND HAS NOT YET COME TO THE CARIBBEAN

Before answering the question of what I mean by discipline, and what Caribbean countries can learn from the other countries' experiences with it, look at Figure 2 [**Click to Slide #3: Figure 2**]. The graph clearly indicates that the economic turnaround experienced by so many emerging and developing countries in the 1990s completely bypassed the Caribbean. There has been no such increase in growth for the region. In fact, things have gone in the opposite direction. Growth has slowed in the Caribbean, even as it has accelerated in other emerging and developing economies. From 1980-1994, non-commodity-exporting Caribbean countries grew at 3.9 percent per year, slightly faster than the emerging and developing economy average of 3.5 percent over that same period of time. But now zoom in on the period from 1994 to 2015. Caribbean growth actually *fell* to 2.0 percent per annum as growth in emerging and developing economies was increasing to 5.5 percent per year.

Put another way, while the rest of the emerging world has cut in half the number of years it takes to double their people's standard of living from 30 to 15 years, the average doubling time in Caribbean nations has actually *increased* from 23 to 69! Furthermore, slow growth in the Caribbean cannot be blamed on, or explained away by, a "small-country fixed

effect.” Since the year 2000, the Caribbean has grown 33 percent more slowly than non-Caribbean small states (Chamon, Charap, Chen, and Leigh, 2017).

DISCIPLINE DRIVES TURNAROUND

What then, were the changes that triggered this period of accelerated, catch-up growth in the emerging and developing world that has bypassed the Caribbean? While large supplies of low-cost labor in the rural and informal economies of developing countries like China and India surely played a role in sustaining the process—per the first assumption of Arthur Lewis’s famous model of economic development—over the two decades from 1995 to 2015 no commensurate change in the demographics of the non-Caribbean developing world occurred to suggest that an increase in its supply of labor was responsible for the growth acceleration. In fact, over those two decades, the growth rate of the working-age population in Asia and Latin America was actually *decreasing* (and was roughly constant in Africa), even as emerging-market growth rates were increasing.

Instead, the proximate cause of the growth acceleration in non-Caribbean emerging and developing economies was the shift in economic policy toward increased efficiency that moved conditions on the ground in those countries more closely in line with the second assumption of the Lewis model: namely, that owners of capital plow the profits they make from their industrial activities back into their businesses, creating a virtuous cycle of profitability and ever-expanding employment for previously under-utilized workers. The most poignant example of such a shift was the implementation of policies that caused a precipitous and permanent drop in the rate of inflation in the developing world after 1994 [**Click to Slide #4: Figure 3**].

The drop in developing-country inflation illustrated in Figure 3 is really just a proxy for

the clear change of direction in the broader economic policies and priorities of leaders in much of the developing world that took root in the early 1990s. Beyond the necessary task of vanquishing high inflation, this change of direction manifested itself through the adoption of policies more conducive to capital formation: macroeconomic stabilization, more openness to international trade and financial flows, increased respect for the rule of law, a larger role for the market in allocating goods and services, and a more modest role for government in the national economy.

From lower inflation, which reduces volatility in relative prices and profits; to increased openness to financial flows, which gives developing countries access to a global pool of savings and makes capital more abundant in the form of foreign direct investment, portfolio equity, and so on; to greater rule of law, which reduces the likelihood that investments will be expropriated by the State and decreases uncertainty, a more business-friendly environment reduces the cost of capital. **[Click to Slide #5: Figure 4]**

Figure 4 demonstrates the impact of pro-business economic policy reform on the cost of capital by plotting the average value of the aggregate market earnings-to-price ratio—the earnings yield—for the subset of emerging and developing countries for which I could obtain data over the relevant time period. Providing a point of comparison, the figure also plots the U.S. earnings yield. Two features of Figure 4 are worth noting. First, there is a sharp drop in the earnings yield for emerging and developing countries—from an average of 14.4 percent before 1994 to an average of 7.1 percent thereafter—but the yield for the U.S. is roughly constant at 5 percent over the entire sample period. Second, except for the spike associated with the 1997–1998 Asian Financial Crisis, the fall in the earnings yield in emerging economies is permanent, and its timing coincides with both the onset of reforms in these countries and their acceleration of GDP growth.

Because the earnings yield is the average cost of equity capital for all publicly traded firms—the risk-free rate of interest plus the equity-risk premium—it provides the broadest visible proxy for the rate of return that owners of capital in emerging and developing economies require to reinvest their profits in the local economy instead of allocating them elsewhere or increasing consumption. The large fall in the required rate of return to capital after the onset of reforms in the 1990s provides a compelling, if admittedly somewhat oversimplified, explanation of the growth acceleration that took hold in the non-Caribbean developing world after 1994.

By opening the economy and increasing the supply of savings, as well as providing stability and reducing uncertainty, economic reforms across the developing world reduced the risk-free rate and the equity-risk premium, leading to a dramatic fall in its average cost of capital. By removing economic distortions and increasing efficiency, reforms also raised the rate of return to invested capital. Falling costs of capital in conjunction with higher prospective returns to plant and equipment provided a strong incentive to increase investment, and in many countries of the developing world we did see higher rates of investment, wages, and GDP growth following major reforms (Chari, Henry, and Sasson, 2012; Henry, 2000; Henry, 2007).

DISCIPLINE IS PRACTICAL NOT IDEOLOGICAL

Again, the reforms implemented by leaders in a range of developing countries over the past two decades can be summarized in a single word: discipline. Discipline, however, is not what you think. The old, neoliberal, if you will, view of discipline sees it as a *carte blanche* philosophical commitment to all of the aforementioned policy changes and an according willingness to adopt extreme measures such as fiscal austerity with blind faith.

In contrast, the new view of discipline I urge this generation of Caribbean leaders to

adopt is based on a systematic observation of the historical record that allows us to draw reasonable, empirically-based inferences about which economic reforms actually generate growth and why. Whereas the old view of reform is a kind of one-size-fits-all approach to growth, the new view sees reform as the adoption of a subset of policies that are rooted in the principles of modern economics, but are practically tailored to suit the specific needs of individual countries and provide the maximum economic impact per unit of political capital needed to enact them.

Specifically, discipline is a sustained commitment to a pragmatic growth strategy executed with a combination of temperance, vigilance, and flexibility that values the long-term prosperity of all over the short-term enrichment of any single group (Henry, 2013). Succinctly, in the local vernacular, discipline means: *Long road draw sweat; short cut draw blood.*

I am not arguing that Caribbean leaders have made no attempts at reform. They have. But it is fair to say that the efforts have been uneven across countries and over time. From individual country attempts to implement policies to enhance growth, to cross-country Caricom initiatives to promote further regional integration such as the Caribbean Single Market and Economy—the free movement of labor across islands in particular—the region is late to the match, if I may use a cricket analogy, and needs to remain focused on the fundamentals in the innings ahead. In the remainder of my remarks, I will provide specific illustrations of discipline at work in in the developing world that offer practical lessons for the Caribbean on the topics of fiscal policy, debt relief, and productivity.

FISCAL POLICY: DISCIPLINE REQUIRES COUNTERCYCLICAL BUDGETING

Discipline in the realm of public finance means that governments should run

countercyclical fiscal policy—surpluses in good times, deficits during downturns. This is no more complicated than the moral of Aesop’s classic tale of the Ant and the Grasshopper. When Andres Velasco became Chile’s minister of finance in March 2006, the country’s treasury had roughly \$6 billion in savings. Over the next two years, that number ballooned to almost \$50 billion, as the worldwide commodity boom drove up the price of copper, Chile’s major export. The country’s good fortune did not go unnoticed—nor did its lack of a commensurate increase in public spending. In November of 2008, thousands of protesters burned an effigy of Velasco in the streets of Santiago, calling him “disgusting” for refusing to share the treasury’s riches. Velasco held his ground, resisting the push for greater spending and higher public sector wages while reminding those calling for his resignation that the copper-generated surplus was money for a rainy day.

As the world economy plunged deep into recession in 2009, the wisdom of Velasco’s tough choices became abundantly clear. While the crisis curtailed access to credit and forced many countries to endure belt tightening, Chile used its arsenal of savings to launch a \$4 billion package of tax cuts to cushion the impact of the global slowdown on its economy and to distribute a raft of subsidies to mitigate the hardships of the poor. By April of 2009, Velasco was the most popular minister in President Michelle Bachelet’s cabinet, with an approval rating of 57 percent—almost double what it had been in August of the previous year.

Every leader would like to have money to address urgent needs during hard times. The real question is whether they have the discipline required to save their fiscal surpluses when the economy is doing well so that they can run deficits when times are lean without having to worry about the national debt getting so large that risk premia spike and financial markets deny access to further borrowing. If Chile is the prudent character in Aesop’s classic tale then, with respect to

practicing countercyclical fiscal policy, we must ask the question where do Caribbean countries—especially the relatively resource rich commodity-exporters Belize, Guyana, and Trinidad—lie on the ant-grasshopper spectrum? That question deserves serious consideration—and action if the data suggest room for improvement. From fiscal rules to sovereign wealth funds on the positive side of the ledger, to subsidies for the consumption of fossil fuels on the negative, a growth-oriented budgeting process prioritizes efficiency over expediency.

FISCAL CONSOLIDATION: DISCIPLINE DOES NOT EQUAL AUSTERITY

For Caribbean countries that require fiscal consolidation, whether due to bad policy or bad luck, the question is what discipline—a sustained commitment to the future—implies for their optimal speed of adjustment. The answer to this question turns on the recognition that problematic deficits and inflation are both the consequence of governments' choices with respect to spending and taxes.

Running large and persistent deficits is tantamount to playing with fire, but the manner in which governments get burned depends on how they choose to finance their revenue shortfall, either through debt—the accumulated bill of IOUs from past deficits—or monetization. In the case of debt, for every nation there is a threshold of debt to GDP at which financial markets will put an end to the government's ability to finance deficits. Governments that choose to monetize their bills will drive up inflation. Since government expenditure in excess of revenues is the root cause of both debt and inflation crises, the two problems ultimately require the same solution—eradicating the deficit.

There are, nonetheless, multiple ways to get to the right place. The key question for Caribbean countries is not whether to eliminate the deficit, but the speed with which to do so,

given their specific circumstances and the tradeoffs involved. Under some scenarios the benefits of austerity exceed the costs and call for rapid, cold-turkey deficit reduction. On other occasions, taking a gradual path toward eliminating the deficit actually constitutes the disciplined course of action. How can Caribbean policymakers decide which approach is optimal? Again, history is the best guide to the future. Thirty years of data from emerging markets suggest that the disciplined course of action depends largely on the prevailing level of inflation in the country at the time austerity is being considered.

The stock market provides a useful lens through which to analyze austerity because it internalizes both the short- and long-run effects of such programs (Henry, 2002). To the extent that austerity creates expectations of slower growth and higher interest rates in the short run, it will depress present values. But the potential of higher growth and lower interest rates in the long run creates an offsetting effect. If the expected long-run benefits outweigh the short-run costs, then the country's stock market will rise when its government announces an austerity program. If the expected costs outweigh the benefits, the market will fall. If the anticipated net effect is zero, there should be little to no market reaction [**Click to Slide #6: Figure 5**].

Figure 5, taken from Chari and Henry (2014), illustrates the average collective reaction of domestic stock markets to the implementation of fiscal austerity in 21 different emerging nations with two different varieties of inflation between 1973 and 1994: 25 episodes of high inflation with a median inflation rate of 118 percent per year, and 56 episodes of moderate inflation with a median inflation rate of 15 percent. The solid line indicates that in anticipation of austerity programs directed at high inflation, the average national stock market experienced cumulative abnormal returns of 44 percent. In contrast, the dashed line indicates that in anticipation of

austerity programs directed at moderate inflation the stock market experienced cumulative abnormal returns of negative 24 percent.

To give the data a little more texture, it's worth noting just how often austerity programs fail. Define a successful program in the case of high inflation as one that causes inflation to fall below 40 percent and stay there for two or more years. Similarly, define a successful program in the case of moderate inflation as one that causes inflation to fall below 10 percent and stay there for two or more years. Using these criteria, Argentina had eight failed programs in fifteen years before finally succeeding on the ninth try. Brazil tried and failed seven times before slaying high inflation with the Real Plan in 1994. Overall, the average country attempted four austerity programs—one roughly every five years—and only twelve of the eighty-one attempts succeeded. Interestingly, the rate of success in high inflation episodes is greater than in the moderate inflation cases. Seven of twenty-five, or 28 percent of austerity programs initiated during high inflation succeed, whereas the number is less than 10 percent (five of fifty-six) in the moderate inflation cases.

Because austerity programs fail with great frequency, one can think of the stock market responses depicted in Figure 5 as roughly the product of two things: the true net present value of a successful program, multiplied by the probability of the program being followed through to completion. With a 28 percent chance of success, the fact that the market rises by 44 percent in anticipation of austerity programs initiated during high inflation suggests that people expect really good things to happen if the program actually succeeds. Analogous logic suggests that the 24 percent fall in the stock market may actually understate how much value people anticipate being destroyed by austerity programs initiated during moderate inflation.

Since austerity programs implemented during moderate inflation appear to destroy value, does this mean that countries should avoid fiscal consolidation? No. The question is not whether to pursue fiscal consolidation in the midst of moderate inflation but how. All fifty-six moderate-inflation consolidation depicted in Figure 5 took place under the auspices of IMF programs—traditional austerity programs where countries devalued the currency, cut the deficit, and curtailed the growth rate of the money supply in one fell swoop. What Figure 5 tells us, therefore, is that austerity or “cold turkey” fiscal consolidation destroys value when implemented in the midst of moderate inflation.

As Caribbean leaders seek to influence the future courses of their countries’ economies, they will need to weigh carefully the costs and benefits of fiscal consolidation. The moderate inflation environment of the Caribbean calls for a vigilant but more gradual approach, grounded in the right mix of home-grown stabilization policies, tailored to a country-specific understanding of the root causes of the deficit.

Gradualism does not mean a lack of commitment. It is about altering the speed of execution, not changing the desired destination or sense of purpose. Moving more slowly toward a specified fiscal target can be a valuable tactic as part of a long-run growth strategy. The key point is not to balance the budget as quickly as possible but to implement positive net present value measures that place public finances on a trajectory that keeps the specter of inflation and debt crises at bay.

To its credit, the IMF took steps in the direction of endorsing a more gradual approach to fiscal adjustment as early as 2010. Speaking in Zurich in May 2012, Managing Director Lagarde praised European countries for their intention to reduce their deficits by about 1 percentage point of GDP per year—a far cry from the reductions of up to 5 percentage points that were being

called for at the time under the European Fiscal Compact—and urged countries to stick to fiscal measures instead of fiscal targets if growth turned out to be weaker than expected.

While the IMF’s position on gradual deficit reduction in Europe was eminently sensible, it must continue to communicate clearly to Caribbean leaders through its actions and words that the Fund’s newfound flexibility is not an *ad hoc* exception for European countries that wield outsized influence in the institution, but rather a fundamental change in its thinking toward fiscal adjustment in advanced *and* developing countries.

DEBT RELIEF: BORROWERS AND LENDERS TAKE RESPONSIBILITY

I turn now to the role of debt relief in Caribbean fiscal policy. Debt relief is an extreme option, not to be taken lightly, but a review of historical events and data demonstrate that when a government’s liabilities exceed its ability to pay, discipline requires borrowers and lenders to bear the burden of adjustment in order to reach an efficient resolution and restore growth.

Following seven years of restructurings and forgone growth during the Third World Debt Crisis in the aftermath of Mexico’s default on its external debt in August of 1982, and despite prior insistence by James A. Baker III that debt relief had no place in the solution, the U.S. Treasury changed tack in 1989. In coordination with the IMF, then-Secretary of the Treasury, Nicholas Brady, unveiled a plan that called on international commercial banks to provide approximately US\$65 billion of debt forgiveness to the sixteen nations in question from Africa, Asia, and Latin America [**Click to Slide #7: Figure 6**].

Figure 6, taken from Arslanalp and Henry (2005), shows that the anticipation of the official announcement of a Brady deal generated average cumulative abnormal returns of 60 percent in the stock markets of the recipient countries over a twelve-month preannouncement

window. Stock prices rose in anticipation of higher future growth, because debt relief was granted in exchange for officials in the Brady countries agreeing to implement growth-enhancing reforms: inflation stabilization, trade liberalization, and privatization of badly run state-owned firms whose lack of profitability was a major drag on public finances and helped give rise to debt overhang in the first place [**Click to Slide #8: Figure 7**].

Figure 7, also taken from Arslanalp and Henry (2005), indicates that as countries instituted and sustained subsets of the reforms that were most relevant to their circumstances, they experienced significant improvements in their economic performance.

It is tempting to conclude that the revaluation of assets simply reflected a transfer of wealth from bank shareholders to the debtor countries, but additional data reject this explanation [**Click to Slide #9: Figure 8**].

Figure 8 demonstrates that publicly traded international commercial banks with large developing-country loan exposure during the Third World Debt Crisis experienced average cumulative abnormal returns of 35 percent during the relevant debt-relief time frame. This evidence suggests that debt relief creates values both for both borrowers and lenders (Arslanalp and Henry, 2005).

Although not a single Caribbean country applied for or received debt relief under the Brady Plan, there are three lessons from that episode that are nonetheless deeply relevant for leaders in the region.

First, when there is debt overhang, whether with respect to the government's external debt, or loans of domestic banks to the local private sector, lenders must be willing to restructure loans that had have gone bad so that overhang can be removed and future investment and financing decisions can be made on the basis of clean books and realistic valuations. Resistance

to writing down debts that cannot be repaid places countries at risk for the extended malaise that stood in the way of Third World turnaround until Secretary Brady's bold change of course.

Second, debt relief is not free. Attaining higher levels of productivity is the only reliable way for countries to generate the resources required to service their debts—even at reduced levels—and provide for their populations. The precise recipe will differ from country to country, but the common denominator must be a sustained commitment to policies that deliver a higher average standard of living. We see this truth at work in the Caribbean today. In all of the cases in the Caribbean where debt restructuring and relief have placed the trajectory of debt to GDP on a downward trend—St. Kitts and Nevis in 2011-12; The National Debt Exchange in Jamaica in 2013; and Grenada in 2013-15—relief and restructuring were part of a package that included substantial macroeconomic reforms.

The third lesson, of course, is that the continuity of macroeconomic reforms is at least as critical as the initial commitment [**Click to Slide #10: Figure 9**]. Again, history is the best teacher. Figure 9 shows that the Brady countries that failed to honor their reform commitments—Jordan, Nigeria, and the Philippines—experienced a much smaller initial rise in the value of their stock markets than other Brady countries—30 percent versus 60 percent—and even those increases completely evaporated within a year as lack of commitment to reforms became obvious.

[**Click to Slide #11: Jamaican Timeline**] For this reason, it is encouraging to see continuity of the reforms here in Jamaica—not only over time following the announcement of the National Debt Exchange in 2013, but also across political parties with the change of government from the People's National Party to the Jamaican Labor Party in February of 2016. This consistency of commitment to reforms across parties stands in contrast to Jamaica's past

and is an important, disciplined step forward. From the formation of the Economic Programme Oversight Committee (EPOC) in 2013 to the establishment of the Economic Growth Council (EGC) in 2016, the engagement of civil society in holding both political parties accountable is a significant achievement. Much work remains to be done, but the multi-stakeholder cooperation on sustaining a pragmatic growth agenda should be applauded. Somewhat ironically, the tripartite collaboration of the government, workers unions, and the private sector in Jamaica evokes memories of a similar social compact twenty-five years ago in Barbados that pulled the country back from the precipice of a predicament—not unlike the one it faces now—by accepting shared sacrifice and incentivizing greater public and private sector productivity.

DISCIPLINE REDUCES THE COST OF DOING BUSINESS

Indeed, productivity is paramount, because a country cannot sustain a rising standard of living unless its productivity also grows. Yet from 2000 to 2015 the average growth rate of productivity for tourism-intensive Caribbean economies was *negative* 1.4 percent per year (Chamon, Charap, Chen, and Leigh, 2017). For commodity-exporting Caribbean economies the figure is better, 0.6 percent per year, but still substantially less than the growth rate of total factor productivity (TFP) for non-Caribbean small states and non-Caribbean emerging and developing economies for whom the average growth rate of TFP exceeds 1 percent per year. Therefore, the question is what can be done to improve productivity? In addition to staying the course on macroeconomic reforms, two things are critical.

First, the principal sectors of opportunity for the Caribbean—call centers, tourism, retirement communities, entertainment and wellness—suggest that services will play a critical role in the region’s future. Therefore, it is essential to have a well-educated workforce that can

respond quickly to new opportunities that arise from changes in the global economy. This can't be emphasized enough.

Second, in addition to sustaining macroeconomic reforms, governments must focus on driving micro-structural reforms that will allow entrepreneurs, managers, workers, and capital markets to perform their tasks more efficiently. Simply put, the focus of microeconomic policy needs to be more on facilitation and less on regulation, implementing changes that will reduce the cost of doing business and make the Caribbean a more profitable place to operate. Profitable firms pay taxes (provided the cost of tax compliance is not too high) and expand their operations. Expanding firms hire additional workers and create employment.

What micro-structural reforms can Caribbean governments implement to make the region a less costly place to do business? Reforms should be simple to implement and start with areas that constitute the principal bottlenecks to growth. How do you identify the principal bottlenecks to growth? One strategy would be to survey and talk with business leaders, entrepreneurs, ministry officials, lawyers, and judges about the key obstacles they encounter in trying to carry out their day-to-day operations. This is effectively what the World Bank has done since 2005 when it conducted its first *Doing Business* survey: *Removing Obstacles to Growth*.

This first report by the World Bank, assessed across 145 countries, the obstacles faced by an entrepreneur in performing standardized tasks: starting a business, hiring and firing workers, the burden of complying with taxes, getting access to credit, registering property, costs of crime and violence, the pervasiveness of the informal sector, dealing with licenses, and registering property. Since the tasks are standardized (i.e. the same in every country), the measures allow for a direct comparison of, for example, how hard it is for an entrepreneur in Trinidad to get credit as compared to an entrepreneur in Sweden.

Since 2005, the World Bank has expanded from 145 to 190 the number of countries it covers in the *Doing Business* survey. Also, in recognition that countries should aspire not so much to compete with each other as to achieve an absolute standard of ease of doing business, the survey also has a metric called “Distance to Frontier,” which quantifies how far a given country is from the “ideal” business environment. The smaller the numerical distance a country is from the frontier, the closer it is to having an ideal business environment. In principle, all countries could reach this level of ease of doing business without the need to outdo others.

[Click to Slide #12: Doing Business Indicators]

Some countries have made considerable progress. India is still a difficult place to do business, ranking 100 out of 190 countries, but it jumped 30 places since last year and has moved up 42 places in the last three years. The average ranking of Caribbean countries, by comparison, is 118. Suriname ranks lowest on the list at 165, Jamaica receives the best marks in 70th place, and Belize is right in the middle of the distribution at 121. The *Global Competitiveness Report* produced by the World Economic Forum, uses slightly different methodology than *Doing Business*, surveys 137 countries instead of 190, and ranks far fewer Caribbean countries—two instead of 13—but it produces very similar conclusions: Jamaica is 70th (exactly the same as in *Doing Business*) and Trinidad is 83rd (versus 102nd in *Doing Business*). Coming back to the World Bank’s measure, more challenging in some ways than the absolute ranking is the observation that Caribbean countries are generally headed in the wrong direction. Today the average distance of a Caribbean country from the frontier is 57.5, versus 54.5 in 2010.

There is clearly much hard work ahead, but one of the important lessons from both the World Bank and World Economic Forum studies is that undertaking reforms to help businesses operate more efficiently need not be overly expensive or take an excessively long time to

implement. The studies are full of examples, of how countries have changed certain administrative functions to reduce the cost of doing business without great financial expense to the government. Furthermore, a flexible business environment does not mean lack of protection or social support for the poor. The Scandinavian countries all provide low cost environments for doing business and strong social safety nets.

And speaking of safety nets, I have not addressed the matter of resilience [**Click to Slide #13: Disaster Insurance**]. The ratio of the length of my exposition on resilience to that of my thoughts on growth reflect my comparative advantage rather than my view about the relative importance of the two topics. Irma and Maria are painful reminders that the human and economic cost of hurricanes can be catastrophic. Clearly, as a region that bears a disproportionate share of the world's natural disasters at a time when the frequency of natural disasters is increasing, the Caribbean must protect its hard-won progress in macro and micro reforms by insuring itself more fully as well as investing in more resilient infrastructure (Otker and Loyola, 2017). Again, pan Caribbean cooperation in this area makes a lot of sense (Leigh, Srinivasan, and Werner, 2017).

CONCLUSION

Let me conclude [**Click to Slide #14**]. The world today looks radically different than it did when Arthur Lewis wrote his seminal paper in 1954, but the connections between capital, labor, productivity, and the policy environment implicitly embedded in the Lewis model are even more critical for Caribbean growth in this age of unprecedented integration. The Caribbean will continue to face significant challenges, but since economics teaches us that small countries stand to benefit the most from globalization, the opportunities are even more significant. The key to unleashing them is discipline. Thank you!

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