Trade Policies in the Caribbean Countries: A Look at the Positive Agenda

by

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Paper prepared for discussion at the meetings of the

Caribbean Group For Cooperation on Economic Development

Washington, D. C.

June 8, 1998

The authors wish to thank Edgardo M. Fararo for constructive comments on an earlier draft.

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SUMMARY AND POLICY RECOMMENDATIONS

In this paper we review the basics of the trade policy situation of the CGCED countries:

- How restrictive – compared with other developing countries – are their policies toward international trade? How do these trade policies relate to their recent growth performance?
- To what degree have the regional arrangements that have been created by them and by their neighbors in the hemisphere (e.g., Mercosur, NAFTA) increased or deceased their trade?
- Based on the answers to these questions, what trade policy issues are likely to be most important for these countries in the near future?

The trade policies of the CGCED countries can be characterized as similar to those that were popular in Latin America (and in other developing countries) before the reforms of the 1980s and 1990s: high and widely ranging tariffs, considerable use of quantitative restrictions and of discretionary licensing, many discretionary exceptions both to who gets protection and who gets special treatment to get around import restrictions.

The recent growth performance of these countries has been modest, almost two percentage points behind growth across all of Latin America and even farther behind the growing list of countries that have effectively used international trade as a vehicle for development. This modest growth and low gains of productivity suggest that the trade policies do not protect the economy, they protect particular interests in the economy, and they do so in a way that maximizes the social cost per degree of protection provided these interests. Their major social effect is to nullify trade's competitive and stimulative effects; the policies have more to do with how domestic resources are used than with how they are generated, or their productivity enhanced.

Using trade as a vehicle for development demands liberalization; it also requires much more. It requires what we describe below as the positive agenda of trade policy: a private sector dynamic, enterprise and human resource development, legal, transportation and communications infrastructure, as well as an openness to international trade and investment.

Our policy conclusions focus on policy reform in the CGCED countries, and on how trading partners can support that reform. Listed here succinctly but more fully explained in the text – they are the following:

Continue with unilateral reforms

Countries that had the same policies in the past but are now making effective use of trade as a vehicle for development made the obvious changes: elimination of QRs and discretionary licensing, lower and more uniform tariffs, elimination of exceptions. Because much of the protection employed by the CGCED countries is non-tariff, a lot of liberalization could be achieved without significant loss of tariff revenues. Indeed, it

might be possible for these countries to liberalize significantly and at the same time to increase the amount of tariff revenue they collect. International negotiations can be an important vehicle to advance and to support such reforms.

CGCED countries in the FTAA negotiations

Use the negotiations to further reforms. Negotiating postures aside, ones own restrictions should not be viewed as assets.

Focus on eliminating NTBs – they are extensive in the CGCED countries and they have high social costs. The CGCED countries (and their trading partners) have much to gain within a program of tariff rationalization that preserves existing levels of revenues.

Negotiating partners – particularly the larger countries – should share the burden of developing techniques for negotiating binding commitments on NTBs. They should phrase their requests from the smaller countries in such terms. Special consideration for the problems of smaller economies should focus on support for reforms of such policies.

Work with import using and consumer interests in the larger countries. Smaller country exporters can find allies on the inside.

Pin down the means by which the larger countries traditionally legalize their backsliding, e.g., antidumping. Again, import using and consumer interests in trading partners can be useful allies.

Objective and transparent rules plus objective and transparent dispute settlement are the basis of a rules-based rather than a power-based system.

Avoid complexity. Against a small country that cannot spread administrative costs over large trade volumes, complexity unleashes power. "Gains from trade" is straightforward economics, complexity is often a stalking horse for a special interest.

Identify and find ways to eliminate discrimination against CGCED countries in existing arrangements, e.g., NAFTA, Mercosur. CGCED trade with Latin America is unusually low, find out why, find ways to increase it.

Liberalization within the Caribbean region

Opening regionally can help to stage the process of opening globally and the participating countries have more effective control of the agenda than they would have in a larger negotiation. On the other hand, neighbors may be too sympathetic toward each others' problems – locking in reforms through international agreement requires an unsympathetic partner.

While the CGCED countries acting together can be a stepping stone to globalization, internal liberalization cannot be the end of the path. The economies (GDPs) of the CGCED countries sum to approximately that of the city of Chicago, the available scale will not allow for global efficiencies, nor will it be sufficient to produce the competitive stimulus and business discipline that comes from effectively contestable markets. Even as a stepping stone, what there is to gain from liberalization among the CGCED countries

may not justify using the region's skilled but limited negotiating resources there rather than in a larger arena.

The international and bilateral development partners

Development partners – bilateral agencies, the regional banks, the World Bank, the UNDP – in deciding how their resources will be used, should not limit their trade agenda to supporting developing country participation in trade negotiations. Their traditional support for capacity-building; human resource and enterprise development, infrastructure, is an important part of the positive agenda of trade reform.

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Using trade as a vehicle for development demands liberalization; it also requires much more. It requires what we describe below as the positive agenda of trade policy: a private sector dynamic, enterprise and human resource development, legal, transportation and communications infrastructure, as well as an openness to international trade and development. In the second half of the paper, we discuss the positive agenda at some length and we compare this agenda with what is traditionally covered by international negotiations over trade policy. We conclude that regional or hemispheric negotiations

can be an important medium for trade policy reform – but not a sufficient one. Unilateral reforms of the sort that have characterized the policy process in developing countries and have sometimes been supported by the international development agencies are a necessary complement.

2. STRUCTURE OF THE PAPER

The following section describes the basic economic characteristics of the CGCED countries. A reader familiar with them could skip the section without loss. Section 4 examines trade restrictions in the CGCED countries and compares them with restrictions in other countries.

Section 5 provides a formal analysis of the impact of CARICOM on trade among the member states, as well as the impacts of NAFTA and of Mercosur on the trade of the CGCED countries.

Section 6 takes up the general issue of how trade serves the development agenda. We explain the positive trade agenda and then in Section 7 we relate this trade agenda to the challenge of inclusion, the challenge of positioning all the citizens of developing countries so that they will enjoy the benefits of globalization. In Section 8 we compare the extent of trade liberalization achieved by developing countries through multilateral negotiations with the extent of their unilateral reforms. In Section 9 we take up the question, "With inclusion as our objective, are international negotiations, regional or multilateral, likely to support all of the necessary elements in trade policy for development?" Reform, of course, begins with and depends on the governments' commitment. Negotiations and outside agents can support, but they cannot drive reform.

As to support, we explain that in a country's (or region's) program to use the trading system as a vehicle for development, agreements with trading partners can be an important tool – particularly for reducing trade barriers. Negotiations however have not supported human resource and enterprise development, nor the establishment of legal and physical infrastructure. Thus the sort of support traditionally provided by the international and bilateral development agencies is a necessary partner to negotiations.

In the final section we examine trade policy options that regional and hemispherical negotiations might offer small economies such as those of the CGCED countries.

3. CHARACTERISTICS OF THE NATIONAL ECONOMIES

Except for their size, the CGCED countries are, on average, about average among developing countries.

The economies are unusually small.

The largest countries, the Dominican Republic and Haiti, are home to 7.8 million and 7.2 million people, respectively, which puts them below 75th on the global list of countries ranked by population. Nine of the fifteen CGCED economies have populations of less than 300,000. (Table 1)

These are mostly middle income economies.

Thirteen of the fifteen CGCED countries are classified by the World Bank as middle income countries, nine of the fifteen have per capita incomes above the average for the middle income countries. Haiti, home to one-third of the region's people, is one of the United Nations' designated least developed countries. Guyana, with a population of about 3/4 million, is the only other country classified by the World Bank as low income (income per head below $750/year). The Bahamas, with 1 percent of the region's population, is the only high income country (by World Bank classification) in the region.

Agriculture and mining provide relatively large shares of the GDP of the poorer countries

The poorer countries of the region share this characteristic with poorer countries around the world -- production of primary products is a relatively large share of economic activity.

Service sectors are large, especially large in the richer countries.

In 12 of the countries, home to 60 percent of the region's people, the share of GDP originating in the services sector is larger than for the aggregate of all developing countries. In the four richest countries, with income per head over $5000/year, the services sector provides more than 2/3 of GDP and in the Bahamas, the richest country in the group, services provide 93 percent of the value of economic activity.

Recent growth performance has been, on average, average

Over the period 1990 - 1995, real economic output in the CGCED countries grew by 2.1 percent per year, almost two percentage points below the average for non-Caribbean Latin America.

Trade structures

Commercial services are important exports.

Compared with Latin America or with other developing countries, commercial services make up a notably larger share of CGCED countries' exports. In aggregate, one-fourth of CGCED countries' export earnings are from sales of commercial services -- services being an important export of poorer countries of the group (Haiti, Guyana) as well as of the richer countries (Barbados, Antigua and Barbuda, The Bahamas).

Manufacturing is relatively unimportant

The manufacturing sectors in the CGCED countries are relatively small, (Table 1) yet manufactures, in Table 2, appear to make up a significant share of CGCED countries' exports. We are however working with figures for manufactured exports that do not adjust for the import content of offshore-assembly (outward-processing) activities. The share of manufacturing in GDP (which measures manufacturing value added) is thus a better indicator of the size of the manufacturing sector in the economies of the CGCED economies.

CGCED countries trade principally with North America and the European Union

Only 5 percent of CGCED merchandise trade is with other CGCED countries. North America (the US plus Canada) is by far the CGCED countries' largest trading partner; three-fifths of CGCED exports are sold in North America, almost half of their

imports originate in North America. The European Union is the second-largest trading partner, buying over one-fifth of CGCED exports and providing one-sixth of CGCED imports.[1] Figures 1 and 2 provide information on the importance of different CGCED trading partners.

4. TRADE RESTRICTIONS IN THE CGCED COUNTRIES

Information on trade policies and trade restrictions in the CGCED countries is relatively scarce. Only one of the countries, the Dominican Republic, has been the subject of a Trade Policy Review by the GATT/WTO and only one, Jamaica, has submitted systematic tariff and trade information to the WTO under the Integrated Data Base Program. We have however put together several indicators of trade and investment restrictions in these countries, and will present that information in this section.

Details

Table 3 provides a summary of trade restrictions and arrangements in the CGCED countries. Looking at the first column, we see that tariffs are relatively high. Tariffs on agricultural goods are 40 percent, and overall many rates are above 25 percent.

Rates in many other developing countries are lower. Latin American post Uruguay Round applied rates average less than 12 percent, the average for East Asian and Pacific developing countries is also on the low side of 12 percent.[2]

Trading in some products, particularly agricultural products, is reserved to state trading enterprises in most of the countries. (Table 3)

Table 4 shows that exchange controls remain in place in many of the countries. In ten of the fifteen, export receipts must be repatriated and surrendered for domestic currency, only seven of the fifteen allow banknotes to be freely imported and exported. Two of the countries still maintain dual currency rate systems, twelve of the fifteen control capital movements.

Quantitative restrictions and non-automatic licensing requirements are applied by many of the countries to most food products and to beverages. Imports of cosmetics, appliances, clothing and even some industrial goods are likewise controlled, some in some countries, some in others. Even within the CARICOM, every member maintains restrictions on some imports from other members, or from a targeted subset of members. Table 5 provides detail on such restrictions.

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[1] We will examine in Section 5 if there is anything "abnormal" in the concentration of CGCED trade with North America. Likewise we will examine the relatively low share of CGCED trade with Latin America – Latin America takes less than 3 percent of CGCED exports.

[2] For industrial countries, post Uruguay Round applied rates average less than 3 percent. Data for non-CGCED countries are from Finger, Ingco and Reincke.

Table 6 compares port costs across Caribbean and Central American countries. The figures show that the cost of unloading the same cargo from the same ship varied in 1986-87 from $446 in St. Barths to $17,897. (The figures do not include customs duties.) Even excluding the lowest figure, the charges in some ports exceed the charges in others by a factor of six. That such differences can exist suggests that the charges in many ports are much in excess of the economic costs of the service provided. Such charges represent then not costs, but protection, perhaps for the workers who provide the services, certainly for domestic producers.

The real exchange rate

Real exchange rate movements over the 1990s have varied considerably among the CGCED countries. The Jamaica dollar, for example, appreciated by 65 percent from 1990 through the first quarter of 1998, the Trinidad and Tobago dollar depreciated by 13 percent. Averaged across the CGCED countries, the real exchange rate appreciated by about 9 percent. Figure 3 compares the movements of the average real exchange rate for the CGCED countries, the Mexican peso and the average for a selection of Latin American comparator countries.[3] Overall, the movements were unfavorable to the trade interests of the CGCED countries.

The overall picture

A summary comparison with countries of Central and Latin America is provided in Table 7. The information provided there is based on concrete information such as that presented in the previous tables, but its aggregation is to a considerable degree impressionistic. The trade restrictions index, for example, was built by first sorting countries into five levels according to the average tariff, then adjusting a country up or down a maximum of one level based on a judgment of the severity of their NTBs. Based on these indices, the sample of eight CGCED countries covered are, on average, more restrictive of trade and of foreign investment - capital flows than are either Central American or other Latin American Countries.

One might reasonably characterize CGCED countries trade regimes as similar to those prevalent in Latin America before the reforms of the 1980s and 1990s. Heights of tariffs, extent of exchange controls are generally similar, but perhaps more characteristic is a dimension of trade policy to which Bela Balassa (1971) called attention in his path-breaking study of protection in developing countries. Early in his report he points out that while policies in place were often justified by reference to import substitution as a development strategy, the policies, as a program of action, had no inherent consistency.

> Rather, the existing system of protection in many developing countries can be described as the historical result of actions taken at different times and for different reasons. These actions have been in response to the particular

[3] The comparator sample includes Bolivia, Chile, Colombia, Costa Rica, Ecuador, Guatemala, Mexico and Nicaragua.

> circumstances of the situation, and have often been conditioned by the demands of special interest groups. The authorities have generally assumed a permissive attitude toward requests for protection and failed to inquire into the impact of the measures applied on other industries and on the allocation of resources in the national economy. (xv)

The details of the trade restrictions in place in the CGCED countries create a similar impression. Each of the countries has in its tariff a provision for special concessions for particular users or for particular uses. Access to such concessions must be applied for, it is not automatic. The pattern of quantitative restrictions and licensing requirements shows a similar tailor-made, one-off nature. For example, QRs or licensing requirements in one country on a few industrial chemicals, in another on paper for cigarette making. Such restrictions suggest not a social-return based identification of comparative advantage or of potential comparative advantage, but rather an attempt to provide a financial return for a particular investment.

The trade policies of the CGCED countries then are familiar – high and discretionary restrictions, use of many non-tariff measures that have high social costs, appreciating real exchange rates. They are much the same as those in place in other developing countries before they embarked on programs of trade-supported development.

The burden of such policies

Though we have not directly estimated the impact of these trade policies on the economies of the CGCED countries, there is sufficient experience from other countries that have moved away from similar policies to suggest strongly that the policies are a burden not a benefit to these economies.

As compared with tariffs, such policies have large social costs. Tariff protection has an efficiency effect and a wealth transfer effect. The efficiency effect is a dead-weight loss – use of more domestic resources to support a given level of consumption. The wealth transfer effect is however a transfer from domestic consumers to domestic producers, and in part to the government in the form of tariff revenue. These transfers take place within the economy, and hence to the economy as a whole, are not costs. They affect the distribution of income/consumption, but not its total size.

Quantitative restrictions and burdensome procedures that raise the costs of importing have higher social costs. What would be tariff revenue – if a tariff were used – and therefore a transfer within the economy, is replaced by a real, a resource cost. Antidumping, an increasingly popular form of GATT-legal backsliding, has a similar effect. An antidumping order offers the exporter the alternative of increasing her price by a given amount, or seeing the importing country government add an antidumping duty of that amount. It thus transforms what would be tariff revenue collected by the local government into additional revenue collected by the exporter.

Based on Hufbauer and Elliott's (1994) calculations of the efficiency and transfer effects of United States protection, the tariff revenue transfer is about four times as large as the efficiency cost of a tariff. Stated another way, a given level of protection provided

to selected domestic producers will have social costs five times larger if provided by a quantitative restriction or a cost-increasing administrative arrangement rather than by a tariff.

The impact of these NTBs –the selective restrictions, the wide-spread use of import licensing and of state trading companies – is to magnify the social costs of trade policy: both the immediate or static social costs of the policies and dynamic, or long run effect on the efficiency of resource use. Such policies grant a privileged position to particular traders and thus prevent trade from having a competitive effect.[4] Eliminating trade's competitive effect unfortunately also eliminates its stimulative effect and its capacity to impose business discipline and hence efficiency in the use of national resources. This form of managed trade – through special licensing arrangements and quantitative restrictions, also has the effect of transferring what might be tariff revenue into profits collected by the privileged enterprises.

5. GRAVITY MODEL ANALYSIS OF TRADE CHARACTERISTICS

We know generally that small countries tend to trade a larger part of their GDP than larger countries and that countries with similar cultural heritage tend to trade more with each other than those with dissimilar. To take such factors into account systematically, researchers frequently use what are called "gravity models." In these models, trade between two countries depends on their relative size (GDP, Population, Land area) and on transaction costs (proxied by distance and cultural similarities). In contrast with economists' usual insistence on developing the analytical basis for a model before it is used, gravity models have come into popular use mainly because of their robust empirical success in the prediction of trade flows.

Analysts have frequently applied gravity models in two tasks: (a) to predict the trade flows that would evolve for the formerly socialist countries as they shifted to market economies, and (b) to assess the effects of preferential trade agreements (PTAs). In the former application, researchers used parameters estimated for market-based economies along with the size and transaction-costs variables for the non-market countries. That procedure was used, for instance, to predict the trade of eastern European countries (e.g. Havrylyshyn and Pritchett, 1991; Wang and Winters, 1992), or Cuba (Montenegro and Soto, 1996). In assessing the effect of PTAs, the basic gravity equation is expanded with dummy variables for trading partners belonging to the same regional grouping. If a dummy for a particular PTA turns out to be positive and statistically significant, the researcher concludes that the PTA has an effect in boosting trade among members. Aitken (1973) was the first to test in this way for such effects. The approach has been

[4] Webb (1997) elaborates on the use of trade restrictions to protect the market power of local trading companies.

used by Braga, Safadi and Yeats (1994), Bayoumi and Eichengreen (1995) and Frankel and Wei (1996).

In both of these applications, the central feature of the model is that the value of trade between two particular countries is estimated by their *gravity variables*: size and transaction costs. Once the model is calibrated, the researcher, by plugging in the parameters for any pair of countries (e.g., GDP, population, land area, distance between them, cultural similarities) can determine how much the countries would trade with each other if they traded "normally," i.e., if there were no special factors that influenced that trade. Montenegro and Soto, 1996, for example, used such an approach to predict trade between Cuba and the United States, if relations between the two countries were normalized.

To test if a PTA between countries has affected the level of trade between them, the researcher asks if trade between the countries is larger than what the *gravity variables* would predict. Such an effect would be verified by the sign and statistical significance of the dummy coefficient for the PTA.[5]

Application to CGCED countries

We use here a gravity model to examine how the trade of the CGCED countries has been affected by the CARICOM and by several regional groups among neighboring countries that might be expected to have a negative impact on them; the NAFTA and the Mercosur.

The effect of CARICOM on trade among members

If CARICOM had no effect on the trade of the CGCED countries, then the normal determinants of trade flows between countries would explain trade flows among them. If however CARICOM has systematically increased trade, then a so-called "dummy variable" that isolates trade among CARICOM members should also be significant. Table 8 reports tests of the significance of all of the parameters of the model, including a dummy variable for intra-CARICOM trade. We see in the table that the CARICOM parameter is highly significant. Though the customs union is incomplete – there remain some internal restrictions – it has significantly increased trade among its member countries.[6]

The effects of NAFTA on CGCED countries' trade

We used the gravity model also to assess the impact of the formation of NAFTA on Caribbean exports to NAFTA countries. We wanted to answer the following: Did the formation of NAFTA imply trade diversion – a reduction of NAFTA imports from the

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[5] In the Appendix we describe the econometric specification of the gravity model and the data we used to estimate the model. The data include only non-fuel merchandise trade.

[6] Thoumi (1989) obtained a similar result.

CGCED countries?[7]. The information the model provides on this question is summarized in the first column of Table 9. Looking at this information, we note first that the variable introduced to detect non-normal imports (too high or too low) of the NAFTA countries from the CGCED countries is not statistically significant.[8] This indicates that the importance of NAFTA countries as trading partners of the CGCED countries is "normal" – a result of the sizes and locations of the economies involved rather than of any special relationship. We note secondly that the NAFTA parameter did not change in magnitude or statistical significance when the NAFTA was implemented in 1994. NAFTA countries' imports from the CGCED countries *before* the signing of NAFTA were about what would be expected considering relative sizes of the economies and the other gravity variables. The situation did not change *after* NAFTA was implemented in 1994.

This result, at first impression, is counter-intuitive. CGCED exports to the US and to Canada are to some degree competitive with Mexican exports, and the NAFTA does provide Mexico better access to those market than is enjoyed by outsiders. Webb (1997, pp. 10-12) presents information on CGCED and Mexican exports of clothing to the US that is consistent with this intuition.

Figures 4-7 look further into the matter. We see in Figure 4 that over 1990-1996 CGCED countries roughly maintained their share of the US import market for textiles and clothing. Mexico's share however increased sharply after 1994. Figure 5 provides much the same picture for the Canadian market.[9]

Figures 6 and 7 provide a similar analysis of CGCED and Mexican shares of US and Canadian imports of <u>all merchandise</u>. We see the same general pattern as we found for imports of textiles and clothing; a more-or-less constant CGCED share and a growing Mexican share.[10] (Again, Canada's imports are in total smaller than those of the United States moreover, both the CGCED countries and Mexico have a smaller share of the Canadian than of the US import market.) There is however, no sharp jump at the time of NAFTA implementation – neither upward for Mexico's nor downward for the CGCED countries' share. The pattern is more consistent with a growing relative supply capacity in Mexico[11] – or with the relative movements of real exchange rates we saw in Figure 3 –

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[7] Presumably, now tariff-free Mexican exports to US under NAFTA would crowd out imports from other countries.

[8] Similar results were obtained by modeling US imports rather than NAFTA imports from CGCED countries.

[9] Canadian imports of textiles and clothing (from all countries) in 1996 were about one-tenth as large as US imports.

[10] In the model, the size of the economy is one of the variables that explains trade. As CGCED exports expanded along with the size of the market, but no more, the NAFTA parameter has the same value before and after the agreement was implemented.

[11] Obviously being inside NAFTA gives Mexican exporters an advantage over exporters from the CGCED countries. The information we have presented suggests that the supply effect has been larger, but one should be careful as to what one describes as cause or effect. The growth of capacity in Mexico could

than with an advantage on the demand side created by the NAFTA. Our analysis has not disentangled the impacts of the various factors.

The effects of MERCOSUR on CGCED countries' trade

Table 9, second column, reports an analysis of CGCED exports to the Mercosur countries. In this case the parameter for CGCED exports to Mercosur countries is statistically significant – and negative – in all the years covered by our sample; 1988-1996, which brackets the period over which Mercosur was implemented. There is no statistically significant change of the size of the parameter over this period. These statistics suggest that (a) like the formation of NAFTA, the formation of Mercosur has not affected CGCED exports, and (b) CGCED exports to Mercosur countries are lower than what "normal" trading relationships would suggest – i.e., imports by Argentina, Brazil, Paraguay and Uruguay from CGCED countries are *below* what would be expected considering size and other gravity variables of the countries involved.

6. THE POSITIVE AGENDA OF TRADE REFORM

Liberalization – opening up to the competition and the stimulus of international markets – is a necessary part of using the trading system as a vehicle for development. There is, of course more, the capacity to take advantage of opportunities offered by the system. Mr. Lee Kuan Yew, Senior Minister of Singapore, in explaining Singapore's development strategy, has made the point as effectively as anyone.[12] Senior Minister Lee began his explanation as follows:

Thirty years ago, we asked ourselves two questions:

1. *How do we make Singapore the best place in the world to do business?*
2. *How do we position the people of Singapore to benefit from that situation?*

In his presentation, the Senior Minister spent little time on trade liberalization. Openness was already there, Singapore began its development program with minimal restrictions on international trade and investment. Mr. Lee described how Singapore set up a sound and honestly enforced system of commercial law, an up-to-date communications and transport infrastructure. He reviewed also the importance of a responsibly managed public budget and a sound monetary system that provided seamless linkages with enterprises all over the world. Equally emphasized was an extensive program of human resource development: health, housing, and education, including extensive job-related training.

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be ascribed to NAFTA making Mexico a more attractive platform for investment, this effect being anticipated and therefore smoothed out over the period covered by our data.

[12] These paragraphs are based on a lecture given by Senior Minister Lee at a training program organized by the World Bank for officials of the Government of Vietnam in April 1994 in Hanoi.

The critical elements

Senior Minister Lee's presentation was a cogent reminder both that development is a broader issue than trade and that trade is a broader issue than removal of quantitative restrictions and reduction of tariffs. The essentials of trade policy for development have been reviewed many times,[13] the key elements of what we will call the positive agenda of trade policy are:

- Enterprise development -- establishing a private sector dynamic.
- Human resource development -- in government and in the private sector.
- Trade facilitation, e.g., efficiency and transparency of customs administration.
- Infrastructure; physical, e.g., transport, communications and legal-institutional.
- Using the WTO and other international instruments effectively.
- Openness to international trade and investment.

We have listed openness last not to suggest that it is the least important of the elements, but emphasize the importance of the others. Openness is however critical.[14] For any country, world prices are the true measure of opportunity costs. Any decision – public or private – made without reference to those costs will misuse resources.[15]

7. THE CHALLENGE OF INCLUSION

Recall if you will the example often used to illustrate the principle of comparative advantage and the resulting gains from trade. Though the best lawyer in the city may also be the fastest typist, it does not make economic sense for her to type her own briefs. The same point on a larger scale: two countries, one more productive in all activities than the other, can both benefit from specialization and trade.

While this example does explain that there will be gains to the country as a whole from improved resource allocation, it does not address how development will evolve from there. Already when many of today's developing countries were colonies of richer

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[13] See, for example, World Bank 1987 and World Bank 1993. Fischer (1998) provides a more recent examination that affirms what is reported in the older reviews.

[14] There is an extensive and growing body of empirical research that confirms the importance of the various factors for development. Benhabib - Spiegel (1994) and Mankiw-Romer-Weil (1992) confirm the role of human capital, particularly as a facilitating variable that magnifies the return to physical capital and to infrastructure. As to the importance of openness to trade, Sachs and Warner (1995) have found that there is an almost two percentage point difference in average annual growth between economies that over the long term are open versus those that are closed. Over twenty years, that growth difference cumulates to an almost 50 percent higher real GDP for the open economies.

[15] A risk of calling attention to the capacity-building dimensions of the positive agenda is that this focus will tempt a government to put off opening up. To do so would be a mistake. Without the stimulus, competition and discipline of exposure to international markets, an attempt to implement all of the positive agenda except openness would soon come to the sorts of policies profiled above, in Section 4.

countries, anthropologists had observed the problem of economic dualism: when modern and traditional economies come in contact, there often evolves in the lower income economy a modern sector that benefits, alongside a traditional sector that did not. More recently, Mexican novelist and historian Carlos Fuentes has called attention to this problem in his writings on neo-liberal Darwinism. Modernization, Fuentes worries, is leaving so many behind. World Bank President James D. Wolfensohn (1997) has referred to such situations as *the tragedy of exclusion*, or from the perspective of a work program, *the challenge of inclusion*.

Hence Senior Minister Lee's second question: *How to position the people of Singapore to benefit from making Singapore the best place in the world to do business?*

The positive trade agenda thus is about more than overall growth, it is about the challenge of inclusion, and the related question, how to improve not just resource allocation, but resource productivity where it is lower.

Inclusion and openness

Does facing the challenge of inclusion suggest a return to import protection? Carlos Fuentes, discussing how to bring the poor – who have been left behind to now – into modern society asks rhetorically "Must we go back to the old formula: import substitution, high tariff barriers, statism?"

"¡No way!" he answers. "The logic of the market is unavoidable, [the way onward] is human development."[16]

The politics of protection is not the politics of inclusion.[17] Protection is special interest politics, a small group within a country struggling to establish or maintain a position of privilege against the more diffuse interests of a larger number of domestic citizens. Just as the status and role of women is a sound clue to a nation's development potential,[18] the political strength of protectionism is a good test of how far the process of inclusion has yet to go.

8. NEGOTIATIONS AND TRADE LIBERALIZATION

Through the 1980s and into the 1990s, trade policy decisions taken by developing countries were mostly taken unilaterally. The medium for these decisions was the policy-making process in individual countries, supported sometimes by multilateral institutions. The information we have to measure the extent of this unilateral liberalization is limited to the part of it that has been supported by World Bank programs, but the numbers for this part alone are impressive. From 1981 through 1994, such unilateral programs to reform exchange rate systems, to eliminate quantitative restrictions and to reduce tariffs

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[16] Fuentes (1995) pp. 3-4. (Authors' translation)

[17] Likewise for the economics.

[18] Landes (1998) p. 413.

affected developing country imports of over 500 billion dollars, in 1993 values.[19] By comparison, at the Uruguay Round, developing countries agreed to tariff reductions that will affect 32 percent or $393 billion of their total merchandise imports (likewise in 1993 values).[20] Thus, while the developing countries were active in the Uruguay Round negotiations, it is fair to say that their trade agenda was dominated over this period by the courageous effort of many individual countries to remove restrictions because the government was convinced that to do so would bring greater benefits than costs to the national economy.

Reform then in developing countries began with governments realizing that the trade policies in place did not serve the national economic interest – that the costs of these policies exceeded their benefits, the policies were isolating the local economy from development opportunities and from the development stimulus that the international trading system offered.

The politics however of opening up is difficult, there are always pressures from producers who are not confident that they can deal effectively with import competition. Reciprocal negotiations have proven to be a useful way to deal with this politics. Negotiation with trading partners to exchange market access brings forward export interests that the government can organize as a counterbalance – export politics is easier to sell than import politics.[21] Thus developing country governments wanting to advance a liberal trade agenda have found reciprocal negotiations an increasingly important part of their policy arsenal.

Among developing as well as among industrial countries, international negotiation, more and more, is where the trade policy action is. An active multilateral agenda continues: the Uruguay Round's built in agenda (e.g., financial services, telecommunications), WTO working groups on several topics, the international community is beginning to consider a "Millennium Round" of WTO negotiations. At the same time, regional negotiations are active in Asia, and Africa; negotiating a free trade area is a big part of the trade agenda in the America hemisphere.

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[19] From 1981, when the World Bank's policy-based lending began, through 1994, the Bank made 238 such loans that supported liberalization of trade policy or foreign exchange policy. These loans, made to 75 different countries, have specified over 2000 trade of foreign exchange policy reforms as conditions for borrowing, and about 80 percent of these reforms have been substantially implemented. The figures above refer to reforms that have been substantially implemented.

[20] The two sets of reductions overlap by an unmeasured amount, i.e., some of the concessions bound by developing countries at the Uruguay Round were previously made unilaterally (re reciprocal negotiations) where they were supported by World Bank programs.

[21] Negotiations also allow a government to lock in reforms against possible backsliding. In this context, the best partner is one not likely to be sympathetic when another party comes under domestic pressure to re-impose restrictions.

9. NEGOTIATIONS AND THE POSITIVE AGENDA

International negotiation, regional and multilateral, has been an effective way to eliminate trade restrictions. CARICOM, Mercosur, NAFTA the European Union, the GATT illustrate the point. Reciprocal negotiations however have done little to advance enterprise development, human resource development, or trade facilitating infrastructure. The WTO has recently established Working Groups on trade facilitation, trade and competition and on trade and investment, but no negotiating agenda has yet emerged.

There are dimensions of the enterprise environment on which negotiations have been a significant determinant of policy. GATT, for example, has a long history of agreements over subsidies that would be allowed and those that would be prohibited. Also, the Uruguay Round Agreements include the specification of intellectual property rules that member countries must have on the books and must enforce, also rules about restrictions that can be placed on international investment and about dimensions of trade administration such as customs evaluation and rules of origin. On these matters however, the negotiations process has provided a minimal sense of reciprocity, except perhaps between the United States and the European Union on subsidies.

In sum, the negotiations process has not taken up significant parts of the positive agenda and except on negotiations over tariffs, has proven more effective in insisting that changes be made than in supporting their implementation.

10. IMPLEMENTING THE POSITIVE AGENDA IN THE CGCED COUNTRIES

Trade policy, more than any other area of policy is ruled by "Murphy's Law" – anything that can go wrong will go wrong. Consequently our policy advice contains more cautions about problems that might crop up than assertions about where to forge ahead. The first and perhaps most important of these is a reminder that reform must be propelled by internal conviction and by internal politics. External agents – negotiations, multilateral lending agencies, bilateral development partners – can support reform but they cannot force it.

Bilateral and international development institutions

International negotiations have not take up many dimensions of the positive agenda. Such dimensions as human resource and enterprise development, infrastructure, cannot be effectively implemented through traditional trade policy instruments. Thus the sorts of development programs countries usually undertake on a unilateral basis – outside of reciprocal negotiations, though often supported by international lending agencies and by bilateral partners – will continue to be important. This suggests that the bilateral partners and the international development institutions – the regional banks, the World Bank, the UNDP – in deciding how their resources will be used, should not limit their trade agenda to supporting developing country participation in trade negotiations.

Capacity-building (human resource and enterprise development, infrastructure) is still important.

Reference to capacity-building projects recalls an important efficiency consideration – openness is about eliminating biases against export activities, not about creating biases in their favor. True to this principle, enterprise development projects that are sensibly "trade-related" should cover enterprises who see potential markets in the domestic economy as well as enterprises that are looking to export.

Regional negotiations – among the CGCED countries

CARICOM has already taken significant steps to reduce trade barriers within the region, and these reductions have stimulated additional trade among the member countries. CARICOM can thus be an effective stepping-stone toward the integration of the CGCED economies into the global economy. The advantages of working within a similar group of smaller economies are many: familiarity and a history of cooperation on many issues facilitate interaction on trade policy. Opening regionally can help to stage the process of opening globally and the participating countries have more effective control of the agenda than they would have in a larger negotiation such as the FTAA negotiations.

On the other side of the coin, a shared understanding of each others' problems brings the risk that the partners will not be sufficiently demanding of each other, and that they will be too understanding of each other's need to pull back on certain commitments when domestic opposition emerges. Locking in reforms through international agreement requires an unsympathetic partner.

A final caution, while the CGCED countries acting together can be a stepping stone to globalization, internal liberalization cannot be the end of the path. The populations of these countries add up to approximately that of the state of Texas in the United States, the economies (GDPs) sum to approximately that of the city of Chicago.[22] Furthermore, after significant reduction under CARICOM of internal barriers, only five percent of CGCED trade is within the CGCED countries. Within the group, the available scale will not allow for global efficiencies, nor will it be sufficient to produce the competitive stimulus and business discipline that comes from effectively contestable markets.[23] Even as a stepping stone, what there is to gain from liberalization among the CGCED countries may not justify using the region's skilled but limited negotiating resources there rather than in a larger arena.

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[22] The small scale of the Caribbean economies taken together implies that any local arrangement should avoid complexity. The potential gains are not large enough to justify the administrative expense of, e.g., complex rules of origin.

[23] As to the politics of using a regional agreement as a stepping stone to globalization, it is legitimate to ask if regional cooperation unites liberal interests more effectively than protectionist. A courageous paper by ECLAC (1996) has raised this question.

CGCED countries in the FTAA negotiations

The CGCED countries recognize that particularly for small countries who can be severely affected by trade diversion,[24] being inside a regional agreement is certainly preferable to being outside. The hemispheric negotiations can be viewed from two perspectives: (a) how to extract from other countries market access commitments of particular interest to the CGCED countries, and (b) how to use the negotiations to support and to lock in reforms within the CGCED countries.

Concessions from trading partners

A sensible point of emphasis by the CGCED countries has been to identify where the NAFTA discriminates against them, and to seek remedy either through the FTAA negotiations or through other avenues. The CGCED countries might likewise review the Mercosur Agreement and other agreements in Latin America. As we pointed out in Sections 5, CGCED trade with Mercosur countries is unusually low.

On products of special export interest to the CGCED countries, it might be useful to work with import users and consumers in partner countries. Though formal processes such as antidumping and safeguards usually exclude formal consideration of the interests of users and consumers, these interests can still have an influence.[25] In more fluid political processes like international negotiations they can have even greater influence.

Another issue of particular relevance to smaller countries is to pay attention to rules that will help to control the larger countries' temptation to backslide. Protectionist interests in the larger countries work hard to include opportune modification of safeguard and antidumping rules.[26] Again, import users in the larger countries can be a useful ally to identify such proposals. As to specifics, smaller countries might insist that industrial users – even consumers – be recognized as "interested parties" in antidumping and safeguard cases and other forms of permitted backsliding.[27]

Objective and transparent dispute settlement (i.e., enforcement) is particularly important for smaller members. The difference between a power-based and a rules-based organization depends on the objectivity and transparency of dispute settlement.

Complexity however works against transparency. To a small enterprise, a complex process, though objective, can be too costly for the small enterprise to sustain. A complex process can thus have the same disadvantage as one based simply on power.

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[24] Bernal (1996) p. 949.

[25] The influence of industrial users can have an influence even where user interest is not formally recognized. Braga (1993), for example, shows that the interests of large consumer products companies were taken into account in US antidumping cases against Brazilian orange juice.

[26] Unfortunately, protectionist interests in developing countries seem to have learned quickly from their kindred spirits in the industrial countries. Since the Uruguay Round was completed, developing countries have undertaken more antidumping cases than the industrial countries. Finger (1998) provides details.

[27] This point is elaborated in Finger (1998).

Knowledge, as well as size, is power. The success of the skilled diplomats of the smaller countries to shape the Uruguay Round agenda and to influence its outcome is proof.

Using negotiations to support reforms in the CGCED countries

Negotiating with trading partners has many times proven to be a useful way to advance a liberalization process, but negotiating with trading partners can also turn a country's economic liabilities – its own trade restrictions – into political assets. The first concern of any participating government should be to keep its focus on how to use the negotiation to support its own reforms.

We found in Section 4 that many of the CGCED countries have in place administrative arrangements and other NTBs that have significantly higher social costs than tariffs. Because these are the more costly of their restrictions and because tariffs are an important source of public revenues for some of the countries, the negotiations should find a way to support their reduction, i.e., to allow the CGCED countries to substitute concessions on such NTBs for commitments to reduce tariffs.

It is true that diplomats have found tariffs concessions easier to compare and to negotiate than reductions of NTBs, but the Uruguay Round negotiations on agriculture did find ways to deal with NTBs.

The CGCED countries need not bear the entire burden of developing techniques to negotiate over such NTBs. A commitment has already been made by the negotiating parties to pay attention to the particular problems of the smaller economies. The larger countries – to meet this commitment – should support (not just insist on) reform of the policies in the smaller countries that are in particular need of reform. The larger countries should help to develop techniques to make such NTBs negotiable, and they should specify their "requests" from the smaller countries in such terms.

It would be unfortunate if the subgroups on the problems of the smaller economies found nothing to do other than to debate if the smaller economies will be exempted from the level of reform expected of the other participants. This resort to the negative side of special and differential treatment for the smaller economies would be a missed opportunity by the smaller economies to advance their own interests through internationally supported reforms of their own policies. It would also be a failure by the larger countries to use in a constructive way their inevitable control over the negotiating agenda.

The smaller economies have much to gain from trade reform, and the FTAA negotiations can be an important instrument to advance this reform. Competent work has already established that there is no correlation between size, by several reasonable measures, and economic growth, nor between size and responsible macroeconomic performance.[28] The balance of risks and opportunities is no different for the small economies than for the large. The smaller countries should participate in the negotiations in full confidence of their own capacity to take advantage of the development potential

[28] Organization of American States (1997)

that the international trading system offers, and in full confidence of the support of their development partners: the other negotiating countries, the multilateral and regional institutions. Further integration by the smaller economies into the international economy is not a threat, it is an opportunity.

TABLES AND FIGURES

TABLE 1: SELECTED CHARACTERISTICS OF THE ECONOMIES IN CGCED COUNTRIES, 1995

Country/Group	Population ('000)	GDP Per Capita ($)	Real GDP Growth /a 1990-95 (%)	Current GDP ($ Mill)	Structure of Production as % of GDP				Gross Dom. Investment as % of GDP (%)	Adult Illiteracy Rate (%)
					Agriculture (%)	Mining (%)	Manufactures (%)	Services (%)		
CGCED:										
Antigua and Barbuda	65	7800	1.8	507	4	17	3	76	22	5
Bahamas	276	12534	-0.3	3459	3	2	2	93	18	2
Barbados	266	6548	-0.4	1742	5	8	8	79	13	3
Belize	216	2676	4.3	578	19	14	13	54	26	9
Dominica	73	3110	1.9	227	26	11	7	56	26	6
Dominican Rep.	7800	1446	4.2	11278	15	6	15	64	20	18
Grenada	91	3030	1.7	276	14	14	5	67	32	3
Guyana	835	744	7.2	621	36	26	11	27	19	2
Haiti	7200	284	-2.9	2043	46	11	6	37	2	55
Jamaica	2500	1762	1.0	4406	9	20	18	53	17	15
St. Kitts & Nevis	41	5484	3.4	225	6	14	12	68	39	10
St. Lucia	158	3517	3.6	556	11	14	7	68	25	10
St. Vincent	111	2305	3.4	256	18	19	4	59	39	18
Suriname	410	816	1.6	335	26	10	16	48	23	7
Trinidad and Tobago	1300	4097	1.1	5327	3	34	9	54	14	2
CGCED Total/Average	21342	1492	2.1	31834	16	15	9	60	22	11
CGCED Total/Average	6342	2919	2.3	18514	14	16	9	62	24	7
(Excl Dom. Rep & Haiti)										
Latin America Total/Ave /b	456558	3628	4.1	1656361	15	11	18	57	19	15
Low and Middle Income	4770800	1130	2.1	5393142	14	16	20	48	27	30
Countries Average /c /d										

Sources: World Bank, World Development Report 1997, World Bank Atlas 1997, and IMF, International Financial Statistics Yearbook 1997

Notes: /a Average annual growth of GDP in constant prices.
/b Exclude CGCED countries.
/c All low and middle income developing countries are based on the classifications of WDR 1997.
/d The real GDP growth rate could reach at 3% in 1990-95 if transition economies were excluded.

TABLE 2: SELECTED CHARACTERISTICS OF THE TRADE PATTERNS OF CGCED COUNTRIES, 1995

Country/Group	Total Trade as % of GDP /a (%)	Structure of Exports as % of Total Exports (g+s)				% of Merchandise Exports Going to			% of Merchandise Imports Coming fr.		
		Agriculture (%)	Mining (%)	Manufacturing (%)	Commercial Services (%)	North America/c (%)	Latin America/d (%)	Other CGCED (%)	North America (%)	Latin America (%)	Other CGCED (%)
CGCED:											
Antigua and Barbuda	171	5	16	6	73	7.0	58.6	3.0	36.7	11.7	10.1
Bahamas	129	11	8	33	48	28.6	4.4	0.6	38.6	8.2	0.1
Barbados	100	13	1	25	61	31.4	36.0	29.4	34.2	20.3	17.0
Belize	119	58	1	12	29	29.5	4.2	2.5	38.2	29.7	4.3
Dominica	164	23	2	53	22	8.6	13.2	12.5	15.1	18.6	14.1
Dominican Rep.	98	13	1	72	14	88.9	0.9	0.3	65.8	15.3	1.3
Grenada	100	27	1	10	62	23.8	27.8	22.0	29.8	42.9	38.9
Guyana	175	36	19	15	30	35.2	9.2	7.7	35.9	29.8	24.2
Haiti	64	13	1	37	49	73.5	1.1	0.0	66.3	9.0	1.1
Jamaica	151	13	6	45	36	57.4	4.5	2.6	59.2	16.7	9.3
St. Kitts & Nevis	122	18	0	30	52	60.9	5.0	5.0	48.3	22.5	22.1
St. Lucia	136	34	0	22	44	28.8	10.3	9.3	30.6	20.0	17.9
St. Vincent	159	47	0	28	25	7.3	15.7	15.5	22.9	6.6	4.8
Suriname	441	16	10	56	18	14.8	6.3	0.0	23.5	57.1	6.3
Trinidad and Tobago	79	11	33	47	9	49.2	27.6	15.8	49.9	18.0	2.9
Average, CGCED Countries	**112**	**15**	**9**	**50**	**26**	**60.8**	**9.2**	**5.1**	**51.9**	**18.0**	**5.4**
Average, CGCED excluding											
Dom. Rep & Haiti	110	16	14	39	31	43.8	24.3	16.6	52.7	17.2	8.9
Average, Latin America	31	21	19	41	19	47.6	19.8	1.2	45.3	18.4	0.4
Average, Low and Middle											
Countries /b	53	12	10	63	15	23.8	5.5	0.3	19.2	4.4	0.1

Notes: /a Total trade includes exports and imports of all merchandise goods and commercial services.

/b All low and middle income developing countries are based on the classifications of WDR 1997.

/c Canada and the United States

/d Includes Mexico

Sources: World Bank, World Development Report 1997, World Bank Atlas 1997, IMF, International Financial Statistics Yearbook 1997; and UN COMTRADE database.

Latin America and Caribbean in WDR or WDI includes, in principle, all countries in the South of America, Mexico and CGCED, of course, included, but WDR and WDI provided data only for four CGCED countries (Dominican Rep., Haiti, Jamaica, and Trinidad & Tobago), others were treated as missing data.

TABLE 3: SUMMARY OF TRADE RESTRICTIONS AND ARRANGEMENTS IN CGCED COUNTRIES

CGCED Country	Tariff Structure (%)	Additional Surcharge /a (%)	QRs and Import License (ML) Required	Other NTBs (State Trading)	Foreign Exchange Transaction	Export Tax & License (XL)	Preferential Trade /b Arrangements
Antigua and Barbuda	0-35% for all 40% for prim agr	CS=5% CT=10-15%	ML for agric goods and other special goods	STE for rice & sugar	1% tax application	none	CARICOM OECS
Bahamas	0-42% for all 30-62% durable	ST=2-7%	ML for agric goods	few other NTBs no imp monopoly	prior approval	with some export taxes	CARICOM
Barbados	5-25% for all 40% for prim agr	CS=75%, ET VAT=15%	ML & QR for food & other sp. goods	STE for chicken wine, sugar, milk	1% tax application	XL for some food products	CARICOM
Belize	0-30% for all 40% for prim agr	VAT=15% OT	ML for agric goods, many gds banned	STE for rice	1.25% tax prior approval	XL & tax 2-5% for agric prod	CARICOM
Dominica	0-30% for all 40% for prim agr	CS=15-16% CT=25%	ML for manuf gds QR for beverages	STEs for rice & sugar	prior approval	some XLs req. and 1% tax for banana	CARICOM OECS
Dominican Rep	5-35% for all 5-80% lux. gds	CS=5-20% ST=3% CT=6%	no ML many gds banned	STEs for petro. resale	dual exch rates applied	XL for sugar	ACS, Lome' Convention
Grenada	0-25% for all 40% for prim agr	CS=5% CT=25%, OT	ML for agric goods QR for cars	STEs for rice, sugar, milk prod	5% tax	XL for sp. goods	CARICOM OECS
Guyana	5-25% for all 40% for prim agr	CT=0-85% OT (envir tax)	ML for petro. & agr, many gds banned	STEs for papers & agric goods	adv. deposit	XL for gold and tax for rice & sugar	CARICOM
Haiti	5-15% for all 25% for gasoline	OC=4% ET=1-5%	ML for agric gds & others some banned	STEs for agric & machinery	application	XL for agric and exp QR for textiles exp QR for textiles	
Jamaica	0-50% for all 40% for prim agr	ST=65-90% CT=15%	ML for agric goods; many gds banned	STEs for food & cars	auction sys.	XL for cars and sp. goods	CARICOM
St. Kitts & Nevis	0-30% for all 40% for prim agr	CS=3% CT=15%	ML for some manuf goods	STEs for chicken, sugar, wheat, eggs	adv. payment	few XL and tax	CARICOM OECS
St. Lucia	0-30% for all 40% for prim agr	CS=4%, ET CT=3-45%	ML for food & other sp. goods	STEs for rice, sugar, flour, fish	2% tax	XL for sp. gds and 2.5% tax for banana	CARICOM OECS
St. Vincent	0-25% for all 40% for prim agr	CT=0-65% CS=2.5%,ET	ML for food & other gds; some banned	STEs for oils& fat, sugar, daily prod	2% tax	XL for agric and 2% tax for banana	CARICOM OECS
Suriname	5-30% for all 40% for prim agr	CS=2% ET=5-18%	ML for all imports; some QRs & ban	STEs for some food items	prior approval	XL for agric and tax for sp. gds	
Trinidad and Tobago	5-25% for all 40% for prim agr 20-30% durable	CS=5-103% VAT=15% ET	ML for consumer gds and many gds banned or with QR	STEs for rice, wheat, fats & oils; petro	only for some goods	XL for food and petro gds	CARICOM

Notes: /a CS=Customs surcharges; ST=Stamp tax; CT=Comsumption tax; ET=Excise tax; VAT=Value Added Tax; and OC=Other charges
/b CARICOM=Caribbean Common Market; OECS=Organization of East Caribbean States; and ACS=Association of Caribbean States.
Sources: UNCTAD, Handbook of Trade Control Measures of LDCs 1987; IMF Exchange Arrangements & Restrictions, 1997; and Caribbean Export Development Agency, Country reports on Import Regimes, 1997.

TABLE 4: FOREIGN EXCHANGE ARRANGEMENTS AND RESTRICTIONS IN CGCED COUNTRIES, MEXICO, COSTA RICA AND EL SALVADOR

Country	Exchange rate structure and Classification[a]	Exchange control authority	Controls on export and import of Banknotes	Export repatriation, surrender requirements	Capital controls
Antigua and Barbuda, Eastern Caribbean Dollar		Ministry of Finance	Yes, foreign currency	No	No
The Bahamas, Bahamian dollar[b]	Pegged	Central Bank	Yes, both domestic and foreign currency	Yes - or used in a manner acceptable to the central bank	All outward transfers require approval, outflows of resident-owned capital are restricted.
Barbados, Barbados dollar	Pegged	Central Bank of Barbados	Yes, on exports of domestic and of foreign currency	Yes	Yes
Belize, Belize dollar	Pegged	Central Bank of Belize	Yes, on both domestic and foreign currency	Yes	Yes, but control is liberally administered
Dominica, Eastern Caribbean dollar	Pegged	Ministry of Finance	Yes, on exportation of domestic currency	Yes, unless the exporter has an authorized foreign currency account	All outward transfers require approval
Dominican Republic, Dominican peso[c]	Managed float	determined by the Monetary Board, administered by the Central Bank	Yes, on both domestic and foreign currency	Yes, on traditional exports	Only registration requirements
Grenada, Eastern Caribbean dollar	Pegged	Ministry of Finance	Yes, on exports	Yes	All outward capital transfers require exchange control approval.
Guyana, Guyana dollar	Ex. rate freely determined in the cambio market.	None	Only declaration requirements	No	Abolished Dec. 31, 1996
Haiti, gourde	determined in the exchange market	Bank of the Republic of Haiti administers the foreign exchange system	No	No	Inward direct investment requires prior approval
Jamaica, Jamaica dollar	determined in the interbank market. There are reqs that some for. ex. be sold to the Bank of Jamaica.	Trading in foreign exchange is prohibited, except by and through an authorized dealer.	No	No	Administered by the Min. of Finance. The Min. of Finance has authority to issue directions regarding the acquisition of foreign assets.
St. Kitts and Nevis, Eastern Caribbean dollar	Pegged	Ministry of Finance	No	Yes	All outward capital transfers require exchange control approval.

St. Lucia, Eastern Caribbean dollar	Pegged	Min. of Finance, Statistics and Negotiating	No	Abolished March 1, 1996	Approval required for transactions over EC$100,000.
St. Vincent and the Grenadines Eastern Caribbean dollar	Pegged	Min. of Finance	na	Yes	All outward capital transfers require exchange control approval.
Suriname, Suriname guilder	freely determined in the interbank market	Central Bank of Suriname	Limits, domestic currency; declaration requirements on large transfers of foreign currency.	Yes, except for companies that have received special permission.	Controls on inward direct investment, outward direct investment is not permitted, but exceptions can be made.
Trinidad and Tobago, Trinidad and Tobago dollar	freely determined on the interbank market	Central Bank	declaration requirements for large amounts	In practice, the foreign-owned petroleum company operating in T&T repatriates all foreign currency after providing for its needs.	Restrictions on inward direct investment and on non-resident purchases of local real estate.
Mexico, Mexican peso	independent floating	None	No	No	Restrictions on purchases abroad, by residents, of foreign securities.
Costa Rica, Costa Rican colón	Managed float	Central bank	No	Repatriation, Yes; Surrender, No.	No
El Salvador, Salvadorian colón	Managed float	Central Reserve Bank	No	No	Registration requirements for some FDI; minimum capital reqs. for businesses owned by foreigners.

Source: International Monetary Fund, Exchange Arrangements and Exchange Restrictions, Annual Report 1997, Washington, DC, International Monetary Fund, 1997.

Notes:
[a] Escept The Bahamas and the Dominican Republic, all countries listed have unitary exchange rate systems.
[b] Dual, separate "investment currency."
[c] Dual exchange rate system, official and interbank rates.

TABLE 5: CARICOM COUNTRIES; RESTRICTIONS ON IMPORTS FROM WITHIN CARICOM, QRS AND LICENSING OF IMPORTS FROM OUTSIDE CARICOM

Country	Restrictions on imports from CARICOM partners	Number of product categories subject to quant. import restrictions or restrictive licensing when imported from outside CARICOM[a]
Antigua and Barbuda	import licenses required for 12 product categories when imports are from non-OECS[c]	51 - includes most foods, consumer non-durables, household appliances
Barbados	import licenses required for 12 product categories, mostly vegetable oils.	20 - foods, beverages, motor vehicles
Belize	import licenses required for 10 product categories; food, beverages, furniture	33 - foods, beverages, clothing
Dominica	duties on cigarettes, rum and motor vehicles from MDC[b]	32 - food, beverages, consumer non-durables, wooden furniture
Grenada	duties on cigarettes, rum, motor vehicles import licenses required for 16 product categories - foods, beverages, appliances	45 - food, consumer goods, vehicles
Guyana	import licenses required for wheat flour, animal and veg. fats and oils and products include. waxes	meats, fruits, groundnuts; products made from
Jamaica	duties on milk and cream (fresh, evaporated or condensed), steel re-bars	25 - milk, cream and products; vehicles and parts; industrial chemicals
St. Kitts and Nevis	import license required for sugar, beer, some appliances, foods, beverages	45 - food, beverages, vehicles, appliances
St. Lucia	duty on rum from MDC[b], import licenses required on 30 product categories	127
St. Vincent and the Grenadines	duty on rum import license required for 16 product categories when imported from Belize or from non-OECS[c]	42 - food, beverages, cosmetics, carpets, mats, plastic pipes and tubing (used in the banana industry) recapped tires
Suriname	?	quotas on 16 product categories prohibitions on 20 product categories - foods, footwear, wood products, fishing boats
Trinidad and Tobago	duties on selected products import licenses required for animal and vegetable fats and oils	35 - foods, beverages, cigarette paper, animal and veg. fats and oils, ships and boats

Source: Tabulated from reports of the Caribbean Export Development Agency

Notes:

[a] Does not include restrictions based on sanitation, security or public health or public morals.

[b] More Developed Countries

[c] Organization of Eastern Caribbean States.

TABLE 6: COMPARISON OF PORT CHARGES IN CARIBBEAN COUNTRIES DURING 1986-87
(charges in US$)

Port	Handling	Total
Antigua	4,508	5,749
Aruba	11,570	12,381
Barbados	17,336	17,897
Costa Rica	2,887	4,145
Freeport	650	1,473
Grenada		9,410
Guatemala	529	3,074
Haiti	1,950	12,802
Honduras	3,0000	6,825
Jamaica	4,725	5,744
Nassau		2196
St. Barths	150	446
St. Croix		1,546
St. Kitts	3,477	3,876
St. Lucia		5,535
St. Thomas		1,491
St. Vincent	3,778	4,315
Trinidad	4,433	9,672

Source: Alexander J Yeats, "Do Caribbean Exporters Pay Higher Freight Costs?" World Bank Discussion Paper WDP-0062, November 1989

Note: The figures are based on a vessel of constant size with the same cargo tonnage.

TABLE 7: HERITAGE FOUNDATION, WALL STREET JOURNAL INDICES FOR RESTRICTIVENESS OF IMPORT POLICY AND OF CAPITAL FLOWS AND FOREIGN INVESTMENT POLICY

Country	Trade	Foreign Capital Flows and Investment
Bahamas	5	3
Barbados	4	2
Belize	5	2
Dominican Republic	5	3
Guyana	4	3
Haiti	4	4
Jamaica	2	2
Suriname	5	3
Average (CGCED countries above)	4.3	2.8
Costa Rica	4	2
El Salvador	3	2
Guatemala	3	3
Honduras	4	2
Nicaragua	5	2
Average (Central American countries above)	3.5	2.4
Bolivia	2	2
Brazil	4	3
Chile	2	2
Colombia	4	2
Ecuador	3	2
Mexico	3	2
Paraguay	2	1
Peru	3	2
Uruguay	2	2
Venezuela	4	3
Average (Latin American countries above)	3.5	2.5
Average (Latin American and Central American countries above)	3.5	2.5

Source: Heritage Foundation and Wall Street Journal (1997) , Index of Economic Freedom(New York: Dow Jones and Company)

TABLE 8: GRAVITY MODEL RESULTS

Tests on CARICOM Countries and on the Central American Common Market Countries.

	1988	1989	1990	1991	1992	1993	1994	1995	1996
Intercept	-32.76***	-37.58***	-40.84***	-40.56***	-42.91***	-45.57***	-37.98***	-40.71***	-34.42***
Size variables									
GDP country i	1.32***	1.28***	1.26***	1.29***	1.31***	1.31***	1.28***	1.25***	1.51***
GDP country j	1.33***	1.32***	1.29***	1.36***	1.39***	1.32***	1.30***	1.31***	1.59***
Population country i	-0.17***	-0.17***	-0.18***	-0.19***	-0.23***	-0.18***	-0.20***	-0.20***	-0.39***
Population country j	-0.02	-0.18**	-0.20***	-0.28***	-0.30***	-0.21***	-0.18**	-0.19***	-0.44***
Area country i	-0.13***	-0.09***	-0.10***	-0.05	0.03	0.00	0.01	0.00	0.03
Area country j	-0.28***	-0.13***	-0.08**	-0.06	0.03	0.01	0.00	-0.01	0.06
Proximity variables									
Average distance country i	1.70***	2.14***	2.17***	2.18***	2.35***	2.43***	2.00***	2.17***	1.94***
Average distance country j	1.96***	1.89***	2.17***	1.93***	1.77***	2.13***	1.68***	1.78***	0.53
Distance between i and j	-1.44***	-1.41***	-1.35***	-1.36***	-1.36***	-1.40***	-1.33***	-1.27***	-1.22***
Common border	0.19	-0.01	0.12	0.11	0.14	-0.04	-0.01	-0.24	-0.38
Country i is an island	-0.47***	-0.73***	-0.60***	-0.61***	-0.78***	-0.48***	-0.51***	-0.61***	-0.59***
Country j is an island	-0.08	-0.15	-0.22*	-0.17	-0.17	-0.10	-0.09	-0.21*	0.19
Common language									
Spanish	1.33***	1.20***	1.12***	1.21***	1.30***	1.40***	1.39***	1.32***	1.49***
English	0.29	0.29	0.32	0.28	0.01	0.00	0.17	0.27	0.01
Arabic	2.65***	2.65***	3.01***	2.86***	2.24***	2.48***	2.47***	2.67***	2.87***
Portuguese	0.15	-0.30	0.10	0.26	0.12	0.03	0.04	-0.06	0.31
Intra-Regional Trade									
Caricom countries	3.15***	3.24***	3.41***	3.44***	3.08***	3.53***	3.13***	3.37***	3.67***
Central American Countries	0.64	1.62**	1.91***	1.91***	2.08***	2.02***	1.93***	2.32***	3.59***
Summary statistics									
Number of Obs: 2556									
Pseudo R2 (1-Sum Sq. err/ Total Sum Sq)	81.6	80.9	81.8	81.9	81.6	82.3	82.1	82.5	79.4

Statistical significance: *** 99%, ** 95%, * 90%

TABLE 9: EFFECT OF NAFTA AND MERCOSUR ON CARIBBEAN EXPORTS
Gravity model estimates.

Year	Magnitude and statistical significance of a dummy variable that captures Caribbean exports to countries in NAFTA	Magnitude and statistical significance of a dummy variable that captures Caribbean exports to countries in MERCOSUR
1988	-0.19	-2.21 ***
1989	0.22	-2.49 ***
1990	-0.24	-2.52 ***
1991	0.05	-2.70 ***
1992	-0.13	-3.23 ***
1993	0.15	-2.35 ***
1994	0.08	-3.09 ***
1995	0.21	-3.30 ***
1996	0.32	-2.56 ***

Note: the value of the dummy variable reflects whether the level of trade among these countries is above (if the dummy is positive) or below (if the dummy is negative) what would be expected for countries of similar size (GDP, population, land area) and that deal with similar transaction costs (distance, common borders, common language).

*** denotes statistical significance at 99%.

FIGURE 1: DESTINATION OF CGCED EXPORTS, 1980-1996

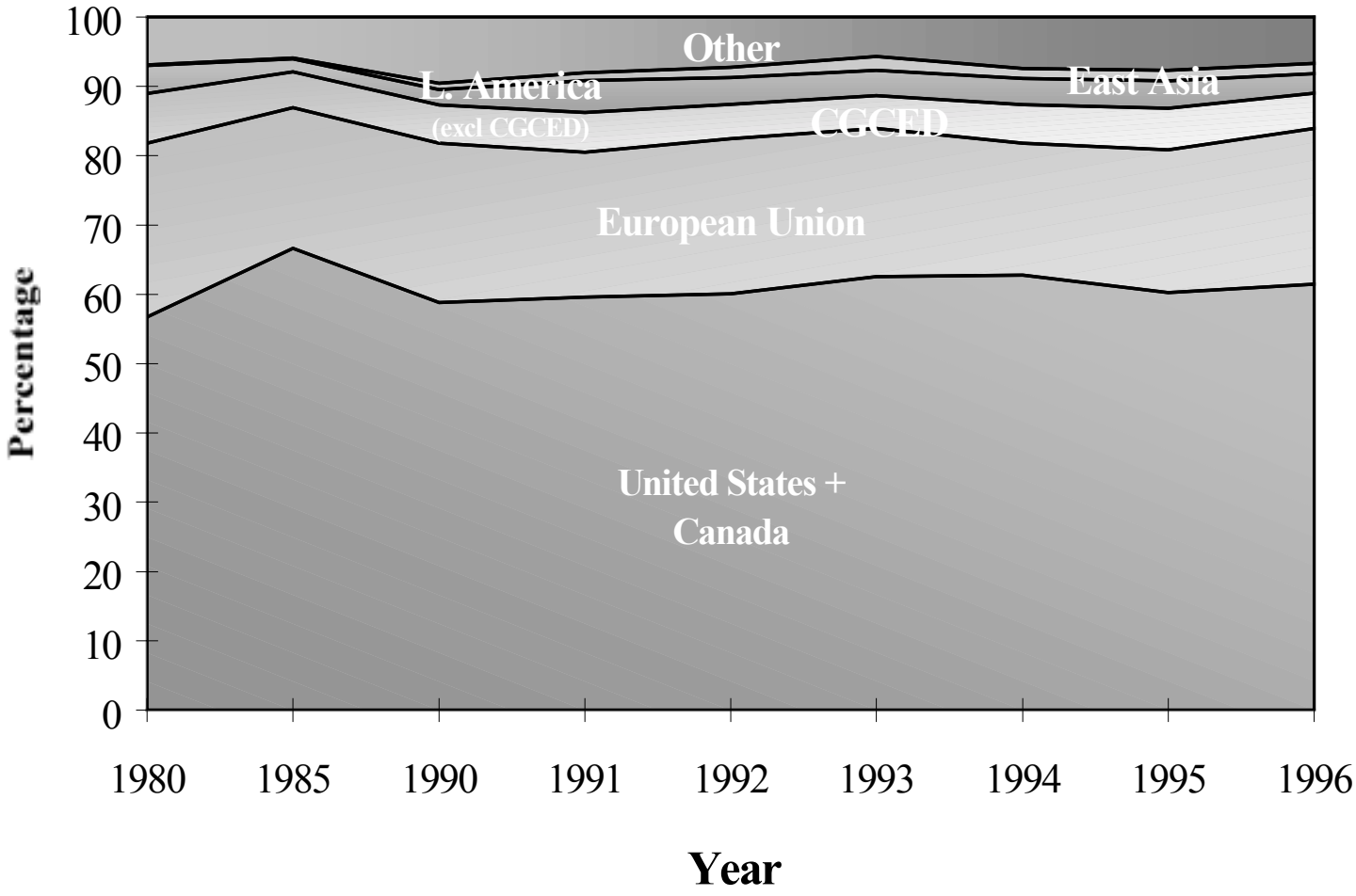


FIGURE 2: ORIGIN OF CGCED IMPORTS, 1980-1996

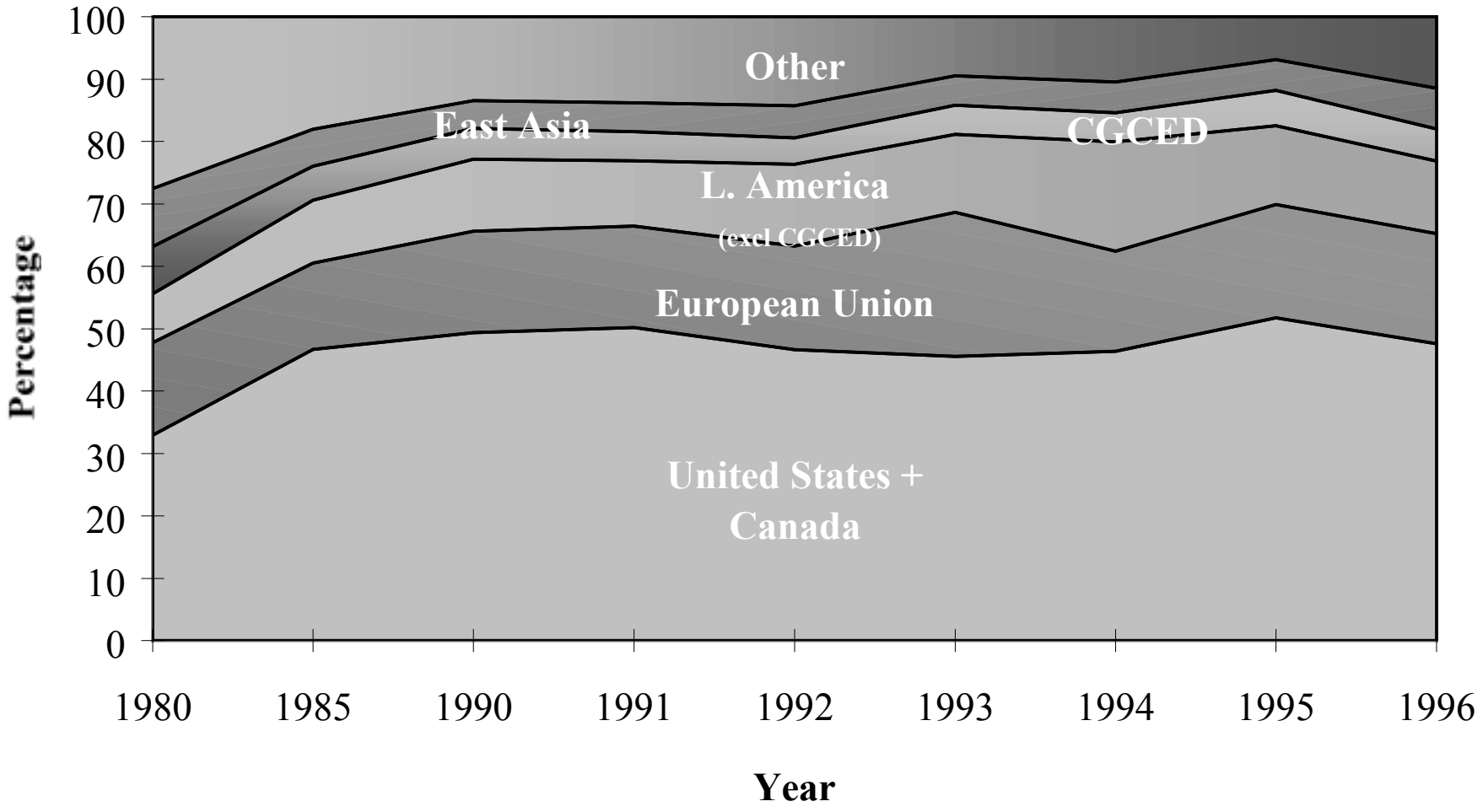


FIGURE 3: REAL EXCHANGE RATE MOVEMENTS, CGCED COUNTRIES AND COMPARATOR COUNTRIES

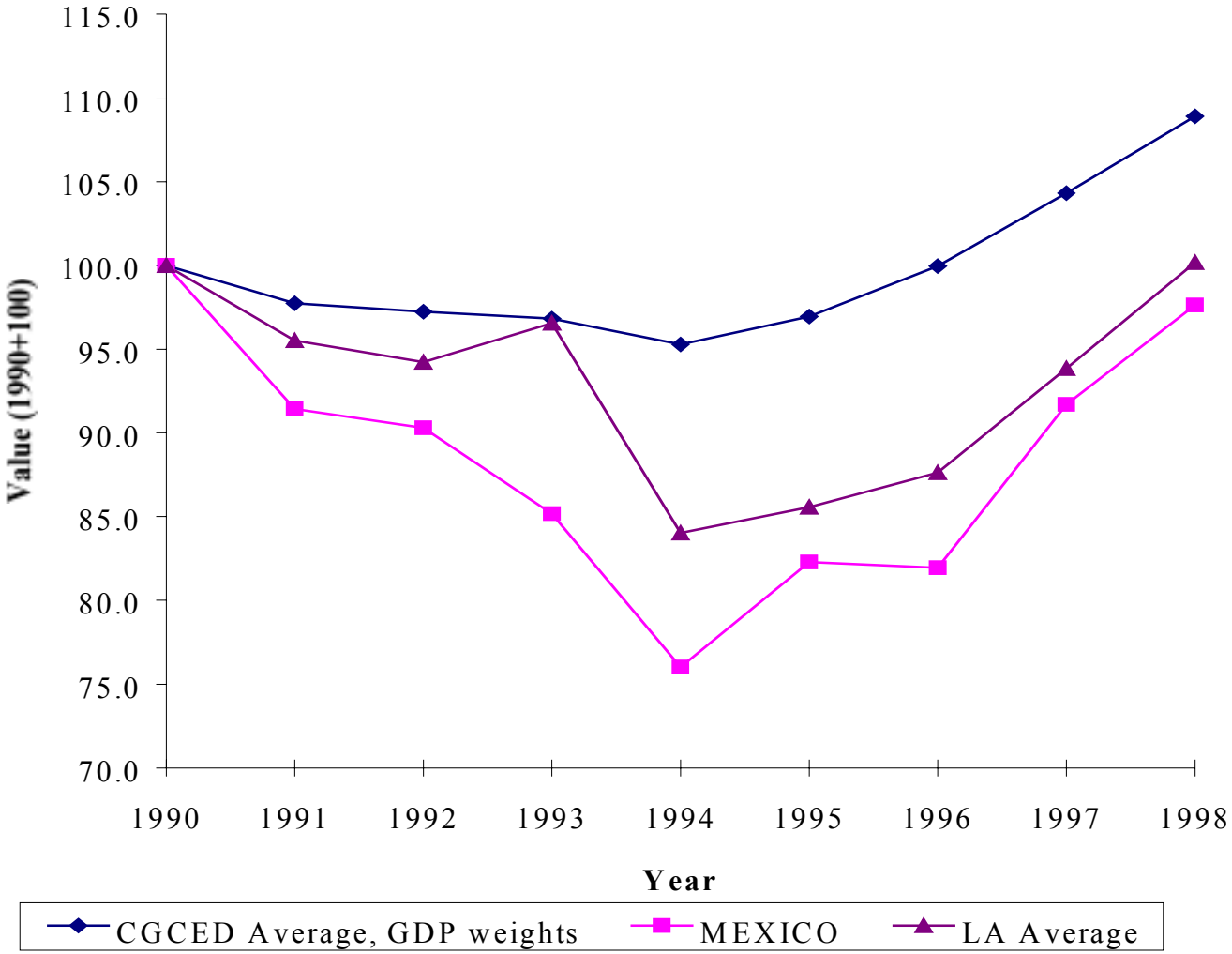


FIGURE 4: CGCED AND MEXICAN SHARES OF US IMPORTS OF TEXTILES AND CLOTHING

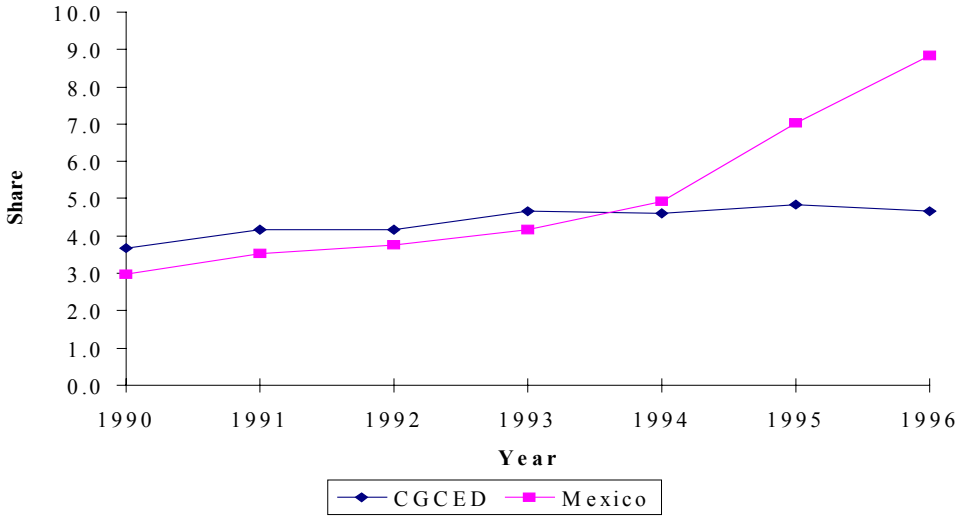


FIGURE 5: CGCED AND MEXICAN SHARES OF CANADIAN IMPORTS OF TEXTILES AND CLOTHING

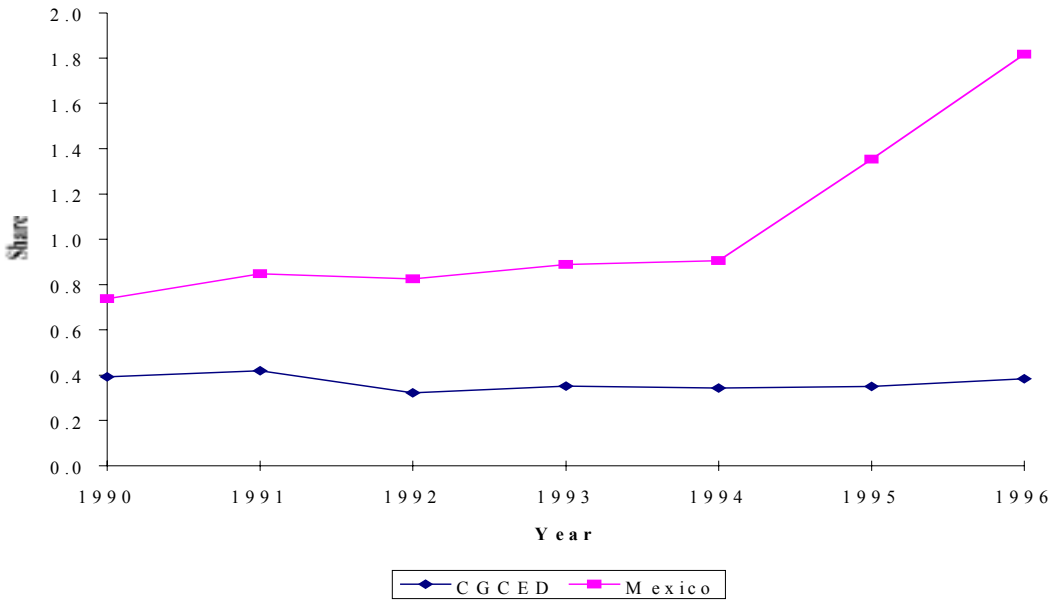


FIGURE 6: CGCED AND MEXICAN SHARES OF US IMPORTS OF ALL MERCHANDISE

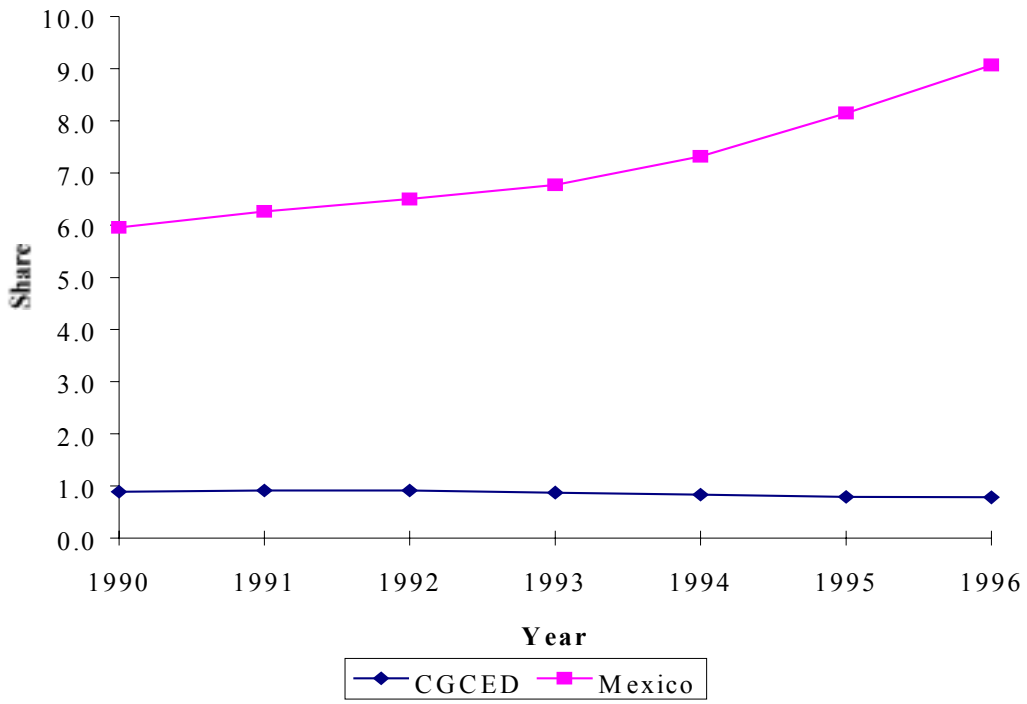
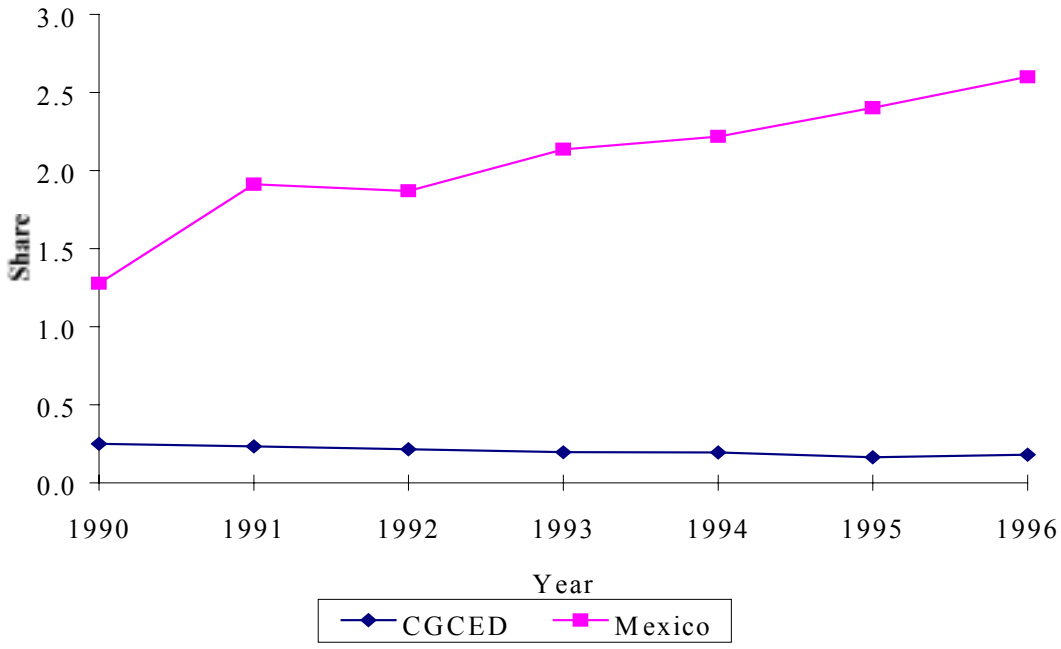


FIGURE 7: CGCED AND MEXICAN SHARES OF CANADIAN IMPORTS OF ALL MERCHANDISE



APPENDIX

The gravity model

The empirical robustness of the gravity model made it a common place in the literature when analyzing trade-flow patterns. Its empirical success is the main reason why we take this approach here to tackle the issue of trade flows in Caribbean countries. Tinbergen (1962), Pöyhönen (1963) and Linneman (1966) provided initial specifications and estimates of the determinants of trade flows. More recently, Anderson (1979), Bergstrand (1985), Helpman and Krugman (1985) and Deardorff (1997) provided partial foundations for the gravity equation, although none of the models generate exactly the equation generally used in empirical work.

The gravity model explains bilateral trade between a country (i), the importer, and a specific trading partner (j), the exporter country, in terms of the following equation:

(I)

$$(TT)_{ij} = BY_i^{\beta 1} N_i^{\beta 2} Y_j^{\beta 3} N_j^{\beta 4} \overline{D}_i^{\beta 5} \overline{D}_j^{\beta 6} D_{ij}^{\beta 7} A_{ij}^{\beta 8} T_i^{\beta 9} T_j^{\beta 10} I_i^{\beta 11} I_j^{\beta 12} L_{ij}^{\beta 13} \prod_k P_{kij}^{\gamma kij} \prod_k P_{ki-j}^{\gamma k-j} \prod_k P_{k-ij}^{\gamma k-i}$$

where

TT_{ij} is the value of trade (imports + exports) of country *i* from and to country *j*,

Y_m is the Gross Domestic Product of country *m*,

N_m is the population of country *m*,

$\overline{D}_i$ is the average distance of country *i* to exporter partners, weighted by exporters' share in world GDP ("remoteness" of country *i*),

D_{ij} is the distance between the economic center of gravity of the respective countries,

A_{ij} is a dummy that takes value 1 if countries *i* and *j* share a land border and 0 otherwise

T_m is the land area of country *m*,

I_m is a dummy that takes value 1 when country *m* is an island,

L_{ij} is a dummy for cultural affinities, proxied by the use of the same language in countries *i* and *j* (one dummy for each one of the following languages: English, Spanish, Arabic and Portuguese).

P_{kij} is a dummy variable representing the *k*th preference relationship between countries *i* and *j*. This variable takes the value 1 if both countries, *i* and *j* belongs to the same bloc *k* and represents the intra-bloc bias of the PTA,

P_{ki-j} is a dummy variable that takes the value 1 when country *i* belonging to the *k*th preference trade agreement imports from non-member countries. This variable represents the import side of extra-bloc openness of country *i*,

P_{k-ij} is a dummy variable that takes the value 1 when country j belonging to the *k*th preference trade agreement exports to non-member countries. This variable represents the export side of extra-bloc openness of country *i*,

B, β_1 to β_{13}, γ_{kij}, γ_{k-j} and γ_{k-i}, are parameters, and

ε_{ij} is a log-normally distributed error term with $E(Ln\varepsilon_{ij}) = 0$

The Data

We used annual non-fuel imports/exports data of 72 countries for 1988 to 1996 from the UN-COMTRADE database. This set of countries represents more than 70% of total world trade. The distance variable was taken from Havrylyshyn and Pritchett, 1991[29]. The source for the rest of variables utilized is BESD.

To follow the evolution of trade for Caribbean countries, we created a regional dummy that includes the fifteen countries in the region. To address the specific issue of the impact of NAFTA and MERCOSUR formation on Caribbean countries' exports to member countries of those PTA, we created two dummies. One tracks the evolution of imports from Caribbean countries made by NAFTA members and the other does the same for imports from Caribbean countries made by MERCOSUR members. Changes in the value of these parameters or in their statistical significance will indicate the effect (if any) of those PTAs on their imports from Caribbean countries.

[29] Lant Pritchett generously provided the data.

The Econometric Approach

We estimated two equations, one for total trade and one only for imports. Because trade volumes are bounded from below by zero, the appropriate estimation procedure is a Tobit model[30].

The estimated equation for total trade is[31]:

$$Ln(X+M)_{ij} = \alpha + \beta 1\, LnY_i + \beta 2\, LnN_i + \beta 3\, LnY_j + \beta 4\, LnN_j + \beta 5\, Ln\overline{D}_i + \beta 6\, Ln\overline{D}_j$$
$$+ \beta 7\, LnD_{ij} + \beta 8\, LnA_{ij} +$$
$$+ \beta 9\, LnT_i + \beta 10\, LnT_j + \beta 11\, LnI_i + \beta 12\, LnI_j + \beta 13\, LnL_{ij} + \sum_k \gamma_{kij}\, LnP_{\gamma kij}$$
$$+ \sum_k \gamma_{k-j}\, LnP_{ki-j} + \sum_k \gamma_{k-i}\, LnP_{k-ij} + Ln\varepsilon_{ij}$$

Results

a) Total trade

We estimated a set of 9 regressions --one for each year-- for the annual data 1988-1996 with the aim of identifying not only the 'level' effect on trade of PTAs but also any variation of this effect through time.

Table 8 presents the estimated value of the parameters and the statistical significance measured by asymptotic t statistics[32]. We found that, as in many other applications of the model in the literature reviewed, the central variables of the gravity model --level of **GDP** of countries *i* and *j*, and the absolute **distance** between *i* and *j*-- have the expected sign and are all significant at 1%: trade increases with the level of GDP of the importer and exporter and decreases with distance. The estimates for **population** were negative and statistically significant whereas the coefficients for **area** were negative

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[30] See, for example, Maddala [1992] for a discusision of the bias in OLS estimates in models with limited dependent variables.

[31] We estimate a log transformation of equation I. Since the data for imports are in thousands of dollars, to model the truncation of the sample at the value 0 we assumed imports to be one thousand dollars when country *i* had 0 imports from country *j* .A similar assumption, albeit in a different context, is applied in Maddala [1992], p 181.

[32] To save space, not all the dummies from the model were reported in Table 8. Results are available from the authors upon request.

and only statistically significant for the first three years of the sample and non significant for the remaining years.

Regarding the proximity variables, the estimates for average distance of countries i and j from all trading partners suggested recently by Polak (1996)[33] were of positive sign and statistically significant. The dummy for **common borders** was not statistically significant and the dummy for **island** was negative and statistically significant when one of the countries was an island[34].

The dummies for **common language** between countries showed to be positive and always statistically significant for the cases of Spanish, English (except in 1992) and Arabic.

Table 8 presents also the estimated value of intra-regional trade for Caribbean and for Central American countries. Both were positive, meaning that intra-regional trade was *above* what it would be considered normal for countries of similar characteristics. The dummy for intra-trade for the Caribbean countries turned out to be significant in 1988, 1992-1994 and in 1996. The dummy for Central American countries was statistically significant in 1990-1996.

We calculated a pseudo R^2 as 1 minus Sum of Squared errors/Total Squared Sum, which turned out to be above 80% except for 1996 (79.4%), indicating a well fit of the data to the model.

b)Imports

With the purpose of capturing possible effects of the formation of NAFTA and MERCOSUR on Caribbean exports to those countries, we estimated a model similar to the one above described with **log of non-fuel imports** as the dependent variable. Table 9 shows that in general the results for the gravity variables were in line to those for the previous model for total trade. As for the impact of NAFTA and MERCOSUR on Caribbean exports, the value of the dummy coefficients for NAFTA imports from Caribbean countries for 1988-1996 was not statistically significant in any of the years covered by our sample. This implies that NAFTA imports' from the Caribbean countries were for the whole period what would be expected for countries of that size and gravitational variables. On the contrary, for MERCOSUR countries the gravity model results indicate that imports from Caribbean countries made by Argentina, Brazil, Paraguay and Uruguay were *below* what would be expected considering size and other

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[33] Polak suggested the inclusion of this variable to take into account the empirical fact that, *after controlling for absolute distance*, remote countries generally trade more. A similar development is found also in Deardorff (1997) and an application in Frankel (1997).

[34] Not all the researchers used a dummy for **island**. Its inclusion here is based only on the empirical performance of the model selected. Regarding its sign, some authors found the dummy for **Island** to be positive and significant for the importer as well as for the exporter (Montenegro and Soto, 1996) but others found that the sign depends on the direction of trade: positive when imports are modeled as the independent variable, and negative for exports (Havrylyshyn and Pritchett, 1991).

gravity variables of the countries involved (the dummy coefficients were negative and statistically significant), their value fluctuating around -2.5 without any noticeable trend.

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