# Report on Trade Liberalization

*by*

The Tourism Taskforce
on
Trade Liberalization

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# Preface

In December 1994 the Bahamian Government with 33 other countries in the Western Hemisphere declared –

> "A key to prosperity is trade without barriers, without subsidies, without unfair trade practices, and with an increasing stream of productive investments.
> "Eliminating impediments to market access for goods and services among our countries will foster our economic growth…
> "We, therefore, resolve to begin immediately to construct the 'Free Trade Area of the Americas' [FTAA]."[1]

This Declaration was repeated at every meeting of Trade Ministers since 1994 and it is embodied in the proposed Free Trade Area of the Americas Agreement.

In late summer 2002 Mr. J. Barrie Farrington, President of the Bahamas Hotel Employers Association, and Mr. Frank Comito, Executive Director, The Nassau Tourism Development Board approached Mr. Ralph J. Massey,[i] an economist, to do a study on trade liberalization for the "Tourism Taskforce on Trade Liberalization". Over a five month period ten drafts were produced and vetted. The focus of this collaborative effort was initially on "Free Trade"…chapters three and four…and then on the immediate concerns of the industry.

The Tourism Taskforce concluded that whether the Bahamas continued in FTAA or not –

1. **The Bahamas needs both foreign direct and domestic investment to produce sustained growth.**
2. **It is a high cost country and this fact limits its development options and endangers tourism, the source of its prosperity for the past half-century.**
3. **It must take concerted action to improve its competitive position and avoid even more drastic remedial measures.**
4. **It must change and this includes its "norms of behavior, conventions, and codes of conduct".**
5. **Its people must become its greatest asset.**
6. **It must become a desirable place to do business.**

Points one and two are the most pressing for the tourism industry and therefore for the country. They are addressed in Chapters One and Two.

The Taskforce is aware that small countries can succumb to foreign pressures and implement legislation that is deleterious to their self-interests. It appears that the financial legislation of Christmas 2000 that drastically affected the offshore financial sector is a good example of this.

It is also aware that the fate of small countries is not solely in the hands of bigger countries. Yes…countries such as Chile and New Zealand have adopted programs that have been successful.

But a better example is Ireland. This is a small island country that struggled for its political independence. Some say it started in 1172 when the "Normans outlawed the Irish";[2] it ended in a tough 3-year urban guerilla war in 1922.

Ireland also experienced poverty and starvation on a massive scale in the mid 19th century and an important economic "victory" at the end of the 20th Century. Page one of the Irish Industrial Development Authority website relates to the latter and appears on the following page.

These Irish goals and accomplishments are consistent with the 1994 Miami FTAA Declaration. A more detailed account appears in Appendix I, The Irish Example.

[i] Ralph J. Massey received a BA Degree in Economics from Case Western Reserve University where he graduated magna cum laude Phi Beta Kappa. He was a Harry A. Millis Fellow in Industrial Relations and a Research Associate in the Department of Economics at the University of Chicago where he received a MA Degree. This was followed by a 37-year career in international business and banking and a 7-year association with the Nassau Institute.

www.idaireland.com

IDA Ireland is the agency with government responsibility for securing new investment from overseas in manufacturing and international services sectors. IDA Ireland also encourages existing foreign enterprises in Ireland to expand their businesses.

Over 1,200 companies have chosen Ireland as their base to serve the European market and beyond. These companies are involved in a wide range of activities from manufacturing to e-Business activities in sectors as diverse as electronics, software, pharmaceuticals, healthcare, finance and international telecommunications.

Ireland provides investors with a unique investment environment through a combination of --

• A skilled and flexible workforce,
• One of the lowest corporate tax rates in the world and
• The youngest and one of the best educated populations in Europe."

However, in the case of the Bahamas the 1994 Declaration is sharply inconsistent with the laws, practices and beliefs of Bahamian politicians, businessmen, labour leaders and citizens. These laws, practices and beliefs are part of the "institutional setting" that economists identify as the key determinant of economic growth. This is the subject of Chapter Two.

This report addresses these issues and the associated options, risks and rewards. It does all of this with a degree of candor that some might find "insensitive". But the Taskforce believes that the gravity of the present crisis and the magnitude of the problems to be resolved require it.

## Chapter One

# The Bahamas in Crisis

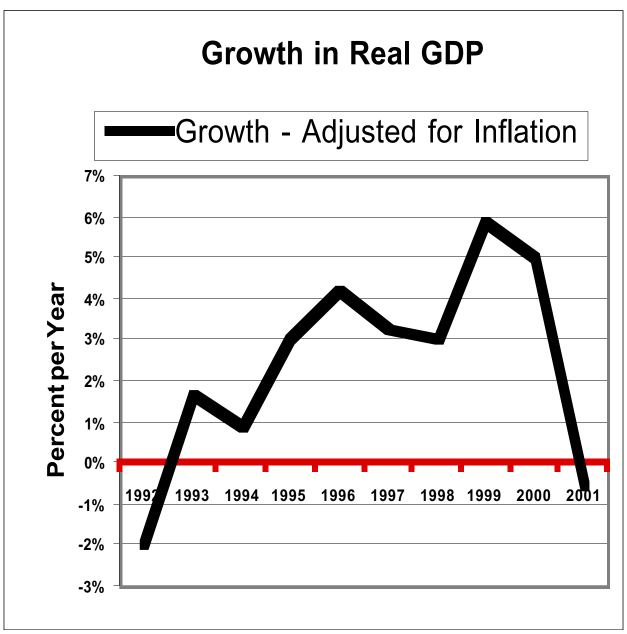
### The Good Times 1993 - 2000

The FTAA Declaration and the draft Agreement recognize the importance of investment, and particularly foreign direct investment, in achieving sustained economic growth. The Bahamas has only to look at its own recent history to recognize this reality.

**The Balance of Payments 1997 – 2001**

| | B$ Millions |
|---|---|
| Net Imports of Goods and Services | (2,672) |
| Net Capital Inflow | 2,525 |
| Net Errors & Omissions | 306 |
| Increase in Foreign Reserves | 159) |

Source: Central Bank of the Bahamas




In 1992 Hubert A. Ingraham became Prime Minister and literally got on a plane and toured the investment capitals of the world. His message was "There's a change in the Bahamas…It's a good place to invest…See me to get on the fast track."

He was successful. As we all know the key investor was Sun International. The importance of these investments appear in the "Net Capital Inflow" in the Balance of Payments Summary for 1997-2001 in the table to the left.

The Bahamian prosperity triggered by the investment flows of the 1990s was stunning. They ended a decade of economic stagnation. GNP grew over six years (from 1995 to 2000) at 4.1 percent per year in real terms…that is GNP adjusted for inflation. The entire 10-year period that had two depression years, 1992 and 2001, registered an annual growth of 2.5 percent per year…an outstanding achievement.

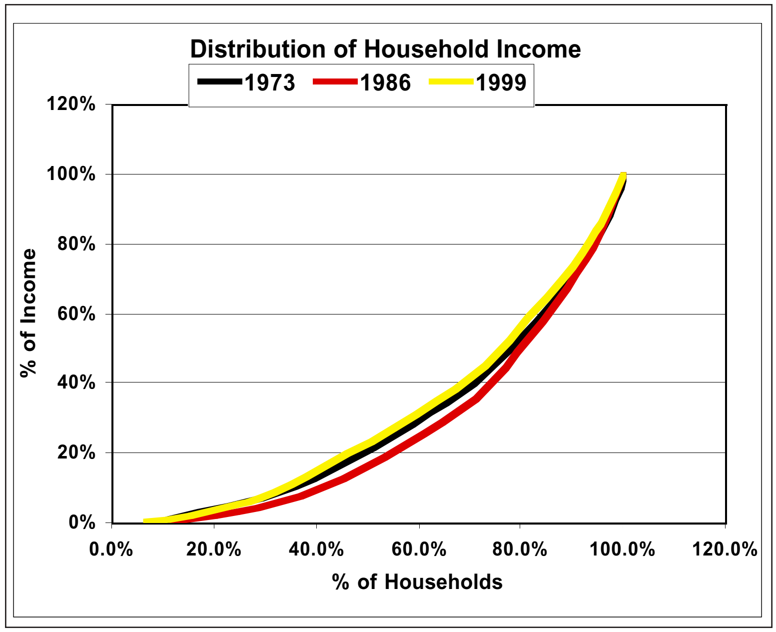
Other less-developed countries have realized this and this is seen in the references to Ireland and Mexico in this Report. This Bahamian experience with prosperity lends credence to a statement by a Nobel Prize winning Professor of Economics from Massachusetts Institute of Technology –

**"The notion that the poor countries of the world can in any reasonable interval achieve rich-country incomes without trade and capital flows is utterly implausible."**

And even more importantly, the benefits of that prosperity were distributed in favor of the "working classes". The Distribution of Household Income for the years 1973, 1986 and 1999 as reported by the Department of Statistics are shown on the following page.

Between 1973 and 1986 the Lorenz Curve, a curve that plots the distribution of income among households, bowed to the right meaning that income became divided more unequally. Between 1986 and 1999 the curve bowed to the left indicating a reversal; the share of the lower 60 percent of households of total income increased 31 percent. The visibly small movement in the shape of the Lorenz Curve in the graph drastically understates its importance.

However, the alarming fact of Bahamian life is the disconnection between business and economic reality and both the political rhetoric and popular beliefs so often reported in the media. For instance, the Hon. Hubert A. Ingraham stated before Parliament that the 1990s prosperity had overlooked the common man and this necessitated the passage of the three labour bills in December 2001. This rationale is clearly not true and every repetition of this message inflames and perpetuates the anti-foreign and anti-business bias of Bahamian culture.

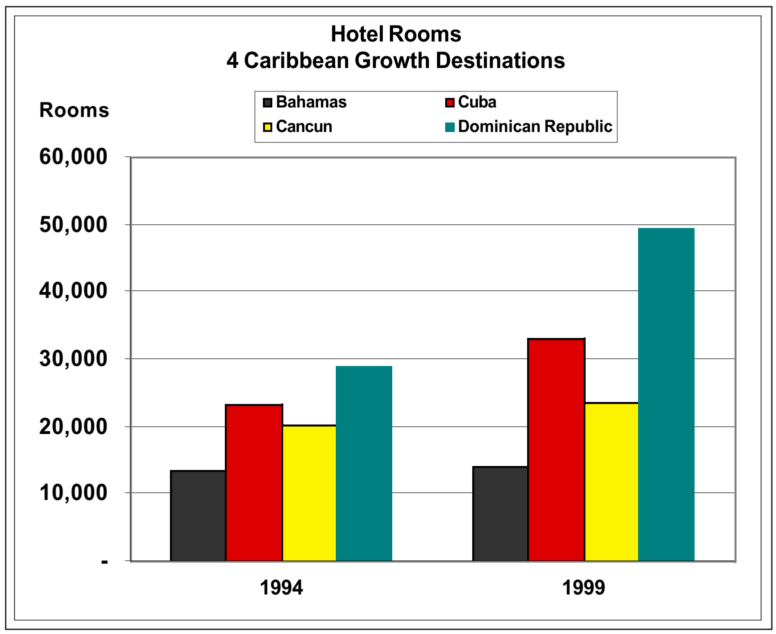



## Bahamian Hotels

The $2.2 billion invested in the hotel industry, particularly the $1.2 billion invested in Atlantis, was the driving force in this prosperity.

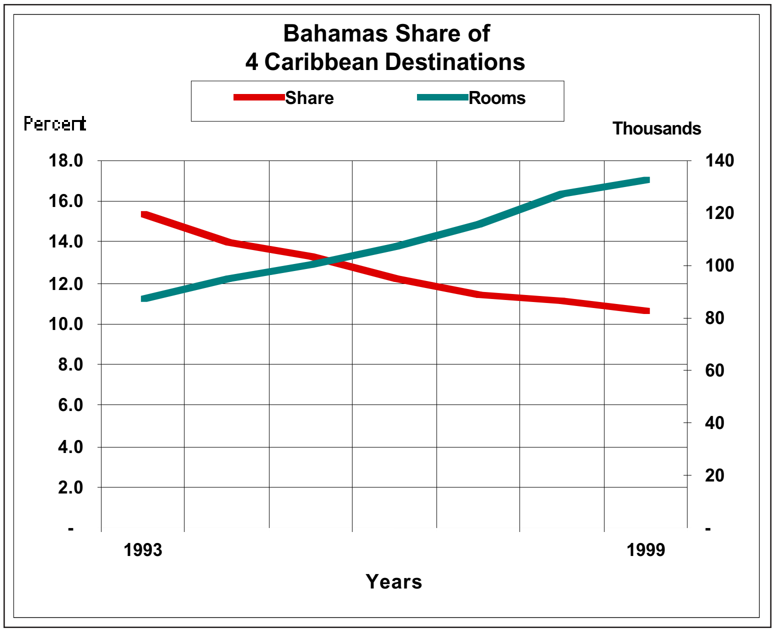
The creation of the Atlantis mega-resort provided the Bahamas with a competitor to Orlando and Las Vegas. A failure to enter this tourism sector in all likelihood would have produced another 10 years of economic stagnation in the Bahamas.

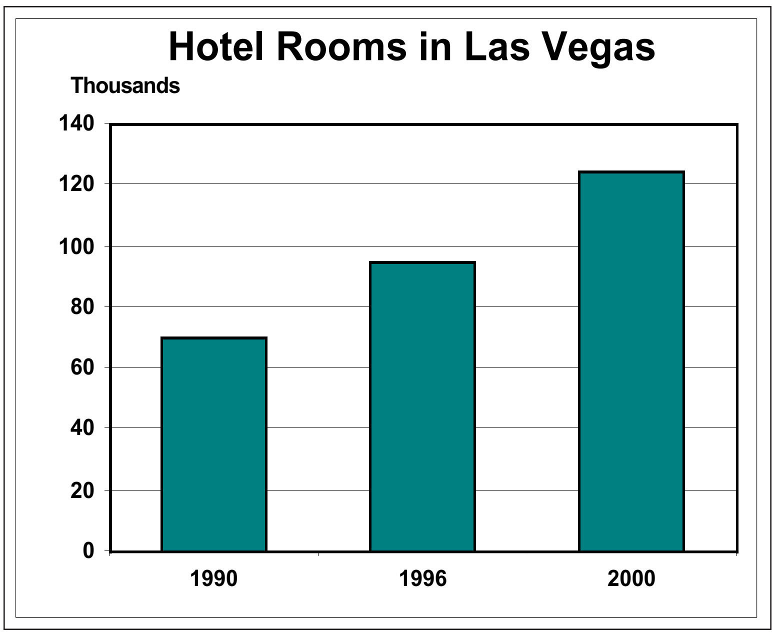
Furthermore, it should be no surprise that the profitability of this market segment contributes disproportionably to the recovery in Gross and Net Operating Profits.




### Investments in Bahamian Hotels 1994-2000

| | $Millions |
|---|---|
| Atlantis | $1,200 |
| Our Lucaya | 400 |
| Emerald Bay | 250 |
| Sandals | 150 |
| British Colonial | 80 |
| Breezes | 50 |
| Nassau Marriott | 41 |
| Other Hotels | 70 |
| Total | $2,240 |




The investment in Bahamian tourism had two major parts: the Atlantis mega-resort infrastructure and the refurbishment and modernization of existing hotel rooms. A minor part was the net addition in the total of installed rooms. The Bahamian total did not expand greatly nor did it match the expansion elsewhere.

The four Caribbean growth destinations are the Bahamas, Cuba, Cancun and the Dominican Republic. As can be seen in the graphs to the left the 6 percent growth in total rooms in the Bahamas between 1994 and 1999 was exceeded by the 43 percent growth of Cuba, the 17 percent of Cancun and the 71 percent growth of the Dominican Republic. Not shown is Jamaica that declined 13 percent.

The total rooms in these four markets grew by 51 percent and the Bahamian share dropped from 15.4 percent in 1993 to 10.7 percent in 1999 as can be seen in the graph to the left.

**The uncomfortable truth is that the $2.2 billion created a real presence in the mega-resort business. However, it was not sufficient to stop the decline of the Bahamas in the Caribbean tourism market.**

At the same time as this growth was occurring in

## High Operating Costs

**Comparative Operating Costs**
**Nassau vs. Two Comparable Hotels**
**Jan – Nov 2002**

| | | Nassau | Caribbean | North American |
|---|---|---|---|---|
| **1.** | **Room Occupancy** | **70%** | **72%** | **71%** |
| | **Average Room Rate…** | **$131** | **$129** | **$115** |
| | Nassau Over………………… | | +2% | +14% |
| | **Gross Operating Profit** | **9%** | **22%** | **35%** |
| | Nassau Under………………. | | -59% | -74% |
| | **Selected Nassau Expenses Over** | | | |
| **2.** | Room Payroll……………… | | +40% | +17% |
| | Food & Beverage Payroll | | +25% | +17% |
| **3.** | Food & Beverage Expenses | | +21% | +183% |
| | General & Administrative | | +27% | +75% |
| **4.** | Power, Mechanical & Utilities | | +36% | +114% |
| | Information Technology | | +25% | +25% |

Source: A monthly operating report of one hotel operator

### 1. Gross Operating Profit

The lag in the growth of tourism capacity in Bahamas relative to the tourist growth destinations is in large part due to the high operating costs and lower rates of return experienced in the Bahamas.

This is clearly seen in the actual operating data for the first 11 months of 2002 in the monthly operating report of a representative hotel operator. It is a "CONFIDENTIAL" monthly report to company management that uses a common accounting system with common definitions and standards. This is the Comparative Operating Data for three hotels, a Nassau, a Caribbean and a North American. The occupancy rates were comparable and the average daily room rate was $131.00 for Nassau, $129.00 for the Caribbean and $115.00 for the North American. The Nassau average room rate was 2% and 14% higher respectively.

The shocker is the "BOTTOM LINE", Gross Operating Profit…9% for Nassau, 22% for the Caribbean and 35% for the North American. The Nassau hotel's Gross Operating Profit was a stunning 59% below the Caribbean hotel and 74% below the North American hotel.

Strictly speaking, Gross Operating Profit is not really the "BOTTOM LINE" since it does not include interest, depreciation, amortization and taxes. This means that the Nassau hotel was at best in a "break-even" position on net profits.

### 2. Pay and Productivity

Repeatedly Ministry of Tourism executives, Central Bankers, businessmen and key union executives talk about pay and productivity…exclusively in general terms without hard data. The combined Pay and Productivity penalty is identified in the Room and Food & Beverage Payroll costs in the Monthly Operating Report. The Nassau Room Payroll was 40% greater than the Caribbean hotel and 17% greater than the North American hotel and the Nassau Food & Beverage Payroll was respectively 25% and 17% greater.

Unfortunately, this Report does not identify the separate effects of pay and productivity. Nevertheless, it is clear that payroll and productivity place the Nassau hotel at a distinct competitive disadvantage.

**Weekly Salaries w/o Gratuities Nassau vs. Two Comparable Hotels Yearend 2002**

| | Nassau | Dominican Republic | North American |
|---|---|---|---|
| **Waiter** | $205 | $42 | $230 |
| Nassau +/- | | +492% | -11% |
| **Cashier** | $297 | $78 | $460 |
| Nassau +/- | | +380% | -36% |

**Hourly Compensation Costs for Manufacturing Workers**

| Country | US Dollars |
|---|---|
| Bahamas | $10.83 |
| Mexico | 2.34 |
| Brazil | 3.02 |
| Korea | 8.09 |
| Spain | 10.88 |
| Ireland | 13.28 |
| France | 15.88 |
| Japan | 19.59 |
| United States | 20.32 |
| Germany | 22.86 |

Sources: US Department of Labor, 2002 & An Authoritative Bahamian source

The first table above shows the weekly salaries without gratuities for a waiter and a cashier in a Nassau hotel versus the Dominican Republic and North America.

Nassau has a very large salary disadvantage relative to the Dominican Republic (Nassau salaries are much higher.) and a smaller but significant advantage versus the North American (Nassau salaries are lower.). The Payroll costs previously cited and this data suggest that --

1. The hotel in the Dominican Republic uses more labour thus reducing its significant cost per unit of labour advantage versus Nassau (Its payroll advantage is smaller relative to its unit labour cost advantage.)
2. North America's higher labour productivity more than offsets its salary disadvantage versus Nassau (Higher labour productivity creates a payroll advantage.).

And there is other evidence on the comparative cost of labour as seen in the lower table to the left. The U. S. Department of Labor collects data on manufacturing wage rates in many countries. The data for a representative Bahamian worker has been added in the table to the left. Such a worker earns $10.83 per hour in base pay plus benefits. It is significantly more than Mexico, Brazil and Korea. This table simply shows the relative cost per worker per hour and does not measure worker productivity.

Among other things this data explains why it is so difficult to establish manufacturing businesses in the Bahamas. Whether Bahamians recognize it or not, this relatively high labour cost limits the country's development options in the Global Economy.

## 3. Pilferage, Wastage & Management

Where the competitive disadvantage is greatest is in Food & Beverage Expenses. It is absolutely astounding that "Food & Beverage Expenses" for Nassau are 183% above the North American hotel. This difference reflects the high cost of pilferage and wastage.

This Report states over and over that the Rule of Law is a critical element in economic development. The Bahamas is a country that accepts stealing and the slow and uneven administration of justice. These raise the cost of transacting business; and high transaction costs limit the size of the firm and growth itself.

In the banking business, for instance, it increases loan losses and diminishes a bank's willingness to lend in all but the most secure circumstances.

## 4. Utility & Mechanical Costs

The second greatest cause for the relatively poor profit performance of the Nassau hotel is Mechanical & Utility Expenses that are 36% greater than the Caribbean and 114% greater than the North American hotels.

A major culprit is the inflated cost of electricity. A Bahamian business can expect to pay the Bahamas Electricity Corporation 16-18 cents per kilowatt hour for electricity. Now that is roughly twice the level of all countries in the table on page 10.

But this disadvantage is largely a self-imposed disadvantage resulting from Government ownership. One informed Bahamian businessman believes that a well managed private power producer in the Bahamas could produce at 9-10 cents per kilowatt hour. This means that the cost to Bahamians of an inefficient BEC is almost 50 cents on every dollar spent on electricity.

**International Industrial Electricity Prices**

**(Cents per Kilowatt hour)**

| | |
|---|---|
| Bahamas | 16-18 |
| Ireland | 8.42 |
| UK | 7.55 |
| France | 7.16 |
| Netherlands | 8.02 |
| U.S. | 8.44 |
| Germany | 8.83 |
| Spain | 8.95 |

Source: National Utility Services Ltd. Int'l Electricity Price Survey, 1999 & A Bahamian Power Specialist

The international lending agencies for years have recommended the privatization of the state owned utilities. The rationale most often given for this is that it will provide a cash inflow to the Bahamian Government that can be redeployed in debt reduction, increased foreign exchange reserves, etc.

What is not mentioned is that such privatization, if done properly, can dramatically reduce the cost of doing business in the Bahamas. This is an essential ingredient to promote investment, sustain economic growth and avoid more drastic measures such as the devaluation of the currency.

### Other Important Observations.

1. Another hotel operator with an international presence described his Bahamian experience succinctly: "His Nassau hotel was his biggest investment and both the highest operating costs and the lowest rate of return."

2. Sun International‘s Atlantis was an investment in the mega-resort sector of the tourism market, the first for the Bahamas. This investment alone maintained the public profile of the Bahamas in international tourism. The company brought new concepts, resources and managerial skills.

Yet…Atlantis faces the same cost pressures as the above cited "traditional" hotels. For instance, if you calculate the Return on Investment (Gross Operating Profit as a Percent of Investment) for the Atlantis casino and eleven in Las Vegas in the first year of their respective operations, one finds that the ROI for Atlantis in its first year of operation was 10.0% versus 17.1% for the Las Vegas eleven. The average for the top six Las Vegas casinos was 26.4%.

### Conclusions.

**When Bahamians at all levels consider what the country should do in the present crisis, they must confront squarely several uncomfortable truths:**

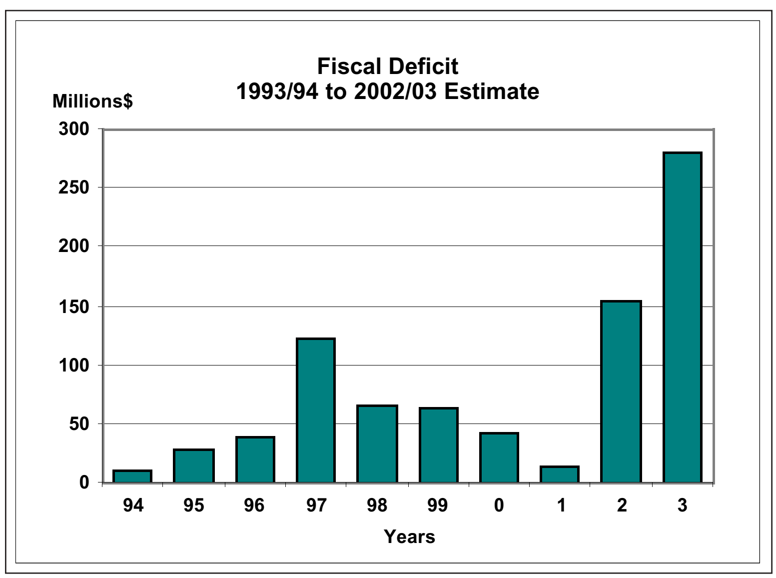
1. **The country is a high cost country and this puts it at a competitive disadvantage in all businesses including tourism, the mainstay of its prosperity over the past 50 years.**

2. **The resultant low rate of return causes new investment dollars to go elsewhere.**

3. **Unfortunately, foreign direct investment is a key ingredient for economic growth and the Bahamas must attract it to prosper.**

## Macro Economic Stability and Devaluation

Relative to other countries the Bahamas has had until recently a good record of macro economic stability. Its high operating costs have not been fueled by the kind of fiscal imbalances and inflation that have typified the



major countries of Latin America. In the case of Mexico, for instance, the value of the U. S. Dollar in pesos rose from 13 pesos in 1975 to an equivalent 10,040 pesos per dollar in 2002 as a direct result of its fiscal failures and inflation (See the first page of Appendix II, The Mexico Example).

The problem in the Bahamas is that the fiscal deficits rose dramatically during the 1997 and 2002 elections; the Bahamas does have a significant level of Bahamian Dollar debt; and the situation now threatens to spin out of control.

- The deficit in fiscal 2001 was $14 million and a zero balance was budgeted for fiscal 2002. In fact it reached $154 million.
- The budget for 2003 called for a deficit of $147 million. However, it is expected to increase to as much as $280 million, over one-fourth of budgeted expenditures.

**Countries that lose macro economic stability become "bankrupt"…they are forced to renegotiate their debt and devalue their currency. Devaluation is a de facto tax on local currency saving and income, a forced reduction in the standard of living. Unfortunately that is how the real world works. The Bahamas may avoid such a disaster if it takes decisive and difficult steps now.**

## Expansionary Fiscal Contraction

In one sense the Bahamas is in the same position as Ireland in 1987…namely it faces a fiscal crisis. The Irish Parliament was led by a party coalition that included the Labour Party. It fell in January 1987 and was replaced by a new coalition without Labour. Many of the country's development measures were well in place; free secondary education introduced in 1967 was producing a good flow of skilled workers; and the Industrial Development Authority had been successful in inducing foreign companies to locate in the Irish Republic.

The problem was that the country beginning in the 1970s became hooked on annual increases in Government employment financed by higher taxes and debt. This economic policy formula produced stagnation and a financial crisis. In 1986 the government debt to GDP ratio hit 129 percent. This compares to 39 percent for the Bahamas in May 2002.

> "The choice was stark: either we [Ireland] reasserted control over our financial affairs or these would pass out of our control, and perhaps into the hands of the IMF. If that were to happen, Ireland would lose a large measure of her national economic sovereignty."[4]

Widespread political support got behind a four-year development strategy that called for massive cuts in spending and more selective cuts in taxes. This support included a commitment by the major opposition parties including Labour. The deficit fell, business confidence improved, investment and GDP grew and a fiscal surplus was created. This was described as an "expansionary fiscal contraction"; and The Economist magazine in the 1990s described Ireland as the "Emerald Tiger" rather than as previously, a country "In Hock and Out of Work". (See Appendix I, The Irish Example.)

> The reality is that countries like Ireland and the Bahamas are "narrowly limited in their ability to inflate and create credit; if they indulge in expansion rates greater than those of their neighbors and trade partners, they soon face payment difficulties as imports increase and exports decline. They then have to reduce expansion rates and fall in line with their neighbors and partners."[5]

**The Bahamas must find the leadership skills and the political will to confront its cost and fiscal problems in order to avoid the far more drastic remedy…Devaluation…the dreaded "D" word.**

Chapter Two

# The Bahamas' Institutional Setting

## Sustained Economic Growth

For the past 55-years the world has been struggling with the problem of achieving sustained economic growth. In the less developed part of the world it has truly been the elusive goal.

In the search for growth several distinct "models" have been tried.

1. **Big Investments.** In the immediate post-World War II period the Stalinist economic programs of the 1930s were the model since Russia took big steps during the Great Depression in building heavy industry and during World War II in producing guns, tanks and planes in great quantities. The top-down, centralized command economy favoring steel mills, dams, etc., became the model. However, it did not work since the big investments did not trigger domestic saving, investment and sustained growth.
2. **Import Substitution.** The United Nations' Economic Commission for Latin America promoted import substitution at all costs as an alternative. This meant expanding one's industrial production to become self-sufficient in manufactured goods. The premise was that the terms of international trade worked inexorably against the commodity exporter; and the high manufacturing costs of small-scale production would prove bearable. In fact, government protection, preferences and subsidies created great opportunities for growth sapping "cronyism and corruption".[6] This is the experience of Latin America.
3. **Stabilization Funding.** It appeared that inflation, fiscal instability and devaluation were the critical problems and the International Monetary Fund (IMF) stepped in and made short-term stabilization loans. This funding, however, allowed countries to defer taking difficult measures and, in effect, such lending created a welfare dependency syndrome.

   "Out of 124 countries that borrowed from the IMF between 1949 and 1999, nearly 70 per cent borrowed in at least three-quarters of all the years after the year of their first loan…Dependence can stretch on for decades: 56 percent of those 124 countries stayed on the IMF dole for 20 or more years…" and in the case of Russia massive loans "instead of speeding up reforms…slowed them."[7]
4. **Exports and Freer Markets.** Because of the failure of these three models some underdeveloped countries and then the international lending institutions, supported by extensive research, embraced a free trade and free markets model. This was most dramatic in the case of China that reversed its Communist policies in agriculture, private enterprise and trade.

However, the transition to a freer economy with sustained economic growth is extremely difficult as witnessed by the crises in countries with economic development models as diverse as Korea, Japan, Indonesia, Malaysia, Argentina, Mexico and Brazil. Objective analysis of this experience has led those searching for the formula for growth, or for the incentives that will promote growth, to talk about "Second Generation Reforms" and "The Institutional Setting" (See Appendix III, The "Right" Answer.).

## The Institutional Setting

The Bahamian Crisis appears as a mixture of high costs and a fiscal imbalance. But the story is more complex than that; and this causes us to start with the work of Adam Smith.

Adam Smith, as described in the "Free Trade History" section of Chapter Three, worked and wrote in the last half of the 18th century. He described the Industrial Revolution as a "spontaneous order" that guided productive activity within a set of social conventions and norms and a work ethic. In Game Theory terms economic transactions within the institutional setting of a free market society produce a positive-sum outcome…they increase the real wealth. The Game Theory analogy is that players sit down at a table for a game of poker, they play and the result is that the total value of the chips held at the end of the game increases producing a positive-sum outcome. But the world of Adam Smith changed…especially after 1913. The government's role in what could or should happen in a society greatly expanded as did the volume and variety of economic transactions. And…the nature and roles of the participants in economic transactions changed and the transactions themselves became ever-more impersonalized.

James M. Buchanan[iii] in the 1970s looked at the link between social values and economic organization.

> "For Buchanan, self-interest and the willingness to work hard, set in a framework that protects individual property rights, generate the beneficial outcomes that define a market order…
>
> "The growth of government has become a significant feature of the 20th century. Government intervention in the marketplace has weakened the underpinnings of the market economy through legislation and regulation that alter the institutional setting of market activity as well as the incentives facing individuals. These changes reduce economic liberty and restrict economic growth as individuals begin to invest in wealth transfer activities instead of wealth creation activities…
>
> **"The emergence of the modern welfare state and the concomitant expansion of government in both economic and social spheres have increased both the opportunity for, and the relative pay-off of income redistribution activities. Rather than providing inputs into productive market activities, individuals may now invest in rent seeking, rent protection, and rent avoidance (See Appendix IV, Definition of Rent)…[These strategies are] likely to shift [economic life] from the positive-sum game of mutually beneficial exchange to, at best, a zero-sum game that imposes forced exchanges on others."**[8]

Buchanan concluded that the social and legal framework of a market society had diminished in the modern world. Within modern democracies two opposing forces are generated:

> "One to sustain a free, liberal order based on the market (the rule of law); and one to establish a personal regime for personal gains (the discretionary rule of men). If the presumption is that the latter force will dominate the former force in a democracy, the argument above implies that we will see an absolute decline in fundamental ethics within society." Furthermore, "the emergence of the modern welfare state, coupled with the development of highly industrialized societies, generates a 'spontaneous disorder' rather than a 'spontaneous order'."

Subsequent to the work of James Buchanan others have focused attention on the firm and "brand names" as the elements in a modern society that may have the capacity to shape individual values in a way that supports economic activity and produces a positive-sum outcome.

- **In a world that encourages rent-seeking the firm alone can assign and enforce rewards and punishments to eliminate free riding, minimize opportunistic behaviour and maximize the economic outcome.**
- **Corporate and product "brand names", in fact, can create images with positive economic value although words such as "McDonalds" and "Coca Cola" conjure up negative images for many. If the consumer responds favourably to a product or service, "goodwill" is created for that "brand name" and the value of the enterprise increases. This also creates an incentive for the firm "to recruit its members carefully and screen out undesirable and unreliable employees. This means that the [firm] is likely to recruit its members based upon the same ethical qualities underpinning traditional markets."**

The other development that counters the "pessimism" of James Buchanan is the open embrace of free-market ideas by the FTAA. The principles evident in the Declaration have evolved from a half-century of trial and error in framing economic policy.

## A Centrally Managed Economy

Unfortunately Bahamians in general embrace neither the ideals that underpin traditional markets nor those includ-

[iii] James M. Buchanan won the 1986 Nobel Prize in Economic Science and is the Advisory General Director of the James M. Buchanan Center for Political Economy at George Mason University.

ed in the FTAA Declaration. The problem is that the institutional setting of the Bahamas is one of a small isolated, inward looking country rather an outward looking country ready to succeed in a more integrated world.

In fact, the Bahamas is an economic policy paradox.

- On the one hand it benefits from free trade. It freely imports products from the lowest cost producers around the world; and it competes in the global market for tourist and financial services.
- Nevertheless, it has a top-down, highly regulated, centrally managed economy with significant business and labour sectors protected from competition.

James Gwartney[iv] co-authored the first report (1997) on the *Economic Freedom of the World*[9] that contained "thumbnail" descriptions of each country in the study. The full text of his description of the Bahamas follows:

> "In 1995 the Bahamas ranked 35th among the 115 countries in our study. At first glance this economy appears to be quite free. Government expenditures and taxes are relatively low. There is no income tax. Direct income transfers and subsidies are small and most businesses are privately owned.
>
> "Probing beneath the surface, however, one discovers that this is a highly regulated, central-managed economy. The business sector is characterized by a complex and contradictory set of entry restraints, targeted tax breaks, and indirect subsidies. A bureaucratic licensing system restrains entry into many business activities and exerts political control over the economy. While foreigners are virtually excluded from the wholesale and retail business sector, they qualify for attractive tax breaks in other areas (export manufacturing and light industry, for example). When they meet certain criteria, new hotels are exempted from property taxes for up to ten years and granted other tax concessions for even longer periods of time. The government also uses both regulatory power and tax concessions to promote the offshore banking industry.
>
> "Regulations abound in other areas. A residency and work permit system controls and taxes foreigners. Price controls are imposed on petroleum and food products. Domestic citizens are not allowed to maintain foreign currency bank accounts. Foreign exchange controls limit the movement of capital. Tariff rates vary widely among product categories, distorting relative prices and reducing gains from international trade.
>
> "During the 1980s, the employment of state-operated enterprises expanded and the government became a major hotel owner and operator. A reform government elected in August 1992 and re-elected in 1997 has privatized the largest part of these holdings.
>
> "Nevertheless, state enterprises and excessive regulations continue to exert a major impact on the economy. While the new government has speeded the investment process, regulations limiting the entry and development of business remain on the books. Residents dealing with the government telephone monopoly often confront lengthy waiting periods. The government-operated airline has 635 employees, while operating only 9 planes. [At last report Bahamasair had 688 employees and 7 planes.] Hopefully, a decade of economic stagnation is ending and this country will move toward deregulation and economic liberalism in the near future."

## Income Redistribution and Stagnation

James Gwartney's analysis was based on 1995 data before it was clear that economic stagnation did end; but –

- The country prospered and yet moved toward greater regulation rather than deregulation.
- It subsequently encountered a recession in both tourism and offshore financial services.
- Then in 2002 the winning political party campaigned with the message that it would reorder the relationship between Bahamians and foreigners.
- Now the current Government is challenged by the terms of its membership in FTAA.

Bahamians may feel that external forces are pummeling them; and politicians can engage in anti-foreign rhetoric. Nevertheless, in formulating a policy response to their 1994 FTAA Declaration, Bahamians should be candid.

[iv] James Gwartney is a Professor of Economics at the DeVoe Moore Centre for the Study of Critical Issues in Economic Policy, Florida State University.

Its centrally managed system of government is the result of the following:

- The country is extremely small and easy to subject to political control.
- The country has had a poor island economy that has been marginal to its immediate neighbors and the world.
- The country has a culture of slavery, colonialism and roots in African cultures that were far less developed than those of Europe and Asia.
- The country since 1967 has been a parliamentary democracy without the substantive checks and balances of an active constitution or an independent judicial system.

**Given this background it is no surprise that for the Bahamas the redressing of present and past political and economic inequities and the redistribution of income dominate policy decision-making.**
**These policy objectives –**

- **Increase the pay-offs for income redistribution activities such as rent-taking and rent-seeking,**
- **Have made the Bahamas a high cost country in the global economy thus limiting its development options and threatening its major industry and**
- **Produce economic stagnation.**

**The Bahamas is an example of the negative consequences of the modern welfare state as described by James Buchanan.**

- **Bahamians are responding rationally to a system that is, in effect, a democratically elected autocracy. The politician gets votes by rewarding party loyalty with lifetime government jobs; and an enfeebled justice system produces rent taking opportunities for the party faithful.**
- **This is a logical consequence of a mix of a modern democracy and a middle class that does not yet have the numbers and commitment to demand the ethical and legal framework associated with individual freedom, the protection of private property and free markets.**

**The Bahamas' "Institutional Setting" has been a major factor in creating a high cost operating environment that is not conducive to economic growth.**

William Easterly, a former Senior Research Advisor at the World Bank, wrote in *The Elusive Quest for Growth* –

> "Divided societies' governments face incentives to redistribute existing income. In more cohesive societies, governments face incentives to promote development. The fundamental difference between redistributionist and developmentalist governments is social polarization. Societies divided into factions fight over division of spoils; societies unified by a common culture and a strong middle class create a consensus for growth—growth that includes the poor."[10]

Nancy Birdsall who worked with the Inter American Development Bank[v] has these sobering comments on the traditional 'Welfare State" approach in less developed countries:

> "The most avoidable and thus the most disappointing source of inequality are policies that hamper economic growth and fuel inflation—the most devastating outcome of all for the poor. Most populist programs designed to attract the political support of the working class hurt workers in the long run.
>
> •"When financed by unsustainable fiscal programs, they bring the inflation and high interest rates that exacerbate inequality…
> •"Price controls, usually imposed on the products most consumed by the poor, often lead to their disappearance from stores…
> •"The imposition of a minimum wage temporarily benefits those who have formal jobs but makes it harder for the unemployed to find work…
> • "Regulatory privileges, trade protection, and special access to cheap credit and foreign exchange—all bad economic policies—will inevitably increase the profits of a wealthy minority."[11]

## Rule of Law

It is important to look at specific problem areas. The most pressing is the increasing level of lawlessness.

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[v] Nancy Birdsall is a former Executive Vice President of the Inter American Development Bank and is now a Senior Associate and Director of the Carnegie Endowment for International Peace and a Senior Fellow at the Brookings Institute.

The Rule of Law is a universally acknowledged critical element in the "formula" for sustained economic growth; it is the critical part of the institutional setting. The absence of the Rule of Law raises the cost of doing business; it enriches the politically privileged and impoverishes the disadvantaged.

You can see this most clearly in an extreme case such as Afghanistan where "warlord-ism" destroyed the economy. At the other extreme there is Great Britain in the 18th and 19th centuries. According to Thomas Sowell, "the evolution of the Rule of Law in the British Isles not only helped promote the internal development of Britain itself, it helped attract to Britain…much of the commerce of Europe."[12]

Despite its roots in the British judicial system, two centuries of Bahamian history, the many outstanding lawyers and a pervasive and prosperous Christianity, the Rule of Law does not carry the day in the Bahamas. Attorney General Alfred Sears is reported as "echoing the conclusion of the crime commission" with comments on "the pervasive culture of dishonesty that exists in the Bahamas."[13]

Pilferage of merchandise in super markets runs 5 to 7 times the U. S. level. The hotel and tourism retail sectors are fraught with examples of employee theft that constitutes one of the factors making the Bahamas a high cost place to do business.

And one cannot in numbers describe the full impact of the slow and "unjust" operation of the justice system on business. However, there is anecdotal evidence and, in fact, there are legendary cases. One such case is described in "Stolen Property", Appendix V. It is a truly unbelievable story of "condoned thievery", the unenforceability of commercial contracts and the absence of the Rule of Law.

And then there is street crime. Paul Farquharson, the Police Commissioner, has stated publicly[14] that –

- The judicial system is "Cocked-up";
- It has been evident for decades; and
- No one is doing anything about it.

He pointed out that there are "laws on the books that need to be applied and we must have swift justice." In 2002 4,455 criminal cases were received at the prosecutions office, 3,000 were addressed, 9,196 cases are pending before the courts and 14,000 warrants are outstanding. He contends that the "criminal felt that if he went to court and pleaded 'not guilty', the chances of his case eventually being heard was almost nil."

**The point is that the failure of the Rule of Law and the associated crime are dramatically "destroying" the good life and the economic prospects of the Bahamas; and talking about it is no substitute for doing something about it.**

## People

For businessmen…unfortunately…the Bahamian people appear at times to be the country's biggest liability rather than its biggest asset. The newspapers tell a story of embarrassingly low academic test scores and employers complain about a basic deficiency in the "three Rs", poor work attitudes and theft. The public educational system is a failure as measured by the academic test scores of its school leavers. (See Appendix VI, Literacy in the Workforce) And there is the constant public pressure to hire Bahamians and complaints about work permits that are a kind of human "tariff wall".

While majority rule brought political equality in 1967, it has been accompanied by an underinvestment in and a failure of public education. The country has an inadequate supply of skilled people at a time when the knowledge level required for all jobs has increased. (Refer to Appendix I, The Irish Example.)

**In the long run the key to the country's future is inevitably tied to its people.**

In this regard it is important to look at two judgments:

**A population growth and natural resource economist.** "The main fuel to speed our progress is our stock of knowledge; the brake is our lack of imagination. The ultimate resource is people—skilled, spirited, and hopeful people who will exert their will and imaginations for their own benefit [while exercising the basic morals of property and honesty], and inevitably they will benefit not only themselves but the rest of us as well."[15] (Refer to "The Ultimate Resource", Appendix VII.)

**An economic development specialist.** "Probably the best single vaccine against the worst effects of globalization-provoked inequality is education; the more there is of it, the lower the inequality of real total wealth in the long run."[16]

**The effective investment in people, the “Ultimate Resource”, is a long-term commitment by its very nature; up until now Bahamian politicians have concentrated periodically on those programs that promote immediate electoral benefits such as school construction and teachers’ salaries. Relatively little attention is addressed to student and teacher performance; this failure will lead to significant social unrest in the future.**

## Labour

Organized labour in the Bahamas has been concentrated mainly in the State Corporations and Departments. Here union-management relations are a “political tango” with the Government granting benefits in ways to get electoral support and union leaders earning union support with disruptive and aggressive actions outside the terms and procedures of their labour contracts.

There is political support to move the Bahamas toward the Western European model of trade unionism without recognizing the economic consequences of that model. In Europe compulsory unionism dominates most countries. “In Germany and France, for example, union contracts cover 95 percent of the workers, while in Italy coverage is 92 percent. By comparison, only 18 percent of the U.S. labor force works under union contracts.”[17]

The deficiencies of European trade unionism have been extensively documented. Two decades of unusually high unemployment have brought Europe’s web of labor regulations under considerable scrutiny.

- In the 1960s and 1970s unemployment rates were below U. S. rates but by 1990 the rate was twice the U. S. rate. The picture of long-term joblessness is the same. “As of 1999, 47.5 percent of the unemployed in the European Union had been out of work for a year or more, compared with only 6.8 percent in the United States…
- “Although results are mixed, there is evidence that union strength and dismissal restrictions are associated with poor overall job creation.
- “Also, there is a clear connection between dismissal restrictions and the length of unemployment. Although the purpose of such laws is to prevent workers from being fired, they also make it harder for workers that are let go to be rehired later.”[18]

Despite testimony warning against a national labour contract by the Nassau Institute, the Government passed The Employment Act of 2001 in December of that year. In the middle of a recession the Government raised labour costs. This action reduced the workweek and as predicted the take-home pay of workers. The economic law of supply and demand prevailed.

**Furthermore, the policy objective of mandatory trade unions for the private sector, including managerial unions, remains in place.**

## Business Environment

Government intervention and control are pervasive and costly. The licensing and permit processes control all new and every significant change in business activity: and this control is by a Government bureaucracy that is slow, inefficient and unmindful of the needs of business and the economic impact of its slowness and inefficiency. In addition, poor law enforcement raises the cost of crime and security…the cost of doing business.

For instance, the Government controls the number and location of competitors and therefore the level of competition. At the same time the Consumer Protection Department sets maximum prices at retail on a broad array of “essentials”. No new “essential” product can leave a warehouse without a retail price approved by Government. Price controls overlook the effectiveness of market competition and are anachronisms that have long ago been abandoned elsewhere. One can make a persuasive case that the consumer has benefited more in lower prices and better service from increased competition that has occurred than from the work of the price control bureaucracy.

## The Newest Regulation

In addition to the labour bills, there has been a steady stream of other legislation. The most pervasive and damaging has been the 11 financial bills of Christmas 2000. They constitute a massive increase in government regulation of the commercial and trust banks and also the nonbank providers of financial services. The latter include lawyers, real estate agents, etc.

The OECD wanted to eliminate the low tax competition presented by offshore financial centers; while the United States was pursuing drug traffickers and terrorists. The net effect has been to dramatically raise the fixed costs of doing such business in the Bahamas and to eliminate or reduce the advantages in doing it here in the first place.

This unfortunate experience causes everyone to resist any change…and that is understandable. It further raises the importance of business participation in framing legislation and rules.

## Conclusion

The present crisis in the Bahamas…a potential fiscal crisis, a recession in its key industries and the need to respond to the FTAA…requires action; the policy crisis this creates can be the opportunity to move a proud nation and people forward on a national recovery plan.

A recovery plan, whether it involves continued FTAA participation or not, requires a massive change in the county's political thinking and in its administrative capabilities. The change is so massive that just thinking about it can produce a sense of helplessness and despair; this sense can only be dispelled by ordering ones priorities and taking concrete steps daily to reach those goals.

In effecting a National Development Plan the leaders of Bahamian society should examine –

1. The spirit that motivated the Jews in Germany on their emancipation in the 19th century. They started as an entirely isolated people…destitute with a few privileged rich and no middle class. They absorbed German Kultur (culture) and Bildung (self-improvement through education). "At the beginning of the century, most German Jews had been paupers. In Prussia, where the majority lived, 70 percent had led 'marginal, insecure' lives; many were wandering peddlers and beggars. By 1870, that figure had dropped to 5 percent…60 percent…were now of 'secure middle-class' status. Theirs was perhaps the fastest and greatest leap any minority experienced in modern European history."[19]
2. The leadership skills and techniques of Mayor Rudolph Giuliani that so dramatically changed a seemingly unmanageable New York City for the better and helped that city respond intelligently and quickly to the first battle of a new war.[20] "Leadership is a privilege, but it carries responsibilities—from imposing a structure suitable to an organization's purpose, to forming a team of people who bring out the best in each other, to taking the right, unexpected risks. A leader must develop strong beliefs, and articulate and act on those beliefs, and be accountable for the results."
3. The wave of volunteerism and civic responsibility that has dramatically transformed many communities, cities and neighborhoods as business, civic, church, union, and government leaders have worked unselfishly and collaboratively with a common resolve toward a more prosperous and civil society.

A National Development Plan requires spirit, leadership and common resolve.

## Chapter Three

# Free Trade & Reality

In examining the question of membership in FTAA the appropriate place to start is with several basic economic concepts even if this approach sounds unnecessarily "academic".

A **"Free Market" Transaction** is one where two individuals (or groups, or a combination of an individual and a group) agree to exchange a good or service at a price. They act in their own self-interest, maximizing their net gain while evaluating their alternatives without interference or coercion by others. Both parties gain from the transaction. In terms of Game Theory this is a "win-win" outcome in a two-person exchange; and it contrasts with the optimal outcome for one partner where there are no ethical constraints or institutional sanctions…namely "I take what you have in exchange for nothing", a "win-lose" or "zero-sum" outcome.

A **"Free Market"** is a place where many similar transactions occur. There is an interaction between sellers and buyers of a good or service so that at a moment the total amounts supplied and demanded are equal at a price.

In addition, there is an interaction within and between markets. Many have used the pencil to illustrate this point. They hold up an ordinary pencil and then talk about the market for pencils and the separate markets for wood, graphite, paint, rubber and tin. In the production of a pencil, these separate markets integrate countless specific decisions. This complex market integration process, for instance, ends with a pencil that costs 25 cents at Wongs on Mackey Street. It is this efficient decentralized market coordination of free markets that central planners cannot duplicate and displace.

Furthermore, "market-based economies have demonstrated powerful capabilities to allow their average members to obtain more goods than before given the same amount of resources."[21] This market-based economic order particularly characterized the industrial revolution of the 18th and 19th centuries.

**"Free Trade"** is the term normally used for cross border international transactions that are unhindered by fiscal barriers and restraints and unaided by bounties or subsidies. These have a powerful economic potential that will be examined first in theory and then in practice.

The theory that explains these gains is the economic law of **Comparative Advantage** that is illustrated with a simple two-country example in Appendix VIII. Even though one country may be able to produce everything more efficiently than another, it is still in their interests for each country to specialize in production; and the result is a greater total production than before specialization. In Game Theory such an outcome is described as a "positive sum".

This gain in real life results in economic growth, lower consumer prices, increased profits for the successful producers and the demise of those producers that existed solely as a result of Government protection.

These definitions would appear to suggest that Government has no role in free markets. The truth of the matter is that free markets cannot function well without an institutional setting that minimizes market transaction costs. These include –

1. Freedom from pillage and plunder by foreigners and nationals alike
2. Protection of property from damage by war or civil disobedience
3. Legally valid and easily transferable titles to property
4. Enforceable contracts
5. A free flow of information

"To reach their full potential…markets need help from the government. Markets and governments have an uneasy relationship. Markets coordinate the economy better than any centralized alternative; governments sometimes distort and even destroy markets. But help from the government is essential if the economy is to reach its full potential."[22]

## Free Trade History

Adam Smith made the first "ground breaking theoretical case for free trade" in 1776. In examining economic growth he saw three things:

1. Output greatly increased with the rational application of new ideas and the specialization of labour.
2. Governments imposed restraints on imports and encouraged exports with bounties, treaties and colonies. These measures blocked change but they did satisfy some national objectives and protected specific private interests.
3. The benefits of trade free of those restraints accrue to specific businesses but more importantly to consumers in the form of lower prices. "In every country it always is and must be the interest of the great body of the people to buy whatever they want from those who sell it cheapest."[23]

Adam Smith demonstrated the advantages of free trade to society as a whole; but he was skeptical. He doubted that it could ever "carry the day" because of "the prejudices of the public, but what is much more unconquerable, the private interest of many individuals who irresistibly oppose it."[24]

This free trade conflict between national economic welfare and political/private interests persists everywhere… including the Bahamas.

### Growth in International Trade

| Period | Per Cent Per Year |
|---|---|
| 1780-1840 | 2.50 |
| 1840-1870 | 4.67 |
| 1870-1913 | 9.77 |

Source: Philippe Legrain, Open World: The Truth about Globalization, Abacus, 2002, page 95.

Despite Smith's skepticism the world experienced two great bursts in international trade. The first came in the century after Adam Smith (see table); and was propelled by electricity, railways, steamships and the telegraph. As an example these allowed the exchange of Argentine wheat and beef for British manufactured goods. Up until then Argentina, one of the six richest agricultural areas of the world, was at a comparative disadvantage relative to British agriculture. Literally, it was too far away. But…this changed. Within a lifetime Argentina became one of the richest countries in the world and with Canada, Australia, New Zealand and the U.S. became part of a new global order.

But dislocation and political conflict accompanied that growth. Within Great Britain free trade pitted the landed gentry against the exporters. The landed gentry prospered behind regulations and tariffs that kept cheap foreign grain out. A pair of textile manufacturers "organized the Manchester-based urban interests against the landed elite. The seven-year campaign of the Anti-Corn Law League achieved victory in 1846 with the repeal of the Corn Laws and the elimination of all duties on imported grain."[25]

This "free trade induced" era of prosperity ended in 1913 with World War I and its aftermath. The competitive nationalism that led to the war; the centralized command economies during the war; and the Great Depression after it produced political movements hostile to political freedom and free trade. These included Communism in Russia, National Socialism in Germany, Fascism in Italy, Fabian socialism in England and Keynesianism in both England and the U.S.A. They produced higher tariffs everywhere.

The brief recovery in international trade of the early 1920s was more than wiped out with the recession. The US economy declined 30 per cent and imports fell 70 per cent between 1929 and 1932. Between 1929 and 1938 the volume of trade for the U. S. was down 20 per cent, for the UK 30 per cent and France and Germany 38 percent. It was not until the early 1970s that international trade recovered to 1913 levels.

U.S. tariff reductions actually started before World War II in a series of bilateral trade agreements and continued after the war with the General Agreement on Tariffs and Trade (GATT) that covered 23 countries and 80 percent of world trade. Also there was the movement to free exchange rates and to eliminate multiple rates and capital controls. The initial beneficiaries of these initiatives were the United States, Western Europe and then the Pacific Rim countries of Japan, Taiwan, Hong Kong and Singapore.

Even bigger changes came in the 1990s with the collapse of Communism and the significant enlargement of the Global marketplace.

## The Perfect World

In the perfect world every country would be led by a Prime Minister who would be wise enough to see that free trade benefits people as a whole…it produces growth and lower prices to the consumer. After a brief discussion with the other PMs in his part of the world, he and they would each unilaterally eliminate tariffs, quotas and restrictive regulations. Without wearisome and costly negotiations, the "doctrine of comparative advantage" would take over. "I grow bananas" and "You catch conch" would become a reality. The PMs would help the adjustment in the short run by collecting a tax from the now more profitable banana growers or conch catchers and give temporary readjustment grants to those less fortunate who would be displaced. The consumers and tax paying citizens collectively would be the big winners.

## The U. S. Paradox

Unfortunately in some respects the world has not changed much since the days of Adam Smith; and it helps to be clear about how free trade works…especially in the U.S., a good but admittedly imperfect country.

In 1950 the free world faced the Communist Bloc, and one could not have imagined the position of the U. S. a half-century later. Within 50 years the U. S. became –

- The world's military and economic super-power by a big margin,
- The world's great super market with shoes, clothing, appliances and cars from Asia often selling with price tags so low as to defy simple logic,
- The home for wealthy Latinos…producing a booming housing market in South Florida…and the destination of choice for the less fortunate…those often traveling in anything that floats,
- The provider of golden opportunities for those with great talent and ambition like Asian engineers in Silicone Valley, Asian mathematicians in every university and Russian ice skaters in the country's skating clubs, and
- The "victim" of "de-industrialization" as the new economy spawned by the computer revolution and free trade drastically changed its factory towns.

However, the United States exceeded the fondest hopes of Adam Smith. The U.S. is "rightfully considered among the most open economies on earth" and certainly one of the most prosperous.

Nevertheless, free trade has not completely carried the day. Big pockets of protectionism remain that both block the exports of many countries to the U. S. and are an economic drag…although not an overwhelming one.

Please note the following:

- "Nowhere is there a larger gap between the U.S. government's free-trade rhetoric and its protectionist practices than in the sugar program. Through preferential loan agreements and tariff-rate quotas, the U.S. government thwarts price competition to maintain an artificially high domestic price for sugar—a price that can be twice the world market price or higher."[26] The program benefits sugar cane growers in Florida and Louisiana, sugar beet growers in the West and certain foreign countries that have a U.S. sugar quota. The program costs the consumer $1.9 billion a year in higher consumer prices for food.
- In March 2002 the Bush administration took measures to protect U.S. steel producers against steel imports. "By any relevant economic measure, the costs of protection will far exceed the benefits, and any benefits accruing to steel firms from that protection will be fleeting."[27]
- There are still substantial restrictions on food, textiles and apparel imports despite assumptions to the contrary and…
- There are export subsidies. These have been contested under the rules of the World Trade Organization by the European Union and in August 2002 the EU was awarded damages of up to $4 billion.

In fact, measures taken by the Bush administration would suggest that protectionism is on a comeback. It is hard to believe at this time that the free trade movement will be reversed as it was after 1913 since its benefits are clear.

As in all free trade disputes, the problem…especially in free democracies…is that the beneficiaries of trade restrictions are small in number while the costs of providing those benefits are spread across the economy to the far more numerous and less well-organized consumers and taxpayers.

## Chapter Four

# From GATT to GATS

## GATT & WTO

In 1944 the United Nations established the World Bank (the International Bank for Reconstruction and Development) and the International Monetary Fund in its post World War II recovery effort. The third organization was the General Agreement of Tariffs and Trade (GATT) that created the process of trade liberalization.

GATT originally included 23 countries that did 80% of world trade; and it established the principles of "most favored nation" and "national treatment". In the initial round the U.S. reduced its overall duty rate from 40% to 20%. The process was slow and over 50 years involved eight rounds of negotiations.

GATT was succeeded on January 1, 1995 by the World Trade Organization (WTO) that describes itself as a rules-based, member-driven organization with all decisions made by the member governments and with rules that are the outcome of negotiations among members. It is a trade liberalization organization and not a common market embracing a common currency and a customs union as is the case with the European Union.

Brink Lindsey, a senior fellow at the Cato Institute in Washington, contends that the dramatic reductions in trade barriers over the past two decades have less to do with the GATT/WTO negotiating process and more to do with "the realization that protectionism was causing economic stagnation."[28] He cites the "bold moves" made by "Australia, New Zealand, Argentina, Bolivia, Peru, Chile, the Philippines, Thailand, Indonesia and India." The other big event was the abandonment of Communism by the entire Eastern Bloc except for Cuba and North Korea.

## Caricom

The Caribbean Community (CARICOM) was established in July 1973 with the Bahamas as one of 15 members. CARICOM in 1991 agreed to move beyond the limits of the original agreement by adopting a series of protocols that constituted the CARICOM Single Market and Economy (CSME). Protocol 1 eliminated the distinction between the Community and the Common Market. While the Bahamas was originally a "Member" of the Community, it is now identified as an "Associate Member" of CSME.[29]

CSME is diverse with members ranging in size from Montserrat with a population of 5,000 to Haiti with 7.2 million and with real annual per capita GDP (stated in 1999 US dollars) ranging from $621 for Haiti to $11,214 for the Bahamas.

Its objective is to establish a single market and economy that would involve "the free movement of goods, services, capital and people across the region." With regard to people it is the only integration scheme outside the European Union to call for the free movement of people. CSME may be considered as a work in progress. Since 1991 it has made "some progress in formulating and implementing the new rules and regulations described in the Protocols."[30] Perhaps its biggest success has been in its negotiations on "market access and financial assistance." with the U. S., Canada, the EU and others under the Generalized System of Preferences.[31]

## NAFTA

The North American Free Trade Agreement between the U.S., Canada and Mexico began on January 1, 1994 and is an "enhanced" free trade area. It has been controversial; and the Mexican experience is used as an argument against Bahamian membership in FTAA. A more balanced view is that it has been a success although a qualified one since income inequality increased. This is related to the institutional and cultural problems that are discussed in "The Mexican Example", Appendix IX.

## GATS

In 1995 the General Agreement on Trade in Services (GATS) was incorporated as a part of the WTO and established a liberalization process for services that is similar the one for merchandise trade that was established 47 years earlier.

Services are defined very broadly and are separated into 12 areas –

Business including professional and computer
Financial
Communication
Health and Social
Construction and related engineering
Tourism and travel
Distribution
Recreational, cultural and sporting
Educational
Transport
Environmental
Other

The Agreement defines four modes of service delivery.

1. **Cross-border supply** is service flows from one country to another (e.g. banking or architectural services transmitted via telecommunications or mail.)
2. **Consumption abroad** is a situation where a service consumer or his/her property moves into another country to obtain the service (e.g. tourism, ship repair or aircraft maintenance.)
3. **Commercial presence** is a situation where a service provider in one country establishes a presence, including ownership or lease of premises, in another country to provide the service (e. g. insurance and hotel chains.)
4. **Presence of natural persons** consists of persons of one country entering the territory of another to supply a service (e.g. accountants, doctors, or teachers).

"GATS is built upon the principle of progressive liberalization. Members are mandated to undertake periodic negotiating rounds to improve the commitments and thus achieve a progressively higher level of liberalization."[32]

GATS is in its infancy and, in fact, is moving on a parallel track to FTAA. Although the Agreement was signed in 1995, negotiations began in January 2000 and are scheduled for completion in January 2005. Progress through October 2002 is described as slow but steady with greater participation by developed rather than under-developed countries.[33]

## Chapter Five

# Tariffs, etc.

Import duties are the principal form of Bahamian taxation and in this regard the country is not greatly different from some other small Caribbean countries. However, it is greatly different from the majority of the other 33 countries in FTAA that have used tariffs as an instrument to keep out selected imports, to protect domestic producers and to achieve economic self-sufficiency. These countries realize the limits of this development model and are moving to freer trade within the negotiating process of FTAA. "Trade without barriers" is the objective of FTAA.

It appears that to continue in the FTAA the Bahamas may have to change its tax system. However, let us evaluate the alternatives.

**Tariffs** are levied at the port of entry against values substantiated by specified documentation. This process is by no means simple; but it is nevertheless the simplest and most controllable taxation alternative…and therefore the most desirable for the Bahamas given the problems that it faces.

For business, the payment of import duties increases the funds invested in inventories; and thus a tariff system is less desirable that a sales tax than is collected when the merchandise is sold at retail.

The FTAA recognizes that very small economies have special problems; and the Agreement both recognizes the broad differences between countries and the objective to "create opportunities for the full participation of the smaller economies." This suggests a predisposition to understand the magnitude of the changes that countries like the Bahamas now face. These include the privatization of the utilities, essential education and judicial reform and increased government efficiency.

**Within the context of a National Development Plan the Taskforce very strongly recommends that the Bahamas –**

1. **Retain a modified tariff system, and**
2. **Defer the adoption of a sales tax to an even greater extent than that contemplated in the Sales Tax option outlined below.**

A **Sales Tax** is paid by consumers at the time of sale and it taxes people on what they spend thus encouraging savings and investment. The costs to collect and administer this system and the potential for tax avoidance would be greater than the present tax system.

Such a system, however, has flexibility. It could be structured with different rates for different categories of goods. Food and medical supplies could be set at zero while services could attract another rate. It would have one clear benefit, a "deferral" of tax collection to the point of sale. The System could be installed in phases so as to allow for the significant organization, staffing and training requirements.

The following are the possible steps in a phased tax-conversion process. This is a "sketch" of a possibility that has not advanced to even the first stage of a documented tax proposal. Despite this limitation, it does suggest how a proposal might look.

1. Classify in 2003 all imports under the present system into four categories: necessities (bread basket items), luxury goods (cars and gasoline, etc.), protective tariffs (chickens, beer, paint, etc.) and standard.
2. Reduce all protective tariffs to the standard rate in 2008.
3. Establish the sales tax rates as follows: Necessities - Zero Percent (0%), Standard - 15% and Luxury - 25%.
4. Treat the issue of duty-free retail or tourism luxury retailing as a special case so that this tourism sector does not inadvertently disappear from the Bahamian tourism experience.
5. Install in 2008 a sales tax on all services of 15%. Services would include but would not be limited to

legal, accounting and medical. Tourism would be included but all present taxes on tourism would be revoked. The exception would be the departure tax and that would change only to conform to rates charged by other major tourist destinations. A thorough valuation of real estate and insurance transactions would also be a part of a Tax Plan.

6. Reduce in 2008 the present taxes on petroleum fuel products to 25% when sold at retail.
7. End the present tariff system and install the sales tax system in 2013.

The tax rates used above imply a reduction in the effective tax rate paid by Bahamians. This would only be feasible with the privatization of the utilities, sustained economic growth and a significant improvement in the efficiency of Government services. Such a tax reduction would be an inducement to the Bahamian public to make the sacrifices called for under the Plan.

## Example Value Added Tax

| | |
|---|---|
| Cost at Port of Entry | $100 |
| VAT Paid to Treasury (100 x .15) = | 15 |
| Cost to Importer/Wholesaler | 115 |
| Wholesale Markup (115 x.25) = | 29 |
| VAT Calculation: | |
| Output Tax (115 + 29) x .15 = | $22 |
| Less: Input Tax | 15 |
| VAT Paid to Treasury | 7 |
| Cost to Retailer | 151 |
| Retailer Markup (151 x .25) = | 38 |
| VAT Calculation: | |
| Output Tax (151 + 38) x .15 = | $28 |
| Less: Input Tax | 22 |
| VAT Paid to Treasury | 6 |
| Cost to Customer | $195 |

Of utmost importance in this whole process would be a detailed analysis of the present tax structure in order to avoid the inadvertent weakening of specific businesses. Those that come to mind are the Duty Free/Luxury Goods shops, hotels and ground transportation.

The third alternative is **Value Added Tax (VAT)**, a tax system widely used in Europe. It is more complicated than both the tariff and sales tax systems since the tax is paid each time that a product or service is sold and resold and not only at the time of import or at final retail sale.

Let us examine the VAT as it would apply in the Bahamas and assume that the cost of the product is $100 at port of entry, the VAT rate is 15 percent and both the wholesaler and retailer have a 25 percent markup. The calculations are shown in the table.

In this case the importer/wholesaler and retailer would be registered with the Government and would make the appropriate payments to the Treasury and all imports are taxed and all exports are not.

This is inherently a more complex system with higher administrative costs for both business and government. This is an unnecessary complication for the Bahamas.

**A Flat Income Tax** is an attractive alternative to a graduated income tax. It has been proposed in the U.S. and was successfully installed in Russia in January 2001 where it has attracted favorable comment. It is very simple income tax system when compared, for instance, to the U.S. Income Tax Code; and if it were adopted in the U.S., it would produce very substantial economic savings to the country.

For the Bahamas, however, it would be a departure from the “low tax-no income tax” policy that has served the country well. To be very specific it would further damage the Bahamas as an offshore refuge for high net worth individuals.

A **Payroll Tax** is the least desirable alternative since it is a tax on a single factor of production.

## Chapter Six

# FTAA and the Bahamas

## The Agreement

The Bahamas and 33 other countries in the Western Hemisphere agreed to create a Free Trade Area of the Americas at the Summit of the Americas meeting in Miami in December 1994.

The motivating force of these 34 countries was to increase trade and investment and to achieve free trade over a period of time. A lengthy implementation period was anticipated to accommodate the needs of some developing country participants.[34]

The objective was to build on the experience of GATT, WTO and NAFTA. The initiative has advanced through a series of meetings, implementation plans and has a second draft of the agreement (dated November 1, 2002). The development of the Agreement is reaching a critical point since the parties were to submit initial "offers on market access" between December 15, 2002 and February 15, 2003.

The agreement is a mammoth document and at this stage even reading it is complicated by the fact that alternative versions of the text are included in the document.

This Agreement deals with the liberalization of merchandise trade, a complicated subject in and of itself. There are sections on tariffs, non-tariff barriers, agriculture, customs procedures, rules of origin, subsidies, anti-dumping, countervailing measures and dispute settlement.

However, the Agreement goes beyond trade to include –

- Investment, services, competition, government procurement and intellectual property and
- Commitments not to relax labour and environmental laws.

## FTAA Objectives

In order to develop specific recommendations it is important first to clarify the exact policy objectives contained in the Agreement and not to get lost in the details. These are contained in five chapters as follows:

1. **Market Access**. Treat the imported goods of any country at least equally to the "most favoured" treatment offered to other countries and commit to specific initial tariff reductions.
2. **Investment**. Treat a foreign investor as favourably as a Bahamian investor or the investor from another country with respect to "the establishment, acquisition, expansion, management, conduct, operation, and disposition of investments."
3. **Services**. Like the General Agreement on Trade in Services (GATS) the definition of services is all inclusive and to make that point clear the text from the prior Chapter is repeated as follows:

    - Cross-border supply is service flows from one country to another (e.g. banking or architectural services transmitted via telecommunications or mail.)
    - Consumption abroad is a situation where a service consumer or his/her property moves into another country to obtain the service (e.g. tourism, ship repair or aircraft maintenance.)
    - Commercial presence is a situation where a service provider in one country establishes a presence, including ownership or lease of premises, in another country to provide the service (e. g. insurance and hotel chains.)
    - Presence of natural persons consists of persons of one country entering the territory of another to supply a service (e.g. accountants, doctors, teachers, etc.).

    The FTAA Agreement anticipates that member countries will progressively open sectors of their economies to competition; but that the Members will "undertake to accord special and differential treatment to smaller economies and less developed countries…with respect to time periods and temporary exceptions."[35]

4. **Competition Policy**. Adopt or maintain measures to outlaw anticompetitive conduct in order to promote economic efficiency and consumer welfare and take appropriate action with respect to such anticompetitive conduct.
5. **Dispute Settlement**. Establish fair, transparent and effective mechanisms for dispute settlement among countries and develop mechanisms to solve private trade controversies.

The purpose of FTAA is clear: promote free trade and create free markets. The redirecting of those who "irresistibly oppose" such measures is left to elected officials: and fortunately for these officials there is no provision for the free movement of people.

For the Government, the PLP and all Bahamians, signing the final Agreement will be a watershed event. This is so because the Agreement's objectives are inconsistent with the premises and assumptions now imbedded in Bahamian law, politics and culture. Changing that "Bahamian Way" will require conviction, consensus and commitment.

Several major issues arise naturally in considering the advisability of continuing in the FTAA.

## Continuing in FTAA

### Reasons Not To Continue.

1. There is no immediate overriding need since its short-term needs could probably be met without FTAA. The Bahamas is not like Brazil, for instance, that is seeking more favourable access to the U.S. market for its orange juice, sugar, steel, textiles and shoes.
   In contrast the Bahamas sells services primarily and U.S. tourists are free to travel to Nassau rather than Orlando for a vacation experience. Bahamian tourism is not now facing "tariff like" barriers.
2. The Bahamas can implement a development program that meets its needs without incurring the administrative costs of participation or the costs of changing the Bahamian system of taxation. It could unilaterally make changes that it chooses and on a time table to its liking.
3. A "Going Alone" policy could enhance Bahamian feelings of sovereignty and autonomy.

### Risks of Not Continuing.

1. The Bahamas signed the Declaration in 1994 and a failure to continue reinforces the perception that it is not a responsible international citizen and does not live up to its commitments.
   A good example of this is the Mutual legal Assistance Treaty of 1992 between the U. S. and the Bahamas. In that case the Bahamian failure to respond meaningfully to 300 requests for assistance between 1992 and June 2000 was an important reason for causing the U. S. Government to change its position on the OECD campaign against the offshore financial centres and to support this initiative.
2. A "Going Alone" policy would further the notion that it can and should isolate itself from the world…lessening the perceived need to change or to addressing the nation's fundamental problems.

The Chinese Example of "Going Alone"

"China is the most dramatic example of having technological knowledge but failing to sustain growth of income per head. The Chinese learned to cast iron a millennium and a half before the Europeans. They had iron suspension bridges, which the Europeans would later imitate. Chinese agriculture was a marvel of high-yield rice fields, with hydraulic engineering performing the irrigation and draining of fields. Chinese agriculture used an iron plow, the seed drill, weeding rakes, the deep-tooth harrow, many different types of fertilizer, and chemical and biological pest control. By the time of the Ming dynasty (1368-1644), China had gunpowder, the paddle wheel, the wheelbarrow, the spinning wheel, the waterwheel, printing, paper (even the critical breakthrough of toilet paper), the compass, and triple-masted ocean-going ships.

But the Chinese chose not to compete in the world economy with their advanced technology, and they closed their borders [during the Ming dynasty]. So China remained stagnant through the nineteenth century, when westerners using these same technologies were able to impose their will on China."

Source: Easterly, William, Page 175.

3. It would lose its ability to take actions against FTAA members that it considered discriminatory and detrimental to its interests with respect to Bahamian investment abroad, telecommunications, e-business, etc.

**Reasons to Continue.**

1. The Bahamas needs foreign investment. FTAA membership would increase the attractiveness of the Bahamas as a place to do business since the FTAA dispute settlement procedures do provide a legal recourse to the foreign investor.
2. Bahamian companies seeking to grow outside the Bahamas would benefit from FTAA standards on trade, investment and services and the related dispute settlement recourse.
3. U. S. Department of Customs clearance in the Bahamas is important to Bahamian citizens and tourists alike. If the Bahamas did not join the FTAA, FTAA members could seek comparable facilities or the elimination of the Bahamian facility. The Bahamas may be more effective in retaining U.S. Customs pre-clearance as part of its FTAA bargaining strategy.
4. The challenge of membership could be the catalyst to implement the changes necessary to achieve sustained economic growth and a reduction in the cost of living.

**The Risks of Continuing.**

While free trade can increase economic welfare, the entrenched government and private interests that resist free trade can produce severe social and political discord. This is especially so if –

1. The changes and their timing are unrealistic,
2. Critical changes such as education reform may not occur and the beneficial results of membership would be obscured.
3. Free trade is perceived as serving foreign interests only and the Bahamian Government is perceived as not being able to protect Bahamian interests.

## Eliminating Tariffs

**Reasons not to Change.**

1. The cost of changing the present tax system is substantial in terms of training, recruitment, management and control; and changing it now would very negatively impact the capacity of the Government to address other issues that are more important. This change now is not in the country's self-interest.
2. Modifying the present tariff system to eliminate the present protective tariff elements should satisfy other FTAA members. However, the Bahamas would be in a position of using its scarce resources on "form" and not "substance".

**Reasons to Change.**

1. A tax on the sale of both goods and services conforms to the stated objectives of FTAA.
2. A sales tax on goods reduces the cost of doing business in the Bahamas since tariffs are paid on entry into the Bahamas and thus increases the investment in inventory. This reduction in investment is especially important for small start-up businesses that normally have limited funding.
3. A tax on goods also is a de facto value added tax since the base for the calculation of the tax now includes Bahamian marketing costs and profits.
4. A tax on services such as medical, legal, accounting, etc. further broadens the tax base.

## Market Access Restraints

**Reasons to Remove Barriers to Foreign Investors.**

The Bahamas needs investments in an increasingly diverse and enriched vacation experience in order to promote tourism growth. It must do so against its major Caribbean rivals, mega-destinations like Las Vegas and Orlando and the on-board facilities of cruise ships. FTAA membership would provide potential investors in the Bahamas with the same protections as available elsewhere.

**Reasons Not to Change.**

Government has a political obligation to promote Bahamian entrepreneurs who often have real competitive disadvantages relative to foreign investors.

## Chapter Seven

# A National Development Plan

The Bahamas needs a National Development Plan that addresses the major problems facing the nation with specific objectives and the promise of concrete achievement. What follows is not a "Plan" but a listing of the major long-term objectives that go beyond the initial submission requirements of the FTAA Agreement.

The Plan should assume the following:

- The Bahamas needs both foreign direct and domestic investment to produce sustained growth.
- It is a high cost country and this fact limits its development options and endangers tourism, the source of its prosperity for the past half-century.
- It must take concerted action to improve its competitive position and to avoid even more drastic remedial measures.
- It must alter its "institutional structures" that include its "norms of behavior, conventions, and codes of conduct". This is particularly difficult.
- Its people must become its greatest asset.
- It must become a desirable place to do business.

There is nothing that is easy in such a plan. It is particularly difficult since the changes involve protected business interests, powerful labour unions and entrenched bureaucracies.

Nevertheless, the Plan will only be successful with strong leadership, courage and a public conviction, consensus and commitment.

Success will create sustained economic growth. This would fulfill, for instance, the often stated dream of the economist and commentator Dr. Walter Williams "To visit the first truly prosperous black country in the world."

## Tariffs, etc.

In their submission to the FTAA the Bahamas should provide a convincing argument to support the retention of a "modified" tariff system because of the difficulty imposed by the other elements in its National Development Plan. If that is not possible, it should opt for the phased introduction of a sales tax.

In this regard, the most important immediate goal should be an increased efficiency in the collection of today's import duties, business licensing fees and real estate taxes.

## Investments.

Fully embracing the FTAA would require that all foreign investors be treated as favourably as a Bahamian investor or an investor from another country. The hotel sector of the tourism economy remains fairly open to such investment. The investment policy of the Government presently restricts foreign investment in a number of sectors including retail and wholesale trades, public transportation, domestic advertising, public relations, non-specialty restaurants, real estate and recreational services.

Entry into a free trade environment through FTAA must consider these "protected" sectors and the consequences of immediately opening them up to foreign investment. As a small, developing nation consideration should be given to transitioning these sectors into a free trade arrangement.

## Education.

The Ministry of Education should develop and adopt a long term plan that will raise the academic and business capabilities of all school leavers so that by 2020 Bahamians will be demonstratively the "Best in the Caribbean." This assumes the –

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[iv] Walter Williams is the John M. Olin Distinguished Professor of Economics, George Mason University, Fairfax, Virginia.

1. Development of appropriate curriculum, student testing and remedial programs
2. Development of standards, testing and re-certification procedures for existing teachers
3. Increased compensation levels to attract and retain superior teachers

## Privatization.

The objective is for the Government to sell all the corporations and utilities to private investors including BTC, Bahamasair, BEC, the Water Works, the Post Office and the Airport Authority. The objectives should be to –

- Sell the Government's entire equity positions,
- Create a wide-scale Bahamian stockholder base in the form of publicly traded securities, and
- Regulate the new enterprises only if there is a natural monopoly and then to set performance standards and pricing targets that will approximate those prevailing in larger foreign markets.

## Justice.

The objective is to firmly establish the "Rule of Law" and the elimination of the "injustice of justice postponed." This would include -

- The immediate commitment to eliminate political interference in the Police Department and Defense Force, and
- Cause the Chief Justice and the Attorney General to develop a plan that will eliminate the backlog of cases and the delays that plague the present system. This assumes the installation of new systems, the selection and training of personnel and the separation of those unwilling and unable to support the reforms.

## Regulatory Framework.

As indicated in the Report in the discussion of "Free Trade & Reality", the move toward a freer economy, which is the clear intent of the FTAA, is likely to produce net benefits to the Bahamian consumer. With this in mind the Government should -

- End all price and rent controls, and
- At more distant target dates specific Bahamian business preferences should end and equal treatment assured under the law to legitimate foreign investors.

## Government Administration.

The Government should free up resources for the increased cost of the education and judicial initiatives by raising the efficiency of all departments. This means the adoption of appropriate plans for new systems and training, the weeding out of pockets of corruption and the installation of sound managerial techniques. The latter would include annual performance reviews, pay increases related to performance and significant reductions in total staff levels.

## A Helpful Perspective.

None of the above proposed elements of a National Recovery Plan are easy since they seem to be diametrically opposite to the norms and ways of Bahamian society. In an increasingly competitive world the Bahamas needs to change to maintain its standard of living. The proposed elements are based on the best thinking available today. Making steady progress on these fronts will require a collective political will where the goals are accepted and the difficult daily and often exceedingly small steps are identified and taken.

April 15, 2003

## Appendix

# I. The Irish Example

Ireland, a small island country of two and half million people, roughly one-third the size of Haiti, has emerged as the "how-to-do-it poster boy" of economic growth.

Let us look at it from the pages of the British magazine, the Economist. In January 1987 a special report on Ireland (a supplement within the magazine) was titled "How the government spent the people into a slump". Particularly telling was the picture of a poverty-stricken family standing on a Dublin bridge under the caption "In Hock, Out of Work". One year later its special report was titled "Poorest of the Rich". Nine years later the special report on Ireland was now the Economist's cover story. Ireland was now "Europe's shining light", its "Emerald Tiger". In ten years…one decade…Ireland went from "In Hock and Out of Work" to "Emerald Tiger".

These comments raise the question "What should government do?" if it is seeking economic growth. One major element is investment in people.

In the case of Ireland, Ray Mac Sharry, a former Irish Minister of Finance, and Padraic White, a former Managing Director of the Industrial Development Authority (the IDA), note that the growth of investment in education from 1960 onward played an important role in their economic growth. After 1967, Ireland introduced free secondary schooling and made major public investments in third-level education including the construction of Regional Technical Colleges, two new universities and an expansion in facilities at the country's existing universities. "The result was a sharp increase in participation rates at all levels of education. And today, Ireland has one of the highest tertiary enrolment rates in the OECD area."[36]

In the national campaign to catch up, its people became Ireland's prime advertising asset. When the IDA began its operations to attract foreign investment in 1970 it emphasized taxes and financial inducements. In 1983 their public relations thrust took a radically different look and tone. It featured Ireland's educated youth, European Union common market membership and one-liners like –
"Ireland—Home of the Young Europeans",
"People are to Ireland as oil is to Texas" and
"People are to Ireland as champagne is to France".
The most effective was a picture of a graduating class in cap and gown on the steps of their university under the caption

"Hire them, before they hire you."

This bit of Irish exaggeration worked! Ireland accounts for just one per cent of the European Union's population; yet it secures over 20 per cent of new inward investment in the manufacturing, software, telecommunications businesses and shared-services sectors.

The "incredible growth" in Gross Domestic Product (GDP) was 9.9% over the five year period 1996-2000. The average annual increase has declined in the past two years (see table) as a result of the economic slowdown but Ireland's performance is still very favourable relative to other countries.

**Real GDP Growth**

| Country | 2001 | 2002 (F) |
|---|---|---|
| Ireland | 6.8% | 3.6% |
| UK | 2.3 | 1.9 |
| France | 2.0 | 1.4 |
| Germany | 0.7 | 0.7 |
| Netherlands | 1.4 | 1.4 |
| Spain | 2.7 | 2.1 |
| Portugal | 1.9 | 1.7 |
| US | 1.1 | 2.5 |
| Japan | -0.7 | -0.7 |

Source: The World Competitive Yearbook 2001;
OECD Economic Outlook June 2002

But the struggle to attract foreign investment had its difficulties and profound ebbs and flows.

There were investments before the founding of the

Industrial Development Authority in 1970 that included General Electric and Pfizer.

In its first five years of IDA operation there were investments in synthetic fibers and in chemicals and pharmaceuticals. Then there was the oil crisis of 1973, the kidnapping by the Irish Republican Army of the Managing Director of the largest foreign employer in the country and the IRA assassination of the British Ambassador to Ireland. These created problems in getting new investors.

But the IDA overcame these negative events in the late 1970s with high tech computer investors. In the early 1980s it attracted medical and pharmaceutical companies; and then came another international crisis and plant closures followed by recovery.

Ireland became the template for development and the World Bank has a Foreign Investment Advisory Agency ready to help any ambitious country.

Appendix

# II. The Mexican Example

Historically Mexico has been a profoundly nationalist, socialist and financially unstable country. As a result of the political chaos following the Revolution of 1910, Mexico was governed between 1929 and 2000 by a single party whose leader was selected every six years and elected without effective opposition.

This type of government produced continuity…a relief from the past; but it was incredibly corrupt. For instance, the expropriation of the foreign oil companies in 1929 was a "national milestone" that produced a well funded political/business bureaucracy and a very powerful union that itself was in the business of supplying oil field services to Pemex. As will be shown below the politically less favoured have suffered most from this system.

**The Foreign Exchange Rate: One Measure of Financial Instability**

| Year | Mexican Pesos Per US Dollar |
|---|---|
| 1975 | 13 |
| 1980 | 23 |
| 1985 | 257 |
| 1990 | 2,813* |
| 1995 | 6,419* |
| 2000 | 9,459* |
| 2002 | 10,040* |

* Actual market rate restated to 1975 basis
For instance, actual 2002 is 10.0 Pesos Per Dollar.

The economic system was inward looking. In the 1950s Mexico adopted the "import substitution" policy promoted by Raul Prebisch, the godfather of the highly influential United Nations Economic Commission for Latin America.

For example, Ford Motor Company made the first automobile manufacturing proposal in 1960.[37] It consisted of two parts:

- An "impartial" appraisal of a.) The high cost of low volume vehicle manufacturing (2.5 times U.S. costs), b.) Future market volumes and c.) The absolute need to eliminate all new and used vehicle imports.
- The specific request for a production quota and the commitment to increase Mexican manufactured content.

The Mexican government approved five automobile manufacturing programs for a country of 35 million people.

Another distinguishing policy feature was the principle that the worker had a "right" to the job, in effect, a de facto property right. Thus the alternative to bankruptcy or liquidation was government acquisition. Eventually the Government owned 900 companies that ranged from sugar, steel and textile mills to home appliance manufacturing, all commercial banks and even a night club.
As a result of the debt crisis of 1982 the government began the process of economic liberalization. In 1986 it joined GATT and by 1994 the maximum tariff was reduced from 100% to 20% and by 1994 80% of the state-owned firms had been sold.

In January 1, 1994 Mexico entered NAFTA. Unfortunately, on that very day the Zapatista uprising began in Chiapas; in March the presidential candidate was assassinated; in December 1994, two weeks after the inauguration of President Ernesto Zedillo, Mexico suffered a mega-devaluation that triggered financial crises in other countries (the "Tequila Crisis"); and in 1995 its Real Gross Domestic Product declined by 9.2%.

These events make an appraisal of Mexico under NAFTA more difficult. However, several studies by the Federal Reserve Bank of Dallas are worth noting. The good news through the year 2000 was that –

- Between 1994 and 2000 Mexican GDP has grown faster than any other Latin American economy and the U.S.
- "Among developing nations today, only China and Brazil received more foreign investment"[38]
- Manufactured goods exports have surged and replaced raw materials as Mexico's main export.

Unfortunately, this good news does not hide the fragility of the banking system and its poor legal environment nor the inequality in the distribution of income.[39]

- "The biggest problem is that property rights are not effectively enforced… collecting on a bad check takes five times longer in Mexico than in the United States…Resolving more complicated contractual disputes can take several years." More attention and investment must be made to reduce the procedural delays in the judicial system.[40]
- "Mexican banks are very hesitant to lend in an environment where contracts are not properly enforced." A good example is lending to bus companies on a purchase and lease back basis. In the early 1980s a group of banks could not repossess their buses for non-payment of rent because the drivers had a prior claim to the asset based on their "right to work."[41]
- "Mexican entrepreneurs face burdensome regulations and a notoriously inefficient bureaucracy."

The inequality in the distribution of income is in part due to –

- The failure of the old regime to invest in education…a third of the working population has not completed primary school.
- A population that grew from 35 million in 1960 to 100 million in 2000.
- The initial flow of economic integration benefits going to the better-educated and prepared.

The bottom line is that NAFTA is a success, but in the short-run at least, a "qualified" one because of significant demographic, educational, legal, political and cultural problems in Mexico.

## Appendix

# III. The "Right" Answer

Over the past half century sustained economic growth has been a world-wide objective and the WTO and FTAA fully embrace this objective. In fact, a very specific set of assumptions and objectives are embedded in it. This Report identifies them and in the following discussion defines the logic supporting them.

The first place to look is in the work of seven economists who have won the Nobel Prize in Economics. The initial "year" shown below is the date of the award.

**1974. Friedrich von Hayek** (1899-1992) grew up in Austria prior to the emergence of National Socialism in Germany and wrote The Road to Serfdom in 1944. This book is a landmark statement of the importance of free markets and a free society and an indictment of totalitarianism; it is "a timeless meditation on the relation between individual liberty and government authority." His "ideas are at the forefront of the movement towards a society based on freedom of association and exchange according to the rule of law, and away from the control of society from the center according to the whim of government."

**1976. Milton Friedman** (1911 - ) is regarded by most as the successor to Hayek and the leader of the Chicago School of monetary economics. While his work on the money supply thrust him onto the national scene, it was the rigor of his analysis and his insistence that it be applied to concrete problems that made him a true academic celebrity. For instance, he played a prominent role in the Chilean economic reforms of the 1970s, the all volunteer army, school vouchers and the Freedom of the World Index.

**1979. Theodore Schultz** (1902-1998) was an agriculture economist who studied farmers in the U. S., Russia and Africa and concluded that farmers were "fine-tuning entrepreneurs" whose entrepreneurial qualities were "weakened by government policies that distort price incentives." But he is most recognized for his broadening of the definition of capital to include human capital that increases with investments in education, health and worker mobility.

**1986. James M. Buchanan** (1919 - ) was awarded for his explorations into the political bases of economic decision making. He "developed the theory of public choice which explores the problems societies face when deciding how to allocate their collectives resources."[42]

**1987. Robert Solow** (1924 - ) examined the components of economic growth: savings and investment, population and technical knowledge. He concluded that each country had its own "steady state" rate of economic growth that could only be increased with a change in the third element, technical knowledge. He described that element as "the part of total output that is attributable to the quality of the interactions between labour and capital in current production."

With respect to trade liberalization he stated –

"The notion that the poor countries of the world can in any reasonable interval achieve rich-country incomes without trade and capital flows is utterly implausible. If the poor countries of the world have to depend upon themselves for the saving to finance the investment that they need, or have to develop by themselves the skills and technology they need to become rich by our standards, it's going to take forever.

"Where I think the open-economy partisans run into problems…is that they tend to look at overall progress and brush off the fact that a lot of people lose in this process…A society in which a small number of people get very rich and a large number of people get very poor is not really progressing, even if when you add it up and average it, it appears to show rapid progress."[43]

**1991. Ronald Coase** (1926 - ) identified and clarified the significance of transaction costs and property rights to the institutional structure and functioning of the firm.

The ability to coordinate the factors of production and control transaction costs determines not only the size of the firm but overall economic efficiency and the rate of economic growth.

**1993. Douglass North** (1920 - ) noted that economies often do not function efficiently. He focused on those institutions that determine the rules of the game, the most basic relationships in social life, and particularly economic relationships. Institutions include the family firm, capital markets, the credit system, the legal system, standard contracts, relationships between firms and the government, and so on. He postulated that institutions give society stability and likewise restrain and enforce compliance to the "rules". In a world of dynamic change, however, the rules also resist change but eventually they do change after delays.

His critics contend that he assumes that economic progress is in the direction of "the English ideal of liberal individualism, impersonal dealings, the rule of law, and laissez-faire economic policy – in short, to Adam Smith's market."[44] In fact, this is the assumption underlying the FTAA.

And there are others that provide valuable insights.

**Bernard Lewis**, a prominent Middle East historian from Princeton University, observed that the Muslim empire between 600 and 1400 AD was the dominant, most advanced civilization west of China. Then the Muslim world began a long decline relative to Western Europe as evident in a long string of military defeats. The ultimate shock was the 1948 defeat of five Arab armies…not by an Imperial Western power…but by a "contemptible gang of Jews." "The world of Islam had become poor, weak, and ignorant…the dominance of the West was clear for all to see, invading the Muslim in every aspect of his public and–-more painfully--even his private life."[45]

Bernard Lewis avoids the Muslim blame game of transferring guilt to foreigners and chronicles unsuccessful Muslim efforts to import and absorb the perceived elements of Western military and business prowess. He attributes this decline to the structure of the Muslim faith and society not as first conceived but as it subsequently developed.

The Islamic world is divided into believers and infidels. The believers had the Islamic law, the true and perfected descendent from Judaic-Christian beliefs, whose all encompassing theology went beyond religion as we know it. It was so self-centered in its revealed truth that it limited contact with the west and inhibited the observation and acceptance of Western advances of any type. Furthermore, it limited and retarded the development of a secular state operating outside of a religion.

Bernard Lewis sees two cures.

1. "Attribute all evil to the abandonment of the divine heritage of Islam and return to a real or imagined past. That is the way of the Iranian Revolution and the so-called fundamentalist movements and regimes in other Muslim countries."
2. "A secular democracy, best embodied in the Turkish Republic founded by Kemal Ataturk." But the road to democracy is long, hard and full of pitfalls. These include "the lack of freedom—freedom of the mind from constraint and indoctrination, to question and inquire and speak; freedom of the economy from corrupt and pervasive mismanagement; freedom of women from male oppression; freedom of citizens from tyranny."

He considers the secular military dictatorships of Egypt, Iraq, Pakistan and Syria to be in an uncertain middle ground between the two cures.

**Francis Fukuyama**, a political scientist from George Mason University, has promoted the concept of "Social Capital". He considers it to be analogous to investments in physical assets and human beings. He describes it as those norms of behavior that lead to cooperation between individuals and are related to traditional virtues like honesty, the keeping of commitments, and the reliable performance of duties, reciprocity, and the like.

He concludes that social capital "is important to the efficient functioning of modern economies, and is the *sine qua non* of stable liberal democracy. It constitutes the cultural component of modern societies, which in other respects have been organized…on the basis of formal institutions, the rule of law and rationality."[46]

He is careful to point out that in some societies such norms exist within a family but do not apply to relationships outside the family. Here there is no commitment "to treat all people morally." This accounts for widespread corruption in public office that strangles economic growth in Africa, Latin America and southern Italy.

**William Easterly** in his book *The Elusive Quest* for Growth concludes:
"We have learned once and for all that there are no magical elixirs to bring a happy ending to our quest for growth.

- Prosperity happens when all the players in the development game have the right incentives.
- It happens when government incentives induce technological adaptation, high-quality investment in machines, and high-quality schooling.
- It happens when donors face incentives that induce them to give aid to countries with good policies where aid will have high payoffs, not to countries with poor policies where aid is wasted.
- It happens when the poor get good opportunities and incentives, which requires government welfare programs that reward rather than penalize earning income.
- It happens when politics is not polarized between antagonistic interest groups, but there is a common consensus to invest in the future.
- Broad and deep development happens when a government that is held accountable for its actions energetically takes up the task of investing in collective goods like health, education, and the rule of law."[47]

**The IMF, the World Bank and the Inter American Development Bank** now promote "Second Generation Reforms" that focus on the structure of institutions, improvements in the administrative, legal, and regulatory functions of the state and incentives and actions that encourage private sector development and institutional reform.[48]

Appendix

# IV. Rent

**Economic Rent** is a payment to a factor of production in excess of what is necessary to keep it in its present employment.

**Rent Taking** occurs when an individual bound either explicitly or implicitly by a contract violates the terms of that contract for private gain. For instance, elected officials who have the power to reduce costs for some at the expense of others may do so to produce more votes in a coming election. Or they have the power to raise the cost of an individual's dealings with the state and get compensated for not doing so. This is also known as "corruption".

**Rent Seeking** is the use of resources in an attempt to appropriate a surplus in the form of a rent. An industry may use resources to lobby a government to impose a restriction such as a TARIFF on an imported good so that the industry my raise prices. Consumers suffer two losses: the higher cost of the product consumed and the loss of output from the resources devoted to rent-seeking.

Source: *The MIT Dictionary of Modern Economics*, Fourth Edition, MIT Press, pages 121 & 372.

## Appendix

# V. Stolen Property

A current case illustrates the point that the justice system needs to be revamped. The principals are identified as John and Jane Smith…she is Bahamian and he is American. When John retired early in the United States, they elected in 1998 to relocate to Nassau where Jane would manage the remaining commercial real estate inherited from her deceased parents; and they jointly would start an Internet based service company for Bahamian business. The story starts with one property and one lessee identified as "Client" that produced three "related" legal disputes: The Eviction, Cutlass Assault and Assailant cases.

1. Client signed a five-year lease with Jane's mother in 1996.
2. Jane in early February 2000 gave Client a 90-notice to vacate on the basis that he violated the terms of the lease…he was $4,000 in arrears on his rent. This is the **Eviction Case**. In addition, he violated the terms of his business license and the "environmental code" insofar that he was polluting the water table. This conduct caused Jane to lose the renter on an immediately adjacent property.
3. In May 2000 Client erected a sign in violation of the lease agreement.

   This was the occasion for the **Cutlass Assault Case** that ran parallel or at the same time as the Eviction Case. While John and Jane were supervising a handyman in removing the sign, Client and a relative arrived on the scene and Client pushed both John and Jane and threatened them with death with the cutlass in his hand. The police were called, took the cutlass but did not arrest Client.

   a. The Attorney General's Office did not prosecute the Client for "assault with a deadly weapon"; and John and Jane on their inquiry were told that the police lost the case. With a direct appeal to the Chief of Police, the case was recovered and a prosecution date was set.
   b. In July 2001 the Magistrate hearing the case excused himself from the case and another Magistrate took it in September.
   c. The case came to trial in October 2001. The arresting officer did not appear with the cutlass and the Bahamian handyman, who witnessed the entire affair, simply refused "to get involved" and was never called for fear of his becoming a hostile witness. The Magistrate issued a warrant for the officer's arrest and adjourned the case.
   d. The case came to trial in December 2001 but the Prosecutor was new to the case and the cutlass and the officer who took it from Client were not present. The case was adjourned.
   e. The case reconvened in January 2002. Client testified that he did get upset and did indeed come running out of the building with a cutlass that he "held at his side the whole time." The Magistrate adjourned the case to review the documents and develop his judgment.
   f. The case reconvened in February 2002. Client was not present; the Magistrate still was not able to give a judgment and he adjourned the case.
   g. The case reconvened in March 2002 and the Magistrate acquitted the Client of the charges "because the prosecution did not adequately prove its case."
4. In the first week of June 2000 Jane took possession of the building, locked Client out and hired guards.
5. One week later Client forcibly re-occupied the property at night. The Police were called but would make not make an arrest since it was a "civil matter" for the courts.
6. Jane immediately initiated new eviction proceedings through the Magistrate's Court.
7. The case convened on June 16th, 2000. Client failed to return to court and the Magistrate ordered Client to leave the premises within 30-days.
8. On July 17th Client requested a new hearing to overturn the eviction and got it.
9. The court reconvened on August 4th, 2000 and the Magistrate ruled in favor of Jane and ordered Client to leave the premises immediately. He did so for three months.

10. On November 7th, 2000 Client broke in and reoccupied the property. He had a notice of appeal that was "granted out of time".
11. The next day Client filed for an injunction allowing him to remain on the premises until the appeal went through. The injunction was wrongly issued since John and Jane were not present and it was based on false information.
12. As of the date of this Report Client is still occupying the building and not paying rent; and the legal actions of John and Jane are suspended pending a ruling on the Client's injunction.

Separate from this experience at this property Jane was assaulted and robbed of $1,200 in February 2001 while she was collecting rent at another property. A car approached her as she was leaving the property; the Assailant jumped out, grabbed the rent envelope and hit her in the face causing her to fall.

The sequence of events that follows is the **Assailant Case**:

1. Jane filed a Police Report and got a medical examination. The domicile of the Assailant was known but it took John 4 months to get the police to arrest him.
2. In late 2001 the case charging Assailant with "causing harm" was convened. Jane presented her testimony and documentation but her witness and the examining doctor were not present. The case was adjourned.
3. The case was reconvened in January 2002. The assailant was not present and a warrant was issued for his arrest.
4. The case was reconvened in May 2002. The prosecution witnesses did not appear. These included a Jamaican women who worked for a law firm and who was the eyewitness to the assault, and the examining doctor, an Asian national. The eyewitness expressed a fear of reprisal by Assailant as the reason for her failure to appear.
5. The case reconvened in August 2002 but the Judge stated that she was not ready to hear the case.
6. The case reconvened in September 2002. The Assailant admitted that he stole the $1,200 but claimed that he did not hit Jane. He produced a witness that falsely testified that Jane was wearing 6-inch heals and tripped on the pavement.
7. The case reconvened 12 days later and the Judge indicated that he was not ready.
8. The case reconvened in October 2002 and the Judge was not present.
9. The case reconvened in November 2002 and Assailant was acquitted because the prosecution did not prove its case beyond the shadow of a doubt.

Appendix

# VI. Literacy in the Workforce

The following is a letter from the President of a Bahamian corporation to the President of a Civic Association that sponsors programs to create a better Bahamas (identified as "CA#2"):

"I appreciate receiving a copy of the latest Annual Report of CA#2, and wanted to commend your efforts to make The Bahamas a better place to live and work. The mission and goals of the organization are all very admirable and may eventually make some difference. However, having reviewed your list of beneficiaries, it seems to me that your priorities do not directly impact the main problem contributing to crime in The Bahamas. Let me explain my position.

"During my years living and working in The Bahamas my company has been continually encouraged and admonished to provide training for our employees to advance their knowledge and understanding of the latest technology, and to prepare them for a better future. This we have done to a considerable extent, and continue to do so.

"However, this experience has also taught us that it is not training we need, it is learning. Unfortunately, we have discovered…much to our chagrin…that too many young, bright, intelligent high school graduates (males, especially) can't learn because they can't read and write effectively. After conducting much training without much evidence of learning, we confirmed our suspicions with professional testing. Needless to say, we found this to be very disappointing and frustrating.

"Other experiences have served to verify the extent of this tragic situation. We have been approached by public high school administrators to help provide reading texts written for grades two and three so they can use them to teach grades eleven and twelve students how to read. We have also been asked to help provide copies of the well-known program "Hooked on Phonics" to accomplish the same objective. Of course, the Ministry of Education will not approve the purchase of these teaching materials for a high school. Therefore, the public school administrators and the PTA Associations have to seek private funding – and do it in a way that does not raise awareness of the problem. I guess the authorities think that if they don't talk about it, the problem doesn't exist!

"Why does this have anything to do with CA#2? It is my opinion that illiteracy is the main factor contributing to crime in The Bahamas. It is no surprise to me that Fox Hill Prison is full of strong, bright, intelligent young men because crime may be the only profession that does not require reading and writing as a prerequisite!

"I know the official literacy rate is high – as judged by the number of High School certificates awarded. But that means nothing if a high percentage of those certificate holders are effectively illiterate because they have never been taught to read and write.

"It is a well established fact that most newspapers throughout the world are written at a grade six reading level. That means that all primary school graduates should be able to pick up a newspaper, read it, understand it and tell you what they read in their own words. (You might find it interesting to test your own children.) I wonder how many of our primary school students can do that? I strongly suspect that many, if not most attending public schools cannot do it. And if they can't do it, they can't learn effectively and they will have an exceedingly difficult time providing an honest living for themselves and their families.

"My strong and sincere opinion on this subject causes me to provide support to Project Read (and similar programs) instead of to CA#2. And I would strongly encourage your organization to seriously investigate the effective literacy of the Bahamian young people and determine to what extent it contributes to the crime problem. Having done so, I believe you will add Project Read and other similar programs to your list of beneficiaries. You may also decide to encourage the educational establishment to face the facts and teach the kids first to read and write – and to do it at a young age while it is easy to do.

"It is ridiculous to think The Bahamas will ever be able to cope with the WTO, the FTAA or to develop an e-commerce industry until most of the kids can read effectively in primary school. I believe this is an urgent matter. If it is not dealt with soon, many Bahamians will be marginalized and dislocated by the global economy as it begins to touch this country in a significant way. I don't have to tell you what will happen to the crime statistics when that begins to happen. In fact, I believe it has already begun.

"I have lived and worked in the Far East, including Singapore, and it is interesting to compare that country to The Bahamas – as many have done in the past. Both countries are similar. For example, they are both small and have no natural resources. However, unlike The Bahamas, Singapore is a very wealthy country primarily because their society and culture and population place a very high priority on a good advanced education for all. It is time The Bahamas adopted a similar priority. CA#2 is in a unique position to help cause that to happen. The benefits would go far beyond helping the crime problem, but that would be one of the most immediate benefits. Another benefit would be an immediate and dramatic improvement in productivity.

"Educated young people have a future; uneducated young people do not. And, in my opinion, an education means only one thing – the ability to learn. And the ability to learn requires only one thing – the ability to read and write well at an early age. The challenge is at the primary school level, not at the College of the Bahamas level. Let's get started.

"Further discussion would be welcomed.

"Sincerely,

"The President of a Bahamian Company"

Appendix

# VII. The Ultimate Resource

One of the most optimistic economic views on the importance of people is that of Julian L. Simon who stands in sharp contrast with the pessimists who see limits and bad endings in both the short term and the long run.

"In the short run, all resources are limited…

"The longer run, however, is a different story. The standard of living has risen along with the size of the world's population since the beginning of recorded time. There is no convincing economic reason why these trends toward a better life should not continue indefinitely…

"Increased population and a higher standard of living cause actual and expected shortages, and hence price rises. A higher price represents an opportunity that attracts profit-minded entrepreneurs and socially minded inventors to seek new ways to satisfy the shortages. Some fail, at a cost to themselves. A few succeed, and the final result is that we end up better off than if the original shortage problems had never arisen. That is, we need our problems, though this does not imply that we should purposely create additional problems for ourselves."[49]

Thus it seems that in the long run successful problem solving by people adds to the stock of knowledge and that allows them to overcome new shortages…thus making people the Ultimate Resource.

Appendix

# VIII. Comparative Advantage

## An Example of Comparative Advantage

| | Cottonland | Woodland | Total |
|---|---|---|---|
| **Production without Trade** | | | |
| Bales of cloth per day | 10 | 2 | 12 |
| Pieces of furniture per day | 05 | 3 | 08 |
| Total | 15 | 5 | 20 |

**Note: Production Alternatives**

| | |
|---|---|
| Cottonland | 1 piece of furniture = 2 bales of cloth |
| Woodland | 1 piece of furniture = 2/3 bales of cloth |

| | Cottonland | Woodland | Total |
|---|---|---|---|
| **Production with trade** | | | |
| Bales of cloth per day | 20 | 0 | 20 |
| Pieces of furniture per day | 0 | 8 | 08 |
| Total | 22 | 8 | 28 |

Even if a country can produce everything more efficiently than another country, there is still scope for trade. A country can maximize its wealth by putting its resources into its most competitive industries, regardless of whether other countries are more efficient in absolute terms in those industries.[50]

As a hypothetical example, consider two countries that have land and people than can produce cotton cloth and/or furniture. Assume that Cottonland produces both cloth and furniture better than Woodland and so it is named "Cottonland" and the other country is named "Woodland".

Cottonland has an absolute advantage…it is more efficient…in the production of both cloth and furniture. However, to achieve greater wealth, each country should specialize in the item in which it enjoys greatest advantage among all the products it produces…where it has a comparative advantage.

In terms of its "Production Alternatives", or the cost of not transferring resources, Cottonland is twice as efficient in producing cloth as furniture.

The implications are that Cottonland should produce cloth and trade for Woodland's furniture and Woodland should produce furniture and trade for cloth. Channeling resources into the most productive enterprise in each country will result in more products to trade.

This simple example illustrates the overall growth impact of international trade. In addition, it helps explain why countries that are neighbors and tend to be similar in their economic capabilities tend to trade with each other more than with countries that are more separate economically and geographically.

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# Tourism Task Force on Trade Liberalization Participating Organizations and their Mission

**Bahamas Hotel Association**
P.O. Box N 7799
Nassau, Bahamas
Phone: 242-322-8381 Fax: 242-326-5346
**Mission:** The Bahamas Hotel Association serves the needs of The Bahamas' hotel industry by providing a forum to facilitate the promotion, profitability, quality growth and security of the tourism industry consistent with the needs of The Bahamas.

**Bahamas Hotel Catering & Allied Workers Union**
P.O. Box GT 2514
Nassau, Bahamas
Phone: 242-323-5933 Fax: 242-325-6546
**Mission:** The BHCAWU, the recognized bargaining agent for hotel and catering workers in the Bahamas, is dedicated to the growth and development of the whole person and the educational, cultural, social, political and economic advancement of its members

**Bahamas Hotel Employers Association**
P.O. Box N 7799
Nassau, Bahamas
Phone: 242-322-2262 Fax: 242-325-8998
**Mission:** The BHEA strives to achieve and maintain a stable industrial relations environment in the hotel sector through understanding and mutual respect between Employers and Employees. By so doing, it will contribute to the continued development and expansion of the tourism sector and maximize its contribution to the Bahamian economy.

**Bahamas Tour Operators Association**
P.O. Box N 1401
Nassau, Bahamas
Phone: 242-322-2606 Fax: 242-326-5785
**Mission:** To further the interests of the sightseeing and tour business and enhance the value and beneficial advantage of the industry.

**Nassau Tourism & Development Board**
P.O. Box N 4740
Nassau, Bahamas
Phone: 242-326-0992 Fax: 242-323-2998
**Mission:** Working in partnership with industry leaders and government, to advance a tourism product which is clean, safe, exciting, uniquely Bahamian and perceived as value received for value spent.