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THE EVOLUTION OF STRUCTURAL ADJUSTMENT AND STABILIZATION POLICY IN JAMAICA

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I. INTRODUCTION

The history of economic policy in Jamaica since World War II, viewed at some distance, reflects the broad sweep of fashion in the history of economic development. The cycles of industrialization by foreign investment, import substitution, populist socialism, and structural adjustment are all present. The most recent phase of that history, that of structural economic reform, has however presented some confusion in the literature on Jamaica. At one extreme, economic reform may be dated from 1977, when Jamaica signed its first Stand By Agreement with the IMF, accompanied by the usual list of conditionalities and their implications for economic reform. Witter and Anderson (1991), largely using that fact, and Lora (1997), using a narrow list of indicators, imply that Jamaica is an early reformer. At the other extreme, some key elements of economic reform were not implemented until 1991. Following this vein, Handa and King (1997) suggest that economic reform is a phenomenon of the 1990s.

The survey of economic reform below reveals a country drawn reluctantly into the reform era, implementing some aspects of economic reform from the early 1980s, delaying others until the 1990s and ignoring a few elements entirely. Economic liberalism has not caught the popular imagination in Jamaica. The fundamental liberal ideas underlying structural adjustment reform are not popular in Jamaica, and have for the most part been foisted on the people by first, an unwilling administration, and later, by an unfocused one merely following to a limited extent world economic fashion. This unwillingness and lack of commitment will be important in understanding the inconsistency in the reform process as it unfolded in Jamaica.

Jamaica represents an interesting case study of economic reform for a number of reasons. First, the various aspects of economic reform occurred during distinct periods. This case stands in contrast to those, such as Chile in the late 1970s, that changed economic policy radically over a relatively short period of time. The Jamaican case, therefore, may be instructive in understanding issues surrounding the timing and sequencing of reform.

The other reason why Jamaica presents an important case study is that, amongst reforming economies, it has one of the worst records of economic performance in Latin America and the Caribbean during the era of economic reform. While average growth in the region was 2.2 percent per annum in the 1980s, Jamaica grew at an annual average of only 1.4 percent[1]. In the 1990s, the discrepancy worsened. The economies of Latin American and the Caribbean averaged 3.0 percent per annum from 1991 to 1996, but Jamaica's average growth rate was a mere 1.3 percent. Even within the Caribbean alone, Jamaica's relatively poor performance is manifest. The average growth rate for the period 1980 to 1996 is 3.0, whereas Jamaica managed only 1.4 percent annually over the same period.

Finally, many of the particular circumstances of the Jamaican economy would have led to the expectation that Jamaica would have responded favorably to economic reform. Jamaica, by the standards of the wider Latin American region, is an exceedingly small economy with a productive structure correspondingly highly dependent on foreign trade. Jamaica also enjoys proximity to the major market of the United States. And Jamaica enjoyed spectacular growth rates in the 1960s prior to the implementation of the policy framework that economic reform is designed to dismantle. All these considerations suggest that Jamaica would have been a good candidate to highlight the positive outcomes of economic reform.

The survey begins with the economic and policy context in which economic reform has occurred in Jamaica in Section 2. In Section 3, six elements of economic reform are reviewed, namely trade liberalization, domestic financial liberalization, opening of the capital account, privatization, tax reform, and labor market reform. Section 4 reviews the state of stabilization policy, through the effects of fiscal, monetary, and exchange rate policy, during the period of economic reform. The consistency of the various aspects of economic reform, their sequencing, and their complementarity with the stabilization policy is examined in the Section 6. In the final section, economic outcomes during and after the reform period are discussed.

II. INITIAL CONDITIONS

Jamaica's post-war economic history falls naturally into four phases, delineated by the strategy for economic development pursued during each phase. Impressive growth rates, a stable macroeconomic environment, and increasing industrialization characterized the 1950s and 1960s. By sharp contrast, the 1970s and 1980s, under greatly increased state intervention in economic matters, brought double-digit inflation, currency depreciation, and general economic stagnation, along with rising poverty. The difference between the two decades lay only in the philosophical motivation for the state intervention. Whereas in the 1970s state control was motivated by populism, under the Seaga administration in the 1980s it had a more pragmatic and less explicitly ideological purpose, somewhat but not greatly constrained by the obligations of structural adjustment programs. The 1990s has been the period of more serious economic reform, but in the presence of macroeconomic crises.

1. Industrialization by Invitation: 1960s

The model of economic development that underlay the policies pursued by Jamaican administrations during the 1950s and 1960s reflected separately the work of Raul Prebisch and Arthur Lewis. As elsewhere in Latin America and the Caribbean, the motivation for the economic development model was the perceived need to industrialize the economy, as a means of creating employment to absorb population growth that the agricultural sector was incapable of fully employing. Following from this, the economic policy thrust of the 1950s and 1960s had the imperative of industrialization.[2] Growth was more or less taken for granted, so the role of development policy and the debate surrounding it in Jamaica (as elsewhere) was to determine the character of growth and consequently the structure of the resulting economy. In particular, a direct objective of policy, following Lewis, was employment creation. The mechanisms of the structural change were to be the system of taxation, state promotion, and, to lesser extent, market protection, while the agent of economic change would be foreign direct investment.

The industrialization initiative through tax legislation began in the late 1940s with the passage of legislation in the period 1947 to 1949 designed to encourage the development of the textile and cement industries. The tariff structure was revised in 1951 to remove anti-industrial biases (Figueroa, 1993). Other legislation during the decade provided incentives for locating manufacturing in Jamaica. In the 1960s, legislation enacting tax holidays, accelerated depreciation, and other tax concessions for various industries were passed, including those for textiles, bauxite, and tourism, and any industry with an exported product (Stephens and Stephens, 1986). Tax concessions were also granted on a broader basis to all new enterprises in one instance and to all industrial initiatives in another act of legislation.

The public agency of state promotion was the Jamaica Industrial Development Corporation (JIDC), which was established in 1952 to promote Jamaica as a location for foreign industry. The JIDC pursued its mission through marketing initiatives and through the distribution of general promotional material (Figueroa, 1993). The JIDC also provided factory space at moderate rental to favored industries, and provided technical and financial assistance (Stephens and Stephens, 1986). The management of industrial property, though part of the JIDC's functions, was an exception to the general pattern that government for the most part stayed out of commercial activity.

By the standards of later decades in economic history, there was little protection of the domestic market from imported competition. What protection existed was accomplished by the use of quantitative import restrictions, which were imposed on a small number of manufactures during the 1950s. During the 1960s, the number of items subject to quantitative restriction increased three-fold (Figueroa, 1993). Nevertheless, the extent of domestic protection remained small.

The role of government in this process of economic development was at once involved but restricted. The governments of the time were activist, recognizing a need to both steer and promote economic development. Along with this went a willingness to use the normal apparatus of government (import levies, the tax structure, quantitative restrictions) in order to achieve its objectives of government. At the same time, government was not participatory. Its role was limited to encouragement and incentives, largely shying away from directly owning and engaging in productive activity.[3] Further, aside from its role in the provision of social infrastructure, government also stayed out of purely welfare and redistributional activities in the way that government in, say, the United States had embraced at the time.

Monetary policy was passive. From the second World War up to the 1960s, monetary policy was dictated by a currency board, established under the Currency Notes Law of 1939 (Lue Lim, 1991), with the British pound being used as the reserve currency. A central bank, the Bank of Jamaica, was established in 1991, but monetary policy continued to be determined by the passive exchange of domestic currency issue with sterling up until 1966. Even after the abandonment of the de facto currency board arrangement, maintaining the integrity of the exchange peg with the pound was the determining anchor of policy. Therefore, when the British currency was devalued against the United States dollar in 1968, the Jamaica currency devalued correspondingly in order to maintain its par with the pound.

The growth and development of the Jamaican economy during this period was quite spectacular, either in the context of other developing economies or in that of the subsequent performance of the Jamaican economy. GDP grew at an annual average rate of 5.1 percent between 1960 and 1972 (Table 1), while inflation was kept to an average of 4.5 percent.

The economy underwent a structural change. The relative importance of agriculture declined, as the service sector expanded and the industrialization thrust bore some fruit with the growth of the nascent manufacturing sector. At the same time, the mineral and tourism industries drove economic growth. The mineral industry was based on the extraction and exportation of bauxite ore. From initial explorations in the 1940s, Jamaica quickly rose to become the leading producer and exporter of bauxite in the world. The tourist industry expanded throughout the 1960s and Jamaica was transformed from being an exclusive to a mass tourist destination. On the backs of the development of these two industries, the construction sector experienced great expansion.

Table 1
GDP GROWTH, ANNUAL

1961	2.4	**1971**	4.4	**1981**	2.6	**1991**	0.5
1962	1.4	**1972**	7.9	**1982**	1.2	**1992**	1.9
1963	2.7	**1973**	2.8	**1983**	2.3	**1993**	1.3
1964	8.6	**1974**	-5.4	**1984**	-0.9	**1994**	1.1
1965	7.8	**1975**	-1.2	**1985**	-4.6	**1995**	0.5
1966	3.9	**1976**	-6.3	**1986**	1.7	**1996**	-1.8
1967	2.5	**1977**	-2.4	**1987**	6.2	**1997**	-2.4
1968	6.1	**1978**	0.7	**1988**	1.5	**1998**	-0.7
1969	6.5	**1979**	-1.8	**1989**	4.6		
1970	7.7	**1980**	-5.7	**1990**	5.5		

Source: Statistical Institute of Jamaica, International Financial Statistics, International Monetary Fund.

Notwithstanding the development of a tiny "screw-driver" manufacturing capacity (along with some food-processing industry), economic prosperity was built upon the natural endowments of bauxite and beaches. The impressive growth rates of the period derived from the initial investment in and exploitation of those resources. The reach of the economic prosperity was limited as a large portion of the population remained marginalized from the process of economic development. This was at least partly due to the dualistic nature of the urban labor market and to the inability of the agricultural sector, based on preferential treatment of its export products and on an inefficient domestic/subsistence sector, to provide much prosperity for the rural population.

2. State Populism: 1970s

Between 1972 and 1980, under the populist Manley administration, economic policy in Jamaica was motivated by the objective of redistribution. Again, given the growth performance of the economy coming into the decade, growth was taken for granted, and the object of economic management was the pursuit of equity. The policy mechanism that guided that objective was market restrictions and government intervention, and, as the decade unfolded, these were accompanied by the expediency of effectively restraining international trade with Jamaica.

The economic role of government increased greatly, in every way. Firstly, the government took an increasing role in productive activity. This was initially a matter of ideology, as the administration sought to control the "commanding heights of the economy". In pursuit of this principle, public ownership came to the banking sector, public utilities, and mining. The largest commercial bank operating in Jamaica at the time, Barclays Bank DCO of

Britain, was purchased outright by the government. The local operation of Cable & Wireless, the telecommunications monopoly was also taken into public ownership. The electricity utility was nationalized, as was the public transportation company.[4] While these public acquisitions were in the pursuit of an economic principle, later on, as the economy faltered, public ownership increased as the government took over failing enterprises in an attempt to maintain the level of employment. In this way, the government came to own several hotel properties and some manufacturing enterprises. This latter consideration imposed a considerable burden on the fiscal accounts.

Government also took on a larger responsibility for redistribution and social equity. To that end, there were increases in public expenditure on health, education, and housing. Increased expenditure on education involved the construction of new schools and the abolition of tuition at all levels of the educational system. The redistributive aim was also pursued through public works programs whose primary justification was employment creation. Indeed, it was called the "Special Employment Program". Finally, subsidies were introduced on certain staple foods and on kerosene oil for home cooking.

An effect of the increased roles of government was therefore the expansion of the public sector. In the five years after October 1972, the number of persons employed in public administration increased by 66 percent and the real non-debt service expenditure of the government increased by 88 percent. During this phase of economic development, the public sector expanded from 10.2 percent of GDP to 16.2 percent.

The general retreat from market determined outcomes in the economy, evidenced by the above interventions, was accompanied by price controls which were imposed on a varied and ever-growing list of commodities, including rental housing. A minimum wage was also established.

Probably the most significant shift of economic policy that occurred in the 1970s was the closure of the Jamaican economy with respect to international trade. Exchange controls were invoked in 1974, and were made increasingly stringent throughout the remainder of the decade. A License requirement was introduced for the importation of all consumer goods, tariffs were raised, and quantitative restrictions were imposed on a wide range of imported commodities, including outright prohibition of some. Foreign capital was discouraged, both in word, and through the nationalization of various foreign-owned enterprises. Finally, the government established a monopoly on the importation of various food items, with the establishment of the Jamaica Commodity Trading Corporation. All of the above represented restrictions on foreign trade. During this time, foreign consumer items disappeared from store shelves.

By every measure, the performance of the macroeconomy during this period was poor. While real GDP grew by 7.9 percent in the last year of the previous economic program, during 1974, the first full calendar year of the new policies, the economy contracted by 5.4 percent. Thereafter, the economic contraction continued almost throughout the decade. The average rate of contraction of the economy during this period was almost 2 percent per year. The inflation rate, which had previously not been above single digits, averaged over 12 percent during this phase. Unemployment rose from 22 percent to 30 percent between 1972 and 1989, and the level of investment declined.

The economy, as it stood in 1980, was therefore at the zenith of government intervention and the nadir of economic performance. International trade was severely restricted by the combination of high tariffs, license requirements, and capital controls. Domestic economic productivity was hampered by domestic price controls, financial repression, and labor market regulations. The public sector was large and involved in all areas of the economy, included whole or partial ownership of nearly 400 productive enterprises. The economy produced a per capita output that was 26 percent below its peak of seven years earlier.

III. FIRST GENERATION REFORMS

With the change of administration in 1980 came only a subtle shift of economic strategy. The new administration remained as distrustful of market-oriented economic solutions as its predecessor. The difference was that governmental intervention in economic matters would be directed towards a return to the encouragement of foreign investment, or "dependent capitalism" as elsewhere described (Stephens and Stephens, 1986), but with the emphasis on the "dependent" rather than on the "capitalism". Therefore, the period 1980 to 1989 represented pragmatically guided, state-directed development. However, under the stimulus of IMF and World Bank agreements, there was some, limited, movement towards economic reform.

The stagnation of the Jamaican economy that accompanied the earlier phase continued during this one. For the first three years, annual growth was near 2 percent, after which the economy suffered two years of contraction. Near the end of the period, the economy evidenced a return to real growth for the first time in decades, posting 6.2 percent growth in 1987. In 1989, however, the country was devastated by Hurricane Gilbert, which destroyed a substantial portion of the economic infrastructure and capital stock, as a result of which the economy had little growth that year. For the period as a whole, the economy expanded at a negligible 0.6 percent per year, which with population growth translated into declining per capita income.

Monetary and fiscal management during the 1980s, under the scrutiny of the IMF, resulted in a gradual improvement in fiscal balances and inflation. For the period as whole, inflation averaged 8.4 percent annually. The structure of the economy shifted in a way consistent with the trend that was unfolding prior to the period of state populism. Manufacturing and construction expanded in place of agriculture, which resumed its secular decline in relative importance.

After 1989, with the return to power of Manley's party, economic reform accelerated as elements of the reform agenda not hitherto pursued were brought into the program. The economy suffered from the shocks of adjustment. The lifting of capital controls sparked a massive depreciation and inflation. The consequence of this and the structural adjustment compelled by trade reform produced a steadily declining economy in the 1990s.

1. Import Liberalization

As described above, the new administration in 1980 inherited a trade regime that was tightly restricted and controlled. Average import tariffs were over 50 percent according to World Bank (1994) estimates; there were a large number of quantitative restrictions effected through the requirement of an import licence; and most basic food items could be imported only by the government import monopoly. Early in the new administration, the import monopoly of the Jamaica Commodity Trading Corporation was expanded to include new items. The 1980s were a period of some, but not wholesale, liberalization of the trade regime.

The changes in the trade regime has taken place in four phases. The first phase occurred between 1983-85, after Jamaica entered into the World Bank Structural Adjustment Loan agreement of 1983. Some 180 items were removed from the list of items requiring import licences. There was, however, a clear reluctance to embrace trade liberalization on the part of the administration of the day. While some imports were liberated from the need for an import licence, there was a corresponding increase in import tariffs on those items (under the heading of "Stamp Duties") in an explicit attempt to maintain a protective barrier. Further, items were being added to list of licence requirements up to 1987, including automobile parts, toys and games, some kinds of fish, and dairy products.

The second exercise in trade reform occurred in 1987. In that year, another large group of items was removed from the list of those requiring import licences, leaving only fruit and vegetables, nuts, oils and seeds, vehicles of all types, and their parts and accessories. The Jamaica Commodity Trading Company remained the sole importer or a reduced list of commodities, including fish, dairy products, raw cereals, and fats and oils.

The third phase occurred during 1990-91. The import licencing requirement was eliminated for a range of vegetables, peas, and roots, oils and fats, and products made from the aforementioned. At the same time, export licencing was lifted in relation to fruit, vegetables, plants, and coffee. In 1991, the remaining quantitative restrictions and licencing requirements for both imports and exports were removed, and the Jamaica Commodity Trading Company ceased to act as sole importer of any commodities. A new import tariff schedule was also issued with marginally lower tariffs on average, but significantly lower tariffs on some major imported items.

The fourth round took place with the publication of the tariff schedules of 1993 and 1995, which represented a substantial reduction in tariff levels, almost across the board. The tariff reductions 1993, 1995, 1998 have occurred under the Common External Tariff Agreement (*CET*) of the Caribbean Community (*Caricom*), a trading bloc consisting primarily of English-speaking countries of the Caribbean region. The CET specified a schedule for the reduction of external tariffs (that is, on commodities imported from outside the region). Beginning January 1, 1993, but before the end of 1994, import tariffs in the larger countries of the group should have been in the range of 5 to 35 percent; by the end of 1996, the upper limit was to be reduced to 30 percent; another five percentage point reduction was to take place by the end of 1997; and further reductions were to be specified after that.

Jamaica took advantage of the complexity of its import tariff structure to adhere to the letter of the agreement while violating its spirit. Commodities imported into Jamaica attract tax levies under various names – Customs Duty, Stamp Duty, General Consumption Tax, and Special Consumption Tax. While only the first two are applied differentially to imports and domestic production (and are therefore import tariffs in the strictest sense), the latter two legislatively apply to commodities whether produced domestically or imported, and are therefore not import tariffs. In some cases, however, such as automobiles, they are levied at rates well above average on commodities for which there is no domestic production capacity, and so may be *de facto* import tariffs.

While the customs tariff schedule by itself will understate the magnitude of the import tariff, the changes in that schedule may be used as an indicator of the rate at which the trade regime has been liberalized. Table 2 provides the average rate from a sample of 80 representative commodities from the customs tariff schedule. The average was also computed for all five thousand commodities in the full tariff schedule for three of the five years shown in the table, as a corroboration of the representativeness of the sample, and the magnitudes and changes were close matches. The table reveals that the average customs tariff, which was at 25 percent throughout the 1980s, declined to 22.1 percent in 1991, to 15.9 percent in 1993, to 14.0 percent in 1995, and finally to 11.8 percent at the end of 1998. The table also indicates the reduction in the dispersion of tariff rates.

Table 2
INDICATORS OF TRADE LIBERALIZATION

	Average Import Tariff (%)	Standard Deviation of Tariffs
1980	25.7	24.3
1981	25.0	20.7
1982	25.0	20.7
1983	25.0	20.7
1984	25.0	20.7
1985	25.0	20.7
1986	25.0	20.7
1987	25.0	20.7
1988	25.0	20.7
1989	25.0	20.7
1990	25.0	20.7
1991	22.1	16.8
1992	22.1	16.8
1993	15.9	13.4
1994	15.9	13.4
1995	14.0	13.4
1996	14.0	13.4
1997	14.0	13.4
1998	11.8	14.7

Source: Author's calculation, from data published in the proclamations, rules, and regulations of the parliament.
Note: Average and standard deviation are computed from a sample of 72 commodities.

Notwithstanding the dismantling of quantitative import restrictions throughout the 1980s, most trade liberalization has occurred in the 1990s. Moreover, with the modest nature of the early tariff reductions, it may be argued that substantive tariff reductions did not occur until the mid 1990s.

2. Domestic Financial Liberalization

During the 1970s and 1980s, the Jamaican economy was constrained by one of the more repressed financial sectors in the Caribbean. Interest rates on savings deposits and lending, as well as the terms of various types of credit transactions, were restricted. Quantitative credit controls were widely employed. And reserve ratios were repressively high.

After inheriting an already repressed financial sector from the Manley administration of the 1970s, the government of the 1980s set about increasing the restrictions on financial activity. In this regard 1984 was an active year. In that year, a ceiling on the issuance of private sector credit by commercial banks was established, and the cash reserve ratio on commercial bank deposits was raised five times, from 5 percent in January to 14 percent by the end of October. In 1985, commercial credit by commercial banks was frozen at its existing level, with only the government's development banks exempted. Credit offered by trust companies, merchant banks, and finance houses was also capped. Later in the year, the ceilings on credit for "productive" activities was lifted while that for "consumption" remained. The credit ceilings remained in force until 1987.

In 1986, the cash reserve ratio was raised from 15 to 20 percent. In addition to the cash reserve ratio, the Jamaica central bank uses the ratio of specified liquid assets to deposits as a means of credit control and of directing the lending portfolio of commercial banks. Between, 1986 and 1989, while the cash reserve ratio remained constant, the liquid assets ratio was lowered from 38 to 20 percent. During this period, there were several and frequent changes to the interest rates set by the central bank for savings deposits and prime lending. Quantitative credit ceilings were imposed again in December 1989.

The liberalization of the domestic capital market began in 1991. The use of quantitative credit restrictions, such as overall credit ceilings and selective credit restrictions, was discontinued. In addition, ceilings on savings deposit rates along with other restrictions on consumer credit were lifted. At the same time, however, financial intermediation was being restricted with the rise in the liquid assets ratio of commercial banks from 20 percent in 1989, to 33.5 percent in 1992, and then to 50 percent until 1995.

Indicators of domestic financial reform are presented in Table 3. The first four columns show both reserve and liquid assets ratios, along a weighted average of the two, as well as the actual reserve-deposit ratio that commercial banks maintained in response to these requirements. The weighted average and actual reserve-deposit ratios reveal that restrictions on bank portfolios were increased in two waves, the first during 1984 and the second during 1992-93. The increased restrictiveness in the early 1990s contrasts sharply with the loosening of restrictions suggested by the removal of deposit rate controls proxied and indexed in the column labeled "Control of Deposit Rates", which is a binary index with a zero value when deposit rates are restricted and a unit value whenever they were not.

Table 3
INDICATORS OF DOMESTIC FINANCIAL REFORM

	Required Reserve Ratio	Required Liquid Assets Ratio	Weighted Average of Ratios	Actual Reserve-Deposit Ratio	Control of Deposit Rates	Liquid Liabilities /GDP	Private Sector Credit /GDP
1980	5	36.0	23.00	8.1	0	0.27	0.13
1981	5	36.0	23.00	6.9	0	0.32	0.16
1982	5	36.0	23.00	6.5	0	0.38	0.20
1983	5	36.0	23.00	8.8	0	0.43	0.23
1984	14	40.0	34.00	20.0	0	0.41	0.20
1985	15	48.0	39.00	21.9	0	0.46	0.18
1986	20	38.0	39.00	21.2	0	0.48	0.19
1987	20	35.0	37.50	21.0	0	0.48	0.21
1988	20	20.0	30.00	22.0	0	0.56	0.23
1989	20	20.0	30.00	20.0	0	0.51	0.25
1990	20	27.5	33.75	20.4	0	0.48	0.23
1991	20	33.5	36.75	21.0	1	0.47	0.22
1992	23	33.5	39.75	28.1	1	0.51	0.16
1993	25	50.0	50.00	25.6	1	0.48	0.19
1994	25	50.0	50.00	27.1	1	0.49	0.18
1995	25	47.0	48.50	25.4	1	0.50	0.21
1996	25	47.0	48.50	25.4	1	0.46	0.23
1997	25	47.0	48.50	25.1	1	0.48	0.18
1998	25	47.0	48.50	21.4	1	0.44	0.14

Source: Statistical Digest, Bank of Jamaica, various issues.
Notes: "Reserve" and "Liquid Assets" ratios refers to those imposed on commercial banks; Average of Ratios" is the simple average of the reserve ratio and the liquid assets ratio; "Control of Deposit Rates" is binary variable with a value of zero whenever the central bank imposes restrictions on the interest rate that commercial banks may offer on ordinary savings deposits; "Liquid Liabilities" refers to the total liquid liabilities of the financial sector; "Private Sector Credit" is domestic credit to the private sector.

There was thus a contradiction between the deregulation of credit transactions and the disintermediation implied by the increase in reserve requirements. This contradiction arose because of the conflicting obligations. One obligation was the need to remove restrictive practices in the face of pressure from the multilateral institutions to liberalize. At the same time, the objective of stabilization was present, and therefore the need to absorb liquidity generated by monetized fiscal deficits. It is not surprising, then, in the presence of these contradictory influences, that there is little evidence of increased financial intermediation during the nineties. Table 3, showing ratios of both liquid liabilities of the banking system and private sector credit to GDP, confirms the absence of such an increase in the level of financial intermediation.

3. Opening of Capital Account

Exchange controls, implemented in 1974, remained in place throughout the 1980s. Commercial banks alone were authorized to trade in foreign exchange, and only in respect of transactions for which import licences had been granted. Private citizens could not legally trade in foreign exchange or hold foreign exchange denominated assets or liabilities. There were changes to the foreign exchange regime during the 1980s. In 1984, a managed auction was introduced for the allocation of foreign exchange. The auction was abandoned in 1989. Throughout the decade, however, highly restrictive exchange controls remained in place.

In January 1990, exporters became authorized to hold foreign exchange denominated accounts. This was less an act of liberalization than an attempt to benefit from the status quo. Because of the restrictiveness of the exchange controls, earners of foreign exchange were holding on to a portion of their earnings in any case, in cash and in illegal foreign accounts. The authorization of foreign exchange "retained" accounts was an attempt to channel some those *de facto* holdings into the banking system and therefore into the official foreign exchange market.

Genuine liberalization began in July of 1990 when commercial banks were empowered by the Bank of Jamaica by means of *delegated authority* issued under the *Exchange Control Act* to open foreign exchange accounts. Later in that year, the Bank of Jamaica ceased determining the official rate, and commercial banks were allowed to set their own buying and selling rates for the limited amount of foreign exchange trading which was authorized. At the same time, a surrender requirement equal to 25 percent of foreign exchange purchases was implemented, and raised to 50 percent by year end.

In September of 1991, the *Exchange Control (Removal of Restrictions) Order* was implemented, lifting exchange controls and permitting private individuals to buy foreign exchange from authorized dealers without the presentation of an import license or authority from the central bank. At this time, the foreign exchange surrender requirement was reduced to 40 percent. In 1992, the *Exchange Control Act* was repealed entirely, and foreign exchange dealers other than commercial banks were authorized.

But the liberalization of the foreign exchange market was less than complete. For much of 1992 and 1993, notwithstanding the authorization of market determined exchange rates, the central bank specified an indicative exchange rate to the commercial banks and put them under heavy moral suasion to adhere to that rate. As a result of this practice, the market more often than not failed to clear and importers had difficulty obtaining foreign exchange through the banking system. A parallel foreign exchange market continued to operate. This practice of indicative exchange rates was discontinued after 1993. Between 1992 and 1996, the surrender requirement was gradually reduced from 40 percent to 5 percent.

The premium extracted for the sale of foreign exchange on the parallel market is an indicator of the severity of the constraint imposed by exchange controls and of the rigor of its enforcement. Table 4 measures this black market premium, and reveals that it peaked in 1982 at 65 percent, and despite a relapse in 1989 to 28 percent, quickly disappeared after the discontinuation of the use of indicative exchange rates, reaching negligable proportions by 1993.

Table 4
EXCHANGE RATES

	Premium	Free Market	Official
1980	1.40	2.5	1.8
1981	1.48	2.6	1.8
1982	1.65	2.9	1.8
1983	1.09	3.6	3.3
1984	1.14	5.6	4.9
1985	1.19	6.5	5.5
1986	1.18	6.5	5.5
1987	1.18	6.5	5.5
1988	1.22	6.7	5.5
1989	1.28	8.3	6.5
1990	1.27	10.2	8.0
1991	1.07	23.0	21.5
1992	1.12	24.8	22.2
1993	1.02	33.0	32.5
1994	1.00	33.2	33.2
1995	1.00	39.6	39.6
1996	1.00	34.9	34.9
1997	1.00	36.3	36.3
1998	1.00	37.1	37.1

Source: Statistical Digest, Bank of Jamaica; World Currency Yearbook.

4. Privatizations

In 1980, the government of Jamaica had whole or partial ownership of enterprises in a range of industries, including tourism, telecommunications, food processing and distribution, banking, manufacturing, electronic media, agriculture, transportation, and construction. Sectorally, their largest presence was in tourism and banking. In the tourist sector in 1980, public ownership represented well over half the capacity of the large hotel market in Jamaica at that time. In the Banking sector the government owned the largest commercial bank – National Commercial Bank. In media, they owned only television station.

Jamaica's privatization programme was ostensibly launched in 1981 during the first full year of the new Seaga administration. As with other aspects of economic reform, the administration's pursuit was less than vigorous. In the launch year, two privatizations were executed, one for a food processing firm, the other for an airline catering company. Both were small enterprises, and the gross proceeds from the two privatizations was only US$1.7m. In the second year of the program, the government *acquired* an oil refinery from Exxon for US$55m. No further divestments occurred for five years, during which time the government also acquired a sugar estate, a shopping complex, and a rice farm (Stephens and Stephens, 1986). Therefore, after the first six years of "privatizations", the public sector owned substantially more productive capacity than it did at the start of the program.

Privatizations began in earnest only in 1986, as the administration reluctantly adhered to the requirements of World Bank Structural Adjustment loan agreements. In that year, there was whole or partial divestment of five publicly-owned enterprises. The most significant was the sale of 51 percent of the shares of the largest commercial bank – National Commercial Bank. Four further divestments followed in 1987, including 90 percent of the shares of a cement company and 19 percent of the shares of the telecommunications monopoly to Cable & Wireless International. The following year, 1988, only two acts of privatization occurred, including a further divestment of shares of the telecommunications company.

The divestment of publicly-owned productive capacity accelerated in 1989 with the change of administration. In the first year of that administration, twelve public enterprises were divested, including seven hotels. Whereas the number of whole or partial enterprises privatized averaged 1.6 from 1981 to 1988, between 1989 and 1996, that figure jumped to 6.6. In the later period, the average annual value of net privatizations was five times as large as in the earlier period. The major privatizations in the 1990s included large sugar and banana estates, two airlines, a steel producer, and the remainder of National Commercial Bank.

By the end of 1996, altogether, 66 privatizations occurred for accumulated proceeds of almost US$500 million. The aggregates reveal that, notwithstanding the frenetic pace of privatization between 1989 and 1996, at the end of that period, a substantial amount of productive capacity remained under public ownership, including the two international airports and a sea port, an oil refinery, bauxite mining companies, the power supply company, and the water utility. That is, more productive capacity remained in the hands of the government than had been privatized in the previous years 15 years.

During 1997 and 1998, there was a substantial reversal of the movement of publicly-owned enterprises to private ownership brought about, not by a deliberate abandonment of the principles of privatization, but as a result of expediency as part of the government's response to the banking crisis (detailed below). As the government sought to prevent the collapse of several financial sector institutions, by the end of 1998, it had taken at least partial ownership or effective control of all but one commercial bank, all but two insurance companies, along with several trust companies and merchant banks. As part of the equity holdings of failed financial institutions, the government has acquired ownership of several non-banking enterprises in agriculture and tourism.

Table 5 tracks the privatization efforts from 1980 to 1998. The index of privatization, which reflects the accumulated proceeds of privatization, falls initially in 1982, remains flat until 1986, from where it rises gradually to 1989, after which it rises substantially before tailing off towards 1995. Following the acquisitions of the banking crisis, the index falls in 1997 and 1998.

Table 5
PRIVATIZATION OF PUBLIC ENTERPRISES

	Index	Value of Privatizations (US$m.)		Number of Privatizations	
		Accumulated	Change	Accumulated	Change
1980	0.03	0.0	0.0	0	0
1981	0.03	1.7	1.7	2	2
1982	0.00	-53.3	-55.0	1	-1
1983	0.00	-53.3	0.0	1	0
1984	0.00	-53.3	0.0	1	0
1985	0.00	-53.3	0.0	1	0
1986	0.02	-23.6	29.7	7	6
1987	0.06	63.8	87.4	11	4
1988	0.07	81.0	17.3	13	2
1989	0.13	198.9	117.9	25	12
1990	0.16	256.3	57.4	28	3
1991	0.18	289.2	32.9	37	9
1992	0.20	321.6	32.4	43	6
1993	0.22	370.3	48.7	51	8
1994	0.25	430.0	59.8	60	9
1995	0.25	430.6	0.5	63	3
1996	0.25	431.0	0.4	66	3
1997	0.16	243.8	-187.2	60	-6
1998	0.14	219.5	-24.3	58	-2

Source: Author's calculations based on data provided by National Investment Bank of Jamaica, Ministry of Finance, and the Financial Sector Adjustment Company.
Notes: "Index" is a linear transformation of "Accumulated" value of privatizations, mapped to a 0-1 interval; "Value of Privatizations", which is net of acquisitions, is expressed millions of nominal U.S. dollars; Negative values appear in this table whenever acquisitions exceed divestments; "Number of Privatizations" is a count of each act of privatization, even where an enterprise is only partially divested.

5. Tax Reforms

At the beginning of the 1980s, Jamaica's tax structure, with respect to both direct and indirect taxes, consisted of a complicated web of levies applied at high marginal rates. Income taxes rates had been raised on five separate occasions during the 1970s. By 1980, taxes on personal and corporate income were levied on the basis of six tax brackets above a zero tax threshold. The highest bracket attracted a tax of 80 percent on marginal income. By 1985 the highest bracket had been reduced to 57.5 percent. There were also some 16 tax credits and a large number of allowances (Alleyne, 1998). Corporate income was taxed on a differentiated scale depending on whether the enterprise was in the agricultural sector (and taxed at a rate of 25 percent) or not (and taxed at a rate of 35 percent in the first instance, with an additional "profits tax" of 10 percent).

Beginning in 1986, there were several reforms of the tax structure. Personal income taxes were greatly simplified in that year with the introduction of a single tax rate of 33 1/3 percent above the zero tax threshold. The corporate income tax structure was also simplified. The agricultural/non-agricultural differentiation was abolished, as was the additional profits tax, and all corporate income was taxed at a uniform rate of 33 1/3 percent. In 1992, the personal income tax rate was reduced to 25 percent.

The changes to the income tax code are partially reflected in Table 6, which shows the highest marginal tax rates that have been applied to each type of income. The two columns reflect the fall in marginal tax rates, dramatic in the case of personal income, that occurred between 1981 and 1992.

Table 6
MAXIMUM MARGINAL INCOME TAX RATE

	Personal	**Corporate**
1980	0.80	0.45
1981	0.58	0.45
1982	0.58	0.45
1983	0.58	0.45
1984	0.58	0.45
1985	0.58	0.45
1986	0.33	0.45
1987	0.33	0.33
1988	0.33	0.33
1989	0.33	0.33
1990	0.33	0.33
1991	0.33	0.33
1992	0.33	0.33
1993	0.25	0.33
1994	0.25	0.33
1995	0.25	0.33
1996	0.25	0.33
1997	0.25	0.33
1998	0.25	0.33

Source: Revenue Board, Government of Jamaica.

Indirect taxes were equally complicated. *Excise* duties were levied at rates between 2.5 and 17.5 percent; *consumption duty* ranged from 5 to 27.5 percent; a few commodities attracted a *retail sales tax* of 10 percent, while others attracted *stamp duties* and *additional stamp duties*; and there were taxes levied on specified industries, such as the *telephone service tax*, the *entertainment tax*, and the *hotel accommodation tax*. None of the above taxes were universally applied.

In October 1991, this complicated structure of indirect taxes was replaced by a single *General Consumption Tax*, applied at an almost uniform rate of 10 percent on domestic production and imported commodities alike. A few commodities, such as drugs and some basic food items, and some purchasers, such as educational institutions, were exempt from the tax. The *GCT* was later raised to 12.5 percent (1993), and still later to 15 percent (1995).

The GCT revenue to GDP ratio, expressed as a fraction of the GCT rate, is an indicator of the efficiency of tax collection. This indicator is meaningful only since 1992, which is the first full year in which the GCT was levied. The data for 1992 to 1998 is presented in Table 7, which shows that the efficiency of collection declined consistently after 1994. This, however, may not be a good indicator of the change in the efficiency of tax collection during the period of economic reform for two reasons. First, the broad-based GCT replaced a plethora of industry taxes and excise taxes and, partially, the income tax as well which was reduced at the same time as the GCT was introduced. The taxes removed and reduced were easier to avoid and evade than the GCT, so the shift to an expenditure tax was itself an exercise in increased efficiency of collection. Second, increased evasion of the GCT evidenced in the index was motivated by the rise in the GCT rate itself over the period. We may therefore not generalize that the fall in the index reflect decreased efficiency of collection *in general*.

Table 7
EFFICIENCY OF TAX COLLECTION

	GCT Tax Rate	GCT Revenue /GDP /Tax Rate
1992	0.1	0.32
1993	0.125	0.33
1994	0.125	0.35
1995	0.15	0.30
1996	0.15	0.29
1997	0.15	0.28
1998	0.15	0.27

Source: Author's calculations from data in Social and Economic Survey, Planning Institute of Jamaica.

These reforms had a positive effect on tax collection. The ratio of tax revenue to GDP was only 21 percent in 1985, the year prior to the reform of the income tax structure. By the end of the decade, the tax collections had risen to 24 percent of GDP. Following the shift from income to expenditure taxes in 1991, the tax collection ratio continued to rise, eventually reaching a peak of 27 percent from 1993 to 1995 before the economic recession began.

Tax reform was one of the more active areas of economic reform. The changes in the tax structure were substantial in scope and large in magnitude. They changed in a fundamental way the incidence of taxation, in particular with the shift from industry taxes and formal sector income taxes to the *general consumption tax*, which broadened the tax net considerably.

6. Labor Market Reforms

The area of least reform was that of the labor market. During the 1970s, a plethora of measures were implemented which encased in legislation benefits and rights of workers and imposed their attendant costs and labor market inefficiencies. Amongst these were paid maternity leave, dismissal costs, an obligation on the part of firms to recognize and negotiate with unions, and the power of courts to compel re-employment (not merely pay damages) in wrongful termination cases. Minimum wages were also in place by the end of the 1970s. Finally, individual income tax rates, discussed above, were punitively high at the upper end.

The simplification and reduction of income taxes described in detail above are the primary economic policy change that has affected the labor market. In addition to reducing the cost of employment, the income tax reduction has lowered the cost differential between formal and informal sector labor. However, the legislative framework that governs labor relations remained in place throughout the period up to 1998. Labor dismissal costs, though low by Latin American standards, were actually increased during the period of economic "reform". Up to 1991, all workers were legally entitled to only two weeks notice or equivalent pay in lieu of notice. In 1991, the dismissal cost for workers with more than ten years experience with the company was increased to three weeks.

Minimum wages were never an important determinant in the labor market in Jamaica. Minimum wages were introduced in 1976. However, except for the year of its introduction and only occasionally since then, the minimum wage has been to too low to be a binding constraint upon the allocation of labor. Table 8 evidences this claim by showing, not only the nominal value of the minimum wage, but its ratio to average formal sector wages – the labor market segment in which minimum wages are potentially relevant. The table reveals that that ratio rose above 20 percent on only two occasions since 1990.

Table 8
WAGES

	Ratio of Minimum to Average	Index of Real Average Wage
1980	0.19	n/a
1981	0.21	n/a
1982	0.20	n/a
1983	0.17	n/a
1984	0.13	n/a
1985	0.16	n/a
1986	0.19	94.4
1987	0.16	100.9
1988	0.14	102.7
1989	0.21	100.0
1990	0.18	91.3
1991	0.17	65.2
1992	0.14	68.8
1993	0.17	83.6
1994	0.12	99.0
1995	0.15	95.9
1996	0.19	97.4
1997	0.15	107.4
1998	0.14	110.4

Sources: (1) Ministry of Labor, (2) Employment, Hours, and Earnings in Large Establishments, Statistical Institute of Jamaica.

Labor market reform was therefore minimal. Apart from the effects of income tax changes on the labor market, by 1998 the labor market remained substantially unreformed. A substantial tax burden remained, labor obligations upon employers were substantial, and thus the incentives to shift employment to the informal sector were great.

IV. MACROECONOMIC POLICIES

The economic environment for growth and development is governed not only by structural economic reforms but also by the state of stabilization policy, which is determined by the fiscal, monetary, and exchange rate policy stances of the government. In 1980, Jamaica was at the end of a decade of moderate monetary/fiscal instability.

1. Fiscal Policy

Fiscal policy shifted radically in the 1980s and again in the 1990s. In 1980, government expenditure amounted to 35 percent of GDP, while revenue was only 20 percent, leaving a fiscal deficit that was a massive 15 percent of GDP (see Table 9). Even the primary deficit was as much as 9 percent. During the first five years of the decade, there was an impressive attempt at fiscal rectitude with public expenditure contracting to 30 percent of GDP by 1986 and revenue rising to 28 percent of GDP. The large deficits in the early part of the decade were financed by massive external borrowing, however, so the external debt grew from 23 percent of GDP in 1980 to 77 percent in 1984.

Table 9
FISCAL DATA

	Total Gov't Expend. /GDP	Gov't Expend. (excl. Interest) /GDP	Gov't Rev. /GDP	Fiscal Surplus /GDP	Primary Surplus /GDP	Internal Debt /GDP	External Debt /GDP
1980	0.354	0.295	0.204	-0.150	-0.091	0.364	0.228
1981	0.315	0.255	0.213	-0.102	-0.042	0.441	0.267
1982	0.331	0.267	0.221	-0.110	-0.045	0.452	0.328
1983	0.306	0.217	0.216	-0.091	-0.001	0.490	0.603
1984	0.290	0.193	0.231	-0.059	0.038	0.530	0.773
1985	0.294	0.195	0.244	-0.049	0.050	0.513	0.768
1986	0.295	0.196	0.277	-0.019	0.081	0.407	0.768
1987	0.270	0.200	0.289	0.020	0.089	0.452	0.749
1988	0.321	0.233	0.284	-0.037	0.051	0.461	0.692
1989	0.311	0.218	0.327	0.016	0.109	0.383	0.692
1990	0.284	0.194	0.305	0.022	0.112	0.307	0.696
1991	0.284	0.196	0.308	0.024	0.112	0.216	1.171
1992	0.244	0.157	0.266	0.022	0.109	0.241	0.690
1993	0.281	0.191	0.314	0.033	0.123	0.223	0.755
1994	0.296	0.192	0.308	0.013	0.117	0.290	0.639
1995	0.298	0.201	0.319	0.022	0.118	0.268	0.579
1996	0.354	0.230	0.287	-0.067	0.058	0.354	0.420
1997	0.360	0.258	0.277	-0.083	0.019	0.422	0.423
1998	0.362	0.225	0.293	-0.069	0.067	0.478	0.428

Source: (1) Economic and Social Survey, Jamaica, Planning Institute of Jamaica, various years. (2) Statistical Digest, Bank of Jamaica, various issues. (3) Ministry of Finance.

For the remainder of the 1980s, fiscal policy remained largely unchanged but for an improvement in revenue, probably related to tax reform in 1986. Public expenditure fluctuated around 30 percent of GDP, with revenue rising from 28 percent to 32 percent. There was a need for exceptional expenditure in 1988 and 1989 following a natural disaster near to the end of 1988, but expenditure returned to ordinary levels by 1990.

By 1989, the fiscal balance was in surplus, equivalent to 2 percent of GDP, at which level it remained until 1996. Debt servicing weighed heavily on the exchequer, so the primary surplus was much larger at around 12 percent of GDP. At the end of the period, from 1996 to 1998, the fiscal situation worsened dramatically. Expenditure's GDP ratio jumped by 5 percentage points in 1996, as revenue shrank at the start of a severe recession, so the fiscal balance sank to a deficit of 7 percent of GDP.

A large part of the fiscal problem after 1996 was due to a large domestic debt. The inflation episode of 1991 had deflated substantially the real value of the domestic debt, but the treasury subsequently engaged in a policy of switching the national debt portfolio from international to domestic creditors during the ensuing years. By 1995, the domestic debt was almost up to its pre-inflation level and fiscal deficits after that year were financed by new domestic borrowing. Since domestic interest rates were high (see *Monetary Policy* below), the debt servicing obligations imposed were great. The internal debt/GDP ratio rose from 27 to 48 percent between 1995 and 1998 while the external debt, which had been approximately 70 percent in the early part of the decade, was reduced to 43 percent by 1998 (Table 9).

In summary, the fiscal accounts improved significantly in the early 1980s. Fiscal policy remained steady and positive from 1987 to 1995, but after that deteriorated suddenly and significantly.

2. Monetary Policy

For most of the last three decades, Jamaica has been a moderate inflation economy with an average inflation rate of 23 percent over that time. As in most of Latin America, inflation has been volatile. Monetary policy has traditionally been subservient to the demands of fiscal policy. Throughout the 1980s, monetary policy continued to play such an accommodative role. Consequently, monetary growth rates and real interest rates fluctuated depending on fiscal exigencies, as is evidenced in Table 10.

Generally, monetary policy was accommodative and inflationary. From 1980 to 1995, the average annual growth rate of the monetary base was 35 percent, while that of M1 was 30 percent. There were large increases in monetary aggregates in 1988 as monetary policy had to oblige the fiscal requirements of the hurricane in that year, and again during 1991-92 as monetary policy accommodated the sharp depreciations that followed exchange liberalization.

But an orthodox disinflation policy was evidenced from as early as 1993 and pursued aggressively from 1995. So by 1998, the growth rate of the monetary aggregates had fallen considerably and interest rates were high. M1 grew by 95 percent during the year of the inflation spike, and averaged a 30 percent rate of increase from 1993 to 1995. By 1997-1998 however, its average growth was only 4.25 percent per year. In the presence of a growing fiscal deficit and no disinflation credibility, interest rates rose. In 1996, real interest rates, which had been negative in the early 1990s, subsequently rose to as high as 23 percent. As a consequence of such a restrictive monetary policy, the inflation rate fell below 20 percent in 1996 and was down to single digits by 1998.

Table 10
MONETARY POLICY

	Inflation	Money Base Growth Rate	M1 Growth Rate	Real Avg. Lending Rate (%)
1980	29.0	40.9	13.9	-9.6
1981	4.6	-4.1	8.1	11.1
1982	6.5	-11.5	13.1	9.3
1983	16.6	71.8	21.6	0.3
1984	31.2	91.8	23.7	-8.5
1985	23.1	35.0	15.2	5.0
1986	10.7	18.6	40.8	13.4
1987	8.4	19.7	5.2	15.5
1988	8.8	37.1	53.0	14.8
1989	17.2	22.7	-8.5	9.3
1990	29.8	15.6	27.4	1.4
1991	80.2	28.2	94.7	-25.6
1992	40.2	88.5	71.3	4.2
1993	30.1	44.6	26.2	15.0
1994	26.9	34.3	25.7	14.9
1995	25.5	29.7	38.0	18.4
1996	15.8	7.1	14.5	22.7
1997	9.2	11.8	2.7	23.6
1998	7.9	22.1	5.8	23.3

Source: Statistical Digest, Bank of Jamaica.
Notes: "Inflation" is measured point-to-point at end of year, and is based on the CPI; "Real Average Lending Rate" refers to the weighted average interest rate charged by commercial banks on all types of credit, deflated by the current year CPI.

3. Exchange Rate Policy

During the 1980s under the Seaga administration, exchange rate policy was separated from monetary policy by the exchange controls that remained in effect and by quantitative allocation of scarce hard currency. Thus, the nominal exchange remained stable at J$5.5 to the U.S. dollar from 1985 until 1989 (Table 11), under a carefully managed and manipulated auction system.

Upon the removal of exchange controls in 1991, the exchange rate was managed by moral suasion. There was a sharp jump in the exchange rate from J$8.0 to J$21.5 and then to J$28 in the immediate aftermath of the liberalization of the capital account. Much of that movement represents speculative overshooting of the exchange rate along with the uncertainty of the new exchange ragtime. The *de facto* policy regime that emerged for the period 1992-93 was one of central bank pressure on the commercial banks to adhere to the indicative exchange rate issued by the central bank. During this time, notwithstanding the "liberalization" of the foreign exchange market, it was common for importers and other users of hard currency to be unable to make purchases through the commercial banks, having to resort instead to a parallel market. The exchange rate data shown in Table 4 reveals that at the end of 1992, foreign exchange sold on the parallel market commanded a premium of 12 percent over the central bank's indicative rate.

Table 11
EXCHANGE RATES

	Nominal Exch. Rate	Real Exch. Rate	Real Depre-ciation
1980	1.8	60	-12.8
1981	1.8	63	4.1
1982	1.8	61	-2.5
1983	3.3	100	63.8
1984	4.9	120	19.1
1985	5.5	112	-6.2
1986	5.5	102	-8.7
1987	5.5	99	-3.3
1988	5.5	95	-4.4
1989	6.5	100	5.6
1990	8.0	101	1.4
1991	21.5	155	52.9
1992	22.2	118	-24.2
1993	32.5	136	15.6
1994	33.2	112	-17.3
1995	39.6	110	-2.5
1996	34.9	86	-21.5
1997	36.3	84	-2.9
1998	37.1	80	-3.9

Source: Statistical Digest, Bank of Jamaica.
Notes: "Real Exchange Rate" is an index measured against the United States dollar.

Between 1993 to 1995, Jamaica had a freely floating exchange rate that followed the lead of monetary policy. During this period, interest rates reflected increased inflationary uncertainty following the episode of 90 percent annual inflation in 1991 and also reflected the rise in the internal debt from 23 percent of GDP to 29 percent. Attractive interest rates stimulated capital inflows that generated and sustained an overvaluation of the exchange rate. In 1994, the Jamaica currency appreciated in real terms by 17.2 percent, and by a further 2.5 percent in 1995.

After 1995, the policy regime was switched to a managed float with heavy and frequent central bank intervention in the market that at times appeared to be exchange rate targeting. The temptation to actively manage the exchange rate reflected more than economic considerations. As generally happens in countries with contentious histories of relationships with the IMF, the exchange rate assumed a political significance out of proportion to its economic role. That is, a devaluation was viewed as an index of governmental failure. As a result, the government was willing to commit large resources towards the defence of an overvalued exchange rate.

In the nexus of fiscal, monetary, and exchange rate policy, the deterministic element changed over the period of analysis. Coming from the 1970s, fiscal policy was dominant, driven by the use of the fiscal budget to promote social objectives, while monetary policy served to accommodate it with whatever consequences there were for the exchange rate. In the 1980s, the approach was more pragmatic, with policy-making shifting between a focus on the exchange rate and on the fiscal budget. The 1990s witnessed the rise in the importance of monetary policy. At the same time, there was a disconnection of fiscal policy from monetary with the monetizing of fiscal deficits being eschewed as a means of financing. This combination of fiscal expansiveness in the presence of monetary conservatism are important in understanding the failure of the Jamaican economy to respond to the signals of economic reform.

V. SOCIAL POLICY

The level of public expenditure on social services is shown in Table 12. Real per capita social expenditure declined between 1990 and 1993, but then increased in 1996 to a level greater than that of 1990. Public social expenditure as a percentage of GDP decreased by one percentage point during the period under review. If this measure is seen as an indicator of the economic priority of social services, it signifies a "moderate" priority (as defined in ECLAC, 1997), but one that is declining in the hierarchy of priorities. Therefore, while the percentage declined, indicating the focus of the government on the macroeconomic issues above, the *level* of spending compares favorably with other Latin American and Caribbean Countries.

Table 12
PUBLIC EXPENDITURE ON SOCIAL SERVICES

	Constant J$ Dollar Index	Constant J$ Dollar, per capita Index	Share of Total Public Expend.	Share of GDP
1980	140.0	155.1	0.29	0.10
1981	156.1	169.0	0.36	0.11
1982	159.6	170.0	0.36	0.12
1983	154.9	162.1	0.38	0.12
1984	112.6	116.3	0.31	0.09
1985	99.7	101.9	0.30	0.09
1986	78.2	79.3	0.23	0.07
1987	86.0	87.1	0.27	0.07
1988	137.2	138.9	0.36	0.12
1989	100.0	100.0	0.26	0.08
1990	97.0	96.2	0.27	0.08
1991	114.1	112.2	0.32	0.09
1992	88.8	86.4	0.29	0.07
1993	126.6	122.2	0.35	0.10
1994	121.0	115.5	0.33	0.10
1995	116.2	109.7	0.31	0.09
1996	129.2	120.5	0.30	0.11
1997	149.3	138.1	0.34	0.12
1998	137.2	125.7	0.32	0.11

Source: Economic and Social Survey Jamaica, various issues, Planning Institute of Jamaica.

Real per capita spending on social services exhibits much volatility in the fiscal budget. This may be due to the large relative impact of projects within the total social budget. From

Table 12 reveals that, once per capita social spending declined in 1984, it remained approximately 25 percent below those earlier levels up to the end of our period of analysis. ECLAC (1997) defines per capita spending on social services of between US$70 and US$200 as "moderate". Jamaica therefore falls in the moderate range.

The allocation of expenditures amongst the various social services reveals the implicit or explicit prioritization. The share allocated to each social service is shown in Table 13. Within the social services, the allocation to education increased by 7 percentage points from 46.8 to 53.8 percent. The allocation to health showed a corresponding decrease, declining from 26 to 22.8 percent of the social services budget. The allocation to the category "other social services" increased dramatically. These include social security, support for community groups and NGOs, as well as services that cater to children, such as day care, foster care and the family court. The Adoption Board and activities surrounding children in especially difficult circumstances, such as street children, children with disabilities, and children in extreme poverty also fall under this budget line. Much of the increased expenditure reflects the emphasis of donor communities, such as UNICEF and UNDP, in these areas.

Table 13
EXPENDITURE ON SOCIAL SERVICES, RATIO TO TOTAL SOCIAL EXPENDITURE

	Education	Health	Other
1980	0.48	0.23	0.29
1981	0.46	0.23	0.31
1982	0.47	0.22	0.31
1983	0.48	0.23	0.28
1984	0.51	0.26	0.22
1985	0.52	0.29	0.19
1986	0.58	0.26	0.16
1987	0.53	0.28	0.18
1988	0.44	0.21	0.34
1989	0.52	0.27	0.20
1990	0.53	0.29	0.18
1991	0.51	0.27	0.22
1992	0.49	0.31	0.20
1993	0.51	0.28	0.20
1994	0.45	0.30	0.25
1995	0.53	0.23	0.24
1996	0.54	0.26	0.20
1997	0.58	0.24	0.17
1998	0.59	0.25	0.16

Source: Economic and Social Survey Jamaica various issues, Planning Institute of Jamaica.
Note: "Other" included social security. Rows sum to 1.0, except for rounding errors.

1. Education

Table 14 looks at the allocation to pre-primary, primary, secondary and tertiary education as a percentage of the education budget. The table shows that primary education is allocated almost a third of the education budget, in 1996 and 1993, up from 29 percent in 1990. The allocation to tertiary education has declined from 19 to 17 percent of the budget between 1990 and 1996.

Table 14
EDUCATION SECTOR SHARES OF TOTAL EDUCATION BUDGET

	1990	1993	1996
Pre-Primary Education	0.017	0.026	0.026
Primary Education	0.289	0.324	0.320
Secondary Education	0.264	0.302	0.273
Tech./Voc. Education	0.038	0.042	0.039
Tertiary Education	0.190	0.159	0.177

Source: Ministry of Education.

One fifth of the education budget is being used on tertiary education, which does not benefit the lowest quintile. Less than 5 percent of the population benefits directly from tertiary education, and this is predominantly in the upper quintiles (46 percent from the richest quintile versus 3.3 percent from the poorest quintile).[5] The relatively high allocation to tertiary education at the expense of primary and first cycle secondary represents a failure to use educational provision as a compensatory mechanism of social equity. All of those in the highest quintile move from the primary level to the secondary level versus less than 80 percent of those in the poorest quintile. 50 percent of those in the poorest quintile complete only first cycle secondary. That is, children in the poorest quintile complete their education by age 14, whereas only 20 percent of the upper quintile stop their education at age 14. Most complete secondary education and continue to tertiary level education. This is outcome ensures the intergenerational transmission of poverty (Urrutia, 1999).

2. Health

The budgetary allocations to the health sector also have implications for social equity. An important part of health maintenance is access to and utilization of health facilities, where access is both physical and economic. The government has as its philosophy the intention to provide universal access to health care, but the ways in which the government funds are allocated has implications for equity in health care and health outcomes.

Jamaica has a system of health care delivery organized around the *Primary Health Care* approach, where primary health care is the first point of contact with the health system and involves mainly control of communicable diseases, and preventive health care. Secondary and Tertiary health care occur in hospitals through a referral system, and cover such health conditions that require surgery, or other forms of specialized care. The system has produced favorable health outcomes.

Table 15 shows that the percentage of the budget allocated to primary health care as a percentage of the total health budget is declining. But more importantly, the allocation to secondary and tertiary care is more than 50 percent of the total health budget. As was the case with education, the upper quintiles benefit disproportionately from subsidies in secondary and tertiary health care, as these quintiles choose to access their primary health care from private physicians but use the public faculties for inpatient care.

Table 15
HEALTH SECTOR SHARES OF TOTAL HEALTH BUDGET

	1990	1993	1996
Executive Director & Administration	0.071	0.022	0.053
Training	0.018	0.017	0.018
Primary Health Care	0.205	0.157	0.170
Secondary/Tertiary Health Care	0.589	0.512	0.580
Health Services Support	0.117	0.028	0.034

Source: Ministry of Health

During the period, the Ministry of Health had as its mission to promote and safeguard the health of the Jamaican people through the provision and monitoring of preventive, curative, and rehabilitative services, in a cost-effective way. In keeping with the government's expressed "partnership approach", the ministry forged closer links with the private sector, NGOs, community-based organizations, and international donor and lending agencies. The main thrust of activities centered on the health sector reform programs where emphasis was on decentralization; quality assurance; human resource development; and the national health insurance.

The Ministry of Health under the government's structural adjustment programs itself underwent reform. The strategies included decentralization, with the formation of regional boards with autonomy for the region; the Quality Assurance Programme for managerial training of both private and public health services personnel; Human Resource Development Program designed to stem the flow of personnel from the health sector; and the introduction of cost sharing strategies, mostly in the form of user fees.

While these strategies are designed to improve revenue generation, the income so generated forms less than 10 percent of the recurrent budget of the health care institutions, and so are of limited success on that measure. Also, such a strategy does present a barrier for some to access care because of the cost. Inequities were also introduced as public sector reform and economic crises often compelled cost cutting exercises, which resulted in reduced delivery of services (IDB/PAHO/WHO 1996).

VI. POLICY CONSISTENCY

From the above descriptions of economic reform, inconsistency and inappropriate sequencing are fair descriptions of the economic reform process in Jamaica. The various aspects of reform were not carried out at the same time, and with an appreciation of the need for policy coherence.

There was little economic reform in the early 1980s, save for the contraction in the size of the government, if that is classified as a part of economic reform, and the replacement of some quantitative import restrictions with high tariffs. Two aspects of economic reform were implemented beginning in 1986 – tax reform and privatization. The simplification of the income tax code, the reduction of income taxes, and the switch from income to expenditure taxes were accomplished in two phases in 1986 and 1991. As observed above, the privatization of publicly-owned enterprises, an intention from 1981, was implemented modestly in 1986.

All other aspects of structural adjustment were phenomena of the 1990s. The liberalization of international capital flows occurred between 1990 and 1994. The liberalization of international trade in goods and services, while obscured by some trade regime changes during the 1980s, was effected largely by the tariff schedules implemented in 1991 and 1995. Furthermore, the privatization program was accelerated between 1989 and 1994.

The inconsistency in the reform and policy environment was apparent in three areas. Firstly, none of the above was accompanied by an attempt to increase the flexibility of labor markets. Labor legislation remained oppressive and cumbersome throughout the entire period. Secondly, some elements of the economic policy framework were contradictionary in themselves. In the 1980s, the financial sector was repressed by means of quantitative credit restrictions and interest rate controls. In the 1990s, all such had been abandoned and replaced by the use of orthodox instruments of monetary control such as open market operations and reserve ratios. However, reserve ratios were moved to levels that were much higher than prudentially necessary.[6] Reserve ratios were sufficiently high to constrain the sector from performing the amount of financial intermediation that would otherwise have obtained. So the effect of the abandonment of credit and interest rate controls was contradicted by high reserve ratios. It is for this reason that we observe in Table 3 that the indicators of the quantity of financial intermediation did not change significantly over the period, despite the appearance of reform in the management of the financial sector.

Finally but most importantly, the efficacy of the structural reforms, implemented mostly in the early 1990s, were compromised by stabilization policy and its immediate aftermath. Contractionary monetary policy and high real interest rates in the period 1993 to 1998 hampered economic activity and discouraged any potential investment response to structural reforms. As a part of the stabilization outcome, the appreciation of the Jamaican dollar as capital inflows responded to high interest rates made it difficult for exports to expand. In any case, the contractionary policy depressed the economy at precisely the time it ought to have been adjusting structurally.

Firms in all sectors were faced simultaneously with loss of their protected markets, high cost of capital, and increased import competition. Under these circumstances, it would have been difficult to find the capital necessary to move into new sectors opened up by the liberal trade and payments regime.

Therefore, the various elements of economic reform were not implemented consistently and coherently. Jamaica, it turns out, may have been an early adopter of economic reform, but in the end is a "late reformer", or at the very least, must be described as a protracted reformer, with reform dragging out over at least an 18-year period. This puts Jamaica in rather stark contrast to the true early reformers such as Chile, and the "shock" reformers such as Bolivia and Peru.

VII. STAGNATION AND CRISIS IN JAMAICA

The Jamaican economy has been one of the worst performers in the Latin American and Caribbean region in the 1990s. The average rate of economic growth from 1990 to 1998 was 0.7 percent. Certainly, its reform record of lateness and inconsistency, discussed above, has been a contributory factor to this poor performance. But this reform record is not unique to Jamaica and alone cannot explain its macroeconomic record.

A major contributor to economic stagnation has been the decline of the economic and social infrastructure, a process that began in the late 1970s under the pressure of fiscal constraints and has continued right up to the present. Initially, the fiscal pressures derived from economic contraction in the 1970s and early 1980s. Thereafter, it came from increasingly voracious debt obligations. In 1980, at a time when debt service amounted to a mere 22 percent of total public outlays (expenditure plus amortization), public investment accounted for 33 percent (Table 16). By 1998, debt service consumed 62 percent, and as a consequence, investment's share had shrunk to 7 percent.

Table 16
EXPENDITURE SHARES OF TOTAL PUBLIC OUTLAYS

	Programs, Wages, & Salaries	Public Investment	Interest	Amortization
1980	0.45	0.33	0.16	0.07
1981	0.49	0.26	0.18	0.07
1982	0.50	0.25	0.18	0.06
1983	0.48	0.10	0.24	0.18
1984	0.48	0.12	0.30	0.11
1985	0.43	0.13	0.29	0.15
1986	0.38	0.17	0.28	0.17
1987	0.42	0.20	0.22	0.16
1988	0.39	0.21	0.23	0.18
1989	0.39	0.18	0.24	0.19
1990	0.41	0.16	0.26	0.17
1991	0.37	0.16	0.24	0.23
1992	0.35	0.11	0.25	0.29
1993	0.42	0.15	0.27	0.17
1994	0.32	0.14	0.25	0.30
1995	0.38	0.15	0.25	0.21
1996	0.36	0.13	0.27	0.24
1997	0.41	0.11	0.21	0.27
1998	0.40	0.05	0.27	0.27

Source: Economic and Social Survey, various issues, Planning Institute of Jamaica.
Notes: Rows sum to 1.0, except for rounding errors.

From the middle of the 1970s and continuing through the 1980s, almost every element of the physical economic infrastructure failed to expand at a rate commensurate with the needs of a modern economy. The quantity and quality of the road network is poor. The major artery linking the two major cities of Kingston and Montego Bay consists of single lane in each direction (and at one point a single lane for both directions). The water supply is inadequate and unreliable. It so poor that, during the 1990s, even the capital city had water lock offs for most of the day at least half of the year, during most years. The telecommunications infrastructure saw vast improvement with a burst of investment following privatization to Cable & Wireless, but in 1995 mean waiting for a new land line was still as high as 4.1 years, reflecting that that infrastructure still had not reached islandwide.

At the same time, the social infrastructure declined commensurately. The quantity and quality of the educational and health infrastructure in Jamaica have improved appreciably since the early 1970s. For example, in 1974 there were 804 primary schools for a population of 2.0m. In 1996, the same number of schools were serving a population of 2.5m. Similarly, in 1974 there was a docter per 4,444 persons in the public service, but by 1995 this ratio had fallen to one per 6,043. This has produced an increasing disjuncture between the human resource needs of economic growth and the capacity of the labor force.

In addition to its reform record and inadequate economic and social infrastructure, two internal shocks contributed to the poor growth performance of the Jamaican economy. The first was a sudden spike in the inflation rate in 1991 along with the subsequent stabilization efforts. The second shock was a banking crisis. Both are examined in turn.

1. Inflation and Stabilization

Throughout the 1950s and 1960s, Jamaica, like the rest of the world at that time, was what we would now call a low-inflation economy, with the rate of inflation always in single digits. However, from 1973 to 1998, the average inflation rate in Jamaica was 22.2 percent, still moderate by the standards of Latin America and the Caribbean. Up to 1991, inflation exceeded 30 percent on only two occasions – in 1978 the price level rose by 49.4 percent, and in 1984 it was 31.2 percent (Table 10).

Much of the outcome for poverty and income distribution in Jamaica in the aftermath of structural adjustment was conditioned by a spike in the rate of inflation to 80.2 percent in 1991. This occurred as a result of a dramatic depreciation of the local currency following the removal of capital controls in that year, accompanied by an accommodating monetary policy.

Between 1980 and 1990, the domestic currency depreciated at an annual average rate of 19 percent (Table 4). In the months immediately following exchange liberalization in September 1991, the value of the currency dropped a precipitous 167 percent. With an import/GDP ratio of near 50 percent, the change in the exchange rate was quickly reflected in domestic prices.

The extent to which prices adjusted in response to the currency depreciation and the long gradual nature of the reversion to low inflation was due to the presence of accommodating monetary policy both before and after the depreciation episode. In 1988, with the destruction wrought by a devastating hurricane, there was a substantial monetized fiscal deficit. In the fiscal years both preceding and following the hurricane, the fiscal accounts posted a surplus equivalent to 2 percent of GDP, but in 1988 there was a deficit of 4 percent of GDP. As a result of central bank accommodation of this deficit, base money grew by 37 percent in that year, while M1 expanded by 53 percent. By the time the exchange rate was freed two years later, there was therefore excess liquidity that depreciation-induced price increases could take advantage of. Moreover, the central bank was more than willing to accommodate the subsequent inflation, as the monetary base expanded by 28 and 89 percent in 1991 and 1992 respectively.

With monetary policy initially accommodating the price adjustment, along with a culture of backward-looking wage contracts, the inflation rate fell only gradually. But the inflation episode prompted an intention to achieve single-digit inflation and the shift to the orthodox, conservative monetary policy linked to base money targeting that was described above.

The inflationary episode, however, had severe consequences for the economy, in terms poverty and income distribution. The subsequent stabilization attempt had its own consequences for the level of economic activity in general and for the financial sector in particular, precipitating a banking crisis.

2. The Rise and Fall of the Financial Sector

The dominant internal shock that has determined the evolution of the Jamaican economy in the 1990s has been the banking crisis. In 1996, the insolvent positions of several banks and insurance companies became apparent, spurring the intervention of the government in the sector.

The beginning of the 1990s, as described above, was the period in which many of the restrictions that had repressed the operations of the financial sector were removed. The abandonment of the more repressive practices in the management of the financial sector (such as the removal of interest rate ceilings and the shift by the central bank from direct credit controls to the use of market instruments), along with the liberalization of the external capital account, created new opportunities to be exploited by financial intermediaries. These opportunities included trading in foreign exchange, in government securities, and in the burgeoning market for commercial paper.

The exploitation of these opportunities motivated an aggressive expansion in the size and scope of the financial sector in the early part of the 1990s. In the ten years to 1996, the total number of institutions in the non-insurance portion of the sector increased by 94 percent. The areas of most aggressive expansion were in merchant banking and building societies – the number of merchant banks tripled, while the number of building societies multiplied by a factor of six (Planning Institute of Jamaica, 1998). The expansion in the asset base of the sector was equally impressive. From 1986 to 1994, the peak of the financial sector expansion, the total real value of assets in the non-insurance financial sector expanded by 64 percent. Finally, while the real GDP grew by only 21 percent in the six years to 1994, the real product of the financial sector more than doubled. The data describe a sector emerging from repression.

At its zenith, however, the sector was in a vulnerable condition due to a combination of overexpansion, a skewed capital structure, and accumulated inefficiencies and bad practices that a permissive environment allowed. The first of these may have because of the usual dynamic of sectoral overexpansion in growing industries. Industry size tends to overshoot its equilibrium level during adjustments between equilibria. This argument suggests that even in the absence of shocks external to the sector precipitating a "banking crisis", a shake-out in the number of institutions was due in any case.

Of greater significance was the skewed capital structure that derived from perverse price signals. Many banks departed from their core traditional lending business to take equity positions in non-banking activities. They owned and operated enterprises outside of the financial sector, particularly in the tourist and agricultural sectors. The path of direct investment may have been chosen because of insufficient demand for the bank's capital as a result of the long poor performance of the economy in general. The effect of this investment shift was to heighten the banking sector's vulnerability to the fluctuations of the wider economy by reducing its ability to shrink its exposure in the short term.

Capital misallocation was evident also in the mismatched term structure of assets and liabilities. Two decades of volatile inflation and secular depreciation had created a reluctance on the part of the public to hold long-term instruments of any kind denominated in local currency. Both banks and, significantly, insurance companies therefore came to rely on short term instruments to raise capital. The capital was then invested long (including equity in non-traded companies), setting up a situation wherein the appearance an inverse yield curve would be damaging.

Finally, the usual accounting and management misdeeds that arise in a weak regulatory framework, common to banking crises everywhere, were present in Jamaica on the eve of the crisis. Connected lending was widespread and misclassification and obfuscation of bad debts was common. Where the rule of the regulator was lacking, the discipline of the marketplace did not fill the space. Decades of moderately high and volatile inflation were sufficient to allow such practices to go unpunished.

1994 was a year in which a number of factors that would have a detrimental effect on the financial sector were coming together. First, a shake-out in an industry that had probably over-expanded in response to liberalization was imminent. A second factor was the imposition of revised regulation for the financial sector in 1992. In that year, the *Bank of Jamaica Act* was amended, the *Banking Act* was revised, and the *Financial Institutions Act* replaced the *Protection of Depositors Act*. An effect of these legislative changes was to regulate and regularize the operations of the non-banks and near banks, but also to impose stricter regulations on commercial banks.

Probably the most important factor in explaining the misfortune of the financial sector was the orthodox stabilization policy detailed above. This was accompanied by an accumulation of domestic debt. The internal public debt rose from 22 percent of GDP in 1993 to almost 50 percent by the end of 1998 (Table 9). This impressive increase in public borrowing in the presence of a non-accommodating monetary policy had the effect of driving up interest rates. High interest rates not only increased the banks' bad debt portfolio, but also raised their cost of funds at a time when their asset mix, heavily into equity, could not adjust quickly enough to recover that cost.

The problems in the financial sector became manifest in 1995. Table 17 indicates that the total assets of the banks and building societies shrank by 10.5 percent between end-of-year 1994 and 1998. But the reduction in the market value of the asset base was probably greater than that, as the real estate market declined and the bank's accounting failed to keep up with declining market valuations. In the two years between 1996 and 1998, the number of institutions in the non-insurance financial sector declined by 45 percent. Moreover, every local commercial bank, with only a single exception, was forced into a position wherein it had to seek public assistance.

Table 17
TOTAL ASSETS OF NON-INSURANCE FINANCIAL SECTOR

	Commercial Banks	Merchant Banks	Building Societies	Trust Companies	TOTAL	RATIO to GDP, Index
1980	8.9	0.4	1.3	0.6	11.2	46.0
1981	10.3	0.4	1.5	0.6	12.9	53.1
1982	11.3	0.4	1.8	0.9	14.4	60.3
1983	13.3	0.4	1.8	1.2	16.6	71.0
1984	12.4	0.5	1.5	1.2	15.7	71.5
1985	12.0	0.6	1.5	1.3	15.5	76.5
1986	12.3	0.9	1.6	0.2	15.0	74.7
1987	12.7	1.6	1.8	0.2	16.3	78.1
1988	14.7	2.2	2.1	0.2	19.3	92.7
1989	15.3	3.7	2.3	0.2	21.5	100.0
1990	14.0	3.7	2.4	0.2	20.2	91.2
1991	15.5	3.4	2.5	0.2	21.5	96.0
1992	15.4	3.5	2.9	0.1	21.9	100.0
1993	15.1	2.7	2.9	0.1	20.8	92.5
1994	17.4	2.7	4.5	0.1	24.7	111.5
1995	17.1	2.4	4.1	0.1	23.7	106.9
1996	15.8	2.3	3.8	0.1	22.0	102.0
1997	15.7	1.8	4.0	0.1	21.6	100.2
1998	16.7	1.6	3.7	0.1	22.1	104.9

Sources: Statistical Digest, various issues, Bank of Jamaica; Economic and Social Survey Jamaica, 1998, Planning Institute of Jamaica.
Notes: All values are in billions of constant (1989) Jamaican dollars, except "Ratio to GDP", which is an index number (base = 1989).

The decline in the insurance market was particularly severe. By 1998, the number of new policies sold had fallen to barely 1/3 of their peak of 1993. Over the same period, annualized premium income declined by 45 percent, and total sum assured for the industry fell by 59 percent.[7] With such a precipitous collapse, the eight stock companies and the two mutual societies in the insurance industry were all in financial difficulty by 1996.

Beginning in early 1997, the government intervened in the financial sector under the institutional auspices of the *Financial Sector Adjustment Company* (FINSAC). The interventions took many forms. The structural measures included the closure of some insolvent banks, merger of others, liquidity support, and the purchase of subsidiary holdings and real estate; the financial support came in the form of bonds issued in exchange for non-performing loans and acquisition of equity through the purchase of ordinary and preference shares. By the end of 1998, the cumulative cost of the restructuring through Finsac amounted to 37 percent of GDP, which puts the Jamaican case amongst the largest in the 1990s.

Table 18
BALANCE OF PAYMENTS

	Current Account /GDP	Current Account (US$m.)	…of which: Remittances (US$m.)	Financial Account (US$m.)	…of which: Net Foreign Direct Invest. (US$m.)
1980	-0.05	-136.1	162.7	107.9	27.7
1981	-0.10	-306.8	199.3	44.3	-11.5
1982	-0.12	-383.3	219.0	267.0	-15.8
1983	-0.16	-338.6	174.8	-2.4	-18.7
1984	-0.17	-315.2	178.5	551.1	12.2
1985	-0.13	-273.4	294.4	227.3	-9.0
1986	-0.01	-17.9	209.4	-105.6	-4.6
1987	-0.04	-125.7	217.7	360.5	53.4
1988	0.01	46.6	587.8	88.0	-12.0
1989	-0.08	-282.6	523.8	98.2	57.1
1990	-0.08	-312.1	314.9	404.5	137.9
1991	-0.12	-240.1	294.8	254.9	133.2
1992	0.01	28.5	387.2	297.3	142.4
1993	-0.06	-184.0	415.9	257.1	77.9
1994	0.00	6.9	494.9	355.9	86.5
1995	-0.04	-183.2	654.6	206.0	95.4
1996	-0.04	-237.7	693.5	439.6	150.8
1997	-0.06	-375.9	698.5	238.3	136.6
1998	-0.07	-482.9	698.3	339.3	356.0

Source: 1980-1988: International Financial Statistics, International Monetary Fund; 1998: Author's estimate based on data in Statistical Digest, Bank of Jamaica.
Notes: All figures are in millions of US$. "Financial Account" follows the definition in International Financial Statistics, and includes non-reserve asset transactions.

The effect of this entire episode on the policy environment was significant, and occurred in two ways. First, the government was forced to effectively reverse the process of privatizing publicly owned enterprises. During 1997 and 1998, the government acquired an equity position in almost every locally owned bank and insurance company. The privatization index in Table 5 loses more than a third of its value in those two years. The policy environment also changed as a result of the enlargement of the internal public debt. Table 9 shows that the internal public debt increased dramatically from 35 percent of GDP at the end of 1996 to 48 percent at the end of 1998. That debt figure, however, does not even include the public debt implied by the implicit insolvency of bank rescue agency, *FINSAC*, which was incorporated as an ordinary corporation wholly owned by the government, and whose accounts therefore do not appear in the public accounts. That implicit public debt contained in the accounts of *FINSAC* is of the order of an additional 20 percent of GDP.

Late, piecemeal, and contradictory reforms therefore form the background against which to understand the poor performance of the Jamaican economy. In particular, the inconsistency between the structural reforms in domestic markets and international trade on the one hand, and stabilization policy on the other. But the failure to maintain investment in the economic and social infrastructure, along with the effects of the banking crisis also played a role in the outcome for the economy.

VIII. CONCLUSIONS

Jamaica's economic performance has mirrored its policy thrusts only to a limited extent. During the period of industrialization by invitation up to 1972, the economy grew rapidly, averaging 5.2 percent per annum, and developed at least a superficial industrial capacity. From 1973 to 1980 under state populism, the economy declined dramatically, contracting at an average of 2.4 percent per year. After 1980, economic reform was supposed to have regenerated investment and growth, but this has not happened. The average rate of economic growth from 1981 to 1998 was a mere 0.1 percent – negative in per capita terms. Given the promise of economic reform, this outcome begs for an explanation.

The description of the process of economic reform in Jamaica reveals that, while some aspects of economic reform began in the early 1980s, many others were phenomena of the 1990s. It is arguable that economic reform reached a critical threshold only in 1994 or 1995. The lag required for the structural adjustment of the economy is probably long enough that improved economic outcomes would not have been manifest as early as 1998. Further, at the same time as economic reform was approaching its zenith, stabilization policy effected a contractionary stimulus on investment and output, and that effect would have magnified by the banking crisis. So, at least up to 1998, a combination of late implementation of economic reform, reversals, and contradiction by stabilization policy, along with low levels of public investment in the economic and social infrastructure, ensured that no growth or employment benefits followed from economic reform in Jamaica.

Notwithstanding the benefit of almost two decades of reform experience, mostly in Latin America and the Caribbean but also in Africa, it is still too early to draw clear conclusions about which reforms are critical and what are the threshold levels of the reform instruments for effecting results. Towards this end, more quantification of the reform experience is required so that future researchers may carry out cross-country quantitative analysis. Such a quantification requires a broader view of economic reform than currently exists in the literature. For one thing, quantification has paid attention only to the areas that have changed the most during the era of reform. Others that may be critical to growth and development, either on their own or as complementary factors, has been largely ignored.

One such is the quantity and quality of the economic and social infrastructure. It was argued above that this may have been a contributory factor to the performance of the macroeconomy in the case of Jamaica. This index may be critical in light of the focus on the overall size of government and the implication in the existing treatment that smaller government is an improvement in the reform environment, even after the publication of the World

Development Report 1997 with its focus on the importance of the role of the state (World Bank, 1997). Another element worthy of inclusion in quantitative analysis of economic reform, studied in the empirical growth literature but less so in the structural adjustment literature, is improvements in the quality of governance and rule of law. Here, the need is for improved methods of quantifying the quality of governance as existing practice in the growth literature relies on subjective surveys.

Methods of aggregation and summarization of economic reform quantification also need to go beyond simple averaging. The burgeoning literature on empirical economic growth has identified some of the elements crucial to economic growth, namely trade openness, low inflation, quality of governance, and infrastructural adequacy amongst others. That literature should inform the assignment of weights in the averaging of the elements of economic reform.

In these and other ways, the analysis of the era of economic reform has far to go. It is an exercise of crucial importance in advancing our understanding of the role and evolution of policy in general. For the case of Jamaica, the quantification and analysis of economic reform contained herein has revealed that Jamaica, far from being the early reformer portrayed elsewhere, is a late and unenthusiastic reform whose reform process was inadequate to overcome other obstacles to investment and growth.

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Notes

[1] Data in this paragraph is from *World Development Indicators on CD-ROM 1998*, World Bank.

[2] This was a departure from the previous period of *crown colony rule*, during which industrialization was actively discouraged for fear of damaging Britain's export trade (Stephens and Stephens, 1986).

[3] The establishment of a national airline in 1965 was a notable exception.

[4] Nationalizations were limited to acquiring a controlling interest, and were with compensation.

[5] Data is computed from the Survey of Living Conditions, 1996.

[6] In any case, by virtue of a regulatory decision that reserve ratio requirements and commercial bank current accounts be kept in distinct accounts at the central bank, the reserve requirement served no prudential purpose.

[7] Data supplied by the Life Insurance Companies Association.