

*As Prepared for Delivery*

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[Mr. Grainger, Thank you for the gracious introduction. Governor Williams, thank you for the warm welcome.]

Dear President Warren Smith of the Caribbean Development Bank,  
Dear Governors of the Caribbean Development Bank, Board of Directors,  
Distinguished Guests, Ladies and Gentlemen,

It is a great honor to speak to you this evening. I would like to extend my sincere appreciation to the Caribbean Development Bank for the invitation. I also want to thank the Government of Trinidad and Tobago, especially the Central Bank and Governor Williams, for your hospitality.

I would like to take this opportunity to congratulate Dr. Warren Smith on his appointment and wish him every success in his new role as President of the Caribbean Development Bank. The Caribbean Development Bank has a long tradition of Presidents committed to structural transformation of the economies in the region, starting with its very first President, Sir Arthur Lewis. I did not get a chance to know Dr. William Gilbert Demas, the Bank's second President, a Central Bank Governor of Trinidad and Tobago, and another distinguished economist, to whom this series of lectures is dedicated; but my remarks tonight would have sounded familiar to such a champion of regional development and integration.

In preparing for this lecture, I thought of what Nobel Laureate James Meade said about Mauritius, which, like many of your countries, is an island with a small population. Meade said in 1961, seven years before independence: "It is going to be a great achievement if [the country] can find productive employment for its population without a serious reduction in the existing standard of living.... [T]he outlook for peaceful development is weak." Of course, Mauritius has actually grown at a rate of over 5 percent per year, increasing income per capita from \$700 in the 1970s to \$7,000 today and diversifying its economy from sugar to tourism, finance, and textiles.

So, unlike Meade, I have not come here today to lay out the pessimistic view about the prospects of the Caribbean countries. I have come as an optimist because, as Winston Churchill once said, "a pessimist sees the difficulty in every opportunity; an optimist sees the opportunity in every difficulty."

This is really the theme of my talk: your challenges – smallness and insularity and uncertainty – can also be your opportunities. Let me start by laying out some of those difficulties – before I turn to how they can become opportunities and how you can seize them in order to generate growth and create jobs.

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**I. The Caribbean: Structural Challenges and Slow Recovery**

Over the past couple of years, the Great Recession has not spared the Caribbean countries. GDP growth of all the Caribbean countries fell from 6 percent per year in 2006-2008 to almost zero in 2009. Worse

still the recovery has been sluggish. The World Bank estimates growth at 3 ½ percent in 2010-12, compared to 4 ½ percent for the main countries of Latin America.

Perhaps more worrying are the longer-term trends, which predate the Great Recession. To put it simply: countries in the region have not been keeping pace with growth rates in emerging markets around the world. In 1980, the Caribbean's average per capita income was twice as high as that of the average developing country; today it is only a third higher. Countries in the region have been growing at 2 percent per year since 1970 – while small island states on average have been growing at an average annual rate of 3.6 percent and the whole world at an average rate of 3.5 percent.

Most countries in the region went through a structural transformation in the 60s and 70s, but from a dependence on agriculture to a dependence on tourism, still with limited diversification. Moreover, in a 2005 World Bank report on the region's growth prospect, we noted that the region had experienced a decline in productivity, hence erosion in competitiveness. An example of this is the yield for bananas: in St Lucia, Jamaica or Dominica, it is only 20 to 35 percent of that of Ecuador.

Not all countries in the region are of course alike. Guyana and Trinidad and Tobago are resource-wealthy, commodity-based economies, whereas Barbados and the Eastern Caribbean countries are largely service driven economies. Several countries have high income per capita – above \$20,000 for the Bahamas –, while Haiti is one of the poorest and most fragile countries in the world. Some countries did better in terms of growth in the 1980s and others in the 1990s. There are also large differences in terms of population as the Caribbean is home to some of the world's smallest states, such as St. Kitts and Nevis, which has a population of 50,000. Therefore I do not want to generalize too much.

However, in many ways, most of your countries face the same structural disadvantages of small states and islands. Spelling out these disadvantages can be overwhelming. Small size means an inability to generate the economies of scale that are driving growth in many cities and countries around the world. Being remote reduces access to these cities and their markets. All this increases the cost of doing business: economists Pedro Martins and Alan Winters have calculated that, even with zero wages or zero returns to capital, production costs in small remote countries might still exceed world prices. The small size of the economy also translates into high fixed costs of running a bureaucracy and providing public services: it is estimated that, to deliver services, small states spend on average 3.7 percentage points more of their GDP compared to large states. Small islands are also particularly vulnerable to natural shocks. Small economies have to be open and as such are vulnerable to external economic shocks. And being small, their ability to hedge production risks is severely constrained.

Indeed, Sir K. Dwight Venner, with whom I was a member of the Growth Commission led by Professor Mike Spence, has captured these challenges quite vividly: "The country I'm from, St. Lucia, has 160,000 people. The cost of government per capita is very high; the markets are very small; and the cost of production is very high. Also every year we have a hurricane season, which can destroy the country's GDP. In some countries, it can also lead to high debt levels. Their infrastructure is destroyed before they paid for it, so they borrow again. Then it is destroyed a second, and sometimes even a third time".

You are familiar with these challenges. But tonight I want to stress them because the world we live in is increasingly uncertain. By one count, there were 150 crises per year in the 1980s and there are now over 370 per year. That is, on average, one every single day – crises of all types from economic to natural disasters!

Natural disasters are phenomena of the Caribbean, and the impact is usually dramatic. In 2004, tropical storm Ivan destroyed 250 percent of Grenada's GDP and affected 60 percent of the population. In 2010, the Haiti earthquake caused damages amounting to 120 percent of Haiti's GDP and affected a third of the population. We are still living with the consequences today.

Climate change will also contribute to uncertainty in the region. Some countries, such as Belize, Guyana, and the Eastern Caribbean islands, face risks of rising sea levels due to global warming or threats to their coral reef. I am encouraged to note that Grenada and St Vincent and the Grenadines have already mobilized climate financing from the Pilot Program for Climate Resilience. Such financing can help to decrease the vulnerability of critical infrastructure in these countries over the next couple of years.

Another set of shocks that is of particular concern to us at the World Bank is the rising level and volatility of food prices. We estimate that, as a result of the recent rising food prices, 44 million more people have been thrown into poverty. In fact, among countries in the Latin America and Caribbean region, 5 out of the 6 countries the most vulnerable to food price volatility are in the Caribbean. In some countries, like Haiti and Jamaica, food accounts for more than half of household's consumption, making large numbers of families particularly vulnerable to food price volatility.

And in today's world, these uncertainties are here to stay.

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## II. Seizing Opportunities

But these challenges are no destiny. Difficulties can become opportunities for change.

Take Africa – a continent that has been associated with hunger, poverty, collapse, and labeled as a “hopeless continent” by the Economist magazine just a decade ago. Today, do you know that Sub-Saharan Africa is a trillion dollar economy that has grown faster than Brazil and India between 2000 and 2010 in nominal dollar terms and is projected by the IMF to grow faster than Brazil between 2010 and 2015? As I have said in other occasions, the continent is poised to join the ranks of the so-called BRICs!

So Africa can. And the Caribbean can too. Let me highlight three opportunities.

First opportunity: **your brand**. Who does not know about the Caribbean? Its location, its geography, its beaches, its natural habitat, its culture, and its historical links to Europe and North America are what make the region unique. For many people around the world, the Caribbean is associated with beautiful images, and positive thoughts.

The Caribbean brand is precious because, given all the challenges of being islands, this brand is the main reason why investors would be willing to pay a premium to offset the lack of economies of scale. This brand is a joint brand, which all of you in the region have a collective responsibility for.

Many countries in the region have already been successful at developing a vibrant tourism industry and a viable brand, explaining for a large part the levels of income achieved today. Tourism accounts for 29 percent of the region's total exports. But the traditional tourism product faces challenges from competitors in other regions such as Asia. And your regional brand has better name recognition than many of the individual country's names.

There is an opportunity to develop new product lines based on a regional brand. For that, you will need to define what you want to be known for. Higher-end tourism has been identified as a major area of

emerging opportunities for the Caribbean region. This includes adventure tourism, nature-based tourism, cultural tourism, meetings and conferences, and community tourism. Can the Caribbean brand build upon regional packages that combine the strength of your individual countries?

Such regional brand needs to be actively promoted. Ireland, Fiji, Mauritius, and other successful islands have first-class investment, trade, and tourism promotion agencies to attract a diversified set of investors and visitors. A regional brand should also be aimed at new markets. The natural target is the fast developing emerging markets and their growing middle class who are increasingly looking to go abroad. You should make a conscious effort to attract the nearby Brazilian and Mexican tourists. And do you know that Chinese love to come to the US, to Florida and the West Coast: why would they not combine this with a stay in the Caribbean?

This leads me to the second opportunity, which World Bank President Zoellick has been emphasizing over the past years: “we are moving into a world of **multi-polar growth**.”

The Caribbean region has traditionally had its eyes turned toward Europe and North America – for good reasons given the historical connection with Europe and the proximity and size of North American markets. This has served the region well, but the Great Recession has also demonstrated the limits of this model. Today, multiple poles of growth have emerged and for your region this means new markets and new investors, and an opportunity to hedge shocks through a diversification in markets.

Consider this. The United States contributed 27 percent of the world’s GDP growth in the 80s and a whopping 36 percent in the 90s; but only 21 percent in the 2000s. By contrast, the share of China and India increased from 5, to 12, and now to 32 percent! And closer to home, the share of Brazil increased from 1, to 2, and now 3 percent. Against this shifting economic geography, Caribbean countries exports are still going primarily to the US and Europe, with 54 percent to the US and 19 percent to the EU, but less than 1 percent to China and India combined, and merely 3 percent to neighboring Argentina, Brazil, and Mexico combined. These numbers represent a huge opportunity.

Caribbean countries are already very open economies: the average trade openness ratio, the ratio of the sum of exports and imports to GDP, is at 62 percent. How does one do more to tap the potential of these new markets? This requires a determined strategy – but it is likely that the high cost of trade in and out of the region is a major barrier to trading with new markets. For instance, Jamaica hosts the 7<sup>th</sup> largest natural deepwater harbor in the world: imagine the potential of such port in a multi-polar world! Yet, the reality is that, despite the proximity to the US, for 60 percents of products, the freight and insurance costs from the Caribbean to the US are higher than average costs worldwide. When surveyed by our World Bank teams, professionals from logistics firms across the world rank Haiti 98<sup>th</sup> out of 155 countries, Jamaica 108<sup>th</sup>, and Guyana 140<sup>th</sup>. Such average ranking might be fine for countries where trade is not such an integral part of life and business; but this is not good enough for the Caribbean.

Reducing the cost of trade means minimizing the reliance on trade taxes to generate public revenues. It also means streamlining trade regulatory requirements and addressing bottlenecks in the logistics chain.

The emergence of these new markets does not mean that traditional markets are vanishing. In fact, the region could do more to take advantage of its traditional markets and diversify its trade with them.

There are several viable opportunities. For examples, for health treatments, you must all know that, with the astronomical health care costs in the US, people are now travelling all the way to Thailand and

India for heart surgery, plastic surgery, etc. And ditto for education and business services. The connection to the UK, USA, and Canada means that you could attract top universities to set up campuses here for world class degrees, like what's happening in Malaysia. I keep wondering what is keeping the region back from doing this. At the moment, of the 15 countries in the region, only Jamaica makes it into AT Kearney's top 50 Global Services Location Index, which measures attractiveness for offshore job-generating opportunities. Can Caribbean countries come together to increase the scale of their markets and offer packages of diversified health and education services for instance? Can Caribbean countries become more attractive for offshore opportunities?

The third major opportunity I would like to discuss is the **acceleration of technological development**. The rapid decline in costs, the increase in access, and the innovation in services are a game changer for small, remote economies. Technology played an important role in the take-off of Singapore, Cyprus, Mauritius, and other successful small economies. Technology is an opportunity to reduce distance to markets, make business and government services more efficient, and attract offshore services.

At the moment, the region is lagging behind in terms of access to technology and affordability. Access to broadband services is still limited in the Caribbean, with broadband penetration below 8 percent in 2008, compared to over 30 percent in OECD countries. Affordability of broadband services is also a major barrier: today the average price of one megabit down-speed service across the region is approximately \$36 per month, close to three times the price in the United States and seven times the price in the United Kingdom. This represents more than 10 percent of GNI per capita, compared to 1 percent in the U.S.

How do you seize this opportunity? Well, limited competition is to blame for the poor situation in the region. In areas where competition has been stronger, the situation is better. For instance, the number of mobile cellular subscriptions has increased from 8 percent of the population in 2000 to 104 percent in 2008. But many other technology-related markets remain structured around monopolies or duopolies, leading for instance to a lack of competitive access to submarine cables for international connections. So unleashing the power of competition is key.

Public private partnership is another way to seize this opportunity. In Mauritius, the government has built the Ebene CyberCity designed to transform the country into a diversified, high-tech, high income services and knowledge-based economy. This Knowledge Park was developed with the help of a \$100 million credit from India. Many Indian IT companies, like Infosys, Hinduja TMT Ltd, and PentaFour Software are present in the city. This cyber city is a good example of South-South collaboration in IT.

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### **III. Addressing Four Core Basics**

Seizing those opportunities has the potential to generate greater economic growth and create sorely needed jobs. Generating jobs is critical given the growing youth population, unemployment levels over 10 percent in many countries, and the need for social cohesion. So whatever countries do in education, health services, or accessing new markets, we need to make sure that jobs are created along the way. This is critical to social stability.

However, to enhance the chances that Caribbean countries will be able to turn these opportunities into growth and jobs, countries also need to get the basics right. These are the first steps to be taken. As Martin Luther King said, "take the first step in faith. You don't have to see the whole staircase, just take the first step." Let me focus on four basics.

The first basic that I want to highlight is **sound macroeconomic management**. This is one of the reasons for the turnaround of Africa in this new century. This is also a lesson from the Great Recession: in a world of greater uncertainty, countries that have their macro and fiscal situation in order fare much better in response to crises.

Sound macroeconomic management starts with fiscal discipline. This is particularly challenging given the cost of delivering services in small economies and the significant costs of natural disasters in the region. Prioritizing expenditures, seeking efficiency gains, and mobilizing revenues are therefore critical tasks.

Countries in the region will also have to deal with their high debt levels. In a study of 44 countries over 200 years, Economists Carmen Reinhart and Ken Rogoff found that, in emerging markets, above a threshold of debt-to-GDP ratio of 60 percent, median growth rates fall by 2 percent every year. Of the 15 CARICOM Member States, 10 already have a public-debt-to-GDP ratio over this threshold of 60 percent. Debt service is above 20 percent of current revenues in several countries. Hence, in many of the Caribbean countries, debt is both crowding out private investment and absorbing scarce public resources.

The key to debt sustainability is private-sector-led economic growth and good fiscal management: but can the spiral of indebtedness be broken without some debt restructuring? I speak from my experience of working on Nigeria's previously serious external debt overhang.

Already several countries in the region have undertaken debt restructuring over the years. In my experience, making progress toward a permanent solution to debt overhang requires your countries to take a very active leadership of the issue and to develop a comprehensive and creative solution. Now is a good time to begin the analysis of options and the World Bank can help with this analytical part. Options are likely to revolve around a balanced set of measures that include, first, facilitation of private-sector led growth; second, better protection against natural disasters; third, tighter management of public finances and future debt flows; and fourth, restructuring of current stocks of debt. Countries can come together to get it done.

The second basic is **deeper regional integration**. I appreciate very well from my experience in Africa the sensitivities around such deep integration. At first glance, it might well seem that whatever one country wins, another loses. Free movement of people, for instance, has created concerns in all regions that are seeking deeper integration. But regional integration is the only viable way to create scale for your economies. More fundamentally, having neighbors that are stable and prosperous is good for each country.

Regional integration can create important economies of scale by implementing initiatives jointly and pooling resources together. The Eastern Caribbean Central Bank, Civil Aviation Authority, Supreme Court, and Telecommunications Authority are important achievements. What more could be done in terms of joint regulation? In addition, small countries that are doing well – such as Luxembourg or Andorra in Europe – have achieved a very strong level of institutional integration with their neighbors. Similarly, Caribbean countries could also come together to seek better integration with their neighbors. Similar business platforms or regulatory regimes in several sectors could prove a big advantage.

Regional integration also offers an opportunity to better manage uncertainty. The region has good experience to build upon in this area, with the Caribbean Catastrophe Risk Insurance Facility. CDB's President, Dr. Warren Smith, has been a very active member of this facility's Board and a staunch

advocate for the facility. Supported by the World Bank and endowed with \$150 million, this facility enables Caribbean governments to purchase insurance coverage to finance immediate post-disaster recovery needs. The pooling of risks through regional integration is critical to the facility's success. This facility was the very first to make a cash payment to the Haitian Authorities after the devastating earthquake in 2010. Other regional fiscal mechanisms could mutualize risks, for instance emergency funds financed by remittances or tourism revenues (or oil revenues in the case of Trinidad and Tobago).

The third basic that needs to be addressed is that of **mobilizing more private sector financing to fuel growth**. In the past, growth has relied heavily on public sector financing and today's debt situation proves that this was not a sustainable path. Countries need to be innovative to attract financial resources: this must be within reach given the existing financial centers in the region. Earlier I talked about attracting investors from the emerging markets. There is much to do.

An innovative source of finance is to tap more into your diaspora. Caribbean countries receive the equivalent of 7 percent of GDP in remittances every year. One million or more of Jamaicans, depending on the source, have emigrated abroad. While Jamaica is often cited, alongside Ghana, as an example of "brain drain", it is forgotten that Jamaica receives nearly \$2 billion in remittances annually. These Jamaicans may not be very wealthy, but because of their number, significant amounts of development funding could be raised if the diaspora can be encouraged to invest even small sums in Jamaica.

Diaspora bonds are an innovative instrument to mobilize the diaspora's savings. These bonds would be structured like any bonds on the market, but would be sold by governments, private companies, and public-private partnerships to Caribbeans living abroad. They would be sold in small denominations, from \$100 to \$10,000, to individual investors or, in larger denominations, to institutional and foreign investors.

There are precedents for diaspora bonds. Greece announced a few months ago that it was preparing to issue \$3 billion worth of diaspora bonds in the United States. India and Israel have issued diaspora bonds in the past, raising over \$35 billion, often in times of financial crises.

In another scheme, which would raise even more funding, remittances could be used as collateral to raise financing from international markets. In several developing countries — including Brazil, Egypt, El Salvador, Guatemala, Kazakhstan, Mexico, and Turkey —, this approach has allowed banks to raise more than \$15 billion since 2000.

Diaspora bonds are being discussed in Jamaica and this is an area where regional cooperation could further scale up the impact.

Finally, underlying most of these challenges – from fiscal management to the financial sector – is the **quality of governance and institutions**. In many countries, I have seen myself the corrosive effects of state capture, criminality, and corruption.

In the Caribbean, in countries that are located between a major supply of cocaine to the South and primary consumer markets in the North, criminality is a particular concern: murder rates in the Caribbean – at 30 per 100,000 people annually – are higher than in any other region of the world. Crime is not only a deterrent for investors, it also undermines social cohesion.

But governance is not an issue to be left to law enforcement agencies alone; it is by itself a major development challenge and needs to be addressed as part of any strategy to accelerate growth. It has been estimated, for instance, that bringing homicide rates to Costa Rica's levels could boost economic growth by 5.4 percent in Jamaica and Haiti, and about 1.7 percent in the Dominican Republic.

In Nigeria, when I was Minister of Finance, fighting corruption was an integral part of our development strategy and we identified key areas to focus our efforts on public procurement, the management of revenues from the oil sector, and budget transparency. We made much progress and tripled economic growth, although several of these reforms have since been rolled back. But addressing the root cause of governance failures is challenging. So one needs to have a stiff back and utmost political will. To quote one of my former Nigerian colleagues, Nuhu Ribadu, "when you fight corruption, corruption fights back." But corruption is also scared if policymakers have the backbone to stand against it.

Improving governance in the private sector, by curbing red tape and dismantling monopolies, is necessary to unleash entrepreneurship, attract new investors, and create jobs. It is encouraging that, according to the World Bank's Doing Business indicators, progress is being made in areas such as dealing with construction permits, starting a business, and protecting investors. It should not take over three years and a half to resolve a commercial dispute in Trinidad and Tobago, while it takes half that time on average in Latin America. In the regulatory area, restrictions and special privileges might seem appealing politically, but they are bad economics.

Grand corruption is also increasingly international, as it involves illicit international financial flows, sophisticated financial schemes, tax evasion, money laundering, and the theft of public assets. Addressing grand corruption requires a high level of political commitment and international cooperation.

In this area, I would like to congratulate the Caribbean financial jurisdictions that have signed financial information exchange agreements to meet the international standard in this important area. This should help sustain activity in Caribbean financial jurisdictions in an era of global competition and increased international scrutiny. I am happy that the World Bank was able to support you in these negotiations.

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So to recap: Macroeconomic management; regional integration; innovative financing; and governance. These are four basics that the region needs to address to turn the growth opportunities into reality and create jobs.

The challenges are not smaller today than they have been in the past – they are perhaps taller and present you with a new urgency. Challenges are compounded by the uncertainty of the world we live in. I am convinced that countries that will succeed in the future are those that seriously tackle their challenges in a way that allows them to manage in an era of increased global uncertainty and volatility.

Let me end by saying that I have the utmost faith in the ability of the Caribbean leadership to grasp today's changing global dynamics and take advantage of existing and emerging opportunities whilst meeting squarely the challenges. We at the World Bank are ready to partner with the Caribbean governments, the Caribbean Development Bank and other institutions in the region. In Nigeria, we have a saying "*aka nni kwo aka ekpe, aka ekpe akwo aka nni. nwacha adi ocha*" which translates to, if the right hand washes the left hand, the left hand washes the right hand, they will both be clean. This is the spirit that will guide our partnership. Thank you.