Country Economic Memorandum
Report No. 60374-JM

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Poverty Reduction and Economic Management Unit
Caribbean Countries Management Unit
Latin America and the Caribbean Region
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Overview and Policy Options

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Part II: Creating an Enabling Environment for Growth: Key Policy Challenges

Part III: Unlocking the Potential for Private Sector Development and Growth
Acknowledgments

This publication is a summary of the Jamaica Country Economic Memorandum: Unlocking Growth (Report No. 60374-JM).

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A basis for optimism. This Country Economic Memorandum assesses the key causes that have stalled Jamaica’s economy over the past four decades and presents recommendations to unlock its growth potential. There is a basis for optimism in that Jamaica has had political stability, high rates of private investment, significant reduction of poverty in rural and urban areas, and improved income distribution. Nonetheless, this report shows that, since independence in 1962, long-term economic growth has been disappointing and underperformed most other countries.

Jamaica’s disappointing economic performance is a case of low productivity. While Total Factor Productivity (TFP) in Jamaica was growing above the world and regional averages in the 1960s, since the 1970s performance collapsed despite high investment. This has been attributed to the spread of low productivity across the economy. Estimations for 1992-2008 show that labor productivity was negative in eight of 10 sectors and it was positive but negligible in the sectors for communication services and manufacturing and transport. Jamaica’s TFP per worker also lags significantly behind most other countries in the LAC region. Understanding and acting on the factors behind Jamaica’s low productivity will go a long way in unlocking growth potential and creating conditions for greater reductions in poverty.

Jamaica’s poor growth performance and low productivity has three core ‘binding constraints’ amid many contributing factors. There are many potential obstacles to growth. The non-exhaustive list includes frequent natural disasters, low productivity of capital, loss of competitiveness, distortions
from tax incentives, limited space for productive public spending due to high public debt, inadequate human capital, migration of skilled labor, the high cost of crime, and lapses in governance. The leading binding constraints are (i) crime, (ii) deficient human capital, and (iii) fiscal distortions (tax incentives and waivers as well as government’s budget management policies and practices). The most significant growth impact will come from removing these key growth obstacles.

- **Crime is the most evident and severe problem in Jamaica.** Once crime is established, it is difficult to overcome. It severely limits future growth and leads to a vicious circle as low growth further increases crime and higher crime rates further reduce growth. Crime erodes social stability and makes rule of law a critical area of concern. It has a negative effect on human capital, creating incentives for migration among the most skilled, educated, and entrepreneurial citizens. It constrains business expansion and diverts resources from productive activities to crime protection. Because of crime and other structural conditions, investment in Jamaica tends to flow into isolated activities. All-inclusive resorts, mining, and Export Free Zones are the best examples of this ‘enclave’ development model with its low spillovers (while tourists avoid crime-ridden areas, their dollars remain in the resort; mining communities and international businesses are similarly isolated from the greater Jamaica). A 2007 United Nations–World Bank study illustrates the link between growth and lower crime rates. It states that Jamaica could experience an annual increase of 5.4 percent in per capita GDP, if it cut crime rates to the levels prevailing in Costa Rica.

- **The available evidence shows that Jamaica has a low level of human capital, with poor quality of education and insufficient training of its labor force, despite the country’s efforts.** From 1995 to 2008, Jamaica saw an increase in enrollment rates in both secondary and tertiary level education, however existing quality indicators put Jamaica below the Caribbean region average. There is also evidence that human capital is a scarce factor because private returns to schooling and private returns to training are extremely high (with higher wages to be found outside of Jamaica). In 2008, 72 percent of the labor force indicated a lack of job training. The combination of poor education and low levels of training suggests an overall low quality of the human capital that results in a negative impact on the level and growth of productivity. The migration rate of skilled workers has also increased because of difficult living and business conditions (including crime and government policies). In general, it is believed that the people who migrate are more able, more entrepreneurial and less risk averse; the country therefore loses very important assets for productivity, innovation and entrepreneurship.

- **Jamaica’s fiscal policies and budget-management practices and policies constrain growth.** Inconsistent, complex tax policy with numerous exemptions and special privileges has reduced tax revenue by an estimated 20 percent, significantly reducing the government’s spending capacity. The complex system of taxes
and incentives also creates distortions for the allocation of capital and lowers investment productivity. High debt-servicing costs and a high wage bill have reduced the fiscal space available for productivity enhancing public spending, including public investment that is complementary to private investment and expenditure on education and health. Underlying institutional and political economy factors are major impediments to strengthening fiscal and expenditure policy and management of public finances.

Jamaica has an opportunity to grow much faster than it had in the past and the key to unlock this potential is within its reach: turning its high investment into high productivity. Jamaica has to do this with limited fiscal resources and an ongoing program of fiscal consolidation. Recent fiscal reforms are necessary but not sufficient for increasing growth. There is no silver bullet for all Jamaica’s problems, or any single, unique binding constraint whose removal would solve them. This will require actions on several fronts that have a direct bearing on total factor productivity and the efficiency of investment. These include addressing crime as a national priority, reducing tax distortions and increasing labor force skills. Jamaica can consider complementing the ongoing fiscal consolidation program with reforms in these three areas. These reform actions, if quickly implemented, will scale up productivity in traditional sectors and encourage investment in new sectors. It is time this be done if Jamaica is to avoid losing another decade of growth and if the country is to make a clean break from the economic and social fragility of the past.

Two of Jamaica’s best performing sectors provide examples of how advances are possible once the constraints are resolved: tourism and food-processing. The improved environment can stimulate productivity in sectors where Jamaica has a comparative advantage, as well as encourage the emerging new activities which have been identified through value chain analysis in the food processing and tourism sectors. A meaningful reduction in crime will make tourists feel safe to move out of resorts enclaves and enjoy new or revived tourist venues for site-seeing, entertainment, shopping, and dining. Improved labor and managerial skills can make the tourism sector more competitive in the region. Jamaica already enjoys an international market for its food products. Improvements throughout the Jamaican processed foods supply chain, including agriculture, labor, transportation, food safety certification, and marketing will quickly advance this sector.
1. The primary objective of this report is to identify the main obstacles to growth in Jamaica. The report takes a holistic approach, examining a large set of economic and social factors that may be hindering growth and filtering them through a growth diagnostic analysis to narrow the focus to those that constrain growth the most. Building on the results of the growth diagnostic analysis, the report then discusses each key obstacle and identifies possible reform scenarios to unlock growth in Jamaica. The report also examines how the country might further accelerate growth through private sector development.

2. The findings of this study indicate that Jamaica’s disappointing economic performance is traceable to low productivity caused by (i) deficiencies in human capital and entrepreneurship that are due to high migration rates and to deficiencies in the quality of education and training offered to the labor force, among other factors, (ii) a high rate of crime, and (iii) distortionary tax incentives combined with “enclave” development that does not spill over to the rest of the economy. The potential for accelerating future growth rests primarily on the ability of the country to remove or at least ease these key growth obstacles. Once they are removed, Jamaica can further accelerate growth by enhancing private sector development. A matrix of policy options keyed to the obstacles mentioned above can be found at the end of this overview (table 4).

3. The report has three parts. The first analyzes historical growth performance and poverty reduction to provide a long-term view of Jamaica’s economic development (chapters 1 and 2). A comprehensive growth diagnostic analysis is then applied to identify key obstacles to growth (chapter 3). Building on these findings, the second part of the report focuses on labor markets (chapter 4) and public financial management (chapter 5) with the objective of identifying the causes of the low labor productivity and fiscal distortions that hamper growth in Jamaica. Crime has been largely left out of the report because it has been heavily studied and because it is still too early to assess the impact of recently initiated crime-prevention projects. Part II also analyzes the impact of recent reforms undertaken to alleviate obstacles to growth linked to human capital and fiscal distortions (chapter 6). Part III of the report looks at how Jamaica might further accelerate growth through exports and private sector development once key growth constraints have been removed or eased (chapters 7 and 8).

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1 Planning Institute of Jamaica prepared a growth strategy titled as “Growth Inducement Strategy for Jamaica in the Short and Medium Term” in March 2011. The objective of this strategy is reported as analyzing the current state of the economy and, on this basis, developing recommendations for policy and action to induce economic growth, starting with the upcoming budget process for the new fiscal year 2011/12 and going forward into the medium-term 2012/2014. In this respect, the CEM is a complementary analytical study focusing on long-term economic growth.
Part I: Obstacles to Growth in Jamaica

THE JAMAICAN ECONOMY IN BRIEF

4. Jamaica grew quickly in the 1950s, but swings in economic policy in subsequent decades produced a significant contraction in per capita GDP. With growth propelled by the development of new activities, mainly mining and tourism, Jamaica’s per capita gross domestic product (GDP) grew by about 6 percent a year in the 1950s (figure 1). In the 1960s, however, the rate slowed to 2.9 percent. In the early 1970s, the country made a major change in its development strategy. Adopting an import-substitution model, the Government turned to state intervention. Several companies were nationalized, higher tariffs created barriers to imports, some foreign products were banned outright, and strict exchange controls were imposed. In the early 1980s economic growth remained poor, despite the efforts to revitalize the market economy. With Jamaica facing an adverse international context, per capita GDP declined by 7.5 percent in constant terms from
1981 to 1985. The statist reform was extremely costly for Jamaica, without any clear economic gain, and the market-oriented reversal in the early 1980s took years before beginning to bear fruit. By 1985, real GDP per capita was 35 percent lower than in 1972, retreating to its 1969 level.

5. GDP growth accelerated in the second half of the 1980s and into the early 1990s. Since then, however, growth has been lackluster. Over the past 20 years, real per capita GDP has increased at an average of only 1 percent. Only a few sectors have been relatively dynamic, and the unemployment rate has remained above 10 percent. Liberalization of trade worldwide has erased the tariff advantages Jamaica long enjoyed, sapping sugar and banana production, two traditional products, as well as the garment industry, which had flourished in the 1980s. In the 2000s, Jamaica’s average rate of real GDP growth ranked 180th out of 196 countries. Jamaica also underperformed compared with other economies with similar high debt-to-GDP ratios (table 1).

6. Economic performance has been poor across the board. Of 46 economic subsectors, only financial services and telecommunications had growth rates of more than 4 percent a year between 1992 and 2008. During that period, 18 subsectors declined, and 19 grew at a rate of less than 2 percent a year. Even Jamaica’s best-performing sectors—the most modern, dynamic, and export-oriented, and that attracted most FDI inflows—underperformed compared with what similar sectors achieved in the rest of the world.

7. The leading sectors in the Jamaican economy followed an “enclave” development pattern, which limits spillovers to other sectors. Mining, for example, is highly capital intensive. Most capital goods and services are imported, and the sector employs less than 1 percent of Jamaica’s labor force. The tourism industry is responsible for 10 percent of total employment, but it has developed in a way that prevents strong intersectoral linkages. Enclaves are likely to be a response to high crime rates and fiscal incentives that grant duty concessions to imported food and favor large-scale, capital-intensive hotels. Some of these tax incentives are included in the Export Free Zone Act, along with other arrangements that discourage or prevent strong links between firms located in these zones and other sectors or enterprises.

<table>
<thead>
<tr>
<th>Rank</th>
<th>Country</th>
<th>Year 2008</th>
<th>Ratio to Jamaica</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Singapore</td>
<td>27,991</td>
<td>7.4</td>
</tr>
<tr>
<td>2</td>
<td>Portugal</td>
<td>11,413</td>
<td>3.0</td>
</tr>
<tr>
<td>3</td>
<td>Trinidad and Tobago</td>
<td>10,981</td>
<td>2.9</td>
</tr>
<tr>
<td>4</td>
<td>Uruguay</td>
<td>8,788</td>
<td>2.3</td>
</tr>
<tr>
<td>5</td>
<td>Mexico</td>
<td>6,592</td>
<td>1.7</td>
</tr>
<tr>
<td>6</td>
<td>Chile</td>
<td>6,229</td>
<td>1.6</td>
</tr>
<tr>
<td>7</td>
<td>Panama</td>
<td>5,587</td>
<td>1.5</td>
</tr>
<tr>
<td>8</td>
<td>Costa Rica</td>
<td>5,196</td>
<td>1.4</td>
</tr>
<tr>
<td>9</td>
<td>Jamaica</td>
<td>3,792</td>
<td>1.0</td>
</tr>
</tbody>
</table>

Source: WDI
8. The Jamaican economy exhibits a high degree of informality, which is in line with its development level. Some studies have found that informality has increased from 13 percent of GDP to more than 40 percent in the past two decades. The country’s informal sector is very complex; it includes illegal activities such as the drug trade, but also music and entertainment, one of the most creative and dynamic sectors of the Jamaican economy. The size of Jamaica’s informal economy is lower than many comparator countries in Latin America and the Caribbean (LAC).

9. The Jamaican economy is characterized by very low levels of productivity and productivity growth. Growth in total factor productivity (TFP) has been negative in the past two decades. Estimates for 1992–2008 show that labor productivity was negative in 8 of 10 sectors; it was positive but negligible in manufacturing and in transport and communication. Jamaica’s TFP per worker also lags significantly behind most other countries in LAC (figure 2). Most of the change in the income gap between Jamaica and the United States can be traced to differences in the stock of human capital and TFP.

10. Jamaica’s disappointing growth and productivity rates cannot be attributed a priori to low levels of investment, which is commonly adduced in comparisons of LAC countries with the fast-growing economies of Asia. In Jamaica, total fixed investment averaged 25 percent of GDP during 1960–2008. The ratio was even higher over the past two decades, averaging 28 percent a year. The LAC Region’s average was 20 percent over the past four decades. The fast-growing East Asia Region invested an average of 28 percent of GDP during 1960–2008. These figures show that Jamaica has had investment levels close to those of the fast-growing East Asia region, although it must be acknowledged that the latter have increased in the past two decades, reaching an average of 33 percent.

Figure 2: Relative TFP per worker in LAC Countries, 2005

Source: Daudé and Fernández-Arias (2010)
11. High levels of public debt and large swings in the debt-to-GDP ratio have burdened the country for decades. The history of high debt is related to chronic public deficits, weak budget coverage, and contingent liabilities arising from a large number of weakly regulated public bodies. The ratio of public debt to GDP has been very volatile since the 1980s, and the government has not been able to reduce it. Debt was about 140 percent of GDP at the end of 2009.

INCLUSIVENESS OF GROWTH

12. Although Jamaica’s recent growth has been disappointing by regional and global standards, poverty has nonetheless declined significantly. Real GDP growth has historically been low in Jamaica, and the enclave development pattern allows little linkage between leading sectors and the rest of the economy. These two factors can leave a large portion of the population vulnerable to poverty shocks. Between 1997 and 2007, the Jamaican economy grew by just 12.7 percent, equivalent to a 0.79 percent average annual growth rate of per capita real GDP. During the same period, poverty was halved from 19.9 percent of the population in 1997 to 9.9 percent in 2007. Poverty is reported to have spiked substantially since 2007—rising to 12.3 percent in 2008 and 16.5 percent in 2009—due mostly to the effects of the global crisis (figure 3).

13. Jamaica’s growth elasticity of poverty was exceptionally high in the last decade. Between 1997 and 2007, the elasticity of poverty reduction with respect to a change in mean income was −16, much higher than the values usually observed in other countries. This elasticity is calculated as the percent change in the poverty headcount (expressed as a percentage of total population) for a 1 percent change in real GDP per capita. Under a common rule of thumb, the poverty elasticity of growth is assumed to be around −1.2. From the late 1990s to mid-2000s, poverty reduction in India, China, Vietnam, and Mexico has yielded elasticities of −0.2, −0.5, −1.0, and −6.8, respectively. The rise in poverty in Jamaica was also disproportional after 2007, when growth collapsed with the global crisis.

14. The main driver of the post-2003 decrease in poverty has been growth in per capita consumption, followed by declining inequality. A decomposition of poverty reduction reveals that higher mean consumption accounted for nearly three-quarters of poverty reduction, while narrowing inequality contributed about one-quarter. According to the national accounts data, per capita consumption grew faster than nominal GDP per capita. A substantial part of the growth in per capita consumption is explained by slower growth in the cost of poor households’ consumption basket relative to the average basket. Because the poverty lines grew more slowly than overall inflation, the consumption basket of the poor became relatively cheaper, contributing to poverty reduction. The rapid growth of international remittances, which increased from 10 percent of GDP in 2000 to more than 17

Figure 3: Poverty Rates in Jamaica

<table>
<thead>
<tr>
<th>Year</th>
<th>Rural</th>
<th>Urban</th>
<th>KMA</th>
</tr>
</thead>
<tbody>
<tr>
<td>2003</td>
<td>10</td>
<td>15</td>
<td>5</td>
</tr>
<tr>
<td>2004</td>
<td>9</td>
<td>16</td>
<td>5</td>
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<td>2005</td>
<td>8</td>
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<td>2006</td>
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<td>2007</td>
<td>6</td>
<td>19</td>
<td>5</td>
</tr>
<tr>
<td>2008</td>
<td>5</td>
<td>20</td>
<td>5</td>
</tr>
<tr>
<td>2009</td>
<td>4</td>
<td>21</td>
<td>5</td>
</tr>
</tbody>
</table>

Source: STATIN

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2 It should also be noted that the poverty elasticity of growth is greater in absolute value when the initial headcount ratio is lower.
percent of GDP in 2007, was another factor in the growth of per capita consumption. Although it is not quantifiable, informal support from criminal gang networks may also explain a part of the growth in per capita consumption of poorer households. With respect to inequality, the Gini coefficient fell from 38.3 in 2003 to 36.8 in 2007. Already in 2003, Jamaica was the least unequal country in Latin America and the Caribbean. However, inequality continued to decline between 2003 and 2007, with all measures of inequality decreasing over the same period. The reduced inequality contributed significantly to the overall reduction in poverty during 2003–07.

15. **Gains for the poor have been broad-based across urban and rural areas.** Poverty declined substantially in all three main localities: the Kingston metropolitan area (KMA), other towns, and rural areas (see figure 3). Although urban areas excluding KMA registered the greatest percentage decline in poverty, these areas account for less than a quarter of Jamaica’s poor. Thus, the primary driving force behind the decline in aggregate poverty has been the lower poverty headcount in rural areas, which had a high concentration of poor in 2003.

16. **The poverty headcount is higher for households with a female head, mainly because these households have more nonworking members.** On the other hand, the poverty headcount is lower for households where the primary earner is a woman. In 2003, the poverty headcount was nearly four percentage points higher for female-headed households than for male-headed households. Without controlling for any other determinant of household welfare, households headed by males or females are equally likely to be poor. What accounts for the higher headcount among female-headed households is their larger size—the difference is the number of children. On the other hand, households with female primary earners tend to have higher per capita consumption and lower incidence of poverty than households with male primary earners. Several factors explain this difference. First, households where the primary earner is female have significantly more working-age members than households with male primary earners. Moreover, female primary earners are much less likely than male earners to work in agriculture, which pays significantly less than other sectors, or to live in rural areas, which have lower levels of welfare and a higher incidence of poverty.

17. **Poverty among households in which the primary earner works in agriculture has fallen substantially, but at a slower rate than for households with primary earners in other sectors.** The headcount among households in which the primary earner works in agriculture declined from 37.3 percent in 2003 to 22.6 in 2007, with a brief spike in 2006. However, poverty among households with the primary earner in service sectors fell one-third faster. Two related developments explain this pattern. First, most of the aggregate reduction in poverty occurred in the rural areas, but the rate at which poverty fell was faster in urban areas and KMA. Second, the size of the agricultural sector—measured by the share of households with the primary earner in agriculture—declined steadily from 23 percent in 2003 to 19 percent in 2007. Normally, the richer households—those with greater physical and human capital assets—are more likely to exit the agricultural sector, and households that do not shift into nonagricultural occupations tend be worse off.

18. **A drop in the importance of education as a determinant of household welfare and a slight narrowing of welfare differences between the employment sectors of principal earners contributed to the observed reduction in inequality.** Between 2003 and 2007, the real wage premiums of completing progressively higher levels of education did not exhibit an obvious pattern. However, the effect of the level of education of the primary earner on overall household welfare appears to have fallen over time. On the other hand, part of the
observed decline in inequality between 2003 and 2007 was also driven by a narrowing of welfare gaps determined by the primary earner’s employment sector. After controlling for the level of education and the primary earner’s years of experience, the narrowing can be seen as a potential sign of some improvement in the functioning of the labor market.

WEIGHING THE FACTORS BEHIND LOW GROWTH

19. The list of potential causes of Jamaica’s low growth is large, and sorting out their relative importance is complex. Chapter 1 of this report shows that Jamaica’s economy has grown more slowly than that of most other countries over the long term. Poor growth performance has occurred in spite of political stability since independence in 1962, several market-oriented reforms since the 1980s, and relatively high rates of private investment over the years. On the other hand, despite low growth, poverty continued to decline and income distribution improved over time, creating a better social environment (see chapter 2). Jamaica’s poor growth performance may have several explanations—among them natural disasters, mismeasurement of GDP and capital stock, low public investment, low productivity of capital, wages rising faster than productivity, distortions from tax incentives, high tax rates, high public debt and crowding out of private investment, inadequate human resources, migration of skilled labor, disincentives from large inflows of remittances, the high cost of crime, poor export performance, lapses in governance, and slow advances in technology. From a policy perspective it is necessary not only to identify constraints but also to understand their interactions and to generate a hierarchy of “most” binding constraints. These are the restraints that, if removed, would yield the largest payoff in terms of economic growth.

20. Chapter 3 reveals that Jamaica still underperforms even after controlling for possible mismeasurement of GDP and capital stock. Measurement problems due to rising informality may have led to underestimations of GDP in certain periods, but they cannot explain low growth over four decades. Natural disasters no doubt pushed up Jamaica’s level of replacement investment, but Jamaica still underperforms other Caribbean and Central American countries that are equally subject to major natural disasters. Investment in crime prevention is significant, but it affects the productivity of investment rather than reducing the country’s rate of investment relative
to other countries. Complementary public investment is not lower than in comparator countries that have grown faster. The level of investment in construction is also no higher than in regional comparators.

21. Jamaica’s large number of tax incentives create significant distortions, with possible negative impacts on innovation and productivity. The incentives provide relief from income taxes on earnings and grant eligible enterprises concessions on import taxes and duties for up to 15 years. Some incentives provide other benefits, such as capital allowances. The fact that tax incentives can be discretionary generates complex distortions. The sectors that have benefited the most are tourism, industry, bauxite and mining, agro-processing, creative industries, shipping, and information and communication technology (ICT). Some studies of Jamaica’s incentives suggest a substantial bias in favor of capital-intensive projects, particularly larger projects. Such tax exemptions encourage informality in the business sector and penalize firms with small amounts of capital, a characteristic of the large majority of native firms. Jamaica’s nominal income and corporate tax rates are relatively high in comparison with those of other Caribbean countries, but effective tax rates are heterogeneous and extremely low for some sectors. Among the largest taxpayers, for example, the collected tax rates were 2 percent for the telecommunications industry, 5 percent for the hotels/tourism industry, and 9 percent for construction (figure 4). Corporate income tax (CIT) incentives allow projects with negative rates of return on investment to be profitable for the private sector. The allocation of capital implied by such a state of affairs is highly inefficient. The evidence suggests that the tax regime could be a binding constraint on Jamaica’s growth because it distorts capital accumulation.

22. Many Jamaican firms complain about access to finance; however, the evidence does not give strong support to the argument of public debt crowding out private financing. From a macro perspective, Jamaica does not restrict capital flows and has, in fact, promoted foreign direct investment (FDI) with fiscal incentives. It has large inflows of workers’ remittances that could be invested if there were good opportunities. Instead,
the money has been consumed or invested in housing. National saving rates are in line with Jamaica’s level of development. Jamaican firms show good indicators when compared with businesses in other economies. Real interest rates are not high. Financial regulations have improved since the crisis of the mid-1990s. On the more intuitive side, Jamaica has been able to invest at a high level compared with other LAC countries, even after controlling for over-estimates. If a financing constraint exists, it is not reflected in investment, and therefore its shadow price should be low. Although business opinion seems at odds with these generalizations, the ratio of complaining firms in Jamaica to those in the rest of the world indicates that financing does not show up as an important concern in Jamaica’s economy. For Jamaican business, the top three major constraints involve crime, cost of electricity, and workers’ skills. However, it is still possible that distortions in the financial markets affect the allocation of capital.

23. The available evidence shows that Jamaica has a low level of human capital, with poor quality of education and insufficient training of its labor force (figure 5), despite the country’s efforts. The country’s educational level is low for its level of development but in line with other Caribbean countries. However, the quality of education in Jamaica is low compared with other countries of similar development. The Caribbean Examination Council (CXC) general proficiency tests provide an indicator of “basic skills” development, and Jamaican students’ performance has been weak in English and mathematics (table 2). Spending on workers’ training and the stock of highly educated workers are both very low. Human capital is not abundant, and the returns to schooling in Jamaica have been extremely high for at least 25 years. The relatively low stock of human capital and the high returns to schooling are clear indicators that human capital is scarce. This problem has long been recognized in Jamaica. Several policies have been implemented, and more needs to be done. The challenges for Jamaica are raising the overall quality of its human capital, starting from early childhood, and retaining qualified workers. The brain drain has not stopped; on the contrary, the migration rate of qualified workers has increased.

24. Jamaica is one of the most crime-prone places in the world. With a murder rate of 60 persons per 100,000 inhabitants and an average of five murders a day, Jamaica has the Caribbean region’s worst record (figure 6). In fact, Jamaica’s murder rate is among the top five in the world. Crime has diverted valuable resources from productive industries into security and healthcare expenditures. The overall estimate of the cost of preventing violence or reducing its consequences is approximately 5 percent of GDP. Rising crime is also perceived as one of the main obstacles to tourism. This has been partly mitigated by the development of all-inclusive enclave resorts, where tourists can enjoy beach-
Crime may adversely affect economic activities beyond the short-run costs of prevention measures. It may also constrain business expansion by reducing final demand and limit productive work hours because of the need to close firms early. Evidence suggests that crime and violence encourage highly trained professionals and entrepreneurs to emigrate. Studies point to immense long-term economic gains if Jamaica’s crime rates could be reduced. Jamaica could experience an increase of 5.4 percent annually in its per capita GDP growth rate if it could cut crime rates to the levels prevailing in Costa Rica. The result would raise income per capita by 69 percent over 10 years.

25. **Jamaica performs very poorly on many dimensions of governance.** Jamaica’s most evident and severe problem is its crime environment, which erodes social stability and casts doubt on the rule of law. In addition, Jamaica also performs poorly on its legal system. Judicial operations, including backlogs

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3 According to Jamaica Tourist Board statistics, 85 percent of the hotel room nights sold in 2009 were in all-inclusive hotels.

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Table 2: Jamaican Student Performance on the CXC (General Proficiency, 1999-2008, % passes)

<table>
<thead>
<tr>
<th>Year</th>
<th>English Language</th>
<th>Mathematics</th>
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<td>1999</td>
<td>60.3</td>
<td>26.8</td>
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<td>2000</td>
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</tr>
<tr>
<td>2008</td>
<td>54.4</td>
<td>43.0</td>
</tr>
</tbody>
</table>

Source: CXC
in court proceedings, alternative dispute resolution, and sentencing, are areas where Jamaica performs poorly. Businessmen also perceive corruption to be particularly serious in Jamaica owing to lack of transparency. The prevailing paradigm for public-private dialogue is predominantly informal, with an alarmingly high amount of ministerial discretion in the provision of exemptions from taxes and customs duties. Informal dialogue has led to rent-seeking behavior to the detriment of the wider economy.

26. Like other countries in the Region, Jamaica does not have abundant export opportunities, and Jamaican firms have trouble absorbing new technologies and fostering innovation. Earlier advantages based on preferential treatment generated distortions that later proved to be costly—for example, in the garment industry. For other products, such as sugar and bananas, the country has lost competitiveness. At the same time, it has not been dynamic enough to find new products to overcome these shocks, and exports have become less diversified despite the appearance of some new export products of the 2000s. Survey evidence supports the hypothesis that many Jamaican firms lack the capacity to absorb new technologies, possibly because of poor educational attainments, low levels of workforce training, limited availability of specialized services and professional manpower, and reluctance of entrepreneurs to address the challenges associated with the knowledge-based economy.

27. In Jamaica, the enclave model—implemented through Export Free Zones (EFZs) and in mining and tourism industries—has not generated the most-needed spillovers. EFZs can play an important role in attracting FDI by offsetting some aspects of an adverse investment climate through world-class facilities and best-practice policies. In Jamaica’s case, crime and inefficient bureaucracy appear to be the greatest obstacles to business growth. Failure to remove these obstacles is partly addressed by creating EFZs. But a recent study points out that EFZ firms have low value added and create few production linkages with local firms. The lack of spillovers is observed in the tourism and mining sectors, too. The dominant model of all-inclusive resorts promoted by generous tax incentives favors large, isolated hotels that lack linkages to the rest of the economy. Mining employs less than 1 percent of the country’s labor force and has few linkages with the other sectors of the economy.

28. In conclusion, Jamaica’s disappointing economic performance can be traced to low productivity. Once low productivity across the economy is taken into account, the country’s generalized underperformance becomes less
puzzling. Estimations for 1992–2008 show that labor productivity was negative in 8 of 10 sectors; it was positive but negligible in manufacturing and transport and communication. In the 1960s, Jamaica’s TFP was growing faster than the world and regional averages, but it collapsed in the 1970s. Jamaica’s TFP per worker also lags significantly behind most other countries in the LAC region. Removing the factors that account for Jamaica’s low productivity will go a long way in unlocking the island’s growth potential and creating conditions for even deeper poverty reduction than in the past.

29. The main causes of Jamaica’s low productivity are (i) high levels of crime, (ii) deficiencies in human capital, and (iii) fiscal distortions.

- Crime is the most obvious and severe problem in Jamaica. It severely limits future growth, leading to a vicious circle as low growth further increases crime and higher crime rates further reduce growth. Crime erodes social stability and makes the rule of law a critical concern. It has a negative effect on human capital, creating incentives for migration. It constrains business expansion and diverts resources from productive activities to protection from crime. Because of crime and other structural conditions, investment in Jamaica tends to flow into isolated activities. All-inclusive resorts, mining, and EFZs are the best examples of this enclave development model with its low spillovers to the rest of the economy.

- Jamaica has a low level of human capital. Existing quality indicators for education put Jamaica below the average for the Caribbean region. There is evidence that human capital is a scarce factor because private returns to schooling and training are extremely high and have not declined in recent years. Jamaica also has difficulty retaining its qualified workers, as evidence by the growing migration of qualified workers. Through migration the country loses very important assets for productivity, innovation, and entrepreneurship. The Jamaican labor market is flexible, but substantial deficiencies exist in the skill content of the labor force. A large portion of the Jamaican labor force has no formal training. In 1995, as many as 80 percent of workers indicated that they had no formal training. In 2008, the figure remained high, at 72 percent. The combination of low educational attainment and low levels of training suggests an overall low quality of human capital, which hinders productivity.

- Jamaica’s fiscal policies and budget-management practices and policies constrain growth. Inconsistent, complex tax policies, with numerous exemptions and special privileges, has reduced tax revenue by an estimated 20 percent. The complex system of taxes and incentives also creates distortions for the allocation of capital and lowers investment productivity. High debt-servicing costs and a high wage bill have reduced the fiscal space available for productivity-enhancing public spending. Existing rules and organizational structures have not supported the required fiscal discipline. From a political economy perspective, the relatively sharp division of the country into opposing political camps has made it difficult to reach a national consensus and make binding commitments.

30. Given the causes of Jamaica’s low growth, policy recommendations likely to have large payoffs are reducing crime, investing more in education and training (and in retaining trained workers), removing perverse incentives, and moving away from the enclave development model. There is no silver bullet for all Jamaica’s problems, nor any single, unique binding constraint whose removal would solve them. Rather, the country requires concerted change on several fronts. It would hardly pay to improve human capital if crime were not reduced and the brain drain not staunched. Reducing crime would hardly pay if there were not better economic opportunities in the local economy. The government must therefore move forward very efficiently, which calls for urgent improvement in accountability and governance. Jamaica has to do this with limited fiscal resources. The recent debt swap will give the country more room for maneuver, but public resources will not be abundant. The country, therefore, must conceive policies that can relax its constraints to growth with minimum spending. This is not an easy task, but it requires a push for even greater efficiency, for the elimination of distortions, and for greater involvement of the private sector.

Part 1: Obstacles to Growth in Jamaica.
LABOR MARKET PERFORMANCE IN JAMAICA

31. Chapter 4 explores the main issues and challenges facing the Jamaican labor market, focusing particularly on their links to growth and labor productivity. The analysis in Part I, particularly the growth diagnostics in chapter 3, show that both labor productivity and TFP are low in Jamaica, significantly constraining economic growth. Therefore, identifying the factors behind low labor productivity and developing reform options to improve it will be important for creating an enabling environment for growth. A well-functioning labor market is critical for economic growth for many reasons. An efficient labor market contributes to growth by allocating labor to where it is most productive. High labor productivity requires (i) that employers have enough knowledge of the skills of prospective employees and how they mesh with production needs, and (ii) that employers have incentives to retain and train workers as well as the flexibility to hire and fire workers. From the supply perspective, job-seekers need to (i) know where the most appropriate openings are, (ii) be able to access these openings and present their credentials, and (iii) possess the resources and motivation to perform at full capacity on the job.

32. Jamaica is in the mid-stage of a demographic transition with positive impact on growth. However, a smaller share of the population now works or actively seeks employment. Population projections show a gradual flattening of the demographic pyramid. According to these projections, the share of the population between 15 and 64 years of age is expected to
Part II: Creating an Enabling Environment for Growth: Key Policy Challenges

rise from 60 percent in 2005 to 65 percent in 2015, remaining at that level until 2030. This demographic group approximates the country’s potential labor force, although its actual size depends on such factors as secondary and tertiary school enrollment, female labor force participation, migration, and retirement behavior. Currently, Jamaica’s labor force participation has shown a declining trend in comparison with the growing share of working age population. Labor force participation decreased from 69 percent in 1990 to 64 percent in 2009, a change that could be explained almost entirely by the sharp increase in inactivity among women. Nonetheless, compared with other LAC countries, Jamaica remains above average in female labor force participation. Between 1995 and 2008, the working-age population and employment both increased, despite declining participation ratios, while the growth rate averaged 0.7 percent. This implies stagnant labor productivity, with a sharp declining trend since 2002. Had Jamaica not benefitted from the demographic transition, growth would likely have been even slower.

Labor productivity has been low and declining since the 1970s except in a few years. Jamaica’s labor productivity has lagged behind that of most other countries. In 1980, Jamaica had a GDP per worker of $9,960 at constant PPP, marginally above that of the Arab Republic of Egypt, Morocco, the Dominican Republic, and Bolivia; and slightly lower than that of Yemen, Tunisia, Malaysia, and Bahrain. (The range was $7,627 for Egypt to $11,008 for Bahrain.) By 2008, however, Jamaica’s GDP per worker was equivalent to $8,822, higher only than Bolivia’s. Meanwhile, Malaysia had reached a GDP per worker of $25,590, and four other countries had exceeded $13,000, or 1.5 times Jamaica’s level. At the sectoral level, labor productivity has grown in mining and manufacturing, while it has declined in sectors such as construction and commerce. The improvement in manufacturing productivity coincided with the large-scale expansion of the textile industry that occurred from the mid-1980s to the late 1990s. The industry has contracted since 2000. Although volatile, mining productivity remained at high levels during 2002–06 before falling sharply in 2007. Notably, real wages have largely followed the evolution of labor productivity at the aggregate and sectoral levels, except for 1985–2002.

According to the Doing Business 2010 Report, Jamaica’s labor market regulations are flexible enough not to constrain labor productivity. The Doing Business rankings are based on methodology developed by Botero et al. (2004). As a common law country—in the tradition of other members of the British Commonwealth of Nations—Jamaica’s employment regulations are generally flexible, and the country ranks 39th globally in ease of employing workers. In particular, it ranks among the top 10 in flexibility in three subcomponents—“difficulty of hiring,” where regulation allows appropriate degrees of flexibility in the use of fixed-term contracts; “rigidity of hours,” which considers the distribution of hours during the week and year to accommodate changes in business activity; and “difficulty of redundancy,” where Jamaica maintains no legal restrictions on dismissing redundant workers. However, the generous level of redundancy payments increases the costs of dismissals and effectively limits flexibility.
The analysis suggests that low levels of educational attainment and labor force training are major constraints on realized labor productivity, whereas skills mismatch did not feature significantly in the observed decline in productivity. A large portion of the labor force in Jamaica has no formal training. In 1995, 80 percent of workers indicated that they had no training; in 2008, the share was still high at 72 percent. According to the 2006 World Bank Investment Climate Survey, a significant portion of Jamaican firms cited lack of skilled labor as a severe constraint on growth, although results should be taken with caution owing to small sample size. Available empirical studies also indicate that lack of skills is a constraint on realized labor productivity. On the other hand, an examination of advertised vacancies and unemployment rates in Jamaica reveals relatively low and declining skills mismatch. The skill formation and human capital challenges facing Jamaica have long been recognized. Over the years, various institutional and policy initiatives have been implemented to address both the quantity and quality of the human resources problem. However, more needs to be done at all educational levels and in the area of social trust.

An additional phenomenon that works against labor productivity is the high level of migration among the most skilled workers. Emigration puts additional pressure on the national educational system to produce enough skilled workers to compensate for emigration. Brain drain is likely a consequence of perceptions among highly educated individuals of limited opportunities for career development. Enhancing career prospects in Jamaica for such individuals depends ultimately on improving the country’s overall business environment and living conditions, notably by reducing crime, and on better health and education systems. The challenge is to turn the phenomenon of brain drain into a process of brain circulation, whereby the highly skilled Jamaican diaspora comes to see opportunities to engage in productive investment in the country and has the appropriate channels through which to do so. To foster brain circulation, projects may be directed toward making members of the diaspora invest directly in productive projects or act as entrepreneurs.

Informal labor, although highly prevalent in Jamaica, has been declining in importance since 1990. Despite this trend, some evidence points to a diverging distribution of wages between formal and informal labor. The country’s complex informal sector includes music and entertainment, one of the most creative and dynamic sectors of the Jamaican economy. Reducing the informal economy’s size is a challenge faced by many developing nations, one that requires strengthening both the demand and supply for formal labor. In general, this requires strengthening the demand for labor in sectors that are more likely to engage in formal employment. For this purpose, a solid business climate that gives stability for potential investors is key. On the supply side, strengthening the labor force’s skills is an important step. Individuals with tertiary education are significantly less likely to work informally. International evidence also shows that technical and vocational education that trains workers in job-relevant skills improves the chances of finding jobs in the formal sector.

**Figure 7**
Age of Entry and Education Levels for Jamaica Migrants

![Figure 7](image-url)

Source: Staff Calculations based on the American Community Survey 2009
A strategy that aims to improve the skills component of the labor force would likely help to improve labor productivity in the future.

38. The skill formation and human capital challenges facing Jamaica have long been recognized, but more needs to be done. Over the years, various institutional and policy initiatives have been implemented to address the human resources problem. A commission was established in 2003 to boost the performance of students in early-childhood education. In addition, Jamaica targets early-childhood development through a conditional cash-transfer initiative (PATH), which provides assistance to vulnerable groups and seeks to improve the health and education of the poor. The government has sought to reform the secondary-school system by improving teacher training and upgrading facilities and equipment, but the emigration of trained and experienced teachers and a high level of vacancies have hampered the reform process. The HEART Trust/NTA has been Jamaica’s main agency providing technical and vocational training. The agency trained an estimated 380,000 persons between 1982 and 2008. Overall, the Jamaican authorities have introduced several policy and institutional measures to address the severe skills gap facing the country. However, more needs to be done at all educational levels and in the area of social trust.

PUBLIC FINANCIAL MANAGEMENT AND GROWTH

39. Chapter 5 focuses on public financial management in Jamaica, with the objective of identifying policy and institutional weaknesses that create fiscal distortions that hamper growth. High debt-servicing costs and a high wage bill in the public sector have reduced the fiscal space available for productive government spending. Inconsistent and complex tax policy, with numerous exemptions and special privileges, not only reduces government revenues but also creates distortions in the allocation of capital and lowers investment productivity. The analysis in Part I, particularly the growth diagnostics in chapter 3, show that tax distortions could be a binding constraint to growth in Jamaica as they distort capital accumulation and encourage an enclave development pattern with few spillovers to the rest of the economy. The adverse effects on economic growth are magnified by other weaknesses in fiscal management, such as a weak legislative and institutional structure for debt management; inefficient public investment; weak links between government priorities, planning, and budget; the lack of in-year expenditure controls; and the lack of accurate financial statements. While the Government has made progress in strengthening the management of public finances, current practices and processes limit its ability to strengthen its fiscal position.

40. Underlying institutional and political economy factors are significant impediments for strengthening fiscal and expenditure policy and management of public finances. Existing rules and organizational structures have not supported the required stringency. From a political economy perspective, the relatively sharp division of the country into opposing political camps has made it difficult to reach a national consensus and make binding commitments. Moreover, Jamaica is grappling with an implicit social contract that includes a significant role for organized crime in the economy and society. That contract is eroding the legitimacy of the state and undermining the degree to which formal rules are regarded
as binding, which affects revenue collection, expenditure management, and other fiscal issues. Moreover, organized crime and high crime rates draw political attention to security issues and require significant spending at the expense of pressing needs for fiscal consolidation and public-sector actions to support growth.

41. Past efforts at fiscal consolidation have succeeded only partly because of structural weaknesses inherent in public financial management and the underlying political dynamics of the budget process. The key structural weaknesses that have played a significant role in Jamaica’s debt build-up and helped create a fiscal environment not conducive to growth can be grouped into five main areas: (i) weak institutions; (ii) ineffective fiscal policy (or central government revenue and expenditure policies, such as tax policy, wages, and public investment allocation); (iii) inefficient budgeting processes, including insufficient control over public expenditure and the public investment planning process; (iv) ineffective debt management practices and debt build-up; and (v) the weak management of public bodies.

42. Fiscal management in Jamaica is guided by a set of rules that does not support a strategic approach necessary to address existing challenges. Existing legislation is largely silent on budget preparation and on principles for fiscal management. It promotes treating a large share of expenditures as fixed. Budget planning is fragmented, especially for capital expenditures. Public bodies have been allowed to operate with implicit or explicit Government guarantees. Prior to the recent fiscal-responsibility amendments in 2010, there was no requirement to make the resulting fiscal liabilities explicit in budget deliberations. Supplemental budgets have been adopted at least once and in some cases twice a year (table 3). However, existing rules do not encourage sufficient scrutiny of what changes are being made with those budgets and why. Recently, the Government has adopted a Fiscal Responsibility Framework (FRF) to strengthen control over expenditures (including lending) by the Ministry of Finance and Public Service (MFPS) and to increase budget transparency.

Table 3:
Supplemental Budget Amounts and Frequency

<table>
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<tr>
<th>Financial Year*</th>
<th>Original Approved Budget</th>
<th>Revised Budget</th>
<th>Revised Budget</th>
<th>Number of Supplementary Estimates</th>
<th>Dates of Supplementary Estimates</th>
</tr>
</thead>
<tbody>
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<td></td>
<td>$,000</td>
<td></td>
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<tr>
<td>2000/2001</td>
<td>167,387,973</td>
<td>188,459,488</td>
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<td>13/03/2001</td>
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<td>2003/2004</td>
<td>261,704,873</td>
<td>279,161,324</td>
<td>-</td>
<td>1</td>
<td>02/03/2004</td>
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<tr>
<td>2004/2005</td>
<td>328,153,402</td>
<td>331,547,754</td>
<td>328,176,223</td>
<td>2</td>
<td>07/12/2004</td>
</tr>
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</table>

Source: Ministry of Finance and Public Service
43. **Key components of Jamaica’s fiscal policy, in particular its tax policy, adversely affect the government’s fiscal position and contribute to Jamaica’s consistently low growth rates.** Jamaica’s tax system remains complicated. The Government offers waivers and incentives for a large group of activities and for a variety of purposes. A significant portion of these waivers and incentives are discretionary. Complicated tax policy and resulting low tax collections create distortions in resource allocation and contribute to the country’s consistently low growth rates in at least three important ways. First, the existence of an inefficient tax structure lowers tax revenues and reduces the fiscal space for productive public spending that would boost growth. Second, the difficulty of paying taxes discourages compliance, further lowering tax revenues. Third, the complex tax and incentives system creates distortions in the allocation of capital and decreases the productivity of investment, lowering the potential growth of the Jamaican economy. On the other hand, public sector employment and the resulting wage bill continue to be a source of fiscal pressure. Social partnerships and collective bargaining for public sector wages have had limited traction in controlling the wage bill owing to the politicization of key unions and the fragmentation of unions and staff associations. The public investment planning process is neither strategic nor comprehensive. Systems are weak for ensuring that public investment allocations are clearly prioritized and aligned with strategic development plans and programs. Public investment undertaken by public bodies is not included in the overall public investment plan. The execution of public investments has also been an area of some concern.

44. **Jamaica has long carried a high public-debt burden; despite this, legislative and institutional frameworks remain weak.** While debt management has improved significantly, it is still plagued by substantial weaknesses, including the lack of a comprehensive medium-term debt-management strategy, the absence of legislative and institutional frameworks for consolidating the debt-management process, and the lack of borrowing limits. The legislation governing debt management is fragmented and does not include aspects of modern debt-management laws. Jamaica prepares debt-management strategy but with inadequate focus on medium-term risk and sustainability. Restructuring of the Government’s debt management unit into front, middle, and back office functions is still pending. The lack of effective coordination between the debt management unit, the central bank, fiscal policy, and cash management constrains debt management by increasing ad hoc issuance of debt that may weaken adherence to the debt-management strategy.
45. Achieving fiscal consolidation and reforming the tax system can be painful and politically unattractive. It is important, therefore, to give careful consideration to how such a policy stance can be made politically feasible. Tax reforms would require a broad social consensus, as any effective reform would have winners and losers. Fiscal consolidation would have to be pursued over a five-year horizon or longer. As such, it would include at least one election. In the interest of national recovery, the main political parties should publicly commit to tax reforms and fiscal consolidation as a sine qua non—to avoid populist competition over who is willing to spend more.

46. It will be important for Jamaica to move forward on tax reforms and fiscal consolidation in ways that are politically feasible and robust. Any strategy will require good communication by the government on the reform steps being taken, the available policy choices, and the reasons for favoring or disfavoring each. The public should see that the costs associated with reforms are allocated fairly across different groups in society. The strategy should include a clear protection of the poorest while making it clear that most, if not all, other groups will have to contribute to reforms. Good communication on difficult policies characterized Jamaica’s agreement with the International Monetary Fund (IMF) and the Jamaica debt exchange (JDX) of February 2010. These experiences with good communication and transparency should be replicated.

Figure 8: Public Debt in Jamaica

% of GDP

Source: Ministry of Finance and Public Service
47. **Jamaica has been in a low-growth, high-fiscal-deficit, and high-debt equilibrium for some time.** From an institutional and political economy perspective, this raises the question of why politicians have not sought to address the situation and change the status quo. Jamaica has had a democratic political system since independence. In principle, such a regime should generate incentives for politicians to heed the demands of citizens. Furthermore, one would expect that voters care about growth because it generates employment and other economic opportunities. But even though growth has been low for long periods, voters have reelected incumbent parties multiple times (figure 9). Three key factors help explain this paradox. They are (i) Jamaica's high degree of political polarization, (ii) high emigration rates among skilled workers (and sophisticated voters), and (iii) fragmentation of one of the main parties, which allowed the other main party to continue in government.

48. **Recognizing the complexity of technical reform and the underlying political dynamics, the way forward should be pragmatic and based on a two-phased approach of medium-and long-term reforms.** Several technical reforms would be relatively easy to implement because they do not require regulatory changes and can provide positive short-term results in the management of public finances. Some of these involve actions to strengthen the implementation of existing regulation. These include establishing consistent standards for commitment control to improve in-year control of budget execution and public bodies. Medium-term actions to make more systemic changes would require more effort and time to implement. These include tax reforms, stronger links between planning and budgeting, and limits on permissible changes in the allocation of supplemental budgets. With ongoing political commitment, Jamaica can be successful in undertaking reform to strengthen its fiscal position.

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**Figure 9: Fiscal Deficits, Elections, and Growth: 1992–2009**

- **Source:** Ministry of Finance and Public Service
49. Using a simulation model, chapter 6 analyzes potential growth and distributional impacts of recently implemented policies as well as possible reforms for enhancing growth. The forward-looking exercise compares a set of alternative scenarios for 2007–20. These scenarios are (i) business-as-usual with no reform, (ii) tax reform, (iii) JDX, (iv) adoption of the Fiscal Responsibility Framework (FRF), (v) accelerated productivity growth, and (vi) changes in the skill content of the labor force. The results of these simulations are then mapped to the 2007 Jamaica Survey of Living Conditions to explore the potential impacts on household welfare, poverty, and the distribution of income. The model assumes three representative households—unskilled rural, unskilled urban, and skilled. This categorization is important because the three household types vary substantially in their sources of income.

50. The business-as-usual (BaU) scenario incorporates the adverse impacts of the global food, fuel, and financial crises of 2008–09 and projects a smooth but gradual recovery during 2011–20. The combined impacts of the food, fuel, and financial crises led to a cumulative loss of 4.6 percent of real GDP in 2008–10 (relative to 2007). From 2011 onwards, under the scenario, the economy recovers and achieves annual growth of 2 percent by 2012 and 2.1 percent in 2014 and each year thereafter. The baseline growth is plausible, as the recent crisis created considerable slack in the economy. Per capita income grows at an average annual rate of 0.8 percent over the entire period 2007–20.

51. The BaU scenario reveals that debt sustainability was at great risk without policy reforms implemented in 2008–10. Under the BaU scenario, the Government maintains a fairly strong fiscal stance, with noninterest recurrent outlays remaining at 13 percent of GDP and capital expenditures stable at 3.4 percent. This enables the government to continue recording strong primary surpluses, averaging
6.1 percent of GDP between 2007 and 2020. However, the high level of existing debt and high costs of debt service push the economy toward increasing debt. By 2012, the stock of public debt exceeds 150 percent of GDP and continues to rise to above 200 percent of GDP by 2020. These debt dynamics illustrate the difficult situation and the pressing need for fiscal and debt reform that faced the government in 2009–10. Despite the global recovery, and even with strong primary surpluses, the debt trajectory would likely have been unsustainable without the aggressive policy actions the Government took.

52. Under the BaU conditions, poverty and inequality are likely to continue their downward trends but at slower rates than in the past. Poverty is likely to continue to decline but at a slower pace. The micro-accounting exercise conducted as part of the simulation suggests that the moderate poverty headcount could fall by another 3.5 percentage points in the BaU scenario, while the Gini coefficient could decline by half a point. The main reason the BaU scenario does not deliver more poverty reduction is the relatively slow rate of growth in per capita consumption.

53. The first alternative scenario incorporates the major tax changes in fiscal years 2009 and 2010 as well as JDX (February 2010). The JDX-plus-tax reform scenario introduces the expected revenue effects of the tax amendments implemented in FY 2009–10. In addition, the scenario takes into account the decrease in the rate of interest paid on domestic and foreign debt after the JDX. The improved fiscal outcome of this scenario makes a strong case for strengthening revenue collection because it puts Jamaica on a declining debt path. The immediate effect of the tax reform is a J$19.7 billion increase in indirect tax revenue in 2010, somewhat below the Government’s forecast of a J$26.3 billion increase. At the same time, the JDX saves the Government another J$26.9 billion in interest in 2010. Therefore, the overall result of the policy change is an improvement in the overall balance equal to 5.3 percent of GDP in 2010. This substantial strengthening of the fiscal position broadens the resources available to the Government for making debt payments and decreases borrowing needs. Debt ratios stop rising immediately. By 2014, the debt-to-GDP ratio falls to 130 percent, and it continues declining to 120 percent of GDP by 2020. Reduced borrowing needs also play into the virtuous circle of lower debt and higher overall balance: compared with the BaU scenario’s interest payments of 24 percent of GDP in 2020, interest costs in the JDX-plus-tax reform scenario are 12 percent of GDP in the same year. The lower interest payments limit the overall deficit to just 3.4 percent of GDP, compared with a projected 17 percent in the BaU case.

55. The improvement in the fiscal position has important positive spillovers for real GDP growth. Initially, growth is depressed by the tax increase—the contraction in 2009 is 2.6 percent, rather than 2.5 percent without the tax increase. However, growth recovers quickly. By 2015, it is 0.2 percentage points higher than under BaU; by 2020, the premium widens to 0.3 percentage points. As a result, GDP per capita in 2020 is more than 2 percent greater than under the BaU scenario. The positive growth spillover is due mainly to the decreased borrowing needs of the government, which has a positive impact on private investment. Real consumption per capita remains unchanged from the first reform scenario. This is because the JDX-plus-tax reform scenario in reality represents a transfer of resources within the economy and does not generate new income.

56. The reform scenario leads to slightly greater poverty reduction and lower inequality. The moderate poverty headcount could fall by an additional 0.3 percentage points, while the Gini coefficient could decline by a quarter points. However, there are several reasons to doubt that this scenario would produce a big boost in poverty reduction. First, consumption per capita does not increase relative to BaU, which means that poverty reduction can come only from distributional changes. Second, some distributional changes are pro-poor, but others are biased against the poorest households. These include the overall increase in general consumption tax (GCT) rates, which hurts poor households that spend all of their
income on consumption, and the large increase in demand for investment goods, which do not require rural factors in the production process. As a result, the wages of unskilled rural households decline under the first reform scenario relative to those of unskilled urban and skilled households.

57. The second reform scenario strengthens fiscal discipline even more through the adoption of the FRF, which limits fiscal deficits and further improves debt dynamics. In this scenario—in addition to implementing the tax reform and the JDX—the Government adheres to a fiscal rule whereby the overall deficit is kept below 2 percent of GDP in every year after 2011, with capital expenditures bearing the brunt of adjustment. This fiscal rule is just an assumption, and other adjustments could be made in the budget to reach a given deficit target—for example, reducing wage or non-wage recurrent expenditures. The slower accumulation of debt in the preceding years brings down final-year debt ratios even further than under the first two scenarios. Instead of 200 percent in the BaU scenario and 120 percent of GDP in the JDX-plus-tax reform scenario, the debt-to-GDP ratio now declines to below 106 percent by 2020. As in the previous reform scenario, the reduced borrowing needs of the Government lessen the crowding out of private-sector investment and yield some small growth spillovers. However, most of the debt reduction in the second reform scenario occurs from slower debt accumulation, not faster growth.

58. The third reform scenario assumes higher productivity growth in addition to the tax reform, the JDX, and the FRF. Jamaica can improve its level of productivity by, for instance, reducing crime, enhancing human capital accumulation, and lowering the debt overhang. In the BaU scenario, productivity grows at an average annual rate of 0.7 percent, similar to the country’s observed TFP growth between 2000 and 2008. To reach a post-crisis (2011–20) average real GDP growth of 3.0 percent, productivity growth would have to rise to 3.9 percent a year, or 1.8 percent a year for the entire 2007–20 period. These implied rates of productivity growth would be high by both regional and international standards. However, they underscore the challenges facing an economy where high investment rates have not translated into accelerated growth, population growth is slowing, the educational system has struggled to produce enough skilled workers, and emigration rates are high for skilled workers.

59. The fourth reform scenario assumes higher share of skilled workers. Low labor skills and training are key constraints to growth in Jamaica. The country can increase its growth potential by improving labor skills, retaining educated workers, and reversing the brain drain. In 2007, just 28.7 percent of Jamaica’s employed workers were skilled, using the definition of a secondary-school certificate. Productivity, growth, and export performance all rise in an alternative scenario that brings the share of skilled workers to 30 percent by 2020, compared with 28.7 percent in the JDX-plus-tax reform scenario. Overall productivity increases resulting from higher skill content of the labor force and higher incomes associated with higher productivity give rise to greater saving, investment, and capital accumulation. As a result, real GDP in 2020 is 0.7 percentage point higher than in the JDX-plus-tax reform scenario. The real GDP growth rate accelerates because of higher skill content, and gains would likely be larger in later years. Exports in 2020 increase by 0.75 percent relative to the JDX-plus-tax reform scenario, becoming more intensive in manufacturing and less intensive in sectors that tend to use a less skill-intensive input mix, such as agriculture and services. The additional supply of skilled workers lessens the upward pressure on skilled workers’ wages. At the same time, unskilled workers become relatively scarcer and therefore receive higher wages than in the JDX-plus-tax reform scenario. However, these changes are quite minor and do not have a material effect on aggregate inequality.

60. The simulations show that the tax reforms in FY2009–10 and the JDX of 2010 were necessary to maintain debt sustainability but may not be sufficient to generate higher growth. Investment in accelerating labor productivity growth and raising labor’s skill content can pay important dividends in faster growth.
growth and improved export performance. Under the JDX-plus-tax reform scenario, the debt-to-GDP ratio in 2020 is half that of the BaU scenario. Growth performance and poverty reduction also improve in the first reform scenario, and the fiscal position is strengthened substantially. Additional fiscal consolidation—achieved by adhering to the FRF’s fiscal deficit rule (applied in the second reform scenario)—can yield further growth and debt reduction benefits, but policymakers must use caution in identifying expenditure cuts. In most cases, capital expenditure is one of the first items cut when nations face overall resource constraints. As the simulations in this report show, however, reducing productive public capital expenditure may lead to lower growth through negative productivity spillovers, largely nullifying the benefits of additional fiscal consolidation. Jamaica’s growth performance can be improved by investing in measures to accelerate growth in labor productivity and raising labor’s skill content. The simulations do not specify the channels through which these improvements can or should be realized. The key lesson, however, is that these types of reforms, if successful, can exert strong growth effects on real GDP and export performance. Therefore, they should be prioritized and explored in more detail.
The potential for accelerating future growth rests primarily on the ability of Jamaica to remove or at least ease the key obstacles to growth identified in Parts I and II of this report. Once the key obstacles are removed, Jamaica can further accelerate growth by enhancing private sector development. The analysis in Parts I and II of this report identified a number of growth obstacles—chiefly low productivity caused by deficiencies in human capital, high crime, and distorted tax and incentive regimes. Removing or easing these obstacles will be critical for creating an environment conducive to growth and broad-based economic development. Improvements in the macroeconomic environment should encourage the private sector to invest and produce more. Jamaica’s private sector, however, faces additional constraints specific to the business environment. Primary products and tourism have increasingly dominated exports, and the expansion into the textile industry in the 1980s was quickly overrun by pressures from regional and global competitors. Sectoral growth rates in Jamaica have lagged international competitors, and Jamaican exporters have been losing global market share, even in areas of increasing specialization such as tourism. The country has not taken advantage of opportunities to move into new, fast-growing products or to use its current exports as a launching pad for broadening its array of products. These failings point to ways in which Jamaica can further benefit from improving the business environment, increasing export orientation, and laying the ground for a long-term focus
on private sector development. Chapter 7 explores the private sector dimension of growth in Jamaica over the past few decades, focusing on sectoral growth, export performance, and the business environment.

62. One of the main features of the Jamaican economy’s development in the past two decades has been the steady decline in the share of manufacturing and the large increase in the importance of services. In 1995, the services sector accounted for just over half of total value added; by 2007, it accounted for 70 percent of value added and more than half of exports. The services sector is also the largest employer on the island, averaging 63 percent of employment during 2004–08. Within services, the composition has been relatively stable over the past two decades. The growing importance of services and construction in total employment has come at the expense of employment in agriculture and manufacturing, which have seen their employment shares decrease. Manufacturing was the third most important sector in Jamaica in the 1990s, with 12 percent of total value added, but it decreased to around 9 percent in the 2000s, sinking to fourth below transport and communications. Within manufacturing, most of the decrease in activity came from the decline of the apparel industry in the second half of the 1990s.

63. The sectors performed differently in terms of their profitability and their ability to attract FDI. For the services sectors, large profitability losses occurred in the 1990s, whereas in the 2000s profitability was much more stable. Most types of services neither lost nor gained profitability in the previous decade, although wholesale and retail trade sagged. Finance and insurance was an exception, scoring considerable gains. Among the service sectors for which FDI data are available, tourism led the way, followed by ICT. The performance in non-services sectors was also diverse, with agriculture, manufacturing, and electricity performing well and mining falling behind.

64. As a small, open island economy, trade has historically been very important to Jamaica, representing 111 percent of GDP in 2008. Jamaica’s export performance, however, has been weakening. The importance of exports in overall GDP has dwindled since the early 1990s, driven in part by a dramatic decline of the apparel industry. Although exports have since recovered, their current share of GDP is still below what it was in the early 1990s. Between 1980 and 2008, goods exports grew at an annual average of 4.4 percent, considerably below the Latin America average of 8.9 percent. Consequently, Jamaica’s global market share in goods has been falling since 1980, while the average for Latin America has been increasing. Jamaica’s main export products—sugar, bananas, and textiles—have suffered greatly from the erosion of trade preferences. The share of textiles and apparel in total Jamaican exports fell from 26.2 percent in 1995 to 2.3 percent 10 years later. The mining industry remains an important foreign exchange earner in Jamaica, although its performance has varied with swings in global prices. As with trade in goods, Jamaica has lost global market share in tourism and the broader services sector. And like the rest of the Caribbean, Jamaica depends on services for a large share of exports—around 55 percent in 2008. However, even in services
exports, Jamaica lost ground. Its share of world service exports stood at roughly 0.13 percent between 1988 and 2000, and it declined to less than 0.08 percent in 2008. Travel is the main foreign exchange earner for Jamaica’s services sector, accounting for 72 percent of service exports and 42 percent of total exports in 2008.

65. Not only has the performance of leading Jamaican sectors trailed international competitors, but their emergence has also steered the country toward an enclave economy. Mining, principally bauxite and alumina, is highly capital intensive, but the initial impact of the investment is not in line with its size, given that most of the capital goods and services used are imported. Mining employs less than 1 percent of the country’s labor force and has few linkages with the other sectors of the economy. The tourism industry employs approximately 80,000 people directly and 180,000 indirectly, making it responsible for 10 percent of total employment. In many other countries, tourism has major spillover effects; by contrast, intersectoral linkages from Jamaica’s tourism industry are weak and have been exacerbated by the promotion policies aimed at this sector. Similarly, ICT has been a strategic and fast-growing sector, promoted through tax incentives. Some of these benefits are included in the Export Free Zone Act, an arrangement that could prevent the development of strong links between firms located in these zones and other sectors or enterprises.

66. Jamaican exports have become increasingly concentrated over time, both in terms of products and markets. The top 10 exported products represented 81 percent of total goods exports in the 1980s and 1990s, and this ratio rose to 88 percent in the 2000s. The country’s export concentration is high by both global and regional standards, and it is rising. In the 2000s, Jamaica exported fewer types of products than in the 1990s. Jamaica’s diversification in export markets has also been low. The United States is Jamaica’s most important export destination by far, and U.S. citizens account for the largest part of tourist arrivals. The United States, the United Kingdom, Canada, and the Netherlands continue to account for most of Jamaica’s merchandise exports—as a group, 65 percent in 1991, 71 percent in 2000, and 68 percent in 2008. Between 1998 and 2008, Jamaica had some success in expanding the number of markets reached by its products. However, volumes of products exported did not increase greatly. According to research on opportunities for learning and new product development, a country that is very specialized in one product may have difficulty developing new products and diversifying its production and exports. This is because the actual exportable products are few, and producing new products requires knowledge and technologies that the country cannot easily derive from the production of its few existing goods. In other words, the variety of goods produced and the relevance of the country’s production technology for the production of other goods that are widely traded in world markets determine the potential of a country to diversify its production and exports. In Latin America and the Caribbean, only Trinidad and Tobago has a lower potential than Jamaica for producing new goods for export. Jamaica has 15 percent of Brazil’s opportunities, for example.

67. Studies of the Jamaican business climate find that firms encounter important constraints on their operations. Surveys of Jamaican businesses confirm concerns over productivity, workforce quality, and brain drain as important constraints on their operations. On the Doing Business indicators, Jamaica lags behind its regional competitors in such indicators as ease of paying taxes, enforcing contracts, registering property, and trading across borders. Jamaica’s taxation on profits is particularly high when compared with its neighbors. Tax regulations are onerous and cumbersome, including a myriad of tax incentives for various sectors that add distortion and excessive discretion in the allocation of resources. On average, firms make 72 payments a year, which eat up 414 hours of staff time. The Global Competitiveness Index highlights additional areas of the business environment that are particularly challenging for Jamaica. These include concerns over crime and violence and its toll not only in human lives, but also in terms of additional costs for firms doing business in Jamaica. Jamaica’s rate of intentional homicides is much higher than in neighboring countries that compete with
Jamaica for FDI. Among the business environment issues, violence and crime may arguably be the most important, given their pervasive effect on many other variables that influence business operations and growth. Greater public-sector efficiency, increased access to finance, a lower tax burden, and improvements in labor-force quality are also areas where respondents say Jamaica needs to do more to improve its competitiveness. Jamaica also underperforms in terms of logistics, compared with some of its neighbors and regional averages. Studies on competitiveness in Jamaica identify the cost of energy as a major impediment to investment.

68. The analysis represents an opportunity for public sector reforms that can help improve the country’s business environment. Jamaica can benefit significantly from reforms to improve the business environment, increase export orientation, and enhance private sector development over the long term. An improved environment would stimulate productivity in sectors where Jamaica has a comparative advantage, as well as encourage the emergence of new activities. Meanwhile, the private sector must move away from the poor performance of past decades and enhance competitiveness, improve diversification, and raise productivity by, among other things, investing in on-the-job training for workers.

TWO INDUSTRY CASE STUDIES: FOOD PROCESSING AND TOURISM

69. Jamaica can improve its export performance by exploiting the sectors in which it enjoys comparative advantages. The analysis presented in chapter 7 demonstrates that Jamaica’s export performance has long been weak and that poor product and market diversification are major challenges for increasing exports. Chapter 8 reviews the performances and main challenges faced by Jamaica’s food-processing and tourism sectors. These sectors were chosen because of their importance to overall economic activity on the island, their capacity to facilitate diversification of the Jamaican economy, and their potential to create linkages with small and medium-sized enterprises (SMEs) and so to support local community development. These sectors are different—one is in manufacturing, the other in services—but they face a similar challenge: how to diversify from their currently predominant activities to better use Jamaica’s natural endowments. At the same time, both sectors can improve their linkages to local SMEs, helping to increase demand for goods or services that local firms may be able to provide. In this regard, the two sectors provide a microcosm of the country’s development challenges and opportunities.

70. While becoming increasingly important for the manufacturing industry, the food-processing sector in Jamaica has nonetheless seen its contribution to total GDP decrease steadily over the past two decades. The food-processing industry includes activities that add value to agricultural and aquacultural raw materials. These activities include dehydration, production of concentrates, meat packing, milling, and canning. As such, food processing involves a vast array of products—from fruits, vegetables, and staple foods (wheat, corn, rice) to marine and meat products. Total food-processing value added in Jamaica approached US$600 million in 2008. As of June 2010, the food-processing sector, including beverages and tobacco, had 183 registered firms in Jamaica, with 13,950 employees, a number that probably reflects only the formal employment in the industry. Labor force surveys provide a broader measure of employment in the sector. In 2008, they show that the sector had 29,153 workers. The majority of formal firms are of medium size, employing between 10 and 49 workers. Food processing’s share of GDP declined from 6.1 percent in 1992 to 4.3 percent in 2008, mirroring the overall decline of manufacturing’s profile in the Jamaican economy. Between 1993 and 2008, the sector actually posted real average growth of -0.2 percent.

71. Exports of processed food products have fared better than those of unprocessed products, and some subsectors have shown robust growth. Nonetheless, the lack of product and market diversification remains a challenge. The industry’s overseas sales have grown at an average of 4.5 percent since 1997. Some subsectors performed above the industry av-
verage, notably beverages. Others have also reported reasonable growth rates, including the category “preparation of vegetables, fruits, nuts, or other parts of plants” and “sauces and spices.” These trends suggest the potential for growth and dynamism in Jamaica’s food-processing industry. Food-processing industry exports have shifted toward beverages, spirits, and vinegar, while sugar’s share has declined. In 2009, beverages, spirits, and vinegar accounted for roughly 65 percent of the food-processing industry’s export earnings. Much of that growth came from the development of the ethanol industry, whose exports grew from USS2.5 million in 1998 to USS170 million in 2009. Lack of diversification remains a main challenge, however. Jamaica’s food-processing industry is less diversified than in other Caribbean economies. The United States, United Kingdom, and Canada accounted for at least three-quarters of the industry’s exports in the past decade, reflecting the fact that country’s food-processing exporters have concentrated on reaching the Jamaican diaspora rather than mainstream markets.

72. **The sauces and spices subsector highlights the potential for growth and linkages to the local economy**. The sauces and spices subsector accounted for about 2.5 percent of total food-processing exports in 2009. While a small subsector, sauces and spices has growth potential because, compared with segments such as beverages, food preparation, and cereals, it has a better overall combination of rising exports, high SME participation, potential linkages to local agriculture, and potential for competitive advantage. The latter includes exporting a value-added product that leverages Jamaica’s unique country-of-origin attributes—aromatic flavoring, taste, and pungency. These unique attributes, if packaged together with organic certification, could help Jamaica expand its presence in existing markets, especially in North America and the European Union.

73. **Jamaica’s sauces and spices exports have grown steadily since 2001, but the country can do better**. Jamaica’s export performance in its traditional markets has not been encouraging, and the country is not connected to fast-growing world export markets. Jamaica exported USS10.5 million worth of products in 2009, accounting for 0.1 percent of world exports. The United States was the top importer, accounting for more than USS7.3 million of products. It is natural for the United States to be Jamaica’s top importer because of its proximity and the large Jamaican diaspora in the United States. However, Jamaica could do more to connect to dynamic, fast-growing markets. Imports of sauces and spices by Brazil, Saudi Arabia, and Hungary, for example, have grown at significantly higher rates than Jamaica’s current main markets, but Jamaica did not export sauces or spices to any of them in 2009. One way for Jamaica to maintain and expand its market share in the more mature North American and European markets is to focus on emerging niches, such as organic and ethnic foods. A significant trend in the food-processing industry in recent years has been the exceptional growth in demand for such foods. Worldwide, the organic food market has been growing by 20 percent to 30 percent annually in recent years.

74. **An industry focus group analysis conducted in Kingston in March 2010** identified the major constraints affecting the country’s food-processing industry (figure 8). Quality, consistency, and reliability in the supply of raw materials were identified both as a constraint and as an important gap relative to some competitor countries. Processors report that they must maintain significant and expensive inventories of semi-processed raw materials in order to compensate for fluctuations in supply. Other important factors that affect availability of raw materials include inadequate infrastructure, lack of adequate knowledge of the best growing techniques, and poor post-harvest care. Packaging is the second-most-important constraint that the focus group identified. Past efforts to address packaging costs were not successful. The high cost of certification to meet minimum market requirements has been a significant constraint to SMEs in the food-processing industry. This constraint is felt more by those firms trying to export, affecting both market access and product competitiveness. Electricity, the availability of skilled labor, cumbersome tax procedures, crime, and low levels of trust in...
society are also major concerns in the food-processing industry.

75. Strategic actions are needed to loosen constraints and provide a comprehensive approach for the food-processing industry. Losses in competitiveness and export shares in world markets can be partly explained by the inability of the sector to diversify into more dynamic markets. To reach new markets, however, several links within the food-processing value chain must be strengthened. Among them are these:

- **Sourcing of key inputs**: Efforts to strengthen linkages between agricultural producers and the food-processing industry should be continued; however, current initiatives should be monitored and assessed for effectiveness. Packaging should be promoted as a key element of a strategy to access new markets.

- **Market information**: Industry associations and government trade-promotion bodies will have to do more to provide relevant, targeted, and up-to-date information on market trends and requirements.

- **Access to certification**: For the Jamaican sauces and spices subsector, efforts at improving access to certification should include prioritization of quality standards according to market-access requirements, improving interagency coordination between certification bodies and export-promotion organizations, and creating forums for public-private coordination.

- **Market strategies**: All these initiatives should be part of a wider effort at defining market strategies to improve export performance. Technical assistance may be needed, especially for SMEs, to enhance the capacity of the industry and its firms to formulate better market approaches, including product development and distribution strategies.

76. **Tourism** is one of the Jamaican economy’s most important sectors, accounting for about 42 percent of foreign-exchange earnings from the productive sectors (goods and services) in 2008. Tourist arrivals in 2009 totaled 2.7 million overnight visitors and cruise passengers. The estimated direct contribution of
tourism to Jamaica’s overall GDP ranges from 7.3 to 8.1 percent annually, the latter figure representing 2009. A broader assessment of tourism’s impact on the economy raises the figure around 28 percent of GDP. Direct employment is estimated at an average of 7.5 percent of Jamaica’s total (formal) employment for the period 2005–09. In the last year of that period, the hotels and restaurant services sector employed more than 78,000 people. The growth rate in Jamaican tourism has not been sufficient to maintain its share of the island’s services economy, nor has it kept up with the rest of the world. Jamaica’s average annual growth rate of 5.3 percent for 1991–2009 trailed its Caribbean competitors.

While Jamaica’s tourism sector includes many small and medium enterprises in hotels and restaurants, most of the investment and expansion in accommodations over the past five years has come in the form of larger and all-inclusive hotels. Jamaica pioneered the concept of enclave tourism through the Sandals all-inclusive hotels. The number of hotels on the island with more than 200 rooms increased from 27 in 2004 to 34 in 2008. All-inclusive hotels have increased their importance in the sector, accounting for 75 percent of total rooms in 2009, up from less than 60 percent in 2004, and 35 percent of all units, compared with 26 percent in 2004. Occupancy rates in all-inclusive hotels are markedly higher than in other types of hotels. Among the vulnerabilities inherent in maintaining a strategy of undifferentiated “sand, sea, and sun” tourism are (i) high “leakage rates” as revenues are repatriated to owners’ countries and limited linkages to the rest of the economy, and (ii) sustainability, both fiscal and environmental. The tourism sector’s linkages to the overall economy are weak in Jamaica. Given the predominance of large, foreign-owned hotels, most tourism earnings do not stay in Jamaica.4

An industry focus group conducted in Kingston in March 2010 identified constraints affecting the tourism sector (figure 10). Eco-tourism stakeholders were invited to participate so as to focus the analysis on a subsector that, given Jamaica’s natural endowments, could be an important niche for diversification. Environmental degradation has been significant in Jamaica and limits the country’s ability to use its natural endowments for a differentiated tourism experience. The industry identified labor skills as another major issue, including absenteeism, poor work ethic and customer orientation, and poor quality of service. Financing facilities do exist for tourism, but most industry stakeholders either did not seem to be aware of them or did not find them sufficient or helpful. Lack of qualified human resources at the managerial level could be a constraint. Safety and security is considered to be a major impediment for travel and tourism activities. This is particularly important in view of the sector’s ambition to diversify its base beyond the walls of enclave tourism. Lack of trust and weak observance of a “code of ethics” seem to hinder cluster initiatives aimed at improving the provision of tourism inputs and strengthening linkages to the local economy. Focus group participants and other firms interviewed highlighted the rising cost of electricity in the past few years as a threat to tourism. In addition, firms pointed to the excessive number of taxes as another constraint to business.

The Jamaican government has for some time been aware of the desirability of moving away from large-scale tourism. In 2002, a Master Plan for Sustainable Tourism was developed, with the main objective of moving the sector toward greater sustainability. The master plan attempted to avoid past implementation problems by creating a shared vision for the tourism industry through an extensive stakeholder-consultation process. The master plan is currently undergoing a mid-term review, providing some encouragement that lessons drawn from its implementation will soon become available to inform and guide current and future tourism policy initiatives.

Strategic actions are needed to address constraints and provide a comprehensive approach to sustainable tourism. The necessary strategy can be achieved by enhancing exist-

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4 The leakage rate is generally high for the Caribbean region (it is estimated at 80 percent), one of the highest in the world.
ing efforts, introducing environmental mainstreaming into policy design, and increasing private participation in providing finance for sustainable tourism. Some specific points to be addressed are the following:

- **Crime:** Taking tourists away from the highly secluded, all-inclusive resorts to areas of natural beauty and interest around the island will require special attention to safety and security.

- **Finding niches:** Mainstreaming sustainable tourism involves bringing together public-private organizations that will commit to promoting tourism through carbon-clean, green, ethical, and high-quality projects.

- **Financial issues:** The Government could improve access to existing funding mechanisms that promote sustainable tourism, such as the Tourism Enhancement Fund. Greater efforts to spread the word about the program could generate quick wins.

- **Private sector initiatives:** Green funds could be used to increase private participation in improving sustainable tourism. Green funds are global, private sector driven mechanisms to increase access to finance for environmental sustainability.

81. **Enhancing public-private dialogue and labor skills.** The food-processing and tourism industries, along with other industries, can benefit from greater public-private dialogue. Competitiveness councils (or variations thereof) that bring together high-level government decision-makers, business executives, and academics have been used to institutionalize public-private mechanisms in many countries. The challenges of Jamaica’s food-processing and tourism industries also point to the need to improve the quality and relevance of the education system, including vocational training. Here, too, better public-private dialogue and coordination could help with the feedback process. 

![Figure 13: Tourism Sector: Main constraints](image1)

<table>
<thead>
<tr>
<th>Environment</th>
<th>Availability of skilled.</th>
<th>Access to finance</th>
<th>Corruption</th>
<th>Trust &amp; Collaboration</th>
<th>Tax administration</th>
</tr>
</thead>
<tbody>
<tr>
<td>5</td>
<td>2</td>
<td>1</td>
<td>1</td>
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*Source: Kim, 2010, N=10*

![Figure 14: Tourism Sector: Gap Analysis](image2)

![Diagram showing environmental, product variety, marketing, training/HR, access to finance, and tax administration priorities for Costa Rica, Trinidad, and Jamaica](image3)

*Source: Kim, 2010*
To be implemented by government (G) or by private sector (P)

<table>
<thead>
<tr>
<th>Constraints to Growth</th>
<th>Policy Recommendations</th>
<th>Medium Term</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Issue 1: High crime</strong></td>
<td><em>Analysis of crime prevention policies is beyond the scope of this CEM. However, some widely recognized policies are noted below.</em> <em>(Also see UNODC and The World Bank 2007)</em></td>
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</tr>
<tr>
<td></td>
<td>Prevent crime through the study and design of environments to encourage desirable behavior and discourage anti-social behavior. [G]</td>
<td>Improve police and justice services. Use criminal-justice approaches to reduce organized crime, drug trafficking, and other problems not susceptible to prevention approaches. [G]</td>
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<td></td>
<td>To address issues of youth violence, borrow from the toolkit of evidence-based programs from other regions, such as early-childhood-development and mentoring programs, interventions to retain high-risk youth in secondary schools, and opening schools after-hours and on weekends to offer young people attractive activities to occupy their free time. [G]</td>
<td>Given that Jamaica is a transit country and not a producer of cocaine, complement interdiction by strategies outside the region and seek assistance from destination countries to support interdiction efforts. [G]</td>
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<td></td>
<td>Transform the culture of violence by starting a strong media campaign to build awareness of the sanctity of life and to encourage citizens to resolve conflicts in a peaceful manner. [G]</td>
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### Issue 2: Poor quality of human capital

Deficiencies in human capital and entrepreneurship can be traced to deficiencies in education, a poorly trained labor force, and the migration of skilled labor.

<table>
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<tr>
<th>Constraints to Growth</th>
<th>Policy Recommendations</th>
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<tbody>
<tr>
<td><strong>Short Term</strong></td>
<td><strong>Medium Term</strong></td>
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<tr>
<td>Increase competition in all markets. [G]</td>
<td>Continue promoting competition in all markets. [G]</td>
</tr>
<tr>
<td>Design strategies for the development of pre-employment skills to prepare future workers. Invest more in early-childhood education, particularly in programs that improve quality. Increase investment in technical and vocational education and training (TVET). Modernize curricula and equipment, and offer better training for trainers, particularly in emerging sectors (ICT, telecommunications). Emphasize measuring learning outcomes and applying the data obtained. Use incentives provided by financing, institutional autonomy, and accountability mechanisms to steer the system toward producing better education outcomes. [G &amp; P]</td>
<td>Improve the formal education system focusing on critical thinking and innovation. [G]</td>
</tr>
<tr>
<td>Invest in on-the-job training to upgrade workers’ skills. Involve enterprises and employers’ organizations in the definition of qualifications, occupational standards, training delivery, and certification. Encourage a shift from input-based to outcome-based training through a competency-based approach. [G &amp; P]</td>
<td>Improve school-system quality and increase investment in tertiary and TVET. [G]</td>
</tr>
<tr>
<td>Use active labor market training programs to reintegrate the unemployed and disadvantaged back into the workforce. Develop and implement a strategy for increasing opportunities for adults to upgrade or acquire new skills. Design and implement entrepreneurship programs that provide training in basic business skills, especially for the young. [G &amp; P]</td>
<td>Consider policies to turn brain drain into a process of brain circulation by creating opportunities and channels for highly skilled Jamaicans living abroad to engage in productive investment in the country. [G &amp; P]</td>
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<tr>
<td>Constraints to Growth</td>
<td>Policy Recommendations</td>
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<td><strong>Issue 3: Distortionary tax policy, complex tax system, and challenging business environment</strong></td>
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<tr>
<td>Distortionary tax incentives and the promotion of enclave development produce few spillovers to the rest of the economy.</td>
<td>Freeze the issuance of new tax incentives and reduce discretionary tax incentives (ongoing). [G]</td>
</tr>
<tr>
<td>A complex tax system and problems related to paying taxes reduce tax compliance and discourage business development.</td>
<td>Review and initiate consultations on tax exemptions (with a view to reducing and phasing out a majority of them). [G]</td>
</tr>
<tr>
<td>Economic activity is highly concentrated. Jamaican exporters have lost competitiveness and have not taken advantage of emerging opportunities in the global marketplace.</td>
<td>Initiate a dialogue on how the tax base can be effectively broadened, drawing on existing reviews of the tax system (Matalon report and others). [G &amp; P]</td>
</tr>
<tr>
<td>Crime and violence, complicated tax rules, an inefficient bureaucracy, and poor logistics have stressed the business environment and constrained firms’ growth.</td>
<td>Continue unifying tax policy and simplifying the process of paying taxes. [G]</td>
</tr>
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</table>

**Short Term**

**Medium Term**

Slash tax incentives and make the system transparent. [G & P]

Consider a new tax code to make the tax system business-friendly and conducive to economic growth through simplification of policies and procedures for payment. [G & P]

Improve information dissemination and eliminate coordination failures. Provide relevant, targeted and up-to-date information on market trends and requirements, particularly to SMEs. Follow emerging opportunities in world markets and encourage local producers to respond to such opportunities. Facilitate technical assistance, especially for SMEs, to enhance their capacity to formulate better market approaches, including product development and distribution strategies. Encourage diversification of production and export markets. [G & P]

Continue improving the access of firms to existing funding mechanisms and facilitate greater access to global resources (such as the Earth Lung project, the Global Environment Facility, and green funds that aim to increase private participation in sustainable tourism). [G & P]

Reduce the cost of energy (electricity). [G & P]

To be implemented by government (G) or by private sector (P)
### Policy Recommendations

<table>
<thead>
<tr>
<th>Constraints to Growth</th>
<th>Short Term</th>
<th>Medium Term</th>
</tr>
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<tbody>
<tr>
<td><strong>Issue 4: Weak public financial management and public service provision</strong></td>
<td>Develop a clearer set of guidelines for budget preparation and in-year implementation. Reform the practice of in-year budget reporting to Parliament and supplementary budgets. Institute a regular session of the House approximately six months after the start of the fiscal year to hear revenue and expenditure performance. Disclose complete and comprehensive information on budget results through annual budget reports. [G]</td>
<td>Consider developing new organic budget legislation. Improve the institutional framework for budgeting with a view to (i) enabling more strategic decision-making and (ii) ensuring greater budget credibility. Consider instituting a more specialized Standing Budget Committee in the House (with approximately 20 members) and ensure that members have access to professional analytic support. [G]</td>
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<td>Policy and institutional weaknesses in the area of public financial management create fiscal distortions and hamper growth.</td>
<td>Conclude development of a scoring system for public investment proposals (ongoing). Start developing a comprehensive pipeline of projects (including projects proposed by public bodies and projects to be funded by domestic and foreign sources) with an eye to economic and social development. [G]</td>
<td>Develop legislation and implementing regulations that will set out key principles for public investment management. Define the roles of the Planning Institute of Jamaica, the Ministry of Finance and Public Service, and sector ministries with respect to public investment management. Put in place the technical and political mechanisms (scoring, cabinet retreat) for deciding on budget allocations for projects in the pipeline. [G]</td>
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<td>Continue divestment of public bodies. Improve fiscal prudence and management of public bodies. Increase the realism of corporate plans and accuracy and the timeliness of reporting. Identify selected (2–3) public bodies that create fiscal risks (e.g., JUTC) and start a public debate on options. [G &amp; P]</td>
<td>Continue divestment of public bodies. Build mechanisms for independent verification of reporting by remaining public bodies. Generate a clear public commitment with regard to burden and risk sharing between beneficiaries (users, employees, managers) and general taxpayers for the selected public bodies. [G &amp; P]</td>
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<td>Consolidate the legal framework for debt management through the passage of a modern law that will provide a clear framework for the management of public debt and government guarantees. Fully implement the new functional organizational structure of the government’s debt-management unit, with a front, middle, and back office. Develop and maintain a comprehensive and methodologically sound medium-term debt-management strategy. [G]</td>
<td>Separate debt management from cash management. Facilitate creation of a formal calendar for the issuance of debt. Improve institutional capacity for preparing medium-term debt-management strategies with sound analytical underpinnings. Prepare and publish comprehensive annual debt reports. [G]</td>
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<td>Improve public service provision. Simplify customs procedures and increase quality of public service provision. [G]</td>
<td>Create an efficient and effective public sector that provides high-quality services transparently. Create an efficient customs system capable of competing with other countries in the region. [G]</td>
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