



GRENADA

A DIAGNOSTICS REVIEW OF THE INVESTMENT CLIMATE

June 2004

**Foreign Investment Advisory Service
a joint service of the
International Finance Corporation
and
The World Bank**

At the request of the Grenada Industrial Development Corporation (GIDC), the Foreign Investment Advisory Service (FIAS), a joint facility of the International Finance Corporation (IFC) and the World Bank, conducted a diagnostic review of the investment climate in Grenada in order to assist the Government of Grenada to identify the strengths and weaknesses of its business environment.

The field mission for this project took place in January 2004. The FIAS team worked closely with the staff of the GIDC, our working counterpart, who organized and participated in joint meetings with officials of other Ministries and representatives of the private sector. FIAS would like to thank the GIDC for the assistance it provided to the visiting team. The FIAS team would also like to thank the representatives of the Government of Grenada and the private sector who met with the team and provided useful information and materials.

The project is co-financed by FIAS and the Government of the Netherlands through its Consultant Trust Fund managed by the World Bank. FIAS is solely responsible for the views and recommendations expressed in this report.

ACRONYMS

CARICOM	Caribbean Community
CSME	Caribbean Single Market and Economy
ECIPS	Eastern Caribbean Investment Promotion Service
ECSE	Eastern Caribbean Securities Exchange
FDI	Foreign Direct Investment
FTAA	Free Trade Area of the Americas
GARFIN	Grenada Authority for the Regulation of Financial Institutions
CIT	Corporate Income Tax
GCT	General Consumption Tax
GIDC	Grenada Industrial Development Corporation
IPA	Investment Promotion Agency
NIS	National Insurance Scheme
OECS	Organization of East Caribbean States
SME	Small and Medium Enterprise
UNCTAD	United Nations Conference on Trade and Development
WTO	World Trade Organization

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EXECUTIVE SUMMARY

i. One of the main development aims of the Government of Grenada is the promotion of the private sector in order to generate growth, employment and income earning opportunities. The general macro-environment in Grenada has been conducive to investment in the recent past. Alongside its OECS partners, this small economy of 100,000 people has exhibited a high level of macro-economic, macro-social and macro-policy stability, which is the key element of a macro-environment in terms of its influence on investment. This macro stability has contributed to Grenada's good performance in FDI flows in the past.

ii. However, Grenada still lags behind most of its OECS neighbors in terms of broad socio-economic development and faces challenges in its efforts to attract further investment. Increasing indebtedness threatens its macro-stability, FDI inflows have stagnated in the last couple of years, and it continues to be constrained by the host issues related to the small size of its economy. How to make Grenada's relatively favorable investment climate even more conducive to investment is a critical question to answer if the country wants to meet its development aspirations.

Investment climate survey

iii. To better understand the dynamics of the private sector, an investment climate survey was conducted in Grenada during January – April, 2004, which covered a total of 201 firms. Although the sample aims to reflect the composition of the private sector in Grenada, a conscious decision was made to include proportionally more firms from the manufacturing and tourism sectors in order to get some sectoral perspectives. Special attention was also paid to including foreign owned firms.

iv. The survey revealed that new business activities have been in decline over the past several years. As a result, most firms have been in operation for more than 10 years. Among the host of factors investigated, the most serious constraints to doing business in Grenada include a lack of highly skilled well qualified labor force, high cost and lack of access to finance, high tax burden and problems with the supply of electricity.

Policies

v. In general, private investors who are interested in investing in Grenada face few policy hurdles as they seek to move from intention to implementation. In terms of FDI entry, Grenada enforces the best-practice principle of a negative list for foreign investment. However, Grenada's investment legislation sometimes lags behind investment practice, and it continues to discriminate against foreign investors through the Alien (Landholding Regulation) Act and Exchange Control Act, which set more stringent requirements for foreign residents when carrying out some transactions in Grenada.

vi. Grenada is a member of the CARICOM. However, it has not met some of its commitments to the CARICOM, nor those to the WTO. Despite the advanced stage of these initiatives, about one-third of the companies in Grenada are not aware of these processes and most expect no impact on their operation from either the CSME or FTAA. One of the consequences of Grenada's unfinished trade liberalization agenda is that, although most enterprises depend on imports for inputs, two thirds of the firms serve only the domestic market despite its small size.

vii. Tax rates are considered high and a key constraint to business growth. Further, Grenada administers a complex and opaque investment incentives regime. Many of the incentives legislations are outdated and do not reflect Grenada's economic reality today. The Hotel Aid Act, for example, deals with hotels only, not the broader categories of tourism. The incentives' administration has also generated widespread complaints among businesses for its unfairness and arbitrariness. The Government has recognized these problems and established a Fiscal Incentive Review Committee to look into the various issues.

Regulations

viii. In Grenada, the majority of the private firms have a fairly positive view of government efficiency, and the consistency and predictability of the officials' interpretation of rules. Regulations with respect to the establishment of businesses, such as business registration and obtaining licenses and permits, are not considered a big problem by the large majority of the enterprises. Procedures for access to land and buildings can take a long time and are rated a more problematic. But overall, they are still considered quite manageable.

ix. By far, the most serious administrative constraint is the customs regulations. Although the customs delay is not significantly out of line by regional standard, businesses expect faster port clearance in Grenada because of smaller total transaction volumes. Import clearance is much more problematic than clearances for export and has resulted in incidents of bribery of customs officials, although the such incidents continue to be generally rare in Grenada.

x. Business inspections are considered to be one of the least problematic aspects in operating a business. They seem to be carried out infrequently. Most companies are not affected by foreign exchange regulations, competition law regulations, and patent and trademark regulations either. The lack of standards, however, is found to have deterred some investors in the tourism sector from investing in Grenada.

xi. There appears to be a general confidence in the judicial system and that rights are enforced. However, about 15 percent of the firms have doubts, especially among the larger firms. The majority of reported disputes are with clients.

xii. Crime is reportedly becoming a problem in Grenada, especially petty theft. However, in spite of this threat, serious security measures are not yet taken by many

firms and security costs are not significant in relation to sales. A little over half of the companies report all or most of the crime incidences they experience to the police and most of these incidents appear to have been resolved.

Infrastructure

xiii. One of the key elements influencing Grenada's prospect for attracting investment is the high cost of utilities. Electricity costs, in particular, are much higher than comparable costs in large mainland territories, such as the United States, and in energy-producing countries such as Trinidad & Tobago. Electricity outages are frequent and affecting more than half of the firms. Access to water and telecommunications is less of a problem, but water stoppages do occur and appear to be more costly than power outages because they tend to last longer.

xiv. The extent to which transportation is a constraint to business depends on the destination of transport. On the whole, international transportation to destinations outside the CARICOM is more of a problem than within the region, which in turn is more problematic than local transportation. Port delays and infrequent/unreliable ship services to other islands and beyond are the key problems related to international transportation. As a result, inventory is substantial in Grenada. Two thirds of the firms keep stocks for more than one month and 10 percent of them have inventory periods that last as long as half a year.

Finance

xv. Getting reasonably priced finance is considered a key constraint to business operation and growth in Grenada. More firms rated the cost of financing as a severe obstacle to their businesses than any other factors considered. There is a general perception that that the local banking sector is underdeveloped and that commercial banks, in particular, do not provide the venture and project support required of many companies. Own funds and retained earnings are by far the most important sources of financing, followed by commercial bank credit, while trade credit and equity financing have very limited roles in Grenada. There is also extremely limited reliance on overseas financing options.

xvi. Despite the overall dissatisfaction about the cost and access to finance, most firms are reasonably happy about working with the local banks. A majority of the companies in Grenada have overdraft facilities or line of credits at the local banks and important proportions of them are being utilized. Although the banks' lending policies are still quite conservative as indicated by the levels of collateral to loan ratios, there are signs that commercial banks are moving more to project and cash-flow as opposed to asset-based lending in recent years.

Labor

xvii. Despite the public-sector-led nature of Grenada's growth in recent years, employment in the private sector expanded by 8.6 percent between 2001-03. Employment increases have been especially noticeable in information and communication, financial services and the tourism related activities. Employment growth is also more significant in small and medium sized companies than micro and large companies, and in domestic establishments than foreign firms. Temporary employment is also on the rise, especially temporary female employment.

xviii. Wages and compensation, as expected, rise with skills, and are generally higher in the manufacturing firms and foreign companies. There is also a considerable difference between wages and compensation, reflecting supplementary benefits for the workers paid for by the companies. Such discrepancies may be another indication of the skills shortage in Grenada as they are the largest for people with managerial skills. It is also a sign of protective labor regulation, which is considered to be a serious constraint second only to customs regulation.

xix. Reflecting Grenada's educational system, the workforce is reasonably well educated with 61 percent of the workers having secondary or higher education. Nevertheless, issues related to inadequate skills and education levels of the workforce are ranked as the No. 1 constraint to business growth. The key skills missing are technical skills, and to a lesser degree, managerial capacities. Half of the companies indicate that they offer formal training to employees. Public training institutions are clearly not meeting the demands of the enterprises as the large majority of the training is provided internally by the companies, or by private training facilities. Firms feel strongly that there is a need for more training centers.

Capacity and innovation

xx. In Grenada, capacity utilization rates vary significantly between firms. While some firms are running at full capacity, others have left idle as much as 90 percent of their productive capacity. Overall, however, the capacity of Grenada's private sector is well utilized at 77 percent. Although more firms reported increases in their capacity utilization rates between 2001 and 2003 than those which reported a decline, about half of the companies saw no change during this time. Such stagnation in productivity and resource use is the more noticeable among domestic firms than their foreign counterparts.

xxi. Most companies reported little innovative activity in terms of introducing new products. The most predominant innovative initiative is the upgrading of an existing product line, which was reported by almost half of the companies. The most important way of acquiring new technology is through new machinery and equipment, while actual expenditure on R&D is limited. Customers are generally the most significant influence to reduce production costs and to develop new products and services. Competition is also important. For domestic and micro firms, local competition is the most important force behind taking cost reduction measures and improving product and service qualities.

Manufacturing firms, on the other hand, are heavily influenced by international competition.

Institutional Arrangements for Investment Promotion

xxii. In Grenada, even though the Grenada Industrial Development Corporation (GIDC) represents the institutional arrangements for promoting investment, the most senior levels of government also play a role in investment management and promotion. Two institutional changes took place recently which created an Inter-ministerial Investment Management Committee and a Ministry of Private Sector Development, to which the GIDC would report. It is too early to evaluate their effectiveness. One thing to bear in mind, however, is that in considering the structure and function of the GIDC, the level of autonomy, financing and staffing of the organization is more important to its success than its reporting link.

xxiii. There are legal changes that are necessary to allow for a more streamlined investment promotion process. Currently, the GIDC is neutered, at certain levels, by the limitations of its legal approval authority. That approvals from the highest levels of the government are required for all sorts of issues – from investment incentives to personnel decisions – significantly hampers the organization’s effectiveness in investment promotion. The Government needs to revisit the legislation to grant greater approval authority to the board of the GIDC.

xxiv. Under such constraints, the GIDC has focused its efforts on investment services and investment policy advocacy. This focus is further augmented with the recent movement towards a “one-stop-shop” for investment. However, examples of successful one-stop-shops have been few. The efforts to transform the GIDC in this direction should concentrate on making the organization a highly professional, well staffed, and adequately-funded promotional organization with reasonable powers of approval and with links to the senior levels of the governmental apparatus.

xxv. The biggest gaps in relation to GIDC’s operations are in the areas of image building and investment generation, which require financial resources that have traditionally not been available to the organization. The problem is further compounded by the absence of an institutional presence in overseas markets. In this regard, St. Lucia’s approach in the 1980s is worth considering.

Policy recommendations

- On the macro level, Grenada needs to address the emerging macro-economic tensions to ensure sustained macro-economic stability. One approach to this challenge is the shift from a public to private-sector driven growth strategy that is at the heart of this report. Another is enhanced social partnership discussions with a view to ensuring continued macro-economic stability. In this regard, heightened dialogue with the trade union movement is likely to be necessary.

- With respect to foreign investment entry, the Investment Code should be revised and updated in order to provide a comprehensive position of the Grenada's attitude toward foreign direct investment and the provisions of its investment regime. The merits of the Alien (Landholding Regulation) Act and Exchange Control Act should be examined carefully, with due attention accorded to the experiences of other countries in the CARICOM. At a bare minimum, Grenada should put in place the procedures to ensure that existing alien landholding regulations do not apply to CARICOM nationals
- In the area of trade policy, the Government should adhere to its multilateral commitments and complete the liberalization agenda. The government should also improve information to the business community on the CSME and FTAA negotiations and stimulate the undertaking of assessments of the impact of trade liberalization for the different sectors of the economy.
- To address the issues of high tax burden and uneven application of tax incentives, the on-going Fiscal Incentive Review needs to be completed the soonest. In the review process, the Review Committee should make the distinction identified in this report on incentives and examine international experiences in this area. In addition, procedures related to payment and assessment of GCT should be simplified.
- In order to improve the efficiency of customs administration, special attention needs to be paid to improving the professional skills of customs officials and upgrading the technological bases of the customs offices in order to speed up customs clearance procedures. Special efforts should be made to increase the use of electronic processes and automation at customs. The Government should also promote closer co-operation between Grenada and the customs and immigration authorities in neighboring countries, particularly for the yachting and marina industry.
- While both high utility and transport costs are related to Grenada's size and geography, the Government should continue its efforts to improve the reliability of electricity services and the quality of the road network and to promote regional co-operation in the transport sector. The positive results from the liberalization of the telecommunication sector provide an example in this regard.
- With respect to finance, the Government should aim at facilitating competition to encourage entry of all types of financial institutions. The operations of the Grenada Authority for the Regulation of Financial Institutions (GARFIN) may need to be examined to ensure that they are compatible with a fast changing industry. In addition, establishing clear regulations to facilitate sharing of credit information through private credit bureaus is another critical first step towards improving the access to credit for many firms.

- To fill in the skills gap, the Government should step up its efforts to stimulate the expansion of private training facilities and encourage co-operation with training facilities elsewhere in the region. Some initiatives have been undertaken in the hospitality sector, but a more coherent strategy needs to be elaborated. Further, there are immigration measures that Grenada could take, in association with its sister countries in the CARICOM, to encourage greater mobility of skilled labor.
- With respect to the GIDC, the Government should revisit the Industrial Development Corporation Act to afford the board of GIDC greater authority in decision making. In addition, careful examination is warranted of the current incentives approval mechanism, which should be addressed by the Fiscal Incentive Review Committee, the nature of the One Stop Shop that the GIDC aspires to become, and the models of overseas representation for investment activity.

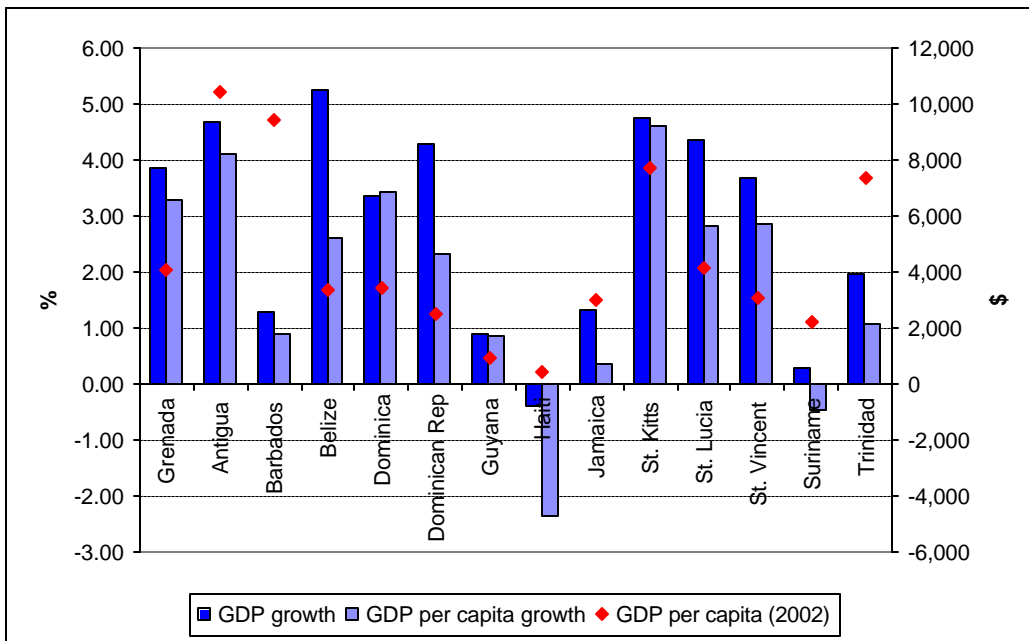
CHAPTER I

GRENADA IN HISTORICAL AND REGIONAL PERSPECTIVES

A. Overview of the Economy

1. The economies of the Caribbean region present a mixed picture of economic growth over the last two decades. Several of the larger economies, notably Haiti, Jamaica and Suriname, have experienced very anaemic levels of growth, while some others, particularly Antigua and St. Kitts, have experienced much higher and steadier levels of per-capita income growth (Figure 1.1). Grenada falls between these two extremes of growth and development performance. It has registered much stronger growth than the larger Caribbean economies, while at the same time, its 2002 per-capita income of US\$4,060 is below the average of the Organization of East Caribbean States (OECS).

Figure 1.1: Growth Performance of Grenada and Comparators, 1980-2002

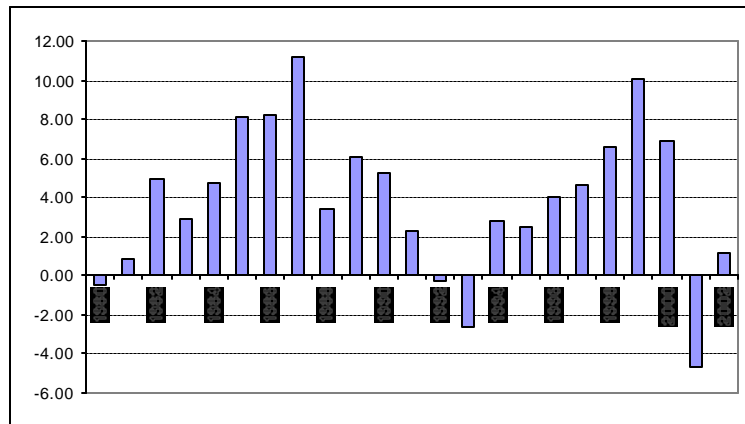


Source: World Bank.

2. Being a small island economy, Grenada's economy is more heavily influenced by worldwide economic cycles than the larger countries, including those in the Caribbean region. As Figure 1.2 demonstrates, Grenada's growth path in the last two decades punctuates the two economic cycles around the world. Since the late 1980s, growth in Grenada has been led by tourism as agriculture, in particular the production and export of bananas, cocoa and nutmeg, the traditional mainstay of the economy, continues to decline. Grenada also has a modest manufacturing sector, which contributes about 7 percent to GDP and caters largely to the domestic market. This involves beverages,

flour, garments, paper products, paints, many of which are protected against foreign competition by quantitative import restrictions.

Figure 1.2: Grenada GDP Growth,1980-2002 (%)



3. The Grenadian economy is highly import dependent, with imports accounting for 49 percent of GDP. The USA is the main source of imports (44 percent), followed by countries of the Caribbean Community (CARICOM) (20 percent), in particular Trinidad and Tobago. Exports of goods account for 14 percent of GDP. Although the deficit on the trade balance is partly compensated by growing tourism revenues, the current account balance has been negative over the years. However, the deficit on the current account has been more than compensated by a surplus on the capital account, especially fuelled by foreign direct investment (FDI) in the tourism sector.

4. One of the advantages that Grenada has experienced with its integration into the OECS has been macro-economic stability. The economic union within, yet also separate from, the institutional apparatus of the broader regional grouping of the CARICOM, has created a stable environment, which has been quite conducive to investment and economic growth. Grenada's inflation rate of just over 1 percent in 2002, for example, typified the price stability that has characterized this group of countries, and is in sharp contrast to the chronic macro-economic instability experienced by several of the larger economies within CARICOM.

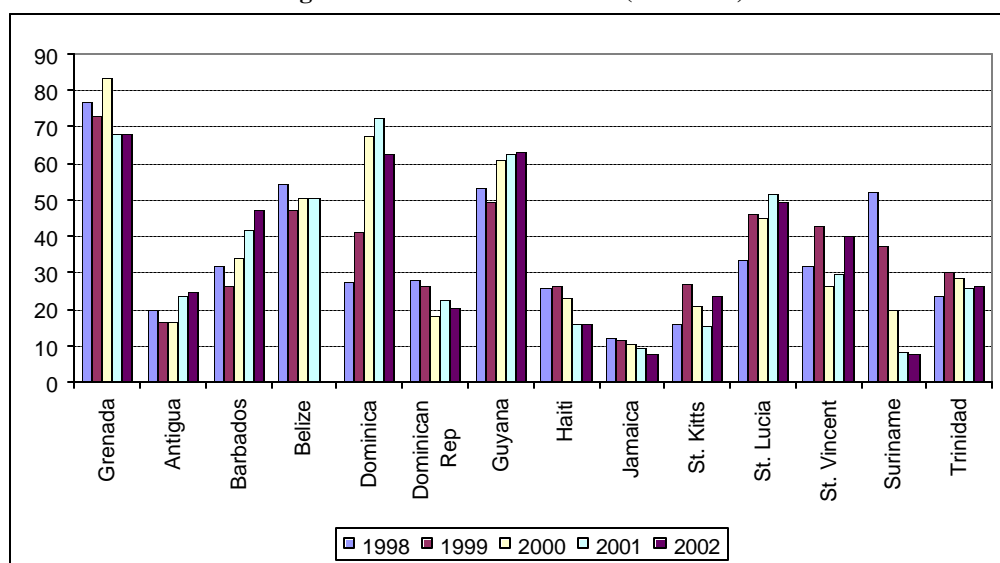
5. However, macro-economic stability alone has been insufficient to allow Grenada to match the economic performance levels of high performing economies within and outside the Caribbean region, as indicated both by per-capita income data and the Human Development Index, which, in 2003, positioned Grenada below all CARICOM economies with the exception of Haiti. Furthermore, even in relation to macro-economic stability, there are concerns on the horizon. In 2003, for example, the Caribbean Development Bank reported that government borrowing in 2002 is estimated to have pushed the country's external debt stock to about 60 percent of GDP, and that the Government's debt position is significantly higher when domestic liabilities (78 percent of GDP) and contingent liabilities (over 100 percent of GDP) are included.¹

¹ Caribbean Development Bank, Annual Report, 2003.

6. Figures from the Grenadian Government suggest a somewhat different, but equally troubling, picture. In 2002, based on these figures, the debt to GDP ratio stood at 103 percent of GDP in 2002,² climbing dramatically from the 2001 debt to GDP ratio of 67 percent. The 2002 ratios are very high both in relation to Grenada's economic history and in comparison to the debt to GDP ratios in other countries.

7. In part, the increasing debt liabilities reflect the very significant infrastructure expansion that the Government has financed. The public sector investment program has contributed significantly to the relatively strong growth performance in Grenada between 1996 and 2000, but the increased debt that has resulted through this process, and the dramatic debt expansion of 2002, suggest that Grenada may well have passed the limit of public-sector led economic growth. Figure 1.3 shows that Grenada has by far the largest proportion of public investment among all countries in the region.

Figure 1.3: Public Investment (% GFCF)



8. Therefore, the macro-economic picture suggests that while Grenada has done quite well, significant levels of economic growth are still required in order for the country to meet its development aspirations, and future growth will have to be driven by the private sector.

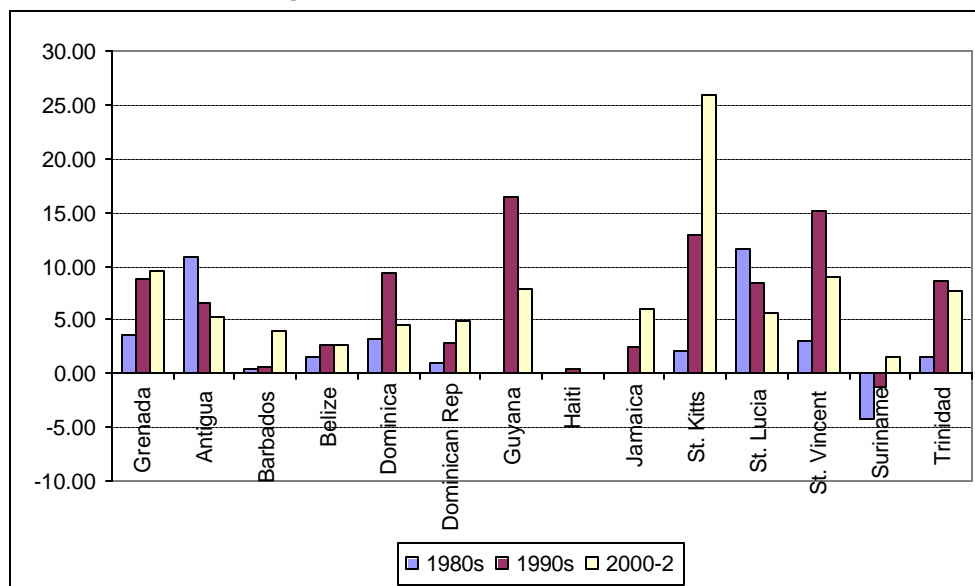
B. Grenada's FDI Performance

9. Grenada presents a far more positive picture in relation to its FDI performance. FDI inflows as a percentage of GDP more than doubled between 1980-2000, and registered an 11 percent annualized growth rate between 1997 and 1999. Since then, however, there has been virtually no growth in FDI inflows into Grenada (Figure 1.4).

² The domestic debt was 24 percent of GDP and external debt, 79 percent of GDP.

Compared to its Caribbean neighbors, Grenada has lagged behind some of its OECS neighbors, notably Antigua and St. Lucia in the earlier days and St. Kitts more recently, but has clearly done better than most other CARICOM countries.

Figure 1.4: FDI to GDP Ratio, 1980-2002



10. A country’s FDI performance needs to be taken against the context of overall changes in global FDI flows.³ For the last several years, the UNCTAD has produced an “FDI Performance Index” that ranks countries by comparing their relative levels of FDI inflows in relation to their relative levels of economic power.⁴ Thus, an FDI performance index of one would suggest that the country is attracting exactly the proportion of global FDI that is represented by its proportion of global economic activity. In relation to this index, several economies in the CARICOM region, notably Jamaica and Trinidad and Tobago, whose FDI Performance Index was 1.7 and 2.8, respectively, for the period of 1998-2000, have been noted by the UNCTAD as “high performing” with regard to their levels of FDI inflow.

11. Grenada is not captured explicitly in the UNCTAD FDI performance rankings. But using the same methodology, it can be calculated that Grenada’s average FDI Performance Index between 1998-2000 was 3.6. This ratio declined to 3.2 over the period 1999-2001. Yet, even with this decline, Grenada continued to attract far more FDI than is predicted based upon its proportion of global economic activity. It has also been doing better than both Jamaica and Trinidad and Tobago, the two recognized “high performing” CARICOM countries.

12. However, Grenada is not at the top of the Eastern Caribbean league with respect to FDI performance. St. Kitts and Nevis, for example, had an average FDI Performance

³ As a result of the global economic downturn, the worldwide FDI flows halved between 2000-02.

⁴ The numerator of the FDI Performance Index is the ratio of a country’s FDI inflows as a proportion of world inflows, while the denominator is the ratio of a country’s GDP as a proportion of global GDP.

Index of 5.7 during the period of 1998-2000, which increased to 7.2 between 1999-2001 notwithstanding the worldwide FDI decline. Clearly, these comparative data have to be treated with caution since FDI inflows are notoriously cyclical and volatile, particularly in small economies. At the same time, the fact that strong FDI performance has not by itself contributed to high levels of growth suggests that Grenada needs to consider carefully policy changes that will also increase levels of private indigenous investment.

13. Against the background of these comparisons, Grenada has an opportunity to increase its level of FDI inflows as part of a broader strategy of encouraging private-sector driven growth in its economy. In order to position itself for increased inflows of FDI, and, as importantly, in an effort to encourage additional private investment from domestic sources, Grenada needs to assess carefully its investment climate, its investment potential and its institutional structure for managing investment and implement appropriate changes.

C. The Challenges of Investment Attraction in Grenada

14. Grenada faces challenges in its efforts to attract investment. Some of these challenges are largely outside of the control of the policy makers, even though, despite the uncontrollable nature of these challenges, they can still be converted into opportunities.

15. Obviously the most significant uncontrollable challenge relates to its small market size. With a population in the vicinity of 100,000, Grenada is unlikely to attract any foreign investment that is oriented to its domestic market. This eliminates, for Grenada, that significant portion of global FDI flows that is “market-seeking” in its orientation.

16. This is true even though Grenada is integrated within the CARICOM. Through this integration effort, especially the associated Caribbean Single Market and Economy Project (CSME), which is geared toward greater market integration for the region, Grenada effectively increases its domestic market to a population of approximately 12 million. But even a market of this size is unlikely to create significant potential for market-seeking FDI, particularly given the geographical disparateness of the island economies that are the principal constituents of CARICOM.

17. In addition, the higher input costs associated with the small scale of operations in Grenada suggest that only a select type of high-value niche products are likely to be competitively produced in Grenada. Even with this focus on niche products, it is critical that linkages, between export-oriented and local firms, and between foreign and domestically-owned firms be explored and nurtured.

18. Yet, the good news for Grenada is that with increasing trade liberalization and the consequential closer integration of global markets, FDI flows are more than ever likely to be “efficiency-seeking,” in which the market size of the production location bears little

relevance to its attractiveness to prospective investors. Clearly, such investment projects seek to serve global rather than national markets.

19. Grenada has already been successful in attracting some “efficiency-seeking” investments geared to serving global markets. It is critical that the country’s investment climate become even more conducive to the attraction of these types of investments, for which there is intensive global competition among countries and are, therefore, particularly sensitive to the level of receptiveness of the host country’s investment environment.

20. This need to develop a more receptive host country investment environment applies even with the regional integration efforts in which Grenada seeks to participate. Within CARICOM, there are strong similarities in the areas of competitive advantage of the various national economies. Consequently, competitiveness is likely to be more closely linked to the quality of economic and policy management, rather than the existence of natural production advantages. This is already in evidence in the differing levels of economic performance across the region. Similarly, if the countries of the Americas are successful in consummating a hemispheric free trade area, the size of this regional behemoth will significantly blur the distinction between market-seeking and efficiency-seeking investment. In this event, investment flows will be highly influenced by the nature of the policy environment and other aspects of the investment climate.

D. Investment Climate and Survey

21. Defining investment climate precisely is difficult. But one useful definition is the “policy, institutional, and behavioral environment, both present and expected, that influences the returns, and risks, associated with investment.”⁵ This environment is generally seen as having the following three main components:

- Political and macroeconomic stability is an absolute pre-requisite for any kind of private investment, including FDI. Numerous studies have amply demonstrated that a country’s macroeconomic conditions, including its fiscal, monetary and exchange rate policies, are among the most important determinants for FDI.
- A sound regulatory framework and efficient supporting institutions to enforce the relevant laws and regulations are imperative for investors to enter and thrive. This relates to government interactions with business. Especially in a globally-integrated competitive market, the difference between countries in the costs of starting and operating a business has a huge impact on where an investor will go and how much contribution the investment will make to the host economy.
- An adequate physical and social infrastructure complements a good policy and regulatory framework to create the necessary environment for attracting

⁵ Stern, Nicholas, 2002, *A Strategy for Development*, Washington, DC: World Bank.

investment. These include the quantity and quality of power, transport and communication systems, access to finance, qualified labor force, and the provision of social services.⁶ They are also important if the full potential benefits of any private sector investment, especially FDI, are to be realized.

22. To assess the investment climate in Grenada, a survey of 201 firms was conducted in the tri-island state between January - April 2004 in order to gather the firm-level data imperative for the assessment. The survey instrument shares much of its structure and focus with other investment climate assessments carried out under the World Bank Group investment climate initiative, but is at the same time shaped by the distinctive priorities of the country.

23. The sample was selected from a list of firms which are making contributions to the national insurance scheme (NIS) for their workers.⁷ The sampled firms were chosen to ensure that they broadly reflect the Grenadian economic structure and focus on the areas where the Government actively encourages more investment. In addition, special attention was paid to large companies (those with 25 or more employees), firms in manufacturing and tourism and tourism-related sectors, as well as foreign owned establishments in order to gain a deeper understanding of their dynamics.

24. Although most of the sampled firms are located in St George's town (98 firms) and St George's parish (68 firms), other parishes are represented as well, including 12 firms in St David's, 11 firms in St Andrew's, 3 firms in St John's parishes, and 5 firms in Carriacou. Some of the key features of the sample are highlighted here, while a more detailed breakdown of the participating firms by size and sector can be found in the Appendix.

25. *Sector distribution.* The sample includes 44 manufacturing firms and 56 tourism-related firms. The tourism sectors are broken down into hotels, including firms with hotel services as the main activity, and other tourism services, which includes restaurants, yachting activities, tour guides, diving shops, travel bureaus, and shops catering to tourists (e.g., duty free shops). The classification of enterprises by sector is based on the recording of primary activity. It should be noted that 5 of the retail firms have manufacturing as secondary activity.

⁶ For the purpose of this report, a deliberate choice has been made not to include assessment of basic social infrastructure such as education and healthcare provisions. Clearly, these are important aspects of a country's overall investment climate. But as their assessment requires a very different approach and methodology, this report restricts itself to physical, financial and human resources in its discussion of infrastructure.

⁷ In constructing the sample frame, a number of sources were considered. The Company Registrar's Office provided a list, but not all companies on the list are actually operating and that there is no information on employment. The Grenada Industrial Development Council (GIDC) also maintains several company lists, but they cover only selected sectors and in particular companies accessing incentives. They also lack employment information. The NIS provided the most consistent list of companies with information on employment, sector and location, facilitating the breakdown of the sample frame to focus on specific target groups of companies.

26. *Foreign companies.* The sampled firms include 45 companies with foreign ownership. Foreign-owned companies are more dominant in the financial, information and communication, and the tourism-related sectors, but play a limited role in manufacturing. There are also several foreign-owned construction companies in Grenada. Among the foreign-owned firms, 60 percent are fully foreign owned and only 4 out of 45 have a foreign ownership of less than 50 percent. The largest source of foreign ownership is other CARICOM countries (19 firms), followed by the USA (12 firms) and the UK (7 firms).

27. *Age of establishments.* Most of the firms (63 percent) have been in operation for more than 10 years, and just under half of these were established over 20 years ago. Especially in more recent years, there has been a downward trend towards new business start-ups. In 2000, for example, there were 14 new firms established in Grenada. Over the following three years, however, number of new establishments declined gradually to 9, 6, and 4, when in 2003 two out of the four new firms were wholly foreign owned companies investing in the tourism industries. This statistics is consistent with the macroeconomic data of low private investment in Grenada in recent years.

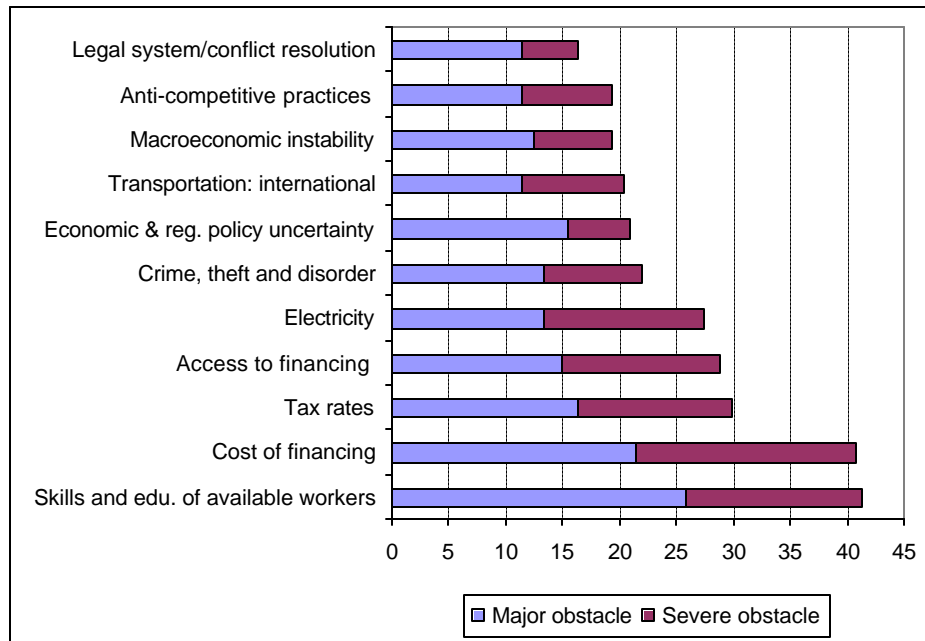
28. *Women in business.* Overall, very few firms (21 percent) are owned by women.⁸ Female directors and managers are more common (45 percent), especially in food processing, retail trade, hotels and restaurants, and other tourism-related businesses. However, the overall figures disguise a large discrepancy between domestic and foreign owned firms - women figure far more prominently in domestic firms than in foreign owned firms. Whereas only 18 percent of the owners of the foreign companies are women, 30 percent of the indigenous establishments have female owners. When it comes to female directors and managers, the ratios rise to 29 and 51 percent for foreign owned and domestic companies, respectively.

29. To get an initial sense of how firms view the overall investment climate in Grenada, the survey asked the firms to rate the extent to which a large number of factors constrain the operation and growth of their businesses. The general picture is quite favorable. For 8 of 19 factors considered, more than half of the firms reported that there was “no problem” with them.⁹ Figure 1.5 reports those factors that were considered as major or severe constraints to private business. The lack of qualified labor is found to be the biggest obstacle to doing business in Grenada. This constraint was felt particularly strongly by the foreign companies. Meanwhile, difficulties in getting finance, both in terms of cost and access, are also seriously constraining firm growth, especially the small domestic firms in manufacturing. In addition, nearly 30 percent of the companies find the tax rates too high and many have problems with electricity.

⁸ Including having women as the largest shareholders

⁹ These factors include health of workers (AIDS/HIV), local transportation, access to land, telecommunications, labor relations, transportation with CARICOM region, water and corruption.

Figure 1.5: Factors Rated as Major or Severe Obstacles (% firms)



30. In the next chapter, Grenada's investment policy and regulatory work will be examined in detail. Grenada's infrastructure, including both its physical and financial resources, is analyzed in Chapter III. Chapter IV discusses Grenada's human capital and enterprise's innovative practices. The report concludes with a chapter devoted to the institutional requirement for strategic investment promotion.

CHAPTER II

INVESTMENT POLICY AND REGULATORY FRAMEWORK

A. Investment Policies

31. In general, the macroeconomic environment in Grenada is perceived to be fairly stable. Low inflation and a pegged currency, which has been maintained at the same level for the past 25 years, create a relatively favorable environment for business development. However, concerns over macroeconomic instability, including a significant deficit on the current account and deteriorating overall fiscal balance, are rising and have cast a shadow over this otherwise positive picture. As the survey revealed, 7 percent of the firms reported that macroeconomic instability was a severe constraint to their operation and growth, and another 12 percent said it was a major problem (Figure 1.5). Investors in Grenada are of the view that domestic interest rates are at levels that are too high to encourage investment, when taken in the context of the fixity of export prices associated with the fixed exchange rate. Similarly, uncertainties over the economic and regulatory policy regimes were perceived by 21 percent of the firms as a serious obstacle to business development (Figure 1.5). Absence of clear policy guidelines and outdated legal framework result in inconsistencies of policy implementation, which increase the risks and costs of doing business and deter investment.

Entry of Foreign Investment

32. In general, private investors who are interested in investing in Grenada face few policy hurdles as they seek to move from intention to implementation. There are a few infrastructure sectors such as electricity, telecommunications and water that require government licenses. In addition, licenses are required to operate financial institutions. Regulation in these areas is obviously critical and there is no legislation that prohibits private investors, including foreign investors, from applying for the requisite license.

33. In relation to prohibition on the entry of foreign investment, Grenada does adopt the best-practice principle of a negative list for foreign investment: that is, the government specifies which sectors are not eligible for foreign investment, leaving open all other sectors for the participation of foreign investors. At the same time, Grenada's investment legislation in this area lags behind investment practice. The Investment Code that is still operational in Grenada dates to 1983. A revised investment code document drafted in 1991, however, continues to include in the negative list areas such as the retail and distribution trade, in which there is foreign investment in Grenada.

34. While the use of a negative list is appropriate, Grenadian policy makers need to update the list periodically to ensure that the country benefits from all types of foreign investment that can generate social benefits. Indeed, one of the possible areas for policy reform in Grenada is the generation of a revised and updated investment code that

provides a comprehensive position of the Country's attitude toward foreign direct investment and the provisions of its investment regime.

35. Although there is little discrimination against foreign investors in terms of the sectors of the economy in which investment is permitted, Grenada continues to discriminate against foreign investors in other ways that need to be investigated carefully on their merit. As is true elsewhere in the Caribbean, Grenada has long featured in its investment laws an Alien (Landholding Regulation) Act. This act contains the following three features of differential treatment for foreign versus local investors:

- Foreign residents need governmental permission to acquire land;
- Foreign residents require a license in order to hold or transfer shares or debentures or to be a director of a domestic company; and
- If the license to transfer shares is granted, transfers between local residents and foreign residents attract a transfer tax of 15 percent for the foreign resident and 5 percent for the local resident unless an exemption has been granted by the Minister of Finance.

36. Understandably, land is a particularly sensitive issue in small economies such as those of the Caribbean. Nevertheless, it is not clear that alien landholding regulations are the most effective mechanism for dealing with the problems of land price speculation and reduction in the access of land to low or middle-income residents, which are often identified as the reasons for continued use of alien landholding laws.

37. Further, the restrictions on foreigners trading in shares and the differential transfer taxes applied to share transfer arrangements included in these regulations actually have nothing to do with land. Grenada should examine the experiences of countries in the Caribbean, such as Trinidad & Tobago, which have repealed their alien landholding registration laws. At a bare minimum, Grenada should put in place the procedures to ensure that existing alien landholding regulations do not apply to CARICOM nationals.

Trade Policies

38. Grenada is a member of the CARICOM, which has embarked on a process of trade liberalization and the establishment of a Caribbean Single Market and Economy (CSME). A common external tariff has been established with a maximum import duty for both manufacturing and agricultural products.¹⁰ However, being classified as one of the "less developed countries" within CARICOM, together with other OECS countries and Belize, Grenada is allowed to continue imposing quantitative import restrictions on a range of sensitive products that compete with domestic producers. According to CARICOM agreements, Grenada is committed to change these quantitative import restrictions into import duties. This has not yet happened in Grenada. The experience of

¹⁰ The maximum import duty is 20 percent for manufacturing and 40 percent for agricultural products, respectively.

the other islands is that often these restrictions are turned into duties at prohibitive rates. In addition to import duties, a general consumption tax of 25 percent is charged on imports (CIF plus CET) except on qualifying CARICOM imports. Imports are also subject to a 5 percent customs services charge on the CIF value.

39. Grenada is also participating in the FTAA process. As a member of WTO, Grenada has also committed to liberalize its trade policies. However, some of its main commitments under the WTO have yet to be translated into domestic legislation, particularly in the area of valuation of imports, which is still based on customs valuation, as opposed to transaction value. In order to compensate for the loss of government revenue as a result of increased trade liberalization, the government intends to introduce a value added tax as of January 2006. In 2003, customs revenues still account for 53 percent of government revenues.

40. Most companies interviewed are aware of the CSME and the FTAA processes (77 and 71 percent of the firms, respectively) (Table 2.1). The largest group of respondents (32 percent for the CSME and 41 percent for the FTAA) expects no impact of these regional liberalization efforts on their sales. Companies in the tourism sector appear to be more positive about the potential impact of both processes, while those in manufacturing generally view them as a threat to their businesses. This latter group believes that they would be disadvantaged vis-à-vis some larger economies in the region, such as the Trinidad and Tobago, where energy is cheaper and companies can take advantage of larger economies of scale, which results in lower production cost. Some of the firms interviewed commented that the Government was not doing enough to inform the businesses and society about the CSME and FTAA; others felt that the government should provide more incentives in the form of tax holidays and other concessions, especially to small businesses, before the CSME comes into effect.

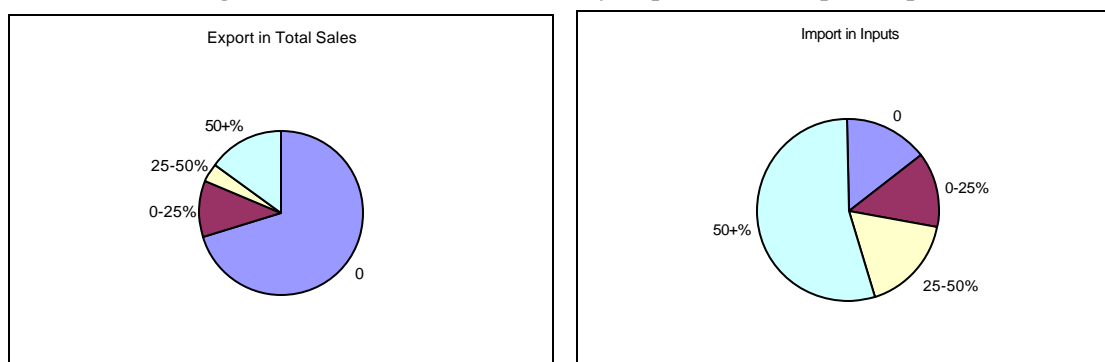
Table 2.1: Awareness and Impact of CSME and FTAA Process (% of firms)

	Awareness		Potential Effect on Sales			
	Not aware	Aware	No Effect	Decrease	Increase	N.A.
CSME						
Total	23.4	76.6	31.8	21.4	27.9	18.8
Manufacturing	15.9	84.1	27.0	37.8	18.9	16.2
Tourism	28.6	71.4	45.0	7.5	35.0	12.5
Domestic	21.8	78.2	32.0	20.5	29.5	18.0
Foreign	28.9	71.1	31.3	25.0	21.9	21.9
FTAA						
Total	29.4	70.6	40.8	20.4	18.3	20.4
Domestic	28.8	71.2	42.3	18.0	20.7	18.9
Foreign	31.1	68.9	35.5	29.0	9.7	25.8
Manufacturing	18.6	81.4	34.3	37.1	17.1	14.3
Tourism	36.4	63.6	22.9	2.9	34.3	42.9

41. One of the consequences of the unfinished trade liberalization agenda is that, despite the small domestic market, two thirds of the Grenadian firms serve only the domestic market (Figure 2.1). Of the 29 companies (15 percent) which reported

significant exports - more than 50 percent of their total sales – a third are foreign companies and 45 percent are in the tourism-related activities. Other CARICOM countries are the most important destinations for Grenadian exports, followed by the US and the UK.

Figure 2.1: Distribution of Firms by Importance of Import/Export



42. By contrast, there is a considerable dependence on imports for obtaining inputs. About half of the companies reported that they imported more than 50 percent of their inputs. It should be noted that a considerable number of firms use imported inputs which are purchased from local traders rather than imported directly. For the firms that do import directly, the US and CARICOM countries are the most important sources of imported inputs, while the UK ranks a distant third.

Investment incentives

43. Possibly the most controversial issue in developing countries as it relates to the entry of investors is the appropriate role of investment incentives. Grenada, like much of the developing world, has operated on the principle that investment incentives are critically important to investment decisions. Both domestic and foreign private investors in Grenada provide support for the position that incentives influence their investment decisions. At the same time, many studies have suggested that incentives are not particularly important to investment decisions.¹¹ Both domestic and foreign private investors in Grenada provide support for this position as well.

44. The above seemingly contradictory positions are easily reconcilable as soon as incentives are disaggregated. Like many developing countries, Grenada provides two types of incentives to investors, but these incentives are typically packaged together. One set of incentives grant exemptions from taxes on imported products, which serve to bring these products closer to world market costs. These incentives are essential to investment decisions, particularly for those companies that compete on regional or global markets. This is particularly true of the very high duty regimes that typify the trade environments of many developing countries.

¹¹ For example, Lim, D. 1983, "Fiscal Incentives and Direct Foreign Investment in Less Developed Countries," *Journal of Development Studies* 19(2):207-12 and Ernest & Young, 1994, *Investment in Emerging Markets: A Survey of the Strategic Investment of Global 1000 Companies*, New York.

45. But even a tax as low as the 5 percent “customs handling charge” applied in Grenada can have a significant impact on increasing the cost of inputs for investors serving global markets. This is why the “enclave” status that Grenada has negotiated with some firms (i.e., 100 percent export) involves the waiving of this tax, in addition to other duties. The government needs to ensure that if such waivers are agreed upon during entry negotiations, they are implemented with immediate effect and not, as in at least one case, one year after the start-up of investment operations.

46. The second set of incentives focus on providing income tax relief for approved firms. These incentives are much less important to investment decisions, particularly to those companies with long term investment perspectives. The level of corporate taxes is likely to influence investments oriented to global or regional markets, for which there is significant competition among destinations that are relatively equal in attractiveness in all other dimensions.

47. Grenada’s incentive structure is captured principally in three acts. The Investment Code Incentive Act (1983) and the Fiscal Incentives Act (1974) provide incentives for approved manufacturing activity in the form of import duty concessions and corporate tax relief via tax holidays from 10 to 15 years. The approval criteria is primarily the level of value-added, capital intensity or export proclivity. The Hotels Aid Act (1954, 1966, 1993) provides import duty concessions on building materials and equipment used in hotel construction and operation and income tax relief for specified hotels.¹²

48. Separately, incentive legislation also exists for the off-shore financial services industry that is being re-examined in the aftermath of the improved regulatory systems that allowed Grenada to be removed from the OECD’s Financial Action Task Force’s non-cooperative country list in 2003.

49. The incentive structure is opaque and discretionary because of the definitional challenges incorporated within the various acts. While, for example, value-added is a very useful goal at the conceptual level, precise calculations of the value to be added by investment projects are nearly impossible in practice. The lack of a transparent incentive administration structure leads to the situation where most incentives are granted by the highest level of government, the Cabinet. But this element of the country’s incentive administration structure adds an additional element of bureaucracy and delay to the incentive administration process.

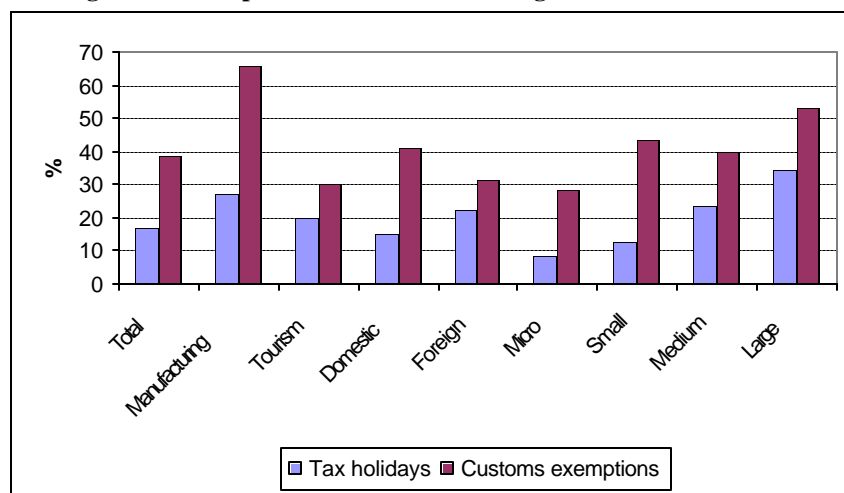
50. In addition, the incentive administration structure has not kept pace with developments in the Grenadian and international economies. For example, incentives in the service industry, outside tourism, are handled through Acts that did not envisage significant investment activity in the service sector, and these acts have not been updated to reflect the changing investment trends. Similarly, the 1953 Hotels Aid Act, understandably, deals with incentives for hotels only and not for broader categories of

¹² Certain provisions were enacted with the 1993 amendment to the Act, which sought to “regularize” tax holidays granted to certain hotels.

tourism. These anomalies are reflected, for example, in a situation in which a hotel with 10 rooms receives incentives, while a yacht that can accommodate many more guests is not eligible for an equivalent set of incentives.

51. Survey results confirm this incentives structure in Grenada (Figure 2.2). Tax holidays are in particular accessed by manufacturing companies, of which more than a quarter are making use of incentives, and hotels and restaurants, of which more than 50 percent have accessed tax holidays. On the other hand, only one of the 26 tourism-related (other than hotels and restaurants) firms in the sample have access to tax holidays. In addition, foreign firms benefit more from tax holidays than domestic firms, and the proportion of firms enjoying them increases steadily with firm size category.

Figure 2.2: Proportion of Firms Accessing Investment Incentives



52. Customs exemptions are much more widely accessed than corporate tax holidays. They are especially important for domestic companies in a wide variety of sectors, but are particularly popular among manufacturing firms, of which two thirds obtained customs incentives, and tourism, where the firms accessing tax holidays also accessed customs exemptions. Although more non-hotel tourism-related firms benefit from customs incentives than tax incentives, this access remains limited to about 20 percent of the sampled companies in the sector. Among those firms making use of the investment incentives, almost all of them (88 percent) reported that these incentives were highly important in making their investment decisions. This is particularly the case with foreign firms, more than 95 percent of which stated that these incentives were very important.

53. The Government of Grenada has recognized that the country's incentive legislation is outdated and needs to be re-examined in light of WTO imperatives. In this regard, the Cabinet has established a Fiscal Incentive Review Committee. This is an important initiative. In the review process, the Committee should make the distinction identified at the outset of this section on incentives. If any investor in Grenada is to compete on world markets, the investment project cannot be subject to taxes on trade that place input costs significantly above world market levels. For many OECS countries, taxes on trade are an important component of government revenue. This is an approach to

revenue generation that Grenada, along with the entire OECS region, need to consider carefully. It is unlikely to be possible for any country to continue in this direction, while at the same time giving its firms the potential to compete on international markets and satisfying its WTO obligations for comparable tax treatment for firms oriented to local and export markets.

54. In relation to relief from corporate taxes, the Fiscal Incentive Review Committee should examine carefully the trade-offs between tax holidays and lower corporate tax rates. The current level of corporate taxes in Grenada, at 30 percent, does not seem like an unusually high rate. However, the tax level has to be examined in the context that there are few deductions allowed when computing corporate taxes. Further, the withholding tax on interest payments of 15 percent also adds to the overall tax burden of firms that have obtained external financing. Indeed, the level of tax rates were identified as the third most important problem in operating businesses in Grenada (Figure 1.5), especially for domestic companies, possibly because more foreign firms have access to investment incentives.

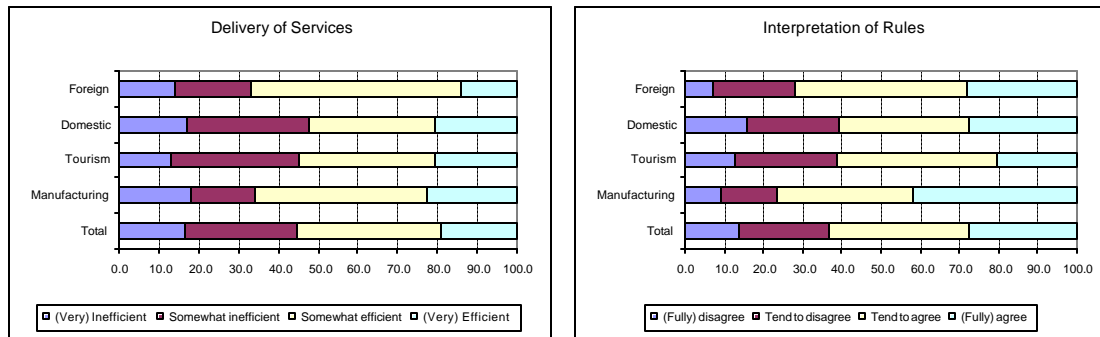
55. International experience (e.g., Mauritius and Ireland) has suggested that lowering corporate tax rates may be a far more effective mechanism for long-term investment attraction than an unwieldy collection of tax holidays. Those countries that have made the trade-off, by lowering corporate tax rates, such as Ireland, have moved to much lower rates than the current rate of tax in Grenada.

B. Government Regulations

56. In a market economy, the main function of the government in economic activities centers around its regulatory role. It is widely recognized that government regulations are necessary to ensure national security, public health, personal and environmental safety, as well as product quality. Therefore, what is at issue is not whether the government should regulate private businesses or not, but whether such regulations are designed in incentive compatible ways to avoid adverse selection and moral hazard, are implemented expeditiously without harassment and corruption, and serve public interests.

57. In Grenada, the majority of the private firms have a fairly positive view of government efficiency. Nearly 20 percent of the firms considered the Government to be efficient or very efficient, with another 36 percent rated the Government as “somewhat efficient.” (Figure 2.3) Foreign firms and firms in manufacturing appear to be more satisfied with the Government than the others, although manufacturing companies are also among those who complain the most about government inefficiency in Grenada. Only a few companies (3 percent) perceive the government as very inefficient in delivering services. Similarly, a fairly positive view prevails about the consistency and predictability with which government officials interpret rules and regulations that affect private establishments.

Figure 2.3: Government Efficiency in Delivering Services and Interpreting Regulations



58. Dealing with government can become time-consuming for managers of many firms. In Grenada, however, time spent by senior management – 6.8 percent on average - in dealing with requirements imposed by government regulations is relatively limited compared to other countries in Central and South America, where the percentages are frequently 10 or higher. In more than two thirds of the cases, managers spend less than 5 percent of their time on administrative and regulatory issues, which compares very favorably with most developing countries.¹³ However, small companies, as well as companies in tourism-related sectors, encounter significantly more administrative hurdles than the other businesses.

59. Despite the generally positive view of the government among private businesses, some companies in Grenada report that gifts or informal payments must be made to public officials in order to “get things done.” Indeed, 17 percent of the companies reported that corruption was a major or severe obstacle to doing business in Grenada, while another 27 percent said it was a minor or moderate problem. Furthermore, about 13 percent of the firms estimated that such expenses would cost establishments like theirs on average 5 percent of their annual sales.¹⁴ Notwithstanding the approximate nature of such estimates, it points to the fact that these payments are not insignificant, considering that profit margins are in the order of 10 percent in most sectors.

Business Start-up, Locating and Operation Procedures

60. In general, the various procedures that regulate business entry, locating and the day-to-day operations are not considered problematic in Grenada. With the exception of customs regulations, for example, more than 60 percent of the firms rated each type of procedure as “no problem” (Table 2.2.). In some cases, such approval ratings are above 80 percent, indicating that investors are generally satisfied with Grenada’s regulatory environment.

¹³ Usually, in less than 20 percent of the cases would top managers spend 5 percent or less of their time dealing with government requirements.

¹⁴ The magnitude ranges between 0.1 and 25 percent.

Table 2.2: Firm Responses to Administrative Procedures (%)

	No problem	Minor/Moderate Obstacle	Major/Severe Obstacle
<i>Entry procedures</i>			
Business registration	83.1	13.4	1.5
Business licensing	77.1	17.4	3.0
Proc. for access to land & premises	67.7	20.9	9.0
Proc. for utility hook-up	63.2	29.4	5.5
<i>Operating procedures</i>			
Business inspections	77.6	17.4	2.5
Fire, safety & sanitary regulation	74.6	17.9	5.5
Labor regulation	61.7	26.4	10.0
Tax administration	59.7	31.3	7.0
Customs regulation	39.8	40.8	16.9
<i>Other procedures</i>			
Patent and trademark reg.	81.1	14.4	1.5
Competition regulation	76.6	13.4	7.5
Foreign exchange regulation	74.1	19.9	4.0
Price regulation	68.7	20.4	9.0
Standards & certification	66.7	22.9	8.5

61. *Entry procedures.* As the large majority of private firms in Grenada have been in business for a long time, the number of those with recent experiences in establishment procedures is relatively limited. For example, there are only 10 firms that have obtained sectoral licenses over the past three years, and a total of 16 firms that have done land title registration during that time (Table 2.3). However, even for this small number of companies, experiences differ widely in terms of both the time needed to complete these procedures and the associated costs. Of the 31 companies having registered a business in the last three years, for example, 12 accomplished this within a week, another 8 within a month, while 3 of the firms spent a year to complete all the related steps.¹⁵ Similarly, while some companies paid as little as EC\$150 (US\$56) for the registration procedure, others paid EC\$5,000. In comparison with regional experiences, this procedure does not seem to be particularly lengthy in Grenada, but the government should strive to standardize the procedure in order to increase predictability in its administration.

62. Table 2.3 presents the median time and costs for undergoing the various entry procedures in Grenada.¹⁶ It should be noted that the use of intermediaries such as legal firms, which is a common practice especially among foreign investors, facilitates the process of setting up a business, but may increase costs significantly. However, the payment of bribes seems to be very uncommon, reported only by three companies. Nevertheless, many firms reported that it is often necessary to make informal payments to

¹⁵ These three companies come in different sizes (one each in micro, small and medium size category), sectors (one each in food processing, garment and textile and financial services), ownership (two domestic and one wholly foreign owned; two with male owner and one with female owner), and location (one each in St. George's, St. George's parish, and St. Andrew's parish). So such extraordinary experience is not restricted to certain types of companies in a specific sector.

¹⁶ Given the small number of responses in some cases, caution should be used in interpreting the cost measures.

public officials “to get things done quickly,” even though corruption was not perceived as a real problem.

Table 2.3: Duration and Cost of Establishment Procedures

	Duration (days)		Cost (EC\$)	
	Median	No. Firms	Median	No. Firms.
Company registration	30	31	1,500	19
General trade license	7	14	500	11
Sectoral license	16	10	1,000	8
Import license	3	25	25	11
Land title registration	60	16	12,500	4
Construction permit	58	24	2,000	12
Electricity connection	16	36	1,000	16
Water/sewage connection	18	21	1,000	13
Telephone connection	7	44	270	25

63. *Inspections.* Inspections are generally not a problem in Grenada. In the past 12 months, only a small number of firms were inspected by the various agencies (Table 2.4.). Sanitation and environmental inspections seem to be undertaken most frequently than others, but in no case were more than 20 percent of the firms inspected by any agency during the 12-month period. Most often, a firm is visited only once or twice a year, if at all, by an one agency. However, there have been cases where an establishment was inspected by the same agency monthly. Hotel, restaurant and other tourism companies were relatively often the target of most inspections, and the food processing industry underwent frequent sanitation/epidemiology inspections. Normally, the inspections last no more than a day.

Table 2.4: Frequency and Duration of Inspections

	No. Firms	Maximum Frequency (visits/year)	Median Duration (days/visits)
Tax Inspectorate	15	12	1.0
Labor and Social Security	7	6	0.6
Fire and Building Safety	19	3	0.8
Sanitation/Epidemiology	40	12	0.3
Customs inspection	18	44 ¹⁷	1.0
Environment	24	7	0.5

64. *Tax administration.* The level of taxes have a direct bearing on the returns of the business to the owners. Moreover, the lack of transparency in tax administration procedures often result in considerable time lost for complying with tax regulations and can offer scope for fines and bribes. Relatively speaking, the taxation system is an area of major concern to private businesses in Grenada. Not only are tax rates considered an important obstacle to business operation, firms also complain about the lack of clarity and

¹⁷ One company reported in the survey questionnaire that it had been inspected by the customs officials 150 times during the last 12 months. However, as the company also reported 150 import declarations, it is suspected that the inspections, or some of them, may have taken place at the port, not on the company’s premise.

transparency in how concessions were granted. In addition, tax administration is rated among the least satisfactory aspect of government regulations. (Table 2.2.)

65. On the incidence of tax payments, the survey revealed that half of the business establishments in Grenada were exempt from, or otherwise evading, the corporate income tax payment in the last 12 months (Table 2.5). About 71 percent of the firms contributed to the National Insurance Scheme (NIS).¹⁸ In most cases, the CIT is paid once a year, although about 14 percent of the firms reported paying the CIT monthly, while the GCT forms were submitted on a monthly basis, as are social security payments.¹⁹

Table 2.5: Tax Compliance

	CIT	GCT	NIS
Share of firms reporting payments (%)	51.2	57.2	70.6
No. of firms reporting fines	8	15	12
Median fines (EC\$)	5,500	400	1,157

66. A small number of firms (around 10 percent) reported that they had been subject to fines for tax reporting related issues. Fines are more often imposed for GCT non-compliance, but are more severe for CIT violations. Foreign firms are proportionally less often fined than their domestic counterparts, although the precise reason for this outcome cannot be divined from the survey results.

67. *Customs administration.* Among all government regulations that affect business operations, by far the most serious constraint is customs regulations (Table 2.2). Trade transactions carried out by the sampled firms relate mainly to import transactions. Over the past 12 months, only 18 firms reported that they had made export transactions, whereas a total of 101 firms reported undertaking import transactions during this period. On average, it takes about 1.5 to 2 days for exports to clear the customs. Clearance of imports is more time-consuming, with a median duration of 4 days. Payment of bribes appears to be fairly unusual, but not completely nonexistent. Four companies reported paying bribes, all for customs processing of import transactions.

68. Several companies complained about the length and difficulty of the clearance procedures at customs. It was reported that some investors had been discouraged by customs harassment, the amount of paperwork, and the elaborate procedures. To avoid the hassle at customs, several companies pay for a brokerage service to do the customs clearing.

69. It was also reported that restrictive customs practices had a particularly adverse impact on the yachting industry. Regulations make it difficult to take yachts, which are registered in other countries, to travel to Grenada. The customs regulation is bureaucratic and the fees for customs registration and clearance are high. Local yacht chartering companies indicated that the paperwork for taking out a yacht on a trip in the region

¹⁸ As the sample was constructed from the list of firms provided by the NIS, all were contributing at some point, even if not in the past 12 months.

¹⁹ Other main taxes to be paid include excise tax, property tax and stamp tax.

requires a full day, obliging those renting a yacht to arrive in the islands at least one day before their scheduled departure. It was also noted that there was no cooperation between immigration and customs offices of different islands in the region, requiring the repetition of procedures in order to sail from one island to the next.

70. A problem reported by the retail sector and by liquor production companies concerns the growth of illegal trade of highly taxed goods such as liquor and cigarettes. Using small boats, these products are smuggled from the tax-free islands in the area into Grenada.

71. *Competition and standards.* Anti-competitive practices were regarded as at least a moderate problem, with nearly 20 percent of the firms reporting that they were a major to severe constraint to their businesses. (Figure 1.5.) Indeed, the government still maintains a large number of items on the price control list, although it aims to reduce this number. Consequently, 9 percent of the surveyed firms reported that price regulation is a serious obstacle to their operation and growth. Meanwhile, several commodity boards, such as the powerful Nutmeg Association, remain monopolies which control the purchase, sales and export of most of Grenada's spice products.

72. Partially reflecting the small size of Grenada's local market and partially as an indication of the prevailing protection, more than half of the surveyed firms reported that their market share exceeds 50 percent. This is particularly notable for the manufacturing sector, where several products are still protected under quantitative import restrictions. Foreign companies, being larger and better positioned in general, have more market power than their Grenadian counterparts.

73. Standards and certification are considered a minor problem. Most firms are not aware of any regulation regarding standards and certification. One shop owner could recall that once a year the shop is visited by inspectors of the weights and measures department to check whether the scale is still correct. According to a tour operator, the lack of standards is a problem in the tourism sector. Tour operators from abroad usually call to enquire about fire and safety standards at the hotels before deciding on sending their customers. They are put off by the fact that Grenada does not have standards to be met or certified for. Therefore, setting and enforcing appropriate industrial standards not only protects consumer rights through better product quality, but also encourages responsible investment.

74. *Conflict resolution.* There appears to be a general confidence in the judicial system to enforce contractual and property rights in business disputes. However, there also exist a substantial minority of 33 firms which have doubts, especially among larger firms and firms in the tourism sector. The majority of reported disputes are with clients, and there are hardly any issues with the local governments (Table 2.6). Foreign firms, large firms, and firms in tourism-related industries appear to have been involved in more disputes with clients and suppliers than the others. Most firms prefer to settle out of court, because the disputes are no serious enough and it is easier to settle out of court.

Table 2.6: Proportion of Firms in Dispute (%)

	National government	Regional / Local government	Suppliers	Clients
Total	6.5	1.0	7.5	21.4
Manufacturing	9.1	-	4.5	13.6
Tourism	7.1	1.8	14.3	17.9
Domestic	6.4	1.3	5.1	19.2
Foreign	6.7	-	15.6	28.9
Small	-	1.4	7.0	18.3
Medium	9.1	-	5.5	16.4
Large	10.7	1.3	9.3	28.0

75. *Security.* Crime is reportedly becoming an increasing problem, especially petty theft. In spite of this threat of rising crime, costly security measures are not yet taken by many firms. Half of the companies report that their security costs are negligible in relation to sales, but for 10 percent of the firms, security measures cost more than 5 percent of their total sales. The median value of security costs in Grenada is about 2 percent of the annual sales. As expected, small firms tend to be more lax about security issues than large and foreign companies.

76. Similarly, the costs of crime are estimated to be negligible by a majority of the companies (62 percent). In the last year, 74 firms reported losses due to theft, robbery, vandalism or arson against them, with a median loss value estimated at 4 percent of the total sales. A little over half of the companies report all or most of the crime incidences they experience to the police and most of these incidents appear to have been resolved.

CHAPTER III

PHYSICAL AND FINANCIAL INFRASTRUCTURE

A. Physical Infrastructure and Support Services

77. Reliability, quality and costs of infrastructure facilities play an important role in determining the competitiveness of private businesses and in the attractiveness of the overall investment climate. In recent years, the Government of Grenada made significant effort in this area by upgrading roads and other basic infrastructure facilities. At the same time, as part of the Government's privatization program, the majority shares in several publicly owned utility companies, such the Electricity and Telephone companies, have been sold. In the area of telecommunications, while Cable and Wireless, a joint venture between Cable and Wireless (W.I) Ltd. and the Government of Grenada, still holds a monopoly on land-based lines, the market for mobile telephone has been liberalized recently and a foreign mobile phone company from Ireland, Digicel, has started operations. Further liberalization is planned.

Utilities

78. One element influencing Grenada's prospects for attracting investment, including FDI, which is directly linked to the country's size and geography, is the high cost of utilities. Electricity costs, in particular, are much higher than comparable costs in large mainland territories, such as the United States, and in energy-producing countries like Trinidad and Tobago. Existing foreign investors in Grenada have indicated that electricity costs are almost three times as high as comparable costs in the United States. Consequently, electricity was considered the fifth biggest obstacle to doing business in Grenada. For water and telecommunication services, although a majority of the firms find them not a problem to business operation and growth, about 15 percent of the companies have encountered major to severe problems in these areas.

79. Costs apart, the reliability of the services is even more important. Although some investors report that the provision of electricity services has improved significantly over the last decade, the survey revealed that more than half of the private companies have experienced power outages or surges from the public grid over the past 12 months (Table 3.1). For some companies (13 percent), power problems occur at least once a month, and in 70 percent of the cases the interruptions last more than a couple hours each time. Needless to say, such interruptions seriously disrupt normal business operations by causing production stoppage and delivery delays. As a remedy, many big firms invest to keep a generator on the premise as back-up.

Table 3.1: Utility Service Interruptions

	Firms Affected (%)	Incidence Frequency (days/year)	Average Duration (hours)	Associated Costs (EC\$/year)
Power outages	51	4	3	1,250
Insufficient water supply	22	12	6	3,500
Unavailable mainline telephone	8	3	4	2,175

80. Interruptions due to insufficient water supply and lapses in mainline telephone services are less common, affecting 22 and 8 percent of the companies, respectively. However, for the companies affected, they tend to happen more often than electrical outages and the problems require more time to resolve. For water supply, in particular, several companies report that it sometimes shuts off for more than 24 hours at a go, shutting down production completely for days. There appears to be a general shortage of water in some months, when water is available only a few hours a day.

81. To deal with this problem, 15 percent of the firms supplement public water supply with private sources. Of the 25 firms which reported making use of own wells or reservoirs, 5 rely on them for 100 percent of their water supply. In addition, 10 companies reported purchasing water from private vendors in order to meet their water consumption needs for business operation. Inadequate water supply is felt particularly strongly by the companies in the tourism sector, among which a much higher proportion has turned to private sources for water supply than the overall average in Grenada.

82. Naturally, when such service interruptions happen, they impose costs on the enterprises because of lost production time, the extra time and cost needed to re-set the machines, and the associated production and sales losses as a result of the utility disconnection. Estimating such costs, however, has been difficult for the surveyed firms. A quarter of the companies put the loss figures due to power outages at above EC\$10,000 annually, while the median value is around EC\$1,250. For unreliable water and telephone provisions, even though they seem to affect a smaller population than power problems, the costs associated with the interruptions of these services – EC\$3,500 and EC\$2,175, respectively - are higher than those of electricity.

83. It should be noted that companies which have a generator tend to rate power outages less of a problem than those which do not. They do not really associate costs with power interruptions either. As noted by some enterprises, since the generator represents a sunk cost for the company, it is actually cheaper to run the generator than to buy from the public grid. A similar reasoning applies to water tanks – once installed, the impact of water shortage is reduced and the tank costs very little to maintain. Therefore, the survey results discussed above may understate the extent and severity of the problems with the access to utilities. In fact, companies that have a generator on stand-by may not actually know the number of power cuts having taken place. Finally, for companies located outside of the main island, utility access problems are magnified. One Carriacou-based entrepreneur reported, for example, that the island experiences frequent power cuts.

84. As for telecommunication services, although complaints about interruptions are relatively mild compared to other factors of the investment climate, they disproportionately affect some of the fastest growing industries, such as ICT firms and tourism-related businesses, much more than traditional industries. A call center reported, for example, that the few service interruptions had been very costly for the company. Moreover, while Grenada compares reasonably well with its neighbors in terms of mainline telephone coverage, it lags behind all countries in the region but Haiti when it comes to mobile phone services.²⁰ Indeed, a majority of the countries in the Caribbean have moved to rely more on mobile phones than fixed line services - the ratio of mobile to mainline telephones is 3.2 times in Jamaica, compared to Grenada's 23 percent. The recent liberalization of the mobile phone market may help Grenada catch up in this respect.

85. Clearly, for a small island nation like Grenada, with limited power and water resources, the question of how to ensure reliable and reasonably-priced utility supply does not have an easy answer. However, by improving the policy and regulatory framework, the Government can provide incentives for long-term investment in these areas in order to expand the coverage of utilities and encourage more efficient resource utilization. Some businesses also think that utility companies have a role to play in assisting companies upgrading energy efficiency.

Transportation and Ports

86. The extent to which transportation is a constraint to business depends a great deal on the destination of transport. On the whole, international transportation to destinations outside the CARICOM is considered more of a problem than within the region, which in turn is more problematic than local transportation.²¹ However, according to some companies, local transportation is becoming a problem as the roads are small and in need of repair outside the major cities.²² This makes it very difficult for trucks with heavy loads to pass.

87. The increase in the number of vehicles in recent years has resulted in increased congestion, further magnifying the need for more and better inland transportation facilities. In addition, as the public transportation system does not reach many residents on the island, and buses only operate on a regular basis till the early evening, companies which operate in shifts have to provide evening transport services for their employees. Nevertheless, transport failures are not common, affecting only 6 percent of the firms over the last year, and mainly refer to sea transportation facilities.

88. Grenada has one major seaport in St. George's (capital city) and eight smaller ports, including one in Carriacou. General port development in recent years include new

²⁰ According to World Bank statistics.

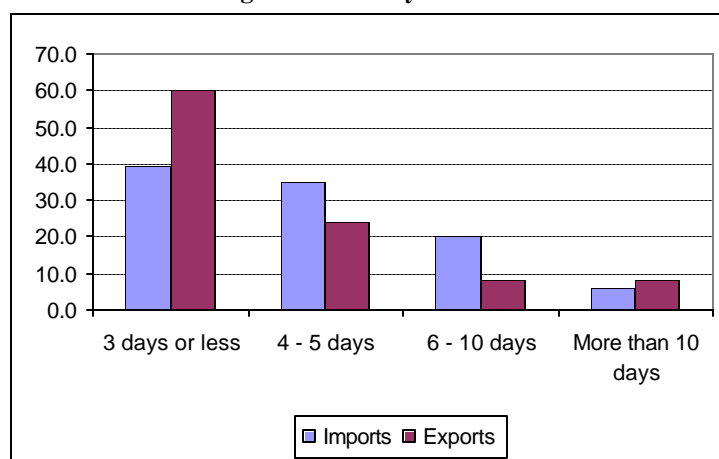
²¹ The proportions of firms ranking local, CARICOM and international transportation as a major or severe constraint to growth are 10, 14 and 20 percent.

²² The road density in Grenada (about 1 km per 1000 people) is below the Latin American average, but 50 percent of the roads are paved, which is substantially higher than the regional average of 24 percent.

berth spaces, a container park and other operational improvements. An EC\$21 million port expansion began in August 1997 and was designed to accommodate an increased volume of container traffic.

89. Despite the general grievance over customs regulations, including the 5 percent handling charges imposed on the importing and exporting companies, the survey results indicate that rules are generally enforced when it comes to port charges as there is a fairly common response to the handling costs of a 40-ft container (about EC\$ 700). Figure 3.1 presents the average delays for a shipment of supplies to clear through the ports in Grenada. As reported by the businesses, clearing the customs at ports is relatively quick for exports (2 days), but slow for imports (5 days).²³ More than a quarter of the companies have to wait for a week or more before their shipments are released from the ports. Such delays add significantly to the turnaround time for the companies.

Figure 3.1: Delays at Ports



90. Table 3.2 reports the average transport costs to ship a 40-ft container and time needed to reach the destination. Only a small number of companies (10) provided this information, but their responses are highly consistent with one another. Overall, transportation costs account for about 12 percent of the sales price in Grenada, although the ratio is somewhat higher for micro and small sized enterprises (15 percent), and for domestic firms (14 percent) as compared to foreign companies (9 percent).

Table 3.2: Transport Costs and Time

	Cost of Transport (EC\$)	Time to Destination (days)
Local	475	1
CARICOM	3,500	5
International	16,850	10

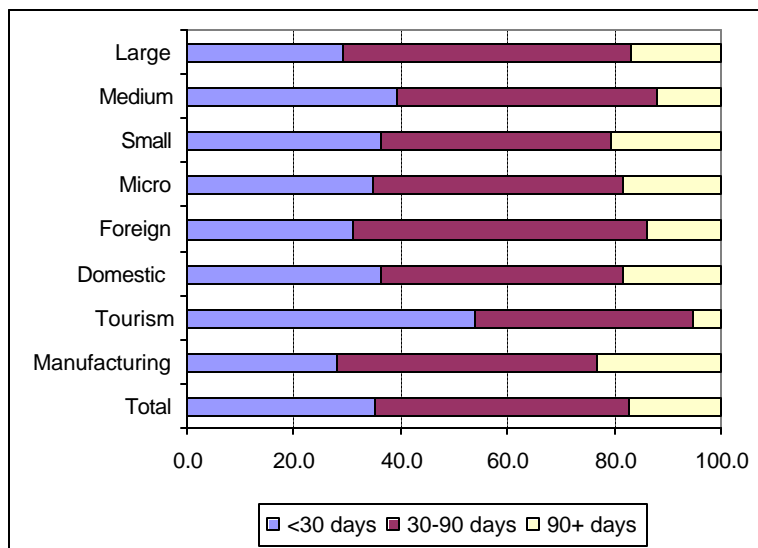
91. One of the obstacles in transport with other CARICOM countries and beyond is the low frequency of boat services between Grenada and the destinations. As reported by businesses, the only shipment service that is frequent is the one between Grenada and

²³ These numbers are consistent with information on customs administration.

Trinidad & Tobago, yet it is not always reliable. Shipments to more distant places, even Miami, may be as rare as once a month. Shipping companies, of which Grenada has six major ones, explained that if there were more goods to be shipped to and from Grenada, they would provide more frequent services. The low trade volume and lack of economy of scale are also partially responsible for the high costs of freight, insurance costs and handling charges that many companies find burdensome. As an example, a 20-ft container costs more than US\$2,000 in Grenada, compared to US\$900 in Trinidad and Tobago.

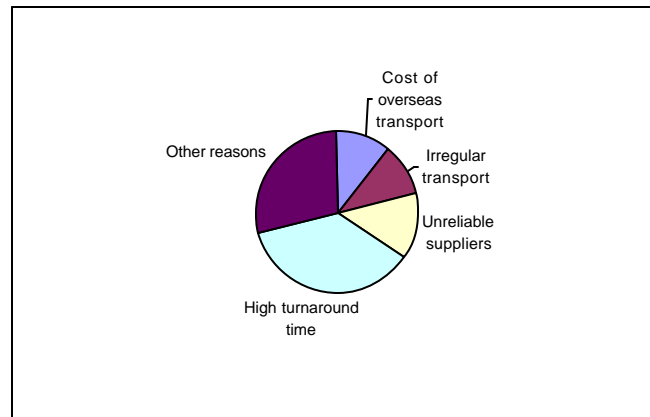
92. Given Grenadian companies' dependence on imports for inputs, long customs delays, high transport costs and unreliable shipping services, it is hardly surprising that firms in Grenada keep very high inventory on hand. As shown in Figure 3.2, two thirds of the firms keep stocks of more than one month and 10 percent of them have inventory periods that last as long as half a year. Such substantial inventory not only ties down the firms working capital resources, but also incur additional costs in terms of storage and safekeeping, etc.

Figure 3.2: Share of Firms by Inventory Periods



93. Among the reasons for keeping large volumes of stocks, high turnaround time came out No. 1 on a list of contributing factors (Figure 3.3). Other reasons include unreliable supplies either because suppliers are not dependable or because it is difficult to find the products locally. The costs and irregularity of overseas transportation services are also important reasons. In addition, the companies prefer to maintain high levels of inventory in order to ensure efficient operations, to take advantage of lower prices for bulk purchases, and to avoid thefts and other losses during transit.

Figure 3.3: Reasons for Holding Inventory



Business Support Services

94. Business support services can play a significant role in improving business operations and efficiency. The availability and quality of such services, as well as the extent of their utilization, are important aspects of a country’s overall investment climate. In Grenada, a range of these professional services are available, and to a varying degree companies make use of them (Table 3.3). Although the relative popularities of the various services remain constant across all firm sizes - that is, all firms make use of insurance and legal services more than marketing and management consultancy - micro and large companies turn to these services less frequently than their small and medium sized counterparts. One possible explanation is that micro firms do not find them as necessary due to a lower level of complexity of their businesses, while large companies have in-house experts to handle the relevant issues themselves. What is not at issue is the affordability of the services as there is just as high a proportion of the micro firms saying that the various services are affordable.

Table 3.3: Business Support Services

	Utilization (% firms used)	Affordability (% firms saying yes)	Quality (average rank)
Insurance	77.4	85.7	3.0
Legal services	73.3	83.3	3.1
Accounting	69.9	82.8	2.9
IT services	52.9	92.4	3.3
Engineering	39.7	81.7	3.2
Marketing	32.6	76.5	3.1
Management	27.7	88.2	3.0

Note: Scale for quality ranking: 1= very poor, 2 = poor, 3 = good, 4 = very good).

95. In all these business support areas, a number of firms, ranging from 5.6 percent for legal advice to 46 percent for management consulting, have made use of the international professional service providers, either exclusively or in combination with domestic providers. The great majority of the companies in Grenada think that these services are both affordable and of good quality.

B. Getting Finance

96. A critical factor in undertaking investments for growth and improving efficiency is the access to reasonably priced funding. In Grenada, equity, quasi-equity and long-term debt financing are available from a number of local, regional and international institutions. The Grenadian banking system includes the following institutions: the Grenada Development Bank; commercial banks including, the National Commercial Bank of Grenada, Grenada Bank of Commerce, Barclays Bank, the Bank of Nova Scotia and Grenada Cooperative Bank; and several fledgling venture institutions. However, as foreign investors are required to obtain permission from the Minister of Finance in order to borrow from local financial institutions,²⁴ these banks and institutions tend to serve the local and/or regional business communities. Moreover, they are not very active in the area of equity financing.

97. The European Investment Bank and the International Finance Corporation also offer loan and equity financing, and generally without any bias towards any groups of investors. In addition, various merchant banks, particularly those based in Trinidad and Tobago, provide access to regional capital markets, both through direct loan and equity financing, as well as through underwriting of corporate bonds for sale to regional investors.

98. Despite these institutional set-ups, the cost of and access to finance are considered to be one of the biggest obstacles to business operation and growth in Grenada. (See Chart 1.5.) Indeed, the cost of financing was rated as a severe obstacle to enterprise development by more companies than any other factors that constitute the investment climate.

Sources of Finance

99. In Grenada, by far the most important source of finance for working capital is own funds and retained earnings, followed by commercial bank credit (Table 3.4). Among the 131 firms that provided information on how their working capital needs are met, 85 percent reported using own funds and retained earnings, of which 40 percent relied on this source exclusively.

²⁴ A requirement of the Exchange Control Act.

Table 3.4: Sources of Finance

	Retained Earnings	Banks	Trade Credit	Venture Capital	Equity	All Other Sources
<i>Working Capital</i>						
Average share in total finance (%)	60.2	25.5	4.5	1.8	1.5	8.2
No. firms accessing the source	111	68	28	3	9	36
No. firms relying the source entirely	45	8	0	2	1	1
<i>New Investment</i>						
Average share in total financing (%)	48.4	42.0	0.4	0.8	2.1	6.4
No. firms accessing the source	51	41	2	1	3	11
No. firms relying the source entirely	25	17	0	0	1	2

100. Local commercial banks are relied upon to provide the working capital to 57 percent of the domestic firms and 36 percent of the foreign companies. In addition, 6 establishments reported using loans from overseas commercial banks for financing their working capital, half of them are foreign owned companies. It should be noted that although the additional requirements on foreign investors with regard to their access to local financial institutions do seem to deter some foreign companies from accessing local banks, two of the wholly foreign owned companies rely 100 percent on local bank loans to meet their working capital requirement.

101. In contrast to many developing countries in the region, supplier or customer credits are not commonly utilized as a form of financing in Grenada. In several Central American countries, for example, trade credits account for over 15 percent of working capital resources,²⁵ compared to Grenada's 4.5 percent. Further, neither equity nor venture capital is a significant source of funding for Grenada's companies, and there is no significant difference between the various types of companies in how they finance their working capital needs.

102. A total of 74 firms reported new investment during the past year. For new investments, own funds and bank lending continue to be the most significant sources of financing in Grenada, although in this case the banks' importance outweighs that of retained earnings for half of the firms. Another notable feature is that equity financing is relied upon by large companies for 10 percent of their new investments, and that family and friends are important sources of capital (12 percent) for tourism sector firms.

103. Only a few companies (26) reported borrowing in foreign currencies, 9 of which are FDI and most are large companies. One important reason for this limited reliance on overseas financing sources is that domestic residents can only open savings account in foreign currencies on the island, not checking account. This makes it virtually impossible to conduct business transactions in foreign exchange.

²⁵ Supplier credits finance about 18.3, 13.0 and 16.3 percent of the working capital in Guatemala, Honduras and Nicaragua, respectively.

Working with Local Banks

104. A majority of the companies in Grenada have overdraft facilities or line of credits at the local banks. Larger companies make more use of these facilities than smaller companies and they are more popular among domestic firms than foreign firms. Of the companies that reported using them currently, 38 percent indicated that their utilization rates were 100 percent, while at the same time about half of the companies reported using less than 50 percent of the approved limits.

105. For their most recent loans or overdrafts, half of the firms obtained them fairly recently. That is, within the last two years. However, this also means that for a significant group of companies (47 percent,) their last loan was concluded several years ago.

106. When borrowing from the local banks, a collateral or a deposit is usually required. However, this requirement does not seem to be applied equally to all firms. Fewer foreign companies, for example, reported pledging collaterals against their loans than their local counterparts, and large manufacturing companies appear to be able to do away with them more easily than the rest. Moreover, the requirement of collateral appears to have been relaxed steadily in recent years as the proportion of firms reporting collaterals dropped significantly from 90 percent in 2001 to only 60 percent in 2004. This means a significant number of firms do not need to pledge collateral for their new loans.

107. As is the case elsewhere, land and buildings are the most important forms of collateral in Grenada, which are used by two thirds of the companies to secure loans and overdrafts from local banks and account for the more of the collateral values than all alternatives (Table 3.5). Second in line are the personal assets (i.e., their houses) of the owners and/or managers of the companies. Indeed, about 20 percent of the firms rely exclusively on their personal assets to secure bank loans for their business operations.

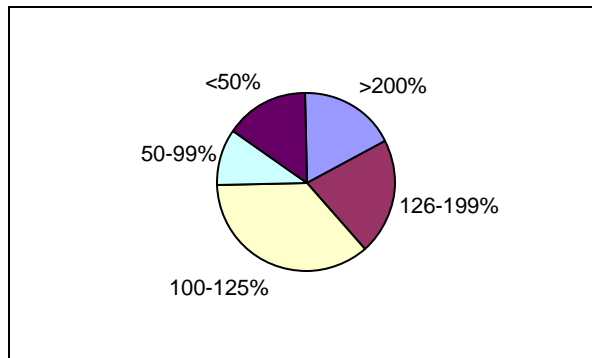
Table 3.5: Types of Collateral

	Land & Buildings	Machinery	Intangible Assets	Personal Assets
No. firms providing as collateral	52	27	21	29
No. firms using as 100% collateral	26	3	4	15
Average share in total collateral (%)	77.3	39.8	46.2	69.5

Note: Based on the 78 firms which provided complete information on collateral.

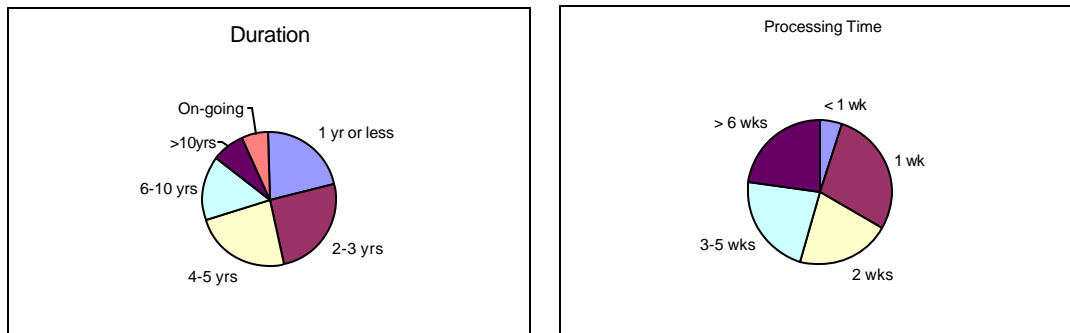
108. The value of collateral in relation to the value of the loan varies quite significantly, with the collateral to loan value ratios ranging from under 50 percent to five times. Although on the whole collateral levels do not appear to be excessive, that close to 40 percent of the firms have collateral to loan ratios of more than 125 percent indicates that bank lending policies are quite conservative in Grenada (Figure 3.4).

Figure 3.4: Collateral to Loan Ratio



109. The interest rates paid by the firms are fairly consistent, varying between 9-12 percent in most cases. The duration of the loans, however, varies significantly, ranging from one week to 20 years and some loans are on-going. (Figure 3.5.) The loan durations tend to be longer for larger firms. Similarly, there is a wide range of experiences in terms of how quickly a loan application is processed. In a majority of the cases, this was done fairly quickly – within 2 weeks - but it has proved to be a lengthy affair for some firms. Longer application periods have been experienced by medium and large domestic firms, likely for loans of longer duration.

Figure 3.5: Duration and Processing Time of Loans



110. With regard to external financing, three quarters of the companies reported that they had not sought to access other sources of funding than local bank loans. According to these companies, they are not doing so because they are reasonably satisfied with the services of the local banks, there is no real need for them at the moment to seek alternative sources of financing, or that they are not familiar with what else is available and how to proceed. Some also believe that they will not be able to meet the requirements of other fund sources.

111. About 60 percent of the companies reported that their accounts are reviewed by external auditors. These include most foreign companies, two-thirds of the medium and large companies, but less than half of the micro companies. The lack of accurate financial information from independent sources about the firms increases the financial institutions' costs and burden in processing loan applications, which is passed on to the borrowers as denied access and high financing costs.

Additional Remarks

112. Although some investors report that their bank has provided them with useful support, albeit at relatively high interest costs, many respondents indicate that they have experienced problems with obtaining finance. There is a general perception that the local banking sector is underdeveloped and that commercial banks, in particular, do not provide the venture and project support required of many companies. The banks, in response to the criticism that their approaches to lending are traditional and conservative, suggest that there is an absence of “bankable” projects in Grenada, particularly projects oriented to the export sector, and that they face extreme difficulty getting accurate financial information from many Grenadian firms. Proportion of firms providing collateral for their loans is declining also suggests that commercial banks are moving more to project and cash-flow as opposed to asset-based lending, which is what firms have been saying that they would like to see.

113. One type of financial institution which exists around the world and provides important services to the business communities, but remains obscure in Grenada are credit unions. Next to the dominant national and international banks, only a few credit unions are operating. According to some of those interviewed, credit unions are not getting off the ground in Grenada because of the operations of the Grenada Authority for the Regulation of Financial Institutions (GARFIN). Under GARFIN’s indiscriminating regulation, all financial institutions are treated alike, without taking into account the particular characteristics of credit unions relative to other financial institutions. For example, profit maximization is less important an objective for credit unions than for other financial institutions. Moreover, smaller credit unions may not be able to meet the more stringent regulations applicable to larger financial institutions.

114. For many years, firms operating in Grenada and the Eastern Caribbean region did not have access to a source of funding that firms in most countries take for granted: the ability to gain public equity through initial public offerings. Since 2001, this situation has changed with the introduction of the Eastern Caribbean Securities Exchange (ECSE). This is a regional securities exchange operated by the Eastern Caribbean Central Bank designed to provide an integrated market for corporate stocks and bonds and government securities for the eight member territories of the OECS. The introduction of the ECSE, the first regional securities market in the Western Hemisphere, clearly provides increased opportunities for access to public equity for companies operating in Grenada. The nascent exchange has yet to have a significant impact in this area, however, as most of its activity, to date, has revolved around issuance of government securities. Only a handful of corporate stocks are currently listed on the exchange.

115. With the growth of the ECSE more companies will take advantage of this access to financing. There are also other areas of financing need. Currently, the proposed trade support network in Grenada does not explicitly include financing activities. It is worthwhile to include an institution such as the Grenada Development Bank as a formal part of the country’s trade support network. It is routine for governments in developed

and developing countries to have some level of involvement in trade financing through export-import banks. An element of the support that is necessary is training in the generation of appropriate financial information. Additionally, Grenadian firms can utilize more effective working capital management to assist in the provision of financing. The data suggest that Grenadian firms currently place much less reliance on trade credit as a financing mechanism than their counterparts in other countries.

CHAPTER IV

LABOR AND INNOVATION

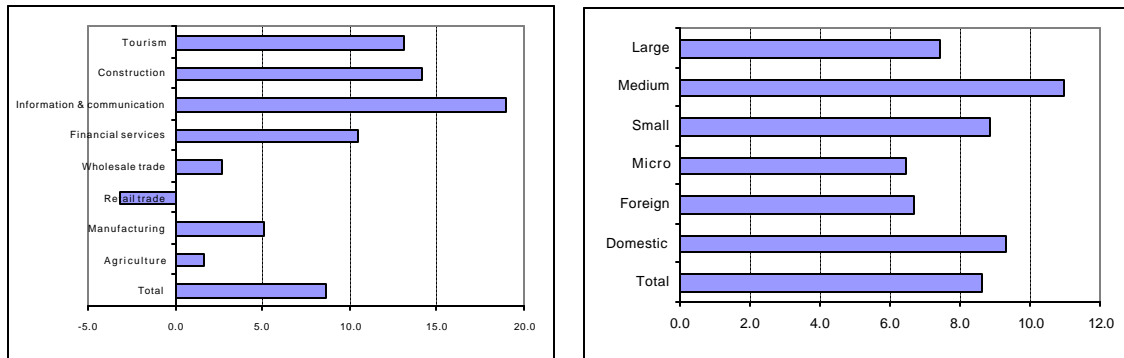
A. Labor Market

116. With an unemployment rate of 12 percent of the workforce, one of the clearly stated development objectives of the Government of Grenada is to generate employment and income earning opportunities through private sector growth. At the same time, as labor is also a key factor which determines how and how much private businesses can grow, it is an important aspect of the overall investment climate. A flexible and well-regulated labor market will on the one hand facilitate companies to recruit the type and quality of workers they require to operate efficiently, and on the other hand ensure that workers' welfare are protected.

Employment Dynamics

117. Permanent employment in the private sector grew by 8.6 percent in the two years between 2001-03.²⁶ With the exception of retail trade, all sectors experienced expansion in their employment levels. Some especially fast growing sectors include information and communication (19 percent), construction (14 percent), tourism (13 percent), and financial services (11 percent). In addition, medium sized companies have expanded their workforce at a faster pace than either smaller or bigger firms, while foreign companies have generally lagged behind domestic firms in creating new jobs in Grenada (Figure 4.1).

Figure 4.1: Employment Growth by Sector and Type of Firms



118. A third of the companies reported employing temporary workers. In effect, with a growth rate of 33 percent over the last two years, the expansion of temporary

²⁶ The calculation is based on the responses from the 159 companies which reported their employment levels for all three years between 2001-03. This treatment excludes all those firms that were established after 2001. However, since the survey does not capture the firms which have gone out of business by early 2004, a decision was made not to include the new firms as well.

employment has surpassed that of permanent jobs. Temporary workers now make up 8 percent of the total workforce in the private sector. They are mainly engaged in activities that have a seasonal characteristics, such as agriculture and construction, as well as the new industries like information and communication. Micro and small enterprises rely far more on temporary workers than bigger firms, while financial services industries and foreign companies offer proportionally fewer temporary job opportunities than the rest. It should be noted that temporary female employment has experienced a particularly strong increase (51 percent) during this period.

119. Foreign workers play a small but significant role in the labor market of Grenada. 30 percent of the firms reported employing foreign nationals, which account for 3.3 percent of the private sector labor force. Foreign workers are found in all sectors except agriculture, but concentrate in construction (35 percent) and non-hotel tourism industries (15 percent). Although large companies employ more foreign workers, they make up a much higher proportion of the workforce in micro and small establishments than in medium and large firms. About 20 percent of the foreign employees are temporary workers, mainly in construction, but also in hotels. In addition, large foreign firms also have higher percentages of temporary workers than smaller domestic establishments. The largest group of foreign workers is from other CARICOM countries, but the UK and other European countries are also major countries of origins among foreign workers.

Wages and Compensation

120. The data collected about wages and total compensation of workers show considerable variations between different skill levels.²⁷ Even within the same skills category, there are large discrepancies between different types of establishments. Table 3.7 presents the median wage values for the sampled companies in 2003. The data show that wages are generally higher in manufacturing firms than the national average, and higher in foreign firms than domestic companies. Moreover, wages appear to increase with firm size, except that due to the inclusion of professional services establishments, micro firms seem to compare very well with their larger counterparts.

Table 4.1:²⁸ Median Wages (EC\$)

	Management	Skilled workers	Unskilled Workers
No. Respondents	31	32	19
Total	42,884	13,196	10,095
Manufacturing	69,962	14,627	11,135
Tourism	39,167	13,798	10,716
Domestic	27,556	10,772	6,177
Foreign	80,352	18,531	16,810
Micro	43,280	12,893	26,625
Small	25,340	13,491	7,137
Medium	27,778	5,075	2,628
Large	79,977	18,652	10,885

²⁷ An unskilled worker is defined as one who does not need any training at all to perform the required tasks.

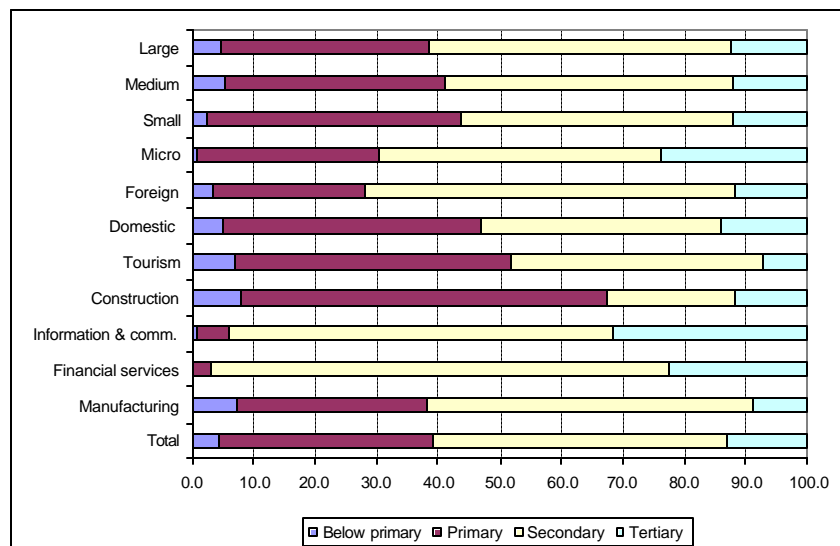
²⁸ Caution should be used in reading this table as some values may not be entirely representative due to the small number of responses in some categories.

121. There are also considerable differences between wages and the total compensation offered by the enterprises. Depending on skills category, the median compensation premium ranges between 3-30 percent of base wage. Such discrepancies may be another indication of skills shortages as they are the largest for people with managerial skills, and a reflection of strict labor regulation, which is considered by 10 percent of the companies as a major or severe constraint to business operation.²⁹

Skills and Training

122. Grenada has a good educational system. For a total population of less than 100,000, there are 62 primary schools, 20 high schools and 3 post-secondary schools including one medical school. Adult literacy is above 98 percent, on par with most developed countries, and approximately 2000 students graduate from secondary schools every year. In recent years, courses on information technology has been introduced at all levels of education. Consequently, as reflected by the survey, the educational attainment of the Grenadian labor force is reasonably high, with nearly half of the workers having high school diploma and another 13 percent with tertiary education.³⁰ (Figure 4.2)

Figure 4.2: Educations Attainment of the Labor Force (%)



123. Interestingly, the general expansion of jobs in recent years has occurred at the two extremities of the skills spectrum: among the fastest growing sectors are some highly skills-intensive industries such as information and communication and financial services, where workers with secondary and higher education account for more than 90 percent of

²⁹ As is true elsewhere in the Anglophone Caribbean, Grenada's labor laws, particularly as amended in 1999, are generally viewed to be quite protective of the rights of workers. However, no specific complaint was heard in this regard from the enterprises interviewed during the field mission. Further investigation is thus recommended to arrive at more concrete conclusions.

³⁰ The high educational attainment levels in micro firms reflect the inclusion of small financial services companies.

the workforce, but also those which depend heavily on unskilled labor like construction and tourism, where workers with little formal education make up the bulk of the total employment. It should be noted, however, that within tourism a difference should be made between hotels and other tourism related services because while the former recruits many unskilled workers, 60 percent of the workforce in the latter have secondary or higher education levels.

124. On the balance, however, there is the general feeling of skills shortage among private enterprises in Grenada. Issues related to inadequate skills and education levels of the workforce were ranked as the No. 1 constraint to business growth (Figure 1.5). As identified by the enterprises, the key skills missing in Grenada are technical skills such as industrial engineering, and managerial skills at middle and senior management levels. The lack of skills is further reflected by the difficulties with which firms recruit qualified personnel. As seen in Table 4.2, there have been far fewer vacancies for management and skilled posts than for unskilled posts, and when they do occur, it takes much longer to find suitable candidates to fill these vacancies than for unskilled posts.

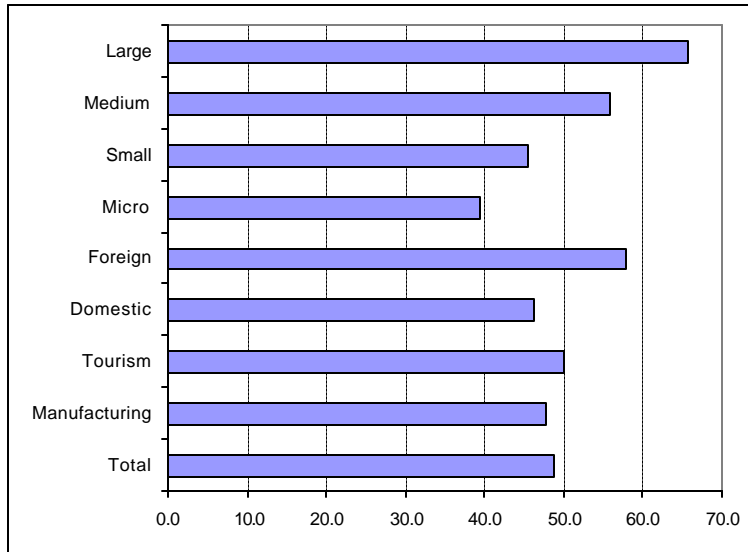
Table 4.2: Time Needed to Fill a Vacancy

	Management	Skilled worker	Unskilled worker
No vacancies reported (% firms)	29.4	23.9	12.4
Median delay (weeks)	8	4	1

125. To remedy the skills shortage problem, about one half of the companies reported offering formal training to their employees (Figure 4.3). Although foreign companies are more likely to offer training than domestic companies and larger establishments tend to train more than smaller ones, there remain a considerable number of firms – a third or more – that do not provide any formal training. Among the companies that do, 84 percent said they provided formal training to skilled workers in 2003, but only 31 percent indicated that they offered such opportunities to unskilled workers. In this regard, foreign firms stand out for not only offering formal training to their workers more frequently than their domestic counterparts, but also covering a larger proportion of the workforce.³¹

³¹ Among the foreign firms which provided formal training to the workers, 92 percent of the skilled workers and 39 percent of the unskilled workers received training in 2003, as compared to 81 and 29 percent, respectively, for domestic firms.

Figure 4.3: Share of Firms Offering Formal Training (%)



126. Across all firm size categories and different economic sectors, structured in-service training is by far the most commonly used training mode for private companies in Grenada. It provides 61 percent of the formal training to skilled workers and 85 percent of that to unskilled workers (Table 4.3). This suggests that although Grenadian firms under-invest in training in general, the private sector is taking on the main responsibility of upgrading the skills content of the labor force. Even among the external training providers, the importance of the private sector stands out once again as private training facilities are frequented several times more than public training institutes. Indeed, the public training centers in Grenada lag so far behind the private sector in offering the kind of training demanded by the companies that they account for barely 9 and 3 percent of the total training provided to skilled and unskilled workers, respectively.

Table 4.3: Share of Firms by Types of Training Institutions

	Skilled Workers			Unskilled Workers		
	Internal	External		Internal	External	
		Private	Public		Private	Public
Total	77.6	52.0	19.4	92.6	31.5	13.0
Manufacturing	61.9	36.6	1.5	96.4	3.6	0.0
Tourism	56.3	25.8	18.0	79.8	16.8	3.3
Domestic	52.7	35.7	11.7	79.1	16.5	4.4
Foreign	67.0	30.5	2.6	91.4	8.6	0.0
Micro	61.3	27.7	11.0	98.0	2.0	0.0
Small	56.9	28.1	15.1	91.7	1.1	7.2
Medium	49.6	48.0	2.4	68.9	28.5	2.5
Large	56.9	35.5	7.5	78.3	18.3	3.3

127. The large majority of the companies in Grenada recognize the merit of formal training in skills upgrading and are not satisfied with the existing training facilities available to them. According to the enterprises, the Government should collaborate with the private sector to provide more training facilities in all areas, and that young people

should be allowed to go on day release or otherwise be exposed to world of businesses in order to be better prepared for work once they leave school. Meanwhile, despite the lion's share that private sector is taking in meeting Grenada's training need, some employers say that they are hesitant to train more as many workers leave after being trained. There is clearly a more important role for the Government to play in providing more and better training facilities in order to meet Grenada's skills upgrading needs.

Labor Relations

128. Most companies reported that their workers were not unionized (Table 4.4). Unionization ratios are much higher in large and medium sized firms, as well as foreign companies. However, only 3 companies reported days lost due to strikes or other forms of labor disputes last year. The relatively cordial relationship between labor and management is further confirmed by the trade unions. Indeed, the reliability of the workforce and the ease with which they can resolve labor related issues have been cited by foreign companies as an important reason for them to remain and expand their businesses on the island.

Table 4.4: Distribution of Firms by Unionization Ratio

	<10%	10-50%	50+%
Total	77.0	1.5	21.5
Manufacturing	79.5	2.3	18.2
Tourism	78.6	0.0	21.4
Domestic	80.6	1.9	17.4
Foreign	64.4	0.0	35.6
Micro	93.0	0.0	7.0
Small	89.1	3.6	7.3
Medium	66.7	2.4	31.0
Large	34.4	0.0	65.6

129. Despite the generally cordial relationship between labor and management, however, the trade union movement does not feel that it is as involved as is necessary in the development of policies geared to improving the competitiveness of Grenadian enterprises and the welfare of Grenadian citizens. Examples throughout the region have suggested that close consultation between key social partners is essential to enhanced competitiveness and sustainable growth, particularly in the context of the relative inflexibility associated with the fixed exchange regimes that are popular in the Eastern Caribbean, and have generally served the region well.

B. Innovation

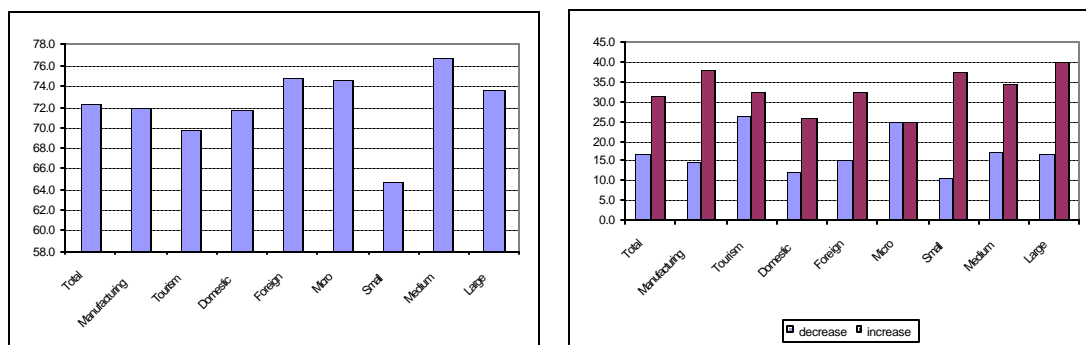
130. Growth and continued productivity improvement cannot be achieved without efficient use of resources and technological upgrading. Given its small market size, Grenada has no choice but to aim for attracting efficiency-seeking investment. How efficient and innovative its existing firms are reflect how conducive its investment climate is towards this type of companies.

Capacity Utilization

131. An important indicator of a firm's productivity and efficiency is the extent of its capacity utilization. Under-utilized capacity over a prolonged period indicates that the underlying business environment is constraining the firm from reaching its potential. It is, therefore, an alarming sign that warrants further in-depth investigation.

132. In Grenada, capacity utilization rates vary significantly between firms. While some firms (20 percent) are running at full capacity, others have left idle as much as 90 percent of their productive capacity (Figure 4.4). Overall, however, the capacity of Grenada's private sector is well utilized. The major exception are small companies, of which 94 percent are domestic establishments and two thirds are in the manufacturing and tourism industries. This suggests that the small firms in Grenada, especially those in food processing, garment and textile, as well as non-hotel tourism industries are less efficient producers than the rest of the private sector.

Figure 4.4: Average Capacity Utilization and Changes



133. For half of the companies, little change has taken place in how their productive resources are utilized over the last couple of years. Such stagnation in productivity and resource use is the more noticeable among domestic firms than their foreign counterparts. Among the other half, the majority (31 percent of total firms) experienced an increase in their capacity utilization, while the rest (17 percent) saw a rising proportion of their assets put aside unused. It is interesting to note that although small firms as a group still exhibit the lowest level of capacity utilization in Grenada, more of them than many other categories of firms have made progress towards improving their resource utilization efficiency over the last two years.

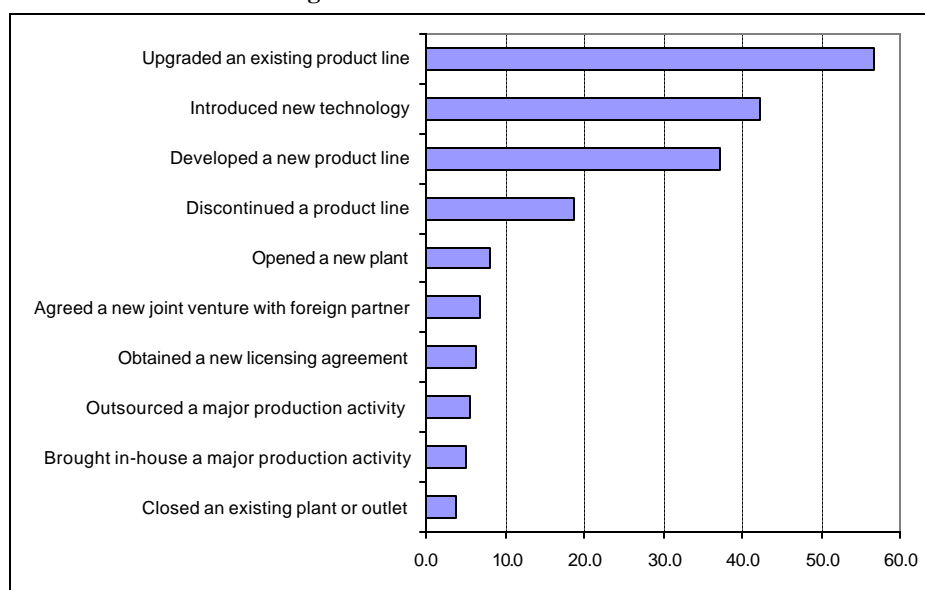
Innovative Initiatives

134. Traditionally, attention tended to be focused on formal R&D activities and technological inventions. But recent research has shown that modern technologies, including advanced managerial and organizational structures, can be adopted through many less formal channels. Indeed, the most relevant innovations take place in the process of doing business.

135. In Grenada, nearly 60 percent of the firms reported re-investing in their establishments for product and technology upgrading during the last 12 months. The median amount of investment as a percentage of net profit is a staggering 78 percent. Indeed, close to a quarter of the firms (47) reported that they reinvested 100 percent of their profits in the companies for better product quality and higher growth.

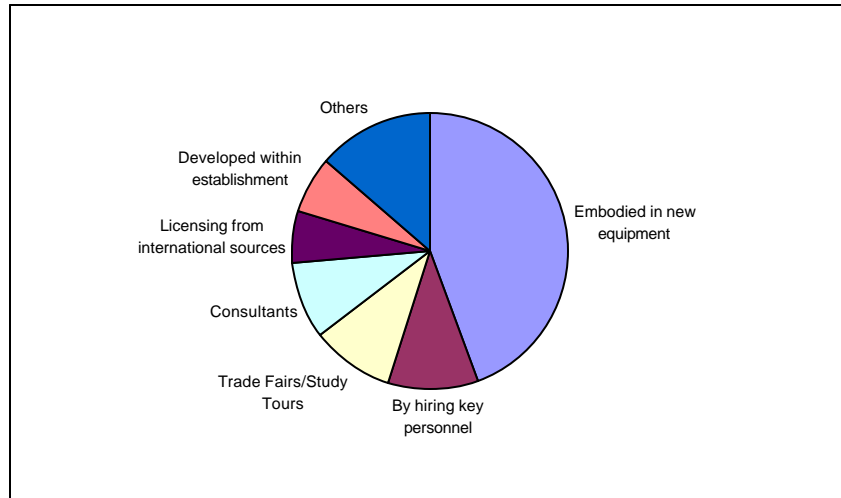
136. As a result, a significant proportion of Grenadian firms (more than 60 percent) have taken some initiatives over the last three years in order to improve productivity and meet the changing demands of the market (Figure 4.5). By far, the most predominant initiative is the upgrading of an existing product line. More than 55 percent of the firms have done so. In addition, a significant number of firms reported having introduced a new technology that changed the way their main product was produced or having developed a new product line. Innovative activity was especially strong in food-processing, financial services, information and communications, and tourism-related businesses. Meanwhile, adjusting to the market demand and internal efficiency rationalization, several companies (30) dropped a product line during this time.

Figure 4.5: Innovation Initiatives



137. To acquire new technological innovations, Grenadian firms rely mostly on the adoption of advanced technologies through new machinery and equipment (Figure 4.6). This is a particularly useful way for SMEs to upgrade their technological capacity. Manufacturing companies also rely on this to a greater extent than the firms in other industries. Other important ways for acquiring new technology include hiring skilled personnel, attending trade fairs and study tours, as well as using specialized consultants. For large foreign firms, the importance of licensing or turnkey operations from international sources and technological transfer from parent company rival that of new machinery for introducing new technologies.

Figure 4.6: Technological Innovation



138. By contrast, actual expenditure on R&D is very limited. Only 8 companies indicated that they had spent money on R&D activities in 2003 (three in tourism, two in manufacturing, one in telecommunications and one in construction). The total amount was a modest EC\$ 1.4 million.

139. Clearly, customers are the most important driving force behind the private sector's innovative initiatives for reducing production costs and developing new products and services. Competition from domestic and foreign competitors provide another push for firms to innovate and improve. Indeed, for domestic and micro firms, local competition is *the* most important force behind taking cost reduction measures and improving product and service qualities. For manufacturing companies, on the other hand, foreign competitors impose the main influence on reducing production costs.

CHAPTER V

INSTITUTIONAL ARRANGEMENTS FOR PROMOTING INVESTMENT: GIDC

Senior Governmental Involvement in Investment Promotion

140. An important element of the investment climate of a country is represented in the institutional arrangements that have been put in place for promoting investment. In Grenada, these institutional arrangements are represented largely through the operations of the Grenada Industrial Development Corporation (GIDC), although the most senior levels of government also play a role in promoting investment.

141. At the most senior level, the Government has recently established an Inter-ministerial Investment Management Committee, which is comprised of senior level technocrats. This Committee has been conceived in response to the need to provide a mechanism through which investors can have access to top ministerial officials in a structured manner, while taking away the pressure for the Prime Minister to have to meet with all potential investors. This Committee will be responsible for interfacing with investors.

142. Since the Committee has only recently been established, it is not possible to evaluate the effectiveness of its operation. However, the concept of an inter-ministerial committee with the responsibility of promotion and management of investment is a useful one. Another recent institutional consideration to create a Ministry of Private Sector Development, which would be the ministerial reporting relationship for the GIDC, is also a useful concept. It follows the pattern in many countries in which the promotion organization reports to a ministry of industry & commerce.

143. In considering the structure and reporting relations of the GIDC, international experience suggests that the level of autonomy, financing and staffing of a national Investment Promotion Agency (IPA) is more important to its success than its reporting link. In several countries, national IPAs have been given reporting links to the Prime Minister or President's Office in an effort to give these organizations more political clout. If this political clout is translated into financial resources and flexibility in staffing the organization with individuals with appropriate skill sets, then it can be quite effective. Otherwise, simply placing the organization under the office of the head of state is unlikely to change its operational effectiveness.

144. Of course, the movement to an inter-ministerial structure for the management of investment does not mean that for certain particularly important investment projects the Prime Minister may not have to be personally involved. The Government of Grenada has been described as a "pro-business" government by existing investors, and a key feature of such governments is the willingness of the most senior government official to become involved in the promotion of investment where this becomes necessary. The well-known

case of Intel's investment in Costa Rica is but one of the better-known examples of national leadership in the investment promotion effort.

145. Another example of senior levels of governmental involvement in the promotion of investment revolves around the process of incentive administration and oversight of the GIDC. In these cases, however, senior levels of government are too involved. The current system, for example, has in practice meant that incentives for every investment in Grenada are approved at the cabinet level. This is an unusually senior level approach to the administration of investment incentives.

146. Two other models tend to be employed by most countries. One model is that incentives are approved by the investment promotion organization. The other is that they are approved at the ministerial level, typically the Ministry of Finance, usually on the recommendation of the investment promotion organization.

147. Two of Grenada's principal forms of incentive legislation, the Hotels Aid Act and the Fiscal Incentives Act, indicate that approval authority for incentives resides at the Ministerial level. Even though the Hotels Aid Act introduces a role for Cabinet in its 1954 Hotel Aid Regulations, it is an optional role and does not translate to a legal requirement for Cabinet approval. At a minimum, Grenada could improve the efficiency of its incentive administration process and reduce the delay for incentive decisions by enforcing the existing legislation that requires ministerial, and not cabinet, approval of investment incentives.

Oversight of the GIDC

148. At the same time, there are legal changes that are necessary to allow for a more streamlined investment promotion process. Currently, for example, the GIDC is neutered, at certain levels, by the limitations of its legal approval authority. The GIDC was created with the enactment of the 1985 Industrial Development Corporation Act. This Act follows the model of investment promotion legislation in other countries, although unusually, for a legislation created as recently as 1985, it opted for an anachronistic title for its investment promotion organization. By 1985, for example, it should have been clear that the promotion of investment in Grenada would embrace services and agriculture, in addition to industry.

149. The Industrial Development Corporation Act also followed the practice in vogue in creating a board at the creation of investment promotion organizations. This board would involve individuals from the broader society who, as specified in the Grenadian legislation, have qualifications or experience in matters relating to industry, commerce, finance, accountancy, banking, economics, science, law, administration, agriculture or tourism. But then, having stipulated the appointment of what would probably be a high-powered board, the legislation neuters the board by specifying that all approvals of personnel within the organization must have the prior written approval of the Minister, except for individuals who earn a salary of less than EC\$6,000 per annum, of whom in 2004 there would be very few.

150. The Government of Grenada needs to revisit the legislation to grant greater approval authority to the board of its investment promotion organization. In so doing, although the GIDC has not taken its name seriously and has sought to promote investment in all sectors of the Grenadian economy, a change of name to create a greater level of consonance between law and reality may also be useful.

The Function of GIDC as an Investment Promotion Agency

151. The reality is that the GIDC is not only involved in promoting investment across all sectors of the economy, but that it is perceived by the business community as performing an effective facilitatory role. While it has been effective in facilitating investment and in working with existing investors, which, after all, are the most likely candidates for new investment, GIDC is hampered in executing a more effective campaign of promoting additional investment from foreign or domestic sources.

152. There are four critical functions involved in effective investment promotion: image building, investment generation, investment service and investment policy advocacy. The GIDC has focused most of its efforts on the latter two functions. The internal structure of the GIDC comprises three divisions: investment promotion, industrial estates and accounts and administration. The investment promotion division focuses primarily on investment service, as does the industrial estates division. The management of the GIDC spends considerable attention on issues of investment policy advocacy. The organisation's investment service function is particularly noteworthy. This is linked to the fact that within the GIDC's industrial estates division it manages two industrial estates, which provide office and factory space for investors. The GIDC receives, from the investment community in Grenada, compliments for its role as a supportive landlord and an effective investment facilitator.

153. The GIDC is seeking to make its role as an investment facilitator and promoter even more effective with a movement to a "one-stop-shop" for investment, in which all approvals and permits required by investors can be obtained at, or through, the GIDC. The current models for the institutional transformation of GIDC focus on two sets of design issues: one is transferring the legal authority for the approval of incentives to the GIDC, the other is ensuring that GIDC becomes a one-stop-shop by having the capacity to approve other ancillary permits or approvals needed by investors.

154. This report has already expressed concern at the fact that currently incentive approval is implemented at the level of cabinet. It is certainly more appropriate for incentives to be approved at lower levels of government. This could be done through an empowered investment promotion agency, as is the case in some countries. It is also appropriate to point out, however, that in many countries, ministries of finance, with responsibility for the country's financial operations, regard that they should have an approval role in relation to incentives. This report argues that what is more important than whether the investment promotion organization or the Ministry of Finance is the approval authority is the level of transparency and predictability in the incentive system.

If there is sufficient predictability, transparency and automaticity in the incentive administration process, the precise nature of the approval authority becomes a less contentious issue. This is the direction in which Grenada should focus its efforts through its Fiscal Incentive Review Committee.

155. At the level of ancillary approvals, efforts to mandate that the promotion organization control these approval processes has not met with success in countries that have tried to move in this direction. Critical agencies of government, such as immigration, environmental control and physical planning and others, have been unwilling to give up their legal authority in their substantive areas of control. Institutional efforts to bypass these agencies by trying to consolidate all approval authorities in investment promotion agencies have led to the “one-more-stop-shop” criticisms.

156. The efforts to transform GIDC into a one-stop shop should concentrate on making the organization a highly professional, well staffed, well managed, and adequately-funded promotional organization with reasonable powers of approval and with links to the senior levels of the governmental apparatus. In this environment, the GIDC, with its successful recent history of operations, will be in a position to function effectively in the areas of service and broader areas of promotion.

157. The biggest gaps in relation to GIDC’s operations are in the areas of image building and investment generation. But these promotional functions require financial resources that have traditionally been unavailable to the organization. At present, the GIDC is particularly constrained in assuming these functions by its limited promotional budget. The current budget, which has remained the same for some time, is EC\$200,000. A budget of this magnitude severely limits the extent to which the organization can function in an effective promotional capacity.

158. Compounding the budget constraint is the absence of an institutional presence in overseas markets. This is a problem that has affected the entire OECS region because of the small size of the countries. Recognizing this problem, the countries, assisted by bilateral aid sources, did for several years implement an Eastern Caribbean Investment Promotion Service (ECIPs). The ECIPs was geared to building the investment image of the region and targeting prospective investors, who could then be funnelled to the national promotion agencies of the region. The GIDC has used the ECIPs service in the past, but that entity closed its operations several years ago due to funding problems.

159. Currently, the GIDC uses Grenada’s consulate facilities in North America and Europe and honorary consuls in other locations to assist it in investment generating activity. It should be noted, however, that international experience with investment promotion has suggested that consulate operations have to be managed extremely carefully in order for them to serve as effective institutional vehicles for the generation of investment. Few countries have been able to make effective use of their consulates in this capacity.

160. Grenada needs to examine the models of overseas representation for investment activity very carefully. If consulates are to be the model of institutional choice, and they certainly represent the least cost approach, appropriate incentive systems and training need to be part of this institutional model.

161. On the other hand, a dedicated international presence also has to be managed carefully in relation to cost and effectiveness. But there are examples of success in this regard, in the context of countries similar in size and structure to Grenada. In the 1980s, for example, St. Lucia had dedicated promotional representation in the North American market that had an impact on the attraction of investment, in the electronics sector in particular, to that country. The overseas representation was very lean, however, and involved principally one professional.

162. The St. Lucian model suggests that the size of the overseas representation is less important than the professionalism of staff members and the incentives and reporting systems that operate within the organization. This is the general lesson from the international experience of effective investment promotion in all of its components.

APPENDIX

Distribution of Firms by Size and Sector

	Micro	Small	Medium	Large	Total	Domestic	Foreign
	<10	10-24	25-74	75+			
<i>Total</i>	<i>71</i>	<i>55</i>	<i>43</i>	<i>32</i>	<i>201</i>	<i>156</i>	<i>45</i>
Agriculture	2	2	0	1	5	5	0
Food processing	7	7	6	2	22	19	3
Garment & textile	2	3	1	0	6	6	0
Other manufacturing	6	4	4	2	16	15	1
Retail trade	9	3	7	3	22	17	5
Wholesale trade	4	2	3	2	11	8	3
Financial services	5	3	4	2	14	6	8
Information & Comm.	2	3	0	3	8	5	3
Construction	3	5	1	5	14	10	4
Hotels and restaurants	3	3	8	5	19	12	7
Other tourism related	21	10	4	2	37	29	8
Other	7	10	5	5	27	24	3
Manufacturing	15	14	11	4	44	40	4
Tourism	24	13	12	7	56	41	15
Foreign	15	7	8	15	45	-	-