

Trade and Financial Services in the Caribbean

Trade in Financial Services plays an increasingly important role in Caribbean economies and offers a window of opportunity for further diversification and growth in the region. The Caribbean has continued to shift from emphasis on primary commodity exports towards the services sector, mainly through tourism, but also notably through financial services.

Currently, many countries in the Caribbean are successfully undergoing this transition process, anchoring this success through trade in financial services activities. In this regard, one remarkable characteristic of trade in financial services in the region is that market access conditions in most Caribbean countries are considerably more liberal than those specified commitments made under trade agreement signed by these countries. This openness has resulted from privatization and unilateral liberalization processes undertaken by Caribbean countries to achieve more efficiency in the financial services sector and to spur greater diversification of their economies.

GATS

A few international commitments with respect to financial services have been undertaken at the multilateral level (GATS), and very limited participation has taken place in the context of the extended WTO Negotiations on Financial Services (Fifth Protocol).¹

CSME

More advanced level of services commitments have been agreed in the context of the CARICOM Single Market and Economy (CSME),² which removes restrictions on the right of establishment, the provision of services, and the movement of capital, setting forth the core principle of national treatment, among others.

CARICOM-DR

Financial Services trade is also covered under the Trade on Services Annex of the Dominican Republic – CARICOM free trade agreement which establishes the principle of national treatment between the parties. The two partners will negotiate their commitments on services in the coming year.

CARIFORUM-EC

CARICOM countries and the Dominican Republic (CARIFORUM) recently concluded negotiations with the European Communities of an economic partnership agreement (EPA) which includes provisions for the liberalization of investment, cross-border trade in services (including financial services). The agreement is expected to be signed on July 1, 2008.

¹ Only Dominican Republic is in the process of ratifying the Fifth Protocol and Jamaica has not yet accepted it.

² The Caribbean Single Market entered into force on January 30, 2006.

The EU has committed to opening more than 90 percent of its services sectors. These range from Business services, Communications, Construction, Distribution, Environmental, Financial, Transport, Tourism and Recreation services. The commitments will start when the EPA enters into force for all EU states except the new members, (Eastern and Central European states) whose commitments will start in 2011, and Bulgaria and Romania in 2014. In the case of investment (Mode 3) the EC has liberalized almost all sectors for CARIFORUM firms in the European Union with only some exclusions in a few sectors and limitations in mainly the new EU member states. In other modes of supply there has been great progress as well. In Mode 1 (cross border trade) the EC has liberalized the vast majority of sectors. The same applies to Mode 2 (consumption abroad).

In terms of the level of liberalization by CARIFORUM countries compared to the EC, there is clear asymmetry. The EC opened more than 90 percent of service sectors. As mentioned above. In the case of CARICOM, the sectoral coverage is between 65 and 75 percent, whereas the Dominican Republic's market opening in services is more than 90 percent. The sectors that were liberalized by CARIFORUM states include those that have positive development impacts and in which Member States are seeking investment or new technologies as well as sectors that are important to create economic opportunities in outsourcing contracts from European firms. To a large extent, most countries liberalized cross-border trade and investment. However, there is quite limited temporary entry (Mode 4) coverage for contractual service suppliers and independent professionals. The main sectors that most CARIFORUM states have liberalized in the EPA are: Business services (accounting, architecture, engineering, etc); computer and related; research and development; environmental services; management consultancy; maritime transport; entertainment; tourism; among others. Some of the commitments will be phased-in over time in some member states to address sensitivities at the national level. The services that CARIFORUM have opened should lead to increased investment in the region in order to develop new service industries. As well, market entry can result in greater efficiencies in a range of services that are inputs to manufacturing and other services. It is expected that there will be increased trade in the short term in business services if regional firms position themselves to take advantage of outsourcing opportunities from European firms.

CARICOM-Canada Trade Agreement

In January 2001, at their meeting in Jamaica, then Prime Minister Jean Chrétien and CARICOM Heads of Government agreed to begin discussions on the scope of a new reciprocal trade agreement. In July 2007, during a trip to Barbados, Prime Minister Stephen Harper of Canada and CARICOM Chairman, then Prime Minister of Barbados, Owen Arthur, announced the re-launch of trade negotiations.

The issue of trade and investment in financial services will be at the forefront of the Canada-CARICOM negotiations. Canada is an important source of foreign direct investment (FDI) for CARICOM. In fact, the bulk of Canadian investment is in the financial services sector. Canadian investment in Caribbean economies recently increased significantly. Barbados, which has a double taxation treaty with Canada, attracts the largest share (CDN\$38.4 billion in 2006) of Canadian FDI in the region.

Financial Services as a Main Contributor to GDP

Many countries in the region experience the growth of trade in financial services as one of the main contributors to GDP, which is helping them to face the challenges of overcoming vulnerability as well as providing them with a means of diversification that is increasingly needed in the current international trade environment (erosion of preferences, high extra-regional competition in tourism, etc):³

OECS Members have service-oriented economies where financial services constitute the second most important economic activity after tourism, representing 11% of GDP in 2005. All OECS Members operate both domestic and offshore financial services. Domestic banks are regulated by the Eastern Caribbean Central Bank (ECCB) and full foreign ownership is permitted in insurance and banking services. There are no residency or citizenship requirements applied to bank managers or directors; exchange controls have been removed, and none of the OECS Members have legislation that prevents borrowing or placing deposits with banks located abroad. All OECS Members have offshore banking and insurance legislation and offshore companies benefit from various tax exemptions (e.g. corporate tax and stamp duty)⁴. The ECCB operates a regional market for government securities of the Eastern Caribbean Currency Union (ECCU) member states. The Regional Governments Securities Market (RGSM), established in November 2002 and regulated by the Eastern Caribbean Securities Regulatory Commission (ECSRC), currently issues two types of securities with varying maturities: treasury bills and bonds.

Similar to OECS countries Barbados is, in practice, generally open to trade and foreign investment in financial services. Financial services constitute the second source of exports of services for Barbados. Exports of financial services reached US\$64 million in 2000; this included financial services supplied by international companies. Imports of financial services consist mostly of insurance services. The enactment of the International Business Companies Act in 1965, together with subsequent legislation, created a liberal environment in which foreign companies and professionals were encouraged to invest and establish a commercial presence in Barbados. This framework was completed by tax and bilateral investment treaties designed to ensure minimal taxation of these companies and individuals. The offshore subsector is well developed and provides management services of foreign funds for foreign persons; both residents and non-residents may incorporate an offshore bank. The Central Bank of Barbados is responsible for the regulatory and prudential oversight of both the domestic and the offshore banking sector. In a similar way to banking services, insurance services in Barbados comprise the

³ Country-specific information is based on the WTO Trade Policies Reviews, Reports of the Secretariat: OECS (WT/TPR/S/190, 1 October 2007), Barbados (WT/TPR/S/101, 10 June 2002), Belize (WT/TPR/S/134, 14 June 2004), Dominican Republic (WT/TPR/S/105, 9 September 2002), Guyana (WT/TPR/S/122, 1 October 2003), Haiti (WT/TPR/S/99/Rev.1, 7 October 2003), Jamaica (WT/TPR/S/139/Rev.1, 9 March 2005), Suriname (WT/TPR/S/135, 14 June 2004), and Trinidad and Tobago (WT/TPR/S/151/Rev.1, 12 October 2005).

⁴ There has been considerable regulatory, oversight and legislative reform in all OECS Members following on from the G7 Financial Action Task Force's report on the state of money laundering in various offshore centres. As a result, all Caribbean countries have been removed from the list of non-cooperative jurisdictions designated by the Financial Action Task Force.

international and domestic subsectors. The Securities Commission is the regulatory authority for the entire Barbadian capital market, including the mutual funds industry.

Foreign service providers play an important role in Belize's financial sector and receive national treatment. The international (offshore) subsector has successfully developed in the country and enjoys several tax exemptions. The Central Bank of Belize makes and enforces all regulations for the banking sector and the insurance sector also has its own supervisory agency.

The services sector constitutes the main pillar of the Dominican Republic's economy both in terms of value added and of employment, accounting for 55% of GDP in 2000. The contribution of the financial services subsector to Dominican GDP was 4% in 2001. The total assets of the Dominican financial sector amount to RD\$218 billion, equivalent to 62.4% of the Dominican Republic's 2001 GDP. The banking sector is monitored by the Superintendency of Banks in accordance with the Banking Law (Law No. 708) of 14 April 1964. The Foreign Investment Law of 1995 eliminated virtually all exemptions to market access and national treatment. Foreign banks may establish subsidiaries or branch offices in the Dominican Republic. In order to promote and regulate the trade of equities in the Dominican Republic, a Stock Market Law (Law No. 19-00) was adopted on 18 April 2000 which established the Superintendency of the Stock Market as an autonomous public organization. Similarly, the insurance sector is regulated by the Superintendency of Insurance.

Financial services in Guyana are generally open to foreign investors as witnessed by the relatively large number of foreign banks operating in the country. Financial services is one of the main subsector contributing to GDP accounting for 3.6% of GDP in 2001. The Bank of Guyana has statutory responsibility for authorizing and supervising all licensed financial institutions in Guyana. The Commissioner of Insurance supervises the insurance industry. A stock exchange was established on 30 June 2003, under the supervision of the Guyana Securities Council. The Securities Industry Act (1998) regulates the activities of the securities market.

The services sector in Haiti accounts for 64% of real GDP in 2002. In recent years, foreigners have mainly invested in the supply of banking services. Foreign banks are subject to the same regulations as national banks.

The services sector in Jamaica accounted for some 71.9% of GDP in 2003 and employed around three quarters of the labour force. The financial services subsector accounted for 8.5% of GDP in 2003. The regulatory framework of Jamaica has been strengthened with the establishment of the Financial Services Commission and increased monitoring and supervision by the Bank of Jamaica. There are no restrictions to private foreign ownership of banks, and the banking, life, non-life insurance sectors benefit from national treatment. Sector-specific legislation applies to banking, insurance and securities trading.

Services is the largest sector of Suriname's economy both in terms of employment and contribution to GDP, accounting for half of its GDP. In 2001, financial services overtook trade in goods, restaurants and hotels as the single most important service activity in the country and represented 8.5% of Suriname's 2002 GDP. During the period 1990-2000, Suriname received US\$770 million in FDI of which financial services accounted for 3.2%. The Central Bank is the entity responsible for regulating and supervising the Surinamese financial system. There are no legal restrictions concerning the number of nationally owned or foreign credit institutions, including banks, and insurance companies which can operate in Suriname. Suriname does not apply restrictions on the number of banks and there are no legal ceilings concerning the participation of foreign equity in new or existing credit institutions, including banks and insurance companies.

Trinidad and Tobago's recent liberalization and reform efforts have had the greatest impact on financial services, becoming one of the main activities in the services sector. The services sector accounted for 60% of GDP and three quarters of total employment in 2004. Financial services constituted the second most important services activity in this context. Liberalization in the financial services sector, triggered by the removal of exchange rate controls in the early 1990s, was accompanied by enhanced regulation and supervision. There are currently three different regulatory authorities for the financial system: the Financial Institutions Supervision Department of the Central Bank, the Commissioner of Co-operative Societies, and the Securities and Exchange Commission.

The Bahamas has applied for Membership of the World Trade Organization (WTO), where it currently enjoys Observer status, and has started negotiations on its accession. The Bahamas is an active member of CARICOM and has a strong offshore financial services sector which contributes an estimated 7% to GDP in 2007.

The successful development of the financial services sector in the Caribbean and the continuous efforts made by the Caribbean countries to improve its performance have made the region emerge as one of the leading destinations for the offshore financial services niche and for outsourcing business processes from banking and financial firms based in developed countries, taking advantage of the expertise that has already been acquired in financial services and therefore, and as a logical extension of the industry.

Caribbean⁵ offshore financial centers account for 49% of all bank claims in offshore centers according to the Bank for International Settlements, making it a US\$2 trillion industry for the region. The primary market for Caribbean offshore financial services is North America, with 80% of credit going to the Western Hemisphere.⁶

Cayman Islands, British Virgin Islands, Turks and Caicos, Barbados, the Bahamas, OECS countries and Belize have been the main offshore financial services success stories in the Caribbean. The offshore financial services industry in the Bahamas employs over

⁵ The Bank for International Settlements defines the Caribbean Offshore Financial Centers as the Bahamas, Bermuda, Cayman Islands, the Netherlands Antilles, and Panama in their report.

⁶ Von Peter, Goetz, Stever, and Upper. "Highlights of International Banking and Financial Market Activity." Bank for International Settlements Quarterly Review. June 2007.

4,000 people, about 3% of the labor force and earnings from offshore companies spending in the domestic economy totaled US\$134 million in 2004.⁷ The success of offshore financial services in the Bahamas and Barbados has come after years of fostering the development of the industry, in which reputation is especially important. The scope of offshoring jobs has broadened in the region to include transaction processing, finance, human resources, and investment banking analytics.

Local and regional financial sectors are also opportunities to foster trade and investment ties with the Caribbean, along with the growing outsourcing industry which provides services to firms in developed countries mostly located in the US and Europe.

Countries in the Caribbean are committed to continue developing the financial services industry through favorable regulatory environment as well as investing in innovation and local expertise in order to increase competitiveness and growth.

Remittances and Financial Services

The transmission of remittances from the Caribbean diaspora is one important area where the role of institutionalized and effective financial services mechanisms of the type developed in the Caribbean is mostly needed. This is particularly relevant taking into consideration the high volume of remittances from Caribbean immigrants back to their home countries, and their increasing impact in the region's development. Worker remittances now total almost 20% of regional GDP in the Caribbean.⁸ Currently, the transmission of remittances is primarily carried out by money transfer operators outside the financial services system which apply high prices for the provision of the service. Improving access to formal financial intermediation for the transmission of remittances is necessary to reduce costs and to extend the benefits of the formal banking system to its users, transforming remittance recipient clients into bank clients, and increasing as a result savings, access to credit and investment in the region with positive impact in its financial services sector growth. In this regard, cooperation with the United States could prove crucial for the facilitation of local Caribbean banks branches operations in the US with respect to remittances. Under current US regulations foreign bank branches, which may be federally or state-licensed can only accept deposits of any size from foreigners, but they may accept deposits only in excess of \$100,000 (wholesale deposits) from US citizens and residents. A foreign bank seeking to accept retail deposits (initial deposits under \$100,000) may do so only by establishing a US subsidiary bank which process of establishment is generally more costly.

The Jamaica National Building Society (JNBS) presents a successful case in the incorporation of remittances transmission users into the formal banking system. The JNBS through its subsidiary JN Money Services Ltd. (JNMS) which serves Jamaicans living in the diaspora by facilitating remittance services in Canada, the US and the UK, implemented a process of sending and receiving money transfers by using swipe card technology. As a result, it now has over 70,000 cards users and 50% of remittance

⁷ Economist Intelligence Unit. Bahamas. Country Profile 2007

⁸ Sahay, Robinson, and Cashin. The Caribbean: From Vulnerability to Sustained Growth. International Monetary Fund. 2006.

recipients have been brought into the formal banking system, with 25% of those receiving their remittances through a card product which is then used to make purchases at small businesses that accept debit card purchases. The majority of the bank's small business clients also benefit from making remittance payouts through increased access to both credit and remittance receiving customers. Rates of saving have increased considerably, not only through direct deposits to savings accounts, but also by reducing the amount of cash in circulation and through the increased use of electronic transactions.⁹ International business opportunities in area of financial services offer a wide scope for fostering trade between US-based firms and the Caribbean, and in particular for enhancing working and commercial relationship between South Carolina and the Caribbean nations.

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⁹ Orozco, Manuel. *The Role of Remittances in Leveraging Sustainable Development in Latin America and the Caribbean*. Inter-American Dialogue, March 6, 2007. Testimony presented before the Subcommittee on Domestic and International Monetary Policy, Trade and Technology at the hearing entitled, "The Role of Remittances in Leveraging Sustainable Development in Latin America and the Caribbean". March 7, 2007.