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THE U.S. MESSAGE FOR JAMAICA'S SEAGA: IT'S TIME TO KEEP YOUR PROMISE

INTRODUCTION

Jamaican Prime Minister Edward Seaga visits Washington, D.C., this week. His arrival should trigger in the Reagan Administration a reappraisal of Jamaica's strategic role in U.S. Caribbean policy. The island's seeming potential and its special relationship with the Reagan Administration prompted Ronald Reagan in 1982 to state: "Jamaica is making freedom work."[1] There then was solid reason to be optimistic about Jamaica's future. There is less today, and the culprit is Seaga. He has not kept his promises to mobilize and unleash free market forces to resuscitate his nation's economy.

Seaga's Jamaica Labour Party (JLP) swept to electoral victory on October 30, 1980, with a mandate for change as great as that won by Reagan less than a week later. On becoming Jamaica's new Prime Minister, Seaga promised an ambitious program to reverse eight years of socialism that virtually had destroyed the island's economy. To do so, he promised to pursue a free market strategy. To show his strong pro-Western stance on foreign policy, Seaga broke relations with Cuba and downgraded ties with other Soviet bloc nations.

Today, Jamaica's great promise remains unfulfilled. To be sure, declines in world prices for bauxite and alumina, principal Jamaican commodities, have slowed the government's development programs, leading to heavy borrowing abroad and a $3.2 billion foreign debt.

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1. Speech by President Ronald Reagan to the Organization of American States, Washington, D.C., February 24, 1982.

Yet the main cause of today's economic woes is that Seaga's government has failed to create a fertile investment climate for foreign and local businessmen. The sad truth is that state control of Jamaica's economy has actually increased in some sectors since the JLP assumed power.

Jamaica is too important to U.S. and Caribbean regional security to allow its potential to remain largely untapped. Unless Seaga can revitalize his nation's economy before the island's next elections (which could be called at any time, but must be held by the end of 1988), former Prime Minister Michael Manley and his socialist People's National Party (PNP) could return to power. This would be a blow to the validity of the free enterprise concept for the developing world and to U.S. efforts to stem Soviet and Cuban influence in the Caribbean.

As Seaga meets with top U.S. officials this week, they must make it clear that continuation of the nearly $1 billion in U.S. aid given to Jamaica since 1980 is contingent upon the rapid structural reforms that will ignite the power of free market forces for the country's 2.3 million inhabitants. The state must divest itself of all assets not essential to its functioning and phase out such pervasive monopoly/monopsony powers as virtual control of the tourism and bauxite industries and the right to be sole importer of such diverse goods as automobiles and fertilizers. Perhaps most important, the obstacles to foreign and domestic investment must be removed to stimulate growth and reduce Jamaica's crushing debt burden.

Jamaica and Edward Seaga still offer hope and promise for the model they can become in the developing world. And while some of this promise has tarnished in the past six years, the U.S. should remain ready to help Jamaica--but only if Seaga pursues those policies which allow Jamaica to help itself.

JAMAICA SINCE INDEPENDENCE

Jamaica's future looked bright following its independence from Great Britain in 1962. The third largest island in the Caribbean, with a total area of over 4,000 square miles, it was blessed with abundant natural resources, political stability, and an industrious people with a stunning 79 percent literacy rate. Ruled by the Jamaica Labour Party during its first ten years as an independent nation, Jamaica experienced strong economic growth, with real Gross Domestic Product averaging a 5.2 percent increase per annum. This was due primarily to domestic financial stability combined with private foreign direct investment in the bauxite/alumina and tourism industries.

Jamaica's economic situation changed dramatically after Michael Manley's People's National Party won the 1972 elections. Manley's two-term, 8-year administration transformed Jamaica into a case study of the failures of socialism. Far-left policies crippled the island's key economic sectors--agriculture, tourism, and mining. Example: a government scheme for turning private plantations into cooperatives sharply reduced banana and sugar production. Tourism revenues dropped precipitously after the government erected obstacles to foreign investment in the industry. On top of this there were food shortages, a breakdown of essential services, and crime. Some hotels were taken over by the government after being abandoned by their owners.

With revenues declining from other sectors of the economy, Jamaica became increasingly dependent on bauxite/alumina production. Manley, however, forced foreign mining companies to sell a controlling interest in local operations to his government and proceeded to cripple production incentives even further by imposing a massive levy on exports. Predictably, net bauxite/alumina production plummeted, declining by a third, while major companies involved in Jamaica began looking for more hospitable mining conditions elsewhere. When the International Monetary Fund made new loans contingent on sounder fiscal policies, Manley broke with the IMF and turned to Libya and elsewhere for financial aid. These sources proved insufficient, leading to depletion of Jamaica's foreign exchange reserves.

Jamaica's middle class began fleeing the PNP's punitive socialist policies. The loss of managers, coupled with a lack of foreign exchange to buy spare parts and raw materials, forced dozens of factories and small businesses to close, boosting official unemployment to 36 percent overall, with underemployment and youth unemployment reaching more than 50 percent.

Jamaica's disastrous economic situation, coupled with widespread fear that Manley would lead the nation irrevocably into the Soviet-Cuban camp, prompted 87 percent of the voters to turn out in the 1980 elections. The PNP suffered a massive electoral defeat, retaining only 9 seats in the 60-seat Parliament. Promising to "facilitate the unfettered development of the country's private sector," and "restore Jamaica's economic development based on the principle of entrepreneurial initiative,"[2] Edward Seaga and the Jamaica Labour Party took control of the island's government.

THE JLP'S ECONOMIC POLICIES

After nearly six years of virtual total control of the Jamaican government's executive and legislative branches, the JLP has failed to

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2. Investing in Jamaica, Caribbean/Central American Action, March 1986, p. 2.

revive the economy. It is not a failure of the free market model, however, but a failure to try the free market model.

Though the JLP's pre-election manifesto promised "a set of policies to stimulate the private sector,"[3] it also called for national reconstruction that would include "a number of major public sector projects."[4] Overlooked at the time by observers who saw Seaga as a Caribbean Ronald Reagan, this statement was a clear indication that the state was to remain the dominant player in Jamaica's economy, regardless of the change of government.

Under Seaga, the state still owns 75 percent of the sugar industry, more than half of the tourism sector, all bauxite lands, the telephone company, the national railway, the national airline, the largest commercial bank, the only cement company, and the only oil refinery--purchased from ESSO in 1982. A review of Seaga's record in the four key economic sectors--agriculture, tourism, mining, and manufacturing/processing--illustrates the continuing dominance of the state:

Agriculture

Although the system of state-managed cooperatives largely has been abandoned, the government remains in firm control of Jamaica's agricultural sector. The state operates various marketing monopolies for agricultural products and largely determines the prices paid to farmers for their crops. In this area, Communist China, with its successful agricultural reforms, is probably more free market than Seaga's Jamaica.

The Jamaica Commodity Trading Corporation, established in 1981, has a monopoly right to import a broad range of basic commodities, including foodstuffs, fertilizers, and private motor vehicles. The government's policy of importing food and subsidizing its price proved to be a major disincentive for domestic agricultural production. Under strong U.S. pressure, the government agreed to reduce food subsidies gradually but, fearing political and social backlash, set up a vast food stamp program supported by U.S. aid. Food stamps, augmented by tons of American agricultural surplus provided under the U.S. PL 480 program, have damaged Jamaica's domestic agricultural market mechanism as severely as they have in dozens of other developing countries. States Carl Stone, Jamaica's foremost political scientist: "The existing Food Stamps Programme is mockery to any real commitment to local agriculture. Our poor people are being subsidized

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3. Jamaica Labour Party, Change Without Chaos, A National Programme for Reconstruction, October 1980, p. 12.

4. Ibid.

to buy imported food when our farmers can't sell their produce because of low levels of consumer buying power."[5]

Bananas and sugar cane, two of Jamaica's most important agricultural exports, continue to be handicapped by government controls and heavily politicized unions. Though Seaga complains about U.S. limits on sugar imports, the fact is that Jamaican sugar production has fallen so much that the island for several years has been unable to fulfill its quota of allowed sugar sales to the U.S. Banana production hit a 20-year low in 1984, achieving only 20 percent of the government's planned export target for the British market.

Instead of allowing the free market to find a solution to declining agricultural production, Seaga launched a vast new government project called AGRO-21 to develop one-sixth of Jamaican farmland. AGRO-21 is reminiscent of former Prime Minister Manley's socialist agricultural policy. The government, for instance, is to be a venture partner "to hold equity for the people," while the project's structure consists of "many agencies working together, coordinated by the AGRO-21 Secretariat."[6] Government land is leased to farmers. Seaga declared that "all such leases will be subject to agreement to develop the land on the basis of <u>an agreed farm plan</u> which ensures that the land is never used in a manner contrary to the planned national interest."[7]

<u>Tourism</u>

Seaga has revitalized Jamaican tourism by making Jamaica attractive to U.S. visitors and educating Jamaicans on tourism's importance to the nation's economy. The government still owns 60 percent of the hotel sector. Businessmen operating hotels leased from the state are eager to purchase resort properties, but complain that government refuses to sell. Instead of divesting itself of tourism assets, the government has actually bought more hotels and has sought to expand its holdings with the purchase of the Montego Bay Freeport and other properties. Tourism-related public enterprises such as Air Jamaica and National Hotels and Properties operate at a loss, adding to government indebtedness.

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5. Carl Stone, "Agricultural Policies," <u>The Daily Gleaner</u>, December 3, 1984, p. 8.

6. Prime Minister Edward Seaga's Budget Presentation 1984-85, p. 37.

7. Prime Minister Seaga's Budget Presentation 1985-86, p. 32 (emphasis in original).

Mining

From 1980 to 1985, Jamaican bauxite/alumina production was cut in half. As a result, foreign exchange earnings fell from $353.3 million (in U.S. dollars) to $125.1 million. The combined value of all Jamaica's exports has fallen 46.7 percent.

Falling world prices for bauxite/alumina should have prompted Seaga to look for ways to make Jamaican production of the commodity competitive. Yet Seaga reduced only slightly the oppressive levy on pre-export profits that had been imposed by the Socialists. This tax, on an accrual basis, equals nearly a fifth of total operating costs. Because of their continuing large losses, three of the five multinationals involved in mining and refining on the island ceased operations; another is considering closing.

Instead of encouraging bauxite/alumina production through generous tax incentives, the Jamaican government has moved in the direction of greater intervention by setting up its own company and leasing a closed-down plant from Alcoa. Even though there is now a world surplus of aluminum smelters, the Seaga administration is building a gigantic smelter in Colombia on a joint venture basis with the Colombian government.

Manufacturing/Processing

The government has been reluctant to relax its control over Jamaica's manufacturing and processing sector. This means that foreign investors and local businessmen remain at the mercy of an unresponsive bureaucracy. The Jamaican National Investment Promotion, Ltd. (JNIP), established by Seaga to assist foreign businesses in navigating their way past other government agencies, itself has become part of the bureaucratic problem. A JNIP director even has gone on record stating that "the private sector is incapable of taking on investment projects without the assistance of a government agency."[8] While there is a putative system of investment incentives for foreign businessmen, approval may take months and is highly arbitrary. Although not necessarily official policy, the cabinet-level committee responsible for approving investment favors capital-intensive import-substitution projects over labor-intensive export-oriented activities.

Jamaica's expected influx of foreign investors has never happened. And a large share of those who did establish enterprises on the island have now left, citing hopeless tangles of red tape, an

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8. Scott D. Tollefson, "Jamaica: The Limits of A Showcase Policy," SAIS Review, Summer/Fall 1985, p. 202.

unreliable infrastructure, union problems and high labor costs. The cost of running a 500-worker textile plant in Jamaica, for example, is three times the cost of doing so in Haiti, nearly double that in Costa Rica, and 42 percent higher than in Mexico, which offers the added incentive of its maquiladora free zone program and proximity to the U.S.[9] Despite these investment disincentives, and a persistent 25 percent unemployment rate, the Seaga government doubled the minimum wage in 1984.

Jamaican businessmen also are hampered by a heavy tax burden and the government's increased control over the credit market. Although the first phase of a tax reform program began this January as a flat 33 percent tax on all income over $8,580 Jamaican dollars (about 1,500 U.S. dollars), abolition of nearly all tax breaks coupled with a variety of payroll taxes for the National Housing Trust, pensions, and education bring the true total tax rate to roughly 40 percent. And though small businesses create many more new jobs than their large firms, the establishment of small enterprises has been slowed enormously by the imposition of a license fee for shopkeepers which is the equivalent of more than twice Jamaica's average per capita income.

Making matters worse for the economy, Seaga has extended state control over the credit markets. The result: a net transfer of resources from the private to the public sector. The Prime Minister's policy that foreign exchange earnings "...belong to the government to be used for the government and not for the greedy few,"[10] understandably exacerbates capital flight and contributes to the burgeoning underground economy. Credit controls imposed in 1985 in an attempt to placate the IMF prompted the U.S. Agency for International Development (AID) to state that Jamaican exports were being hurt by "the relatively stringent credit restrictions being employed to restrain demand."[11]

RELATIONS WITH THE U.S.

The coincidence of Edward Seaga's and Ronald Reagan's elections made Jamaica a natural centerpiece of the Reagan Administration's new activist policy toward the Caribbean. Marxist takeovers of Grenada and

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9. Clyde Farnsworth, "Haiti's Allure for U.S. Business," The New York Times, June 17, 1984, p. III-4.

10. 1984-85 Budget Presentation, p. 15.

11. U.S. AID, Program Assistance Approval Document for $34.5 million additional Economic Support Fund loan, June 1985, p. 4.

Nicaragua in the 1970s had awakened U.S. awareness of the region's strategic importance. Convinced that economic growth and political stability form the best bulwark against communist expansionism, the Reagan Administration crafted a policy designed "to make Jamaica an example of what could be accomplished when assistance was provided to a government that shared the U.S. belief that private sector growth could lead to economic development."[12]

Jamaica was to be the fulcrum of the Caribbean Basin Initiative (CBI), the Administration's ambitious program to invigorate sickly regional economies. The U.S. plan to resuscitate Jamaica was based on a combination of foreign direct investment, CBI-generated trade preferences, and greatly increased bilateral and multilateral assistance.

In January 1981 Seaga visited the White House as Reagan's first foreign guest. A U.S. Business Committee on Jamaica was launched to promote private investment on the island. Headed by then-Chase Manhattan Bank chairman David Rockefeller, the Committee was composed of 25 U.S. corporate chiefs.

Including the aid requested for Fiscal Year 1987, U.S. bilateral assistance to Jamaica since Seaga took office totals more than $1 billion, making Jamaica the globe's second highest per capita recipient of U.S. assistance after Israel. The Reagan Administration also used its influence to increase multilateral assistance for Jamaica. In 1981, for example, the World Bank gave $133.1 million to Jamaica (three times the previous year's amount), and the following year Jamaica became the largest per capita recipient of World Bank loans. In 1981 also, the IMF made a three-year pledge of $698 million (the maximum allowed under the IMF quota system) to Jamaica based on Seaga's promises to cut public spending, deregulate the import licensing system, eliminate rent ceilings, and phase out price controls on selected foods. And to help the island's depressed mining sector, the U.S. bought $67 million worth of Jamaican bauxite for the U.S. strategic stockpile.

Despite such U.S. generosity, the Jamaican government did not deliver on its stated commitment to the free market development which the assistance specifically was to fuel. American businesses introduced to Jamaica by David Rockefeller's (now-disbanded) committee encountered so many bureaucratic restrictions and other problems that only a handful remain involved on the island. Total U.S. investment since 1981 is only about $100 million. Ironically, one of Jamaica's

12. U.S. General Accounting Office, AID's Assistance to Jamaica, GAO/ID 83-45, April 19, 1983, p. 1.

few truly successful free market projects is the Kingston Free Zone, and it was initiated in 1976 by the Manley government.[13]

Although U.S. aid was to provide Seaga with a "cushion" to allow him to make major structural adjustments without undue political or social upheaval, this strategy may have done more harm than good. The PL 480[14] and government food stamp programs discouraged domestic food production, while the AID-funded government housing program, coupled with the reimposition of rent controls, has undercut private construction financing.

Although Seaga generally strongly supports U.S. regional policies, including the Grenada rescue mission and aid to the Nicaraguan Freedom Fighters, Jamaica's United Nations voting record belies this. In 1985, Jamaica voted against the U.S. 77.3 percent of the time, more than even the socialist government of Greece.[15]

JAMAICA'S FUTURE

Seaga's JLP suffered a serious setback in Jamaica's July 29 local elections. As a result, 11 of the island's 13 local government authorities now are controlled by the socialist PNP. Pressure is building on Seaga to call national elections before 1988, when his term expires. Although Seaga probably will be able to hang onto power until then, public opinion polls indicate that unless he ignites the economy, Michael Manley's PNP will return to power in Jamaica in the twilight months of the Reagan Administration.

A PNP government would probably oppose most of current U.S. Caribbean and Central American policy. Manley has vowed, for example, that he would restore ties to Cuba and would support the Sandinista regime in Nicaragua.

Although the PNP is chiefly a social democratic party, its powerful left wing is dominated by Marxists who maintain close ties with the island's official Communist Party, the Worker's Party of Jamaica (WPJ). Photographs of Fidel Castro and "Che" Guevara are still

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13. Tollefson, op. cit., p. 193.

14. PL 480 was set up for the purpose of creating overseas markets for U.S. agricultural products.

15. The Heritage Foundation, National Security Record No. 93, July 1986, p. 4.

taped to the walls of the PNP's party headquarters in Kingston, while members of Manley's party address one another as "comrade."[16] Travel and other contacts between PNP officials and the Soviet bloc continue regularly, while a delegation from the Communist Party of the Soviet Union has attended the PNP's annual convention during the past two years.[17] Because Jamaica is considered a Caribbean trendsetter, the restoration of socialism there could be the harbinger of political shifts elsewhere in the English-speaking Caribbean.

POLICY RECOMMENDATIONS

The large volume and variety of U.S. development assistance made available to Jamaica over the past six years was intended to facilitate the free market restructuring of the island's economy. This aid must be considered strategic as well as humanitarian, for a politically stable, capitalist, pro-Western Jamaica was to counter pro-Soviet forces in the region. U.S. assistance was made in good faith with the understanding that the Seaga government would undertake the major economic changes it promised.

The Jamaican government has reneged on many of its promised economic reforms and has acceded to others reluctantly only after diplomatically embarrassing pressure from U.S. government agencies and the IMF. Although Jamaica agreed to sell to private investors many of the government-owned enterprises in return for U.S. Economic Support Funds (ESF), only token privatization has occurred.[18] Concludes the U.S. General Accounting Office: "Jamaican resistance was strong" against policy reforms.[19] As such, the island's economy today is only marginally better than under the Manley regime, with 30 percent unemployment, a 25.5 percent inflation rate, and a per capita foreign debt higher than Mexico and Brazil.[20]

This week the Reagan Administration must be a tough host when it greets Seaga. He must be told that continuation of the high level of

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16. Joseph B. Treaster, "For Jamaicans, One-Party Rule Is a Party Too Few," The New York Times, August 15, 1984, p. 2A.

17. Statement by the Prime Minister on Matters Concerning National Security, 1st November, 1983. See also Pravda, September 29, 1985, p. 5.

18. U.S. AID/Jamaica's Monitoring of and Controls Over Dollar and Local Currency Resources Provided Under Economic Support Fund and PL-480 Title I Programs, August 12, 1985.

19. U.S. General Accounting Office, AID's Assistance to Jamaica, Enclosure I, p. 8.

20. Financial Times, August 7, 1986, p. 4

U.S. development assistance (which has averaged 30 percent of the island's GDP since 1981) depends on rapid and genuine progress in the structural reforms essential to a free market economy. Specifically, changes in Seaga's macroeconomic, trade, and structural policies should include:

1) A reduction in the overall public sector deficit by at least 3.5 percent of GDP in the initial year 1986-1987 and further reductions in subsequent years. This would raise domestic savings and permit the current account deficit in Jamaica's balance of payments to be reduced to sustainable levels. This is a prerequisite for encouraging the private initiative necessary for sustained growth.

2) A monetary policy that does not favor the public sector in the allocation and terms of credit. In particular, liquidity ratios must be abolished and the official floor on savings deposits eliminated to free assets for investment purposes. The current corporate tax structure must be modified to provide business incentives, including the elimination of stamp duties on stock transactions and double taxation of dividends. This would induce greater private sector growth.

3) Government exchange controls should be phased out gradually to allow the currently overvalued Jamaican dollar to fall to a market-determined rate.

4) Import controls must be removed, stamp duties eliminated, and tariffs lowered and restructured to allow a free exchange rate to stimulate exports and facilitate import protection.

5) Major reforms are needed in domestic tax laws and regulatory policies to remove their anti-export, anti-agricultural, and anti-tourism biases. To eliminate the bias against exports, a simple and effective exemption/rebate mechanism could be introduced that compensates exporters for tariffs and indirect taxes on inputs to exported products.

6) The Jamaica Commodity Trading Corporation must be phased out and all other public sector monopoly/monopsony powers eliminated to allow the private sector opportunities for competition at all levels.

7) All obstacles to private foreign direct investment must be removed, with true streamlining of investment procedures and regulations. Private capital inflows, particularly private direct investment and repatriation of capital held abroad, are necessary if Jamaica is to grow economically and not make its crushing debt servicing burden unsustainable. Capital will enter Jamaica only if investors can be assured that it can freely leave the island.

8) The government must sell its hotels, airlines, agricultural land, and other such non-essential assets to reduce its stifling

influence in key economic sectors. Proceeds from divestiture could be used to reduce the nation's foreign debt.

No amount of foreign aid can spur Jamaica's economic growth unless Seaga is prepared--at last--to lead his country along a free market development path. Without reforms, gross domestic product almost certainly will decline further and unemployment will rise, followed by Seaga's certain defeat in a national election.

CONCLUSION

Because Edward Seaga is identified so closely with the Reagan Administration, the failure of his economic revitalization program will be viewed internationally as a setback for U.S. developmental and regional security policies. This could damage the credibility of the free enterprise model which the U.S. seeks to introduce to the developing world and could unravel the Reagan Administration's carefully woven Caribbean strategy. The U.S. State Department and AID must recognize that many of Seaga's promises have been empty. The time has come this week for the U.S. to tell Seaga, as friend to friend, that the U.S. can not continue subsidizing Jamaica's disastrous economic policies. Jamaica can still realize its great economic and human potential if Seaga begins to carry out a genuine free market development strategy. The U.S. remains Seaga's willing partner, but the final responsibility for his country's future rests on his shoulders alone.

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