

Multi-year Expert Meeting on

# **TRADE, SERVICES AND DEVELOPMENT**

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## **SESSION 4:**

### **FINANCIAL SERVICES AND REGIONAL INTEGRATION**

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Role of regulatory and development  
cooperation in improving the  
efficiency and effective supply of  
financial services

# CARCOM SINGLE MARKET and ECONOMY - an RTA

- Signed in 1989 in Grand Anse
- Successor to Treaty of Chaguaramus in 1973
- And to CARIFTA ( the Caribbean Free Trade Area)
- 1989 marked a step toward a more integrated environment
- Early steps at free trade and a common external tariff had been reasonably successful

# Financial initiatives

- A development bank was established ( The Caribbean Development Bank)
- Meetings of Central Bank Governors which were already taking place on a regular basis , were renamed Council
- Multilateral payment systems setup (CMCF)
- CMCF was frozen in 1989 when debtors could no longer pay and creditors could no longer afford to provide credit
- Rights of establishment were agreed, including financial establishment.
- A Caribben Development Fund was established after several years. (Petroleum Development Fund)

# Financial Harmonization

- Harmonization of fiscal and monetary policy is a goal, but has been difficult to achieve because of issues of autonomy
- Establishment of a monetary Union for the entire CARICOM was also a goal which proved difficult to achieve, . However, the OECS already had a functioning Monetary Union
- Harmonization in services was also called for: in banking and securities and commercial arbitration and competition policy

# Harmonization goals

- Harmonization was achieved in competition policy
- A Caribbean Financial action Task force was formed to which issued guidelines on the probity of transactions in the international financial centres(IFCs) – Nevertheless the Stanford problem occurred.
- In the domestic commercial banking a Caribbean group of Regional Bank Supervisors was formed to harmonize commercial bank supervision in the region. This has contributed to stable banking systems in the region.

# Attempts at a Single Currency

- In 2000 Caribbean Central Banks developed criteria for the establishment of a single currency
- It was agreed that countries would have to maintain foreign exchange reserves, equivalent to 36 months import cover, 12 months export cover, maintain a fixed exchange rate for 36 months or the restrict exchange rate to no more than 1.5% either side of parity for 12 months and maintain a debt service ratio of 15 % of export of goods and services.
- However CARICOM countries failed these tests and with time they became less and less achievable.

# Financial structure

- The region's financial structure varies from low diversification to moderate diversification.
- In terms of ownership structure, most commercial banks in Barbados are foreign owned, compared to Trinidad and Tobago where until recently all were locally owned. Most member countries have a mix of local and foreign commercial banks.
- More banks in the region are now completely regionally owned or have some cross-border regional ownership.



# Free movement of capital

- Free movement of capital is theoretically said to have been achieved by most countries in the region, but operationally, customers report that transactions are subject to availability and to production of documentation and delays where amounts are significant.

# Free movement of labour

- Free movement of labour has been implemented on a phased basis
- Presently several categories of workers are permitted to work cross border without work permits. It is expected that this phased approach will continue .
- Using the section on services to utilize the delivery of services by services providers in the region has also come up against hurdles from time to time, but the process is becoming smoother with time.

# A single stock exchange

- Efforts to create a single Stock Exchange have not materialized even though each of the 4 Exchanges in the region is small.
- No agreement could be reached on which platforms could be used and efforts at integrating the platforms were not successful.

# Basel rules for Effective Supervision

- All commercial banks in the region subscribe to the Basel rules on effective supervision with varying levels of effectiveness
- The Caribbean group for Bank supervisors routinely discuss the issue of guidelines at the regional level, but the guidelines are eventually issued by each Central Bank at the national level.

# Crisis prevention

- Except for the CL Financial failure, and earlier problems in the Jamaica banking system several years ago, commercial banking in the region have escaped collapses for the most part.
- Since the global Financial crisis there has been increased focus on crisis management, and at the regional level guidelines were being developed by the Council of regional central Bank governors to provide guidance in the event of crisis management.

# Insurance company failure in one member country.

- One particular event however does relate to the global financial crisis. This was the failure of an insurance company with several links to commercial banking and other financial entities including a money market broking company, which caused dislocation in the insurance sector in Trinidad and Tobago with significant repercussions in several other countries in the region.
- The risk of contagion in small economies is of course greater than in large and can be regional where intercompany transactions are significant.

# Balance of Payments support from the region

- Not many countries in the region are able to provide balance of payments support to other member countries.
- Trinidad and Tobago can do so and has done so.
- From time to time deposit placement ( or repurchase agreements) have been used , but these are infrequent.

# Regional Approach to negotiation of trade agreements

- Agreements to have a common approach to external trade agreements was part of the regional approach
- The EPA with the EU was one such arrangement.
- even so there were difficulties with certain sections of the final agreement with some members.



# EPA and market access

- The EU CARIFORUM EPA was put in place when preferential access to the EU market came to an end. It is reciprocal rather than preferential.
- The arrangement goes beyond trade but is not as deep as many other RTAs.
- However, access to the EU market as a result of the EPA has proved disappointing.

# Active risk management and stress testing

- Risk based supervision was introduced to banks prior to the financial crisis.
- Stress testing was however introduced after the crisis.

# Capital adequacy

- Capital adequacy provisions were made somewhat higher in some Caribbean countries than the traditional 8% of risk based assets, so when the international crisis struck, banks in some of the islands were facing the crisis from a position of higher than internationally required capital

# There is evidence of gradual financial integration

- While there was occasional cross border deposit placement among central banks for many years, interbank placement started to rise in the past 20 years, principally because of changing ownership structures and regional ownership of banks across the Caribbean. In Barbados, two of the seven commercial banks are now regionally owned and 5 are foreign owned.

# Debt issues

- From time to time financial institutions in one country in the region would subscribe to substantial sums of government securities issues.

# Subsidiaries preferred to branches

- Even before the financial crisis, some jurisdictions in the region had expressed a preference for or requested that subsidiaries should be the choice of establishment in their jurisdiction over branches. However, in Barbados, many foreign banks are still set up via a branch banking arrangement

# Foreign Currency lending

- Higher levels of foreign currency lending are evident in the floating rate economies such as Jamaica and Trinidad and Tobago. This is less the case in Barbados and the OECS which still operate on fixed exchange rate regimes.

# Hedging instruments

- Hedging instruments tend to be available in the floating rate economies while fixed exchange rate regimes have little resort to hedging instruments in the local market. However the management of the Central banks portfolio of assets and the governments foreign exchange denominated non US debt are routinely the subject of hedging



# Financial Goals not achieved

- Of a single currency ( this however obtains in subregion)
- A CARICOM Investment regime
- A Caribbean Financial Services Agreement (draft approved august 2013)
- Regional Stock Exchnage

# The progressive regionalization approach

- The approach to progressive regionalization proved implementable in terms of facilitating many regional approaches e.g competition policy, telecommunications, intellectual property Disaster Risk reduction.
- Establishment of a Caribbean Court of Justice was also a major step, though it is only used by a few members.
- While these steps toward regionalism have led to increased trade and investment within the region, they have not helped particularly to improve exports outside the region
- However increased use of CARICOM in negotiating fora has been helpful in ensuring defensive negotiating positions.

# Increased efficiency and effectiveness

- Financial cooperation has led to greater cross border business
- to the ability to finance larger projects
- To the greater availability of capital and foreign exchange
- to the ability to more easily have jointly financed projects
- to the ability to support larger projects
- to greater diversification of the financial sector
- greater sophistication of the non-bank financial sector

# Lessons from the Caribbean Experience

- That a phased approach to financial harmonisation seems to avoid crises but takes time
- that alternatives must be considered when setbacks occur (CMCF)
- that efforts must be made to achieve buy-in from affected sectors or groups.(e.g the short-lived CARICOM travellers cheques)

# Lessons from the Caribbean experience

- That regionalism must have its champions. It does not happen just with the passing of time.
- That simultaneous with improving financial cooperation within the regional sphere action must be accelerated with countries and regions outside.
- Response must be rapid in order to take advantage of opportunities as they arise, so bureaucratic hurdles must be minimized while still ensuring oversight at the regional level.

