Public infrastructure investment: A Caribbean perspective

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Introduction and background
Public infrastructure investment is seen as a critical aspect for economic development and poverty reduction in every country. The extent to which this is hindered therefore becomes a cause for great concern. Significant efforts have been made over the past 20 years to demonstrate evidence of the positive impacts. However, there is consensus that under the right conditions, infrastructure development can play a major role in promoting growth and equity, and through both channels help to reduce poverty.

Infrastructure in general refers to physical assets or networks that provide certain critical functions to society. The value of infrastructure derives from the services it provides such as mobility, energy supply, water connectivity and flood protection. It also enables a range of economic activities from production and transport of goods to providing a beautiful environment for tourists. Research indicates that high economic productivity is difficult to sustain without quality infrastructure.

Infrastructure development in the Caribbean has been fairly moderate, as can be seen in the well-developed port and telecommunications sectors. Progress has been made in the areas of access to potable water, electricity and paved roads. However, different states are at varying stages and major gaps exist in the region.

Overall, the Caribbean experienced the highest levels of growth from the 1960s to the early 1980s, which was commensurate with public infrastructure spending. However, since the mid-1980s the pace of infrastructure development has been lagging and not keeping pace with population growth, urbanisation, global trade, social mobility and the environmental sustainability of economies.

During the mid-1980s oil crisis, all the Caribbean small states except for Trinidad and Tobago were severely impacted. The macro-economic structural adjustment programmes that followed resulted in drastic cuts in public infrastructure spending in attempts to reduce the fiscal deficits. This continued apace, leading to infrastructure bottlenecks and the consequent negative impact on growth and development.

Privatisation and PPP
In response, some states embarked upon privatisation programmes where they sought to divest the state of non-core assets. In Jamaica several state assets were divested over the period. The experiences were mixed in that some were successful while others were not.

Jamaica, in response to bottlenecks in education and the road network, entered agreements with private parties to undertake infrastructure works in these areas. However, when these unplanned fiscal commitments were included in the national accounts at a later date, they compounded the already in-train fiscal crisis.

The search for private sector participation was not unique to Jamaica. Other countries with similar fiscal challenges entered various types of agreements with the private sector for the delivery of public infrastructure. Specifically, there was a major deficit in public transportation in the 1980-90s and mini-buses were prevalent throughout the Caribbean. The need for higher quality service resulted in Jamaica transferring a major aspect of public transportation to central government.

The Caribbean was severely impacted by the 2008-09 recession and continues to experience the ripple effects as evidenced by the fiscal shortfalls, high unemployment and increase in poverty. Specifically the International Monetary Fund (IMF) in its Caribbean

Project examples
Capacity constraints/bottlenecks in the airport and road transport sectors resulted in Jamaica entering concession agreements for an airport (Sangster International Airport) and a tolled highway (Trans Jamaican Highway). Both concessions are of the public–private partnership (PPP) modality and the contracts are for 30 and 35 years, respectively. Similarly, in Trinidad and Tobago the need for adequate potable water for the population in and around two industrial estates resulted in a 20-year period of PPP concessions for water production. Both are desalination plants in the Point Lisas and Point Fortin areas. They sell industrial grade water to the Trinidad and Tobago Water Authority for resale to the industrial estates in both locations, thus alleviating the water shortage previously affecting the people. Antigua and Barbuda, in its quest to improve quality and access to health care, entered a PPP concession for the Mount St John Medical Centre located in the capital, St John’s. This is a modern 185-bed hospital which offers a wide range of services and functions as the main medical facility for Antigua and Barbuda.

Regional opportunities – Panama Canal expansion
The addition of a third lane to facilitate super-sized vessels traversing the expanded Panama Canal is projected to carry 50 per cent more cargo on a daily basis. Jamaica specifically, and the region generally, could gain tremendously from the huge potential opportunities if the necessary infrastructures are in place. States should take immediate action to harness the vast prospects ahead.
review for 2012 noted that the region was hit hard through lowered tourism arrivals, remittances and exports. It stated that the general fallout in revenues further widened the infrastructure gaps with the consequential effects on growth.

What is apparent in the infrastructure gap is that the private sector has an important role to play. However, the various public–private arrangements showed up technical gaps in the region on PPP matters including capacity within governments. This has resulted in the PPP process not being fully leveraged for all the potential benefits.

The Commonwealth Secretariat sensitised member countries through training to the advantages of establishing a policy and institutional framework to enhance the process. Subsequently, both Jamaica and Trinidad and Tobago have government-approved PPP policies which were effected in the latter part of 2012. Further assistance of the Inter-American Development Bank (IADB) and the World Bank are ongoing for institution strengthening and capacity building.

**Challenges in the Caribbean’s small states**

The Caribbean has made some strides in the development of infrastructure, positively impacting human development as well as per capita income. The latter has resulted in all Caribbean small states, with the exception of Haiti, being classified as middle income, which automatically led to reduced development flows to the region. Given the high debt and low growth that pervades the economies, leaders have proposed an alternative to the per capita income approach that entails the evaluation of needs and shortcomings that is not captured by income indicators but is rather reflected in other types of gaps.

Regardless of the middle income status of the Caribbean, the reality indicates that there is a serious gap in the stock of infrastructure compared with:

- The needs of the region
- Emerging Asian countries
- Advanced economies

The infrastructure gap is especially visible in the need for cheaper energy sources, paved roads and greater access to potable water.

The Caribbean Development Bank (CDB) in its annual report for 2012 noted that the average output growth slipped to one per cent compared with 1.2 per cent in 2011. Further, CDB stated that the decline in output was associated with a fall off in private investment, alongside fiscal consolidation and a concomitant reduction in capital outlay. Surveys of international investors in the Caribbean have identified local business environment factors such as infrastructure, availability of skilled professional workers and government regulations as the factors that most influence investment in the region. However, limited infrastructure was mentioned as the most limiting factor. The challenges indicate that several initiatives should be implemented simultaneously to confront the many hurdles.
The way forward: Competitiveness and debt reduction

The macro-economic outlook for the Caribbean is conditioned largely by developments in the international economy. The World Economic Outlook (October 2013) indicates that global activity is expected to strengthen moderately but the risks to the forecast remain on the downside. Overall output is expected to expand to two per cent in 2014, an increase of 0.75 per cent on 2013, and should be driven mainly by a stronger United States economy as well as reduced fiscal tightening. The general outlook is for steady recovery but with suppressed growth rates. Given the macro-economic outlook, it is imperative that the Caribbean addresses simultaneously the deep issues that hamper growth. There should be sustained focus on correcting the two critical issues of debt sustainability and international competitiveness since these have a direct impact on infrastructure spending from both the revenue and expenditure sides.

To improve competitiveness specifically, cheaper energy sources to lower production costs should be aggressively pursued. Likewise, fiscal consolidation programmes towards debt reduction, which are in progress for the highly indebted states, should continue. This is necessary since increased revenues and reduced debt obligations allow more to be spent on infrastructure. In order to achieve results it is critical that the strategies employed are deliberate and sustained.

The Caribbean continues to depend on foreign direct investments which have fallen significantly since 2008–09. States should continue to implement deliberate strategies to improve the governance infrastructure (institutions and policies) that are conducive to these flows to the region since studies have shown that the benefits from these inflows are most pronounced for smaller and developing economies. St Lucia and Trinidad and Tobago are the highest ranked states (64 and 66 respectively) in the World Bank’s Doing Business Report for 2014. This demonstrates that much more needs to be done to attract businesses to the region.

PPP readiness in the Caribbean

The medium-term outlook to 2017 suggests growth in low gear and, given the infrastructure deficit in the region, reductions in capital spending are definitely not an option. The IADB has stated that, in order to catch up or keep up with emerging Asian countries, infrastructure spending should be increased to approximately four to six per cent over the two per cent currently being undertaken in Latin America and the Caribbean (LAC).

In order to narrow the gaps, further and deeper engagement of the private sector in the provision of infrastructure through the PPP modality should be elevated. Hence deliberate actions towards the broad support of a PPP environment should be pursued. There is consensus in the region that the PPP modality is a viable option. PPPs, if properly designed and supervised, have the potential of bringing about efficiency gains in the delivery of infrastructure. PPPs can also provide relief from borrowing constraints that may arise from prudent financial management policies. However, there is a serious gap in the state of PPP readiness as well as the greater difficulties for the smaller states in the establishment of a workable PPP policy and institutional framework.

In order to support and attract PPP investors, strong institutional frameworks and a positive investment climate are fundamental. The PPP environment is critical and both Jamaica and Trinidad and Tobago have been included among a list of 19 countries in the LAC region’s 2010 PPP Readiness Index Report. The rankings of 13 and 11 respectively indicate that both states have begun some work towards improving their state of readiness for PPPs. However, upon further examination of the six categories and 19 indicators, more work needs to be done. Jamaica is actively pursuing reforms and capacity-building to improve its readiness in this area. Even more work is needed for smaller island states to put a policy and institutional framework in place.

The multilateral development banks working in the region have indicated and provided support for the PPP modality. Infrastructure continues to be a major business of development banks and therefore countries should leverage support to accelerate the PPP agenda. This is important since PPVs are one of the alternatives in complementing public infrastructure spending.

Challenges

The Caribbean has some very particular challenges:

- Open economies that are vulnerable to external shocks and whose relatively small size prevents economies of scale
- Limited natural resources
- High dependency on tourism, foreign direct investment and remittances
- Removal of preferential treatment from bananas and sugar exports
- Vulnerability to natural disasters that wreak havoc on infrastructure and cause economic shocks
- Climate change – the potential implications to infrastructure in sectors such as fisheries, tourism and energy production are huge given their importance to Caribbean economies
- Low savings rate – this has remained at approximately 18 per cent of gross domestic product (GDP) since the 1980s, in comparison to emerging economies in Asia which are well over 30 per cent. The low savings rate has contributed to low investment in physical infrastructure
- High public debt can limit the ability to provide infrastructure. The high debt burden is one of the most crippling problems in the Caribbean, which was exacerbated by the global recession of 2008–09. In 2012, overall public sector debt was estimated at about 79 per cent of regional GDP. Interest payments on the existing debt stock were in the range of 16–41 per cent of total revenues. Past attempts at tackling debts in the region have not yielded lasting results, the IMF has stated. The World Bank classifying most Caribbean countries as middle income exacerbates the malady. Hence, the majority of the region, except Haiti, no longer benefits from international debt relief nor qualifies for concessional borrowing from the World Bank.
Increase in savings rate

The use of PPPs will not satisfy the gaps. Governments should promote a savings culture which would ultimately form an investment pool for infrastructure development. The IADB, in its 2013 LAC Report, has recommended an increase in domestic savings to boost investment in infrastructure. Infrastructure requires long-term financing in local currency to be sustainable. Institutional investors like the pension funds, insurance companies and mutual funds are natural long-term investors as they seek assets that match the duration of their liabilities, the IADB stated. A portion of pension savings in infrastructure investments would be ideal and can promote productivity and efficiency in both the public and private sectors. Also, by investing long term the institutions would be more active investors thus improving the governance of the enterprises in which they invest.

Domestic savings are supported and should be actively promoted since foreign capital inflows are not reliable. This was seen in the recent recession where capital flows to the region dried up. Also, research has shown that the average stock of infrastructure project appraisal and selection system.

Domestic saving is recommended for pursuit since it acts as a counterpart to foreign saving in that it gives a welcoming signal to foreign investors if residents are also investing locally. An attempt to increase the savings rate is a worthy challenge to undertake and a viable alternative for closing the infrastructure gap. Initially there could be a problem with confidence since three states have executed sovereign debt restructurings. However, targeted long-term policy actions conducive to matching long-term investors looking for stable cash flows with long-term assets, such as infrastructure projects, should be fruitful. An upside to domestic savings is reduced foreign currency exposure, especially for the countries with high debt levels.

The savings culture should be encouraged since the lowest savers in the emerging Asian economies save more than the highest savers in LAC and this translates to higher infrastructure spending and growth. Specifically, Jamaica had a National Savings Programme in the 1960–70s where savings were promoted even at the primary school level. If the savings habit is inculcated from the primary school level, then the child will grow up to be an adult who saves. Incidentally, the period of this programme overlapped a period of growth that the country experienced.

This savings plan should be broad-based and all inclusive (household through to the institutional investors) using several supporting initiatives over a sustained period. This endeavour would require targeted policy actions by governments emanating from long-term planning. Over a period confidence should return to increase private domestic savings. This would be a potential pool of domestic flows into infrastructure investments that should be of a high quality, having passed through a reformed/improved project appraisal and selection system.

Increasing the savings rate could be daunting for some states, but there is a precedent. In Chile the savings rate increased from 1.5 per cent of GDP in 1982 to 30 per cent of GDP in 1989 and since then has remained at close to 25 per cent.

financing in developing countries has remained at a 90 per cent self-financing rate despite the integration of the financial markets (Aizerman, Finto and Radzinell, 2007). The study also showed that those countries with a high self-financing rate grew faster.

Although foreign direct investments are more predictable and have increased in recent years, studies have shown that only ten per cent have been invested in infrastructure, which is inadequate for the current lag and rising needs.

Conclusion

The Caribbean has had a period of prolonged retrenchment in public infrastructure investment, which has consequently resulted in low growth for the region as well as delayed the achievement of some human development goals. It is imperative that the infrastructure gap be narrowed if the region is to meet its needs and achieve consistent growth. The Caribbean is resilient in the face of many challenges and the infrastructure deficit is among those to be confronted. Hence in going forward it is imperative that sustained and deliberate policy actions are pursued in the relevant areas for each state. The following initiatives should be sustained and tackled in a multi-pronged approach to achieve results:

- Debt reduction strategies to be maintained for those countries in fiscal consolidation
- International competitiveness programmes to be aggressively pursued, including access to cheaper energy sources to lower production costs
- Savings programme to be implemented and actively promoted to increase the domestic savings rate which should ultimately build a pool for infrastructure finance
- PPP readiness to be aggressively elevated and pursued in order to increase the engagement of the private sector in infrastructure development
- Further actions to be implemented to be more business friendly
- Continue to build resilience to natural disasters: legal updates and innovation are required for building codes and other mechanisms to better protect Caribbean infrastructure from the expected impacts of climate change

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REFERENCES
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ENDNOTES
1 Malaysia, China, Thailand, Indonesia, Philippines, Vietnam and India.