Jamaica: A Case Study in Debt Sustainability and Sustainable Development

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Abstract. Jamaica’s debt burden has pitched economic development against environmental protection in the country’s quest for sustainable development. Anemic economic growth has prompted the government to institute revenue and expenditure reforms and implement two debt exchanges that have stabilized the economy. However, the debt burden has limited government’s fiscal space to engineer a much needed capital formation with the most promising prospect for any major foreign direct investment coming from a proposed US$1.5 billion investment to build a World Class Logistics Hub in a protected area. Thus, the debt situation has led the government to prioritize “what is to be developed” at the expense of “what is to be sustained” as Jamaica channels its sustainable development course.

Keywords: debt sustainability, sustainable development, Jamaica, environmental protection, public debt.
Introduction
The General Assembly of the United Nations (UN) designated the year 2014 as the International Year of Small Island Developing States (SIDS) to recognize the contributions of SIDS in world affairs. This commemoration provides an opportunity to highlight the challenges faced by SIDS and harness resource to tackle them. In the light of this, the Third International Conference on Small Island Developing States (SIDS Conference) is scheduled to take place in Samoa in September 2014. The theme of the SIDS Conference, “The sustainable development of small island developing States through genuine and durable partnerships,” sets a clear tone for the desire to engage stakeholders in the sustainable development process of SIDS. In fact, since the Barbados Programme of Action (BPoA) (United Nations, 1994), the international community has made special provision to accommodate the distinctive characteristics of and provide support for SIDS in their sustainable development efforts. However, one area of challenge that continues to threaten sustainable development in SIDS is debt sustainability (UNDP, 2010a; UNDESA, 2014). Although the international community has instituted programs to help alleviate debt burden for the poorest countries through the Heavily Indebted Poor Countries (HIPC) Initiative, the enhanced HIPC and the Multilateral Debt Relief Initiative (MDRI), most SIDS identified as having or at the risk of falling into a public debt burden are not poor enough or indebted enough to benefit from these initiatives despite their economic vulnerability (UNDP, 2010a). The quest to attain sustainable development within an economic environment characterized by unsustainable debt levels has thus become a commonplace in many SIDS.

Debt sustainability is described as a situation in which the borrower is able to continue servicing their debt without a large future correction in the balance of income and expenditure (IMF, 2004). However, several definitions have been proffered for sustainable development over the years. Kates, Parris and Leiserowitz (2005) presented a comprehensive review of the concept of sustainable development. Among the popular definitions cited in the literature are those given by the United States (U.S.) National Research Council and the 2002 World Summit on
Sustainable Development. The U.S. National Research Council identified two components of sustainable development: “What is to be sustained” and “What is to be developed.” In this framework, the sustainability arm includes nature (earth, biodiversity and ecosystems), life support (ecosystem services, resources, and the environment), and community (cultures, groups and places). The development arm encompasses people (child survival, life expectancy, education, equity, and equal opportunities), economy (wealth, productive sectors and consumption), and society (institutions, social capital, states and regions). In between these arms are the linkages that ensure that what is to be sustained aligns with what is to be developed and vice versa within an identified timeframe. This framework is not at variance with the Johannesburg Declaration of the 2002 World Summit on Sustainable Development that introduced the concept of three pillars of sustainable development — economic development, social development and environmental protection (United Nations, 2002). Elements of both the sustainability and development arms fit under one or more of the three pillars of sustainable development. The U.S. National Research Council’s definition, however, offers a good analytical framework for examining the debt sustainability-sustainable development nexus in SIDS. Bakari (2014) noted the inherent conflict between economic growth and environmental protection in the sustainable development concept. For any nation under a debt burden, this conflict could be more contentious. This is even more so for SIDS because of their small sizes and dependence on foreign markets. Faced with huge and growing public debts, highly indebted SIDS have focused on strategies to grow their economy by prioritizing the development arm over the sustainability arm. At the extreme, the sustainability arm is even sacrificed in an attempt to capitalize on emerging opportunities that could lead to economic development. This conflict in the drive for sustainable development is better elucidated using a case study and Jamaica provides a perfect case for such analysis. With a debt to GDP ratio of 146%, Jamaica is currently under a heavy public debt burden. During the 2000s, annual debt servicing as a percentage of government
revenues exceeded 112% on average. In 2009, interest payment alone accounted for 65% of central government tax revenues (UNDP, 2010b). Given such a situation in which the government was spending more on debt obligations that it was earning yearly, Jamaica’s public debt situation was unsustainable. Meanwhile, the Government of Jamaica (GOJ) embarked on a number of initiatives to rescue the dire fiscal situation the nation was facing in an attempt to stabilize and grow the economy. However, while these initiatives could result in economic growth and development, they have repercussions on social development and environmental protection. In essence, they potentially could pitch the development arm of sustainable development against the sustainability arm.

This article explores the debt sustainability-sustainable development nexus using Jamaica as a case study. Our aim is to expound on how Jamaica, a SIDS country with public debt burden, is constantly being pressured to prioritize growth over sustainability as a result of the public debt burden. With modest successes already recorded by the GOJ in stabilizing the economy, other SIDS in similar situation may opt to follow the Jamaica example, although the implications for sustainable development are not particularly promising. These implications need to be highlighted more in public discussions and policy debates than they currently are. This paper, it is hoped, will make a meaningful contribution to inform such discussions.

Following this introduction, a brief background information on Jamaica is presented. This is followed by a discussion of the country’s economic growth and public debt experience. Next, the challenges of sustainable development presented by the debt situation are highlighted. The paper ends with the main conclusion from this study and offers some cautionary notes.

**Country Profile**

Jamaica is an upper-middle income SIDS country with a land area of approximately 11,000 square kilometers (sq km) and a population of 2.7 million. The average life expectancy is 73 years (2011 estimate) and poverty headcount was 17.6% of the
population in 2010\(^1\). More than two-thirds of the poor live in rural areas and children account for more than 40% of the poor (PIOJ 2009). The GDP per capita amounted to US$5358 in 2012 while unemployment was 15.4% in July 2013 (IMF, 2013). Jamaica is a typical SIDS with heavy reliance on tourism and primary products, mainly from mining and agriculture. Remittances have also grown to be an important source of household income and foreign exchange in the last two decades reaching US$2.123 billion in 2011 (UN-OHRLLS, 2013).

The Jamaica economy has been on a decline or at best experiencing weak growth. During the two decades preceding 2010, the International Monetary Fund (IMF) reported that the economy grew at an annual average of less than 2 percent (IMF, 2010). In recent times, real GDP recorded negative growth between 2008 and 2010 and again between 2012 and 2013. Inflation, for most parts, is high reaching 16.8% at the height of the food, fuel and financial crises in 2008 but dropped to a low of 6% in 2011. There has been a persistent and sometimes rapid depreciation of the domestic currency. The daily exchange rate of the Jamaican dollar to the US dollar progressively rose from J$51.15=US$1 on January 1, 2003 to J$106.38=US$1 on December 31, 2013, representing a 108% depreciation over an eleven-year period\(^2\). Since the beginning of 2014, the local currency has further depreciated by another 5.5% to J$112.20 as of June 30, 2014.

The situation has not always been like that for Jamaica. Following its independence from Great Britain in 1962, Jamaica enjoyed a robust and growing economy until it experienced its first external shock due to the 1973 oil crisis. This was followed by major political events in 1976 and 1980 that constituted internal shocks to the economy. Throughout the 1980s and the early years of the 1990s, Jamaica again experienced economic growth at the same time it adopted a more market-based economy that encouraged liberalization. With no adequate regulatory supervision, deregulation in the banking sector led to a domestic financial crisis

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\(^1\) World Bank’s World Development Indicators country data.
\(^2\) From Bank of Jamaica Economic Data:
during the mid- to late-1990s in which a number of financial institutions failed or were failing. The government assumed management of these failing banks and in the process guaranteed depositors’ monies (CaPRI, 2008). This would come to be the turning point in Jamaica’s public debt story. Meanwhile, as the government struggled to manage the enormous debt assumed from the failed banks, an external shock hit with the September 2001 attack in the United States that adversely impacted on tourist arrivals. This was followed by the global food, fuel and financial crises of 2007/2008. In between these internal and external shocks experienced by Jamaica, the country was hit by a number of natural disasters, arising mainly from hurricanes. Among the major storms that affected Jamaica since 1980, Hurricane Gilbert which made land fall in September 1988 caused the greatest damage, valued at 26% of the GDP. As shown in Figure 1, the country did not experience significant storm activities in the 1990s but was hit by major storms during the 2000s at a higher frequency than ever experienced, including Hurricanes Charley and Ivan in 2004, Hurricane Dean in 2007, and Tropical Storm Nicole in 2010. Although the value of damages caused by these later storms was less than that caused by Hurricane Gilbert, the persistence and reoccurrence of these events make recovery more challenging and the costs prohibitive with no enough time allowed for reconstruction and recovery before another storm hits. These shocks put together have long-term implications for economic development. One of those implications is public debt accumulation as limited government revenues are devoted to urgent reconstruction efforts thus leaving the government with no option than to borrow to finance its budget.
Figure 1: Damage from Major Storm Events in Jamaica (1980-2010)

Source: Based on data from EM-DAT: The OFDA/CRED International Disaster Database and country data from World Bank’s World Development Indicators.

Economic Growth and the Public Debt Burden

Although Jamaica’s debt to GDP ratio of 146% is regarded high by any standard, this is not a historic high for the country. In fact, during the 1990/91 fiscal year, the debt to GDP ratio was as high as 194% (see Figure 2). However, with a growing economy, the ratio was reduced to below 100% within three years and had reached its lowest value of 71% in 1996/97 fiscal year. Ironically, it was at the time of best public debt performance that the government had to assume significant amount of new debts by guaranteeing depositors, pensioners and policyholders’ interests in failing financial institutions through the establishment of the Financial Sector Adjustment Company (FINSAC) in 1997 with a mandate to “restore stability to Jamaica's financial institutions.” As Figure 2 indicates, in 1995/96 prior to the financial crisis, domestic debt constituted only 30% of public debts. By 1996/97, it had risen to 43% and reached a peak of 61% in 2002/03. The domestic debt portion of the national debt has remained at above 50% since then. Rising from a low of
71%, the nation's public debt to GDP ratio reached a local peak of 124% during 2002/2003. The steady rise could be attributed to the adjustment process following FINSAC which was aggravated by the shock to the tourism sector post-2001. The debt to GDP ratio declined slowly between 2002/03 and 2006/07 before it returned to a path of increasing trend during 2007/2008, the same period when the food, fuel and financial crises began.

![Figure 2: Trends in Public Debt in Jamaica (1990/91-2012/13)](image)

Source: Debt Management Unit, Ministry of Finance and Planning, Government of Jamaica.

In the context of this debt burden, the expenditure pattern of the government is noteworthy. Figure 3 shows trends in major public expenditures and household final consumption expenditure. Immediately following independence, gross fixed capital formation as a proportion of GDP was high while government general consumption expenditure was low but rising. By 1969, gross fixed capital formation reached a peak of 32% of GDP and declined very rapidly to a historic low of 12% of GDP in 1977. Meanwhile, government general consumption expenditure kept
growing until it reached a peak of 22% of GDP in 1982. Understandably, due to the challenges faced by the country during the 1970s, the government had to reduce capital investment and increase expenditure on social services. With the turn in economic fortunes in the 1980s and early 1990s, government investment in capital stock rose again while consumption expenditure declined before the sequence of domestic and global shocks in the latter half of the 1990s and in the 2000s caused gross fixed capital formation to steeply decline again while consumption expenditure increased but at a slower pace than it did before. While household final consumption expenditure fluctuated between 60% and 70% of GDP from 1960 to 2000, it has been on an upward trend reaching 80% or more of GDP since 2005. This reflects the additional financial burden that households have had to bear as the government introduced new tax packages to generate revenues.

Figure 3: Trends in Economic Growth and National Expenditures in Jamaica (1960-2012)

Source: World Bank’s World Development Indicators.
As evident in the data, government’s investment in capital stock is pro-cyclical with economic growth while consumption expenditure in counter-cyclical. The counter-cyclical increase in government consumption expenditure tends to correlate with increase in public debt which suggests that public debts are used for consumptive rather than investment purposes. This presents an interesting background for analyzing the concept of increased public expenditure in times of recession to stimulate the economy. In Jamaica, there is tremendous pressure on the government to increase expenditure on social services in periods of economic downturn rather than reduce its expenditures. For example, the government introduced a no user-fee policy for children at public hospitals in May 2007 and expanded this to cover adults in April 2008. This has resulted in increases in public health expenditure as a percentage of GDP but with no credible evidence of improvement in the quality of health care delivery. Without the stream of revenues required to meet expenditures, the government was confronted with the hard choice of choosing between default on sovereign debt or borrowing, the latter of which adds to the debt burden. Although programmes and services such as the Programme of Advancement through Health and Education (PATH) – a safety net programme that has been implemented with great success – are geared to reduce poverty and help bridge the income inequality gap, they are financed with external debts that add to the current debt stock while the benefits accruing to them are in the medium to long-term. Prevalence of crime and violence in the country also meant that significant amount of public expenditure is devoted to policing and crime prevention activities which, although enhance social harmony and foster conducive business environment, by themselves are not growth promoting, compete for scarce government revenue, and by their very nature cannot be delayed.

Faced with these conflicting demands and the undesirability of an austerity measure or the lack of willingness on the part of the government to institute an unpopular policy, the government was forced to engage in a unilateral debt restructuring of its domestic debt with the implementation of the Jamaica Debt Exchange (JDX) programme in February 2010. JDX allowed the government to
renegotiate the terms of its domestic debt stock to reduce interest payments and extend maturity (UNDP, 2010b; King and Kiddoe, 2010). In February 2013, encouraged by the success of JDX, pressed by the dire public debt situation or both, the government was once again back at the negotiating table for a second domestic debt restructuring in three years. The National Debt Exchange (NDX) had similar purpose as JDX and had been made a precondition for an IMF’s Extended Fund Facility (EFF) which the government badly needed to support its short fall in revenues. Jamaica subsequently secured a four-year Extended Arrangement under the EFF worth 615 million Special Drawing Rights (equivalent to US$948.1 million) from the IMF in May 2013.

The Sustainable Development Challenge

Jamaica’s economic growth has been constrained by both domestic and external shocks that have limited growth and put pressure on the country’s social fabric. In order not to jeopardize social development in an environment of lackluster economic growth, the government resorted to borrowing at an unsustainable level. This further limits growth potential due to the crowding out of private investment as a result of high government borrowing from the domestic market. Irrespective of the interim success achieved through the JDX and NDX, the IMF (2013) noted that Jamaica’s debt burden continues to exceed the benchmark for emerging market. The implication is that while the gross financing needs of the government have improved, the country is not out of peril yet in terms of debt sustainability.

Before the JDX, NDX and the EFF, the government implemented a number of monetary and fiscal policies and initiatives aimed at raising revenue and reducing expenditure. Notable among these are several tax packages and the Memorandum

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3 IMF’s stress testing at the baseline indicates that Jamaica’s debt burden continues to exceed the benchmark for emerging market. In particular, debt level was shown to exceed the benchmark for the baseline while gross financing needs exceeded the benchmark for real GDP growth, exchange rate, and contingent liability shocks but remained under the benchmark for the baseline and for primary balance and real interest rate shocks.
of Understanding (MOU) between GOJ and public sector workers. The tax packages saw increases in the general consumption tax (GCT) rate and the inclusion of several goods and services previously excluded in the GCT bracket. These and other revenue measures were aimed at improving the government’s fiscal balance. On the expenditure side, containment of the government’s wage bill was deemed paramount and the first MOU was reached between the GOJ and the Jamaica Confederation of Trade Unions in February 2004. The parties agreed to “a general policy” of public sector wage restraint between April 1, 2004 and March 31, 2006. The MOU also covered a commitment from the government to control inflation and balance the budget. While wages were frozen in accordance with the MOU, the targets for inflation were never attained nor the budget balanced at the end of the MOU. Notwithstanding, the MOU has been extended several times and the public sector still operates under one form of wage restrain or another.

The GOJ has been able to stabilize public sector wages and salaries at about 11% of GDP during 2008/09 and 2012/13, largely due to the MOUs. In contrast, despite the many tax packages, revenue steadily declined during the same period, except in 2012/13. As the government continues to pursue revenue generating measures that include tax and public sector reforms, public sector workers find themselves on the receiving end. With wage freeze in place, inflation and exchange rate depreciation averaging 11% and 4%, respectively, between 2002 and 2010 (IMF, 2013), public sector employees earn less today in real terms than they earned prior to the first MOU, even with ten years of experience on the job. This erosion of purchasing power has implications for the standard of living and quality of life of many households, especially the middle/working class. This has meant that many persons who previously had no need for state assistance had to seek for such through available social programmes such as PATH.

Rising poverty level, high unemployment rate and high crime rate have posed challenges for social development but the government, within it tight fiscal space, is addressing these challenges and has recorded some progress in crime fighting and

poverty reduction. The GOJ is also at the forefront of environmental protection and disaster management and risk reduction in the Caribbean region. In fact, Jamaica was the first country to upgrade Climate Change to a ministerial portfolio in January 2012. Not surprising, Jamaica was rated as being on track to ensuring environmental sustainability in the latest review of the country’s progress towards the Millennium Development Goals (MDGs). However, faced with the challenge of growing the economy under a heavy debt burden, the government has always considered its options in relation to the country’s natural resources and the tipping point may have been reached.

Over the last decade, there has been an increasing tussle between natural resources exploitation and preservation in Jamaica. Jamaica is home to the Cockpit Country, an area with rich cultural history and home to many endemic species of plants and animals. It has been touted as a candidate to become a World Heritage Site. The Cockpit Country is also rich in bauxite deposit and since 2006 there has been ongoing debate on whether to allow bauxite mining in the Cockpit County in expectation that it will generate the much needed foreign exchange for Jamaica, provide employment opportunities and boost government revenues from taxes. So far, the government has resisted granting such licenses. More recently though, the government announced the plan to build a World Class Logistics Hub that will lead to economic growth by making Jamaica a major transshipment port. However, Goat Islands, the site identified to be the best suited for the logistics hub, is located in the Portland Bight Protected Area (PBPA). The PBPA was created in 1999 with the purpose of protecting 1876 sq km of marine and terrestrial area that support endemic species of birds, iguanas, crocodiles, manatees, marine turtles, and fish. The mere fact that the government is seriously considering a major construction project in a protected area regardless of whether or not it materializes epitomizes the constant conflict between environmental protection and preservation. While the GOJ has been mostly progressive in matters relating to the environment, the unsustainable debt level appears to be a tipping point where the much needed

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economic growth may be pursued at the expense of environmental protection. In as much as it is widely expected that the logistics hub will be a major injection of Foreign Direct Investment in the local economy that will spur growth and generate 10,000 new jobs, there is the concern that the employment opportunities that will be created will mostly go to foreign experts because of the limited skills available locally and only low-paying jobs will be available to locals. In the logic of that argument, proponents do not see any long-term benefit in the logistics hub that will warrant sacrificing a protected area.

All in all, the situation in Jamaica shows that debt accumulation was either caused or heightened by shocks to the economy. With the economy performing below par, economic development has been hard to achieve and the government continues to borrow to sustain social development. As the debt situation became dire and unsustainable, environmental protection is gradually being relegated in the scheme of things, as priority is given to “what is to be developed” at the expense of “what is to be sustained.” Debt restructuring embarked upon by the government has produced some relief, but it has also allowed the government to borrow more, thus adding to the debt stock. With new debts being channeled to provide budgetary support or pay maturing debts rather than for targeted investment in capital stock, the prospect for any major thrust to the economy hinges on a proposed US$1.5 billion investment by the China Harbour Engineering Company (CHEC) to build a World Class Logistics Hub in Jamaica. The proposed mega investment, however, pitches the economic development pillar of sustainable development against the environmental protection pillar.

As Schmid (2014) indicated, government revenue at levels below the expected level contributes to budgetary underperformance which when considering the rigidity of expenditure leads to lower capital expenditure. Hence, “the consistent underexecution of capital expenditure can lead to a deterioration of public goods and infrastructure with adverse consequences for future growth” (Schmid, 2014, p.7). Given this scenario, injection of foreign investment funds is badly needed and the logistics hub idea provides a rare opportunity to stimulate the economy, not only
because of the foreign direct investment that it will bring but also the multiplier effect that it will have on several economic sectors.

However, while the choice of the site for the proposed logistics hub was still being decided with opposing views from stakeholders on the desirability of the preferred location, CHEC revealed that, due to the high cost of electricity in Jamaica, it plans to generate its own electricity for the hub using coal, a cheaper but higher CO\textsubscript{2}-emitting source of energy. So not only is GOJ’s reputation for environmental protection threatened by signaling its willingness to open up a protected area for a major construction project, its efforts in abating CO\textsubscript{2} emissions, enshrined in the National Development Plan—Vision 2030 Jamaica, will be seriously undermined with CHEC’s plan to use coal for electricity generation. As it stands, it does not appear though that the government has a choice in that decision if it really wants to attract the logistics hub investment.

Conclusion
This Jamaica case study is illustrative of what many SIDS face. Governments are constantly confronted with an “either/or” scenario and constrained to choose between economic growth and sustainable development when they are under a debt burden. Unable to engineer their own capital formation, these countries are rarely afforded the luxury to attain sustainable development because of the pressure of debt repayment and mounting recurrent expenditures. Given the overwhelming evidence of the vulnerability of SIDS and the impact of unsustainable debt level on their economies, they deserve a special programme of debt relief that is not conditioned by the country’s income level but rather defined by its economic and natural disaster risk vulnerabilities. Proposed innovative ideas for debt relief for SIDS that include debt conversion for climate change adaptation (UNDP, 2010) should be given a serious consideration by the international community. Had this been on the table, Jamaica would have a choice to keep the Portland Bight Protected Area in exchange for debt forgiveness. Such arrangements for debt conversion will not only relief Jamaica of its debt burden, it will free up government
revenue for investment in capital formation whilst ensuring that environmental protection does not suffer. This would allow Jamaica to develop “what is to be developed” while sustaining “what is to be sustained.”

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References


