

## **DeLisle Worrell: The Barbados IBFS sector and the efficiency of international commerce**

Lecture by Dr DeLisle Worrell, Governor of the Central Bank of Barbados, at the Carleton University, Ottawa, 17 September 2015.

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Small international business and financial services (IBFS) centres like Liechtenstein, Guernsey, the Caymans and Barbados – to take a random selection – have an enduring place in international commerce, because they serve to make the international system more efficient. Through the services that international companies locate in these centres, companies are able to offer products and services to the global market more cost effectively than they would otherwise be able to do. It is because of this economic reason that the foremost centres have proven so resilient, in the face of repeated waves of misrepresentation. The truth, as I will show in this presentation, is that international firms that use subsidiaries in IBFS centres to locate appropriate aspects of their global operations, are more competitive than those that do not.

The sources of IBFS competitiveness vary by country, and include the expertise available in the centre, its global interconnectedness, the local penetration of information and communications technology (ICT), the quality of life available in the centre, the quality of infrastructure, and many others. Importantly, most centres will offer local expertise that is on par with London, New York and Singapore, at significantly lower costs than would be the case for the large global financial centres. In this essay we cite evidence of Barbados' competitive standing in international financial markets.

### **How IBFS centres contribute to global efficiency**

The main factors which make international firms that use well regulated, well networked IBFS centres more efficient than the competition include:

- Such centres may reduce market frictions and information costs to the international firms whose subsidiaries they host;
- They are able to offer internationally comparable skills at lower wages and other costs; and
- They offer a corporate tax regime which provides for lower taxes on value added in the export of goods and services.

Because of these factors the IBFS centre is able to offer benefits to producers and consumers of IBFS goods and services, while at the same time providing an economic benefit to the host country. The investing company is able to produce the services located in the IBFS centre for sale in third countries at significantly lower cost, with no sacrifice in quality. The third country receiving the finance, product and/or service is able to access the output at a more attractive price. The benefit to the IBFS centre is the wages, fees, taxes and other value added in the centre.

There are only a handful of studies which have attempted empirical verification of the extent of efficiency gains due to the use of IBFS centres. Naitram (2014) quantifies the impact of 17 small centres, using data from the IMF's *Coordinated Portfolio Investment Survey*. His findings were that small IBFS centres that offer a wide range of services transmit finance efficiently from investors to productive end users, largely by reducing market frictions.

A study by Hejazi (2015) speaks to efficiency gains for Canadian companies from using IBFS centres as conduits to the global economy. He draws inferences from the complementarity between Canadian outward investment, since Canada became a net exporter of FDI in the

mid-1990s, and the growth of Canadian exports. He finds that the complementarity between FDI and exports is stronger when the Barbados IBFS centre is used as a conduit for investment abroad than it is otherwise.

The study by Worrell and Lowe (2013) reports that Caribbean IBFS centres benefit their economies through their contributions to GDP, government revenues and employment. The sector is especially important as a source of tertiary level jobs in a labour force with levels of educational achievement that are superior to most emerging market and developing economies (EMDEs).

### **Barbados' competitive strengths**

Each year the World Economic Forum issues a *Global Competitiveness Report* on the overall score of almost 150 countries, including Barbados. In the 2014–15 report Barbados' competitive strengths included:

- Health services: life expectancy is high, and there are no major communicable diseases present;
- Education is of high quality, enrolment is high and most teachers are trained;
- There is a good infrastructure of roads, port, airport, and the reliability and coverage of electricity is high;
- The relatively high use of the internet, and the availability of the latest technologies;
- The low level of organised crime, judicial independence, the legal framework, the reliability of Police services, the ethical behaviour of firms, the strength of auditing and reporting systems;
- The soundness of banks and the quality of financial regulation;
- In the labour market, the capacity to attract talent, the high proportion of women in the workforce, and cooperation in labour-employee relationships;
- The intensity of local competition, the quality of local suppliers; and
- The number of patents relative to the size of the country, and partnerships between UWI and industry.

Barbados has additional competitive strengths, beyond those mentioned in the *Global Competitiveness Report*. Important for attracting investment is the fact that English is the native language. Barbados' cultural and historical ties with North America have undoubtedly been a factor in making that region the main source of investment in the Barbadian IBFS sector. The Barbadian climate is excellent and the society offers cultural variety and convenience that makes for a high quality of life.

An important source of competitiveness for Barbados is the fact that the country maintains a sound, comprehensive and up-to-date regulatory framework for all IBFS activity. Joint teams from the World Bank and IMF confirmed the soundness of overall regulation in the most recent Financial System Stability Assessment (2013). Peer reviews are underway for Barbados under the Global Forum for the exchange of tax information, and under the aegis of the Caribbean Financial Action Task Force on money laundering. This regulatory framework is a competitive strength for Barbados, in an international market where it has become vital for companies and financial institutions to protect their good name.

Barbados is proactive in international fora, including the Steering Group of the Global Forum, the Regional Consultative Group for the Americas of the Financial Stability Board and the Working Group on Financial Issues of the CFATF.

Another competitive aspect in which Barbados has an edge is the country's large and growing network of Double Taxation Agreements (DTAs) and Bilateral Investment Treaties

(BITs). The list of countries with whom Barbados has DTAs and BITs is given in Tables 1 and 2.

**Table 1: Double Taxation Agreements (DTAs)**

Double Taxation Agreements in Force	DTAs Awaiting Ratification
<ul style="list-style-type: none"> <li>• Austria, 2007</li> <li>• Bahrain, 2013</li> <li>• Botswana, 2005; protocol, 2015</li> <li>• Canada, 1980; protocol, 2013</li> <li>• Caricom, 1995</li> <li>• China, 2000; protocol, 2010</li> <li>• Cuba, 2000</li> <li>• Czech Republic, 2012</li> <li>• Finland, 1989; protocol 2012</li> <li>• Iceland, 2012</li> <li>• Luxembourg, 2011</li> <li>• Malta, 2002; protocol, 2014</li> <li>• Mauritius, 2005</li> <li>• Netherlands, 2007</li> <li>• Norway, 1990; protocol, 2012</li> <li>• Panama, 2011</li> <li>• Qatar, 2013</li> <li>• San Marino, 2013</li> <li>• Singapore, 2014</li> <li>• Spain, 2011</li> <li>• Sweden, 1991; protocol, 2012</li> <li>• Switzerland, 1963</li> <li>• UK, revised 2012</li> <li>• USA, 1984; protocols 1991, 2004</li> <li>• Venezuela, 2001</li> </ul>	<ul style="list-style-type: none"> <li>• Ghana</li> <li>• Italy</li> <li>• Portugal</li> <li>• Rwanda</li> <li>• UAE</li> </ul>

**Table 2: Bilateral Investment Treaties**

<b>BITs in Force</b>	<b>BITs Awaiting Ratification</b>
<ul style="list-style-type: none"><li>• Canada, 1997</li><li>• China, 1999</li><li>• Cuba, 1998</li><li>• Germany, 2002</li><li>• Italy, 1997</li><li>• Mauritius, 2005</li><li>• Switzerland, 1995</li><li>• UK, 1993</li><li>• Venezuela, 1995</li></ul>	<ul style="list-style-type: none"><li>• Benelux countries</li><li>• Ghana</li></ul>

### **Activities in the Barbados IBFS sector**

The legal framework for IBFS activities in Barbados may be described under four heads. First there are international business companies (IBCs) involved in a wide range of commercial and funding activities, which are exempt from capital controls. These companies are not permitted to offer services to Barbadian residents.

Financial institutions which fall into this category receive a separate license, which requires them to be supervised either by the Central Bank of Barbados or the Barbados Financial Services Authority, in accordance with the relevant international supervisory norms.

Some firms find it preferable to register as domestic companies, even though they offer services only to non-residents. In such cases the company may benefit from a preferential domestic corporation tax, which offers rebates based on the percentage of exports in the firm's output. The firm then may qualify for exemption of revenues earned in Barbados under an appropriate DTA.

The fourth element in the legal framework is a special "carve out" from the Barbados DTA for Canadian insurance companies which qualify. These so-called exempt insurance companies gain relief under guidelines specific to the activity.

### **The future**

Barbados is a competitive, high quality provider of IBFSs. International companies are able to increase their competitive offerings on the global market by judicious use of Barbados' IBFS centre. The economic logic that is driven by competitive forces is what drives expectations of continuing growth of IBFS services in Barbados and elsewhere.

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