GEO

Guyana Economic Opportunities

Guyana Investment Strategy:

A Preliminary Framework

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I. INTRODUCTION

The Private Sector Commission with the assistance of Dr. Arnold McIntyre has prepared a paper on a possible policy framework for an Investment Strategy for Guyana. In preparing the paper detailed consideration was given to the earlier reports on an Investment Strategy:

(a) Guyana: Proposals for An Investment Strategy (USAID/BEEP Project; October, 1997)
(b) Guyana: Quantitative Assessment of Revenue Impact of Investment Incentives Proposed in Draft Investment Strategy (USAID/BEEP Project; June, 1998).

The members of the Private Sector Commission participated in a one-day seminar on 20 October, 1999, to analyse the principal recommendations in these reports and arrive at a set of preliminary proposals on a policy framework for Guyana's Investment Strategy.

II. ECONOMIC CONTEXT

Guyana's economic policy is based on a macroeconomic policy framework that was developed between the Government of Guyana (GOG) and the multilateral financial institutions (IMF and World Bank) as part of Guyana's structural adjustment programme. Any proposals for an investment Strategy must take these policy parameters as given. The macroeconomic policy framework is aimed at achieving stability and confidence in the domestic economic environment via the achievement of exchange rate stability, low inflation, prudent fiscal management and reduced external indebtedness.

Generally, it is agreed that Guyana has made significant strides in achieving macroeconomic stability and building confidence. The latter is extremely important to encouraging investment. Investment is a long-term process and a lot of investments are irreversible. Given these considerations investors react negatively to a lot of uncertainty as perceptions of risk increase significantly and act as a disincentive to private investment. Therefore, the greater macroeconomic stability that has been achieved in Guyana has reduced uncertainty and provides a sound basis to implement an effective Investment Strategy. The strategy would focus on accelerating private investment, particularly in export activity, via the adoption of selective micro policies, e.g. investment incentives and regulatory changes.

Another important medium-term economic consideration is the fundamental changes taking place in the international trading arrangements that will greatly influence Guyana's economic prospects. Guyana is involved in three sets of complex but interrelated external negotiations - a successor agreement to the LOME Convention, a Free Trade Area of the Americas (FTAA) and another round of WTO negotiations – that will alter the preferential trading arrangements the Caribbean has traditionally benefited from. The alterations to the preferential arrangements will require that existing export activities improve efficiency and new export activities come on-stream. This implies increased levels of private investment in the local economy. Therefore, the

implementation of an effective Investment Strategy is a timely response to the changing external circumstances.

III. CREATION OF A PUBLIC/PRIVATE PARTNERSHIP

A vital part of developing an effective public policy is achieving consensus between the social partners – government, business and labour – on national economic strategy. Consensus building is an on-going exercise that can be sustained through dialogue between the social partners resulting in the creation of a public/private sector partnership.

The discussion on an Investment Strategy could be part of an ongoing dialogue between the public and private sector and at some stage labour on public policy. This would mean that the discussion on an Investment Strategy would be the first item on an on-going discussion between the social partners on public policy. Such an institutional arrangement would be important for the effective implementation of economic policy in general, and an investment strategy in particular.

IV. MACROECONOMIC POLICY

As noted earlier the GOG is currently implementing a macroeconomic policy framework as part of its arrangement with the international financial institutions. The policy framework clearly defines the policy parameters within which the Investment Strategy must be developed.

A key element of GOG's macro policy is tight fiscal policy. Guyana has achieved fiscal stability to maintain prudent fiscal management. Therefore, any policy recommendations related to Investment or tax incentives must be evaluated on the basis of their fiscal consequences. The JAFRI/MONTRIE Report does provide a fiscal assessment of the draft proposals contained in the Draft Investment Strategy. The Report takes into consideration the quantitative assessment of the individual investment/tax incentives proposed in the Draft Investment Strategy.

V. ELEMENTS OF AN INVESTMENT STRATEGY

A. Objectives

It is extremely useful to establish some clear objectives for an Investment Strategy. In so doing it is important not to burden the strategy with too many targets as we only have a limited range of policy instruments contained in the strategy. In these circumstances, the following general objectives can be articulated.

- To accelerate private investment flows to stimulate increases in economic growth, employment and foreign exchange earnings via the expansion of exports

- To facilitate the transfer of knowledge, skills and entrepreneurial expertise via direct foreign investment either through wholly-owned subsidiaries or joint ventures.

- To stimulate the development of small enterprises via increased demand for locally produced goods and services.

B. The Importance of Private Investment

The macroeconomic policy framework being implemented by Guyana attaches a lot of importance to the role of the private sector in the domestic economy. The state pursues the objectives of efficiency and equity simultaneously. The GOG focuses on policy reforms aimed at removing bottlenecks or restrictions to the development of private businesses (including small enterprises). Simultaneously, the state ensures that the expansion of private enterprises does not create economic disparities or contribute to increased poverty.

It is important to recognize the importance the state attaches to the expansion of private investment but realize that it is one of a few key objectives to be pursued by public policy and not the principal objective.

C. Small Enterprise Development

The development goals of poverty alleviation and the development of local entrepreneurship demand that a lot of importance be attached to small enterprise development as part of Guyana's Investment Strategy.

A special policy regime including specific investment incentives designed to promote small enterprises should be a critical part of the dialogue between the GOG and the private sector on an investment strategy. A key objective of the *"special regime"* must be to build on existing policy initiatives by developing a comprehensive policy framework consistent with GOG's macro policy framework.

D. Investment Incentives

A large number of countries including many developing countries employ investment/tax incentives as part of a package of measures to stimulate private investment. Generally, it is felt that they may not be the most influential factor in the decision-making process of an investor but with other things being equal they do encourage private investment flows. In other words, they would not be a panacea for bad macro policy but would be complementary to sound macro policy in stimulating increased investment flows.

Since the adoption of the CARICOM Harmonized Fiscal Incentives Scheme to Industry most CARICOM countries have implemented a variety of national investment incentive schemes that have almost completely undermined the harmonised scheme. Consequently, there is quite a lot

of variety in the fiscal incentives provided by CARICOM member states to the domestic economy in general, and to specific sectors, e.g. tourism.

In the dialogue on an Investment Strategy it would be useful to examine the Fiscal Incentive Schemes being pursued by other CARICOM Member States and benefit from their experience. The Draft Investment Strategy did consider the fiscal incentive schemes being pursued by other CARICOM Member States.

(i) Objectives

Fiscal or tax incentives are generally intended to achieve the following objectives:

- To reduce the initial cost of the investment.
- To stimulate re-investment
- To provide producers access to intermediate inputs and capital goods at international prices.

(i) Sectoral Priorities

Typically, a country can either adopt a simple, transparent set of fiscal incentives to be granted to all of the economic sectors. Or, it can provide a specific package of incentives to each individual sector that is targeted as a development priority. In other cases, countries establish Free Trade Zones for specific economic activities to be located in, e.g. textiles/clothing in Mauritius.

A critical part of the discussion on fiscal incentives will be to determine whether Guyana would want to adopt an economy-wide package or sector-specific incentives for targeted sectors. Or, alternatively establish Free Trade Zones.

(ii) Fiscal Incentives

The Draft Investment Strategy identified a set of investment incentives and the fiscal consequences of these were estimated by the JAFRI/MONTRIE Report. After critical examination of both reports the following revised proposals could be advanced:

- **Review of Consumption Tax**

The quantitative assessment revealed important concerns about moving to a uniform consumption tax rate with reduced concessions. A limited statistical database did not permit a detailed empirical investigation. However, it was recognised that the adoption of simple, transparent criteria for the granting of concessions would expand the tax base. This could facilitate the adoption of a narrower range of rates with the lowering of some rates. This could be examined as a possible medium-term policy adjustment while a more detailed Indirect Tax

Reform exercise is conducted to improve transparency, efficiency and revenue generation. These exercises could include examining the feasibility of introducing a Valued Added Tax. A VAT would address the issues of tax concessions in an efficient manner.

- **Corporate Tax Rates**

The quantitative assessment points to revenue losses resulting from a Uniform Corporate tax rate of 35% proposed in the Draft Investment Strategy. A medium-term goal of tax reform could examine the feasibility or desirability of adopting a uniform rate at below 45%. A gradual reduction could be examined consistent with rates in other CARICOM Member States, e.g. 40%.

- **Tax Holiday**

As noted earlier tax holidays are not the most influential factor in the decision-making process of an investor but they are maintained by a large number of countries. An issue for dialogue is whether they should be provided to a select set of economic activities, e.g. non-traditional exports. The duration of the tax holidays is a key policy issue for discussion. Perhaps more importantly, the tax regime that an investor will face after the expiration of the tax holiday must be well established and unambiguous. Many countries have put in place select tax credits in specific areas, e.g. training, R & D and export marketing to reduce the tax liabilities of investors after the expiration of the tax holiday. This is absolutely essential so the investor is not encouraged to seek renewal because his tax status is unclear. This is another key policy issue to be considered in the dialogue.

- **Accelerated Depreciation Allowances**

Generally, it was agreed in both reports that accelerated depreciation allowances are an extremely effective investment incentive. Therefore, serious consideration should be given to adopting the proposals in the Draft Investment Strategy. Note, accelerated depreciation allowances encourage re-investment in plant and equipment.

- **Zero Import Duty for Plant and Equipment**

This is extremely important for exporters as if they purchase imports of plant and equipment at above international prices because of border taxes they would be at a disadvantage from their competitors. Economic policy should not increase the costs of exporters because it hampers competitiveness. Therefore, serious consideration should be given to this measure, principally for exporters.

- **Removal of Dividend Withholding Tax for Non-Residents**

These are short-run revenue losses to removing the 15% withholding tax. However, the issue is whether it acts as a disincentive to foreigners or non-resident Guyanese investing in the local economy. Stimulating significantly higher investment by non-resident Guyanese is an important policy objective. However, it must not worsen Guyana's tight fiscal situation. Therefore, the policy dialogue could examine the feasibility of alternative tax measures.

(i) Institutional Arrangements

The benefits of fiscal incentives can be completely eroded if the application/approval process is cumbersome and characterized by long delays. Therefore, it is important that a simple, transparent and efficient process is established so that the process does not become a disincentive to apply for any package of fiscal incentives.

The granting of investment/tax incentives typically comes under the authority of the Minister of Finance. Therefore, in constituting any committee or arrangement to review applications and decide on the granting of incentives the Minister of Finance has a pivotal role to play. Private Sector participation in any administrative arrangement is desirable. Whatever the arrangement that is adopted, the emphasis must be on developing simple and transparent criteria to guide the approval process. In addition, the arrangements should facilitate timely decision-making not to discourage serious investors. Finally, in establishing criteria for *"approved enterprises"* one could consider the value of the investment, export earnings, employment and possibly location (in the special case of Guyana). This should be an important part of the dialogue on an Investment Strategy.