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THE SIGNIFICANCE OF NON-BANK FINANCIAL INTERMEDIARIES IN THE CARIBBEAN

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The significance of non-bank financial intermediaries in the Caribbean

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In many underdeveloped countries economists are preoccupied with the role of commercial banks. This study focuses on non-banks and gives close attention to certain neglected dimensions of analysis of non-bank financial structure and development. Insights are gained which help to explain the similarities and differences in financial structure between one Caribbean territory and another and between Caribbean territories and developed countries. But the data on a number of non-banks in the Caribbean were too inadequate (and perhaps the substitutability between near money assets and money too great) for us to have developed a general theory of non-bank intermediation, with respect to underdeveloped economies.

As incomes rise people show an increasing preference for long-term, rather than short-term, saving. Therefore, as non-banks are generally in a better position than banks to provide long-term finance, they have an increasingly important role to play in economic transformation. However, non-bank asset preferences (rather than the volume of non-bank saving *per se*) in the Caribbean are far from optimum, from a social point of view. Non-optimization occurs, partly because the Caribbean economies are too open for the development of an efficient capital market and partly because in the main non-bank sector (insurance) multinational corporations dominate; these dependency characteristics intensify the problem of bringing about effective financial policy in the underdeveloped economies of the Caribbean.

".... interesting reading for students of the general theory of financial structure".

THE SIGNIFICANCE OF NON-BANK FINANCIAL INTERMEDIARIES IN THE CARIBBEAN

An Analysis of Patterns of Financial Structure and Development

by

Maurice A. Odle

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NOTE

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In the best academic tradition, our sponsors, while participating in decisions about the planning of the programme, have not attempted to influence the conduct of the research or the conclusions drawn, which are those of the authors alone.

Preface

The subject of this study, "non-banks", was chosen because of the apparent dearth of information in this field at both the micro and macro level, and in both developed and underdeveloped countries. Whereas, since the War, a great deal of research has been done on commercial banks, not very much has been done on non-banks as a group or on the most important institutions of the group, the insurance companies. With a few notable exceptions, the usual pattern has been to relegate the treatment of non-banks to the final chapter of a book. In this study we have not succeeded in expounding a distinct and comprehensive theory of non-bank financial intermediation, not least because we have found out that the institutions are more "near-banks" than non-banks. But we think this study can be a useful point of departure for further work.

The treatment of the subject is influenced by current views in the Caribbean on the need for structural transformation of the region's economies. There is therefore a strong normative element running through the study and frequent mention is made of the policies that need to be pursued in order to bring about financial transformation. But this does not mean that the theoretical aspect has been neglected in favour of the prescriptive. On the contrary, the study draws heavily on the theoretical developments in monetary economics since the war and seeks to modify and extend these theories, when applied to the financial system in the Caribbean. In trying to maintain a certain theoretical and empirical mix, comparative reference is made not only to the Caribbean territories of Guyana, Trinidad and Jamaica, but also to Britain and the U.S.A., in an effort to highlight the basic and strategic factors making for similarity and difference in financial structure. Although certain bank and non-bank roles are substitutable (since the difference is one of degree rather than kind) the relative sizes of (a) the bank and non-bank sectors, and (b) the non-bank subsectors have important implications for economic development.

A deep gratitude is owed to Mr. Asgar Ally, who, as Research Assistant on this project, had the frustrating task of travelling around the Caribbean (sometimes accompanied by me, sometimes alone) collecting data by questionnaire, interview and other methods. Although the data collected on some institutions are still inadequate for purposes of definitive analysis, the fault is not his but is indicative of the poor state of financial statistics in the region.

Mr. Clarence Ellis (and also Mr. Ramdass and Miss Wharton), of the Central Bank of Guyana, provided invaluable computational help and Mrs. Pat Robinson (Director of Research at the Central Bank of Trinidad) and Mr. Alister McIntyre (Director of the Institute of Social and Economic Research U. W. I.) were a constant source of encouragement. Also useful were the comments by participants, on papers written for the 1969 and 1970 Regional Monetary Conferences.

This study might not have been possible without the generous financial help of the Central Banks of Guyana, Trinidad and Jamaica and

Mr. D'Andrade, Dr. McLeod and Mr. Muschette were very kind in making available certain facilities (including office accommodation) at these institutions. Many other people at the government statistical departments and at the various non-bank financial intermediaries also provided useful help. Finally, a deep gratitude is owed to Mrs. Arthur and Mrs. Jameer, who bore the brunt of the typing.

M.A.O.

March, 1970

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CHAPTER I

Non-Bank Financial Intermediaries in the Commonwealth Caribbean: an Overview

In this study we will not be examining all the economies in the Caribbean; in fact we will only be analysing the financial intermediaries in the largest three Commonwealth territories in the Caribbean—Jamaica, Trinidad and Guyana. These countries have been selected partly because of their quantitatively greater economic significance, partly because the lack of non-bank financial statistics is less pronounced, and partly because of the existence in each area of an indigenous Central Bank, with nominal controlling power over the financial system.

THE THEORY OF FINANCIAL STRUCTURE AND INTERMEDIATION

Perhaps the most pioneering work[1] on the theory of financial structure has been done by Raymond Goldsmith. It is impossible to do justice to the monumental work of Goldsmith on financial structure (and its comparative aspects) in a few lines. It is only intended to bring out here certain salient features that might have general importance to this study. Goldsmith has attempted not only to deduce a theory about the share of saving by financial intermediaries in total saving but also to relate saving by financial intermediaries to national product, national wealth and capital formation. Goldsmith is therefore interested in two aspects of financial intermediation—the factors determining the composition of the financial superstructure and the relationship between the financial superstructure and the real infrastructure.

The composition of the financial superstructure is closely related to the size of that superstructure. In the early stages of development, when business is family-sized and the government sector small, external financing is low relative to internal financing. The little internal financing that exists is dominated by debt claims rather than equities and these claims tend to be short term in nature because of the preeminence of commercial banks among financial institutions. When economies approach maturity, the claims/equity ratio tends to fall although claims still maintain a majority share of total financial

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1 See R. Goldsmith: *Financial Structure and Development. Yale University* Press, 1969. This mainly theoretical work is a culmination of his other historical and analytical writings, such as, *Financial Intermediaries in the American Economy since 1900,* Princeton University Press, 1958; *The Financial Development of Mexico.* O.E.C.D., Paris, 1966; "An Approach to the Analysis of Financial Structure and Development" (Paper presented in Buenos Aires at the Eighth Conference of Central Banking officials in the American Continent) and *The Flow of Capital Funds in the Post-War Economy,* Columbia University Press, 1965.

assets; the share of financial institutions in total financial assets rises and increasing diversification among financial institutions leads to a declining share of commercial banks and an increasing share of non-banks. A measure of the role of financial intermediaries as issuers, called the Financial Intermediation Ratio, is therefore the ratio of the issue of the non-financial sector to G.N.P./the ratio of the issue of the financial sector to G.N.P.

The second aspect, the relationship between the financial superstructure and the real infrastructure, is called the Financial Interrelations Ratio (F.I.R.). The F.I. R. is therefore the ratio of intangible assets/tangible assets or wealth (wealth is calculated by multiplying G.N.P. by the average capital/output ratio). Goldsmith therefore attempts to establish a link, not only between financial flows and the system of real flows[2] but also, between the financial stock and the real stock. The long run F.I.R. is calculated using the formula:

$$\frac{F_1}{W\tau} = \beta\bar{\tau}^{1} \left[(\gamma - \pi + \gamma\pi)^{-1} + 1 \right] \left[\kappa\eta + \bar{\phi}(1 + \lambda) + \xi \right] \left\{ 1 + \theta \left[(1 + \psi)^{\eta/2} - 1 \right] \right\}$$

where τ is the date at which measurement is made, β is the capital/output ratio, γ is the growth of real national product, π is the change in the price level, ψ denotes stock price movements, $\kappa\eta$ is the weighted average of sectoral δ (which is really the external financing ratio of the non-financial sectors i.e. value of issues of equities and securities/G.N.P.), $\bar{\phi}$ is the value of issues by financial institutions (and the relative importance of the main intermediaries) ξ measures the role of international financial transactions and θ is the share of issues of equity securities in total issues of non-financial units.

Goldsmith found that the F.I.R. varied from about 2/3 in under-developed economies to about $1\frac{1}{2}$ in very mature economies. The size of the F.I.R. mainly depends on the extent to which saving and investing are separated i.e. the extent to which "business enterprises, home owners and governments need to resort to external financing through borrowing or through issuance of equity securities or are able to finance their expenditures internally out of their own saving. The level of the financial interrelations ratio thus can be traced back to fundamental features in a country's economic structure, such as the concentration of production, the distribution of wealth, the incentive to invest, the propensity to save, and the extent to which business activities are legally separated from household activities by devices such as incorporation.[3]" He found no correlation even in the long run between the ratio of growth of real national product and the F.I.R., because the rate of price change in developed countries was not similar. Therefore the really useful ratios are the Financial Intermediation Ratio (δ/ϕ) and its components—ratio of issue of non-finan-

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[2] See also, A. Sdralevich: "The Interrelationships of the Italian Financial System", *L'Industria*, Apr.—June, 1968.

[3] R. Goldsmith: *Financial Structure and Development*. *Op. Cit*, p. 40.

cial sector/G.N.P. (δ) and ratio of issue of financial sector/G.N.P. (ϕ). He found a significant (though not very close) relationship between the new issue ratio of domestic non financial sectors (capital formation ratio by external financing ratio) and the rate of growth of real national product per head for 1949-63. He also found a "fairly definite association between the ratio of issues of financial institutions (ϕ) and the level of real income per head for less developed countries for which the ratio rises rapidly with the level of income. Thus Spain, Greece, Argentina and Puerto Rico all combine a value of ϕ in the order of 0.10 with an average real income of between $500 and $850. On the other hand, Nigeria, Pakistan, India, Thailand and the Phillipines with average incomes of less than $200 all have a ratio of financial institutions' issues to national product of less than 0.03, while the ratio is in the order of 0.05 for Mexico and Jamaica, both of which have incomes of about $400. Even here, however, a few countries have considerably higher values of ϕ (e.g. Brazil as a result of inflation) or lower values (Venezuela and Trinidad) than would be expected on the basis of their income level. These irregularities among less developed countries nevertheless compare favourably with the picture presented by developed countries."[4]

The first table in the Appendix (1.AI) shows the growth of financial institutions' assets in individual countries at current prices and constant prices. The growth rates vary widely during the various periods of the countries' development. In addition, issues of financial institutions as a percent of gross national product, annual rate of change of financial assets to annual rate of change of G.N.P. and asset/G.N.P. ratios show such wide variation between countries of approximately the same standard of living (Table 1.AII) as to suggest that these countries are not on exactly the same financial path.[5] To a certain extent, the figures shown for Jamaica in Tables 1.AI and 1.AII are an underestimate because only a limited number of insurance companies are included; for Trinidad and Jamaica also, all private pension funds are not included.

Table 1.1 shows the estimated relative sizes of assets of banks and estimated assets of selected non-banks (insurance companies, building societies and government or post-office savings banks) in Guyana, Trinidad, and Jamaica. Non-bank assets as a percentage of these bank and non-bank assets is falling (although we would expect the percentage to be higher and to be increasing or at least stable, if figures for all other non-banks were available) for Guyana and Trinidad; for Jamaica, partly because the Government Savings Bank is holding its own in the face of stiff competition from the commercial banks in particular, the percentage is not falling, but rising. There seems to be such a wide variation in the size of the percentages for the three territories that, later in the study, an attempt will be made to give reasons for these disparities. When, as in Table I.2, we deduct demand deposits

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4 Goldsmith: *Op. Cit.*, p. 383-385.

5 See J.G. Gurley: "Financial Structures in Developing Economies," *Fiscal and Monetary Problems in Developing Countries*. D. Krivine (ed.) F.A. Praeger, 1967.

TABLE 1.1 Relative sizes of Assets of Banks and Estimated Assets of Selected Non-Banks[1] in Guyana, Trinidad and Jamaica—$000 (E.C.)*

YEAR	GUYANA				TRINIDAD				JAMAICA			
	Insurance Companies[2]	Non-bank (including insurance)	Bank	Non-Bank as a % of Total bank and non-bank	Insurance Companies	Non-Bank (including insurance)	Bank	Non-Bank as a % of Total bank and non-bank	Insurance Companies	Non-Bank (including insurance)	Bank	Non-Bank as a % of Total bank and non-bank
1961	94, 190	123, 090	51, 254	70.6	283, 920	309, 320	199, 927	60.7	216, 800	279, 900	322, 378	47.5
1962	97, 980	121, 480	51, 381	70.3	276, 680	296, 680	212, 219	58.3	251, 700	320, 100	337, 186	48.7
1963	93, 240	116, 940	64, 845	64.3	307, 150	327, 450	252, 999	56.4	294, 900	373, 300	342, 048	52.2
1964	111, 000	133, 400	74, 690	64.1	312, 730	333, 130	267, 107	55.5	420, 600	510, 300	420, 298	54.8
1965	99, 040	120, 440	84, 900	58.7	330, 110	349, 910	286, 157	55.0	456, 700	556, 100	479, 026	53.7
1966	134, 270	157, 170	90, 468	63.5	336, 660	355, 860	300, 538	54.2	520, 900	641, 200	519, 576	55.2

* Eastern Caribbean currency.

1 Refers to Government Savings Banks, Building Societies and Insurance Companies.

2 Insurance figures are estimated on the basis of premium income figures using premium income/asset ratio of 1 : 10 for life companies and 1 : 7 for non-life companies. The estimate is a long-term one and is for the insurance companies as a whole. In Guyana, out of a total of 35 foreign companies, the number reporting each year varied between 7 and 13. For Jamaica, only 13 life companies reported regularly out of a total of 24 and only 64 non-life companies reported in 1965 and 59 in 1966 out of a total of 116 (numbers were not available for 1961-1964)

Source: Central Bank Bulletin, Guyana. *Annual Statistical Digest,* Trinidad. *Monetary Statistics,* Jamaica.

TABLE 1.2 Relative sizes of "Pure Savings" accounts[1] at Banks (non demand) and Selected Non Banks[2] $000 (E.C.)

YEAR	GUYANA			TRINIDAD			JAMAICA		
	Non Bank	Bank	Non Bank as a % of Total Savings	Non Bank	Bank	Non Bank as a % of Total Savings	Non Bank	Bank	Non Bank as a % of Total Savings
1961	89,600	24,541	78.5	207,400	111,774	65.0	182,800	111,905	62.0
1962	87,900	30,078	74.5	202,600	121,510	62.5	208,700	132,566	61.2
1963	84,200	40,790	67.4	223,200	140,875	61.3	243,000	171,067	58.7
1964	95,200	48,308	66.3	226,800	144,448	61.1	328,300	192,500	63.0
1965	85,700	57,109	60.0	237,800	158,563	60.0	361,800	218,837	62.3
1966	109,600	63,342	63.4	240,700	174,532	58.0	440,500	260,380	62.8

[1] Consists of Time and Savings Deposits at Banks

[2] The selected non banks are Insurance Companies, Building Societies and Government Savings Banks; and the insurance figures are approximations

Source: *Central Bank Bulletin*, Guyana. *Annual Statistical Digest*, Trinidad. *Monetary Statistics*, Jamaica.

and compare only time and savings deposits at banks with savings in the three non-banks, we find that there is much more similarity in the percentages for Jamaica and Trinidad, reflecting perhaps the greater importance of bank demand deposits in Jamaica, than in Trinidad. By calculating assets as a percentage of G.D.P.,[6] Table 1.3 attempts to show the relative importance of banks and non-banks in the economy. It shows that in Guyana, for selected non-banks the percentage has remained fairly stable, whereas for banks it has increased. In Trinidad the percentage for non-banks has declined, whereas for banks it has remained fairly stable; and in Jamaica the percentage has increased for both non-banks and banks, implying perhaps a more rapidly developing financial structure in Jamaica, since G.D.P. in Jamaica has also been growing very fast. The relatively small size of the percentage in Trinidad (where G.D.P. has also been growing fast) suggests perhaps a relatively underdeveloped financial structure and in Guyana the big size might be due to a slowly rising G.D.P. To be more definitive in our interpretation of the statistics, we ought to know more about the N.F.I., other than insurance companies, building societies and gov rnment savings banks, but reliable figures are not always available.

THE THEORY OF NON-BANK FINANCIAL INTERMEDIATION

Non-bank financial intermediaries in Britain and the U.S.A. have in the last decade been receiving special attention from monetary economists and policy makers because of the recognition that they are capable of thwarting traditional monetary policy whose weapons are directed mainly at commercial banks. Previously, N.F.I. were not a problem because they controlled a relatively small part of total financial assets; however, since the second World War, N.F.I. have grown at such a fast rate that in many countries they collectively control a greater percentage of financial assets than commercial banks. Also, at the same time that N.F.I. reached an asset level of quantitative importance (1950s), there was a return to the use of monetary policy for controlling the economy after its virtual disuse in the previous two decades. During the 1930s, expansionary monetary policy, which was needed instead of contractionary monetary policy, proved to be a failure and fiscal policy was mainly relied on. During the war there continued to be expansionary fiscal policy for obvious reasons, and this situation continued during the immediate postwar reconstruction period. However, when inflationary and balance of payments problems hit Britain and the U.S.A. in the 1950s attempts were made to restrict the level of economic activity via indirect (monetary) methods, but these attempts were anything but successful, and so searching enquiries were made on the workings of the monetary sys-

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[6] See J. M. Burns: "The Relative Decline of commercial banks: A Note," *Journal of Political Economy*, Jan./Feb., 1969.

TABLE 1.3 Assets of Non-Banks and Banks as a percent of G.D.P.[1] $ m (E.C.)

YEAR	GUYANA				TRINIDAD				JAMAICA			
	G.D.P.	Selected[2] Non-banks Assets	Selected Non-banks as %of G.D.P.	Banks as % of G.D.P.	G.D.P.	Selected Non-banks Assets	Selected Non-banks as % of G.D.P.	Banks as % of G.D.P.	G.D.P.	Selected Non-banks Assets	Selected Non-banks as % of G.D.P.	Banks as % of G.D.P.
1961	290	123.1	42.4	17.6	954.8	309.3	32.4	20.9	1172.6	279.9	23.9	27.5
1962	307	121.5	39.6	16.6	1005.7	296.7	29.5	21.1	1153.9	320.1	27.7	29.2
1963	275	116.9	42.5	23.6	1094.2	327.5	29.9	23.1	1227.8	373.3	30.4	27.9
1964	303	133.4	44.0	24.8	1148.6	333.1	29.0	23.2	1314.7	510.3	38.8	31.9
1965	330	120.4	36.5	25.8	1188.0	349.9	29.5	24.1	1402.1	556.1	39.7	34.2
1966	351	157.2	44.8	25.6	1326.5	355.9	26.8	22.7	1548.0	641.2	41.4	33.6

[1] G.D.P. figures are used because G.N.P. figures are not always available.

[2] Refers to Insurance Companies (estimated) Building Societies and Government Savings Banks.

Source: Central Bank Bulletin, Guyana. *Annual Statistical Digest*, Trinidad. *Monetary Statistics*, Jamaica.

tem in these countries.[7] When it was seen that N.F.I. were partially responsible for the ineffectiveness of monetary policy, economists began to make a theoretical and policy distinction between banks and non-banks.

The definitional distinction usually made between banks and non-banks is that (a) the deposit liabilities of banks alone are money since they are used as final means of payment whereas non-bank liabilities are not and (b) banks can create deposits whereas non-banks cannot. Doubts have recently been cast on the usefulness of both of these distinctions.

The "monopoly" position of commercial banks has been questioned on (a) the technical operational level and (b) its relevance for total spending in the economy. It is said that some institutions are already performing technical operations and functions like commercial banks. For example, on the British situation, A.B. Cramp quotes the Committee on the Truck Acts as saying "arrangements, we were told, already exist in many cases for the payment of wages into accounts in building societies..." and the Trustee Savings Banks as telling the Radcliffe Committee that their members "accept cheques in payment of wages into the Bank" and the Finance Houses Association as stating that they are "acting in every sense as bankers: the operation of current accounts, acceptance of deposits, the granting of overdraft facilities."[8] With respect to its relevance for total spending in the economy, the Radcliffe Report stated that "though we do not regard the supply of money as an unimportant quantity, we view it as only part of the wider structure of liquidity in the economy. It is the whole liquidity position that is relevant to spending decisions, and our interest in the supply of money is due to its significance in the whole liquidity picture."[9] The liabilities of N.F.I., although in most cases not as liquid as money, constitute an important part of this total liquidity.

There used to be some controversy in the literature as to whether N.F.I. could create deposits in the same way that banks could create deposit money. The controversy surrounding this capacity of non-banks has now disappeared in the same way as the one that once surrounded banks. At first, discussion on this matter took place, wrongly, in a narrow context, in that it was thought that deposits at N.F.I. were made only at the expense of deposits at banks: "If a private individual then shifts a deposit from a bank to an N.F.I., say in response to an interest rate differential, and the N.F.I. deposits this sum in its own bank account, the total deposits of the banking system will remain unchanged... However the total deposits of the financial system have increased since the building society has accepted a

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7 See Radcliffe Report: *Committee on the Working of the Monetary System* H.M.S.O. 1959 and J. Gurley and E. Shaw: *Money in a Theory of Finance*, The Brookings Institution, 1960.

8 A.B. Cramp: "Financial Intermediaries and Monetary Policy," *Economica*, May, 1962, P. 147.

9 Radcliffe Report: *Op. Cit.*, p. 132.

deposit liability which did not exist before."[10] The process of credit creation arose, it seemed, from the fact that whenever a deposit is made in a N.F.I., a small cash reserve is retained, and the rest is used to make loans to the private or public sector. The private or public sector will use these funds to invest and so generate additional income, a part of which is saved in the N.F.I. (and a part in banks) who use these deposits to start another round of credit creation. The non-bank multiplier is therefore dependent, partly on the amount of the loan-generated income which flows back to the N.F.I. in the form of deposits and partly on the size of the cash reserve holding.[11] Even if the size of the "flow back" is smaller for N.F.I. than for banks, this is partly offset by the fact that the reserve holding is usually smaller for N.F.I., since their deposits are not officially demand deposits (although in practice some of these deposits closely resemble demand deposits.) When it was realized that N.F.I. in some instances catered for types of saving needs that banks did not service and so coaxed out additional deposits (that would not have arisen if banks alone existed) the controversy moved on to a different plane. Economists began to conceive of N.F.I. as institutions in their own right, capable of creating their own financial assets. "The difference between the monetary system and non-monetary intermediaries in this respect, then, is not that one creates and the other does not, but rather that each creates its own unique form of debt."[12] The real difference between banks and N.F.I. would appear, therefore, to be that deposits in the N.F.I. do not promote the willingness of the corresponding creditors to spend as much as bank debt does, because of differences in liquidity. But even this distinction is not entirely valid, since, as mentioned earlier, certain N.F.I. accord some of their deposits the same liquidity as banks do theirs. Today, there is therefore a movement away from the rather "sterile" arguments about concepts such as deposit money creation, credit creation, credit expansion, near money creation, etc. towards a more rewarding comparison of the relative sizes of bank and non-bank assets.

A comparison of bank and non-bank assets in most developed countries would tend to show that non-bank assets are collectively greater than bank assets and that the non-bank share of total assets is increasing. We would also expect the non-bank share to be rising in underdeveloped countries, since the creation of new N.F.I. (and the rapid expansion of not so old ones) is a response to the need for new savings outlets and sources of loanable funds and this increasing sophistica-

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10 R. S. Thorn: "Non-Bank Financial Intermediaries, Credit Expansion and Monetary Policy" in *I.M.F. Staff Papers*, Vol. VI, Nov., 1958 P. 370. See Also G. Clayton: "British Financial Intermediaries in Theory and Practice," *Economic Journal*, Dec., 1962—"The short answer is that there is a multiplier effect arising from a switch out of money into a non-bank deposit". P. 876.

11 See A. N. McLeod: "Credit Expansion in an Open Economy", *Economic Journal*, Sept., 1962.

12 J. Gurley and E. Shaw: *Op. Cit.*, p. 198.

tion of the financial system is partly a product of the increasing sophistication, growth and diversification of the real sector.

The tendency for the bank share of total assets to fall and the non-bank share to rise may have certain economic consequences. Firstly, it is thought that monetary policy might be less effective because the medium through which it works, the commercial banking system, is decreasing relative to G.N.P. It is said that monetary policy affects non-banks less directly and with some time lag. Secondly, if in order to make monetary policy more effective stronger measures are imposed on banks, there may be a distortion of economic activity with bank borrowers getting relatively less loans and non-bank borrowers getting relatively more loans. Thirdly, "there is a loss of flexibility in our financial system—that is, a diminution of the ability of that system to channel available credit rapidly from one sector of the economy to another in response to changing credit demands. The commercial banks alone provide this kind of flexibility. Other lending institutions can substitute for them only in the specialized areas in which these institutions operate.[13]"

SOME FACTORS DETERMINING THE SIZE AND COMPOSITION OF NON-BANK FINANCIAL INTERMEDIATION

Earlier it was shown that, from a functional point of view, the rigid traditional distinction between banks and N.F.I. ought to be somewhat tempered. In fact, since in terms of liquidity of deposits and ability to create credit there might be as much difference between various types of N.F.I. as between banks and N.F.I., there might be some justification in considering each intermediary as merely occupying a special place in the financial spectrum; the difference between them therefore being one of degree rather than kind. Nevertheless, if only because of differences in the impact of monetary policy, there might be some justification in maintaining a generic distinction between banks and N.F.I.

N.F.I. can be said to be of four types:

(1) Savings Institutions—Savings Banks, Postal Saving, Building Societies and Credit Unions and Cooperatives.

(2) Insurance Institutions—Life and Non Life Companies, Pension Funds and Social Security Funds.

(3) Unorganized Money Market Operators—Money Lenders, Pawnbrokers, etc.

(4) Public Finance Corporations—Industrial and Agricultural Credit Corporations, etc.

Like most classifications the above one is arbitrary, in the sense

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[13] American Bankers Association: *The Commercial Banking Industry*. (Prepared for the U.S. Commission on Money and Credit). Prentice Hall Inc., 1962, P. 14.

that the savings and time deposit activity (non-demand deposits) of commercial banks could conceivably be grouped under the non-bank heading, 'savings institutions'. As it stands, however, the above classification has a certain functional usefulness.

The size and composition of non-bank financial intermediation might be said to be influenced by the behaviour of the household sector, the business sector and the government sector, and the general economic environment. Whenever size of non-bank intermediation is mentioned below, this is usually in relation to either G.D.P. (proxy for G.N.P.) or the size of commercial bank intermediation; reference to composition is in the context of the size of any one non-bank intermediary in relation to other non-bank intermediaries.

Since the War, non-bank financial intermediation in many countries has grown at a faster rate than bank intermediation. Not only have the existing non-bank institutions grown at a faster rate, but also new non-bank institutions[14] have arisen. The faster growth of the N.F.I. has occurred for a number of reasons. Whereas banks provide a particular type of service to depositors and investors, non-banks provide a more varied stream of service, catering for the needs of almost every type of would-be saver or investor. Non-banks therefore provide the means for the institutionalizing of saving that would otherwise have been hoarded or held idle. Non-banks also compete with banks for the funds of depositors who traditionally saved in banks; non-banks are able to do this because, in many cases, they are vigorous price and non-price competitors. Whereas banks are inhibited by custom and inter-bank collusion from raising their interest rates on deposits, non-banks are not limited to the same extent, and so the latter are able to attract those depositors who are more income-conscious than liquidity conscious, assuming the deposit capital risk in each institution is either nil or equal.[15] This greater ability of non-banks to raise their interest rate on deposits also makes it possible for savers to hedge against inflation in a post-war world where prices have been seen to be continually rising. The non-banks have been, also, more free to raise their interest rates on loans, partly because they are not subject to rigid Bank rate/lending rate ratios etc. as are banks and partly because the markets for their asset holdings (e.g. mortgages and long term securities) are buyers' markets and capable of bearing a higher rate of interest. Non-banks also tend to have an advantage in non-price competition; for example, insurance companies' policy holders and building societies' depositors are almost certain of securing a mortgage, if they so desire.

To sum up this section on the extent to which the household sector has influenced the growth of non-bank financial intermediation—we

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14 However, it is doubtful whether new institutions like public finance corporations should be included since they do not act like the typical intermediary of transferring funds from surplus to deficit units.

15 The difference in rates, then, supposedly reflects the difference in withdrawal waiting time and other withdrawal facilities.

can say that individuals have institutionalized deposits of once-idle funds, made new types of deposit[16] as a result of the activating and stimulating influence of non-banks and have in certain instances preferred to deposit funds at non-banks rather than banks because of better price and non-price services[17] offered by non-banks. The evidence seems to indicate that non-banks are a real rival to banks: "Non-bank intermediary liabilities are close substitutes for money whether money is defined traditionally or broadly. The demand for money is negatively related to changes in yields on non-bank intermediary liabilities, and it has in fact been reduced by quality changes in non-bank intermediary liabilities as Gurley and Shaw argue.[18]" This conclusion of Lee, based on a comparison of demand and time deposits and savings and loan association (building society) shares, has important implications for the continuing tendency of individuals to economize on money balances and for the faster growth of non-banks *vis-à-vis* banks. Further evidence is available supporting the substitutability hypothesis: "Time deposits and savings and loan association shares are also very good substitutes for money and can be ranked in decreasing order of closeness to money..."[19]

The general tendency towards planning in the present day economic world has also affected individuals' saving and consumption habits with certain implications for non-banking intermediation. Because most families plan to own a house, sometime in the near or distant future, there would be a natural tendency towards saving in an institution like a building society (or insurance company) which more or less guaranteed loans to its depositors. Similarly, individuals would want to save in insurance companies in order to ensure that consumption levels remain constant for oneself in post-retirement life or for one's family after one's death. "It is our contention that people desire assets and not saving, that the desired assets depend upon normal income and that the amount of the difference between desired and initial assets that will be made up in any period depends on the period's length."[20] Saving for post-retirement life has assumed greater quantitative significance since World War II, partly because of increasing longevity; also the number of families (if not the average size of families) has increased rapidly in recent decades, partly be-

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16 Along with banks, "organized" non-banks have been responsible for the probable fall in intra-individual, intra-family and shopkeeper loans ('relations credit'), "box-hands", pawnbroking and moneylending.

17 For example, government savings banks have attracted the deposits of small irregular savers, and non-life insurance companies have attracted funds at the cost of risk taking that a bank would not entertain.

18 T. Hun Lee: "Substitutability of Non-Bank Intermediary Liabilities for Money. The Empirical Evidence," *Journal of Finance*, Sept. 1966. P. 455.

19 V. K. Chetty: "On Measuring the Nearness of Near Moneys," *American Economic Review*, June, 1969. p. 280.

20 I. Friend and P. Taubman: "The Aggregate Propensity to Save: Some Concepts and their application to International Data", *The Review of Economics and Statistics*, May, 1966. See also M. Friedman: *A Theory of the Consumption Function*, Princeton University Press. 1957.

cause of a fall in the age at marriage, and this has affected demand for mortgages.

In most countries, non-bank saving is well over 50 per cent of total bank and non-bank saving. Table 1.AIII shows the quantitative significance of savings of a selected number of non-banks in the U.S.A., compared with commercial bank savings. The non-bank share (which is rising) would have been even much more significant if figures had been available for non-life insurance companies, non-insured pension funds, state and local government retirement funds, investment companies' funds and the savings of credit unions. It is probable, also, that personal savings are a more important element in non-bank saving, than in savings of banks and that a greater and greater proportion of personal disposable income is going into non-banks.

"Saving" by business firms for "transactions purposes" can be served by holding either short-term securities, demand or time deposits in banks or "time deposits" in building societies[21]. As stated above, the ability of non-banks to compete with banks for deposits would depend on the extent to which the differences in interest rates offset differences in liquidity. "Saving" by business firms for precautionary purposes can be done either via the typical savings account or constantly renewed time deposits, (or to a lesser extent, by holding non-life insurance policies.) In this area, non-banks seem to offer a more specialized service than banks and because of their more flexible operations, savings at non-banks should rise rapidly when the business sector is growing. "Saving" by business firms for "speculative purposes" most often takes the form of hedging against a possible loss rather than trying to make a very large future gain. This saving can be done either by holding Treasury Bills directly (where the risk of an adverse movement of the rate of interest in the given period is small) or by holding time deposits[22].

On the lending side, some businessmen (like individuals) would prefer to save in non-banks where they can get a long-term loan rather than save in banks which grant mainly short-term (though renewable) loans. Those agricultural, industrial and commercial concerns wanting a mortgage are likely to give some weight to this consideration in placing their savings, since liquidity needs severely limit the volume of mortgage loans banks can make. The rise of public finance corporations to provide long-term development finance is an indication that even the private non-banks are incapable of coping with the great demand for medium and long-term finance. In the absence

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21 Studies have shown that banks' time deposits and demand deposits compete with one another; thus, logically, time deposits at building societies not only compete with time deposits at banks but also with demand deposits . See, for example, D. E. Bond: "The effects of change in the ceiling rates on deposits at commercial banks," *Yale Economic Essays*, Fall, 1967.

22 This "transactions", "precautionary" and "speculative" terminology is said to be unfortunate since Keynes used it in relation to individuals and to describe money balances held, rather than institutionalized saving.

of an efficient equity market, public finance corporations are therefore an important source of long-term credit.

The behaviour of the government sector since the War has also contributed to the rapid growth of non-bank financial intermediation. The rebirth of monetary policy in the 1950s has led to major constraints being put on the operations of banks. For example, the reserve ratios in banks have been increased (and once increased seldom fell immediately after the need for the restrictive monetary policy passed) and this has made it impossible for banks to satisfy all their customers, some of whom turned to non-banks. Restrictions on bank advances have not only had a similar effect but, by reducing the most profitable section of the banks' business, have also made it less possible for banks to raise their deposit rates (which anyhow tend to be sticky because of collusion and the traditional tie to bank rate) to attract new deposits. The growth of the public sector and the public debt has also contributed to the rapid growth of N.F.I., since long term securities (with their high yield) ideally "match" the long-term liabilities of institutions such as life insurance companies. Moreover, the tacit government commitment to maintaining a reasonably high level of economic activity has helped to prevent financial failures and crises and has made depositors feel that their savings at the less tried (compared to banks) N.F.I. are safe. In some countries, e.g. the U.S.A., the government actually guarantees certain non-bank deposits.

The changing economic environment has also been responsible for the rapid growth of non-bank financial intermediation. The more developed and sophisticated an economy becomes, the more varied an outlet for deposits is demanded and the more varied tends to be the supply and use of funds. In the same way that individuals' taste for new goods rises with rising incomes, individuals have a high income elasticity for placing savings at the relatively new type (non-bank) financial institutions. As pointed out earlier, this is partly due to the fact that the durable goods[23] that individuals wish to buy, e.g. houses, are of a nature requiring a discontinuous, and large long-term outlay of credit, which non-banks find easy to provide. It is also because business firms are becoming more concentrated (making self-finance difficult) and because technological change demands a minimum size plant for efficiency that the capital/output ratio in some sectors is tending to rise thereby increasing demands on the long-term finance of private and public N.F.I. There is thus mutual stimulation and continuous interaction between the real sector (and its components) and the non-bank financial sector (and its components).

SCOPE AND STYLE OF NON-BANK FINANCIAL INTERMEDIATION

It is hardly possible to discuss the adequacy of the level of non-bank

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23 By offering policy loans, insurance companies also rival banks in the finance of relatively small medium-term purchases e.g. motor-cars. These effects would be accentuated if there are tendencies towards redistribution of incomes in the society.

financial intermediation in isolation since, as we said earlier, banks and non-banks can, to a certain extent, be considered as functional substitutes. Thus, even if statistically the volume of non-bank intermediation is low in one country, relative to that in another comparable country, commercial banking might be able to make up this leeway and vice versa. This might account for some of the differences between Guyana, Trinidad and Jamaica, for bank and non-bank assets as percentages of G.D.P., between 1961 and 1966 (See Table 1.3). Similarly, internal financing can take the place of external financing, and primary securities (banks' direct holding of equity, government and other securities) can be useful substitutes for secondary securities (assets representing claims of non-bank depositors.) In the same way, the quality of non-bank financial intermediation can partly compensate for deficiencies in quantity.

The adequacy of the scope or quantity of non-bank financial intermediation can conceivably be assessed by calculating the ratio of the non-bank financial superstructure (intangible non-bank assets) to the real infrastructure (tangible assets or wealth) and seeing how closely this approaches some optimum or shadow figure. Because of certain statistical difficulties (especially that of calculating wealth) the proxy relationship—non-bank assets/G.N.P.—might be used instead; the ratio of change in non-bank assets/change in G.N.P. might then be used to gauge how quickly a country is approaching some optimum non-bank assets/G.N.P. ratio.

The non-bank assets/G.N.P. ratio that we consider optimum for a country is probably related to that country's standard of living or G.N.P. per head, since Table 1.AII shows that the *total* assets/G.N.P. ratio is generally bigger for developed countries than for underdeveloped countries. It is difficult to say whether this ratio will continue to rise for developed countries, since Table 1.AI's growth rate of assets and Table 1.AII's growth of assets/growth of G.N.P. show that for some developed countries there has been a decline and for others there has been an increase. Perhaps the most we can say is that the rate of approach towards the optimum ratio will slow down with economic development, implying financial economies of scale. The same can be said for an optimum non-bank assets/G.N.P. Ratio.

Any deviation from the optimum or norm would suggest an oversupply or undersupply of financial intermediation, unless there are certain peculiarities about an economy which explain the significant difference between it and the mean for countries with a similar standard of living or G.N.P. per head. We have already alluded to factors such as the distribution of income and the size of the government sector as possibly affecting the need for external or indirect financing and therefore probably influencing our financial ratios. Another factor stimulating financial intermediation is the degree of separation between producers and consumers by intermediate units ("layering ratio"). Is there then an "oversupply" or "undersupply" of financial intermediation in the Caribbean? It is difficult to conceive of an oversupply of private financial intermediation since saving is a voluntary act; also borrowing from financial intermediaries is always

forthcoming except in a slump and really depends on the expected rate of return from any investment that might be undertaken. However, it is said that there is greater ease of entry into the financial sector, than the real production field, since the physical capital requirements are smaller[24]. But the profit test of survival is the same in the finance sector as in the production sector; if there is an oversupply of loanable funds, lending rates would be so low relative to deposit interest rates that certain financial intermediaries would make losses and have to leave the industry and if there is price collusion, all intermediaries should make abnormally low profits. If there is an undersupply, on the other hand, market forces should cause profits to be very high, assuming the average rate of return on investments or loans to the many seekers is significantly greater than the rate of interest needed to coax the marginal deposit from the relatively few savers. In the Caribbean, it is thought that there is an undersupply of lending to local undertakings because of the metropolitan "credit worthiness" standards adhered to by foreign intermediaries as reflected in the large quantities of foreign securities held; this undersupply is really an allocational problem and a different head office/branch firm relationship would result in the scarcity of loanable funds being much less acute. A measure of undersupply therefore, is the extent to which more real projects would be undertaken if more finance were available (i.e. the degree to which finance instead of other factors is a constraint on production). It is believed that foreign financial inflows, private and public, fall far short of domestic outflows (which take the form of repatriated profits and foreign securities and other foreign asset holdings).

The quality of financial intermediation is almost as important as the quantity of financial intermediation. Non-banks (and banks) should be so geared as to be able to (a) coax out the last potential dollar from depositors in order to be able to maximize their loan offerings (b) operate on a least-cost basis and (c) distribute funds so as to maximize their income since in so doing society's income is maximized (provided that there are no discrepancies between social costs and private costs and social benefits and private benefits.) The problem of maximizing output and minimizing costs is nearly the same as that faced by firms in the real sector except that because modern financial technology is perhaps more easily transmitted and adopted, than production technology, the N.F.I. in the Caribbean are expected to be using the latest techniques for infusing confidence in depositors, standardizing loan techniques and terms and improving credit analysis and surveillance of borrowers. However, there is every certainty that

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24 The oversupply view partly stems from the belief that in the Caribbean there was slavish imitation and colonial transplantation of every type of metropolitan institution; but this is really an argument for rationalization of our existing institutions to suit our particular needs. Moreover, Table 1.3 and Tables 1.AI, 1.AII and 1.AIV do not really indicate that there is an over-supply of financial intermediation in Trinidad and Jamaica. See also C.Y.Thomas: *Monetary and Financial Arrangements in a Dependent Monetary Economy*. I.S.E.R., U.W.I., Jamaica, 1965 for an analysis of the relationship between metropolitan and colonial based financial institutions.

TABLE 1.4 Savings of selected types of Private Non-Banks as a % of total

	1961		1963		1966	
	Guyana	Trinidad	Guyana	Trinidad	Guyana	Trinidad
Insurance Companies[1]	68.9	86.3	72.6	86.0	80.2	87.6
Building Societies	6.9	3.2	6.0	3.4	4.9	3.6
Government Savings Bank[2]	22.5	5.8	19.7	5.2	13.1	3.7
Credit Unions and Friendly Societies[3]	n.a.	2.7	n.a.	3.1	n.a.	3.5
Other Private Cooperative Societies[4]	1.7	2.0	1.7	2.3	1.8	1.6

1 Slight variation in the number of companies reporting in Trinidad; in Guyana also the figures are approximate ones. Insurance saving relates to the estimated size of the "insurance fund" of life companies and "reserve fund" of non-life companies.

2 The Post Office Savings Bank is arbitrarily included as a private non-bank.

3 The figures for Trinidad are an estimate. Figures for Guyana are hardly ever published and because the actual figures are believed to be quantitatively quite insignificant, an estimate has not been made.

4 In Trinidad, some cooperatives seem to be secondary rather than primary institutions e.g. The Agricultural Societies receive a significant part of their funds from the Agricultural Bank which is a quasi-government institution. Figures for Trinidad and Guyana are approximations and relate to both active and inactive societies.

Source: *Central Bank Bulletin* and *Quarterly Review of Financial Statistics*, Guyana., *Annual Statistical Digest*, Trinidad.

TABLE 1.5 Percentage size of Commercial Bank and Insurance Saving (combined) compared with other Private Non-Banks[1] $m. (E.C.)

Year	Guyana				Trinidad			
	Total Private Financial Saving	Banks and Insurance Companies	Banks and Insurance Companies as a % of Total Saving[2]	Other Non Banks as a % of Total Saving	Total Private Financial Saving	Banks and Insurance Companies	Banks and Insurance Companies as a % of Total Saving	Other Non Banks as a % of Total Saving
1961	129.8	101.5	81.3	18.7	409.5	379.2	92.6	7.4
1963	146.8	123.3	84.0	16.0	478.6	445.3	93.0	7.0
1966	194.8	172.7	88.7	11.3	529.3	497.6	94.0	6.0

[1] Includes Post Office Savings Bank.

[2] Insurance saving represents an estimate of life 'insurance fund' and non-life 'reserve fund'.

Source: *Central Bank Bulletin* and *Quarterly Review of Financial Statistics*, Guyana. *Annual Statistical Digest*, Trinidad.

the third objective is not being attained in the Caribbean; if the N.F.I., (in particular insurance companies, pension funds, special sugar funds, and post office banks), were to lend locally the funds that they use to purchase foreign securities, the social benefits would far exceed the present private benefits to these N.F.I. (i.e. the creation of incomes locally would exceed any higher interest earned on foreign securities.) In many cases the Caribbean governments seem to be ignorant of these "external economies" arguments, as is demonstrated for example by the continuation of Government Savings Bank legislation, stipulating a certain percentage portfolio holding of foreign securities.

There are other criteria which can be used for assessing the quantity and quality of financial intermediation. One criterion used by Goldsmith is the "density" of financial intermediation. Density refers to the number of financial institutions relative to size of national income and population. Table 1.AIV shows the number of institutions operating in certain territories, including some Caribbean countries. But mere numbers are an insufficient guide; we ought to know something about the extent to which a branch system operates and the number of branches. We need to know more about the degree of "institutional concentration" i.e. the extent to which more than one institution serves basically the same function. For example, mortgage banks do not exist in the Caribbean but building societies probably perform the same function. Thus we need to know the extent to which the intermediaries are competitors or complements and the local/foreign ownership ratio. We also need to know the distribution of institutional financial power; insurance companies, government (post office) savings banks and to a lesser extent, building societies, dominate the non-banking scene (though in the Caribbean the building societies are unusually small, as seen in Table 1.4) and in the whole financial system the extent to which commercial banks and insurance companies dominate the others (see Table 1. 5) constitutes a new sort of "financial dualism".[25]

Finally, we believe that the open nature of the Caribbean economy has contributed to the "open finance" policy pursued by the N.F.I. and the banks (e.g. purchasing of foreign securities, financing of import-export trade) since finance tends to follow trade. Naturally the two things have reinforced one another. The duopolistic nature

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25 In the chapter, "Financial Dualism and Monetary Development and Independence", of *The Economics of the Developing Countries*, Hutchinson, 1964, H. Myint's dualism relates to the extent to which the money market financed solely the modern expatriate plantation and mining sector and the unorganized money market financed the indigenous peasant and small scale producer sector. We believe that this distinction, though still important in some Asian and African countries, is less operative today in the underdeveloped countries of the Caribbean, where the peasant sector is relatively small and has increasing access to the organized financial market. In some Asian countries, for example, it is estimated by one author that the unorganized financial market rivals the organized market in size; see A. A. Rozental: "Unorganised Financial Markets and Development Strategy", *Journal of Development Areas*, Vol. I, No. 4, July 1967.

of the economies i.e. the predominance in most cases of two industries, and the branch plant or structurally dependent nature of these industries and economies have in some way contributed to the types of financial dualism referred to above. Further reference will be made to some of the points mentioned above, later in this study.[26]

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26 The effect of the stage of economic development on the patterns of financial structure varies between countries. However, for many economies in the very early stage of development, especially those which were peasant rather than plantation based, the unorganized financial market was probably almost as big as the organized financial market. In the next stage of economic development, the organized financial market becomes much bigger than the unorganized financial market; not only do the organized banks become bigger than the organized non-banks but the organized non-banks themselves become bigger than the unorganized non-banks. In the mature stage of economic development non-banks assume supremacy over banks, who, however, remain important; and unorganized non-banking is exceedingly small (almost negligible) compared with organized non-banking. A fuller discussion of the inter-group, inter-intermediary and intra-intermediary structures is presented in the following chapters.

TABLE 1.AI Growth of Financial Institutions' Assets in Individual Countries, percent per year

	1930-38		1939-48		1949-63	
	Current Prices	Constant Prices	Current Prices	Constant Prices	Current Prices	Constant Prices
Argentine	3.6	4.8	20.8	7.0	21.1	−3.0
Australia	3.3	4.3	10.6	6.9	8.0	2.9
Belgium	3.4	1.4	13.1	−1.4	8.2	6.9
Brazil	6.3	1.2	17.5	5.0	27.9	3.8
Canada	2.9	4.8	9.1	3.5	8.4	5.5
Denmark	3.3	3.4	8.0	−0.9	7.1	4.1
Egypt—U.A.R.	−2.9	0.7	19.4	6.7	7.3	6.1
France	4.4	4.5	22.5	−8.1	16.0	8.9
Germany	3.6	6.0	−5.3	−10.2	14.4	11.6
Great Britain	3.6	3.8	9.2	2.9	5.4	2.1
Greece	5.8	1.9	61.1	−8.6	20.4	13.4
India	7.8	12.2	16.0	4.1	7.7	6.4
Israel					31.8	18.1
Italy	4.2	5.2	36.4	−6.9	16.4	12.8

Table 1. AI (continued)

Jamaica					11.5	6.9
Japan	7.9	4.9	40.0	−15.4	25.0	19.3
Mexico	11.4	9.0	23.2	9.1	15.5	8.3
Netherlands	3.6	4.3	8.8	5.8	8.9	5.2
New Zealand	5.5	5.1	8.0	2.4	6.6	3.4
Nigeria	5.4	12.1	17.3	−6.0	16.7	14.0
Norway	0.5	0.3	12.1	3.9	5.8	1.2
Pakistan					8.3	6.8
Phillipines	5.6	9.3	13.6	−1.2	10.2	8.8
Puerto Rico	−0.6	1.1	16.8	11.8	11.6	7.2
Rhodesia					11.8	9.4
Russia—USSR	26.2	5.6	10.9	3.7	10.4	9.6
South Africa	7.4	8.4	13.0	7.7	8.2	4.7
Spain	1.4	−0.9	13.2	0.8	14.8	7.6
Sweden	4.6	2.6	6.5	0.8	8.2	4.1
Switzerland	1.1	3.5	3.8	−2.0	8.0	6.4
Thailand	3.5		34.8	3.3	12.6	9.7
Trinidad			20.9	11.5	9.1	4.9
U.S.A.	2.3	3.9	9.6	2.4	6.6	4.5
Venezuela	4.3	8.2	14.5	7.5	12.3	11.3
Yugoslavia	1.1	5.4	21.3	−0.4	22.9	16.1

Source: R. Goldsmith: *Financial Structure and Development*, Yale, 1969.

TABLE 1. AII Issues of Financial Institutions as percent of GNP, Rate of Change of Assets/Rate of Change of GNP, and Asset/GNP Ratios

	1930-1938			1939-1948			1949-1963		
	Issues as a percent of GNP	Rate of change of assets/rate of change GNP	Assets/GNP (percent)	Issues as a percent of GNP	Rate of change of assets/rate of change GNP	Assets/GNP (Percent)	Issues as a percent of GNP	Rate of change of assets/rate of change GNP	Assets/GNP (Percent)
Argentine	3.1	3.22	97	14.1	1.13	113	9.6	0.77	52
Australia	4.7	3.80	131	15.1	1.31	165	8.5	0.83	129
Belgium	3.7	−2.14	140	9.8	0.77	102	10.6	1.63	161
Brazil	3.8	1.30	67	11.4	1.03	70	19.5	0.93	55
Canada	4.3	−1.47	155	10.4	0.79	124	10.1	1.19	166
Denmark	6.7	1.27	198	13.7	0.80	166	11.8	1.00	166
Egypt—UAR	−1.4	0.45	60	9.6	1.33	90	6.9	1.25	111
France	5.5	−16.27	130	6.6	0.73	63	11.4	1.31	104
Germany	4.2	1.53	99	−5.3	8.13	107	12.8	1.06	124
Great Britain	5.6	2.43	158	13.6	1.22	184	8.6	0.86	162
Greece	3.5	1.06	66	5.2	0.86	37	9.3	1.44	83
India	1.7	−2.26	30	4.2	1.03	35	3.5	1.62	53
Israel						61	22.9	1.34	138
Italy	6.0	62.42	137	23.1	0.78	67	18.6	1.77	174
Jamaica						46	4.8	1.05	50
Japan	18.4	0.92	212	31.8	0.68	61	29.3	1.68	217
Mexico	3.0	2.02	33	6.4	1.17	41	6.1	1.18	56
Netherlands	5.9	−1.54	187	12.6	0.89	169	13.5	1.03	176

Table 1. AII (continued)

	1930-1938			1939-1948			1949-1963		
	Issues as a percent of GNP	Rate of change of assets/rate of change GNP	Assets/GNP (percent)	Issues as a percent of GNP	Rate of change of assets/rate of change GNP	Assets/GNP (Percent)	Issues as a percent of GNP	Rate of change of assets/rate of change GNP	Assets/GNP (Percent)
New Zealand	9.3	1.95	160	12.2	1.06	167	8.1	0.79	130
Nigeria	0.0	−1.70	12	0.4	0.61	5	1.8	2.61	20
Norway	1.3	0.16	187	19.8	1.17	219	8.8	0.68	148
Pakistan						22	2.7	1.87	37
Philippines	1.9	−2.89	48	3.8	0.85	39	5.2	1.45	60
Puerto Rico	−0.3	0.76	41	6.6	1.41	62	7.8	1.22	82
Rhodesia						136	14.0	1.16	169
Russia—USSR	3.3	−17.24	23	2.1	1.29	27	3.3	1.60	44
South Africa	8.1	2.12	124	18.3	1.50	184	13.4	1.00	185
Spain	1.1		81	10.5	1.02	83	12.0	1.14	105
Sweden	7.5	1.61	161	9.2	0.83	142	10.9	1.04	148
Switzerland	3.4	−0.78	325	9.9	0.49	225	20.4	1.20	272
Thailand			27	3.9	1.03	29	4.5	1.38	47
Trinidad			19	4.6	1.73	40	3.0	0.87	33
U.S.A.	4.4	−1.75	185	12.6	0.78	147	9.6	1.15	167
Venezuela	1.3	4.38	33	4.1	1.20	41	5.4	1.39	66
Yugoslavia	0.7	−0.42	79	6.4	0.94	68	21.5	1.51	138

Source: R. Goldsmith: *Financial Structure and Development*, Yale, 1969.

TABLE 1. AIII Share of Savings of Selected Non-Banks and of Banks, U.S.A.

	Life Insurance	Mutual Savings Banks	Savings & Loans Associations	Total of Selected Non-Banks	Bank Demand Deposits	Bank Savings & Time Deposits	Total Bank	Total Bank & Selected Non-Banks
(Billions US$)								
1945	43.3	15.4	7.4	66.1	75.9	30.1	106.0	172.1
1950	61.8	20.0	14.0	95.8	92.3	36.3	128.6	224.4
1955	86.5	28.1	32.1	146.7	109.9	48.4	158.3	305.0
1956	92.1	30.0	37.1	159.2	111.4	50.6	162.0	321.2
1957	97.3	31.7	41.9	170.9	110.3	56.1	166.4	337.3
1958	102.6	34.0	48.0	184.6	115.5	12.3	178.7	363.3
1959	108.0	34.9	54.6	197.5	115.4	65.9	181.3	378.8
(Percentages)								
1945	25.2	8.9	4.3	38.4	44.1	17.4	61.6	100
1950	27.5	8.9	6.2	42.7	41.1	16.2	57.3	100
1955	28.4	9.2	10.5	48.1	36.0	15.9	51.9	100
1956	28.7	9.4	11.5	49.6	34.7	15.7	50.4	100
1957	28.8	9.4	12.5	50.7	32.7	16.6	49.3	100
1958	28.2	9.4	13.2	50.8	31.8	17.4	49.2	100
1959	28.5	9.2	14.4	52.1	30.5	17.4	47.9	100

Source:
(1) *Life Insurance Companies as Financial Institutions (Op. Cit.)*, p. 35.
(2) *The Commercial Banking Industry (Op. Cit.)*, pp. 69 and 78.

TABLE 1. AIV Number of Types of Financial Institution in Operation

	1860	1880	1900	1910	1929	1938	1948	1963
Argentine			5	7	7	8	10	10
Australia			7	7	9	11	13	15
Belgium		10	11	12	15	18	18	20
Brazil				6	7	8	11	12
Canada		11	11	11	13	16	17	17
Denmark		7	9	9	12	12	12	16
Egypt—UAR			5	5	5	6	8	10
France	9	9	11	11	13	14	19	20
Germany	12	12	15	18	20	21	22	23
Great Britain	13	14	16	17	23	23	23	23
Greece				4	7	7	8	8
India		5	5	8	10	14	17	18
Israel							12	14
Italy		11	12	14	14	15	17	18
Jamaica							12	14
Japan		5	10	10	13	15	19	33
Mexico			4	4	9	16	20	20
Netherlands		10	11	11	16	17	18	18
New Zealand		8	8	11	11	12	14	14
Nigeria					4	4	5	7
Norway		6	10	12	12	12	16	16
Pakistan							6	12
Philippines				6	6	8	9	12
Puerto Rico					5	5	9	14
Rhodesia							7	10
Russia—USSR			6	6	4	4	4	4
South Africa				8	10	10	13	16
Spain			6	6	10	11	12	14
Sweden		8	12	15	18	18	20	22
Switzerland	7	7	7	11	15	15	18	17
Thailand						5	6	7
Trinidad					7	7	8	8
U.S.A.	7	9	10	12	19	19	19	20
Venezuela				3	3	3	6	14
Yugoslavia					9	9	2	8

Source: R. Goldsmith: *Financial Structure and Development*, Yale, 1969.

CHAPTER II

The Nature of Operations of Insurance Companies in the Caribbean

ASPECTS OF THE THEORY OF INSURANCE

Insurance can be of lives or it can be of property. Life and non-life (general) insurance are usually, but not always, carried out by separate companies.

There are at least three major attributes of saving by policy holders in life insurance companies.[1] The first is that most policy holders are dominated by precautionary motives, since the holding of a policy or the payment of a premium is an attempt to spread risks or to hedge against early mortality. The second attribute is that a life policy is a long-term contract fulfilled by a regular saving of a stable amount ("locked-in saving"). A withdrawal from the contract earns the surrendering policy holder only a portion of the premium paid (after expenses have been deducted) and so there is economic pressure towards the continued payment of premium, once it has started. The third attribute is that life companies are potential sources of liquidity, since the companies' liabilities are the assets of policy holders. Policy holders can borrow on the security of these assets (or realise them) although this type of liquidity is inferior to that of commercial banks, government savings banks and building societies

Since the War, endowment policies have grown so much faster than 'whole of life' policies that it can be said that people are progressively viewing life insurance, not so much as a source of possible income for one's dependents, if premature death occurs, but as a way of making very long term savings. More recently, the advent of policies with profit, which more than compensate for the rate of inflation and the average rate for discounting future income, combine aspects of pure insurance, security provision for post retirement and profit making[2] (partly making the life insurance policy, then, an investment with a postponed or once-and-for-all return.)

As a protection against death, life insurance saving is unique, but as a protection against living post-retirement life in poverty, life insurance companies have rivals in commercial banks. But even so, life insurance has certain advantages, like income-tax concessions and the ability to combine life assurance with savings; also an annuity contract gives certainty of income for the rest of one's life, whereas commercial bank savings may be run down too fast or too slow.[3]

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1 See C.Y.Thomas: *Op. Cit.*, for a discussion on some of these points.

2 See L.L.Werboff and M.E.Rozen: "Market shares and competition among financial intermediaries", *Private Financial Institutions* (U.S.Commission on Money and Credit). Prentice Hall, 1963.

3 See G.Clayton & W.Osborn: *Insurance Company Investment. Principles and Policies*, George Allen & Unwin, 1965.

The growing importance of life insurance saving has certain implications for the community's consumption function. Since, by endowment types of insurance saving, the individual over his life cycle is trying to even out the flow of income during his post-working life into a more regular flow of expenditure, this reinforces the tendency for the short-run marginal propensity to consume to be less than one, but for average consumption levels to be fairly unitary over one's life time.[4] This attempt to make "income" more permanent over time would tend to have some effect also on investment and the stability of investment patterns.[5]

Non-life insurance refers primarily to the insuring against loss of property (and to the insuring against sickness, accident and general casualty, which are also sometimes done by life companies.) Here the theory of pure insurance is much more relevant than in the case of life insurance, where saving is done for purposes other than the avoidance of risk. It is therefore possible to apply individual risk theory where the gain or loss resulting from an individual policy is considered. The premium paid partly represents the probable loss that the individual would suffer, were it not for the fact of insurance. Thus non-life insurance allows the individual to exchange his good for a more secure (insured) good at a premium or price: "The problem of optimal insurance coverage is formally similar to the problem of optimal inventory stockage under uncertainty. To inventory a product is to "insure" against sales loss—the larger the inventory given the distribution of demand, the greater the "insurance coverage". If casualty or liability loss (demand) is less than the insurance coverage (inventory level), excessive insurance cost (inventory holding cost) is incurred. If casualty or liability loss (demand) is greater than the insurance coverage (inventory level), one must absorb the cost of the unrecoverable loss (sales loss). These two components of loss must be balanced in determining optimal insurance (inventory) levels."[6] The premiums paid have some relationship to the type of insurance coverage. The maximum acceptable premium "is the premium where he would just be indifferent between having and not having the insurance."[7] Mossin also sets out the mathematical and statistical conditions for optimal insurance at a given premium, optimal re-insurance quota and the optimal amount "deductible" (i.e. the first number of dollars the insurer has to pay on any claim) and concludes: "We have directed attention to the wealth effect on the propensity to take insurance coverage, and the common conclusion in all four cases was that this effect is negative if the individual's utility function shows risk

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4 See A. Ando and F. Modigliani: "The 'Life Cycle' Hypothesis of Saving: Aggregate Implications and Tests", *American Economic Review*, March, 1963.

5 See R. Eisner: "A permanent income theory for investment: Some empirical explorations", *American Economic Review*, June, 1967.

6 V. L. Smith: "Optimal Insurance Coverage", *Journal of Political Economy*, Jan/Feb., 1968, p. 68. Minimum and maximum regret criteria can be used.

7 J. Mossin: "Aspects of Rational Insurance Purchasing", *Journal of Political Economy*, July/August, 1968. p. 554.

aversion decreasing with wealth."[8] It would be difficult for an individual firm to calculate the exact benefit of insurance since probability analysis is only useful for calculating the expected losses from risk-taking and is not capable of dealing with uncertainty. "The firm purchases the factor input insurance service and transfers its risk of certain losses to the insurer. The effect of this risk transfer is to eliminate extreme variation in the cost curves, from one time period to the next, which would result if catastrophic losses (fire, acts of God etc.) were borne by the firm. Thus some of the iregularities and vicissitudes of the economic life of the firm are smoothed out by insurance. The firm is then freed to concentrate on the entrepreneurial and business risks which are a function of innovation and are essentially uninsurable."[9]

When the insurance company insures life or property it is accepting "a collective risk", which is a function of the variation in the pure premium distribution and the number of exposure units or claims. Thus in "pooling" the risks of the individuals and firms wanting insurance, the insurance company is itself accepting risks. Because of the risk factor, the insurance company tries to maximize expected yield in the long-run rather than the short-run owing to the fact that in order to meet a claim assets may have to be sold and a capital loss sustained or the rates of interest on new securities may be less than on old securities, causing a lowering of investment income and an endangering of the contractual undertaking on old policies.[10]

Because of the nature of the life insurance contract the accumulation of funds is essential for the payment of certain future liabilities, the only uncertainty being the pattern of occurrence of these liabilities; in non-life insurance, however, the accumulation of funds is in the nature of a safeguard, since unless there is a claim funds may never be paid out. For a group of life policies, premiums in the early years would tend to exceed claims, whereas for a group of non-life policies it is less so. The great unpredictability in the time of occurrence of a fire, accident or other catastrophe makes it necessary for non-life companies to be more careful about their reserve policy and to adopt a more liquid asset structure. Non-life companies, such as fire, also have to make sure that the geographical distribution of their liabilities is not too concentrated (otherwise reinsurance needs to be great) since the occurrence of one claim does affect the occurrence of a second claim (a similar situation exists for life companies in an epidemic); this has implications for probability of loss calculations, since risk theory usually assumes independence of risks and claims.

STRUCTURE AND GROWTH OF INSURANCE BUSINESS

"The inadequacy of statistical data prevents us from giving an accur-

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8 J. Mossin: *Op. Cit.*, p. 563.

9 D. B. Houston: "Risk, insurance and sampling", *Essays in the theory of Risk and Insurance*, J. D. Hammond (Ed.). Scott, Foresman & Co., 1968. p. 169.

10 See C. Arthur Williams (Jnr.): "Game-Theory and insurance consumption", *Essays in the Theory of Risk and Insurance (Op. Cit.)*

ate measurement of either the rate of development of insurance business or the precise role of these institutions in the mobilisation and distribution of savings."[11] Although this was written in 1964/5, it can be said to be still true for Guyana (and also Jamaica).

There is a serious lack of adequate non-bank financial statistics, because, until recently, there has been a preoccupation with banks, to the neglect of non-banks. This neglect is particularly acute in Caribbean countries and is related to both the breadth and depth of the statistics supplied. For example, there are practically no figures collected systematically by any government department or agency on private pension funds. The inadequacy of institutional insurance statistics is particularly great. In Guyana and Jamaica, many companies do not submit annual reports to the Statistical Department, the chief offenders being the foreign companies (agencies or branches of metropolitan companies), who sometimes give as their excuse the fact that their balance sheets are consolidated i.e. integrated with those of their head offices. This situation can be remedied, at a small cost, by a change in the companies' accounting procedures and should be made a condition for their operating in the Caribbean. The figures of those companies which do submit reports are deficient in certain vital areas. For example, the asset structure is not sufficiently detailed; we need a clear picture of the maturity structure of securities held and a breakdown of mortgages into residential, commercial, industrial and agricultural, and also by size. There is need therefore to improve the collection of non-bank statistics in order for us to understand better the workings of the N.F.I. and the way they affect the economic process. Commissioners, charged with the task of collecting adequate statistics, should be appointed for the major N.F.I. or there should be a single Commissioner responsible for all the N.F.I. (a sort of Central Non-Bank). At the moment, throughout the area, there seems to be some misunderstanding between the Central Bank and the Government Statistical Department as to who is really responsible for the collection of the non-bank financial statistics.

Insurance business in the Caribbean has certain well-defined structural features. One feature is the large number of registered companies that operate in the area compared to the number of commercial banks. In Guyana, in 1962, there were 41 companies, in Trinidad 66 companies and in Jamaica 140 companies. A second feature is the relatively large number of non-life companies that carry on business. In Trinidad there are 24 life and 42 non-life companies, in Jamaica 24 life and 116 non-life companies, and in Guyana 24 life and 17 non-life, although the figures for Guyana may be an underestimate since it seems as though there are a few unregistered foreign agencies not issuing new policies, but servicing old ones. A third feature is that the size of life insurance business is considerably greater than that of non-life business. Table 2.1 shows that life insurance business is about twice the size of non-life business in Trinidad; in Guyana the relative importance of life has apparently decreased over time but this may be due to the increased number of non-life companies re-

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11 C.Y. Thomas: *Op. Cit.*, p. 132.

TABLE 2.1 Distribution of Premiums Between Life and Non-Life Policies, Guyana, Trinidad and Jamaica*—$m (E.C.)

	Year	Life	Non-Life	Total	Life %	Non-Life %
Guyana	1960	6.178	2.474	8.652	71.4	28.6
	1961	7.368	2.931	10.299	71.5	28.5
	1962	7.566	3.047	10.613	71.3	28.7
	1963	7.697	2.325	10.002	76.8	23.2
	1964	9.301	2.570	11.871	78.3	21.7
	1965	7.704	3.143	10.847	71.0	29.0
	1966	9.729	5.283	15.012	64.8	35.2
	1967	11.402	5.565	16.967	67.2	32.8
	1968	10.959	6.237	17.196	63.7	36.3
Trinidad	1954	7.311	4.328	11.639	62.8	37.2
	1955	8.684	5.201	13.885	62.5	37.5
	1956	9.821	5.556	15.377	63.9	36.1
	1957	11.055	6.100	17.155	64.4	35.6
	1958	12.559	6.884	19.448	64.6	35.4
	1959	15.461	7.898	23.359	66.2	33.8
	1960	17.696	9.400	27.096	65.3	34.7
	1961	19.410	10.488	29.898	64.9	35.1
	1962	18.846	11.395	30.241	62.3	37.7
	1963	20.265	12.126	32.391	62.6	37.4
	1964	19.823	12.617	32.440	61.1	38.9
	1965	21.406	12.260	33.666	63.6	36.4
	1966	21.779	10.965	32.744	66.5	33.5
Jamaica	1965	32.846	18.322	51.168	64.2	35.8
	1966	36.154	22.766	58.920	61.4	38.6
	1967	41.179	22.982	64.161	64.2	35.8

* For Guyana, out of a total of 34 foreign companies, the number reporting each year varied between 7 and 13. For Jamaica, only 13 life companies reported out of a total of 24; for non-life premiums, reporting was also limited e.g. 64 companies in Jamaica reported in 1965 and 59 in 1966 out of a total of over 116 companies.

porting. In Jamaica, the relative importance of life and non-life business is nearly the same as in Trinidad, and in Guyana towards the end of the time period.[12] A fourth feature is the large number of foreign insurance companies operating in the Caribbean; for example, in Guyana, of the 41 companies registered, 34 are known to be foreign. A fifth feature is that it is believed that foreign companies have a relatively greater dominance in non-life business than in life business probably because of the short-term nature of the non-life contract and also the smaller need to provide on the spot services, such as policy loans, as is the case with life business. A sixth feature is that probably a few large companies dominate the others, especially in life business.

In trying to assess the growth of insurance companies, at least four variables are important:

(1) The number of companies in existence.

(2) The total number of policies issued, the numbers of the various types of policy and the average value of all policies.

(3) The size of total premium income and size of premium income for the various types of policy.

(4) The size of total assets.

We have already spoken about the relatively large number of insurance companies in existence and the fact that over time the number has been increasing. However, a more important criterion should be the number in effective operation. It is possible for a company to be registered but to be operationally stagnant; moreover it is only recently that the deposit or registration fee (necessary before insurance companies can carry on business in the Caribbean) has been raised to significant proportions.

The total number of life policies relative to the size of the population is a useful indication of the extent to which life insurance has penetrated the community. In Trinidad, the population in 1966 was 985,000 and the number of policies for companies reporting was 127,758 i.e. a "penetration ratio" of approximately 1 to 8. When account is taken of the fact that the average size family in Trinidad is fairly large and also that with a fast population growth rate the number of people below working age is relatively great, the degree of penetration of life insurance seems to be fairly great. Figures are not available for Guyana and in Jamaica the number of policies held by about 17 reporting companies was 123,536. Table 2. 2 shows the number of the various types of policy and the average value of each type of policy in Trinidad:

Although the number of companies reporting tends to vary between types of policy, the figures probably indicate the growing importance

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12 Because all the companies do not report in Jamaica and Guyana, it is perhaps not possible to attach much significance to the very small territorial differences in the relative sizes of life and non-life insurance business.

TABLE 2.2 Numbers for Types of Life Policy and Average Value of Each Type—Trinidad 1966

	Number of Type of Policy	Average Value of Type of Policy $(E.C.)
Endowment	58,095	4,206.6
Ordinary Life	45,162	7,292.3
Group Life	249	249,976.0
Industrial Life	24,252	713.8
All types	127,758	5114.4

Source: Statistical Department, Trinidad.

of endowment policies over ordinary life policies and reflect the changing nature of insurance saving. However, the average value of all life policies in Trinidad of $5113 in 1966 seems rather small when compared to the average value for reporting companies in Jamaica of $8086, in view of the fact that the G.D.P. per head in Trinidad in 1966 was $730 and in Jamaica $484. In Guyana, which had a G.D.P. per head in 1966 of $320 the average value of policies for one very large domestic life company at the end of 1966 was $3806. Table 2.3 illustrates these facts:

TABLE 2.3 Average Value of Life Policies Compared $ (E.C.)

	Average value of Policies	G.D.P. per head
Guyana	3806	320
Trinidad	5113	730
Jamaica	8086	484

In Trinidad, most of the endowment policies that were issued in 1966 were of relatively small value, whereas for new ordinary life business there was a fairly even spread between small, medium and large size policies (indicating perhaps a rapidly rising standard of living.) Table 2.4 bears this out

Change in the size of premium income can also be a useful indication of the growth of insurance companies. Premium income might be paid on a wide variety of policies; [13] in fact companies have been

13. For a description of these policies, see J. D. Hammond and A. L. Williams: *Essentials of Life Insurance*, Scott, Foresman & Co., 1968

TABLE 2.4 Numbers* of Small, Medium and Large New Endowment and Ordinary Life Policies—Trinidad 1966 $(E.C.)

	No. up to $5,000	No. above $5,000 but under $10,000	No. $10,000 and under $20,000	No. $20,000 and over
New Endowment Policies	2458 (11)	612 (10)	644 (10)	111 (8)
New Ordinary Life Policies	1480 (12)	1181 (12)	1988 (12)	700 (12)

* Figures in brackets refer to the number of companies reporting on the particular item.

Source: Statistical Department, Trinidad.

offering a greater and greater variety of policies in their competition for the savings of individuals. Also, since the agents of insurance companies tend to make 'vigorous sales efforts' to commit individuals to insurance policies, it would be interesting to find out whether this active and "physically imposing" form of competition would cause premium income to grow faster than G.D.P. or whether there are certain unchangeable laws or forces at work which tend to make insurance saving, as reflected in premium income, a stable percentage of G.D.P. In this regard, it is believed by some economists that the rapid growth of insurance saving (life) might be at the expense of other less actively competitive financial intermediaries. The real issue, therefore, is whether individuals aim at some optimum asset preference scale and equate the utility from the last dollar saved in a life insurance company with the utility from a last dollar saved in a bank or some other non-bank or whether individuals can be persuaded against their "will" to substitute one financial asset for another. Table 2.5 shows the rates of growth of premium income and G.D.P. in Guyana and Trinidad; it shows that for most years life premium income has been growing faster than non-life premium income, that both life and non-life premium income have tended to grow faster than G.D.P. (but only marginally so in Trinidad) and that towards the end of the 1954-66 period these tendencies have been somewhat reversed in Trinidad. The reasons for the above tendencies might be, not so much that insurance companies are enticing saving away from other institutions, but that people have an income elasticity greater than unity for insurance services within a certain income range (and that Trinidad might be approaching the end of this income range) and also that when income growth slows down there is a time lag before insurance growth slows down, because of the contractual nature of insurance saving. (The growth rates of premium income in Guyana contain a small element of estimation for the last year). Generally, the contractual nature of insurance saving makes for some degree of stability in life premium income, and life and non-life premium income combined, as a percentage of G.D.P. and

TABLE 2.5 Growth in Premium Income and Growth in G.D.P. (Life and Non-Life) in Guyana and Trinidad $m(E.C.)

GUYANA	Year	G.D.P.	Rate of increase	Rate of increase in G.D.P. per head *	Life Premium income	Rate of increase	Non-Life Premium Income	Rate of increase	Life and non-life premium income	Rate of increase	Life Premium as % of G.D.P.	Non-Life Premium as a % of G.D.P.	Life & Non-life Premium as a % of G.D.P.
	1960	263.5		8.1	6.178		2.474		8.652		2.3	0.9	3.3
	1961	289.8	10.0	7.3	7.368	19.3	2.931	15.6	10.299	19.0	2.5	1.0	3.6
	1962	307.2	6.0	3.3	7.566	26.8	3.047	39.6	10.613	3.0	2.5	1.0	3.5
	1963	275.4	−10.4	−12.9	7.697	1.7	2.325	−23.7	10.002	−5.8	2.8	0.8	3.6
	1964	302.9	10.0	7.5	9.301	20.8	2.570	10.5	11.871	18.7	3.1	0.8	3.9
	1965	329.6	8.1	6.0	7.704	−17.2	3.143	22.3	10.847	−8.6	2.3	1.0	3.3
	1966	350.9	6.5	6.6	9.729	26.3	5.283	68.1	15.012	38.4	2.8	1.5	4.3
	1967	376.1	7.2		11.402	17.2	5.565	5.3	16.967	13.0	3.0	1.5	4.5
TRINIDAD	1954	430.6			7.311		4.328		11.639		1.699	1.0	2.703
	1955	499.4	16.0	12.5	8.684	18.8	5.201	20.2	13.885	19.3	1.739	1.0	2.462
	1956	556.3	11.4	8.1	9.821	13.1	5.556	6.8	15.377	10.7	1.765	1.0	2.497
	1957	659.1	18.5	15.5	11.055	12.6	6.100	9.8	17.155	11.6	1.677	0.9	2.603
	1958	719.4	9.1	5.9	12.559	13.6	6.884	12.9	19.443	13.3	1.746	1.0	2.703
	1959	799.1	11.1	7.2	15.461	23.1	7.898	14.1	23.359	20.1	1.935	1.0	2.923
	1960	865.9	8.4	5.3	17.696	14.5	9.400	19.0	27.096	16.0	2.044	1.1	3.129
	1961	954.8	10.3	8.9	19.410	9.7	10.488	11.2	29.898	10.3	2.033	1.1	3.131
	1962	1005.7	5.3	1.5	18.846	−2.9	11.395	8.6	30.241	1.1	1.874	1.1	3.007
	1963	1094.2	8.8	6.0	20.265	7.5	12.126	6.4	32.391	7.1	1.852	1.1	2.960
	1964	1148.6	5.0	2.1	19.823	−2.2	12.617	4.0	32.440	0.2	1.726	1.1	2.824
	1965	1188.0	3.4	0.9	21.406	8.0	12.260	−2.3	33.666	3.8	1.802	1.0	2.834
	1966	1326.5	11.7	9.3	21.779	1.7	10.965	−10.6	32.744	−2.7	1.642	0.8	2.468

* Source of population data—*Quarterly Statistical Digest*, Trinidad. *Bank of Guyana Bulletin*

for Trinidad this is confirmed by fairly small standard deviations of 0.29 and 0.77 respectively.

As a more rigorous test, we correlated life premium income, non life premium income, total premium income and total premium income per head, with G.D.P. for Trinidad, and arrived at correlation coefficients, 0.88, 0.30, 0.60 and 0.51, respectively. The correlation coefficient, 0.88, is significant at the 0.05 confidence level. We can usefully refer to the ratio of premium income to G.D.P. as the "Insurance Intermediation Ratio"(I.I.R.)[14]. The I.I.R. could conceivably be a useful ratio for financial planning. For Guyana, as Table 2.6 shows the correlation coefficients are all significant at the 0.01 (annuities are included in life premium income), confidence level.

It should be noted that the growth of life and non-life premium income is interrelated other than through changes in G.D.P. For example, the growth of fire insurance business is in some way connected with the growth of life insurance companies, which are the main source of mortgages in the Caribbean. And we suppose that the more fire protection is available the more willing people are to seek (and life companies more willing to grant) a mortgage loan. Thus there is continuous interaction between life and non-life business.

The stability of the life premium/G.D.P. relationship, as shown, seems to indicate that two conflicting tendencies are exactly offsetting each other (and that life insurance is probably reaching a "saturation point".) The first is what we might consider as the "prosperity effect", (Subsumed under the prosperity effect might be a "substitution effect" whereby financial assets are substituted for tangible or physical assets, like jewelry). As incomes in an underdeveloped country rise from a previously very low level, saving via life insurance companies

TABLE 2.6 Correlation between Premium Income and G.D.P.

Premium Income/G.D.P.	Correlation Coefficient for Trinidad	Correlation Coefficient for Guyana
Life Premium Income/G.D.P.	0.88	0.92
Non-Life Premium Income/G.D.P.	0.30	0.96
Total Premium Income/G.D.P.	0.68	0.97
Total Premium Income per head/G.D.P.	0.51	n.a.

14. The I.I.R. for Trinidad when calculated would be even higher if (a) we had included "annuities" in our premium income figures (b) one or two companies had not failed to report each year (c) national income figures (alternatively G.N.P.) had been used instead of G.D.P. figures, even though a small amount of premium income is paid by people not residing in Trinidad; or 'permanent income' had been used (alternatively wages and salaries in life-premium/G.D.P. ratio) instead of G.D.P., given the contractual or long term nature of insurance saving.

(and to a lesser extent other financial intermediaries) should rise more than proportionately since people would be in a better position to make long term saving (i.e. they are now able to postpone consumption for a longer period, having surpassed the "subsistence level of income" situation). This tendency is being encouraged by the fact that income tax allowances on premium income paid by policy holders are fairly high; for example, in Guyana, premium income allowances were raised to $\frac{1}{6}$ of the policy holders' earned income in 1966 and to $\frac{1}{5}$ in 1968. In countries like Guyana, where the marginal income tax rate is said to be high even on moderate incomes, the holding of insurance policies, and the allowance on premium paid thereon, is said to be an attractive way of "evading excessive tax". A conflicting tendency is due to a reduction in the "risk effect". Now, people undertake contractual saving, via insurance companies, primarily in order to avert any risk to the receipt of present income (not being in a position to bear or absorb losses) or for bequeathing of future income to heirs. When their incomes rise, therefore, they should become less concerned with risk avoidance and adopt saving habits of a more liquid or semi-transactions nature e.g. bank depositing. If the positive prosperity effect more than offsets the negative risk effect, this would be reflected over time in a rise in the ratio of premium to G.D.P. In open economies, like those of the Caribbean, rapid inflation is not expected to accompany rapidly rising incomes and so there should be no bias against long term saving (e.g. insurance) or any added urge towards a more liquid form of saving. Nor should the current interest on bank deposits be especially favoured to the future interest on participating and equity linked insurance policies.

Re our fourth criterion for assessing the growth of insurance business—the size of assets—a grave statistical difficulty exists, in that although assets are probably the most important item for determining the economic impact of this institution, paradoxically they have the most deficient statistical coverage. Even in Trinidad, in the Annual Statistical Digest, asset figures appear only for life companies and these pertain only to investment balances in the country. In order to estimate the total assets figure for Trinidad, a life premium income/assets ratio of 1 : 10 and a non-life premium income/assets ratio of 1 : 7 were used. Table 2. 7 shows that total insurance assets for Trinidad, towards the end of the 1954-66 period, were not increasing as fast as previously, probably because G.D.P. itself was slowing down; in both 1955 and 1966, total assets as a percentage of G.D.P. were approximately 26 per cent and this shows the close relationship between the growth of insurance business and G.D.P. (Note that the size of the premium/assets ratios used probably inflates the true assets figures)

ASSET STRUCTURE OF INSURANCE COMPANIES

"We all know that life assurance began as risk sharing, and then developed into a risk bearing enterprise. As premiums were found to be too large, and as mortality rates improved, surpluses built up and the practice of paying bonuses was gradually adopted. In due course it became apparent that, with the help of tax relief on premiums, a with-

TABLE 2.7 Growth of Insurance Assets Compared with Growth in G.D.P. Trinidad–$m(E.C.)

Year	Percent Increase in G.D.P.	Local Assets of life insurance companies	Percent Increase in local assets	Total Life* and non-life assets	Percent Increase in total assets
1954		14.437		108.70	
1955	16.0	18.524	+28.3	130.70	20.2
1956	11.4	20.971	+12.2	139.32	6.6
1957	18.5	23.834	+14.6	159.28	14.3
1958	9.1	26.298	+10.3	181.70	14.1
1959	11.1	34.797	+32.3	216.83	19.3
1960	8.4	42.468	+22.0	263.78	21.7
1961	10.3	48.652	+14.6	283.92	7.6
1962	5.3	53.223	+9.4	276.58	2.6
1963	8.8	58.739	+10.4	307.05	11.0
1964	5.0	60.972	+3.8	312.73	1.8
1965	3.4	65.763	+7.9	330.11	5.6
1966	11.7	72.586	+10.4	336.56	2.0

* Estimated on basis of a premium/asset ratio of 1:10 for life assets and 1:7 for non-life assets.

Source: Computations based on data in previous tables.

profits endowment assurance was a good investment as well as providing life-cover, and a substantial amount of savings money flowed into the insurance companies."[15] A similar development can be traced to the fire, motor, marine, aviation and other business of non-life companies.

The aim of an insurance company is to maximize gain and to minimize losses. The assets which embody probably the greatest gain are "risky" assets and those which avoid the greatest loss are "safe" assets. Thus the company operates a sort of trade off policy (using probability analysis) until it arrives at a portfolio balance which gives it the highest mathematically expected yield from its entire holdings of assets.

Before arriving at its optimum asset portfolio, the insurance company is subject to a number of constraints. The first constraint is the legal requirement that an insurance company must be in a position

15. A. E. Bloomfield: "Presidential Address" delivered to the Faculty by the Deputy General Manager of the Standard Life Assurance Company, Trinidad, on 21st Oct., 1968.

to meet any legitimate claims, as set out in the contract. Thus an insurer's preference function is usually more diversified and at the same time more heavily weighted in favour of safe assets than most companies. But diversification enables the investor to escape almost all but the risk resulting from swings in economic activity. "It is common practice for investment counsellors to accept a lower expected return from defensive securities (those which respond little to changes in the economy) than they require from aggressive securities (which exhibit significant response.")[16] In metropolitan countries, before the War, little money was invested in equity shares (aggressive securities), because these were considered to be too risky. In the early post-war period, more shares began to appear in companies' portfolio, but it was accepted as prudent practice that bonuses should not be paid out of capital appreciation because of the supposed likelihood of intermittent (albeit infrequent) capital depreciation. However, a recent change in outlook has come about, because the sustained rise in equity share prices, and prices generally, since the War, had led people and companies to believe that both movements will continue indefinitely. Thus insurance companies typically hold government securities, mortgages and shares (or real estate) in ascending order of riskiness. A rise in holdings of shares (where default risk is great) may be offset by a corresponding rise in securities and a fall in mortgages.[17] However, today it is still true to say that insurance companies are risk averters, rather than risk lovers, although competition for savings will increasingly force them to be more adventurous.

A second constraining factor is the need for liquidity. Now the insurance company, like most financial institutions, for sound portfolio management, needs working balances with which to make routine expenditures (especially if revenue flows and expenditure flows are not easily synchronized) and also some degree of liquidity built into its asset portfolio in order to be able to make opportune switches from time to time for purposes of short-term gain. However, the peculiar characteristics of the insurance business may make necessary additional liquidity. Non-life insurance companies need to have a fairly liquid portfolio, because the timing of claims (e.g. fire) cannot be predicted with any great degree of accuracy. Life insurance companies also need additional liquidity to cope with sudden increases in deaths or surrendering of policies, although the degree of liquidity in their asset portfolio is usually less than that in non-life companies, because their liabilities are more long term.

A third constraining factor is that in some countries there are regulations concerning the holdings of certain assets as a proportion of total assets and in the case of certain loans, e.g. mortgages, a loan to value ratio is stipulated. However, the present day view is that given

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16. For an elegant exposition, based on the Tobin model, see W. F. Sharpe: "Capital Asset Prices: A theory of market equilibrium under conditions of risk," *Journal of Finance*, Sept., 1964.

17. See S. Rayama and K. Hamada: "Substitution and Complementarity in the Choice of Risky Assets," *Risk Aversion and Portfolio Choice*, D. Hester and J. Tobin (Eds.) John Wiley and Sons, 1967.

the condition of a high and sustained level of economic activity, private financial failures are remote and so safety and solvency regulations are unnecessary.[18]

A fourth constraint, pertaining particuarly to life insurance companies, is that these companies regard loans on policies as part of the insurance contract, and consequently consider these as a compulsory type of investment which they must undertake. Thus, the amount of money which insurance companies consider investing in the different markets according to their assessment of the yields, is the difference between the surplus of income over expenditure and the largest size of expected policy loans. There are two other reasons why life insurance companies regard policy loans as a constraining factor. "First policy loans are small in amount and are therefore very costly to administer. Their net yield is far below the interest rate charged and is not particularly attractive relative to alternative investment media. Second, and far more important, a policy loan is frequently the prelude to a lapse of the policy, and insurance companies are interested in keeping policies in force."[19]

There are certain operational techniques, peculiar to the industry, that insurance companies employ in trying to implement their investment policy. Life insurance companies frequently adopt a principle of "matching" the time profile of their liabilities structure with a certain maturity pattern in their asset portfolio. Thus, because their ordinary life and endowment liabilities are long term, insurance companies tend to prefer mortgages and long term securities to short term securities (moreover, long-term securities carry a higher yield than short-term securities). The reason for preferring assets at the far end of the liquidity spectrum (e.g. a 20 year security rather than four consecutive 5 year securities) is that the amount of the insurance premium is fixed for any individual holding a policy and the size of the premium is based on the interest expected from investments; in our example, therefore, choice of the four consecutive 5 year securities leaves the insurance company wide open to movements in the price (and so rate of interest) of these securities over time. "The unique risk of such a contract derives from the circumstance that the interest rate to be earned in the future on premium receipts, is guaranteed today. This income risk is one of the paramount aspects of the investment situation of life insurance companies."[20]

Non-life insurance companies do not adopt the matching technique because their liabilities are not as long term and because the premium charged is dependent, not on investment income, but on risk or probability of occurrence of a mishap. Thus the asset structure of

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18. See T. Gies, T. Mayer and E. Ettin: "Portfolio regulations and policies of financial intermediaries," *Private Financial Institutions. Op. Cit.*

19. J. B. Cohen and E. D. Zinbarg: *Investment Analysis and Portfolio Management*, Richard C. Irivin, INC., Illinois, 1967. p. 703.

20. L. S. Wehrle: "Life Insurance Investment: The experience of Four companies", in *Studies of Portfolio Behaviour.* D. Hester and J. Tobin (Eds.) John Wiley & Sons, 1967. p. 192.

non-life companies tends to be more liquid (and to contain more securities) than that of life companies and the degree of liquidity varies between fire, motor, marine and accident companies according to the nature of their business. Generally, because "insurance exposure" (as measured by the ratio of annual premium to capital and surplus) is greater in non-life than life companies, the degree of "investment exposure" (as measured by the ratio of risky assets to capital and surplus) tends to be less.

Table 2.8 shows the distribution of local assets in the portfolio of life insurance companies in Trinidad. It shows that mortgages are not only the largest single item in the asset portfolio, but have increased steadily from 40.5% of total assets in 1954 to 46.4% in 1966. On the other hand, real estate holdings have fallen as a percentage of total assets. Since customers' default on mortgage loans is the main source of these real estate holdings, this fall might be due to mortgage loans applications being more carefully scrutinized, customers being more wary of "over-reaching" themselves or incomes in Trinidad being more stabilized. Defaults may be due to stricter adherence to the custom of restricting mortgage loans to 60 to 70% of the value of the property, with resultant second mortgage problems. It is also noticeable that policy loans have fallen significantly, and since such loans have in the past been used primarily to repay debt on goods like motor cars and expensive household appliances,or to make down payment on a house, the greater availability and easier terms of hire purchase facilities, and possibly bank loans, might account for this steady fall; or more likely, the fall might be due to the increased incidence of surrenders (and lapses) of life insurance policies. Table 2.9, on the asset portfolio of local insurance companies in Guyana, shows that mortgage loans held approximately the same relative portfolio position as in Trinidad, but government securities are probably higher and policy loans lower, because non-life companies (greater risk averters than life companies) are included.

Published information is not available as to whether the average maturity or size of mortgage held by insurance companies was increasing or decreasing over time. We might expect the size of mortgages to be increasing because of increases in the cost (and price) of housebuilding but we do not think the mortgage size was increasing faster than the value of total mortgages, otherwise the number of people receiving mortgages would fall. In fact, there has been a rapid increase in the demand for mortgages, owing to the universal desire for better housing (stimulated in some territories by the income tax allowance on interest paid on mortgage loans for new property.) Life insurance companies, themselves, not only find mortgages suitable because of the matching principle, but also because the mortgage is relatively capital safe and high yielding. It is difficult to say whether the small portfolio fluctuations originate in the demand side or the supply side. It is also difficult to judge from the data whether a "normal distribution ratio" exists i.e. whether companies consciously try to arrive at some definite pattern of distribution between assets which they believe to be normal. For example, is the size of securities holdings determined by (a) traditional rate of return theory (b) the need

TABLE 2.8 Distribution of Local Assets in Portfolio of Life Companies—Trinidad—$000 (E.C.)

Year	Total	Mortgage Loans	% of Total	Policy Loans	% of Total	Real Estate	% of Total	All* Other	% of Total
1954	14,437	5,583	40.5	4,572	31.7	1,407	9.7	2,605	18.1
1955	18,524	7,757	41.9	5,238	28.3	1,935	10.4	3,594	19.4
1956	20,971	8,799	42.0	6,224	29.7	2,902	13.8	3,046	14.5
1957	23,834	10,576	44.4	7,202	30.2	2,835	11.9	3,221	13.5
1958	26,298	13,191	50.2	7,991	30.4	2,114	8.0	3,002	11.4
1959	34,797	15,203	43.7	8,862	25.5	2,190	6.3	8,542	24.5
1960	42,466	18,845	44.4	9,720	22.9	2,216	5.2	11,685	27.5
1961	48,652	21,504	44.2	11,248	23.1	1,474	3.0	14,426	29.7
1962	53,223	23,866	44.8	12,443	23.4	1,658	3.1	15,256	28.7
1963	58,739	26,579	45.2	13,339	22.7	2,868	4.9	15,952	27.2
1964	60,972	27,236	44.7	13,870	22.6	3,342	5.5	16,614	27.2
1965	65,763	30,377	46.2	14,527	22.1	3,552	5.4	17,307	26.3
1966	72,586	33,686	46.4	15,976	22.0	3,736	5.1	19,188	26.5

* Includes Government Securities

Source: Computations based on figures obtained from the Annual Statistical Digest, C.S.O., Trinidad and Tobago.

TABLE 2:9 Distribution of Local and Foreign Assets in Asset Portfolio of Local Insurance Companies, Guyana $m(E.C.)

	1966	1967
Total Assets	46.5	50.0
Local Deposits	0.992	0.989
Percent of Total	2.1	1.9
Foreign Deposits	0.445	0.261
Percent of Total	1.0	0.5
Local Treasury Bills	0.459	0.630
Percent of Total	1.0	1.2
Foreign Treasury Bills	0.049	—
Percent of Total	0.1	—
Local Securities	4.8	5.0
Percent of Total	10.2	10.0
Foreign Securities	10.3	10.9
Percent of Total	22.1	22.0
Local Mortages and Real Estate	17.0	18.9
Percent of Total	36.6	37.7
Foreign Mortgages and Real Estate	3.1	3.3
Percent of Total	6.7	6.5
Local Other Loans	3.4	2.4
Percent of total	7.4	5.1
Foreign Other Loans	3.7	2.6
Percent of total	7.9	5.1
Fixed Assets	1.4	1.5
Percent of total	2.9	3.0
Local other assets	0.790	0.875
Percent of total	1.7	1.7
Foreign Other Assets	0.467	0.452
Percent of total	1.0	0.9
Other	0.916	0.967
Percent of total	2.0	1.9

SOURCE: Computations based on figures obtained from the Annual Reports, Bank of Guyana

to spread risks and diversify in order to maintain some portfolio balance (c) the need for liquidity (d) the honouring of a moral commitment to the government or (e) the fact that some asset has to act as a residual item?

Not only is the total volume of assets of insurance companies important, but also the local component of those assets. Table 2.10 shows that about two-thirds of the assets accumulated between 1954 and 1966 by life insurance companies in Trinidad were local and as much as one-third was foreign, although towards the end of the period the percentage of foreign assets held fell decisively. It would be useful to find out whether the considerable foreign component is part of the general attempt to diversify (this time geographically), is due to differences in interest rates, or, as might be the case for securities, is an attempt to seek greater liquidity owing to the lack of an effective local money market; only partly can it be due to an attempt to match foreign liabilities with foreign assets. Table 2.9, which was previously referred to, shows the local (Guyana) insurance companies' holdings of assets that are local and foreign. In 1967, of the 50 million of assets, $14,405,000 or 29% of total assets was invested abroad, with foreign securities being 75% of foreign investment (the rest of foreign investment being mainly policy loans and mortgage loans.)

Table 2.11 was drawn up in order to determine whether there are any significant differences between the asset portfolios of local and foreign companies. So many insurance companies in Jamaica fail to report that it is difficult to come to any definitive conclusions. However, it is generally believed that foreign companies hold more foreign securities than local companies and offer less mortgage loans and policy loans. There may also be operational differences between Canadian, British and American insurance companies operating in the Caribbean.

It is regretable, also, that data are not available which distinguish between big insurance companies and small insurance companies. Such data would have made it possible to decide whether, as a result of their size and the capacity to absorb small absolute losses, big companies were in a position to hold riskier portfolios; data would also help us to determine whether there is a natural market tendency towards competition or monopoly. At the moment, insurance companies behave somewhat collusively (possibly due to the leadership "dictates" of a few large companies) with respect to their premium rates and lending rates.

It is also noticeable that equities hardly appear in the asset portfolio of insurance companies in the Caribbean. We believe that the virtual non-holding of equities is due more to a lack of supply (and an effective secondary market) rather than the product of risk aversion on the part of insurance companies. (This non-holding of equities probably makes insurance premiums higher than they ought to be.) Therefore, insurance companies in the Caribbean probably think that the pattern of asset holdings in their portfolio is not really optimum. The insurance companies' view of optimality may not necessarily be the same as that of policy holders, and the private policy holders' view of

TABLE 2.10 Accretions to Holdings of Local and Foreign Assets by Life Insurance Companies in Trinidad $000 (E.C.)

Year (1)	Total Income (2)	Total Expenditure (3)	Funds available for investment (4)	Income (5)	Accretions to Local Investment (6)	% of Total Accretions (7)	Accretions to foreign Investment (8)	Total Accretions as % of Total Income (9)
1954	8, 564	4, 321	4, 243	49. 5	2, 075	48. 9	2, 168	51. 1
1955	10, 282	5, 145	5, 137	49. 9	4, 087	79. 5	1, 050	20. 5
1956	11, 430	6, 383	5, 047	44. 1	2, 447	48. 4	2, 600	51. 6
1957	12, 884	6, 942	5, 942	46. 1	2, 863	48. 1	3, 079	51. 9
1958	14, 907	8, 541	6, 366	42. 7	2, 464	38. 7	3, 902	61. 3
1959	18, 727	10, 750	7, 977	42. 6	8, 499	106. 5	– 522	–6. 5
1960	22, 789	12, 008	10, 781	47. 3	7, 669	71. 1	3, 112	28. 9
1961	24, 894	15, 220	9, 674	38. 9	6, 186	63. 9	3, 488	36. 1
1962	23, 323	16, 337	6, 989	30. 0	4, 571	65. 4	2, 415	34. 6
1963	26, 657	17, 093	9, 564	35. 9	5, 516	57. 7	4, 048	42. 3
1964	26, 520	18, 973	7, 547	28. 5	2, 233	29. 6	5, 314	70. 4
1965	28, 152	20, 130	8, 022	28. 5	4, 791	59. 7	3, 231	40. 3
1966	28, 476	19, 986	8, 490	29. 9	6, 823	80. 4	1, 667	19. 6

Source: Computations are based on figures obtained from the Annual Statistical Digest, C.S.O. Trinidad & Tobago

TABLE 2.11 Distribution of Assets of Local and Foreign Insurance Companies, Jamaica $m. (E.C.)

	Year	Total Assets	Government Securities	Other Securities	Treasury Bills	Loans on Mortgages	Loans on Policies	Cash	Other Assets
LOCAL	1963	22.56	3.36	9.60	—	4.80	4.80	0.014	0.096
	1964	17.28	3.60	0.24	—	6.72	6.24	0.576	0.48
	1967	25.92	7.44	0.24	—	9.60	7.68	0.221	0.720
(Percentages—Local)	1963	100.0	14.9	42.5	—	21.3	21.3	—	—
	1964	100.0	20.8	1.4	—	38.9	36.1	—	2.8
	1967	100.0	28.7	0.9	—	37.0	29.6	0.1	2.8
FOREIGN	1962	69.12	13.92	12.96	0.019	24.96	7.68	1.354	8.16
	1963	84.48	16.80	22.56	0.370	27.36	13.44	1.267	2.64
	1964	93.12	19.68	16.32	0.614	30.24	16.80	3.158	6.24
	1965	100.32	20.64	16.80	0.542	33.60	18.24	2.196	8.40
	1966	122.40	28.32	21.12	0.370	37.92	20.16	2.544	11.76
	1967	137.76	32.16	24.0	1.378	42.24	23.52	4.152	10.32
(Percentages-Foreign)	1962	100.0	20.1	18.8	0.1	36.1	11.1	2.0	11.8
	1963	100.0	19.9	26.7	0.5	32.4	15.9	1.5	3.1
	1964	100.0	21.1	17.5	0.7	32.5	18.1	3.4	6.7
	1965	100.0	20.6	16.7	0.5	33.5	18.2	2.2	8.3
	1966	100.0	23.1	17.3	0.3	31.0	16.5	2.1	9.7
	1967	100.0	23.3	17.4	1.0	30.7	17.1	3.0	7.5

18 foreign agencies included. *Source:* Monetary Statistics, Jamaica.

optimality may depend on whether they are satisfied with the volume (and conditions) of mortgage and policy loans; and the government's view may hinge on how great a volume of securities insurance companies are willing to accept and how high a price they are willing to pay for securities of varying maturities. Later in this study, we shall give the economist's view as to the degree of impact the operations of insurance companies have on the economies of the Commonwealth Caribbean and what portfolio and other adjustments are needed to approach nearer the social optimum.

LIABILITIES STRUCTURE OF INSURANCE COMPANIES

There is a marked difference between the liabilities structure of life and non-life companies, because of differences in obligations to their policy holders. Life insurance companies need to "accumulate" huge amounts of funds, because "life insurance policies are essentially contracts for the future delivery of specific amounts of dollars at specified dates in the future in return for agreed inflows of dollars in a prescribed manner through time." [21] Table 2. AI therefore shows the need for domestic life insurance companies in Guyana to increase their "insurance fund" at some rate corresponding to the rate of increase in premium income. Life insurance companies also need to build up a reserve fund to hedge against a rise in mortality rates etc. over and above that previously estimated by the actuary. However, for statistical reasons, this reserve fund does not need to rise at the same rate as premium and over time its rate of increase should be falling. If the difference between total income and total expenditure is greater than the addition that needs to be made to the insurance fund and reserve fund for that year, the "surplus" can be paid out as dividend.

The liabilities structure of non-life insurance companies is different in that the condition for the contract is that the premiums shall not be repaid by the company at a set future date; payment is only made when an accident etc. claim is made and those not making a claim do not get a refund (only a small rebate). Thus there is no need for an accumulated or insurance fund, and only a reserve fund is held as is shown in Table 2. AII. This reserve fund, called a general reserve fund, has two parts—a technical reserve fund for purposes which we have been referring to and a contingency reserve for calamities that might occur over and above that predicted by the actuary. Table 2. 12 shows that between 1945 and 1968 both the premium income and the combined insurance and reserve fund of domestic life companies increased eight-fold. However, during the same period, the reserve fund of non-life insurance companies increased at a slower rate than premium income owing perhaps to economies of scale in risk taking. In keeping with the theory of the insurance firm, we would expect the contingency reserve fund for non-life companies to be held in a fairly liquid form in order to make it easy and convenient to supplement when necessary the stream of maturing securities of the technical reserve fund that

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21 L. Wehrle: *Op. Cit.*, p. 192.

TABLE 2.12 A Comparison Between the Growth of Premium Income and Insurance and Reserve Funds for Domestic Companies—Guyana $m (E.C.)

Year	Premium income Life	Rate of Increase	Insurance Fund Life	Rate of Increase	Insurance Fund and Reserve Fund, Life	Rate of Increase	Premium income Non-life	Rate of Increase	Reserve Fund Non-life	Rate of Increase
1945	0.698		5.2		5.6		0.576		1.4	
1950	1.092	56.4	7.5	44.2	7.9	41.1	0.891	23.4	2.0	42.9
1955	1.617	48.1	12.5	66.7	13.3	68.4	1.355	52.1	2.4	20.0
1956	1.754	8.5	14.0	12.0	14.8	11.3	1.510	11.4	2.6	8.3
1957	1.957	11.6	15.3	9.3	16.4	10.8	1.628	7.8	2.7	3.8
1958	2.128	8.7	16.9	10.5	18.0	9.8	1.810	11.2	2.9	7.4
1959	2.258	6.1	18.6	10.1	19.7	9.4	1.928	6.5	3.2	10.3
1960	2.460	8.9	20.6	11.8	21.7	10.2	2.127	10.3	3.5	9.4
1961	2.579	4.8	22.6	9.7	23.7	9.2	2.552	20.0	3.8	8.6
1962	2.620	1.6	23.7	4.9	25.2	6.3	2.564	0.4	3.9	2.6
1963	2.715	3.6	25.6	8.0	27.1	7.5	2.100	–18.1	4.2	7.7
1964	2.777	2.3	27.1	5.9	28.5	5.2	2.203	4.9	4.4	4.8
1965	3.155	13.6	29.0	7.0	30.9	8.4	2.299	4.4	4.6	4.5
1966	3.762	19.2	30.9	6.6	32.9	6.5	2.564	11.5	5.0	8.7
1967	4.711	25.2	33.6	8.7	35.6	8.2	2.851	11.2	5.5	10.0

Source: Computations based on data in previous tables.

would be used to satisfy claims. (In fact, non-life companies tend to hold more securities and less mortgages than life companies.) Thus, although insurance companies need to have a reserve or precautionary fund, this reserve is not held in a cash form and it tends to be fully invested at all times.[22]

Table 2.13 is an attempt to actually determine the stability of the liabilities structure of domestic life and non-life insurance companies in Guyana. It shows that life companies, between the period 1945 to 1968, tried to keep their reserve fund fairly stable at 5 to 5½% of total liabilities, irrespective of the size of total liabilities. It also shows that life companies increase their insurance fund at about the same rate as the increase in total income since total income as a percentage of the insurance fund is fairly constant around 18%. Total claims per year, as a percentage of the insurance fund, is also fairly constant at around 5 and 5½% (slightly higher towards the end of the period), suggesting perhaps an 18 to 20 year time lag before the average new policy matures. For non-life companies, the reserve (general) fund has been rising steadily, being 31% of total liabilities in 1945 and 45.0% of total liabilities in 1968, due perhaps to a rising rate of claims, motor vehicle in particular.

INCOME AND EXPENDITURE OF INSURANCE COMPANIES

The income and expenditure statement is another useful source of information for understanding the operations of insurance companies and for trying to determine how efficient insurance companies really are.

Total income consists of premium income, investment income and a miscellaneous category, called "other income". The rate of growth of premium income would depend partly on the growth in the number of policies and partly on the differences in the rate of growth of the various types of policies e.g. if endowment policies increased faster than ordinary or whole of life policies (and the sum insured is the same), then premium income would rise at a faster rate. The rate of increase in investment income is related partly to the rate of increase in premium income funds, and partly to the rates of interest on various assets held and the changes in the portfolio distribution or combination in which these assets are held.

Investment income is related to premium income because, as we said earlier, the size of the fixed rate premium that the insurance company demands is related to its expected income from investment. Table 2.14 attempts to show the relationship between investment income and premium income and between the rates of increase of premium income and investment income for life and non-life companies in Guyana and

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22 To highlight the differences and similarities with the traditional non-financial firm, see E. L. Whalen: "A Rationalization of the Precautionary Demand for Cash", *Quarterly Journal of Economics*, May 1966; also see S. C. Isiang: "The Precautionary Demand for Money: An Inventory Theoritical Analysis," *Journal of Political Economy*, January/February, 1969.

TABLE 2.13 Reserve Fund as a Percentage of Total Liabilities and Total Claims as a Percentage of Insurance Fund—Guyana $ m (E.C.)

	LIFE (Domestic)						NON—LIFE (Domestic)				
Year	Total Liabilities	Reserve Fund	Reserve Fund as a % of Total Liabilities	Total Income	Insurance Fund	Total Income as a % of Insurance Fund	Total Claims	Total Claims as a % Insurance Fund	Total Liabilities	Reserve Fund	Reserve Fund as a % of Total Liabilities
1945	6.2	0.4	6.5	0.968	5.2	18.6	0.256	4.9	4.5	1.4	31.1
1950	9.1	0.4	4.4	1.453	7.5	19.4	0.568	7.6	6.4	2.0	31.3
1955	14.5	0.8	5.5	2.307	12.5	18.5	0.523	4.2	7.1	2.4	33.8
1956	16.2	0.8	4.9	2.450	14.0	17.5	0.648	4.6	7.6	2.6	34.2
1957	17.8	1.1	6.1	2.781	15.3	18.2	0.808	5.3	7.9	2.7	34.2
1958	19.5	1.1	5.6	3.110	16.9	18.4	0.938	5.6	7.9	2.9	36.7
1959	21.1	1.1	5.2	3.303	18.6	17.8	0.910	4.9	8.4	3.2	38.1
1960	23.2	1.1	4.7	3.626	20.6	17.6	0.827	4.0	8.9	3.5	39.3
1961	25.4	1.1	4.3	3.910	22.6	17.3	1.245	5.5	9.5	3.8	40.0
1962	27.5	1.5	5.5	4.051	23.7	17.1	1.411	6.0	9.8	3.9	39.8
1963	29.1	1.5	5.2	4.209	25.6	16.4	1.505	5.9	10.7	4.2	39.3
1964	30.9	1.4	4.5	4.384	27.1	16.2	1.515	5.6	10.2	4.4	43.1
1965	32.7	1.9	5.8	4.927	29.0	17.0	1.709	5.9	10.6	4.6	43.4
1966	35.2	2.0	5.7	5.629	30.9	18.2	2.128	6.9	10.9	5.0	45.9
1967	38.2	2.0	5.2	6.848	33.6	20.4	2.152	6.4	11.7	5.5	47.0
1968	40.4	1.3	3.2	7.979	36.8	21.7	2.027	5.5	12.2	5.6	45.9

Source: Computations based on data in previous tables.

Trinidad. Both premium income and investment income show some degree of fluctuation. Investment income as a ratio of premium income is also fluctuating, probably because (a) fluctuations of premium income and investment income reinforce one another and (b) there are varying time lags before increases in premium income are invested and yield income. There is little correlation between premium income and investment income in the short run and therefore the theory that premium rates are set in accordance with expected income may not be applicable to very short policies. Paradoxically, there may not also be very close correlation in the very long run between premium rates and investment income on whole of life policies because of the difficulty in predicting what the rate of interest on securities, mortgages, etc. will be in the very distant future. (The distinctly lower investment income/premium income ratio for Trinidad is probably because investment income refers to "investment in the country", only).

Premium income received by life companies in the Caribbean tends to be mainly from ordinary life policies and endownment policies, as is shown in Table 2. AIII for Trinidad. For non-life companies, fire and motor vehicle policies tend to dominate, as shown in Table 2. 15, below:

Insurance companies' expenditure consists of two broad items (plus taxation[23]): (1) claims and (2) selling (commission), management and other expenses.[24] Table 2. 16 shows that total expenditure has been moving very erratically, rising in most years but falling in some. Life expenditure has shown a less uneven rising tendency than non-life (as is expected) and is less unstable in Trinidad than in Guyana. (Fluctuations in Guyana in the early 1960s might be due to civil disturbances). Total income has also fluctuated quite a lot, although total expenditure has probably fluctuated more than total income. Table 2. 17 shows that premium income is a fairly stable percentage of total income and that premium income is a higher percentage of total income for non-life than for life companies, because non-life assets tend to be more liquid (or safe) and so lower yielding.

Table 2. 17 also shows that, for life companies in Guyana and Trinidad claims paid as a percentage of premium income have been rising appreciably,[25] whereas for non-life companies there is no upward or

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23 In considering total expenditure we include taxes paid, merely because this is the way it is presented in the balance sheet of insurance companies: however this method of treatment really exaggerates the size of total expenditure and consequently some of our calculations are not exactly "true" figures e.g. "residual income" is, as a result, probably too low.

24 Insurance companies really incur three costs: claims, expenses and the interest that has to be credited to policy holders' reserve.

25 Nevertheless, claims as a percentage of total income may not be excessive in the Caribbean. In the USA in 1959, 50% of total income of life companies was used to make benefit payments, whereas in Guyana it was just over 40% and in Trinidad under 40%, on average. See E. Keith: "The Impact of Federal Taxation on the Flow of Personal Savings through Investment Intermediaries", *Private Financial Institutions (Op. Cit.)*

TABLE 2.14 Rates of Increase in Premium Income and Investment Income and Ratio of Investment Income to Premium Income Guyana and Trinidad $m (E.C.)

		NON-LIFE					LIFE				
	Year	Premium Income	Rate of Increase in premium Income	Investment Income	Rate of Increase in investment Income	Investment Income as a ratio of premium income	Premium Income	Rate of Increase in premium Income	Investment Income	Rate of increase in investment Income	Investment Income as a ratio of premium Income
GUYANA (Domestic)	1945	0.576		0.174		0.302	0.698		0.231		0.331
	1950	0.891	+54.7	0.219	+25.9	0.246	1.092	+56.4	0.357	+54.5	0.327
	1955	1.355	+52.1	0.283	+29.2	0.209	1.617	+48.1	0.615	+72.3	0.380
	1956	1.510	+11.4	0.303	+ 7.1	0.201	1.754	+ 8.5	0.681	+10.7	0.388
	1957	1.628	+ 7.8	0.329	+ 8.6	0.202	1.957	+11.6	0.811	+19.1	0.414
	1958	1.810	+11.2	0.352	+ 7.0	0.194	2.128	+ 8.7	0.970	+19.6	0.456
	1959	1.928	+ 6.5	0.360	+ 2.3	0.187	2.258	+ 6.1	1.032	+ 6.4	0.457
	1960	2.127	+10.3	0.394	+ 9.4	0.185	2.460	+ 8.9	1.152	+11.6	0.468
	1961	2.552	+20.0	0.424	+ 7.6	0.166	2.579	+ 4.8	1.311	+13.8	0.508
	1962	2.564	+ 0.5	0.513	+21.0	0.200	2.620	+ 1.6	1.415	+ 7.9	0.540
	1963	2.100	–18.1	0.473	– 7.8	0.225	2.715	+ 3.6	1.487	+ 5.1	0.548
	1964	2.203	+ 4.9	0.634	+34.0	0.288	2.777	+ 2.3	1.598	+ 7.5	0.575
	1965	2.299	+ 4.4	0.648	+ 2.2	0.282	3.155	+13.6	1.722	+ 7.8	0.546
	1966	2.654	+11.5	0.599	– 7.6	0.234	3.762	+19.2	1.820	+ 5.7	0.484
	1967	2.851	+11.2	0.616	+ 2.8	0.216	4.711	+25.2	2.086	+14.6	0.443
	1968	3.237	+13.5	0.654	+ 6.2	0.202	5.559	+18.0	2.388	+14.5	0.430

TABLE 2.14—*Continued*

		NON-LIFE					LIFE				
	Year	Premium Income	Rate of Increase in premium Income	Investment Income	Rate of Increase in investment Income	Investment Income as a ratio of premium income	Premium Income	Rate of Increase in premium Income	Investment Income	Rate of increase in investment Income	Investment Income as a ratio of premium Income
TRINIDAD*	1957	6.138		0.194		0.032	11.632		1.252		0.108
	1958	6.884	+12.2	0.211	+ 8.8	0.031	13.352	+14.8	1.555	+24.2	0.116
	1959	7.898	+14.7	0.241	+14.2	0.031	16.155	+21.0	2.572	+65.4	0.159
	1960	9.400	+19.0	0.286	+18.7	0.030	19.798	+22.6	2.991	+16.3	0.151
	1961	10.488	+11.6	0.337	+17.8	0.032	21.051	+ 6.3	3.843	+28.5	0.183
	1962	11.395	+ 8.6	0.370	+ 9.8	0.032	19.682	— 6.5	3.640	— 5.3	0.185
	1963	12.126	+ 6.4	0.505	+36.5	0.042	22.217	+12.9	4.440	+22.0	0.200
	1964	12.617	+ 4.0	0.767	+51.9	0.061	22.442	+ 1.0	4.016	— 9.5	0.179
	1965	12.260	— 2.8	0.610	—20.5	0.050	23.811	+ 6.1	4.341	+ 8.1	0.182
	1966	10.965	—10.6	0.497	—18.5	0.045	24.056	+ 1.0	4.508	+ 3.8	0.187

* Investment Income includes a not insignificant income item called "other revenue"

1965 and 1966 Non-Life figures are provisional, for Trinidad.

Source: Computations based on data in previous tables.

TABLE 2.15 Relative Sizes of Premiums for Types of Non-Life Business for Foreign Companies. Trinidad. 1965* $ (E.C.)

Type of Business	Premium Paid	% of Total
Fire and Extraneous Perils	2,254,076	32.0
Accident Insurance (Personal)	709,229	10.1
Employers' Liability and Workmen Compensation	1,097,378	15.6
Marine Insurance	335,122	4.7
Motor Vehicle Insurance	2,391,835	33.9
Air Insurance	5,020	0.1
Other	251,713	3.6
TOTAL	7,044,373	100.0

* Slight variation in the number of companies reporting.

Source: Special Request, Statistical Department, Trinidad.

downward tendency (but only a slight fluctuation around the mean). However, this situation does alter for life companies in Guyana when we calculate claims as a percentage of total income (perhaps because investment income has risen appreciably) whereas the situation does not alter for Trinidad's life companies. Table 2.18 shows that death claims as a percentage of total claims (excluding surrenders) has risen appreciably and endowment (matured claims) as a percentage has fallen as much; surrenders have also been rising dramatically, although in the last two years of the 1957-66 period this was not the case for Trinidad.

Table 2.18 also indicates that death and endowment claims are both higher percentages of total claims (excluding surrenders) in Guyana than in Trinidad but that the reverse is true for surrenders. In Guyana, endowment is the biggest type of claim and surrenders second in importance. In Trinidad, during 1957-66 period, surrenders and endowments were the major types of claim. The figures have certain implications for insurance theory; one implication is that since endowment and surrenders collectively are such a major part (and deaths a relatively minor part) of total claims, ordinary statistical calculations are more important than pure actuarial (mortality) considerations. There is also an important implication for the theory of insurance saving; since the rate of surrenders is so high, especially for Trinidad, and since endowment policies have grown to such prominence, it means that policy holders now look upon insurance saving as a medium term rather than a long term form of saving. These phenomena may be peculiar to the Caribbean since they are hardly ever emphasized in the traditional type text-book.[26]

[26] e.g. no mention in A. Robichek and A. Coleman: *Management of Financial Institutions, Notes and Cases*, Holt, Rhinehart and Winston, 1967.

TABLE 2.16 Percentage Rate of Increase of Total Expenditure, Total Income, "Underwriting Profit" and Premium Income, Guyana and Trinidad.

		NON-LIFE				LIFE			
	Year	Total expenditure	Total Income	Under-Writing Profit	Premium Income	Total expenditure	Total Income	Under-Writing Profit	Premium Income
GUYANA (Domestic)	1945								
	1950	–44.5	30.0	142.8	23.4	342.2	50.1	14.7	56.4
	1955	56.3	34.2	32.1	52.1	–42.7	58.8	98.3	38.9
	1956	19.1	10.5	48.1	11.4	5.4	6.2	6.9	8.5
	1957	–3.2	7.9	86.0	7.8	21.6	13.5	7.0	11.6
	1958	11.9	10.5	2.9	11.2	23.2	11.8	1.4	8.7
	1959	4.4	5.9	14.9	6.5	16.5	6.2	5.3	6.1
	1960	14.6	10.1	–13.8	10.3	–4.3	9.8	29.1	8.9
	1961	19.5	18.2	9.0	20.0	25.8	7.8	–10.4	4.8
	1962	31.5	4.5	–205.0	0.4	28.0	3.6	31.1	1.6
	1963	–37.3	–16.6	217.6	–18.1	0.3	3.9	15.0	3.6
	1964	19.3	5.8	–63.9	4.9	4.9	4.2	2.3	2.3
	1965	–5.6	3.7	161.8	4.4	10.0	12.4	19.1	13.6
	1966	12.5	13.1	16.8	11.5	22.4	14.2	–3.4	19.2
	1967	9.1	10.5	18.7	11.2	14.9	21.7	40.2	25.2
	1968	12.0	9.8	–2.2	13.5	0.4	16.5	52.7	18.0
TRINIDAD	1957								
	1958	81.4	12.0	–113.0	12.2	23.0	15.7	7.1	14.8
	1959	–28.1	14.7	106.2	14.7	25.9	25.6	25.3	21.0
	1960	29.8	19.0	–1.2	19.0	11.7	21.7	35.2	22.6
	1961	44.7	11.7	–69.6	11.6	36.7	9.2	–10.3	6.3
	1962	–12.7	8.7	260.1	8.6	7.3	–6.3	–27.8	–6.5
	1963	14.3	7.4	–12.3	6.4	4.6	14.3	36.9	12.9
	1964	–1.9	6.0	35.0	4.0	11.0	–5.1	–21.1	1.0
	1965	2.6	– 5.1	–21.3	– 2.8	6.1	6.2	6.3	6.1
	1966	–7.0	–14.1	–24.9	–10.6	0.6	14.6	6.7	1.0

Notes: 1965 and 1966 Non-life figures for Trinidad are provisional.

Source: Computations based on (a) Special Request to Companies in Guyana (b) Annual Statistical Digest, Trinidad.

TABLE 2.17 Claims Paid as a Percentage of Premium Income and Premium Income as a Percentage of Total Income, Guyana and Trinidad. $m (E.C.)

		LIFE						NON-LIFE					
	Year	Total Income	Premium Income	Premium Income as % of Total Income	Claims Paid	Claims Paid as % of Premium Income	Claims Paid as % of Total Income	Total Income	Premium Income	Premium Income as % of Total Income	Claims Paid	Claims Paid as % of Premium Income	Claims Paid as % of Total Income
GUYANA (Domestic)	1945	0.968	0.698	72.1	0.256	36.7	26.4	0.940	0.576	61.3	1.121	194.6	119.3
	1950	1.453	1.092	75.2	0.568	52.0	39.1	1.122	0.891	79.4	0.140	15.7	12.5
	1955	2.307	1.617	70.1	0.523	32.3	22.7	1.640	1.355	82.6	0.266	19.6	16.2
	1956	2.450	1.754	71.6	0.648	36.9	26.4	1.813	1.510	83.3	0.311	20.6	17.2
	1957	2.781	1.957	70.4	0.808	41.3	29.1	1.957	1.628	83.1	0.387	23.8	19.8
	1958	3.110	2.128	68.4	0.938	46.1	30.2	2.162	1,810	83.7	0.510	28.2	23.6
	1959	3.303	2.258	68.4	0.910	40.3	38.0	2.290	1.928	84.2	0.439	22.8	19.2
	1960	3.626	2.460	67.8	0.827	33.6	30.3	2.522	2.127	84.3	0.590	27.3	22.9
	1961	3.910	2.579	66.0	1.245	48.3	39.1	2.982	2.552	85.6	0.880	34.5	29.5
	1962	4.051	2.620	64.7	1.411	53.9	51.2	3.116	2.564	82.3	1.966	76.7	63.0
	1963	4.209	2.715	64.5	1.505	55.4	48.3	2.599	2.100	80.8	0.478	22.8	18.3
	1964	4.384	2.777	63.3	1.515	54.6	47.1	2.751	2.203	80.1	0.701	31.8	25.4
	1965	4.927	3.155	64.0	1.709	54.5	43.6	2.852	2.299	80.6	0.526	22.9	18.4
	1966	5.629	3.762	66.8	2.128	56.6	45.7	3.226	2.564	79.5	0.632	24.6	19.5
	1967	6.848	4.711	68.8	2.152	45.7	41.7	3.564	2.851	80.0	0.745	26.1	20.9
	1968	7.979	5.559	69.7	2.027	36.5	34.9	3.914	3.237	82.7	0.882	27.2	22.5
TRINIDAD	1957	12.884	11.632	90.3	3.882	33.4	30.1						
	1958	14.907	13.352	89.6	4.671	35.0	31.3						
	1959	18.727	16.155	86.3	5.811	36.0	31.0						
	1960	22.789	19.798	86.9	6.327	32.0	27.7						
	1961	24.894	21.051	84.6	8.543	40.6	34.3						
	1962	23.323	19.682	84.4	9.571	48.6	41.0						
	1963	26.657	22.217	83.3	9.401	42.3	35.2						
	1964	26.520	22.442	84.6	10.541	47.0	39.7						
	1965	28.152	23.811	84.6	10.801	45.4	38.3						
	1966	28.564	24.056	84.2	10.621	44.2	37.1						

Source: Computations based on:
(a) Special Request to Companies in Guyana.
(b) Annual Statistical Digest, Trinidad.

TABLE 2.18 Changes in Death and Endowment Claims in Guyana and Trinidad $m (E.C.)

	Year	Total claims[1] (excl. surrenders)	Death	Death as a % of total claims	Endowment	Endowment as a % of claims	Other Claims	Other claims as a % of total claims	Surrenders	Surrenders as a % of total claims	Total expenditure	Total claims as a % of total expenditure	Surrenders as a % of total expenditure	Surrenders and total claims as % of total expenditure
GUYANA (Domestic)	1959	0.910	0.240	26.4	0.659	72.4	0.011	1.2	0.346	38.0	1.909	47.7	18.1	65.8
	1960	0.827	0.214	25.9	0.600	72.6	0.013	1.6	0.275	33.3	1.826	45.3	15.1	60.4
	1961	1.245	0.334	26.8	0.905	72.7	0.006	0.5	0.285	22.9	2.298	54.2	12.4	66.6
	1962	1.411	0.275	19.5	1.122	79.5	0.014	1.0	0.664	47.1	2.941	48.0	22.6	70.6
	1963	1.505	0.282	18.7	1.222	81.2	0.001	0.1	0.530	35.2	2.932	51.3	18.1	69.4
	1964	1.515	0.279	18.4	1.215	80.2	0.021	1.4	0.552	36.4	3.077	49.2	17.9	67.2
	1965	1.709	0.432	25.3	1.267	74.1	0.010	0.6	0.441	25.8	3.371	50.7	13.1	63.8
	1966	2.128	0.595	28.0	1.521	71.5	0.012	0.6	0.450	21.1	4.126	51.6	10.9	62.5
	1967	2.152	0.599	27.8	1.537	71.4	0.016	0.7	0.709	32.9	4.741	45.4	14.9	60.3
	1968	2.027	0.474	23.4	1.543	76.1	0.010	0.5	0.761	37.5	4.762	42.6	16.0	58.5
TRINIDAD	1957	2.641	0.725	27.5	1.801	68.2	0.115	4.4	1.241	47.0	6.942	38.0	17.9	55.9
	1958	3.114	0.904	29.1	2.067	66.4	0.143	4.6	1.557	50.0	8.541	36.5	18.2	54.7
	1959	3.883	1.257	32.4	2.443	62.9	0.183	4.7	1.928	49.7	10.750	36.1	18.2	54.7
	1960	4.150	1.374	33.1	2.616	63.0	0.160	3.9	2.177	52.5	12.008	34.6	18.1	52.7
	1961	5.309	1.899	35.8	3.180	59.9	0.230	4.3	3.234	60.9	15.220	34.9	21.2	56.1
	1962	5.472	1.972	36.0	3.155	57.7	0.345	6.3	4.099	74.9	16.337	33.5	25.1	58.6
	1963	5.741	2.261	39.4	3.026	52.7	0.454	7.9	3.660	63.8	17.093	33.6	21.4	55.0
	1964	5.644	2.291	40.6	2.853	50.5	0.500	8.9	4.897	86.8	18.973	29.7	25.8	55.5
	1965	7.609	3.334	43.8	3.428	45.1	0.847	11.1	3.192	42.0	20.130	37.8	15.9	53.7
	1966	7.395	3.191	43.2	3.433	46.4	0.771	10.4	3.226	43.6	20.007	37.0	16.1	53.1

* For Trinidad, death includes disability claims, endowment is equated with maturity claims and 'other claims' are equated with annuities.

[1] Incl. death, endowment, other claims.

Source: Computations based on (a) Special Request to Companies in Guyana
(b) Annual Statistical Digest, Trinidad.

In Table 2.AIV, we try to determine whether certain types of non-life business are more risky than others and whether there is any significant difference between foreign and local non-life companies in Trinidad. Because of the variation in the number of companies reporting, it is difficult to make a categorical judgement, but at least motor vehicle insurance seems to be a relatively risky business and fire a relatively safe business[27], judging from the size of claims paid as a percentage of premium income. Table 2.AV tends to show that for motor vehicle insurance, private cars, hired cars, goods vehicles and tractors, and motor cycles are very risky third party business and that private cars and goods vehicles and tractors are fairly risky "other than third party" business (although the variations in the number of companies reporting may make the conclusions invalid). These figures seem to confirm the complaints made by many insurance companies in the Caribbean about the high motor vehicle accident-rate and seem to justify their ceasing to pay the full loss re claims; this policy of not paying the full claim is an old one[28] and is an alternative to raising the premium rates for everyone. Raising the premium rates for everyone, however, has the disadvantage that the careful driver has to subsidize the careless driver. However, because motor vehicle insurance is legally compulsory, a government should not allow premium rates (or their alternative) to rise without the companies having to justify themselves. Moreover, it is only for the marginal (in Guyana) policy holders that the insurance companies are not paying the full claim (because companies seldom change the contract terms for old customers) and so the marginal policy holders who get into accidents, are really subsidizing the intra-marginal policy holders (who may also get into accidents). Besides, it can be claimed that an accident is not only caused by the negligence of the one or more parties involved but by the general incidence of congestion, (external diseconomies) and so a scheme should be devised whereby *all* motorists contribute towards the expenses in meeting rapidly increasing accident claims.

EFFICIENCY OF INSURANCE COMPANIES

There are a number of indices and ratios we can use to test the efficiency of insurance companies.

One such index is the "insurance wealth effect" or the rate of return on the holdings of assets. Table 19, below, shows the income earnings on investment balances in Trinidad for life insurance companies in Trinidad. It shows that during the 1957-66 period, the earnings rate

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27 Fire claims as a % of premium income is consistently below 50% and this seems very surprising in view of the fact that "as reasoned opinion has been expressed that every £100 of premium income in a fire insurance account may be split up as follows: Claims and cost of settlement £50....." H.E.Raynes: *Insurance*. Oxford University Press, 1960. (p. 160).

28 See A.H. John: "The London Assurance Company and the Marine Insurance Market of the Eighteenth Century" in *Economica*, May, 1958. (especially p. 140).

rose and then began to even out. The earnings rate might have been higher if figures were available for investment balances out of the country since it is believed that one reason for holding foreign balances is that the private rate of return (if not the social rate of return) is higher on these balances. The tendency for the earnings rate to rise is in keeping with the general rise in prices of goods and services in the economy and the earnings rate would have been higher were it not for the fact that the higher recent rates have been offset by investments acquired when interest rates were lower.

TABLE 2.19 Changes in Income Earnings on Local Assets, Life Insurance Companies. Trinidad $000 (E.C.)

Year	Investment Balances	Income on Balances	Income as % of Balances
1957	23,834	1,252	5.3
1958	26,298	1,555	6.1
1959	34,797	2,572	7.4
1960	42,466	2,991	7.0
1961	48,652	3,843	7.9
1962	53,223	3,640	6.8
1963	58,739	4,440	7.6
1964	60,972	4,016	6.6
1965	65,763	4,341	6.6
1966	69,833	4,508	6.5

Source: Computations based on figures in Annual Statistical Digest, Trinidad.

A second index of efficiency is a comparison of a total expenditure (claims and expenses)/total income ratio with a reserve/total liabilities ratio. If the total expenditure/total income ratio is getting smaller, then either the premium rate should be lowered (making total income smaller) or the reserves/total liabilities ratio should be lowered[29] (making it possible to distribute more dividends); in fact there should always be a tendency to lower the reserves/total liabilities rate as insurance grows, because of the benefits of risk spreading, unless growth is due to entry of new firms rather than expansion of existing firms. But more research needs to be done in order to determine whether the size of reserves varies in fact with the liquidity, yield, risk and general composition of the asset portfolio. Despite the fluctuations (and the inadequacy of the statistics) Table 2.20 tends to

[29] Note that total claims/total income might be falling but that total claims/premium income might be rising, thus making the argument less strong (but still valid) for a fall in premium rates.

TABLE 2.20 Relationships Between Expenditure, Income and Net Underwriting Profit for Life and Non Life Insurance Companies, Guyana and Trinidad $m (E.C.)

GUYANA (Domestic)

Year	Total Expenditure (1)	Total Income	Net Underwriting (N.U) Profit	Premium Income	N.U. Profit as % of Total Income	N.U. Profit as % of Premium Income	Total expenditure as a % of premium Income	N.U. Profit as % of Total expenditure
NON-LIFE								
1945	1.652	0.940	−0.712	0.576	−75.7	−12.4	286.8	−43.1
1950	0.917	1.222	0.305	0.891	25.0	34.2	102.9	33.3
1955	1.433	1.640	0.207	1.355	12.6	15.3	105.8	14.4
1956	1.706	1.813	0.107	1.510	5.9	7.1	113.0	6.3
1957	1.651	1.957	0.306	1.628	15.6	18.8	101.4	18.5
1958	1.847	2.162	0.315	1.810	14.6	17.4	102.0	17.1
1959	1.928	2.290	0.362	1.928	15.8	18.8	100.0	18.8
1960	2.210	2.522	0.312	2.127	12.4	14.7	103.9	14.1
1961	2.642	2.982	0.340	2.552	11.4	13.3	103.5	12.9
1962	3.474	3.116	−0.358	2.564	−11.5	−14.0	135.5	10.3
1963	2.178	2.599	0.421	2.100	16.2	20.0	103.7	19.3
1964	2.599	2.751	0.152	2.203	5.5	6.9	118.0	5.8
1965	2.454	2.852	0.398	2.299	14.0	17.3	106.7	16.2
1966	2.761	3.226	0.465	2.564	14.4	18.1	107.7	16.8
1967	3.012	3.564	0.552	2.851	15.5	19.4	105.6	18.3
1968	3.374	3.914	0.540	3.237	13.8	16.7	104.2	16.0
LIFE								
1945	0.410	0.968	0.558	0.698	57.6	79.9	58.7	136.1
1950	0.813	1.453	0.640	1.092	44.0	58.6	74.5	78.7
1955	1.038	2.307	1.269	1.617	55.0	78.5	64.2	122.3
1956	1.094	2.450	1.356	1.754	55.3	77.3	62.4	123.9
1957	1.330	2.781	1.451	1.957	52.2	74.1	68.0	109.1
1958	1.638	3.110	1.472	2.128	47.3	69.2	77.0	89.9
1959	1.909	3.303	1.394	2.258	42.2	61.7	84.5	73.0
1960	1.826	3.626	1.800	2.460	49.6	73.2	74.2	98.9
1961	2.298	3.910	1.612	2.579	41.2	62.5	89.1	70.1
1962	2.941	4.051	1.110	2.620	27.4	42.4	112.3	37.7
1963	2.932	4.209	1.277	2.715	30.3	47.0	108.0	43.6
1964	3.077	4.384	1.307	2.777	29.8	47.1	110.8	43.6
1965	3.371	4.927	1.556	3.155	31.6	49.3	106.8	46.2
1966	4.126	5.629	1.503	3.762	26.7	40.0	109.7	36.4
1967	4.741	6.848	2.107	4.711	30.8	44.7	100.6	44.4
1968	4.762	7.979	3.217	5.559	40.3	57.9	85.7	67.6

(1) Already includes tax paid; therefore our profit figure represents net underwriting profits. The concept of underwriting profit is one of the most confused and debatable accounting practices in the insurance business

Source: Computations based on data in previous tables.

TRINIDAD

NON-LIFE

Year	Total Expenditure (1)	Total Income	Net underwriting (N.U) Profit	Premium Income	N.U. Profit as % of Total Income	N.U. Profit as % of Premium Income	Total Expenditure as a % of premium Income	N.U. Profit as % of Total expenditure
1957	4.073	6.332	2.259	6.138	35.7	36.8	66.4	55.5
1958	7.389	7.095	—0.294	6.884	—4.1	—4.3	107.3	—4.0
1959	5.311	8.138	2.827	7.898	34.7	34.7	67.2	53.2
1960	6.894	9.686	2.792	9.400	28.8	28.8	73.3	40.5
1961	9.975	10.824	0.849	10.488	7.8	7.8	95.1	8.5
1962	8.708	11.766	3.058	11.395	26.0	26.0	76.4	35.1
1963	9.949	12.631	2.682	12.126	21.1	22.1	82.0	27.0
1964	9.762	13.384	3.622	12.617	27.1	28.7	77.4	37.1
1965	10.020	12.870	2.850	12.260	22.1	23.2	81.7	28.4
1966	9.323	11.462	2.139	10.965	18.7	19.5	85.0	22.9
LIFE								
1957	6.942	12.884	5.942	11.632	46.1	51.1	59.7	85.6
1958	8.541	14.907	6.366	13.352	42.7	47.7	64.0	74.5
1959	10.750	18.727	7.977	16.155	42.6	49.4	66.5	74.2
1960	12.008	22.789	10.781	19.798	47.3	54.5	60.7	89.8
1961	15.220	24.894	9.674	21.051	38.9	46.0	72.3	63.6
1962	16.337	23.323	6.986	19.682	30.0	35.5	83.0	42.8
1963	17.093	26.657	9.564	22.217	35.9	43.0	76.9	56.0
1964	18.973	26.520	7.547	22.442	28.5	33.6	84.5	39.8
1965	20.130	28.152	8.022	23.811	28.5	33.7	84.5	39.9
1966	20.007	28.564	8.557	24.056	30.0	35.6	83.2	42.8

show that (judging from the movements of the "underwriting profit" figure) the total expenditure/total income ratio has been rising for life companies in Guyana and Trinidad, although this tendency seems to have been reversed towards the end of the period. A less clear picture emerges for non-life companies, possibly because of the nature of the business; the rate of increase in managerial and commission expenses may not be as high as for life companies, but claims fluctuate more widely, and income tends to increase more slowly because of shorter-term assets.

A third index is the size of the operating expenses/total claims ratio and the operating expenses/premium income ratio. If expenses are rising faster than claims, this could cause policy dividends to fall or premium rates on new policies to rise unless the company decided to absorb these "losses". Such a situation would also imply that even if insurance companies at some time experience economies of scale, this stage does not last for very long; we intuitively believe that after a certain stage life insurance companies experience rising marginal costs, partly because of the difficulty involved in coaxing the really "marginal saver" to buy an insurance policy and partly because of the secular rise in salaries, wages and the cost of materials. But perhaps more research needs to be done on the theory of the insurance firm. Table 2. 21 shows that operating expenses as a percent of total claims have been fluctuating, due as much to claims as to expenses fluctuations (sudden increases in expenses might represent increased costs of putting a large volume of business on the books.) In Trinidad, the percentage has been more stable and at a level higher than the average for Guyana. Because operating expenses are, on average, nearly three-quarters the size of total claims, this reinforces our view that traditional statistical calculations are just as important as pure actuarial calculations in the general workings of life insurance companies. For non-life companies, operating expenses are much greater than total claims and managerial expenses as a percentage of operating expenses much lower than for life companies (for life companies, 90 percent in Guyana and 80 per cent in Trinidad, on average.) The operating expenses/premium income ratio is perhaps even more useful than the operating expenses/total claims ratio. Table 2. 22 shows that operating expenses for life companies are becoming a greater and greater proportion of premium income (the non-life trend is less clear-cut). This has important implications for the theory of life insurance operations in the Caribbean; it implies that insurance companies have increasingly to rely on investment (and "other") income in order to satisfy their contractual obligations. (In the U.S.A., net investment income was equivalent to 45 percent of net inflow of savings in 1952 and 71 percent in 1959, due partly to rising interest rates.) Table 2. 20, previously referred to, shows that total expenditure (which includes expenses) is even greater than premium income, for life companies, and in the last few years, for non-life companies, in Guyana, although it has not yet reached this stage in Trinidad. Table 2. 23, below, shows a detailed breakdown of certain expenditure items for life insurance companies in Trinidad. It shows that commissions paid are nearly double wages and salaries

TABLE 2.21 Operational Expenses as a Percentage of Total Claims and Managerial Expenses as a Percentage of Operational Expenses, Guyana and Trinidad $m (E.C.)

		LIFE						NON-LIFE					
	Year	Total Claims	Rate of Increase in total claims %	Operating expenses	Rate of increase in operating expenses	Op. expenses as a % of total claims	Managerial expenses as a % of Op expenses	Total claims	Rate of Increase in total claims	Operating Expenses	Rate of Increase in operating expenses	Op. expenses as a % of total claims	Managerial expenses as a % of Op. expenses
GUYANA (Domestic)	1945	0.256		0.149		58.2	94.6	1.121		0.155		13.8	47.1
	1950	0.568	+121.9	0.234	+57.0	41.2	86.7	0.140	−87.5	0.281	+81.3	200.7	43.4
	1955	0.523	−7.9	0.475	+103.0	90.8	67.6	0.266	+90.0	0.445	+58.4	167.3	16.0
	1956	0.648	+23.9	0.408	−14.1	63.0	90.2	0.311	+16.9	0.619	+39.1	199.0	19.9
	1957	0.808	+24.7	0.470	+15.2	58.2	93.4	0.387	+24.4	0.490	−20.8	126.6	23.2
	1958	0.938	+16.1	0.574	+22.1	61.2	82.8	0.510	+31.8	0.536	+9.4	105.1	24.3
	1959	0.910	−3.0	0.580	+1.0	63.7	93.8	0.439	−13.9	0.539	+0.6	122.8	25.2
	1960	0.827	−9.1	0.641	+10.5	77.4	97.2	0.580	+32.1	0.656	+21.7	113.1	22.1
	1961	1.245	+50.5	0.617	−3.7	49.6	96.8	0.880	+51.7	0.620	−5.5	70.5	31.5
	1962	1.411	+13.3	0.661	+7.1	46.8	94.1	1.966	+123.4	0.612	−1.3	31.1	32.8
	1963	1.505	+6.7	0.695	+5.1	46.3	96.0	0.478	−75.7	0.689	+12.6	4.1	31.5
	1964	1.515	+0.7	0.765	+10.1	50.5	97.4	0.701	+46.7	0.881	+27.9	125.7	26.1
	1965	1.709	+12.8	0.993	+29.8	58.1	95.6	0.526	−25.0	0.901	+2.3	171.3	30.6
	1966	2.128	+24.5	1.353	+36.2	63.6	94.3	0.632	+20.2	1.193	+32.4	188.3	24.1
	1967	2.152	+1.1	1.646	+21.7	76.5	96.7	0.745	+17.9	1.063	−10.5	142.7	27.9
	1968	2.027	−5.8	1.723	+4.7	85.0	97.1	0.882	+18.3	1.175	+10.5	133.2	28.1
TRINIDAD	1957	3.882		2.947		75.9	79.1						
	1958	4.671	+20.3	3.766	+27.8	80.6	80.9						
	1959	5.811	+24.7	4.801	+27.5	82.6	79.8						
	1960	6.327	+8.9	5.399	+12.5	85.3	79.5						
	1961	8.543	+35.0	6.388	+18.3	74.9	84.5						
	1962	9.571	+12.0	6.437	+ 0.6	67.3	79.5						
	1963	9.401	−1.8	7.141	+10.9	76.0	78.3						
	1964	10.541	+12.1	8.104	+13.5	76.9	71.7						
	1965	10.801	+2.5	8.140	+0.4	75.4	76.8						
	1966	10.621	−1.7	8.172	+0.4	76.9	77.0						

Source: Computations based on data in previous tables.

TABLE 2.22 Operating Expenses as a Percentage of Premium Income, Life and Non-Life Insurance Companies, Guyana and Trinidad $m (E.C.)

		LIFE			NON-LIFE		
	Year	Premium Income	Operating expenses	Operating expenses as a % of Premium Income	Premium Income	Operating Expenses	Operating Expenses as a % of Premium Income
GUYANA (Domestic)	1945	0.698	0.149	21.3	0.576	0.155	26.9
	1950	1.092	0.234	21.4	0.891	0.281	31.5
	1955	1.617	0.475	29.4	1.355	0.445	32.8
	1956	1.754	0.408	23.3	1.510	0.619	41.0
	1957	1.957	0.470	24.0	1.628	0.490	30.1
	1958	2.128	0.574	27.0	1.810	0.536	29.6
	1959	2.258	0.580	25.7	1.928	0.539	28.0
	1960	2.460	0.641	26.1	2.127	0.656	30.8
	1961	2.579	0.617	23.9	2.552	0.620	24.3
	1962	2.620	0.661	25.2	2.564	0.612	23.9
	1963	2.715	0.695	25.6	2.100	0.689	32.8
	1964	2.777	0.765	27.5	2.203	0.881	40.0
	1965	3.155	0.993	25.1	2.299	0.901	39.2
	1966	3.762	1.353	36.0	2.564	1.193	46.5
	1967	4.711	1.646	34.9	2.851	1.063	37.3
	1968	5.559	1.723	31.0	3.237	1.175	36.3
TRINIDAD	1957	11.632	2.947	25.3			
	1958	13.352	3.766	28.2			
	1959	16.155	4.801	29.7			
	1960	19.798	5.399	27.3			
	1961	21.051	6.388	30.3			
	1962	19.682	6.437	32.7			
	1963	22.217	7.141	32.1			
	1964	22.442	8.104	36.1			
	1965	23.811	8.140	34.2			
	1966	24.056	8.172	34.0			

Source Computations based on data in previous tables.

TABLE 2.23 Relationship Between Wages and Salaries, Commissions and Other Expenditure, Life Companies—Trinidad $ (E.C.)

	1965		1966		1967	
	Amount	% of Total	Amount	% of Total	Amount	% of Total
Wages and salaries	1,510,729(15)	19.3	1,401,378(13)	15.8	1,706,118(13)	18.3
Commissions Paid	2,354,147(15)	30.1	2,868,638(14)	32.4	2,537,042(14)	57.2
Investment expenses	67,725(10)	0.9	370,291(8)	4.2	511,884(9)	5.6
Office Expenses	1,081,031(16)	13.8	1,509,573(13)	17.0	1,410,653(14)	15.1
Income Tax	986,786(13)	12.6	1,035,000(11)	11.7	1,234,722(14)	13.2
Other Taxes Paid	113,629(13)	1.6	87,722(9)	1.0	108,680(9)	1.2
Other expenditure in Trinidad	1,698,887(13)	21.7	1,584,068(12)	17.9	1,809,588(13)	19.4
Total	7,812,913	100.0	8,856,671	100.0	9,318,687	100.0

( ) denotes number of companies reporting.

Source: Special request, Statistical Department, Trinidad.

(administrative expenses) whereas Raynes[30] cites the typical commission/administrative expenses ratio as being 18 : 25; thus the top heavy expenditure element in insurance operations may be due to abnormally high administrative expenses.

A fourth index is the premium income/assured value ratio. According to insurance theory, such a ratio might be expected to fall for three reasons. The first is that with continuous post-war inflation, the insurance assets (e.g. real estate and rent therefrom) should appreciate in value ("hidden reserves") faster than management expenses, and such windfalls should be passed on in the form of lower premiums. The second reason why the premium income/assured value ratio might be expected to fall (or profits on policies to be increased) is that as companies become larger, risk bearing becomes more possible so that investments can be made in assets with higher yields, part of which should be passed on to the consumer. The third reason is that the average life span has been increasing, so the premium rate charged should fall (applicable to life companies only.) Table 2. 24 shows that the premium income/assured ratio has been decreasing in the Caribbean, although this might be for reasons other than the ones we have given; for example, such a fall might be due to a relative rise in the number of "whole of life" and "group life" (and other term insurance) policies and a relative fall in the number of higher premium endowment policies. (In Trinidad, endowment claims have made a relative fall, but not in Guyana–Table 2. 18).

A fifth index, which might indicate the degree of efficiency of insurance companies, is the tax/premium income ratio; if this ratio is increasing, it would show the ability of insurance companies either to economize on operating expenses (e.g. as a result of economies of scale) or to increase their investment income at a fast rate. Table 2. 25 shows that tax as a percentage of premium income might have been tending to increase (especially in Guyana), despite the wide fluctuations. Later on in the study, we shall explore whether the rise has been due to either an increase in the tax rates, a relative rise in income or a relative fall in expenses, or a combination of all these factors; or whether the rise in the ratio may be merely due to the rate of increase in premium income failing to keep pace. In the case of Trinidad, there might have been a sharp rise in the tax/premium income ratio after 1966, since the spate of surrendering of policies which made necessary a new withholding tax, would have caused tax to rise sharply, and premium income to fall because of the exit of the surrendering policy holders. Note also that if a company stops issuing new policies, the tax/premium income ratio would rise; such a rise may also reflect increasing "efficiency" since it may be good for the economy, if not the firm, if inefficient firms go out of existence as quickly as possible (provided the efficient firms expand by an equivalent amount at some later date.)

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30 H. E. Raynes (*Op. Cit.*) was however referring to fire insurance companies in particular and these non-life companies tend to spend less on commissions.

TABLE 2.24 Life Premium Income as a Percentage of Assured Values,* Guyana, Trinidad and Jamaica $000 (E.C.)

	GUYANA			TRINIDAD			JAMAICA		
Year	Premium Income	Assured Value	Premium Income as a % of assured value	Premium Income	Assured Value	Premium Income as a % of assured value	Premium Income	Assured Value	Premium Income as a % of assured value
1954	—	—	—	7,311	139,898	5.2	—	—	—
1955	—	—	—	8,684	164,788	5.3	—	—	—
1956	—	—	—	9,821	189,893	5.2	—	—	—
1957	—	—	—	11,055	226,507	4.9	—	—	—
1958	—	—	—	12,559	243,507	5.2	—	—	—
1959	—	—	—	15,461	308,160	5.0	—	—	—
1960	—	—	—	17,696	372,283	4.8	—	—	—
1961	—	—	—	19,410	438,654	4.4	16,056	450,240	3.6
1962	—	—	—	18,846	459,570	4.1	17,875	506,400	3.5
1963	—	—	—	20,265	486,936	4.2	21,307	592,320	3.6
1964	1,462	34,014	4.3	19,823	566,902	3.5	26,765	755,620	3.5
1965	1,637	39,355	4.2	21,406	592,265	3.6	30,374	869,760	3.5
1966	1,895	47,514	4.0	21,779	707,408	3.1	34,022	998,480	3.2
1967	2,135	54,531	3.9	—	—	—	37,872	1188,480	3.2
1968	2,323	61,162	3.8	—	—	—	—	—	—

* Calculated on the basis of a selected number of companies reporting this particular statistic.

Source: Computations based on data in previous tables

TABLE 2.25 Taxes Paid as a % of Premium Income and as a % of All Income for Non-Life and Life (Domestic) Insurance Companies in Guyana and Non-Life and Life Companies in Trinidad. $m (E.C.)

		NON-LIFE					LIFE				
	Year	Taxes Paid	Premium Income	Taxes Paid as a % of Premium Income	Total Income	Taxes Paid as a % of Total Income	Taxes Paid	Premium Income	Taxes Paid as a % of Premium Income	Total Income	Taxes Paid as a % of Total Income
GUYANA (Domestic)	1945	0.060	0.576	10.4	0.940	6.4	0.005	0.698	0.7	0.968	0.5
	1950	0.107	0.891	12.0	1.222	8.8	0.011	1.092	1.0	1.453	0.8
	1955	0.182	1.355	13.4	1.640	11.1	0.030	1.617	1.9	2.307	1.3
	1956	0.139	1.510	9.2	1.813	7.7	0.038	1.754	2.2	2.450	1.6
	1957	0.141	1.628	8.7	1.957	7.2	0.052	1.957	2.7	2.781	1.9
	1958	0.074	1.810	4.1	2.162	3.4	0.126	2.128	5.9	3.110	4.1
	1959	0.207	1.928	10.7	2.290	9.0	0.073	2.258	3.2	3.303	2.2
	1960	0.167	2.127	7.9	2.522	6.6	0.083	2.460	3.4	3.626	2.3
	1961	0.209	2.552	8.2	2.982	7.0	0.151	2.579	5.9	3.910	3.9
	1962	—	2.564	—	3.116	—	0.203	2.620	7.7	4.051	5.0
	1963	0.126	2.100	6.0	2.599	4.8	0.212	2.715	7.8	4.209	5.0
	1964	0.254	2.203	11.5	2.751	9.2	0.245	2.777	8.8	4.384	5.6
	1965	0.298	2.299	13.0	2.852	10.2	0.228	3.155	7.2	4.927	4.6
	1966	0.118	2.564	4.6	3.226	3.7	0.195	3.762	5.2	5.629	3.5
	1967	0.366	2.851	12.8	3.564	10.3	0.234	4.711	5.0	6.848	3.4
	1968	0.437	3.237	13.5	3.914	11.2	0.251	5.559	4.5	7.979	3.1
TRINIDAD	1957	0.726*	6.138	11.8	6.332	11.5	0.113**	11.632	1.0	12.884	0.9
	1958	1.135	6.884	16.5	7.095	16.0	0.104	13.352	0.8	14.907	0.7
	1959	0.857	7.898	10.9	8.138	10.5	0.138	16.155	0.9	18.727	0.7
	1960	1.099	9.400	11.7	9.686	11.3	0.284	19.798	1.4	22.789	1.2
	1961	1.540	10.488	14.7	10.824	14.2	0.289	21.051	1.4	24.894	1.2
	1962	1.230	11.395	10.8	11.766	10.5	0.330	19.682	1.7	23.323	1.4
	1963	1.272	12.126	10.5	12.631	10.1	0.539	22.217	2.4	26.567	2.0
	1964	0.759	12.617	6.0	13.384	5.7	1.028	22.442	4.6	25.520	3.9
	1965	0.872	12.260	7.1	12.870	6.8	1.189	23.811	5.0	28.152	4.2
	1966	0.673	10.965	6.1	11.462	5.9	1.124	24.056	5.0	28.564	4.3

* Overestimate since it includes "other expenses"; thus tax as a percentage of both premium income and total income are also overestimates.
** Figures refer to both local and foreign life companies.

1965 and 1966 Non-Life figures for Trinidad are provisional.
Source: Computations based on data in previous tables.

A sixth ratio, which relates to the efficiency of the economic system as a whole, rather than to insurance companies, is the local assets/total assets ratio (although this may conflict with our first index—the earnings/assets ratio, since foreign assets may be higher earning.) Recently introduced laws in Trinidad and Guyana are designed to "encourage" insurance companies to hold a higher percentage of local assets, primarily in order to help increase local capital formation. In Trinidad, as a result of the introduction of the 1966 Insurance Act, the local component of the 1966 increase in asset holdings of life companies rose to 80.4 percent (59.7 percent in 1965), the new legal minimum being 60 percent of the stock of assets. In Guyana, in 1967, the amount of foreign assets held by domestic companies was still as high as 29 percent of total assets and for this reason the government introduced legislation in January 1970 to increase local assets to 90 percent of total assets held against local policies.

THE PROBLEM OF MULTINATIONAL FINANCIAL CORPORATIONS

Reference has already been made to the fact that there are many foreign insurance companies operating in the Caribbean, e.g. of the forty-one companies registered in Guyana, thirty-one are known to be foreign. These foreign companies are really subsidiaries (called "agencies") of parent firms and the parent firms, located in the North Atlantic metropole, and the branch firms, located in the Caribbean hinterland, (and other countries), constitute a multinational financial corporation (MNFC), with an inter-relationship almost similar to that obtaining in the multinational corporations (MNC) of the real sector. (MNFC also dominate the banking and hire purchase industries in the Caribbean.)

There are many reasons for the emergence of the MNFC structure. A first and underlying reason is that finance tends to follow trade.[31] There tends to be a fairly close correlation between the expansion and contraction of world trade and the expansion and contraction of the activities of MNFC. The MNFC tend to follow the MNC overseas because they like to deal with businesses with which they are well acquainted. This may be the historical reason for foreign firms dominating the non-life insurance business in the Caribbean. The next development was probably for life insurance protection to be provided for the needs of the expatriate personnel with the logical extension later in the coverage to the local people. (Also, as stated earlier, there is some amount of interaction between the activities of life and non-life companies; and because of external economies and the demonstrated success of the early insurance companies, other companies followed.) The expansion overseas of insurance companies was therefore, a product of both conservatism and adventurousness.

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31 Branch firms of MNFC exist not only in underdeveloped countries but also in developed countries. For some of the reasons for the emergence of the MNFC structure in commercial banking, see J. Koszul: "American Banks in Europe" in *The International Corporation*, C. Kindleberger (Ed.) M.I.T. Press, 1970.

A second reason for the emergence of the MNFC structure in the insurance industry may be the fear on the part of each insurance company in the metropole that if it did not operate in the hinterland, other firms would and these rival firms would become so big and efficient (because of economies of scale and the benefits of a geographically diversified portfolio) that it would be outcompeted in the metropole itself (in terms of the lower premium rates, mortgage rates etc., which its rivals could offer.)

A third reason is that the typical non-life insurance firm in the metropole may fear that the branch firm of a MNC, which is its customer, may develop such good and beneficial contacts in the hinterland with a rival insurance company that the parent firm of the MNC may want to switch insurance companies in the metropole.

A fourth reason is that the MNFC, like MNC, are profit seekers and realize that, by operating in the hinterland, they can acquire more funds for use either in the hinterland or in the metropole.

A fifth reason is that by operating in more than one country the MNFC can (a) move funds around to where income from asset holdings is highest (b) maintain a lower liquidity ratio in its global operations because of the shiftability of funds (for example, for three foreign life insurance companies operating in Trinidad in 1965, for whom data are available, remittances to the parent company were $2,355,284 and receipts from the parent company were only $476,326) (c) diversify its portfolio and spread its risks both geographically and over different types of economy (and political and social situation), and (d) benefit from economies of scale.

A sixth reason is that the MNFC might have been restricted in the metropole by certain regulations preventing it from competing as vigourously as it would have liked. In the U.S.A., for example, regulations exist limiting the holding of certain assets to a certain percentage of the total asset portfolio of insurance companies. Generally, the MNFC might expect monetary policy and the general financial milieu to be less restrictive in the hinterland, than in the metropole (including fixed exchange rates and free convertibility).

Because of the very large number (compared with banks) of foreign insurance companies operating in the Caribbean, there are certain adverse effects on the operations of the industry. (The very large number of companies perhaps indicates that the shifting of risk by reinsurance makes for extreme ease of entry.) The first adverse effect is that there may be excessive competition. The foreign insurance companies operate not as complements but as competitors. Each foreign insurance company tries to integrate its activities with those of the parent firm and the latter's other subsidiaries, rather than with the asset portfolios of either the other insurance companies or the non-insurance financial institutions in the Caribbean country in which it operates. (Even reinsurance tends to be not with other insurance companies operating in various Caribbean territories but with insurance companies operating in the metropole). Thus corporate financial integration tends to contribute to national and Caribbean financial fragmentation.

The second adverse effect is that excessive competition could theoretically lead to lending rates (on mortgages, policy loans etc.) being too high. Now excessive competition may lead to premium rates being relatively low, but low premium rates, given certain contractual obligations, are only possible if investment income is expected to be high. This competitive situation is probably tempered by some amount of tacit collusion, since few firms have ever been forced to leave the industry.

The third adverse effect is that foreign insurance companies may employ a "credit worthiness" standard which is based on conditions obtaining in the metropole rather than in the hinterland. This may be reflected in an unduly low portfolio allocation for local agricultural and industrial mortgages and equities, with unfavourable consequences for structural transformation of the Caribbean economies. Moreover, foreign insurance companies may be "investment leaders" and their distorting portfolio pattern may be partly imitated by the local insurance companies.

The fourth adverse effect is that if the asset portfolio of the hinterland firm is fully integrated with that of the parent firm (and the latter's other subsidiaries) it is very difficult to make a true assessment of the investment pattern and tax liability of the hinterland firm.

The MNFC structure also has unfavourable affects on the hinterland economy. Firstly, the existence of many foreign insurance companies hinders or stunts the growth of an indigenous insurance structure. Secondly, the preference of the foreign insurance companies for foreign securities acts as an income drain. (In addition, the profits of foreign insurance companies are repatriated). This preference for foreign securities partly results from the fact that the local money and capital market is very narrow and very underdeveloped. It is said that foreign companies prefer foreign securities, not so much because of the price or rate of interest, but because such securities are more readily marketable and are more easily available in terms of the desired volume, maturity pattern and timing of issue. However, such preference constitutes a vicious circle, since if there are few buyers and sellers of local securities the local money and capital market would remain underdeveloped. Moreover, the hinterland government, in the terms of issue of its own securities, is forced to compete with the terms of issue of foreign governments, and this is especially the case in the Caribbean where the insurance companies are a virtual monopsonist of government long-term securities. Thirdly, the operations of foreign insurance companies lead to serious credit distortion. Not only do the foreign companies prefer foreign securities, but also they prefer to hold equities and agricultural and industrial mortgages of the branch firms of MNC rather than of locally owned industries. Because the branch firms of MNC in the Caribbean import most of their inputs, backward and forward linkages are few and little progress is made towards structural transformation.

A number of suggestions have been made in recent years for dealing with foreign insurance companies. One suggestion is that, if by various aids local insurance companies become more competitive,

they may grow at a faster rate than foreign insurance companies. However, some local insurance companies are hardly in a position to compete effectively with foreign companies, who are backed by giant MNFC, and moreover it would take too long for the success of such a policy to be realized; also, the setting up of new local insurance firms may merely cause a redistribution of existing savings rather than the coaxing out of new savings and the greater competition may lead to higher costs and an undesirable shift of income from investors to savers. And the effect of any new orientation in the asset portfolio policy of the local companies may be completely offset by the traditional preferences of the foreign companies. A second suggestion is local participation in the foreign companies via majority share ownership. However, share ownership is not synonymous with managerial control, which the foreign companies are very reluctant to relinquish because of the integrated nature of the operations of MNFC. A third suggestion is the introduction of regulations stipulating what minimum percentage of the asset portfolio of insurance companies should be devoted to local securities rather than foreign securities, investment rather than consumption, and what investment sectors should be favoured over others. However, this suggestion can only be a second best solution (with the first and second suggestions being fourth and third best solutions, respectively.) A fourth suggestion is the nationalization of the insurance industry. This seems to be the only really effective measure for control of the industry, especially since the MNFC structure leads to easy evasion of traditional monetary policy. Also, at the present moment, there are too many firms in the industry and nationalization would lead to rationalization,[32] a fall in excess capacity, a lowering of costs and perhaps a fall in premium rates. (Further reference will be made to the problem of rationalizating the insurance industry in Chapters V and VI.)

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32 For there to be as many as 140 insurance companies, over 100 of which are foreign, operating in a country as small as Jamaica is a really grotesque state of affairs and intensifies the dysfunctional nature of the integration of the financial system with that of the metropole. In recent years, the American companies have, moreover, been holding a greater proportion of their funds in Jamaica merely because of the fear of Dollar devaluation, and a stronger balance of payments situation in the U.S.A. would immediately cause an outflow. "Locking-in" legislation was therefore necessary to make local assets match local liabilities.

TABLE 2. AI Liabilities Structure of Domestic Life Insurance Companies in Guyana $ m (E.C.)

Year	Capital			Insurance Fund		Reserve Fund		Claims Intimated, not yet paid	Provision for Income Tax	Other Liabilities	Total Liabilities
	Guarantee	Share* capital (issued)	Premium	Life	Other	General	Other				
1945	0.100	—	—	5.2	—	0.4	—	0.1	—	0.4	6.2
1950	0.100	—	—	7.5	—	0.4	—	0.1	—	1.0	9.1
1955	0.100	—	—	12.5	—	0.8	—	0.2	—	0.9	14.5
1956	0.100	—	—	14.0	—	0.8	—	0.2	—	1.1	16.2
1957	0.100	—	—	15.3	—	1.1	—	0.2	—	1.1	17.8
1958	0.100	—	—	16.9	—	1.1	—	0.2	0.1	1.1	19.5
1959	0.100	—	—	18.6	—	1.1	—	0.2	0.1	1.0	21.1
1960	0.100	—	—	20.6	—	1.1	—	0.2	0.1	1.1	23.2
1961	0.100	—	—	22.6	—	1.1	—	0.3	0.1	1.2	25.4
1962	0.100	—	—	23.7	—	1.5	—	0.5	0.2	1.5	27.5
1963	0.100	0.2	—	25.6	—	1.5	—	0.5	0.2	1.0	29.1
1964	0.100	0.3	—	27.1	—	1.4	—	0.5	0.2	1.3	30.9
1965	0.100	0.3	—	29.0	—	1.9	—	0.5	0.2	0.7	32.7
1966	0.100	0.3	—	30.9	—	2.0	—	0.7	0.2	1.0	35.2
1967	0.100	0.6	—	33.6	—	2.0	—	0.8	0.2	0.9	38.2
1968	0.100	0.6	—	36.8	—	1.3	—	0.8	0.2	0.6	40.4

* Share Capital issued represents the smaller life Insurance Companies e.g. Prakash (1963) Guyana National (1964) and Hand-in-Hand Life (1967)

Source: Special requests to insurance companies.

TABLE 2. AII Liabilities Structure of Domestic Non-Life Insurance Companies in Guyana $m (E.C.)

Year	Capital			Insurance Fund		Undis-tri-buted Profit	Reserve Fund		Unpaid Premium to Re-insurers	Balances due to foreign Offices	Claims inti-mated, not yet paid	Provi-sion for Income Tax	Other liabi-lities	Total liabi-lities (Local & foreign)	(Foreign liabi-lities)
	Gua-rantee Capital	Script & stock Capital	Pre-mium (Rebate)	Life	Other		Gene-ral	Other							
1945	—	2.160	0.1	—	—	0.1	1.4	—	—	—	0.3	—	0.4	4.5	—
1950	—	2.508	0.7	—	—	0.2	2.0	—	0.008	0.006	0.1	0.2	0.7	6.4	(0.009)
1955	—	2.508	0.9	—	—	0.2	2.4	—	0.1	0.1	0.1	0.3	0.5	7.1	(0.140)
1956	—	2.508	1.0	—	—	0.3	2.6	—	0.1	0.1	0.1	0.3	0.6	7.6	(0.171)
1957	—	2.508	1.1	—	—	0.4	2.7	—	0.1	0.1	0.1	0.3	0.6	7.9	(0.221)
1958	—	2.508	1.2	—	—	0.4	2.9	—	0.1	0.1	0.1	0.3	0.3	7.9	(0.143)
1959	—	2.508	1.3	—	—	0.4	3.2	—	0.1	0.033	0.1	0.3	0.5	8.4	(0.098)
1960	—	2.508	1.4	—	—	0.5	3.5	—	0.007	0.008	0.2	0.3	0.5	8.9	(0.015)
1961	—	2.508	1.5	—	—	0.5	3.8	—	0.014	—	0.3	0.3	0.6	9.5	(0.017)
1962	—	2.508	1.1	—	—	0.4	3.9	—	0.014	—	0.6	0.2	1.1	9.8	(0.015)
1963	—	2.508	1.3	—	—	0.4	4.2	—	0.1	0.037	0.6	0.2	1.4	10.7	(0.126)
1964	—	2.508	1.3	—	—	0.4	4.4	—	0.1	0.1	0.6	0.3	0.5	10.2	(0.163)
1965	—	2.508	1.4	—	—	0.4	4.6	—	0.017	0.1	0.6	0.4	0.6	10.6	(0.100)
1966	—	2.508	1.4	—	—	0.4	5.0	—	0.1	0.1	0.7	0.2	0.5	10.9	(0.175)
1967	—	2.508	1.6	—	—	0.5	5.5	—	0.1	0.1	0.5	0.4	0.5	11.7	(0.185)
1968	—	2.508	1.8	—	—	0.5	5.6	—	0.1	0.1	0.6	0.5	0.5	12.2	(0.190)

Source: Speical requests to Insurance Companies.

TABLE 2.AIII Distribution of Life Premium Income Among Various Types of Policies, Trinidad and Tobago—$(E.C.)

	1965	%	1966	%	1967	%
Endowment Renewal	7,695,766(13)	38.1	5,685,794(11)	26.8	6,689,830(11)	29.1
New Endowment	845,679(11)	4.2	836,351(11)	3.9	1,170,374(10)	5.1
Ordinary Life Renewal	6,792,896(15)	33.6	8,628,384(13)	40.6	9,647,757(12)	42.0
New Ordinary Life	1,560,520(14)	7.8	1,503,991(14)	7.1	1,664,709(12)	7.2
Group Life Renewal	211,678(8)	1.0	390,651(10)	1.8	333,700(9)	1.5
New Group Life	101,551(8)	0.5	25,813(6)	0.1	364,821(5)	1.6
Industrial Renewal	579,319(3)	2.9	77,575(2)	0.4	1,142(1)	—
New Industrial	54,702(2)	0.3	2,095,153(3)	9.9	—	—
Immediate Annuity	70,012	0.3	186,017	0.9	157,730	0.7
Deferred Annuity	2,290,308	11.3	1,821,654	8.5	2,950,150	12.8
Total	20,202,449		21,251,383		22,980,213	

( ) Indicates number of companies reporting.

Source: Special request, Statistical Department, Trinidad.

TABLE 2. AIV Claims Paid and Expenses of Management (Wages, Salaries and Commissions) As % of Premium Income for Non-Life Foreign Companies 1965, and Local Companies, 1966—Trinidad $ (E.C.)

	FOREIGN COMPANIES					LOCAL COMPANIES				
Type of Business	Premium Income	Claims paid	Claims paid as % of premium income	Expenses of management	Management expenses as % of premium income	Premium Income	Claims paid	Claims paid as % of Premium Income	Expenses of management	Management expenses as % of premium income
Fire and Extraneous Perils	2,254,076	610,346	27.1	739,181	32.8	1,243,456	65,098	5.2	856,009	68.8
Accident Insurance (Personal)	709,229	310,227	43.7	222,086	31.8	40,912	13,214	32.3	23,726	58.0
Employers liability and workmen compensation	1,097,378	479,393	43.7	313,720	28.6	450,032	188,127	41.8	107,044	56.9
Marine Insurance	335,122	64,564	19.3	201,252	60.1	203,072	125,980	62.0	60,348	29.7
Motor Vehicle Insurance	2,391,835	1,529,402	63.9	499,550	20.9	2,314,261	1,108,002	47.9	825,700	35.7
Air Insurance	5,020	—	—	2,944	58.6	41	—	—	11	26.8
Other	251,713	73,091	29.0	67,462	26.8	135,511	38,656	28.5	38,575	28.5
Total	7,044,373	3,067,023	43.5	2,046,195	29.0	4,387,285	1,539,077	35.1	1,911,413	43.6

Figures are not always comparable since number of companies reporting on each item varies. The maximum number of foreign Companies that reported is 40 and local companies 17.

Source: Special request, Statistical Department, Trinidad.

TABLE 2.AV Motor Vehicles Insurance, Types of Policies and Premiums and Claims Made 1965—Trinidad $ (E.C.)

Type of Vehicle	Third party Premiums	Third party claims paid	Claims paid as % of premium	Other than third party premium	Other than third party claims paid	Claims paid as % of premium
Private cars	149,392(25)	168,265(24)	112.6	972,008(25)	851,907(22)	87.6
Hire cars (Taxis)	50,068(11)	73,916(10)	147.6	12,614(2)	220(1)	1.7
Omnibuses	—	59,156(2)	—	30,152(3)	1,195(3)	4.0
Goods Vehicles and Tractors	226,708(23)	95,329(16)	42.0	256,375(23)	227,211(20)	88.6
Motor cycles	8,770(11)	9,062(3)	103.3	4,888(6)	990(2)	20.3
All other	524,525(11)	19,984(3)	3.8	156,335(12)	22,168(7)	1.4

( ) Indicates number of companies reporting

Source: Special request, Statistical Department, Trinidad.

TABLE 2. AVI Relationship Between Investment Income and Total Expenditure, For Insurance Companies in Guyana and Trinidad $m(E.C.)

Year	LIFE (Domestic Cos.-Guyana)			LIFE (Trinidad)			NON-LIFE (Domestic Cos.-Guyana)			NON-LIFE (Trinidad)		
	Total expenditure	Investment Income	Investment income as a % of total expenditure	Total expenditure	Investment income	Investment income as a % of total expenditure	Total expenditure	Investment income	Investment income as a % of total expenditure	Total expenditure	Investment income	Investment income as a % of total expenditure
1945	0.410	0.231	56.3				1.652	0.174	10.5	—	—	—
1950	0.813	0.357	43.9				0.917	0.219	23.9	—	—	—
1955	1.038	0.615	59.2				1.433	0.283	19.7	—	—	—
1956	1.094	0.681	62.2				1.706	0.303	17.8	—	—	—
1957	1.330	0.811	61.0	6.942	1.252	18.0	1.651	0.329	19.9	4.073	0.194	4.8
1958	1.638	0.970	59.2	8.541	1.555	18.2	1.847	0.352	19.1	7.389	0.211	2.9
1959	1.909	1.032	54.1	10.750	2.572	23.9	1.928	0.360	18.7	5.311	0.241	4.5
1960	1.826	1.152	63.1	12.008	2.991	24.9	2.210	0.394	17.8	6.894	0.286	4.1
1961	2.298	1.311	57.0	15.220	3.843	25.2	2.642	0.424	16.0	9.975	0.337	3.4
1962	2.941	1.415	48.1	16.337	3.640	22.2	3.474	0.513	14.8	8.708	0.370	4.2
1963	2.932	1,487	50.7	17.093	4.440	26.0	2.178	0.473	21.7	9.949	0.505	5.1
1964	3.077	1.598	51.9	18.973	4.016	21.2	2.599	0.634	24.4	9.762	0.767	7.9
1965	3.371	1.722	51.1	20.130	4.341	21.6	2.454	0.648	26.4	—	—	—
1966	4.126	1.820	44.1	20.007	4.508	22.5	2.761	0.599	21.7	—	—	—
1967	4.741	2.086	44.0				3.012	0.616	20.5	—	—	—
1968	4.762	2.388	50.1				3.374	0.654	19.4	—	—	—

For Trinidad, investment income for life and non-life companies includes a not insignificant item called 'other revenue'.

Source: Computations based on data in previous tables.

CHAPTER III

The Operations of Building Societies

INTRODUCTION

Building Societies are "societies established for the purpose of raising, by the subscriptions of the members, a stock or fund for making advances to members out of the funds of the society upon security by way of mortgage of freehold or leasehold estate."[1] Although the legal definition in Britain (1962 Act) continues to imply that shareholders (and depositors) are members and owners, in practice this is hardly so today. In the early days "all shareholders were members and owners in a practical as well as a legal sense. Each participant was required to attend a certain number of meetings each year, or he incurred a fine; he was eligible to vote for the directors and other officers and was expected to participate at one time or another on one or more of the committees that performed the actual operations. With respect to ownership, these associations were partnerships in which all participants assumed unlimited liability for the actions of the group."[2] With the introduction of "permanent" societies and the gradual erosion of the position of "terminating" societies, however, the real meaning of membership underwent a process of change. In terminating societies, an individual's membership ceased after he had been given a loan (whose value was a fixed number of times the value of the individual's shareholdings in the society) and had repaid the principal and interest. Thus the membership of a terminating society would dwindle until theoretically there were no more members. However, towards the end of the life of each terminating society it became increasingly difficult to match the inflow of savings with the demand for loans. Another difficulty was that it was "almost impossible to obtain new members after the first year or two for the reason that..... A new member has to pay down not only the current subscriptions, but also a sum equal to the subscriptions already paid by an original member, with interest."[3] These inadequacies of terminating societies led to their replacement by permanent societies, with savers and borrowers being treated as separate entities i.e. as creditors and debtors, although to a certain extent they are still "mutual" institutions.

THE THEORY OF GROWTH OF BUILDING SOCIETIES

Building Societies are thrift institutions. For this reason it is said that the growth of building societies is partly determined by the extent

1 Wurtzburg & Mills: *Building Society Law*, Stevens & Sons, 1964, pp. 1-2.

2 A. Teck: *Mutual Savings Banks & Savings and Loan Associations*, Columbia University Press, 1968, p. 31.

3 S. J. Price: *Building Societies. Their Origin and History*, W. Heffer and Sons, Cambridge, England. 1958, p. 113.

to which building societies can effectively compete with other thrift institutions, such as time and savings deposits at commercial banks and deposits at the Government Savings Bank, credit unions, cooperative societies, etc. The main competitor is said to be the commercial bank. Competition can be price or non-price in nature. Price competition refers to the differences in rates of interest that building societies and banks are prepared to pay their creditors. Non-price competition may refer to the safety, speed and convenience of withdrawal facilities and the eager favouring of loan requests of those who already hold deposits.

In a stimulating article, D. A. & C. P. Alhadeff have attempted to show that non-price factors are more important than price differentials for explaining the faster growth of savings and loan associations (S.L.A., called building societies in the U.K.) in the U.S.A., compared with the time and savings deposits of commercial banks. Some of the non-price factors stressed are: (i) "The preference function of individual savers has changed. Although the slopes of the rate of return curves decreased, the slopes of the indifference curves decreased still more. This relative change induced some small savers to shift from time deposits to share accounts. For similar reasons large savers have also shifted accounts,"[4] (ii) the size of average savings accounts of individuals has risen at both institutions but, because of different slopes of the indifference curve for different savings levels, there has been a shift of some savings from commercial banks to S.L.A. (iii) people had forgotten the heavy losses that share accounts had suffered during the depression of the 1930s and therefore did not attach much risk to the holding of those accounts (iv) because people had a strong demand for housing, they were likely to save in an institution at which preference would be given to their application over others for a mortgage loan, other things being equal and (v) the salesmanship of S.L.A. was much more vigorous than that of commercial banks.

Marvin Rozen, however, disagrees with the view of D. A. & C. P. Alhadeff that interest rate differentials are not important and states that they have not made a distinction between the amount of risk people think they are assuming and the amount actually assumed and that "it does not seem likely that willingness to assume greater risk plays an important role in explaining S.L.A. growth. If people are more willing to assume risk, other outlets for their funds give ample scope for realization of this shift in their preferences. Contrariwise, people have more likely come to believe that funds in S.L.A. are becoming as safe as funds in commercial banks. Hence it is not a constant risk differential (based on favourable experience) and an unchanging attitude that explain the shift in the savings flows."[5]

The above controversy can hardly be resolved conclusively since it contains a subjective behavioural factor. Later on in this chapter, we

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4 D. A. & C. P. Alhadeff: "The struggle for commercial bank savings," *The Quarterly Journal of Economics*, Feb., 1958, p. 8.

5 M. Rozen: "Competition among Financial Institutions for Demand and Thrift Deposits", *The Journal of Finance*, May, 1962, p. 325.

shall attempt to get away from the indeterminacy of this argument by devoting more time instead to examining changes in the value of share and deposit holdings at building societies in the Caribbean and trying to correlate these changes with movements in the rate of interest that building societies themselves offer, in order to see whether these interest rate movements partly account for any changes in the ratio of share to deposit holdings in building societies.

Another factor that might possibly contribute to the substitution of time deposits at building societies is the interest rate on Treasury Bills and very short bonds; E. J. Stevens[6] says that there is some evidence that the interest rate does have an effect on time deposits but it is difficult to test this hypothesis in the Caribbean because Treasury Bills and short-bonds have only been readily available in the three territories in recent times.

GROWTH OF BUILDING SOCIETIES IN THE CARIBBEAN.

The apparent growth rate of building societies is of course determined partly by the size of their savings at the beginning of the period under review. For example, if in year one the savings were only 1 unit in value and in year two 2 units, there would be a 100% increase. But to base conclusions on this may be quite misleading. Table 3.1 indicates that at the beginning of the period for Guyana and Trinidad (but not for Jamaica) building society savings were low relative to savings at the commercial banks and the Government Savings Bank; it is also noticeable that building societies are a relatively less unimportant financial intermediary in Guyana than in Trinidad. Table 3.2 shows that the ratio of building society saving to commercial bank time deposits remained fairly constant during the period, for Guyana and Trinidad; the ratio fell in Jamaica, despite the rapid growth of building society saving, because of the even more rapid increase of commercial bank time deposits.

A number of possible reasons can be offerred for the relatively small amount of building society savings in Guyana and Trinidad: One reason might be that because there is only one society in Guyana and Trinidad, and this society is located in the capital, only savings in one major urban area are effectively tapped and that there may be savings in other urban and rural areas going a begging. In Jamaica, however, there are a number of societies, although their geographic location may not be ideal. The difference in building society market structure between Guyana and Trinidad and Jamaica raises the question whether the economies of scale of a single unit (re buildings, personnel etc.) are not being more than fully offset by the economies of strategic location. An alternative to having many societies is to have a system of branch societies, especially since the existence of many societies does not rule out the possibility of collusion.

A second reason why building societies grew much more slowly in Guyana and Trinidad than in Jamaica may be that, until very recently,

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6 See E. J. Stevens: "Deposits at Savings and Loan Associations," *Yale Economic Essays*, Fall, 1966.

TABLE 3.1a Changing Importance of Building Society Saving and Commercial Bank Time Deposits, Guyana.

Year	G.D.P. $m	Commercial Bank Time Dep. $000	Commercial Bank Time Dep. as a % of G.D.P.	Building Society Shares & Dep. $000	Building Society Shares & Dep. as a % of G.D.P.
1954	191.7				
1955	191.3	509	0.3	2,303	1.2
1956	207.0	1,195	0.6	3,238	1.6
1957	231.7	782	0.3	4,050	1.7
1958	234.1	2,072	0.9	4,539	1.9
1959	239.4	1,519	0.6	5,721	2.4
1960	263.5	1,039	0.4	6,918	2.6
1961	289.8	1,511	0.5	6,986	2.4
1962	307.2	5,046	1.6	6,032	2.0
1963	275.4	10,122	3.7	5,442	2.0
1964	302.9	9,754	3.2	4,764	1.6
1965	328.3	11,473	3.5	5,578	1.7
1966	347.0	12,799	3.7	6,269	1.8
1967	378.5	16,343	4.3	7,018	1.9
1968	406.7	20,471	5.0	7,439	1.8

TABLE 3.1b Changing Importance of Building Society Saving and Commercial Bank Time Deposits, Trinidad.

Year	G.D.P. $m	Commercial Bank Time Dep. $000	Commercial Bank Time Dep. as a % of G.D.P.	Building Society Shares & Dep. $000	Building Society Shares & Dep. as a % of G.D.P.
1954	430.6	11,723		5,113	1.2
1955	499.4	16,345	3.3	4,982	1.0
1956	556.3	17,817	3.2	4,948	0.9
1957	659.1	37,065	5.6	4,941	0.7
1958	719.4	16,570	2.3	5,176	0.7
1959	799.1	19,744	2.5	5,459	0.7
1960	865.9	24,456	2.8	5,937	0.7
1961	954.8	17,112	1.8	5,897	0.6
1962	1005.7	24,569	2.4	5,929	0.6
1963	1094.2	33,916	3.1	6,666	0.6
1964	1148.6	29,665	2.6	6,990	0.6
1965	1188.0	37,516	3.2	7,410	0.6
1966	1326.5	45,887	3.5	7,643	0.6
1967	1377.9	55,221	4.0	8,453	0.6
1968	1527.5	77,049	5.0	8,647	0.6

Notes: 1967 and 1968 figures are provisional.

TABLE 3.1c Changing Importance of Building Society Saving and Commercial Bank Time Deposits, Jamaica.

Year	G.D.P. $m	Commercial Bank Time Dep. $000	Commercial Bank Time Dep. as a % of G.D.P.	Building Society Shares & Dep. $000	Building Society Shares & Dep. as a % of G.D.P.
1954	574.6				
1955	654.7				
1956	760.8				
1957	921.1				
1958	593.8	11,371	1.2		
1959	1018.1	11,760	1.2		
1960	1033.9	13,360	1.3		
1961	1107.4	22,982	2.1	34,200	3.1
1962	1152.5	29,054	2.5	37,100	3.2
1963	1224.0	45,648	3.7	43,100	3.5
1964	1313.8	45,034	3.4	50,100	3.8
1965	1421.8	49,080	3.5	56,100	3.9
1966	1548.0	67,382	4.4	61,500	4.0
1967	1615.2	72,984	4.5	71,500	4.4
1968		112,354			

Source: Central Bank Bulletin, Guyana, Annual Statistical Digest, Trinidad and Monetary Statistics, Jamaica.

TABLE 3.2 Rate of Growth of Shares and Deposits Saving in Building Societies, Guyana, Trinidad and Jamaica. $000 (E.C.)

	GUYANA				TRINIDAD				JAMAICA			
Year	Building Society Shares	Rate of increase of Building Society Shares	Building Society Deposits	Rate of increase of Building Society Deposits	Building Society Shares	Rate of increase of Building Society Shares	Building Society Deposits	Rate of increase of Building Society Deposits	Building Society Shares	Rate of increase of Building Society Shares	Building Society Deposits	Rate of increase of Building Society Deposits
1945					2,429		2,561					
1950					2,214	−8.9	2,588	1.1				
1951					2,404	8.6	2,551	−1.4				
1952					2,668	11.0	2,302	−9.8				
1953					2,680	0.4	2,286	−0.7				
1954					2,744	2.4	2,369	3.6				
1955	1,839		464		2,633	−4.0	2,349	−0.8				
1956	2,623	42.6	615	32.5	2,895	10.0	2,053	−12.6				
1957	3,448	31.5	602	−2.1	2,870	−0.9	2,071	0.9				
1958	3,857	11.9	682	13.3	3,080	7.3	2,096	1.2				
1959	4,634	20.1	1,087	59.4	3,347	8.7	2,112	0.8				
1960	5,513	19.0	1,405	29.3	3,608	7.8	2,229	5.5				
1961	5,027	−8.8	1,960	39.5	3,730	3.4	2,167	−2.8	17,000		17,200	
1962	4,415	−12.2	1,617	−7.5	4,018	7.7	1,911	−11.8	19,100	12.4	18,000	4.7
1963	3,899	−11.7	1,543	−4.6	4,453	10.8	2,213	15.8	22,800	19.4	20,300	12.8
1964	3,501	−10.2	1,263	−18.1	4,723	6.1	2,267	2.4	26,300	15.4	23,800	17.2
1965	3,983	13.8	1,595	26.3	5,021	6.3	2,389	5.4	30,200	14.8	25,900	8.8
1966	4,548	14.2	1,721	7.9	5,160	2.8	2,483	3.9	34,700	14.9	26,800	3.5
1967	5,012	10.2	2,007	16.6	5,616	8.8	2,837	14.3	41,600	19.9	29,900	11.6

Source: Central Bank Bulletin, Guyana, Annual Statistical Digest, Trinidad and Monetary Statistics, Jamaica.

people preferred to make deposits in foreign-owned, rather than locally-owned, financial institutions, partly because they had more confidence in these foreign intermediaries being able to relieve any "run" on their funds by borrowing from the metropolitan parent firm. This attitude was perhaps less prevalent in Jamaica because their first building society was set up as long ago as 1864. But it seems as though many people in Guyana and Trinidad prefer to hold time deposits at commercial banks rather than save in building societies.

A third reason is that people probably felt that the asset portfolio of the building society in Guyana and Trinidad was fairly risky in that it consisted mainly of mortgages (since building prices were market determined) and that if there were a slump in market values in any one region the building society could not borrow from branch societies because branches did not exist; in the case of Jamaica, however, some building societies could at least borrow from others.

A fourth reason is that the "old" building society in Guyana failed in the late 1930s and this might have encouraged people to have a sceptical attitude towards building societies in Guyana, (and probably in neighbouring Trinidad.) The non-existence of a Central Bank (until recently) to give explicit or implicit undertakings of financial support (lender of last resort) certainly aggravated the situation.

A fifth reason is probably that insurance companies offer stiff competition to building societies. Insurance companies in the Caribbean have traditionally held a fairly high proportion of mortgages, because equities are not available in the form and quantity that is required and Government securities are not very marketable, because of the lack of an effective capital market. The demand for mortgage loans from building societies would therefore tend to be lower than it otherwise might have been and this would affect the ability of building societies to raise their interest rates on mortgages, which in turn would affect their ability to raise shares and deposit rates in order to attract funds. In Jamaica, on the other hand, a slightly more efficient market for equities and securities exists and these types of asset bulk larger in the portfolio of insurance companies, at the expense of mortgages.

A sixth reason might be that the interest rate differentials between shares and deposits at building societies and time and savings deposits at commercial banks are less significant in Guyana and Trinidad than in Jamaica.

Despite the six reasons cited above, it is very surprising that building societies are not more significant in Guyana and Trinidad (and to a less extent in Jamaica), since property is usually a favourite form of wealth-holding in underdeveloped countries because of the relative scarcity of other high yielding assets. Also building societies enjoy a privileged tax position relative to commercial banks and insurance companies, which are probably their main competitors.

THE LIABILITIES STRUCTURE

The main components of the liabilities structure of building societies are shares, deposits and reserves. "By issuing both deposits and

shares, building societies take advantage of the fact that some people have a more pronounced risk aversion than others and therefore prefer to hold deposits which are prior charge on the assets of the societies, though yielding a lower rate of interest than shares."[7]

Shares in a building society are not the normal type of shares but are a semi-contractual payment since the rate is fixed in advance. Usually more than one type of shares is offered by building societies and the interest rate on these varies with their liquidity or ease of withdrawal, rather than with any risk involved. In many countries, building societies started out with deposits alone constituting their liabilities; later on, the pressure of rivals caused shares to be introduced, and because of increasing competition, the changing expectations and interest consciousness of savers and the increasing ease of withdrawal, shares have tended to grow at a faster rate than deposits, so much so, that they now account for a larger percentage of total liabilities than deposits. In Britain, for example, deposits in 1967 accounted for only 5% (£322 m) of the total share and deposit capital (£6987 m) of building societies.[8] Table 3. 3 shows that for all three territories in the Caribbean shares are much greater in value than deposits, although the degree to which this is so is less for Jamaica.

Table 3. AI shows that throughout the 1946-60 period shares and deposits remained equal in size; but as was seen in Table 3. 3, since 1960 the value of shares increased much faster than deposits in Jamaica and Trinidad. Since building society deposits in these two countries still increased quickly in an absolute sense, the much faster rise of shares might be the result of higher interest rates being offered on shares in order to acquire more funds to accommodate an almost insatiable demand for mortgages. A more general reason for shares rising faster than deposits in Jamaica and Trinidad might be the greater confidence people have in building societies and it is significant that in Guyana, which was plagued by political unrest in the 1960s, the ratio of shares to deposits hardly changed between 1961 and 1967.

Table 3. 4 gives a detailed breakdown of the liabilities portfolio for the building society in Trinidad. It shows that not only has the value of shares increased at a fast rate but that deposits actually fell in an absolute sense between the period 1950 and 1963. Deposits began to rise again, from 1963 to 1966. Table 3. 5 shows that between 1963 and 1966 the deposit rate was 3 percent, which is higher than what it was in previous years and that in 1965 the interest rate (on funds held for 12 months of the year) fell from 5½ percent to 5 percent. These immediate reversals of trends in the values of shares and deposits when there was a change in the rate of interest show fairly conclusively that savers in building societies are very interest-conscious and switch funds between shares and deposit accounts (especially since the numbers of share investors and depositors moved in the

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7 J. Moreh: "Investment in Building Societies-I," *The Bankers Magazine* May, 1968, p. 281.

8 See Central Office of Information, London (British Information Services): *British Financial Institutions*. June, 1969, p. 65.

TABLE 3. 3 Assets and Liabilities of Building Societies, Jamaica, Trinidad and Guyana—1961-1967 $ m(E.C.)

		ASSETS						LIABILITIES				
	Year	Total	Cash	Treasury Bills	Real Estate Mortgages	Loans	Other	Total	Savings Deposits	Reserve Funds	Shares	Other
Jamaica	1961	37.7	0.8	0.4	33.5	0.4	2.6	37.7	17.2	2.4	17.0	1.1
	1962	41.0	0.9	0.2	36.2	0.4	3.3	41.0	18.0	3.1	19.1	0.8
	1963	47.2	2.3	0.2	40.0	0.3	2.4	47.2	20.3	3.3	22.8	0.8
	1964	54.7	1.9	0.2	46.7	0.3	5.6	54.7	23.8	3.7	26.3	0.9
	1965	61.5	1.5	0.1	53.8	0.3	5.8	61.5	25.9	4.2	30.2	1.2
	1966	67.8	1.7	—	59.4	0.3	6.4	67.8	26.8	4.9	34.7	1.4
	1967	78.1	1.9	—	68.3	0.4	7.5	78.1	29.9	5.6	41.6	1.0
Trinidad*	1961	7.0	—	—	6.7	—	0.3	7.0	2.2	0.4	3.7	0.7
	1962	7.5	—	—	7.2	—	0.3	7.5	1.9	0.2	4.0	1.4
	1963	8.1	—	—	7.7	—	0.4	8.1	2.2	0.2	4.5	1.2
	1964	8.3	—	—	8.0	—	0.3	8.3	2.3	0.3	4.7	1.0
	1965	8.5	—	—	8.1	—	0.4	8.5	2.4	0.3	5.0	0.8
	1966	9.3	—	—	9.2	—	0.1	9.3	2.5	0.3	5.2	1.3
	1967	10.0	—	—	9.8	—	0.2	10.0	2.8	0.4	5.6	1.2
Guyana	1961	8.4	—	—	1.4	7.0	—	8.4	2.0	—	5.1	1.3
	1962	7.5	—	—	0.1	6.7	0.7	7.5	1.6	—	4.5	1.4
	1963	6.8	0.1	—	—	6.0	0.7	6.8	1.5	—	4.0	1.3
	1964	6.2	0.1	—	0.1	5.3	0.7	6.2	1.3	—	3.6	1.3
	1965	7.0	0.1	—	0.9	5.7	0.3	7.0	1.6	—	4.0	1.4
	1966	7.3	0.1	0.1	6.3	—	0.5	7.3	1.7	1.0	4.6	—
	1967	8.1	0.1	0.6	7.0	—	0.4	8.1	2.0	1.0	5.1	—

* For Trinidad, government securities and some other assets are subsumed under "real estate mortgages".

Source: (1) Compilation of Commonwealth Caribbean Financial Statistics by F. Alleyne of I.S.E.R., U.W.I.
(2) For Guyana, direct request to new Building Society.

TABLE 3.4 Assets and Liabilities of Building Societies, Trinidad $000 (E.C.)

				ASSETS				LIABILITIES				
Year	Share Investors Nos.	Depositors Nos.	Borrowers Nos.	Total $000	Balances due on mortgages $000	Investment $000	Other $000	Total $000	Shares $000	Deposits $000	Balance of profit & reserves $000	Other $000
1945				5,984	4,375	1,482	128	5,984	2,429	2,561	121	874
1950				5,716	5,507	2	207	5,716	2,214	2,588	141	773
1951	7009	1968	2553	5,808	5,579	2	227	5,808	2,404	2,551	97	756
1952	7200	1950	2633	5,802	5,561	2	240	5,802	2,668	2,302	127	705
1953	3922	1948	1995	5,869	5,665	2	202	5,869	2,680	2,286	122	781
1954	4043	1945	1965	5,962	5,558	2	402	5,962	2,744	2,369	122	727
1955	4059	1927	2060	5,856	5,663	2	191	5,856	2,633	2,349	127	747
1956	3925	1949	1910	5,859	5,706	2	151	5,859	2,895	2,053	130	781
1957	3886	1956	1723	5,863	5,567	2	295	5,863	2,870	2,071	123	798
1958	4341	1882	1839	6,136	5,735	2	324	6,136	3,080	2,096	130	831
1959	4352	1871	1847	6,471	6,262	2	206	6,471	3,347	2,112	129	882
1960	4401	1749	1832	6,888	6,656	2	231	6,888	3,608	2,229	148	903
1961	4658	1026	1723	6,994	6,730	14	250	6,994	3,730	2,167	379	718
1962	5209	1746	1698	7,507	7,220	27	260	7,507	4,018	1,911	186	1392
1963	7897	1746	1788	8,060	7,741	27	292	8,060	4,453	2,213	219	1175
1964	7430	1770	1769	8,340	8,039	27	274	8,340	4,723	2,267	251	1100
1965	8130	1656	2253	8,467	8,135	27	305	8,467	5,021	2,389	285	771
1966	10806	1730	2334	9,338	9,173	27	138	9,338	5,160	2,483	305	1390
1967	8693	1765	2343	10,015	9,819	38	159	10,015	5,616	2,837	352	1,210
1968	6513	1651	1635	9,853	9,595	44	214	9,853	5,913	2,734	421	786

Notes: 1967 and 1968 figures are provisional.
Source: Annual Statistical Digest, Trinidad.

TABLE 3.5 Current Transactions of Building Societies in Trinidad $000 (E.C.)

	SHARES			DEPOSITS			ADVANCE ON MORTAGES				RATE OF INTEREST	
	Numbers	Interest Thereon	Withdrawn (including interest)	Deposits received	Interest Thereon	Withdrawn (including interest)	Advances	Repay-ments of Principal	Interest	Manage-ment expenses	On Shares	On Deposits
		$000	$000	$000	$000	$000	$000	$000	$000	$000	$000	$000
1945		226	332		31		1,672		293	48	5½ & 5½	1.4
1950		236	341		30		750		393	83	5½ & 6	1.5
1951	30,780	250	231	1,439	46	1,496	642	911	420	91	5½ & 6	1.8
1952	31,582	269	183	1,029	43	1,288	697	1,115	426	96	5½ & 5½	1.8
1953	32,829	262	448	1,211	40	1,247	673	568	421	101	5 & 5½	1.8
1954	33,448	287	451	1,055	40	1,143	631	738	448	105	5 & 6	1.8
1955	34,656	271	654	1,222	40	1,164	677	538	443	110	5 & 5½	1.8
1956	37,553	306	285	1,143	37	1,440	752	807	489	114	5½ & 6	1.7
1957	36,435	301	579	1,183	61	1,151	588	627	507	120	5 & 5½	2.9
1958	39,613	286	288	1,624	60	1,184	801	616	513	122	5 & 5	2.9
1959	42,656	314	356	1,363	61	1,346	1,111	564	536	128	5 & 5	2.9
1960	45,907	343	381	1,217	59	1,321	1,102	388	599	134	5 & 5	2.9
1961	51,349	356	443	1,867	48	1,292	1,098	1,099	608	151	5 & 5	3.0
1962	54,487	373	291	1,240	56	1,315	1,200	667	643	150	5 & 5	3.0
1963	61,264	432	279	1,681	70	1,267	1,319	390	716	155	5 & 5½	3.0
1964	66,193	463	464	1,182	42	1,158	1,186	906	779	168	5 & 5½	3.0
1965	67,890	473	462	1,192	88	1,279	974	876	772	174	5 & 5	3.0, 3.33 & 4.0
1966	71,209	498	653	1,332	113	1,238	1,771	849	837	183	5 & 5	4 & 6

Source: Annual Statistical Digest, Trinidad.

same direction as values.) This raises the question of whether perhaps building societies, by increasing one or more of their interest rates, do not attract new savings but merely increase their cost of acquiring the same volume of funds. "Bank reluctance to compete on savings rates can also be explained on the grounds that no opportunity to discriminate is provided—the intramarginal savers receive a 'free ride' as all savers benefit from high rates. Of course, this affects S.L.A. too, as is shown by the numerous ingenious schemes for giving the long-term saver some preferential reward and utilizing premiums to attract marginal savers without disturbing too much those already holding accounts."[9]

The differentiation of shares, in Guyana for example, into $5.00 shares, subscription investment shares, fully paid-up shares and bond certificates, is an attempt, under competitive conditions, to attract more savings but at the same time keep down costs. Now, is this practice good for the financial system, fair to savers and economically worthwhile to building societies? J. Moreh thinks that the attempt by building societies to maintain their liabilities more liquid than competing deposits is useful for the financial system because it fills a gap in the range of liquidities. There is some controversy as to whether the paying of a higher rate on fixed-term deposits (or as is sometimes proposed, the paying of a higher rate the bigger the deposit) is more fair than paying the same interest rate, irrespective of the period of deposit. However the paying of a higher interest rate to attract more funds could reduce the marginal rate of "profit" if the interest rate on mortgages is not also raised.[10] But "the practice is in keeping with building society pricing policy which allows loss at the margin. Building societies do not seek profit as such and their aim seems to be the maximization of mortgage loans (subject to restriction on the level of mortgage rate.) This aim does not entail equality between marginal cost and marginal revenue but between average cost and average revenue, in which case marginal cost may exceed marginal revenue."[11]

Table 3.6 shows that the bulk of shares in Guyana is $5.00 shares, and this preponderance has increased, possibly because of movements in the rate of interest. In 1956, the rate of the $5.00 shares increased from 3½ percent to 4 percent and there was a significant rise in $5.00 shares and a significant fall in subscription investment shares, whose interest had remained at 3½ percent. When there was a further increase in $5.00 shares by ½ percent to 4½ percent in 1957, the same thing happened despite the fact that subscription investment shares also increased by ½ percent. There was a similar occurrence in 1959 when $5.00 shares rose by another ½ percent to 5 percent and subscription investment shares continued to fall, even though

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9 M. Rozen: *Op. Cit.*, p. 327.

10 See J. Palmer: "Tougher competition for Building Societies," *The Bankers Magazine*. April, 1968.

11 J. Moreh: "Investment in Building Societies—II, *The Bankers Magazine*, June, 1968. p. 343.

TABLE 3.6 Structure of Share Capital Element in Liabilities of the New Building Society, Guyana. $(E.C.)

	$5.00 SHARES						
		SHAREHOLDERS					
Year	Total Value of $5.00 shares	Private Financial Institutions	Business Firms	Individual Customers	Other Customers	Total No. Sold	Rate of Interest Paid
1945	35,310	—	—	34,251	1,059	7,062	3%
1950	573,603	80,304	137,665	344,162	11,472	114,720	3%
1955	1,839,141	257,480	441,394	1,103,484	36,783	367,828	3½%
1956	2,622,995	236,070	524,598	1,836,097	26,230	524,599	4%
1957	3,447,830	241,348	517,175	2,654,829	34,478	689,566	4½%
1958	3,856,605	269,962	578,491	2,969,586	38,566	771,321	4½%
1959	4,634,450	324,411	695,168	3,568,527	46,344	926,890	5%
1960	5,512,589	385,881	826,888	4,244,694	55,126	1,102,517	5%
1961	5,026,806	351,876	754,021	3,870,641	50,268	1,005,361	5% + 5½% + 6%
1962	4,414,848	309,039	662,228	3,399,432	44,149	882,969	5% + 5½% + 6%
1963	3,898,894	272,923	584,834	3,002,148	38,989	779,778	5% + 5½% + 6%
1964	3,500,598	245,042	525,090	2,695,460	35,006	700,119	5% + 5½% + 6%
1965	3,983,453	278,842	597,518	3,067,259	39,834	796,690	5% + 5½% + 6%
1966	4,548,079	318,365	682,212	3,502,021	45,481	909,615	5% + 5½% + 6%
1967	5,011,680	350,818	751,752	3,858,994	50,116	1,002,336	5% + 5½% + 6%

Table 3.6 (continued)

Year	SUBSCRIPTION INVESTMENT SHARES			FULLY PAID INVESTMENT SHARES		BOND CERTIFICATES	
	Total Value of Subscription Investment shares	No. of Shares Sold	Rate of Interest Paid	Total Value of Fully Paid Investment Shares	Rate of Interest	Value of Bond Certificates	Rate of Interest Paid
1945	111,859	1,118	3%	27,563	2%	66,014	3½%
1950	157,828	1,578	3%	8,545	2%	38,898	3½%
1955	153,484	1,534	3½%	5,083	2%	32,936	3½%
1956	117,003	1,170	3½%	3,371	2%	26,336	3½%
1957	108,778	1,087	4%	2,707	2%	21,059	3½%
1958	111,487	1,114	4%	2,541	2%	18,974	3½%
1959	117,778	1,177	4%	2,332	2%	16,373	3½%
1960	111,126	1,111	4½%	1,375	2%	14,507	3½%
1961	95,043	950	4½%	641	2%	9,703	3½%
1962	82,139	821	4½%	644	2%	9,730	3½%
1963	58,190	581	4½%	654	2%	9,035	3½%
1964	47,452	474	4½%	663	2%	8,482	3½%
1965	52,795	527	4½%	659	2%	8,496	3½%
1966	48,891	488	4½%	646	2%	6,504	3½%
1967	51,056	510	4½%	677	2%	6,397	3½%

Source: Special Request, the New Building Society, Guyana.

the rate increased by ½ percent in 1960 to 4½ percent. (Because the interest rate differential was narrowing, percentage-wise, this phenomenon might imply a perverse situation where savers have a rising marginal utility with respect to income from interest or that a time lag existed.) But from 1961 to 1965, because of civil disturbance, $5.00 subscription investment shares, fully paid investment shares and bond certificates fell, even though the rate rose on $5.00 shares and remained steady on the others. The trend was reversed from 1965 for $5.00 shares and perhaps from 1967 for subscription investment shares. Despite the fact that civil disturbances began in 1962 and ended in 1964, at the end of 1967 the value of $5.00 shares was still not back to the 1961 level. This illustrates the view that savings or savers, once lost to an institution are difficult to recapture in a strongly competitive situation.

The increase of the interest rate to 6 percent for those who did not make any withdrawals for the year and the increase to 5½ percent for those savers who did not withdraw more than $250 (or 10 percent of their funds, whichever was the more) did not prevent a substantial fall in building society savings during the disturbance period in Guyana; note also that in Trinidad, when the rate of interest on shares fell from 6 percent to 5½ percent in 1952, the number of investors fell from 7,200 to 3,922 and this number of 7,200 was not again surpassed until 1963. It is not surprising that share-holding is so interest sensitive since, as Table 3.6 indicates, the holders are either private financial institutions, business firms or large individual savers who are the type that would be interest-conscious.

Deposits, as has been indicated earlier, have been falling in relative importance mainly because of the switching between deposits and shares and also because of the competition from other thrift or savings institutions. It is possible that deposit accounts are intrinsically more stable than share accounts (even if the data do not indicate this for the Caribbean territories for the period under review) because depositors, who are usually less well off than share investors, tend to be risk averters, whereas share investors are willing to shift their funds between financial institutions in order to gain a higher rate of interest. However, as Table 3.4 points out for Trinidad, the average size of both deposits and share accounts has increased and this development would tend to increase the instability of building societies' liabilities (for example, savings from five persons totalling $5,000 are likely to be more stable than those of a single person saving $5,000). Stable balances require lower liquidity and lower operating and administrative costs and so building societies would prefer to secure all their required funds via deposits; however, in a competitive financial situation, this is not possible, and so building societies have to outbid their competitors in order to retain (and attract more) share accounts. This in turn may cause interest rates on mortgages to be higher than they might otherwise be. Certainly there are circumstances (e.g. if the advertising efforts of each financial firm merely offset one another without increasing total saving in the community) when excessive competition can be harmful for the whole community.

Table 3.7 shows that for the building society in Guyana, the largest

number of accounts are still of the small size type (up to a $1,000) but that the highest percentage increases in the number of accounts have occurred in the $1,000 to $7,000 range. This shows that the traditional nature of building societies is changing and that the depositors of funds are increasingly the interest-conscious well-to-do class. This does not rule out the possibility that an individual may regard the share and the deposit as a joint product and have both types of account.

Table 3.7 (and previously Table 3.4) also indicates that even though *per capita* income is relatively small the "penetration" of building society saving is very low in the Caribbean. In 1966 in Trinidad, the number of depositors was 2,334 and the number of share investors was 10,806 in a population of over 900,000, and in Guyana the number of depositors in 1967 was 2,368 in a population of 670,000; whereas in Britain in 1967, shareholding investors numbered 7,397,000 and depositors 596,000 in a population of 56 million.

The third important component of the liabilities structure is the reserve fund. A reserve fund is held in order that building societies would be able to (a) meet and accommodate without unusual delay, any sudden increase in the demand for withdrawals, (b) cover a possible fall in the price of securities or the price of defaulting properties that might have to be sold (but when demand exceeds supply, which is usually the case, the incidence of defaulting properties, and so need for reserves, is expected to be less.) Table 3.3, previously referred to, shows that Jamaica has a much higher reserves/total deposits ratio than Trinidad. One reason for this might be the difference in market structure. Because Trinidad has only one building society, it can benefit from economies of scale in reserve holding, whereas in Jamaica each society has to hold a certain minimum of reserves, independent of the size of holdings of other societies. In Britain, in 1963, the reserve percentage for societies with assets exceeding £100 million was 3.99 percent; for societies with assets between £5 million and £10 million it was 5.40 percent. In fact, the bigger the building society (a) the smaller is the required reserve ratio; and (b) the smaller is the percentage loss on mortgage forfeitures.[12] The reserve ratio would also depend on the ratio of shares/deposits and the ratio of fixed term shares/other shares; for example, a relatively small value of deposits would increase the need for reserves, as would a relatively low value of fixed term shares. The optimum size of the reserve ratio would also depend on the ratio of government securities/total assets and the maturity distribution of these government securities. Thus, while we agree with Dr. Thomas[13] that the non-marketability of mortgages and securities in Guyana, the absence of a lender of last resort, the low number of depositors and therefore the high average size of deposits and the relatively low reserves/total liabilities ratio were important factors contributing to the building society crisis in Guyana during the period 1961-63,

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12 See J. Moreh: *Op. Cit.*—I.

13 See. C. Y. Thomas: *Op. Cit.*, p. 126. The liquidity problem in building societies stems essentially from the fact that they borrow short and lend very long.

TABLE 3.7 Structure of Deposit Element in Liabilities of the New Building Society, Guyana $ (E.C.)

		SIZE, VALUE AND NUMBER OF DEPOSITS					
		Up to $100	Between 100-500	Between 500-1,000	Between 1,000-2,000	Between 2,000-3,000	Between 3,000-4,000
Year	Total Value	Value No. (2)	Value No. (3)	Value No. (4)	Value No. (5)	Value No. (6)	Value No. (7)
1945	68,315	$16,396-163	14,346- 77	12,978- 25	8,198- 8	5,466- 2	6,832- 2
1950	149,458	35,870-358	31,386-156	28,397- 56	17,935- 16	8,968- 3	7,473- 2
1955	463,991	83,518-835	92,798-468	88,158-172	64,959- 64	32,479- 16	27,839- 9
1956	614,886	110,679-1106	104,531-522	92,233-184	86,084- 86	49,190- 24	43,042-13
1957	601,720	96,275-962	90,258-451	102,292-204	78,224- 78	54,155- 27	48,138-12
1958	682,146	109,143-1091	102,322-566	115,965-279	88,679- 88	61,393- 30	54,572-16
1959	1,087,442	152,242-1521	141,367-763	130,493-222	119,619-119	108,744- 51	97,870-32
1960	1,404,638	140,464-1404	182,603-913	168,556-335	154,510-154	140,464- 70	126,417-42
1961	1,960,039	156,803-1567	176,404-880	196,004-380	215,604-215	235,205-117	254,805-84
1962	1,617,466	129,397-1290	145,572-726	161,747-310	177,921-175	194,096- 96	210,271-69
1963	1,543,499	123,480-1233	138,915-690	154,350-305	169,785-168	185,220- 91	200,654-66
1964	1,263,423	100,796,1006	113,396-595	125,995-249	138,595-136	151,194- 71	167,263-54
1965	1,595,398	98,423-976	110,726-552	123,029-244	135,331-134	147,634- 69	159,937-52
1966	1,721,177	98,443,980	110,749-550	123,054-243	135,560-133	147,665- 72	159,971-51
1967	2,006,964	111,541-1108	125,485-624	139,428-276	153,370-149	167,313- 82	181,256-82

Table 3.7 (continued)

Total Value	Year	SIZE, VALUE AND NUMBER OF DEPOSITS											
		Between 4,000-5,000		Between 5,000-7,000		Between 7,000-10,000		Between 10-15,000		Between 15-20,000		Above 20,000	
		Value (8)	No.	Value (9)	No.	Value (10)	No.	Value (11)	No.	Value (12)	No.	Value (13)	No.
1945	68,315	4,099	1	—		—		—					
1950	149,458	8,967	2	10,462	2	—		—					
1955	463,991	18,560	4	23,200	4	18,560	2	13,920	1				
1956	614,886	41,489	10	30,744	6	24,596	3	32,297	3				
1957	601,720	42,120	10	36,103	7	30,086	4	24,069	2				
1958	682,146	47,750	11	40,929	8	34,107	4	27,286	2				
1959	1,087,442	86,995	21	76,122	15	65,246	9	54,373	5	32,623	2	21,748	1
1960	1,404,638	112,372	28	98,325	19	84,278	12	70,232	7	84,278	5	42,139	2
1961	1,960,039	156,803	38	117,602	23	98,002	13	137,203	13	117,602	7	98,002	4
1962	1,617,466	129,397	31	97,048	18	80,873	11	113,223	11	97,048	6	80,873	4
1963	1,543,499	123,480	30	92,610	17	77,175	10	108,045	10	92,610	6	77,175	3
1964	1,263,423	100,796	23	75,598	15	62,998	8	88,197	8	75,597	5	62,998	3
1965	1,595,398	98,423	21	73,817	13	61,514	8	86,120	8	73,817	5	426,627	4
1966	1,721,177	98,443	24	73,883	14	61,527	8	86,138	8	73,833	4	552,161	5
1967	2,006,964	181,256	59	83,657	16	69,714	9	97,599	9	83,657	5	682,402	5

Source: Special Request to the New Building Society, Guyana.

there are many other factors that need to be taken into account. Of course, like commercial banks, building societies will always try not to have an unnecessarily large reserve ratio; e.g. when commercial banks have a high ratio they confer a "considerable advantage on bank shareholders as against depositors and borrowers."[14]

THE ASSET STRUCTURE

The asset structure of building societies is a relatively simple one to understand as these societies consider it their role to provide as high a percentage (of total assets) of mortgage loans as possible. They therefore only hold government securities as (a) a reserve to meet any sudden increase in the demand (which is sometimes discontinuous) for mortgage loans (b) a means of obtaining liquid funds in the event of a rapid rise of withdrawals by share investors and depositors and (c) an outlet for funds when mortgage demand is low. Cash and Treasury Bills are held mainly to pay interest and to satisfy sudden increases in withdrawals, which tend to be equivalent to a significant percentage of share and deposit liabilities in any one year (in fact, investors tend to make significant use of ease of withdrawal facilities.) Non-mortgage loans are usually given, upon the security of their investing shares, only to share investors who may find themselves in temporary difficulties. In the building society's view these loans are preferable to withdrawals since funds once lost are difficult to regain.

Despite these limitations on portfolio operation, building societies still manage to maintain a very high mortgages/total assets ratio. Table 3.8 for Guyana, shows that the value and size of mortgage loans vary very widely. However, the number of loans granted for amounts of less than $5,000 is nearly 2½ times the number of over $5,000 loans. Since in the inflationary housing market very few houses cost less than $5,000 the relatively low number of over $5,000 mortgage loan raises questions about the causes and consequences of such a policy. The origin of such a policy lies in the legal regulations under which the New Building Society is empowered to make advances. These provide:

(i) that no advance in excess of three quarters of the value of the security offered shall be made;

(ii) that no advance in respect of such security shall exceed ten thousand dollars;

(iii) that no advance shall be made upon property subject to a prior mortgage or mortgages unless all such prior mortgages are in favour of the society.[15]

These very restrictive regulations would probably force mortgagors to seek a second mortgage elsewhere (although the building society would have the first lien on the property in the case of default). From

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14 Rt. Hon. Aubrey Jones: "The Report on Bank Charges—I", *The Bankers Magazine*, August, 1967. p. 61.

15 *Laws of British Guiana*, Chapter 201, P. 2966.

TABLE 3.8 Value, Size and Number of Loans, New Building Society, Guyana $(E.C.)

Year	Not exceeding $500 (1) Value	No.	Between $501-1,000 (2) Value	No.	Between 1,001-2,000 (3) Value	No.	Between 2,001-3,000 (4) Value	No.
1945	16,471	56	30,290	42	92,044	62	69,890	28
1950	18,908	62	53,472	68	185,088	126	191,834	79
1955	15,240	53	75,644	96	305,897	206	258,790	105
1956	16,826	64	80,385	101	361,789	241	354,286	142
1957	18,579	67	110,553	136	483,398	322	601,657	236
1958	15,430	71	108,737	136	491,028	327	621,488	247
1959	16,839	63	102,817	134	489,207	330	665,672	265
1960	20,711	73	114,730	146	468,627	314	733,653	294
1961	20,621	81	112,669	145	526,024	353	733,615	294
1962	24,239	91	137,650	174	520,477	348	648,365	262
1963	25,130	103	158,519	207	496,260	338	616,256	248
1964	38,466	136	137,101	188	481,688	328	641,520	256
1965	40,615	143	150,333	198	458,904	302	938,248	383
1966	39,929	172	137,274	183	492,526	317	989,235	404
1967	44,464	181	114,885	153	495,315	325	890,625	371

Table 3. 8 continued

Year	Between 3, 001-4, 000 (5) Value	No.	Between 4, 001-5, 000 (6) Value	No.	Between 5, 001-10, 000 (7) Value	No.	Exceeding 10, 000 (8) Value	No.
1945	28, 078	8	27, 483	6				
1950	133, 305	38	161, 769	36	150, 099	23		
1955	301, 283	86	298, 049	66	904, 344	131	30, 168	3
1956	451, 715	130	450, 168	101	1, 418, 392	201	10, 202	1
1957	558, 349	159	543, 552	121	1, 734, 799	248	30, 068	3
1958	612, 766	176	530, 314	119	2, 062, 271	294	60, 208	6
1959	661, 366	189	713, 059	159	2, 765, 438	396	80, 380	8
1960	740, 358	210	803, 403	178	3, 604, 401	510	110, 758	11
1961	721, 408	205	1, 016, 188	225	4, 051, 372	562	170, 146	16
1962	774, 824	221	938, 064	210	3, 509, 976	499	137, 317	13
1963	794, 726	228	848, 870	191	3, 010, 621	433	43, 909	4
1964	791, 999	226	693, 379	154	2, 432, 952	364	—	—
1965	782, 879	226	762, 726	169	2, 494, 816	373	42, 116	4
1966	735, 458	212	836, 343	186	2, 977, 954	436	140, 115	11
1967	686, 356	199	917, 179	204	3, 131, 780	449	729, 710	52

TABLE 3.8 *(Cont'd)*

Year	(9) Rate of Interest charged during year (%)	(10) Total Value of Loans made during year	(11) Total number of new loans made during year	(12) Total amount collected as repayments on loans during year.	(13) Total balances due on loans at end of year
1945	6	95,007	52	74,821	264,256
1950	7	251,226	82	183,613	894,475
1955	7	800,045	167	442,108	2,189,415
1956	7	1,389,430	310	614,080	3,143,763
1957	7	1,450,473	384	1,565,076	4,080,955
1958	7	1,057,509	146	822,147	4,502,242
1959	7	1,692,000	269	1,045,455	5,494,778
1960	7	1,896,602	280	1,194,888	6,596,641
1961	7	1,548,067	215	1,314,734	7,352,043
1962	7	Nil.	Nil.	1,222,915	6,660,912
1963	7	Nil.	Nil.	1,017,820	5,871,646
1964	7	87,162	34	1,123,062	5,217,105
1965	7	1,206,897	271	1,220,983	5,670,631
1966	7	1,635,542	264	1,373,512	6,348,834
1967	7	1,827,723	193	1,604,671	7,010,224

Source: Special Request to the New Building Society, Guyana.

a broad social point of view, the regulations make it possible for a larger number of people to get loans than might otherwise have been the case; however, the Government probably ought to make sure that it is not the relatively well-to-do who are securing these loans. Also since the poor may have difficulty in securing a second mortgage, loans on property of a value of less than $10,000 should probably be 100% of the value of the property.[16] If a person seeking a larger type of loan is relatively rich, a building society may prefer to give such a loan rather than two smaller loans, equivalent in value, because the risks would not be greater and the administrative expenses would certainly be less. In practice, most of the mortgage loans tend to go to the middle class owing to the conflict of interest between building society shareholders desiring high standards of security and working class borrowers wanting longer repayment terms and advances equal to the full value of the property; also, most of the mortgage financed houses are owner occupied, so the poor, who pay rent, are again excluded from these facilities.[17]

Table 3.8 also shows that the rate of interest on mortgages in Guyana has been surprisingly constant at 7 percent since 1950. Since the demand for mortgages must have fluctuated somewhat during this period (especially during the 1961-63 civil disturbance period) this stickiness of the rate implies either that securities holdings are a mere residual (securities holdings falling when mortgage demand rises and rising when mortgage demand falls) or that the price elasticity of demand for mortgage credit is unity. We believe that the demand for mortgages is interest elastic within a fairly wide range, that market conditions were not being allowed to operate, and that when demand increased other rationing devices (e.g. first come, first served or changes in the repayment period) were being used. The reluctance to raise the interest rate may have been out of fear of public indignation. However, if the interest rate on mortgages had been raised this would have made it possible to increase interest rates on shares even more (to attract more funds) and so make possible the satisfying of more would-be seekers of mortgage loans.[18]

Table 9 shows that, as a result of raising the interest rates on shares without also raising the mortgage rate, surplus income over expenditure had begun to fall since 1957 for the New Building Society (even

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16 The normal loan to value ratio in the U.K. is 80 percent, in Guyana 75 percent.

17 Since people's incomes rise over time, mortgages to the poor should perhaps consist of very low monthly payments in early years and correspondingly higher monthly payments in latter years. Legislation should also perhaps be introduced discriminating against mortgages for existing property (although an exception should be made for slum dwellings) since these might result in mere speculative transfers rather than the creation of new assets in the community. See E. J. Cleary: *The Building Society Movement*, Elek Books, 1965.

18 For an analysis of recent British experience in using this device, see E. D. Holmes: "Building Societies: A Record Year", *The Bankers Magazine*, May, 1969.

TABLE 3.9 Surplus Income Over Expenditure, New Building Society, Guyana $ (E.C.)

Year	Total Income (Local)	Total Income (Foreign)	Total Income (Local & Foreign)	Total Expen-diture (Local)	Total Expen-diture (Foreign)	Total Expen-diture (Local & Foreign)	Surplus Income Over Expen-diture
1945	18,353	287	18,640	18,324	—	18,324	316
1950	56,377	267	56,644	43,357	—	43,357	13,287
1955	148,507	4,704	153,211	115,160	—	115,160	38,051
1956	205,575	7,166	211,741	168,396	—	168,396	44,345
1957	277,138	8,743	285,881	220,492	—	220,492	65,389
1958	325,567	9,471	335,038	276,277	—	276,277	58,761
1959	383,689	13,045	396,734	323,638	—	323,638	73,096
1960	441,474	16,732	458,206	412,555	—	412,555	45,651
1961	541,135	14,782	555,917	458,978	—	458,978	96,939
1962	529,700	10,572	540,362	452,604	15,392	467,996	72,366
1963	484,944	6,067	491,011	411,450	—	411,450	79,561
1964	419,994	6,069	426,063	377,078	—	377,078	48,985
1965	415,625	10,284	425,909	396,390	—	396,390	29,519
1966	441,872	23,546	465,418	435,300	—	435,320	30,098
1967	470,059	34,702	504,761	477,026	—	477,026	27,735

Source: Special request to the New Building Society, Guyana.

TABLE 3.10 Velocity of Turnover of Mortgage Loans, Trinidad and Britain

	TRINIDAD ($M)			BRITAIN (£M)		
Year	Mortgage Advances	Balances due on Mortgages	Velocity	Mortgage Advances	Balances due on Mortgages	Velocity
1950	0.750	5.507	0.1362	269.7	1059.8	0.2545
1955	0.677	5.663	0.1195	394.4	1752.0	0.2251
1960	1.102	6.656	0.1656	559.4	2647.7	0.2113
1965	0.974	8.135	0.1197	955.4	4544.7	0.2102

Source: (1) Annual Statistical Digest, Trinidad

(2) Report of the Chief Registrar of Friendly Societies for 1967.
Part 2: Building Societies, Britain

before the 1961-63 period when there were civil disturbances) and this fall continued after 1963, mainly due to expenditure increases outstripping income increases.

Finally an attempt was made to compare the "velocity of turnover of mortgage loans" in Trinidad (the only territory for which figures were available) with that in Britain. Table 3.10 indicates that the velocity of turnover (ratio of advances to balances due, about which societies are particularly concerned when funds are low) in Trinidad is relatively low, perhaps either because the period of repayment is longer in Trinidad, and there is some amount of defaulting and delays in repayment ("deliquency"), or there is a switch from mortgages to securities.

TABLE 3.A1 Building Societies, Jamaica, 1945-1960 £000 (J.)

	Liabilities	Shares	Deposits	Total Balances	Investments
1945	1613	711	657	1392	92
1946	1842	766	798	1638	69
1947	2066	810	953	1840	69
1948	2238	862	1072	2000	57
1949	2405	937	1148	2156	54
1950	2589	1048	1214	2310	61
1951	2844	1142	1338	2350	60
1952	3086	1198	1511	2733	75
1953	3441	1342	1780	3058	101
1954	3874	1468	2038	3421	110
1955	4314	1633	2267	3884	137
1956	4444	1743	2272	3981	142
1957	4748	1920	2352	4226	164
1958	4795	2202	2366	4292	187
1959	6257	2716	2931	5517	251
1960	6879	3043	3147	6087	297

Source: C. V. Callender: *The Development of The Capital Market Institutions of Jamaica.* I.S.E.R., U.W.I., 1965

CHAPTER IV

The Operations of Government Savings Banks

INTRODUCTION

Government savings banks (frequently called Post Office Savings Banks) were introduced in developed countries during the industrial revolution. "The rapid movement of people from farms to areas surrounding newly opened mines and factories created noticeable increases in unemployment. Many families previously relying on farming or on association with a farming community for their daily needs now found themselves with neither funds nor land nor benefactors."[1] Many workers, who previously eked out a semi-subsistence living in rural areas, now found themselves in the hurly-burly of an urban and monetary economy and desired to save small amounts for a rainy day, after satisfying their subsistence needs. The private commercial banks were situated in only the main commercial centres and a few of the larger industrial towns and so were not easily accessible to many potential savers, or were not operationally designed to cope with the small intermittent savings of the many marginal savers.

Government savings banks were introduced in the Caribbean in the second half of the 19th century. The Government Savings Bank of Jamaica was introduced in 1870, directly as a result of a series of forgeries by the Secretary of the Trelawny (private) Savings Bank; and in Guyana the Government Savings Bank was introduced in 1889. These banks were introduced primarily in order to capture the intermittent savings from fluctuating agricultural incomes, to encourage a money economy and to reduce the incidence of hoarding. In the second quarter of the 20th century, the increasing number of branches was justified on the grounds that more people were desirous of saving in an institution which was safer than the private commercial banks, amongst whose counterparts in Europe and America there were frequent failures during the slumps and depressions of the period. Since the Second World War, Caribbean Governments have further increased the number of branches, not only to satisfy the needs of savers in many remote areas, but also to increase the sources of cheap funds for their development programmes (being now perhaps, less prisoners of the balanced budget doctrine.) It was also believed that many small deposits would be less volatile than the comparatively few large deposits in commercial banks.

There are many factors that can influence the volume of savings in government savings banks: on the basis of these factors we can probably formulate theories, and these theories tend to be more complementary than competitive. One theory is that the depositors at a government savings bank are those who think that their incomes are

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1 A. Teck: *Op. Cit.*, p. 5

"transient" and discontinuous and therefore demand safety and security (from the institution for their saved funds) more than interest. A government savings institution is thought to be more secure and more capable of bearing transferred risk than a private institution. Since these savings will be run down when income ceases to be earned, this is a precautionary theory in disguise. A second theory is that those who save in a government savings bank are "target savers", who are not concerned with interest but merely wish to save a certain amount, for purposes of safety, after which they consume all their income.[2] This is a sort of "static theory of saving" and is sometimes used to explain the slow growth of savings in government savings banks in some other countries. A third theory is that a person saves in a government savings bank only if his income is below a certain level. When, with the passing of time, his income surpasses this level and new tastes are acquired, he becomes less of a risk averter and also demands services complementary to the act of saving e.g. the individual would wish to save in an institution where he can get a loan (if he so desires) on the basis of his savings. The importance of this "level of income" theory would partly depend on the existing and changing distribution of income.

Because the growth rate of government savings banks since the War has varied widely between Caribbean countries (and between non-Caribbean countries), other factors might also be important (besides the above theories) in determining the growth of government savings banks e.g.the relative size of interest rates, and non-price factors such as the degree of advertising, the number, attractiveness and location of branch premises, speed of withdrawal facilities etc. Broader economic factors, such as the relative growth rates of the urban and rural sectors, increases in the number of people employed, changes in number of pay days (e.g. weekly payments instead of a single monthly payment) may also be important.

GROWTH OF GOVERNMENT SAVINGS BANKS IN THE CARIBBEAN

In order to assess the relative importance of government savings banks in the Caribbean, we calculated government savings banks deposits and commercial bank deposits as percentages of G.D.P. Table 4.1 shows that the Government Savings Bank has much greater importance to the Guyana economy than to the Trinidad or Jamaica economy; in Trinidad the Government Savings Bank has least importance. Table 4.1 also shows that in Guyana, and in Trinidad, the Government Savings Bank was increasing in importance for most of the 1950s, whereas in Jamaica the Government Savings Bank was decreasing in importance. But in the 1960s, when the Government Savings Bank was declining in importance in both Guyana and Trinidad, the Bank's position remained stable in Jamaica. We may note also that, in Guyana, when the Government Savings Bank was expanding,

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2 This theory is somewhat similar in nature to that of A. Spiro: "Wealth and the Consumption Function," *Journal of Political Economy*, August, 1962 and is an attempt to explain the very large number of "dormant" accounts at the government savings banks, in the Caribbean.

TABLE 4.1 Government Savings Bank Deposits and Commercial Bank Deposits as Percentages of G.D.P., Guyana, Trinidad and Jamaica

	GUYANA				TRINIDAD				JAMAICA			
Year	(G$M) G.D.P. at Factor Cost	(G$000) Government Savings Bank Deposits	Government Savings Bank as a % of G.D.P.	Commercial Bank Total Deposits as a % of G.D.P.	(T$M) G.D.P. at Factor Cost	(T$000) Government Savings Bank Deposits	Government Savings Banks as a % of G.D.P.	Commercial Bank Total Deposits as a % of G.D.P.	(£M) G.D.P. at Factor Cost	(£000) Government Savings Bank Deposits	Government Savings Bank as a % of G.D.P.	Commercial Bank Total Deposits as a % of G.D.P.
1950	135.0	13,755	10.2	12.7		10,572			70.1	1,698	2.4	21.7
1951	150.6	14,526	9.6	14.1		11,792			81.7	1,795	2.2	20.4
1952	158.6	15,960	10.1	13.9		12,190			95.0	2,214	2.3	18.9
1953	175.8	15,545	8.8	16.9		13,307			106.7	2,185	2.1	20.0
1954	191.7	17,184	9.0	15.9	430.6	14,365	3.3	24.4	119.7	2,385	2.0	19.6
1955	191.5	18,718	9.8	15.9	499.4	14,900	3.0	22.3	136.4	2,482	1.8	18.2
1956	207.0	18,568	9.0	15.2	556.3	14,194	2.6	21.8	158.5	2,821	1.8	18.3
1957	231.7	18,979	8.2	15.0	659.1	13,417	2.0	24.9	191.9	3,233	1.7	18.9
1958	234.1	19,993	8.5	15.9	719.4	13,264	1.8	22.6	198.7	3,741	1.9	19.2
1959	239.4	20,417	8.5	16.1	799.1	13,375	1.7	23.8	198.2	4,205	2.1	21.3
1960	263.5	21,389	8.1	16.9	865.9	13,127	1.5	22.4	215.3	5,140	2.4	20.4
1961	289.8	20,494	7.1	13.9	954.8	12,819	1.3	19.9	230.6	5,284	2.3	21.7
1962	307.2	16,988	5.5	15.9	1005.7	11,123	1.1	20.2	240.4	5,668	2.4	20.8
1963	275.4	16,806	6.1	22.7	1094.2	10,672	1.0	22.0	255.8	6,341	2.4	22.7
1964	302.9	15,703	5.2	23.8	1148.6	10,292	0.9	21.6	273.9	7,095	2.6	23.3
1965	328.3	14,258	4.3	23.8	1188.0	9,500	0.8	22.5	297.1	7,588	2.6	23.3
1966	350.9	14,597	4.2	23.8	1326.5	9,400	0.7	20.6	322.5	7,906	2.4	25.0
1967	377.5	14,739	3.9	25.0	1377.9	9,100	0.7	21.3	336.5	8,272	2.4	27.0

Source: Central Bank Bulletin, Guyana; Annual Statistical Digest, Trinidad; Monetary Statistics, Jamaica.

commercial bank deposits as a percentage of G.D.P. remained steady, but that when the Government Savings Bank was declining commercial bank deposits as a percentage of G.D.P. tended to increase. In Trinidad there was a very gradual declining trend in commercial bank deposits as a percentage of G.D.P., whereas in Jamaica the percentage remained fairly stable in the 1950s but declined in the 1960s.

However, commercial bank savings deposits, rather than total commercial bank deposits, might be considered a substitute for government savings bank deposits. Table 4.2 shows that, in the 1960s, while government savings deposits in Guyana, as a percentage of G.D.P., have been falling rapidly, commercial bank savings deposits have been increasing just as rapidly (in 1960 they were almost equal, but in 1968 commercial bank savings deposits were over four times as big). In Trinidad, commercial bank savings deposits have remained a stable percentage of G.D.P. in the 1960s, whereas in Jamaica they have risen as fast as in Guyana.

From Tables 4.1 and 4.2, it is thus seen that in the 1960s Government Savings Bank deposits have been increasing in Jamaica, but falling in both Guyana and Trinidad, and that at the same time commercial bank savings deposits have been expanding as a percentage of G.D.P. in Jamaica and Guyana but have remained fairly constant in Trinidad. There may be some reasons for these differences in growth rates. One reason may be the inadequacy of the number of Government Savings Bank branches (compared with the number of commercial banks or the number of commercial bank branches.) Thus the rapid growth in Jamaica may be due to the fact that there are now over three hundred Government Savings Bank branches in that country, whereas in Guyana in 1968 there were only 61 branches; in Guyana in the last few years, the increase in the number of Government Savings Bank branches has certainly not kept pace with the increase in the number of commercial banks and commercial banks' branches.[3] Trinidad is such a highly urbanised economy that the greater willingness of the Government Savings Bank to set up branches in rural areas does not give it a significant advantage over commercial banks, as obtains in Jamaica and Guyana. Table 4.AI shows that there might be some justification in closing down some of the less active Post Office branches in Trinidad (although a very low number of deposits does not always indicate a very low total value of deposits) and for concentrating and competing vigorously in the more rewarding urban and semi-rural areas. In the case of Trinidad, commercial bank competition is not a sufficient reason for the decline of the Government Savings Bank, since commercial bank savings deposits and commercial bank total deposits also fell as a percentage of G.D.P. This phenomenon, of course, has important implications in Trinidad for the supply of money, the money multiplier and monetary policy.[4]

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3 Here the term "branches" is being used loosely and really refers to premises, since in a sense nearly all commercial banks operating in the Commonwealth Caribbean are branches of metropolitan (foreign) firms.

4 In Trinidad, there does not seem to have been a compensating increase in "other" saving e.g. building society saving increased relatively slowly during the period.

TABLE 4.2 Government Savings Bank Deposits and Commercial Banks Savings Deposits as Percentages of G.D.P., Guyana, Trinidad & Jamaica $000 (E.C.)

	GUYANA				TRINIDAD				JAMAICA			
Year	Commercial Banks Savings Deposits	Commercial Banks Savings Deposits as a % of G.D.P.	Government Savings Bank Deposits	Government Savings Bank Deposits as a % of G.D.P.	Commercial Banks Savings Deposits	Commercial Banks Savings Deposits as a % of G.D.P.	Government Savings Bank Deposits	Government Savings Bank Deposits as a % of G.D.P.	Commercial Banks Savings Deposits	Commercial Banks Savings Deposits as a % of G.D.P.	Government Savings Bank Deposits	Government Savings Bank Deposits as a % of G.D.P.
1945			9,913				8,932					
1950			13,755	10.2	25,776		10,572				8,150	2.4
1951			14,526	9.6	26,966		11,792				8,616	2.2
1952			15,960	10.1	28,932		12,190				10,627	2.3
1953			15,545	8.8	34,172		13,307				10,488	2.1
1954			17,184	9.0	41,044	9.5	14,365	3.3			11,448	2.0
1955	12,970	6.8	18,718	9.8	46,833	9.4	14,900	3.0			11,914	1.8
1956	14,712	7.1	18,568	9.0	52,874	9.5	14,194	2.6			13,514	1.8
1957	17,443	7.5	18,979	8.2	54,010	8.2	13,417	2.0			15,518	1.7
1958	19,240	8.2	19,993	8.5	69,079	9.6	13,264	1.8	69,379	7.3	17,957	1.9
1959	20,746	8.7	20,417	8.5	78,742	9.9	13,375	1.7	77,875	7.6	20,184	2.1
1960	23,389	8.9	21,389	8.1	86,355	10.0	13,127	1.5	83,962	8.1	24,672	2.4
1961	23,030	7.9	20,494	7.1	94,662	9.9	12,819	1.3	89,923	8.1	25,363	2.3
1962	25,032	8.1	16,988	5.6	96,941	9.6	11,123	1.1	103,512	9.0	27,206	2.4
1963	30,668	11.1	16,806	6.1	106,959	9.8	10,672	1.0	125,419	10.2	30,437	2.4
1964	38,554	12.7	15,703	5.2	114,783	10.0	10,292	0.9	147,466	11.2	34,056	2.6
1965	45,636	13.9	14,258	4.3	121,047	10.2	9,500	0.8	169,757	11.9	36,422	2.6
1966	50,543	14.6	14,597	4.2	128,645	9.7	9,400	0.7	192,998	12.5	37,949	2.4
1967	56,343	14.9	14,739	3.9	140,977	10.2	9,100	0.7	221,736	13.7	39,706	2.4
1968	62,438	15.4	14,447	3.6	158,084	10.2	—	—	275,635	—	—	—

Source: Central Bank Bulletin, Guyana; Annual Statistical Digest, Trinidad; Monetary Statistics, Jamaica.

A second reason for the differences in the growth rates of Government Savings Banks in Guyana, Trinidad and Jamaica, may be political. In Guyana, deposits fell rapidly in the early 1960s as a result of civil disturbances. Given our "level of income" theory, some of these deposits, once lost, may never be regained because these depositors might have reached a level of income where saving tastes begin to change and they only continued to hold deposits at the Government Savings Bank through inertia. With a change in the political climate, therefore, they would redeposit, not in the Government Savings Bank, but in a private commercial bank. Differences in the political philosophy of development may also be important. In both Guyana and Trinidad, there may be greater fear that the Government would "manipulate" the funds for developmental purposes (making deposit withdrawal "risky") than in Jamaica, where the developmental philosophy is more "laissez-faire".

There may be other reasons for the differences in growth in the Caribbean of the Government Savings Banks, but these are more difficult to isolate: Agriculture is contributing less and less to G.D.P. and so rural incomes, and therefore savings in rural areas, where most of the Government Savings Bank branches are located, are not rising as fast; Jamaica may be trying to reduce the adverse effect on saving of a declining agricultural share by pursuing a vigorous branch bank (government) expansion to capture the marginal savings. Another reason might be that in Guyana and Trinidad the distribution of income is becoming more skewed in favour of the rich rather than the poor, who alone tend to save in the Government Savings Bank. Also, indirect (and the true incidence of direct) taxation might have been proceeding in a more regressive direction in Guyana and Trinidad; and the prices of staple goods might have been rising at a fast rate, compared with other goods. We need to know much more about the saving pattern in all other savings institutions[5] before ascribing any validity to some of the reasons offered above. Nevertheless, we can say that the overall saving behaviour in Trinidad seems rather strange, since it is the "richest" of the three Commonwealth Caribbean territories. The marginal propensity to save (i.e. "pure" savings) does not seem to be falling appreciably in the Keynesian sense or being equal to the average propensity to save in the Kuznets/Smithies[6] sense, but yet it seems as though MPS $<$ APS. However, our time period is much too short for definitive conclusions.

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5 For example, in Jamaica credit union saving, which, to some extent, competes with saving in commercial banks and government savings banks, rose even faster in the 1960s than Government Savings Bank deposits; and in Trinidad credit union saving increased while Government Savings Bank deposits fell. See also A. Salyzyn: "The Competition for Personal Savings Deposits in Canada," *Canadian Journal of Economics and Political Science*, August, 1966.

6 See A. Smithies: "Forecasting Postwar Demand," *Econometrica*, Vol. 13, January, 1945, pp. 1-14.

THE LIABILITIES STRUCTURE

Tables 4. 3 and 4. 4, representing the liabilities structure for Guyana and Trinidad, respectively, show a certain basic similarity. They both show that despite the fact that deposits has fallen, the number of deposits has not fallen at the same rate; in fact the number of deposits in Trinidad has been increasing, even if very slowly, and the absolute number of deposits in Guyana rose in 1967 and again in 1968. This, therefore, indicates that either (a) some savers with above average size deposits are ceasing to save with the Government Savings Bank; (b) some savers, although remaining as depositors, are running down their balances; (c) some savers are making smaller deposits or (d) the rate of departure of small savers is not being matched by the rate of entry of new small savers (i.e. a few very active accounts might be responsible for the bulk of the transactions) or it may be due to a combination of all four factors.

In the case of Trinidad, because the number of deposits is greater than the number of withdrawals, but the value of withdrawals is greater than the value of deposits, the average size of deposit must be smaller than the average size of withdrawal. In Guyana, on the other hand, the number of deposits has not exceeded the number of withdrawals during the 1962-66 period of decline. It is also noticeable that, whereas in Trinidad the number of deposits or withdrawals has always been far less than the number of depositors accounts when the value of deposits was falling, in Guyana, the number of deposits or withdrawals had been more than the number of depositors accounts during the pre-1961 period of expansion. This perhaps indicates that more depositors accounts are dormant in Trinidad than in Guyana. But even in Guyana, the number of dormant[7] accounts is very high. Table 4. 5 shows that 78. 3 percent of the total number of depositors at the Government Savings Bank in Guyana have accounts of $50 or less and that about 45 percent of these accounts are dormant. Thus most of the people who save in the Government Savings Bank are very small savers and are perhaps also either target savers or people who try to have at least a small sum saved (for precautionary reasons) even though their financial circumstances might be desperate. In 1965, the size of the average account in Guyana was $121, whereas in Trinidad it was $81.

Table 4. 5 also shows that in Guyana most active accounts are the relatively large accounts and these are responsible for the larger number of deposits and withdrawals already shown in Table 4. 3, especially since the average deposit or withdrawal is as high as (approximately) $80, a sum larger than the size of most accounts. Table 4. AIII shows that the people who have small accounts in Guyana are mostly housewives, labourers or low income (fixed) government clerical workers and the people who have medium or large-sized

[7] A dormant account, according to the definition used by the Government Savings Bank in Guyana, is one in which no transaction has taken place for 5 years. In December, 1968, the number of dormant accounts in Trinidad was 68. 2%, although their definition of a dormant account is slightly different from Guyana's.

TABLE 4.4 Number and Value of Deposits/Withdrawals and Investments and Other Finances of the Government Savings Bank, Trinidad $000 (E.C.)

	Deposits During Year		Withdrawals During Year		Depositors* Accounts		Reserve Fund	Total Assets or Liabilities	Investment	Management Expenses
Year	No.	$000	No.	$000	No.	$000	$000	$000	$000	$000
1936	—	1,348	—	1,056	48,608	2,475	2	2,477	2,395	18
1940	—	1,395	—	1,575	61,961	2,999	192	3,225	3,216	22
1945	69,017	4,861	55,562	3,607	79,489	8,932	502	9,434	8,695	33
1949	77,853	5,747	76,446	5,129	103,681	10,572	433	11,005	10,656	54
1951	96,677	6,589	78,698	5,607	108,559	11,792	–575	11,792	11,184	78
1952	89,727	6,294	88,479	6,152	113,639	12,190	–692	12,352	11,636	81
1953	95,870	7,043	86,761	6,191	117,971	13,307	–178	13,307	12,914	86
1954	91,026	6,863	81,195	6,091	120,787	14,365	289	14,654	13,779	87
1955	90,283	6,522	83,893	6,291	124,385	14,900	–1321	14,900	13,411	103
1956	87,855	5,472	78,376	6,482	127,131	14,194	–1860	14,696	12,798	129
1957	84,278	4,895	73,024	5,958	129,403	13,417	–2160	14,616	12,310	142
1958	80,349	4,806	67,792	5,234	131,488	13,264	–1217	14,515	13,096	281
1959	102,911	5,101	109,564	5,268	133,185	13,375	927	13,939	12,894	123
1960	74,610	4,835	66,719	5,366	134,780	13,127	1453	13,912	12,125	123
1961	72,259	4,878	63,657	5,459	135,656	12,819	1193	12,819	11,066	122
1962	58,710	3,663	62,842	5,597	135,861	11,123	503	12,578	11,483	116
1963	53,283	—	52,557	4,247	135,696	10,672	28	12,346	12,190	113
1964	51,448	—	46,488	3,603	136,997	10,292	347	12,109	11,672	114
1965	—	2,748	—	3,559	—	9,721	348	11,311	10,710	215
1966	—	2,511	—	3,154	—	9,434	343	9,644	8,782	—

* Includes interest on deposits

Source: Annual Statistical Digest, Trinidad.

TABLE 4.5 Number and Size of Active and Dormant Accounts, Government Savings Bank, Guyana $ (E.C.)

Categories	Classified Number of Accounts			
	Active	Dormant	Total	Percentage
Not exceeding $3	4,041	40,171	44,212	37.5
Exceeding $3 but not exceeding 5	11,307	9,656	20,963	17.8
Exceeding 5 but not exceeding 50	18,913	8,275	27,188	23.0
Exceeding 50 but not exceeding 100	5,256	640	5,896	5.0
Exceeding 100 but not exceeding 250	7,678	493	8,171	6.9
Exceeding 250 but not exceeding 500	5,513	210	5,723	4.9
Exceeding 500 but not exceeding 1,000	2,653	108	2,761	2.3
Exceeding 1,000 but not exceeding 5,000	2,714	97	2,811	2.4
Exceeding 5,000 but not exceeding 10,000	190	4	194	.2
Exceeding 10,000 but not exceeding 15,000	27	3	30	—*
Exceeding 15,000 but not exceeding 20,000	11	—	11	—*
Exceeding 20,000 but not exceeding 25,000 (Maximum)	3	—	3	—*
Exceeding 25,000 (Government and other authorised accounts).	6	—	6	—
Total in 1965	58,312	59,657	117,969	100.
Total in 1954	89,333	26,357	115,690	100.
Total in 1952	80,543	29,074	109,617	100.

* Percentage negligible

Source: Special Request to P.O.S.B.

accounts are mainly the rural self-employed income earners, for example small businessmen, who probably operate "semi-current" accounts and are responsible for most of the transactions at the Government Savings Bank.

The ratio of Government Savings Bank branches to population, in Guyana in 1966 was 1: 12, 000 and in Jamaica, 1: 6, 500. Even for Jamaica (See Table 4.6) this does not signify a very high "penetration ratio", since there are 21, 000 branches in the U.K., making for a penetration ratio of 1: 2, 500. Ignoring differences in per capita, and distribution of, income, the relatively large number of branches might be a reason for the rapid and sustained growth of the Government Savings Bank in Britain.

THE ASSET STRUCTURE

The asset structure of government savings banks in the Caribbean has been dominated by the legal requirement that only one-third of their funds can be invested in domestic government securities and that the remaining two-thirds must be invested in United Kingdom and Dominion or Colonial securities. This legal requirement, a product of Currency Board thinking, was supposedly intended to reinforce savers' confidence in the government savings bank; it was also thought that smaller savers, who were usually risk averters, would be more inclined to save their high utility marginal funds at an institution which backed their savings with securities of the mother country or an overseas extension of the mother country.

Until fairly recently, the Commonwealth Caribbean territories more than adhered to this legal requirement in that they held in foreign securities more than the stipulated two-thirds of their funds. But in the mid 1950s, Trinidad and Jamaica reduced their holdings of foreign securities to the required minimum and in 1957, Jamaica altered her regulations and reduced the minimum to be invested outside of the country to one-third.[8] Table 4.7, accordingly, shows that of the three territories, Jamaica is holding the largest amount of local securities, as a percentage of total assets.

Government savings banks are financial institutions which borrow short (increasingly so, given the greater and greater ease and frequency of withdrawal) and lend long. Since local securities, in the absence of an active capital market, are not as marketable as foreign, the holding of foreign securities may make possible the lengthening of the average maturity of the asset portfolio; if a greater percentage of the securities held can be long term (than would otherwise be the case) the government savings bank therefore benefits. However, the government and the rest of the community "suffer". The government suffers if, because of the small amount of local securities taken up by the government savings bank, it has to offer a lower price (higher interest) than otherwise to induce other people to hold these securities. The community as a whole suffers because funds should be lent

8 See C.V. Callender: *Op. Cit.*, p. 119.

TABLE 4.6 Numbers and Value of Deposits/Withdrawals and Investments, Government Savings Bank, Jamaica 1958-1967 £000 (J.)

	DEPOSITS		WITHDRAWALS		Excess of Deposits over Withdrawals	Depositors Accounts At March 31		Total Investment, Domestic and Foreign	Management Expenses	Reserve* Fund at end of Period
Year	No.	£000	No.	£000	£000	No.	Amount £000	£000	£000	£000
1958	264, 381	3, 741	237, 656	3, 241	500	414, 373	4, 515	3, 707	55	—
1959	247, 576	4, 205	249, 535	3, 925	280	428, 593	4, 896	4, 258	64	—
1960	258, 098	4, 750	243, 056	4, 618	132	443, 770	4, 623	5, 146	78	423
1961	238, 552	4, 857	240, 412	4, 861	—4	456, 682	5, 270	4, 537	79	553
1962	232, 796	4, 177	222, 813	4, 142	35	467, 185	5, 429	4, 736	114	594
1963	224, 820	4, 209	221, 369	3, 821	388	479, 803	5, 950	4, 760	142	599
1964	237, 150	5, 047	224, 288	4, 402	645	493, 835	6, 742	5, 637	191	332
1965	260, 776	5, 273	238, 487	4, 819	454	507, 829	7, 363	7, 057	408	182
1966	245, 753	5, 292	245, 265	5, 156	136	521, 655	7, 689	6, 710	490	112
1967	217, 513	5, 656	221, 737	5, 341	315	531, 149	8, 096	8, 290	171	36

* Includes deficiency for years 1965 and 1966

Source: Monetary Statistics, Department of Statistics, Jamaica

TABLE 4.7 Assets and Liabilities of Government Savings Banks, Guyana, Trinidad and Jamaica $M (E.C.)

		ASSETS					LIABILITIES			
								Deposits		
	Year	Total	Cash	Local	Foreign	Other	Total	Government	Savings	Other
GUYANA	1961	20.5	—	5.5	11.6	3.4	20.5	—	20.5	—
	1962	17.0	—	5.5	9.9	1.6	17.0	—	17.0	—
	1963	16.9	—	5.5	9.7	1.8	16.9	—	11.8	5.1
	1964	16.2	—	5.5	9.4	1.3	16.2	—	15.7	0.5
	1965	14.4	—	5.5	7.8	1.1	14.4	—	14.3	0.1
	1966	14.6	—	5.5	7.5	1.6	14.6	—	14.6	—
	1967	14.8	—	5.5	7.5	1.8	14.8	—	14.7	0.1
TRINIDAD	1961	12.8	0.1	1.6	8.2	2.9	12.8	—	12.8	—
	1962	12.6	0.1	1.0	8.9	2.6	12.6	—	11.1	1.5
	1963	12.3	0.1	0.5	9.0	2.7	12.3	—	10.7	1.6
	1964	12.1	0.1	0.9	8.5	2.6	12.1	—	10.3	1.8
	1965	11.3	—	0.4	7.7	3.2	11.3	—	9.5	1.8
	1966	9.4	0.1	0.3	6.0	3.0	9.4	—	9.4	—
	1967	9.3	0.1	0.7	6.0	2.5	9.3	—	9.1	0.2
JAMAICA	1961	25.4	—	16.3	9.1	—	25.4	2.8	22.0	0.6
	1962	27.4	—	18.7	8.7	—	27.4	2.8	24.5	0.1
	1963	31.2	—	22.0	9.2	—	31.2	2.8	27.4	0.1
	1964	35.0	—	24.9	10.1	—	35.0	4.3	29.8	0.9
	1965	37.9	—	28.3	9.6	—	37.9	4.3	31.7	1.9
	1966	39.8	—	32.1	8.2	—	39.8	5.2	32.6	2.0
	1967	42.2	—	34.0	7.7	0.5	42.2	6.2	33.6	2.4

Source: F. Alleyne: *Commonwealth Caribbean Financial Statistics. Op. Cit.*

locally to create domestic economic activity rather than leaked abroad (especially since government interest rate payments to domestic holders are a mere "transfer" payment.)

Finally, because of the large number of depositors (when active), the government savings bank can benefit from economies of scale in the regulation of its asset portfolio and have a more illiquid portfolio than one would expect from an institution which borrows short and lends long. "On the borrowing side, the intermediary with a large number of depositors can normally rely on a predictable schedule of claims for repayment and so get along with a portfolio that is relatively illiquid." [9] Cash and liquid assets as a percentage of total assets can be even less if there is a steady stream of maturing securities. In the extreme case, the government savings bank can hold as illiquid a portfolio as it likes, since the government (who benefits from this illiquidity) guarantees deposits or acts as the effective "lender of last resort".

9 J. Gurley and E. Shaw: *Op. Cit.*, p. 194.

TABLE 4. AI Geographical Distribution of Deposits and Withdrawals, Government Savings Bank, Trinidad 1968

Post Offices (Branches)	Total Deposits	Total Withdrawals	Post Offices (Branches)	Total Deposits	Total Withdrawals
Arima	801	246	Arouca	864	295
Belmont	411	85	Blanchisseuse	51	16
California	541	156	Carapichaima	539	183
Caroni	519	128	Cedros	370	207
Chaguanas	1, 262	286	Claxton Bay	192	58
Couva	298	121	Cumuto	88	22
Cunupia	536	131	Curepe	1, 462	377
Diego Martin	956	62	Erin	301	100
Forest Reserve	52	37	Fyzabad	168	61
Gonzales	356	71	Gran Couva	9	15
Guaico	164	64	Guapo	337	91
Guayaguayare	323	153	La Brea	239	164
Laventille	723	69	Manzanilla	80	59
Marabella	561	141	Matelot	366	146
Mayaro	440	225	Moruga	344	148
Morvant	1, 432	111	New Town	229	40
Oropouche	85	25	Palo Seco	314	132
Penal	362	162	Point Fortin	194	110

Continued

TABLE 4.AI *Continued*

Post Offices (Branches)	Total Deposits	Total Withdrawals	Post Offices (Branches)	Total Deposits	Total Withdrawals
Princes Town	280	142	Rio Claro	293	128
Sangre Grande	562	345	San Juan	1, 565	229
Santa Flora	417	135	Siparia	537	147
St. James	527	57	Tabaquite	392	203
Tableland	199	94	Tacarigua	796	361
Toco	433	187	Tunapuna	1, 098	194
U.W.I.	108	8	Williamsville	172	72
Woodbrook	166	8	George Street	167	10
Park Street	263	20	St. Vincent Street	489	7
Charlotteville	287	72	Moriah	321	52
Roxborough	627	184	Speyside	139	105
Scarborough	1, 417	1, 892	San Fernando	3, 654	4, 073
			Sub-Total	30, 878	13, 222
			General Post Office	4, 953	14, 362
			Total	35, 831	27, 584

No. of Action Accounts in the Savings Bank as at 31st Dec., 1968 = 43, 140 or 31. 8%

No. of Dormant Accounts in the Savings Bank as at 31st Dec., 1968 = 92, 723 or 68. 2%

Total: 135, 863

[illegible] Post Office Savings Bank, Trinidad.

TABLE 4. AII Deposits, Withdrawals and Investments, Government Savings Bank, Jamaica, 1871-1960 £000 (J.)

Year	No. of Branches	Amount of Deposits During year	Amount of Withdrawals During Year	Net Deposits (Deposits minus Withdrawals)	Amount at Credit of the Depositors	British & Colonial Stock	Local Govt. Securities
1871	n.a.	100	54	46	n.a.	n.a.	n.a.
1900	n.a.	210	238	–28	n.a.	n.a.	n.a.
1918	n.a.	165	154	11	n.a.	n.a.	n.a.
1925	n.a.	337	350	–13	544	414	89
1935	n.a.	477	533	–56	795	n.a.	n.a.
1940	n.a.	569	595	–26	855	747	116
1945	168	2253	1762	491	2378	1697	476
1946	173	4275	3684	591	3011	2461	496
1947	179	3024	3120	–96	2914	2420	495
1948	178	1772	1869	–97	2320	2158	480
1949	178	1740	1785	–45	2275	1742	477
1950	182	1698	1696	1	2276	1622	471
1951	179	1795	1702	92	2368	1672	480
1952	181	2214	1872	342	2710	1775	595
1953	182	2185	2003	181	2891	1917	583
1954	188	2385	2170	215	3107	2151	635
1955	188	2482	2349	132	3296	2248	745
1956	192	2821	2557	264	3621	2040	860
1957	200	3233	2993	241	3928	2138	1085
1958	211	3741	3242	499	4515	2039	1668
1959	220	4205	3939	273	4896	2039	1708
1960	232	4948	4970	–22	5140	—	—

Source: C. V. Callender: *The Development of the Capital Market Institutions of Jamaica. Op. Cit.*

TABLE 4. AIII Characteristics of Sample of Small, Medium and Large Accounts at Government Savings Bank Guyana, 1969 $ (E.C.)

	$100-$499			$500-$9, 999			$9, 999-$15, 000		
OCCUPATION OF DEPOSITORS	No. of Depo-sitors	Urban	Rural	No. of Depo-sitors	Urban	Rural	No. of Depo-sitors	Urban	Rural
Labourer	3	—	3	—	—	—	—	—	—
Farmer	5	—	5	5	—	5	5	—	5
Housewife	4	—	4	1	1	—	1	1	—
Clerk	1	1	—	—	—	—	—	—	—
Watchman	1	1	1	—	—	—	—	—	—
Domestic Servant	1	—	1	—	—	—	—	—	—
Postman	1	—	1	—	—	—	—	—	—
Overseer	1	—	1	—	—	—	—	—	—
Machine Operator	1	1*	—	—	—	—	—	—	—
Prison Warder	1	—	1	—	—	—	—	—	—
Merchant	1	1*	—	1	1*	—	1	1*	—
Teacher	—	—	—	1	—	1	1	—	1
Winchman	—	—	—	1	1	—	1	1	—
Mechanic	—	—	—	2	—	2	2	—	2
Proprietor	—	—	—	—	—	2	2	—	2
Diamond Seeker	—	—	—	1	—	1	1	—	1
Goldsmith	—	—	—	1	—	1	1	—	1
Tailor	—	—	—	1	—	1*	1	—	1*
Cartman	—	—	—	1	—	1	1	—	1
Shopkeeper	—	—	—	1	—	1	1	—	1
Businessman	—	—	—	1	1*	—	1	1*	—
Chauffeur	—	—	—	1	—	1	1	—	1
Total	21	4	17	20	4	16	20	4	16

* Indicates that the account is dormant

Source: Special Request, Post Office Savings Bank, Guyana.

CHAPTER V

The Significance of the Credit Role of Non-Bank Financial Intermediaries in the Caribbean

INTRODUCTION

In the past, the main interest in the workings of financial intermediaries concerned their ability to maximize the volume of saving that could be coaxed out of "surplus units", their ability to perform this function at minimum cost and the extent to which their efficiency in attracting savings was a reflection of inter-institutional (financial) competition. Thus statistical and analytical emphasis was on the liabilities and income and expenditure structures of these financial intermediaries. Today, however, there is major concern about ture of these financial intermediaries. Planners and economists seek to know the distribution of credit between consumption and investment purposes and whether the pattern of credit is predominantly short, medium or long term.

It is believed that commercial banks provide mainly short-term credit to consumers and producers because of the "demand" or short-term nature of their deposits (although the system of renewal of advances does make some bank advances in effect medium term). It is therefore interesting to know the extent to which N.F.I. fill this gap in medium and long term credit for consumers and producers.

In trying to assess the credit role of N.F.I. in the Caribbean, certain difficulties are encountered. One clear difficulty is threefold: the lack of statistics on some institutions, the lack of data on some firms of a particular type of institution and the lack of a detailed asset breakdown by those firms who do submit returns. Very little information is available, for example, on the volume of private pension funds and on the use of these funds; also many insurance companies, for example, do not submit returns. And, generally, the information on the asset structure of financial intermediaries is not sufficiently detailed, partly because the government statistical departments, in the past, did not give enough importance to this aspect of the operations of N.F.I. These three problems, as we have said earlier, stem from the previous preoccupation of the monetary authorities with banks at the expense of non-banks.

A second major difficulty in trying to assess the significance of the credit role of N.F.I. is the problem of trying to isolate and identify the direct and indirect effects on real sectors and sub-sectors. The major reason for the problem is the lack of adequate national accounting figures; for example, construction activity is not adequately broken down into the major sub-sectors (residential, commercial and industrial), nor is the regional location (urban and rural) given for the building sub-sectors. There is also the correlation problem and the

problem of identifying the various indirect effects throughout the system from the increase in a certain activity e.g. building.

A third major difficulty in trying to assess the significance of the credit role of N.F.I. is that some intermediaries are not deficit/surplus units in the strict meaning of the term (i.e. they are more or less secondary financial institutions). For example, money lenders (information on whom is hardly available) borrow a significant proportion of their funds from commercial banks (as do Finance Companies to a lesser extent) and lend these funds in turn to those people who might not have satisfied the banks' criterion of credit worthiness. Also, "the omission of trustee organisations, again with occasional exceptions, is justified by the fact that they differ basically from all other financial institutions in that they are not the owners of the assets they administer and do not incur liabilities of their own, but hold and administer with more or less freedom of investment decision, financial and tangible assets of the beneficiary owners, who usually, are private individuals. The operations of trustees therefore do not constitute financial intermediation in the strict sense and no debt or substitution at all is involved."[1] Many quasi-government financial institutions are also of this latter category; industrial and agricultural credit corporations (sometimes called boards or societies) acquire most of their funds from the government who can hardly be described as a surplus unit. These quasi-government institutions are however very important members of the credit system in that they supply risky long term credit to old and new industries; their provision of risk capital to new industries, in particular, fills an important gap in the credit structure which neither commercial banks or others are prepared to fill.

Because of the difficulties and problems cited above, we shall analyse briefly only the mortgage and securities markets. We shall not analyse in detail the market for consumer credit for a number of additional reasons. One reason is that a study of the consumer credit market can best be done in the context of a general analysis of the credit role of commercial banks.[2] A second reason is that a large part of the loans actually given is not classified e.g. insurance companies in the Caribbean do not usually record the purpose of "policy loans". A third reason is that the loans given by credit unions and cooperative societies (and to a lesser extent, finance houses) are not really loans given by financial intermediaries in the strict sense. Credit unions, for instance, are exclusive associations of people who pool their savings to make loans to their own members.

A Credit Union is therefore a sort of "closed circuit" type consumer credit system (a union sometimes consists solely of members of a factory or office or "lodge") in which all savers are also borrowers and for any one saver consumption is a short time period removed. Detailed analysis of credit unions is therefore not undertaken in this

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1 R. Goldsmith: *Op. Cit.*, p. 20.

2 See N. Miller: *Organisation and Structure of Commercial Banking in the Commonwealth Caribbean*, (Forthcoming).

TABLE 5.1 Savings in Credit Unions, Trinidad and Jamaica $000 (E.C.)

Year	Share Capital (Trinidad)	Share Capital (Jamaica)
1961	n.a.	5, 438
1962	4, 221	6, 874
1963	5, 370	8, 275
1964	7, 116	10, 051
1965	9, 169	11, 126
1966	11, 431	13, 229
1967	13, 769	15, 010

Source: (1) Annual Statistical Digest, Trinidad

(2) Monetary Statistics, Jamaica.

study, although Table 5.1 shows that they are not an insignificant institution.[3]

We shall also not attempt an analysis of the equity market. The main reason for taking this decision is that there is little published information on business finance other than the mere quotation of share prices. We need to know what types of external financing (loans, shares, etc.) are employed by non-financial companies and their relative volumes. We also need to know the volume of internal financing from undistributed profits, depreciation allowances etc. Then we would be able to assess the importance of shares in external and total business financing, and only after this is done will we be able to determine the exact ratio of N.F.I. holdings of shares to total share financing in particular, and business finance in general. Later on in the study, a brief attempt will be made to assess the importance of N.F.I. in the equity market in the Caribbean, based on limited data, and certain suggestions will be made for making the provision of long-term credit by N.F.I. to non financial firms more effective.

I

THE MORTGAGE MARKET

Mortgages are not standardized but vary tremendously with respect to property location, type, age, size and quality. The mortgage market,

[3] A similar comment can be made about an unorganized money market phenomenon, called "Box-hand" in Guyana, "Sou-sou" in Trinidad, and "Pardner" in Jamaica. For an analysis, see C. Geertz: "The Rotating Credit Association: A "Middle Rung" in Development", in *Economic Development and Cultural Change."* Vol. X, No. 3, April, 1962.

therefore, differs fundamentally from the securities market, in that mortgages are issued in small amounts and the turnover in outstanding first mortgages is relatively low, compared with the secondary market for securities. Moreover, mortgage market flexibility is limited by legal, transactions and administrative costs, differences in the terms of lending by various N.F.I., and rigidities or lags in interest rate movements.

DEMAND FOR MORTGAGES

The demand for mortgages is a sort of derived demand. The market is quite sectorized in that the determinants of demand might vary between residential, commercial, industrial and agricultural property. There might also be some significant variation between short term demand and long term demand. Huang[4] has stated that the demand for residential mortgages is determined by the imputed yield, disposable personal income, the rent-to-cost-of-houses ratio, the ratio of mortgage debt outstanding to total financial assets and the change in the average maturity of home mortgages. This is not an exhaustive list of short-term determinants. For example, it can be said that the size of the loan-to-value ratio affects the demand for mortgages to some extent. In analysing the American situation, Gelfand found that of the three credit terms—mortgage maturity period, interest rate and down payment requirement—the liberalization of the down payment is most capable of expanding housing demand: "Eliminating the down payment so that no down payment is required would improve potential housing demand to 48. 2 percent, a betterment factor of more than one-third."[5]

There are other factors (long term) which can affect the demand for mortgages over time. One factor accounting for the increase in demand over time is the greater certainty of expectation of employment and income in the future. This is an important factor, since a mortgage in effect brings forward (or "mortgages") future income. A second reason for the increase in mortgage demand over time is the psychological factor: "Debt increases on the demand side by long run modifications in social attitude toward mortgage indebtedness. . ."[6] It is said that people are much more willing today to incur debt for the financing of very large expenditures than they were in pre-war days. This second reason, of course, is somewhat connected to the first, re greater certainty of future income. A third reason is that houses are high cost durable goods, which depreciate very slowly with respect to time and almost as slowly with respect to obsolescence. It is therefore possible to postpone repairs and alterations or the

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4 D. S. Huang: "The short-run flows of non-farm residential mortgage credit," *Econometrica*, April, 1966.

5 J. E. Gelfand: "The Credit Elasticity of Lower-Middle Income Housing Demand," *Land Economics*, Nov., 1966, p. 472.

6 M. Megee: "Statistical Prediction of Mortgage Risk," *Land Economics*, Nov., 1968, p. 462.

purchase of a new house, for some time, and for this reason mortgage demand could rise suddenly when demand conditions are favourable (or fall suddenly when demand conditions are less favourable.)[7] In fact, the rate of depreciation has risen in post-war years, because of a change in people's housing tastes and a general desire for a better standard of housing. "In effect, the difficulty lies in a failure to conceive the possibility of a process in the housing market that has been a major factor in other durable goods markets, particularly in automobiles. This is the acceptance within the market of an increased rate of depreciation."[8] A fourth reason for the increase in mortgage demand is the population factor. The rate of increase in population is higher than in pre-war days because a fall in the mortality rate and a fall in the age at marriage have been enough to offset the tendency for the average size of family to fall. The number of households (and therefore of mortgages) has also increased because of a change in the family structure; unmarried adults are more independent minded and prone to "set up house" on their own (partly because of rising incomes.) Fifthly, the universal problem of the migration of rural folk to towns must also be a factor contributing to the increased demand for mortgages, since urban housing standards tend to be higher than rural standards.

The determinants of the demand for mortgage loans by commercial, industrial and agricultural concerns are likely to be different from those for residential mortgages. For instance, whereas the rate of interest has a significant effect on the demand for residential mortgages (partly because of the ease of calculating the non-transferable interest burden, which is large in absolute terms), it has only a minor effect on businessmen and might merely affect the timing of their demand.[9] Whereas a residential building is a consumer durable good, an industrial building is a producer asset or investment. The businessman considers that his building enters the production process in the same way as does his plant or machinery; the demand for an industrial mortgage is therefore a joint demand and is mainly determined by the overall rate of return. Other factors such as the depreciation rate on buildings that is granted as a tax allowance, may play a contributory role in affecting industrial demand for mortgages.

THE SUPPLY OF MORTGAGES

Mortgage loans are supplied by N.F.I., other intermediaries, and by individuals. In some countries mortgages supplied by individuals are

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7 This is one of the reasons for the belief that in developed countries there is a long period construction cycle. However, for a view that "the long cycles in big cities were the results of shocks and major uncertainties not from within but from outside the building industry, predominantly from major set-backs in manufacturing," see M. Melnyk: "The Problem of Long Cycles in Residential Construction," *Land Economics*, Nov., 1968, p. 491.

8 A. H. Schaaf: "Some Theory and Policy Implications of the Postwar Housing Boom," *Land Economics*, May, 1966, p. 183.

9 The effect may vary between firms (e.g. big and small) because of differences in ability to raise funds by alternative means.

very significant; for example, in the U.S.A., individuals are said to be the second biggest mortgage lenders.[10] Suppliers have a great deal of control over the market because demand at most times exceeds supply; therefore, increases in the rate of interest, or an equivalent worsening in the "quality" or terms of supply, may be mainly due to the demand pull factor rather than cost-push conditions. There is however some degree of stickiness in interest rates in this nominally sellers' market, partly owing to fears of public protest if there is an increase in interest rates; suppliers are therefore more prone to alter the "quality" or other conditions of supply.

Some of the factors that Huang[11] found to be influencing the institutional supply of mortgages are: (1) the mortgage yield (2) the yield on long term assets (3) the reserve position of financial institutions and (4) the net increases in savings in financial institutions.

The relative importance of each of the above determinants may vary between N.F.I. For example, building societies are likely to supply as mortgage loans the same percentage of their asset portfolio even when market conditions are not attractive. However, insurance companies are more prone to switch from mortgages to securities when conditions are not very attractive. But, to a certain extent, both institutions are constrained in their ability to switch because of forward commitments to their customers.

An alternative to changing the quantity of mortgages is varying the quality of the mortgage. For example, when there is an increase in demand, N.F.I. can either raise the rate of interest, reduce the loan to value ratio or increase the time of waiting.

Non-residential mortgages (commercial, industrial and agricultural) are more risky than residential mortgages because the value of the property is closely bound up with the progress and prospects of the particular industry, whereas the value of the residential property is less subject to particular influences and more subject to general factors, which change very slowly. Whereas the decline of an industry can be very sudden, the decline of an urban area, even if it were dependent on a particular industry, is much slower because of the relative immobility of labour and the labourers' dependents.

Generally, N.F.I. find the mortgage a convenient asset to hold, because although it is relatively safe, it is at the same time relatively high yielding. Any riskiness that a non-bank may perceive in a mortgage is not usually a capital risk as such but the risk of waiting (i.e. liquidity). As we said earlier, the secondary market in mortgages is not a very active one and so if there is a run on a non-bank, the latter has to rely solely on its reserves, the liquidity of its securities, (including the flow of maturing securities,) mortgage repayments and

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10 See R. P. Kent: *Money and Banking,* Holt, Rinehart and Winston, 1961, pp. 745-768.

11 D. S. Huang: *Op. Cit.*

TABLE 5.2 Main Sources of Finance for New Real Estate Loans, Guyana $(E.C.)

	Credit Corporation Rural & Urban Including Public Officers' Housing		New Building Society		Sugar Industry Labour Welfare Fund Committee		Insurance* Companies		Total	
	LOANS		LOANS		LOANS		LOANS		LOANS	
Year	No.	Amount	No.	Amount	No.	Amount	No.	Amount	No.	Amount
1961	338	1,122,834	—	1,418,155	2,008	768,915	—	2,414,255	2,346	5,724,159
1962	123	639,536	—	85,354	2,746	858,188	—	1,316,468	2,869	2,900,046
1963	91	386,279	—	—	1,691	565,048	—	814,788	1,782	1,766,115
1964	151	538,496	—	87,162	1,238	412,844	—	1,739,827	1,389	2,823,329
1965	188	453,418	—	928,333	1,427	549,634	—	2,376,979	1,615	4,398,364
1966	564	1,820,929	—	1,635,273	1,137	423,362	—	3,319,637	1,701	7,199,211
1967	198	1,027,657	—	1,631,512	1,018	370,624	—	3,998,045	1,216	7,027,838
1968	224	786,974	—	1,295,082	1,482	1,298,680	—	3,868,543	1,706	7,249,279

* The 7 local companies operating in Guyana (before 1966, reference was to 4 companies).

Source: Quarterly Review of Financial Statistics, Guyana.

the good graces of the lender of last resort (whether Central Bank or commercial banks).[12]

Although life insurance companies, in particular, find that mortgages, which are long-term assets, fit very nicely into their "matching" portfolio policy (since their liabilities are mainly long-term) even they would want to hold regularly more mortgages in their portfolio, if they knew that at times of need some of these mortgage assets could be unloaded on a smooth working secondary mortgage market. The formation of an effective secondary mortgage market might also lower the cost of lending by reducing risks and administrative costs and by increasing the mobility of mortgage capital between scarce and surplus areas.

N.F.I. SHARE IN CARIBBEAN MORTGAGE MARKETS

N.F.I. tend to dominate the "open"[13] mortgage market. Table 5.2 shows the volume and value of loans granted in Guyana by selected N.F.I. We have included the Sugar Industry Welfare Funds because these can, to some extent, be considered as pension funds. We have also included the mortgage loans made by the Guyana Credit Corporation, a quasi-government institution. Non-Banks supply more than half of the total mortgages granted in Guyana, although their dominance seems to have declined suddenly in 1968, as seen in Table 5.3 below:

TABLE 5.3 N.F.I. Mortgages as a Percentage of All Mortgages, Guyana $ (E.C.)

	Mortgages Cancelled (All Sources)		New Mortgages (All sources)		New N.F.I. Mortgages	New N.F.I. Mortgages as a % of all New Mortgages
Year	No.	Value	No.	Value	Value	
1964	1029	4,510,077	988	4,440,264	2,823,329	63.6
1965	1188	4,935,783	1199	6,522,101	4,398,364	67.4
1966	1355	5,780,513	1694	10,060,240	7,199,211	71.6
1967	1314	6,185,978	1291	11,222,625	7,029,838	62.6
1968	1397	7,251,949	1681	17,003,761	7,249,279	42.6

Source: Quarterly Review of Financial Statistics, Guyana

The situation in Trinidad is in many respects similar to the one in Guyana. Table 5.4 shows that insurance companies are the main non-bank financier of mortgages (55 percent in 1955 and 80 percent in

12 Building Societies also resort to increasing the rate of interest on deposits held (and delaying withdrawals for a long time) or restricting the size of withdrawals.

13 "Open" here refers to institutional loans and does not include inter-personal loans.

TABLE 5.4 Value of Mortgage Loans by Selected Non-Bank Financial Intermediaries,* Trinidad $(E.C.)

Year	Life Insurance Companies	Non-Life Insurance Companies	Total Life and Non-Life Companies	Building Societies	Agricultural Credit Bank	Total
1955	5,853,000	2,900,000	8,753,000	5,856,000	1,622,900	16,231,900
1956	7,757,000	3,900,000	11,657,000	5,859,000	1,541,299	19,057,299
1957	10,576,000	5,000,000	15,576,000	5,567,000	1,459,983	22,602,983
1958	13,191,000	6,500,000	19,691,000	5,735,000	1,429,954	26,855,954
1959	15,203,000	7,500,000	22,703,000	6,262,000	1,349,759	30,314,759
1960	18,845,000	9,000,000	27,845,000	6,565,000	1,426,142	35,927,142
1961	21,504,000	10,500,000	32,000,000	6,730,000	1,433,218	40,167,218
1962	23,866,000	12,000,000	35,866,000	7,220,000	1,746,614	44,832,614
1963	26,579,000	13,000,000	39,579,000	7,741,000	1,949,772	49,269,772
1964	27,236,000	13,500,000	40,736,000	8,039,000	2,427,882	51,202,882
1965	30,377,000	15,000,000	45,377,000	8,135,000	3,100,139	56,612,139
1966	32,091,000	16,000,000	48,091,000	9,173,000	3,875,672	61,139,672

* Rounded figures

Source: Annual Statistical Digest, Trinidad.

1966) and that of the insurance companies, life companies are the main providers of mortgage finance. Life insurance companies are able to carry a greater volume of mortgages because their business is bigger and because their liabilities structure is more long-term. Throughout the 1955-1966 period, the ratio of life insurance holdings of mortgages to non-life holdings has shown a remarkable constancy of 2 : 1. An indication of the importance of N.F.I. provision of mortgage credit can be gauged by comparing the increase in registered real property instruments shown in Table 5.AI. (Commercial bank advances to the construction sector were $6.7m., $8.7m. and $9.8m. in 1966, 1967 and 1968, respectively, but these were mainly for working capital, rather than mortgages).

Generally, we can say that in Guyana and Trinidad (and also we suppose in Jamaica, were adequate figures available), non-banks are the most important institutions providing mortgage credit. This is not surprising since commercial banks would want to hold only a small volume of mortgages given their very short-term liabilities portfolio. We can also say that insurance companies dominate the market and that life insurance companies have a paramount place. This dominance by insurance companies however does not indicate that insurance companies are the most mortgage conscious N.F.I. since building societies hold a higher percentage of such assets in their portfolio. But the lower percentage held by insurance companies is equivalent to a much higher absolute level of holdings. The dominance by insurance companies does not indicate that there exists a quasi-monopoly market structure since there are many insurance firms (with no one firm dominating the industry). In developed countries, building societies (and not insurance companies) tend to dominate the mortgage market, partly because they rival insurance companies in size of asset portfolio and partly because they devote a larger percentage of their portfolio to the holding of mortgage assets. Table 5.AII shows that such a situation exists in Britain.

Most of the mortgage loans in the Caribbean are for residential building. Table 5.5, for Guyana, shows that industrial and commercial mortgages are a very small holding indeed for domestic life insurance companies. However, despite the small amount , in absolute terms, of

TABLE 5.5 Residential and Non-Residential Mortgages, Domestic Life Insurance Companies, Guyana $M (E.C.)

	1966	1967	1968
Residential Mortgages	19.9	21.9	23.3
Industrial & Commercial Mortgages	0.2	0.2	0.2
Agricultural Mortgages (negligible)	—	—	—
Total	20.1	22.1	23.4

Source: Special Request to the Bank of Guyana.

industrial and commercial mortgages held by domestic life insurance companies, if more detailed information were available, the statistics might still show that all insurance companies in particular, and N.F.I. in general, have a fair amount of influence on this segment of the mortgage market. This is because of the small absolute size of industrial and commercial mortgages from all sources.

The situation is not very much different in Trinidad. There, business mortgages held by life insurance companies are also a very small percentage of total mortgages held, as can be seen from Table 5. 6, below:

TABLE 5. 6 Mortgage Investments in the Country, Life Insurance Companies, Trinidad $ (E.C.)

Year	Total Mortgages	Residential Mortgages	Residential as a % of Total	Business Mortgages	Business as a % of Total
1965	29, 699, 051	29, 084, 056(10)	97. 9	614, 995(4)	2. 1
1966	31, 186, 125	30, 334, 669(10)	97. 4	851, 456(4)	2. 7
1967	36, 037, 157	35, 625, 148(11)	98. 9	412, 009(4)	1. 1

( ) denotes number of companies reporting.

Source: Special Request to the Statistical Department, Trinidad.

Business loans by insurance companies and other N.F.I. are small, but there are quasi-government institutions which attempt to fill this gap, even if not very adequately, for example, the Guyana Credit Corporation in Guyana, The Agricultural Credit Bank in Trinidad and the Agricultural Credit Board in Jamaica. As we said earlier, it is not surprising that N.F.I. holdings of non-residential mortgages are appreciably smaller than their holdings of residential mortgages, since there are special risks attached to the former. This is particularly the case with agricultural mortgages and as indicated in Table 5. 5, the holdings of agricultural mortgages by domestic life insurance companies in, for example, Guyana, are negligible.

Farmers tend to need credit which is of an intermediate or long term nature, but because of the special risks in farming, creditors are only willing to give farmers short-term, high collateral, high interest credit. Credit for erecting buildings, clearing, drainage, machinery, buying and rearing of livestock involves a relatively long gestation period compared with manufacturing activity. Additional reasons for the reluctance to lend to farmers are:-

(1) Farm accounting methods are poor and so creditors are very wary.

(2) Farms are small and many and this increases creditors' problems of administering these loans.

(3) Total credit to a farmer may be disproportionately large relative to the farmer's equity.

(4) Excessive rainfall, drought or hurricane, may badly upset forecasts.[14]

In this sort of context, it is not surprising that N.F.I. are not very willing to make mortgage loans for agricultural purposes. In the Caribbean, the difficulties of export marketing (of non-plantation crops) are super-imposed on the above problems and may have increased the reluctance of N.F.I. to grant mortgage loans to these sub-sectors. Table 5.7, for Trinidad, shows that an overwhelming proportion of the value of loans made by the Agricultural Credit Bank, a quasi-government institution, is for mortgage purposes and indicates that (by giving these long term loans to agriculture) an important gap in the credit structure is in the process of being filled. Table 5.8, for Jamaica, shows that this proportion is considerably less than in Trinidad, even when we make the generous assumption that all long term loans referred to are for mortgage purposes. Generally, we would expect long term credit, including mortgages, granted by financial institutions in general, and N.F.I. in particular, to increase significantly in the future because financial institutions are becoming better equipped than money lenders (a) to standardize loan techniques and terms and extend loan maturity and (b) to take advantage of improvements in credit analysis and surveillance of borrowers. The per unit cost to financial institutions, therefore, when making a large number of loans, will be lower than the per unit cost to money lenders.

Again, it is difficult to make a definitive judgement about the adequacy of the respective mortgage sub-markets and the role of N.F.I. in particular, because, although we know something about certain aspects of business external financing, we do not know the demand (at a price) for building and the extent to which building needs are satisfied by internal and retained funds or "other" funds (e.g. shares). Also, in the case of Jamaica, we only have adequate information on mortgage holdings for one or two of the N.F.I. and so cannot say to what extent the mortgages shown in Table 5.AIII were financed by N.F.I.

THE GOVERNMENT SECURITIES MARKET

From the point of view of N.F.I. in the Caribbean, there can be said to be three broad markets for securities: (1) the market for domestic securities (2) the market for regional (Caribbean) securities and (3) the market for foreign securities. Each of these three broad markets can be sub-divided into (a) central government securities (b) local government securities and, in some countries, (c) public corporation (utility) securities, although the latter two markets are not usually as active, in a market sense,[15] as the market for central government securities.

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14 For an analysis of these problems, see R. P. Kent: *Op. Cit.*, pp. 724-744.

15 For an analysis of primary and secondary marketing problems relating to local government securities, see R. P. Robinson: *Postwar Market for State and Local Government Securities*, Princeton University Press, 1960.

TABLE 5.7 Mortgage Loans and Other Advances of the Agricultural Credit Bank, Trinidad $(E.C.)

	LOANS ON MORTGAGES (AGRICULTURAL PROPERTIES)				CROP ADVANCES (SHORT-TERM LOANS)*			
Year	No. of Borrowers	Amount Advanced During Year	Amount Repaid During Year	Outstanding Indebtedness at end of Year	No. of Borrowers	Amount Advanced During Year	Amount Repaid During Year	Outstanding Indebtedness at end of Year
1957	66	390, 379	471, 695	1, 459, 983	32	469, 796	357, 445	259, 672
1958	57	337, 100	367, 129	1, 429, 954	44	379, 758	457, 045	182, 385
1959	74	359, 604	439, 799	1, 349, 759	43	450, 113	369, 810	262, 689
1960	n.a.	504, 346	427, 963	1, 426, 142	n.a.	457, 757	465, 105	255, 344
1961	87	328, 938	321, 862	1, 433, 218	46	349, 780	380, 131	224, 989
1962	137	714, 013	400, 616	1, 746, 614	34	207, 953	308, 174	124, 769
1963	136	629, 788	426, 630	1, 949, 772	24	106, 300	207, 693	103, 376
1964	n.a.	851, 913	373, 803	2, 427, 882	n.a.	194, 117	183, 421	114, 072
1965	n.a.	1, 225, 917	553, 660	3, 100, 139	n.a.	267, 047	197, 630	183, 490
1966	n.a.	1, 364, 093	588, 560	3, 875, 672	n.a.	229, 526	218, 599	194, 417

* Loans to be repaid within a period of one to three years.

Source: Annual Statistical Digest, Trinidad.

TABLE 5. 8 Short, Medium and Long Term Loans by Agricultural Credit Board, Jamaica £ (J.)

	FULL YEAR					1966				1967			
	1961	1962	1963	1964	1965	March	June	Sept.	Dec.	March	June	Sept.	Dec.
Direct Borrowers													
Short Term	14, 990	26, 846	12, 663	300	N.A.	3, 000	1, 000	—	687	1, 004	3, 225	4, 968	2, 372
Medium Term	61, 734	17, 105	15, 837	695	N.A.	3, 500	4, 900	—	6, 900	1, 500	151	5, 401	14, 342
Long Term	61, 229	9, 700	1, 534	—	N.A.	1, 925	—	4, 000	6, 968	—	1, 500	5, 000	3, 400
Total	137, 953	53, 651	30, 034	995	N.A.	8, 425	5, 900	4, 000	14, 555	2, 504	4, 876	15, 369	20, 114
A.C. Banks and Approved Organizations													
Short Term	383, 798	329, 600	336, 658	9, 600	N.A.	175, 265	177, 798	139, 445	134, 870	139, 280	147, 300	141, 270	104, 430
Medium Term	619, 969	471, 654	224, 120	8, 330	N.A.	43, 215	42, 400	41, 720	36, 415	54, 340	95, 660	97, 660	95, 545
Long Term	152, 475	19, 850	10, 325	1, 450	N.A.	6, 500	5, 320	2, 640	6, 900	3, 350	6, 977	6, 178	4, 074
Total	1, 294, 195	874, 755	601, 137	20, 375	N.A.	233, 405	231, 418	187, 805	192, 740	199, 474	249, 542	245, 108	204, 049

Note: (a) Short-term Loans are for up to 2 years
(b) Medium term Loans are for over 2 years to 7 years
(c) Long term Loans are for over 7 years.

Source: Monetary Statistics, Jamaica.

There are some interrelations between the markets. The conditions in the foreign securities market (and to a lesser extent, the Caribbean securities market) affect the domestic securities market, since, if price and maturity terms are more favourable in the former less domestic securities may be bought, and this would force an adjustment in domestic securities prices. However, the converse does not obtain, since even if domestic securities are more attractive than foreign securities, the prices of foreign securities will not change because (a) a fall in the demand by a Caribbean territory for foreign securities would constitute too small a percentage reduction of total demand for foreign securities (assuming the foreign country to be a large metropolitan country like Britain) and (b) many former holders of metropolitan securities cannot suddenly switch completely to buying the domestic securities of a Caribbean country because there may not be an adequate supply, in terms of the required volume and maturity stream.[16] The interest rates of central government, local government and public corporation securities should bear some interrelationship with respect to liquidity and marketability. Similarly, the segments (short, medium and long) of a market should bear some relationship to one another, within limits, as represented by a yield curve.

DEMAND FOR SECURITIES

For some institutions, for example government savings banks, the holding of a minimum percentage of their asset portfolio in securities is statutory. For some others, for example commercial banks, it is both statutory and convenient, given the demand or short term nature of their liabilities portfolio. For insurance companies and building societies, securities are held partly as a residual asset, and partly because a reasonable rate of return is associated with a risklessness which helps to offset the riskiness of other assets in their portfolio. For insurance companies, securities are partly considered a residual rather than a first choice asset for a number of reasons. Firstly, the companies try to accommodate their policy holders who desire loans. Secondly, the companies attempt to acquire assets which have the highest rate of return; in this regard, mortgages are usually a more attractive asset than government securities. Thirdly, insurance companies prefer to hold mortgages rather than securities in the hope that those mortgagers who are not policy holders, will in time be induced to become policy holders: "It could be claimed that there could have been greater investment in Government securities but it should be noted that insurance companies deal with people and create much goodwill and influence business by the grant of loans on mort-

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[16] Moreover, to attract private foreign buyers, the differential between domestic and foreign securities interest rates may need to be so high (because of domestic secondary market and capital risk problems) as to be an unattractive proposition for any Caribbean government.

gage."[17] However, insurance companies partly want to hold securities as assets in their own right, in order to attain "balance" or the desired levels of liquidity and risklessness of an optimum portfolio.

Also, life insurance companies find that fixed interest long term securities very nicely match some of their fixed long term liabilities. Again, insurance companies may also want to hold a certain amount of domestic government securities, even though the rate of interest or return on alternative assets is rising, either because they fear certain political repercussions, if they were to reduce their holdings, or because they feel that they have a "moral commitment" to the government.

Building societies consider their main asset portfolio objective to be the granting of mortgages. They only hold securities because the near "demand" nature of their liabilities portfolio requires a certain level of liquidity; securities satisfy the desire for liquidity because at the end of the spectrum[18] they can be almost as liquid as cash and in addition earn a tangible rate of return.

Many non-financial firms also demand securities. This demand to hold securities is as a partial alternative to holding transactions and precautionary cash balances. Studies have shown that the desire to hold cash varies inversely with the rate of return on securities.[19]

SUPPLY OF SECURITIES

The supply of government securities is related to the actual and desired levels of public expenditure. Some factors which may explain how public expenditure can be expected to behave, according to Peacock and Wiseman are:[20]

(1) The relative productivity of the resources used in the public and private sectors.

(2) The welfare attitude of the government to the poor section of the population.

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17 H. K. George: "Economic Aspects of Insurance in Guyana." A paper presented at the Guyana Economic Society Meeting, March, 1970, by the General Manager/Secretary of the Demerara Mutual Life Assurance Society, Ltd.

18 The extent to which the most liquid (short term) securities are needed to be held depends on the marketability of these securities and the maturity structure of these securities.

19 See for example, W. J. Baumol: "The transactions demand for cash. An inventory theoretic approach," *Quarterly Journal of Economics*, Nov., 1952 and also J. Tobin: "The interest elasticity of transactions demand for Cash," *Review of Economics and Statistics*, Aug., 1956.

20 A. T. Peacock and J. Wiseman: *The Growth of Public Expenditure in the United Kingdom*, Oxford University Press, 1961.

(3) The growth and change in composition of the population and the resultant effect on education and health expenditure.

(4) The community's income elasticity of demand for services, which the government may provide more efficiently than the private sector.

(5) The growth in size and importance of conurbations and the resultant demand for amenities.

(6) The political nature of the society and current views about the role of government.

Because of the above six factors, government expenditure tends to grow faster than the national product and faster sometimes than revenue, even in tax systems whose yields have a high income elasticity or which experience frequent rises in tax rates. Governments therefore resort to borrowing. Borrowing can be from internal or external sources. Governments prefer to borrow internally because such borrowing is said to impose no real burden on the community, given the "transfer payments" or "we owe it to ourselves" principle. However, in the Caribbean a great deal of external borrowing still takes place; such borrowing can be from private or governmental sources. It has already been shown how difficult it is for a poor country to induce foreigners to hold its securities at a reasonably low rate of interest; because of this marketing problem, most of the external public debt is inter-governmental. Theoretically, there should be some interplay between the terms of loans secured from foreign governments and prices and maturities of securities offered to domestic buyers. To the casual observer, the differences in the rates of interest and terms "offered" to foreign governments and domestic buyers may indicate that the government is acting like a price discriminating monopolist and discriminating against the domestic buyers; however, the "tying of the aid" offered by foreign governments is an additional cost and so the real costs might be equal even though the monetary rates of interest were different.[21]

Any government would like to issue only long term securities to match the long gestation nature of public capital expenditure but a higher interest has to be offered to induce potential buyers to hold such securities. Here a feel for the market situation (re expected demand) in the timing of issues is important for the minimizing of the costs of debt management. Nevertheless, the domestic market for securities in almost every Caribbean country is a "buyers market" since, if potential institutional buyers do not like the terms of an offer, they can probably buy foreign securities instead. Their switch will not affect the price of foreign securities since their demand is a small part of total demand; whether the prices of domestic securi-

[21] But one factor which may tend to favour the issue of securities to foreign rather than domestic buyers is that there may be a premium on the use of scarce foreign exchange in the present (since the import component of government expenditure may be very high) and external borrowing postpones the use of existing foreign reserves.

tries will tend to fall would depend on the extent of the switch and on the rigidity of the interest rate policy of the government.

SOME COMPARATIVE MARKET FEATURES

It must again be mentioned that lack of adequate statistical data on the asset side of N.F.I. portfolios severely limits the depth and breadth of our analysis. For example, Trinidad's Annual Statistical Digest includes domestic securities held by life insurance companies under a category called "all other". The Digest also does not give *any* information on the asset portfolio of non-life companies. Our questionnaires, which, among other things, tried to elicit this sort of information, were largely ignored. On learning that some unpublished information might be available at the Statistical Department in Trinidad, we made a direct request. The results of our efforts are shown in Table 5.9 which gives some information on the asset portfolio of the insurance companies in Trinidad. The figures pertain solely to investments in the country. Because of the great fluctuation in the number of companies reporting the figures are not very useful for analytical purposes. However, it would appear that in recent years, securities holdings have become even higher than mortgages as a percentage of total assets. It is somewhat unusual for holdings of government securities to be the biggest item in the portfolio of insurance companies, especially since recently life insurance companies have been issuing many "with profits" policies. This might, therefore, be a short run or transitory phenomenon induced by recent government legislation reducing foreign asset holdings. On liquidating foreign asset holdings, domestic securities would be a useful short run repository of these funds until a decision is taken as to how the funds should be invested locally. As was said earlier, a legal and administrative time lag exists with respect to mortgage placings and the market for mortgage transactions is generally less active than the securities market. Moreover, at certain times the interest rate may have to be reduced (or length of repayment period increased) to encourage an increase in mortgage holdings, assuming the demand for mortgages is interest elastic.

In Guyana, there is no long time series on the asset holdings of insurance companies and the questionnaire method used by us bore little or no fruit. However, figures are available for recent years for domestic insurance companies. Table 5.10 shows the holdings of local long term securities by domestic insurance companies. It would appear from the figures that domestic insurance companies have some degree of monopsony over the long term segment of the local securities market. Virtually all of the remainder of long term local securities are held by foreign insurance companies, the Government Savings Bank (which used to be a major buyer of new issues before the decline of this institution) and government and private pension fund schemes.

The influence of domestic insurance companies in the long term segment of the securities market is probably greater than the percentage

TABLE 5.9

	1967		
t ıding of t year	New investments and loans made during current year	Investments realized and loans repaid during the current year	Amount outstanding at end of current year
ABSOLUTE			
Loans on Po, 229(13)	7, 082, 773(12)	4, 000, 199(10)	17, 974, 881(13)
Gov't. Secur, 317(6)	6, 136, 493(6)	6, 288, 260(6)	1, 171, 189(3)
, 033(13)	7, 062, 357(9)	220, 000(3)	16, 803, 672(5)
Municipal Se, 650(2)	—	1, 750(1)	155, 900(3)
Deposits in , 267(13)	670, 383(5)	409, 105(5)	2, 897, 207(12)
Shares in L, 965(7) , 397(1)	753, 392(2) 668(1)	5, 100(1) —	2, 064, 297(6) 83, 065(1)
Loans on M, 669(10) , 456(4)	10, 122, 156(11) —	4, 380, 064(10) 154, 721(4)	35, 625, 148(11) 412, 009(4)
Fixed Asset, 924(6)	59, 875(3)	43, 468(5)	189, 033(4)
Real Estate, 118(7)	694, 529(2)	65, 615(2)	4, 823, 029(6)
Other Invest 185(4)	5, 047, 751(4)	91, 717(2)	5, 206, 363(5)
, 210	37, 630, 383	15, 659, 994	87, 405, 792
PERCENTA			
Loans on Pc	18. 8	25. 5	20. 5
Gov't. Secur	16. 3 18. 8	40. 2 1. 4	1. 3 19. 2
Municipal S	—	—	0. 2
Deposits in	1. 8	2. 6	3. 3
Shares in L	2. 0 —	— —	2. 4 0. 1
Loans on M	26. 9 —	28. 0 1. 0	40. 8 0. 5
Fixed Asset	0. 2	0. 3	0. 2
Real Estate	1. 8	0. 4	5. 5
Other Invest	13. 4	0. 6	6. 0
	100. 0	100. 0	100. 0

( ) Denotes

Source: Spe

Between pages 140 and 141

holding in Table 5.10 indicates because the Government Savings Bank would be a fairly passive buyer in the market. Because of this, the market for local securities is not a perfect one. One reason for the dominance of insurance companies in the market for long term securities is the "matching" principle, whereby life insurance companies try to match their long term liabilities by buying long term assets; these companies may not readily switch between securities of different maturities when relative prices (rates of interest) change, thus reinforcing any tendency to rigidity in interest movements.

There are at least three inferences from the above analysis. Firstly, funding in government debt management should not be very difficult when we consider that insurance companies are growing at a rapid rate. The second implication is that the rigidity in the behaviour of insurance companies lends support to the financial theory that there exists a gap between the longest period for which the banks prefer to lend and the minimum period sought by insurance companies. "The joint stock banks are usually ready to extend up to seven years' credit, and may in certain circumstances go a year or two longer still; on the other hand the longer term investors, notably the insurance companies, will interest themselves in fifteen-year debt or longer, and may in certain circumstances be ready to go a little shorter. There is however no obvious major group of institutions catering for debt which falls between the banks on the one hand and the long term investors on the other".[22] The third implication concerns public finance theory; if we use the long term securities rate as the social time preference rate for discount purposes, there may be a downward bias (because the yield curve for securities may be fairly flat rather than rising steeply upwards.)

It is difficult to say very much on the role of insurance companies in the local securities market in Jamaica, because (a) published information shows a relatively small number of companies reporting (b) additional information secured from the Statistical Department does not give a breakdown into local and foreign securities held and (c) response to our questionnaires was poor.

TABLE 5.10 Domestic Insurance Companies' Holdings of Long Term Local Securities, Guyana $000 (E.C.)

Year	Total Amount Bought	Amount Bought by Insurance Companies	Securities Bought by Insurance Companies as a % of Total
1965	5,348.2	1,253.0	23.4
1966	1,044.2	504.2	48.3
1967	1,021.3	408.2	40.0

Source: Based on data in Bank of Guyana Annual Report, 1968.

22 Radcliffe Report: *Op. Cit.*, p. 312.

Although we do not have adequate statistical data, we probably can still say that, because of the significant holdings of local securities by commercial banks and non-financial firms, the dominance of N.F.I. in the securities market is not as great as in the mortgage market. We probably can also state that, because of the relatively large holdings by insurance companies and governments savings banks, the dominance of N.F.I. is greater in the long end of the securities liquidity spectrum than in the short end. With adequate information, we might also have been able to say in which of the three types of the domestic securities market (central government, local government and public corporations) dominance was greatest.

We would also like to have had accurate information on the size of the total public debt/GDP ratio and the internal debt/GDP ratio for each territory and to correlate these with, say, the rate of interest on securities. For example, is the relatively small size of the public sector[23] the reason for the rate of interest on Treasury Bills in Jamaica being the lowest for the three territories, as shown in Table 5.11? Or is it the fact that the recent growth rate of incomes in Jamaica has been so high that people and institutions are looking for any outlet for their surplus funds (demand exceeding supply) so that the Government can afford to have a relatively low Treasury Bill rate?[24] The answers to these questions would help us to give valid explanations for the changing patterns of N.F.I. securities holdings over time and between Caribbean territories.[25]

THE FUTURE ROLE OF N.F.I. IN THE SECURITIES MARKET

The securities market is likely to continue growing at a rapid rate because of the ever growing financial needs of the government (sellers) and the continuous search for repositories of savings out of growing

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23 In the 1956-62 period, government expenditure in Jamaica averaged 12.1% of G.N.P. (measured at current prices) whereas in Guyana the figure was over 25%.

24 These Treasury Bill Rates are themselves "high" in relation to the long term securities rates (and foreign Treasury Bill rates) and the size of the rates is only partly related to the interest offered on savings and time bank deposits.

25 The much more rapid growth of commercial bank demand and time deposits in Jamaica (which, compared to the slower growth rate in Guyana and Trinidad, may itself be a reflection of the higher G.D.P. growth rate in Jamaica) may be a direct cause of the lower Treasury Bill Rate there, since commercial banks, when faced with a rapid increase of demand and time deposits may tend to hold more short (Treasury Bills) assets in order for their asset portfolio to match the increase in the liquidity of their liabilities portfolio. (An unexpected increase in the demand for Treasury Bills could cause a fall in the Treasury Bill rate, without affecting immediately the long-term securities rate, which tends to be more stable).

incomes by individuals and institutions[26] (buyers) who desire a combination of security with a reasonable rate of return. To these qualities of security and reasonable rate of return, an efficiently operating market is likely to add a certain degree of liquidity. However, in practice, financial institutions are not able to unload securities onto the market as freely as they would like, partly because the large institutions by so doing can adversely affect price and partly because Central Banks do not always live up to their name of cheap "lenders of last resort". Moreover, the character of the market is also likely to change over time because "bonds have not proven to be good hedges against inflation. Investors must accordingly be given confidence that the capital values of personal investments are at least preserved, and, more likely, increased over a period of time, and that they will not be eroded by mismanagement and price inflation."[27] One way of restoring this confidence is by the compensatory offer of a higher rate of interest. However this device will only partially weather the storm of competition from stocks (debentures of private firms) and shares, since, in any economy enjoying steadily rising incomes, individuals and institutions would be more prone to accept a riskier, but higher yielding, portfolio. Thus, if during certain years government securities held by N.F.I. in the Caribbean are seen to rise as a percentage of total assets, [28] this only obscures an underlying and fundamental tendency towards the reduction of these holdings. Those N.F.I. in the Caribbean with long term liabilities e.g. life insurance companies, are in the best position to effect a fundamental change in their asset portfolio: "The relatively small amount invested in equities is more out of lack of investment opportunities than because of design. As readers will be aware investment opportunities in shares of public companies are very limited and few and far between. In many cases, when there is a good issue of shares, the full amount applied for is not allotted."[29]

The securities market will therefore receive tougher competition in the future. To survive, it will have to adopt new methods, some of which have already been mentioned. One radical idea, that was once suggested for the adoption by the securities market in Britain, was to equate the rate of interest with changes in G.N.P. "The peculiarity of government finance which is becoming increasingly hard to justify is the failure of the monetary authorities to consider issuing securities similar in nature to the equity share issued by ordinary commercial firms. Just as ordinary firms issue shares whose dividends vary

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26 One fillip to the process is that financial and non-financial firms are becoming more expert in economizing on transactions balances, (via better timing and synchronization of payments and receipts) and hold interest earning short term securities in the interval between receipts and payments.

27 D. Williams: "The Growth of Capital and Securities Markets" in *Finance and Development*, No. 3, April, 1962. p. 217.

28 For an analysis of movements in asset holdings, see A. D. Entine: "Government Securities Holdings of Selected Financial Intermediaries, 1954-1962," *The Journal of Finance*, Dec., 1964.

29 H. K. George: *Op. Cit.*

with the economic success and prosperity of the company, so the government might issue securities in the form of "national equities" whose dividends varied with the economic success and prosperity of the country."[30]

III

N.F.I. CREDIT AND ECONOMIC GROWTH

The financial system operates by accepting loanable funds from surplus units via the issue of indirect financial securities and transmitting these funds to deficit units via the purchasing of primary securities. "While the proportion of G.N.P. that is externally financed has not changed much over the past half-century, the proportion that is indirectly financed has risen and, of course, the proportion that is directly financed has fallen. In short, a growing share of primary issues has been sold to financial intermediaries. But the relative gainers have been the non-monetary intermediaries and the relative loser has been the monetary system."[31] While the trend for the N.F.I. to gain at the expense of the banking system might have progressed quite far in developed countries, it would appear that the share of the banking system in the underdeveloped Caribbean territories has not declined as much; however, if adequate data were available for all N.F.I. operating in the Caribbean, a more clear cut tendency for the bank share of financial intermediation to decline might have been discerned.

There are certain clearly defined reasons why the existence of financial institutions has led to an increase in the volume of credit. "For many entrepreneurs, the increased availability of funds as a result of financial intermediation may be considerably more significant than simply the reduction of costs. This is probably particularly true in underdeveloped countries, where most markets are much less perfect than in developed countries."[32] However, although financial institutions have caused an increase in the volume of credit and this increase has been quickly absorbed, (irrespective as to whether, as a consequence, the price of credit has fallen, remained steady or risen) it has never been clearly shown that this increase in credit has led to an increase in G.N.P.

The reasons why the existence of financial institutions has led to (a) an increase in the supply of credit (b) a reduction in the cost of supply of credit and (c) an improvement in the allocation of expenditure are as follows: Firstly, there is an increase in the supply of credit be-

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30 A. Day: "A New Stake in the Country?," *Westminster Bank Review,* Feb., 1964. pp. 2-3.

31 J. Gurley and E. Shaw: "Financial Intermediaries and the Saving Investment Process," *Journal of Finance,* Vol. XI, No. 2, May, 1956. p. 260.

32 H. T. Patrick: "Financial Development and Economic Growth in Underdeveloped Countries," *Economic Development and Cultural Change* Vol. 14, No. 2, Jan. 1966. p. 185.

cause without financial intermediaries saving would be held as idle money for a time, owing to a lack of knowledge of suitable investment outlets: thus, without adequate financial intermediaries, effective aggregate saving by a community in any time period is less. Secondly, claims against financial intermediaries are easier to liquidate than primary debt securities, in terms of less delay, cost, formality, etc. and this encourages saving. Thirdly, because a financial institution pools, and therefore reduces, risks, the possibility of loan default is less, so that even the poor and marginal income recipients are willing to save; and the 'lender of last resort' assurance that the government gives to financial institutions (explicit and tacit) reduces the urge to withdraw funds in a crisis. Fourthly, people tend to save more because the relatively high yield on secondary securities acts as an incentive and reward for postponing present consumption.[33]

The existence of financial institutions reduces the cost of supplying funds, because they can enjoy economies of scale with respect to administration, negotiation, accounting, appraising and collecting. Moreover, each unit's investment does not now need to be equal to its saving and this is important in view of the indivisibility of many investments whereby the funds of many savers are needed to finance one investment ("funnel effect"). But although cost of supply is lower, this does not necessarily mean that supply price is lower, the difference being considered the intermediaries' reward for providing the (increased) services. Another reason why the price of credit is not lower (and the volume of credit not greater) is that financial markets are somewhat imperfect.

The existence of financial institutions helps to bring about a better allocation of expenditure for some reasons additional to those mentioned immediately above: one additional reason is that there exists an unequal distribution of entrepreneurial opportunities and abilities among the population; the best savers are not the best investors and by offering credit to those willing to pay the highest for it, financial institutions help to bring about an "efficient" allocation of resources. A second reason is that the existence of financial institutions would tend to cause the share of large project financing to rise and the share of small project financing to fall, and this could be helpful to growth if economies of scale exist. A third reason is that the regional distribution of capital expenditure is likely to be more concentrated because of the greater knowledge of investment outside of the geographical area of the saver and such clustering permits greater external economies (although also leading to some social problems connected with intensive urbanisation).

Although we may be able to show that the existence of financial institutions leads to a more favourable supply, price and allocation of credit, this does not conclusively demonstrate the direction of causa-

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33 For an expansion of these views, see R. Goldsmith: *Op. Cit.* Also see J. Tobin and W. C. Brainard: "Financial Intermediaries and the Effectiveness of Monetary Controls," *Financial Markets and Economic Activity*, John Wiley & Sons, 1967.

tion between credit and growth. However, Adelman and Morris[34] have attempted to show that, for 70 underdeveloped and semi-developed countries, the rate of growth of real national product per head has been more closely associated with the level of financial development than with other economic or non-economic factors and that the association is closer for countries with relatively higher incomes. Goldsmith, however, thinks that the question of whether differences in financial structure and development can account for differences in the speed and pattern of development "certainly cannot be settled before the theory of finance is developed much further in the direction of analysing the process of financial development and its relation to economic growth in operational testable terms and before we possess a substantial number of case studies for different representative countries and periods that use the framework of such a financial theory."[35]

Similarly, it is very difficult for us to say that, on the basis of our findings in this study on Guyana, Trinidad and Jamaica, differences between the size of (a) their total financial sector to G.N.P. (b) their banking sector to G.N.P. (c) their non-banking sector to G.N.P. and (d) their respective non-bank sub-sectors to G.N.P., account for differences in the level of income per head or the rate of growth. One reason is that the existence of certain financial institutions is a necessary but not a sufficient condition for rapid economic growth. Another factor preventing us from making definitive statements concerning the relationship between financial and economic development in Caribbean territories is, as we have pointed out earlier, the poor state of financial and other statistics in the region.

It is intuitively believed that the average unit of non-bank credit is as conducive to increasing the real income multiplier as the average unit of bank credit (which is mainly short-term) because a great deal of non-bank credit is long-term in nature e.g. mortgages and securities credit. The tendency for the interest rate on non-bank credit to be higher than that on bank credit probably reflects a higher rate of return in the real sector and is due more to the importance of differences in demand, than to differences in the supply conditions, of such credit. Moreover, nowadays, the non-bank financial multiplier is often said to be nearly as significant as the bank multiplier: "It is really true of both types of institutions that 'they can only relend what is deposited with them,' as used to be claimed by the banks in denying that they could 'create' credit, and is now claimed by other financial intermediaries in denying that they can 'create' credit, but it becomes clear that both do in fact participate in the multiple expansion of income, savings and credit."[36]

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34 I. Adelman and C. Morris: *Society, Politics and Economic Development*, Baltimore, Johns Hopkins Press, 1967.

35 R. Goldsmith: *Op. Cit.*, p. 409

36 A. N. McLeod: *Op. Cit.*, p. 618. For a useful survey, see also: D. K. Sheppard and C. R. Barrett: "Financial Credit Multipliers and the Availability of Funds," *Economica*, May, 1965

MORTGAGES, GOVERNMENT SECURITIES AND ECONOMIC GROWTH

Non-banks are the major source of mortgage credit. Most of the mortgages are for residential rather than for business purposes. But assuming that residential buildings are a capital, rather than a consumer good, then N.F.I. mortgage credit should account for a significant proportion of private capital formation, and therefore growth. Similarly, N.F.I. hold a large proportion of long term securities and because such funds are used by the government on capital expenditure items, like construction activity, this type of N.F.I. credit should account for a significant proportion of public capital formation. Then, mortgage and securities credit together, should form a very significant portion of the community's capital formation, with important consequences for growth.

Table 5.12 shows the actual and expected ratio of government capital formation to total fixed capital formation for Jamaica. Table 5.13 for Guyana shows, among other things, private building and construction, and government building and construction, as percentages of gross capital formation. A significant proportion of the materials going into the construction industry is imported and this is likely to seriously reduce the actual income multiplier (which includes all indirect effects) below the potential income multiplier. For a number of reasons, some of which were mentioned above, we have not been able to correlate the levels (and increments) of total, government, and private construction activity with non-bank credit and with G.N.P. [37]

TABLE 5.11 Rates of Interest in Guyana, Trinidad and Jamaica

	Year	Bank Rate	Primary Lending Rate	Savings Deposits Rate	Treasury Bill Rate (Average Monthly)
GUYANA	1966	6.50	7.50	4.00	6.11
	1967	6.50	7.50	3.50	6.34
	1968	6.50	7.50	3.50	6.01
	1969	6.50	7.50	3.50	6.12
TRINIDAD	1967	6.50	7.75	3.50	6.45
	1968	6.00	8.25	4.00	5.12
JAMAICA	1966	5.50	7.50	3.50	4.88
	1967	6.00	8.00	4.00	5.35
	1968	5.00	7.00	3.00	3.48

Source: Annual Reports, Central Banks.

37 See also E. S. Shaw's comments on R. Goldsmith's "Financial Structure and Economic Growth in Advanced Countries. An Experiment in Comparative Financial Morphology" in *Capital Formation and Economic Growth*, N.B.E.R., Princeton University Press, 1955.

TABLE 5.12 Ratio of Government Capital Formation to Total Fixed Capital Formation, Jamaica. £m. (J.)

Year	Capital Formation £M	Government Sector £M	Government Sector as a % of Capital Formation
1956	38.8	2.8	7.2
1957	52.1	5.6	10.7
1958	47.4	4.9	10.3
1959	46.1	5.6	12.1
1960	50.7	5.5	10.8
1961	48.3	5.5	11.4
1962	45.2	5.1	11.3
EXPECTED1963	50.6	8.1	16.0
1964	53.1	10.7	20.1
1965	55.8	11.6	20.8
1966	58.6	12.2	20.8
1967	61.5	12.1	19.7

Source: Five Year Independence Plan 1963-68, Jamaica.

CONSUMER CREDIT AND ECONOMIC GROWTH

A not insignificant amount of consumer financing is done by finance houses, insurance companies (policy loans), credit unions and other N.F.I. Finance houses are the main N.F.I. for instalment credit (although, in Guyana, retailers now finance their own hire-purchase following the collapse of the finance house, Olds Discount, in 1961). Instalment credit has probably had a favourable upward effect on the level of consumption and its present-day importance is the result of improved financial technology on the supply side and changed social attitudes on the demand side. "The growth of instalment credit can be attributed to a number of causes, including the growth of specialized consumer financing machinery, the promotion of credit sales by lenders and dealers in consumer durable goods, changing attitudes toward consumer debt, extension of credit facilities to cover a progressively wider range of goods and services, and a persistent tendency, going back many years, toward easier credit terms."[38]

There is some controversy in the literature on the effect of consumer credit on growth. Some contend that purchases of consumer durables should be treated as form of investment included in personal saving, and that on this basis increases in consumer credit have probably increased the rate of capital accumulation, assuming that other forms of saving and business capital accumulation have not been adversely affected. Also, it is thought that the existence of attractive durable goods may have led to greater work effort and attracted women into

[38] W. L. Smith: "Consumer Instalment Credit. A Review Article," *American Economic Review.*, Dec., 1957. p. 967.

TABLE 5.13 Types of Capital Formation, Guyana. $m (E.C.)

	1957	1958	1959	1960	1961	1962	1963	1964	1965	1966	1967
Imported Machinery	23.1	25.7	27.5	45.2	40.4	29.8	22.9	36.1	42.4	52.6	64.5
% gross capital formation	(36.4)	(37.8)	(40.1)	(51.2)	(52.8)	(53.6)	(45.0)	(67.4)	(34.6)	(56.7)	(58.7)
Locally Produced Machinery	0.7	2.8	5.4	4.5	3.6	1.8	0.5	1.1	1.9	1.4	1.5
Private Building and Construction	24.6	9.0	8.3	14.1	10.8	10.4	6.4	7.2	6.9	6.6	9.0
% of gross capital formation	(37.8)	(13.3)	(14.2)	(15.9)	(14.1)	(18.7)	(12.5)	(13.4)	(8.3)	(7.1)	(8.2)
Government Building and Construction	12.2	15.8	13.9	9.9	15.6	12.9	8.1	6.9	23.6	24.1	29.1
% of gross capital formation	(19.2)	(23.3)	(23.8)	(11.2)	(20.4)	(23.2)	(15.9)	(12.9)	(28.4)	(25.9)	(26.5)
Capital Sunk in Mines	2.6	9.6	4.1	5.9	7.0	2.4	2.0	1.5	2.0	1.6	0.8
Fixed Capital Formation	63.2	62.9	59.2	79.6	77.4	57.3	39.9	52.8	76.8	86.3	105.0
Change in Stocks	0.3	5.0	−0.9	2.8	−1.0	−1.7	11.0	0.8	6.4	6.5	4.8
Gross Capital Formation	63.5	67.9	58.4	82.4	76.4	55.6	50.9	53.6	83.2	92.8	109.8

Source: Quarterly Statistical Digests, Guyana.

the labour force, and that in the consumer goods industries productivity is high because these industries lend themselves well to mass production methods. Other economists contend that producer capital goods are "more productive" than consumer durable goods and that if consumer durables are not treated as capital, the increase in consumer credit has reduced the rate of capital accumulation and growth.

We believe that the above controversy has little relevance to Caribbean territories. Because most consumer goods in the Caribbean are imported, increases in consumer credit at the expense of producer credit reduce the potential economic growth rate; however, this does not mean that the community's welfare is lower, given its social time preference.

CONCLUSION

In conclusion, we can say that N.F.I. (private and quasi-government) are a very significant part of the credit system in the Caribbean. N.F.I. credit plays a more significant role in the household and government sector (mainly central government) than in the business sector, the extent to which this is so varying only very slightly between the Caribbean territories. We can also say that the N.F.I. dominate the market for long term credit rather than for short term credit and that life insurance companies are the dominant institution. However, statistical limitations restrict our quantification of N.F.I.'s exact significance (direct and indirect) in the financing of various sectors and subsectors; for example, we do not have adequate information on institutional credit (long, medium and short) to industrial, commercial and agricultural firms, nor on the amount of trade credit, and credit by money lenders.

TABLE 5.AI Registered Real Property Instruments, Trinidad, $ 000 (E.C.)

	REGISTERED REAL PROPERTY INSTRUMENTS											
				OF WHICH								
	Total Number Registered	Transfers		MORTGAGES AT INTEREST							Releases	
				Up to 6%		Over 6% and up to 12%		Over 12%		Without Interest		
	No.	No.	Consideration $000	No.	Consideration $ 000	No.	Consideration $ 000	No.	Consideration $000	No.	Consideration $000	No.	Consideration $000
1963	4367	1495	3157.8	165	707.9	455	1354.5	90	93.0	14	100.3	617	1766.6
1964	4933	1590	4487.7	180	1173.8	482	1611.6	112	167.3	10	19.1	585	1782.1
1965	4894	1298	3546.6	186	1071.4	485	1731.9	75	64.4	7	47.1	610	2297.2
1966	5180	1437	4826.2	231	1465.7	440	2218.2	68	117.9	6	51.7	544	1838.9
1967	5179	1642	5421.0	210	945.0	678	3457.9	172	82.5	4	10.1	722	2553.9
1968													
1968													
1st Quarter	1290	396	1154.9	15	175 0	159	760.6	16	43.6	1	0.5	143	596.1
2nd Quarter	1203	387	1428.9	12	551.5	133	723.3	19	36.5	—	—	142	410.6
3rd Quarter	1220	393	1322.7	8	63.1	151	1032.2	26	27.8	4	6.0	159	297.6
4th Quarter	1202	364	1713.7	4	52.5	138	742.5	30	51.2	2	20.0	159	706.7

Source: Quarterly Economic Report, Central Statistical Office, Trinidad

TABLE 5.AII Relative Importance of Various Financial Institutions in the Mortgage Market in Britain

£ million	1929	1936	1952	1958	1959	1960	1961	1962	1963
Total Mortgage Transactions*	273	365	556	755	1073	1180	1283	1395	—
Building Societies	75	140	266	375	517	560	546	613	849
Local Authorities		7	26	51	55	66	99	84	100
Insurance Companies				100	87	168	200	117	107
Commercial Banks			13	22					
Each Institution as a % of total									
Building Societies	27	38	48	50	48	47	43	44	
Local Authorities		2	5	7	5	6	8	6	
Insurance Companies				13	8	14	16	8	

* Financial Year beginning April.

Source: E.J.Cleary: *The Building Society Movement,* 1965 (P.282)

TABLE 5. AIII Mortgages and Land Transfers, Jamaica £000 (J.)

		New Mortgages		Mortgages Discharged		Land Transfers	
	Year and Parish	No.	£000	No.	£000	No.	£000
1957	Total	3813	5519	2591	2797	4125	11021
	Kingston & St. Andrew	2889	4151	2106	2163	3057	6428
	Other Parishes	924	1368	485	634	1068	4598
1958	Total	4574	7299	2838	3310	5871	12837
	Kingston & St. Andrew	3527	5677	2293	2511	4086	9212
	Other Parishes	1047	1722	545	799	1785	3625
1959	Total	5153	8447	2809	3856	6159	14408
	Kingston & St. Andrew	4065	1437	2254	2913	4453	10370
	Other Parishes	1088	7010	555	943	1706	4038
1960	Total	3270	6611	1964	2718	3860	8764
	Kingston & St. Andrew	2471	4491	1570	2104	2747	6142
	Other Parishes	799	2120	394	614	1113	2622
1961	Total	6462	13343	2781	4838	6946	17797
	Kingston & St. Andrew	5003	9858	2160	3405	5150	13051
	Other Parishes	1459	3485	621	1433	1796	4746
1962	Total	4589	12677	3348	5810	5433	18759
	Kingston & St. Andrew	3436	10379	2404	4284	3797	15357
	Other Parishes	1153	2298	944	1526	1636	3402
1963	Total	4896	9190	3953	9449	3063	7882
	Kingston & St. Andrew	3677	6950	2671	6931	2217	5486
	Other Parishes	1219	2240	1282	2518	846	2396
1964	Total	4425	9182	2710	4773	4587	13691
	Kingston & St. Andrew	3376	7152	2060	3353	3174	9463
	Other Parishes	1049	2030	650	1420	1413	4228
1965	Total	5170	11685	2842	5397	6461	18029
	Kingston & St. Andrew	4124	9551	2247	4415	4555	13859
	Other Parishes	1046	2134	595	982	1906	4170
1966	Total	4707	13757	2728	5462	5494	19968
	Kingston & St. Andrew	3705	11068	2170	4413	3726	15259
	Other Parishes	1002	2689	558	1049	1768	4709
1967	Total	4755	13241	2845	6221	5811	20328
	Kingston & St. Andrew	3596	9807	2219	4983	3655	14590
	Other Parishes	1159	3434	626	1238	2156	5738

Source: (1) Annual Abstract of Statistics; (2) Monetary Statistics, Jamaica

CHAPTER VI

Non-Bank Financial Intermediaries and Financial Policy in the Caribbean

INTRODUCTION

It would not be very satisfactory to discuss financial policy with respect to N.F.I. alone since, for example, any changes in the commercial banking sector should also affect the non-banking sector, given that there is some degree of substitution by individuals between money and near money assets[1]. Similarly, it would be quite unsatisfactory to equate financial policy with monetary policy; fiscal policy and other regulatory devices should also be considered in order to determine the extent to which they reinforce traditional monetary policy or are inconsistent and offset one another. Therefore, reference will also be made to banking policy and fiscal and other measures; that is, total public policy will be considered.

The financial policy of a country should be related to its production policy since there is continuous interaction between the financial super-structure and the real infrastructure. In the Caribbean, there is hardly any financial planning by the governments, even though there are national production plans. Some of the defects in planning in the Caribbean are (a) the national production plans usually consist of a mere set of projects strung together and are not a system of fully integrated sectors (b) planning is only attempted for the public sector and (c) implementation of the plans is not pursued with any great degree of persistence. The underlying factor inhibiting planning in the Caribbean is the structurally dependent nature of the economies. Structural dependence refers to the fact that most of what is produced in the Caribbean is exported and most of what is consumed is imported. There is also structural dependence in the financial system, not only because many of the most important institutions (bank and insurance) are foreign, but also because a significant proportion of the assets held relate mainly to the financing of import/export trade (directly or indirectly) or are foreign securities and foreign shares. Commercial banks, for example, were set up in the Caribbean primarily in order to service the import/export sector. The financial structure thus reinforces the type of production structure and vice versa, and it is difficult for planners to change this system, because the main production and financial sectors are foreign owned.

Nevertheless, if we are going to attempt to do any planning in the production sector we should at the same time plan for the financial

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1 Financial policy, therefore, has to take into account the actual and potential sources of funds (internal and external), the possible variations in the sources and composition of these funds and their probable effects on expenditure and income.

sector. If we are really to alter the production structure, then we should also try to alter the financial structure. And in trying to alter the financial structure (banks and N.F.I.), we need to have much more information than we have at the moment. For example, we need to know the relationships between particular categories of expenditures, and particular types of credit instrument.[2] More generally, we need to know the sources and uses of all funds if we are going to be able to "encourage" saving and expenditure in the correct directions. "The potential usefulness of the flow-of-funds accounts as a theoretical tool is still largely unrealized. In the flow of funds we now have a complete and internally consistent body of data on financial flows, interlocked with national income data. Data on the financial markets are meshed with data on the goods and services markets."[3]

The type of financial planning that a country would undertake—indicative or command type planning—would depend very much on the responsiveness of the real and financial systems, the objectives and aspirations of the people, and other factors constraining and limiting change, such as real and financial structural dependence.

I

FISCAL POLICY AND N.F.I.

In order to affect the operations of N.F.I., three broad strands of fiscal policy can be used: (1) Debt policy. (2) Expenditure Policy and (3) Tax Policy. To bring about some desired effect, these can either be used singly or collectively.

Debt policy refers to a government regulating the supply of securities in order to increase or reduce the volume of spending, or the regulation of the composition of the debt in order to affect the liquidity and therefore timing and power of spending of the community. Debt policy attempts to affect N.F.I. directly, by reducing or increasing their ability to extend credit to their customers. In the Caribbean, debt management is hardly used to contract the volume of private sector credit and spending,[4] partly because Central Banking is in a fairly rudimentary stage of development, partly because inflation is not a problem in the very open economies and partly because the balance of payments is not yet a very acute problem. Governments in the Caribbean tend to issue securities merely to acquire funds to finance their expansionary development plans. We shall not discuss debt

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2 See J. Cohen: "Integrating the Real and Financial Via the Linkage of Financial Flow", *Journal of Finance*, March, 1968.

3 L. S. Ritter: "The Flow-of-Funds Accounts: A New Approach to Financial Market Analysis", *Journal of Finance*, May, 1963, p. 230.

4 For an analysis of the need for structural changes in the money and credit industry in the Caribbean, see C. Y. Thomas: *The Structure, Performance and Prospects of Central Banking in the Caribbean.* (Forthcoming).

policy in the context of fiscal policy, since it can be much more conveniently discussed under traditional monetary policy.

Changes in government expenditure have only an indirect and marginal effect on N.F.I. If the government expenditure were to increase, then part of the additional incomes created might be saved in N.F.I., making it now possible for the latter to increase credit and create primary and secondary rounds of spending and saving. Also, the changing composition of government expenditure might affect N.F.I. only marginally; for example if the Guyana government were to spend more on inter regional transportation, this might encourage rural savers to use the urban situated commercial banks, and might cause a slight decline in savings in the rurally situated Government Savings Banks. These composition of expenditure effects on N.F.I. are, however, for the most part, negligible.

Government tax policy towards N.F.I. has in recent years undergone some change, especially with respect to insurance companies. Some obvious questions are: (a) should we tax financial intermediaries at all; (b) should we tax financial intermediaries at a rate lower than that for the real sector and have as revenue compensation a higher tax rate on real sector firms and individuals; (c) should the tax rate vary between some financial intermediaries and other financial intermediaries and between local institutions and foreign institutions; (d) what are the effects of these taxes on credit and real resource allocation and (e) are these taxes consistent with monetary and other policy measures?

It is sometimes said that financial intermediaries should not be taxed since a main aim of society is to increase savings. However, this is not a valid argument since the real aim of society is to increase the supply of real goods and services and if we tax non-financial corporations we should also tax financial intermediaries. Also, there is no guarantee that interest to savers will rise to encourage more savings or lending rates will fall to encourage more borrowing if a government taxes financial intermediaries less than non-financial firms.

There may be some justification for varying the tax rate between financial intermediaries for at least two reasons: (1) The desire for a more even distribution of income, and general social policy may require the giving of tax preference to mutual and semi-mutual institutions, like insurance companies and (2) The government may desire to stimulate a particular type of credit, for example mortgage credit, and this may require the giving of a tax stimulus to mortgage institutions. Similarly, if the government thinks that foreign intermediaries are not allocating credit as optimally as local intermediaries, then there should be a lower tax on local intermediaries in order to stimulate the growth of the latter at the expense of the foreign intermediaries. Tax measures pertaining to financial intermediaries should be intended not only to raise revenue but be aimed also at helping to allocate credit more efficiently between sectors.

There should also be consistency between the tax measures and other policy devices of the government. For example, it would be inconsis-

tent to tax N.F.I. at a lower rate than commercial banks and yet extend lender-of-last resort facilities only to commercial banks, as happens in the Caribbean. Similarly, it would be inconsistent if a government were to give top priority (in its other policies) to a particular type of activity but taxed the intermediary specializing in this type of credit more than other intermediaries. Thus, there must be consistency in the way public policy distinguishes between bank and non-banks and between some non-banks and other non-banks.

SOME RECENT TAX MEASURES IN THE CARIBBEAN

The two main financial intermediaries are commercial banks and life insurance companies. Until very recently, there was a difference in the Caribbean in the income tax rates on these two institutions. For example, in Guyana before the 1970 budget, commercial banks (and non-life insurance companies) were taxed at the 45% of "profits" rate applicable to non-financial corporations, whereas life insurance companies) were taxed at the 25% of net investment income rate. The rate for life insurance companies in Guyana was, in 1970, increased to 45%. in this same 1970 budget, other taxes and regulations were imposed, similar to those introduced in Trinidad in 1966—an increase in special deposits, a limitation on foreign securities holdings, a limitation on expenses and a tax on premature surrendering of policies.

> Insurance companies have always objected to government imposition of taxes on income: Insurance companies frequently claim they should be exempt from all except real estate taxes. They argue, first, that their property is mainly of an intangible character, consisting of such assets as bonds, notes, and mortgages. They maintain (as do the banks) that the taxation of these assets constitutes double taxation since this property is only representative of other property. Second, these companies hold that they (particularly life insurance companies) perform a valuable service for the state in preventing dependent people from becoming public charges; this service, they say, has as much claim to tax exemption as that performed by benevolent societies, which are exempt. Third, they argue that much of their business is conducted by mutual companies, which are cooperatives and non-profit making institutions. Receipts in excess of expenses go to policy holders in the form of reduced cost of insurance. Fourth, it is claimed that the incidence of insurance taxes is on the policy holders, many of whom are poor farmers, office employees, and clerks who should be relieved of taxes rather than burdened with additional ones.[5]

Insurance companies in Guyana have objected to the increase in the profits tax rate on the grounds that premium rates on existing policies were set at a level consistent with the expected income from investments after the original 25% tax rate had been paid, and that a rise in the rate makes it less possible for them to honour their contract. These insurance companies say that they will therefore have to raise the premium rate on new policies, reduce the dividends paid out on old "with-profits" policies and reduce their reserve holdings, un-

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5 H. M. Groves: *Financing Government*, Holt, Rinehart and Winston 1964. (Sixth Edition) p. 390.

less the government allows them to honour their old contractual arrangements before deducting taxes[6]. However, this seems like a request for privileged treatment since non-financial corporations could equally ask for taxable income to be the residual after a rate of dividend, that shareholders had come to expect, had been paid out. Further evidence that the position of insurance companies is not entirely unique, is the fact that even the government has to pay a fixed interest on its securities, irrespective of the amount of tax revenue it receives or the amount of new loans it can secure.[7]

The solution that insurance companies should adopt is to build into their portfolio structure enough flexibility to cope with this sort of situation, when it arises. The reserves held by insurance companies should be made large enough to meet these contingencies, in the same way that any other business hedges against uncertainty. As partly reflected in the discontinuous movements in Table 6.1, increases in taxation are now a fact of life and should be expected.[8] Insurance companies seem to be objecting more to a change in taxation than to the level of taxation. But a government's commitment to the community requires it to have some flexibility in its fiscal policy. Thus insurance companies should adapt their operational procedures and portfolio structure to suit the revenue needs of the government rather than the government having to adopt a certain fiscal policy to suit the convenience of insurance (and other) companies.

In Trinidad, the special deposit requirement was increased to $ 250, 000 for life business; a choice between this sum and 40 percent of premium for Trinidad liabilities was stipulated for motor vehicle business and where "a company intends to carry on insurance business other than long term or motor vehicle insurance business the deposit shall be either $100, 000 or an amount equivalent to 40 percent of the premium income."[9] In Guyana, however, every life and non-life company was required to pay the new deposit of $250, 000. The ostensible reason for changing the old $50, 000 requirement in Guyana was that "this requirement for the protection of the interests of policy holders was laid down more than a quarter century ago. In the light of present day money values, it does not provide such protection."[10] However, this does not seem to be a very acceptable reason since the economic

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6 If such a request were granted, the government would therefore have to demand some controlling power over the fixing of premium rates.

7 Insurance companies should also not expect privileged tax treatment merely because they hold a large proportion of government's long term securities, since other holders of long term securities could also demand *pro rata* treatment.

8 To be fair to the insurance companies, however, such a large increase in the tax rate (80%) creates many administrative problems and might best have been imposed over a period of say, three years. But change in the tax rate is not entirely unexpected. For example, the rate of tax on life insurance companies in Guyana was changed in 1931 from 3% to 5% and changed twice since 1946.

9 *The Insurance Act*, 1966. Part II Registration: 11. 2(c).

10 *Co-operative Republic Budget* 1970, Guyana, p. 42

environment today is quite stable and different from the one of failures and 'runs' of a quarter century ago. Moreover, other N.F.I. do not have to pay this type of deposit. Also, it is unlikely that insurance companies would be readily allowed to recall and liquidiate any of the $250, 000 "approved securities deposited with the Secretary to the Treasury" if it finds itself faced with, say, a spate of surrenders.[11] What, then, is the real purpose of this deposit? It would appear that it is a mere government device for raising a certain amount (once-and-for-all) of revenue. It is also possible that the Government hopes it will restrict freedom of entry to the insurance industry, especially because of the alarming growth of foreign agencies.

The 1966 Insurance Act in Trinidad also stated that "every company shall have invested in assets in Trinidad and Tobago an amount equal to at least sixty percent of the Trinidad and Tobago dollar liability in each Statutory Fund" whereas in the 1970 Co-operative Republic Budget for Guyana, it is stated that "all life insurance companies both local and foreign will be required to achieve and maintain a level of investment in Guyana equivalent to 95 percent of their Statutory funds and other reserves held against policies sold in Guyana". As mentioned earlier, this is an admirable provision since, even if the foreign securities are higher yielding, the private benefits to the companies are much less than the social benefits (economies external to the companies), of investing locally. The companies may now have to buy more domestic government securities, grant more domestic mortgages (and possibly lower their credit worthiness standards, which may not be a bad thing) and seek out and encourage equity issues.[12] On the other hand, insurance companies may feel that these domestic assets are less diversified, more risky, and less liquid because the more developed money and capital markets abroad made their foreign asset holdings more marketable than their counterpart holdings in the Caribbean, and this may have ramifications throughout their portfolios. The companies may now want to hold less local mortgages and equities and more domestic government securities in order to maintain the previous overall level of liquidity in their portfolio; and since premium rates were based on a certain expected income, the companies may want to hold only equities as their foreign assets in order to compensate for any loss in total income in having to hold more local and less foreign assets. The crux of the matter is that one asset represents a different level of liquidity, security and rate of return

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11 We believe that insurance companies do not take this "deposit" into account in arriving at their optimum portfolio distribution and in fact regard it as a "fixed cost" (even though they earn interest on these $ 250, 000 worth of securities).

12 Theoretically, the holding of less foreign and more local securities by insurance companies should help to reduce the rate of increase of tax rates in the short and long run. In the short run the rise of the internal debt reduces the need to increase taxes, and in the long run the creation of more income internally would automatically cause government tax revenue to rise. (In Guyana, there was also introduced a 10% tax on non-life premiums paid abroad to foreign companies).

TABLE 6.1: Rate of Increase in Taxes Paid by Life and Non-Life Insurance Companies Compared with Rate of Increase in Total Income, for Guyana and Trinidad $000 (E.C.)

		NON-LIFE			
	Year	Total Income of Non-Life Ins. Companies	Percentage Increase in Income	Tax** Paid	Percentage Increase in Tax Paid
GUYANA	1945	576		60	
	1950	891	+54.7	107	+78.3
	1955	1,355	+52.1	182	+70.1
	1956	1,510	+11.4	139	−23.6
	1957	1,628	+7.8	141	+1.4
	1958	1,810	+11.2	74	−47.5
	1959	1,928	+6.5	207	+179.7
	1960	2,127	+10.3	167	−19.3
	1961	2,552	+20.0	209	+25.1
	1962	2,564	+0.5	—	—
	1963	2,100	−18.1	126	—
	1964	2,203	+4.9	254	+101.6
	1965	2,299	+4.4	298	+17.3
	1966	2,564	+11.5	118	−60.4
	1967	2,851	+11.2	366	+210.2
	1968	3,237	+13.5	437	+19.4
TRINIDAD	1957	6,332		726	
	1958	7,095	+12.0	1,135	+56.3
	1959	8,138	+14.7	857	−24.5
	1960	9,686	+19.0	1,099	+28.2
	1961	10,824	+11.7	1,540	+40.1
	1962	11,766	+8.7	1,230	−20.1
	1963	12,631	+7.4	1,272	+3.4
	1964	13,384	+6.0	759	−40.3
	1965	12,870	−3.9	872	+14.9
	1966	11,462	−11.0	673	−22.8

		LIFE			
	Year	Total Income of Life* Ins. Companies	Percentage Increase in Income	Tax** Paid	Percentage Increase in Tax Paid
GUYANA	1945	968		5	
	1950	1, 453	+50. 1	11	+120. 0
	1955	2, 307	+58. 8	30	+172. 7
	1956	2, 450	+6. 2	38	+26. 7
	1957	2, 781	+13. 5	52	+36. 8
	1958	3, 110	+11. 8	126	+142. 3
	1959	3, 303	+6. 2	73	—42. 1
	1960	3, 626	+9. 8	83	+13. 7
	1961	3, 910	+7. 8	151	+81. 9
	1962	4, 051	+3. 6	203	+34. 4
	1963	4, 209	+3. 9	212	+4. 4
	1964	4, 384	+4. 2	245	+15. 6
	1965	4, 927	+12. 4	228	—6. 9
	1966	5, 629	+14. 2	195	—14. 5
	1967	6, 848	+21. 7	234	+20. 0
	1968	7, 979	+16. 5	251	+7. 3
TRINIDAD	1957	12, 884		113	
	1958	14, 907	+15. 7	104	—8. 0
	1959	18, 727	+25. 6	138	+32. 7
	1960	22, 789	+21. 7	282	+104. 3
	1961	24, 894	+9. 2	289	+2. 5
	1962	23, 323	—6. 3	330	+14. 2
	1963	26, 657	+14. 3	539	+63. 3
	1964	26, 520	—0. 5	1, 028	+90. 7
	1965	28, 152	+6. 2	1, 189	+15. 7
	1966	28, 564	+1. 5	1, 214	+2. 1

* Refers to domestic life companies for Guyana.
** Tax for non-life companies in Trinidad includes "other expenses".

Source: Inland Revenue Department and Annual Reports of Insurance Companies, Guyana; Annual Statistical Digest, Trinidad.

from another, and that portfolio management involves arriving at a distribution of assets which achieves the desired trade-off between these asset attributes.

Another provision, introduced in the 1970 Guyana budget, is the limiting of tax deductions; "expenses incurred in securing and maintaining policies on the books of the company will no longer be chargeable as it is now, against investment income for the purposes of taxation. Only expenses incurred in earning of the investment income of life insurance companies will be allowed and these will be fixed for the purpose of income tax at a maximum of 12% of the investment income in any year". This seems to be a reasonable amendment, since the alternative is to allow all expenses, but tax all income (i.e. investment income, premium income and "other" income). If only investment income is taxed, only part of expenses can logically be allowed, since a part of expenses is already included in the premium charged. Moreover, we believe that insurance company expenses are already inflated and are used as a buffer, rising whenever it appears that tax to be paid is going to be high. "This difference between total resources and total necessary payments is called organisational slack. Slack consists in payments to members of the coalition in excess of what is required to maintain the organisation .... Many forms of slack typically exist ... wages in excess of those required to maintain labour are paid, executives are provided with services and personal luxuries in excess of those required to keep them ... For example, it was reported that after losses of about $50 million for the first three quarters of 1946, the Ford Motor Company announced that it had found methods of reducing operating costs (on a given volume of output) by about twenty million dollars per year."[13] We have previously shown that death and "other" claims are a relatively small part of the total expenditure of insurance companies, compared with management expenses, commission fees, etc. It is believed that foreign insurance companies deliberately inflate "head office expenses" in order to reduce their tax liability.

In the 1966 Trinidad Insurance Act and in the 1970 Guyana budget, there was introduced a withholding tax on policies which are surrendered, because of the significant rise in the number of surrendered policies. Now, in most countries, there are three main reasons for life insurance saving: (1) to provide for one's dependents on death (ordinary or whole of life policies) (2) to accumulate long term savings and also hedge against premature death (endowment policies) and (3) to hedge against premature death and at the same time make an investment ("with profit" policies). Of these three reasons, the only one that explains the giving of an income tax allowance to individuals for insurance saving is the first i.e. to relieve the hardship to one's dependents if premature death occurs. The other two reasons contain elements which can conceivably be challenged. For example, why

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13 K. Cohen and R. Cyert: *The Theory of the Firm. Resource Allocation in a Market Economy*, Prentice Hall INC., 1965. pp 333-334. See also O. E. Williamson: *The Economics of Discretionary Behaviour: Managerial Objectives in a Theory of the Firm*, Prentice Hall INC., 1964.

should a policy holder be given an allowance for mere long term saving when a person who continuously builds up (without withdrawals) his savings at another intermediary does not get an allowance; and also why should the bonus from "with profit" policies not be taxed (even though premiums on these policies are higher than on non-participating policies) when profits from any other type of investment business are?

Because of the high rate of surrendering of policies, it would appear that, besides the above three reasons, there is at least one other reason for holding life insurance policies in the Caribbean i.e. as a vehicle for *medium* term savings. There is therefore justification in imposing a withholding tax on the surrender value of the policy, equivalent to the tax allowance granted over the period the policy was held.[14] There is however the problem that some surrendering policy holders may be such small income earners that they were not taxable anyhow during the period that they held policies and so did not benefit from the allowance given. Therefore, a fixed percentage tax is not very equitable and the tax should ideally be based on a calculation of tax "evaded" during the period the policy was held. Table 6.2 shows that the average sum assured of surrendered policies is significantly less than the average sum assured of all policies and lends credence to the view that the people who surrender policies are mainly from the poorer sections of the community. The average amount payable for surrendered policies is about one quarter of the average sum assured and this shows that people are surrendering their policies after the policies have reached approximately one-third of their matured life, on average.[15] This probably indicates that these people were marginal savers, who were "pressured" to hold a policy by the persuasiveness of high-powered salesmen and that the growth rate of life insurance saving may slow down in the near future. On the other hand, the rapid rise in the rate of surrendering of policies in Trinidad may be due to (a) some reluctance on the part of life insurance companies to grant policy loans (in Trinidad, policy loans fell from 32% of total assets in 1954 to 22% in 1966.[16]) (b) some people surrendering small policies in order to take out a more comprehensive family policy and (c) some amount of retrenchment or income fluctuation among casual workers.

The rate of surrender of policies in Guyana is only slightly less than in Trinidad; we would therefore expect the same reasoning (as above)

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14 On the other hand, perhaps in order to encourage long term savings, there should be a smaller withholding tax on a person who has surrendered his policy after say twenty years than one who has surrendered after the minimum period of three years. The Trinidad provision of not taxing the over 60 aged policy holder, who surrenders, only partially allows for this.

15 We have taken into account the fact that on surrendering, deductions are made from the nominal value of the policy at that moment, for expenses incurred in servicing the policy, etc.

16 The tax on the surrendering of policies may "encourage" policy holders to surrender less and demand policy loans more. On the other hand, less people may buy policies because of the partial closing of the surrender exit for policyholders who experience hardship.

TABLE 6.2 Policy Surrenders During Year (Gross Values), Life Insurance Companies, Trinidad. $(E.C.)

Year	No. of Surrendered Policies	Assured Sum of Surrendered Policies	Average Sum Assured	Amount Payable (incl. Cash Bonus)	Average Amount Payable	Average Sum Assured of all Policies
1965	3, 177(14)	10, 600, 915(12)	3, 337	3, 055, 874(15)	962	4, 827
1966	3, 571(11)	11, 195, 857(10)	3, 135	3, 049, 045(13)	854	4, 957
1967	4, 125(12)	17, 955, 628(11)	4, 353	4, 318, 359(13)	1, 047	n.a.

( ) denotes number of companies reporting.

Source: Special request to Statistical Department, Trinidad.

to apply as in the Trinidad situation, although the contents of Table 6.3 on the nature of all discontinued policies, are not conclusive evidence.

The incidence of lapses is another possible indicator of insurance savers over-reaching themselves. Table 6.4 shows that the average sum assured for lapsed policies in Trinidad is approximately twice the average sum assured of all policies, and this could be the main reason for the lapses. The figures for Jamaica do not entirely refute this argument.

The income tax paid by all insurance companies in Guyana was $583, 508 in 1964 and $769, 807 in 1968 and the income tax paid by life insurance companies in Trinidad was $1, 028, 000 in 1964 and $1, 205, 000 in 1966. These sums are fairly small compared to total government tax revenue, and will remain so even if the new Insurance Acts cause tax paid by insurance companies to rise significantly. It therefore seems that the Government should concentrate on using monetary policy and direct controls to alter the asset structure of N.F.I., in order to help bring about optimum resource allocation, rather than be particularly concerned about "extracting the last dollar" from N.F.I. through fiscal policy. Of course, this does not imply that an "efficient portfolio" is incompatible with payment of a higher level of taxes. If the government wishes N.F.I. to purchase more equities and so accept more risk in their portfolio, a percentage rise in the tax rate should not necessarily act as a deterrent. Moreover, "If investors are concerned about the entire dispersion of the distribution around its mean, a proportional tax—even one with incomplete loss offsets—tends to increase the demand for risky assets by all investors except those whose demands would be relatively small in any case. This occurs because the tax reduces the means and dispersions of the distributions of returns in such a way as to make risky assets relatively more attractive than they would be without tax, thus leading some investors to try to compensate for part of the tax-induced loss of income."[17]

II

MONETARY POLICY AND N.F.I.

There is some degree of controversy in the literature as to whether (a) monetary policy should be used to regulate N.F.I. and (b) if used, the extent to which it would be effective.

The usual argument advanced against using monetary policy to regulate N.F.I. is that equal treatment should be accorded to equals and that if banks and non-banks are not performing the same functions, then different treatment should be accorded the two types of institu-

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[17] S. J. Lepper: "Effects of Alternative Tax Structures on Individuals' Holdings of Financial Assets", *Risk Aversion and Portfolio Choice*. *Op. Cit.*, p. 56.

TABLE 6.3 The Nature of Discontinued and New Business for a Single Large Insurance Company in Guyana $(E.C.)

Year	1964	1965	1966	1967	1968
NUMBER OF POLICIES					
New Business	1247	1393	1470	1583	1451
Discontinued Business	1037	965	1013	1281	1285
Discontinued Business as a % of New Business	83.2	69.3	68.9	80.9	88.6
SUM INSURED					
New Business	6,388,861	8,493,650	12,108,220	12,199,750	10,759,525
Discontinued Business	2,763,125	3,153,558	3,948,638	5,182,916	4,128,701
Discontinued Business as a % of New Business	43.2	37.1	32.6	42.5	38.4
ANNUAL PREMIUMS					
New Business	231,252	293,519	399,910	423,110	373,363
Discontinued Business	120,313	119,311	141,219	183,648	184,740
Discontinued Business as a % of New Business	52.0	40.6	35.3	43.4	49.5
AVERAGE SIZE OF POLICIES					
Average Size of New Policies	5123.4	6097.4	8236.9	7706.7	7415.2
Average Size of Policies at Start of the Year	2668.0	2932.3	3271.9	3805.7	4264.6
Average Size of the Discontinued Policies	2664.5	3267.9	3898.0	4046.0	3213.0
Average Size of Death Claims	2367.5	2974.9	3494.2	3586.5	3915.2

Source: Special Request made to Guyana and Trinidad Mutal Life Insurance Company, Guyana.

TABLE 6.4 Life Insurance Policy Lapses in Trinidad and Jamaica* $(E.C.)

Year	1965	1966	1967
TRINIDAD			
No. of Policies Lapsed	2911(12)	2445(10)	4789(10)
Assured Sum of Lapsed Policies	24, 131, 874	24, 417, 385	42, 457, 120
Average Sum Assured	8290	9987	8866
Average Sum Assured of all Policies	4827	4957	n.a.
JAMAICA			
No. of Policies Lapsed	17, 920	10, 014	5, 709
Assured Sum of Lapsed Policies	48, 000, 000	68, 640, 000	77, 760, 000
Average Sum Assured	2679	6854	13621
No. of Total Policies in Force	123, 434	123, 536	112, 714
Insured Value of Total Policies	869, 760, 000	998, 880, 000	1188, 480, 000
Average Size of Total Policies	7046	8086	10544
No. of Lapses as a % of Total Policies	2.4	2.0	4.2

( ) denotes number of companies reporting.

* 18 foreign agencies included for Jamaica.

Source: Special request made to Statistical Department, Trinidad; Monetary Statistics, Jamaica.

tion. Since it was believed that banks were the only institution performing the payments mechanism, special control over banks, rather than non-banks, was thought necessary. (This argument is different from the one that the authorities may think that long-term credit is more important than short-term credit and so give preferential treatment to those intermediaries, mainly non-banks, who grant long term credit).

There are at least three arguments in favour of using monetary policy to regulate N.F.I. The first is that N.F.I. can create credit in the same way that banks can. Most present-day economists now agree, with this argument, although they have differing views as to the degree of the capacity of N.F.I. (because of certain leakages) to create credit. "Commercial banks do have a special ability to expand credit for a reason that is simple but often overlooked. What is truly unique about commercial banks is the speed and automaticity

of the process by which reserves lost by one bank when it makes loans are restored to the banking system."[18]

A second argument in favour of using monetary policy to regulate N.F.I. is that the deposits in N.F.I. are so near to money in certain characteristics that N.F.I. can attract deposits away from banks by offering higher rates of interest and so vitiate the effect of traditional monetary policy.[19] Although banks have a near monopoly in their demand deposit function, building societies, for example, are said to be serious competitors for their time and savings deposits. Other "close substitutes for money" include time deposits in commercial banks, shares and deposits in credit unions and deposits in the government savings bank. Although these are not media of exchange, and there is some waiting time before withdrawal is possible, in their precautionary role they are close substitutes for money. There is however some argument as to whether the policy reserves in life insurance companies should be considered close substitutes for money since, even though policy loans (which presumably increase when bank credit is scarce) and surrender benefits (cash value of policy) are available, the waiting time and inconvenience are so considerable that policy-holders only seek a loan when they need a very large amount and only surrender their policies in cases of dire emergency.

A third argument in favour of using monetary policy to regulate N.F.I. is that what is important is the effect of N.F.I. on the total spending capacity of the community (rather than whether N.F.I.'s deposits are money or not) and that alterations of the composition of N.F.I.'s asset portfolios affect liquidity and therefore the rapidity and volume of total spending. Given the size of their share of total assets in the community, N.F.I.'s actions do have very important quantitative effects on total spending.

Although it is recognized that N.F.I. can affect total spending in the community, there are differing views as to how to deal with them, because of the problem of evasion or "slippage". On the control of the N.F.I., the Radcliffe Committee remarked: "Such a prospect would be unwelcome except as a last resort, not mainly because of its administrative burdens, but because the further growth of new financial institutions would cause the situation continually to slip under the grip of the authorities."[20] Many economists, however, disagree with this Radcliffe Committee view: "This is not a view that I can accept. It may be that one control tends to breed another, but it is better in my judgement, to regulate the growth of new financial institutions than to

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18 W. L. Smith: "Financial Intermediaries and Monetary Controls," *The Quarterly Journal of Economics*, Nov., 1959, p. 536.

19 For an elaboration of W. L. Smith's view on this matter, See A. Ghosh's *Financial Intermediaries and Monetary Policy in a Developing Economy*. The World Press Private Ltd., 1964. pp. 54-55. It is believed that when the Central Bank restricts credit and the interest rate rises, N.F.I are more able to raise their deposit rates to attract funds because of the rise in the rate of return on bonds, etc.

20 Radcliffe Report: *Op. Cit.*, Para. 394.

risk the possibility that things will get out of hand. Certainly, controls involve some degree of arbitrariness, but all policy short of laissez faire is arbitrary. Moreover, provided they have access to all the available information, the authorities will be in a good position to view the situation as a whole and, on that basis, to decide where to exert pressure and to what extent."[21] The U.S. Commission on Money and Credit, which followed the Radcliffe example in thinking that there was no need to have special controls over N.F.I., such as requiring these institutions to hold reserves in the form of deposits in the Federal Reserve Bank, has also been under attack: "In a decidedly curious display of reasoning it holds that since households tend to shift from bank deposits, cash, and investments to shares in savings and loan associations during depression, there is no additional inflationary pressure to combat during expansion. But surely this conclusion rests upon the notion that household liquidity becomes frozen in these shares and will not be used when the authorities want to restrain demand."[22]

Recently, the argument seems to have come full circle. Whereas, since the Radcliffe Report, discussion surrounded the methods that could be used to effectively control non-banks in the same way as banks were controlled, doubts are now being expressed on the desirability of having restrictions even on banks. Johnson is of the view that restrictions should not be imposed on commercial banks simply to facilitate debt management policies especially since statutory liquid assets are by their very nature not available for use in a crisis and emergencies have to be provided for by banks out of additional liquid funds. The main qualification that Johnson makes to total freedom for the commercial banks

> arises from the fact that while banks compete with other institutions as financial intermediaries, bank deposits compete with currency as a means of payment; and that whereas bank depositors pay charges for using the deposit payments mechanism, and receive some interest offset for the capital they have invested in it, users of the currency payments mechanism neither pay the costs of supplying currency nor receive interest on their currency holdings. Removal of the taxes imposed on the banks, while it would remove the distortion of competition between banks and other financial intermediaries, would increase the attraction of using deposits rather than currency for payments and so would increase or reduce distortions of competition at this margin, depending on whether the cost of supplying the deposit payments mechanism is greater or less than the cost of supplying the currency payments mechanism. Unfortunately, there is no evidence on the relative magnitudes of these costs; but it could be reasonably argued that the issue is relatively unimportant by comparison with the financial intermediation issue.[23]

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21 J. S. G. Wilson: "Building the Financial System of a Developing Country," *Lloyds Bank Review*, July, 1969, p. 48.

22 L. Tarshis: "Money and Credit. A Review Article," *American Economic Review*, June, 1962, p. 417.

23 H. Johnson: "The Report on Bank Charges—II," *Bankers Magazine*, August, 1967, p. 66.

MONETARY MEASURES IN THE CARIBBEAN

It is generally agreed that, if unrestricted, N.F.I. can reduce the effectiveness of monetary policy; however, as seen from the above, there is some disagreement as to whether (a) N.F.I. should be controlled and (b) what form control should take. The advocates of control of N.F.I. claim that, the greater the monetary problem, the greater is the restrictive pressure that is brought to bear on banks by the authorities; non-banks therefore increase their growth rate at the expense of banks, thereby aggravating the monetary problem and causing further pressure to be placed on banks, *ad infinitum* (perhaps a similar argument can be made for controlling all non-banks rather than a particular non-bank, given a certain amount of substitutability).

If governments in the Caribbean were to attempt to control N.F.I. via monetary policy, there would be difficulties additional to the ones that would be experienced in a developed country. One difficulty would stem from the fact that the money and capital markets are at a very rudimentary stage of development. The establishment of adequate money and capital markets is one pre-requisite for the voluntary holding of more domestic government securities (in preference to foreign securities) by N.F.I. The government would also have to be seen to be acting as an effective lender of last resort to N.F.I. to encourage the latter to hold more government securities.[24] A second and related difficulty is the fact that securities markets in underdeveloped countries tend to be fairly narrow. "There are basically three attributes of narrow, as opposed to broad, securities markets. One, the absolute number of buyers and sellers is few, and hence the maximum average frequency of transactions is low; two, position-takers are lacking; and three there is not a wide spectrum of owners and ownership motives."[25]

A good example of a narrow securities market is the sub-market for government long term securities. There are very few buyers in this sub-market and by far the most important of the "oligopsonists" are the insurance companies. Because insurance companies were allowed, until very recently, to purchase a significant amount of foreign securities, Caribbean governments had to compete with interest rates offered on foreign securities and this would have tended to make the cost of servicing the long term internal debt higher than it otherwise would have been.

Another problem that a government would face in trying to operate traditional monetary policy is that life insurance companies hold their securities "firmly" and do not take part in frequent buying and selling transactions on the market even when prices and rates of interest

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[24] It could however be argued that debt management is not an efficient way of controlling intermediaries whose deposits are not demand deposits and who also are being encouraged to make more *long* term loans (e.g. mortgages and equities) to the private sector.

[25] R. C. Porter: "Narrow Security Markets and Monetary Policy: Lessons from Pakistan" in *Economic Development and Cultural Change*, Oct., 1965, p. 48.

move favourably. This tendency on the part of insurance companies to hold their securities until maturity[26] has already been explained by the fact that the companies view investment income as a risky factor, because fixed premium rates were partly based on expected investment income, which in turn was based on interest rates at the time of issue of the insurance policies.

The government would also experience problems in trying to use active monetary policy to control building socieites' mortgage lending. A rise in the interest rate (although it makes societies feel "locked-in" and therefore more illiquid) does not encourage them to hold more securities since, in a buoyant mortgage market, societies can push up the mortgage rate and so maintain the previous interest rate differential. Also a fall in the interest rate, while encouraging societies to sell domestic securities to make a capital gain, may not lead to an increase in mortgage lending, since societies can use the realized funds to purchase higher interest foreign securities, instead.

For some of the above reasons, orthodox open market operations would hardly prove an effective means of controlling indirectly some N.F.I. in the Caribbean; difficulties would also be experienced in trying to introduce a comprehensive system of reserve requirements. Caribbean governments (probably slavishly following the pattern in metropolitan countries) have not tried, either, to introduce direct controls over the operations of N.F.I. Therefore, the operations of N.F.I. in the Caribbean are almost unregulated. Since the formation of the Bank of Jamaica, the only non-bank intermediaries that seem to have been given instructions are Finance Houses: "In view of the substantial increase in instalment credit, the commercial banks and finance houses have been requested by the Central Bank to exercise restraint and selectiveness in the extension of credit."[27] In Guyana, instalment credit is not financed by Finance Houses, as the latter no longer exist (since the collapse of Olds Discount in 1961) but the situation is extremely uncontrolled: "Financial institutions specified by the Bank for the purpose of section 44 of the Ordinance are insurance companies, insurance agencies, the New Building Society Ltd., the Guyana Credit Corporation and the Post Office Savings Bank. The Bank has not issued any orders to these institutions to control the volume, terms and conditions of credit."[28]

III

PROBLEMS OF FINANCIAL PLANNING

In a centrally planned economy, financial planning "shows intersector financial flows, particularly the sources of investment funds

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26 See chapter II, above

27 Bank of Jamaica Bulletin, March, 1969, p. 15

28 Bank of Guyana Annual Report, 1968, p. 34. Of course, special problems would be experienced in trying to control the insurance agencies, which are subsidiaries of foreign concerns.

and in some cases the use of credit in the economy. As a rule the overall plan takes the form of a sources-and-uses-of-funds statment, prepared on an annual basis and for the country as a whole."[29] Although there are not many economies that are centrally planned, many countries are realizing the short-comings of their money and capital markets. Some of these countries actually borrow a few of the regulatory techniques of central planning to aid the process of maximization of saving and the bringing about of an optimum allocation of financial resources. "The significant feature of this technique, as a method for mobilizing saving and employing it effectively, is the central direction of saving and investment and the means for bringing the two together with a minimum need of financial markets, assets and debt."[30]

Almost every private financial institution in the Caribbean indulges in some amount of portfolio planning. The institution may try to maximize (or minimize the cost of) its acquisition of saving and allocate credit so that it maximizes its expected yield. The sum of the actions of all institutions, however, does not necessarily lead to the maximizing of the community's saving or the bringing about of the optimum allocation of financial resources for the whole community. There may be a substantial discrepancy between private costs and social costs and private benefits and social benefits. The government may therefore have to intercede to stimulate change in the volume and composition of saving and the volume and composition of credit.

Saving can be both voluntary and compulsory. Saving can also be contractual and non-contractual. Most saving in private institutions is non-contractual. Insurance saving is an example of contractual saving. Insurance saving is also the most important form of non-bank saving and it is therefore worthwhile to be able to forecast its growth. For example, life insurance saving in the Caribbean may slow down if the rate of surrenders and policy loans, and the increase in operating expenses, continue.

FORECASTING INSURANCE SAVING

In order to determine the future growth of insurance saving, we can probably use a simple projection method. However, this method by itself may not give a very accurate estimate. A more sophisticated and useful approach might be to use also regression analysis, which attempts to pin-point the effect that certain independent variables have on determining the growth of insurance saving.

Below are the results of the regression of Trinidad's annual life insurance saving or premium (Q) on national income (B), population (C) national income per head (D) and wages and salaries (E). Data were obtained for the period 1955 to 1966. (As national income

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29 G. Garvey: *Money, Banking and Credit in Eastern Europe*. Federal Reserve Bank of New York Bulletin, 1966, p. 53.

30 J. G. Gurley: *Op. Cit.*, p. 105.

figures for the period 1963 to 1966 were not available, the figures actually used were estimates).

Life Premium		Constant		Independent Variables	$\bar{R}^2$
Q	=	−36.754	+	0.032 B	0.931
		(2.163)		(0.003)	
Q	=	−0.026	+	0.052 C	0.887
		(0.005)		(0.006)	
Q	=	−22.098	+	0.050 D	0.953
		(4.472)		(0.005)	
Q	=	−11.328	+	0.027 D + 0.023 E	0.942
		(1.320)		(0.043) (0.010)	

In trying to arrive at the square of the coefficient of multiple correlation, we used $\bar{R}^2$ instead of R^2 (the unadjusted coefficient of determination) in order to prevent any bias in our estimate of the percentage of change in life premium income that can be explained by our variables. For all four of our equations $\bar{R}^2$ is not extremely high.

This may be due to the fact that the most important variables have not been included in the regression relationship or that our eleven observations (1955-1966) are too small a number not to allow any temporary or short-term random movement to be reflected in the figures. In our first three simple regression equations, the independent variable is seen to be significant (since it is more than twice the standard error).[31] However, in the fourth or multiple regression equation, the national income variable is not significant. This must be due to the fact that the other variable, wages and salaries, is a large part of national income (and national income per head is already included as a variable in the same equation) since $\bar{R}^2$, the explanatory power of the equation, is not really smaller than in the other equations. We therefore cannot readily say what percentage of variations in life premium income is due to changes in national income per head and what percent to changes in wages and salaries. This is an example of the general problem of multicollinearity where, in an economic time series, two or more independent variables are highly correlated.[32]

In three of the equations also, the constant term is large and significant and has the expected negative sign. This is not surprising be-

[31] Annual premium income is a mere proxy for yearly increases in insurance saving. A much truer indication of annual life insurance saving would be increases in the "insurance fund" and, for non-life insurance saving, increases in the "reserve fund". For a full discussion of this theoretical distinction, see J. Kindhal "Saving in Life Insurance and Pension Funds: Some Problems of Interpretation", *Southern Economic Journal*, July 1963.

[32] In our equations, there may also be an element of autocorrelation, wherein a downward bias in the standard errors obtained by the simple method of least squares distorts the tests of significance and makes the results appear significant in cases where they are not.

cause of the contractual nature of life insurance saving. Only in equation two is the constant small, but yet significant, and this is not surprising either, given the relatively large size of the population coefficient and the relatively small size of $\bar{R}^2$.

The equation results for non-life saving in Trinidad are as follows:

Non-Life Premium		Constant		Independent Variables	$\bar{R}^2$
Q	=	−4.846 (1.059)	+	0.021 B (0.001)	0.987
Q	=	−0.020 (0.001)	+	0.035 C (0.001)	0.996
Q	=	−16.040 (3.198)	+	0.032 D (0.004)	0.884
Q	=	−4.283 (1.190)	+	0.007 D + 0.025 E (0.002) (0.002)	0.995

The comments we made in analysing the regression results for life insurance saving could similarly apply for non-life "saving"[33].

PLANNING MORTGAGE FINANCE

There are a few points we ought to make with respect to mortgage finance which might have the policy implication of government assuming some degree of control over the business. The first is that there may be justification for limiting the value of residential mortgages to a certain percentage of total mortgages. At the moment the mortgage market is too "residential oriented" with business mortgages only a few percent of total mortgages.[34]

This limitation would encourage mortgage institutions to grant more mortgages for agricultural and industrial purposes (also less priority should perhaps be given to mortgage loans for commercial purposes) and, where necessary, even to seek out businessmen desirous of business loans. Some might argue that this is a retrograde step in that just when other countries, for instance U.S.A., are thinking of getting rid of their portfolio restrictions, we are imposing controls in the Caribbean and that these controls prevent intermediaries from adjusting to the changing needs of the community and environment. However, there is a major difference between the proposed controls and those existing in, say, the U.S.A. In the U.S.A., controls are mainly for a defensive purpose and pertain to safety requirements of minimum

[33] Our regression could have been expanded if statistics on the value and number of buildings (or mortgages), vehicles, etc. were available.

[34] In Canada, in 1960, no less than 23% of mortgage loans was for business purposes (although it might be claimed that the higher standard of living and industrialization warrants this).

liquidity, minimum bond holdings etc. The controls we suggest, however, have a purely aggressive and developmental goal.

Our second suggestion is that the granting of mortgage loans should reflect, more explicitly, a government policy of spatial and regional planning. At the moment, the random manner in which houses are going up in Guyana suggests that the town and country planners of the central and local government authorities are not paying sufficient attention to at least two factors. The first factor is economic. House building should be encouraged around particular growth centres where residence is in fairly close physical contact with industry and other sources of employment. This is in contradistinction to allowing people to build houses in a "scatter" fashion. The scatter mode of building imposes an additional social cost in that each of these scattered communities soon demands all the recognised social amenities such as electricity, water, access roads etc. This causes a "reverse sequence" —instead of government deciding where a new settlement should be situated and then encouraging settlement there, the reverse occurs, with resultant losses in economies of scale. The second factor is a social one. There has arisen in Guyana in the last decade, as in Trinidad and Jamaica, a new type of development, in the form of exclusive "middle class" suburban areas. Formerly, modest houses and big houses were mixed together and therefore well-to-do and less well-to-do, white collar workers and blue collar workers, lived side by side. Now there are springing up low-cost housing areas and middle-class housing areas with perhaps the social costs of snobbery etc. exceeding any engineering gains of economies of scale from specialized *in situ* building.

A third suggestion is that mortgage financing should be more closely integrated with the building materials industry and that the rate of increase of mortgage finance should not exceed the rate of growth in the building materials industry: "The contribution of house construction to the economy has been of a once-for-all nature and has done comparatively little towards raising the country's productive efficiency. There has been little or no attempt to stimulate the domestic production of building materials, and the result is that housing construction has a very high income leakage abroad. Imports of building materials equalled $6.4 m. in 1956 and were up to $9.7 m. in 1960. When it is born in mind that over nine-tenths of the surface area of the country is covered with forests, and that rock supplies are also abundant it is easy to realise how unfortunate it has been that the housing programme was not complemented by the development of existing output capacity, or the creation of new capacity in domestic building materials industry."[35] Tables 6.5 and 6.6 show that the position in Guyana, today, is probably no different from what it was in 1960. There has been a great increase in the use of cement, although Guyana does not have a cement industry; and not all of the imported cement has come from Caribbean countries.

Table 6.7 shows that in Jamaica the importation of construction matetials is also considerable. The value of the list of selected construction

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35 C. Y. Thomas: *Op. Cit.*, p. 12.

TABLE 6.5 Imports of Certain Building Materials, Guyana

Good	Unit	1965	1966	1967	1968
Cement	000 cwt.	598	1,057	1,603	1,205
Galvanised & Aluminium sheets	000 cwt.	92	79	99	89
Window Glass	000 sq.ft.	641	888	1,049	2,084
Nails	000 cwt.	27	22	11	12
Paint	000 lbs.	2,370	2,688	2,999	3,231

Source: *Economic Survey of Guyana*.1964 & 1968 Reports, Statistical Division Ministry of Economic Development.

materials was £14.3 m.in 1967 and £13.9 m.in 1968;the list includes a few of the goods cited by Brewster and Thomas[36] as "basic materials" (i.e.basic to horizontal and vertical production process in a weighted sense.) Regional import substitution would therefore help to bridge the present gap between the structure of supply of output of building materials and the demand for these materials by the construction industry;at the moment,the construction industry in the Caribbean is almost a "prefab-assembly-screwdriver" type industry. There is nothing wrong *per se* with a large construction industry, since the historical evidence is that this industry tends to be large no matter what the stage of development. Home-ownership,for example,is not a once-for-all event,since standards and tastes are rising (as reflected in a higher chosen rate of obsolescence) almost as fast as,say,in the automobile industry. Caribbean countries should therefore try to derive full benefits from the ongoing construction boom.

Associated with the high demand for home-ownership would be a rapidly rising demand for complementary goods, such as washing machines, refrigerators and other amenities of the home,and these goods should be a necessary part of the regional import substitution programme. The rising demand for home-ownership is also linked to the very rapid rise in imported motor vehicles. The motor car makes it possible for individuals to build homes in isolated areas (and home-ownership in turn stimulates the demand for motor cars,making for a continuous process of interaction) and this "dispersal effect" helps to create serious spatial problems of internal regional planning in most Caribbean countries.[37]

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36 H.Brewster & C.Thomas: *The Dynamics of West Indian Economic Integration*,I.S.E.R, University of the West Indies, 1967.

37 We were told by one insurance company in Guyana that it is reluctant to provide insurance coverage for buildings in remote areas, lacking in fire-fighting services, and this has therefore a dampening down effect on the dispersal tendency. For a theoretical analysis see J. F. Kain, "Postwar Metropolitan Developments, Housing Preferences and Auto Ownership", *American Economic Review*, May, 1967.

TABLE 6.6 Building Materials and Import Content of Gross Capital Formation, Guyana $000 (E.C.)

Imported Goods	1958	1959	1960	1961	1962	1963	1964	1965	1966	1967	1968
Imported Machinery	25,714	27,549	45,202	40,378	29,825	22,897	36,065	45,972	52,614	64,488	n.a.
Imports of Building materials	4,408	4,519	5,808	5,185	3,664	3,472	3,865	5,178	5,989	6,146	6,886
Total Imported Goods (assuming negligible use of fuel and other intermediate goods for construction)	30,122	32,068	51,010	45,563	33,489	26,369	39,930	51,150	58,603	70,634	n.a.
Total Gross Capital Formation	67,865	58,419	82,440	76,417	55,593	50,919	53,576	80,629	92,786	109,750	n.a.
Imported Goods as a % of Capital Formation	44.4	54.9	61.9	59.6	60.2	51.8	74.5	63.4	63.1	64.4	n.a.
Imported Machinery as a % of Capital Formation	37.9	47.2	54.8	52.8	53.6	45.0	67.3	57.0	56.7	58.8	n.a.
Building Materials as a % of Capital Formation	6.5	7.7	7.1	6.8	6.6	6.8	7.2	6.4	6.4	5.6	n.a.

Source: Special Request made to the Statistical Division, Ministry of Economic Development, Guyana.

TABLE 6.7 Imports of Selected Construction Materials, Jamaica

Item	Unit	1964	1965	1966	1967	1968
Railway Sleepers, rails & Accessories	ton	3,077	7,708	3,310	1,133	536
Pitch Pine	000 sq.ft.	23,631	28,331	25,308	26,697	26,660
Building materials—asbestos	cwt.	10,918	57,163	39,041	90,271	1,822
Builders' woodwork, building board	000 lb.	6,829	7,273	6,368	6,257	5,926
Refractory bricks	cwt.	67,950	91,070	79,066	118,973	149,661
Glass—window, plate	000 sq.ft.	2,295	2,078	2,164	2,421	2,196
Iron and Steel bars, girders, angles, etc.	ton	32,676	34,360	39,268	32,890	38,725
Universals, Plates and Sheets	ton	5,953	25,731	24,154	25,542	30,665
Steel Tubes and Fittings	ton	11,134	5,223	6,104	8,721	10,036
Pipe Fittings (cast)	ton	6,179	6,349	10,773	7,826	9,892
Finished structural parts of iron, steel and aluminium	cwt.	25,582	14,866	71,246	201,816	201,984
Insulated cables and electric wires	000 lb.	2,103	2,859	2,741	3,376	4,763
Sinks, washbasins, etc.	cwt.	36,371	39,881	37,836	37,719	46,325
Tiles—wall, floor	cwt.	19,045	21,661	19,943	29,633	43,670
Electric lighting fixtures	cwt.	3,430	2,158	2,148	2,175	3,231

Source: Economic Survey, Jamaica, 1968.

PROBLEMS OF EQUITY FINANCE

It has already been shown that shares held by insurance companies (and other N.F.I.) are a very small percentage of total portfolio assets. A life insurance company manager in Guyana has also been quoted as saying that the reason for this is a lack of supply rather than a lack of demand on the part of life insurance companies.

An explanation of this phenomenon may lie in the structurally dependent nature of Caribbean economies and the principles that govern the investment policies of insurance companies. The major real sectors in the Caribbean economies are foreign-owned and, for long-term finance, depend on either self financing, borrowing from the parent firm or floating issues on metropolitan stock markets. Thus only the small sectors in the Caribbean economies may want to make significant use of a stock exchange. However, the policies of insurance companies are "eclectic in so far as they prefer to invest in large and medium-sized companies. It is not very often that they will be interested in the equity of a small company; and the inducements (including the quality of its management, its prospects and its stability) must be exceptionally attractive before they will do so."[38] Moreover, small firms themselves do not like to acquire finance via the issuing of shares, because of fear of losing control.

All this makes for a very unsatisfactory state of affairs, from the national point of view. Life insurance companies, because their liabilities are long term in nature, should be expected to hold a significant percentage of their total assets in shares in any dynamic and growth-conscious capitalist society. The present situation in the Caribbean is therefore tantamount to a misallocation of the society's scarce financial resources, given the traditional complaint that the underdeveloped Caribbean societies are lacking in sources of long-term capital. Table 6.8 (on life companies in the U.S.A.) gives an indication of the relative size of private business securities that Caribbean life insurance companies could potentially entertain within their asset portfolio. Any intrinsic shortage (or "gap") of capital funds in the Caribbean is therefore more apparent than real (and the fault is also on the demand side) since life insurance companies are capable of supplying much more long-term finance to business, than they presently do. (It is very doubtful whether foreign life insurance companies would have held more equities if these were locally available since they do ot usually attempt to match local liabilities with local assets and it probable that the principle of a "consolidated balance sheet" is flected in an asset portfolio determined by global considerations of parent firm and subsidiary firms combined.)

ile an inelastic supply of new equity issues need not create de- nary pressure, it does have several implications for the com- ion of aggregate demand between consumption and investment diture."[39] Because the asset portfolio of insurance companies

layton and W. Osborn: "Insurance Companies and the Finance of Indus- *Oxford Economic Papers*, Feb., 1958.

loore: *An Introduction to the Theory of Finance. Asset holder our under Uncertainty*, The Free Press (Macmillan Co.) 1968, p. 287.

TABLE 6.8 Growing Significance of Business Securities in Asset Portfolio of Life Insurance Companies, U.S.A. $m (U.S.)

			GOVERNMENT SECURITIES				BUSINESS SECURITIES						
End of period	Year	Total Assets	Total	United States	State and Local	Foreign	Total	Bonds	Stocks	Mortgages	Real Estate	Policy Loans	Other Assets
Statement Value	1941	32,731	9,478	6,796	1,995	687	10,174	9,573	601	6,442	1,878	2,919	1,840
	1945	44,797	22,545	20,583	722	1,240	11,059	10,060	999	6,636	857	1,962	1,738
	1960	119,376	11,679	6,427	3,588	1,664	51,857	46,876	4,981	41,771	3,765	5,231	5,273
	1961	126,816	11,896	6,134	3,888	1,874	55,294	49,036	6,258	44,203	4,007	5,733	5,683
	1962	133,291	12,448	6,170	4,026	2,252	57,576	51,274	6,302	46,902	4,107	6,234	6,024
	1963	141,121	12,438	5,813	3,852	2,773	60,780	53,645	7,135	50,544	4,319	6,655	6,385
	1964	149,470	12,322	5,594	3,774	2,954	63,579	55,641	7,938	55,152	4,528	7,140	6,749
	1965	158,884	11,679	5,119	3,530	3,030	67,599	58,473	9,126	60,013	4,681	7,678	7,234
	1966	167,022	10,837	4,823	3,114	2,900	69,816	61,061	8,755	64,609	4,883	9,117	7,760
Percentage of	1941	32,731	29.0	71.7	21.0	7.3	31.1	94.1	5.9	19.7	5.7	8.9	5.6
Totals and	1945	44,797	50.3	91.3	3.2	5.5	24.7	91.0	9.0	14.8	1.9	4.4	3.9
Sub-Totals	1960	119,376	9.8	55.0	30.7	14.3	43.4	90.4	9.6	35.0	3.1	4.4	4.4
	1961	126,816	9.4	51.6	32.7	15.7	43.6	88.7	11.3	34.9	3.2	4.5	4.5
	1962	133,291	9.3	49.6	32.3	18.1	43.2	89.1	0.9	35.2	3.1	4.7	4.5
	1963	141,121	0.8	46.7	31.0	22.3	43.1	88.3	11.7	35.8	3.1	4.7	4.5
	1964	149,470	0.2	45.4	30.6	24.0	42.5	87.5	12.5	36.9	3.0	4.8	4.5
	1965	158,884	7.4	43.8	30.2	26.0	42.5	86.5	13.5	37.8	2.9	4.8	4.6
	1966	167,022	6.5	44.5	28.7	26.8	41.8	87.5	12.5	38.7	2.9	5.5	4.6

Source: Federal Reserve Bulletin, February, 1969.

in the Caribbean is consumption oriented, this would tend to inhibit growth. If small industries, for fear of losing control, prefer a "gearing ratio" in which debt dominates equity, then the solution is clear: Insurance companies must be prepared to give medium and long term loans (besides mortgage loans) to businessmen, in the form of fixed-interest industrial bonds. Evidence that insurance companies are beginning to think this way is the recent $\$\frac{1}{4}$ m "direct placement" by Colonial Life Insurance Company (Guyana) in a $10 m. dollar Housing Scheme of the government of Guyana; such action needs to be taken also in the private sector by insurance firms.

There are certain benefits (to both the lender and borrower) to be derived from insurance companies (and other N.F.I.) acting as quasi-development bankers, and making private placements instead of participating in public share offerings. Firstly, the lender can benefit immensely if the loan can be tailored to meet his wishes. For example, the rate of return and the amounts that must be given to the borrower at different periods could be negotiated. Secondly, the insurance company has a sure outlet for its funds for years ahead (at rates of interest compatible with its contractual obligations to policy holders). The borrower also benefits a great deal. Firstly, the loan can be tailored to meet his specific, rather than general, needs. Secondly, the borrower knows in advance that he is able to acquire the loan funds at the precise moment he needs them rather than having to wait around for shares to be subscribed, underwriter to be procured, etc. as obtains in public offerings.

However, it is said that private placements also involve certain disadvantages to both lender and borrower. One supposed disadvantage to the lender is that with private placements he has less marketability; but it has been pointed out earlier in this study that life insurance companies, in particular, because their liabilities are long-term, do not need a great deal of liquidity or marketability. A second disadvantage to lenders, such as life insurance companies which have a fixed premium agreement with policy holders, is the refundability in bond investments which allow borrowers to recall outstanding issues and refund at more favourable rates; but recently call-ability has been considerably limited in countries like the U.S.A. One disadvantage that borrowers are said to experience is undue dependence on a single supplier of funds, but the advantages, mentioned earlier, certainly outweigh this particular disadvantage.[40]

Life insurance companies in the Caribbean will need to explore more fully high income earning "direct placements" because of competition from the recent rise of trust companies; and they fear that those who once considered their insurance savings and investment as a hedge against inflation (e.g. with-profit policy holders) will switch their saving medium. Non-life insurance companies are also capable of providing more finance to industry, although the nature of their liabilities de-

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[40] For an elaboration, see G. Clayton and W. Osborn: *Insurance Company Investment. Principles and Policy. Op. Cit.*, p. 201 and J. Cohen and E. Zinbarg: *Op. Cit.*, pp. 698-701.

mands a somewhat more liquid asset portfolio than that of life companies.

FINANCING CARIBBEAN REGIONAL IMPORT SUBSTITUTION

Brewster and Thomas have stated that "the co-ordination of the region's capital market is important from two points of view. Firstly, territorial differences in such factors as the definition of nationality of shareholders, the terms and conditions under which branches of foreign financial institutions may operate, and the issuing and placing of shares, could operate so as to maintain discrimination within the integrated area ....the second reason ...is that it is necessary to maintain a common regional market for capital funds. This ensures both increased mobility of funds and thereby possibly a reduction in the flow of capital funds from the regional market to the metropolitan markets and in particular in the United Kingdom."[41]

The first stage towards implementing a "pooling of savings" policy in the Caribbean should be the closing of the financial sector of these economies to movements outside of the area, thus causing "regional financial diversion"; the regional financial multiplier should rise significantly, enough to make some impact on the financing of regional import substitution. The second stage is when the vastly increased volume of credit lowers the price or terms and conditions of credit, thus causing "regional financial creation." In the third stage, the pooling of savings approach may have such a beneficial effect on growth and prosperity in the Caribbean that there may be "import substitution in foreign aid." In the final distant stage, the Caribbean may even become a real[42] net exporter of capital. Of course, other supporting institutions are necessary for this regional credit policy to succeed: "The question of a common regional credit policy is heavily contingent on the success of the Monetary and Payments Union in regionalizing existing national and expatriate financial institutions."[43]

Table 6.9 for Guyana, indicates that the size of foreign securities holdings by selected institutions was in 1967 half the size of the public external debt. Recently, Caribbean governments have been trying to devise measures to control the foreign securities holdings of certain financial intermediaries e.g. insurance companies.[44]

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41 H. Brewster and C. Thomas: *Op. Cit.*, pp. 30-31.

42 "Real" as distinct from the present position where capital is exported despite the fact that it is badly needed (as reflected in the size of the external debt in the Caribbean.)

43 H. Brewster and C. Thomas: *Op. Cit.* P. 32. There may also be need for a "Committee of Governors of Central Banks"; see E. Kirschen et al: *Financial Integration in Western Europe.* Columbia University Press, 1969, p. 101.

44 In 1967, the value of the foreign securities privately held in Guyana was large enough to make adherence to the IMF foreign assets regulations, by the Central Bank, really unnecessary.

TABLE 6.9 Foreign Securities Holdings of Selected Institutions, Guyana, 1967 $ (E.C.)

Institution	Value of Foreign Securities Held*	Total External Debt (Public)
Insurance Companies	24,516,300	—
Commercial Banks	14,281,000	—
Government Savings Bank	7,518,000	—
Building Societies	594,000	—
Government Pensions	3,600,000	—
Sugar Welfare Fund	5,500,000	—
Sugar Rehabilitation Fund	900,000	—
Sugar Price Stabilisation Fund	900,000	—
Privately Held Foreign Securities	57,809,300	—
Central Bank Holdings	36,913,000	124,967,000

* Does not include Pension Funds for all Private Firms (See Table 6.14)

Source: Special request made to Central Bank, Guyana.

Tables 6.10, 6.11 and 6.12, for Guyana, indicate that almost all the foreign securities are non-Caribbean. There is some justification in attempting to control, not only insurance companies, but also the other main expatriate financial institution—commerical banks. Commercial banks and foreign insurance companies in the Caribbean prefer to hold as much of their funds abroad as possible and their local balances (or local assets) are really dependent on strategic factors in much the same way that levels of investment and production of the multinational corporations (such as bauxite and oil) in the Caribbean are dependent on head office decisions in the metropole.[45]

45. The MNFC and MNC only bring technology to the Caribbean area and they exploit the region's resources in much the same way. The MNFC have an all pervasive effect in the financial sector in much the same way that the MNC dominate the real sector. Besides being able to influence the volume of credit locally, the rates of metropolitan commercial banks affect the rates of other competitive local financial institutions; also the foreign insurance companies can affect the government securities rate. Moreover, a faster growth of foreign banks and foreign insurance companies may cause a slower growth of local institutions, resulting in credit distortions. The intention of the M.N.F.C. is to maximize profits of its global operations rather than profits in any particular territory. Thus, if investment opportunities are not as attractive in the "branch territory" as in the metropole, funds will flow from the branch territory to the metropole, provided that this is in keeping with the diversification of its portfolio and the spreading of risks globally. In the case of multi-national insurance companies there is no real operational necessity for territorial assets to match territorial liabilities. Thus, even if there is a temporary increase in the profitability

TABLE 6.10 Local, Regional and Foreign Securities Holdings of Building Societies, Guyana $ (E.C.)

Year	Total Securities Held at End of Year	Local	Regional (Caribbean)	Foreign
1945	20,040	—	—	20,040
1950	—	—	—	—
1955	154,914	18,472	4,772	131,670
1956	238,292	25,572	4,772	207,948
1957	242,962	25,572	4,772	212,618
1958	289,784	25,572	28,292	235,920
1959	405,326	116,324	28,292	314,870
1960	452,881	116,324	18,337	332,380
1961	452,881	116,324	18,337	332,380
1962	240,804	116,324	—	124,480
1963	240,804	116,324	—	124,480
1964	240,804	116,324	—	124,480
1965	492,503	161,895	—	330,608
1966	678,011	206,731	—	471,280
1967	801,281	263,179	24,500	513,602
1968	825,446	255,113	24,500	575,833

Source: Special Request made to New Building Society, Guyana.

Besides altering their asset portfolios, insurance companies also need to adjust their liabilities structure in order to regionalize their operations. One important aspect of this adjustment process should be their ceasing to reinsure with extra regional companies and insuring instead with Caribbean based companies. This would reduce a significant financial leakage, as shown for a limited number of companies in Table 6.13 and as partially reflected also in Tables 6.AI and 6.AII. Reinsurance within the Caribbean should not increase the riskiness of insurance operations for at least five reasons. Firstly, the Caribbean economies are still structurally tied to metropolitan economies (and subject to metropolitan, rather than regional, variations in economic activity) and so reinsurance in the Caribbean should

of investments in the branch territory, the flow of funds to the metropole may not be reversed, since the maximization of profits in insurance companies, given the long-term contractual nature of the business, is a long-run objective and in the short-run there is greater interest in liquidity for satisfying any unusual increase in claims in any particular territory.

TABLE 6.11 Local, Regional and Foreign Securities Holdings of Government Savings Bank, Guyana $m (E.C.)

Year Dec. 31	Value of Investments Held at End of Year	Local	Regional (Caribbean)	Foreign	No. of
1945	10.000	Nil	—	—	53
1946	11.078	Nil	0.238	10.840	55
1950	13.613	0.120	0.409	13.084	54
1955	16.619	—	—	—	58
1956	15.540	—	—	—	58
1957	14.929	—	—	—	58
1958	18.701	0.948	0.484	17.269	58
1959	20.216	5.005	0.374	14.837	58
1960	19.954	5.005	0.383	14.566	58
1961	20.124	5.455	0.374	14.295	58
1962	17.229	5.455	0.374	11.400	58
1963	16.957	5.455	0.374	11.128	58
1964	16.920	5.455	0.374	11.091	58
1965	15.054	5.455	0.323	9.276	59
1966	14.818	5.455	0.323	99.040	61
1967	14.649	5.455	0.323	8.871	62
1968	13.781	7.007	—	6.774	61

Notes: 1945, 1955, 1956, 1957, Ledger Values.
1950, 1958-68, Face Values.

Source: Special Request Made to Government Savings Bank, Guyana.

not be much more risky than reinsurance outside the region. Secondly, dwarf agricultural species enable them much better to withstand very occasional hurricanes than previously they could. Thirdly, most of the new buildings being erected in the Caribbean are of stone and so the risk of great fire losses (regionally simultaneous or otherwise) is less. Fourthly, malaria, typhoid, yellow fever and other epidemics have now been eradicated from Guyana, as was the case sometime ago in the rest of the Caribbean area. Fifthly, most insurance companies in the Caribbean have now built up a very large insurance fund and reserve fund (which some observers believe to be excessive) and so are in a better position to take the risk of reinsurance within the Caribbean. (There are increasing returns in risk bearing).

IV

OTHER INSTITUTIONAL REFORMS

A lot of the traditional hostility to non-banks comes from those vested interests who believe non-banks to be rivals to banks and at the same time inferior allocators of capital. Arguments have been put forward by these people in favour of bringing non-banks within the scope of Central Bank (or "Central Non-Bank") control by requiring them to maintain minimum cash reserves and empowering the Central Bank to vary the required minimum. It has also been suggested that non-banks should not be allowed without permission to accepts deposits subject to less than seven (7) days notice, thus reducing the degree of perfection of substitution between non-bank deposits and the deposit liabilities of commercial banks. There is certainly need to influence the issue of credit by non-banks; however, as has been pointed out by certain critics, although non-banks have their own credit powers, their ability to defeat the restrictive purposes of monetary policy is not entirely unrelated tothe size of the money supply and that by controlling the money supply the authorities may be able to exert a powerful influence on the activities of non-banks.[46] Moreover, we are not interested in mere control of non-banks, since in this study we are more concerned about making possible a dynamic, rather than a passive, role for non-banks. Non-banks ought to be positively guided in a certain direction; in the earlier parts of the study we hinted at certain reform needs and in the present section we shall suggest other areas of reform.

In examining the need for reform, the first question that springs to mind is whether the existing non-banks are serving our needs optimally. Needs are subjective but assuming that fast growth is the major objective of the society (or at least of the government, which in turn represents the people) then the non-banks should be investment oriented rather than consumption oriented, within the time horizon set. To a certain extent, we have shown that a "gap"in the field of private long-term finance does exist and that, paradoxically, this gap is more a product of inadequate demand by the real sector rather than inadequate supply by the financial sector; however, the problem is institutional and therefore more apparent than real, and an administrative shift to a system of direct or private placements, rather than the traditional type of share issues, could rectify this situation (note that the inadequacy of demand is partly due to structural defects in our dependent economies). We have also shown that there is a "gap" in the field of public financing as reflected in the size of the public external debt owing partly to the large volume of foreign securities bought by non-banks, and that what is now being attempted in Caribbean countries is to limit the holding of foreign securities.[47]

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46 See T. W. Newlyn: "The Supply of Money and its Control," *Economic Journal*, June, 1964, pp. 343-5; See also R. J. Ball: *Inflation and the Theory of Money*, George Allen and Unwin, 1964, pp. 196-200.

47 We should note that even the Canadian Government limits its private financial institutions' holdings of foreign securities.

TABLE 6.1

End of Year (Dec.)	Treasury Bills			Total Assets			
	Total	Local	Reg.	Total Local	Total Regional (Caribbean)	Total Foreign	Total
1945	0.3	0.0	—	—	—	—	6.2
1950	0.3	—	—	—	—	—	9.1
1955	0.4	—	—	—	—	—	14.5
1956	0.4	—	—	—	—	—	16.2
1957	0.5	—	—	—	—	—	17.8
1958	0.5	—	—	—	—	—	19.5
1959	0.5	—	—	—	—	—	21.1
1960	0.6	—	—	15.2	4.3	4.7	23.2
1961	0.6	—	—	16.0	4.3	5.1	25.4
1962	0.7	—	—	17.9	4.9	4.7	27.5
1963	0.8	—	—	17.9	6.3	4.9	29.1
1964	0.9	—	—	18.8	7.2	4.9	30.9
1965	0.9	0.15	0.18	20.1	7.5	5.1	32.7
1966	0.6	0.25	0.049	21.6	8.3	5.3	35.2
1967	0.6	0.14	—	24.0	8.9	5.3	38.2
1968	0.3	0.57	0.093	25.9	9.5	5.0	40.4

* A small p
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Source: Sp

Between pages 186 and 187

more diversified their portfolio the more they are able to take risks. In fact, the government by its actions may be able to "encourage" in surance companies (main holder of government securities) to hold more risky assets: "If the monetary authorities increase the quantity of money and lower the rate of interest towards the level guaranteed by the insurance companies in their contracts, investment managers will not tend to switch from government bonds into cash but will reach out for higher yielding private debt and equities. Their actions will tend to stabilize the market in industrial shares and to lower the costs of private borrowing through debentures or shares so that an increase in industrial investment would be rendered more likely."[49] It is difficult to resolve this problem of comparative efficiency since even the rates of return or profitability are not a sufficient criterion.[50]

Greater efficiency in our non-banking system may also require either greater amalgamation or greater competition. Amalgamation may refer to two types of institutions combining or, two institutions of the same type combining; similarly, competition refers to an inter-type or intra-type situation.

Greater competition could conceivably affect both the volume of deposits and the volume and price of credit. We do not think that the total volume of non-bank saving can be increased significantly if deposit rates are raised since saving is more a function of income than of interest; and although institutional differences in the rate of interest (along with changes in taste) may cause differences in the growth of savings between institutions, total savings of the community may not increase significantly. Moreover, we would like to change the emphasis in the Caribbean from concern with increases in saving to greater interest in the use of savings. If we assume that savings cannot increase significantly in the short run, then the volume of credit cannot increase (except by an increase in velocity) and so we need to concern ourselves more with the allocation of credit. Moreover, the price of credit is not such a constraint on growth in the Caribbean as is the availability of credit to certain sectors, given the misplaced application of metropolitan "credit worthiness" standards. Unfortunately, changes in the pattern of credit can only come about slowly, since at any one moment in time the bulk (stock) of credit is already committed and shifts can only take place in the increments (flow) of credit.

There is probably need for both "intra amalgamation" and "inter amalgamation" in the insurance industry in the Caribbean. Benefits from

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49 G. Clayton & W. Osborn: *Insurance Company Investment. Principles and Policy, Op. Cit.*, p. 225. Also a rise in the rate of interest is not restrictive, but beneficial to the life companies, because life insurance companies hold securities until maturity.

50 Profitability should be distinguished from efficiency, since the latter refers to the optimality of the asset portfolio distribution, from the point of view of returns to the whole economy (which includes the sum of external economies). However, profitability should somewhat reflect efficiency in allocation of resources in a perfectly competitive situation.

intra amalgamation would accrue on both the liabilities and assets side of the portfolio. (The "costs" of amalgamation are likely to be small because at the moment there is very little intra firm competition any way). Intra amalgamation, i.e. the amalgamation of many insurance firms, would make possible certain economies of scale on the liabilities side. At the moment, in the Caribbean, there is a very large number of insurance companies in relation to banks, and in relation to the size of their business (albeit large). If there were amalgamation not only would the number of administration buildings and other infrastructure be reduced, but also administrative expenses[51] and "commissions." Prior to governments' limiting of expenses as deductions from taxable income, a situation existed in the industry where many agents "chased" a single prospective policy holder, without necessarily offering competitive premium rates; and, as shown earlier in this study, non-claims expenditure of insurance companies in the Caribbean is relatively high. Intra amalgamation would also cause a smaller need for reserves, irrespective of whether the amalgamation results in a branch system or a few large firms.[52]

Intra amalgamation would also cause certain benefits to accrue on the asset side as a result of larger scale "production." Larger insurance companies would be able to afford proportionately a less liquid portfolio (because of the statistical factor) and hold more risky assets, like equities and mortgages.

There are however certain problems with respect to intra amalgamation. One is the existence of a large number of foreign companies; these companies cannot be a part of an amalgamation process because they are already branches of metropolitan companies. The solution seems to be to nationalize these foreign companies or to ask them to cease operating in the Caribbean; cessation of activities would not necessarily cause insurance saving to fall since these foreign companies probably merely reduce the saving that would have been done in local companies, anyway. These foreign companies are also the worse offenders with respect to the purchasing of foreign securities.[53] A second problem is that amalgamation may cause a lowering of "output" and a raising of "price" in the insurance industry. This, as we have previously seen, may not necessarily occur, since there is already a state of imperfect competition in the industry. The third

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51 Although employment in this labour intensive service industry may fall as a result of amalgamation, we do not think that greater employment in financial institutions is an effective way of reducing unemployment in the labour surplus economies of the Caribbean.

52 It seems as though domestic life insurance companies in Guyana are now thinking along these economy lines, since three of the larger companies have recently started to advertise collectively.

53 Calculating the net foreign exchange effects of foreign asset holdings is quite an involved matter. We also have to take into account the net of claims and premiums paid to and collected from non-residents and income and dividends accruing from foreign securities, mortgages and equities. See, for example, R. A. Sowelem: *Towards Financial Independence in a Developing Economy*, G. Allen and Unwin, 1967.

problem is that amalgamation may restrict the effectiveness of traditional monetary policy even further since we have already seen that open market operations are less effective against insurance companies (because they hold securities until maturity) than against banks. But a fewer number of insurance firms would make government supervision of the industry easier. However, the ability of insurance companies to influence the price of government securities may increase after amalgamation as the following analogy illustrates:

> Given the desire of the authorities to maintain orderly markets for the national debt and, at the same time, to influence interest rates and liquidity, bank amalgamation may complicate official operations by exposing the markets to significant distortions and by reducing the elasticity of gilt-edged prices to open market operations. Why should this be so? The answer lies in the fact that a reduction in the number of buyers and sellers, other things being equal, will result in a smaller turnover of securities. Hence where previously buyers and sellers among the banks were brought together by the market mechanism, now a proportion of sales and purchases will tend to be matched up within the large establishment just as in the case of gross inflows and outflows of cash. Both the authorities and the banks would now find that their leverage on price movements would be greater; the narrower any market, the more likely it is that buying or selling will move that market against prospective buyers or sellers as the case may be.[54]

Inter amalgamation of the insurance industry would relate to the combining of the activities of Insurance companies, National Insurance Schemes, Private Pension Funds (and in Guyana, the recently mooted National Cooperative Insurance Scheme). There certainly is need for control over these various facets of the insurance industry instead of allowing them to develop along separate paths. To ensure uniformity of purpose, one solution would be for the government to assume control over the whole industry.

There are at least three additional reasons why government should assume total control over insurance companies. The first reason is a moral one. An important reason why life companies have developed so rapidly is the previously low profits tax rate and policyholders' income tax allowance on life premiums paid. Non-life companies have also developed rapidly because motor vehicle insurance is compulsory. There is no intrinsic reason why any type of private company should receive such special benefits. The second reason is that there are important benefits to be derived from economies of scale. Thirdly, with government control efficiency should increase, since the allocation of credit to various sectors would now more closely approximate to the wishes of the government, and we assume to the greater long run welfare of the community.[55]

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54 E. Davies and E. Nevin: "Monetary Policy and the Mergers," *The Bankers' Magazine*, April, 1968, p. 224.

55 If insurance saving were to fall with a government take-over and as a result of switching of media other non-bank saving were to rise by a corresponding amount, then this would indicate the need for government to control the entire financial system instead of piecemeal reforms.

Very little is published about the volume and growth of private pension fund saving (except in the sugar industry) in the Caribbean, and the uses to which these funds are put. In developed countries, pension funds are very big; for example in Canada they are approximately one-third the size of insurance saving. There is therefore need to have some credit control over the allocation of pension fund saving between various sectors and sub-sectors. We suspect that as high a percentage of total pension funds, as of "sugar funds", is used for the purchase of foreign securities. In the case of the bauxite industry, a multinational enterprise, most of the pension funds are held abroad. This is a very unsatisfactory state of affairs. Pension funds can be used to build up the Caribbean equity market and the 'direct placement' scheme we referred to earlier. In rich countries, because of the long term nature of the liability involved, pension funds are mainly invested[56] in equity. Table 6.14 shows the size of pension funds in Guyana.

During last year, Guyana introduced a comprehensive national insurance scheme.[57] Such an introduction may cause a reduction of the growing workmen's compensation and other industrial insurance, "managed fund," and "annuity" business of insurance companies, al-

TABLE 6.14 Private Pension Fund Holdings, Guyana $000 (E.C)

Annual Gross Payment to Fund	1964	1965	1966	1967	1968
Employees' Contribution	1,143	1,185	1,502	1,620	1,691
Employers' Contribution	2,432	2,139	2,153	2,851	3,459
Contribution to Sugar Welfare Fund	1,422	1,280	1,340	1,431	1,440
Contribution to Central Government Pension Fund	452	455	497	550	614

Note The volume of assets in any pension fund scheme depends on the length of time the fund is in operation, the rate of annual payment to the fund, the rate of interest on the assets of the fund and the rate of retirement payment out of the fund. The volume of pension fund assets in Guyana is very significant. In the Demerara Bauxite Company, (a branch firm of a multi-national corporation) alone, it is roughly estimated that pension fund assets in 1968 totalled over $20 m. (E.C), most of which was held abroad in the Royal Trust Company of Canada (and might have been partly used for investment in the operations of the corporation in other countries).

Source: Special request made to the Statistical Department, Guyana.

56 See D. Wrightsman: "Pension Funds and Economic Concentration," *Quarterly Review of Economics and Business*, Winter, 1967; see also: W. G. Nursaw: *Principles of Pension Fund Investment*, Hutchinson & Co., 1966.

57 We have not yet been able to assess whether employers will consider such a scheme as a tax on the employment of labour and whether this will have the effect (in the short term) of adding to the surplus of labour in Guyana.

though private insurance saving may rise if the introduction of a national insurance scheme stimulates "insurance mindedness" generally or if people regard the two things as being complementary. Already, we have been told that some employers are terminating their private pension fund schemes. All this shows the need for rationalization and control over the total insurance industry in the Caribbean.

There is also need to rationalize the "small savings" sector in the Caribbean. In Guyana, a National Co-operative Bank has just been set up and Cooperative Societies, Friendly Societies, Trade Unions and individual holders of savings accounts in foreign commercial banks are being exhorted to transfer their savings to this bank. Nowhere is it stated what is expected to be the effect of this bank on the organized[58] and unorganized markets, e.g. whether these institutions are expected to go along separate but complementary savings and credit paths or whether the aim is to stimulate competition in the performance of substitute roles. Certainly the cooperative financial sector has not been a dynamic sector in the past and the injection of a new cooperative bank into this confusing situation shows the need for a clear strategy of financial planning of small savings under the umbrella of a truly *National* savings bank. In fact, we need to go even further and plan for all savings, big and small, and assume control also over all commercial banks in the area.

If the governments in the Caribbean do not take the bold step of assuming control over the whole savings sector, or as a compromise the small savings sector, there are at least a few *ad hoc* measures that can be taken to stimulate savings in the government savings bank.

One device is to complement the physically fixed branches of the government savings bank with a system of mobile vans, in the belief that because savers in government savings banks are usually poor, they would tend to be immobile. There is no guarantee that this venture would prove to be very successful, as is shown by experience in other countries: "Many people were reluctant to use the vans, but preferred to go to the nearest post-office. However the publicity that was given the campaign did result in a considerable increase in savings bank business at all post offices during this period."[59] (A mobile service would tend to help more of those people who make small regular savings out of fairly 'permanent' incomes, rather than those people who make intermittent savings out of small "unfixed" incomes as do many savers in government savings banks. Intermittency can be judged by the number of dormant accounts and the low average number of deposits in the government savings bank per account holder). In Guyana, The Royal Bank of Canada has recently started such a mobile service and this may have serious consequences for the

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58 It is quite possible that many small savers will merely transfer their savings from one government institution, the Post Office Savings Bank, to another government institution, The National Co-Operative Bank.

59 D. Smith: "The Post Office Savings Banks of the Federation of Malaya and Singapore," *Mobilization of Domestic Capital. Report and Documents OF THE Second Working Party of Experts*, UNECAFE, Bangkok, 1953, p. 102.

Government Savings Bank; moreover, because of computerization of their system, the commercial banks are increasingly able to handle profitably many very small accounts, once the preserve of the Government Savings Bank.

A second device might be to imitate Britain's 1966 Post Office Savings Bank Act whereby investment accounts were introduced "on which depositors with a minimum balance of £50 in their ordinary accounts can earn a higher rate of interest."[60] In 1969 the rate of interest in Britain was 6½ percent and depended on the earnings of deposits when invested by the Post Office. But the investment accounts in Britain are subject to one month's notice of withdrawal, liable to income tax (interest) and subject to a legal maximum holding.

A third device could be similar to the British "Save as you Earn" scheme, whereby all working people could be encouraged to save a regular monthly amount via deduction from pay, by standing orders or in cash; at the end of five years, savings could qualify for a bonus equivalent to one year's savings, free of income tax.

A fourth device might be a decree that wages and salaries of all government employees will be paid through the government savings bank, even though there is no guarantee that a significant part of the wages and salaries, once paid, will remain there.

The experience gained from implementing the third and fourth devices (and the confidence people gain from using a Post Office Account) could be a useful forerunner to the introduction of a giro system.[61] In a giro system, all accounts are held in a single centre and payments between account holders can be made by sending transfer instructions to the centre which then informs both payer and payee simultaneously that a transfer has been made. Payments to people without giro accounts can be made by sending a giro cheque to the giro centre, which authenticates it and sends it to the payee who can cash it at a post office; or a giro cheque may be crossed and sent to the payee who places it in his bank account. A giro is intended to modernize the postal and money orders remittance services of the Post Office and to give businessmen and individuals a more efficient mail order, hire-purchase and instalments payment system. In 1968, Britain entered the international giro system: "October 18 will be the day that the Post Office, through its 23,000 branches, goes into serious competition with the big banks, offering a cheap and fast service for paying all kinds of bills, and giving everybody over 16 the opportunity to hold a current account. It will also be the day that the Post Office sets about wooing the millions of adults in Britain who make no use of the banking system."[62]

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60 Central Office of Information, (BIS): *British Financial Institutions. Op. Cit.*, p. 59.

61 A giro system is a very expensive system to set up and might be only financially worthwhile if the governments of the Caribbean assume control over their whole financial system at a national and regional level. Financial viability of a giro is typically based on its interest on investments (2/3) and its income from charges for services (1/3)

62 The *Guardian* (Britain) newspaper, Friday, Aug., 16, 1968.

The governments of the Caribbean, especially in Guyana and Trinidad, will have to decide whether they want a vibrant government savings bank or whether they consider the bank an anachronism and wish it a slow and natural death. Certainly there is a place for a government savings bank in small income Caribbean economies; certainly the government savings bank cannot hope to maintain its share of thrift deposits by doing nothing. It will have to compete and continually make innovations (as the other savings institutions are doing) merely in order to stand still.[63] Competition to the government savings bank is expected to come from all quarters. For example, non-financial firms in some countries have been encouraging workers to make deposits in the firms they work for. In India, in 1966 savings deposits by workers in industrial and commercial companies were 10 percent (£155 m) of total bank deposits and were rising at the rate of 25 percent per year since 1964 (compared with 12-14 percent for commercial banks).[64]

The government can also affect the volume of deposits and the direction of credit by Guarantee Schemes. Such schemes can be used to stimulate the development of the building societies in Guyana and Trinidad, since we noted that in these two countries building society liabilities (or ratios of assets to G.D.P.) were small compared with Jamaica and other countries. Of course, it is possible that a significant rise in building society saving may cause a small fall in time deposits at banks; and a significant rise in building society mortgage assets may cause a slight fall in mortgage assets of insurance companies.

The deposits and shares of building societies could rise if a comprehensive system of government guarantee and insurance were introduced. Such a system could be along the lines of the system in the USA, where the Federal Savings and Loan Insurance Corporation insures shareholders' accounts in savings and loan associations, the Federal Home Loan Banks provide rediscount facilities and the Federal National Mortgage Association provides a "secondary market"[65] wherein lenders can sell some of their holdings.

The supply of mortgage assets can also increase under a simple government guarantee system. Because of the guarantee, building societies would be prepared to take more risks, lower their credit worthiness standards and have a higher mortgage assets to total assets ratio than would otherwise be the case. In the USA, the Federal Home Administration (FHA) insures urban mortgage loans. The F.H.A. finances itself from premiums, debentures (which are

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63 For example, there ought to be many more government savings bank branches in the towns, and particularly in the shopping areas of the towns, as obtains in Britain and other developed countries, where the institution is holding its own.

64 See D. R. Khatkhate: "Personal Deposits with Industrial Firms—their Growth in Developing countries," *The Bankers' Magazine*, Oct., 1969.

65 In Jamaica we believe the Development Finance Corporation is trying to build up such a market for mortgage securities and this may partly account for the significant growth in building societies in that country over the last few years.

guaranteed by the government) and from any monies subsequently collected from defaulted mortgages it had taken over. The F.H.A. is totally self supporting and in 1960 its reserves to insured loans ratio was 775/31, 322 (million).[66]

A government guarantee scheme can also be used to influence the type and size of mortgage. In 1968, in Britain, "The Government introduced on Option Mortgage Scheme under which it shares the risk with insurance companies when they guarantee loans granted by building societies up to 100 percent of the value of the property or its purchase price. These arrangements are available to borrowers in cases where the valuation or purchase price of the house is not more than £5000".[67] Such a scheme, whereby the government guarantees that portion of advances which exceeds the normal loan to value ratio, would tend to help the poor and would be welcome in the Caribbean where the building societies have become "middle class institutions"—deposits and share accounts, and also mortgage loans, being predominantly held by the middle class.

Generally, the advantages from government guarantee schemes for deposits of financial institutions tend to outweigh the disadvantages. Some advantages on the liabilities side are: (a) it makes it possible for an institution to have a lower reserve ratio and so maximize the use of scarce financial resources; (b) it discourages sudden withdrawals which might otherwise occur (owing to economically or politically induced shifts of confidence); (c) it discourages hoarding for any purpose; and (d) it tends to lower interest rates on deposits, since the risk element is removed and only the waiting element remains (and so interest rates on loans ought also to be lower). Some advantages on the asset side are: (a) total funds for risky assets, e.g. mortgages, ought to be higher; (b) the period of repayment ought to be longer and general amortization policy ought to be more generous and (c) in the case of mortgages, if the government has to approve building standards before insurance is granted, this may cause methods and quality of construction and planning of residential areas to be much improved. We pointed out earlier that we do not think residential planning in the Caribbean is very efficient.[68]

There are at least two possible disadvantages[69] of deposit guarantee or insurance schemes, that we can mention: Firstly, in a unit bank system (the type of structure most necessitating guarantee schemes), larger institutions have to pay premiums to the government to support an insurance system which will benefit primarily the smaller institu-

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66 See R. P. Kent: *Op. Cit.*, pp. 745-768.

67 Central Office of Information (BIS): *British Financial Institutions: Op. Cit.*, p. 64.

68 A government guarantee scheme can also be used to discriminate against foreign institutions (and also against consumer oriented institutions in the absence of the typical selective credit control policy) in the Caribbean, such as insurance companies and commercial banks.

69 For a wider discussion, see J. A. Marlin: "Bank Deposit Insurance II: Its Growth Outside the USA", *The Bankers' Magazine*, Oct., 1969.

tions (even though premiums can be set on the basis of the riskiness of an institution's portfolio) although all benefit from the greater stability of the financial system. Secondly, deposit insurance may make it possible for the inefficient firms to survive (but the regulations contingent on insurance may make the inefficient less inefficient and so increase competition all round).

Although government guarantee and insurance schemes might be used very effectively to increase the supply of mortgages, this does not mean that we fully agree with such a policy. At the moment, mortgages in the Caribbean are already subsidized in a variety of ways, directly and indirectly: (a) Savers in life insurance companies, a predominantly mortgage institution in the Caribbean, get a significant tax relief and this stimulates their saving in this institution (b) life insurance companies themselves, until very recently, were taxed at a lower rate than other companies in the Caribbean (c) a tax deduction is given in most territories for interest repayments on mortgages on new or altered houses and this stimulates mortgage demand (d) business building is stimulated by a substantial capital allowance and (e) the property tax rate in the Caribbean is very low.

It would be interesting to know whether the above types of tax relief represent a positive and deliberate policy or are a mere continuation of past policies. At the moment, the total value of non-residential mortgages seems low in relation to residential mortgages, and so built into the tax system should be some preferential stimulus to business and agricultural mortgages. The tax system should also encourage greater use of local materials in construction activity. On the other hand, if the government favours the holding of government securities and equities, rather than mortgages, then its tax system should reflect these preferences. Obviously, all the strands of public policy need to be as consistent as possible.

Generally, in order for financial policy to be really effective in the Caribbean, much more needs to be known about the workings of the non-bank financial system. At the moment, the data are very inadequate and we are continually operating on the frontier of "zones of ignorance." The relative importance, scope and nature of institutional operations are changing at such a rapid rate that we ought to have a review of the disparate non-bank financial system, at least every five years, in order to determine how efficiently it is serving the needs of the community. If the Central Bank does not want to perform this 'Central Non-Bank' role, then we need to appoint a Commissioner as part of a National Savings Department[70] (attached to the Ministy of Finance or the Ministry of Economic Development).

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70 For the alternative suggestion of a 'National Credit Council', see N. Ambegokar: "Selective Credit Regulation", *The Bankers' Magazine*, Oct., 1969.

V

SIMILARITIES AND DIFFERENCES IN FINANCIAL STRUCTURE

It is very difficult for us to make definitive statements about similarities and differences in the financial structures of Guyana, Trinidad and Jamaica, because of lack of adequate data. With adequate data we would have been able to calculate: (a) the total bank and non-bank financial assets to G.N.P. ratio, (b) the N.F.I. assets/GNP ratio and (c) the assets to G.N.P. ratio for each N.F.I. We would then have been able to say whether ratio (b) offsets or reinforces any differences in ratio (a) and from ratio (c) say which are the N.F.I. mainly accounting for the offsetting and reinforcing effects. As it is, we do not even have accurate G.N.P. figures for all three territories for a long enough series; and for most financial institutions, the data are lacking in either length, depth or breadth.

SOME FACTORS MAKING FOR SIMILARITY

There are certain characteristics of the Caribbean economy which would tend to make for similarity in financial structure. One is the real sector dependence of the economies, and as we said earlier, there is continuous interaction between real sector dependence and dependence in the financial structure. For example, because repatriation of profits is high in the mineral and sugar sectors and because of the general openness and low level of industralization of the economies, the size of the financial multiplier, as reflected in the changing level of bank and non-bank deposits, may tend to be low. A second characteristic is a very high rate of unemployment (between 14 and 21 percent). This may tend to cause small savings and thrift accounts to be low relative to G.N.P. A third factor is that the distribution of income may be fairly skewed, partly because the large expatriate sector and the rest of the economy constitute a sort of dualism (and we believe that the lending practices of the banks and non-banks aggravate the dualism). This skewness may also cause a slow growth of small savings and thrift accounts. A fourth factor is that there is a large rural sector in Caribbean economies.[71] In the rural economy plantation agriculture tends to be a larger sector than peasant agriculture. Partly because there might be a slight tendency by members of the peasant sector to hoard, and partly because the sector may not be completely monetized, there may be an adverse effect on institutional saving; where saving in the peasant sector does take place it is likely to be of a thrift nature, partly because of many small incomes, and partly because the discontinuous pattern of activity and expenditure in agriculture does not necessitate the holding of demand deposits for transactions purposes.

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[71] In Guyana, in addition to a large monetized and semi-monetized agricultural sector, there is a large Amerindian (Red Indian) population, whose activities are almost completely non-monetized.

SOME ACTUAL DIFFERENCES

The Jamaican financial system now seems more developed than the financial system in Guyana and Trinidad, for the following reasons:

(1) The commercial bank assets to G.D.P. ratio is higher in Jamaica than in Guyana and Trinidad.

(2) The Government Savings Bank assets to G.D.P. ratio is higher in Jamaica than in Trinidad, but lower than in Guyana.

(3) The building society assets to G.D.P. ratio is higher in Jamaica than in Guyana and Trinidad.

(4) The credit union assets to G.D.P. ratio is slightly higher in Jamaica than in Trinidad. In Guyana credit union saving is quantitatively almost negligible.

Some of the differences between Trinidad and the other two territories might be more apparent than real, because (1) there is a greater discrepancy between G.D.P. and G.N.P. for Trinidad than for Guyana or Jamaica, (2) the quality or efficiency of financing may be higher in Trinidad, and (3) other financial institutions e.g. quasi-government institutions and also trade credit and self financing may be compensatingly more developed in Trinidad, given the fact that saving media are substitutable.

Nevertheless, there is such a big difference between the sizes of Trinidad's and Jamaica's bank assets as to suggest structural differences in the financial systems. Demand deposits in commercial banks in Jamaica are twice the size of demand deposits in Trinidad and this might be only partly due to greater industrialization (Table 6.15); also the difference in size between savings deposits and time deposits in commercial banks in Jamaica is much greater than for Trinidad, and this might be only partly due to switching caused by differences in the rate of interest.

The continuous fall in Government Savings Bank deposits in Trinidad and the fall between 1961 and 1966 in Guyana may account for commercial bank savings deposits being approximately double both demand and time deposits in Trinidad and treble both demand and time deposits in Guyana. (Savings deposits as a percentage of G.D.P. is lower in Trinidad than in Guyana, but demand deposits as a percentage of G.D.P. is higher in Trinidad than in Guyana, perhaps because of differences in industrialization and rates of interest).

The building society assets to G.D.P. ratio is relatively very low in Trinidad but this does not necessarily mean that at the going market price the community's total demand for mortgages far outstrips the supply, since any apparent "gap" is probably filled by compensatingly greater mortgage loans by other private and quasi-government financial institutions. Moreover, the doubling of building society assets in Trinidad between 1961 and 1967 (probably, partly because of the setting up of a market for mortgage securities) suggests that building societies are going increasingly to play a more important credit role in the future, in the Caribbean. Not only is

TABLE 6.15 Types and Sizes of Commercial Bank Deposits, Guyana, Trinidad and Jamaica $000 (E.C.)

	GUYANA				TRINIDAD				JAMAICA			
Year	Total	Demand	Time	Savings	Total	Demand	Time	Savings	Total	Demand	Time	Savings
1961	38, 709	14, 168	1, 511	23, 030	189, 912	78, 138	17, 112	94, 662	204, 378	91, 473	22, 982	89, 923
1962	47, 164	17, 086	5, 046	25, 032	202, 771	81, 261	24, 569	96, 941	241, 809	109, 243	29, 054	103, 512
1963	61, 102	20, 312	10, 122	30, 668	240, 533	99, 658	33, 916	106, 959	279, 821	108, 754	45, 648	125, 419
1964	69, 919	21, 611	9, 754	38, 554	247, 703	103, 255	29, 665	114, 783	307, 748	115, 248	45, 034	147, 466
1965	79, 058	21, 949	11, 473	45, 636	267, 663	109, 099	37, 516	121, 047	332, 432	114, 595	49, 080	169, 757
1966	83, 209	19, 687	12, 799	50, 543	273, 186	98, 654	45, 887	128, 645	387, 638	127, 258	67, 382	192, 998
1967	93, 591	20, 905	16, 343	56, 343	293, 106	96, 908	55, 221	140, 977	439, 277	144, 557	72, 984	221, 736
1968	104, 848	21, 939	20, 471	62, 438	321, 769	92, 332	76, 113	115, 324	571, 512	183, 523	112, 354	275, 635

Source: F. Alleyne: Commonwealth Caribbean Financial Statistics.

TABLE 6.16 Types of Commercial Bank Deposits as Percentages of G.D.P., Guyana, Trinidad and Jamaica.

	GUYANA			TRINIDAD			JAMAICA		
Year	Demand Deposits as a % of G.D.P.	Time Deposits as a % of G.D.P.	Savings Deposits as a % of G.D.P.	Demand Deposits as a % of G.D.P.	Time Deposits as a % of G.D.P.	Savings Deposits as a % of G.D.P.	Demand Deposits as a % of G.D.P.	Time Deposits as a % of G.D.P.	Savings Deposits as a % of G.D.P.
1961	4.9	0.5	7.9	8.2	1.8	9.9	7.8	2.0	7.7
1962	5.6	1.6	8.2	8.1	2.4	9.6	9.5	2.5	9.0
1963	7.4	3.7	11.2	9.1	3.1	9.8	8.9	3.7	10.2
1964	7.1	3.2	12.7	9.0	2.6	10.0	8.8	3.4	11.2
1965	6.7	3.5	13.8	9.2	3.2	10.2	8.2	3.5	12.1
1966	5.6	3.6	14.4	7.4	3.5	9.7	8.2	4.4	12.5

Source: Computations based on data in Table 15.

TABLE 6.17 Assets of Select Financial Institutions as Percentages of G.D.P., Guyana, Trinidad and Jamaica.

Year		Commercial Bank Assets as a % of G.D.P.	Insurance Assets (approx.) as a % of G.D.P.	Building Society Assets as a % of G.D.P.	Government Savings Bank Assets as a % of G.D.P.	Credit Union Assets* as a % of G.D.P.
GUYANA	1961	13.3	32.5	2.9	7.1	n.a.
	1966	23.7	38.3	2.1	4.2	n.a.
TRINIDAD	1961	19.9	29.7	0.7	1.3	0.4
	1966	20.6	25.4	0.7	0.7	0.6
JAMAICA	1961	17.4	18.5	3.2	2.3	0.6
	1966	25.0	33.6	4.4	2.4	0.8

* Share capital is used as a proxy for assets and the percentages shown for Trinidad and Jamaica are for 1962 (instead of 1961) and 1964 (instead of 1966).

Source: Computations based on data in previous tables.

there a high income elasticity of demand for mortgage loans, but building societies themselves are becoming increasingly disposed towards supplying loans to working-class people with moderate incomes.

We do not have enough data to decide whether the differences in financial structure are so much more significant than the similarities as to indicate that the territories are on essentially different financial paths.[72] However, we can certainly say that the banking system in Jamaica is now more developed than that in Guyana or Trinidad, although this may be a mere passive phenomenon (reflecting the higher growth that Jamaica has experienced in the last decade) rather than a product of deliberate government policy. Lack of data prevents us from stating categorically that the non-bank financial system is more developed in Jamaica than in Guyana or Trinidad, although we expect that Jamaica, by being larger than the other two territories (in terms of G.D.P. only, since Trinidad has a higher G.D.P. per head) is better able to benefit from any economies of scale in financial intermediation.

MONETARY IMPLICATIONS

There are certain monetary implications of the apparent active switch of savers from Government Savings Bank deposits to deposits in commercial banks, in Guyana and Trinidad. The mere act of switching should have caused a primary increase in the nominal money supply with certain secondary effects. The size of the money multiplier would depend on whether the switch is to either savings deposits, time deposits or demand deposits, because banks keep a different reserve ratio for each of the three types of deposit. The overall effect on the system should be expansionary (because the bank multiplier is supposed to be subject to less leakages than the non-bank multiplier) and should be reflected in the balance of payments, although other unknown factors might be offsetting this impact on the balance of payments.

The switch from saving in government savings banks to commercial banks has certain implications for monetary policy. It shows that at any moment in time, by a switch from near-money to money, the financial system can become very liquid with repercussions throughout the economy, and tends to support the argument of those who would like to impose statutory delays on withdrawals from non-banks. However a distinction should be made between various types of non-

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72 A part of the difference in financial structure might be due to differences in standard of living since financial intermediation ratios do not remain constant during the growth process. Another explanatory factor may be the differences in importance of various real sectors in the three territories. The level of general urbanization and industrialization may also be an important factor e.g. in the USA in 1967, the non-life to life insurance assets ratio was 45/177 (billion $ US) whereas in 1965 the ratio in Canada was only 1830/11424 (million $ Canadian).

banks. As Gurley and Shaw pointed out: "it may also be questioned whether the public looks upon policy reserves in life insurance companies as close substitutes for money,"[73] a statement supported by later research: "policy reserves are not regarded as liquid assets by the great majority of policy holders and are not a close substitute for money."[74] But even this finding needs to be modified before it can be applied to the Caribbean countries, since we have seen earlier that there is a high propensity to surrender life insurance policies in the Caribbean and some part of the surrendered funds may be placed in banks directly, or may flow into banks after a round of spending.

VI

CONCLUSION

As countries become fully developed, non-banks collectively tend to supersede banks in importance (using holdings of assets as a percentage of G.D.P. as our measure of importance). But this does not mean that in all underdeveloped countries banks are still much more dominant than non-banks. The more primary producing and less industrialized the underdeveloped country, the more important non-banks tend to be because demand deposits as a form of bank saving are not very significant; this tendency is more pronounced if multinational firms (when using mainly metropolitan sources of finance) dominate the primary sectors, and if in agriculture the savings and investment processes are not very separate.

The financial structure in the Caribbean is not optimum from a social point of view and this is only partly due to the important role that the expatriate financial firms play in the system. We need, inter alia, to "close" the asset portfolio (and so prevent the leakage of funds abroad) of the financial institutions operating in the Caribbean and to "encourage" them (especially life insurance companies) to make available more industrial loans for long term development purposes. Our investigations also seemed to reveal that the individual non-banks are not operating very efficiently, even from a private point of view, and the extent to which this is so varies from one non-bank to another and from one Caribbean territory to another. We believe the governments and central banks must play a more positive part in planning for the transformation of the financial system. This transformation does not have to follow the financial path taken by developed countries but should be related to the long-term production objectives and particular needs and aspirations of the Caribbean people. Also, we should look upon the transforming of our financial superstructure as a prelude (and not necessarily as a pre-requisite) to the transforming of our real infrastructure.

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73 Gurley and Shaw: *Op. Cit.*, p. 4.

74 Life Insurance Association of America: *Life Insurance Companies as Financial Institutions* (Monograph prepared for the US Commission on Money and Credit) Prentice-Hall INC., 1962, p. 242.

Finally, we ought to emphasize that the composition of total saving is almost as important as the volume of total saving; and although both the source of funds and use of funds in the Caribbean is a product of the economic structure (rather than vice versa) over time, the financial sector can, with appropriate financial planning, make a substantial contribution towards changing the composition of output—the key to development in the Caribbean. The financial patterns referred to in the study reflect the special characteristics of the Caribbean economies: small, open, dualistic and underdeveloped, with foreign domination in the two main financial sub-sectors. The similarities in the Caribbean financial patterns tend to be greater than the differences but the differences between the Caribbean and other underdeveloped countries, and between underdeveloped countries as a whole and developed countries, might be expected to be much more significant, given the complex and dynamic nature of financial structure and development. From all that has been said above on the need for disaggregation, it is obvious that further analysis is needed to isolate the macro and micro factors determining (a) the ratio of organized to unorganized financing (b) the ratio of bank to non-bank financial intermediation (c) the relative sizes of demand, time and savings deposits in commercial banks (d) the relative sizes of individual non-banks and the peculiar patterns of their structure and operation in the Caribbean (e) the ratio of "pure" intermediation to "non-pure" intermediation in the non-bank financial sector and (f) the ratio between debt and equity. Given certain growth paths of the real economy, it would still be difficult to predict the relative (and absolute) rates of growth of the banking sector and the various components of the non-bank sector, mainly because of substitutability. For example, countries of basically the same size, economic structure and per capita income, can have essentially different financial paths in a laisser-faire situation, given different interest rate structures and so differences in the marginal rate of financial substitution. The determinants of these financial patterns could have been more readily discerned if better data, on a larger number of Caribbean countries, had been available, permitting rigorous econometric analysis.

TABLE 6. AI Direct B.O.P. Effects (Current Account) of Operations of Life Insurance Companies, Trinidad $ (E.C.)

	Companies Incorporated in Trinidad	Companies Incorporated Overseas	Total	B.O.P. Effects
1965				
Remitted to either branch or Parent Company	294, 000(1)	2, 355, 284(3)	2, 649, 284	
Remitted for other Purposes	1, 352, 400(1)	435, 929(3)	1, 788, 329	
Received from either branch or Parent Company	934, 149(1)	476, 326(4)	1, 410, 475	−2, 994, 036
Received for other Purposes	—	33, 102(2)	33, 102	
1966				
Remitted to either branch or Parent Company	691, 912	395, 249(2)	1, 087, 161	
Remitted for other Purposes	717, 786(2)	779, 800(1)	797, 586	
Received from either branch or Parent Company	706, 442(2)	205, 000(1)	911, 442	−964, 728
Received for other Purposes	8, 577(1)	—	8, 577	
1967				
Remitted to either branch or Parent Company	305, 000(2)	475, 882(2)	780, 882	
Remitted for other Purposes	14, 887(1)	201, 829(2)	216, 716	
Received from either branch or Parent Company	300, 000(1)	1, 488, 186(3)	1, 788, 186	+277, 451
Received for other Purposes	—	506, 863(2)	506, 863	

( ) denotes number of companies reporting.

Source: Special Request made to Statistical Department, Trinidad.

TABLE 6A. II Direct B.O.P. (Current) Effects of Operations of Non-Life Insurance Companies, Trinidad and Jamaica

	($) NON-LIFE (TRINIDAD)				
	FOREIGN 1965			LOCAL 1965	
	Parent Company	Others	Total	Parent Company	Others
Remittances to	1, 798, 380	137, 868	1, 936, 248	349, 161	603, 333
Receipts from	715, 133	36, 630	751, 763	181, 155	8, 577
B.O.P. Deficit	1, 083, 247	101, 238	1, 184, 485	168, 006	594, 756

	(£) NON-LIFE (JAMAICA)			
	FOREIGN AND LOCAL			
	Total	1965	1966	1967
Remittances to	952, 494	306, 240	327, 360	346, 640
Receipts from	189, 732	92, 160	240, 480	264, 960
B.O.P. Deficit	762, 762	214, 080	86, 880	81, 680

Source: (1) Special Request made to Statistical Department, Trinidad
(2) Monetary Statistics, Jamaica.

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