ENDING GLOBAL POVERTY IS SERIOUS BUSINESS.

SEVEN

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To: Chairman Elliot Engel, Ranking Member Connie Mack,
and members of the subcommittee

Re: Building A Culture of Innovation on Hispaniola: A Private Sector Framework and Specific Recommendations on Rebuilding Haiti

Six months after the earthquake in Haiti, international aid agencies have disbursed less than 5% of promised aid. Meanwhile, Dominican President Leonel Fernandez acted faster than any other leader in the world to assist Haiti. He traveled to the worst hit places in Haiti only two days after the disaster, directed all the "*comedores economicos*" into Haiti, and transported many of the wounded to hospitals throughout the Dominican Republic.

Haitian President, René Preval, is viewed as the most thoughtful practitioner of results-oriented politics and bridge building between contentious factions in the nation's recent history. His influence on the culture and politics of Haiti will, by most people's accounts, live far beyond his tenure as president.

The earthquake has reinforced what many have long believed: that the two nations are married to one another, and that the circumstances and leadership now exist to improve that union for the benefit of all the citizens of Hispaniola. Marcela Escobari, the Executive Director of the Center for International Development at Harvard, agrees, "There is no solution that builds long term prosperity in Haiti that does not put the Dominican Republic in a pivotal role."

What is Prosperity and Why does it Matter?

The challenge is to create island-wide prosperity for all citizens. According to Stanford sociologist, Thomas Sowell, "We need to confront the most blatant fact that has persisted across centuries of social history - vast differences in productivity among peoples, and the economic and other consequences of such differences." Nowhere in the world does this matter more than the island of Hispaniola.

We need to move away from a definition of prosperity as simply a flow of per capita income. I list here seven kinds of stock, or capital, that exist in the Dominican Republic, Haiti, and all other countries, the last four of which constitute social capital:

1. **Natural endowments** such as location, subsoil assets, forests, beaches, and climate;

2. **Financial resources** of a nation, such as savings and international reserves;

3. **Man-made capital**, such as buildings, bridges, roads, and telecommunications assets;

4. **Institutional capital**, such as legal protections of tangible and intangible property, efficient government departments, and firms that maximize value to shareholders and compensate and train workers;

5. **Knowledge resources**, such as international patents, and university and think tank capacities;

6. **Human capital**, which represents skills, insights, capabilities;

7. **Culture capital**, which means not only the explicit articulations of culture like music, language, and ritualistic traditions but also attitudes and values that are linked to innovation: trust, belief in competition, and self-determination.

This enables us to consider a broader system and the decisions for investment in an enabling environment. Nobel laureate, Amartya Sen, suggests "the advantage of a stock view would be to give us a better idea of a nation's ability to produce things in the future."

"A Marriage Made in Heaven"

Haiti is weaker than ever before. The highest forms of capital are gone. There are unconfirmed numbers showing that unemployment in Haiti is at least 70%. The country needs immediate, low-skilled jobs more than anything else. On the other hand, the D.R. has shed almost 100,000 textile jobs since 2000 because labor is too expensive compared to China. The CAFTA-D.R. agreement with the United States mandates that all textiles need to have U.S. raw materials to be allowed into the U.S. with low tariffs, which prevents them from being able to compete. As a result, in 2007 the D.R. exported USD 1.4bn in textiles, in 2009 that number shrank to USD 900mm.

Harvard's Escobari says, "It should be a marriage made in heaven. Haiti has lower salaries than China and under the HOPE Act, they can source fabrics from anywhere in the world (at half price of what the D.R. can), and still export it to the U.S. with low tariffs. Haiti needs to create lots and lots of jobs. This is for the situation in which they find themselves, not the situation they wish they had."

This makes a lot of sense, especially in light of the fact that a short time ago, FoxConn, the world's largest electronics manufacturer announced that it was raising wages by over 30% at its largest facilities in Southern China, where it makes the Apple iPad and iPhones. And, according to most analysts, this trend will continue throughout the so-called "special economic zones" in China.

So why hasn't Dominican integration with Haiti happened at a higher rate? One of the most successful Dominican entrepreneurs says, "I needed a bullet proof vehicle to go to my own factories in Haiti, I couldn't send my engineers there and fear for their lives. I closed two factories within a month."

Pierre-Marie Boisson, a Harvard-trained, Haitian bank director says, “It’s logical to have a unique island economy; but under current circumstances, the complete integration or one island economy scenario is unlikely, politically.”

He adds, “What we are facing is free trade, at best; in that case, the two economies' great disparities create a great risk of *trade diversion* as opposed to the desirable *trade creation*.” Trade diversion simply means that a lot of the products that Haiti currently imports from other countries would be imported from the D.R.

Boisson says, “But Haiti itself would only marginally benefit, primarily because of existing impediments to business investment; we can’t liberalize trade without greatly improving Haiti's competitiveness.”

Boisson is correct. The international products that D.R. would supplant generate custom duties to the Haitian government; and, this might hurt Haiti's tradable production by eliminating any remaining degree of protection for vulnerable producers. So we need to move gradually.

Here is how it might work:

The Dominican Republic runs 56 successful free trade zones in the country, most of them private; they are islands of efficiency and provide a world-class industrial environment. We need to deploy know-how to a new “Special Zone” on the frontier between Haiti and the D.R., where the U.S. validates the HOPE act, and the D.R. allows ‘controlled’ legal immigration. The factories currently closing could hire Haitians, who are hard working, and combine this with the institutional strength on Dominican soil.

Escobari suggests, “Haiti/D.R. could create incentives to get Dominican entrepreneurs to create microcosms of efficiency and security in Haiti, and provide them the political and institutional support to help them succeed.” This also applies to both agriculture and construction, but there are few industries that respond as quickly to the right incentives as the textile industry. There are few occasions as good as this one, where the public and private sectors, working towards a common vision, could quickly alter the fate of an extremely fragile country.

Should the wage pressure in China continue, China would no longer be a low-cost producer in many lower value-added industries, such as textiles and apparel. This presents a significant opportunity for the Dominican Republic, Haiti, and other countries in the region. The logic of co-production, where textile plants in the Dominican Republic with DR-CAFTA benefits, combined with sewing operations in Haiti with preferential market access under HOPE and HELP legislation, could achieve world-class efficiencies.

All Haitians benefit if co-production, special zones, and the inevitability of free trade and integration encourages Haiti to put its house in order and adopt an effective investment-led growth agenda. Boisson warns us, “Having a market of 20 million instead of 10 million people can only stimulate investment, job creation and prosperity. But we

need to make sure that it is done for the benefit of the 20 million island inhabitants and not for the 10 million living in the D.R. and a handful of Haiti's richest businessmen."

President Préval seems open to this and has stated that what Haiti needs is not just a reconstruction, but also a "refoundation." This means the international community, the Dominican Republic, and Haiti need to focus on the following priorities:

1. The protection of tangible and intangible property: physical security and the protection of intellectual property.
2. Training Haitians: more incentives to train and give workers choices. They become a competitive advantage to businesses; it improves their power in the market place and puts upward pressure on wages.
3. Market Access: an incentive to attract foreign investment to Haiti would be by providing enhanced market access to major markets such as the United States and Europe.
4. Fiscal Incentives: tax exemptions for investments in designated sectors or geographic areas. There could be exemptions from local Haitian taxes, exemptions for co-production activities in the Dominican Republic, and tax credits to foreign companies in their home countries. Any taxes paid locally could be used to capitalize strategic investment funds, such as with the Caribbean Basin initiative a generation ago.
5. Migration: Solving the complex migration problem should not be a precondition for free trade negotiation; it should be part of a long-term agenda, and should be faciltated by a trusted third party.
6. Production costs: even if everything else were fixed, energy costs would prevent the upgrading of the economy.
7. Hidden taxes on the economy: bureaucratic red tape, i.e., the time to register a business.
8. Specialized and advanced transportation and communication logistics: investors will need to be assured that they will have access to global supply chains and markets. That means efficient ports, roads, and telecommunications.

Finally, we need to create "A Culture of Innovation" on Hispaniola. Culture is how a people attach meaning to life and it becomes both how others see them and how they see themselves. We also need to find role models and foster a belief in competition as a force that spurs human initiative and fosters creativity. We need to comprehend that we will never design or create a system where benefits are distributed to all parties across the island equally and at the same rate. We must, therefore, recognize that as long as everyone's lives are improved, it is all right for some people to become wealthy.

Most importantly, we need to stop the fatalism that places the locus of control for their future on the international community. Haitians and Dominicans share the burden of what Thomas Sowell called, the "vast differences in productivity" on their island, as they (together) will suffer the consequences of those differences. Citizens of Hispaniola need

to follow the historic examples of their leaders, Fernandez and Préval, and look for opportunities to take action and build bridges.