## ABSTRACT

## EXCHANGE RATE LIBERALIZATION IN THE CARIBBEAN : THE CASE OF JAMAICA AND TRINIDAD AND TOBAGO

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For more than twenty years, a free floating exchange rate had been advocated by central banks and economists alike. It was believed that market forces should play a major role in exchange rate determination (Hashmi 1994). Upon close examination, it was realized that exchange rates were not really free to fluctuate in response to supply and demand and other market forces. Typically, a given currency would be maintained by the intervention of its central bank at a value determined by that country to be appropriate to its balance of payments position, conducive to maintaining a satisfactory level of reserves, and in some cases, in fixed relation to some key currency of the world such as the US dollar.

This thesis examined the issue of exchange rate liberalization in Jamaica and Trinidad and Tobago in terms of its objectives, benefits and macroeconomic consequences. Liberalization was expected to eliminate distortions in the allocation of resources, increase competitiveness, and encourage higher levels of productivity in order to achieve sustained economic growth.

In the transitional stages of the liberalization process, however, the new exchange rate regime was expected to have a contractionary impact on the real economy. Because of the differences in structure in the economies of both Jamaica and Trinidad and Tobago, the extent of such contractions varied and the proposed benefits of the move to liberalize yielded different results.

In general, it was found that exchange rate liberalization in these two countries had to be regulated in some way since the exchange rate is the single, most important price in these economies. It is basic to the standard of living since virtually all economic transactions are exchange rate sensitive. The experiences of Jamaica and Trinidad and Tobago prove that liberalization can set off a frenzy of speculative buying and depreciations. Governments had no option but to adopt tools aimed at influencing the exchange rate to avoid such rates from oscillating widely.