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Dominican Republic: Political and Economic Conditions and Relations with the United States

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Summary

President Leonel Fernández of the Dominican Liberation Party (PLD), who served as president previously (1996-2000), took office on August 16, 2004. President Fernández has presided over a period of rapid economic growth (an estimated 10% in 2006), enjoys continued popular support, and has a majority in both legislative chambers. He has restored investor confidence in the Dominican economy and enacted some fiscal reforms, but struggled to resolve the country's ongoing problems with corruption and electricity shortages. Fernández seeks to maintain close ties with the United States and to improve relations with neighboring Haiti. His government has been criticized, however, for its mistreatment of undocumented Haitian migrants and Dominicans of Haitian descent. Fernández will seek re-election in May 2008 but is likely to face tough competition from within his own party and from several opposition candidates. Also, on March 1, 2007, the Dominican Republic-Central America-United States Free Trade Agreement (CAFTA-DR) entered into force in the Dominican Republic after a series of delays. This CRS report will be updated.

Background

The Dominican Republic occupies the eastern two-thirds of the Caribbean island of Hispaniola, which it shares with Haiti. A population of about 9.2 million occupy an area about the size of New Hampshire and Vermont combined. With a per capita income of $2,370, it is considered by the World Bank to be a lower middle-income country. After fighting to achieve its independence from Spain in 1821 and then Haiti in 1844, the Dominican Republic embarked upon a bumpy road toward its current democratic form of government, characterized by long episodes of military dictatorship and frequent coups.

Political Situation

During the 1990s, the Dominican Republic posted rapid economic growth and developed stronger democratic institutions. The "Pact for Democracy" in 1994 paved the way for free and fair elections by removing the aging Joaquin Balaguer, a six-term president and acolyte of the deceased dictator, Rafael Trujillo, from power in 1996. Leonel Fernández of the center-left PLD succeeded Balaguer and presided over a period of strong economic growth. In 2000, after top PLD officials were charged with misusing public funds, Hipólito Mejía (2000-2004), an agrarian engineer of the populist Dominican Revolutionary Party (PRD), defeated the PLD candidate, Danilo Medina. He lost support, however, by spending excessively and deciding to bail out all deposit holders after three massive bank failures in 2003. Mejía seemed to focus more on his re-election bid, which required a constitutional amendment reinstating presidential re-election, than on resolving the country's deep economic crisis.

Fernández Government. President Fernández of the PLD took office on August 16, 2004, after being elected in the first-round with 57% of the vote in May 2004. Fernández has restored investor confidence in the Dominican economy and enacted some fiscal reforms recommended by the International Monetary Fund (IMF), including major tax increases and limits on some forms of government spending. In addition to pursuing economic and political reforms, President Fernández launched an anti-crime initiative in 2005, which has been relatively successful. The program set high performance standards and increased merit-based pay for police officers working in the country's most violent neighborhoods. According to Dominican authorities, the country's murder rate fell slightly, from 25 per 100,000 people in 2005 to17 per 100,000 people in 2006. The anti-crime initiative is currently being expanded into other areas.[1]

During the first two years of his term, President Fernández faced stiff resistance to many of his legislative initiatives, particularly proposed tax increases, from the PRD, which dominated both chambers of the Dominican Congress. His position has improved, however, as a result of the PLD's strong performance in the May 2006 legislative elections. The PLD captured 22 of 32 seats in the Senate and 96 of 178 seats in the Chamber of Deputies in elections that were deemed to be free and fair. Until recently most analysts were predicting that Fernández would be easily re-elected in May 2008. Those predictions have changed somewhat since Danilo Medina, the former minister of the presidency, announced his intention to challenge President Fernández for the PLD nomination in late 2006. The PLD primary is scheduled for May 6, 2007.[2] The main opposition candidate, Miguel Vargas Maldonado of the PRD, who was minister of public works from 2000-2004, hopes to capitalize on the divisions within the PLD.

Corruption. The Dominican Republic ranks among the countries in which corruption is perceived to be "rampant" according to Transparency International's 2006 Corruption Perception index.[3] Although the Fernández government has charged some former government and business officials with corruption, trials have been subject to frequent delays and resulted in few successful prosecutions. For example, although Luis Alvarez Renta, a dual American citizen implicated in the 2003 Banco Intercontinental

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[1] "Dominican Republic-Haiti: Violence Continues," *Latin News Daily*, January 26, 2007; "Miami Firm Helps Cut Crime," *Knight Ridder Tribune News*, March 19, 2006.

[2] "Dominican Republic: Two's a Crowd," *EIU - Business Latin America*, February 12, 2007.

[3] Transparency International, *Corruption Perceptions Index 2006*, November 6, 2006, Available at [http://www.transparency.org/news_room/in_focus/cpi_2006].

scandal, was ordered to pay $173 million by a U.S. federal court in November 2005, trials against Ramon Baez, Alvarez Renta and other top suspects in the scandal did not get underway in the Dominican Republic until October 2006. Fernández has been criticized for failing to improve the prosecution rate for those accused of corruption, to ensure that there is open bidding for public infrastructure projects, or to crackdown on delinquent electricity customers, many of which are large corporations.[4]

Human Rights. According to the State Department's Country Report on Human Rights Practices covering 2006, although the Dominican government has improved its human rights record, some "serious problems remained." Recent reforms of police tactics and increased punishments of officers accused of misconduct led to a 36% decline in killings carried out by security forces. Allegations of the use of torture and physical abuse by police also declined. Although prison conditions continued to range from "poor to extremely harsh"in most prisons, some 20% of the country's 13,000 prisoners have been moved to newer prisons with better living conditions. Finally, despite the enactment of an anti-trafficking in persons law in August 2003, the Dominican government has struggled to arrest and prosecute those accused of human trafficking, particularly in cases involving public officials.

Status of Haitians and Dominican-Haitians. The Dominican government continues to receive international criticism for its treatment of an estimated one million Haitians and Dominican-Haitians living within its borders.[5] Each year thousands of migrants, many without proper documentation, flock from Haiti, the poorest country in the hemisphere, to the Dominican Republic to work in the sugar, construction, and tourism industries. Haitians and their Dominican-born children are regularly denied identity documents necessary to prove their citizenship and job status and to permit their children to attend school, a practice that was condemned by an October 2005 Inter-American Court of Human Rights ruling against the Dominican government. Human rights organizations have also criticized the ongoing forced repatriations of undocumented Haitian migrants.[6] There is ongoing concern about the illegal trafficking of Haitian children into the Dominican Republic to work as domestic servants. In early January 2006, 25 Haitian immigrants died of asphyxiation while being transported by human smugglers from Haiti to the Dominican Republic.

Many observers predict that relations between Haiti and the Dominican Republic will improve now that President Préval, with whom Fernández had a positive working relationship when both men governed in the late 1990s, has taken office. A bilateral commission to work on border security, trade, environmental protection, and other issues has been re-started. The status of Haitians and Dominican-Haitians living in the Dominican Republic may be one of the most difficult bilateral issues to resolve.

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[4] Ken Stier, "Tropical Paradox: The Dominican Republic's Economic Plan is at Odds With Its Politics," *Time*, April 24, 2006.

[5] "Haitian Migrants Denied Basic Rights in Dominican Republic," Amnesty International, March 21, 2007.

[6] "Jesuits Urge Stop to Deporting Haitians from Dominican Republic," *EFE*, July 7, 2006.

Economic Conditions

During the 1990s, fueled by rapid expansion in both the tourism and free-trade zone (FTZ) sectors, the Dominican economy grew at an annual rate of 6-8%. Remittances from Dominicans living abroad contributed an additional $1.5 billion per year to the country's stock of foreign exchange. Economic expansion was also facilitated by the passage of several market-friendly economic reforms in the late 1990s by then President Leonel Fernández. One critical reform was a 1997 law allowing the partial privatization of unprofitable state enterprises. Some observers criticized Fernández's privatization of the electric sector, saying that it failed to remedy power shortages and financial difficulties.[7]

The success of both tourism and export-processing zones is extremely dependent upon the global economy. The country's free trade zones (FTZs) have recently had trouble competing with cheaper goods coming from Central America and China. Since the expiration of global textile quotas on December 31, 2004, the Dominican garment industry has lost some 40,000 jobs as companies have shifted production to countries with lower wages. In February 2007, the closure of two companies in the Santiago free zone left 27,000 people jobless in the country's second-largest city. A 2006 report by the International Confederation of Free Trade Unions asserts that working conditions in the FTZs have deteriorated significantly during that same period. Dominican businesses are hopeful that these trends can be reversed by the recent entry into force of CAFTA-DR.[8]

President Fernández inherited an economy that had been wracked by banking scandals and economic mismanagement during the preceding PRD administration of Hipólito Mejía. The country's public finances were placed under enormous strain after Mejía bailed out the country's third largest bank, Banco Intercontinental (Baninter), which collapsed in May 2003. The Baninter scandal was a direct result of weak banking regulations that enabled bank executives to defraud depositors of U.S. $2.2 billion worth of account holdings — an amount equal to almost 67% of the Dominican Republic's annual budget.[9] Two other commercial banks were bailed out in late 2003, resulting in approximately $700 million in losses to the Dominican Central Bank. The country's precarious economic situation was exacerbated by the Mejía administration's failure to comply with IMF conditions, costing the country millions of dollars in foreign assistance. At the end of 2003, inflation in the Dominican Republic had reached 42%, unemployment stood at 16.5%, and the peso had lost more than half of its value.

Since Fernández took office in August 2004, however, the peso has more than regained its pre-crisis value and inflation has decelerated. In February 2005, President Fernández signed a new $665 million standby agreement with the IMF, and the government's economic and fiscal performance under the agreement appears to be good.

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[7] Bacho Perez, "Widespread Blackouts Leave President Scrambling to Boost Power," *Agence France-Presse*, Feb. 8, 2000.

[8] International Confederation of Free Trade Unions, "EPZs in the Dominican Republic and Haiti: Taking on Grupo M," November 2006; "Dominicans: Business Hopes Trade Pact Will Aid Free Zones," *Inter Press Service*, March 2, 2007.

[9] Jose de Cordoba, "Caribbean Cloud: With a Banker Facing Charges, A Nation Questions Its Success," *Wall Street Journal*, June 23, 2003.

Despite high oil prices, economic growth reached 9.3% in 2005 and roughly 10% in 2006 due to expansion in the construction, communications, and agriculture and fisheries sectors. Economists warn that structural problems in the Dominican economy — including a lack of export competitiveness, institutional weakness, and an ongoing energy crisis — could constrain the country's future economic growth potential.[10]

Energy. Electricity providers, saddled with dollar-denominated debts, are still struggling to provide service to a Dominican populace angry at high power bills and continued blackouts. They have been unable to collect for some 40% of their production due to delinquent electricity customers (many of which are large corporations), inefficiencies, and technical losses. A draft bill in the Dominican Congress would criminalize electricity fraud.[11]

President Fernández has considered a variety of other measures to overcome the electricity crisis and reduce its dependence on foreign oil. Those measures have included a national energy-savings plan and construction of a new privately funded oil refinery. The Fernández government has announced that it will invest $500 million for solving the country's electricity problems and $111 million for building hydroelectric plants. In June 2005, President Fernández signed a PetroCaribe agreement with President Hugo Chávez of Venezuela that provides for up to 50,000 barrels of Venezuelan oil per day to the Dominican Republic at a partially subsidized price. In 2006, the Dominican government deferred some $309 million in payments to Venezuela through PetroCaribe. In February 2007, the Dominican Chamber of Deputies approved a bill that would establish a regulatory framework and tax incentives to promote the production of renewable fuels.[12]

Relations with the United States

The Dominican Republic enjoys a strong relationship with the United States that is evidenced by extensive economic, political, and cultural ties between the two nations. It is one of the most important countries in the Caribbean, because of its large size, diversified economy, and close proximity to the United States. Although the Dominican Republic withdrew its contribution of 300 troops to the coalition in Iraq in May 2004, the Bush Administration has expressed appreciation to the Dominican government for its participation. The United States is currently assisting President Fernández's efforts to improve Dominican competitiveness, attract foreign investment, fight corruption, and reform the country's tax code.

Foreign Aid. The United States is the largest bilateral donor to the Dominican Republic, followed by Japan and Spain. For FY2006, the United States allocated an estimated total of $28 million to the Dominican Republic. The Administration requested an estimated $35 million in total assistance for FY2007 and FY2008. These aid amounts

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[10] "Dominican Republic: Rapid Expansion," *Economist Intelligence Unit*, November 6, 2006.

[11] "IMF Asks for Criminalization of Electricity Fraud in the Dominican Republic," *Global Insight Daily Analysis*, April 2, 2007.

[12] "PetroCaribe Accord Renewed,"*Caribbean Update*, February 1, 2007. "Lower House Approves Renewables Bill in the Dominican Republic," *Global Insight*, February 20, 2007.

include support for a variety of Development Assistance and Child Survival and Health Programs, a Peace Corps staff of some 176 volunteers, and a small military aid program. The FY2008 request includes some $11 million in economic assistance, some of which will support efforts to improve the country's business regulatory framework and to ensure that vulnerable sectors benefit from the DR-CAFTA.

Counter-Narcotics Issues. In September 2006, President Bush again designated the Dominican Republic as one of four major drug transit countries in the Caribbean. According to the U.S. Joint Interagency Task Force South, the number of drug smuggling flights from Venezuela to Haiti and the Dominican Republic increased by 167% from 2005 to 2006. Two thirds of those flights landed in Dominican territory. To counteract those illicit activities, the Dominican government, acting with Haitian and U.S. officials, has stepped up drug-related seizures, arrests, and extraditions. It also signed the Cooperating Nations Information Exchange System enabling the installation of new equipment to track and respond to drug smuggling aircrafts. The Dominican government has struggled to implement its anti-money-laundering law (enacted in 2002), but has taken steps to reduce the influence of drug traffickers on the country's judicial system.[13]

Trade. The United States is the Dominican Republic's main trading partner. The United States exported $5.3 billion in goods to the Dominican Republic in 2006, with electrical machinery (14%) and mineral fuel (10%) among the leading items. In the same year, the United States imported $4.5 billion in Dominican goods. Some 40% of U.S. imports were apparel and clothing, a figure that is some 15% less than in 2005. The Dominican Republic has a U.S. sugar quota of 180,000 tons, the largest of any U.S. trading partner. The Dominican Republic has benefitted from its involvement in the Caribbean Basin Initiative (CBI), a unilateral U.S. trade preference program begun in the mid-1980s, and the expanded trade benefits of the Caribbean Basin Trade Partnership Act (CBTPA) of 2000. In 2006, some 23% of Dominican exports to the United States entered under CBI, and another 32% under CBTPA. Both CBI and CBTPA have been replaced by the U.S.-Dominican Republic-Central America Free Trade Agreement (CAFTA-DR).

On August 5, 2004, the Dominican government, along with the governments of Costa Rica, El Salvador, Honduras, Guatemala, and Nicaragua, signed the CAFTA-DR with the United States. In July 2005, after a contentious debate and a close vote, both houses of the U.S. Congress passed implementing legislation for the CAFTA-DR, which President Bush signed into law on August 2, 2005 (P.L. 109-53, 119 Stat. 462). In September 2005, the Dominican Congress ratified the agreement. The Dominican Republic was scheduled to implement the DR-CAFTA on July 1, 2006, but that date was postponed several times as the Dominican government worked throughout 2006 to bring the country into compliance with the agreement. The Dominican Republic became fully compliant with the DR-CAFTA (and thereby able to implement the agreement) on March 1, 2007.

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[13] U.S. Department of State, *International Narcotics Control Strategy Report 2007*, March 2007.